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INSTITUTIONAL INVESTOR
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A SECURITIES FRAUD AND CORPORATE GOVERNANCE QUARTERLY

Second Quarter 2005

FIDUCIARIES BEWARE: BIG BUSINESS WANTS TO ROLL BACK NEW INVESTOR PROTECTIONS

By Tony Gelderman

"[I]f [corporate America] won't play by the rules because it's the right thing to do; then [they should] do it because it's good for business and good for the Nation's economy." So said New York's Attorney General Eliot Spitzer, in a recent *Wall Street Journal* op-ed piece. Mr. Spitzer was borrowing an elegantly simple theme from Robert Kennedy, who in the 1960's exhorted America to embrace the tenets of the civil rights movement "because it's good for business." Open accommodations, fair housing, fair credit, and non-discriminating hiring are all basic components of fair access to the consumer marketplace and thus vital to the American economy. In the same sense, transparent financial reporting, independent boards of directors and conflict-free auditors, investment banks and analysts are basic components of a properly functioning

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INSTITUTIONAL INVESTOR RECOVERY — DO YOU NEED HELP?

By Peter M. Saparoff

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Even without becoming a Lead Plaintiff in a securities class action, there are numerous "behind the scenes" activities an institutional investor should participate in to be certain it is fulfilling its fiduciary duties. This activity is required with the filing of a new class action and does not end until final settlement distributions are received from the Claims Administrator. Indeed, the activity of some institutions may be so extensive that they should retain outside counsel to help them fulfill their fiduciary duties.

The Institution Should Become Aware of the Class Action at its Inception.

An effective Class Action Recovery Program should contain data on every securities class action that is filed. If the institution sustained very substantial losses, the institution may consider whether it should file its own action. Alternatively, the institution may work closely with the Lead Plaintiff and Lead Counsel to ensure that any settlement is adequate. In addition, the institution may aid the Lead Plaintiff in preparing the Consolidated

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Save the Date!

The next BLB&G Institutional Investor Forum will be in NYC on Oct. 20-21, 2005. For more information, visit the Forum website at:

www.iiforum.org.

Inside Look

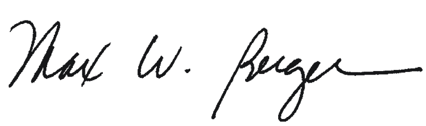
This quarter, the *Advocate* focuses on two important issues concerning investors: the pushback by business interests to recent investor protections and the fiduciary duties of institutional investors. In “Fiduciaries Beware: Big Business Wants to Roll Back New Investor Protections,” Tony Gelderman summarizes the three years of corporate reform following the historic scandals of the early 2000s and the recent pushback by business interests to these reforms. As Tony details, transparent financial reporting; independent boards; and conflict-free auditors, investment banks and analysts are vital to the American economy. The investigations led by Eliot Spitzer, the explosion in the number and value of meritorious securities fraud claims and the enactment of Sarbanes-Oxley all contributed to the efforts to restore confidence in the markets. Unfortunately, as the article explains, business interests are now pushing back against the three years of reform, seeking to undermine public support for prosecutions and to chill recent shareholder activism. We are pleased to bring you Tony’s insight and analysis on this hot topic.

In “Institutional Investor Recovery — Do You Need Help?,” Peter Saparoff, a partner in Mintz Levin Cohn Ferris Glovsky and Popeo, P.C. who represents some of the largest mutual funds in the country, provides suggestions and guidance for institutional investors in fulfilling their fiduciary duties. As Mr. Saparoff explains, institutional investors should become aware of the class action at its inception and remain proactive throughout the litigation, especially during the settlement and claims administration phases. As Mr. Saparoff encourages, every institution should be certain that it timely files proofs of claims in all settlements in which it is eligible, including government settlements which are growing in number. We are delighted that Mr. Saparoff contributed to this issue of the *Advocate*.

Apart from the main articles, we again draw your attention to our regular *Eye on the Issues* column. Benjamin Galdston, our *Eye on the Issues* correspondent, discusses some of the most significant legal and regulatory developments. As a quick perusal of the stories in the *Eye* evidence, we could fill the entire *Advocate* with news reports affecting securities and corporate law.

We invite you to stay tuned for the next edition of the *Advocate*. As promised in our last issue, we will provide an in-depth analysis of how the court in *WorldCom*, together with the New York State Common Retirement Fund, have changed the duties of the “gatekeepers” to Corporate America.

We have enjoyed bringing this issue of the *Advocate* to you. We hope you enjoy reading it and, as always, we welcome your comments, questions and input.



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INSTITUTIONAL INVESTOR RECOVERY

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Amended Complaint to include details making the case more difficult to dismiss. Finally, by being aware of a case at its inception, the institution is assured that it will be aware of any settlement and claim filing dates.

The Institution Should Be Proactive With Respect to Class Action and SEC Settlements.

Every institution should be certain that it timely files proofs of claim in all settlements in which it is eligible to file, including the government settlements which are growing in numbers. Indeed, recently over forty alleged class actions have been filed against advisers to mutual funds alleging that the advisers are not filing proofs of claim and have “damaged” the Funds accordingly (“Mutual Fund Claims Cases” or “MFCC”). The institution — or its outside provider — should have an accurate list of all class and government settlements, time periods covered, due dates, CUSIP’s and other pertinent information.

The institution should not assume that simply responding to the notices it happens to receive in the mail is sufficient. There are so many settlements per year (approximately 150 in 2004 for example) that a “reactive” process is inevitably going to result in missing out on some — if not many — filings. Nor is the argument that “we relied on our custodians to do it” persuasive, unless the institution has a specific contract under which the custodian has agreed to file proofs of claim and the institution has reviewed the custodian’s procedures and reasonably satisfied itself that they are sufficient.

Filing effective proofs of claim is not as simple as filling out forms and dropping them in the U.S. Mail. Obtaining accurate transactional information is a time-consuming process. In addition, Claims Administrators challenge many proofs as deficient and supplemental information is required before the proofs are allowed, requiring substantial follow-up.

Also, the institution needs to closely track recoveries. For example, if the institution is a small mutual fund, does the settlement have an impact on the Net Asset Value of the fund? Does the Plan of Distribution generally match what the claimant's expectations were? Have all "allowed" claims been paid? Will there be a supplemental distribution? Is there a process to insure that checks are promptly deposited?

Quarterly Quote

"To be a philanthropist with other people's money is really not a very persuasive argument for leniency.... If it was not for your age and health I would impose a far greater sentence."

U.S. District Judge Leonard Sand in response to former Adelphia CEO John Rigas' request for leniency at Rigas' sentencing hearing following his criminal conviction for securities fraud.

Settlements Should Be Carefully Considered

Overview

Rule 23 of the Federal Rules of Civil Procedure provides for notice to shareholders and a hearing on the fairness of all class action settlements. With the increased focus on the role of institutional investors in securities class actions has come increased scrutiny by said investors of proposed settlements.

Suggested procedures to follow in evaluating settlements are discussed below. These procedures are based on the assumption that the viability of pursuing the institution's claims individually could become an issue. Thus, the institution should assess its ability to litigate on the merits before objecting.

Internal Factors

(1) Know Your Own Transactions: After receipt of a settlement notice, the first step that must be undertaken to properly evaluate the settlement is obtaining all transactional information from the institution and interviewing the portfolio managers as to the reasons for their transactions.

(2) Loss Calculation: Obviously, the transactional review enables one to ascertain if the "losses" are sufficient to justify the time, effort, expense and distraction of objecting. One should initially review shares purchased during and held throughout the class period. Usually, if other shares are purchased and sold during the class period, any "gains" from these transactions are netted out of the overall "loss" calculations, unless there were partial disclosures during the class period. In addition, many Plans of Allocation require the claimant to have held its shares through the last day of the class period to be eligible. Thus, losses on sales prior to the end of the class period may not be covered.

Huge losses by themselves, however, should not precipitate an objection. The settlement may be low because the case lacks merit. Also, any knowledge by the institution's portfolio manager of facts which class plaintiffs alleged were "omitted" may hinder the ability to object and file a separate action.

(3) Present Holdings: Since settlements often deal with activities several years ago, the institution may have re-purchased the securities of the Company. How much money does the institution want to extract from the Company whose securities it presently holds in order to recover past losses?

External Factors

There are also "external factors" to consider:

(1) Merits of the case: An assessment of the merits must be undertaken, including discussions with both plaintiffs' and defense counsel, their reasons for the settlement and, if necessary, independent research;

(2) Size of Class: A broader class covering several years usually justifies a bigger settlement;

(3) Size of monetary settlement: The calculations of potential per share recovery from the settlement should be reviewed;

(4) Parallel government action: Has the Company settled with the government with respect to activities covered by the class period? If so, the fact that the government took action may militate in favor of a larger settlement;

(5) Use of funds paid in SEC settlement: Did defendants pay penalties and fines and disgorgement in the SEC settlement? Are said funds available to investors under the Fair Funds Act and how will those funds be distributed?

(6) Scope of release: If the release effectively precludes any further claims against defendants during the class period, are there indications that the defendants may be facing further problems?

(7) The reputation of counsel: Is Lead Counsel known for small settlements, or is it known for pushing cases toward trial and achieving substantial settlements in difficult cases?

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Eye On The Issues

LEGISLATIVE/REGULATORY UPDATES AND RECENT DECISIONS OF INTEREST

By Benjamin Galdston

Crime Blotter Update. WorldCom's former chief executive Bernard Ebbers, convicted in March for fraud and other charges, agreed to pay as much as $45 million to investors and his former employer, now called MCI, Inc. The agreement requires Ebbers to pay $5 million in cash and to turn over nearly all of his assets for liquidation. Investors will receive 75% of the funds while MCI will receive 25%. In the prosecution against former Tyco International chief executive officer L. Dennis Kozlowski and its former chief financial officer Mark Schwarz, a Manhattan jury returned guilty verdicts on 20 of 23 counts after 11 days of deliberations. Kozlowski and Schwarz were charged with grand larceny, securities fraud, conspiracy, and falsifying business records in stealing some $150 million from the company through unauthorized loans and bonuses they gave themselves. Kozlowski became the poster child for executive greed when it was revealed that he spent company funds on Manhattan apartments, expensive paintings, a $6,000 shower curtain, and a Roman-themed birthday bash for his wife on a Greek island. Meanwhile, former HealthSouth chief executive Richard Scrushy was acquitted on all criminal charges stemming from the collapse of the Montgomery, Alabama hospital services company. Scrushy, known as "King Richard" for his dictatorial style, was facing a potential life sentence for charges stemming from the $2.7 billion accounting fraud. Scrushy was the first CEO accused of violating the Sarbanes-Oxley corporate reporting law. Observers believe a home field advantage, including a judge that seemed hostile to the federal prosecutors and Scrushy's enormous popularity as a local benefactor and church leader, was decisive in the victory. *Wall Street Journal, June 30, 2005; New York Law Journal, June 20, 2005; USA Today, June 29, 2005.*

Institutional Investors Recover Record Amounts In 2004. According to a new study published by PricewaterhouseCoopers LLP, both public and private enforcement actions for violations of the federal securities laws set new records in 2004. While the government dramatically increased the number of enforcement actions and the amount of monies recovered through fines, penalties and disgorgement, private securities litigation settlements dwarfed prior historic highs. The year was also remarkable for corporate governance reform and individual accountability, which institutional lead plaintiffs increasingly now require in many settlements. Both public and private actions targeted foreign private issuers in record numbers, as U.S. investors fell victim to fraud abroad in cases like Parmalat and Royal Ahold. Overall, investors filed 223 civil cases – an increase of only 5.5 percent over the prior year – but recovered approximately $5.4 billion for injured investors. This amount excludes the whopping $6.2 billion recovered by WorldCom investors, which included payments directly from WorldCom directors. *"2004 PricewaterhouseCoopers LLP Securities Litigations Study," May 2005.*

Ninth Circuit Affirms Seizure of Executive Pay Under Sarbanes-Oxley. The Ninth Circuit upheld a key ruling on a Sarbanes-Oxley provision that allows the SEC to seize multi-million dollar executive severance packages and place the funds into indefinite escrow while it investigates fraud allegations. The case concerns former Gemstar-TV Guide executives Henry Yuen and Elsie Ma Leung, who negotiated multi-million dollar severance packages shortly after the company disclosed a restatement of its financial results. The SEC later charged that Yuen and Leung caused Gemstar to fraudulently inflate Gemstar's revenues by $223 million and sought a court order for seizure and escrow of the monies and stock as "extraordinary payments" under the Sarbanes-Oxley Act. Finding the payments were several times the executives' usual salary and far more than provided in their original employment agreement, the District Court ruled that the payments were "clearly unusual and extraordinary" and appeared to be the fruit of allegedly fraudulent financial results. On appeal, the two former executives argued that the term "extraordinary payments" is unconstitutionally vague and that the District Court erred in its interpretation. But the Ninth Circuit was not persuaded, finding that the District Court properly focused on the nature, purpose and circumstances of the payments and found the payments had nothing to do with Gemstar's ordinary business. *The Recorder, March 24, 2005.*

$4.2 Billion Enron Settlements. J.P. Morgan Chase & Co. and Citigroup agreed to pay $4.2 billion to settle claims by Enron shareholders for their part in the litigation led by the Regents for the University of California. Early settlement agreements such as this put pressure on remaining defendants to settle, rather than face enormous joint and several liability. Previously, J.P. Morgan learned a costly lesson by holding out for a better deal which never materialized in the WorldCom litigation. There, the investment bank rejected an early settlement offer — which co-defendant Citigroup accepted — before settling for $2 billion, a significant premium over the $1.37 billion prior offer. Trial in the Enron litigation is scheduled to begin in October 2006. *Bloomberg June 10, 2005; Associated Press June 16, 2005.*

Regime Change at the SEC. SEC chairman William Donaldson announced his resignation on June 2, 2005, ending a two-year stewardship marked by active enforcement and innovative new regulations. Donaldson, a Bush appointee, set out to restore investor confidence by implementing stricter regulations, including requiring greater oversight of mutual funds and hedge funds. Donaldson also stepped up enforcement and increased monetary fines for wrongdoers. In April, Donaldson's chief enforcement officer Stephen M. Cutler also announced his return to the private sector. Cutler led the SEC's Enforcement Division since October 2001 and is credited with bringing renewed vigor to SEC investigations. Under Donaldson and Cutler, the agency prosecuted some of the largest financial reporting failures in U.S. history, including those at Enron, WorldCom, Adelphia, Qwest, Tyco, and HealthSouth. During that time the Commission obtained judgments in enforcement actions totaling more than $6 billion. President Bush nominated U.S. Rep. Christopher Cox as Donaldson's replacement. Cox is chairman of the Homeland Security Committee and is known for his longstanding efforts to repeal the estate tax, the capital gains tax on savings and investment, and taxes on dividends. Cox is generally considered to be pro-business. Cox was formerly a senior associate counsel to President Reagan and co-authored the Private Securities Litigation Reform Act of 1995 (the "PSLRA"). *Washington Post, May 12, 2005; New York Times, June 2, 2005.*

Morgan Stanley to Pay $1.4 Billion for Sunbeam Fraud. A Florida jury awarded billionaire financier Ron O. Perelman $1.4 billion in his lawsuit against Morgan Stanley, the world's largest securities firm. Perelman claimed that in 1998, Morgan Stanley deceived him into selling camping gear manufacturer Coleman to Sunbeam Corp. in exchange for cash and stock in a deal valued at $1.5 billion. In 2001, Sunbeam went bankrupt following revelations of accounting fraud and Perelman's shares became worthless. According to Perelman's complaint, Morgan Stanley advised him to accept the deal, without disclosing what it knew about the pervasive accounting fraud at Sunbeam. The jury found clear evidence that the investment firm acted fraudulently and awarded $850 million in punitive damages and $604.3 million in compensatory damages, one of the largest awards ever granted by a jury in any action other than a class action. *AP BusinessWire, May 19, 2005.*

New York Stock Exchange Fined For Specialist Misconduct. The New York Stock Exchange agreed to pay $20 million and institute improved self-regulatory measures to address its failure to monitor exchange specialists who engaged in widespread trading ahead of their customer orders between 1993 and mid-2003. Under terms of the settlement, the NYSE must improve its oversight of specialists and other floor traders, including implementing video and audio surveillance of its trading floor. Last year, seven specialist firms paid a total of $247 million to settle charges that their employees interfered with customer orders or delayed execution of those orders – usually for just a few crucial seconds – so they could trade on their firm's own account. The SEC estimates that specialists earned as much as $20 million in improper gains for themselves and their firms. Fifteen former specialists were indicted in April on charges that they traded to benefit their firms at the expense of their customers. Meanwhile, the agency continues to investigate the individual specialists. *Wall Street Journal, April 12, 2005; Associated Press, April 12, 2005.*

Adelphia Criminal Fraud Settlements Announced. Adelphia Communications and its founding Rigas family agreed to pay $725 million to settle an SEC civil enforcement action and resolve criminal charges. According to the SEC complaint, Adelphia, at the direction of its founder John J. Rigas and his three sons, fraudulently excluded billions of dollars in liabilities from Adelphia's consolidated financial statements by hiding them on the books of off-balance sheet affiliates. The SEC also alleged that Adelphia concealed "rampant self-dealing by the Rigas family," including the undisclosed use of corporate funds for purchases of Adelphia stock and luxury condominiums. Under the settlement agreement, the Rigas family must forfeit over $1.5 billion in assets derived from the fraud, including interests in certain cable properties. Adelphia will obtain title to those cable properties and pay $715 million to a victim fund. In a separate agreement, Deloitte & Touche will pay $50 million to settle charges stemming from its audit of Adelphia's financial statements. The SEC issued an Order finding that Deloitte "turned a blind eye" to the massive fraud perpetrated at Adelphia by the Rigas family, despite having identified Adelphia as one of its highest risk clients. Last summer, John Rigas and his son, Timothy, Adelphia's former chief financial officer, were convicted of fraud and conspiracy. *Reuters, May 18, 2005.*

Federal Judges Say Frivolous Lawsuits Not a Problem. In a recent survey, seventy percent of 278 federal judges felt that baseless litigation was either a "small problem" or a "very small problem" in the United States. Only three percent felt frivolous litigation was a "large" or "very large" problem. The survey was conducted by the Federal Judicial Center as part of efforts to reform Rule 11 of the Federal Rules of Civil Procedure which authorizes, but does not require, judges to impose sanctions on attorneys who file frivolous litigation. As part of the White House's well-publicized campaign against the "culture of litigation," the Lawsuit Abuse Reduction Act proposes modifications to Rule 11 that would require judges to impose mandatory sanctions on attorneys involved in such meritless lawsuits. According to the survey, more than eighty percent of the judges indicated that "Rule 11 is needed and it is just right as it now stands." Complete results of the survey are available at the organization's website: www.fjc.gov. *Business Insurance News, May 27, 2005.*

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U.S. securities marketplace and thus vital to the American economy.

As the 1990s came to a close, so did the longest bull market in U.S. history. As the national markets declined, a succession of unthinkably large securities frauds came to light — frauds which were propelled by a corporate mentality of showing stronger financial results — no matter what. The steady beat of fraud disclosures finally moved from the back page to the front page with the implosion of Enron in the fall of 2001, followed quickly in the spring of 2002 by WorldCom, the largest accounting fraud ever. Institutional investors and mom-and-pop investors were both affected. It was clear to most in the securities industry that serious action was necessary to restore investor confidence in the U.S. securities markets. What ensued was far-reaching reform on Wall Street and in corporate boardrooms. However, the reform movement may be sputtering after only 36 months. In fact, certain business interests seem intent on derailing the reforms which have only recently been put in place.

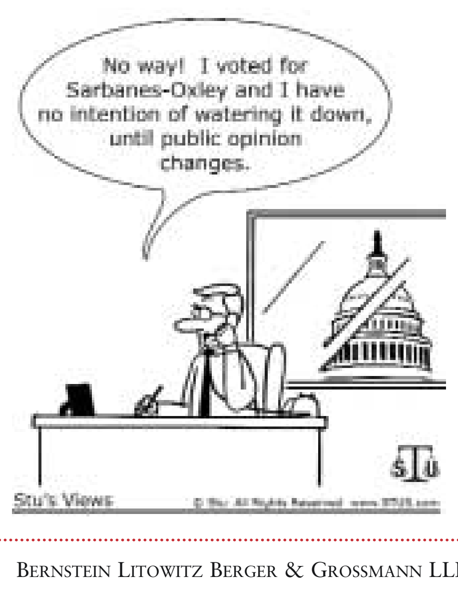
Three Years of Much-Needed Reform

The corporate reform movement in many ways is personified by Eliot Spitzer, whose investigation of Merrill Lynch's stock rating system became public at about the time the WorldCom fraud hit the press. Mr. Spitzer showed the nation, in plain language, how one of the country's oldest securities firms had given its customers tainted and biased advice, simply because the firm wanted investment banking business from the same companies it was recommending to its customers. Mr. Spitzer's investigation led to a ground-breaking settlement severing the link between compensation for analysts and investment bankers. Merrill Lynch paid a $100

The corporate reform movement in many ways is personified by Eliot Spitzer, whose investigation of Merrill Lynch's stock rating system became public at about the time the WorldCom fraud hit the press.

million fine. The next year, Mr. Spitzer shocked the investment world with his revelations of market-timing and late trading practices at several of the largest mutual funds in the country. And just last year, Mr. Spitzer took on the insurance industry for the payment of illegal kickbacks in return for steering business to insurance partners.

The editorial page of *The Wall Street Journal* paints Mr. Spitzer as nothing more than a politician seeking publicity. Ironically, while the editorial page has castigated Mr. Spitzer's investigations, its news reporters have reported that the U.S. Justice Department has charged more than 900 individuals in more than 400 corporate fraud cases since mid-2002. With these numbers, it strains credibility to characterize the wave of corporate fraud as "just a few bad apples."



The Justice Department has won a number of high profile convictions including John Rigas and Timothy Rigas of Adelphia and Bernard Ebbers of WorldCom, to name a few. And it is not just Mr. Spitzer and the Justice Department going after corporate wrong-doers: Manhattan District Attorney Robert M. Morgenthau has now successfully prosecuted former Tyco Chief Executive L. Dennis Kozlowski for larceny and securities fraud. Today it is understood that business executives, even businesses themselves, face a real risk of prosecution for perpetrating corporate fraud. This risk was all but non-existent just three years ago.

On the civil side of the courthouse, the list of successes in combating corporate governance failures is equally stunning. Consider the explosion in the number and value of meritorious securities fraud claims. In 1997, fourteen securities class actions settled for a total of $141 million. By 2004, the total number of securities class action settlements had ballooned to 132, with a total year-end settlement amount of $5.23 billion. Atop all of these cases is *WorldCom,* a class action which will generate over $6 billion for aggrieved investors. Just as stunning as the dollar amount of the *WorldCom* settlement is the fact that it includes sizeable personal payments by the former WorldCom directors, sending an unequivocal message to every public company boardroom in America: if you allow a securities fraud "too-big-to-miss" to go unchecked, you place your personal assets at risk. The *WorldCom* settlement is also expected to force investment banks to beef up due diligence before agreeing to issue debt to the public.

In addition to the criminal prosecutions and the significant civil litigation, regulatory agencies have been shaken up and reinvigorated. The passage of the Sarbanes-Oxley Act was a seminal event in the corporate reform movement, establishing the Public Company Accounting Oversight Board to implement auditors' independence standards, as well as requiring CEOs to certify the accuracy of audited financial statements. The

Securities and Exchange Commission's enforcement budget has been greatly expanded and the commission, under the leadership of William Donaldson, imposed a number of large fines and disgorgements against companies engaged in serious accounting fraud, totaling $3 billion in 2004. The SEC has also successfully promulgated regulations aimed at creating independent mutual fund boards, among other initiatives.

Nevertheless, the goal of restoring full public confidence in our capital markets as honest places to invest hard earned money has not yet been achieved. After all, HealthSouth's Richard Scrushy was recently acquitted on all charges despite testimony from a number of senior executives that Scrushy directed them to participate in the fraud. The problem of continuing corporate fraud is no more evident than in the number of securities class action fraud cases filed and the losses suffered in the alleged frauds. According to a study conducted by the Stanford Law School Securities Class Action Clearinghouse in connection with Cornerstone Research, securities class action lawsuit filings increased by 17% in 2004 from the previous year, while the market capitalization losses corresponding to these lawsuits almost tripled from $58 billion in 2003 to $169 billion in 2004. These statistics tell a simple truth — securities fraud on Wall Street has not peaked. The key culprits in 2004 were drug giants, insurance heavyweights and big players in the energy sector. Investors continue to get fleeced at an alarming rate and this is not a positive bellwether for long-term investor confidence, and thus the U.S. economy as a whole.

The Push Back Has Arrived

It is against this backdrop of successful criminal and civil prosecutions, as well as the continued incidents of major corporate securities fraud, that certain business interests are beginning a public relations counter-offensive, hoping to manufacture a backlash against prosecutors and litigators alike. Why? To undermine public support for prosecutions and chill the enthusiasm of shareholder activists.

The opening salvos were fired off the editorial page of the *The Wall Street Journal* and from the pages of *Forbes* magazine. The themes are consistent: shareholder litigants are misguided; securities fraud cases deliver poor returns for litigants; plaintiff lawyers' legal fees are excessive; and Mr. Spitzer and his like are enemies of free markets. U.S. Chamber of Commerce President Thomas Donohue has joined in, calling Mr. Spitzer's strategy of seeking far-reaching settlements that combine reforms and fines in lieu of prosecution as "the most egregious form of intimidation that we have seen in the U.S. in a long time." And it is not just rhetoric out of the Chamber — its legal arm has filed suit against the SEC, attempting to thwart the new regulatory requirement that 75 percent of mutual fund directors be independent. Indeed, Sarbanes-Oxley, enacted in part to restore investor confidence, is now being criticized as regulation overkill. Business interests point to the high costs of compliance with Sarbanes-Oxley as justification for the need for corrections to the Act.

Today it is understood that business executives, even businesses themselves, face a real risk of prosecution for perpetrating corporate fraud. This risk was all but non-existent just three years ago.

Most recently, Mr. Donaldson has announced his resignation as Chair of the SEC and President Bush has nominated Republican Congressman Chris Cox to replace Mr. Donaldson. Mr. Cox is viewed as sympathetic to the notion that Sarbanes-Oxley has placed undue burdens on corporate America and was a chief proponent of laws limiting securities lawsuits by private investors as a member of Congress. He should be viewed by the corporate governance community with some suspicion.

To be sure, shareholder activists have their share of columnists and commen-

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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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INSTITUTIONAL INVESTOR RECOVERY

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(8) Source of funds: Has D&O insurance been exhausted? Is the Company or are other defendants paying in additional monies?

Objecting to a settlement can be a difficult and burdensome decision. A preferable alternative is to ascertain one's "losses" once the class action is filed. Then, once Lead Plaintiff is appointed, the investor can coordinate closely with the Lead Plaintiff. In this way, when entering into settlement negotiations, Lead Plaintiff will be able to cite specific loss figures to defendants. This is a valuable weapon to enhance the plaintiffs' demands during negotiations and can sometimes prevent the problem of an investor being surprised by a settlement that seems far too low. In addition, if the investor still wants to object, it has had enough "lead time" to adequately assess its position.

Conclusion

Institutional investors must be pro-active throughout every stage of the class action process. Given the vast number of settlements to be evaluated (with proofs of claim due virtually every day), retention of outside counsel to handle the entire process is recommended.

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tators favorably reporting the efforts by aggressive prosecutors and lead plaintiffs. It was *Fortune* magazine that first lifted the veil of fraud at Enron. *New York Times* columnist Gretchen Morgenson, writing about the *WorldCom* class action litigation said, "Thanks to Mr. Hevesi's efforts [as lead plaintiff]...banks will probably be more apt to pick apart a company's financial state before agreeing to sell its securities. That may not sound like much, but on Wall Street, where the investors often come last, it is progress indeed."

Where Do We Go From Here?

What outcome do we really want from this environment, where prosecutors' and shareholders' litigation has mushroomed? Do critics of shareholder activists have a point when they argue that tying law abiding companies in knots of regulation does nothing more than cost shareholders money and chill innovation? Is there a kernel of truth to the assertion that institutional investors and the public are simply vengeful, seeking punishment as satisfaction? Every investor should hope not.

The battle has begun over the hearts and minds of the public, which is weary of corporate scandals but also properly suspicious of over-reaching governmental action. The political fault lines are emerging. The public will watch the ensuing battle and it will be public opinion that dictates how far corporate governance reforms will go or how far business interests will achieve a rollback. The challenge for fiduciaries today is to sift through the charges and countercharges and to act in accordance with the best interest of their beneficiaries. This will, of course, mean filing suit to recover money lost to fraud and it will mean entering proxy fights where necessary. It will also mean speaking out if the SEC seeks to rollback Chairman Donaldson's reforms.

An excellent question for fiduciaries to consider when embarking on corporate governance reform initiatives, such as seeking lead plaintiff status in a securities case or opposing management in a proxy issue, would be: "Is it good for business?" After all, as the owners, shareholders want business to be good.

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