
SFMS Securities Law Bulletin

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**Inside this issue:**




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# The Supreme Court's Upcoming Clarification On The Reach of Secondary Actor Liability Under the Federal Securities Laws

***By Natalie Finkelman Bennett, Esquire and Patrick A. Klingman, Esquire***

This December, the Supreme Court is scheduled to again hear argument on the reach of so-called "secondary" liability under the federal securities laws, which it last looked at in *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148 (2008). The specific issue this time is whether Janus Capital Management, a mutual fund advisory firm that effectively runs the Janus family of funds, and/or its publicly-traded corporate parent (collectively, "Janus"), can be held liable for false and misleading statements regarding "market timing" contained in the prospectuses of Janus' mutual funds.

For the past 16 years, since *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994), was issued, there has been no aiding and abetting liability for securities fraud -- a defendant cannot be liable under Section 10(b) of the Securities Exchange Act of 1934 or SEC Rule 10b-5, absent a "showing that the plaintiff relied upon the [defendant's] statements or actions." *Id.*, 511 U.S. at 180. Nevertheless, the *Central Bank* Court cautioned that "[t]he absence

*(Continued on page 10)*

# Department of Labor Will Require Service Providers To Make Mandatory Fee Disclosures By July 16, 2010

***By James E. Miller, Esquire and Eric L. Young, Esquire***

In an act of rule-making that addresses certain of the issues that SFMS has addressed in ground-breaking litigation regarding so-called "revenue sharing payments" from mutual funds to service providers offering 401k investments, which also are commonly referred to as kickbacks, and which SFMS has challenged as illegal, prohibited transactions on behalf of certain of its clients, the Department of Labor ("DOL") recently announced a rule that will require enhanced disclosure of 401(k) fees by requiring plan providers to report to plan sponsors direct and indirect compensation received in connection with account services. That requirement will take effect on July 16, 2011, according to the DOL.

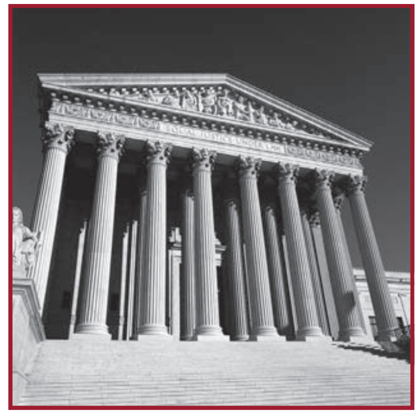
The DOL regulations, which have been issued in the wake of Congress' unfortunate failure to enact Representative Miller's 401(k) Fair Disclosure and Pension Security Act of

*(Continued on page 9)*

# Seventh Circuit Scores A Victory For Investors And Rejects Fifth Circuit Standard For Class Certification In Securities Cases

***By Laurie Rubinow, Esquire***

In *Schleicher v. Wendt*, 2010 WL 3271964 (7th Cir. Aug. 20, 2010), the Seventh Circuit Court of Appeals issued a significant decision regarding class certification which represents a victory for shareholders. In the Wendt case, the Seventh Circuit affirmed the district court's grant of class certification and rejected the defendants' arguments on appeal, noting that, "if accepted, [these] arguments would end the use of class actions in securities cases." In so holding, the Seventh Circuit pointedly rejected the Fifth Circuit Court of Appeals decision in *Oscar Private Equity Investments v. Allegiance Telecom, Inc.*, 487 F.3d 261 (5th Cir. 2007)(holding that loss causation must be rigorously analyzed at the class certification stage), and held that the Oscar decision was contrary to the Supreme Court's precedent in *Basic, Inc. v. Levinson,* 485 U.S. 224 (1988) and that Oscar "represents a go-it alone strategy by the Fifth Circuit [that] is not compatible with [Seventh Circuit] decisional law ... and ***we disapprove of its holding***," noting that Oscar did more than just tighten the requirements for class certification [because] "[i]t would make certification impossible in many securities suits" and, finally, rejecting the defendants' reliance upon a "materialization of the risk" defense, finding that "[t]he phrase adds nothing to the analysis" of whether fraud in the form of a false or misleading statement or omission has occurred. The Wendt decision is a persuasive and compelling rejection of the Oscar decision that should assist shareholders in combating attempts by defendants to utilize the erroneous decision in Oscar to eliminate shareholder rights.



# Class Certification Decision Affirmed By Seventh Circuit Court of Appeals

***By Jayne A. Goldstein, Esquire and Nathan Zipperian, Esquire***

On August 20, 2010, the Seventh Circuit Court of Appeals affirmed the district court's certification of a securities fraud class action in *Schleicher v. Wendt*, 09-2154, 2010 WL 3271964 (C.A.7 (Ind.), Aug. 20. 2010). The opinion, penned by the Honorable Frank H. Easterbrook, clarified that plaintiffs need not establish loss causation or the materiality of false statements or omissions before a class can be certified and offered a scathing critique of the Fifth Circuit's approach to class certification in securities cases.

This securities fraud suit was filed against certain managers of Conseco (later renamed CNO Financial Group), who were alleged to have made false statements that led investors to pay too much for their shares in 2001-2002. Defendants argued that, before a class could be certified, plaintiffs must prove "everything (except falsity) required to win on the merits." *Id.* at *2. The Seventh Circuit resoundingly rejected the argument, holding that "whether statements were false, or whether the effects were large enough to be called material, are questions on the merits" and that "certification is largely independent of the merits..." *Id.* at *5.

Defendants had based their argument on the Fifth Circuit's decision in *Oscar Private Equity Investments v. Allegiance Telecom, Inc.*, 487 F. 3d 261 (5th Cir. 2007), which held that a district court should resolve issues of whether contested statements actually caused material changes in stock prices before certifying a class. Rejecting what it called the Fifth Circuit's "go-it-alone" strategy, the Court in Schleicher went out of its way to expressly disapprove of the holding in Oscar that proof of loss causation is essential to class certification, observing that requiring proof of loss causation at the certification stage would make class certification "impossible in many securities statutes." Writing for the panel, Judge Easterbrook further opined that the approach adopted by the Fifth Circuit was starkly at odds with the Federal Rules Committee's decision in 1966 to separate class certification from a decision on the merits. *Id.* at *6. The Court's harsh criticism of Oscar continued, stating that it did not "think it appropriate for the judiciary to make its own further adjustments by reinterpreting Rule 23 to make likely success on the merits essential to class certification in securities-fraud suits." *Id.*

The Schleicher decision is significant for its emphatic rejection of the argument that falsehood and materiality are issues to be considered as the class certification stage. "Falsehood and materiality are issues on the merits; whether a statement is materially false is a question common to all class members and therefore may be resolved on a class-wide basis after certification." *Id.* at *7. It also is important in that it explicitly recognizes, and rejects, the Fifth Circuit's inappropriate activism in attempting to eliminate class actions in securities fraud litigation.

# *Tellabs* Redux – Still Litigating After All These Years

***By Patrick A. Klingman, Esquire and Karen M. Leser-Grenon, Esquire***

The first complaint was filed in June, 2002, alleging a class period from late 2000 through mid-2001. It has been up to the Supreme Court, as the vehicle for the Court's most comprehensive analysis to date of the pleading requirements for scienter (the "intent" element for securities fraud) under the Private Securities Litigation Reform Act, *see Tellabs, Inc. v. Makor Issues & Rights, Ltd.,* 551 U.S. 308 (2007), down to the Seventh Circuit Court of Appeals again and ultimately back to the U.S. District Court for the Northern District of Illinois, which subsequently certified a class and appointed class representatives. In August, 2010, following the completion of discovery on issues almost a decade old (and after the departure of three of the four officer-defendants from Tellabs, the company-defendant, and even the death of one of the class representatives), the District Court issued its opinion of the defendants' motion for summary judgment. *Makor Issues & Rights, Ltd. v. Tellabs, Inc.,* No. 02 C 4356, 2010 WL 3275284 (N.D. Ill. Aug. 13, 2010).

Summary judgment is a procedural device which essentially tests whether there are any disputed facts worthy of devoting the time and effort of trial; the party moving for summary judgment must show that, based on evidence uncovered during discovery and any other relevant, admissible material, "there is no genuine issue as to any material fact and that the movant is entitled to a judgment as a matter of law." Federal Rule of Civil Procedure 56 (c). In a lengthy and detailed decision, which touched on areas ranging from the business records exception to the hearsay rule of evidence to collateral estoppel (the doctrine by which the Court concluded that certain factual and legal determinations reached in a related action, brought against *Tellabs* and the same four officer-defendants by current and former *Tellabs* employees for alleged violations of ERISA, were equally binding in the securities action), as well as traditional securities fraud concepts such as loss causation, the Court found an absence of evidence to support the majority of the plaintiffs' claims. And even as to those claims that survived, the Court found that the plaintiff-class in the related ERISA lawsuit, comprised of *Tellabs*' retirement plan participants and beneficiaries whose accounts held *Tellabs* stock (who overlapped with the securities fraud class but who had lost their ERISA trial), were likewise foreclosed from any recovery in the securities case.

By the time of the Court's decision, plaintiffs' securities fraud action centered around three categories of alleged misstatements made by *Tellabs*' officers or in its announcements: (1) representations regarding *Tellabs*' financial results for the fourth quarter of 2000 (and the extent to which those results were the product of "channel stuffing," whereby *Tellabs* flooded its customers with unwanted products); (2) unfounded revenue projections, made in 2001 when demand for the company's flagship networking device, the TITAN 5500, was allegedly slowing; and (3) that demand for the TITAN 5500 was continuing to grow, when in fact demand was waning. *Makor Issues*, 2010 WL 3275284, at *3.

Channel stuffing, whereby a manufacturer "floods" its downstream customers with unordered products, creates a short-lived illusion of increased demand between the time when the company sends the excess product down the lines of distribution and the time when the distributors return the unwanted excess. *Id.* at *41. Because such sales practices are obviously intentional, they can be powerful indicia of securities fraud and were arguably the most compelling of the securities claims asserted. However, the Court granted summary judgment on this claim because there was no evidence that

*(Continued on page 6)*

# Court Denies Motion to Dismiss In Huron Consulting Securities Fraud Case Arising From Restatement

***By Scott R. Shepherd, Esquire and Laurie Rubinow, Esquire***

In *Hughes v. Huron Consulting Group, Inc.,* 2010 WL 3087501 (N.D.Ill. August 6, 2010), the Honorable Elaine E. Bucklo denied a motion to dismiss securities fraud claims in a case arising from a restatement of financial results for a period of over three years. As the Court explained, Huron is "a corporation founded in 2002 by a number of partners and professionals formerly employed by Arthur Andersen, the well-known business and

*(Continued on page 12)*

## Bank of America Securities, Derivative and ERISA Litigation Permitted To Move Forward

***By Nathan Zipperian, Esquire***

On August 27, 2010, the Honorable P. Kevin Castel of the United States District Court for the Southern District of New York issued a lengthy opinion substantially upholding the amended complaint in *In re Bank of America Corp. Securities, Derivative and "ERISA" Litigation*, No. 09-MD-2058, 2010 WL 3448194 (August 27, 2010 S.D.N.Y.).

This case arises out of Bank of America's allegedly false and misleading statements and omissions in connection with its September 2008 merger with Merrill Lynch (the "Merger"), which were revealed to the market in several corrective disclosures between January 12, 2009 and January 21, 2009. The amended complaint alleges, *inter alia*, that defendants violated the federal securities laws by misrepresenting or failing to disclose that Bank of America ("BoA") and Merrill Lynch ("Merrill") had secretly agreed to allow Merrill to pay up to $5.8 billion in bonuses to its executives and employees; that Merrill had suffered losses in excess of $15 billion during October and November 2008 alone; and that BoA was only able to consummate the Merger because it received a $138 billion taxpayer bailout prior to the close of the Merger.

Judge Castel substantially upheld lead plaintiffs' claims alleging: (1) securities fraud and false proxy statements related to BoA's agreement to allow Merrill to pay up to $5.8 billion in discretionary bonuses to Merrill employees; (2) false proxy statements for failure to disclose Merrill's fourth quarter 2008 losses; (3) false offering statements related to the secret bonus agreement with Merrill; and (4) control person liability with respect to these claims.

Specifically, the Court rejected defendants' arguments that the possibility of Merrill bonus payments with the "prior written consent" of BoA was an adequate disclosure concerning the bonus agreement because, "[w]hen the Joint Proxy was filed on October 31, 2008, the bonus payment to Merrill employees was more than hypothetical." *In re Bank of America Corp. Securities, Derivative and "ERISA" Litigation,* 2010 WL 3448194, at *25. Indeed, Judge Castel found that "[i]f the 'prior written consent' had been given to make payments of up to $5.8 billion, a reasonable investor may well have considered that information important to both the purchase of shares and the granting or withholding of a proxy." *Id.* at *26.

The Court rejected defendants' arguments that they had adequately disclosed Merrill's dire fourth quarter performance through various risk disclosures and projections, stating as follows: "By the time the Joint Proxy issued, the stormy forecast for the fourth quarter was not merely a projection: the storm had arrived. These losses were a known fact to company insiders, yet were not disclosed to BofA's shareholders." *Id.* at *33.

Judge Castel also declined to dismiss negligence-based claims related to alleged material misstatements over Merrill's bonuses and the scope of Merrill's losses, as well as a claim related to whether the bank intentionally hid an agreement with regulators to obtain bailout money.

Although he substantially upheld the Amended Complaint, Judge Castel did dismiss claims related to, *inter alia*, whether BoA should have conducted better due diligence, and whether it should have revealed why it considered invoking a contractual clause to back out of the merger.

## SFMS Files Class Action Lawsuit Against Ernst & Young On Behalf Of Investors In Stewardship Credit Arbitrage Fund, LLC

***By Patrick A. Klingman, Esquire***

SFMS has instituted legal action against Ernst & Young, LLP ("E&Y") in the United States District Court for the District of Connecticut (Civil Action No. 3:10-cv-01517 (JCH)) on behalf of all persons or entities (the "Class") who invested or otherwise contributed to the Stewardship Credit Arbitrage Fund, LLC ("Stewardship" or the "Fund") between March 15, 2006 and October 22, 2008. Among other claims, the Complaint alleges that Ernst & Young, Ltd. (Bermuda), Ernst & Young, Ltd. (Bahamas) and E&Y, as the auditor of the Fund between 2003 and 2008, issued "clean" audit opinions regarding the Fund and its financial position. However, these statements were false and misleading because Ernst & Young, among other things, never examined whether the collateral which secured the overwhelming majority of the Fund's investments even existed. By the end of the Class Period, after revelations that most of the Fund's assets were invested in a "Ponzi" scheme operated by Thomas

*(Continued on page 12)*

## Eight Circuit Rules That A Broker-Dealer Can Be Held Liable As A Control Person

***By Scott R. Shepherd, Esquire and Karen M. Leser-Grenon, Esquire***

The Eighth Circuit recently held that a broker-dealer can be liable as a control person under the federal securities laws if it exercises direct or indirect control over one of its registered representatives. *Lustgraaf v. Behrens*, No. 09-2960, 2010 WL 3271242 (8th Cir. Neb. Aug. 20, 2010). The complaint was filed by a group of investors against Kansas City Life Insurance Company ("KCL") and Sunset Financial Services ("Sunset"), a broker-dealer. Plaintiffs in the case invested money with one of the agents from KCL and Sunset, Mr. Behrens, who allegedly misappropriated the funds through a Ponzi scheme. Mr. Behrens brokered the money through a separate entity, National Investments, Inc. ("National Investments"), an entity which Mr. Behrens controlled. In connection with the investments by plaintiffs, Mr. Behrens sold promissory notes to plaintiffs, listing National Investments as the borrower. The plaintiffs alleged that Mr. Behrens promised that he would invest plaintiffs' money and provide them with a steady stream of income. The complaint asserted that Sunset and KCL should be held liable for Mr. Behrens' misappropriation of the investors' money based on control-person liability under section 20(a) of the Securities and Exchange Act of 1934.

The U.S. District Court for the District of Nebraska dismissed plaintiffs' control-person claims against Sunset. The U.S. Court of Appeals for the Eight Circuit reversed the District Court's dismissal, holding that, where a broker-dealer exercises considerable direct or indirect control over its representatives, or where the broker-dealer provides material aid to the alleged violator, the broker-dealer may be held liable. In this case, the fact that the broker-dealer gave Mr. Behrens access to the securities markets was sufficient, even though Mr. Behrens operated and utilized a separate entity, National Investments, to orchestrate his Ponzi scheme. According to the Eighth Circuit's decision, plaintiffs must allege facts demonstrating that the alleged control person actually exercised control over the primary violator's general operations in order to state a claim for control-person liability. Facts showing that the controlling shareholders were actively participating in the decision-making process of the primary violator are necessary. The existence of shared directors also is a factor to be considered in determining control according to the Eighth Circuit, but this factor is not determinative. Lastly, the Court offered some examples of facts that would not be sufficient to show control person liability. For example, two entities sharing office locations is not a sufficient allegation of control, nor is the allegation that there is some crossover in agents and representatives.

The Eighth Circuit Court of Appeals' decision in *Lustgraaf v. Behrens* is an important one, as it allows more aggressive action by defrauded investors to hold control persons liable under Section 20(a) of the securities laws in the proper circumstances.

## Court Denies Motion to Dismiss In Pfizer Derivative Case

***By James C. Shah, Esquire and Karen M. Leser-Grenon, Esquire***

In *In re Pfizer Inc. Shareholder Derivative Litigation*, 2010 WL 2747447 (S.D.N.Y. July 13, 2010), the Honorable Jed S. Rakoff denied a motion to dismiss claims for breach of fiduciary duty against the Board of Directors (the "Board") and certain officers of Pfizer, Inc. ("Pfizer"). The shareholder derivative cases at issue were filed after the United States Department of Justice announced on September 2, 2009 that Pfizer had agreed to pay $2.3 billion in fines and penalties arising from the illegal "off-label" marketing by Pfizer and one of its subsidiaries of various regulated drugs. Significantly, the Court rejected defendants' argument that the plaintiff shareholders were required to either make written demand on the Board before instituting action or spell out specific allegations establishing each individual Board member's knowledge of wrongdoing. In so holding, Judge Rakoff persuasively reasoned as follows:

"[T]here may be situations where the absence of particularized allegations as to what each director knew and what he or she did about that knowledge would not support excusing demand. However, demand futility is to be evaluated based on the facts of each particular case rather than through the invocation of rigid rules. *See Grobow v. Perot*, 539 A.2d 180, 186 (Del.1988) (stating that "[r]easonable doubt" for demand futility purposes "must be decided by the trial court on a case-by-case basis employing an objective analysis," and not by "rote and inelastic" criteria), overruled on other grounds, *Brehm v. Eisner,* 746 A.2d 244 (Del.2000). ***Under the unique facts of this case, defendants have demonstrated a substantial likelihood that a majority of the board faces personal liability.***

As illustrated by the sheer size of the 2009 fines, the wrongdoing here alleged was not only pervasive throughout Pfizer but also was committed in the face of the board's repeated promises to closely monitor and prevent such misconduct.... Among other things, Pfizer's Chief Compliance Officer [was required] to report directly to the board the allegations of misconduct here at issue so that the

*(Continued on page 11)*

## Tellabs Redux – Still Litigating After All These Years

*(Continued from page 3)*

"*Tellabs* ever shipped 'unwanted' or 'unordered' product to its customers." *Id.* at *43-*45.

The Court also determined that no evidence supported loss causation as to this claim, which required proof "that Defendants' alleged misrepresentations proximately caused Plaintiffs' losses." *Id.* at *45. According to the *Makor Issues* Court, there was no evidence that the company's revised revenue warnings were prompted by the alleged channel stuffing: "[w]hile the Court agrees that Plaintiffs need not demonstrate that the corrective disclosures specifically corrected a previous representation or disclosed the alleged fraudulent scheme, in order to demonstrate loss causation Plaintiffs must show a 'link' between the concealed information and the motivation to make the disclosure." *Id.* at *47.

With respect to the 2001 revenue projections, the Court concluded that plaintiffs had failed to present evidence that the then-CEO had "actual knowledge" of the statements' falsity. Among other provisions, the PSLRA affords special protection to projections (*i.e.*, "forward-looking statements") -- while the scienter requirement for statements of current fact is either knowing falsity or recklessness, the scienter demanded for forward-looking statements is stricter and permits liability only upon proof of knowing falsity, which the Court found had not been met. See Major Issues, 2010 WL 3275284, at *48-*56.

The last category of alleged misstatements concerned demand for *Tellabs*' TITAN 5500 product. The Court first concluded that the company's then-CEO could not be liable for misrepresentations made by another officer-defendant because the federal securities laws do not impose an obligation "to rectify others' misstatements." Id., 2010 WL 3275284, at *58. It did, however, find that, as to two of the three other similar statements, "genuine question[s] of material fact" remained regarding whether they were misleading. *Id.* at *60. Even this slight victory was diminished by the Court's subsequent conclusion that, because the ERISA class was "collaterally estopped" from proceeding against defendants (as they brought substantially similar claims, even though under ERISA, but had lost), it could not proceed and effectively was carved out of the securities class. *Id.* at *63-*66.

It will be interesting to see if, at long last, this is the end of the *Tellabs* case or if another chapter will be written with another appeal of this decision.

# The Second Circuit "Bespeaks Caution"

***By Patrick A. Klingman, Esquire***

The Second Circuit Court of Appeals, because its jurisdiction embraces New York federal courts and, hence, the nation's capital markets, is among the most influential sources on interpretation of the federal securities laws. With relatively few decisions reaching the U.S. Supreme Court, the Second Circuit's recent opinion, *Iowa Public Employees' Retirement System v. MF Global, Ltd.*, No. 09-3919-cv, 2010 WL 3547602 (2d Cir. Sept. 14, 2010), is likely to be considered a significant interpretation of the "bespeaks caution" doctrine for the foreseeable future.

According to the "bespeaks caution" rule, "[a] forward-looking statement accompanied by sufficient cautionary language is not actionable because no reasonable investor could have found the statement materially misleading" (*i.e.*, a reasonable investor would not presume that "the future is settled, or unattended by contingency"). *MF Global*, 2010 WL 3547602, at *2. The doctrine is of relatively recent vintage -- the first apparent use in the Second Circuit was *Goldman v. Belden's* observation "that not all predictions are actionable and that liability probably should not be imposed

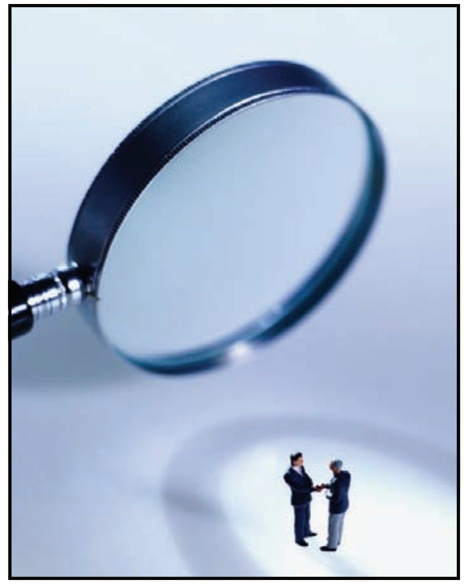

on the basis of words that 'bespeak caution.'" *Id.*, 754 F.2d 1059, 1068 (2d Cir. 1985) (citation omitted). It attempts to address the question of what to do about forward-looking information (*i.e.*, predictions), which has the tendency "to be embarrassed by the passage of time." *MF Global*, 2010 WL 3547602, at *2. The Securities and Exchange Commission ("SEC") generally prohibited the disclosure of forward-looking information, but then in 1979, changed course and created a regulatory "safe harbor." Thereafter, Congress embraced the doctrine when enacting the Private Securities Litigation Reform Act of 1995, which created a "safe harbor" for forward-looking statements. According to *MF Global*, the "bespeaks caution" doctrine

*(Continued on page 11)*

# *Louisiana School Employees' Retirement System v. Ernst & Young*: Another Difficult Decision Regarding Auditor Liability

***By James E. Miller, Esquire and Jayne A. Goldstein, Esquire***

Courts continue to impose very difficult and, as some would argue, unreasonably high barriers to imposing federal securities liability upon accountants and auditors. *In Louisiana School Employees' Retirement System v. Ernst & Young*, 2010 WL 3655657 (6th Cir. 2010), the Sixth Circuit Court of Appeals affirmed the dismissal of a securities fraud complaint against Ernst & Young ("E&Y"). The Sixth Circuit's decision highlights the difficulty in holding accountants and auditors liable for securities fraud, even in those cases where the facts appear to establish a high degree of culpability on the part of the accountants/auditors. In so holding, the Sixth Circuit found that the recklessness necessary to establish auditor liability under the federal securities laws is conduct "akin to conscious disregard [that] is highly unreasonable [and] an extreme departure from standards of ordinary care" such that "any reasonable man would have known it." Furthermore, the Sixth Circuit imposed an even higher burden on plaintiffs attempting to plead securities fraud against an auditor, stating that "[t]he standard for recklessness is more stringent when the defendant is an outside auditor ... [and proof of] recklessness [for an auditor defendant] requires a mental state so culpable that it approximates an actual intent to aid in the fraud being perpetrated by the audited company." In evaluating an auditor's application of accounting principles, the Sixth Circuit also held that, to establish scienter (*i.e.,* fraudulent intent) on the part of an auditor, a complaint must plead much more than misapplication of accounting principles. Specifically, the Sixth Circuit held that a plaintiff must prove that (1) the accounting practices were so deficient that the audit amounted to "no audit at all"; (2) an egregious refusal to see the obvious or investigate the doubtful; or (3) the accounting judgments made amounted to decisions that no reasonable accountant would have made under the same circumstances. In reaching this decision, the Sixth Circuit rejected the lead plaintiff's argument that E&Y's use of stale and incorrect data in preparing its audit opinion and disregard of numerous "red flags" at the company that was the subject of the audit, including reduced reserve percentages, an investment banker's alleged refusal to participate in a transaction and a history of accounting errors at the company, as well as the presence of numerous violations of Generally Accepted Accounting Principles ("GAAP") and Generally Accepted Auditing Standards ("GAAS") in the audit, gave rise to liability under the federal securities laws on the essential basis that competing inferences could be drawn from these facts that were at least as compelling and which militated against a finding of fraud. Unfortunately, however, in reaching this decision, the Sixth Circuit Court of Appeals appears to have improperly viewed the facts pled in a light most favorable to E&Y, as opposed to the lead plaintiff, and established a standard within its jurisdiction that may prove difficult to overcome. The consequence of such decisions, of course, is to permit auditors to all too often act as knowing and complicit co-conspirators in cases of corporate fraud and malfeasance. SFMS will continue to follow and report on developments in this important field.



# The Final Word On Financial Regulatory Reform: The Dodd-Frank Wall Street Reform and Consumer Act

***By Jayne A. Goldstein, Esquire, James E. Miller, Esquire and Laurie Rubinow, Esquire***

At long last, Congress has enacted comprehensive financial regulatory reform. The Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub.L. 111-203, H.R. 4173) was signed into law by President Barack Obama on July 21, 2010. The Dodd-Frank Act is the most sweeping change to financial regulation in the United States since the Great Depression, and represents a paradigm shift in the American financial regulatory environment. The key elements of the Dodd-Frank Act are as follows:

**Encourages Whistleblowers**

- Provides significant incentives for individuals who know of a securities violation to contact the Securities and Exchange Commission ("SEC") and assist in the investigation and prosecution of wrongdoing.
- When information provided by the whistleblower leads to an SEC enforcement action that results in monetary sanctions of more than $1 million, the SEC must pay the whistleblower 10-30% of those amounts.
- Provides protections to whistleblowers and, if successful in court for retaliation, provides for recovery of double pay back, reinstatement with appropriate seniority, attorneys' fees and expert costs.

**Expands Secondary Liability**

- SEC has the restored ability to impose aiding and abetting liability on persons who "recklessly" (previous standard was "knowingly") provide substantial assistance to someone who violates the Exchange Act.
- Clarifies that the SEC may use enforcement actions against "control" persons unless they acted in "good faith" and did not directly induce the conduct at issue.

**Provides SEC Jurisdiction Over Foreign Securities Transactions**

- Provides U.S. courts with jurisdiction over actions brought by the SEC under Exchange Act and Investment Advisors Act relating to securities investments outside the U.S. in certain circumstances (but does not provide the same rights to private plaintiffs).

**Creates Fiduciary Standards For Brokers**

- Authorizes SEC to issue rules to impose fiduciary duties on brokers and dealers when they provide "personalized investments advice about securities to a retail customer."

**Provides SEC Budget Increases**

- Doubles the SEC budget between 2011 to 2015.

Creates a new $100 million SEC "Reserve Fund" to supplement the agency's budget.

**Creates Investor Advocate and Advisory Committee**

- Creates "Investor Advocate" who will report to SEC Chairman.
- Creates new "Investor Advisory Committee" comprised of Investor Advocate, state regulators and representatives of a broad cross-section of investing public to meet at least twice a year and advise and consult with SEC on investor protection issues.

**Provides For SEC Operational Improvements**

- Hiring market specialists
- Sharing information with other agencies
- Paying penalties to victims
- Investor testing
- Requires self-examination

**Imposes Penalties In Administrative Proceedings**

- Penalty awards can now be made in administrative proceedings, which should result in more cases brought as administrative hearings, where pretrial discovery is limited, no right to jury trial and the administrative law judge's decision is reviewed by SEC commissioners who originally directed the proceeding to be filed.

**Provides For Nationwide SEC Trial Subpoenas**

- Enables both the SEC and Defendants in SEC federal court litigation to issue subpoenas requiring the witnesses to appear in person anywhere in the United States and to appear in person at trials and hearings, the result of which is to make financial fraud cases easier to try in federal courts.

*(Continued on page 13)*

## Department of Labor Will Require Service Providers To Make Mandatory Fee Disclosures By July 16, 2010

*(Continued from page 1)*

2009 (H.R. 2989), which was vehemently opposed by the financial services and insurance industry, contains several notable requirements but also does not appear to address the pernicious nature of revenue sharing kickbacks in the meaningful manner that certain retirement industry reformers had hoped. The following is a summary of the DOL's general requirements under its fee disclosure rule:

- *Covered Plans* -- Employee Pension Benefit Plans, Including Defined Benefit Pension Plans and 401k Plans, And Other Retirement Plans Covered Under The Employee Retirement Income Security Act ("ERISA") -- But Is Not Applicable To Individual Retirement Accounts ("IRAs"). Other Benefit Plans (Including Welfare Benefit Plans) Are Not Covered.

- *Covered Service Providers* -- Fiduciary Service Providers Under ERISA Or The Investment Advisers Act of 1940 (which generally applies to mutual funds); Service Providers That Perform Banking, Consulting, Custodial, Insurance, Investment Advisory, Investment Management, Recordkeeping Or Third Party Administration Services For A Covered Plan; and Service Providers That Receive Indirect Compensation In Connection With Providing Accounting, Actuarial, Appraisal, Auditing, Legal Or Valuation Services To A Covered Plan. To Be A Covered Service Provider, An Individual Or Entity Must Receive At Least $1,000 In Compensation (Whether Direct Or Indirect).

- Covered Service Providers must describe (a) the services provided to the covered plan; (b) a statement as to whether such services are being provided by the service provider in a capacity as a fiduciary to the covered plan; (c) a statement of all direct compensation received by the service provider; (d) a statement of all indirect compensation received by the service provider; (e) a statement of all compensation paid to and among related parties to the service provider; (f) compensation associated with termination of contractual arrangements with a service provider; (g) a description of compensation, whether direct or indirect, received in connection with recordkeeping services; (h) a description of the manner in which compensation is received by the service provider; (i) additional disclosures for service providers admitting fiduciary status; and (j) additional investment disclosures for service providers performing recordkeeping and brokerage services.

In issuing this rule, the DOL expressly acknowledges that "[c]ompensation arrangements in the market for retirement plan services are complex, [p]ayments from third parties and among service providers can create conflicts of interest between providers and their clients;" and a 401(k) plan vendor may receive "revenue sharing" from a mutual fund that it makes available to clients." Nevertheless, the DOL only has created these regulations to increase the level of certain disclosures regarding fees (with the consequence of the failure to disclose being that a service provider cannot claim that its fees are reasonable if it fails to so disclose) without addressing the fact that, under ERISA, if a service provider is a fiduciary, it is prohibited from receiving revenue sharing payments and similar consideration under ERISA Section 406(b)(3) without regard for whether any fees received from third parties are reasonable or not. Therefore, although the DOL's recent rules create a useful first step in addressing the payment and receipt of revenue sharing kickbacks, it fails to squarely address the plain illegality of the receipt of such payments in many circumstances. In fact, the DOL specifically states that it expresses no view on the effect of this rule with respect to other statutory provisions and/or other statutory or administrative exemptions that may be available to service providers.

Meanwhile, at the Securities and Exchange Commission ("SEC"), a proposal has been issued to sharply limit the sales fees that mutual funds can charge on shares sold through brokers, as well as to limit the total annual sales and marketing fees that can be charged by mutual funds. Since these sales and marketing fees (often referred to as 12b-1 fees) are the chief funding vehicle that permit mutual funds to pay hidden and largely undisclosed revenue sharing kickbacks, these new SEC rules may have the effect of reducing revenue sharing payments in the future. We will continue to monitor and report on these regulations and developments in this important field.

## The Supreme Court's Upcoming Clarification On The Reach Of Secondary Actor Liability Under The Federal Securities Laws

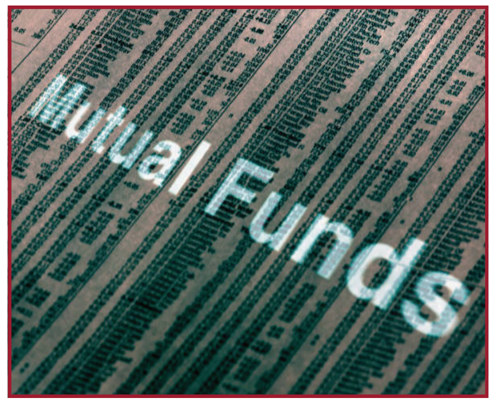
*(Continued from page 1)*

of § 10(b) aiding and abetting liability does not mean that secondary actors in the securities markets are always free from liability under the securities Acts." *Id.* at 180. To the contrary, *Central Bank* reiterated that "[a]ny person or entity, including a lawyer, accountant, or bank, who employs a manipulative device or makes a material misstatement (or omission) on which a purchaser or seller of securities relies may be liable as a primary violator under 10b-5, assuming all of the requirements for primary liability under Rule 10b-5 are met." *Id.* (emphasis in original).

Based on *Central Bank*, the principle emerged that "a secondary actor cannot incur primary liability under the [federal securities laws] for a statement not attributed to that actor at the time of its dissemination." *Wright v. Ernst & Young LLP*, 152 F.3d 169, 175 (2d Cir. 1998), *cert.* denied, 525 U.S. 1104 (1999); *see Pacific Inv. Management Co. LLC v. Mayer Brown LLP*, 603 F.3d 144, 148 (2d Cir. 2010) ("Absent attribution, plaintiffs cannot show that they relied on defendants' *own* false statements, and participation in the creation of those statements amounts, at most, to aiding and abetting securities fraud") (emphasis in original); *cf., Howard v. Everex Sys., Inc.,* 228 F.3d 1057, 1061 n.5 (9th Cir. 2004) ("[S] ubstantial participation or intricate involvement in the preparation of fraudulent statements is grounds for primary liability even though that participation might not lead to the actor's actual making of the statements").

In *First Derivative Traders v. Janus Capital Group, Inc.,* 566 F.3d 111 (4th Cir. 2009), *cert.* granted, 130 S.Ct. 3499 (2010), the plaintiff alleged that certain statements regarding market timing contained in the Janus funds' prospectuses, which were freely available at a Janus website (jointly controlled by the parent and the subsidiary advisory firm), were false and misleading because, contrary to the prospectuses, Janus had allowed certain hedge funds to engage in "time zone arbitrage" in connection with Janus' funds. *Id.,* 566 F.3d at 116-117. Once this news came out via a 2003 investigation by New York's Attorney General, the value of the parent company's stock decreased by 23%. *Id.,* 566 F.3d at 118. At the District Court and on appeal, defendants principally argued that the plaintiff's allegations were insufficient to establish that Janus made the statements (*i.e.,* inadequate allegations of attribution).

Surprisingly, although the Fourth Circuit Court of Appeals traditionally has not been known for advancing the cause of potential securities fraud claimants, the *Janus Capital* panel held that attribution can be inferred. Recognizing that "[d]irect attribution of a public statement ... is an inexact proxy for determining whether investors will attribute a publicly available statement to a particular person or entity," *Janus*, 566 F.3d at 124, the panel concluded that, in the realm on mutual funds,




"interested investors would infer that [the subsidiary advisory firm] played a role in preparing or approving the content of the Janus fund prospectuses," including the allegedly misleading market timing statements. *Id.* at 127. However, the same was not true with respect to the corporate parent -- according to *Janus Capital*, it would not be "apparent to the investing public that the investment advisor's parent company, which sponsors a family of funds, participates in the drafting or approving of prospectuses issued by the individual funds." *Id.* at 128. However, the Fourth Circuit panel did find that allegations of control person liability under Section 20(a) were sufficient as to the corporate parent. *Id.* at 130-131.

At first blush, *Janus Capital* may seem somewhat of a stretch -- shareholders of a company seeking to hold it and its subsidiary liable for misstatements in the prospectuses of seemingly independent mutual funds for which the subsidiary, but not the parent, has some oversight role. But upon closer examination, the Fourth Circuit is to be commended for its decision, which clearly endorses the perception of most mutual fund investors -- that investment advisory firms, regardless of their formal (*i.e.,* legal) relationship, effectively control mutual funds. Whether such pro-investor, pragmatic views prevail before the Supreme Court remains to be answered. We will continue to keep you updated regarding developments with respect to secondary liability.

## Court Denies Motion to Dismiss In Pfizer Derivative Case

*(Continued from page 5)*

board could deal with them directly, rather than relying on management. There is no reason to believe this reporting requirement was not fully complied with, thus guaranteeing that each member of the board was bombarded with allegations of continuing misconduct of the very kind that the prior settlements looked to the board to prevent. *Cf. Abbott Labs,* 325 F.3d at 806 ("Where there is a corporate governance structure in place, we must then assume the corporate governance procedures were followed and that the board knew of the problems and decided no action was required."). In such circumstances, nothing in either federal or Delaware law holds it insufficient for individual directors' knowledge and liability to be pleaded inferentially. *See, e.g., id.* at 809; *McCall,* 239 F.3d at 824 (holding that demand was excused based on directors' intentional or reckless disregard of "red flags" suggesting that company was committing health care fraud, based on allegations relating to directors' prior experience in the health care industry, audit information, improper acquisition practices, a qui tam action, a federal investigation, and a New York Times investigation); *Veeco Instruments,* 434 F.Supp.2d at 278; *cf. In re Biopure Corp. Deriv. Litig.*, 424 F.Supp.2d 305, 307-08 (D.Mass. 2006) (permitting plaintiffs to "rely on an inference that the defendant officers and directors had knowledge of the FDA's clinical hold" on the company's principal product for purposes of pleading demand futility). ***To put it bluntly, the allegations of the Complaint evidence misconduct of such pervasiveness and magnitude, undertaken in the face of the board's own express formal undertakings to directly monitor and prevent such misconduct, that the inference of deliberate disregard by each and every member of the board is entirely reasonable."***

The Court's holding in the *Pfizer* case is a significant one, as it should permit shareholders to succeed on derivative claims against officers and Board members in instances where a company allegedly has been infected by systemic fraud and malfeasance.

## The Second Circuit "Bespeaks Caution"

*(Continued from page 6)*

represents the judiciary's contribution toward regulating such representations. *Id.*, 2010 WL 3547602, at *3.

The *MF Global* panel concluded that the district court improperly used the "bespeaks caution" doctrine to dismiss all of the plaintiff's 1933 Act claims. Specifically, the underlying complaint alleged that, contrary to the defendant-brokerage firm's claims in its prospectus of risk management controls already in place, one of the company's brokers had been permitted to evade trading limits and collateral requirements and thereby lose over $140 million speculating to wheat futures. *Id.*, 2010 WL 3547602, at *1. The company covered the loss, but once the incident became known, it revealed that the company's internal risk controls had not been applied to brokers trading for their own accounts or when taking client orders by phone. *Id.* On this news, the firm's stock price declined by more than a third over two days, for a market cap loss of more than $1.1 billion. *Id.* Nevertheless, the district court dismissed all claims based on the prospectus' risk management statements because it found that cautionary language elsewhere in the filing rendered the misstatements inactionable pursuant to the "bespeaks caution" doctrine. *Id.* at *2.

The district court characterized the plaintiff's allegations as the failure "to disclose the risk of a future negative event." *Id.* at *3. The *MF Global* court disagreed, concluding that the dismissed allegations "specifies an omission of present fact, to which bespeaks caution does not apply." *Id.*, 2010 WL 3547602, at **2, 3. Specifically, the *MF Global* court explained as follows:

"[W]hile it is true that predictions about the future can represent interpretations of present facts (and vice versa), there is a discernible difference between a forecast and a fact, and courts are competent to distinguish between the two. A forward-looking statement (accompanied by cautionary language) expresses the issuer's inherently contingent prediction of risk or future cash flow; a non-forward-looking statement provides an ascertainable or verifiable basis for the investor to make his own prediction."

*Id.* at *4. Since "characterizations of *MF Global*'s risk-management system ... invite the inference that the system will reduce the firm's risk," the *MF Global* court seemed to signal that, upon remand, the district court should find such statements to be factual assertions and thus unprotected by the "bespeaks caution" doctrine. *Id.* at *5 (quoting *Rombach v. Chang*, 355 F.3d 164, 173 (2d Cir. 2004) ("Cautionary words about future risk cannot insulate from liability the failure to disclose that the risk has transpired")). Thus, decisions like *MF Global*, albeit incrementally, continue to act as bulwarks against the overly generous protection afforded by statutory and regulatory "safe harbors."

## Court Denies Motion to Dismiss In Huron Consulting Securities Fraud Case Arising From Restatement

*(Continued from page 3)*

financial services firm that collapsed in the wake of the Enron accounting scandal." On July 31, 2009, Huron announced that it would restate its financial results for the fiscal years 2006, 2007, and 2008, as well as for the first quarter of 2009, due to improper accounting of payments made in the course of Huron's acquisition of other companies. Specifically, the restatement revealed the following facts:

- In several instances, Huron had accounted for payments made to selling shareholders of the acquired firms as "goodwill."
- This accounting treatment was highly advantageous to Huron, since goodwill --unlike expenses -- does not offset income.
- A number of payments to selling shareholders did not meet the requirements for goodwill treatment under Generally Accepted Accounting Principals ("GAAP").
- These payments should have been booked as expenses.
- This improper accounting had allowed Huron to report aggregate net income during the 13 quarter period at issue that was nearly double what it would have been if Huron's accounting had been in accordance with GAAP.

The restatement caused Huron's stock prices to collapse, plummeting nearly 70% on the first trading day after it was announced, and causing massive losses to investors.

The Court rejected defendants' argument that plaintiffs had failed to plead a claim of securities fraud. First, the Court refused to accept the notion that defendants were unaware of the accounting consequences to Huron of the selling shareholders' redistribution agreements in light of the respective effects those agreements had on Huron, on the one hand, and the selling shareholders, on the other. Specifically, the Court observed that Huron benefitted handsomely from the selling shareholders' redistribution of Huron's payments because those payments could then be used to entice key employees to stay with the company (and to achieve their performance goals), without Huron's having to account for additional employment-related expenses. In addition, since the selling shareholders, on the other hand, were obvious losers under the deal, the Court stated that a reasonable person could infer that the selling shareholders would only agree to give away a portion of their acquisition proceeds if that were a negotiated condition of the acquisition. Defendants offer no alternative explanation. As a result, the Court reasoned that the logical inference was that these extremely sophisticated accounting and financial professionals identified an accounting "loophole," which they knew to be improper but believed could be papered over with side agreements, and that this inference was at least as compelling as the inference that they innocently failed to appreciate that their accounting was inconsistent with GAAP. The Court also noted that Huron's public explanation for the accounting error implicated management by stating that management "misunderstood or misapplied" GAAP.

The Court rejected the argument that plaintiffs had pled nothing more than a "must have known" theory, based on allegations of defendants' accounting and financial expertise. In so holding, the Court concluded that allegations regarding defendants' professional experience was an appropriate canvas upon which the tableau of fraud was painted. In sum, the Court held that the concrete fraud plaintiffs properly alleged was that defendants' goodwill accounting for acquisition payments occurred in spite of their knowledge of (or, indeed, involvement in) side agreements that rendered goodwill accounting for those payments improper. The Court's decision in *Huron Consulting* constitutes a well-reasoned and highly persuasive decision that recognizes the rights of shareholders to assert claims when sophisticated accounting frauds are allegedly perpetrated by financial professionals.

## SFMS Files Class Action Lawsuit Against Ernst & Young On Behalf Of Investors In Stewardship Credit Arbitrage Fund, LLC

*(Continued from page 4)*

Petters, now serving a federal prison term for fraud, E&Y belatedly informed the Fund's investors that its 2008 audit opinion, issued only months before, could no longer be relied upon. The Complaint alleges that, by failing to even examine the underlying collateral and engaging in other similar conduct, E&Y's audits were so reckless that they amounted to no audits. If you would like to review a copy of the Complaint filed in this case, please contact us by telephone ((866) 540-5505) or email (pklingman@sfmslaw.com; bferling@sfmslaw.com).

## The Final Word On Financial Regulatory Reform: The Dodd-Frank Wall Street Reform and Consumer Act

*(Continued from page 9)*

**Creates New Deadlines for SEC Enforcement Actions, Inspections and Examinations**

- Once SEC notifies a target that it is considering an enforcement action ("Wells" notice), the staff will have 180 days to file its case.

**Grants SEC Authority To Restrict Customer Arbitration Agreements**

- Authorizes SEC to issue rules limiting, imposing conditions upon, or prohibiting agreements requiring arbitration by customers of brokers, dealers, municipal securities dealers and investment advisors.

**Imposes New Requirements For Securities Industry-Wide Bars**

- When a securities professional is suspended or barred due to misconduct, the suspension will prohibit that person's association with any "broker, dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization."

**Closes Regulatory Gaps**

- Provides the SEC and Commodity Futures Trading Commission ("CFTC") with authority to regulate over-the-counter derivatives so that irresponsible practices and excessive risk taking can no longer be hidden from regulatory oversight. SEC, CFTC and other regulators must coordinate with each other to develop rules in furtherance of the Act.
- CFTC has jurisdiction over all swaps, which under the new Act include virtually all over-the-counter derivatives, with some exclusions, including an exclusion for a security-based swap.
- The SEC has jurisdiction over security-based swaps (swaps based on a single security or loan or referencing a single issuer).

**Creates Central Clearing and Exchange Trading For Derivatives**

- Subject to some exceptions, requires central clearing and exchange trading for derivatives that can be cleared and provides a role for regulators and clearing houses to determine which contracts should be cleared.
- "End-user" exemption: SEC and CFTC have authority to review swaps to see if they meet the criteria to be exempt.
- Must Register with CFTC and SEC: Swap dealers and major swap participants must register and submit periodic reports with CFTC. Security-based swaps dealers and major security-based swap participants must register and submit periodic reports with SEC.

**Improves Market Transparency**

- Requires data collection and publication through clearing houses or swap repositories to improve market transparency and provide regulators important tools for monitoring and responding to risks.

**Creates Financial Safeguards**

- Adds safeguards to system by ensuring dealers and major swap participants have adequate financial resources to meet responsibilities.
- Provides regulators the authority to impose capital and margin requirements on swap dealers and major swap participants, not end users.

**Establishes Higher Standard of Conduct**

- Establishes a code of conduct for all registered swap dealers and major swap participants when advising a swap entity.
- When acting as counterparties to a pension fund, endowment fund, or state or local government, dealers are to have a reasonable basis to believe that the fund or governmental entity has an independent representative advising them.

**Creates New Regulatory Regime for Credit Rating Agencies**

- New Office and New Focus at SEC: Creates an Office of Credit Ratings at the SEC with expertise and its own compliance staff and the authority to fine agencies; SEC is required to examine Nationally Recognized Statistical Ratings Organizations ("NRSRO") at least once a year and make key findings public.
- Disclosure: Requires NRSRO to disclose their methodologies, their use of third parties for due diligence efforts and their ratings track records.
- Independent Information: Mandates that agencies consider information in their ratings that comes to their attention from a source other than the organizations being rated if they determine it to be credible.

*(Continued on next page)*

## The Final Word On Financial Regulatory Reform: The Dodd-Frank Wall Street Reform and Consumer Act

*(Continued from previous page)*

- Conflicts of Interest: Prohibits compliance officers from working on ratings, methodologies, or sales; mandates that a report to the SEC when certain employees of the NRSRO go to work for an entity that the NRSRO has rated in the previous 12 months.
- Liability: Investors can bring lawsuits against rating agencies for a knowing or reckless failure to conduct a reasonable investigation of the facts or to obtain analysis from an independent source; and NRSROs are now subject to "expert liability" with the nullification of Rule 436(g), which provides an exemption for credit ratings provided by NRSROs from being considered a part of the registration statement.
- Right to De-register: SEC can de-register an agency for providing bad ratings over time.
- Educational: Requires rating analysts to pass certain qualifying exams and have continuing education requirements.
- Regulatory Requirements to Use NRSRO Ratings: Encourages investors to conduct their own analysis and decreases over-reliance on ratings.
- Independent Boards: Requires at least half the members of NRSRO boards to be independent, with no financial stake in the credit ratings.
- Ends Shopping for Ratings: SEC will provide a new mechanism to prevent issuers of asset-backed securities from picking the agency they think will give the highest rating, after conducting a study and submission of a report to Congress.

**Creates New Rights and Requirements With Respect To Executive Compensation and Corporate Governance**

- Vote on Executive Pay and Golden Parachutes: Explicitly gives SEC authority to issue rules permitting shareholder access to proxy materials. Provides shareholders a say on pay with the right to a non-binding vote (to be held every three years) on executive pay. Shareholders are required to vote at least once every six years on whether vote will occur every one, two or three years.
- Shareholders approve "golden parachutes."
- Provides shareholders with a powerful opportunity to hold executives of companies accountable and a chance to disapprove where shareholders see misguided incentive schemes that threaten individual companies and then the broader economy.
- Institutional investment managers will be required to report at least annually how they voted on any required "say-on-pay" or "golden parachute" votes.
- Nominating Directors: Gives the SEC authority to grant shareholders proxy access to nominate directors.
- Committees: New standards for listing on an exchange will require that compensation committees include only independent directors and have authority to hire compensation consultants to foster independence from the executives they are reviewing. A compensation committee can only select consultants after taking into consideration a variety of factors such as: other services, the amount of fees received, conflict of interest policies and procedures, business or personal relationships between the advisor and members of the compensation committee, and any stock of the company owned by the advisor
- Clawback: Public companies must set policies to take back executive compensation if the company is required to restate its financial statements. The company will recover from any current or former executive officer who received incentive-based compensation (including stock options).
- SEC Review: SEC must clarify disclosures relating to compensation by requiring companies to provide charts that compare their executive compensation with stock performance over a five-year period.
- Decreased Broker Discretion: Brokers cannot vote shares held in trust on matters involving executive compensation, director elections or "other significant matters" unless specific instructions are provided by the beneficial owner.
- Enhanced Compensation Oversight for the Financial Industry: Requires federal financial regulators to issue and enforce joint compensation rules specifically applicable to financial institutions with a federal regulator.

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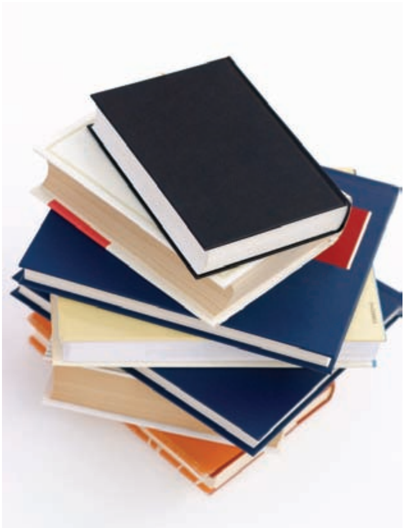
## The Final Word On Financial Regulatory Reform: The Dodd-Frank Wall Street Reform and Consumer Act

*(Continued from previous page)*

Although investors and other interested parties will have to wait some time to determine whether the Dodd-Frank Act is effective in improving the efficiency and fairness of the capital markets, Congress has made an impressive start in tackling many of the key issues that caused the financial crisis. Although it would have been helpful for Congress to also expand private litigants= rights more significantly, on balance, it appears that Dodd-Frank will accomplish many of its goals. Of course, investors and other interested parties will also have to wait for the promulgation of related regulations by the SEC to fully evaluate the impact of Dodd-Frank. In short, with respect to these regulations, the proof will be in the proverbial pudding.

## Recommended Readings

- *100 Simple Things You Can Do to Prevent Alzheimer's*, by Jean Carper - another valuable and insightful book written by SFMS client and New York Times Best-Selling Author, Jean Carper, who is one of the preeminent living authors on helpful strategies for those concerned about their long-term health. To view Jean's hysterical viral video involving a faux Sarah Palin commercial to promote her latest book, please visit http://jeancarper.com/2010/09/26/sarah-palin-book-commercial-on-memory-loss-funny-outtakes-and-bloopers/
- *Adam Smith: An Enlightened Life,* by Nicholas Phillipson - in this detailed biography of the father of modern capitalism, we learn that Adam Smith stood for only certain of the principles attributed to him by modern day devotees and that Smith himself was more of a moral-man than a market-man, who was influenced greatly by his closest colleague, David Hume, an avowed atheist and controversial philosopher from the Enlightenment.
- *Confessions of an Economic Hit Man*, by John Perkins - a chilling account of an individual who claims that he was covertly recruited by the U.S. government and worked on the payroll of an international consulting firm with the job of convincing the political and financial leadership of underdeveloped countries to accept enormous development loans from institutions like the World Bank so that, once saddled with debts they could not hope to pay, those countries would be forced to acquiesce to political pressure from the United States on a variety of issues. The author denies the existence of any conspiracy and instead posits the existence of a corporatocracy. If true, this book has profound implications for how we should view the U.S.'s role in the world over the past 50 years.
- *King of Capital: The Remarkable Rise, Fall and Rise Again of Steve Schwarzman and Blackstone*, by David Carey and John E. Morris - an insightful and detailed history of the creation and survival of the world's largest private equity firm, by two authors who give enormous access to the inner workings of a usually secretive environment.
- *Mahabharata in Polyester: The Making of the World's Richest Brothers and Their Feud*, by Hamish McDonald - a must read for anyone interested in India's emergence as a world economic power. In this book, the author traces the rise of the Ambani family from a two-room house with a dirt floor in Gujarat to one of the richest families in world history in one generation.



## SFMS News

**Lesley Weaver joins SFMS**. We are pleased to welcome Lesley Weaver, who will be based in the firm's San Francisco, California office. Lesley earned her A.B. *magna cum laude* from Harvard College and her J.D. from the University of Virginia. She has extensive experience representing U.S. and international institutional investors and individuals in securities class actions and corporate governance matters, including significant recoveries in *In re Marsh & McLennan Secs. Litig.* ($400 million), *In re Cardinal Health Secs. Litig.* ($600 million), *In re Cisco Secs. Litig.* ($99 million), and *In re Boeing Secs. Litig.* ($92.5 million). Prior to joining the firm, Lesley was a partner at Lerach Coughlin and later was senior counsel at Grant & Eisenhofer. Lesley can be reached by email (lweaver@sfmslaw.com) or by telephone (415/992-7282).

**SFMS Achieves Victory In Class Certification Appeal**. SFMS is pleased to report that it has achieved a major victory before the Ninth Circuit Court of Appeals in *Wolin v. Jaguar Land Rover North America, LLC*, 617 F.3d 1168 (9th Cir. 2010). In this case, SFMS was able to persuade a unanimous panel of the Ninth Circuit to reverse a decision by the Honorable Andrew Guilford of the United States District Court for the Central District of California, which denied a motion for class certification. The *Land Rover* decision is significant, as it makes clear that a plaintiff need not prove that a majority of a proposed class suffered injury in order to certify a class where common issues of fact and law otherwise predominate and the other predicates for class certification have been met. SFMS congratulates James C. Shah who successfully argued the appeal before the Ninth Circuit.

**Three SFMS Attorneys Named As Super Lawyers**. SFMS is pleased to announce that, once again, Scott R. Shepherd, Natalie Finkelman Bennett and Jayne A. Goldstein have been named Super Lawyers. SFMS congratulates Scott, Natalie and Jayne on this well-deserved recognition from their peers.

SFMS

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