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BULLETIN

INSTITUTIONAL INVESTOR

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From time to time, issues emerge regarding securities class actions that have the potential to affect institutional investors in a very significant way. Where we, at Bernstein Litowitz Berger & Grossmann LLP, believe that it is important to bring these issues to your attention before the publication of our regular quarterly newsletter, we will issue a special informtion *BULLETIN*, such as this one. Our next regular issue of the *Advocate* should reach you during the first week of March, 2000.

MASS SOLICITATIONS DUPE INSTITUTIONAL INVESTORS

By Max W. Berger and Robert S. Gans

The purpose of this bulletin is to alert you to an alarming trend among certain class action attorneys to solicit institutional investors to participate in securities litigation as lead plaintiffs through deceptive means. As detailed in a recent important decision emanating from the United States District Court for the Northern District of California, many institutional investors have fallen prey to these techniques, which include advising investors that it is necessary to register with a particular law firm at the outset of litigation to participate in any recovery, when no such requirement exists. We believe that this matter requires your immediate attention, since many institutions already have been victimized by these deceptive solicitation efforts.

As detailed in prior issues of the *Advocate*, the Private Securities Litigation Reform Act of 1995 (the "PSLRA") requires courts to appoint as lead plaintiff in any class action alleging federal securities law violations "the person or group of persons that . . . has the largest financial interest in the relief sought by the Class." Congress enacted this provision to encourage large institutional shareholders to assume control over securities class action litigation. Nevertheless, many traditional class action attorneys who have been unable to attract institutional clients have been creative in their attempts to subvert the Congressional intent and perpetuate the regime of class action litigation dominated by attorneys whose clients only have a nominal interest in the litigation.

For example, certain law firms have taken advantage of a provision of the PSLRA that requires the plaintiff in the first-filed case to publish a notice in a national business publication or wire service informing class members of the pendency of the action, and of their right to apply to the Court to be appointed lead plaintiff. Although Congress contemplated that only one notice would be published, attorneys have used this provision to publish dozens of notices, most of which more closely resemble advertisements for particular law firms than anything else. The goal of these advertisements is to attract either a large investor that is unfamiliar with its rights and responsibilities under the PSLRA, or a large group of small, unsophisticated investors that

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Continued on next page.

the soliciting attorney will seek to have appointed as the "lead plaintiff group" in the litigation, and which invariably selects the soliciting law firm to serve as lead counsel. This strategy, when successfully employed, allows the attorney to perpetuate the pre-PSLRA problem of lawyer-controlled litigation, without regard to the interests of the class.

More recently, many law firms have adopted a variation of this model, investing tens of thousands dollars in direct mailings to all institutional investors, their money managers, and their brokerage firms. Typically, these mailings are not directed to any individual with significant decision-making authority for the investment entity; instead, they are designed to look like proof of claim forms that would be provided to class members later in a case to secure a portion of any recovery obtained, and provide relatively little information regarding the facts of the case. The mailings, also, often misleadingly imply that it is necessary to complete and return an enclosed "certification" form to participate in the action. Neither the certification form itself, nor the materials accompanying the form, specify the obligations that a lead plaintiff is expected to perform. The form merely contains boilerplate language stating the willingness of the recipient to serve as a "named plaintiff" or "class representative"— terms that are used interchangeably, and without any explanation of the added duties and responsibilities assumed by a lead plaintiff in the litigation. In most instances, the recipient need only fill in his stock purchase information, sign the form, and return it to the law firm in a postage paid, preaddressed envelope. Finally, most of the mass solicitations sent by law firms never inform the recipient that he can participate in the Action without assuming any of these duties or obligations, and will be notified of any recovery during the course of the litigation.

Institutions should not be fooled by these mass solicitations. You do not need to take any kind of affirmative action to participate as a class member in securities class actions. By returning a certification form, you are agreeing to be a named party to the action, and are assuming substantial obligations in connection with the litigation — obligations that you may not want to assume in some circumstances, and that you need not assume to participate in any recovery obtained on behalf of the Class. These obligations, as recognized by the SEC and various courts addressing the issue, include the following:

You do not need to take any kind of affirmative action to participate as a class member in securities class actions.

- Maintaining authority and responsibility to consult with and direct counsel with respect to major litigation events, including important motions, trial and settlement;
- Consulting with counsel in advance to determine whether major litigation tasks are necessary and appropriate;
- Meeting with counsel regularly to review the progress and status of the case; and
- Attending major hearings and trial of the Action.

Recently, Judge William Alsup of the United States District Court for the Northern District of California addressed the propriety of mass solicitations and lead plaintiff group formation in a decision that is likely to be followed throughout the nation. Judge Alsup's opinion arose from a bitter dispute between competing law firms for appointment as lead counsel in the case *In re Network Associates, Inc., Securities Litigation,* which was filed on behalf of purchasers of Network Associates common stock between January 20, 1998 and April 19, 1999. On one side of the battle was the law firm Milberg Weiss Bershad Hynes & Lerach LLP, which purported to represent over 1700 individuals seeking to be appointed lead plaintiffs who responded to numerous notices published by the law firm over wire services. Opposing their motion was a group led by the law firm Weiss & Yourman, which claimed to represent more than one hundred institutions and thousands of individuals who responded to a direct mail solicitation campaign orchestrated by the firm.

Over a period of seven months, the two law firms engaged in a paper war, which centered upon Milberg's allegation that Weiss & Yourman's direct mail campaign violated ethical rules and criminal statutes. In his thoroughly researched and detailed opinion, Judge Alsup criticized the mass solicitation tactics engaged in by both law firms. The Court bemoans the fact that the "race to the courthouse," which the PSLRA was designed to eradicate, has been replaced by "a race to both the courthouse and thence to the publisher", in an effort to accumulate as many large investors to support an application for appointment as lead plaintiff as possible. In this regard, Judge Alsup recognizes that the notices do not serve the purpose of attracting institutional investors to assert control over this litigation, as intended by Congress, but instead are designed "to steer investors away from seeking the lead role on their own and to steer them toward registering with a lawyer who already has a lead plaintiff candidate." The result is the formation of mass plaintiff groups incapable of asserting any real control over the litigation. Indeed, the Court noted that the group name used in a lead plaintiff motion is

not stated in the published notice or the certification form signed by the members of the group, nor are the names of the proposed lead counsel indicated on most certification forms. As a result, the members of the group "do not, in all probability, even know they belong to a group or know its name or know how their form is being used." Therefore, the Court disqualified both groups from serving as lead plaintiffs.

Significantly for institutional investors, the same concerns that precluded the Court from appointing a lead plaintiff group also prevented a large investment fund with millions of dollars in losses from serving as the sole lead plaintiff in the Action. Judge Alsup found that the fund, which was represented by the Weiss law firm, was confused by the mass solicitation issued by the firm, and had submitted a signed certification form based only on its mistaken belief that "it was necessary to do so to participate in any recovery." The Court found that the proposed lead plaintiff had very little understanding of the case or the nature of the lead plaintiff motion, and was not even aware that its selected counsel was already suing an affiliated entity for securities fraud in a separate case.

Nevertheless, even though the Court criticized the substance of the published notices and mass mailings used to attract lead plaintiffs, it refused to prohibit the practice of mass solicitations altogether. In finding that such mailings are not contrary to the PSLRA, Judge Alsup was swayed by the views of the SEC, which opined in a brief filed with the Court that "[t]he effect of mailings could be to encourage additional investors to come forward, negotiate with and retain counsel, and move to be lead plaintiff, thereby enhancing competition for lead plaintiff and lead counsel." The SEC warned, however, that such mailings and published notice campaigns are not only potentially deceptive, but also can undermine the goal of the PSLRA.

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Indeed, the SEC noted that in a securities fraud case involving Digital Lightwave, Inc. pending in Florida, at least one member of the ten-person lead plaintiff group appointed in the action did not even know that he was a lead plaintiff until after lead counsel submitted a

Continued on back page.

Don't Be Duped — Steps To Follow

Institutional investors can avoid being duped only if they act wisely and cautiously, which should include taking the following steps:

✔ ***Read unsolicited mailings carefully, and tell your money managers to do the same.*** There is no requirement to submit a form to anyone at the outset of a securities class action to participate in any recovery. Any mailing that states or implies that it is necessary to register with a particular law firm should be discussed with a known and trusted attorney. Any mailing or notice that states or implies that you will get a higher percentage of any recovery obtained for the Class simply by virtue of serving as a lead plaintiff is false.

✔ ***Do not sign anything unless you want to be a lead plaintiff.*** Many of the certification forms used in connection with mass solicitation campaigns do not clearly state that, by submitting the form, you are agreeing to be a lead plaintiff in the litigation. The forms often interpose the term "class representative" for "lead plaintiff", and generally do not detail the duties and responsibilities of a lead plaintiff in overseeing litigation. The best course is to consult with an attorney you know and trust before responding to these solicitations.

✔ ***Choose an attorney carefully***. You are not limited to using an attorney who publishes a notice, directs a mailing to you, or files a complaint to represent you in connection with securities litigation. You are free to select any attorney of your choice to file a lead plaintiff motion on your behalf, to apply to serve as lead counsel for the Class, or even to simply monitor the litigation for you.

✔ ***Act quickly.*** The PSLRA provides sixty days from the time notice of the filing of a securities class action is published for lead plaintiff motions to be filed. It is important that you use that time, in consultation with an attorney of your choice, to investigate the claim, evaluate your losses, and determine whether it is in your best interest to file a lead plaintiff motion. Delay could result in your making a rushed and uninformed judgment that you could later regret.

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BLB&G INSTITUTIONAL INVESTOR Advocate
Bernstein Litowitz Berger & Grossmann LLP
1285 Avenue of the Americas
New York, NY 10019

Continued from page 3.

settlement of the case to the Court for approval. In this instance, lead counsel failed to respond to this "lead plaintiff's" repeated requests for information regarding the status of the action for over six months, and never even informed him that he had been appointed a lead plaintiff by the Court. Thus, while the SEC concluded that the practice of mass solicitation itself should not be banned, it stressed to Judge Alsup that it was not "sanctioning the methods utilized by Weiss & Yourman in forming a proposed lead plaintiff group." The Court concurred in the SEC's judgment, however, that abuses in the practice should be dealt with through regulatory or other means short of a blanket prohibition.

Despite the abuses recognized by Judge Alsup, and echoed by the SEC, the practice of soliciting institutional investors through mass mailings is likely to continue, and probably will accelerate. Further, the prospects for implementing a regulatory framework to cure the abuses inherent in this process are questionable at best, and even under the most ambitious schedule would likely take years to complete.

The lead plaintiff provisions of the PSLRA were passed to protect the rights of institutional investors. By monitoring securities fraud filings carefully and scrutinizing unsolicited mailings from law firms (read checklist on page 3), you can help end abuse, and ensure that these goals are achieved.

Max W. Berger can be reached at mwb@blbglaw.com. Robert S. Gans can be reached at robert@blbg.law.com

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BLB&G INSTITUTIONAL INVESTOR Advocate
Bernstein Litowitz Berger & Grossmann LLP
1285 Avenue of the Americas
New York, NY 10019
Phone: 212-554-1400
E-mail: blbg@blbglaw.com
www.blbglaw.com

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Editor: Gerald H. Silk
Editorial Director: Ava C. Thorin
Contributing Attorneys: Max W. Berger, Robert S. Gans