

Bulletin

A Quarterly
Newsletter for
Institutional Investors
by Barroway Topaz
Kessler Meltzer & Check, LLP

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BARROWAYTOPAZ
KESSLERMELTZERCHECK LLP

Attorneys at Law

280 King of Prussia Road, Radnor, PA 19087
610-667-7706 • Fax: 610-667-7056

580 California Street, Suite 1750, San Francisco, CA 94104
415-400-3000 • Fax: 415-400-3001

Barroway Topaz Litigators Obtain Historic Jury Verdict in First Credit Crisis Securities Fraud Trial

Andrew L. Zivitz, Esquire, Matthew L. Mustokoff, Esquire and John Gross, Esquire

On November 18, 2010, a nine-person Miami jury returned a historic verdict of federal securities fraud against Florida-based BankAtlantic Bancorp, its chief executive officer and chief financial officer. The jury found that these defendants misled investors when the bank issued false statements concerning its commercial real estate “land loan” portfolio, and that these public misrepresentations cost investors millions of dollars in market losses. This case marks the first class action lawsuit against a financial institution arising out of the credit crisis to be tried to verdict.

After three years of litigation, five weeks of trial and three days of deliberation, the jury

handed down an award of \$2.41 per share of BankAtlantic common stock purchased during the class period — a number that represents the inflation in the security’s price as a result of the stock fraud. Depending on the number of claims filed by class members, this verdict could result in a recovery of tens of millions of dollars for BankAtlantic shareholders.

Barroway Topaz partners Andrew Zivitz and Matthew Mustokoff and associate Mark Danek, representing plaintiff Erie County Employees Retirement System, served as co-lead trial counsel to the class throughout the litigation which began in the early days of the

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A Brand New Day? The Dodd-Frank Wall Street Reform and Consumer Protection Act’s Impact on Investors

Naumon A. Amjed, Esquire and Joshua E. D’Ancona, Esquire

The near collapse of the financial markets in late-2008 led Congress to pass the “Dodd-Frank Wall Street Reform and Consumer Protection Act” (hereinafter the “Act”).¹ The most sweeping financial reform bill in decades, the Act regulates multiple sectors of the U.S. economy and is likely to have a significant impact on many investors.² The Act was passed over fierce industry lobbying and partisan politics, with almost all Republican members of Congress voting against the measure. It was signed into law by President Obama on July 21, 2010. The Act’s full implementation — already underway — will take several years.

¹ 124 Stat. 1822, Pub. L. 111-203 (Jul. 21, 2010) (“Act”).

² The Act’s preamble states that its purpose is to “promote the financial stability of the United States by improving accountability and transparency in the financial system, to end ‘too big to fail,’ to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices, and for other purposes.” Act, Preamble.

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GUEST AUTHOR ARTICLE

Analyzing Litigation in Mergers and Acquisitions

Professor Randall Thomas



Randall Thomas has earned a reputation of being one of the most productive and thoughtful corporate and securities law scholars in the nation. His recent work addresses issues such as hedge fund shareholder activism, executive compensation, corporate voting, corporate litigation and the structure of firms. He joined the Vanderbilt law faculty in 2000 to develop and direct the Law & Business Program, having served previously on the law faculties of the University of Iowa, the University of Michigan, Duke University, Boston University, and the University of Washington. Prior to teaching law, Professor Thomas was in private practice for four years, and clerked for U.S. District Judge Charles Joiner of the Eastern District of Michigan. An acclaimed teacher, Professor Thomas teaches courses in the area of corporate law, including corporations and securities regulation and directs the law school's LL.M. program.

On December 7, 2010, my colleagues, C.N.V. Krishnan, Ronald W. Masulis, and Robert B. Thompson[†] and I published a report analyzing patterns and trends in litigation relating to corporate merger or acquisition (M&A). Our analysis, covering a sample period of 1999–2000, yielded several notable points, some of which are summarized in this brief article. The full report is available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1722227.

Generally, our report documents the types of suits triggered by M&A offers, the factors that influence whether offers are followed by litigation, the impact of M&A lawsuits on the transaction (offer completion rates and takeover premium in completed deals), and the factors that influence whether such suits settle for monetary damages. On a macro level, our analysis found that 12% of M&A offers announced during our sample period were followed by litigation. The lion's share of this litigation was initiated by shareholders. Our analysis of the circumstances leading to M&A related lawsuits allows us to report the following general trends:

- (a) actions filed in federal court, though far fewer than state court actions, attract a significantly higher proportion of bidder and target initiated litigation than state actions;
- (b) bidder and target lawsuits have significantly lower rates of settlement than other types of lawsuits. Within this category, lawsuits involving target corporations have lower completion rates, but result in higher takeover premiums if completed. One reason for this may be that managers in the target corporation typically want to either kill the deal as originally proposed or obtain a higher premium, which will lead to both a lower completion rate and a higher average premium in completed deals;
- (c) offer completion rates are the highest for controlling shareholder squeeze-out offers relative to other M&A offer types. This is not surprising given that a controlling

shareholder can unilaterally insure that a deal is completed, simply by having a target board of directors propose a merger transaction and then voting its controlling share interest in favor of the transaction; and

(d) after controlling for offer features and M&A financial and legal advisor reputation, industry and time fixed effects, as well as for selection bias, that offers subject to lawsuits are completed at a significantly lower rate than offers that are not subject to litigation. However, contested transactions are also associated with a significant increase in takeover premiums for completed deals.

Turning to the characteristics of transactions that are followed by litigation, our analysis suggests that larger offers (that involve larger sums of money and therefore higher potential damages for plaintiffs), hostile offers (that raise potential board entrenchment motives), offers with target termination fee provisions (that can result in challenges to the size of breakup fees), offers with a higher percentage of cash financing (that trigger strict *Revlon*¹ duties for target company boards of directors), and controlling shareholder squeeze-outs (where concentrated shareholders try to influence deal terms in their favor) are more likely to be followed by litigation than M&A transactions lacking one of the aforementioned factors.

As noted above, litigation initiated by shareholders accounts for the vast majority of lawsuits in our sample. This observation is consistent with the proposition that litigation causes or aids in obtaining higher bid premiums because bidders often raise their offers in order to respond to the target shareholders' claims of an unreasonably low initial offer price, so as to increase target shareholder support for the bid. The economic effect of shareholder litigation is that while the probability of deal closing decreases by 5.8%, the takeover premium in completed deals increases by about 9% after controlling for other offer features. Moreover, the expected rise in

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[†] Case Western Reserve University, University of New South Wales, and Georgetown University Law Center, respectively.

¹ In *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986) the Delaware Supreme Court held that directors have a duty to maximize shareholder value.

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Barroway Topaz Obtains Appraisal Rights, More Stock for Talecris Stockholders

Michael Wagner, Esquire and Quinn Kerrigan, Esquire

Barroway Topaz recently achieved significant benefits for shareholders of Talecris Biotherapeutics Holdings Corp. (“Talecris” or the “Company”), including securing shareholder appraisal rights where those rights were jeopardized by an oppressive merger structure. Talecris, which makes medical treatments derived from blood plasma, is in the process of being acquired by Grifols, S.A., a Spanish holding company that manufactures and markets, among other things, intravenous medications, medical products, and diagnostic systems. We filed a class action complaint in Delaware’s Court of Chancery relating to the Company’s proposed merger with Grifols. In exchange for each share of Company stock, Talecris’ public shareholders are being asked to accept \$19.00 cash and newly issued, non-voting “Class B” Grifols stock.

Additionally, and alarmingly to us, the proposed merger contemplated reincorporating the Company in Virginia before merging with Grifols, which would have eliminated statutory appraisal rights available to shareholders under Delaware law, the Company’s state of incorporation. Under Delaware law, appraisal rights are available where cash is a substantial part of the merger consideration. Despite the fact that the merger agreement entered into between the Company and Grifols was explicitly made pursuant to Delaware’s merger statutes,

the Virginia reincorporation would eliminate shareholder appraisal rights under 8 Del. C. § 262. In addition, in public filings related to the transaction, Grifols acknowledged that Talecris stockholders were not entitled to appraisal rights with little explanation or acknowledgment of dissenting shareholder’s rights under Delaware law.

The proposed merger was driven by Talecris’ controlling stockholder, Talecris Holdings, an investment vehicle funded by private equity firms Cerberus Capital and Ampersand Ventures. Previously owning essentially all of Talecris and currently controlling nearly 50% of the Company’s outstanding common stock, Talecris Holdings sought to exit its investment in Talecris. We alleged that Cerberus, in particular, was eager to save face with its investors after disastrous investments in Chrysler and GMAC. Talecris Holdings had made several prior attempts to monetize its investment in the Company, most notably a failed merger with CSL Limited in August 2008 and an initial public offering (“IPO”) in October 2009, which reduced Talecris Holdings’ stake to its current level at just below 50%. Determined to exit its investment completely, Talecris Holdings pursued additional transactions in the months following the IPO, ultimately agreeing to the merger with Grifols.

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Conflicted Financial Advisor Agrees to Pay Talbots

Michael Wagner, Esquire

As a result of a recent lawsuit concerning Talbots, the clothing retailer, Barroway Topaz lawyers have obtained a payment by Perella Weinberg Partners (“Perella Weinberg”) following the sale of a controlling stake in Talbots to a special purpose acquisition company (“SPAC”) that Perella Weinberg sponsored. The SPAC transaction resulted from financial advice that Perella Weinberg gave to the Audit Committee of Talbots’ board of directors (i) to help enable Talbots’ former controlling stockholder, Japanese retailer AEON, exit its investment in Talbots and (ii) to restructure Talbots’ outstanding loans. It is rare for a shareholder lawsuit to result, as this one did, in a substantial payment to the company by one of the company’s outside advisors.

Talbots, like many upscale clothing retailers, has greatly suffered from the nationwide economic downturn, and in the fall of 2009 in particular was facing significant pressures from lenders and reduced revenues that ultimately threatened the Company with possible bankruptcy. Additionally, AEON, which controlled a majority of Talbots’ stock, wanted to exit its investment and focus its operations elsewhere, particularly in Japan. Talbots’ Audit Committee was charged with the task of restructuring Talbots’ debt and seeking a transaction that would enable AEON to sell its Talbots stock. To assist the committee, Perella Weinberg was hired to provide financial advice and seek out potential parties to acquire AEON’s stake in Talbots. Perella

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Analyzing Litigation in Mergers and Acquisitions *(continued from page 3)*

the takeover premium more than offsets the expected fall in the probability of the deal closing, raising the “net” expected takeover premium paid in offers that are subject to pre-deal-completion litigation.

Examining settlements of shareholder lawsuits, we found, as expected, that deal completion rates are significantly associated with more settlements, after controlling for offer characteristics and the reputations of legal and financial advisors. Moreover, while a terminated deal occasionally produces gains for target shareholders, in most cases positive settlements only occur if the deal closes. We also noted that lawsuits challenging controlling shareholder squeeze-outs have significantly higher probabilities of settlement with cash consideration resulting for the plaintiff shareholders. We believe the higher likelihood of a settlement in these types of cases is due to legal doctrines that place the burden of establishing the fairness of the transaction on the controlling shareholder. However, if a controlling shareholder uses a tender offer, the likelihood of a settlement declines, reflecting a legal carveout of these transactions from the otherwise pro-shareholder legal regime.

Finally, turning to the influence of the M&A advisor’s reputation on potential litigation, our report concluded that top target law firms significantly impede litigation settlements, supporting the proposition that top law firms would

vigorously pursue efforts to obtain M&A litigation dismissals. However, top bidder law firms are associated with significantly more lawsuit settlements, supporting the premise that bidder legal advisors strive to settle M&A lawsuits in order to insure deal completion. Top target and bidder law firms are both positively associated with cash settlements of lawsuits. This is likely consistent with client objectives in the sense that top target law firms tend to negotiate settlements in strong cases that support increased payment to shareholders and attract the involvement of top bidder law firms, while top bidder law firms are able to leverage larger payments to facilitate suit settlement and deal completion at acceptable levels.

Our results demonstrate the importance of considering litigation’s impact on the market for corporate control in empirical research examining the determinants of M&A transaction outcomes. We believe further research in the area would benefit greatly from improved federal securities law disclosure requirements concerning deal litigation. Nevertheless, we believe our report provides investors and corporations a meaningful description of the circumstances leading to M&A litigation as well as the impact of such litigation on the probability of deals closing and ultimate premium level.

Barroway Topaz Obtains Appraisal Rights, More Stock for Talecris Stockholders *(continued from page 5)*

To ensure the sale of its controlling interest in Talecris and its exit from the Company, Talecris Holdings entered into a Voting Agreement with Grifols, committing to vote its near-majority stake in the Company in favor of the merger and against any competing transaction. In addition, the Company’s directors and executive officers pledged to vote their combined stake of more than 1% of Company stock in the merger’s favor, assuring majority stockholder approval and consummation of the transaction, and the elimination of stockholder appraisal rights, without obtaining the vote of a single public shareholder. In our complaint, we alleged, among other things, that Company shareholders were entitled to appraisal rights under Delaware law and that material information relating to the Merger needed to be disclosed.

The firm conducted discovery on an expedited basis, reviewing and analyzing over 80,000 pages of documents and

conducting seven depositions within a two-week period. The depositions included those of the Company’s CEO, Talecris Holdings’ board appointees, a purported independent Talecris director, and two investment banks that had provided the merger parties with financial advice.

After completing discovery and poised to file our opening brief in support of a motion for preliminary injunction, we reached an agreement with Defendants to settle the case. Defendants agreed to provide Talecris shareholders with appraisal rights under Delaware law. In addition, Defendants agreed to issue to the public Talecris stockholders an additional 500,000 shares of Grifols “Class B” shares as a part of the merger price, and to make meaningful additional and revised material disclosures of information regarding the transaction. The settlement will be presented to the Delaware Chancery Court for its consideration in the coming months.

Conflicted Financial Advisor Agrees to Pay Talbots *(continued from page 5)*

Weinberg looked at several potential funding sources but focused its efforts on SPACs.

SPACs are essentially publicly traded pools of cash, sponsored by financial firms and funded by public investors through their purchase of shares in an initial public offering. SPACs typically have a roughly two-year period from their IPO to invest that money in the equity of other companies. Should a SPAC's sponsor fail to invest the pool of money by the investment deadline, the SPAC would be liquidated and the money returned to investors. SPACs are traditionally used to make investments in privately held companies and enable those companies to become publicly traded through a so-called "reverse IPO" in which the private company merges into the publicly traded SPAC, with the publicly traded company surviving the merger.

Potentially lucrative for sponsors should a SPAC's pool of money be invested, sponsors can lose millions should no transaction occur before the investment deadline. Perella Weinberg sponsored a SPAC, BPW Acquisition Corp. ("BPW"), which had approximately \$330 million in cash and an investment deadline of February 2010.

In addition to looking at other SPACs and possible funding sources in the fall of 2009, the people at Perella Weinberg who were advising Talbots contacted their Perella Weinberg colleagues who were looking for investments for BPW, to see if BPW might be willing to, in effect, assume AEON's stake in Talbots and provide the cash necessary to restructure Talbots' debt. The Audit Committee ultimately followed Perella Weinberg's advice and agreed to pursue a transaction with BPW under which BPW stockholders and Perella Weinberg would receive Talbots stock in exchange for BPW's cash, and AEON would divest its majority stake in Talbots. Unlike how SPACs traditionally make investments, BPW would be merging into Talbots, with Talbots surviving the transaction.

The Perella Weinberg-advised Audit Committee, facing extremely limited financing options as well as possible bankruptcy, ultimately agreed to the transaction with Perella Weinberg-sponsored BPW. Under the transaction's terms, BPW's stockholders would receive Talbots stock valued at \$11.25 per BPW share, paying a premium for BPW's cash that was otherwise worth BPW's \$10 per share IPO price.

We filed a lawsuit on behalf of Talbots' minority stockholders in the Delaware Court of Chancery, principally against Talbots' directors, AEON, and Perella Weinberg. We sought to enjoin the BPW-Talbots transaction as well

as damages for Talbots. Among other things, we alleged that Perella Weinberg was hopelessly conflicted as Talbots' financial advisor and engineered the transaction for its own benefit at Talbots' expense.

We took expedited discovery in February 2010, reviewing more than 100,000 pages of documents and conducting the depositions of several Talbots directors, Perella Weinberg principals, and an AEON representative. We also hired a financial expert, who submitted a written report and was deposed by the defendants. We were poised to seek an injunction to prevent the transaction until discovery revealed how much Talbots truly needed essentially immediate funding. We therefore negotiated for and obtained significant corporate governance reforms from Talbots, while allowing the transaction to go through in April 2010 and proceeding with our damages claim against Perella Weinberg.

After the transaction closed and we sought additional discovery in the litigation from Perella Weinberg and other defendants, we entered into settlement discussions and ultimately reached an agreement with the defendants to settle the case in exchange for substantial payments to Talbots. Specifically, under the settlement, Talbots will receive \$3.75 million in cash from certain defendants including Perella Weinberg, and Perella Weinberg will return 175,000 shares of Talbots stock (worth more than \$2 million as of December 3, 2010) to Talbots.

The settlement of this case is particularly unusual in that Perella Weinberg, as a part of the settlement, is making a substantial payment to Talbots resulting from advice that Perella Weinberg rendered to Talbots as the Company's financial advisor. There are very few other cases that have resulted in similar relief, and the settlement in this case will be presented to the Delaware Chancery Court on December 20, 2010.

Barroway Topaz Litigators Obtain Historic Jury Verdict in First Credit Crisis Securities Fraud Trial *(continued from page 1)*

financial crisis in November 2007. “The trial opened a most revealing window into fundamentally dishonest reports BankAtlantic made to its stockholders about the riskiness of its land portfolio,” Mr. Zivitz remarked shortly after the verdict was announced. “The jury’s award represents a clear rebuke for the bank’s deceitful disclosure practices. But it’s also a historic success for investors who were victimized by the bank’s behavior.”

Background to the BankAtlantic Case

On October 25, 2007, BankAtlantic Bancorp, the parent company of federally chartered bank BankAtlantic, announced that its commercial real estate land loan portfolio contained \$250 million in non-accruing and internally high risk (or “classified”) loans, notwithstanding statements made in the prior two quarters that the portfolio continued to perform well in spite of the Florida real estate downturn. Following the company’s announcement of these results in the third quarter of 2007, BankAtlantic’s stock price declined nearly forty percent on the next trading day. Subsequent investigation into the actions of BankAtlantic and its senior-ranking executives led to the filing of several lawsuits alleging securities fraud. The United States District Court for the Southern District of Florida selected State-Boston Retirement System to serve as lead plaintiff. Barroway Topaz was tapped to serve as co-class counsel and its client, Erie County Employees Retirement System, was appointed co-class representative.

Working with co-lead counsel, Barroway Topaz continued to investigate the circumstances leading up to the October 2007 investor losses and filed an amended complaint against the defendants in early 2008, alleging violations of the anti-fraud provisions of the Securities Exchange Act of 1934. Specifically, the plaintiffs alleged that BankAtlantic set out on a course to artificially inflate its share price (or prevent the stock price from dropping further) by (i) issuing false and misleading statements concerning the quality and composition of the bank’s Florida land loan portfolio; and (ii) falsely representing that the bank adhered to conservative underwriting practices in SEC filings, press releases and earnings calls with Wall Street analysts. These allegedly false and misleading statements included commentary on the bank’s borrowers (“There’s really nothing significant to note on the credit quality front” and “we see no trends to make us nervous”); characterizations of asset quality (“We insist on hard equity” from our borrowers); and assurances that the bank was monitoring its land loan portfolio and saw no problems emerging (“There are no asset classes that we are concerned about in the portfolio” and “[t]he portfolio has always performed

extremely well, continues to perform extremely well”). In reality, BankAtlantic’s land loan portfolio had rapidly deteriorated and ominous default trends were emerging. Plaintiffs alleged that these undisclosed risks — a toxic \$500 million land loan portfolio and lax underwriting standards for real estate developer loans — ultimately materialized in the form of non-accruals (resulting in the taking of loss reserves and a corresponding hit to the bank’s earnings) and classified loans on the verge of default, and that the unanticipated announcement of BankAtlantic’s loan write-downs in October 2007 resulted in a stock plunge of forty percent, causing investors millions of dollars in losses.

The Litigation

In May 2009, the Court denied the defendants’ motion to dismiss the complaint, finding that plaintiffs had sufficiently pled the contours of a securities fraud based on BankAtlantic’s misrepresentations and omissions of material facts concerning the deterioration of its land loan portfolio and its undisclosed failure to adhere to conservative lending practices in underwriting land developer loans.

Over the ensuing year, the parties conducted extensive discovery, exchanging more than two million pages of documents and conducting over twenty depositions of current and former BankAtlantic officers, directors and employees, as well as five putative experts seeking to testify on the subjects of real estate lending, the economic collapse and damages. The discovery process proved contentious at times, as the defendants often contested their obligation to produce many of the critical documents. The defendants’ actions in this regard proved largely unsuccessful, as plaintiffs ultimately obtained thousands of pages of e-mails, internal reports, committee meeting minutes and other bank documents that demonstrated the defendants’ state of mind with respect to the mounting problems in the land loan portfolio. For example, plaintiffs’ counsel obtained the bank’s internal monthly “loan watch lists,” which identified the bank’s high risk classified land loans. These reports revealed the existence of hundreds of millions of dollars in at-risk loans which, the bank’s chief executive officer Alan Levan publicly insisted, “continued to perform extremely well” even as the Florida real estate market took a turn for the worse in the first two quarters of 2007. Likewise, plaintiff’s counsel obtained e-mails between and among bank executives and lending officers demonstrating the defendants’ knowledge of the ongoing deception. In one such email exchange establishing bank management’s knowledge of the mounting problems, defendant Jarett Levan, the President of the bank, asked his father and co-defendant Alan

Levan, the chief executive officer, whether he should be “embarrassed” for telling analysts during an investor conference in New York earlier that day that they “see no trends that make us nervous.” The elder Levan replied that he “would have approached this differently,” that he “wouldn’t be so bold on the credit front” and that the bank “is going to have problems” with the land loan portfolio. In another e-mail, a member of the bank’s Major Loan Committee responsible for approving land loans over \$5 million ranted about the poor quality of the portfolio to a colleague, calling the loans “garbage” and accusing the bank’s executive management of “stick[ing] their heads in the sand and pretend[ing] there is no problem.”

Key Pre-Trial Rulings

After the close of discovery in May 2010, both the plaintiffs and defendants filed motions for summary judgment. These motions sought judgment or dismissal of some or all of the claims in the litigation based on the documentary and deposition record developed during the year-long discovery period. Both parties also filed motions to prevent the other side’s use of certain evidence obtained during discovery and to exclude objectionable aspects of expert testimony to be offered at trial. The Court denied the defendants’ summary judgment motion which sought to have the case dismissed due to a lack of evidence of fraud. As the Court stated in its opinion denying the motion, “an issue of fact exists as to whether Defendants knew that their [public] statements presented an obvious danger of misleading investors, in that they identified BankAtlantic’s lending practices as conservative and omitted to disclose the true credit quality of the land loan portfolio.”

The Court then granted several key motions in the plaintiffs’ favor. Most importantly, the Court granted partial summary judgment for plaintiffs on the issue of “falsity,” one of the elements of a securities fraud claim. In so ruling, the Court found that four statements made by defendant Alan Levan about the land loan portfolio during a July 25, 2007 earnings conference call were objectively false. This critical ruling resulted in the jury being instructed at the close of the trial to consider those four conference call statements as proven false as a matter of law; the jury was still required to deliberate as to the remaining elements of the plaintiffs’ fraud claim — *i.e.*, whether the statements had been made with an intent to deceive and whether they caused the company’s stock price to decline. Finally, the Court granted in large part the plaintiffs’ motion seeking to exclude the defendants’ proposed expert on damages, resulting in the exclusion of the proposed expert’s entire fifteen-page damages report with the exception of a single paragraph. As a result of this ruling, defense counsel strategically chose not to put this damages expert on the stand at trial, leaving plaintiffs’ damages expert to testify unopposed.

The Trial

The trial commenced on October 12, 2010 in Miami before The Honorable Ursula Ungaro of the U.S. District Court for the Southern District of Florida. In the five weeks that followed, Barroway Topaz partners Zivitz and Mustokoff shared trial duties in cross examining several of the individual defendants and current BankAtlantic officers, as well as conduct the direct examination of plaintiffs’ damages expert, Candace Preston, who testified before the jury that BankAtlantic’s stock price was inflated during the class period as a result of the defendants’ ongoing misrepresentations regarding the land loan portfolio and underwriting practices.

The defendants argued that these alleged misrepresentations were not actionable under the securities laws because BankAtlantic sufficiently warned about the declining real estate market in Florida which affected the collateral of the loans. The defendants further contended that any decline in BankAtlantic’s stock price in October 2007 upon the revelation of the \$250 million in non-accruing and classified loans was the result of the economic downturn, not the revelation of previously undisclosed risks to the land loan portfolio. This so-called “market forces” defense has been seen in several securities cases to have emerged out of the subprime and credit crisis over the past few years.

On November 18, 2010, after hearing the testimony of fourteen witnesses and the lawyers’ closing arguments, the jury found that fraud had been perpetrated on BankAtlantic’s investors during the class period and, specifically, that all purchasers of BankAtlantic common stock between April 26, 2007 and October 25, 2007 were damaged by \$2.41 per share per day — a number that could amount to tens of millions of dollars depending on the number of claims ultimately submitted by class members. Just as significant, according to Mr. Mustokoff, is the fact that the jury rejected the defendants’ “market forces” defense — one that is heavily relied upon by corporate defendants in similar securities class actions arising from the financial crisis. According to Mustokoff, “while BankAtlantic generically warned about the collapsing real estate market, which everyone knew about from reading the newspaper, it didn’t warn of the magnitude of risk and the mounting losses in its land loan portfolio known internally within the bank. That’s what was not disclosed to the public, and it was that deception which caused the shareholder losses in October 2007.”

The case is styled *In re BankAtlantic Bancorp, Inc. Sec. Litig.*, S.D. Fla. No. 07-61542.

A Brand New Day? The Dodd–Frank Wall Street Reform and Consumer Protection Act’s Impact on Investors *(continued from page 1)*

In this article, we briefly discuss some of the Act’s main investor-related provisions, including provisions: creating incentives for whistleblowers to reveal corporate fraud, allowing shareholders to provide input on executive pay, and mandating government studies on whether private investors should be allowed to sue certain classes of defendants that were effectively shielded from private suit in recent U.S. Supreme Court decisions.³ A full discussion of the Act, which spans nearly 1,000 pages, is beyond the scope of this article.

1. Whistleblower Provision

In a section entitled “Whistleblower Protection,” the Act establishes laws that enhance the Securities Exchange Commission’s (“SEC”) ability to combat securities fraud using information from private individuals. Specifically, the Act authorizes the SEC to pay individuals who voluntarily provide “original information” that leads to a successful SEC enforcement action an award of 10% to 30% of any sanction over one million dollars collected by the SEC in the action.⁴ In order to further encourage disclosure, the whistleblower provision prohibits employers from punishing employees who provide the SEC with information showing corporate malfeasance.⁵ It also provides that the SEC must, to the extent practicable, keep the identity of any whistleblower confidential. The SEC will finalize rules implementing the new whistleblower law by April, 2011.

2. Say On Pay

The Act includes several provisions allowing shareholders to comment on executive pay.⁶ Under the Act, public companies are now required to provide: (1) a non-binding shareholder vote on executive compensation at least every three years, (2) a non-binding vote on the frequency of the say-on-pay vote at least every six years, (3) disclosure of any special executive compensation (“golden parachute”) arrangements made in connection with specified change in control transactions, and (4) a non-binding shareholder vote on golden parachute arrangements. While allow-

ing shareholders to express views on executive pay can be meaningful, the non-binding nature of the votes mandated by the Act renders them advisory votes that corporations may freely reject.

3. Clawback Provisions

The Act expands the mandatory recoupment, or “clawback,” policies enacted under the Sarbanes-Oxley Act (which was passed after scandals at Tyco, Enron and Worldcom in the early 2000s) for incentives paid in connection with corporate wrongdoing.⁷ Under the Act, the SEC must direct national exchanges and securities associations to require listed companies to enact compensation clawback policies featuring two basic elements. First, the policies must include mechanisms to “claw back,” or recover, any incentive-based compensation paid on the basis of improperly reported financial information. Second, the policies must include a mechanism by which companies can claw back any such compensation paid during the three years before the “date that the company is required to prepare [any] accounting restatement” to correct a prior filing. A company that fails to create and enforce Act-compliant clawback policies could be penalized, possibly by de-listing. The specific rules implementing the Act’s clawback provisions will be established through SEC rulemaking in the months to come.

4. The Act’s Responses to Supreme Court Decisions

Limiting the Scope of Public and Private Fraud Actions

The Act also responded to rulings by the United States Supreme Court impacting the scope and reach of the federal securities laws.

In *Central Bank of Denver v. First Interstate Bank of Denver*,⁸ and later in *Stoneridge Investment Partners LLC v. Scientific Atlanta, Inc.*,⁹ the Supreme Court eliminated the ability of private investors to bring suit against a person who aids or abets a primary violator of the federal securities laws. For example, under these rulings, a bank that knowingly constructs sham transactions to manipulate

³ As discussed in Section 4 of this article, these SEC studies will incorporate comments submitted by interested members of the public.

⁴ Act § 922(a)-(b). “Original information” includes information not otherwise known by the SEC or available from public sources or media. Id.

⁵ Act § 922(a)-(h).

⁶ Act § 951.

⁷ Act § 954. Section 304 of the Sarbanes-Oxley Act of 2002 requires a CEO or CFO to return incentive-based compensation to an issuer when a financial restatement occurs “as a result of misconduct.” 15 U.S.C. § 7243. In contrast, executive wrongdoing apparently is not needed to trigger the Act’s new clawback provisions.

⁸ 511 U.S. 164 (1994).

⁹ 552 U.S. 142 (2008).

the financial results of a publicly traded company cannot be named in a lawsuit by the public company's defrauded investors. The rulings not only impacted private litigants' ability to pursue "aiding and abetting fraud" claims, but also left in doubt the precise scope of the SEC's authority to prosecute such claims.

Separately, in 2010 in *Morrison v. National Australia Bank* ("NAB"),¹⁰ the Supreme Court ruled that the primary antifraud provision of the federal securities laws — Section 10(b) of the Securities Exchange Act of 1934 — applies only to "domestic transactions" and not to transactions involving securities registered on non-U.S. exchanges. The ruling was grounded on a finding by the Court that the U.S. securities laws were silent as to their extraterritorial application, and therefore had none.¹¹ It dramatically cut the rights of both private litigants and the SEC to bring federal securities fraud claims based on foreign transactions and swept away decades of case law interpreting the transnational reach of federal law.

With respect to the SEC, the Act clarified what *Central Bank/Stoneridge* had put in doubt and gave back what NAB took away. The Act expressly provided the SEC with authorization to prosecute aiders and abettors under the Securities Act of 1933 and other investor-protecting statutes. It also clarified that the SEC may prosecute individuals who recklessly or intentionally aid or abet violations of the Securities Exchange Act of 1934.¹² Separately, the Act responded to NAB by fully restoring the SEC's power to prosecute foreign securities fraud to pre-NAB limits.¹³

The Act also addressed — though not as decisively — the plight of private securities plaintiffs after NAB and *Central Bank/Stoneridge*. As to NAB, the Act directed the SEC to "solicit public comment and thereafter conduct a study to determine the extent to which private rights of action under the antifraud provisions [of the federal securities laws] should be extended" to reach foreign securities transactions (within the limits in place before NAB).¹⁴ In other words, should the right of private litigants to bring fraud suits concerning foreign transactions be coextensive

with the newly-restored SEC right? Specifically, the SEC has requested public comment on: (1) the scope of such a private right of action, including whether it should extend to all private actors or whether it should be more limited to extend just to institutional investors or otherwise; (2) what implications such a private right of action would have on international comity; (3) the economic costs and benefits of extending a private right of action for transnational securities frauds; and (4) whether a narrower extraterritorial standard should be adopted.¹⁵ The comment period runs until February 18, 2011. After the comment period closes, the SEC will have until January 21, 2012 to submit the results of its study to Congress, which may then take up the matter.

Similarly, in connection with private litigants' ability to assert claims against aiders and abettors, the Act directed the Comptroller General of the United States to study "the impact of authorizing a private right of action against any person who aids or abets another person in violation of the [federal] securities laws."¹⁶ The Comptroller General must complete the study and report its findings to Congress within one year. Both the NAB and *Central Bank/Stoneridge* studies will be subject to significant public and behind-the-scenes political pressure from interested groups, making their outcomes impossible to predict at this time.

¹⁰ 130 S. Ct. 2869 (2010).

¹¹ Id. at 2878.

¹² Act § 929M-O.

¹³ Act § 929P(b) (entitled "Extraterritorial Jurisdiction of the Antifraud Provisions of the Federal Securities Laws").

¹⁴ Act § 929Y.

¹⁵ SEC Release No. 34-63174 (Oct. 25, 2010).

¹⁶ Act § 929Z. The U.S. Comptroller General is the head of the U.S. Government Accountability Office, which "supports the Congress in meeting its constitutional responsibilities and helps improve the performance and accountability of the federal government for the benefit of the American people." See <http://www.gao.gov/>.

Calendar of Upcoming Events

Evolving Fiduciary Obligations of Pension Plans 2011 • February 1, 2011

Hotel DuPont – Washington, DC

The Evolving Fiduciary Obligations of Pension Plans conference will again provide a comprehensive examination of many vital issues that executives, investment professionals, and legal advisors of pension plans must understand in order to properly fulfill their roles.

It will offer objective viewpoints on how fiduciaries can best meet their goals and elude problems, in addition to offering timely information and guidance on various investment and legal tools that can be utilized to resolve issues as they surface.

Over the course of this one-day event, attendees will hear from a variety of peers and outside experts who will share their knowledge, experience, and expertise about the most critical issues facing plan sponsors, their legal counsel, and their boards.

2011 ICGN Mid-Year Conference • February 28 – March 2, 2011

Shangri-La Hotel – Kuala Lumpur, Malaysia

The focus of the conference is on the economic growth in Asia and its implications on corporate governance. Also a Palm Oil Industry tour and discussion is being arranged for March 2 open to all conference attendees.

Rights & Responsibilities of Institutional Investors 2011 • March 10, 2011

Renaissance Amsterdam Hotel — Amsterdam, Netherlands

Now in its sixth year, The Rights & Responsibilities of Institutional Investors will provide an insightful examination of the vital issues confronting investors. This year's program will offer objective analysis of the issues facing shareholders and provide the information fiduciaries need to meet those challenges, including how they can maximize recovery when losses do occur.

Compliance and legal officers and other decision-makers from European public pension and insurance funds and mutual fund companies will share information on how to best protect assets through responsible fiduciary practices.

Sir Richard Branson will serve as this year's keynote speaker. Please visit www.riiconference.com for more information.

Council of Institutional Investors 2011 Spring Meeting • April 3-5, 2011

Omni Shoreham Hotel — Washington, DC

Looking ahead to the future of Corporate Governance.

NCPERS Annual Conference & Exhibition 2011 • May 22-26, 2011

Wynn Las Vegas Hotel — Las Vegas, Nevada

Attendees benefit from the comprehensive educational programming, dynamic speakers, and networking opportunities with money managers, investment service providers and public fund colleagues from across the nation. More than 1,000 trustees, administrators, state and local officials, investment, financial and union officers, pension staff and regulators attend each year.


**BARROWAYTOPAZ
KESSLERMELTZERCHECK LLP**
Attorneys at Law

280 King of Prussia Road, Radnor, PA 19087
610-667-7706 • Fax: 610-667-7056

580 California Street, Suite 1750, San Francisco, CA 94104
415-400-3000 • Fax: 415-400-3001

www.btkmc.com

Barroway Topaz Bulletin Editors:

Darren J. Check, Esquire • Stuart L. Berman, Esquire • David Kessler, Esquire
Kathy L. VanderVeur, Institutional Relations Administrator

Please direct all inquiries regarding this publication
to Darren J. Check, Esq.
at 610-822-2235 or dcheck@btkmc.com

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