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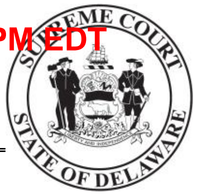

IN THE SUPREME COURT OF THE STATE OF DELAWARE

ASBESTOS WORKERS LOCAL 42 PENSION FUND, derivatively on behalf of Nominal Defendant JPMORGAN CHASE & CO., a Delaware corporation,

Plaintiff Below, Appellant,

v.

LINDA B. BAMMANN, *et al.*,

Defendants Below, Appellees,

and

JPMORGAN CHASE & CO.,

Nominal Defendant Below, Appellee.

No. 322, 2015
Court Below: Court of Chancery of the State of Delaware
(C.A. No 9772-VCG)

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NATURE OF PROCEEDINGS

This appeal arises out of a shareholder derivative action filed against various current and former directors and officers of JPMorgan Chase & Co. ("JPMorgan") related to the so-called "London Whale" trading losses suffered in 2012 by JPMorgan's Chief Investment Office ("CIO"). Plaintiff contends that the individual defendants breached their fiduciary duties to JPMorgan by failing to monitor risk in CIO and thereby prevent the trading losses. Plaintiff did not make a demand on JPMorgan's Board of Directors before filing suit, but rather contended that such a demand was futile because a majority of JPMorgan's directors face a substantial likelihood of personal liability based on their failure to monitor risk.

This was not the first shareholder derivative action filed in the wake of the London Whale losses that argued that demand on JPMorgan's Board was excused as futile. In 2012 and 2013, other JPMorgan shareholders filed similar actions in state and federal courts in New York, which eventually were consolidated in the U.S. District Court for the Southern District of New York and in New York Supreme Court. Plaintiffs in both consolidated actions asserted the same claims against the same current and former directors and officers of JPMorgan based on the same factual allegations. Plaintiffs in both actions also contended that demand was excused as futile because a majority of JPMorgan's directors supposedly face a substantial likelihood of personal liability based on their alleged failure to oversee and prevent a single portfolio in a single business unit from engaging in risky trading that ultimately resulted in large losses.

Defendants moved to dismiss both New York actions for failure adequately to plead demand futility under Rule 23.1. The New York courts granted those motions, both holding that the plaintiffs failed to allege particularized facts demonstrating that a majority of JPMorgan's directors consciously and in bad faith disregarded clear and prominent red flags warning of facially improper risk taking in the single CIO portfolio that suffered the losses, and thus had not sufficiently pled that demand was futile. *In re JPMorgan Chase & Co. Derivative Litig.*, 2014 WL 1297824, at *5 (S.D.N.Y. Mar. 31, 2014), *reconsideration denied*, 2014 WL 3778181 (S.D.N.Y. July 30, 2014); *Wandel* v. *Dimon*, Hr'g Tr. at 55-58, Index No. 651830/12 (N.Y. Sup. Ct. Jan. 15, 2014) (B127-30).

Defendants subsequently moved to dismiss this action, contending that Plaintiff was collaterally estopped under applicable New York law from litigating for the third time the same threshold demand-futility issue and, in any event, failed adequately to plead demand futility under Chancery Court Rule 23.1. Indeed, as Defendants pointed out in their reply brief (B592, 599), while that motion was pending, a different JPMorgan shareholder filed yet another, entirely duplicative shareholder derivative action based on the same CIO losses—further underscoring the importance of collateral estoppel and why it should apply here. *Morrison* v. *Bamman*, C.A. No. 10356-VCG (Del. Ch. filed Nov. 14, 2014).

The Court of Chancery granted Defendants' motion on collateral estoppel grounds. The court rejected Plaintiff's argument that collateral estoppel should not apply because it purportedly had alleged additional facts not alleged by the shareholders in the New York actions, explaining that collateral estoppel turns on

"the underlying conduct . . . not whether the Complaint raises new additional facts, or a more compelling characterization of those facts." (Ex. A to Pl.'s Br. at 43 (hereinafter, "Op. at __").) If simply pleading additional facts regarding the same underlying conduct were sufficient to avoid collateral estoppel, the court recognized, then "collateral estoppel would never apply and the plaintiff could litigate serially by endlessly alleging more factual support for the proposition he chooses to advance[, which is] clearly contrary to the efficiency and fairness principles underlying collateral estoppel." (*Id.*)

Plaintiff now appeals, arguing that collateral estoppel does not bar its complaint because it alleged more facts in support of its demand-futility argument than plaintiffs in the New York actions did. Plaintiff also contends that the Court of Chancery erred in holding that Plaintiff had waived any argument based on various agency settlements related to the London Whale losses by failing to raise that argument in opposing Defendants' motion to dismiss. Finally, Plaintiff asserts that this Court should conclude that demand was excused as futile. For the reasons explained below, this Court should reject all of these arguments and affirm the Court of Chancery's order.

SUMMARY OF ARGUMENT

1. Denied. The relevant question for purposes of collateral estoppel is whether the demand-futility issue in this case is substantially identical to that already decided in the New York actions. It unquestionably is, as Plaintiff's supposed "additional facts" do not materially change the central issue: whether a majority of JPMorgan's directors face a substantial likelihood of personal liability

for failing to monitor risk in the single CIO portfolio that suffered large trading losses. This Court's policy of encouraging shareholders to use Section 220 before filing derivative suits has no bearing on the application of collateral estoppel in this case. There is no "public policy exception" to the full faith and credit obligation to give force to other courts' judgments, and Plaintiff did not argue that the New York plaintiffs were inadequate representatives of JPMorgan. Nor could such an argument succeed in this case, given that (i) both of the New York complaints were based on voluminous documentary evidence (including, in the state-court action, books and records obtained under Section 220), and (ii) Plaintiff's demand-futility allegations are identical in all material respects to those in the New York actions, notwithstanding the additional documents Plaintiff obtained.

2. Denied. Delaware courts commonly enforce waiver when a plaintiff fails to include an argument in opposing a motion to dismiss. As those decisions recognize, raising an argument for the first time at oral argument deprives the defendant of a meaningful opportunity to respond. Plaintiff's appeal to a "lenient" motion to dismiss standard is both irrelevant to the waiver question and inapplicable in this demand-futility case under Rule 23.1.

3. Denied. Plaintiff has failed to plead sufficient particularized facts to become the first Delaware plaintiff ever to survive a motion to dismiss by alleging a substantial likelihood of personal liability based on a *Caremark* claim for failure to monitor business risk (if such a claim even exists).

STATEMENT OF FACTS

A. The Parties

Nominal Defendant JPMorgan is a financial services company incorporated in Delaware. (A032 ¶ 26.) Plaintiff Asbestos Workers Local 42 Pension Fund is a pension fund that purports to own JPMorgan stock. (A031 ¶ 25.) The director defendants are ten current and three former outside (or non-management) directors of JPMorgan. (A032-46 ¶¶ 27-31, 33-37; A050-51 ¶¶ 46-48.) James Dimon, JPMorgan's Chairman and CEO, is the only JPMorgan officer who also serves on the Board. (A038-39 ¶ 32.) The remaining defendants are two former JPMorgan Chief Financial Officers (Douglas Braunstein and Michael Cavanagh) and the former Chief Investment Officer (Ina Drew). (A046-48 ¶¶ 38-40.)

B. Plaintiff's Claims

JPMorgan takes in more deposits than it makes in loans, resulting in excess cash. Its CIO is principally responsible for managing the structural risk arising from this imbalance between loans and deposits, including investing excess cash to meet future liquidity needs and provide a reasonable return. (A090 ¶ 140.) One of the CIO's many investment portfolios was the Synthetic Credit Portfolio ("SCP"). Managed by a group of traders in London, the SCP was intended to function as a hedge against potential losses that JPMorgan might suffer elsewhere in its business operations. (A156-157 ¶¶ 248, 250-51.) As has been well publicized, trading in the SCP during the first part of 2012 ultimately resulted in losses of roughly $6.3 billion. (A020 ¶ 4; A183 ¶ 312.)

Plaintiff seeks to assert claims on behalf of JPMorgan against the individual defendants for breach of their fiduciary duties based on the SCP's trading losses. (A224-27 ¶¶ 372-86.) According to the complaint, JPMorgan's directors allowed "CIO to gamble bank assets in a large-scale speculative trading venture, employing complex synthetic credit derivatives investments, directly leading to" the 2012 losses. (A020 ¶ 4.) Plaintiff alleges that the directors ignored numerous "red flag[s]"—including an increase in the size of CIO's portfolios, an increase in CIO's revenue, and excessions of risk limits—that should have alerted them to deficiencies in CIO's risk controls and its risky trading. (A023 ¶ 9, A027 ¶ 15.)

C. The Board Review Committee

After the announcement of CIO's trading losses, JPMorgan's Board received demands from several different shareholders asking the Board to investigate CIO's losses and commence litigation against any responsible parties. (B65 ¶ 4.) Other shareholders proceeded to file suit alleging that demand on the JPMorgan Board should be excused as futile. In May 2012, the Board formed a Review Committee of three outside directors to examine the allegations raised in the shareholder demands and derivative complaints, conduct a review of CIO's losses, oversee the ongoing investigation of the losses by a JPMorgan management Task Force, and recommend to the Board what, if any, action should be taken. (B414; B65-66 ¶ 5; A190 ¶ 330.)

The Review Committee conducted an extensive, eight-month investigation of the shareholders' allegations. (B414.) In January 2013, the Review Committee released its report, which "concluded that the Board and the Risk Policy

Committee discharged their duties with respect to the oversight of the Firm and the CIO." (*Id.*; A190 ¶ 330.) The report nonetheless made numerous recommendations for "how the practices and processes of the Board and its committees could be enhanced to strengthen the Firm's overall risk management function and the oversight of that function." (B423.)[1] The Review Committee ultimately recommended that no litigation be brought by JPMorgan based on the allegations raised in the shareholder demands, and that JPMorgan seek dismissal of all pending shareholder derivative actions. (B430-31.) The Board accepted these recommendations. (*Id.*)

D. The Consolidated Federal Derivative Action

In May 2012, one JPMorgan shareholder filed a derivative action in the U.S. District Court for the Southern District of New York raising—like Plaintiff here—claims of breach of fiduciary duty against JPMorgan's directors and officers based on CIO's 2012 losses. *Baker* v. *Dimon*, No. 12-3878 (S.D.N.Y. May 15, 2012). A different JPMorgan shareholder later filed a second derivative action in the same court asserting similar claims, and the two actions were consolidated before Judge George B. Daniels. *In re JPMorgan*, Dkt. No. 20, No. 12-3878 (S.D.N.Y. Oct. 18, 2012).[2]

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[1] The JPMorgan management Task Force also issued a report addressing the causes of CIO's 2012 losses and the "comprehensive remedial measures the Firm has undertaken" or planned to undertake in response to those losses. (B444; *see also* B549-62.)

[2] Judge Daniels also is (or was) responsible for three other shareholder actions arising out of CIO's 2012 losses: (i) a class action asserting claims under the federal securities laws, *In re JPMorgan Chase & Co. Sec. Litig.*, 2014 WL 1297446 (S.D.N.Y. Mar. 31, 2014) (granting in part and denying in part motion to dismiss); (ii) a class action asserting claims under ERISA, *In re JPMorgan Chase & Co. ERISA Litig.*, 2014 WL 1296882 (S.D.N.Y. Mar. 31, 2014)

In the consolidated amended complaint, filed in April 2013, plaintiff made substantially the same allegations that Plaintiff makes here. The consolidated complaint alleged that "CIO has actually been operating as a high-risk proprietary trading desk since at least 2006 when it started trading in synthetic credit derivatives." (B138 ¶ 2.) By 2011, the federal plaintiff alleged, "CIO had become massively risky and out of control . . . and the fault lay squarely with JPMorgan's Board." (B139 ¶ 4.) The federal plaintiff further asserted that JPMorgan's directors (i) "approv[ed] and/or condon[ed] the CIO's change in purpose from Company-wide risk mitigation to a highly risky proprietary trading desk," (ii) "chose not to implement new risk management efforts related to these new risks," and (iii) "fail[ed] to respond to numerous obvious indications that the SCP was becoming drastically riskier." (B140 ¶ 9; B246 ¶ 305.)

The federal court granted defendants' motion to dismiss under Federal Rule 23.1,[3] holding that plaintiff failed adequately to allege that demand was futile. *In re JPMorgan*, 2014 WL 1297824, at *4-7. In particular, the court held that plaintiff "has not adequately pled sufficient facts to support its assertion that the

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(dismissed for failure to state a claim), *vacated and remanded*, Dkt. No. 71, No. 14-1514 (2d Cir. Nov. 25, 2014); and (iii) a derivative action brought by a shareholder who made a pre-suit demand on the Board and contended that the demand was wrongfully refused, *Espinoza* v. *Dimon*, 2014 WL 1303507 (S.D.N.Y. Mar. 31, 2014) (dismissed for failure adequately to plead wrongful refusal). On appeal in the *Espinoza* case, the U.S. Court of Appeals for the Second Circuit certified to this Court a question of Delaware law regarding the scope of a Board's obligation to investigate in response to a shareholder demand. *Espinoza* v. *Dimon*, 2015 WL 4747068 (2d Cir. Aug. 12, 2015).

[3] "Court of Chancery Rule 23.1 is either identical to or consistent with the principles behind Fed. R. Civ. P. 23.1." *Levner* v. *Saud*, 903 F. Supp. 452, 456 n.4 (S.D.N.Y. 1994) (citing *Allison* v. *Gen. Motors Corp.*, 604 F. Supp. 1106, 1117 (D. Del. 1985)).

Board consciously disregarded red flags regarding risk in CIO." *Id.* at *5. Plaintiff's motion for reconsideration was denied, *In re JPMorgan Chase & Co. Deriv. Litig.*, 2014 WL 3778181, at *1, and its appeal is pending. *See Wayne Cnty. Emps.' Ret. Sys.* v. *Dimon*, No. 14-3245-cv (2d Cir.).

E. The Consolidated *Wandel* Action

In May 2012, a different JPMorgan shareholder filed a derivative action in New York Supreme Court, also asserting breach of fiduciary duty claims based on CIO's 2012 losses. In April and May 2013, other shareholders filed identical derivative actions in that same court, including two that had obtained JPMorgan books and records under Section 220, making substantially the same allegations and asserting virtually identical claims. These actions ultimately were consolidated before Justice Jeffrey K. Oing in the Commercial Division of the New York Supreme Court. *Wandel* v. *Dimon*, Dkt. No. 35, Index No. 651830/12 (N.Y. Sup. Ct. May 22, 2013).

In their consolidated complaint, filed in June 2013, plaintiffs argued that CIO's 2012 losses were "the direct consequence of Defendants' failures to properly implement appropriate internal controls, oversight and risk management." (B292-93 ¶ 8.) According to the complaint, the Board "ignored numerous . . . red flags," including letters from a shareholder advocacy group, "warnings from regulators," and "risk level breaches." (B293 ¶ 10.) Plaintiffs further alleged that defendants "systematically concealed" from shareholders and regulators the transformation of CIO from an office charged with "reduc[ing] risk for the Firm, into a poorly supervised proprietary trading operation." (B290 ¶¶ 1-2.)

The New York state court also granted defendants' motion to dismiss under Rule 23.1 for failure adequately to allege that demand was futile. *Wandel*, 1/15/14 Hr'g Tr. at 58 (B130). As relevant here, the court held that the plaintiffs had failed to plead that the directors faced a substantial likelihood of liability on any of the claims asserted and thus could not impartially consider a demand. The court concluded:

> [T]he allegations are quite extensive, but at the end of the day my determination is that I don't find that there is a reasonable belief for me to arrive at the conclusion that . . . the majority of the board members here were [not] disinterested and could not exercise their independent business judgment decisions with respect to a demand.

Id. at 57 (B129). Plaintiffs' appeal of that decision is pending. *See Wandel* v. *Dimon*, Index No. 651830/12 (N.Y. App. Div., 1st Dep't).

F. The Dismissal of This Action

Like plaintiffs in the two consolidated New York actions, Plaintiff here did not make a demand on the Board, but rather argued that demand should be excused as futile. (A198 ¶ 349.) The complaint here likewise asserts that the directors are not disinterested because they face a substantial likelihood of personal liability for their purported failure to monitor risk in CIO. (A199 ¶¶ 350-51.)[4] Defendants moved to dismiss the complaint on two alternative grounds. First, in light of the dismissals of the New York actions, Defendants argued that collateral estoppel

[4] Plaintiff abandoned below all other arguments raised in its complaint for why demand supposedly was futile (Op. at 40 n.136), and makes no attempt to re-assert those grounds in this Court.

precludes Plaintiff from relitigating yet again in this case the same demand-futility issue already decided by the New York courts. (B26-36.) Second, Defendants alternatively contended that Plaintiff had failed sufficiently to plead demand futility under Rule 23.1. (B37-62.)

The Court of Chancery granted Defendants' motion on collateral estoppel grounds. Because it is "well-settled that collateral estoppel may be applied in the shareholder derivative context," the court recognized that the New York judgments could operate to preclude Plaintiff from relitigating the threshold demand-futility issue. (Op. at 39 (quoting *Carroll* v. *McKinnell*, 2008 WL 731834, at *2 (N.Y. Sup. Ct. Mar. 17, 2008).) The court stated that Plaintiff had not argued that it (through the New York plaintiffs) lacked an opportunity to fully and fairly litigate the demand-futility issue or that the New York plaintiffs were inadequate representatives of JPMorgan shareholders. (Op. at 40 & n.135.)

As a result, the only remaining question was whether "the identical issue was necessarily decided" in the two New York actions. The court rejected Plaintiff's argument that the issues were not identical simply because the "controlling facts" alleged by Plaintiff were different from those at issue in the prior actions. (Op. at 40-41.) Because the "underlying conduct that gives rise to the Plaintiff's claims is the same at issue in the New York Actions," the court explained, the issues were identical for purposes of collateral estoppel under New York law. (*Id*. at 42-43.) And even if Plaintiff theoretically *could* avoid preclusion simply by alleging more or different facts, the court concluded that the additional

facts alleged by Plaintiff here were "merely cumulative to the factual situations alleged in the prior actions." (*Id*. at 44.)

The court declined to consider Plaintiff's contention, made for the first time at oral argument, that collateral estoppel should not apply because Plaintiff filed its complaint after the release of agency settlements concerning JPMorgan's liability for the London Whale losses. (Op. at 47.) Although Plaintiff mentioned those settlements in the background section of its opposition to Defendants' motion, Plaintiff did not argue that those settlements rendered the demand-futility issue here different from the issue already decided in the New York actions. Because Defendants "had no meaningful opportunity to respond to such an argument," the court held that Plaintiff waived any reliance on those settlements. (*Id*. at 48 (citing *Emerald P'rs* v. *Berlin*, 2003 WL 21003437, at *43 (Del. Ch. Apr. 28, 2003), *aff'd*, 840 A.2d 641 (Del. 2003) (TABLE).) The Court did not address the merits of Plaintiff's demand-futility argument. (*Id.*)

ARGUMENT

I. THE COURT OF CHANCERY CORRECTLY HELD THAT COLLATERAL ESTOPPEL BARS PLAINTIFF FROM RELITIGATING THE ISSUE OF DEMAND FUTILITY.

A. Question Presented

Did the Court of Chancery correctly conclude that Plaintiff is collaterally estopped from litigating for the third time in this action whether demand on the Board should be excused because a majority of JPMorgan's directors supposedly face a substantial likelihood of personal liability on a *Caremark* claim for failure to monitor risk in CIO?

B. Scope of Review

This Court's review of a dismissal under Rule 23.1 is *de novo* and plenary. *Brehm* v. *Eisner*, 746 A.2d 244, 253 (Del. 2000).

C. Merits of the Argument

Delaware courts are obligated to accord a judgment entered by another state or federal court of competent jurisdiction the same force and effect as would another court in the state in which the rendering court sits. *Iowa-Wisconsin Bridge Co.* v. *Phoenix Fin. Corp.*, 25 A.2d 383, 391 (Del. 1942). This requirement, "recognized by all civilized nations as a rule of expediency, justice and public policy which demands that there be an end of litigation," *id.*, originates from the U.S. Constitution's Full Faith and Credit Clause and 28 U.S.C. § 1738. *Pyott* v. *La. Mun. Emps.' Ret. Sys.*, 74 A.3d 612, 615 (Del. 2013). It encompasses the doctrines of both res judicata and collateral estoppel. *Id.* (citing *San Remo Hotel, L.P.* v. *City & Cnty. of San Francisco*, 545 U.S. 323, 336 (2005)).

Two New York courts already have held that demand on JPMorgan's Board to bring suit based on CIO's 2012 losses was not futile. *In re JPMorgan*, 2014 WL 1297824, at *2-7; *Wandel*, 1/15/14 Hr'g Tr. at 55-58 (B127-30). As this Court must give those judgments "the same force and effect that [they] would be given" in New York, New York collateral estoppel law applies. *Pyott*, 74 A.3d at 616.

Under New York law, collateral estoppel applies if two elements are met.[5] First, "the party seeking the benefit of collateral estoppel must prove that the identical issue was necessarily decided in the prior action and is decisive in the present action. Second, the party to be precluded from relitigating an issue must have had a full and fair opportunity to contest the prior determination," and the burden is on that party to establish the absence of such opportunity. *D'Arata* v. *N.Y. Cent. Mut. Fire Ins. Co.*, 564 N.E.2d 634, 636 (N.Y. 1990). If these elements are met, collateral estoppel "bars not only parties from a previous action from litigating an issue decided therein, but those in privity with them as well." *Gramatan Home Inv'rs Corp.* v. *Lopez*, 386 N.E.2d 1328, 1332 (N.Y. 1979).

It is well established under New York law that "where one shareholder derivative action is dismissed for failure to adequately plead that the corporation's board of directors is disqualified from considering whether to initiate litigation, all other shareholders of that corporation are precluded from relitigating that issue." *Carroll*, 2008 WL 731834, at *2; *see also Parkoff* v. *Gen. Tel. & Elecs.*, 425

[5] As the Court of Chancery found, as relevant to this case, the federal law of collateral estoppel is effectively identical to New York law. (Op. at 38 n.129 (citing *Carroll*, 2008 WL 731834, at *2)); *accord Marvel Characters, Inc.* v. *Simon*, 310 F.3d 280, 286 (2d Cir. 2002). Plaintiff does not dispute this.

N.E.2d 820, 824 (N.Y. 1981) ("Because the claim asserted in a stockholder's derivative action is a claim belonging to and on behalf of the corporation, a judgment rendered in such an action . . . will generally be effective to preclude other actions predicated on the same wrong brought by other shareholders."). Plaintiff identified no contrary New York authority before the Court of Chancery (Op. at 39), and does not contest this point in this Court (*see* Pl.'s Br. at 17-23).

Nor does Plaintiff contend that it (through the other shareholder plaintiffs with which it is in privity) lacked a full and fair opportunity to contest the demand-futility issue in the New York actions. (*See* Pl.'s Br. at 17-23; *see also* Op. at 39-40.) Because Plaintiff bears the burden to establish the absence of a full and fair opportunity to litigate, *D'Arata*, 564 N.E.2d at 636, Plaintiff concedes this issue by its silence in this Court. Supr. Ct. R. 14(b)(vi)(A)(3). As a result, the only disputed issue before this Court regarding collateral estoppel is whether the identical demand-futility issue already was decided by the New York courts. Plaintiff argues that the issue in this case is not "identical" because Plaintiff "alleged new facts" here derived from the documents it obtained through its Section 220 request. (Pl.'s Br. at 19.) Plaintiff also claims that applying collateral estoppel here would contravene Delaware courts' "longstanding admonishments . . . that plaintiffs make full use of § 220." (*Id*. at 23.) Neither argument has merit.

1. The New York Courts Already Have Decided the Identical Demand-Futility Issue Presented Here.

As the Court of Chancery correctly recognized, Plaintiff's demand-futility argument in this case raises the "precise question" that was at issue in the two New

York actions: "whether a majority of the Company's directors face a substantial likelihood of personal liability for failure to oversee risk undertaken by CIO." (Op. at 40-41.) Like the New York plaintiffs, Plaintiff seeks to advance a *Caremark* claim for "failure to monitor *business risk* under Delaware law," which requires particularized allegations that the directors "*consciously* disregarded red flags signaling that the company's employees were taking facially improper, and not just ex-post-ill-advised or even bone-headed business risks." (*Id*. at 34-36 (quoting *In re Goldman Sachs Grp., Inc. S'holder Litig.*, 2011 WL 4826104, at *22 n.217 (Del. Ch. Oct. 12, 2011).) The two New York courts framed the issue the same way. *See In re JPMorgan*, 2014 WL 1297824, at *4 ("Plaintiff's claim implicates the *Caremark* theory of liability" and "is premised on an alleged failure to monitor business risks [in CIO]."); *Wandel*, 1/15/14 Hr'g Tr. at 30-38, 56 (B102-10, B128) (finding no "conscious decision not to act in the face of red flags").

In support of its *Caremark* theory, Plaintiff here advances virtually the same allegations, drawn from substantially the same sources, as the New York plaintiffs. All three complaints allege that CIO historically was a "conservative, low-risk business unit" that was "transformed" into a risky "short-term proprietary trading center," eventually "leading to at least $6.3 billion in losses by mid-2012." (A019-21 ¶¶ 4-5; *see* B163 ¶ 71 ("CIO had been converted into a proprietary trading desk that sought risky, short-term profits."); B316 ¶ 84 (CIO was "aggressively transformed . . . into a high-risk, proprietary trading desk").) All three complaints also contend that JPMorgan's directors "failed to ensure that [CIO's] risk management and procedures" were adequate in light of CIO's alleged

transformation and supposed red flags warning of increasing risk. (A020 ¶ 4; *see* B140 ¶ 10 ("Despite knowing about the CIO's risks . . . the Board chose not to change its risk management efforts related to the CIO's proprietary trading."); B292 ¶ 8 (CIO's 2012 losses "are the direct consequence of Defendants' failures to properly implement appropriate internal controls, oversight and risk management.").) Also like the New York plaintiffs, Plaintiff here relies heavily on the March 2013 report of the U.S. Senate Permanent Subcommittee on Investigations ("PSI Report").[6] And the *Wandel* complaint in New York state court, like Plaintiff's complaint here, contains extensive quotations from JPMorgan books and records obtained via Section 220.[7] Many of those quotations are identical. (*Compare* B391 ¶ 317, *with* A205 ¶ 357, bullet 3.)

Because Plaintiff's complaint relies on the same sources in support of the same underlying allegations, Plaintiff makes the exact same demand-futility arguments that the New York plaintiffs made.

- *New York Federal Action*: Demand should be excused because the directors supposedly face a substantial likelihood of personal liability for failure to oversee CIO's "risk management, supervision, and control infrastructures," including by "approving and/or condoning the CIO's change in purpose from Company-wide risk mitigation to a highly risky proprietary trading desk focused on short-term profits." (B244-45 ¶¶ 299, 305.)
- *New York State-Court Action*: Demand should be excused because the directors supposedly face a substantial likelihood of personal liability for failure to "properly monitor and oversee the Company's internal controls

[6] (A017 p. 1, A030 ¶ 21; *see* B165-66, 169, 181 ¶¶ 80, 92, 125; B290, 293-94, 306-07, 315, 320, 321 p.1, ¶¶ 12, 54-55, 79, 96, 99.)

[7] (*E.g.*, B391-92, 395, 397 ¶¶ 317-23, 330-31, 335-37; *see* A100-08, 202-16 ¶¶ 162-71, 357.)

and risk exposure" (B295 ¶ 17) and for approving, concealing or disguising the wrongs alleged in the complaint (B369 ¶ 258), including that CIO purportedly was "aggressively transformed into a high-risk, proprietary trading desk." (B290, 316 ¶¶ 1, 84.)

- *Here*: Demand should be excused because the directors supposedly face a substantial likelihood of personal liability for failure "to ensure that the risk management procedures designed and implemented for the CIO were consistent with that business unit's corporate strategy and risk appetite," and for failure to act when they "should have known that the change in the CIO's purpose and strategy was a sign that they had a duty to act through their risk oversight role." (A199 ¶¶ 350, 352.)

After considering the same allegations that Plaintiff advances here, both New York courts rejected plaintiffs' demand-futility arguments.[8] As Judge Daniels held in the federal action, "[p]laintiff's allegations do not come close to pleading a 'sustained or systemic failure' of oversight by the Board required to state a *Caremark* claim." *In re JPMorgan*, 2014 WL 1297824, at *5 n.6. And as Justice Oing determined in the state-court action, notwithstanding the "supposed red flags" alleged by plaintiffs, "the substantial likelihood of [the directors] being personally liable in the face of the exculpatory c[l]ause within the Delaware statute, that's also suspect too." *Wandel*, 1/15/14 Hr'g Tr. at 56 (B128).

2. Plaintiff's "Additional Facts" Do Not Make the Issue in This Case and the New York Actions Different.

Plaintiff argues that the issues are not identical because documents it obtained through Section 220 supposedly "provide evidence that various

[8] The New York courts also rejected some of the same demand-futility arguments that Plaintiff has abandoned in this case, including arguments based on director compensation and benefits, issuance of false statements in JPMorgan's securities filings, and approval of compensation policies for CIO traders that encouraged risk taking. *In re JPMorgan*, 2014 WL 1297824, at *7-8; *Wandel*, 1/15/14 Hr'g Tr. at 56 (B128).

Defendants were on notice, well earlier than the New York Actions alleged, of *specific* information at *specific* times, and, in the face of this specific information, they deliberately failed to act to establish necessary controls." (Pl.'s Br. at 22.) Plaintiff contends that it alone alleged that "as early as 2009, the JPMorgan Board and its committees were informed that the CIO was engaged in highly risky proprietary trading activity, yet took no action to ensure that the protocols employed by the CIO were commensurate with the increased risk." (*Id*. at 20-21.)

As the Court of Chancery correctly held, Plaintiff's argument "misapprehends the standard." (Op. at 40-43.) Under New York law, "[t]he identity element of collateral estoppel does not require the issues to be exactly identical," only "substantially or essentially the same." 9 CARMODY-WAIT 2D, NEW YORK PRACTICE § 63:472; *see also Thomas* v. *Venditto*, 925 F. Supp. 2d 352, 361 (E.D.N.Y. 2013) (identity element is satisfied if issues are "substantially the same"); Restatement (Second) of Judgments § 27, cmt. c (1982) (collateral estoppel "prevent[s] repetitious litigation of what is essentially the same dispute" even where "there is a lack of total identity").[9] As a result, simply alleging additional facts in support of the same theory of liability does not render the "issue" different for collateral-estoppel purposes. Such additional allegations raise a distinct issue only if they relate to different underlying conduct that allegedly creates liability. *See*, *e.g.*, *Brautigam* v. *Blankfein*, 8 F. Supp. 3d 395, 401

[9] New York courts rely on the Restatement when applying the doctrines of collateral estoppel and res judicata. *See*, *e.g.*, *Ryan* v. *N.Y. Tel. Co.*, 467 N.E.2d 487, 490 (N.Y. 1984).

(S.D.N.Y. 2014) (finding "factually distinct circumstances which affected the analysis regarding whether demand was excused" because "transactions at issue are not the same"). Indeed, if the law were otherwise, shareholders could endlessly relitigate the demand-futility issue simply by including a few more facts in each iteration of the complaint—undermining the entire purpose of collateral estoppel of "reduc[ing] litigation and conserv[ing] the resources of the court and litigants." *See Kaufman* v. *Eli Lilly & Co.*, 482 N.E.2d 63, 67 (N.Y. 1985).

Courts have applied these principles to preclude relitigation of substantially the same issue in shareholder derivative actions. For example, a New Jersey federal court concluded that New York law barred a shareholder plaintiff from relitigating demand futility when the complaint contained "substantially similar allegations" to a prior state-court action in which the court held that demand futility had not been established. *In re Bed Bath & Beyond Inc. Deriv. Litig.*, 2007 WL 4165389, at *3 (D.N.J. Nov. 19, 2007). The court held that the inclusion of additional factual allegations, causes of action, and defendants in that second complaint did not necessarily "alter the central issue—whether demand on the . . . board would have been futile." *Id.* at *6. Similarly, applying Massachusetts law—which, like New York law, permits preclusion where "the issues overlap substantially"—the First Circuit held that a shareholder plaintiff was collaterally estopped from relitigating demand futility because there was "[n]othing in the Second Amended Complaint . . . that amount[ed] to a 'significant change' in the futility issue from what was presented to the [first] court." *In re Sonus Networks, Inc.*, 499 F.3d 47, 62 (1st Cir. 2007).

The two cases on which Plaintiff relies actually illustrate why the demand-futility issue here is no different from the issue in the New York actions. In *Asbestos Workers Philadelphia Pension Fund* v. *Bell*, 2014 WL 1272280 (N.Y. Sup. Ct. Mar. 28, 2014) (cited in Pl.'s Br. at 19-20), the court concluded that the issues before it were not identical to those in a prior action because the subsequent complaint included allegations regarding entirely different conduct—a grant of supposed "unfettered authority" to a board committee to securitize and sell problematic loans—than what was alleged in the prior action. *Id*. at *2. *Bell* thus stands not for the proposition that the addition of new "factual allegations" necessarily renders the issues in a subsequent action different, but rather for the commonsense notion that the issues are not substantially identical if those new factual allegations relate to different alleged conduct.

The U.S. Supreme Court's decision in *Commissioner* v. *Sunnen*, 333 U.S. 591 (1948) (cited in Pl.'s Br. at 21), is even further afield. *Sunnen* arose in the unique context of annual tax obligations, where "[e]ach year is the origin of a new liability and of a separate cause of action." *Id*. at 598. Because of that unique feature of tax litigation, the Supreme Court has expressly rejected the application of *Sunnen*'s collateral estoppel analysis outside the tax context. *United States* v. *Stauffer Chem. Co.*, 464 U.S. 165, 172 n.5 (1984). Plaintiff does not seek to raise a new claim, but rather seeks to relitigate the *same* claim that already has been rejected in the two New York actions.

Even if it were theoretically possible to raise a distinct issue simply by pleading additional facts about the same underlying conduct, Plaintiff's "additional

facts" are merely cumulative of the insufficient facts alleged in the New York actions. (Op. at 44.) Even Plaintiff acknowledges that it seeks to allege the same claims rejected in the New York actions based "on a more robust record and for time periods not covered in the New York Actions." (Pl.'s Br. at 13.) That does not raise a new or different demand-futility issue. Merely adding more of the same evidence in support of the same claims, even dating back to earlier years, does not change the central issue: those allegations still—like the facts pled in the New York actions—do not suggest that a majority of the Board had knowledge of red flags indicating facially improper risk taking in CIO.

For example, Plaintiff relies on various presentations in 2009 and 2010 to the Board's Audit Committee that advised of increases in CIO's "size, complexity, and range of product investment." (Pl.'s Br. at 14, 20-21.) To start, these presentations say nothing about facially improper risk taking in CIO. Moreover, plaintiffs in the New York state-court action also alleged that CIO's portfolios increased significantly in size during the financial crisis, that the Board was aware of that increase, and that the increase heightened the demands on risk management and controls in CIO.[10] In fact, the New York state-court complaint similarly identified the "relevant period" as January 1, 2009 to the present (B295 ¶ 17), and alleged the existence of red flags dating back to 2009 and 2010.[11]

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[10] (B318-19, 383, 385-86, 391, 395 ¶¶ 90-91, 287, 299, 317, 330.)

[11] (B321, 382-83, 393 ¶¶ 100, 285, 287, 324.)

In the end, all three categories of evidence Plaintiff contends (Pl.'s Br. at 18) are present in its complaint as a result of its additional books and records demands are no different from what the New York plaintiffs alleged as the basis for demand futility. (*See supra* at I.C.1.) Accordingly, even if simply pleading additional facts, without more, could raise a different issue, Plaintiff has not done so here.

3. Plaintiff Cannot Avoid Collateral Estoppel Merely Because It Obtained Additional Documents Under Section 220.

Plaintiff further argues that this Court should decline to apply collateral estoppel because "[c]reating an extra hurdle for a diligent derivative plaintiff to surmount is contrary to the longstanding admonitions of the Delaware courts that plaintiffs make full use of § 220." (Pl.'s Br. at 22-23.) In other words, Plaintiff asks this Court not to apply collateral estoppel whenever a shareholder plaintiff has obtained more documents under Section 220 than prior shareholder plaintiffs that failed to plead demand futility. This argument fails for multiple reasons.

As an initial matter, "there is 'no roving "public policy exception" to the full faith and credit due judgments'" that would allow Delaware courts to decline to give effect to other states' judgments in order to further Delaware's own policies. *Pyott*, 74 A.3d at 616 (quoting *Baker* v. *Gen. Motors Corp.*, 522 U.S. 222, 232-33 (1998)). New York law governs the collateral-estoppel issue here, and Plaintiff has pointed to no New York case suggesting an exception for plaintiffs who obtain additional corporate books and records before filing suit. Delaware's policy in favor of encouraging pre-suit Section 220 demands thus cannot overcome the

"'exacting'" obligation to give full effect and force to the New York judgments. *See id*. (quoting *Baker*, 522 U.S. at 233).

Moreover, contrary to Plaintiff's concerns about conflicting incentives (Pl.'s Br. at 23), creating an exception to collateral estoppel is not necessary to encourage shareholders to use Section 220 rather than file premature derivative suits. Shareholders still have every incentive to obtain books and records to increase the chances that they can surmount Rule 23.1's particularity requirements. *See*, *e.g.*, *White* v. *Panic*, 783 A.2d 543, 557 (Del. 2001) ("[F]urther pre-suit investigation in this case may have yielded the particularized facts required to show that demand is excused."). Such demands also may enable a later-filing plaintiff to be named lead plaintiff. *King* v. *Verifone Hldgs., Inc.*, 12 A.3d 1140, 1151 (Del. 2011).

This Court explained in *Pyott* that whether a prior plaintiff filed suit prematurely without first obtaining books and records under Section 220 may be relevant to the analysis of the adequacy of that plaintiff's representation of the corporation. 74 A.3d at 618.[12] But *Pyott* considered the question of adequacy of representation only *after* finding that the elements of collateral estoppel under California law had been met, not in determining whether collateral estoppel should apply in the first place. And while acknowledging that "[u]ndoubtedly there will be cases where a fast filing stockholder also is an inadequate representative," this

[12] "A person is not bound by a judgment for or against a party who purports to represent him if . . . [t]he representative failed to prosecute or defend the action with due diligence and reasonable prudence." Restatement (Second) of Judgments § 42(1) (1982) (quoted in *Pyott*, 74 A.3d at 618 n.21). The Restatement states that inadequate representation is not "failure of a representative . . . *to develop all possible resources of proof*," but representation "so grossly deficient as to be apparent to the opposing party." *Id.* § 42(1)(e), cmt. f (emphasis added).

Court declined to adopt a presumption of inadequacy of representation for "fast filers." *Id.* Here, Plaintiff has not argued that plaintiffs in the New York actions were inadequate corporate representatives. (Op. at 43 n.147.)

On appeal, Plaintiff repeatedly (and incorrectly) states that the New York plaintiffs all filed suit in 2012, in an apparent effort to depict them as prototypical fast filers. (*See*, *e.g.*, Pl.'s Br. at 1-2, 11.) That is both factually inaccurate and irrelevant. Three of the four initial state-court complaints and (more importantly) the consolidated complaints in both New York courts were filed in 2013—after the release of the PSI Report and Board Review Committee and management Task Force reports. Those reports contained extensive detail about the events leading to CIO's 2012 trading losses. And the New York state-court plaintiffs obtained thousands of pages of JPMorgan books and records under Section 220—hardly a "cursory" effort or mere "smattering of documents," as Plaintiff erroneously suggests (*id.* at 2). Given the amount of publicly available information about CIO's 2012 losses, the substantial body of documents relied on by plaintiffs in both prior actions, and the substantial similarity of the allegations in all three complaints, there can be no argument that the prior plaintiffs provided "grossly deficient" representation of JPMorgan. *See Pyott*, 74 A.3d at 618 (quoting *In re Sonus Networks*, 499 F.3d at 66 (in turn quoting Restatement (Second) of Judgments § 42(1)(e), cmt. f (1982))). In sum, Delaware's policy of encouraging shareholders to use Section 220 provides no valid basis to create an exception to collateral estoppel, either as a general matter or in this case.

II. PLAINTIFF WAIVED ANY ARGUMENT THAT THE AGENCY SETTLEMENTS PRECLUDE COLLATERAL ESTOPPEL, AND THAT ARGUMENT WOULD FAIL IN ANY EVENT.

A. Question Presented

Did the Court of Chancery err in concluding that Plaintiff waived any argument about the effect of the agency settlements on collateral estoppel by failing to make that argument in opposing Defendants' motion to dismiss?

B. Scope of Review

This Court's review of a dismissal under Rule 23.1 is *de novo* and plenary. *Brehm*, 746 A.2d at 253.

C. Merits of the Argument

1. The Court of Chancery Properly Found Waiver.

For the first time at oral argument on Defendants' motion to dismiss, Plaintiff's counsel argued that the demand-futility issue here is different from that in the New York actions because Plaintiff raised allegations regarding five regulatory agency settlements concerning CIO's 2012 losses. (A759-60.) Even though that was Plaintiff's lead argument at oral argument, Plaintiff's counsel admitted that Plaintiff did not make that argument in its opposition to Defendants' motion, much less as the "central distinction between the two New York cases and this case." (A761, A763.) The Court of Chancery thus held that Plaintiff waived that argument by depriving Defendants of any "meaningful opportunity to respond." (Op. at 47-48.) That decision was correct under "settled Delaware law." *See Emerald P'rs*, 2003 WL 21003437, at *43; *see also In re Mobilactive Media, LLC*, 2013 WL 297950, at *12 n.152 (Del. Ch. Jan. 25, 2013) ("[I]ssues adverted

to in a perfunctory manner, unaccompanied by some effort at developed argumentation, are deemed waived.") (internal quotation marks omitted).

On appeal, Plaintiff argues that waiver should not be applied at the motion-to-dismiss stage because "Delaware case law on the waiver of an argument for failure to raise it in a brief indicates that the brief referred to is either a post-trial brief or an appellate brief." (Pl.'s Br. at 28.) In fact, Delaware courts routinely apply waiver at the motion-to-dismiss stage, even with respect to an entire *claim* that was raised in the complaint but not in an opposition brief.[13] The distinction that Plaintiff attempts to draw also makes little sense. At whatever stage of the case, the purpose of the requirement that a party include legal arguments in its brief is "to put the opposing parties and the court on notice of the issues to be decided." *Martinez* v. *E.I. du Pont de Nemours & Co.*, 2012 WL 6845678, at *4 n.18 (Del. Super. Ct. Dec. 5, 2012) (internal quotation marks omitted). By failing to raise any argument based on the agency settlements until oral argument, Plaintiff deprived Defendants of a meaningful opportunity to respond.

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[13] *See, e.g.*, *Spring Real Estate, LLC* v. *Echo/RT Holdings, LLC*, 2013 WL 6916277, at *7 (Del. Ch. Dec. 31, 2013) ("[A] plaintiff may waive a claim if it does not brief the sufficiency of its allegations in response to a defendant's motion to dismiss. Spring Capital's single citation to an ostensibly governing statute, without an accompanying legal or factual argument about the allegations of the Complaint, is an inadequate response to Echo/RT's arguments."); *Tang Capital P'rs, LP* v. *Norton*, 2012 WL 3072347, at *7 & n.31 (Del. Ch. July 27, 2012) ("Plaintiffs' second public policy point . . . was raised for the first time at oral argument. . . . This delay constitutes a waiver."); *Forsythe* v. *ESC Fund Mgmt. Co. (U.S.)*, 2007 WL 2982247, at *11 (Del. Ch. Oct. 9, 2007) ("Finally, the defendants point out that the plaintiffs failed to brief their claims that the Investment Advisor and Special Limited Partner aided and abetted the General Partner's breach of its oversight duties. The plaintiffs have waived these claims by failing to brief them in their opposition to the motion to dismiss.").

Nor is Plaintiff correct that the applicable motion to dismiss standard requires the Court to grant an "inference" that Plaintiff adequately raised this argument merely by mentioning the agency settlements in the factual background sections of its 227-page complaint and of its brief in opposition. Plaintiff argues that it is entitled to "all reasonable inferences" under a "lenient motion to dismiss standard," relying on a case that arose under the "minimal . . . conceivability" standard of Court of Chancery Rule 12(b)(6). (Pl.'s Br. at 31 (citing *Cent. Mortg. Co.* v. *Morgan Stanley Mortg. Capital Hldgs. LLC*, 27 A.3d 531, 535-37 (Del. 2011).) But this case is governed by Rule 23.1, which is "more stringent than the standard" under Rule 12(b)(6), and Rule 23.1 imposes "strict requirements of factual particularity." *In re Citigroup Inc. S'holder Deriv. Litig.*, 964 A.2d 106, 120, 139 (Del. Ch. 2009).

Even more fundamentally, Plaintiff's argument is directed to the wrong issue. Under whatever pleading standard, the "inferences" a court will draw from a plaintiff's *complaint* pertain to the substance of its allegations—*i.e.*, whether the complaint states a claim—not to whether the plaintiff has preserved a legal argument in opposing a motion to dismiss. Plaintiff has pointed to no authority in the motion-to-dismiss context relaxing the well-established principle that a litigant waives an argument by failing to raise it in its brief. Accordingly, the Court of Chancery correctly concluded that Plaintiff waived any argument that the agency settlements distinguish the demand-futility issue in this case from the issue in the prior New York actions.

2. The Agency Settlements Would Not Defeat Collateral Estoppel In Any Event.

Even if this Court were to consider it, Plaintiff's argument based on the agency settlements fails to distinguish the demand-futility issue here from the issue already decided in the New York actions. Plaintiff identifies nothing in those settlements that implicates *the Board* in any way and thus would establish a substantial likelihood of personal liability on Plaintiff's *Caremark* claim. Indeed, the settlement with the Securities and Exchange Commission—on which Plaintiff principally relies and attaches as an exhibit to its brief—repeatedly states that "JPMorgan Senior Management did not adequately update the Audit Committee" about facts concerning risk taking in CIO. (Pl.'s Ex. B at 3 ¶ 7; *see also id.* at 17 ¶ 76 ("Nor, more broadly, did JPMorgan Senior Management disclose to the Audit Committee its concerns regarding the operation of [CIO's Valuation Control Group].").) The allegation that management failed to inform the Board of risk levels in CIO does nothing to support (and indeed cuts against) an allegation that the Board *consciously* disregarded red flags revealing facially improper risk taking.

Because Plaintiff has not pointed to anything in the agency settlements relevant to the directors' liability, those settlements do not distinguish the issue here from the issue in the prior New York actions.

III. PLAINTIFF FAILS ADEQUATELY TO ALLEGE THAT DEMAND WAS EXCUSED AS FUTILE.

A. Question Presented

Given Rule 23.1's particularity requirements and the clause in JPMorgan's charter exculpating its directors from money damages for breaches of their fiduciary duties to the "fullest extent" allowed by 8 *Del. C.* § 102(b)(7), has Plaintiff adequately pled (for the first time in any Delaware court) that demand was excused because a majority of JPMorgan's directors face a substantial likelihood of personal liability on a *Caremark* claim for failure to monitor risk in CIO?

B. Scope of Review

Because it dismissed the complaint on collateral estoppel grounds, the Court of Chancery did not reach the merits of Plaintiff's demand-futility argument. As a result, if this Court chooses to address the merits, it would necessarily decide the issue *de novo*.

C. Merits of the Argument

If not affirmed on the basis of collateral estoppel, the Court of Chancery's dismissal of the complaint still should be affirmed on the alternative ground that Plaintiff fails adequately to plead demand futility.[14] Abandoning the complaint's other theories of demand futility, in opposing Defendants' motion to dismiss, Plaintiff relied solely on its contention that a majority of the Board faces a

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[14] *See Cent. Laborers Pension Fund* v. *News Corp.*, 45 A.3d 139, 141 (Del. 2012) ("[T]his Court may rest its appellate decision on any issue that was fairly presented to the Court of Chancery, even if that issue was not addressed by that court.").

substantial likelihood of personal liability for failing to monitor risk in CIO. (*See* A279-308; *see also* Op. at 34-36, 40 & n.136.)

No Delaware court ever has sustained a *Caremark* claim based on directors' alleged failure to monitor business risk in a particular business unit. In fact, one court referred to such a claim as a mere "theoretical possibility." *In re Goldman Sachs*, 2011 WL 4826104, at *22 n.217. As the Court of Chancery recognized (Op. at 35), "[b]usiness risk is the very stuff of which corporate decisions are constituted," making it "difficult to see how successful maintenance of" a *Caremark* claim based on failure to monitor business risk "can be consistent with this jurisdiction's model of corporate governance." *See also In re Citigroup*, 964 A.2d at 126, 131 (recognizing that financial institutions are "in the business of . . . managing investment and other business risks," and that how they "evaluate the trade-off between risk and return" is "[t]he essence of . . . business judgment.").

If such a *Caremark* claim even exists, a plaintiff must allege that the directors "'*consciously* failed to implement any sort of risk monitoring system or, having implemented such a system, *consciously* disregarded red flags signaling that the company's employees were taking facially improper, and not just ex-post ill-advised or even bone-headed, business risks.'" (Op. at 36 (quoting *In re Goldman Sachs*, 2011 WL 4826104, at *22 n.217).) Plaintiff here failed to carry this "weighty" burden of pleading that a majority of JPMorgan's directors face a substantial likelihood of personal liability on that basis. (B43-56 (internal quotation marks omitted); B609-23.)

Plaintiff's sole argument on this issue—and the only argument properly presented to this Court, *see* Supr. Ct. Rule 14(b)(vi)(A)(3)—is that demand should be excused as futile here for the same reasons it was excused in *In re American International Group, Inc.* (*AIG*), 965 A.2d 763 (Del. Ch. 2009), *aff'd sub nom. Teachers' Ret. Sys. of La.* v. *PricewaterhouseCoopers LLP*, 11 A.3d 228 (Del. 2011). But *AIG* was a very different case. The *AIG* complaint "fairly support[ed] the assertion that AIG's Inner Circle led a—and [the court] use[d] this term with knowledge of its strength—criminal organization. The diversity, pervasiveness, and materiality of the alleged financial wrongdoing at AIG is extraordinary." 965 A.2d at 799. In stark contrast to the allegations here, the *AIG* plaintiffs alleged that AIG as an organization "embarked on widespread illegal misconduct at the direction and under the control" of its CEO and Chairman of the Board. *Id*. at 774. No such pervasive or illegal conduct is alleged here; Plaintiff instead seeks to hold JPMorgan's directors personally liable for failing to prevent a single portfolio managed by a small group of traders in a single business unit in London from incurring trading losses. Thus, whatever *AIG* held about the potential liability of AIG's "Inner Circle" that allegedly operated AIG as a "criminal organization" has no bearing on the facts alleged here.

The legal analysis in *AIG* also is irrelevant to the demand-futility issue in this case. First, *AIG* concerned a *Caremark* claim based on an alleged failure to monitor pervasive fraudulent schemes at the highest level of management that resembled a "criminal organization," not a failure to monitor *business risk* in a single business unit. Second, the *AIG* court considered that *Caremark* claim not

under the "particularized pleading requirement of Rule 23.1," which is applicable here, but under the "plaintiff-friendly Rule 12(b)(6) standard." *AIG*, 965 A.2d at 810-11. The court held that demand was excused because a special litigation committee, acting with the full delegation of the Board's authority to address shareholder demands, decided to take no position on the plaintiffs' claims, equating to a decision to let those claims proceed. *Id*. at 809-10. As a result, the Rule 12(b)(6) standard governed the plaintiffs' *Caremark* claim, and that is the only reason the court "grant[ed] the Stockholder Plaintiffs the benefit of all reasonable inferences" in that case. *Id*. at 782 (quoted in Pl.'s Br. at 33).

By contrast, the issue here is whether demand should be excused as futile because a majority of JPMorgan's directors allegedly face a substantial likelihood of personal liability based on their supposed failure to monitor business risk. Plaintiff therefore must satisfy the heightened particularized pleading requirement of Rule 23.1, not the more lenient standard of Rule 12(b)(6). That is a critical difference. Plaintiff seeks to allege a substantial likelihood of liability in a case governed by Rule 23.1 based on trading losses incurred in a single portfolio in a single business unit during a part of 2012. *AIG*, a case governed by Rule 12(b)(6) based on allegations that upper management led a "criminal organization," provides no support for Plaintiff's demand-futility argument here. *See id*. at 799 (suggesting that a different outcome might have resulted in a case under Rule 23.1 without the "extraordinary" allegations of the "diversity, pervasiveness, and materiality of the alleged financial wrongdoing at AIG").

To the extent Plaintiff contends that the agency settlements alone are "sufficient grounds" to show demand futility based on a substantial likelihood of personal director liability (Pl.'s Br. at 32, 33), that is flatly inconsistent with well-established Delaware law. As this Court recognized in *Stone* v. *Ritter*, 911 A.2d 362, 366, 373 (Del. 2006), a "bad outcome" does not equal "bad faith," and "directors' good faith exercise of oversight responsibility may not invariably prevent employees from violating criminal laws, or from causing the corporation to incur significant financial liability." Indeed, the *Stone* Court affirmed the dismissal of *Caremark* claims under Rule 23.1 notwithstanding allegations that the corporation entered into settlements with the U.S. Attorney, the Federal Reserve, FinCEN, and the Alabama Banking Department. *Id.* at 373. Plaintiff must show much more than the mere fact of agency settlements to establish demand futility, and it has failed to do so.

In the end, although Plaintiff makes virtually no effort to support the merits of its *Caremark* claim in this Court, Plaintiff has come nowhere close to pleading the particularized facts required by Rule 23.1 demonstrating that a majority of JPMorgan's directors consciously and in bad faith disregarded red flags warning of facially improper risk in CIO. As in the New York actions, many of Plaintiff's supposed red flags were contained in presentations to particular Board committees comprised of less than a majority of directors,[15] but Delaware law does not permit

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[15] (*See, e.g.*, A203 ¶ 357, bullet 1 (March 2009 presentation to Audit Committee); A205 ¶ 357 (September 2010 presentation to Risk Policy Committee).)

the wholesale imputation of such knowledge to the full Board. *Desimone* v. *Barrows*, 924 A.2d 908, 943 (Del. Ch. 2007). In any event, as Defendants explained in their motion to dismiss briefing (B50-56; B618-22), Plaintiff's alleged red flags generally relate to increases in the size and complexity of trading in CIO or to occasional excessions of or temporary increases in CIO or firm-wide risk limits. None of those allegations at all suggest that CIO traders in London or elsewhere were taking *facially improper* risks, or that any JPMorgan director consciously disregarded reports of such risk taking. Absent particularized facts suggesting that JPMorgan's directors had knowledge of and consciously disregarded facially improper risk taking (and assuming such a claim exists), Plaintiff has failed to plead a substantial likelihood of personal liability on a *Caremark* claim for failure to monitor business risk.

CONCLUSION

The Court of Chancery correctly applied New York law of collateral estoppel to preclude Plaintiff from relitigating whether demand should be excused because a majority of JPMorgan's directors allegedly face a substantial likelihood of liability on a *Caremark* claim for failing to monitor risk in CIO. In the alternative, this Court should affirm the dismissal of this action on the ground that Plaintiff failed adequately to plead demand futility.

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