

PUBLIC PENSION FUND UPDATE

How do Trustees Maximize Recovery of Loss?

Securities Litigation and Trustee Fiduciary Duty

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Pension Funds, Fiduciary Duty and Securities Litigation: How to Maximize Recovery of Loss

“Class action litigation by shareholders to enforce securities laws is a powerful tool to hold corporate wrongdoers accountable...”
Pensions & Investments Magazine, July 25, 2011

As the law firm that litigates more securities fraud cases than any other¹, The Rosen Law Firm is well qualified to help you guard your rights as an institutional shareholder and perform your fiduciary duty to maximize recovery of loss.

Despite the passage of stricter federal laws such as the Sarbanes-Oxley Act of 2002, which strengthened requirements for public company officers and directors in the areas of corporate governance and financial reporting accountability, every fiscal quarter sees a roster of public companies that have run afoul of these and other regulations. What is the general nature of securities fraud cases, and how can pension trustees maximize recovery of losses for their beneficiaries?

Most securities litigation cases center around allegations of:

- Accounting manipulation, or lack of internal control over financial reporting
- Concealment of corporate misconduct
- Failure to disclose materially negative trends in the business

Often, there is a material negative development in a company’s business that they do not disclose right away, perhaps believing that they can rectify the situation if given a little time. The situation invariably gets worse, and when the true details enter the market, investors suffer when the stock price drops. This was the case when General Electric revealed that for years it was under-reserving for losses in its legacy insurance business, and then took a \$6.6 BILLION charge against earnings that shocked investors, and punished the stock price.

Another common occurrence is accounting manipulation for purposes of improper recognition of revenue or deferral of expenses which can cloud the true picture of a company’s financial and operating condition. When the true details enter the market, investors again suffer damages from a stock price drop.

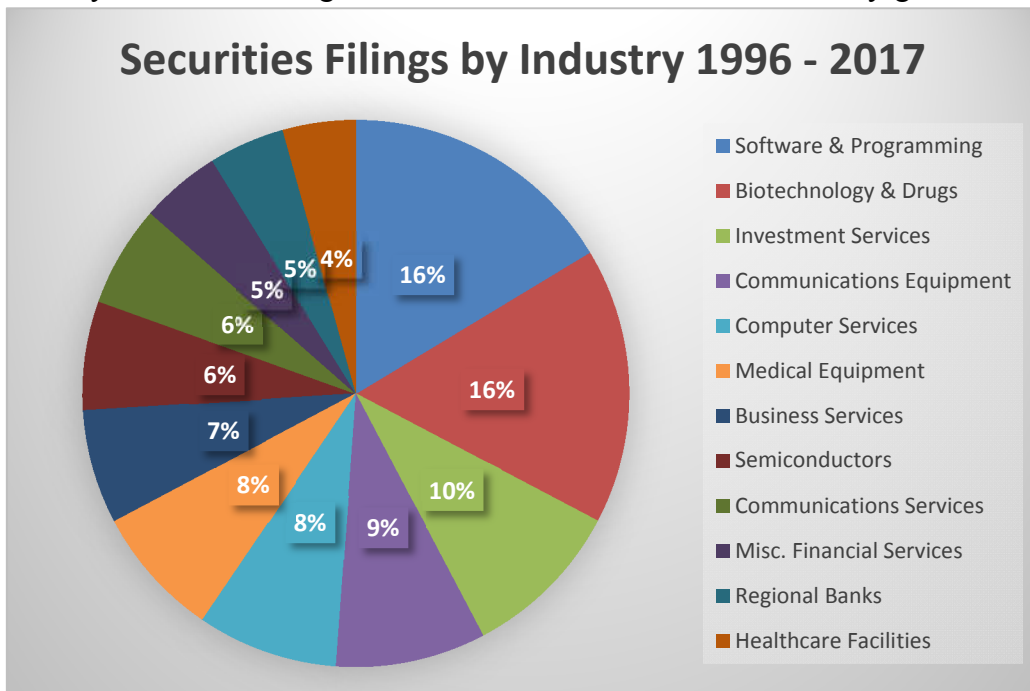


Figure 1 | Source: Stanford Securities Class Action Clearinghouse

¹ ISS Securities Class Action Services, *The Top 50 of 2017*: <https://www.issgovernance.com/file/publications/ISS-SCAS-Top-50-2017.pdf>

The number of securities lawsuits filed in federal court in 2017 reached a record high for the second straight year, totaling 412 filings which was a 50% increase over the previous year. In all, more than 8% of U.S. exchange listed companies were the subject of a securities class action suit last year, and approximately \$1.5 billion in settlements were recovered for investors.

Over the last 20 years, more than **\$96 billion** has been recovered for investors. Companies in the computer software and biotech industries were sued the most. (*see fig.1*)

Securities litigation is one of the most complex legal specialties. As a pension trustee with fiduciary responsibility, it's important that you be familiar with the basics. Learn more by reviewing the outcome of a recent precedent-setting Rosen Law Firm case. Click the link below:

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Historically, there has been a rise in securities class action filings after markets plunge, as investors look for valid reasons for the substantial downward revaluation of assets. Paradoxically, last year's record rate of securities fraud filings occurred during a period of thriving financial markets. The rise of price-volatile crypto-currencies and initial coin offerings (ICO's) that inadequately disclosed the risks involved led to the filing of suits in late 2017 which could have contributed to the increase in filings.

Your options for a recovery of loss:

Securities fraud cases typically take 2-3 years to reach a resolution, while some are dismissed or settled within the first year. It depends on the strength of the allegations, the complexity of the case and points of law at issue, among other factors. Until a class is certified by the judge in a class action suit, the pension fund is NOT represented by counsel unless it retains one. The fund may retain the counsel of its choice, but alternatively could remain an absent member of the class and do nothing until it receives a notice in the mail of a pending settlement. At that point trustees can file their "proof of claim" with the claims administrator to get their pro-rata share of the settlement funds that have been decreed by the court.

Taking Charge: As A Fiduciary, Should I Remain Passive or Take An Active Role?

Lead Plaintiff

An investor who agrees to be a lead plaintiff in the class action may derive substantial benefits over simply being a passive member of the class. This is because the lead plaintiff has a seat at the negotiating table and can participate in the plan of allocation for dividing up the funds recovered in settlement. The lead plaintiff looks out for the welfare of the class as a whole and can reject a proposed settlement if they deem that it's not in the best interests of the class or if they believe that a better settlement can be extracted. If the allegations against the defendant company are especially egregious, or the fund has a relatively large loss, trustees may strongly consider a lead plaintiff role to ensure their fund's interests are protected.

Opt Out

Another alternative for the investor is to opt out of the class action and file their own individual action against the defendant company. An investor could potentially recover many times the amount that they would have recovered as a passive member of a class action, because their counsel is negotiating with the defendant company directly on their behalf only, rather than on behalf of the whole class of investors.

Some of the most respected and sophisticated institutions in the world are also some of the most active in filing securities litigation lead plaintiff motions:

- Abu Dhabi Investment Authority
- Arkansas Teacher Retirement System
- Houston Municipal Employees' Pension System
- TIAA-CREF Funds
- New York City Employees' Retirement System

Typically, plaintiff's counsel will wait until the class action case survives the defendant company's "motion to dismiss" before filing an opt out suit to make sure the case has merit and is worth pursuing. No matter which option an investment manager selects, their image with pensioners/shareholders is enhanced by the knowledge that the fiduciaries are looking out for shareholders' interests and pursuing every dollar they have coming to them. In an era when many pension funds are underfunded, this is especially important.

Group Action

Many institutional investors are in constant communication with their peers, comparing notes on strategies, performance, etc. If you have peers who have also incurred a loss in the common stock or bonds of the same company due to allegations of corporate malfeasance, you may find a tactical advantage in banding together and forming a "group action" for your suit. Not only do cases with institutional investor plaintiffs garner higher settlements as a percentage of loss than cases with individuals as plaintiffs, but a group action composed of institutions signals to the judge that the case has strong merit. In these instances, a group action may be the way to proceed.

Caveat Emptor Environment

Despite an increasing amount of federal regulation, and the overarching, time-tested framework of the Securities Act of 1933 and Exchange Act of 1934 (which came out of the experience of the Great Depression) many public companies still find themselves running afoul of the law with their stock price getting punished as a result, leaving angry investors in their wake. Just a sampling of recent headlines demonstrates that securities fraud remains endemic to American capital markets:

Even more alarming is the reality that SEC enforcement actions declined 33% in fiscal year 2017², suggesting that the deterrent role of private securities litigation may be more important than ever.

The Wall Street Journal – May 2018: "Wells Fargo Settles Securities Fraud Class Action for \$480 Million"

Reuters – January 2018: "Petrobras to pay \$2.95 billion to settle U.S. corruption lawsuit"

Reuters – February 2018: "GE faces shareholder lawsuit over insurance shortfall, SEC probe"

Institutional investors, being large shareholders with significant influence over corporate management, are the key to maintaining oversight and transparency. The Rosen Law Firm has represented hedge funds, as well as labor union and public pension funds, and understands the practices most likely to bridge management and shareholder interests. Adoption of effective corporate governance principles through litigation and advocacy allows for greater productivity, shareholder value and transparency. For more information about our free portfolio monitoring for potential recoverable losses, contact us at 212.686.1060 or visit us at: www.rosenlegal.com.

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***Ranked 1st in the nation
for number of securities
class action settlements in
2017 by ISS Securities
Class Action Services.***



² Cornerstone Research, *SEC Enforcement Activity: Public Companies and Subsidiaries Fiscal Year 2017 Update*