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A SECURITIES FRAUD AND CORPORATE GOVERNANCE QUARTERLY

THE HCA DERIVATIVE LITIGATION

A Study on Achieving Corporate Governance Reform Through Shareholder Litigation

By Daniel L. Berger, Jeffrey N. Leibell and Avi Josefson

The staggering losses investors have suffered as a result of the massive accounting debacles at companies like Enron, WorldCom, Global Crossing, Qwest, Adelphia and others have left investors clamoring to recover tens of billions of dollars in losses from bankrupt estates or companies teetering on the brink of insolvency, as well as from those companies' accountants, investment bankers and attorneys. Investor confidence in corporate America has been severely undermined, and shareholders are outraged by ineffective internal control practices and outright management pillaging. These disasters have vividly illuminated the need for U.S. corporations to substantially improve their corporate governance.

While Congress has enacted the Sarbanes-Oxley Act of 2002 (the "Act"), and the New York Stock Exchange has proposed to the SEC several new rules (the "NYSE Proposals") aimed at improving corporate governance, there has been little focus on the ability to achieve significant corporate governance reforms through shareholder litigation. Institutional investors seeking redress from these recently revealed massive frauds — and, perhaps more importantly — seeking to prevent the occurrence of future frauds, would do well to take note of the sweeping state-of-the-art corporate governance reforms secured through the recently settled HCA Derivative Litigation, which BLB&G prosecuted over the last five years.

Representing the New York State Common Retirement Fund, the Court-appointed lead derivative plaintiff, as well as the California Public Employees' Retirement System ("CalPERS"), the New York City Pension Funds, the New York State Teachers' Retirement System and the Los Angeles County Employees' Retirement Association, BLB&G has helped to build what is now the benchmark for good corporate governance planning. As pointedly observed by Richard H. Koppes, the former Deputy Executive Officer

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REGISTER NOW FOR THE NEXT INSTITUTIONAL INVESTOR FORUM!

The 9th BLB&G Institutional Investor Forum, "Managing Securities Litigation: A Comprehensive Guide for Public Pension Funds and Other Institutional Investors," will be held in New York City on ***November 13-14, 2003.*** If you are interested in attending the November Forum, you can register online or get more information by visiting **www.iiforum.org** or contacting Douglas McKeige (800-380-8496 or doug@blbglaw.com) or Tony Gelderman (504-525-3373 or tony@blbglaw.com). iiforum.org

HCA DERIVATIVE LITIGATION

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and General Counsel of CalPERS and the founder and past president of the National Association of Public Pension Attorneys, the corporate governance plan HCA adopted as a result of the settlement of that litigation "meets, or exceeds in some cases, many of the leading best practices in corporate governance now being proposed for this country, and contains a number of provisions that are critical for truly effective good corporate governance in any large public company today."

Background

The HCA case began in 1997 after revelations of the government's investigation of HCA (then Columbia/HCA Healthcare) for widespread healthcare fraud. HCA was alleged to have (i) provided improper economic incentives to doctors to refer patients to HCA facilities; (ii) submitted Medicare cost reports that included non-allowable expenses; and (iii) systematically "upcoded" patients' diagnoses in its Medicare billing to increase its reimbursement. The disclosure of these schemes embroiled HCA in numerous criminal and civil litigations, including federal and state prosecutions, a variety of *qui tam* lawsuits, and class action suits brought on behalf of HCA patients and shareholders. The investigation, litigation and resolution of these cases resulted in extraordinary costs to HCA and its shareholders. In response to the damages caused by those litigations, several of the nation's largest public pension systems brought the HCA Derivative Litigation against certain of the Company's current and former officers and directors. This derivative action asserted the Company's rights against those individuals whose conduct precipitated the fraud, and thereby sought to secure monetary compensation for the Company for the damages HCA suffered as a result of that fraud and, more importantly, to reform the Company's corporate governance to prevent recurrence of such corporate malfeasance.

The HCA Derivative Litigation was prosecuted for several years. After initially being dismissed, the claims were reinstated by the Court of Appeals for the Sixth Circuit in a landmark decision. (The Court of Appeals' decision was the subject of "Institutional Investors Prevail in Columbia/HCA Derivative Action," in the Second Quarter, 2001 issue of the *BLB&G Institutional Investor Advocate*.) In the two years since the Court of Appeals' ruling, plaintiffs prosecuted the action and conducted extensive discovery, which culminated in a historic settlement. The settlement was approved by the court in 2003. While the settlement includes a monetary component to be paid to the Company out of insurance policies, the highlight of the settlement is HCA's adoption of the broadest and most extensive corporate governance plan (the "Plan") ever imposed through litigation. As described in more detail below, the Plan addresses the specific failings of HCA's governance that permitted the above-described company-wide fraud to occur, and goes well beyond those specific failings to broadly strengthen all aspects of the Company's internal controls and governance.

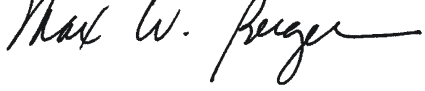
Inside Look

This quarter, the *Advocate* focuses on the issue which, in the wake of the recent corporate scandals, has dominated the headlines of the financial press for some time now: corporate governance reform. As the regulators labor to devise new rules to improve corporate governance at public companies, we draw your attention to another method of achieving reform—shareholder litigation. In *The HCA Derivative Litigation: a Study on Achieving Corporate Governance Reform Through Shareholder Litigation*, Dan Berger, Jeff Leibell and Avi Josefson discuss the groundbreaking corporate governance plan adopted by HCA as a part of the settlement of the HCA Derivative Litigation. As noted in the article, HCA's plan is viewed by corporate governance experts as one of the leading reform plans in the country, and some of its provisions are deemed to be far more progressive than recently proposed or enacted rules or regulations. As the lawyers who prosecuted this case for the past five years on behalf of the New York State Common Retirement Fund, California Public Employees' Retirement System, the New York City Pension Funds, the New York State Teachers' Retirement System and the Los Angeles County Employees' Retirement Association, we are proud to bring you the highlights of this historic settlement.

We also draw your attention to our regular *Eye on the Issues* column. As has been the case for many months now, we could fill the entire *Advocate* with important news reports affecting securities and corporate law. In this issue, Tim DeLange, our *Eye* correspondent, has again insightfully summarized the most significant developments for your easy reference.

This issue of the *Advocate* also comes on the heels of our eighth Institutional Investor Forum, held on June 12 and 13, 2003 in New York City. We are told that the attendees (senior officials from public pension funds around the country) yet again found the Forum valuable, informative and fun. For an overview of the Forum, see the enclosed *Forum Highlights*. If you would like to attend our next Forum scheduled for November 13 and 14, 2003, please contact us as soon as possible.

We hope that you will enjoy reading this issue of the *Advocate*. As always, we endeavor to make it informative and we welcome your comments, questions and input.



The Plan

The Plan truly heightens the standards for corporate governance, with many provisions that far exceed those recently established by the Act, as well as those propounded by the NYSE Proposals. Indeed, according to Professor Melvin A. Eisenberg, a preeminent expert in corporate governance, the Plan is "an excellent, state-of-the-art corporate governance plan." Among other advances, the Plan greatly improves both the definition of director independence and the placement of independent directors in key board positions; expands the powers of key board committees, including the Audit and Corporate Governance Committees; and provides shareholders with direct input into executive compensation. In fact, many of the Plan's provisions are so novel and so far exceed current corporate governance "best practices," that Institutional Shareholder Services, the world's leading provider of proxy voting and corporate governance advisory services, including advice regarding corporate governance best practices, does not yet include them among the 61 criteria they use to evaluate corporate governance strengths and weaknesses. Set forth below is a summary of the more significant provisions of the Plan, each of which exceeds the requirements imposed by the Act or the NYSE Proposals.

1. Director Independence

Of the great strides forward in corporate governance accomplished by the Plan, the most significant is in the area of director independence. The Plan incorporates several provisions to ensure that the directors of HCA will be independent of external influences that could impact their judgment and conflict with their fiduciary obligations to the Company and its shareholders.

A. Board Elections

Under the Plan, nominees must be proposed for election to the Board so that, should the proposed nominees be elected by the shareholders, a full two-thirds of the Board would be "Independent Directors." The Plan also requires key board committees to be comprised solely of independent directors. These provisions represent a substantial improvement over the prior HCA requirements, which necessitated only that a "substantial majority" of the Board members be "non-employees" of the Company, and exceed the NYSE Proposals, which require only that a simple majority of the Board be independent.

B. Definition of "Independent Director"

The Plan also introduces a strenuous definition of who may be considered an Independent Director. That definition leaps ahead not only of current corporate governance standards, but also of the stringent new standards being established by Congress, the SEC and the New York Stock Exchange. The Plan defines an Independent Director as, among other things, one who has not — in the past five years — (a) been employed by the company; (b) personally performed services for the Company; or (c) been employed or affiliated with a present or former independent auditor of the Company.

Significantly, for a director to be considered independent under the Plan, the Governance Committee — which itself is comprised solely of Independent Directors — also must take affirmative action to establish that the director has no material relationships with the Company. The Plan specifically requires that the Governance Committee determine whether material relationships exist between the Company and any director or nominee who is an officer, director or owner of more than 10% of a business enterprise that is a consultant or advisor to the Company or a significant supplier

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HCA Corporate Governance Plan — Key Provisions

- Nominees for election to the Board of Directors must be proposed so that a full two-thirds of the Board would be Independent Directors.
- Independent Director may not have been an employee of the Company; performed services for the Company; or been employed by the Company's independent auditor in the past five years.
- Independent Directors given the power to retain outside consultants and required to meet outside the presence of any non-Independent Director.
- Governance Committee must affirmatively establish that Independent Directors have no material relationships with the Company.
- Board required to oversee the Company's internal control system.
- Key Board committees, including the Audit and Governance Committees, must be comprised solely of Independent Directors
- Audit Committee must either change the Company's external auditing firm after seven years, or affirmatively determine and document that such change is not in the Company's best interests.
- Audit Committee to pre-approve the performance of any non-audit services.
- Audit Committee must separately meet with auditors and management prior to issuing the Company's earnings releases.
- Company to give shareholders the opportunity to vote on the issuance of any equity compensation to any of the Company's highest paid executives.

According to Professor Melvin A. Eisenberg, a preeminent expert, the Plan is "an excellent, state-of-the-art corporate governance plan."

Eye On The Issues

LEGISLATIVE/REGULATORY UPDATES
AND RECENT DECISIONS OF INTEREST

By Timothy DeLange

Two Large U.S. Banks Settle Enron Investigations for $300 Million. J.P. Morgan Chase and Citigroup, the two largest U.S. banks by assets, agreed to pay more than $300 million to settle state and federal investigations into their roles in Enron's collapse. J.P. Morgan will pay $135 million and Citigroup will pay $120 million. Citigroup's penalty includes a settlement of charges that the bank helped Enron competitor, Dynegy, Inc., manipulate its financial statements. In addition to the federal payments, the two banks agreed to pay $50 million total to New York State and New York City to settle similar investigations. The SEC said most of the settlement funds would go to the fraud victims. Both banks still must defend ongoing Enron-related lawsuits filed by investors. "These two cases serve as yet another reminder that you can't turn a blind eye to the consequences of your actions — if you know or have reason to know that you are helping a company mislead its investors, you are in violation of the federal securities laws," said Stephen M. Cutler, the SEC Director of Enforcement. *CNN/Money, July 28, 2003; New York Times, July 28, 2003; The Washington Post, August 4, 2003.*

SEC Chief Donaldson Claims Crackdown Has Calmed Investors. Speaking on the one year anniversary of the enactment of the Sarbanes-Oxley Act, SEC Chairman William Donaldson stated that the recent crackdown on corporate corruption is fostering a "spirit of integrity" and renewed investor confidence. Donaldson acknowledged, however, that some companies have yet to grasp the importance of the reform. Specifically, Donaldson criticized those companies who lavish executives with exorbitant pay packages and generous stock options. Donaldson also remarked that new rules may be needed to ensure companies put enough money into their pension funds for employees. *The Associated Press, July 30, 2003.*

Public Companies Must Vouch For Internal Controls. Pursuant to the provisions of the Sarbanes-Oxley Act, the SEC recently approved rules requiring companies to include in their annual reports an explanation of the company's internal controls. The final rules require the annual internal control reports to include: a statement of management's responsibility over internal controls and reporting; a statement on the framework used to evaluate the effectiveness of the controls; management's assessment of the effectiveness of these controls over the past year, with any material weaknesses that management has identified; and a statement that the firm's registered accounting firm has audited the financial statements included in the annual report and attested to management's assessment of the internal controls. SEC Commissioner Harvey J. Goldschmid heralded the new rule as a "landmark" and the most important item the Commission has handled within the last year. *The Washington Post, May 27, 2003; Federal Securities Law Reports, June 4, 2003.*

Institutional Investors, Accounting Irregularities Increase Settlement Values. According to a 2003 study by NERA, an international economic consulting firm, there is no statistically significant changes in filing or settlement trends in federal securities class actions since the passage of the Sarbanes-Oxley Act. The study found, however, that only half as many cases have been dismissed since the passage of the Sarbanes-Oxley Act compared to the previous eleven month period. The study also found that settlements are about twenty percent higher in cases where the lead plaintiff is an institutional investor. In addition, the Study found that cases with accounting allegations, settle for approximately twenty percent more than cases without such allegations. In sum, eighty percent of federal securities class action lawsuits end in settlement; nineteen percent are dismissed; and about one percent end in judgments. *NERA "Recent Trends in Securities Class Action Litigation," June 2003.*

Shareholders Wielding Power in Record Numbers. So far this year, shareholders have hit more than half of the country's 2,000 largest public companies with shareholder or proxy proposals. The 1,082 proposals filed in 2003 is already more than a third higher than the 800 filed in 2002. Almost three-quarters of shareholders' resolutions filed in 2003 concern corporate governance. Even more drastic is the increase in proposals concerning executive compensation: 324 so far this year, up from 106 last year. Shareholder proposals and initiatives are spearheaded by powerful institutional investors, including public and union pension funds. For example, the Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF) raised concerns regarding corporate governance and executive pay to some twenty five companies earlier this year and all but two companies agreed to adopt the suggested changes. *New York Law Journal, June 11, 2003.*

First IPO Settlement Yields $1 Billion for Investors. More than 300 companies that went public during the Internet boom of the late 1990s have reached a $1 billion settlement with investors claiming their stock offerings were rigged. Investors alleged that the companies, along with the banks that took them public, manipulated the IPO market during the technology stock boom of the late 1990s. The $1 billion settlement was the result of a yearlong mediation and includes an agreement from the companies suing their IPO underwriters to assign their claims against the banks to the investors. The claims against fifty-five investment banks who underwrote the IPOs are still pending. Investors allege, among other things, that the

banks entered into secret arrangements with their 180 clients, which resulted in stimulating artificial demand for the stocks recently taken public and boosting the prices of these stocks to exorbitant levels. *Bloomberg, June 26, 2003.*

Accounting Restatements Continue to Climb. Restatements filed with the SEC rose in the first half of 2003 to 158, up eighteen percent from 134 filed in the first half of 2002. According to the Chicago-based Huron Consulting Group, the main reasons for the restatements included the application of proper accounting rules, human or system errors and fraud. Atop the accounting list of reasons for the restatements was revenue recognition. Restatements also surged due to the demise of Arthur Anderson, which prompted 1,300 U.S. companies to hire new auditors. These new auditors at companies such as Freddie Mac have challenged Anderson's accounting and forced previous results to be restated. *The Los Angeles Times, July 30, 2003.*

Controversial Sarbanes-Oxley Act Rule Takes Effect. On August 5, 2003, one of the final and most controversial provisions of the Sarbanes-Oxley Act goes into effect: the requirement for attorneys to report evidence of violations of securities law. The provision requires lawyers who practice before the SEC to report evidence of material violations to the chief legal officer or chief executive officer of a public company. If the lawyer does not receive an appropriate response to the report, the lawyer is required to report evidence of the violation to the company's audit committee, the qualified legal compliance committee or the full board. These requirements are far less controversial than the SEC's original proposal that would have required attorneys to withdraw from their duties and report the withdrawal to the SEC. Dubbed the "noisy withdrawal," the SEC has postponed indefinitely a decision on whether it will implement this requirement or a similar proposal requiring the corporation, not the attorney, to report the withdrawal. *Chicago Lawyer, August 2003.*

Wall Street Settlement Hinges on Court's Approval. U.S. District Court Judge William H. Pauley, who must sign off on the $1.4 billion agreement to settle charges against Wall Street banks relating to conflicts of interests has raised several questions regarding the settlement. Specifically, Judge Pauley has asked how much of the payments would be tax-deductible, whether the investment banks would ask insurers to cover their payments, how regulators would go about distributing the nearly $400 million earmarked for harmed investors and whether the proposed conflict-of-interest rules regarding bank analysts will apply to the firms' foreign affiliates. Responding to the judge's questions, the SEC said that half of each firm's total fine and restitution payments would be considered penalties and, therefore, not tax-deductible. The remaining half would be considered disgorgement to investors and tax deductible. The SEC also noted that the settlement called for the SEC to appoint an administrator for the restitution fund and that it expected the primary recipients to be those who directly bought securities mentioned in the settlement from one of the ten firms. Judge Pauley has not indicated when he might make a final ruling on the settlement. *The New York Times, June 4, 2003; The Washington Post, June 17, 2003; The Washington Post, July 4, 2003*

Stock Analysts and Investment Bankers Face New Conflict of Interest Rules. The SEC recently approved rules aimed at eliminating conflicts of interest between stock analysts and investment bankers. These new rules come on the heels of the $1.4 billion settlement by ten of Wall Street's largest investment banking firms over charges that their analysts misled investors by publishing overly optimistic reports on companies in exchange for lucrative investment-banking fees. The new rules require all securities firms to establish compensation committees to review and approve pay packages for research analysts. All Wall Street firms must disclose all compensation received from companies that are the subject of research reports. The rules also prohibit upbeat reports issued just before and just after the firms have helped take a company public. *The Washington Post, July 30, 2003.*

Stock Options Now Require Shareholder Approval. Under rules approved by the SEC, companies trading on the New York Stock Exchange and Nasdaq must get shareholder approval before granting stock options and other equity compensation. The new rules also require shareholder approval of a change in the exercise price of existing option grants. "These rule changes are an important step by our nation's principal markets. They have responded to the commission's call for an increased shareholder voice in the equity compensation practices of listed companies," praised SEC Chairman Donaldson. *Chicago Sun-Times, July 1, 2003.*

The SEC Favors Objectives-Oriented Approach To U.S. Financial Reporting. On July 25, 2003, the SEC announced the release of a staff study prepared by the Office of the Chief Accountant and the Office of Economic Analysis on the adoption by the U.S. financial reporting system of a principles-based accounting system. The SEC submitted the study to the Committee on Banking, Housing, and Urban Affairs of the U.S Senate and the Committee on Financial Services of the U.S. House of Representatives. The SEC staff supports an "objectives-oriented" approach which should result in more meaningful and informative financial reporting to investors. This approach would also hold management and auditors responsible for ensuring that financial reporting complies with the objectives of the standards. The SEC recognized that the Financial Accounting Standards Board ("FASB") has already begun the shift to objectives-oriented standards and is doing so on a prospective, project-by-project basis. *SEC Release 2003-86, July 25, 2003.*

Timothy A. DeLange is an associate in the California office of BLB&G. He prosecutes securities actions on behalf of the firm's institutional investor clients and can be reached at timothyd@blbglaw.com.

Informed Sources

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Q Why has Martha Stewart been indicted, while other seemingly guilty corporate executives have not?

A Martha Stewart's indictment involves a straightforward and discrete set of events relating to the government's investigation into her broker's dealings in ImClone stock. Prosecutors allege that in connection with this investigation, Ms. Stewart (1) perjured herself, (2) altered evidence, and (3) engaged in securities fraud by making false and misleading public statements relating to the existence of a "standing" $60 sell order with her broker.

In contrast, indicting the former CEOs of Enron (Ken Lay) or WorldCom (Bernie Ebbers), for example, is far more complicated. To establish the criminal intent required to indict, the government needs to conduct detailed, systematic, and necessarily time-consuming investigations into the myriad events that caused the demise of Enron and WorldCom and the specific roles these individuals played in such events. Stay tuned! They are not out of the woods yet.

HCA DERIVATIVE LITIGATION

Continued from page 3.

to the Company, or any director or nominee who has any business relationship with the Company that is required to be disclosed under Section 404 of Regulation S-K of the rules and regulations promulgated by the SEC. Immediate family members of those who do not meet these requirements also are precluded from serving as Independent Directors.

The Plan also imposes a self-reporting requirement should a director learn that he or she no longer is independent, together with a complementary requirement that, in such a circumstance, the Board must take all steps necessary and permitted by law to cause the Company to remain in compliance with the Plan.

C. Directorial Power

Having established stringent qualification requirements for Independent Directors, the Plan takes an additional step forward by imbuing those directors with powers that allow them to significantly impact the functioning of the Board and the Company. Under the Plan, the Independent Directors, acting as a group, have the authority to retain consultants, whereas under the Act, only an audit committee and nominating and corporate governance committee have such authority. In contrast, the NYSE Proposals only require that a nominating and corporate governance committee be able to retain search firms, and a compensation committee to retain compensation consultants. The Plan also requires the Independent Directors to establish objective and subjective performance criteria for the CEO, and to meet together outside the presence of the CEO or any non-Independent Director at least four times each calendar year. These provisions provide the Independent Directors with actual power to influence and investigate the operations of the Company.

2. Board Committees

The Plan requires that the Board constitute and maintain an Audit Committee, a Compensation Committee, a Governance Committee, and an Ethics and Compliance Committee. Each of these committees must consist solely of Independent Directors. The Plan further requires that members of the Board possess experience in areas such as business or management for complex and large consolidated companies or other complex and large institutions; accounting or finance for complex and large consolidated companies or other complex and large institutions; or other significant and relevant areas deemed to be valuable to the Company. In addition, the Plan requires that at least two members of the Audit Committee possess accounting or financial experience. In contrast, the Act and the NYSE Proposals only

require that one such member of the Audit Committee possess accounting or financial expertise.

A. The Audit Committee

In addition to the membership requirements of the Audit Committee described above, the Plan mandates that the Audit Committee meet separately with management and HCA's auditors prior to the filing of the Company's Forms 10-K and 10-Q to discuss, among other things, the appropriateness of the Company's accounting policies. This requirement ensures that Audit Committee members will be involved with HCA's mandatory SEC filings and with Company management. By comparison, the NYSE Proposals do not require such meetings prior to the filing of such information, and do not address the topics to be discussed at meetings between the Audit Committee and management.

The Plan also strengthens the oversight role of the Audit Committee by mandating specific checks to be enforced on the Company's independent auditors. The Plan requires HCA to change its external auditing firm after seven years of serving as external auditor (beginning three years after the effective date of the Plan) unless the Audit Committee affirmatively determines, based on information obtained through the performance of other duties delineated in the Plan, that rotating external auditors is not in HCA's best interests. The Audit Committee must document such consideration, setting forth the reasons for its decision, and repeat and document this process every three years until the Audit Committee selects another external auditing firm. By comparison, the NYSE Proposals contain no such requirement, and the Act only requires rotation of the audit partner — not the entire firm — every five years.

To ensure the independence of the Company's auditors, the Plan requires the Company to obtain Audit Committee approval prior to hiring any partner or senior manager of the Company's independent auditor within two years of such person's employment by that auditor. By contrast, the NYSE Proposals only require the audit committee to set guidelines for the hiring of former company auditors. The Act only precludes audit firms from auditing a company whose Chief Executive Officer, Chief Financial Officer, Chief Accounting Officer or Controller participated in auditing the company within the prior year.

Continued on back page.

Quarterly Quote

Did J.P. Morgan and Citigroup Pay Enough?

On July 28, 2003, Manhattan District Attorney Robert Morgenthau announced a $300 million settlement with Citigroup and J.P. Morgan Chase for their role in the Enron debacle, acknowledging that securing jail time for the responsible bankers would have been nearly impossible:

> *"We have to show intent to commit fraud, and we didn't think we could show that here."*

At the same time, Neal Batson, a bankruptcy examiner appointed by the Court to analyze Enron's demise, concluded that executives at both banks were complicit in the fraud at Enron:

> *"[Citi and J.P. Morgan] had actual knowledge of the wrongful conduct in these transactions."*

Are we missing something here?

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Bernstein Litowitz Berger & Grossmann LLP prosecutes class and private actions, nationwide, on behalf of institutions and individuals. Founded in 1983, the firm's practice concentrates in the litigation of securities fraud; corporate governance; antitrust; employment discrimination; and consumer fraud actions. The firm also handles, on behalf of major institutional clients and lenders, more general complex commercial litigation. The firm's client base in securities fraud and corporate governance litigation includes large public pension funds and other institutional investors.

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Importantly, the Plan also provides that the Audit Committee has to pre-approve the performance of any non-audit services. This requirement is significant because non-audit services provided to the company are often very lucrative to the auditor, and the prospect of the fees to be obtained in connection with these services may affect the auditor's independence. By comparison, the Act provides for a *de minimus* exception for non-audit services under certain conditions, and, significantly, allows an audit committee to pre-approve groups or types of non-audit services — an exception that may swallow the rule.

B. The Governance Committee

As noted above, the Plan requires that the Board maintain a Governance Committee. This committee is charged with the responsibility to monitor and evaluate the independence and performance of Board members. In short, it is the Company's watchdog. In addition, the Governance Committee must evaluate for re-nomination each existing director based upon the specific Performance Criteria and Core Competencies established by the Plan. By comparison, the NYSE Proposals require only that a nominating and corporate governance committee identify individuals qualified to become directors, and to select or recommend that the board of directors select director nominees for each annual meeting of shareholders.

3. Oversight of the Company's Ethics and Compliance

The Plan also enhances HCA's corporate governance outside of the boardroom by, among other things, mandating the creation of two senior executive positions designed to ensure the integrity of the Company's compliance with its ethical obligations and with accepted accounting standards and procedures. Those positions are Senior Vice President of Internal Audit, and Senior Vice President of Ethics, Compliance and Corporate Responsibility. In addition, the Plan requires the board to oversee HCA's internal control system, and sets out, in great and state-of-the-art detail: (i) the components of internal control; (ii) what oversight of HCA's internal control system requires; (iii) the response the board must take when it becomes aware of material departures from internal control programs; and (iv) the details of the board's responsibility for internal control, such as review and periodic evaluations of HCA's internal control structures and internal audit function. The NYSE Proposals, in contrast, merely require the existence of an internal audit function, which may be outsourced, and do not provide for comparable oversight of ethics and compliance.

4. Executive Compensation

Finally, the Plan also addresses executive compensation, a topic that has garnered significant attention recently, as executive compensation has not declined in correspondence to the decline in market performance at many U.S. companies. Importantly, the Plan requires the Company to give shareholders the opportunity to vote on the issuance of any equity compensation to any of the Company's five highest paid executives, unless the equity compensation is issued pursuant to a plan previously approved by the Company's shareholders. Providing direct involvement of the Company's shareholders in matters of executive compensation is unprecedented, and is not included in the provisions of the Act or the NYSE Proposals.

Conclusion

There are several points to glean from this overview of the Plan. One is that, despite the significant improvements to corporate governance that have been achieved by Congress through the Act, and that may yet be achieved by the NYSE Proposals, much room for improvement remains. Another point is that litigation by responsible shareholders may serve as a vehicle to achieving such improvement. Although litigation certainly is not the solution to every company's corporate governance deficiencies, in those cases where governance standards have been weakened to the point that malfeasance capable of damaging the company and its investors — such as the fraud that occurred at HCA — becomes possible, shareholder litigation remains a powerful tool to achieve significant and lasting corporate governance reforms.

Daniel L. Berger is a Managing Partner of the firm and can be reached at dan@blbglaw.com. Jeffrey N. Leibell is Senior Counsel to the firm and a Certified Public Accountant. He can be reached at jeffl@blbglaw.com. Avi Josefson is an associate of the firm and can be reached at avi@blbglaw.com.

Contact Us

We welcome input from our readers. If you have comments or suggestions, please contact Editor Beata Gocyk-Farber, at 800-380-8496 or beata@blbglaw.com. If you would like more information about our firm, please visit our website at

www.blbglaw.com

Editor: Beata Gocyk-Farber
Editorial Director: Alexander Coxe
Contributors: Max W. Berger, Daniel L. Berger, Jeffrey N. Leibell, Avi Josefson, and Timothy A. DeLange

BLB&G
BERNSTEIN LITOWITZ BERGER & GROSSMANN LLP

800-380-8496
E-mail: blbg@blbglaw.com

New York
1285 Avenue of the Americas
New York, New York 10019
Tel: 212-554-1400

California
12544 High Bluff Drive
San Diego, CA 92130
Tel: 858-793-0070

Louisiana
701 Poydras Street, Suite 3640
New Orleans, LA 70139
Tel: 504-525-3373

New Jersey
220 St. Paul Street
Westfield, NJ 07090
Tel: 908-928-1700