CA, INC.
SPECIAL LITIGATION COMMITTEE REPORT

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I. EXECUTIVE SUMMARY

A. *The Formation of the SLC*

The Special Litigation Committee (the "SLC") of CA, Inc. ("CA" or the "Company") (formerly known as Computer Associates International, Inc.) was formed by the CA Board of Directors (the "CA Board") on February 1, 2005 in response to the filing of a consolidated amended derivative complaint on January 7, 2005 (the "2005 Derivative Action"), which alleges various claims on behalf of CA against twenty-two (22) current and former CA directors, officers, and employees and its current and former independent auditors. The claims in the 2005 Derivative Action arise out of a massive accounting fraud perpetrated by the Company's senior-most executives from as far back as the late 1980s through 2001, and their cover-up of that fraud, which lasted through mid-2004. That conduct – the practice of extending CA's fiscal quarters beyond their natural conclusion to prematurely recognize additional revenue – has come to be known as, and will be referred to as, "the 35-Day Month."

As a result of this conduct, CA was forced to restate $2.2 billion in revenues, and the ensuing cover-up has been described by the U.S. Attorney's Office for the Eastern District of New York (the "USAO") as "the most brazen and most comprehensive obstruction that we've witnessed in recent history." To date, eight of the Company's former senior executives have pled guilty to federal securities fraud and/or obstruction of justice charges. The Company itself has acknowledged that, through the conduct of those CA executives, it violated the law and accepted responsibility as part of a Deferred Prosecution Agreement ("DPA") entered into with the USAO, dated September 22, 2004.

In its authorizing resolution, the CA Board charged the SLC to investigate the claims made in the 2005 Derivative Action, and to determine and control the Company's response to those claims. The CA Board has also charged the SLC to "determine and control" the Company's response to certain motions for relief from judgment, made pursuant to Federal Rule of Civil Procedure 60(b), that were filed in connection with the 2005 Derivative Action. This report constitutes a summary of the SLC's investigative efforts and findings, and the SLC's determination as to whether, in exercising its business judgment under Delaware law in the best interests of CA and its shareholders, the claims alleged in the 2005 Derivative Action should be pursued, dismissed, or otherwise resolved.[1]

B. ***The SLC's Investigation***

The SLC, through and with the assistance of counsel, conducted an independent, in-depth, and extensive factual investigation, including: (i) conducting ninety (90) interviews of CA's current and former directors, officers, employees, and outside advisors; (ii) reviewing millions of pages of documents; and (iii) hiring four (4) expert consultants, in order to determine whether pursuit of any or all of the claims alleged in the 2005 Derivative Action would be in the best interests of the Company. The SLC hired the law firm of Fried, Frank, Harris, Shriver & Jacobson LLP ("Fried Frank") to assist it with respect to all facets of its investigation, except for analyzing claims alleged against KPMG and Ernst & Young ("E&Y"), the Company's current and former outside auditors, respectively. The SLC hired the law firm of Cohen & Gresser LLP to investigate the claims alleged against KPMG and E&Y, and Fried Frank did not participate in that aspect of the investigation.

The SLC reviewed the underlying merits of each claim with counsel, and considered myriad factors, including the factual and legal validity of the claims, the likelihood

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1 On October 31, 2006, the CA Board charged the SLC to investigate, and to determine and control the Company's response to another derivative suit filed in the Delaware Court of Chancery on September 13, 2006, which alleges claims that are virtually identical to those alleged in the 2005 Derivative Action (the "Delaware Derivative Action"). This report also addresses the claims alleged in the Delaware Derivative Action.

of recovery of damages if those claims were successful, potential costs to the Company in legal fees, advancement and indemnity costs, and possible interference with the Company's on-going operations by diverting management time and focus, should it determine to go forward with any given claim. During its investigation, the SLC received the cooperation of the Company, the Company's current and former outside counsel, and all of the individual defendants named in the 2005 Derivative Action and the Delaware Derivative Action, except for defendant Charles Wang, the Company's co-founder and former Chairman and Chief Executive Officer ("CEO"), who refused to be interviewed by the SLC.[2] Defendant E&Y, the Company's former outside auditor, likewise would not cooperate with the SLC's investigation. The SLC does not believe that the refusal of these two defendants to cooperate materially impeded its ability to perform its mandate or to reach its conclusions.

The SLC benefited substantially from not having to start from scratch its investigation of the 35-Day Month fraud. Rather, many of the facts underlying the 2005 Derivative Action had already been established through the government investigation into CA's accounting practices, which resulted in the above-noted guilty pleas and the Company entering into the DPA. Likewise, the SLC has been able to utilize, where it concluded that the information was reliable, the investigative materials generated by CA's Audit Committee, which, on behalf of the CA Board and with the assistance of outside counsel, began an independent investigation into CA's accounting practices in July 2003.

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2 Sanjay Kumar, CA's former Chairman, CEO, and President, and Stephen Richards, CA's former head of North American and worldwide sales, each agreed to cooperate with the SLC only after they were sentenced by U.S. District Judge I. Leo Glasser in connection with their criminal cases, which occurred on October 30 and November 2, 2006, respectively. The SLC believes that their cooperation, which began in late December (Richards) and late January (Kumar), and had the effect of delaying the issuance of this report, was substantial and materially aided the SLC's investigation.

Given that the facts underlying the 35-Day Month practice at CA had already been established and are undisputed, the focus of the SLC's investigation was to determine the role and relative culpability, if any, of each of the defendants named in the 2005 Derivative Action in the accounting fraud and subsequent cover-up, including whether members of CA's Board failed to exercise appropriate oversight at various points in time. At the same time, the SLC sought to understand the underlying systemic corporate failures that caused, and allowed, the fraud to occur and to continue for as long as it did. Because the fraud was orchestrated by the most senior members of CA management, with the participation and acquiescence of countless more junior CA employees, the SLC believes that it is both instructive and vital to understand, and where possible to explain, the causes for that management failure.[3]

C. *The SLC's Findings With Respect to CA's Systemic Corporate Failure*

(a) *Failure of CA's Leadership*

First and foremost, CA suffered from a profound failure of leadership. In many ways, CA never outgrew the start-up mentality that characterized its inception in 1976, but was incompatible with a publicly-traded, multi-billion dollar, international software enterprise. CA's two primary managers and leaders throughout its existence – Charles Wang, CA's co-founder, and Sanjay Kumar, his successor and protégé – were the dominant and guiding forces behind its culture, a culture created by Mr. Wang and perpetuated by Mr. Kumar. Under their leadership, CA grew rapidly by acquiring approximately eighty-five (85) companies in the 1980s and 1990s. However, this rapid growth was not accompanied by similar growth and maturity in CA's management practices, as the Company continued to operate in a manner

[3] The role and relative culpability of E&Y and KPMG is the subject of a separate report by the SLC and will not be addressed in this report.

consistent with that of a small start-up company, lacking appropriate control processes and procedures at the management level.

Here is where CA's leaders, in particular, Mr. Wang, who was CEO for the vast majority of the period when the 35-Day Month occurred at CA, failed the Company. Mr. Wang shunned written policies and procedures in the apparent belief that they fostered bureaucracy and inefficiency. He avoided and discouraged group meetings, rarely, if ever, gathering even his most senior executives together in an organized way to discuss business. He reserved decision-making to a very limited group of executives that he controlled and dominated. As one witness aptly explained to the SLC, Mr. Wang ran CA as if he were "running it out of his garage." While the SLC recognizes that excessive controls and procedures may contribute to bureaucracy and inefficiency, CA fell far short of approaching what was necessary to control a Fortune 500 company.

Mr. Wang caused additional harm to CA by creating a "culture of fear," which caused CA employees, at all levels, to refrain from offering dissenting opinions. He did this by making personnel decisions in an arbitrary manner, routinely firing CA personnel on a subjective basis. This had the effect of suppressing corporate dialogue, by both lower and mid-level employees, as well as in the highest ranks of senior management. According to one witness, CA employees felt as if they were constantly "hanging on by their fingernails." In the SLC's view, this culture was the breeding ground in which the 35-Day Month practice originated and later flourished. This atmosphere proved particularly toxic at CA, since, under Mr. Wang, missing Wall Street estimates was to be avoided at all costs.

This problem was exacerbated by Mr. Wang's preference for promoting from within, rather than looking outside the Company for experienced candidates to fill CA's executive suite. As a result, Mr. Wang surrounded himself with young executives of limited experience – including CA's Chief Financial Officer ("CFO"), and the heads of Financial Reporting and Sales Accounting – whom he and Mr. Kumar could easily dominate. Thus, while it appeared by reviewing titles and an organizational chart that CA had the typical group of senior financial executives, in reality, CA's senior management was often too young, too inexperienced, and too dependent on CA's senior leaders to make meaningful judgments and to provide a credible alternative voice or dissenting opinion.

Mr. Kumar perpetuated Mr. Wang's practices as President and COO while he served under Mr. Wang. Mr. Kumar was universally described as a micromanager, intimately involved in every aspect of CA's business. Mr. Kumar acted as Mr. Wang's right hand, providing Mr. Wang with critical information about CA's business (indeed, the SLC identified few, if any, people other than Mr. Kumar who had regular personal contact with Mr. Wang) and effectuating the decisions made by Mr. Wang. After he became CEO in August 2000, Mr. Kumar continued to operate as a micro-manager and maintained the (inexperienced) executive suite put in place by Mr. Wang, which he continued to dominate and control directly.

(b) *Organizational Weaknesses*

As a result of this culture and the "tone at the top," the SLC found that CA had several organizational weaknesses that left the Company vulnerable in many respects.

Reporting Structure. CA suffered from a substantial failure to communicate, both within and across departments. During the period in which the fraud occurred, the Company employed a horizontal organizational structure that discouraged open communication among employees of different departments and limited access to important company information, as well as power and control, to a select and small group of senior executives. As such, CA was devoid of the mid-level managers normally found in other companies of similar size, and the senior managers to whom they reported retained decision-making authority for an unusually large array of issues. The SLC repeatedly heard that there was no such thing as a meeting at CA and that decisions were made quickly and without proper consideration and analysis. This allowed the proverbial "buck" to stop with very few people in a large organization.

Processes and Procedures. Given the lack of leadership on this issue by Mr. Wang, processes and procedures were not viewed as a priority at CA. Despite the fact that it was (and is) one of the largest software companies in the world, CA employed what was essentially a homegrown hodge-podge of accounting and financial reporting systems. CA's processes required far too much manual intervention for a company of CA's size. For example, the SLC found that, at the quarter end, CA's CFO manually reviewed contracts for revenue recognition issues and then created handwritten lists of contracts to be booked. This lack of clear processes and procedures allowed for manipulation and was one factor that permitted the deception to go unnoticed for many years.

Training and Education. CA's lack of training, coupled with an absence of written policies and procedures, created a work force, from top to bottom, that was unable to recognize the wrongfulness of its own conduct and, at its core, to look out for the best interests of the Company and its shareholders. An egregious example of this failure is that CA did not have a written set of revenue recognition policies and procedures, which left employees to learn from word-of-mouth and by e-mail what was "appropriate" accounting policy and practice.

Further, as noted above, CA historically promoted from within, creating senior management ranks largely trained by CA and in the CA "way." While this is not definitionally a negative, in CA's case, it ensured that management was dominated by individuals who embraced the "CA way" of doing things (i.e., one that did not emphasize proper policies, procedures, or controls) and lacked outside perspective. The SLC believes that a prime example of this phenomenon is the promotion of Ira Zar to the position of CFO in June of 1998. Mr. Zar came to CA straight out of college, and was only thirty-six (36) years old when he was appointed CFO at the recommendation of Mr. Wang, and with the support of Mr. Kumar. Mr. Zar had worked under senior CA managers for his entire career, had no independent experience in the software industry or otherwise, and was not a certified public accountant ("CPA"). Because of this, and while universally regarded as smart and sophisticated, Mr. Zar lacked the stature and experience to recognize, and prevent, the serious ramifications of the 35-Day Month practice. Indeed, the SLC found that CA's executive suite was populated by individuals who lacked industry and business experience and savvy and were too willing to put "job security" (and the benefits that accompanied a senior leadership position) above doing what they knew was right.

Internal Finance and Audit Controls. As noted above, CA's controls did not grow at the same rate as the organization, and, as a result, there were severe weaknesses in its systems. For example, the head of the Internal Audit department until January 2000, who was not a CPA and headed three (3) other divisions at CA at the same time, remained in this capacity and with these responsibilities throughout this period of growth. Further, in 2001, by which time CA was a Fortune 500 company, its Internal Audit department consisted of only five (5) full and part time employees. Because it had limited capabilities, Internal Audit generally performed only international and non-critical domestic work.

Indeed, in keeping with CA's tradition of promoting from within, both executives who headed Internal Audit during the period of fraudulent conduct were promoted from other departments at CA, and neither had prior experience with the internal audit function. Not surprisingly, during the period of the fraud, no one viewed Internal Audit with respect. In fact, some current and former CA employees were surprised to learn, when being interviewed by the SLC during 2006, that CA even had an Internal Audit department in the past. The failure to have a functioning Internal Audit department with the size and sophistication to match the Company's growth contributed to allowing the Finance and Sales departments to openly engage in the conduct that they used to perpetrate the fraud at CA.

In the end, the fraud at CA was directed by a group of CA's most senior managers who acted intentionally to violate the accounting rules and then covered it up. However, the fraud pervaded the entire CA organization at every level, and was embedded in CA's culture, as instilled by Mr. Wang, almost from the Company's inception. Indeed, the improper practices became CA's standard practices to the point that the fraud was "hidden in plain sight" and became part of CA's normal day-to-day business. CA's failure to have an organizational structure, policies, and practices consistent with that of a multi-billion dollar market-cap, publicly-traded company contributed substantially to promoting an environment which allowed the fraud to begin and to continue at the levels it did for as long as it did.

With this description of CA's culture as a prologue, this report now turns to a summary and analysis of the claims alleged in the 2005 Derivative Action.

D. *The SLC's Conclusions with Respect to the Claims in the 2005 Derivative Complaint*

The SLC has categorized the claims made in the 2005 Derivative Action into six (6) different groups of defendants (some of which overlap against certain defendants). A brief summary of each of the categories, and the SLC's conclusion with respect to each group, is as follows:

- ***The Criminal Defendants.*** The seven (7) former CA officers and employees who have pled guilty to various charges of securities fraud and/or obstruction of justice – Mr. Kumar, Mr. Richards, Mr. Zar, Steven Woghin (CA's former General Counsel), David Kaplan (CA's former head of Financial Reporting), David Rivard (CA's former head of Sales Accounting), and Lloyd Silverstein (CA's former head of the Global Sales Organization). (For ease of reference, throughout this report, these defendants will be referred to collectively as the "Criminal Defendants").[4] The 2005 Derivative Action alleges that the Criminal Defendants are liable to CA for breaches of fiduciary duty, corporate waste, common law fraud, violation of § 14(a) of the Securities Exchange Act of 1934 (the "Exchange Act"), common law and statutory contribution, and unjust enrichment as a result of their criminal conduct.

  The SLC has concluded that it is in the best interests of the Company to pursue claims arising from this conduct against the Criminal Defendants to the fullest extent possible, bounded only by their assets and the cost of recovery. The SLC has reached a settlement with Mr. Kumar, pursuant to which the Company will receive a $15.25 million judgment against Mr. Kumar secured in part by real property and executable against his future earnings, and, as a result, it will seek dismissal of all claims against him.[5] *The SLC anticipates reaching settlements with the remaining Criminal Defendants shortly after the conclusion of their criminal restitution proceedings. To the extent that settlements are not reached, the SLC will direct the Company to vigorously pursue these claims.*

- ***The Former Officer Defendants.*** The three (3) former CA officers who have not been criminally prosecuted, but who are nonetheless alleged to have been actively involved in, or responsible for, the 35-Day Month practice – Peter Schwartz (CA's former CFO,

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4 This group does not include Thomas Bennett, CA's former Senior Vice President of Business Development (2000-2004), who is the eighth CA executive to have pled guilty to federal criminal charges, as he is not named as a defendant in the 2005 Derivative Action or the Delaware Derivative Action.

5 The SLC's settlement with Mr. Kumar follows an agreement Mr. Kumar reached with the USAO concerning his criminal restitution (the "Restitution Order"). The Restitution Order, which was jointly submitted by the USAO and Mr. Kumar to the Honorable I. Leo Glasser for approval on March 30, 2007 (04-CR-00846 (ILG) Docket No. 332-2), provides for (a) the entry of a judgment in the amount of $798,600,000 against Mr. Kumar, (b) the payment of $50 million by Mr. Kumar into a fund to be distributed by the Feinberg Group (the "Feinberg Fund") on or before July 31, 2007 for the benefit of CA's shareholders, (c) the payment of $2 million by Mr. Kumar to the United States, on or before December 31, 2008, to be distributed to the victims of Mr. Kumar's criminal offenses, and (d) post-incarceration payments by Mr. Kumar in annual payments equal to twenty percent (20%) of "total income" as defined by the IRS on Form 1040, with certain modifications. Based on his sworn financial disclosures, the SLC believes that, following his agreement with the USAO, Mr. Kumar had no material assets remaining.

1985-1998), Charles McWade (CA's former head of Financial Reporting, 1994-1997, and business development, 1997-2001), and Michael McElroy (CA's former senior vice president of Legal, 1988-2004). (For ease of reference, throughout this report, these defendants will be referred to collectively as the "Former Officer Defendants"). The 2005 Derivative Action alleges that the Former Officer Defendants are liable to CA for breaches of fiduciary duty, corporate waste, common law fraud, violations of § 14(a) of the Exchange Act, common law and statutory contribution, and unjust enrichment as a result of their alleged knowledge of, and participation in, the 35-Day Month practice.

The SLC has concluded that it is in the best interests of the Company to pursue claims against Mr. Schwartz as it has determined that he knew of, and participated in, the 35-Day Month practice, and has directed the Company to vigorously pursue this claim (including filing all necessary Rule 60(b) motions) and to regularly report to the CA Board regarding the status of the litigation. The SLC has reached a settlement with Mr. McWade, pursuant to which the Company will receive $1 million from Mr. McWade and, as a result, it will seek dismissal of all claims against him. After weighing various factors in the exercise of its business judgment, such as, among other things, the cost of litigation and Mr. McElroy's inability to satisfy a meaningful judgment, the SLC has determined to seek dismissal of the claims with respect to Mr. McElroy.

- ***The KESOP Defendants.*** The three (3) beneficiaries of CA's 1995 Key Employee Stock Ownership Plan (the "KESOP") – Charles Wang, Sanjay Kumar, and Russell Artzt – pursuant to which they received an award of 20.25 million shares of CA common stock, then valued at $1.1 billion, on May 21, 1998. (For ease of reference, throughout this report, these defendants will be referred to collectively as the "KESOP Defendants"). The 2005 Derivative Action alleges that the KESOP Defendants were unjustly enriched at the expense of CA's shareholders by their receipt of the KESOP shares as a result of the fraud perpetrated at the Company.

  The SLC has concluded that it is in the best interests of the Company to pursue this claim against Mr. Wang as it has concluded that he knew of, directed, and participated in, the 35-Day Month practice, and has directed the Company to vigorously pursue this claim (including filing all necessary Rule 60(b) motions) and to regularly report to the CA Board regarding the status of the litigation. The SLC has reached a settlement with Mr. Artzt, pursuant to which the Company will receive $9 million from Mr. Artzt (the cash equivalent of approximately 354,890 KESOP shares) and, as a result, it will seek dismissal of all claims against him. The SLC notes that during its investigation, it did not uncover evidence that Mr. Artzt directed or participated in the 35 Day-Month practice or was involved in the preparation or dissemination of the financial statements that led to the KESOP's accelerated vesting. As noted above, the SLC has reached a settlement with Mr. Kumar, pursuant to which it will seek dismissal of all claims against him.

- ***The Oversight Director Defendants.*** The one (1) current and seven (7) former CA Board members who served on the CA Board during the period of the fraudulent conduct – Russell Artzt (1981-2005), Alfonse D'Amato (1999 – present), Willem de

Vogel (1981-1990, 1991-2002), Richard Grasso (1994-2002), Shirley Strum Kenny (1994-2002),[6] Sanjay Kumar (1994-2004), Roel Pieper (1999-2002), and Charles Wang (1981-2003). (For ease of reference, throughout this report, these defendants will be referred to collectively as the "Oversight Director Defendants"). The 2005 Derivative Action alleges that the Oversight Director Defendants are liable to CA for breaches of fiduciary duty, corporate waste, common law fraud, violations of § 14(a) of the Exchange Act, and common law and statutory contribution as a result of their alleged failure to properly oversee the Company during the period of fraudulent conduct, and that the management directors (Messrs. Wang, Kumar, and Artzt) are liable to CA for their role in the fraud.

The SLC has concluded that it is in the best interests of the Company to pursue claims arising from this conduct against Mr. Wang in the manner described above. As noted above, the SLC has reached settlements with Messrs. Artzt and Kumar, pursuant to which it will seek dismissal of all claims against them. The SLC will seek dismissal of these claims with respect to the remaining directors since the SLC believes that these claims lack merit.

- ***The Settlement Director Defendants.*** The seven (7) current and one (1) former CA Board members who served on the CA Board during the USAO investigation and who authorized the Company to enter into a settlement of certain class action and derivative litigation in August of 2003 and later the DPA – Kenneth Cron (2002-2006), Alfonse D'Amato, Gary Fernandes (2003 – present), Robert La Blanc (2002 – present), Jay Lorsch (2002 – present), Lewis Ranieri (2001 – present), Walter Schuetze (2001 – present), and Alex Vieux (2002-2004)[7] (For ease of reference, throughout this report, these defendants will be referred to collectively as the "Settlement Director Defendants"). The 2005 Derivative Action alleges that the Settlement Director Defendants are liable to CA for breaches of fiduciary duty, corporate waste, violations of § 14(a) of the Exchange Act, and common law and statutory contribution because they authorized the above-described settlement and entered into the DPA, both without seeking contribution from the Criminal Defendants. The Settlement Director Defendants, in addition to Messrs. Wang and Artzt, are also alleged in the Kaufman Complaint to have breached their fiduciary duties by failing to properly oversee the Company during the government investigation.

  The SLC has concluded that it is in the best interests of the Company to seek dismissal of the settlement and DPA-related claims in their entirety since the SLC believes that these claims lack merit, except that it will pursue this claim against Mr. Wang in the manner described above. The SLC has reached a settlement with Mr. Artzt, pursuant to which it will seek dismissal of all claims against him.

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6 Dr. Kenny is not named as a defendant in the 2005 Derivative Action, but is named as a defendant in the Delaware Derivative Action.

7 Mr. Vieux is not named as a defendant in the 2005 Derivative Action, but is named as a defendant in the Delaware Derivative Action.

- ***The Auditor Defendants.*** The Company's current and former outside auditors, KPMG and E&Y, respectively. As noted above, the claims alleged against these defendants are analyzed in a separate SLC report.

The following constitutes an executive summary of the findings of the SLC with respect to each of the above-described groups of defendants. The details and facts underlying these conclusions are set forth at length later in this report.[8]

The Criminal Defendants. The Criminal Defendants have each admitted, in connection with their guilty pleas and to the SLC, that they participated in and facilitated the 35-Day Month practice and then conspired to conceal the practice from CA's Board and the USAO. By way of example, Sanjay Kumar, Stephen Richards, and Ira Zar have each admitted that they regularly and improperly held CA's books open at the ends of CA's fiscal quarters in order to ensure that CA generated enough revenue to meet Wall Street analyst estimates, often at the direct instruction of Mr. Wang. Steven Woghin, David Kaplan, David Rivard, and Lloyd Silverstein (along with Messrs. Kumar and Richards) have each admitted that they negotiated, executed, and/or improperly accounted for license agreements that were completed in the days immediately following the quarter end. These individuals also encouraged CA employees under their supervision to take actions in furtherance of the 35-Day Month practice. During the government investigation into CA's accounting practices, these CA senior executives – which included the Company's CEO, CFO, and General Counsel – lied to the Board about the existence of the 35-Day Month practice and otherwise deceived the government and the Audit Committee. This conduct is undisputed and, to date, the Company has suffered and continues to suffer, substantial harm as a result of their conduct.

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8 Where the SLC has determined that it has valid and viable claims that it intends to pursue, it has not detailed in this report all of the facts that it has uncovered during the course of its investigation.

During the years in which the Criminal Defendants openly engaged in fraud, CA paid them hundreds of millions of dollars in undeserved compensation (mostly to Mr. Kumar). To date, CA has been required, under Delaware law, to advance the Criminal Defendants, in total, in excess of $25 million in legal fees in connection with their criminal prosecutions. Further, as a direct result of their conduct, the Company was required to pay: (i) $225,000,000 in restitution to CA's shareholders and $1,916,259 for the restitution fund administrator's fees pursuant to the DPA; (ii) over $3,200,000 for Independent Examiner's fees pursuant to the DPA; (iii) $174,000,000 to CA shareholders in the settlement of certain civil litigation; and (iv) at least $80,000,000 in investigative fees and costs. These out-of-pocket costs alone total nearly $500,000,000. The harm that these former senior CA executives have caused goes beyond the monetary, as CA still must grapple with the legacy of their criminal conduct and its effect on CA's core constituents, including its employees, customers, shareholders, and suppliers.

The SLC has concluded that the claims against the Criminal Defendants clearly have merit and should be pursued. The SLC believes that the Criminal Defendants should be compelled to return the compensation they were paid but did not earn and to reimburse CA for the substantial costs it has incurred as a direct result of their conduct. To that end, as described further below, but limited by the fact that many of the Criminal Defendants do not have significant assets and those assets that do exist are subject to restitution orders sought and obtained by the USAO in connection with their criminal sentences, the SLC has already begun to discuss settlement with, and to pursue recovery from, the Criminal Defendants.

To date, and as noted above, the SLC has reached a settlement with Mr. Kumar, pursuant to which the Company will receive a judgment in the amount of $15,250,000 secured in part by real property and executable against his future earnings. This amount is in addition to the $52 million that Mr. Kumar will repay to CA's shareholders as part of his criminal restitution proceedings. As a result, the SLC will seek dismissal of all claims against Mr. Kumar.

The Former Officer Defendants. As to the Former Officer Defendants – Peter Schwartz, Charles McWade, and Michael McElroy – the results of the SLC's investigation were varied.

Peter Schwartz. Mr. Schwartz was CA's CFO from 1985 to June 1998 and is alleged in the 2005 Derivative Action to have been "the primary architect of the scheme to pump up CA's revenues from $58 million in 1994 to $5 billion in 1998," by "directing" the 35-Day Month practice. 2005 Compl. ¶ 162. However, the 2005 Derivative Complaint alleges no specific acts of fraudulent conduct attributed to Mr. Schwartz or specific facts related to how he "directed" the practice. Two divergent accounts of Mr. Schwartz's involvement in the 35-Day Month practice emerged during the SLC's investigation. In his interview with the SLC, Mr. Schwartz emphatically denied that the 35-Day Month practice occurred during his tenure as CFO, while others, including certain of the Criminal Defendants interviewed by the SLC, credibly insisted that Mr. Schwartz not only knew about the practice, but that he was one of its originators. Indeed, certain of the Criminal Defendants described specific conversations they had with Mr. Schwartz evidencing his knowledge and approval of the practice.

In addition, there is one fact that is certain. PricewaterhouseCoopers ("PwC"), which was retained by the SLC to examine certain of CA's financial reporting periods, concluded that CA prematurely recognized revenue on backdated contracts during at least the first quarter of CA's fiscal year 1998 (April 1, 1997 – June 30, 1997) through the first quarter of fiscal year 1999 (April 1, 1998 – June 30, 1998), the last quarter Mr. Schwartz served as CFO. The SLC also found that the 35-Day Month practice existed, and was in fact the standard operating procedure at CA, during much of Mr. Schwartz's tenure as CFO. Given that Mr. Schwartz was known for his intimate involvement in the minute details of CA's business (as he was, by his own account, the "first to arrive" and "last to leave"), it is, in the SLC's view, not credible that the practice could have continued and flourished without his knowledge. As such, the SLC rejected Mr. Schwartz's protestations of ignorance concerning the 35-Day Month practice, in the face of contrary witness testimony, and found his position not to be credible.

Moreover, as CA's long-time CFO, Mr. Schwartz was responsible for the accounting processes and procedures (or lack thereof) that allowed the 35-Day Month practice to flourish. In fact, the SLC finds it incredible that the CFO of a to-be Fortune 500 Company could be ignorant of a revenue recognition fraud when it is his responsibility to ensure the integrity of CA's financial operations. Accordingly, the SLC has concluded that it is in the best interests of the Company to pursue claims against Mr. Schwartz for the full amount of the enormous harm caused to CA.

Charles McWade. Mr. McWade held various senior positions at CA such as head of Sales Accounting (1983-1994), head of Financial Reporting (1994-1997), and vice president of Business Development (1998-2001). Mr. McWade is alleged to have participated in, and been one of the originators of, the 35-Day Month practice with Mr. Schwartz, to whom he reported directly. The 2005 Derivative Action alleges that Mr. McWade, "supervised the development, negotiation and sale of software licensing agreements for which revenue was . . . prematurely recognized and he encouraged, directed, or consented to other CA employees doing the same." 2005 Compl. ¶ 165. However, the 2005 Derivative Complaint alleges no acts of specific fraudulent conduct attributed to Mr. McWade or facts related to how he "supervised" the practice.

As noted above, the SLC has reached a settlement with Mr. McWade pursuant to which the Company will receive $1 million and, as a result, will seek dismissal of all claims against him.

Michael McElroy. Mr. McElroy, a CA licensing lawyer who worked at the Company from 1988 to 2004, is alleged to have participated in the 35-Day Month by drafting, negotiating, and executing licensing agreements after the quarter end that were backdated to the prior quarter and "encourag[ing] and instruct[ing] other CA employees to do the same." 2005 Compl. ¶ 165. In contrast to Mr. Schwartz, Mr. McElroy was more forthcoming with the SLC regarding his involvement in the 35-Day Month practice.

Mr. McElroy admitted to the SLC, and the documentary record establishes, that he participated in the negotiation and finalization of contracts after the quarter end. Indeed, those in the Legal Department, including Mr. McElroy, openly joked about the 35-Day Month practice, often remarking that it was the "32nd" or "33rd" of the month. Mr. McElroy eventually came to learn that CA was recognizing revenue from those contracts in the prior quarter, but nonetheless claimed that he did not understand that this was wrong from an accounting perspective. He assumed, but took no steps to confirm, that the Finance department was properly determining when it was appropriate to book revenue.

To the SLC, Mr. McElroy exemplified the "see no evil, hear no evil" approach taken in the Legal department, led by Mr. Woghin, with respect to post-quarter contracting activity. Instead of acting as a gatekeeper to protect CA, Mr. McElroy, and others in the Legal department, blindly hoped that CA's finance and accounting personnel ensured that CA was in compliance with applicable accounting standards, but did nothing to verify that this was so in the face of contrary evidence. The SLC has concluded that, while the Company has potentially valid claims against Mr. McElroy, it has, in the exercise of its business judgment, and balancing the various factors, including Mr. McElroy's financial status, the cost of pursuing claims against him, and the litigation risk of establishing that he acted with the requisite scienter or played a role in revenue recognition, concluded that it is in the best interests of the Company to seek dismissal of the claims asserted against him.

The KESOP Defendants. As a result of the 35-Day Month practice, Messrs. Wang, Kumar, and Artzt received, on an accelerated basis, a massive stock award that they neither deserved nor earned. At the time, the KESOP award – in excess of $1.1 billion – was *one of the largest single payout to corporate officers by a public company ever*.[9] Pursuant to the terms of the KESOP, when the Company's stock price traded above $53.33 (adjusted to reflect three separate three-for-two stock splits) for sixty (60) days in a twelve (12) month period, as it did on May 21, 1998, 18,900,000 shares of CA common stock granted to the KESOP Defendants vested on an accelerated basis and were no longer subject to forfeiture.[10]

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9 Louise Kehoe and William Lewis, *Computer Associates Chief May Get $550m Bonus*, Financial Times, May 21, 1998 ("The stock option bonus, said by pay experts to be one of the largest of its kind in the U.S., is to be split three ways"); Gary Silverman, *Execs Pay Worth a Whole Lot of Burgers*, Newsday, May 22, 1998, at A73 ("'The size of the grant is without parallel,' said Graef Crystal, an executive-compensation expert in San Diego. 'It's like if someone pole vaulted 70 feet'").

10 As a result of the May 21, 1998 accelerated vesting, Charles Wang received 11,340,000 CA shares; Sanjay Kumar received 5,670,000 CA shares; and Russell Artzt received 1,890,000 CA shares. Following the accelerated vesting, and as is described at length below, shareholders filed derivative lawsuits in the Delaware Court of Chancery and the U.S. District Court for the Eastern District of New York alleging that CA's Compensation Committee improperly adjusted the KESOP award for stock splits, and therefore, the KESOP Defendants received 9.5 million shares in excess of what the plan allowed. In December 2000, pursuant to a settlement of the derivative litigation in Delaware, Messrs. Wang, Kumar, and Artzt returned 4.5 million of the 18.9 million KESOP shares that vested on May 21, 1998. Charles Wang returned 2,700,000 shares; Sanjay Kumar returned 1,350,000 shares; and Russell Artzt returned 450,000 shares. In exchange for the return of the shares, the Messrs. Wang, Kumar, and Artzt received a release from the Company for all claims related to the KESOP shares. The three

Since the accelerated vesting, the Company has publicly acknowledged, and the SLC has confirmed, that CA's earnings for the third and fourth quarters of fiscal year 1998 (September 1997 – March 1998) and the first quarter of fiscal year 1999 (April – June 1998), the three quarters in which CA's shares traded above the levels required to trigger the KESOP vesting, were materially overstated due to CA's fraudulent revenue recognition practices. Given that CA's stock price was materially and fraudulently inflated during the period it traded above the level required for the accelerated vesting, and the KESOP would not actually have vested in the absence of fraud, the SLC has concluded that Messrs. Kumar, Wang and Artzt were unjustly enriched by their receipt of the KESOP shares under Delaware law, which defines unjust enrichment as "the unjust retention of a benefit to the loss of another . . . against the fundamental principles of equity and justice." *Schock v. Nash*, 732 A.2d 217, 232 (Del. 1999). The Company is entitled to restitution, and to the return of the improperly awarded KESOP shares, "even when the defendant retaining the benefit is not the wrongdoer." *In re HealthSouth Corp. S'holders Litig.,* 845 A.2d 1096, 1105 (Del. Ch. 2003), *aff'd,* 847 A.2d 1121 (Del. 2004).

Here, the recipients of the KESOP undoubtedly received a substantial benefit to the detriment of the Company and its shareholders that in good conscience they should not be allowed to keep. This is particularly true with respect to Messrs. Wang and Kumar, since they originated and directed the 35-Day Month practice and were ultimately responsible for CA's financial statements. As noted above, the SLC has directed the Company to pursue claims against Mr. Wang on a variety of theories, including unjust enrichment with respect to his

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executives also received 1,350,000 KESOP shares that vested on January 11, 1996, and that, as result of the accelerated vesting, were no longer subject to forfeiture.

receipt of the KESOP shares. As also noted above, the SLC has reached settlements with Messrs. Artzt and Kumar, pursuant to which it will seek dismissal of all claims against them.

The Oversight Director Defendants. Messrs. Wang, Kumar, and Artzt, along with the non-management Oversight Director Defendants – Alfonse D'Amato, Willem de Vogel, Richard Grasso, Shirley Strum Kenny, and Roel Pieper – are also alleged to have breached their fiduciary duties by participating in and by failing to take steps to prevent and uncover the 35-Day Month practice. However, the 2005 Derivative Complaint fails to articulate any facts as to how the non-management Oversight Director Defendants knew or should have known of the fraud, but rather alleges that, "the duration and magnitude of the fraud at CA demonstrates a pervasive failure of oversight," and that "[i]t is impossible to imagine how this fraud could have been perpetrated under the very noses of CA's purportedly sophisticated Directors absent a complete failure of oversight or their knowing participation." 2005 Compl. ¶¶ 215-16.

Because the 2005 Derivative Complaint provided no areas of inquiry to pursue to determine whether a failure of oversight occurred, the SLC first identified, and then investigated two primary theories of potential culpability under Delaware law. Under Delaware law, a failure of oversight occurs when "either (1) the directors knew, or (2) should have known that violations of the law were occurring *and*, in either event, (3) that the directors took no steps in a good faith effort to prevent or remedy that situation, *and* (4) that such failure proximately resulted in the losses complained of." *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, 971 (Del. Ch. 1996) (emphasis added).

This test can be satisfied by showing either that (i) "the directors utterly failed to implement *any* reporting or information systems or controls," or "having implemented such a system or controls, *consciously* failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention," *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006) (emphasis added); or (ii) that the directors "had notice of serious misconduct and simply failed to investigate," i.e. intentionally ignored "red flags," *David B. Shaev Profit Sharing Account v. Armstrong*, 2006 WL 391931, at *5 (Del. Ch. Feb. 13, 2006). A violation of the duty of oversight constitutes a breach of the duty of loyalty, and as such, a plaintiff must prove intentional bad faith conduct on the part of the directors. *See id.* It is worth noting that the Delaware courts have consistently observed that this claim is one of, if not the most, difficult theories under which to establish liability.

With this framework in mind, the SLC investigated (i) the adequacy of the reporting systems and controls in place at the Company during the period of fraudulent conduct, and (ii) potential "red flags" that could have alerted the directors to the 35-Day Month practice, but were ignored.

First, the SLC examined the information and reporting systems in place during the period of fraudulent conduct, and found that the Board had legally adequate reporting systems in place at the time. For example, at all times relevant to the 2005 Derivative Action, CA had a duly constituted Audit Committee. CA's Audit Committee retained "big four" accounting firms – E&Y, and later KPMG – as its independent, outside accountant to audit CA's consolidated financial statements and to review CA's internal accounting controls worldwide. The Audit Committee met periodically throughout each fiscal year, and on each occasion met with CA's outside auditors without management present. The Audit Committee also met regularly with representatives from CA's internal audit department without management present.

The SLC also examined the specific information the Board received regarding the accounting systems and controls in place during the period of fraudulent conduct. By all accounts, and as discussed above, CA lacked the accounting controls needed by a company of its size and caliber. This was first reported to the Audit Committee in KPMG's management letter for fiscal year 2000. This report in no way suggested that CA's internal controls were materially deficient or that a revenue recognition fraud was occurring; rather KPMG characterized the Company's accounting systems as being "less integrated" and requiring "more manual intervention than is typical" for a company of similar size. The Audit Committee was told that CA's management was working to address this issue. Thus, based on its receipt of information such as this, the SLC believes that the Board was receiving relevant and legally sufficient information regarding CA's accounting systems.

Further, the SLC found that, based on the information that the Board received, the directors had no reason to believe that CA's accounting systems were deficient, and did not consciously fail to monitor the Company's operations. At the conclusion of each fiscal year, CA's outside auditors issued a "clean" or "unqualified" audit opinion, and their management letters did not reflect *any* matters that they considered to be material weaknesses.[11] At no time did E&Y, KPMG, or CA's Internal Audit department ever tell the CA Board that CA's accounting systems and controls were inadequate, let alone that a revenue recognition fraud was occurring. As such, the SLC concludes that the non-management Oversight Director

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11 An "unqualified opinion" is defined as an "independent auditor's opinion that a Company's financial statements are fairly presented, in all material respects, in conformity with generally accepted accounting principles." John Downes & Jordan Elliot Goodman, *Dictionary of Finance and Investment Terms* 765 (6th ed. 2003). A material weakness is "a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected." Public Company Accounting Oversight Board Bylaws and Rules Standards – AS2.

Defendants satisfied their fiduciary duties under Delaware law by having legally sufficient information and reporting systems and controls in place during the relevant time period.

Second, as noted above, the 2005 Derivative Action is devoid of any "red flags" or events that were ignored and should have alerted the non-management Oversight Director Defendants (which excludes Messrs. Artzt, Kumar, and Wang) to the existence of the 35-Day Month practice.[12] However, as part of its investigation, the SLC independently sought to discover if any of these events existed and to examine the adequacy of the CA Board's responses to those events. During its investigation, the SLC discovered no evidence whatsoever that the non-management Oversight Director Defendants were ever made aware of the 35-Day Month practice. Rather, the SLC identified several potential "red flags" that, taken alone or together, might have put the Board on notice of potential misconduct. However, in the SLC's view, as discussed below, the potential "red flags" that it identified, once examined closely, either did not constitute "red flags" or were pursued by the non-management Oversight Director Defendants in a legally adequate manner.

At the outset, it is important to note that almost all of the Criminal Defendants whom the SLC interviewed that interacted with the CA Board acknowledged that they lied to the directors and/or CA's outside counsel and otherwise actively concealed the 35-Day Month practice. When asked pointedly, those Criminal Defendants explicitly stated that there was nothing the non-management Oversight Directors could have done to uncover the fraud given the information that they were provided. Indeed, certain of the Criminal Defendants indicated that, in all likelihood, they would have continued to lie to those directors had they attempted to

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[12] Under Delaware law, this pleading failure would have justified the SLC in seeking dismissal. *See Shaev*, 2006 WL 391931, at *1 (dismissing complaint where "new complaint alleges . . . literally nothing to suggest that the defendants willfully or recklessly ignored information that would have led to the discovery of the misconduct at issue").

dig deeper. This conduct continued even after the government investigation began, when certain of the Criminal Defendants did, in fact, lie directly to the Audit Committee and the Board as a whole. These admissions, made at a time when the Criminal Defendants had no incentive or reason to protect the CA Board, were a meaningful factor in the SLC's analysis of this claim.

The Vesting of the KESOP Shares and the Subsequent Stock Drop. The first potential "red flag" identified by the SLC that could have given rise to director concern was the vesting of the KESOP on May 21, 1998. As discussed above, the accelerated vesting of the KESOP, pursuant to which Messrs. Wang, Kumar, and Artzt received CA stock then-valued at $1.1 billion, was tied to the Company's stock price. However, as vesting became likely and imminent, the non-management Oversight Director Defendants took no additional, incremental steps whatsoever to ensure the accuracy of CA's financial statements, notwithstanding this immense accelerated transfer of shareholder wealth and the temptation to tamper with the Company's financial performance that it could create. Instead, the only step taken by any director was to ensure that the number of days CA's stock traded above the target price required for vesting was counted correctly.

Then, within sixty days of the vesting of the KESOP, on July 20, 1998, the CA Board held its regular quarterly meeting. At that meeting, the Board was informed that CA management expected the Company's growth to slow in the coming months. According to most of the participants, Mr. Kumar explained to the Board that he had recently met with CA's top sales executives from around the world and learned anecdotally that some of CA's multi-national customers were reducing their spending, and deferring purchasing decisions, due to the then-existing economic “crisis” in Asia.[13] As a result of the stated concerns (which were supported by Mr. Wang), the Board, led by director Richard Grasso, insisted that those concerns immediately be disclosed by the Company to the market. The next day, on July 21, 1998, CA issued a press release announcing its quarterly results, but also warning that CA’s growth would slow for the reason noted above (and others). On the following day, the price of CA’s stock dropped by thirty-one percent (31%).

The SLC was troubled by the timing of these events. Had CA management “learned” of this information sixty days earlier, and had it been promptly disclosed to the market (as the Board later advocated that it should), the KESOP would not have vested on May 21, 1998. However, despite its proximity to the vesting of the KESOP, the timing of when CA management learned of CA’s slowing growth resulting from the Asian economic crisis, or whether these problems actually existed, was never fully explored by the Board.

Finally, almost immediately following the July 21 press release and the resultant stock price drop, shareholders filed a series of class action lawsuits. The Board was advised, as early as August 1998, that the lawsuits claimed that CA’s senior officers knew the information disclosed in the July 21 press release at an earlier date, but did not disclose that information in order to allow the KESOP shares to vest. At the same time, however, Mr. Woghin, the Company’s General Counsel, told the Board that there was no substance to these lawsuits. Mr. Woghin reported to the Board that the suits contained no particularized factual allegations – and they did not in actuality – and merely alleged, in essence, that a fraud “must have occurred.”

These events, taken together, could have raised a specter that something was amiss at the Company. However, even if viewed most skeptically, these events would not have

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13 There is a factual dispute as to whether Mr. Kumar or Mr. Schwartz first raised this issue with the Board, but resolution of this issue is not material to the SLC’s conclusion.

constituted a "red flag" pointing to the 35-Day Month practice. Indeed, the potential issue raised by these events, namely, the timeliness of management's disclosure of material information – slowing growth resulting from the Asian economic crisis – does not relate to CA's revenue recognition practices, which was the ultimate problem.

In addition, there were numerous factors supporting the directors' conduct: (i) at the time the KESOP vested, CA's outside accountants were in the process of completing their audit for the fiscal year ending March 31, 1998, and did not recommend to the Audit Committee that it take any further action to verify the accuracy of CA's financials as a result of the imminent vesting; (ii) the non-management Oversight Defendant Directors, none of whom had any experience in the software industry, were entitled to rely upon CA management's statements (which were supported by Mr. Wang) regarding when they learned of CA's "slowing growth" in the absence of any contradictory information; and (iii) following the filing of the class action litigation, Mr. Woghin described the suits dismissively to the Board as typical strike suits with no factual substance. Under these circumstances, the SLC concludes that these events did not constitute a "red flag" indicating potential unlawful revenue recognition practices and the Board was not legally obligated to do more in response to these events.

The New Business Model. The second set of facts identified by the SLC as potential "red flags" began with CA's May 11, 2000 Board meeting, where Mr. Kumar proposed that CA adopt a "new business model." Under the new business model, CA would recognize revenue from licensing agreements, its primary source of revenue, on a ratable basis, as opposed to recognizing all of the revenue from a contract up front, as was its historical practice. The Board declined to approve a transition to the new business model initially, but instead concluded that management first needed to evaluate how the investing public would perceive and understand it, and report back to the Board with its findings. On October 24, 2000, after receiving the information that it had previously requested, CA's Board authorized management to implement the new business model.

While some members of the press questioned CA's motive for moving to a ratable revenue recognition model, suggesting that CA moved to the new model in order to mask declining performance, the press did not assert that it was designed to cover up a pre-existing scheme to improperly recognize revenue. With the benefit of hindsight, it can easily be surmised that one of the purposes animating management's desire to move to the new business model was to end the 35-Day Month practice. Indeed, several witnesses have told the SLC that the desire to end the 35-Day Month was, in fact, one of the reasons behind the switch (although this was denied by Mr. Kumar, the new business model's primary proponent). However, and critical here, there is absolutely no evidence that any outside director knew of the 35-Day Month practice, much less the impact the new business model would have on it.

Moreover, the SLC found that the decision to adopt the new business model was supported by several legitimate business reasons, and, at the time, was considered by many on the CA Board and outside the Company to be forward thinking, conservative, and a positive step for the Company. Further, the CA Board did not simply rubber-stamp the new business model at management's behest, but rather requested that management perform a significant amount of additional work and report back to it in order to allow the directors to make an educated decision. As such, the SLC concludes that the decision to adopt the new business model did not constitute a "red flag" and the known facts would not have led a reasonable director to suspect that the motivation for the new business model was to end a long-running fraud at the Company. The Board did not breach its duty of oversight by failing to investigate further at that time.

The New York Times Article. Finally, the SLC identified as a potential "red flag" an April 29, 2001 article by Alex Berenson of The New York Times, entitled "A Software Company Runs Out of Tricks; The Past May Haunt Computer Associates." Mr. Berenson's article, which was featured prominently in the Sunday edition of the paper, accused CA of using several "accounting tricks," including the 35-Day Month, to inflate its revenue and earnings, and remarked that CA stood for "creative accounting." Specifically, the article stated, in its fifth paragraph, that "[t]he practices were so widespread that employees joked that C.A. stood for 'Creative Accounting,' and that March, June, September and December, when fiscal quarters end, had 35 days, giving the company extra time to close sales and book revenue." However, notwithstanding this sentence, the 35-Day Month practice was not the focus of the article and received no mention beyond that quoted above. Rather, the article focused primarily on CA's new business model, its Unicenter software, and its method of accounting for maintenance and license revenue.

While it is unlikely that the New York Times article constituted a "red flag" under Delaware law (*see McCall v. Scott,* 239 F.3d 808, 819-20 (6th Cir. 2001) (press reports are a "red flag" only when "taken as a whole" with numerous other indicia of fraud)), the SLC nonetheless carefully examined the circumstances surrounding this newspaper story, including interviewing most of the key participants twice. In the end, the SLC, after substantial and extensive deliberations, found that the non-management Oversight Director Defendants took legally adequate steps to address the allegations made in the article.

Following the publication of the article, Dr. Kenny, Chair of the Audit Committee, was tasked by Mr. Kumar to investigate the merits of the allegations. On May 8, 2001, nine (9) days after the article was published, but on only one (1) day's notice, Dr. Kenny convened a meeting with CA's management and KPMG and E&Y to address the allegations in the article. Given the passage of time, the record is scarce as to exactly what was discussed at this meeting, which is reported to have lasted forty-five (45) minutes to an hour. Nonetheless, at the meeting, CA management, and Mr. Zar in particular, assured Dr. Kenny that CA had at all times used appropriate accounting practices. Likewise, and more importantly, Dr. Kenny sought and received assurances from both E&Y and KPMG that CA's accounting during the period at issue in the article was appropriate. Dr. Kenny took no further action to re-review CA's financial statements at the time, and requested no further follow-up from management or the auditors. By all accounts, the 35-Day Month was not specifically raised or discussed during the meeting.

Dr. Kenny reported to the non-management Oversight Director Defendants directly after the meeting. In her report, Dr. Kenny stated that management, and CA's outside auditors, had assured her that there was no substance to the allegations in the article and that CA used no "accounting tricks." While the SLC found that Dr. Kenny may have misconstrued, and therefore overstated, the assurances actually given to her by the auditors, Dr. Kenny relied upon her understanding of those assurances, and, in concert with the other members of the Audit Committee, Alfonse D'Amato and Willem de Vogel, determined that no further action was necessary at the time.

While the SLC believes that it would have been a better response for the Audit Committee as a whole to have: (i) questioned the audit firms and management more thoroughly regarding each of the allegations in the article, including the 35-Day Month; (ii) taken more time, and given more time to the auditors, to evaluate and prepare their response to the specific allegations in the article; and (iii) obtained independent advice from outside advisors with respect to the allegations in the article, simply because other steps could have been taken does not mean that what the Board did do was legally insufficient. As such, the SLC found that, even if the New York Times article were considered a "red flag," the non-management Oversight Director Defendants engaged in legally sufficient oversight, did not demonstrate a conscious disregard of their responsibilities, and did not breach their duty of oversight or care.

The SLC also examined Dr. Kenny's independence in light of her personal and professional relationship with Mr. Wang. The SLC was concerned about Mr. Wang's donation of the Charles B. Wang Center for Asian and Asian American Culture to the State University of New York at Stony Brook (the building cost over $52 million), where Dr. Kenny served as President. The donation was announced in 1996 (after Dr. Kenny joined the Board), and the building was completed in October 2002. Dr. Kenny was named as Chair of the Audit Committee on June 6, 2000, at which time the Board determined that Dr. Kenny was independent within the meaning of the New York Stock Exchange ("NYSE") independence rules in place at that time.[14] However, the SLC was troubled by the fact that the Board does not

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14 The NYSE rules in effect in June 2000 specify the relationships that disqualify a director from being considered "independent" for purposes of serving as a member of an issuer's audit committee. A director will not be considered "independent" if, among other things, he or she has:

> been employed by the corporation or its affiliates in the current or past three years;
>
> an immediate family member who is, or has been in the past three years, employed by the corporation or its affiliates as an executive officer;
>
> been (i) a partner, controlling shareholder, or executive officer of an organization that has a business relationship with the corporation or (ii) has had a direct business relationship with the corporation (e.g., a consultant), unless the corporation's board determines in its business judgment that the relationship does not interfere with the director's exercise of independent

appear to have considered at length, either at the time Dr. Kenny joined the Board in 1994 or at the time she was appointed head of the Audit Committee, whether this relationship, which was publicly known and discussed at the Board level, impaired her independence.

In the end, based upon the SLC's interviews of Dr. Kenny and others, the SLC found no evidence that Dr. Kenny's relationship with Mr. Wang impaired her ability to independently evaluate the allegations made in the article, adversely impacted or affected the analysis that she performed, or ultimately colored her conclusions. That said, it is far from a best practice to have the head of the Audit Committee have such an important and meaningful relationship to the CEO (which Mr. Wang was in June 2000 when she was appointed), and would likely not be permissible under today's independence rules.

Overall, the SLC reaches a different conclusion with respect to Mr. Wang, who was the Company's CEO and Chairman during much of the period in which the fraudulent conduct occurred. The SLC has uncovered credible and corroborated evidence that Mr. Wang both directed and participated in the 35-Day Month practice by (i) instructing his subordinates, including Messrs. Kumar, Richards and Zar, to obtain additional revenue after the closes of quarters to be counted in the prior quarter in order to meet analyst expectations, and (ii) negotiating and participating in the negotiation of deals that he knew to be backdated. Indeed, it is the SLC's view that Mr. Wang was the direct cause of the 35-Day Month practice, both due to his actual conduct and the culture that he established, and that it existed for most, if

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judgment. Business relationships can include commercial, industrial, banking, consulting, legal, accounting and other relationships. A director can have this relationship directly with the company, or the director can be a partner, officer or employee of an organization that has the business relationship; or

been employed as an executive of another entity where any of the corporation's executives serve on that entity's compensation committee.

not all, of his tenure as CEO. It was only under Mr. Kumar's watch as CEO that the practice ended with the implementation of the new business model.

As such, the SLC believes that Mr. Wang breached his fiduciary duties to CA by knowingly participating in the 35-Day Month practice. In addition, the SLC believes that Mr. Wang failed CA's shareholders, failed CA's employees, and failed CA's customers by failing to protect the assets of CA through an appropriate management structure and to install the necessary procedures and controls in the hands of properly-trained and experienced executives. At the same time, Mr. Wang missed no opportunity to enrich himself at CA's expense. Accordingly, the SLC has directed the Company to vigorously pursue a claim for breach of fiduciary duty, among other claims, as noted above, against Mr. Wang for the full amount of the enormous harm caused to CA.

The SLC was particularly troubled by Mr. Wang's refusal to cooperate with the SLC's investigation, claiming, through his counsel, that any interview would be duplicative of prior testimony that he has given. The SLC believes that this excuse lacks credibility and moral force. Mr. Wang, as the Company's co-founder, and former CEO and Chairman, had an obligation to cooperate with a duly-appointed, independent committee of the Board investigating the reasons for a massive financial fraud that occurred under his leadership at the Company he created. Mr. Wang had a duty to contribute to the SLC's understanding of these events so that, at the very least, steps can be taken to ensure that they are not repeated. Mr. Wang abdicated that duty.

The Settlement Director Defendants. The 2005 Derivative Action alleges that the Settlement Director Defendants breached their duty of care to the Company when, in August 2003, they authorized the settlement of then-pending class action and derivative litigation, and allowed the settlement to become final before U.S. District Court Judge Thomas Platt in December of 2003. Because the settlement was "global" and encompassed a derivative action, which was brought on behalf of the Company, the Company's officers and directors (including certain of the Criminal Defendants) received releases from the Company in connection with the settlement. Plaintiffs allege, again without setting forth any facts, that the Settlement Director Defendants knew at the time they authorized the global settlement that CA's senior management had engaged in fraud, but nonetheless breached their duty of care by failing to seek contribution from those individuals in exchange for the releases.

Under Delaware law, a directors' decision to authorize a settlement will be protected by the business judgment rule, a judicial presumption that the directors acted in a manner consistent with the duty of care – that is, "on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company." *Aronson v. Lewis,* 473 A.2d 805, 812 (Del. 1984). In order to rebut this presumption, it must be shown that the directors acted with (i) fraud, (ii) illegality, (iii) a conflict of interest, (iv) or gross negligence. Thus, the SLC sought to determine whether the CA Board's decision was tainted by any of the above factors such that its decision constituted a breach of the duty of care.

It is clear that the decision to authorize the settlement occurred at a difficult time for the CA Board and the Company. By August 2003, the Company had been embroiled in the class action litigation for five (5) years, had been defending a joint USAO and Securities and Exchange Commission ("SEC") investigation for over a year and a half, and, at the request of the USAO, had just authorized the Audit Committee to conduct an internal investigation into CA's accounting practices. To fully understand the context in which the decision to settle the civil litigation was made, some additional background about the government investigation is in order. The progression of the government investigation can be broken down into roughly two (2) phases.

From February 2002 through January 2003, the Board was informed repeatedly by CA management that the Company had done nothing wrong and by the Company's counsel, Wachtell, Lipton, Rosen & Katz LLP ("WLRK"), that it had found little to no substance to the accounting issues being examined as part of the government investigation. WLRK's advice and assessment turned out to be accurate in many respects, as nearly all of the issues originally being investigated by the government were resolved in CA's favor or otherwise became non-issues, from which the Board took comfort. Further, the Board was told by management that the April 29, 2001 New York Times article and the government investigation that followed (which focused on the same general issues) were both the result of (i) disgruntled former employees with little actual knowledge who fed the government and the press inaccurate information, and (ii) cooperation between the plaintiffs' lawyers at the Milberg Weiss law firm, lead counsel in the class action litigation, and the government.

Beginning in January 2003, when the CA Board learned that the government had recently issued grand jury subpoenas to CA and its customers, the CA Board recognized that there were revenue recognition issues that it was told were, in fact, being addressed. The message the Board received about the government investigation, however, changed substantially in July 2003. At a July 2, 2003 Board meeting, the Board was told by WLRK that: (i) the government refused to settle any charges arising out of the investigation of CA on a civil basis because it "believed that senior management of the company had intentionally held quarters open and used backdated contracts to meet earnings estimates"; and (ii) Ira Zar, David Rivard, and Lloyd Silverstein – then three of the Company's senior financial managers – had been identified as "subjects" of the government's investigation. At that time, the Board was also told that the government had suggested that the Board authorize its own independent investigation into CA's accounting practices, which the Board did at that meeting. This news came as a shock to many Board members, although some still believed that, because the government had not provided the Company with any evidence of wrongdoing by CA's executives, it was only "saber-rattling" to extract a better settlement.

At the same time, the civil class action and derivative litigation was progressing towards a settlement, with the help of mediation by a retired U.S. District Judge. At a June 18, 2003 Board meeting, counsel to CA in the class actions, Piper Rudnick, told the Board that the parties to the litigation had reached a preliminary settlement, and outlined the terms of the proposed agreement to the Board. The Board was universally pleased to learn that the settlement was an "all-stock" deal, involving the issuance of 5.7 million shares of CA stock (then-valued at approximately $130 million) and did not involve a cash payment by the Company. Counsel further advised the Board that a settlement would likely have a favorable impact on the government investigation. At the suggestion of counsel, the Board formed an independent committee to evaluate the proposed settlement. After receiving periodic updates regarding the settlement, in August 2003, two separate and independent committees were formed to evaluate the terms and merits of the settlements of the class action and derivative litigation, respectively, and to recommend a course of action for the Company.

The class action settlement committee, comprised of directors D'Amato (who served as chair), Lorsch, Ranieri, and Schuetze, was represented by Peter Fleming of Curtis, Mallet-Prevost & Mosle LLP, one of the senior members of the New York trial bar. At a telephonic committee meeting to consider the settlement, Mr. Fleming told the committee that:

(i) the Company faced potential liability of two (2) to five (5) billion dollars at trial; (ii) the Company's summary judgment motion would likely be denied and that a trial was likely; (iii) the federal judge who presided over the parties' mediation had recommended a settlement amount that was larger than the agreed-upon amount; and (iv) CA must win every trial that it faced, and only needed to lose one for a substantively catastrophic outcome to occur. Mr. Fleming's talking points state that he recommended the settlement "in the strongest possible way."

The members of the committee generally recalled Mr. Fleming's advice, particularly the downside risk of two (2) to five (5) billion dollars. After considering Mr. Fleming's advice, and the committee's prior knowledge of the litigation (including the advice of WLRK and others that the existence of the class action suit was an impediment to resolving the government investigation), the committee decided to recommend the class action settlement to the full Board. This is a decision the SLC cannot and does not quibble with, either as a matter of process under Delaware law, or on its merits. This was a decision that was, and remains, in CA's best interest in all respects and was supported by valid business considerations.

The derivative settlement committee, comprised of directors Lorsch (who served as chair), Cron, Fernandes, La Blanc, Schuetze, and Vieux (i.e., those directors not named as defendants in the 2003 Derivative suit), had, in the view of the SLC, a more difficult decision to make. This committee was represented by James McGuire, then counsel at White & Case LLP, now a New York State Supreme Court Justice (Appellate Division), who was assisted by Richard Holwell, then a partner at White & Case, now a U.S. District Judge for the Southern District of New York. This committee was faced with, among other things, the task of determining whether, in the context of settling the derivative case, it was in CA's best interests to grant releases to its officers and directors as part of the global settlement.

Though recollections vary, contemporaneous evidence establishes that the committee asked Mr. McGuire two questions on that subject during the telephonic meeting in which it considered the settlement: (i) whether the settlement of the derivative case could be delayed pending the outcome of the Audit Committee's investigation, and (ii) whether some defendants could be carved out of the releases in the settlement. Mr. McGuire answered "no" to both questions, advising the Committee that any attempt to delay or restructure the settlement would jeopardize the "global" deal that had been negotiated. Further, the committee considered the advice that the directors had previously received from counsel regarding the favorable impact a civil settlement may have on the government investigation. After weighing the risks and rewards associated with the derivative settlement, the committee likewise decided to recommend the derivative settlement to the full Board.

The SLC found its evaluation of the derivative settlement committee's actions to be one of the more difficult tasks it faced. In the end, the SLC concluded that the directors employed a rational decision-making process and made what has proven to be a good business decision in the context of a global settlement. There were valid business considerations that the Board reasonably and honesty believed, and these considerations drove and supported the decision to authorize the settlement. That said, the SLC was concerned by the selection of counsel for the derivative settlement committee (picked by management), and the time spent considering these issues (one relatively short telephonic meeting). However, these facts do not suggest that the decision or process was the product of gross negligence,[15] was outside the

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15 Gross negligence is defined under Delaware law as "reckless indifference to or deliberate disregard of the whole body of stockholders or actions which are without the bounds of reason." *In re The Walt Disney*

bounds of reason, or was for any disloyal or bad faith reason. As such, this decision is protected by the business judgment rule. In addition, because there was no bad faith conduct, this decision is also protected by the Company's Certificate of Incorporation and Delaware General Corporation Law § 102(b)(7).

Finally, the SLC found that the Settlement Director Defendants did not breach their fiduciary duty in connection with their oversight of the Company throughout the government investigation. It bears repeating that liability for breach of fiduciary duty in this context hinges on whether the directors "had notice of serious misconduct and simply failed to investigate," i.e. intentionally ignored "red flags." *Stone*, 911 A.2d at 360. Here, the Board had a clear red flag – the investigation commenced by the USAO and SEC. In response, the Board retained WLRK as Company counsel, and directed WLRK to cooperate with the government in order to resolve the investigation as quickly as possible. In addition, the Board retained PwC to evaluate the allegations of improper accounting raised by the government, and directed and supervised PwC during its work. At the later suggestion of the USAO, the Board immediately authorized the Audit Committee to conduct a full-scale independent investigation with the assistance of independent counsel, Sullivan & Cromwell LLP ("S&C"). It is worth noting that, while S&C certainly played a key role, Audit Committee chair Walter Schuetze (the former Chief Accountant to the SEC) was personally involved in all major interviews and actions and was the driving force behind the Audit Committee's investigation.

Once the 35-Day Month practice was uncovered in September and October of 2003, the Audit Committee promptly requested and received the resignations of Messrs. Zar,

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Co. Derivative Litig., 907 A.2d 693, 750 (Del. Ch. 2005), *aff'd*, 906 A.2d 27 (Del. 2006) (citation omitted); *see also Albert v. Alex Brown Mgmt. Serv., Inc.*, 2005 WL 2130607, at * 4 (Del. Ch. Aug. 26, 2005) ("Gross negligence . . . involves a devil-may-care attitude or indifference to duty amounting to recklessness") (citation omitted).

Rivard, and Silverstein. In response to further events, the Audit Committee terminated the employment of Mr. Kaplan in December 2003, and Messrs. Richards, Woghin, and others in April 2004. Ultimately, Mr. Kumar resigned at the Board's request in June 2004. Given the actions taken by the Board throughout the government investigation, the SLC concludes that the Board did not intentionally "ignore" the government investigation in bad faith. To the contrary, the SLC found that the Board responded to the government investigation in an adequate manner.

* * *

In sum, and to state the obvious, for most of its history CA was not a model of corporate governance. The scope of the SLC's investigation – of claims against twenty-two (22) individuals and entities – revealed flaws in how the business was managed. In addition, while the directors fulfilled their fiduciary obligations, the SLC found that they did not always grasp the opportunities that should be the aspirational goal of every board.[16] As such, although not part of the SLC's mandate, the SLC nonetheless believes that it is appropriate, for the benefit of the current and future members of CA's Board (and others), to comment on the Board's response to these events. In offering this commentary, the SLC recognizes that it is easy, with the clarity of hindsight, to criticize the Board's reactions to these events given what is now known about the scope and magnitude of the fraud. The SLC also offers this

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16 Chancellor Chandler's influential decision in the *Disney* matter recognized this distinction:

> But the law of corporate fiduciary duties and remedies for violation of those duties are distinct from the aspirational goals of ideal corporate governance practices. Aspirational ideals of good corporate governance practices for boards of directors that go beyond the minimal legal requirements of the corporation law are highly desirable, often tend to benefit stockholders, sometimes reduce litigation and can usually help directors avoid liability. But they are not required by the corporation law and do not define standards of liability.

Disney, 907 A.2d at 745 n.399.

commentary while acknowledging that the Company's most senior managers, who directly controlled the information flow to the Board, engaged in active efforts to conceal information from the Board (and some have pled guilty to serious federal crimes).

The SLC believes that the non-management Oversight Directors were presented with opportunities, at several points in time, where they could have engaged in a searching analysis. The Board could have taken incremental steps to seek verification of the Company's financials when the vesting of the KESOP was imminent; it could have actively probed the accountants once the KESOP vested; it could have probed management's explanation as to the timing of when it learned of the effects of the events in Asia; it could have connected the news of slowing growth in Asia to the billion dollar stock award that vested eight (8) weeks earlier; it could have treated the allegations made in the shareholder litigation following the vesting of the KESOP in a less cursory fashion; it could have probed management, specifically Mr. Zar, and its outside accountants, more thoroughly when the New York Times article was published; it could have sought independent legal or accounting advice and taken more time to consider the issue. The events discussed above, alone or in concert, may have put a skeptical director on alert that something was amiss, but no director at CA drew that conclusion.

Likewise, the SLC believes that, although the directors satisfied their duties during the government investigation, there are still things that the CA Board could have done better (and thus provide lessons for this and other boards). First, the SLC found that the CA Board could have taken steps to more fully understand the role played, and actions taken (and not taken), by WLRK in its representation of the Company during the investigation. The SLC found that the directors believed that WLRK was conducting a full scale investigation "to get to the bottom of things," when instead WLRK was hired to defend the Company and not to uncover wrongdoing. Second, in 2003, when the government expressed dissatisfaction with CA's document collection and production efforts, the CA Board could have probed to understand what had occurred and, if a problem existed, taken action to remedy that problem, such as insisting that outside counsel actively assist the Company with the collection efforts rather than relying exclusively on inside legal staff to do this critical job. The SLC recognizes, however, that WLRK never suggested to the Board that any additional action be taken at any time, and the Board was continually assured by inside and outside counsel that the Company was fully cooperating with the government. Third, overall, the CA Board could have viewed the assurances it received from management – especially those made after January 2003 when it learned that CA and its customers had received grand jury subpoenas – with a greater skepticism and insisted that outside counsel independently assess and verify those assertions.

This is a theme that the SLC will return to throughout this report – that the CA Board, at various points in time, too often accepted the explanations and assurances of CA management and its advisors without applying a high degree of skepticism or fully understanding the details of what was being done. Such skepticism and careful probing of management and advisors might have led the directors to take further action in situations where, although action was not required to satisfy their fiduciary duties under Delaware law, it nonetheless might have benefited the Company and saved it from further harm.

This leads to several additional conclusions that the SLC takes away from its investigation concerning a board's use of outside, professional advisors, whether those professionals are legal, financial, accounting, or otherwise. While these conclusions may seem intuitive, in hindsight, the SLC, in both this investigation and in drawing on its own Board experiences, has found this not always to be so. The SLC believes that it is imperative that

Boards clearly define, and understand, the scope of the engagement of those professionals. It is clear that those professionals hired by a Board will understand, and adhere to the scope of that engagement, and a Board must ensure that it has the same understanding of that scope. As a corollary, a Board must ensure that it remains updated and aware of what those professionals are doing during the course of the engagement, so in the event that circumstances change, a Board can likewise change the scope of the professionals' engagement, if necessary. Moreover, especially in situations as critical as the one that CA confronted, the professionals have a responsibility to take all necessary steps to make sure that the Board – and not just Company management – understands precisely what the professionals are, and are *not*, doing. But in the end, at all times, the onus is on the Board to actively and appropriately manage and supervise its professionals, and without having these understandings, a Board will not have the wherewithal to do so.

In considering the lessons learned from its investigation, the SLC believes it equally important to highlight those instances where directors went far beyond the level of conduct required under law and instead did approach the ideal all directors should aspire to attain. Clearly in this category is the internal investigation undertaken by CA's Audit Committee, and particularly its chair, Walter Schuetze. As soon as the Board learned of the government's suggestion that the Audit Committee conduct its own investigation of CA and its management, that request was approved. The Audit Committee promptly hired its own independent counsel that was free from interference and influence by CA management and began the process of imaging computers and understanding the facts that could be gleaned from the documentary record. When those documents showed that a problem clearly existed, the Audit Committee took swift and effective action, including promptly seeking the resignations of the three (3) executives in charge of the sales accounting function. The Audit Committee continued its efforts by conducting scores of interviews and regularly meeting with the government.

Importantly to the SLC, while the Audit Committee certainly relied on its professionals, it did not delegate its work. Instead, the Audit Committee members, particularly Mr. Schuetze, personally participated in the investigation – conducting the interviews, meeting with the USAO and the SEC and, in a hands-on fashion, directing the investigation. Indeed, Mr. Schuetze spent a substantial amount of time in New York (away from his Texas home) supervising the Audit Committee's work. Director and Audit Committee member Lewis Ranieri also deserves credit for his actions and leadership during the Audit Committee investigation. While obviously this level of personal sacrifice and dedication goes far beyond that which is required by Delaware law, it is an exemplar of director dedication.

In sum, CA's recent past has been filled with a seemingly endless stream of litigation, investigations, criminal prosecutions, and overall disruption as a result of the criminal 35-Day Month practice. All of these distractions continue to work to the detriment of CA's core business – developing and selling software on behalf of its public shareholders. The SLC believes it is time for the Company to finally resolve any and all outstanding issues associated with the criminal activity that occurred at the Company in order to allow it to move forward and focus on the future. To that end, the SLC has concluded that it is in the Company's best interest to pursue certain meritorious claims against those who directed and benefited most from the fraud (where those suits can reasonably lead to a monetary recovery), but seek dismissal of the claims against others who can best be characterized as victims of a complex and sophisticated criminal scheme, including a well-orchestrated and purposeful obstruction by those guilty of the malfeasance.[17]

II. THE COMPANY

CA, a Delaware corporation, has its principal place of business in Islandia, New York. The Company was co-founded in 1976 by Charles Wang and Russell Artzt, and Mr. Artzt remains with the Company as Executive Vice President in charge of products. CA is one of the largest computer software companies in the world, and more than ninety-eight percent (98%) of Fortune 1000 companies use its software products.

In fiscal year 2006,[18] CA had revenue of $3.64 billion, and employed over 15,000 people. The bulk of CA's earnings come from revenue generated by contracts in which CA licenses its software products. CA's common stock trades on the NYSE. The four (4) primary departments within the Company that will be referred to throughout this report, are the Sales department ("Sales"), the Finance department ("Finance"),[19] the Sales Accounting department ("Sales Accounting"), and the Global Sales Organization ("GSO" or "Global Sales Operations").

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17 One final note is appropriate. The SLC believes that certain aspects of this costly litigation and investigation are the direct result of a plainly inaccurate account of the facts surrounding the discovery of the 35-Day Month practice at CA reported in the press. The entire claimed basis for the Rule 60(b) Motions is that the so-called "23 Boxes" of documents, which were first reported in a Wall Street Journal article, were "secretly" withheld from the government and Company counsel. Had the documents not been hidden, the theory goes, many harms could have been avoided, and the 2003 Settlement may never have happened. However, contrary to public perception, the SLC found that there was no "secret" cache of "23 boxes" of documents that were collected and hidden, but instead, the SLC found that the Company's document collection efforts were deficient in many respects, and, once remedied, substantial amounts of incriminating documents were collected and produced to the government. Moreover, there was no material information in those documents that was not disclosed in CA's October 8, 2003 press release announcing the resignations of Mr. Zar and others.

18 CA's fiscal year begins on April 1 and ends on March 31. Its first quarter ends on June 30, its second quarter on September 30, and its third quarter on December 31.

19 The Financial Reporting department ("Financial Reporting") falls under the supervision of the Finance department.

III. THE 2005 DERIVATIVE ACTION

Overview. In June and July of 2004, certain parties affiliated with Sam Wyly and two individual CA shareholders, Bert Vladimir and Irving Rosenzweig, filed three derivative actions in the U.S. District Court for the Eastern District of New York (the "Eastern District"), captioned *Ranger Governance, Ltd. v. Wang et al.*, 04-2697, *Vladimir v. Wang et al.*, 04-2789, and *Rosenzweig v. Wang et al.*, 04-2959. By order dated October 19, 2004, the three derivative actions were consolidated and re-captioned *In re Computer Associates International Inc., Derivative Litigation*, 04-2697 (TCP). On January 7, 2005, the operative Consolidated Stockholders Derivative Complaint was filed. *See* Consolidated Stockholders Derivative Complaint, dated Jan. 7, 2005 (the "2005 Derivative Complaint"). As discussed in detail below, the 2005 Derivative Complaint asserts eight (8) causes of action against twenty-two (22) current and former CA directors, officers, and employees, as well as claims against CA's current and former independent auditors, KPMG and E&Y, respectively. *See* 2005 Derivative Compl. ¶¶ 8-30, 32-33.

The filing of the 2005 Derivative Complaint precipitated the creation of the SLC by CA's Board, which occurred by resolution dated February 1, 2005. In that resolution, the CA Board authorized the SLC to (i) control and determine the Company's response to the 2005 Derivative Complaint, and (ii) control and determine the Company's response to three motions that were filed under Federal Rule of Civil Procedure 60(b), seeking relief from the final judgments entered in the 1998 and 2002 class actions and related derivative litigation. On October 31, 2006, the CA Board authorized the SLC to control and determine the Company's response to a substantially similar derivative complaint filed in the Delaware Court of Chancery, captioned *Kaufman v. Kumar*, *et. al.*, 06 Civ. 2418-N (the "Kaufman Complaint") that raises substantially similar claims.

Because the history of the prior class action and derivative litigation is material to the SLC's investigation, the history of those litigations is described below in brief.

A. *The 2003 Settlement and the Rule 60(b) Motions*

1. The Class Action and Derivative Litigation

As noted above, following the July 21, 1998 press release announcing that CA expected slowing growth, and the resultant thirty-one percent (31%) stock drop, a number of class action lawsuits were filed in the Eastern District against CA and certain of its officers, alleging various violations of federal securities laws. By order dated October 9, 1998, those individual cases were consolidated and captioned *In re Computer Associates Class Action Securities Litigation*, 98 Civ. 4839 (TCP) (the "1998 Class Action").

The 1998 Class Action alleged that CA began to experience serious financial difficulties prior to the vesting of the KESOP shares, and that these difficulties led CA to artificially inflate its revenues, in part, to protect the interests of the beneficiaries of the KESOP. The plaintiffs claimed that CA: (i) inflated revenue by recognizing revenue on long-term contracts upfront, allegedly in violation of generally accepted accounting principles ("GAAP"); (ii) offered excessive discounts to make revenue appear larger on certain products; and (iii) engaged in certain unspecified "improper revenue recognition practices that artificially inflated CA's operating results." On November 15, 1999, U.S. District Judge Thomas Platt denied the defendants' motion to dismiss the complaint, and discovery proceeded, with both sides collectively taking over fifty (50) depositions. In that litigation, CA also produced hundreds of thousands of pages of documents.

In February 2002, following the announcement that the USAO and SEC had commenced a preliminary investigation into CA's accounting practices, another series of class action lawsuits were filed against CA and certain of its officers and directors. By order dated

July 25, 2002, those individual cases were consolidated by Judge Platt and captioned *In re Computer Associates 2002 Class Action Securities Litigation*, 02 Civ. 1226 (TCP) (the "2002 Class Action") (collectively with the 1998 Class Action, the "Class Actions"). The 2002 Class Action, which was also consolidated with the 1998 Class Action, expanded the end of the class period for the 1998 Class Actions from July 22, 1998 to February 25, 2002. Further, the 2002 Class Action included certain allegations of accounting fraud not originally found in the 1998 Class Action, including the allegation that CA improperly extended its quarters.

Also in 2002, CA shareholder Charles Federman filed a derivative action in the Delaware Court of Chancery against certain CA directors, officers, and employees arising out of the same conduct alleged in the Class Actions. The derivative action was subsequently transferred to the Eastern District in August 2003, and captioned *Federman v. Artzt, et. al.*, 03 Civ. 4199 (TCP) (the "2003 Derivative Action"). On August 25, 2003, Judge Platt consolidated the 2003 Derivative Action with the Class Actions. Plaintiffs in the 2002 Class Action and the 2003 Derivative Action served no additional discovery requests of their own, but received the discovery produced to plaintiffs in the 1998 Class Action.

On September 5, 2002, following the close of discovery in the 1998 Class Action, the CA defendants in the Class Actions filed a motion for summary judgment, seeking dismissal of all claims. That motion remained pending when, in May 2003, the parties to the Class Actions participated in mediation supervised by retired U.S. District Judge Frederick B. Lacey. In June 2003, the parties to the Class Actions and the 2003 Derivative Action reached a "global settlement," pursuant to which (i) all of the then-pending shareholder litigation against and on behalf of CA would be resolved, and (ii) CA would pay shareholders 5.7 million shares of CA stock (the "2003 Settlement"). The 2003 Settlement was later modified to include a cash component if CA shares traded below a designated level on the date the settlement became final. *See* Stipulation and Agreement of Settlement of Securities Class Actions with CA Defendants ¶¶ 3, 6(b), *In re Computer Assocs. Class Action Sec. Litig.*, 98 Civ. 4839 (TCP) (E.D.N.Y. Aug. 25, 2003)); Stipulation and Agreement of Settlement of Derivative Actions ¶ 3, *Federman v. Artzt, et al.*, 03 Civ. 4199 (TCP) (E.D.N.Y. Aug. 25, 2003)).

Following a fairness hearing held before Judge Platt on December 5, 2003, the 2003 Settlement was approved as fair by orders signed on December 8, 2003 and entered December 10 and 11, 2003.

The release granted in the 2003 Derivative Action, which ran from the Company to its officers and directors, provided:

> Upon the Effective Date of this Settlement, *Plaintiff and CA shareholders, derivatively on behalf of CA, and CA*, on their own behalf and on behalf of their respective predecessors, successors, affiliates, heirs, executors, administrators, successors and assigns, and any person they represent, for good and valuable [consideration] *shall, by operation of the Order of Final Judgment and Dismissal, release and be deemed to release and forever discharge, and shall forever be enjoined from prosecuting, any Settled Derivative Claims and/or Unknown Claims against any of the Released Parties* including, without limitation, any claim relating to the parties [sic] entry into this Settlement.

Stipulation and Agreement of Settlement of Derivative Actions ¶ 3, *Federman v. Artzt, et al.*, 03 Civ. 4199 (TCP) (E.D.N.Y. Aug. 25, 2003) (emphasis added)). The term "Released Parties" was defined to include the named defendants[20] and "all other current and former officers and directors of CA." *Id.* ¶ 1(d). Because the release is limited to "officers and directors," certain of the Criminal Defendants who were not corporate officers – David Kaplan, David Rivard, and

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[20] The named defendants were Directors Artzt, de Vogel, Grasso, Ranieri, D'Amato, Kenny, Kumar, Pieper, and Wang.

Lloyd Silverstein – are not covered. In contrast, former CA officers Sanjay Kumar, Stephen Richards, Steven Woghin, and Ira Zar are, technically, covered by the terms of the release.

Similarly, the release granted in connection with the Class Actions stated:

> By operation of the Order and Final Judgment, upon the Effective Dates of this Settlement and without any further action, *Representative Plaintiffs and all the members of the Settlement Class* on behalf of themselves, their heirs, executors, administrators, successors and assigns, and any person they represent, for good and valuable consideration, *shall, with respect to each and every Settled Claim, release and forever discharge, and shall forever be enjoined and barred from prosecuting any settled Claims against any of the Released Parties*.

Stipulation and Agreement of Settlement of Securities Class Actions with CA Defendants ¶ 3(a), *In re Computer Assocs. Class Action Sec. Litig*., 98 Civ. 4839 (TCP) (E.D.N.Y. Aug. 25, 2003) (emphasis added). In the settlement of the Class Actions, "Released Parties" was defined to include CA and all of its "past or present . . . officers, directors . . . [and] employees." *Id.* ¶ 1(p). Thus, the release in the Class Actions is broader than the release in the 2003 Derivative Action because it covers "employees," in addition to officers and directors. As such, all of the defendants named in the 2005 Derivative Complaint are covered by this release.

2. **The Rule 60(b) Motions**

In connection with the filing of the 2005 Derivative Complaint, three separate Rule 60(b) motions were filed in the Eastern District by (i) Sam Wyly and his related Wyly entities (collectively, the "Wyly Movants");[21] (ii) Ranger Governance, Ltd. ("Ranger

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21 In addition to Mr. Wyly, those joining in his request for Rule 60(b) relief were Cheryl Wyly, Donald R. Miller, Jr., The Andrew David Sparrow Wyly Trust, The Cheryl R. Wyly Marital Trust, The Christiana Parker Wyly Trust, The Emily Ann Wyly Trust, The Jennifer Lynn Wyly Trust, The Kelly Wyly Elliott Trust, The Lisa Wyly Revocable Trust, The Martha Caroline Wyly Trust, The Charles Joseph Wyly III Trust, The Laurie L. Wyly Revocable Trust, Dortmund Limited, East Carroll Limited, Elegance Limited, Greenbriar Limited, Marmalade, Ltd., Miller Family Partners, Quayle Limited, Stargate, Ltd., and Tallulah, Ltd.

Governance") (a Wyly-led group of investors separate from the Wyly Movants), Bert Vladimir, and Irving Rosenzweig; and (iii) Muriel Kaufman, respectively.[22]

(a) *The Wyly Movants*

On December 7, 2004, the Wyly Movants filed a motion seeking relief from the December 10, 2003 order approving the settlement of the Class Actions (the "Class Action Rule 60(b) Motion"), claiming that the class action settlement was procured by fraud, misrepresentation, and other misconduct.[23] At this time, Mr. Wyly and Ranger Governance are also involved in concurrent litigation with CA, arising from settlement agreements entered into with CA by Mr. Wyly and Ranger Governance following two proxy contests waged by Mr. Wyly and Ranger Governance during the summers of 2001 and 2002. *See* Amendment to Change in Control Severance Agreement, February 14, 2000 ¶ 10 (the "2002 Wyly Agreement") (collectively, the "Proxy Settlement Agreements").

When Ranger Governance filed its derivative complaint on behalf of CA on June 29, 2004, CA informed it that the lawsuit was barred by the non-compete provisions in the Proxy Settlement Agreements. In response, on August 9, 2004, Mr. Wyly and Ranger Governance filed a complaint in state court in Texas seeking a declaration that Ranger

22 As discussed further below, at the time Ms. Kaufman filed her Rule 60(b) motion, she had not yet filed a derivative complaint.

23 As discussed below, the SLC has opposed this motion on various grounds, including, among others, that (i) the Wyly Movants lack standing to challenge the releases given in the Class Actions since they were not lead plaintiff (and their counsel was not lead counsel) in the underlying Class Actions, and (ii) reopening of the Class Actions offered no potential benefit to CA or its shareholders; to the contrary, it would expose the Company to unnecessary expense and potential liability. *See* Order Consolidating All Actions And Appointing Lead Plaintiffs And Approving Selection Of Lead Counsel, *Barroway*, *et. al*., *v. Computer Assocs. Int'l*, *Inc*., *et. al*., 98 Civ. 4839 (TCP) (E.D.N.Y. Oct. 9, 1998); Order (1) Consolidating All Related Actions; (2) Appointing Lead Plaintiffs; (3) Approving Lead Plaintiffs' Selection of Counsel; and (4) Establishing Briefing Schedule, *In re Computer Assocs. Class Action Sec. Litig*., 02 Civ. 1226 (TCP) (E.D.N.Y. July 25, 2002) (collectively, the "Lead Plaintiff & Counsel Orders"). The SLC's position is more fully articulated in its memoranda of law dated March 18, 2005 and November 1, 2006, and in a memorandum that will be filed shortly after the filing of this report.

Governance's pursuit of this action did not violate the Proxy Settlement Agreements. Mr. Wyly and Ranger Governance also claimed that they were entitled to damages (i) because the Proxy Settlement Agreements, and the related predecessor agreements, were allegedly procured by fraud, and (ii) because CA allegedly breached the Ranger Agreement by failing to elect an independent director to its Board and failing to impose certain heightened corporate governance standards. On September 10, 2004, CA removed the Wyly state court action to the U.S. District Court for the Northern District of Texas, and on September 1, 2005, it was transferred to the Eastern District, where it remains pending concurrently with the 2005 Derivative Action.

(b) *The Individual Derivative Plaintiffs*

(i) Muriel Kaufman

On October 5, 2004, Muriel Kaufman, a CA shareholder who was not a party to any of the prior litigation, filed her own Rule 60(b) motion seeking to vacate the final judgment in the 2003 Derivative Action, but not the final judgment in the Class Actions. On September 14, 2004, Ms. Kaufman filed an action under § 220 of the Delaware General Corporation Law seeking to obtain certain of CA's books and records. As a result, CA produced to Ms. Kaufman numerous documents relevant to this action. Ultimately, and as noted above, on September 13, 2006, Ms. Kaufman filed a separate derivative complaint in the Delaware Court of Chancery asserting claims that are substantially duplicative of the claims alleged in the 2005 Derivative Complaint.[24]

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24 On December 19, 2006, the SLC sought dismissal of the Kaufman Complaint as duplicative of this action because (i) the 2005 Derivative Action was filed two years prior to the Kaufman Complaint, and (ii) the 2005 Derivative Action, which involves the same parties and issues, provides a forum for prompt and complete justice. Briefing on that motion has not yet been completed.

(ii) Ranger Governance, Bert Vladimir, and Irving Rosenzweig

On December 9, 2004, Ranger Governance (Mr. Wyly's entity), Bert Vladimir, and Irving Rosenzweig, plaintiffs in the 2005 Derivative Action, collectively filed a motion for relief under Rule 60(b) seeking to vacate the final judgment in the 2003 Derivative Action, making the same arguments that the Wyly Movants made in seeking to upset the final judgment in the Class Actions (the "Derivative Rule 60(b) Motions"). The three Rule 60(b) motions are referred to here collectively as the "Rule 60(b) Motions," unless otherwise noted.

3. **The 2005 Derivative Action is Stayed**

By orders dated January 27, 2005 and February 8, 2005, U.S. Magistrate Judge Thomas Boyle stayed discovery in the 2005 Derivative Action pending the outcome of the Rule 60(b) Motions, finding that, "the outcome of [the Rule 60(b) Motions] will define and determine the scope of the claims that may be raised in the present case." *See* Order at 2, *Computer Assocs. Int'l*, *Inc*., *Derivative Litig*., 04 Civ. 2697 (TCP) (ETB) (E.D.N.Y. Feb. 8, 2005).

4. **The SLC's Motion to Stay and Response to the Rule 60(b) Motions**

On February 14, 2005, the SLC, prior to its retention of Fried Frank as counsel, filed a motion to stay all proceedings with respect to the 2005 Derivative Action and the Derivative Rule 60(b) Motions, pending the outcome of its investigation. On April 8, 2005, after Fried Frank was retained, the SLC filed a memorandum in further support of its February 14 motion to stay the 2005 Derivative Action.

On March 18, 2005, the SLC filed its responses to the Rule 60(b) Motions. The SLC opposed the Class Action Rule 60(b) Motion filed by the Wyly Movants because reopening of the Class Actions offered no potential benefit to CA or its shareholders; to the contrary, it would expose the Company to unnecessary expense and potential liability. In its opposition to certain discovery requests made by the Wyly Movants, dated November 1, 2006, the SLC also argued that because the Wyly Movants were not appointed lead plaintiffs in the Class Actions (and its counsel was not appointed lead counsel) by Judge Platt under the Private Securities Litigation Reform Act, they lack standing to seek to upset the settlement of the Class Actions. Following the conclusion of its investigation, and understanding the process by which the CA Board settled the Class Actions, the SLC has only strengthened its belief that the settlement of the Class Actions should remain intact and undisturbed.

With respect to the Derivative Rule 60(b) Motions, the SLC took no position as to the merits of the motions, but instead asked the Court to stay any resolution to allow the SLC time to conduct its investigation and determine the Company's response to both the 2005 Derivative Action and the Derivative Rule 60(b) Motions. This was necessary, the SLC advised the Court, because of the possibility that (i) it would join in certain aspects of the request for Rule 60(b) relief at such time as the SLC completed its investigation, and/or (ii) settle certain claims in the 2005 Derivative Action, and/or (iii) seek to have certain aspects of the 2005 Derivative Action dismissed, in the latter two cases (both of which have happened) rendering substantial portions of the requested relief moot.[25]

B. ***The Derivative Complaints: Claims***

The 2005 Derivative Complaint asserts eight (8) causes of action against twenty-two (22) current and former CA directors, officers, and employees (collectively, the "individual

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25 In connection with the Rule 60(b) Motions, the movants sought and received substantial document discovery, including (i) the so-called "23 boxes" of documents referenced in a Wall Street Journal article, and (ii) the discovery materials (i.e., produced documents and deposition transcripts) from the underlying Class Actions and the 2003 Derivative Action. In all, the SLC has produced approximately 250,000 pages of documents. The movants' request for additional deposition discovery, which the SLC has opposed, has been fully briefed.

defendants") as well as five (5) causes of action against CA's current and former outside auditors, KPMG and E&Y. *See* 2005 Derivative Compl. ¶¶ 8-33. Counts one through seven and count nine relate to the individual defendants; counts eight, ten, and eleven, and part of counts two and nine, relate to the auditor defendants (and will not be discussed in this report). *See id.* ¶¶ 251-319. In addition, the Kaufman Complaint asserts three causes of action against certain of the individual defendants, which are substantially duplicative of the claims asserted in the 2005 Derivative Action. *See* Kaufman Compl. ¶¶ 102-117. The allegations in the Kaufman Complaint are identified and discussed separately below.

1. **The 2005 Derivative Complaint**

Count One. Count one alleges that Charles Wang, Sanjay Kumar, Peter Schwartz, and Ira Zar, all former CA CEOs or CFOs, are liable to CA under § 304 of the Sarbanes-Oxley Act, 15 U.S.C. § 7243. *See* 2005 Derivative Compl. ¶¶ 251-262.[26] Specifically, count one asserts that these defendants must disgorge all bonuses and other incentive-based compensation and profits on stock sales for the twelve (12) months after the first public issuance or filing of CA's financial statements for the fiscal years 1998, 1999, 2000, and 2001 (the period from March 31, 1998 to March 31, 2002) because CA restated its financials for fiscal year 2000 and part of fiscal year 2001, and admitted in the DPA that it improperly recognized revenue from at least 1998 through 2001. *See* 2005 Derivative Compl. ¶¶ 260-262.

26 Section 304 provides, in relevant part, that if an issuer of securities is required to make an accounting restatement due to material noncompliance, as a result of misconduct, with a financial reporting requirement under the securities laws, both the CEO and CFO of the issuer shall reimburse the corporation for any bonus or other incentive-based or equity-based compensation received by those individuals during the twelve (12) month period following the first public issuance or filing with the SEC, whichever comes first, of the financial document embodying the financial reporting requirement.

Count Two. Count two alleges that the Criminal Defendants, the Former Officer Defendants, the Oversight Director Defendants (except Shirley Strum Kenny and Alfonse D'Amato), and the auditor defendants are liable to CA for contribution under the Private Securities Litigation Reform Act (the "PSLRA"), 15 U.S.C. 78u-4(f)(8), which states that "[a] covered person who becomes jointly and severally liable for damages in any private action may recover contribution from any other person who, if joined in the original action, would have been liable for the same damages." *See* 2005 Derivative Compl. ¶¶ 264-266. Specifically, count two asserts that the 5.7 million shares that CA was required to pay pursuant to the 2003 Settlement should be recovered, in part, from those defendants under § 78u-4(f)(8). *See id.* ¶ 265.

Count Three. First, count three alleges that the Criminal Defendants, the Former Officer Defendants, and the Oversight Director Defendants (except Shirley Strum Kenny and Alfonse D'Amato) are liable for breaching their fiduciary duties under Delaware law for failing to properly oversee CA during the years in which the fraud occurred. *See id.* ¶¶ 271-273. Second, this count alleges that the Settlement Director Defendants (except Alex Vieux) improperly (i) approved the 2003 Settlement, in which CA granted releases to its current and former directors and officers, and (ii) the DPA, both without seeking contribution from the wrongdoers. *See id.* ¶¶ 86-89, 263.

Count Four. Count four alleges that the Criminal Defendants, the Former Officer Defendants, and Messrs. Wang and Artzt are liable for common law restitution and unjust enrichment, and are required to return to CA all bonuses, incentive payments, and other undeserved and unwarranted benefits that they received under CA's 1991, 1995, and 2000 executive compensation and incentive plans. *See id.* ¶¶ 279-283.

Count Five. Count five alleges that the Criminal Defendants, the Former Officer Defendants, and the Oversight Director Defendants (except Shirley Strum Kenny and Alfonse D'Amato) are liable for common law corporate waste for (i) paying undeserved compensation to the Criminal Defendants, the Former Officer Defendants, and the Oversight Director Defendants, and (ii) approving the 2003 Settlement and the DPA without seeking contribution from the wrongdoers. *See id.* ¶¶ 284-286.

Count Six. Count six alleges that the Criminal Defendants, the Former Officer Defendants, and the Oversight Director Defendants (except Shirley Strum Kenny and Alfonse D'Amato) are liable for common law fraud for failing to disclose known facts regarding misconduct by those who participated in the 35-Day Month practice. *See id.* ¶¶ 288. This count further alleges that the above-described defendants misrepresented CA's financial results, which resulted in the transfer of undeserved compensation to certain CA executives. *See id.* ¶¶ 289-290.

Count Seven. Count seven alleges that the Criminal Defendants, the Former Officer Defendants, the Settlement Director Defendants (except Alex Vieux), Russell Artzt, Willem de Vogel, and Charles Wang caused CA to file false and materially misleading proxy statements relating to CA's 2002 Incentive Plan (the "2002 Plan") and the 2003 CA Compensation Plan for Non-Employee Directors (the "2003 Plan") in violation of § 14(a) of the Exchange Act. *See id.* ¶¶ 292-298. Specifically, count seven alleges that the challenged proxy statements failed to disclose (i) violations of federal securities laws, (ii) the participation of certain individual defendants in the securities violations and accounting fraud, and (iii) the failure of certain individual defendants to cooperate with government authorities investigating accounting improprieties and the involvement of certain directors in the obstruction of justice.

Id. ¶ 296. It is further alleged that the 2002 Plan and 2003 Plan were approved by shareholders as a result of the false and misleading proxy statements, and would not have been approved if material information had been properly disclosed. *Id.* ¶¶ 294-297.

Count Nine. Count nine alleges that the auditor and individual defendants (except Shirley Strum Kenny and Alex Vieux) are liable for common law contribution and indemnification for the 5.7 million shares CA paid in the 2003 Settlement and the $225 million CA paid pursuant to the DPA. *Id.* ¶¶ 304-307.

2. **The Kaufman Complaint**

The Kaufman Complaint asserts three (3) causes of action against certain of the individual defendants that are substantially duplicative of those raised in the 2005 Derivative Action.

Count One. Count one alleges that the Criminal Defendants (except David Kaplan and David Rivard), the Oversight Director Defendants (except Roel Pieper), and the Settlement Director Defendants are liable to CA for breaching their fiduciary duties by, among other things, (i) failing to properly oversee CA during the period in which the fraud occurred, (ii) failing to properly oversee CA during the government investigation into the Company's accounting practices, and (iii) causing the Company to approve the 2003 Settlement. *See* Kaufman Compl. ¶¶ 102-105. This claim is virtually identical to count three in the 2005 Derivative Complaint, and, as such, it will be analyzed in conjunction with that claim.

Count Two. Count two alleges that the Criminal Defendants (except David Kaplan and David Rivard), the Oversight Director Defendants (except Roel Pieper), and the Settlement Director Defendants are liable to CA for common law corporate waste for (i) using corporate assets to eliminate their personal exposure to liability as the result of the claims alleged in the Class Actions and the 2003 Derivative Action, and (ii) paying undeserved compensation to certain CA executives based on CA's fraudulent financial results. *See id.* ¶¶ 106-110. This claim is virtually identical to count five in the 2005 Derivative Complaint, and, as such, it will be analyzed in conjunction with that claim.

Count Three. Count three alleges that the Criminal Defendants (except David Kaplan and David Rivard), the Oversight Director Defendants (except Roel Pieper), and the Settlement Director Defendants are liable to CA for common law contribution and indemnification for causing CA to pay (i) all the consideration as part of the 2003 Settlement, and (ii) the penalties and other monetary compensation paid to the government in connection with the DPA. *Id.* ¶¶ 111-113. This claim is virtually identical to count nine in the 2005 Derivative Complaint, and, as such, it will be analyzed in conjunction with that claim.

C. ***The Derivative Complaints: Individual Defendants***

The following constitutes a brief overview of each of the individual defendants named in the 2005 Derivative Complaint and the Kaufman Complaint, including their roles at the Company, the claims alleged against them, and the SLC's conclusions as to whether the Company has a viable claim against each defendant.[27]

1. **The Criminal Defendants**

Beginning on January 22, 2004, seven (7) of CA's senior-most executives were charged with, and ultimately pled guilty to, federal criminal charges of securities fraud and obstruction of justice in connection with the 35-Day Month practice. Each of the Criminal Defendants has been criminally sentenced, as described below. A decision on the issue of criminal restitution to be paid by the Criminal Defendants has been deferred by U.S. District

27 Former CA directors Shirley Strum Kenny and Alex Vieux are named as defendants in the Kaufman Complaint, but not in the 2005 Derivative Action. Dr. Kenny and Mr. Vieux are included in the descriptions below, along with those who were named as defendants in the 2005 Derivative Action.

Judge I. Leo Glasser until April 2007, and the SLC understands the Criminal Defendants are engaged in discussions with the USAO on this issue.

David Kaplan. Mr. Kaplan, a CPA, joined Ernst & Whinney (which later became E&Y) as a Staff Accountant after graduating from the State University of New York at Binghamton in 1989. After one year at Ernst & Whinney, Mr. Kaplan joined Canada Drive Royalty Acquisitions, a CA subsidiary, in 1990. From 1990 to 1993, Mr. Kaplan worked as a controller for Canada Drive Royalty Acquisitions. From 1993 to 1997, Mr. Kaplan worked in various finance-related departments at CA, including Sales Accounting, General Accounting, and Financial Reporting. In 1997, Mr. Kaplan became Vice President of Financial Reporting, and in 2001 he was appointed Senior Vice President of Finance and Administration. Mr. Kaplan resigned from CA on December 3, 2003, after refusing to submit to an interview by CA's Audit Committee.

On April 8, 2004, Mr. Kaplan pled guilty to one (1) federal criminal count each of (i) conspiracy to obstruct justice, and (ii) conspiracy to commit securities fraud, for his role in the 35-Day Month practice. *See* Transcript of Plea at 16-20, 25, 30-31, *United States v. David Kaplan*, Cr. No. 04-330 (ILG) (E.D.N.Y. Apr. 8, 2004) ("Kaplan Plea Tr."). Also on April 8, 2004, the SEC filed a complaint against Mr. Kaplan alleging that he violated various federal securities laws. *See* Complaint ¶¶ 28-44, *S.E.C. v. David Kaplan*, 04 Civ. 1465 (ILG) (E.D.N.Y. Apr. 8, 2004) ("Kaplan SEC Complaint"). Specifically, the SEC complaint alleged that Mr. Kaplan: (i) created false internal books and records and prepared false and misleading Forms 10-K and 10-Q; (ii) mislead CA's outside auditors; and (iii) obstructed the SEC's investigation. *See id.* ¶¶ 20-27.

On November 1, 2004, the SEC and Mr. Kaplan entered into a final consent judgment whereby Mr. Kaplan consented, without admitting or denying the allegations against him, to a final judgment that required him to disgorge $128,770 in ill-gotten gains and interest and imposed a $100,000 civil penalty. *See* Final Judgment by Consent Against Defendant David Kaplan at 4-5, *S.E.C. v. David Kaplan*, 04. Civ. 1465 (ILG) (E.D.N.Y. Nov. 1, 2004). As a result of that judgment, Mr. Kaplan is permanently enjoined from (i) violating the federal securities laws, and (ii) serving as an officer or director of a public company. *See id* at 1-4, 6.

As part of its investigation, the SLC interviewed Mr. Kaplan on June 8, 2006 and November 15, 2006. On January 29, 2007, Mr. Kaplan was sentenced to six (6) months home detention followed by three (3) years supervised release. In connection with Mr. Kaplan's sentencing, the SLC submitted a letter to the Court advising it of his cooperation in the SLC's investigation, which, in the SLC's view, evidenced his attempt to ameliorate the immense harm that his criminal conduct has caused CA. *See* Letter from William McCracken and Renato Zambonini to the Honorable I. Leo Glasser, U.S. District Judge, Eastern District of New York (Jan. 26, 2007).

Based on his admitted knowing and intentional criminal conduct, the SLC has directed the Company to pursue claims against Mr. Kaplan for breach of fiduciary duty (count three); restitution and unjust enrichment (count four); fraud (count six); violation of § 14(a) of the Exchange Act (count seven); and indemnification (count nine). The SLC has begun a discussion with Mr. Kaplan's counsel concerning a settlement of the Company's claims against him, and expects that a settlement will be reached shortly after Mr. Kaplan's criminal restitution obligation is determined.

Sanjay Kumar. Mr. Kumar began his CA career in August 1987, after CA acquired Texas-based software maker Uccel. After the Uccel acquisition, Mr. Kumar became CA's Manager of Research and Development. In November 1988, Mr. Kumar rose to the position of Vice President and, in April 1989, Senior Vice President for Strategic Planning. Mr. Kumar served as CA's Executive Vice President for Operations from January 1993 to December 1993, and then, on January 20, 1994, was promoted to President and COO, at which time he joined the CA Board.

On August 4, 2000, the CA Board, at Mr. Wang's recommendation, appointed Mr. Kumar to succeed Mr. Wang as CEO, and, on November 15, 2002, Mr. Kumar was named Chairman of the CA Board. *See* Minutes of a Meeting of the CA Board at 1-2 (Aug. 4, 2000); Minutes of a Meeting of the CA Board at 1-2 (Nov. 15, 2002). Mr. Kumar resigned these positions at the request of the CA Board on April 20, 2004, at which time he took the title of Chief Software Architect. *See* Press Release, Computer Assocs. Int'l, Inc., CA Announces Management Changes (Apr. 21, 2004). On June 4, 2004, Mr. Kumar resigned from CA. *See* Press Release, Computer Assocs. Int'l, Inc., Kumar to Leave Computer Associates (June 4, 2004).

On September 17, 2004, Mr. Kumar (along with Mr. Richards) was indicted on nine (9) counts of securities fraud and obstruction of justice for his role in directing the 35-Day Month practice at CA, and then orchestrating a cover-up of the practice. *See* Indictment ¶¶ 21-39, 41-48, 50-59, 64-79, 82-83, *United States v. Sanjay Kumar & Stephen Richards*, Cr. No. 04-846 (ILG) (E.D.N.Y. Sept. 23, 2004) ("Kumar/Richards Indictment"). On June 29, 2005, the USAO filed a superseding indictment against Mr. Kumar, which re-alleged eight (8) of the counts made against him in the original indictment and provided further factual details in support of those allegations. *See* Superseding Indictment ¶¶ 22-39, 41-50, 52-53, 56-58, 60-61, 65-66, 72-87, 90-91, *United States v. Sanjay Kumar & Stephen Richards*, Cr. No. 04-846 (ILG) (E.D.N.Y. June 28, 2006) ("Kumar/Richards Superseding Indictment").

On September 22, 2004, the SEC filed a complaint against Mr. Kumar. The SEC complaint alleged that Mr. Kumar helped orchestrate and further the 35-Day Month practice by: (i) deciding with other CA executives to extend CA's fiscal quarters until CA had reached a predetermined revenue target; (ii) in at least fiscal year 2000, helping CA obtain various contracts after the quarter-end, including backdated contracts, while knowing or recklessly disregarding the fact that CA would prematurely recognize the revenue from those contracts; (iii) signing false forms filed with the SEC while knowing or recklessly disregarding the fact that those filings were materially false and misleading; and (iv) obstructing the investigation of CA's outside counsel, CA's Audit Committee, and the government. *See* Complaint ¶¶ 2, 16-39, *S.E.C. v. Sanjay Kumar & Stephen Richards*, 04 Civ. 4104 (ILG) (E.D.N.Y. Sept. 22, 2004) ("Kumar/Richards SEC Complaint").

On April 24, 2006, two (2) weeks before his criminal trial was set to begin, Mr. Kumar (along with Mr. Richards) pled guilty to all of the charges lodged against him in the superseding indictment. *See* Transcript of Plea at 67-68, 73-75, *United States v. Sanjay Kumar & Stephen Richards*, Cr. No. 04-846 (ILG) (E.D.N.Y. Apr. 24, 2006) ("Kumar/Richards Plea Tr.").

On June 14, 2006, the SEC and Mr. Kumar entered a partial consent judgment whereby Mr. Kumar consented, without admitting or denying the allegations against him, to a final judgment that permanently enjoined him from (i) violating the federal securities laws, and (ii) serving as an officer or director of a public company. *See* Judgment Imposing a Permanent

Injunction and other Equitable Relief by Consent Against Defendant Sanjay Kumar at 1-4, *S.E.C. v. Sanjay Kumar & Stephen Richards*, 04 Civ. 4104 (ILG) (E.D.N.Y. June 14, 2006).

On November 2, 2006, Mr. Kumar was sentenced to twelve (12) years imprisonment. In connection with Mr. Kumar's sentencing, the SLC submitted a letter to the Court advising it of his failure to cooperate in the SLC's investigation, which, in the SLC's view, evidenced his continuing failure to make any attempt to ameliorate the immense harm he has caused to CA and its core constituents, including its employees, customers, shareholders, and suppliers. *See* Letter from William McCracken and Renato Zambonini to the Honorable I. Leo Glasser (Oct. 24, 2006). Following his sentencing, Mr. Kumar agreed to cooperate with the SLC's investigation and was interviewed by the SLC on seven (7) occasions beginning on January 29, 2007, and continuing through February 28, 2007.

In March 2007, Mr. Kumar and the USAO reached an agreement concerning Mr. Kumar's criminal restitution obligation, the result of which is that Mr. Kumar will pay for the benefit of CA's shareholders $52 million over the next twenty-four (24) months, and then additional sums out of any future earnings. Following this agreement, the SLC entered into negotiations with Mr. Kumar to settle CA's numerous claims against him. These negotiations were hampered by the fact that, in the SLC's view, based on a review of his sworn financial statements, Mr. Kumar had no material assets remaining following his agreement with the USAO. Nonetheless, the SLC has entered into a binding term sheet with Mr. Kumar, to be followed by a definitive agreement, in which Mr. Kumar will consent to the entry of a judgment in the amount of $15,250,000 to be secured in part by real property owned by Mr. Kumar's wife and executable against Mr. Kumar's post-incarceration earnings. The settlement will be presented to the Court for approval in the near future as part of an omnibus motion seeking the approval of multiple settlements. Thus, as a result of these agreements, CA and its shareholders should receive in excess of $67 million from Mr. Kumar.

Stephen Richards. Mr. Richards, a native Australian, worked at Ernst & Whinney in Sydney, Australia for six (6) months in 1987 before joining CA Australia in May 1988 as a Technical Support Analyst. Mr. Richards then moved into CA's Pre-Sales Department in 1989, and began working in the Sales Department in 1990, where he worked until 1998. Mr. Richards moved to the U.S. in April 1998 when he became the General Manager of Sales for the Northeastern and South Central U.S. regions. In April 1999, Mr. Richards was promoted to head of North American Sales, and on February 29, 2000, Mr. Richards became the head of Worldwide Sales. Mr. Richards resigned from CA on April 26, 2004. *See* CA Press Release, CA Announces Interim CEO and New COO (Apr. 26, 2004).

On September 17, 2004, Mr. Richards was indicted on nine (9) counts of securities fraud and obstruction of justice for his role in directing the 35-Day Month practice at CA, and then covering it up. *See* Kumar/Richards Indictment ¶¶ 18-20, 22-23, 25-27, 29-31, 33-40, 42-47, 49-50, 60-63, 69-81, 84-96. On June 29, 2005, the USAO filed a superseding indictment against Mr. Richards, which re-alleged eight (8) of the counts made against him in the original indictment and provided further factual details in support of those allegations. *See* Kumar/Richards Superseding Indictment ¶¶ 19-21, 23-28, 30-40, 44-49, 51-55, 63-64, 67-71, 77-89. On April 24, 2006, two (2) weeks before his criminal trial was set to begin, Mr. Richards (along with Mr. Kumar) pled guilty to all of the charges lodged against him in the superseding indictment. *See* Kumar/Richards Plea Tr. at 75-83.

On September 22, 2004, the SEC filed a complaint against Mr. Richards. The SEC complaint alleged that Mr. Richards furthered the 35-Day Month practice by: (i) participating with other CA executives in the practice of extending CA's fiscal quarters until CA had reached a predetermined revenue target; (ii) instructing and allowing subordinates to negotiate and obtain contracts after the quarter-end while knowing or recklessly disregarding the fact that CA would improperly recognize the revenue from those contracts; (iii) knowingly or recklessly failing to alert CA's Finance or Sales Accounting departments that CA salespersons under Mr. Richards were obtaining contracts with backdated signature dates after the quarter-end; and (iv) obstructing the investigation of CA's outside counsel, CA's Audit Committee, and the government. *See* Kumar/Richards SEC Complaint ¶¶ 3, 40-54.

On June 14, 2006, the SEC and Mr. Richards entered a partial consent judgment whereby Mr. Richards consented, without admitting or denying the allegations against him, to a final judgment that permanently enjoins him from (i) violating the federal securities laws, and (ii) serving as an officer or director of a public company. *See* Judgment Imposing a Permanent Injunction and Other Equitable Relief by Consent Against Defendant Stephen Richards at 1-4, *S.E.C. v. Sanjay Kumar & Stephen Richards*, 04 Civ. 4104 (ILG) (E.D.N.Y. June 14, 2006). The SEC and Mr. Richards have not yet reached agreement on the monetary penalty that Mr. Richards will be required to pay.

On November 14, 2006, Mr. Richards was sentenced to seven (7) years imprisonment. In connection with his sentencing, the SLC submitted a letter to the Court informing it of Mr. Richards' failure to cooperate in the SLC's investigation, which, in the SLC's view, evidenced his continuing failure to make any attempt to ameliorate the immense harm he has caused to CA, and its core constituents, including its employees, customers, shareholders, and suppliers. *See* Letter from William McCracken and Renato Zambonini to the Honorable I. Leo Glasser (Oct. 24, 2006). Following his sentencing, Mr. Richards agreed to cooperate with the SLC's investigation, and was interviewed by the SLC on December 22, 2006.

Based on his admitted knowing and intentional criminal conduct, the SLC has directed the Company to pursue claims against Mr. Richards for breach of fiduciary duty (count three); restitution and unjust enrichment (count four); fraud (count six); violation of § 14(a) of the Exchange Act (count seven); and indemnification (count nine). The SLC has begun a discussion with Mr. Richards' counsel concerning a settlement of the Company's claims against him, and expects that a settlement will be reached shortly after Mr. Richards' criminal restitution obligation is determined.

David Rivard. Mr. Rivard, a certified public accountant, began his career as an auditor at E&Y from 1989 to August 1998. During that time, E&Y was CA's independent auditor, and Mr. Rivard made his initial contact with CA in 1991 when working on the CA audit. Mr. Rivard was involved with every E&Y audit of CA from 1991 through 1998, and was the Audit Senior Manager in charge of the day-to-day operations of E&Y's fiscal year 1998 audit of CA. Mr. Rivard joined CA in August 1998 as the Vice President of Sales Accounting at the invitation of Ira Zar, who had recently been appointed CA's CFO. On September 7, 2001, Mr. Rivard became the Vice President of Finance. On October 7, 2003, Mr. Rivard resigned from CA at the request of the Audit Committee and Mr. Kumar. *See* Press Release, Computer Assocs. Int'l, Inc., Computer Associates Announces Preliminary Results of Board Inquiry (Oct. 8, 2003).

On April 8, 2004, Mr. Rivard pled guilty to one (1) federal criminal count each of: (i) conspiracy to obstruct justice, and (ii) conspiracy to commit securities fraud. *See* Transcript of Plea at 28-34, *United States v. David Rivard*, Cr. No. 04-329 (ILG) (E.D.N.Y.

April 8, 2004) ("Rivard Plea Tr."). On January 30, 2007, Mr. Rivard was sentenced to four (4) months of home detention and three (3) years of supervised release. Also on April 8, 2004, the SEC filed a complaint against Mr. Rivard alleging that he violated various federal securities laws. *See* Complaint ¶¶ 20-32, *S.E.C. v. David Rivard*, 04 Civ. 1464 (ILG) (E.D.N.Y. Apr. 8, 2004) ("Rivard SEC Complaint"). Specifically, the SEC complaint alleged that Mr. Rivard (i) acted as CA's signatory on many backdated contracts; (ii) himself backdated the date of his signature of many contracts (iii) disseminated information throughout CA which furthered the 35-Day Month practice; and (iv) directed the alteration of records to hide the 35-Day Month practice from outside auditors. *Id.* ¶ 20.

On November 1, 2004, the SEC and Mr. Rivard entered into a final consent judgment whereby he consented, without admitting or denying the allegations against him, to a final judgment that required him to disgorge $83,700 in ill-gotten gains and interest and imposed a $75,000 civil penalty. *See* Final Judgment by Consent Against Defendant David Rivard at 5, *S.E.C. v. David Rivard*, 04 Civ. 1464 (ILG) (E.D.N.Y. Nov. 1, 2004). As a result of that judgment, Mr. Rivard is permanently enjoined from (i) violating the federal securities laws, and (ii) serving as an officer or director of a public company.

As part of its investigation, the SLC interviewed Mr. Rivard on June 22 and June 29, 2006. On January 30, 2007, Mr. Rivard was sentenced to four (4) months home detention followed by three (3) years supervised release. In connection with Mr. Rivard's sentencing, the SLC submitted a letter to the Court advising it of his cooperation in the SLC's investigation, which, in the SLC's view, evidenced his attempt at ameliorating the immense harm that his criminal conduct has caused CA. *See* Letter from William McCracken and Renato Zambonini to the Honorable I. Leo Glasser (Jan. 26, 2007).

Based on his admitted knowing and intentional criminal conduct, the SLC has directed the Company to pursue claims against Mr. Rivard for breach of fiduciary duty (count three); restitution and unjust enrichment (count four); fraud (count six); violation of § 14(a) of the Exchange Act (count seven); and indemnification (count nine). The SLC has begun a discussion with Mr. Rivard's counsel concerning a settlement of the Company's claims against him, and expects that a settlement will be reached shortly after Mr. Rivard's criminal restitution obligation is determined.

Lloyd Silverstein. Prior to joining CA, Mr. Silverstein worked as an accountant at Holtz Rubenstein & Co. from 1977 to 1982. From 1982 to 1988, Mr. Silverstein worked as a controller and CFO at Microwave Power Devices. Mr. Silverstein began his CA career in 1988 as the Director of Finance, and held that position until 1993, when he moved to Sales Accounting. In 1997, Mr. Silverstein became head of Sales Accounting, and from October 1998 to October 2001, Mr. Silverstein was Vice President in charge of the Global Sales Organization, a department that served as a liaison between the Finance, Sales, and Legal departments. In October 2001, Mr. Silverstein moved to the Strategic Licensing and Pricing department. On October 7, 2003, Mr. Silverstein resigned from CA at the request of the Audit Committee and Mr. Kumar. *See* Press Release, Computer Assocs. Int'l, Inc., Computer Associates Announces Preliminary Results of Board Inquiry (Oct. 8, 2003).

On January 22, 2004, Mr. Silverstein pled guilty to one (1) federal criminal count of conspiracy to obstruct justice. *See* Transcript of Arraignment & Pleading at 6-9, 15, 19-21, *United States v. Lloyd Silverstein*, Cr. No. 04-0024 (ILG) (E.D.N.Y., Jan. 22, 2004) ("Silverstein Plea Tr."). Also on January 22, 2004, the SEC filed a complaint against Mr. Silverstein alleging violations of various federal securities laws. Complaint ¶¶ 28-39, *SEC v.*

Lloyd Silverstein, 04 Civ. 255 (ILG) (E.D.N.Y. Jan. 22, 2004) ("Silverstein SEC Complaint"). Specifically, the SEC complaint alleged, among other things, that Mr. Silverstein and others at CA "engaged in a practice in which CA held its books open after the end of each quarter and improperly recorded, in that elapsed quarter, revenue from the contracts that had not been finalized and executed before the expiration of the quarter." *Id.* ¶ 1. At that time, Mr. Silverstein entered into a partial consent judgment whereby he consented, without admitting or denying the allegations against him, to a final judgment that permanently enjoins him from (i) violating the federal securities laws, and (ii) serving as an officer or director of a public company. *See* Partial Final Judgment Imposing a Permanent Injunction and Other Equitable Relief by Consent Against Defendant Lloyd Silverstein at 2-4, *S.E.C. v. Lloyd Silverstein*, 04 Civ. 255 (E.D.N.Y. Jan. 30, 2004). The SEC and Mr. Silverstein have not yet reached agreement on a monetary penalty that Mr. Silverstein will be required to pay.

As part of its investigation, the SLC interviewed Mr. Silverstein on October 13, 2006. On January 31, 2007, Mr. Silverstein was sentenced to six (6) months home detention followed by three (3) years supervised release. In connection with Mr. Silverstein's sentencing, the SLC submitted a letter to the Court advising it of his cooperation in the SLC's investigation, which, in the SLC's view, evidenced his attempt to ameliorate the immense harm that his criminal conduct has caused CA. *See* Letter from William McCracken and Renato Zambonini to the Honorable I. Leo Glasser (Jan. 30, 2007).

Based on his admitted knowing and intentional criminal conduct, the SLC has directed the Company to pursue claims against Mr. Silverstein for breach of fiduciary duty (count three); restitution and unjust enrichment (count four); fraud (count six); violation of § 14(a) of the Exchange Act (count seven); and indemnification (count nine). The SLC has begun a discussion with Mr. Silverstein's counsel concerning a settlement of the Company's claims against him, and expects that a settlement will be reached shortly after Mr. Silverstein's criminal restitution obligation is determined.

Steven Woghin. Mr. Woghin graduated from the University of Michigan Law School in 1971. Upon graduation, he worked as an attorney for the U.S. Postal Service for one year. From 1972 to 1982, Mr. Woghin worked as an attorney in the anti-trust division of the Department of Justice. From 1982 to 1985, Mr. Woghin worked as a Special Assistant U.S. Attorney in the Eastern District of Virginia. In 1985, Mr. Woghin left the U.S. Attorney's Office for the private sector, working first for a small firm in New York City, and then later as a partner specializing in litigation at Arter & Hadden LLP in Dallas, Texas.

At Arter & Hadden, Mr. Woghin developed a relationship with Mr. Kumar, who was then at Uccel Corp., when Mr. Woghin represented Uccel in several litigations. After CA acquired Uccel in 1987, Mr. Woghin was asked to represent CA in several litigation matters. Mr. Woghin developed a business relationship with CA over time, and joined CA in 1992 as a Vice President in the Legal department. He remained in that position until Mr. Kumar, unsolicited by Mr. Woghin, offered him the position of Senior Vice President and General Counsel in 1995, which he accepted. Mr. Woghin was fired from CA by Mr. Kumar on April 8, 2004.

On September 22, 2004, Mr. Woghin pled guilty to one (1) federal criminal count each of: (i) obstruction of justice, and (ii) conspiracy to commit securities fraud. *See* Transcript of Plea at 13-16, 23, 28-30, *United States v. Steven Woghin*, Cr. No. 04-847 (ILG) (E.D.N.Y. Sept. 22, 2004) ("Woghin Plea Tr."). Also on September 22, 2004, the SEC filed a complaint against Mr. Woghin alleging that he violated various federal securities laws. *See*

Complaint ¶¶ 4, 37-54, *S.E.C. v. Steven Woghin*, 04 Civ. 4087 (ILG) (E.D.N.Y. Sept. 22, 2004) ("Woghin SEC Complaint"). Specifically, the SEC complaint alleged, among other things, that Mr. Woghin furthered the 35-Day Month practice by: (i) signing materially false and misleading financial statements; (ii) approving backdated contracts, including drafting a contract with a misleading date; and (iii) allowing CA's Legal department to approve contracts while knowing or recklessly disregarding the fact that the contracts contained false and misleading signature dates. *Id.* ¶ 2. At that time, Mr. Woghin entered into a partial consent judgment whereby he consented, without admitting or denying the allegations against him, to a final judgment that permanently enjoins him from (i) violating the federal securities laws, and (ii) serving as an officer or director of a public company. *See* Partial Final Judgment Imposing a Permanent Injunction and Other Equitable Relief by Consent Against Defendant Steven Woghin at 1-5, *S.E.C. v. Steven Woghin*, 04 Civ. 4087 (ILG) (E.D.N.Y. Sept. 30, 2004). The SEC and Mr. Woghin have not yet reached agreement on a monetary penalty that Mr. Woghin will be required to pay.

As part of its investigation, the SLC interviewed Mr. Woghin on July 31, 2006 and November 15, 2006. On January 16, 2006, Mr. Woghin was sentenced to two (2) years imprisonment. In connection with Mr. Woghin's sentencing, the SLC submitted a letter to the Court advising it of his cooperation in the SLC's investigation, which, in the SLC's view, evidenced his attempt to ameliorate the immense harm that his criminal conduct has caused CA. *See* Letter from William McCracken and Renato Zambonini to the Honorable I. Leo Glasser (Jan.12, 2007).

Based on his admitted knowing and intentional criminal conduct, the SLC has directed the Company to pursue claims against Mr. Woghin for breach of fiduciary duty (count three); restitution and unjust enrichment (count four); fraud (count six); violation of § 14(a) of the Exchange Act (count seven); indemnification (count nine). The SLC has begun a discussion with Mr. Woghin's counsel concerning a settlement of the Company's claims against him, and expects that a settlement will be reached shortly after Mr. Woghin's criminal restitution obligation is determined.

Ira Zar. Mr. Zar began his business career at CA in 1982 upon graduation from Baruch College. Although not a CPA, between 1982 and 1994, Mr. Zar worked in various financial-related positions at CA, including Controller, International Controller, manager of Financial Reporting, and head of Sales Accounting. In April 1994, Mr. Zar became Senior Vice President of Finance, as well as Treasurer. On June 22, 1998, Mr. Zar was appointed CFO following the resignation of Peter Schwartz. On October 7, 2003, Mr. Zar resigned from CA at the request of the Audit Committee and Mr. Kumar. *See* Press Release, Computer Assocs. Int'l, Inc., Computer Associates Announces Preliminary Results of Board Inquiry (Oct. 8, 2003).

On April 8, 2004, Mr. Zar pled guilty to one (1) federal criminal count each of: (i) conspiracy to obstruct justice, (ii) securities fraud, and (iii) conspiracy to commit securities fraud. *See* Transcript of Plea at 18-23, 33-39, *United States v. Ira Zar*, Cr. No. 04-331 (ILG) (E.D.N.Y. Apr. 8, 2004) ("Zar Plea Tr.").

Also on April 8, 2004, the SEC filed a complaint against Mr. Zar alleging that he violated various federal securities laws. The SEC complaint alleged that Mr. Zar: (i) oversaw and implemented the 35-Day Month practice; (ii) backdated contracts; (iii) oversaw the preparation and filing of false and misleading SEC filings; and (iv) obstructed the investigation of CA's outside counsel, CA's Audit Committee, and the government. *See* Complaint ¶¶ 20-35, *S.E.C. v. Ira Zar*, 04 Civ. 1463 (E.D.N.Y. Apr. 9, 2004). At that time, Mr. Zar entered into a partial consent judgment whereby he consented, without admitting or denying the allegations against him, to a final judgment that permanently enjoins him from (i) violating the federal securities laws, and (ii) serving as an officer or director of a public company. *See* Partial Final Judgment Imposing a Permanent Injunction and Other Equitable Relief by Consent Against Defendant Ira Zar at 1-5, *S.E.C. v. Ira Zar*, 04 Civ. 1463 (E.D.N.Y. Apr. 9, 2004). The SEC and Mr. Zar have not yet reached agreement on a monetary penalty that Mr. Zar will be required to pay.

As part of its investigation, the SLC interviewed Mr. Zar on July 28, 2006 and November 15, 2006. On January 26, 2007, Mr. Zar was sentenced to seven (7) months imprisonment followed by seven (7) months home detention. In connection with Mr. Zar's sentencing, the SLC submitted a letter to the Court advising it of his cooperation in the SLC's investigation, which, in the SLC's view, evidenced his attempt to ameliorate the immense harm that his criminal conduct has caused CA. *See* Letter from William McCracken and Renato Zambonini to the Honorable I. Leo Glasser (Jan. 24, 2007).

Based on his admitted knowing and intentional criminal conduct, the SLC has directed the Company to pursue claims against Mr. Zar for breach of fiduciary duty (count three); restitution and unjust enrichment (count four); fraud (count six); violation of § 14(a) of the Exchange Act (count seven); and indemnification (count nine). The SLC has begun a discussion with Mr. Zar's counsel concerning a settlement of the Company's claims against him, and expects that a settlement will be reached shortly after Mr. Zar's criminal restitution obligation is determined.

2. **Former Officer Defendants**

The following defendants served as officers at CA during the period in which the fraud occurred, but have not been criminally indicted by USAO or sued by the SEC.

Michael McElroy. Mr. McElroy graduated from New York University Law School in 1969. Upon graduation, Mr. McElroy worked as an associate at a small law firm named Valicenti Leighton Reid & Pine. In 1975, when the Valicenti firm dissolved, Mr. McElroy joined another small firm called Burke & Burke Daniels Leighton & Reid ("Burke & Burke"), at which Tony Wang (Charles Wang's brother) and Arnold Mazur, both of whom later became senior CA executives, were partners. Mr. McElroy worked at Burke & Burke until 1987, when the firm merged to become Satterlee, Stephens, Burke & Burke.

In January 1988, Tony Wang offered Mr. McElroy a position in CA's New York office as a Vice President in the Legal department, which he accepted. Mr. McElroy was promoted to the position of Senior Vice President in the Legal department in 1989. He served as the Company's Corporate Secretary from April 1988 to April 1991, and from January 1997 to October 22, 2002.[28] As a lawyer at CA, Mr. McElroy reported to Mr. Woghin, and was unofficially known as CA's senior licensing attorney. On April 19, 2004, Mr. McElroy was fired from CA for cause. As part of its investigation, the SLC interviewed Mr. McElroy on July 27, 2006.

As described further below, the SLC, in the exercise of its business judgment, has determined that dismissal of the claims alleged against Mr. McElroy in the 2005 Derivative Complaint is in the best interests of CA. The SLC has received and reviewed a sworn financial statement prepared by Mr. McElroy which evidences that Mr. McElroy's net worth (excluding protected retirement assets) is less than $500,000, and concludes that the costs of litigation against him, including its obligations to advance legal fees and costs under Delaware law, outweigh any possible recovery that it may obtain. Moreover, Mr. McElroy, while a senior

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28 The last Board meeting that Mr. McElroy attended as Corporate Secretary was October 22, 2002.

lawyer, was not involved with or responsible for revenue recognition or financial reporting decisions. Thus, as a matter of economic resource allocation and fairness, the SLC has determined, in the exercise of its business judgment, to seek dismissal of the claims against Mr. McElroy.

Charles McWade. Prior to joining CA, Mr. McWade worked at Ernst & Whinney from 1969 to 1983, where he ultimately became a partner. After CA became a public company in 1981, the Company hired E&Y as its outside auditor, and Mr. McWade worked on the CA audit. Mr. McWade joined CA in July 1983, after he was offered a position by Tony Wang and Abraham Poznanski, CA's then-CFO. Mr. McWade served as CA's Treasurer and in other senior financial positions until 1994. From 1994 to 1997, Mr. McWade served as head of the Financial Reporting department, and from 1998, until he resigned on April 2, 2001, Mr. McWade was a Senior Vice President in charge of development, primarily responsible for mergers and acquisitions. From July 2001 to July 2006, Mr. McWade served as a consultant to CA, assisting with, among other things, tax matters. As part of its investigation, the SLC interviewed Mr. McWade on August 16, 2006.

As described above, the SLC has reached a settlement with Mr. McWade, pursuant to which Mr. McWade will pay the Company $1 million, and the Company will seek dismissal of all claims against him.

Peter Schwartz. After graduating from Yale University in 1965, Mr. Schwartz served as a fighter pilot in the Marine Corps from 1965 to 1974. From 1974 to 1976, Mr. Schwartz worked at the National Institute for the Deaf, following which he worked in the Internal Audit department of the Xerox Corporation from 1976 to 1983. In 1983, Tony Wang, whom Mr. Schwartz knew from Yale, offered Mr. Schwartz a position in the Finance department at CA. Mr. Schwartz accepted the offer and served as a Vice President of Finance from 1983 to 1985, at which time he was appointed CFO, a position he held until his resignation on June 22, 1998.[29] As part of its investigation, the SLC interviewed Mr. Schwartz on August 1, 2006.

As described further below, the SLC has determined that Mr. Schwartz was aware of, and participated in, the 35-Day Month practice while a senior officer at CA, and is therefore liable to CA for the losses it sustained on account of his actions. As such, the SLC has directed the Company to pursue claims against Mr. Schwartz for breach of fiduciary duty (count three); restitution and unjust enrichment (count four); fraud (count six); and indemnification (count nine).

3. Oversight Director Defendants

The following director defendants served on the CA Board during the period in which the 35-Day Month practice occurred. As described above, the 2005 Derivative Complaint and the Kaufman Complaint allege that Oversight Director Defendants breached their fiduciary duties to CA by failing to properly oversee CA (i) during the period of fraudulent conduct, and (ii) during the government investigation into the Company's accounting practices.

Russell Artzt. Mr. Artzt co-founded CA in 1976 with Charles Wang, whom he met in a math class at Queens College, and Mr. Artzt remains employed by the Company in a senior development position to this day. From 1976 to 1987, Mr. Artzt was CA's Senior Development Officer. From 1987 to 2002, Mr. Artzt was Executive Vice President of Research and Development. From 2002 to 2005, Mr. Artzt was Executive Vice President of Alliances

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29 The SLC has concluded that after his resignation as CFO, Mr. Schwartz continued at CA in an executive officer position through the summer of 1998; Mr. Schwartz also served as a consultant to CA through March 31, 2003.

and eTrust Solutions. Mr. Artzt is currently Executive Vice President in charge of products at CA.

Mr. Artzt was a member of the CA Board from November 1980 to August 24, 2005, when the CA Board determined to limit the number of management directors. Mr. Artzt served on the Corporate Operations Committee (formerly known as the Executive Committee) from 1987 to August 24, 2005. Mr. Artzt, along with Messrs. Wang and Kumar, were recipients under the KESOP, with Mr. Artzt receiving ten percent (10%) of the shares issued.

Mr. Artzt was interviewed by the SLC on June 28, 2006 and March 8, 2007. As a result of these interviews and its investigation, the SLC concluded that Mr. Artzt was unjustly enriched by the KESOP. As a result, the SLC has reached an agreement in principle to settle all claims against Mr. Artzt in exchange for the payment to CA of $9 million (the cash equivalent of 354,890 CA shares). This settlement agreement will be presented to the Court for approval as part of an omnibus motion. The SLC notes that during its investigation, it did not uncover evidence that Mr. Artzt directed or participated in the 35 Day-Month practice or was involved in the preparation or dissemination of the financial statements that led to the KESOP's accelerated vesting.

Alfonse D'Amato. Mr. D'Amato has been a member of the CA Board since June 29, 1999. Mr. D'Amato was invited to join the Board by Charles Wang, CA's then-Chairman and CEO. He has served on the Audit Committee and Corporate Governance Committee (formerly known as the Nominating Committee) since joining the CA Board. Mr. D'Amato was a member of the Compensation and Human Resource Committee (formerly known as the Stock Option and Compensation Committee) from August 25, 1999 to August 29,

2001. In August 2003, Mr. D'Amato served as chair of the committee that considered the settlement of the Class Actions.

Prior to joining the Board, Mr. D'Amato served three (3) terms in the United States Senate, from 1981 to 1999, as a Senator from the state of New York. While in the Senate, Mr. D'Amato served as Chair of the Senate Committee on Banking, Housing and Urban Affairs and the Commission on Security and Cooperation in Europe. After leaving the Senate, Mr. D'Amato was a director of Avis Rent-a-Car, Inc., later Avis Group Holdings, Inc., from 1999 to 2001, and an advisor director for Newtek Capital in 2002. He has served as a director of Signature Bank since 2005. Since 1999, Mr. D'Amato has been Managing Director of Park Strategies LLC, a consultancy and lobbying firm he founded with Wayne Berman, former assistant Secretary of Commerce for policy under President George H.W. Bush.

As part of its investigation, the SLC interviewed Mr. D'Amato on July 21, 2005, September 27, 2006, and March 8, 2007. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. D'Amato.

Willem de Vogel. Mr. de Vogel served as a member of the CA Board from August 1981 until August 1990, and then again from October 22, 1991 to August 28, 2002, when his term as a director expired and the Board imposed an eight-year limit for service as a director. Mr. de Vogel first became involved with CA when an affiliated entity invested in the Company in 1977. After CA became a public company in 1981, Tony Wang, Charles Wang's brother, asked Mr. de Vogel to join the CA Board. Mr. de Vogel served as a member of the Compensation and Human Resource Committee (formerly known as the Stock Option and Compensation Committee) from 1982 to August 1990, and from 1991 to August 28, 2002. Mr.

de Vogel was a member of the Audit Committee from March 1986 to August 8, 1990, and from October 1991 to August 28, 2002.

Mr. de Vogel has also served as a director of Morton Industrial Group, Inc. (formerly MLX Corp.) from 1986 to 2002 and as a director of Pameco Corp. from 1999 to 2001. Mr. de Vogel has served, and continues to serve, as a director of Factory 2-U Stores Inc. (since 2000) and Classic Vacation Group Inc. (since 2001). Mr. de Vogel has been President of Three Cities Research, Inc., a private equity firm, since 1982.

As part of its investigation, the SLC interviewed Mr. de Vogel on August 15, 2006. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. de Vogel.

Richard Grasso. Mr. Grasso served as a member of the CA Board from January 20, 1994 until August 28, 2002, when his term as a director expired and the Board imposed an eight-year limit for service as a director. Mr. Grasso became acquainted with CA in 1986 when CA was first listed on the NYSE, where he was employed. In late 1993, Charles Wang, who knew Mr. Grasso from the Company's affiliation with the NYSE, approached Mr. Grasso and asked him to join the CA Board. Mr. Grasso served as a member of the Compensation and Human Resource Committee (formerly known as the Stock Option and Compensation Committee) from 1994 to August 28, 2002 and the Corporate Governance Committee (formerly known as the Nominating Committee) from May 1996 to July 11, 2002.

Prior to joining the Board, Mr. Grasso was a floor clerk at the NYSE beginning in 1968, and spent the next thirty-five (35) years at the NYSE, where he rose through the ranks of the organization. Mr. Grasso served as President and COO of the NYSE from 1988 to 1995, as Executive Vice Chairman from 1991 to 1995, and as Chairman and CEO from 1995 to 2003. Mr. Grasso resigned from his position at the NYSE on September 17, 2003.

As part of its investigation, the SLC interviewed Mr. Grasso on September 25, 2006. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. Grasso.

Shirley Strum Kenny. Dr. Kenny served as a member of the CA Board from July 1994 to August 28, 2002, when her term as a director expired and the Board imposed an eight-year limit for service as a director. Dr. Kenny joined the Board in 1994 at the request of Mr. Wang and Irving Goldstein, both of whom she knew as graduates of Queens College of the city of New York, where she was then serving as President. Dr. Kenny served as a member of the Audit Committee from 1995 to August 28, 2002, and as the Audit Committee's Chair from June 6, 2000 to May 14, 2002, at which time Walter Schuetze, who had recently joined the Board, was appointed as Chair. Dr. Kenny also served as a member of the Corporate Governance Committee (formerly known as the Nominating Committee) from May 1996 to August 28, 2002.

Prior to joining the CA Board, from 1989 to August 1994, Dr. Kenny served as President of Queens College. At that time, Dr. Kenny resigned that position to become President of the State University of New York at Stony Brook ("SUNY Stony Brook"), in which capacity she has served since September 1994. Dr. Kenny served as a director of Toys R' Us Inc. from 1990 to 2002.

As part of its investigation, the SLC interviewed Dr. Kenny on June 30, 2006 and November 17, 2006. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Dr. Kenny.

Roel Pieper.[30] Mr. Pieper served as a member of the CA Board from March 1, 1999 to August 28, 2002, when he resigned following Mr. Wang's retirement. Mr. Pieper was invited to join the Board by Mr. Wang, whom Mr. Pieper knew personally, and Mr. de Vogel. Mr. Pieper served as a member of the Compensation and Human Resource Committee (formerly known as the Stock Option and Compensation Committee) from August 25, 1999 to August 28, 2002.

Prior to joining the Board, Mr. Pieper worked in various managerial positions at Software AG from 1981 to 1988. From 1988 to 1989, he served as a Senior Vice President in the Technology Division of Software AG, and from 1989 to 1990, he served as its Chief Technology Officer. From 1991 to 1993, he served as the Chief Executive Officer of AT&T's Unix System Laboratories. From 1993 to 1995, he served as the Chairman and CEO of UB Networks, Inc. and from 1995 to 1997 he served as the CEO of Tandem Computers. From 1997 to 1998, Mr. Pieper served as a Senior Vice President and General Manager of Worldwide Sales and Marketing at Compaq Computer Corp. From 1998 to 1999, Mr. Pieper was a member of the Board of Management and an Executive Vice President of Technology, Strategy and Planning at Royal Philips Electronics, N.V. Mr. Pieper has been a General Partner of Insight Capital Partners since 1999, and Managing Director at Favonius Insight Ventures since 2001.

Mr. Pieper has also served as a director of numerous public companies, including General Magic, Inc. from 1996 to 2000; Quokka Sports Inc. from 1997 to 2000; Unify Corp. from 1997 to 1998; Nextlevel Systems Inc. from 1997 to 1998; General Instrument Corp. from 1997 to 1998 (Chairman); Lernout & Hauspie Speech Products from 1999 to 2001

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[30] Mr. Pieper was named as a defendant in the 2005 Derivative Complaint, but was not named in the Kaufman Complaint.

(Chairman); New Media Industries PLC from 2000 to 2002; and Nutri Pharma ASA from 2001 to 2002 (Chairman). Mr. Pieper has also served, and continues to serve, as a director of Viewsoft, Inc. (since 1995); Kaspia Systems, Inc. (since 1995); Smart Valley Inc. (since 1995); Stonehenge Telecom N.V. (since 1999); as Chairman of Ring! N.V. (since 2001); Oblicore Inc. (since 2004); and as Chairman of LB Icon AB (since 2004).

As part of its investigation, the SLC interviewed Mr. Pieper on August 27, 2006 and March 20, 2007. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. Pieper.

Charles Wang. Mr. Wang co-founded CA in 1976 with Russell Artzt, and served as CA's CEO from 1976 to August 4, 2000, and as its Chairman from April 1980 to November 15, 2002. Prior to founding CA in 1976, Mr. Wang was the Vice President of Sales for Standard Data Corp. Mr. Wang currently owns the New York Islanders hockey team and is the co-owner of the New York Dragons arena football team. Mr. Wang is also involved in several real-estate ventures on Long Island, New York, including plans to develop the area surrounding the Nassau Coliseum in Uniondale.

As noted above, Mr. Wang was Chairman and CEO during much of the period when CA was engaging in a widespread revenue recognition fraud. The SLC has uncovered credible and corroborated evidence that Mr. Wang was aware of, and was an active participant in, the 35-Day Month practice, during which he, among other things (i) directed his subordinates to obtain additional revenue after the close of quarters to be counted in the prior quarter, and (ii) negotiated and participated in the negotiation of deals that he knew to be backdated. In addition, Mr. Wang is the only former member of CA's Board that has refused to unconditionally and fully cooperate with the SLC's investigation, despite having been offered numerous opportunities to do so.

Based on the foregoing, the SLC has directed that the Company pursue claims against Mr. Wang for breach of fiduciary duty (count three); restitution and unjust enrichment (count four); corporate waste (count five); fraud (count six); violation of Section 14(a) of the Exchange Act (count seven); and indemnification (count nine).

4. **Settlement Director Defendants**

In August 2003, the following directors served on the committee that considered the settlement of the Class Actions and/or the committee that considered the settlement of the 2003 Derivative Action.[31] As described above, the 2005 Derivative Complaint and the Kaufman Complaint allege that the Settlement Director Defendants breached their fiduciary duties to CA by (i) failing to properly oversee CA during the government investigation into the Company's accounting practices, and (ii) improperly approving the 2003 Settlement. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against the Settlement Director Defendants.

Kenneth Cron. Mr. Cron served as a member of the CA Board from June 15, 2002 to September 18, 2006, when the Board determined to limit the number of management directors. Mr. Cron served as CA's interim CEO from April 26, 2004 to February 9, 2005, following Mr. Kumar's resignation. Mr. Cron also served on the Compensation and Human Resource Committee from August 28, 2002 to April 23, 2004. In August 2003, Mr. Cron served on the committee that considered the settlement of the 2003 Derivative Action.

31 As mentioned above in the section detailing the Oversight Director Defendants, Alfonse D'Amato served as Chair of the Committee that considered the settlement of the Class Actions. Hereinafter, Mr. D'Amato is included in references to both the Oversight Director Defendants and the Settlement Director Defendants, unless otherwise noted.

Prior to joining the Board, Mr. Cron worked as a Division President at CMP Media Inc. from 1978 to 1999. He has also served as Chairman and CEO of Uproar Inc. from September 1999 to March 2001 (Chairman and CEO). From March 2001 to April 2004, he served as Chairman and CEO of Vivendi Universal Games, Inc., and has served as the Chairman of Midway Games, Inc. since June 2004.

As part of its investigation, the SLC interviewed Mr. Cron on June 22, 2005 and July 14, 2006. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. Cron.

Gary Fernandes. Mr. Fernandes has been a member of the CA Board since May 16, 2003.[32] Mr. Fernandes was first asked to join the CA Board by Mr. Kumar in 2002, but Mr. Fernandes declined the offer because of non-competition arrangements with his former employer, Electronic Data Systems, Inc. ("EDS"). In 2003, EDS consented to Mr. Fernandes joining the CA Board. Mr. Fernandes has served as a member of the Compensation and Human Resource Committee since August 27, 2003, and has been Chair of the Strategy Committee since August 9, 2006. In August 2003, Mr. Fernandes served on the committee that considered the settlement of the 2003 Derivative Action.

Prior to joining the Board, Mr. Fernandes worked at EDS, and, over the course of a twenty-nine (29) year career starting in 1969, rose from the position of systems engineer to Vice Chairman. Mr. Fernandes has also served as a director of numerous public companies, including John Wiley & Sons Inc. from 1989 to 2000; Southland Corp. from 1991 to 1995; Groceryworks.com from 2000 to 2002 (Chairman); Anacomp Inc. from 2003 to 2005; and webMethods, Inc. from 2002 to 2005. Mr. Fernandes has served, and continues to serve, as a

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32 Mr. Fernandes attended the May 13, 2003 CA Board meeting as a "guest of the Board." Minutes of a Meeting of the CA Board at 1 (May 13, 2003). At that meeting, it was resolved that he would be elected a director of the Company effective May 16, 2003.

director of 7-Eleven Inc. (since 1999); Blockbuster Inc. (since 2004); and BancTec Inc. (since 2006).

As part of its investigation, the SLC interviewed Mr. Fernandes on July 27, 2005 and July 11, 2006. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. Fernandes.

Robert La Blanc. Mr. La Blanc has been a member of the CA Board since July 15, 2002. Mr. La Blanc was invited to join the Board after meeting with Mr. Kumar, Mr. Wang, and CA director Lewis Ranieri, whom Mr. La Blanc knew as a fellow former executive of Salomon Brothers Inc. Mr. La Blanc served on the Compensation and Human Resource Committee from August 28, 2002 to August 27, 2003. Mr. La Blanc has served on the Corporate Governance Committee since August 28, 2002 and the Audit Committee since May 26, 2004. In August 2003, Mr. La Blanc served on the committee that considered the settlement of the 2003 Derivative Action.

Prior to joining the Board, from 1969 to 1979, Mr. La Blanc was a general partner of Salomon Brothers. Mr. La Blanc then founded Robert E. La Blanc Associates, Inc., where he has held the position of President since 1981. Mr. La Blanc has served as a director of numerous public companies, including Storage Technology Corp. from 1979 to 2004; Gilbert Associates Inc. in 1997; Salient 3 Communications, Inc. from 1997 to 2003; Tribune Co. from 2000 to 2001; and Avatech Solutions, Inc. from 2004 to 2005. Mr. La Blanc has served, and continues to serve, as a director of the Titan Corporation (since 1996); Chartered Semiconductor Manufacturing Ltd. (since 1998); and FiberNet Telecom Group, Inc. (since 2003). Mr. La Blanc is also currently a director of a family of Prudential Mutual Funds.

As part of its investigation, the SLC interviewed Mr. La Blanc on July 27, 2005 and July 13, 2006. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. La Blanc.

Jay Lorsch. Mr. Lorsch has been a member of the CA Board since April 1, 2002. Mr. Lorsch was invited to join the Board as part of Mr. Kumar's claimed effort to promote CA as the "gold standard" in corporate governance. Mr. Lorsch has served as (i) Chair of the Corporate Governance Committee since July 11, 2002, (ii) a member of the Corporate Operations Committee since August 28, 2002, and (iii) a member of the Compensation and Human Resource Committee since May 11, 2004. In August 2003, Mr. Lorsch served as (i) a member of the committee that considered the settlement of the Class Actions, and (ii) Chair of the committee that considered the settlement of the 2003 Derivative Action.

Mr. Lorsch has been on the faculty at the Harvard Business School since 1978, during which time he has served as the Louis Kirstein Professor of Human Relations. Mr. Lorsch has also served as a consultant to numerous Fortune 500 companies, and has served as a director of Brunswick Corp. from 1983 to 2003; Sandy Corp. from 1987 to 1996; and Benckiser N.V. from 1998 to 1999.

As part of its investigation, the SLC interviewed Mr. Lorsch on July 15, 2005 and July 20, 2006. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. Lorsch.

Lewis Ranieri. Mr. Ranieri has been a member of the CA Board since June 26, 2001. Mr. Ranieri joined the CA Board at the request of directors Alfonse D'Amato and Richard Grasso, both of whom Mr. Ranieri knew personally. Mr. Ranieri has served as (i) Chairman of the Board since April 21, 2004, following Mr. Kumar's resignation, (ii) Chair of the Compensation and Human Resource Committee (formerly known as the Stock Option and Compensation Committee) since August 29, 2001, and (iii) a member of the Strategy Committee since August 25, 2004. Mr. Ranieri served as lead independent director of the Board from May 14, 2002 to April 20, 2004, and as a member of the Audit Committee from January 21, 2003 to April 20, 2004. In August 2003, Mr. Ranieri served on the committee that considered the settlement of the Class Actions.

Prior to joining the Board, Mr. Ranieri was employed at Salomon Brothers Inc. from 1968 to 1987, where he rose to the position of Vice Chairman. Mr. Ranieri has served as a director of numerous public companies, including Bank United Corp. from 1988 to 2001 (Chairman); Delphi Financial Group Inc. from 1992 to 2003; Transworld Healthcare Inc. from 1997 to 2002; and Delphi International Ltd. from 1997 to 2002. Mr. Ranieri has served, and continues to serve, as Chairman of Franklin Bank Corp. (since 2001); as Chairman of American Financial Realty Trust (since 2002); as Chairman of Capital Lease Funding, Inc. (since 2003); and as a Director of Reckson Associates Realty Corp (since 1998). Mr. Ranieri has also served as Chairman, President and CEO of Ranieri & Co., Inc. since 1988, is the founder of Hyperion Partners L.P. and Hyperion Partners II L.P., and is Chairman or a director of various other Hyperion entities.

As part of its investigation, the SLC interviewed Mr. Ranieri on July 10, 2006 and March 1, 2007. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. Ranieri.

Walter Schuetze. Mr. Schuetze has been a member of the CA Board since April 1, 2002. Mr. Schuetze was asked to join the Board by Mr. Kumar in early 2002 as part of Mr. Kumar's claimed effort to promote CA as the "gold standard" in corporate governance. Mr.

Schuetze had previously performed consulting work for CA, at Mr. Kumar's request, by serving on a "blue-ribbon panel" to review CA's accounting practices in response to the April 29, 2001 New York Times article.

Mr. Schuetze has chaired CA's Audit Committee since May 14, 2002. As Chair of the Audit Committee, Mr. Schuetze was responsible for managing the internal investigation of the Company's accounting practices, which began in July 2003. In August 2003, Mr. Schuetze served as (i) a member of the committee that considered the settlement of the Class Actions, and (ii) a member of the committee that considered the settlement of the 2003 Derivative Action.

Prior to joining the Board, Mr. Schuetze joined Eaton & Huddle in 1957, which subsequently merged with Peat Marwick Mitchell & Co., the accounting firm that later became KPMG, where he was a partner. Mr. Schuetze left KPMG in 1973 to serve as a charter member of the Financial Accounting Standards Board ("FASB") until 1976, and then returned to work for KPMG from 1976 to 1992. Mr. Schuetze was also a member, and Chairman, of the Accounting Standards Executive Committee of the American Institute of Certified Public Accountants ("AICPA"). Mr. Schuetze served as the SEC's Chief Accountant from January 1992 to March 1995. From 1995 to 1997, Mr. Schuetze worked as an independent consultant. From November 1997 to February 2000, he served as the Chief Accountant at the SEC's Division of Enforcement. Mr. Schuetze has served as a director of Transmontaigne Inc. since 2002 and a director of NES Rentals Holdings Inc. since 2004. Mr. Schuetze has also served as an independent consultant since 2000.

As part of its investigation, the SLC interviewed Mr. Schuetze on July 6, 2006. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. Schuetze.

Alex Vieux. Mr. Vieux served as a member of the CA Board from July 15, 2002 to August 25, 2004. Mr. Vieux was asked to join the Board in 2002 at the request of Mr. Pieper, whom Mr. Vieux knew generally from the European software industry. Mr. Vieux served as a member of the Corporate Operations Committee from August 28, 2002 to August 25, 2004. In August 2003, Mr. Vieux served on the committee that considered the settlement of the 2003 Derivative Action.

Prior to joining the Board, Mr. Vieux worked at Andersen Consulting from 1981 to 1985. In 1985, Mr. Vieux took a position as the U.S. business correspondent for the French daily Le Monde. In 1988, Mr. Vieux was named Visiting Professor at the University of Paris Dauphine. Mr. Vieux is currently Chairman and CEO of Red Herring Magazine. In addition, Mr. Vieux has served, and continues to serve, as a director of numerous public companies, including as Chairman of Dasar Inc. (since 1990); Korea Thrunet Co., Ltd. (since 1999); Madge Networks N.V. (since 2000); XRT SA (since 2000); Commerce One, Inc. (since 2002); Qualys Inc. (since 2002); Daum Communications Corp. (since 2003); and Avanquest Software (since 2005). Mr. Vieux served as a director of Cibox LCI SA from 1998 to 2001.

As part of its investigation, the SLC interviewed Mr. Vieux on June 14, 2006. Based on its investigation, for reasons described in detail below, the SLC has determined to seek dismissal of the claims asserted against Mr. Vieux.

IV. FORMATION OF THE SLC

A. *Board Resolutions*

Following the filing of the 2005 Derivative Complaint, the CA Board, on February 1, 2005, adopted a resolution (the "2005 Resolution") that established the SLC. *See* Resolution of the CA Board (Feb. 1, 2005). The 2005 Resolution delegated to the SLC the authority and power to:

> control and determine the Corporation's response to the [2005 Derivative] Action and [the Rule 60(b)] Motions and the claims and arguments asserted in the Action and Motions. The Committee may, in its discretion, conduct an investigation into such claims and Motions and shall have full and sole authority to determine the appropriate actions to be taken on behalf of and in the name of the Corporation with respect to those claims and Motions, including whether to pursue the claims in the Action, whether to seek an extrajudicial resolution of such claims, or whether to seek an order from the Court to dismiss the Action.

Id. The 2005 Resolution also gave the SLC the authority to retain such outside counsel and other advisors it deemed necessary to perform its duties. Pursuant to the 2005 Resolution, the SLC was initially comprised of independent CA directors William E. McCracken and Laura S. Unger. The composition of the SLC was subsequently modified as described below.

Following the filing of the Kaufman Complaint, the CA Board, on October 31, 2006, adopted a resolution that authorized the SLC to control and determine CA's response to that litigation (the "2006 Resolution"). *See* Minutes of a Meeting of the CA Board (Oct. 31, 2006). Specifically, the 2006 Resolution delegated to the SLC the authority and power to:

> control and determine the Corporation's response to the Delaware Derivative Action and the claims and arguments asserted in the Delaware Derivative Action. The SLC may, in its discretion, conduct an investigation into such claims and shall have full and sole authority to determine the appropriate actions to be taken on behalf of and in the name of the Corporation with respect to those claims, including whether to pursue the claims, whether to seek

> extrajudicial resolution of such claims, or whether to seek an order from the Court to dismiss those claims.

Id. This resolution likewise gave the SLC the authority to retain such outside counsel and other advisors it deemed necessary to perform its duties.

B. *The Members of the Special Litigation Committee of the Board of Directors of CA, Inc.*

1. **Current SLC Members**

(a) *William McCracken*

Mr. McCracken joined the CA Board on February 1, 2005 as an independent director, and was appointed to the SLC on that date. Mr. McCracken also serves on the Compensation and Human Resource Committee and the Strategy Committee of the CA Board.

Mr. McCracken graduated from Shippensburg University of Pennsylvania in 1964 with a B.A. in Physics and Mathematics. Mr. McCracken worked at International Business Machines Corp. ("IBM") for thirty-six (36) years, from 1965 until he retired in August of 2001, and served in numerous positions at IBM as he worked his way up the ranks of the organization. Some of the highlights are: from 1988 to 1990, he was a Vice President in Channel Management within IBM's PC Division; from 1991 to 1993, he was a General Manager (President) of IBM's PC Division overseeing Europe, the Middle East, and Africa ("EMEA"); from 1993 to 1994, he was the Division President in the EMEA and Asia Pacific PC divisions; from 1994 to 1998, he served as General Manager (President) of Worldwide Marketing and Sales for the PC company; from 1998 to 2000, he served as the General Manager (President) of the Printing Systems Division; and from 1994 to 2001, Mr. McCracken was a member of the Chairman's Worldwide Management Council.

In 2003, Mr. McCracken formed Executive Consulting Group LLC, a general business and management strategy consulting company, and is currently its President. He has done general management and board consulting for companies such as Texas Pacific Group, Loral Space & Communications, and IBM. In addition, since July 31, 2003, Mr. McCracken has been a member of the board of IKON Office Solutions, Inc., a publicly-traded distributor of copier and printer technologies.

Mr. McCracken is also involved with several charitable institutions. For example, Mr. McCracken is currently Chairman of the Lutheran Social Ministries of New Jersey, a provider of community outreach services, affordable housing for special needs, low income, and elderly residents, and elder care; President of the Plainfield, New Jersey chapter of Habitat for Humanity; and a member of the New Jersey State Anti-Poverty Network.

(b) *Renato Zambonini*

Mr. Zambonini joined the CA Board on April 11, 2005 as an independent director, and was appointed to the SLC on that date. Mr. Zambonini also serves on the Strategy Committee of the CA Board.

Mr. Zambonini attended the University of Glasgow from 1964 to 1966, when he left to work as a COBOL programmer. He began working as a computer operator at Honeywell Information Systems in Newhome, Scotland in 1969. In 1974, after he immigrated to Canada, Mr. Zambonini worked as a programmer for Comtech Group International in Toronto. During his six-year tenure at Comtech, Mr. Zambonini spent two years in Cork, Ireland from 1977 to 1979 establishing a research and development center. From 1980 to 1985, Mr. Zambonini worked for Warrington Inc., a distributor of retail products, where he helped establish an early version of enterprise management software. In 1986, Mr. Zambonini joined Boston-based Cullinet Software Inc.

In 1989, while Mr. Zambonini was still working at Cullinet Software, it was acquired by CA. Rather than staying with the combined entity, Mr. Zambonini left to join

Cognos Inc., a business software provider, after he was referred there by a former co-worker of Cognos's founder and then-CEO Michael Potter. Mr. Zambonini joined Cognos in September 1989 as a Vice President of Research and Development. From 1990 to December 1992, he worked as a Senior Vice President in Research and Development, and from 1992 to 1993 he worked as a Senior Vice President in Product Development and Business Development. In January 1993, Mr. Zambonini was appointed President and COO of Cognos, at which time he joined the Cognos Board. In September 1995, Mr. Zambonini was named CEO. In April 2002, he resigned as President, while maintaining the post of CEO. In 2002, the Ottawa Business Journal named Mr. Zambonini as its CEO of the Year. In June 2004, Mr. Zambonini resigned as CEO, and was appointed Chairman of the Board, a position that he continues to hold.

In addition, Mr. Zambonini has been a director of (i) BCE Emergis Inc., a publicly-traded company that provides ebusiness solutions to the North American financial services and Canadian healthcare industries, since June 2004, and (ii) Reynolds & Reynolds Company, a publicly-traded company that provides integrated business solutions to automotive retailers, since 2003. Mr. Zambonini has been chair of the Ottawa Hospital Foundation's Legacy Campaign since December 2001.

2. **Former SLC Member Laura Unger**

Ms. Unger, a former Commissioner of the SEC, joined the CA Board on August 25, 2004 as an independent director,[33] after initially declining to join the CA Board in 2002

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[33] The DPA entered into by CA confirmed Ms. Unger's appointment to the CA Board, and provides that: "CA agrees to add new independent directors to its Board of Directors and to undertake corporate governance reforms such that, by December 31, 2005, CA will have: in addition to former SEC Commissioner Laura Unger, added a minimum of two independent directors to CA's board of Directors." DPA, ¶ 12(a).

because of other commitments. As noted above, Ms. Unger was appointed to the SLC on February 1, 2005, and resigned from the SLC on April 7, 2005, as described further below, to be replaced by Mr. Zambonini.

Ms. Unger graduated from the University of California at Berkeley in 1983 with a degree in rhetoric. She then graduated from New York Law School in 1987, and was subsequently licensed to practice law in Connecticut and New York. After graduating law school, Ms. Unger joined the New York Regional Office of the SEC, working in the SEC's Enforcement Division. In 1990, she moved to the SEC's Washington D.C. office, while continuing to serve in the Enforcement Division. For several months in 1990, Ms. Unger served as a Congressional Fellow in then-Senator Alfonse D'Amato's office, and from October 1990 to November 1997, she worked as counsel to the Senate Committee on Banking, Housing and Urban Affairs, which, at the time, was chaired by Mr. D'Amato.

On September 18, 1997, President William Clinton nominated Ms. Unger for a position as Commissioner of the SEC, and Ms. Unger was sworn in as Commissioner on November 5, 1997. Ms. Unger served as a Commissioner of the SEC from November 5, 1997 until she was named acting chair of the SEC on February 12, 2001. Ms. Unger served as acting chair of the SEC until she left the Commission on August 3, 2001.

Since leaving the SEC, Ms. Unger has served in a variety of positions. From June 2002 to June 2003, Ms. Unger served as a regulatory expert for CNBC. In May 2003, Ms. Unger became an independent consultant for JP Morgan Chase in connection with the Global Research Analyst Settlement, and continues to work in that capacity. From April 2002 to August 2004, Ms. Unger served on the Board of Borland Software Corp., a publicly traded software company. In October 2002, she joined the Board of Ambac Financial Group, Inc., and continues to serve in that capacity.

Ms. Unger also serves on the Board of the Children's National Medical Center, a nationally recognized leader in pediatric medicine. She also serves on (i) the Non-Member Advisory Board of the U.S. Institute, (ii) the Wall Street Lawyer Advisory Board, and (iii) the SEC Historical Society Advisory Council.

C. ***SLC Independence Review***

Prior to conducting any substantive investigatory work, the SLC and its counsel, Fried Frank, engaged in a thorough review of the independence of each member with respect to the defendants named in the 2005 Derivative Action. In conducting the independence review, the SLC was guided by principles of Delaware law regarding the independence of special litigation committees. As such, the SLC and its counsel sought to determine whether its members were, "*for any substantial reason,* incapable of making a decision with only the best interests of the corporation in mind." *In re Oracle Corp. Derivative Litig.*, 824 A.2d 917, 938 (Del. Ch. 2003) (emphasis in original); *see also Kaplan v. Wyatt,* 499 A.2d 1184, 1189 (Del. 1985) ("a director is independent when he is in a position to base his decision on the merits of the issue rather than being governed by extraneous considerations or influences").

The factors that the SLC considered in its independence review included: (i) the SLC's involvement, if any, in the actions at issue in the 2005 Derivative Action; (ii) the SLC's financial interest, if any, in the actions at issue in the 2005 Derivative Action; (iii) the SLC's professional and personal relationships, if any, with the defendants in the 2005 Derivative Action; (iv) the SLC's mutual connections with the defendants in the 2005 Derivative Action, if any, to institutions, businesses, charitable organizations, or other entities; and (v) any pre-judgments made by the SLC members, if any, about the veracity of the claims alleged in the 2005 Derivative Action.

The SLC and its counsel also considered any other factors that would "weigh on the mind of a reasonable special litigation committee member . . . in a way that generates an unacceptable risk of bias." *Oracle,* 824 A.2d at 938-39 ("a director may be compromised if he is beholden to an interested person. Beholden in this sense does not mean just owing in the financial sense, it can also flow out of personal or other relationships to the interested party") (citations omitted); *see also Beam v. Martha Stewart*, 845 A.2d 1040, 1051 (Del. 2004) (doubts about a director's independence may arise "because of financial ties, familial affinity, a particularly close or intimate personal or business affinity"); *Biondi v. Scrushy*, 820 A.2d 1148, 1166 (Del. Ch. 2003) (finding that an SLC lacked independence where the SLC Chairman "publicly and prematurely issued statements exculpating one of the key company insiders whose conduct [was] supposed to be impartially investigated by the SLC"); *Katell v. Morgan Stanley Group, Inc.*, 1995 WL 376952, at *8 (Del. Ch. June 15, 1995) ("When a special committee's members have no personal interest in the disputed transactions, this Court scrutinizes the members' relationship with the interested directors") (citation omitted).

To that end, Mr. McCracken and Ms. Unger met with Fried Frank on March 15 and March 23, 2005, respectively, to review each of their respective backgrounds, and to discuss their relationships with current and former Company officers, directors, and employees in the context of the factors enumerated above. Further, Mr. McCracken and Ms. Unger met with Fried Frank on March 30, 2005 and April 7, 2005 to further discuss the issue of independence.

Based upon Fried Frank's review of Ms. Unger's background, Fried Frank and Ms. Unger jointly concluded that she was independent and financially disinterested from the defendants in the 2005 Derivative Action. However, Fried Frank and Ms. Unger jointly determined that it would be in the best interests of the Company for Ms. Unger to discontinue her participation on the SLC due to her past professional association with defendant Alfonse D'Amato, as noted above. While Ms. Unger did not believe that her past association with Mr. D'Amato compromised her ability to act independently, she nonetheless wanted to avoid even the appearance of a conflict. In Ms. Unger's letter announcing her resignation from the SLC, dated April 7, 2005, she stated:

> I am absolutely confident in my ability to render impartial and objective judgment in performing my duties as a member of the Committee and would make a valuable contribution to the Committee's efforts. To render a credible decision about the shareholder litigation, however, the Committee must meet rigorous independence criteria in both appearance and fact. After discussions with counsel regarding recent judicial interpretations on independence, I do not wish for any question about the appearance of my independence to compromise the Committee's important work.

Letter from Laura Unger to the CA Board (Apr. 7, 2005). No substantive investigative work was conducted while Ms. Unger served on the SLC.

Based upon Fried Frank's review of Mr. McCracken's background, Fried Frank and Mr. McCracken jointly concluded that he was independent and financially disinterested from the defendants in the 2005 Derivative Action. Specifically, Mr. McCracken: (i) had no involvement in any of the actions at issue in the 2005 Derivative Action; (ii) had no financial interest in the actions at issue in the 2005 Derivative Action; (iii) had no professional or personal relationship with any of the defendants; (iv) was not aware of any mutual connections to any institutions, businesses, charitable organizations, or other entities with any of the defendants; and (v) had made no pre-judgments about any of the claims alleged in the 2005 Derivative Action.

On April 11, 2005, the CA Board elected Mr. Zambonini to serve as an independent director. That same day, he was appointed to the SLC. On May 9, 2005, Mr. Zambonini met with Fried Frank to review his background, and to discuss his relationships, if any, with current and former Company officers, directors, and employees in the context of the factors enumerated above. Based upon Fried Frank's review of Mr. Zambonini's background, Fried Frank and Mr. Zambonini jointly concluded that he was independent and financially disinterested from the defendants in the 2005 Derivative Action. Specifically, Mr. Zambonini: (i) had no involvement in any of the actions at issue in the 2005 Derivative Action; (ii) had no financial interest in the actions at issue in the 2005 Derivative Action; (iii) had no professional or personal relationship with any of the defendants (except as noted below); (iv) was not aware of any mutual connections to any institutions, businesses, charitable organizations, or other entities with any of the defendants; and (v) had made no pre-judgments about any of the claims alleged in the 2005 Derivative Action.

Based upon Fried Frank's interviews of Messrs. McCracken and Zambonini, and its independent research of the public record, Fried Frank found that:

- The SLC members were appointed to the Board after: (i) the alleged wrongdoing; (ii) the resignation from CA of all of the defendants who were charged with criminal conduct; (iii) the settlement of the 2003 Derivative Action and the Class Actions; (iv) the signing of the DPA; and (v) the commencement of the 2005 Derivative Action.

- Neither of the SLC members has worked for or with any of the individual defendants in the past.

- Neither of the SLC members are dependent upon any of the defendants for employment or other pecuniary gain.

- Neither of the SLC members has served on corporate, charitable, or other boards of directors (except for CA) with any of the defendants.

- Neither of the SLC members has been involved with charitable or educational institutions to which any of the defendants contribute funds of which they are aware.
- Neither of the SLC members has a prior personal or social relationship with any of the defendants.
- Neither of the SLC members made any prior judgments regarding the merits of the 2005 Derivative Action or the Rule 60(b) Motions.

The only mutual relations to the defendants that the SLC and Fried Frank uncovered during its independence review were the following. First, E&Y serves as Cognos's independent audit firm, and as such, Mr. Zambonini has had contact with E&Y in a professional capacity during his tenure as Chairman and CEO of Cognos (although he has never interacted with the E&Y accountants who rendered services to CA). Second, both members of the SLC have attended technology industry events also attended by Mr. Wang and/or Mr. Kumar in the past; however, neither of the SLC members interacted personally with them at these events. For example, Mr. Zambonini was a member of the Enterprise Software CEO round table, which met every six months, along with Mr. Kumar and approximately thirty other CEOs. However, Mr. Zambonini never had a one-on-one conversation with Mr. Kumar at these meetings. Third, Mr. Zambonini met Charles Wang when his former employer, Cullinet, was acquired by CA in 1989. However, as noted above, Mr. Zambonini declined to work for CA after the merger of Cullinet and CA, and Mr. Zambonini has not been in contact with Mr. Wang since that time. Thus, the SLC members and Fried Frank jointly concluded that none of the above-described connections would in any way impair their independence with respect to E&Y, Mr. Kumar, and Mr. Wang.

For these reasons, both Messrs. McCracken and Zambonini, in consultation with Fried Frank, have concluded that they are independent and financially disinterested from the defendants named in the 2005 Derivative Action, and their conclusions are the product of an unbiased review of the facts and circumstances alleged in the 2005 Derivative Complaint.[34]

D. ***Retention of Counsel***

After interviewing multiple law firms, on March 8, 2005, the SLC, then composed of Mr. McCracken and Ms. Unger, retained Fried Frank as counsel to assist the SLC with its investigation of the claims alleged in the 2005 Derivative Complaint. Fried Frank had no prior attorney-client relationship with CA, nor any of the individual defendants, nor the members of the SLC. However, because Fried Frank had at the time, and currently has, an attorney-client relationship with E&Y, the SLC retained separate counsel to advise it with respect to the claims alleged in the 2005 Derivative Complaint against both KPMG and E&Y. Fried Frank had no attorney-client relationship with KPMG at any point prior to or during the SLC investigation, and does not now.

After interviewing several additional law firms, the SLC retained Cohen & Gresser LLP as counsel in connection with its investigation of the claims alleged against E&Y and KPMG. Cohen & Gresser had no prior attorney-client relationship with CA, KPMG, E&Y, the individual defendants, or the members of the SLC. As a result of this division of the SLC investigation, Fried Frank did not participate in the investigation of the claims against E&Y and KPMG, while Cohen & Gresser did not participate in the investigation of the claims against the individual defendants. Both firms consulted from time to time on strategic considerations

34 These same conclusions apply to the Kaufman Complaint, which was filed in September 2006, and is virtually identical to the 2005 Derivative Action. As noted above, the only additional defendants named in the Kaufman Complaint not named in the 2005 Derivative Complaint are Shirley Strum Kenny and Alex Vieux, with whom the SLC members had no prior personal or professional relationship, and from whom the SLC members are independent and financially disinterested.

related to the investigation, and coordinated their activities to proceed in the most efficient and cost-effective manner.

V. SLC WORK PLAN

Overview. With the assistance of counsel, the SLC conducted a detailed and thorough factual and legal investigation in order to determine whether it is in the best interests of the Company and its shareholders to pursue, settle, or dismiss any or all of the claims asserted in the 2005 Derivative Action and the Kaufman Complaint. The SLC members have been intimately involved in every aspect of the investigation. Counsel to the SLC conducted approximately ninety (90) interviews[35] – at least thirty (30) of which were attended by one or both of the SLC members. Among those individuals interviewed personally by the SLC members were (i) the Criminal Defendants (with the exception of Lloyd Silverstein), (ii) the Former Officer Defendants (with the exception of Charles McWade), (iii) the Oversight Director Defendants (with the exception of Willem de Vogel), (iv) the Settlement Director Defendants (with the exception of Alex Vieux), and (v) other former CA officers, employees, and advisors, including counsel from WLRK and S&C. Several of these individuals were interviewed multiple times.

In addition, SLC counsel reviewed millions of pages of documents, and the SLC members themselves have reviewed scores of pertinent documents, including interview memos, legal memos, minutes, notes, and e-mails. SLC counsel performed a substantial amount of legal research and analysis, the results of which were considered by the SLC at various stages of the investigation. The SLC held twenty (20) formal meetings during the course of its investigation, and held dozens of additional conference calls and informal meetings at which

[35] This includes interviews conducted with the assistance of the SLC's counsel in connection with the claims alleged against the audit firms in the 2005 Derivative Litigation.

the issues raised during the investigation were discussed. Indeed, Mr. Zambonini traveled from his home in Ottawa, Canada on more than twenty occasions. The investigation was directed by the SLC members in all respects.

As described further below, the SLC's investigation was necessarily divided into two (2) distinct phases as a result of the simultaneous criminal prosecution of Sanjay Kumar and Stephen Richards. At the outset of the SLC's investigation, the USAO requested that the SLC refrain from conducting interviews that in any way touched upon the underlying accounting fraud.[36] As such, during the first phase of its investigation, the SLC limited its investigation to narrowly-tailored interviews while conducting substantial document review. Following the guilty pleas of Messrs. Kumar and Richards on April 24, 2006, the SLC was able to conduct and finish its investigation unrestricted.

A. ***Phase I: The SLC's Limited Investigation***

During this phase of its investigation, the SLC attempted to conduct and complete its investigation into the CA Board's decision to authorize the 2003 Settlement without (as per the direction of the USAO) conducting any interviews that discussed or touched upon the underlying accounting fraud. However, the SLC ultimately concluded that the two issues could not be divorced, and that obtaining a full understanding of the CA Board's knowledge with respect to the underlying accounting fraud was critical to understanding its decision to enter into the 2003 Settlement. Thus, the SLC concluded that this portion of the

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[36] On June 24, 2005, the USAO filed a motion with this Court seeking a stay of all deposition discovery sought by the plaintiffs in connection with the Rule 60(b) Motions. The USAO filed briefs supporting this motion on June 30 and November 7, 2005. By order dated November 30, 2005, this Court granted the relief sought by the USAO and stayed all deposition discovery. *See* Memorandum and Order, dated Nov. 30, 2005, *In re Computer Assoc. 2002 Class Action Sec. Litig.*, 02 Civ. 1226 (TCP). Out of deference to the USAO's prosecution, the SLC voluntarily limited its investigation pursuant to the USAO's request.

investigation could not be (and was not) completed until after the resolution of the criminal cases against Messrs. Kumar and Richards.

1. **Interviews**

In this first phase, the SLC conducted the following interviews during the spring and summer of 2005. Where not already articulated above, a brief description of that individual's role in the events at issue is provided:

THE SETTLEMENT DIRECTOR DEFENDANTS	
1.	*Kenneth Cron*
2.	*Alfonse D'Amato*
3.	*Gary Fernandes*
4.	*Robert La Blanc*
5.	*Jay Lorsch*
OUTSIDE COUNSEL	
6.	*Peter Fleming.* Mr. Fleming, of Curtis, Mallet-Prevost, Colt & Mosle LLP, was counsel to the committee created by the Board to assess the merits of a settlement of the Class Actions.
7.	*James McGuire.* Mr. McGuire, formerly of White & Case LLP, was counsel to the committee created by the Board to assess the merits of a settlement of the 2003 Derivative Action. Mr. McGuire is now a New York State Supreme Court Judge, Appellate Division.
8.	*David Nachman.* Mr. Nachman of DLA Piper Rudnick Gray Cary US LLP (the Piper Rudnick), was counsel to the Company and the individual defendants in the Class Actions.

The SLC also requested, received, and reviewed documents from each of these individuals. *See* Letters from Douglas H. Flaum to Peter Fleming and David Nachman (Apr. 11, 2005); Letter from Douglas H. Flaum to James McGuire (Apr. 14, 2005); Letter from David Hennes to Lewis Liman (May 24, 2005). The SLC also requested, received, and reviewed documents from Russell Artzt, Sanjay Kumar, and Charles Wang. *See* Letters from David Hennes to Stephen E. Kesselman, Vincent A. Sama, and Eric Halper (May 20, 2005).

2. **Documents Reviewed**

The SLC also began (and substantially completed) reviewing millions of pages of documentary evidence during the first phase of its investigation, including:

	DOCUMENTS
1.	The so-called "23 boxes" of documents produced to the government by the Company in September 2003.
2.	The 150 boxes of documents produced by the Company in the Class Actions.
3.	Interview memoranda from 176 interviews of CA employees conducted by WLRK and S&C between April 2002 and November 2004.
4.	Transcripts of the depositions given by CA employees in connection with the Class Actions.
5.	Minutes, and where available, notes of the meetings of CA's Board, Audit Committee, Compensation Committee, Executive Committee, and Corporate Governance Committee from 1997 to 2004.
6.	Board and Audit Committee packages from 2001 to 2005 (and earlier, to the extent available).
7.	Counsels' talking points for meetings of CA's Board and Audit Committee, and meetings with the USAO and SEC, where available.
8.	Exhibits to the Audit Committee's oral reports to the USAO and SEC in October and November 2004.
9.	E&Y reports, presentations, memoranda and management letters.
10.	KPMG reports, presentations, memoranda and management letters.
11.	Certain reports prepared by PwC for the CA Board, WLRK, and S&C in connection with the government and Audit Committee investigations.
12.	WLRK's correspondence with the USAO and the SEC regarding the investigation from 2002 to the present.
13.	Documents produced by current and former directors, including notes taken at Board and Audit Committee meetings.
14.	Certain publicly-available information, including SEC filings and news media reports, CA Press Releases, SEC Complaints, civil complaints filed against CA, and documents related to the criminal investigation of former CA officers and employees including informations, indictments, and plea agreements.
15.	Significant portions of the PwC forensic database, containing the contents of the computers of eighty-nine CA employees, including e-mails.

3. **Experts**

The SLC retained several experts to assist it with its investigation, primarily to provide expert accounting and financial advice. The SLC also retained a private investigatory firm in an attempt to discover, and in some cases verify, the assets possessed by the Criminal Defendants. Those experts are as follows:

PricewaterhouseCoopers. PwC is the largest of the "Big Four" accounting firms, providing assurance, tax, and advisory services to companies around the world. PwC's clients include at least four of the ten largest public companies in the United States. CA and WLRK first retained PwC in connection with the government investigation in February 2002.

Given its familiarity with CA and its financial reports, the SLC retained PwC in April 2006 to analyze the impact of the 35-Day Month practice on the periods leading up to the accelerated vesting of the KESOP, primarily the quarters ending December 31, 1997 and March 31, 1998, and through CA's fiscal year 2001. PwC calculated the adjusted revenue, income, and earnings per share ("EPS") numbers for each of the quarters examined after accounting for revenue that was deemed to be improperly recorded.

Ray Ball, Ph.D. Dr. Ball is the Sidney Davidson Professor of Accounting at the University of Chicago Graduate School of Business. The SLC retained Dr. Ball to conduct an analysis on the impact of the 35-Day Month practice on CA's share price in order to determine if, had the fraud and CA's true financial results been disclosed earlier, CA's share price would have met the targets required for the accelerated vesting of the KESOP shares. Dr. Ball is one of the world's leading experts on the effect of earnings announcements on stock prices and currently teaches masters and doctoral courses on Financial Accounting and International Accounting. Dr. Ball has received numerous teaching awards, including being named the American Accounting Association's Distinguished International Lecturer for 1999 and its Educator of the Year in 2003 and is the author or co-author of four (4) books and over sixty (60) papers. His research focuses on financial reporting and disclosure; earnings and stock prices; international accounting and finance; market efficiency; and the institutions of a market economy. Dr. Ball also received the American Accounting Association's inaugural award for Seminal Contribution to the Accounting Literature.

Dr. Ball has served as a professor at numerous educational institutions in addition to the University of Chicago, including the University of Queensland, Australia, from 1972 to 1976 (Professor of Accounting & Business Finance); the Australian Graduate School of Management from 1976 to 1986 (Foundation Professor); the William E. Simon Graduate School of Business Administration at the University of Rochester from 1986 to 2000 (Wesray Professor of Business Administration); and the London Business School from 1996 to 2002 (Professor and Visiting Professor of Accounting). Dr. Ball has served, and continues to serve, as a Professor at the European Institute for Advanced Studies in Management (since 1998); as a Distinguished Fellow at the Centre for Independent Studies in Sydney, Australia (since 1996); and as an Academic Affiliate of Analysis Group Inc. (since 2000).[37]

Analysis Group, Inc. Analysis Group is a national consulting firm that provides economic, financial, and business strategy consulting to law firms, corporations, and government agencies. Analysis Group has provided research, analysis, and expert testimony in many complex litigations involving accounting and financial issues. Analysis Group's professional staff, which includes Ph.D.s in accounting, as well as CPAs, CMAs, and CFAs, works closely with a network of academic experts who are leaders in these disciplines. The SLC retained Analysis Group to support Professor Ball's analysis of the impact of the 35-Day Month practice on CA's share price in order to determine if, had the fraud and CA's true financial results been

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37 Dr. Ball has served on numerous academic journals, including the *Journal of Accounting Research* from 1972 to 1987 (Associate Editor); the *Australian Journal of Management* from 1976 to 1979 (Foundation Editor); the *Journal of Accounting and Economics* from 1979 to 2000 (Associate Editor and Editor); the *Journal of Banking and Finance* from 1983 to 1988 (Associate Editor); and the *Journal of Business Finance and Accounting* from 1985 to 1988 (Editorial Board). Dr. Ball has served, and continues to serve, on the Advisory Board of *Accounting Research Network* (since 1996); as Associate Editor of the *Asia and Pacific Journal of Accounting and Economics* (since 1999); as Editor of the *Journal of Accounting Research* (since 2000); on the Editorial Board of the *European Accounting Review* (since 2002); and as Advisory Editor of *Global Management Research* (since 2003).

disclosed earlier, CA's, CA's share price would have met the targets required for the accelerated vesting of the KESOP shares.

Alvarez & Marsal. Alvarez & Marsal, a leading professional services firm, was retained by the SLC to provide forensic accounting advice.

SafirRosetti. The SLC retained SafirRosetti, a private investigatory firm, in an attempt to discover, and in some cases verify, the assets possessed by the Criminal Defendants. SafirRosetti provided the SLC with information regarding the Criminal Defendants' stock holdings, ownership of real property, motor vehicles, and other valuable assets both in the names of the defendants and their spouses.

4. The SLC's Good Faith Attempts to Cooperate with the Plaintiffs and the Plaintiffs' Response

The SLC also made a good-faith effort to cooperate with all plaintiffs in the 2005 Derivative Action. For example, on May 6, 2005, counsel for the SLC met with counsel for Irving Rosenzweig and Bert Vladimir, plaintiffs in the 2005 Derivative Action. At this meeting, the SLC requested that the plaintiffs share any information that they believed would be helpful to the SLC's evaluation of the claims made in the 2005 Derivative Action. However, counsel for Messrs. Rosenzweig and Vladimir were unable to provide any basis for the claims they alleged in the 2005 Derivative Action, other than the guilty pleas of (at that time) five (5) of CA's former officers and employees.

On June 15, 2005, counsel for the SLC, and the members of the SLC, met with counsel for the Wyly entities. At this meeting, the SLC also requested that the Wyly entities share any information they believed would be helpful to the SLC's evaluation of the claims made in the 2005 Derivative Action. However, counsel for the Wyly entities declined to provide any substantive information to the SLC.

During its investigation, counsel for the SLC has periodically met with and updated counsel for the various plaintiffs, including counsel for Ms. Kaufman, on the status of its investigation and requested that they share any relevant information in their possession with the SLC. To date, no factual information has been shared with the SLC.

B. *Phase II: After the Guilty Pleas of Messrs. Kumar and Richards*

On April 24, 2006, Messrs. Kumar and Richards pled guilty to all counts in the superseding indictment filed by the USAO. Shortly thereafter, counsel to the SLC contacted the USAO regarding its investigation, and, several weeks later, the USAO advised the SLC that it no longer objected to the SLC pursuing its investigation (but asked to be kept apprised of developments and retained the right to object to specific interviews if it believed it prudent to do so). *See* Letter from Eric Komittee, Assistant United States Attorney, United States Attorney's Office, to the Honorable Thomas C. Platt, United States District Judge, Eastern District of New York (Apr. 26, 2006). Accordingly, the SLC immediately began its investigation without restriction.

1. **Interviews Conducted**

During this phase of its investigation, the SLC and its counsel conducted an additional eighty-two (82) interviews, some of which extended multiple days. These interviews included (i) all of the named individual defendants, except for Mr. Wang; (ii) certain current and former employees in various CA departments, including Sales, Finance, Sales Accounting, Legal, and GSO; and (iii) certain of CA's outside advisors during the relevant period. As noted above, the SLC members personally participated in many of these interviews.

Through these interviews, the SLC was able to gain a full understanding of the conduct at issue in the 2005 Derivative Action and the Kaufman Complaint. Below is a complete list of the individuals interviewed by the SLC, with descriptions where not already provided:

THE SETTLEMENT DIRECTOR DEFENDANTS	
1.	*Kenneth Cron*
2.	*Alfonse D'Amato*
3.	*Robert La Blanc*
4.	*Lewis Ranieri*
5.	*Walter Schuetze*
6.	*Alex Serge Vieux*
THE OVERSIGHT DIRECTOR DEFENDANTS	
7.	*Russell Artzt*
8.	*Alfonse D'Amato*
9.	*Willem de Vogel*
10.	*Richard Grasso*
11.	*Shirley Strum Kenny*
12.	*Roel Pieper*
NON-DEFENDANT DIRECTORS	
13.	*Linus Cheung*. Mr. Cheung served on the CA Board from June 26, 2001 to March 27, 2002, and has not been named a defendant in any suit.
CRIMINAL DEFENDANTS	
14.	*David Kaplan*
15.	*Sanjay Kumar*
16.	*Stephen Richards*
17.	*David Rivard*
18.	*Lloyd Silverstein*
19.	*Steven Woghin*
20.	*Ira Zar*
FORMER OFFICER DEFENDANTS	
21.	*Michael McElroy*
22.	*Charles McWade*
23.	*Peter Schwartz*
FORMER SENIOR MANAGEMENT	
24.	*Gary Quinn*. Mr. Quinn joined CA as a programmer in the IT department in 1985. From 1986 to 1987, he worked in product development; in 1988 he worked in the Sales department, and from 1988 to 1991 he worked in Pre-Sales, providing technical support for sales personnel; from 1991 to 1998, he was head of the Technology and Education Groups; from 1993 to 1995 he worked in Global Marketing; from 1996 to 2001, he worked in the IT and facilities areas; from April 2001 to 2003, he returned to Sales; Mr. Quinn was then the Executive Vice President of Partner Advocacy, until his resignation in September 2006.

25.	*Douglas Robinson*. Mr. Robinson joined CA when CA acquired his then-employer Cullinet in 1989. From 1989 to 1991, he was the head of the Internal Audit department; from 1991 to 1993, he was the head of Sales Accounting; from 1993 to 1995, and again from 2002 to 2006, he was a Senior Vice President in the Finance department; from 1995 to 2000 he was the head of Investor Relations; and from October 2003 to April 2004, he served as CA's interim CFO. Mr. Robinson resigned from CA in August 2005.
INTERNAL AUDIT EMPLOYEES	
26.	*Grace Caden*. Ms. Caden, a CPA, joined CA's Sales Accounting department in 1987. From 1993 to 1996, she worked in the Microproducts division, and in July 1996 she joined CA's Internal Audit department. Ms. Caden served as the head of the Internal Audit department from 2000 to 2004. Ms. Caden is currently employed by the Company as Vice President of Internal Audit.
27.	*Anthony Valenzano*. Mr. Valenzano joined CA's Internal Audit department in 1999, and is currently employed in that department.
SALES EMPLOYEES	
28.	*Paul Balzano*. Mr. Balzano joined CA as a systems engineer in 1984. From 1986 to 1989, he worked as a database specialist; in 1989, he joined the Sales department as an account manager; in the early 1990s, he began working in the global accounts division of the Sales department; in 1998, Mr. Balzano was transferred to the Global Sales Organization; Mr. Balzano has worked in various capacities in the Strategic Accounts Group within Sales since early 2000. Mr. Balzano is currently employed by the Company as a manager in the Sales department.
29.	*Christina Savino Costanza*. Ms. Costanza joined Sales Accounting in 1994.
30.	*Alex Fourney*. Mr. Fourney joined CA in August 1985. In fiscal year 2000, Mr. Fourney worked as a Vice President in the Global Accounts Group within Sales; in fiscal year 2001 Mr. Fourney worked as a Senior Vice President in the Strategic Business Alliances Division; in fiscal year 2002 Mr. Fourney became a Vice President and manager in Sales.
31.	*Sam Greenblatt*. Mr. Greenblatt joined CA's Advance Sales department in 1994. Mr. Greenblatt is currently employed by the Company as Senior Vice President of Technology.
32.	*Karen Kikel*. Ms. Kikel joined CA in June 1989. In 1994 she served as an assistant to Mr. Kumar; in 1995 she began working as a sales manager in global sales; from 1998 to February 2003 she served in the Global Sales Organization, after which she served as a paralegal in the Legal department.
33.	*Hayley Tabor*. Ms. Tabor worked as a CA sales executive from 1991 to 2001. From 2001 to 2006, Ms. Tabor was responsible for sales, marketing, customer relations, and technical services for CA's operations in Europe, the Middle East, and Africa. Ms. Tabor left CA in 2006.
34.	*Mark Wagasky*. Mr. Wagasky worked as a CA sales executive from 1995 to 2004, and resigned from CA in July 2004.

35.	*James Christopher Wagner*. Mr. Wagner was the Senior Vice President for commercial sales at CA from 1995 through 1998. In 1998, he became Senior Vice President for CA professional services. From 1998 through 2000, Mr. Wagner reported directly to Sanjay Kumar. Mr. Wagner left CA in April 2000.
	SALES ACCOUNTING EMPLOYEES
36.	*Peter Bordonaro*. Mr. Bordonaro joined CA as a contract administrator in the Sales Accounting department in May 1995. Mr. Bordonaro worked in the Global Sales Organization from 1998 to February 2003, at which time he returned to Sales Accounting as a business manager.
37.	*Carmella Bythrow*. Ms. Bythrow joined CA in January 1988 in the Sales Accounting department. Ms. Bythrow was promoted to the position of Assistant Vice President in Sales Accounting in late 1999.
38.	*Christina Savino Costanza*. Ms. Costanza joined the Sales Accounting department at CA in January 1994. She began working as a contract manager in Sales Accounting in the late 1990s.
39.	*John Gallo*. Mr. Gallo worked as a contract supervisor in the Sales Accounting department in fiscal year 2000.
40.	*Scott Hughes*. Mr. Hughes joined CA in August 1999 as a contract administrator in the Sales Accounting department. In April 2001 he was promoted to the position of contract supervisor in Sales Accounting.
41.	*Tina Ratcliff*. Ms. Ratcliff joined CA in the Sales Accounting department in July 1991.
42.	*Kurt Sprenger*. Mr. Sprenger joined CA in March 1990. In 1992 he began working as a contract supervisor in the Sales Accounting department.
	FINANCE EMPLOYEES
43.	*Paul Goncalves*. Mr. Goncalves joined the Sales Accounting department in mid-1994. In 1996 Mr. Goncalves began working as an international controller; in 1999 Mr. Goncalves began working as an assistant controller for CA's operations in the U.S., and by 2004 he worked as controller for those operations.
	DEVELOPMENT EXECUTIVES
44.	*Sam Greenblatt*. Mr. Greenblatt joined CA's Advance Sales department in 1994. Mr. Greenblatt is currently employed by the Company as Senior Vice President of Technology.
45.	*Bill Merrow*. Mr. Merrow joined CA's Advance Sales department in 1995. Mr. Merrow is currently employed by the Company as Senior Vice President of Development.
46.	*Gary Starkey*. Mr. Starkey joined the Advance Sales department in 1986. Mr. Starkey is currently employed by the Company as Senior Vice President of the Executive Technology Advisors.
47.	*Nigel Turner*. Mr. Turner worked in the Advance Sales department from 1995 to 2002. Mr. Turner resigned from CA in October 2006.
	CURRENT AND FORMER LEGAL EMPLOYEES
48.	*James Black*. Mr. Black joined CA's Legal department in 1997. Mr. Black resigned from CA in April 2006.
49.	*Joshua DeRienzis*. Mr. DeRienzis worked in CA's Legal department from 1999 to 2005, and resigned from CA in July 2005.

50.	*Bonnie Yeomans*. Ms. Yeomans has worked CA's Legal department since 1991. Ms. Yeoman's is currently an assistant General Counsel at CA.
ASSISTANTS	
51.	*Lucy Neubauer*. Ms. Neubauer was an administrative assistant to Charles Wang from 1999 to 2002. Ms. Neubauer resigned from CA in April 2004.
52.	*Joanne Passaretti*. Ms. Passaretti was an administrative assistant to Charles Wang in 1999. Ms. Passaretti is currently employed by the Company in CA's Italy office.
KPMG EMPLOYEES	
53.	*Margaret Gonzales*. Ms. Gonzales is a senior manager of KPMG.
54.	*Larry Smith*. Mr. Smith served as an engagement partner of KPMG from 2000 to 2002.
OUTSIDE COUNSEL	
55.	*Robert Giuffra*. Mr. Giuffra, of Sullivan & Cromwell LLP, was counsel to the Audit Committee in connection with its investigation of the Company's accounting practices.
56.	*Richard Urowsky*. Mr. Urowsky, of Sullivan & Cromwell LLP, was counsel to the Audit Committee in connection with its investigation of the Company's accounting practices.
57.	*Scott Smith*. Mr. Smith, of Covington & Burling LLP, was corporate counsel to CA from 1999.
58.	*John Savarese*. Mr. Savarese, of Wachtell, Lipton, Rosen & Katz, was counsel to CA in connection with the government investigation.

The following former CA employees have refused to be interviewed by the SLC: (i) Thomas Bennett, a former Senior Vice President of business development (2000-2004) who pled guilty to obstruction of justice for his part in covering up the 35-Day Month practice; (ii) Jim Berryhill, former Senior Vice President and General Manager of Sales; (iii) Richard Chiarello, former head of worldwide Sales (1989-1998); (iv) Richard Finegan, former divisional vice president of Financial Accounting (1998-2004); (v) Gayle Kemper, former Senior Vice President and general manager of Sales (1987-2003); (vi) Michael Miller, former general manager in the Sales department (1987-2001); (vii) Abraham Poznanski, former CFO and Senior Vice President of Internal Audit (1979-2001); (viii) Bryan Shepherd, former head of worldwide Sales; (ix) Chris Telano, former member of the Internal Audit department (1998-2000); and (x) Donald Watnick, former head of litigation in the Legal department (2000-2004).

While the SLC has reason to believe these individuals may have information relevant to its investigation, the SLC believes this information would be largely corroborative of information provided by other witnesses, and thus does not believe that its inability to interview these individuals has materially impeded its ability to perform its mandate or reach its conclusions.

2. **Additional Information**

In addition to continuing to review the documents listed above during the first phase of its investigation, the SLC reviewed (i) e-mails, notes, and other documentation provided by Mr. Kumar; (ii) the materials produced by the USAO to Mr. Kumar pursuant to 18 U.S.C. § 3500; and (iii) and counsel's notes from Board and Audit Committee meetings. The SLC met with members of CA management on three occasions (once personally and twice telephonically) to receive their views of the impact of continued litigation on the Company

3. **SLC Meetings**

As noted above, in total, during the course of its investigation, the SLC met formally twenty (20) times. At these meetings, the SLC, with the aid of counsel, reviewed the results of its investigation, planned additional steps needed, and deliberated as to what course of action was in the best interests of the Company with respect to the claims made in the 2005 Derivative Action and the Kaufman Complaint. At least five (5) of the SLC's formal meetings were dedicated, in whole or in part, to deliberations of the various claims; and during these meeting the SLC members deliberated for over thirty (30) hours. The SLC members deliberated informally, both together and with counsel, for dozens of additional hours. The results of its factual findings and deliberations are detailed below.

In addition, the SLC members personally negotiated and reached settlements with certain of the defendants and their counsel, including Sanjay Kumar, Russell Artzt, and Charles McWade.

4. Preparation of this Report

The SLC played a significant role in the drafting of its report. The SLC members spent innumerable hours drafting and reviewing this report and met with counsel on more than twenty-five (25) occasions to draft and discuss its substance. In addition, following an independence review conducted by Fried Frank, Christopher Lofgren, an independent CA Board member who joined the Board on November 11, 2005, reviewed two (2) drafts of the executive summary of this report, and then met with the SLC members to discuss his views.

VI. THE 35-DAY MONTH PRACTICE

The following section details the 35-Day Month practice – and the involvement therein, if any, of the individual defendants. These facts are taken primarily from the record established during the government investigation, supplemented by information learned during the course of the SLC's investigation. Although the participants in the wrongdoing engaged in widespread deception – both in terms of their revenue recognition practices and their conspiracy to conceal those practices – the SLC has used, and relied on, documents, interview memoranda, and other data from previous investigations that could be substantiated and that it determined were reliable. Together, these sources tell the story of the fraud and obstruction perpetrated at CA.

A. *Origins of the Fraud: Wall Street's Estimates and the Hockey Stick Effect*

1. The Pressure to Meet Analysts' Expectations

The 35-Day Month practice grew over time, but always started with the same motivation: to ensure, regardless of its actual performance, that CA met or exceeded Wall Street's expectations. *See* DPA, Stipulation of Facts ¶ 8. Every fiscal quarter, when Wall

Street analysts "estimated what they believed would be CA's total revenue" for the quarter,[38] the market judged CA's stock based on its ability to meet these analysts' estimates. *Id.* ¶ 6. If CA met or exceeded the estimates, the Company's stock price would generally rise (all other things being equal); if CA failed to meet expectations, CA's stock price would generally be negatively affected. *See id.* CA's statements about its future growth prospects also played a role in the market's reaction (as is true with all stocks).

When the sales efforts to close business by the quarter end did not bear fruit, CA's senior management simply gave itself more time, and shifted the end of the quarter (and the beginning of the new quarter) until CA had enough business to meet the "Street's" expectations, and then lied about when that business was finalized. *See id.* ¶¶ 9-11. Indeed, three (3) of the Company's senior-most executives, Messrs. Kumar, Zar, and Richards, met informally each day for several days after the end of each quarter to size up the numbers and determine whether CA had, by that time, met or exceeded estimates (or if they needed to continue to extend the quarter and book additional business in this deferred "window").[39] *See id.* ¶ 9. Charles Wang also participated in certain of these meetings, and it was under his leadership that it became unacceptable for CA to miss Wall Street's expectations. In addition, those below Messrs. Wang, Kumar, Zar, and Richards, including Messrs. Rivard, Kaplan, and Silverstein, also played a role in these meetings, and routinely reported on the status of CA's numbers both before and after the quarter end.

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38 These estimates were broken down so that analysts "predicted the earnings per share" of CA stock. DPA, Stipulation of Facts ¶ 6.

39 Mr. Richards, who became the head of the North American division of Sales in 1999 and the head of Worldwide Sales in 2000, joined these discussions in 1999.

2. **Closing Back-End Loaded Quarters**

Compounding the problem – and very much related to it – was the fact that CA, like most software companies, struggled with "back-end loaded" quarters, a phenomenon commonly referred to as the "hockey stick effect."[40] That is, the overwhelming majority of CA's contract revenue generally did not arrive before the last week of the quarter, making the end of the quarter "a mad dash" to bring in revenue. Thus, at CA the quarter end was always chaotic and extraordinarily busy.

There were many factors that contributed to this "mad dash" around the quarter close:

First, as permitted under the applicable accounting rules, the Company booked the entire contract revenue from its license fees (even for multi-year contracts) upon execution of a contract – or "up front" – and generally derived its revenue from a relatively small number of large contracts. *See id.* ¶ 5.[41] Therefore, in order to make its numbers for the quarter, CA

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40 The term "hockey stick effect" was known throughout the software industry. Courts have described the phenomenon as follows:

> [L]icense revenues tend to come in within the last month of each quarter, a so-called "hockey stick effect." . . . The reason for the effect is well-understood. Purchasers of software harbor a belief, perhaps borne of experience or superstition, that sellers will cut the best deal near the end of a quarter because they are counting on the sale to make their quarterly projections. As a result, purchasers hold out until the end, trying to extract the last concessions before signing a binding deal. This leads to the last-minute booking of many sales when times are good, and the potential that many deals might fall through right before quarter's end or slip into later quarters if buyers are experiencing budget pressure. To the extent that the negative scenario is the one that pans out, there is the obvious risk that [a software company] will fail to meet its quarterly earnings projection.

In re Oracle Corp. Derivative Litig., 867 A.2d 904, 910 (Del. Ch. 2004).

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> [W]hen a software license agreement was finalized, for accounting purposes CA allocated its revenue among the license fee and the usage and maintenance fees, with 80 percent or more normally allocated to the license fee. CA then calculated the present value of the license fee, which was normally collected incrementally over the term of the agreement. The present value of the license

needed to negotiate and finalize many of the large contracts in its pipeline, even if it meant racing to do so at the end of the quarter.

Second, because CA sold computer software licenses, its products required almost no time or manpower to produce and ship (which was done by e-mail or overnight mail) to multiple customers once the original "code" was created, as required under the accounting rules.[42] Thus, even when the end of the quarter was fast approaching, CA always had the ability to deliver its product by the quarter end – or in CA's case close enough to quarter end to plausibly (albeit wrongly) account for transactions as though delivery on the contracts had occurred before the quarter-end cut-off.

Third, because the software cost little, if anything, to produce incrementally, a large portion of the revenue from a contract dropped directly to the Company's bottom line. Incremental costs arising from a new licensing deal were generally limited to sales commissions and other relatively insignificant costs. As such, finalizing one large additional contract could substantially aid CA in meeting estimates.

Finally, CA's customers exploited both CA's need for large contracts and its ability to deliver on those contracts quickly by waiting until the end of the quarter – when CA was perceived as "highly motivated" to obtain the contract revenue necessary to make its numbers – to negotiate with the Company. Indeed, customers found that when they delayed

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> fee, which was referred to within CA as the "GAAP Value," was then recognized as revenue in the quarter in which the agreement was purportedly finalized and signed.

DPA, Stipulation of Facts ¶ 5. This changed when the Company moved to the new business model, described below.

42 CA often "shipped" trial versions of its software out to clients before the end of a quarter so that they would have it in case a transaction was ultimately closed.

negotiations to the very last minute, they were able to "hold CA's feet to the fire" and extract concessions, such as large discounts or free products.

Yet, even with – or possibly because of – the negative impact the hockey stick effect had on CA's negotiating strength, the phenomenon only increased over time. Ultimately, CA's fiscal quarters grew to be so back-end loaded that the Company faced the prospect of closing nearly *all* of its contracts in the last few days of the quarter. For example, a June 29, 1999 e-mail from a vice president in Sales Accounting to David Rivard, less than two days before the close of the first quarter of fiscal year 2000, states: "% still missing is frightening!" *See* E-mail CA Sales Executive to David Rivard (June 29, 1999). An attachment to that e-mail reflects that, with two (2) days remaining in the quarter, ninety-eight percent (98%) of the contracts the Company expected to close in the quarter had not yet reached the Sales Accounting department. *Id.* In explaining the reason for the e-mail, Mr. Rivard remarked that Sales Accounting was preparing to "get slammed" with an enormous amount of work because of the number of contracts that had not yet been received. The increasing impact of the hockey stick effect resulted in a corresponding increase in the magnitude of the 35-Day Month practice.

B. ***The Scope and Impact of the Fraud***

In this environment, multiple former CA officers, executives and employees knowingly decided to break the law, booking extra contract revenue and reporting the inflated revenue totals to the public in order to meet expectations. DPA, Stipulation of Facts ¶ 7. While CA employees did not, in general, create fictitious contract revenue, they did artificially extend the Company's fiscal quarters, "keeping the books open" after the quarter close in order to prematurely recognize revenue on contracts negotiated and finalized in the early days of the subsequent quarter. *Id.* ¶ 9. This illegal practice, known as the 35-Day Month, was a long and systemic effort, requiring the knowledge and at least tacit cooperation and approval of many

CA executives and employees, from the junior to mid-level to senior employees. *Id.* ¶ 7. The SLC has concluded that the 35-Day Month was a direct result of the corporate culture created by Charles Wang, the Company's co-founder and driving force.

1. The Scope of the Fraud

(a) *The "Eternal" Nature of the Practice*

As far as the SLC can determine, CA employees engaged in the 35-Day Month practice at least as far back as 1984, and possibly before. *See* Kumar Fatico Hr'g Tr. 45-46, *U.S. v. Kumar*, 04 Cr. 846 (ILG) (E.D.N.Y. Oct. 23, 2006). Mr. Kumar told the SLC that the 35-Day Month practice existed at CA before he arrived in 1987. Mr. McElroy, who joined CA in 1988, told the SLC that the 35-Day Month practice existed as far back as he could remember. Messrs. Silverstein and Kaplan told the SLC that the 35-Day Month practice existed when each joined Sales Accounting in 1992 and 1993, respectively. Indeed, although he joined CA in 1998, Mr. Rivard told the SLC that the 35-Day Month practice "existed for as long as CA had been keeping records." Other witnesses conveyed the same sentiment, asserting that the practice "went on for years" prior to their joining the Company, or that it had simply gone on "forever."

(b) *The Pervasiveness of the Practice*

Given its long history, it was inevitable that the 35-Day Month practice would become part of CA's culture.[43] While this was evidenced by the guilty pleas of Messrs. Richards, Woghin, Zar, Kaplan, Rivard, and Silverstein – who, in total, headed every major non-development department at CA – an equally important indicator of the "systemic,

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43 The SLC was told that the 35-Day Month was also practiced at software companies that CA acquired. CA executives apparently asked about it as part of their diligence review during acquisitions and used its existence to negotiate a better purchase price. However, some witnesses have said that the practice at CA went so far "beyond" that which occurred at other companies that backdating contracts became known as the "CA way of doing business." *See U.S. v. Kumar*, Fatico Hr'g Tr., Oct. 23, 2006 at 46.

company-wide" nature of the practice was the fact that even lower-level employees perpetuated and took part in it. *See* DPA, Stipulation of Facts ¶ 7. For instance, both senior executives and lower-level staff were forced to work overtime to close deals that were negotiated post-quarter and were to be recognized in the prior quarter. According to Mr. Kumar, it was simply understood by everyone at CA that CA's quarters ran "from the 5th to the 5th." There were no "extra days," but, instead, the quarters themselves were shifted.

The practice permeated CA to such an extent that several employees told the SLC that "everybody" at the Company knew about it; no one bothered to hide it. Employees in the Sales, Sales Accounting, Legal, and Finance departments were overheard joking about contracts being executed on the "32nd of September" or the "33rd of March," and other fictional dates.[44] *See* E-mail from CA Controller to Steven Woghin (July 29, 1998). Long before investigators discovered it, CA employees themselves dubbed the practice the "35-Day Month." DPA, Stipulation of Facts ¶ 7. Moreover, this "dark" humor was not limited to employees that worked after the close of the quarter to book premature contract revenue. Employees in departments that were not involved in late contracting activity were also well aware of the practice, although not its illegality.

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44 In fact, an e-mail was circulated among CA employees on October 2, 2000 containing a fake press release entitled, "CA's Q3 Cut-short by late identification of calendar error." The press release announces that:

> an anomaly had been identified in respect to the Gregorian Calendar (that was introduced by Pope Gregory XIII in 1582) which is now used by most countries in the world. . . . [C]urrent research indicates that Chronologists at this time did not forsee [sic] the impending quarter-end pressures that would face companies like CA, and therefore no correction was made. There was also evidence of rampant embolism, the practice of inserting one or more days into a calendar in an attempt to keep it in phase with seasons. Over time this has had the effect of sales people believing that there is in fact more time to close business before the quarter-end, then there actually is.

Due to the open way in which the 35-Day Month practice was effectuated, practiced, and discussed, many CA employees simply assumed the practice was permissible, because it was "too obvious" and too pervasive to be unlawful.[45] Compounding this problem was the fact that, for most of its existence, CA did not provide any formal training or have any formal procedures with respect to revenue recognition, or other accounting practices, leaving employees to learn on the job.[46] According to these employees, they relied primarily upon their co-workers and occasional memoranda and e-mail reminders distributed by senior management regarding GAAP. *See, e.g.,* Memorandum from Charles McWade to CA's Financial Controllers (Aug. 13, 1997). This lack of training at CA, and the open manner in which quarter-ends were extended, allowed the 35-Day Month practice to be passed on from one generation of CA employees to the next without question.

(c) *"Blessing" the Practice*

Junior, mid-level, and senior-level employees also assumed that the 35-Day Month practice had been "blessed" by senior management and was otherwise proper. Senior executives sent out regular e-mails that helped their subordinates stay aware of the date to which quarters were to be artificially extended. For instance, on December 29, 1998, Mr. Rivard, in his first full quarter at CA, sent an e-mail to Messrs. Zar, Kaplan, and Silverstein

45 For instance, a manager in Sales Accounting backdated a letter to reflect the date of a backdated contract, which the letter was amending. *See* November 3, 2003 Preliminary [Oral] Report of the Audit Committee of CA on Certain Revenue Recognition Questions in the Fiscal Year Ended March 31, 2000, Exhibits Volume II, Exhibit 68. The letter, dated December 31, 1999, matter-of-factly refers to a phone conversation that occurred on January 12, 2000, thirteen days after the letter itself was supposedly sent: "I am enclosing for your records a revised counter-signed copy of your December 31, 1999 agreement . . . . The Order Form has been revised . . . in accordance with your phone conversation with [a regional vice president in CA's sales department] on January 12, 2000 . . . ." *Id.* The contract at issue was backdated and improperly recorded as revenue in the third quarter of fiscal year 2000.

46 For example, CA's sales accounting employees did not receive a desk set of procedures with respect to CA's accounting practices, or revenue recognition.

stating that "January 5 will be the last day of business for December." E-mail from David Rivard to Ira Zar, David Kaplan, and Lloyd Silverstein (Dec. 29, 1998).[47] Mr. Rivard then sent the message to an assistant vice president in Sales Accounting who disseminated it to numerous other employees involved in the contracting process. Likewise, senior executives sent word down the ladder when they wished to book contracts after what they had already deemed the "last day of business." These e-mails advised lower-level employees that certain late contracts "may be commissioned and/or booked" in the prior month. *See* E-mail from CA Sales Accounting Executive to David Rivard and CA Sales Accounting employees (Oct. 6, 1998).

E-mail was not the only method of communicating the practice. Employees merely had to reference the Finance department calendar to find out how long the Company's books would remain open in a given quarter. *See* E-mail from CA Finance employee to Finance and Financial Reporting employees (Sept. 28, 1998) ("Re: October 1998 World Calendar"). As Mr. Silverstein told the SLC, the quarter generally remained open until the third business day of a new fiscal quarter,[48] but the Finance department distributed a calendar that contained the dates on which the quarters were expected to close, because the exact dates would vary. The calendar also listed "every job that would run" during the year, including when "maintenance would run," when the "final invoice would run," and when the "cut-off would be" for contracts to be accepted in the quarter.

The casual discussion of the last day of business in e-mails and the Finance department calendar stood in stark contradistinction to e-mails sent during the period in which

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47 Another oft-used phrase was "projected close date." *See* E-mail from Lloyd Silverstein to a CA Sales executive (Aug. 23, 1999). Thus, on August 23, 1999, when a manager in the Sales department asked Mr. Silverstein for the "projected close date" for the second quarter of fiscal year 2000 (ending September 30, 1999), Mr. Silverstein replied "October 5th." *Id.*

48 This is consistent with Mr. Kumar's view that the quarters were not "extended" as much as "shifted."

CA executives attempted to implement a "hard close" at the end of the quarter. Those e-mails, which started to be circulated once CA began to countersign contracts prior to the quarter close in compliance with the two-signature requirement of SOP 97-2,[49] indicated that senior executives were enforcing a "hard close" in which "all agreements" were required to be "signed" and "products shipped" by "the last day of the calendar month." *See, e.g.,* E-mail from David Kaplan to multiple recipients (June 28, 2001). While in concept the "hard close" should have ended the 35-Day Month practice, in practice, it was for some period of time subject to the same manipulation as the regular quarter-end.

Moreover, the practice of backdating received widespread management approval. In an e-mail titled "Contract Signing Prep," Mr. Rivard announced that "dates typed in" to the "CA signature block [were] the same date as typed/written in [to the] Licensee signature block." E-mail from David Rivard to multiple recipients (Feb. 8, 2000). Mr. Rivard added parenthetically that the pre-printed signature block date was to be the "last day of [the] month/quarter," without regard for the actual date on which the contract was signed. *Id.* The use of "pre-printed" dates was another way that CA executives circumvented the true end of the quarter, and was simply backdating by another name since the effect was the same – misrepresenting the actual date on which a contract was completed.

As is discussed above, senior managers also actively "blessed" the 35-Day Month practice by specifically encouraging their subordinates to close and backdate individual deals after the quarter-end. For example, in an early April 2000 e-mail, CA employees

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49 Another issue identified in the DPA was CA's practice of not affixing its own signature to contracts within a given quarter, which was also a violation of GAAP. *See* DPA, Stipulation of Facts ¶¶ 13-16. This practice was identified by KPMG when it began to audit CA; KPMG told CA management that it had until the end of fiscal year 2000 to come into compliance, which KPMG thought CA then did. The SLC has found no evidence that the CA Board was made aware of this practice at the time.

referenced Mr. Richards as the senior executive who "pushed to get" a late contract executed and backdated for the quarter that closed on March 31, 2000. E-mail from former CA Sales Accounting executive to David Kaplan (Apr. 6, 2000) ("Re: Futuristic Deal – Late Entry!"). Because CA was "placed under pressure for revenue," lower-level employees were told that Mr. Richards had "cleared" the deal to be booked in the prior quarter. *Id.*

CA senior executives also provided justifications for the 35-Day Month practice. For instance, when Mr. Kaplan raised concerns about the practice early in his career, Mr. Zar, among others, gave him several reasons why it was "okay" for CA to engage in the 35-Day Month practice such as: (i) the vast majority of CA's revenue would be generated by contracts arriving at the end of a month and, because of this, CA needed several days to book contracts arriving at the end of the month; (ii) the true effective date of the contracts was in the prior quarter; (iii) the contract appeared to be signed by the customer within the prior quarter; (iv) the product was shipped in the prior quarter; and (v) the quarter was still ninety (90) days long, but it would simply shift five (5) days later, an immaterial fact.

Mr. Rivard also raised concerns when he joined CA from E&Y, but Mr. Zar gave him "numerous reasons" as to why the 35-Day Month practice was acceptable, including: (i) recognition of late revenue was justified because the contracts were multi-million dollar contracts with real value; (ii) the contract process did not start and end in two (2) days and therefore it made no sense to recognize a contract in the next quarter when the work on it had mostly been performed in the prior quarter; and (iii) deals were essentially done by the end of a quarter and the remaining work was merely "dotting i's and crossing t's." Mr. Zar sought to reassure Mr. Rivard by telling him that CA was working towards ending the 35-Day Month practice, and that CA was "a big ship and could not be turned around too quickly," particularly in a sales-driven culture.[50]

Indeed, Mr. Zar himself "bought into" the justifications provided by his superiors. Since he had no experience outside CA, Mr. Zar told the SLC that he was "indoctrinated" to view the 35-Day Month practice as normal, watching his superiors extend quarters in the same manner for many years before he became CFO. He was taught that the few extra days after the quarter end were not actually "post-quarter." Mr. Zar also saw the practical problems associated with letting deals "slip" in the days following the quarter-end, knowing that if a deal did not close, CA would have to wait until the end of the next quarter for it to close. In the intervening months, there was a risk the client might be acquired, reduce their budget, or any other number of scenarios that would cause CA to lose the business.

(d) *The CEOs' Encouragement of the Practice*

As noted above, the "tone at the top" encouraged this practice and allowed it to flourish. Under Mr. Wang, CA was known as a "one-headed" dragon, and no significant decisions were made without his participation and approval. Indeed, it was clear at the highest levels of management that even Mr. Kumar worked for Mr. Wang, and that Mr. Kumar was executing Mr. Wang's directives. Based upon statements made by nearly all witnesses that the SLC interviewed, the SLC determined that the 35-Day Month practice began on Mr. Wang's watch. As discussed above, the SLC found that the 35-Day Month pre-dated Mr. Kumar's arrival to CA in 1987, and existed and expanded throughout Mr. Wang's tenure as CEO. The SLC found further that Mr. Wang encouraged and participated in the practice.

Mr. Kumar, who was the Company's public face, and, from 1994 to August

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50 Mr. Zar told the SLC that he does not recall such conversations.

2000, President and COO under Mr. Wang, executed the 35-Day Month practice, often at the explicit direction of Mr. Wang (and at other times to avoid Mr. Wang's anger). Mr. Kumar's own criminal conduct is clear, undisputed, and admitted: (i) he personally directed CA salespersons to backdate contracts to make it appear as if they had been signed in the prior quarter (Kumar/Richards Superseding Indictment ¶¶ 24, 34, 42, 47-49); (ii) he directed other CA senior executives to issue the same instructions (Kumar/Richards Superseding Indictment ¶¶ 42-43); (iii) he negotiated and signed agreements on behalf of CA after the quarter end that were backdated to appear as if they were completed in the prior quarter or left them intentionally undated (Kumar/Richards Superseding Indictment ¶¶ 29, 41); and (iv) he directed the meetings with CA executives at which it was determined how long fiscal quarters would be extended (Kumar/Richards Superseding Indictment ¶¶ 22-23).

Indeed, after the end of the first quarter of fiscal year 2000, in the first week of July 1999, Mr. Kumar, at the direction of Mr. Wang, flew to France to close a deal worth approximately $32 million to CA. The contract, which Mr. Kumar signed, was backdated and recognized in the first quarter. The next quarter, Mr. Kumar let it be known to CA's senior sales managers that he was not happy that he had to "save" the prior quarter for CA. As such, at the end of the second quarter, Mr. Kumar insisted that CA's regional sales managers travel to corporate headquarters in Islandia to close the quarter. As a result, the regional sales managers, then under the direct supervision of Mr. Kumar, continued to close business for the second quarter from Islandia during the first week of October 1999.

Mr. Kumar also pulled his senior executives, including Mr. Woghin, the Company's former General Counsel, who was not routinely involved in sales transactions, into the backdating scheme. For example, in early January 2000 after the end of a particularly difficult quarter, Mr. Kumar told Mr. Woghin that CA was in the process of negotiating a $300 million contract, and instructed him to work with a senior CA Sales executive to "get the deal done." Mr. Woghin complied, and after he had resolved all of the outstanding legal issues in the proposed contract, Mr. Kumar told Mr. Woghin to send the final draft of the contract directly to him. Ultimately, the customer and Mr. Kumar, on behalf of CA, executed the agreement, which intentionally omitted the date block beneath each signature, leaving in the recital that the contract had an effective date of December 31, 1999. This allowed CA to improperly book $180 million of GAAP revenue in the third quarter of fiscal year 2000, which ended on December 31, 1999. *See* Kumar/Richards Superseding Indictment ¶ 41.

These are but three (3) vivid examples of Mr. Kumar's participation in, and encouragement of, the 35-Day Month practice, and how he co-opted other members of senior management along the way.

2. **The Financial Impact of the Practice**

The scope of the 35-Day Month practice at CA was truly enormous, as was its impact on CA's publicly reported financial statements. For example, in fiscal year 2000 alone, which ran from April 1, 1999 to March 31, 2000, CA improperly recognized revenue from approximately 165 license agreements with an aggregate GAAP value of approximately $1.75 billion. *See* DPA, Stipulation of Facts ¶¶ 13-16. For fiscal year 2000, CA reported $6.103 billion in revenue, meaning that 28.7% of its revenue came from the improperly booked contracts. *Id.* In addition, the 35-Day Month practice allowed CA to report continuous growth, another closely watched indicator of CA's success, when in fact, CA's growth was unsteady.

C. ***The Criminal Defendants and Departmental Roles***

To appreciate how the 35-Day Month practice operated in practice at CA, the SLC sought to understand the role played by each of the CA executives who has pled guilty.

Because each of the seven (7) Criminal Defendants led a different department at CA – Sales, Sales Accounting, Finance, Financial Reporting, Global Sales Organization, and Legal – the story of how those defendants participated in the 35-Day Month practice is best told within the structural framework of CA itself.

1. **CA's Sales Department**

Sales was the foundation of the CA empire, with Mr. Kumar – by all accounts a superb salesman – at the helm, and Mr. Richards ranking as his top aide and right hand man.[51] Sales, which was responsible for identifying potential contract opportunities, meeting with CA customers, negotiating the terms and conditions of contracts, and then obtaining the customer's signature, was the first link in the chain that effectuated the 35-Day Month.[52]

Until April 2000, Sales was organized geographically,[53] with general managers taking responsibility for assigned continental divisions and reporting to senior management, while regional managers and Sales representatives in the field reported to the general managers. At the beginning of each quarter, CA Sales managers attended quarterly Sales meetings, led by Mr. Wang and later Mr. Kumar, at which the Sales managers discussed the deals they had closed for the prior quarter, and their sales forecasts for the current quarter. According to Mr.

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51 As noted above, from December 1998 to April 2000, Mr. Richards was the head of North American Sales, reporting directly to Mr. Kumar. In April 2000, Mr. Richards became the Executive Vice President of Worldwide Sales, a position that had been vacant since Richard Chiarello left the Company in December 1998.

52 Assisting the Sales force was the Pre-Sales group. Its members, including defendant Russell Artzt, worked as "talking heads" and "evangelists" for CA technology. The group members also functioned as "hammers," in that they would go to clients late in the negotiation process to attempt to convince them that they needed CA's products. However, the group was not typically involved in the negotiations over particular terms and conditions that preceded the execution of the contract.

53 At the start of fiscal year 2001, Sales was restructured along product lines (*e.g.*, Enterprise, Information, Management, Mainframe, and Services), with geographical distinctions existing only within each product group.

Kumar, at these meetings it was not unusual for there to be discussion about deals that had closed after the quarter end, but were nonetheless recognized in the prior quarter. CA Sales managers then communicated sales quotas to their subordinates, and Sales personnel worked through the quarter, and beyond, to meet those goals.

CA's Sales managers later attended a second quarterly meeting at the beginning of the third and final month of the quarter, again led Mr. Wang and then Mr. Kumar, at which the Sales managers discussed the deals they still needed to close in order to achieve the numbers they had forecasted and committed to. According to Sales employees, they worked on deals for a particular quarter until they were told that the quarter had "closed," which, as discussed above, was often three (3) to five (5) days after the calendar date on which the quarter should have closed. *See* DPA, Stipulation of Facts ¶ 9.

At CA, this three (3) to five (5) day period was often referred to as the "flash period." *Id.* At most companies, a flash period is typically the period in which preliminary quarterly results are calculated. Not so at CA, where the flash period – which was really viewed as a continuation of the quarter – was used to negotiate and close new deals to be booked in the prior period.[54] *Id.* ¶¶ 7, 9-10.

Notwithstanding the fact that CA's quarters were shifted by several days, Sales employees also knew that, to be counted as revenue in a quarter, a contract closed within the flash period had to bear a customer signature date within the prior quarter. *See* Memorandum from Lloyd Silverstein to CA Sales employees at 2 (Oct. 15, 2002). Accordingly, Sales personnel used different tactics to ensure that contracts were "properly" backdated. First, Sales

54 As discussed above, senior-level managers often sent out e-mails to communicate "the last day of business" for an artificially extended quarter indicating when negotiations truly had to conclude for the quarter.

personnel asked customers to re-sign an agreement completed during the flash period, with a new date indicating that it was signed by the customer prior to the quarter end. Second, and more often, CA Sales personnel gave contracts to customers for signature post-quarter with pre-printed date blocks bearing the date of the last day of the prior quarter. This use of pre-printed dates to backdate contracts became the dominant method of backdating in late 1998 or early 1999.

At times, customers recognized that CA was engaged in wrongful conduct, and resisted CA's backdating efforts. For example, on April 7, 2000, Messrs. Richards and Kumar told a CA salesperson to ask a customer to execute an agreement worth $16 million with an execution date of March 31, 2000. *See* Kumar/Richards Superseding Indictment ¶ 28. The customer refused to sign the backdated contract, but agreed to sign the agreement without an execution date. *Id.* After the customer signed the agreement, Mr. Richards instructed the CA salesperson to write in an execution date of March 31, 2000. *Id.; see also* April 6, 2000 E-mail from CA Sales Executive to Messrs. Kumar and Richards (Apr. 6, 2000).

In a sales-driven culture, the Sales department, at the direction of senior management, was the driving force behind the 35-Day Month practice, which then required the participation of the Company's other non-revenue generating departments.

2. **CA's Finance Department**

The Finance department was responsible for "closing" the quarter, including tabulating CA's quarterly revenues on a contract-by-contract basis (Kaplan Information ¶ 7) and therefore its participation was essential to effectuate the 35-Day Month practice. The role of the Finance department is best explained by discussing the individuals who ran it during the period of the 35-Day Month, and the tools that they used to track CA's financial performance on a daily basis.

Peter Schwartz. From 1985 to June 22, 1998, the Finance department was led by Peter Schwartz, CA's then-CFO, who, as discussed below, resigned following the vesting of the KESOP (although he stayed on for several months in an operating capacity). Mr. Schwartz fiercely adhered to the hierarchical nature of CA, keeping the employees that worked below him shielded from contact with any senior-level decision-making and decision-makers. For instance, Mr. Kaplan, who reported directly to Mr. Schwartz, told the SLC that he never communicated with anyone above Mr. Schwartz; and, indeed, similarly, Mr. Kaplan commented that he rarely communicated with Mr. Schwartz. Mr. Kaplan explained that decision-making at CA was reserved to a very small cadre of executives.

According to witnesses, including those that reported directly to him, Mr. Schwartz not only "clearly knew" about the 35-Day Month practice, but also helped to implement it.[55] During his tenure as CFO, Mr. Schwartz is reported to have been part of the "foundation" of the 35-Day Month practice, determining when to close the quarter for accounting purposes. Witnesses told the SLC that Mr. Schwartz also advised Finance personnel that holding quarters open was a legitimate accounting technique, and in some instances explicitly encouraged backdating. For instance, Mr. Schwartz told a Sales employee that he could not be commissioned unless the date on a contract was changed to make it appear as though the contract was executed in the prior quarter. According to Mr. Kumar, he questioned Mr. Schwartz about the quarter-end shift, and Mr. Schwartz told Mr. Kumar that accounting for such things was "his problem" and not Mr. Kumar's. Mr. Silverstein told the SLC that CA employees would routinely go into Mr. Schwartz's office in the first days of the new quarter and discuss the status of deals listed on the Status Reports (discussed below) that

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55 It should be noted that Mr. Zar, Mr. Schwartz's successor, did not have any information regarding Mr. Schwartz's knowledge of, or participation in, the 35-Day Month practice.

were then recognized in the prior quarter even though they had not been consummated by the quarter end.

During his interview with the SLC, Mr. Schwartz denied any knowledge of the 35-Day Month practice. Mr. Schwartz professed surprise to learn that contracts were backdated when he was CFO, and stated that he personally took steps to ensure that contracts were signed in the proper quarter before they could be recognized as revenue. Although he admitted to the existence of a "flash period," he defined it only as a period in which CA "counted everything," not a period in which contracts continued to be executed and booked as revenue.

However, given the weight of the evidence described in this report, understanding Mr. Schwartz's role at the Company and his hands-on management style, and having had the opportunity to observe him in person, the SLC does not find Mr. Schwartz's account credible.

Ira Zar. Mr. Zar joined CA immediately after graduating from college, and was appointed CFO in June 1998 at age thirty-six (36) with no experience outside of CA. Mr. Zar's appointment is viewed by the SLC as an attempt by Mr. Wang to ensure that he was surrounded by smart, but less than savvy and seasoned, executives beholden to him, who were therefore unable to exercise independent judgment. Mr. Zar, by all accounts Mr. Schwartz's protégé, plainly admitted – both in connection with his guilty plea and in his interviews with the SLC – the existence of the 35-Day Month practice during his tenure as CFO. *See* Zar Plea Tr. at 37-38. In post-quarter meetings with Messrs. Wang, Kumar, and Richards on the "flash date" (the last day of the flash period), Mr. Zar printed the "flash report" and discussed with Messrs. Kumar and Richards the "preliminary" results for the quarter. *See* Kumar/Richards Superseding Indictment ¶ 23; Zar Plea Tr. at 11-14. If CA had not yet generated enough revenue to meet estimates by this time, Messrs. Wang and Kumar instructed Mr. Zar to continue to keep CA's books open after the flash period, which he did, while they attempted to finalize additional deals that were supposedly in the pipeline. *See* Kumar/Richards Superseding Indictment ¶ 222; DPA, Stipulation of Facts ¶10. Mr. Zar knew this was wrong at the time, yet remained complicit. *See* Zar Plea Tr. at 38.

3. CA's Sales Accounting Department

The Sales Accounting department, headed by Mr. Rivard beginning in August 1998,[56] was responsible for (i) ensuring contracts met revenue recognition requirements prior to execution and booking, (ii) executing contracts on behalf of CA, and (iii) entering contract information into CA's databases for booking. *See* Rivard Information ¶ 7. While Sales brought in the backdated deals, and Finance prematurely recognized the revenue from those deals, the Sales Accounting department functioned as a middleman, assisting Sales with terms and conditions during contract negotiations to facilitate revenue recognition, executing backdated contracts on CA's behalf, concealing evidence of the fraud, and providing backdated deals to Finance for booking.

As one of his early acts as CFO, Mr. Zar recruited Mr. Rivard to CA from E&Y to head Sales Accounting. Because of his outside perspective, Mr. Rivard quickly recognized that the 35-Day Month was improper, but did nothing to stop it. *See* Rivard Plea Tr. at 32-34. Swayed by the assurances he received from Messrs. Zar and Kaplan that this was how companies operated in the "real world," and that he would find the same thing at any other software company he went to work for, he chose to stay at CA and, according to Mr. Rivard, help to gradually improve CA's practices.

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56 Before Mr. Rivard, Mr. Zar headed Sales Accounting. Mr. McWade was the head of Sales Accounting in the mid-1980s.

Notwithstanding his intentions, Mr. Rivard assisted Sales employees in negotiating contracts beyond the quarter end, knowing that those contracts, once executed, would be recognized in the prior quarter. For example, Mr. Rivard was involved in the negotiation of a license agreement that continued past September 30, 1999 and into the first week of October. October 14, 2003 [Oral] Preliminary Report of the Audit Committee of CA on Certain Revenue Recognition Questions in the Fiscal Year Ended March 31, 2000, Exhibits Volume I, at Exhibits 7-16. The deal was finally executed by the customer on October 5, 1999, but bore a date of September 30, 1999 in both signature blocks. Mr. Rivard signed the contract on behalf of CA, knowing that the dates accompanying the customer's signature and his own were false. *See* October 14, 2003 Preliminary [Oral] Report of the Audit Committee of CA on Certain Revenue Recognition Questions in the Fiscal Year Ended March 31, 2000, Exhibits Volume II, at Exhibit 70, 81; Rivard Plea Tr. at 32.

Finally, the Sales Accounting department took charge of "cleaning up" completed contracts for presentation to CA's outside auditors – which was significant since CA's auditors only reviewed final contracts for revenue recognition purposes. *See* DPA, Stipulation of Facts ¶ 12. Following the close of the quarter, Mr. Rivard instructed Sales Accounting personnel "to remove all processing notations" – that is, to use White-Out to conceal the "fax lines," which would have otherwise showed the true time and date that the contract was received by Sales Accounting from Sales personnel in the field. *See id.*; Rivard Plea Tr. at 32. Although Mr. Rivard first "pushed back" against this procedure, Mr. Zar convinced him that it was "easier" than waiting for the original contracts to arrive (which would not contain incriminating fax lines), and Mr. Kaplan suggested that the action was par for the course.

4. CA's Global Sales Organization

The GSO, which was established in 1998, worked as a "liaison" between the Finance, Legal, and Sales departments by assisting with the approval of contractual terms and conditions. The ostensible purpose for the GSO was to implement tighter controls on the discounts Sales employees offered customers, typically at quarter end. In this role, the GSO reviewed business proposals submitted by Sales personnel, and assisted in negotiating business-related issues. Mr. Silverstein, as head of the GSO, assisted Sales personnel in the negotiation of the contracts. *See* Silverstein Plea Tr. at 19.

Prior to commencing contract negotiations with a customer, Sales personnel were required to prepare a Business Analysis and Review Form ("BARF") that outlined the proposed transaction, including the discounts and concessions the Sales employee was considering offering to the customer. *see also* Preliminary [Oral] Report of the Audit Committee of CA on Certain Revenue Recognition Questions in the FY Ended March 31, 2000, Exhibits Volume II, at Tab 85. This form was then submitted to the GSO for approval, and then modified as the business terms changed during the course of negotiations.

While checking the level of discounts authorized to customers was the GSO's primary responsibility, it also dealt with discreet licensing issues and other issues brought to its attention by the Legal department. Once a deal was executed, the Sales employee responsible for the deal created a final version of the BARF, which was then approved by the GSO. Generally, CA would not recognize revenue from a contract until the BARF received all necessary approvals, including from the GSO, Legal, and Sales Accounting. In addition, contracts valued over a threshold amount had to be approved by the GSO before revenue could be recognized. *See* Silverstein Compl. ¶ 20. In many cases, the BARFs indicated that business terms were being negotiated past the quarter end, and, likewise, final GSO approval came after the end of the quarter in which the contract was booked. (*See* November 3, 2003 Preliminary [Oral] Report of the Audit Committee of CA on Certain Revenue Recognition Questions in the Fiscal Year Ended March 31, 2000, Exhibits Volume I, at Exhibit 8; *id.*, Exhibits Volume II, at Exhibits 57, 58).

To further the 35-Day Month practice, Mr. Silverstein, and others in the GSO, communicated to CA Sales personnel that "it was okay to backdate contracts and make it look as though the deals had been signed in the [prior] quarter." Silverstein Plea Tr. at 20. Much of the GSO staff either assumed or knew that backdated contracts were booked in the quarter prior to that in which they were actually signed. For his part, Mr. Silverstein became aware that backdated contracts were being prematurely recognized shortly after he joined the Sales Accounting department in 1992, and brought the issue to the attention of Mr. Zar, among others. Mr. Zar told Mr. Silverstein that he should not concern himself with when revenue was recognized, and Mr. Silverstein was told by others that even though the practice was wrong, it was immaterial. *See id.* at 19-20. After receiving these assurances, Mr. Silverstein continued to participate in the 35-Day Month practice. *See id.* at 20.

5. **CA's Legal Department**

In the context of the contract licensing process, the Legal department was responsible for providing approvals for non-standard contractual language, without which Sales executives could not execute a non-standard license agreement. Likewise, the Finance department would not recognize revenue from non-standard contracts until the Legal department approved them. Since most CA deals were large and complex, they frequently contained non-standard contractual language, thereby requiring the input of, and approval from, the Legal department.

While in some instances the Legal department participated in the 35-Day Month practice by actively covering up fraud and misrepresenting signature dates, its most persistent failure was in turning a blind eye to the improper activities of others, thereby allowing the practice to flourish. CA lawyers worked in tandem with Sales personnel and others in the negotiation of contracts after the quarter end, oftentimes with the understanding that the revenue from those contracts would be recognized in the prior quarter. *See* Woghin Plea Tr. at 28. Nonetheless, CA's lawyers chose to believe that somehow CA's Finance department ensured that CA stayed within the applicable accounting rules. In this way, CA's lawyers facilitated the 35-Day Month practice, and failed in their roles as gatekeepers to protect CA.

Mr. Woghin, CA's General Counsel, pled guilty to participating in the 35-Day Month practice, and allowing others in the Legal department to do the same. Mr. Woghin allowed the Legal department personnel "to routinely participate in the negotiation and drafting of software license agreements on behalf of CA during the week following the calendar end of fiscal quarters." *Id.* Mr. Woghin understood that this post-quarter activity was meant to "generate revenue for CA which could be improperly recognized in the prior fiscal quarter." *Id.* Attorneys in the Legal department were available at the quarter end and thereafter, and often worked around the clock to assist in closing deals. CA's in-house counsel did not stop working until an announcement had been made that the quarter had closed.

Mr. Woghin and Mr. McElroy, who were both senior CA lawyers, did more than allow the junior lawyers to facilitate the practice; they were, at times, active participants. As discussed above, Mr. Woghin finalized a contract for Mr. Kumar during the first week of January 2000 with a date of December 31, and revenue from this contract was recognized in the December quarter. *See id.* While Mr. Kumar did not explicitly tell Mr. Woghin that the contract would be prematurely recognized for revenue recognition purposes, Mr. Woghin understood as much. Mr. Woghin took no steps to find out how the revenue from the contract was recognized; rather, he admittedly "stuck his head in the sand" when he knew that Mr. Kumar was "scrambling for revenue" after the quarter had already closed.

Mr. McElroy, CA's most senior licensing attorney – responsible for international transactions – also participated in the 35-Day Month practice. Indeed, Mr. McElroy admitted his involvement in the 35-Day Month practice to the SLC, stating that he participated in the modification of contracts after the close of a quarter, and that he had "assumed" that, if the contract bore a signature date from the prior quarter, revenue from that contract would be recognized in that quarter. Mr. McElroy told the SLC that he also assumed that CA's Finance department ensured that CA stayed within applicable accounting guidelines, and that while his participation in the 35-Day Month practice "may have been wrongful," he did not know – or want to know – this at the time.[57]

VII. ADDITIONAL ACCOUNTING ISSUES

The 2005 Derivative Action alleges that certain CA executives manipulated CA's accounting through other means in addition to the 35-Day Month practice. The complaint alleges four (4) additional improper practices, that (i) CA double-booked revenue upon the extension or renewal of contracts (2005 Derivative Compl. ¶ 52), (ii) CA improperly allocated revenue from maintenance fees to license fees (*id.* ¶ 49), (iii) CA improperly allocated revenue to products such as Unicenter that were given to customers for free (*id.* ¶ 51), and (iv) CA

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57 Moreover, CA's attorneys casually discussed participating in the practice over lunch, "griping" about how the intense post-quarter negotiations caused them to work late hours and "ruined" their New Years celebrations. And, as noted above, CA attorneys regularly joked about the 35-Day Month practice, with one CA lawyer making his way around the office wishing his colleagues a "Happy March 33rd." These lawyers assumed or recognized that they were assisting in the improper booking of revenue, yet none took any steps to stop it.

improperly recognized license revenue from contracts with extended payment terms (*id.* ¶ 53). Plaintiffs allege no particularized facts, and provide no detail, to support these allegations. Rather, these allegations appear to be reprinted from the 1998 and 2002 Class Actions. *See* Am. and Consolidated Compl. For Violations of the Securities Exchange Act of 1934, *In re Computer Associates 2002 Class Action Sec. Litig.* ¶¶ 5, 34-38, 41-50, 64-69, 02 Civ. 1226 (TCP) (Oct. 22, 2002); Class Action Compl. for Violations of Federal Securities Laws, *Barroway v. Computer Associates Int'l, Inc.*, 98 Civ. 4839 (TCP) (July 21, 1998).

These additional issues are dealt with in a separate report by the SLC and are not addressed here for two (2) primary reasons: (i) the additional accounting issues were the primary subject of both the Class Actions, and the four-year-long government investigation, and there is no evidence that the Board was ever informed that CA's practices were improper, with the exception of CA's cancel/convert accounting for which CA issued a reclassification, which was publicly disclosed on May 15, 2000, that did not adversely impact CA's stock price and was later determined by PwC to be immaterial; and (ii) given the harm caused to the Company by the 35-Day Month practice, it alone provides a more than sufficient basis on which to evaluate the merits of each of the claims in the 2005 Derivative Action. As such, those issues will not be addressed herein.

VIII. Board Oversight During the Period of Fraudulent Conduct

The SLC has uncovered no facts to support any claim or argument that CA's non-management outside directors were aware of the 35-Day Month practice while it was occurring. Indeed, those directly involved in the fraud have told the SLC that, in their view, the outside directors could not have known, given the active concealment of the fraud, the role of the Board, and lack of software experience on the Board. Thus, the SLC set out to determine whether, in light of the applicable legal standards, there were "red flags" that the outside directors were aware of, or should have been aware of, but nonetheless ignored. As noted above, the 2005 Derivative Complaint identifies no red flags that would have alerted the outside directors to the existence of the 35-Day Month practice, so the SLC began its analysis by identifying what it believed were key events at CA, analyzing whether those events were red flags, and examining the Board's response to those events.

A. *The Key Employee Stock Ownership Plan*

On May 25, 1995, CA's Board approved the KESOP in an effort to "enhance shareholder value by encourag[ing], recogniz[ing] and reward[ing] sustained outstanding individual performance by certain key employees who are largely responsible for the management, growth and protection of [CA's] business." *See* Computer Assocs. Int'l, Inc., Proxy Statement (Form DEF 14A) (July 6, 1995) ("1995 Proxy"); KESOP § 1.1. Those "key employees" were CA's three (3) most senior executives – Charles Wang (CA's then-Chairman and CEO), Sanjay Kumar (CA's then-President and COO), and Russell Artzt (CA's then-Executive Vice President of Research and Development). KESOP § 2.1.9. CA shareholders approved the KESOP on August 19, 1995, retroactive to May 25, 1995.

1. **The Origination of the KESOP**

The idea for the KESOP dated from late 1994, when Charles Wang raised the notion of an executive compensation package with Willem de Vogel, who was then the chair of CA's Compensation Committee. Mr. Wang initially proposed the idea to Mr. de Vogel specifically as a means to incentivize Mr. Kumar, who was second in command to Mr. Wang, to remain with CA. By that time, Mr. Kumar's meteoric rise through the management ranks at CA was noteworthy, and he had been identified as the heir apparent to Mr. Wang. Messrs.

Wang and Kumar were, at that time, very close, as exemplified by the fact that in the early 1990s, Mr. Kumar supplanted Tony Wang, Charles Wang's brother, as the CA executive responsible for running the day-to-day operations at CA. Mr. Wang told Mr. de Vogel that he was concerned that Mr. Kumar would be recruited away from CA, and he wanted to ensure that Mr. Kumar's financial stake in CA was substantial enough to prevent him from leaving.

It appears that this view was shared by the CA Board as a whole, which was concerned about retaining CA's senior management during the beginning of the software industry boom that occurred in the mid-1990s. The highly regarded Mr. Kumar was viewed by the Board as a whole as a "plumb target for any technology types," and thus particularly vulnerable.[58]

What later became the KESOP took shape over a series of informal meetings between Mr. Wang and Mr. de Vogel. These conversations, and the resulting outline of a concept, ultimately precipitated a meeting at CA headquarters, at which Mr. de Vogel, Mr. Grasso, and Irving Goldstein,[59] the members of the Board's Compensation Committee, with the assistance of Pearl Meyer, then of the well-known executive compensation consulting firm, Frederic W. Cook & Co, created the KESOP.

As the KESOP began to take shape, Mr. Wang made clear his view that, as co-founder and CEO of the Company, the Compensation Committee should not only include him in the KESOP, but make him its largest beneficiary. Mr. de Vogel acquiesced to this demand,

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58 Mr. de Vogel reported to the SLC that Mr. Schwartz, CA's CFO, was angry about the decision to exclude him and believed that it was unfair. Mr. Kumar told the SLC that Mr. Wang did not want Mr. Schwartz included in the plan, and sought to exclude him from a similar plan following the KESOP.

59 At this time, the CA Board consisted of Directors Artzt, de Vogel, Goldstein, Grasso, Kenny, Kumar, Wang, and Edward C. Lord. Mr. Goldstein, who was a graduate of Queens college with Mr. Wang, was a member of the CA Board and Chair of the Audit Committee from 1990 until his death in May 2000. Mr. Lord was a member of the CA Board from 1988 to March 1996. 1995 Proxy.

since in his view, at the time the KESOP was being considered, Mr. Wang did not have a sufficiently large ownership stake in CA, and the stock he did own was not tied to his remaining at CA.[60] Directors Grasso and Kenny also believed that Mr. Wang should be included in the KESOP both as a retention tool (they viewed him as the founder, driving force, and public face of CA) and to reward him for his continued service to CA. One final consideration that drove Mr. Wang's inclusion in the KESOP was that it persuaded him to sign a non-competition agreement with CA, something he had refused to do in the past.

The Compensation Committee included Mr. Artzt in the KESOP because he was a co-founder of the Company, along with Mr. Wang, and because it viewed his technological expertise as important to CA's future success. The Compensation Committee also believed that Mr. Artzt (i) knew the Company very well, (ii) served as an important intermediary between Messrs. Wang and Kumar, and (iii) was important to developing "a successor generation of leadership" at CA.

2. The Structure of the KESOP: The Connection Between the KESOP and CA's Share Price

The Compensation Committee tied the KESOP's vesting provisions to the Company's share price – as opposed to revenue or earnings targets – because it believed this was the best way to increase "shareholder value." That is, the Compensation Committee believed that if it set a "very high" target price for the KESOP's vesting provisions, and these provisions were met or exceeded, both the shareholders and the CA executives would benefit.

The notion of increasing shareholder value also led the Compensation Committee to design the KESOP as a restricted stock grant, as opposed to an award of stock

60 As of the filing of CA's July 6, 1995 Proxy Statement in which the KESOP was proposed to CA's shareholders, Mr. Wang owned 7,966,614 shares, or approximately five percent (5%), of CA's outstanding common stock. *See* 1995 Proxy.

options. Mr. de Vogel favored a restricted stock grant over stock options, believing that restricted stock put the CA executives in the same shoes as CA's shareholders, and would make the plan more transparent. Mr. Grasso told the SLC that, in his view, according to the Black-Scholes pricing model and the prevailing market view on valuation, it made more sense to the Compensation Committee to use restricted stock rather than options.

As for the size of the KESOP, the Compensation Committee intended to compensate the KESOP Defendants in a manner that was commensurate with CA's peer companies. *See* Grasso Dep. 16:9-16, Oct. 17, 2001. The Compensation Committee, with assistance from its outside consultants, looked at what they believed was "reasonable" compensation when compared with other top executives in its industry, and found that the industry standard at the time was to provide top management with the opportunity to earn a three-to-five-percent (3-5%) ownership interest in the company over a three-to-five-year period. *See* de Vogel Dep. 34-35:22-25, 1-4, Sept. 24, 2001. Accordingly, the KESOP was designed with these targets in mind.

3. The Mechanics of the KESOP

(a) *The Grant Provisions*

As initially drafted, the KESOP authorized the Compensation Committee to grant up to 6,000,000 shares of CA common stock to be divided among the beneficiaries in certain percentages, that is: Mr. Wang would receive sixty percent (60%) of any grant, Mr. Kumar would receive thirty percent (30%), and Mr. Artzt would receive ten percent (10%). *See* KESOP §§ 3.1, 3.2. The KESOP authorized an immediate grant of 2,000,000 shares (the "Initial Grant") that would vest on March 31, 2000 (the "Normal Vesting Date") in certain percentages, depending on the performance of CA's common stock (the "Normal Vesting Conditions"). *See* KESOP §§ 2.1.6, 2.1.7, 3.2, 4.3. Further, the KESOP authorized the

Compensation Committee to grant up to an additional 4,000,000 shares (the "Additional Grant") if CA's stock price met or exceeded certain targets in a given year (the "Grant Provisions"). *See* KESOP § 3.3; *see* Appendix A. Any Additional Grants made by the Compensation Committee were subject to the same Normal Vesting Date and Normal Vesting Conditions as the Initial Grant. See KESOP §§ 2.1.6, 2.1.7, 3.2, 4.3.

Following the creation of the KESOP, CA declared three (3) separate three-for-two stock splits, which became effective on September 6, 1995, July 16, 1996, November 28, 1997, respectively. The KESOP provided that the target prices for both the Grant Provisions and the Normal Vesting Conditions be adjusted to account for these stock splits. *See* KESOP § 3.3. In addition, the Compensation Committee proportionally increased the number of shares granted pursuant to each three-for-two split. As a result, the Initial Grant increased to 6,750,000 shares, and the Additional Grant increased to 13,500,000 shares. Thus, in sum, following the CA stock splits, the KESOP Defendants were eligible to earn 20,250,000 CA shares.

(b) *The Vesting Provisions*

Because the KESOP was intended as a retention tool, the Initial Grant and any Additional Grants required the beneficiaries to remain employed at CA until the Normal Vesting Date (March 31, 2000) or all shares granted to them under the KESOP (both the Initial Grant and the Additional Grants) would be forfeited, unless the shares had already vested pursuant to the accelerated vesting schedule, as described below. *See* KESOP § 4.1. Section 4.3 of the KESOP provided the Normal Vesting Conditions for the KESOP shares:

(i) Under § 4.3.1, if CA's closing stock price were to exceed $38.81[61] for any sixty trading days during CA's fiscal year 2000, then all shares in the Initial Grant and any Additional Shares would vest in their entirety.

[61] All share prices are adjusted for the three three-for-two stock splits.

(ii) Under § 4.3.2, if CA's closing stock price were to exceed $31.11 for any sixty trading days during CA's fiscal year 2000, but were not to exceed $38.81 for sixty trading days, then forty percent (40%) of the shares in the Initial Grant would vest and all other shares would be forfeited.

(iii) Under § 4.3.3, if CA's closing stock price were to exceed $22.22 for any sixty trading days during CA's fiscal year 2000, but were not to exceed $31.10 for sixty trading days, then twenty percent (20%) of the shares in the Initial Grant would vest and all other shares would be forfeited.

(iv) Also under § 4.3.3, if CA's closing price were to exceed $22.22 for any sixty trading days prior to the Normal Vesting Date, then twenty percent (20%) of the shares in the Initial Grant would vest (although they would remain subject to forfeiture under § 4.1 if the employee left the Company prior to March 31, 2000).

(c) *The KESOP's Accelerated Vesting Provisions*

The KESOP also contained an "accelerated" vesting provision, which enumerated the conditions pursuant to which *all* shares granted under the KESOP would vest immediately and no longer be subject to forfeiture (the "Accelerated Vesting Provision"). *See* KESOP § 4.4. Under the Accelerated Vesting Provision, if CA's stock price closed at or above $53.33 on any sixty (60) trading days during any twelve-month period prior to the Normal Vesting Date of March 31, 2000, all shares granted in the Initial Grant and any Additional Grants would vest immediately. *See* KESOP § 4.4. Once vested, the shares were no longer subject to forfeiture, although they were subject to limitations on transfer for up to seven years following the vesting.[62] *See* KESOP § 5.1. As described below, the KESOP Defendants were awarded the majority of their shares pursuant to the accelerated vesting clause.

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62 However, the Compensation Committee lifted all transfer restrictions on Mr. Wang's KESOP shares upon his retirement from CA. *See* Minutes of a Meeting of the CA Board at 2 (Feb. 28, 2003). The Compensation Committee also lifted the transfer restrictions on a large portion of Mr. Kumar's KESOP shares to allow him to use the shares as collateral for a loan. On May 20, 2005, the SLC sent letters to counsel for Messrs. Wang, Kumar, and Artzt, apprising them of the SLC's investigation and requesting that their clients refrain from pledging, disposing, gifting, or otherwise transferring any stock issued to them pursuant to the KESOP. *See* Letter from David Hennes to Vincent Sama, counsel for Mr. Wang,

B. ***The KESOP Shares Vest***

On May 21, 1998, two days after a joint Audit Committee and Board Meeting, CA's share price closed above the $53.33 target for sixty (60) days in a twelve-month period, thereby triggering the KESOP's Accelerated Vesting Provision. *See* KESOP § 4.4. As a result, the remainder of the Initial Grant (5,400,000 shares) and all Additional Grants (13,500,000 shares) vested;[63] in addition, the total award, including shares granted earlier under another provision of the KESOP, was no longer subject to forfeiture.[64] *See* KESOP §§ 3.2, 3.3, 4.1, 4.4. On the date of vesting, the 18,900,000 CA shares were worth $1.04 billion.[65] It is undisputed that, at the time, the KESOP resulted in one of the largest payouts in U.S. Corporate history.[66] On June 12, 1998, after an adjustment for taxes, CA transferred the shares to the beneficiaries. Computer Assocs. Int'l, Inc., Proxy Statement (Form DEF 14A) (July 2, 1998) ("1998 Proxy").[67] Subsequently, in March 2000, as part of a settlement of derivative litigation relating to the grant provisions of the KESOP – unrelated to any allegations of accounting fraud – the

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(May 20, 2005); Letter from David Hennes to Stephen Kesselman, counsel for Mr. Artzt, (May 20, 2005); Letter from David Hennes to Eric Halper, counsel for Mr. Kumar, (May 20, 2005).

63 In total, Mr. Wang received 11,340,000 shares, Mr. Kumar received 5,670,000 shares, and Mr. Artzt received 1,890,000 shares pursuant to the KESOP.

64 On January 11, 1996, CA's share price met the Normal Vesting Condition enumerated in § 4.3.3 and twenty percent (20%) of the Initial Grant, 1,350,000 CA shares, vested: 810,000 shares for Mr. Wang, 405,000 for Mr. Kumar, and 135,000 for Mr. Artzt. *See* Computer Associates Int'l, Inc., Definitive Proxy Statement (Form Def 14A) at 12 (July 10, 1996). However, because they vested under the Normal Vesting Conditions, the shares of each executive were still subject to forfeiture if that executive left the Company before March 31, 2000. *See* KESOP § 4.3.3. Nonetheless, when the Accelerated Vesting Condition was satisfied, as discussed above, these shares were no longer subject to forfeiture. *See* KESOP §§ 4.1, 4.4.

65 At the time of the award, CA had a market capitalization of $30 billion, and its stock traded at $54.95. *See* Computer Associates Int'l, Inc., Annual Report (Form 10-K) at 3 (May 22, 1998).

66 *See supra* note 11.

67 CA issued Mr. Wang 9,334,205 shares, Mr. Kumar 4,088,130 shares, and Mr. Artzt 1,320,931 shares. 1998 Proxy at 18.

KESOP Defendants agreed to return a total of 4,500,000 KESOP shares to the Company. Stipulation of Settlement at ¶ 1, *Sanders v. Wang*, 98 Civ. 4961 (TCP).[68]

Because the KESOP was tied to CA's share price, the SLC sought to determine to what degree, if any, the 35-Day Month practice affected the vesting of the KESOP. The SLC also examined whether the accelerated vesting of the KESOP was a red flag, and, if it was, whether the Board took any steps to investigate CA's financial health at a time when this historic transfer of shareholder wealth occurred.

As discussed above, the SLC has concluded that the origins of the 35-Day Month practice predated the vesting of the KESOP by many years. Thus, the SLC retained PwC to determine whether CA's reported financial results were overstated due to the practice during 1997 and 1998.[69] The SLC has concluded, based on PwC's work and its investigation, that CA's financial statements and publicly reported growth rate were materially overstated in fiscal year 1998 (April 1, 1997 through March 31, 1998), and the first quarter of fiscal year 1999 (April 1 through June 30, 1998), the quarter in which the KESOP vested.

The SLC also retained Professor Ray Ball, the Sidney Davidson Professor of Accounting at the University of Chicago Graduate School of Business, to determine what impact disclosure of the fraud and CA's true financial results would have had on CA's stock price. Professor Ball concluded that had the 35-Day Month practice been disclosed to the market in mid-1998, CA's stock price would have declined thirty-seven percent (37%). To put

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68 As noted above, the plaintiffs in that case alleged that the Board improperly adjusted the KESOP grant to account for three separate three-for-two CA stock splits, and the Delaware Court of Chancery agreed. *See Sanders v. Wang*, 1999 WL 1044880, at *6 (Del. Ch. Nov. 10, 1999). As part of the settlement, Mr. Wang returned 2,700,000 shares to the Company, Mr. Kumar returned 1,350,000 shares, and Mr. Artzt returned 450,000 shares. Stipulation of Settlement at ¶ 1, *Sanders v. Wang*, 98 Civ 4961 (TCP).

69 CA's restatement, issued on April 26, 2004, did not cover this period. Computer Associates Int'l, Inc., Unscheduled Material Events (Form 8-K) at 5-7 (April 26, 2004).

it simply, had the real facts been known, the KESOP shares would not have vested on May 21, 1998, and Messrs. Wang, Kumar, and Artzt would not have received over $1 billion in CA stock.

At the Board level, prior to the KESOP vesting, the CA Board, as a whole, did not specifically monitor CA's share price in connection with the vesting of the KESOP, nor did it take any extra, incremental steps to ensure that CA's financials were accurate. Indeed, other than several directors loosely monitoring the number of days that CA's share price traded above $53.33, none of the Board members can recall doing anything special or different related to the impending vesting. Likewise, the Board took no additional steps, formal or informal, to verify CA's financials before or after the KESOP vested.

The directors interviewed by the SLC uniformly expressed the view that since they generally and regularly took appropriate steps to ensure the accuracy of CA's financial results, there was no need to take additional steps before or after the KESOP vested. Indeed, on May 19, 1998, two days before the KESOP vested, CA's Audit Committee met and received E&Y's "clean" audit opinion for fiscal year 1998, which ended on March 31, 1998. *See* Minutes of a Meeting of the CA Board at 1-2 (May 19, 1998). Shortly thereafter, the Audit Committee reviewed E&Y's management letter, which reported no material weaknesses. *See* Minutes of a Meeting of the CA Audit Comm. at 1-2 (Aug. 12, 1998). Finally, there is no evidence that any of the Board or Audit Committee's advisors, legal or accounting, recommended that the Company perform any additional work or testing in light of the vesting.

C. ***The Promulgation of SOP 97-2***

During the vesting period for the KESOP, and prior to the actual vesting, the accounting rules governing software revenue recognition changed materially. On December 15, 1997, AICPA promulgated Statement of Position ("SOP") 97-2, which became effective for

CA on April 1, 1998, the start of CA's fiscal year 1999.[70] *See* SOP 97-2 c.92. SOP 97-2 required that a software vendor, such as CA, meet four criteria before revenue may be recognized: (i) persuasive evidence that an arrangement exists; (ii) delivery of the product has occurred; (iii) the vendor fee is fixed or determinable; and (iv) collectability of the vendor fee is probable. SOP 97-2 c.08. SOP 97-2 makes clear that for a software vendor that "has a customary business practice of utilizing written contracts," such as CA, "evidence of the arrangement," pursuant to (i) above, "is provided only by a contract signed by *both* parties." SOP 97-2 c.16 (emphasis added).[71]

The promulgation of SOP 97-2, which drew substantial industry attention, provided a clear opportunity for the Board to examine CA's revenue recognition practices in closer detail. CA's outside auditor at the time, E&Y, provided repeated assurances to the Audit Committee that CA's accounting practices were sound with respect to SOP 97-2:

- At a January 27, 1997 Audit Committee meeting, Jerry Reynolds and Mark Wovsaniker of E&Y "reviewed a number of existing and proposed FASB and ACSEC pronouncements. With the possible exception of FAS 123 and the forthcoming revision of SOP 91-1, none of these standards would have any material impact on the Company. They felt comfortable that the prior year's work with FAS 123 and on-going liaison on SOP 91-1 would minimize the effect of these pronouncements." Minutes of a Meeting of the CA Audit Comm. at 1 (Jan. 27, 1997).

- At an August 13, 1997 Audit Committee meeting, Mr. Wovsaniker "advised the Committee that the release of an updated SOP on revenue recognition (a clarification of SOP 91-1) was imminent, but that he did not anticipate a major impact on CA. He also stated that he felt that *the Company had good financial controls and was conservative in its accounting approach generally*." Minutes of a Meeting of the CA Audit Comm. at 1

70 Prior to the enactment of SOP 97-2, software companies, including CA, had to meet the revenue recognition requirements of SOP 91-1. SOP 97-2 c.01.

71 Before the enactment of SOP 97-2, SOP 91-1 had required that "even if all other requirements set forth in this SOP for recognition of revenue are met, revenue should not be recognized on those licenses until persuasive evidence of the agreement exists. Such evidence is usually provided by the signed contract." Douglas Carmichael, "Is it Time to Record the Sale? Software Revenue Recognition Under SOP 97-2," *The CPA Journal*, July 1998, available at *www.nysscpa.org/cpajournal/1998/0798/features/f440798.htm* (citing SOP 91-1).

(Aug. 13, 1997) (emphasis added). At that time, E&Y presented its March 31, 1997 management letter to the Audit Committee, which states that although E&Y did not "anticipate that the revisions to the SOP [would] significantly impact the Company financially, certain administrative and sales accounting internal controls could be impacted." Letter from E&Y to the CA Audit Comm. at 1 (May 23, 1997). The management letter recommended that CA implement certain controls regarding revenue recognition issues. *Id.* At the August 13 meeting, management reported that most of the recommendations had been implemented or were intended to be implemented. *See* Minutes of a Meeting of the CA Audit Comm. at 1 (Aug. 13, 1997).

- At a February 23, 1998 Audit Committee meeting, Mr. Wovsaniker briefed the Audit Committee on the implications of SOP 97-2, which at that time did not yet apply to CA, and told the Audit Committee that it "would have *almost no impact on the Company's operations or financial results*" (with the exception of several paragraphs unrelated to the requirement that a signed contract exist before revenue can be recognized). Minutes of a Meeting of the CA Audit Comm. at 1 (Feb. 23, 1998) (emphasis added).

- At a May 19, 1998 joint Board and Audit Committee meeting, Mr. Wovsaniker stated that SOP 97-2 was "*not expected to have a material impact on [CA's] revenue recognition*." Minutes of a Meeting of the CA Board and Audit Comm. at 2 (May 19, 1998) (emphasis added).

- At an August 12, 1998 Audit Committee meeting, Mr. Wovsaniker, in discussing SOP 97-2, told the Audit Committee that he "believed *the Company was in compliance with the provision[]*." Minutes of a Meeting of the CA Audit Comm. at 2 (Aug. 12, 1998) (emphasis added). At that time, Mr. Wovsaniker suggested that CA continue to monitor its business to ensure that CA remained in compliance. *Id.*

D. ***The July 21, 1998 Press Release***

The vesting of the KESOP had at least one unintended consequence, as it reportedly caused CA's then-CFO, Peter Schwartz, to resign. It was the common belief at CA that Mr. Schwartz was unhappy both at the size of the KESOP and the fact that he was not included as a beneficiary. Although Mr. Schwartz denied both motivations as a basis for his departure, he agreed that it was his view that the KESOP was far richer than he thought appropriate. According to Mr. Kumar, Mr. Schwartz had a falling out with Mr. Wang over his exclusion from a subsequent compensation plan, which prompted his resignation.[72]

To replace Mr. Schwartz, Mr. Wang recommended to the Board, with Mr. Kumar's support, that it appoint thirty-six year-old Ira Zar as CA's new CFO. At the time that Mr. Zar was recommended to succeed Mr. Schwartz, the Board was presented with no alternative candidates, either external or internal. Indeed, Mr. Kumar told the SLC that Mr. Wang chose Mr. Zar precisely because he was "in the CA family," and that Mr. Wang only considered Charles McWade and Abraham Poznanski,[73] who were also members of the "CA family," as alternative candidates for the position.[74] At a June 22, 1998 Board meeting, "[a]fter discussion of Mr. Zar's background and experience gained during his sixteen years of employment by the Corporation," the Board appointed Mr. Zar to be CA's next CFO. Minutes of a Meeting of the CA Board at 2 (June 22, 1998).

On July 20, 1998 – less than sixty (60) days after the KESOP vested – the CA Board held its regularly scheduled quarterly meeting. *See* Minutes of a Meeting of the CA Board at 1 (July 20, 1998). Mr. Zar, who was making his first presentation to the Board as CFO, reviewed CA's financial performance for the first quarter of fiscal year 1999 and

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72 Although Mr. Schwartz's resignation was technically dated June 22, 1998, he continued to function as an executive officer of the Company through the summer of 1998. For example, he played a substantial role at the Company's July 20, 1998 Board meeting and participated in the analyst calls that occurred on July 21, 1998.

73 Mr. Poznanski had previously served as CA CFO from 1981 to 1985, and in 1998 was Senior Vice President of the Internal Audit department, .

74 According to Mr. Kumar, Mr. Wang's CFO search was not limited to insiders because he feared that an outsider would expose the 35-Day Month practice, and reiterated a theme that the SLC heard time and again – that no one thought about the 35-Day Month practice as "wrong" while it was being perpetrated, and therefore fear of its discovery did not generally factor into senior management's decisions.

provided a projected outlook for the second quarter. *Id.*[75] When Mr. Zar completed giving his presentation, according to the minutes of the meeting, Mr. Kumar told his fellow Board members that "some large customers of the Corporation that are doing business in Asia have been reducing their spending and appear to be deferring purchase decisions in light of the current economic uncertainty in Asia." *Id.* at 2. Mr. Kumar explained to the Board that he had just come back from a conference in Australia where he had met with CA's top salespeople from around the world, and they had reported to him the impact the Asian economic crisis was having on CA's multi-national business. Sanjay Kumar Dep. 237-239, Aug. 7, 2001. Mr. Wang added that he also had recently visited Asia, and that he had observed that business there "had slowed to a halt." *See id.* During its investigation, the SLC has found no indication or evidence that CA management presented any financial analysis or extrinsic data to support their concerns, or a quantification of the expected decline in growth, and the CA Board did not ask them to do so.

Nonetheless, the Board members, led by Mr. Grasso, determined that this information was material, and that CA needed to promptly disclose the information to the market. The CA Board, which had been presented with a draft press release for approval, recommended that it be revised to reflect the stated concerns. *See* Minutes of a Meeting of the CA Board at 2 (July 20, 1998). It was the view of Mr. Woghin, confirmed by Mr. Kumar, that management did not intend to create a disclosable event, but rather to simply condition the Board for possible reduced performance in the coming months.

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75 As noted above, Mr. Zar was appointed CFO on June 22, 1998, and this was the first Board meeting that he had ever attended. Mr. Zar said that he was very scared that he would be asked a question to which he would not know the answer, given his inexperience as CFO, and therefore did not speak at the meeting, except to present his report to the Board. Mr. Schwartz, whom Mr. Zar had been chosen to replace, participated at this meeting on a substantive level.

Interestingly, Mr. Kumar's recollection of these events differs from the recollections of all other attendees at the meeting. According to Mr. Kumar, it was Mr. Schwartz who raised concerns about the impact of the Asian economic crisis. Indeed, Mr. Kumar recalled being shocked that Mr. Schwartz had raised the issue to the Board without first discussing it with management, and trying, in vain, to persuade the Board to take additional time to understand the situation before issuing a public statement. Mr. Kumar's recollection is consistent with the testimony he gave in his August 7, 2001 deposition in the 1998 Class Action Litigation. *See* Kumar Dep. 237-39. Mr. Schwartz had no recollection of the details of this meeting, either in his August 16, 2001 deposition in the Class Actions or his August 1, 2006 interview with the SLC. *See* Schwartz Dep. 97-101, dated Aug. 14, 2001. In any event, the issue of who raised this issue is not material to the SLC's consideration of the issue.

On July 21, 1998, after the close of trading on the NYSE, CA announced its quarterly results. CA announced that it had met Wall Street EPS estimates of $0.34 (excluding the charge taken for the KESOP vesting). Press Release, Computer Assocs. Int'l, Inc., Computer Associates Reports Record First Quarter, Operating Earnings Up 25% (July 21, 1998). However, in that press release, CA cautioned the market that "the ripple effect of the Asian economic turmoil on our multinational clients . . . coupled with deferred software purchasing decisions as customers deal with their 'Y2K' projects and mainframe hardware transition issues, leads us to believe that our revenue and earnings growth will slow over the next several quarters." *Id.*[76] The next day, CA's share price fell thirty-one percent (31%).

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76 Notably, while the press release mentions Y2K concerns, there is no mention of Y2K concerns in the July 20, 1998 Board minutes and none of the directors interviewed by the SLC recall it being discussed. *See* Minutes of a Meeting of the CA Board at 2 (July 20, 1998). Recollections vary, but some at the meeting recall discussing the mainframe transition issue, but none recall discussing Y2K, although that was an issue of constant discussion in the period leading up to January 1, 2000.

The share price decline resulting from the July 21 press release did not prompt action by the Board. At no point following the July 20 Board meeting, or following the stock market response to the July 21 press release, did the Board take any steps to determine when CA management learned of the information concerning the expected slowing of CA's growth rate. In particular, the Board took no steps to determine if Messrs. Kumar or Wang were aware of this issue before the KESOP vested, or whether there was a link between the timing of when they "learned" of this information and the vesting of the KESOP. Indeed, no director appears to have ever raised the question of whether – had the issue been known and disclosed two (2) months earlier – the $1 billion in KESOP shares would have vested.

E. ***Derivative and Class Action Litigation Filed in Response to the KESOP and the July 21 Press Release***

1. **The 1998 Class Actions**

The linkage, however, was not lost on the securities plaintiffs' bar, and others at CA. As described above, between July 1998 and October 1998, eleven (11) putative class action complaints were filed against CA and Messrs. Wang, Kumar, and Artzt in the Eastern District, which were later consolidated into a single litigation, the 1998 Class Action. The 1998 Class Action alleged that CA began to experience serious financial problems prior to the vesting of the KESOP, and that the financial slide led CA to begin artificially inflating its revenues, in part, to protect the KESOP beneficiaries' interests in the accelerated vesting. The plaintiffs claimed, among other things, that CA was (i) inflating revenue by recognizing revenue on long-term contracts upfront, purportedly in violation of GAAP, (ii) offering excessive discounts to make revenue appear larger on certain products, and (iii) otherwise engaging in improper revenue recognition practices that artificially inflated CA's operating revenue. However, *none of these lawsuits allege that CA was using a "35-Day Month" or backdating contracts*.

2. **The 1998 Derivative Actions**

In addition, in July and August 1998, derivative lawsuits were also filed in both the Eastern District and the Delaware Court of Chancery. Plaintiffs in those derivative actions argued that the KESOP authorized the Compensation Committee to grant the KESOP Defendants six million shares in total, and did not permit any adjustments for stock splits or dividends on any shares, which adjustment the Compensation Committee had made, as described above. The derivative action filed in the Eastern District also contained allegations of fraud, similar to those made in the 1998 Class Action, but likewise included no allegations of a "35-Day Month" or backdating.

The Board received an update about these lawsuits at an August 12, 1998 Board meeting. *See* Minutes of a Meeting of the CA Board (Aug. 12, 1998); Woghin Talking Points at 1 (Aug. 12, 2998).[77] At that time, Mr. Woghin told the Board that the class action lawsuits had no merit, but rather "are based solely on a theory that there 'must have been' fraud because Charles, Sanjay and Russ had a motive to keep the stock price high until their shares vested under [the KESOP], and, for that reason, wrongfully delayed in issuing the cautionary warning eventually included in the July earnings release." Woghin Talking Points at 1 (Aug. 12, 1998).

With regard to the derivative lawsuits, Mr. Woghin told the Board that the plaintiffs claimed that "Charles, Sanjay and Russ defrauded CA by maintaining the share price artificially high for their own financial gain, thereby committing fraud, and that all the directors breached their duty of care by allowing this to happen." *Id.* Mr. Woghin told the Board that the

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[77] At that time the Board was comprised of Directors Artzt, de Vogel, Goldstein, Grasso, Kenny, Kumar, and Wang, and retained this composition until May 2001.

"allegations of all the complaints are extremely thin," and that the Company had "a reasonably good shot" at achieving dismissal of the derivative lawsuit due to the shareholders' failure to make a demand. *Id.* at 1-2.

The final comment in Mr. Woghin's talking points states: "Bottom line is that we have been through this before. We know what to expect and how to deal with it through very effective counsel." *Id.* at 2. This was the message that the Board received – that these were strike suits that would be dealt with in the ordinary course of business. As new directors joined the Board through the course of the litigation, they were similarly assured that there was no merit to the litigation.

The SLC viewed the filing of these lawsuits as the end of a series of events starting with the vesting of the KESOP, which could have prompted the Board to more closely examine the Company's financial health. However, not even the filing of the lawsuits, which explicitly linked the KESOP and the July 21 press release, caused the Board to take steps, formal or informal, to examine these events and their linkage, if any. With regard to the lawsuits, the Board universally believed, based on Mr. Woghin's advice, and its own experiences with class action litigation, that the lawsuits were without merit.

F. ***CA Changes Outside Auditors from E&Y to KPMG***

The vesting of the KESOP required the Company to take a $675 million charge against earnings in the first quarter of fiscal year 1999 (the "KESOP charge"), ending June 30, 1998. This caused CA to report a $481 million loss for the quarter. *Id.* When the KESOP was created, E&Y advised the Compensation Committee that when it vested, the charge would be a "one-time" charge – meaning that it would happen only in one (1) fiscal quarter – that would be taken in the quarter with the majority of the days in which CA's share price closed at or over $53.33. *See* de Vogel Dep. 37-38.

Under this scenario, the charge would have been taken in the fourth quarter of fiscal year 1998, ending March 31, 1998. When the vesting of the KESOP became likely, E&Y changed its advice, advising CA to take the charge over two (2) quarters, divided by the percentage of days that CA's stock traded over the required price. Finally, right before the KESOP actually vested, E&Y changed its advice again, advising CA to take a one-time charge in the quarter that the KESOP actually vested, which CA did. E&Y's constantly changing advice caused great unhappiness at CA. *See* Minutes of a Meeting of the CA Board and Audit Comm. at 2 (May 19, 1998).

This issue came to a head at the May 19 joint Board and Audit Committee Meeting. Mr. Wovsaniker, the lead E&Y partner for the CA audit, told the Board that because E&Y could not predict with certainty when the KESOP would vest, it would be most appropriate to recognize the KESOP charge as of the day the target is actually reached. *See id.* This had the effect of pushing the charge into the first quarter of fiscal year 1999 – the then-current period – rather than the already-closed fourth quarter of fiscal year 1998. More importantly, from the Board's perspective, this would focus even more attention on the KESOP, because the KESOP charge would affect CA's current earnings. The Board ultimately acquiesced to Mr. Wovsaniker's position, but not without a considerable amount of frustration and dissatisfaction with E&Y. *See* Minutes of a Meeting of the CA Audit Comm. at 1-2 (Aug. 12, 1998).

The Board's unhappiness with E&Y's change in position led the Board to seek to replace E&Y. *See* Minutes of a Meeting of the CA Board at 2 (May 26, 1999). At an August

12, 1998 Audit Committee meeting, Mr. Goldstein, then-Chair of the Audit Committee – speaking on behalf of the Board – "expressed dissatisfaction with the untimely nature of Ernst & Young's guidance respecting the timing of the charge for the" KESOP. *See* Minutes of a Meeting of the CA Audit Comm. at 1-2 (Aug. 12, 1998). The E&Y representatives present, Thomas Hudgins, Mark Wovsaniker, and Martin Shannon, told the Audit Committee that E&Y would provide more timely advice in the future. *See id.* at 2. CA's dissatisfaction with E&Y continued into 1999. At a May 26, 1999 Board meeting, Mr. Kumar reported to the Board on a meeting he had with the then-Chairman of E&Y to discuss the inconsistency of E&Y's advice with respect to the KESOP charge. *See* Minutes of a Meeting of the CA Board at 2 (May 26, 1999).[78] The minutes of that Board meeting reflect that the directors "expressed displeasure with the quality and consistency of the advice given by Ernst & Young," and directed management to consider retaining the services of another of the major auditing firms to replace E&Y. *Id.* at 2.

At a June 18, 1999 Audit Committee meeting, Mr. Zar presented his recommendation for a possible replacement for E&Y, in the event that the Board decided to make a switch. *See* Minutes of a Meeting of the CA Audit Comm. at 1-2 (June 18, 1999). Mr. Zar told the Audit Committee that throughout his search for a potential replacement, he had considered the factors that had contributed to the Board's dissatisfaction with E&Y, "including lack of decisiveness, inconsistency in advice, and less than effective advocacy in professional associations." *Id.* at 2. Mr. Zar then proposed KPMG and PwC as the best candidates, and advised the Committee that, in his view, KPMG would be the best choice due to its prior

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78 The May 26 meeting was Roel Pieper's first meeting as a director. At this time the Board was comprised of directors Artzt, de Vogel, Goldstein, Grasso, Kenny, Kumar, Pieper, and Wang.

experience with the Company.[79] *Id.* Ultimately, at a June 29, 1999 Board meeting, after considering the proposals of, and meeting with representatives from KPMG, PwC, and E&Y, the Board selected KPMG to replace E&Y. *See* Minutes of a Meeting of the CA Board at 2 (June 29, 1999).[80]

At an August 25, 1999 Audit Committee meeting, Mark Goodburn of KPMG, the new lead partner for the CA audit, reported that KPMG had successfully transitioned onto the CA account and, in the course of that transition, had, among other things, reviewed E&Y's workpapers for the fiscal year 1999 audit. *See* Minutes of a Meeting of the CA Audit Comm. at 1-2 (Aug. 25, 1999). At a follow-up Audit Committee meeting on August 31, 1999, KPMG representatives presented their plan for CA's fiscal year 2000 audit. *See* Minutes of a Meeting of the CA Audit Comm. at 1-2 (Aug. 31, 1999). As part of that plan, Mr. Goodburn told the Audit Committee that KPMG "intended to take a 'fresh look' at the Corporation's accounting practices." *Id.* at 2.

In the fall of 1999, KPMG raised with CA management the issue of CA's compliance with the two-signature requirement of SOP 97-2. Prior to this time, CA had, as a matter of practice (and in contravention of the plain language of SOP 97-2), failed to countersign agreements prior to the quarter-end. This is because CA considered a contract binding upon receiving the customer's signature, and considered its own signature to be

79 KPMG audited the books of four of CA's European subsidiaries and Platinum Technology International, Inc., which was acquired by CA in April 1999.

80 The Board elected Alfonse D'Amato to the Board at this meeting, effective immediately. *See* Minutes of a Meeting of the CA Board at 2 (June 29, 1999). Mr. D'Amato's first meeting as a director was the July 15, 1999 meeting. *See* Minutes of a Meeting of the CA Board at 2 (July 15, 1999). Once Mr. D'Amato joined the Board, it was comprised of directors Wang, Artzt, Kumar, Grasso, Kenny, de Vogel, Pieper, and Goldstein.

irrelevant. *Id.* E&Y had not raised this as an issue with CA.[81] When KPMG reviewed CA's practices, it told CA that under SOP 97-2 all contracts had to be fully executed by *both* parties by the quarter-end, and gave CA until the fourth quarter of fiscal year 2000 (ending March 31, 2000) to come into compliance. *Id.* at 15-16.

CA management resisted this approach, arguing that it would be physically impossible for CA to timely countersign all of its license agreements, because only a few executives had the authority to sign contracts on behalf of CA, and the majority of CA's contracts came in on the final night of the quarter. *Id.* at 15. CA management ultimately agreed to bring the Company into compliance, and purportedly did so, by implementing a "hard close," discussed above, whereby all paperwork for contracts had to be processed before the quarter end. *See, e.g.* E-mail from Sanjay Kumar to CA Sales executive (Jan. 13, 2000).

At a January 25, 2000 Audit Committee meeting, KPMG representatives reported on the first six (6) months of their audit work. *See* Minutes of a Meeting of the CA Audit Comm. at 2 (Jan. 25, 2000). Mr. Goodburn reported that he anticipated that KPMG would audit transactions accounting for at least eighty-five percent (85%) of the Company's revenue worldwide. *Id.* Mr. Goodburn also described "the efforts that KPMG would devote to reviewing the quality of the Corporation's internal communications and accounting policies, with particular attention to its policies regarding execution of contracts." *Id.*

81 In its March 31, 1998 management letter, E&Y suggested that there were "sales contracts for which the Company did not countersign a contract due to a dispute with the customer over contract terms and/or acceptance signatures were not dated." Letter from E&Y to the CA Audit Comm. at 1 (May 26, 1999). However, E&Y did not associate these sales contracts with a general practice of failing to sign or date CA's own signature on contracts, along with when there was no dispute over contract terms. In addition, E&Y told CA that this issue, among several others noted in the same section of the letter, was not "material to consolidated results," either "individually or in the aggregate." *Id.*

By the end of fiscal year 2000, KPMG believed that the Company had moved into compliance on the counter-signature issue, and KPMG's management letter, dated September 27, 2000, does not identify the countersignature issue as a problem. With respect to CA's internal controls, KPMG's management letter states that it:

- "would generally characterize the Company's accounting systems and related processes as being less integrated and requiring more manual intervention than is typical for enterprises of similar size and breadth." Letter from KPMG to the CA Audit Comm. at 1 (Sept. 27, 2000).

- "[t]he Company's finance staff requires an understanding of off-line processes or familiarity with a generally oral history of transactions. This dependency contributes to the risk of errors in the accounting and financial reporting process." *Id.* at 2.

- KPMG concluded that "[t]he Company does not have a comprehensive set of written accounting policies and procedures." *Id.*

Finally, KPMG recommended that CA, "at a minimum," develop a set of desk procedures summarizing key accounting policies and procedures. *Id.* The Audit Committee – then comprised of directors de Vogel, Goldstein, and Kenny – reviewed the September 27 management letter with KPMG at an October 24, 2000 Audit Committee meeting. At that time, Mr. Zar advised the Audit Committee that the Company was in the process of preparing such desk procedures. *See* Minutes of a Meeting of the CA Audit Comm. at 2 (Oct. 24, 2000).

G. *CA's "New Business Model"*

In May 2000, CA's senior management approached the Board with the idea of changing CA's then-existing up-front revenue recognition system to a "new business model," whereby, among other things, revenue would be recognized ratably over the life of the agreement. *See* Minutes of a Meeting of the CA Board at 2 (May 11, 2000). While this change had many legitimate reasons – indeed, it was considered a "best practice" by some – certain members of CA's management (not Mr. Kumar) also saw the change as a way to end the 35-

Day Month practice, since the end of the quarter push to find new business (the hockey stick effect) would no longer be needed. As such, the SLC sought to determine whether the Board expressed any skepticism about the need for the switch, or whether it suspected that the switch might be a cover for improper revenue recognition practices.

At a May 11, 2000 Board Meeting, Messrs. Kumar and Wang (with Mr. Kumar taking the lead) presented the new business model to the Board. *See* Minutes of a Meeting of the CA Board at 2 (May 11, 2000). Mr. Kumar told the Board that CA had "to get out of this mode" – booking nearly all of CA's revenue at the end of a quarter. Mr. Kumar also warned the Board that it would be impossible for CA to continue growing under the old model, because approximately seventy-five percent (75%) or more of CA's sales were completed in the last few days of the quarter. The Board was told that switching to the new business model would significantly reduce the bargaining power held by the Company's customers to negotiate discounts at the end of the quarter. In short, Mr. Kumar, who was the driving force behind the new business model, believed that the primary benefit of the new model was that it would allow CA to sell software in a different way and with more flexibility than its competitors.

The Board was aware of the issues surrounding the race at the quarter close, both at CA and in the industry as a whole, and the Board discussed how a new model could alleviate the quarter-end pressures and reduce the Company's vulnerabilities with respect to discounts. For example, Mr. Pieper, who also sat on the Board of Veritas Software, which he claimed pioneered the ratable revenue recognition model in the software industry, attested to the benefits of such a model. Further, management's suggestion that CA switch to the new business model was not the first time the idea of ratable revenue recognition had been raised at the Board level, as the idea was periodically raised by Mr. Kumar and discussed at Audit

Committee meetings. The Board universally believed that the switch was requested to end "the hockey stick effect," and it had no reason to suspect that management had other, unstated, reasons for changing to the new business model. Likewise, the SLC found no evidence to suggest that the Board suspected that ending the 35-Day Month practice was a motive for management's proposal to switch to the new business model.

The Board was generally supportive of the switch and thought Mr. Kumar had presented powerful arguments to support the change. However, the Board did not approve the new business model at the May 11 Board meeting since the directors were concerned about Wall Street's reaction and felt that management's "execution plan" would not be effective, i.e., that the Company was not prepared to effectively communicate the model to Wall Street. The Board feared that if not communicated properly, switching to the new business model would make it appear to the investing community as though the Company's revenue numbers had dramatically decreased. Accordingly, the Board asked management to prepare a pro forma model of CA's financial statements demonstrating what the previous five (5) years would have looked like under the new business model, and a comprehensive plan for educating Wall Street. CA management promptly began working to provide the Board with the requested information.[82]

Management next proposed the new business model in July 2000, but again the Board rejected the idea. Finally, in October 2000, having gathered enough data to provide the Board with sufficient financial comparisons to previous years, management "re-pitched" the new business model. Mr. Kumar "requested that the Directors consider adopting a new business model for the Corporation that he believed would have several material benefits for the

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82 Indeed, Mr. Kumar told the SLC that Mr. Wang was extremely concerned about Wall Street's reaction to the presentation of CA's financials under the new business model, and asked how he was going to explain to his mother how CA went from a $6 billion company to a $3 billion company seemingly overnight.

Corporation including relieving pressure on the Corporation's negotiations with customers concerning discounts; providing greater visibility into future revenue streams; and adding greater flexibility to the terms of the Corporation's licensing transactions." Minutes of a Meeting of the CA Board at 2 (Oct. 24, 2000). After further debate, the Board decided to adopt the model. On October 25, 2000, CA issued a press release announcing this "dramatic shift in its business model." Computer Assocs. Int'l, Inc., Unscheduled Material Events (Form 8-K) at 12 (October 25, 2000).

H. ***April 29, 2001 New York Times Article***

In late March 2001, CA's senior management discovered, through internet postings and information from former CA employees, that Alex Berenson, a reporter from the New York Times who had written several articles critical of CA in the past, was researching a new article regarding CA's accounting practices. *See* E-mail from Sanjay Kumar to Steven Woghin, Ira Zar, and CA Public Relations employees (Mar. 21, 2001). Beginning in mid-April, Mr. Berenson began sending questions via e-mail to CA's public relations department, which then forwarded those questions to CA's senior executives, including Messrs. Kumar, Woghin, and Zar. *See, e.g.,* E-mail from Alex Berenson to CA Public Relations employee (Apr. 25, 2001). While Mr. Berenson's questions dealt with various accounting issues, such as CA's transition to the new business model and its license/maintenance accounting, none of his questions raised the 35-Day Month or the timing of revenue recognition more generally. *See, e.g.*, E-mail from Alex Berenson to CA Public Relations employee (Apr. 27, 2001). CA's executives declined to be interviewed by Mr. Berenson, since they were of the opinion that the article would be negative, and no amount of cooperation from CA would change that result. *See, e.g.* E-mail from Sanjay Kumar to CA Public Relations employee (Apr. 26, 2001).

However, there is no evidence that the CA Board was consulted about the Company's response (or lack thereof) to Mr. Berenson's questions, or that the Board was forewarned that an article would be forthcoming.

On April 29, 2001, Mr. Berenson's article, entitled "A Software Company Runs Out of Tricks; The Past May Haunt Computer Associates," was featured prominently on the front page of the business section of the Sunday edition of The New York Times. *See* Alex Berenson, *A Software Company Runs Out of Tricks; The Past May Haunt Computer Associates*, N.Y. Times, Apr. 29, 2001, at C1. The lengthy article focused on claims that CA: (i) implemented the new business model as a means to cover up its shrinking earnings; (ii) recognized fees associated with maintenance up front as opposed to ratably, which is required by GAAP; (iii) classified most of the fees from extended or renewed agreements as new license revenue; (iv) falsely represented its Unicenter program as a successful product when it, in fact, struggled; and (v) gave Unicenter to customers for free to enhance its appearance to Wall Street. *See id.* While several paragraphs of the article dealt with each of these four allegations, a single paragraph raised the 35-Day Month.

That paragraph, which was the fifth paragraph of the article, provides in full:[83]

> Computer Associates, they say, has used accounting tricks to systematically overstate its revenue and profits for years. The practices were so widespread that employees joked that C.A. stood for 'Creative Accounting,' and that March, June, September and December, when fiscal quarters end, had 35 days, giving the company extra time to close sales and book revenue.

Id.

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83 The Company's senior executives received a preview of the article on Saturday evening, April 28, and immediately began planning the Company's response. Because several of the issues raised by Mr. Berenson were the subject of the then-pending Class Actions, the consensus of CA's management was that the article was an attempt by Milberg Weiss to "stir the pot" in order to promote the plaintiffs' interests in that litigation. The Company's response, drafted primarily by Messrs. Woghin and Zar, was posted on CA's website on April 30.

Certain senior CA managers reported that the 35-Day Month allegation "jumped off the page" at them, given their knowledge of the practice, while others paid little attention to it due to its lack of prominence in the article and the fact that the practice had ended. Regardless of their personal reaction to the 35-Day Month allegation, no senior CA executive raised the practice or discussed it, either amongst themselves or with the Board. Further, the Company's written response to the article presented a rebuttal to each of the allegations contained in the article, *except* for the 35-Day Month allegation. According to those interviewed by the SLC, senior management did not make an affirmative decision not to discuss the issue or not to address it in the Company's response, but rather, no one raised the issue, apparently in the hope that, since it was purely "historical," if ignored it would just go away.

The Board members' initial reactions to the article were varied.[84] However, the directors universally felt that the article was sensationalized journalism that resulted from the media's perpetual inability to understand CA's business. For example, CA's switch to the new business model, considered a forward thinking and conservative business move by the directors (and those in the industry), had nonetheless been the subject of extensive criticism in the media, and the Board viewed the allegations in the article as further evidence of the media's continued inability to appreciate the model.[85]

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84 At this time the Board was comprised of directors Wang, Kumar, Artzt, D'Amato, de Vogel, Grasso, Kenny, and Pieper.

85 It should be noted that Wall Street analysts also viewed the new business model as a positive. For example, a report issued by Deutsche Bank on April 30, 2001 in response to the publication of the article states:

> We continue to view CA's new business model (which combines a new, more flexible term licensing approach with more conservative pro rata revenue recognition) as a major positive. Our field work indicates that customers like it as do investors. Moreover, it addresses a number of the issues raised by the article.

Deutsche Bank, CA: New York Times Publishes Negative Article – Strong Buy (Apr. 30, 2001).

The Board also knew that several of the allegations contained in the article were, in fact, demonstrably false. For example, the Board knew that Unicenter was a real and valuable CA product used by many large corporations, and as such, the article's allegation that Unicenter was "shelfware" was untrue.[86] In the Board's view, some allegations were scurrilous, such as the allegation that CA hired "young, cute girls" to sell multi-million dollar software packages to "geeky-type" technology specialists, and this too diminished the impact of the article as a whole.

The Board was also wary of Mr. Berenson as a journalist, because he had already written several articles portraying CA in a negative light, and appeared to the directors to both lack objectivity and to be on a sort of "crusade" against CA. Indeed, this was Mr. Berenson's third negative piece on CA in just over a month (*see* Alex Berenson, *Computer Associates Considers Severance for Some it Fired*, N.Y. Times, Mar. 28, 2001, at C5; Alex Berenson, *Questions on Firings and Severance at Computer Associates*, N.Y. Times, Mar. 20, 2001, at C1) and the article was being criticized outside the company as being "irresponsible."

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86 The AberdeenGroup, a leading provider of fact-based research focused on the global technology-driven value chain, issued a response to the article. *See* AberdeenGroup, Aberdeen Field Experience at Odds with NY Times' View of Computer Associates' Viability (May 1, 2001):

> Aberdeen typically doesn't respond publicly to stories published in the mainstream press. However, the April 29, 2001, *New York Times'* piece on Computer Associates (CA) rates an exception to this rule. The story contains substantive inaccuracies to which Aberdeen can speak from direct field experience. Additionally, the story is laced with innuendoes that undermine its credibility. . . . The *Times'* implication that Unicenter TNG's success is primarily a CA-fabricated myth is just not true. Though shelfware incidents certainly do occur — for CA as well as for most software suppliers — Unicenter TNG remains a market powerhouse at work in enterprises that are household names . . . . *[O]ne would think that objective investigative journalism could dig up more impressive Unicenter exemplars than Bradlees and New Pig.*

Id. (emphasis added).

For example, a Prudential Securities release issued on April 30, 2001 states, "[w]e would also point out, however, that the article has a number of inconsistencies that suggest this third, Sunday Business Section headline article, is clearly an attack that does not look at any of the positive aspects of the company – and more importantly the stock." Prudential Securities, New York Times Newsflash: Mainframe Software Has Been a Difficult Business Fraught With Accounting Issues – Does Anyone Not Know That? (April 30, 2001). The report went on to state that it believed that certain of Mr. Berenson's analyses were "irresponsible and sensational." *Id.* Likewise, with respect to the new business model, Deutsche Bank stated:

> [w]e believe that, regardless of past issues and stories, CA is now a very customer friendly company that, with the advent of its new business model back in 10/2000, is gaining increased business momentum. Our field work shows that customers and prospects like CA's new flexible licensing approach and CA's previewed F4Q (March) results, which included GAAP revenue of $732 million along with a gross increase in residual value of $1.3 billion (based on the GAAP balance sheet) are evidence of that.

Deutsche Bank, CA: New York Times Publishes Negative Article – Strong Buy (April 30, 2001).

None of the directors focused on the paragraph mentioning the 35-Day Month when they read the article, and no member of management, including Mr. Kumar, drew their attention to it. There is no evidence that the directors, either as a whole or in small groups, discussed this allegation, or the article as a whole, immediately following the article's publication. Indeed, it appears that the analyst community failed to focus on the 35-Day Month allegation as well, as none of the analyst reports issued in response to the article and reviewed by the SLC mention the 35-Day Month allegation. To the extent that Wall Street questioned

Mr. Kumar about the allegation, he replied that the Company used a ratable revenue recognition model under which there is no need for a 35-day month.

To aid the Company with its response to the article, CA retained a public relations firm and a crisis management consultant. *See* Minutes of a Meeting of the CA Board at 1 (May 7, 2001). According to Mr. Woghin, this was the first time, to his knowledge, that CA had sought outside help for the Company. Further, Mr. Kumar suggested that Dr. Kenny, Chair of CA's Audit Committee, meet with CA's auditors to discuss the article and satisfy herself that the Company's current accounting practices were sound.[87] On the morning of May 7, prior to a telephonic Board meeting scheduled for later that day, Dr. Kenny sent a memo, drafted by Mr. Woghin, to KPMG, E&Y, and certain members of CA management, requesting that they attend a meeting the next day "to get a clearer picture of the issues that were raised . . . in the recent New York Times article." *See* E-mail from Priscilla Smith, Dr. Kenny's Assistant, to E&Y, KPMG, Scott Smith, Ira Zar, Steven Woghin, David Kaplan, and Grace Caden (May 7, 2001). Dr. Kenny also sent a memo to CA's independent directors, in which she proposed a meeting for May 8, so that she could report to them on the outcome of her meeting with the auditors and management. Memorandum from Shirley Strum Kenny to Willem de Vogel, Alfonse D'Amato, Roel Pieper, Richard A. Grasso (May 7, 2001). Mr. Zar then made follow-up calls to the audit firms to ensure that they would attend. Although they were given only one (1) day's notice, neither of the audit firms raised any objections regarding the timing of the meeting, or requested additional time to prepare.

Later on May 7, the Board met telephonically, at which time Mr. Kumar updated the Board on events that had occurred following the article's publication. *See* Minutes of a

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87 Dr. Kenny was appointed Chair of the Audit Committee on June 6, 2000 after the death of director and Audit Committee Chair Irving Goldstein.

Meeting of the CA Board at 1 (May 7, 2001). The article was presented to the Board by Mr. Kumar as (i) part of the class action plaintiffs' attack on CA and (ii) the result of comments by disgruntled former CA employees. The minutes of that meeting reflect that Mr. Kumar reported that CA "had received substantial support from noted financial analysts who regularly follow and report on the Corporation and its stock." *Id.*[88] Mr. Kumar also told the Board that the Company had been receiving counsel from public relations experts and crisis management advisors with respect to the Company's response. *Id.*

At the conclusion of the meeting, Mr. Kumar told the Board that the Audit Committee would meet the next day, May 8, "to consider, independent of the Corporation's management, whether it is advisable for the Corporation to take any additional steps respecting its review of the Corporation's financial reporting practices." *Id.* at 2. Mr. Kumar also told the Board that CA management was in the process of forming a blue ribbon panel of independent experts to review its financial reporting practices and confirm that CA followed "best practices." *Id.* The substance of the article was not discussed at this meeting.

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88 This report was accurate. *See, e.g.*, CIBC World Markets Corp., *NYT Article Should be Taken with Both a Grain of Reality As Well As Salt* (Apr. 30, 2001); Deutsche Banc Alex. Brown Inc., *CA: New York Times Publishes Negative Article-Strong Buy* (Apr. 30, 2001) ("*In our opinion, New York Times article on 4/29 was filled with errors, half-truths, and old and out-of-date information*") (emphasis added); Prudential Securities, *CA: New York Times Article on Computer Associates Misrepresentative, In Our View* (Apr. 30, 2001); Dain Rauscher Wessels*, CA: The New York Times: Taking A Few Kernels Of Truth To The Extreme* (Apr. 30, 2001) ("While we think CA's business is under some pressure and maintain our Neutral stance, *we found most of the article exaggerated and one-sided*") (emphasis added); Morgan Stanley Dean Witter, *No New News – CA Responds* (May 1, 2001) ("*Overall, we believe the article had no material new news and contained inaccuracies and misleading statements*") (emphasis added); Jim Murphy, *Capital Markets Report Mark to Market: If You Won't Identify Yourself, Shut Up*, DOW JONES NEWSWIRE (May 2, 2001) ("*In the aftermath of the Times' trashing of CA, one of the surprising things was the strong defense of the company – 'on the record,' mind you - by prominent analysts at prominent firms, none of whom, apparently, was contacted by the New York Times for its story Sunday*") (emphasis added); *See* E-mail from Chuck Phillips (Software/B2B Industry Analyst, Managing Director at Morgan Stanley) to Alex Berenson, forwarded to Sanjay Kumar (Apr. 29, 2001) (noting *"inaccuracies"* contained in the article and generally defending CA).

The Board felt reassured by Mr. Kumar at this meeting because they were told that there was nothing to support the allegations in the article. The directors took further comfort from the fact that Mr. Kumar (i) had personally requested that the Chair of the Audit Committee look into the allegations raised in the article, and (ii) had, on his own initiative, begun assembling the blue ribbon panel. These actions, the directors felt, were not the sort of thing a CEO with something to hide would undertake. That said, the Board nonetheless realized it was its responsibility to "disprove these sorts of allegations" and to make sure there were no "irregularities or tricks going on" with respect to the Company's accounting practices.

1. **Preparation for the May 8 Meeting**

According to those interviewed by the SLC, very little, if anything, was done in preparation for the meeting called by Dr. Kenny. Dr. Kenny did not request that management or the auditors provide her with any materials to prepare. Prior to the meeting, Mr. Woghin recalled sending Dr. Kenny only the article itself and the Company's written response. CA management slated to attend – Messrs. Zar, Woghin, Kaplan and Grace Caden (head of CA Internal Audit) – did not meet to prepare for the meeting, or discuss in advance what would be said. While this appeared to the SLC to be unusual considering the circumstances, the SLC was told that it was "not the CA way" to have formal meetings to discuss such things. Likewise, there is little evidence that KPMG, which was in the middle of completing CA's annual audit for fiscal year 2002, did any additional work in preparation for the meeting. As noted above, neither management nor the audit firms objected to the timing of the meeting, and did not request any additional time in order to prepare.

2. **The May 8 Meeting**

At 8:00 a.m. on May 8, Dr. Kenny met with (i) Larry Smith of KPMG, (ii) Martin Shannon of E&Y, (iii) Ira Zar, Steven Woghin, David Kaplan and Grace Caden of CA, and (iv) Scott Smith of Covington & Burling LLP, CA's outside corporate counsel, at Dr. Kenny's office at SUNY Stony Brook. According to Dr. Kenny, the other members of the Audit Committee, Messrs. de Vogel and D'Amato, did not attend this meeting because it was preliminary, and was held simply to determine if further action was required. If that turned out to be the case, according to Dr. Kenny, she would have called in the other members of the Audit Committee for any follow-up meetings. Several attendees commented that, in hindsight, it was unusual for her to hold such a meeting without the other members of the Audit Committee present, but at the time, no one thought of, or raised, this as an issue.

Given the passage of time, the record is scant as to what actually transpired at this meeting, and the attendees, in particular Dr. Kenny (whom the SLC interviewed twice on this issue)[89] generally had trouble recalling detailed information about the substance of the discussions. The meeting itself is reported to have lasted between forty-five (45) minutes to an hour. Nonetheless, the SLC was able to glean certain facts from the collective recollections of the attendees, and the limited documentary record.

According to those who attended, Dr. Kenny opened the meeting with general comments regarding its purpose. The tone at the meeting was not adversarial, and while the attendees appreciated the seriousness of the meeting, they did not feel that they were under attack. Without asking specific questions, Dr. Kenny then asked Mr. Zar to address the allegations contained in the article, and turned the meeting over to him. Mr. Zar reviewed the

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[89] As noted above, given that the SLC closely examined the Board's response to the New York Times article, it interviewed the key participants – Dr. Kenny, Ira Zar, David Kaplan, and Steven Woghin – twice regarding this issue.

Company's response to most of the allegations in the article, and Dr. Kenny interjected questions during his presentation. Mr. Zar did not use any materials in his presentation other than the response posted on CA's website.

A memo generated after the meeting indicates that Mr. Zar addressed (i) CA's shift to the new business model and use of pro forma accounting, (ii) allegations that CA had engaged in "accounting tricks" to inflate its revenues, (iii) CA's allocation of revenue as maintenance, (iv) Unicenter, and (v) CA's use of reserves in connection with acquisitions. *See* Kenny Talking Points (drafted by Steven Woghin) at 1-2 (May 7, 2001). However, Mr. Zar did not address the 35-Day Month allegation and, to his relief, no one asked him to do so during or after his presentation. It was reported that Ms. Caden and Mr. Woghin also spoke briefly at the meeting, but that Mr. Zar was the primary presenter on behalf of management.

Following Mr. Zar's presentation, with all attendees still present, Dr. Kenny questioned the representatives from the accounting firms. Those who attended recall that Dr. Kenny asked the auditors general, high-level questions such as: "have you ever seen anything that would lend credence to the allegations in the article?" or "is there anything in the article to be concerned about?" The attendees universally recall that both audit firms responded that there was not. Dr. Kenny did not "cross examine" the auditors, or ask detailed questions about the accounting issues on a more granular level.

There appears to be a disconnect between the assurances given by the auditors at this meeting, which have been described as "general," and Dr. Kenny's takeaway that, in essence, the auditors gave CA a "clean bill of health." Generally, the audit firms told Dr. Kenny that their prior audits were performed in conformance with generally accepted accounting standards ("GAAS"), and that CA's accounting practices were in conformity with

GAAP. The attendees also recall the auditors addressing CA's license/maintenance and cancel/convert accounting, and CA's transition to the new business model. In addressing the new business model and CA's pro forma accounting, Mr. Smith of KPMG cited an attestation report that KPMG had recently completed. *See* Minutes of a Meeting of the CA Audit Comm. at 2 (May 8, 2001). To create this report, KPMG had examined CA's pro forma accounting, and confirmed that its assumptions were reasonable. *See id.* Dr. Kenny did not ask the auditors to address the 35-Day Month allegations at any point during the meeting, and they did not do so on their own initiative.

Next, Dr. Kenny asked Mr. Zar to leave the meeting, and then asked the auditors if there were any issues they wished to bring to her attention. Dr. Kenny was told that there were none. *See id.* at 3; Kenny Talking Points (drafted by Steven Woghin) at 2 (May 7, 2001). Next, all of CA management was asked to leave the meeting, and Dr. Kenny asked the auditors again if there was anything they wished to discuss without management present. The auditors again told Dr. Kenny that there were no issues to discuss. *See* Minutes of a Meeting of the CA Audit Comm. at 3 (May 8, 2001); Kenny Talking Points at 2 (May 7, 2001). According to Dr. Kenny, although she does not specifically recall what was said, she recalled that the auditors raised no concerns during the executive session, and in her view, she would have expected them to do so if they had any concerns about CA's financial statements or the allegations raised in the article.

The SLC believes that Dr. Kenny rightfully took comfort, although in the SLC's view possibly somewhat excessive comfort, from those assurances. Dr. Kenny honestly expected that the auditors, or management, would have raised any accounting issues if they existed, or if the auditors had any doubt as to their existence, and their failure to do so was interpreted by Dr. Kenny as an affirmation that there were none. Accordingly, Dr. Kenny did not request that the auditors perform any follow-up work after the meeting, and the audit firms did not on their own accord recommend that any further action be taken.

As noted above, the 35-Day Month allegation was never specifically raised or discussed by anyone at any time during this meeting. CA management purposely avoided raising the issue, and recalled feeling relieved that no one else at the meeting did. The SLC asked members of management present at the meeting as to what would have transpired had Dr. Kenny asked about the 35-Day Month practice. The SLC was told that, while each of them would have liked to believe that they would have answered any question about the 35-Day Month practice truthfully, they believe that they would have sought to avoid the issue or – if pushed – been dishonest, much in the way they responded during the first year and a half of the government investigation. Mr. Zar candidly observed to the SLC that it took over a year and half for the Company, represented by WLRK, who in turn was assisted by PwC, to get to the bottom of the issue once the government investigation began, and surmised that a similar result would have occurred had Dr. Kenny began questioning the practice at this meeting.

3. **The May 8 Audit Committee Meeting**

Following Dr. Kenny's morning meeting, at 4:30 p.m., she telephonically reported her findings to the Audit Committee and the Board's other independent directors, who participated by invitation. *See* Minutes of a Meeting of the CA Audit Comm. at 1 (May 8, 2001). The minutes from the meeting reflect that, Dr. Kenny reported "in some detail the responses supplied by Mr. Zar and the members of the accounting firms." *Id.* at 2. Prior to the meeting, and at her request, Mr. Woghin had prepared a set of talking points for Dr. Kenny to use as a basis for her report. These talking points noted each of the allegations raised in the article – except for the 35-Day Month – and the response given by Mr. Zar. *See* Kenny Talking

Points (May 8, 2001) (drafted by Steven Woghin). Dr. Kenny told the directors present that Mr. Zar had assured her that the Company's accounting practices were appropriate. Mr. de Vogel questioned Dr. Kenny at various points throughout her report.

According to the minutes, Dr. Kenny reported further "that both KPMG . . . and Ernst & Young . . . denied the Corporation had used any 'accounting tricks' as alleged in the Times article." Minutes of a Meeting of the CA Audit Comm. at 2-3 (May 8, 2001). As described above, those who were present at the morning meeting did not recall the auditors making such a broad statement and believed that this conclusion overstated the assurances given by the audit firms, although it reflects what Dr. Kenny honestly believed she had been told. Here, again, the SLC found a disconnect between what CA's outside auditors had done, and what the directors understood the auditors to have done. As noted above, the auditors provided Dr. Kenny with general assurances regarding their prior audit work, but the SLC has uncovered no evidence to support the conclusion that the auditors told Dr. Kenny that the allegations made in the article were "false." Mr. Woghin and Mr. Smith, who were present at the meeting, however, did not correct or qualify Dr. Kenny's statement to the directors on the call.

As a result, the directors understood from Dr. Kenny's report that the outside auditors had examined CA's accounting, and determined that no problems existed. Further, the directors on the call reported that they assumed from Dr. Kenny's report that all of the allegations in the article had been individually addressed by the auditors, including the 35-Day Month allegation. Based on Dr. Kenny's report, the directors believed that there was no substance to the allegations in the article.

At the conclusion of the meeting, which is reported to have lasted approximately fifteen (15) minutes, the directors thanked Dr. Kenny for undertaking this task on behalf of the Board. *See* Minutes of a Meeting of the CA Audit Comm. at 3 (May 8, 2001). The Audit Committee took no further action in response to the article following this meeting. According to Mr. de Vogel, "the temperature came down" after Dr. Kenny gave a report of her inquiry.

4. **Dr. Kenny's Independence**

While Dr. Kenny may have appeared to be the obvious choice to conduct this inquiry on behalf of the Board given her role as Audit Committee Chair, the SLC was concerned about the possibility that her relationship with Mr. Wang, who was Executive Chairman at this time, impaired her ability to view the allegations in the article objectively. Dr. Kenny, as noted above, became Chair of the Audit Committee on June 6, 2000, and Mr. Wang had a long and well-documented professional relationship and personal friendship dating back to the period when Dr. Kenny served as President of Queens College, where Mr. Wang was a prominent and successful alumnus.[90]

In 1996, after Dr. Kenny had left Queens College to become President of SUNY Stony Brook, and two (2) years after she joined the CA Board, Mr. Wang pledged a $20 to $25 million donation for the purpose of constructing the Charles B. Wang Center for Asian and Asian American Culture (the "Wang Center") at SUNY Stony Brook.[91] The donation is Mr. Wang's largest known charitable contribution to date, and it represented the largest single

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90 *See* Alex Berenson, *A Gift Raises Questions On Computer Associates*, N.Y. Times, Dec. 3, 2002, at C1; John Giuffo*, SUNY, Inc.: The Decline of Higher Education Under Pataki*, The Village Voice, Sept. 18-24, 2002.

91 Bruce Lambert, *Computer Chief to Give SUNY an Asian-American Center*, N.Y. Times, Dec. 8, 1996, at 49.

donation in the history of the State University of New York at that time.[92] Ultimately, Mr. Wang's Foundation has reportedly spent more than $52 million on the construction of the Wang Center, which opened on October 22, 2002.[93] The details of the donation and the building process were the subject of extensive media coverage from the initial announcement in December 1996 to its opening, and Mr. Wang often commented on his donation at CA Board meetings.[94]

The SLC believes that this is another example of a situation where things could have been done better. The SLC was troubled by the fact that it appears that no meaningful evaluation of Dr. Kenny's independence was conducted when Dr. Kenny became Chair of the Audit Committee, at which time Mr. Wang was CEO and Chairman, and his substantial donation to SUNY Stony Brook was known to the Board. Nor was any evaluation performed at the time of the initial donation, which occurred in December 1996, after Dr. Kenny joined the CA Board. The only evaluation ever performed occurred when Dr. Kenny became President of SUNY Stony Brook. Dr. Kenny went before the University's ethics commission, because Stony Brook had existing contracts with CA, and it was determined that it would not be a problem, *from the University's perspective*, for Dr. Kenny to sit on CA's Board.

Ultimately, given the actions taken by Dr. Kenny and the Audit Committee, and the information provided to Dr. Kenny by management and CA's outside auditors, the SLC

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92 SUNY Stony Brook, "Charles B. Wang Center," https://www.stonybrook.edu/sb/wang/about.shtml (last visited Feb. 2, 2007).

93 Suraj Rambhia, *An Interview with Charles B. Wang*, The Stony Brook Statesman, Oct. 30, 2006 (available at http://www.sbstatesman.com/media/storage/paper955/news/2006/10/30/news/2006/10/20/News/An.Interview.With.Charles.B.Wang-2407766.shtml) (last visited Feb. 2, 2007).

94 *See, e.g.,* Lambert, *supra* note 93; Berenson, *supra* note 92; Press Release, SUNY Stony Brook, "Governor Pataki, Charles Wang Open New Center at Stony Brook," (http://www.state.ny.us/governor/press/02/oct22_5_02.htm) (last visited Nov. 2, 2006).

concludes, based on all available evidence, that her relationship with Mr. Wang did not impair her ability to independently evaluate the allegations made in the article.[95] Likewise, under NYSE independence rules in place at the time,[96] Dr. Kenny was considered an "independent" director and permitted to serve as Chair of the Audit Committee.

5. **Mr. Kumar's May 8, 2001 E-mail**

At the same time, on May 8, 2001, Mr. Kumar sent an e-mail to CA's senior executives, including Messrs. Richards, Zar, and Woghin, regarding the 35-Day Month issue. Mr. Kumar states in the e-mail that "[t]wice in 10 days I have been asked by a newspaper reporter about CA booking business after the 30/31 of a month at the end of a quarter." Mr.

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95 Interestingly, the SLC learned that when conflict arose between Messrs. Wang and Kumar and the Board was faced with a decision as to who should remain at the Company, Dr. Kenny did not throw her support behind Mr. Wang as certain other directors had. Instead, the SLC learned that Dr. Kenny attempted to mediate between the two sides and remain neutral.

96 The NYSE listing standards in effect at the time stated that a director will not be considered "independent" if, among other things, he or she has:

> been employed by the corporation or its affiliates in the current or past three years;
>
> an immediate family member who is, or has been in the past three years, employed by the corporation or its affiliates as an executive officer;
>
> been (i) a partner, controlling shareholder, or executive officer of an organization that has a business relationship with the corporation or (ii) has had a direct business relationship with the corporation (e.g., a consultant), unless the corporation's board determines in its business judgment that the relationship does not interfere with the director's exercise of independent judgment. Business relationships can include commercial, industrial, banking, consulting, legal, accounting and other relationships. A director can have this relationship directly with the company, or the director can be a partner, officer or employee of an organization that has the business relationship; or
>
> been employed as an executive of another entity where any of the corporation's executives serve on that entity's compensation committee.

The NYSE listing standards in effect now require that the board make an affirmative determination that a director has no "material relationship" with the listed company. Material relationships can include commercial, industrial, banking, consulting, legal, accounting, charitable, and familial relationships, among others. The June 6, 2000 CA Board resolution appointing Dr. Kenny as Chairperson of the Audit Committee, states that the CA Board made a determination that Dr. Kenny was independent within the meaning of the NYSE rules. Statement of Action taken on the Unanimous Consent of the CA Board (June 6, 2000).

Kumar stated further that he knew:

- "that there are many many instances that we pay commissions to sales people that bring in business right after the end of a quarter at the previous quarter's rate as a means of motivating the sales organization."
- "that we push very hard to get as much business in at the end of a quarter as possible, and that we keep pushing to keep the momentum to get all the business that we can to start the next quarter off to a hot start."
- "that if a deal slips at the end of a quarter that it is going to slip to the end of the next quarter and that is the reason that we push sales staff to get the deals even after the close of the quarter to book it in the new quarter."
- "that sales managers often tell their sales staff that we need more and more to make sure that we start the next quarter off well."
- "that sales managers promise the previous quarter's commission rates for the first week or ten days of the new quarter to keep the momentum going."

Mr. Kumar stated that he could see "how an outsider, who does not understand the facts, can get the wrong impression" about CA's quarter end practices.

Mr. Kumar concluded the e-mail by asking CA's senior executives to ensure that they "are vigilant and comply with quarter end cutoffs," and to ensure that their subordinates "are doing the right thing to make sure that [CA] adhere[s] to the applicable revenue recognition rules as well as our internal policies and procedures." According to Mr. Zar, this was Mr. Kumar's attempt to convey to management "the party line," and that rather than actively coordinating their stories, management viewed an e-mail such as this as the "official commentary," and would then repeat that story. Likewise, Mr. Kaplan, who believed that someone had shown him this e-mail, viewed this as Mr. Kumar's attempt to create a record. Mr. Kumar denied that this e-mail constituted an attempt to coordinate management's "story," however, regardless of Mr. Kumar's intent, that is how the e-mail was interpreted by those who received it. Indeed, several of the points Mr. Kumar made in the e-mail were later repeated by

CA employees to CA's counsel and the government when the government began its investigation of the issues raised in the New York Times article in February 2002.[97]

IX. THE GOVERNMENT INVESTIGATION AND THE SETTLEMENT OF THE CLASS ACTION AND DERIVATIVE LITIGATION

A. *2002 – Commencement of the Government Investigation*

January-March 2002. In January 2002, the Company began to receive reports from various former CA employees that the USAO had contacted them to discuss their employment at CA. On February 20, 2002, several newspapers reported that the government had launched an investigation into CA's accounting practices. *See, e.g.,* Mark Harrington & Robert Kessler, *CA Faces FBI Probe; Feds looking at possible accounting fraud*, Newsday, Feb. 20, 2002; Alex Berenson, *Inquiry Into Computer Associates*, N.Y. Times, Feb. 20, 2002, at C7. That same day, Mr. Woghin sent a memo to the Board informing the directors that the Company had retained WLRK,[98] specifically partners Martin Lipton and John Savarese, to handle the government investigation; and that WLRK had in turn reached out to the government "in order to understand their concerns and answer their questions before this matter proceeds too far." Memorandum from Steven Woghin to the Members of the CA Board at 1 (Feb. 20, 2002). In the Board's view, CA had brought in the "strongest" law firm that it knew of to represent the Company in, and if possible to quickly resolve, the investigation.[99]

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97 For example, as discussed below, Mr. Silverstein met with the government on September 6, 2002, at which time he imparted the "party line" that sales people thought that contracts were prematurely booked due to the timing of the commissions they received, but that those sales people would not be in a position to know how CA accounted for any particular contract. *See supra* at 213-215.

98 According to Messrs. Woghin and Kumar, WLRK was retained at the request of Mr. Grasso.

99 WLRK had previously represented CA in an attempt by the Wylys to take control of the CA Board through a proxy contest. Several of the directors, including Lewis Ranieri and Richard Grasso, had previous experience with WLRK outside of their membership on the CA Board.

The following day, at a February 21, 2002 Board meeting, Mr. Wang advised the Board that the Company learned that the USAO had "commenced a preliminary inquiry into certain matters originally published in The New York Times in April of 2001." Minutes of a Meeting of the CA Board at 1 (Feb. 21, 2001). Mr. Savarese reported to the Board that he had made initial contact with the USAO, and predicted that he would meet with the USAO within the week to discuss the situation. *Id.* at 1-2. Mr. Lipton advised the Board that he had spoken with representatives from KPMG about the allegations in the New York Times article, and that KPMG remained "thoroughly satisfied" with its prior audits of CA's financial statements. *Id.* at 2.

According to Mr. Savarese, at the outset of the investigation, the Board was eager to "get comfortable" with the matters under investigation, understand what the government's concerns were, and what the Company's strategy would be going forward. Both Mr. Savarese and Mr. Kumar told the Board that the Company was committed to cooperating with the government and responding to the government's requests for information.

One (1) week later, on February 27, 2002, the Board met again to receive an update from counsel. WLRK reported, based on teleconferences with the USAO and the SEC, that the government was looking into four (4) issues: (i) whether the Corporation's product, Unicenter TNG ("Unicenter"), had achieved market acceptance or was, as first asserted in the New York Times article, "shelfware"; (ii) whether CA's accounting for cancel/convert transactions was appropriate; (iii) whether CA properly booked revenue on contracts that had been executed and delivered upon, but which had not been fully executed *by the Company* in the period the revenue was recognized; and (iv) whether there was a relationship between the vesting of the KESOP and the timing of the July 21, 1998 press release. *See* Minutes of a

Meeting of the CA Board at 2-3 (Feb. 27, 2002). Mr. Savarese reported that he had met with CA management and KPMG to discuss these four (4) issues, and had learned "significant information" regarding each area.

The Board was told by WLRK that: (i) there were "strong facts to refute" the allegations regarding Unicenter sales; (ii) CA had issued a reclassification of its revenue when KPMG reviewed CA's cancel/convert accounting in May 2000, and the change did not draw investor or SEC attention at that time, and that the cancel/convert accounting issue was "ancient history"; (iii) KPMG had informed Mr. Savarese that CA's practice of not countersigning contracts was "proper, just not [the] best practice," and was "not used to shift revenue from one quarter to [an]other"; therefore the issue "should not be a problem"; and (iv) David Nachman, who represented the Company in the Class Actions, "ha[d] well developed facts" regarding the vesting of the KESOP and the timing of the July 21 press release and that this area should likewise not prove problematic. Notes of Scott Smith LLP at 1-3 (Feb. 27, 2002). WLRK told the Board that it was meeting with the SEC later that day and that it planned to (i) share with the SEC what it had learned, (ii) confirm that there were no additional areas of inquiry to those listed above, and (iii) confirm that CA would move as quickly as possible to respond to the government's concerns.

While no one present at the meeting questioned whether WLRK, which had only been retained a week earlier, had adequate time to come to the preliminary assessments reported to the Board at this meeting, most of these issues were well known to the Board prior to WLRK's involvement. As noted above, all the issues that the government was investigating were raised in the April 29, 2001 New York Times article, and in part in the Class Actions, and the Board viewed the government investigation as an extension of those events.

For example, CA's cancel/convert accounting practice had been a long running focus of the 1998 Class Action. Mr. Savarese was therefore able to discuss this issue with Mr. Nachman, who, he believed, already had a "firm grasp" of the accounting material. The Unicenter issue had been raised in the New York Times article, and had been addressed by the Audit Committee in May 2001.[100]

Further, the Board, in part based on statements made by WLRK and management, continued to believe that the plaintiffs in the then-ongoing Class Actions (along with certain disgruntled former CA employees) were feeding the press and the government "bogus" information in an effort to pressure the Company in the litigation. Indeed, it was reported to the Board that Melvyn Weiss, lead counsel in the Class Actions, had called Mr. Nachman the day after the news of the investigation broke and asked him, "now do you want to settle?" CA had steadfastly refused to discuss settlement in the past. Many of the directors recall being assured personally at the time (and on numerous other occasions as the investigation progressed) – either by WLRK or management, or both – that there had been no wrongdoing.[101]

The Board met again two (2) days later on March 1, 2002. At this Board meeting, Mr. Savarese told the Board that he had met with the government and conveyed three (3) points: (i) he "stressed the Board's great concern that CA shareholders have been badly injured by what appeared to be a campaign of leaks coordinated with short selling activity that

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100 Mr. Woghin told the SLC that CA had "a lot of meetings" with WLRK "right out of the box," and that WLRK ultimately "produced a list of clients who used Unicenter." Mr. Savarese and Mr. Woghin therefore concluded that the "anecdotal and statistical information" suggested that "Unicenter was a real product," contrary to the government's allegation.

101 Prior to joining the Board on March 25, 2002, Mr. Lorsch said that he spoke to Mr. Lipton "at length," and that Mr. Lipton told him that there was "no substance" to the government's allegations.

has hammered the stock price"; (ii) he "conveyed the Board's and the Company's pledge that [the government] will receive prompt and complete cooperation from the Company"; and (iii) he "provided a detailed account of what [WLRK had] been able to learn about the underlying historical facts relating to the '4 areas of concerns' [the government] had described." Savarese Talking Points at 1-2 (Mar. 1, 2002).[102] In addition, Mr. Savarese told the Board that the revenue recognition aspect of the government's investigation not only included, as had been previously reported, contracts that had not been timely executed by the Company, but also "backdated [contracts]," i.e., contracts backdated by CA *customers* to appear as if they were signed by the quarter end, but were not.

However, Mr. Savarese also made it clear to the Board that the government appeared to be "most interested in two (2) issues," both unrelated to backdating: (i) CA's cancel/convert practice, and (ii) whether the Company "used 'pro forma' reporting in an appropriate way to present its transition to the [new business model] adopted in Oct. 2000," which the government had added as a new, fifth area of concern. *Id.* Again, because the New York Times article had focused on (and was even thought to be the result of) the Company's switch to the new business model, the Board and management had already devoted a considerable amount of time to addressing the public's concerns on the subject.[103]

Mr. Savarese reported that the government had an "open mind" on all these points, but had "clearly devoted more time and energy to this than previously thought – the

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102 Throughout this section, the SLC has relied upon "talking points" prepared by Mr. Savarese for use at meetings with the Board and the government. Mr. Savarese told the SLC that it was generally his practice to follow very closely, if not verbatim, his talking points when giving a presentation to the CA Board. Members of the Board reported that Mr. Savarese typically read from prepared remarks, and that he typically delivered them in an uninterrupted fashion.

103 Some on the Board believed that the government investigation, in its entirety, was – like the New York Times article – the result of a continued misunderstanding of the new business model.

USAO asked sophisticated, intelligent questions." *Id.* In response to this report, Mr. Savarese recalls that the Board acted in a way that demonstrated it was "generally concerned," and wanted to make sure that the Company "devoted appropriate resources" to cooperating fully in order to resolve the situation.

At the conclusion of the meeting, Mr. Woghin addressed the question of legal representation for the non-management directors in connection with the government investigation. Mr. Woghin told the directors that "Messrs. Lipton and Savarese had been directed to determine, during their meetings with government representatives, whether any conflict of interest appeared among the Directors or between any of the Directors and the Corporation." Minutes of a Meeting of the CA Board at 3 (Mar. 1, 2002). Mr. Savarese confirmed for the Board that he and Mr. Lipton had conferred with the government, KPMG, and Mr. Woghin, and that WLRK was satisfied that no conflict existed at that time. Mr. Savarese also confirmed that WLRK had reached its conclusions "independent of any contact with the Corporation's management." *Id.* at 4. Both Mr. Woghin and WLRK told the Board that WLRK would "immediately advise the Directors if they believe that separate counsel is needed." *Id.*[104]

At this point, it is important to note that the SLC's investigation has uncovered a disconnect between what CA management and WLRK believed WLRK's role was to be, and what at least some directors believed WLRK was doing. Specifically, WLRK was retained to interact with the government, respond to government inquiries and requests, and to generally

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104 Mr. de Vogel was initially uncomfortable with this arrangement, notwithstanding the fact that both Mr. Lipton and Scott Smith of Covington & Burling, CA's corporate counsel, assured him that it was appropriate. Mr. de Vogel then spoke with his regular litigation counsel from another prominent law firm, who advised him that by obtaining opinions from both WLRK and Covington & Burling, Mr. de Vogel had satisfied himself that it was appropriate to proceed in this fashion.

"defend" the Company and its officers and directors in connection with the government investigation. This is confirmed by WLRK's engagement letter with CA, which states as follows: "Our firm has been engaged to represent Computer Associates in connection with an inquiry by the Northeast Regional Office of the Securities & Exchange Commission and the United States Attorney's Office for the Southern District of New York in respect of certain accounting matters." Letter from John Savarese to Steven Woghin (June 11, 2002). WLRK was not retained or instructed to conduct an "independent investigation or inquiry" into the areas of concern raised by the government.[105]

In contrast, the CA Board members generally believed that WLRK had undertaken a broader mandate. Several directors expressed the view that they believed that WLRK was conducting an internal investigation designed to "get to the bottom of" of the areas raised by the government, uncover the "true facts," and independently determine whether there had been any wrongdoing by CA or its officers. The directors' belief about the scope of WLRK's engagement was based upon their view as to what a top-notch law firm would do when representing *both* the Company *and* its independent directors in connection with a governmental investigation.[106] No one from management or WLRK explained or made clear to the directors, none of whom were lawyers, the more limited scope of WLRK's actual engagement. This misunderstanding, the SLC believes, caused members of the CA Board to

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105 That said, WLRK did attempt to discover whether there was any basis to the government's allegations. WLRK told the SLC that he told the Board that the Company had to develop credible answers to the government's allegations. Indeed, we are aware of no instance where Mr. Savarese told the Board that there were investigative steps WLRK could, or should, have taken, but did not because of the nature of WLRK's investigation.

106 While Roel Pieper's recollection was that Mr. Lipton told the Board that WLRK would perform an internal investigation, the SLC believes that it is more likely that Mr. Pieper misunderstood Mr. Lipton, who like Mr. Savarese, told the Board that WLRK needed to understand the facts before it could respond to the government's allegations.

take excessive comfort from the fact that WLRK repeatedly informed the Board that it was unaware of any wrongdoing and that CA was developing credible defenses to the government's allegations.

April-May 2002. In April 2002, WLRK began interviewing CA employees regarding the government's areas of concern, one of which was late-signed and backdated contracts. At this time, WLRK conducted five (5) interviews. Initially, on April 26, 2002, WLRK interviewed Peter Schwartz, the Company's former CFO, who had headed the Finance department until June 1998 (but stayed on for several months in an executive capacity), and other high level finance and internal audit employees. With respect to the issue of CA's signature, the employees interviewed were forthcoming about the fact that, prior to KPMG becoming CA's auditor, CA had routinely failed (for, in their view, good-faith business reasons) to countersign license agreements prior to the quarter end, in violation of GAAP. WLRK believed that these witnesses appeared credible in part because of their candor in revealing this information.

At the same time, CA management was adamant that its customers (as opposed to CA) signed CA license agreements on time. The employees interviewed at this time, including Messrs. Schwartz and Kaplan and other senior executives, gave false or misleading answers to WLRK in order to assure them that CA did not backdate contracts. For example, a senior Finance executive told WLRK that there was a mechanism in place at CA that effectively prevented any late executed contracts from being recognized; in particular, that Financial Reporting would generate a list of contracts to be "backed out" of revenue because they were signed after the end of the quarter. In his interview, Mr. Schwartz told WLRK that there were quarter-end reviews of contracts to confirm that they were recognized in the same quarter in which they were signed. Mr. Kaplan, likewise, falsely told WLRK that any mistakes in revenue recognition – for example, late signature dates or late shipping dates – would have been caught at the end of the month or quarter.

In addition, CA executives gave WLRK plausible, but false, reasons for why it appeared that contracts may have been booked late. These executives told WLRK that while contracts were consistently recognized in the quarter in which customers signed them, there was a period of five (5) days after the month end in which contracts were "administratively processed," making it seem as though late contracts were booked in the prior quarter.

Mr. Kaplan also told WLRK that there was no relationship between the timing of sales commissions and the timing of revenue recognition. In this way, Mr. Kaplan confirmed what Mr. Schwartz and other senior executives had already told WLRK: that former CA employees, and Sales personnel in particular, might think there was a 35-Day Month practice because CA sometimes paid sales commissions in the month prior to the month in which a contract was actually signed. This made sense, WLRK was told, because Sales employees were being rewarded for their hard work in a timely fashion and did not have to wait until the next quarterly period to get paid.[107]

While the SLC uncovered no explicit agreement to lie to WLRK, the SLC has learned that certain CA senior executives, including Messrs. Zar, Kaplan, and Rivard informally coordinated the responses they would give to questions about the 35-Day Month. On several occasions, for instance, Mr. Rivard met with the other executives to "get the gist" of what people were saying, and to establish false but believable and consistent answers to questions

[107] In a February 2003 telephonic interview, Stephen Richards added that Sales employees would sometimes receive this commission out of a sense of fairness, as they had done most of the work on the deal in the prior quarter and most of the negotiations for the deal took place in the prior quarter.

about CA's revenue recognition practices. These "stories" were consistent with Mr. Kumar's May 8, 2001 e-mail, which was viewed as a defense to the 35-Day Month allegations when they were first raised in the New York Times article. Ultimately, these falsehoods and half-truths provided to WLRK were then passed on to the government and the CA Board.

1. **May 14, 2002 Board Meeting**

At a May 14, 2002 Board meeting, Mr. Savarese reported that, based on WLRK's most recent meeting with the government, it was clear that the USAO was hearing "decidedly negative (though perhaps misinformed) accounts about" the issues it was investigating, including a "laxity in the q[uarter]-end controls, which effectively permitted [contracts] signed after the q[uarter]-end to be counted." Savarese Talking Points at 1 (May 14, 2002). Mr. Savarese's notes of the meeting indicate that he told the directors: "yes there will be mistakes, but no evidence they were made <u>purposefully</u>." Notes of John Savarese at 2 (May, 14, 2002) (emphasis in original). Further, Mr. Savarese reported that he had effectively addressed the government's concerns regarding the new business model and CA's pro forma accounting – something the Board was very appreciative of – but that all of the other allegations were still "live issues." So by this time, (i) at least one of the original five (5) issues had been resolved in a manner satisfactory to the government and (ii) the Board had not been told of evidence of intentional misconduct.

Mr. Savarese also reported to the Board that, on the other issues, the government "has not reached any conclusions yet," and that the investigation was ongoing so the Company was "not out of the woods yet." *Id.* To that end, the Board was told that the government had issued subpoenas to certain of CA's customers and its auditors. According to several Board members, the fact that the Company was able to successfully address certain of the government's allegations was encouraging, and lent credence to management's claims that there was no substance to the remaining allegations, and that the government simply needed to better understand CA's business. Given the areas of investigation that remained – (i) Unicenter, (ii) the cancel/convert practice, (iii) the timing of the KESOP, and (iv) backdating – the Board and its counsel took certain proactive steps in an attempt to understand, and to ultimately resolve, them.

In contrast, CA's executive management team, including Messrs. Wang and Kumar, knew that the backdating allegations were, in fact, quite substantive and, following this meeting, met to discuss what to do about the government's now-intensifying focus on this issue. According to Mr. Kumar, Mr. Wang instructed Mr. Kumar to "stonewall" the government, and believed, based on a similar tactic that he employed in a prior investigation by the USAO on a personal matter, that the investigation would eventually "go away." Mr. Wang felt that the backdating issue was an "old issue" and therefore "his issue" – since it occurred before the new business model – and that the investigation was therefore a renewed attack on him. Accordingly, at Mr. Wang's instruction, CA's senior management remained silent about the 35-day month issue.

2. **PwC's Work**

(a) *The "KESOP Study"*

In the early summer of 2002, Mr. Schuetze, who, like Mr. Lorsch, was elected to the Board on March 25, 2002, sketched out his preliminary thoughts to WLRK on a study of CA's accounting practices around the time the KESOP vested (the "KESOP Study").[108] The study originated from a conversation between Messrs. de Vogel and Schuetze, in which Mr. de Vogel expressed concern about ensuring the accuracy of CA's financial reports for the quarters

108 Prior to joining the Board, Mr. Schuetze was assured by Messrs. Kumar, Zar, and Woghin that the allegations in the April 29, 2001 New York Times article were without basis.

in which the KESOP vested. Mr. Schuetze and Mr. de Vogel reasoned that a study of those quarters would be a "good test" to see if CA's senior management had improperly inflated CA's revenue, because that was the time when they had the greatest incentive to do so. At Mr. Schuetze's request, PwC conducted a study of the two (2) fiscal quarters immediately preceding the vesting of the KESOP shares (the third and fourth quarters of fiscal year 1998, October 1, 1997 to March 31, 1998).

The scope of PwC's work, as designed by Mr. Schuetze, was to determine whether: (i) there was persuasive evidence that license agreements recognized in the relevant periods properly contained customer signatures and dates; (ii) reserves, loss accruals and allowance accounts did not reflect large or unusual movements and were consistent with prior and subsequent periods; (iii) capital expenditures did not reflect large or unusual items and were consistent with the trend and amounts in prior and subsequent periods; (iv) provisions, accruals (and releases of accruals), and payments relating to income tax accounts did not reflect any large or unusual fluctuations and were reasonable; and (v) there were no large or unusual "unrecorded liabilities" that were accrued or paid subsequent to the relevant period. Woghin Talking Points at 1 (Aug. 23, 2002). In connection with the study, PwC looked at 126 CA North American contracts with a GAAP value of $1 million or more (totaling $1.26 billion), and a selection of 54 North American contracts with a GAAP value of less than $1 million (totaling $27.85 million).

However, PwC did not perform a forensic audit – one in which all relevant documents and e-mails were examined – of the two quarters at issue, but followed a set of agreed-upon revenue and expense procedures. Rather than doing a full scale audit, it was agreed that PwC would initially focus on CA's central files and only look at other documentation when it thought it necessary to do so. In an August 27, 2002 memo, PwC explained that its "agreed-upon procedures" included examining "[s]elected contracts . . . for appropriate customers' signatures and dates." Memorandum from PwC (Aug. 27, 2002). PwC only engaged in further investigation when it spotted "[p]otential exceptions," and then it reviewed "other, related, contract and sales arrangement documentation; and . . . other indicia of persuasive evidence of the arrangement." *Id.*[109]

At the conclusion of the KESOP Study, at a meeting held on August 23, 2002, the Board was told by Mr. Woghin that PwC found that "only 5 contracts of the 180 reviewed for the period either lacked evidence of a customer signature [x], or of a date [y], or reflected an untimely customer signature and date [z]." Woghin Talking Points at 1 (Aug. 23, 2002) (emphasis in original). Further, "PwC concluded that the compliance rate of properly signed and dated customer contracts is *inconsistent with an assertion of manipulation of revenue recognition* practices and that there were adequate reserves that CA maintained for any exceptions to its revenue recognition policies." *Id.* (emphasis added). Mr. Woghin also reported to the Board, "[o]n the basis of PwC's findings, and on the prior Ernst & Young audit actually performed at the time for the fiscal year in question, Mr. de Vogel and Mr. Schuetze are satisfied that CA fairly presented its financial results for the third and fourth [fiscal] quarters of 1998." *Id.* at 2.

Mr. Schuetze, who retained a written copy of the study after the investigation had concluded, was satisfied with PwC's work upon its completion. He took comfort in PwC's work because he believed that the PwC partner leading the study, was "thorough" and had

109 The only reports that PwC reviewed were "TOPS reports," which were printouts of contract files from the TOPS database. These reports were reviewed "for completeness" and "for any large or unusual items." Memorandum from PwC (Aug. 27, 2002).

confidence that PwC had followed the established procedures. *See, e.g.,* E-mail from Steven Woghin to Sanjay Kumar and Ira Zar (Aug. 26, 2002). While certain directors mistakenly believed that PwC had conducted a forensic audit, all the directors appropriately took comfort from the results of this study and the fact that it had been designed by Mr. Schuetze, former Chief Accountant to the SEC, and implemented by PwC, one of the "big four" accounting firms.

(b) *The Customer Signature Review and Analysis*

In addition to the KESOP Study, in the early summer of 2002, WLRK retained PwC to conduct several additional studies, including a study to address the 35-Day Month allegation, entitled "Customer Signature Review and Analysis," which was referred to as the "532 Contract Study." For the 532 Contract Study, as established with WLRK, PWC examined the contracts produced by CA to the government, which included all contracts from (i) CA's top six customers, and (ii) the "top 25" contracts, for each quarter of fiscal years 1998 through 2001. Memorandum from PwC at 1 (Sept. 4, 2002). The total revenue associated with the contracts reviewed by PwC was $13 billion. *Id.*

PwC's review process was as follows:

> For each contract selected for review, the contract effective date was compared to the customer signature date in order to identify instances where the contract's effective date preceded the quarter in which the customer's signature was dated. For each instance identified, the actual date of revenue recognition was researched to determine that revenues were recognized after customer signatures were obtained and not on the basis of the effective contract date.

Id. at 2. In addition, PwC examined CA's procedures for establishing revenue reserves. *Id.* However, at WLRK's direction, PwC again did not conduct a forensic audit and therefore did not examine documentation other than the actual contracts themselves – i.e., the same information that had been produced to the government. *See, e.g.* E-mail from PwC to WLRK (May 18, 2002).

In September 2002, PwC issued the final results of its Customer Signature Review and Analysis study. PwC found that "a review of 532 contracts [total value of $13 billion] produced in response to the [SEC's] February 26, 2002 informal document request disclosed *no evidence to indicate that CA routinely or intentionally recognized contract revenues before customer signatures were obtained*." Memorandum from PwC at 1 (Sept. 4, 2002) (emphasis added). According to Mr. de Vogel, Dan Dooley of PwC told him that PwC had uncovered "all kinds of reserves" supporting the fact that CA actually "undercounted" revenue and that Mr. Dooley gave the impression that he believed he could strongly defend CA's accounting practices in court. This report, in conjunction with the KESOP Study, gave the Board considerable comfort with respect to the revenue recognition aspects of the government investigation.

However, as with the precise parameters of the role being undertaken by WLRK, many directors seemed to not fully appreciate the precise scope of PwC's work on both the 532 Contract Study and the KESOP Study. Here again, at least some directors believed a forensic audit was being conducted, and were surprised to learn during their interviews with the SLC that this was not the case. The failure of the Board to fully understand the precise scope of PwC's work again gave the Board a greater degree of comfort about that investigation than was warranted under the circumstances.

CA management encouraged this misunderstanding by using the results of PwC's work as further cover for the 35-Day Month practice, and its position that the Company had done nothing wrong. For example, on November 25, 2002, the Wall Street Journal published an article reporting that the government was investigating whether the Company had prematurely recognized revenue from licensing agreements.[110] That same day, Mr. Woghin sent a memo to the Board concerning the article, in which he stated that:

> [i]t is important to note that this allegation was investigated thoroughly by PwC and reported upon by them to the government previously. In its analysis and report, PwC found nothing to support such an allegation. The government has not asked the company for additional information since the PwC report was delivered.

Memorandum from Steven Woghin to the Members of the CA Board at 1 (Nov. 25, 2002).

3. Mr. de Vogel's Meeting with the Government

While PwC was in the middle of its work, the Board determined that director Willem de Vogel should meet with representatives of the USAO and the SEC in order to respond to the government's concerns regarding the KESOP and, hopefully, move the investigation towards a conclusion. *See* Memorandum from Warren Stern and John Savarese to Steven Woghin at 1 (July 19, 2002) ("Stern Memo"). At a July 2, 2002 Board meeting, WLRK told the Board that the goal of this meeting was to "to lay out in very forceful terms that we have asked PwC to analyze in detail the documents we've already produced to the government, to focus on the issues the government has expressed concern about in the past, and to assess whether there are any problems." Savarese Talking Points at 1 (July 2, 2002). According to WLRK, this was a good time to take this step since WLRK told the Board that "the government has not been all that active. Reviewing documents/meeting with some W[itnesses]/but clearly

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110 The article stated: "Federal investigators have been gathering information from some former Computer Associates International Inc. employees who claim that the software maker often back-dated and forward-dated customer contracts to shift revenue between fiscal quarters in an effort to meet earnings targets, according to the former employees and lawyers with knowledge of the matter." Jerry Guidera, *Computer Associates' Deals Probed – Investigators Study Dates Of Contracts to Determine Effects on Quarterly Results*, WALL ST. J., Nov. 25, 2002, at A3.

some of the wind has come out of their sails already and we expect that this upcoming meeting will help to spill some more air out." *Id.*

Mr. de Vogel, accompanied by WLRK, met with the government on July 18, 2002 and made a presentation about the creation of the KESOP, telling the government that the KESOP had been his idea, and providing an explanation of the plan. *See* Stern Memo at 4. Mr. de Vogel explained the technical aspects of the KESOP, the grant and vesting provisions, the seven-year transfer restrictions, and why the targets in the KESOP were "hurdles that were hard to clear." Mr. de Vogel added that, in his view, the fact that Messrs. Wang and Kumar paid portions of the taxes on the KESOP in cash "implied that they had not schemed to inflate the price" because they were increasing their long-term risk, which would not be rational if they knew that CA's financials were improperly inflated. *Id.*

According to WLRK's summary of the meeting, a representative of the SEC expressed some measure of agreement with Mr. de Vogel's argument regarding the KESOP, and a representative from the USAO said that "while he might disagree with this argument, he thought the logic behind the formulation of the KESOP that [Mr. de Vogel] had previously explained was in some respects persuasive." *Id.*

At this meeting, WLRK also addressed CA's cancel/convert accounting, and then gave a "Contract Signature Presentation" in which it presented the preliminary results of the 532 Contract Study, which, as noted above, was ultimately completed in early September. WLRK reported that PwC had reviewed 532 contracts for customer signature issues and had identified twenty-nine (29) contracts with potential issues. *Id.* at 1-3. Mr. de Vogel added that the twenty-nine (29) contracts appeared to have been randomly distributed over the seven-year period reviewed (from fiscal years 1994-2000), and that none of the twenty-nine (29) contracts occurred in the two (2) quarters preceding the vesting of the KESOP. WLRK noted that PwC had concluded that the twenty-nine (29) contracts with issues "might well be" the result of "simple human error." *See id.* at 3.

Finally, WLRK explained to the government, for the first time, the operation of CA's "late executed contract" reserve. According to WLRK, the late executed contract reserve was established to account for contracts signed after the quarter end but nonetheless recognized in the prior quarter, and he presented the reserve as evidence of the Company's good faith and conservatism with respect to revenue recognition. Mr. de Vogel "volunteered that CA recognized that sales people might 'cheat' by backdating contracts, so it established a reserve. This led to discussion that made clear that reserves were established for a number of reasons relating to mistaken revenue recognition." *Id.*[111]

According to WLRK's summary, at the conclusion of the meeting, the government representatives told Mr. de Vogel and WLRK that their presentations were "extremely helpful." *Id.* at 5. The government remarked that the retention of PwC was an "impressive step," and that the government appreciated CA's cooperation. *Id.*

At a July 22, 2002 Board meeting, Mr. de Vogel reported on his meeting with the government. Mr. de Vogel said that he felt good about the meeting, that it had gone well, and that he felt that he had made it clear to the government that the KESOP was a good plan. WLRK reported to the Board that Mr. de Vogel "put an engaging, appealing and astute face on

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111 Recollections vary as to when each director learned about the late executed contract reserve, with most directors believing they did not learn of the practice until July 2003, and some asserting they learned of it as late as January 2004. However, the written documentation reflects that this information was imparted to the directors no later than February 2003, and probably earlier, since Mr. de Vogel discussed it with the government in July 2002. Memorandum from Steven Woghin to the Members of the CA Board at 2 (Feb. 21, 2003). With the exception of Mr. Fernandes, who joined the Board in May 2003, all of the directors interviewed believed the late executed contract reserve was a good business practice because it allowed the "machinery to keep going" while accounting for some mistakes along the way.

a [company] that they otherwise tend to hear bad things about from former disgruntled employees." WLRK told the Board that the government said it was "v[ery] impressed by [the] degree of [the] Co[mpany]'s cooperation to date," with Mr. de Vogel's presentation, and with the retention of PwC. Savarese Talking Points at 1 (July 22, 2002). However, WLRK reported that the scope of the government's investigation had remained unchanged, and that it would continue to interview and to issue grand jury subpoenas to former employees, particularly sales employees. *Id.* at 2.

Also at this meeting, David Nachman, counsel to the Company in the Class Actions, reported to the CA Board on the status of the Class Actions. Mr. Nachman "expressed the view that although the plaintiffs had a weak case, it was unlikely that the Corporation would succeed in obtaining summary judgment and that a trial likely would be required." Minutes of a Meeting of the CA Board at 5-6 (July 22, 2002). Mr. Nachman also reported that additional class action and derivative litigation had been filed in February 2002 following the announcement that the government had initiated an investigation into CA's accounting practices. *Id.* at 6.

4. **WLRK Interviews**

During July and August 2002, WLRK continued to interview CA employees regarding CA's revenue recognition practices, including Messrs. Kaplan, Rivard, and Silverstein. Prior to their interviews, several of these executives discussed their impending interview with Mr. Woghin who, at a minimum, encouraged them not to offer any information WLRK did not specifically request.[112] Each of these individuals provided WLRK misleading

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112 For example, according to Mr. Rivard, Messrs. Zar and Woghin came to Mr. Rivard's office to alert him to the fact that WLRK wanted to meet with him. When they told Mr. Rivard that WLRK had questions about CA's revenue recognition practices, the three sat for a while and "ran through the various things Mr. Rivard should tell the lawyers in his interview." For example, Mr. Rivard might say that there was a

information concerning the Company's revenue recognition practices, this time with more detail. Many of the interviewees incorrectly discussed the concept of an "administrative window," explaining that while contracts had to be signed by the end of the quarter, at one point in time Sales executives had until the flash date to physically deliver and process the finalized contracts to CA.

Mr. Silverstein told WLRK that contracts were supposed to arrive at CA before quarter end, but that Sales Accounting needed time to review paperwork related to contracts that had been completed. He then said that any contracts that arrived after the end of the quarter *might* be recognized as revenue, depending on whether all the circumstances indicated that the contract was signed in the field before quarter end. Mr. Silverstein told WLRK that "[t]here had to be something more than the contract just appearing out of thin air with the date on it" in order to book it, including a pre-quarter-end postmark on a mailed-in contract or a pre-quarter-end phone call from the Sales employee telling CA headquarters that the contract was signed. Moreover, Mr. Silverstein purported to explain why employees might think that revenue was recognized early, telling WLRK that CA might have commissioned a transaction as if it was "done" in the prior month, even if the revenue was recognized later. Mr. Silverstein then falsely claimed that, because CA did not want to impede the sales process, it continued to process deals for commission purposes if they arrived during the flash period.

Mr. Savarese reported to Mr. Kumar the results of these interviews.

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policy in place regarding revenue recognition to which sales accounting adhered, although this was not true. Mr. Kaplan stated that Mr. Woghin gave him bad advice, namely that "the less you say [in interviews with WLRK and S&C] the better you are." Mr. Woghin denies that he ever instructed any CA employee as to how to answer questions about the 35-Day Month practice.

5. **CA Annual Meeting**

On July 11, 2002, CA's Board resolved to limit directorships to eight (8) years. *See* Minutes of a Meeting of the CA Board at 2 (July 11, 2002). Also on that day, Kenneth Cron, Robert La Blanc, Alex Vieux, and Thomas Wyman were elected to the CA Board,[113] and directors de Vogel, Grasso, Pieper, and Kenny, who collectively had served almost forty (40) years on the CA Board, resigned, effective August 28. As a result, following CA's August 28, 2002 annual meeting, the Board was comprised of outside directors Cron, D'Amato, La Blanc, Lorsch, Ranieri, Schuetze, Vieux, and Wyman, along with Messrs. Kumar, Wang, and Artzt. Computer Assocs. Int'l, Inc., Proxy Statement (Form DEF 14A) (July 26, 2002). With the exception of directors D'Amato and Ranieri, no outside director had been with the Company since the beginning of the government investigation.

6. **September 6, 2002 Meeting with the Government**

According to Mr. Silverstein, after the August interviews, WLRK told Mr. Silverstein that it believed that he did a very good job of explaining why a salesperson might believe that CA had backdated contracts (when it actually had not) and that they had therefore chosen him to answer questions from the government on behalf of CA. Mr. Silverstein recounted to the SLC that he was reluctant to do so, but did not share this reluctance with the WLRK attorneys at the time. Notwithstanding his hesitance, according to Mr. Silverstein, he was convinced to meet with the government by Messrs. Woghin and Zar, who told him that (i) the government was not really asking about the 35-Day Month practice, but rather about how

113 Mr. Wyman, who was formerly the Chairman and CEO of CBS Inc., served only until January 8, 2003, when he passed away.

the Company paid commissions to its salespeople, (ii) he did not have to volunteer information, and (iii) to keep his knowledge of the 35-Day Month in his "back pocket."[114]

Following these instructions, on September 6, 2002, Mr. Silverstein conveyed CA's "party line" to the government. *See* Silverstein Plea Tr. at 20. By all accounts, Mr. Silverstein did a "fine job" of persuading the government that disgruntled employees, and not a widespread practice of prematurely recognizing revenue, were responsible for the 35-Day Month allegations. When the government asked him about the 35-Day Month practice, and whether he was aware of any contracts that were recognized in quarters prior to those in which they were signed, Mr. Silverstein told the government that he was not aware of any such contracts. Mr. Silverstein explained that due to the timing of sales commissions, it appeared to Sales personnel that contracts were being recognized early, but that, because CA reserved against late contracts – a practice which Sales representatives would not be privy to – no contract revenue would be prematurely recognized.[115]

Following the September 6 meeting with the government, Messrs. Wang and Kumar again discussed CA's strategy with respect to the government investigation and again determined to remain silent about the 35-Day Month issue. According to Mr. Kumar, Mr. Wang again told him that the 35-Day Month was a "historical problem," and that there was no reason to "destroy" CA's current business by disclosing the practice now. Mr. Wang again told

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114 Mr. Woghin denies that he ever instructed any CA employees as to how to answer questions about the 35-Day Month practice.

115 Representatives of the USAO, SEC, and FBI were all in attendance for these statements. *See* Silverstein Plea Tr. at 19. From CA, Charles McWade and Rick Finegan also attended the meeting, along with Mr. Savarese. Mr. McWade presented on the Company's cancel/convert practice; however, according to Mr. Savarese, Mr. Finegan did not participate. Thus, on both July 18 and September 6, representatives of CA made false statements to the government, some knowing and intentional, concerning CA's revenue recognition practices

Mr. Kumar that the government would eventually "go away" if the Company continued to "stonewall" on the issue.

Consistent with that conversation, at an October 22, 2002 Board meeting, according to Mr. Kumar, Mr. Wang told the Board that CA had good quarter-end cut off procedures in place, which were sometimes difficult to enforce, but nonetheless adequate. At no time before his resignation from the Board on November 15, 2002, did Mr. Wang advise the Board that he was aware of any evidence to the contrary.

7. **2002 Summary**

Based on the SLC's investigation, it is clear that throughout 2002, both CA management and WLRK (who had been misled by CA management) told the Board that there was no substance to the issues being examined as part of the government investigation, and that CA had developed credible answers to the government's questions. Indeed, the Board was consistently told that the April 2001 New York Times article and the government investigation were the result of (i) disgruntled former employees with little actual knowledge who fed the government inaccurate information, and (ii) cooperation between the plaintiffs' lawyers at the Milberg Weiss law firm and the government. This view was confirmed, in their minds, by (i) the fact that at least one of the issues being investigated by the government had been resolved in CA's favor, (ii) the results of PwC's work, which addressed the 35-Day Month allegations and the allegations regarding the KESOP, and (iii) the positive reports they had received concerning the presentations to the government made by Messrs. de Vogel and Silverstein. This is the view that the Board took into 2003, when the government investigation took a material turn for the worse.

B. *January 2003 – June 2003: The Government Investigation Escalates*

1. **WLRK Interviews**

During the week leading up to a January 21 Board meeting, WLRK conducted additional interviews of CA employees, interviewing four (4) CA Sales and Legal department employees regarding certain documents the Company had produced in response to a grand jury subpoena issued to CA on December 19, 2002 (the "December Subpoena").[116] Those interviews were prompted by, among other things, the fact that the Company produced an e-mail which stated "remember no backdating on this one" with respect to a particular transaction. Each of the employees interviewed presented explanations for any documents that raised issues and asserted that they believed each particular transaction at issue was signed by the quarter end.

2. **January 21, 2003 Board Meeting**

At the January 21, 2003 Board meeting, attended by Messrs. Savarese and Lipton, WLRK reported to the Board that there had been material negative developments in the investigation: (i) in December 2002 the government had issued "7 or 8 [grand jury] subpoenas to various customers requesting e-mails, faxes, memos, etc. re: when contracts with CA were signed"; and (ii) the government claimed it had "[f]ound some disturbing documents suggesting backdating," but that the claims "need[ed] to [be] analyze[d] in detail." Savarese Talking Points at 1 (Jan. 21, 2003). Mr. Savarese's talking points indicate that he reviewed with the Board several of the documents that he believed were troubling the government and discussed the additional work WLRK did to analyze the situation. *Id.* Mr. Savarese did not raise an

[116] The December Subpoena called for sixteen (16) contracts and documents related to those contracts, including drafts, internal and external correspondence (including e-mail), a list of all persons who worked on the transactions, and other documents.

alarm at this meeting, and the message that he conveyed was that the Company and WLRK would keep working at the outstanding issues and would keep the Board posted.[117]

WLRK also told the Board that the Company had consistently cooperated fully with the government and was in the process of responding to the December Subpoena. The directors interviewed reported that the tone of WLRK's report indicated that the Company was making good progress with the government, and it would only be a matter of time before this issue was taken care of and the whole investigation would be over. The directors stated that the report they received at this meeting was "not alarming," and that while there were clearly issues to be addressed, they did not have the sense that the Company was in any danger at this point because of these developments.

As it had in the past, WLRK advised the Board to be patient, and that the investigation would take time to resolve. WLRK also listed five (5) impediments to a resolution of the government investigation, including: (i) the Milberg Weiss Class Actions; (ii) a "[s]teady stream of former disgruntled [e]mployees being located by Milberg Weiss investigators and turned over to FBI"; (iii) "KESOP Plan = huge jury appeal"; (iv) "[s]ome troubling documents/facts"; and (v) "[c]ancel/convert activity." *Id.* at 2. These impediments were presented to the directors because, according to counsel, the Board was anxious to resolve the investigation and needed to understand why it was continuing to take time.

As to the relationship between the Class Actions and the government investigation, both Mr. Savarese and Mr. Lipton told the Board that the Class Actions were a serious impediment to resolving the government investigation since, in their view, the USAO would be reluctant to end its investigation while the Class Actions were pending in the same

117 According to Mr. Kumar, Messrs. Lipton and Savarese knew that there were isolated instances of problem contracts, but neither was told during this time that a systemic practice of shifting CA's quarters existed.

district. The directors unanimously recall being told that resolving the Class Actions was a necessary, but not sufficient, precondition to resolving the government investigation. This meeting was the last time the Board would receive a direct, firsthand update from outside counsel for nearly six (6) months.

Shortly after the January 21 meeting, on January 29, 2003, WLRK submitted a letter to the USAO setting forth the preliminary results of their review of the materials collected in response to the December Subpoena. Letter from John Savarese to Eric Corngold and David Pitofsky, U.S. Attorney's Office for the Eastern District of New York, at 2 (Jan. 29, 2003). With respect to the scope of the review, the letter states:

> [i]n the course of responding to the Subpoena, we have carefully analyzed the available documentary materials (including contracts, correspondence, faxes, emails and related revenue recognition entries), and in some cases have interviewed CA personnel involved in the transactions, to assess whether the revenues associated with the sixteen agreements identified in the Subpoena were recognized by CA in the appropriate financial reporting period.

Id. Despite this representation, there were additional documents at CA that had not been collected. As discussed below, these documents were later produced in the fall of 2003. The letter then states that "of the sixteen agreements [the USAO] identified, there is only one relatively small agreement which appears, given the currently available information, likely to have been recognized prematurely." *Id.* at 3.

The January 29 WLRK letter also provides explanations, including those given to the Board, for documents related to each contract that appeared to evidence premature revenue recognition, based upon a review of additional documents and interviews of CA employees. For example, with respect to a contract dated September 30, 1999, but for which there was a copy with a fax date of October 5, 1999, WLRK reported that the CA Sales employee who negotiated the deal clearly recalled standing at the fax machine on September 30 waiting for the fax, and then personally delivering the fax to Mr. Kumar when it arrived that day. *Id.* at 4. WLRK then added that the same CA Sales employee recalled that certain pages of an exhibit had been omitted from the original signed contract, and offered this as an explanation as to why the customer faxed another copy on October 5. *Id.* at 5. WLRK offered similar explanations for documents related to the other contracts identified in the subpoena. *Id.*

The WLRK letter concluded as follows:

> In closing, we want to emphasize that *CA continues to deny vigorously that it has intentionally recognized revenue in a period other than the one in which the contract was signed*. We have carefully reviewed the files relating to contracts enumerated in your Subpoena, and – aside from the few potential issues affecting nominal amounts of revenues discussed above – see nothing that would establish the contrary. *In our discussions with senior managers and sales people, we have been impressed by the force of their assurances that CA did not engage in this practice*. Moreover, as we and PwC explained and documented during our July 18 and September 6 meetings with you, *CA took pains through its reserve process to assure that revenue associated with any contract that was received during the quarter would not be recognized until it was proper to do so*.
>
> We also recognize that you may have information and documents that we do not have and that may bear upon the revenue-recognition questions addressed in this letter. If that is the case, we would like the opportunity to discuss any further questions or concerns you may have. In short, CA is prepared to do everything within its power to meet your concerns and put any questions about this to rest.

Id. (emphasis added). This communication to the government was fully consistent with the views WLRK was expressing to CA's Board.

3. **WLRK Telephone Interview with Stephen Richards**

On February 19, 2003, WLRK interviewed Stephen Richards, CA's then-head of Sales, by telephone for the first time. According to WLRK's summary of the interview, "Mr.

Richards emphatically denied ('absolutely not') that CA encouraged its sales representatives to backdate contracts." Mr. Richards' testimony was consistent with that of other senior CA executives, who told WLRK that Sales employees were often confused about revenue recognition because: (i) the effective date and the execution date on contracts was sometimes different; (ii) they were pushed to continue to close deals after the quarter end in order to prevent the deals from slipping; and (iii) on occasion, they were commissioned in the quarter prior to the quarter in which a contract was executed as a reward for their efforts. Mr. Richards also told WLRK that Sales employees had no reason or way to know how revenue from a contract was recognized as an accounting matter, and that even he did not know how or when CA recognized revenue from contracts. Mr. Richards further stated that he did not believe that Sales managers encouraged their teams to backdate deals, and he "emphatically denied that Mr. Kumar has ever encouraged or suggested backdating." The theme conveyed by Mr. Richards – that there was no 35-Day Month – was knowingly false.

4. **February 21, 2003 Memo to the Board**

On February 12, 2003, the USAO sent a letter to WLRK which enclosed a second grand jury subpoena. In the letter, the USAO stated its view that "CA *has not complied fully with an [outstanding] subpoena . . . has not responded fully to questions we have raised*," and was of the view that "*CA's production has been incomplete*." Letter from David Pitofsky to John Savarese at 1 (Feb. 12, 2003) (emphasis added). The letter stated that, in particular:

> [g]iven the complex nature of CA's licensing agreements and our understanding as to the vigorous negotiations commonly preceding the execution of such agreements, we expected to receive a significant volume of documents in addition to the final, executed agreements; however, CA has produced very few drafts and limited correspondence (either internal or external).

Id. at 1-2. The USAO then requested that CA "provide a complete production of documents responsive to the December 19th Subpoena forthwith." *Id.* at 2. In addition, the USAO provided an example of a document it had received from a CA customer, but not from CA. Specifically, the letter enclosed a copy of a CA Order Form on which it appeared that the signature date had been altered. The USAO stated that, regardless of the significance of the document with respect to backdating, this document "raises the obvious question of why it was not produced by CA." *Id.* at 3.

The next week, on February 21, 2003, Mr. Woghin sent a memo to the Board, in which he reviewed the Company's response to the December Subpoena. Memorandum from Steven Woghin to the Members of the CA Board at 1 (Feb. 21, 2003). Mr. Woghin reported that CA had been able to find anecdotal or documentary evidence to support the timing of the revenue recognized on all but two (2) of the contracts identified in the subpoena. *Id.* With regard to one of those contracts, the memo states: "[a]s PricewaterhouseCoopers had previously reported to the government, CA maintained adequate reserves for such an item." *Id.* at 2. The memo noted that the other contract at issue was for only $440,636, and stated that CA was continuing to look for evidence to support the timing of the revenue recognized for both contracts. *Id.* The Board took comfort in the fact that management vigorously denied that they had engaged in wrongdoing and was able to refute a vast majority of the government's concerns.

After addressing the documentation that CA provided to the government for each of the contracts at issue, Mr. Woghin, for the first time, told the Board that the "*government questions whether we have fully and completely responded to their subpoena since they apparently have received some materials from CA customers that we have not been able to* *locate and produce*." *Id.* (emphasis added). The memo informed the Board that the government might be "concern[ed]" that "what they continue to 'hear' about backdating of agreements from their informants is inconsistent with the information we have produced." *Id.* However, Mr. Woghin did not share with the Board the text of the February 12 letter from the USAO. Likely as a result, Mr. Woghin believed that the memo depicted a rosier view of reality at the time.

While the directors generally did not specifically recall receiving this memo, the directors recalled learning at or around the first half of 2003 that the government expressed concern with the adequacy of CA's document productions. The directors also recalled that they told Mr. Woghin to make sure CA devoted sufficient resources to complying with the government's document requests and that Mr. Woghin said he would do so.[118]

5. CA's Last Chance to "Come Clean"

During the early part of 2003, WLRK continued to meet with the government to discuss the 35-Day Month issue. By this time, the government was no longer showing interest in any of the other issues it had originally identified, which Mr. Woghin told the Board "after 15 months" had "all . . . seemingly dropped off the table." Woghin Talking Points at 3 (May 13, 2003).[119] The sole "[q]uestion," at this point, as Mr. Woghin put it, was "how to deal with

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118 The Board next met on February 28, 2003, to consider the retirement package Charles Wang was to receive, who as noted above, announced his retirement on November 15, 2002. The Board, and particularly the Compensation Committee, then comprised of Directors Cron, La Blanc, and Ranieri, devoted a substantial amount of time to this issue during this period.

119 The government told CA it had stopped pursuing the issues it originally had raised with respect to the new business model during a meeting in April 2002. It is not clear precisely when the government stopped pursuing the other issues, including cancel/convert, the timing of the KESOP, and Unicenter. Mr. Savarese told the SLC that the government was satisfied on the Unicenter issue and the cancel/convert practice by late October or early November 2002, although a memo from Mr. Woghin to the Board says that the government was still actively involved in this issue through the middle of November 2002. Memorandum from Steven Woghin to the Members of the CA Board at 1 (Nov. 14, 2002). Moreover, in February 2003, Mr. Savarese told the government by letter that he was responding to the government's

this remaining issue [of the 35-Day Month practice] with the government." *Id.* Thus, the Board was aware that the government was no longer investigating four of the five issues it had identified early in 2002. This fact was very significant to most of the directors, who, as noted above, universally believed that it was only a matter of time before the 35-Day Month issue likewise would be resolved.

In early April 2003, WLRK had a conversation with the USAO, in which the government again expressed the view that the Company had not been forthcoming with regard to the 35-Day Month issue. The USAO explained that the government had developed evidence that there was a 35-Day Month practice at CA, and that the government wanted to give CA one last chance to "come clean." In the words of the Assistant U.S. Attorney ("AUSA") leading the investigation, CA could only prevent a ratcheting up of the investigation by making a "shoestring catch."[120]

WLRK reported this alarming discussion directly to Messrs. Kumar, Woghin, and Zar, but not to any outside CA Board member. At this meeting, Mr. Kumar continued to deny the existence of a 35-Day Month practice, and for the first time instructed WLRK to conduct a "full investigation," using any and all of the Company's resources, to disprove the government's claim. Messrs. Kumar and Woghin told Mr. Savarese that they would promptly relate this development to the Board, but that was not done.

"request for information regarding the events leading up to the reclassification in CA's fiscal year 2000 financial statements, and for the two (2) prior years, of the accounts associated with CA's 'cancel/convert' activity." Letter from John Savarese to Eric Corngold, David Pitofsky, and Alexander Vasilescu, Senior Trial Counsel, U.S. Sec. and Exch. Comm'n (Feb. 6, 2003).

120 A "shoestring catch" is a baseball term for a running catch made near the ground; in other words, a last-minute save.

Thus, in late April 2003, WLRK re-interviewed Messrs. Richards and Rivard, and also interviewed, for the first time, several other CA employees, including Mr. Zar. During his May 19, 2003 telephonic interview, Mr. Zar told WLRK that, generally speaking, "sales accounting people knew that a deal had to be signed by the end of the quarter in which it was booked." Mr. Zar also said that he was not aware that Sales personnel might encourage customers to sign contracts with incorrect pre-printed signature dates without changing the date. During his April 22, 2003 interview, Mr. Rivard told WLRK that the "flash date" was "never purposefully extended to book more revenue." Mr. Rivard said that abuses of the booking system might have occurred, but that he was not personally aware of any. Mr. Richards and a general manager of Sales during fiscal year 2000 both told WLRK that CA Sales personnel used pre-printed customer signature dates on contracts, and that "the sales organization would continue to keep the printed date . . . of 3/31/2000" even if the quarter had already ended. Both Mr. Richards and the general manager told WLRK that they did not worry about revenue recognition issues, and assumed that the Sales Accounting and Finance departments ensured that revenue was accounted for properly "on the back end," although the general manager explained that others believed this was done to allow CA to book revenue in an earlier quarter.

Mr. Savarese told the SLC that Mr. Richards and the general manager were "adamant" that any abuses that had occurred were isolated, and "not uniformly done." Based on these explanations, Mr. Savarese believed that the real issue was a disconnect between Sales and Sales Accounting/Finance – and made plans to present the issue to the government at a scheduled May 20 meeting.

6. **May 13, 2003 Board Meeting**

(a) *The Class Action Litigation and Mediation*

At a May 13, 2003 CA Board Meeting, Messrs. Kumar and Woghin reported to the Board on the status of the Class Actions and the government investigation. Minutes of a Meeting of the CA Board at 8 (May 13, 2003).

According to Mr. Kumar, the Board was very interested in settling the civil litigation at this point. Present in their minds was WLRK's advice to the Board that a settlement would reduce the number of constituencies agitating the government, and would therefore help bring a conclusion to the investigation. With respect to the Class Actions, Mr. Woghin reported that U.S. District Judge Platt had recommended that the parties attempt to mediate a settlement of all outstanding shareholder litigation, and had appointed retired U.S. District Judge Frederick B. Lacey to serve as mediator. *See* Woghin Talking Points at 1 (May 13, 2003). Mr. Woghin told the Board that the plaintiffs would be willing to accept a combination of stock and cash in a settlement, but would not be willing to accept less than $150 million. *Id.* Mr. Woghin reported that, after two (2) sessions with Judge Lacey, and numerous telephone conferences both with Judge Lacey and between the parties, the parties had been unable to reach a settlement. *See id.* at 2.

Mr. Woghin also told the Board that the Company's motion for summary judgment, which had been filed on September 5, 2002, would be placed back on the Court's docket, but that it was "likely the Court will deny our motion and will set a trial date for the fall of 2003." *Id.* at 2. Mr. Woghin did not explain to the Board, and the Board did not ask, why the Court was likely to deny the Company's motion, and there was no discussion of whether there were "bad facts" for CA in the civil litigation.

(b) *The Government Investigation*

With respect to the government investigation, Mr. Woghin reported to the Board that the government had issued additional subpoenas to CA in March and April asking for information covering transactions executed in fiscal year 2000.[121] Mr. Woghin explained that the government was "focused on the timing of revenue recognized at the end of each quarter," but did *not* convey to the Board the substance of Mr. Savarese's April 2003 call or the severity of the government's position. *Id.* Mr. Woghin did, however, tell the Board that the Company had identified certain issues in the process of responding to the subpoenas, including: (i) cases where contracts with pre-printed signature dates were completed in the first few days after the close of a quarter, but booked in the prior quarter; and (ii) contracts completed after the quarter close that were caught by Sales Accounting and "a reserve was taken backing the revenue out from the prior quarter." *Id.* at 3. Mr. Woghin explained that WLRK had recently met with several CA Sales, Sales Accounting, and Finance personnel in order to understand the flow of paperwork from Sales to Finance through the contracting process.

Mr. Woghin then presented to the Board an outline of how CA could propose to resolve the government investigation: "[c]an acknowledge there were some mistakes" but: (i) "nothing was intentional"; (ii) CA "tried to catch errors when they did occur"; (iii) even if errors occurred, they were "not criminal – these were real contracts with . . . real revenues"; (iv) the "problem is historical and has been addressed"; and (v) "all remedial action was taken by the Company *before* the government investigation and on our own initiative." *Id.* (emphasis in original). Mr. Woghin recommended to the Board that the Company attempt to convince the USAO that the problem was neither material nor criminal, and try to negotiate a non-criminal,

121 The subpoenas issued by the government in April, June, and July of 2003 are discussed in detail below.

civil settlement with the SEC. The Board unanimously agreed with this approach, and that set the stage for WLRK to present these arguments to the government.

At this meeting, Gary Fernandes was elected to the Board, which, in the SLC's view, was a significant event due to his extensive experience in the software industry and the perspective he brought to the Board. The directors universally recall Mr. Fernandes being more skeptical than others on the Board of the positions taken by management in general, and Mr. Kumar in particular. According to Mr. Kumar, early in Mr. Fernandes' tenure on the Board, Mr. Fernandes asked Mr. Kumar pointedly whether there had been a systemic practice of extending quarters at CA, and, in response he had told him there was not.

7. **May 20, 2003 Meeting with the Government**

On May 20, Mr. Savarese met with the government prepared to seek a civil settlement and, during the meeting, acknowledged to the government that CA could have had better controls in place. However, while attempting to explain the circumstances underlying certain contracts identified by the government as suspect, the AUSA interrupted him, saying that the meeting should end if Mr. Savarese planned on presenting a series of "excuses" to the government.

Recognizing that his planned approach was ineffective, if not counter-productive, instead Mr. Savarese focused on discussing the inculpatory evidence that the government had asked him to provide. Mr. Savarese told the government that while there were several weaknesses in CA's contracting process, including that Sales employees sometimes left incorrect pre-printed dates on contracts in order to assure themselves of early commissions, CA management "adamantly" insisted that this was not a widespread practice. Mr. Savarese told the government that the situation at CA – as between Sales and Sales Accounting – was analogous to the "right hand not knowing what the left hand was doing," as Sales personnel assumed that Finance and Sales Accounting would know how to properly recognize revenue from contracts with pre-printed dates, while the Finance and Sales Accounting departments relied on the pre-printed dates when determining how to recognize revenue, assuming the Sales employees dated contracts correctly. Mr. Savarese's talking points reflect that he reported to the government that "the weaknesses [in sales accounting] resulted by chance, not by design," and "it is not clear that errors that may have resulted from the system materially distorted CA's business." Savarese Talking Points at 18 (May 20, 2003).

The government was, to say the least, not persuaded. The AUSA asked Mr. Savarese if he was saying that he was not in a position at that time to represent to the government that he knew the full scope of the problem. Mr. Savarese said that he was not, but that from what he had been told and from the documents he had seen, the issue appeared to be confined to isolated instances of human error. When Mr. Savarese raised the idea of a civil settlement, the government representatives rejected this concept and suggested that he ask the Board to have an independent committee – with its own separate counsel – conduct an independent investigation (so that the Company's representatives could be in a position to speak to the government with full knowledge of the situation).

8. **June 9, 2003 Phone Conference with the Government**

In a follow-up call with WLRK on June 9, the government maintained the position that it had staked out in May. The USAO and SEC told WLRK that: (i) they wanted to know the Board's decision regarding the government's suggestion that they initiate an independent investigation; and (ii) to tell him that the government now considered three (3) CA senior executives – Messrs. Zar, Rivard, and Silverstein – "subjects" of the USAO investigation.[122] While Mr. Savarese promptly reported what he had been told to Mr. Woghin, he did not tell any members of the Board. In fact, no one reported the substance of the May 20 meeting or the June 9 telephone call to CA's outside directors until a July 2, 2003 Board meeting, discussed below. Importantly, CA's directors did not receive a first-hand briefing from outside counsel for the nearly six-month period of January 21, 2003 through July 2, 2003.[123]

C. ***June 2003 – A Settlement Framework is Reached***

During this same time frame, settlement negotiations in the Class Actions were progressing. On June 8, 2003, Mr. Kumar provided the Board with an update on the Class Actions by e-mail: "regarding the topic that I called each of you on about 10 days ago. . . . We continue to haggle with [the] other side and are making progress." E-mail from Sanjay Kumar to Alfonse D'Amato, Alex Vieux, Robert La Blanc, Gary Fernandes, Jay Lorsch, Kenneth Cron, Lewis Ranieri, Walter Schuetze, Russell Artzt, Steven Woghin, and Ira Zar (June 8, 2001). Shortly thereafter, Mr. Woghin advised the Board by memo that a tentative global settlement had been reached to settle a number of litigations then pending against CA. These litigations included: (i) the 1998 Class Action; (ii) the 2002 Class Action; (iii) the 2002 ERISA class action lawsuit; (iv) two "greenmail" derivative lawsuits pending in the Delaware

122 According to the U.S. Attorney's Manual, "[a] 'subject' of an investigation is a person whose conduct is within the scope of the grand jury's investigation," while a "target" of an investigation "is a person as to whom the prosecutor or the grand jury has substantial evidence linking him or her to the commission of a crime and who, in the judgment of the prosecutor, is a putative defendant." 9 U.S. Attorney's Manual § 11.151 (2006), *available at* http://ww.usdoj.gov/usao/eousa/foia-reading-room/usam/title9/11mcrm.htm#9-11.151.

123 Mr. Savarese claims that he asked to meet with the Board following his discussions with the government but that Mr. Woghin told him that he himself would keep the Board informed and did not schedule a Board meeting for Mr. Savarese to attend until early July. In contrast, Mr. Woghin recollects only that Mr. Savarese was busy on other matters during this timeframe. Either way, the most salient fact remains – CA's directors did not receive a timely, direct, firsthand account of the government meetings that occurred in May and June.

Chancery Court;[124] and (v) the 2003 Derivative Litigation. Mr. Woghin described the settlement to the Board as follows: "In consideration for a global settlement of all litigation, it is proposed that CA would create a fund to be distributed to the class members of 5.7 million shares of common stock. This represents slightly less than 1% of the outstanding stock of the company and thus would have limited dilutive effect." Memorandum from Steven Woghin to the Members of the CA Board at 1 (undated). At CA's then-current stock price, the settlement was valued at approximately $133.2 million.

At a June 18, 2003 telephonic Board meeting,[125] Mr. Kumar outlined the terms of the proposed settlement. *See* Minutes of a Meeting of the CA Board at 1 (June 18, 2003). Mr. Kumar repeated that the lawsuits "would involve the issuance of 5.7 million shares of the Corporation's Common Stock" and also that the settlement "was tentative and remained subject to the resolution of various issues." *Id.* David Nachman, counsel to the Company in the Class Actions, then discussed the history of the litigation, and the risks and benefits of the settlement. *Id.* Mr. Nachman addressed two (2) main concerns of the Board with respect to the settlement – the amount ($133 million) and the form (all stock, no cash). *Id.* Mr. Nachman expressed his view that the settlement was very much in CA's interest, and further pointed out that while the

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124 The Company described the "greenmail" derivative suits in its public filings as follows:

> In July 2002, two derivative lawsuits were filed against the then directors of the Company in the Delaware Chancery Court. These lawsuits alleged waste and breach of fiduciary duties in connection with the Company's payment to and standstill agreement with Sam Wyly and Ranger Governance Ltd., pursuant to which they agreed, among other things, not to engage in a proxy contest with the Company for five years and to extend Mr. Wyly's noncompete agreement with the Company. By stipulation of the parties to the litigation, the Chancery Court dismissed these lawsuits, with prejudice, in April 2004.

Computer Assocs. Int'l Inc., Annual Report (Form 10-K) at 10 (June 14, 2004).

125 This was Gary Fernandes' first CA Board meeting as a director. At this time, the Board was comprised of Messrs. Artzt, Cron, D'Amato, Fernandes, Kumar, La Blanc, Lorsch, Ranieri, Schuetze, and Vieux.

settlement would be expensive, "proceeding to trial could result in substantially greater costs, as well as potential liability for the Corporation's directors." *Id.* The Board discussed the details of the proposed settlement with an emphasis on the amount of stock involved, and the potentially dilutive effect of the settlement. The Board did not discuss the releases that would be given by CA as part of the settlement at this meeting, but instead focused on the financial aspects of the settlement.

Mr. Nachman also discussed certain factors that he believed would cause the settlement to enhance the likelihood of resolving the government investigation, although he told the Board that resolving the civil cases in "no way assure[s] a speedy or favorable outcome in the investigation." *Id.* at 1-2. It was explained to, and understood by, the Board at this meeting that the government would view a settlement of the Class Actions favorably. In addition, the Board discussed and continued to believe that Milberg Weiss was providing the government negative and inaccurate information about the Company, and that a settlement would put an end to that cooperation.[126]

At the conclusion of the meeting, the directors unanimously felt that settling the civil litigation would be a positive step for the Company, and resolved that the Company should continue to move forward towards a settlement along the lines that had been outlined. The Board reasoned that the market would view the settlement favorably, and that this would have a positive impact on CA's stock price, which would act to offset any dilution caused by the stock issuance.

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126 This was consistent with the advice the Board had received from Mr. Lipton and Mr. Savarese of WLRK at the January 21, 2003 Board meeting, when WLRK identified the Class Actions as an impediment to resolving the government investigation.

Mr. Nachman also recommended that the Board form an independent committee to assess the merits of the settlement. *Id.* Mr. Nachman recognized that he could not advise the Board regarding the settlement because he represented the individual defendants (some of whom were Board members), who would benefit from any releases granted by the Company, and recommended that independent counsel be retained to assist the committee. As discussed further below, the Board subsequently created two (2) separate committees, one (1) to review the class action settlement, and one (1) to review the derivative settlement. *Id.*

Also at this meeting, Mr. Kumar "discussed recent developments in the SEC/Justice Department investigation of the corporation and stated that the Board would meet in the near future to discuss those developments and related matters." *Id.* at 3. This update was, to say the least, very cursory and non-specific as Mr. Kumar did not inform the Board about the most salient facts relating to recent discussions with the government: (i) that the government had identified numerous contracts it believed had been backdated; (ii) that the government was suggesting an Audit Committee investigation; and (iii) that Messrs. Zar, Rivard and Silverstein were "subjects" of the government's investigation. The Board would not learn these facts until July 2, several weeks later.

D. ***July 2003 – The Audit Committee Investigation is Authorized***

At a July 2, 2003 telephonic CA Board Meeting, Mr. Savarese (in his first presentation to the Board since January 2003) provided the Board with a report of his May 20 meeting and June 9 call with the government. *See* Minutes of a Meeting of the CA Board at 1-2 (July 2, 2002).

The Board was told that the government had rejected WLRK's attempts to persuade the government that any improperly-booked contracts were the result of "isolated" mistakes, and "refused to discuss a settlement." Instead, Mr. Savarese reported, among other things, that: (i) in rejecting his settlement offer, both the USAO and SEC "*assert[ed] that they believed that senior management of the company had intentionally held quarters open and used backdated contracts to meet earnings estimates*" (emphasis added); (ii) there were nine (9) transactions with signature dates at issue for fiscal year 2000, and the second quarter contracts alone amounted to $200 million, or one-third of North American license revenue for that quarter; (iii) WLRK had concluded that CA's record keeping made it "difficult" to establish when contracts were actually signed, but that there were "certain transactions in which circumstances suggest that the contract was signed after quarter-end and back dated"; and (iv) the government identified Messrs. Zar, Rivard, and Silverstein as "subjects" of the government's investigation. Savarese Talking Points at 10-11, 3-4 (July 2, 2003).[127] Mr. Savarese proceeded to review certain of the transactions mentioned above, and the circumstances that suggested that the revenue from these contracts might have been prematurely recognized. Mr. Savarese added that:

> We are aware of other contracts, however, which were not booked in revenues because of timing concerns, and, as noted previously, periods in which reserves against contracts received late were taken. It is possible that some contracts were recognized as a result of a mistake in Sales Accounting.

Id. at 9-10. Mr. Savarese also told the Board, twice, as follows:

> As we said at the outset, we want to *emphasize that the senior managers have all denied any knowledge that revenue was intentionally recognized in the wrong period*, but acknowledge that mistakes may have occurred. We *also want to emphasize that we have not conducted an intensive analysis of the facts from the standpoint of GAAP as understood in the 2000 fiscal year*. There is an argument that it would not necessarily have violated

127 Each of the directors understood that being named a "subject" of the government investigation was serious, and meant that the government was examining that person's conduct. To the extent it was unclear, Mr. Savarese read to the Board the relevant section of the U.S. Attorney's Manual that explained the distinction between a "subject" and a "target."

> GAAP at that time to book a contract signed after the end of the quarter if all material terms had been agreed prior to the end of the quarter. *This would entail an in-depth inquiry into the facts and circumstances of each contract, including forensic searches of computer systems and, possibly, inquiries to customers. In sum, we have not reached the conclusion that the company's financial statements were materially deficient or that any person acted wrongfully.*

Id. The Board was also told that the USAO believed that an independent committee of the Board should "conduct a full internal inquiry and report its results to the Government." Minutes of a Meeting of the CA Board at 1 (July 2, 2003).

To the Board, this report was "qualitatively different" from all other reports it had received from Mr. Savarese and management regarding the investigation to date. Indeed, the directors interviewed variously described this report as a "thunderbolt" and a "sucker punch" which precipitated a "deafening" silence on the call.[128] Notwithstanding Mr. Woghin's February 21, 2003 memo,[129] to most, if not all, of the directors, this was the first clear indication that the government was dissatisfied with CA's cooperation, and that reality did not match with what had previously been reported to the Board. Nonetheless, the Board reacted to the news with a measured expression of concern. Although it was clear to the Board that the government investigation had taken a turn for the worse, the directors did not panic.

As a whole, the Board generally continued to believe that the problem was far more limited than it ultimately turned out to be, since it had not seen any evidence, from the government or WLRK (which had developed none), implicating CA's senior managers. At this

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128 In contrast, one director, Mr. Lorsch, told the SLC that from Mr. Savarese's tone, he took away from the meeting that the Board should not "worry" and that the government's accusations lacked merit.

129 As noted above, this memo suggested that the government was receiving information from CA customers that seemed to be at odds with what CA itself was producing, causing the government to question whether CA was responding fully to the government's document requests. Memorandum from Steven Woghin to the Members of the CA Board at 2 (Feb. 21, 2003).

point, simply because Messrs. Zar, Silverstein and Rivard had been identified as "subjects," the Board did not, in general, presume that they were, in fact, complicit in any wrongdoing, and believed that the newly-authorized Audit Committee investigation would shed light on that issue.

At the conclusion of the meeting and its deliberations, the Board unanimously resolved to authorize the Audit Committee to conduct an investigation into CA's accounting practices. *See* Minutes of a Meeting of the CA Board at 2 (July 2, 2003). The Board members believed the investigation was the best way to test the government's allegations and move the investigation to a conclusion. There is no record that the settlement of the civil litigation was discussed at this meeting.

By no later than July 11, 2003, the Audit Committee – which consisted of directors D'Amato, Ranieri, and Schuetze – had retained S&C as its counsel.[130] S&C promptly began the process of understanding the situation, primarily through a series of discussions with WLRK.[131] On July 22, 2003, the Audit Committee had a conference call with two (2) S&C partners, Robert Giuffra and Richard Urowsky, to discuss "the process by which Sullivan & Cromwell intended to assist the Committee in conducting an investigation of the timing of the Corporation's recognition of certain license revenue." Minutes of a Meeting of the CA Audit Comm. at 4 (July 22, 2003).

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130 S&C was selected on the recommendation of Mr. D'Amato, who had worked with S&C partner Robert Giuffra when he was counsel to the Senate Committee on Banking, Housing and Urban Affairs, a committee that Mr. D'Amato chaired.

131 Plaintiffs in the 2005 Derivative Complaint allege that "CA hired [S&C] to replace Wachtell." 2005 Compl. ¶ 247. That is not true. S&C was retained by and represented CA's Audit Committee in connection with its internal investigation, and WLRK continued to represent CA in responding to the government investigation.

Following the Audit Committee meeting, the Board held a meeting at which Mr. Woghin reported on the status of the civil litigation and the government investigation. *See* Minutes of a Meeting of the CA Board at 3 (July 22, 2003). Mr. Woghin provided the Board with more detail regarding the financial terms of the proposed civil settlement, which now included a potential cash component if CA's stock price dropped below a certain level. This cash component was incorporated in the settlement at the request of the plaintiffs and resulted from the uncertainty of the government investigation. *See* Memorandum from David Nachman to Files/CA at 2 (July 28, 2003). Mr. Woghin advised the Board that the Audit Committee had retained S&C to assist with its investigation, and "reviewed the actions expected to be taken in the Committee's investigation, the anticipated timing of each, and certain issues to be considered in carrying out the investigation." Minutes of a Meeting of the CA Board at 3 (July 22, 2003); *see also* Minutes of a Meeting of the CA Audit Comm. at 4 (July 22, 2003).

Around noon on July 24, 2003, Mr. Nachman spoke by phone with Melvyn Weiss, lead counsel to the plaintiffs in the Class Actions, and advised him that the government investigation of CA's accounting practices was continuing. Mr. Nachman told Mr. Weiss that it appeared that the government was no longer interested in the four (4) issues that had formed the basis of the 1998 Class Actions – the KESOP, CA's cancel/convert accounting, Unicenter, and the new business model – but that the government was now focused on the timing of CA's revenue recognition during CA's fiscal year 2000. Mr. Nachman told Mr. Weiss that the Board had authorized the Audit Committee to investigate this issue with the assistance of independent counsel and auditors. *See* Memorandum from David Nachman to Files/CA at 2 (July 28, 2003).

The next day, on July 25, 2003, Judge Platt held a status conference. At that conference, the parties told Judge Platt that they had agreed, subject to CA Board approval, to a global settlement. Further, Mr. Nachman told the Court that he "had *not* ventured any predictions regarding the outcome [of the government investigation]; the company had been successful, apparently, in addressing many of the government's concerns, but *there were certain issues – not even those initially raised, and not those specifically raised in this litigation – that remained subject of intense government scrutiny*." *Id.* at 2-3 (emphasis added). Mr. Nachman also reported that the Audit Committee was investigating the issues that were still the subject of government scrutiny. Finally, Mr. Nachman reported that there was no way to predict the outcome of the government investigation with certainty, which is why the plaintiffs had requested "down-side protection" (the cash component) in the initially all-stock settlement. *Id.*

That same day, Mr. Woghin sent a memo to the Board reporting that the parties to the civil litigation had met with Judge Platt and agreed, subject to Board approval, to settle the litigation on substantially the same terms presented to the Board by Mr. Nachman at the June 18 Board meeting. The memo summarized the proposed settlement for the Board, which now: (i) created a fund of 5.7 million shares from which all claims and attorneys' fees would be satisfied; (ii) included a provision whereby 2.2 million of the 5.7 million shares would be converted to cash if, at the time the settlement became final, CA's shares traded at $23.43 or less; and (iii) provided that CA would contribute a maximum of $1.75 million towards the costs of administering disbursement of the settlement fund. Memorandum from Steven Woghin to the Members of the CA Board at 1 (July 25, 2003).

E. ***August 2003 – The Settlement is Approved***

1. **The August 4, 2003 S&C Meeting with the Government**

On August 4, 2003, Messrs. Giuffra and Urowsky of S&C met with representatives of the USAO and the SEC for the first time to introduce themselves, and to get an understanding of the status of the investigation. At the meeting, the government told S&C that (i) it was dissatisfied with the Company's and counsel's cooperation (particularly the pace and volume of e-mail production), and (ii) it had evidence demonstrating that the Company and its senior managers had engaged in the 35-Day Month practice to falsely represent the Company's quarterly financial reports. The S&C lawyers were surprised with the government's "chilly" tone, which conveyed the impression that the situation was "quite serious," and that the Audit Committee investigation had to "get moving." The USAO and the SEC, however, declined to provide specifics to S&C concerning the evidence that the government had and, specifically, which executives at CA were involved.

On August 7, 2003, at the request of Walter Schuetze, Mr. Woghin sent a memo to the Board reporting on the August 4 meeting. The one-page memo states:

> In addition to expressing dissatisfaction with both Wachtell Lipton and the company's cooperation to date, *the government explained that it believed that the company had engaged in a systematic practice of backdating license agreements*. This is what the government refers to as the "35 day month." *It believed* (but without offering any proof) *that senior managers of the company (both current and former) had directed this practice and that it was done with the specific intent to represent falsely the company's quarterly revenues.*

Memorandum from Steven Woghin to the Members of the CA Board (Aug. 7, 2003). The memo also states that the government expected the Audit Committee to complete its investigation by October 15, 2003. *Id.*[132]

Despite the stark nature of the memo, the directors for the most part viewed the information as largely reflecting what they had heard at the July 2 Board meeting.[133] All the

132 Although S&C did not draft or comment on the memo – it was written by Messrs. Woghin and Schuetze – Messrs. Giuffra and Urowsky confirmed that the memo accurately reflected what transpired at the meeting.

directors expressed the belief that the Audit Committee, led by Mr. Schuetze (who was the former Chief Accountant of the SEC), would get to the bottom of these issues, including whether there was any wrongdoing. Further, most of the directors continued to take some degree of comfort from the fact that the government had not offered the Company or the Audit Committee any specific evidence or factual detail to support its claims. At this time, in Mr. Giuffra's view – which was formed in large part by his discussions with Mr. Savarese and which he shared with the Audit Committee – there was still a possibility that the government was only posturing or "saber-rattling" in an attempt to extract a favorable settlement.

2. Retention of Counsel for the Settlement Committees

On August 11, 2003, Mr. Woghin retained counsel for the two (2) committees that were to consider the proposed civil settlements. Mr. Woghin selected Peter Fleming, a partner at Curtis, Mallet-Prevost, Colt & Mosle LLP, and James M. McGuire, counsel at White & Case LLP, to represent the class action and derivative settlement committees, respectively. Mr. Nachman recommended Mr. Fleming to Mr. Woghin, and Mr. D'Amato had suggested Mr. McGuire to Mr. Woghin several months earlier (as an attorney CA might consider retaining to assist WLRK in dealing with the government investigation; Mr. Woghin and Mr. D'Amato did not discuss Mr. McGuire in this context, or at this time).[134]

On August 14, 2003, Mr. Woghin sent a memo to the Board outlining the process for the settlements, and attaching the biographies of Messrs. Fleming and McGuire.[135]

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133 Given what they had been told at the July 2 Board meeting, this memo was "not news" to the Board, and Mr. Woghin was not contacted by any Board members to discuss this memo.

134 According to Mr. Woghin, the delay in retaining counsel for the committees, from June 18 to August 11, was attributed to several procedural and mechanical issues that CA needed to resolve prior to retaining counsel, such as conflict checks.

135 The SLC discovered that the biography for James M. McGuire distributed to the Board was not, in fact, Mr. McGuire's biography. Rather, it was the biography of a White & Case ("W&C") partner named James J. McGuire. James J. McGuire is a former Assistant U.S. Attorney for the Southern District of

In the memo, Mr. Woghin explained that the original settlement committee, which was established on June 18 and was comprised of directors D'Amato, Lorsch, Ranieri, and Schuetze, would review the class action settlement. A separate committee comprised of the independent non-interested directors who were not defendants in the derivative suit – directors Cron, Fernandes, La Blanc, Lorsch, Schuetze, and Vieux – would review the derivative settlement. *See* Memorandum from Steven Woghin to the Members of the CA Board (Aug. 14, 2003).

From August 11 to 18, 2003, Messrs. Fleming and McGuire each took steps to review the respective settlements in preparation for meetings with each committee, which were scheduled to occur telephonically on August 19.

Mr. Fleming received a preliminary briefing on the class action litigation from Mr. Nachman, and then reviewed the relevant pleadings, including the complaint and summary judgment papers. Mr. Fleming billed the Company a flat fee of $25,000 for his evaluation of, and advice regarding, the settlement.

Mr. McGuire reviewed the papers in the class action and derivative litigations, and had numerous conversations with Messrs. Nachman and Savarese regarding issues related to the derivative settlement. According to his billing records, Mr. McGuire devoted a total of

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New York, and had significantly more experience with white collar and complex commercial litigation than James M. McGuire. Given his lack of experience in these areas, James M. McGuire (who had most recently served as counsel to then-New York Governor George Pataki) enlisted the help of then-W&C partners, Richard Holwell, now a U.S. District Judge, who had more experience in securities and fiduciary duty matters, and Lawrence Byrne, a former Assistant U.S. Attorney. Mr. Holwell was also present for the telephonic meeting held by the derivative settlement committee on August 19, discussed in detail below, but no one involved in the call recalls him participating substantively. Mr. Holwell, who spent a total of 8.4 hours on the matter, declined to be interviewed by the SLC, informing the SLC through a representative of White & Case that he had no recollection of the events.

sixty-five (65) hours to the assignment.[136] In total, Mr. McGuire listed eight (8) calls with Mr. Nachman on his billing records prior to the August 19 committee meeting. Among the issues discussed on these calls – and particularly relevant to the SLC – was whether the class action plaintiffs would agree to a settlement if the derivative case was left unsettled, or if the releases in the derivative case were narrowed or limited. Mr. Nachman was emphatic with Mr. McGuire that he believed the settlement of the class action and derivative litigations was a "global" deal, and that it was probable that the settlement would collapse if the releases, which would run from the Company to its officers and directors, were limited or altered in any respect.

On August 18, Mr. McGuire spoke with William Federman, the attorney representing the derivative plaintiffs, in part to determine whether the proposed settlement was, and had to be, part of a "global" deal. Mr. McGuire concluded, based on his conversations with counsel, including Messrs. Federman and Nachman, that the Board could not approach the settlement of the derivative and Class Action litigations in any way other than as a "global" deal.

Mr. McGuire also spoke several times with Mr. Savarese to educate himself about the internal and government investigations, and discussed the potential impact of the releases contained in the derivative settlement on the government investigation.[137] In addition to providing factual background on the government investigation, Mr. Savarese expressed concern to Mr. McGuire about whether the Board's credibility with the government would be negatively affected if the Board released CA's management from liability prior to the resolution

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136 In addition to Mr. McGuire, other W&C lawyers, including Messrs. Holwell and Byrne, devoted about forty-seven (47) hours to the matter.

137 Mr. McGuire also spoke briefly to Mr. Giuffra, who told Mr. McGuire about S&C's August 4 meeting with the government, and advised him that he was "too new" to the situation to give a proper assessment as to how the investigation would turn out.

of the Audit Committee and government investigations. Mr. Savarese told the SLC that he did not take a position on this issue, but merely raised it as one to be considered by the derivative settlement committee. Mr. Savarese discussed this issue with Messrs. McGuire, Woghin and Nachman, but did not raise it with the Board. In fact, none of the directors were ever made aware, by any counsel, internal or external, that Mr. Savarese (or anyone else) had raised this as an issue to be considered.

That said, and as noted above, Messrs. Lipton and Savarese had, during the course of the investigation, repeatedly told the Board that it was unlikely that CA could resolve the government investigation unless the civil litigation was first settled. As such, Mr. Ranieri recalled that, from his perspective, the entire Board understood a civil settlement to be positively related to the resolution of the government investigation. Mr. Fernandes believed that the one factor that "got [the Board] over the hurdle" in order to settle the civil litigation was that the settlement was thought to be "the key" to resolving the government investigation.

Mr. McGuire also spoke with Messrs. Savarese and Nachman, among others, about the possibility of limiting the scope of the releases in the derivative settlement. Mr. Nachman told Mr. McGuire that, in his opinion, it would be within the Board's business judgment to grant full global releases notwithstanding the Audit Committee investigation. Ultimately, the idea of limited releases was apparently raised among counsel as a potentially viable alternative, since it provoked a response from counsel for Charles Wang.

On August 18, 2003, Messrs. McGuire and Savarese received a memo from Mr. Wang's attorneys, which advocated and exhorted that Mr. Wang should be given a full release in connection with the settlement. The memo, which contained several obvious misstatements of fact and law, advocated a position that a global settlement (including a full release for all individual defendants) is "consistent with the position CA has taken in its public disclosures" and "anything less than a global settlement unnecessarily jeopardizes court approval." Memorandum from Daniel Murdock and Robert Bostrom, Winston & Strawn LLP, to James McGuire at 1-2 (Aug. 18, 2003). The memo also stated that it would be an "irrational exercise" of the directors' business judgment to block a global settlement in order to preserve claims against the individual defendants due to market risks and the risk of additional exposure. *Id.* at 1-3. Finally, the memo stated that "a partial settlement . . . would also create the impression that CA's independent directors have suspicions (which they presumably do not have)." *Id.* at 2.

Mr. McGuire stated that the memo was "not very persuasive" since it was "aggressive" and its claims were "pretty preposterous." Mr. Savarese responded by memo dated August 19 (with a copy to Mr. McGuire), in order to "correct certain of the material errors" made by Mr. Wang's counsel, including that: (i) Mr. Wang's attorneys had implied that CA and the individual defendants were "jointly represented" by WLRK when this was clearly not true; (ii) CA had not, as Mr. Wang's attorneys had alleged, publicly stated that the government's allegations were "unsupportable"; and (iii) Mr. Wang's attorneys incorrectly claimed that the Audit Committee's investigation was "commenced . . . simply to convince skeptical prosecutors of what CA's own investigation has revealed." Memorandum from John Savarese to Daniel Murdock and Robert Bostrom at 1-2 (Aug. 19, 2003).[138] Neither Mr.

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[138] In a further response, dated August 20, Mr. Wang's counsel asserted that its August 18 memo referred only to the allegations of wrongdoing alleged in the civil actions, not the allegations made by the government. Letter from Daniel Murdock to John Savarese and Warren Stern at 1 (Aug. 20, 2003). They also acknowledged that their "observation" on the Audit Committee investigation was "hyperbolic" and "not intended to denigrate the investigation's integrity or CA's good faith in initiating it." *Id.* at 2.

Wang's memo nor Mr. Savarese's response was distributed to the members of the derivative settlement committee or to any other Board member.

3. The Settlement Committees Meetings

On August 19, 2003, the class action and derivative settlement committees each participated in a telephonic meeting with their respective counsel. Recollections vary, but those involved recall that each call lasted between thirty (30) minutes and one (1) hour. The members of both committees participated in the class action call, which occurred first.[139] The members of the class action settlement committee then dropped off the call when the derivative settlement committee heard from its counsel and deliberated. Mr. McGuire listened in on the class action settlement call, and Mr. Woghin, who participated in both calls, was the only member of CA management present on either of the calls. None of the committee members recall consulting with their counsel, requesting or receiving additional materials, or consulting informally with each other, prior to the calls.

(a) *The Class Action Settlement Committee Meeting*

This call began at 7:00 a.m. Eastern Standard Time on August 19. Mr. Fleming told the committee that he had reviewed the complaint and the summary judgment papers in the class actions, and that he estimated the Company's exposure in the class action litigation at between two (2) and five (5) billion dollars. Mr. Fleming reviewed the history of the mediation with Judge Lacey, who he said was "willing to call fools fools," and told the directors that Judge Lacey had recommended a settlement "substantial[ly in] excess" of the amount ultimately agreed upon. Fleming Talking Points at 1 (Aug. 19, 2003).

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139 Mr. La Blanc, who was a member of the derivative settlement committee, did not participate in the class action settlement committee call.

Mr. Fleming told the committee that the risks of not going forward with the settlement were: (i) the two to five billion dollar exposure; (ii) if a trial were lost, a successful appeal would be unlikely in the current environment (post-Enron/WorldCom); (iii) the continued distraction of management and costs to the Company; and (iv) continued pressure on CA's stock. *Id.* at 2. While Mr. Fleming told the committee that he "was a trial lawyer at heart," and thus did not generally like to settle a case, he advised the committee that he would strongly counsel against trying this case. Further, Mr. Fleming told the committee that this case was especially risky since the Company would not only have to win the first trial, but would have to "win them all." Finally, Mr. Fleming's notes state that he recommended the class action settlement "in [the] strongest possible way." *Id.*

Most, if not all, of the directors interviewed recalled the two-to-five-billion-dollar figure, and that Mr. Fleming strongly advocated settling the class action. For example, Mr. Cron stated that the number was "etched in his mind"; Mr. D'Amato noted that CA "could have lost billions of dollars" if the case went to trial; and Messrs. Lorsch, Ranieri, and Schuetze told the SLC substantially the same thing.

These recollections are consistent with the one set of handwritten notes from the settlement calls that were produced by the directors. Mr. Schuetze's notes from the class action committee call state, "'Exercise of Business Judgment Rule;' Possible loss $2 – 5 billion; Trial likely; Proposed settlement – Issuance 5.7 million shares CA stock plus possible $52 million cash if price declines; Believes settlement is good for CA – in CA's best interest – recommend settlement." Notes of Walter Schuetze (Aug. 19, 2003). Mr. Schuetze recalled that there was a lengthy discussion about the background of the litigation and the benefits of settling, and, following Mr. Fleming's presentation, the committee concluded that the settlement was in CA's best interests. The class action settlement committee voted unanimously to recommend the settlement to the full Board.

(b) *The Derivative Settlement Committee Meeting*

Following the class action settlement committee call, the members of that committee dropped off the call, and the derivative settlement committee had its call with Mr. McGuire (and Mr. Holwell, who as noted above, had listened in on Mr. Fleming's presentation). Mr. McGuire provided the committee with an overview of his credentials, and an overview of the allegations contained in the derivative action. Mr. McGuire explained to the derivative settlement committee that he had reviewed the settlement and studied the summary judgment papers filed in the class action, but had *not* conducted an independent factual investigation of the allegations contained in the derivative complaint. *See* Memorandum from James McGuire and Richard Holwell to Files at 2 (Aug. 19, 2003).

None of the committee members questioned Mr. McGuire about the specifics of what he had done to prepare for the call, but rather relied upon the reputation of the White & Case firm in concluding that they could rely on his advice. That said, Mr. McGuire did not advise the committee that he needed any additional time in order to adequately advise the committee or that he was in any way uncomfortable about the advice he was giving, and the committee members assumed that he would have done so if it was necessary.

Mr. McGuire told the committee that he believed it likely that Judge Platt would deny the Company's motion for summary judgment because, although "the motion appeared strong . . . it was unusual for such motions to be granted." *Id.* Mr. McGuire said that absent a settlement, both the class action and derivative litigation would go to trial. Mr. McGuire then outlined the terms of the derivative settlement for the committee, noting that although the Company would not receive a cash payment, "certain existing and new corporate governance measures would be maintained for a period of some years." *Id.* Mr. Woghin then outlined for the committee what those specific measures were. *Id.*

According to those who participated on the call, Mr. Fernandes asked what the potential ramifications would be of granting the releases if it turned out that CA management was found to have engaged in wrongdoing, and whether it was possible for CA to settle without giving releases (in whole or in part) to its officers and directors. According to Mr. McGuire's summary of the meeting (drafted that day), in response to Mr. Fernandes' question, he said that:

> while he was not aware of any evidence that any of the director defendants had engaged in wrongdoing, if the U.S. Attorney's Office reached the conclusion that a director had engaged in criminal misconduct, they would then have to decide whether to pursue charges against the corporation. In making that decision, one of the factors that the prosecutors would consider was how the Company had responded to evidence of misconduct, including whether the Company had improvidently released potential claims against the director defendants in the derivative litigation.

Id. at 3-4.

In considering Mr. McGuire's advice, the derivative settlement committee also discussed the possibility of (i) deferring the settlement until after the conclusion of the Audit Committee and government investigations, or (ii) "narrowing or tailoring" the releases to preserve the Company's ability to pursue future action against certain individuals. Recollections vary as to the extent that these issues were discussed. One director recalled that the issues were discussed "fairly exhaustively" and another director told the SLC that it was "very hard to get to yes" on the releases. On the other hand, other directors recalled a much shorter discussion, and Mr. Vieux does not recall the issue being discussed at all. The SLC concludes that the Board discussed the issue to some extent and generally relied on the advice of Mr. McGuire, who told the committee that the settlement was an "all or nothing" deal.

This is consistent with the contemporaneous documentary evidence. Mr. Schuetze's notes from the call state in their entirety:

> "Exercise of Business Judgment Rule"; trial likely; In settlement, institute therapies – maintain for three years certain therapies; Cost of trial – 30 to 40 million plus distraction; Query – what about partial releases to individual directors? Group B concluded, based on its judgment, given all of the facts, that the Board should go forward with a global settlement with full releases to directors.

Notes of Walter Schuetze (Aug. 19, 2003). According to Mr. McGuire's summary memo concerning the meeting:

> Counsel pointed out that deferring settlement of the derivative actions could threaten to upset the global resolution of both the class actions and derivative actions and, further, that an attempt to limit the release of claims against the director defendants could also endanger a global resolution of all the litigation.

Memorandum from James McGuire and Richard Holwell to Files at 4 (Aug. 19, 2003).

Mr. McGuire's memo describes the conclusion of the meeting as follows: "Further discussion ensued and the directors concluded that the avoidance of this risk, together with the other benefits of settlement outlined by Mr. McGuire, outweighed whatever theoretical benefits might result from a continuation of the derivative actions." *Id.* Ultimately, the committee concluded that the derivative settlement was in the best interests of CA because it was (i) a necessary and advisable part of the global settlement of the civil litigation, and (ii) an important step in laying the groundwork for an ultimate resolution of the government investigation, as counsel had explained to them earlier in 2003.

Immediately following the derivative settlement committee conference call, Mr. McGuire sent an e-mail to Mr. Woghin, which stated:

> I think the spirited, exceptionally thorough discussion among a highly informed group of independent directors will itself go a

> long way at preventing any of the harm that conceivably could ensue in the event that the possibility we discussed ever arose. The company is very fortunate to have directors of their caliber.

E-mail from James McGuire to Steven Woghin (Aug. 19, 2003).[140] Mr. Woghin told Mr. Kumar via e-mail:

> Had a VERY thorough discussion with Committee B, including *what if we don't settle the derivative suit, what if we give limited releases*. Lots of probing of the possible effect on the government, exposure of this board, etc. Committee ultimately unanimously agreed to recommend to the board settlement of the derivative action with the standard form of releases.

E-mail from Steven Woghin to Sanjay Kumar (Aug. 19, 2003) (capitalization in original) (italics added). Mr. Woghin told the SLC that this e-mail was not intended to be self-serving, but rather was designed to keep Mr. Kumar apprised of what had actually occurred.

At an August 21, 2003 CA Board Meeting, at which all of the outside directors participated telephonically, Mr. Kumar reported on the actions taken by the committees in connection with the settlements. He then summarized again the terms of the proposed settlement and reviewed the creation of the settlement committees. The minutes reflect that the respective committee chairs – Mr. D'Amato with regard to the class action litigation and Mr. Lorsch with regard to the derivative litigation – noted that each respective committee had undertaken a thorough review of the financial terms and the risks, and both committees had unanimously recommended that the Board approve the settlements. *See* Minutes of a Meeting of the CA Board at 1-2 (Aug. 21, 2003).

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140 The "possibility" discussed on the August 19 call – and likely referred to here – was the possibility that the government would find that representatives of the Company had "engaged in criminal misconduct." Memorandum from James McGuire and Richard Holwell to Files (Aug. 19, 2003). Mr. McGuire said that, if this were to occur, the government "would then have to decide whether to pursue charges against the corporation." *Id.*

Certain directors at the meeting raised the possibility of deferring the decision on the settlement to August 27, 2003, the date of the Board's annual meeting. However, the minutes state that CA management explained to the Board that it would be "desirable" to announce the settlement prior to the annual meeting. *Id.* at 2. Indeed, the "desire" to make an announcement at CA's annual meeting was, in part, a driving force behind the timing of when the Board met to decide to authorize the settlement. The Board then approved the committee recommendations: "Following discussion, the Board approved the settlement, with Messrs. Artzt and Kumar abstaining." *Id.*

F. ***Post-Settlement Approval; the Audit Committee Investigation Continues***

At the August 27, 2003 annual CA Board Meeting, Mr. Giuffra made his first presentation to the full Board. Mr. Fernandes' notes of Mr. Giuffra's presentation at this meeting reflect that he gave a decidedly negative report: "Government's Attitudes: Evidence of tens of millions of post quarter transaction bookings; Backdated contracts [included in revenue and] earnings; Inadequate response to discovery requests; No Question on Mis-Booking – only on [how] high up the management chain; they are more aggressive & emphatic." Notes of Gary Fernandes (Aug. 27, 2003). The Board felt that this report echoed what they had been hearing for the last two (2) months: that the government had information that the Board did not, but that still no evidence had been provided about any specific acts of wrongdoing by any CA executive.

Despite this report and, as discussed further below, the many other events that would occur, and facts that would be uncovered during the Audit Committee investigation before the settlement was finally approved on December 8, 2003, no director ever questioned, or reconsidered, whether it remained in the Company's best interest to grant releases to all of CA's officers and directors. When asked about this, the directors responded in one of three ways: (i) despite having many top law firms advising them (WLRK, S&C, White & Case, Curtis-Mallet, Covington & Burling, and Piper Rudnick), no counsel ever suggested they revisit the issue and the directors assumed counsel would have advised them if they should – or even could – re-evaluate the settlement;[141] (ii) through December 2003, the directors had no information that led them to believe that *very* top management (Messrs. Wang or Kumar) had been involved in any wrongdoing; and (iii) as additional negative facts arose, the benefit to shareholders of the global settlement became even more apparent and thus the risk of upsetting the global deal even greater.

On August 29, 2003, Judge Platt preliminarily approved the settlement. The commentary from financial analysts that covered CA's stock was overwhelmingly positive. For example, Banc of America, which rated CA as a "buy," reported that the settlement "*could lead to some resolution with the SEC and DOJ*." Banc of Am. Sec., Company Settles All Accounting-Related Shareholder Lawsuits; Could Pave Way for Progress with SEC and DOJ (Aug. 25, 2003) (emphasis added). Similarly, Friedman, Billings, Ramsey & Co. ("FBR") upgraded CA to "Outperform," noting that "[i]t appears that CA has been able to settle these lawsuits for *a very small amount*." Friedman, Billings, Ramsey, CA: Computer Associates Litigation Overhang Removed – Upgrading to Outperform (Aug. 25, 2003) (emphasis added)). FBR added that the settlement was "*extremely positive for the company* . . . as it removes . . . a much greater unknown" than the government investigation. *Id.* (emphasis added). Consistent with Wall Street's reaction, CA's stock price rose from $24.82 on August 25, when the settlement was announced, to $27.00 by the close of business on September 3.

141 Some directors believed that once approved, the decision to settle could not be reversed, while others recognized that the settlement was still subject to Court approval.

1. The September and October 2003 CA Document Productions

It is at this point in the chronology of the government investigation that the documents which have come to be known as the "23 Boxes" were collected and analyzed. Given the importance attached to these documents by the plaintiffs in connection with the Rule 60(b) motions and the press reporting on this issue, the SLC was determined to understand their origin.

The origin of these documents is the subject of great debate due to a September 24, 2004 Wall Street Journal article entitled "In CA Probe: Recovered Emails, Surprise Cache of Documents."[142] The press account of the origin of the documents, in the view of the SLC, is largely inaccurate. This press account, including its title, created the myth of a "surprise cache of documents" that Mr. Woghin and CA had collected, and then concealed, in order to prevent their discovery. The article references a "surprise delivery" of twenty-three (23) boxes of documents by Mr. Woghin, implying that, for whatever unexplained reason, he had ended his document-withholding scheme and unexpectedly produced the documents that he had purportedly collected and hidden.[143] The SLC has concluded that the facts do not support this version of the events. The SLC found instead that the evidence supports the view that the Company failed to produce certain of these documents earlier in the government investigation

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142 This article seems to be largely the source of the declarations by plaintiffs' counsel in the Class Action cases, who allege that Mr. Woghin "withheld" and "intentionally concealed" these documents. Declaration of Alexander Widell at 4, *In re Computer Assocs. Class Action Sec. Litig.*, No. 98 Civ. 4839 (TCP) (E.D.N.Y. Sept. 12, 2006); Joint Declaration of Samuel K. Rosen and Lee Squitieri, *Computer Assocs. Int'l, Inc. Derivative Litig.*,. No. 04 Civ. 2697 (TCP) (E.D.N.Y. Sept. 12, 2006). As explained further below, as a factual matter there is no evidence to support such a claim. The two declarations cited above were not, and could not have been, based on actual knowledge of the facts.

143 For instance, the Wyly movants read the Wall Street Journal article to indicate that in September or October 2003, after the settlement had been finalized, "CA's lawyers became aware that Woghin . . . brought 23 boxes of documents he had been withholding to the[ir] attention . . . ." Memorandum of Law in Support of Motion for Relief Pursuant to Rule 60(B) of the Federal Rules of Civil Procedure at 6-7, *In re Computer Assocs .Class Action Sec. Litig.*, No. 98 Civ. 4839 (TCP) (E.D.N.Y. June 14, 2005). As discussed below, this account is not accurate.

due to markedly deficient and delayed document collection efforts during the early part of 2003, and that, once remedied, the documents were collected and produced in due course.

(a) *The 2002 Document Requests and Grand Jury Subpoena*

Beginning in late February 2002, the SEC began issuing voluntary document requests to CA relating to each of the areas of investigation identified by the government at the outset of its investigation (which are described above). Specifically, on February 26, 2002, the SEC issued a voluntary document request to CA seeking seventeen (17) broad categories of documents (the "SEC Document Request"). On February 27, 2002, WLRK, the SEC, and the USAO met to discuss CA's response to the SEC Document Request, including certain limitations on the request proposed by WLRK and the timing of CA's production. Initially, according to WLRK, the SEC agreed to permit CA to narrow the scope of its document productions in various respects. For example, the government permitted CA to limit the scope of certain of its collection efforts to documents maintained in the "Company's Finance Department license files" in order to expedite its response, but reserved the right to broaden its request at a later point. *See* Letter from John Savarese to Alexander Vasilescu, U.S. Sec. and Exch. Comm'n, and David Pitofsky at 2 (Mar. 12, 2002); Letter from John Savarese to David Pitofsky and Alexander Vasilescu at 2 (Apr. 24, 2002); Memorandum from John Savarese to File (Nov. 11, 2003). As such, at this time, the Company did not attempt to collect documents from outside CA's central files. Memorandum from John Savarese to File (Nov. 11, 2003).

The document collection process established by the Company in 2002, and followed through the fall of 2003, was that CA would collect and review documents internally, and then provide the potentially responsive documents to WLRK, who would then produce the documents to the government on behalf of the Company. The Company refused WLRK's offer to manage the documents collection and production, and established this protocol purportedly because (i) CA had substantial experience in producing documents, and (ii) CA was seeking to reduce its costs. Even with the benefit of hindsight, it is unclear whether the 35-Day Month practice would have been uncovered earlier had WLRK handled the document collection at CA. Nonetheless, that same hindsight makes plain that it certainly would have been a better practice than the one employed by CA and WLRK.

WLRK, on behalf of the Company, began producing documents from the Finance department's North American license files in response to the SEC Document Request on March 7, 2002, and continued to do so on a rolling basis. By April 19, 2002, CA, through WLRK, had produced sixty-eight (68) boxes of documents to the SEC, and indicated that "a very substantial amount of additional documents" would be forthcoming. Letter from John Savarese to Alex Vasilescu at 2 (Apr. 19, 2002). By May 1, 2002, WLRK informed the government that CA had completed its response to the SEC Document Request "as limited" by various agreements with the government, with the exception of the Company's response to Request No. 8 of the SEC Document Request, which called for, among other things, "all documents concerning contracts or licenses that were backdated." Letter from John Savarese to David Pitofsky and Alexander Vasilescu at 2 (May 1, 2002); *see* Letter from Alexander Vasilescu to John Savarese (voluntary request attached) (Feb. 26, 2002).

With respect to Request No. 8, WLRK informed the government that the Company's response required "further review that remains ongoing." Letter from John Savarese to David Pitofsky and Alexander Vasilescu at 2 (May 1, 2002). Indeed, at this time the Company had not made any efforts to specifically search for backdated license agreements. Memorandum from Donald Watnick to File at 1 (Mar. 29, 2002). Instead, at the recommendation of Mr. Woghin and Donald Watnick, CA's then-head of litigation, PwC reviewed the contracts produced to the government in response to Request Nos. 1, 2, and 3 of the SEC Document Request[144] to determine whether "either the customer's signature or the Company's counter-signature on a contract took place after the period in which the revenue associated with such contracts was recorded."[145] Letter from John Savarese to Alex Vasilescu at A-2 (Apr. 19, 2002).

Throughout the summer of 2002, the Company continued to produce documents in response to additional informal requests from the SEC, including the documents reviewed by PwC in connection with the 532 Contract Study. Then, as noted above, on December 19, 2002, the USAO issued the December Subpoena, which was the first grand jury subpoena issued to CA. As described above, the December Subpoena called for sixteen (16) contracts and all documents related to those contracts, including drafts, internal and external correspondence (including e-mail), a list of all persons who worked on the transactions, and other documents. In addition, the government increased its efforts to subpoena third parties, the majority of whom

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144 Specifically, Request Nos. 1, 2, and 3 of the SEC Document Request called for:

> 1. All contracts and licenses, correspondence and communications, concerning the sale or license of software to CA customers whose accounts reflect the top sources of revenue for CA during FY 1995-2001.
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> 2. All contracts and licenses, correspondence and communications, concerning the sale or license of software to the following CA customers: Merrill Lynch and Co., NASDAQ, Electronic Data Systems Corp., Citibank, N.A., Time Warner and/or AOL Time Warner, CS First Boston, J.P. Morgan, and any of their independent divisions, subsidiaries or other related entities.
>
> 3. All contracts and licenses, correspondence and communications, concerning the sale or license of software to CA customers whose accounts reflect the top sources of revenue for the sale or licensing of Unicenter TNG during FY 1995-2001.

Letter from Alexander Vasilescu to John Savarese (voluntary request attached) (Feb. 26, 2002).

145 This review took several weeks and was separate from the 532 Contract Study, which PwC subsequently conducted at WLRK's request. Memorandum from John Savarese to File at 3 (Dec. 2, 2003). Like the 532 Contract Study, PwC did not review documents other than the contracts themselves to determine whether they were signed in a timely manner.

were CA customers, to obtain additional documents. On January 10, 2003, the Company began producing documents responsive to the December Subpoena from CA's central licensing files, and indicated that it would continue to produce responsive documents on a rolling basis. According to WLRK, the Company then endeavored to collect documents from areas outside of the Finance department, including from the GSO, Legal and Sales Accounting departments, all in response to the December Subpoena.[146] Memorandum from John Savarese to File (Nov. 11, 2003).

It was at this time that CA began to collect, and produce, certain documents that WLRK surmised that the government had received from CA's customers and found troubling. For example, as discussed above, on January 29, 2003, in connection with a larger production, CA produced to the government an e-mail relating to a license agreement with a large CA customer, which said, "remember, no backdating on this one." At the time, with explanations provided by CA management and others, the Company was able to offer, in WLRK's view, seemingly innocent and plausible explanations for such documents both to the government and to the Board.[147] As such, as described above, in a letter to the USAO accompanying the January 29 document production, WLRK "emphasized" that CA continued to "deny vigorously that it has intentionally recognized revenue in a period other than the one in which the contract

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146 The Legal department, with the help of the Finance department, sought to identify the CA employees involved in the negotiation, drafting, or approval of the identified transactions, and then personally contacted them and requested that they provide all documents related to the transactions contained in the employees' personal files. *See* E-mails between Steven Woghin and Donald Watnick (Jan. 2, 2003). CA did not send out document collection memos or e-mails to broad groups of employees, nor did it image the computers of employees involved in the transactions or otherwise attempt to independently obtain electronic documents related to the transactions off of CA's back-up servers.

147 As discussed above, this document, and others collected around this time, were discussed at CA's January 21, 2003 Board meeting. At that meeting, WLRK presented the explanations provided by CA employees – including the Criminal Defendants, whom the Board did not suspect of wrongdoing at the time – for the documents that CA believed were troubling the government.

was signed." Letter from John Savarese to David Pitofsky and Eric Corngold at 7 (Jan. 29, 2003).

Then, as discussed above, in a February 12, 2003 letter from the USAO to WLRK enclosing a new grand jury subpoena requesting the "originals" of all documents produced in response to the December Subpoena, the USAO expressed dissatisfaction with the level of CA's document production efforts. In that letter, the government specifically cited the Company's failure to produce a significant number of drafts, correspondence, and other documents relating to license agreements identified in the December Subpoena. The letter states the government's belief that:

> CA has not complied fully with the subpoena served on CA dated December 19, 2002. . . . Given the complex nature of CA's licensing agreements and our understanding as to the vigorous negotiations commonly preceding the execution of such agreements, we expected to receive a significant volume of documents in addition to the final, executed agreements; however CA has produced very few drafts and limited correspondence (either internal or external).

Letter from David Pitofsky to John Savarese at 1-2 (Feb. 12, 2003). In addition, the USAO called Mr. Savarese to express its dissatisfaction with the number of e-mails produced by the Company.[148]

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148 The government's frustration regarding CA's document collection and production efforts was, as discussed above, in part relayed to the Board in a February 21, 2003 memo from Mr. Woghin. The memo states that the "government questions whether we have fully and completely responded to their subpoena since they apparently have received some materials from CA customers that we have not been able to locate and produce." Memorandum from Steven Woghin to the Members of the CA Board at 2 (Feb. 21, 2003). Mr. Woghin stated further that, "to satisfy themselves that the documents [CA] produced were complete, they have now requested that we produce the 'originals' of all documents previously produced." *Id.* at 3. Mr. Woghin told the Board that CA would produce those documents to the government by the end of the week. *Id.* Mr. Woghin told the SLC that this memo painted a "rosier" picture than that which actually existed. The Board was not provided with the USAO's February 12 letter to WLRK at the time.

As a result, WLRK questioned Mr. Woghin regarding CA's failure to produce significant amounts of e-mail, and Mr. Woghin explained that the Company's policy was not to retain e-mail on its servers, keep back-up tapes, or have archive servers, and that all e-mail was deleted after thirty (30) days pursuant to CA's document retention policy.[149] According to Mr. Savarese, Mr. Woghin was adamant that there was no e-mail to be found due to CA's failure to retain e-mail on its servers, and its stringent document retention policy.[150] According to Mr. Woghin, due to this failure, he advised WLRK that it would have to search individual employees' computers for e-mail. However, the Company did not make any efforts to obtain e-mail from CA employees' computers, other than to request that employees search for and produce their own e-mail, because, in Mr. Woghin's view, WLRK did not suggest that they do so.

Despite the government's concern regarding CA's document collection and production efforts, particularly with respect to e-mail (and the representation made to the Board that all necessary steps would be taken), no immediate changes were made to the process by which documents were collected at CA. Into the spring of 2003, CA continued to collect and produce documents responsive to the SEC Document Request, the December Subpoena, and various additional requests.[151]

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149 According to several individuals interviewed by the SLC, Mr. Wang disliked e-mail, because he felt it hampered direct communication between sales people and clients.

150 Mr. Woghin gave the same explanations to S&C when it was first retained in the summer of 2003.

151 In a March 6, 2003 letter, the SEC requested that CA provide an update on the status of production with respect to Request No. 8 of the SEC Document Request, asking if CA had completed its production in response to this request, and if not, what documents were currently outstanding. *See* Letter from Danielle Friedman to John Savarese (Mar. 6, 2003). In a March 13 response, Mr. Savarese summarized his view of how CA had attempted to comply with the request and noted that additional documents relating to backdating had been discovered in an effort to comply with the USAO's December Subpoena. *See* Letter from John Savarese to Danielle Friedman (Mar. 13, 2003). Mr. Savarese explained that if, in the process

(b) *The April, June, and July 2003 Subpoenas*

In the spring of 2003, the government issued additional subpoenas to CA requesting all of CA's license agreements (some of which were covered by earlier requests) and related documents for particular fiscal quarters, which, when analyzed in their entirety, enabled the Audit Committee to conclude that the 35-Day Month practice existed at CA.

On April 14, 2003, the SEC issued a subpoena to CA (the "April 14 Subpoena") requesting, for the second, third, and fourth quarters of CA's fiscal year 2000 (July 1, 1999 to March 31, 2000), a spreadsheet "of contracts that composed the reported revenue for each requested quarter." SEC Subpoena, *In re Computer Assocs. Int'l, Inc.* (NY-7008) (Apr. 14, 2003). The SEC requested that the spreadsheet contain the following information for each contract listed: (i) the parties to the contract; (ii) the date the contract was signed by CA; (iii) the date the contract was signed by the customer; (iv) the sales agents involved in the contract negotiations; (v) the total amount of the contract; and (vi) the amount included as revenue in that quarter from the contract. This subpoena also requested that CA produce, among other things, the following documents for those quarters: (i) all contracts entered into by CA in the amount of $5,000,000 and above; and (ii) all correspondence and memoranda, including e-mail, faxes, and handwritten notes, concerning *all* contracts reported as revenue.

In a letter accompanying the April 14 Subpoena, the SEC requested "that before any documents are produced in response to [(i) and (ii) above], Computer Associates first produce all contract signature pages for each contract that was reported as revenue in each quarter." Letter from Danielle Friedman, Staff Attorney, U.S. Sec. and Exch. Comm'n, to John Savarese (Apr. 14, 2003) (emphasis in original). To respond to this subpoena, WLRK, as

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of complying with more recent document requests, CA uncovered any additional documents responsive to Request No. 8, those documents would be promptly produced.

specifically requested by the government, worked first on collecting and producing the contract signature pages, and then on creating the requested spreadsheet, before seeking the underlying documents from CA.

On May 28, 2003, WLRK produced to the SEC, on behalf of CA, the contract signature pages requested in the SEC's April 14 letter. Then, on June 17, 2003, WLRK produced the spreadsheet requested in the April 14 Subpoena, identifying the contracts recognized by CA in the second, third, and fourth quarters of fiscal year 2000. In a letter accompanying the June 17 production, WLRK stated, "CA has assumed the authenticity of documents maintained in the ordinary course of its business and the accuracy of the information in those business records." Letter from Warren Stern to Alexander Vasilescu (June 17, 2003). For example, WLRK told the government that it relied on the signature dates that appear on the faces of the contracts that exist in the Finance department's files, "[a]ccordingly, the information with respect to signature dates set forth in the spreadsheet should not be interpreted as a representation that the contract was actually signed on the dates indicated in the documents." Further, during this time, the Company continued to produce documents responsive to the December Subpoena, which were "recently located in the course of ongoing efforts to respond to government inquiries." Letter from John Savarese to David Pitofsky (June 13, 2003).

On June 27, 2003, the SEC issued another subpoena to CA, this time requesting the following documents for the second, third, and fourth quarters of CA's fiscal year 2000 and the first fiscal quarter of CA's fiscal year 2001 (April 1, 2001 to June 30, 2001) (the "June 27 Subpoena"): (i) all "forecast reports" issued by the GSO; (ii) all reports used by CA management and/or CA's sales force to track contract negotiations, and all documents related to those reports; (iii) documents that identify the departments and persons who created, distributed, and received the above-described reports; and (iv) organizational charts for various departments at CA. SEC Subpoena, *In re Computer Assocs. Int'l, Inc.* (NY-7008) (June 27, 2003). Following the issuance of this subpoena, Mr. Woghin, for the first time, began sending document collection memos to broad groups of CA employees, requesting that employees search their files for all documents related to the licensing agreements requested in the April and June Subpoenas and requiring them to respond in writing regarding the results of their efforts.

On July 17, 2003, the SEC issued a subpoena requesting documents related to all contracts, and related documents, recognized in the first quarter of CA's fiscal year 2000 (April 1, 2000 to June 30, 2000). *See* SEC Subpoena, *In re Computer Assocs. Int'l, Inc.* (NY-7008) (July 17, 2003) (the "July 17 Subpoena").[152] The SEC also requested that CA now "produce those documents previously identified in the subpoena dated April 14, 2003" – which, as indicated above, were the contracts for $5,000,000 or more and related correspondence (including e-mails and faxes). These documents, the SEC stated, "by agreement, ha[d] not yet been produced." Letter from Danielle Friedman to Warren Stern at 1 (July 17, 2003).

In connection with this production, the SEC specifically requested that CA "undertake a thorough search for responsive documents, particularly faxes, cover letters and e-mails that attach or reference partially executed contracts tendered by customers in responsive quarters." *Id.* Indeed, the SEC cited to the Company the recent decision in *Zubulake v. U.B.S. Warburg*, 217 F.R.D. 309 (S.D.N.Y. 2003), which outlined the efforts that broker-dealers must undertake with respect to producing e-mails and the possibility of recovering deleted e-mail,

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[152] The documents requested in this subpoena had not been requested in the April 14 Subpoena.

and stated that "the staff would appreciate a search being undertaken that is consistent with the persistence of the parties in *Zubulake*." *Id.* In addition, the SEC specifically instructed the Company to search its field offices, in addition to CA's Islandia headquarters, for responsive documents. *Id.*

As a result, CA searched sales files, work papers, and employees' files, and a team of CA employees was assigned to review the documents collected from CA's worldwide offices. This team included Finance and Sales Accounting department employees, and occurred primarily during July and August 2003. The team reportedly reviewed and organized the documents into boxes by fiscal quarter based on the review criteria, and "flagged," or specifically identified, any documents that raised potential revenue recognition issues to bring to the Legal department's attention. Mr. Kaplan, who was involved in this review process, kept a running list of the contracts for which there were documents suggesting issues, which was later produced to the government.

All former CA executives involved in the document collection and review process, including those that have pled guilty, emphatically denied that documents were ever intentionally destroyed, altered, or withheld from WLRK or the government.[153] Messrs. Kaplan and Rivard, who were involved in responding to the government's document requests early in the process and were in part responsible for the document review that occurred in the summer of 2003, candidly admitted their role in the 35-Day Month practice to the SLC, and credibly denied that any documents were withheld from counsel. This account was corroborated by Doug Robinson, the former head of CA's Internal Audit, Sales Accounting, and Investor

153 Mr. Kaplan specifically recalled being shown by the FBI documents that he had flagged during the review process, and he assumed that all flagged documents were turned over to the government as long as they were not privileged.

Relations departments, who was heavily involved in the document collection and offered the same account. These accounts are likewise corroborated by substantial contemporaneous e-mail traffic concerning the review. Ultimately, once the Company undertook to collect the relevant documents, they were turned over to WLRK, and when reviewed and analyzed, they evidenced the 35-Day Month.

Throughout July 2003, CA produced documents to the government responsive to the April, June, and July subpoenas, including Status Reports and Missing Reports for fiscal year 2000 and the first quarter of fiscal year 2001.[154] At the same time, the Audit Committee investigation was getting underway. Due to the concern expressed by the government regarding CA's document productions, as evidenced in the SEC's July 17 letter and expressed at the August 4 meeting, one of the Audit Committee's initial priorities was to understand the scope of CA's prior document collection and production efforts, and to remedy any deficiencies in those efforts going forward. *See* E-mails between Tracy High and Donald Watnick (Aug. 8, 2003); Memorandum from Tracy High to Donald Watnick (Aug. 12, 2003). During August and early September 2003, S&C began requesting information from the Company regarding its document collection efforts, interviewing CA employees regarding the document collection process, and gathering information regarding CA's back-up systems.

Beginning in mid-September, at S&C's insistence (and over the objection of Mr. Woghin), PwC began the process of imaging the hard drives of numerous CA employees and

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154 WLRK was first made aware of the Status Reports in April 2003 during its interviews of CA employees. The WLRK letter accompanying the production of the reports explains that, (i) Status Reports "were used by the CA sales force, finance department, and others to, among other things, track contracts," and (ii) Missing Reports "were prepared by the Financial Reporting department based upon information contained in the status reports." Letter from Louis Barash, WLRK, to Alexander Vasilescu at 2 (July 23, 2003).

examining CA's back-up tapes.[155] This was a multi-step process, in which PwC (i) interviewed legal and technical employees to better understand the structure of CA's information systems, (ii) assessed various computer systems utilized by CA to determine the location of relevant data; (iii) captured and recovered information from the computers and Blackberry devices of relevant CA employees, (iv) analyzed the recovered information, and (v) reported the results of this analysis to both WLRK and S&C. In total, at the direction of S&C, PwC examined 101 computers and Blackberry devices belonging to eighty-seven (89) CA employees.

In the end, the SLC found that the documents produced during the summer and fall of 2003 were not a "secret cache" hidden at the Company. Instead, the SLC found a document collection process that was flawed in many respects, which resulted in serious delays.[156] In retrospect, the SLC believes that the Company's document collection and production efforts could have been improved if the Company had acted earlier to (i) send document collection requests to broad groups of employees; (ii) search CA's worldwide sales offices; (iii) hire forensic specialists to locate and preserve electronic documents, particularly e-mail; and (iv) have its outside counsel coordinate and participate in the document collection efforts. This is particularly true after it became clear that the government believed that the Company's productions were deficient. Nonetheless, the myth that the 23 Boxes constituted a "hidden cache" that then became a "surprise delivery," is simply that, just a myth.

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155 At the outset of its investigation, S&C perceived resistance from Mr. Woghin to some of its suggestions, including the imaging of the computers of CA employees, and he also told S&C that he wanted to sit in on interviews of CA employees. Ultimately, S&C asked the Audit Committee to direct Mr. Woghin not to interfere with its investigation. This was done.

156 The question of whether the Company's document collection efforts were intentionally deficient has not been definitively answered. All of the CA executives involved in the document collection process interviewed by the SLC stated that it was not.

(c) *The Compilation of Documents Responsive to the April, June, and July 2003 Subpoenas*

During late August and early September 2003, after documents that had been collected by CA had been turned over to WLRK in several batches, WLRK reviewed and organized the documents. WLRK attorneys, at the request of the government, created color-coded folders and chronologies using the documents for each contract from fiscal year 2000, incorporating the Status and Missing Reports (produced to the government in July), e-mails, fax cover sheets, and cover letters. By mid-September 2003, WLRK attorneys had concluded that the chronologies, in conjunction with the spreadsheets produced in response to the April Subpoena, indicated that numerous contracts were executed by CA's customers after the quarter end in fiscal year 2000, but had been backdated and recognized as revenue by CA in the prior quarter.

Mr. Savarese then called Mr. Giuffra, and asked him to come to WLRK's offices, where the contract chronologies were reviewed with him.[157] Messrs. Savarese and Giuffra then called Mr. Schuetze and informed him that documents that the Company had recently provided to WLRK evidenced possible premature revenue recognition. Mr. Schuetze instructed the lawyers to "get to the bottom" of these issues, and immediately flew from Texas to New York to meet with counsel, spending a substantial amount of time in New York as the Audit Committee's investigation became more intense.

On September 19, 2003, CA continued to produce to the SEC and USAO documents responsive to the April 14, June 27, and July 17 Subpoenas, and made subsequent

157 As noted above, the September 24 Wall Street Journal article contained many inaccuracies. Most tellingly, there was no "surprise delivery" of "23 boxes" of "paperwork." As described above, the SLC believes that the documents at issue were collected from various CA offices and delivered over several months. After they were reviewed and organized, Mr. Savarese called Mr. Giuffra and presented him with the contract chronologies that WLRK had assembled.

productions on October 7 and 10, and November 3, 7, and 14, 2003.[158] WLRK's letter to the SEC, accompanying the October 7, 2003 production, referenced what the review had revealed, and states, "we want to call your attention to the fact that these productions contain a number of documents suggesting that certain license agreements were signed by customers *after* the quarter end, although the agreements themselves bear a quarter end signature date." Letter from John Savarese to Alexander Vasilescu at 2 (Oct. 7, 2003).

(d) *The SLC's Review of the Documents*

The SLC reviewed these documents as well, which include, among other things, e-mails regarding contract negotiations, various contract status reports, and copies of signed contracts. Following its review of these documents, the SLC came to the same conclusion that WLRK and S&C did – that the documents evidenced possible premature revenue recognition. The SLC did not find any "smoking gun" documents pointing to misconduct by CA's officers, such as Mr. Kumar, and found no documents discussing "backdating" or other criminal acts. In fact, Mr. Kumar's name was noticeably absent from these documents, and his name appeared primarily on innocuous e-mails in which he approved certain discounts or other contract terms proposed by sales personnel.

Instead, the SLC found that the documents, when analyzed together with (i) information regarding when CA recorded the revenue from certain contracts (which is not in the documents), and (ii) its prior knowledge about the fraud, implicated numerous lower level employees, and bore the fingerprints of executives actively involved in revenue recognition decisions at the quarter end, such as Messrs. Rivard and Silverstein. As a result, and as is discussed further below, the SLC believes that the Audit Committee took the most effective

158 As noted above, the documents that constitute the so-called "23 Boxes" were produced on September 19 and October 7, 2003.

action that it could given the knowledge that it had – it promptly requested and received the resignations of Messrs. Rivard and Silverstein, in addition to Mr. Zar, to whom they, and the entire Finance organization, reported. The next day, as discussed below, it then publicly disclosed the findings of the review, and the employment decisions it had made. Thus, the information contained in the "23 Boxes" was all publicly-available and known to the plaintiffs and their counsel, who, as discussed below, acknowledged the government investigation, but nonetheless determined to proceed with the settlement at the fairness hearing in early December.[159]

Indeed, the USAO reached a similar conclusion with respect to the contents of the 23 Boxes. In connection with its motion seeking a stay of discovery, the USAO observed that the "23 boxes . . . rendered no additional evidence of fraud beyond that which [the Wyly Movants] already had." Government's Reply in Support of Motion to Intervene and Stay Discovery at 7, *In re Computer Assocs. Class Action Sec. Litig.*, 02 Civ. 1226 (TCP) (E.D.N.Y. Nov. 7, 2005) (emphasis in original). The USAO based this observation on the fact that the "23 boxes' contents were in the public record far in advance of the settlement fairness hearing before this court." *Id.* The USAO then went on to compare the words of the Wyly Movants' brief to the words in the CA press release from August 8, 2003 to show that, almost three months before the settlement hearing, the Wyly Movants (and everyone) were in possession of the very information that the Wyly Movants now claim to be "newly discovered." *Id.* at 7-8. The USAO concluded, therefore, that "the notions that the Wyly Movants were 'ignorant' of the facts proved by the 23 boxes' contents, and that the boxes contents now evidence a 'fraud on the Court,' are simply preposterous." *Id.* at 8.

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159 Following the October 8 press release, discussed below, no plaintiff requested confirmatory discovery or to see any of the information that the Audit Committee developed in its investigation.

2. October-November 2003 – The Results of the Audit Committee Investigation

After CA's initial productions in response to the April, June, and July Subpoenas, the Audit Committee took a number of steps to understand the scope of the problem evidenced by the documents. ***First***, as noted above, the Audit Committee accelerated its on-going investigation by imaging CA employees' computers in order to recover additional documentary evidence relating to the timing of customer signatures and by conducting additional interviews of CA employees. By November 21, 2003, PwC had imaged the computers and hand-held devices of fifty-five (55) CA employees, including Messrs. Kumar, Zar, and Richards.[160] This effort produced voluminous amounts of e-mail that was previously thought not to exist. ***Second***, during the first week of October, the Audit Committee – along with S&C attorneys and representatives from PwC – interviewed sixteen (16) CA employees, including Messrs. Kumar (for the first time) and Zar.

As the Audit Committee "ratcheted up" its investigation, CA's senior managers met and discussed what their response to the investigation should be. Sometime in late September or early October 2003, Messrs. Kumar, Richards, Woghin, and Zar met in a conference room at a Manhattan law firm at which time they discussed how to coordinate their response to the Audit Committee investigation. At the meeting, which purportedly lasted approximately forty-five (45) minutes, the assembled group laid out the explanations they should give to the Audit Committee when questioned about the practice. According to Mr. Kumar, the group discussed "carefully chosen" words for the executives to use and agreed to

160 Ultimately, PwC imaged the computers and personal electronic devices of eighty-nine (89) CA employees.

rely on documents such as the "McWade Memo"[161] and the idea of an "administrative window." Mr. Woghin recalled this meeting, and that the executives engaged in general conversation about the government investigation, but denied that any specifics as to how to respond to the Audit Committee or the government were discussed.

Accordingly, at their interviews, which occurred on October 3 and 6 respectively, Messrs. Zar and Kumar[162] both denied the existence of the 35-Day Month practice. Mr. Zar gave several excuses in an attempt to explain away documents evidencing the 35-Day Month practice. Mr. Zar told the Audit Committee that CA followed the revenue recognition policies outlined in the McWade Memo. He asserted that some contracts may have been improperly accounted for in fiscal year 2000 because new employees from CA's then-recent acquisition of Platinum Technologies Inc. were unfamiliar with CA's policies or SOP 97-2, and that many of the problems resulted from "minor modifications" to contract paperwork post-signing. However, in the view of the Audit Committee and its counsel, Mr. Zar's answers raised questions and caused the Audit Committee to lose confidence in him. As a result, the Audit Committee determined to seek Mr. Zar's resignation, although the directors did not believe that they had evidence that he had personally engaged in fraud.

In his interview, Mr. Kumar – as he had in the past – denied any involvement in the Company's quarter-end activity and revenue recognition practices. He said that he generally avoided making "relationship calls" to clients late in the quarter, for fear that it would

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161 That memo, written by Mr. McWade and dated August 13, 1997, properly states that a "client must **sign** the license agreement . . . no later than the last date of the month in which revenue is being recognized, and it must be received by the controller no later than the FLASH date corresponding to the month in which revenue is being recognized." Memorandum from Charles McWade to Financial Controllers at 1 (Aug. 13, 1997) (bold and capitalization in original).

162 Messrs. Schuetze, Ranieri and D'Amato attended the interview of Mr. Kumar, and Mr. Schuetze attended the interview of Mr. Zar.

"tip off" the client that CA was desperate for the contract. Similarly, he told the Audit Committee that he did not supervise or participate in revenue recognition decisions, relying instead on Mr. Zar. When Mr. Schuetze asked Mr. Kumar directly whether he had been involved in, or had knowledge of, any backdating, Mr. Kumar denied any such involvement or knowledge. To the Audit Committee and its counsel, Mr. Kumar appeared to be credible.

In contrast, during S&C's interviews of various Sales Accounting and Finance department employees, the Audit Committee learned that mid- and lower-level employees had significant experience with backdating contracts and booking late contract revenue. The picture of the 35-Day Month that began to emerge from those interviews was that of a widespread, common knowledge practice that was embedded in the way CA did business.

Following the interviews (and a review of the evidence), at an October 7, 2003 CA Board Meeting, Mr. Schuetze reported to the Board that the Audit Committee had determined that CA had prematurely recognized revenue from "a number of software contracts" during fiscal year 2000. Minutes of a Meeting of the CA Board at 1 (Oct. 7, 2003). Mr. Schuetze told the Board that while the contracts were "genuine," it was "still [a] serious issue" which might require a restatement for fiscal year 2000. Notes of Scott Smith at 1 (Oct. 7, 2003). Mr. Kumar followed Mr. Schuetze's report by telling the Board that he had, pursuant to the Audit Committee's recommendation, sought, and expected to receive, the resignations of Messrs. Zar, Rivard, and Silverstein, all of whom had overseen sales accounting during the relevant period. Minutes of a Meeting of the CA Board at 1-2 (Oct. 7, 2003).[163] While the Board expressed dismay at this revelation, the directors also expressed a sense of relief that,

[163] These were the same three (3) individuals that the USAO had identified to WLRK as "subjects" of the government's investigation in June.

although revenue had been prematurely recognized, the revenue itself was real.[164] Nevertheless, the Board was "very quiet" after Mr. Schuetze spoke. "[T]here were ten seconds when no one knew what to say." As one Board member told the SLC, he was in a "state of shock" over the revelation.

At this point, neither S&C nor WLRK knew of, or presented, evidence of criminality by Messrs. Zar, Rivard, or Silverstein to the Audit Committee or the Board. Rather, the majority of directors interviewed understood that the executives were asked to resign because the accounting improprieties happened "on their watch," and because these individuals did not have credible explanations for what had occurred or for their conduct relating to revenue recognition. According to notes taken at this meeting, the directors asked several questions, including (i) whether the problem was limited to fiscal year 2000, and (ii) whether there were other members of management involved. Mr. Schuetze commented that, as of then, the Audit Committee had not uncovered a "pattern of activity," but that the Audit Committee's investigation was continuing and "they may find more." Notes of Scott Smith at 2 (Oct. 7, 2003).[165]

The next day, on October 8, 2003, the Company issued a press release announcing the preliminary results of the Audit Committee's investigation, and the resignations of Messrs. Zar, Rivard, and Silverstein. *See* Press Release, Computer Assocs. Int'l, Inc., Computer Associates Announces Preliminary Results of Board Inquiry (Oct. 8, 2003). The press release stated that:

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164 Mr. Cron told the SLC that the problem "was terrible," but that he was consoled somewhat by the fact that "it was not what the government said *plus more*; it was just what the government said."

165 No CA counsel, inside or outside, raised the issue of the settlement or the releases at this meeting, and the settlement was not discussed.

> The Audit Committee's investigation is continuing, but we have determined that CA recognized certain revenue prematurely in the fiscal year ending March 31, 2000. The committee found that a number of software contracts in that fiscal year appear to have been signed after the end of the quarter in which revenues associated with such contracts had been recognized. Those revenues should have been recognized in the quarter in which the contract was signed.

Id. The press release stated further that the Audit Committee "found no evidence that the revenues and cash flows associated with these contracts were not genuine." *Id.* As noted above, the SLC found that this press release accurately conveyed what the documents that had been collected demonstrated. The press release also reported that Mr. Kumar had asked for, and received, the resignations of "those who oversaw sales accounting during the relevant time," Messrs. Zar, Rivard, and Silverstein. *Id.*

The night before the press release was issued, Mr. Nachman, at the request of Mr. Woghin, called Richard Schiffrin, co-lead counsel for the plaintiffs in the Class Actions, to advise him of the impending release, and what the Audit Committee had uncovered, in an attempt to determine whether it would upset the settlement. Mr. Schiffrin told Mr. Nachman that the plaintiffs would proceed with the settlement notwithstanding what the Audit Committee had discovered and announced. Mr. Nachman did not report any of those discussions to the Board. Plaintiffs had until November 11, 2003 to opt out of the settlement, and on December 5, 2003, a fairness hearing was held in front of Judge Platt. As is discussed further below, plaintiffs took no steps to upset the settlement, but instead continued to advocate for it.

(a) *The October 14 Meeting with the Government*

On October 14, Messrs. Giuffra, Urowsky, Savarese, and Schuetze met with the government, in their first meeting since the October 8 announcement. Mr. Giuffra's talking points reflect that he expressed to the government that the Audit Committee, S&C, and WLRK had been working hard to cooperate in the government's investigation. Mr. Giuffra noted that he had spoken with Mr. Schuetze "almost daily," particularly in the previous three (3) weeks. He explained that, with the help of PwC, the Audit Committee and its counsel had reviewed more than three hundred (300) contracts, mostly from fiscal year 2000, and identified twenty-six (26) contracts that appeared to have been recognized in the wrong quarter. Mr. Giuffra provided the government with four volumes of contract chronologies, which included documents related to these twenty-six (26) contracts. *See* October 14, 2003 [Oral] Preliminary Report of the Audit Committee of CA on Certain Revenue Recognition Questions in the Fiscal Year Ended March 31, 2000, Volumes I-IV. In addition, Mr. Savarese reported to the government that the recent productions of documents were made to the government promptly after CA discovered them.

At the same time, Mr. Giuffra also "stress[ed]" that the Audit Committee's conclusions were still "preliminary" and that the Audit Committee was "not yet in [a] position to draw conclusion[s] as to how or why this happened." Giuffra Talking Points at 1, 7 (Oct. 14, 2003). He noted that while the Audit Committee had "determined that it had 'lost confidence'" in Messrs. Zar, Rivard, and Silverstein as a result of a combination of four factors:

> (1) the number of contracts appearing to have late customer signatures in F[iscal] Y[ear] 2000; (2) the lack of controls over decisions made by lower level sales accounting personnel relating to the period when contracts were booked; (3) the handling of post-quarter-end modifications to contracts w[ithout] establishment of clear, bright line rules; and (4) the need to maintain adequate documentation.

Id. at 3. Mr. Giuffra reported that the Audit Committee had not yet developed evidence that any of the three (3) were involved in intentional wrongdoing. Indeed, the Audit Committee had not determined that Messrs. Zar, Rivard,[166] and Silverstein "knew or should have known [that] contracts were signed by customers after q[uarter]-end," much less that any of the three had "violated securities laws . . . [or] knowingly violated GAAP." *Id.* at 10.

At this point in the fall of 2003, the scope of the fraud itself was also still unclear. As is indicated in a highlighted portion of Mr. Giuffra's talking points, at the time of the October 14 meeting, a "majority of contracts w[ith] customer signature issues appear[ed] to be in [the second quarter of fiscal year 2000, dated] September 30, 1999." *Id.* at 6 (emphasis in original). This evidence led the Audit Committee to consider (and to suggest to the government) a "possible explanation" that these contracts were incorrectly accounted for because of the "large Platinum acquisition" that had occurred several months earlier. *Id.*[167] Likewise, there was at least some evidence supporting Mr. Zar's rationale of allowing "minor modifications" to contracts that required only "ministerial changes" after the quarter close, although Mr. Giuffra recognized that "CA did not document [the] 'minor modification' process," casting doubt on the validity of the practice. *Id.* at 7.

In addition, Mr. Giuffra discussed two (2) memoranda regarding contract revenue recognition at CA distributed to CA employees in the late 1990s, the McWade Memo, which Mr. Giuffra used as an example of CA "policy," and a memo by Mr. Silverstein. In contrast to the McWade Memo, the Silverstein Memo, dated October 15, 1998, could be seen as counseling backdating. It stated that:

> [t]he effective date, signature dates and initial payment dates must all be in the month the business is to be recognized. If an error is made (i.e., the client dates his signature October 1, 1998 when the

166 Mr. Rivard declined to be interviewed by the Audit Committee.

167 The acquisition of Platinum caused "additional pressures on [the] CA Sales Accounting staff," because "a substantial number of Platinum employees did not remain for a transition period." *Id.*

> transaction is effective September 30, 1998), clean paperwork must be executed to correct this error. Cross outs and white out are not acceptable.

Memorandum from Lloyd Silverstein to CA Sales Employees at 2 (Oct. 15, 1998). Although Mr. Giuffra noted that the Silverstein memo "raises questions," he also explained that the Audit Committee was not able to question Mr. Silverstein after his resignation and thus could not obtain information regarding what Mr. Silverstein intended to convey. Giuffra Talking Points at 9 (Oct. 14, 2003).

Finally, Mr. Giuffra emphasized that there was "no evidence to suggest that revenues and cash flows associated with those contracts were not genuine." *Id.* at 3. According to Mr. Giuffra, this was part of an effort to lay the groundwork for a settlement and to distinguish the 35-Day Month practice from the frauds that had recently occurred at Enron and WorldCom.

(b) *The October 20 Board Dinner*

The evening before an October 21, 2003 Board meeting, the Board held a dinner, which several members of CA's senior management, including Stephen Richards, attended. According to Mr. Richards, he spoke with Mr. Kumar prior to the dinner and asked him to arrange an opportunity for him to speak with director Ranieri about his upcoming SEC testimony, and that Mr. Kumar did so. At the dinner, Mr. Richards recalls that he spoke privately with Mr. Ranieri and asserts that he told him that (i) he felt "uncomfortable" testifying before the SEC, and (ii) based on his counsel's advice, he was considering asserting his Fifth Amendment rights at the deposition. According to Messrs. Richards and Kumar (who joined the second half of the conversation) Mr. Ranieri told him that if Mr. Richards did not testify he would have to leave CA and that he, Mr. Ranieri, could not "protect" Mr. Richards if he was "outside the Company." According to Mr. Richards, Mr. Ranieri told him that the Company would continue to fight the government's allegations, and that CA would prevail in the end.

Mr. Ranieri did not specifically recall this conversation; however, Mr. Ranieri told the SLC that his "script" for such conversations was to tell CA employees that they should talk to the government and tell the truth. Mr. Ranieri told the SLC that he would assure such employees that if they cooperated with the government and had not done anything wrong, then the Company would support them and would not "leave them out to dry." With respect to the individuals who asserted their Fifth Amendment rights with the government and would not cooperate with the Audit Committee, the Audit Committee's position was that they had to leave the Company. Mr. Ranieri explained to the SLC that the Audit Committee's policy was enforced without exception. While Mr. Ranieri did not specifically recall his response to Mr. Richards, he believed that any conversation with Mr. Richards was consistent with other conversations he had with CA employees concerning the need to testify and cooperate.

While the record is unclear as to exactly what was said during this particular conversation, it appears that Mr. Richards conveyed to Mr. Ranieri that he felt uncomfortable testifying in front of the SEC. Under these circumstances, while the SLC does not believe that Mr. Richards' statements to Mr. Ranieri constituted a "red flag," it analyzed these statements as such for purposes of its investigation. The relevant facts are as follows: on the next day, October 21, the Audit Committee's counsel advised the Board that it intended to interview Mr. Richards. On October 22, 2003, S&C interviewed Mr. Richards in order to ascertain what, if anything, Mr. Richards knew about the 35-Day Month practice at CA. During his interview, Mr. Richards stated, among other things, that he understood CA's revenue recognition policy to require that customers sign contracts in the quarter in which the contract was booked. Mr.

Richards said that he had no reason to believe that CA improperly recognized revenue during fiscal years 1999 and 2000, and that he was not aware of any effort at CA to inflate revenue through backdating contracts. While it is now obvious that Mr. Richards was not telling the truth, the Audit Committee then had no facts to lead them to conclude that Mr. Richards was untruthful. Further, the next day, October 23, as discussed below, Mr. Richards testified before the SEC and did not assert his Fifth Amendment rights. Thus, the Audit Committee had no factual basis to believe that he testified falsely, and even if the earlier discussion with Mr. Ranieri was a red flag, he, and the other members of the Audit Committee, satisfied their duties to investigate.

(c) *The October 21, 2003 Board Meeting*

The Board, like the government, also questioned why the evidence of the 35-Day Month practice found in the documents had not been discovered earlier. In advance of an October 21 Board meeting, Mr. Woghin raised the issue with Mr. Savarese, who stated the question and answer as:

> why we didn't locate the "bad" email and fax traffic documents earlier. Simple answer is that they turned up in the course of collecting [documents] in response to the July 17, 2003 S.E.C. subpoena, and that we have brought these "bad" [documents] to the government's attention promptly after discovering them ourselves. There may well be more to this but I think that is a fair, preliminary answer.

E-mail from John Savarese to Steven Woghin (Oct. 14, 2003). Mr. Savarese also conveyed this view to the Board at the October 21 Board meeting. Mr. Savarese informed the Board that the documents were "produced in mid-September 2003 in response to an SEC request in mid-July 2003." Savarese Talking Points at 2 (Oct. 21, 2003).

According to his talking points, Mr. Savarese informed the Board further that possible elements of a resolution with the government could include, among other things, a deferred prosecution agreement, an SEC consent decree, "disgorgement" by the CEO and CFO under Sarbanes-Oxley § 304, and "civil lawsuits."

The Board also received an update on the Audit Committee investigation. According to Mr. Giuffra's talking points, he updated the Board regarding: (i) the interviews conducted and documents reviewed by the Audit Committee; (ii) the Audit Committee's meeting with the SEC and USAO on October 14; and (iii) the next steps in the investigation. Mr. Giuffra reported that the Audit Committee had identified twenty-six (26) contracts to the government that appeared to have been signed after the end of a fiscal quarter, but were recognized in the prior quarter. Mr. Giuffra also stated that there were likely a "large number" of additional contracts signed after the quarter end.[168] The Audit Committee reported that its immediate focus was to determine the impact of the fraud on CA's prior financial statements, and whether CA needed to issue a restatement, and then to determine who was responsible.

With respect to document production, Mr. Giuffra told the Board that the government "wanted to know about production of doc[uments] and subpoena compliance," but that Mr. Savarese had provided the government with a "factual report" that "did [an] effective job" of explaining that the Company had complied with all of the SEC's subpoenas. Giuffra Talking Points at 6 (Oct. 21, 2003); Notes of Scott Smith at 5 (Oct. 21, 2003). Counsel did not raise the issue of the settlement and the releases at this meeting and the Board did not discuss it.

The independent directors met separately after the October 21 Board meeting, with Mr. Schuetze reporting on the Audit Committee investigation. Mr. Schuetze told the other

168 Mr. Giuffra stressed in his talking points that he did not "want to suggest that all contracts w[ith] typed-in quarter-end date[s] were signed after quarter-end," and explained that the review had "confirmed extensive use of typed-in quarter end dates," but that "on some occasions," the evidence indicated that "sales representatives would go back to customers and obtain contracts w[ith] signatures as of quarter-end." *See* Giuffra Talking Points at 2-3 (Oct. 21, 2003).

directors that he had informed the government about the Audit Committee's preliminary findings, the resignations of the three (3) CA executives, and that a restatement was a real possibility. The directors discussed how a restatement might affect senior management bonuses, as notes from the meeting indicate: "only year end effects it, SOX 304 to be considered, other board action for management generally." Notes of Scott Smith from Independent Director Meeting at 2 (Oct. 21, 2003). Mr. Fernandes (who joined the Board in May 2003) raised the question of how it could be that the Board did not know about the revenue recognition issues earlier, given the involvement of WLRK since February 2002. *Id.* Mr. Schuetze responded that the Board and WLRK had consistently been assured by management that CA had properly accounted for contract revenue, and the problem had not been found until they collected documents in response to the July 2003 subpoena, and analyzed them in September 2003. *See id.*[169]

(d) *Mr. Kumar's Compensation Review*

On October 10, 2003, The New York Times published an article by Floyd Norris entitled, "His Bonus was Based on Inflated Profits: Will He Give it Back?" The article questioned whether Mr. Kumar should return the incentive-based compensation that he received during the time CA had improperly recognized revenue. *See* Floyd Norris, *His Bonus was*

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169 The Company and its counsel were contemplating the civil settlement in late October. At the time, CA developed public relations materials to be used upon the approval of the settlement. On October 21, 2003, the same day that the Board met, WLRK provided comments to Mr. Woghin on a "Q&A" regarding the settlement. Warren Stern, a WLRK partner assisting Mr. Savarese, wrote:

> You should anticipate a question as to whether the settlement, if approved, would preclude claims against directors and officers arising from the matters under investigation by the A[udit] C[ommittee] and the government. Answer, "we are not prepared to speculate as to all of the effects of the settlement on claims that have not been asserted, but it could."

E-mail from Warren Stern to Steven Woghin (Oct. 21, 2003). There is no indication that the Board reviewed this e-mail or the Q&A, or that anyone raised the issue of the impact of the releases to the Board at this time.

Based on Inflated Profits: Will He Give it Back?, N.Y. Times, October 10, 2003, at C1. That day, Mr. Schuetze requested, by e-mail, that Mr. Kumar provide the Audit Committee with a detailed analysis of his compensation for fiscal years 1999 through 2002. E-mail from Sanjay Kumar to Walter Schuetze (Oct. 10, 2003). Mr. Kumar provided the Audit Committee with the proxy statements for each year at issue, and retained Towers Perrin, an employee-benefits consultant, (i) to provide an additional analysis of his compensation under CA's 1994 Annual Incentive Compensation Plan, and (ii) to explain the possible effects inter-quarter movements of revenue might have had on his compensation under that plan. *See* Report by Towers Perrin at 1 (Oct. 17, 2003).

At the October 21 CA Board Meeting, Mr. Kumar "presented an analysis, requested by Mr. Schuetze, concerning the incentive compensation paid to" him in fiscal years 1999 and 2000. *See* Minutes of a Meeting of the CA Board at 4 (Oct. 21, 2003). The Towers Perrin report concluded that inter-quarter movement of revenue likely did not have an impact on Mr. Kumar's compensation under CA's 1994 Compensation Plan. Report by Towers Perrin (Oct. 17, 2003). The report reasoned that, because "the Compensation Committee exercised its discretion to reduce the plan awards by forty-six percent (46%) in FY99 and twenty-five percent (25%) in FY00," the issue was almost a "moot point." *Id.* "[R]evenues would had to have been $741.9 million lower in FY00 before Mr. Kumar's calculated award would have been lower than his actual award." *Id.*

(e) *The Continuation of the Audit Committee's Investigation*

At the same time, the Audit Committee's investigation continued, as it conducted eleven (11) new interviews in the last twelve (12) days of October, including an interview with Mr. Richards the evening before his SEC testimony, as noted above. While acknowledging that he did not give S&C the "full picture," Mr. Richards believes he answered S&C's questions literally and truthfully.

On October 23, 2003 Mr. Richards testified in front of the SEC and perjured himself in three (3) material ways. First, Mr. Richards denied knowing that revenue from contracts finalized after the close of a quarter was improperly recognized in the prior quarter, and stated that he assumed CA's Finance and Sales departments would ensure compliance with revenue recognition requirements. *See* Kumar/Richards Superseding Indictment ¶ 70. Although he admitted to pressuring Sales managers to finalize license agreements after the ends of quarters, he claimed that he did so only because these sales managers had not reached their sales quotas, and not so as to allow revenue from these contracts to be recognized in the prior quarters. *Id.* ¶ 69. As discussed above, these statements were unquestionably false, as Mr. Richards subsequently admitted to knowingly participating in the 35-Day Month practice. *See* Kumar/Richards Plea at 79-80. Second, when he was asked to explain the use of pre-printed signature dates on contracts, Mr. Richards asserted that the practice was "[f]rankly, a very, very subtle sales tool," used to "remind" a client of its "commitment to complete a transaction in a certain time frame." *See* Kumar/Richards Superseding Indictment ¶ 89. In truth, as discussed above, the practice was used to allow late-arriving contract revenue to be booked in the prior quarter, and Mr. Richards admitted this in his guilty plea. Third, Mr. Richards told the SEC that he was never involved in discussions with anyone at CA, including Mr. Kumar, regarding whether CA was going to be able to reach Wall Street's estimates, and that in fact, he was unaware of CA's performance until such information was made public in a press release. *See id.* Again, as discussed above, this was also false; Messrs. Wang, Kumar, Richards, and Zar often met at the end of a quarter to discuss CA's prospects for meeting Wall Street's estimates and how many backdated contracts would be needed to do so. *See* Kumar/Richards Plea at 80-82.

(f) *The November Meetings with the Government*

On November 3, 2003, S&C met with the government to present an update on the Audit Committee's investigation. S&C provided additional documentary evidence of backdated contracts to the government, and discussed the continuing nature of the investigation. With respect to Mr. Kumar, S&C reported to the government that the Audit Committee was interested to know if the government was aware of any evidence of wrongdoing by Mr. Kumar, and stated that it stood ready to meet with the government with or without counsel to receive such evidence. The government declined this request for information.

S&C met with the government again on November 24, 2003. Mr. Giuffra (i) told the government that the Audit Committee was working with PwC to determine the necessity and/or size of any required restatement of CA's financials (and whether to restate for both backdated contracts and untimely or non-existent CA countersignatures), and (ii) discussed the status of two (2) CA employees: Messrs. Kumar and McElroy. S&C told the government that the Audit Committee had no information implicating Mr. Kumar in any wrongdoing, and repeated his statements that either Messrs. Schuetze or Ranieri would like to meet with the government, with or without counsel, to hear the government's evidence against Mr. Kumar. However, the government declined to have such a meeting. Indeed, despite this (and other) requests, at no point did the government ever share its evidence against Mr. Kumar with the Audit Committee. With respect to Mr. McElroy, Mr. Giuffra added that the Audit Committee appreciated the government's decision to inform it that Mr. McElroy had asserted his Fifth Amendment rights, and had scheduled a second interview with him based on this information.

G. ***December 2003 – The Settlement is Finalized***

The Board met again on December 3, 2003. At that time, WLRK reported to the Board that: (i) David Kaplan and Gayle Kemper had been terminated from CA because they refused to be interviewed by the Audit Committee; (ii) Mr. McElroy had asserted his Fifth Amendment rights during an interview with the SEC; (iii) the Audit Committee was still not aware of any evidence implicating Mr. Kumar; (iv) the Audit Committee was now investigating charges of obstruction; and (v) the government wanted to interview Mr. Woghin.

With respect to Mr. Kumar, Mr. Savarese reported to the Board that he was not aware of any evidence linking Mr. Kumar to the 35-Day Month practice. Mr. Giuffra also reported that he had explained to the government that the Audit Committee had no evidence of Mr. Kumar's involvement, and that he had asked the government to share any evidence that the government had. Mr. Giuffra told the Board that the government did not respond to this request, but also "did not say, for example, [the Audit Committee] should look harder for evidence of wrongdoing." Giuffra Talking Points at 4 (Dec. 3, 2003). Mr. Giuffra also told the Board that the Audit Committee would "look into" the questions the government had "raised . . . about CA doc[ument] production, including regarding e-mail production," but pointed out that "WLRK ha[d] provided good explanations" for why the documents were not produced earlier. *Id.* at 7; *see* Notes of Scott Smith at 2 (Dec. 3, 2003).

On December 5, 2003**,** a fairness hearing was held regarding the settlement,[170] at which Melvyn Weiss, lead counsel for the plaintiffs in the Class Actions stated:

> As we are all aware, *there is a criminal investigation that is ongoing, and I just wanted the Court to understand, as we have*

170 November 10, 2003 was the deadline for shareholders to opt out, and November 18, 2003 was the deadline to file written objections. There were 644,000 notices sent to class members, with less than 500 opt-outs and two objections, which were ultimately withdrawn. *Id.*

> *stated in our papers, that we've took all of that into account in coming to the conclusions we did as to what would be a fair, reasonable and adequate settlement for the class members.*

Transcript of Record at 3, *In re Computer Assocs. Class Action Sec. Litig.,* No. 98 Civ. 4839 (TCP) (E.D.N.Y. Dec. 5, 2003) (emphasis added).

Mr. Nachman appeared on behalf of the Company in the Class Actions and stated:

> I think it . . . bears repeating, this settlement does not resolve or affect any potential regulatory criminal or other action that may arise from the previously announced investigations by the SEC and Department of Justice into the company's past financial statements and accounting practices. . . . I wanted to add in connection with this settlement, as the Court knows, no assurances have been provided concerning the possible outcomes of the SEC and Justice Department investigations, nor have any assurances been provided that the audit committee will not recommend additional actions beyond the ones already taken.

Id. at 20-21.[171]

Further, with regard to the Board's approval of the settlement, Mr. Nachman stated:

> the non-defendant directors currently on the board of CA who had to consider the settlement and particularly the settlement of the derivative suit were in turn advised by yet another independent counsel in connection with their deliberations . . . so that one of the things especially in this day and age that we all wanted to ensure, and I think all parties were sensitive to, is that the entry into the settlements was not only appropriate on the substance in terms of amounts and so on, but the process by which we got here was appropriate, transparent and a proper one, and I think we're all very comfortable with that and feel that that's been done.

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171 Mr. Weiss also acknowledged the government investigation in his declaration, filed on December 1, 2003 supporting the final approval of the class action settlement: "In February 2002, the SEC and Department of Justice announced separate investigations of CA and its accounting practices. The government is still pursuing these investigations and has not provided information or assistance to plaintiffs." *In re Computer Assocs. Class Action Sec. Litig.*, No. 98-CV-4839 (TCP), *In re Computer Assocs. 2002 Class Action Sec. Litig.*, No. 02-CV-1226 (TCP) at 32, n. 9.

Id. at 23. Mr. Woghin attended the hearing as counsel to the Company in the 2003 Derivative Action, but did not make any statements on the record. The Court issued orders approving the settlement on December 8, 2003, and entered those Orders on December 10 and 11. Order and Final Judgment With Respect to CA Defendants, *In re Computer Assocs. Class Action Sec. Litig.*, No. 98 Civ. 4839 (TCP) (E.D.N.Y. Dec. 8, 2003); Order and Final Judgment With Respect to CA Defendants, *Federman v. Artzt,* No. 03 Civ. 4199 (TCP) (E.D.N.Y. Dec. 8, 2003).

Following the approval of the settlement, during the late December 2003 and January 2004 timeframe, as discussed at the December 3, 2003 Board meeting, the Audit Committee took additional steps to investigate the obstruction of the government investigation. The Audit Committee conducted more than fifteen (15) additional interviews in which, among other things, it questioned CA employees about the Company's response to the government investigation. Specifically, the Audit Committee asked detailed questions about (i) CA's document collection and review processes, and whether CA employees had destroyed or altered documents in order to conceal the 35-Day Month practice from the government; (ii) the interviews previously conducted by WLRK, and whether CA employees had deliberately misled WLRK; and (iii) whether CA employees discussed the government investigation and the interviews conducted by WLRK and S&C with CA senior managers.

H. ***2004 – The Guilty Pleas***

January-February. Throughout 2003, the Board had not been provided with any evidence directly implicating the Company's most senior executives in revenue recognition fraud. However, that changed beginning with Lloyd Silverstein's guilty plea on January 22, 2004. Mr. Silverstein pled guilty to one count of obstruction of justice, and told the Court during his allocution that he participated in the 35-Day Month practice and then covered it up.

See Silverstein Plea Tr. at 20. Mr. Silverstein admitted that, in 2002, he "was told by a CA executive" – Mr. Kaplan – "not to discuss the Company's end-of-quarter practice with the outside lawyers. When I met with the outside lawyers, I did not do so." *Id.*. Mr. Silverstein also told the Court that, when he was asked to speak to the government directly, "[s]everal CA executives" – later identified to the SLC as Messrs. Zar and Woghin – told him "not to disclose the practice. When I was interviewed by the government in September, 2002, I did not do so." Silverstein Plea Tr. at 20.

After Mr. Silverstein pled guilty, the Board again considered whether Mr. Kumar had been involved in the 35-Day Month practice or the cover up. One week earlier, on January 14, 2004, the Audit Committee interviewed Mr. Kumar, and, during that interview, Mr. Kumar again denied all knowledge of the 35-Day Month practice. On the day of Mr. Silverstein's guilty plea, the Audit Committee conducted a telephonic interview of Mr. Kumar, who explained that he had little contact with Mr. Silverstein, and had no knowledge of the conspiracy to obstruct justice. When the Audit Committee relayed Mr. Kumar's account to the government during a January 28, 2004 meeting, the government responded by stating that the Audit Committee should continue looking for evidence against Mr. Kumar. The government also told Mr. Schuetze that he had his "head in the sand" with regard to Mr. Kumar, and that the government would not settle with the Company while Mr. Kumar remained CEO, but nonetheless continued to refuse to share any evidence that it might have had that implicated Mr. Kumar in the 35-Day Month practice. Mr. Giuffra then presented to the government the evidence that the Audit Committee had uncovered concerning the widespread wrongdoing at CA, and the involvement of many of its employees.

Later that day, the Board met without counsel in a meeting called by Mr. Kumar. At this meeting, Mr. Fernandes engaged Mr. Kumar in a "one-on-one . . . interrogation," while the rest of the Board observed. After the session, Mr. Fernandes was convinced that Mr. Kumar should leave the Company. However, a majority of the Board disagreed, as even Mr. Fernandes felt that, at this time, there was no "smoking gun" that implicated Mr. Kumar in wrongdoing. Mr. Kumar told the SLC that he also met privately with Mr. Fernandes around this time in Mr. Fernandes' office in Dallas, Texas. At this meeting, Mr. Kumar tried to convince Mr. Fernandes that (i) he did not implement the new business model to conceal the fraud, (ii) the fraud was allowed to occur because CA's controls were weak, not because he condoned or participated in it, and (iii) once CA's revenue numbers were "put back" in the proper quarters and calculated with the reserves, the effect of the fraud on the Company's numbers would be immaterial.

On February 1, 2004, "Super Bowl Sunday," the Board met at CA headquarters for eight (8) hours to consider the evidence of Mr. Kumar's knowledge of, and involvement in, the 35-Day Month practice and the obstruction of justice. First, Walter Schuetze provided the Board with an update on the status of the Audit Committee's investigation, including the work being done to determine whether CA needed to issue a restatement. Second, Mr. Schuetze reported that, with respect to Mr. Kumar, the Audit Committee had interviewed him three (3) times and found that he had credible answers as to why he did not know about the 35-Day Month practice. Third, Mr. Schuetze related the "head in the sand" comment made to him at the January 28 meeting with the government, and stated that the government continued to decline to provide him with any evidence of wrongdoing by Mr. Kumar. Finally, Mr. Schuetze reported that the government took the position that it would not settle with the Company until Mr. Kumar was removed from the CEO position.

The Board then heard a twenty to thirty-minute presentation from Messrs. Giuffra and Savarese, who made the government's case against Mr. Kumar. According to WLRK, much of the evidence presented by counsel – which related to several contracts in which Mr. Kumar played a role that were ultimately found to have been backdated, and other comments reportedly made by Mr. Kumar about "needing" more contracts to close in the early days of a quarter – was discovered by the Audit Committee in the days between the January 20 and February 1 Board meetings. Messrs. Giuffra and Savarese also raised several mitigating factors including that (i) there was no direct evidence linking Mr. Kumar to the fraud, (ii) Mr. Kumar's e-mails generally indicated that he was cooperative during the government investigation, (iii) Mr. Kumar took several steps to implement the gold standard of corporate governance at CA, and (iv) one of the primary sales executives who had implicated Mr. Kumar was terminated by CA and had "an axe to grind."

After the presentations, the lawyers from WLRK and S&C left the room and Mr. Kumar answered questions from several different directors, including Messrs. D'Amato, Cron, Lorsch, Fernandes, and Schuetze. The Board questioned Mr. Kumar as to how he could have been the "hands on" COO, and then CEO, he was reported to have been and not have known about the 35-Day Month practice. Mr. Kumar responded that (i) he had only worked in research and development before becoming COO, and had no experience in sales or finance, and (ii) he was told directly by Messrs. Wang and Schwartz that contracts signed after the quarter end were reserved for, and that he did not know that the reserve had ended until May 2003. The directors then asked several pointed questions of Mr. Kumar, including, among others, (i) "were you ever aware of backdating contracts," (ii) "did you direct anyone to book [a contract] one way or another," and (iii) "who will come forward and say that Sanjay Kumar did direct [the practice]." Notes of Scott Smith at 15-20 (Feb. 1, 2004). Mr. Kumar maintained that he did not participate in, or have knowledge of, the 35-Day Month practice.

Following the directors' questioning, the lawyers from WLRK and S&C rejoined the meeting. The directors asked further questions of the lawyers regarding both the evidence against Mr. Kumar and their fiduciary duties as directors. After extended debate, the Board took no action against Mr. Kumar, pointing to the facts that: (i) there was no evidence directly pointing to Mr. Kumar; (ii) Mr. Kumar was a valuable asset to the Company, (iii) Mr. Kumar had been responsible for the new business model and other positive corporate governance actions, and (iv) it was "inconceivable" to some that he had taken part in any wrongdoing. Moreover, none of the senior executives who had left the Company, such as Mr. Zar, had pointed a finger at Mr. Kumar, which the Board viewed as supporting Mr. Kumar's position.

The Audit Committee investigation continued throughout February, with counsel interviewing fourteen (14) additional CA executives and employees, including Charles Wang, who denied any knowledge of the 35-Day Month practice and indicated that Mr. Kumar ran the business side of CA.

March-June. On March 10, 2004, Mr. Kumar met with Mr. Schuetze in San Antonio, Texas. According to Mr. Kumar, Mr. Schuetze asked him directly about the 35-Day Month practice. Mr. Kumar said that he explained to Mr. Schuetze why, in his view, the 35-Day Month practice was "not a problem." Mr. Kumar said that, during the discussion with Mr. Schuetze, he "minimized the number of late deals" that had been completed by CA. Mr. Kumar told Mr. Schuetze that if he were to recalculate CA's numbers properly, taking into account CA's reserves, it would show that the impact of the practice was not material. At no time did Mr. Kumar disclose his knowledge of or participation in the 35-Day Month practice.

At a March 12, 2004 CA Board meeting, the Board discussed succession planning for CA's senior management, including the CEO, CFO, COO, General Counsel, and Chief Compliance Officer positions. During the executive session, CA's independent directors again discussed the evidence that had been presented to them at the February 1 meeting, and debated the best course of action to take with respect to Mr. Kumar. The directors discussed the difficulty the Company would have putting a new management team in place without Mr. Kumar's assistance, and determined that the Company must act quickly to fill vacant positions.

As a cooperating witness, Mr. Silverstein's guilty plea precipitated further guilty pleas by senior CA executives. As described above, on April 8, 2004, Messrs. Kaplan, Rivard, and Zar all pled guilty to charges relating to their involvement in the 35-Day Month practice, and the resulting obstruction of justice. That same day, Mr. Woghin, whose name was disclosed in public documents related to Mr. Zar's criminal proceeding, was fired at the direction of the Audit Committee.

At the same time, documentary evidence was discovered which began to directly implicate Mr. Kumar in the 35-Day Month practice. The Audit Committee recovered a laptop computer used by a former CA Sales executive that contained multiple post-quarter-close congratulatory e-mails from Mr. Kumar regarding deals finalized shortly after the quarter close. For example, on April 6, 2000, several days after the quarter close, the Sales executive sent an e-mail to Messrs. Kumar and Richards stating that he was having trouble closing a deal and stating:

> If we could get someone to ask [the customer] to "do us a favor" and sign the contract, leaving the date block blank (they technically can't backdate the signature block, even though the contract says an effective date of 3/31/00 . . . the new company wasn't technically formed until 4/1/00). I'll take care of fixing any mistakes that [the customer] inadvertently leave[s] off the fax contract.

E-mail from CA Sales executive to Stephen Richards and Sanjay Kumar (Apr. 6, 2000). The Sales executive then sent an e-mail the next day to Messrs. Kumar and Richards saying that "[t]he Eagle has landed . . . $11.9M GAAP . . . $19.7M lifecycle . . . contract addendum and P.O. . . . I'm taking my kids shopping tomorrow – on you!" E-mail from CA Sales Executive to Stephen Richards and Sanjay Kumar (Apr. 7, 2000). Mr. Kumar responded that "[s]hopping is on me." E-mail from Sanjay Kumar to CA Sales Executive and Stephen Richards (Apr. 8, 2000). In an April 6, 2004 interview with the Audit Committee, Mr. Kumar once again reaffirmed his prior false statements that he had no knowledge of the 35-Day Month practice, and added that he had believed that the late executed contract reserve prevented any premature recognition of revenue.[172]

On April 14, 2004, Mr. Schuetze, along with S&C, again met with the government. At this meeting, Mr. Schuetze informed the government that CA was prepared to restate its financial statements for fiscal year 2000 and the first two quarters of fiscal year 2001. Mr. Schuetze described for the government the work that went into preparing the restatement, and the involvement of counsel, PwC, and KPMG in those efforts. Mr. Schuetze also told the government that the Company was in the process of determining what additional personnel decisions needed to be made.

172 On April 16, 2004, at Mr. Schuetze's request, Mr. Giuffra circulated these e-mails and S&C's summary of Mr. Kumar's interview to the entire Board.

In mid-April 2004, approximately one week before an April 20 Board meeting, Mr. Kumar again met with Mr. Schuetze, this time in New York, in order to make a pitch on his own behalf. According to Mr. Kumar, he met with Mr. Schuetze because he knew Mr. Schuetze's support was critical to his continued employment at CA and he had heard that Mr. Schuetze had begun to advocate for Mr. Kumar to leave the Company. At this meeting, Mr. Kumar again lied to Mr. Schuetze by denying all involvement in the 35-Day Month Practice.

On April 20, the Board met again to discuss Mr. Kumar. At this meeting, S&C gave an extensive presentation regarding the evidence that had been compiled against Mr. Kumar. ***First***, Mr. Zar's criminal information and guilty plea was reviewed with the Board, and the Board was told that the individual referred to as "Executive One" in the Information had been identified as Mr. Kumar, and that "Executive One" was described as having directed and participated in the 35-Day Month practice. The Board was told that, based on Mr. Zar's plea, the government's case against Mr. Kumar was "no longer circumstantial," and that the USAO had used the terms "Executive One" and "Executive Two" intentionally in order to assist the Board with making personnel decisions.

Second, the Board reviewed the e-mails, described above, that explicitly referenced backdating and a backdated deal. The Board was told that the AUSA leading the investigation had said that he "could not imagine a stronger smoking gun," than these e-mails. In his defense, Mr. Kumar told the Board, as he had told the Audit Committee in his April 6 interview, that he did not recall receiving the e-mails, and that it was likely he never read them.

Third, the Board reviewed the evidence regarding Mr. Kumar's involvement with the $180 million undated EDS license agreement finalized in January 2000, which was recognized in the December 1999 quarter.

Fourth, the Board heard a presentation on the legal obligations of directors with respect to selecting a CEO, reviewed the steps the Audit Committee had taken to date and the results of its investigation, and heard the pros and cons of keeping or removing Mr. Kumar from his position.

Mr. Kumar's counsel then gave a presentation on behalf of Mr. Kumar. Mr. Kumar's counsel: (i) reiterated Mr. Kumar's position that he believed that a reserve was in place to account for late signed contracts; (ii) pointed out that there was nothing in the criminal informations filed against Messrs. Kaplan and Rivard implicating Mr. Kumar, leaving Mr. Zar as the only witness against Mr. Kumar (discussed below); (iii) presented defenses for the e-mails described above that explicitly referenced backdating and a backdated deal; and (iv) concluded that the government does not have enough evidence to make a criminal case against Mr. Kumar.

By this time, certain members of the Board, including Messrs. Schuetze and Lorsch had become "fed up" with Mr. Kumar, joining Mr. Fernandes in believing that Mr. Kumar had to be removed as CEO. Mr. D'Amato felt that the Board no longer had the "luxury of more time" to obtain definitive proof and had to act on the facts before it. Yet, certain members of the Board, particularly Alex Vieux, vehemently maintained that it was in the shareholders' best interest to have Mr. Kumar lead the Company unless and until there was more solid proof that Mr. Kumar was involved in the improprieties and a highly qualified executive was immediately available to replace him.[173]

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173 Mr. Vieux told the SLC that CA had a two-day business meeting in Washington D.C. sometime in March 2004, during which Mr. D'Amato met with Mr. Vieux and told him that the Board wanted to oust Mr. Kumar. Mr. Vieux said that the Board still needed Mr. Kumar to run the Company, and that to get rid of Mr. Kumar would be "precipitous."

Ultimately, the Board determined to demote Mr. Kumar from CEO to the position of "Chief Software Architect," and remove him from the Board. As Mr. Ranieri explained to the government the following day, Mr. Kumar would play an "advisory role" and Mr. Kumar was "simply to be a resource during the transition" while the Board conducted a search for a new CEO. Ranieri Talking Points (drafted by S&C) (April 20, 2004). Mr. Kumar was not to exercise any executive control, and play no role in accounting, financial reporting, revenue recognition, or sales. *Id.* At this point, the Board was reluctant to let Mr. Kumar go completely, since the CA World sales conference was upcoming, and, in their view, no one else "spoke the CA language with customers." Indeed, the Board feared that without Mr. Kumar, the Company would appear to be in a state of disarray in front of its entire customer base.[174]

On June 4, 2004, after CA World, the Board requested and received Mr. Kumar's resignation.

X. APPLICABLE LAW AND ANALYSIS OF THE CLAIMS

A. *Count One: Violation of The Public Company Accounting Reform and Investor Protection Act of 2002 ("Sarbanes-Oxley"), 15 U.S.C. § 7243*

Count one of the 2005 Derivative Complaint seeks disgorgement, under § 304 of Sarbanes-Oxley, of any bonuses, incentive compensation and/or profits from stock sales received by Messrs. Kumar, Schwartz, Wang, and Zar – all former CA CEOs and CFOs – from March 31, 1998 through March 31, 2002.[175] As described above, the SLC has determined that

174 According to Mr. Kumar, he met with certain members of the Board, including Messrs. Artzt, Ranieri, D'Amato, and Vieux, at S&C's midtown offices following the Board meeting. Mr. Kumar recalls being told he was being demoted, but assured that the Company would settle the government investigation and then bring him back as CEO in six months time. The directors identified by Mr. Kumar dispute his recollection of these events, and recall a more general conversation, such as "if you are cleared," we may bring you back.

175 *See* 2005 Compl. ¶¶ 251-62. As discussed above, Mr. Wang was CEO from June 1976 until August 4, 2000; Mr. Kumar was CEO from August 4, 2000 until April 20, 2004; Mr. Schwartz was CFO from 1985

the Company has valid claims, under different theories, against all four (4) of these former CA CEOs and CFOs (and has determined to settle with Messrs. Kumar and Zar). However, for the reasons stated below, the SLC concludes that there is no legal merit to this particular claim, and that this claim should be dismissed.

Section 304 provides:

> if an issuer is required to prepare an accounting restatement due to the material noncompliance of the issuer, as a result of misconduct, with any financial reporting requirement under the securities laws, the chief executive officer and chief financial officer of the issuer shall reimburse the issuer for –
>
> (1) any bonus or other incentive-based or equity-based compensation received by that person from the issuer during the 12-month period following the first public issuance or filing with the Commission (whichever first occurs) of the financial document embodying such financial reporting requirement; and
>
> (2) any profits realized from the sale of securities of the issuer during that 12-month period.

15 U.S.C. § 7243. To obtain reimbursement from a CEO or CFO under § 304, it must be shown that (1) the issuer has restated its financial statements; (2) the restatements were required because of a "material noncompliance . . . with any financial reporting requirement under the securities laws"; and (3) the material noncompliance was the "result of misconduct." *Id.; see also* Harold S. Bloomenthal, Sarbanes-Oxley Act in Perspective § 10.5 (2006-2007 ed.). All three elements are plainly evident in this case.

However, while the plain language of § 304 appears to support a disgorgement claim in this case, "[e]very court that has considered the issue directly has concluded that § 304 contains no implied private right of action." *In re Digimarc Corp. Derivative Litig.*, 2006 WL

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until June 22, 1998 (and continued to play an executive role after that); and Mr. Zar was CFO from June 22, 1998 until October 7, 2003.

2345497, at * 2 (D. Or. Aug. 11, 2006); *see also In re Bisys Group, Inc. Derivative Action*, 396 F. Supp. 2d 463, 464 (S.D.N.Y. 2005) ("This Court holds that there is no private right of action under § 304 of Sarbanes-Oxley").[176] Thus, neither the derivative plaintiffs nor CA have standing to assert this claim.

For example, in *Neer v. Pelino*, 389 F. Supp. 2d at 657, the U.S. District Court for the Eastern District of Pennsylvania held that shareholders lacked standing to seek reimbursement under § 304, finding that it did not create an express or implied private right of action. Reviewing the text of the statute, the Court observed that Sarbanes-Oxley explicitly created a private right of action to enforce the pension fund trading blackout restrictions under § 306, but failed to include a similar provision in § 304, suggesting that Congress did not intend to create a private right of action under § 304. *Id.* at 655. The Court then looked to the legislative history of the Act, finding that "neither supporters nor opponents of the House draft wanted to give private parties the right to seek disgorgement under this provision," and that nothing in the Senate Report suggested a different intent. *Id.* at 657. Rather, the Court found that Congress intended that the SEC, and not private parties, have the power to enforce § 304 and to seek disgorgement of profits on behalf of the issuer. *See id.* As a result, the Court

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[176] *See also Neer v. Pelino*, 389 F. Supp. 2d 648, 657 (E.D. Pa. 2005) ("In light of the text and structure of the [Sarbanes-Oxley] Act and its legislative history, we find that Congress did not intend to create an implied cause of action in Section 304"); *In re Goodyear Tire & Rubber Co. Derivative Litig*., 2007 WL 43557, at *7 (N.D. Ohio Jan. 5, 2007) ("The Court holds that no private right of action exists under Section 304 of the Sarbanes-Oxley Act of 2002."); *Kogan v. Robinson*, 432 F. Supp. 2d 1075, 1082 (S.D. Cal. 2006) (the court "joins all other courts that have considered this issue" and "[i]n light of the text and structure of Section 304 and the Sarbanes-Oxley Act, this Court declines to imply a private right of action"); *In re Whitehall Jewelers, Inc. S'holder Derivative Litig.*, 2006 WL 468012, at * 8 (N.D. Ill. Feb. 27, 2006) ("this court is inclined to concur with its colleagues in *Neer* and *Bisys Group* that no private right of action is available under § 304"); Harold S. Bloomenthal, Sarbanes-Oxley Act in Perspective § 10.4 ("All of the district courts that have reached the issue in derivative actions based on Section 304 have concluded that it does not create a private action that can be brought by a shareholder in a derivative action seeking to compel the chief executive and financial officer to reimburse the issuer").

dismissed the shareholders' § 304 claim for lack of standing. This same analysis undoubtedly bars plaintiffs' § 304 claim here as well.

There is also a question as to whether § 304, enacted by Congress on July 30, 2002, can be retroactively applied to require disgorgement as a result of misconduct that occurred prior to the date of enactment. As alleged by plaintiffs in the 2005 Derivative Complaint, "in April of 2004, CA was required to restate more than $2 billion as a result of material noncompliance with the financial reporting requirements of the federal securities laws." 2005 Compl. ¶ 258. This restatement covered CA's publicly-disclosed financials for fiscal years 1998, 1999, 2000, and 2001, which ended on March 31, 2002. *See id* ¶ 260. Thus, although CA's restatement was announced in April 2004, after the effective date of § 304, the restatement was a result of misconduct that had occurred before § 304 was enacted.

The federal courts have not yet definitively determined whether § 304 can be applied retroactively to reach financial statements that are restated due to misconduct that occurred prior to the effective date of the statute. However, in *In re AFC Enterprises, Inc. Derivative Litigation*, 224 F.R.D. 515, 521 (N.D. Ga. 2004), the U.S. District Court for the Northern District of Georgia considered this question and concluded, in dicta, that "[a]bsent a clear indication from Congress to the contrary, the presumption is that legislation does not apply retroactively" (citation omitted). The Court found no such clear indication of congressional intent in § 304. *See id.* ("There is no 'clear indication' from Congress that this forfeiture provision of the Sarbanes-Oxley Act was intended to have retroactive application to misconduct which occurred before its effective date"). However, the Court expressly declined to rule on this issue "at this early stage of the litigation without a developed factual record." *Id.*

The SLC believes that this is the correct analysis.[177] Regardless of the ultimate outcome of the retroactivity analysis in this case, the uncertainty surrounding retroactive application of § 304 is an additional factor that undermines a § 304 claim, and further counsels against pursing this claim.

Given the clear legal impediments to bringing a successful § 304 claim, the SLC concludes that it is not in CA's best interests to bring this claim, as the likely costs attendant to litigating a resolution of the legal issues outweigh any possible recovery for the Company. The SLC reaches this conclusion based on this legal analysis, as well as the fact that it has other valid and viable claims against Messrs. Wang and Schwartz, and that those claims provide a more than sufficient basis for recovery for the Company.

B. ***Count Two: Statutory Contribution Against the Individual Defendants and Auditor Defendants***

Count two of the 2005 Derivative Action seeks contribution from all individual defendants and Auditor Defendants[178] pursuant to the PSLRA, 15 U.S.C. § 78u-4(f)(8), which states that "[a] covered person who becomes jointly and severally liable for damages in any private action may recover contribution from any other person who, if joined in the original action, would have been liable for the same damages." On CA's behalf, plaintiffs seek to recover from the individual defendants and Auditor Defendants the 5.7 million shares of CA

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177 Some commentators have noted that this remains an open question. *See* Harold S. Bloomenthal & Samuel Wolff, Securities and Federal Corporate Law § 20:14.12 (2d ed. 2001); Paul H. Dawes, *The Disgorgement Mandates of Sarbanes-Oxley Section 304: Do They Reach Innocent CEOs and CFOs?*, in Securities Litigation & Enforcement Institute 2006, PLI Corp. Law & Practice Course, Handbook Series No. 8805, at 111 (2006).

178 The Individual Defendants named in this claim are as follows: Russell Artzt, Sanjay Kumar, Stephen Richards, Ira Zar, Steven Woghin, David Kaplan, David Rivard, Lloyd Silverstein, Charles Wang, Willem de Vogel, Richard Grasso, Roel Pieper, Michael McElroy, Charles McWade, and Peter Schwartz. For reasons previously discussed, the analysis in this section will not address plaintiffs' statutory contribution claim against the Auditor Defendants.

common stock that CA paid to settle the Class Actions and the 2003 Derivative Action. *See* 2005 Compl. ¶ 264.

For the reasons stated below, the SLC has determined that a statutory contribution claim is unlikely to succeed on the merits because (i) it is barred by statute and the judicially-approved settlement agreement to which CA was a party; and (ii) it may be barred by the applicable statute of limitations. Further, in the exercise of its business judgment, the SLC has concluded that strategic considerations counsel against pursuit of this claim. As previously discussed, CA has other viable claims against the individual defendants whom the SLC believes are culpable that are more likely to succeed and are less susceptible to costly legal challenge. Against the remaining individual defendants, CA does not believe that such claims are factually viable or in the best interests of the Company. As such, there is no need to upset the existing Class Action settlement and expose CA to the costs associated with relitigating the Class Action claims where other valid and viable claims already exist. Therefore, the SLC has determined that this claim should be dismissed.

1. **A Claim for Statutory Contribution is Barred by the 2003 Settlement and Final Judgment**

First, the Order and Final Judgment entered by Judge Platt on December 10, 2003, provides that:

> Pursuant to time [sic] PSLRA and 15 U.S.C. § 78u-4(f)(7), the Released Parties are hereby discharged from all claims for contribution by any person or entity, whether arising under state, federal or common law, based upon, arising out of, relating to, or in connection with the Settled Claims of the Settlement Class or any Settlement Class Member. Accordingly, to the full extent provided by the PSLRA, the Court *hereby bars any action by any person or entity, for contribution against the Released Parties arising out of the Securities Class Actions.*

Final Judgment ¶ 9 (emphasis added). Thus, the Final Judgment makes clear that all claims for contribution arising out of the settlement against "released parties," by any person or entity, are barred.

> The Final Judgment defines "Released Parties" as:
>
> The *CA Defendants* and each of their *past or present* subsidiaries, parents, successors, predecessors, insurers, reinsurers, *officers*, *directors*, shareholders, members, *employees*, agents, fiduciaries, partners, principals, registered representatives, analysts, advisors, investment advisors, independent contractors, underwriters, issuers, insurers, co-insurers, reinsurers, investment bankers, consultants, personal representatives, divisions, assigns, attorneys, accountants . . . heirs, beneficiaries, members of their immediate families and any person, firm, trust, corporation, or other individual or entity in which any CA Defendant has a controlling interest or which is related to or affiliated with any of the CA Defendants and the legal representatives, heirs, successors in interest or assigns of the CA Defendants (the "Released Parties").

Final Judgment ¶ 7 (emphasis added, repetitions in original). The "CA Defendants" are defined to include CA, Inc., Charles Wang, Sanjay Kumar, Russell Artzt, Ira Zar, Willem de Vogel, Richard Grasso, Shirley Strum Kenny and Irving Goldstein. *Id.* at p. 1. As a result of that definition, and the use of the terms "past or present . . . officers, directors, . . . [and] employees," all defendants named in the 2005 Derivative Action are "released parties." *Id.* ¶ 7.[179] As a result, CA's statutory contribution claim against all individual defendants is barred by the Final Judgment.

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179 The following defendants in the 2005 Derivative Action who were not parties to the Class Action settlement are released by paragraph 7 of the Final Judgment: "past or present directors," including Kenneth Cron, Alfonse D'Amato, Lewis Ranieri, Gary Fernandes, Robert La Blanc, Jay Lorsch, Roel Pieper, and Walter Schuetze; "past or present officers," including Stephen Richards, Steven Woghin, Michael McElroy, Charles McWade, and Peter Schwartz; and "past or present employees," including David Kaplan, David Rivard, and Lloyd Silverstein. The remaining defendants to the 2005 Derivative Action – including Charles Wang, Sanjay Kumar, Russell Artzt, Ira Zar, Willem de Vogel, and Richard Grasso – were parties to the Class Action settlement and are released as "CA defendants." Shirley Strum Kenny and Alex Vieux were also released from liability as "CA defendants," but were not named as defendants in the 2005 Derivative Compliant.

2. The Statute Bars CA From Pursuing a Claim for Statutory Contribution Against Certain Defendants

Under the PSLRA, contribution cannot be sought "by any person against [a] settling covered person." 15 U.S.C. § 78u-4(f)(7). Thus, all "settling covered persons" are protected against a claim for contribution by CA. A "covered person" is defined, in relevant part, as "a defendant in any private action arising under this chapter." 15 U.S.C. § 78u-4(f)(10)(C)(i). Those defendants who were parties to the settlement of the Class Actions, as approved in the Final Judgment, are therefore "settling covered persons," against whom CA cannot seek contribution. Thus, statutory contribution claims against Russell Artzt, Richard Grasso, Sanjay Kumar, Willem de Vogel, Charles Wang, and Ira Zar, all of whom were named as defendants in the Class Actions and were parties to the settlement, and are therefore "settling covered persons," are barred by the PSLRA.

Further, 15 U.S.C. § 78u-4(f)(7)(A)(ii) bars claims for contribution arising out of a settled class action "by the settling covered person against any person, other than a person whose liability has been extinguished by the settlement of the settling covered person." CA is a "settling covered person," as it was a defendant in the Class Actions, and a party to the settlement. Thus, CA's claim for contribution is barred, except as to a person "whose liability has been extinguished by the settlement of the settling covered person." 15 U.S.C. § 78u-4(f)(7)(A)(ii). Taken alone, the text of the PSLRA suggests that it may be possible for CA to seek contribution from those individuals who have been released from potential liability for the actions at issue in the Class Action complaint, but who were not named as defendants to that action or parties to the settlement thereof – i.e., persons whose "liability has been extinguished" by CA's settlement. *See id.*[180]

However, as previously discussed, the bar order entered as part of the Final Judgment more broadly defines the class of released parties than does the PSLRA, and therefore more broadly restricts the availability of contribution by discharging the "Released Parties . . . from *all claims for contribution by any person or entity*." Final Judgment ¶ 9 (emphasis added).

The PSLRA requires that:

> [u]pon entry of the settlement by the court, the court shall enter a bar order constituting the final discharge of all obligations to the plaintiff of the settling covered person arising out of the action. The order shall bar all future claims for contribution arising out of the action–
> (i) by any person against the settling covered person; and
> (ii) by the settling covered person against any person, other than a person whose liability has been extinguished by the settlement of the settling covered person.

15 U.S.C. § 78u-4(f)(7)(A).

In contrast, the bar order in the Final Judgment does not carve out an exception for contribution actions against "a person whose liability has been extinguished by the settlement of the settling covered person," where such a person otherwise falls within the definition of "Released Parties." *See* Final Judgment ¶ 7. While the PSLRA mandates entry of such a bar order, it does not prohibit the entry of an order barring contribution from a more broadly-defined class of individuals.[181] The bar order contained in the Final Judgment was

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[180] This includes Kenneth Cron, Alfonse D'Amato, Gary Fernandes, David Kaplan, Robert La Blanc, Jay Lorsch, Michael McElroy, Charles McWade, Roel Pieper, Lewis Ranieri, Stephen Richards, David Rivard, Walter Schuetze, Peter Schwartz, Lloyd Silverstein, and Steven Woghin.

[181] *See, e.g., In re Consol. Pinnacle West Sec. Litig.*, 51 F.3d 194, 197 (9th Cir. 1995) (upholding bar order prohibiting contribution claims against non-party insurers); *In re PNC Fin. Serv. Group, Inc. Sec. Litig.,*

negotiated and agreed to by the parties, and approved by the Court. The fact that the Final Judgment prohibits contribution claims against non-party individuals not explicitly referenced in the PSLRA does not affect its validity or enforceability, and it is controlling here.

3. A Statutory Contribution Claim May be Barred by the Statute of Limitations

In addition to being barred by the Final Judgment, plaintiffs' statutory contribution claim may be barred by the short six-month statute of limitations for such actions. *See* 15 U.S.C. § 78u-4(f)(9). The relevant statute of limitations provides:

> In any private action determining liability, an action for contribution shall be brought not later than 6 months after the entry of a final, nonappealable judgment in the action, except that an action for contribution brought by a covered person who was required to make an additional payment pursuant to paragraph (4) may be brought not later than 6 months after the date on which such payment was made.

15 U.S.C. § 78u-4(f)(9). After two amendments, the Final Judgment was entered January 5, 2004. *See* Compl. ¶ 265.[182]

Plaintiffs contend that this was the "final, nonappealable judgment," entry of which began the six-month statutory limitations period. Plaintiff's initial complaint, captioned *Ranger Governance, LTD. v. Computer Associates International, Inc. et al.* (the "Initial Complaint"), was dated and received by the Court on June 29, 2004 – within the six-month

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440 F. Supp. 2d 421, 442-43 (W.D. Pa. 2006) ("The overwhelming weight of authority addressing the issue of whether the PSLRA was intended to provide the exclusive approach to a court barring claims upon the entry of a partial settlement has soundly rejected the proposition. . . . No aspect or provision of the PSLRA addresses or suggests that it is the only bar order that may be sanctioned by the courts"); *In re Rite Aid Corp. Sec. Litig.*, 146 F. Supp. 2d 706, 731-32 (E.D. Pa. 2001) (upholding bar order prohibiting contribution claims against "released parties" defined broadly to include "Settling Defendants and their respective [non-party] predecessors, successors, affiliates, officers, attorneys, agents, insurers, and assigns" except as it categorically applied to "attorneys").

182 The judgment to which plaintiffs presumably refer is actually dated January 5, 2004, and not January 6, 2004, as plaintiffs allege.

limitations period. However, the Initial Complaint did not allege a claim for contribution under 15 U.S.C. § 78u-4(f)(8) against the individual defendants, or enumerate specific facts relating to the Class Action settlement for which CA would seek contribution. Plaintiffs' statutory contribution claim was detailed for the first time in the 2005 Derivative Complaint, filed January 7, 2005 – more than six months after the Final Judgment was entered, and therefore untimely under § 78u-4(f)(9).[183] Thus, the question is whether this claim "relates back" to the Initial Complaint, filed on June 29, 2004 – if so, the statutory contribution claim will be considered timely. If not, it will be barred by the statute of limitations.

Federal Rule of Civil Procedure 15(c) states, in relevant part, that for the purpose of determining whether an amended complaint has been filed within the applicable limitations period,

> [a]n amendment of a pleading relates back to the date of the original pleading when (1) relation back is permitted by the law that provides the statute of limitations applicable to the action, or (2) the claim or defense asserted in the amended pleading arose out of the conduct, transaction, or occurrence set forth or attempted to be set forth in the original pleading.

Federal Rule of Civil Procedure 15(c)(1) does not apply, since nothing in the PSLRA explicitly provides for the relation back of an amended complaint. However, Federal Rule of Civil Procedure 15(c)(2) may allow plaintiffs' statutory contribution claim to "relate back" to the original derivative complaint if it arises "out of the [same] conduct, transaction, or occurrence set forth . . . in the original pleading."

As a preliminary matter, the relation back doctrine of Fed. R. Civ. P. 15(c) "is to be liberally construed," *In re Flag Telecom Holdings, Ltd. Securities Litigation*, 411 F. Supp.

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183 A First Amended Complaint was filed on July 28, 2004. However, like the initial complaint, this First Amended complaint did not seek contribution for payments made by CA to settle the class action or derivative litigation, and it was outside the six-month period in any event.

2d 377, 385 (S.D.N.Y. 2006), in accord with the purpose of the Rule, which "is to provide maximum opportunity for each claim to be decided on its merits rather than on procedural technicalities." *Slayton v. Am. Express Co.*, 460 F.3d 215, 228 (2d Cir. 2006) (quotation omitted). However, "[f]or a newly added action to relate back, the basic claim must have arisen out of the conduct set forth in the original pleading." *Id.*; *see also Mayle v. Felix*, 545 U.S. 644, 659 (2005) ("relation back depends on the existence of a common core of operative facts uniting the original and newly asserted claims").

More specifically, "[t]he inquiry in a determination of whether a claim should relate back will focus on the notice given by the general fact situation set forth in the original pleading." *Flag Telecom*, 411 F. Supp. 2d at 385 (quotation omitted); *see also Union Carbide Corp. v. Montell N.V.*, 944 F. Supp. 1119, 1140 (S.D.N.Y. 1996) ("[T]he principal inquiry is whether adequate notice of the matters raised in the amended pleading has been given to the opposing party by the general fact situation alleged in the original pleading") (quotation omitted). As such, "[w]here the amended complaint does not allege a new claim but renders prior allegations more definite and precise, relation back occurs." *Slayton*, 460 F.3d at 228. Analysis of this issue is, not surprisingly, fact and case specific, but prior case law provides some, although not dispositive, guidance.

For example, in *Slayton*, a securities fraud case, the Second Circuit held that an allegation that American Express improperly inflated its revenue and failed to follow GAAP, asserted for the first time in the amended complaint, related back to a claim in the initial complaint that the company had inadequate internal controls, which led to the overstatement of accounts receivable. *Id.* at 228-29. The allegations in the original and amended complaint all related to the plaintiffs' causes of action for securities and common law fraud, and the amended complaint's allegations merely "amplified, or stated in a slightly different way," the claims made in the original complaint. *Id.*

In contrast, in *In re Alcatel Securities Litigation*, 382 F. Supp. 2d 513, 528-29 (S.D.N.Y. 2005), the Court held that plaintiffs' securities fraud claims arising from the company's acquisitions did not relate back to the original complaint, which alleged misstatements in the prospectus in connection with the company's initial public offering ("IPO"). Whereas the initial complaint centered on the IPO and the allegedly misleading statements made in the prospectus, it did not allege that these misstatements were part of an overall fraudulent scheme to misstate earnings and hide unfavorable business developments, which was the focus of the amended complaint. The Court therefore rejected plaintiffs' argument that the amended complaint alleged the "same basic wrongs," and held that the original complaint failed to provide defendants with adequate notice of their intent to bring suit for fraudulent conduct in connection with the company's acquisitions prior to its IPO. *Id.* at 528. Thus, the Court found that relation back was improper, and rejected the allegations made in the amended complaint as time-barred. *Id.* at 529.

In this case, the Initial Complaint alleged violations of 15 U.S.C. § 7243 (Sarbanes-Oxley) (count one), Breach of Duty Under Faithless Servant Doctrine and the Doctrine of Unjust Enrichment (count two), Breach of Fiduciary Duty (count three), Gross Negligence (count four), Corporate Waste (count five), Fraud (count six), and Conspiracy (count seven), arising from CA's fraudulent accounting practices, the compensation paid to those involved in such practices, and the expenses incurred to conduct internal audits and investigations into the company's financial statements. *See* Initial Compl. ¶¶ 44-65. These claims arose generally out of the "widespread conspiracy at CA to artificially inflate earnings figures in order to increase the price of CA stock going back to at least 1998." Initial Compl. ¶ 27. In contrast, the Initial Complaint did not assert any wrongdoing in connection with the Class Action settlement and, indeed, mentioned the Class Action settlement just once in its recitation of background facts, noting that "[i]n December 2003, to settle class actions alleging fraud and securities violations in connection with the provision of false financial reports, CA agreed to issue and deliver to class members and attorneys approximately $100 million worth of CA stock." Initial Compl. ¶ 26. The Initial Complaint contained no allegations that this settlement was improper, and did not seek contribution for amounts paid by CA as a result.

Viewed broadly, it could be argued that the Initial Complaint very generally alleged the same set of circumstances that give rise to the claim for contribution under the securities laws. Specifically, the accounting fraud detailed in the Initial Complaint was the basis for the Class Actions and resulted in the settlement, for which the 2005 Derivative Complaint seeks contribution.

However, there is nothing in the Initial Complaint evidencing plaintiffs' intent to pursue a claim for contribution under 15 U.S.C. § 78u-4, and there is no allegation attacking the class action settlement as improper or unfair. Likewise, there is no factual nexus between the underlying accounting fraud and the decision to settle the Class Actions. Thus, in the SLC's view, the far better argument is that this is not a case in which the later complaint simply restated in greater detail an initial cause of action, but rather one in which an entirely new cause of action has been asserted based on a statutory provision that was not mentioned in the original complaint.

In sum, in the SLC's view, a claim for statutory contribution is not timely under the PSLRA, and it is likely that any such claim will be contested on that basis, adding additional expense and delay to this litigation. Thus, given this uncertainty and, as discussed above, because a claim for statutory contribution under 15 U.S.C. § 78u-4(f)(8) is unlikely to succeed due to the releases granted in the Final Judgment and the statutory bar against contribution claims against "settling covered persons," the SLC has determined that it is not in the Company's best interests to pursue this claim and that it should be dismissed.

C. ***Count Three: Breach of Fiduciary Duty***

Count three of the 2005 Derivative Complaint alleges that each of the individual defendants breached their fiduciary duties owed to the Company. 2005 Compl. ¶¶ 271-72; *see also* Kaufman Compl. ¶¶ 103-04. As described above, this cause of action can be divided into four distinct claims. First, it is alleged that CA's directors and officers breached their fiduciary duties to the Company by failing to properly oversee CA's business practices during the years in which the 35-Day Month practice and improper revenue recognition was taking place. *See* 2005 Compl. ¶ 272; *see also* Kaufman Compl. ¶¶ 37, 44. Second, it is alleged that CA's Board of Directors failed to properly oversee CA's business practices through the course of the government investigation. *See* Kaufman Compl. ¶ 104. Third, it is alleged that CA's Board of Directors breached its fiduciary duties by approving the 2003 Settlement, pursuant to which CA released all then-current and former directors and officers from liability, and by authorizing and approving the DPA, both without seeking contribution from known wrongdoers. *See* Kaufman Compl. ¶¶ 104, 112; 2005 Compl. ¶¶ 265, 273, 276, 285. Finally, it is alleged that CA's Board of Directors breached its fiduciary duties by failing to take action against Mr. Kumar immediately after Lloyd Silverstein pled guilty to federal criminal charges in late January 2004. Kaufman Compl. ¶¶ 93-97.

1. The *Caremark* Claim

The *Caremark* claim alleged in the 2005 Derivative Complaint and the Kaufman Complaint challenges the CA Board's oversight during two (2) distinct periods in time: (i) the period during which the 35-Day Month practice occurred, and (ii) the period during which the government investigation occurred. Both periods are analyzed separately herein.

First, as stated above, the 2005 Derivative Complaint alleges that during the period of fraudulent conduct the Oversight Director Defendants – Russell Artzt, Alfonse D'Amato, Willem de Vogel, Richard Grasso, Sanjay Kumar, Roel Pieper, and Charles Wang[184] – breached their duty of oversight by failing to take steps to prevent and uncover the 35-Day Month practice. *See* 2005 Compl. ¶¶ 271-277.[185]

In support of this claim, the 2005 Derivative Complaint alleges that the Oversight Director Defendants ignored "numerous red flags that indicated the lack of oversight at CA" and that this failure caused "serious, if not irreparable, damage to the Company, its reputation and its business prospects." 2005 Compl. ¶ 272(a). However, plaintiffs do not identify *any* of these "red flags" of which they claim the Board was, or should have been, aware. Plaintiffs further assert – again without any supporting factual allegations – that the Oversight Director Defendants (i) failed "to have in place sufficient controls and procedure to monitor CA's practices" (*id.* ¶ 272(b)), (ii) "knowingly or recklessly disseminat[ed] and

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184 Shirley Strum Kenny is not named as a defendant in the 2005 Derivative Complaint, notwithstanding the fact that she served on the CA Board during the period in which the fraud occurred. She was named as a defendant in the Kaufman Complaint.

185 Likewise, the Kaufman Complaint alleges that directors Willem de Vogel, Richard Grasso, and Shirley Strum Kenny breached their duty of oversight by "failing to detect the accounting fraud and the subsequent efforts by [management] to cover it up." *See* Kaufman Compl. ¶ 44. However, the Kaufman Complaint is devoid of *any* factual allegations relating to the time period in which the fraud occurred. Indeed, this unsupported allegation contained in the "Parties" section of the complaint is the only mention of the claim in the entire complaint. *See id*.

permit[ed] to be disseminated, misleading information to shareholders, the investing public and the public at large" (*id.* ¶ 272(c)), and (iii) allowed "the Company to engage in wholesale improper accounting practices which subjected the Company to fines, penalties, lawsuits and further investigation." (*Id.* ¶ 272(d)).

Second, the Kaufman Complaint alleges that the Criminal Defendants, the Oversight Director Defendants,[186] and the Settlement Director Defendants – Russell Artzt, Kenneth Cron, Alfonse D'Amato, Gary Fernandes, Sanjay Kumar, Robert La Blanc, Jay Lorsch, Lewis Ranieri, Walter Schuetze, and Alex Vieux – "directed, participated in and/or obstructed the government's investigation into the accounting fraud and/or permitted or failed to take action against others who obstructed the investigation thereby subjecting the Company to criminal indictment, heavy monetary fines, debarment from all government business, and other severe sanctions." Kaufman Compl. ¶ 104(a).[187]

Conclusion. As is discussed below, the SLC has determined that the non-management Oversight Director Defendants and the Settlement Director Defendants exercised legally sufficient oversight at CA, and as such, did not breach their duty under Delaware law during the periods in question. In addition, as discussed above, the SLC has concluded, in exercising its business judgment under Delaware law, that it is in the best interests of the

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186 The only exception is Roel Pieper, who is not named as a defendant in the Kaufman Complaint, notwithstanding the fact that he served on the CA Board during the period in which the fraud occurred.

187 Part of this allegation is plainly and demonstrably wrong. In actuality, CA has not been debarred from "all government business" as alleged by Ms. Kaufman. Quite to the contrary, as the Board of Directors was informed, CA risked debarment had it *not* entered into the DPA, and CA's customer list continues to include several government entities. (*See e.g.,* Deborah Solomon & Anne Marie Squeo, *Crackdown Puts Corporations, Executives in New Legal Peril – More Than Ever, Businesses Face Risk of Prosecution; Post-Enron, a Changed View – Companies Rush to Cooperate*, WALL ST. J., June 20, 2005, at A1 ("In April 2004, the government threatened to indict the company if it didn't replace top management, attorneys on both sides say. An indictment would have been devastating to the company's already-tarnished reputation, and a finding of guilt would have precluded CA sales to the federal government, a major customer")).

Company to seek dismissal of this claim with respect to Mr. McElroy. As also discussed above, with respect to Messrs. Wang and Schwartz, the SLC has concluded that the Company has valid and viable claims for breach of fiduciary duty based on, among other things, their knowledge of, and participation in, the 35-Day Month practice, and that it is in the best interests of the Company to pursue those claims. Finally, as noted above, the SLC has reached settlements with Messrs. Artzt, Kumar, and McWade pursuant to which it will seek dismissal of all claims against them.

(a) Director Decision Making: The Duty of Care[188]

Directors and officers owe a duty of care to the Company (*see Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985)) that requires them to "'use that amount of care which ordinarily careful and prudent men would use in similar circumstances,' and 'consider all material information reasonably available' in making business decisions." *In re the Walt Disney Co. Derivative Litig.,* 907 A.2d 693, 749 (Del. Ch. 2005) ("*Disney IV*"), *aff'd*, 906 A.2d 27 (Del. 2006); *see also Brehm v. Eisner*, 746 A.2d 244, 259 (Del. 2000) ("in making business decisions, directors must consider all material information reasonably available"); *Aronson*, 473 A.2d at 812 ("directors have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them"). As such, the business judgment rule is a judicial presumption that directors and officers acted "on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company."

188 CA is incorporated in the state of Delaware. As a result, under New York law, the fiduciary obligations owed by CA's officers and directors are analyzed under Delaware substantive law. *See BBS Norwalk One, Inc. v. Raccolta, Inc.*, 60 F. Supp. 2d 123, 129 (S.D.N.Y. 1999), *aff'd*, 205 F.3d 1321 (2d Cir. 2000) ("Consistent with the internal affairs doctrine, a claim of breach of fiduciary duty owed to a corporation is governed by the law of the state of incorporation").

Aronson, 473 A.2d at 812; *see also Disney IV*, 907 A.2d at 755 ("[t]he presumption of the business judgment rule creates a presumption that a director acted in good faith").

(b) Director Oversight: The Duty of Loyalty

Nonetheless, director liability may be premised on a director either (i) *intentionally* failing to act where action is required, or (ii) *intentionally* failing to cause the company to have adequate information and reporting systems in place. In either case, such conduct by a director constitutes a failure to discharge his/her fiduciary duties in good faith, and, therefore, violates the duty of loyalty. *See Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006) ("*Stone II*") ("Where directors fail to act in the face of a known duty to act, thereby demonstrating a conscious disregard for their responsibilities, they breach their duty of loyalty by failing to discharge that fiduciary obligation in good faith"); *Guttman v. Huang*, 823 A.2d 492, 506 (Del. Ch. 2003) (the "standard for liability for failures of oversight . . . requires a showing that the directors breached their duty of loyalty by failing to attend to their duties in good faith"). Indeed, a lack of good faith is a "necessary condition to liability" in the oversight context and "a failure to act in good faith requires conduct that is qualitatively different from, and more culpable than, the conduct giving rise to a violation of the fiduciary duty of care (i.e., gross negligence)." *Stone II*, 911 A.2d at 369.

Accordingly, directors alleged to have violated their duty of oversight do not receive the protection of the business judgment rule, as there is no "business judgment" to which the courts can defer. *See, e.g.*, *Rattner v. Bidzos*, 2003 WL 22284323, at *8 (Del. Ch. Oct. 7, 2003) (refusing to apply the business judgment rule when making a demand futility decision). However, liability under this theory is extremely rare, and courts have noted that an oversight claim is "possibly the most difficult theory in corporation law upon which a plaintiff might hope to win a judgment." *Caremark*, 698 A.2d at 959, 967; *see also Halpert Enter., Inc.*

v. Harrison, 2007 WL 486561, at *5 (S.D.N.Y. Feb. 14, 2007) (citation omitted); *Stone II*, 911 A.2d at 372 (same); *Rattner*, 2003 WL 22284323, at *8 ("a claim for failure to exercise proper oversight is one of, if not the, most difficult theories upon which to prevail").

To establish a failure of oversight, a plaintiff must show "either (1) that the directors knew or (2) should have known that violations of law were occurring *and*, in either event, (3) that the directors took *no steps* in a good faith effort to prevent or remedy that situation, *and* (4) that such failure proximately resulted in the losses complained of." *Caremark,* 698 A.2d at 971 (emphasis added); *see also Saito v. McCall*, 2004 WL 3029876, at *6 (Del. Ch. Dec. 20, 2004). This test can be satisfied by showing either that: (i) "the directors *utterly failed* to implement *any* reporting or information system or controls," or "having implemented such a system or controls, *consciously* failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention"; or (ii) that the directors "had notice of serious misconduct and simply failed to investigate," i.e., intentionally ignored "red flags." *Stone II*, 911 A.2d at 370 (emphasis added); *Shaev*, 2006 WL 391931, at *5 ("a *Caremark* plaintiff can plead that 'the directors were conscious of the fact that they were not doing their jobs,' and that they ignored 'red flags' indicating misconduct in defiance of their duties").

The "failure to exercise oversight" claim and the "failure to investigate" claim are "closely related," but distinct. *Shaev,* 2006 WL 391931, at *5. For both claims, however, "imposition of liability requires a showing that the directors *knew* that they were not discharging their fiduciary obligations." *Stone II*, 911 A.2d at 370 (emphasis added); *Guttman*, 823 A.2d at 505 (director liability is premised on "a showing that the directors were conscious of the fact that they were not doing their jobs"); *In re the Walt Disney Co. Derivative Litig*., 906

A.2d 27, 67 (Del. 2006) ("*Disney V*") ("A failure to act in good faith may be shown . . . where the fiduciary intentionally fails to act in the face of a known duty to act, demonstrating a conscious disregard for his duties").

(i) Failure to Exercise Oversight

(1) Legal Standard

The duty of oversight does not require directors to possess detailed information about all operational aspects of a business. *See Caremark,* 698 A.2d at 971. Rather, directors must "attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists, and that failure to do so under some circumstances may, in theory at least, render a director liable for losses caused by non-compliance with applicable legal standards." *Id.* at 970; *see also Shaev*, 2006 WL 391931, at *5. However, "only a *sustained or systematic failure* of the board to exercise oversight – such as an utter failure to attempt to assure a reasonable information and reporting system exists – will establish the lack of good faith that is a necessary condition to liability." *Caremark,* 698 A.2d at 971 (emphasis added)*; see Halpert,* 2007 WL 486561, at *5 (citation omitted); *Stone II*, 911 A.2d at 369 (affirming the standard for oversight liability articulated in Caremark).

As noted above, to render directors liable for a failure to implement adequate information systems and controls, the directors' failure must amount to bad faith, meaning that the failure to act was intentional. *See Stone II*, 911 A.2d at 370 ("a showing of bad faith conduct, in the sense described in *Disney* and *Caremark*, is essential to establish director oversight liability"); *Disney IV*, 907 A.2d at 755 ("Upon long and careful consideration, I am of the opinion that the concept of *intentional dereliction of duty*, a *conscious disregard for one's responsibilities*, is an appropriate (although not the only) standard for determining whether fiduciaries have acted in good faith") (emphasis in original).

There is no legal formula prescribing the steps directors must take to ensure that a company has in place reasonable information and reporting systems. Delaware courts, however, have provided some guidance as to the types of controls a board can implement in order to satisfy their duty of oversight. For example, a duly-constituted audit committee that meets regularly, and the retention of an independent audit firm, are the types of reporting systems that a Board can implement to satisfy its duty of oversight. *See Shaev*, 2006 WL 391931, at *5 (a failure of oversight can be shown by demonstrating that a board "entirely lacked an audit committee or other important supervisory structures, or that a formally constituted audit committee failed to meet"); *Ash v. McCall*, 2000 WL 1370341, at *15 n.57 (Del. Ch. Sept. 15, 2000) ("the existence of an audit committee, together with [the] retention of Arthur Anderson as . . . outside auditor to conduct annual audits of the Company's financial reporting, is some evidence that a monitoring and compliance system was in place").

Whether the reporting systems actually worked is not the test. Indeed, in a recent decision, the Delaware Supreme Court explicitly rejected an attempt to "equate a bad outcome with bad faith" in the oversight context. *Stone II*, 911 A.2d at 373. In that case, certain employees of AmSouth Bancorporation failed to file Suspicious Activity Reports ("SARs"), as required under federal law, in connection with a customer's establishment of custodial accounts that were then used by the customer in a criminal scheme. *See id.* at 365. AmSouth ultimately became the subject of a federal criminal investigation because of the failure of its employees to file SARs. *See id.* at 366.

In order to resolve the criminal investigation, AmSouth, like CA, entered into a deferred prosecution agreement in which it admitted that "at least one" employee knowingly failed to file SARs in a timely manner, and, like CA, agreed to pay a substantial fine. *Id.* In addition, the Federal Reserve and Alabama Banking Department issued an order requiring AmSouth to, among other things, engage an independent consultant to review its compliance programs and make recommendations "for new policies and procedures to be implemented by the Bank," much like the independent examiner required under CA's DPA. *Id.* at 366; *see* DPA ¶¶ 19-22.

Plaintiffs brought a claim against the AmSouth Board of Directors alleging solely that the directors "had utterly failed to implement any sort of statutorily required monitoring, reporting or information controls that would have enabled them to learn of problems requiring their attention." *Stone II,* 911 A.2d at 370. The Supreme Court affirmed the Court of Chancery's dismissal for failure to make a demand on the AmSouth Board, as there were no particularized facts that "created reason to doubt whether the directors had acted in good faith in exercising their oversight responsibilities." *Id.* at 373. Based on findings made by AmSouth's independent consultant (which were incorporated into the complaint), the Supreme Court concluded that "the Board received and approved relevant policies and procedures, delegated to certain employees and departments the responsibility for filing SARs and monitoring compliance, and exercised oversight by relying on periodic reports from them." *Id.*

The Supreme Court added that "the directors' good faith exercise of oversight responsibility may not invariably prevent employees from violating criminal laws, or from causing the corporation to incur significant financial liability, or both." *Id.* at 373*; see also Shaev,* 2006 WL 391931, at *5 ("one thing that is emphatically not a *Caremark* claim is the bald allegation that directors bear liability where a concededly well-constituted oversight mechanism, having received no specific indications of misconduct, failed to discover fraud").

Thus, a claim that a board must have violated its duty of oversight simply because fraud – even criminal fraud – occurred lacks merit. *See Shaev*, 2006 WL 391931, at *5 (rejecting a claim that "only a board violating its fiduciary duties could possibly have remained ignorant" of alleged accounting improprieties);[189] *Stone v. Ritter*, 2006 WL 302558, at *2 (Del. Ch. Jan. 26, 2006) ("*Stone I*"), *aff'd*, 911 A.2d 362 (Del. Nov. 6, 2006) ("Neither party disputes that the lack of internal controls resulted in a huge fine – $50 million, alleged to be the largest ever of its kind. The fact of those losses, however, is not alone enough").

In sum, "[i]n the absence of red flags, good faith in the context of oversight must be measured by the directors' actions 'to assure a reasonable information and reporting system exists' and not by second-guessing after the occurrence of employee conduct that results in an unintended adverse outcome." *Stone II*, 911 A.2d at 373 (citation omitted). Thus, with this legal framework in mind, the SLC sought to determine whether the non-management Oversight Director Defendants "breached their duty of oversight," by "utter[ly] fail[ing] to attempt to assure a reasonable information and reporting system exist[ed]." *Caremark*, 698 A.2d at 971.

(2) Analysis

In considering plaintiffs' claim that the directors failed to ensure that CA had sufficient information and reporting systems in place during the period of the fraud, the SLC looked first to the allegations in the 2005 Derivative Complaint. However, other than the bald allegation that the directors "fail[ed] to have in place sufficient controls" (*see* 2005 Compl. ¶ 272(b)), plaintiffs provided no facts on this issue (except to acknowledge that CA had a duly constituted Audit Committee that met regularly during each of the fiscal years at issue). *See id.*

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189 As noted above, the claim rejected in *Shaev* is the exact claim alleged by plaintiffs in the 2005 Derivative Complaint. Rather than identifying *any* red flags, plaintiffs allege that "it is impossible to imagine how this fraud could have been perpetrated under the very noses of CA's purportedly sophisticated directors absent a complete failure of oversight or their knowing participation." 2005 Compl. ¶ 216.

¶ 217 ("The Audit Committee met only three times during each of fiscal years 1998 and 1999"). Thus, as part of its investigation, the SLC considered, using Delaware law as its guide, the sufficiency of CA's information and reporting systems. As described below, the SLC has concluded that the information and reporting systems during the fraud were designed to ensure that appropriate information reached the Board, and were therefore legally sufficient under Delaware law. As such, the SLC will seek dismissal of this claim.

As an initial matter, the CA Board established a duly-constituted Audit Committee, which met at regular intervals throughout the fiscal year. In preparation for such meetings, CA management typically provided the Audit Committee members with written materials regarding CA's financial results. Specifically, the CA Audit Committee held the following meetings:

- In fiscal year 1998 (April 1, 1997 to March 31, 1998), the Audit Committee held three (3) formal meetings.
- In fiscal year 1999 (April 1, 1998 to March 31, 1999), the Audit Committee held two (2) formal meetings.
- In fiscal year 2000 (April 1, 1999 to March 31, 2000), the Audit Committee held four (4) formal meetings.[190]
- In fiscal year 2001 (April 1, 2000 to March 31, 2001), the Audit Committee held four (4) formal meetings.

Further, CA's Audit Committee retained E&Y, and then KPMG – both "Big 4" accounting firms – as CA's independent outside accounting firm to audit CA's consolidated financial statements.[191] At its meetings, the Audit Committee met independently with CA's

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190 Plaintiffs allege incorrectly that the Audit Committee met twice during fiscal year 2000. *See* 2005 Compl. ¶ 217.

191 For fiscal years 1997, 1998 and 1999, E&Y planned and performed annual audits of the consolidated financial statements of CA and its subsidiaries, and considered the Company's internal control structure in order to determine auditing procedures for the purpose of expressing an opinion on the consolidated financial statements and not to provide assurance on the internal control structure. *See* Letter from E&Y

outside auditors, without the presence of management. The Audit Committee also received and reviewed annual management letters from CA's outside auditors presenting the results of their audit for each fiscal year. CA maintained an Internal Audit department, which performed primarily international work and non-critical domestic work. The head of Internal Audit attended each Audit Committee meeting and reported to the Audit Committee on the scope and results of its work. In connection with its receipt of management letters from its auditors, the Audit Committee received the credentials of, and a description of audit responsibilities for, each of the employees who worked in the Internal Audit department. At no time was the Audit Committee told that the outside auditors or the Internal Audit department needed additional resources.

Indeed, the information the Board received regarding the implementation of SOP 97-2, which governed revenue recognition at CA, provides an example of how those systems worked to ensure that the Board received relevant information. In the year leading up to, and shortly after the implementation of SOP 97-2 at CA (see section VIII.C., *supra*), the Audit Committee received five (5) reports from E&Y regarding the new accounting rules and their impact on CA's business. For example, prior to SOP 97-2 becoming effective, the Audit Committee was told by the E&Y partner on the CA account that SOP 97-2 would "not have a major impact on CA" and "would have almost no impact on the Company's operations or financial results." Shortly after SOP 97-2 became effective, E&Y told the Audit Committee that it "believed the Company was in compliance with the provision." The message from the

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to the CA Audit Comm. at 1 (May 26, 1999). For fiscal year 2000, KPMG planned and performed an audit of the financial statements of CA, and considered internal controls in order to determine auditing procedures for the purpose of expressing an opinion on the Company's financial statements. This did not include examining the effectiveness of internal controls or providing assurances on internal controls. *See* Letter from KPMG to the CA Audit Comm. at 1 (Sept. 27, 2000).

three (3) other reports by E&Y was similar. Thus, given the numerous reports the Audit Committee received regarding SOP 97-2, the Board reasonably believed that it was receiving relevant information regarding CA's accounting practices, and that reporting advised it that CA was in compliance with the governing accounting guidelines.

The changeover to KPMG – which was precipitated by the Audit Committee when it became dissatisfied with the quality and timeliness of E&Y's work (itself evidencing a level of involvement and oversight) – further highlights the fact that the Board was receiving adequate information. When KPMG was hired, it reviewed CA's internal accounting and finance controls. KPMG then reported in its first management letter, dated September 27, 2000, that it "would generally characterize the Company's accounting systems and related processes as being less integrated and requiring more manual intervention than is typical for enterprises of similar size and breadth." The management letter continues: "[t]he Company's finance staff requires an understanding of off-line processes or familiarity with a generally oral history of transactions. This dependency contributes to the risk of errors in the accounting and financial reporting process." Contributing to this problem was the fact that "[t]he Company does not have a comprehensive set of written accounting policies and procedures." KPMG then recommended that CA develop a set of desk procedures summarizing key accounting policies and procedures. The Audit Committee was subsequently assured by Mr. Zar that the Company was working on such procedures. KPMG raised no issues to the Audit Committee concerning the Company's implementation of, or compliance with, SOP 97-2. Thus, given the identification of these issues by KPMG to the Audit Committee, and the corrective action taken by CA's CFO, the Board reasonably believed that it was receiving information regarding CA's accounting practices sufficient to conduct the appropriate degree of oversight.

In addition, there were information and reporting systems in place to ensure that the entire Board received an appropriate level of information. Specifically, the Board held the following meetings:

- In fiscal year 1998 (January 1, 1998 to March 31, 1998), the Board held eight (8) formal meetings.
- In fiscal year 1999 (April 1, 1998 to March 31, 1999), the Board held fourteen (14) formal meetings.
- In fiscal year 2000 (April 1, 1999 to March 31, 2000), the Board held thirteen (13) formal meetings.
- In fiscal year 2001 (April 1, 2000 to March 31, 2001), the Board held six (6) formal meetings.

In preparation for such meetings, CA management typically provided Board members with written materials, on a monthly and quarterly basis, regarding CA's financial results. The Board also received memoranda from Mr. Woghin, CA's General Counsel, informing the Board of, or updating the Board on, certain material legal events at the Company. The Board often reviewed additional materials, such as PowerPoint presentations regarding CA's quarterly results and draft press releases announcing those results. Generally, CA's CFO, General Counsel, and outside corporate counsel attended these meetings in order to present to the Board and answer any questions that arose.[192] The SLC also found that several members of the Board were in contact with Messrs. Wang, Kumar, Zar, and Woghin outside of meetings when issues arose.

Because CA's Board had these reporting mechanisms in place, to both the Audit Committee and full Board, the SLC concludes that the non-management Oversight Director Defendants exercised legally sufficient oversight at CA, and, as such, did not breach their duty

192 CA's outside securities counsel, Scott Smith of Covington & Burling LLP, was present at Board meetings in order to respond to director questions as appropriate.

of oversight under Delaware law. *See Shaev,* 2006 WL 391931, at *5 (dismissing a *Caremark* claim where there is merely a "bald allegation that directors bear liability where a concededly well constituted oversight mechanism, having received no specific indications of misconduct, failed to discover fraud"); *Guttman,* 823 A.2d at 498 (dismissing complaint where it failed to address "whether the company had an audit committee during [the contested period], how often and how long it met, who advised the committee, and whether the committee discussed and approved any of the allegedly improper accounting practices"). An "unintended adverse outcome" is not a sufficient basis for a claim (*Shaev,* 2006 WL 391931, at *5), and the SLC will seek to dismiss this claim.[193]

(ii) Failure to Investigate

(1) Legal standard

For a "failure to investigate" claim to succeed, there must be "specific red-or even yellow-flags" that put the Board on notice of potential misconduct. *See Guttman,* 823 A.2d at 507. As the Delaware courts have observed, such flags "are only useful when they are either waved in one's face or displayed so that they are visible to the careful observer." *In re Citigroup Inc. S'holders Litig.,* 2003 WL 21384599, at *2 (Del. Ch. June 5, 2003); *see also Guttman,* 823 A.2d at 507 ("the complaint does not plead a single fact suggesting specific red or even yellow flags were waved at the outside directors"); *Rattner,* 2003 WL 22284323 at *13 (same).

Under Delaware law, "absent grounds to suspect deception, neither corporate boards nor senior officers can be charged with wrongdoing simply for assuming the integrity of employees and the honesty of their dealings on the company's behalf." *Caremark*, 698 A.2d at

193 That being said, as described above, several layers below the Audit Committee and Board, the SLC found that CA's internal reporting structure was deficient in many respects.

969. Further, once a red flag is "waved" to the Board, for the Board to be liable, the Board must *willfully* and *intentionally* ignore that flag. *See Stone I*, 2006 WL 302558 at *2 ("[n]or do plaintiffs point to facts suggesting a conscious decision to take no action in response to red flags. Without these well-pled allegations, there is no possibility the defendants faced a substantial likelihood of liability").

For example, in *Stone II*, described at length above, the Delaware Supreme Court defined "red flags" as "facts showing that the board *was aware* that AmSouth's internal controls were inadequate, [and] that these inadequacies would result in illegal activity." 911 A.2d at 370 (emphasis added). In that case, the Court of Chancery found that:

> Plaintiffs' complaint is devoid of the particularized allegations of fact needed to tie the defendants to any of the alleged wrongdoing. Plaintiffs fail to point to any facts either showing how the [criminal] scheme, or any other problems at AmSouth, waved a 'red flag' in the face of the board. Nor do plaintiffs point to facts suggesting a conscious decision to take no action in response to red flags. Without these well-pled allegations, there is no possibility the defendants faced a substantial likelihood of liability.

Stone I, 2006 WL 302558 at *2. Thus, in the absence of specific facts that waved a red flag "in the face" of the directors, and evidence of a conscious decision to ignore those facts, directors will not be found liable for a breach of their duty of oversight. *Id.*

The District Court's decision in *In re Veeco Instruments Inc.*, 434 F. Supp. 2d 267, 277-78 (S.D.N.Y. 2006) provides an example of what constitutes a "red flag" under Delaware law. In that case, an employee reported to management that Veeco had violated federal export laws. The company then conducted an internal audit, and found that several violations of law had actually occurred. *See id.* at 273. The initial report of the employee, and the result of the Company's audit, were reported to the board. Because Veeco derived seventy percent (70%) of its revenue from export sales, and a single violation of federal export laws could have led to the suspension of its export privileges, "the reported violations threatened to jeopardize the future viability of Veeco." *Id.* at 278. Seven (7) months later, the same employee reported another set of export law violations.

The plaintiffs, while failing to plead specific facts regarding the Board's response to the first reported violation, claimed that, in light of the second reported infraction, "the Audit Committee permitted additional violations to occur, either by completely disregarding the first report, or by establishing procedures that were wholly inadequate and ineffective and that failed to protect the Company from potentially enormous liability." *Id.* at 278. In denying the Board's motion to dismiss, the Court held that "[t]his is not a case where the directors had 'no grounds for suspicion' or 'were blamelessly unaware of the conduct leading to the corporate liability.'" *Id.* at 279 (quoting *Caremark,* 698 A.2d at 969). The Court added that "[t]his is precisely the type of case the Delaware Chancery Court was contemplating when it recently held, 'A claim that an audit committee or board had notice of serious misconduct and simply failed to investigate, for example, would survive a motion to dismiss, even if the committee or board was well constituted and otherwise functioning.'" *Id.* at 278 (citations omitted).

In light of this well developed legal framework, the SLC first examined the 2005 Derivative Complaint and the Kaufman Complaint for any alleged "red flags" identified to the Board, but found that they alleged no warnings that the Board was aware of but intentionally ignored. Despite this pleading failure,[194] the SLC sought independently to identify facts or circumstances that should have alerted the Board to the revenue recognition fraud, but were intentionally ignored. At the outset, it is important to note that certain of the Criminal

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[194] As discussed above, this pleading failure alone is grounds for dismissal. *See Guttman*, 823 A.2d at 507.

Defendants who had access to the Board told the SLC that CA's independent directors had no knowledge of the 35-Day Month practice. Nonetheless, based upon its own independent investigation, the SLC identified three potential "red" or "yellow" flags. The SLC's analysis of these is discussed below.

(2) Analysis

a. The Vesting of the KESOP, the July 20 Board Meeting, and the Class Action and Derivative Litigation[195]

The KESOP Vesting. The SLC examined the May 21, 1998 accelerated vesting of the KESOP as a potential "yellow flag." As discussed above, pursuant to the accelerated vesting provisions of the KESOP, which was tied to the Company's stock price, Messrs. Wang, Kumar, and Artzt received CA stock then-valued at $1.1 billion. While the KESOP provided a general motive to artificially inflate CA's stock price, thereby potentially creating a risk of fraud, the SLC found no evidence pointing to specific, or even general, misconduct that was intentionally ignored by the Board in the time period leading up to the accelerated vesting. *See Shaev,* 2006 WL 391931, at *5 ("in order to show that the board violated some fiduciary duty by inaction, a complaint must do much more than simply say that an employee perceived the company to face risk, even a large risk").

Although the accelerated vesting itself was not a "red flag" that a revenue recognition fraud was taking place, the SLC nonetheless sought to determine whether the Board took any steps to ensure the propriety of CA's financial statements, given the motive that the KESOP created. As a result of its investigation, which included interviews with every non-management director at the time (except Irving Goldstein, who passed away in May 2000), the

195 At this time, the Board was comprised of directors Artzt, de Vogel, Goldstein, Grasso, Kenny, Kumar, and Wang.

SLC has determined that the Board took no special steps in that regard. Indeed, it is undisputed that the only KESOP-specific action taken by the Board during the period prior to the accelerated vesting was to ensure that the vesting trigger actually occurred, that is, that CA's stock in fact traded at or above $53.33 for sixty (60) days in a twelve-month period. The Board repeatedly questioned E&Y about the details associated with the charge resulting from the KESOP, but not about the Company's underlying financial statements. It is the SLC's view that, given the enormity of the award, it would have been "better practice" for the outside directors to have taken additional steps to ensure the accuracy of CA's financials during the vesting period; however, their failure to do so did not constitute a breach of their duty of oversight, as there was no indication of a problem with those financials.

This determination is buttressed by the fact that the Board had *very* current information from CA's outside auditors at the time the KESOP vested. Indeed, just *two* (2) *days* before the KESOP vested, at a May 19 joint Board and Audit Committee meeting, the Board received E&Y's audit report for fiscal year 1998, which encompassed the two completed quarters (the third and fourth quarters of fiscal year 1998) preceding the vesting of the KESOP. Representatives from E&Y informed the Board that it had provided an unqualified, or clean, opinion on the Company's financial statements.[196] There is no evidence that E&Y, management, or CA internal audit raised any issue with respect to CA's financial statements for fiscal year 1998 (which ended March 31, 1998), or recommended that the Board or the Audit Committee take any additional action with respect to those financial statements.

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196 As noted above, an "unqualified opinion" is defined as an "independent auditor's opinion that a Company's financial statements are fairly presented, in all material respects, in conformity with generally accepted accounting principles." John Downes and Jordan Elliot Goodman, *Dictionary of Finance and Investment Terms* 765 (6th ed. 2003).

As discussed further below, the Board was entitled to, and did, rely upon its outside auditors to ensure that CA employed proper accounting practices during the periods in which the KESOP vested. *See Cantor v. Perelman*, 235 F. Supp. 2d 377, 388 (D. Del. 2002) ("the Marvel board delegated the corporate accounting duties to E&Y. Further, the board relied upon Ernst & Young expertise in accounting matters . . . Lastly, Ernst & Young provided a clean accounting report to Marvel. As a result, the court finds that the Marvel board met its fiduciary duties with regard to accounting"), *aff'd in part, rev'd in part*, 414 F.3d 430 (3d Cir. 2005).

The July 21, 1998 Press Release. The SLC similarly concluded that the events that transpired at the July 20, 1998 CA Board meeting do not constitute a "red" or "yellow" flag pointing to false financial statements or revenue recognition fraud. As described above, on July 20, 1998, within sixty (60) days of the vesting of the KESOP, CA held its regular quarterly Board meeting. At that meeting, CA management told the Board that it expected CA's growth to slow in the coming months due to various factors,[197] including the Asian economic crisis and the imminent release of new mainframe hardware by IBM. This view was purportedly based upon anecdotal reports from top sales executives, with whom Mr. Kumar had just met at a CA sales conference. Mr. Wang, who had recently returned from a trip to Asia, supported this view.

It is undisputed that no member of management presented any quantitative analysis regarding CA's projected growth at this meeting. Indeed, this view conflicted with that of Mr. Zar, CA's new CFO, who had just given the Board his more positive view of CA's

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197 As noted above, the majority of the participants at the Board meeting recall that it was Mr. Kumar that identified this issue to the Board, as reflected in the minutes. Mr. Kumar recalls that Peter Schwartz raised the issue, and that he was surprised at the time. The issue of who first raised the issue is immaterial to the analysis here, as it is undisputed that it was raised by either Mr. Kumar or Mr. Schwartz and supported by Mr. Wang.

projected growth. At the urging of Mr. Grasso, and with the approval of the Board, on July 21, CA issued a press release in which it cautioned the market that "the ripple effect of the Asian economic turmoil on our multinational clients . . . coupled with deferred software purchasing decisions as customers deal with their Y2K projects and mainframe hardware transition issues, leads us to believe that our revenue and earnings growth will slow over the next several quarters." Press Release, Computer Assocs. Int'l Inc., Computer Associates Reports Record First Quarter, Operating Earnings Up 25% (July 21, 1998). On the following day, the price of CA's stock dropped by thirty-one percent (31%).

The SLC has concluded that CA management's announcement that it expected growth to slow, despite its proximity to the KESOP award, did not signal to the non-management directors that management had previously engaged, and was then engaging, in fraudulent revenue recognition practices. Even if the directors had taken a cynical view and assumed the worst of Messrs. Kumar, Schwartz, and Wang, it might have led the Board to question the timing of when they learned of the information relating to the Asian economy, which would not have led to the discovery of improper revenue recognition practices, much less a carefully concealed backdating conspiracy.

Moreover, as noted above, the CA Board was not automatically required to assume the worst of the Company's senior managers, with no grounds causing it to do so. *See Caremark*, 698 A.2d at 969 ("absent grounds to suspect deception, neither corporate boards nor senior officers can be charged with wrongdoing simply for assuming the integrity of employees and the honesty of their dealings on the company's behalf"). In the Board's view, at the time, Messrs. Kumar, Schwartz, and Wang were highly valued executives who had greatly increased shareholder value and whom the Board trusted. As such, the Board was entitled, in good faith, to believe and credit management's statements that CA's growth would slow in the future, and the timing of when management learned this information. Therefore, the SLC concludes that CA management's comments did not constitute a "red" or "yellow" flag that gave the Board notice of actual or potential revenue recognition misconduct.

The Class Action and Derivative Litigation. The plaintiffs' securities bar, however, did assume the worst of CA's management. Shortly after the July 21 press release and the resultant stock price drop, shareholders filed a series of class action lawsuits. The Board was advised, as early as August 1998, that the lawsuits claimed, among other things, that Messrs. Artzt, Kumar, and Wang knew the information disclosed in the July 21 press release at an earlier date, but did not disclose that information in order to allow the KESOP shares to vest. Nonetheless, even with the filing of these lawsuits (which did *not* allege the premature booking of revenue), there was still no "red flag" waving in the face of the Board, which they intentionally ignored.

Shortly after the suits were filed, Mr. Woghin told the Board that there was no substance to them. He specifically advised the Board that the plaintiffs in those lawsuits had alleged, in sum, that "a fraud must have occurred" because "Charles [Wang], Sanjay [Kumar] and Russ [Artzt] had a motive to keep the stock price high until their shares vested under the '95 Comp Plan, and, for that reason, wrongfully delayed in issuing the cautionary warning eventually included in the July earnings release." Mr. Woghin also reported that these "strike suits" were "garden-variety shareholder class action types," containing allegations that were "extremely thin." Mr. Woghin's notes indicate that he concluded his report by saying, "[b]ottom line is that we have been through this before. We know what to expect and how to deal with it through very effective counsel." Further, a review of the derivative complaints filed in August 1998, which directors de Vogel, Goldstein, Grasso, and Kenny would have received from Mr. Woghin because they were named as defendants, confirms Mr. Woghin's characterization of the lawsuits. The complaints, which contain no particularized factual allegations, were objectively quite "thin."

The SLC concludes that allegations in the shareholder suits, taken alone or together with the KESOP vesting and July 21 press release, did not constitute a "red" or "yellow" flag putting the Board on notice of actual or potential revenue recognition fraud. Indeed, had the Board ordered a full investigation of each of the allegations in the litigation, absent would have been an inquiry into the propriety of CA's revenue recognition practices, since no such allegation was made. As such, had the Board ordered an investigation, the harm that ultimately befell CA would not have been prevented.

b. The New Business Model[198]

CA management's proposal that CA adopt a "new business model" in May 2000, while alleged to have been a "cover-up" for financial fraud (2005 Compl. ¶¶ 52, 211), is not alleged in the 2005 Derivative Complaint to be a "red flag" to the Board that signaled revenue recognition misconduct. Nonetheless, the SLC analyzed the events surrounding its proposal and adoption to see if it was, and to gauge the Board's reaction.

As described above, Mr. Kumar presented the Board with several legitimate business reasons for moving to the new business model, including (i) providing greater visibility into CA's future revenue streams, (ii) adding greater flexibility to the terms of the Company's licensing transactions; (iii) putting an end to the hockey stick effect, whereby CA booked the vast majority of its quarterly revenue in the last few days of the quarter; and (iv)

198 At this time, the Board was comprised of directors Artzt, D'Amato, de Vogel, Grasso, Kenny, Kumar, Pieper, and Wang.

curbing the ability of CA's clients to wait until the last minute at the quarter end to execute deals in order to extract large discounts. The ratable recognition of revenue under the new business model was, in all respects, a more conservative accounting approach than the "up-front" revenue recognition model CA had historically used, as recognized by the Board. Rather than suggest misconduct, the proposal of the new business model enhanced management's credibility with the Board.

Although certain of the Criminal Defendants (Messrs. Kaplan and Rivard) have stated that the end of the 35-Day Month practice was one motive to move to the new business model, it was not the only or primary motive (and Mr. Kumar – who was the driving force behind the new business model – has told the SLC that it was not even a factor in his mind). Given the benefits to the model and the Board's undisputed lack of knowledge concerning the 35-Day Month practice, it cannot reasonably be concluded that a request to move to the new business model, standing alone, should have been viewed as a cover for a nefarious motive on the part of management. As such, the SLC concluded that the proposal of the new business model did not constitute a red or yellow flag.

Moreover, and importantly, the Board did not simply rubber-stamp management's proposal and agree to adopt the new model. The Board, recognizing that the change could result in confusion in the marketplace as to CA's financial reporting and financial performance, requested that management perform additional work to understand the presentation of CA's financials in order to ensure that the switch to the new model would be transparent to the market. It is undisputed that CA's Finance department performed a substantial amount of work for the Board to justify the switch, and that the switch was approved in October 2000 only after the Board received and considered this data, almost six (6) months later. There is simply no evidence that the Board willfully and intentionally ignored this event.

c. The April 29, 2001 New York Times Article

The SLC also examined the April 29, 2001 New York Times article as a potential red flag. As described above, the article alleged that CA: (i) implemented the new business model as a means to cover up its shrinking earnings; (ii) recognized fees associated with maintenance up front as opposed to ratably, which is required by GAAP; (iii) classified most of the fees from extended or renewed agreements as new license revenue; (iv) falsely represented its Unicenter program as a successful product when it, in fact, struggled; and (v) gave Unicenter to customers for free to enhance its appearance to Wall Street. In addition, the article also claimed that CA stood for "Creative Accounting" and that "March, June, September and December, when fiscal quarters end[ed], had thirty-five (35) days, giving the Company extra time to close sales and book revenue." Alex Berenson, *A Software Runs Out of Tricks; The Past May Haunt Computer Associates*, N.Y. Times, Apr. 29, 2001. This was the only reference to the 35-Day Month practice in the article, and it appeared in the fifth paragraph of the article.

At the outset, the SLC questioned whether the article constituted a red flag to the CA Board. On the one hand, the article articulates (albeit without specificity or attribution) allegations of accounting fraud at CA; on the other hand, the article was presented to the Board by CA management as an unfounded and unsubstantiated attack on CA instigated by the class action plaintiffs. Indeed, many of the issues raised in the article, and discussed at far greater length, were the subject of the then-pending Class Actions, and, as such, the Board had familiarity with the allegations. For example, CA's cancel/convert accounting practices were a focus of both the article and the Class Actions, and the Board was familiar with the Company's historical practices. CA's switch to the new business model and pro forma accounting was another primary focus of the article, and the Board had similarly, and recently, spent a great deal of time evaluating the model both before and after its implementation. In addition, certain members of the Board questioned Mr. Berenson's journalistic integrity, and believed that he demonstrated considerable bias, given his use of anonymous sources and that he had written several unfavorable, and in the Board's view inaccurate, articles about CA prior to the April 29 article.

As such, the Board viewed the article with a skeptical eye, and, given the context and its use of anonymous sources, it is doubtful, at most, whether this article was a "red flag" for purposes of a *Caremark* claim. Indeed, the only decision the SLC found in which press reports (there, also New York Times articles) were determined to have been a potential "red flag" to a board of directors concluded that the press reports were a "red flag" only when "taken as a whole" with other facts, including, (i) alleged internal audit reports of fraud, (ii) the director defendants' alleged personal knowledge of improper practices, (iii) a pending *qui tam* action in which particularized allegations of fraud were alleged, and (iv) an investigation by the federal government. *See McCall v. Scott*, 239 F.3d 808, 819-20 (6th Cir. 2001) (applying Delaware law). Therefore, it is unlikely that the April 29, 2001 New York Times article, without similar surrounding circumstances (which are absent here), is sufficient to constitute a "red flag" under the law.

Even so, for the sake of completeness of analysis, the SLC treated the article as a "red flag" to the Board, putting it on notice of potential revenue recognition misconduct such that it had a duty to act. Following an extended investigation of this issue, in which the SLC interviewed most of the key participants twice, the SLC concludes that in the unlikely event the article was a "red flag," the Board nonetheless addressed the article adequately under the law.

First, as noted above, on May 7, 2001, shortly after the article was published, the Board held a special meeting to discuss the article and the Company's response. The Board was advised by Mr. Kumar (who, at the time, the Board had no reason to distrust) that (i) CA had posted a written response to the allegations in the article on CA's website, (ii) the Company had received substantial support from financial analysts who regularly follow and report on the Company; (iii) CA had retained the services of a public relations consultant and a crisis management firm to aid the Company in its response to the article; (iv) management had begun efforts to form a blue ribbon panel of independent experts to review the Company's financial reporting practices; and (v) the Audit Committee would meet on May 8, 2001, to consider, independent of management, whether further action was necessary.

Second, on May 8, 2001, Dr. Kenny, then-Chair of the Audit Committee, met with representatives from CA's current and former outside auditors, KPMG and E&Y, and CA's senior management, including the CFO (Mr. Zar), head of Internal Audit (Ms. Caden), head of Financial Reporting (Mr. Kaplan), and the General Counsel (Mr. Woghin), and Scott Smith, CA's outside counsel. At this meeting, Mr. Zar addressed CA's (i) switch to the new business model and pro forma accounting, (ii) cancel/convert accounting, (iii) license/maintenance accounting and related issues related to maintenance revenue, (iv) use of reserves in connection with acquisitions, and (v) Unicenter. Mr. Zar provided support for the Company's position that the allegations made with respect to each of these issues were without basis. Further, the representatives from the accounting firms provided Dr. Kenny with assurances that they stood by their prior audit work, and that their prior audits had been performed in conformity with GAAS. While the SLC found that Dr. Kenny did not "cross-examine" Mr. Zar or the auditors, the general consensus of the attendees was that she honestly and competently investigated the issues.

In addition, according to Dr. Kenny, it was her belief that either management or the auditors would have informed her if there was anything at all to be concerned about. Instead, Messrs. Zar and Kaplan intentionally failed to raise the 35-Day Month as an issue, despite their knowledge of the practice. Near the conclusion of the meeting, Dr. Kenny first asked Mr. Zar to step out of the meeting, and asked the auditors and remaining members of management if there was anything they wanted to raise outside of Mr. Zar's presence. Both groups assured her that there were no such issues. Then, Dr. Kenny asked all of the CA employees to leave the meeting, and again asked the auditors if there was anything they wanted to raise. Again, the auditors assured her that there were no such issues.

Third, later on May 8, 2001, the Audit Committee, and remaining non-management directors, held a telephonic meeting to receive a report from Dr. Kenny on her meeting earlier in the day. Dr. Kenny made a presentation to the directors, based on notes prepared by Mr. Woghin, of the explanations and assurances that she had been given by both management and the audit firms. By all accounts, Mr. de Vogel was the most active participant on the call, asking probing questions throughout Dr. Kenny's presentation. Significantly, as reported in the minutes, Dr. Kenny reported to the directors that the "audit firms had assured her that CA had not employed any of the accounting tricks alleged in the article." While this may have overstated the assurances actually given by the auditors, neither Mr. Woghin nor Mr. Smith, who participated on this call and in the earlier meeting, corrected or qualified this statement, and the directors hearing this report took considerable comfort from this representation.

Based upon these events, the SLC concluded that the non-management Oversight Director Defendants satisfied their duty of oversight to the Company. The directors did not intentionally ignore or disregard the article.[199] Rather, the full Board met about the article, the Chair of the Audit Committee met with the outside auditors and management to address the points raised in the article, and the Audit Committee and independent directors met to decide what further action, if any, should be taken. Thus, the directors did not "utterly fail" to take action in breach of their duty of good faith.

That said, during the course of its investigation, the SLC identified an issue that was not raised in either the 2005 Derivative Complaint or the Kaufman Complaint. The SLC examined whether, as a result of Dr. Kenny's personal and professional relationship with Mr. Wang, detailed above, the steps she took in response to the article were marked by a conflict of interest such that that they amounted to a sham. Several factors led the SLC to conclude that they were not.

First, every attendee at the May 8 meeting with the accounting firms that was interviewed by the SLC stated that they believed that Dr. Kenny made a good faith attempt to understand the implications of the article. Second, Mr. Kumar had replaced Mr. Wang as CEO by this time (although he was still Executive Chairman).[200] Third, Mr. Wang was not the subject of the article, the Company and its accounting practices were. Fourth, the SLC

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199 As set forth earlier in this Report, numerous financial analysts and independent research groups published responses to the New York Times article which disagreed with the positions taken by Mr. Berenson.

200 It was reported to the SLC that, subsequently, in November 2002 when a conflict arose between Messrs. Kumar and Wang over whether Mr. Kumar should remain as CEO, Dr. Kenny adopted a neutral position instead of putting her support behind Mr. Wang.

uncovered no evidence suggesting that Dr. Kenny conducted her investigation in bad faith. Fifth, the SLC found Dr. Kenny's assertions that her relationship with Mr. Wang did not impair her ability to evaluate the allegations in the article to be honestly held and credible. *See In re J.P. Morgan Chase & Co. S'holder Litig*., 906 A.2d 808, 823 (Del. Ch. 2005) (finding that plaintiffs failed to demonstrate that a JPMC director who was also the president of a museum was not independent where "the plaintiffs state that JPMC is a significant benefactor [of the museum], but they never state how JPMC's contributions could, or did, affect the decision-making process of the president of one of the largest museums in the nation"); *Official Comm. of Unsecured Creditors of Integrated Health Servs. v. Elkins*, 2004 WL 1949290, at *10 (Del. Ch. Aug. 24, 2004) ("Our cases have determined that personal friendships, without more; outside business relationships, without more; and approving of or acquiescing in the challenged transactions, without more, are each insufficient to raise a reasonable doubt of a director's ability to exercise independent business judgment").

Thus, the SLC has concluded that Dr. Kenny's relationship with Mr. Wang did not render her efforts a sham. The SLC found that, despite her relationship with Mr. Wang, Dr. Kenny made a "genuine, good faith effort-to do her job as a director." *See ATR-Kim Eng Fin. Corp. v. Araneta*, 2006 WL 3783520, at *19 (Del. Ch. Dec. 21, 2006) ("Under Delaware law, it is fundamental that a director cannot act loyally towards the corporation unless she tries-i.e., makes a genuine, good faith effort-to do her job as a director").

Thus, in sum, the SLC's investigation failed to uncover any instances in which "red flags" of revenue recognition fraud were identified to the Board, but were nonetheless ignored. Instead, the SLC found that there were few, if any, clear notices of revenue recognition problems, and the Board adequately responded in instances where there was any indication of misconduct. It bears repeating that "Delaware law requires only diligence, not heroism." *Shaev,* 2006 WL 391931, at *6. Here, the SLC has concluded that the Oversight Director Defendants engaged in legally sufficient oversight, and will seek dismissal of this claim.

d. Reliance on Expert Advice: Accountants

In considering whether the non-management Oversight Director Defendants could be held liable for breach of their fiduciary duties of oversight during the period of fraudulent conduct, the SLC also considered the extent to which they justifiably relied on the opinions and reports of experts – here, CA's independent auditors, E&Y and then KPMG.

Under Delaware General Corporation Law § 141(e), board members are relieved from liability for damages resulting from their actions if they "rel[ied] in good faith upon the records of the corporation and upon such information, opinions, reports or statements presented to the corporation by . . . any other person[s] as to matters the [board] member reasonably believes are within such other person's professional or expert competence and who has been selected with reasonable care by or on behalf of the corporation." *See, e.g., Disney V*, 906 A.2d at 60 (the purpose of § 141(e) "is to protect directors who rely in good faith upon information presented to them from various sources, including 'any other person as to matters the member reasonably believes are within such person's professional or expert competence and who has been selected with reasonable care by and on behalf of the corporation'").

For example, in *Cantor,* 235 F. Supp. 2d at 388-89, the district court, applying Delaware law, rejected a claim alleging a breach of the duty of oversight where employees of the corporation were alleged to have prematurely booked licensing revenue, because the board relied upon its outside auditors to ensure that the company was properly recognizing revenue. The district court found that:

> Here, the Marvel board delegated the corporate accounting duties to Ernst & Young. Further, the board relied upon Ernst & Young expertise in accounting matters, such as the best method of accounting for Marvel's business. Lastly, Ernst & Young provided a clean accounting report to Marvel. As a result, the court finds that the Marvel board met its fiduciary duties with regard to accounting.

Id. at 388; *see Ash*, 2000 WL 1370341, at *9 (board's reliance on the due diligence opinions of expert accounting and financial advisors Deloitte & Touche and Bear Stearns in deciding whether to approve a merger was in good faith).

Here, the 2005 Derivative Complaint pleads no particularized facts to show that the Board's reliance on E&Y and KPMG was unreasonable or not in good faith, and is thus subject to dismissal on that ground alone. Again, notwithstanding this pleading failure, the SLC independently undertook to see if such facts nonetheless existed. They do not. The SLC has concluded that the Board's reliance on E&Y and KPMG was appropriate. The SLC found that the CA Board relied upon its independent outside auditors – two (2) highly qualified, "Big 4" accounting firms – to ensure that CA was in compliance with applicable accounting standards and that its revenue recognition practices were appropriate. At no time, either before or after SOP 97-2 came into effect, did E&Y raise the timing of CA's revenue recognition as an issue, and, to the contrary, E&Y assured the Audit Committee on five (5) occasions that it believed that CA was in compliance with its requirements. Further, both E&Y and KPMG consistently provided CA with a "clean" or "unqualified" audit report for the fiscal years during which the fraudulent conduct occurred. Likewise, there is no evidence that the Board was, or should have been, aware of the 35-Day Month practice such that the directors' reliance on the audit firms was unreasonable or in bad faith.

In short, the SLC uncovered no evidence to rebut the presumption that the Board properly relied on its outside auditors concerning the Company's accounting practice. Rather, the SLC found that the Board actually, and in good faith, relied upon nationally-recognized accounting firms that it reasonably considered were qualified to audit CA. Thus, the SLC concludes that § 141(e) provides additional support for its decision to seek dismissal of claims related to the Board's oversight of CA's revenue recognition practices.

e. Oversight and the Government Investigation

Finally, the SLC examined the CA Board's oversight through the course of the government investigation, from when the Board was first notified of its existence in February 2002 through 2003. Ms. Kaufman alleges that the Oversight Director Defendants exercised "poor or non-existent oversight" during 2002 and through the first six months of 2003 (Kaufman Compl. ¶ 64).[201]

Commencement of the Investigation in 2002. Ms. Kaufman fails to plead the existence of *any* facts regarding the government investigation or the CA Board's oversight during 2002. The Kaufman Complaint is devoid of *any* factual allegations regarding the CA Board's information and reporting systems, or "red flags" that alerted, or should have alerted, the CA Board to the obstruction of the government investigation, but were ignored during 2002. This, of course, is grounds for dismissal. *See Canadian Commercial Workers Indust. Pension Plan v. Alden*, 2006 WL 456786, at *7 (Del. Ch. Feb. 22, 2006) ("The *Caremark* section of the Amended Complaint then conclusorily avers that Defendants 'ignored their duties to the Company.' Absent supporting facts, such bald conclusions need not and will not be accepted as sufficient to survive a motion to dismiss").

[201] This claim is found only in the Kaufman Complaint. *See* Kaufman Compl. ¶¶ 102-104.

Despite this pleading failure, the SLC, during its investigation, sought to identify any potential "red flags" that could have alerted the Board to the obstruction during 2002, but found none. Further, as detailed below, the SLC found that the Board took legally adequate steps to address the government investigation throughout 2002.

The SLC found that, in February 2002, upon learning that the USAO and SEC had commenced a preliminary investigation into CA's accounting practices, the Board retained highly-qualified counsel, WLRK, to represent the Company in connection with those investigations. Within the first week after learning of the investigation, the Board received two reports from WLRK, and thereafter in 2002 received numerous additional reports from WLRK (as well as from the Company's General Counsel, Mr. Woghin). During that time, WLRK and management consistently assured the Board that the Company was cooperating fully with the investigation, that WLRK could represent both management and the Board as there was no known conflict between the two groups, and that certain issues initially raised by the USAO had been resolved in the Company's favor. The SLC found no evidence that the Board was presented with any contrary information during 2002 to suggest otherwise, and none appears in the Kaufman Complaint.

Following WLRK's retention, the firm retained PwC, another nationally-recognized accounting firm, to conduct the 532 Contract Study, among others, to address the government's revenue recognition allegations. As described above, PwC reported to the Board that "a review of 532 contracts (total value of $13 billion) produced in response to the SEC's February 26, 2002 informal document request disclosed *no evidence to indicate that CA routinely or intentionally recognized contract revenues before customer signatures were obtained*." (emphasis added). At the same time, the Board itself retained PwC to conduct the

KESOP Study. As described above, the KESOP Study was a study of the two quarters that preceded the vesting of the KESOP, which addressed five separate accounting issues for those quarters, and was designed by directors Schuetze and de Vogel to determine whether any wrongdoing had occurred during the time when CA management had the greatest motive to commit fraud. Likewise, the results of the KESOP Study provided no indication of revenue recognition fraud. The results of these studies were conveyed to the Board, and no limitation qualified their results.

In July 2002, Mr. de Vogel, a member of the Audit Committee (and a creator of the KESOP), met personally with the government in order to address its concerns with regard to the KESOP, and to hear its view with respect to the investigation. At this meeting, the government appeared to have an open mind, and the SLC has uncovered no evidence to suggest that the government provided Mr. de Vogel with any evidence of either accounting fraud or obstruction.

In sum, in response to the commencement of the government investigation, the CA Board retained highly-regarded outside counsel and an independent "Big 4" accounting firm to assist it, and certain Board members became personally involved in the Company's response to the government. The Board received numerous updates from counsel and management during 2002. There is simply no evidence that the CA Board failed to act where action was required, and the SLC concludes that the CA Board satisfied its duty of oversight during this period. *See Stone I*, 2006 WL 302558, at *2 (plaintiffs failed to "point to facts suggesting a conscious decision to take no action in response to red flags. Without these well-pled allegations, there is no possibility the defendants faced a substantial likelihood of liability").[202]

The Investigation in 2003. The Kaufman Complaint pleads the existence of events in 2003 and 2004 that could constitute "red flags" and that did alert, or should have alerted, the Board to the obstruction of the government's investigation or the underlying fraud.[203] However, prior to the filing of the Kaufman Complaint (and after), the SLC independently identified and examined these, and other events, and the Board's response.

Specifically, the SLC examined the Board's response to (i) a July 2, 2003 CA Board meeting at which the Board was told, among other things, that (a) the government had suggested that the Audit Committee conduct its own investigation and (b) that the government believed that CA's senior managers had intentionally held fiscal quarters open in order to prematurely recognize revenue from licensing agreements and (c) that three CA executives were "subjects" of the government investigation; (ii) an August 7, 2003 memo from Mr. Woghin, which, among other things, alerted the Board that the government had expressed dissatisfaction with the Company's cooperation to date; (iii) the production of the so-called "23 Boxes" in September 2003; (iv) a December 3, 2003 CA Board meeting at which the Board was

[202] On July 2, 2002, Kenneth Cron, Robert La Blanc, Alex Vieux, and Thomas Wyman were elected to the CA Board, and directors de Vogel, Grasso, Pieper, and Kenny resigned effective August 25, 2002. As such, directors de Vogel, Grasso, Pieper, and Kenny cannot be held liable for any action, or failure to act, after August 25, 2002. Directors Cron, La Blanc, and Vieux cannot be held liable for any action, or failure to act, before August 25, 2002. Mr. Wyman died on January 8, 2003, shortly after being elected to the CA Board.

[203] These events included (i) a July 2, 2003 CA Board meeting, at which Mr. Savarese recommended that the Board direct the Audit Committee to conduct an independent investigation into the Company's accounting practices, and informed the Board that Messrs. Zar, Rivard, and Silverstein were "subjects" of the government investigation; (ii) the disclosure of the "23 boxes" of documents in September 2003; (iii) the October 7, 2003 employment terminations of Messrs. Zar, Rivard, and Silverstein, and the evidence indicating accounting fraud that had been uncovered by that time; (iv) a December 3, 2003 Board meeting, at which the Board was advised that the government was investigating whether CA employees had obstructed the investigation, and (v) the guilty pleas of Messrs. Silverstein, Zar, Kaplan, and Rivard during January and April 2004. *See* Kaufman Compl. ¶¶ 6-10, 66, 75, 77-78, 81, 89-90.

told that the government was investigating possible obstruction charges; and (v) the guilty pleas of Messrs. Silverstein, Zar, Kaplan, and Rivard during January and April 2004. The SLC's analysis of these issues is discussed below.

The July 2, 2003 Board Meeting. At this meeting, as described above, Mr. Savarese reported, among other things, that: (i) in rejecting his settlement offer on behalf of CA, both the USAO and SEC "assert[ed] that they believed that senior management of the company had intentionally held quarters open and used backdated contracts to meet earnings estimates;" and (ii) the government had identified Messrs. Zar, Rivard, and Silverstein as "subjects" of the government's investigation. The Board was also told that the government had suggested that the Board begin its own investigation. However, at this time, there were no concrete allegations that any member of CA senior management was involved in revenue recognition fraud or had obstructed the government's investigation. Nonetheless, the SLC assumed, for purposes of analysis, that Mr. Savarese's report constituted a "red flag."

The non-management directors universally reported to the SLC that this meeting was the first at which there was a strong indication that the government was dissatisfied with CA's cooperation. Mr. Savarese also informed the Board that while senior management had denied any intentional wrongdoing, they acknowledged that mistakes had been made with respect to revenue recognition. No evidence was presented to the Board that senior managers had lied to, or otherwise deceived, WLRK or the government. In response to the information presented to it, the Board, at the government's suggestion, authorized the Audit Committee to conduct an independent internal investigation with respect to the government's revenue recognition allegations. The Board authorized the Audit Committee to retain independent counsel, and other independent advisors, as it saw fit, to assist with its investigation.

Thus, when presented with government allegations that were in conflict with what senior management told WLRK and the Board – with no hard evidence to support either position – the Board determined to authorize an independent investigation, conducted with the assistance of independent counsel and independent accountants, that would resolve the issue. Within three weeks of the July 2 meeting, the Audit Committee had retained, and met with, S&C in order to initiate its investigation. Two weeks after that, S&C had its first meeting with the government. This is not a case in which directors simply sat idle in the face of a "red flag"; rather, the Board took decisive steps to address the issue. As such, the SLC concludes that the Board satisfied its duty of oversight with respect to what it learned at the July 2 meeting.

The August 7, 2003 Memo. As described above, on August 7, 2003, at Mr. Schuetze's request, Mr. Woghin sent the CA Board a memo informing it that S&C had met with government representatives, and that: (i) the government "expressed dissatisfaction with both Wachtell Lipton and the company's cooperation to date," and (ii) the government "believed that the company had engaged in a systematic practice of backdating license agreements;" and (iii) the government "believed (but without offering any proof) that senior managers of the company (both current and former) had directed this practice and that it was done with the specific intent to represent falsely the company's quarterly revenues." Memorandum from Steven Woghin to the Members of the CA Board (Aug. 7, 2003).

The SLC found that the directors properly viewed this memo as "more of the same" information it had heard from Mr. Savarese at the July 2 meeting. As such, they generally believed that they had already acted with respect to this information by authorizing the Audit Committee to conduct its investigation, and believed that the investigation would address the issues raised in the memo. With respect to the issue of the Company's cooperation, the Board likewise believed that the Audit Committee investigation would address any issues that existed. While the SLC was struck by the stark nature of the memo, which plainly states the government's position, it nonetheless found that, at this time, the directors were not legally required to take further action beyond having already authorized an independent investigation, which was now beginning, only one month earlier.

The September 2003 Document Productions. Much has been made of the so-called "23 Boxes" that were produced by the Company to WLRK, and then to the government by WLRK, in September and October of 2003. Following a review and analysis of these documents, the Audit Committee concluded that contracts were, in fact, backdated. With respect to the production of the documents, neither the Board, nor the Audit Committee, was told that the documents had been compiled and concealed by Mr. Woghin, as (incorrectly) alleged by plaintiffs. To the contrary, the Board was repeatedly informed that the documents were collected in the normal course of the Company's response to government subpoenas. Nonetheless, when reviewed and analyzed, the documents evidenced a revenue recognition fraud, and, as such, were clearly a "red flag" to the Board.

The SLC found that the Audit Committee's response to these documents was timely and effective. ***First***, S&C, on behalf of the Audit Committee, engaged PwC to, among other things, image the computers of numerous current and former CA employees to obtain further documentation. ***Second,*** in the first week of October 2003, counsel to the Audit Committee interviewed sixteen (16) employees regarding the information contained in the documents, including Messrs. Kumar, Zar, Kaplan, McWade, and Ms. Caden (then-head of Internal Audit). Members of the Audit Committee personally attended the interviews of Messrs. Zar and Kumar. ***Third***, the Board held a meeting on October 7, 2003 to discuss the

Audit Committee's findings. ***Fourth***, the Audit Committee recommended that Mr. Kumar terminate the employment of Messrs. Zar, Rivard, and Silverstein, the executives in charge of the Finance, Sales Accounting, and GSO departments, respectively, who were responsible for implementing and overseeing CA's revenue recognition policies. ***Fifth***, the Audit Committee disclosed its findings to the public in a press release on October 8, 2003, announcing that CA had improperly recognized revenue from numerous licensing agreements during fiscal year 2000.[204] ***Sixth*****,** the Audit Committee caused its counsel to promptly advise the USAO and SEC of all facts and developments resulting from its investigation, which it did on October 14, 2003. Given that the Board took these steps once it had learned that there was documentary evidence demonstrating that there was a practice of backdating at CA, any claim that the Board failed to take any steps to investigate the "red flag" are without basis.

The October 20 Board Dinner. At a dinner preceding the October 21 Board meeting, Mr. Richards had a conversation with Mr. Ranieri during which he expressed apprehension to Mr. Ranieri about testifying before the SEC, and told him that his lawyers had recommended that he assert his Fifth Amendment rights. It is unclear exactly how Mr. Ranieri responded within the context of the conversation; however, Mr. Richards claims that Mr.

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204 The Kaufman Complaint states that, after being informed of the contents of the "23 Boxes," the Board members "failed to disclose any of their knowledge or information about the fraud or the ongoing conspiracy either to the Court or to the Company shareholders." Kaufman Compl. ¶72. This is plainly false. As discussed above, the October 8 press release, which is not mentioned in the Kaufman Complaint, disclosed that:

> The Audit Committee's investigation is continuing, but we have determined that CA recognized certain revenue prematurely in the fiscal year ending March 31, 2000. The committee found that a number of software contracts in that fiscal year appear to have been signed after the end of the quarter in which revenues associated with such contracts had been recognized. Those revenues should have been recognized in the quarter in which the contract was signed.

The press release also disclosed that the Company had terminated Messrs. Zar, Rivard, and Silverstein. *See* Press Release, Computer Associates Announces Preliminary Results of Board Inquiry (Oct. 8, 2003).

Ranieri said that he could not "protect" Mr. Richards if he was outside the Company, but that he could "protect him" if Mr. Richards remained "on the inside." Mr. Ranieri does not recall the conversation, but recalls that his general practice at the time was to advise CA employees of the Audit Committee's policy, which was that all employees should provide full and honest testimony and that any employee who asserted his Fifth Amendment rights and consequently failed to cooperate with the Audit Committee's investigation would be terminated.

Regardless of the precise words used, it is clear that two days later, on October 22, the Audit Committee interviewed Mr. Richards. On October 23, Mr. Richards testified before the SEC. In both his Audit Committee interview, and his testimony before the SEC, Mr. Richards provided misleading answers that implied that he did not participate in and was not aware of the 35-Day Month practice. Given that the Audit Committee interviewed Mr. Richards promptly after Mr. Ranieri's conversation with him, and that Mr. Richards ultimately testified before the SEC and did not assert his Fifth Amendment rights, the SLC concludes that the Audit Committee responded appropriately to the situation at the time. Six months later, once actual evidence was uncovered implicating Mr. Richards, the Board terminated his employment.

The December 3, 2003 Board Meeting. At a December 3, 2003 CA Board meeting, the Board was advised, for the first time, that the government had expressly questioned whether any CA employees had obstructed the government investigation. Mr. Kumar reported to the Board that, upon learning that the government was looking into possible obstruction charges, the Audit Committee, with assistance from S&C, had expanded the purview of its investigation and undertaken to investigate whether "there was any basis for concern that the Corporation had obstructed the government's investigation." Minutes if a

Meeting of the CA Board at 2 (Dec. 3, 2003). Accordingly, the Audit Committee began investigating possible instances of obstruction. The SLC concludes that, by expanding the mandate of the Audit Committee to investigate the allegation of obstruction raised by the government, the Board satisfied its duty of oversight at this time.

Thus, here again, the Board, when faced with clear red flags, took steps to fully investigate and develop the facts, and ultimately took action to address the situation. The Board did not willfully ignore events as they occurred. As such, the SLC concludes that the director defendants therefore engaged in legally sufficient oversight throughout 2003.

f. Reliance on Expert Advice: Counsel

As noted above, under § 141(e) of the Delaware General Corporation Law, directors are relieved from liability for damages resulting from their actions if they relied in good faith on experts that had been selected with reasonable care. *See, e.g., In re Cheyenne Software Inc. S'holder Litig*., 1996 WL 652765, at *2 (De. Ch. Nov. 7, 1996); *Disney V,* 906 A.2d at 59 (declining to hold compensation committee liable where they relied on opinion of expert selected with reasonable care, the issue was within expert's professional competence, and opinion was "not so deficient" as to give committee reason to question his opinion).

With respect to the government investigation, the CA Board retained, in good faith, WLRK – a nationally-recognized law firm with whom the directors had prior experience – to advise the Company in connection with the government investigation. Later, the Audit Committee independently retained, in good faith, S&C, another nationally-recognized law firm to advise it in connection with its investigation. The SLC found that the CA Board and Audit Committee actually, and in good faith, relied upon the advice given by both WLRK and S&C at each step throughout the government and the Audit Committee investigation.[205] As such, the SLC concludes that § 141(e) provides additional support for its decision to seek dismissal of claims related to the CA Board's oversight during the government investigation.

g. Exculpatory Clause Under Del. Gen. Corp. Law § 102(b)(7)

Finally, CA's Certificate of Incorporation ("Certificate") protects its directors from monetary damages in the event of a breach of the duty of care, as permitted by § 102(b)(7) of the Delaware General Corporation Law.[206] Under § 102(b)(7) and CA's Certificate, no director shall be personally liable to CA or to CA shareholders for monetary damages unless they, among other things: (i) breach their duty of loyalty, or (ii) engage in intentional misconduct, knowing violation of the law, or acts or omissions not in good faith. *See* CA Certificate ¶ Tenth. Because this claim is for a breach of the duty of loyalty, the exculpatory clause does not bar this claim on its face. *See Stone II*, 911 A.2d at 367. However, as described above, the SLC has concluded that the directors at issue did not breach their duty of loyalty in

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205 The Board also often relied upon advice from CA's in-house counsel, Steven Woghin, throughout this period. While Mr. Woghin later pled guilty to fraud and obstruction, the Board was unaware of this and thus properly relied upon Mr. Woghin, a former Department of Justice attorney.

206 CA's exculpatory clause during the period at issue is found in Paragraph Tenth of the CA Certificate. The clause closely mirrors the language of § 102(b)(7) and reads as follows:

> No director shall be personally liable to the corporation or its shareholders for monetary damages for any breach of fiduciary duty by such director as a director, except (i) for breach of the director's duty of loyalty to the corporation or its shareholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) pursuant to Section 174 of the Delaware General Corporation Law, or (iv) for any transaction from which the director derived an improper personal benefit. If the General Corporation Law of Delaware is amended after approval by the shareholders of this article to authorize corporate action further eliminating or limiting the personal liability of directors, then the liability of a director or the corporation shall be eliminated or limited to the full extent permitted by the General Corporation Law of Delaware, as so amended.

CA Certificate ¶ Tenth.

the oversight context, and did not act in bad faith. As such, the SLC concludes that the CA Board is protected by CA's exculpatory clause, and that this provides additional support for its decision to seek dismissal of this claim.

2. **The Decision to Settle**

The 2005 Derivative Complaint also alleges that, in authorizing the settlement of the Class and Derivative Actions, the Settlement Director Defendants breached their duty of care by (i) issuing 5.7 million shares of CA common stock, then-valued at $133 million, and (ii) granting releases to CA's officers and directors. This breach allegedly occurred because those directors approved the settlement without seeking contribution from the Criminal Defendants, "[n]otwithstanding their knowledge of the wrongdoing committed by the Individual [director and officer] Defendants." 2005 Compl. ¶ 86.[207] Plaintiffs allege that by the time the Court approved the settlement in December 2003, CA's Board: "(1) knew that [Ira] Zar and [David] Kaplan had lied to CA's current and former outside lawyers; (2) knew that [Steven] Woghin had engineered a cover-up by withholding key documents until after the settlement; and (3) knew that [Sanjay] Kumar was involved." 2005 Compl. ¶ 223.

Ms. Kaufman alleges further that the directors were then in possession of documents (the 23 Boxes) that "indicated that Company executives, including at least Zar, Woghin, and Kumar, systematically had violated proper accounting procedures." Kaufman Compl. ¶ 71. Plaintiffs allege that, despite this knowledge, "the current director defendants did nothing to disclose those activities . . . to prevent a fraud on the Court and the consummation of an unfair agreement to the Company." 2005 Compl. ¶ 87.

207 Ms. Kaufman similarly alleges that the Settlement Director Defendants breached their duty of care to the Company by "caus[ing] the Company to enter into unfair and improper Settlements whereby the wrongdoers were released from any liability for their harm to the Company." Kaufman Compl. ¶ 104(b).

For the reasons discussed below, the SLC has concluded that this claim should be dismissed. Primarily, this claim is infirm because its factual underpinnings are wholly erroneous. The SLC's lengthy investigation on this issue has revealed that the outside directors – at the time the settlement was authorized and approved – did not know any of the items set forth above that form the basis of plaintiffs' claim. While all these issues were actively being investigated by the Audit Committee and its counsel, these were not yet known to be true. Further, what was known by the directors – that CA had prematurely recognized revenue from numerous contracts during fiscal year 2000 – was disclosed to the public in the October 8, 2003 press release. Under the applicable legal standards, this claim should be dismissed.

(a) The Business Judgment Rule

As described above, the business judgment rule is a judicial presumption that directors and officers acted in a manner consistent with the duty of care – that is, "on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company." *Aronson,* 473 A.2d at 812; *see also Disney IV*, 907 A.2d at 755 ("[t]he presumption of the business judgment rule creates a presumption that a director acted in good faith"). The deference afforded to corporate decision-making by the business judgment rule "serves to protect and promote the role of the board as the ultimate manager of the corporation," and "'operates to preclude a court from imposing itself unreasonably on the business and affairs of a corporation.'" *Disney IV*, 907 A.2d at 746 (quoting *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 360 (Del. 1993)).

Thus, courts are typically precluded from second-guessing the substantive decisions of corporate directors, as such second-guessing would ultimately prove injurious to shareholders. *See Caremark*, 698 A.2d at 967 ("To employ a different rule – one that permitted an 'objective' evaluation of the decision – would expose directors to substantive second guessing by ill-equipped judges or juries, which would, in the long-run, be injurious to investor interests"). "Where a director *in fact exercises a good faith effort to be informed and to exercise appropriate judgment*, he or she should be deemed to satisfy fully the duty of attention." *Id.* at 968 (emphasis in original).

The business judgment rule's presumption of due care " applies when there is no evidence of 'fraud, bad faith, or self-dealing.'" *Disney IV*, 907 A.2d at 747 (quoting *Grobow v. Perot*, 539 A.2d 180, 187 (Del. 1988)). In order to overcome the presumption created by the business judgment rule, a plaintiff must prove that the defendants acted with (i) fraud, (ii) illegality, (iii) a conflict of interest, or (iv) gross negligence. *See Kahn ex rel. DeKalb Genetics Corp. v. Roberts*, 679 A.2d 460, 465 (Del. 1996); *Crescent/Mach I Partners, L.P. v. Turner*, 846 A.2d 963, 984 (Del. Ch. 2000) ("To overcome the presumption of the business judgment rule, plaintiffs bear the burden to show that the defendant directors failed to act (1) in good faith; (2) in the honest belief that the action was in the best interest of the corporation; or (3) on an informed basis").

Typically, the actions of directors will not subject them to liability for breach of the duty of care unless the plaintiff can show "gross negligence." *Growe v. Bedard*, 2004 WL 2677216, at *7 (D. Me. Nov. 23, 2004) (applying Delaware law and stating "[t]o establish a breach of the duty of due care, a plaintiff must ordinarily establish gross negligence on the part of directors") (citing *Emerald Partners v. Berlin*, 787 A.2d 85, 90 (Del. 2001)); *Benihana of Tokyo, Inc. v. Benihana, Inc.*, 891 A.2d 150, 192 (Del. Ch. 2005) ("Director liability for breaching the duty of care is predicated upon concepts of gross negligence"). Absent any of these conditions, the board's decision "will be upheld unless it cannot be 'attributed to any rational business purpose.'" *Disney IV*, 907 A.2d at 747 (quoting *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971)).

(i) There Was No Fraud, Illegality, or Conflict of Interest

The SLC has found no evidence to suggest that the decision to authorize the settlement was tainted by fraud, illegality, or a conflict of interest, and none is alleged in the 2005 Derivative Complaint.[208] As is described above, there is no evidence that any non-management members of CA's Board were aware of, or participated in, the 35-Day Month practice at any time.

The only potential conflict of interest identified by the SLC in connection with the Board's decision to authorize the settlement comes from the fact that the releases granted as part of the negotiated settlement covered the Board. However, under Delaware law, such allegations clearly do not rise to the level of a breach of the duty of loyalty. As the Delaware Court of Chancery held in *H-M Wexford LLC v. Encorp, Inc.*, 832 A.2d 129, 149 (Del. Ch. 2003), the argument that "the releases Board members received constituted a material benefit to the directors that made the settlement a self-interested transaction" does not "come up to the mark." In that case, "[t]he complaint fail[ed] to allege that anyone had sued, or even threatened suit against, the directors at the time they authorized either settlement proposal." *Id.* As such, "[b]ecause the threat of personal liability was so insubstantial, there is no force to Wexford's

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208 The 2005 Derivative Complaint does not allege this conflict. However, the Kaufman Complaint alleges that directors Artzt, D'Amato, and Ranieri were defendants "in the class action and derivative lawsuits, and, as such, faced significant personal liability under securities laws," and thus "approv[ed] unfair settlements for personal interests, to the detriment of the Company." Kaufman Compl. ¶ 35 (a) & (b). This is not accurate. Directors D'Amato and Ranieri, who sat on the class action settlement committee were not named as defendants in the Class Actions and, as such, did not face any potential liability in those lawsuits. Further, as is noted in the August 21, 2003 Board meeting minutes, which the Company provided to Ms. Kaufman, Mr. Artzt abstained from the decision to authorize the settlement and, as such, played no role in approving the settlements.

contention that, because the Settlement Agreement includes releases running in favor of the directors, those directors were 'interested' in that transaction." *Id.*[209]

In an analogous situation, the Delaware courts have also found that a Board's decision to amend a company's certificate of incorporation to include a §102(b)(7) provision, which, as discussed above, protects directors (i.e., themselves) from monetary liability arising from due care violations, is insufficient to establish director interest for the purpose of excusing pre-suit demand. In *Orloff v. Shulman*, 2005 WL 3272355, at *13 (Del. Ch. Nov. 23, 2005), the Court of Chancery stated that it "has at least twice before rejected claims of this kind, noting that they are 'but variations on the "directors suing themselves" and "participating in the wrongs" refrain.'" *Id.* at *13 (quoting *Decker v. Clausen*, Civ. 1989 WL 133617, at *2 (Del. Ch. Nov. 6, 1989)); *see also Caruana v. Saligman*, 1990 WL 212304, at *4 (Del. Ch. 1990)). The Court of Chancery expressly held that the directors' approval of the § 102(b)(7) provision, in and of itself, was insufficient to demonstrate that directors lacked the independence necessary to make a business decision as to whether to proceed with a suit challenging their actions. *See id.*

This makes perfect sense: "it is more or less universally the case that when a corporation pays value to settle a claim, it demands and receives releases in favor of its

209 The Delaware courts have also addressed the issue of director independence in the context of pre-suit demand. In this analogous situation, the courts have repeatedly held that "[i]n order to rebut the presumption of director disinterestedness and independence, a stockholder must show that the directors' self-interest materially affected their independence." *McGowan v. Ferro*, 859 A.2d 1012, 1029 (Del. Ch. 2004). "In other words, to be disqualifying, the nature of the director interest must be substantial, not merely incidental." *Id.* (quotation omitted). To adequately allege director interest sufficient to excuse pre-suit demand under Delaware law, "the complaint must allege 'specific facts establishing that the potential for liability is not a mere threat but instead may rise to a substantial likelihood." *Kohls v. Duthie*, 791 A.2d 772, 779 (Del. Ch. 2000) (citations omitted). Under this rationale, "a mere threat of personal liability resulting from one's participation as a director in approving a transaction should not suffice to sterilize a director's discretion." *Id.* at 780; *see also Guttman*, 823 A.2d at 500 (requiring a showing that "the threat of liability to the directors required to act on the demand is sufficiently substantial to cast a reasonable doubt over their impartiality" before a court will excuse pre-suit demand).

directors, officers and other agents, in order to preclude the possibility of having to defend against any additional claims arising out of the matters at issue in the settlement." *H-M Wexford*, 832 A.2d at 149. From a policy and practical standpoint, "[t]here would be little sense in a rule providing that the presence of such prophylactic measures in a settlement agreement results in that agreement being treated as an interested party transaction." *Id.* at 149-50. Thus, the mere fact that the CA Board received a release in connection with the settlement does not create a conflict.

In addition, as discussed above, the class action and derivative litigation settlements were evaluated and approved by two (2) separate committees of independent directors, established for this purpose by the Board. The class action settlement committee consisted of directors D'Amato, Lorsch, Ranieri, and Schuetze, none of whom were named as defendants in the class action litigation. The derivative settlement committee consisted of directors Lorsch, Cron, Fernandes, La Blanc, Schuetze, and Vieux, none of whom were named as defendants in the derivative litigation. Each committee was represented by separate, independent outside counsel.

Because the settlements were negotiated and approved by separate committees of independent directors, their decision to enter into a settlement on CA's behalf was not compromised by a conflict of interest, and is entitled to business judgment protection. *See In re Oracle Sec. Litig.*, 829 F. Supp. 1176, 1187 (N.D. Cal. 1993) (applying Delaware law and holding independent committees of disinterested directors' decision to settle protected by the business judgment rule, but finding that committee lacked independence because it was not advised by outside counsel); *Abramowitz v. Posner*, 513 F. Supp. 120, 127 (S.D.N.Y. 1981) (applying Delaware law and holding that "the business judgment rule may properly be invoked by disinterested directors, acting independently, even when some board members, because of their interest in the transaction, are disqualified from participating in the board's decisions"), *aff'd*, 672 F.2d 1025 (2d Cir. 1982).

Therefore, the business judgment rule will protect the Current Director Defendants from liability for their decision to authorize the settlement unless that decision was (i) the result of gross negligence, or (ii) the decision wholly lacked a rational business purpose. As described above, the SLC, in reviewing the facts and circumstances of this decision, has concluded that the Board did not commit gross negligence, and the decision was based on valid, objective business considerations. As such, the SLC will seek to have this claim dismissed.

(ii) Gross Negligence

With respect to actions of corporate fiduciaries, gross negligence has been defined as "reckless indifference to or deliberate disregard of the whole body of stockholders or actions which are without the bounds of reason." *Disney IV*, 907 A.2d at 750 (citation omitted); *see also Benihana*, 891 A.2d at 192. To show gross negligence, a plaintiff must articulate facts suggesting a "wide disparity" between the decision-making process employed by the board, and a process that would be rational. *See Guttman,* 823 A.2d at 507 n.39 ("If gross negligence means something other than negligence, pleading it successfully in a case like this requires the articulation of facts that suggest a *wide* disparity between the process the directors used to ensure the integrity of the company's financial statements and that which would have been rational") (emphasis in original). As a result, "duty of care violations are rarely found." *Disney IV*, 907 A.2d at 750.

The SLC has concluded that the facts surrounding the Board's decision to authorize the 2003 Settlement do not "suggest a *wide* disparity between the process the directors used . . . and that which would have been rational," amounting to gross negligence.

Id. (emphasis in original). As discussed above, through its investigation, the SLC found that:

- The civil litigation began in 1998, at which time Mr. Woghin advised the Board that the claims made by the plaintiffs were "extremely thin." The civil litigation continued for five years, and the Board received periodic updates regarding the litigation throughout.

- WLRK, and other outside counsel, repeatedly advised the Board that the existence of the Class Actions was an impediment to resolving the government investigation.

- At a May 13, 2003 Board meeting, Mr. Woghin advised the Board that the Company had participated in mediation with the plaintiffs with the assistance of a retired U.S. District Judge, and that the parties were unable to reach a settlement. Mr. Woghin informed the Board that he believed the Court would deny the Company's then-pending motion for summary judgment, and that the case would go to trial in the fall of 2003.

- The directors remained informed about the status of the settlement negotiations through management e-mails on the subject.

- Prior to a June 18, 2003 Board meeting, the Board received a memo from Mr. Woghin outlining the terms of a proposed settlement, and had been in e-mail contact with Mr. Kumar about the negotiations.

- At a June 18, 2003 Board meeting, David Nachman, CA's outside counsel, and Sanjay Kumar presented the proposed "global" settlement to the Board. Mr. Nachman strongly advocated that the directors agree to the settlement and provided his opinion that the settlement was a preliminary step toward resolving the government investigation. The Board formed an independent committee to evaluate the settlement.

- At a July 22, 2002 Board meeting, Mr. Nachman reported to the Board on the status of the Class Actions and the 2003 Derivative Action, and the proposed settlement. Mr. Nachman reported that while the plaintiffs had a weak case, the case would likely go to trial.

- On July 25, 2003, Mr. Woghin sent the Board a memo updating it on the status of the settlement discussions. Mr. Woghin reported that the parties to the Class Actions and 2003 Derivative Action had met with the Court, and agreed to a settlement on substantially the same terms outlined by Mr. Nachman at the June 18 Board meeting, pending Board approval.

- On August 11, 2003, James McGuire (then counsel at the law firm White & Case, and now an appellate judge) and Peter Fleming (one of New York's leading trial lawyers) were retained as counsel for the derivative and class action settlement committees, respectively.

- On August 14, 2003, Mr. Woghin sent the Board a memo announcing the members of two (2) settlement committees – one for the Class Actions and one for the 2003 Derivative Litigation – providing the resumes of counsel for the committees, and outlining the settlement process.

- On August 19, 2003, both settlement committees participated in a conference call with their respective counsel, during which the committees raised and considered the relevant issues associated with the settlements, including the necessity of the settlements being "global" and the propriety of granting releases to CA's officers and directors prior to the conclusion of the government and Audit Committee investigations.

- On August 21, 2003, the Board met again to consider, and decide upon, the settlement. Mr. Kumar again reviewed for the Board the terms of the proposed settlement, and then reviewed the actions taken by the Board with respect to the settlement to date. Directors D'Amato and Lorsch, Chairs of the class action settlement committee and the derivative settlement committee, respectively, reported to the Board regarding the review conducted by each committee and the recommendation of each committee that the Board approve the respective settlements. After a discussion, and with Messrs. Kumar and Artzt abstaining, the Board approved the settlements.[210]

- The majority of the Board understood that the settlement was final when they authorized it in August 2003. None of the Company's lawyers advised the Board to the contrary, and no lawyers raised the issue of the releases to the Board after August 2003.

The SLC has concluded that these facts do not suggest gross negligence on the part of the director defendants, but rather, demonstrates that they used a rational process designed to ensure that the Board acted on an informed and adequate basis in making its

210 Despite the fact that the Company provided Ms. Kaufman with the August 14 memo, the June 18 and August 21 Board meeting minutes, and other documents outlining the settlement process employed by the Board (pursuant to her § 220 request), Ms. Kaufman omits the following facts from her complaint: (i) the creation of the independent class action and derivative settlement committees, (ii) the committees' retention of independent counsel, and (iii) the August 19 committee meetings. Instead, Ms. Kaufman alleges that the Board approved the settlements at a "hastily called" Board meeting, at the urging of Messrs. Kumar and Woghin, without the benefit of outside counsel. Kaufman Compl. ¶¶ 7, 66. This allegation is, of course, wrong, and directly contrary to documents in the possession of Ms. Kaufman.

decision. The directors did not act with "reckless indifference to or a deliberate disregard of the whole body of stockholders." *Id.* (quotations omitted); *see also Albert v. Alex Brown Mgmt. Serv., Inc.*, 2005 WL 2130607, at * 4 (Del. Ch. Aug. 26, 2005) ("Gross negligence . . . involves a devil-may-care attitude or indifference to duty amounting to recklessness") (citation omitted).

Nor was the Board wholly uninformed of the facts. *See Van Gorkom*, 488 A.2d at 874-875 (finding breach of fiduciary duty where Board authorized sale of company after a twenty-minute presentation and two-hour deliberation, without any supporting documentation, prior notice, or input from counsel or management). The SLC believes that, when considering the entirety of the factual record, the "board has acted in a deliberate and knowledgeable way in identifying and exploring alternatives," and therefore deserves the protection of the business judgment rule. *Citron v. Fairchild Camera & Instrument Corp.*, 569 A.2d 53, 66 (Del. 1989).[211]

As noted above, plaintiffs allege that by December 2003, when the 2003 Settlement was finalized, the directors *knew* that (i) Messrs. Zar and Kaplan had lied to CA's current and former outside lawyers, (ii) Mr. Woghin had engineered a cover-up by withholding documents, and (iii) Mr. Kumar was involved in wrongdoing. Likewise, Ms. Kaufman alleged that the "23 Boxes" "indicated that Company executives, including at least Zar, Woghin and Kumar, systematically had violated proper accounting procedures." Kaufman Compl. ¶ 71. These allegations are factually incorrect.

First, as discussed above, the Board did not know if Mr. Zar had lied, but decided that he should be terminated because the accounting fraud occurred on his watch as

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211 As noted above, the SLC believes that there were several aspects of the process that could have been improved. None of these, however, render the Board's decision to approve the settlement "grossly negligent" or the result of "bad faith." *See Disney III*, 907 A.2d at 745, n.399.

CFO. Further, Mr. Kaplan resigned from CA on December 3, 2003, after refusing to be interviewed by the Audit Committee, but this did not mean that the directors "knew" that Mr. Kaplan had obstructed the government's investigation or that he had "lied" to counsel. ***Second***, the Board was never told that Mr. Woghin had withheld documents. To the contrary, the Board was told explicitly by Mr. Savarese on October 21, 2003 that the documents had been collected in the ordinary course of responding to the government's subpoenas and by S&C that WLRK had provided "good explanations" about the document collection issues. ***Third***, as is quite clear from the extensive investigation into Mr. Kumar's involvement in the fraud conducted through 2003 and 2004, and the information garnered by that investigation, the Board did not "know" that Mr. Kumar was involved in the fraud until well after the settlement was approved and finalized by the Court. As a review of the "23 Boxes" demonstrates, those documents did not implicate Mr. Kumar in the 35-Day Month. Nor did they implicate Messrs. Zar and Woghin, as alleged by Ms. Kaufman.

Thus, the only "new" information the Board had by December 2003 when the settlement was finalized was that which was announced in the October 8 press release – that there had been some form of an accounting fraud at CA. However, this was something that had been explicitly contemplated by the derivative settlement committee at the August 19 meeting. The derivative settlement committee also contemplated the possibility that evidence of wrongdoing on the part of CA's management might arise in the Audit Committee and government investigation, and nonetheless determined that it was in the best interests of the Company to go forward with the settlement.[212]

212 As discussed above, and as reflected in contemporaneous documents, the derivative settlement committee discussed the possibility of (i) deferring the settlement until after the conclusion of the Audit Committee and government investigations, or (ii) "narrowing or tailoring" the releases to

In other words, the scenario which the derivative settlement committee considered in making its decision in August 2003 had now arisen. At that time, it determined that the Company's interest in a global settlement of the civil litigation outweighed any potential benefit to pursuing claims against potential wrongdoers. That is a decision that is protected by the business judgment rule. *See Crouse-Hinds Co. v. InterNorth, Inc.*, 634 F.2d 690, 702-704 (2d Cir. 1980) (business judgment rule protects directors' failure to "reconsider" a merger agreement in light of a subsequent tender offer); *John Hancock Capital Growth Mgmt., Inc. v. Aris Corp.*, 1990 WL 126656, at *2 (Del. Ch. 1990) (business judgment rule protects the implicit rejection by the board of a bond repurchase, as a result of an earlier transaction that precluded the purchase).

Further, the reasons given by the directors as to why they did not reconsider the settlement were that: (i) despite having many top law firms advising them, no counsel ever suggested they revisit the issue and the directors assumed counsel would have advised them if they should – or ever could – re-evaluate the settlement; (ii) through December 2003, the directors had no information that led them to believe that top management (Messrs. Wang or Kumar) had been involved in any wrongdoing; and (iii) as additional negative facts arose, the benefit to shareholders of the global settlement became even greater and more apparent. Thus, the SLC found that the directors did not violate their fiduciary duties by refusing to reconsider and seeking to upset the 2003 Settlement, but rather, found the reasons given by the directors as to why they did not reconsider the settlement to be credible, reasonable, and given in good faith.

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preserve the Company's ability to pursue future action against certain individuals in the event that evidence of wrongdoing emerged.

Indeed, it is difficult to see how CA could have benefited by upsetting the global settlement to pursue claims of *de minimis* value, relative to the risk and exposure that the Company faced. Under plaintiffs' theory, one plausible outcome was that CA would abandon the global settlement, lose a multi-billion dollar jury verdict in a case scheduled for trial, but preserve claims against former executives who have, collectively, under $3 million in assets.[213] This is why the business judgment rule protects directors from ill-considered, hindsight second guessing such as that engaged in by Ms. Kaufman.

(iii) Rational Business Purpose

The SLC has also concluded that the decision to authorize the settlement was not "unintelligent" and can certainly be "attributed to a rational business purpose." *Disney IV*, 907 A.2d at 747-48; *see Khanna v. McMinn*, 2006 WL 1388744, at *23 (Del. Ch. May 9, 2006) ("'[t]his Court will not second-guess the judgment of a board of directors if it bases its decision on a rational business purpose'"). The SLC found the following with respect to the purpose underlying the Board's decision:

- Counsel advised the Board that the Class Actions and 2003 Derivative Action would go to trial, at an estimated cost of $30 to $40 million, not including the distraction to management that would result.

- The settlement extinguished liability for the Company in the Class Actions, which was estimated by counsel to be between $2 and $5 billion, in exchange for 5.7 million shares of CA stock (then-valued at $140 million) and no cash payment.

- The Board believed, based on the advice of counsel, that resolving the Civil Litigation would help resolve the government investigation by ending the cooperation between the plaintiffs' lawyers and the government.

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213 This represents the collective assets of Messrs. Zar, Rivard, and Silverstein, the only members of CA management determined to bear any amount of responsibility for the 35-Day Month practice at CA through December 2003 when the settlement was approved. As discussed above, the Board had not been presented with any evidence at that time that Messrs. Kumar or Wang were involved in the fraud, or the cover-up of the fraud.

- The derivative settlement committee considered the benefits of and the risks associated with granting the releases. Counsel advised the settlement committees that deferring the settlement or attempting to limit the releases could upset a "global" settlement of the Class Actions and 2003 Derivative Action.

Therefore, it is clear to the SLC that these were valid business considerations that the Board reasonably and honestly believed, and these considerations drove and supported the decision to authorize the settlement in 2003. These business considerations were equally compelling in December 2003 when the settlement was approved. Indeed, as noted above, if anything, the motivation to extinguish CA's civil liability as a step towards resolving the government investigation had increased. As such, the SLC has concluded that the Company has no basis to rebut the presumptions afforded by the business judgment rule, and the SLC will seek dismissal of this claim.

(iv) Reliance on Expert Advice

As discussed above, § 141(e) of the Delaware General Corporation Law relieves directors from liability if they relied in good faith upon experts who have been selected with reasonable care by or on behalf of the corporation. *See Cheyenne Software*, 1996 WL 652765, at *2 ("[D]irectors are protected from a breach of the duty of due care when the directors reasonably believe the information upon which they rely has been presented by an expert 'selected with reasonable care' and is within that person's 'professional or expert competence'"). Two qualified lawyers, Peter Fleming of Curtis Mallet and James McGuire of White & Case, advised the settlement committees. Both attorneys recommended that the committees authorize their respective settlements. In addition, at the time the "global" settlement was initially presented to the Board, Mr. Nachman advised the Board that he believed the global settlement was in the best interests of the Company and might help lead to resolution of the government investigation. This was consistent with earlier advice from WLRK that settlement of the Class Actions would be a positive step towards resolving the government investigation.[214] In sum, the Board received advice from no fewer than four separate law firms, and each of those firms advised the Board that the settlement was in the best interests of the Company. At no point in time did any counsel advise the Board that its opinion had changed.

Further, the presumption that the Board exercised proper business judgment includes the presumption that it appropriately relied on experts. *See Ash*, 2000 WL 1370341, at * 9 ("The McKesson board is entitled to the presumption that it exercised proper business judgment, including proper reliance on experts"); *Brehm*, 746 A.2d at 261 (executive compensation consultant "is presumed to be an expert on whom the Board was entitled to rely in good faith under Section 141(e) in order to be 'fully protected,'" and plaintiffs must rebut this presumption to establish director liability).

To rebut such a presumption, plaintiffs must plead "particularized facts" showing gross negligence, which includes one of the following: (i) that the directors actually did not rely on expert advice; (ii) that the reliance was not in good faith; (iii) that the directors did not reasonably believe the expert was qualified; (iv) that the directors failed to act with reasonable care in selecting the expert; (v) that the issue of the case was so obvious to the directors that regardless of expert advice, they themselves should have picked up on it, or (vi) that the decision was so unconscionable as to be wasteful or fraudulent. *See Ash,* 2000 WL 1370341, at * 9 ("Plaintiffs have not rebutted the presumption with particularized facts creating

214 To be clear, WLRK was "not asked to opine on whether the Board of Directors should approve the proposed derivative settlement" and did not do so, but did opine about the effect of a settlement on the government investigation. *See* Letter from John Savarese to Dan Murdock and Robert Bostrom (Aug. 20, 2003).

reason to believe that the McKesson board's conduct was grossly negligent"); *Brehm*, 746 A.2d at 262 (plaintiff must set "forth particularized facts creating reason to believe that the Old Board's conduct was grossly negligent" to rebut the presumption of proper reliance on an expert); *Crescent/Mach I Partners*, 846 A.2d 963 at 985 ("to overcome the presumption that the director defendants acted on an informed basis plaintiffs must show gross negligence").

Here, there are no facts to rebut the presumption afforded by the business judgment rule. *See supra* at 239-251; *Brehm*, 746 A.2d at 262. The SLC has found that the directors actually and reasonably relied in good faith on the advice of counsel in making their decision, and that the directors reasonably believed that counsel were qualified based upon the recommendation of Mr. Woghin, the attorneys' resumes,[215] the professional reputations of their respective firms, and the presentations made by the attorneys themselves.

While Mr. McGuire was originally recommended to CA by Mr. D'Amato, an interested director, the SLC found that these facts – that Mr. D'Amato recommended him for a separate matter months prior to his retention and Mr. Woghin independently contacted Mr. McGuire for this representation – do not indicate that the Board relied on Mr. McGuire in bad faith or that they failed to exercise due care in the selection of counsel. Further, Messrs. Fleming and McGuire provided the Board with a reasonably adequate basis for their conclusions, following their review of the litigation papers, information gathered from various sources knowledgeable about the litigation, consultation with other counsel, and their professional experience.

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215 The fact that, as noted above, the biography of Mr. McGuire attached to the August 14 memo was not, in fact, his biography, but the biography of a White & Case partner also named James McGuire, does not render their reliance on him unreasonable since they had no reason to suspect or believe that it was not the "correct" James McGuire. Further, the Board was comfortable with his presentation, and another White & Case partner, now U.S. District Judge Richard Holwell, also participated on the call.

Likewise, the fact that Mr. Woghin, and not the committee members themselves, selected these lawyers does not change this conclusion. *See In re Western Nat'l Corp. S'holders Litig.*, 2000 WL 710192, at * 22 (Del. Ch. May 22, 2000) (holding that in approving merger, special committee of independent directors could reasonably rely on advice of outside counsel recommended by corporation's general counsel, where outside counsel "appeared qualified" and did not have any conflicts of interest with parties to transaction). The SLC has uncovered no evidence that Mr. Woghin tried to interfere with the Board's decision-making process, or to select lawyers that would reach a certain result. Given the Board's state of knowledge at the time – there is no evidence to support any claim that it knew of wrongdoing by Mr. Woghin at this time – the SLC believes that it was not unreasonable to allow Mr. Woghin to coordinate the retention of counsel.[216]

Finally, as noted above, the decision to authorize the settlement was not so unconscionable as to be considered wasteful or fraudulent, thereby making the Board's reliance on counsel's advice unreasonable. To the contrary, as evidenced by the extensive discussions among counsel and the Board regarding the benefits and potential risks of settling, the decision required the Board to weigh multiple factors, including the substantial benefits a settlement would provide to the Company. Ultimately, the settlement did, in fact, provide substantial benefit to the Company: (i) CA's stock price rose consistently following the announcement of

216 This conclusion is in accord with the recent Chancery Court decision in *Valeant Pharm. Int'l v. Jerney*, 2007 WL 704935 (Del. Ch. Mar. 1, 2007), which discusses reliance on expert advice in the context of evaluating a decision to pay large cash bonuses to company executives for entire fairness under Delaware law. In that case, the court held that it was unreasonable for the defendant, a former director and president of a corporation, to rely on the advice given by a compensation expert for several reasons, including (i) that the expert performed earlier work for management on the same matter; (ii) that the expert provided advice on the payment of an option bonus, not a cash bonus; (iii) that the advice given by the expert was based on inflated values related to an IPO pricing and spinoff; and (iv) that the expert was chosen by an interested party – one of the company executives receiving the bonus. *Id.* While Mr. Woghin, who chose the lawyers representing the committee members in the instant case, was similarly interested, no other indicia exist to question the committee's reliance on those lawyers.

the settlement until the Audit Committee announced its preliminary findings in October 2003; (ii) the Company settled for substantially less than it would have had the Board delayed settling, and avoided a jury verdict that was potentially in the billions of dollars; (iii) the Company avoided the significant distraction to management that would have resulted from a trial; and (iv) CA has not been wholly precluded from seeking restitution from the wrongdoers (as evidenced by the Kumar settlement). Thus, the SLC concludes that the Settlement Director Defendants are entitled to the protection of § 141(e) of the Delaware Code, and that this provides a further basis for dismissal.

(1) CA's Exculpatory Clause

As discussed above, CA's Certificate protects directors from monetary damages in the event of a breach of the duty of care, as permitted by § 102(b)(7). *See supra* note 204. The SLC found no evidence that the Settlement Director Defendants breached their duty of loyalty in approving the settlement, and no such allegation was made in the 2005 Derivative Complaint. Likewise, there is no evidence that the Settlement Director Defendants engaged in intentional misconduct or knowingly violated the law.

Finally, the SLC found no evidence suggesting that the Board consciously disregarded its responsibility to the Company, or that it knew that it was making a decision based on inadequate information and deliberation, but did not care. *See Disney V,* 906 A.2d at 66 ("intentional dereliction of duty, [and] a conscious disregard for one's responsibilities" is misconduct that is "properly treated as a non-exculpable, nonindemnifiable violation of the fiduciary duty to act in good faith"); *The Litig. Trust of MDIP, Inc. v. Rapoport*, 2004 WL 3101575, at *4 (D. Del. Nov. 29, 2004) ("the underlying alleged facts must tend to show that the defendants *knew* that they were making material decisions without adequate information and without adequate deliberation, and that they simply did not care if the decisions caused the corporation and its stockholders to suffer injury or loss") (citation omitted) (emphasis in original).

Rather, as described at length above, the Board took steps in good faith to ensure that it was adequately informed with respect to the settlement, and is therefore entitled to the protections of CA's Certificate and § 102(b)(7). This further supports the SLC's decision to seek dismissal of this claim.

3. **The Kumar Decision**

The Settlement Director Defendants are also alleged to have breached their duty of care for failing to remove Mr. Kumar as CEO before it did on April 20, 2004, as a result of his then-alleged role in the accounting fraud and cover-up. Specifically, the Kaufman Complaint alleges that in early 2004, "[d]espite a wealth of evidence that the cover up was directed from the very top, the Director Defendants continued in their by now familiar – and increasingly inexplicable – blind faith in their CEO, failing to move against Kumar." Kaufman Compl. ¶ 94. For the reasons discussed below, the SLC has concluded that there is no basis for this claims.

As described in detail above, the decision as to how the Board should treat Mr. Kumar once evidence of general wrongdoing had surfaced was far from "blind" – to the contrary, it was carefully considered on several occasions. In the period of slightly more than five months – once Mr. Silverstein pled guilty on January 22 – the Board met four times concerning Mr. Kumar. Within three months after Mr. Silverstein's plea, the Board demoted him to a non-management position (on April 20, 2004), and then secured his resignation in early June, the exact action Ms. Kaufman alleges should have been taken. All of these actions were taken months prior to any action by the SEC or USAO against Mr. Kumar, which occurred in September 2004. Finally, the record is clear that the Board kept Mr. Kumar for as long as it did, and deliberated as extensively as it did, because it believed that his continued leadership was in the best interests of CA's shareholders. These deliberations, and the resulting decisions – both to refrain from taking action against Mr. Kumar and ultimately removing him – are classic business judgments.

(a) The Business Judgment Rule

The decision of the directors not to take action against Mr. Kumar in early 2004 was carefully considered and is therefore protected by the business judgment rule. *See Aronson*, 473 A.2d at 813 ("a conscious decision to refrain from acting may nonetheless be a valid exercise of business judgment and enjoy the protections of the rule"); *Rattner,* 2003 WL 22284323 at *7 ("the business judgment rule [] operates in instances of . . . a conscious decision to refrain from acting"). As a result, and as discussed above, plaintiffs must prove that the defendants acted with (i) fraud, (ii) illegality, (iii) a conflict of interest, or (iv) gross negligence in order to overcome the presumption that they acted with due care in deciding not to take action against Kumar in early 2004. *See Crescent/Mach I Partners,* 846 A.2d at 984.

In the end, this analysis is guided by concepts of gross negligence, since the SLC found no evidence that the Board's decision was tainted with fraud, illegality, or a conflict of interest. To the contrary, the decision was made by the Board's independent directors who had no interest, other than their interest in doing what was best for CA and its shareholders, in the outcome of the decision that was made with respect to Mr. Kumar's employment.

As noted above, with respect to actions of corporate fiduciaries, gross negligence has been defined as "reckless indifference to or deliberate disregard of the whole body of stockholders or actions which are without the bounds of reason." *Disney IV*, 907 A.2d at 750 (citation omitted); *see also Benihana*, 891 A.2d at 192. To show gross negligence, there must be a "wide disparity" between the decision-making process employed by the board, and a process that would be rational. *See Guttman,* 823 A.2d at 507 n. 39. The SLC has concluded that the facts surrounding the Board's decision to not take action against Mr. Kumar at the February 1, 2004 Board meeting do not "suggest a *wide* disparity between the process the directors used . . . and that which would have been rational." *Disney IV*, 907 A.2d at 750 (emphasis in original).

Following the discovery in October 2003 that there had been some form of wrongdoing at CA, the Board began gathering information regarding Mr. Kumar's possible involvement in both the accounting fraud and any effort to cover up that fraud. Among other things, (i) the Audit Committee requested a meeting with the government specifically for the purpose of obtaining information regarding Mr. Kumar's culpability, if any (which occurred on November 3, 2003), (ii) the Board inquired and received reports about the evidence against Mr. Kumar at each subsequent Board meeting (and each time counsel (both WLRK and S&C) reported that they had uncovered no evidence linking Mr. Kumar to the fraud), (iii) Mr. Schuetze requested, and Mr. Kumar provided to the Board, a report prepared by outside consultants regarding the compensation Mr. Kumar received during the period of fraudulent conduct, and (iv) the Audit Committee's investigation was "ratcheted up" in order to gain as much documentary evidence and witness testimony possible. These steps were taken prior to any action by the government against Mr. Kumar, or any CA executive.

Then, following the guilty plea of Mr. Silverstein on January 22, 2004, at which time it became clear that there had been some form of a coordinated effort to obstruct the government's investigation, the Board took several additional steps to understand what, if any, role Mr. Kumar had played in either the fraud or the cover up.

First, the same day as Mr. Silverstein's plea, the Audit Committee's counsel interviewed Mr. Kumar by telephone, who was traveling, to question him about his contacts with Mr. Silverstein. Mr. Schuetze participated in the interview personally. Mr. Kumar told the Audit Committee that he had little contact with Mr. Silverstein, and had no knowledge of the conspiracy to obstruct justice.

Second, six days later, on January 28, 2004, CA's independent directors met with Mr. Kumar to question him further regarding his involvement in the accounting fraud, and the alleged obstruction. Also on January 28, 2004, Mr. Schuetze attended a meeting with the government at which he asked the government to provide the Company with any evidence it had implicating Mr. Kumar. The government refused to provide any such evidence, but instead told Mr. Schuetze that he had "his head in the sand," with respect to Mr. Kumar, and that he should continue to investigate.

Third, Mr. Fernandes met with Mr. Kumar privately and questioned him about the 35-Day Month practice. Mr. Kumar admitted to the SLC that he lied to Mr. Fernandes and attempted to convince him that the 35-Day Month occurred because CA's controls were weak, but that ultimately, the impact of the practice was not material and thus would not be a "problem" for CA in the end.

Fourth, on February 1, 2004, the Board held a lengthy meeting at which it, (i) received a report from Mr. Schuetze regarding what the Audit Committee had learned about Mr. Kumar to date; (ii) received updates and advice from WLRK and S&C regarding what they had learned about Mr. Kumar, and the government's view with respect to Mr. Kumar (particularly that the government would not settle with CA while Mr. Kumar remained CEO), (iii) met with Mr. Kumar (without WLRK or S&C) to give him the opportunity to address the evidence against him, and answer questions from the directors, (iv) received advice from WLRK, S&C, and Covington & Burling regarding the directors' duty with respect to their decision; (v) held an executive session during which the directors outlined a plan for making their decision with respect to Mr. Kumar, and (vi) decided to take no immediate action with respect to Mr. Kumar, but to continue to monitor the situation. The record is abundantly clear that the Board questioned WLRK, S&C, and Mr. Kumar extensively concerning any evidence of Mr. Kumar's knowledge of, or participation in, the fraud. The Board also fully explored what the impact of any decision would have on the government investigation and CA as a whole. Having gathered all the relevant facts, and acting with the advice of three separate law firms, the directors decided not to take any action against Mr. Kumar at that time.

The SLC has concluded that these facts in no way suggest gross negligence on the part of the directors, but rather, demonstrates that the Board "acted in a deliberate and knowledgeable way." *Citron,* 569 A.2d at 66. The Board did not display the "devil-may-care attitude or indifference" required to show gross negligence, but instead took numerous steps to fully inform itself with respect to the facts and their duties as directors. As such, the decision not to take action against Mr. Kumar deserves the protection of the business judgment rule.

Further, the SLC found that the decision not to take action against Mr. Kumar can be attributed to a rational business purpose. *See Disney IV*, 907 A.2d at 747-8. The directors universally believed that Mr. Kumar added substantial value to CA as CEO, and were concerned that his departure would cause a major disruption to CA's business during an already turbulent time for the Company. The directors also considered the fact that CA's business had improved by that time, as reflected in CA's share price. As such, the directors approached any change to the business very cautiously. The question before the Board was whether they would do more harm by taking action than not, and it chose to wait until it had more definitive information before making such a decision. As such, the SLC found that the Board based its decisions on valid business considerations, and the decision to wait was not "unintelligent" or "irrational." *Id.*

The Board revisited the question of what to do about Mr. Kumar following the April 8 guilty pleas of Messrs. Kaplan, Rivard, and Zar. ***First,*** on April 14, 2004, Mr. Schuetze again met with the government in order to (i) report on the results of the Audit Committee's investigation to date, including that CA planned to issue a restatement, and (ii) to report on personnel issues then being addressed by the Board. ***Second,*** on April 16, 2004, Mr. Schuetze requested that S&C circulate to the Board certain documentary evidence that the Audit Committee uncovered and believed potentially implicated Mr. Kumar in the backdating conspiracy. In addition, at Mr. Vieux's request, S&C circulated to the CA Board a summary of Mr. Kumar's interview in which he addressed the documents then at issue. ***Third,*** during the week prior to an April 20, 2004 Board meeting, Mr. Schuetze met with Mr. Kumar to allow him to plead his case and question him privately regarding his knowledge of, and participation in, the 35-Day Month practice. Mr. Kumar again lied to Mr. Schuetze.

Finally, on April 20, 2004, the Board held another lengthy meeting at which (i) S&C gave a presentation updating the Board on the information the Audit Committee had gathered regarding Mr. Kumar to date, including the materials distributed to the CA Board prior to the meeting, and counseled the Board regarding its options with respect to Mr. Kumar, (ii) Mr. Kumar's attorney gave the Board a presentation on his behalf, and (iii) the Board ultimately decided to strip Mr. Kumar of executive level status and demote him from CEO to the position of "Chief Software Architect" and removed him from the Board. As discussed above, the

Board did not totally sever Mr. Kumar from the Company at this time because CA's annual customer conference, CA World, was approaching and the Board believed that it would be extremely difficult to find someone to take Mr. Kumar's place at this important customer event on such short notice.

Then, on June 4, 2004, following CA World, the Board requested and received Mr. Kumar's resignation.

Thus, ultimately, after carefully considering the newly discovered evidence and balancing several competing considerations, including the weight of the evidence and how best to transition the Company to new leadership, the Board acted against Mr. Kumar. The Settlement Director Defendants satisfied their duty of care both when they decided not to take action on February 1 and when they finally did, both in April and June. Both decisions were the product of an informed decision-making process and were grounded in a rational business purpose. These decisions are the classic business decisions – the hard calls that must be made even if they turn out different than anticipated – that are protected by the business judgment rule.

(i) CA's Exculpatory Clause

Finally, as discussed above, CA's Certificate protects the Board from monetary damages in the event of a breach of the duty of care, as permitted by § 102(b)(7). The SLC found no evidence that the Settlement Director Defendants breached their duty of loyalty – engaged in intentional misconduct or knowingly violated the law – in deciding not to take action against Mr. Kumar in February. Likewise, the SLC found no evidence suggesting that the Board consciously disregarded its responsibility to the Company, or that it knew that it was making a decision based on inadequate information and deliberation, but did not care. *See Disney V,* 906 A.2d at 66 ("intentional dereliction of duty, [and] a conscious disregard for one's responsibilities" is misconduct that is "properly treated as a non-exculpable, nonindemnifiable violation of the fiduciary duty to act in good faith"); *Rapoport*, 2004 WL 3101575, at *4 ("the underlying alleged facts must tend to show that the defendants *knew* that they were making material decisions without adequate information and without adequate deliberation, and that they simply did not care if the decisions caused the corporation and its stockholders to suffer injury or loss") (citation omitted) (emphasis in original).

Rather, as described at length above, the Board took steps in good faith to ensure that it was adequately informed with respect to the evidence against Mr. Kumar and his culpability, and is therefore entitled to the protections of CA's Certificate and § 102(b)(7). This further supports the SLC's decision to seek dismissal of this claim.

D. ***Count Four: Restitution and Unjust Enrichment***

Count four of the 2005 Derivative Complaint alleges that Messrs. Artzt, Kaplan, Kumar, McElroy, McWade, Richards, Rivard, Schwartz, Silverstein, Wang, Woghin, and Zar improperly received compensation from CA under the Company's 1991, 1995 (the KESOP) and 2000 executive compensation and incentive plans (collectively, the "Incentive Plans" or "Plans"). *See* 2005 Compl. ¶ 280. Plaintiffs allege that these defendants earned bonuses and other incentive payments by inflating the Company's earnings, revenues, and share price by issuing financial reports that they knew to be false. Plaintiffs claim that these defendants should not, in equity and good conscience, be allowed to keep the bonus and incentive compensation they received, and therefore seek restitution for the amounts paid under these Incentive Plans. *See id.* ¶¶ 281-82.

Under Delaware law, unjust enrichment is defined as "the unjust retention of a benefit to the loss of another, or the retention of money or property of another against the fundamental principles of equity and justice." *Schock*, 732 A.2d at 232 (quoting *Fleer Corp. v. Topps Chewing Gum, Inc.,* 539 A.2d 1060, 1062 (Del. 1988)); *see also HealthSouth,* 845 A.2d at 1105 (unjust enrichment violates "the fundamental principles of justice or equity and good conscience").

Restitution is the remedy for unjust enrichment, as it "serves to deprive the defendant of benefits that in equity and good conscience he ought not to keep, even though he may have received those benefits honestly in the first instance." *Schock,* 732 A.2d at 232-33 (quoting *Fleer*, 539 A.2d at 1062). To obtain restitution, it must be shown that (i) the defendant was unjustly enriched; (ii) the defendant secured a benefit; and (iii) it would be unconscionable to allow the defendant to retain that benefit. *See Schock*, 732 A.2d at 232; *HealthSouth*, 845 A.2d at 1105. It need not be shown that the defendant engaged in, or had knowledge of, wrongdoing. *See Schock*, 732 A.2d at 233; *HealthSouth*, 845 A.2d at 1105 ("restitution is permitted even when the defendant retaining the benefit is not a wrongdoer"); *Tucker v. Scrushy*, 2006 WL 37028, at *5 (Ala. Cir. Ct. Jan. 3, 2006) ("knowledge is immaterial under the law of unjust enrichment") (applying Delaware law).

For the reasons discussed herein and below, the SLC has determined that CA has a valid and viable claim for unjust enrichment against Mr. Wang for most of the shares of CA common stock awarded to him under the KESOP, which the SLC intends to pursue.[217] Further, the SLC has also determined that it has valid and viable unjust enrichment claims for incentive compensation paid to the Criminal Defendants and Mr. Schwartz under the 1991 and 2000 Plans, which the SLC also intends to pursue. As noted above, the SLC has reached settlements

217 Under New York law, unjust enrichment claims are governed by a six-year statute of limitations. Thus, certain aspects of this claim are untimely and will not be pursued. *See AmBase Corp. v. City Investing Co. Liquidating Trust*, 2002 WL 59431, at *5 (S.D.N.Y. Jan 15, 2002) (applying New York law), *aff'd*, 326 F.3d 63 (2d Cir. 2003).

with Messrs. Artzt, Kumar, and McWade pursuant to which it will seek dismissal of all claims against them. Finally, as discussed above, the SLC has determined that it is not in the Company's best interests to pursue a claim for unjust enrichment against Mr. McElroy, as the cost of litigating such a claim far outweighs any possible return that the Company would obtain. As such, the SLC will seek dismissal of this claim against Mr. McElroy.

E. ***Count Five: Corporate Waste***

Count five of the 2005 Derivative Complaint alleges that the individual defendants and the Settlement Director Defendants are liable to CA for corporate waste for (i) paying undeserved compensation to the individual defendants, (ii) approving the settlement of the Class Actions without seeking contribution from the individual defendants, and (iii) entering into the DPA with the USAO, also without seeking contribution from the individual defendants. *See* 2005 Compl. ¶ 285. The Kaufman Complaint alleges a similar claim. *See* Kaufman Compl. ¶¶ 106-110. While the 2005 Derivative Complaint generally alleges liability on the part of all Settlement Director and individual defendants, this claim can only properly be interpreted as applying to those director defendants who had the authority to, and did (i) make compensation decisions, and (ii) settle the civil and criminal litigation arising out of CA's fraudulent accounting practices.

The test for waste under Delaware law is "severe," and gives officers and directors wide latitude to exercise business judgment without facing liability for unwise decisions. *See, e.g., Glazer v. Zapata Corp*., 658 A.2d 176, 183 (Del. Ch. 1993) (finding that plaintiff is unlikely to prove waste under "severe" test, and denying injunction for failure to show probability of success on the merits). As the Delaware Supreme Court recently reiterated, "[t]o recover on a claim of corporate waste, the plaintiffs must shoulder the burden of proving that the exchange was 'so one sided that no business person of ordinary, sound judgment could conclude that the corporation has received adequate consideration.'" *Disney V*, 906 A.2d at 74 (quoting *Brehm v. Eisner*, 746 A.2d 244, 263 (Del. 2000)).

Thus, "a claim for waste will arise only in the rare, unconscionable case where directors irrationally squander or give away corporate assets." *Id.*; *see also White v. Panic*, 783 A.2d 543, 554 (Del. 2001) ("As a practical matter, a stockholder plaintiff must generally show that the board irrationally squander[ed] corporate assets – for example, where the challenged transaction served no corporate purpose or where the corporation received no consideration at all") (citations omitted). In contrast, "[i]f reasonable, informed minds might disagree on the question, then in order to preserve the wide domain over which knowledgeable business judgment may safely act, a reviewing court will not attempt to itself evaluate the wisdom of the bargain or the adequacy of the consideration." *Zapata*, 658 A.2d at 183 (citation omitted). Simply stated, "[i]f under the circumstances any reasonable person *might* conclude that the deal made sense, then the judicial inquiry ends." *Steiner v. Meyerson*, 1995 WL 441999, at *1 (Del. Ch. July 19, 1995) (emphasis added).

In the *Disney* case, the Delaware Supreme Court recently addressed the issue of waste in connection with a board's compensation decision. According to the complaint, Disney's board committed waste by permitting a lucrative severance payout to its then-president, Michael Ovitz, under the no-fault termination provision of his employment contract, when it allegedly could have contested that issue. Rather, the plaintiffs claimed, the Disney board had grounds to terminate Ovitz for cause, thereby avoiding the large payments to which Ovitz was entitled under the no-fault provision. *See Brehm*, 746 A.D.2d at 265.

In rejecting this claim, the Court of Chancery found that the plaintiffs had failed to "allege with particularity facts tending to show that *no reasonable business person* would have made the decision that the New Board made under these circumstances." *Id.* at 266 (emphasis added). The Delaware Supreme Court then upheld the dismissal, stating:

> One can understand why Disney stockholders would be upset with such an extraordinarily lucrative compensation agreement and termination payout awarded a company president who served for only a little over a year and who underperformed to the extent alleged. That said, there is a very large – though not insurmountable – burden on stockholders who believe they should pursue the remedy of a derivative suit instead of selling their stock or seeking to reform or oust these directors from office.

Id. at 267. Despite expressing concerns about "lavish executive compensation," the Court held that such decisions are left to the business judgment of directors, and though we may have "aspirations that boards of directors . . . live up to the highest standards of good corporate practices," failure to do so is not grounds for liability under Delaware law. *Id.* at 249.

This is the legal framework under which the waste claims alleged in the 2005 Derivative Complaint were analyzed by the SLC. For the reasons discussed below, including (i) the broad discretion afforded directors in making business decisions, (ii) the undisputed lack of knowledge of the non-management directors concerning the 35-Day Month practice, and (iii) the lack of evidence suggesting that those directors acted contrary to CA's best interests, the SLC will seek dismissal of this claim (except as to Mr. Wang).

1. **Payment of Undeserved Compensation**

Plaintiffs first allege that "the payment of the Underserved Compensation and Other Ill-Gotten Gains to the individual defendants . . . provided no benefit to the Company" and amounted to "a waste of corporate assets." 2005 Compl. ¶ 285; *see also* Kaufman Compl. ¶ 109. Although plaintiffs seek to hold all Current Director Defendants and individual defendants liable, this claim can only be reasonably interpreted to apply to those directors who had responsibility for the challenged employee compensation decisions.[218] However, plaintiffs identify no particular compensation decision that they challenge, apparently claiming that all compensation paid at all times amounted to waste.

Under Delaware law, "[t]o be sure, directors have the power, authority and wide discretion to make decisions on executive compensation." *Brehm*, 746 A.2d at 262 n.56 (citing 8 Del. Code § 122(5)).[219] Compensation decisions made by an independent and informed board, acting in good faith, are entitled to the protection of the business judgment rule and will not be second-guessed by courts. *See Prod. Res. Group L.L.C. v. NCT Group, Inc.*, 863 A.2d 772, 799 (Del. Ch. 2004) ("Informed decisions regarding employee compensation by independent boards are usually entitled to business judgment rule protection"); *Litt v. Wycoff*, 2003 WL 1794724, at *6 (Del. Ch. Mar. 28, 2003) ("employee compensation decisions made by a fully informed, disinterested, and independent board of directors are usually entitled to the protection of the business judgment rule").

As discussed above, the requirement that a board be informed means only that a board's decision must be based on "all material information *reasonably available*." *Van Gorkom*, 488 A.2d at 872 (emphasis added) (citation omitted); *see also Minn. Invco of RSA No. 7, Inc. v. Midwest Wireless Holdings LLC*, 903 A.2d 786, 797 (Del. Ch. 2006) ("to invoke the [business judgment] rule's protection, directors have a duty to inform themselves, prior to

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218 Thus, the claim in the 2005 Derivative Complaint against the non-director Individual Defendants – Messrs. Kaplan, McElroy, McWade, Richards, Rivard, Schwartz, Silverstein, Woghin, and Zar – who were not authorized to make such compensation decisions, is without basis, and should be dismissed.

219 Section 122(5) of the Delaware General Corporation Law provides that "[e]very corporation . . . shall have the power to . . . [a]ppoint such officers and agents as the business of the corporation requires and to pay or otherwise provide for them suitable compensation."

making a business decision, of all material information reasonably available to them") (quotation omitted).

Here, unfortunately, the material information reasonably available to the directors did *not* include the most critical data: that numerous officers were engaged in a wide-ranging fraud and obstruction. In light of this reality, the SLC has found no evidence to suggest that any of the non-management directors acted in bad faith in setting the compensation of any CA employee, or that the Board was, or should have been, aware of the 35-Day Month practice when it approved any form of compensation. To the contrary, the SLC believes that had the directors known that CA employees were involved in a fraudulent accounting scheme, the individuals involved would have had their employment terminated, and would not have received any incentive compensation. As such, the SLC believes that the non-management directors are protected by the business judgment rule, and that this claim should be dismissed. For the reasons noted above, however, the SLC will pursue this claim against Mr. Wang. As noted above, the SLC has reached settlements with Messrs. Artzt and Kumar, pursuant to which it will seek dismissal of all claims against them.

2. **Civil Litigation Settlement**

Plaintiffs next contend that the August 2003 settlement of the Class Actions and Derivative Litigation without seeking contribution amounted to corporate waste, and thereby seek to hold the Current Director Defendants and individual defendants liable. *See* 2005 Compl. ¶¶ 285-86; *see also* Kaufman Compl. ¶ 108. Again, although the 2005 Complaint generally alleges waste against all individual defendants, the decision to settle the pending litigation was the sole responsibility of the Settlement Director Defendants – Messrs. Cron, D'Amato, Fernandes, Kumar, La Blanc, Lorsch, Ranieri, Schuetze, and Vieux.[220] As such, there is no basis for a claim arising out of the decision to settle the civil litigation as against the other non-director individual defendants who did not authorize the settlement.[221]

As discussed at length above (*see* supra 378-358), the SLC has determined that CA's directors acted in a manner consistent with their duties of loyalty and due care in approving the settlement of the Class Actions and Derivative Litigation in August 2003. In connection with the settlement, the Company extinguished several billion dollars of potential liability. The approval of the settlements by the Board was supported by valid business considerations, and was the result of a deliberative process in which the Board appropriately relied on the advice of counsel. Because the SLC has concluded that the decision is protected by the business judgment rule, the SLC has likewise concluded that the decision to settle did not amount to corporate waste. Under no circumstances was this a decision that was "so one sided that no person of ordinary, sound judgment could conclude that the corporation has received adequate consideration." *Disney V*, 906 A.2d at 74 (quotation omitted). The SLC will seek dismissal of this claim as well.

3. **Decision to Enter Into the DPA**

Finally, the 2005 Complaint alleges that the Current Director Defendants and individual defendants wasted corporate assets when they agreed to settle the criminal charges against CA by entering into the DPA, which was executed on September 22, 2004, without seeking contribution. *See* 2005 Compl. ¶ 285. Although this claim again names both the

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220 Mr. Vieux was not named as a defendant in the 2005 Derivative Complaint, but is named as a defendant in the Kaufman Complaint.

221 Accordingly, this claim should be dismissed against Messrs. Artzt, de Vogel, Grasso, Kaplan, Kumar, McElroy, McWade, Pieper, Richards, Rivard, Schwartz, Silverstein, Wang, Woghin, and Zar, who did not authorize the settlement.

individual defendants and the Current Director Defendants, it can only apply to those directors who authorized CA's entry into the DPA on September 21, 2004.[222] With respect to those directors who authorized CA to enter into the DPA, the SLC has concluded that the decision to enter into the DPA without seeking contribution was motivated by rational business considerations, and cannot be considered to have been one of those "rare, unconscionable case[s] where directors irrationally squander or give away corporate assets." *Disney V*, 906 A.2d at 74. As a result, the SLC has determined that this claim should be dismissed.

As discussed above, CA itself was charged with securities fraud and obstruction of justice in connection with the 35-Day Month practice. *See* DPA ¶ 1. Under the terms of the DPA, CA, among other things, (i) accepted full responsibility for the fraudulent conduct of its officers and employees, (ii) instituted certain corporate reforms, (iii) agreed to fully cooperate with the USAO and the SEC, and (iv) paid $225 million in restitution to CA shareholders who suffered losses because of this conduct. *See* DPA ¶¶ 8, 23. In return, the USAO agreed to recommend that prosecution of CA be deferred for eighteen (18) months, after which the USAO would seek dismissal of all charges against the Company, with prejudice. *See* DPA ¶ 24. Further, the USAO agreed not to file any additional charges against CA relating to its fraudulent accounting practices. *See id.*[223]

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222 Those directors include Messrs. Artzt, Cron, D'Amato, Fernandes, La Blanc, Lorsch, Ranieri, and Schuetze. Plaintiffs' claim against Messrs. de Vogel, Grasso, Kaplan, Kumar, McElroy, McWade, Pieper, Richards, Rivard, Schwartz, Silverstein, Wang, Woghin, and Zar should be dismissed since these defendants played no role in approving the DPA.

223 CA's compliance with the terms of the DPA was to be monitored by an Independent Examiner. *See* DPA ¶ 19. On September 14, 2006, the USAO extended the term of the Independent Examiner, which would otherwise have expired on September 16, 2006, until May 1, 2007, due to outstanding issues with CA's internal accounting controls and the reorganization of its Accounting department. *See* Letter from the USAO to the Honorable I. Leo Glasser (Sept. 14, 2006).

The SLC has concluded that the Board's decision to enter into the DPA spared CA from the tremendous costs and negative publicity that would have likely resulted from a criminal prosecution and trial, regardless of the outcome. As commentators have recently noted, "[t]he reality is that few public or regulated companies can withstand the uncertainties and consequences that flow from an unresolved federal criminal indictment, much less conviction." Scott A. Resnik & Keir N. Dougall, *The Rise of Deferred Prosecution Agreements*, N.Y.L.J. Dec. 18, 2006, at 9. The decision to enter into the DPA resolved the federal criminal charges against CA without risking a criminal conviction or a prolonged, public criminal trial. Most importantly, it allowed the Company to move on, and to allow new management to focus on building a profitable software business on behalf of CA's shareholders.

Had CA been indicted, much less convicted at trial, it is possible that CA would have ceased to exist as a going-concern, given the negative publicity and business consequences resulting from such an outcome. Even in the early stages of the criminal investigation, the Board was acutely aware of the potential negative impact that a continuing government investigation and criminal litigation could have on CA's business.

The SLC has therefore concluded that the decision to enter into the DPA was not "so one sided that no business person of ordinary, sound judgment could conclude that the corporation has received adequate consideration." *See Disney V*, 906 A.2d at 74. Rather, the SLC has determined that the decision to enter into the DPA was a rational and well-advised decision, which has allowed the Company to reform its management and to emerge from the government investigation as a healthy and competitive business organization.

The decision not to seek contribution from the Criminal Defendants does not change this analysis. By this time – September 22, 2004 – five (5) CA senior executives had already pled guilty, and Messrs. Kumar and Richards had been fired from CA, criminally indicted, and were awaiting trial. Given the stakes for CA, and the posture of Mr. Kumar, the only one of the Criminal Defendants with any substantial assets – he was publicly fighting the criminal charges lodged against him at the time – it was not unreasonable to go forward with the DPA without seeking contribution. Indeed, since Mr. Kumar had been fired, CA had no leverage to compel him to contribute to a settlement, and delay in entering into the DPA could have been catastrophic for CA.

Indeed, the likely negative consequences of a continued criminal prosecution, regardless of the outcome, counseled strongly in favor of a negotiated resolution, even if such a resolution did not involve seeking contribution from the wrongdoers. In any event, the DPA preserved CA's ability to seek restitution in connection with the sentencing of the Criminal Defendants, which it is pursuing. *See* DPA ¶ 6(g) ("CA may be entitled to apply as a victim, on behalf of itself and/or its present or former shareholders, for an award of some or all of the amount of any such disgorged compensation obtained from such present and former CA officers or employees").[224] As part of a settlement with the government, Mr. Kumar has agreed to pay restitution of $52 million, which will be distributed to former CA shareholders.

The SLC is also pursuing monetary settlements from the Criminal Defendants. For example, it has already settled with Mr. Kumar and will receive a partially secured $15.25 million judgment. As such, even if the decision did constitute corporate waste (it did not), this

[224] On October 20, 2006, in connection with the sentencing of Mr. Kumar, CA submitted a Victim Impact Statement to the U.S. Department of Probation, in which it sought restitution for the costs incurred by CA as a result of Mr. Kumar's crimes. The SLC joined in this application.

claim is not yet ripe, given the avenues for recovery that the SLC is currently pursuing. *See Saito*, 2004 WL 3029876 at *5 (claim that directors breached their fiduciary duties by "failing to pursue claims for monetary redress against the former HBOC directors . . . is premature and fails to allege any harm" because "plaintiffs fail to allege that . . . Director Defendants have made a definitive decision whether to sue" these individuals); *Laties v. Wise*, 2005 WL 3501709, at *2 (Del. Ch. Dec. 14, 2005) (waste claim not ripe where "there are no allegations . . . that the directors made a definitive decision not to seek restitution").

In sum, the SLC has concluded that the waste claims alleged in the 2005 Derivative Complaint and Kaufman Complaint lack merit, and should be dismissed in all respects, except with respect to waste claims alleged against Mr. Wang in the 2005 Derivative Complaint.

F. ***Count Six: Fraud***

Count six of the 2005 Derivative Complaint alleges that the individual defendants "owed a duty of full disclosure to CA," but failed to disclose to the Company known facts regarding their misconduct and that of other CA officers, directors, and employees. 2005 Compl. ¶ 288. Plaintiffs further allege that the individual defendants intentionally, knowingly, and recklessly misrepresented CA's financial results, "thereby inducing CA's other directors to vote for, pay and incur the expense of transferring Undeserved Compensation to CA executives on the basis of false representations in amounts greater than those to which those employees were entitled." 2005 Compl. ¶¶ 289-90. For these alleged fraudulent acts, plaintiffs seek compensatory, consequential, and exemplary damages on CA's behalf. *See* 2005 Compl. ¶ 291.

Under New York law, "[t]o state a cause of action for fraud, a plaintiff must allege a representation of material fact, the falsity of the representation, knowledge by the party making the representation that it was false when made, justifiable reliance by the plaintiff and resulting injury." *Lerner v. Fleet Bank, N.A.*, 459 F.3d 273, 291 (2d Cir. 2006) (quotation omitted); *see also Schlaifer Nance & Co. v. Estate of Warhol*, 119 F.3d 91, 98 (2d Cir. 1997) ("Under New York law, for a plaintiff to prevail on a claim of fraud, he must prove five elements by clear and convincing evidence: (1) a material misrepresentation or omission of fact; (2) made with knowledge of its falsity, (3) with an intent to defraud, and (4) reasonable reliance on the part of the plaintiff, (5) that causes damages to the plaintiff").[225]

Where a fraud claim is based not on an affirmative misrepresentation but on concealment of material information, a plaintiff must also demonstrate that the defendant, as here, had a duty to disclose such information. *See Lerner*, 459 F.3d at 291-92 (citation omitted); *see also Sci. Accessories Corp. v. Summagraphics Corp.*, 425 A.2d 957, 962 (Del. 1980) (officers, directors, and "key managerial employees" have a "duty to disclose information that is relevant to the affairs of the agency entrusted to [them]"); *Potter v. Pholad*, 560 N.W.2d 389, 394 (Minn. Ct. App. 1997) (applying Delaware law and holding that "officers, as agents of the corporation, have an obligation to disclose information material to the board's ability to make an informed decision"). Regardless of whether the case is predicated on an affirmative misrepresentation or on acts of concealment, the scienter element requires proof of an "attempt to deceive," which can be demonstrated by showing "knowledge of falsity or reckless pretense

225 New York law governs plaintiffs' common law fraud claim. While the law of the state of incorporation generally governs actions arising from corporate relationships and obligations (the "internal affairs doctrine"), "[t]he tort of fraud is considered to be committed where the misrepresentation is uttered." *Aquilio v. Manaker*, Nos. 90-CV-45, 91-CV-93, 1991 WL 207473, at *6 (N.D.N.Y. Oct. 10, 1991). The conduct on which plaintiffs base their fraud claim occurred in New York, thereby requiring the application of New York law. However, the elements of a fraud claim under Delaware law mirror those under New York law, so the outcome would be the same. *See, e.g., DCV Holdings v. ConAgra, Inc.,* 2005 WL 698133, at *7 (Del. Mar. 24, 2005).

of knowledge." *Board of Educ. of Hudson City Sch. Dist. v. Sargent*, 146 A.D.2d 190, 199 (3d Dep't 1989).

Because CA has, among other things, restated its financial statements from fiscal years 2000 and 2001, and admitted as part of the DPA that it improperly recognized revenue from at least 1998 through 2001, there is no question that CA's financial statements contained misrepresentations of CA's revenue and earnings. Given the scope of the restatement and the size of the fraud, those misrepresentations are unquestionably material. Further, it is clear that the CA Board reasonably relied on the Company's publicly-reported financial statements in awarding incentive compensation to CA's officers and employees. Finally, the SLC has concluded that certain of the defendants acted with the requisite knowledge of falsity and an intent to deceive.

As such, the SLC has concluded that the Company has valid and viable fraud claims against Messrs. Kumar, Richards, Zar, Woghin, Kaplan, Rivard, and Silverstein, all of whom have admitted, in connection with their guilty pleas, that they intentionally participated in and facilitated the 35-Day Month practice, and subsequently conspired to conceal the existence of this practice from the Audit Committee and the government. Likewise, for the reasons discussed in this Report, the SLC has also determined that the Company has valid and viable claims for fraud against Messrs. Wang, Schwartz, and McWade. The SLC intends to pursue claims against all of these defendants except for Messrs. Kumar, Artzt, and McWade with whom the SLC has reached settlements, pursuant to which it will seek dismissal of all claims against them.

With respect to the CA Board members named as defendants in count six – Messrs. Artzt, de Vogel, and Grasso – as discussed above at length, the SLC has found no evidence demonstrating that the Board members knew, or were reckless in not knowing, about the 35-Day Month practice or obstruction of justice at CA. Indeed, these directors were amongst the many people misled by those at CA who had knowledge of the fraudulent activity. As such, the SLC has concluded that the Company does not have a viable claim for fraud against these individuals, and that this claim should be dismissed.

Finally, with respect to Mr. McElroy (and as discussed above), the SLC has concluded that although there may exist a facially viable claim for fraud, it is not in the Company's best interest to pursue such a claim. In addition to the considerations discussed above, for this claim to succeed, the SLC will need to demonstrate, at a minimum, that Mr. McElroy was reckless in not knowing that CA's financial statements, for which he had no responsibility, were misstated. As a result, the SLC will seek dismissal of this claim against Mr. McElroy.

G. ***Count Seven: Violations of Section 14(a) of the Exchange Act***

Count seven of the 2005 Derivative Action alleges that Messrs. Artzt, Cron, D'Amato, de Vogel, Fernandes, Kaplan, Kumar, La Blanc, Lorsch, McElroy, McWade, Ranieri, Richards, Rivard, Schuetze, Silverstein, Wang, Woghin, and Zar caused CA to file false and materially misleading proxy statements relating to (i) CA's 2002 Incentive Plan (the "2002 Plan"), issued on July 26, 2002, and (ii) CA's 2003 Compensation Plan for Non-Employee Directors (the "2003 Plan"), issued on July 21, 2003, in violation of § 14(a) of the Exchange Act, 15 U.S.C. § 78n. *See* 2005 Compl. ¶¶ 293-96. The 2002 Plan "was intended to replace future awards under the Company's 1994 Annual Incentive Compensation Plan," while the 2003 Plan "increase[d] director compensation to approximately $150,000" and provided for fifty percent (50%) of this to be paid in deferred stock, rather than options. *See id.* ¶¶ 293-94.

Plaintiffs claim that the challenged proxy statements failed to disclose (i) violations of federal securities laws; (ii) the participation of the individual defendants in these violations and the accounting manipulations; and (iii) the failure of certain individual defendants to cooperate with government authorities investigating accounting improprieties and the involvement of certain directors in the obstruction of justice. *See id.* ¶ 296. Plaintiffs further allege that the 2002 and 2003 Plans were approved by shareholders as a result of the false and misleading proxy statements, and would not have been approved if material information had been properly disclosed. *See id.* ¶¶ 295, 297.

Section 14(a) prohibits the solicitation of proxies "in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. § 78n(a). SEC Rule 14a-9 prohibits proxy solicitation "by means of any proxy statement . . . containing any statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading." 17 C.F.R. § 240.14a-9(a); *see also Koppel v. 4987 Corp.*, 167 F.3d 125, 131 (2d Cir. 1999).

To assert a viable claim under Rule 14a-9, a plaintiff must show that (i) the proxy materials contained a false or misleading statement of a material fact; (ii) that was the result of knowing, reckless or negligent conduct; and (iii) the proxy solicitation was an essential link in effecting the proposed corporate action. *See Bond Opportunity Fund v. Unilab Corp.*, 87 Fed. Appx. 772, 773 (2d Cir. 2004); *Mendell v. Greenberg*, 927 F.2d 667, 673 (2d Cir. 1991); *Vides v. Amelio*, 265 F. Supp. 2d 273, 276 (S.D.N.Y. 2003). Likewise, "the omission of information from a proxy statement will violate [section 14(a) and Rule 14a-9] if either the SEC requirements specifically require disclosure of the omitted information in a proxy statement, *or* the omission makes statements in the proxy statement materially false or misleading." *Vides*, 265 F. Supp. at 276-77 (quotation omitted).

Under § 14(a), it must only be shown that the misstatement or omission in the proxy statement was made on the basis of negligence. *See Wilson v. Great Am. Indus., Inc.*, 855 F.2d 987, 995 (2d Cir. 1988) ("Under Rule 14a-9, plaintiffs need not demonstrate that the omissions and misrepresentations resulted from knowing conduct undertaken by the director defendants with an intent to deceive" and "[l]iability can be imposed for negligently drafting a proxy statement"); *see also In re Elan Corp*., 2004 WL 1305845, at *16 (S.D.N.Y. May 18, 2004) ("pursuant to the PSLRA, Count V of the Complaint must be dismissed for failing to set forth any facts giving rise to a strong inference that the defendants acted at least negligently in misrepresenting or failing to set forth the material facts in the . . . proxy materials").

With respect to the first element of a § 14(a) claim – that the proxy statements contain a false or misleading statement of a material fact, or omit to state a material fact necessary in order to make the statement not false or misleading – the SLC concludes that the challenged proxy statements failed to disclose CA's fraudulent accounting practices and the obstruction of the government investigation by certain CA executives. *See* Computer Assocs. Int'l, Inc., Proxy Statement (Form DEF 14A) (July 26, 2002); Computer Assocs. Int'l, Inc., Proxy Statement (Form DEF 14A) (July 21, 2003). Therefore, this element of plaintiffs' § 14(a) claim is satisfied.

The next issue is whether those facts were material so as to require their disclosure. To show the materiality of the omitted facts, there must be a "substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote." *TSC*

Indus., Inc. v. Northway, Inc., 426 U.S. 438, 439 (1976). In other words, "[i]f a reasonable shareholder would have viewed disclosure of an omitted fact as having 'significantly altered the total mix of information made available' then that fact is material." *Mendell*, 927 F.2d at 673 (quotation omitted); *see also Seinfeld v. Gray*, 404 F.3d 645, 650 (2d Cir. 2005). The SLC believes that the failure to disclose information regarding its fraudulent accounting practices and the obstruction of the government investigation "significantly altered the total mix of knowledge," thereby making the omitted facts material under section 14(a). *Seinfeld*, 404 F.3d at 650 (quotation omitted).

The next issue is whether the defendants acted with the requisite culpable mental state. As noted above, the standard is negligence. *See Wilson,* 855 F.2d at 995 ("Under Rule 14a-9, plaintiffs need not demonstrate that the omissions and misrepresentations resulted from knowing conduct undertaken by the director defendants with an intent to deceive. Liability can be imposed for negligently drafting a proxy statement") (citation omitted). For those Criminal Defendants who have pled guilty – Messrs. Kumar, Richards, Zar, Rivard, Silverstein, Kaplan, and Woghin – the SLC can demonstrate that they knowingly and intentionally failed to disclose their fraudulent conduct in CA's proxy materials, and can, therefore, prove negligence (and more). As a result, the SLC has concluded that it has valid and viable claims against the Criminal Defendants for violation of § 14(a). With respect to Mr. Wang, as noted above, the SLC has concluded that he knew of, and participated in, the 35-Day Month practice. Therefore, the SLC will pursue a claim against Mr. Wang for failing to disclose his fraudulent conduct in CA's 2002 proxy statement, issued in July of that year, because he served as executive chairman through November 2002. However, because Mr. Wang left CA on November 15, 2002 and therefore was not involved in the 2003 proxy solicitation, filed with the SEC on July

21, 2003, this aspect of the claim will be dismissed. Finally, the SLC has determined that it is not in CA's best interests to pursue a claim against Mr. McElroy, as discussed previously.

As discussed at length above (*see* supra at 313-384), with respect to the directors named in count seven – Messrs. Cron, D'Amato, de Vogel, Fernandes, La Blanc, Lorsch Ranieri, and Schuetze – the SLC has uncovered no evidence that they acted knowingly, recklessly, or negligently in failing to disclose information regarding CA's fraudulent accounting practices, information which they did not have at the time these proxy statements were filed and could not have reasonably obtained. As such, the SLC has concluded that the Company does not have a viable claim for violation of § 14(a) against these Board members, and that this claim should be dismissed.

As noted above, the SLC has reached settlements with Messrs. Artzt, Kumar, and McWade pursuant to which it will seek dismissal of all claims against them.

H. ***Count Nine: Common Law Contribution and Indemnity***

Count nine of the 2005 Derivative Action seeks common law contribution and indemnification from all defendants "for the damages caused by their acts and omissions which gave rise to the claims which CA was required to pay hundreds of millions of dollars to settle." 2005 Compl. ¶ 306; *see also* Kaufman Compl. ¶¶ 111-13. The SLC has determined that claims for common law contribution against the defendants are precluded by the bar order contained in the Final Judgment, as discussed above in connection with plaintiffs' statutory contribution claim, and should be dismissed. Under New York law, however, CA is entitled to indemnification from the actual wrongdoers.[226] The SLC will pursue a claim for

[226] As discussed above, New York substantive law will apply to plaintiffs' contribution and indemnity claim. However, Delaware law regarding contribution, as codified at 10 Del. Code § 6302(a), does not differ substantially from New York law and its application would yield the same result, as described herein.

indemnification against the Criminal Defendants (except Mr. Kumar), and Messrs. Wang and Schwartz. As noted above, the SLC has reached settlements with Messrs. Artzt, Kumar, and McWade pursuant to which it will seek dismissal of all claims against them.

1. **Contribution**

Under New York law, common law "[c]ontribution may be available among joint tortfeasors who are liable for the same injuries to a third party." *In re Global Serv. Group LLC*, 316 B.R. 451, 464 (Bankr. S.D.N.Y. 2004); *see also Trump Village Section 3, Inc. v. N.Y. State Hous. Fin. Agency*, 307 A.D.2d 891, 896 (1st Dep't 2003) ("Contribution is generally available as a remedy when two or more tort-feasors share in responsibility for an injury, in violation of duties they respectively owe to the injured person") (citations omitted); *Matthews v. U.S.*, 150 F. Supp. 2d 406, 419 (E.D.N.Y. 2001). Moreover, a claim for contribution does not require that the party from whom contribution is sought to be liable under the same theory of liability, or for the same conduct. *See In re Adelphia Commc'ns Corp.*, 322 B.R. 509, 528 (Bankr. S.D.N.Y. 2005); *Raquet v. Braun*, 90 N.Y.2d 177, 183 (1997) ("contribution is available 'whether or not the culpable parties are allegedly liable for the injury under the same or different theories'") (citations omitted). However, "the source of a state law contribution claim must be an obligation imposed by state, rather than federal, law." *W.R. Grace & Co. v. Zotos Int'l,* 2005 WL 1076117, at *9 (W.D.N.Y. May 3, 2005); *see LNC Inves. V. First Fidelity Bank*, 935 F. Supp. 1333, 1340 (S.D.N.Y. 1996) ("many courts have held that the existence, scope and limitations of a right of contribution under a federal statute are governed by federal law"). Therefore, CA cannot assert a claim for contribution under state law to recover the amounts it paid to settle the federal securities laws claims contained in the Class Actions.

Further, as discussed above, the Final Judgment entered on January 5, 2004, precludes CA from seeking contribution from the "released parties":

> *whether arising under state, federal or common law*, based upon, arising out of, relating to, or in connection with the Settled Claims of the Settlement Class or any Settlement Class Member. Accordingly, to the full extent provided by the PSLRA, *the Court hereby bars any action by any person or entity, for contribution* against the Release Parties arising out of the Securities Class Actions.

Final Judgment ¶ 9 (emphasis added). This bar order specifically applies to all claims for contribution – "whether arising under state, federal or common law" – and not just those arising under the PSLRA. As described above, the "released parties" include not only the Individual defendants named in the Class Actions, but also "[t]he CA Defendants and each of their past or present subsidiaries, parents, successors, predecessors, insurers, reinsurers, officers, directors, shareholders, members, employees, agents, fiduciaries, partners, principals." *Id.* ¶ 7. Thus, it is clear that all of the individual defendants named in the 2005 Derivative Complaint are "Released Parties" under the Final Judgment in the Class Action, and therefore cannot be held liable for contribution under New York common law. The SLC will seek dismissal of this claim.

2. **Indemnification**

Unlike a claim for contribution, a claim for indemnification is not precluded by the terms of the bar order in the Final Judgment, discussed above.[227] Thus, the SLC has determined that there exists a valid and viable claim for indemnification against the Criminal Defendants, as well as against Messrs. Wang and Schwartz, all of whom the SLC believes knowingly and intentionally participated in the 35-Day Month practice, thereby causing injury to the Company. The SLC will pursue this claim.

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[227] This is consistent with the PSLRA, which requires the entry of a bar order barring contribution claims "by the settling covered person against any person, other than a person whose liability has been extinguished by the settlement of the settling covered person," but does not purport to bar claims for indemnification. *See* 15 U.S.C. 78u-4(f)(7).

Under New York law, "[i]ndemnity involves an attempt to shift the entire loss from one who is compelled to pay for a loss, without regard to his own fault, to another party who should more properly bear responsibility for that loss because it was the actual wrongdoer." *Trump*, 307 A.D.2d at 895 (quotation omitted). However, in contrast to a claim for common law contribution, "a party who has itself participated to some degree in the wrongdoing cannot receive the benefit of the common law indemnity doctrine." *Durabla Mfg. Co. v. Goodyear Tire & Rubber Co.*, 992 F. Supp. 657, 660 (S.D.N.Y. 1998) (citation omitted).

On its face, CA's admission of guilt and acceptance of responsibility in the DPA appear to implicate CA in the wrongdoing and preclude a claim for indemnification by the Company. *See* DPA ¶ 2. However, as a corporate entity, CA can act only through its agents and employees. *See Braswell v. U.S.*, 487 U.S. 99, 109-10 (1988) ("Artificial entities such as corporations may act only through their agents"). Thus, CA's participation in the 35-Day Month practice occurred only by virtue of the fraudulent conduct of its former officers and employees, and it would turn the law on its head if CA itself could not seek indemnity because their wrongful conduct is imputed to the Company. Without minimizing the Company's acceptance of responsibility under the DPA, the CA officers and employees identified above were indeed the "actual wrongdoer[s]," who "should more properly bear responsibility for" the losses suffered by CA as a result of their fraud. *Trump*, 307 A.D.2d at 895. Equitable considerations require that CA be entitled to recoup its losses from those who caused its injury. Thus, for these reasons, the SLC has concluded that there exist valid and viable common law indemnity claims against the Criminal Defendants (except Mr. Kumar with whom the SLC has reached a settlement), as well as against Messrs. Wang and Schwartz which the SLC will pursue. As noted, the SLC has reached a settlement with Mr. McWade pursuant to which it will seek dismissal of all claims against him.

XI. CONCLUSION

Throughout its exhaustive and independent investigation of the allegations in the 2005 Derivative Action and the Kaufman Complaint, the SLC was mindful that its mandate was to determine what courses of action are in the best interests of the Company. The SLC believes, after weighing all the available information, that it has reached conclusions that are truly in the best interests of CA and its shareholders. The SLC hopes that with this Report, and by taking the actions recommended herein, CA can finally put the past behind it and move on to a successful future for the benefit of all who have put their faith in CA.