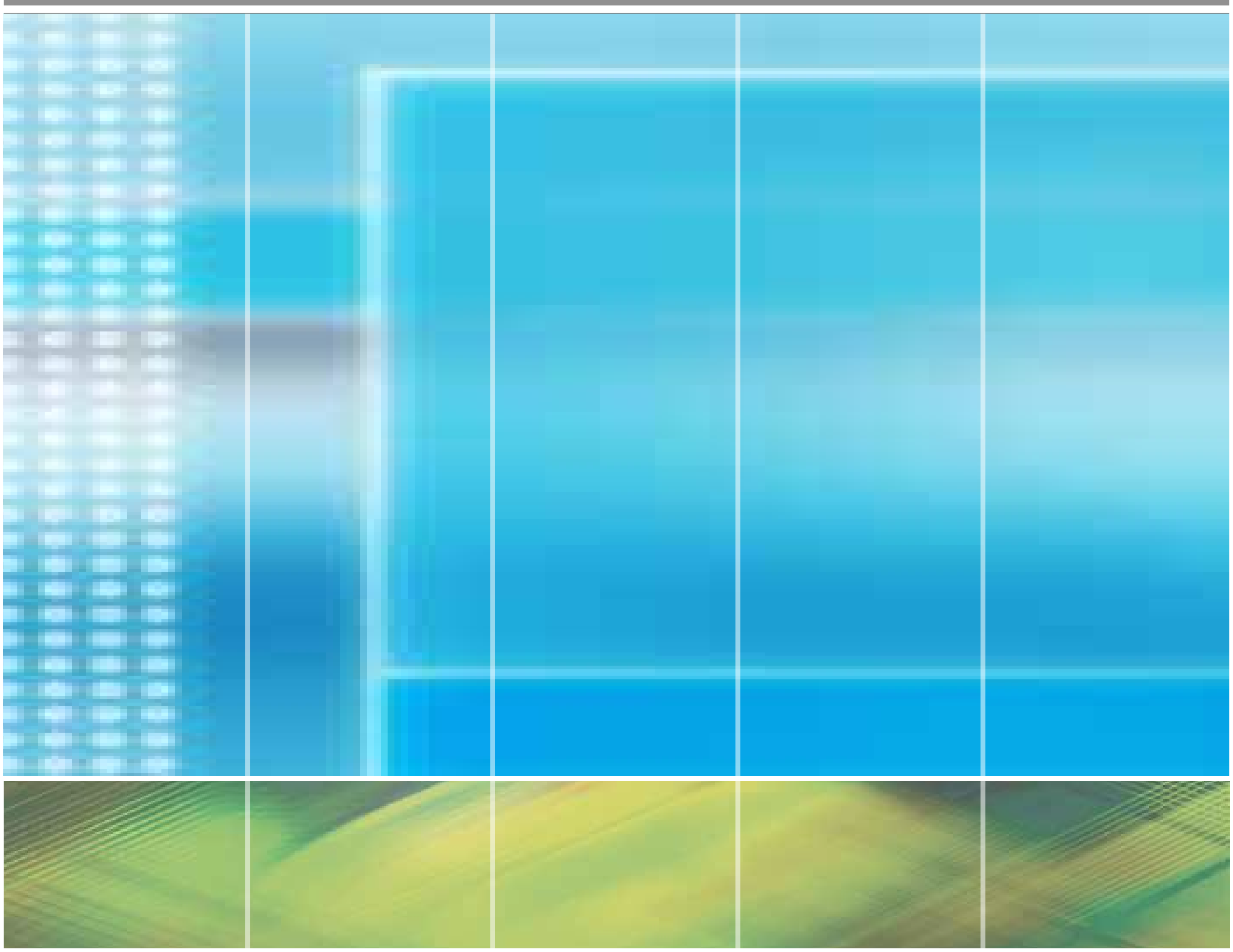
CORNERSTONE RESEARCH

Securities Class Action Filings

2011 Mid-Year Assessment



Research Sample

- The Stanford Law School Securities Class Action Clearinghouse in cooperation with Cornerstone Research has identified 3,321 federal securities class action filings between January 1, 1996, and June 30, 2011.

- These filings include 313 IPO Allocation filings, 68 Analyst filings, 25 Mutual Fund filings, 40 Options Backdating filings, 23 Ponzi filings, and 209 Credit-Crisis filings; the last category includes 21 Auction Rate Securities filings.

- The sample used in this report excludes IPO Allocation, Analyst, and Mutual Fund filings.

- Multiple filings related to the same allegations against the same defendant(s) are consolidated in the database through a unique record indexed to the first identified complaint.

TABLE OF CONTENTS

TABLE OF FIGURES

OVERVIEW

Federal securities fraud class action filing activity decreased moderately in the first six months of 2011, reversing the increase in filings in the second half of 2010. A total of 94 federal securities fraud class actions (filings or class actions) were filed in the first half of the year, a 9.6 percent decrease in activity from 104 filings in the second half of 2010 (Figure 1). This decline includes a drop in credit-crisis filings; there were just two such filings in the first half of 2011. Interestingly, filings tend to occur faster than before. The median lag time between the end of the class periods and the filing dates decreased to eight days, the lowest level observed since 1997 and well below the 112-day median for the second half of 2009.

Nontraditional filings appear to compensate for the relative scarcity of typical securities class actions. Twenty-four filings related to Chinese reverse mergers accounted for 25.5 percent of all filings in the first half of 2011. There was a total of 25 filings against Chinese companies, up from 12 such filings, nine of which were related to reverse mergers, in all of 2010. There were 21 merger and acquisition (M&A) filings in the first half of 2011. Taken together, Chinese reverse merger and M&A filings represented 47.9 percent of all filings during the last six months, up from 32.7 percent in the last six months of 2010. If Chinese reverse merger and M&A filings were excluded, the number of traditional filings remaining would be 57 in the first half of 2010, 70 in the second half of 2010, and 49 in the first half of 2011 (Figure 2). These numbers are similar to the low number of filings seen in 2006 and early 2007.

In the first six months of 2011, only 8.5 percent of filings named companies in the Standard & Poor's (S&P) 500 Index, down from 15.4 percent in the second half of 2010. Litigation activity in the S&P 500 Financials and Health Care sectors also decreased substantially. Only one of 81 companies in the S&P 500 Financials sector was named as a defendant in a class action in the first half of 2011. An average of 11.7 percent of Financials sector firms were named in class actions for the 11 years ending December 2010. There were no filings against companies in the S&P 500 Health Care sector in the first half of 2011, reversing the uptick in Health Care sector filings observed in 2010.

The losses in market capitalization associated with the announcements ending the class periods have remained low. Although the total Disclosure Dollar Loss (DDL) of $48 billion in the first half of 2011 represented a 152.6 percent increase from the second half of 2010, the market capitalization losses remained well below the historical average of $64 billion occurring between 1997 and 2010. There were two mega DDL filings—filings with more than $5 billion in end-of-class market capitalization losses—which together represented 47.6 percent of the DDL Index™ in the first half of 2011. The market capitalization declines over the entire class periods also remained low in 2011. The total Maximum Dollar Loss (MDL) in the first half of 2011 was $256 billion, a 98.4 percent increase from the second half of 2010 but still well below the historical average of $340 billion. Five MDL filings, each with more than $10 billion in market capitalization losses, represented 84.4 percent of the MDL Index™ in the last six months.[1]

Figure 1

CLASS ACTION FILINGS SUMMARY
SIX-MONTH PERIODS

	Average (1997 H1–2010 H2)	2009 H2	2010 H1	2010 H2	2011 H1
Class Action Filings	97	84	72	104	94
Disclosure Dollar Loss ($ Billions)	$64	$35	$53	$19	$48
Maximum Dollar Loss ($ Billions)	$340	$199	$345	$129	$256

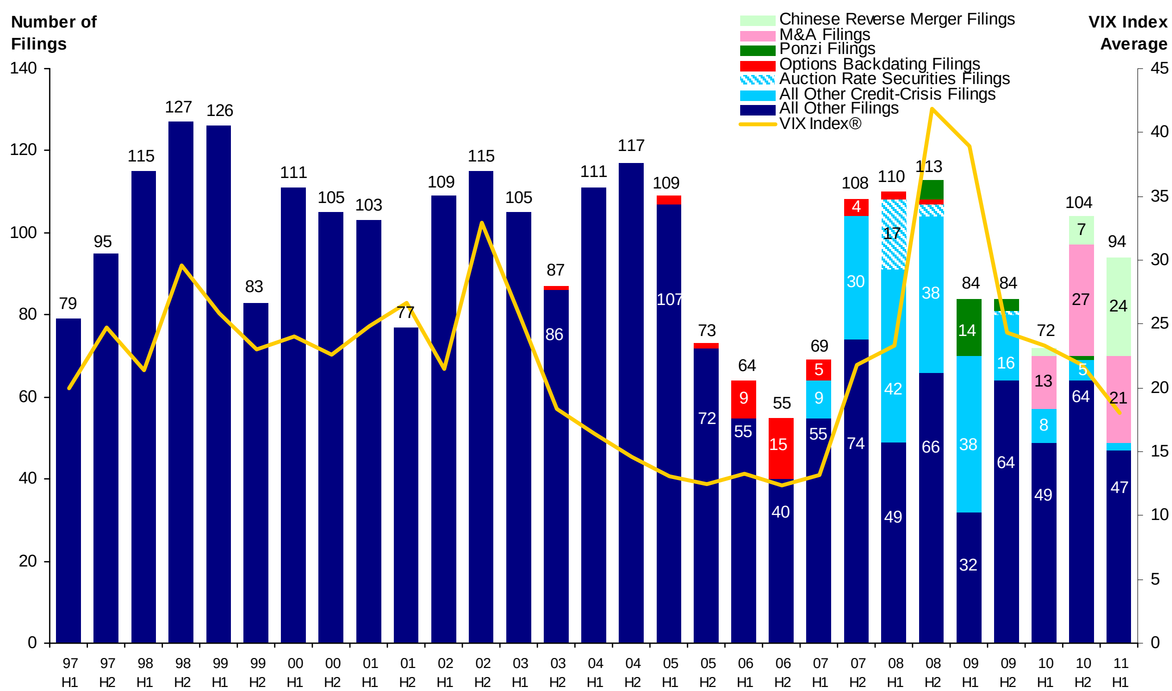
1 Disclosure Dollar Loss and Maximum Dollar Loss are defined in the "Market Capitalization Losses" section of this report.

NUMBER OF FILINGS

The Class Action Filing Index™ (CAF Index) reports 94 filings in the first half of 2011 (Figure 2). Filings related to the credit crisis have continued to decrease, with only two such filings between January 1 and June 30, 2011. Filings related to Chinese issuers increased dramatically in the last six months, with 25 such filings, including 24 filings associated with reverse merger companies. There were 21 M&A filings in the first half of 2011, continuing a new pattern evident in 2010 when there were 27 M&A filings in the second half of that year. If Chinese reverse merger and M&A filings were excluded, the CAF Index would report 57 filings in the first half of 2010, 70 in the second half of 2010, and 49 in the first half of 2011, numbers consistent with the low filing levels seen in 2006 and early 2007. In the last three six-month periods, there has been an average of 59 traditional filings per period, slightly less than the average of 63 filings per period in 2006 and the first half of 2007, when filings were lower than at any time in the last 14 years.

Figure 2

CAF INDEX™
SEMIANNUAL NUMBER OF CLASS ACTION FILINGS
1997–2011 H1

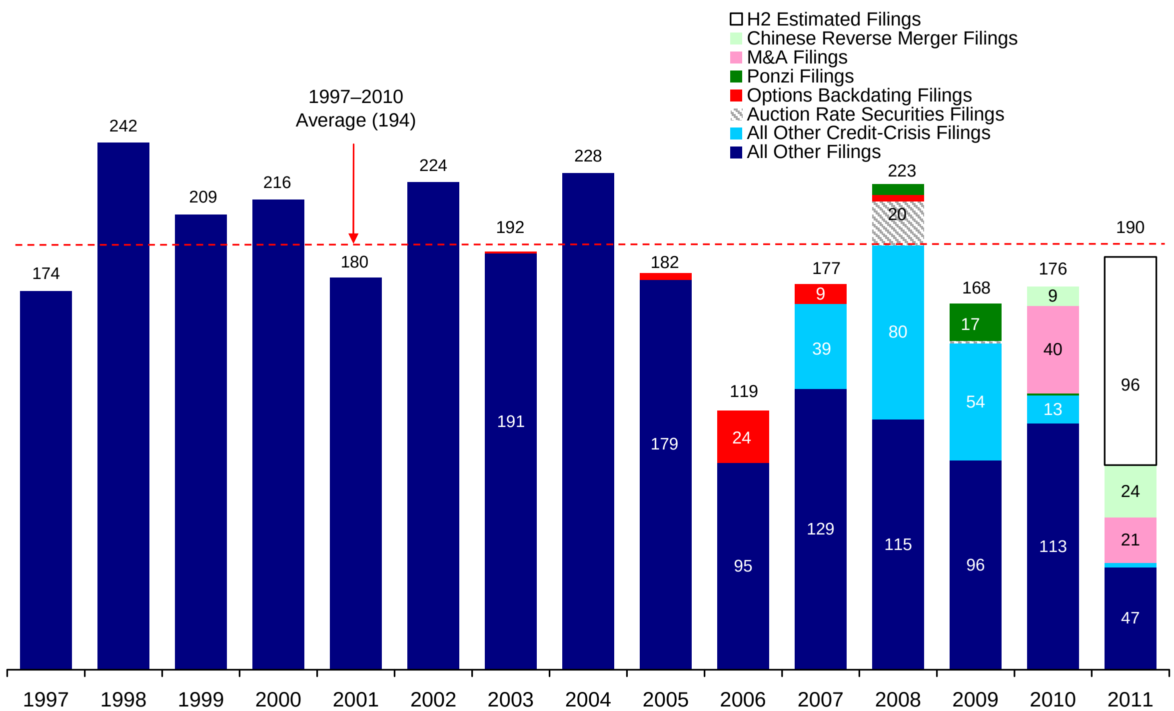


NUMBER OF FILINGS *continued*

If the filing frequency observed in the first half of 2011 continues through the remainder of the year, there will be a total of 190 filings in 2011, on par with the average annual number of filings from 1997 to 2010.[2] This would represent an 8 percent increase from 2010 and would be only 2.1 percent below the average annual number of filings for the 14 years ending December 2010 (Figure 3).

Figure 3

CAF INDEX™
ANNUAL NUMBER OF CLASS ACTION FILINGS
1997–2011 H1



This projection for the total number of 2011 filings assumes that filings against Chinese reverse merger companies (CRMs) will continue at the same level during the second half of 2011. However, the number of CRMs is limited; the Public Company Accounting Oversight Board (PCAOB) found that 159 CRMs were formed between January 1, 2007, and March 31, 2010, while Bloomberg included approximately 80 such companies in the Bloomberg Chinese Reverse Mergers Index (see "New Developments" section). At the extreme, if one assumes that there will be no CRM filings in the second half of 2011, and other types of filings continue at the same pace, there will be a total of 165 filings for the year, making 2011 the second lowest year in filings activity after 2006.

2 Annualized figures are based on 181 calendar days from January 1 to June 30, 2011, and 365 days for the full year of 2011.

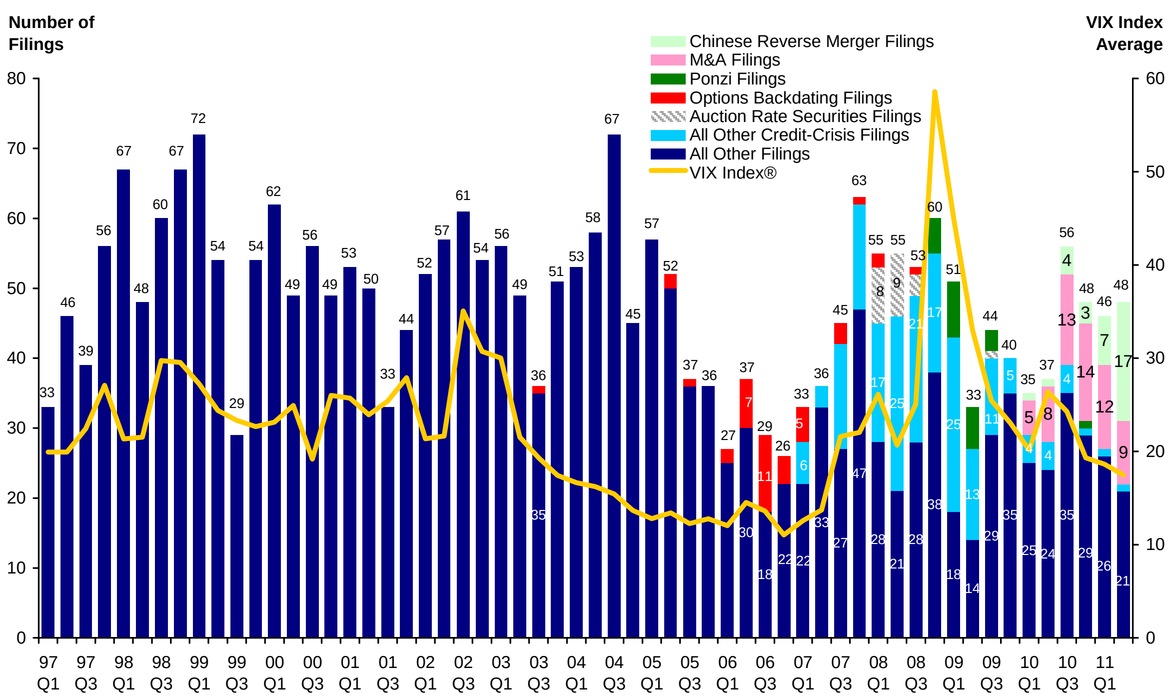
NUMBER OF FILINGS *continued*

The CAF Index also reveals a decline in the quarterly number of filings during the past 12 months. Quarterly filings decreased from 56 in the third quarter of 2010 to 48 in the fourth quarter, 46 in the first quarter of 2011, and 48 in the second quarter of 2011. The decline is more striking if Chinese reverse merger and M&A filings are excluded; the number of traditional filings declined from 39 in the third quarter of 2010 to 22 in the second quarter of 2011.

Class action activity continues to be positively correlated with market volatility. The fourth quarter of 2008, a historical peak in stock market volatility as measured by the Chicago Board Options Exchange (CBOE) Volatility Index® (VIX), saw a flurry of class actions. During the fourth quarter of 2006, the VIX was at its lowest point since its inception in the 1990s and there was a historically low number of filings (Figure 4). As of the second quarter of 2011, stock market volatility reached its lowest level since the second quarter of 2007, the period immediately preceding the start of the credit crisis. The decline in the number of traditional filings—excluding Chinese reverse merger and M&A cases—in the last four quarters coincides with the downward trend in market volatility during the same period.

Figure 4

CAF INDEX™
QUARTERLY NUMBER OF CLASS ACTION FILINGS AND CBOE VIX®
1997–2011 H1

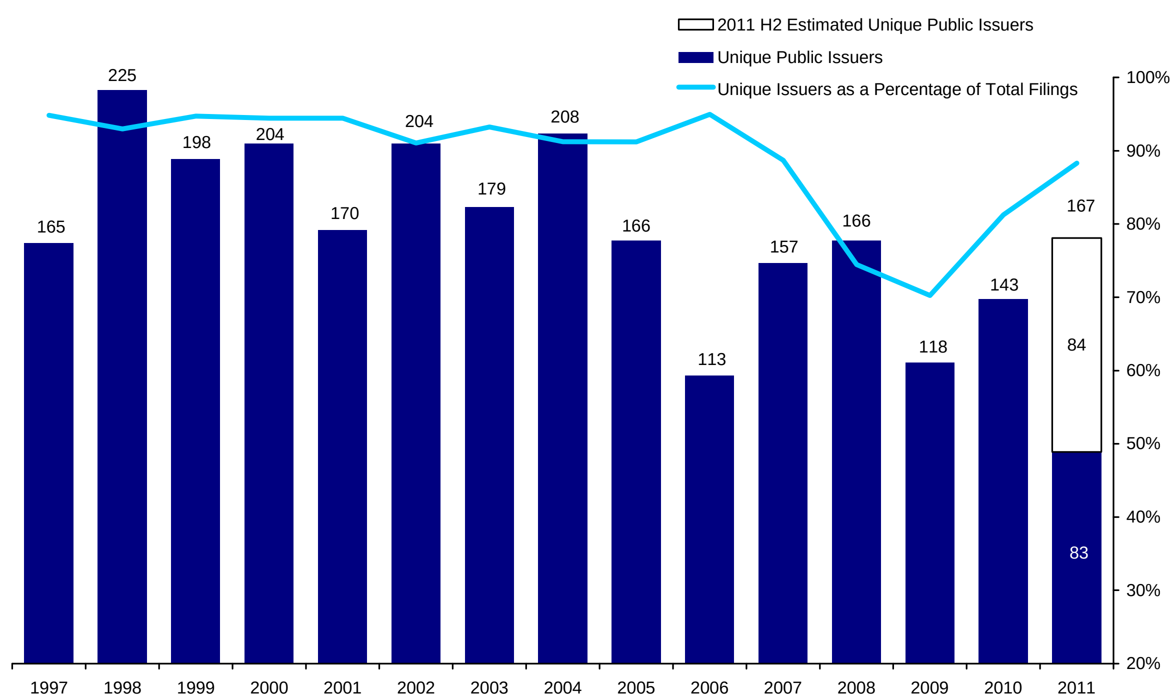


NUMBER OF FILINGS *continued*

The Class Action Filings-Unique Issuers Index (CAF-U Index™) is a metric that tracks the number of unique issuers whose exchange-traded securities were involved in class actions. In the first half of 2011, there were 83 unique issuers targeted by filings. If filings against unique issuers continue at the same pace in the second half of 2011, there will be 167 unique issuers targeted by class actions for the year. The number of unique issuers as a percentage of the total number of filings increased to 88.3 percent, continuing the upward trend from 2010 after declining to a historical low of 70.2 percent in 2009. The increase in unique issuers as a percentage of total filings reflects a decline in credit-crisis lawsuits, which were concentrated in a set of financial companies (Figure 5).

Figure 5

CAF-U INDEX™
NUMBER OF UNIQUE ISSUERS WITH EXCHANGE-TRADED SECURITIES
1997–2011 H1



The projection in Figure 5 assumes that there will be the same number of filings against unique CRMs in the second half of 2011. At the extreme, if one assumes that there will be no Chinese reverse merger filings in the second half of 2011, while other types of filings continue at the same pace, then there will be 143 unique public issuers targeted by class actions in 2011.

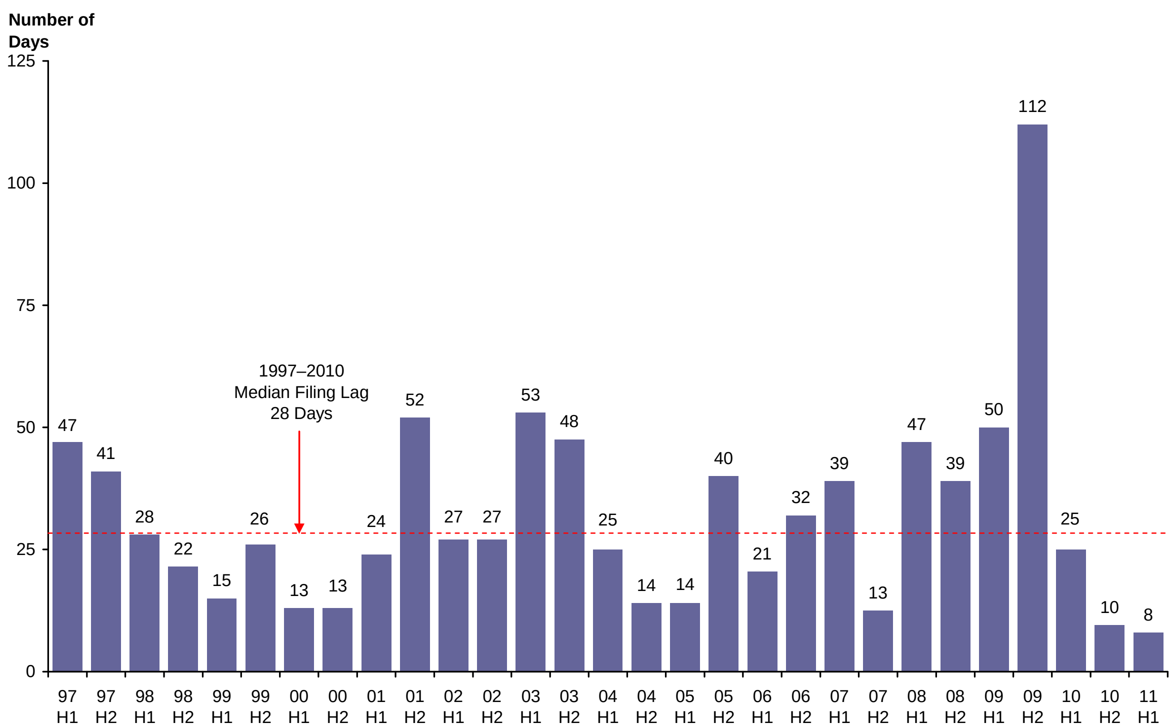
NUMBER OF FILINGS *continued*

In the first half of 2011, the median lag between the end of the class periods and the filing dates dropped to the lowest recorded semiannual level since 1997. The median lag was eight days in the first half of 2011, a 20 percent decrease from the median lag of 10 days during the second half of 2010 and 71.4 percent below the median lag of 28 days for the 14 years ending December 2010 (Figure 6). The decline in the median filing lag in the first half of 2011 was associated with a decrease in the number of filings that had a six-month or longer filing lag. There were 11 such filings in the first half of 2011, compared with 12 such filings in the second half of 2010 and 20 such filings in the first half of 2010. Between 1997 and 2010, there was an average of 19 such filings in each six-month period.

The decline in the median filing lag can be partially attributed to the large number of filings related to M&A activity, private securities, and securities other than common equity, which tend to be filed quickly. If these filings were excluded from the analysis, the median lag would increase to 17 days for the first half of 2011.

Figure 6

SEMIANNUAL MEDIAN LAG BETWEEN CLASS END DATE AND FILING DATE
1997–2011 H1



HEAT MAPS

The Heat Maps of S&P 500 Securities Litigation™ facilitate analysis of the level of class action activity by industry sector. We focus on companies in the S&P 500 Index, which includes 500 large, publicly traded companies in all major sectors. Starting with the composition of the S&P 500 Index at the beginning of each year, we examine two factors for each sector. First, what percentage of these companies was subject to new class actions during the year? Second, of the total market capitalization of the companies in the Index, what share was accounted for by companies named in new class actions?

Only 8.5 percent of filings in the first half of 2011 named companies in the S&P 500 Index, down from 15.4 percent in the second half of 2010. This decrease in the proportion of filings involving S&P 500 companies can be partially explained by an increase in the share of nontraditional filings, such as Chinese reverse merger and M&A cases, which predominantly involved smaller firms that were not part of the S&P 500 Index. Overall, eight companies, or approximately one out of every 63 companies in the S&P 500 Index at the beginning of 2011, were defendants in a class action filed in the first half of 2011, compared with about one out of every 19 S&P 500 companies in the full year of 2010 (Figure 7).[3]

Figure 7

HEAT MAPS OF S&P 500 SECURITIES LITIGATION™
PERCENTAGE OF COMPANIES SUBJECT TO NEW FILINGS*
2000–2011 H1

	Average 00–10	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011 H1
Consumer Discretionary	**5.3%**	3.3%	2.4%	10.2%	4.6%	3.4%	10.3%	4.4%	5.7%	4.5%	3.8%	5.1%	2.5%
Consumer Staples	**3.9%**	7.3%	8.3%	2.9%	2.9%	2.7%	8.6%	2.8%	0.0%	2.6%	4.9%	0.0%	0.0%
Energy	**2.1%**	0.0%	0.0%	8.0%	0.0%	4.2%	0.0%	0.0%	0.0%	0.0%	2.6%	7.7%	0.0%
Financials	**11.7%**	4.2%	1.4%	16.7%	8.6%	19.3%	7.3%	2.4%	10.3%	31.2%	13.1%	10.3%	1.2%
Health Care	**10.1%**	2.6%	7.1%	15.2%	10.4%	10.6%	10.7%	6.9%	12.7%	13.7%	3.7%	15.4%	0.0%
Industrials	**3.4%**	2.8%	0.0%	6.0%	3.0%	8.5%	1.8%	0.0%	5.8%	3.6%	6.9%	0.0%	0.0%
Information Technology	**6.6%**	9.7%	18.2%	10.3%	5.2%	3.6%	7.5%	9.0%	2.6%	2.9%	0.0%	3.9%	3.9%
Materials	**1.3%**	4.1%	0.0%	0.0%	2.9%	0.0%	3.1%	0.0%	0.0%	0.0%	0.0%	3.2%	0.0%
Telecommunication Services	**7.7%**	23.1%	16.7%	15.4%	8.3%	0.0%	0.0%	0.0%	0.0%	0.0%	11.1%	0.0%	11.1%
Utilities	**6.8%**	5.0%	7.9%	40.5%	2.8%	5.7%	3.0%	0.0%	3.1%	3.2%	0.0%	0.0%	2.9%
All S&P 500 Companies	**6.4%**	**5.0%**	**5.6%**	**12.0%**	**5.2%**	**7.2%**	**6.6%**	**3.6%**	**5.4%**	**9.2%**	**4.8%**	**5.4%**	**1.6%**

Legend	0%	0%–5%	5%–15%	15%–25%	25%+

* The chart is based on the composition of the S&P 500 as of the last trading day of the previous year.

Sectors are based on the Global Industry Classification Standard.

Percentage of Companies Subject to New Filings equals the number of companies subject to new securities class action filings in federal courts in each sector divided by the total number of companies in that sector.

3 In Figures 7 and 8, when we refer to the number and market capitalization of companies involved in new securities litigation, we have consolidated all new filings against the same company so that the totals reflect unique companies.

HEAT MAPS *continued*

The percentage of S&P 500 companies in the Financials sector targeted in lawsuits in the first half of 2011 was 1.2 percent, down substantially from 31.2 percent, 13.1 percent, and 10.3 percent in 2008, 2009, and 2010, respectively. The trend for the Financials sector is consistent with the decrease of credit-crisis filings over the same period. No companies from the S&P 500 Health Care sector were named as defendants in class actions during the first half of 2011, which reversed an uptick in filings in this sector observed in 2010 when 15.4 percent of companies, representing 33.7 percent of sector market capitalization, were named in litigation.

A single filing created a spike in the Heat Map for the S&P Telecommunication Services sector for the first six months of 2011 after a period of little class action activity between 2004 and 2010. The issuer represented 11.1 percent of the companies in the Telecommunication Services sector and 28.4 percent of the sector's market capitalization.[4] This filing is related to an M&A transaction and therefore does not represent an increase in traditional filing activity in the sector.

Overall, the level of class actions against S&P 500 companies is historically low both in terms of the number of companies named as defendants and the percentage of market capitalization represented by the defendants (Figure 8).

Figure 8

HEAT MAPS OF S&P 500 SECURITIES LITIGATION™
PERCENTAGE OF MARKET CAPITALIZATION SUBJECT TO NEW FILINGS*
2000–2011 H1

	Average 00–10	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011 H1
Consumer Discretionary	**7.3%**	6.5%	1.3%	24.7%	2.0%	7.9%	5.7%	8.9%	4.4%	7.2%	1.9%	4.9%	1.5%
Consumer Staples	**5.1%**	34.5%	6.3%	0.3%	2.3%	0.1%	11.4%	0.8%	0.0%	2.6%	3.9%	0.0%	0.0%
Energy	**3.2%**	0.0%	0.0%	1.7%	0.0%	44.9%	0.0%	0.0%	0.0%	0.0%	0.9%	3.3%	0.0%
Financials	**24.3%**	3.3%	0.8%	29.2%	19.9%	46.1%	22.2%	8.2%	18.1%	55.0%	38.3%	31.1%	6.9%
Health Care	**18.2%**	11.0%	5.4%	35.2%	16.3%	24.1%	10.1%	18.1%	22.5%	20.0%	1.7%	33.7%	0.0%
Industrials	**8.0%**	3.9%	0.0%	13.3%	4.6%	8.8%	5.6%	0.0%	2.2%	26.4%	23.2%	0.0%	0.0%
Information Technology	**9.3%**	8.5%	37.6%	5.7%	1.0%	1.5%	12.4%	9.9%	4.2%	1.7%	0.0%	6.8%	6.2%
Materials	**2.7%**	8.6%	0.0%	0.0%	1.4%	0.0%	5.1%	0.0%	0.0%	0.0%	0.0%	12.5%	0.0%
Telecommunication Services	**11.7%**	39.5%	13.3%	19.9%	4.0%	0.0%	0.0%	0.0%	0.0%	0.0%	1.7%	0.0%	28.4%
Utilities	**8.7%**	5.6%	17.4%	51.0%	4.3%	4.8%	5.6%	0.0%	5.5%	4.0%	0.0%	0.0%	0.6%
All S&P 500 Companies	**11.7%**	**11.1%**	**10.9%**	**18.8%**	**8.0%**	**17.7%**	**10.7%**	**6.7%**	**8.2%**	**16.2%**	**8.6%**	**11.2%**	**3.3%**

Legend	0%	0%–5%	5%–15%	15%–25%	25%+

* The chart is based on the market capitalizations of the S&P 500 companies as of the last trading day of the previous year. If the market capitalization on the last trading day is not available, the average fourth-quarter market capitalization is used.

Sectors are based on the Global Industry Classification Standard.

Percentage of Market Capitalizations Subject to New Filings equals the total market capitalization of companies subject to new securities class action filings in federal courts in each sector divided by the total market capitalization of all companies in that sector.

4 The Telecommunication Services sector is the smallest of the S&P 500 Index sectors, comprising nine companies and representing 3 percent of the Index's market capitalization as of the beginning of 2011.

MARKET CAPITALIZATION LOSSES

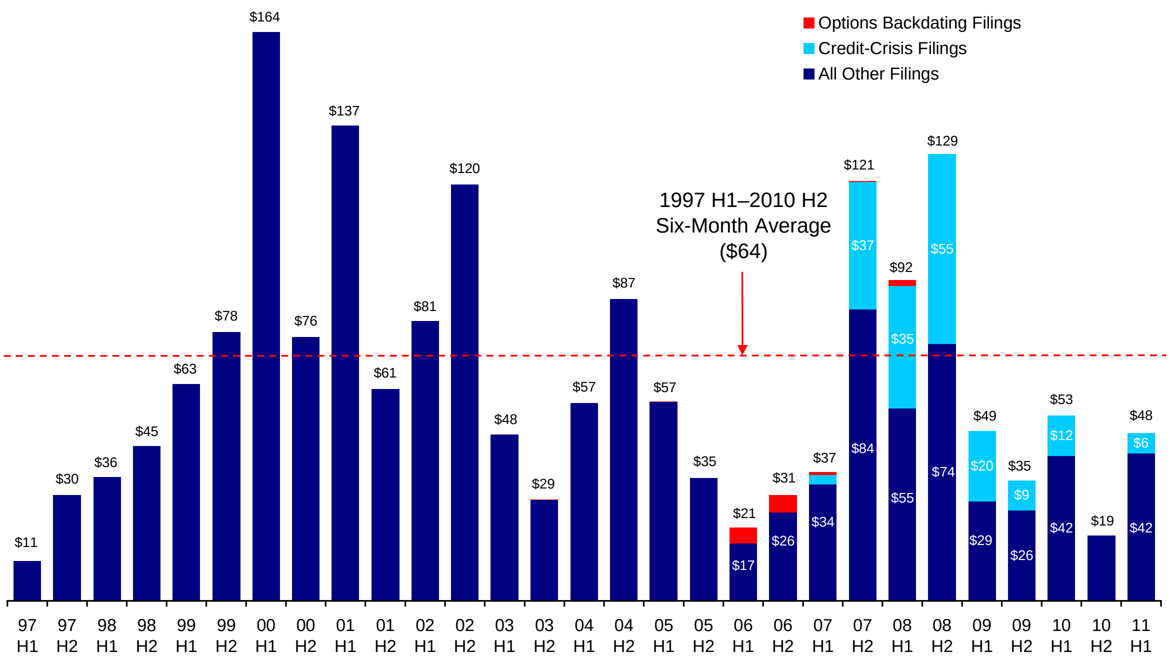
To measure changes in the size of filings, we track market capitalization losses for defendant firms during and at the end of class periods.[5] Declines in market capitalization may be driven by market, industry, and firm-specific factors. To the extent that the observed loss reflects factors unrelated to the allegations in the class action complaint, indices based on class period losses would not represent potential defendant exposure in class actions. This is especially relevant for the post-*Dura* securities litigation environment.[6] This report tracks market capitalization losses at the *end* of each class period using DDL and market capitalization losses *during* each class period using MDL.

DDL is the dollar value change in the defendant firm's market capitalization between the trading day immediately preceding the end of the class period and the trading day immediately following the end of the class period. MDL is the dollar value change in the defendant firm's market capitalization from the trading day with the highest market capitalization during the class period to the trading day immediately following the end of the class period. MDL and DDL should not be considered indicators of liability or measures of potential damages. Instead, they estimate the impact of all of the information revealed during or at the end of the class period, including information unrelated to the litigation.

In the first half of 2011, we observed an increase in both DDL and MDL compared with the previous six-month period (Figures 9 and 10). However, both measures remained well below historical averages.

Figure 9

DISCLOSURE DOLLAR LOSS INDEX™
SIX-MONTH PERIODS
1997–2011 H1
Dollars in Billions



---

5 Market capitalization measures are calculated for publicly traded common equity securities, closed-ended mutual funds, and exchange-traded funds only.

6 In April 2005, the Supreme Court ruled that the plaintiffs in a securities class action are required to plead a causal connection between alleged wrongdoing and subsequent shareholder losses.

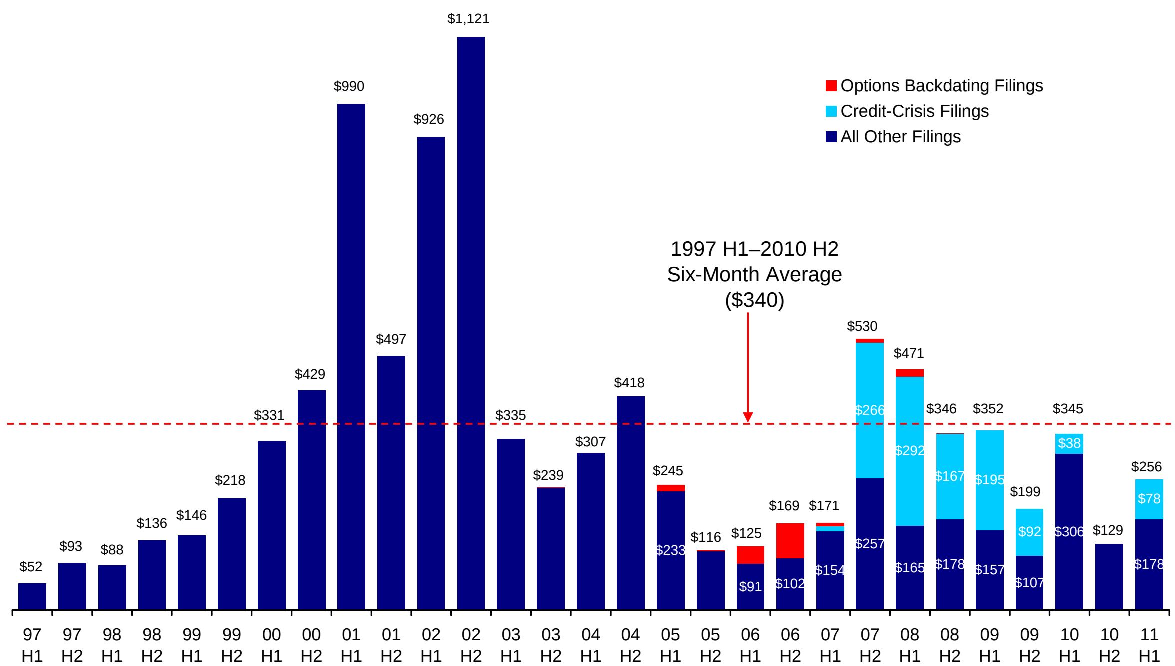
MARKET CAPITALIZATION LOSSES *continued*

The Disclosure Dollar Loss Index™ (DDL Index) tracks the sum of DDL for all class actions filed in a given half year. In the first half of 2011, the DDL Index totaled $48 billion, which represented a 152.6 percent increase from the second half of 2010 and was 25 percent below the 14-year historical average. The DDL Index shows that disclosure losses have remained below the historical average since the first half of 2009 (Figure 9). The low DDL Index in the first half of 2011 is consistent with the relatively low number of filings in the recent six-month periods, the high incidence of class actions against Chinese companies that tend to have small market capitalizations, and the continued trend of filings involving M&A activity and private securities.

The Maximum Dollar Loss Index™ (MDL Index) shows that market value losses during the class period for filings in the first half of 2011 increased by 98.4 percent to $256 billion compared to the prior six-month period (Figure 10). For reasons similar to those that explain the low DDL Index in the last six months, the MDL Index remained 24.7 percent below the historical average of $340 billion for the 14 years ending December 2010.

Figure 10

MAXIMUM DOLLAR LOSS INDEX™
SIX-MONTH PERIODS
1997–2011 H1
Dollars in Billions



MARKET CAPITALIZATION LOSSES *continued*

Figure 11 provides summary statistics for 2011 filings compared with the previous three six-month periods and the historical average from 1997 through 2010. The average DDL in the first half of 2011 increased substantially to $732 million, which was 130.2 percent higher than the second half of 2010 and comparable to the historical semiannual average DDL in the 14 years ending December 2010. The increase in average DDL primarily can be attributed to two mega filings during the first six months of 2011, which represented 47.6 percent of the total DDL during that period, and the lack of mega DDL cases in the second half of 2010.

The median DDL for the first half of 2011 decreased to $85 million, a 39.7 percent decline from the median in the second half of 2010, and 29.8 percent below the historical average between 1997 and 2010. One factor that contributed to the trend of decreasing median DDL was the increase in filings against Chinese companies.

The median MDL of $0.36 billion in the first half of 2011 was 7.7 percent lower than the second half of 2010 and is well below the historical semiannual average of $0.68 billion for the 14 years ending December 2010. The average MDL of $3.87 billion was a large increase compared with the second half of 2010 and is comparable to the historical average of $4.29 billion between 1997 and 2010.

Figure 11

FILINGS COMPARISON
SIX-MONTH PERIODS

	Average (1997 H1–2010 H2)	2009 H2	2010 H1	2010 H2	2011 H1
Class Action Filings	97	84	72	104	94
Disclosure Dollar Loss					
Total ($ Millions)	$64,368	$34,752	$53,403	$18,778	$48,342
Average ($ Millions)	$801	$552	$1,161	$318	$732
Median ($ Millions)	$121	$134	$162	$141	$85
Median DDL % Decline	23.1%	19.0%	14.2%	23.3%	17.4%
Maximum Dollar Loss					
Total ($ Billions)	$340	$199	$345	$129	$256
Average ($ Billions)	$4.29	$3.15	$7.49	$2.19	$3.87
Median ($ Billions)	$0.68	$0.93	$0.73	$0.39	$0.36

MEGA FILINGS

An analysis of mega filings, as measured by DDL and MDL, shows that a small number of filings accounted for most of the total market capitalization losses associated with class actions. Compared with the previous six-month period, there were fewer mega MDL filings in the first half of 2011, but they made up a larger portion of the MDL Index. In contrast, there were more mega DDL filings than in the previous six months.

Disclosure Dollar Loss

In the first half of 2011, there were two mega DDL filings—filings with a DDL of $5 billion or more. These filings accounted for $23 billion or 47.6 percent of the DDL Index in the first half of 2011. One of these filings was related to the credit crisis. In 2010, four mega filings represented 49.6 percent of the DDL Index, one of which was related to the credit crisis. However, there were no mega DDL filings in the second half of 2010. Mega filings represented 56.4 percent of the total DDL of all filings between 1997 and 2010.

Maximum Dollar Loss

Mega filings represented a larger portion of the MDL Index in the first half of 2011 compared with the second half of 2010. In the first half of 2011, there were five mega MDL filings—filings with an MDL of $10 billion or more. These five filings accounted for $216 billion or 84.4 percent of the MDL Index in the first half of 2011. One mega MDL filing was related to the credit crisis and three exceeded $25 billion. In the second half of 2010, there were four mega MDL filings, which accounted for 54.4 percent of the MDL Index in that period. None of the mega MDL filings in the second half of 2010 were related to the credit crisis and none exceeded $25 billion. Mega filings represented 73.8 percent of the total MDL of all filings between 1997 and 2010.

NEW DEVELOPMENTS

Increase in Class Actions against Chinese Companies

Over the last six months, there has been increased scrutiny of Chinese firms that gained access to U.S. equity markets via a process known as a reverse merger (also referred to as a reverse takeover or RTO).[7] Reverse mergers occur when an existing U.S.-listed shell company acquires a nonlisted firm, at which point the target firm's shareholders take control of the combined entity. The reverse merger process has allowed numerous companies, including many Chinese firms, to gain access to U.S. capital markets. According to the PCAOB, audits of some of these firms may not have been performed in accordance with PCAOB standards.[8]

During the first half of 2011, there were class actions filed against 25 Chinese companies, 24 of which gained access to the U.S. capital markets through a reverse merger. This is a substantial increase from 2010, when there were 12 filings against Chinese issuers, nine of which had previously undertaken a reverse merger.

The PCAOB issued a practice alert to its members in July 2010, emphasizing the need to ensure that audits of U.S. companies with foreign operations are completed in accordance with regulatory requirements.[9] This alert was followed by a research note identifying 159 reverse mergers involving firms from the China Region[10] that were completed between January 1, 2007, and March 31, 2010.[11] More recently, the Securities and Exchange Commission (SEC) began to target certain auditors for their work on companies that have undertaken reverse mergers.[12]

SEC Commissioner Luis Aguilar expressed concern over possible reverse merger accounting deficiencies and fraud in an April 2011 speech.[13] Subsequently, the SEC issued a June 2011 investor bulletin that warned investors about the risks associated with investing in companies that have undertaken reverse mergers.[14] Additionally, in June 2011, the NASDAQ exchange filed a proposed rule change with the SEC that would impose stricter listing requirements for companies that became public through reverse merger transactions.[15] In addition, Chinese firms that have completed reverse mergers have also begun to face increased scrutiny from market analysts and investors.[16] The Bloomberg Chinese Reverse Mergers Index, an equity index that tracks the performance of nearly 80 Chinese-based firms that have completed reverse mergers, declined in value by 44.4 percent in the first six months of 2011.

---

7 See also: Cornerstone Research, *Investigations and Litigation Related to Chinese Reverse Merger Companies—Financial, Economic, and Accounting Questions*, July 2011.

8 PCAOB, "Staff Audit Practice Alert No. 6," July 12, 2010.

9 Ibid.

10 The PCAOB practice alert defines "China Region" as the People's Republic of China, the Hong Kong Special Administrative Region, and Taiwan.

11 PCAOB, "Research Note # 2011-P1," March 14, 2011.

12 SEC Cease-and-Desist Order, *In the Matter of Moore Stephens Wurth Frazer & Torbet LLP and K. Dean Yamagata, CPA*, December 20, 2010.

13 Speech by Luis A. Aguilar, "Council of Institutional Investors Spring Meeting," April 4, 2011.

14 *SEC Investor Bulletin*, *Reverse Mergers*, June 9, 2011.

15 "Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing of Proposed Rule Change to Adopt Additional Listing Requirements for Reverse Mergers," June 8, 2011. http://www.sec.gov/rules/sro/nasdaq/2011/34-64633.pdf.

16 Barboza, David, and Azam Ahmed, "Muddy Waters Research Is a Thorn to Some Chinese Companies," *The New York Times*, June 9, 2011.

NEW DEVELOPMENTS *continued*

Class Actions Related to Mergers and Acquisitions

Class actions related to M&A transactions continued to be a notable phenomenon in the first half of 2011. These filings usually claim that shareholders received an unfair transaction price or were presented with inadequate or misleading information about the transaction from the company. Most of these filings also allege a breach of fiduciary duty. In the first six months of 2011, there were 21 filings related to M&A transactions, which represented a 22.2 percent decrease from the 27 M&A-related filings in the second half of 2010. The decrease in M&A filings occurred despite an increase in M&A activity over the last six months. According to Thomson Reuters, the number of announced domestic M&A transactions over $100 million increased 6.8 percent from the second half of 2010 to the first half of 2011.

Although M&A-related lawsuits traditionally are filed in state courts, the trend of filing parallel class actions in federal court took off in 2010 and continued in the first half of 2011.[17] Professor Joseph Grundfest, Director of the Stanford Law School Securities Class Action Clearinghouse in cooperation with Cornerstone Research, previously commented that the increase in federal M&A class actions suggests that "…plaintiff lawyers are scrambling for new business as traditional fraud cases seem to be on the decline...[and] may well bring an increasing percentage of these claims in federal court in an effort to control the litigation and to share in any fees that might result."[18] The federal class actions typically allege violations of Section 14 of the Securities Exchange Act of 1934, which forbids solicitation of proxies in violation of rules and regulations, and breach of fiduciary duty. M&A-related class actions filed in federal court may be a continuing phenomenon because litigation creates an obstacle and financial risk to the completion of the proposed transaction. As a result, companies tend to favor settlements to expedite deal completion, which provides incentives for plaintiff law firms to challenge transaction terms.[19]

17 Of the 21 M&A-related filings in federal court, 19 have corresponding filings in state courts.

18 Press Release, "Securities Class Action Filings Targeting M&A Transactions Increase Dramatically While Credit-Crisis Filings Fall Sharply According to Annual Report by Stanford Law School and Cornerstone Research," January 20, 2011. http://securities.stanford.edu/scac_press/Cornerstone_Research_Filings_2010_YIR_Release.pdf.

19 Trent, Ashley, "M&A Deal Lawsuits Soar," *Inside Counsel*, May 2011. http://www.insidecounsel.com/2011/05/01/ma-deal-lawsuits-soar?page=2.

Please direct any questions, requests for additional information, or permission to reprint charts to:

Alexander Aganin
650.853.1660 or aaganin@cornerstone.com

Boston
617.927.3000

Los Angeles
213.553.2500

Menlo Park
650.853.1660

New York
212.605.5000

San Francisco
415.229.8100

Washington
202.912.8900

www.cornerstone.com