

Important Decision Narrowing Federal Criminal Securities Fraud Case Against Former Chief Financial Officer of Bristol-Myers Squibb

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On March 19, 2008, five days before the scheduled commencement of trial, Judge Faith S. Hochberg of the United States District Court in Newark, New Jersey, issued an important pre-trial decision that narrowed significantly the government's criminal securities fraud case against Skadden client Frederick S. Schiff, the former chief financial officer of Bristol-Myers Squibb Company (BMS). *United States v. Schiff*, 2008 WL 726897 (D.N.J. 2008). The two-count indictment alleges that Mr. Schiff made omissions of material facts in BMS's securities filings and other forums regarding BMS's sales practice of using financial incentives to spur wholesaler purchasing and the resulting growth of its wholesalers' inventory levels. The government claimed that, when this information became known to the public, it caused a stock price drop of billions of dollars.

Judge Hochberg ruled that the government could not argue to the jury or present evidence that Mr. Schiff, who signed most of the securities filings, was liable for purported omissions in those documents. The court concluded that Mr. Schiff did not have a legal duty to disclose the allegedly omitted information, and that, absent such a duty, "non-disclosure of material information will not give rise to liability under Rule 10b-5." The court rejected the government's efforts to ground a duty of disclosure on (i) reported sales and earnings figures alleged to be misleading because of a failure to disclose the use of certain sales practices in the Management Discussion & Analysis (MD&A) section of those filings and (ii) the alleged prior misleading statements on analyst calls, which were claimed to be "all of a piece" and "in play," such that MD&A disclosure was purportedly necessary to make those earlier statements not misleading. As to the former, the court concluded that, in the absence of an allegation of improper revenue recognition, the sales and revenue figures in SEC filings cannot constitute misleading statements upon which to base omission liability. As to the latter, the court held that "[i]t defies logic to charge as a crime that an utterance in an analyst call must have other words written in a later SEC filing in order to make the utterance in the prior phone call 'not misleading.'"

The court also precluded the government from introducing evidence of the drop in BMS's stock price, which the government intended to use as proof of the materiality of the alleged omissions. Mr. Schiff contended that the government was required but failed to establish some nexus between the alleged misconduct and the drop in BMS's stock price, and moved to preclude the government's expert from testifying at trial. After a full evidentiary hearing, the court precluded the government's proffered expert testimony and any arguments or evidence about BMS's stock price drop in its case-in-chief. Conversely, the court ruled that Mr. Schiff's expert — who opined that the stock price was not in fact caused by the alleged omissions — could testify at trial to demonstrate the government's failure to prove materiality.

The government has filed a notice of appeal to the U.S. Court of Appeals for the Third Circuit.