ACCOUNTANTS' LIABILITY: CURRENT CHALLENGES

January 2012

Dana S. Douglas
Partner
+1 312 701 7093
ddouglas@mayerbrown.com

Brian J. Massengill
Partner
+1 312 701 7268
bmassengill@mayerbrown.com

Terri A. Mazur
Partner
+1 212 506 2680
tmazur@mayerbrown.com

Jonathan C. Medow
Partner
+1 312 701 7060
jmedow@mayerbrown.com

Stanley J. Parzen
Partner
+1 312 701 7326
sparzen@mayerbrown.com

Richard M. Rosenfeld
Partner
+1 202 263 3130
rrosenfeld@mayerbrown.com

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The Paper Chase:
SEC v. Deloitte Touche Tohmatsu CPA Ltd.

Richard M. Rosenfeld
Partner
+1 202 263 3130
rrosenfeld@mayerbrown.com

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What is it about?

- SEC subpoenas Deloitte Touche Tohmatsu CPA Ltd. ("DTT China") re: Longtop Financial Technologies Limited
  - SEC issued subpoena May 27, 2011 to Gibson Dunn, prior counsel to DTT China
- Jurisdiction: Longtop is a foreign private issuer whose American depositary shares (ADSs) traded on the NYSE from the date of its initial public offering in October 2007 until May 17, 2011
- NYSE halted trading prior to delisting Longtop's ADSs in August 2011
  - When trading was halted, Longtop's ADSs were priced at $18.93 per share with 57 million shares outstanding, resulting in a market capitalization of approximately $1.08 billion. At its trading high on November 5, 2010, the ADS were priced at $41.74 or a market cap of $2.38 billion

The SEC's Point of View

SEC v. DTT China

- **The Issue:**
  - DTT China has thus far not accepted service of the subpoena and therefore not responded
- **SEC's Action:**
  - SEC subpoena enforcement action
  - Filed in District Court in Washington, DC
    - Securities and Exchange Commission v. Deloitte Touche Tohmatsu CPA Ltd., File No. 1:11-mc-00512 (D.D.C. filed September 8, 2011)

Potential Consequenses of the SEC's Actions

- Fines
- Ban by the SEC: Rule 102(e) proceedings potentially ban service providers (accountants, lawyers) from appearing before the Commission
  - Period of time or lifetime
  - Effectively ends auditing of companies who wish to raise capital in the US
- Ban by the Public Company Accounting Oversight Board (PCAOB): PCAOB involvement could potentially result in sanctions including de-registration

Where the Matter Stands

- Regularly new developments: New papers filed last week
- Order to Show Cause
  - SEC moved for an Order to Show Cause why DTT China should not be required to respond to the SEC's subpoena
    - Court ordered DTT China to appear before the court to show cause why it should not be ordered to produce documents
    - SEC to serve order on DTT China by "delivery upon their counsel"
- DTT China's Motion to Clarify Order
  - Seeks clarification on whether court intended to address service
  - SEC opposes, claiming court's order is clear
  - No ruling by the court
    - Parties continue to negotiate briefing schedule

Significance of Order to Show Cause

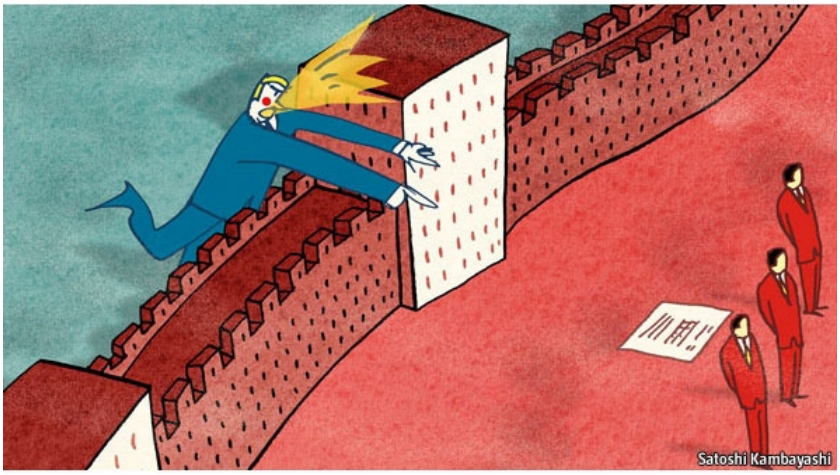
- Judges Ruling: Procedural Ruling
  - Held: Despite acknowledging that DTT China has not been served, the application can go forward – service not a prerequisite
  - One persuasive factor was that DTT China had US counsel and was not prejudiced because SEC's counsel:

    "[has] had numerous conversations with . . . counsel for the [DTT China,]" "advise[d] him of the pending filing [of the application for an order to show cause and to enforce a subpoena[,]" and "sent him copies of the SEC's filings via e-mail[.]" Moreover, the court observed, the SEC had represented that DTT China's counsel "was seated in the gallery of the courtroom" at a status hearing.
  - DTT China must appear to argue the show cause hearing explaining why it should not be required to respond to the SEC's subpoena

What this means and what comes next in this case

- The critical issues are service and appearance, and the stakes are very high
  - DTT China has thus far refused service
  - The SEC's position would make it possible to serve counsel in the US for non-US auditors (and possibly other entities)
- If the show cause order stands as ordered, DTT China will be forced to appear through US counsel and therefore forced to admit they have US counsel
  - Thus, if the SEC's position stands, a subpoena can simply be served on US counsel

What is Really Driving the SEC?



The Bigger Picture: SEC v. China

- Longtop is one of some reportedly 55 to 60 open Enforcement Division financial fraud investigations of US listed Chinese companies
- Approximately 300 Chinese companies are publicly traded in the US. At least 159 entered US capital markets through reverse mergers since 2007
- More than two dozen listed Chinese companies trading in the US have announced auditor resignations or accounting issues since March 2011
- "Deloitte is just the unfortunate one that got hit first," Paul Gillis, a visiting professor of accounting at Peking University

This becomes political

SEC v. Chinese State Secrets and Soverignty

- "Compliance with an SEC subpoena is not an option, it is a legal obligation," said Robert Khuzami, the director of the SEC's Division of Enforcement. "Subpoena recipients who refuse to comply should expect serious legal consequences"

  v.

- DTT China issued a press release stating: "As a matter of national sovereignty, the law of the People's Republic of China precludes our firm from producing the requested documents to a foreign regulator without approval from China Securities Regulatory Commission"

SEC and PCAOB Knew This Was Coming

- Chinese member firms of Big-4 networks, as well as other auditing firms, on their Form 1 initial registrations, and subsequent Form 2s, have advised the PCAOB that they could not provide a blanket consent to comply with all PCAOB requests for documents because of legal conflicts with China law
  - DTT China also provided a legal opinion stating same
- The registration statements were accepted by the PCAOB

Getting From Here to There

- PCAOB officials have visited China multiple times, trying (unsuccessfully, so far) to get access to inspect China-based firms auditing US-listed companies
  - Talks have recently restarted
- American and foreign regulators have resolved disagreements before, recently the PCAOB announced a new accord with Norway after being blocked from inspections there since 2008

Resolution of SEC and PCAOB v. China

- This issue is difficult and the posturing has not helped
- China is notoriously difficult about sovereignty
- China fears the flood-gate effect
- But both sides also have a clear incentive to reach an agreement
  - SEC must fight fraud under its mandate
  - PCAOB's mandate requires inspection of registered firms in China
  - China needs financing for Chinese firms and the ability to list on recognized and serious markets
- Without an agreement, investors will continue to wonder whether they can trust financial statements of Chinese companies

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Litigation Developments: China Reverse Merger Companies

Terri A. Mazur
Partner
+1 212 506 2680
tmazur@mayerbrown.com

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Overview

- Securities class actions have been filed against more than 40 China companies since 2010 (33 filings in 2011) , most of which went public in the U.S. through reverse mergers ("China Reverse Mergers" or "CRMs")
- Filings against CRMs may be subsiding: while there were 24 actions filed against CRMs in the first half of 2011, only 9 such actions were filed between July and December 2011

Nature of the Allegations

- Class action complaints against CRMs have alleged:
  - GAAP violations (more than in other cases)
  - Misrepresentations in financial statements
  - Unreliable financial statement disclosures
  - False forward-looking statements
  - Internal control weaknesses
  - Restatements
  - Rule 10b-5 violations
- Auditors have been named in only 4.7% of the CRM actions

Do Discrepancies between Chinese Financial Filings and SEC Filings State a 10b-5 Claim?

- A number of the CRM cases alleging misrepresentations in financial statements assert purported discrepancies between the China companies' filings with the Chinese State Administration for Industry and Commerce ("SAIC") and State Administration of Taxation ("SAT") as compared with their U.S. SEC filings as a basis for claims under the Exchange Act Section 10(b) and Rule 10b-5
  - Plaintiffs often rely on reports published by interested short-sellers of CRMs' stock (such as the aptly named short-seller Muddy Waters) who purport to expose fraud in the CRMs' business operations and discrepancies in their PRC and US SEC filings
- To date, there have been five decisions on motions to dismiss Rule 10b-5 claims (and/or claims under Sections 11 and 20(a)) against CRMs
- Courts are split on whether such discrepancies are sufficient to state a Rule 10b-5 claim and plead misstatement or fraud in U.S. GAAP financial statements

PRC Filings vs. U.S. SEC Filings

- SAIC is the business registrar in China; its primary purpose is for public filings of articles of incorporation, ownership, etc.
  - The SAIC does not audit or review financial statements submitted with China companies' annual filings (Roth Capital Partners, Industry Note (July 12, 2010) ("Roth Note"))
- Financial data in SAT filings appear to be more reliable than SAIC filings due to audit and enforcement actions of the Chinese tax authorities, but still may not match U.S. filings (Roth Note at 1.)

PRC Filings vs. US SEC Filings

- CRMs' SEC filings reported significantly larger net revenue and income than they reported in their SAIC and SAT filings, in the cases at issue
- PRC filings may not always match US filings for a variety of legitimate reasons, including:
  - Different accounting principles (financial reporting vs. tax reporting, PRC accounting methods and standards vs. US GAAP standards for financial reporting)
  - Consolidated reporting vs. single entity reporting
  - Different scopes
  - Multiple jurisdictions

PRC Filings vs. US SEC Filings

- CRMs also tend to under-report earnings in their SAIC filings, purportedly "to avoid disclosing their operating metrics to customers, suppliers, and competitors, which could adversely impact their business." (Roth Note at 2.)

PRC Filings vs. US SEC Filings

- Tax Reporting in China ("SAT" Filings)
  - Tax filings are more comprehensive than SAIC filings
  - Companies are required to submit audited financial statements
  - Unlike the SAIC, local tax bureaus frequently audit these reports and levy fines
  - Tax filings are highly confidential and are not available to research analysts, investors or market participants
  - SAIC and tax bureaus maintain separate databases and have distinct areas of authority and function, and there is "minimal (if any) inter-agency communication." (Roth Note at 4.)
  - PRC tax filings also may not match SEC filings based on a number of legitimate factors, including, among others: different accounting principles, consolidation approaches, offshore business aspects, and treatment of tax concessions (Id.)

The Decisions

- Discrepancies Between in SAIC and SEC Filings Filings State a Claim:
  - Dean v. China Agritech, Inc. (C.D. Cal. Oct. 27, 2011), In re China Education Alliance, Inc. Securities Litigation (C.D. Cal. Oct. 11, 2011), and Henning v. Orient Paper, Inc. (C.D. Cal. July 20, 2011): in these cases, the courts held that allegations that the CRMs' revenue and income in their U.S. filings were "demonstrably higher" than those reported in their Chinese filings adequately pleaded a false statement and gave rise to, along with other allegations, a strong inference of scienter, and thus stated claims under Section 10(b) and Rule 10b-5. The court in China Agritech rejected defendants' arguments that different accounting principles explained the discrepancies between the SAIC and SAT filings and U.S. SEC filings as "unpersuasive." (2011 WL 5148598 at *5.)
- Discrepancies Do Not State a Claim:
  - Katz v. China Century Dragon media, Inc. (C.D. Cal. Nov. 30, 2011): the court dismissed plaintiffs' claims under Sections 11 and 12(a)(2) of The Securities Act of 1933 for failure to plead falsity with sufficient specificity with respect to their claims that China Dragon's profit and revenue reports in its SEC filings – rather than its SAIC filings – were false, holding: "Although Plaintiffs plead the SAIC numbers differ from the SEC numbers, this is 'merely consistent with' the SEC numbers' being false, and does not suffice to make that claim plausible."

Other Decisions

- In re China North East Petroleum (S.D.N.Y. Oct. 6, 2011): the court granted defendants' motion to dismiss, holding that plaintiff Acticon did not suffer any economic loss where it held all of its shares for months after the final allegedly corrective disclosure was made on September 1, 2010. During that time, Acticon had several opportunities to sell its shares at a profit, but chose not to. Thus, its claimed losses could not be imputed to any alleged misrepresentations

PCAOB 2010 Inspection Results and Standard-Setting Agenda

January 2012

Brian J. Massengill
Partner,
+1 312 701 7268
bmassengill@mayerbrown.com

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PCAOB Inspections of Big 4 – 2010 Results

PCAOB Commentary on Inspection Results

Independent inspections by the PCAOB began only eight years ago. Yet, in sharp contrast to the profession's quarter century of self examination, **PCAOB inspections have identified scores of problems in audits by firms in each of the large accounting firm networks**, and other firms that audit public company financial statements.

Source: http://pcaobus.org/News/Speech/Pages/04042011_DotyLookingAhead.aspx

PCAOB Inspections of Big 4 – 2010 Results

PCAOB Commentary on Inspection Results

Although the PCAOB's 2010 inspection reporting cycle is not yet complete, so far **PCAOB inspectors have continued to identify significant deficiencies** related to the valuation of complex financial instruments, inappropriate use of substantive analytical procedures, reliance on entity level controls without adequate evaluation of whether those processes actually function as effective controls, and several other issues. **PCAOB inspectors have also identified more issues than in prior years.**

In any event, the Board is troubled by the volume of significant deficiencies, especially in areas identified in prior inspections. The PCAOB is working on several initiatives to drive improvements in audit quality.

Source: http://pcaobus.org/News/Speech/Pages/04062011_DotyTestimony.aspx

PCAOB Inspection of Big 4 – 2010 Results

Comparison to 2008 and 2009 Results

		2008 Inspection	2009 Inspection	2010 Inspection
Deloitte	Audits Reviewed	N/A	73	57
	Problems Identified	7	15	26
	Restatements/Adjustments	1/"some"	0/1	0/1
E&Y	Audits Reviewed	N/A	58	62
	Problems Identified	8	5	13
	Restatements/Adjustments	2/"some"	0/"some"	0/0
KPMG	Audits Reviewed	N/A	60	52
	Problems Identified	9	8	12
	Restatements/Adjustments	0/"some"	0/"some"	0/1
PWC	Audits Reviewed	N/A	76	71
	Problems Identified	6	9	28
	Restatements/Adjustments	0/"some"	0/1 & "some"	2/1

PCAOB Inspections of Big 4 – 2010 Results

What could be driving the rhetoric?

- Stated reason of poor results
- Chairman Doty term started January 2011
- Ambitious regulatory agenda that would have significant impacts on auditors

PCAOB's Ambitious Standard-Setting Agenda

- **The November 2011 Agenda directly links many of the items to inspection results. For example:**

  "**Issues identified through the inspection of audits conducted during the economic crisis indicate that there is a need for the Board to address certain of its standards** including the auditor's reporting model, quality control, fair value measurements, and the use of specialists. Additionally, the standard-setting projects on quality control, part of the audit performed by other auditors, and identification of other public accounting firms or persons not employed by the auditor in the auditor's report will consider challenges pertaining to PCAOB inspections of accounting firms based outside the US."

- **Also, foreshadows things to come:**

  "OCA works with the Division of Registration and Inspections to monitor current accounting firm practices with respect to independence, including non-audit services being provided to audit clients, to determine if any additional rulemaking is necessary in the area of ethics and independence."

PCAOB, Office of the Chief Auditor, Standard-Setting Agenda (November 2011).

PCAOB's Ambitious Standard-Setting Agenda

- **Doty's comments on the overall agenda:**

  "...**they are intended to spur debate over how to change auditing, from a culture that emphasizes client service to a culture that emphasizes public service**. Our oversight should foster conduct consistent with the franchise our federal securities laws accord the audit profession.

  I am mindful that culture does not change quickly. It would be naïve to think that merely changing the auditor's report would trigger the culture change we need. **This is why I have advocated a holistic approach aimed at enhancing the credibility and transparency of audits as well as their relevance**."

  James R. Doty, Chairman, PCAOB,
  PCAOB Open Board Meeting, Washington, DC (June 21, 2011).

PCAOB 2010 Inspection Results and Standard-Setting Agenda

PCAOB's Ambitious Standard-Setting Agenda

1. Sixteen items on standard setting agenda, nine of which will not be addressed today (e.g., auditors of brokers and dealers; confirmations; related parties; going concern)

2. Communications with Audit Committee (Matter No. 30)

- Proposed Auditing Standard issued (March 2010)
- Re-proposed standard for public comment (December 2011)
- Comment period ends (February 29, 2012)
- Adopt final standard (Q2 2012) with potential effective date for fiscal years beginning after December 15, 2012

PCAOB's Ambitious Standard-Setting Agenda

3. Auditor's Reporting Model (Matter No. 34)

- Concept Release issued (June 2011) – modify auditor reporting model to "increase transparency and relevance"
- Four proposals:
  - Auditor's Discussion and Analysis
  - Required and expanded use of emphasis paragraphs
  - Audit for assurance on information outside of financial statements
  - Clarification of language in the standard auditor's report
- Roundtable (September 2011)
- Proposed Auditing Standard (Q2 2012)
- Adopt final standard or re-propose (Q4 2012)

PCAOB 2010 Inspection Results and Standard-Setting Agenda

PCAOB's Ambitious Standard-Setting Agenda

4. Part of Audit Preformed by Other Auditors (Principal Auditor)

- Issue proposed standards for public comment (Q1 2012)
- Adopt final standard or re-propose (Q4 2012)

5. Assignment and Documentation of Firm Supervisory Responsibilities (Failure to Supervise) (Matter No. 31)

- Concept Release issued (August 2010)
- Staff drafting proposed amendments to Quality Control Standards
  - Address assignment and documentation of firm supervisory personnel
- Issue proposed amendments for public comment (Q1 2012)
- Adopt final amendments or re-propose (Q3 2012)

6. Quality Control Standards (Matter No. 31)

- Issue proposed standards for public comment (Q3 2012)
- Adopt final standards or re-propose (Q1 2013)

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PCAOB's Ambitious Standard-Setting Agenda

7. Auditor Independence, Objectivity and Professional Skepticism

- **Concept:** Release on auditor independence and audit firm rotation

PCAOB 2010 Inspection Results and Standard-Setting Agenda

PCAOB's Ambitious Standard-Setting Agenda

7. Auditor Independence, Objectivity and Professional Skepticism

- **Chairman Doty:**
  "The PCAOB has now conducted annual inspections of the largest audit firms for eight years. Our inspectors have reviewed more than 2,800 engagements of such firms and discovered and analyzed hundreds of cases involving what they determined to be audit failures. . . . **Based on this work, I believe it is incumbent on the PCAOB to take up the debate about firm tenure and examine it, with rigorous analysis and the weight of evidence in support and against**. I don't have a predetermined idea as to whether the PCAOB ultimately should adopt term limits. **My only predilection is that the PCAOB deepen the analysis of how we can better insulate auditors from client pressure and shift their mindset to protecting the investing public**." James R. Doty, Chairman, PCAOB, SEC & Financial Reporting Institute 30th Annual Conference (June 2, 2011).

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PCAOB's Ambitious Standard-Setting Agenda

7. Auditor Independence, Objectivity and Professional Skepticism

- **Premise:**
  - Problem with auditing
  - Caused by lack of independence, objectivity and professional skepticism
- **Theory:** "mandatory audit rotation might bolster the auditor's willingness to resist management pressure and to bring a fresh look at the company's accounting."

PCAOB 2010 Inspection Results and Standard-Setting Agenda

PCAOB's Ambitious Standard-Setting Agenda

7. Auditor Independence, Objectivity and Professional Skepticism

- **Reaction to Proposal:** Comment period ended December 14, 2011. Received 602 comment letters: accounting firms, accounting industry groups, companies, audit committees.
- **Next Steps:**
  - Roundtable in Q1 2012
  - "Board to consider next steps" in Q2 2012
- **Other Proposals for auditor rotation:**
  - European Union
  - India

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PCAOB's Ambitious Standard-Setting Agenda

8. Audit Transparency – Identification of Engagement Partners and Other Firms or Persons

- **Purpose:** Improve transparency of audits by disclosing additional information
- **Disclosure of the Engagement Partner's name in:**
  - Audit report
  - Form 2 – Annual Report Form
  - * Not proposing signing audit report by name

PCAOB's Ambitious Standard-Setting Agenda

8. Audit Transparency – Identification of Engagement Partners and Other Firms or Persons

- **Disclosure of accounting firms and other persons who took part in the audit:**
  - Name of firm and location of headquarters
  - Explanatory paragraph in audit and appendix
  - 3% threshold measured based on hours incurred
- **Likely to be enacted:**
  - Received 38 comment letters on proposal
  - Target adoption Q3 2012
  - Maybe effective for 2012 year-end audit cycle

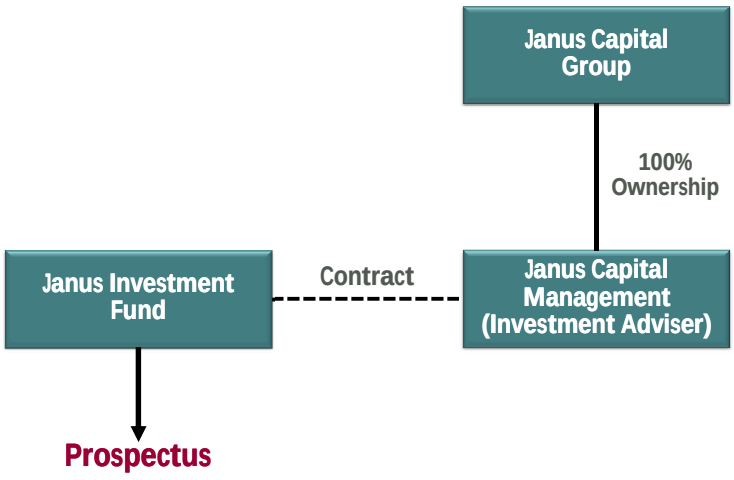
Janus v. First Derivative Traders:

The First Six Months

January 2012

Jonathan C. Medow
Partner
+1 312 701 7060
jmedow@mayerbrown.com

Janus v. First Derivative Traders,
131 S.Ct. 2296 (2011)



The Holding

"For purposes of Rule 10b-5, the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it."

131 S.Ct. at 2302

An Apparent "Clean" Win For The Defense

"We draw a clean line. . . . [T]he maker is the person or entity with ultimate authority over a statement and others are not."

131 S.Ct. at 2302 n.6

The Facts:

- All of the Funds officers were also officers of JCM. Id. at 2299
- "First Derivative and its amici persuasively argue that investment advisers exercise significant influence over their client funds." Id. at 2304

Potential Ambiguity

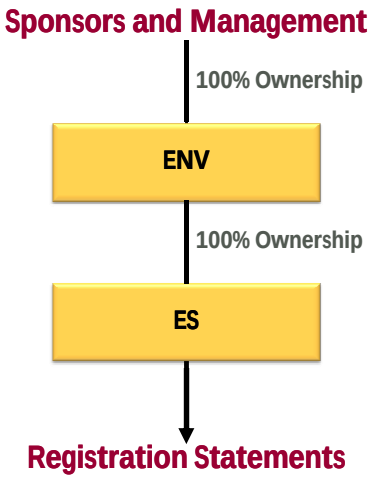
"For purposes of Rule 10b-5, the maker of a statement is the person or entity with **ultimate authority** over the statement, including its content and whether and how to communicate it.

. . . . . .

And in the **ordinary case**, attribution within a statement or **implicit from surrounding circumstances** is **strong evidence** that a statement was made by–and only by–the party to whom it is attributed."

131 S.Ct. at 2302

City of Roseville Employees' Retirement Sys. v. EnergySolutions, Inc., 2011 WL 4527328 (S.D.N.Y. Sept. 30, 2011)



City of Roseville Employees' Retirement Sys. v. EnergySolutions, Inc.,
2011 WL 4527328 (S.D.N.Y. Sept. 30, 2011)

De Facto Ultimate Authority Found

- ENV was sole owner of ES pre-IPO/selling stockholder in the IPO
- ENV to retain control post-IPO
- Registration Statement said ES would be "controlled company" post-IPO
- Sponsors controlled ES through ENV – "ENV therefore had 'ultimate authority' over the two Offerings, as required by Janus." (*18)

"Janus recognized that attribution could be 'implicit from the surrounding circumstances.' Here, where the Registration Statements contain so many indicia of control, the lack of an explicit statement that ENV was speaking through the Registration Statements does not control the answer to the question of whether it made those statements. A reasonable jury could find that, on the facts alleged here, ENV's role went well beyond that of 'a speechwriter draft[ing] a speech.' . . ." (*18)

Munoz v. China Expert Technology, Inc.,
No. 1:07-cv-10531-AKH (S.D.N.Y. Nov. 4, 2011)

- PKF Hong Kong audited financial statements of China-based registrant
- PKF New York served as the Filing Reviewer per Appendix K
- PKF New York's motion to dismiss was denied, notwithstanding Janus

Munoz v. China Expert Technology, Inc.,
No. 1:07-cv-10531-AKH (S.D.N.Y. Nov. 4, 2011)

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
China Expert Technology, Inc.

We have audited the accompanying consolidated balance sheet of China Expert Technology, Inc. and its subsidiaries as of December 31, 2004 and the related consolidated statements of income, stockholders' equity and cash flows for each of the two years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of China Expert Technology, Inc. and its subsidiaries as of December 31, 2004 and the consolidated results of their operations and their cash flows for each of the two years in the period ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America.

PKF
Certified Public Accountants
February 22, 2005, except for the restatement discussed in Note 2 to the consolidated financial statements, as to which the date is March 10, 2006

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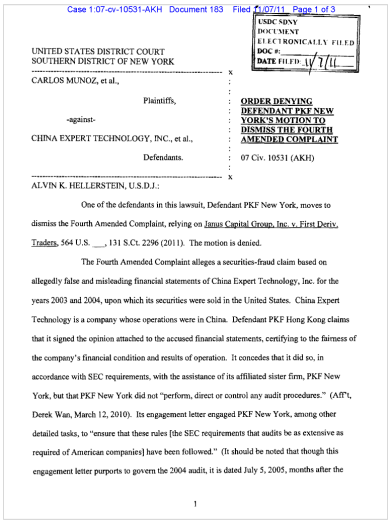
Munoz v. China Expert Technology, Inc.,
No. 1:07-cv-10531-AKH (S.D.N.Y. Nov. 4, 2011)



Case 1:07-cv-10531-AKH Document 183 Filed 11/07/11 Page 1 of 3

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DOC #:
DATE FILED: 11/7/11

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

CARLOS MUNOZ, et al.,

Plaintiffs,

-against-

CHINA EXPERT TECHNOLOGY, INC., et al.,

Defendants.

ORDER DENYING DEFENDANT PKF NEW YORK'S MOTION TO DISMISS THE FOURTH AMENDED COMPLAINT

07 Civ. 10531 (AKH)

ALVIN K. HELLERSTEIN, U.S.D.J.:

One of the defendants in this lawsuit, Defendant PKF New York, moves to dismiss the Fourth Amended Complaint, relying on Janus Capital Group, Inc. v. First Deriv. Traders, 564 U.S. ___, 131 S.Ct. 2296 (2011). The motion is denied.

The Fourth Amended Complaint alleges a securities-fraud claim based on allegedly false and misleading financial statements of China Expert Technology, Inc. for the years 2003 and 2004, upon which its securities were sold in the United States. China Expert Technology is a company whose operations were in China. Defendant PKF Hong Kong claims that it signed the opinion attached to the accused financial statements, certifying to the fairness of the company's financial condition and results of operation. It concedes that it did so, in accordance with SEC requirements, with the assistance of its affiliated sister firm, PKF New York, but that PKF New York did not "perform, direct or control any audit procedures." (Aff't, Derek Wan, March 12, 2010). Its engagement letter engaged PKF New York, among other detailed tasks, to "ensure that these rules [the SEC requirements that audits be as extensive as required of American companies] have been followed." (It should be noted that though this engagement letter purports to govern the 2004 audit, it is dated July 5, 2005, months after the

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Munoz v. China Expert Technology, Inc.,
No. 1:07-cv-10531-AKH (S.D.N.Y. Nov. 4, 2011)

In the case at hand, the relationship is not so clear-cut. Plaintiffs have properly pleaded that PKF New York exercised more than assistance. According to their complaint, not only did PKF New York participate in the audits, but it also exercised authority over what was said in the audit opinion. Indeed, the PKF New York engagement letter specifically stated that PKF New York would "review the entire filings with the SEC for compliance." Furthermore, according to the complaint, PKF New York's Managing Director gave final approval of the opinions before they were signed, and then the audit documents were simply signed "PKF" with no indication as to which corporate entity issued them. These allegations, and others, create genuine issues of fact as to whether PKF New York explicitly or implicitly controlled sufficiently—and thus "made"—the statements in question. To determine such issue, discovery is required. PKF New York may renew its motion after discovery closes to allow me to re-examine the issue upon all the relevant facts.

PCAOB Rulemaking Docket Matter No. 29

"Accordingly, the Board is soliciting comment on a series of amendments to PCAOB standards that would:

- Require the audit report to disclose the name of the engagement partner responsible for the most recent period's audit,
- Require registered firms to disclose in their PCAOB annual report on Form 2 the names of the engagement partner for each audit report already required to be reported on the form, and
- Require disclosure in the audit report about other persons and independent public accounting firms that took part in the most recent period's audit."

PCAOB Release No. 2011-007 at 3

PCAOB Rulemaking Docket Matter No. 29

Independent Auditor's Report

We have audited the accompanying balance sheets of X Company as of December 31, 20X2 and 20X1, and the related statements of income, retained earnings, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. The engagement partner responsible for the audit resulting in this report was [name].

[Signature]

[Date]

PCAOB Rulemaking Docket Matter No. 29

"The engagement partner responsible for the audit resulting in this report was [name]"

Liability Ramifications:

Attribution, which can be "implicit from surrounding circumstances," is "strong evidence that a statement was made by—and only by—the party to whom it is attributed."

Janus, 131 S.Ct. at 2302

"Without attribution, there is no indication that Janus Investment Fund was quoting or otherwise repeating a statement originally 'made' by JCM.

. . . . . .

More may be required to find that a person or entity made a statement indirectly, but attribution is necessary."

Id. at 2305 n.11

PCAOB Rulemaking Docket Matter No. 29

"The engagement partner responsible for the audit resulting in this report was [name]"

Liability Ramifications:

"[I]t seems unlikely that the mere identification of the audit engagement partner in the body of an audit report will be deemed to be a 'statement' by the audit engagement partner for purposes of the federal securities laws making him or her primarily responsible for all of the contents of the report."

Statement of PCAOB Board Member Lewis H. Ferguson, at 3
October 11, 2011

Janus v. First Derivative Traders

PCAOB Rulemaking Docket Matter No. 29

"The engagement partner responsible for the audit resulting in this report was [name]"

Liability Ramifications:

"If the engagement partner does not sign the audit report, but is merely named in it, there would seem to be a basis for arguing, under Janus, that he or she was not 'making' the statements in the report."

Statement of PCAOB Board Member Daniel L. Goelzer, Appendix
October 11, 2011

PCAOB Rulemaking Docket Matter No. 29

"The engagement partner responsible for the audit resulting in this report was [name]"

Liability Ramifications:

"I would be surprised if the bar took the position that this changed the law or changed the liability of an engagement partner in some fundamental respect, but that is the question."

Comments of PCAOB Chairman James R. Doty
Tr. of November 9, 2011 Standing Advisory Group Meeting, at 319

"I have significant reservations about whether naming the engagement partner in the audit report could increase the liability faced by engagement partners."

Statement of PCAOB Board Member Jay D. Hanson, at 3
October 11, 2011

Janus v. First Derivative Traders

PCAOB Rulemaking Docket Matter No. 29

"The engagement partner responsible for the audit resulting in this report was [name]"

Liability Ramifications:

"We believe that a proper application of this case law to the Board's proposed decision to disclose the engagement partner's name should not result in an increase in the liability of the engagement partner. However, to date no court has considered this argument and we believe it is conceivable that some courts may read this case law differently. Furthermore, plaintiffs can be expected to assert claims against named engagement partners despite the Janus decision. Until case law becomes settled on these matters, we believe that the cost to defend such claims could be significant."

KPMG LLP Comment Letter, January 5, 2012, at 5

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PCAOB Rulemaking Docket Matter No. 29

"The engagement partner responsible for the audit resulting in this report was [name]"

Liability Ramifications:

"Although this standard should be helpful to individual auditor defendants, the case law under Janus is just now developing. If the PCAOB's rule were adopted, a plaintiff could cite the audit report's assertion that a particular audit partner was 'responsible' for the issuance of the audit report and, hence, he or she had 'ultimate authority' or 'control' over the report—possibly sufficient to survive a motion to dismiss under Janus as a 'maker' of a false or misleading statement. This has happened already. [citing Munoz]."

Ernst & Young LLP Comment Letter, January 9, 2012, at 10

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The Subjective Falsity Pleading Requirement

The Emerging Consensus of the Necessity for Subjective Falsity Pleading As to Some Matters Alleged In Section 11 Securities Claims

Stanley J. Parzen
+1 312 701 7326
sparzen@mayerbrown.com

January 2012

The Language of Section 11

"In case any part of the registration statement, when such part became effective, contained an **untrue statement of a material fact or omitted to state a material fact** required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security may . . . sue--"

- Every person who signed the registration statement;
- Every director or partner in the issuer at the time of filing;
- Every accountant who has consented to being named as having prepared or certified any part of the registration statement with respect to the matters prepared or certified;
- Every underwriter with respect to the security.

Suits Brought Against Accounting Firms

What is based on opinion and subject to subjective falsity?

What is a "material fact"?
In a Section 11 claim, a **belief or opinion** communicated by a defendant may be a material fact.

- When asserting a claim based on a belief or opinion, many courts have held that liability exists only to the extent that the statement of belief or opinion was **both objectively false and subjectively false** (disbelieved by the defendant at the time it was expressed)

Fait v. Regions Fin. Corp. (2d Cir. 2011)
(citing Virginia Bankshares v. Sandberg (U.S. 1991).

Fait v. Regions Financial Corporation (2d Cir.)

Facts: Plaintiffs allegedly purchased Regions' securities following Regions' acquisition of AmSouth Bancorp

- The registration statement incorporated Regions' financial statements, upon which E&Y had issued an unqualified audit opinion
- Plaintiffs claimed the financial statements contained material misstatements on two items:
  - Goodwill allocation from the AmSouth acquisition; and
  - The adequacy of Regions' loan loss reserves.

  Note: that both goodwill and loss reserves are inherently subjective and, to a large extent, predictive.

Fait v. Regions Financial Corporation (2d Cir.)

The Second Circuit Held:

- The goodwill constitutes a statement of opinion and loan loss reserves reflect management's opinion or judgment about what, if any, portion of amounts due on the loans ultimately might not be collectible
  - The court concluded both determinations were "inherently subjective"
- Actions based on matters of opinion are actionable only if the statements:

  "misstate the opinions or belief held, or, in the case of statements of reasons, the actual motivation for the speaker's actions, and are false or misleading with respect to the underlying subject matter they address"
  - Because plaintiffs had failed to allege subjective falsity, the Second Circuit affirmed the district court's dismissal of the Section 11 claim

Historical Authority for Subjective Falsity Analysis

Shortly after the Securities Act of 1933 was enacted, William O. Douglas (named to the SEC in 1934 and to the Supreme Court in 1939) observed that some parts of a financial statement may be "within the realm of opinion"

William O. Douglas & George E. Bates,
The Federal Securities Act of 1933,
43 YALE L.J. 171 (1933)

So the view that certain balance sheet items are matters of opinion has historical support.

Other Possible Applications of Subjective Falsity Analysis

- **Loan Loss Reserves** – Belmont Holdings v. SunTrust Banks (N.D. Ga.). Note: OTTI can well fit within this category or be close enough to it to be subject to the rule as would be property and casualty loss reserves
- **Valuation of Mortgage-Backed Assets and Decision on When to Write Them Down** – In re Barclays Bank Sec. Litig. (S.D.N.Y.)
- **Assertion that Acquisition is in Shareholders' Best Interest** – Flake v. Hoskins (D. Kan.)
- **Appraisals** – Tsereteli v. Residential Asset Securitization Trust (S.D.N.Y.)
- **Securities Ratings** - Tsereteli v. Residential Asset Securitization Trust (S.D.N.Y.)
- **Fairness Opinion** – In re Global Crossing Sec. Litig. (S.D.N.Y.); Freedman v. Value Health (Conn.)
- **Statements about Future Cash Flow and Asset Values** – In re Thornburg Mortg. Sec. Litig. (D.N.M.)

Counter-Arguments Raised to Subjective Falsity and Responses

- Subjective falsity does not apply to Section 11 claims
  - Courts in multiple circuits have applied the Supreme Court language of Virginia Bankshares (a Section 14 case) to Section 11 cases
- Auditors "certify" the financial statements
  - Auditors issue opinions on the financial statements and perform audit procedures to provide a reasonable basis for that opinion
  - The auditor is liable only for that portion of the registration statement for which it consents and the consents states it is only the report for which consent is given
  - Although, some cases do use the word "certify"

Counter-Arguments Raised to Subjective Falsity and Responses

- Whether financial statements complied with GAAP is an issue of fact, not opinion, because GAAP compliance can be objectively determined
  - Auditors issue an opinion indicating they believe the financial statements comply with GAAP
  - Further, the issue is what the balance sheet item is not the report
  - Compliance with GAAP permits a multitude of results—there is no one right answer

Counter-Arguments Raised to Subjective Falsity and Responses

- Liability stands as long as plaintiffs allege that the auditor could not have reasonably believed the statements of opinion. Put differently, all that is required is objective falsity
  - Conclusory allegations are not enough. Virginia Bankshares held plaintiffs must establish both defendant's:

    "disbelief, or undisclosed belief or motivation" and provide "objective evidence . . . that the statement also expressly or impliedly asserted something false or misleading about its subject matter"
  - Some courts have not been clear about the subjective falsity requirement pre-Virginia Bankshares
  - The better view of the cases is that both types of falsity are required

Counter-Arguments Raised to Subjective Falsity and Responses

- The Western District of Washington held in In re Washington Mutual Sec. Litig. that a bank's loan loss allowance was a "statement of fact"
  - This is what the district court held but no court has followed the WaMu decision and it has been expressly rejected by other courts
  - The court in WaMu relied on In re AOL (S.D.N.Y.), which would no longer be good law after the Second Circuit's decision in Fait

    Note: Other courts have referenced only the GAAP requirement but the subjective falsity issue was not raised in those cases

Subjective Falsity in In re Lehman Brothers (S.D.N.Y.)

Application of the Subjective Falsity Requirement to The Audit Report as Opposed to the Balance Sheet Item (Section 10 and Section 11 case)

- At issue was E&Y's opinion that its audit complied with GAAS and that Lehman's financial statements complied with GAAP
  - **Held:** "E&Y's statement regarding GAAS compliance inherently was one of opinion"
  - **Held:** "The representation in the auditor's standard report regarding fair presentation, in all material respects, in conformity with [GAAP] indicates the auditor's belief that the financial statements, taken as a whole, are not materially misstated"

The complaint failed to allege facts sufficient to warrant a finding that E&Y did not actually hold the opinions it expressed or that it knew that it had no reasonable basis for holding the opinions.

MAYER·BROWN

Dana S. Douglas
Partner
dsdouglas@mayerbrown.com
Chicago
Ph: +1 312 701 7093
Fax: +1 312 706 8662

Experience

Dana Douglas focuses on a wide range of complex commercial litigation and criminal matters, including professional liability litigation, antitrust litigation, post-merger shareholder litigation, post-closing disputes, contract disputes, partnership disputes and complex discovery matters. Dana also has represented witnesses in connection with federal criminal investigations and has defended indicted individuals and corporations.

In the professional liability field, Dana represents many major accounting firms in connection with a wide variety of claims brought by client and client successors, including claims related to allegedly negligent and fraudulent audit work. Dana also has provided representation to accounting firms in federal securities actions, as well as in other claims brought by third parties. Dana currently is representing a major accounting firm in connection with a federal regulatory investigation.

In the antitrust field, Dana has represented domestic and international corporations in price-fixing, market allocation, resale price maintenance and conspiracy cases. As a part of her litigation practice, Dana has extensive experience managing complex discovery projects.

Prior to joining Mayer Brown in 2002, Dana served as a law clerk to the Honorable Samuel A. Alito Jr., who then served on the US Court of Appeals for the Third Circuit.

Notable Engagements

- Representation of accounting firms and their audit partners in SEC and PCAOB investigations.
- Representation of PwCIL in *In re Satyam Computer Services, Ltd. Securities Litigation*, 09-MD-2027, SDNY.
- Participation in the briefing leading to significant decisions in favor of accounting firms and financial institutions. *See The People ex rel. v. Siemens Financial Services, et al.,* 387 Ill.App.3d 606 (2009); *FDIC v. Ernst & Young LLP*, 374 F.3d 579 (7th Cir. 2004); *Donnybrook Investments, Ltd. v. Arthur Andersen LLP*, 2006 WL 1049588 (N.D.Ill. 2006); *Baker O'Neal Holdings v. Ernst & Young LLP*, 2004 WL 771230 (S.D. Ind. 2004).
- Development and implementation of records retention policies and procedures for a major accounting firm's business lines, risk functions and administrative functions.
- Representation of the sellers of a construction company in a post-closing adjustment arbitration and related allegations of breaches of representations and warranties.
- Representation at arbitration of a real estate investment company in connection with a partnership dispute involving allegations of financial fraud. The representation involved the supervision of complex forensic accounting experts.

- Representation of a state pension fund and its employees in connection with a high-profile federal fraud investigation and trial.
- Representation of Arthur Andersen in a federal jury trial resulting in verdicts of 13 breaches on 13 claims against a fiduciary liability insurer and subsequent significant judgments and recoveries for defense and indemnity.

Education

University of Pennsylvania Law School, JD, 2001; Associate Editor, Journal of International Economic Law • Northwestern University, BA, with honors, 1998; Gamma Sigma Alpha

Admissions

- State of New York Supreme Court, Appellate Division, Third Judicial Department, 2011
- US District Court for the Central District of Illinois, 2008
- US District Court for the Eastern District of Wisconsin, 2007
- US District Court for the Northern District of Illinois, 2003
- US District Court for the District of Colorado, 2003
- US Court of Appeals for the Third Circuit, 2002
- Illinois, 2002

Publications

- "New York Court Reaffirms Strong In Pari Delicto Defense," Mayer Brown Legal Update, October 29, 2010
- "Fraud and Forbearance: State Courts Divided on Whether to Recognize Claims by Securities Holders," *Financial Fraud Law Report*, October 2010
- "Claims Against Accounting Firms – Implications of Merck & Co. v. Reynolds," Mayer Brown LLP, April 30, 2010
- "Illinois Appellate Court Resolves Issue of When Limitations Period for Accounting Malpractice Claim in a Tax Liability Case Begins to Run," Mayer Brown LLP, April 20, 2010
- "Parties that Settle with the US SEC May Face Greater Collateral Legal Risk," Mayer Brown LLP, April 15, 2010
- "A View from the Trenches - Four 'All American' Jury Concepts," (co-author with Alan Salpeter) *The 7th Circuit Rider* , 2006

Seminars & Presentations

- "Expanding Challenges Facing US Accounting Firms," Mayer Brown Seminar, June 9 & 16, 2011
- "Emerging Challenges Facing US Accounting Firms," Mayer Brown Seminar, February 15 & 24, 2011
- "The Great Debate – States' Rights and Immigration Enforcement," Chicago Inn of Court, January 12, 2011

Professional Activities

- Chicago Chapter of the American Inn of Court
- Member, American Bar Association: Professional Liability and Securities sections

MAYER·BROWN

Brian J. Massengill
Partner
bmassengill@mayerbrown.com
Chicago
Ph: +1 312 701 7268
Fax: +1 312 706 8741

Experience

Brian Massengill focuses his practice on the intersection of litigation with accounting and finance issues. He is the co-leader of the firm's Professional Liability practice group.

Brian brings his background as a Certified Public Accountant (license inactive), including eight years with a national accounting firm, to bear on his legal work. He devotes the majority of his practice to the defense of accounting firms and has represented national firms in a variety of matters including securities class actions, arbitrations, SEC and PCAOB investigations, and state accountancy board proceedings.

Brian's combined legal and accounting experience also enables him to serve clients in a variety of other contexts. He has represented companies in disputes arising from purchases and sales of businesses, including purchase price (post-closing adjustment) disputes, and suits alleging breaches of representations and warranties. He also has represented companies in contract and other disputes involving complex causation and damages issues. As part of his litigation practice, Brian has worked extensively with experts in the areas of auditing, accounting, causation and damages.

Prior to joining Mayer Brown in 1996, he was Law Clerk to The Honorable Frank H. Easterbrook, US Court of Appeals for the Seventh Circuit.

Notable Engagements

- Representing PricewaterhouseCoopers International in matters relating to Satyam Computer Services Ltd.
- Representing Ernst & Young LLP in a series of matters concerning Bally Total Fitness, including securities class actions and shareholder derivative suits.
- Representing accounting firms and their audit partners of in a number of SEC and PCAOB investigations.
- Assisting a major accounting firm in the analysis of risk issues, and the development and implementation of records retention policies and procedures for its business lines, risk functions and administrative functions.
- Consult with major accounting firms on risk management and regulatory compliance matters.
- Successfully represented Ernst & Young LLP in a series of matters arising out of the bankruptcy of Asche Transportation Services, including obtaining dismissal of a securities class action and judgment for the firm after a lengthy arbitration hearing.
- Successfully represented clients in purchase price arbitrations and matters involving assertions of breaches of representations and warranties in M&A transactions. These include the

representation of a Fortune 100 company in a dispute relating to its $800 million acquisition of a manufacturing company; the representation of a privately held company in a post-closing adjustment arbitration relating to the sale of a major appliance manufacturer; the representation of the sellers of a construction company in a post-closing adjustment arbitration and related allegations of breaches of representations and warranties; representation of the seller of an airline catering business in a post-closing adjustment arbitration; and the representation of the seller of a members only manufacturer direct buying company in a post-closing adjustment arbitration.

- Representing a domestic manufacturer in an international arbitration relating to a contract dispute with a supplier involving complex damages issues.

Education

University of Chicago Law School, JD, 1995; University of Chicago Law Review • Certified Public Accountant (CPA), Illinois, 1985; (license inactive) • Indiana University, BS in Accounting, 1984

Admissions

- New York, 2011
- US Court of Appeals for the Third Circuit, 2001
- US Court of Appeals for the Seventh Circuit, 1996
- US District Court for the Northern District of Illinois, 1995
- Illinois, 1995

Publications

- *Securities Investigations: Internal, Civil and Criminal*, PLI Corporate and Securities Law Library (2d ed. 2010)
- "Fraud and Forbearance: State Courts Divided on Whether to Recognize Claims by Securities Holders," *Financial Fraud Law Report*, October 2010

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Terri A. Mazur
Partner
tmazur@mayerbrown.com
New York
Ph: +1 212 506 2680
Fax: +1 212 849 5680

Experience

Terri Mazur is a trial lawyer with a national practice who focuses on complex commercial disputes, particularly in the areas of antitrust and federal securities regulation. She represents national and multinational corporations in monopoly, attempted monopoly, price fixing, market allocation, and conspiracy cases. Terri also represents major companies, accounting firms and individuals in multi-district, class and individual actions involving securities (including claims under Sections 10(b), 11 and 20(a)), professional liability, breach of contract, breach of fiduciary duty, fraud and deepening insolvency claims. Terri defends lenders in class actions, particularly in the area of consumer issues, in federal and state courts across the country. Over the years, Terri has represented corporations in suits involving copyright infringement, breach of contract, business torts, trade secrets, covenants not to compete, RICO claims, and insurance coverage. In the products liability field, she has successfully represented a chemical and lubricant manufacturer and a manufacturer of fire safety-related equipment.

Terri has successfully tried numerous cases, both bench and jury trials, as well as evidentiary hearings (TROs, preliminary injunctions, class certification), in federal and state courts throughout the country. She has written numerous appellate briefs and argued before the Courts of Appeals for the Third, Seventh, Ninth, and Tenth Circuits, as well as in the Illinois and New Mexico appellate courts.

Terri was recently appointed to the NYSBA Antitrust Section's Executive Committee and to the NYSBA's Committee on Women in the Law, where she co-chairs the Annual Meeting subcommittee. She chairs the firm's Women's Initiatives Committee, which focuses on the retention, professional development, and advancement of women at Mayer Brown, and serves on Mayer Brown's Committees for Diversity and Inclusion and Professional Advancement. Terri frequently speaks on issues affecting women lawyers, as well as on securities, antitrust, class action and discovery issues. She joined Mayer Brown in 1987.

Notable Engagements

- Won summary judgment for YouTube and its parent Google in a billion-dollar copyright infringement action brought by Viacom in Federal District Court in New York. The Washington Post called the win "an immense legal victory" for Google, and the New York Times observed that "the ruling in the closely watched case could have major implications for the scores of Internet sites" that rely on user-generated content. (Viacom v. Google, etal., S.D.N.Y. 2010).
- Represented Ernst & Young in In re Cendant Corporation Securities Litigation, a multi-billion-dollar action centered in the District of New Jersey that involved multiple class and derivative actions, separate state actions, SEC and DOJ proceedings, criminal trials, securities and

rofessional liability claims, ultimately settling on favorable terms. (In re Cendant Corporation Securities Litigation, D.N.J.).
- Successfully represented Cancer Treatment Centers of America and its founder, Richard Stephenson, in federal securities and consumer fraud claims arising out of the purchase of a variable life insurance policy. (Stephenson, et al v. Hartford Life & Annuity Insurance Co., et al., N.D. Il).
- Represented Lexecon in its successful $45 million jury verdict and $50 million settlement from the Milberg Weiss law firm in an abuse of process case. (Lexecon v. Milberg Weiss, N.D. Ill. 1998).
- Successful defense of lessor in class action under the federal Consumer Leasing Act challenging the disclosure and reasonableness of early termination charges in an automobile lease, including dismissal of disclosure claims and summary judgment on counterclaim against class representative. (Kedziora v. Citicorp National Services, Inc. (N.D. Ill., 7th Circuit 1996)).
- Represented Grant Thornton in Washburn v. Brown, a lawsuit brought by the liquidators of insurance companies asserting RICO claims, among others, resulting in a settlement on favorable terms. (N.D. Illinois).

Education

Northwestern University School of Law, JD, cum laude, 1984; Executive Editor, Journal of Criminal Law and Criminology • Cornell University, BA, magna cum laude, 1981

Admissions

- US District Court for the Southern District of New York, 2010
- US District Court for the Eastern District of New York, 2010
- New York, 2006
- US Court of Appeals for the Third Circuit, 1997
- US Court of Appeals for the Seventh Circuit, 1992
- US Court of Appeals for the Ninth Circuit, 1988
- US District Court for the Northern District of Illinois (member, Trial Bar) 1988
- Illinois 1987
- US District Court for the District of New Mexico (member, Trial Bar) 1985
- US Court of Appeals for the Tenth Circuit, 1985
- New Mexico 1984

Publications

- Contributing author, *Antitrust Developments Handbook*, American Bar Association, Third Edition, 1993
- "The Use of Illegally Obtained Evidence to Rebut the Insanity Defense," 74 *J. of Crim. L. & Criminology* 391, 1983

Professional Activities

- New York State Bar Association, Sections on Antitrust and Commercial Litigation, member of the Executive Committees of the Antitrust Section and the Committee on Women in the Law

- American Bar Association, Sections on Antitrust and Litigation
- Federal Bar Association
- New York State Bar Association
- New York City Bar Association
- National Association of Women Lawyers
- Board Member, Northwestern University School of Law - Law School Fund Board

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Jonathan C. Medow
Partner
jmedow@mayerbrown.com
Chicago
Ph: +1 312 701 7060
Fax: +1 312 706 8657

"...'as good as any I've seen'..." — *Chambers USA 2007*

Experience

Jonathan Medow is a senior trial lawyer who has practiced with Mayer Brown since 1983. Throughout his career, and particularly during the last ten years, Jonathan's practice has focused heavily on the defense of major accounting firms in significant cases across the country. He has represented Ernst & Young, Deloitte & Touche, KPMG, Arthur Andersen and Grant Thornton.

Over the entirety of his career, Jonathan has handled a variety of matters in a number of fields. He has extensive trial experience, including in disputes between natural gas producers and pipelines, challenges to dead-hand poison pills, and a host of bankruptcy matters (contested plan proceedings, valuation disputes, etc.). He has successfully argued appeals in various courts, including in the United States Court of Appeals for the Second Circuit. Jonathan has also represented clients on a pro bono basis. He has, among other things, used DNA evidence to secure the acquittal of a defendant wrongfully charged with aggravated sexual assault.

Among the comments clients have made about Jonathan are: he is "as good as any I've seen" (*Chambers USA* 2007); he "does a fantastic job – he is capable, smart and works hard" (*Chambers USA* 2006); and he is an "expert" in the field of securities litigation (*Chambers USA* 2008).

Prior to joining Mayer Brown, Jonathan served as a Law Clerk to The Honorable Susan Getzendanner, US District Court for the Northern District of Illinois (1981-1983).

Notable Engagements

- *SEC Investigation of Waste Management*. Negotiating on behalf of Arthur Andersen a resolution of one of the largest investigations of a major accounting firm in Commission history.
- *IKON Securities Litigation*. Obtaining summary judgment in Ernst & Young's favor in a major market fraud case.
- *Asche Arbitration*. Defeating all claims asserted against Ernst & Young during a 30+ day arbitration initiated by a bankruptcy trustee.
- *Grand Court Lifestyles Litigation*. Obtaining partial summary judgment in Deloitte & Touche's favor on claims filed by a committee of unsecured creditors, and thereafter negotiating a favorable settlement.
- *Alabama Hospital Association v. Ernst &Young*. Negotiating a favorable resolution on behalf of Ernst & Young of claims arising out of a series of health care mergers.

- *Charter Communications Security Litigation*. Negotiating a favorable resolution on behalf of Arthur Andersen in a major market fraud case.
- *Confidential SEC Investigations*. Successfully representing auditors and audit firms in various SEC investigations closed without the institution of charges.
- *People v. Larry Lee*. Obtaining an acquittal of a defendant wrongfully charged with aggravated sexual assault.
- *Magma Power v. Dow Chemical*. Obtaining judgment in Dow's favor on claims asserted under Section 16(b) of the Securities Exchange Act and thereafter defending the judgment on appeal.
- *In re Sheffield Properties*. Successfully establishing the valuation of the One Magnificent Mile office and retail tower in Chicago.
- *Natural Gas Pipeline v. The Anschutz Corporation*. Successfully arbitrating a claim for the return of substantial proceeds.

Education

Harvard Law School, JD, magna cum laude, 1981; Board of Editors, Law Review • Stanford University, BA, with distinction, 1978; Phi Beta Kappa

Admissions

- US Court of Appeals for the Third Circuit, 2001
- US Court of Appeals for the Second Circuit, 1997
- Various federal district courts, 1995-1996
- US Court of Appeals for the Seventh Circuit, 1988
- US District Court for the Northern District of Illinois, 1981
- Illinois, 1981

Publications

- "The First Amendment and the Secrecy State: *Snepp v. United States*," 130 *U. Pa. L. Rev.* 775, 1982
- "The Supreme Court, 1979 Term," 94 *Harv.L.Rev.* 75, 223-31, 1980

MAYER·BROWN

Stanley J. Parzen
Partner
sparzen@mayerbrown.com
Chicago
Ph: +1 312 701 7326
Fax: +1 312 706 8668

Experience

Stanley Parzen focuses on complex litigation in federal and state courts and in arbitration, including trials and appeals. He devotes the majority of his practice to the defense of accounting firms and other professionals.

Stanley has represented accounting firms in connection with a wide variety of claims brought by clients and client successors, including trustees and liquidators, including claims relating to allegedly faulty audit work, often relating to failed banks, savings associations, or insurance companies; allegedly faulty computer systems design; and allegedly improper tax advice and tax return preparation. A variety of issues has arisen in these cases, including the auditor's obligation with respect to alleged internal controls at an audit client, whether the knowledge and actions of the client's officers and directors and shareholders should be attributed to the client, whether the deepening insolvency theory is an appropriate theory or measure of damages, accounting for subprime loans and securitizations, and whether the actions of the accountant had any causal relationship to the damages sought in the case.

In addition, he has provided representation to accounting firms in numerous federal securities and derivative actions brought by stockholders in diverse federal and state courts as well as other claims brought by third parties. A variety of issues has arisen in these cases including the propriety of the use of the fraud on the market theory, whether the plaintiffs had ever pleaded a claim for fraud under the applicable pleading standards, and whether the demand requirement for a derivative case to be filed had been satisfied. He has also represented a number of accounting firms in disputes with partners and retired partners, primarily relating to covenants not to compete and retirement benefits. Stanley has also represented international associations of member firms in dispute with former member firms.

Stanley has also represented accounting firms and a coordinating entity in matters before various federal and state regulatory bodies. Among other such work, he has represented clients in investigations conducted by the SEC, the PCAOB, the FDIC and the Comptroller of the Currency. He has also represented a number of firms before various state boards of accountancy.

Prior to joining Mayer Brown, he served as a Law Clerk to The Honorable Harrison L. Winter, US Court of Appeals for the Fourth Circuit, Maryland (1976-1977).

Notable Engagements

- Successfully argued that an accounting firm could not be liable for negligence to a prospective employee of an audit client who relied upon audit report in accepting employment. *Ellis* v. *Grant Thornton LLP*, 530 F.3d 280 (4th Cir. 2008).

- Successfully argued that the Comptroller of the Currency could not bring an enforcement action against an accounting firm where the only participation by the firm in the bank's operations was issuance of an audit report. *Grant Thornton LLP* v. *Comptroller of the Currency.* 514 F.3d 1328 (D.C. Cir. 2008).
- Successfully argued that the trustee of a bankrupt company could not sue the auditor of the company for failure to include a going concern in the audit report. *Fehribach* v. *Ernst & Young LLP*, 493 F.3d 905 (7th Cir. 2007).
- Successfully briefed and argued motions to dismiss in litigation brought by purchasers of a series of affiliated mutual funds against Ernst & Young LLP; among other things, the district court held that purchasers of a close-ended mutual fund could not proceed on a fraud on the market theory because there was no market on which the mutual fund shares traded (*In re Van Wagoner Funds, Inc. Securities Litigation*, 382 F. Supp. 2d 1173 (ND Cal. 2004), Order of July 25, 2005).
- Successfully argued to the Illinois Supreme Court that taxpayers of Cook County, Illinois could not bring an action on behalf of the county under the common law against an accounting firm that had allegedly failed to determine that a municipal refinancing had involved yield burning (*County of Cook ex rel Rifkin v. Bear Stearns & Co.*, 215 Ill. 2d 466, 831 N.E. 2d 563 (2005); see also *Schachitti v. UBS Financial Services, et al.*, 215 Ill. 2d 484, 831 N.E. 2d 544 (2005)).
- Successfully sought interlocutory review and obtained reversal of an order of the district court certifying a class of securities purchasers against Grant Thornton LLP; the United States Court of Appeals for the Fourth Circuit held that a defendant could challenge the efficiency of the market at the class certification stage when the plaintiffs sought to base the propriety of the class device upon the fraud on the market theory and that the plaintiffs had not shown sufficient indicia of an efficient market to permit class certification (*Gariety et al. v. Grant Thornton LLP*, 368 F.3d 356 (4th Cir. 2004)).
- Successfully argued to the United States Court of Appeals for the Sixth Circuit that the fact that the alleged errors in the financial statements were large in magnitude and the fact that the accounting firm had been sued in other cases were both not germane in determining whether the complaint sufficiently alleged scienter against the accounting firm (*Fidel v. Ernst & Young LLP*, 392 F.3d 220 (6th Cir. 2004)).
- Successfully opposed a preliminary injunction motion filed by a retired partner of Arthur Andersen LLP seeking to enjoin arbitration under the arbitration clause in the Arthur Andersen LLP partnership agreement (*Viets v. Arthur Andersen LLP,* 2003 WL 21525062, 31 Employee Benefits Cas. 1388 (SD Ind. 2003)).
- Successfully defended Arthur Andersen LLP in connection with a request from retired partners for an injunction to enjoin the sale of certain of its practices after its indictment by the United States Government; the United States District Court for the Northern District of Illinois denied the request for injunctive relief.
- Argued a number of other cases establishing important principles for accounting firms; for example, (1) the United States Court of Appeals for the Eighth Circuit upheld the right of an accounting firm to sue its audit client under RICO for defrauding the accounting firm in the course of its audit work (*Alexander Grant & Company v. Tiffany Industries*, 742 F.2d 408 (8th Cir. 1984)), (2) the Illinois appellate court held that a claim by an audit client was time barred because the books and records of the audit client reflected what was allegedly not told to the board of directors of the client (*Illinois College of Optometry v. Grant Thornton*, LLP, No. 1-98-0037, 746 N.E.2d 908 (1st Dist. Mar. 1, 1999)), and (3) the Illinois appellate court held that an accounting firm had been released from claims because the plaintiff had previously released

other persons who had alleged breached a fiduciary duty to the plaintiff (*Cherney v. Soldinger*, 299 Ill. App. 3d 1066, 702 N.E.2d 231 (Ill. App. 1998)).

- Tried a number of matters for accounting firms both in court and in arbitration; for example, (1) obtained a judgment for an accounting firm, after a two-week bench trial, in which the plaintiffs sued the accounting firm alleging negligence in the audit reports of an acquired firm (*Pioneer Computer Group, Ltd. v. Grant Thornton*, SD Cal.), (2) succeeded in having the Kansas appellate court overturn the trial court judgment (finding the accountants liable for failing to tell the trustee of a trust not to make certain investments) and enter judgment for the accountants holding they had no duty to speak (*Gillespie v. Seymour*, 876 P.2d 204 (Kan. App. 1994)).
- Drafted and argued numerous other motions and appeals resulting in favorable decisions for accountants; for example, see *Donnybrook Investments, Ltd. v. Arthur Andersen LLP*, 2006 WL 1049588 (N.D.Ill. 2006); *Courtney v. Halleran*, 2005 WL 241471 (N.D.Ill. 2005) aff'd, 485 F.3d 942 (7th Cir. 2007). ; *Baker O'Neal Holdings v. Ernst & Young LLP*, 2004 WL 771230 (S.D. Ind. 2004); *New England Health Care Employees Pension Fund v. Ernst & Young LLP*, 336 F.3d 495 (6th Cir. 2003); and many others.
- Participated in the briefing leading to other significant decisions in favor of accounting firms; see *FDIC v. Ernst & Young LLP*, 374 F.3d 579 (7th Cir. 2004); *RTC v. Grant Thornton LLP*, 41 F.3d 1539 (D.C. Cir.1994); *Hendricks v. Grant Thornton*, 973 S.W.2d 348 (Tex. Civ. App—Beaumont); and *Hartman v. Blinder*, 687 F. Supp. 938 (D. NJ 1987).
- *MDIF v. Grant Thornton*, Maryland State Court, lawsuit brought by receiver of state-insured savings and loan.
- *FDIC v. Shah, et al.*, ND Cal., third-party claims brought by officers and directors of savings and loan; motion to dismiss granted.
- *FSLIC v. Wagner*, E.D. Cal., third-party claim brought by officers and directors of savings and loan; voluntarily dismissed in response to motion to dismiss.
- *Comeau v. Rupp*, 762 F. Supp. 1434, D. Kan., 1991, lawsuit by FDIC asserting claim on behalf of savings and loan.
- *Phelan v. First California Savings*, CD Cal., lawsuit brought by stockholder of savings and loan; motion for summary judgment granted.
- *Washburn v. Brown*, ND Ill., lawsuit brought by liquidator of insurance company.
- *Carrier Ins. Co. v. Alexander Grant & Company*, SD Iowa, lawsuit brought by insurance company and its majority stockholder.
- *Harden v. Firstmark*, SD Ind., lawsuit brought by stockholders of financial services and insurance company against Price Waterhouse alleging failure to issue a going concern qualification; court rejected fraud created the market theory.
- *RTC v. Arthur Andersen*, ND Ill., alleged malpractice claim brought by RTC on behalf of failed financial institution.
- *RTC v. Grant Thornton*, SD NY and D. NM, alleged malpractice claims brought by RTC on behalf of failed financial institutions.
- *Commissioner of Insurance, State of Michigan v. Ernst & Young, LLP*, defense of claim brought on behalf of US estate of Canadian insurance company.
- *Gateway 2000 v. Ernst & Young LLP*, claim relating to computer order system.

Education

Harvard Law School, JD, cum laude, 1976; Harvard Law Review • Earlham College, BA, 1973

Admissions

- US District Court for the District of Colorado, 2011
- US Court of Appeals for the Fourth Circuit, 2003
- US District Court for the Eastern District of Wisconsin, 2002
- US Court of Appeals for the Sixth Circuit, 2002
- US District Court for the Eastern District of Michigan, 1997
- US District Court for the Western District of Michigan, 1995
- US Court of Appeals for the Tenth Circuit, 1994
- US Court of Appeals for the District of Columbia, 1994
- US Court of Appeals for the Fifth Circuit, 1992
- US Court of Appeals for the Second Circuit, 1990
- US District Court for the Northern District of California, 1988
- US Court of Appeals for the Ninth Circuit, 1986
- US Court of Appeals for the Eighth Circuit, 1984
- US Court of Appeals for the Seventh Circuit, 1981
- US District Court for the Northern District of Illinois, 1978
- Illinois, 1978

Publications

- "Fraud and Forbearance: State Courts Divided on Whether to Recognize Claims by Securities Holders," *Financial Fraud Law Report*, October 2010

Seminars & Presentations

- "Securities and Financial Roundtable," Litigating Class Actions, Law Seminars International, October 24-25, 2011

MAYER·BROWN

Richard M. Rosenfeld
Partner
rrosenfeld@mayerbrown.com
Washington DC
Ph: +1 202 263 3130
Fax: +1 202 263 3300

Experience

Richard M. Rosenfeld is co-lead of Mayer Brown's US Securities Litigation & Enforcement group working from both the Washington, DC and New York offices.

Richard has nearly 17 years of experience practicing in the securities field, including more than a decade in government regulatory and enforcement positions. Most recently, he was asked to return to the government from private practice in the midst of the financial crisis to serve as Chief Investigative Counsel in the Office of the Special Inspector General for the Troubled Asset Relief Program (SIGTARP).

In his role at SIGTARP, Richard helped build and lead a team of top white collar, securities and bank fraud specialists tasked with conducting criminal and civil investigations into some of the most complex bank, securities and mortgage frauds in US history. He managed more than 80 lawyers, federal agents, accountants and analysts pursuing more than 150 investigations. Additionally, he led SIGTARP's involvement in several of the TARP-related bailout programs, including the investment management agreements for the more than $100 billion Public/Private Investment program.

In private practice, Richard represents financial institutions, funds, companies and individuals in a variety of business, regulatory and compliance issues. He advises on transactions, policies and procedures, investigations, regulatory enforcement and litigation before the SEC, other financial services regulators and the US Department of Justice. These matters typically involve allegations of fraud, whether it be financial reporting violations, insider trading, market manipulation, or other regulatory or compliance issues. Richard has substantial securities litigation experience in the federal courts, in addition to leading internal investigations and advising clients on regulatory compliance, corporate governance and other SEC-related issues.

Earlier in his career, he served in the Division of Enforcement at the SEC. During his time with the Commission, he handled some of the most complex securities frauds in SEC history and was detailed as a special prosecutor to multiple US Attorney's offices across the country to assist in matters involving cross border money laundering, tax evasion and securities, bank, mail and wire fraud. He ended his career with the Commission as the first and only internationally based SEC representative in London where he organized, managed and directed one of the largest multinational financial fraud litigations in SEC history and worked with the highest ranking regulators of several countries to address cooperation in international securities matters.

Richard was a partner at two prominent firms in London and Washington, DC prior to his return to the government to assist with the bailout.

Education

Cornell Law School, JD • Rutgers University, BA, with highest honors

Admissions

- District of Columbia 1997
- Connecticut 1995
- Maryland 1995