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## INSTITUTIONAL INVESTOR RECOVERY — DO YOU NEED HELP?

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Even without becoming a Lead Plaintiff in a securities class action, there are numerous “behind the scenes” activities an institutional investor should participate in to be certain it is fulfilling its fiduciary duties. This activity is required with the filing of a new class action and does not end until final settlement distributions are received from the Claims Administrator. Indeed, the activity of some institutions may be so extensive that they should retain outside counsel to help them fulfill their fiduciary duties.

### *The Institution Should Become Aware of the Class Action at its Inception.*

An effective Class Action Recovery Program should contain data on every securities class action that is filed. If the institution sustained very substantial losses, the institution may consider whether it should file its own action. Alternatively, the institution may work closely with the Lead Plaintiff and Lead Counsel to ensure that any settlement is adequate. In addition, the institution may aid the Lead Plaintiff in preparing the Consolidated Amended Complaint to include details making the case more difficult to dismiss. Finally, by being aware of a case at its inception, the institution is assured that it will be aware of any settlement and claim filing dates.

### *The Institution Should Be Proactive With Respect to Class Action and SEC Settlements.*

Every institution should be certain that it timely files proofs of claim in all settlements in which it is eligible to file, including the government

settlements which are growing in numbers. Indeed, recently over forty alleged class actions have been filed against advisers to mutual funds alleging that the advisers are not filing proofs of claim and have “damaged” the Funds accordingly (“Mutual Fund Claims Cases” or “MFCC”). The institution — or its outside provider — should have an accurate list of all class and government settlements, time periods covered, due dates, CUSIP’s and other pertinent information.

The institution should not assume that simply responding to the notices it happens to receive in the mail is sufficient. There are so many settlements per year (approximately 150 in 2004 for example) that a “reactive” process is inevitably going to result in missing out on some — if not many — filings. Nor is the argument that “we relied on our custodians to do it” persuasive, unless the institution has a specific contract under which the custodian has agreed to file proofs of claim and the institution has reviewed the custodian’s procedures and reasonably satisfied itself that they are sufficient.

Filing effective proofs of claim is not as simple as filling out forms and dropping them in the U.S. Mail. Obtaining accurate transactional information is a timeconsuming process. In addition, Claims Administrators challenge many proofs as deficient and supplemental information is required before the proofs are allowed, requiring substantial follow-up.

Also, the institution needs to closely track recoveries. For example, if the institution is a small mutual fund, does the settlement have an impact on the Net Asset Value of the fund? Does the Plan of Distribution generally match

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what the claimant's expectations were? Have all "allowed" claims been paid? Will there be a supplemental distribution? Is there a process to insure that checks are promptly deposited?

## Settlements Should Be Carefully Considered

### Overview

Rule 23 of the Federal Rules of Civil Procedure provides for notice to shareholders and a hearing on the fairness of all class action settlements. With the increased focus on the role of institutional investors in securities class actions has come increased scrutiny by said investors of proposed settlements.

Suggested procedures to follow in evaluating settlements are discussed below. These procedures are based on the assumption that the viability of pursuing the institution's claims individually could become an issue. Thus, the institution should assess its ability to litigate on the merits before objecting.

### Internal Factors

**(1) Know Your Own Transactions:** After receipt of a settlement notice, the first step that must be undertaken to properly evaluate the settlement is obtaining all transactional information from the institution and interviewing the portfolio managers as to the reasons for their transactions.

**(2) Loss Calculation:** Obviously, the transactional review enables one to ascertain if the "losses" are sufficient to justify the time, effort, expense and distraction of objecting. One should initially review shares purchased during and held throughout the class period. Usually, if other shares are purchased and sold during the class period, any "gains" from these transactions are netted out of the overall "loss" calculations, unless there were partial disclosures during the class period. In addition, many Plans of Allocation require the claimant to have held its shares through

the last day of the class period to be eligible. Thus, losses on sales prior to the end of the class period may not be covered.

Huge losses by themselves, however, should not precipitate an objection. The settlement may be low because the case lacks merit. Also, any knowledge by the institution's portfolio manager of facts which class plaintiffs alleged were "omitted" may hinder the ability to object and file a separate action.

**(3) Present Holdings:** Since settlements often deal with activities several years ago, the institution may have repurchased the securities of the Company. How much money does the institution want to extract from the Company whose securities it presently holds in order to recover past losses?

### External Factors

There are also "external factors" to consider:

**(1) Merits of the case:** An assessment of the merits must be undertaken, including discussions with both plaintiffs' and defense counsel, their reasons for the settlement and, if necessary, independent research;

**(2) Size of Class:** A broader class covering several years usually justifies a bigger settlement;

**(3) Size of monetary settlement:** The calculations of potential per share recovery from the settlement should be reviewed;

**(4) Parallel government action:** Has the Company settled with the government with respect to activities covered by the class period? If so, the fact that the government took action may militate in favor of a larger settlement;

**(5) Use of funds paid in SEC settlement:** Did defendants pay penalties and fines and disgorgement in the SEC settlement? Are said funds available to investors under the Fair Funds Act and how will those funds be distributed?

**(6) Scope of release:** If the release effectively precludes any further claims against defendants during the class period, are there indications that the defendants may be facing further problems?

**(7) The reputation of counsel:** Is Lead Counsel known for small settlements, or is it known for pushing cases toward trial and achieving substantial settlements in difficult cases?

**(8) Source of funds:** Has D&O insurance been exhausted? Is the Company or are other defendants paying in additional monies?

Objecting to a settlement can be a difficult and burdensome decision. A preferable alternative is to ascertain one's "losses" once the class action is filed. Then, once Lead Plaintiff is appointed, the investor can coordinate closely with the Lead Plaintiff. In this way, when entering into settlement negotiations, Lead Plaintiff will be able to cite specific loss figures to defendants. This is a valuable weapon to enhance the plaintiffs' demands during negotiations and can sometimes prevent the problem of an investor being surprised by a settlement that seems far too low. In addition, if the investor still wants to object, it has had enough "lead time" to adequately assess its position.

## Conclusion

Institutional investors must be pro-active throughout every stage of the class action process. Given the vast number of settlements to be evaluated (with proofs of claim due virtually every day), retention of outside counsel to handle the entire process is recommended.

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