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The New Professional Plaintiffs in Shareholder Litigation

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THE NEW PROFESSIONAL PLAINTIFFS IN SHAREHOLDER LITIGATION

Jessica Erickson[*]

Abstract

In 1995, Congress solved the problem of professional plaintiffs in shareholder litigation—or so it thought. The Private Securities Litigation Reform Act (PSLRA) was designed to end the influence of shareholder plaintiffs who had little or no connection to the underlying suit. Yet it may have failed to accomplish its goal. In the wake of the PSLRA, many professional plaintiffs simply moved into other types of corporate lawsuits. In shareholder derivative suits and acquisition class actions across the country, professional plaintiffs are back. They are repeat filers involved in dozens of lawsuits. They are the attorneys' spouses, parents, and children. They may even be entities created for the primary purpose of filing litigation. These new professional plaintiffs have flown almost entirely under the radar of corporate law scholarship. This Article pulls back the curtain on professional plaintiffs, examining court filings and other public records in the first comprehensive study of professional plaintiffs' role in corporate law. In most instances, professionalism is a good thing—but not when it comes to choosing plaintiffs.

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INTRODUCTION

In the early 1990s, corporate America claimed to be under siege by professional plaintiffs. Companies asserted that plaintiffs were filing securities class actions armed with little more than suspicion of bad business decisions.[1] According to conventional lore, these plaintiffs worked in tandem with their attorneys, deliberately positioning themselves to file lawsuits by purchasing a few shares of stock in a large number of public companies.[2] Investor groups joined in the chorus, arguing that these

1. *See, e.g.*, *Securities Litigation Reform: Hearings Before the Subcomm. on Telecomms. & Fin. of the Comm. on Energy and Commerce*, 103d Cong. 216, 499–503 (1994) [hereinafter *Hearings Before the Subcomm. on Telecomms. & Fin.*] (testimony of Stephen F. Smith, General Counsel and Dir. of Investor Relations, Exabyte Corporation); *Common Sense Legal Reform Act: Hearings Before the Subcomm. on Telecomms. & Fin. of the Comm. on Energy and Commerce*, 104th Cong. 39–42 (1995) (statement of James Kimsey, Chairman, America Online, Inc.).

2. *See* H.R. REP. NO. 104-369, at 32–33 (1995) (Conf. Rep.) ("Professional plaintiffs who

plaintiffs had little incentive to protect the interests of absent class members.[3] The system was broken, and many critics placed the blame squarely with professional plaintiffs.

In response, Congress enacted the Private Securities Litigation Reform Act of 1995 (PSLRA).[4] The PSLRA overhauled enforcement of the federal securities laws. It placed strict limits on the number of securities class actions that a single investor could file, and it prohibited investors from receiving payment in exchange for lending their names to litigation.[5] It also established a rebuttable presumption that the lead plaintiff would be the applicant with the largest financial stake in the litigation.[6] These provisions created strong incentives for large institutional investors to take control of securities class actions.

In the wake of the PSLRA, concerns about professional plaintiffs largely faded.[7] Since 1995, there has been scholarly debate over the role of large, institutional investors, but not an in-depth discussion of other, more traditional types of professional plaintiffs in corporate law scholarship.[8] In short, scholars and policy makers have declared "Mission Accomplished" in the world of shareholder litigation.[9]

Yet, entirely under the radar of corporate law scholarship, the war goes on. Professional plaintiffs have not disappeared—many have simply moved to other types of corporate lawsuits. Because the PSLRA only covers federal securities class actions,[10] it does not apply to shareholder suits that arise under state law.[11] In these suits, professional plaintiffs may

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own a nominal number of shares in a wide array of public companies permit lawyers readily to file abusive securities class action lawsuits."); S. REP. NO. 104-98, at 6 (1995) ("Lawyers typically rely on repeat, or 'professional,' plaintiffs who, because they own a token number of shares in many companies, regularly lend their names to lawsuits.").

3. *See, e.g.*, *Hearings Before the Subcomm. on Telecomms. & Fin.*, *supra* note 1, at 54 (letter from pension fund managers to Sens. Christopher Dodd and Pete Domenici); *id*. at 447–55 (testimony of Bartlett Naylor, National Coordinator of the Office of Corporate Affairs, Int'l Brotherhood of Teamsters).

4. 15 U.S.C. § 78u-4 (2006).

5. *Id.* § 78u-4(a)(3)(B)(vi), (4).

6. *Id.* §§ 78u-4(a)(3)(B)(iii)–(v).

7. I am referring here to individuals who serve as plaintiffs in shareholder suits. As discussed below, many institutions—especially labor and public pension funds—have also begun to serve as repeat plaintiffs in these suits. This Article focuses almost exclusively on the role of individual plaintiffs, rather than these institutional plaintiffs.

8. Recent court decisions typically only mention professional plaintiffs when discussing pre-PSLRA history or interpreting specific provisions in the PSLRA. *See, e.g.*, *In re* ESS Tech., Inc. Secs. Litig., No. C-02-04497RMW, 2007 WL 3231729, at *3 (N.D. Cal. Oct. 30, 2007); *In re* Sterling Fin. Corp. Secs. Class Action, No. 07-2171, 2007 WL 4570729, at *2 (E.D. Pa. Dec. 21, 2007). The Milberg Weiss indictments were more recent, but related almost entirely to pre-PSLRA allegations. *See infra* pp. 7–9.

9. *See* President George W. Bush, Remarks on the *USS Abraham Lincoln* (May 1, 2003).

10. *See* 15 U.S.C. § 78u-4(a)(1) (2006).

11. As discussed below, the Securities Litigation Uniform Standards Act, which Congress

be alive and well, often using the exact same practices that Congress thought it eliminated back in 1995.

How have professional plaintiffs stayed out of the legal limelight? In large part, the answer is that no one is looking for them. This Article shines a spotlight on the phenomenon of professional plaintiffs by looking in the most obvious place of all—the public record. This Article relies on publicly available documents to conduct the first examination of professional plaintiffs in shareholder litigation. These documents include court filings from state and federal courts across the country, including many unpublished decisions that have gone unnoticed in legal scholarship. This Article also relies on even less conventional sources, including business registration statements, marriage licenses, and obituaries.

Who are the new professional plaintiffs? Research reveals four possible types of professional plaintiffs in shareholder litigation today. First, the plaintiffs are repeat plaintiffs.[12] They file multiple lawsuits, some allegedly knowing little about the underlying claims. Second, the plaintiffs are attorneys or their family members.[13] Rather than justifying their claims to independent shareholders, many attorneys appear to rely on their spouses, children, and other family members to serve as plaintiffs. Third, the plaintiffs may be entities created, at least in part, for the purpose of filing litigation.[14] Some shareholders may have created partnerships or other entities for the primary purpose of filing litigation. Finally, some plaintiffs may not meet the most basic requirements for filing these lawsuits.[15]

This phenomenon is disturbing, but is it widespread? The short answer is that we do not know. With limited public information, it is impossible to unearth the full extent of these practices. Yet the incentives in shareholder litigation, combined with the data presented here, give reason to believe that there may be a systemic problem, at least among some types of cases. Shareholder litigation is extremely profitable for plaintiffs' attorneys, often resulting in hourly fees of $500 or more.[16] Attorneys cannot file these suits without plaintiffs, a requirement that is considered "one of the most

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passed after the PSLRA, preempts certain types of state law claims. It does not, however, preempt the claims at issue in this Article—shareholder derivative suits and most acquisition class actions. *See* Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat. 3227, 3229 (1998).

12. *See infra* Section II.A.

13. *See infra* Section II.B.

14. *See infra* Section II.C.

15. *See infra* Section II.D.

16. *See* Elliott J. Weiss & Lawrence J. White, *File Early, Then Free Ride: How Delaware Law (Mis)Shapes Shareholder Class Actions*, 57 VAND. L. REV. 1797, 1830 (2004) (noting that for acquisition class action settlements that involved no monetary recovery, the median fee awarded was $472 per hour; for settlements that involved a monetary recovery, the median fee awarded was $1,240 per hour).

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challenging aspects" of a class action.[17] Add to that the fact that defense attorneys and judges rarely inquire into the background of shareholder plaintiffs,[18] and incentives exist for unscrupulous behavior.

These practices also cast a negative light on the vast majority of plaintiffs' law firms that likely do *not* engage in these practices. Hearing about these practices, one could conclude that they are commonplace, even if they are in fact restricted to a fairly small group of firms. Yet, the reputational effects may dissuade legitimate plaintiffs from getting involved in shareholder suits and may ultimately lessen the deterrence value of these suits.

This impact should matter to corporate investors. Litigation plays a crucial role in protecting investors, allowing them to hold corporate managers accountable for their misdeeds. Yet, as the law and economics literature demonstrates, when left to their own devices, plaintiffs' attorneys do not always make decisions that are in the best interests of investors.[19] Instead they can agree to what economists term "non-zero sum" settlements that benefit the plaintiffs' attorney without the defendant incurring any significant loss, while "an absent third party, the corporation, bears the expenses of both sides."[20] These settlements are common in shareholder litigation.[21] Shareholder plaintiffs are the last line of defense against these opportunistic settlements. By design, however, professional plaintiffs do not perform this function.[22] In short, professional plaintiffs are a problem, both for investors and for the legal system more generally.

This Article proceeds in three parts. Part I describes the *old* professional plaintiffs in shareholder litigation, detailing Congress's efforts in the 1990s to eliminate these plaintiffs. Part II describes the *new* professional plaintiffs in shareholder litigation, combining empirical data with a discussion of illustrative cases. Part III builds on this discussion by proposing a new conceptual framework to address the problem of professional plaintiffs in

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17. BRIAN ANDERSON & ANDREW TRASK, THE CLASS ACTION PLAYBOOK 75 (Oxford Univ. Press 2010).

18. *See infra* pp. 37–38.

19. *See* John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 COLUM. L. REV. 669, 671–72 (1986); Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 3–4 (1991); Weiss & White, *supra* note 16, at 1799.

20. For a description of these settlements, *see* John C. Coffee, Jr., *The Unfaithful Champion: The Plaintiff as Monitor in Shareholder Litigation*, 48 LAW. & CONTEMP. PROBS. 5, 25 (1985).

21. *See* Jessica M. Erickson, *Corporate Governance in the Courtroom: An Empirical Analysis*, 51 WM. & MARY L. REV. 1749, 1807–08 (2010); Weiss & White, *supra* note 16, at 1828.

22. Indeed, this problem first came to my attention through the efforts of two investors who had become disillusioned with the law's efforts to protect their financial interests. These two investors have conducted considerable research into the problem of professional plaintiffs in shareholder litigation today, and their work was valuable in assisting my own efforts.

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corporate litigation.

I. The Old Professional Plaintiffs

In corporate litigation and elsewhere, professional plaintiffs have long been criticized as "professional pawn[s]" who help attorneys line their pockets at the expense of the real victims of legal injustice.[23] This criticism was common in the corporate arena prior to the reform of the federal securities laws in 1995.[24] The criticism focused on the most prominent area of corporate litigation—securities class actions. Unlike the state law claims addressed in Part II, securities class actions are brought under federal law. In securities class actions, shareholders typically allege that the corporation lied to the market about its business model or financial results. This Part provides an overview of the problem as it existed prior to 1995, as well as Congress's efforts to solve it.

A. *Historical Critique*

In the 1980s and early 1990s, corporate America claimed to be under attack in courtrooms across the country.[25] Companies claimed that securities class actions were filed within days, or even hours, of a drop in the company's stock price.[26] As one executive asserted, "The duty to investigate has been reduced to perusal of the morning paper."[27] This charge was aimed largely at a single target—professional plaintiffs. This

23. Rodriguez v. Investco, L.L.C., 305 F. Supp. 2d 1278, 1285 (M.D. Fla. 2004); *see also* Gordon v. Virtumundo, Inc., 575 F.3d 1040, 1056–57 (9th Cir. 2009) (noting that some plaintiffs have created "litigation mill[s]" to "seek[] out and captur[e]" unlawful activity to use in their "prolific lawsuits"); Murray v. GMAC Mortg. Corp., 2005 WL 3019412, at *2 (N.D. Ill. Nov. 8, 2005) (denigrating professional plaintiffs as willing to accept a "quick and easy class settlement without the need for actually putting in any real effort representing the proposed class members in this action").

24. These concerns are reflected in the Congressional Record leading up to the passage of the PSLRA. *See supra* note 2.

25. These claims are reflected in dozens of letters that corporations sent to members of Congress , as well as in the testimony of numerous corporate executives. *See, e.g.*, *Securities Litigation Reform Proposals: Hearings Before the Subcomm. on Sec. of the Comm. on Banking, Hous. & Urban Affairs*, 104th Cong. 19–21 (1995) (prepared statement of Christopher J. Murphy III, CEO, 1st Source Corporation); Letter from William E. Foster, Chairman & CEO, Stratus Computer, Inc., to Sen. Edward Kennedy (Dec. 27, 1993) (on file with author); Letter from Thomas M. Walker, CFO of Information Resources, Inc., to the Hon. Carol Moseley-Braun (July 5, 1994) (on file with author).

26. According to statements in Congress, approximately 20% of securities class actions were filed within forty-eight hours of the announcement of bad news. *See Securities Litigation Reform Proposals: Hearings on S.240, S.667, and H.R. 1058 Before the Subcomm. on Sec. of the Comm. on Banking, Hous. & Urban Affairs*, 104th Cong. 118 (1995) (statement of Sen. Peter Domenici).

27. *Supplemental Testimony of Stephen F. Smith, General Counsel and Dir. of Investor Relations of Exabyte Corp. Concerning Litigation Under the Fed. Sec. Laws Before the Subcomm. On Energy and Commerce*, 103d Cong. 503 (1994).

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Section describes the professional plaintiffs who drew the attention of Congress and the courts in the pre-1995 period. As we shall see, the debate regarding these plaintiffs was part of a broader debate about the role of litigation in policing corporate misconduct.

1. Repeat Plaintiffs

The plaintiffs who most provoked Congress's ire in the pre-1995 period were repeat plaintiffs who filed dozens of securities class actions.[28] According to conventional lore, these plaintiffs typically owned a small number of shares in a large number of public companies.[29] These investment portfolios put them in a prime position to file lawsuits against a wide range of companies. As one judge wryly described them, these plaintiffs were "the unluckiest and most victimized investors in the history of the securities business."[30]

Viewed in isolation, repeat plaintiffs are not necessarily problematic. After all, plaintiffs who file multiple lawsuits get experience as class representatives. As a result, they may come to understand more about the underlying allegations in corporate fraud claims. In other words, experience might be a good thing.

In Congress, however, no one seemed to think so. Congress was concerned that repeat plaintiffs were not properly representing the interests of absent class members.[31] Rule 23 of the Federal Rules of Civil Procedure provides that the named plaintiff in a class action must "fairly and adequately protect the interests of the class."[32] In the early 1990s, lawmakers were concerned that repeat plaintiffs were not fulfilling this obligation for two reasons.

First, Congress believed that many repeat plaintiffs knew little about the lawsuits brought in their names.[33] As one congressional report noted, "In many cases the 'lead plaintiff' has not even read the complaint."[34] This fact was problematic because the role of representative plaintiffs is to monitor class counsel, ensuring that litigation decisions reflect the best interests of the class. Shareholder plaintiffs who are not familiar with the underlying claims cannot perform this responsibility. To be fair, Congress may have overstated the role of these plaintiffs. Shareholder plaintiffs often play a nominal role in class action litigation, and many attorneys operate "virtually [as] independent entrepreneur[s]" in a role similar to a private

28. *See, e.g.*, *supra* note 2.
29. *See id.*
30. *In re* Urcarco Secs. Litig., 148 F.R.D. 561, 563 (N.D. Tex. 1993).
31. *See* H.R. Rep. No. 104-369, at 33 (1995).
32. FED. R. CIV. P. 23.
33. *See* H.R. REP. NO. 104-369, at 33 (Conf. Rep.).
34. *See id.*

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attorney general.[35] Yet Congress wanted a greater role for shareholder plaintiffs in securities class actions.

Second, Congress suspected that shareholders were being paid to serve as repeat plaintiffs in securities class actions. In its official legislative report, the House of Representatives stated that "lead plaintiffs often receive compensation in the form of bounty payments or bonuses."[36] The Senate Report similarly stated that "[p]rofessional plaintiffs often are motivated by the payment of a 'bonus' far in excess of their share of any recovery."[37] Such payments created a conflict of interest between the shareholder plaintiff and the rest of the class. While class members want the highest possible recovery, named plaintiffs who have been promised a kickback may be more interested in securing their own personal payout than in protecting the class.

Later investigations proved lawmakers right. The Department of Justice subsequently brought criminal charges against the largest plaintiffs' firm in the country, Milberg Weiss LLP, and four of the firm's attorneys.[38] These charges related almost exclusively to conduct that occurred prior to 1995. During this time period, as the defendants later admitted, the firm maintained a roster of shareholders to serve as plaintiffs in securities class actions.[39] The firm paid those shareholders a portion of the fees that the firms received, typically 10%.[40] According to court documents, "[b]y entering into such secret payment arrangements, [the attorneys] were able to secure a reliable source of individuals who were ready, willing, and able to serve as named plaintiffs in [c]lass [a]ctions that Milberg Weiss wanted to bring."[41] Following the indictments, Milberg Weiss agreed to pay $75 million dollars to settle the criminal charges,[42] and certain partners at the firm agreed to pay substantial fines and go to prison.[43] In short, Congress

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35. Coffee, *supra* note 19, at 681.

36. H.R. REP. NO. 104-369, at 33 (Conf. Rep.).

37. S. REP. NO. 104-98, at 10 (1995).

38. *See* First Superseding Indictment, United States v. Milberg Weiss Bershad & Schulman LLP, CR 05-587(A) (May 18, 2006 C.D. Cal.).

39. Statement of Facts in Support of David J. Bershad Plea Agreement and Information, United States v. Milberg Weiss Bershad & Schulman, CR 05-587(A)-JFW., 2009 BL 152534 ¶ 4 (C.D. Cal. July 6, 2007).

40. *Id.* ¶ 6.

41. *Id.* ¶ 7.

42. *A Stiff Fine, but No Trial, for Milberg*, N.Y. TIMES, June 17, 2008, *available at* http://dealbook.nytimes.com/ 2008/06/17/milberg-firm-said-to-be-near-a-deal/ (explaining that under the firm's latest agreement with prosecutors, the firm will pay the government $75 million).

43. *See, e.g.*, Press Release, U.S. Attorney's Office for the Central District of California, William Lerach, Former Name Partner in Milberg Weiss, to Plead Guilty to Conspiracy to Obstruct Justice and Make False Statements to Federal Judges across U.S. (Sept. 18, 2007) (noting that a former partner agreed to plead guilty; to pay a $250,000 fine; to forfeit $7.75 million to the government; and to receive a one to two year sentence in federal prison); *A Stiff Fine, but No Trial, for Milberg*, *supra* note 42 (explaining that one of the firm's famous partners is in prison

was right when it suspected back in 1995 that at least some plaintiffs were being paid to participate in securities class actions.

2. Lawyers and Their Families as Plaintiffs

During this pre-1995 period, many plaintiffs' lawyers also served as plaintiffs in shareholder suits. There is no empirical data reflecting how often this occurred, but academic scholarship discussed the phenomenon openly. Professor John Coffee observed, for example, that "some plaintiff's law firms [have] even invested their own firm's profit-sharing plan broadly in the stocks of numerous corporations in order to have an in-house plaintiff at hand."[44] He also stated that "[f]requently . . . one plaintiff's attorney will serve as a client for another."[45] Similarly, in 1993, *Fortune Magazine* documented how a well-known plaintiffs' firm had asked another plaintiffs' attorney to "provide the . . . firm with a list of his stock holdings . . . and keep it up to date," allowing the firm to file at least six securities class actions on the attorney's behalf.[46]

As courts have recognized, these cases raised the possibility of a conflict of interest between the attorney plaintiff and the rest of the class. In the 1993 decision *Jaroslawicz v. Safety Kleen Corp.*,[47] for example, a federal court denied plaintiff David Jaroslawicz's motion to serve as class representative in a securities class action.[48] In denying the motion, the court noted that Mr. Jaroslawicz, a personal injury attorney in New York City, had served as co-counsel in at least forty-two other cases with Pomerantz Levy Haudek Block & Grossman (Pomerantz Levy), one of the two firms representing the class.[49] In other words, Mr. Jaroslawicz was represented by Pomerantz Levy in the lawsuit before the court, but was co-counsel with Pomerantz Levy in a number of other suits. As a result, Mr. Jaroslawicz potentially had a significant financial interest in maintaining the goodwill of Pomerantz Levy, which the court feared could overshadow his commitment to the class.[50] The court also stated that the litigation appeared to be "manufactured," and it noted that Mr. Jaroslawicz owned only thirteen and a half shares of stock in the defendant corporation, worth approximately $400.[51]

There was also evidence in the pre-1995 period that lawyers used their family members as plaintiffs. Cases during this period included examples

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and another one is headed there under an announced guilty plea).

44. Coffee, *supra* note 19, at 682.

45. *Id.* at 682–83 n.39.

46. Andrew E. Serwer, *What to Do About Legal Blackmail*, FORTUNE, Nov. 15, 1993, *available at* http://money.cnn.com/magazines/fortune/fortune_archive/1993/11/15/78596/index. htm.

47. 151 F.R.D. 324 (N.D. Ill. 1993).

48. *Id.* at 326.

49. *Id.* at 328.

50. *Id.* at 329–30.

51. *Id.* at 326, 330.

of attorneys using their spouses,[52] parents,[53] siblings,[54] and other close relatives[55] as plaintiffs in securities class actions.

These cases, predictably, raised the ire of the courts. In many cases, courts expressed concern that the plaintiff would share in the eventual attorneys' fees received by their attorney relative, and that these payouts could influence the plaintiff's representation of the class. In one case, for example, a federal court held that a plaintiff was an inadequate class representative because her husband was class counsel.[56] The court determined that "the potential conflict of interest inherent in this situation is obvious" because "the possible recovery of [the plaintiff] as a member of the class is far exceeded by the financial interest she and her husband, as a marital unit, might have in the legal fees engendered by this lawsuit."[57]

3. Entities as Plaintiffs

During this same time period, there were also indications that lawyers may have established entities for the purpose of filing litigation. For example, according to press accounts in 1993, an attorney in New Jersey was suspended from the practice of law for using his own companies as plaintiffs in his lawsuits.[58] The press reported that this suspension arose specifically out of shareholder lawsuits filed against the Trump casinos.[59] The lawsuits were filed by two different entities, Peter Stuyvesant Ltd. and Fairmount Financial Corp., using two different legal theories.[60] An investigation determined that Stuyvesant and Fairmount were in fact related and that both entities were owned by one of the attorneys in the litigation.[61] The court was extremely critical when it discovered this connection, stating that "[c]lass representatives are supposed to occupy a

52. *See, e.g.*, Stull v. Poole, 63 F.R.D. 702, 704 (S.D.N.Y. 1974).

53. *See, e.g.*, Kirby v. Cullinet Software, Inc., 116 F.R.D. 303, 309 (D. Mass. 1987).

54. *See, e.g.*, Susman v. Lincoln Am. Corp., 561 F.2d 86, 95 (7th Cir. 1977).

55. *See, e.g.*, *In re* Consumers Power Co. Secs. Litig., 105 F.R.D. 583, 603 (D. Mich. 1985).

56. *Stull*, 63 F.R.D. at 704.

57. *Id.* As we shall see, this decision has not stopped other members of the firm from relying on their own family members to serve as plaintiffs. *See infra* text accompanying notes 159–77. Other courts raised related concerns even in cases where the plaintiff would not share in the attorneys' fees. *See Susman*, 561 F.2d at 95. On the other hand, a few courts have sanctioned these relationships, holding that the relative was capable of monitoring the litigation given the particular circumstances of the case. *See, e.g.*, Lewis v. Goldsmith, 95 F.R.D. 15, 20 (D.N.J. 1982) (permitting the plaintiff to serve as the class representative even though his uncle was class counsel).

58. *See* L. Stuart Ditzen, *Richard Greenfield Is Barred by U.S. Court for One Year*, PHILADELPHIA ENQUIRER, Dec. 23, 1993, *available at* http://articles.philly.com/1993-12-23/business/25943547_1_federal-courts-class-action.

59. *See* L. Stuart Ditzen, *Class-Action Lawyer Suspended, Fined in N.J. for Ethical Violations*, PHILA. ENQUIRER, Nov. 17, 1993, *available at* http://articles.philly.com/1993-11-17/business/25945045_1_class-action-suits-class-action-lawyer-trump-casinos/2.

60. *See id.*

61. *See id.*

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position of trust, championing the interests of the multitude of persons they represent."[62] The court referred the matter to state disciplinary authorities,[63] and the attorney appears to have been fined and suspended from the practice of law.[64]

B. *The Problems with the Old Professional Plaintiffs*

As the examples above illustrate, lawmakers were aware of a variety of problems with professional plaintiffs prior to 1995. These problems all reflected the same core concern about the plaintiffs' ability to represent absent class members in securities class actions. Plaintiffs with a conflict of interest in the litigation—whether the promise of a private payment or the hope of future business from class counsel—could be tempted to put their own interests ahead of the interests of the class. Such conflicts could make it difficult, if not impossible, for the named plaintiffs to protect the interests of the class.

These conflicts may not appear particularly troubling given the traditional role of shareholder plaintiffs in class action litigation. Conflict of interest or not, these plaintiffs rarely have a meaningful role in the litigation. Shareholder plaintiffs typically have a minimal financial stake in the litigation, and whatever stake they do have is dwarfed by that of the plaintiffs' attorneys who stand to receive significant contingency fees. As a result, one could legitimately ask why Congress was so concerned about professional plaintiffs back in 1995. If plaintiffs rarely played a meaningful role in these cases, why worry about *professional* plaintiffs?

And yet Congress *was* worried. Congress believed that the traditional model of entrepreneurial litigation was broken, at least in securities class actions. In an ideal world, plaintiffs' attorneys protect the interests of absent class members. The legal system tries to accomplish this ideal by awarding plaintiffs' attorneys a percentage of the overall recovery. This fee structure is designed to ensure that plaintiffs' attorneys have an incentive to bargain for the largest possible recovery.

The problem is that these incentives do not always work, as scholars have long recognized.[65] The fact that plaintiffs' attorneys receive a

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62. Ditzen, *supra* note 58.

63. *Id.*

64. *Id.*

65. There is a substantial body of literature on the dangers of a purely entrepreneurial model of shareholder litigation. *E.g.*, John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter is Not Working*, 42 MD. L. REV. 215, 221 n.15 (1983) (discussing issues of risk aversion, potential for collusion, an inadequate system, property rights, and the disparity in search costs); Coffee, *supra* note 19, at 679 (discussing "opportunism and overenforcement"); Bruce Hay & David Rosenberg, *"Sweetheart" and "Blackmail" Settlements in Class Action: Reality and Remedy*, 75 NOTRE DAME L. REV. 1377, 1377–78 (2000) (analyzing issues of sweetheart and blackmail settlements); Alon Klement, *Who Should Guard the Guardians? A New Approach for Monitoring Class Action Lawyers*, 21 REV. LITIG. 25, 38, 72 (2002)

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percentage of the ultimate settlement does not always mean that their incentives are aligned with those of the absent class members. As the research of Professor John Coffee and others has demonstrated, plaintiffs' attorneys have incentives that often cause them to underinvest in certain types of shareholder litigation and overinvest in others.[66] In the types of suits targeted by professional plaintiffs, the concern was that attorneys were *overinvesting* in litigation.

As discussed above, many believed that attorneys in the early 1990s were filing securities class actions based on the hint of wrongdoing.[67] Plaintiffs' attorneys then used securities class actions as a means to obtain discovery from the target corporation. This discovery was typically one-sided, with the plaintiffs' attorneys requesting mountains of documents from the defendants but having little to produce themselves. Many corporations agreed to nuisance settlements to avoid the high cost of discovery and the risk of an unfavorable jury verdict at trial. In the words of the chairman of America Online, Inc., "Even when a company committed no fraud, indeed no negligence, there is still the remote possibility of huge jury verdicts, not to mention the costs of litigation. In the face of such exposure, defendant companies inevitably settle these suits rather than go to trial."[68]

Congress believed that these practices had a negative impact on investors. Shareholder litigation represents a transfer of wealth from one group of shareholders to another.[69] In a securities class action, existing shareholders typically pay former shareholders who bought their stock during the class period.[70] This wealth transfer makes sense if it deters misconduct or disgorges ill-gotten gains. When litigation is filed to procure a nuisance settlement, however, these gains disappear. In the mid-1990s, Congress believed that many securities class actions were strike suits—profitable for attorneys, but not beneficial for investors or the market more generally.

Admittedly, the testimony before Congress reflected a fairly one-sided view of the issues. Corporate America mounted a strong lobbying effort in Congress, and the actual problems may well not have been as serious as the

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(commenting on collusion, sweetheart deals, and settlement inefficiencies).

66. *See* Coffee, *supra* note 65, at 243; Coffee, *supra* note 19, at 686–90. These concerns are not a uniquely American phenomenon. *See* Erik P.M. Vermeulen & Dirk A. Zetzsche, *The Use and Abuse of Investor Suits: An Inquiry into the Dark Side of Shareholder Activism*, 7 EUR. COMPANY & FIN. L. REV. 1, 71–72 (2010), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1428901 (discussing the use of professional plaintiffs in European shareholder litigation).

67. *See supra* pp. 6–7.

68. H.R. REP. NO. 104-50, pt. 1, at 17 (1995).

69. *See* John C. Coffee, Jr., *Reforming the Securities Class Action: An Essay on Deterrence and Its Implementation*, 106 COLUM. L. REV. 1534, 1557–61 (2006); Jill E. Fisch, *Confronting the Circularity Problem in Private Securities Litigation*, 2009 WIS. L. REV. 333, 334 (2009).

70. Coffee, *supra* note 69, at 1557.

companies claimed. Yet even critics of this effort recognized the need for a better monitor of shareholder interest in these suits. For example, Professor Joel Seligman, who argued against widespread legal changes to the federal securities laws, stated that he was "impressed by the testimony" related to professional plaintiffs and agreed that these plaintiffs tended to "undermine the integrity" of the judicial process.[71]

When it comes to identifying a better monitor of shareholder interests, securities class actions enjoy a distinct advantage over other types of class action litigation. In many class actions, the plaintiffs have only a minimal stake in the outcome. A plaintiff who is suing over a $5 free drink coupon likely does not have the financial incentive to monitor the litigation.[72] In securities class actions, however, many shareholders *do* have a significant financial interest in the litigation. Many large investors have millions of dollars at stake in securities class actions, far more than the typical class action plaintiff. Accordingly, shareholder litigation was uniquely situated for reforms that placed more power in the hands of strong shareholder plaintiffs.

C. *Legislative Attack*

The problems in securities class actions ultimately led to broad-based support for new legislation in both houses of Congress. In 1995, Congress passed the Private Securities Litigation Reform Act.[73] The PSLRA did not apply to shareholder suits filed under state law, including shareholder derivative suits and acquisition class actions, but it did place strict limitations on securities class actions filed under federal law.

Most importantly, the PSLRA ended the race to the courthouse in which the attorney with the first-filed complaint would typically receive control over the litigation.[74] Instead Congress established a rebuttable presumption that the investor with the largest financial loss would be the lead plaintiff, a provision that was designed to put these suits in the hands of large institutional investors.[75] As one representative of institutional investors testified before Congress, "As the largest shareholders in most companies, we are the ones who have the most to gain from meritorious

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71. *See Hearings Before the Subcomm. on Telecomms. & Fin.*, *supra* note 1, at 70–72 (1994) (statements of Professor Joel Seligman).

72. *See* Class Action Complaint, Levitt v. Southwest Airlines Co., 846 F. Supp. 2d 956, 957–58 (N.D. Ill. 2012) (explaining that plaintiff, who is also a lawyer at the well-known plaintiffs' firm of Wolf Haldenstein Adler Freeman & Herz LLP, filed a class action challenging Southwest Airline's decision not to honor free drink coupons).

73. Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (1995) (codified as amended in scattered sections of 15 U.S.C.).

74. H.R. REP. NO. 104-369, at 33 (1995) (Conf. Rep.) (stating that this practice caused plaintiffs' attorneys to become "fleet of foot and sleight of hand").

75. 15 U.S.C. § 78u-4(a)(3)(B)(iii)(I)(bb) (2006).

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securities litigation."[76]

The PSLRA also included provisions aimed directly at professional plaintiffs. The Act provided that no plaintiff shall serve in more than five securities class actions in a three-year period.[77] Additionally, plaintiffs were barred from receiving any compensation other than their pro rata share of the recovery and reimbursement for reasonable costs and expenses.[78] Finally, plaintiffs were required to file a sworn statement with the complaint certifying that they (1) had reviewed the complaint and authorized its filing, (2) had not purchased the securities at the direction of counsel or to participate in a lawsuit, and (3) were willing to serve on behalf of the class.[79] The certification also had to list any transactions in the securities during the class period and identify any other lawsuits in which the plaintiff had sought to serve as lead plaintiff over the past three years.[80] These restrictions were designed to put securities class actions in the hands of plaintiffs with a real financial stake in the litigation.

The relief that corporate America felt following the passage of the PSLRA was short-lived. The PSLRA only applies to fraud claims brought under the federal securities laws.[81] Lawyers quickly learned that they could make nearly the same allegations under state law and thereby avoid the strict requirements of the PSLRA. Armed with this statutory loophole, plaintiffs' attorneys took their old tactics to a new venue.

Just a few years after the passage of the PSLRA, Congress was presented with compelling evidence that its efforts had simply shifted the problems to state court.[82] While the number of securities fraud cases filed in federal court had declined, there was an equal increase in the number of state law securities fraud cases.[83] In California alone, the number of state securities class action filings in the first six months of 1996 was almost five times greater than in the first six months of 1995.[84] The SEC called this shift potentially "the most significant development in securities litigation" since passage of the PSLRA.[85] The SEC's testimony prompted Congress to pass the Securities Litigation Uniform Standards Act (SLUSA)[86] in 1998. The SLUSA expressly preempted many state law

76. H.R. REP. NO. 104-369, at 34 (Conf. Rep.).

77. 15 U.S.C. § 78u-4(a)(3)(B)(vi).

78. *Id.* § 78u-4(a)(2)(A)(vi).

79. *Id.* § 78u-4(a)(2)(A)(i)–(iii).

80. *Id.* § 78u-4(a)(2)(A)(iv)–(v).

81. *Id.* §78u-4(b).

82. H.R. REP. NO. 105-803, at 14–15 (1998) (Conf. Rep.).

83. *See id.* at 14 (citation omitted).

84. *Id.* at 15. (The first six months of 1995 were prior to the passage of the PSLRA.)

85. U.S. SECURITIES AND EXCHANGE COMM'N OFFICE OF THE GENERAL COUNS., REPORT TO THE PRESIDENT AND THE CONGRESS ON THE FIRST YEAR OF PRACTICE UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995 (1997).

86. Securities Litigation Uniform Standards Act of 1998, Pub. L. No. 105-353, 112 Stat.

fraud claims, preventing attorneys from filing the same suits under a different body of law.

The SLUSA, however, included a carve-out that has proven crucial in the subsequent revival of professional plaintiffs—it exempted all shareholder derivative suits and many acquisition class actions.[87] A shareholder derivative suit is a suit filed under state law to vindicate alleged wrongs committed against the corporation.[88] The typical claim is that the corporation's managers harmed the corporation by breaching their fiduciary duties to the corporation. Acquisition class actions are also brought under state fiduciary duty law, but the allegations relate specifically to a proposed merger or acquisition. In these suits, the shareholders typically allege that the corporation's board of directors breached its fiduciary duties by agreeing to sell the corporation for a price below the corporation's true value.[89] Congress likely spared these suits from preemption because it was focused on the more traditional fraud claims that shareholders were filing to avoid the PSLRA.[90]

With the passage of the SLUSA, Congress believed that its work in this area was finally complete. The PSLRA targeted abusive practices in securities litigation, and the follow-up legislation in 1998 gave the necessary teeth to the PSLRA's restrictions.

This legislation has accomplished many, but certainly not all, of its stated goals. Today, institutional investors—primarily labor and public pension funds—serve as the lead plaintiffs in approximately two-thirds of all securities class actions.[91] The role of these plaintiffs, however, many of whom have become repeat plaintiffs themselves, has not been without controversy.[92] Studies show that they have been able to obtain slightly

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3227 (enacted to amend the Securities Act of 1933 and the Securities Exchange Act of 1934).

87. *See* 15 U.S.C. § 77p(d), (f)(2)(B) (2006).

88. Aronson v. Lewis, 473 A.2d 805, 811 (Del. 1984).

89. In recent years, the lines between these suits have begun to blur. My own research shows that many derivative complaints now include federal securities claims. Erickson, *supra* note 21, at 1774. Other commentators have noted the rise of federal claims in acquisition class actions. *See* Kevin LaCroix, *A Closer Look at 2011 Securities Lawsuit Filings*, THE D&O DIARY (Jan. 3, 2012), http://www.dandodiary.com/2012/01/articles/securities-litigation/a-closer-look-at-2011-secu rities-lawsuit-filings/ (stating that more than one quarter of all securities class actions in 2011 related to mergers or acquisitions).

90. In addition, these suits have traditionally been within the province of state law, and Congress may have been hesitant to extend its reach in this area any more than necessary. *See, e.g.*, H.R. REP. NO. 105-640, at 17 (1998) (noting that the SLUSA includes "an exception to preserve [s]tate court jurisdiction over derivative actions").

91. Ellen M. Ryan & Laura E. Simmons, *Securities Class Action Settlements: 2010 Review and Analysis*, CORNERSTONE RESEARCH, at 8 (2011), http://www.cornerstone.com/files/News/029 b31a7-ff84-4000-b1ff-d177014ced27/Presentation/NewsAttachment/fd13e1e4-5564-4d46-86a3-882f232147a9/Cornerstone_Research_Settlements_2010_Analysis.pdf.

92. Scholars, for example, have raised concerns that plaintiffs' attorneys may make substantial campaign contributions to politicians who oversee labor and public pension funds in the

better settlements for shareholders, at least in part vindicating Congress's faith in them.[93]

In the wake of these legislative reforms, concerns about individuals serving as professional plaintiffs faded from view. There has been no examination of professional plaintiffs in corporate law scholarship since 1995.[94] As we shall see, however, the legal system has not won the war against professional plaintiffs. Instead these plaintiffs may have simply moved into new legal territory.

II. THE NEW PROFESSIONAL PLAINTIFFS

As this Part documents, professional plaintiffs may be alive and well in shareholder litigation. And they appear to be using many of the same practices that Congress thought it eradicated back in the 1990s. In the wake of the legislative reforms, professional plaintiffs shifted into state law shareholder suits, specifically, acquisition class actions and shareholder derivative suits. The discussion below groups these practices, and the allegations that relate to them, into four categories: (1) using the same shareholders in multiple lawsuits; (2) using plaintiffs' lawyers or their family members as plaintiffs; (3) using questionable entities as plaintiffs; and (4) using shareholders who may not meet the basic qualifications to serve as plaintiffs, including dead plaintiffs and plaintiffs who may not know they are plaintiffs. These phenomena have flown under the radar of corporate law scholarship and raise questions about the legitimacy of these lawsuits.

An introductory caveat is important. This Article defines "professional plaintiffs" to include the four types of plaintiffs above. The use of this term does not imply anything about the plaintiffs' involvement in these suits or their motivation for filing these suits. Similarly, to the extent that the

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hopes of representing these funds in securities suits. *See, e.g.*, Stephen J. Choi et al., *The Price of Pay to Play in Securities Class Actions*, 8 J. EMPIRICAL LEGAL STUD. 650, 650–51 (2011); James D. Cox & Randall S. Thomas, *Does the Plaintiff Matter? An Empirical Analysis of Lead Plaintiffs in Securities Class Actions*, 106 COLUM. L. REV. 1587, 1611–14 (2006).

93. The empirical evidence is somewhat mixed, but it generally shows that institutional investors have had a positive impact on settlement values. *See* Stephen J. Choi et al., *Do Institutions Matter? The Impact of the Lead Plaintiff Provision of the Private Securities Litigation Reform Act*, 83 WASH. U. L. Q. 869, 870 (2005) (finding that participation by public pension funds correlates with a greater likelihood of a high value outcome but not willing to claim finding as conclusive); James D. Cox et al., *There Are Plaintiffs and . . . There are Plaintiffs: An Empirical Analysis of Securities Class Action Settlements*, 61 VAND. L. REV. 355, 385 (2008); Ryan & Simmons, *supra* note 91, at 8.

94. The one notable exception is the research on acquisition class actions published by Robert Thompson and Randall Thomas in 2004. *See* Robert B. Thompson & Randall S. Thomas, *The New Look of Shareholder Litigation: Acquisition-Oriented Class Actions*, 57 VAND. L. REV. 133, 187–89 (2004). In their article, Thompson and Thomas report detailed findings on the plaintiffs in acquisition class actions filed in the Delaware Court of Chancery in 1999 and 2000. These findings are discussed below.

discussion below relies on allegations raised in various lawsuits, the veracity of these allegations generally cannot be determined from the available record. In the end, therefore, the illustrations and allegations below do not, and indeed could not, cast aspersions on any particular plaintiffs or on the plaintiffs in corporate litigation more generally. The most they can do is illustrate that many of the practices targeted by Congress may still occur today.

A. *Repeat Plaintiffs*

In enacting the PSLRA, Congress criticized repeat plaintiffs in securities class actions as the "world's unluckiest investors."[95] As this Section illustrates, this bad luck has apparently continued. Although the PSLRA largely halted the use of repeat plaintiffs in federal securities class actions,[96] the use of repeat plaintiffs has continued in shareholder lawsuits filed under state law. This Section provides empirical data regarding the use of repeat plaintiffs before turning to illustrative cases that highlight this practice.

1. Empirical Data

To understand the role of repeat plaintiffs in shareholder litigation today, one must first understand what is meant by a "repeat plaintiff." This Section uses the following definition: a shareholder is a repeat plaintiff if he or she filed more than *three* shareholder suits over the period between 2009 and 2012 or *five* shareholder suits over the period between 2002 and 2012. This definition identifies plaintiffs who are regular filers of these suits, while also giving more scrutiny to plaintiffs who have filed multiple lawsuits in recent years.

I used several methods to track these repeat plaintiffs.[97] First, I used data collected as part of a prior empirical study on shareholder litigation in federal court.[98] Second, I supplemented that data with additional data on state law shareholder suits in both state and federal court.[99] Third, I used

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95. H.R. REP. NO. 104-369, at 32 (1995) (Conf. Rep.).

96. As discussed below, repeat plaintiffs still play a small role in securities class actions, although the exact nature of this role is unclear.

97. This effort, while data-driven, was not intended to identify all repeat plaintiffs. Online state and federal docket systems are often woefully incomplete, making it impossible to identify all shareholder suits filed by these plaintiffs. *See* Bernard Black et al., *Is Delaware Losing Its Cases?*, at 17, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1578404 (noting that these limitations mean that it is simply "not feasible" to examine all corporate law cases).

98. This data covered shareholder derivative suits filed in federal court in 2005 and 2006. *See* Erickson, *supra* note 21, at 1757–58.

99. I conducted a number of searches in the dockets database and the pleadings database in Westlaw to identify suits filed by repeat plaintiffs between 2002 and 2012. I also searched in the EDGAR database, which includes filings with the Securities & Exchange Commission by publicly traded corporations, for the names of many of these plaintiffs.

data on federal securities class actions, which was generously provided by Cornerstone Research, Stephen Choi, and Adam Pritchard.[100] This combined data, while not a complete list of all shareholder suits, allowed me to identify a significant number of repeat plaintiffs. I then searched for these plaintiffs in the Dockets database in Westlaw to get a more precise count of the suits that they filed between 2002 and 2012.[101]

In doing so, I uncovered more than 700 lawsuits filed by repeat plaintiffs during this ten-year period. These lawsuits were filed by more than sixty repeat plaintiffs who filed an average of eleven lawsuits each.[102] These plaintiffs were not always the only plaintiffs in these lawsuits. Many shareholder lawsuits have multiple plaintiffs, and in many cases, more than one repeat plaintiff filed a lawsuit against a single company. These figures thus reflect the pervasiveness of repeat plaintiffs in shareholder litigation.

These suits were primarily filed under state law. As Table 2 below illustrates, nearly half of these suits (47.8%) were acquisition class actions. Another 29.3% were shareholder derivative suits. A smaller percentage of these suits (16.8%) were securities class actions, indicating that repeat plaintiffs do still exist in these suits as well. The remaining suits were other types of shareholder lawsuits or could not be categorized based on the information available.[103]

This mix is changing over time. Between 2010 and 2012, nearly 65 percent of cases involving repeat plaintiffs were acquisition class actions, up from approximately 35 percent between 2002 and 2009. The increasing use of repeat plaintiffs in these cases likely reflects the fact that acquisition class actions have skyrocketed in popularity in recent years, forcing plaintiffs' firms to maintain a larger stable of shareholders willing to serve as plaintiff at a moment's notice.

A few of these plaintiffs are well-known to corporate lawyers. Alan R. Kahn, for example, has been termed a "quasi-mythical figure[]" by the Delaware Court of Chancery.[104] He has served as the plaintiff in many landmark Delaware decisions,[105] several of which involve controlling

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100. This data identifies the lead plaintiff or first-filed plaintiff in securities class actions filed between 2002 and 2011. I used this data because many plaintiffs who file securities class actions also file state law shareholder suits.

101. Given the limitations of these databases, these searches are necessarily underinclusive and, accordingly, the numbers presented throughout this Subsection are only estimates.

102. These figures do not include plaintiffs' attorneys or their family members who serve as plaintiffs. Nor do they include institutions who serve as plaintiffs in multiple suits. Such plaintiffs are discussed separately in subsequent sections.

103. In many securities class actions involving repeat plaintiffs in my study, the repeat plaintiff owned a relatively small number of shares in the target corporation and typically did not seek appointment as lead plaintiff.

104. *In re* Revlon, Inc. S'holders Litig., 990 A.2d 940, 943 n.3 (Del. Ch. 2010).

105. *See, e.g.*, Kahn v. Tremont Corp., 694 A.2d 422 (Del. 1997); Kahn v. Lynch Commc'n Sys., Inc., 669 A.2d 79 (Del. 1995); Kahn v. Sullivan, 594 A.2d 48 (Del. 1991).

shareholder transactions, an area in which shareholders are particularly vulnerable. Based on the publicly available data reviewed here, Mr. Kahn or members of his family have filed forty-five lawsuits over the past ten years.[106]

Yet there are many more repeat plaintiffs who have not captured the attention of courts and commentators. Doris and Steven Staehr, for example, appear to have filed more shareholder suits than any plaintiff in my study other than Alan Kahn—a total of forty lawsuits.[107] Yet, in discussions with defense counsel, few recognized their names. Nor have the Staehrs drawn the attention of judges. The same is true for most of the other repeat plaintiffs in my data set. These plaintiffs may have filed ten, twenty, or even thirty lawsuits, but they rarely attract scrutiny. The next question is whether they *deserve* scrutiny.

2. Concerns about Repeat Plaintiffs

Should the legal system care about repeat plaintiffs? Many repeat plaintiffs may well be faithful stewards of shareholder interests, but as Judge Frank Easterbrook observed, a repeat plaintiff "could be tempted to file suits designed to extract payoffs from the corporation even if the average investor will lose in the process."[108] My research uncovers two specific reasons for this concern. First, some repeat plaintiffs appear to have little involvement in the suits filed on their behalf. Second, there are allegations that at least a few plaintiffs have been paid in exchange for lending their names to litigation. These concerns are unsubstantiated, but nonetheless mirror Congress's concerns in the 1990s, raising serious questions about the ability of some repeat plaintiffs to protect absent class members.

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106. My data indicates that between 2002 and 2012, Mr. Kahn personally filed forty-two shareholder lawsuits. His wife and daughter have filed an additional three. Mr. Kahn has a long history in the investing community, and he appears motivated by a strong commitment to corporate governance.

107. *See, e.g.*, Verified Shareholder Derivative Complaint for Breach of Fiduciary Duty, Waste of Corporate Assets and Unjust Enrichment, Staehr v. Miller, No. 1:08-cv-20990-PAS (S.D. Fla. Apr. 11, 2008); Verified Shareholder Derivative Complaint for Breach of Fiduciary Duty, Waste of Corporate Assets, Unjust Enrichment and Violations of the Securities Exchange Act of 1934, Staehr v. Essner, No. 1:07-cv-10465-RJS (S.D.N.Y. Nov. 20, 2007); Verified Shareholder Derivative Complaint for Breach of Fiduciary Duty, Abuse of Control, Constructive Fraud, Gross Mismanagement, Waste of Corporate Assets, Unjust Enrichment, Breach of Fiduciary Duties and for Violations of the Sarbanes-Oxley Act of 2002, Staehr v. Burns, No. 3:06-cv-07069-JGC (N.D. Ohio Mar. 2, 2006). The relationship between Doris and Steven Staehr is not clear, but they may be mother and son.

108. Murray v. GMAC Mortg. Corp., 434 F.3d 948, 954 (2006). Again, my goal is not to criticize all shareholder plaintiffs or even all shareholder plaintiffs who file a significant number of lawsuits. Some shareholder plaintiffs take a very active role in litigation and serve as effective monitors. My concern, as outlined below, is that others may not perform this role and that the judicial system does little to distinguish between these two types of shareholder plaintiffs.

a. Little Involvement in Litigation

Some repeat plaintiffs appear to have very little involvement in the underlying litigation. Courts have long recognized that plaintiffs in shareholder lawsuits are "nominal" plaintiffs and that attorneys therefore control the suits.[109] Yet, shareholder plaintiffs still have a duty to monitor the litigation and exercise control over their attorneys.[110] Some plaintiffs in my study appear to be fulfilling this role diligently. Others may not be.

In one case, for example, a federal judge in the Southern District of New York castigated plaintiff Robert Garber for being "appallingly ignorant of the many derivative actions that have been filed in his name."[111] Mr. Garber had filed more than twenty shareholder lawsuits against corporations and their managers.[112] When questioned about these cases, Mr. Garber "generally could not recall basic information" about them, including where the suits were filed, the basic allegations in the suits, or in some instances, the corporations named as defendants.[113] The court noted that the record in the case was "startling" and reflected an "absentee plaintiff[]" who was "at the beck and call of his friend and fellow attorney [Alfred G.] Yates."[114]

The Delaware Court of Chancery has raised similar concerns about another shareholder plaintiff with an "uncanny zeal for litigation."[115] The court stated that it was "troubl[ed]" by the plaintiff's participation in the suit because he owned only twenty-five shares of stock in the corporation, which were purchased after the initial allegations of wrongdoing had already emerged.[116] Moreover, the court noted that the plaintiff had a "surprising level of ignorance with respect to other lawsuits in which he is a representative plaintiff."[117] The court stated that it could not "conclude that [the plaintiff] is in cahoots with his counsel to generate class and derivative litigation in bad faith. Yet when a person jumps in the ocean and then complains of getting wet, one certainly has to wonder."[118]

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109. Coffee, *supra* note 19, at 674, 678 (referencing courts' emphasis that plaintiff's attorneys have "no 'true' identifiable client").

110. *Cf.* Jaroslawicz v. Safety Kleen Corp., 151 F.R.D. 324, 328–30 (N.D. Ill. 1993) (rejecting adequacy of representation in part because of plaintiff's desire to maintain goodwill with counsel, which could lead to sub-optimal class outcome).

111. *In re* JPMorgan Chase & Co. S'holder Derivative Litig., No. 1:08-cv-00974-DLC, 2008 WL 4298588, at *9 (S.D.N.Y. Sept. 19, 2008).

112. The exact number of suits is unclear. He testified in the JPMorgan litigation that he has filed "approximately twenty-five other actions against corporations and their officers." *Id.* at *5. My research found that he has filed approximately twenty suits in the last ten years.

113. *See id.*

114. *See id.* at *8–9.

115. *In re* Fuqua Indus. Inc. S'holder Litig., 752 A.2d 126, 134 (Del. Ch. 1999).

116. *Id.* n.27.

117. *Id.* (emphasis omitted).

118. *Id.* (some punctuation omitted). Despite these concerns, the court declined to disqualify

My research highlights two reasons to wonder about the involvement of some repeat plaintiffs. First, certain plaintiffs filed many of their lawsuits within a fairly short period of time. For example, one plaintiff filed more than two dozen lawsuits in 2011 and 2012.[119] Another plaintiff appears to have filed nine lawsuits in 2006 and seven lawsuits in 2007. The fact that these plaintiffs have a significant number of suits pending at once may raise questions about their ability to monitor these suits.[120]

Second, several repeat plaintiffs appear to own a relatively small number of shares in the companies they sue.[121] This is not always the case; some repeat plaintiffs own thousands of shares.[122] In many cases, however, the plaintiff appeared to own a fairly small number of shares in the target corporation—as little as nine shares of stock.[123]

b. Alleged Payments to Plaintiffs

Repeat plaintiffs also raise concerns because of allegations that some have been paid to participate in litigation, allegations that resemble those from the pre-PSLRA period. One example can be found in *Carrigan v.*

Mr. Freberg as a plaintiff in the suit, holding that he "does in fact understand the basic nature of the derivative claims brought in his name, even if barely so." *Id.* at 134.

119. For a selection of these suits, see Coyne v. Morton's Rest. Group, Inc., No. 7128 (Dec. 20, 2011); Verified Class Action Complaint, Coyne v. RightNow Techs., Inc., No. 6996 (Del. Ch. Oct. 28, 2011).

120. *See* Egelhof v. Szulik, No. 04 CVS 11746, 2008 WL 352668, at *4 (N.C. Super. Ct. Feb. 4, 2008) *aff'd in part, rev'd in part on other grounds sub nom.* Egelhof *ex rel.* Red Hat, Inc. v. Szulik, 193 N.C. App. 612 (2008) ("While the size of ownership is not determinative of standing, a potential plaintiff's lack of a real financial stake in the litigation is a warning sign that he or she may not be willing or able to devote the time necessary to fulfill the fiduciary obligations imposed by law on a shareholder derivative plaintiff.").

121. I am relying on a small sample of cases here because shareholder plaintiffs are generally not required to disclose the number of shares that they own. Securities class actions are an exception because the PSLRA requires plaintiffs to disclose "all of the transactions of the plaintiff in the security that is the subject of the complaint during the class period specified in the complaint." 15 U.S.C. § 78u-4(a)(2)(A)(iv) (2006).

122. For example, Mr. Kahn, who is referenced above, alleged in a complaint challenging the acquisition of 3Com Corporation that he owned 47,000 shares of stock in the company—a sizable amount under any definition. Verified Class Action Complaint, Kahn v. 3Com Corp., No. 5087, at 2 (Del. Ch. Nov. 18, 2009); *see also, e.g.*, Plaintiff Jean Marie Cinotto's Declaration in Support of Motion for Lead Plaintiff and Appointment of Lead Counsel, Cinotto v. Kavanaugh, No. 2:08-cv-01998-CWH, at 3 (D.S.C. July 17, 2008) (alleging that plaintiff and her husband owned 10,000 shares in the target corporation).

123. *E.g.*, Certification Pursuant to Federal Securities Laws, Ex. A to Shareholder Class Action Complaint, Pinchuck v. Termeer, No. 1:10-cv-11776, at 4 (D. Mass. Oct. 18, 2010) (stating that Mr. Pinchuck purchased 9 shares of stock in the target corporation during the class period); Mercier v. Inter-Tel Inc., 929 A.2d 786, 788 (Del. Ch. 2007) (stating that Mr. Mercier owned 100 shares of stock in the target corporation); Affidavit of Dan Himmel in Support of Moving Plaintiffs' Motion to Appoint Lead Plaintiff, Lead Counsel, and Liason Counsel, Himmel v. Borne, No. 3:10-cv-00441-BAJ-SCR, at ¶ 3 (M.D. La. July 2, 2010) (stating that Mr. Himmel owned 101 shares of stock in the target corporation).

Solectron Corporation, a case filed in the Superior Court of California.[124] In that case, the plaintiff Richard Carrigan challenged the proposed acquisition of Solectron Corporation by Flextronics International Ltd.[125] Mr. Carrigan may have business ties to Steven Staehr,[126] the plaintiff who together with a relative filed more shareholder suits than nearly anyone else in my study.[127] Mr. Carrigan was originally represented in the suit by the same law firm that represented the Staehrs in many of their cases.[128]

Early in the litigation, the defendants suggested that Mr. Carrigan may have been paid for his involvement in the litigation. In their answer, they alleged that "[o]n information and belief, Richard Carrigan has received improper personal benefits through this lawsuit or through his prior service as a class representative in securities class action lawsuits or other relationships with plaintiff's counsel or their affiliates."[129]

Later in the litigation, things changed. Mr. Carrigan became embroiled in a disagreement with his former law firm. This split prompted Mr. Carrigan to file a declaration in mid-2011 in which he alleged that his former law firm had sought to protect Steven Staehr at the expense of the shareholder class in the *Solectron* suit.[130] In his declaration, Mr. Carrigan stated explicitly that he had "personal knowledge" that the law firm had paid Mr. Staehr "hundreds of thousands of dollars to act as a plaintiff in over 30 cases."[131] In short, the defendants accused Mr. Carrigan of being paid to serve in the Solectron lawsuit, and Mr. Carrigan accused Mr. Staehr

124. Complaint Based on Self-Dealing and Breach of Fiduciary Duty, Carrigan v. Solectron Corporation, No. 1:07-cv-087219, at ¶ 1 (Cal. Super. Ct. June 4, 2007).

125. *Id.*

126. Mr. Carrigan and Mr. Staehr have invested in some of the same companies. By itself, this would not mean much. But these companies appear to be quite small, with stock that was not publicly traded at the time they originally invested, suggesting that the two may know each other. *See, e.g.*, Grant Enterprises, Inc., Amendment No. 6 to Form SB-2, Registration Statement under the Securities Act of 1933, at 5–6 (Nov. 2, 2006) (disclosing that the company was controlled by Mr. Carrigan and had a total of forty-one investors, including Mr. Carrigan and Mr. Staehr); Eastern Services Holdings, Inc., Amendment No. 6 to Form SB-2, Registration Statement under the Securities Act of 1933 (Sept. 20, 2006) (disclosing that Mr. Carrigan was the sole employee of the main subsidiary of the company, which provides tax consultation to casinos, and that the company had only forty-one shareholders at that time, including Mr. Carrigan and Mr. Staehr).

127. *See supra* note 107 and accompanying text.

128. *Compare* Complaint Based upon Self-Dealing and Breach of Fiduciary Duty, Carrigan v. Solectron Corporation, No. 1:07-cv-087219, at 15 (Cal. Super. Ct. June 4, 2007) (identifying Robbins Umeda & Fink LLP as Mr. Carrigan's counsel), *with* Docket, Staehr vs. Chizen, No. 1:06-cv-072922 (Cal. Super. Ct. Oct. 13, 2006) (identifying Robbins Umeda & Fink LLP as Mr. Staehr's counsel).

129. Defendants' Amended Answer to Revised Third Amended Complaint, Carrigan v. Solectron Corp., No. 1:07-cv-087219, at ¶ 60 (Cal. Super. Ct. Aug. 14, 2009).

130. *See id.*

131. *See* Declaration of Richard Carrigan in Support of Plaintiff and Class Representative's Response to Court's Order to Show Cause, Carrigan v. Solectron Corp., No. 1:07-cv-087219, at ¶¶ 1, 7 (Cal. Super. Ct. Aug. 5, 2011).

of being paid to serve in other lawsuits.[132]

The law firm vehemently denies both sets of allegations.[133] In addition, the context of the dispute raises questions about the accuracy of Mr. Carrigan's allegations. The law firm was in a dispute with the lawyer who had been Mr. Carrigan's contact at the firm, and there appears to have been bad blood between the individuals involved. Nor did Mr. Carrigan explain in his declaration how he knew about the alleged payments to Mr. Staehr or offer supporting details. As a result, one cannot say with any certainty whether such payments in fact occurred. The allegations, however, certainly raise troubling questions.

On the other side of the country, another public fight between attorneys has uncovered allegations of payments to plaintiffs. In 2011, two plaintiffs' attorneys in New York sued a third plaintiffs' attorney. The defendant was allegedly a so-called referral attorney, an attorney who refers shareholder plaintiffs to other lawyers who then perform much of the litigation work in the suits.[134] The lawsuit concerned, among other things, the payment of these referral fees.[135] During the legal battle, the plaintiffs alleged that the referral attorney had, without their knowledge, "paid [an individual] with the goal of inducing him to serve as a plaintiff."[136] The defendant denied this allegation, but the parties dismissed the case before the court could investigate these allegations.[137] As in the *Solectron* litigation, it is impossible to know whether this plaintiff was in fact paid for participating in litigation, at least based on the public record alone. The point here is that there were allegations that such payments occurred and there was no judicial investigation of the allegations.

The two cases above allege direct payments to plaintiffs. Other cases raise the possibility of indirect benefits. For example, some repeat plaintiffs are attorneys themselves whose practices may depend in part on referrals.[138] Recall the *Safety Kleen* decision discussed above in Part I.[139] In that pre-PSLRA decision, the court denied the plaintiff David Jaroslawicz's motion to serve as class representative because he had served as co-counsel in dozens of cases with class counsel Pomerantz Levy.[140] In other words, he was an inadequate class representative because he had a

132. *See id.*

133. See Telephone Interview with Craig W. Smith, Robbins Arroyo LLP (Feb. 22, 2013).

134. First Amended Complaint, Jacobs v. Harris, No. 650637/2011, at ¶ 14 (N.Y. Sup. Ct. Apr. 22, 2011).

135. *See id.*at ¶ 29.

136. *Id.* at ¶ 10 (emphasis omitted).

137. *See* Dismissal Order with Prejudice, Jacobs et al. v. Harris, No. 650637/2011, at ¶ 3 (N.Y. Sup. Ct. Sept. 6, 2011).

138. An even larger number of the plaintiffs are attorneys in shareholder lawsuits or related to attorneys in shareholder lawsuits. These attorneys are discussed separately in the next section.

139. *See supra* pp. 8–9.

140. Jaroslawicz v. Safety Kleen Corp., 151 F.R.D. 324, 330 (N.D. Ill. 1993).

significant business relationship with the law firm that was representing the class.[141]

This decision was handed down nearly twenty years ago, but Mr. Jaroslawicz continues to serve as a plaintiff in shareholder lawsuits.[142] According to my research, he has served as a plaintiff in approximately a dozen shareholder lawsuits over the last ten years.[143] His counsel in many of these suits is Pomerantz Haudek Grossman & Gross LLP,[144] which appears to be related to the firm that represented Mr. Jaroslawicz in the *Safety-Kleen* litigation (Pomerantz Levy). It appears that Mr. Jaroslawicz still serves as co-counsel with Pomerantz Haudek Grossman & Gross LLP in other litigation.[145] In other words, there is reason to believe that a relationship similar to the one that concerned the court back in 1993 still exists. As we shall see, the same can be said for other problems identified in the pre-1995 period.

B. *Lawyers and Their Families as Plaintiffs*

A second category of professional plaintiffs involves the use of plaintiffs' attorneys and their families as plaintiffs. This Section presents empirical data on the use of these plaintiffs and then turns to specific examples that illustrate the phenomenon.

1. Empirical Data

To find plaintiffs' attorneys who have served as plaintiffs, I first

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141. *Id.*

142. For a sampling of these cases, see Summons, Jaroslawicz v. Transatlantic Holdings, Inc., No. 651718/2011 (N.Y. Sup. Ct. June 21, 2011); Jaroslawicz v. Hambrick, No. 1:1-cv-000886 (Ohio Ct. Com. Pl. Apr. 6, 2011); Abramoff v. Pien, Case No. RG05232060 (Ca. Super. Ct. Sept. 12, 2005). In addition, a plaintiff who appears to be his wife has also filed multiple lawsuits. *See, e.g.*, Nadoff v. Medco Health Solutions, No. 2:11-cv-04248 (D.N.J. July 22, 2011); Nadoff (as custodian for Michael Seth Jaroslawicz) v. Wolford, No. CGC-10-505737 (Cal. Super. Ct. Dec. 1, 2010); Nadoff v. McDaniel, No. 08116438 (Dec. 9, 2008). In at least one of these suits, her husband is listed as one of the attorneys representing the putative class. *See, e.g.*, Complaint and Demand for Jury Trial, Nadoff v. Medco Health Solutions, No. 2:11-cv-04248, at 20 (D.N.J. July 22, 2011) (listing David Jaroslawicz as an attorney).

143. *See id.*

144. *See* Complaint, Jaroslawicz v. Transatlantic Holdings, Inc., No. 651718/2011, at 18 (N.Y. Sup. Ct. June 21, 2011) (listing Pomerantz Haudek as counsel); Shareholder Class Action Complaint, Jaroslawicz v. Lavin, No. 1:10-cv-06815, at 22 (N.D. Ill. Oct. 22, 2010). The firm is now called Pomerantz Grossman Hufford Dahlstrom & Gross LLP.

145. *See* Class Action Complaint, Spataro v. Lincoln Nat'l Corp., No. 11-cv-2035, at 14 (S.D.N.Y. Mar. 23, 2011) (ERISA class action complaint listing both Pomerantz Haudek Grossman & Gross LLP and Jaroslawicz & Jaros LLC as counsel); Class Action Complaint, CLAL Finance Mutual Fund Mgmt., Ltd. v. JPMorgan Chase & Co., No. 10-cv-8392, at 23 (S.D.N.Y. Nov. 5, 2010) (Commodity Exchange Act complaint listing same two firms, among others, as counsel); Class Action Complaint, Randolph-Rand Corp. v. YKK Corp., No. 07-cv-10324–DC, at 18 (S.D.N.Y. Nov. 14, 2007) (antitrust class action complaint listing same two firms as counsel).

identified law firms that regularly represent plaintiffs in shareholder litigation.[146] I then searched for the names of the attorneys at these firms in the Dockets database in Westlaw. This search revealed more than fifty cases in which plaintiffs' attorneys appear to have served as plaintiffs between 2002 and 2012.[147]

Much more difficult is identifying plaintiffs' lawyers' family members who have served as plaintiffs. Lawyers do not typically make their family trees available online (with one notable exception described below). As a result, I uncovered cases involving family members largely by chance.[148] Still, my research reveals approximately fifty more shareholder lawsuits since 2002 brought by plaintiffs who appear to be family members of plaintiffs' attorneys. Whether these suits are only a drop in a much larger bucket is unclear. At a minimum, however, plaintiffs' attorneys or family members of plaintiffs' attorneys appear to have filed more than 100 lawsuits since 2002.

Should this phenomenon disturb us? Some may argue that there is nothing wrong with these attorneys or their family members serving as plaintiffs. After all, attorneys can be victims of corporate misconduct, and they should be able to use the legal system to redress their harms. Indeed, plaintiffs' attorneys are presumably more likely to recognize corporate misconduct because they battle against it every day. And they are more familiar with the litigation process and therefore may be able to provide better oversight of the litigation.

Even so, there is reason to be skeptical. As courts have long recognized, shareholder plaintiffs are supposed to serve as an independent check on the litigation, ensuring that the lawsuit is in the best interests of the corporation and its shareholders.[149] It is obviously difficult to perform this role when the attorney is one's spouse or close family member.[150] Similarly, an attorney plaintiff who routinely works as co-counsel with the other

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146. I generated this list through my own knowledge and research of this area. As with the previous section, my goal was to explore the problem, not present a definitive count. As a result, the actual scope of the problem may be greater than these figures reflect.

147. As in the previous Section, these plaintiffs played varied roles in the litigation. In some instances, they served as the lead plaintiffs and therefore had a high degree of control over the litigation. In other cases, they played smaller roles in the litigation.

148. In gathering the data on repeat plaintiffs described above, I often came across plaintiffs whose last names I recognized. Using publicly available information, I was able to confirm whether these plaintiffs were related to plaintiffs' attorneys.

149. *See, e.g.*, Stull v. Poole, 63 F.R.D. 702, 704 (S.D.N.Y. 1974).

150. It is difficult to determine the precise details of the representations from the public record. In some cases, the attorney relative serves as an attorney of record in the suit. In other cases, however, the attorney relative is not listed as an attorney of record. In these cases, the exact arrangements are unclear. If the attorney simply refers his relative to another lawyer with no expectation of payment or future referrals, there may be no reason for concern. On the other hand, if the attorney works on the suit but is not listed as counsel of record or if the attorney is compensated through direct payments or the hope of future business, there may be greater reason for concern.

attorneys in the litigation may be unwilling to jeopardize his business relationships by taking a strong position in litigation. In short, these attorney plaintiffs face possible conflicts of interest that may make it difficult for them to properly represent absent class members.[151]

2. Illustrative Examples

Several examples illustrate this practice. The first involves a law firm based in New York City called Paskowitz & Associates. Laurence Paskowitz is the named partner at the firm, and he often serves as an attorney in shareholder lawsuits.[152] Over the last several years, however, Mr. Paskowitz has also served as a plaintiff in multiple shareholder lawsuits.[153] Mr. Paskowitz is represented in some of these suits by an attorney named Roy Jacobs.[154] Mr. Jacobs' office is on the same floor of the same office building as Paskowitz & Associates,[155] and Mr. Jacobs is listed as part of Mr. Paskowitz's firm in several court filings.[156] In other words, Mr. Paskowitz is both a plaintiffs' lawyer and a plaintiff, often represented by a close business associate.

For other attorneys, litigation is a family affair. Jules Brody is a partner at Stull, Stull & Brody, a plaintiffs' firm with offices in New York City and California.[157] Mr. Brody is married to Adele Brody,[158] who has filed

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151. This does not mean that any particular lawyer is an inadequate shareholder plaintiff. It simply means that these plaintiffs may merit additional scrutiny. As discussed below, such scrutiny rarely occurs.

152. *See, e.g.*, LINKEDIN, http://www.linkedin.com/pub/laurence-paskowitz/9/720/795 (last visited Oct. 1, 2012) (stating that he specializes in class actions, antitrust litigation, consumer fraud, and complex business litigation and arbitration).

153. *See, e.g.*, Class Action Complaint, Paskowitz v. Dayton Power & Light, No. 20:11-cv-03103-GAB (Ohio Ct. C.P. Apr. 27, 2011); Complaint for Breach of Fiduciary Duty, Paskowitz v. Zenith Nat'l Ins. Corp., No. BC432177 (Cal. Super. Ct. Feb. 19, 2010); Complaint, Paskowitz v. Pacific Capital Bancorp, No. 09-cv-6449 (C.D. Cal. Sept. 4, 2009); Motion for Temporary Restraining Order, Paskowitz v. Toro, No. 2110-N (Del. Ch. Apr. 27, 2006). In my conversations with Mr. Paskowitz, he stated that he was not the lead plaintiff in many of these cases. *See* Email to Jessica Erickson from Laurence Paskowitz (Feb. 10, 2011) (on file with author).

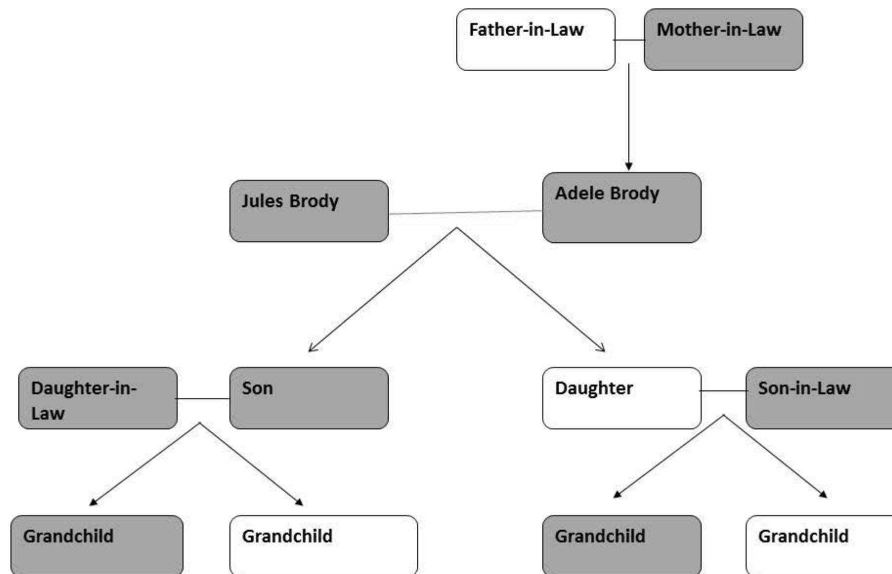
154. *See, e.g.*, Letter from Roy L. Jacobs to United States District Court, Paskowitz v. Pac. Capital Bank Corp., No. 2:09-cv-6449 (C.D. Cal. Jan. 5, 2010) (identifying himself as one of Mr. Paskowitz's attorneys in the shareholder suit); Class Action Complaint, Paskowitz v. Looney, No. 1:07-cv-01053 (D. Col. May 18, 2007) (Mr. Jacobs identified as "of counsel" for Mr. Paskowitz).

155. *See, e.g.*, Verified Shareholder Derivative Complaint, Delman v. Gifford, No. 11-cv-6749, at 59 (S.D.N.Y. Sept. 27, 2011) (stating, on the signature page, that both Mr. Paskowitz and Mr. Jacobs work on the forty-sixth floor of 60 East 42nd Street in New York City).

156. *See, e.g.*, Verified Class Action Complaint, Case No. 6090, DeHorn v. Soran, (Del. Ch. Dec. 21, 2010), at 13; Berlin v. Wells Fargo Bank Nat'l Assoc., Case No. 09-6928 (C.D. Cal. Sept. 23, 2009), at 31. In my discussions with Mr. Paskowitz, he told me that they each own their own law firms, but that Mr. Paskowitz hires Mr. Jacobs to serve as "of counsel" to Mr. Paskowitz's firm for particular cases. *See* Email to Jessica Erickson from Laurence Paskowitz (Feb. 10, 2011) (on file with author).

157. *See* Brief Biography of Stull, Stull & Brody, at 17, http://www.ssbny.com/wp-

multiple shareholder lawsuits over the past ten years.[159] Indeed, Mrs. Brody was identified as one of the "Most Frequently Named Plaintiffs" in a 2004 study of shareholder lawsuits filed in Delaware.[160] This fact alone may raise concerns, but my research suggests that multiple other members of Mr. Brody's family have filed shareholder lawsuits as well. I have included below Mr. Brody's family tree, which the family made public on the Internet.[161] The shaded boxes represent the individuals in his family who have filed shareholder suits or other class action litigation.



As this figure illustrates, Mr. Brody's wife, son, son-in-law, and daughter-in-law appear to have served as plaintiffs in shareholder lawsuits or related lawsuits.[162] In addition, Mr. Brody's wife Adele has apparently sued on

content/uploads/2012/03/SSBBio2-22-12.pdf.

158. *See* Marriage Announcement, *Jules Brody to Marry Adele Nussbacher*, N.Y. TIMES Oct. 17, 1965, *available at* http://select.nytimes.com/gst/abstract.html?res=F60710FC3454177A93C5A8178BD95F418685F9.

159. *See, e.g.*, *In re* Hearst-Argyle Television, Inc., S'holders Litig., No. 3205-CC (Del. Ch. Sept. 4, 2007); Brody v. Catell, No. 0008835/2006 (N.Y. Sup. Ct. Apr. 19, 2006); Brody v. Bellsouth Corp., No. 1:02-cv-02283 (N.D. Ga. Aug. 16, 2002).

160. Thompson & Thomas, *supra* note 94, at 188.

161. This genealogy information was available online. *See* Selected Families & Individuals, http://www.rabbiyehudahyudelrosenberg.com/. When I contacted the law firm to confirm this information, this portion of the website was taken down. A copy of the page that was taken down is on file with the author.

162. Ms. Weisman appears to have served as a plaintiff in one or more antitrust class actions. *See* Weisman v. Hearst Corp., No. 1:00-cv-05316 (S.D.N.Y. July 18, 2000); Weisman v. Nine West Group, Inc., No. 7:99-cv-00394 (S.D.N.Y. Jan. 20, 1999).

behalf of her mother's estate in at least one lawsuit.[163] She has also served as the custodian for her two minor grandchildren in multiple lawsuits.[164]

The lawsuits involving the two grandchildren are interesting. I was able to locate the complaints for two of these suits.[165] Both suits appear to have been filed when the children were less than five years old.[166] The only reference to their minor status that I could locate came in the certifications attached at the end of the complaints where Adele Brody (their grandmother) is identified as their custodian.[167] Also notable is the fact that, according to the certifications, the children owned only 100 shares of stock in the defendant corporations.[168] The certifications also disclosed that the children were repeat litigants, having served or sought to serve as lead plaintiffs in a total of six other lawsuits in the prior three years.[169] In some of these cases, one of the children appears to be represented by her family's law firm.[170]

Are these plaintiffs proper representatives of the class? The short answer is that no one knows. As explained in greater detail below,[171] defense attorneys and judges typically conduct remarkably little research into the background of shareholder plaintiffs. As a result, they typically do not notice that the plaintiff is a plaintiffs' attorney or related to a plaintiffs' attorney. In other words, it is difficult to know whether these plaintiffs are proper class representatives because no one is asking the right questions.

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163. Residuary Estate v. El Paso Corp., No. 4:02-cv-02838 (S.D. Tex. July 25, 2002).

164. *See, e.g.*, Class Action Complaint for Violation of the Federal Securities Laws, Rubin v. Am. Express, No. 1:02-cv-06440 (S.D.N.Y. Aug. 13, 2002) [hereinafter *American Express Complaint*]; Brody v. Bristol-Myers Squibb, No. 1:02-cv-2385 (S.D.N.Y. Mar. 27, 2002); Class Action Complaint for Violation of the Federal Securities Laws, Yaish v. Oracle Corp., No. 3:01-cv-01237 (N.D. Cal. Mar. 12, 2001).

165. *See* Class Action Complaint for Violation of the Federal Securities Laws, Rubin v. Am. Express Co., No. 1:02-cv-6440 (S.D.N.Y. Aug. 13, 2002); Class Action Complaint for Violations of Federal Securities Laws, Brody v. Bristol-Myers Squibb Co., No. 02-cv-2385 (S.D.N.Y. Mar. 27, 2002) [hereinafter *Bristol Complaint*].

166. According to the family's website one of the grandchildren was born in 1999 and another was born in 1998. *See* Selected Families & Individuals, *supra* note 161. The two cases in question were filed in 2002.

167. *See Bristol Complaint*, Plaintiff Certification (attached at back); *American Express Complaint*, Plaintiff Certification (attached at back). It is unclear why their grandmother, as opposed to their parents, is listed as their custodian.

168. *Id.*

169. *Id.*

170. *See, e.g.*, Smilow v. J.P. Morgan Chase, No. 1:02-cv-01910-SHS (S.D.N.Y. Mar. 8, 2002) (indicating on the docket that the plaintiff was represented by Aaron, her father; and Jules Brody, her grandfather); DeltaThree.com IPO v. DeltaThree.Com, Inc., No. 1:01-cv-05425 (S.D.N.Y. June 15, 2001) (indicating, on the docket, that the plaintiff was represented by Aaron, her father; Tzivia, her aunt; and Jules Brody, her grandfather).

171. *See* discussion *infra* Subsection II.D.3.

Erickson: The New Professional Plaintiffs in Shareholder Litigation

C. *Entities as Plaintiffs*

Institutional plaintiffs can fly under the judicial radar even more easily than individuals can. It is remarkably easy to set up a corporation or other business entity.[172] Plaintiffs who want to avoid scrutiny as repeat plaintiffs can set up multiple companies and divide their investments among them. This Section explores the possibility that attorneys may be using such entities as plaintiffs. This Section does not include empirical data because one cannot reach definitive conclusions about specific institutions based on publicly available information. Instead, this Section relies largely on illustrative examples.

1. Illustrative Examples

A recent case from the Delaware Court of Chancery, *In re SS & C Technologies, Inc. Shareholders Litigation*, highlights the possibility that individuals may have created entities at least in part to serve as plaintiffs in shareholder lawsuits. The case was an acquisition class action arising out of the sale of SS & C Technologies, Inc., brought by an institutional plaintiff called Paulena Partners.[173] During the litigation, counsel for the plaintiffs informed the defendants that the complaint had incorrectly identified Paulena Partners as the plaintiff, when in fact the actual SS&C stockholder was another entity called Bamboo Partners.[174] Both Paulena Partners and Bamboo Partners were managed by a man named Dean Drulias.[175]

This disclosure prompted the defendants to depose Mr. Drulias. During the deposition, they learned that Mr. Drulias had had an interest in numerous partnerships, as the Figure below illustrates.[176]

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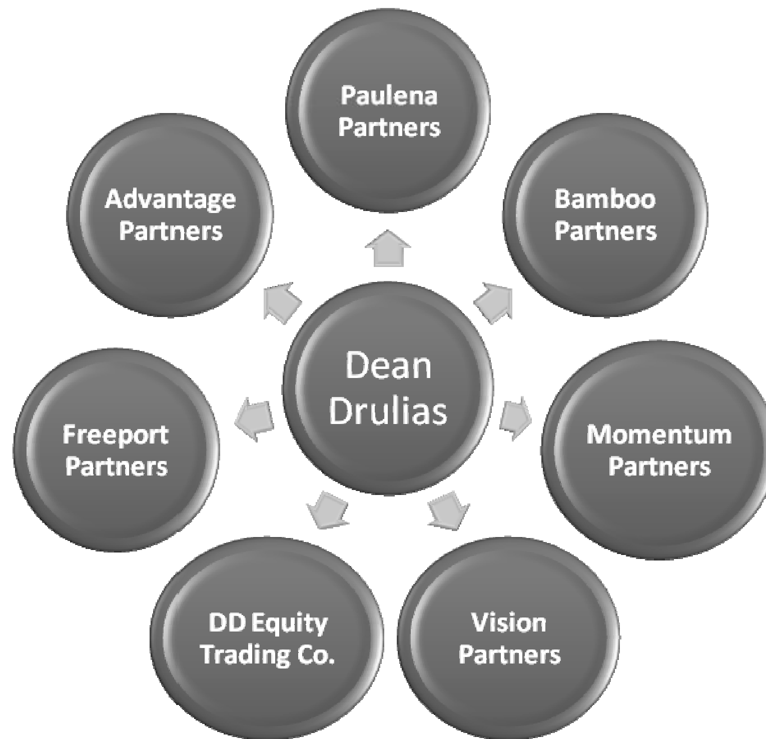
172. In most states, an individual only needs to file simple paperwork with the state and pay a nominal fee. As a recent Reuters investigation found, many states even allow the real owners of corporations to hide behind nominal officers and directors who have little or no role in the company and who are often executives of the mass incorporator. *See* Kelly Carr & Brian Grow, *Special Report: A Little House of Secrets on the Great Plains*, REUTERS, June 28, 2011, *available at* http://www.reuters.com/article/2011/06/28/us-usa-shell-companies-idUSTRE75R20Z20110628. Reuters uncovered, for example, a single house in Cheyenne, Wyoming, where more than 2000 companies are registered, serving as "a little Cayman Island on the Great Plains." *Id*. The Reuters investigation highlights how easy it is for individuals to hide behind corporate entities.

173. *In re* SS & C Techs., Inc. S'holders Litig., 948 A.2d 1140, 1142 (Del. Ch. 2008).

174. *Id.* at 1144.

175. *Id.*

176. *Id.* Some of the partnerships in this Figure were actually the same entity because, as Mr. Drulias testified, he changed the name of these partnerships when he took over management of them. *Id.* n.13.



Each of these partnerships owned a few shares of stock in between sixty and eighty public companies.[177] According to the court, these interests meant that "at any given time [Mr. Drulias had] a minuscule, indirect interest in several hundred publicly traded companies."[178] In total, these partnerships filed at least thirty shareholder class actions, although Mr. Drulias could not remember the exact number in his deposition.[179] He was represented in many of these lawsuits by the Brualdi Law Firm, a repeat player in the world of shareholder litigation.[180]

The court was extremely critical of these partnerships. It noted that Mr. Drulias had made a number of false statements in court filings, and these misstatements "are easily susceptible to the inference" that they were intended to conceal a "web of partnerships."[181] The court also noted that the purpose of these partnerships may have been to "spawn[]" litigation.[182] The court held that these misstatements demonstrated a "pattern of, at best,

177.*Id.* at 1144.

178. *Id.* Bamboo Partnerships owned three shares of stock in SS & C. *Id.* Mr. Drulias testified that he owned approximately 2% of these entities, often indirectly through other entities. He was not asked who owned the remaining 98%, and there is no public information available on this point. *See id.*

179. *Id.* at 1145.

180. *Id.*

181. *Id.*

182. *Id.*

carelessness, and at worst, a deliberate effort to mislead the court."[183] The court then imposed sanctions on the plaintiff.[184]

2. Extent of These Practices

The SS&C example raises disturbing questions, but the critical issue is whether the problems are more widespread. Limited to publicly available information, it is impossible to know. Yet there is reason to wonder about at least some plaintiffs in these suits.

First, we know remarkably little about many of the institutions that serve as plaintiffs in shareholder litigation. A significant percentage of shareholder suits are filed on behalf of institutions.[185] Many of these institutions are public pension or labor funds, but others are not. In my own data set, there are a significant number of cases filed by institutions with names suggesting that they may be private investment partnerships or similar financial institutions. In researching these entities, I discovered that little information is available about at least some of them. Most disclose nothing about themselves in the court records.[186] Many have no Internet presence whatsoever. In some instances, the chief information available online about the entities is the many lawsuits filed in their names.[187] In an era when Google can give us information about almost anything, some of these entities appear to be invisible—except, that is, in the courtroom.

This is not to suggest that these entities are illegitimate. The law allows private investment vehicles to remain largely private. Yet this invisibility means that we know remarkably little about many of the institutions that file shareholder suits, and in light of the *SS & C* decision, this lack of knowledge may be problematic.

Moreover, no one appears to be investigating these entities. In researching this Article, I spoke with numerous defense attorneys about their experiences in shareholder litigation. They told me that they conduct very little research about the named plaintiffs.[188] In fact, unless they have a

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183. *Id.* at 1151.

184. The court held that the plaintiff acted in bad faith during the litigation. It based this decision in large part on the plaintiff's motion to withdraw from the litigation without giving notice to the class in order to keep the alleged issues with these partnerships private. *Id.* at 1151–52.

185. *See, e.g.*, Erickson, *supra* note 21, at 1766–67 (finding that one-third of shareholder derivative suits filed in federal court between mid-2005 and mid-2006 were filed by institutions).

186. Plaintiffs in shareholder lawsuits typically disclose only their names, the fact that they owned stock in the target corporation during the time in question, and (if necessary for diversity jurisdiction) their states of citizenship. Other details—such as the general nature of their businesses or the names of their owners—are not disclosed until discovery. If the case does not get to discovery (and most do not), this information may never be disclosed. See *id.* at 1765.

187. This discussion does not identify specific entities because it is impossible to tell from the public record whether specific entities are legitimate. The purpose of this discussion is instead to highlight broader questions about the use of institutions as plaintiffs.

188. This point is illustrated by the SS & C litigation itself. No one would have ever known

specific reason to suspect misconduct or the case is quite significant, they typically conduct "zero" investigation into these plaintiffs.[189]

Why do defense attorneys fail to ask even the most basic questions about these plaintiffs? Defense attorneys told me that this decision stems from two considerations. First, and most importantly, professional plaintiffs often appear in acquisition class actions, and these suits move extremely quickly. There are often only a few months between the filing of the litigation and the scheduled closing of the merger. During this brief window, defense attorneys devote all of their energies to ensuring that the merger closes on schedule. As a result, they often focus on litigation strategies that will lead to a quick settlement or a blanket dismissal. Challenging the adequacy of the plaintiff is unlikely to accomplish either goal, at least in the eyes of defense attorneys.[190]

Second, defense attorneys may be naïve about the identity of shareholder plaintiffs. They might suspect that plaintiffs may own only a few shares of stock in the target corporation or may not know much about the underlying litigation, but the defense attorneys do not think that there are more serious problems. Their beliefs may even be self-perpetuating. Defense attorneys do not research plaintiffs because they do not think they will find anything useful, and they do not think they will find anything useful because they have never researched the plaintiffs. In short, we do not know what types of entities serve as plaintiffs in shareholder litigation because no one is asking the question.

D. *Dead Plaintiffs and Other Problems from the Filing Graveyard*

The problems outlined above are quite reminiscent of the problems that preceded the PSLRA. My research suggests, however, that new problems may have emerged in the wake of the PSLRA. This Section highlights three new types of alleged problems relating to the plaintiffs in shareholder litigation: (1) plaintiffs who may have died during the litigation, (2) plaintiffs who may not have owned the required stock during the litigation, and (3) plaintiffs who may not have known that they were plaintiffs. As with the prior Section, limited to allegations in the public record, it is not possible to present empirical data showing how often these problems have occurred. Thus, the discussion below relies on illustrative allegations to

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that Dean Drulias was associated with entities involved in approximately thirty lawsuits if he had not accidentally offered up the wrong entity as the plaintiff.

189. These attorneys often conduct more research in higher-profile or higher-dollar value cases. As discussed further in Part III, these cases are different than the more typical cases that are the focus of this Article.

190. These attorneys may believe that plaintiffs' attorneys will merely substitute a new plaintiff if the original plaintiff comes under fire. This belief may not always be correct, because the plaintiffs' attorney may not be able to find another shareholder willing to serve as a plaintiff in the suit. In many suits, however, there is more than one plaintiff, and therefore disqualifying one plaintiff would not eliminate the entire suit.

raise broader questions about the practices in these suits.

1. Dead Plaintiffs

In at least two cases, litigation may have continued for several months after the death of the shareholder plaintiff. The first case is a shareholder derivative suit filed by a shareholder named Maxine Babus on November 3, 2006.[191] This lawsuit, which was filed on behalf of Loral Space & Communications Inc. in New York state court, alleged that the Loral board breached its fiduciary duties in connection with the sale of $300 million of preferred stock.[192] On March 21, 2007, months after the suit was filed, the parties entered into a Memorandum of Understanding in which the purchaser of the preferred stock agreed to pay Loral to settle the litigation.[193]

On April 27, 2007, according to the company's public filings, the plaintiffs in a parallel Delaware suit filed a motion to intervene in the New York suit.[194] In this motion, the interveners told the court that the New York shareholder plaintiff, Maxine Babus, had died on November 12, 2006, just days after the suit was filed.[195] According to these court filings, the attorneys were ready to settle the case even though they did not have a named plaintiff.

My research uncovered another case in which the plaintiff's death may not have been disclosed to the court for several months. In *Orton v. Brown*, the plaintiff, J. Robert Orton Jr., filed a shareholder derivative suit on behalf of MBIA Inc. in the Southern District of New York.[196] The suit was filed on April 24, 2006.[197] More than a year later, on May 1, 2007, the defendants filed a Suggestion of Death informing the court that the plaintiff had died.[198] No additional information was provided, and the suit was voluntarily dismissed several months later.[199] My own research suggests that Mr. Orton may have died in May 2006, approximately two weeks after the suit was filed.[200] If this research is correct, Mr. Orton's

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191. *See* Babus v. Targoff, No. 603842/2006 (N.Y. Sup. Ct. Nov. 3, 2006).

192. *See* Shareholder Derivative Complaint, Babus v. Targoff, No. 603842/2006 (N.Y. Sup. Ct. Nov. 3, 2006).

193. *See* Loral Space & Commc'ns Inc., Form 10-Q, at 27 (for the quarterly period that ended Sept. 30, 2007).

194. *Id.*

195. *Id.*

196. Orton v. Brown, No. 1:06-cv-03146 (S.D.N.Y. Apr. 24, 2006).

197. *Id.*

198. *See* Suggestion of Death Upon the Record, Orton v. Brown, No. 1:06-cv-03146 (S.D.N.Y. May 1, 2007).

199. *See* Stipulation and Order of Dismissal, Orton v. Brown, No. 1:06-cv-03146-LLS (S.D.N.Y. Sept. 18, 2007).

200. *See* Social Security Death Index for J. Robert Orton, ANCESTRY.COM, http://www.ancestry.com (last visited Nov. 19, 2012) (stating that he died on May 10, 2006). This

death was not brought to the court's attention for nearly twelve months,.[201]

A dead plaintiff is obviously unable to serve as an advocate for the plaintiff corporation or absent class members. One could say the same about other plaintiffs who do not meet the basic qualifications to file these suits.

2. Plaintiffs Who May Not Own Stock

Plaintiffs lack standing to file shareholder litigation if they do not own the required stock in the target corporation. In shareholder derivative suits, a shareholder is only permitted to file suit on behalf of the plaintiff corporation if the shareholder owned stock in the target corporation at the time of the alleged misconduct and continued to hold this stock throughout the litigation.[202] This requirement is based in large part on the principle that derivative plaintiffs represent the company, and therefore should have financial interests that are aligned with the company's interests.[203]

Some plaintiffs, however, may have filed derivative suits even though they could not comply with this basic requirement. In *Parfi Holding AB v. Mirror Image Internet, Inc.*,[204] for example, the court discovered that two of the plaintiffs no longer held stock in the plaintiff corporation.[205] Indeed, one of the plaintiffs had divested its stock in the plaintiff corporation nearly six years earlier, before the litigation was even filed.[206] The plaintiff's counsel may have ignored this fact or failed to inquire whether the plaintiff met the requirements to serve as a derivative plaintiff.

This problem may be more widespread. Shareholders in derivative suits must allege continuous stock ownership from the time of the alleged misconduct through the conclusion of the suit. Shareholders often satisfy this pleading requirement by alleging that they are and were, "at all relevant times," a shareholder of the plaintiff corporation.[207] In many suits, however, the allegations are slightly different. Instead of alleging that the

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obituary does not specify that this decedent was J. Robert Orton Jr., although other information suggests that he was. *See, e.g.*, Obituary, Robert Orton Jr., CINCINNATI ENQUIRER, May 23, 2006 (referencing the death of J. Robert Orton Jr. in La Jolla, California on May 10, 2006).

201. *See, e.g.*, Memo. of Law in Support of Motion to Dismiss, Orton v. Brown, No. 1:06-cv-03146 (S.D.N.Y. Oct. 2, 2006); Plaintiff's Initial Disclosures Pursuant to FED. R. CIV. P. 26(a), Orton v. Brown, No. 1:06-cv-03146 (S.D.N.Y. Mar. 21, 2007).

202. *See* DEL. CODE ANN. tit. 8, § 327 (2011).

203. *See* Parfi Holding AB v. Mirror Image Internet, Inc., 954 A.2d 911, 939 (Del. Ch. 2008).

204. *Id.*

205. *Id.* at 935–38.

206. *Id.* at 935.

207. *See, e.g.*, Shareholder Derivative Complaint, Salzman v. Bartz, No. 11-cv-03269, at ¶ 18 (N.D. Cal. July 1, 2011). Many courts have required the plaintiff to go even further; they have required the plaintiff to specifically identify when he or shepurchased stock in the plaintiff corporation and whether he or she continues to own this stock. *See, e.g.*, *In re* VeriSign, Inc., Derivative Litig., 531 F. Supp. 2d 1173, 1202 (N.D. Cal. 2007).

plaintiff owned stock "*at all* relevant times"[208] to the litigation or providing the details of their stock purchases and sales, plaintiffs often allege only that they owned stock "*at times* relevant" to the litigation.[209]This difference may simply reflect a drafting choice, but given *Parfi Holding*, there is certainly an argument that more should be done to confirm the plaintiff's stock holdings in derivative litigation.

3. Plaintiffs Who May Not Know They Are Plaintiffs

Among the most troubling allegations are those regarding plaintiffs who may not know they are plaintiffs. One recent lawsuit raises the possibility that a lawsuit may have been filed on a plaintiff's behalf without her knowledge or consent. In this 2010 lawsuit, two plaintiffs' attorneys in New York City filed a lawsuit against a referral attorney who they alleged "supplied" them with a plaintiff who had not consented to participate in the litigation.[210] Not knowing about the plaintiff's lack of consent, the attorneys filed suit on the plaintiff's behalf in federal court.[211] Following the filing of the case, a reporter allegedly located the plaintiff and phoned her for comment.[212] The complaint alleges that the plaintiff then "learned that [the referral attorney] had volunteered her to serve as a plaintiff without her knowledge."[213] The suit was subsequently dismissed. The attorneys note that the referral attorney's alleged "strategy would 'work' in the vast majority of derivative cases, as the named plaintiff is only rarely subjected to any sort of personal discovery."[214] Had the reporter not contacted the plaintiff, it is certainly possible that the suit would have continued without the knowledge or participation of a named plaintiff.

How often do such problems occur? When it comes to professional plaintiffs, empirical evidence is hard to come by. Anecdotal evidence sheds light on this corner of the legal system, but attorneys and judges are not asking the tough questions that could lead to broader insights. As a result, we do not know how often shareholders are being paid to participate in litigation. We do not know how often plaintiffs' lawyers are serving as plaintiffs themselves. We do not know if institutional plaintiffs are legitimate entities. We do not even know if plaintiffs are named in

208. Shareholder Derivative Complaint, *supra* note 207.

209. A search of the pleadings database in Westlaw reveals some of these complaints. For example, a search for "derivative & (plaintiff /15 (owner or holder) /15 (stock or shares) /15 "at times relevant")" brings up more than 300 examples of this type of language in derivative complaints. It is impossible to determine from the public record which of these plaintiffs, if any, fail to satisfy the standing requirements.

210. *See* First Amended Complaint, Jacobs v. Harris, No. 650637/2011, at ¶ 18 (N.Y. Sup. Ct. Apr. 22, 2011).

211. *Id.*

212. *Id.* ¶ 19.

213. *Id.*

214. *Id.* ¶ 18.

litigation without their knowledge. In all of these instances, no one ever bothers to check. And because no one ever bothers to check, there is a window of opportunity for unscrupulous lawyers who are willing to skirt the rules to procure a client.

III. Toward a New Professionalism in Shareholder Litigation

In corporate law, it seems, the more things change, the more they stay the same. Many of the exact practices that Congress targeted in the 1990s may be continuing in the state courts. As these practices are exposed, lawmakers must again confront the theoretical questions that accompany these practices. When Congress passed the PSLRA, many commentators asked whether professional plaintiffs hurt anyone[215]—a question that is still critical today. This Part explains why the new professional plaintiffs are bad for corporate law. The discussion begins by exploring the ethical implications of professional plaintiffs. It then shifts to a broader examination of the impact of professional plaintiffs on investors and entrepreneurial litigation more generally. Finally, this Part considers new legislative proposals to address the problem of professional plaintiffs.

A. *The Problems with the New Professional Plaintiffs*

1. Lax Ethics

The allegations outlined in Part II are undoubtedly troubling and perhaps even scandalous. Few would argue in favor of a legal system in which lawyers surreptitiously pay plaintiffs to lend their names to litigation or sue on behalf of their family members. Beyond the shock value, however, some of the allegations in Part II may implicate the ethical rules that govern the practice of law.[216] The use of professional plaintiffs may raise two specific ethical concerns.

First, ethics rules prohibit payments to shareholder plaintiffs beyond their pro rata share of the recovery and reimbursement of reasonable expenses. The Model Rules of Professional Conduct (Model Rules) provide that a lawyer may not share legal fees with a nonlawyer except in certain narrow circumstances.[217] A lawyer also cannot provide financial

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215. This was a common question, for example, in the wake of the Milberg Weiss indictments when the government alleged that the law firm had paid plaintiffs. *See, e.g.*, Lonny Hoffman & Alan F. Steinberg, *The Ongoing Milberg Weiss Controversy*, 30 Rev. Litig. 183, 186 (2011) ("The single greatest source of controversy surrounding the Milberg prosecution, however, has always been whether anyone was actually harmed by what the lawyers did.").

216. This discussion is meant to highlight possible ethical problems with the use of professional plaintiffs. It does not mean that any attorneys have violated their ethical obligations, much less that any particular attorneys have violated their ethical obligations. Such a determination would depend on the specific facts in each case, many of which are not available from the public record.

217. Model Rules of Prof'l Conduct R. 5.4. These rules do not prohibit payments that

assistance to a client in connection with pending or contemplated litigation.[218] In short, if attorneys are paying plaintiffs to participate in litigation, they may be violating their ethical obligations.[219]

Second, ethical issues arise if attorneys make false statements to the court. The Model Rules provide that an attorney may not make a false statement of fact or law to the court.[220] Depending on their precise representations to the court, attorneys may violate this rule when they represent professional plaintiffs.

These ethical concerns about the use of professional plaintiffs have a critical impact on the application of class action law. The legal system requires judges to determine whether the proposed class representative is an adequate representative of the class.[221] In a shareholder lawsuit, this determination depends in large part on whether the named plaintiffs have interests that conflict with the interests of other class members.[222] Such a conflict impedes the ability of plaintiffs to perform their "most important task"—selecting and supervising class counsel to ensure that they are acting in accordance with the interests of the class.[223]

The use of professional plaintiffs has direct implications under the laws governing class actions. If plaintiffs have been paid to participate in litigation, for example, their interests likely diverge from the interests of the class. These plaintiffs may be more concerned with protecting their side payments than with maximizing the recovery to the class, especially if the side payments exceed the plaintiffs' likely recovery in the litigation.[224] These concerns would take on even more significance if the plaintiff is dead, nonexistent, or does not know that he or she has been named in the suit.

Despite these concerns, the law lacks an effective mechanism to enforce existing rules. It is theoretically possible for lawyers to be disbarred for violating their ethical obligations, but in most cases this possibility is merely theoretical. Lawyers typically only face ethics proceedings if the alleged violation is referred to the state bar association. Named plaintiffs are unlikely to make such a referral, especially if they are being paid for

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compensate plaintiffs for their expenses in the litigation.

218. *Id.* R. 1.8(e).

219. These payments may also violate federal law. *See* 18 U.S.C. § 201 (2006) (making it a criminal offense to "corruptly demand[], seek[], receive[], accept[], or agree[] to receive or accept anything of value . . . in return for being influenced in testimony under oath or affirmation as a witness").

220. MODEL RULES OF PROF'L CONDUCT R. 3.3(a)(1).

221. FED. R. CIV. P. 23(a)(4). A similar requirement applies to shareholder derivative suits under Rule 23.1 of the Federal Rules of Civil Procedure.

222. *See, e.g.*, *In re* Am. Int'l Grp., Inc. Sec. Litig., 265 F.R.D. 157, 172 (S.D.N.Y. 2010).

223. Gill v. Monroe Cnty. Dep't of Soc. Servs., 92 F.R.D. 14, 16 (W.D.N.Y. 1981).

224. A similar concern arises if class counsel uses his or her family members or business associates as plaintiffs.

their cooperation or are related to class counsel. The defendant could refer a case to disciplinary authorities, but as discussed above, defendants typically conduct little or no investigation into the shareholder plaintiff. Moreover, the defendant may *prefer* an inadequate plaintiff because it may be able to bargain for a lower settlement if the plaintiff is vulnerable to challenge.

Absent the plaintiff or the defendant raising these ethical issues, the court is unlikely to discover them. Few courts conduct their own inquiries into the background of the named plaintiffs, at least beyond a few cursory questions directed at counsel. Issues may arise through mere happenstance during the course of the litigation, as in many of the allegations discussed in Part II, but most cases will escape judicial scrutiny.[225]

This analysis does not mean that defendants *never* contest the qualifications of the named plaintiff. In larger cases with significant money at stake, the defendant has a greater incentive to oppose class certification by investigating the named plaintiff's qualifications. As discussed in the next Section, however, the problems identified in this Article do not typically arise in these larger cases. Instead, these problems arise more often in the run-of-the-mill cases that settle at minimal cost to the defendants. In these cases, defendants have little incentive to challenge the adequacy of the plaintiff and the court has little incentive to delay the settlement by conducting its own investigation.[226]

In sum, ethical and other rules may prohibit many of the practices associated with professional plaintiffs. The problem is that there is not an effective means to enforce these rules. As we shall see, without a means to enforce these rules, there is no one at the settlement table to protect the interests of absent class members.

2. Missing Monitors

Plaintiffs have always occupied an uneasy role in entrepreneurial litigation. On one hand, attorneys cannot file a shareholder derivative suit or acquisition class action without a named plaintiff.[227] On the other hand,

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225. The same problems come into play during class certification. In the vast majority of cases, the court does not certify the class until after the parties have reached a settlement. In the settlement documents, the parties typically agree that the named plaintiff is an adequate representative and that the case otherwise satisfied the requirements of Rule 23. The prevalence of these settlement-only classes means that most named plaintiffs are never subjected to the scrutiny of the class action process.

226. Macey & Miller, *supra* note 19, at 64 ("The defendant is unlikely to challenge the named plaintiff's typicality or adequacy, even when such a challenge might be successful, if the defendant believes that counsel representing this particular individual is someone who is likely to cut a favorable deal in settlement.").

227. *See, e.g.*, Theodore Eisenberg & Geoffrey P. Miller, *Incentive Awards to Class Action Plaintiffs: An Empirical Study*, 53 UCLA L. REV. 1303, 1305 (2006) ("The named plaintiff remains an essential prerequisite in all class cases.").

few people think these plaintiffs matter very much, as reflected in the well-accepted belief that shareholder plaintiffs are "figurehead[s],"[228] "pawns,"[229] and a "necessary nuisance."[230] In other words, shareholder plaintiffs hold the keys to the courthouse doors, but often do little once these doors have been opened. Given this nominal role, why should we care about professional plaintiffs? After all, if plaintiffs do not matter, maybe professional plaintiffs do not matter. As we shall see, however, plaintiffs *do* matter. Plaintiffs have the potential to play a crucial role in preventing collusive settlements. This Subsection explains how the rise of professional plaintiffs may undermine the ability of shareholders to monitor their attorneys and protect absent class members.

a. The Need for a Monitor at the Settlement Table

If judges expect so little from plaintiffs, why does the legal system still require them? This section argues that the rule requiring plaintiffs is not an anachronism from the legal past. Instead, it reflects modern economic theory regarding the incentives in shareholder litigation.

As discussed in Part I, the contingency fee system creates incentives for plaintiffs' attorneys to protect the interests of absent class members.[231] Attorneys work hard on behalf of the class because they ultimately get a percentage of any settlement or judgment. If these incentives work, figurehead plaintiffs—and by extension, professional plaintiffs—are not problematic, because plaintiffs' attorneys stand ready and willing to fight for larger settlements on the entire class's behalf.

As discussed in Part I, however, plaintiffs' attorneys have incentives that often cause them to underinvest in certain types of shareholder litigation and overinvest in others.[232] In securities class actions in the 1990s, attorneys overinvested in litigation because companies were agreeing to settle even arguably frivolous claims in order to avoid high discovery costs and the risk of catastrophic jury awards.[233] In shareholder suits filed under state law, attorneys may similarly overinvest in litigation, but for different reasons.

Commentators have long believed that attorneys are overinvesting in state shareholder suits. In the early 1990s, for example, one study concluded that "shareholder litigation is a weak, if not ineffective, instrument of corporate governance" and "the principal beneficiaries of

228. *In re* Cendant Corp. Sec. Litig., 404 F.3d 173, 191 (3d Cir. 2005).

229. Mars Steel Corp. v. Cont'l Ill. Nat'l Bank & Trust, 834 F.2d 677, 681 (7th Cir. 1987).

230. Declaration of Michael Hartlieb, Carrigan v. Solectron Corp., No. 1:07-cv-087219 (Cal. Super. Ct. Aug. 5, 2011).

231. *See* discussion *supra* Section I.B.

232. *See supra* note 66.

233. *See* discussion *supra* Section I.B.

cash payouts in shareholder suits are attorneys."[234] More recent studies show that these problems have persisted. In 2011 alone, shareholders challenged *ninety-six percent* of acquisitions involving U.S. public companies valued at over $500 million.[235] This figure strongly suggests that plaintiffs' attorneys are reflexively filing many shareholder suits.

The overinvestment in these suits arises in large part because of what economists call non-zero sum settlements.[236] Most settlements are zero-sum negotiations—every dollar in the plaintiff's pocket equals a dollar out of the defendant's pocket. In many shareholder lawsuits, however, the parties at the settlement table can reach settlements that benefit the plaintiffs' attorney without the defendant incurring any significant loss.[237] These non-zero sum settlements give plaintiffs' attorneys an incentive to file frivolous suits and defendants an incentive not to fight them.[238]

Non-zero sum settlements are common in shareholder litigation, often including nonmonetary benefits for the plaintiffs combined with significant fees for the attorneys. Many acquisition class actions routinely end with disclosure-based settlements in which the corporation agrees to make additional disclosures regarding the acquisition in exchange for settling the suit.[239] Similarly, shareholder derivative suits frequently end with the corporation agreeing to make arguably cosmetic changes to its corporate governance practices in exchange for dismissal of the suit.[240] The attorneys' fees in these types of cases are often significant, with one study finding that the plaintiffs' attorneys in acquisition class actions make nearly $500 per hour in suits involving nonmonetary settlements.[241]

Attorneys can often achieve a similar result in settlements that *do* include a monetary component. Many acquisition class actions are filed soon after the initial announcement of the deal. These complaints typically allege that the offer is too low. Following this initial offer, however, the prospective purchaser and the target's board often continue negotiations,

234. *See* Roberta Romano, *The Shareholder Suit: Litigation without Foundation?*, 7 J.L. ECON. & ORG. 55, 65, 84 (1991).

235. CORNERSTONE RESEARCH, RECENT DEVELOPMENTS IN SHAREHOLDER LITIGATION INVOLVING MERGERS AND ACQUISITIONS 2. This percentage is up from 53% just a few years earlier. *Id.* Nor are these suits limited to the very largest deals. Ninety-one percent of the deals valued at over $100 million were challenged in 2011. *Id.* at 3.

236. *See* Coffee, *supra* note 20, at 23.

237. Settlements can benefit the plaintiffs even if the defendant does not incur a significant loss. The concern here is that plaintiffs' attorneys and defendants are too quick to agree to settlements that do not benefit shareholders in large part because the settlements are so cheap for defendants.

238. Of course, not all suits filed by professional plaintiffs end with such settlements. My point relates more broadly to the incentives in these lawsuits.

239. *See* Weiss & White, *supra* note 16, at 1830 (describing empirical data about settlements in acquisition class actions).

240. *See* Erickson, *supra* note 21, at 1823–24.

241. *See* Weiss & White, *supra* note 16, at 1830.

which can lead to a higher final price. It is relatively easy for plaintiffs' attorneys to file suit immediately after the initial announcement of the offer, wait for the parties to negotiate a higher price or amended deal terms, and then take credit for the changes.[242] The Delaware Court of Chancery has criticized these settlements, stating that they can be little more than a "Kabuki dance."[243] Despite this criticism, however, these settlements remain a cheap form of currency in shareholder suits.[244]

These settlements are not surprising given the incentives in these suits. Non-zero sum settlements benefit defendants who can buy a release at a nominal cost. They also benefit plaintiffs' attorneys who get significant fees for relatively little effort. The only people who do not benefit from these settlements are shareholders—the real parties in interest in these suits. These settlements occur because no one at the settlement table is protecting shareholder interests. In other words, the legal system is missing a crucial monitor at the settlement table.

These settlements do not just hurt the shareholders of the particular company targeted in the lawsuit. They also undermine the role of private litigation in deterring corporate fraud. Corporate wrongdoers have little to fear from litigation if they know that they can escape significant monetary liability by agreeing to a nonmonetary settlement and high attorneys' fees. In short, the fact that we are missing a monitor at the settlement table not only leads to problematic settlements—it also undermines the deterrent role of shareholder litigation.

b. The Role of Shareholders Versus Other Monitors

If the current incentives in shareholder litigation lead to problematic settlements, the question becomes how to stop these settlements. As we will see, shareholders play a critical role in stopping problematic settlements, but this role is undermined by the continued presence of professional plaintiffs. To understand this role, however, we must first examine alternative proposals to address the incentive problems in

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242. The Delaware Court of Chancery has analyzed these settlement dynamics in a number of decisions. *See, e.g.*, *In re* Cox Commc'ns, Inc. S'holders Litig., 879 A.2d 604, 621 (Del. 2005).

243. *In re* Revlon, Inc. S'holders Litig., 990 A.2d 940, 945 (Del. 2010). A Kabuki dance is an event "that looks to have an uncertain outcome but actually comes to a conclusion the participants have scripted in advance." *See* State v. Bowser, 266 P.3d 1253, at *4 (2012).

244. Concerns about professional plaintiffs are bolstered by the research of Professor Michael Perino, who examined whether the cases named in the Milberg Weiss indictments ended differently than other comparable cases. *See* Michael A. Perino, *The Milberg Weiss Prosecution: No Harm. No Foul?*, 11 Briefly iii (May 2008), http://papers.ssrn.com/sol3/papers.cfm?abstract _id=1133995. He found a statistically significant difference in the attorneys' fees between the cases named in the indictment and other comparable cases. *Id.* at 39–58. This difference was modest, and Professor Perino found no difference in the overall size of the settlements, so his findings should not be overstated. But his research does suggest that investors suffer in cases where the named plaintiff has a financial interest adverse to the interests of the class.

shareholder litigation. Scholars have put forth at least two types of proposals to address these problems: (1) those that rely on the watchful eye of judges, and (2) those that rely on altered economic incentives for plaintiffs' attorneys.

Many commentators have pinned their hopes on more effective oversight by judges.[245] If judges routinely rejected cosmetic settlements and exercised more careful oversight of plaintiffs' attorneys, they could prevent collusion in shareholder suits. In a series of recent opinions, the Delaware Court of Chancery has endorsed this approach.[246] The court has made clear that it will closely examine settlement terms, rejecting those that benefit attorneys at the expense of shareholders.[247] In my discussions with members of the Delaware bar, several observed that these efforts have started to change the state of play in Delaware. For example, parties may be more reluctant to agree to nonmonetary settlements. They may also conduct more confirmatory discovery before presenting settlements to the court. In sum, Delaware courts are looking harder at these cases, and this scrutiny may be changing how lawyers litigate.

Will the changes in Delaware change shareholder litigation more generally? There is some reason to doubt that they will. Even if Delaware is eager to perform this gatekeeping function, other courts may not be. Over the last several years, plaintiffs' attorneys have increasingly started to file lawsuits outside Delaware.[248] Indeed, of the cases filed by repeat plaintiffs in my study, less than one-quarter were filed in Delaware.[249] The rest were filed in other state and federal courts across the country. Even if we trust Delaware judges to root out professional plaintiffs, we may not have the same confidence in judges in other jurisdictions. This observation is not meant as a criticism of these judges. Delaware judges are uniquely situated to take an active role in shareholder litigation because they see these cases day in and day out. Judges in other jurisdictions may simply not

245. *See, e.g.*, Chris Brummer, *Sharpening the Sword: Class Certification, Appellate Review, and The Role of the Fiduciary Judge in Class Action Lawsuits*, 104 COLUM. L. REV. 1042, 1043 (2004); Alexandra Lahav, *Fundamental Principles for Class Action Governance*, 37 IND. L. REV. 65, 136–38 (2003); Jonathan R. Macey & Geoffrey P. Miller, *Judicial Review of Class Action Settlements*, 1 J. LEGAL ANALYSIS 167, 193 (2009) (establishing a sliding scale for judicial oversight of class action settlements).

246. *See, e.g.*, *In re* Revlon, Inc. S'holders Litig., 990 A.2d at 956; *In re* Del Monte Foods Co. S'holders Litig., 2010 WL 5550677, at *9–11 (Del. Ch. Dec. 31, 2010).

247. For example, the court has noted that law firms can "build (and sometimes burn) reputational capital with the Court" and stated that it will replace plaintiffs' attorneys who fail to protect the interests of absent class members. *In re* Revlon, Inc. S'holders Litig., 990 A.2d at 955–56.

248. *See* Bernard Black et al., *Is Delaware Losing Its Cases?*, at 1, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1578404.

249. Specifically, 23.2% were filed in the Delaware Court of Chancery. The cases that were filed in federal court typically relied on diversity jurisdiction, although the complaints occasionally included federal question claims as well.

know to be on the lookout for professional plaintiffs, problematic settlements, or any of the other potential problems in these cases.

Delaware is trying to solve the problem of multi-forum litigation, an effort that may have implications for professional plaintiffs. In a 2010 decision, Delaware Court of Chancery Vice Chancellor J. Travis Laster invited corporations to adopt provisions specifying the Delaware courts as the "exclusive forum for intra-entity disputes."[250] More than eighty companies have taken up this invitation, adopting exclusive forum provisions in either their charters or bylaws.[251] The legal validity of these provisions is uncertain—they are currently under challenge in the courts,[252] and at least one judge has refused to apply them.[253]

The research on professional plaintiffs provides an additional reason to enforce these provisions. As discussed above, Delaware is uniquely situated to address the problem of professional plaintiffs. Moreover, judges would be better able to recognize professional plaintiffs if shareholder lawsuits were all filed in a single court. Yet, these provisions are not a cure-all. Even if they survive legal challenge, they may not bring all professional plaintiffs to the attention of the court. Moreover, even Delaware does not have a perfect record when it comes to identifying these plaintiffs.[254]

Many scholars have instead advocated reforms that change the incentives for plaintiffs' attorneys. As just one example, some scholars have argued that courts should use an auction system in which plaintiffs' attorneys bid for the right to control the litigation.[255] Any proceeds from the auction would be distributed to the class.[256] The winning bidder would then keep the entire recovery in the litigation.[257] This proposal garnered

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250. *In re* Revlon, Inc. S'holders Litig., 990 A.2d at 960.

251. *See* Claudia H. Allen, *Study of Delaware Forum Selection in Charters and Bylaws*, at ii, http://www.ngelaw.com/files/Publication/4050bc71-8f96-4442-9ed1-8ce7fc59716d/Presentation/PublicationAttachment/411832b1-153c-4d49-9dd4-b4e16548082f/Exclusive_Forum_Provisions_Study_4_7_11.pdf.

252. *See, e.g.*, Verified Complaint, iClub Inv. P'ship v. FedEx Corp., No. 7238, 2012 WL 467504, at ¶ 1 (Del. Ch. Feb. 13, 2012); Verified Complaint, Neighbors v. Air Prods. & Chems., Inc., No. 7240, 2012 WL 467520, at ¶ 1 (Del. Ch. Feb. 13, 2012); Verified Complaint, Boilermakers Local 154 Ret. Fund v. Curtiss-Wright Corp., No. 7219, 2012 WL 381849, at ¶ 1 (Del. Ch. Feb. 6, 2012).

253. *See* Galaviz v. Berg, 763 F. Supp. 2d 1170, 1174–75 (N.D. Cal. 2011).

254. The lawsuits filed by the entities associated with Dean Drulias discussed in Section II.C illustrate this point. These entities filed multiple lawsuits in the Delaware Court of Chancery before anyone noticed the potential problems. Moreover, the court would likely not have learned about the connection between these partnerships if Mr. Drulias had not mistakenly identified the wrong partnership in his original complaint. In short, even the Delaware Court of Chancery did not notice these potential problems until they became almost too obvious to miss.

255. *See, e.g.*, Macey & Miller, *supra* note 19, at 6.

256. *Id.* at 106–08.

257. *See id.*

significant attention initially, and a few courts experimented with it,[258] but ultimately lawmakers have been unable to structure an auction model that solves the problems inherent in shareholder litigation.[259] As Professor Coffee has noted, the limitations of such proposals "suggest that the legal system cannot pin all its hopes on the attorneys' fee award as the optimal incentive device."[260]

The intractability of these problems suggests that we should not be so quick to write off the plaintiffs in shareholder lawsuits. If judges cannot protect plaintiffs and attorneys cannot protect plaintiffs, maybe plaintiffs can protect plaintiffs.

The law is increasingly moving in this direction. The PSLRA, for example, is based on the idea that plaintiffs matter. By granting control of the litigation to the shareholder with the greatest financial stake, Congress made clear that shareholder plaintiffs have a crucial role to play in securities class actions.[261] The Delaware Court of Chancery has moved in a similar direction, giving preference to larger shareholders when determining the leadership structure in shareholder lawsuits.[262] In other words, as much as we say that plaintiffs do not matter, lawmakers continue to think they do. Given the problems with other monitors in securities class actions, lawmakers have good reason to think that plaintiffs matter.

This analysis does not mean that plaintiffs are a panacea. Large, institutional shareholders can be co-opted in many of the same ways as attorneys. Any hope that institutions would be unbiased monitors has been dashed by allegations that large pension funds may be trading their participation in litigation for campaign contributions.[263] These problems do not mean that plaintiffs are irrelevant—instead, they simply mean that

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258. *See, e.g.*, *In re* Cendant Corp. Litig., 264 F.3d 201, 220 (3d Cir. 2001) (holding that the auction procedure used by the district court violated the PSLRA).

259. *See, e.g.*, Jill E. Fisch, *Lawyers on the Auction Block: Evaluating the Selection of Class Counsel by Auction*, 102 COLUM. L. REV. 650, 727–28 (2002); Randall S. Thomas & Robert G. Hansen, *Auctioning Class Action and Derivative Lawsuits: A Critical Analysis*, 87 NW. L. REV. 423, 434–36 (1993). Stephen Choi and Robert Thompson similarly found that the PSLRA's mandate that courts conduct a Rule 11 inquiry at the end of every securities class action has had minimal impact. *See* Stephen J. Choi & Robert B. Thompson, *Securities Litigation and Its Lawyers: Changes During the First Decade After the PSLRA*, 106 COLUM. L. REV. 1489, 1507–11 (2006).

260. John C. Coffee, Jr., *Litigation Governance: Taking Accountability Seriously*, 110 COLUM. L. REV. 288, 308 (2010).

261. This aim is clear from the legislative history. *See, e.g.*, H.R. REP. NO. 104-369, at 34 (1995) (Conf. Rep.) ("The Conference Committee believes that increasing the role of institutional investors in class actions will ultimately benefit shareholders and assist courts by improving the quality of representation in securities class actions.").

262. *See* Hirt v. U.S. Timberlands Serv. Co. LLC, No. 19575, 2002 WL 1558342, at *2 (Del. Ch. June 18, 2002).

263. *See, e.g.*, Stephen J. Choi et al., *The Price of Pay to Play in Securities Class Actions*, U. Mich. Law & Econ., Empirical Legal Stud. Ctr. Paper No. 09-025, at 2 (2011), http://ssrn.com/abstract=1527047.

plaintiffs are one piece of a larger puzzle. Judges, attorneys, and shareholders are all imperfect monitors, and therefore none of them alone is sufficient. The best hope for curbing the agency costs inherent in shareholder litigation is legal rules that give *all* of these actors greater incentives to act in the best interests of absent class members.

How do professional plaintiffs fit into this analysis? If the ideal lead plaintiff is an institutional shareholder with strong financial incentives to monitor the litigation, some professional plaintiffs are about as far from this ideal as we can get. Many professional plaintiffs own a relatively small number of shares in the target corporation, which means that they have little financial interest to monitor the litigation. Moreover, some have other interests that cause them to turn a blind eye when their attorneys make decisions that are contrary to the interests of the class. These interests may include familial relationships, the promise of future business, or even illegal kickbacks. In short, money or other interests may separate professional plaintiffs from the rest of the class.

The research on professional plaintiffs also demonstrates that these problems may go deeper than we previously imagined. Conventional wisdom holds that institutional plaintiffs increasingly control shareholder litigation. This wisdom may quell concerns about the problems in shareholder litigation because these institutions, for all their faults, are better guardians of shareholder interests than the plaintiffs of the past. As a result, it may be easy for commentators to dismiss the problems in shareholder litigation if they believe that these problems will be solved as institutions extend their reach. The research on professional plaintiffs shows that this belief is misplaced. Institutions play a role in shareholder litigation, to be sure, but so do professional plaintiffs. Indeed, the sheer number of cases filed by repeat and other individual plaintiffs suggests that institutional plaintiffs are not on their way to dominating all of these cases.

The evidence instead suggests that shareholder litigation is moving toward a bifurcated litigation model. Under this new model, institutions control larger, more high-profile lawsuits, while professional plaintiffs and other individual shareholders control many smaller lawsuits with little money at stake. This model explains the persistence of professional plaintiffs. These plaintiffs do not file the cases that institutional plaintiffs want to control. In many instances, professional plaintiffs file the lawsuits that institutional plaintiffs want to avoid.[264] As a result, the rise of institutional plaintiffs may not mean much for the large number of shareholder lawsuits dominated by professional plaintiffs.[265] These smaller

264. Not all cases fall into this bifurcated model. In many cases in my data set, the repeat plaintiff filed a complaint along with other plaintiffs, including institutional plaintiffs. In many of these cases, the institutional plaintiff was either appointed lead plaintiff or appeared to control the suit.

265. The bifurcated litigation model also has implications for exit-based reforms proposed by

suits may not grace the front pages of the *Wall Street Journal*, but they still have important consequences for investors who see their returns diminished by what can amount to a litigation tax on mergers or other corporate decisions.

In the end, despite all of the rhetoric to the contrary, plaintiffs matter. Scholars have long preached the dangers of a pure entrepreneurial model, yet the legal system has done little to address the problem of professional plaintiffs. To eliminate professional plaintiffs from shareholder litigation, states must consider legal reforms that ensure a more meaningful role for shareholder plaintiffs.

B. *A Disclosure-Based Solution*

States should address the problem of professional plaintiffs by adopting a disclosure-based regime that brings attention to these possible conflicts of interest. Part II outlined a number of potential conflicts that can affect a plaintiff's ability to protect absent class members. Under the current system, however, the court only learns about these conflicts if the defendant investigates the shareholder plaintiff or if the court conducts its own inquiry into the plaintiff's qualifications. As discussed above, however, defendants often do not have the proper incentives to investigate plaintiffs, and few courts fill this gap with their own inquiry.[266]

States can alter these incentives by requiring disclosure of potential conflicts of interest. A few jurisdictions have experimented with such requirements. The Delaware Court of Chancery, for example, requires the plaintiffs in class actions and derivative suits to sign a certification that they have not "received, been promised or offered and will not accept any form of compensation" for participating in the litigation.[267] The PSLRA requires plaintiffs to file a similar certification. These rules address some, but not all, of the concerns outlined in Part II.

New certification rules should sweep more broadly. States should require shareholder plaintiffs in representative litigation to attach a signed certification to their complaint that would include at least four types of information.

First, the certification should include a statement that the plaintiff will not accept any payment for serving as a representative party other than their pro rata share of the recovery, except as ordered or approved by the court. This rule would not prohibit plaintiffs from receiving compensation

some scholars. *See, e.g.*, John C. Coffee, Jr., *Litigation Governance: Taking Accountability Seriously*, 110 COLUM. L. REV. 288, 298 (2010) (proposing reforms that would make it easier for shareholders to opt out of class actions). Given the low dollar values at stake in most of these suits, as well as the slim chance of success, large institutional investors do not have an incentive to opt out of the class and file their own independent actions. *Id.* at 327.

266. *See* discussion *supra* Subsection II.D.3.

267. Del. Ch. R. 23(a) and 23.1(b).

for reasonable costs and expenses. This rule is similar to those under both Delaware law and the PSLRA.

Second, the certification should identify all shareholder lawsuits filed by the named plaintiff over the past several years. This requirement reflects the fact that shareholders may not be effective monitors if they are participating in a significant number of lawsuits. It also recognizes that attorneys will be less likely to push the envelope if they have to justify their litigation decisions to a broader group of shareholders.

The PSLRA includes a similar requirement, but may not go far enough. The PSLRA requires plaintiffs to identify all other securities class actions "in which the plaintiff has sought to serve as a representative party."[268] Many shareholders appear to have interpreted this requirement to require disclosure only of the suits in which shareholders have sought to serve as lead plaintiff. Many shareholders do not disclose suits they have filed where they have not sought to serve as the lead plaintiff. In many shareholder lawsuits filed under state law, however, the court does not appoint a lead plaintiff. Instead these suits are often litigated under a joint leadership structure involving numerous shareholders and attorneys. Accordingly, certification requirements in these suits should include *all* shareholder suits filed by the named plaintiff, even if the plaintiff did not ultimately seek to serve as lead plaintiff in the litigation.

Moreover, the certification should cover suits filed in all jurisdictions. Congress was able to accomplish its objective because all securities class actions fell within its jurisdiction. In contrast, shareholder lawsuits brought under state law are typically filed in state or federal courts across the country. Imagine, for example, if Delaware adopted a rule requiring disclosure of prior suits filed in its courts. An enterprising plaintiff could easily circumvent this requirement by filing additional suits in California, Nevada, or any other jurisdiction. One could imagine plaintiffs playing a game of litigation hopscotch as they moved throughout the country filing lawsuits. To prevent this possibility, states should require disclosure of any corporate or securities lawsuit in which the shareholder has sought to serve as a representative plaintiff, not just lawsuits filed in that particular jurisdiction.

Third, the certification should identify all of the plaintiff's transactions in the stock at issue during the relevant time period. This requirement mirrors a similar requirement in the PSLRA. Extending this requirement to shareholder suits filed under state law has two intended goals. First, this certification would help ensure that named plaintiffs actually owned stock in the target corporation during the relevant time period, a concern discussed in Section II.D. Second, this certification would highlight the plaintiff's stock ownership to the court, allowing the court to exercise

268. 15 U.S.C. § 78u-4(a)(2)(A)(v).

special oversight in cases where the plaintiff has little financial interest in the litigation.

Finally, the certification should include disclosure of any business, financial, or familial relationships between the plaintiff and plaintiffs' counsel. This requirement is not currently part of any certification regimes, but there is a strong argument that it should be. As discussed in Part II, some lawyers appear to be using their family members or business partners as plaintiffs in shareholder suits. These relationships have the potential to undermine the plaintiffs' ability to effectively monitor their counsel. States should address this problem by requiring plaintiffs to disclose material relationships with their counsel. If the plaintiff is an institution, the plaintiff should also disclose whether plaintiffs' counsel has a financial interest in the institution.

This rule should cover all attorneys involved in the litigation, even if the attorney has not entered an appearance in the case. This rule reflects the fact that there may be more attorneys involved in the litigation than are listed on the docket. For example, attorneys who refer the plaintiff to lead counsel often do not enter a formal appearance. Other attorneys may perform work on the case behind the scenes, perhaps as part of a committee of attorneys working under the supervision of lead counsel. New rules should require disclosure of relationships with any of these attorneys, recognizing that the potential for conflict does not depend on whether the attorney has entered an appearance in the case.

This rule should also cover campaign contributions by attorneys. Many public pension funds are repeat filers of securities class actions and other shareholder lawsuits. There are allegations that these funds may be trading their participation in litigation in exchange for campaign contributions.[269] Certification requirements could target this problem by requiring institutional plaintiffs to disclose any campaign contributions from any of the attorneys involved in the litigation.

These disclosure rules would have two distinct benefits. First, they would give courts the information they need to carry out their responsibilities. Professional plaintiffs flourish because many courts do not know to look for them. Yet, even if courts seldom conduct their own investigations, few would turn a blind eye once potential problems are revealed.

Second, these rules would discourage plaintiffs' attorneys from relying on problematic plaintiffs. If plaintiffs are required to disclose material information about themselves, their attorneys would have less incentive to push the envelope. For example, attorneys may be unlikely to use their spouses or children as plaintiffs if they know that these relationships must be disclosed in a certification to the court. Similarly, attorneys may be less

269. *See supra* note 93.

likely to use plaintiffs who own only a few shares of stock in the target corporation if they have to disclose the plaintiff's stock ownership in the certification. In this way, disclosure rules could not only bring problems to the attention of courts—they could also change litigation practices on the ground.[270]

These certification requirements would not solve all of the problems in shareholder litigation. These requirements are intended to uncover potential conflicts of interest between the named plaintiff and the rest of the class.[271] Yet the ideal plaintiff is not just an unbiased shareholder. The ideal plaintiff is also knowledgeable about the case and willing to monitor class counsel. Many shareholders, even those who are not professional plaintiffs, have inadequate incentives to perform these responsibilities. Moreover, even the most motivated plaintiffs will still have limited control over the litigation, given the economic reality of contingency fee cases. Yet certification requirements would uncover the most egregious problems, setting the stage for additional reforms in this area down the road.

Ultimately, the debate over professional plaintiffs reflects a deeper debate over the gatekeepers in entrepreneurial litigation. The law expects shareholder plaintiffs to serve a gatekeeping function, yet does little to ensure that plaintiffs meet this expectation. The legal system must do more to encourage plaintiffs to cast a watchful eye over the litigation. Shareholder litigation is uniquely suited for these reforms because many shareholders have the financial stake necessary to take an active role in litigation. Professional plaintiffs undermine this effort, putting lawsuits back in the hands of plaintiffs' attorneys. In the end, professionalism is often a good thing—but not when it comes to choosing plaintiffs.

CONCLUSION

In shareholder derivative suits and acquisition class actions across the country, plaintiffs' attorneys appear to be using the exact same practices that provoked Congress's ire almost twenty years ago. Some attorneys are using the same plaintiffs in dozens of suits. Others are relying on their close relatives to serve as plaintiffs. As the first study of its kind, this Article shows that professional plaintiffs have been hiding right under our noses all along.

These findings have implications even outside the bounds of corporate law. Shareholder litigation is one type of entrepreneurial litigation, and the

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270. It is obviously possible that plaintiffs or their attorneys could lie in these certifications. An attorney who is willing to make ethically suspect payments to plaintiffs may also be willing to make false representations to the court. It is more likely, however, that the attorneys push the envelope because they know that no one is looking. A system that forces disclosure will reduce this temptation.

271. Or, in a shareholder derivative suit, conflicts between the named plaintiff and the corporation on whose behalf the suit was brought.

same incentives that drive shareholder litigation often drive other types of entrepreneurial litigation as well. Are the practices uncovered in shareholder litigation common in other types of entrepreneurial litigation? If so, what are the implications for the legal system more broadly? These questions remain for another day, but one thing is clear. Professional plaintiffs are back, and the time has come for a new solution to this old problem.