WOLF POPPER
ESTABLISHED IN 1945

845 Third Avenue, New York, NY 10022
212-451-4600 • wolfpopper.com

# How to Recover More in Securities Litigation? Resolve the Historical Data Conundrum!

By Adam Savett

We are figuratively drowning in data. Current estimates are that every day we generate 400 million terabytes of data. Access to data, especially historical data, is vital to preserve the ability to file claims in settled securities class actions. Institutional investors have a fiduciary duty to file those claims, or to show that choosing not to do so is prudent. If an institution does not take a proactive approach to securing their historical data, significant problems can flow from that decision.

## 1. Determining Eligibility

In order to successfully file a claim in most securities class action settlements, an institutional investor will first need to determine whether they are eligible to participate in the litigation. This typically involves comparing the definition of the class (the group of investors that are to be included in a given litigation) to the current, or more commonly, the historical securities transactions of that fund. The class definition will typically spell out which securities are included in the litigation as well as the period during which the fund had to purchase or sell the securities at issue ("class period.") On the surface this sounds straightforward; the reality is far more complex.

## 2. Ten Years, Really?

As an initial matter, the class period for a federal securities fraud class action can span a period of five years. Layered on top of that is the length of time that most cases take to reach the settlement stage -- 2-5 years. One can immediately sense that the data needed to file claims in settled cases can, and often is, quite historical in nature.

This presents a real problem for institutional investors. Obtaining access to, searching through, and

extracting 10+ year old securities transaction data is often not something that was planned for when custodial bank relationships were initiated or terminated, or when internal fund management and accounting systems were built or sunset.

### 3. Failing to Look to the Future

Layered on top of service provider turnover is the apparent failure to look to the future when starting these new relationships. Indeed, an analysis of more than 200 Requests for Proposals (RFPs) issued during the last 7 years for custodial bank services revealed that less than 10% of the RFPs even mentioned securities class action claims filing. An even smaller percentage mentioned access to historical information if, and when, a custodial relationship is terminated. We have often encountered a reluctance on the part of a former custodian to grant a client access to their historical securities transaction information. This reluctance is often accompanied by a request for a fairly significant payment, which we call a “data hostage fee.” Both issues might be avoidable, as discussed below.

### 4. Increasing Breadth = Increasing Complexity

Just as importantly, the breadth of class action settlements continues to expand. Historically, it was fairly common for a securities class action settlement to include just one security identifier (CUSIP, SEDOL, or ISIN). Cheap and ready access to the debt markets meant that an increasing number of companies issued debt securities or multiple tranches of preferred shares. These debt securities are often now included in securities class actions and the resulting settlements. A quick analysis of settled cases finds that the percentage of settlements involving fixed income securities has dramatically increased over the years and now encompasses more than 20% of all settlements in a given year.

### 5. Regulatory and Client Scrutiny is on the Rise

The need for this data is becoming more important as regulators and beneficiaries are turning a keener eye on the size of securities litigation settlements and the failure of investors to file claims in settled cases. More than two decades ago, a pair of prominent academics published the first of several seminal papers on the responsibilities and practices of institutional investors with regard to filing claims in settled securities class action cases. Their startling findings - that the vast majority of institutions lacked any formal process for tracking and claiming settlements - continue to reverberate through the industry to this day. Following on the heels of that groundbreaking study, the SEC’s Office of Compliance Inspections and Examinations contacted a number of investment advisors seeking a broad swath of information on practices and policies with regard to class action claims filing. While those inquiries were informal in nature, they did highlight that the SEC and other regulators are paying attention to this area.

### 6. Liability – The Risks are Real

The costs of not filing, or not filing properly, can be high indeed. The institutional investor, of course, suffers the direct hit of not recovering funds it has already lost and is entitled to claim. Both the institution and its management may suffer the costs of defending, and possibly settling, litigation over alleged breaches of fiduciary duty for failing to safeguard plan assets.

In January 2005, 40 mutual fund managers were sued by shareholders in class action lawsuits alleging that the funds had failed to collect nearly $2 billion in settlement payouts to which the funds (and the funds' shareholders) were entitled. The lawsuits alleged that the funds' failure to claim this money was a breach of the managers' fiduciary duty and a violation of federal law. The lawsuits sought compensatory damages for all of the money that the funds left on the table, punitive damages, and the forfeiture of all commissions and fees paid by fund shareholders.

In 2007, an investment advisor took a $56 million charge as a result of having to reimburse certain clients and internal mutual funds for claims filing mistakes. The size of the missed claims for several of the mutual funds was significant enough to materially impact the NAV for those funds at the time of reimbursement.

Several years after that, various Wachovia and Wells Fargo entities were sued for allegedly failing to notify clients that they were members of a specific class action settlement class, and that as a result, those clients did not file claims and thus did not receive any proceeds. In denying a motion to dismiss that case in 2010, a federal judge recognized that a fiduciary relationship exists between the beneficial owner of securities and the nominee or record owners, and that such a duty could be breached by a failure to notify beneficial owners of class action settlements. While the parties eventually settled the case for a relatively minor sum, it took four years of distracting, expensive, and hard-fought litigation.

These situations continue to pop up, with FINRA arbitrations and additional cases being filed in the ensuing years alleging essentially the same issues – a failure to notify clients or a failure to file claims where a fiduciary or contractual duty exists to do so.

### 7. Access to Data is Not Enough

Merely obtaining access to the data will be insufficient if the data will not provide the information needed to file and perfect a claim. A number of issues arise in the context of fund management and accounting systems and custodial relationships. We can highlight four in order to show the depth and breadth of the problems.

- At the time of a custodial transfer, the new custodian receives the positions in the portfolio, not the transactional history for the portfolio. The new custodian will therefore lack sufficient information to file and perfect a claim on behalf of the client.

- Custodial banks will overwrite historical transactional information when an issuer undergoes a CUSIP change. If the new CUSIP is not included in the class definition, because for example, the change was implemented after the end of the class period, a search on the "massaged" data for the included CUSIP (the old one) will not reveal any eligible transactions, thus potentially leading an investor to not file an otherwise eligible claim.

- Similar issues exist with bond maturities, where they are wiped from the prime broker's records a certain time after maturity. Again, a search for the correct CUSIP will not find the relevant transactions, as they have been removed from the records.

- Some vendors' systems will by default extract information with the settle date and not the trade date, resulting in incorrect data and possibly denied claims.

### 8. Solution #1 - Have a plan

As a baseline, an institutional investor needs to have a defensible policy for tracking and seeking recoveries via securities litigation. Such a policy should address the roles of both internal and external resources. Any policy should clearly spell out who is responsible for filing claims in settled matters on behalf of the fund. The policy should also spell out steps to be taken when changing service providers.

## 9. Solution #2 - Put it in writing!

The need for access to historical data should be addressed at the outset of the relationship with a service provider, such as a custodial bank, preferably in the contract. This will guarantee that an institutional investor has the right to access their own historical data, for example, to allow a third-party claims filing service to file claims on behalf of the fund. A custodian may insist on inserting a pre-negotiated fee structure for this access. While we think these fees are generally garbage profit centers, it is worth noting that it is far better to negotiate such fees at this point, rather than at the end of the relationship when the clock is ticking.

Additionally, it is important to understand the limitations that a custodian or other third-party filer may place upon their services. Also, most custodians will not file claims that include data that predates their custodial role. Many service providers impose minimum monetary loss thresholds before they will file a claim on behalf of an institution. At the other end of the spectrum, some service providers will not agree to caps on their so-called "success fees," and may seek windfall profits from the claims filed on behalf of institutional investors.

## 10. Solution #3 – Avoid Pain by Creating Redundancy

There are compelling reasons to consider having a third party other than a custodian monitor your portfolio and archive your data. One is to ensure that the institutional investor has a source for clean warehoused historical data. Another is to ensure that whoever is filing claims for your institution considers it a core part of their service offering, and thus pays it the attention it needs and deserves.

With these thoughts in mind and best practices in place, you can rest assured that your institution is well on its way to recovering every penny for which you are entitled.

## About the Author

**Adam Savett, Of Counsel**

Adam Savett joins Wolf Popper LLP with more than two decades of experience representing and advising some of the largest and most sophisticated institutional investors, government entities, individuals, and businesses in securities, antitrust, consumer protection, and other complex litigation.

Adam is a nationally recognized leader on complex litigation, class actions, and settlement claims filing. He is a frequent speaker, author, and commentator on class actions and securities litigation, and his comments have appeared in a wide variety of publications, such as The New York Times, Wall Street Journal, CFO Magazine, and Pensions & Investments.

Adam was previously named one of the 100 Lawyers You Need to Know in Securities Litigation by Lawdragon Magazine and has been an invited speaker before numerous industry groups, including the Federal Judicial Center (FJC), National Conference on Public Employee Retirement Systems (NCPERS), Bank Depository Users Group (BDUG), National Council on Teacher Retirement (NCTR), Association of Global Custodians (AGC), and SIFMA's Global Corporate Actions Forum.

# About Wolf Popper LLP

Wolf Popper is a leading complex litigation law firm that represents clients in high stakes individual and class action litigations in state and federal courts throughout the United States. The firm specializes in securities fraud, mergers and acquisitions, consumer fraud litigation, healthcare litigation, ERISA, and commercial litigation and arbitration. Wolf Popper was founded in 1945, and is headquartered in New York City. Wolf Popper also has offices in Washington, DC; Houston, Texas; Chicago and Springfield, Illinois; Boston, Massachusetts; and San Juan, Puerto Rico.

Wolf Popper's attorneys are experienced litigators, many of whom have prior experience at AmLaw 100 firms or in government agencies. Wolf Popper's reputation and expertise has been repeatedly recognized by courts, which have appointed Wolf Popper and its attorneys as lead counsel in complex litigations throughout the country. Over the past eighty years, Wolf Popper has recovered billions of dollars for its clients.

Wolf Popper was one of the first laws firms in the United States to develop a class action securities litigation practice. The practice was founded in 1958, and grew out of the Firm's historical commitment to protecting the rights of individuals. Wolf Popper's long-established role in the securities bar provides its clients with an understanding and insight into federal securities and state fiduciary duty laws that could only be obtained through years of practice in the fields.

Wolf Popper provides a range of services which are designed to aid shareholders seeking to recover damages related to fraud and other corporate misconduct, as well as shareholders who seek to advocate for improved corporate governance.

Wolf Popper routinely represents damaged and defrauded institutional and other large investors in class action and individual securities litigations. Wolf Popper is regularly appointed lead or co-lead counsel in complex securities litigations. Wolf Popper is very selective in the cases it litigates. The Firm's careful factual and legal research and selective prosecution has resulted in a significant percentage of the securities litigations in which the Firm is involved being sustained over, or being settled prior to a decision on, a motion to dismiss. Wolf Popper regularly litigates cases alleging materially false and misleading statements in violation of the federal securities laws, as well situations involving as other corporate misconduct, such as (i) excessive compensation being paid to a company's management; (ii) self-dealing transactions between a company and its management or directors; or (iii) where a majority/controlling shareholder seeks to cash out the public, minority shareholders at a grossly unfair price or in a manner that compromises the process necessary to ensure that the public shareholders are treated fairly.

Wolf Popper's portfolio monitoring service aims to educate the Firm institutional investor clients about securities litigation and corporate misconduct issues that impact their investment portfolios. The Firm provides monthly and case specific reports related to current litigations and disclosures of potential fraud or other corporate misconduct. Wolf Popper also provides clients with monthly reports of recently reached class action settlements to help clients identify settlements in which they might be entitled to participate.

Wolf Popper serves as a trusted advisor to institutional shareholders, and strives to help board members, directors, administrators, and other fiduciaries meet their duties and responsibilities to protect fund assets and mitigate the risks and liabilities. Wolf Popper represents a number of state, county, and municipal pension funds as well as Taft-Hartley plans and other sophisticated institutional investors. Wolf Popper's portfolio monitoring services are provided to institutional investors at absolutely No Out-of-Pocket Cost and Risk Free. Wolf Popper provides litigation services to institutional investors on a contingent fee and non-recourse basis.

Wolf Popper has a long history of representing international clientele. Wolf Popper's office in San Juan, Puerto Rico provides the firm with a gateway to the civil law system in Latin America and Europe; Wolf Popper has working relationships with firms throughout those jurisdictions. Latin American institutional investors worldwide can expect fully bilingual services in portfolio monitoring and securities litigation from diverse and experienced attorneys.

Wolf Popper's founders always recognized the value of a workforce comprised of talent across the demographic spectrum. The Firm has been committed to diversity and inclusion and gender equality since its inception and is proud to continue to embrace that tradition of inclusion to the benefit of the Firm and the clients we serve.

To learn more, please visit us at *www.wolfpopper.com*, or email us at *outreach@wolfpopper.com*.

**www.wolfpopper.com** **Wolf Popper LLP** **@WolfPopperLLP**