

The Expert's Corner

WHAT WE NOW KNOW ABOUT HOW LEAD PLAINTIFFS SELECT LEAD COUNSEL (AND HENCE WHO GETS ATTORNEYS FEES!) IN SECURITIES CASES

William B. Rubenstein*

A key way to get class action fees is to be appointed lead counsel. In securities cases, firms conventionally achieved this goal by being first to file, often with a penny-ante plaintiff who was within their control. Believing that this situation created conditions for frivolous lawsuits and class action abuse, Congress, through the Private Securities Litigation Reform Act (PSLRA), authorized the largest intervening investor to gain control of a securities case and select lead counsel;¹ the PSLRA thereby placed a real client at the heart of securities litigation, a client who Congress authorized to select, monitor, and, ultimately, control class counsel.

Yet fifteen years later, entrepreneurial plaintiffs firms continue to dominate securities class actions, perhaps to an even greater extent than they did before the PSLRA. That they've accomplished this speaks to their entrepreneurial capacities, though the mechanisms by which they have been able to accomplish it have remained largely cloaked in urban legend.

Until recently.

An interesting trove of materials has turned up in litigation challenging the marketing of sub-prime mortgage backed securities. In *Iron Workers Local No. 25 Pension Fund v. Credit-Based Asset Servicing and Securitization, LLC*, ___ F. Supp. 2d ___, 2009 WL 1444400 (S.D.N.Y. 2009), federal district court Judge

¹ The lead plaintiff provisions of the PSLRA provide for the "most adequate plaintiff," 15 U.S.C. § 77z-1(a)(3)(B)(i), to serve as the lead plaintiff, with the rebuttable presumption that the "most adequate plaintiff" is the one with the largest financial interest in the recovery of the class. 15 U.S.C. § 77z-1(a)(3)(B)(iii)(I)(bb).

*William B. Rubenstein, a law professor at Harvard Law School, specializes in class action law; he has litigated, and regularly writes about, consults, and serves as an expert witness in class action cases, particularly on fee-related issues. Professor Rubenstein's work can be found at www.billrubenstein.com. The opinions expressed in this article are solely those of the author.

Jed Rakoff appointed the Public Employees' Retirement System of Mississippi (MissPERS) lead plaintiff with Bernstein Litowitz serving as lead counsel. This decision was made after a battle between MissPERS and the Iron Workers Local No. 25 Pension Fund (Iron Workers Fund), during the course of which the court discovered – to its apparent surprise – that both MissPERS and the Iron Workers Fund were involved in "monitoring agreements" with plaintiffs firms.

Specifically, in order to woo large institutional investors like public pension funds to participate in securities class actions, some plaintiffs firms have entered into arrangements whereby they monitor the funds' investments for irregularities and suggest possible grounds for litigation. If, after considering whether or not to bring suit, the funds do decide to commence litigation, the firm that did the monitoring leading to the suit is retained to do so (or at least has an inside track to be selected). The firms are paid nothing for this "service" other than the fees they receive from the cases it generates. Professor Coffee reports that, "most plaintiffs firms in this field are now offering such services, and openly advertising them on their Web sites."²

In *Iron Workers*, MissPERS and the Iron Workers Fund were vying to be appointed lead plaintiff of a putative class of investors who purchased subprime mortgage-backed certificates from defendant Merrill Lynch and/or its affiliates and who alleged that the defendant failed to disclose the extent of the underlying risk of these certificates. During the process of trying to decide which fund to appoint lead plaintiff, Judge Rakoff discovered that both funds had entered into monitoring arrangements with plaintiff firms. Judge Rakoff expressed surprise upon learning of the existence

² John C. Coffee, Jr., 'Pay-to-Play' Reform: What, How and Why?, May 21, 2009 N.Y.L.J. 5 (col. 1).

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