UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

OFFICE OF THE
GENERAL COUNSEL

September 13, 2007

Stuart M. Cohen, Clerk
New York State Court of Appeals
20 Eagle St.
Albany, NY 12207-1095

Re: Vigilant Insurance Co. v. The Bear Stearns Cos., Index No. 602160/03

Dear Mr. Cohen:

Please find enclosed for filing the original and one copy each of the Securities and Exchange Commission's

1) Notice of motion for permission to file statement amicus curiae;

2) Motion for permission

3) Proposed amicus statement.

In addition, we have enclosed an extra copy of the notice of motion as well as a stamped, self-addressed envelope. Please file stamp and return the extra copy.

Thank you for your attention to this matter.

Respectfully submitted,

Mark Pennington
Assistant General Counsel
202-551-5189

cc: John H. Gross
Joseph Finnerty
James A. Skarzynski

COURT OF APPEALS
STATE OF NEW YORK

VIGILANT INSURANCE CO., FEDERAL INSURANCE CO., and GULF INSURANCE CO., Plaintiffs-Appellants, v. THE BEAR STEARNS COMPANIES, INC., Defendant-Respondent.	Index No. 602160/03

NOTICE OF MOTION OF THE SECURITIES AND EXCHANGE COMMISSION FOR PERMISSION TO FILE STATEMENT AMICUS CURIAE

PLEASE TAKE NOTICE that, together with the accompanying proposed statement amicus curiae, the Securities and Exchange Commission will move this Court on October 1, 2007, at 10 a.m., for an Order granting permission for the Commission to file the proposed amicus statement. *See* 22 NYCRR 500.23.

As set forth in the statement, the Commission has a strong interest in making clear that, contrary to defendant-respondent Bear Stearns Companies' contention in the Appellate Division, the Commission did not employ what Bear Stearns refers to as a "legal fiction" concerning the nature of the relief sought in a

settled civil law enforcement action that it brought against Bear Stearns, nor did it obtain in that action a form of relief not permissible under the federal securities laws. The Commission's proposed statement explains that there is no triable issue of fact in this case as to whether the Commission sought and obtained disgorgement of ill-gotten gains, a permitted form of relief in Commission actions under the federal securities laws, and not compensatory damages, a form of relief that is not permitted.

For the foregoing reasons, the Commission requests permission to file the statement amicus curiae submitted with the motion.

Respectfully submitted ,

JACOB H. STILLMAN
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September 13, 2007

CERTIFICATE OF SERVICE

I hereby certify that on this 13th day of September, 2007, I caused to be served one copy each of the (1) Notice of Motion, (2) Motion of the Securities and Exchange Commission for Permission to File Statement *Amicus Curiae*, and (3) proposed Statement of the Securities and Exchange Commission *Amicus Curiae*, on counsel for the parties by overnight courier at the following addresses:

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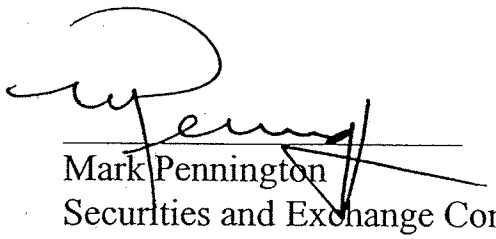

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COURT OF APPEALS
STATE OF NEW YORK

VIGILANT INSURANCE CO., FEDERAL INSURANCE CO., and GULF INSURANCE CO., Plaintiffs-Appellants, v. THE BEAR STEARNS COMPANIES, INC., Defendant-Respondent.	Index No. 602160/03

MOTION OF THE SECURITIES AND EXCHANGE COMMISSION FOR PERMISSION TO FILE STATEMENT AMICUS CURIAE

The Securities and Exchange Commission submits this motion for permission to file the proposed statement amicus curiae submitted with this motion. *See* 22 NYCRR 500.23. As set forth in the proposed amicus statement, the Commission has a strong interest in making clear that, contrary to Bear Stearns Companies' contention, the Commission did not employ a so-called "legal fiction" concerning the nature of the relief sought in a settled civil law enforcement action that it brought against Bear Stearns, nor did it otherwise induce the district court that presided over that federal action to grant a form of relief not permissible under the federal securities laws. The Commission's proposed statement explains that there is no triable issue of fact in this case as to whether the Commission sought

and obtained disgorgement of ill-gotten gains, a permitted form of relief under those laws, and not compensatory damages, a form of relief that is not permitted.

For the foregoing reasons, the Commission requests permission to file the statement amicus curiae submitted with this motion.

Respectfully submitted ,

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September 13, 2007

COURT OF APPEALS
STATE OF NEW YORK

VIGILANT INSURANCE CO., FEDERAL INSURANCE CO., and GULF INSURANCE CO.,	
Plaintiffs-Appellants,	Index No. 602160/03
v.	
THE BEAR STEARNS COMPANIES, INC.,	
Defendant-Respondent.	

STATEMENT OF THE SECURITIES AND EXCHANGE COMMISSION AMICUS CURIAE

INTEREST OF THE COMMISSION

In its briefs in the Appellate Division, defendant-respondent Bear Stearns Companies argued that the Securities and Exchange Commission employed what Bear Stearns referred to as a "legal fiction" concerning the nature of the relief sought in a settled civil law enforcement action that the Commission brought against it. *See*, Appellants' Joint Brief at 33-35 (discussing Bear Stearns's "legal fiction" argument). The Commission employed this legal fiction, Bear Stearns said, in order to obtain compensatory damages, a form of relief that is not permitted in Commission actions under the federal securities laws, rather than

disgorgement of ill-gotten gains, which is a permitted form of relief. This "legal fiction" claim was unfounded, and we do not believe that Bear Stearns raised a triable issue of fact as to whether under the federal securities laws, the relief granted against it was not disgorgement, but damages.

Acceptance of Bear Stearns's erroneous argument could raise questions in future cases about whether the Commission is seeking relief that is outside of its authority. Moreover, part of the basis for Bear Stearns's argument that the Commission obtained damages rather than disgorgement was the contention that a court hearing a settled Commission case cannot order disgorgement unless the Commission presents evidence of the precise amount of ill-gotten gains. This proposition, if accepted, could interfere with the Commission's ability to settle cases in an efficient manner, as it would prevent the Commission from settling without further investigation even though both the Commission and the defendant are willing to settle for disgorgement of a particular amount in light of the available evidence and the Commission's regulatory objectives.

The Commission submits this statement amicus curiae in order to make clear that it did not mislead the federal district court in the Commission's case, whether through the use of a "legal fiction" or otherwise, and that as a matter of law, the relief that it obtained was entirely proper and within the authority of the

Commission to seek, and the district court to grant. We take no position upon any other issue raised in this appeal, including the substantive state law questions.

BACKGROUND

This matter arises from Bear Stearns's attempt to obtain reimbursement from its insurers for $25 million that Bear Stearns paid in disgorgement as part of the settlement in SEC v. Bear Stearns, No. 03-2937 (S.D.N.Y.), one of the cases brought by the Commission in cooperation with the State of New York and securities industry self-regulatory organizations against major investment banks to remedy conflicts of interests that threatened the independence of the firms' securities analysts. In the Appellate Division, Bear Stearns conceded that true disgorgement of ill-gotten gains under the federal securities laws would not be an insurable loss under New York law. It asserted, however, that the $25 million was not actually disgorgement, but was instead compensatory damages for those injured by Bear Stearns's conduct, and that as such it was an insurable loss. Bear Stearns urged that the Commission engaged in the "legal fiction" of calling the relief disgorgement because the securities laws authorize the Commission to obtain disgorgement but do not authorize it to seek compensatory damages.

We explain below the background of the Commission's case, and in particular, that the key documents in the settlement – the Commission's complaint,

Bear Stearns's consent to entry of judgment, and the district court's judgment – all called for Bear Stearns to pay "disgorgement." In the argument section of this statement we demonstrate that Bear Stearns raised no triable issue of fact as to whether these documents mean anything other than what they say, namely that Bear Stearns agreed to, was ordered to, and did, pay disgorgement.

A. The Commission's Complaint Alleged That Bear Stearns Failed to Guard Against Conflicts of Interest That Threatened the Independence of its Securities Analysts, and Sought Disgorgement of the Ill-gotten Gains Arising from this Misconduct.

The Commission alleged that investment banking was an important revenue source for Bear Stearns (Complaint, ¶ 24), and that the firm's research analysts were encouraged to help the firm's investment banking business generate profits. (See, e.g., ¶ 11.) Research analysts "were aware that, in certain circumstances, their positive and continued coverage of particular companies was an important factor for the generation of investment banking business." (¶ 28.) Indeed, the research analysts' compensation was significantly based on their involvement in investment banking activities, including the fees and secondary trading commissions generated from those activities. (¶¶ 29, 38.) For example, the complaint quotes a senior analyst who, in describing his key accomplishments for

fiscal year 2000, highlighted how his activities generated investment banking profits for the firm:

> Corporate finance: generated over $23 million in fees to the firm in nine separate transactions: *Storage networking: identified a new financial opportunity for the firm, which resulted in six transactions * * *. I should be designated as a finder for Ancor [Ancor Communications], JNI [JNI Corp.] and Vixel [Vixel Corp.]. *iApplinces: identified a new industry category * * * which was a source of two IPOs * * *. *Agilent [Agilent Technologies]: I should be designated as a finder – or at least a save for Agilent. BS pitched the business and lost. I went in and re-won the business, generated fees of around $2.5 million to the firm. (¶ 34.)

Bear Stearns's research analysts thus were subject to a fundamental conflict of interest between supporting the firm's investment banking business and providing objective research. The Commission alleged that this conflict of interest, coupled with Bear Stearns's failure to ensure compliance with SRO rules by adequately and appropriately managing this conflict, generated significant investment banking business (and thus more profits) for Bear Stearns. (See, e.g., ¶¶ 21-24, 34, 49, 68, 69 (analyst's statement that "we got paid for this [favorable rating] * * * and I am going to Cancun tomorrow b/c of them!"), 70-72, 75-77). It sought entry of a judgment "[o]rdering Bear Stearns to account for and disgorge all proceeds it has obtained as a result of its conduct," among other relief.

B. Bear Stearns Agreed to Pay Disgorgement, and the District Court Entered a Judgment Ordering it to Do So.

Before the Commission filed its complaint, Bear Stearns submitted an offer to settle the proposed Commission action, as well as other potential actions by self-regulatory organizations and state regulators, by paying a total of $80 million, including $25 million in disgorgement, along with other relief. [1] The Commission accepted Bear Stearns's settlement offer, and on April 21, 2003, Bear Stearns signed a consent to entry of final judgment in the district court embodying the terms of that settlement, including payment of "$25,000,000 as disgorgement of commissions and other monies." On April 28, 2003, the Commission filed its complaint.

On October 31, 2003, the federal district court approved the proposed settlement and entered a final judgment that provided that "[a]s a result of the violations alleged in the Complaint," Bear Stearns would pay a total amount of $80 million, which included "$25 million, as disgorgement of commissions and other monies."

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[1] In addition to disgorgement, the $80 million included a $25 million penalty, $25 million to be used to procure independent research and to fund other undertakings called for by the settlement, and $5 million for investor education.

C. Despite the Plain Language of the Complaint, of the Consent to Judgment and of the Final Judgment, Bear Stearns Urged In The Appellate Division That it Did Not Pay Disgorgement, and That the Commission Used a "Legal Fiction" to Obtain Compensatory Damages.

In its appeal to the Appellate Division from the grant of summary judgment against it on the issue of insurability of the disgorgement payment, Bear Stearns asserted that in the federal district court, the Commission had "employed the 'disgorgement' language as a legal fiction" (App. Div. Br. 54) to obtain compensatory damages. For instance, it argued that:

> [I]n the consent judgment, [the Commission] effectively sought and obtained legal relief, compensatory damages for investors who purchased stock at inflated values due to the influence of analysts' reports. Nevertheless, because it lacked statutory authority to obtain such relief, the SEC could not expressly refer to compensatory damages in the Consent Judgment. All it could assert as its basis for authority – *and it was a pure legal fiction* – was that the relief was "disgorgement." (App. Div. Br. 56-57, emphasis added.)

ARGUMENT

A "legal fiction" is an assumption made by courts that something is true, even though it may be untrue; fictions are typically employed in judicial reasoning to alter how a legal rule operates. See Black's Law Dictionary (definition of "legal fiction"). The Commission did not employ a legal fiction in order to obtain compensatory damages, which are an impermissible form of relief in Commission

actions under the federal securities laws. Rather, the Commission sought and obtained disgorgement.

The Commission's complaint clearly alleges that Bear Stearns received money, including investment banking revenue, that it would not otherwise have received but for its misconduct. Indeed, the very purpose of employing analysts to support the investment banking operation was to increase the firm's investment banking business. Furthermore, as we have explained, the complaint, the consent to entry of judgment and the district court's judgment itself all explicitly described the payment as "disgorgement." The grounds urged by Bear Stearns in the Appellate Division in support of its "legal fiction" argument are not sufficient to call into question these unambiguous documents, or to raise a triable issue of fact as to whether it was required to disgorge ill-gotten gains.

Bear Stearns made essentially two arguments in support of its contention that it paid damages and not disgorgement. First, it noted that the Commission's complaint does not allege a specific amount of ill-gotten gains, and that the Commission had not proffered evidence as to the precise amount of those gains at the time the case was settled. Rather, Bear Stearns said, the Commission based the amount, in part, on Bear Stearns's market share. Second, it observed that the Commission, in keeping with its usual practice with respect to disgorged funds,

proposed that the money be distributed to uncompensated investors who had been injured by Bear Stearns's misconduct. Neither of these contentions should be allowed to disturb the conclusion that, as a matter of law, what Bear Stearns paid was disgorgement under the federal securities laws.

The lack of specific allegations concerning the amount of disgorgement is not dispositive, or even noteworthy. The Commission usually pleads facts showing that there were ill-gotten gains and requests unspecified disgorgement of an amount to be determined in the action. Furthermore, due to the nature of the misconduct in this particular case and the point in time at which the matter was settled, it would have been a complex matter to ascertain specifically what amount of investment banking fees should be considered ill-gotten gains arising from the analysts' conflicts of interest. For instance, sometimes investor losses can shed light on the amount of ill-gotten gains, but in this instance it was difficult at the time of the settlement to identify which investors had been harmed.

Nor is the absence from the record of complete evidence from which the amount could have been calculated compelling. Bear Stearns agreed to settle the case before it was even filed, and the Commission had not conducted the discovery that would have been required if the matter had gone to trial, which would have produced more extensive evidence as to the amount of disgorgement.

In short, based on all the information that it had at the time it accepted the settlement offer, the Commission believed that the disgorgement amount reasonably represented Bear Stearns's ill-gotten gains, even though the disgorgement amount was not based on a full discovery record or a precise method of calculation. Moreover, the settlement was part of an industry-wide investigation of similar practices followed at a number of the largest investment banks, and the Commission believed that the payment offered by Bear Stearns was proportional to the payments offered by the other settling firms. None of the factors identified by Bear Stearns supports the conclusion that the Commission was seeking, or the district court awarded, anything other than ill-gotten gains from the alleged misconduct.

The Commission's intention at the time of settlement to ask that the disgorged funds be distributed to injured investors also does not suggest that the payment was not disgorgement. To the contrary, the Commission ordinarily proposes such a disposition for disgorged funds, and the courts have recognized that this does not change the nature of the remedy.

The purpose of disgorgement is to deprive wrongdoers of ill-gotten gains. Once funds are disgorged, there remains the separate issue of what to do with the money, and it is "within the court's discretion to determine how and to whom the

CONCLUSION

For these reasons, we urge that there is no triable issue of fact as to whether under the federal securities laws, the relief granted in the Commission's case was disgorgement, not compensatory damages.

Respectfully submitted,

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September, 2007

money will be distributed." SEC v. Fischbach Corp., 133 F.3d 170, 176 (2d Cir. 1997). The Commission typically asks the court to distribute disgorged funds to uncompensated investors who have been injured by defendants' actions. Id. at 174 (citing the Commission's policy of "whenever possible * * * recommend[ing] a distribution plan by which a defendant's unlawful gains are paid out to defrauded investors"). Indeed, Congress explicitly recognized the practice of using a disgorgement fund for the benefit of the victims of a violation in Section 308 of the Sarbanes-Oxley Act of 2002, which provides that civil penalties obtained in Commission actions may be added to the disgorgement fund to be distributed "for the benefit of the victims of" the violation. 15 U.S.C. 7246(a). Compensation of injured investors has been recognized as a "distinctly secondary goal" of disgorgement that does not transform the payment into compensatory damages. Fischbach Corp., 133 F.3d at 176.

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September 7, 2007

By First Class Mail and E-Mail

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Re: *Vigilant Insurance Company v. The Bear Stearns Companies Inc.*,
No. 602160/03 (NY County)

Dear Michael:

I write in response to your letter of June 18, 2007 in order to clarify some of the issues going forward regarding the production of documents in the above-referenced matter. We will address the issues raised in your letters of March 23 and 30, 2007 under separate cover.

Privilege Log for Bear Stearns Documents: Bear Stearns has never refused to produce a privilege log. The Bear Stearns privilege log, however, will be limited to identifying the documents withheld on grounds of privilege that otherwise come within the categories of documents Bear Stearns has agreed to produce. The Bear Stearns responses to plaintiffs' document requests are quite specific as to the categories of documents that Bear Stearns has agreed to produce. Because Bear Stearns, based on the objections set forth in its responses, has not agreed to produce all documents that concern in any way to the research analyst regulatory investigation but instead has identified the specific categories of documents to be produced, it follows that those privileged documents that fall outside the categories of documents Bear Stearns has agreed to produce will not be logged. Bear Stearns thus will provide a comprehensive privilege log that will include all responsive documents (as specified in the Bear Stearns responses to plaintiffs' document requests) withheld on grounds of privilege. Please let us know if you require further clarification on this point.

Your letter makes a bald assertion that responsive documents were wrongly redacted and withheld, without asserting any support for that contention or pointing to any specific documents. Regardless, if you are referring to the documents Bear Stearns produced to the Regulators, we fail to see how whether anything that might have been wrongly redacted or

withheld is relevant considering it would not have been considered by the Regulators and therefore cannot have influenced the terms of the settlement which is the crux of this litigation. Moreover, Bear Stearns has, with respect to such documents, only agreed to produce the documents as they were produced to the Regulators which, of course, means that the production to you will include the same redactions as those made in the production to the Regulators.

Continuing Production of Non-Privileged Documents: We are continuing to review and produce documents received from our client. Bear Stearns believes that it has produced almost all, if not all, of the documents that Bear Stearns produced to the Regulators. We also believe that we have now produced many documents reflecting communications between Bear Stearns and the Regulators, although Bear Stearns cannot confirm that it has produced all of the communications with the Regulators, as its review and production is continuing.

Cadwalader Documents/Privilege Log: We have been working with Cadwalader in connection with its response to the subpoena and its production of responsive documents in its possession. As previously stated, Cadwalader's production will encompass the same categories Bear Stearns agreed to produce. If you require a formal response to document this fact, we will work with Cadwalader to supply such a response. With respect to your comments regarding a Cadwalader privilege log, we have never stated that Cadwalader would not produce any privilege log whatsoever. To the contrary, you will be provided with a log reflecting Cadwalader documents that have been withheld on the basis of privilege. As explained above regarding the logging of Bear Stearns' privileged documents, privileged communications and documents that do not come within the categories of documents Cadwalader has agreed to produce will not be logged.

Documents Relating to the Underlying Investigation: We are, quite frankly, at a complete loss regarding your assertion that we somehow "reaffirmed Bear Stearns' refusal to produce documents that relate to the Regulators' underlying investigation." Bear Stearns has not refused to produce documents that relate to the Regulator's underlying investigation. In fact, Bear Stearns has already produced, or will produce, the Bear Stearns document production to the Regulators as well as all of its communications with the Regulators. If you have a specific response to a specific document request that you wish to discuss further, please let us know.

Electronic Production: Bear Stearns is currently in the process of reviewing electronic information beyond what was previously produced to the Regulators. Bear Stearns fully intends to produce non-privileged electronic information that is responsive to your document requests. Relevant, non-privileged Cadwalader emails will also be produced.

Other Insurance: Bear Stearns does not believe that any insurance coverage would apply to the losses at issue in this case, and therefore there are no documents that would be responsive to your requests.

Tax Returns: As we discussed at our March 26, 2007 Meet and Confer, Bear Stearns has agreed to provide you with information concerning the relevant category, for tax purposes, Bear Stearns used for its payments to the Regulators. We hereby confirm that Bear Stearns included the non-penalty portion of the payments made in settling the research analysts regulatory investigations as an expense on its tax returns.

Internal Investigatory Materials: We have confirmed that, other than preparing its defense of the various regulatory investigations, Bear Stearns conducted no other internal investigation of the matters raised by the Regulators.

Interrogatory Responses: Bear Stearns does not intend to serve amended and/or supplemental interrogatory responses because it has fully complied with its obligations under the New York Civil Practice Law & Rules ("CPLR"). Regarding Bear Stearns' Responses and Objections to Interrogatory Nos. 1-8 and 12-13, Bear Stearns has produced documents which contain the information sought in the interrogatories and has objected to the suggestion that Bear Stearns, as opposed to plaintiffs, must bear the burden of extracting the information you seek from the documents. Regarding Bear Stearns' Responses and Objections to Interrogatory Nos. 17-18, 20 and 24, Bear Stearns has objected to those interrogatories and stands by its objections. Also, contrary to your assertion, Bear Stearns has answered all of its substantive interrogatory responses under oath. Bear Stearns objected to the remaining interrogatories, and the CPLR does not require that Bear Stearns provide objections under oath. Regardless, Bear Stearns' Supplemental Response, which was duly verified, explicitly incorporated its prior responses.

Very truly yours,

Francis D. Landrey

cc: John H. Gross (by e-mail only)
Howard S. Schrader (by e-mail only)
Evan Shapiro (by e-mail only)
Grant Hering (by e-mail only)