

In this issue... we return to the Tellabs case, introduce a new excess D&O policy form and announce additional Side A capacity.

TELLABS REVISITED

In the March 2007 newsletter,¹ we discussed the Tellabs case that was to be heard by the U.S. Supreme Court. At issue was how courts should interpret the language of the 1995 Private Securities Litigation Reform Act (PSLRA) that requires there to be a "strong inference" of scienter—wrongful intent—in order to overcome a defendant's motion to dismiss a securities class action lawsuit.

The Decision²

The opinion of the Court was delivered by Justice Ginsburg on June 21, 2007, and as was widely expected, the court rejected by an 8-1 majority the Seventh Circuit's interpretation, which had been to ask whether a "reasonable person could infer that the defendant acted with the required intent."

That criterion, said the Court, was not sufficient to meet the "strong inference" requirement of the PSLRA; lower courts must take into account competing inferences that suggest an absence of scienter. Justice Ginsburg set out a three-step process whereby lower courts could make the appropriate determination. The steps can be summarized as follows:

- Accept all factual allegations as true.
- Consider the complaint in its entirety.
- Take into account plausible opposing inferences that explain the defendant's conduct.

If the lower court believes that a "reasonable

person would deem the inferences of scienter cogent and at least as compelling as any opposing inferences," then the defendant's motion to dismiss should be denied and the lawsuit allowed to proceed.

Comments

1. Although the Seventh Circuit's approach was rejected, that approach was already something of an anomaly. Other circuits (notably the Sixth Circuit as cited by Justice Ginsburg) had adopted a "stiffer standard" for testing scienter that might be even stricter than that of the Supreme Court. This could mean other circuits having to slightly lower their standard, possibly making it easier for a complaint to survive a motion to dismiss.
2. The court did not find in favor of Tellabs, but against the approach used by the Seventh Circuit. The case was remanded back to the lower court for further review, and indeed it may be that after applying the three-step process the lower court still finds for the plaintiffs and allows the case to proceed.
3. The Court reaffirmed securities class action lawsuits as an important recourse for aggrieved shareholders: "This Court has long recognized that meritorious private actions to enforce federal antifraud securities laws are an essential supplement to criminal prosecutions and civil enforcement actions..."
4. The Tellabs decision tacitly underscores the ability of individual judges throughout the

nation's federal system to make their own assessments when faced with motions to dismiss securities class action lawsuits.

Reactions

The general consensus among observers seems to be that while Tellabs' appeal successfully rejected the Seventh Circuit's methodology, talk of a significant setback for

plaintiffs should probably be muted. A "mild victory"³ for defendants appears to be the prevailing sentiment. The Milberg Weiss law firm, lead counsel for the plaintiffs in Tellabs, appeared completely unruffled: "Investors everywhere should be very comfortable with the Supreme Court's decision. We believe the decision will not have an adverse impact on the prosecution of securities fraud cases..."⁴ ❖

NEW EXCESS D&O FORM

Chicago Underwriting Group has introduced a new excess D&O policy form, **ORUG-87**, which is intended to replace ORUG-59. Created in response to producer and policyholder demand, the new form offers a more streamlined excess contract that adheres as closely as possible to the provisions of the primary and underlying carriers, as applicable. Many of the coverage features we currently provide by endorsement are now built in, yet the basic policy form is still shorter than ORUG-59.

The new form is approved and available in over 40 states⁵ and we expect to be quoting it on most new and renewal excess placements. Form ORUG-87 can be seen on our web site.⁶

SIDE A CAPACITY

Our \$10,000,000 additional capacity for Side A exposure has proved popular with brokers and policyholders looking for highly-rated security (A.M. Best **A+**; Standard & Poor's **AA**; Moody's: **Aa2**) as critical protection for non-indemnifiable losses sustained by individual directors and officers. The additional capacity could be used to provide stand-alone Side A limits of up to \$25,000,000 or increase the Side A portion of a traditional A, B, C policy from the current maximum of \$15,000,000 to \$25,000,000 (the maximum limits for Side B and Side C remain at \$15,000,000).

Resources:

¹ <http://www.cug.com/img/pdf/Issue49.pdf>

² http://www.cug.com/img/pdf/tellabs_SCotUS.pdf

³ <http://www.cug.com/ments/51-3.html>

⁴ <http://www.cug.com/ments/51-4.html>

⁵ <http://www.cug.com/ments/51-5.html>

⁶ <http://www.cug.com/img/ORUG-87/ORUG-87.pdf>



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