

Senators from Utah, Senator BENNETT and Senator HATCH.

Mr. WARNER. Mr. President, reserving the right to object, I shall not. We also have an understanding that the closing statements of the managers appear in the RECORD as the last.

Mr. DOLE. I did get consent you could offer the managers' amendment right now.

The PRESIDING OFFICER. Without objection, it is so ordered.

AMENDMENT NO. 1464, AS MODIFIED

Mr. WARNER. Mr. President, I send to the desk a technical amendment to be added to the managers' amendment.

Mr. STEVENS. Has the agreement been entered into?

The PRESIDING OFFICER. Yes, it has. Without objection, the agreement is entered into.

Mr. WARNER. Mr. President, this is a technical amendment which includes the State of Maine as covered by the amendment of the Senator from New Hampshire.

I ask that it be accepted. It is to a previously agreed to amendment.

The PRESIDING OFFICER. Without objection, amendment No. 1464 is modified and is agreed to in that form.

The amendment (No. 1464), as modified, was agreed to, as follows:

At the appropriate place in the bill add the following new section:

SEC. .

The State of New Hampshire and the State of Maine shall be deemed as having met the safety belt use law requirements of section 153 of title 23 of the U.S. Code, upon certification by the Secretary of Transportation that the State has achieved—

(a) a safety belt use rate in each of fiscal years ending September 30, 1995 and September 30, 1996, of not less than 50 percent; and

(b) a safety belt use rate in each succeeding fiscal year thereafter of not less than the national average safety belt use rate, as determined by the Secretary of Transportation.

Mr. WARNER. Mr. President, I move to reconsider the vote.

Mr. CHAFEE. I move to lay that motion on the table.

The motion to lay on the table was agreed to.

VISIT TO THE SENATE BY MEMBERS OF THE CHILEAN SENATE

Mr. DODD. Mr. President, I wanted to take a moment, if I could, to say that we just had a very wonderful opportunity in the Senate Foreign Relations Committee room to have a very healthy and productive discussion with a group of our colleagues, Senators from Chile, who are here in the United States, to meet with their counterparts in the Senate and some Members of the House and the administration on a variety of subject matters, not the least of which—and it will not come as a great surprise—is NAFTA.

I know many colleagues share the view that Chile would be a welcome partner in the NAFTA agreements. That is a matter we will address in the future.

I would like to take this opportunity to introduce to my distinguished colleagues four Members of the Chilean Senate. With us today are Senator Arturo Alessandri, Senator Sebastian Pinera, Senator Hernan Larrain, and Senator Jaime Gazmuri.

We are pleased to welcome four of our colleagues from Chile to the U.S. Senate. We are delighted you are here on an important visit to our country.

[Applause]

PRIVATE SECURITIES LITIGATION REFORM ACT

The PRESIDING OFFICER. The clerk will report.

The legislative clerk read as follows:

A bill (S. 240) to amend the Securities Exchange Act of 1934 to establish a filing deadline and to provide certain safeguards to ensure that the interests of investors are well protected under the implied private action provisions of the Act.

The PRESIDING OFFICER. Is there objection to the immediate consideration of the bill?

There being no objection, the Senate proceeded to consider the bill, which had been reported from the Committee on Banking, Housing, and Urban Affairs, with an amendment to strike out all after the enacting clause and inserting in lieu thereof the following:

SECTION 1. SHORT TITLE; TABLE OF CONTENTS.

(a) *SHORT TITLE.*—This Act may be cited as the “Private Securities Litigation Reform Act of 1995”.

(b) *TABLE OF CONTENTS.*—The table of contents for this Act is as follows:

Sec. 1. Short title; table of contents.

TITLE I—REDUCTION OF ABUSIVE LITIGATION

Sec. 101. Elimination of certain abusive practices.

Sec. 102. Securities class action reform.

Sec. 103. Sanctions for abusive litigation.

Sec. 104. Requirements for securities fraud actions.

Sec. 105. Safe harbor for forward-looking statements.

Sec. 106. Written interrogatories.

Sec. 107. Amendment to Racketeer Influenced and Corrupt Organizations Act.

Sec. 108. Authority of Commission to prosecute aiding and abetting.

Sec. 109. Loss causation.

Sec. 110. Applicability.

TITLE II—REDUCTION OF COERCIVE SETTLEMENTS

Sec. 201. Limitation on damages.

Sec. 202. Proportionate liability.

Sec. 203. Applicability.

TITLE III—AUDITOR DISCLOSURE OF CORPORATE FRAUD

Sec. 301. Fraud detection and disclosure.

TITLE I—REDUCTION OF ABUSIVE LITIGATION

SEC. 101. ELIMINATION OF CERTAIN ABUSIVE PRACTICES.

(a) *PROHIBITION OF REFERRAL FEES.*—Section 15(c) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(c)) is amended by adding at the end the following new paragraph:

“(8) *PROHIBITION OF REFERRAL FEES.*—No broker or dealer, or person associated with a broker or dealer, may solicit or accept, directly or indirectly, remuneration for assisting an attorney in obtaining the representation of any person in any private action arising under this title or under the Securities Act of 1933.”.

(b) *ATTORNEY CONFLICT OF INTEREST.*—

(1) *SECURITIES ACT OF 1933.*—Section 20 of the Securities Act of 1933 (15 U.S.C. 77t) is amended by adding at the end the following new subsection:

“(f) *ATTORNEY CONFLICT OF INTEREST.*—In any private action arising under this title, if a plaintiff is represented by an attorney who directly owns or otherwise has a beneficial interest in the securities that are the subject of the litigation, the court shall make a determination of whether such ownership or other interest constitutes a conflict of interest sufficient to disqualify the attorney from representing the party.”.

(2) *SECURITIES EXCHANGE ACT OF 1934.*—Section 21 of the Securities Exchange Act of 1934 (15 U.S.C. 78u) is amended by adding at the end the following new subsection:

“(i) *ATTORNEY CONFLICT OF INTEREST.*—In any private action arising under this title, if a plaintiff is represented by an attorney who directly owns or otherwise has a beneficial interest in the securities that are the subject of the litigation, the court shall make a determination of whether such ownership or other interest constitutes a conflict of interest sufficient to disqualify the attorney from representing the party.”.

(c) *PROHIBITION OF ATTORNEYS’ FEES PAID FROM COMMISSION DISGORGEMENT FUNDS.*—

(1) *SECURITIES ACT OF 1933.*—Section 20 of the Securities Act of 1933 (15 U.S.C. 77t) is amended by adding at the end the following new subsection:

“(g) *PROHIBITION OF ATTORNEYS’ FEES PAID FROM COMMISSION DISGORGEMENT FUNDS.*—Except as otherwise ordered by the court upon motion by the Commission, or, in the case of an administrative action, as otherwise ordered by the Commission, funds disgorged as the result of an action brought by the Commission in Federal court, or as a result of any Commission administrative action, shall not be distributed as payment for attorneys’ fees or expenses incurred by private parties seeking distribution of the disgorged funds.”.

(2) *SECURITIES EXCHANGE ACT OF 1934.*—Section 21(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78u(d)) is amended by adding at the end the following new paragraph:

“(4) *PROHIBITION OF ATTORNEYS’ FEES PAID FROM COMMISSION DISGORGEMENT FUNDS.*—Except as otherwise ordered by the court upon motion by the Commission, or, in the case of an administrative action, as otherwise ordered by the Commission, funds disgorged as the result of an action brought by the Commission in Federal court, or as a result of any Commission administrative action, shall not be distributed as payment for attorneys’ fees or expenses incurred by private parties seeking distribution of the disgorged funds.”.

SEC. 102. SECURITIES CLASS ACTION REFORM.

(a) *RECOVERY RULES.*—

(1) *SECURITIES ACT OF 1933.*—Section 20 of the Securities Act of 1933 (15 U.S.C. 77t) is amended by adding at the end the following new subsection:

“(h) *RECOVERY RULES FOR PRIVATE CLASS ACTIONS.*—

“(1) *IN GENERAL.*—The rules contained in this subsection shall apply in each private action arising under this title that is brought as a plaintiff class action pursuant to the Federal Rules of Civil Procedure.

“(2) *CERTIFICATION FILED WITH COMPLAINTS.*—“(A) *IN GENERAL.*—Each plaintiff seeking to serve as a representative party on behalf of a class shall provide a sworn certification, which shall be personally signed by such plaintiff and filed with the complaint, that—

“(i) states that the plaintiff has reviewed the complaint and authorized its filing;

“(ii) states that the plaintiff did not purchase the security that is the subject of the complaint at the direction of plaintiff’s counsel or in order

to participate in any private action arising under this title;

“(iii) states that the plaintiff is willing to serve as a representative party on behalf of a class, including providing testimony at deposition and trial, if necessary;

“(iv) sets forth all of the transactions of the plaintiff in the security that is the subject of the complaint during the class period specified in the complaint;

“(v) identifies any action under this title, filed during the 3-year period preceding the date on which the certification is signed by the plaintiff, in which the plaintiff has sought to serve as a representative party on behalf of a class; and

“(vi) states that the plaintiff will not accept any payment for serving as a representative party on behalf of a class beyond the plaintiff's pro rata share of any recovery, except as ordered or approved by the court in accordance with paragraph (3).

“(B) NONWAIVER OF ATTORNEY-CLIENT PRIVILEGE.—The certification filed pursuant to subparagraph (A) shall not be construed to be a waiver of the attorney-client privilege.

“(3) RECOVERY BY PLAINTIFFS.—The share of any final judgment or of any settlement that is awarded to a representative party serving on behalf of a class shall be calculated in the same manner as the shares of the final judgment or settlement awarded to all other members of the class. Nothing in this paragraph shall be construed to limit the award of reasonable costs and expenses (including lost wages) directly relating to the representation of the class to any representative party serving on behalf of the class.

“(4) RESTRICTIONS ON SETTLEMENTS UNDER SEAL.—The terms and provisions of any settlement agreement of a class action shall not be filed under seal, except that on motion of any party to the settlement, the court may order filing under seal for those portions of a settlement agreement as to which good cause is shown for such filing under seal. For purposes of this paragraph, good cause shall exist only if publication of a term or provision of a settlement agreement would cause direct and substantial harm to any party.

“(5) RESTRICTIONS ON PAYMENT OF ATTORNEYS' FEES AND EXPENSES.—Total attorneys' fees and expenses awarded by the court to counsel for the plaintiff class shall not exceed a reasonable percentage of the amount of damages and prejudgment interest awarded to the class.

“(6) DISCLOSURE OF SETTLEMENT TERMS TO CLASS MEMBERS.—Any proposed or final settlement agreement that is published or otherwise disseminated to the class shall include each of the following statements, along with a cover page summarizing the information contained in such statements:

“(A) STATEMENT OF PLAINTIFF RECOVERY.—The amount of the settlement proposed to be distributed to the parties to the action, determined in the aggregate and on an average per share basis.

“(B) STATEMENT OF POTENTIAL OUTCOME OF CASE.—

“(i) AGREEMENT ON AMOUNT OF DAMAGES.—If the settling parties agree on the average amount of damages per share that would be recoverable if the plaintiff prevailed on each claim alleged under this title, a statement concerning the average amount of such potential damages per share.

“(ii) DISAGREEMENT ON AMOUNT OF DAMAGES.—If the parties do not agree on the average amount of damages per share that would be recoverable if the plaintiff prevailed on each claim alleged under this title, a statement from each settling party concerning the issue or issues on which the parties disagree.

“(iii) INADMISSIBILITY FOR CERTAIN PURPOSES.—A statement made in accordance with clause (i) or (ii) concerning the amount of damages shall not be admissible in any Federal or

State judicial action or administrative proceeding, other than an action or proceeding arising out of such statement.

“(C) STATEMENT OF ATTORNEYS' FEES OR COSTS SOUGHT.—If any of the settling parties or their counsel intend to apply to the court for an award of attorneys' fees or costs from any fund established as part of the settlement, a statement indicating which parties or counsel intend to make such an application, the amount of fees and costs that will be sought (including the amount of such fees and costs determined on an average per share basis), and a brief explanation supporting the fees and costs sought.

“(D) IDENTIFICATION OF LAWYERS' REPRESENTATIVES.—The name, telephone number, and address of one or more representatives of counsel for the plaintiff class who will be reasonably available to answer questions from class members concerning any matter contained in any notice of settlement published or otherwise disseminated to the class.

“(E) REASONS FOR SETTLEMENT.—A brief statement explaining the reasons why the parties are proposing the settlement.

“(F) OTHER INFORMATION.—Such other information as may be required by the court.”

(2) SECURITIES EXCHANGE ACT OF 1934.—Section 21 of the Securities Exchange Act of 1934 (15 U.S.C. 78u) is amended by adding at the end the following new subsection:

“(j) RECOVERY RULES FOR PRIVATE CLASS ACTIONS.—

“(1) IN GENERAL.—The rules contained in this subsection shall apply in each private action arising under this title that is brought as a plaintiff class action pursuant to the Federal Rules of Civil Procedure.

“(2) CERTIFICATION FILED WITH COMPLAINTS.—

“(A) IN GENERAL.—Each plaintiff seeking to serve as a representative party on behalf of a class shall provide a sworn certification, which shall be personally signed by such plaintiff and filed with the complaint, that—

“(i) states that the plaintiff has reviewed the complaint and authorized its filing;

“(ii) states that the plaintiff did not purchase the security that is the subject of the complaint at the direction of plaintiff's counsel or in order to participate in any private action arising under this title;

“(iii) states that the plaintiff is willing to serve as a representative party on behalf of a class, including providing testimony at deposition and trial, if necessary;

“(iv) sets forth all of the transactions of the plaintiff in the security that is the subject of the complaint during the class period specified in the complaint;

“(v) identifies any action under this title, filed during the 3-year period preceding the date on which the certification is signed by the plaintiff, in which the plaintiff has sought to serve as a representative party on behalf of a class; and

“(vi) states that the plaintiff will not accept any payment for serving as a representative party on behalf of a class beyond the plaintiff's pro rata share of any recovery, except as ordered or approved by the court in accordance with paragraph (3).

“(B) NONWAIVER OF ATTORNEY-CLIENT PRIVILEGE.—The certification filed pursuant to subparagraph (A) shall not be construed to be a waiver of the attorney-client privilege.

“(3) RECOVERY BY PLAINTIFFS.—The share of any final judgment or of any settlement that is awarded to a representative party serving on behalf of a class shall be calculated in the same manner as the shares of the final judgment or settlement awarded to all other members of the class. Nothing in this paragraph shall be construed to limit the award to any representative party serving on behalf of a class of reasonable costs and expenses (including lost wages) directly relating to the representation of the class.

“(4) RESTRICTIONS ON SETTLEMENTS UNDER SEAL.—The terms and provisions of any settle-

ment agreement of a class action shall not be filed under seal, except that on motion of any party to the settlement, the court may order filing under seal for those portions of a settlement agreement as to which good cause is shown for such filing under seal. For purposes of this paragraph, good cause shall exist only if publication of a term or provision of a settlement agreement would cause direct and substantial harm to any party.

“(5) RESTRICTIONS ON PAYMENT OF ATTORNEYS' FEES AND EXPENSES.—Total attorneys' fees and expenses awarded by the court to counsel for the plaintiff class shall not exceed a reasonable percentage of the amount of damages and prejudgment interest awarded to the class.

“(6) DISCLOSURE OF SETTLEMENT TERMS TO CLASS MEMBERS.—Any proposed or final settlement agreement that is published or otherwise disseminated to the class shall include each of the following statements, along with a cover page summarizing the information contained in such statements:

“(A) STATEMENT OF PLAINTIFF RECOVERY.—The amount of the settlement proposed to be distributed to the parties to the action, determined in the aggregate and on an average per share basis.

“(B) STATEMENT OF POTENTIAL OUTCOME OF CASE.—

“(i) AGREEMENT ON AMOUNT OF DAMAGES.—If the settling parties agree on the average amount of damages per share that would be recoverable if the plaintiff prevailed on each claim alleged under this title, a statement concerning the average amount of such potential damages per share.

“(ii) DISAGREEMENT ON AMOUNT OF DAMAGES.—If the parties do not agree on the average amount of damages per share that would be recoverable if the plaintiff prevailed on each claim alleged under this title, a statement from each settling party concerning the issue or issues on which the parties disagree.

“(iii) INADMISSIBILITY FOR CERTAIN PURPOSES.—A statement made in accordance with clause (i) or (ii) concerning the amount of damages shall not be admissible in any Federal or State judicial action or administrative proceeding, other than an action or proceeding arising out of such statement.

“(C) STATEMENT OF ATTORNEYS' FEES OR COSTS SOUGHT.—If any of the settling parties or their counsel intend to apply to the court for an award of attorneys' fees or costs from any fund established as part of the settlement, a statement indicating which parties or counsel intend to make such an application, the amount of fees and costs that will be sought (including the amount of such fees and costs determined on an average per share basis), and a brief explanation supporting the fees and costs sought.

“(D) IDENTIFICATION OF LAWYERS' REPRESENTATIVES.—The name, telephone number, and address of one or more representatives of counsel for the plaintiff class who will be reasonably available to answer questions from class members concerning any matter contained in any notice of settlement published or otherwise disseminated to the class.

“(E) REASONS FOR SETTLEMENT.—A brief statement explaining the reasons why the parties are proposing the settlement.

“(F) OTHER INFORMATION.—Such other information as may be required by the court.”

(b) APPOINTMENT OF LEAD PLAINTIFF.—
(1) SECURITIES ACT OF 1933.—Section 20 of the Securities Act of 1933 (15 U.S.C. 77t) is amended by adding at the end the following new subsection:

“(i) PROCEDURES GOVERNING APPOINTMENT OF LEAD PLAINTIFF IN CLASS ACTIONS.—

“(1) EARLY NOTICE TO CLASS MEMBERS.—

“(A) IN GENERAL.—In any private action arising under this title that is brought on behalf of a class, not later than 20 days after the date on which the complaint is filed, the plaintiff or

plaintiffs shall cause to be published, in a widely circulated national business-oriented publication or wire service, a notice advising members of the purported plaintiff class—

“(i) of the pendency of the action, the claims asserted therein, and the purported class period; and

“(ii) that, not later than 60 days after the date on which the notice is published, any member of the purported class may move the court to serve as lead plaintiff of the purported class.

“(B) ADDITIONAL NOTICES MAY BE REQUIRED UNDER FEDERAL RULES.—Notice required under subparagraph (A) shall be in addition to any notice required pursuant to the Federal Rules of Civil Procedure.

“(2) APPOINTMENT OF LEAD PLAINTIFF.—

“(A) IN GENERAL.—Not later than 90 days after the date on which a notice is published under paragraph (1)(A), the court shall consider any motion made by a purported class member in response to the notice, and shall appoint as lead plaintiff the member or members of the purported plaintiff class that the court determines to be most capable of adequately representing the interests of class members (hereafter in this subsection referred to as the ‘most adequate plaintiff’) in accordance with this paragraph.

“(B) CONSOLIDATED ACTIONS.—If more than one action on behalf of a class asserting substantially the same claim or claims arising under this title has been filed, and any party has sought to consolidate those actions for pretrial purposes or for trial, the court shall not make the determination required by subparagraph (A) until after the decision on the motion to consolidate is rendered. As soon as practicable after such decision is rendered, the court shall appoint the most adequate plaintiff as lead plaintiff for the consolidated actions in accordance with this paragraph.

“(C) REBUTTABLE PRESUMPTION.—

“(i) IN GENERAL.—Subject to clause (ii), for purposes of subparagraph (A), the court shall adopt a presumption that the most adequate plaintiff in any private action arising under this title is the person or group of persons that—

“(I) has either filed the complaint or made a motion in response to a notice under paragraph (1)(A);

“(II) in the determination of the court, has the largest financial interest in the relief sought by the class; and

“(III) otherwise satisfies the requirements of Rule 23 of the Federal Rules of Civil Procedure.

“(ii) REBUTTAL EVIDENCE.—The presumption described in clause (i) may be rebutted only upon proof by a member of the purported plaintiff class that the presumptively most adequate plaintiff—

“(I) will not fairly and adequately protect the interests of the class; or

“(II) is subject to unique defenses that render such plaintiff incapable of adequately representing the class.

“(iii) DISCOVERY.—For purposes of clause (ii), discovery relating to whether a member or members of the purported plaintiff class is the most adequate plaintiff—

“(I) may not be conducted by any defendant; and

“(II) may be conducted by a plaintiff only if the plaintiff first demonstrates a reasonable basis for a finding that the presumptively most adequate plaintiff is incapable of adequately representing the class.

“(D) SELECTION OF LEAD COUNSEL.—The most adequate plaintiff shall, subject to the approval of the court, select and retain counsel to represent the class.”.

(2) SECURITIES EXCHANGE ACT OF 1934.—Section 21 of the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended by adding at the end the following new subsection:

“(k) PROCEDURES GOVERNING APPOINTMENT OF LEAD PLAINTIFF IN CLASS ACTIONS.—

“(1) EARLY NOTICE TO CLASS MEMBERS.—

“(A) IN GENERAL.—In any private action arising under this title that is brought on behalf of

a class, not later than 20 days after the date on which the complaint is filed, the plaintiff or plaintiffs shall cause to be published, in a widely circulated national business-oriented publication or wire service, a notice advising members of the purported plaintiff class—

“(i) of the pendency of the action, the claims asserted therein, and the purported class period; and

“(ii) that, not later than 60 days after the date on which the notice is published, any member of the purported class may move the court to serve as lead plaintiff of the purported class.

“(B) ADDITIONAL NOTICES MAY BE REQUIRED UNDER FEDERAL RULES.—Notice required under subparagraph (A) shall be in addition to any notice required pursuant to the Federal Rules of Civil Procedure.

“(2) APPOINTMENT OF LEAD PLAINTIFF.—

“(A) IN GENERAL.—Not later than 90 days after the date on which a notice is published under paragraph (1)(A), the court shall consider any motion made by a purported class member in response to the notice, and shall appoint as lead plaintiff the member or members of the purported plaintiff class that the court determines to be most capable of adequately representing the interests of class members (hereafter in this subsection referred to as the ‘most adequate plaintiff’) in accordance with this paragraph.

“(B) CONSOLIDATED ACTIONS.—If more than one action on behalf of a class asserting substantially the same claim or claims arising under this title has been filed, and any party has sought to consolidate those actions for pretrial purposes or for trial, the court shall not make the determination required by subparagraph (A) until after the decision on the motion to consolidate is rendered. As soon as practicable after such decision is rendered, the court shall appoint the most adequate plaintiff as lead plaintiff for the consolidated actions in accordance with this paragraph.

“(C) REBUTTABLE PRESUMPTION.—

“(i) IN GENERAL.—Subject to clause (ii), for purposes of subparagraph (A), the court shall adopt a presumption that the most adequate plaintiff in any private action arising under this title is the person or group of persons that—

“(I) has either filed the complaint or made a motion in response to a notice under paragraph (1)(A);

“(II) in the determination of the court, has the largest financial interest in the relief sought by the class; and

“(III) otherwise satisfies the requirements of Rule 23 of the Federal Rules of Civil Procedure.

“(ii) REBUTTAL EVIDENCE.—The presumption described in clause (i) may be rebutted only upon proof by a member of the purported plaintiff class that the presumptively most adequate plaintiff—

“(I) will not fairly and adequately protect the interests of the class; or

“(II) is subject to unique defenses that render such plaintiff incapable of adequately representing the class.

“(iii) DISCOVERY.—For purposes of clause (ii), discovery relating to whether a member or members of the purported plaintiff class is the most adequate plaintiff—

“(I) may not be conducted by any defendant; and

“(II) may be conducted by a plaintiff only if the plaintiff first demonstrates a reasonable basis for a finding that the presumptively most adequate plaintiff is incapable of adequately representing the class.

“(D) SELECTION OF LEAD COUNSEL.—The most adequate plaintiff shall, subject to the approval of the court, select and retain counsel to represent the class.”.

SEC. 103. SANCTIONS FOR ABUSIVE LITIGATION.

(a) SECURITIES ACT OF 1933.—Section 20 of the Securities Act of 1933 (15 U.S.C. 77t) is amended by adding at the end the following new subsection:

“(j) SANCTIONS FOR ABUSIVE LITIGATION.—

“(1) MANDATORY REVIEW BY COURT.—In any private action arising under this title, upon final adjudication of the action, the court shall include in the record specific findings regarding compliance by each party and each attorney representing any party with each requirement of Rule 11(b) of the Federal Rules of Civil Procedure.

“(2) MANDATORY SANCTIONS.—If the court makes a finding under paragraph (1) that a party or attorney violated any requirement of Rule 11(b) of the Federal Rules of Civil Procedure, the court shall impose sanctions on such party or attorney in accordance with Rule 11 of the Federal Rules of Civil Procedure.

“(3) PRESUMPTION IN FAVOR OF ATTORNEYS’ FEES AND COSTS.—

“(A) IN GENERAL.—Subject to subparagraphs (B) and (C), for purposes of paragraph (2), the court shall adopt a presumption that the appropriate sanction for failure of the complaint to comply with any requirement of Rule 11(b) of the Federal Rules of Civil Procedure is an award to the opposing party of all of the reasonable attorneys’ fees and other expenses incurred as a direct result of the violation.

“(B) REBUTTAL EVIDENCE.—The presumption described in subparagraph (A) may be rebutted only upon proof by the party or attorney against whom sanctions are to be imposed that—

“(i) the award of attorneys’ fees and other expenses will impose an undue burden on that party or attorney; or

“(ii) the violation of Rule 11(b) of the Federal Rules of Civil Procedure was de minimis.

“(C) SANCTIONS.—If the party or attorney against whom sanctions are to be imposed meets its burden under subparagraph (B), the court shall award the sanctions that the court deems appropriate pursuant to Rule 11 of the Federal Rules of Civil Procedure.”.

(b) SECURITIES EXCHANGE ACT OF 1934.—Section 21 of the Securities Exchange Act of 1934 (15 U.S.C. 78u) is amended by adding at the end the following new subsection:

“(1) SANCTIONS FOR ABUSIVE LITIGATION.—

“(1) MANDATORY REVIEW BY COURT.—In any private action arising under this title, upon final adjudication of the action, the court shall include in the record specific findings regarding compliance by each party and each attorney representing any party with each requirement of Rule 11(b) of the Federal Rules of Civil Procedure.

“(2) MANDATORY SANCTIONS.—If the court makes a finding under paragraph (1) that a party or attorney violated any requirement of Rule 11(b) of the Federal Rules of Civil Procedure, the court shall impose sanctions in accordance with Rule 11 of the Federal Rules of Civil Procedure on such party or attorney.

“(3) PRESUMPTION IN FAVOR OF ATTORNEYS’ FEES AND COSTS.—

“(A) IN GENERAL.—Subject to subparagraphs (B) and (C), for purposes of paragraph (2), the court shall adopt a presumption that the appropriate sanction for failure of the complaint to comply with any requirement of Rule 11(b) of the Federal Rules of Civil Procedure is an award to the opposing party of all of the reasonable attorneys’ fees and other expenses incurred as a direct result of the violation.

“(B) REBUTTAL EVIDENCE.—The presumption described in subparagraph (A) may be rebutted only upon proof by the party or attorney against whom sanctions are to be imposed that—

“(i) the award of attorneys’ fees and other expenses will impose an undue burden on that party or attorney; or

“(ii) the violation of Rule 11(b) of the Federal Rules of Civil Procedure was de minimis.

“(C) SANCTIONS.—If the party or attorney against whom sanctions are to be imposed meets its burden under subparagraph (B), the court shall award the sanctions that the court deems

appropriate pursuant to Rule 11 of the Federal Rules of Civil Procedure.”

SEC. 104. REQUIREMENTS FOR SECURITIES FRAUD ACTIONS.

(a) SECURITIES ACT OF 1933.—

(1) STAY OF DISCOVERY.—Section 20 of the Securities Act of 1933 (15 U.S.C. 77t) is amended by adding at the end the following new subsection:

“(k) STAY OF DISCOVERY.—In any private action arising under this title, during the pendency of any motion to dismiss, all discovery and other proceedings shall be stayed unless the court finds, upon the motion of any party, that particularized discovery is necessary to preserve evidence or to prevent undue prejudice to that party.”

(2) PRESERVATION OF EVIDENCE.—Section 20 of the Securities Act of 1933 (15 U.S.C. 77t) is amended by adding at the end the following new subsection:

“(l) PRESERVATION OF EVIDENCE.—It shall be unlawful for any person, upon receiving actual notice that a complaint has been filed in a private action arising under this title naming that person as a defendant and that describes the allegations contained in the complaint, to willfully destroy or otherwise alter any document, data compilation (including any electronically recorded or stored data), or tangible object that is in the custody or control of that person and that is relevant to the allegations.”

(b) SECURITIES EXCHANGE ACT OF 1934.—Title I of the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended by adding at the end the following new section:

“SEC. 36. REQUIREMENTS FOR SECURITIES FRAUD ACTIONS.

“(a) MISLEADING STATEMENTS AND OMISSIONS.—In any private action arising under this title in which the plaintiff alleges that the defendant—

“(1) made an untrue statement of a material fact; or

“(2) omitted to state a material fact necessary in order to make the statements made, in the light of the circumstances in which they were made, not misleading;

the complaint shall specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the plaintiff shall set forth all information on which that belief is formed.

“(b) REQUIRED STATE OF MIND.—In any private action arising under this title in which the plaintiff may recover money damages only on proof that the defendant acted with a particular state of mind, the plaintiff’s complaint shall, with respect to each act or omission alleged to violate this title, specifically allege facts giving rise to a strong inference that the defendant acted with the required state of mind.

“(c) MOTION TO DISMISS; STAY OF DISCOVERY.—

“(1) DISMISSAL FOR FAILURE TO MEET PLEADING REQUIREMENTS.—In any private action arising under this title, the court shall, on the motion of any defendant, dismiss the complaint if the requirements of subsections (a) and (b) are not met.

“(2) STAY OF DISCOVERY.—In any private action arising under this title, during the pendency of any motion to dismiss, all discovery and other proceedings shall be stayed unless the court finds upon the motion of any party that particularized discovery is necessary to preserve evidence or to prevent undue prejudice to that party.

“(3) PRESERVATION OF EVIDENCE.—It shall be unlawful for any person, upon receiving actual notice that a complaint has been filed in a private action arising under this title naming that person as a defendant and that describes the allegations contained in the complaint, to willfully destroy or otherwise alter any document, data compilation (including any electronically

recorded or stored data), or tangible object that is in the custody or control of that person and that is relevant to the allegations.

“(d) LOSS CAUSATION.—In any private action arising under this title, the plaintiff shall have the burden of proving that the act or omission alleged to violate this title caused any loss incurred by the plaintiff. Damages arising from such loss may be mitigated upon a showing by the defendant that factors unrelated to such act or omission contributed to the loss.”

SEC. 105. SAFE HARBOR FOR FORWARD-LOOKING STATEMENTS.

(a) SECURITIES ACT OF 1933.—Title I of the Securities Act of 1933 (15 U.S.C. 77a et seq.) is amended by inserting after section 13 the following new section:

“SEC. 13A. APPLICATION OF SAFE HARBOR FOR FORWARD-LOOKING STATEMENTS.

“(a) SAFE HARBOR.—

“(1) IN GENERAL.—In any private action arising under this title that is based on a fraudulent statement, an issuer that is subject to the reporting requirements of section 13(a) or section 15(d) of the Securities Exchange Act of 1934, a person acting on behalf of such issuer, or an outside reviewer retained by such issuer, shall not be liable with respect to any forward-looking statement, whether written or oral, if and to the extent that the statement—

“(A) projects, estimates, or describes future events; and

“(B) refers clearly (and, except as otherwise provided by rule or regulation, proximately) to—

“(i) such projections, estimates, or descriptions as forward-looking statements; and

“(ii) the risk that actual results may differ materially from such projections, estimates, or descriptions.

“(2) EFFECT ON OTHER SAFE HARBORS.—The exemption from liability provided for in paragraph (1) shall be in addition to any exemption that the Commission may establish by rule or regulation under subsection (e).

“(b) DEFINITION OF FORWARD-LOOKING STATEMENT.—For purposes of this section, the term ‘forward-looking statement’ means—

“(1) a statement containing a projection of revenues, income (including income loss), earnings (including earnings loss) per share, capital expenditures, dividends, capital structure, or other financial items;

“(2) a statement of the plans and objectives of management for future operations;

“(3) a statement of future economic performance contained in a discussion and analysis of financial condition by the management or in the results of operations included pursuant to the rules and regulations of the Commission;

“(4) any disclosed statement of the assumptions underlying or relating to any statement described in paragraph (1), (2), or (3); or

“(5) a statement containing a projection or estimate of such other items as may be specified by rule or regulation of the Commission.

“(c) EXCLUSIONS.—The exemption from liability provided for in subsection (a) does not apply to a forward-looking statement that is—

“(1) knowingly made with the expectation, purpose, and actual intent of misleading investors;

“(2) except to the extent otherwise specifically provided by rule, regulation, or order of the Commission, made with respect to the business or operations of the issuer, if the issuer—

“(A) has been, during the 3-year period preceding the date on which the statement was first made, convicted of any felony or misdemeanor described in clauses (i) through (iv) of section 15(b)(4)(B), or has been made the subject of a judicial or administrative decree or order arising out of a governmental action that—

“(i) prohibits future violations of the anti-fraud provisions of the securities laws, as that term is defined in section 3 of the Securities Exchange Act of 1934;

“(ii) requires that the issuer cease and desist from violating the anti-fraud provisions of the securities laws; or

“(iii) determines that the issuer violated the anti-fraud provisions of the securities laws;

“(B) makes the forward-looking statement in connection with an offering of securities by a blank check company, as that term is defined under the rules or regulations of the Commission;

“(C) issues penny stock, as that term is defined in section 3(a)(51) of the Securities Exchange Act of 1934, and the rules, regulations, or orders issued pursuant to that section;

“(D) makes the forward-looking statement in connection with a rollup transaction, as that term is defined under the rules or regulations of the Commission; or

“(E) makes the forward-looking statement in connection with a going private transaction, as that term is defined under the rules or regulations of the Commission issued pursuant to section 13(e) of the Securities Exchange Act of 1934; or

“(3) except to the extent otherwise specifically provided by rule or regulation of the Commission—

“(A) included in a financial statement prepared in accordance with generally accepted accounting principles;

“(B) contained in a registration statement of, or otherwise issued by, an investment company, as that term is defined in section 3(a) of the Investment Company Act of 1940;

“(C) made in connection with a tender offer;

“(D) made by or in connection with an offering by a partnership, limited liability corporation, or a direct participation investment program, as those terms are defined by rule or regulation of the Commission; or

“(E) made in a disclosure of beneficial ownership in a report required to be filed with the Commission pursuant to section 13(d) of the Securities Exchange Act of 1934.

“(d) STAY PENDING DECISION ON MOTION.—In any private action arising under this title, the court shall stay discovery during the pendency of any motion by a defendant (other than discovery that is specifically directed to the applicability of the exemption provided for in this section) for summary judgment that is based on the grounds that—

“(1) the statement or omission upon which the complaint is based is a forward-looking statement within the meaning of this section; and

“(2) the exemption provided for in this section precludes a claim for relief.

“(e) AUTHORITY.—In addition to the exemption provided for in this section, the Commission may, by rule or regulation, provide exemptions from liability under any provision of this title, or of any rule or regulation issued under this title, that is based on a statement that includes or that is based on projections or other forward-looking information, if and to the extent that any such exemption is, as determined by the Commission, consistent with the public interest and the protection of investors.

“(f) COMMISSION DISGORGEMENT ACTIONS.—

“(1) IN GENERAL.—If the Commission, in any proceeding, orders or obtains (by settlement, court order, or otherwise) a payment of funds from a person who has violated this title through means that included the utilization of a forward-looking statement, and if any portion of such funds is set aside or otherwise held for or available to persons who suffered losses in connection with such violation, no person shall be precluded from participating in the distribution of, or otherwise receiving, a portion of such funds by reason of the application of this section.

“(2) JUDGMENT FOR LOSSES SUFFERED.—In any action by the Commission alleging a violation of this title in which the defendant or respondent is alleged to have utilized a forward-looking statement in furtherance of such violation, the Commission may, upon a sufficient showing, in addition to all other remedies available to the Commission, obtain a judgment for the payment

of an amount equal to all losses suffered by reason of the utilization of the forward-looking statement.

“(g) EFFECT ON OTHER AUTHORITY OF COMMISSION.—Nothing in this section limits, either expressly or by implication, the authority of the Commission to exercise similar authority or to adopt similar rules and regulations with respect to forward-looking statements under any other statute under which the Commission exercises rulemaking authority.”

(b) SECURITIES EXCHANGE ACT OF 1934.—Title I of the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended by adding at the end the following new section:

“SEC. 37. APPLICATION OF SAFE HARBOR FOR FORWARD-LOOKING STATEMENTS.

“(a) SAFE HARBOR.—

“(1) IN GENERAL.—In any private action arising under this title that is based on a fraudulent statement, an issuer that is subject to the reporting requirements of section 13(a) or section 15(d) of the Securities Exchange Act of 1934, a person acting on behalf of such issuer, or an outside reviewer retained by such issuer, shall not be liable with respect to any forward-looking statement, whether written or oral, if and to the extent that the statement—

“(A) projects, estimates, or describes future events; and

“(B) refers clearly (and, except as otherwise provided by rule or regulation, proximately) to—

“(i) such projections, estimates, or descriptions as forward-looking statements; and

“(ii) the risk that actual results may differ materially from such projections, estimates, or descriptions.

“(2) EFFECT ON OTHER SAFE HARBORS.—The exemption from liability provided for in paragraph (1) shall be in addition to any exemption that the Commission may establish by rule or regulation under subsection (e).

“(b) DEFINITION OF FORWARD-LOOKING STATEMENT.—For purposes of this section, the term ‘forward-looking statement’ means—

“(1) a statement containing a projection of revenues, income (including income loss), earnings (including earnings loss) per share, capital expenditures, dividends, capital structure, or other financial items;

“(2) a statement of the plans and objectives of management for future operations;

“(3) a statement of future economic performance contained in a discussion and analysis of financial condition by the management or in the results of operations included pursuant to the rules and regulations of the Commission;

“(4) any disclosed statement of the assumptions underlying or relating to any statement described in paragraph (1), (2), or (3); or

“(5) a statement containing a projection or estimate of such other items as may be specified by rule or regulation of the Commission.

“(c) EXCLUSIONS.—The exemption from liability provided for in subsection (a) does not apply to a forward-looking statement that is—

“(1) knowingly made with the expectation, purpose, and actual intent of misleading investors;

“(2) except to the extent otherwise specifically provided by rule, regulation, or order of the Commission, made with respect to the business or operations of the issuer, if the issuer—

“(A) has been, during the 3-year period preceding the date on which the statement was first made, convicted of any felony or misdemeanor described in clauses (i) through (iv) of section 15(b)(4)(B), or has been made the subject of a judicial or administrative decree or order arising out of a governmental action that—

“(i) prohibits future violations of the anti-fraud provisions of the securities laws;

“(ii) requires that the issuer cease and desist from violating the anti-fraud provisions of the securities laws; or

“(iii) determines that the issuer violated the anti-fraud provisions of the securities laws;

“(B) makes the forward-looking statement in connection with an offering of securities by a

blank check company, as that term is defined under the rules or regulations of the Commission;

“(C) issues penny stock;

“(D) makes the forward-looking statement in connection with a rollout transaction, as that term is defined under the rules or regulations of the Commission; or

“(E) makes the forward-looking statement in connection with a going private transaction, as that term is defined under the rules or regulations of the Commission issued pursuant to section 13(e); or

“(3) except to the extent otherwise specifically provided by rule or regulation of the Commission—

“(A) included in financial statements prepared in accordance with generally accepted accounting principles;

“(B) contained in a registration statement of, or otherwise issued by, an investment company;

“(C) made in connection with a tender offer;

“(D) made by or in connection with an offering by a partnership, limited liability corporation, or a direct participation investment program, as those terms are defined by rule or regulation of the Commission; or

“(E) made in a disclosure of beneficial ownership in a report required to be filed with the Commission pursuant to section 13(d).

“(d) STAY PENDING DECISION ON MOTION.—In any private action arising under this title, the court shall stay discovery during the pendency of any motion by a defendant (other than discovery that is specifically directed to the applicability of the exemption provided for in this section) for summary judgment that is based on the grounds that—

“(1) the statement or omission upon which the complaint is based is a forward-looking statement within the meaning of this section; and

“(2) the exemption provided for in this section precludes a claim for relief.

“(e) AUTHORITY.—In addition to the exemption provided for in this section, the Commission may, by rule or regulation, provide exemptions from liability under any provision of this title, or of any rule or regulation issued under this title, that is based on a statement that includes or that is based on projections or other forward-looking information, if and to the extent that any such exemption is, as determined by the Commission, consistent with the public interest and the protection of investors.

“(f) COMMISSION DISGORGEMENT ACTIONS.—

“(1) IN GENERAL.—If the Commission, in any proceeding, orders or obtains (by settlement, court order, or otherwise) a payment of funds from a person who has violated this title through means that included the utilization of a forward-looking statement, and if any portion of such funds is set aside or otherwise held for or available to persons who suffered losses in connection with such violation, no person shall be precluded from participating in the distribution of, or otherwise receiving, a portion of such funds by reason of the application of this section.

“(2) JUDGMENT FOR LOSSES SUFFERED.—In any action by the Commission alleging a violation of this title in which the defendant or respondent is alleged to have utilized a forward-looking statement in furtherance of such violation, the Commission may, upon a sufficient showing, in addition to all other remedies available to the Commission, obtain a judgment for the payment of an amount equal to all losses suffered by reason of the utilization of the forward-looking statement.

“(g) EFFECT ON OTHER AUTHORITY OF COMMISSION.—Nothing in this section limits, either expressly or by implication, the authority of the Commission to exercise similar authority or to adopt similar rules and regulations with respect to forward-looking statements under any other statute under which the Commission exercises rulemaking authority.”

(c) INVESTMENT COMPANY ACT OF 1940.—Section 24 of the Investment Company Act of 1940

(15 U.S.C. 80a-24) is amended by adding at the end the following new subsection:

“(g) REGULATORY AUTHORITY FOR FORWARD-LOOKING STATEMENTS.—

“(1) IN GENERAL.—The Commission shall review and, if necessary to carry out the purposes of this title, promulgate such rules and regulations as may be necessary to describe conduct with respect to the making of forward-looking statements that the Commission deems does not provide a basis for liability in any private action arising under this title.

“(2) REQUIREMENTS.—A rule or regulation promulgated under paragraph (1) shall—

“(A) include clear and objective guidance that the Commission finds sufficient for the protection of investors;

“(B) prescribe such guidance with sufficient particularity that compliance shall be readily ascertainable by issuers prior to issuance of securities; and

“(C) provide that forward-looking statements that are in compliance with such guidance and that concern the future economic performance of an issuer of securities registered under section 12 shall be deemed not to be in violation of this title.

“(3) EFFECT ON OTHER AUTHORITY OF COMMISSION.—Nothing in this subsection limits, either expressly or by implication, the authority of the Commission to exercise similar authority or to adopt similar rules and regulations with respect to forward-looking statements under any other statute under which the Commission exercises rulemaking authority.”

SEC. 106. WRITTEN INTERROGATORIES.

(a) SECURITIES ACT OF 1933.—Section 20 of the Securities Act of 1933 (15 U.S.C. 77t) is amended by adding at the end the following new subsection:

“(m) DEFENDANT’S RIGHT TO WRITTEN INTERROGATORIES.—In any private action arising under this title in which the plaintiff may recover money damages only on proof that a defendant acted with a particular state of mind, the court shall, when requested by a defendant, submit to the jury a written interrogatory on the issue of each such defendant’s state of mind at the time the alleged violation occurred.”

(b) SECURITIES EXCHANGE ACT OF 1934.—Section 21 of the Securities Exchange Act of 1934 (15 U.S.C. 78u) is amended by adding at the end the following new subsection:

“(m) DEFENDANT’S RIGHT TO WRITTEN INTERROGATORIES.—In any private action arising under this title in which the plaintiff may recover money damages, the court shall, when requested by a defendant, submit to the jury a written interrogatory on the issue of each such defendant’s state of mind at the time the alleged violation occurred.”

SEC. 107. AMENDMENT TO RACKETEER INFLUENCED AND CORRUPT ORGANIZATIONS ACT.

Section 1964(c) of title 18, United States Code, is amended by inserting before the period “, except that no person may rely upon conduct that would have been actionable as fraud in the purchase or sale of securities to establish a violation of section 1962”.

SEC. 108. AUTHORITY OF COMMISSION TO PROSECUTE AIDING AND ABETTING.

Section 20 of the Securities Exchange Act of 1934 (15 U.S.C. 78t) is amended—

(1) by striking the section heading and inserting the following:

“LIABILITY OF CONTROLLING PERSONS AND PERSONS WHO AID AND ABET VIOLATIONS”; AND

(2) by adding at the end the following new subsection:

“(e) PROSECUTION OF PERSONS WHO AID AND ABET VIOLATIONS.—For purposes of any action brought by the Commission under paragraph (1) or (3) of section 21(d), any person that knowingly provides substantial assistance to another person in the violation of a provision of this title, or of any rule or regulation issued under this title, shall be—

“(1) deemed to be in violation of such provision; and

“(2) liable to the same extent as the person to whom such assistance is provided.”.

SEC. 109. LOSS CAUSATION.

Section 12 of the Securities Act of 1933 (15 U.S.C. 77l) is amended—

(1) by inserting “(a) IN GENERAL.—” before “Any person”;

(2) by inserting “, subject to subsection (b),” after “shall be liable”; and

(3) by adding at the end the following:

“(b) LOSS CAUSATION.—In an action described in subsection (a)(2), the liability of the person who offers or sells such security shall be limited to damages if that person proves that any portion or all of the amount recoverable under subsection (a)(2) represents other than the depreciation in value of the subject security resulting from such part of the prospectus or oral communication, with respect to which the liability of that person is asserted, not being true or omitting to state a material fact required to be stated therein or necessary to make the statement not misleading, and such portion or all of such amount shall not be recoverable.”.

SEC. 110. APPLICABILITY.

The amendments made by this title shall not affect or apply to any private action arising under title I of the Securities Exchange Act of 1934 or title I of the Securities Act of 1933 commenced before the date of enactment of this Act.

TITLE II—REDUCTION OF COERCIVE SETTLEMENTS

SEC. 201. LIMITATION ON DAMAGES.

Section 36 of the Securities Exchange Act of 1934, as added by section 104 of this Act, is amended by adding at the end the following new subsection:

“(e) LIMITATION ON DAMAGES.—

“(1) IN GENERAL.—Except as provided in paragraph (2), in any private action arising under this title, the plaintiff's damages shall not exceed the difference between the purchase or sale price paid or received, as appropriate, by the plaintiff for the subject security and the value of that security, as measured by the median trading price of that security, during the 90-day period beginning on the date on which the information correcting the misstatement or omission is disseminated to the market.

“(2) EXCEPTION.—In any private action arising under this title in which damages are sought, if the plaintiff sells or repurchases the subject security prior to the expiration of the 90-day period described in paragraph (1), the plaintiff's damages shall not exceed the difference between the purchase or sale price paid or received, as appropriate, by the plaintiff for the security and the median market value of the security during the period beginning immediately after dissemination of information correcting the misstatement or omission and ending on the date on which the plaintiff sells or repurchases the security.”.

SEC. 202. PROPORTIONATE LIABILITY.

Title I of the Securities and Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended by adding at the end the following new section:

“SEC. 38. PROPORTIONATE LIABILITY.

“(a) APPLICABILITY.—This section shall apply only to the allocation of damages among persons who are, or who may become, liable for damages in any private action arising under this title. Nothing in this section shall affect the standards for liability associated with any private action arising under this title.

“(b) LIABILITY FOR DAMAGES.—

“(1) JOINT AND SEVERAL LIABILITY.—A person against whom a judgment is entered in any private action arising under this title shall be liable for damages jointly and severally only if the trier of fact specifically determines that such person committed knowing securities fraud.

“(2) PROPORTIONATE LIABILITY.—Except as provided in paragraph (1), a person against

whom a judgment is entered in any private action arising under this title shall be liable solely for the portion of the judgment that corresponds to that person's degree of responsibility, as determined under subsection (c).

“(3) KNOWING SECURITIES FRAUD.—For purposes of this section—

“(A) a defendant engages in ‘knowing securities fraud’ if that defendant—

“(i) makes a material representation with actual knowledge that the representation is false, or omits to make a statement with actual knowledge that, as a result of the omission, one of the material representations of the defendant is false; and

“(ii) actually knows that persons are likely to rely on that misrepresentation or omission; and

“(B) reckless conduct by the defendant shall not be construed to constitute knowing securities fraud.

“(c) DETERMINATION OF RESPONSIBILITY.—

“(1) IN GENERAL.—In any private action arising under this title in which more than 1 person is alleged to have violated a provision of this title, the court shall instruct the jury to answer special interrogatories, or if there is no jury, shall make findings, concerning—

“(A) the percentage of responsibility of each of the defendants and of each of the other persons alleged by any of the parties to have caused or contributed to the violation, including persons who have entered into settlements with the plaintiff or plaintiffs, measured as a percentage of the total fault of all persons who caused or contributed to the violation; and

“(B) whether such defendant committed knowing securities fraud.

“(2) CONTENTS OF SPECIAL INTERROGATORIES OR FINDINGS.—The responses to interrogatories, or findings, as appropriate, under paragraph (1) shall specify the total amount of damages that the plaintiff is entitled to recover and the percentage of responsibility of each person found to have caused or contributed to the damages sustained by the plaintiff or plaintiffs.

“(3) FACTORS FOR CONSIDERATION.—In determining the percentage of responsibility under this subsection, the trier of fact shall consider—

“(A) the nature of the conduct of each person; and

“(B) the nature and extent of the causal relationship between that conduct and the damages incurred by the plaintiff or plaintiffs.

“(d) UNCOLLECTIBLE SHARE.—

“(1) IN GENERAL.—Notwithstanding subsection (b)(2), in any private action arising under this title, if, upon motion made not later than 6 months after a final judgment is entered, the court determines that all or part of a defendant's share of the judgment is not collectible against that defendant or against a defendant described in subsection (b)(1), each defendant described in subsection (b)(2) shall be liable for the uncollectible share as follows:

“(A) PERCENTAGE OF NET WORTH.—Each defendant shall be jointly and severally liable for the uncollectible share if the plaintiff establishes that—

“(i) the plaintiff is an individual whose recoverable damages under the final judgment are equal to more than 10 percent of the net financial worth of the plaintiff; and

“(ii) the net financial worth of the plaintiff is equal to less than \$200,000.

“(B) OTHER PLAINTIFFS.—With respect to any plaintiff not described in subparagraph (A), each defendant shall be liable for the uncollectible share in proportion to the percentage of responsibility of that defendant, except that the total liability under this subparagraph may not exceed 50 percent of the proportionate share of that defendant, as determined under subsection (c)(2).

“(2) OVERALL LIMIT.—In no case shall the total payments required pursuant to paragraph (1) exceed the amount of the uncollectible share.

“(3) DEFENDANTS SUBJECT TO CONTRIBUTION.—A defendant against whom judgment is not col-

lectible shall be subject to contribution and to any continuing liability to the plaintiff on the judgment.

“(e) RIGHT OF CONTRIBUTION.—To the extent that a defendant is required to make an additional payment pursuant to subsection (d), that defendant may recover contribution—

“(1) from the defendant originally liable to make the payment;

“(2) from any defendant liable jointly and severally pursuant to subsection (b)(1);

“(3) from any defendant held proportionately liable pursuant to this subsection who is liable to make the same payment and has paid less than his or her proportionate share of that payment; or

“(4) from any other person responsible for the conduct giving rise to the payment that would have been liable to make the same payment.

“(f) NONDISCLOSURE TO JURY.—The standard for allocation of damages under subsections (b) and (c) and the procedure for reallocation of uncollectible shares under subsection (d) shall not be disclosed to members of the jury.

“(g) SETTLEMENT DISCHARGE.—

“(1) IN GENERAL.—A defendant who settles any private action arising under this title at any time before final verdict or judgment shall be discharged from all claims for contribution brought by other persons. Upon entry of the settlement by the court, the court shall enter a bar order constituting the final discharge of all obligations to the plaintiff of the settling defendant arising out of the action. The order shall bar all future claims for contribution arising out of the action—

“(A) by any person against the settling defendant; and

“(B) by the settling defendant against any person, other than a person whose liability has been extinguished by the settlement of the settling defendant.

“(2) REDUCTION.—If a person enters into a settlement with the plaintiff prior to final verdict or judgment, the verdict or judgment shall be reduced by the greater of—

“(A) an amount that corresponds to the percentage of responsibility of that person; or

“(B) the amount paid to the plaintiff by that person.

“(h) CONTRIBUTION.—A person who becomes liable for damages in any private action arising under this title may recover contribution from any other person who, if joined in the original action, would have been liable for the same damages. A claim for contribution shall be determined based on the percentage of responsibility of the claimant and of each person against whom a claim for contribution is made.

“(i) STATUTE OF LIMITATIONS FOR CONTRIBUTION.—Once judgment has been entered in any private action arising under this title determining liability, an action for contribution shall be brought not later than 6 months after the entry of a final, nonappealable judgment in the action, except that an action for contribution brought by a defendant who was required to make an additional payment pursuant to subsection (d) may be brought not later than 6 months after the date on which such payment was made.”.

SEC. 203. APPLICABILITY.

The amendments made by this title shall not affect or apply to any private action arising under title I of the Securities Exchange Act of 1934 commenced before the date of enactment of this Act.

TITLE III—AUDITOR DISCLOSURE OF CORPORATE FRAUD

SEC. 301. FRAUD DETECTION AND DISCLOSURE.

(a) IN GENERAL.—The Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended by inserting immediately after section 10 the following new section:

“SEC. 10A. AUDIT REQUIREMENTS.

“(a) IN GENERAL.—Each audit required pursuant to this title of the financial statements of an

issuer by an independent public accountant shall include, in accordance with generally accepted auditing standards, as may be modified or supplemented from time to time by the Commission—

“(1) procedures designed to provide reasonable assurance of detecting illegal acts that would have a direct and material effect on the determination of financial statement amounts;

“(2) procedures designed to identify related party transactions that are material to the financial statements or otherwise require disclosure therein; and

“(3) an evaluation of whether there is substantial doubt about the ability of the issuer to continue as a going concern during the ensuing fiscal year.

“(b) REQUIRED RESPONSE TO AUDIT DISCOVERIES.—

“(1) INVESTIGATION AND REPORT TO MANAGEMENT.—If, in the course of conducting an audit pursuant to this title to which subsection (a) applies, the independent public accountant detects or otherwise becomes aware of information indicating that an illegal act (whether or not perceived to have a material effect on the financial statements of the issuer) has or may have occurred, the accountant shall, in accordance with generally accepted auditing standards, as may be modified or supplemented from time to time by the Commission—

“(A)(i) determine whether it is likely that an illegal act has occurred; and

“(ii) if so, determine and consider the possible effect of the illegal act on the financial statements of the issuer, including any contingent monetary effects, such as fines, penalties, and damages; and

“(B) as soon as practicable, inform the appropriate level of the management of the issuer and assure that the audit committee of the issuer, or the board of directors of the issuer in the absence of such a committee, is adequately informed with respect to illegal acts that have been detected or have otherwise come to the attention of such accountant in the course of the audit, unless the illegal act is clearly inconsequential.

“(2) RESPONSE TO FAILURE TO TAKE REMEDIAL ACTION.—If, after determining that the audit committee of the board of directors of the issuer, or the board of directors of the issuer in the absence of an audit committee, is adequately informed with respect to illegal acts that have been detected or have otherwise come to the attention of the accountant in the course of the audit of such accountant, the independent public accountant concludes that—

“(A) the illegal act has a material effect on the financial statements of the issuer;

“(B) the senior management has not taken, and the board of directors has not caused senior management to take, timely and appropriate remedial actions with respect to the illegal act; and

“(C) the failure to take remedial action is reasonably expected to warrant departure from a standard report of the auditor, when made, or warrant resignation from the audit engagement; the independent public accountant shall, as soon as practicable, directly report its conclusions to the board of directors.

“(3) NOTICE TO COMMISSION; RESPONSE TO FAILURE TO NOTIFY.—An issuer whose board of directors receives a report under paragraph (2) shall inform the Commission by notice not later than 1 business day after the receipt of such report and shall furnish the independent public accountant making such report with a copy of the notice furnished to the Commission. If the independent public accountant fails to receive a copy of the notice before the expiration of the required 1-business-day period, the independent public accountant shall—

“(A) resign from the engagement; or

“(B) furnish to the Commission a copy of its report (or the documentation of any oral report

given) not later than 1 business day following such failure to receive notice.

“(4) REPORT AFTER RESIGNATION.—If an independent public accountant resigns from an engagement under paragraph (3)(A), the accountant shall, not later than 1 business day following the failure by the issuer to notify the Commission under paragraph (3), furnish to the Commission a copy of the accountant's report (or the documentation of any oral report given).

“(c) AUDITOR LIABILITY LIMITATION.—No independent public accountant shall be liable in a private action for any finding, conclusion, or statement expressed in a report made pursuant to paragraph (3) or (4) of subsection (b), including any rule promulgated pursuant thereto.

“(d) CIVIL PENALTIES IN CEASE-AND-DESIST PROCEEDINGS.—If the Commission finds, after notice and opportunity for hearing in a proceeding instituted pursuant to section 21C, that an independent public accountant has willfully violated paragraph (3) or (4) of subsection (b), the Commission may, in addition to entering an order under section 21C, impose a civil penalty against the independent public accountant and any other person that the Commission finds was a cause of such violation. The determination to impose a civil penalty and the amount of the penalty shall be governed by the standards set forth in section 21B.

“(e) PRESERVATION OF EXISTING AUTHORITY.—Except as provided in subsection (d), nothing in this section shall be held to limit or otherwise affect the authority of the Commission under this title.

“(f) DEFINITION.—As used in this section, the term ‘illegal act’ means an act or omission that violates any law, or any rule or regulation having the force of law.”

(b) EFFECTIVE DATES.—The amendment made by subsection (a) shall apply to each annual report—

(1) for any period beginning on or after January 1, 1996, with respect to any registrant that is required to file selected quarterly financial data pursuant to the rules or regulations of the Securities and Exchange Commission; and

(2) for any period beginning on or after January 1, 1997, with respect to any other registrant.

The PRESIDING OFFICER. The Senator from New York.

Mr. D'AMATO. Mr. President, S. 240, the Private Securities Litigation Reform Act of 1995, is the bill we take up today. There is no doubt that this bill is considered by some to be rather contentious. But this legislation is important and necessary to fix the problem caused by frivolous lawsuits that are making it difficult for companies to raise the capital needed to fuel our economy.

This bill seeks to strike the right balance, which is always difficult, between protecting the rights of those who are truly aggrieved and yet not opening the door to frivolous litigation. This legislation is necessary as there has developed a small but very effective cadre of lawyers who bring suits not to help recover losses for those who are truly aggrieved but because they see an opportunity to strike it rich for themselves.

There is a term for this kind of lawsuit, they are called “strike suits.” A strike suit occurs when a lawyer searches very carefully for negative news announcements by a company or a decline in a company stock price. Then these lawyers race to the courthouse to file a suit alleging securities frauds, alleging mismanagement, or

misinformation. I look to my colleagues on the floor from Alaska for an analogy—there is gold in the hills if a firm offers a security. There are lawyers who are mining that gold for themselves. Sometimes, even if a stock price goes up, lawyers will race to bring suits because they allege that they were not given information that this company would have higher earnings than anticipated. Imagine. If there is bad news, you are vulnerable. If there is good news, you are vulnerable.

Mr. President, the purpose of the courts and the American judicial system is not to make these lawyers rich. It is to legitimately protect those who have been aggrieved; those who have been taken advantage of, who have suffered due to fraud, or who have suffered due to the deliberate withholding of information or insider trading.

The question is not should these suits be stopped. The contentious nature of this legislation comes from the question of how to protect the rights of our citizens and the integrity of the capital markets to assure there is not insider trading, taking advantage of information, withholding information, or misrepresenting facts to steal people's money, and at the same time protect companies from strike suits.

Let me first commend my distinguished colleagues, Senators DOMENICI and DODD, for their tireless work in spearheading the effort to reform securities litigation. I also want to thank Senator GRAMM for his leadership on this issue as chairman of the Securities Subcommittee.

Over the past 2 years, the Banking Committee has heard substantial testimony that certain lawyers file frivolous strike suits alleging violations of Federal securities laws in hopes that defendants will quickly settle. These suits, which unnecessarily interfere with, and increase the cost of, raising capital, are often based on nothing more than a company's announcement of bad news, not evidence of fraud. In addition, the fact that many of these lawsuits are brought as class actions has produced an in terrorem effect on corporate America.

S. 240 provides a strong disincentive for filing abusive lawsuits. It hits strike suit artists where it hurts—in the pocketbook. S. 240 does not contain a loser-pays provision. That would go too far. A loser-pays provision makes it difficult, if not impossible, for injured investors to maintain a legitimate cause of action.

Instead, the bill requires courts to make specific findings about whether an attorney violated rule 11 and to sanction attorneys who do.

One study showed that, in the early 1980's every company in one part of the business sector that had a market loss of \$20 million or more in its capitalization was sued. Another survey of venture-backed companies in existence for less than 10 years—small companies that are the engine of economic growth—showed that one in six of

those companies had been sued at least once.

These lawsuits are expensive. The statistics show that although many suits are still pending, these suits have consumed on average over 1,000 hours of management time and legal cost—per case—of over \$690,000 that the company has had to pay out. That is a lot of time and that is a lot of money.

Does Congress want to let this trend continue? This Senator cannot sit idly by and permit small businesses to be the target of abusive lawsuits. Most of these companies are startup or high-technology businesses, which play an important role in our economy. These businesses provide new, innovative products to consumers, improving the quality of life and the way we conduct business.

Small startup, high-technology firms depend on research and development for their new products. As products succeed, fail, or sometimes just take longer to develop, the stock price of these companies may fluctuate. This stock price fluctuation or product development slowdown is not, on its face, evidence of fraud. Yet, in many States, alleging that a product did not succeed and the price of the company's stock dropped is enough to sustain a complaint in a securities fraud lawsuit.

S. 240 creates a uniform pleading standard that will help to weed out frivolous complaints before companies must pay heavy legal bills. S. 240, codifies the pleading standard of the second circuit in New York, which requires that a plaintiff plead facts giving rise to a strong inference of the defendant's fraudulent intent.

Small, startup, and high-technology companies have become sitting ducks for securities fraud lawsuits. The costs of defending a securities fraud complaint, which does not have to show any evidence of fraud, is enormous. According to the American Electronics Association, who testified at one of the committee's hearings, of the 300 or so lawsuits filed every year, almost 93 percent settle at an average settlement cost of \$8.6 million.

Furthermore, it is not just the company that is sued. Other, peripheral, deep-pocket defendants are joined to ensure there is enough money available to produce a meaningful recovery. As a result, underwriters, lawyers, accountants, and other professionals have become prime targets of securities fraud lawsuits. Insurance companies that provide director and officer liability insurance also pay up in these settlements. In 1994 alone, insurers and companies paid out \$1.4 billion to settle securities fraud lawsuits.

Mr. President, this is not to say that some of those suits may not have been bona fide. But all too often companies are paying simply to stop the litigation because they cannot afford the legal bills or they cannot afford the incredible negative exposure that a case can bring, especially under the system of joint and several liability.

S. 240 modifies the doctrine of joint and several liability for peripheral defendants, who are named in the lawsuit more for their deep pockets than their culpability.

In the current system, if you have any connection to the defendant companies, if they can tie you in at all, you can be held liable for the full amount of the judgment. Even that defendant who has only a scintilla of liability for wrongdoing, or culpability or negligence—not gross negligence, not knowing or wanton misconduct, not fraud—has a chance of being held 100 percent liable for damages. That is just not fair. That is wrong.

Who benefits from these settlements? Not the plaintiffs. According to the statistics, the victims of these so-called frauds generally get pennies on the dollar. They are just being used.

Not only is this unfair, but often the investors do not understand exactly what the settlement represents, what their portion of the settlement is, or why the lawyers even recommended the settlement.

S. 240 requires that certain information be provided to class members and that counsel be available to answer questions about the settlement.

No longer will attorneys be able to make a settlement for \$6 million, \$7 million, and not properly inform the people in the class. Nor will the attorneys be able to pocket most of the settlement while class members receive pennies for their losses.

As one witness told the committee, and I quote:

As a stockholder, I feel that lawyers use the stockholders as a steppingstone, preying on their misfortune, as a means to file a lawsuit that will inevitably settle, in which the lawyers will reap millions in fees while their clients recover pennies on the dollar in their losses.

S. 240 limits the award of the attorney's fees to a "reasonable" percentage of the damages awarded to investors. Notably, it is the investors who end up paying the costs of these lawsuits.

Institutional investors, with about \$9.5 trillion in assets, approximately \$4.5 trillion of which are pension funds, are long-term investors. This means that the value of retirees' pension fund investments are adversely affected by abusive litigation. As the Council for Institutional Investors advised the committee, and I quote:

We are . . . hurt if the system allows someone to force us to spend huge sums of money in legal costs by merely paying ten dollars and filing a meritless cookie cutter complaint against a company or its accountants.

Abusive litigation also severely impacts the willingness of corporate managers to disclose information to the marketplace. Many companies refuse to talk or write about future business plans, knowing that projections that do not materialize will inevitably lead to lawsuits, many of which will simply allege that a prediction did not come true. Once discovery begins, plaintiff's counsel begins what we call a fishing

expedition for evidence. And as one witness told the committee, the overbroad discovery request in this typical case ended up with the company producing over 1,500 boxes of documents at an expense of \$1.4 million. Companies cannot continue to spend the time and the money that these cases cost. So many times they are forced to settle meritless cases.

As a result, investors do not have the benefit of knowing about the future plans of a company because companies are afraid to make that information available. As a former SEC Chairman told the committee, and I quote:

Shareholders are also damaged due to the chilling effect of the current system on the robustness and candor of disclosure. Understanding a company's own assessment of its future potential would be amongst the most valuable information shareholders and potential investors could have.

S. 240 will encourage companies to make what we call forward-looking statements by reducing the threat of abusive litigation. Companies that make projections and that provide a clear warning to investors that the projections may not be accurate will be protected from costly litigation.

Some have said that this safe harbor for forward looking statements would give license for companies to say anything. That it will give license to the quick buck artist, the penny stock guys, the people who come out with IPO's. This is not true. We have excluded newly started companies which have not established a track record from this protection. Only recognized companies with substantial interests will get this protection. Most importantly, if a defendant knowingly makes a false or misleading forecast, they are not protected.

The statement that this legislation will allow companies to knowingly lie and get away with it—and that statement has been made—is just not true. If you knowingly lie, if you intentionally mislead, you can be held liable. There is no safe harbor for initial public offerings, for blank check offerings, for rollups, for penny stocks, for tender offers and leveraged buyouts. Safe harbor does not affect the power to bring an enforcement case.

Now, exactly who are the victims of securities fraud? Many times, there is no victim. Instead there is just a professional plaintiff whose name appears in the lawsuits, these names appear time after time after time. In one case, a retired lawyer appeared as the lead plaintiff in 300 lawsuits, he bought small numbers of shares in many companies and then served when they were sued. Last year, an Ohio judge refused to permit class action certification, noting that the lead defendant had filed 182 class action suits in 12 years.

Now, that is not what the private right of action is intended to do.

S. 240 discourages the use of professional plaintiffs by eliminating the bonus payments to plaintiffs and prohibiting referral fees. In other words, if

you are one of these people who bought 10 shares in 700, 800, or 900 companies you can no longer receive a bonus when a lawyer uses your name for a suit.

The practice of using professional plaintiffs permits the lawyers to hire the client. Professional plaintiffs also permit the lawyer to win the "race to the courthouse" in filing a complaint. Often whoever files a claim first becomes the lead plaintiff, the lead counsel, even when multiple complaints are filed against the companies alleging securities fraud.

Because the huge settlements in these cases provide significant fees to counsel, the competition is fierce. This bill creates a new procedure to ensure that the plaintiffs who are legitimately damaged, who have a real stake, who are not these professional plaintiffs, who own 1 share or 10 shares in multiple companies, can control the suit. This bill says the institutional investors, the people who have billions in pension funds, the retirees, those managers will have a greater stake in the case.

Can you imagine empowering somebody who owns 10 shares to represent you when you represent 500 million. Someone who has a half billion dollars invested could have no say in who the attorney will be, or what the eventual settlement will be while the case is managed by someone who has only 10 shares.

Mr. DOMENICI. Will the Senator yield for some observations?

Mr. D'AMATO. Certainly.

Mr. DOMENICI. The Senator said it would be managed by shareholders with 10 shares.

Mr. D'AMATO. That is what is taking place now.

Mr. DOMENICI. Actually, it is even worse than that because it is managed by the lawyer of the shareholder of 10 shares.

Mr. D'AMATO. Correct. Because in many cases the shareholder receives a bonus from the lawyer but is not otherwise involved in the case.

Mr. DOMENICI. The lawyer calls himself an entrepreneurial lawyer in this case. He is in business. It is not the shareholder; it is the lawyer who is in the business of managing the lawsuit. In fact, I will quote some courts that have found that to be the case.

Mr. D'AMATO. That is correct. I thank the Senator for bringing this point to the floor. Again I would like to commend Senator DOMENICI and Senator DODD who have labored for years to craft a bill that is fair, that is balanced, that protects those investors, the small investors, the pension people, who have invested their life savings and also protects businesses who raise the capital that keeps our communities healthy, from lawyers who go after deep pocket firms and file suits against people just because their projections did not come true. This bill will curb private securities fraud lawsuits, but only the frivolous ones that result from abusive practices. Victims of se-

curities fraud will not be left without remedy. The time for reform of this system is now. This bill has 51 cosponsors and I urge all of my colleagues to support this legislation. It is well crafted. It is contentious only because it tries to strike a balance. Whenever you try to find a middle ground there are people on either side who think you should go further in their direction. No one can doubt that the system is out of control and it needs fixing; that is what we attempt to do with this legislation.

Mr. President, I yield the floor.

Mr. DOMENICI. Senator DODD, why do you not proceed and I will follow you, if it is all right?

Mr. DODD. Let me inquire, Mr. President, of my colleague from Maryland, does my colleague from Maryland, the ranking member of the banking committee if he wishes to proceed first. I am obviously interested in the bill, but I also appreciate immensely the seniority system.

Mr. SARBANES. We are quite happy to hear the three proponents of the bill who are on the floor now. We heard from Senator D'AMATO, and we would be happy to hear from the Senator from Connecticut and Senator DOMENICI. And then those of us who oppose it might have a chance to make our statements. But I would be happy to defer to the Senator from Connecticut. Then we can address his comments.

Mr. DODD. I thank my colleague from Maryland.

Mr. President, let me begin by thanking my colleague from New Mexico. I worked with him for a long time on this issue, Mr. President. We go back several years. This is not a recent event but rather goes back into the previous Congress and before, so I thank him for his tremendous efforts in helping us fashion a piece of legislation here that we hope will attract the support of a substantial number of our colleagues. It has already, as my colleague from New York pointed out—and I thank my colleague from New York, the chairman of the Banking Committee, for his leadership on this issue for setting up a set of hearings for us, timely hearings, and a markup of this legislation and bringing the bill to the floor.

I also want to commend my colleague from Maryland who has a different point of view on this legislation but nonetheless is working cooperatively with us, expressing his points of view very forcefully and offered various amendments in the committee, and I am confident he will again on the floor.

Mr. President, this is an important day for American investors and for the American economy. This is the day we start a full Senate debate on a bill that would restore, in my view, fairness and integrity to our securities litigation system.

To some this may sound like a dry and technical subject. But in reality it is crucial to our investors, our economy and our international competi-

tiveness. We are all counting on our high-technology firms to fuel our economy into the 21st century. We are counting on them to lead the charge for us in the global marketplace, so to speak. Those are the same firms that are most hamstrung, I would point out, by a securities litigation system that, frankly, works for no one, save plaintiffs' attorneys.

Over the past year-and-a-half the process by which private individuals bring securities lawsuits has been under the microscope. The result of this intense scrutiny has been to dramatically change the terms of the debate. We are no longer arguing about whether the current system needs to be repaired. We are now focused on how best to repair it. Even those who once maintained that the litigation system needed no reform are now conceding that substantive and meaningful changes are required if we are to maintain the fundamental integrity of private securities litigation.

The flaws, Mr. President, of the current system are simply too obvious to deny. The record is replete with examples of how the system is being abused, and misused. In fact, the Chairman of the Securities and Exchange Commission, Arthur Levitt, said at the beginning of this year—and I quote him—"There is no denying," he said, "that there are real problems in the current system,"—speaking of securities litigation—"problems that need to be addressed not just because of abstract rights and responsibilities, but because investors and markets are being hurt by litigation excesses."

The legislation under consideration today is based upon a bill that the distinguished Senator from New Mexico and I have introduced for the last several Congresses. While there are some provisions from the original version of S. 240 that, frankly, I would have liked to have seen included in this bill—and we will discuss that later—I understand, as I think my colleagues do, the need to produce a consensus document if you are going to proceed. Producing a balanced bill is never easy. The old saw, Mr. President, that "if a compromise makes everyone somewhat angry, then it must be fair" is perfectly apt for today's debate. But that is what we have today, Mr. President, a bill that carefully and considerably balances the need for our high-growth industries with the legitimate rights of investors, large and small.

I am proud of the spirit of fairness and equity that permeates this legislation. I am also proud, Mr. President, of the fact that this legislation tackles a very complicated and difficult issue in a thoughtful way that avoids excess and achieves, I believe, and I think my colleagues from New York and New Mexico do, a meaningful equilibrium under which all of the interested parties can survive and thrive.

Moreover, Mr. President, perhaps most importantly, this is a broadly bipartisan effort. This bill passed the

Banking Committee 11-4, with strong support from both sides of the political aisles. And the 51 cosponsors of S. 240 in this body are composed of U.S. Senators from both parties, reflecting all points on the so-called ideological spectrum. H.L. Mencken once said, every problem has a solution that is neat, simple, and usually wrong. Believe me, if there were a simple solution to the problem besetting securities litigation today almost everyone in this Chamber would have jumped at it. But those problems are so pervasive and complex that we have moved far beyond the point where the public interest is served by waiting for the courts or other bodies to fix them for us.

The private securities litigation system is far too important to the integrity and vitality of American capital markets to continue to allow it to be undermined by those who seek to line their own pockets with abusive and meritless suits. Let me be clear, Mr. President, private securities litigation is an indispensable tool with which defrauded investors can recover their losses without having to rely upon Government action.

Mr. President, I cannot possibly overstate just how critical securities lawsuits brought by private individuals are to ensuring public and global confidence in our capital markets. I believe that very deeply. These private actions help deter wrongdoing, help guarantee that corporate officers, auditors and directors, lawyers and others properly perform their jobs. That is the high standard to which this legislation seeks to return the securities litigation system. But as it stands today, the current system has drifted so far from that noble role that we see more buccaneering barristers taking advantage of the system than we do corporate wrongdoers being exposed by it.

But there is more at risk, Mr. President, if we fail to reform this flawed system. Quite simply put, the way the private litigation system works today is costing millions of investors, the vast majority of whom do not participate in these lawsuits, their hard-earned cash. As Ralph Whitworth of the United Shareholders Association told the securities subcommittee—I quote him—“The winners in these suits are invariably lawyers who collect huge contingency fees, professional ‘plaintiffs,’ who”—as our colleague from New York has already described—“collect bonuses, and, in cases where fraud has been committed, executives and board members who use corporate funds and corporate-owned insurance policies to escape personal liability. The one constant,” he went on to say, “is that the shareholders pay for it all.”

And Maryellen Anderson from the Connecticut Retirement and Trust Funds testified that the participants in the pension funds,

*** are the ones who are hurt if a system allows someone to force us to spend huge

sums of money in legal costs * * * when that plaintiff is disappointed in his or her investment.

Our pensions and jobs depend on our employment by and investment in our companies.

If we saddle our companies with big and unproductive costs * * *. We cannot be surprised if our jobs and raises begin to disappear and our pensions come up short as our population ages.

There lies the risk of allowing the current securities litigation system to continue to run out of control. Ultimately, it is the average investor, the retired pensioner who will pay the enormous costs clearly associated with this growing problem.

Much of the problem lies in the fact that private litigation has evolved over the years as a result of court decisions rather than explicit congressional action.

Private actions under rule 10(b) were never expressly set out by Congress, but have been construed and refined by courts, with the tacit consent of Congress.

But the lack of congressional involvement in shaping private litigation has created conflicting legal standards and has provided too many opportunities for abuse of investors and companies.

First, it has become increasingly clear that securities class actions are extremely vulnerable to abuses by entrepreneurs masquerading as lawyers. As two noted legal scholars recently wrote in the Yale Law Review:

*** The potential for opportunism in class actions is so pervasive and evidence that plaintiffs' attorneys sometimes act opportunistically so substantial that it seems clear that plaintiffs' attorneys often do not act as investors' "faithful champions."

It is readily apparent to many observers in business, academia—and even Government—that plaintiffs' attorneys appear to control the settlement of the case with little or no influence from either the “named” plaintiffs or the larger class of investors.

For example, during the extensive hearings on the issue before the Subcommittee on Securities, a lawyer cited one case as a supposed showpiece—using his words—of how well the existing system works. This particular case was settled before trial for \$33 million.

The lawyers asked the court for more than \$20 million of that amount in fees and costs. The court then awarded the plaintiffs' lawyers \$11 million and the defense lawyers for the company \$3 million.

Investors recovered only 6.5 percent of their recoverable damages. That is 6½ cents on the dollar.

That is a case cited by those who are opposed to this legislation as a showcase example of how the system works.

This kind of settlement sounds good for entrepreneurial attorneys, but it does little to benefit companies, investors or even the plaintiffs on whose behalf the suit was brought.

It should not surprise anyone that those who benefit most from the flaws in the current system are the same people who are the most vociferous in opposing the provisions in this bill that would clean up the mess.

It is not the companies, nor investors nor even plaintiffs—large or small—who are fueling the opposition.

The loudest squeals come from the lawyers who will no longer be able to feather their nests by picking clean as many corporate defendants as possible.

A second area of abuse is frivolous litigation. Companies, particularly in the high-technology and biotechnology industries, face groundless securities litigation days or even hours after adverse earnings announcements.

In fact, the chilling consequence of these lawsuits is that companies, especially new companies in emerging industries, frequently release only the minimum information required by law so that they will not be held liable for any innocent, forward-looking statement that they may make.

In fact, I received a letter just this past Monday from Raytheon Co., one of the Nation's largest high-technology firms.

Raytheon made a tender offer of \$64 a share for E-Systems, Inc., a 41-percent premium over the closing market price. Let me allow Raytheon to explain what happened next:

Notwithstanding the widely held view that the proposed transaction was eminently fair to E-Systems shareholders, the first of eight purported class action suits was filed less than 90 minutes after the courthouse doors opened on the day that the transaction was announced. Ninety minutes, Mr. President. This was a letter sent to me on June 19.

You tell me we do not have a problem here. Minutes after announcement, the lawsuits, before any examination, any inquiry is made, 90 minutes later there is a lawsuit being filed for millions of dollars claiming unfairness. That is what is wrong, and that is what this bill tries to correct. This ought not to be a matter of division in this body. This is a mess, and it should be cleaned up.

No one lawyer could possibly have investigated the facts this quickly. What the lawyers want is to force a quick settlement. That is all this is. This is a holdup. You would get arrested in most States if you try to do this to a retailer.

The Supreme Court in *Blue Chip Stamps versus Manor Drug Store* echoed this concern about abusive litigation, pointing out:

[I]n the field of Federal securities laws governing disclosure of information, even a complaint which by objective standards may have very little success at trial has a settlement value to the plaintiff out of any proportion to its prospect of success at trial . . . the very pendency of the lawsuit may frustrate or delay normal business activity of the defendant which is totally unrelated to the lawsuit.

The third area of abuse is that the current framework for assessing liability is simply unfair and creates a powerful incentive to sue those with the

deepest pockets, regardless of their relative complicity in the alleged fraud.

The result of the existing system of joint and severable liability is that plaintiffs' attorneys seek out any possible corporation or individual that has little relation to the alleged fraud—but which may have extensive insurance coverage or otherwise may have financial reserves.

Although these defendants could frequently win their case were it to go to trial—we all know it happens—the expense of protracted litigation and the threat of being forced to pay all the damages makes it more economically efficient for them to settle with the plaintiffs' attorneys, and that is what happens.

The current Chairman of the SEC, Arthur Levitt, as well as two former Chairmen, Richard Breeden and David Ruder, have all spoken out against the abuses of joint and several liability.

Chairman Levitt said at the April 6 hearing of the Securities subcommittee that he was concerned, in particular, "about accountants being unfairly charged for amounts that go far beyond their involvement in particular fraud."

Frequently, these settlements do not appreciably increase the amount of losses recovered by the actual plaintiffs, but instead add to the fees collected by the plaintiff's attorneys.

Again, the current system has devolved to a point where it favors those lawyers who are looking out for their own financial interest over the interest of virtually everybody else involved, and that is the fact.

The bill before us today contains four major initiatives to deal with these complex problems. Let me identify them briefly.

First, the legislation empowers investors so that they, not their lawyers, have greater control over their class action cases by allowing the plaintiff with the greatest claim to be the named plaintiff and allowing that plaintiff to select their counsel.

That sounds so commonsensical, I do not know why we have to write it into law, but that is what you have to do. In fairness to the plaintiff, that ought to be the lead plaintiff.

Second, it gives investors better tools to recover losses and enhances existing provisions designed to deter fraud, including providing a meaningful safe harbor for legitimate forward-looking statements so that issuers are encouraged, instead of discouraged, from volunteering much-needed disclosures that potential investors ought to have in making decisions about whether to invest or not.

Third, it limits opportunities for frivolous or abusive lawsuits and makes it easier to impose sanctions on those lawyers who violate their basic professional ethics.

Fourth, it rationalizes the liability of deep-pocket defendants, while protecting the ability of small investors to fully collect all damages awarded them through a trial or settlement.

I would like to go into each of these provisions in a bit more detail.

EMPOWERING INVESTORS

The legislation ensures that investors, not a few marauding attorneys, decide whether to bring a case, whether to settle, and how much the lawyers should receive, and that is the way it ought to work.

The bill strongly encourages the courts to appoint the investor with the greatest losses—usually an institutional investor like a pension fund—to be the lead plaintiff.

This plaintiff would have the right to select the lawyer to pursue the case on behalf of the class.

So for the first time in a long time, plaintiffs' lawyers would have to answer to a real client, not one they have hired.

We are bringing an end to the days when a plaintiffs' attorney can crow to Forbes magazine that "I have the greatest practice of law in the world. I have no clients."

That is one of the lawyers talking. A practice without clients, and that is what this has turned into.

The bill requires that notice of settlement agreements that are sent to investors clearly spell out important facts such as how much investors are getting—or giving up—by settling and how much their lawyers will receive in the settlement.

This means that plaintiffs would be able to make an informed decision about whether the settlement is in their best interest—or in their lawyers' best interest.

Again, what a radical thought to be included in the bill, allowing the plaintiffs to decide what is in their interest rather than the attorneys deciding it. The fact we even have to write this into law tells you volumes about the mess the present system is in.

And the bill would end the practice of the actual plaintiffs receiving, on average, only 6 to 14 cents for every dollar lost, while 33 cents of every settlement dollar goes to the plaintiffs' attorneys. This is the average you get back as a plaintiff under the present system.

The bill would require that the courts cap the award of lawyers' fees based upon how much is recovered by the investors. And that is what it ought to be, how much do the investors get back as plaintiffs, then you set the fees.

Simply putting in a big bill will not guarantee the lawyers multimillion-dollar fees if their clients are not the primary beneficiaries of the settlement.

Taken together, Mr. President, these provisions should ensure that defrauded investors are not cheated a second time by a few unscrupulous lawyers who siphon huge fees right off the top of any settlement.

The bill requires auditors to detect and report fraud to the SEC, thus enhancing the reliability of independent audits.

The bill maintains current standards of joint and several liability, for those

persons who knowingly engage in a fraudulent scheme, thus keeping a heavy financial penalty for those who would commit knowing security fraud.

The bill restores the ability of the Securities and Exchange Commission to pursue those who aid and abet in securities fraud, a power that was diminished by the Supreme Court in last year's Central Bank decision.

The bill clarifies current requirements that lawyers should have some facts to back up their assertion of securities fraud by adopting the reasonable standards established by the Second Circuit Court of Appeals. Again, Mr. President, imagine that—you have to have facts to back up your assertion. I thought that is what they taught you. I learned that in the first year of law school. Now I have to write it into the legislation here because we get these 90-minute lawsuits being filed. So we require that in the bill as well.

This legislation is there for using a pleading standard that has been successfully tested in the real world. This is not some arbitrary standard pulled out of a hat or crafted in committee; it follows the Federal courts.

The bill requires the courts, at settlement, to determine whether any attorney violated rule 11 of the Federal Rules of Civil Procedure, which prohibits lawyers from filing claims that they know to be frivolous.

If a violation has occurred, the bill mandates that the court must levy sanctions against the offending attorney. Though the bill does not change existing standards of conduct, it does put some teeth into the enforcement of these standards.

The bill provides a moderate and, I think, thoughtful statutory safe harbor for predicative statements made by companies that are registered with the SEC.

Further, the bill provides no such safety for third parties, like brokers, or in the case of merger offers, tenders, roll-ups, or the issuance of penny stocks. There are a number of other exceptions to the safe harbor provisions, as well, Mr. President, which my colleagues can look at.

Importantly, anyone who deliberately makes a false and misleading statement in a forecast is not protected by the safe harbor. My colleague from New York made that point, and I emphasize it again here this afternoon.

By adopting this provision, the Senate will encourage, we think, responsible corporations to make the kind of disclosures about projected activities that are currently missing in today's investment climate.

This legislation preserves the rights and claims of small investors. The legislation preserves the rights of investors whose losses are 10 percent or more of their total net worth of \$200,000.

These small investors will still be able to hold all defendants responsible for paying off settlements, regardless of the relative guilt of each of the named parties.

But while the bill will fully protect small investors, so that they will recover all of the losses to which they are entitled, the bill establishes a proportional liability system to discourage the naming of deep-pocket defendants, merely because they have deep pockets.

The court would be required to determine the relative liability of all the defendants and thus deep-pocket defendants would only be liable to pay a settlement amount equal to their relative role in the alleged fraud.

A defendant who was only a 10 percent responsible for the fraudulent actions would be required to pay 10 percent of the settlement amount.

In some circumstances, the bill requires solvent defendants to pay 150 percent of their share of the damages to help make up for any uncollectible amount in the lawsuit.

By creating a two-tiered system of both proportional liability and joint and several liability, the bill preserves the best features, I think, of both systems.

There has been an unfortunate tendency during the course of many debates on these proposed reforms for advocates on both sides to increase the rhetoric, to use increasingly extreme examples in order to politicize and polemize the atmosphere of this debate.

When the steam of overheated rhetoric blows off, when the extremists on both sides have been discounted, I believe we are left with the inescapable conclusion: Action is needed—and needed now, Mr. President—to make the securities litigation system work in the manner for which it was designed.

A system of litigation in which merits and facts matter little, in which plaintiffs recover less than lawyers, in which defendants are named solely on the basis of the amount of their insurance coverage, or the size of their wallets, does not serve us well at all.

In short, we have a system in which there is increasingly little integrity and confidence—a system incapable of producing confidence and integrity in our Nation's capital markets.

This bill is an important step in repairing an ailing system. It is a bill that has strong bipartisan support within this Chamber. And it has broad support outside these walls, as well, from virtually every segment of the business and investment community.

Mr. President, this legislation needs to be enacted and I urge my colleagues to support it.

Mr. President, I noted that our colleague from New Mexico was on the floor. I do not know whether or not he is still here. I see him now.

I yield the floor, and we will now hear from the Senator from New Mexico.

The PRESIDING OFFICER (Mr. INHOFE). The Senator from New Mexico is recognized.

Mr. DOMENICI. Mr. President, might I first say that when I first started

working on this legislation—actually, it came to me after reading some articles about the litigation and the contention of both sides as to what was happening to class action lawsuits as they applied to securities and to companies that issued stocks and securities and bonds—I came to a conclusion that it would be a very interesting thing to look into and, perhaps, see what I could do.

I made one glaring mistake. I had arrived at the conclusion that there was something very, very wrong, but I failed to understand, I say to my friend and cosponsor—and we varied. I put it in one time and the Senator put it in the next time. It was Domenici-Dodd and then Dodd-Domenici. But I failed to recognize how those lawyers, small in number, for this is not the whole of America, this is a small group. I failed to recognize or perceive how tough they were going to be in saving their domain—and tough they are, and tough they are to this day. They are getting people to run advertisements in our States—in my State, it is not so easy because Representative RICHARDSON, a Democrat, voted for the House reform; I am for it here, and all the Representatives from New Mexico voted for it. I do not know where Senator BINGAMAN is, but he was a cosponsor. Maybe he does not like the bill on the floor. So I am not talking for myself on these ads. Can you imagine what point we have reached, in terms of lawyering, and the old concept of who the lawyers work for? Who do they belong to? They belong to the justice system and they work for the courts of America. Here they are running ads and protecting their domain. It is rather amazing. I never thought we were going to get into this when we started down this path, but I soon found out.

I want to say that, while this cries out for reform, apparently our judges are not going to make the reform, although they created the rules; these are court-created private rights of action, as I understand it. Section 10b private lawsuits are not statutory. Judges created it. They are not going to fix it. Although, there seems to be a tendency, in the last 6 months, for the judges to be a little more through this process. Senator DODD explained that somewhere they caught them red-handed. Ninety minutes after an announcement of a merger intention, they are suing for collusion or fraud and just claiming huge damages. The courts are beginning to say, "What is this?"

But I began to find out, when we started having our first hearings, that we were talking about some very, very rich lawyers—not rich over 40 years of practice or an accumulation of assets, but because they made millions every year—not a few hundred thousand dollars, but millions. And surely it would be tough for them to ever appreciate that maybe they were not adding very much of a positive nature to the United States society, or to securities or bonds or stocks, or to the plaintiffs that they sued for as a class.

Now, our country is suffering from hyperlexia. That is a nice word, and I believe it means a serious disease caused by an excessive reliance on law and lawyers. Hyperlexia. It is a disease—and a disease it is. For those who think that hyperlexia, relying upon law and lawyers, is the basic ingredient for good regulation, for good behavior, you have just told the American people that it is going to cost you an awful lot of money for that, because it is inconclusive, and very vague. Each case sets its own pattern. So people do not know how to behave and what the law is.

So from this Senator's standpoint, I do not think we would be here if it were not for the chairman of the Banking Committee, the distinguished Senator from New York, Senator D'AMATO, who took this cause on and, obviously, is leading it here on the floor today. He brought a balance to it, because he had a feel for both sides. I thank him tonight because we are going to make some good, solid law. When it is interpreted by our courts and by the bar of America, we are going to end up doing right, because those who are cheating and ripping off stockholders—they are going to still get stuck, but those doing almost nothing wrong, except their company's stock price goes up or down, they are no longer going to get stuck for millions in settlements just to pay to the lawyers.

So, from this Senator's standpoint, I do not usually use words like vexatious or vexatiousness, but I found that the Supreme Court described this confusing system, "presents a danger of vexatiousness, different in degree and kind from that which accompanies litigation in general." I believe my good friend Senator DODD alluded to that; that is, there is a degree and a kind of vexatiousness about this that is much different from a normal complaint in a lawsuit in negligence or other Common Law torts.

So let me define the word. I tried to find out what does the word mean, because to me it meant to bring fear or such. It comes from a verb, to vex, which means, "to harass, to torment, to annoy, to irritate and to worry." And, as a noun it is synonymous with "troublesome." In the legal context it means "a case without sufficient grounds brought in order to cause annoyance to the defendant or a proceeding instituted maliciously and without probable cause."

It is time that we stop vexatious securities litigation, and fix it we will. During our hearings—and I am no longer on the Banking Committee, and I will help the chairman out wherever I can for the next couple of days as we attempt to pass this legislation, but obviously the responsibility and the credit is to the Banking Committee and those who are working on it now.

During the hearings, we found that the threat of a huge jury award is being misused to sue emerging, rapidly

growing companies, especially in the high-technology and biomedical technologies where stock prices are volatile under the best of circumstances. A drop in a stock price is all that these—and I will call them, for the remainder of my discussion on the floor, I will name those lawyers involved in this as a new kind of lawyer. I will call them entrepreneurial lawyers, because they are in it to manage the suit, and in a very real sense the lawsuit becomes their business rather than the business of the plaintiff. The way it is currently structured, they do not even have to respond to anyone.

Let me proceed.

Cases settle regardless of merit. We could go on with many, many reasons for this litigation not serving the public good. But let me wrap up with just one on this first part of my comments. This system is not deterring fraud because insurance companies, most of the time, make the settlements and pay the money. So what we have and what is wrong with this system is very, very fundamental. Lawyers, not clients, control these cases. That is number one.

Number two, this system obstructs voluntary disclosure of information. Who will voluntarily disclose information when they are apt to be liable for just doing that?

And the last is defendants are forced to settle meritless cases. When you add that up, it is time to change the system.

The Wall Street Journal labeled these cases as "the class action shake-down racket." That is what it is, a shakedown racket.

Let me talk about who wins when one of these lawsuits is settled, for this is the most significant part of it all. Investors are only recovering about 7 cents on the dollar when compared with the amount of losses alleged. The lawyers earned on average \$2.12 million per settlement, about 30 percent of the whole, during a 12-month period ending July of 1993 according to a study by the National Economic Research Association.

Other studies confirm that investors recover only 6 to 14 cents under the system. Obviously, the system is not working, because the SEC and others who have analyzed it say that a system, to be working, is supposed to do the following. The primary yardstick is that it enables defrauded investors to seek compensatory damages and thereby recover the full amount of their losses. So we ought to start by measuring this system against the criterion of full amount of losses recovered. You will find it fails. On a scale of A through F—F being failure. It gets worse than an F in terms of its ineffectiveness.

As investors are recovering a few cents on the dollar, attorneys are boasting that these securities class actions are a perfect practice, according to—I think my friend from Connecticut quoted this one—one of these distin-

guished lawyers, who said in Forbes magazine, "The reason this is a great practice is because there are no clients."

These are clientless lawsuits. These are clientless lawyers who claim to be acting in the best interests of investors. The institutional investors believe that these lawsuits are merely transferring money from one set of shareholders to another with the plaintiffs' class action lawyers taking a lion's share. That looks a lot like greenmail.

Mr. BENNETT. Will the Senator yield for a question?

Mr. DOMENICI. I will be pleased to yield.

Mr. BENNETT. You speak of clientless lawyers and clientless cases. Is that the reason all of the money goes to the lawyers and not to the clients?

Mr. DOMENICI. You got it. As a matter of fact, what it really means is that the lawyers have quickly become more interested in settling a lawsuit on terms that are satisfactory to their pockets. So, if it looks like they can fight on but they are going to get \$6 million in this settlement and the others are going to get 8 cents on their shares, that is looking pretty good.

What prevents it from happening? Maybe the judges are getting more involved now. But, normally, for many and many a year, nobody had anything to say about it. In reality, although if you had a lawyer here, he would tell you that he is bound by this and he is bound by that and the judge can do this and the judge can do that. But history says they are getting the lion's share of the money and the client or plaintiff is not getting very much.

Does one think the client is managing the case and calling the shots? In many cases the members of the class do not even know what is happening. Let me also tell you, plaintiffs are not making very much unless they are very fortunate. If they are professional plaintiffs, they are doing pretty well because they receive bonuses of \$10,000 to \$15,000 for letting the lawyers use their names, and, frankly, we are going to prohibit that. I think that ought to be prohibited and should have been prohibited. It has no place in solid lawyering. What happens is some people have shares in 300 or 400 companies and the lawyers the same person's name on 20, 30, 50 lawsuits. These are individuals with 10 shares and the lawyers give them this bonus. The rest of the class does not make very much, but that fellow does very well. I think we had one, Mr. President, who was 92 or 94 years old that we found out—do you remember that case? He had a lot of these. He had 10 shares of stock and he was a very big friend of these entrepreneurial law firms. He was readily available. He pulled the trigger.

Mr. BENNETT. Will the Senator yield further?

Mr. DOMENICI. I am pleased to.

Mr. BENNETT. It is my understanding that the judge referred to him

in one case as "the unluckiest investor in the world" because he was always suing for losses. He did not invest in order to make any money. He invested so he could be a professional plaintiff, and he was in court so often the judge referred to him in that manner.

Mr. DOMENICI. I was not there when that was done and I do not recall it, but it surely seems right to me. And if you say it, it happened. It is exactly what is happening.

The race to the courthouse has been described by both the chairman of the full committee and by Senator DODD. I will not proceed beyond saying that whenever you find, in the American judicial system, that a substantial portion of a certain kind of lawsuit is based upon the premise that whoever gets to the courthouse first gets to control the lawsuit, then it seems to me you do not have to have that situation very long until you ought to look and see what is this all about? Because it is an invitation to craft poor complaints, to state anything you want or invent things and then waste a year and a half of time, money, and take depositions to try to find out whether you have a lawsuit or not. When I started practicing law—maybe that is *passee*—that was not the way to practice. Now it seems to be for many of those, and they would like to keep it that way for this system.

It also makes us do sloppy legal work—not us but those who are doing it—sloppy legal work. The cookie-cutter complaint, which is probably the one the Senator referred to as to Raytheon—cookie-cutter complaint. All the allegations are the same, case after case. Senator D'AMATO, we have one, they always use the same allegations and the same words. The lawyers just change the name of the company being sued—it pops out of the computer. In fact, I think some of them have terminals where they are hooked into the stock market. The stock is going to fluctuate and the computer is going to spit out a lawsuit.

The lawyer just signs his name on it. But a judge took one of these not so lightly because a plaintiff's lawyer inserted in the complaint the name of the company he was suing: Philip Morris. They accused Philip Morris of fraudulently manufacturing toys, t-o-y-s, not cigarettes. Philip Morris does not manufacture toys, a typical cookie cutter complaint—a demand for hundreds of millions of dollars in damages. This bill is about stopping this kind of lawsuit. It is shoot, aim, ready. Instead of ready, aim, shoot, it is shoot, aim, ready.

The National Association of Securities and Commercial Lawyers suggests that 56 percent of the cases they had hand picked to provide data on to the Securities Subcommittee were filed within 30 days of the triggering event. A triggering event is usually a missed earnings projection, a so-called earnings surprise. Twenty-one percent of the cases were filed within 48 hours of

the triggering event. The stock prices dropped, and class action suits are filed with little due diligence to investigate the basis of the case.

But you can count on it. If the lawyer is a good entrepreneur and sticks with it, he will get paid something even for that kind of suit, whether there is anything to the suit. Companies have to settle.

Of the 111 cases filed in 1990 and 1991, 25 percent were filed by pet plaintiffs, the plaintiff that we described a while ago. In 25 percent of the cases, they went out and hired the plaintiff and paid them a bonus. Even if they had a lawsuit that was decent, the point of it is that was an effort to get to the courthouse quick with the pet plaintiff. So you could be the lead counsel, or at least you could maybe be representing \$500 million worth of securities for a \$150, \$200, \$300 pet plaintiff.

So from this Senator's standpoint, the bill before us is a very good approach to settling and solving these problems. As I see it, the details of this bill will be debated and amendments will be offered. So I am not going to go into details.

But I would like to just close with one current situation. I know about it because a company has one of its biggest production plants in New Mexico. The general counsel for Intel testified that Intel had been sued. When it was a startup, such a suit probably would have bankrupted the company long before it investigated in microchips.

This is an example of the innovation and entrepreneurship that these cases are threatening to snuff out. So let me give you one about Intel. If this had been filed when it was a young company, we would not have Intel.

On December 19, 1994, Intel was sued over the flaw in the Pentium chip. Despite the fact that it would take 29,000 years for the chip's flaw to become apparent, and despite the fact that on December 20, 1994, Intel responded to market concerns about the chip by implementing its "no questions asked" replacement policy. The lawyers who filed on December 19 are asking \$6 million in fees for 1 day's work. Even though they dropped the suit and Intel did not have to pay anything to the shareholders, the lawyers have inserted a provision in the settlement which forbids defendants, the defendant Intel, from publicly discussing the fee or any other provision of the settlement.

S. 240 before this Senate would require disclosure of settlements, even this kind of settlement—nothing to the plaintiffs, everything to the lawyers. With better disclosure I doubt whether that will happen very often.

Can you imagine a public disclosure for that? We did not do anything for anyone, but we get \$6 million. That is nice. It is interesting. Would you not like to be doing that? It is pretty good. It might even be better than being a Senator. Who knows?

Well, there are many more like this. I have a great deal of explanation.

Prof. Joseph Grundfest of Stanford Law School has said that the plaintiffs lawyers have done little if anything to earn their hefty request.

Says Grundfest: "much of the settlement would have come about even if no lawsuit was filed * * * to reward lawyers for that at all is the equivalent of double-dipping."

Mesa Airlines' officers and directors were sued for keeping their mouth shut. They had a corporate policy not to talk to analysts. The analysts make some projections about Mesa. The airline neither confirmed nor denied whether they agreed or disagreed with the analysts. The mesa officers just tried to run an efficient airline. The plaintiff's lawyers have alleged that Mesa's failure to talk about analysts' projections was "deemed to be acceptance" of the content of the analysts' prediction. The company missed the earnings projections, their stock price dropped, and they got sued.

Prudential Bache Securities. Investors represented by the firm who testified before the committee received 4 cents on the dollar under the class action lawsuit settlement. The firm took \$6 million plus expenses. Other investors who hired their own lawyers, and went to arbitration came away fully compensated.

Frivolous litigation is time-consuming and distracts chief executive and other corporate officials from productive economic activity. It has been estimated that defending one of these lawsuits is as costly as starting up a totally new product line.

These frivolous lawsuits are such a menace to publicly traded companies on the NASDAQ that the NASDAQ Self-Regulatory Organization decided to recommend reforms to Senator DODD and me.

SYSTEM IS BROKEN

The conclusion of any one who has examined the issue carefully is: The current securities implied private litigation system is broken. The system is broken because too many cases are pursued for the purpose of extracting settlements from corporations and other parties, without regard to the merits of the case. The settlements yield large fees for plaintiffs' lawyers but compensate investors only for a fraction of their actual losses. Janet Cooper Alexander of Stanford University has proven that most securities class actions are settled by the parties without regard to whether the case has merit. Chairman of the SEC, Arthur Levitt acknowledged that "virtually all securities class actions are settled for some fraction of the claimed damages, and some alleged that settlements often fail to reflect the underlying merits of the cases. If true, this means that weak claims are overcompensated and strong claims are undercompensated." Prof. John Coffee has concluded the plaintiffs' attorneys in many securities class actions appear to "sell out their clients in return for an overly generous fee award," and that

the defendants may also join in this collusion by passing on the cost of the settlement to absent parties, such as insurers."

The plaintiffs' lawyers like to sue the officers and directors, and the accountants, underwriters and issuers. These cases are brought under joint and several liability which means that any one defendant could be made to pay the entire judgment even if he or she were only marginally responsible. If a person is one percent liable he/she could be asked to write a check for 100 percent of the awarded damages. That is not fair.

Our bill builds upon the State law trend of imposing proportionate liability.

Under proportionate liability each person found responsible pays a share of the damages that is equivalent to the harm he or she caused.

Our bill would retain joint and several liability for the really bad actors, but would provide proportionate liability for those parties only incidentally involved. In response to the Securities and Exchange Commission's staff concern we also included a special provision to address the problem of the insolvent codefendant. We believe this provision strikes the correct balance. This liability reform is important to outside officers and directors, auditors and others who often get named in the law suit but who have little if any true liability. It helps change the economics that drive these frivolous cases.

BIG MONEY DAMAGES

The system seeks huge monetary recoveries from outside directors, outside lawyers, and independent accountants who may be only marginally involved in activities for which corporate officers should be primarily liable. Experienced people are declining to serve on boards because of the liability exposure. This denies growing companies the expertise they need to succeed. The system is not deterring fraud because insurance companies pay most of the settlement amount.

The current system also discriminates against defendants. People who have deep pockets are often named in the law suits to coerce settlements. Accountants bear the brunt of our current system of joint and several liability. Suing the accountant insures that the settlement will be 50 percent larger because of their deep pocket.

The fundamental purposes of the Federal securities laws are to promote investor confidence and deter fraud. But the system is failing its deterrent mission. A system where the merits don't matter isn't a deterrent. A system where most settlement funds are paid by insurance companies isn't a deterrent.

A system that is having a chilling effect on corporate disclosure is actually working at cross-purposes with its objective. Class action securities cases inhibit voluntary disclosure by corporations, discouraging them from making any public statements except

when absolutely required, for fear that anything they say which might move the company's stock price might trigger a lawsuit.

In order for our capital markets to function efficiently, for Wall Street analysts to evaluate stocks, or for main street investors to buy, hold, or sell a stock, they need a lot of information. An important type of information is the projections of how the company will do in the future—the so-called forward-looking statement.

By its definition, a forward looking statement is a prediction about the future. Earnings projections, growth rate projections, dividend projections, and expected order rates are examples of forward looking statements. Predictions about the future have become one of the more common types of frivolous securities lawsuits filed.

Few people know why it is important for the bill to provide a safe harbor for predictive statements. Let me ask a few questions to help my colleagues understand.

First, do you believe that earnings projections about the future are promises?

Second, do you believe stock volatility is stock fraud?

Third, do you believe that projections about future earnings should be unanimous among every single employee in the company in order for that prediction to be eligible for protection for abusive lawsuits?

Fourth, do you believe that it is fraud when an officer or director or other employee receives a significant portion of his compensation in stock options sells stock regularly?

Fifth, if you believe that any statement about future performance can, and should be used against you no matter how well intended, no matter how well reasoned, regardless of how dramatic circumstances change?

The five statements I just read are the basis for most predictive statement, class action securities cases.

To me, these cases represent everything that I find discouraging about our legal system—professional plaintiffs, fishing expeditions for documents, boiler-plate fraud accusations, contingency fee lawyers, and settlement that resemble legal blackmail.

A safe harbor is needed to encourage companies to make information available. To keep the system honest, there are laws on the books to make sure that executive trades do not create even the appearance of illegal insider trading, the process is highly regulated by the SEC. In addition, most companies have their own internal policies regulating when executives can make trades. These controls ensure that executives do not trade during lengthy black out periods within months of important announcements. The SEC also has imposed rules regarding executive selling that require prompt reports, which are then available to the investing public.

First, if you believe that efficient capital markets need information, you

agree with investors, the SEC, and securities analysts. As the California Public Employees Retirement System [CALPERS] recently stated, "forward-looking statements provide extremely valuable and relevant information to investors."

SEC Commissioner Arthur Levitt recently wrote: "There is a need for a stronger safe harbor than currently exists. The current rules have largely been a failure * * *."

Former SEC Chairman Richard Breen testified:

Shareholders are also damaged due to the chilling effect of the current system on the robustness and candor of disclosure. . . . Understanding a company's own assessment of its future potential would be among the most valuable information shareholders and potential investors could have about a firm.

Second, if you believe that disclosure of information helps investors make intelligent decisions you should be calling for reform because the very nature of forward-looking statements makes them particularly fertile ground for abusive lawsuits. If a company fails to meet analysts' profit expectations, or production of a new product is delayed, it is often faced with a law suit. As a result, companies are increasingly reluctant to disclose forward-looking information. Numerous studies have documented this trend. According to testimony given by James Morgan, National Venture Capital Association, one study found that over two-thirds of venture capital firms were reluctant to discuss their performance with analysts or the public because of the threat of litigation.

Keeping quiet is not an escape route from these frivolous cases. One company in my State had a policy not to talk to analysts which developed from a fear of being sued. But they were sued anyway for failing to disagree with an analysts' projection. The legal theory was that the company incorporated by silence the analysis's estimations. Mesa Airlines is not the only company to be sued for keeping its mouth shut.

Third, if you recognize that predictions about the future do not always come true and that investing has some risks attached, you should support the statutory safe harbor: Institutional investors are the most professional, sophisticated investors in our markets. In addition, they have a fiduciary duty to retirees to prudently manage their pension funds. These institutional investors have argued that forward looking statements accompanied by warnings should be per se immune from liability. The Council of Institutional Investors told the SEC that any safe harbor must be 100 percent safe. This means that all information in it must be absolutely protected from law suits even if it is irrelevant or unintentionally or intentionally false or misleading. The bill does not go as far as the institutional investors suggested. We think it strikes the correct balance.

The SEC Rule 175 permits issuers to make forward looking statements

about certain categories of information provided that the prediction is made in good faith with a reasonable basis. Currently, this SEC safe harbor rule actually discourages issuers from voluntarily disclosing this information. To quote the SEC:

Some have suggested that companies that make voluntary disclosure of forward-looking information subject themselves to a significantly increased risk of securities anti-fraud class actions." As such, "contrary to the Commission's original intent, the safe harbor is currently invoked on a very limited basis in the litigation context." Critics state that the safe harbor is ineffective in ensuring quick and inexpensive dismissal of frivolous private lawsuits. (SEC Securities Act of 1993 Release No. 7101, October 1994)

An American Stock Exchange survey supports that conclusion. It found that 75 percent of corporate CEO's limit the information disclosed to investors out of fear that greater disclosure would lead to an abusive lawsuit.

As the SEC has realized, forward-looking statements are predictions—not promises. This bill recognizes that a reasonable basis for such information doesn't have to be a unanimous basis. This bill creates a statutory safe harbor which:

Provides a clear definition of "forward looking statement" for both the 1933 and 1934 acts;

Covers written and oral statements;

Requires that the predictive statement contain a Miranda warning describing the statement as a prediction and a disclosure that there is a risk that the actual results may differ materially from those predicted;

No safe harbor protection for statements knowingly made with the expectation, purpose, and actual intent of misleading investors. There is no so-called license to lie under this bill;

Protects statements made by issuers, persons acting on their behalf such as officers, directors, employees, and outside reviewers retained by the issuer. Accounting and law firms are eligible for the safe harbor, brokers and dealers are not;

No safe harbor protection for initial public offerings [IPOS], penny stocks, roll-up transactions and issuers who have violated the securities laws;

Provides the SEC with new authority to sue for damages on behalf of investors in predictive statement cases. The SEC's recovery should be much better than the average of 6 cents on the dollar currently recovered by private attorneys;

Encourages SEC to review the need for additional safe harbors.

New Mexico is a high-technology State. It is the home to Los Alamos and Sandia National Laboratories. We have more engineers and PhD's per capita than any State in the Union. High technology and high growth companies are our future, yet they are the companies that are hit most often by frivolous lawsuits. They have volatile stock. I do not really see how New Mexico can expect to develop the spin-off companies from the labs and to

grow high technology companies unless we pass legislation that has a meaningful safe harbor for predictions about the future.

I am pleased that the final bill includes a statutory safe harbor. Originally, S. 240 contained an instruction to the SEC to develop a new safe harbor. However, the SEC has been working on it for more than a year and they are gridlocked. They held some very good hearings and some of the material presented before them has been very useful to the committee in developing its statutory safe harbor.

We want to get back to basics. The central principle underlying the securities laws is that investors should receive accurate and timely disclosure of the financial condition of publicly traded companies.

The objective of this bill is to recognize that litigation isn't George Orwell's 1994 version of Big Brother looking out for investors' best interest. We reject "stock volatility is fraud"; we reject "justice is pennies for lawyers"; We reject "equity is millions for lawyers."

S. 240 will encourage disclosure, strengthen confidence, realine the role of the entrepreneurial plaintiffs' lawyers with the best interests of their clients, and change the risk/benefit equation of taking cases to the jury.

The basis of our bill is to make the plaintiffs' bar, "Stop, think, investigate, and research."

The spirit motivating this bill is the obligation that Chairman Levitt identified, "to make sure the current system operates in the best interest of all investors. This means focusing not just on the interests of those who happen to be aggrieved in a particular case, but also on the interests of issuers and the markets as a whole."

With S. 240, we have decided to take a historic step. For the first time since Congress created the Federal securities laws in 1933 and 1934, we have decided to revisit section 10(b) and rule 10b-5 in order to fix many of the problems created by the courts and our own failure to act during the past 60 years. If you would like to put an end to the inconsistency and confusion, you should support S. 240. If you would like to relieve the courts of the burden of revisiting 10b-5 every year and put an end to the judicial activism associated with this area of the law, vote for this bill. If you want to allow the abuse of investors and companies, the stifling of job creation and the continued shaping of the contours of the law to continue, you should vote against it. In the end, S. 240 will give courts greater guidance to deal with meritorious securities class actions and greater incentive to eliminate most, if not all, of the frivolous ones. We owe it to investors, companies, and our capital markets to take this historic step.

Mr. President, hopefully, in the next few days, we will change this law and go to conference with the House, and maybe before this year is out, set some of these things straight.

I yield the floor.

Mr. SARBANES addressed the Chair. The PRESIDING OFFICER (Mr. BENNETT). The Senator from Maryland is recognized.

Mr. SARBANES. Mr. President, I have listened to my colleagues now for well over an hour very carefully. This is an important piece of legislation, and it deserves very careful attention. I think perhaps the best summary, in a sense, of some of the statements we have heard was the comment made by my distinguished colleague from Connecticut, who said that there might well be a tendency in the course of debating this bill to use increasingly extreme examples and overheated rhetoric. I think that was his exact quote. And we have already seen some of that at work over the opening debate that has taken place now for well over an hour.

I do not know of anyone who differs with the goal of deterring frivolous lawsuits, and sanctioning appropriate parties when such lawsuits are filed. My colleague from Connecticut at one point said this bill is an important step in repairing an ailing system. Parts of this bill are an important step in doing that. Other parts of this bill will, in my judgment, contribute to an unhealthy system. And the challenge that is before the Senate over the next few days as we work through this legislation is to be able to distinguish between those parts in this legislation.

In the course of this consideration, amendments will be offered. Amendments were offered in committee. Some were decided by very close votes. We hope by proposing those amendments to be able to focus on what the problems are. But let me just generally make the point that this legislation as now drafted will affect far more than frivolous suits. The examples that have been cited, the horror cases, are examples that any of us would want to address and try to deal with. This bill goes beyond that. This bill overreaches that mark and, in fact, in my judgment, will make it more difficult for investors to bring legitimate fraud actions. That is the essential question. That is the discernment we have to make here.

Jane Bryant Quinn said in an article less than a week ago in the Washington Post, entitled "Making it Easier to Mislead Investors," and I quote from the opening of this article:

A lawsuit protection bill speeding through Congress will give freer rein to Wall Street's eternal desire to hype stocks. It's cast as a law against frivolous lawsuits that unfairly torture corporations and their accountants, but the versions in both the House and Senate do far more than that. They effectively make it easier for corporations and stockholders to mislead investors. Class action suits against the deceivers would be costly for small investors to file and incredibly difficult to win. I'm against frivolous lawsuits. Who is not? But these bills would choke meritorious lawsuits, too.

At the end of this long article, she concludes as follows, and I quote:

Baseless lawsuits do indeed exist. Lawyers may earn too much from a suit, leaving defrauded investors too little. The incentives to sue should be reduced, but not with these bills. They let too many crooks get away.

And an article in the U.S. News & World Report, the most recent issue, by Jack Egan entitled, "Will Congress Condone Fraud," says in part, and I quote, speaking about this legislation:

It just might come to be remembered as legislation that has steeply tilted the playing field against investors. It makes it very hard for shareholders to sue over legitimate grievances.

And, at the end, it goes on to say:

The pendulum has swung too far toward the lawyers, and now it is swinging too far the other way. Unfortunately, some major investor frauds may have to take place before it again moves back toward the center.

The challenge for the Senate is to get this pendulum in the right place to begin with, here, now, over the course of the next few days so that they do not have to have major investor frauds in order to swing the pendulum back toward the center.

This legislation, and certain of its provisions, goes too far. In fact, two provisions that were in the original bill as introduced were dropped in the course of evolving this legislation. Those provisions, had they remained in the bill, would deal with a number of the problems which we intend to outline over the next few days in the course of its consideration. That was in the original proposed legislation, and was taken out. As a consequence, the legislation, in my judgment, has been weakened, and the balance has tilted in an unfair and unjust way.

The fact is that this bill will make it harder to bring securities fraud actions and to recover losses. Individual investors, local governments, pension plans, all will find it more difficult to bring fraud actions and to recover their full damages as a result of this legislation.

I know examples are going to be used, but I say to my colleagues, you have to move beyond those examples. The provisions in the bill which deal with the egregious examples that would be cited ought to be in this bill and they ought to be passed. The difficulty is that the bill overreaches and it goes too far. Let me give you some instances of that.

The safe harbor provision will for the first time protect fraudulent statements within the Federal securities laws. Individual investors will not be able to sue people who make fraudulent projections of important items such as revenues and earnings.

The SEC has been working to address the question of forward looking statements, but the Chairman of the SEC, Arthur Levitt, has raised very serious questions about the safe harbor provision in this legislation. If I wanted to engage in the Senator's rhetorical combat that he spoke about earlier, I would say, rather than safe harbor, it is a pirate's cove that is in this legislation. The proportionate liability provision will for the first time put fraud

participants ahead of innocent victims and individual investors. Fraud victims will not recover their full damages.

The argument is made that you have people who are held liable, they vary in their proportionate share of the responsibility, and the deep-pocket people are held entirely liable when the principal malefactor goes bankrupt or cannot pay the award. This is in a suit that is proven to be successful, been upheld as being meritorious in court. Well, there is a problem amongst the malefactors. But to throw the burden on the innocent victim as a solution to that problem is a departure which really astounds one.

In other words, you are the victim of the fraud. A number of people have participated in it in varying degrees, and you are going to be held to assume a large part of the burden before the participants in the fraud have to be responsible. As a consequence, fraud victims will not recover the full damages.

The managers of the bill speak about its balance. In fact, the bill has a tilt, as this column in U.S. News & World Report said, and I quote it again:

It just might come to be remembered as legislation that's steeply tilted the playing field against investors.

There is not included in this legislation provisions that the SEC and the State securities regulators feel are necessary to protect victims of securities fraud. I was interested that the Senator from Connecticut quoted Arthur Levitt as saying in a hearing there is a need for change.

That is quite true. But Chairman Levitt criticizes the measure that is now before us. If you are going to cite Arthur Levitt as supporting the proposition for change, which actually none of us is contending against here—we are not coming to the floor and saying do nothing, just leave the existing law. We are saying that there are some provisions in this legislation that ought to be passed, but there are other provisions that overreach and go too far, and Arthur Levitt says the same.

The very person cited in a sense as an expert for the proposition that change ought to be made has also told us that some of the changes contained in this legislation are undesirable.

In addition to the safe harbor issue, which we will come back and revisit in the course of the amending process, is the proportionate liability issue. This bill does not extend the statute of limitations for securities fraud actions. Fraud victims will not have time to bring their cases to court. That in fact was a provision that was in the original bill as introduced and has been dropped from the provision now before us.

The bill does not restore the ability of investors to sue individuals who aid and abet violations of the securities laws. Fraud victims will not be able to pursue everyone who helped commit a securities fraud.

It is asserted that this bill as it has reached the proper balance, but the

fact remains that it is opposed, the legislation as before us, by a host of securities regulators, by State and local government officials, by consumer groups, by labor unions, by bar associations, and others, including the North American Securities Administrators Association, the Government Finance Officers Association, the National League of Cities, the U.S. Conference of Mayors, the Consumer Federation of America, and a number of the large trade unions, including the Teamsters and the United Auto Workers.

The assault from the other side has been on the lawyers. These groups do not represent the lawyers. These groups represent the public, consumers, investors, and they have all reached the judgment that this bill is unbalanced—unbalanced.

Let me just speak for a moment or two about the background. It is asserted by some that there is a crisis in the securities litigation system that is threatening our capital markets. Let us take a look very quickly at our capital markets and some statistics about it.

For 1993, the U.S. equity market capitalization stood at \$5.2 trillion, over one-third of the world total. More than 600 foreign companies from 41 different countries are listed on our exchanges and more foreign companies come every year. Average daily trading volume on the New York Stock Exchange has increased from 45 million shares in 1980 to 291 million shares in 1994. From 1980 to 1993, mutual fund assets increased by more than 10 times to \$1.9 trillion.

In effect, Mr. President, what this demonstrates is that the U.S. capital markets remain the largest and the strongest in the world.

Now, this, I would submit, is not in spite of the Federal securities laws but in part because of the Federal securities laws. This tremendous growth in the American marketplace and its pre-eminent position worldwide is not in spite of Federal securities laws but in part because of Federal securities laws. The Federal securities laws have generally provided for sensible regulation and self-regulation of exchanges, brokers, dealers, and issues.

This regulation has helped to sustain investor confidence in our markets. Without that confidence in the markets, you are not going to get the kind of dominant position that we have had. And confidence in the markets on the part of investors is a consequence not only of the public regulatory scheme administered by the SEC but also because investors know that they have effective remedies against people who try to swindle them.

In other words, if you weaken unreasonably or improperly these remedies, you are going to affect investor ability to have recourse in instances in which they have been unfairly or improperly exploited, and the consequence of that is you begin to cast a doubt over the integrity of the securities markets.

Both Republican and Democratic Chairmen of the Securities and Exchange Commission have stressed the crucial role of the private right of action in maintaining investor confidence.

In 1991, then-Chairman Richard Breen testified before the Banking Committee, and I quote:

Private actions . . . have long been recognized as a "necessary supplement" to actions brought by the Commission and as an "essential tool" in the enforcement of the Federal securities laws. Because the Commission does not have adequate resources to detect and prosecute all violations of the Federal securities laws, private actions perform a critical role in preserving the integrity of our securities markets.

Current Chairman Arthur Levitt echoed this very point in testimony delivered this year.

The Securities Subcommittee held hearings over the past 2 years reviewing the Federal securities litigation system. It received testimony from plaintiffs' lawyers, from corporate defendants, from accountants, from academics, from securities regulators, and from investors. There was considerable disagreement among the witnesses over how well the existing securities litigation system is functioning. Some argued, and my colleagues who have already spoken argue, American business, particularly younger companies in the high-technology area, face a rising tide of frivolous securities litigation. Corporate executives suggested that securities class actions are filed when a company fails to meet projected earnings or its stock drops.

Clearly, some frivolous securities cases are filed as, indeed, some frivolous cases of every sort are filed. However, the Director of the SEC's Division of Enforcement testified in June 1993 with respect to statistics from the Administrative Office of the U.S. Courts:

The approximate aggregate number of securities cases, including Commission cases, filed in Federal district courts does not appear to have increased over the past 2 decades. Similarly, while the approximate number of securities class actions filed during the past 3 years is significantly higher than during the 1980's, the numbers do not reveal the type of increase that ordinarily would be characterized as an "explosion."

Some said that these actions were inhibiting the capital formation process. In fact, initial public offerings have been setting records in recent years: \$39 billion in 1992; \$57 billion in 1993. The \$34 billion in initial public offerings in 1994 was exceeded only by the records set in the previous 2 years.

On May 22, the New York Times reported, and I quote:

One of the great booms in initial public offerings is now under way, providing hundreds of millions in new capital for high-tech companies, windfalls for those with good enough connections to get in on the offerings and millions in profit for the Wall Street firms underwriting the deals.

Asserting a crisis in securities litigation, which the figures do not seem to bear out, this bill makes it harder to bring lawsuits. We should ask ourselves

not simply whether these changes will result in fewer lawsuits, but whether each proposed change will make the securities laws serve our Nation better. We should ask whether legitimate cases can still be brought or whether the provisions in this legislation, which it is asserted are designed to screen out the frivolous cases, will go beyond that and, in effect, make it difficult to bring legitimate cases.

I hope Members will focus on this very issue. It is very important not to become, as it were, mesmerized by these extreme examples which my colleague from Connecticut said would obviously be cited, because no one is protecting the extreme examples.

The question is whether the provisions here will make it impossible or highly difficult to bring legitimate actions, whether it will swing the pendulum too far in the other direction. One of the articles I quoted said:

Unfortunately, some major investor frauds will have to take place before it, again, moves back toward the center.

We do not want that to happen. We have an opportunity here on the floor by correcting this legislation to prevent that from happening.

Let me very quickly turn to some of the major defective provisions in the legislation.

First is the so-called safe harbor provision. This legislation has a statutory definition of an exemption from liability for forward-looking statements which the bill broadly defines to include both oral and written statements. Examples include projections of financial items such as revenues and income for the quarter or for the year, estimates of dividends to be paid to shareholders, and statements of future economic performance, such as sales trends and development of new products. In short, forward-looking statements include precisely the type of information that is most important to investors deciding whether to purchase a particular stock.

The SEC currently has a safe harbor regulation for forward-looking statements that protects specified forward-looking statements that were made in documents filed with the SEC. To sustain a fraud suit, the investor must show that the forward-looking information lacked a reasonable basis and was not made in good faith.

The SEC, recognizing the desirability of having some safe harbor for forward-looking statements, has been seeking to define it in regulation.

It has been conducting, in fact, a comprehensive review of its safe harbor regulation. This legislation, as originally introduced by Senators DOMENICI and DODD, would have allowed the SEC to continue this regulatory effort. And Chairman Levitt endorsed that approach. However, the committee print substitute for S. 240, unlike the bill as introduced, abandoned this approach in favor of enacting a statutory safe harbor.

The committee print now before us, in effect, protects fraudulent forward-

looking statements. For the first time, such statements would find shelter under the Federal securities law. In a letter to the committee, Chairman Levitt, expressing his personal views about a legislative approach to safe harbor, stated:

A safe harbor must be thoughtful so that it protects considered projections but never fraudulent ones.

The bill, as reported, provides safe harbor protection for all statements except those knowingly made with the expectation, purpose, and actual intent of misleading investors. The committee report states that expectation, purpose, and actual intent are separate elements, each of which must be proven by the investor, otherwise the maker of the statement is shielded.

This language so troubled Chairman Levitt that he wrote to committee members on May 25, the morning of the markup. He stressed that the substitute committee print failed to adhere to his belief that a safe harbor should never protect fraudulent statements.

I want to be very clear about this. No one is arguing whether there should be some provision for a safe harbor. The question is: What should that provision be? What is reasonable? What is proper? What is balanced? What constitutes overreaching? The chairman of the SEC said the following in that letter to the committee on the morning of the markup:

I continue to have serious concerns about the safe harbor fraud exclusion as it relates to the stringent standard of proof that must be satisfied before a private plaintiff can prevail. As Chairman of the Securities and Exchange Commission, I cannot embrace proposals which would allow willful fraud to receive the benefit of safe harbor protection. The scienter standard in the amendment may be so high as to preclude all but the most obvious frauds.

He warned that the bill's standard of "knowingly made with the expectation, purpose, and actual intent of misleading investors" was a far more stringent standard than currently used by the SEC and the courts. The committee report states that the safe harbor provision is intended to encourage disclosure of information by issuance. Encouraging reasonable disclosure is one thing. Encouraging fraudulent projections is obviously yet another.

The safe harbor provision that is in this bill, which was not in the original bill as introduced by Senators DODD and DOMENICI—this safe harbor provision before us would hurt investors trying to make intelligent investment decisions and penalize companies trying to communicate honestly with their shareholders. It runs counter to the entire philosophy of Federal securities laws, the very laws that have helped give us such strong markets, laws that rest on the premise that fraud must be deterred and punished when it occurs. That is one of the major areas in which attention will have to be focused over the next few days.

Next I turn to the proportionate liability provision in the bill. The dif-

ficulty with the proportionate liability section in the bill is we need to understand the issue of liability for reckless conduct.

In 1976, the Supreme Court held that a defendant is liable under Federal securities antifraud provisions only if he or she possesses the state of mind known in the law as "scienter." Conduct that is intended to deceive or mislead investors satisfies the scienter requirement. While the Supreme Court did not decide the question, courts in every Federal circuit have held that reckless conduct also satisfies the scienter requirement. This follows the guidance of hundreds of years of court decisions in fraud cases. As the Restatement of Torts states, "The common law has long recognized recklessness as a form of scienter for the purposes of proving fraud."

Now, the most commonly accepted definition of reckless conduct was set forth by the Seventh Circuit in the Sundstrand case. That standard—and I will quote it, an order which attached joint and several liability—said:

A highly unreasonable omission involving not merely simple, or even gross, negligence, but an extreme departure from the standards of ordinary care and which present a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it.

Now, recklessness liability is often applied to the issuers' professional advisers—attorneys, underwriters, accountants. And under joint and several liability, all parties who participate in a fraud are liable for the entire amount of the victim's damages—both those parties who intended to mislead the investors, and those whose conduct was reckless.

The rationale for this is that a fraud cannot succeed without the assistance of each participant, so each wrongdoer is held equally liable.

This bill limits joint and several liability under the Federal securities laws to certain defendants, specifically excluding defendants whose conduct was reckless. This change will hurt investors in cases where the perpetrator of the fraud is bankrupt, has fled, or otherwise cannot pay the investors' damages. In those cases, innocent victims of fraud will be denied full recovery of their damages. Chairman Levitt said:

The Commission has consistently opposed proportionate liability.

Before the Securities Subcommittee, he said:

Proportionate liability would inevitably have the greatest effect on investors in the most serious cases (for example, where an issuer becomes bankrupt after a fraud is exposed). It is for this reason that the Commission has recommended that Congress focus on measures directly targeted at meritless litigation before considering any changes to the liability rules.

Now, even the authors of the measure before us recognize something of a problem, so they have tried to make

some compensating features with respect to proportionate liability, and we will address those in greater detail when we propose an amendment.

Let me just simply make this point. They would provide coverage to victims with a net worth under \$200,000 who lose more than 10 percent of that net worth. Well, that hardly is meaningful. Virtually anyone who owns a home has a net worth of \$200,000. And to require many small investors to lose more than 10 percent of that net worth—in other words, you would have to lose \$20,000 before you would be made whole by those who have participated in or condoned the fraud.

There is another provision for a 50-percent coverage, but neither provision will make fraud victims whole. They will protect only a tiny number of investors. For most investors, the balance of their losses may be uncollectible. So the innocent party is going to be called upon to bear this burden. Just think of the equities of that.

Reckless participation. Participants will no longer be responsible for the result of their conduct. Innocent investors—individuals, pension funds, county governments—will have to make up the loss. This is not fairness—certainly not to the investors.

In addition, I am disappointed that this legislation, as reported, does not contain provisions to help investors bring meritorious suits. In his letter to the members of the Banking Committee, Chairman Levitt stated:

In addition to my concerns about the safe harbor, there is not complete resolution of two important issues for the Commission. First, there is no extension of the statute of limitations for private fraud actions from 3 to 5 years.

My very able, distinguished colleague from Nevada, who is a member of the subcommittee that considered this legislation, and is extremely knowledgeable on all aspects of it, will later, in the course of the amending process, address this specific provision.

For over 40 years, courts held that the statute of limitations for private rights of action under section 10(b) of the Securities Exchange Act of 1934, the principal antifraud provision of the Federal securities laws, was the statute of limitations determined by applicable State law. While these statutes varied, they generally afforded securities fraud victims sufficient time to discover and bring suit.

In 1991, in the *Lampf* case, the Supreme Court significantly shortened the period of time in which investors may bring such securities fraud actions. By a 5 to 4 vote, the Court held that the applicable statute of limitations is 1 year after the plaintiff knew of the violation and in no event more than 3 years after the violation occurred. This is shorter than the statute of limitations for private securities actions under the law of more than 60 percent of the States today.

This shorter period does not allow individual investors adequate time to

discover and pursue violations of securities laws. Testifying before the Banking Committee in 1991, SEC Chairman Richard Breeden stated “the time-frames set forth in the [Supreme] Court’s decision is unrealistically short and will do undue damage to the ability of private litigants to sue.” Chairman Breeden pointed out that in many cases,

Events only come to light years after the original distribution of securities and the . . . cases could well mean that by the time investors discover they have a case, they are already barred from the courthouse.

The FDIC and the State securities regulators joined the SEC in favor of overturning the *Lampf* decision.

On this basis, the Banking Committee in 1991 without opposition adopted an amendment to a banking bill. The amendment lengthened the statute of limitations for securities fraud actions to 2 years after the plaintiff knew of the securities law violation, but in no event more than 5 years after the violation occurred.

When the bill reached the Senate floor in November 1991, some Senators indicated they would seek to attach additional provisions relating to securities litigation. They argued that the statute of limitations should not be lengthened without additional reform of the litigation system. No arguments were raised specifically against the extension of the statute of limitations. To expedite consideration of the bill, the extension of the statute of limitations was dropped. Senators DOMENICI and DODD included the extended statute of limitations in their comprehensive securities litigation reform bill, both in the last Congress and in this Congress.

There was no rationale for dropping that provision out. Chairman Levitt testified before the Securities Subcommittee in April 1995, “extending the statute of limitations is warranted because many securities frauds are inherently complex, and the law should not reward the perpetrator of a fraud who successfully conceals its existence for more than 3 years.”

I defy any of my colleagues to explain to us why the perpetrator of the fraud ought to be given a shorter period of time in which to get away with this fraudulent conduct.

Finally, let me turn to the failure to restore aiding and abetting liability. This was another matter touched on by Chairman Levitt when he expressed his disappointment that “the draft bill does not fully restore the aiding and abetting liability eliminated in the Supreme Court’s *Central Bank of Denver* opinion.”

Prior to that decision, courts in every circuit in the country had recognized the ability of investors to sue aiders and abettors of securities frauds. Most courts required that an investor show that a securities fraud was committed, that the aider and abettor gave substantial assistance to the fraud, and that the aider and abettor has some de-

gree of scienter—intent to deceive or recklessness toward the fraud.

Why should the aiders and abettors of the fraud escape any liability? As Senator DODD stated at a May 12, 1994, Securities Subcommittee hearing, “aiding and abetting liability has been critically important in deterring individuals from assisting possible fraudulent acts by others.” Testifying at that hearing, Chairman Levitt stressed the importance of restoring aiding and abetting liability for private investors:

persons who knowingly or recklessly assist the perpetration of a fraud may be insulated from liability to private parties if they act behind the scenes and do not themselves make statements, directly or indirectly, that are relied upon by investors. Because this is conduct that should be deterred, Congress should enact legislation to restore aiding and abetting liability in private actions.

The North American Securities Administrators Association and the Association of the Bar of the City of New York also endorsed restoration of aiding and abetting liability in private actions.

In summing up, let me simply say I support the goal of deterring and sanctioning frivolous securities litigation. This bill, though, will deter legitimate fraud actions as well. By protecting fraudulent forward looking statements, and by restricting the application of joint and several liability, this bill may undermine the investor confidence on which our markets depend. Further, it fails to include provisions that are needed to ensure that investors have adequate time and means to pursue securities fraud actions.

We are not alone in concluding this legislation will threaten our markets by undermining investor confidence. Since the Banking Committee approved this bill we have received letters of opposition from securities regulators, State and local government officials, consumer groups and others, which I will place in the RECORD following this statement.

The assertion is, on the other side, there is a certain private interest involved. We are trying to get at the abuse of the existing securities laws. But, in effect, independent observers, as it were, the securities regulators, local government officials, State government officials, have looked at this thing and they say this is excessive. This is overreaching.

In a June 8, 1995 letter, the Government Finance Officers Association [GFOA] strongly supported our position. Consisting of more than 13,000 State and local government financial officials, the GFOA’s members both issue securities and invest billions of dollars of public pension and taxpayer funds. In its letter, the GFOA opposed S. 240 as reported:

We support efforts to deter frivolous securities lawsuits, but we believe that any legislation to accomplish this must also maintain an appropriate balance that ensures the rights of investors to seek recovery against those who engage in fraud in the securities markets. We believe that S. 240 does not

achieve this balance, but rather erodes the ability of investors to seek recovery in cases of fraud.

The North American Securities Administrators Association, which represents the 50 State securities regulators, wrote earlier this week "to express * * * opposition to S. 240 as it was reported out of the Banking Committee." The letter expresses "NASAA's view that the bill succeeds in curbing frivolous lawsuits only by making it equally difficult to pursue rightful claims against those who commit securities fraud."

And they mention the amendments pertaining to safe harbor, proportional liability, the statute of limitations, and aiding and abetting liability as being desirable changes to be made in this legislation.

On May 23, 1995, 12 separate groups wrote to the Committee, including the National League of Cities, the American Council on Education, and the California Labor Federation of the AFL-CIO. They wrote that the committee print "has not moved at all in the direction of the achieving the balance we believe is so critical."

The St. Louis Post Dispatch had an editorial headed "Don't Protect Securities Fraud"; the Los Angeles Times, "This Isn't Reform—It's a Steamroller: GOP bill curbing lawsuits would flatten the small investor"; the Philadelphia Inquirer, "Going easy on crooks in 3-piece suits"; and other papers across the country.

Mr. President, I ask unanimous consent that the letters that I cited and earlier made reference to, the articles, and these editorials be printed in the RECORD at the end of my statement.

The PRESIDING OFFICER. Without objection, it is so ordered.

(See Exhibit 2)

Mr. SARBANES. Mr. President, the securities markets are crucial to our economic growth; we should evaluate efforts to tamper with them very, very carefully. I hope in the course of our consideration of this measure over the next few days that Members will focus on the issues. I mean, the issue is not an extreme example for which there are provisions in the bill to deal with, with which no one quarrels. The issues are these items which I have cited about which we have heard from the Chairman of the Securities and Exchange Commission, from the Government Finance Officers Association, from the North American Securities Administrators Association, from a broad range of consumer groups, and from leading editorials and columnists across the country.

I very much hope my colleagues will support amendments to correct the flaws in this legislation. If that were to be done, then we could move forward with a piece of legislation that I think would accomplish the proper balance.

Mr. President, I yield the floor.

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION,
Washington, DC, May 19, 1995.

Hon. ALFONSE M. D'AMATO,
Chairman, Committee on Banking, Housing,
and Urban Affairs, U.S. Senate, Wash-
ington, DC.

DEAR MR. CHAIRMAN: As Chairman of the Securities and Exchange Commission I have no higher priority than to protest American investors and ensure an efficient capital formation process. I know personally just how deeply you share these goals. In keeping with our common purpose, both the SEC and the Congress are working to find an appropriate "safe harbor" from the liability provisions of the federal securities laws for projections and other forward-looking statements made by public companies. Several pieces of proposed legislation address the issue of the safe harbor and the House-passed version, H.R. 1058, specifically defines such a safe harbor.

Your committee is now considering securities litigation reform legislation that will include a safe harbor provision. Rather than simply repeat the Commission's request that Congress await the outcome of our rule-making deliberations, I thought I would take this opportunity to express my personal views about a legislative approach to a safe harbor.

There is a need for a stronger safe harbor than currently exists. The current rules have largely been a failure and I share the disappointment of issuers that the rules have been ineffective in affording protection for forward-looking statements. Our capital markets are built on the foundation of full and fair disclosure. Analysts are paid and investors are rewarded for correctly assessing a company's prospects. The more investors know and understand management's future plans and views, the sounder the valuation is of the company's securities and the more efficient the capital allocation process. Yet, corporate America is hesitant to disclose projections and other forward-looking information, because of excessive vulnerability to lawsuits if predictions ultimately are not realized.

As a businessman for most of my life, I know all too well the punishing costs of meritless lawsuits—costs that are ultimately paid by investors. Particularly galling are the frivolous lawsuits that ignore the fact that a projection is inherently uncertain even when made reasonably and in good faith.

This is not to suggest that private litigation under the federal securities laws is generally counterproductive. In fact, private lawsuits are a necessary supplement to the enforcement program of the Commission. We have neither the resources nor the desire to replace private plaintiffs in policing fraud; it makes more sense to let private forces continue to play a key role in deterrence, than to vastly expand the commission's role. The relief obtained from Commission disgorgement actions is no substitute for private damage actions. Indeed, as government is downsized and budgets are trimmed, the investor's ability to seek redress directly is likely to increase in importance.

To achieve our common goal of encouraging enhanced sound disclosure by reducing the threat of meritless litigation, we must strike a reasonable balance. A carefully crafted safe harbor protection from meritless private lawsuits should encourage public companies to make additional forward-looking disclosure that would benefit investors. At the same time, it should not compromise the integrity of such information which is vital to both investor protection and the efficiency of the capital market—the two goals of the federal securities law.

The safe harbor contained in H.R. 1058 is so broad and inflexible that it may compromise investor protection and market efficiency. It would, for example, protect companies and individuals from private lawsuits even where the information was purposefully fraudulent. This result would have consequences not only for investors, but for the market as well. There would likely be more disclosure, but would it be better disclosure? Moreover, the vast majority of companies whose public statements are published in good faith and with due care could find the investing public skeptical of their information.

I am concerned that H.R. 1058 appears to cover other persons such as brokers. In the Prudential Securities case, prudential brokers intentionally made baseless statements concerning expected yields solely to lure customers into making what were otherwise extremely risky and unsuitable investments. Pursuant to the Commission's settlement with Prudential, the firm has paid compensation to its defrauded customers of over \$700 million. Do we really want to protect such conduct from accountability to these defrauded investors? In the past two years or so, the Commission has brought eighteen enforcement cases involving the sale of more than \$200 million of interests in wireless cable partnerships and limited liability companies. Most of these cases involved fraudulent projections as to the returns investors could expect from their investments. Promoters of these types of ventures would be immune from private suits under H.R. 1058 as would those who promote blank check offerings, penny stocks, and roll-ups. It should also address conflict of interest problems that may arise in management buyouts and changes in control of a company.

A safe harbor must be balanced—it should encourage more sound disclosure without encouraging either omission of material information or irresponsible and dishonest information. A safe harbor must be thoughtful—so that it protects considered projections, but never fraudulent ones. A safe harbor must also be practical—it should be flexible enough to accommodate legitimate investor protection concerns that may arise on both sides of the issue. This is a complex issue in a complex industry, and it raises almost as many questions as one answers: Should the safe harbor apply to information required by Commission rule, including predictive information contained in the financial statements (e.g. pension liabilities and over-the-counter derivatives)? Should it extend to oral statements? Should there be a requirement that forward-looking information that has become incorrect be updated if the company or its insiders are buying or selling securities? Should the safe harbor extend to disclosures made in connection with a capital raising transaction on the same basis as more routine disclosures as well? Are there categories of transactions, such as partnership offerings or going private transactions that should be subject to additional conditions?

There are many more questions that have arisen in the course of the Commission's exploration of how to design a safe harbor. We have issued a concept release, received a large volume of comment letters in response, and held three days of hearings, both in California and Washington. In addition, I have met personally with most groups that might conceivably have an interest in the subject: corporate leaders, investor groups, plaintiff's lawyers, defense lawyers, state and federal regulators, law professors, and even federal judges. The one thing I can state unequivocally is that this subject eludes easy answers.

Given these complexities—and in light of the enormous amount of care, thought, and work that the Commission has already invested in the subject—my recommendation would be that you provide broad rulemaking authority to the Commission to improve the safe harbor. If you wish to provide more specificity by legislation, I believe the provision must address the investor protection concerns mentioned above. I would support legislation that sets forth a basic safe harbor containing four components: (1) protection from private lawsuits for reasonable projections by public companies; (2) a scienter standard other than recklessness should be used for a safe harbor and appropriate procedural standards should be enacted to discourage and easily terminate meritless litigation; (3) “projections” would include voluntary forward-looking statements with respect to a group of subjects such as sales, revenues, net income (loss), earnings per share, as well as the mandatory information required in the Management’s Discussion and Analysis; and (4) the Commission would have the flexibility and authority to include or exclude classes of disclosures, transactions, or persons as experience teaches us lessons and as circumstances warrant.

As we work to reform the current safe harbor rules of the Commission, the greatest problem is anticipating the unintended consequences of the changes that will be made in the standards of liability. The answer appears to be an approach that maintains flexibility in responding to problems that may develop. As a regulatory agency that administers the federal securities laws, we are well situated to respond promptly to any problems that may develop, if we are given the statutory authority to do so. Indeed, one possibility we are considering is a pilot safe harbor that would be reviewed formally at the end of a two year period. What we have today is unsatisfactory, but we think that, with your support, we can expeditiously build a better model for tomorrow.

I am well aware of your tenacious commitment to the individual Americans who are the backbone of our markets and I have no doubt that you share our belief that the interests of those investors must be held paramount. I look forward to continuing to work with you on safe harbor and other issues related to securities litigation reform.

Thank you for your consideration.

Sincerely,

ARTHUR LEVITT.

SECURITIES AND EXCHANGE COMMISSION,
Washington, DC, May 25, 1995.

Hon. ALFONSE M. D’AMATO,
Chairman, Committee on Banking, Housing,
and Urban Affairs, U.S. Senate, Wash-
ington, DC.

DEAR MR. CHAIRMAN: I understand that this morning you and the members of the Banking Committee will be considering S. 240 and that you will be offering an amendment in the nature of a substitute. While I have not had the opportunity to analyze fully the May 24th manager’s amendment to the Committee print, I appreciate your leadership and efforts to address the concerns of the Commission in drafting your alternative.

The safe harbor provision in the amendment, in my opinion, is preferable to the blanket approach of H.R. 1058. It addresses a number of the concerns pertaining to the size of the safe harbor and the exclusions from the safe harbor. The Committee staff appears to be genuinely interested in the Commission’s views of its draft legislation and has attempted to be responsive. I was pleased to see the latest draft deleted the requirement that a plaintiff must read and actually rely upon the misrepresentation before a claim is actionable. Your attempt to

tailor the breadth of the safe harbor of the Securities Exchange Act of 1934 to the more narrow safe harbor of the Securities Act of 1933 was encouraging. However, I continue to believe that the definition should be further narrowed to parallel the items contained in my letter of May 19th. Moreover, there remain a number of troubling issues.

I continue to have serious concerns about the safe harbor fraud exclusion as it relates to the stringent standard of proof that must be satisfied before a private plaintiff can prevail. As Chairman of the Securities and Exchange Commission, I cannot embrace proposals which allow willful fraud to receive the benefit of safe harbor protection. The scienter standard in the amendment may be so high as to preclude all but the most obvious frauds. I believe that there should be a direct relationship between the level of scienter required to prove fraud and the types of statements protected by the safe harbor. My letter of May 19th indicated the discreet list of subjects that are suitable for safe harbor protection, assuming a simple “knowing” standard. Accordingly, if the Committee is unwilling to lower the proposed scienter level to a simple “knowing” standard, the safe harbor should not protect forward-looking statements contained in the management’s discussion and analysis section. This would be better left to Commission rulemaking.

In addition to my concerns about the safe harbor, there is no complete resolution of two important issues for the Commission. First there is no extension of the statute of limitations for private fraud actions from three to five years. Second, the draft bill does not fully restore the aiding and abetting liability eliminated in the Supreme Court’s Central Bank of Denver opinion. I am encouraged by the Committee’s willingness to restore partially the Commission’s ability to prosecute those who aid and abet fraud; however, a more complete solution is preferable.

I also wish to call your attention to a potential problem with the provision relating to Rule 11 of the Federal Rules of Civil Procedure. I worry that the standard employed in your draft may have the unintended effect of imposing a “loser pays” scheme. The greater the discretion afforded the court, the less likely this unintended consequence may appear.

I would like to express my particular gratitude for the courtesy and openness displayed by the Committee and its staff. I hope we will continue to work together to improve the bill so as to reduce costly litigation without compromising essential investor protections.

Thank you for your consideration.

Sincerely,

ARTHUR LEVITT.

GOVERNMENT FINANCE
OFFICERS ASSOCIATION,
Washington, DC, June 8, 1995.

Hon. PAUL S. SARBANES,
U.S. Senate, Washington, DC.

DEAR SENATOR SARBANES: I am writing on behalf of the more than 13,000 state and local government financial officials who comprise the membership of the Government Finance Officers Association (GFOA) to bring to your attention serious concerns we have with the Securities Litigation Reform Act, S. 240, recently approved by the Senate Banking Committee. As you know, the GFOA is a professional association of state and local officials who are involved in and manage all the disciplines of public finance. The state and local governmental entities our members represent bring a unique perspective to this proposed legislation because they are both investors of billions of dollars of public pen-

sion funds and temporary cash balances, and issuers of debt securities as well.

We support efforts to deter frivolous securities lawsuits, but we believe that any legislation to accomplish this must also maintain an appropriate balance that ensures the rights of investors to seek recovery against those who engage in fraud in the securities markets. We believe that S. 240 does not achieve this balance, but rather erodes the ability of investors to seek recovery in cases of fraud.

The strength and stability of our nation’s securities markets depend on investor confidence in the integrity, fairness and efficiency of these markets. To maintain this confidence, investors must have effective remedies against those persons who violate the antifraud provisions of the federal securities laws. In recent years, we have seen how investment losses caused by securities laws violations can adversely affect state and local governments and their taxpayers. It is essential, therefore, that we fully maintain our rights to seek redress in the courts.

S. 240 would drastically alter the way America’s financial system has worked for over 60 years—a system second to none. Following are the major concerns state and local governments have with this “reform” legislation:

Fraud victims would face the risk of having to pay the defendant’s legal fees if they lost. S. 240 imposes a modified “loser pays” rule that carries the presumption that if the loser is the plaintiff, all legal fees should be shifted to the plaintiff. The same presumption, however, would not apply to losing defendants. The end result of this modified “loser pays” rule is that it would strongly discourage the filing of securities fraud claims by victims, regardless of the merits of the cases. This is particularly true for state and local governments that have lost taxpayer funds through investments, involving financial fraud in derivatives, for example, but who simply cannot afford to risk further taxpayer funds by taking the risk that they might lose their case and have to pay the legal fees of large corporations. The argument is made that a modified loser pays rule is necessary to deter frivolous lawsuits, but we understand there are only 120 companies sued annually—out of over 14,000 public corporations, and that the number of suits has not increased from 1974.

Fraud victims would find it exceedingly difficult to fully recover their losses. Our legal standard of “joint and several” liability has enabled defrauded investors to recover full damages from accountants, brokers, bankers and lawyers who help engineer securities frauds, even when the primary wrongdoer is bankrupt, has fled or is in jail. S. 240 sharply limits the traditional rule of joint and several liability for reckless violators. This means that fraud victims would be precluded from fully recovering their losses.

Wrongdoers who “aid and abet” fraud would be immune from cases brought by fraud victims. As you know, aiders had been held liable in cases brought by fraud victims for 25 years until a 5-4 Supreme Court ruling last year eliminated such liability because there was not specific statutory language in federal securities law. If aiders and abettors are immune from liability, as issuers of debt securities, state and local governments would become the “deep pockets,” and as investors they would be limited in their ability to recover losses. The Securities and Exchange Commission and the state securities regulators have recommended full restoration of liability of aiders and abettors and GFOA supports that recommendation.

Wrongdoers would be let off the hook by a short statute of limitations. We had supported the modest extension of the statute—

from one year from discovery of the fraud but no more than three years after the fraud to two years after the violation was, or should have been, discovered but not more than five years after the fraud was committed—that was contained in an earlier version of S. 240. We are disappointed that this extension was removed in the Committee's markup of the legislation and hope it will be restored when the full Senate considers the bill.

Under S. 240, corporations could deceive investors about future events and be immunized from liability in cases brought by defrauded investors. Corporate predictions are inherently prone to fraud as they are an easy way to make exaggerated claims of favorable developments to attract investors. The "safe harbor" in S. 240 is a very broad exemption and immunizes a vast amount of corporate information so long as it is called a "forward-looking statement" and states that it is uncertain and there is risk it may not occur. Such statements are immunized even if they are made recklessly. We believe this opens a major loophole through which wrongdoers could escape liability while fraud victims would be denied recovery.

Access to fair and full compensation through the civil justice system is an important safeguard for state and local government investors, and is a strong deterrent to securities fraud. We believe S. 240 as written does not provide such access to state and local governments or to other investors. Just as state and local government investors are urged to use extreme caution in investing public funds, the Senate should use extreme caution in reforming the securities regulation system.

We hope you will work to bring about needed changes in the legislation when it is considered by the full Senate. If there is any way we can help in this effort, please do not hesitate to call on us.

Sincerely,

CATHERINE L. SPAIN,
Director, Federal Liaison Center.

NORTH AMERICAN SECURITIES
ADMINISTRATORS ASSOCIATION, INC.,
Washington, DC, June 20, 1995.

Re S. 240, the "Private Securities Litigation Reform Act."

Hon. PAUL S. SARBANES,
*U.S. Senate, Hart Senate Office Building,
Washington, DC.*

DEAR SENATOR SARBANES: The full Senate may consider as early as Wednesday or Thursday of this week, S. 240, the "Private Securities Litigation Reform Act of 1995." On behalf of the North American Securities Administrators Association (NASAA), we are writing today to express the Association's opposition to S. 240 as it was reported out of the Banking Committee. In the U.S., NASAA is the national voice of the 50 state securities agencies responsible for investor protection and the efficient functioning of the capital markets at the grassroots level.

While everyone agrees on the need for changes to the current securities litigation system, not everyone is prepared to deny justice to defrauded investors in the name of such reform. Proponents of the bill make two claims: first, that they have modified the bill to satisfy many of the objections to the earlier version; and second, that the bill will not prevent meritorious claims from going forward. Neither claim is accurate. First, the changes made to the bill do little to resolve the serious objections to S. 240 raised by NASAA and its members. In fact, it may be argued that during the Banking Committee's deliberations the bill was made less acceptable from the perspective of investors. Second, it is NASAA's view that the

bill succeeds in curbing frivolous lawsuits only by making it equally difficult to pursue rightful claims against those who commit securities fraud.

The reality is that the major provisions of S. 240 will work to shield even the most egregious wrongdoers among public companies, brokerage firms, accountants and others from legitimate lawsuits brought by defrauded investors. Do we really want to erect protective barriers around future wrongdoers?

NASAA agrees that there is room for constructive improvement in the federal securities litigation process. The Association supports reform measures that achieve a balance between protecting the rights of defrauded investors and providing relief to honest companies and professionals who may unfairly find themselves the targets of frivolous lawsuits. Regrettably, S. 240 as approved by the Senate Banking Committee fails to achieve this necessary balance.

Although this bill has been characterized in some quarters as an attempt to improve the cause of defrauded investors in legitimate lawsuits, that simply is not the case. Attempts to incorporate into the bill provisions that would work to the benefit of defrauded investors were rejected when the Banking Committee considered the bill. At the same time, the few provisions in the original bill that may have worked to the benefit of defrauded investors were deleted.

For example, during the Committee's deliberations: (1) the rather modest extension of the statute of limitations for securities fraud suits contained in the original version was deleted; (2) attempts to fully restore aiding and abetting liability under the securities laws were rejected; (3) a regulatory safe harbor for forward-looking statements contained in the original version of S. 240 was replaced with an overly broad safe harbor for such information, making it extremely difficult to sue when misleading information causes investors to suffer losses; and (4) efforts to loosen the strict limitations on the applicability of joint and several liability were rejected, making it all but impossible for more than a very few to ever fully recover their losses when they are defrauded. The truth here is that this is a one-sided measure that will benefit corporate interests at the expense of investors.

As state government officials responsible for administering the securities laws in our jurisdictions, we know the important role private actions play in the enforcement of our securities laws and in protecting the honesty and integrity of our capital markets. The strength and stability of our nation's securities markets depend in large measure on investor confidence in the fairness and integrity of these markets. In order to maintain this confidence, it is critical that investors have effective remedies against persons who violate the anti-fraud provisions of the securities laws.

When S. 240 is considered on the Senate floor, it is expected that several pro-investor amendments will be offered in an attempt to inject some balance into the measure. Among the amendments we expect to be offered are those that would: (1) extend the statute of limitations for private securities fraud actions; (2) fully restore aiding and abetting liability under the securities laws; (3) replace the expansive safe harbor for forward-looking statements with a directive to the Securities and Exchange Commission to continue its rulemaking efforts and report back to Congress; and (4) lift the severe limitations on joint and several liability so that defrauded investors may fully recover their losses.

On behalf of NASAA, we respectfully encourage you to vote in favor of all such

amendments when they are offered on the Senate floor. If all four amendments are not adopted, we respectfully encourage you to oppose S. 240 on final passage.

NASAA regrets that the Association cannot support the litigation reform proposed as reported out of the Senate Banking Committee. The Association believes that this issue is an important one and one that should be addressed by Congress. However, NASAA believes that is more important to get it done right than it is to get it done quickly. S. 240 as it was reported out of the Banking Committee should be rejected and more carefully-crafted and balanced legislation should be adopted in its place.

If you have any questions about NASAA's position on this issue, please contact Maureen Thompson, NASAA's legislative adviser.

Sincerely,

PHILIP A. FEIGN,
Securities Commissioner, Colorado Division of Securities, President, North American Securities Association.

MARK J. GRIFFIN,
Director, Utah Securities Division, Chairman, Securities Litigation Reform Task Force of the North American Securities Administrators Association.

AMERICAN COUNCIL ON EDUCATION,
CALIFORNIA LABOR FEDERATION—
AFL-CIO, CONGRESS OF CALIFORNIA SENIORS—LA COUNTRY,
CONSUMER FEDERATION OF AMERICA,
CONSUMERS FOR CIVIL JUSTICE,
INTERNATIONAL BROTHERHOOD OF TEAMSTERS,
GOVERNMENT FINANCE OFFICERS ASSOCIATION,
GRAY PANTHERS, NATIONAL LEAGUE OF CITIES,
NEW YORK STATE COUNCIL OF SENIOR CITIZENS,
NORTH AMERICAN SECURITIES ADMINISTRATORS ASSOCIATION,
U.S. PUBLIC INTEREST RESEARCH GROUP,

May 23, 1995.

Re: securities litigation reform.

Hon. ALFONSE D'AMATO,
Chairman, Committee on Banking, Housing and Urban Affairs, U.S. Senate, Dirksen Senate Office Building, Washington, DC.

DEAR CHAIRMAN D'AMATO: Our organizations have been actively involved in the securities litigation reform debate. We are writing today to express the very serious concerns our organizations and individual members have with the major provisions of S. 240, the "Private Securities Litigation Reform Act," introduced by Senators Dodd and Domenici, and with the substitute language that emerged on Monday.

Let us be clear: our organizations strongly believe that any securities litigation reform must achieve a balance between protecting the rights of defrauded investors and providing relief to honest companies and professionals who may find themselves the target of a frivolous lawsuit. We agree that abusive practices should be deterred, and where appropriate, sternly sanctioned. At the same time, the doorway to the American system of civil justice must remain open for those investors who believe they have been defrauded.

Although we understand that some of the specifics of S. 240 remain under discussion,

we are extremely disappointed to see that the substitute language now being circulated (and expected to be marked up on Thursday, May 25th) has not moved at all in the direction of achieving the balance we believe is so critical to resolving this debate. While we appreciate the fact that some of the provisions we found most objectionable in the bill as introduced were deleted, we are dismayed to find other equally troubling provisions inserted in the new draft. Perhaps most disturbing is that the one pro-investor provision found in S. 240 as introduced—the extension of the statute of limitations—has been dropped entirely in the latest version of the bill.

Collectively, our organizations and those with which we have worked closely on this issue represent tens of millions of ordinary Americans who increasingly must rely on investments to build retirement nest eggs, finance the college education of children, and to save for major purchases, such as a home. The organizations represent the thousands of state and local governments, that participate in the securities markets both as investors of pension funds and temporary cash balances and as issuers of municipal debt. Our ranks also include colleges and universities and other institutions of higher learning, as well as labor organizations, that participate in the securities markets as investors of endowment and pension funds.

Our general and primary concerns with respect to the provisions of S. 240, as well as with other proposals that now are under discussion or are present in the House version of this legislation, include:

Unreasonable standards for fraud pleadings, burden of proof and damages;

Any form of "means testing" for access to justice of recovery, including conferring a special status on certain, larger investors;

Limits on joint and several liability that will work to immunize from liability certain professional groups;

"Loser pays" rules;

Expansive safe harbor exemptions from private liability for forward looking statements (we believe the more appropriate response is SEC rulemaking in this area); and

Expanding the scope of this bill to go beyond cases involving private class actions brought under the 1934 Securities Exchange Act.

At the same time, we have expressed support for major reform proposals, including:

An early evaluation procedure designed to weed out clearly frivolous cases, with sanctions imposed in certain instances;

A more rational system of determining liability based on proportionate liability for reckless violators and joint and several liability for knowing violators, with provisions made for special circumstances in which knowing securities violators are unable to satisfy a judgment;

The right to contribute among liable defendants according to proportionate responsibility.

Certification of complaints and improved case management procedures;

Improved disclosure of settlement terms;

Curbs on potentially abusive practices on the part of plaintiffs' attorneys;

A reasonable extension of the statute of limitations for securities fraud suits; and

Restoration of liability for aiding and abetting securities fraud.

Although some people may mistakenly believe that the markets run on money, the truth is that the markets run on public confidence. As investors ourselves and as representatives of investors, we can tell you that the confidence we have in the marketplace will be dramatically altered if we come to believe that not only are we at risk of being defrauded, but that we will have no re-

course to fight back against those who have victimized us. We fear that is exactly what will be the case if S. 240 or its substitute version is enacted. There should be little doubt that under such a scenario many investors will seriously reconsider whether they want to remain in the marketplace.

Finally, we want to take this opportunity to put to rest the frequently voiced claim that no defrauded investor with a meritorious case will be denied justice under these reform proposals. That is just plainly and demonstrably untrue.

Any questions about this letter should be directed to any of the contacts listed below:

Contacts;

American Council on Education: Shelly Steinbach.

CA Labor Federation—AFL-CIO: Bill Price.

Congress of CA Seniors—LA County: Max Turchen.

Consumer Federation of America: Mern Horan.

Consumers of Civil Justice: Walter Fields.

International Brotherhood of Teamsters: Bart Naylor.

Government Finance Officers Association: Cathy Spain.

Gray Panthers: Dixie Horning.

National League of Cities: Frank Shafroth.

New York State Council of Senior Citizens: Eleanor Litwak.

North American Securities Administrators Association: Maureen Thompson.

U.S. Public Interest Research Group: Ed Mierzwinski.

— MAY 24, 1995.

Re oppose S. 240—devastating for consumers, seniors, investors.

Hon. PAUL S. SARBANES,
Senate Committee on Banking, Housing, and Urban Affairs, Hart Senate Office Building, Washington, DC.

DEAR SENATOR SARBANES: We are writing to express our strong opposition to S. 240, the so-called "Private Securities Litigation Reform Act." In our earlier analysis of the bill (January 25, 1995), we discussed the eight most harmful provisions for consumers, seniors, and investors. We stressed that S. 240 would effectively eliminate private enforcement of the securities law and greatly reduce the likelihood that innocent victims of fraud could recover their losses from corporate and individual wrongdoers.

Now that the Banking Committee's substitute has been issued in preparation for the markup on Thursday, May 25, we are deeply concerned that the bill has not moved in the direction of balanced reform. On the whole, the bill is now even worse for average Americans. The intentions of the Senate Banking Committee's substitute bill are clear—to promote the interests of big corporations, big accounting firms, big brokerage firms and big investment banking houses at the expense of average Americans. The bill is now entirely anti-consumer, anti-senior, anti-investor, and pro-defendant, pro-industry, and pro-wealthy. Any pretensions of protecting small investors and meritorious fraud actions have been abandoned.

Only one of our concerns (the insider-dominated disciplinary board for accountants) has been addressed, while seven deeply troubling provisions remain or have gotten even worse. We have attached a consumer critique of the Banking Committee's substitute which explains our strong opposition, as well as a recent article which highlights the urgency of our concerns.

S. 240 strikes a blow to the heart of the middle class and average, hard-working Americans who depend on the federal securities system to protect their savings, invest-

ments, and retirements. A study published in the 1991 Maine Law Review found that 87% of managers surveyed were willing to commit financial statement fraud, more than 50% were willing to overstate assets, 48% were willing to understate loss reserves, and 38% would "pad" a government contract. In addition, securities fraud is increasing at an alarming rate. Cases brought by federal and state regulators have increased by more than 45% in just five years.

Moreover, a new major financial fraud that could rival the savings and loan fiasco—involving high-risk, highly speculative derivative securities—is just being discovered. Orange County is not alone. Already, 40 American communities and public institutions across the country have reported derivatives losses totalling some \$3 billion. And indications are that fraud may have played a large role in many of those disasters.

Clearly, this is no time to be immunizing fraud and removing vital investor protection laws that have served American consumers so well for decades. We urge you to vote against S. 240 in the markup on Thursday.

Sincerely,

RICHARD VUERNICK,
*Legal Policy Director,
Citizen Action.*

MERN HORAN,
*Legislative Representative,
Consumer Federation of America.*

MARY GRIFFIN,
Counsel, Consumers Union.

JOAN CLAYBROOK,
President, Public Citizen.

EDMUND MIERZWINSKI,
Consumer Program Director, U.S. Public Interest Research Group.

M. KRISTEN RAND,
Director of Federal Policy, Violence Policy Center.

Attachment.

[From the New York Times, May 22, 1995]

FRIENDS OF FRAUD?

(By Anthony Lewis)

Of all the bills making their way through this Congress, the most devastating to its area of the law may be one that has had relatively little attention: legislation to weaken the protection of the public against securities fraud.

The House passed a bill in March. Now the Senate Banking Committee is working on its version. To judge how devastating the legislation would be, consider what it would have done to some of the most notorious recent fraud cases.

In the 1980's Prudential Securities brokers lure customers to invest in risky securities with deliberately false statements about how much they would make. The defrauded investors and the Securities and Exchange Commission sue Prudential Securities, and in the S.E.C. case alone the firm agreed to repay more than \$700 million to the victims.

The victims would probably have been unable to sue if one section of the current House bill had been law. Known as the "safe harbor" provision, it immunizes from suits by the defrauded all "forward-looking statements" about securities. Companies and their agents could make false "projections" and "estimates" of future performance, even if they were deliberate lies, without fear of lawsuits by those defrauded.

The chairman of the S.E.C., Arthur Levitt Jr., is concerned about the "safe harbor" provision. He has just written to the Senate

committee urging it not thus to protect "purposefully fraudulent" financial predictions.

That is not the only part of the pending legislation that would make it difficult—perhaps impossible—for victims of fraud to sue. Another is a provision of the House bill requiring anyone who brings a securities fraud suit to show at once, when he or she sues, the state of mind of the defendant indicating fraudulent intent. That kind of information is usually found only during the discovery phase of a case.

For example, two months ago shareholders in Koger Properties Inc. won an \$81.3 million judgment in a fraud suit against its accounting firm, Deloitte & Touche. During pretrial discovery, the plaintiffs' lawyers found that the partner in charge of the audit owned stock in Koger, a violation of accounting standards. They could not have known that when they sued.

Still another provision of the House bill, and the Senate's as it stands, would limit what is called "joint and several liabilities." That allows the victims of fraud to recover from others involved if the principal fraud perpetrator is not able to pay.

Last month, for example, Steven Hoffenberg of Towers Financial Corporation pleaded guilty to securities fraud and criminal conspiracy in a Ponzi scheme that cost investors \$460 million. He said his accountants and lawyers helped carry out the fraud by issuing false financial statements and making misleading statements to the S.E.C. Towers is bankrupt, so the victims are suing the lawyers and accountants.

Some of the worst scams in recent history would have left the defrauded investors with little or no recourse if the "joint and several liability" limit had been in effect. The victims of Charles Keating, the great savings and loan swindler, would have been out of luck when he went to prison and said he was broke.

The legislation sounds highly specialized, and it is. But it would have widespread effects on real people. In addition to individual investors who have been defrauded, many local governments have lost large sums in recent years and are suing brokerage firms and others. The big example is Orange County, California, which lost more than \$1 billion, but there are dozens more.

It is a peculiar time to weaken legal protections: a time of spectacular financial frauds. The latest involves the Foundation for New Era Philanthropy, whose scam attracted many charities and such investors as Lawrence S. Rockefeller and William E. Simon. New Era collapsed last week, and the S.E.C. charged its founder with "massive" securities fraud.

But this Congress evidently does not care a lot about the victims of fraud. It is listening to the lobbyists for accounting firms and insurance companies, whose political action committees have made large campaign contributions, and others who want to operate without fear of being sued for securities fraud.

CONSUMERS UNION, CONSUMER FEDERATION OF AMERICA, U.S. PUBLIC INTEREST RESEARCH GROUP, CITIZEN ACTION, PUBLIC CITIZEN, VIOLENCE POLICY CENTER

CONSUMER CRITIQUE OF S. 240 "PRIVATE SECURITIES LITIGATION REFORM ACT"

(1) Abrogation of joint and several liability, which would effectively immunize professional wrongdoers. The original S. 240 eliminated joint and several liability in a wide class of cases, favoring large corporations, accountants, brokers and bankers—who have been found liable—over defrauded

victims. The substitute S. 240 restricts joint and several liability even further.

Under joint and several liability, if one wrongdoer is found liable but has no assets, the victim can be reimbursed fully by the other wrongdoers, without whose assistance the fraud could not have succeeded. This traditional aspect of America's legal system for fraud is based on the policy that it is more fair for other wrongdoers to pay for a loss that cannot be collected from one of the co-conspirators than it is for the victims to go uncompensated. The rule has enabled swindled consumers to recover full damages from accountants, brokers, bankers, lawyers and other wrongdoers who participate in securities scams, even when the primary wrongdoer has no assets left, has fled, or is in jail.

The original S. 240 sharply limited this rule, immunizing reckless wrongdoers from joint and several liability. If S. 240 had been in effect, most investors would not have recovered their life savings in the Charles Keating/Lincoln Savings & Loan debacle. Although Keating had become bankrupt, the victims recovered their damages from the accountants, bankers, and lawyers who assisted Keating. Despite extensive testimony to Congress that restricting joint and several liability will reduce recoveries for defrauded victims and encourage more fraud, the substitute bill restricts joint and several liability even further.

Under the substitute, in the all-too-often cases where a knowing violator's share is uncollectible, the liability of reckless violators for the uncollectible share would be subject to a lower "cap" than under the original bill. The rest of the uncollectible share simply will be lost to the defrauded victims. Although the "cap" would not apply to victims with a net worth over \$200,000 and recoverable damages of more than 10% of their net worth, that basically eliminates anyone who owns a house.

Adjudged perpetrators of securities fraud are given a gift while fraud victims are denied full recover of the money that was stolen from them—that is the policy of S. 240. Under the substitute, it will be virtually impossible for many victims of fraud to recover a large part of their losses.

(2) Failure to restore the liability of those who aid and abet fraud. The original S. 240 failed to restore aiding and abetting liability for accountants, lawyers, brokers, bankers and others who assist primary wrongdoers in committing securities fraud. The substitute also fails to do so.

Last year, in the Central Bank of Denver case, the Supreme Court overturned in a 5-4 ruling 25 years of established precedent (including all 11 federal appellate courts that addressed the issue) by wiping out aiding and abetting liability of accountants, lawyers, brokers, bankers and others who assist primary wrongdoers in committing securities fraud. This right of action has played a vital role in compensating swindled consumers in the major financial frauds of the last several decades and must be restored by Congress. Central Bank severely weakens the deterrence of securities fraud because it sends a dangerous signal to the markets that a primary enforcement tool has been eliminated. That not only hurts defrauded consumers, it hurts all Americans. S. 240 fails to address this issue for obvious reasons—the entire thrust of the bill is to further immunize defendants from liability.

In their Congressional testimony, the Securities and Exchange Commission ("SEC") and state regulators recommended restoring aiding and abetting liability. Even Senator Dodd has stressed the importance of restoring the liability of those who aid and abet securities fraud. During a May 12, 1994 hearing before the Senate Subcommittee on Securi-

ties, Senator Dodd stated "Lawyers, accountants, and other professionals should not get off the hook, in my view, when they assist their clients in committing fraud . . . The Supreme Court has laid down a gauntlet for Congress . . . In my view, we need to respond to the Supreme Court decision promptly and I emphasize promptly."

(3) Discrimination against small shareholders. The original S. 240 contained a blatantly discriminatory wealth-test for filing securities fraud class actions. The substitute replaces the wealthiest with an equally discriminatory wealth-control provision.

The substitute adds a new provision that sets up a strong presumption that the "most adequate plaintiff" in any private class action is the plaintiff that has the largest financial interest in the outcome of the action. The bill then grants this "most adequate plaintiff" the power to select the lead counsel and control the case, including settling for any amount or even dismissing the case.

Perhaps no other change to S. 240 makes plainer the real motives behind the bill and makes hollower any pretensions to protect meritorious fraud actions. This "most affluent plaintiff" requirement would have a devastating effect on average consumers who are defrauded in the securities markets. Mutual funds and large investors, who may have close ties to big corporate fraud defendants (e.g., mutual fund managers enjoy ready access to information from corporate managers) and who may care less about full recovery because its loss reflects a smaller proportion of total investment than smaller investors' losses, can afford to accept less than full recoveries, would have complete control over class actions at the expense of average investors. What makes a mutual fund that has lost \$1 million of its \$1 billion portfolio more adequate to represent a class of defrauded investors than an elderly widow who has lost \$27,000 out of her \$30,000 net worth?

Aside from raising the specter of collusive intervention by large investors simply to dismiss cases or enter into sweetheart settlements, the substitute virtually precludes small investors from being able to obtain attorneys willing to invest their time on cases in which they can have no control and may not be paid fairly (or at all) by lead counsel.

This provision also directly contradicts the primary rationale for class actions—to give average investors who cannot afford to litigate against major corporate defendants on their own a means by which they could band together to seek a remedy for their losses.

(4) Inadequate efforts to deal with unwarranted secrecy. As we outlined in our January letter, the original S. 240 made no effort to address the serious problem of defendant-coerced secrecy orders covering all the underlying documents relevant to the fraud. These orders remain in effect throughout the litigation and generally require that, once a case is terminated, the documents be destroyed or returned to the defendants. Such secrecy orders block significant corporate wrongdoing from public scrutiny and allow defendants, at the time of settlement, to proclaim their innocence without fear of contradiction. The substitute continues to ignore this problem, further demonstrating that the bill is not really intended to solve the real problems in securities litigation.

(5) Imposition of "loser pays" fee shifting. The original S. 240 abrogated a 200-year-old legal principle reflecting our national policy in favor of access to justice. It did so by requiring losing parties who decline to accept out-of-court resolution of their cases to pay all of the prevailing parties' legal fees and costs.

The substitute simply replaces this "loser pays" rule with a different "loser pays"

rule—mandatory sanctions under Rule 11 of the Federal Rules of Civil Procedure which includes a strong presumption in favor of shifting all legal fees and costs to the loser. The new provision suffers from the same flaw as the original—average consumers who have just lost their retirement savings in a financial fraud cannot afford to take the risk that they might lose their house as well if they lose their case. Moreover, the new rule would prolong cases, waste more resources on litigating additional issues, and add to the money spent on legal fees by requiring the court to make specific findings regarding compliance by every party and every attorney, even when no party requests it.

The end result of this “loser pays” rule will be a severe chill on the assertion of securities fraud claims, regardless of their merits.

(6) Free reign for false statements. The original S. 240 allowed the SEC to consider creating a safe harbor exemption for corporate predictive statements—the substitute creates a “safe ocean” exemption from fraud liability for corporate predictions that essentially grants would-be wrongdoers a license to lie. The substitute adopts a wholesale exemption which would completely immunize a vast amount of corporate information (“any statement, whether made orally or in writing, that projects, estimates, or describes future events”) so long as it is called a forward-looking statement and states that it is uncertain and may not occur, even if they are made with reckless disregard for their accuracy. This is a gaping loophole through which wrongdoers could escape liability while fraud victims would be denied recovery.

Corporate “forward-looking statements” are prone to fraud as they are an easy way to make exaggerated claims of favorable developments in order to attract cash. They continue to be a favorite tool of con artists, promoters and illegal insider traders to artificially pump up the price of public company stock in order to profit at investors’ expense. The substitute’s safe harbor provision creates an incentive to provide bad information to consumers and a disincentive to provide the best available information. It would effect an upheaval in the mandatory corporate disclosure system in the United States, with immense potential adverse market consequences.

Finally, by itself, the safe harbor would eliminate many, if not most, fraud class actions. The safe harbor provision would require, with limited exemptions, that every class action member prove actual knowledge of and reliance on the fraudulent statement, an (almost) impossible requirement in class action suits. Under this provision, even purposefully fraudulent forward-looking statements could be made without the possibility of redress through a class action lawsuit.

The SEC is currently in the middle of a rulemaking proceeding to study forward-looking statements and has requested that Congress allow it to complete its process. We believe that Congress should defer establishing a safe harbor provision until the agency experts have thoroughly reviewed this matter.

(7) A flawed limitations period. The current statute of limitations—1 year from discovery of the fraud but in no event more than 3 years after the fraud—is generally regarded as too short. The original S. 240 extended the period to 2 years after the violation was or should have been discovered but not more than 5 years after the fraud. Rather than heed the SEC and the state securities regulators, who testified that the limitations period should be even longer, the substitute simply drops the extension entirely. There is now not a single provision in the bill that

would increase recoveries for fraud victims—it is totally one-sided and should really be called the “Wrongdoer Protection Act of 1995.”

(8) An insider-dominated disciplinary board for accountants. The substitute deletes the provision of the bill that would have allowed the trade association for the accountants—the AICPA—to be a sham self-disciplinary board for public accountants. This is the only one of our original concerns that has been adequately addressed by the substitute bill.

[From the Washington Post, June 18, 1995]

MAKING IT EASIER TO MISLEAD INVESTORS

(By Jane Bryant Quinn)

A lawsuit-protection bill speeding through Congress will give freer rein to Wall Street’s eternal desire to hype stocks.

It’s cast as a law against frivolous lawsuits that unfairly torture corporations and their accountants. But the versions in both the House and Senate do far more than that. They effectively make it easier for corporations and stockbrokers to mislead investors. Class action suits against the deceivers would be costly for small investors to file and incredibly difficult to win.

I’m against frivolous lawsuits. Who isn’t? But these bills would choke meritorious lawsuits, too. They affect only claims filed in federal court, so bilked investors would still have the option of seeking justice in a state courts. But the federal law would set a terrible precedent and leave the markets more open to fraud.

The congressional proposals started out as a way of protecting companies against so-called strike suits—lawsuits filed against companies whose stock price unexpectedly plunges.

The companies complain that “vulture lawyers” lie in wait for these drops in price. When they occur, the lawyers find willing plaintiff and immediately file suit. The usual charge: that the firm, its executives and accountants misled investors with falsely optimistic statements. That’s not true, the companies say, but they tend to settle just to avoid the legal expense. If so, this represents a grave cost—on corporations, shareholders and economic efficiency.

But are strike suits really overwhelming corporations? There’s evidence on both sides of this issue, but most of it fails to document the executives’ broad complaints.

As an example, take the new study by Baruch Lev, a professor at the University of California at Berkeley. He looked at public companies whose share price fell more than 20 percent in the five days around the time of a disappointing quarterly earnings report. There were 589 such cases, from 1988 through 1990. But related class action suits were filed against only 20 of the firms.

Lev compared those 20 companies with similar firms where no lawsuits were filed. Among other things, the litigated companies tended to put out rosy statements—in some cases, just before releasing the bad earnings report. By contrast, the firms that weren’t sued tended to publish more sober statements and to warn investors in advance that earnings would be lower than expected.

Lev warns that his sample is too small to reach statistical conclusions. But his basic data undermine the claims that companies are bombarded with lawsuits whenever their stock goes down.

The new bills contain many provisions to worry investors. For example, if you lost a class action suit, you might have to pay the legal fees for the other side. Psychologically, that could stop you from suing no matter how badly you’d been burned.

The bills also give excessive protection to so-called forward statements, which are the business projections that corporations make.

Under current law, it’s all right to make a reasonable projection, even if it doesn’t come true. But a company can be held liable for making an unreasonable projection that misleads investors. In many of the cases where lawsuits are brought, “executives are telling the public that everything is going to be great while they’re bailing out and selling their own stock,” Jonathan Cuneo, general counsel of the National Association of Securities and Commercial Law Attorneys, told my associate Louise Nameth.

If these bills become law, however, companies could get away with making misleading, even reckless statements. To win a class action lawsuit, you would have to prove that a falsehood was uttered with a clear intent to deceive. That’s incredibly tough to do.

This provision, in particular, troubles Arthur Levitt Jr., chairman of the Securities and Exchange Commission. “The law should not protect persons who make material statements they know to be false or misleading,” he says, “nor should it protect offerings such as penny stocks, nor persons who have committed fraud in the past.”

Baseless lawsuits do indeed exist. Lawyers may earn too much from a suit, leaving defrauded investors too little. The incentives to sue should be reduced. But not with these bills. They’d let too many crooks get away.

[From U.S. News & World Report, June 26, 1995]

WILL CONGRESS CONDONE FRAUD?

(By Jack Egan)

Some of the most unpopular people in Washington these days are shareholders’ lawyers who sue companies at the drop of a stock, usually claiming that management deceived investors about the outlook and is liable for losses when shares fall.

Lawmakers have concluded—without much supporting evidence—that this happens far too frequently, hamstringing corporations and causing executives to be wary of making forecasts. And so legislation is zipping through Congress to curb “frivolous” or “speculative” lawsuits against public companies. The high-sounding Private Securities Litigation Reform Act of 1995 easily passed the House in March. It was approved by the Senate’s banking panel and will soon be taken up by the full body.

It just might come to be remembered as legislation that steeply tilted the playing field against investors. The bill may make executives feel easier about discussing what they see ahead, with shareholders benefiting from more candid disclosure. But it makes it very hard for shareholders to sue over legitimate grievances. The House version even protects management when it lies, provided the deception is a projection.

Unhappy Levitt. The Securities and Exchange Commission, which has always viewed private actions as complementing its own limited enforcement abilities, is not happy. In a letter to Senate Banking Committee Chairman Alfonse D’Amato sympathizing with “the punishing costs of meritless lawsuits,” SEC Chairman Arthur Levitt also wrote that the House-passed bill might “compromise investor protection.” And while the Senate Banking Committee’s bill is more moderate, the SEC chairman complained in another letter that shareholders were still hampered from bringing suits against “all but the most obvious frauds.”

The crusade to throttle shareholder lawsuits has been spearheaded by high-tech companies and the big accounting firms. The stocks of technology companies tend to be quite volatile, flying high and suddenly nose-

diving, often when companies fail to meet ambitious earnings expectations. That makes them especially vulnerable to mugging by lawsuit; according to the American Electronics Association, which represents the industry, 9 out of 10 suits are settled out of court—averaging \$8.6 million—simply to avoid the cost of lengthier litigation.

But claims that nuisance lawsuits are hurting the ability of such companies to raise capital come at a time when technology shares have led the stock market to an all-time high and initial public offerings are running at record levels. "There are 200 to 300 companies sued each year out of 20,000 that are registered," notes Democratic Sen. Richard Bryan of Nevada—about the same as 20 years ago. "I also oppose frivolous lawsuits, but that issue is really a trojan horse for firms that simply want to limit their liability."

The accounting firms felt stung by large liability verdicts against them in connection with the S&L scandal of the early 1990s. But the cases that produced the biggest judgments were brought not by individual shareholders but by the federal government, seeking to recoup its depleted S&L insurance fund. Nevertheless, the "Big Six" are eagerly backing the bill because it would bar shareholders from suing outsiders who are parties to securities fraud—like accountants.

When the full Senate debates the bill, perhaps at the end of June, efforts may be made to make it less hostile to shareholders and to deal with some of the SEC's objections. The Clinton administration has yet to weight in. But a veto threat from the president would be risky, since the lopsided vote in the House is enough for an override.

Shareholders already are barred from suing brokerages and must arbitrate instead. "The pendulum had swung too far toward the lawyers, and now it's swinging too far the other way," notes Richard Kraut, an attorney with Washington-based Storch & Brenner, which specializes in securities law. "Unfortunately, some major investor frauds may have to take place before it again moves back toward the center."

[From the St. Louis (MO) Post-Dispatch,
May 9, 1995]

DON'T PROTECT SECURITIES FRAUD

The House has passed and the Senate is considering a bill to make it much harder for defrauded investors to bring class-action suits against investment firms that defraud them, as well as the accountants who helped them. The impetus for such legislation is the same as that driving tort revision, only with even less justification.

The Senate bill is sponsored by New Mexico Republican Pete Domenici and, surprisingly, Christopher Dodd, Democrat of Connecticut. Though its final provisions have yet to be settled, it is likely to restrict significantly the rights of small investors to sue for fraud.

The industry's complaint: The explosion of securities litigation needs to be curbed. But there isn't one; the number of suits has remained nearly constant in the last 20 years, despite huge growth in the volume of securities. However, recent events have created a new problem: Many accounting firms that put their names to false documents during the junk bond craze and the thrift debacle are finding themselves in court more often than ever before. They want protection. This bill would give it to them.

It would prohibit lawyers and accountants from being named as primary defendants in a class action unless the plaintiffs first can show that these defendants had actual knowledge of the fraud and the precise state of mind of those they helped perpetrate it.

That can only be done by the discovery process in a lawsuit, not beforehand. The bill would also bar any plaintiff from suing who had less than 1 percent or \$10,000 invested in the securities in question. This will keep a lot of people out of court.

When they do get in, if they lose, they will be responsible for court costs if they have holdings of more than very limited size, clearly a deterrent to small-investor suits for securities fraud.

These are just the highlights of a complex bill whose provisions work against not only the rights of small investors, but even large government bodies, such as Orange County or the city of Joplin, Mo., which lost huge amounts on derivatives that may have been sold to them without full disclosure.

Among those senators on the Banking Committee who are in a position to slow down the bill is Missouri's Christopher S. Bond. He should do so. His new colleague from Missouri, John Ashcroft, who has yet to take a position on the bill, should join him.

[From the Los Angeles (CA) Times, Mar. 12,
1995]

THIS ISN'T REFORM—IT'S A STEAMROLLER: GOP BILL CURBING LAWSUITS WOULD FLATTEN THE SMALL INVESTOR

Once again House Republicans have put the timetable for their "contract with America" ahead of the substance of the bills they are ramming through the lower chamber. On Wednesday the House approved a drastic revision of the nation's securities laws as part of the GOP's agenda for legal reform. The proposed Securities Litigation Reform Act, which is a key provision in the "contract," would sharply curb the ability of investors and shareholders to sue stockbrokers, accounting firms and companies for fraud.

The measure, authored by Rep. Christopher Cox (R-Newport Beach), simply goes too far. It is one thing to craft legislation directed at curbing specific abuses of securities litigation, but the House measure would amount to a wholesale dismantling of the system that enables investors and shareholders to seek redress for financial fraud.

Opponents, including state securities administrators as well as consumer groups, maintain that the bill would virtually destroy the ability of citizens of modest means to sue when they are victims of fraud. Arthur Levitt Jr., the chairman of the Securities and Exchange Commission, who has worked to improve investor protections, has reservations about the measure. So has U.S. Atty. Gen. Janet Reno. Small wonder.

The proposed law would tilt the legal system in favor of corporations and their accounting firms, lawyers and investment firms by making it too easy for them to defend themselves against shareholder suits.

What might such a law portend for cases like Orange County? County officials are seeking legal recourse against Merrill Lynch Co., which sold high-risk securities to the county's ill-fated investment pool, ultimately triggering its bankruptcy. The fear is that the proposed law could be interpreted by the courts in ways that would work against plaintiffs in cases like this one.

Under the House bill, a judge could require the losers in a securities fraud case to pay the legal expenses of the winner if the judge determined that the investors' complaint did not originally possess substantial merit. Currently there is no "loser pays" general provision. The proposed law also would demand that the plaintiff show that the company or its officials acted knowingly and recklessly in committing the fraud. The current standards are simpler: They allow investors to sue for fraud if a company withholds information or issues misleading information that affects the market price.

Between these two standards there perhaps is a sensible middle ground—but that's not to be found in the House bill.

Cox casts his bill as a limitation against so-called "strike suits," brought by shareholders who file lawsuits when the share price drops in a company in which they own a small part of the stock. The congressman likes to point out that high-technology companies are a favorite target of such lawsuits. Abuses of such lawsuits absolutely do exist and should certainly be curbed, but the House bill, as drawn, is overly broad in its potential application.

The Senate will take up the securities reform bill soon. We urge it to take a reasoned approach to the problems posed by frivolous securities lawsuits. The current House bill is not the answer.

[From the Philadelphia (PA) Inquirer, June
4, 1995]

GOING EASY ON CROOKS IN 3-PIECE SUITS (By Jeff Brown)

True or false: Republicans are the law-and-order people who want to see more crooks go to jail and stay there longer?

True—unless the crook wears a three-piece suit instead of a ski mask. Corporate executives, accountants, securities industry pooh-bahs—they need special protection against claims they're thieves.

This, in a nutshell, is the point of the Private Securities Litigation Reform Act of 1995, approved, 11 to 4, by the Senate Banking Committee on May 24 and likely to reach the Senate floor this month. It's meant to discourage "frivolous" claims. But what about legitimate ones?

Unlike a similar House bill passed in March, the version sponsored by Sen. Alfonse D'Amato (R., N.Y.), the committee chairman, doesn't include a sweeping requirement that the loser in a stock-fraud case pay the winner's legal fees. But a trial judge could implement "loser pays" by finding the plaintiff had engaged in "abusive litigation."

Loser pays could deter stockholders from filing legitimate lawsuits by making it too risky to challenge rich corporations.

The D'Amato bill has other flaws as well, says Securities and Exchange Commission Chairman Arthur Levitt. "Willful fraud" would be made easier by a "safe harbor" provision, he says, because executives would be overly protected from lawsuits regarding misleading projections about a company's performance.

Stock frauds usually use bloated financial projections to entice investors. D'Amato would require a new, higher level of proof—essentially, that a company intended to mislead, giving defrauded investors the nearly insurmountable task of establishing a corporate executive's state of mind. An executive could make virtually any projection, then insulate himself against a fraud verdict by adding that things might not turn out that way.

The bill has some good provisions to protect investors joining in a class action from abuse by their own attorneys, and it would ensure that plaintiffs are illegitimate victims and not stooges for ambulance-chasers.

But federal court figures don't support Republican claims there's a flood of frivolous suits. There are only a few hundred class-action securities cases filed a year, while there are more than 14,000 public companies. And, of course, many securities suits are legitimate—just ask the victims in the Crazy Eddie or Lincoln Savings & Loan cases. Class actions are the cheapest way for small investors to fight abuses by well-heeled corporations.

SEC lawyers say most people who commit stock fraud could be charged with criminal

violations that carry prison terms. But they aren't because in criminal cases, prosecutors need proof beyond a reasonable doubt. So most stock-fraud cases, which are tough for jurors to grasp, go to civil court, where only a preponderance of evidence is required.

Still, a crook is a crook, whether he burgled your home or lied to sell you stocks at an inflated price. And the D'Amato bill would relax the penalties for many stock crooks.

It would scrap rules that make each participant in a fraud liable for the entire sum—ordered returned to investors or paid in fines. Under the current "joint and several" liability rules if one defendant can't come up with his share, the others have to pay it.

Instead, D'Amato would establish "proportional liability," in which, with few exceptions, each defendant would pay a percentage of the penalty equal to his share of guilt, as determined at trial. Thus, if the defendant who owes 80 percent is bankrupt, the defrauded investors would be unable to recover most of what they are owed, even if another defendant has the money.

This provision was aggressively sought by the accounting profession after some firms were assessed hefty penalties for S&L frauds.

Proportional liability is like letting the getaway driver off with a speeding ticket if he didn't intend for his partner to shoot the bank teller. It protects the partially guilty at the expense of the investor who is completely innocent.

Surely, most corporate executives are honest. But since there's little evidence that frivolous lawsuits are a real problem, it looks as if business groups seek "reform" *legitimat* lawsuits.

A cynic could guess what goes through their minds when they see a thief in a three-piece suit held to account:

"There, but for the grace of God, go I.

Mr. FAIRCLOTH addressed the Chair.

The PRESIDING OFFICER. The Senator from North Carolina.

Mr. FAIRCLOTH. Mr. President, I rise in strong support of S. 240. I was an original cosponsor of this bill in this Congress, and in the last Congress.

Mr. President, securities litigation reform is not a household issue. It is not one that many people follow. But the fact is that it is very important for our economy, and very important for job creation in our country.

Very simply, this bill will attempt to put an end to frivolous class action lawsuits that are filed against America's publically traded companies. These are lawsuits that have little and often no bearing. They are filed for the sole purpose of blackmailing the companies. They are not lawsuits; they are legalized blackmail into settling suits rather than going to court. Everyone that has followed the issue at all knows, or who has ever been sued knows, that it is often cheaper to settle up front than it is to go all the way to trial with the cost of lawyers today. Of course, once the suit is settled, the attorneys that brought them keep the money. They keep the larger portion of it. It has become a cottage industry for certain lawyers that has been created over the last 20 years. I think it is time to put an end to it. And that is the purpose of this bill.

The problem is dramatic. Since 1980, there has been a 73-percent increase in

the number of civil suits filed in Federal court. It is estimated that class action suits have increased three fold in just the last 5 years.

The cost of these suits is no small matter. At the end of 1993, class action suits were seeking \$28 billion in damages.

The impact of these suits is having a detrimental effect on our economy. Many companies are afraid to go public and sell stock. By remaining private, they can avoid these kinds of suits, but they also sacrifice an increase in growth and jobs that can come from going public. This is costing America jobs.

Some have suggested that companies from overseas are afraid to establish businesses in America out of fear that they too will fall victim to these suits. This is costing America jobs as well and economic growth.

Money that would otherwise be spent on new job growth, and on research and development is paid out to lawyers to settle these suits or money is spent fighting them.

Furthermore, excessive costs are passed along to consumers in the form of higher prices. All of this has a ripple affect on our economy. Mr. President, it is making America less competitive and creating fewer jobs at a time in this country's history when we should become competitive, and we should be creating more jobs in order to stay competitive.

In my home State of North Carolina alone, 116 companies have contacted me and asked for help in passing this bill. They are united in their effort to end the abusive lawsuits that are being filed. Together, these companies in one small State alone, in North Carolina, employ 118,000 people. That is why the bill is so important not only to North Carolina but to the Nation as a whole.

Mr. President, let me assure you that nothing in this bill will prevent anyone from filing a legitimate fraud case against any company. Not one sentence in this bill will restrict anyone's rights who has a legitimate complaint.

If it did, I do not think 50 Members of the Senate would have cosponsored the bill.

Also, please do not be fooled by the ads you are seeing or hearing on this bill. They are not paid for by consumers. They are paid for by trial lawyers—wanting to protect their lucrative industry.

Consumers will be helped by this bill. Any consumer that has a job—or wants a job—or wants to keep a job will be helped by this bill. Not one consumer with a legal, legitimate lawsuit will be hurt by this bill.

Mr. President, a point that is not often made is that the consumers and plaintiffs in the class action suits rarely benefit from these lawsuits. You would think that the consumers and plaintiffs are receiving the benefits. But they are not. Study after study shows that lawyers get the vast major portion of any settlement.

We had testimony that the average investor received 6 or 7 cents for every \$1 lost in the market because of these suits—and this is before the lawyers are paid. So after the lawyers are paid, there is practically nothing left.

Mr. President, I particularly want to note that an important part of this bill is the reform of proportionate liability rules. This bill requires that those who are responsible for causing a loss pay their fair share. But it does not require them to pay more than their fair share except in certain extenuating circumstances.

This will stop the tactic of going after the deep pockets—like the accountants. The rule is sue everybody and anybody, and then get the rich defendants to do the paying.

Under this bill, if a party to the suit is found to have contributed to a loss but did not do so knowingly, that person pays only the percentage of the loss he or she caused. For example, if this person caused 2 percent of the loss, they pay 2 percent of the liability claim.

Mr. President, I strongly support S. 240. I think we need to act on it now. And I am going to oppose any amendment that I think will weaken this bill. I think it needs to be passed as it is. This bill has already been moderated enough in committee to give it bipartisan support. So I urge the Senate to pass S. 240 as soon as possible.

Mr. President, I yield the floor.

Mr. BRYAN addressed the Chair.

The PRESIDING OFFICER (Mr. MACK). The Senator from Nevada.

Mr. BRYAN. Mr. President, I thank the Chair.

Mr. President, I rise in opposition to S. 240. I should like to make a couple of preliminary observations.

This is not the kind of riveting stuff that keeps everybody in America who is watching on television at the edge of their seats. Much of this discussion is esoteric, technical, and full of legal nuances, but no one should conclude from that preliminary observation that it does not have an enormous impact on millions and millions of Americans. Everyone who has a retirement account in which he or she has invested in securities, millions of small investors, all have a stake in this legislation.

The American securities market is acknowledged by all to be the world's safest and most effectively regulated, and the underpinning for this system has been twofold. No. 1, the powers which the Congress has vested in the Securities and Exchange Commission to regulate and keep the marketplace honest, fair and open to investors is one important aspect, in addition to the adjunctive support provided by State securities administrators in the respective 50 States. But as has been pointed out by my distinguished colleague, the senior Senator from Maryland, the ranking member of the Banking Committee, private causes of action are recognized by security regulators to be an equally important part

in keeping the marketplace free from fraud.

Mr. President, we are not talking about something that is academic, as if there were problems in the past and all of those have been taken care of. The New York Times in an article dated Friday, June 9 of this year makes this observation, and I quote:

Securities regulators say they are opening investigations into insider trading at a rate not seen since the mid 1980's, the era in which Ivan Boesky, who went to jail for trading on inside information, became a household name.

And then later I quote again.

"It's a growth industry," said William McLucas, Director of the Division of Enforcement of the Securities and Exchange Commission. "In terms of raw numbers, we have as many cases as we have had since the 1980's, when we were in the heyday of mergers and acquisition activity."

The North American Association of Securities Administrators estimates that each year there is approximately \$40 billion of fraud in the securities marketplace. So millions of investors, people who do not think of themselves as stock barons but have their small retirements invested in the securities market, can be affected by what this Congress does on this legislation.

In my view, Mr. President, the bill pits innocent investors, many of whom are elderly and are dependent upon those investments for their sole source of retirement, on one side and those who are trying to immunize themselves from liability by reason of their own fraud on the other side.

I recognize the need for some changes in our securities litigation system. I do not appear before my colleagues this evening as a defender of the status quo.

I commend the distinguished chairman and the sponsors of this bill because in a number of areas the bill which they have introduced improves the present system, and it does so in these areas without disadvantaging the innocent investors who may have been defrauded. These areas include the prohibition of referral fees to brokers, prohibition on attorney's fees paid from SEC settlements, no bonus payments to class plaintiffs, elimination of conflicts of interest, payment of attorney's fees on a percentage basis, and improved settlement notices.

Mr. President, I think all of us would agree that those are important and positive changes which impact the securities litigation system in America. And if we are not in unanimity, there is virtually a consensus everywhere that these go a long way to correcting abuses in the securities litigation system. But any system must be balanced, and it must be fair so that it does not preclude meritorious suits.

The Trojan horse that brings this legislation to the floor unfurls the ensign of preventing frivolous lawsuits. I share that conclusion, as does the distinguished ranking member, who previously spoke in the Chamber. But the passengers inside this Trojan horse have very little interest in deterring

frivolous lawsuits. Their primary objective is to shield themselves, to immunize themselves from liability as a result of their own, in some instances, intentional fraud and, in other instances, reckless misconduct.

It is for that reason my colleague and friend, the junior Senator from Alabama, Senator SHELBY, and I introduced our own bill earlier this year, S. 667, as an alternative to the legislation that is before us today. Our bill is a carefully tailored, fair approach that would prevent frivolous actions from proceeding while at the same time protecting meritorious actions.

Let me make a comment about frivolous lawsuits. I think there is a legitimate problem there, but the way in which we deal with frivolous lawsuits is to impose sanctions on attorneys who file frivolous lawsuits and make them be financially responsible for their misconduct in filing those frivolous lawsuits. I favor enhancements to rule 11 under the Federal Rules of Civil Procedure, and earlier this year I was privileged to offer the Frivolous Lawsuit Prevention Act which is designed to provide an additional power to Federal judges once a determination is made that a frivolous lawsuit or claim is made to impose sanctions, and that means financial responsibility so that the defendant who is required to defend that frivolous lawsuit can make his or her or its expenses whole again. I support that.

I submit to my colleagues that this legislation which we have before us this evening is far more than an attempt to curb frivolous lawsuits because if that were its purpose, I would be in the vanguard of urging my colleagues to adopt this legislation.

S. 667, which has been endorsed by numerous groups including the North American Association of Securities Regulators, the U.S. Conference of Mayors, and the Government Finance Officers Association contains reform measures that will improve the system for all Americans.

S. 667 also contains many provisions to eliminate abusive suits and to protect all parties to litigation including a novel proposal for an early evaluation procedure designed to weed out those cases that are clearly frivolous cases and, as I said previously, to impose sanctions when necessary. It provides for a rational, proportionate liability system.

Mr. President, it protects the defrauded investors fully so that when there is an uncollectible judgment against the primary wrongdoer, they can fully recover the amounts of their losses. It provides a reasonable regulatory safe harbor provision, as my distinguished friend and colleague, the Senator from Maryland, pointed out earlier this evening. And importantly, S. 667 also contains other measures to preserve meritorious suits.

It restores aiding and abetting liability eliminated last year by the Supreme Court in the Central Bank of

Denver case by a 5 to 4 decision. The effect of that case was to wipe out liability of aiders and abettors and to immunize them from lawsuits based upon their own reckless misconduct that has been responsible for losses incurred by innocent investors.

S. 667 would also extend the statute of limitations for security fraud action in a manner suggested by the SEC and virtually every other unbiased witness who appeared before the Banking Committee. It codifies the reckless standard of liability with current law with the Sunstrand case, which Senator SARBANES referred to, and it restricts, Mr. President, secret settlements, protective orders, and the sealing of cases so that the public really knows what happens in these cases.

In my judgment, the bill that Senator SHELBY and I sponsored is reasonable, targeted, and balanced. It solved those problems that have been identified while preserving the system that has made our capital markets the envy of the world as the strongest and most safe. By contrast, Mr. President, the bill before us today makes radical changes in our securities laws, laws that have worked exceedingly well over the past six decades.

Let me discuss some of the arguments made for these radical changes. The primary premise of those who support S. 240 deals with an allegation that there has been an explosion of class action security lawsuits and that we must undertake these radical reforms in order to prevent this abuse.

The Congressional Research Service, at my request, prepared a report that was issued on May 16 of this year and entitled "Securities Litigation Reform: Have frivolous shareholder suits exploded?" Let me read to you some of the findings of the CRS study. Again, Mr. President, I quote:

While some current legislation . . . and the outcry of various corporate executives suggest that the volume of warrantless securities litigation has exploded to crisis proportions, evidence of this "explosion" is far from definitive. We know that in the 1990's, the number of annual Federal class action, securities cases filed has returned to the proximate level of such filings during the early and mid-1970's.

And I continue with the quote.

By the standards of the docket sizes faced by Federal courts, the upper limits of these potentially "abusive" securities suits remain exceptionally small; the filings have never exceeded 315 yearly in 20 years.

"* * * 315 cases a year in the past 20 years." Let me reiterate that point again. "* * * 315 cases in 20 years."

In fact, when multiple filings are consolidated, because some companies face more than one lawsuit as a result of the allegation of securities fraud, approximately 120 to 150 companies are sued each year.

Mr. President, that is out of some 14,000 registered companies—14,000 registered companies. And approximately 120 to 150 companies get sued each year.

The CRS goes on to say:

There are observers who argue that shareholder suits legally and unfairly exploit the high stock price volatility often observed among high tech firms.

However, another analysis of these high tech firms indicates that their unusually short, and unpredictable product cycles may, in fact, predispose their management toward a greater tendency to suppress proper disclosure or to provide false ones.

On balance, the evidence does not appear to be compelling enough for one to definitively assert that warrantless class action suits have exploded.

Mr. President, let us take an even closer look at the underlying premise upon which opponents would rewrite, in my view, in a radical way, our highly successful 60-year-old securities law. First, we are told there is an explosion of securities fraud cases. The CRS report demonstrates that this simply is not the case.

Let me invite my colleagues' attention to a chart that I have had prepared. These are securities class action lawsuits filed from 1974 to 1993. In 1974, over here, perhaps 290 cases; 20 years later, in 1993, approximately 290 cases. So in more than 20 years, when the population of America has geometrically increased, when the amount of general civil litigation—general civil litigation, not securities class actions—has grown dramatically, the number of class actions brought on behalf of securities plaintiffs has remained relatively constant, somewhere at the highest point, 315, and currently 290 cases.

Mrs. BOXER. Will the Senator yield for a question on that point?

Mr. BRYAN. I will be pleased to yield.

Mrs. BOXER. I am astounded by this chart. The proponents of this bill have been saying, since we started in the committee, that there has been an explosion in class action lawsuits filed—an explosion. We are going to hear tonight from all quarters. What the Senator is showing us tonight is really extraordinary. There has been no explosion.

Mr. BRYAN. My colleague is correct. Over the past 20 years, the numbers have been relatively constant. This represents one-tenth of 1 percent of the 235,000 Federal suits filed in 1994—one-tenth of 1 percent. There were 235,000 cases filed in the Federal court system in America last year, and one-tenth of 1 percent involved class action securities lawsuits. So my distinguished colleague is correct in her observation.

Mrs. BOXER. May I just say to my friend, thank you for this very straightforward chart because we are going to hear it all over the place in this U.S. Senate. And I am going to refer back to your chart, I say to my friend. Thank you very much for setting the record straight. There is no explosion of these class action lawsuits. Those are the facts. And I thank my friend for presenting it in such a clear fashion.

Mr. BRYAN. And I thank my colleague for posing the question. Securities class action suits have actually declined sharply in the last 20 years relative to both the number and the proceeds—the number and the proceeds—of initial and secondary public offerings, stock market trading volume, and every other measure of economic activity. To claim that suits by victims of financial swindles have constituted an explosion in civil litigation is patently false.

Now, we are also told, Mr. President, that so many companies are being sued that they are being distracted from other businesses. This is simply not true. According to figures from Securities Class Action Alert, only about 140 public companies were sued in securities fraud actions last year out of some 14,000 public companies reporting to the SEC. The only suits that have been going up are business suits against each other; that is, companies suing companies—companies suing companies, not suits by individuals against businesses. So if the companies who are suing each other are so troubled by litigation, why do they not just stop suing each other?

Mr. President, I think I have the answer. It is because they do not want to prevent themselves from being able to sue. They just want to prevent private individuals from being able to sue them. It is as simple as that. These companies would also have us believe that because of these suits, companies are fearful of going public, that they cannot raise the capital in the securities market.

Mr. President, there is no credible evidence that I am aware of that supports this astounding proposition. The existence of these suits has had no discernible impact on capital formation of business. The Dow Jones Industrial Average has just surpassed 4,000—an all-time high. I would invite my colleagues' attention to this chart. In terms of the initial public offerings, over the period of time that we have referenced here, they have gone up by approximately 9,000 percent in the last 20 years.

In the last 20 years, initial public offerings have risen by 9,000 percent—now, that is the number, Mr. President, of initial public offerings—while the capital raised, that is the amount raised by these initial public offerings, has increased by 58,000 percent. So both in terms of numbers and in terms of the dollars raised, they have gone up 9,000 and 58,000 percent, respectively. Let me say, I am glad to hear that, because that is important that we have the necessary capital formation to finance new enterprises. That is the essence of the free enterprise system.

The contention is invariably made that every time a stock drops to any degree, regardless of the reason, that there is a great rush to the courthouse and lawsuits are filed based solely upon the fact that the stock has declined in value. I want to address that assertion.

In examining this contention, there are three studies that have been called to my attention that reject that thesis.

One study by Prof. Baruch Lev of the University of California at Berkeley, involved public companies whose share price dropped by more than 20 percent in the 5 days following a disappointing earnings report.

Although there were 589 such cases where the stock dropped at least 20 percent from 1988 through 1990, class action suits were filed against only 20 of those firms, approximately 3.4 percent.

Moreover, Professor Lev compared those 20 firms with similar firms that were not sued and found that the firms that faced litigation tended to put out rosy projections, or forward-looking statements, just before releasing the bad earnings report, the issue that my distinguished colleague from Maryland so ably addressed that operates under the rubric of safe harbor, of which much more will be said during the course of this debate by him and, I am sure, my other colleagues.

By contrast, the firms that were not sued tended to publish more sober statements warning investors in advance that earnings would be lower than expected.

There was another study conducted by the firm of Francis, Philbrick, Schipper from the University of Chicago which searched for lawsuits against companies sustaining 20 percent declines in earnings and sales.

The author reported that, out of 51 such at-risk firms during 1988 to 1992, only 1 of the 51 was the target of a shareholder suit related to an earnings announcement.

And still a third such study performed by Princeton Venture Research shows that between 1986 and 1992, less than 3 percent of the companies whose stock dropped by more than 10 percent a day were sued.

So the claim that companies are bombarded with suits whenever their stock goes down is simply not supported by the studies I have seen. None of these studies, even using a 20-percent stock drop, found even 3.5 percent of the companies in this classification that were sued.

Even the Senate Banking Committee staff report published last year, under the able direction and support of Senator DODD and his staff, concluded, and I quote:

There is also no clear evidence of the extent to which price declines drive securities class actions to be filed.

But the proponents of S. 240 tell us, most of these suits are filed just so the plaintiffs can get a settlement. Again, the documentation does not support this conclusion.

The Senate staff report, to which I previously referred, examined sentiments of Federal judges regarding meritless litigation and found, and this again is directly from the staff report:

Seventy-five percent of the judges surveyed . . . thought that frivolous litigation was a small problem or no problem at all.

The SEC told the subcommittee that surveys had shown that "most judges believed that frivolous litigation was not a major problem and could be dealt with through prompt dismissals." And I believe the enhanced provisions of the Federal Code of Civil Procedures, that deals with frivolous lawsuits, is an absolutely appropriate and responsible way to deal with errant and irresponsible lawyers who file clearly frivolous lawsuits.

I believe the strengthening of those provisions under the law, targeted and tailored, is the most effective way of curtailing lawyer abuse.

The evidence clearly shows we ought not to throw the baby out with the bathwater.

S. 240 goes well beyond what is needed to deal with the abuses that exist in today's system. Every Member has cause to be concerned, because once this bill is passed and the next fraud comes along, whether it be a derivative disaster in your State, another Keating, a Milken or a Boesky, your constituents will want to know why you supported legislation that took their rights away to recover for their losses as a result of such fraudulent activity.

Unfortunately, there are provisions in S. 240 that would effectively gut private actions under the securities laws, eliminate deterrence and hurt average Americans who depend on the system to protect their savings, their investments, and their retirements. These provisions would give free rein to the next Charles Keating and could cause incalculable damage to States and localities that suffer the same fate that Orange County has recently faced.

Among the most troublesome provisions in S. 240 is the safe harbor exemption from fraud liability for forward-looking statements that essentially allows executives to say almost anything and be immunized from liability as a result of such misstatements.

Senator SARBANES has indicated he will be offering an amendment to correct this problem, and I intend to join him as a cosponsor of that amendment. It is something that concerns the Federal and State regulators; the SEC has written, the National Association of Securities Administrators has written, government finance officers, and consumer groups all have written the committee expressing their concern.

Corporate predictions, called forward-looking statements, inherently are prone to fraud as they are an easy way to make exaggerated claims of favorable developments to attract investors to part with their cash.

In fact, the Federal securities laws were passed in large part because of the speculative stock projections that led to the stock market crash in 1929.

Recognizing the inherent potential for exaggerated claims, forward-looking statements by public companies were not even permitted until 1979.

I think that bears repeating. Until 1979, no forward-looking statements

were made as a result of the experience that we had in the 1920's and the predilection of those seeking to embellish their own prospects for earnings to attract investors to invest as a result of these extravagant and flamboyant claims.

Since 1979, the SEC, recognizing some forward-looking statements may be important, has allowed limited predictions and protected them from liability if they are made in good faith and with a reasonable basis. Nevertheless, false predictions continue to be a favored tool of con artists, promoters and the illegal inside traders to pump up the price of their stock in order to profit at the expense of innocent investors.

S. 240 sponsors have not explained to my satisfaction why corporate statements that are made in bad faith with no reasonable basis or even with reckless disregard for their falsity need to be immunized from liability when fraud has occurred. I hope during the course of this debate we might have such an explanation. We are talking about statements made in bad faith with no reasonable basis and with reckless disregard for their falsity. I know of no public policy, Mr. President, that suggests that kind of conduct ought to be shielded from liability. Unhappily, S. 240 in its present form would do just that.

Moreover, the SEC is in the middle of a rulemaking process to study forward-looking statements and has asked Congress to allow it to complete its process. The original S. 240, as my colleague from Maryland has pointed out, would have done so. It is a technical area, highly complex and, frankly, it is a subject best left to the administrative agency in a rulemaking process rather than in a broad legislative enactment.

However, in committee, a virtual unlimited exemption or safe harbor—my colleague has aptly referred to this, not as a safe harbor but a pirate's cove, and I think he makes a compelling argument. Any statement either made orally or in writing that projects estimates or describes future events, so long as it is called a forward-looking statement, is immunized as a result of the legislative draft that is before us, even if that statement is made recklessly.

This is a gaping loophole through which wrongdoers or victims of fraud would be denied recovery. The effects of these changes, I think, are difficult to forecast, but I think they would have a devastating impact on the market.

I remind my colleagues that it is already extremely difficult to win a securities case. Under the 1934 Securities Act, a plaintiff must prove fraud or reckless behavior. Recklessness is defined as "highly unreasonable conduct that involves not merely simple or even gross negligence, but an extreme departure from standards of ordinary care."

So I think it is important for our colleagues to understand that no one under the 1934 act is liable as a result of his or her simple negligence, ordinary negligence, or even gross negligence. It requires a higher standard of misconduct—namely, reckless conduct. That seems tough enough to me. Anyone who makes a projection and meets this standard ought to pay his or her victims.

A second troublesome provision in S. 240 is the severe limits on joint and several liability, even when the primary wrongdoer is insolvent. America's legal system for fraud traditionally has been based on joint and several liability. Under this standard, if one wrongdoer is found liable but has no assets, the victim can be reimbursed fully by the other wrongdoers without whose assistance the fraud could not have succeeded. The underlying premise for this legal rationale is in that scale of justice—in the balance. Who should bear the burden of the loss? The innocent investor, who is totally without fault—no fault whatsoever—or a defendant whose conduct is at least reckless and may be subject to intentional fraud? Who ought to bear the burden? The philosophy that undergirds the American system of jurisprudence for centuries has said that under those cases, the scales of justice weigh in favor of the innocent victim, the one who had no responsibility, did not in any way contribute to the misdeed which caused the loss.

The rule has enabled swindle victims to recover full damages from accountants, brokers, bankers and lawyers who participate in securities scams when the primary wrongdoer has no assets left, has fled the jurisdiction, or may be in jail. The original S. 240 sharply limited this rule, immunizing reckless wrongdoers from joint and several liability.

If that had been the law, most investors would not have recovered their life savings in the Charles Keating/Lincoln Savings & Loan debacle. Although Keating had become bankrupt, the victims recovered their damages from the accountants, bankers, and lawyers who assisted Mr. Keating. Of the \$240 million in judgments imposed in favor of class action plaintiffs, nearly 50 percent—or \$100 million of those recoveries—were against accountants, bankers and lawyers—not the primary wrongdoers, but individuals who conducted and assisted Mr. Keating in perpetrating the fraud.

Despite extensive testimony, particularly by the SEC, that restricting joint and several liability will reduce recoveries for defrauded victims and encourage more fraud, the bill, as reported, restricts joint and several liability even further.

In the all-too-often cases in which a knowing violator is bankrupt, in jail, has fled, the liability of reckless violators to the uncollectible share would be capped. That is, there would be a limitation. Those who are proportionately

liable under the system that is incorporated in this print of S. 240 would be subject only to their proportionate share, even though the innocent victim is unable to recover his or her full amount.

There is one exception, as was pointed out, and that would be with respect to victims whose net worth is under \$200,000 and have recoverable damages of more than 10 percent of their net worth.

May I suggest, Mr. President, that is a very narrow window of opportunity. People who own their own homes, automobiles, and have the most modest of assets frequently might have a net worth of \$200,000. So we are not talking about the goliaths of business people who are extraordinary affluent; we are talking about tens of millions of Americans who would be excluded from recovery under this provision. That cap on joint and several liability means it will be virtually impossible for a great many of those victims to recover their losses.

The bill also does several other very damaging things. The bill would also turn over control of class actions to the wealthiest investors, even though their interests may not be as extensive as the small investors' that the class action device was designed to protect. It relegates small investors to a second-class status and makes the securities markets strictly a playgrounds for the big boys—the wealthy.

In committee, a new provision was added that requires courts to designate the "most adequate plaintiff"—words of art—in a private class action. This "most adequate plaintiff"—defined as the plaintiff with the largest financial interest in the case—is given the power to select lead counsel, control the case, and even to make settlement agreements for any amount or even dismissing the case.

This change to S. 240 makes plain the real motives behind the bill and makes hollow any protections that this is to protect meritorious fraud actions. This "most affluent plaintiff" requirement would simply wipe out average investors who are defrauded. The wealthiest investors may have close ties to big corporate defendants who can afford to accept less than the full recoveries. But it gives them complete control over class actions at the expense of average investors.

Aside from raising a specter of collusive intervention by large investors, and simply dismiss cases or enter into sweetheart settlements, the substitute virtually precludes small investors from being able to obtain attorneys willing to invest their time on cases over which they have no control and for which they may not be paid.

This also directly contradicts the reason why class actions were devised in the first instance, and that is to give average investors, who cannot afford to fight big corporations by their own means, the ability to band together and collectively seek a remedy for

their relief. Instead, this provision gives preference to wealthy investors who can afford to seek redress for their losses on their own.

S. 240 also eliminates a principal investor protection provision that was originally part of S. 240, as the distinguished ranking member of the committee, the senior Senator from Maryland, points out. That deals with the statute of limitations issue. Currently, the statute of limitations is 1 year from the point of the discovery of the fraud on the part of the victim, but in no event for more than 3 years after the fraud. The SEC, the North American Association of Securities Administrators—every regulator that I am aware of, who offered testimony or correspondence, indicated that this period is simply too short. It provides insufficient time for meritorious, legitimate plaintiffs to bring their action. The original S. 240 extended the period to 2 years after the violation was, or should have been, discovered by the injured plaintiff, not more than 5 years after the fraud itself.

As the Senator from Maryland pointed out, we dealt with this issue back in 1991 under the Lampf case. That case will have particular relevance to a number of my colleagues, because immediately after the Lampf case, which gave a retroactive interpretation to the law, surprising most securities litigators by concluding that there was only a one to three-year statute of limitations, immediately thereafter, Charles Keating filed a motion to dismiss.

A number of my colleagues joined me in supporting an amendment to the legislation that restored the 2-5 year provision retroactively, so that those cases for dismissal would not find themselves dismissed simply because the statute of limitation provision came as a surprise.

What this provision seeks to do with respect to the prospective cases is the same 2-5 year. As the distinguished Senator from Maryland pointed out, when this proposal came to the floor to correct the retroactive abridgement or shortening of the statute of limitation from 2-5 to 1-3, there was no objection. Everyone agreed.

The only issue—and it was a legitimate question—should we not take a broader look at security litigation reform? There was no objection to the premise you need a longer period of time.

I must say that the SEC has been very clear, and their testimony has been compelling, that even with all of the resources that the SEC can command and marshal, it takes an average of 2.25 years to complete an investigation of an alleged securities fraud. That is the SEC, with immense resources.

We, by failing to provide for the statute of limitations correction which was originally part of this bill and in rejecting the advice of the SEC, the North American Association of Secu-

rity Administrators, and virtually everyone that testified from a regulatory public policy point of view, we give comfort to those who perpetrate fraud on innocent investors.

I will offer an amendment that deals with that issue either later this evening or tomorrow, as our time permits.

I might just add that Senator DODD, one of the prime sponsors, indicated he, too, believes S. 240 needs to be amended to reflect that statute of limitations issues we just talked about. Obviously we will welcome his support.

S. 240 also fails to restore the aiding and abetting liability for private suits and eliminates the ability of the SEC to sue aiders and abettors for reckless behavior as opposed to fraudulent conduct.

Members will recall, Mr. President, I cited in the Keating case that recovery of \$100 million was from aiders and abettors. If S. 240, as this legislation is being processed today, was the law back in 1991, that \$100 million could not have been recovered. It could not have been recovered because the court, just last year, in another case that was a surprise to those who follow the securities industry issues, held that a ruling that had been in effect for 25 years, namely, that aiders and abettors were covered under the provisions of the securities law, that aiders and abettors were, in fact, not covered, and under a 5-4 Supreme Court decision, Central Bank of Denver, such liability for aiders and abettors is eliminated.

We are not talking about proportionately. We are not talking about joint and several liability. We are talking about aiders and abettors. They have a free ride. They are home free. All you need to do is get yourself in the aider and abettor category and you can have a field day. It is "Katie bar the door," do whatever you wish, and insofar as a private cause of action, you are precluded from recovery.

Mr. President, no matter how anyone feels on securities litigation reform, can it possibly be in the best interest of America to insulate from liability a category of persons whose conduct has inflicted upon innocent investors enormous financial loss, maybe even wiping out everything that a retired person might have in his or her investment?

I indicated that the Supreme Court also imposed a limitation even on the SEC—even on the SEC. They can only move against aiders and abettors under a much stricter standard. The defendant must knowingly—and that is the standard which even the SEC is forced to meet now as a consequence of the decision. We will be offering an amendment on this, Mr. President.

I note that Senator DODD, who has worked for many, many years—and all who work with him on the committee and consider ourselves his friend and close colleague acknowledge Senator DODD's fine work. Last year, in an April 29, 1994, "Dear Colleague" letter, Senator DODD made this observation:

Allowing private actions against aiders and abettors is an indispensable part of our securities enforcement system, and I believe Congress must consider legislation to reinstate liability in this area.

Senator DODD was absolutely right on the mark in 1994. The reason is even more compelling in 1995, based upon some of the information that I shared with Members earlier from those on the SEC that tell us about the amount of fraudulent activity. In this particular instance we talked of insider trading.

Senator DODD reiterates:

Lawyers, accountants and other professionals should not get off the hook, in my view, when they assist their clients in committing fraud. . . . The Supreme Court has laid down a gauntlet for Congress. . . . In my view, we need to respond to the Supreme Court's decisions promptly and I emphasize promptly.

As Senator DODD so often does, he speaks with precision, eloquence, and cogency. He is right on the mark, Mr. President. We need to do that in the course of processing any securities legislation.

Mr. President, this bill, also as reported by the Banking Committee, deals with the Securities Act of 1933—that is another provision—not the 1934 act. The 1933 act targets fraud in initial offerings of securities to the public. Initial public offerings historically have been rife with fraud by huckster promoters peddling new securities.

The 1993 act holds such wrongdoers strictly liable. The bill as reported, however, makes it nearly impossible to hold crooks who sell phony securities strictly liable for their fraud.

S. 240 also retains some highly burdensome pleading requirements—burdens that must be met by fraud victims, plaintiffs in these class actions. By “pleadings,” we are talking about an illegal document that commences a lawsuit in which a plaintiff—in this instance a victim of fraud—states forth his cause of action. Those pleading requirements under S. 240 are exceedingly burdensome.

Under current law, fraud plaintiffs are not required to state specific facts establishing the defendant's intent. That is a subjective state of mind. It seems pretty reasonable. It is a pretty onerous burden to be able to allege with particularity what the subjective thought process would be of a defendant.

The reason for that is because such facts are normally only uncovered later during a deposition or discovery process when there is a chance to examine the defendant or defendants under oath.

One of the ways the original S. 240 tried to block cases was through impossible pleading standards requiring plaintiffs to state specific acts demonstrating the state of mind of each defendant. Witness after witness indicated that this would prevent, for all practical purposes, many fraud victims from recovering their money.

The bill as reported merely replaces the impossible standard with the

harshest standard currently used. In my view, and in the view of those who regulate the securities market, it is not much of an improvement over the original language and would prevent legitimate plaintiffs from even asserting a cause of action.

S. 240 also contains an unfair and inflexible limit on victims for recovery. The bill contains a formula designed to limit the amount wrongdoers have to pay their victims. Basically, if the company stock goes up during a 3-month period following public exposure of the fraud, for whatever reason, the victims' recovery is reduced accordingly.

Finally, Mr. President, S. 240 would shield evidence of fraud from the public. S. 240 purports to attempt to eliminate secret settlements. The bill fails to ban the almost universal secrecy orders that are required by defendants as a condition of producing documents during discovery.

These orders remain in effect throughout litigation and generally require that, once a case is over, documents be destroyed or returned.

Such secrecy orders block significant corporate wrongdoing from public scrutiny.

Moreover, these orders allow defendants to proclaim their innocence after settlement without fear of contradiction—and permit them to claim the cases are frivolous when they visit with Members of Congress. And because the documents upon which the case was predicated are sealed, there is no effective rebuttal.

I would note one final irony of S. 240. The bill violates one of the primary tenets of Republican theory—this is, returning government functions to the private sector.

For 60 years, private attorneys general have supplemented the antifraud efforts of Federal regulators at the SEC and at the Justice Department.

Such an enforcement scheme is entirely consistent with the Republican contract.

But as CBO noted in its cost estimate on S. 240, if private rights of action are curtailed, substantial government involvement, including increased SEC efforts, will be needed to assure that the markets remain fair.

Moreover, as CBO stated in its June 19 letter to the committee, the SEC will have to double or triple its resources allocated to this function—and the cost to the American taxpayer could be up to \$250 million over the next 5 years.

That is to say, by reason of the restrictions placed on private causes of action, if one has a view of regulating the marketplace effectively the burden essentially now falls almost exclusively to the SEC, and they would have to up staff and the cost as estimated by CBO is \$250 million; \$250 million paid by the American taxpayer.

I invite my colleagues' attention to pages 30-32 of the committee report for CBO's estimate.

This confirms the view of the last Republican Chairman of the SEC, Richard

Breeden, who testified that the elimination of private actions would require the Commission to hire 800-900 more lawyers to police the markets.

Even if Congress should choose to appropriate the added money—which I seriously doubt—the system will not be as effective.

I hope each Member of this body will remember that when the next financial debacle hits, average Americans, many of whom may be people who live in your district, will be unable to runner their losses.

Last week, my constituents who were victims of the Keating scandal visited Washington, along with other Keating victims from other States.

One way Jeri Mellon from Henderson, NV, a community just 10 miles out of Las Vegas. She is head of the Lincoln bondholders committee. She and Joy Delfosse came to see me.

Every Member of Congress should be standing up for the Joy Delfosses and Jeri Mellons in their States, not the Charles Keatings.

These are retirees whose life savings would have been wiped out if they had not been able to recover as a result of the Keating fraud. And that ability to recover would have been lost if aiders and abettors had not been liable. And that ability to recover may have been lost if the statute of limitations had not been extended. And that recovery may have been lost as a result of the proportionate liability proposal contained in this legislation.

Mrs. BOXER. Will the Senator yield for a question?

Mr. BRYAN. I will be pleased to do so.

Mrs. BOXER. The Senator is right to bring up real people in this conversation. Because oftentimes we get into the legalese and we forget what we are doing here. So I appreciate the fact that the Senator from Nevada brings up the people that he met. I was with him at that occasion. We met people from Florida. We met people from Arizona. We met people from Nevada and California.

I want to ask the Senator a question, because I think anyone watching this debate ought to listen to the response of the Senator. My friend from Nevada who is addressing this Chamber is a learned attorney. He has great experience in seeking justice for people.

Is it the Senator's opinion that the people who were bilked by Charles Keating would have recovered as much as they have recovered, which as I understand it is between 40 percent and 60 percent of their losses, if S. 240 had been the law of the land?

Mr. BRYAN. The answer to the question of the Senator is unequivocally clear. They would have been unable to recover as much as they did. I would simply point out to my distinguished colleague from California, these are innocent people. These are not people who in any way participated in any scam. They are not lawyers. They are ordinary folks whose retirement was on the line. These were retirees.

It is interesting. As I know the distinguished Senator knows, they went to what they describe kind of as a neighborhood bank, Lincoln Savings and Loan. They knew everybody and they would come in and say, "How are you Suzy?" And, "How are you John?" And, "How is the golf game and how are you enjoying retirement?"

And they would say, "Look, what is this stock offering you have, American Continental Corp.?"

And they were told, "You know, you would be crazy not to put money in that, absolutely crazy. There is a much larger return than you would get just if you put this in a regular savings account in the bank."

These are the people, I tell my distinguished colleague from California, real Americans from every State of all political persuasions, of all political philosophies—real people, and the impact upon them is what this debate is all about this evening.

Mrs. BOXER. I have one last question for my friend. As we saw these people tell their stories, it was very moving. They are older. They were targeted by Charles Keating. And what they told us is—and this is the question for my friend—they went to file their suits, because they were clearly led to believe that their investments were protected, and the salespeople for Charles Keating were told to lead them down this primrose path. They called them the meek and the ignorant. They sought out "the meek, the weak and the ignorant." That is a quote from Charles Keating's brochures to their salesmen.

We know that Charles Keating put his whole family on the payroll and drained all this money that he stole. And is it not true, I say to my friend, that he went bankrupt?

Mr. BRYAN. He went bankrupt.

Mrs. BOXER. I say to my friend, he could not be touched by these people because he had a lot of lawyers who protected him. And he went bankrupt.

Is it not true that these good, decent senior citizens had to go to the aiders and abettors?

Mr. BRYAN. That is precisely the case.

As the distinguished California Senator knows, having read the provisions of the print before us, the thing that is particularly alarming is that there are several provisions in this law that is being proposed in its current form, as to the pleading standard, safe harbor, the ability to stay or to prevent discovery—that is ascertaining what the facts are—so long as there is a motion to dismiss; all of those were tactics that were used by Mr. Keating and his lawyers. All of those.

If the law in 1991 was the same as it will be if this is passed, together with the Supreme Court decisions that S. 240 fails to correct, those people might never have gotten into the courthouse door.

Mrs. BOXER. Let me thank my friend again for bringing this down to

what happens to people when we act here in this body, and to say to my friend that we ought to make any bill pass the Keating test.

We ought to look at any bill when we are done amending it. I hope we amend this bill and make it better, and put it to the Keating test. Would those good people, those innocent senior citizens, be able to recover when we are "done with reforming," I put in quotes, the securities law? Yes. We should go after those frivolous lawsuits. We all want to do that. But there are an awful lot of good companies out there that need to have the frivolous lawsuit aspect of this bill looked at. But, my goodness, let us not forget the real people, the retirees, the people who are the targets. Let us not forget them because it reminds me of the S&L scandal. We made one mistake once. I do not want to see us make another one.

I thank my friend for yielding.

Mr. BRYAN. Mr. President, I thank my distinguished colleague from California. I know some of my colleagues have waited for a while. I will finish, and yield the floor in a couple of minutes.

The Senator from California speaks with such clarity and conviction. She is absolutely right to remind us that a little more than a decade ago a big mistake was made with respect to the savings and loan industry. We spent billions and billions of dollars as a result. If we do not correct this legislation, as my distinguished colleague from Maryland, the distinguished colleague from California, and others will point out, we are opening the door to every charlatan and con artist in America to prey on innocent investors with impunity, and there almost a sense of *deja vu*. It may not happen tomorrow. But it will happen, and the consequences will be frightening. I do not think we want to make that mistake. America's securities markets have served as the world's finest. The Lincoln Savings & Loan in Orange County could be in my State. It could be in your State. I do not want to have to explain to the good citizens of my State why I allowed this happen, and why my failure to take action precluded them from being recovered as a result of frauds perpetrated upon them. Each and every one of us share that concern.

I have a number of letters from State and local officials. I am not going to belabor my colleagues this evening with all of those. But let me point out as this issue has been framed that it is the lawyers. Frankly, the lawyers do bear some responsibility here.

We talked about rule 11. And I am in favor of banging the lawyers that file frivolous lawsuits over the head and hit them in the pocketbook. Count me at the head of the line for them. But under the guise of getting the lawyers, unpopular since Shakespeare's time. "Kill the lawyers first"—every student of Shakespeare recalls that quote. Let us try to give here a more objective view.

You have people such as the Association of Governing Boards of Universities and Colleges who have expressed their concern and support the kinds of amendments that we are going to be offering, and oppose the legislation in its current form; the Association of Jesuit Colleges and Universities; the Council of Independent Colleges; the Government Finance Officers Association. These are not closet groups of trial lawyers. The Association of Clerks and Recorders; Election Officials and Treasurers; the Municipal Treasurers Association of the United States and Canada; the National Association of College and University Business Officers; the National Association of County Treasurers and Finance Officers; the National Association of State Universities and Land Grant Colleges; the North American Security Administrators.

Mr. President, I do not believe that one can make the case that these are simply closet advocates for trial lawyers, who I understand are the most disdained group of professionals in America. I understand that. I am not unmindful of that.

But we ought not with the antipathy that we feel toward them for whatever reason wipe out the right of innocent investors to sue. And the bill before us in its current print will do precisely that unless we accept the amendments that the Senator from Maryland, the Senator from California, and I believe the Senator from Florida as well maybe have.

I thank my colleagues for yielding.

Ms. MOSELEY-BRAUN. Mr. President, I would like to speak on the bill.

Mr. President, the United States has the largest and the best capital markets in the world. In no small part that is because markets in the United States are seen as open and fair. And it is one important reason over 50 million Americans are able to participate in our securities markets. Every investor can be confident that our markets are honest, and it is very clear that private securities litigation has played an important role in keeping them honest.

At the same time, there is real need for reform. One study conducted in the 1980's that was cited in the Banking Committee's report on S. 240 found that every single American corporation that suffered a market loss of \$20 million or more in its capitalization had been sued. In other words, every corporation whose stock at one time declined in value by \$20 million or more was sued for securities fraud during the period covered by the study.

Another study included in the committee report stated that one out of every six companies less than 10 years old that received venture capital had been sued at least once and that such lawsuits consumed an average of over 1,000 hours of time of the management of these companies and an average of \$692,000 in legal fees.

What these statistics demonstrate is that either our capital markets are literally overrun with fraud or that there are at least some unsupportable lawsuits being filed. The clear consensus of the Banking Committee was that the evidence did not and does not support the conclusion that our markets are suffering an epidemic of fraud. Rather, the committee's conclusion was very clear that there are abusive security lawsuits being filed, that these suits result in significant adverse consequences for our capital markets and for our economy generally and that, therefore, the reform is necessary. The fact is that securities fraud litigation can be very lucrative, even in cases where there is no fraud. Some would say particularly in cases where there is no fraud.

The Supreme Court made that point very clear in the case of *Blue Chip Stamps versus Manor Drug Store*. The Court in dictum stated that in securities fraud cases "even a complaint which by objective standards may have very little success at trial has a settlement value to the plaintiff out of proportion to its prospect of success * * *."

The Court's opinion was, of course, stated in the driest possible language. In the language of my hometown of Chicago what the Court was really saying was in this area of the law plaintiffs and lawyers who are willing to game the system have all the clout. These few people, and they are a few people, know that they have the corporations and other ancillary parties over a barrel, and they are taking advantage of that fact. They win settlements in all too many cases because of that leverage rather than because of the merits of the case.

What is more, Mr. President, under current law, small investors in a class action case do not really control the case, their lawyers do. One plaintiff lawyer demonstrated the temptation that a few lawyers have succumbed to all too clearly. He said:

I have the greatest practice of law in the world; I have no clients.

The opportunity for coercive settlements is not the only problem in this area. The Supreme Court made it clear again in the *Blue Chip* case that "the very pendency of the lawsuit may frustrate or delay normal business activity of the defendant which is totally unrelated to the lawsuit."

The reason for that is not just the cost of defending against litigation, it is the cost and disruption that flow from the company's attempts to respond to plaintiff's request for discovery, and discovery is not a minor matter. The committee report again stated:

According to the general counsel of an investment bank, "discovery costs account for roughly 80 percent of the total litigation costs in security fraud cases."

Companies have had to produce over 1,500 boxes of documents and to spend well over \$1 million just to comply

with the costs of fact-finding, of discovery. It is not just a matter of documents. The time the key employees of the company may have to spend responding to requests for information may keep them and, often does keep them, from tending to the business of the company and, therefore, that also works to coerce settlements.

Some might argue that this is a technical legal issue and one that is not important to the general American public. However, I would suggest that just the opposite is true. Every American, whether he or she invests in our capital markets or not, has an interest in seeing to it that reform is enacted.

The Director of Enforcement of the Securities and Exchange Commission made that point very well. Testifying before the Senate Banking Committee in the last Congress, he stated that:

There is a strong public interest in eliminating frivolous cases because, to the extent that baseless claims are settled solely to avoid the costs of litigation, the system imposes what may be viewed as a tax on capital formation.

Chairman Arthur Levitt of the SEC reinforced the point in his testimony before the Banking Committee. He stated that:

There is no denying that there are real problems in the current system—problems that need to be addressed not just because of abstract rights and responsibilities, but because investors and markets are being hurt by litigation excesses.

Mr. President, these excesses and the tax they impose on our capital markets and on our economic growth are particularly onerous because they do not even achieve what they are ostensibly designed to achieve—the protection of investors who suffer losses. All too often, under the current system, investors receive settlements that amount to only about 10 percent, or even less, of their damages, and that is another whole set of problems, to hold out false hopes to people in which they may receive less than 10 percent recovery.

The direct legal expenses in settlements paid are, again, only part of the tax. There are also a variety of indirect costs, costs that fall particularly heavy on the entrepreneurial and high-tech companies on which our future economy depends.

Of course, investors want to be protected from fraud, but they also want to be able to get as much information as possible, and they also want to be sure that their companies are focused on their business instead of on potential lawsuits and litigation.

Mr. President, it is important for us all to remember that investors are not just investors. Investors are also employees who want their companies to do well. There are also parents who want to see expanded economic opportunity for their children. They are also participants in the United States economy, and they want to see the kind of strong growth and job creation that goes along with a strong economy.

Our world economy is more and more competitive. Our future prosperity de-

pends on our ability to meet and beat that international competition, and that means we need a continuing supply of new ideas, new products, and new companies that can produce the jobs for tomorrow. These major issues may seem a long way from the arcane securities law issues we are debating and discussing this evening. But, Mr. President, the connection is both strong and direct.

A recent book by Hendrick Smith entitled "Rethinking America," I think, illustrates the connection. That book has chapter after chapter recounting the challenges facing American business in this new global economy. It talks about how some American businesses are succeeding and how some are not.

One of the points it makes in some detail is the short-term focus that afflicts so many American corporations, an affliction that is not shared by our major international competition.

American corporations are all too often intensely focused on the short-term price of their stock instead of the long-term growth and prosperity of the business. This short-term focus, which the current state of our securities laws helps to foster, distracts senior management, makes too many of our businesses less creative, and undermines the ability of American businesses to make the investments that have the best long-term payoff.

Our securities laws have also rendered many of our businesses mute, virtually unable to talk to their investors and owners because of the fear of lawsuits. And that fear not only disadvantages the companies and investors, it also hurts all of us because it is an impediment to the smooth functioning of our capital markets. It makes it less likely that capital is allocated in a way that produces the most and best new jobs and new products.

Let me emphasize that point. New jobs and new products. The engine of our economy depends in large part on the vitality of our capital markets and, in the final analysis, Mr. President, that is what this debate is all about.

I cosponsored S. 240, along with Senator DODD and other members of the committee because this bill has been based on the recognition of all of these facts. S. 240 acknowledges the multiple rolls and multiple interests that we all have in this area, and it is based, I think, on an understanding that we are all in this together. We must maintain strong investor protection while making it more difficult to file frivolous or abusive lawsuits.

We must create a climate where new businesses that create new jobs and new products can get the capital they need while ensuring that defrauded investors have the right to recover their damages.

S. 240, as introduced by Senators DODD and DOMENICI, went a long way toward achieving all of those objectives. The bill attempted to reduce transaction costs so that investors who

are harmed see a smaller portion of their recoveries consumed by attorney's fees and other miscellaneous costs. It was designed to help our capital markets create more jobs and create greater long-term economic growth, something that is also very good for investors.

The original bill has been modified in a number of important ways. Some of these changes represent improvements in the original bill, others represent new concepts. The bill before us is not perfect. In some areas, quite frankly, I would have written it differently and I suspect everybody in the Senate almost always feels the same way about major legislation.

I think it is clear, however, that this bill is a good-faith attempt to balance the competing public objectives in this area and that looking at the overall legislation it successfully achieves balance and that, I think, is a very important notion as we address this issue. Achieving balance is important to keeping our capital markets vital, and it is important to our economic prosperity.

It is important, Mr. President, again to keep in mind what this area of the law is all about and what the bill does and does not do. This may get a little technical, but I guess a lot of the conversation here has gone into the particular aspects of the bill that are the most controversial.

What we are talking about has to do with private rights of action for fraud under section 10(b) of the Securities Exchange Act and rule 10b-5 of the Securities and Exchange Commission. Those laws did not expressly provide private parties with a right to sue corporations or other parties involved in the issuance and sale of securities. However, this area of law has evolved out of a long series of judicial decisions, not legislative actions.

S. 240 will help reduce frivolous and abusive security suits, and it achieves that objective without encouraging fraud and without undermining the rights of investors, and particularly small investors, to recover where there actually is fraud.

Some argue that the bill is somehow unbalanced because it limits joint and several liability and because it does not extend the statute of limitations in private section 10(b) cases. The bill, however, holds everyone—I emphasize that—everyone who commits “knowing” securities fraud jointly and severally liable. Other defendants may be only “proportionately” liable; that is, they may be only responsible for the share of the harm that they cause. That ensures that parties who may be only 1 percent or 2 percent responsible for the fraud are not added defendants in cases simply because they have deep pockets.

Proportionate liability is far from a new concept. We have had it in the tort area in my own State of Illinois for a number of years. It is an important and necessary change. Without it, many

people will not deal with the small entrepreneurial, startup companies that are the most likely to be sued—and I point out that are most likely to create jobs—because the potential liability is so much greater than the profit that can be earned from doing business with these companies. Many companies are increasingly unable to find accounting firms and law firms willing to do business with them and are having increasing difficulty in attracting the best people to sit on their boards of directors. And the result of that is, again, less information and less protection for investors and greater hurdles for the new companies on which our economic future depends.

Of course, in some cases, the parties most responsible for fraud are judgment proof; that is, they have no assets at all that can be found. In those situations, this bill provides, I think, substantial protection for small investors. First, it says that defendants that are proportionately liable have their share of responsibility increased up to 50 percent of their proportionate share, so that all investors are better compensated for the losses they have suffered. For small investors, those with a net worth of under \$200,000, who suffer a loss of at least 10 percent of their net worth, every defendant is jointly and severally liable for paying those damages—a provision in this bill that I think ensures that small investors get that extra protection.

The proportionate liability provisions are not the only provisions, however, that have been the subject of criticism. Some argue that S. 240 is flawed because of a provision that it does not include, and that is the provision that has to do with an extension of the statute of limitations.

Mr. President, it is true that S. 240 is silent on the issue of the statute of limitations. But this is not to disadvantage small investors or any other investors. Four years ago, in a case known as the *Lampf* decision, the Supreme Court of the United States decided that the implied rights of action for private parties under section 10(b) were subject to the same statute of limitations that applied more generally in other areas of the securities law—1 year from the date of discovery of the fraud, or 3 years from the date of the fraud.

It is worth noting that the court did not disadvantage section 10(b) cases relative to other security cases; it simply said that the same statute of limitations applies, which is hardly a revolutionary idea. In the 4 years since the *Lampf* decision was rendered, there has been no substantial evidence presented that investors are being harmed by that decision.

Statutes of limitation, by their very nature, have some degree of arbitrariness to them. In this area, the evidence is that the overwhelming number of cases are being brought within a year of the time the alleged fraud occurs, which tends to indicate that a longer

statute may not be needed. Most cases are not filed just before the statute of limitations expires, so the 1-year/3-year statute of limitations does not seem to be making it difficult for plaintiffs to prepare their complaints.

My own conclusion is that, in light of the evidence, a case has not been made for giving section 10(b) implied private rights of action in fraud cases a longer statute of limitations than other Federal securities law related cases.

Mr. President, one of the provisions of this bill that has been the subject of some attention has to do with the issue of whether or not it includes something that has been called the English rule or losers pay. That has been a rule that never frankly has been applied in American jurisprudence. It is the English rule that says if you file the lawsuit and you lose, then you have to pay the cost of litigation. However, this bill does not have loser pay in it. The bill simply requires the judge to look at rule 11 of the Federal Rules of Civil Procedure, a rule that already exists and pertains to all kinds of civil litigation and which calls for sanctions for frivolous lawsuits to determine in these securities cases whether or not any party has violated rule 11 and, if so, to impose sanctions.

That is a far cry, Mr. President, from the English rule, from what has been called “loser pays.”

The bill also establishes what is called a “safe harbor.” This provision in some ways offers more protection for investors and less, frankly, for issuers of security than do some of the leading court decisions in this area today.

And so what is at issue here with the safe harbor question has to do with what are known as forward-looking statements, statements by issuers of securities that describe future events or that estimate the likelihood of selected future events occurring.

SEC rule 175 states that forward-looking statements made with a reasonable basis and in good faith cannot be used as a basis for a fraud action. That is already law.

However, Mr. President, as a practical matter, the safe harbor that it provides turned out to be not very safe at all. What added real protection was a third circuit case that recognized what is called the *bespeaks caution* doctrine, a doctrine that is now recognized in at least five circuits. Under this doctrine, under the *bespeaks caution* doctrine, forward-looking statements accompanied by meaningful cautionary statements, that is, statements that indicate the risks the forward-looking statements will not come true, are as a matter of law immaterial and therefore cannot be used as a basis for fraud action.

Under this bill, however, the *bespeaks caution* doctrine would not apply to issuers who made statements with the actual intent of misleading investors even if they were accompanied by meaningful cautionary statements.

To that extent, Mr. President, this legislation is more protective of investor's interests in that regard than the evolving state of the law in at least five circuits in this country.

Again, these are all highly technical areas, and there is a lot more that I can say about the issues and other issues raised by this legislation. However, I instead want to make one final point.

A simplistic analysis of this bill says this is a fight between the lawyers and the corporations and that the proponents of the bill, the people who support the bill, are somehow engaged in lawyer bashing. I cannot speak for every supporter of this bill, but I wanted to make it as clear as I can that as a lawyer myself, I care very much about the profession, and my view is that lawyer bashing has no place in this debate. The great bulk of the work of lawyers in the securities litigation area has been of enormous benefit to investors and to the public generally. The securities plaintiffs bar, frankly, has been particularly helpful in helping small investors, and it has played an instrumental role in keeping our capital markets respected worldwide. They have provided a necessary check in a system that, again, presumes honesty.

I would not have agreed to cosponsor this bill if I concluded that it would limit their important and legitimate role of the trial bar, of the securities bar, or if I believed this bill would take away from investors opportunities to recover damages from those who, in fact, had defrauded them.

What makes this bill necessary, however, are the abuses by a relatively small number of people who have thrown the system out of balance. S. 240 does nothing more than restore that balance, Mr. President.

I want to conclude by congratulating again Senator DODD and Senator DOMENICI and the leadership of the Banking Committee for all the hard work that has been put into this legislation and for the way everyone has worked together in a bipartisan fashion and in good faith to resolve some of the complicated issues in this area as they have arisen.

This bill may be a bill that leaves none of us fully satisfied, everybody is going to have another idea. But the compromises represented in S. 240 are good ones. They will be good for our capital markets. This bill will be good for economy. This bill will be good for job creation, and it will be good for the American people, generally, in all their roles.

On that basis, I support this legislation and I urge its passage by the Senate. I yield the floor.

Mr. SPECTER addressed the Chair.

The PRESIDING OFFICER. The Senator from Pennsylvania.

Mr. SPECTER. Mr. President, I thank the Chair.

Mr. President, I have sought recognition to comment briefly on the pending legislation and to offer a motion on be-

half of Senator BIDEN, Senator SHELBY, Senator FEINGOLD, and myself to refer the bill to the Committee on the Judiciary in order to consider some very important issues which have not had a hearing in the Banking Committee, because the Banking Committee under its own procedures does not customarily take up questions on the Federal Rules of Civil Procedure regarding which the pending legislation makes a great number of very significant changes.

The rules which govern court procedure are customarily fashioned by judges, and they are established by the Supreme Court of the United States with an advisory committee which considers the details of these provisions. They are complicated on matters such as how pleadings are formulated, how specific you have to be, and what to say to get in court before you are entitled to discovery; what rules govern when you take depositions, for example; that is, when questions are asked by one side of the parties on the other side. What happens with respect to sanctions when lawyers do not operate in good faith or bring frivolous lawsuits, or what happens on class representation.

These are the kinds of questions which I have had some experience with, although not recently. But I had experience when I practiced civil law before coming to the U.S. Senate. And on the Judiciary Committee, having been a member there for 14½ years, I have had some continuing familiarity with these issues, but nothing compared to the individuals who are in the courts every day.

On that subject, I discussed some of the issues raised by this bill with a longstanding friend of mine going back to college days at the University of Pennsylvania, Judge Edward R. Becker, who is now a very distinguished jurist on the U.S. Court of Appeals for the Third Circuit, and one of the premier Federal judges in the country.

Judge Becker was appointed to the Federal Court in 1971. He served for 10 years as a trial judge day in and day out, and for the past 14 years he has been on the court of appeals and is a recognized expert on Federal procedure, lectures in the field, and is highly regarded as one of the most knowledgeable of the Federal judges.

Some of the comments which Judge Becker has made to me in a relatively brief letter illustrate to some extent the problems which are present in the current legislation.

I compliment the Senator from California, the Senator from Nevada, and the Senator from Maryland, the ranking member of the committee, the chairman of the committee, and also the Senator from New Mexico, Senator DOMENICI, and the Senator from Connecticut, Senator DODD, who have drafted this legislation, for the very constructive work which they have done. But there are many very, very important provisions which have not

been subjected to the kind of analysis which comes only with real experience in the courts on a day-in and day-out basis.

Having had that experience, I know the difference between the legislative process and the judicial interpretive process. Those judges see these matters day in and day out. They know what happens in a very practical sense. They have a much deeper familiarity with the way they work out than we do in the Congress.

As the Presiding Officer knows, and as my colleagues know, frequently in our hearings in the Senate, only one or two Senators are present. When markup occurs it is done as carefully as we can, but not with the kind of craftsmanship which judges employ day in and day out.

These are some of the comments which Judge Becker has made which I think are worthy of consideration. They are not dispositive of all of the issues but are illustrative of the kinds of complex matters which we think require a great deal more consideration than we have had so far.

This legislation is enormously important. It is enormously important as it governs the securities field where capital is formed so that the free enterprise system can function, so that when representations are made in the prospectuses that sufficient information is given to investors to know what is happening, to see to it that the representations are honest, and that the millions and millions of people who invest in securities are protected—and not that there is any absolute guarantee that they will earn dividends or make money on capital gains because there is a certain amount of risk, but that there are representations honestly made, that they are protected against fraud, and that the procedures balance the concerns of the companies, not subjecting them to frivolous litigation but balance the concerns of the investors.

Judge Becker has made this comment, for example, on the rule of procedure which governs the designation of lead counsel:

Most of the provisions prescribe things the courts already do—for example, designating lead counsel—or at least can do within the exercise of their discretion. Section 102 constitutes congressional micromanagement with the untoward effect of depriving judges of the flexibility which is indispensable for effective case management.

One of the bill's important provisions relates to sanctions, which are important in litigation to ensure that the court has the flexibility to manage the case and that lawyers do not abuse the process, that is, they do not bring frivolous lawsuits, and frivolous lawsuits are brought. We know that as a matter of fact. Really no one contests that. Or no one contests the need for limiting frivolous lawsuits. And there is a generally recognized need that we ought to have reform in this field.

Some of the provisions of current law, for example on joint and several

liability, have imposed very extensive liability on accountants who do not know the inner workings of the representations but are held under the concept of joint liability. There needs to be a close look at the kind of liability imposed.

So that when you talk about frivolous lawsuits and how to deter them, we do need to have very substantial review of that issue. But I have found that the provision of the bill regarding the rule which requires mandatory sanctions by the court perhaps goes too far, and we do not know that for sure really until we analyze it in some detail. But this is what Judge Becker had to say about that:

Mandatory sanctions are a mistake and will only generate satellite litigation.

And by satellite litigation, Judge Becker was referring to the situation where, after the case is over, then a whole new litigation process starts as to whether sanctions are really required.

Under present law, the judge has discretion to award sanctions, and there has to be a motion made by the party that thinks that the other party has acted inappropriately. Before a party can ask for sanctions, the party must give notice to the other party of its view that something wrong has been done in order to give the allegedly offending party an opportunity to correct it.

That is done in litigation to try to have the parties work it out. If somebody does not like what the other party is doing, they say, "Wait a minute; you ought to stop that." It gives that party a chance to reflect on the reasons. If it does not stop, then the party can make a motion for sanctions. But under this legislation, the judge has the obligation on his own to review the record and to impose sanctions. That is contrary to the American system of adversarial litigation where the judge does not have the responsibility for making that determination on his own; one of the parties who feels aggrieved says to the court: Something wrong has been done here, and I make a motion to have it corrected. This is more like the inquisitorial system which the French have where the judge is the moving party.

Judge Becker has this to say after commenting on the satellite litigation.

The flexibility afforded by the current regime enables judges to use the threat of sanctions to manage cases effectively. Well managed cases almost never result in sanctions. The provision for mandatory review—

That is, without prompting by the parties—

will impose a substantial burden on the courts and prove completely useless in the vast majority of cases. Requiring courts to impose sanctions without a motion by a party also places the judge in an inquisitorial rule which is foreign to our legal culture, which is based on the judge as a neutral arbiter model.

The judge then refers to a rule drafted by a very distinguished judge, Judge

Patrick Higginbotham of the Court of Appeals for the Fifth Circuit, who is chairman of the Judicial Conference of the Advisory Committee on Civil Rules. And this is what Judge Higginbotham says ought to be done:

In any private action arising under this title, when an abusive litigation practice is brought to the District Court's attention by motion or otherwise, the Court should promptly decide, with written findings of fact and conclusions of law, whether to impose sanctions under rule 11 or rule 26(g)(3) of the Federal Rules of Civil Procedure or its inherent power.

And that is really giving discretion to the court. Perhaps on analysis the provision in the bill on mandatory would be retained. But I think it is indispensable, Mr. President, that that kind of careful analysis be made.

Other provisions set out in the current bill make very substantial changes to the Federal rules. There is a requirement that the potential outcome of the suit be disclosed, and there are special disclosures relating to settlement terms. These provisions have an impact on rule 23, the class action rule. The bill also contains certain unique provisions governing the appointment of lead counsel in class actions, none of which have been given a hearing.

I discussed with the chairman of the committee, the Senator from New York, Senator D'AMATO, the procedures used by the committee, and I think I am accurate in stating—and he can comment on this if the truth is to the contrary—that this is a provision added very late, and there had not been hearings.

There are also changes in the rules relating to discovery under rule 26, and there are differences in rules relating to the specificity of allegations of pleadings, affecting rule 9.

Without going into any great detail, these are all matters which really ought to be reviewed by the Judiciary Committee, which has the expertise under our Senate rules for handling matters of this sort. It is not the kind of a matter which is customarily brought before the Banking Committee.

This same issue was raised by the Chairman of the Securities and Exchange Commission, Arthur Levitt, in a letter dated May 25, 1995, to Senator D'AMATO. Chairman Levitt commented as follows:

I also wish to call your attention to a potential problem with the provision relating to rule 11 of the Federal Rules of Civil Procedure. I worry that the standard employed in their draft may have the unintended effect of imposing a loser-pays scheme. The greater the discretion afforded the court, the less likely this unintended consequence may appear.

The loser-pays scheme, Mr. President, is one which Great Britain has where the loser has to pay the costs of litigation, and that is a very, very abrupt and drastic change in our litigation procedure.

The bill currently provides for mandatory sanctions and contains a pre-

sumption that the loser will pay sanctions and that the appropriate sanction is the other party's attorneys' fees. This would have a very major, chilling effect on bringing any litigation. And that presumption can be overcome but it starts off on an unequal footing where the same requirement is not imposed on the defense, on the other side in the litigation. I am sure that there will be consideration of this substantive revision in the course of the analysis of this bill. But this again is something which really ought to have the benefit of a hearing in the Judiciary Committee.

Mr. President, I had advised the chairman, the Senator from New York [Mr. D'AMATO], that I would not be in the position to vote on this matter until others had a chance to come to the floor, specifically Senator BIDEN. I know that there are other Senators on the floor who wish to speak at this time. And it would be my hope that we can move to a vote this evening. I do not want to keep Senators here unnecessarily but I believe that Senators are present with the expectation of having a vote on final passage on the highway bill where there is still one matter which is left to be worked out.

But I do want to make that stressed statement that until Senator BIDEN returns we have an opportunity to have debate on this subject. There are some matters I want to discuss with the Senator, the chairman, the Senator from New York, who is necessarily absent at this time.

Before yielding the floor—I shall not hold the floor very much longer—there will not be more than one final statement that I will make, as I see my colleague from Utah, rising. I do want to make a brief comment about the bill generally as to information provided to me by the chairman of the Pennsylvania Securities Commission who has raised very substantial problems with the bill. I want to call those to the attention of my colleagues. This is a letter to me from Chairman Robert Lam, dated April 19, 1995, in which Chairman Lam makes this statement. "I have considered the major elements of both" Senate bill 240, which is the one currently being considered, and Senate bill 667, which is a different bill introduced by Senators SHELBY and BRYAN. It is the conclusion of Chairman Lam of the Pennsylvania Securities Commission that the other bill, the one not on the floor, is much preferable. Chairman Lam concludes by saying, Senate bill "240, on the other hand, tilts the balance too far in favor of corporate interests and would have the practical effect of depriving many defrauded investors the ability to cover their losses."

In a letter dated June 20, 1995—I shall include both of these letters for the record, so I do not have to take much time. Chairman Lam writes as follows,

As presently constituted, S.240 not only would affect negatively Pennsylvania investors but also Pennsylvania taxpayers should the Commonwealth Treasury Department

again become a potential victim of wrongdoing in securities transactions undertaken on behalf of the Commonwealth. The importance of the potential negative effects of this Bill on the Commonwealth is reflected by the Treasury Department's recent suit against Salomon Brothers for damages resulting from alleged wrongful conduct engaged in by Salomon in connection with its bidding on government bonds.

And Chairman Lam of the Pennsylvania Securities Commission concludes with this statement.

As a participant in the capital formation process, I would like to emphasize that our financial markets run most efficiently when there is a high degree of public confidence in the integrity of the marketplace. Money is merely the medium of exchange between this confidence and the honest entrepreneur. As written, S.240 will not advance the goal of making capital available to growing U.S. companies. It will result in small investors avoiding participation in our capital markets when they discover that they are unable to bring suit against the perpetrators of aiders and abettors of a securities fraud or, upon winning such a suit, fail to be made whole because the Bill adopts the concept of "caps" on total defendant liability.

I do ask unanimous consent, Mr. President, that the full text of these two letters from Chairman Lam be made a part of the record at the conclusion of my speech.

The PRESIDING OFFICER. Without objection, it is so ordered.

(See exhibit 1)

Mr. SPECTER. In conclusion, Mr. President—the favorite words of any speech, and with finality—I will pursue this motion as the evening progresses and do believe that it is very important that the full range of considerations raised by Chairman Lam be considered, issues that have otherwise been raised, but especially these procedural questions be considered by the Judiciary Committee which under our rules has the jurisdiction to consider them.

MOTION TO COMMIT

Mr. SPECTER. On behalf of Senator BIDEN, Senator SHELBY, Senator FEINGOLD, and myself, I do move to commit the pending bill, Senate 240, to the Committee of the Judiciary.

I thank the Chair and yield the floor.

EXHIBIT 1.

PENNSYLVANIA SECURITIES, COMMISSION,
April 19, 1995.

Hon. ARLEN SPECTER,
U.S. Senate, Hart Senate Office Building,
Washington, DC.

RE: Pending Securities Litigation Reform Bills S. 240 and S. 667

DEAR ARLEN: In my capacity as the Chairman of the Pennsylvania Securities Commission, I am writing to express my views on the two major securities litigation reform bills now before the Senate. The Pennsylvania Securities Commission is responsible for investor protection and overseeing the capital formation process in the Commonwealth.

It is my view that any securities litigation reform legislation must be carefully balanced so that it provides relief to companies and professionals who may be the subject of frivolous lawsuits while preserving a meaningful private remedy for defrauded investors. While much of the debate in Washington has focused on how to protect honest companies and professionals from vexatious

lawsuits, I believe there is an equally compelling need to maintain the ability to deter and detect wrongdoing in the financial marketplace.

From my vantage point, there continues to be an unacceptably high level of fraud and abuse in today's capital markets, particularly with respect to small investors. As the limited resources of government are insufficient to pursue every case of wrongdoing, the ability of defrauding investors to maintain a private cause of action to recover their investment without fear of financial ruin remains critically important to the overall successful enforcement of the securities laws.

It is against this backdrop that I have considered the major elements of both S. 240, the "Private Securities Litigation Reform Act," introduced by Senators DOMENICI and DODD, and S. 667, the "Private Securities Enforcement Improvements Act," introduced by Senators SHELBY and BRYAN. It is my conclusion that S. 667 is very much the preferable legislative vehicle for resolving the securities litigation reform debate. S. 667 achieves the critical balance between making the litigation system more fair and more efficient, while preserving the critical role that private actions play in maintaining the integrity of our financial markets. S. 240, on the other hand, tilts the balance too far in favor of corporate interests and would have the practical effect of depriving many defrauded investors the ability to recover their losses.

Among the provisions of S. 667 that I support are: (1) an innovative early evaluation procedure designed to weed out clearly frivolous cases; (2) a more rational system of determining liability among defendants; (3) certification of complaints and improved case management procedures; (4) curbs on potentially abusive attorney practices; (5) improved disclosure of settlement terms; (6) a reasonable safe harbor for forward looking statements; (7) restoration of aiding and abetting liability; (8) a reasonable extension of the statute of limitations for securities fraud suits; (9) codification of the recklessness standard of liability as adopted by virtually every U.S. Circuit Court of Appeals; and (10) rulemaking authority to the SEC with respect to fraud-on-the-market cases. A detailed comparative analysis between S. 667 and S. 240 is enclosed.

S. 667 proves that it is possible to craft securities litigation reform measures that target abusive practices without sacrificing the opportunity for recovery by defrauding investors. Therefore, I strongly encourage you to become a co-sponsor of S. 667.

Securities litigation reform is one of the most important issues for small investors that will be considered by the 104th Congress. It is my hope that the Senate will give serious consideration to S. 667 as the appropriate response for constructive improvement in the federal securities litigation process. If you have any questions about my position on securities litigation reform, please do not hesitate to contact me at (215) 635-6262 or Deputy Chief Counsel G. Philip Rutledge at (717) 783-5130. I would be pleased to provide you or your staff with any additional information you may require on this most important issue to individual Pennsylvania investors.

Very truly yours,

ROBERT M. LAM,
Chairman

PENNSYLVANIA
SECURITIES COMMISSION,
COMMONWEALTH OF PENNSYLVANIA,

June 20, 1995.

Re: amendments to Senate bill 240, "Private Securities Litigation Reform Act"

Hon. ARLEN SPECTER,
U.S. Senate, 530 Hart Senate Office Building,
Washington, DC.

DEAR ARLEN: It is my understanding that Senate Bill 240 is now before the full U.S. Senate for consideration.

The Pennsylvania Securities Commission is charged under the Pennsylvania Securities Act of 1972 with the protection of investors. While the Commission has stated its position in previous correspondence (April 17, 1995) that it favors certain securities litigation reforms (as contained in S.667), it believes that S.240, as currently constituted, does not achieve the appropriate balance between protecting investors and discouraging frivolous lawsuits against honest companies and professionals. Instead, the practical effect of S.240 would be the elimination of private actions under federal law for Pennsylvanians who found themselves to be a victim of securities fraud.

It is my understanding that amendments to S.240 will be offered on the Senate floor to strengthen its investor protection provisions, i.e. extending the statute of limitations for civil securities fraud actions (Pennsylvania recently extended its statute of limitations period for securities fraud to four years); fully restoring liability for aiding and abetting securities fraud; restoring joint and several liability so defrauded investors can be made whole; and peeling back the immunity for companies to make outrageous claims of future profits or performance.

The Commission asks you to support adoption of these amendments. If, however, all these vital investor protection amendments are not adopted, the Commission, on behalf of Pennsylvania investors, strongly urges you to vote against S.240.

As presently constituted, S. 240 not only would affect negatively Pennsylvania investors but also Pennsylvania taxpayers should the Commonwealth Treasury Department again become a potential victim of wrongdoing in securities transactions undertaken on behalf of the Commonwealth. The importance of the potential negative effects of this Bill on the Commonwealth is reflected by the Treasury Department's recent suit against Salomon Brothers for damages resulting from alleged wrongful conduct engaged in by Salomon in connection with its bidding on government bonds.

As a participant in the capital formation process, I would like to emphasize that our financial markets run most efficiently when there is a high degree of public confidence in the integrity of the marketplace. Money is merely the medium of exchange between this confidence and the honest entrepreneur. As written, S. 240 will not advance the goal of making capital available to growing U.S. companies. It will result in small investors avoiding participation in our capital markets when they discover that they are unable to bring suit against the perpetrators or aiders and abettors of a securities fraud or, upon winning such a suit, fail to be made whole because of the Bill adopts the concept of "caps" on total defendant liability.

Thank you for considering our views. If you or your staff have any questions concerning how this Bill negatively affects Pennsylvania and Pennsylvania investors, please contact G. Philip Rutledge or K. Robert Bertram of the Commission staff at (717) 783-5130.

Very truly yours,

ROBERT M. LAM,
Chairman.

Mr. BENNETT addressed the Chair. The PRESIDING OFFICER. The Senator from Utah.

Mr. BENNETT. Mr. President, the Senator from Illinois has been patient and is scheduled to be the next speaker.

Before we hear from her, I have been asked to perform a few housekeeping details. Senator HATCH, the chairman of the Judiciary Committee, has asked me to announce on his behalf that he cannot come here at the moment. I am sure the Senator from Illinois is delighted that that means she will not be delayed further. But he did ask that the statement be made on his behalf that as chairman of the Judiciary Committee he opposes the referral contained within this motion.

I ask unanimous consent that at 8:30 this evening Senator D'AMATO be recognized to make a motion to table the motion to commit the bill.

The PRESIDING OFFICER. Is there objection?

Mr. SPECTER. Reserving the right to object, there are issues, and I need to discuss them with the chairman which I talked to him about earlier. And also my principal cosponsor, Senator BIDEN, is not available yet to make an argument.

Mr. BENNETT. Mr. President, I renew the unanimous consent request that at 8:30 this evening Senator D'AMATO be recognized to make a motion to table the motion to commit the bill.

The PRESIDING OFFICER. Is there objection?

Mr. SPECTER. I object.

The PRESIDING OFFICER. Objection is heard.

Mr. SARBANES. Mr. President, parliamentary inquiry? What is the parliamentary situation here?

The PRESIDING OFFICER. There is a motion to commit the bill to the Judiciary Committee pending.

Mr. SARBANES. Is there further debate in order?

The PRESIDING OFFICER. There is.

Mr. SARBANES. On the motion or on the bill? Either?

The PRESIDING OFFICER. The motion is pending. You can debate either.

Mr. D'AMATO. At the conclusion of Senator BIDEN's remarks, I ask unanimous consent that he yield the floor back to me for the purpose of making a tabling motion. I would like to simply state that Senator HATCH has indicated that he is not in favor of the motion for sequential referral, and that this is not a new matter. This matter has legislatively been on an agenda now for some four years. That is the only comment I will make.

I will yield the floor.

Mr. BIDEN addressed the Chair.

The PRESIDING OFFICER. The Senator from Delaware is recognized.

Mr. BIDEN. Mr. President, I thank the Senator from New York. What I am about to say, I say standing next to my good friend from Connecticut, Senator DODD, who has worked tirelessly on

this bill, with which I disagree, but I want to make a very brief statement.

I strongly support the position taken by the Senator from Pennsylvania. This litigation makes numerous precedent-setting changes in the country's judicial system. While my colleagues in the Banking Committee had a chance to examine the changes the bill would make to our Nation's security laws, it seems to me that we may have skipped a very important step. The so-called Securities Reform Act makes significant revisions to the Federal rules of evidence relating to mandatory rule 11 sanctions and rule 26 discovery proceedings, and yet, it has not been referred to the Judiciary Committee.

I hold myself partially responsible for that. In truth, I say to my friend from Connecticut, I should have been hollering for this in my committee before this time. I was mildly preoccupied with other things before the committee. To tell you the truth, it was called to my attention by my friend from Pennsylvania, and I realize this is a serious mistake, in my view, and that we have not had this before the Judiciary Committee.

In the past, bills that have made changes to the Federal rules of evidence were referred to the Judiciary Committee to enable the committee with expertise to review the work on this legislation. This bills is no different. Similarly, limiting joint and several liability, restricting the statute of limitations, changing the rules of class action suits in favor of large investors, are all judiciary-related issues. Yet, the Judiciary Committee never had a day of hearing on any of these specific issues.

If the bill becomes law, companies could potentially get away with making misleading, even fraudulent, statements about their earnings. Yet, to win a class action suit, you would have to prove a falsehood was made with a clear intent to deceive. That is an incredibly tough standard. I will admit some frivolous lawsuits are filed. Some lawyers do make too much from a suit, leaving defrauded investors with little. But I do not believe this massive bill is the answer.

So in order to protect the small investors, it seems to me that we should at least look at the significant changes in the rules of evidence. If this bill passes, I make the prediction to us all here, we will be back in two, three, four years undoing it, after another Orange County or another insider trading scandal, or after millions of people are defrauded with some other scam that occurs.

Quite frankly, I think we would be wise to take a close look, with a specific time for referral, if need be, to the Judiciary Committee, to look at these changes in the rule of ethics.

I do not profess to have expertise in the securities industry, but we do know something about the rules of evidence and the shifting burden of truth.

I thank my colleague for his indulgence, and I thank the Senator from Il-

linois. I thank the Senator from Connecticut for not getting up and saying, "Why, JOE, did you not do this earlier?" I yield the floor.

Mr. D'AMATO. Mr. President, I intend to make a motion to table.

Mr. DODD. Mr. President, will my colleague yield?

Mr. D'AMATO. I am happy to yield.

Mr. DODD. Just to say, Mr. President, this has been about 4 years on this matter.

This hour, we are now under consideration of the bill—I say this with all due respect to my good friends on the Judiciary Committee; it has been no secret that this legislation has been pending—at this particular hour to secure sequential referral, in effect, would kill the legislation.

I think all of our colleagues ought to be aware of that at this juncture. This is our opportunity in a moment to move on this. We have had extensive hearings, heard from lawyers and others on all sides, and worked closely with them.

With all due respect to our colleagues on the Judiciary Committee, I would hope this motion to table would be approved.

Mr. D'AMATO. Mr. President, I move to table the motion. I ask for the yeas and nays.

The PRESIDING OFFICER. Is there a sufficient second?

There is a sufficient second.

The yeas and nays were ordered.

The PRESIDING OFFICER. The question is on agreeing to the motion to table the motion to commit. The clerk will call the roll.

The legislative clerk called the roll.

Mr. DOLE. I announce that the Senator from Texas [Mr. GRAMM], the Senator from North Carolina [Mr. HELMS], the Senator from Idaho [Mr. [KEMPTHORNE]], and the Senator from Mississippi [Mr. LOTT] are necessarily absent.

Mr. FORD. I announce that the Senator from New Mexico [Mr. BINGAMAN], the Senator from New Jersey [Mr. BRADLEY], the Senator from Arkansas [Mr. BUMPERS], the Senator from Hawaii [Mr. INOUE], the Senator from Nebraska [Mr. KERRY], the Senator from New Jersey [Mr. LAUTENBERG], and the Senator from Arkansas [Mr. PRYOR] are necessarily absent.

The PRESIDING OFFICER. Are there any other Senators in the Chamber desiring to vote?

The result was announced—yeas 69, nays 19, as follows:

[Rollcall Vote No. 281 Leg.]

YEAS—69

Abraham	Coverdell	Frist
Ashcroft	Craig	Glenn
Baucus	D'Amato	Gorton
Bennett	DeWine	Grams
Brown	Dodd	Grassley
Burns	Dole	Gregg
Campbell	Domenici	Harkin
Chafee	Dorgan	Hatch
Coats	Exon	Hatfield
Cochran	Faircloth	Hutchison
Cohen	Feinstein	Inhofe
Conrad	Ford	Jeffords

Johnston	Moseley-Braun	Rockefeller
Kassebaum	Moynihan	Roth
Kerry	Murkowski	Santorum
Kohl	Murray	Simpson
Kyl	Nickles	Smith
Levin	Nunn	Snowe
Lieberman	Packwood	Stevens
Lugar	Pell	Thomas
Mack	Pressler	Thompson
McConnell	Reid	Thurmond
Mikulski	Robb	Warner

NAYS—19

Akaka	Feingold	Sarbanes
Biden	Graham	Shelby
Boxer	Heflin	Simon
Breaux	Hollings	Specter
Bryan	Kennedy	Wellstone
Byrd	Leahy	
Daschle	McCain	

ANSWERED 'PRESENT'—1

Bond

NOT VOTING—11

Bingaman	Helms	Lautenberg
Bradley	Inouye	Lott
Bumpers	Kempthorne	Pryor
Gramm	Kerrey	

So the motion to lay on the table the motion to commit was agreed to.

Mr. DOMENICI. Mr. President, I move to reconsider the vote by which the motion was agreed to.

Mr. FORD. I move to lay that motion on the table.

The motion to lay on the table was agreed to.

CHANGE OF VOTE

Mr. REID. Mr. President, on rollcall vote 281, I was recorded as voting "no." It was my intention to vote "aye." Therefore, I ask unanimous consent that I be permitted to change my vote. This will in no way change the outcome of the vote.

This request has been cleared by both the majority and the minority.

The PRESIDING OFFICER. Without objection, it is so ordered.

(The foregoing tally has been changed to reflect the above order.)

Mr. STEVENS. Regular order.

NATIONAL HIGHWAY SYSTEM DESIGNATION ACT

The Senate continued with the consideration of the bill.

Mr. DOLE addressed the Chair.

The PRESIDING OFFICER. The majority leader.

Mr. DOLE. Mr. President, let me explain that under our previous agreement, when I call for the regular order, the highway bill comes back. I understand they have agreed to the Stevens-Murkowski amendment with Senator BUMPERS. That would be adopted. There would be speeches for the record; very short. Then we would proceed to final passage of the highway bill.

Mr. CHAFEE. Right, by voice vote.

Mr. DOLE. Does anybody request a rollcall on final passage?

I ask unanimous consent that once the amendment is agreed to, and the committee substitute, as amended, is agreed to, the bill will be advanced to third reading, the bill passed, and the motion to reconsider be laid on the table, with the above occurring without any intervening action.

The PRESIDING OFFICER. Without objection, it is so ordered.

ORDER OF PROCEDURE

Mr. DOLE. There will be no more votes tonight. There will be a vote at 10:55 tomorrow morning. The first vote will be at 10:55. It will be on the amendment by the Senator from Alabama, Senator SHELBY, and Senator BRYAN.

Mr. STEVENS addressed the Chair.

The PRESIDING OFFICER. The Senator from Alaska.

AMENDMENT NO. 1467

Mr. STEVENS. Mr. President, I have an amendment at the desk, and I ask for its immediate consideration.

The PRESIDING OFFICER. At the request of the majority leader, S. 440 is now the pending business.

The clerk will report.

The legislative clerk read as follows:

The Senator from Alaska [Mr. STEVENS], for himself, Mr. MURKOWSKI, Mrs. HUTCHISON, and Mr. BENNETT, proposes an amendment numbered 1467.

At the appropriate place in title I of the bill insert the following new section:

SEC. . MORATORIUM.

(a) IN GENERAL.—Notwithstanding any other provision of law, no agency of the Federal government may take any action to prepare, promulgate, or implement any rule or regulation addressing rights of way authorized pursuant to Revised Statutes 2477 (43 U.S.C. 932), as such law was in effect prior to October 21, 1976.

(b) This section shall cease to have any force or effect after December 1, 1995.

Mr. STEVENS. Mr. President, in response to the request, we have agreed to this amendment which is a moratorium on proceeding with the regulations as proposed by the Department of the Interior that have not been issued in final form yet, but we know they are under consideration.

Let me state that this amendment does not affect any judicial action or decision instituted since 1976, any pending judicial action or any future judicial action. It is not intended to affect any case law with respect to rights of way granted pursuant to Revised Statutes 2477. This deals simply with the proposal to issue regulations to, in effect, determine through sovereign power that the rights of the States would be invaded as those States rights were known under Revised Statutes 2477, which was repealed in 1976.

I have offered this on behalf of my colleague Senator MURKOWSKI and the two Senators from Utah, Senator HATCH and Senator BENNETT. I do believe it will achieve the goal of just having a moratorium on the preparation of regulations so that the committees involved and the States involved may try to work this out without very expensive litigation that would ensue, and in the case of our State it would be just a disastrous prospect of litigating some 600 or more separate rights-of-way.

I am grateful to the Senate for having delayed the action until this time to enable us to have a proposal go to the House, which I hope the House will agree with, to establish this morato-

rium. It will simply delay the process as far as the administrative regulations that were proposed by the Department of the Interior.

Mr. MURKOWSKI addressed the Chair.

The PRESIDING OFFICER. The Senator Alaska.

Mr. MURKOWSKI. I thank the Chair.

Mr. President, I am glad we could come to an agreement on an amendment to restrict the Department of the Interior or any other Federal agency from taking any action on finalizing a rule or regulation with respect to Revised Statute 2477 until December 1, 1995. This will allow some of my colleagues, including my colleague from Arkansas, to take a careful look at this issue. I want to make it clear that we will be offering legislation in the future to resolve this problem for Alaska.

R.S. 2477 simply states: The right-of-way for the construction of highways over public lands, not reserved for public uses, is hereby granted. The 1866 law was repealed by FLPMA in 1976. But between 1866 and 1976, R.S. 2477 allowed the creation of property rights across Federal lands for rights-of-way. These rights-of-way have provided essential access through the Western States—and especially in Alaska. Recognizing this, Congress intentionally protected the R.S. 2477 rights-of-way in FLPMA. However, the Department of the Interior proposed regulations in August of 1994 to make it much more difficult to establish right-of-way claims across Federal lands established under the Revised Statutes 2477.

DOI claims the reason they are doing the regulations is to make a logical process to get R.S. 2477 rights-of-way recognized. BUT the regulations would actually:

Override State law with restrictive new definitions of highway and construction;

Put a cloud on the title to R.S. 2477 roads, treating them as invalid until proven valid;

Prevent any future expansion of scope of an R.S. 2477 right-of-way, preventing making the right-of-way any wider, so a dogsled trail will remain a dog sled trail;

Set a sunset on administrative and court action on validity of R.S. 2477 by extinguishing claims not filed within 2 years and 30 days after final rule is issued;

Although a claimant could still turn to the courts, DOI states that the regulations serve as notice to claimants for purpose of the Quiet Title Act, which provides a 12-year statute of limitations—but true to form, DOI did not put a time limit on themselves to process the claims;

Construction and maintenance will not be permitted without approval of DOI with 3 days notice, preventing the fixing of washed out roads until DOI approval.

The draft R.S. 2477 regulations from the Department of the Interior are nothing more than an attempt to prevent legal access across our public