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FEATURE 1

CENTRAL STATES PENSION FUND TAKES ON FREDDIE MAC

Judge John F. Keenan in the Southern District of New York recently appointed **Central States, Southeast and Southwest Areas Pension Fund** as sole lead plaintiff in the proposed class-action litigation brought by purchasers of common stock of the Federal Home Loan Mortgage Corporation ("Freddie Mac"). Judge Keenan also approved Central States' selection of Coughlin Stoia as lead counsel to represent the proposed class.

The plaintiffs allege that between the November 21, 2007 through August 5, 2008 class period, Freddie Mac and certain officers concealed and misrepresented to investors the company's broad exposure to mortgage-related losses, poor underwriting standards and risk management procedures, and the resulting negative impact on its capital adequacy. Freddie Mac took on massive amounts of subprime and other nontraditional risky loans, in particular "Alt-A" loans, which are issued to borrowers with better-than-subprime credit. It simultaneously failed to maintain an adequate capital cushion to protect it and its shareholders against a downturn in housing prices. The action was filed in the United States District Court for the Southern District of New York.

"The chief executive of the mortgage giant Freddie Mac rejected internal warnings that could have protected the company from some of the financial crises now engulfing it, according to more than two dozen current and former high-ranking executives and others."

As *The New York Times* reported on August 5, 2008, "The chief executive of the mortgage giant Freddie Mac rejected internal warnings that could have protected the company from some of the financial crises now engulfing it, according to more than two dozen current and former high-ranking executives and others." In fact, in mid-2004, the company's former Chief Enterprise Risk Officer, David A. Andrukonis, advised Freddie Mac's CEO Richard F. Syron "that [Freddie Mac's] underwriting standards were becoming shoddier and that the company was becoming exposed to losses." Andrukonis also briefed the risk oversight committee of the company's board of directors on his memorandum, but the committee failed to act. *The New York Times* quoted Andrukonis as saying that the loans "'would likely pose an enormous financial and reputational risk to the company and the country.'" Unfortunately for investors, Andrukonis' warning proved prescient.

Even more alarms were sounded by Freddie Mac's former head of compliance and oversight, Donald Solberg, who warned Syron that the company's capital base needed to be replenished. Additionally, as reported by *The New York Times*, in 2007, U.S. Treasury Secretary Henry M. Paulson, Jr. and Federal Reserve Chairman Ben S. Bernanke urged Freddie Mac and its sibling, the Federal National Mortgage Association ("Fannie Mae"), to raise more money and bolster their balance sheets, with Bernanke threatening to publicly chastise the companies if they did not raise more cash. Finally, as home prices plummeted and defaults shot up in 2007, advisors at Freddie Mac exhorted Syron to slow the company's mortgage purchases.

Ignoring all of these warnings, the company and its officers misled investors as to Freddie Mac's true capital and risk posture, while continuing to increase the company's risk exposure and degrade its capital position. In 2007 alone, Freddie Mac expanded its retained portfolio by approximately $17 billion, increasing its mortgage holdings by 2.4%. This expansion was accomplished through further relaxation of underwriting standards and risk management procedures, which resulted in more low-quality, high-credit-risk mortgages on its books. The consequence was additional weakening of Freddie Mac's capital base as the mortgage-related losses ballooned.

But instead of acknowledging the company's compromised position, the company and its officers continued to mislead investors by offering false assurances of Freddie Mac's soundness. However, four straight quarters of losses, newspaper reports, and an April 15, 2008 report by Freddie Mac's federal regulator

Continued on page 6

Coughlin Stoia Commended for Achievements in *Enron*

FEATURE 2

Investors lost billions of dollars as a result of the massive fraud at Enron Corp. In appointing Coughlin Stoia as sole lead counsel to represent the interests of Enron investors, the court found that the Firm's zealous prosecution and level of "insight" set it apart from its peers. Ever since, Coughlin Stoia attorneys and lead plaintiff **The Regents of the University of California** have aggressively pursued numerous defendants, including many of Wall Street's biggest banks. Coughlin Stoia and The Regents have thus far obtained settlements in excess of $7.3 billion for the benefit of investors, which constitutes a significant percentage of recoverable damages.

Coughlin Stoia and The Regents have been actively litigating the *Enron* action since 2001. The court overseeing the case has had the utmost praise for Coughlin Stoia's efforts and stated that the Firm's attorneys "are to be commended for their zealousness, their diligence, their perseverance, their creativity, the enormous breadth and depth of their investigations and analysis, and their expertise in all areas of securities law on behalf of the proposed class." To date, attorneys at Coughlin Stoia have reviewed 70 million pages of documents, and taken over 350 fact depositions and dozens of expert depositions.

Defrauded Enron shareholders have significantly benefited from Coughlin Stoia's tenacious review of millions of pages of Enron's operational documents. Coughlin Stoia attorneys uncovered internal bank documents and testimony, which revealed how the banks engineered sham transactions to keep billions of dollars of debt off Enron's balance sheet. Faced with damning evidence, many defendants decided to avoid a jury trial and instead made large settlement payments. Three large banks, Canadian Imperial Bank of Commerce, J.P. Morgan Chase and Citigroup, have paid $2.4 billion, $2.2 billion and $2 billion, respectively. Other banks, auditors, a law firm, a partnership and the company's directors have also contributed to the overall $7.3 billion settlement fund. ***This is the largest aggregate class-action settlement not only in a securities class action, but in class-action history.*** The court found that the exceptional "results demonstrate why the firm is so highly respected and feared in the securities field."

Describing Coughlin Stoia as "'a lion' at the securities bar on the national level," the court acknowledged that "Lead Counsel's outstanding reputation, experience, and success in securities litigation nationwide were a major reason why [T]he Regents selected the firm." Professor John C. Coffee, Jr. from Columbia University Law School also proclaimed his admiration for Coughlin Stoia's ability to obtain a $7.3 billion recovery: "'Few, if any, other plaintiffs' counsel . . . could have pulled off such a tour de force' and the achievement 'is attributable in almost equal measure to its credibility, creativity and the intensity of its commitment to this case. In my judgment, Lead Counsel is the adversary most feared today by the defense bar in securities litigation, and that reputation played an important role here.'" The court concurred. "The Court finds that in the face of extraordinary obstacles, the skills, expertise, commitment, and tenacity of Lead Counsel in this litigation cannot be overstated."

Although many defendants have settled, several huge banks still named in the *Enron* action have not paid a penny to the victims of the fraud. After years of preparation and just a few weeks before trial, the Fifth Circuit Court of Appeals essentially let the banks off the hook by vacating the class certification order and ruling that because the banks themselves did not make any false "statements" about their conduct, they could not be liable to the victims even if they knowingly participated in the scheme to defraud Enron's shareholders. In January 2008, the United States Supreme Court issued its opinion in *Stoneridge*, another case involving scheme liability, which limits the ability of shareholders to hold third parties legally responsible for the securities fraud of another party. The remaining defendant banks argue that they should be dismissed from the *Enron* action based on *Stoneridge* and the Supreme Court's decision not to hear an appeal on behalf of Enron shareholders.

Continued on page 6

NEWSBRIEF

Coughlin Stoia Partners Recognized as Two of California's Top 100 Lawyers

The *Daily Journal* has named Coughlin Stoia co-founders **Patrick J. Coughlin** and **Darren J. Robbins** as two of the top 100 lawyers in the state of California.

Patrick J. Coughlin

Darren J. Robbins

Coughlin has been at the helm of several history-making cases. As Chief Trial Counsel, Coughlin led the litigation team in Enron and recovered the largest settlement in U.S. history – in excess of $7.3 billion – for defrauded investors. Coughlin also secured a $12.5-billion settlement from tobacco companies for California cities and counties and is responsible for ending the controversial Joe Camel ad campaign.

Robbins has served as lead counsel in a variety of securities cases and to date has recovered more than $2 billion for injured shareholders. Robbins recently led the team of lawyers that recovered a record $925 million for shareholders of UnitedHealth Group Inc. in a case involving stock options backdating.

Robbins is also at the forefront of litigation related to the subprime fallout and is currently leading actions against Citigroup Inc., Merrill Lynch & Co., Inc., Washington Mutual, Inc. and Countrywide Financial Corp.

Robbins received the California Lawyers Attorney of the Year Award in 2004 and is also a highly sought after speaker at conferences held on a variety of topics ranging from corporate governance to directors and officers liability.

The Congressional Bailout: Mostly Small Change

FEATURE 3

In our nation's history, the greatest presidencies have been those confronted with the greatest challenges. Examples abound: Lincoln, the Civil War and the end of slavery; Roosevelt, the Great Depression and the New Deal; Kennedy, the Civil Rights Movement and the Voting Rights Act. On Day One, the economy will be the greatest crisis inherited by the new Obama Administration. That's because the $700-billion bailout bill passed by Congress did not address any of the root causes of this catastrophe.

Nothing in the bailout bill will deter the recklessness that led to the meltdown. Nowhere was there a clarion call for legislative reforms in exchange for these billions and billions and billions. But there is now. Change has been promised; real change, systemic change, lasting change.

It is no mystery just how we reached this cliff. During a presidential debate, president-elect Obama summed it up well: "This is the final verdict on eight years of failed economic policies . . . a theory that basically says we can shred regulations and consumer protections . . . and somehow prosperity will just trickle down. It hasn't worked." It has actually been more like 20 years of deregulation.

There is no shortage of proposed reforms. The nation's op-ed pages, television and radio waves, and the blogosphere are full of them. Make sure taxpayers get full return; provide foreclosure relief; create new jobs. Systemic reform also will need to address the underlying practices that actually caused this crisis – providing loans with dubious terms to anyone that could sign his or her name; chopping those loans into more pieces than a jigsaw puzzle, then selling them to unsuspecting buyers worldwide; rating impossibly complex financial instruments as AAA with little or no basis and no transparency; making gazillions in transaction fees while leveraging (borrowing and then re-lending other people's money) as if there were no tomorrow; through "swaps," gambling that these borrowers would never, ever default, with little in the bank (so to speak) to cover the bet if it ever came due. It came due.

The 110th Congress addressed little of this. Instead, it threw billions of taxpayer dollars at the banks with what now appears to have been a serious lack of strings even on how they are to be spent. Here's why:

Fear. The bailout steamroller had many members terrified. At least privately, the leadership of both parties were told that without swift and decisive action, we could suffer a financial meltdown *a` la* 1929. Show us the money. We'll fix things later. Later has come.

The Power of Money. Wall Street is an equal opportunity contributor. Calls for systemic reforms go unheeded when both political parties are feeding from the same trough.

Al Meyerhoff is a frequent contributor to the *Corporate Governance Bulletin* and is Of Counsel at Coughlin Stoia Geller Rudman & Robbins LLP.

Pie in the Sky. Promises aplenty were being made about a return to "sensible" (as opposed to "nonsensical") regulation once the banks were saved. They've been saved.

So what now? The last time a bailout on this scale was tried was by Hoover in 1931. He saved his Wall Street friends and delayed the "fall" until after the election. Then the nation's entire banking industry collapsed. President-elect Obama may want to start with a single question: What would FDR do?

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Motion to Dismiss *Huffy* Gets Rolling

Tenacious advocacy following an exhaustive investigation of the circumstances leading to the bankruptcy of Huffy Corp. has advanced a securities fraud class action against four former officers of the Ohio-based bicycle manufacturer into discovery.

Huffy had a celebrated history as one of America's top producers of mass-market bicycles and other sporting goods. By the turn of the century, however, Huffy had outsourced most of its manufacturing overseas, and was struggling to compete in the global market. Stung by the 2002 bankruptcy of Kmart Corp. – one of its largest distributors – and a failed attempt in 2001 to purchase the assets of former rival Schwinn Bicycle Company out of bankruptcy, Huffy began looking for other ways to expand its business. In April 2002, Huffy set its sights on the acquisition of Gen-X, Inc., a Canadian manufacturer and distributor of snowboards, hockey equipment, in-line skates, golf equipment and other action sports products.

Huffy told investors that the acquisition of Gen-X would not only update its business for the 21st century, but would smooth out the seasonality of its earnings, which historically had been strong in advance of summer and the holiday season and weaker in winter. Huffy said the acquisition was supported by extensive due diligence demonstrating that Gen-X was a well-managed, profitable business that would increase earnings.

In October 2004, little more than two years after Gen-X was acquired, Huffy was bankrupt. The company admitted to the bankruptcy court that the Gen-X acquisition lied squarely at the center of its demise. "Soon after the acquisition, the Gen-X operations began to suffer significant losses which were funded by Huffy's other operations," Huffy told the bankruptcy court. An investigation by Coughlin Stoia revealed that Gen-X had bled Huffy dry, as numerous employees recounted how profits from Huffy's other divisions were eaten up by the losses created by the Gen-X operations. These employees revealed that even before the acquisition Huffy was on notice that Gen-X's operations were in disarray, and explained how, shortly after the company was acquired, senior-level executives were sent from Ohio to Gen-X headquarters in Toronto to investigate the mounting problems in its operations. "We don't know where half the inventory we're supposed to have actually is," one such executive told a witness shortly after he returned from Canada.

These circumstances stood in sharp contrast to what Huffy said prior to its bankruptcy, when it repeatedly reassured investors that Gen-X was performing in line with expectations. Even as Huffy's overall earnings began to decline, the company reassured investors that the problems lay elsewhere, in its core bicycle and backboard business, and not with Gen-X.

On July 29, 2005, Coughlin Stoia, on behalf of lead plaintiffs **Alaska Hotel & Restaurant Employees Pension Trust Fund**, now part of the **UNITE HERE National Retirement Fund**, and the late Robert Ross (now represented by his nephew and co-investor, Harry Ross) filed a 122-page consolidated class-action complaint drafted by partner **Dennis J. Herman** and associate **Aelish M. Baig**. The complaint details the numerous misrepresentations Huffy had made about the performance of Gen-X. As a result of the provisions of bankruptcy law, Huffy itself was not named as a defendant in the action, which is proceeding against former CEO Don R. Graber, CFO Robert W. Lafferty and two other former high-ranking officers of the company.

During the pendency of defendants' motion to dismiss, Coughlin Stoia repeatedly filed briefs bringing recent decisions supporting the claims of Huffy investors to the court's attention. Coughlin Stoia also successfully argued that the mandatory stay of discovery under the securities laws should be lifted to permit the service of subpoenas, requiring critical evidence to be preserved by Huffy, Gen-X and others. Finally, on September 17, 2008, Judge Walter H. Rice of the United States District Court for the Southern District of Ohio issued a detailed 91-page order exhaustively analyzing and upholding all of the critical allegations in the consolidated complaint and permitting the case to move forward into formal discovery.

"We are gratified that the court was able to see through defendants' numerous and contradictory arguments that sought to kill this case before it had a chance to get off the ground," said Herman. "We thank the court for the detailed analysis of the allegations, and look forward to vigorous discovery so we can obtain the detailed evidence we will need to prove Huffy's fraud to a jury."

In re Huffy Corp. Sec. Litig., No. 3:05-cv-00028-WHR, Decision and Entry (S.D. Ohio Sept. 17, 2008).

Motion for Sanctions Evidence Destruction Catches Up with Oracle

Plaintiffs have won rare evidentiary sanctions as a result of defendants' willful destruction of evidence in a securities class action brought against Oracle Corp. and members of its board. Plaintiffs argued that Oracle co-founder and CEO Lawrence J. Ellison destroyed emails and other communications relevant to the allegations in plaintiffs' complaint.

The case brought by defrauded investors centers around Ellison's suspicious sales of nearly $900 million in stock right before the company announced a revenue and earnings shortfall. As plaintiffs allege, Ellison sold his Oracle shares based on non-public information regarding problems with Oracle's new software product, Suite 11i. Ellison is also alleged to have known that Oracle had fraudulently overstated the previous quarter's results and had concealed Suite 11i's problems from investors.

After defeating defendants' attempts to have the case dismissed, plaintiffs moved the case forward and sought, among other things, Ellison's business email communications for the relevant two-year period. In response, defendants produced only 15 email communications from Ellison's files, despite the fact that Ellison presumably sent and received hundreds of emails each day over those two years. Following a court battle, plaintiffs ultimately learned that Ellison had destroyed not only emails, but also over a hundred hours of highly relevant tapes and transcripts of interviews conducted with Ellison in preparation for his biography, *Softwar*. Ellison's biographer and close friend, Matthew Symonds, the former political editor for *The Economist*, "took the Fifth" regarding his role in the evidence destruction.

As a result of defendants' willful destruction of evidence, the court awarded plaintiffs evidentiary "adverse inference" sanctions. The court explained that sanctions imposing adverse inferences make it "appropriate to infer that the emails and *Softwar* materials would demonstrate Ellison's knowledge of, among other things, problems with Suite 11i, the effects of the economy on Oracle's business, and problems with defendants' forecasting model." The court also held that it would consider the adverse inferences when deciding defendants' motion for summary judgment and would also give an adverse inference instruction to the jury at trial.

According to Coughlin Stoia partner **Mark Solomon**, who led the fight over Ellison's evidence destruction, "If you have documents that will damage your position in litigation and you are required to produce them, you have a choice. Produce them and accept the consequences or destroy them and hope you don't get caught. Ellison chose to destroy evidence and has been caught squarely in the act. It is hardly surprising, therefore, that the court is willing to award plaintiffs adverse instructions to begin to remedy Ellison's insidious conduct."

Nursing Home Pension Fund, et al. v. Oracle Corp., et al., No. C 01-00988-SI, Order (N.D. Cal. Sept. 2, 2008).

Motion for Class Certification
Class Moves Forward in *TD Banknorth*

After a hotly contested battle, **City of Dearborn Heights Act 345 Police & Fire Retirement System** ("Dearborn Heights") and H. Louis Farmer, Jr. ("Farmer") were named class representatives and a class was certified in an action brought against TD Banknorth, Inc. in Delaware Chancery Court. Plaintiffs allege that the Toronto-Dominion Bank sought to cheat TD Banknorth shareholders out of a fair price for their holdings in its bid to acquire all remaining shares of TD Banknorth, a U.S. banking conglomerate.

Farmer, represented by Coughlin Stoia, originally filed suit in Maine state court. At that time, a related action against Toronto-Dominion, brought by different plaintiffs and pending in Delaware, was on the verge of settling for the modest consideration of three cents per share. Despite the settlement agreement and assertions that the claims against TD Banknorth were weak, Farmer continued to forge ahead in Maine, taking nine depositions and uncovering strong evidence in support of his claims. Aware of its potential claims arising out of defendants' wrongful conduct, Dearborn Heights intervened as a plaintiff in the Delaware action, and along with Farmer, used the evidence obtained in Maine to successfully object to the miniscule settlement proposed in the Delaware case.

Assuming the role of lead plaintiffs and with Coughlin Stoia appointed as sole lead counsel, Dearborn Heights and Farmer moved the Delaware case forward and filed a motion seeking to represent the class of defrauded shareholders and requesting that the court certify the class. Defendants vigorously opposed plaintiffs' motion, arguing that Dearborn Heights and Farmer should not be appointed class representatives because they were not in control of the litigation and did not have sufficient knowledge of the claims brought against TD Banknorth. Coughlin Stoia successfully refuted these arguments, establishing that Dearborn Heights not only fulfilled its fiduciary obligation to its plan participants by pursuing claims against the company, but that both Dearborn Heights and Farmer were informed, knowledgeable and actively engaged in the class action. The court agreed, holding that Dearborn Heights and Farmer "demonstrated a clear understanding of the major factual and legal arguments in the complaint," and that plaintiffs had sufficiently monitored counsel and participated in the litigation.

Coughlin Stoia partners **Samuel H. Rudman** and **Evan J. Kaufman** are spearheading the litigation on behalf of plaintiffs. According to Kaufman, plaintiffs' victory on class certification is significant because "it substantially strengthens plaintiffs' litigation position by enabling Dearborn Heights and Farmer to represent each class member and by increasing the potential recovery in the action." Rudman and Kaufman expect to take the case to trial in May.

In re TD Banknorth S'holders Litig., No. 2557-VCL, 2008 Del. Ch. LEXIS 102 (Del. Ch. July 29, 2008).

California Supreme Court Appeal
Green Light from High Court

The California Supreme Court has agreed to examine a case which decides whether tens of thousands of drivers will be allowed to seek partial refunds of fines they were charged in "caught on camera" red light infractions. Ticketed motorists discovered that the private contractor paid to install and operate the camera systems was receiving a large cut of each infraction fine paid, giving the company an incentive to inflate the number of citations issued.

Coughlin Stoia filed an action in 2001 on behalf of approximately 300,000 ticketed motorists in 14 cities, including San Diego, San Francisco, Santa Rosa, Redwood City, Cupertino and Los Angeles County.

For more information on these and other cases, check out our website at csgrr.com

Plaintiffs seek reimbursement of approximately $23 million – the portion of their fines which the cities gave to the contractor. Until the law was changed in 2004, the fee arrangement between these cities and contractor ACS State and Local Solutions, Inc. specified that approximately one-third of the money paid in fines went into the pockets of the company operating the cameras.

Marked by signs at intersections, these "red light" traffic cameras are linked to sensors in the pavement. ACS operatives then review the photos using criteria from the city to determine violations, obtain the names of vehicle owners from the state, send its records to the city for evaluation and mail citation notices to drivers.

According to **Timothy G. Blood**, Coughlin Stoia partner and lead trial attorney representing the motorists challenging the fee system, "A private corporation is obligated to make as much money as it can for its shareholders. This corporation was doing everything from designing the system to gathering evidence and determining who should or should not be prosecuted."

Last year, the Fourth District Court of Appeals in San Diego ruled for defendants and upheld the pre-2004 controversial contingency fees. In its ruling, the appellate court said that the cities, not the contractor, controlled the citation system and decided whether to issue tickets. Additionally, the appellate court averred that there was no evidence that the pre-2004 fee system giving ACS a percentage of each fine collected caused an increase in the number of tickets written. The appellate court also said that ACS preferred to be paid at a flat rate, but that the cities insisted on tying payments to violations to limit their financial risks and give the company an incentive to perform efficiently.

Following a successful appeal by plaintiffs, the California Supreme Court has agreed to review the ruling issued by the Fourth District Court of Appeals.

In re Red Light Photo Enforcement Cases, No. S165425, Review Granted (Cal. Sept. 24, 2008).

Ninth Circuit Appeal 340B Drug Discount Claims Reinstated

A unanimous three-judge panel of the Ninth Circuit Court of Appeals recently reinstated Santa Clara County's claim that drug manufacturers breached their contract with the federal government by overcharging the county for drugs it procured under the 340B drug discount program.

The 340B program provides that, as a condition of participation in the Medicaid program, drug manufacturers must agree to charge counties and specified entities the lowest prices for drugs that they purchase. Over the last several years, the Health and Human Services Office of Inspector General repeatedly found that drug manufacturers were overcharging 340B entities participating in the program.

Notwithstanding the reports of consistent overcharging by the drug manufacturers, the district court dismissed an action brought by Santa Clara County, concluding that 340B entities did not have the right to sue for breach of contract because their contract with the federal government did not expressly provide them with the right to bring this claim.

In its reversal of the district court's dismissal, the Ninth Circuit rejected the notion that the contract governing 340B entities had to expressly provide them the right to bring a breach of contract claim. The Ninth Circuit held that "[a]pplying the federal common law of contracts, we hold that the covered entities are intended direct beneficiaries of these agreements and thus have the right to enforce the agreements' discount provisions against the [m]anufacturers and sue them for reimbursement of excess payments."

The case has been remanded to the district court and is being prosecuted by Coughlin Stoia partner **Jeffrey W. Lawrence**. According to Lawrence, "This decision vindicates the rights of 340B entities to enforce the contract that was entered into for their benefit. It allows counties and other governmental agencies that fund 340B entities to assure that all of their scarce resources are properly used to provide needed drugs to the most vulnerable members of society."

County of Santa Clara v. Astra USA, Inc., 540 F.3d 1094 (9th Cir. 2008).

Freddie Mac continued from page 1

provided a window into the company's perilous financial condition. As a result, Freddie Mac's stock price plunged from $37.50 per share to $6.49 per share at close the day after the end of the class period.

Coughlin Stoia partner **Ramzi Abadou** argued the successful lead plaintiff motion and is pleased with the opportunity to represent the class in this important litigation: "Freddie Mac, its CEO and others at the company violated the public trust in the most abusive of ways in this case. With Central States now selected as the court-appointed sole lead plaintiff, the Firm very much looks forward to squarely addressing those abuses on behalf of the class."

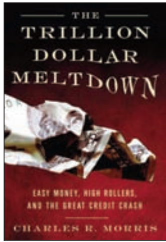
Kuriakose v. Federal Home Loan Mortgage Co., et al., No 1:08-cv-7281 (JFK), Opinion and Order (S.D.N.Y. Nov. 24, 2008).

Achievements in *Enron* continued from page 2

Coughlin Stoia and The Regents disagree and continue to press substantial and sizable claims against the remaining defendants. According to **Trey Davis**, spokesman for The Regents, "It is clear the banks undertook a massive effort to sell Enron to the market. Thus, they had a duty to tell the market at least what they knew from their own deceptive conduct. We continue to pursue Merrill Lynch, CSFB and Barclays as defendants in this case on behalf of investors."

In re Enron Corp. Sec. Litig., MDL No. 1446, 2008 U.S. Dist. LEXIS 84708 (S.D. Tex. Sept. 8, 2008).

Recommended Reading



The Trillion Dollar Meltdown: Easy Money, High Rollers, and the Great Credit Crash

Charles R. Morris
PublicAffairs

Financial institutions around the world are still revealing untold billions in losses. Unable to assess the value of their asset-backed derivative positions, venerable London and New York banks collapse while edgy stock markets swing wildly. Desperate to do anything to stop the free-fall, a frightened Congress accedes to bail-out demands by Wall Street. Former Federal Reserve Chairman Alan Greenspan, who opened the floodgates of low interest rates and cheap money, claims that he could not have anticipated the massive housing bubble and ensuing credit crash. Enter Charles R. Morris, attorney and author who foresaw the coming crisis far enough in advance to have *The Trillion Dollar Meltdown* out in print before the crash was even fully underway. While managing a financial software company, Morris became intrigued by trends in futures and derivatives trading practices, and in early 2007, began intensively researching the bubble in credit derivatives prior to what he foresaw as an unavoidable massive deleveraging of the financial markets.

In readable words, Morris breaks down the arcane derivative "financial innovations" and the policy missteps, greed and delusions that created the largest credit bubble in history. Among a long list of abuses which paved the way for the current crisis, Morris highlights the rollback of FDR-era reforms, particularly the repeal of the Glass-Steagall Act, a "reform" ushered through the Senate in 1999 by the husband of Enron Director Wendy Gramm. Having achieved the deregulation for which they had lobbied for decades, Wall Street's giant commercial banks could now behave more like casinos and make leveraged bets with the house's money. High-rollers like J.P. Morgan and Citigroup went all-in with their chips, gambling with trillions in derivatives worth more than 40 times their assets. As Morris writes, "Citigroup, it was revealed, managed some $400 billion in dicey loans in mysterious off-balance sheet entities called [structured investment vehicles]," an Enron-style sophistry which concealed the risks of these insanely complex side bets derived from instruments like securitized mortgages and credit-card debt.

Citing the lesson of the 1998 collapse of Long Term Capital Management, a hedge fund founded by Salomon's savviest traders and staffed with Nobel Prize-winning economists, Morris notes that "only the very smartest people can make truly catastrophic mistakes." Morris' predictions that a housing bubble slowdown would trigger waves of derivative-linked meltdowns (which would be concealed, sold, or swapped) proved correct: in 2007, after having doubled its previous loss estimates, Citigroup's CFO Gary L. Crittenden admitted to analysts that he could not promise the worst was over; in other words, the CFO of Citigroup *did not know how to value Citigroup's holdings.*

When banks and their hedge-fund doppelgangers rushed to dump these "toxic" assets to free up cash, they found that there were few buyers who wanted to "catch a falling knife." To the dismay of market die-hards, Morris finds that "[t]here is no benevolent market genie behind the curtain, diligently ensuring least-squares approximations to efficient frontiers – just the usual motley of sharks, decent people, charlatans, and some serious intellectuals, mostly playing with other people's money." There is no shortage of responsible parties, and although "Alan Greenspan deserves full blame for his feckless money creation through most of the 2000s," Morris acknowledges that Greenspan "would have been subject to a huge undertow of pressure in that direction from his friends on Wall Street."

As financial markets have foundered on the black shoals of financial deregulation and a glut of the Fed's cheap money, it is less than clear how to chart a course out of these foul waters. Among a raft of reforms, Morris calls for reinstatement of the Glass-Steagall Act, separating the lending and investment functions of commercial banks. Furthermore, Morris advises that derivative trades take place in the light of day on regulated exchanges, and that banks should cease extending credit to hedge funds who refuse to disclose what's on their balance sheets. A novel suggestion is that the lenders who originate securitized loans (such as mortgage-backed securities) should be required to retain the riskiest portion of the loan themselves, incentivizing fair play and due diligence. If Morris was sharp enough to see this coming years ago, maybe we should take his advice.

FAT CAT

Richard S. Fuld, Jr., CEO of the failed brokerage house Lehman Brothers, Inc., testified before Congress last year about his role in the bank's collapse.

Despite surviving two world wars and the Great Depression, Lehman was brought to an inglorious demise as a result of risky bets in derivatives. Investments in these exotic (and unregulated) instruments fueled what *Fortune* magazine called Lehman's "greatest run ever," but when the bets unwound, the company's stock price plummeted from $55 per share to less than 20 cents – one of the world's largest bankruptcies to date. The embattled Fuld blamed the collapse on the "lack of confidence" in Lehman's business model and defended the $484 million he had accumulated in salary and stock since 2000, and the additional $33-million stock bonus he received in March 2008 for his 2007 performance.

Richard S. Fuld, Jr.

Although congressional hearings revealed that the board was steering $20 million in "golden parachutes" to departing executives even as Lehman pleaded for a federal bailout, Fuld will likely keep his salary and bonuses, along with his real estate holdings in Florida, New York and Idaho. Less fortunate are Lehman employees, who owned up to 30% of the now-bankrupt firm.

Calendar of Upcoming Events

January 12-14, 2009

Financial Research Associates, LLC
National Association of Police Organizations ("NAPO")
The 21st Annual Public Safety Pension & Benefits Seminar

The Paris Hotel
Las Vegas, Nevada

This conference covers key issues related to fiduciary obligations surrounding the pension and benefit industry. Participants will also learn the practical tools needed to preserve, defend and enhance their plans.

For more information, visit: www.frallc.com

January 25-27, 2009

Financial Research Associates, LLC
Made in America 2009
The 6th Annual Taft-Hartley Benefits Summit

The Condado Plaza Hotel and Casino
San Juan, Puerto Rico

This annual conference offers trustees and administrators an advanced forum which enables free-flowing, unfiltered and direct dialog between all fund players. Participants will gain insight on key issues concerning pension, investment, health and welfare funds.

For more information, visit: www.frallc.com

January 25-27, 2009

Corporate Directors Forum
Directors Forum 2009 – Directors, Management & Shareholders in Dialogue

Joan B. Kroc Institute for Peace & Justice
University of San Diego
San Diego, California

This conference offers a well-balanced dialogue among directors, management, shareholders and other leaders in corporate governance. Attendance is limited to foster interaction between speakers and attendees. Participants will gain insight into the most current, leading corporate governance issues in an environment that provides ample opportunity to network with other leaders.

For more information, visit: www.directorsforum.com

January 25-28, 2009

Institute for International Research
GAIM USA 2009

Fontainebleau Resort
Miami Beach, Florida

GAIM USA attracts a sophisticated audience representing key decision makers at many of the most influential investment institutions in the world. Attendees from 2008 totaled 900 and were comprised of institutional investors, hedge funds and industry experts from leading banks and service providers. A unique opportunity to meet the leading firms looking to make investments, acquire new talent, develop partnerships and adapt their businesses to the changing market environment.

For more information, visit: www.iirusa.com

February 4-5, 2009

Institutional Investor
The 4th Annual Japan Investment Forum

Imperial Hotel
Tokyo, Japan

The 4th Annual Japan Investment Forum will bring together Japan's leading institutional investors with high-profile asset managers, consultants, banks and regulators. The Forum will explore the variety of investment practices institutional investors can adopt to achieve necessary returns while minimizing risk. It will build on last year's event, which was attended by more than 100 investment executives from Japanese pension and insurance funds.

For more information, visit: www.iiconferences.com

February 9-11, 2009

Institutional Investor
The 19th Annual European Pensions Symposium

Hotel Arts
Barcelona, Spain

This conference is designed to meet the specific needs of European investment executives and will explore ways to invest in these difficult times.

For more information, visit: www.iiconferences.com

February 26-28, 2009

Blueprint for Cure
The 24th Annual Labor of Love Golf Tournament

Fontainebleau Resort
Miami Beach, Florida

Through a special program called the Blueprint for Cure, America's union workers have joined together with the Diabetes Research Institute and Foundation in a unique effort to find a cure for diabetes. The relationship began in 1984, and reached a major milestone when the men and women of the unions funded – and built – the Diabetes Research Institute facility in Miami, the most comprehensive diabetes research facility in the world. The Blueprint for Cure is spearheaded by the Building and Construction Trades Department and endorsed by the American Federation of Labor and Congress of Industrial Organizations.

For more information, visit: www.diabetesresearch.org

March 16-18, 2009

Information Management Network ("IMN")
The 14th Annual Public Funds Summit

St. Regis Monarch Beach
Dana Point, California

The 14th Annual Public Funds Summit will allow attendees to converse over three days about leading asset allocation and investment strategies, manager and trustee selection, and governance issues through interactive panel discussions. The program is specifically crafted to serve the interests and needs of the nation's public pension funds.

IMN will also co-host with Institutional Investor the Money Management Letter's 8th Annual Public Pension Fund Awards for Excellence Dinner as a precursor to the 14th Annual Public Funds Summit.

For more information, visit: www.imn.org

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San Francisco
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(800) 449-4900
www.csgrr.com

Please direct all inquiries to:
Patrick J. Coughlin
patc@csgrr.com

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