**THIRD CIRCUIT TASK FORCE**

**STATEMENT OF EDWARD LABATON**

I am a partner of Goodkind Labaton Rudoff & Sucharow, LLP. A very large part of my practice, has been involved with class actions, primarily securities class actions. I have been engaged in such practice since the mid-1960s. In the first cases in which I was involved, we represented defendants in actions brought as "spurious class actions' under old Rule 23. Since then, I have generally represented plaintiffs. I have also participated as a faculty member in Practising Law Institute and ALI/ABA continuing legal education programs involving securities litigation. Since 1996, I have been the President of the Institute for Law and Economic Policy ("ILEP"), a non-profit, public policy organization which in conjunction with major law schools has co-sponsored six symposia. The symposia have dealt with issues relating to the civil justice system and its role in the protection of investors and consumers. Every symposium has dealt, in part, with issues relating to class actions. The papers delivered at the symposia have been, or will be, published in the law reviews of the co-sponsoring law schools. We have had two symposia with the University of Arizona College of Law, two with Duke University Law School, one with Columbia Law School and, most recently, in March 2001 with Washington University Law School

The following is an outline of the subject matter which I intend to discuss at the Task Force hearing to be held on May 5, 2001:

**Securities Class Actions:**

The lead counsel provisions in Private Securities Law Reform Act ("PSLRA") are designed to have the lead plaintiff actively monitor the litigation. The legislative history makes clear that the provisions are designed to encourage larger shareholders, particularly institutional investors, to take an active role in the conduct of a securities class action. It would be totally inconsistent with the purposes outlined in the statute and in its legislative history to have

someone other than the lead plaintiff select counsel. The lead plaintiff provisions were inspired by the Weiss & Beckerman article in the Yale Law Journal, *Let The Money Do The Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions*.
104 Yale L. J. 2053 (1995)

**Other Class Actions:**

Selection of a lead plaintiff or lead counsel in other cases is not as clear in PSLRA class actions. Most courts prefer to have the parties themselves determine who should be lead counsel and, for the most part, this has worked with a minimum expenditure of judicial time. Where the parties or their counsel are unable to reach agreement some form of court intervention is necessary. In those circumstances the one guiding principle seems obvious: who can best represent the interests of the class. In determining who would best represent the class, no single set of standards applies to every case. For example, in some cases, the first filed case might be especially significant particularly if it was well pleaded and did not follow any news report or governmental action. On the other hand, if within a few days of some public disclosure or governmental action a large number of similar cases were filed, the court might look at other factors such as experience and competence of counsel, the ability of counsel to work together with an agreed upon leadership structure, or the resources which counsel will bring to bear in the case, etc.

**The Auction Process**

The auction process has been limited to about a dozen cases in a few districts. Its use has no benefit and potential for serious harm.

The supposed benefit of more money to the class as a result of an auction process is illusory and short sighted.

It is illusory because the court ultimately has broad discretion in setting the fee and in those circumstances where the court perceives that the case was a "slam dunk" it can award a fee well below recognized norms for contingent fees. (see e.g. Judge Cote's decision

in the Auction House Securities case and Goldberger v. Integrated Resources 2000 U.S. App Lexis 5151 (2d Cir. March 28, 2000)).

It is short sighted because it emphasizes one factor while giving short shrift to factors that a prudent plaintiff would weigh in picking his or her counsel in a complicated or difficult case: can plaintiff's counsel litigate against well financed large and powerful firms; have they done a thorough pre-filing investigation; what is their track record in the area (antitrust, securities, consumer fraud) involved in this case, etc.

The auction process can also lead to unfortunate conflicts and unintended consequences. Professor Coffee has explicated the problems in the Auction House antitrust case formula. He adverts to other situations where a formula which limits the incentive to obtain a higher award, could result in a settlement which short changes the class.

There is another more subtle risk in the auction process -- particularly where the court, as it must, reserves the right not to select the lowest bidder. The court cannot simply award the lead counsel position to the best bidder. It must determine that class counsel have the capacity, experience and resources to effectively represent the class. The court, probably not consciously, may develop a bias in favor of the counsel it selected. The court, after all, will have determined that that counsel can best represent the class. Might it not show a predilection in favor of that counsel, arguing, for example, a motion to dismiss?

I don't mean to suggest any impropriety on the part of judges who have used the auction process, and I'm not a behavioral scientist, but you don't have to be one to recognize the risk that at least some judges will subconsciously protect their decisions by favoring the lawyer they selected to represent a class.

This, of course, is not limited to cases in which an auction process is used; and therefore I suggest that where there is a serious contest for the lead counsel position, the court hearing the case might consider referring the selection of lead counsel to another judge.

I believe there are no benefits and serious detriments to the auction process. But, if there is an auction process, the bids should be sealed, but I see no disadvantage to bids from a consortium of firms. Indeed, this would enable smaller, less well financed but competent firms to be class counsel. It also would recognize the reality that even the larger plaintiff firms often have a fraction of the personnel and economic resources of the firms representing defendants.

Any formula should allow some flexibility to deal with unanticipated problems. Therefore, counsel should be permitted to seek modification of the formula at the end of the case. The court, of course, would retain the ultimate power to determine whether an adjustment is appropriate.

As to whether lead counsel should be one firm or several, depends on the specific circumstances of the given case. Courts selecting counsel should have the flexibility to deal with each case based on the nature of the case and the available resources to prosecute it.

**Conclusion:**

An auction process is inconsistent with the Lead Counsel provisions of the PSLRA. In cases other than those subject to PSLRA, the system of selection of lead counsel works well where counsel can agree on a leadership structure. The courts should generally accept that structure because it is judicially efficient and, because of the power of the court to determine fees, is also cost efficient.

Where the parties cannot agree on a structure, the guiding principle in appointing one or more lead counsel must be: what leadership structure will most benefit the class. An auction process does not help in achieving that goal.

April 30, 2001