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INVESTOR ADVOCATES APPLAUD SEC'S POSITION IN HIGH PROFILE FRAUD CASE: "PRIMARY VIOLATORS" NEED NOT BE PUBLICLY NAMED TO BE LIABLE TO SECURITIES INVESTORS

WASHINGTON, DC, August 7, 2009 – The National Association of Shareholder and Consumer Attorneys (NASCAT) praised the Securities and Exchange Commission (SEC) for its amicus brief filed yesterday in PIMCO Funds, et al v. Mayer Brown LLP, et al now being heard by the United States Court of Appeals for the Second Circuit. In its brief, the SEC said that actual “attribution of a false or misleading statement by a person is only one means” by which a person may be a “primary violator” of SEC Rule 10b-5’s prohibition against making false or misleading statements to investors. A person may also be a primary violator and, thus, held accountable to investors, if that person provides the false or misleading information that another person puts into a false statement, the SEC said.

“In its brief, the SEC takes an important step toward restoring some investor protections lost in recent years in court decisions that have overly restricted and rolled-back investors’ rights of action and curbed their ability to recover losses from those who, by all traditional definitions of the word, unquestionably engaged in fraud,” said Ira Schochet, Esq., NASCAT’s President. “In addition, the SEC also reiterated the long-standing position of the Commission and the Supreme Court that private investor lawsuits are necessary to provide maximum compensation for injured investors while also supplementing enforcement of securities laws and deterring wrongful practices.”

The SEC brief and underlying appeal relate to a lawsuit brought by shareholders and bond holders against the lawyers who allegedly designed and helped sell to counterparties sham transactions and falsified securities offering documents to cover-up hundreds of millions of dollars in losses by Refco, Inc. Refco, the once global, publicly traded derivatives dealer, collapsed in 2005 when its cover-up of the devastating losses unraveled.

Although the lower court judge recognized the merits of the Refco plaintiffs' lawsuit, he cited two Supreme Court rulings (Central Bank and Stoneridge) as forcing the dismissal of the investors' class action lawsuit. Since the lower court ruled, one of the defendants in that lawsuit, Joseph P. Collins, a partner at the law firm of Mayer Brown, LLP and a former Refco legal adviser, has been convicted in a federal court of conspiracy to commit securities fraud and four other counts of illegal actions. Two others have pled guilty to fraud charges.

“Private investors form a key front-line defense against financial fraud and abuse because they are in a unique position to quickly identify and take action against unlawful conduct by corporate issuers and their advisers,” Mr. Schochet continued. “Traditionally, securities market regulation and law enforcement relied upon a ‘three legged stool’ of the SEC, federal and state attorneys general and investor actions. In recent years, however, two legs of the regulatory stool were weakened by laxity in enforcement of federal securities law and Supreme Court decisions, and lower court rulings interpreting those decisions, which have curtailed investors’ rights of action.”

As part of its financial regulatory restructuring proposal, NASCAT has urged Congress to correct the problems caused by these three Supreme Court decisions:

- In 1994, the Court held that investors cannot assert a claim against those who “aid and abet” securities fraud (*Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*). This immunity from private liability applies even to those who knowingly help primary actors perpetrate fraud. In particular, outside advisors, such as accountants, attorneys and underwriters are in an excellent position to both help perpetrate and deter fraud. Unfortunately, in some of the largest frauds in history, such advisors were deeply involved in the underlying transactions enabling the primary actors to carry-out the crimes. Recognizing these outside advisors’ ability to detect and prevent fraud, Congress preserved the SEC’s right to bring aiding and abetting actions against them. However, this is not sufficient to protect investors. Congress should extend that right to private lawsuits so that investors can recover fraud losses and otherwise benefit from the additional protections that private litigation would create.;
- If the elimination of aiding and abetting liability was not enough, in 2008, the Court imposed an overly restrictive view of the circumstances under which investors may assert a claim against secondary actors who knowingly engage in schemes to defraud the investing public (*Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*), thereby enabling undisputed participants in the underlying fraud at issue to escape accountability to investors. In the Charter Communications case at issue in *Stoneridge*, the fraud could not have occurred without the active, knowing participation of the defendant actors – each of whom engaged in

conduct (including falsification of invoices) that was inherently deceptive itself, rather than ordinary business acts that merely aided the fraud. If *Stoneridge* remains the standard, “gatekeepers” in even the most flagrant securities frauds, including investment bankers, feeder funds, and credit rating agencies, will effectively be immune from legitimate claims by injured investors.

- In 2005, the Court issued a ruling that resolved a split among the Circuit Courts of Appeals on the element of loss causation and provided a reasonable standard for establishing this element. (*Dura Pharmaceuticals v. Broudo*). However, many lower courts have since used this decision to erect a new barrier to investors obtaining a recovery from those who defraud them. At issue in *Dura* was whether investors must plead and prove a connection between defendants’ false statements and the eventual drop in the securities price. The Supreme Court held that the law “requires that a plaintiff prove that the defendants’ misrepresentations (or other fraudulent conduct) *proximately caused* the plaintiff’s economic loss.” The Court stated, however, that it did not intend this requirement to become a heavy burden upon harmed shareholders seeking recovery of their losses. Unfortunately, many lower courts have too narrowly interpreted this decision and, in so doing, have raised artificial obstacles for defrauded investors seeking recovery. In the process, these restrictive interpretations of *Dura* have provided immunity to corporate wrongdoers who now knowingly and cleverly separate the timing of the release of bad news leading to stock drops from later disclosures acknowledging that the bad news was actually caused by deceit. Through manipulations of these disclosures, these wrongdoers now are able to escape liability for the frauds they perpetrate on investors.

The National Association of Shareholder and Consumer Law Attorneys is a nonprofit organization comprised of about 100 law firms representing consumers and investors - including pension funds and individuals - in cases of securities fraud and other forms of "white collar" wrongdoing and criminal activity.

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