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FIFTH CIRCUIT UPDATE

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The goal is to capture those cases that are of interest to the business torts litigator that are not discussed in the Bankruptcy, Procedure, and Taxation Updates. As the author, I address, when pertinent, case law in the antitrust, "contorts," and Civil Racketeer Influenced and Corrupt Organizations Act ("R.I.C.O.") arenas as well as any other miscellaneous matters in the business torts realm. Occasionally, this Update transgresses traditional "business torts" in the federal courts arena, and reports on other jurisprudence, including state jurisprudence, when necessity or interest dictates.

I. Miscellaneous Business Torts Jurisprudence

A. Attorney's Fees

- ***Commissioner of Internal Revenue v. Banks***[2]

In an opinion authored by Justice Kennedy, the United States Supreme Court considered two cases involving the same issue: whether the portion of a judgment or settlement paid to a plaintiff's attorney pursuant to a contingency fee agreement is income to the plaintiff under the Internal Revenue Code.[3] The respondent in the first case filed an employment discrimination suit against his former employer and retained an attorney on a contingency fee basis.[4] After trial commenced, the parties settled for $464,000 and the respondent paid $150,000 to his attorney as a contingency fee.[5] The respondent did not include any of the settlement proceeds in his gross income on his federal tax return.[6] The Commissioner of Internal Revenue issued a deficiency notice for

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2. 125 S.Ct. 826, 2005 WL 123825 (Jan. 24, 2005).

3. *Banks*, 2005 WL 123825 at *2 (citing 26 U.S.C. § 1, et seq.).

4. *Id.* at *3.

5. *Id.*

6. *Id.*

the relevant tax year and the tax court upheld the Commissioner's determination by finding that all the settlement proceeds, including the attorney's fees, must be included in gross income.[7]

The respondent appealed, and the Court of Appeals for the Sixth Circuit reversed in part.[8] The Court agreed with the tax court that the net amount received was part of gross income, but held that the amount paid to the attorney was not.[9] The Sixth Circuit reasoned the contingency fee agreement was not an anticipatory assignment because the award was not already earned, vested, or relatively certain in amount at the time of the contract.[10] The Court explained a contingency fee agreement is akin to a partial assignment of income—the attorney is not the mere beneficiary of the award, but earns his fee through his skill.[11] The Circuit Court opined this reasoning applies regardless of whether state law grants the attorney a property interest in part of the award.[12]

The second case also involved an employment dispute. After a jury trial, appeals and post-trial motions, the parties settled, the defendants paid $4,364,547 to the respondent, and pursuant to the formula set out in the contingency fee agreement, an additional $3,864,012 directly to the respondent's attorney.[13] This respondent did not include the amount paid directly to his attorney in his gross income on his federal return, and the Commissioner issued a deficiency notice.[14] Again the tax court upheld the Commissioner's determination.[15] However, in this case, the Ninth Circuit Court of Appeals reversed.[16] Conflicting with the Sixth Circuit decision, the Ninth Circuit viewed state law as determinative.[17] The Court opined that where state law confers an attorney no special property rights in his fee, the whole amount of the award is included in the plaintiff's gross income.[18] Oregon state law grants attorneys a superior lien in the contingency fee portion of the award.[19] According to the Ninth Circuit, as a result, contingency fee agreements operate not as anticipatory contracts, but as a partial transfer to the attorney of some of the client's property in the suit.[20]

The United States Supreme Court reviewed the Internal Revenue Code and previous IRS related case law.[21] The High Court identified the "anticipatory assignment of income doctrine," which holds that a taxpayer cannot exclude an economic gain from his gross income by assigning the gain to another party in advance.[22] The Court explained the rationale behind this doctrine is the concept that "gains should be taxed 'to those who earn them.' "[23] The Court noted that the doctrine does not allow courts to inquire whether a particular assignment actually has a discernable tax avoidance purpose.[24]

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7. *Id.*
8. *Id.* (citing 345 F.3d 373 (2003)).
9. *Id.*
10. *Id.*
11. *Id.*
12. *Banks,* 2005 WL 123825 at *3.
13. *Id.*
14. *Id.*
15. *Id.*
16. *Id.* (citing 340 F.3d 1074 (2003)).
17. *Id.*
18. *Id.*
19. *Id.*
20. *Id.*
21. *Banks,* 2005 WL 123825 at *5.
22. *Id.* (citing *Lucas v. Earl*, 281 U.S. 111, 50 S.Ct. 241, 74 L.Ed.731 (1930); *Commissioner v. Sunnen*, 333 U.S. 591, 604, 68 S.Ct. 715, 92 L.Ed.898 (1948)).
23. *Id.* (quoting *Lucas*, 281 U.S. at 114).
24. *Id.*

The respondents argued that "the anticipatory assignment doctrine is a judge-made antifraud rule" with no relevance to the contingency fee contracts at issue in the instant case.[25] The U.S. Supreme Court acknowledged that in an ordinary case, whether income is to be included in gross income, is resolved by inquiring whether the taxpayer exercised dominion over the income in question.[26] In the case of an anticipatory assignment, the question becomes whether the assignor retained dominion over the income generating asset.[27] The Court noted that in the case of litigation recovery, the "income generating asset" is the cause of action itself. [28]The cause of action arises out of the plaintiff's legal injury, over which the injured party retains dominion.[29] Thus, the Court rejected the respondents' argument, and held that although a plaintiff's claim may be speculative at the moment the contingency agreement is made, the anticipatory assignment doctrine is not limited to instances in which the precise dollar amount is known in advance.[30]

The respondents further argued that the attorney-client relationship should be treated as a sort of business partnership or joint venture for tax purposes.[31] The Supreme Court rejected this argument as well, explaining that the attorney-client relationship is a quintessential principal-agent relationship.[32] The attorney is the agent and has a duty to act only in the interests of the principal, and, therefore, the attorney does not have dominion over the potential award.[33] The Court determined this rule applies regardless of whether or not state law confers any special rights or protection on the attorney, as long as the protections do not change the principal-agent nature of the relationship.[34] Although state law differs as to whether it confers a security interest in the contingency fee, and the remedies available to the attorney for payment, the Court stated it was unaware of any state that actually converts the attorney from agent into partner.[35] Thus, the Court also rejected the argument that the attorney-client relationship should be treated like a business partnership for tax purposes.[36] Ultimately, the United States Supreme Court held that the amount paid to an attorney pursuant to a contingency fee agreement, regardless of state law, is to be included in the plaintiff's gross income.[37]

B. Class Actions

- ***Barrie v. Intervoice–Brite, Inc., et al.***[38]

A panel comprising of Circuit Judges Fortunato P. Benavides, James L. Dennis and Edith Brown Clement considered an appeal from the dismissal of a securities fraud class action alleging violations of § 10(b) of the Securities Exchange Act of 1934 and Securities and Exchange Commission Rule 10b–5.[39] The corporate defendant developed and sold software and was formed as a result of a merger.[40] The company represented the merger

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25. *Id.*

26. *Id.* (citing *Commissioner v. Glenshaw Class Co.*, 348 U.S. 426, 431, 75 S.Ct. 473, 99 L.Ed. 483 (1955)).

27. *Id.*

28. *Id.*

29. *Id.*

30. *Banks*, 2005 WL 123825 at*5.

31. *Id.* at *6.

32. *Id.* (citing Restatement (Second) of Agency § 1, Comment *e* (1957); ABA Modern Rules of Professional Conduct, Conduct Rule 1.3. Comments 1, 1.7 (2002)).

33. *Id.*

34. *Id.*

35. *Id.* at *7.

36. *Id.*

37. *Id.* at *8.

38. 397 F.3d 249 (5th Cir. (Tex.) 2005).

39. *Barrie*, 397 F.3d at 253.

40. *Id.* at 254.

was a success, cited impressive revenues and projected strong earnings.[41] However, two years later, the company announced it would report a loss and lower than projected revenues and earnings per share.[42] A class action lawsuit ensued against the company and its chief officers.[43]

The class alleged that the defendants committed securities fraud by making false and misleading statements regarding the merger and its earnings as well as revenue projections and results.[44] The plaintiffs asserted that misleading statements that were based on improper accounting techniques were made in forward looking statements, press releases, and corporate documents, and were relied upon by analysts in their reports.[45] The defendants filed a motion to dismiss which was granted without prejudice, allowing the plaintiffs to file an amended complaint in compliance with the pleading requirements of the Private Securities Litigation Reform Act ("PSLRA") and Federal Rule of Civil Procedure 9(b).[46] The plaintiffs then filed the amended complaint; in turn, the defendants filed another motion to dismiss.[47] Such motion was granted; the plaintiffs' claims were subsequently dismissed with prejudice for failure to plead in conformity with the pleading requirements of the PSLRA and Rule 9(b); the plaintiffs appealed.[48]

The Fifth Circuit considered the plaintiffs' allegations; its analysis merits repetition. The plaintiffs alleged that the defendants violated § 10(b) by making false statements regarding revenues and earnings.[49] The PSLRA includes heightened pleading requirements for securities class action complaints; plaintiffs must specifically allege the following: (i) each fraudulent statement; (ii) who made the statement; (iii) why it was false; and (iv) that the statement was made with the requisite state of mind.[50] Pursuant to Securities and Exchange Commission Rule 10b–5, plaintiffs must plead the following: (i) a misstatement or omission; (ii) of a material fact; (iii) made with scienter; (iv) on which the plaintiffs relied; and (v) that proximately caused the plaintiffs' injuries.[51] Rule 9(b) also applies in securities fraud cases, and requires that the plaintiff specify (i) the allegedly fraudulent statement; (ii) the speaker; (iii) when and where the statement was made; and (iv) why the statement is fraudulent.[52]

On appeal, the plaintiffs alleged that the district court improperly applied the pleading requirements.[53] Regarding the claim of fraud in revenue recognition, the plaintiffs alleged that the revenues were a result of violations of the American Institute of Certified Public Accountants Statement of Position 97–2 ("SOP 97–2").[54] The defendants asserted their accounting methods were not improper and provided a fact based argument to support such an assertion.[55] The Circuit Court determined that a fact based argument is insufficient to support a motion to dismiss.[56] Because the accounting questions were in

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41. *Id.*

42. *Id.*

43. *Id.*

44. *Id.*

45. *Id.*

46. *Id.*

47. *Id.*

48. *Barrie*, 397 F.3d at 254.

49. *Id.*

50. *Id.* at 255.

51. *Id.* at 256 (citing *Southland Sec. Corp. v. INSpire Ins. Solutions Inc.*, 365 F.3d 353, 362 (5th Cir. 2004)).

52. *Id.* (citing *Southland*, 365 F.3d at 362).

53. *Id.*

54. *Id.*

55. *Id.*

56. *Id.* at 257.

dispute, the Court held dismissal was inappropriate.[57] The Court reviewed the complaint, and determined that the plaintiffs alleged with sufficient particularity that the defendants violated SOP 97–2.[58]

The Fifth Circuit further reviewed the plaintiffs' allegations of fraudulent earnings projections.[59] The complaint identified 23 allegedly fraudulent statements.[60] Six of such statements failed to adequately identify the speaker.[61] Eleven of the statements were made by third-party analysts.[62] In a third-party analyst situation, the plaintiff must plead facts from which the court could infer the defendant exercised the kind of control over the analyst and his reports that would render the defendant liable for the statements therein.[63] The complaint in the instant case did not identify which defendants supplied the allegedly false information to the analysts at issue, and therefore, the Court held these claims failed as well.[64] The other statements were allegedly made by two identified corporate officers.[65] The defendants asserted that the complaint did not specify which officer spoke and which officer failed to correct the misstatement, and, therefore, it did not sufficiently identify who made the alleged misstatement or omission.[66] The Fifth Circuit opined that in a case where it is pled with specificity that one defendant knowingly made a false statement and the other defendant knowingly failed to correct it, even if it is not specified who spoke and who remained silent, the fraud is sufficiently pled as to each defendant.[67] Thus, the Court held the claims as to these statements survived.[68]

After it determined which statements had been adequately plead as to the speaker, date and time, and why the statement was false, the Circuit Court considered whether the Complaint adequately plead scienter, and concluded that it did.[69] Therefore, the Fifth Circuit reversed in part the district court's dismissal and remanded the case for further proceedings.[70]

- ***Newby v. Enron Corp., et al.***[71]

This appeal before a panel composed of Circuit Judges Jerry E. Smith, Carl E. Stewart and Edward Charles Prado involved several securities class actions arising from Enron's downfall.[72] The putative class members in each class action differed.[73] The appellants in the instant case were members of the putative class, and objected to a proposed partial settlement with one of the defendants.[74] The trial court held a "fairness hearing," and ultimately approved the partial settlement.[75]

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57. *Barrie*, 397 F.3d at 257.

58. *Id.*

59. *Id.* at 259.

60. *Id.* at 260.

61. *Id.* at 261.

62. *Id.*

63. *Id.*

64. *Id.* at 262.

65. *Id.*

66. *Barrie*, 397 F.3d at 262.

67. *Id.*

68. *Id.*

69. *Id.* at 263.

70. *Id.*

71. 394 F.3d 296 (5th Cir. (Tex.) 2004).

72. *Newby*, 394 F.3d at 298.

73. *Id.*

74. *Id.* at 299.

75. *Id.* Due to the length and complexity of the facts in the instant case, this brief summary focuses on the approval process for a settlement and not the actual settlement proposed.

The Fifth Circuit scrutinized the process for settlement approval.[76] A proposed settlement is approvable if it is " 'fair, adequate, and reasonable and is not the product of collusion between the parties.' "[77] In determining the appropriateness of a proposed settlement, the trial court considers the following factors: (i) evidence that the settlement was obtained by fraud or collusion; (ii) the complexity, cost and length of the litigation; (iii) the present stage of the litigation and the available discovery; (iv) the probability of the plaintiffs' success on the merits; (v) the range of possible recovery and certainty of damages; and (vi) the opinions of counsel, the class representative and the class members.[78]

The Circuit Court reviewed the record in the instant case and determined that the district court faithfully applied the above detailed six factor test.[79] The district court found as follows: (i) that there was no evidence of collusion or fraud; (ii) that the complexity, length and cost of the impending litigation was enormous for all parties involved; (iii) that the future discovery would be expensive; (iv) that the plaintiffs' chances of prevailing on the merits were not good; (v) that assuming *arguendo* that the plaintiffs did prevail on the merits, the jurisdictional bars to recovery were significant; and (vi) that class counsel and defense counsel agreed with the court's judgment.[80] The Fifth Circuit opined that there was extensive support in the record, specifically the transcript of the fairness hearing, to support each position.[81] Therefore, the Court affirmed the district court's approval of the partial class settlement.[82]

C. Constitutional Torts

• ***Izen v. Catalina***[83]

In a *per curiam* opinion, the Fifth Circuit considered for the second time the granting of summary judgment in favor of IRS agents against a Texas attorney.[84] The relevant facts merit repetition. The plaintiff was a tax attorney who represented tax protestors and other defendants in criminal tax cases.[85] Defendant IRS agent Catalina received a referral from the Waco, Texas IRS office stating the plaintiff had not filed tax returns from 1986 though 1988.[86] The referral also contained allegations from an informant that the plaintiff was involved in money laundering.[87] Catalina conducted a preliminary investigation and concluded that the informant was unreliable.[88] Catalina determined there was insufficient information to investigate the plaintiff for money laundering, but did open a criminal tax investigation for failure to file returns.[89] The investigation was abandoned when the plaintiff filed returns for the missing years.[90] However, upon receiving reports concerning one of the plaintiff's clients, Catalina ultimately commenced a money laundering investigation.[91]

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76. *Id.* at 300.

77. *Id.* (quoting *Cotton v. Hinton*, 559 F.2d 1326, 1330 (5th Cir. 1977)).

78. *Id.* at 301 (citing *Reed v. General Motors Corp.*, 703 F.2d 170, 172 (5th Cir. 1983)).

79. *Id.* at 307.

80. *Id.*

81. *Newby*, 394 F.3d at 308.

82. *Id.* at 310.

83. 398 F.3d 363 (5th Cir. (Tex.) 2005).

84. *Izen*, 398 F.3d at 364.

85. *Id.* at 365.

86. *Id.*

87. *Id.*

88. *Id.*

89. *Id.*

90. *Id.*

91. *Id.* at 366.

Defendant IRS Agent Climer was the undercover agent assigned to the investigation.[92] Climer posed as a client seeking to deposit proceeds from the sale of stolen oil into a trust.[93] Based on the investigation, the plaintiff was indicted for conspiracy to commit money laundering.[94] Then, for undisclosed reasons, the United States moved to withdraw the presentment of the indictment, and the charges against the plaintiff were dismissed.[95]

The plaintiff filed suit alleging numerous constitutional and non-constitutional torts.[96] The district court dismissed the plaintiff's claims.[97] The plaintiff appealed the following: (i) the dismissal of his Fourth Amendment malicious prosecution claim; (ii) the dismissal of his First Amendment retaliation claim; (iii) the dismissal of his Fifth Amendment claim; (iv) the denial of his motion for disclosure of grand jury materials; and (v) the granting of summary judgment in favor of the defendants based on qualified immunity.[98]

During its first review of the instant case, the Fifth Circuit reversed the dismissal of the malicious prosecution and retaliation claims on the basis that the district court had misconstrued the applicable law.[99] Further, the Court held that a genuine issue of material fact existed as to whether the plaintiff was prosecuted for representing criminal tax defendants.[100] On remand, the plaintiff filed an amended complaint which additionally asserted a Federal Tort Claims Act ("FTCA") cause of action against the United States.[101] The district court again granted summary judgment on all claims and the plaintiff again appealed.[102]

During its second review, the Circuit Court first addressed the malicious prosecution claim.[103] The Court explained that in the Fifth Circuit, plaintiffs do not successfully allege a constitutional violation by only satisfying the state law elements of malicious prosecution.[104] Because the plaintiff did not state a claim under the Fourth Amendment directly, the Circuit Court held the district court properly granted the defendants' motion for summary judgment on this claim.[105]

The Fifth Circuit then addressed the plaintiff's FTCA cause of action.[106] This cause of action was based on the state torts of malicious prosecution, false arrest, intentional infliction of emotional distress and negligence.[107] A claim under the FTCA requires exhaustion—i.e., a plaintiff must present his claim first to the appropriate agency and receive an adverse result prior to filing suit.[108] Although the plaintiff did file an administrative complaint with the IRS, the district court held that the scope of the claims in his amended complaint went beyond the claims asserted in his administrative complaint, and, therefore, the claims failed for lack of exhaustion.[109] The Fifth Circuit

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92. *Id.*

93. *Izen*, 398 F.3d at 366.

94. *Id.*

95. *Id.*

96. *Id.*

97. *Id.*

98. *Id.*

99. *Id.*

100. *Id.*

101. *Id.*

102. *Izen*, 398 F.3d at 366.

103. *Id.*

104. *Id.* at 367.

105. *Id.*

106. *Id.*

107. *Id.*

108. *Id.* (citing 28 U.S.C. § 2675).

109. *Id.*

determined that the district court properly dismissed the FTCA claim on this basis.[110]

Finally, the Circuit Court addressed the First Amendment retaliation claim.[111] The First Amendment prohibits adverse action by the government against an individual for exercising his First Amendment rights.[112] In a criminal prosecution context, a plaintiff must establish the following to make out a retaliation claim: (i) that he was engaged in a constitutionally protected activity; (ii) that the defendant's actions caused an injury that would dissuade a person of "ordinary firmness" from again participating in such activity; and (iii) that the defendant's adverse action was substantially motivated against the constitutionally protected conduct.[113] The Fifth Circuit also requires that a plaintiff establish each of the common law malicious prosecution elements. Malicious prosecution requires the lack of probable cause to prosecute.[114] For purposes of malicious prosecution, probable cause means "the existence of facts and circumstances that would excite the belief, in a reasonable mind, acting on the facts within the knowledge of the prosecutor, that the person charged was guilty of the crime for which he was prosecuted."[115]

In the instant case, the district court granted summary judgment because it found the plaintiff had not established the common law elements of malicious prosecution, particularly, whether the agents lacked probable cause to prosecute.[116] The Circuit Court determined that although the initial information received by Catalina was deemed unreliable, the subsequent investigation yielded reliable information concerning the plaintiff's "questionable activities" sufficient to provide probable cause to seek an indictment.[117] The Court further reviewed the information Catalina relied on in seeking the indictment, and held that all of the evidence, taken in its entirety, demonstrated probable cause as a matter of law.[118] Thus, the district court properly granted summary judgment on the retaliation claim.[119] The Fifth Circuit, therefore, affirmed the dismissal of all of the plaintiff's claims.[120]

D. Contracts

• ***Mumblow v. Monroe Broadcasting, Inc.***[121]

Before a panel comprising of Circuit Judges Jerry E. Smith, Reynaldo G. Garza, and District Judge Sarah Vance, sitting by designation, the plaintiff, an individual lender and president of a Louisiana corporation, brought suit to recover his loans to a corporate borrower.[122] The specifics of the transaction merit articulation. The Chairman and principal shareholder of the company acquired properties from the owner of the defendant, also a Louisiana corporation.[123] As part of the negotiations, the Chairman agreed to indemnify the owner of the defendant company against the financial risk of owning and operating such a company.[124] This was memorialized in a "put/call" agreement that gave the Chairman the right to buy, and the defendant the right to call upon him to buy the

110. *Id.*

111. *Id.*

112. *Izen*, 398 F.3d at 367 (citing *Colson v. Grohman*, 174 F.3d 498, 508 (5th Cir. 1999)).

113. *Id.* (citing *Keenan v. Tejeda*, 290 F.3d 252, 258 (5th Cir. 2002)).

114. *Id.* at 368.

115. *Id.*

116. *Id.*

117. *Id.*

118. *Id.*

119. *Id.*

120. *Id.* at 370.

121. No. 03–31013, 2005 WL 459243 (5th Cir. (La.) Feb. 28, 2005).

122. *Mumblow*, 2005 WL 459243 at *1.

123. *Id.*

124. *Id.*

defendant for a price that was the sum of the defendant's debts and liabilities. The Chairman received a loan from the bank, the terms of which required he stop drawing his salary from the company because of its weak financial condition.[125] The plaintiff suggested that they advance their salaries to the defendant to ease the burden on the Chairman.[126] The plaintiff began advancing his salary of $14,000.00 per month to the defendant.[127] The defendant, with the assistance of the Chairman and the plaintiff, arranged a working capital infusion by refinancing its debts through a loan.[128] As collateral for the loan, the plaintiff originally agreed to put up $500,000.00 but later withdrew his offer.[129] The Chairman made up the difference.[130] The loan included a large line of credit.[131] The plaintiff continued to forward his salary to the defendant for another eight months after the loan was final.[132] Nothing other than the cancelled checks existed to memorialize the agreement between the defendant and the plaintiff.[133]

Four months after ceasing to forward his checks, the plaintiff demanded repayment of the loan.[134] The defendant refused, and the plaintiff filed suit.[135] The trial court concluded the following: (i) Louisiana law governed the choice of law determination; (ii) Louisiana law applied to the transactions; (iii) under applicable Louisiana law, the loan was subject to an "implied suspensive condition" that suspended the plaintiff's right to demand repayment until the defendant's asserts were either sold or merged; and (iv) the plaintiff's demand for payment was premature because the suspensive condition had not matured.[136] The plaintiff appealed.[137]

After determining that Louisiana law did in fact control the instant case, the Fifth Circuit turned to the question of whether the "implied suspensive condition" analysis applied by the district court was valid.[138] Under Louisiana law, conditions on an obligation may be implied by law, the nature of the contract, or the intent of the parties.[139] A finding that the parties intended an obligation to be conditional is a finding of fact reviewed for clear error.[140] Clear error exists under the following circumstances: (i) the findings are without substantial evidence to support them; (ii) the court misapprehended the effect of the evidence; and (iii) if, although there is evidence which if credible would be substantial, the testimony considered as a whole convinces the court that the findings were so against the preponderance of the credible evidence that they do not represent the truth.[141]

The trial court cited the plaintiff's knowledge of the defendant's weak financial condition as evidence that the parties intended the payment obligation to be conditional.[142] The Circuit Court disagreed.[143] The Court reviewed the record, and concluded it did

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125. *Id.*

126. *Id.*

127. *Id.*

128. *Id.*

129. *Id.*

130. *Mumblow*, 2005 WL 459243 at *1.

131. *Id.*

132. *Id.*

133. *Id.*

134. *Id.*

135. *Id.*

136. *Id.*

137. *Id.*

138. *Id.* at *2–3.

139. *Mumblow*, 2005 WL 459243 at *3 (citing LA. CIV. CODE art. 1768).

140. *Id.* (citing *Gebreyesus v. F.C. Schaffer & Assoc., Inc.*, 204 F.3d 639, 642 (5th Cir. 2000)).

141. *Id.* at *4 (citing *Moorhead v. Mitsubishi Aircraft Int'l, Inc.*, 828 F.2d 278, 283 (5th Cir. 1987)).

142. *Id.*

not contain substantive evidence leading it to believe the parties intended such a restrictive suspensive condition.[144] Further, courts do not infer such conditions absent compelling proof.[145] The Court explained that courts will only find such conditions wher the express language in the contract compels such a construction.[146] In the case of an oral agreement, such a condition should not be inferred unless it is clear from the evidence that the parties agreed on such a condition.[147] The Fifth Circuit opined as follows:

> Because suspensive conditions are disfavored and the burden of proof is on the party relying on the condition, the trial court should not have inferred a suspensive condition in the absence of evidence that would at least substantially support that inference. In this case, no such evidence exists, and the trial court's inference is therefore clearly erroneous.[148]

The Court did note that, in contrast, the inference that the parties did not intend to impose such a condition on repayment is supported by the evidence in the record.[149] The plaintiff testified that he expected to demand repayment eventually.[150] No witnesses were presented to contradict such an intention.[151] Accordingly, the Fifth Circuit concluded there was no condition on the plaintiff's right to repayment, and remanded the case for the trial court to determine when the plaintiff should be repaid.[152]

E. Jurisdiction and Federal Procedure

- ***United States ex rel Garibaldi v. Orleans Parish School Board***[153]

With a panel composed of Circuit Judges Thomas M. Reavley, Edith H. Jones and James L. Dennis, the Fifth Circuit considered, for a second time, an appeal involving a *qui tam* action under the False Claims Act ("FCA").[154] In the previous appeal, the Circuit Court vacated the plaintiff's judgment on the verdict and rendered judgment for the defendant, holding a school board is not a "person" subject to liability under the FCA.[155] Subsequently, the United States Supreme Court decided *Cook County, Ill. v. United States ex rel Chandler*,[156] in which it held local governments are "persons" amenable to *qui tam* actions under the FCA.[157] Following the *Chandler* decision, the plaintiff in the instant action filed a motion in the district court pursuant to Rule 60(b)(6), requesting relief from the Fifth Circuit's final judgment in *Garibaldi I*.[158] The district court determined *Chandler* overruled *Garibaldi I*, granted the plaintiff's motion and reinstated the judgment in favor of the plaintiff.[159] The defendant school board appealed.[160]

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143. *Id.*

144. *Id.*

145. *Id.*

146. *Id.*

147. *Id.*

148. *Mumblow*, 2005 WL 459243 at *4.

149. *Id.* at *5.

150. *Id.* at *6.

151. *Id.*

152. *Id.* at *7.

153. 397 F.3d 334 (5th Cir. (La.) 2005).

154. *Garibaldi*, 397 F.3d at 335.

155. *Id.*

156. 538 U.S. 119, 123 S.Ct. 1239, 155 L.Ed.2d 247 (2003).

157. *Garibaldi*, 397 F.3d at 336.

158. *Id.*

159. *Id.*

160. *Id.*

The Fifth Circuit identified the question before it as whether the decision in *Chandler,* combined with the facts of the instant case, gave rise to the "extraordinary circumstances" required for a district court to exercise its discretion under Rule 60(b)(6), and grant relief from a final judgment.[161] The Court explained Rule 60(b)(6) authorized a court to grant relief to a party from a final judgment for any reason justifying relief other than those grounds enumerated in clauses (b)(1) through (b)(5), and only in "extraordinary circumstances."[162] The Fifth Circuit noted that it has previously held that a change in decisional law after the entry of a final judgment does not constitute extraordinary circumstances, and is not by itself grounds for relief from such judgment.[163]

The Circuit Court acknowledged that the district court found that the requisite extraordinary circumstances existed, reasoning that the decision in *Garibaldi I* caused the circuit split regarding the definition of "person" under the FCA upon which *certiorari* in *Chandler* was justified.[164] The district court determined the instant case fell within the "extraordinary circumstances" recognized by the Fifth Circuit in *Batts v. Tow-Motor Forklift Co.*[165] According to the district court, the Fifth Circuit stated in *Batts* that Rule 60(b)(6) relief is justified when " 'a subsequent court decision is closely related to the case in question, such as where the Supreme Court resolves a conflict between another circuit ruling and that case occurs.' "[166]

The Fifth Circuit opined that the instant case is not atypical of the frequent instances in which the Supreme Court grants *certiorari* and renders a decision resolving a circuit split.[167] In such a case, several litigants could argue that their case should be reopened because if the relevant decision had been precedent at the time they filed suit, the outcome would have been different.[168] The Circuit Court determined such cases, including the instant case, do not present the "extraordinary circumstances" necessary to justify reopening a judgment.[169] Moreover, the Court noted the language from *Batts* relied on by the plaintiff was dicta, and therefore, "may not have received the considered judgment of the whole court."[170] Thus, the Fifth Circuit concluded as follows:

> [T]he great desirability of preserving the principle of finality of judgments preponderates heavily over any claim of injustice in this case. Disturbing the sanctity of the final judgment in this case would implicate the doctrine of res judicata in many other cases in which litigants might seek to reap the benefit of a change in decisional law after the judgments against them have become final.[171]

- ***Dominguez-Cota v. Cooper Tire & Rubber Co.***[172]

In this brief *per curiam* opinion, the Fifth Circuit considered whether the trial court properly dismissed the plaintiffs' claims on *forum non conveniens* grounds.[173] The underlying litigation involved an automobile accident in Mexico.[174] The plaintiffs were all

161. *Id.* at 337.

162. *Id.*

163. *Id.* (citing *Picco v. Global Marine Drilling Co.,* 900 F.2d 846, 849 (5th Cir. 1990)).

164. *Id.*

165. 66 F.3d 743, 747 (5th Cir. 1995).

166. *Garibaldi,* 397 F.3d at 338 (quoting *Batts v. Tow-Motor Forklift Co.,* 66 F.3d at 748 n.6).

167. *Id.*

168. *Id.*

169. *Id.*

170. *Id.*

171. *Id.* at 340.

172. 396 F.3d 650 (5th Cir. (Miss.) 2005).

173. *Dominguez-Cota,* 396 F.3d at 651.

174. *Id.* at 652.

Mexican nationals and alleged that the car and the tires were both defective.[175] The suit was brought in state court in Mississippi and the defendants removed to federal court.[176] The defendants then moved to dismiss the action based on *forum non conveniens* grounds.[177] In granting the motion, the district court decided the *forum non conveniens* issue before determining whether it had subject matter jurisdiction over the controversy.[178]

The Fifth Circuit considered whether the district court erred in dismissing the case before making the subject matter jurisdiction determination.[179] The Court noted it is a well settled principle that before proceeding with a case a federal district court or appellate court has a duty to examine the basis of its subject matter jurisdiction, *sua sponte* if necessary.[180] The plaintiffs asserted that the United States Supreme Court's holding in *Ruhrgas AG v. Marathon Oil Co., et al.*[181] "grants courts the discretion to evaluate threshold 'non-merits issues' before ruling on subject matter jurisdiction."[182] The plaintiffs characterized *forum non conveniens* as a "non-merits" issue and asserted that the district court's dismissal of the case was proper.[183] The Circuit Court determined that the plaintiffs read *Ruhrgas* too broadly.[184] In *Ruhrgas*, the U.S. Supreme Court held that while federal courts are required to evaluate subject matter jurisdiction before considering the merits of a case, the district court in that case did not abuse its discretion by considering personal jurisdiction before it reached subject matter jurisdiction.[185]

The Fifth Circuit disagreed with the plaintiffs' argument that *Ruhrgas* could be extended to all "non-merits" issues.[186] The Court reasoned that even if *Ruhrgas* could be so read, a *forum non conveniens* inquiry is not entirely separate from the merits of the case.[187] The Circuit Court reminded practitioners of the steps involved in a *forum non conveniens* inquiry.[188] First, the defendant must show that an alternate forum is available and adequate.[189] "An available forum is one where the case and all the parties can come within its jurisdiction."[190] Then, the defendant must show the following: (i) the relative ease of access to sources of proof; (ii) the availability of a compulsory process to secure the attendance of willing witnesses; and (iii) other factors affecting the case such as speed, expense, and enforceability of a judgment.[191] If these factors do not indicate that another forum is better suited for trial, the court should examine public interest factors such as: (i) administrative difficulties and court congestion; (ii) the interest of having local controversies decided at home; (iii) having a case decided in the same place as the law governing the issues; (iv) avoidance of conflict of laws; (v) application of foreign law; and (vi) the burden to the citizens of an unrelated forum with jury duty.[192]

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175. *Id.*

176. *Id.*

177. *Id.*

178. *Id.*

179. *Id.*

180. *Id.* (citing *Torres v. Southern Peru Copper Corp.*, 113 F.3d 540, 542 (5th Cir. 1997)).

181. 526 U.S. 574, 119 S.Ct. 1563, 143 L.Ed.2d 760 (1999).

182. *Dominguez-Cota*, 396 F.3d at 652.

183. *Id.*

184. *Id.*

185. *Id.*

186. *Id.*

187. *Id.* at 653 (citing *Van Cauwenberghe v. Biard*, 486 U.S. 517, 527–28, 108 S.Ct. 1945, 100 L.Ed.2d 517 (1988)).

188. *Id.*

189. *Id.*

190. *Id.*

191. *Dominguez-Cota*, 396 F.3d at 653.

192. *Id.* at 654 (citing *Brokerwood Products International, Inc. v. Cuisine Crotone, Inc.* 104 Fed.Appx. 376 (5th Cir. 2004)).

The Fifth Circuit explained that in order to apply the above analysis, a court must look at the particular facts of a case, and to that extent, must reach the case's merits.[193] Thus, the Circuit Court held that it was unable to characterize *forum non conveniens* as a "non-merits" issue akin to personal jurisdiction, and remanded the case to the district court to determine the subject matter jurisdiction issue.[194]

- ***Schexnayder v. Entergy Louisiana, Inc.***[195]

A panel comprising of Circuit Judges Harold R. DeMoss, Jr., James L. Dennis and Edith Brown Clement considered whether a district court's remand of a case was reviewable.[196] The defendant, Entergy Services, was a group of affiliated companies that owned, operated and provided telecommunication services to parts of several states, including Louisiana.[197] Entergy began to upgrade its infrastructure with fiber optic cable lines.[198] The plaintiffs claimed to own the land where Entergy installed the cables and filed suit against Entergy in state court.[199] The action alleged Entergy engaged in civil trespass and fraud.[200] An intervening plaintiff asserted a federal civil R.I.C.O. claim pursuant to 18 U.S.C. § 1961 against Entergy.[201] Entergy removed the case to federal court based on the federal R.I.C.O. claim, and the plaintiffs filed a motion to remand.[202] The plaintiffs argued: (i) removal jurisdiction cannot be based on an intervener's claim; and (ii) the intervention "followed deficient state procedure."[203] Entergy then filed an amended removal motion asserting federal jurisdiction on the argument that the trial court would have to construe the Public Utility Holding Company Act in order to resolve the trespass and fraud claims.[204] The district court remanded the case to state court and this appeal ensued.[205]

The Fifth Circuit began its analysis by reminding practitioners that "Congress has severely circumscribed the power of federal appellate courts to review remand orders."[206] The controlling statute, 28 U.S.C. § 1447(d), provides as follows: "An order remanding a case to the state court from which it was removed is not reviewable on appeal or otherwise."[207] However, the Circuit Court explained that despite the statute's plain language, the U.S. Supreme Court has created a limited exception, the premise of which is that in order for a remand order to be unreviewable, the district court must act within the authority granted by § 1447(c)-(d).[208] Only remands based on the grounds specified in § 1447 (c) are immune from review under § 1447(d).[209] Read together, federal appellate courts lack jurisdiction under § 1447(d) if the district court based its remand order on either lack of subject matter jurisdiction or a defect in the removal procedure. If the order is to be reviewable, the district court must " 'affirmatively state a non–1447(c) ground for

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193. *Id.*

194. *Id.*

195. 394 F.3d 280 (5th Cir. (La.) 2004).

196. *Entergy*, 394 F.3d at 282.

197. *Id.*

198. *Id.*

199. *Id.*

200. *Id.*

201. *Id.*

202. *Id.*

203. *Id.*

204. *Id.*

205. *Id.*

206. *Entergy*, 394 F.3d at 283 (citing 28 U.S.C. § 1447(d)).

207. *Id.* (quoting 28 U.S.C. § 1447(d)).

208. *Id.* (citing *Quackenbush v. Allstate Ins. Co.*, 517 U.S. 706, 711–12, 116 S.Ct. 1712, 135 L.Ed.2d 1 (1996)).

209. *Id.* (citing *Things Remembered, Inc. v. Petrarca*, 516 U.S. 124, 127, 116 S.Ct. 494, 133 L.Ed.2d 461 (1995)).

remand.' "[210] The Court provided examples of non–1447(c) grounds: (i) remands made for purely discretionary reasons; (ii) abstention-based remands; (iii) remands based on § 1367; (iv) remands based on § 1445(c); and (v) remands based on the district court's discretionary powers under § 1441(c).[211]

In the instant case, the district court based the remand on the following two factors: (i) Entergy's removal petition was untimely based on § 1446(b); and (ii) Entergy could not base the petition on the intervening plaintiff's federal claim.[212] The Fifth Circuit determined these two grounds constituted allowable grounds for remand under § 1447(c), and consequently, that it lacked jurisdiction to review the district court's remand order.[213]

A discussion of the Fifth Circuit's analysis merits scrutiny. Entergy argued that the Circuit Court did have jurisdiction because a district court is not authorized to remand a case for reasons that were not listed in the original motion for remand.[214] The Court opined that while there is no such ruling in the Fifth Circuit case law, Entergy argued this conclusion flows from the Fifth Circuit holding in *In re Allstate*.[215] In *Allstate*, the Circuit Court held that a district court is not authorized to *sua sponte* remand a case for procedural defects.[216] Entergy contended that although the plaintiffs filed a timely motion, the district court remanded the case for reasons not asserted in the motion, and, thus, acted outside of its authority pursuant to § 1447(c).[217] Entergy argued that such a remand order is indistinguishable from a *sua sponte* motion.[218]

The Fifth Circuit disagreed and stated as follows: "We find no grounds in the statutory language of § 1447(c) or (d), and Entergy asserts none, to support such a holding."[219] The Fifth Circuit distinguished motions from issues.[220] In *Allstate*, no motion for remand was ever filed—the court's *sua sponte* action was the equivalent of a motion.[221] In the instant case, a motion was filed—the court merely raised an additional issue on its own.[222] The Circuit Court opined that by its own terms, the statute is limited to motions, not issues.[223] Therefore, the Fifth Circuit held that it did not have the ability to review the district court's remand order under either of the defendant's arguments, and dismissed the appeal.[224]

F. Products Liability and Negligence

- ***Caboni v. General Motors Corp., et al.*[225]**

With a panel composed of Rhesa H. Barksdale, Emilio M. Garza and Harold R. DeMoss, the Fifth Circuit heard an appeal for the second time in this products liability case.[226] The plaintiff was driving a pickup truck manufactured by the defendant when he

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210. *Id.* (quoting *Smith v. Tex. Children's Hosp.*, 172 F.3d 923, 926 (5th Cir. 1999)).

211. *Id.*

212. *Id.*

213. *Id.*

214. *Id.*

215. 8 F.3d 219 (5th Cir. 1993).

216. *Entergy*, 394 F.3d at 283.

217. *Id.* at 284.

218. *Id.*

219. *Id.*

220. *Id.* at 285.

221. *Id.*

222. *Id.*

223. *Id.*

224. *Id.*

225. 398 F.3d 357 (5th Cir. (La.) 2005).

226. *Caboni*, 398 F.3d at 358.

was involved in an accident in which his air bag failed to deploy.[227] The plaintiff filed suit under the Louisiana Products Liability Act[228] ("LPLA") claiming damages for injuries including those resulting from his head hitting the steering wheel.[229] Specifically, the plaintiff alleged the air bag was unreasonably dangerous because it did not conform to the express warranty in the owner's manual.[230] The defendant removed the case to federal district court based on diversity, and filed a motion for summary judgment alleging the plaintiff could not establish the elements required for an express warranty claim under the LPLA.[231] The district court granted the defendant's motion.[232]

In *Carboni I*,[233] the Fifth Circuit reversed and remanded for further consideration, concluding that material issues of fact existed as to the following: (i) whether the statement about the air bag in the owner's manual was an express warranty; (ii) whether the plaintiff was induced to purchase the truck by the warranty; (iii) whether the truck conformed to the warranty; and (iv) whether the falsity of the warranty caused additional injuries to the plaintiff.[234] On remand, the jury found the plaintiff had been injured and that the defendant was 30% responsible for the damages.[235]

The defendant filed a Motion for Judgment as a Matter of Law, which the court denied.[236] The defendant additionally filed a Motion to Amend the Judgment and Grant Remittitur, which was granted.[237] The trial court eliminated the plaintiff's damages for loss of future earning capacity and reduced his medical expenses.[238] The plaintiff refused the remittitur and a new trial was held on the loss of earnings and medical expenses.[239] The jury returned a verdict finding no damages for future medical expenses or loss of earning capacity.[240] Therefore, the trial court entered an Amended Judgment in favor of the plaintiff for a lesser amount.[241] The plaintiff filed a Motion for New Trial, which the trial court denied.[242] The defendant appealed the judgment in favor of the plaintiff.[243]

On appeal, the defendant argued that the plaintiff failed to prove the following: (i) that his truck did not conform to the express warranty; and (ii) that he sustained an enhanced injury that was proximately caused because the express warranty was untrue.[244] The Fifth Circuit first addressed the denial of the defendant's Motion for Judgment as a Matter of Law. The Court reminded practitioners that "judgment as a matter of law is appropriate if 'there is no legally sufficient evidentiary basis for a reasonable jury to find for that party on that issue.' "[245] In reviewing the evidence, the

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227. *Id.*

228. LA. REV. STAT. ANN. §§ 9:2800.51–9:2800.60.

229. *Caboni*, 398 F.3d at 358.

230. *Id.* at 359.

231. *Id.*

232. *Id.*

233. *Caboni v. Gen. Motors Corp.*, 278 F.3d 448 (5th Cir. 2002).

234. *Caboni*, 398 F.3d at 359.

235. *Id.*

236. *Id.*

237. *Id.*

238. *Id.*

239. *Id.*

240. *Id.*

241. *Id.*

242. *Id.*

243. *Caboni*, 398 F.3d at 359.

244. *Id.*

245. *Id.* (quoting FED. R. CIV. PROC. 50(a)(1)).

appellate court must draw all reasonable inferences in favor of the non-movant, and may neither make credibility determinations nor weigh the evidence.[246]

The Circuit Court then reviewed the relevant LPLA provisions.[247] Under the LPLA, a plaintiff can prove that a product is unreasonably dangerous by showing it does not conform to an express warranty, such as the plaintiff asserted in the instant case.[248] The defendant argued for the first time during oral argument that the owner's manual did not constitute an express warranty regarding the air bag because it was only a general description of the truck.[249] Because the defendant failed to brief this issue on appeal, the Fifth Circuit determined the argument was waived.[250]

The defendant further argued that the plaintiff's argument that the air bag failed to conform to the express warranty was without merit.[251] The Circuit Court explained that the proper inquiry under the LPLA is whether the product performed as described by the language of the warranty, not whether it performed as it was designed to perform. [252]The defendant relied on the plaintiff's expert witness at trial in arguing the air bag did not fail to conform to the warranty because the truck was not traveling at a speed that met the threshold level needed to deploy the airbag, and because the crash was not a head on collision.[253] The Fifth Circuit noted there was more than ample evidence in the record to show the air bag did not perform as described by the warranty.[254] The testimony of the plaintiff's expert provided evidence that the truck was traveling 13 to 18 miles per hour above the relevant threshold speed required in the owner's manual, and that the accident was a "near-frontal" crash, which was all the owner's manual required.[255] The Circuit Court concluded that the defendant's argument that the air bag performed as described by the owner's manual failed because a reasonable jury could, and in fact did, arrive at a contrary verdict.[256]

Finally, the defendant argued that the plaintiff failed to show his damages were proximately caused because the express warranty was not true.[257] In the instant case, proximate causation required that the plaintiff show that he sustained more severe injuries than he would have received if the air bag deployed.[258] The defendant argued that the plaintiff failed to present any expert testimony, and that the jurors needed expert testimony to properly evaluate the issue.[259] The defendant asserted that its expert testified that the plaintiff's injuries would have been the same whether or not the air bag had deployed.[260] The Fifth Circuit reviewed the expert testimony on direct and cross-examination.[261] The court explained the trier of fact is not bound by expert testimony—the jurors are entitled to weigh the credibility of *all* witnesses, both expert and lay.[262] Although the jury was free to accept or not accept the testimony of the defendant's

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246. *Id.* (citing *Reeves v. Sanderson Plumbing Prods., Inc.*, 530 U.S. 133, 150, 120 S.Ct. 2097, 147 L.Ed.2d 105 (2000)).

247. *Id.* at 360.

248. *Id.*

249. *Id.*

250. *Id.* (citing *Yohey v. Collins*, 985 F.2d 222, 224–25 (5th Cir. 1993)).

251. *Id.*

252. *Caboni*, 398 F.3d at 360

253. *Id.*

254. *Id.*

255. *Id.*

256. *Id.*

257. *Id.*

258. *Id.* at 361.

259. *Id.*

260. *Id.*

261. *Caboni*, 398 F.3d. at 361.

262. *Id.*

expert, under the LPLA, the plaintiff has the burden of proving each element of the claim, including the enhanced injury element.[263]

The plaintiff contended that despite the contention that the defendant's expert was the only expert witness to testify on this issue, he did in fact present expert testimony, specifically: (i) that he suffered head injuries from hitting the steering wheel (ii) that he probably would not have hit the steering wheel if the air bag had properly deployed; and (iii) he suffered a brain injury as a result of hitting the steering wheel.[264] The Fifth Circuit distinguished the issues—this evidence proved only that he suffered an injury, not that the injury suffered was more severe because the air bag failed to deploy.[265] Because the plaintiff could not show that he suffered an enhanced injury as a result of the failure of the air bag to conform to the express warranty, the Fifth Circuit held that a reasonable jury could not have arrived at a verdict against the defendant, vacated the district court judgment, and rendered a take nothing judgment against the plaintiff.[266]

G. Securities Fraud

• ***Krim v. PCOrder.com***[267]

With a panel comprising of Circuit Judges Patrick E. Higginbotham, W. Eugene Davis and Reynaldo G. Garza, the Fifth Circuit considered whether the plaintiffs in a securities fraud action had standing.[268] The defendant conducted an initial public offering ("IPO") and then a secondary public offering ("SPO") ten months later.[269] Along with each offering, the defendant filed a registration statement with the SEC.[270] The plaintiffs were a group of investors who sought to file a class action pursuant to Section 11 of the Securities Exchange Act of 1933.[271] Section 11 provides a cause of action to any person acquiring shares issued pursuant to an untrue registration statement.[272] In the instant case, the plaintiffs alleged the defendant's registration statements were misleading.[273] The district court denied class certification.[274] The district court held that Section 11 is only available to the following plaintiffs: (i) those who purchased their stock during the relevant public offerings; or (ii) those purchasers that can "trace" their stock back to such offering.[275]

In considering whether the lead plaintiffs could trace their stock to the IPO or SPO, the district court found only one plaintiff was able to do so. One lead plaintiff purchased his stock from a pool of stock that contained only IPO stock, and, therefore, was able to satisfy the traceability requirement and establish standing.[276] However, the other two lead plaintiffs could not make such a showing.[277] At the time of their purchases, the stock pools had become contaminated with "outside shares" and there was no way to track the individual shares through a contaminated pool.[278] Therefore, in light of the intermingling

263. *Id.*

264. *Id.* at 362.

265. *Id.*

266. *Id.* at 363.

267. No. 03–50737, 2005 WL 469618 (5th Cir. (Tex.) Mar. 1, 2005).

268. *Krim*, 2005 WL 469618 at *1.

269. *Id.*

270. *Id.*

271. *Id.*

272. *Id.*

273. *Id.*

274. *Id.*

275. *Id.*

276. *Id.*

277. *Krim*, 2005 WL 469618 at *1.

278. *Id.*

of public offering and non-public offering shares in the market at the time of purchase by two of the lead plaintiffs, the putative class could not prove that all the stock from which they claimed damages was issued pursuant to a defective registration statement; therefore, the district court concluded they could not serve as class representatives and denied the certification.[279] The plaintiffs appealed not the denial of the class certification, but the trial court ruling that standing was dependent upon direct traceability.[280]

The plaintiffs argued that Section 11 standing exists if statistics indicate a high that the shares at issue were purchased pursuant to the defective statement.[281] This probability is a probability based on the number of shares purchased by each plaintiff and the number of public offering shares in the market.[282] The Fifth Circuit first considered the language of the statute.[283] Section 11 provides an almost absolute liability on a company issuing shares pursuant to a defective registration statement, regardless of the intent or lack thereof to provide misleading information.[284] The statute's standing provision limits plaintiffs to "those who purchase securities that are the direct subject of the prospectus and registration statement."[285] The Circuit Court noted that it recently held that aftermarket purchasers do not automatically lack standing.[286] Aftermarket purchasers have Section 11 standing so long as they can demonstrate the ability to trace their shares to the faulty registration statements.[287] The Court explained that in order to be able to take advantage of the lower burden of proof and almost strict liability under Section 11, a plaintiff is required to meet higher procedural standards, such as that required by the statute—to be able to trace the security for which the damages are sought to the statement which provides the defendant's liability.[288]

The plaintiffs were aftermarket purchasers.[289] They argued that they could demonstrate standing by showing a high probability that their securities were issued pursuant to the faulty statement—i.e., by a preponderance of the evidence.[290] The Fifth Circuit opined that accepting "statistical tracing" would impermissibly expand the statute's standing requirement.[291] The Court further noted that the jurisprudence did not support Section 11 standing based on the plaintiff's statistical tracing theory.[292]

Thus, the Fifth Circuit held that aftermarket purchasers seeking Section 11 standing must demonstrate that their shares are traceable to the allegedly faulty registration statement, and determined the statistical tracing method espoused by the plaintiffs was insufficient to meet this requirement.[293] Therefore, plaintiffs seeking to recover for securities fraud must still show that they purchased shares that were issued directly from the defective registration statement.[294] Accordingly, the Fifth Circuit affirmed the dismissal of the plaintiffs' claims.[295]

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279. *Id.* at *2.

280. *Id.*

281. *Id.* at *3.

282. *Id.*

283. *Id.*

284. *Id.*

285. *Id.*

286. *Id.* (citing *Rosenzweig v. Azurix Corp.*, 332 F.3d 854, 872 (5th Cir. 2003)).

287. *Krim*, 2005 WL 469618 at *3.

288. *Id.*

289. *Id.*

290. *Id.* at *4.

291. *Id.*

292. *Id.* at *5.

293. *Id.* at *7.

294. *Id.*

295. *Id.*

• ***R2 Investments LDC v. Phillips***[296]

With a panel composed of Circuit Judges Rhesa H. Barksdale, Emilio M. Garza and Harold R. DeMoss, Jr., the Fifth Circuit provided practitioners with a review of the elements of a securities fraud claim under Section 10(b) and Rule 10b–5.[297] The plaintiff brought suit against the officers and directors of a now bankrupt company, alleging the following: (i) securities fraud; (ii) common-law fraud; (iii) conspiracy; and (iv) negligent representation.[298] The suit was related to the defendants' failure to complete a tender offer to repurchase certain previously issued notes.[299] The defendants moved to dismiss the federal securities claims for failure to state a claim.[300] The district court granted the motion and dismissed the state law causes of action as well, declining to exercise its supplemental jurisdiction.[301] This appeal followed.[302]

In determining whether the plaintiff successfully stated a federal securities fraud claim, the Fifth Circuit reviewed Section 10(b) and Rule 10b–5.[303] In order to successfully state a claim, a plaintiff must allege, in connection with the purchase or sale of a security, the following: (i) a misstatement or omission; (ii) of a material fact; (iii) made with scienter; (iv) upon which the plaintiff relied; (v) that proximately caused the plaintiff's injury.[304] Plaintiffs asserting such claims must also satisfy enhanced pleading requirements pursuant to the Private Securities Litigation Reform Act of 1995 ("PSLRA") as well as FED. R. CIV. PROC. 9(b).[305]

The PSLRA requires a plaintiff to specify the following with particularity: (i) each allegedly misleading statement; (ii) the reasons why it was misleading; (iii) if the allegation is made "on information and belief," all the facts upon which such belief was formed; and (v) that the defendant acted with the required state of mind.[306] Rule 9(b) requires a plaintiff plead with particularity all of the circumstances constituting the fraud, which has been interpreted to mean the plaintiff must specify the following: (i) the allegedly fraudulent statement; (ii) the speaker; (iii) place and time of the statement; and (iv) why the statement was fraudulent.[307]

The Circuit Court reviewed the complaint and agreed with the district court's dismissal.[308] The plaintiffs asserted as the "actionable misstatement" that the defendants had represented in certain SEC filings that the tender offer at issue would be completed by a certain date.[309] Ultimately, the defendants were not able to complete the offer by the specified date.[310] The Fifth Circuit opined that the fact that the defendants were not able to complete the tender offer on time does not make the statement that it has an obligation to repurchase the relevant notes untrue or misleading.[311] Further, the Court reviewed the facts, or lack thereof, alleging the scienter of the defendants.[312] Fifth Circuit

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296. No. 04–10030, 2005 WL 469129 (5th Cir. (Tex.) Mar. 1, 2005).

297. *R2*, 2005 WL 469129 at *1.

298. *Id.*

299. *Id.*

300. *Id.*

301. *Id.*

302. *Id.*

303. *Id.* at *2.

304. *Id.* (citing *Tuchman v. DSC Communications Corp.*, 14 F.3d 1061, 1067 (5th Cir. 1994)).

305. *Id.*

306. *Id.*

307. *R2*, 2005 WL 469129 at *2 (citing *Southland Sec. Corp. v. Inspire Ins. Solutions, Inc.*, 365 F.3d 353 (5th Cir. 2004)).

308. *Id.* at *3.

309. *Id.*

310. *Id.*

311. *Id.*

312. *Id.* at *4.

jurisprudence defines scienter as follows: "[A]n 'intent to deceive, manipulate, or defraud or that severe recklessness in which the danger of misleading buyers or sellers is either known to the defendant or is so obvious that the defendant must have been aware of it.' "[313] "Severe recklessness has been 'limited to those highly unreasonable omissions or misrepresentations that involve not merely simple or even inexcusable negligence, but an extreme departure from the standards of ordinary care.' "[314] The plaintiff must allege facts sufficient to raise a strong inference of scienter in relation to each defendant.[315] The Fifth Circuit determined that the plaintiff in the instant case failed to do so.[316] The Court ultimately held that the plaintiff failed to allege any actionable misstatements with respect to the defendants' SEC filings, and that considering all the facts alleged in the complaint, the plaintiff also failed to sufficiently allege scienter.[317] Thus, the judgment of the district court was affirmed.[318]

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313. *Id.* (quoting *Southland*, 365 F.3d at 366).

314. *Id.* (quoting *Broad v. Rockwell Int'l Corp.*, 642 F.2d 929, 961–62 (5th Cir. 1981)).

315. *Id.*

316. *R2*, 2005 WL 469129 at *4.

317. *Id.*

318. *Id.*