



BULLETIN

A Quarterly Newsletter for Institutional Investors by Schiffrin & Barroway, LLP

DISTRICT COURT GRANTS PRELIMINARY APPROVAL OF \$1.0 BILLION SETTLEMENT IN *IN RE INITIAL PUBLIC OFFERING SECURITIES LITIGATION*; COURT PRAISES COUNSELS' EFFORTS

By John A. Kehoe, Esquire

On February 15, 2005, Schiffrin & Barroway, LLP, along with other members of Plaintiffs' Executive Committee in *In re Initial Public Offering Securities Litigation*, Master File No. 21 MC 92 (SAS), achieved a major victory in the case when United States District Judge Shira A. Scheindlin granted preliminary approval of a one billion dollar settlement guarantee. The billion dollar settlement guarantee was obtained from 298 companies (the "Issuers") and their officers and directors (the

"Individual Defendants") that conducted initial public offerings from 1998 through 2000, in mostly high tech or internet-related companies.

In recognizing counsels' effort to achieve the settlement, retired United States District Judge Nicolas H. Politan, who facilitated the settlement negotiations, wrote that the settlement "was the result of lengthy negotiations among highly experienced and competent counsel acting at arm's length," who "were well-prepared, extremely knowledgeable about the facts and the law, and advocated vigorously for their clients." Additionally, in a 52-page opinion that accompanied the preliminary approval, Judge Scheindlin wrote that the settling parties "are represented by experienced and talented counsel that share expertise in this field and an extensive knowledge of the details of this case."

The settlement agreement, if given final approval, releases the Issuers and Individual Defendants from claims that the Issuers' stock prices had been artificially inflated during and after the initial public offerings through an elaborate scheme characterized by tie-in agreements, undisclosed compensation and analyst misconduct. The Issuers and Individual Defendants are alleged to have profited from the scheme by having taken advantage of artificially inflated stock prices to raise capital, enter into stock-based transactions, and/or to sell their individual holdings at inflated prices.

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S&B UPHOLDS SHAREHOLDERS' INSPECTION RIGHTS

By *Eric L. Zagar, Esquire*

Section 220 of the Delaware General Corporation Law entitles any shareholder of a Delaware-chartered corporation to inspect the books and records of the corporation for any “proper purpose,” including investigating mismanagement and breaches of fiduciary duties by corporate officers and directors in advance of filing a shareholder derivative action on behalf of the corporation. Pursuant to Section 220, Schiffrin & Barroway, on behalf of shareholder Arthur Stein, made a demand on ITT Educational Services, Inc., a Delaware corporation headquartered in Indianapolis, Indiana, to inspect certain documents relating to ITT’s alleged falsification of student records and other corporate misconduct. ITT’s misconduct was also the subject of a federal securities fraud class action pending in the U.S. District Court for the Southern District of Indiana. ITT refused Schiffrin and Barroway’s inspection demand, and therefore, pursuant to Section 220, Schiffrin & Barroway commenced an action¹ in the Delaware Court of Chancery to enforce Mr. Stein’s inspection rights.

ITT’s response to the Delaware action was novel. In addition to filing a motion to dismiss the action in the Delaware Court of Chancery, ITT also filed a motion in the Indiana federal securities fraud action to stay the Delaware action pursuant to the Securities Litigation Uniform Standards Act of 1998 (“SLUSA”),

which provides, among other things, that “upon a proper showing,” a federal district court “may stay discovery proceedings in any private action in a State court, as necessary in aid of its jurisdiction, or to protect or effectuate its judgments.” S&B, on behalf of Mr. Stein, specially appeared in the Indiana federal securities fraud action to oppose ITT’s motion to stay the Delaware action, arguing that ITT had not made a proper showing that a stay of the Delaware action was warranted.

On February 2, 2005, Judge David Hamilton of the U.S. District Court for the Southern District of Indiana issued an Order and Opinion denying ITT’s motion to stay the Delaware action. Judge Hamilton held that “Stein’s pursuit of the Section 220 case in Delaware will not interfere at all with [the federal] court’s consideration or disposition of the consolidated federal securities fraud case, nor will it impair this court’s flexibility in managing the case or its authority to decide the case.”² Judge Hamilton further noted that “Defendants may not be happy with Stein’s and Schiffrin & Barroway’s intent to pursue derivative claims, but the PSLRA and SLUSA were not intended to protect corporate management from shareholder derivative claims.”³ Thus, Judge Hamilton concluded that the “Defendants in this case have not made ‘a proper showing’ at this point requiring a stay of Stein’s Section 220 action in the Delaware courts.”⁴

Judge Hamilton’s decision is a significant victory for shareholders and their advocates. Schiffrin & Barroway is proud to have successfully defended the ability of shareholders to use their inspection rights under Section 220 to hold corporate officers and directors accountable for their conduct. To learn more about Schiffrin & Barroway’s shareholder derivative and corporate governance practice, please contact Eric Zagar at (610) 667-7706 or ezagar@sbclasslaw.com. ■

1. *Stein v. ITT Educ. Servs., Inc.*, C.A. No. 778-N (DEL. CH. Octo. 26, 2004) *City of Austin Police Ret. System v. ITT Education Services*, No. 1: 04-ev-0380-DFH-TAB, 2005 U.S. Dist. Lexis 1646, at *18 (S.D. Ind. Feb. 2, 2005)

2. *City of Austin Police Ret. System v. ITT Education Services*, No. 1: 04-ev-0380-DFH-TAB, 2005 U.S. Dist. Lexis 1646, at *18 (S.D. Ind. Feb. 2, 2005)

3. *Id.* at *28.

4. *Id.* at *32

GOVERNMENTS AROUND THE WORLD CONSIDER AND DEVELOP FORMS OF CLASS ACTION LITIGATION

By Darren J. Check, Esquire

In a world based on mass production, mass consumption, and mass information that is connected as never before through technology, it should come as no surprise that it is more common than ever that larger groups of people and institutions are similarly damaged or injured by a particular incident or product. In the United States, class action litigation has long been a common method for aggrieved shareholders and consumers to seek redress when they have been injured in a common manner by common defendants. This type of litigation, often referred to as “group claims” or “multi-party actions” outside the U.S., has begun to develop and take hold in countries around the world, including Sweden, the Netherlands, and South Korea. While the form of each country’s class actions varies greatly, it is clear that this type of litigation will contin-

ue to expand and provide investors and consumers with an avenue to hold defendants accountable.

Below is an overview of legal systems from around the world relating to class actions. As this form of litigation develops, it will be interesting to see how the EU handles and incorporates the various forms of class litigation that its member countries adopt.

Australia

Referred to as “representative proceedings” or “group proceedings,” class actions were introduced to Australia in 1992. While still considered an emerging phenomenon, this type of litigation is becoming a more popular mechanism for resolving mass claims. Indeed, many of the class actions initiated in Australian courts mirror those that have been brought in

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CORPORATE GOVERNANCE ON THE RISE IN CLASS ACTION SETTLEMENTS

By Kay E. Sickles, Esquire

Since its inception, Schiffrin & Barroway has advanced shareholders’ interests by pioneering corporate governance reform. We have achieved this objective by obtaining settlements that reconfigure and strengthen the relationship between boards of directors and executive management to make corporate leaders more accountable to shareholders through the pursuit of derivative lawsuits on behalf of current shareholders. Through its vigorous representation, Schiffrin & Barroway has recently obtained significant reforms in a number of derivative litigations, notably, *In re Polymedica Corporation Shareholder Litigation*. In that case, the company’s Liberty Medical Supply subsidiary had engaged in improper business practices, including booking revenue for non-existent orders, and certain officers and directors had engaged in insider trading. In settlement of the derivative litigation, the company agreed to institute sweeping corporate governance changes that were targeted to remedy the shortcomings in internal controls that permitted the securities violations to occur, including a reconstituted Governance

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E-DISCOVERY MAKING LIFE EASIER FOR LITIGATORS

By Jonathan R. Cagan, Esquire

With corporate fraud reaching new levels in recent years, advances in electronic discovery are assisting plaintiffs' attorneys in sorting through a large quantity of documents produced by defendants. In just the past four years, major companies such as Tyco, WorldCom and Enron have found themselves embroiled in large, complicated alleged schemes to defraud their investors and the investing public. Securities fraud cases typically involve millions of pages of documents that represent the minutia of the fraud perpetrated by these companies and their management. As early as ten years ago, these documents would have only been produced on paper but, with the advances in software, the documents can now be managed and efficiently reviewed on computer. These advances are of great value to plaintiffs' counsel in securities fraud cases and, as corporate fraud grows larger and more complicated, electronic discovery is not only an option, but a necessity.

In the typical, large securities fraud case, the documents produced can range in volume anywhere from one million pages to tens of millions of pages. If these documents were produced on paper, one million pages would amount to approximately three hundred fifty bankers boxes of documents. Managing such a large production can be, and often is, quite cumbersome. Each document needs to be reviewed, significant facts need to be recorded, and the documents need to be organized in such a way that when important documents are needed, they can be easily found.

Electronic review in a large production of documents significantly improves the management of the documents two key ways. First, the documents can be electronically coded through a process called OCR (Optical Character Recognition) which allows specific words and phrases in a document to be

searched for in much the same way one would search the World Wide Web using search engines. There are many document management software suites that feature several layers of OCR search capability. This software reduces the clutter of irrelevant documents and allows more significant documents to be found and reviewed by an attorney. Obviously, all documents must be reviewed, but OCR search capabilities enable the reviewing attorneys to concentrate their energies on the most significant and fruitful documents in a case from the very beginning of a large review. Second, following the review of an entire production of documents in a case, the documents useful to the case are easy to find and organize. Managing a paper production is much more difficult and costly due to the sheer volume of paper that must be stored in such a way that the documents are readily accessible.

In a paper production, if a new issue arises in the case after a significant portion of the documents have already been reviewed, plaintiffs' counsel often has to start the document review process over to pinpoint that issue. Having that same production in an electronic format and in a user-friendly litigation management software suite allows much more leeway to search for significant documents pertaining to that issue. This can save countless hours and expenses. As technology rapidly evolves, large litigation management becomes essential to the successful disposition of a case. Having discovery produced electronically is not only helpful in managing an existing case but it can also be crucial to cost/benefit calculations that often control the success of large, complicated litigation. ■

BILLIONS STILL BEING LEFT ON THE TABLE: ARE PENSION FUNDS A FUTURE TARGET OF LAWSUITS?

By Nicholas S. Pullen, Esquire

In January 2005, over 40 mutual fund managers were sued by investors in those funds alleging that the funds failed to collect as much as \$2 billion in settlement payouts. The thrust of these suits was that the defendant mutual funds breached their fiduciary duty to their investors by failing to file claim forms in connection with class action settlements. While it does not appear that any court has addressed this threshold issue of whether an institutional investor owes a fiduciary duty to file claim forms, it is clearly well established that officers and directors of a corporation owe a duty to shareholders to protect the corporation's assets. As such, it is possible that a mutual fund may have such an obligation to its investors to collect money from settlements of securities class actions. In fact, in an upcoming article by Professors James D. Cox and Randall S. Thomas,¹ they argue that institutional investors have a clear legal duty to file claims in securities fraud class action settlements. This view derives from the *Caremark Derivative Litigation*, where the Delaware Chancery Court ruled that a board of directors had a duty to monitor whether the corporation was operating within the boundaries of the law to accomplish its purposes. Specifically, Chancellor Allen wrote that directors had a duty to make "a good faith judgment that the corporation's information will come to its attention in a timely manner as a matter of ordinary operations."² If a corporation failed to make this good faith judgment, a corporation could be "liable for losses caused by non-compliance with applicable legal standards."³ Under this theory, institutional investors could face liability if they fail to have an adequate system in place to file claim forms.

While some of these mutual funds did, in fact, file claims in settlements, which resulted in the dismissal of the complaint against particular funds, many apparently did not. The mutual fund industry is not alone in failing to file such claim forms. In fact, Professors Cox and Thomas found that only 28% of institutional investors surveyed actually filed claims in class action settlements. This number is appallingly low considering that in 2004, securities fraud class action settlements produced \$5.45 billion in cash to be distributed to defrauded investors. As a result of institutional investors' failure to file claim forms, they are leaving anywhere from

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S&B'S ERISA DEPARTMENT TAKING PROMINENT ROLE

By Edward W. Ciolko, Esquire

Schiffirin & Barroway's ERISA Litigation Department is nationally recognized and has been a leader in prosecuting claims on behalf of the nation's employees whose defined contribution plan (often referred to as 401(k) plan) retirement savings were imprudently invested in employer securities. These actions, brought under the Employee Retirement Income Security Act of 1974 ("ERISA") against persons charged with administering the 401(k) plans ("fiduciaries"), have grabbed headlines in the wake of corporate scandals at Wall Street high fliers such as Enron and Global Crossing where the companies' 401(k) plans maintained heavy investments in company stock. B investments decimated when details of widespread corporate malfeasance came to light.

While prosecuting dozens of other cases as lead or co-lead counsel on behalf of 401(k) plans and their participants, Schiffirin & Barroway recently (1) negotiated a settlement in principle of ERISA claims brought on behalf of participants in pension plans sponsored by Honeywell International, Inc. ("Honeywell") and (2) earned a landmark decision defeating defendants' motion to dismiss ERISA claims against UnumProvident Corporation ("UnumProvident") and other fiduciaries of the UnumProvident 401(k) Retirement Plan. This decision made clear that defendants could not use the federal securities laws as a shield from liability for breaches of fiduciary duty under ERISA.

Schiffirin & Barroway is serving as Lead Counsel in a breach of fiduciary duty case under ERISA against Honeywell and certain fiduciaries of Honeywell's defined contribution plans. The suit alleges that Honeywell and the individual fiduciary defendants allowed Honeywell's 401(k) plans and their participants to imprudently invest significant assets in company stock despite that defendants knew or should have known that Honeywell's stock price was an imprudent investment due to undisclosed, wide-ranging problems stemming from a consummated merger with Allied Signal and a failed merger with General Electric. A settlement of plaintiffs' claims, which includes a \$14 million payment to the plans and their affected participants and significant structural relief affording participants much greater leeway in diversifying their retirement savings portfolios, is currently pending court approval.

In a similar case brought against UnumProvident and other individual fiduciaries of the company's 401(k) plan where Schiffirin & Barroway served as Lead Counsel, Judge Curtis Collier of the United States District Court for the Eastern District of Tennessee recently denied defendants' motion

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DISTRICT COURT GRANTS PRELIMINARY APPROVAL *(Continued from page 1)*

Under the terms of the settlement, insurers for the Issuers and Individual Defendants have agreed to provide an undertaking to guarantee that the settling class will recover at least one billion dollars. Specifically, the insurers have agreed to pay the settling class one billion dollars less the total of all plaintiffs' recoveries from the Underwriter Defendants in (i) the consolidated securities cases, (ii) the IPO antitrust litigation, and (iii) the Issuers' "excess compensation" claims which are assigned to the settlement class as part of the settlement agreement. The Issuers also agreed to pay up to \$15 million in costs related to giving notice of the proposed settlement to the settlement class.

Schiffirin and Barroway, along with the Plaintiffs' Executive Committee, continues to prosecute claims against the fifty-five Underwriter Defendants that underwrote the Issuers' initial public offerings. The Underwriters are alleged to have conditioned IPO allocations upon a requirement that certain customers agree to purchase, in the aftermarket, additional shares of stocks in which they received allocations, and, in some instances, to make the additional purchases at prearranged, escalating prices ("Tie-in Agreements"). The Tie-in Agreements created an artificial demand for aftermarket shares, thereby causing the stock price to artificially escalate as soon as the shares were publicly traded. The Underwriter Defendants are also alleged to have sought, as part of their manipulative scheme, to further enrich themselves by improperly sharing in the profits earned by certain customers in connection with the purchase and sale of the Issuers' securities.

In addition to the one billion dollar payment guarantee, the settlement agreement requires the Issuers to assign certain claims they may have against the Underwriters in connection with the offering prices and for the Issuers and Individual Defendants to provide "such reasonable cooperation as they and Plaintiffs' Executive Committee agree is appropriate and necessary to provide, in an efficient and reasonable manner, further information concerning the claims in the Complaints [against the Underwriter Defendants]. . . ."

In commenting on the value of the cooperation, Judge Scheindlin wrote that:

Despite the apparent magnitude of the billion dollar guarantee, this settlement is not solely — or even primarily — about monetary recovery. . . . [T]he value of 298 willing allies in litigation, as opposed to the specter of hundreds of uncooperative opponents, is significant. The Issuers know far better than the plaintiff classes precisely what occurred in the period leading up to and including their IPOs, and their willingness to open their files and aid plaintiffs in amassing evidence against the Underwriters may ease the plaintiffs' discovery burden enormously.

In re IPO Sec. Litigation, 226 F.R.D. 186, 198 (S.D.N.Y. 2005) (footnotes omitted)

The Underwriter Defendants vigorously opposed the settlement agreement, and argued that the terms encourage "collusion" between the plaintiffs and the Issuers that would "distort the fact-finding process" and "preclude a fair determination of the Underwriter Defendants' percentage of responsibility for any damages awarded in any IPO trial." They also argued that the "sliding-scale nature" of the billion dollar payment guarantee would provide an improper incentive for the Issuers to implicate the Underwriters and thereby reduce the Issuers' payment guarantee. Judge Scheindlin found that the Underwriters' arguments lacked merit, and wrote that the financial motive decried by the Underwriters "is always present in a multi-defendant case" and that "it is common practice for defendants to point the finger at each other and to minimize their own misconduct."

The Court is still in the process of scheduling a hearing to make final determinations regarding the form, substance and program to notify class members of the preliminary settlement, and to schedule a Rule 23 fairness hearing, which is a necessary step before granting final settlement approval. ■

For more detail on the settlement and up-to-date status on the IPO Litigation, you can contact the firm directly or visit the IPO Securities Litigation website at www.iposecuritieslitigation.com.

GOVERNMENTS AROUND THE WORLD CONSIDER AND DEVELOP FORMS *(Continued from page 3)*

the United States regarding securities, tobacco, pharmaceutical liability, asbestos-related injuries and civil rights. Many of the prerequisites and procedures for a group proceeding in Australia are identical to those in the U.S. such as numerosity of claimants, commonality of claims, and allowing a representative to serve on behalf of many. However, unlike in the United States, in many European countries the losing party in the litigation still has to pay for litigation costs, thereby serving as a significant disincentive for filing actions.

France

Just this past year, France began contemplating legislation that will allow class-action lawsuits to proceed in French courts. France's President, Jacques Chirac, has requested that the country's finance minister, justice minister, and commerce minister promulgate a new law that will permit group actions. While a proposed law of this sort has been met with trepidation by French businesses and the legal community, many consumer and shareholder advocates support this legislation as a response to several scandals that have shaken consumer and investor confidence in France.

Germany

Reports indicate that the German government is considering an American style of class actions in response to a growing number of corporate frauds. In particular, recent litigation against Deutsche Telekom AG ("DT") has forced consideration of a system that would simplify claims brought by large groups of similarly situated plaintiffs. In that case, some 15,000 individual claims were filed with a court in Frankfurt causing an unprecedented logjam of cases. Each claim alleges that DT, Europe's biggest phone company, inflated the value of its assets prior to a large offering in 2000. Because German law requires that each case be litigated separately, claims of this type, which are becoming more commonplace, will need to be managed more effectively.

Italy

The Italian parliament is currently contemplating the enactment of a bill that would introduce consumer class actions into the Italian legal system. This draft bill, approved by the Camera dei Deputati, or Chamber of Deputies, in July 2004 and which now is under consideration by the Italian Senate, allows for a class action to be initiated for damages caused to consumers (including investors) by an unlawful act committed in relation to a contractual relationship. The new law, however, would not allow individuals to sue; rather, associations of consumers, investors or professionals will need to bring such an action in the interest of all those damaged by the same unlawful act. Notably, the mechanics for such actions have not been established and it may be some time before this law takes effect.

The Netherlands

Change is in the air for Dutch class actions. The country's Parliament may soon enact a new law which would resemble the U.S. system of class actions. Interestingly, it is Dutch businesses that lobbied for this change in an effort to simplify both the settlement process and the litigation. Currently, class actions are led by a representative of the class, but settlements are not binding on the entire class as individual plaintiffs may continue to litigate their claims despite a settlement. This new law would make a settlement binding for all members of a class who do not specifically opt out or exclude themselves from a settlement. Defendants and their insurers will be more inclined to enter into class-wide settlements and the process as a whole will prove to be much less cumbersome. The law will apply not only to Dutch citizens, but also to those in the EU who do business with a company in the Netherlands or one that has Dutch interests. The proposed law, which has been approved by the Parliament's second chamber, is now under review by the first chamber. If approved, it will become law and will be known as the Collective Unwinding of Mass Claims Act.

South Korea

In December 2003, following years of debate, South Korea passed a bill establishing a private securities class action system that was enacted in January, 2005. Initially, the bill allows for Korean class actions to be brought only against companies with assets of more than 2 trillion won (or just under \$2 billion) which includes approximately 80 of the 1500 publicly traded companies in South Korea. Starting in July 2007, this restriction will be lifted and similar suits may be brought against smaller companies. Another interesting wrinkle in the law is that an action may only be brought if more than 50 shareholders, owning at least 0.01% of the outstanding shares of the company, agree to bring the case. Many shareholder rights' advocates see the law as having too many hurdles to overcome to be truly beneficial, but with reports of the first Korean class action being filed in April 2005, it will be interesting to see how the law develops.

Sweden

On January 1, 2003, the Group Proceedings Act came into force in Sweden. Commonly referred to as "group actions," they are very similar to the United States' class actions in that (i) they intend to cover groups of plaintiffs that have been similarly affected by some act; (ii) there must be a representative of the group; (iii) it must be the most appropriate type of litigation for the particular claim; and (iv) it may be brought by any member of the group that is intended to be represented. A few interesting differences from the United States' system of class action litigation are apparent, however,

relating to how one becomes a member of the class and who pays for the cost of the litigation. In a Swedish group action, the group members are notified of the action before litigation begins and they must notify the court of their intention to participate as a member of the group. In a sense they must "opt-in" at the beginning of a case. In addition, as is the case in many European courts, when it comes to the cost of the litigation, the loser pays the costs. These two key differences may explain why, according to a recent article in the Swedish law journal *Svensk Juristtidning*, only five group actions have so far been filed. ■

Special thanks to Noah R. Wortman for his help in researching this article.

CORPORATE GOVERNANCE ON THE RISE IN CLASS ACTION SETTLEMENTS (Continued from page 3)

Committee on its Board of Directors, which now consists solely of outside directors, retaining a special regulatory counsel charged with strengthening and auditing Liberty's compliance with internal policies and procedures, and the mandatory reporting of trades in company stock by high-level executives.

Recognizing the significance of corporate governance in the perpetuation of securities fraud, Schiffrin & Barroway is advising its clients in its securities fraud litigations that obtaining the largest financial compensation possible for the shareholders who have been damaged by a corporation's violations of the federal securities laws is not always a singular goal. Schiffrin & Barroway believes that interested and reform-minded shareholders, especially institutional investors that wield substantial influence, can help get to the root of the problems that underlie securities violations — lack of internal controls or interdependent boards of directors and executive management — by obtaining corporate governance reforms as part and parcel of financial settlements in securities class actions under the right circumstances. This approach may avert future indiscretions by company management and therefore enhance shareholder value. Studies have demonstrated that the best corporate practices promote confidence by the investing and funding communities, command a premium share price, and reduce the cost of capital. In addition, obtaining both types of remedies in the settlement of one litigation can promote efficiency in the litigation context, permit companies to dispose of two potential litigations in one settlement, saving time and resources for the company, and can serve to protect current shareholder value. This approach can also save significant administrative expenses such as notice in the settlement context, thereby leaving a greater fund to be divided among the damaged shareholders.

While securities class action settlements which provide both financial compensation and corporate governance are currently in the minority, a growing number of settlements provide both, as illustrated in NERA Economic Consulting's recent article, "Recent Trends in Shareholder Class Action Litigation: Bear Market Cases Bring Big Settlements" (February 14, 2005). In that article, from which the below chart is reproduced, the authors highlight the growing interest in combined settlements. For instance, in 2004, the securities class action, derivative action and ERISA 401(k) litigation arising out of misrepresentations and omissions by the Hanover Compressor Corporation were resolved in one settlement. In that settlement, in which Schiffrin & Barroway represented the class members in the ERISA 401(k) action, monetary and corporate governance relief, including \$29,500,000 in cash, 5,000,000 shares of Hanover common stock and a note in the amount of \$6,650,000, and the appointment of two new directors and enhanced independence requirements for the board of directors, was obtained. Similarly, in *In re Honeywell International Inc. Securities Litigation*, where plaintiffs alleged that Honeywell had made misrepresentations and omissions concerning its merger with Allied Signal, monetary relief of \$100,000,000 as well as corporate governance relief, including new guidelines concerning compensation for the officers and directors, was obtained. Schiffrin & Barroway is at the forefront of these types of global resolution, which we believe will soon become the settlement strategy preferred by large, interested shareholders, with a view towards enhancing shareholder value not just currently, but for years after the settlement papers are signed. ■

Federal Court Securities Class Action Settlements Involving Corporate Governance Changes*

Chart Reprinted with permission of NERA Economic Consulting

Company	Approx. Settlement Date	Settlement Description	Corporate Governance Reforms
AON Corporation	06/04	\$7.25 million	<ul style="list-style-type: none"> • Certain corporate governance procedures were agreed to, but not disclosed
Enterasys Networks, Inc.	12/03	\$17 million plus \$33 million of stock	<ul style="list-style-type: none"> • Requires disclosure of membership of board of directors • Limits terms of directors to one year • Shareholders may recommend directors annually • Expands proxy statement disclosures
Hanover Compressor Co.	01/04	\$80 million (partial settlement)	<ul style="list-style-type: none"> • Requires rotation of outside audit firm • Places restrictions on insider stock sales
HCA Inc.	01/04	\$50 million	<ul style="list-style-type: none"> • Requires independence of two-thirds of HCA's board • Calls for two audit committee members to have accounting/financial experience • Requires rotation of outside audit firm (every seven years)
Homestore.com, Inc.	12/03	\$13 million plus \$59 million of stock	<ul style="list-style-type: none"> • Adds requirements for independent directors and special committees • Requires disclosure of membership of board of directors • Limits terms of directors to two years • Shareholders may appoint new director • Prohibits future use of stock options for director compensation • Requires minimum stock retention by officers after options exercise
Honeywell Inc.	06/04	\$100 million	<ul style="list-style-type: none"> • Ensures independence of outside auditors and board of directors • Adopts provisions relating to compensation of officers and directors, and the performance of internal audits
Ingersoll-Rand Company	12/02	No financial payment (reorganization/reforms only)	<ul style="list-style-type: none"> • Must show employee/directors receive no grant of benefits in the reorganization plan • Shareholders may revoke voting agreement • Restricts certain corporate transactions
Mattel Inc.**	12/02	\$122 million	<ul style="list-style-type: none"> • Certain corporate governance procedures were agreed to, but not disclosed
Sprint Corporation	12/03	\$50 million	<ul style="list-style-type: none"> • Established role of lead independence director • Caps all payments to board members and their families at \$45,000 • Sets \$200,000 limit on payments to organizations linked to directors • Prohibits executives from selling shares while the company is buying its own stock • Shortens directors' terms to one year from three years

* Data obtained from NERA's proprietary database of class action lawsuits, in conjunction with Securities Class Action Alert and Factiva News Searches.

** See Associated Press Newswire article published December 5, 2002.

BILLIONS STILL BEING LEFT ON THE TABLE (Continued from page 5)

\$1 to \$2 billion on the table in unclaimed settlement monies. Institutional investors' failure to file claim forms also leads to a financial windfall for those fiduciaries that do file claim forms. Since settlements are distributed in a prorata share to the proportion of losses suffered, institutional investors are awarded additional monies when they file their claim forms due to the high proportion of institutions that do not file claim forms. Fiduciaries such as the State of Wisconsin Investment Board have boasted that they recover approximately \$7 million a year in class action settlement money.

In response to this increasing problem, Schiffrin & Barroway, LLP offers a free full service portfolio-monitoring program that will track every class action settlement in which an institutional investor may have an interest. For more information about our portfolio monitoring services, please contact Darren Check, Esquire at (610) 822-2235. ■

1. *Letting Billions Slip Through Your Fingers: Empirical Evidence and Legal Implications of the Failure of Financial Institutions to Participate in Securities Class Action Settlements.* (Unpublished)
2. *In re Caremark International Inc. Derivative Litigation*, 698 A2d 959, 970 (Del. Ch. 1996).
3. *Id.*

S&B'S ERISA DEPARTMENT TAKING PROMINENT ROLE (Continued from page 6)

to dismiss plaintiffs' complaint *in toto*. Most significantly, the Court rejected — in the strongest possible terms — a frequently utilized argument by defendants in these types of breach of fiduciary duty cases. Essentially, the defendant-fiduciaries argued that, even assuming they were in possession of non-public information regarding the imprudence of plan investments in UnumProvident stock, the federal securities laws' prohibitions on "insider trading" precluded fiduciaries from taking any ameliorative actions regarding the plan's heavy investment in UnumProvident equity. After an exhaustive review of relevant case law and statutory provisions, the Court repudiated defendants' logic and its sparse supporting precedent, stating, in relevant part:

"Were the Court to accept Defendants argument, it would be holding, as a matter of law, plan participants and beneficiaries have no cause of action under ERISA against plan fiduciaries who possess actual knowledge of information that calls into question the prudence of a significant plan investment and would be of immense benefit to participants and beneficiar-

ies, but keep that information to themselves knowing the participants and beneficiaries have no other means of access to the information and the participants and beneficiaries suffer losses as a result. Such a result would be plainly inconsistent with the very purposes of ERISA (i.e., encouraging employers to offer ERISA benefits and protecting participants and beneficiaries). That one particular method of complying with their fiduciary obligations under ERISA might have also subjected Defendants to liability for insider trading is not sufficient to negate those fiduciary obligations entirely. ERISA, at least in this context, and the federal securities laws share a common goal: disclosure of material financial information. The fact Defendants may have been subject to both disclosure obligations in this case cannot possibly excuse their failure to comply with either." ■

Gee v. UnumProvident Corp., No. 1:03-CV-147, 2005 U.S. Dist. LEXIS 3183, *42-43 (E.D. Tenn. Jan. 14, 2005).

TRENDS IN CLASS ACTION LITIGATION 2004: THE NUMBERS ARE NOW IN

By Roy Jones

Securities class actions in 2004

The numbers are now in regarding the final 2004 figures covering the number of securities class actions, average investor losses per case, and details about the size and form of settlements. And what a year it was — with all of the indicators pointing to no letup in U.S. corporate malfeasance and fraud — raising serious doubts about the reach and bite of the Sarbanes Oxley act, and other regulatory measures in curbing executive excesses. However, those who like to point the finger at U.S. executives as being hard wired for fraud and malfeasance should be cautious: research shows that the number of class action law suits filed against foreign companies has more than trebled since 1996 to reach 29 in 2004, the highest number ever filed in a single year. It's clear that bear market or bull market, institutional investors everywhere must continue to be on their guard and cannot afford to be complacent.

Number of cases: In 2004, 217 cases were filed. The benchmark for judging trends in the number of cases filed is the passage of the 1995 Private Securities Litigation Reform Act (PSLRA). Immediately following the passage of the PSLRA, the number of cases filed in 1996 (110) was entirely in line with the previous long run average. That figure then shot up to 268 in 1998, and has since settled to yield an annual average of 212 cases per year for the post-PSLRA period. It's worth reflecting on the background atmospherics to this. Contrary to popular perception, the PSLRA actually limited the ability of aggrieved investors to bring forward cases — the only good news was the “lead plaintiff” provision that gave rise to the expectation that institutional investors would become lead plaintiff. Having said that, the intention there was not to bring some stability to the system, rather the hope was that institutional investors would not take up the baton as lead plaintiff. But as we report elsewhere, the

institutions are stepping forward in ever increasing numbers, and from beyond the U.S. shores. In addition, we were told that the passing of the Sarbanes Oxley Act would put a floor under the number of case files and then dramatically reduce them. Clearly, the effect has yet to be seen.

Trends in investor losses — and recoveries

Institutional investors often believe that investor losses in securities class actions are relatively small. Well, the figures for 2004 and the longer-term trends should give pause for thought. Turning first to the short-term, we find that of those cases settled in 2004, median investor losses rose to \$340 million, up from \$215 million in 2003. As regards longer-term trends, the median investor loss in 2004 was five times higher than that of 1996, the year when the PSLRA made its debut, and which commentators usually use as the base year.

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TRENDS IN CLASS ACTION LITIGATION 2004

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On the other side of the equation, settlements took a quantum leap upwards in 2004. The total value of all settlements was a staggering \$5.5 billion, which should be set against the 2001 figure of \$1.9 billion. Even more startling, the data shows that over \$4 billion has been recovered in the first quarter of 2005 alone. It looks like 2005 as a whole will be a record breaker for settlements. Turning to the averages, 2004 mean settlements shot up to reach \$27.1 million. That was a 33% increase on the 2003 average settlement of \$23.2 million — itself a 20% increase on the previous year. Reflecting again on the longer term trends, investors should take note that prior to 1996 average settlements were running at \$5.0 million.

Within the averages lies the trend to larger individual settlements on a case-by-case basis. In 2003, 23 settlements were valued in excess of \$20 million, with 6 settlements exceeding \$100 million. Again these figures rose over the preceding year. Through 2004 nine settlements reached values of \$100 million or more. Moreover, and as the data shows, the headline grabbing cases do not explain the increase in average settlements — it is a trend in itself. The explanations are not hard to find. On the one hand, investor losses per case have increased, and on the other hand, the preparedness of institutional investors to become lead plaintiff has also increased, and where this is the case, average settlements are typically one-third higher.

Individual executives now paying out of their own pockets

At first we thought it was an aberration, but the back-on agreement where former WorldCom directors will stump up millions of dollars out of their own, admittedly deep pockets, appears to have cemented in place a new trend. Before looking more deeply at the WorldCom deal, let's spend a moment looking at other similar settlements. In January 2005, eighteen former non-executive directors of Enron agreed to settle one of the many cases brought by investors following the collapse of the company in 2001. The difference is that ten of those directors agreed to pay \$13 million out of their own pockets. That came on top of a 2004 settlement where a dozen former Enron directors agreed to pay \$1.5 million of their own money as well as over \$85 million in insurance proceeds to settle liability in a case brought on behalf of former employees.

Now, back to the WorldCom deal. This arose due to the dogged determination of Alan Hevesi, the comptroller of New York state, and trustee of the state's Common Retirement Fund, who is also the lead plaintiff. It was he who early on stated he would require the culpable directors to be made an example of. He, like us, was probably bothered by the way in which executives guilty of malfeasance and fraud escape personal liability, with liability insurance picking up the tab. We believe that escape route is a moral hazard as it builds in a perverse incentive for fraud — a kind of heads we win, tails you lose scenario.

A first settlement was announced in January this year, ironically where each of the ten former non-executive directors would pay \$18 million of their own money — an estimated 20% of their net combined wealth — to settle a \$54 million class action. That deal was scrapped when the presiding judge ruled that part of it was illegal, as it would have limited the directors' personal liability and exposed other defendants to larger damages. However, after the related settlement with JP Morgan Chase and the rest of the banks involved in the case settled, the negotiations were back on track. This time though, the individual settlements have been pushed up by an extra \$2 mil-

lion. And further food for thought — should the settlement be approved by the court, it will push the total amount recovered from WorldCom defendants to \$6.06 billion. Insurance companies will only pay out \$35 million under the terms of the settlement.

Securities class actions secure — not cost jobs

Many trade unions and some institutional investors cite the negative impact that a securities class action can have on the future of the company and its workers as a reason for non-participation. It's time to put that fear to rest. Only four out of a total of 172 cases (two per cent) were filed as a result of bankruptcies in 2004, and there were no bankruptcy filings following the filing of a class action. This is an important development. Securities class actions do not now damage the future of the company, or the interests of workers by pushing the affected company into bankruptcy. That fear has been lifted. Furthermore, Schiffrin and Barroway has a proud record of working with our clients to ensure that we build all of their interests into the class actions that we are engaged in. For example, and readers can find more details of this on our web site, we acted upon our clients' instructions in the AremisSoft case to rescue the company, and it emerged from bankruptcy as a new entity, with secured employment. As a sign of the faith that we had in our approach we were awarded the same proportion of stock and cash as our attorneys' fees. Both are doing well in the recovery phase.

Securities class actions “go global” in a big way

“In 2004 securities litigation went global in a big way.” That is a major conclusion of the 2004 PricewaterhouseCoopers (PwC) Securities Litigation Study (www.10b5.com). The study goes on to reveal that since 1996, the number of class action law suits filed against foreign companies has more than trebled from 9 to reach 29 in 2004, the highest number ever filed in a single year. That figure, an amazing 70% increase on 2003 is now in proportion to the number of foreign companies listed on U.S.

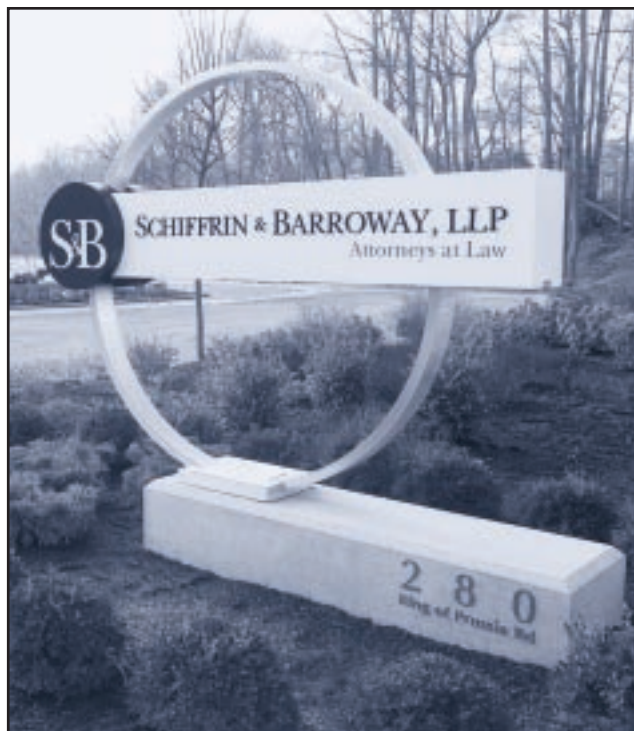
securities exchanges, a significant trend. A breakdown of the data gives substance to the sound bite: companies affected come from China, Mexico and Canada, in addition to a host of European countries. What is more — the worst excesses of corporate greed are not confined to the U.S. — a claim often made by foreign commentators in defense of their national champions. Indeed, 22 of these 29 cases involved financial fraud and accounting irregularities. And to put it truly into perspective, as the study notes “the financial fraud at Parmalat (Italy) is bigger than the combined financial frauds at WorldCom and Enron.” And as to the future? PwC pretty much sum it up with “Expect more securities litigation *sound and fury* — on a global basis — next year.”

Institutional investors increasingly demand lead plaintiff status

The oil tanker has turned — a fitting metaphor for the way in which institutional investors have changed tack, and are now increasingly demanding the role of lead plaintiff in securities class actions. PwC researchers have crunched the numbers, and for the first six months of 2004, institutional investors and union and public pension funds together comprised 47% of lead plaintiffs, compared to 41% in 2003. Correspondingly, the percentage of cases with private investors as lead plaintiff fell to 35% in 2004, from 49 in 2003. In terms of hard numbers, we see that cases filed with institutional investors such as union and public pension funds as lead plaintiff stand to reach a record breaking 69 for 2004. By any account, that is a dramatic increase on the recorded five and six for 1996 and 97 respectively. We welcome this, and our expectation is that just as once an oil tanker has changed direction it stays on that course, then institutional investors too will remain on track. ■



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