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SECURITIES LAW

Monitoring Settlements, Distributions in Securities Class Action Litigation

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Special to the Legal

While much attention has been paid in recent years to the pleading standards under the Private Securities Litigation Reform Act of 1995, the effects of the Sarbanes-Oxley legislation in 2002 and the Supreme Court's 2005 decision in *Dura Pharmaceuticals v. Brouda*, another issue has arisen. Injured institutional investors have begun to pay more attention to ensuring that they receive their fair share of securities class action settlements. Leaving money on the table after a settlement defeats the purpose of securities class action litigation designed to compensate injured investors for economic harm caused by securities fraud. Investors receive a distribution from a settlement only if they participate in the settlement process. But the complexity of the settlement process surprises many investors. Getting from the settlement to the distribution of money to investors can be a time-consuming and labor-intensive process.

PARTIES AGREE TO SETTLE

Once the parties to a securities class action lawsuit reach an agreement in principle, the agreement must be reduced to a writing. A short version of the agreement, usually called a memorandum of understanding, or MOU, can be drafted and signed fairly quickly. The MOU, which is often completed within a week of the oral agreement, contains the bare bones of the agreement, with the details left for the formal settlement stipulation. Once an MOU is signed, and the court is notified of the existence of the settlement, the work on the detailed terms of the settlement begins. Corporate defendants often issue a press release announcing the settlement of the securities case after an MOU is signed.

Working out the details of a settlement can be time-consuming. While parties often draft and agree upon the language in a settlement agreement within a month of the MOU, with more complicated

settlements, such as those involving the issuance of securities to the class, the process can go on for many months.

The settlement stipulation is only one of the documents needed to complete the settlement. The parties must also agree upon the language of the notice to be mailed to members of the class. This notice describes the settlement and invites class members to participate in the settlement, or, alternatively, allows them to object to it. The language of a proof of claim form and release must also be agreed upon. The parties also prepare a summary notice for publication in the media. Finally, proposed forms of order must be prepared for the court's preliminary and final approval of the settlement.

The notice, which typically includes the



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proof of claim form, is mailed to shareholders of record, as identified by the company's transfer agent. The notice also is sent to nominees (typically brokerage firms) that hold securities in "street name" for their clients. The nominees are directed to distribute the notice and proof of claim forms to their clients. In addition, to ensure the most comprehensive notice possible, the summary notice is published in national newspapers and on the Internet. It is designed to reach a broader audience than the mailed long form of notice. Although the summary form of notice lacks the same detail, it contains instructions for obtaining a copy of the long form of notice and proof of claim forms.

COURT APPROVAL

Once the parties have agreed on the language in these documents, they submit them to the court for preliminary approval. In granting preliminary approval, the court authorizing the mailing of the notice sets important deadlines for the final approval of the settlement, including the date of the "fairness" — or final approval — hearing, the dates for submission of the parties' final papers in support of the settlement and the date by which objections to the settlement must

be filed. The court also sets the deadline for injured investors to submit their proofs of claim. These dates are included in both forms of notice. Time frames vary from case to case, but typically the proof of claim deadline is several months after the notice is mailed, and the final approval hearing is often scheduled just before that claims

deadline.

The final approval hearing can take 15 minutes, a full day or even longer. A brief hearing is the norm in a simple matter where there are no objections to the settlement. But the hearing could take a full day or more if the settlement is complex or if there are objections to the settlement. If the court determines that the settlement is not fair, the court will not issue its final approval. If the court does approve the settlement, the final approval order may be issued at the conclusion of the hearing or some time later, usually no more than a week or two after the hearing.

Final approval of the settlement is not the end. Even after the settlement has been finally approved by the court, and the time passes for any appeal from that final approval

order, there still remains much to do before the settlement funds may be distributed.

CLAIMS ADMINISTRATION

Administration of the settlement begins when the first proof of claim form arrives at the claims administrator's offices. A claims administrator, often a certified public accounting firm, is selected by class counsel and approved by the court. The proof of claim form requires a claimant to provide detailed information about her class-period transactions in the subject security and requires the claimant to provide proof of the transactions she identifies in the form, usually by submitting copies of transaction confirmation slips or brokerage account statements. Depending on how actively traded the stock was during the class period, the claims administrator could receive anywhere from 2,000 to 120,000 proof of claim forms, or more.

The claims administrator creates a specialized database for each case it administers. The claimant identification information on each claim form is entered into the database and the claimant is assigned a claim number. The transaction data contained in each proof of claim form is then analyzed by the claims administrator's staff to verify the accuracy of the information, to determine whether a claim is deficient in any way and to calculate the claimant's eligible losses, if any, based on the allocation formula applicable to the settlement. After the analysis is completed, the transaction, deficiency and loss data are entered into the database.

Once the database is complete, the claims administrator then contacts every claimant whose claim was rejected or found to be deficient. A claim will be rejected, for example, if the claimant purchased the securities in question outside of the class period. On the other hand, a claim is deficient if the claimant has not provided sufficient transaction information to verify the eligibility of the claim. Claimants who submit deficient claims are provided an opportunity to cure any identified deficiencies. Rejected claimants have the opportunity to demonstrate that the rejection is not proper. If a claimant does not cure an identified deficiency, the claim is rejected. Any claimant whose claim is rejected may seek the court's review of the administration of their claim. The process of contacting deficient and rejected claimants often takes many months to complete.

When the claims administrator has made a final determination for each claim, including the deficient and rejected claims, it prepares a final report containing detailed information about each claim and its recommendations for the acceptance or rejection of claims. Typically, nine to 15 months elapse between the claims deadline and the issuance of the claims administrator's report.

DISTRIBUTION

Once the settlement administration is completed, class counsel generally requests permission from the court to distribute the

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settlement fund in accordance with the claims administrator's recommendations. Class counsel submits the report of the claims administrator, as well as any requests for court review of rejected claims, if any. The court may hold a hearing on the matter, but typically the court orders the distribution of the settlement fund based upon the papers. This could take a day or a month, depending upon the court's schedule.

From the initial agreement to settle a securities case through to the final court approval can take months or even up to a year. From the time claim forms are due, which typically occurs shortly after the

final approval hearing, until the settlement distribution checks are mailed can stretch anywhere from nine to 18 months.

Once the court signs the distribution order (and the time for filing an appeal of that order has passed), the settlement fund, including the principal contributed by the defendants plus all interest earned in the intervening months, may be distributed, subject only by the time required to print, assemble and mail the checks. If the settlement is not all cash, however, additional delays are typical. With a stock settlement, for example, the issuance of stock certificates by a company's transfer agent adds more administration that may delay distribution for months. As typically results from the nature of a sensible compromise, where the settlement fund is insufficient to pay the total amount of all eligible losses each claimant receives a check for their

proportionate share.

PARTICIPATION

An investor who suffered economic losses from securities that are the subject of a class action settlement must submit a proof of claim to receive a distribution from that settlement. Because monitoring settlements of securities fraud class actions is time-consuming, investors large and small often fail to participate in settlements. As a result, in recent years many institutional investors have retained a claims monitoring service to monitor their financial interest in all pending securities class actions. These monitoring services help the investor ensure timely proof of claim filings. Without adequate vigilance, investors will continue to leave money on the table from securities class action settlements.

Leslie Bornstein Molder contributed to this article. •