THE PRIVATE SECURITIES LITIGATION REFORM ACT IN A POST-ENRON WORLD

by

Larry Bumgardner*

Suppose that a high-tech company, which has seen its publicly traded stock soar in the few years since its initial public offering, reports that it expects the current quarter of its fiscal year to yield a small profit. However, circumstances change, and the company actually loses money that quarter. Predictably, the stock plummets. Just as predictably, shareholders then sue the company for securities fraud, claiming to have been misled and harmed financially by the company's inaccurate statements.

Should the shareholders, who clearly suffered at least short-term damage, be able to recover their losses? By contrast, was this an unforeseeable circumstance for which the company has no liability? Or was this merely a natural reaction in a volatile stock market? Obviously, more facts on exactly what the company said and what actually caused the loss are needed to venture a guess on the fair outcome of this hypothetical. However, corporations in the United States would argue that absolutely no more facts than these would be needed to prompt some shareholders, urged on by plaintiffs' attorneys, to bring a frivolous class action lawsuit against the company under federal securities laws.

Long before "Enron" became a codeword for corporate and financial disaster, these so-called "strike suits" against publicly owned corporations had been a controversial issue in both the securities industry and the legal profession. The proliferation of these suits in the early 1990s led Congress to attempt to deter such claims by enacting the Private Securities Litigation Reform Act of 1995 (PSLRA).[1] The true impact of this statute has been debated since, and even federal courts applying the law have not agreed on its meaning.

But what was primarily a legal debate at the outset has become a very practical and personal matter for the thousands of shareholders and employees who lost their investments, jobs, and much of their retirement in the Enron debacle. The continuing revelations about Enron, its auditor Arthur Andersen, and most recently WorldCom and similar business scandals have reinvigorated debate about the PSLRA and led to calls to revise the law. This paper will study the history and details of the 1995 law, briefly consider some of the issues still unresolved from judicial interpretation of the act, and analyze the current proposals for change.

Brief History of the PSLRA

The failure of many savings and loan associations in the late 1980s, highlighted by the infamous Charles Keating case, might be considered the most significant and immediate catalyst for passage of the PSLRA. According to some estimates, accounting firms had to pay $1.6 billion in penalties and settlements as a result of the savings and loan crisis.[2] Under the concept of joint and several liability at that time, an accounting firm that had audited the books of a savings and loan could be made to pay for the full loss to investors if the financial institution that actually committed the fraud had gone bankrupt or was otherwise unable to compensate the victims.

Initially, this savings and loan crisis provided the impetus for creating a new business form, the limited liability partnership, to protect the personal assets of innocent partners of an accounting firm from the misdeeds of their partners. However, the LLP form did not protect the partnership itself, or

*Associate Professor of Business Law, Pepperdine University, Malibu, CA

partnership assets, from such suits. Thus, accounting firms sought relief from securities law provisions allowing shareholders to recover damages from both the company making inaccurate statements and from the accounting firm that audited that company's books. The most important such provision is found in the Securities and Exchange Commission's Rule 10b-5, promulgated under the Securities Exchange Act of 1934, which makes it illegal "to make any untrue statement of a material fact or to omit to state a material fact," or to "engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person."[3]

Beyond accounting firms, many corporations, especially those in the volatile high-technology world, also felt victimized by these strike suits. Analogizing them to "nuisance suits" in other areas of litigation, the corporate world argued that most of these class action shareholder suits were baseless and were merely efforts to force companies to agree to settlements rather than take the more expensive and less certain route of litigating claims that might result in large damages. Corporations therefore sought much stricter limits on shareholders' ability to bring and to recover under these class action suits.

Still, it took a major shift in the national political climate to make significant reform of these securities law provisions a realistic possibility. When Republican Party candidates for Congress proposed a "Contract with America" as part of the 1994 election campaign, one of the ten planks of the contract promised "common sense legal reform," which included a limit on class action shareholder suits.[4] Once Republicans in the November 1994 election gained control of both houses of Congress for the first time since 1954, an effort to limit these strike suits became a top priority for new House Speaker Newt Gingrich and his Republican majority.

The high-stakes battle between the corporate world and trial lawyers, especially a small group that specialized in securities class action lawsuits, continued throughout 1995 over the specific provisions of what came to be known as the Private Securities Litigation Reform Act. Indicative of the sharp tone of the debate, Senator Alfonse D'Amato of New York, one of the Republican sponsors of the measure, called the proposal an effort to stop "legal blackmail."[5] By contrast, opponent and consumer advocate (and, more recently, presidential candidate) Ralph Nader labeled the measure a "crooks and swindlers protection act."[6]

Moving with unusual speed, the House of Representatives passed a strong version of the bill by early March of 1995. The Senate approved a somewhat watered-down version by late June. A conference committee then produced a compromise measure, although this final product was closer to the Senate version than to the tougher House proposal. Both houses accepted the compromise and passed the bill in early December. Although the White House had sent mixed signals on its view of the legislation, President Clinton surprised some by vetoing the measure only hours before it would have become law without his signature.[7] With bipartisan support, both houses of Congress then quickly mustered the two-thirds majority needed to override the veto, and the PSLRA became law on December 22, 1995. Three years into his first term, it was President Clinton's first veto to be overridden. A headline in *The Wall Street Journal* succinctly summarized the situation: "Congress Sends Business a Christmas Gift."[8]

Substantive Provisions of the New Law

The exact value of this Christmas gift to the business world, however, was never as clear as the headline indicated. Congress certainly intended to restrict these strike suits, noting in the conference committee report that it had "been prompted by significant evidence of abuse in private securities lawsuits."[9] Some of the specific problems cited by the conference committee included the "routine filing" of such lawsuits whenever a stock price dropped, "targeting of deep pocket defendants," and misuse of both discovery and class action processes, all leading to the result that "innocent parties are often forced to pay exorbitant 'settlements.'"[10] To address these and other issues, the PSLRA added significant provisions to the two primary federal securities statutes, the Securities Act of 1933 and the

Securities Exchange Act of 1934. Although the PSLRA is an extensive piece of legislation and much of its detail is beyond the scope of this paper, several specific provisions affecting both substantive and procedural aspects of securities law require greater attention and description.

First, the law strives to reduce potential liability for a company's incorrect earnings projections, announcements about plans for future operations, or other "forward-looking statements." Building on weaker but similar provisions found in case law and in an SEC rule, the PSLRA provides corporations facing a securities fraud suit a statutory "safe harbor," meaning that they cannot be held liable for inaccurate statements in such projections as long as one of three requirements is met. Two ways to qualify for this safe harbor are that the false statement is immaterial, or that the plaintiff cannot prove the statement was made with actual knowledge that it was false or misleading. The third and most significant option is that the statement is "identified as a forward-looking statement, and is accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement."[11] This part of the PSLRA explains the prevalence of forward-looking statement disclaimers at the end of most corporate press releases today. However, it was also a controversial provision, with opponents of the law calling it a "safe ocean," rather than a safe harbor.[12]

A second major element of the law deals with the amount of proof that a plaintiff needs to make a viable claim of securities fraud. The purpose is to make it easier for a corporate defendant to have a meritless claim dismissed at the pleadings stage, thus avoiding the time and expense of a lengthy trial or the need to settle such a case. Seeking to resolve a split in the federal courts on how specifically fraud must be alleged, the new law requires a plaintiff's complaint alleging a misstatement or omission of material fact to "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 complaint shall state with particularity all facts on which that belief is formed."[13]

In addition, this provision of the PSLRA also deals with cases alleging that the defendant acted with scienter, which has been defined by the Supreme Court as "a mental state embracing intent to deceive, manipulate, or defraud."[14] In such cases, the new law requires that the plaintiff's complaint, for each allegedly fraudulent act or omission, "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind."[15] Further, the statute instructs courts to dismiss the complaint if these requirements are not met, giving defendants a strong weapon to use in the early stages of the lawsuit. However, as the convoluted language of this portion of the PSLRA is quite ambiguous itself, these two provisions on pleading standards may have actually created more questions than they answered. Indeed, as will be addressed later in this paper, these provisions remain the subject of extensive judicial debate.

A third substantive change under the PSLRA revises the applicability of joint and several liability in securities fraud verdicts. It seeks to shield a defendant with arguably limited responsibility for the fraud, such as accounting firms and law firms hired by the corporate defendant, from having to pay the full judgment when the corporation becomes insolvent and thus unable to pay. As the conference committee report noted:

> One of the most manifestly unfair aspects of the current system of securities litigation is its imposition of liability on one party for injury actually caused by another. Under current law, a single defendant who has been found to be 1% liable may be forced to pay 100% of the damages in the case. The Conference Committee remedies this injustice by providing a "fair share" system of proportionate liability. … The current system of joint and several liability creates coercive pressure for entirely innocent parties to settle meritless claims rather than risk exposing themselves to liability for a grossly disproportionate share of the damages in the case."[16]

Under the new law, a defendant is subject to joint and several liability only if that defendant "knowingly committed a violation of the securities laws" or if the plaintiff has a net worth of less than

$200,000 and the plaintiff's losses from the fraud are more than 10 percent of that net worth.[17] Otherwise, a defendant is responsible only for its percentage share of responsibility, as determined by a procedure specified in the act.[18] For example, if an accounting firm is found to be only 10 percent responsible when the proven damages are $10 million, the accounting firm normally will be responsible for paying only $1 million in damages under the new law's proportionate share approach, rather than as much as the full $10 million under joint and several liability.

In exchange for this significant benefit to accounting firms, the statute also addresses an auditor's duty to notify management if the audit process uncovers any illegal acts at a corporation being audited. For the most part, the PSLRA codifies what were already self-imposed professional obligations under generally accepted auditing standards.[19] However, of perhaps even greater import today in light of current accounting scandals, the law adds a new requirement -- that the auditor also report any such illegal act to the SEC, if management does not respond appropriately. A 1996 article co-authored by Harvey Pitt, then a securities lawyer in private practice but now chairman of the SEC, concluded that the act "embraces and strengthens the need for auditors to employ specific procedures designed to uncover illegal acts that could have a material impact on clients' financial statements."[20] Moreover, the conference committee report notes that the SEC would have authority to act if existing auditing standards proved inadequate:

> The SEC should not act to "modify" or "supplement" generally accepted auditing standards for SEC registrants until after it has determined that the private sector is unable or unwilling to do so on a timely basis. The Conference Committee intends for the SEC to have discretion, however, to determine the appropriateness and timeliness of the private sector response. The SEC should act promptly if required by the public interest or for the protection of investors.[21]

In addition to limiting the applicability of joint and several liability, the statute also reduces potential damages in strike suits by making a minor amendment to the Racketeer Influenced and Corrupt Organizations Act. RICO provides for treble damages for plaintiffs in civil suits, and securities fraud had been considered a "predicate act" that could trigger a RICO civil suit. As a result, many securities fraud suits included a RICO claim, raising the stakes for defendants in terms of both damages and reputation. With the concurrence of the SEC, the PSLRA removed securities fraud from the definition of racketeering activity for a civil (but not criminal) RICO claim -- another effort to reduce pressure on corporate defendants to settle frivolous claims.[22]

The PSLRA's Procedural Changes

The act's other major changes might be considered more procedural in nature, although many of these may also have at least an indirect effect on the substantive outcome of strike suits. For example, the statute makes several changes affecting the process of filing these class action claims. Previously, the conference committee noted, plaintiffs' attorneys had an incentive to be the first to file a strike suit against a particular corporation, because the first plaintiff was generally named the lead plaintiff and that plaintiff's attorney was usually appointed as counsel for the class action.[23]

Instead, the new law says that the plaintiff with the largest financial stake is presumed (subject to rebuttal) to be the "most adequate plaintiff" and should be chosen as lead plaintiff, and similarly eliminates the financial incentive to be named the lead plaintiff by requiring that the lead plaintiff receive only a pro rata share of the damages based on the loss incurred, with no bounty payments or bonuses allowed.[24] Further, the lead plaintiff is then allowed to choose counsel for the class action. The advantage, according to the committee report, is that "the Conference Committee expects that the plaintiff will choose counsel rather than, as is true today, counsel choosing plaintiff."[25]

The PSLRA also significantly alters the discovery process in an effort to prevent "fishing expedition" lawsuits, where a non-specific or even boilerplate complaint might be used to justify extensive (and expensive) discovery of a corporate defendant's records in order to search for evidence to support the allegations of securities fraud. Under the new law, if the defendant files a motion to dismiss, the discovery process must be stayed while that motion is being considered (with limited exceptions if the court finds that "particularized discovery is necessary to preserve evidence or to prevent undue prejudice").[26] Some observers contend that this provision, coupled with the heightened pleading standards of the statute, creates a Catch-22 situation: Plaintiffs must "state with particularity" the facts showing securities fraud to defeat a motion to dismiss, but they are not allowed to conduct discovery to gain the necessary information while the dismissal motion is pending.[27]

Finally, the law seeks to deter nuisance claims by increasing the likelihood that a court will impose sanctions on plaintiffs who bring "frivolous" suits. The conference committee and ultimately Congress rejected the tougher House provision calling for a general "loser-pays" approach for securities fraud suits.[28] Instead, the PSLRA requires the court, at the conclusion of the case, to determine specifically if the claim violates the general federal court rules against frivolous lawsuits. If so, the court then must impose sanctions on the losing party, and the sanctions are presumed, in the absence of rebuttal evidence, to be reasonable attorneys' fees and other costs.[29]

Whether these and the remaining provisions of the PSLRA have actually accomplished the congressional purpose of reducing unwarranted securities fraud claims is not entirely clear. According to surveys conducted by PricewaterhouseCoopers, the number of securities fraud class action suits actually increased significantly for three years after passage of the 1995 law.[30] They peaked in 1998 before showing modest declines in 1999 and 2000.[31] But by 2001, a new record of 483 shareholder suits more than doubled the total for 2000, although nearly two-thirds of the 2001 filings raised a new type of claim involving allocation of shares in initial public offerings.[32] Another study by the National Economic Research Associates showed that the average size of settlements from 1996 through 1999 was more than 40 percent higher than before the law's enactment.[33] However, these statistics alone may be of limited value in determining the impact of the PSLRA. The presence of many other variables -- ranging from fluctuating stock market and economic conditions to the possible rise of legitimate (as opposed to frivolous) securities fraud claims -- makes it difficult to prove exactly what effect the new law has had on the number and on the success or failure of strike suits.

Court Interpretations

The uncertainty about the law's overall impact is further complicated by continuing disagreement in the federal courts on interpretation of the PSLRA. The ambiguous language of the statute itself and the relatively brief period of time since its enactment have contributed to the unsettled state of the case law. An additional key factor is the absence of any guidance from the Supreme Court, which to date has not decided any cases affecting the meaning of the PSLRA.

The Supreme Court's only direct mention of the law is a passing reference in one opinion in 2001. In *Wharf (Holdings) Ltd. v. United International Holdings, Inc.*,[34] the justices upheld a securities fraud verdict for conduct that occurred before passage of the PSLRA. In rejecting the defendant's argument that this decision could encourage many more securities fraud claims, the Court's opinion notes that the PSLRA imposes "beginning in 1995, stricter pleading requirements in private securities fraud actions that, among other things, required that a complaint 'state with particularity facts giving rise to a strong inference that the defendant acted with the required [fraudulent] state of mind.'"[35] From that one reference, the Court merely reinforces the settled notion that the law was intended to create stricter pleading requirements, but does nothing to elaborate on the exact meaning of the language of the statute.

The pleading standard, in fact, is the provision of the PSLRA that has caused the most disagreement in lower federal courts. Although an extensive review of the issue is not necessary for purposes of this paper, many law review articles have provided detailed analyses of this matter. Conceivably, the outcome of a securities fraud claim may now hinge on where the case is brought, as various federal circuits have yielded at least a three-way split on the meaning of the PSLRA's pleading requirements.[36]

Some of the unresolved questions include whether recklessness by the defendant is enough to prove scienter (and thus give the plaintiff a viable claim), and whether courts must also distinguish between "simple recklessness" and "deliberate or conscious recklessness."[37] Further, can the strong inference of fraudulent intent required by the act be shown by facts "establishing a motive to commit fraud and an opportunity to do so"?[38] Or, must the defendants have received some specific benefit from the purported fraud to support the strong inference of scienter?[39] Although some commentators recently have sought to reconcile differences in the circuit court rulings,[40] a clear statement from the Supreme Court on the issue is the only way to provide even some hope of clarity and consistency on this threshold question for securities fraud claims.

The parameters of the PSLRA's safe harbor for forward-looking statements are also uncertain, although to a lesser degree than for the pleading standard. One cleverly worded summary by attorneys analyzing safe harbor cases notes that case law is "not very clear on either the Safe Harbor's protective 'depth,' or the precise mechanics of how issuers can successfully 'dock' with it to minimize the likelihood of securities litigation."[41] For example, some federal district courts have substantially limited the value of the safe harbor by finding that it does not apply "if a plaintiff alleges that the defendants omitted a material existing fact in connection with the forward-looking statement."[42] Yet, other courts have explicitly rejected this "omission" exception from the safe harbor.[43]

On the issue of sanctions for frivolous claims, supporters of the PSLRA believe that federal courts have been far too reluctant to use even the less-severe sanctions provision of the compromise legislation (as opposed to the loser-pays approach in the original House bill). Sanctions have been rarely imposed as various courts have ruled, for example, that the plaintiff's case was not "wholly frivolous" or even that a law review article might suffice to support the plaintiff's theory.[44] Still, similar to the question of whether the PSLRA as a whole has deterred frivolous claims, other possible variables in the equation may mean it is too early to draw conclusions on the effectiveness or need for the act's sanctions provision.[45]

Enron, Andersen, and Current Debate

The scandal involving Enron and Andersen will provide both a test and a showcase for the PSLRA. Shareholder suits already filed against these and related defendants may help further define and explain the law, if the cases are not settled and actually proceed through the courts. Moreover, the final outcome of these cases likely will affect public and congressional opinion of the statute and class action shareholder suits in general.

Already, various provisions of the PSLRA have come into play in the early stages of the litigation. The University of California, with a sizable loss but arguably not the largest financial loss, was selected as lead plaintiff for the Enron case in a heated competition. Following the procedure established by the PSLRA, a federal judge found that the presumption for the plaintiff with the largest financial loss had been rebutted.[46] The judge also selected the University of California's counsel, William Lerach of Milberg Weiss Bershad Hynes & Lerach, as lead counsel.[47] Ironically, that is the plaintiffs' law firm that helped inspire passage of the PSLRA because of its reputation for aggressively bringing class action shareholder suits. Moreover, battles have already erupted over what discovery will be allowed, or whether the typical PSLRA stay of discovery will apply until any dismissal motions have been considered.[48]

Of course, with a final resolution of the Enron litigation not likely for several years, critics of the PSLRA will not wait for that outcome. In fact, some argue that the law's enactment helped create the Enron scandal. Former federal judge Abner Mikva, who was White House counsel when President Clinton vetoed the law, writes: "While the Enron culprits, whoever they are, embraced greed with particular enthusiasm, their greed was given a huge assist by … the Private Securities Litigation Reform Act. … Simply put, Congress reduced the incentives against committing fraud."[49] By contrast, SEC Chairman Pitt, responding to a question during his congressional testimony, contended: "Anybody who says that the class action legislation contributed to Enron is very, very much mistaken."[50]

Congressional Proposals and Action

Apparently sharing Mikva's view, some members of Congress are seeking changes to the PSLRA. By one count, more than 40 bills that could affect the PSLRA have been introduced in Congress.[51] Further, in a clear reaction to Enron, there are more bills proposing a wide variety of other changes to securities law, corporate governance, pension reform, and even bankruptcy law. However, of those bills specifically aimed at the provisions of the PSLRA, much of the attention initially was focused on two specific proposals.

First, the proposed Accountability for Accountants Act, introduced in the House by Representative Edward Markey, a Democrat from Massachusetts, would reverse several provisions of the PSLRA dealing with auditors.[52] Specifically, it seeks to restore joint and several liability for accounting firms that audit a corporation accused of securities fraud if the corporation is insolvent, or if the accounting firm serves as both auditor and consultant to the corporation. Further, the discovery stay of the PSLRA would no longer apply to the auditor of a corporation sued for securities fraud.[53]

In addition, the Markey bill would effectively reverse a U.S. Supreme Court decision that limited auditor liability in securities fraud actions. In *Central Bank of Denver v. First Interstate Bank of Denver,*[54] the Supreme Court in 1994 interpreted existing federal securities law to hold that defendants that merely aid and abet securities fraud (as opposed to being primarily responsible for the fraud) are not liable to private shareholders suing for damages under Rule 10b-5. The following year, in the wake of *Central Bank*, the SEC and others sought to have Congress include a provision in the PSLRA to make it clear that Congress did indeed intend for aiding and abetting liability to extend to shareholder suits. Congress declined to do so, instead adding to the PSLRA a provision stating that the SEC retains the power to bring a government action based on aiding and abetting liability, implicitly approving the Supreme Court's ruling as to private shareholder suits.[55] The Markey bill, if enacted, would reinstate aiding and abetting liability for private suits.

This issue is especially pertinent to the Enron litigation, although any change to the PSLRA is not likely to be retroactive. Since the Supreme Court's ruling in *Central Bank*, lower courts have struggled with exactly where to draw the line between primary liability and secondary (aiding and abetting) liability.[56] Not surprisingly, with Enron in bankruptcy proceedings and Andersen's future in severe doubt, the current shareholder suit against Enron also names two of Enron's law firms, Vinson & Elkins and Kirkland & Ellis, as defendants. Moreover, the complaint seeks to portray both law firms as active participants in the fraud so that they will be judged primarily liable and thus not eligible for the protection available to defendants who only aid and abet securities fraud.[57]

Senator Richard Shelby, a Republican from Alabama, is the sponsor of a second major bill, the proposed Investor Protection Act.[58] This measure would fully reinstate the concept of joint and several liability in securities fraud cases. Similar to the Markey bill, it would also allow defendants to be held liable in private suits for aiding and abetting. Further, under the Shelby bill, aiding and abetting liability would be possible when the defendant merely "recklessly" (rather than "knowingly") provides substantial assistance in violating the securities laws. Finally, it would allow plaintiffs to bring suits in state courts, rather than federal courts, in an effort to avoid the more stringent provisions of the PSLRA.[59] Both the Markey and Shelby bills, facing stiff opposition because of the significant changes they propose to the PSLRA, did not receive serious consideration in Congress in the first half of 2002.

Instead, Congress chose to take smaller steps in response to Enron. Over some Republican opposition, the Senate Judiciary Committee approved a bill that would lengthen the amount of time allowed to bring securities fraud claims (two years after discovery of the fraud, rather than one, and within five years of the conduct, rather than three).[60] The proposed Corporate and Criminal Fraud Accountability Act, sponsored by Judiciary Committee Chairman Patrick Leahy, a Vermont Democrat, also toughens the criminal penalties for securities fraud and destruction of records.[61] However, House of Representatives supporters of extending the statute of limitations for securities fraud failed in their first effort to pass similar legislation in that chamber.[62]

The more conservative House addressed the Enron scandal in a different manner, by seeking stronger accounting oversight. The proposed Corporate and Auditing Accountability, Responsibility, and Transparency Act, sponsored by Representative Michael Oxley, a Republican from Ohio, orders the SEC to establish an independent disciplinary board to oversee auditors.[63] The Oxley bill passed the House by a wide margin, after Democrats failed narrowly in their efforts to impose stronger restrictions on auditors.[64]

But the political landscape changed significantly in late June 2002, with the revelation that WorldCom had engaged in massive accounting fraud involving $3.8 billion in improperly recorded expenses.[65] With the stock market indexes plunging beneath their lows following the September 11 terrorist attacks, the Senate rushed to pass unanimously the Public Company Accounting Reform and Investor Protection Act.[66] Sponsored by Senator Paul Sarbanes, a Maryland Democrat, this major corporate reform measure provides for significantly more stringent oversight of auditors than the Oxley bill in the House.

Seizing on a popular bill that was certain to pass, some of those seeking changes to the PSLRA tried to incorporate their proposals into the Sarbanes measure. Senator Leahy was successful in adding the longer statute of limitations for securities fraud suits to the corporate reform legislation, as well as the tougher criminal penalties from his proposed Corporate and Criminal Fraud Accountability Act.[67] However, Senator Shelby was blocked in his efforts to reinstate aiding and abetting liability in securities fraud suits brought by private investors. Instead, he had to settle for a study of aiding and abetting cases involving accountants, attorneys, investment bankers, and other securities professionals.[68]

The differing House and Senate bills then went to a conference committee, which acted with remarkable speed. As this paper was being finalized, congressional leaders reached agreement on a compromise. The resulting legislation is much closer to Sarbanes' Senate bill than to Oxley's House version. Further, it appeared that the extension of the statute of limitations for securities fraud suits would remain in the bill, and that President Bush would sign the legislation once both houses formally approved it in late July.[69]

Likely Outcome for the PSLRA

With only small portions of the proposals to revise the PSLRA included in the corporate reform legislation, what are the prospects for additional changes to the controversial 1995 law? The answer is somewhat difficult to predict, as there are conflicting propensities of Congress at work. First, basic inertia and the intricacies of the legislative system make it difficult for Congress to make major changes to any law. That is especially true for a law such as the PSLRA, which passed overwhelmingly and was the subject of intense lobbying. Second, with the two houses of Congress now controlled by different parties, the potential for legislative gridlock further reduces the prospects for agreement on any extensive revision of the PSLRA. On the other hand, there is significant public outrage about the conduct of Enron, Andersen, WorldCom, and others, and very clear sympathy for the victims of the various scandals. In a congressional election year, Congress cannot afford to be seen as doing nothing to address the problem. In fact, that issue arguably contributed to the swift and bold action on the corporate reform measure.

Considering all these factors, the only revisions to the PSLRA likely to come from Congress this year are the small, incremental changes in the Sarbanes legislation. Congress can appear responsive by passing the corporate reform measure, without making massive changes to the 1995 law. Absent still more corporate scandals the size of Enron and WorldCom, the PSLRA is not likely to be reversed or even significantly amended in the near future. Whether right or wrong, the PSLRA continues to be viewed generally as a justified attack on unpopular plaintiffs' lawyers, not as an assault on sympathetic victims of corporate fraud. Until that perception changes, opponents of the PSLRA probably will be frustrated in their efforts to undo the law.

Some observers would argue that this likely outcome is the most appropriate congressional response, at least for the short term. That view is succinctly summarized by former SEC Commissioner Joseph Grundfest, now a Stanford University professor: "Plaintiffs are trying to use the Enron disaster as a reason to change the law for cases that are much more ambiguous. Enron was an ax murderer. The question is, what lesson do you learn from an ax murderer?"[70] Grundfest's comments have merit. Although clarification of the ambiguities of the 1995 law is needed, without more proof that the statute truly assisted in Enron's "ax murderer" conduct, Congress should not rush to impose the death penalty on the PSLRA.

Footnotes

[1] Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (codified in various sections of 15 U.S.C.S.).
[2] John Harwood, *House, in 325-99 Vote, Approves Bill to Curb Fraud Suits Against Companies*, WALL ST. J., Mar. 9, 1995, at A3.
[3] 17 C.F.R. § 240.10b-5 (2002).
[4] Saundra Torry, *On the Docket: Trial Lawyers v. Tort Reformers*, WASH. POST, Nov. 21, 1994, at F7.
[5] Jerry Knight, *Protecting Honest Companies, Or Crooks and Swindlers?; Bill Aimed at Curbing Shareholder Suits Nears Senate Approval*, WASH. POST, June 28, 1995, at F1.
[6] David Robinson, *Congress Is Preparing a 'Swindlers Protection Act,'* BUFFALO NEWS, June 25, 1995, at 13B.
[7] Michael Frisby & Jeffrey Taylor, *Clinton Vetoes Bill Limiting Securities Suits*, WALL ST. J., DEC. 20, 1995, at A3.
[8] Jeffrey Taylor, *Congress Sends Business a Christmas Gift -- Veto Is Overridden on Bill Curbing Securities Lawsuits*, WALL ST. J., Dec. 26, 1995, at A2.
[9] H.R. Conf. Rep. No. 369, 104th Cong., 1st Sess. (1995) {hereinafter Conference Report}.
[10] *Id*.
[11] 15 U.S.C.S. § 78u-5 (2002).
[12] Jerry Knight, *A Measure of Security on Securities Suits; Congress Approves Tougher Standards for Alleging Fraud*, WASH. POST, Dec. 7, 1995, at B11.
[13] 15 U.S.C.S. § 78u-4 (2002).
[14] Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976), at 193.
[15] 15 U.S.C.S. § 78u-4 (2002).
[16] Conference Report, *supra* note 9.
[17] 15 U.S.C.S. § 78u-4 (2002).
[18] *Id*.
[19] Harvey Pitt & David Hardison, *New Reporting Obligations for Outside Auditors*, NAT'L L.J., Mar. 25, 1996, at B4.
[20] *Id*.
[21] Conference Report, *supra* note 9.
[22] Richard Phillips & Gilbert Miller, *The Private Securities Litigation Reform Act of 1995: Rebalancing Litigation Risks and Rewards for Class Action Plaintiffs, Defendants and Lawyers*, 51 BUS. LAW. 1009 (1996).
[23] Conference Report, *supra* note 9.
[24] *Id*.
[25] *Id*.
[26] 15 U.S.C.S. § 78u-4 (2002).
[27] Robert Greenberger, *Panel, in Enron's Wake, to Review Lawsuit Curbs*, WALL ST. J., Feb. 6, 2002, at A8.
[28] Knight, *supra* note 12.
[29] Conference Report, *supra* note 9.
[30] PricewaterhouseCoopers LLP, *2000 Securities Litigation Study* <http://www.pwcglobal.com>.
[31] Jonathan Weil, *Number of Suits Charging Fraud Fell Last Year*, WALL ST. J., May 29, 2001, at B13.
[32] Henny Sender, *Securities Suits Hit Record Total of 483 in 2001*, WALL ST. J., June 10, 2002, at C5.

[33] Tamara Loomis, *Lawyers Seek Review of a Key Class Action Ruling*, N.Y.L.J., Oct. 26, 2000, at 5.
[34] Wharf (Holdings) Ltd. v. United Int'l Holdings, Inc., 532 U.S. 588 (2001).
[35] *Id*. at 597.
[36] David Rovella, *Securities Reform Spawns Discord*, NAT'L L.J., July 18, 2001, at A1.
[37] Janas v. McCracken (In re Silicon Graphics Sec. Litig.), 183 F.3d 970 (9th Cir. 1999).
[38] Steven Rosenfeld, *Federal Courts Disagree on Pleading Securities Fraud*, NAT'L L.J., Sept. 6, 1999, at B7.
[39] Gerard Pecht & Glen Banks, *Standard for Scienter*, NAT'L L.J., Dec. 3, 2001, at A19.
[40] *Id*.
[41] Michael Chepiga & Paul Ferrillo, *Protecting Forward-Looking Disclosures; Examining Private Securities Litigation Reform Act's Safe Harbor Five Years After Its Enactment*, N.Y.L.J., Feb. 5, 2001, at S2.
[42] Joseph Allerhand et. al., *A Few Courts Try To Make Waves in the PSLRA's 'Safe Harbor' -- Part II*, METROPOLITAN CORP. COUNS., Aug. 2001, at 10.
[43] *Id*.
[44] Leon Gold & Richard Spinogatti, *Sanction Provisions of Securities Reform Act Rarely Invoked*, N.Y.L.J., Aug. 8, 2001, at 3.
[45] *Id*.
[46] *University of California To Lead Securities Fraud Suit Against Enron*, CORP. OFFICERS AND DIRECTORS LIAB. LITIG. REP., Mar. 11, 2002, at 11.
[47] *Id*.
[48] *Enron Ex-Executives Fight Motion to Lift Discovery Stay*, CORP. OFFICERS AND DIRECTORS LIAB. LITIG. REP., Mar. 11, 2002, at 10.
[49] Abner Mikva, *Share and Shares Alike: Now Let's Fix the 'Reform' of Our Securities Laws*, LEGAL TIMES, Apr. 8, 2002, at 50.
[50] *Pro-Business Interests Will Use Stanford Study To Fight Assault on Class Action Law*, SEC. WK., Apr. 1, 2002, at 7.
[51] Patricia Villareal, *Enron's Impact on the PSLRA*, TEX. LAW., Apr. 29, 2002, at 31.
[52] H.R. 3617, 107th Cong. (2002).
[53] *Id*.
[54] Central Bank of Denver v. First Interstate Bank of Denver, 511 U.S. 164 (1994).
[55] 15 U.S.C.S. § 78t (2002).
[56] David Rovella, *Milberg Guns for Enron's Lawyers*, NAT'L L.J., Apr. 22, 2002, at A1.
[57] *Id*.
[58] S. 1933, 107th Cong. (2002).
[59] *Id*.
[60] Richard Oppel, *Senate Panel Votes to Ease Rules on Suits in Stock Fraud*, N.Y. TIMES, Apr. 26, 2002, at C1.
[61] S. 2010, 107th Cong. (2002).
[62] Oppel, *supra* note 60.
[63] H.R. 3763, 107th Cong. (2002).
[64] Michael Schroeder, *House, in Bipartisan Vote, Backs Moderate Accounting Overhaul*, WALL ST. J., Apr. 25, 2002, at A2.
[65] Jared Sandberg, Rebecca Blumenstein & Shawn Young, *WorldCom Internal Probe Uncovers Massive Fraud*, WALL ST. J., June 26, 2002, at A1.
[66] S. 2673, 107th Cong. (2002).
[67] Richard Simon & Ronald Brownstein, *Senate Passes Broad Corporate Reforms*, L.A. TIMES, July 16, 2002, at A1.
[68] Lisa Girion, *1995 Tort Reform Act Said to Provide Safe Harbor for Fraud*, L.A. TIMES, July 22, 2002, at C1.
[69] Jim VandeHei & David Hilzenrath, *Hill Leaders Agree on Corporate Curbs*, WASH. POST, July 25, 2002, at A1.
[70] Carrie Johnson, *Fight Renewed Over Limits on Investor Suits*, WASH. POST, May 10, 2002, at E1.