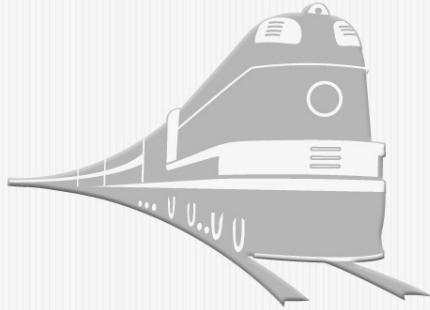


# 2007 BUSINESS LITIGATION EXPRESS



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# 2007 BUSINESS LITIGATION EXPRESS

## Securities Class Actions and Derivative Litigation: Two for the Price of One

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## Securities Class Actions & Derivative Litigation: Litigation Trends

### » Filing Activity

- 42 % decrease in first half of 2007
  - » 59 filings v. 101 average semi-annual filings 1996-2005
  - » Annualized: 124 filings
    - 7 % Increase from 116 filings in 2006
    - 38 % Decrease from 202 filings average 1996-2005
- Second to 2006 as lowest level of filing activity since 1996, immediately after PSLRA became law

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## Securities Class Actions & Derivative Litigation: Litigation Trends

### » Market Capitalization Losses

- 13% Increase from 2006 (\$334B v. \$295B)
- 55% Decline from 1996-2005 average
- (\$334B v. \$608B)

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## Securities Class Actions & Derivative Litigation: Litigation Trends

- » Possible causes for filing decline
  - Less Fraud
    - » Increased enforcement activity
    - » Heightened awareness among corporate insurers
    - » Suggests permanent shift in class action landscape
  - Strong stock market with less volatility
    - » Suggest temporary shift in class action landscape

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## Securities Class Actions & Derivative Litigation: Litigation Trends

- » Easier to dispose of by way of dismissal?
  - Heightened particularity pleading
    - » State with particularity facts giving rise to strong inference that defendant acted with the required state of mind
      - » Strong inference = reasonable person deem inference at least as compelling as any plausible opposing inference
      - » Tellabs, Inc. v. Makor Issues & Rights, Ltd., 127 S. Ct. 2499, 2509-10 (2007)
      - » Required state of mind
      - » Varies among circuits
      - » In re: Silicon Graphics, Inc. Sec. Lit., 483 F.3d 920, 988 (9th Cir. 1999)
  - Post-PSLRA dismissal rate = 39.1%
    - » Includes summary judgment
    - » Pre-PSLRA dismissal rate = 19.4%

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## Securities Class Actions & Derivative Litigation: Litigation Trends

- » Sub prime Mortgage Market
  - 12 Filings with related allegations as of September 2007
  - Derivative litigation to follow?
    - » Citigroup Inc.
      - \$16.9 billion mortgage related losses
      - Charles Prince resigns as CEO
    - » Merrill Lynch & Co.
      - \$18.4 billion in losses, predominately mortgage related
      - Stan O'Neal resigns as CEO
- » Bounty for settlement contributions from high profile defendants
  - WorldCom - \$18 million
  - Enron - \$13 million

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## Securities Class Actions & Derivative Litigation: Litigation Trends

- » Hold more outside advisors accountable
  - StoneRidge Investment Partners v. Scientific Atlanta, No. 06-43
    - » Argued before U.S. Supreme Court on October 9, 2007
    - » Revisit *Central Bank of Denver v. First Interstate Bank of Denver*, 511 U.S. 164 (1994)

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## Securities Class Actions & Derivative Litigation: Litigation Trends

- » Accounting irregularities will remain focus
  - Misrepresentation in financial documents involved in 92% of 2007 filings
  - Allegations of lack of appropriate internal controls increasing in popularity
    - » 70 % of accounting allegations involved internal controls (48 % in 2006)
    - » Will accounting firms become target?

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## Securities Class Actions & Derivative Litigation: Litigation Trends

- » Accounting for option issuance
  - Expensing options
  - Backdating options
    - » SEC Interest
      - 102 investigations
      - 11 recommendations of no enforcement

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## Securities Class Actions & Derivative Litigation: Litigation Trends

- Backdating Options
  - » Private Action
    - Shareholder class action
    - Derivative action – may be preferred method
      - » Statute of limitations
      - » Unaccompanied by significant stock decline
      - » Easier to demonstrate breach of fiduciary duty than willful fraud
  - » Private equity funds next target?

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## Securities Class Actions & Derivative Litigation: Litigation Trends

- » Filed in state court
  - Action brought on behalf of corporation
    - » Shareholder steps in shoes of corporation
    - » Monetary recovery to corporation

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## Securities Class Actions & Derivative Litigation: Derivative Litigation

- » Filed in state court
  - Claims alleged against officers and directors
    - » Based on same conduct alleged in securities litigation
    - » Corporation named as nominal defendant
  - Insurance coverage
    - » Directors & Officers (D & O) insurance carriers extend coverage
    - » Fighting for policy dollars
  - Ethical issues
    - » Joint representation of corporation and director
    - » Representation in both securities litigation and derivative action

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## Securities Class Actions & Derivative Litigation: Derivative Litigation

- » State law applies
  - Private right of action conferred on shareholder
  - Substantive claims
    - » Breach of fiduciary duty
    - » Tag-along claims

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## Securities Class Actions & Derivative Litigation: Sequencing

- » Securities litigation filed first
  - Shorter statute of limitations
  - Necessity to defend suit = element of damage in derivative action

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## Securities Class Actions & Derivative Litigation: Response to Class Action

- » Securities litigation
  - Motion to dismiss
  - Discovery stay until decided
- » Derivative action
  - Motion to stay action pending resolution of motion to dismiss in securities case
  - State equivalent of motion to dismiss
    - » Demand futility
    - » Failure to state claims

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## Securities Class Actions & Derivative Litigation

- » D & O Insurance
- » Issues & Trends

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