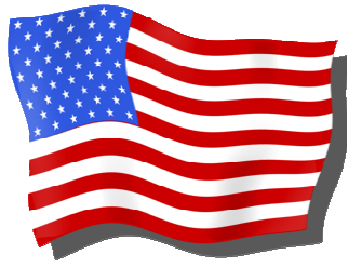


# Opportunities for European Institutional Investors



## Shareholder Actions in the U.S.

*“Pension trustees have a duty to protect the assets in their scheme. At the very least they shouldn’t neglect opportunities to recoup losses, especially where the cost and effort of doing so are commensurate with the expected return.”*

David Paterson, Head of Corporate Governance, NAPF National Association of Pension Funds, UK  
*Speaking at the NAPF Conference in Edinburgh*



# Securities Fraud



# Securities Fraud

Securities fraud occurs when a company makes materially false statements to the public upon which investors rely.

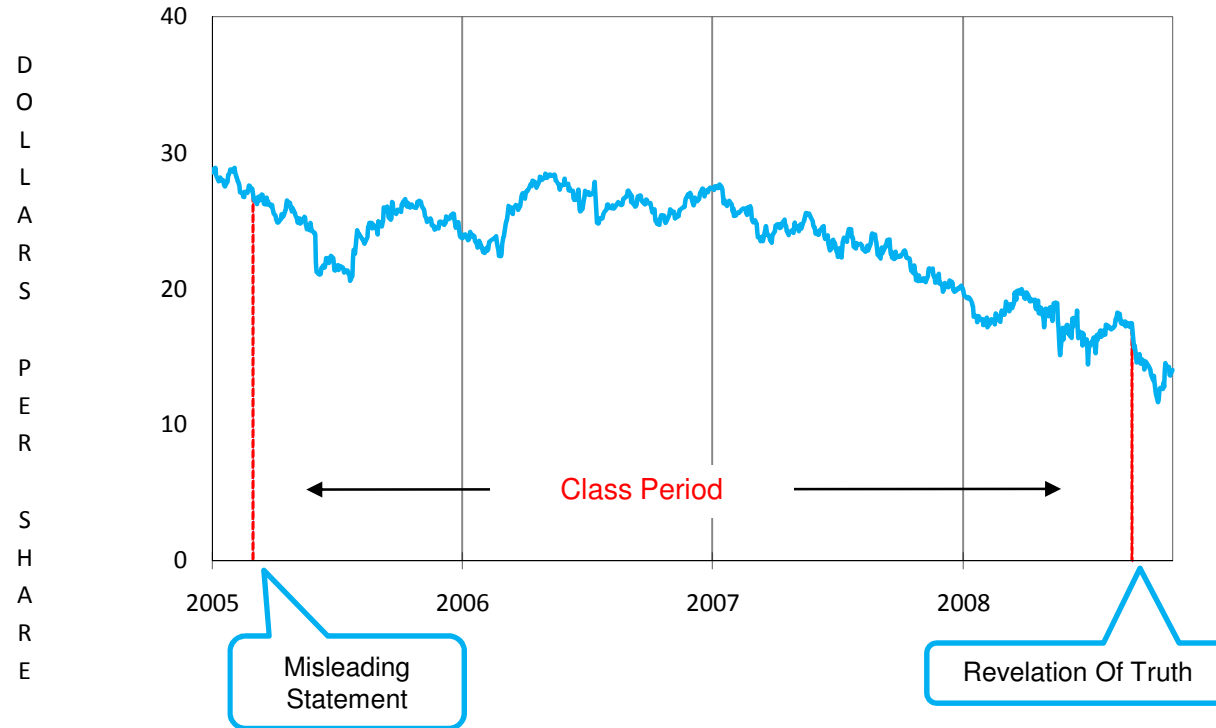
When the truth is disclosed, the stock price declines to reflect the true value of the stock. Losses incurred are typically compensable in U.S. courts.

# What Securities Fraud Looks Like

## STOCK PRICE DURING CLASS PERIOD

### PFIZER, INCORPORATED: PFE

Class Period: July 20, 2005 - January 23, 2009

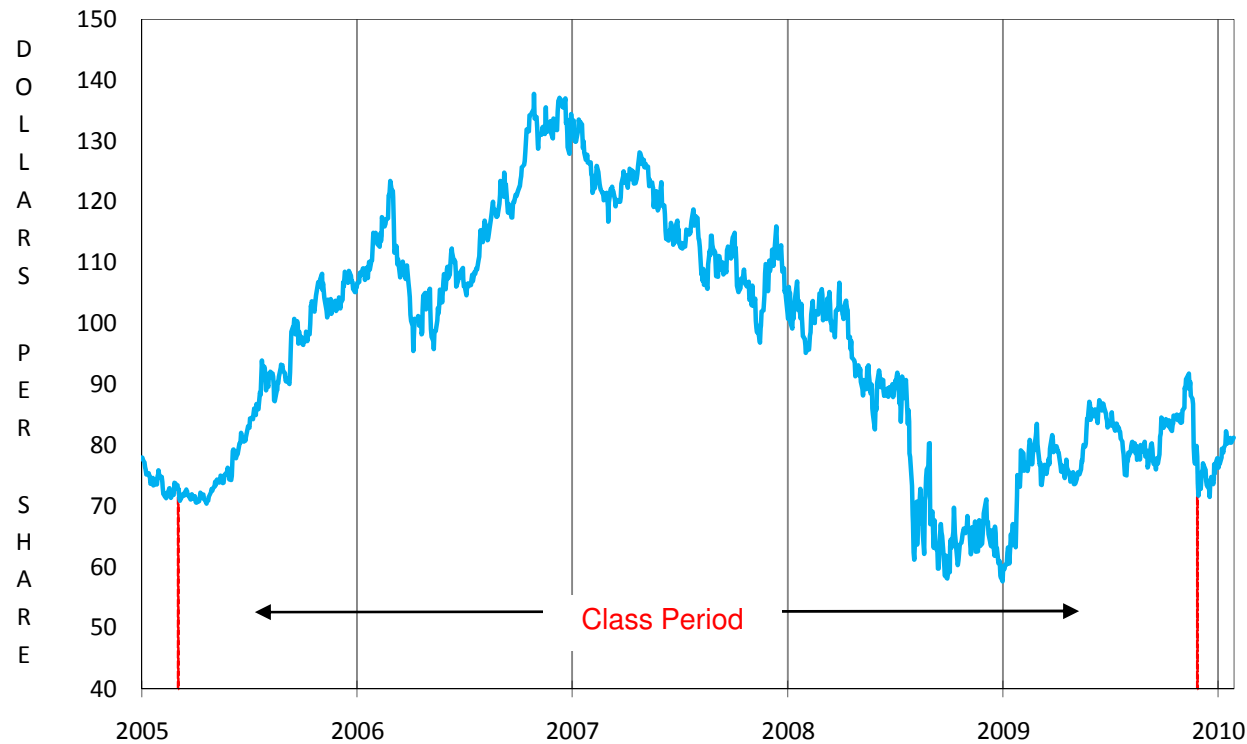


# What Securities Fraud Looks Like

## STOCK PRICE DURING CLASS PERIOD

### TOYOTA MOTOR CORPORATION: TM

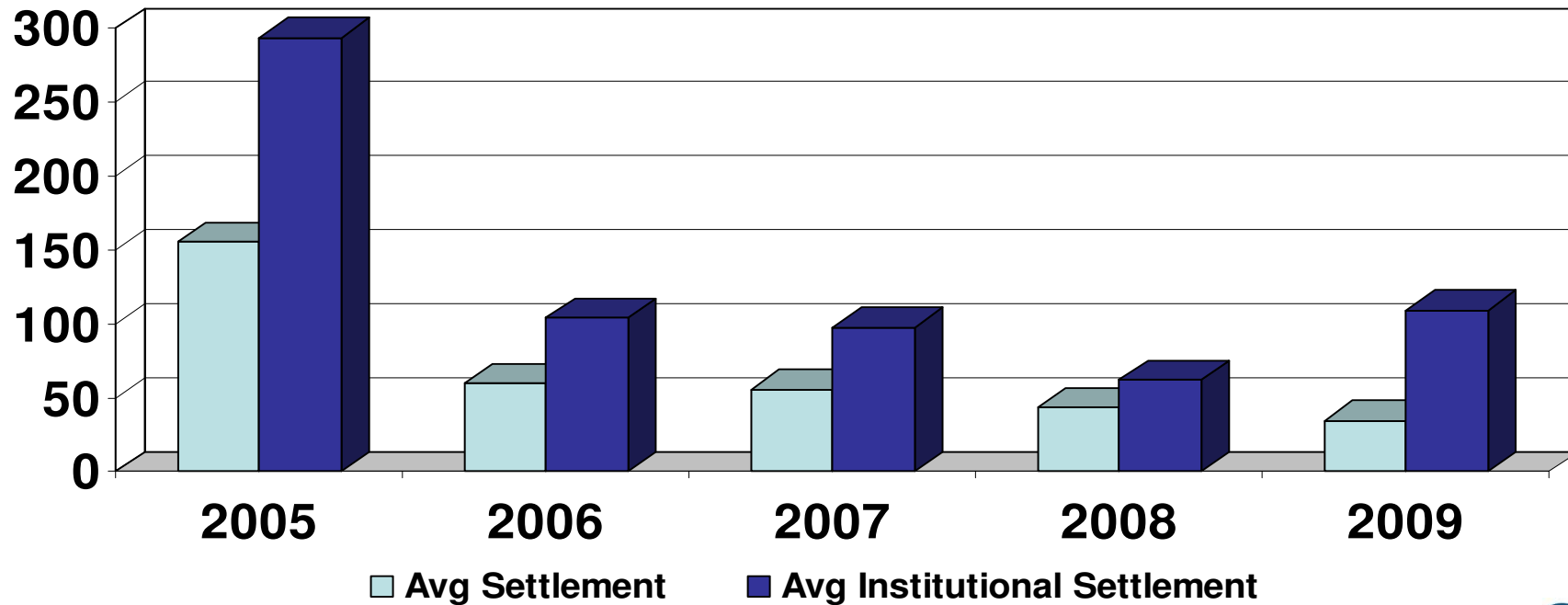
Class Period: May 10, 2005 - February 2, 2010



# Importance of Institutional Investors

## Institutional Investors Make a Difference

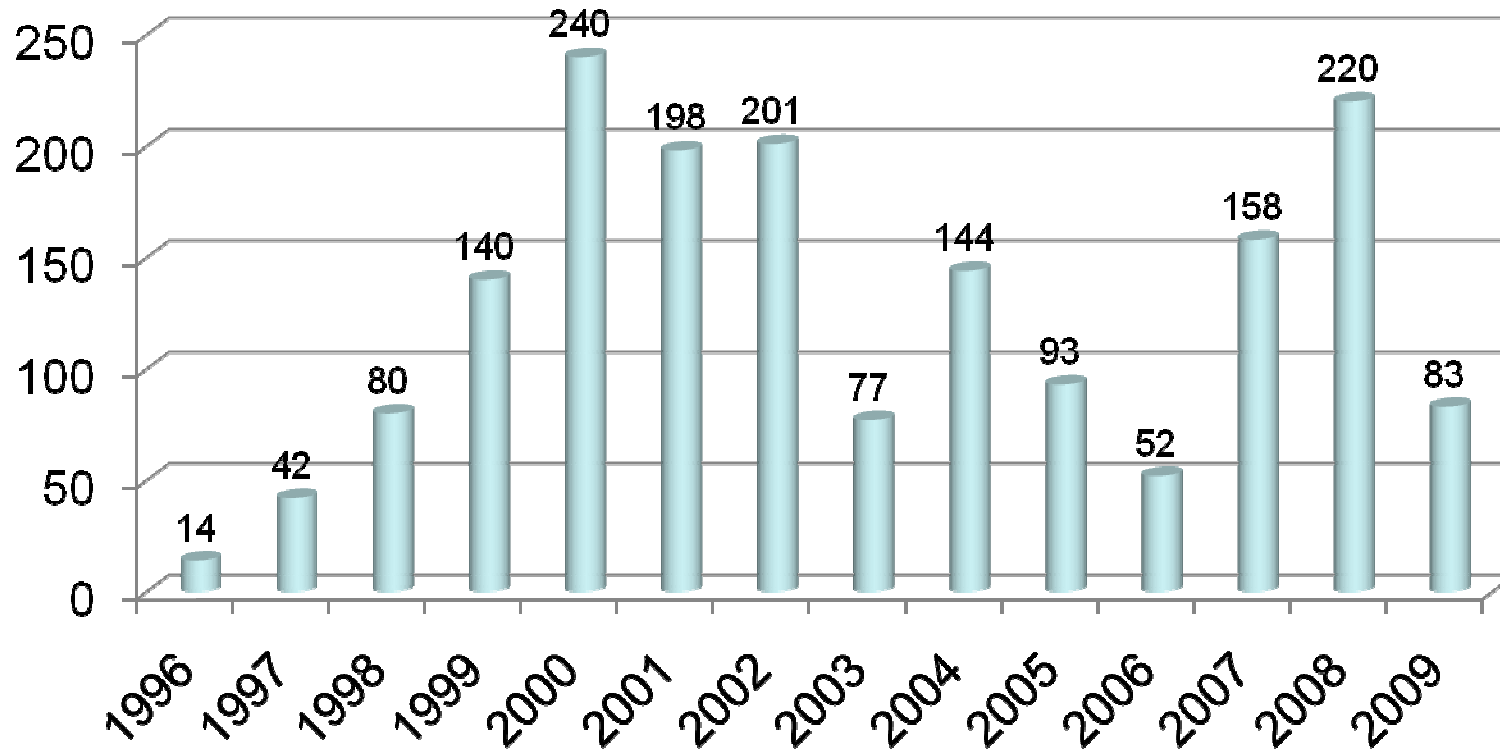
PricewaterhouseCoopers 2009 Securities Litigation Study  
Average Settlements (\$ Millions)



# Market Capitalization Losses due to Fraud

*In Bio. US \$*

## DDL Index – Dollar Disclosure Loss



Source: 2009 Cornerstone Research

Securities class actions seek compensation for share purchases from the first to the last day of the class period. The recognizable losses are calculated based on the portion of the decrease in share value that can be attributed to fraud.

# Typical Case Scenarios

## Accounting/Financial Reporting

- § Overstating revenues/understating costs
- § Overstating inventories/customers
- § Cookie jar/revenue and cost shifting
- § Insider loans concealed
- § Off-balance sheet activity/hidden debts
- § Understating risks of writedowns/losses/valuations related to securitized assets such as mortgage backed securities



# Typical Case Scenarios

## Operational Risk

- § Environmental and/or worker safety risk and costs of compliance/fines
- § Regulatory investigation/criminal investigation (bribery, tax fraud etc.)



# Typical Case Scenarios

## Drugs/Pharmaceuticals

- § Pre-Marketing
  - § Failure to receive FDA approval
  - § Potential market substantially smaller than promised
- § Post-Marketing
  - § Health risk identified/FDA action
  - § Manufacturing defect identified



# Typical Case Scenarios

## Manufacturing

- § Product failure
- § Manufacturing process/equipment failure
- § Raw material problems



# Private Litigation vs. SEC Litigation

Company	Securities Class Action Recovery	SEC Recovery
Enron	\$7.161 Billion	\$424.84 Million
WorldCom	\$6.156 Billion	\$750 Million
AOL Time Warner	\$2.65 Billion	\$308 Million
Lucent	\$667 Million	\$25 Million
Bristol-Myers Squibb	\$574 Million	\$150 Million

Sources: Institutional Shareholder Services; Stanford Securities Class Action Clearinghouse

# Significant Settlements in 2009 & 2010

Case Name	Settlement Year	Total Settlement
UnitedHealth Group, Inc.	2009	\$925,500,000
Countrywide Financial	2010	\$624,000,000
IPO Securities Litigation	2009	\$586,000,000
HealthSouth Group	2009	\$554,000,000
Merrill Lynch & Co.	2009	\$475,000,000
Qwest Communications	2009	\$445,000,000
Marsh & McLennan	2009	\$400,000,000
General Motors Corp.	2009	\$303,000,000
Comverse Technologies	2010	\$225,000,000
The Mills Corp.	2009	\$202,750,000
Schering-Plough Corp.	2009	\$165,000,000
Brocade Communications	2009	\$160,098,500
Bristol-Myers Squibb	2009	\$125,000,000
Peregrine Systems, inc.	2009	\$117,500,000
Homestore.com, Inc.	2009	\$107,421,216
Paramlat Finanziaria, S.p.A.	2010	\$91,400,000
International Rectifier Corp.	2010	\$90,000,000
Moneygram International	2010	\$80,000,000

# Foreign Claimants in U.S. Courts

- § A recent U.S. Supreme Court decision, *Morrison v. National Australia Bank Ltd.* (June 24, 2010), has changed the rules for foreign plaintiffs bringing securities actions in U.S. Courts.
- § The “conduct-and-effects” test no longer applies – prior to *Morrison*, jurisdiction was based on facts involving either substantial wrongful conduct in the U.S. or wrongful conduct that had a substantial effect in the U.S. or on U.S. citizens.

# Foreign Claimants in U.S. Courts

- § Despite the *Morrison* decision, foreign investors may still bring U.S. securities fraud claims.
- § The "Transactional" test is now used for determining the extraterritorial reach of the U.S. securities laws.
- § The provisions of the Exchange Act (10b-5 actions) apply to "transactions in securities listed on domestic exchanges" and to claims relating to "domestic transactions in other securities."

# Foreign Claimants in U.S. Courts

- § The U.S. courts will still be open to foreign institutional investors because they buy and sell vast amounts of U.S. financial assets every year.
- § ***In 2008, foreigners purchased \$38 trillion dollars in U.S. financial assets and sold \$37.8 trillion dollars in assets.***

Source: James K. Jackson, Foreign Investment in U.S. Securities. CRS Report for Congress: Prepared for Members and Committees of Congress. 7-5700. RL32462. (November 18, 2009).

# Foreign Claimants in U.S. Courts

- § European institutional investors can and should play a role in U.S. securities actions.
- § The largest losses provide significant motivation and opportunity.
- § Foreign and U.S. investors can suffer similar losses.
- § The transaction patterns of funds can give rise to significant grounds to seek appointment as Lead Plaintiff; it can have significant economic advantages.

# Options: Securities Fraud Class Actions

## § Lead Plaintiff

Under PSLRA, investor with largest loss is presumptive lead plaintiff

## § Opt-Out

Appropriate under certain circumstances

## § Absent Class Member

Imperative: claims monitoring and processing

# Other U.S. Options Following *Morrison* Decision

- § Assign litigation rights to a U.S. based LLC
- § LLC can then Opt-Out collectively with losses aggregated and increase potential recovery
- § LLC can minimize potential *res judicata* issues (for example when a U.S. court refuses to include investors from certain countries in the class)
- § File lawsuit on behalf of LLC, individual investors are not “named” in the lawsuit

# *Morrison* Decision's Impact on Vivendi Litigation

- Counsel in the Class case have made two primary arguments:
  1. Vivendi shares are “registered” in the U.S. making *Morrison* inapplicable
  2. If *Morrison* does apply, the Court will most likely allow plaintiffs to amend and reinstate the previously dismissed New York common law fraud claims included in the opt-out complaints
- The opt-out cases will remain stayed until Judge Holwell rules on these issues in the Class case

# Royal Bank of Scotland Litigation

- Following the *Morrison* decision foreign claimants in the U.S. securities litigation were excluded from the Class
- We are evaluating bringing claims in the United Kingdom
- Currently, we are working to obtain a Queen's counsel ruling stating that we have at least a 60% chance of winning any litigation

# Converium Holdings AG Global Settlement

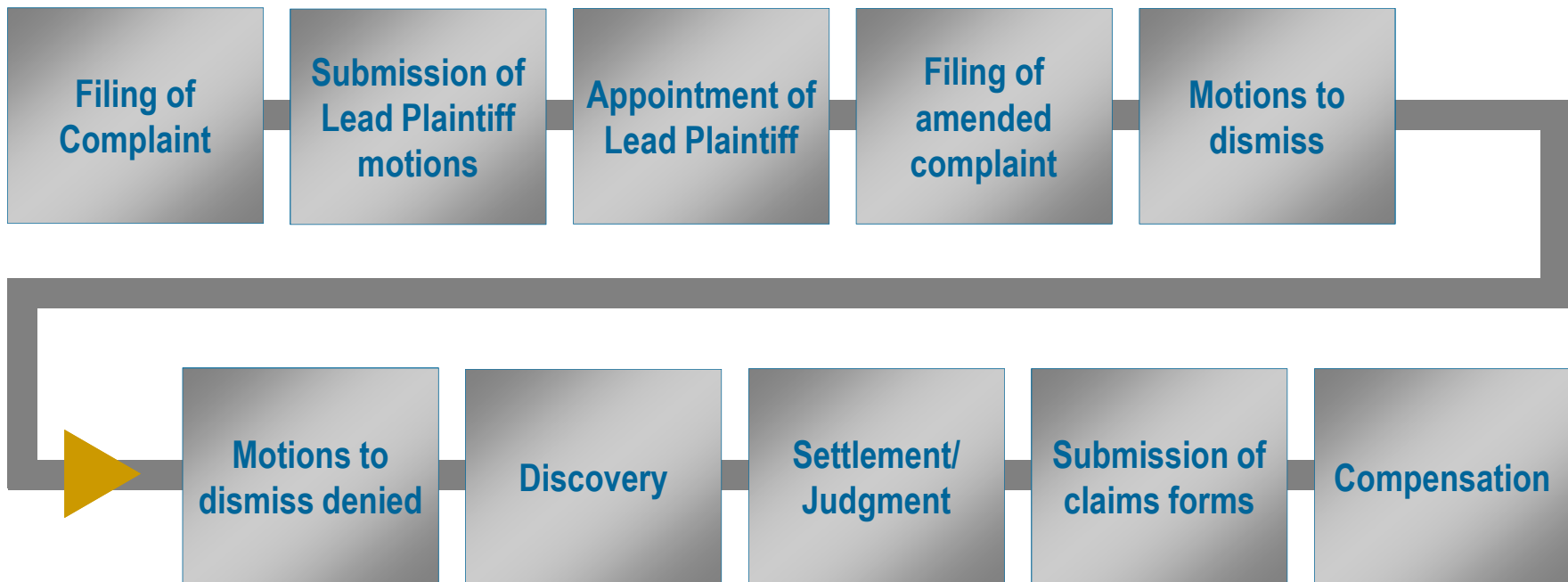
- The Amsterdam Court of Appeal ruled on 12 November 2010 that it has jurisdiction over a global settlement concerning a Swiss corporation
- The Court relied on its previous decisions in Shell and Vedior, noting that it is willing to apply its precedents consistently even to non-Dutch defendants
- Nevertheless, the Court independently found Dutch jurisdiction over non-Dutch shareholders pursuant to various versions of the EVEX Treaty
- The Court's ruling suggests that it may extend jurisdiction to cover non-consensual settlements and that jurisdiction may exist even if the class does not contain any Dutch members

# Foreign investors are members of the class, whether they know it, like it, or not

- Securities class actions affect the claims of all shareholders who purchased the defendant company's shares during the class period.
- All costs are deducted from the entire settlement amount.
- Failure to file claims is comparable to failing to cash a dividend check. In some cases, it might also be a breach of fiduciary duty.

# Stages of a Securities Class Action (10b-5 case)

**Goal: Compensation for Fraud**





# Merger & Acquisition Litigation



# Merger & Acquisition Litigation

- § Corporate directors have a duty to maximize shareholder value in the takeover context
- § Institutional investors can play a critical role, ensuring
  - § Maximum value
  - § A fair process
  - § Full and complete disclosure
- § Individual investor “Frequent Filers” underscore the importance of institutional investor involvement in this litigation

# National Home Health Care Corporation Merger Case



- § Management and private equity squeeze out of shareholders
- § Offer price too low; disclosures inadequate
- § Case resulted in additional \$ per share and disclosures

# Stages of a Merger or Takeover Action

**Goal: Improve Price and Process**





# Shareholder Derivative Litigation



# Shareholder Derivative Actions

- § Plaintiff stands in the shoes of the company and asserts its claims
- § Hold Directors and Officers personally accountable so that shareholders don't bear the costs of their wrongdoing
- § Deter and prevent future misconduct
- § Protect long-term shareholder value

# Corporate Governance Changes Achieved Through Litigation

## **ASHLAND**

Terms of the settlement of a class action lawsuit included an agreement to the following:

- Majority of the Board would be independent
- Major shareholders would solicit directors
- Senior executive bonuses would be linked to achieving agreed upon financial goals
- Company would be required to name a lead director

Source: Institutional Shareholder Services

# Corporate Governance Changes Achieved Through Litigation



Terms of the Microtune settlement included the following:

- Declassification of the Board
- Two-thirds of the Board was made independent
- All directors required to attend the Vanderbilt Directors College

Source: Institutional Shareholder Services

# Corporate Governance Changes Achieved Through Litigation



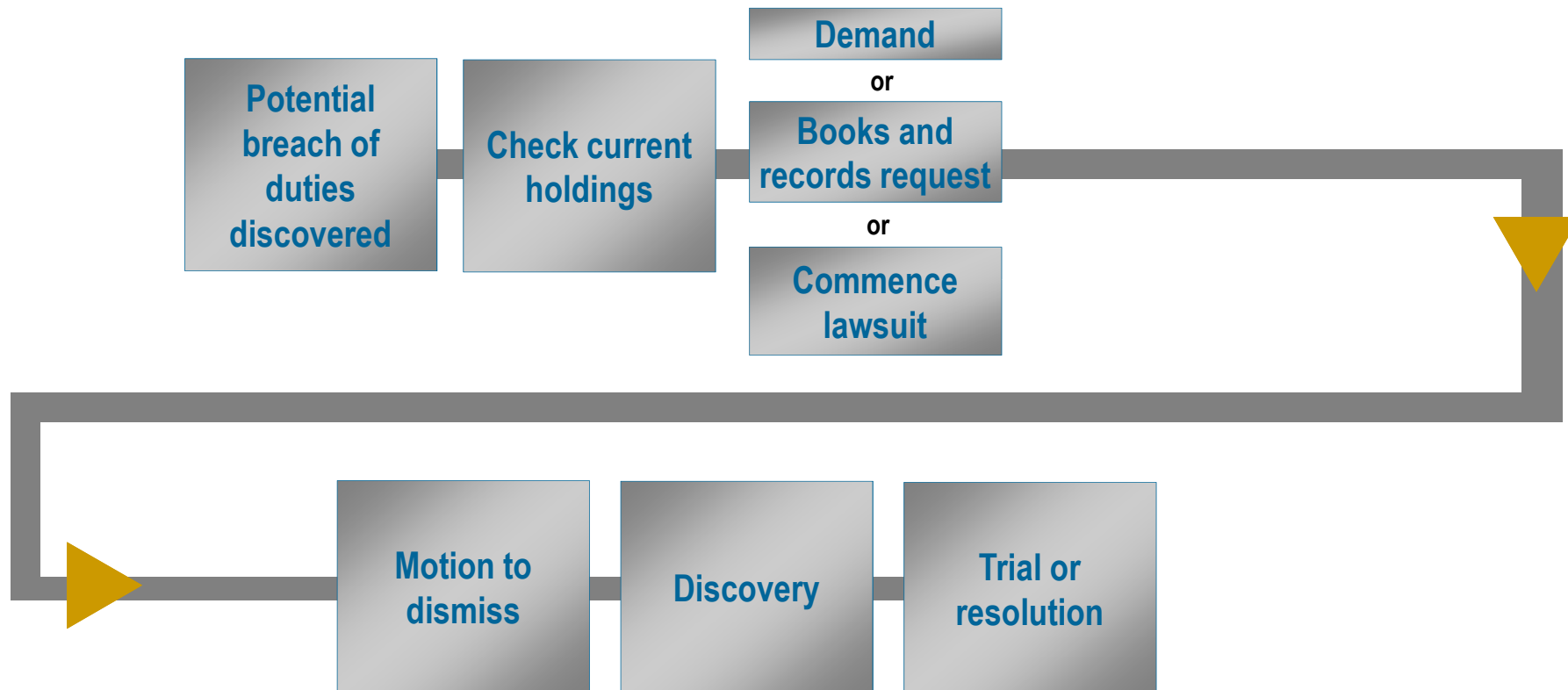
Terms of the TXU settlement included the following:

- Two board members replaced
- 70% of directors required be independent
- Company required to name a lead director
- Poison pill provision rescinded

Source: Institutional Shareholder Services

# Stages of a Derivative Case

**Goal: Corporate governance changes/restore value**





# Asset Backed Securities Litigation



# Mortgage Backed Securities

## Mortgage Backed Securities

- § Mortgage Backed Securities (“MBS”) are a type of asset-backed security and structured credit product created from a pool of 100’s or 1000’s of individual home mortgages.
- § MBS are divided by the issuer into different tranches: senior tranches (rated AAA), mezzanine tranches (AA to BB), and equity tranches (unrated). Losses are applied in reverse order of seniority and so junior tranches offer higher coupons (interest rates) to compensate for the added default risk.
- § By 2009 there was over \$14 trillion in mortgage debt outstanding with nearly \$2.5 trillion pooled into privately issued MBS.

# Collateralized Debt Obligations

## Collateralized Debt Obligations

- § Collateralized debt obligations (CDO's) are a type of asset-backed security and structured credit product created from a portfolio of fixed-income assets such as MBS.
- § Similar to MBS, CDO's are divided by the issuer into senior, mezzanine and equity tranches. Significantly, many triple-A rated CDO tranches were comprised entirely of B and lower-rated MBS.
- § Between 2004 and 2009 more than \$1.5 trillion of CDOs were underwritten and issued to the market, primarily to institutional investors. Over 50% of those CDOs were comprised of MBS.

# Asset Backed Securities Litigation

## MBS and CDO Litigation

- § When the U.S. housing market began to collapse, the value, liquidity and likelihood of future repayment of the trillions of dollars of MBS and CDOs declined significantly.
- § CDO's and MBS were marketed to institutions that relied on credit ratings similar to municipal bonds.
- § The collapse of liquidity in these products led to substantial write-downs, severe credit rating downgrades, and a loss of confidence in the validity of the process used to assign credit ratings to CDOs and MBS.

# Asset Backed Securities Litigation

## MBS and CDO Litigation Grounds for Relief

- § Breach of Contract
- § Breach of Fiduciary Duty
- § Unjust Enrichment
- § Fraud/Misrepresentation
- § U.S. Federal Securities Laws (MBS only)



# Loss Recovery & Corporate Governance Reform



# What should European institutional investors do?

European institutional investors should be familiar with U.S. securities class actions, resulting settlements, and derivative actions to act conscientiously, either:

- **as observers** – as a member of the class
- **as participants** – as a lead plaintiff acting on behalf of the class, selecting counsel, and determining the procession of the case

# What do your investors expect?

Your shareholders expect that you – as do U.S. domiciled investors – act as the fiduciary of their assets by ensuring that:

- Damages are compensated
- All available settlement funds are claimed
- Institutional minority shareholders are not disadvantaged by unfair mergers, takeovers, management-led buyouts and the like
- Improvements in Corporate Governance are achieved that reestablish a sound basis for future investment decisions

# What steps are necessary?

- Monitor your portfolio  
(Motley Rice and Sturman LLC Portfolio Monitoring Services)
  - Monthly by fax or email
  - Continually through Online-Monitoring
- Monitor ongoing cases and existing settlements
- Actively participate or observe cases in which your portfolio is significantly effected
- Proactively seek redress in the event compensable claims exist
- Proactively engage in seeking better terms or indeed to stop unfair mergers, takeovers, and management-led buyouts

# Deborah Sturman

## Sturman LLC



- § Represents European institutional investors in securities actions and advises them in connection with their Legal Portfolio Management and European plaintiffs in complex, international litigation in U.S. courts.
- § Sturman was the initiator of the first class actions in U.S. courts on behalf of victims of WWII slave labour, representing the class in In re Holocaust Victim Assets Litigation and leading to recoveries of approximately \$5 billion.
- § Sturman has been profiled in the Wall Street Journal, the Financial Times and was named runner-up Lawyer of the Year by the National Law Journal.
- § As a legal commentator, Sturman regularly appears in the German, Dutch, French, Swiss and Belgian media.
- § She is fluent in German and Dutch/Flemish and conversant in French and Italian.

# Motley Rice LLC

Motley Rice LLC is one of the largest plaintiffs' litigation firms in the U.S. The firm's attorneys gained recognition for their work on behalf of asbestos victims, the State Attorneys General in their landmark litigation against Big tobacco and the 9/11 families in their lawsuit against terrorist financiers.



The firm represents and advises victims of securities and consumer fraud, aviation disasters, human rights, occupational disease including mesothelioma, environmental contamination and defective drugs/ medical devices.

# Motley Rice and Sturman LLC

## Securities Fraud Practice

The lawyers of Motley Rice and Sturman LLC are prominent in the field of US securities litigation. They assert and defend investor rights in all matters related to US and US-related investments.

Motley Rice lawyers represent US States, pension funds and institutional investors.

Sturman LLC represents European and other non-U.S. domiciled institutional investors as well as private investors in shareholder actions in the US and in Europe.

Both firms have achieved substantial recoveries through litigation and have significantly effected US corporate governance.

# Motley Rice LLC Contact

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