A Challenging Environment

Demand for specialized expertise grows with complexity of disputes in UK and Europe

MCC** interviews **James C. Meehan,** senior vice president, and **Ronnie Barnes,** principal, at **Cornerstone Research's** London office. They can be reached at **jmeehan@cornerstone.com** or **rbarnes@cornerstone.com.

MCC: Cornerstone Research recently opened an office in London. What prompted this move?

Meehan: London is one of the significant litigation markets outside of the United States, and it was important for us to be here to address European litigation and regulatory matters for our clients' current and future needs. We have been working internationally for many years, and our London office brings us closer to these venues. Our firm started out over 25 years ago with two regional offices, one in Menlo Park, California, and one in Cambridge, Massachusetts. We have grown into a broad-based firm with more than 500 staff members and seven U.S. offices. Having been with the firm since its founding, I'm pleased to be leading our London office.

The UK is moving away from the opt-in to the opt-out approach to class actions.

–James C. Meehan

MCC: What financial industry trends are you seeing in terms of regulatory matters being pursued by the European Commission? Where do these matters fit within the broader landscape of issues facing legal departments?

Barnes: As cases are becoming larger and more frequent with increased activity by the various global regulatory bodies, including the European Commission, we are finding that the multidisciplinary expertise we bring is critical. The regulatory cases that involve financial institutions require not only an understanding of economic and competition issues, but also expertise in financial institutions and complex financial instruments.

For example, there have been a number of high-profile matters in the financial institutions space, some alleging manipulation of foreign exchange markets, Libor and other interest rate markets. There was an EU investigation into the credit default swap market, which is particularly interesting as it relates to the intersection of competition or antitrust economics and financial markets. There are similar matters that involve allegations relating to the gold and other metals markets. It's been exciting for me to return to London and work on these cases from Europe, after being in our New York office for several years.

Any large company in any industry may be engaged in litigation or arbitration, but after the credit crisis, financial institutions saw an enormous increase in this regulatory activity, such as on the regulation of mortgage-backed securities, credit derivatives, and related securities. To some extent, these types of cases are still cropping up, and some are legacies from matters that arose immediately post-credit crisis. The difference is that, five years ago, credit-crisis-related matters were top of mind for general counsel; however, if you were to talk to GCs of large financial institutions today, regulatory investigations would most likely be one of the main topics commanding their attention.

MCC: Has a more stringent regulatory environment affected your clients' needs?

Barnes: Given the changes that regulatory investigations have brought, including the fact that many matters now give rise to actual legal cases, clients are looking for a more internally focused effort in addressing potential problems. We are being asked to get involved at an earlier stage. Whether it's a formal regulatory investigation or a private investigation, our role is in research and analysis for clients who want to understand both the scope and concerns of a potential issue.

MCC: How do economic and financial consultants fit into this new regulatory picture and the changing focus of litigation?

Meehan: Cornerstone Research provides expert, and often very specialized, analysis of the economic and finance aspects of litigation, arbitration and other matters. We match experts to clients' needs, drawing on a large pool of international academics from the economics and finance departments of top business schools as well as industry practitioners. This intellectual support is integral to our work and directly constitutes much of the enduring value we bring to clients. Given the high-profile nature of our clients and their matters, Cornerstone Research's ability to fill the need for nuanced expertise on a broad span of issues is garnering significant interest.

MCC: Can you give some examples?

Meehan: It seems as if Europe generally, and the UK more specifically, is moving away from the opt-in to the opt-out approach to collective or class actions. As a result, we have heard several times that experience in dealing with the economic issues involved in the certification of a class will be much in demand as these actions start to become more prevalent. As a firm, Cornerstone Research has been addressing these issues for many years and in many different contexts, from the competition arena to securities litigation and even extending into the realm of structured finance products, such as residential mortgage-backed securities and collateralized debt obligations. As such, we will be ideally placed to provide the advice that our clients will need when navigating this changing and complex landscape.

Regulatory cases that involve financial institutions require multidisciplinary expertise.

–Ronnie Barnes

Another area where the firm has an enormous amount of accumulated experience is that of loss causation. This is the determination of the extent to which price drops in securities can be attributed to the particular allegations in a case and the extent to which they are driven by other unrelated factors. For example, in a securities litigation involving banks and other financial institutions, being able to disentangle the potential impact of alleged misrepresentations regarding asset quality from the effect of a general drying up of liquidity is crucial. In order to do this, an understanding of the relevant economics needs to be coupled with an appreciation of market practicalities and the ability to analyze the relevant data in a meaningful and sophisticated manner. Cornerstone Research, together with our roster of experienced experts, is well positioned to tackle this sort of complicated analysis.

MCC: Cornerstone Research releases an annual report on M&A-related litigation. According to your latest research, more than 90 percent of deals valued over $100 million are challenged by shareholders. How are experts utilized in these types of matters?

Barnes: In these lawsuits, plaintiffs typically allege that a target's board of directors violated its fiduciary duties by conducting a flawed sales process that failed to maximize shareholder value. Common allegations include the failure to conduct a sufficiently competitive sale, the existence of restrictive deal protections that discouraged additional bids and conflicts of interest. Another typical allegation is that the target board failed to disclose enough information about the sale process and the financial advisor's valuation. In these matters we provide valuation, disclosure, corporate governance, strategy, executive compensation, sale process and other analyses. In several matters, we have reviewed comparable mergers to determine that the level of detail and timeliness of disclosures were consistent with standard industry and corporate governance practices. We have also evaluated fairness opinions and valuations, compared alternative bids, analyzed hedging by various counterparties, and calculated damages arising from corporate transaction litigation.

MCC: As finance experts, what kinds of analyses and perspectives can you bring to the table when advising corporate counsel?

Meehan: Clients in Europe are especially looking to Cornerstone Research for our expertise in the areas of international arbitration, competition, energy and commodities, and regulation in financial institutions and other segments.

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Microcaps

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companies must have at least 1.1 million shares issued to at least 400 hundred shareholders – with a market value of public shares no less than $40 million with a minimum share price of $4. As with a NASDAQ listing, various earnings and revenue requirements, in addition to stringent government standards, must be met.

While the range of valuations on a microcap stock can make it difficult to meet uplisting requirements, it also can make the stock attractive to OTC investors. Because such securities are thinly traded (i.e., one large trade can move the market price up or down tremendously), you can have a stock that's trading at 10 cents; then somebody sells 500,000 shares, and it's now trading at 4 cents, thereby affecting the valuation of the company by 60 percent in a matter of seconds. So microcaps are vulnerable to huge swings either way, and that's an inherent risk of the space (and a hindrance to institutional investors, which often need to move large blocks of shares).

The Next Facebook?

Among noninstitutional investors, however, microcaps have an appeal wholly apart from their low price and potential for rapid growth. Retail investors oftentimes "love the story." They think it might be the next Facebook or cancer-eliminating drug and want to get in on the ground floor. A lot of hedge funds follow these types of stocks because they can also take an activist role in them. (Editor's note: Activist strategies led gains in the hedge fund industry this past March.)

Like any sector, microcaps have their star performers. In the early years of the new millennium, dotcoms were hot. Today, biotechs and life sciences are on a tear. Tomorrow might see a resurgence of tech stocks. That's what's exciting about the space – the innovation and entrepreneurial initiatives. Microcaps that successfully up-list are not out of the woods. They've got to make sure that they stay listed, and they have to be more earnings conscious. They'll be followed by a wider audience – an audience with expectations of earnings, growth, new product development and distribution, etc. But that's one of the benefits of being visible on the larger exchanges and the excitement of being part of the microcap space. When a microcap delivers on this potential, investors get the pleasure of watching both the company and its valuations grow.

Acquiring a Microcap Company

A hot microcap company can also become an acquisition target. For a buyer, due diligence would start with looking at the business plan and the company's ability to execute it (the same factors that a company would emphasize in bringing an IPO to market). For an M&A deal, buyers will also want to perform an accretion/dilution analysis and take the pulse of existing investors to avoid a range of potentially hostile scenarios. Management qualifications come back into play, as does the quality of the target's financials and its financial and other professional advisors. Synergies and strategic fit (vertical and horizontal) might also be important areas of exploration. As is inherent in middle-market and large-cap transactions, the microcap target's ability to continue to deliver consistent earnings, dividends and growth, and product and brand recognition, do become factors requiring consideration.

About Marcum LLP

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Challenging

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Our deep understanding of valuation and general damages provides the sophisticated analyses that our clients require. For example, for financial institutions counsel, we use advanced economic and financial techniques to determine the extent to which losses on investments can reasonably be attributed to alleged misrepresentations and omissions in offering materials, and the extent to which such losses are the result of factors unrelated to disclosures in these materials.

MCC: What can you tell me about the firm's work in international trials and arbitration?

Barnes: We address interesting issues, particularly in the international arbitration space. These are commercial damages claims where, hypothetically speaking, two companies enter into a joint venture agreement, and one party alleges that the other party breached the agreement, causing losses and justifying a damages claim. Here, the analysis requires finance expertise, but the trick lies in the fact that there are many ways that the estimates can be seriously miscalculated. For instance, the commonly accepted discounted cash-flow approach, by definition, requires that you estimate a discount rate; however, there are a myriad of ways in which one can get the discount rate wrong, often significantly wrong. This is of particular concern in dealing with cross-border investments where there are issues about selecting the appropriate market benchmark and accounting for control premia or an illiquidity discount. Our vast experience is a real asset to clients in damages valuation.

Meehan: We also bring significant experience in the procedures and customs appropriate to different international venues. For example, we applied our experience with finance and securities markets to address the issues in the first case to reach trial under Ireland's Companies Act. Our staff and experts have consulted in arbitration matters in venues throughout the world, including the International Centre for the Settlement of Investment Disputes, the U.N. Commission on International Trade Law, the International Chamber of Commerce the International Centre for Dispute Resolution, and the London Court of International Arbitration, as well as in disputes involving the Energy Charter Treaty. In addition, our staff and experts have degrees from many of the world's leading universities and in-depth knowledge of businesses around the globe and their languages.

MCC: Please give our readers your final thoughts on the expansion of your European presence.

Meehan: As our clients continue to see increased activity from the various regulatory bodies across the globe, we are committed to providing enhanced support for their litigation and international arbitration needs. Cornerstone Research's approach of finding the right expert from a large international pool supports our clients' needs for specific expertise to address each situation. Our staff consultants' expertise in finance and competition as well as in vertical markets such as financial institutions, pharmaceuticals and energy allows for robust research and analysis of issues that arise in litigation and regulatory matters. We are pleased that Cornerstone Research's presence in Europe has been met with such a positive reception.

The views expressed in this interview are solely those of Mr. Meehan and Dr. Barnes, who are responsible for the content, and do not necessarily represent the views of Cornerstone Research.

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join parties to arbitrations or to seek to consolidate arbitrations. In institutions where such rules have not yet been expressly included, parties may seek to persuade tribunals that they have the power to join or consolidate arbitrations on the basis of the trend.

Careful attention must be paid, however, to the rules that apply in a given situation. In particular, timing requirements can bar a party seeking to add additional parties to an active or contemplated arbitration (or to consolidate arbitrations). Accordingly, parties seeking to add additional parties to an active or contemplated arbitration (or to consolidate arbitrations) should do so as early as possible in the proceeding.

Likely claimants who may want to have a single proceeding with a number of parties should pay careful attention to the applicable arbitral rules when drafting a dispute resolution clause. While an express pre-dispute agreement for all parties to participate in a single arbitration is ideal for a potential claimant seeking to include all potential parties in a dispute, the use of arbitral rules that expressly contemplate multiparty proceedings can assist in the absence of an express agreement.

As noted above, claimants as well as respondents can benefit from the invocation of such multiparty provisions to ensure the efficient resolution of disputes.

To review the footnotes for this article, visit http://www.metrocorpcounsel.com/articles/32123/more-merrier-increase-multiparty-arbitrations-spawns%C2%A0new-institutional-rules.

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Anderson Kill is a national law firm with experience representing clients in disputes involving issues in a number of areas, including international commercial arbitration, insurance coverage, employment issues, contract disputes, construction matters and financial – investor/broker disputes. In the field of arbitration, our practice draws upon our in-depth knowledge of domestic and international arbitration rules, including: American Arbitration Association (AAA) and its international division (ICDR); JAMS; International Court of Arbitration of the International Chamber of Commerce (ICC); the London Court of International Arbitration (LCIA); and the United Nations Commission on International Trade Law (UNCITRAL). Our wealth of litigation and trial experience in courts and before arbitration tribunals informs and enriches our conduct of arbitration matters. Our lawyers also serve as arbitrators and mediators for AAA and on mediation panels in federal and state courts. We also work in the forefront of alternative dispute resolution advancement, lecturing and authoring articles on ADR. To learn more about our alternative dispute resolution practice, visit http://www.andersonkill.com/Alternative-Dispute-Resolution/default.asp.

Stalking Horse

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an auction be held. However, it is not unusual for a potential purchaser to negotiate limited periods of exclusive dealing as it attempts to arrive at a stalking horse purchase agreement with the debtor. The debtor may formally or informally agree to such exclusivity in order to maximize the ability to reach a purchase agreement, but the obligation of exclusivity ultimately is not truly binding on the debtor absent bankruptcy court approval.

Conclusion

A potential purchaser unfamiliar with bankruptcy processes initially may find the process to be cumbersome and foreign. However, once the purchaser learns the process, or obtains legal and financial advisers experienced with it, the purchaser can typically use the process to its advantage as a stalking horse. In addition to attempting to negotiate some or all of the provisions described above, the stalking horse can often gain a significant advantage over other bidders simply by virtue of being the bidder with whom the debtor deals while negotiating the purchase agreement. The stalking horse becomes a known quantity and can use the opportunity to make the debtor and creditor groups feel comfortable that the purchaser will be able to close the deal quickly and efficiently once the sale is approved.