The Fifth Annual Albert A. DeStefano Lecture on Corporate, Securities & Financial Law

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Eliot Spitzer

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LECTURE

THE FIFTH ANNUAL ALBERT A. DESTEFANO LECTURE ON CORPORATE, SECURITIES & FINANCIAL LAW*

WELCOME:

Constantine N. Katsoris
Fordham University School of Law

INTRODUCTION:

Jill E. Fisch
Fordham University School of Law

FEATURED LECTURER:

Eliot Spitzer
New York Attorney General**

WELCOME

PROFESSOR KATSORIS:¹ Welcome to Fordham Law School. Dean Treanor,² unfortunately, could not be with us. He is in China. The

* Eliot Spitzer delivered this address at Fordham University School of Law on April 11, 2005. It has been edited to remove minor cadences of speech that appear awkward in writing and to identify significant sources when referred to by the speakers.
** Eliot Spitzer took office as Attorney General of New York in 1999.
¹ Constantine N. Katsoris is the Wilkinson Professor of Law at the Fordham University School of Law.
² William Michael Treanor is the Dean of the Fordham University School of
DeStefano Family, unfortunately, could not be with us. But they both send their regrets and their warmest regards.

Tonight's lecture is being sponsored by the firm of Becker Ross Stone DeStefano & Klein. The lecture series bearing Al DeStefano's name has had a most distinguished track record. The first DeStefano Lecture – and this is the fifth – consisted of a panel discussion that dealt with the SEC's fair disclosure rules. The following year, I chaired the panel that explored the explosive topic, "Enron: What Went Wrong?" Two years ago, we retraced the history of celebrating thirty years of market regulation. Last year we examined the crisis in confidence of self-regulation in the securities industry.

Tonight we are most fortunate to have as our speaker the Attorney General of New York, the Honorable Eliot Spitzer. This lecture series, however, goes far beyond its five-year track record. Indeed, its roots are far wider and run much deeper. It all began a hundred years ago, on September 28, 1905, when Fordham Law School was founded. This fall we will be celebrating our centennial anniversary with a series of major events throughout the country. In terms of physical brick and mortar, it all began in a small building on the Rose Hill Campus and migrated to several locations downtown, before settling in its present environment here at Lincoln Center.

As someone who has been part of fifty-two of those first hundred years – as a student, alumnus, and faculty member – I can tell you firsthand that the graduates of Fordham Law School do not think of their school in terms of brick and mortar. Indeed, we think of it in terms of heart and soul.

It is not accidental, therefore, that Fordham Law School is identified with the phrase, "In the Service of Others." I can think of no

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one who exemplifies this heart and soul better than Al DeStefano.

Al started at Fordham Law School as an evening student, sixty-six years ago. Just think: He was involved in part of Fordham for over two-thirds of Fordham's existence. He started in 1939, graduating eight years later, first in his class, after serving his country in World War II. As with many students in those days, Al worked his way through law school, with a variety of jobs, including that of assistant librarian. It was one of those jobs that Al had during law school that more truly defines Al DeStefano. He would create and map out cartoon layouts for nationally syndicated cartoon strips such as Little Lulu, Woody Woodpecker, Andy Pandy, and Gangbusters.

At first I found it quite amusing that during the day Al would be briefing cases for class, doing footnote assignments for the Law Review, and at night he would dream up and create these cartoons. In hindsight, however, his role as a creator of cartoons was perfectly natural for Al, for cartoons, in three or four illustrations, tell an entire story. They communicate a message in a clear, concise, and forthright manner. That is what Al DeStefano has done all his life. As a practitioner for over half a century, he advocated positions and persuaded adversaries to compromise and negotiate in a frank and straightforward and transparent manner.

Yet, despite his busy schedule, Al DeStefano found time to come up and teach as an adjunct professor. He taught an oversubscribed course on mergers and acquisitions. Students loved him for his professional skills and knowledge, but more important, for his devotion to the students, and his ability to put things in perspective.

Fordham has always prided itself on its efforts to produce not only the well-trained and skillful professional, but the well-balanced person as well. Buried in Al DeStefano's resume are just some of the humanitarian activities that speak to his compassion. For many years, he was a member of the Board of Fellows of Gallaudet University in Washington, D.C., which is the only liberal arts college for the deaf in the world.7 For over thirty-five years, he served as secretary and trustee of the Helen Keller Services for the Blind.8 For over twenty years, he


served as trustee for the Cleary School for the Deaf.9

Events of the last decade have shown the enormous breakdown in ethical and professional standards, not only in our own profession, but also those of other professions as well. Greed has replaced compassion. Self-interest has replaced loyalty. Enrichment has replaced righteousness. Deceit has replaced transparency. The erosion of values has infested all segments of our society.

Through this series of lectures, we hope to remind ourselves of our mission: To produce skilled professionals of character, integrity, and compassion, people like Al DeStefano, who epitomize heart and soul, instead of brick and mortar.

Moral integrity has been the underlying theme of the DeStefano Lecture, and tonight is no exception. We are most fortunate in having as our speaker State Attorney General Eliot Spitzer, who has championed the cause of truth and integrity in professional life.

At this point, it is my great pleasure to turn the podium over to the Director of the Fordham Center for Corporate, Securities & Financial Law, who will talk a little bit more about the Center and introduce our speaker.

Thank you.

INTRODUCTION

PROFESSOR FISCH:10 Good evening. I am Jill Fisch, Director of the Fordham Center for Corporate, Securities & Financial Law. On behalf of the Fordham Law School community, it is my great pleasure to add my welcome to you, to be here at the Fifth Annual Albert A. DeStefano Lecture.

I would like to thank New York State Attorney General Eliot Spitzer for being here tonight. I would like to thank the firm of Becker Ross Stone DeStefano & Klein for establishing this lecture series, named for our distinguished alumnus.

I also want to acknowledge the Center's Board of Advisers, many of whom are here tonight, and to thank Professors Caroline Gentile and

10. Jill E. Fisch is the Alpin J. Cameron Professor of Law at the Fordham University School of Law and is the Director of the Fordham Center for Corporate, Securities and Financial Law.
Beth Young for their hard work in putting together tonight’s program.

As you know, the Albert A. DeStefano Lecture Series is one of the jewels of Fordham’s program in business law. Together with our other public programs — the Business Law Practitioner Series, which introduces students to distinguished business law practitioners in an informal setting; the other public programs; the academic conferences; our policy-oriented roundtables, which bring together practitioners, policymakers, and academics in a closed-door setting in which they can formulate policy and respond to new developments; and our specialized course offerings, many of which are taught by leaders in the community in corporate law, securities law, and related areas — the DeStefano Lecture Series allows the Fordham Corporate Center to bring leaders from the highest levels of corporate and securities law to the law school. We here at Fordham benefit from their insights into cutting-edge legal developments affecting the business community.

Of course, this year’s speaker is no exception. Eliot Spitzer is widely credited with redefining the role of state attorney general. Since he took office on January 1, 1999, in a range of innovative investigations, Attorney General Spitzer has revealed widespread practices of wrongdoing and responded to them. Just to name a few examples, he uncovered extensive conflicts of interest between equity research and investment banking firms, conflicts that likely contributed to the stock market bubble of the late 1990s. He found widespread practices of late trading and market timing in the mutual fund industry. He revealed bid rigging and anticompetitive practices in the insurance industry, and he sued out-of-state power companies to reduce air pollution in the Northeast.

Spitzer’s investigations have generated billions of dollars in out-of-court settlements, as well as extensive industry reforms. His efforts have also caused U.S. corporations to reexamine and restructure their business practices. His leadership role has earned him a national reputation for his ability to step in where other regulators – often federal government agencies – have failed to respond to patterns of wrongdoing. He has been termed “the people’s lawyer” by the press and has received numerous awards for his public service.11

In last week’s Wall Street Journal, Attorney General Spitzer

responded to criticisms of his enforcement efforts, explaining that the enforcement of the rules that govern business and the capital markets is both the right thing to do and good for the economy.\(^{12}\) Certainly, his efforts have been a major factor in addressing the crisis in investor confidence that followed the revelation of widespread corporate and accounting misconduct at major corporations, including Enron, WorldCom, and Tyco.

Attorney General Spitzer began his legal career in public service, serving first as law clerk to U.S. District Judge Robert W. Sweet and then as assistant district attorney under Robert Morgenthau.\(^{13}\) In the D.A.'s office, he prosecuted organized crime and political corruption cases, and rose to become chief of the labor racketeering unit. He then served in private practice with the Paul, Weiss and Skadden, Arps firms, as well as at Constantine & Partners. Attorney General Spitzer graduated from Princeton University and Harvard Law School, where he was an editor of the Law Review.

Attorney General Spitzer is going to speak to you. Afterwards, he has graciously agreed to take some questions. He has asked me to advise you to get your questions ready. I have told him that since we are in a law school, if you don't have questions, he is allowed to move to the Socratic method. So you should be prepared.

It now gives me great pleasure to present to you New York State Attorney General Eliot Spitzer.

**FEATURED LECTURER**

**ATTORNEY GENERAL SPITZER:** Thank you very much. The one request that I had of Jill was a seating chart, but, clearly, that request did not make it through.

Thank you so much for those gracious words and the kind introduction. Thank you all for being here. You all look terribly young to me, so I gather you are all students.

I can't be here without remembering, about a year ago, I was invited back to my law school. Parenthetically, they did not invite me back to participate in panels or a lecture series until 1999, when I was


\(^{13}\) *Id.*
Attorney General. My record as a student, somehow, didn’t merit any attention until I had a title in front of my name. But I was back one day. A friend of mine was being invested or ascending – whatever the term would be. She was becoming dean of the law school. There were some panels, one of which was on corporate governance. There was an earlier panel. I got there a few minutes early and was sitting in the audience, about 400 people. You may know of Professor Arthur Miller, who is of some civil procedure fame, has had a few TV shows, and is just a stupendous lecturer.14

I was sitting in the back row, as is my nature when I don’t need to participate. He looked out at the audience and he said, “Ah, Attorney General Spitzer, nice to see you here. You never used to show up when you were a student.” This was, unfortunately, more accurate than I wish to admit. He said that in front of 400 people. I took it in good nature.

I went ahead and did my panel. I will come back to that a bit more later. There was a luncheon after the panel I participated in. The prior dean, Dean Clark,15 of Harvard Law School was doing the introductions at the lunch. He saw me sitting out in the audience – again, the same 400 people – and without a cue, he said, “Oh, Attorney General Spitzer, nice to see you here. You never showed up when I was your Corporations professor.”

So there seems to have been a common theme that was there among my professors. They do not think I was in class with regularity. If you disagree with anything we have done since I have been Attorney General over the last six-and-a-half years, attribute it to the fact that my attendance in school was perhaps not what it should have been. I will leave it at that.

Here is what I do want to do for a period of time. I want to make an argument to you that the sort of intervention that my office has been participating in in the marketplace is required to maintain the integrity of the market and is beneficial to the marketplace. I want you to understand, when you leave, that this is not a populist crusade, this is not an effort simply to take from those who have, to give to those who do not; this is a market-based theory. I believe deeply that those of us who

15. Robert C. Clark is the Harvard University Distinguished Service Professor and Austin Wakeman Scott Professor of Law. Professor Clark served as Dean of the Faculty of Law at Harvard Law School between 1989-2003.
understand the market, those of us who believe in the market, support the types of interventions, the types of remedies we have put in place.

The reason I want to make this argument is that, as Jill referred to in her introduction, there has been pushback, and there has been criticism. That is good. It is the nature of our political dynamic. It is the nature of our political process. You welcome it; it furthers debate. But many of those who are taking the other side are attacking what we are doing, saying it is antithetical to the marketplace. You have the president of the U.S. Chamber of Commerce these days who is saying that what we are doing is destroying the market, that I have assumed the obligations of judge, jury, and executioner, that we are going after individuals for honest mistakes, that we are changing the rules in midstream and holding people accountable to a new set of rules, which they did not understand when they committed blatant fraud.16

Clearly, I am not sympathetic to the argument. But there is more than a small universe of people who support that worldview. The Chamber of Commerce – I don’t single them out because Tom Donohue17 has been most vitriolic in his criticism. I single them out because they are, to a certain extent, a preeminent – and they would maintain, I think, the preeminent – voice for U.S. business. In fact, they have gone so far recently as to sue the SEC and challenge the jurisdiction of the SEC and the capacity of the SEC to impose new rules that relate to issues such as proxy voting and mutual funds.18 So there is a battle that goes on right now, a raging battle, between those of us who believe that there is a role for government to step in and those who style themselves after the Chicago School – and we all know that is shorthand for those who defend the concept of a pure free market – who believe that government intervention necessarily is anathema to the market.

The interesting thing about this debate – or one of the many interesting things about this debate – is that we all invoke the same heroes. Whether you are on my side of the debate, justifying or trying to justify what we are doing, or whether you are Tom Donohue, everybody

18. For more information on the U.S. Chamber Institute for Legal Reform (ILR), the Chamber of Commerce’s law firm, visit Institute for Legal Reform, http://www.instituteforlegalreform.org (last visited Nov. 30, 2005).
invokes Theodore Roosevelt19 or Alexander Hamilton.20 To a certain extent, this is a consequence of the most recent biographies that have been written. We always need new heroes – not that these are new heroes – but certainly the biographies that have been written recently of T.R. and Hamilton have brought them back as vibrant, lively characters in our earlier history, and we have come to appreciate once again how important they were, how important their ideology was.

I raise this because I think that, obviously, it favors my argument. Why is that? Anybody who really understands what they stood for, anybody who really understands what they did will see that what we are doing is much closer to what they stood for than what the so-called Chicago School argues. Teddy Roosevelt, 101 years ago, when he ran for the presidency in 1904, was anathema to the business community. He was viewed as an enemy of his class, because he had had a rather comfortable upbringing, and there he was challenging the cartels, challenging the robber-barons. People said to him, “You’re tearing down capitalism. You’re going to destroy the very system that created you.”

Yet if you look back and ask yourself the simple question, did Teddy Roosevelt’s actions help or hinder – did they help us create the vibrant capitalism of the next century, or did he, as his critics say, destroy the capitalist structure? Of course, the answer is obvious. That is why both sides of the debate invoke him.

What he was doing back then was challenging a system that was ossified, challenging a system whose status quo nature was benefiting an oligarchy at the top, the robber-barons of that time period, and saying to them, “Fellows, this is not real capitalism. This is not the marketplace that we want, where value and pricing and competition determine who succeeds. You have formed illegal cartels.” Mind you, this was early on, before many of the antitrust laws that we now accept as part of our legal framework had been passed, before antitrust law was part and parcel of the business environment. But he was saying, “We understand what the marketplace demands, and you are not living by the rules or the ethics that we require.”

19. Theodore Roosevelt was the twenty-sixth President of the United States (1901-09).
So back then Teddy Roosevelt was anathema to the business community. I think that the Tom Donohues of the world, if they were transported back a hundred years, would not be encouraging Teddy Roosevelt to do what he did back then. They would have been among his critics. They would be among those saying to him, “You are destroying capitalism, not preserving it.” What I want to suggest to you is that today the actions we are pursuing are necessary to preserving the capitalist system that, we all agree, creates the wealth, creates the opportunity for people to succeed.

At the end of this lecture – and I am going to try to move quickly, because there is a lot of ground to cover, and I did say to Jill I would welcome your questions – I want you to understand three discrete rules, three discrete rules that justify market intervention. The first one I will pursue at the greatest length, and I will use some stories of the past couple of years, investigations we have made and cases we have brought, to exemplify why it is important.

The first rule is really, in a way, the simplest. The rule is that only government can ensure integrity and transparency in the marketplace – only government. If government is not there to enforce these rules, nothing else can step in and fill that void, and you will see a descent in ethics and in moral conduct. The way I will prove this to you, I hope, is by invoking some of the cases that Jill referred to. I will begin with the analyst case.

Just to state it very succinctly – assuming you have some knowledge of how the securities market works – there are analysts who work under the umbrella of investment banks, and whose job it is to recommend to investors – and, parenthetically, there are about 90 million Americans who now own stock directly or indirectly – to recommend to investors to buy the stock, sell that stock, hold it, and give the market advice that investors rely upon. They do this for their clients, clients of the investment banks. That is one side of the investment banking house.

On the other side of the investment banking house, you have underwriters, underwriters who actually are involved in the issuance of the stock, who sell the stock, either primary offerings at the initial public offering or secondary offerings thereafter. They sell the stock in the capital-formation process to investors.

The problem is that there is a conflict of interest inherent in having both of these functions within one investment house. Let’s see why. If I
am an analyst and I want to sell you stock or tell you that it is worth buying or not worth buying, I may say, “Sell this stock. This company’s no good.” On the other hand, if the other side of the house wants to go to the CEO of that company to persuade him to use this investment bank to do the underwriting, the CEO of that company isn’t going to go to the investment bank if the analysts at the investment bank are saying, “Your stock is worthless, the company’s business model is a failure, and I would sell that stock immediately.”

That is why – that underlying necessary inherent conflict – if you were to look back four or five years and ask yourself, did any of the analysts at what we call the “bulge bracket” firms, the big houses on Wall Street, recommend that people sell stock? The answer is no. Every one of them said, “Buy”. Why did they say, “Buy”? Because they wanted the underwriting business.

I did not discover this. There was no eureka moment, when I said, “Aha, now I understand what is going on.” This was, in fact, commonly understood on Wall Street. Insiders understood this conflict. Insiders discounted the value of the analytical work that was proffered by the analysts on the Street. They knew that this work is just the consequence of conflicts of interest. It is debased. It doesn’t have core integrity. They didn’t rely on it.

Those who did rely on it were the 89 million who watched CNBC, who watched FNN, who had been newly invited into the market, pursuant to what we call the democratization of the stock market, which is a wonderful thing. The middle class now owns stock. We said to the American public, “Buy stock; it is a good long-term investment”; as it is. But they were the ones who were relying upon this analytical work.

What was the response of the investment banking community when we went to them and said, “You know, folks, we think there is an inherent conflict here.” Let me quote Jack Grubman.21

Jack Grubman, you may know, is one of the famed telecom analysts. I do not dispute his brilliance. The guy was stupendous at what he did. But, unfortunately, he was part of this process. At one point, what he observed about the market was – and this is a quote – “what used to be viewed as a conflict of interest is now viewed as a

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synergy."^{22}

Think about this. Think about that as a way of rationalizing your behavior. Yes, we know it used to be a conflict of interest to try to make money off both sides of the transaction, but in essence, until we are caught, it is a synergy, because we make more money. That is what he was saying. We all know that what used to be a conflict is still a conflict. It was always a conflict. But they didn’t want to see it that way, so they justified it.

So we began to gather the evidence, and everybody now knows the infamous emails. I was turning the pages of *The Wall Street Journal* one day. I read the paper. It is a spectacular newspaper. The editorials are crazy, but it is a spectacular newspaper. I see Jack Zamansky here.\textsuperscript{23} Some of their Op-Eds are crazy, too, but that is alright. We love you, Jack, anyway, despite what you write.

I was turning the pages of *The Wall Street Journal* one day, and there was a full-page ad that was the picture of a leather-bound book. This leather-bound book had on the cover the words, "My Favorite Emails, by Eliot Spitzer." I looked at this, and I said, "What is going on here? I have been gathering those emails to publish that book five years from now. Who beat me to the punch? What is this? This is crazy."

It was an ad for Iron Mountain, which, you may or may not know, is a document-retention company. In the fine print at the bottom, it said, "Let us read them and sort them before he does," which I thought was sort of an interesting testament. If you want to get anything of value out of this lecture that is practical, don’t write anything in emails. That is my one little piece of advice. We will find it. Trust me, we will find it.

Anyway, so there we were. We were gathering these emails, building this case. We went to the investment banks. We went to one in particular and we said, "We think there is a problem." We tried to settle. We couldn’t. I won’t bore you with that story. Parenthetically, the last conversation I had with the lawyer for that investment bank, before we sued them -- he is a very prominent lawyer, a stupendous guy. I never will challenge his ethics. He said to me, "Eliot, be careful. We have powerful friends." I said, "Oh, now you tell me. If you had only told

\begin{itemize}
  \item[22.] *Id.*
  \item[23.] Jacob "Jack" Zamansky, head of Zamansky & Associates, has over 26 years of securities fraud litigation experience gained through private law practice and as a federal prosecutor.
\end{itemize}
me that last week, I would have dropped the investigation.” That is not what I told him.

Anyway, we filed suit. One thing led to another. The lawyers for this investment bank came in. I know this is a long introduction, but this is where the story becomes relevant to my rule. The lawyers for this investment bank came into my office. They are as smart and as sophisticated as any lawyers you will encounter. I expected them to say the sorts of things high-paid lawyers are supposed to say – “you don’t understand the industry,” “you are taking the emails out of context,” “just let us explain it,” all this stuff that is never persuasive, but they say it anyway. That is not what they did. They came into my office and they said, “Eliot, you are right, but we are not as bad as our competitors.” I am not making this up. I am not making this up.

I looked at them in amazement. My first thought was, “Your client is paying you for this?” My second thought was, “I thought you guys were going to be tougher than that.” I used to handle street crimes, robberies, rapes, homicides, organized crime cases – it used to take us months before we would get people to break.

Then I said, “Keep talking. Tell me about it.” What they said was, “We know this is a problem. We know that we have debased the integrity of our analytical work. But you cannot expect us to play by a different set of rules than our competitors. If you articulate a rule that applies to our competitors as well as to us, then we are happy to play ethically, but only if they do also.” In other words, they were right at several fundamental levels. They were right that I was right about their having debased the integrity of their analytical work. They were right that their competitors were worse than they. They were right, most fundamentally, that none of it would change until somebody outside the marketplace was willing to come in to define the moral boundary, the ethical line, which they could not cross over. They could not do it themselves. They were not willing to. It is not that there was ambiguity about what they were doing.

As a consequence, they were also right that the way to resolve the problem, perhaps successfully, perhaps not – we gave it our best shot, and we have to wait and see – was to get what we called the global deal. We worked feverishly to figure out a system to restore integrity to the analytical work product. That is what we did.

But the most important observation was indeed the one that they made.
There was an interesting set of vignettes that played out – and I won’t give you too many – in the analyst cases. Right after we had filed our case, after I had had this meeting with this one investment bank – and I do not want to put names on it and sully individual companies; they are all good companies, and we have done everything we can to restore their integrity – I had a meeting with my fellow regulators, the SEC, the NYSE, the NASD, in my office. There were a few of us in the room. I threw out some simple ideas that I thought could materially change and improve the ethical conduct of analysts. One of them – a very simple idea – was that analysts could not be paid anymore based upon how much underwriting work they brought in. Just think about it. The old maxim, “Follow the money,” works. If you are going to pay analysts based on how much underwriting work they bring in, of course they are going to use their analytical work to encourage the firm’s underwriting practice, and they will say what needs to be said.

So I said, “Let’s just sever that link. Figure out a way to create a chasm there.”

What was the response? We had a bunch of similar ideas that were kind of basic and elementary. You did not have to be terribly insightful to come up with these ideas. The other regulators said, “We cannot do that.” I said to them, “Why not?” The response – every one of them – was, “The industry will not like it.” These are the regulators. It was then that I realized how absolutely weak-kneed these other regulators had become over the prior decade. They had lost all of their capacity to stand up, look the industry in the eye, and say, “Stop.” They were so afraid of what the response would be from the industry.

Let me tell you another story that will play into a corollary to this first rule that I will give you in a few minutes. To prove something I said earlier, which is that many people understood this inherent tension – as I said, we were not the first to pick it up. It was out there. It was talked about. Harvey Pitt,24 who was the chair of the SEC for a period of time, had convened a meeting of the CEOs of the major investment houses, for the express purpose – this was after we had begun our investigation, but it was sort of halfway through – for the purpose of discussing the quality of analytical work. He had gathered them together down on Wall Street. In the memorandum in which he invited

24. Harvey Pitt served as the twenty-sixth chairman of the Securities and Exchange Commission from 2001 to 2003.
them to the meeting he said, "Here is the problem. Analytical work is no longer honest. But," he said, "I am not going to do anything about it. It is your problem."

Now, here is the chairman of the SEC saying to the CEOs of the investment banks, "I am not going to intervene in an issue as central to the integrity of our financial markets as the quality of all the analytical work that you put out there, upon which 90 million Americans base their investment decisions." He said, "I am going to leave it to you to solve the problem."


Also at that meeting were the NASD and the NYSE. How much did they do? Nothing, absolutely nothing. I will come back to that in a minute.

Let me switch to a second investigation – I am going to try to go through a couple of them – the mutual fund cases. Not to belabor the point, but you may remember, going on two years ago now, we said, "You know what? We think there are some problems in the mutual fund industry."

Parenthetically, people always ask me, how do you find out about these things? What is the source? Who comes in?

I will tell you a story. I had a meeting one day with a bunch of car dealers. As you may or may not suspect, the attorney general's office has a lot of interaction with car dealers, because their advertising is not always right on the money. I was looking around the room at the car dealers, and one of them put up his hand and he said, "Eliot, we're really sick and tired of dealing with you," something I get used to hearing. I said to them, "Well, you know what? I'm just as sick and tired of dealing with you guys. Give me something better to do." Another one put up his hand and he said, "Have you ever looked at the quality of research on Wall Street?" I said, "No. That is a good idea. I will do that."

After we were involved in the analyst cases, a bunch of analysts came into my office one day and said, "Eliot, we are sick and tired of dealing with you." I said, "Do you have anything better?" They said, "Yeah. Look at mutual funds, late trading." I said, "What is it? We will look at it."

A year after that, the mutual fund industry came in and said, "Look at the insurance industry."
Here is what happened with the mutual fund industry. We did find problems in the mutual fund industry, late trading, timing that was permitted, all of which contribute to the dilution of the return for the long-term investor.

I will tell you one other vignette. It is just too good. It goes back to the day I was at Harvard to participate in this panel. The general counsel of one of the largest mutual fund companies was on the panel with me. At one point, I turned to her and I said, “Look, I have a question for you. Why did you guys object to releasing publicly the information showing how you voted your proxies?” If you think about it, the mutual fund sector has an enormous equity pool. You would have to compare the mutual funds versus the pension funds in terms of who owns more equities in the nation. Mutual funds are enormous, enormous stakeholders. They did not want the people who actually owned the mutual funds to know how they vote proxies. I asked her, “Why is that? Why do you object to this?” She said, “It is too expensive.” I looked at her — and it was an audience such as this with lawyers and sophisticated folks present — I said, “Look, there are two problems with that answer. One, everybody in this room knows it is false. It would cost you eighty-five cents to create a Web site and post how you are voting your proxies. So you cannot possibly persuade us. The second problem flows from the first. When you give an answer that is so patently ridiculous, we know that you are hiding something more fundamental. The more fundamental thing you are hiding is that the reason you do not want to vote your proxies is that you as an industry always vote your proxies with those entrenched executives, the CEOs. Why is that? You want their 401(k) business.” Just like analysts to underwriting, it is the mutual funds to 401(k)s. The companies get to decide which mutual funds manage their 401(k)s. “You don’t want to alienate them by ever voting a proxy adverse to the interests of the CEO. So that is why you do not do it.”

I said to them something that she now appreciates. I said, “You have no idea what is about to hit you.” She did not.

But what we revealed in the mutual fund sector was this late trading and the timing that served as a massive dilution.

I want to focus on a third issue, though. That third issue is the fees that were charged by mutual fund companies. There is 7 trillion dollars in the mutual fund sector — a vast sum of money. With an average of one percent fees across the board — maybe a little higher, maybe a little
lower – you are talking about $70 billion in fees every year, fees that are paid by investors that, frankly, most people do not notice. It is representative of all the disclaimers, all the fine print you do not pay attention to. A few years ago when the market was going up eighteen percent a year, who cared? You would say, “Oh, fifty basis points, no big deal.” If the market is flat or going up four points, this is a big percentage of your return. But people should care, nonetheless — $70 billion.

As part of the settlements that we entered into when we were negotiating with the mutual fund companies, we said to them, “We want you to lower your fees,” not because I am supposed to set fees. The market should set fees. But who is supposed to negotiate fees on the part of investors? The boards of the mutual fund companies, who have a fiduciary duty to the investors. They are supposed to negotiate at arm’s length with the management companies. Lo and behold, they never engaged in that negotiation. The management companies would come to them and say, “These are the fees we want,” and they would say, “Fine.” They did not get competitive bidding. They did not try to ratchet it down. Only in a few limited contexts where there was competitive bidding did they actually apply downward pressure.

We went to the mutual fund companies. I will not explain the methodology now. It is too tedious. We calculated that this was costing investors tens of billions of dollars a year. The lack of competitive bidding swamps the harm that investors suffered as a consequence of late trading and timing. So we said to the boards, “You have got to begin to live up to your fiduciary duty and negotiate this.” In fact, some did ratchet their fees down to that point which the market otherwise would have brought it to. I won’t explain the methodology.

What was the response of the SEC and those who were adverse to our intervention? They said, “You are price fixing.” No such thing. I said, “We are just trying to get the board to do what a board is supposed to do — negotiate.” I will just give you one sentence on methodology. The way we calculated the drop in fees that we wanted was to go to the board and say to them, “You have a few contexts, a few institutional investors, who demand that you get competitive bids. What was the gap, the differential in those instances between what you charged when you got competitive bids and what you charged when you did not? Use the competitive-bid context as a proxy for what the market would bear and then reduce the fees you charged everybody else by that
They did not disagree with this methodology. They said, “That makes sense.” We saved investors a couple of billion dollars that way, or a billion. It will extrapolate out to a lot of money.

What was the response of the SEC? You cannot do it. Again, they had so embraced this notion that any government action was wrong that they rejected the single most important issue. They still are not doing anything in the context of fees in the mutual fund sector.

Let me talk briefly about the insurance investigations. I have to be careful what I say, because, obviously, these are ongoing. I merely observe that securities may be less apposite in criminal procedure when it comes to discussing the insurance investigation. I will leave that for another day.

The thing I would suggest to you is that here we have a perfect argument for why government intervention is necessary. McCarron-Ferguson was passed several decades ago, a statute that said that the federal government will leave to the states some useful things in the securities markets, but McCarron-Ferguson said that the federal government will not regulate insurance. Fine. What has happened as a result?

We have a sector that, to a great extent, has withstood and rejected and been able to push back any scrutiny whatsoever for the last thirty years. When we began to peel back the layers of the onion, merely on the brokerage side – merely on the brokerage side – with Marsh, with Aon, and Willis, which, in aggregate, have, at last calculation, over sixty percent of the world’s insurance brokerage, we have entered three settlements, one with each of these companies, that require them to return over $1 billion to their customers – individuals, businesses, big and small.

But what that does not try to measure – and there will be follow-on
lawsuits by others – is how they perverted the market by brazen bid rigging, price fixing, subversion of the marketplace, all the while that the insurance sector was saying to the world, “We are pure. We are clean.”

That is on the brokerage side. On the carrier side, which we are now beginning to peel back, we are seeing the same thing. We have ten guilty pleas, multiple investigations ongoing. Everywhere we look, we find the same behavior. Why? Because government was simply absent in this regard. The area where it has been the worst – and this stands to reason – is in the context of the offshore subsidiaries that are created. Why is that? The federal government that might have had the capacity to pierce those veils, to find out what is going on in a Barbados subsidiary or a subsidiary created in the Isle of Man or Bermuda. We, in the State of New York, do not have that capacity. We just do not have the resources. We have fifteen lawyers, total, who have done all of the Wall Street-related cases that have gotten the attention over the last number of years – fifteen lawyers. The SEC has, I think, over a thousand. I may be wrong. It may be much more than that.

Consequently, we cannot pierce those veils. We do not have jurisdiction. The federal government said, “We are not going to do it.” The insurance companies began absconding. Look at how many subsidiaries there are. Look at how much reinsurance business, reinsurance brokerage, has been shifted overseas and ask yourself, why? I think, unfortunately, the answer is going to be, because there, there is no scrutiny whatsoever. What will tumble out into the press and into the cases over the next number of months, I suspect, as other investigations heat up by other offices than mine, is that that is really where investigations are necessary. For months, I have been saying to the federal government, “Please investigate this. Begin to examine why all of these companies are doing this.” They have not yet done it, again. Why? They have been saddled by this notion proffered by the Chicago School that any intervention is wrong.

So let me sum up in terms of the first rule. With the second and third rules, I will be very quick.

The first rule: Only government can actually enforce the rule of integrity. The reason is that business will drop to the lowest common denominator ethically. Competition will drive people there. If nobody stands up and says, “This is unacceptable,” then nobody will stop doing what they have been doing. That, unfortunately, is what we have learned.
Self-regulation has been an abject failure. There was a grand compromise that was struck twenty-plus years ago, when we began deregulation. The compromise was, we as government will deregulate; you as business will self-regulate. It has not worked. During all of the investigations that we have brought, that others have brought—not once has any company come in and said, “We have got a problem to report.”

There are many other cases that I could talk about, but I will not. Second and third rules:

The second rule that justifies government intervention—for non-economists, I apologize, but this is really a purely economically-based notion—relates to externalities. Externalities are the value, positive or negative, that is not captured between the private-sector parties to a transaction. What do I mean by that? If I buy power from a utility and I am charged “X” cents a kilowatt-hour, and when they generate that power, they generate pollution that imposes a cost on a state that is northeast of us, there is a cost to society that is not borne and is not reflected in the pricing that I pay and I negotiate with the utility.

Why do I pick that example? Because I think everybody understands that we want to protect the environment. We, therefore, view it as a social good, a public good, which means that it is not captured in this type of pricing. I raise it also because we have brought a number of cases against Midwestern utilities, utility companies out in Virginia and Pennsylvania and Ohio, utilities that in generating their energy pollute our air. We breathe their air. We went to court to enforce the Clean Air Act and say, “Fellows, you are breaking the law. It is bad policy. This is a wise use of our resources.”

Again, I was met with enormous pushback from the Chicago School folks, who say, “This is an abuse of your power and the market.” I said, “No. This is the market.” Market economists understand externalities and costs, positive or negative, that need to be understood by government, so it can either subsidize or limit production of a good.

I will tell you just one very quick story about this. I was testifying down in Washington, DC, in front of the Senate Committee on Environment and Public Works. The senator from Ohio, who had been the governor, looked down at me and he said, “Attorney General Spitzer, when I was the governor, I cleaned up the air in Ohio. We cleaned up our own air. So why don’t you, instead of suing us, just clean up the air
in New York?" I looked at him and I said, "Senator, I’m very proud of you for cleaning up the air in Ohio when you were the governor. But do you remember how you did it? The way you did it was by building smokestacks that were a thousand feet tall at your power plants. You did not build those smokestacks because they were pretty or cheap. You did it because you were shifting the burden. When you build a smokestack a thousand feet tall, the pollution from Ohio Edison goes up into the jet stream and does not come down in Ohio; it comes down in New York. So I am going to sue you." And that is what we did.

Lo and behold, we won. This was not a frivolous suit. We won a summary judgment motion under the Clean Air Act. They just settled, and they are going to spend over $1 billion to stop the pollution, because that is a legitimate form of market intervention.

So the second rule is that externalities need to be measured. Where you can plausibly and rationally and efficiently intervene to stop negative externalities, and therefore protect the market, you should do so.

Now the third rule: This, I will freely observe, is the most subjective. The third rule is perhaps also the most important. The third rule is that we pass laws that capture and define the common values that we share as a community. There are certain values, there are certain common bonds among us as a community, that the market simply will not get to. I would give you two examples. One is a minimum wage for children. The marketplace, if you did not have a minimum-wage law,

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30. *Id.*

would not generate a wage scale either for low-wage workers or kids, children. We prohibit child labor.\(^{32}\) The market alone would not move to a point where children were prohibited from working, and it would not move to a minimum wage that was sufficient for people to put bread on their tables, even if they worked forty hours a week.

We as a community, as a society, believe in a minimum wage, not because the market independently will get us there, but because inherent in our sense of community is that if somebody works forty hours or more, they should be able to earn enough to put food on their tables and buy clothing for their kids. I think most of us agree with that.

Yet the Chicago School used to argue, "You do not need minimum-wage laws."

Other examples of that are the laws prohibiting discrimination.\(^{33}\) When the laws prohibiting discrimination were first proposed in the mid-1960s, the Chicago School theorists said, "You don’t need those laws, because discrimination is inefficient. Any company that discriminates, by either not selling to people of a certain gender or race, or not hiring people of a certain gender or race, will be inefficient. They will not be able to compete. They will be suboptimal." Those are the words they used. They said, "Therefore, discrimination will be eliminated by the pure force of the market."

We know that that is a great theory, but it was wrong. It simply did not happen. Not to suggest that we have overcome all the vestiges of discrimination, but certainly discrimination did not begin to be attacked and recede until we passed laws that prohibited outright and overt discrimination.

So the third argument is a very simple one, and the most powerful one: Certain common values that the market will never achieve must be enacted statutorily, even if they require certain market interventions.

I said that this third rule was the most elastic. Why is that? The reason is very simple. "Common values" is an elastic term. What those


\(^{33}\) See, e.g., 42 U.S.C. 2000(e) (1964) (prohibiting employment discrimination on the basis of race, color, religion, sex, or national origin).
values are cannot be defined by any one person. That is the political process. As soon as you open it up to politics, there is an element of elasticity and uncertainty.

So I freely acknowledge that that third rule is the one that can be most readily abused. Having said that, it is, in a way, the most important, because the laws against discrimination, the laws in favor of a minimum wage – hopefully, a rising minimum wage – are the essence of how we define ourselves as a community.

Let me, before I stop and take your questions, tell you a very brief story that is not terribly flattering about myself, perhaps, but I think tells you something about everything that we have been doing. There is one core central principle that it all comes back to.

Not that you care, but I have three daughters. My wife and I were terribly lucky – three daughters. They are ten, twelve, and fifteen. Most of you, at least, are too young to have teenage daughters. But when you have a teenage daughter, sometimes beginning a conversation with her is not the easiest thing in the world. At the dinner table one night, I figured that out or got evidence of it. I said to her, “Elyssa, what is your favorite word?” She looked me as though – and she was right – this was really a pathetic effort on the part of a father to begin a conversation. She rolled her eyes the way teenagers do, and she said, “Dad, I don’t have a favorite word. Even if I did, I would not tell you. But I know what yours are.” I said, “Oh? What are mine?” She said, “Fiduciary duty.”

As I say, it is kind of pathetic. But the reason I mention it is because everything that we have been talking about comes back to that very simple notion. Whether you are an elected official, whether you are a CEO, wherever you are in life, if people were loyal to the fiduciary duty, most of the problems that we have had would not have emerged. It is nothing more complicated than that, nothing more sophisticated.

My hope is that, as a result of this really difficult period, where we are seeing regulatory lawyers put in the place of corporate CEOs – and that is not a good thing – I hope that at the end of it people will have an allegiance to fiduciary duty that will be deeper, that will prevent us from needing to go through this once again five or ten years from now.

Thank you very much for your attention. I appreciate it.

I see some people want to leave immediately. That is great. We are taking names outside of those who leave early. Some of you have classes. If you are leaving to go to class, that is okay, but if you are
leaving for a drink, it is not.

If you want to ask questions, that’s wonderful. Just put up a hand.

QUESTION: I read an article about the fact that one of the reasons you were able to get into these companies was because the Patriot Act\textsuperscript{34} allowed you to be able to use some excessive–efficient ways to use the search warrant, that otherwise you might not have been able to go in and get a lot of information. Is that accurate?

ATTORNEY GENERAL SPITZER: That is actually not true. I do not know where they said that. We have not done that. First of all, I am not sure that I have powers pursuant to the Patriot Act. It is a federal statute, and, as far as I know, its powers extend to federal law enforcement officers. We were able to obtain the information simply pursuant to our capacity to subpoena business records. It was very simple, very mundane, very boring. It was just the ordinary course of investigative powers that the attorney general has had for decades, if not a century.

QUESTION: Two questions. One is, is it oxymoronic to speak of an honest corporation?

ATTORNEY GENERAL SPITZER: Absolutely not. Let me tell you something. I hope we all appreciate this in due course. It is the case—I don’t want to say it is just a few bad apples—that there are systemic problems that we have been trying to address, and systemic problems need systemic solutions.

Having said that, it is certainly not the case that most of the CEOs out there or most of the businesses are doing things that are crooked. I do not buy that. The market works and it creates wealth. Competition is wonderful. At times this tension—not now, I hope—between my office and the SEC proves that competition works, not only in the private sector, but in government. People wake up. They like healthy competition.

So I believe in the market. The vast majority of CEOs out there are doing the right thing.

I will tell you a true story. I was introduced by a CEO of a major company—again, I will not use a name—at something called the

Business Roundtable.\textsuperscript{35} In the room, there were a hundred CEOs of, perhaps, the hundred largest companies in America. The CEO who introduced me said, “Eliot, we don’t really do long introductions here, but I just want you to appreciate that ninety-nine percent of the CEOs in this room are honest and ethical and hardworking.” I got up to the lectern, and I could not resist. I said, “I agree with you, but I am only interested in the one percent. Who is it?” They did not like that. I think it is one percent.

QUESTIONER: My second question is, I hear you saying you met so much resistance. Is this just the old boys that are in there? To what extent is it political?

ATTORNEY GENERAL SPITZER: Forget partisanship as in politics. I assume that those who take a different view believe in their ideological position, but I also do think that there is an ossified system and that any system that benefits a limited number of people will have those who defend it, especially those who benefit from the system. Tom Donohue – I do not impugn his integrity, obviously; he is the president of the Chamber. But AIG contributed $17 million to the U.S. Chamber of Commerce for them to argue, not in favor of more interventionist regulatory authority, but against the sorts of things we are doing. So that is what they are going to say.

There is an ossified structure that benefits certain people. They will continue to defend the status quo. It is never easy to push back against the status quo. Yet every now and again, the status quo needs to be shaken, because the status quo can become corrupt.

QUESTION: Aram Schvey, from the Crowley Program in International Human Rights here at Fordham Law School.

I wanted to know if you saw the private suits that have been filed under the Alien Tort Claims Act\textsuperscript{36} against various corporations for gross human rights violations overseas as part of the way of dealing with these sort of market externalities – rather than shifting it from one state to another, shifting it from one country to another – and whether the attorney general’s office has ever thought of filing suit based on gross human rights violations.


\textsuperscript{36} 28 U.S.C. § 1350 (1948) (granting jurisdiction to U.S. federal courts over “any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States”)

human rights violations for acts committed overseas by corporations—
for example, with oil extraction in Sudan or the actions of various
companies in Brazil.

ATTORNEY GENERAL SPITZER: The short answer is, we
haven’t thought about it. I would have to look at the statute, and also the
facts, obviously, to ascertain first, jurisdictionally, whether we are in a
position to assert those causes of action, obviously, then factually,
whether the causes of action could be made out. We just have not
thought about it. I apologize.

QUESTION: Could you describe briefly finite reinsurance and why
you think it is unethical?

ATTORNEY GENERAL SPITZER: The answer is, no, you cannot
describe finite insurance briefly. It is too late in the day to get into it,
other than to say finite insurance is not necessarily unethical or illegal.
Mischaracterizing an insurance policy that is not finite insurance as
finite insurance, mis-describing and handling an accounting in a way
that is intentionally designed to shift reserves illegally is illegal. That is
called fraud, and that is what is at the crux of our investigations that are
ongoing right now.

Just to make it clear—a different context—all contingent fees are
not unethical or illegal. Contingent fees—and I will not get into the
whole Marsh insurance debacle—that lead you to violate fiduciary duty
and then to rig bids are illegal. But contingent fees per se are not illegal.
It may be the case that prohibiting them in certain contexts is the best
prophylactic to ensure that the customer gets what he or she is due, but I
would not say, writ large, that all contingent fees are illegal or should be
banned. In some contexts, they should be, but not in all.

QUESTION: Is the idea, based on your three golden rules that you
prefaced for us—

ATTORNEY GENERAL SPITZER: I am not sure they are golden
rules. They are rules.

QUESTIONER: Okay, our new rules that we have now. You say
that a government, at the end of the day, is the only thing that can
enforce them. But when we have more of an international economy at
this point, when we clean up our act and the rest of the world does not,
how do we handle that? We have institutions like the WTO, but they
generally are not held accountable for doing those kinds of things, like
we work so hard here to do.

ATTORNEY GENERAL SPITZER: That is an excellent question.
It gets harder and harder, where capital is as global as it is and moves as quickly as it does, to try to create an ethical environment, when you are fearful, of course, that people will simply flee the jurisdiction – not flee as in running away from it, but move operations elsewhere.

The good news is that the United States’ share of the global economy is still so enormous, there is no multinational company that can forgo a presence here. We are still the single largest market, still the most important capital market. Hopefully, that will continue to be the case. I think it will continue to be the case. Therefore, they cannot avoid abiding by our mandates.

In the context of Sarbanes-Oxley, you are seeing some articles that companies are deciding to de-list from the NYSE. They are moving over to some of the foreign exchanges. But it is actually precious few companies, and I do not think that is meaningful to lower our ethical standards. Virtually all the companies I have dealt with know they have to be here, want to be here, will be here, will live up to the ethical mandates that we create here. Frankly, overseas regulators are increasing and improving in elevating their ethical mandates. When I speak to them, they are saying, “What do we need to do to make sure that the sorts of violations that you have seen in your markets do not exist here?” They want to get rid of them overseas as well, because those violations are injurious to the marketplace.

So I think we can lead the charge in elevating ethical standards rather than, ourselves, falling prey to the argument that was made by the investment bank, which is that we have to sing to the lowest common denominator articulated by some foreign nation, and therefore drop farther and farther down.

QUESTION: Can you discuss your plans for hedge-fund regulation?

ATTORNEY GENERAL SPITZER: I do not have any plans for hedge-fund regulation. Occasionally – more than occasionally – I am asked, “Do you think the SEC is doing something smart or not in requiring hedge funds to register?” I do not think there is any great harm that results from it. I also don’t think there is any great good. The reason for that is that the registration form itself will not reveal any of the underlying problems.

Hedge funds do some bad things. Hedge funds sometimes take

short positions and intentionally circulate misinformation to try to drive the stock down, to benefit from a short position. But that is not a game that is intrinsic to being a hedge fund. In other words, there is nothing about the hedge-fund structure, as a structure, that I have seen that is problematic. In fact, I would argue that, in a way, a hedge fund is more closely aligned with the interest of its investor, because usually, the way their fees are structured, you get one percent, two percent as a fee, and then an override. So the fund manager wants to do well, wants to perform well, and his investors will do well as a result.

The improprieties come in their trading practices. Those trading practices have to be addressed, and should be addressed. But those are not trading practices that result because they are hedge funds. They are just games that are played in the marketplace on a regular basis by all sorts of investors.

One area where hedge funds do often get into trouble is in valuation of their portfolio. The reason for that does go back to the compensation system. If a hedge-fund manager gets an override, if you have been up by more than twenty percent in any given year, if you have a portfolio of liquid stocks, you can mark-to-market every day. That is easy. If you have a portfolio of thinly traded debt, then you can come up with a valuation that may not be a real one, go back to your investors and say, “Look at what a great year we had. You owe me “X” dollars,” and it may not be a real market valuation.

But that is, I think, a secondary issue.

QUESTION: My question is in two parts. One, what do you think about the recent push by the Internal Revenue Service to investigate practices in the nonprofit sector? Second, how do you think especially the smaller nonprofits that are understaffed as it is would be able to cope with extra scrutiny in terms of their tax practices or their spending practices?

ATTORNEY GENERAL SPITZER: You are raising a series of thorny issues. Let me frame it this way. After Sarbanes was passed, there was a lot of talk—and I, unfortunately, contributed to it. One day I said that maybe we need a Sarbanes-Oxley for the not-for-profit sector, because there are problems there, governance problems, as you would expect, the not-for-profit sector being an incredibly diverse sector. There are some enormous entities controlling billions of dollars and then many more small not-for-profits that are thinly staffed and have very little money.
The idea of overlaying that much regulation on the not-for-profit sector is a bad idea. We need to ensure that those who manage the not-for-profit assets of the nation are living up to their fiduciary duty. Imposing upon them all the rigorous constraints of Sarbanes-Oxley probably would be a horrendous idea that would drive people off the boards in the not-for-profit community, would use up, as you say, scarce resources in a sector that is already struggling. So I do not think we should go that route.

What we do have to do, on the other hand, is educate boards in the not-for-profit sector to do more and do better, to be more interventionist, and improve the quality of governance in that sector. But I do not think anybody has quite figured out how we do it. We have a very active charities bureau that works with the not-for-profits on a regular basis, to try to improve the quality of governance. Occasionally, we have to bring litigations. There is the infamous Grasso case, but that is really sort of an exceptional case. More typically, we find just a failure and hand-in-the-cookie-jar type of action.

I am not dodging the question. We need some subtlety. We need to educate. Sarbanes-Oxley does not apply wholesale to the not-for-profit sector. What the IRS is up to I just do not know, so I cannot speak to that.

QUESTION: In your case right now against former Chairman Grasso — I know you probably cannot speak on everything — do you foresee adding anybody else to the suit that is ongoing?

ATTORNEY GENERAL SPITZER: Do you have anybody in mind?

QUESTIONER: Is he going to have to pay back some of that money?

ATTORNEY GENERAL SPITZER: Whether he has to pay it back depends upon whether we win. If we win, he will.

Let me explain very quickly — and I will make this the last answer — why we sued whom we did. This goes back to the prior question. What is the legal principle we want to establish? Why did we bring this case? There is a statute that says that the salary that a not-for-profit pays to any

individual has to be commensurate with the value of the services provided.\textsuperscript{39} We have to vindicate that principle. In my humble opinion – and we will prove this in court, if need be – $200 million was a bit more than the value of the services he provided. So we have to vindicate that principle.

The question is, from whom do you recover it? He has the money, so he should disgorge it – ill-gotten gains, several number of theories. Is the board liable for having permitted this to happen? In the not-for-profit sector, the rule that we have lived by, the rule that I believe is appropriate, is that making a poor judgment, making a bad judgment, when you are on the board of a not-for-profit does not create liability. What does create liability is misrepresenting something to the board, lying to the board, deceiving the board.\textsuperscript{40} That is the distinction that we stuck to, and that is why we sued Mr. Grasso and Mr. Langone,\textsuperscript{41} because Mr. Langone, as a board member, we will prove, did provide misinformation to the board.

Other board members – and this is coming out, and it will come out – are going to be thoroughly embarrassed by the failure on their part to make smart judgments, the failure on their part to be adequately informed. But that is not a theory of liability. That is just an argument for performing better.

So that is the distinction that we tried to create. It is what we have stuck to, day in and day out. Just to state the obvious, there are going to be all sorts of interpretations about why we sued whom we did. People would attribute all sorts of improper motivations. But I can tell you, it was nothing more sophisticated and more complicated than what I just told you.

Thank you all so much. It has been a joy being here.

\textsuperscript{39} N.Y. Not-For-Profit Corp. Law §§ 202(a)(12) & 515(b) (McKinney 2005).
\textsuperscript{40} See N.Y. Not-For-Profit Corp. Law § 720(a).
\textsuperscript{41} Former NYSE director Kenneth Langone was the chair of the NYSE compensation committee when Richard Grasso’s controversial pay was approved.