

**INSTITUTIONAL INVESTORS AS LEAD PLAINTIFFS:  
IS THERE A NEW AND CHANGING LANDSCAPE?**

**By Max W. Berger, John P. ("Sean") Coffey and Gerald H. Silk**

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### **Introduction**

Four years ago, an institutional investor would no more have considered seeking a position as "lead plaintiff" in charge of prosecuting a securities class action lawsuit than it would have predicted that a start-up Internet company such as Yahoo! could trade at more than \$135 per share, or at almost 350 times earnings. The institutional investor's perspective changed, however, in December 1995, when Congress, over President Clinton's veto, enacted the Private Securities Litigation Reform Act (the "Reform Act")<sup>1</sup> to curb perceived abuses in securities class action litigation and to encourage institutional investors, such as public pension funds, to serve as lead plaintiffs in such cases.<sup>2</sup> The purpose of this article is to explore the lead plaintiff provisions of the Reform Act, analyze the evolving legal landscape regarding application of the Reform Act, and consider the impact of the Reform Act and caselaw on institutional investors' involvement in securities class actions.

Indeed, the recent settlements of the *In re Cendant Corporation Litigation*<sup>3</sup> demonstrate the importance of institutional investor leadership in securities class actions. There, the California Public Employees' Retirement System, the New York State Common Retirement Fund and the New York City Pension Funds, the court appointed lead plaintiffs for the class, achieved groundbreaking results. Cendant agreed to pay \$2,832,500,000 in cash – more than three times the highest recovery ever previously obtained in a securities class action, and approximately ten times the recovery in the next largest securities class action involving fraudulent financial statements – and agreed to far-reaching and, in a securities class action, unprecedented, corporate governance changes.<sup>4</sup> And Ernst & Young, the independent auditor of CUC International, Inc. (which merged in December 1997 with HFS, Inc. to become Cendant) and of Cendant's CMS subsidiary, agreed to pay \$335,000,000 in cash, which is the largest amount an accounting firm has paid to settle a securities class action. The total of the two settlements is at least \$3,167,500,000, by far the largest cash settlement ever achieved in a securities class action. The active participation of these significant shareholders undoubtedly enhanced the value of the settlements to the investor class and validated Congress' intent in enacting the Reform Act.

### **The Reform Act**

The Reform Act embodies Congress' intention to facilitate the appointment of institutions as lead plaintiffs in shareholder class action lawsuits.<sup>5</sup> In that connection, the Reform Act requires courts to adopt the presumption "that the most adequate plaintiff [to serve as a lead plaintiff] . . . is the person or group of persons that . . . in the determination of the court, has the largest financial interest in the relief sought by the class" and who "otherwise satisfies the requirements of Rule 23 of the Federal Rules of Civil Procedure."<sup>6</sup> This presumption may be rebutted only by proof that the presumptively most adequate plaintiff (1) will not fairly and adequately protect the interests of the class, or (2) is subject to unique defenses foreclosing adequate representation of the class.<sup>7</sup>

The Reform Act was intended to eliminate the widespread and well-known “race to the courthouse.”<sup>8</sup> Prior to the Reform Act, the lead plaintiff position in a securities class action was typically awarded to the first plaintiff to file a complaint against the defendant. Most of the time, control over the litigation vested in plaintiffs who had very small holdings in the defendant company and were, in turn, controlled by their lawyers, who often filed complaints within twenty-four hours of a negative announcement regarding the defendant company. In contrast, under the Reform Act, the first plaintiff to file a complaint must publish notice within twenty (20) days of such filing to identify the claims and the class and to advise class members of their right to move to serve as lead plaintiff in the action within sixty (60) days from the date of publication of the notice.<sup>9</sup> Within ninety (90) days of the publication of notice, the court is required to “appoint as lead plaintiff the member or members of the purported plaintiff class that the court determines to be the most capable of adequately representing the interests of class members . . . .”<sup>10</sup> Finally, “[t]he most adequate plaintiff shall, subject to the approval of the court, select and retain counsel to represent the class.”<sup>11</sup>

These changes were intended to give institutional plaintiffs, among others, time to assess the merits of securities cases more carefully, determine whether to prosecute a particular case, and choose the most adequate and qualified counsel for the task.<sup>12</sup> However, as explained more fully below, the “race to the courthouse” that the Reform Act intended to eliminate still exists today, only now in a different form. The new law has given many of the traditional plaintiffs’ law firms the ability to communicate early in the process with any number of shareholders by securing a single small shareholder plaintiff in a case and publishing notice, either over a news wire service, the Internet, or both, with the intent to attract responses from other shareholders. This notice publication thus acts as a massive *de facto* solicitation of plaintiffs for these law firms -- the very same firms that Congress sought to “reign in” in the securities litigation arena. The solicitation gives these firms the ability to aggregate hundreds of otherwise unaffiliated shareholders plaintiffs in an attempt to come up with the “group” with largest financial interest in a case, along with the ability to ultimately secure a position as lead counsel. In some cases, this has led to arguably absurd results. For example, in *In re Informix Corp. Securities Litigation*,<sup>13</sup> two groups of aggregated individuals (one of 979 and another of 274) competed for appointment as lead plaintiff.<sup>14</sup>

Moreover, some of the Reform Act’s fundamental goals arguably have been undermined by this new race to the courthouse. For example, the Reform Act intended that clients would seek out and choose their counsel, not, as is the case with aggregation, that counsel would seek out clients through a massive solicitation campaign. In addition, the Reform Act’s lead plaintiff provisions, which Congress drafted to “encourage institutional investors to take a more active role in securities class action lawsuits,” were intended to vest control of the litigation in the hands of the clients, not the lawyers.<sup>15</sup> Such a “group” of unrelated, aggregated individuals will have difficulty exercising any degree of meaningful control over their counsel, however.

### **Application of the Lead Plaintiff Provisions**

Although the Reform Act sets forth a number of standards for selection of lead plaintiffs, the criterion that has sparked the most controversy is the presumption that the “person or group of persons” with the largest financial interest in the case is most adequate for appointment as lead plaintiff. The courts, commentators, and the SEC all seem to agree that the interpretation of the Reform Act’s “group of persons” term is the most important open question regarding the lead plaintiff provisions. The debate centers on what Congress meant by “group of persons”

and whether the gathering of so many individuals who had little or no affiliation prior to the litigation will advance the aims Congress had in mind when it created the lead plaintiff provisions.

In several early Reform Act cases, some courts took a strict view of the Reform Act language, and refused to read into the wording of the statute a numerical limitation on how many persons could be in a group. This was particularly so in cases in which only one lead plaintiff motion was filed on behalf of a “group” of otherwise unrelated investors.<sup>16</sup> In other early cases, however, some courts took the other extreme, rejecting aggregated plaintiffs and opting for a single lead plaintiff.<sup>17</sup> In addition, in these early cases, when institutions moved to assume the role of lead plaintiff, courts were generally quick to enforce Congress’ preference for institutional investors to serve as lead plaintiffs.<sup>18</sup>

As time progressed and courts became more familiar with the Reform Act’s lead plaintiff provisions, courts began staking out positions somewhere between these two extremes, although much closer to the latter view. Concerned that some proposed lead plaintiff structures may be too complex and therefore ineffective in controlling counsel, courts have been more inclined to reject groups of large number of investors, even when no one else has filed a competing lead plaintiff motion. In *Chill v. Green Tree Financial Corp.*,<sup>19</sup> for example, the court rejected the appointment of a group of approximately 300 investors on the ground that their appointment “would threaten the interests of the class, would subvert the intent of Congress, and would be too unwieldy to allow for the just, speedy and inexpensive determination of the action.” Explaining that a case-by-case, “rule of reason” analysis is appropriate, the court instead appointed the six members of the proposed group who had the largest losses as lead plaintiffs. In this and other cases in which courts have whittled down the number of plaintiffs for the leadership role, the rationale is that the fewer the plaintiffs, the more likely they are to exercise meaningful control of the case.<sup>20</sup>

When institutional investors have been appointed lead plaintiffs in securities class actions, those appointments often came only after defeating significant challenges from other would-be, primarily non-institutional, lead plaintiff applicants. For example, in *In re Cendant Corp. Litig.*,<sup>21</sup> fifteen separate plaintiffs or plaintiff groups sought appointment as lead plaintiff despite the fact that a single group consisting of the California Public Employees’ Retirement System, the New York State Common Retirement Fund and the New York City Pension Funds (collectively, the “Public Pension Fund Group”) unquestionably had the largest financial interest in the case, suffering combined losses in excess of \$89 million.<sup>22</sup> Each of the fifteen would-be lead plaintiff groups proffered creative arguments in an attempt to unseat the Public Pension Fund Group and secure the lead plaintiff position for itself.<sup>23</sup> For example, one group argued that the determination of which group has the “largest financial interest in the relief sought by the class” should be based upon a “proportionality” analysis, *i.e.*, an investor with a net worth of \$5,000 who suffered a \$1,000 loss would be regarded as having a greater financial interest than an institution with combined assets of \$10 billion that lost \$50 million.<sup>24</sup> Other groups argued that institutions still holding investments in Cendant could not adequately represent class members who had sold their stock after the fraud was disclosed.<sup>25</sup> After a hearing on these motions, however, the Court appointed the Public Pension Fund Group as lead plaintiffs.<sup>26</sup> Interestingly, not only was the Public Pension Fund Group *not* the first to file an action in the *Cendant* case, it did not even file an action at all before moving for lead plaintiff status. The Public Pension Fund Group’s appointment was nonetheless proper because, under the Reform

Act, in order to be considered by the court for the lead plaintiff position, a plaintiff need only file a complaint *or* move to be appointed lead plaintiff.<sup>27</sup>

In *Gluck v. Cellstar Corp.*,<sup>28</sup> a group of aggregated individuals and entities (the “Group”) competed with the State of Wisconsin Investment Board (“SWIB”), an entity with the largest financial interest in the case, for the lead plaintiff position, and, in the alternative, sought appointment as co-lead plaintiff with SWIB.<sup>29</sup> Rejecting the Group’s challenge, the court in *Cellstar* found that SWIB was well-suited to adequately represent the class.<sup>30</sup> The court found that SWIB had the largest financial interest in the case and, as an institutional investor, had experience acting as a fiduciary and in investment and financial matters, both of which would benefit the class.<sup>31</sup> Interestingly, with respect to the Group’s contention that SWIB was not an adequate or typical class representative, as required by Rule 23 of the Federal Rules of Civil Procedure, the court found that “Congress clearly did not intend to burden prospective Lead Plaintiffs by requiring extensive evidentiary proof of typicality or adequacy in a ‘Reform Act’ designed to reduce the costs of securities class actions and to induce institutional investors to become Lead Plaintiffs.”<sup>32</sup>

In addition, with respect to the Group’s attempt to become a co-lead plaintiff with SWIB, the court held that, under the Reform Act’s procedures, “where the interest of one institutional investor in the litigation far exceeds the interests of other purported plaintiffs, nothing persuades the Court to appoint co-Lead Plaintiffs.”<sup>33</sup> The court found that appointing co-lead plaintiffs would frustrate “one of the principal goals” of the Reform Act, which is “to remove ‘repeat-player’ plaintiffs’ lawyers from the control of securities litigation and to vest control with large investors.”<sup>34</sup> Accordingly, the Court appointed SWIB as lead plaintiff.<sup>35</sup>

In contrast to the courts in *Cendant* and *Cellstar*, some courts have been responsive to arguments from aggregated shareholder groups seeking appointment as lead plaintiff or co-lead plaintiff with an institutional investor. For example, in *In re Oxford Health Plans, Inc. Securities Litigation*,<sup>36</sup> a case arising out of, among other things, Oxford’s financial deterioration due to its failure to disclose problems with its computer system and revenue recognition practices, the court appointed the following three *competing* plaintiffs and plaintiff groups as co-lead plaintiffs: (1) the Public Employee’s Retirement Association of Colorado (“ColPERA”), which suffered a loss of \$20 million, (2) an aggregated group of individual investors called the “Vogel Group,” who suffered a loss of \$10 million, and (3) the PBHG Fund, a private institution consisting of growth mutual funds, which had suffered a loss of approximately \$3 million.<sup>37</sup>

Declining to appoint ColPERA – the plaintiff with the largest loss of all would-be lead plaintiffs in the case -- as sole lead plaintiff, Judge Brieant noted that the language of the Reform Act “expressly contemplates the appointment of more than one lead plaintiff.”<sup>38</sup> The court found that the class could benefit from a balanced mix of individuals and institutions, and that such a structure “provides the proposed class with the substantial benefits of joint decision-making and joint funding.”<sup>39</sup> Thus, the court held that “[t]he use of multiple lead plaintiffs will best serve the interests of the proposed class . . . because such a structure will allow for pooling, not only of the knowledge and experience, but also of the resources of the plaintiffs’ counsel in order to support what could prove to be a costly and time-consuming litigation.”<sup>40</sup>

The Securities and Exchange Commission (“SEC”) has expressed its opposition to the practice of appointing competing would-be lead plaintiffs. In *Oxford Health Plans*, it submitted an *amicus curiae* brief to the court in support of ColPERA’s appointment as lead plaintiff and in

opposition to the appointment of competing would-be lead plaintiffs.<sup>41</sup> In arguing that there was no basis or precedent to support the appointment of competing groups of plaintiffs with separate counsel as co-lead plaintiffs, the SEC stated that “[a]llowing the appointment of multiple plaintiffs would disperse control of the litigation and thus undercut the objective of the [Reform] Act’s lead plaintiff provisions.”<sup>42</sup>

While courts have reduced widely varying rulings in applying the Reform Act’s lead plaintiff provisions, a truly Kafka-esque ruling threatened to yield a bizarre and wholly injudicious result in *Kensington Capital Management v. Vesta Ins. Group Inc.*<sup>43</sup> In that case, the Florida State Board of Administration and plaintiff groups consisting of aggregated individuals or entities were competing for appointment as lead plaintiff.<sup>44</sup> The court held that, because it was “unable and/or unwilling to decide between the competing plaintiff groups,” it would “do the unprecedented and declare a tie to be resolved by the tossing of a coin.”<sup>45</sup> The court also declined to appoint the institution and individual investors as co-lead plaintiffs, finding the approach taken by Judge Brieant in *Oxford Health Plans* to be “unsatisfactory.”<sup>46</sup> In a “separate coin-tossing order,” the court provided: “A designee of the Florida Group shall call ‘Heads’ or ‘Tails’ while the coin is in the air.”<sup>47</sup> Perhaps recognizing the absurdity of its decision, the court’s order specifically provided that if either party wished “to file a petition for mandamus seeking to prevent the selection of a lead plaintiff group by this method, the coin toss will be postponed pending a ruling on such petition.”<sup>48</sup> As one might expect, the parties reached an agreement to serve as co-lead plaintiffs in the case and no coin was ever tossed.

While some cases, such as *Oxford Health Plans* or *Vesta Ins. Group*, have resulted in the appointment of an additional or co-lead plaintiff or group of plaintiffs, the ability of the institution to carry out the role that Congress envisioned has not been materially diminished, and institutions can still maintain control over the prosecution of these cases. In addition, a review of more recent cases addressing the Reform Act’s lead plaintiff provisions confirms that courts are becoming increasingly less tolerant of having aggregated groups of unrelated investors as lead plaintiffs. In *Tumolo v. Cymer, Inc.*,<sup>49</sup> the court denied the motion of 339 unrelated investors to be appointed as lead plaintiffs reasoning that “the expansive number of lead plaintiffs proposed by Tumolo is inconsistent with the legislative intent behind the [Reform Act] and would likely threaten the interests of the purported future class.”<sup>50</sup> The court, recognizing that the Reform Act was enacted to “encourage a meaningful investor with a substantial stake in the litigation, preferably a large institutional investor, to initiate and control the litigation,” found that “[a] solitary or small subset of meaningful investors would likely be a much more appropriate candidate to serve as lead plaintiff in this case.”<sup>51</sup>

A similar result was met by the proposed lead plaintiffs in *In re Baan Co. Securities Litigation*.<sup>52</sup> Basing its opinion in part on an *amicus curiae* brief submitted by the SEC, the court denied an *unopposed* motion by an aggregated group consisting of 466 shareholders (represented by a subgroup of 20 shareholders designated by the entire group) for appointment as lead plaintiff.<sup>53</sup> The court found that, based upon the intent of the Reform Act, a small committee would generally be more effective and efficient than a larger, aggregated group.<sup>54</sup> The court also noted that, while the lead plaintiff decision “should be made under a rule of reason,” optimally, a lead plaintiff group should include no more than three persons and that five or six should be the upper limit.<sup>55</sup> Indeed, the Court in *Baan* stated:

The mere fact that a proposed lead plaintiff group might have the largest combined financial stake, however, does not guarantee

client control. A particular concern arises when lead plaintiff status is sought by a “group” of persons who were previously unaffiliated, each of whom has suffered modest losses, and who thus have no demonstrated incentive or ability to work together to control the litigation. The problem is worse if the members have been recruited by counsel. It ordinarily will be the case that such an assemblage will be unable to manage the litigation and control the lawyers.<sup>56</sup>

More recently, the court in *Bowman v. Legato Sys., Inc.*,<sup>57</sup> denied the motion of an aggregated group consisting of 1,000 shareholders (represented by a subgroup of 6 shareholders designated by the entire group) for appointment as lead plaintiff. Instead, the court appointed the Policeman and Fireman Retirement System of the City of Detroit, a public pension fund system that had suffered significant monetary losses, and found that Detroit “is exactly the type of lead plaintiff envisioned by Congress when it instituted the lead plaintiff requirements.”<sup>58</sup> Rejecting the aggregated group’s motion, the court held:

This Court agrees that the phrases “members” and “group of persons” must be read in the context of the overall scheme and purpose of the Reform Act. It is beyond dispute that one of the Reform Act’s primary purposes was to eradicate lawyer-driven securities fraud class actions. From this fact flows the inevitable conclusion that the Legato Group is not the type of “group” which Congress intended to act as lead plaintiff. . . . The six members of the Legato Group had no pre-existing relationship. To the contrary, it appears that the members of the Legato Group were hand picked by . . . [their lawyers] for the sole purpose of obtaining lead plaintiff status, thus conferring lead plaintiff’s counsel status on . . . [their lawyers].<sup>59</sup>

There can be little doubt that the SEC’s preference for institutional investors played a role in a recent case in Virginia where, again, the SEC filed an *amicus curiae* brief regarding competing lead plaintiff motions. In that case, *Switzenbaum v. Orbital Sciences Corp.*<sup>60</sup>, a group of seven individuals with an aggregate loss of approximately \$857,000 competed with five New York City pension funds whose losses totaled approximately \$716,000. While acknowledging that the group of seven would be the presumptive lead plaintiffs “[i]f damages alone were the only relevant consideration,” the court rejected that group as unable to offer adequate representation to the class. In addition to citing “disorder” within that group’s leadership and other shortcomings, the court expressed concern that the group had provided little information about the ties that the seven members had to each other or to the putative class. Referring to the SEC *amicus* brief, the court rejected, and criticized, the group’s alternative effort to inflate their aggregated losses by including the losses of approximately 200 other putative class members, “as if to suggest that all of them could manage the case together despite the obvious logistical impossibility of doing so.” In contrast, the court observed, the New York pension funds appeared well capable of working together, with the City’s office of corporation counsel able to monitor that the actions of the pension group and its lead counsel.

Similarly, the courts in *In re Telxon Corp. Securities Litigation*,<sup>61</sup> *In re McKessonHBOC, Inc. Securities Litigation*,<sup>62</sup> and *In re Network Associates, Inc. Securities Litigation*<sup>63</sup> rejected

motions by aggregated lead plaintiff groups. The court in *Telxon* rejected the application for lead plaintiff of a group comprised of eighteen unrelated investors named the “Alsin Group.” In addressing the scope of the term “group,” the court noted that a “group” is “a smaller, identifiable subset of a larger population, sharing a common, defining characteristic which serves to distinguish them from that larger population. The word, thus, means more than a mere random collection of unrelated individuals or things.”<sup>64</sup> Applying this definition to the use of the word in the context of the Reform Act, the court held that “the context and structure of the PSLRA evince an intent that a ‘group’ consist of more than a mere assemblage of unrelated persons who share nothing in common *other than* the twin fortuities that (1) they suffered losses and (2) they entered into retainer agreements with the same attorney or attorneys.”<sup>65</sup> After rejecting the motion of the Alsin Group, the Court appointed a group consisting of two brothers on the ground that “[a]s brothers, [they] obviously have a pre-existing relationship and a basis for acting as a collective unit.”<sup>66</sup>

In the *McKessonHBOC* litigation, numerous individual plaintiffs or groups of plaintiffs moved to be appointed lead plaintiff. As in the *Cendant* litigation, many of the movants attempted to carve out niche actions to gain a position as lead plaintiff. The court first addressed the appropriateness of “group plaintiffs.” The court framed the issue as such: “the real issue is not whether Congress meant to authorize the aggregation of unrelated plaintiffs when it passed the Reform Act. It almost certainly did not. The issue is whether the enacted language of the Reform Act allows such aggregation.”<sup>67</sup> The Court then decided to follow the *Telxon* court’s analysis of the term “group” in the Reform Act, and held that:

a ‘group’ has a meaningful relationship preceding the litigation, and is united by more than the mere happenstance of having bought the same securities. The classic example of such a group would be a partnership, which has no separate legal identity, but shares in both assets and liabilities. Other such groups might be the various subsidiaries of a corporation, or members of a family.<sup>68</sup>

Significantly, the court went on to hold that “[i]t should be clear that this narrow construction of “group of persons” definitively forecloses appointment of multiple plaintiffs (or plaintiff ‘groups’) to serve as ‘co-lead’ plaintiffs. This would simply effect an end-run around the Reform Act.”<sup>69</sup> In this regard, the court found that in determining which movant should be appointed lead plaintiff it would “construe the various group motions as alternatively moving to appoint each group’s member with the greatest financial stake in the litigation the lead plaintiff.” Ultimately, the court appointed one plaintiff, the New York State Common Retirement Fund, as sole lead plaintiff.

The Court in the *Network Associates* litigation also rejected this type of aggregation of shareholders. Indeed, the court in *Network Associates* specifically stated:

In no case has a court actually designated such an aggregation as the lead plaintiff. That would be tantamount, given the hundreds or thousands involved, to letting the class represent itself. And, there is no way such an assembly could control and manage counsel. The decisions have flat-out refused to appoint large amalgamations of unrelated persons as lead plaintiff.<sup>70</sup>



In this regard, the court held that “[a]rtificial aggregation of the type here proposed should never be allowed for any purpose, including to serve as lead plaintiff or to sponsor a subgroup as lead plaintiffs. Therefore, the Court will attempt to identify the single candidate with the largest financial interest in the litigation and vet that candidate against the requirements of the PSLRA.”<sup>71</sup>

Some aggregated groups of would-be lead plaintiffs have attempted to disqualify certain institutions from serving as lead plaintiff on the ground that these institutions are “professional plaintiffs.” Specifically, the would-be lead plaintiff groups have relied upon the section of the Reform Act restricting professional plaintiffs from serving as lead plaintiffs. That provision, entitled “Restrictions on professional plaintiffs,” provides that “[e]xcept as the Court may otherwise permit, consistent with the purpose of this section,” a person cannot serve as lead plaintiff in five or more securities class actions during any three year period.<sup>72</sup>

The Conference Report to the Reform Act defines “professional plaintiffs” as those “who own a nominal number of shares in a wide array of public companies [and who] permit lawyers readily to file abusive securities class action lawsuits.” The Conference Report then explicitly states that institutional investors are not the “professional plaintiffs” whose appointment as lead plaintiff Congress sought to restrict:

Institutional investors seeking to serve as lead plaintiff may need to exceed this limitation and do not represent the type of professional plaintiff this legislation seeks to restrict. As a result, the Conference Committee grants courts discretion to avoid the unintended consequences of disqualifying institutional investors from serving more than five times in three years. The Conference Committee does not intend for this provision to operate at cross purposes with the “most adequate plaintiff” provision.

Despite the language of the Reform Act and the Conference Report, two cases have been decided, thus far, in which the “five times in three years” lead plaintiff restriction has been applied to institutions. In *In re Telxon Corporation Securities Litigation*,<sup>73</sup> a lead plaintiff application by the Florida State Board of Administration (the “Florida SBA”) was denied in part because the court there found that the restriction applied to the institution, and barred it from serving as a lead plaintiff. The court found that while there was no authority in the Reform Act to support a blanket exemption for institutional investors, an institution seeking to be excused from the five time restriction must provide the court with a basis to do so in the particular case at hand without solely relying on its status as an institution. Focusing on the purpose of the Reform Act to put control of securities class actions in the hands of the plaintiff with the greatest financial interest in the relief sought, the court provided the following example of such a basis:

If, for instance, the Court were forced to choose between an institutional investor that had exceeded the five actions in three years rule and a single investor whose loss was dwarfed by that institutional investor, or a group of *unrelated* investors, then it certainly would be consistent with the purposes of the PSLRA to allow the institutional investor to serve as lead plaintiff, finding that the presumption arising under [the restriction] had been adequately rebutted.

Even under this holding, therefore, there are circumstances under which the would be permitted to serve as lead plaintiff even if it had already served as lead plaintiff in five securities class actions in three years. In *Telxon*, however, the Florida SBA's losses were actually less than the losses of the competing lead plaintiff applicant.

Unfortunately, the flexibility in the *Telxon* opinion was not evident in the *McKesson HBOC, Inc.*<sup>74</sup> Litigation. There, with respect to the "five times in three years" lead plaintiff restriction, the court ruled that "[t]he text of the statute contains no flat exemption for institutional investors." In that case, the Florida SBA, with losses of approximately \$185 million -- at least 2½ times greater than the losses of any other lead plaintiff applicant -- had joined with the New York State Common Retirement Fund, the Anchorage Police & Fire Retirement System and the Public School Teachers' Pension and Retirement Fund of Chicago, to become lead plaintiff. The court disqualified the Florida SBA from serving as a lead plaintiff because the Florida SBA was currently serving as a lead plaintiff in six securities fraud class actions.

Going beyond the holding in *Telxon*, the court in *McKesson* did not find that the Florida SBA's substantial losses were a sufficient basis to rebut the presumption against serving as a lead plaintiff in more that five securities class actions in a three-year period. In fact, the court found that serving as lead plaintiff in six class actions was inconsistent with Congress's goal to increase client control over plaintiff's counsel. Finding that the Florida SBA was not the only lead plaintiff applicant, that the other lead plaintiff applicants had not served as lead plaintiff in more securities class actions than the Florida SBA, or that the Florida SBA was not the only institutional investor applying for the lead plaintiff appointment, the court held that there were no "special circumstances" present to overcome the presumptive bar.

## **Conclusion**

Just as it would have been difficult for anyone to have predicted the success that a company such as Yahoo! would enjoy in the present stock market, no one ever would have thought, prior to the passage of the Reform Act, that institutions would be vested with the power and opportunity to control the securities litigation landscape, which has, unquestionably, been changed by the lead plaintiff provisions of the Reform Act. The recent settlements of the *Cendant* litigation by the Public Pension Fund Group highlight the impact that institutions can (and will) have in the securities class action arena. Just how much the securities landscape has changed, however, remains to be seen, for who knows whether institutional investors' zeal will accelerate or diminish in time. Or, for that matter, how courts will continue to rule on the thorny questions surrounding selection of a lead plaintiff where there are competing groups.

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1. Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 743, 758 (codified at 15 U.S.C. § 78u-4).

2. See H.R. REP. NO. 104-369, at 31 (1995), *reprinted in* 1995 U.S.C.C.A.N. 730 [hereinafter CONFERENCE REPORT].
3. Master File No. 98-1664 (W HW) (D. NJ).
4. Cendant also agreed to share 50% of any recovery it or its officers and directors obtained in their separate ongoing litigation against Ernst & Young.
5. See CONFERENCE REPORT at 731 (noting that Congress expressly stated that the intent of the legislation is “to increase the likelihood that parties with significant holdings in issuers, whose interests are more strongly aligned with the class of shareholders, will participate in the litigation and exercise control over the selection and actions of plaintiff’s counsel”).
6. 15 U.S.C. § 78u-4(a)(3)(B)(iii)(I).
7. See *id.* § 78u-4(a)(3)(B)(iii)(II).
8. See CONFERENCE REPORT at 732.
9. 15 U.S.C. § 78u-4(a)(3)(A)(i)(I)-(II).
10. *Id.* § 78u-4(a)(3)(B)(i)(I).
11. *Id.* § 78u-4(a)(3)(B)(v).
12. See CONFERENCE REPORT at 731-33.
13. No. C-97-1289-SBA (N.D. Cal. Oct. 17, 1997).
14. See *id.* at 3-4 n.2.
15. CONFERENCE REPORT at 733-34.
16. See, e.g., *In re Ride, Inc. Securities Litigation*, C-97-20059RMW (N.D. Cal. 1997) (“On its face this language calls for aggregation. Any suggestion to the contrary, based on legislative history, cannot prevail against the statute’s plain wording.”); *In re Read-Rite Corp. Securities Litigation*, 1997 WL 405668 (D. Minn. Apr. 3, 1997) (“Although the plain language of the Act does not expressly allow or prohibit such a pooling of shares, nothing in the text prevents the aggregation of shares by the Proposed Lead Plaintiffs to constitute the largest financial interest.”); *D’Hondt v. Digital, Inc.*, 1997 WL 405668 (D. Minn. Apr. 3, 1997) (“In our view, when, as here, the putative class may total in the hundreds of thousands, if not millions, an arbitrary limit on the number of proposed Lead Plaintiffs would be unrealistic, if not wholly unproductive.”).
17. See, e.g., *In re Donnkenny Inc. Securities Litigation*, 171 F.R.D. 156 (S.D.N.Y. 1997) (“To allow an aggregation of unrelated plaintiffs to serve as lead plaintiff defeats the purpose of choosing a lead plaintiff”).
18. See, e.g., *Gluck v. Cellstar Corp.*, 976 F. Supp. 542 (N.D. Tex. 1997) (“[Wh]ere the interest of one institutional investor in the litigation far exceeds the interests of the other purported plaintiffs, nothing persuades the Court to appoint co-lead plaintiffs”).
19. 181 F.R.D. 398 (D. Minn. 1998).

20. See, e.g., *In re Advanced Tissue Sciences Securities Litigation*, 184 F.R.D. 346 (S.D.Cal. 1998) (each competing group consisted entirely of hundreds of unrelated individual investors; noting that neither group contained a pension fund or institutional investor, court rejected each group and exercised supervisory authority to select sub-group of six investors offered as alternative for lead plaintiffs).
21. 182 F.R.D. 144 (D.N.J. 1998).
22. See *id.* at 146-47.
23. See *id.* at 147.
24. *Id.*
25. See *id.*
26. See *id.* at 146.
27. See 15 U.S.C. § 78u-4(a)(3)(B)(iii)(I)(aa)-(cc).
28. 976 F. Supp. 542 (D. Tex. 1997).
29. See *id.* at 545.
30. See *id.* at 546-50.
31. See *id.* at 546.
32. *Id.*
33. *Id.* at 550.
34. *Id.* at 549.
35. See *id.* at 550.
36. 182 F.R.D. 42 (S.D.N.Y. 1998).
37. See *id.* at 44-45.
38. *Id.* at 47.
39. *Id.* at 45.
40. *Id.* at 46.
41. See Memorandum of the Securities and Exchange Commission, Amicus Curiae, *In re Oxford Health Plans, Inc. Securities Litigation*, 182 F.R.D. 42 (S.D.N.Y. 1998) (MDL 1222).
42. *Id.* at 3.

43. No. 98-TMP-1898-S (N.D. Ala. Oct. 19, 1998).
44. *See id.* (Memorandum Opinion) at 5-7.
45. *Id.* at 7.
46. *Id.*
47. *Id.* (Orders) at 6.
48. *Id.*
49. Fed. Sec. L. Rep. (CCH) ¶ 90,453 at 92,099 (S.D. Cal. Jan. 22, 1999).
50. *Id.* at 92,099.
51. *Id.* at 92,099-92,100. The court also noted that a “plaintiff’s group of 339 members would make the administration of this action unnecessarily complex and time consuming.” *Id.* at 92,100. The court had “genuine concerns regarding the degree of control that a group as broad and diffuse as the one proposed herein would retain over the attorneys litigating this action.” *Id.*
52. 186 F.R.D. 214 (D.D.C. Apr. 12, 1999).
53. *See id.*
54. *See id.*
55. *Id.*
56. *Id.* *See also Takeda v. Turbodyne Technologies, Inc.* 1999 U.S. Dist. LEXIS 8965 (D.D.C. June 4, 1999) (quoting *Baan* and rejecting competing groups comprised of hundreds of investors, choosing instead to approve alternative of seven individuals with largest collective losses).
57. No. C-00-20111-JF, 2000 WL 1071821 (N.D. Cal. July 28, 2000).
58. No. C-00-20111-JF, 2000 WL 1071821, at \*3.
59. *Id.* *See also Sakhrani v. Brightpoint, Inc.*, 78 F.Supp.2d 845, 853 (S.D. Ind. 1999) (“This court agrees that selecting as ‘lead plaintiff’ a large group of investors who have the largest aggregate losses but who have nothing in common with one another beyond their investment is not an appropriate interpretation of the term ‘group’ in the PSLRA. Such an interpretation rewards lawyers who solicit plaintiffs and can produce an unmanageably large group of scores, hundreds, or perhaps even thousands of ‘lead plaintiffs.’”).
60. No. 99-197-A, [1999 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶90,510 (E.D. Va. May 21, 1999).
61. No. 5:98-CV-2876, 1999 WL 826076 (N.D. Ohio Aug. 25, 1999).
62. No. C99-2073 RMW (N.D. Cal. Nov. 2, 1999).
63. 76 F.Supp.2d 1017 (N.D. Cal. 1999).

64. No. 5:98-CV-2876, 1999 WL 826076, at \*5-8.
65. *Id.* (emphasis in original).
66. *Id.* at 37.
67. *Aronson v. McKessonHBOC, Inc.*, No. C 99-20742 RMW, at 6.
68. *Id.* at 9.
69. *Id.*
70. 76 F.Supp.2d at 1022 (internal quotes omitted).
71. *Id.* at 1027 (denying lead plaintiff motions made by aggregated groups each consisting of thousands of unrelated investors).
72. 15 U.S.C. § 78u-4(a)(3)(vi).
73. No. 5:98-CV-2876 (N.D. Ohio Aug. 25, 1999).
74. No. C99-2073 RMW (N.D. Cal. Nov. 2, 1999).