TO THE LOWEST BIDDER? THE PRIVATE SECURITIES LITIGATION REFORM ACT AND AUCTIONING THE ROLE OF LEAD COUNSEL

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INTRODUCTION

Although the class action lawsuit provides valuable access to the legal system, Congress has recognized the opportunities for abuse it creates.[1] Attorney abuse, including excessive charges for prosecuting these cases, is a common criticism of the class action process.[2] Because the class action is so lawyer-driven, exploitation is rampant particularly in securities litigation, whose primary method of prosecution is the class action lawsuit.[3] The auction process of determining lead counsel, however, can effectively curtail this exploitation precisely because it transfers control of the litigation back to the plaintiff class.

The auction process is the result of the Private Securities Litigation Reform Act (PSLRA) of 1995 enacted partly in re-

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1. Jill E. Fisch, *Complex Litigation at the Millennium: Aggregation, Auctions, and Other Developments in the Selection of Lead Counsel under the PSLRA*, 64 L. & CONTEMP. PROBS. 53, 53 (2001) [hereinafter Fisch, *Complex Litigation*]. Professor Fisch is a professor of law at Fordham Law School and has written numerous articles on the Private Securities Litigation Reform Act of 1995 and its effects on potential lead plaintiffs and their choices of counsel.

2. Randall S. Thomas & Robert G. Hansen, *Auctioning Class Action and Derivative Lawsuits: A Critical Analysis*, 87 NW. U. L. REV. 423, 423–24 (1993). *See also* Janet C. Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STAN. L. REV. 497, 576 (1991).

3. *See* Common Sense Legal Reforms Act, H.R. 10, 104th Cong. § 202 (1995).

sponse to the concern about lawyer-driven litigation.[4] The PSLRA limits lawyer control by allowing claimants to apply for the role of lead plaintiff in the action based on several qualifying factors.[5] Once a court appoints a lead plaintiff, that plaintiff selects counsel to represent the class, [6] subject to the court's approval.[7] Thus, rather than appoint as lead counsel the first lawyer to file suit, courts allow plaintiffs to select their own counsel, giving plaintiffs more control over the litigation from the beginning.

Unfortunately, the PSLRA fails to provide criteria courts can use to approve the lead plaintiff's choice of counsel. Lacking direction from Congress, innovative courts have successfully implemented an auction process to determine lead counsel[8] by which the counsel bidding the lowest legal fees wins, yet, as critics point out, a price-based auction system could deprive the plaintiff class of more qualified counsel simply because that counsel places a higher bid. As implemented, however, the auction process is more than just a price-driven bidding process; it incorporates several other factors that ensure quality legal representation, including trial experience and experience in securities litigation. Additionally, courts may still appoint the plaintiff's choice of lead counsel, if qualified, provided that counsel matches the winning bid. Thus, the auction process has remedied many of the problems of lawyer-driven securities litigation, thereby meeting the goals of the PSLRA.

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4. Jill E. Fisch, *Class Action Reform: Lessons from Securities Litigation*, 39 ARIZ. L. REV. 533, 533 (1997) [hereinafter Fisch, *Class Action Reform*].

5. Private Securities Litigation Reform Act of 1995, 15 U.S.C. § 78u-4(a)(3)(B)(iii)(I)(aa)–(cc) (2000). PSLRA requires the court to:

> [A]dopt a presumption that the most adequate plaintiff in any private action arising under this chapter is the person or group of persons that—(aa) has either filed the complaint or made a motion in response to a notice . . . ; (bb) in the determination of the court, has the largest financial interest in the relief sought by the class; and (cc) otherwise satisfies the requirements of Rule 23 of the Federal Rules of Civil Procedure.

6. *Id.* at § 78u-4(a)(3)(B)(v).

7. *Id.*

8. *See, e.g.*, *In re* Auction Houses Antitrust Litig., 197 F.R.D. 71 (S.D.N.Y. 2000); *In re* Lucent Techs., Inc., Sec. Litig., 194 F.R.D. 137 (D.N.J. 2000); Sherleigh Assocs. v. Windmere-Durable Holdings, Inc., 184 F.R.D. 688 (S.D. Fla. 1999); *In re* Cendent Corp. Litig., 182 F.R.D. 144 (D.N.J. 1998); Wenderhold v. Cylink Corp., 188 F.R.D. 577 (N.D. Cal. 1999); *In re* BankOne S'holders Class Actions, 96 F. Supp. 2d 780 (N.D. Ill. 2000).

Part I of this Comment discusses the origins of the PSLRA, its enactment, and the lead plaintiff provisions' consequences for lead counsel. Part II describes the courts' creation of the auction process. Part III analyzes and responds to the criticisms of using an auction process to appoint lead counsel. This part describes such criticisms as the auction's emphasis on price, the possibility of the plaintiff's unfamiliarity with court-appointed lead counsel, and the likelihood that the lowest bidder may not be the best-qualified attorney. Addressing these criticisms, this part will also describe benefits of the auction process, including its focus on non-monetary factors such as attorney experience in securities litigation. Part IV concludes that, despite its imperfections, the auction process remains the best solution to one of the most prominent problems facing class action securities litigation.

I. A BRIEF HISTORY OF LEAD PLAINTIFF APPOINTMENT AND PSLRA

The lead plaintiff provisions of the PSLRA directly address concerns regarding attorney control over litigation.[9] Prior to the PSLRA's enactment, courts usually selected lead plaintiffs and lead counsel in securities fraud class actions by appointing whichever plaintiffs and lawyers filed the first complaint. As lead counsel generally received the largest portion of attorneys' fees, this "first-in-time" approach resulted in a race to the courthouse.[10]

A. First in Time

The race to the courthouse created by the first-in-time rule resulted in three negative consequences for plaintiffs.[11] First, in order to file rapidly, lawyers deferred investigating the merits of complaints until after filing.[12] This often led to the filing of meritless claims that increased discovery costs for all defen-

9. Elliott J. Weiss, Comment, *The Impact to Date of the Lead Plaintiff Provisions of the Private Securities Litigation Reform Act*, 39 ARIZ. L. REV. 561, 563 (1997) (commenting that "[t]he lead plaintiff provisions of the [PSLRA] were directed at problems associated with attorneys' initiation and control of securities class actions").

10. Fisch, *Complex Litigation*, *supra* note 1, at 56.

11. *Id.* at 57.

12. *Id.*

dants, including those with little or no culpability.[13] In many of these cases, plaintiffs' attorneys profited whether the claims had merit or not.[14]

For example, in *In re Time Warner, Inc., Securities Litigation,* the Second Circuit Court of Appeals reviewed the dismissal of a complaint alleging that Time Warner withheld information about its plans to issue stock.[15] The plaintiffs alleged that Time Warner sought to sell its stock at a higher price by keeping that information secret for a time.[16] After the Second Circuit Court of Appeals reversed the dismissal, the parties announced they had agreed to settle for less than three percent of the original damages claim.[17] Professors Elliott J. Weiss and John S. Beckerman reported that a lawyer familiar with the negotiations said "that plaintiffs had agreed to settle only because it was clear the district judge was prepared to grant defendants' motion for summary judgment and plaintiffs did not think it likely they would prevail on a second appeal."[18] When asked why he thought the suit settled, the lawyer told Weiss and Beckerman: "Purely economics."[19] But this is only one example of a rather meritless claim resulting in a huge settlement for the plaintiff class.[20] Indeed, Professor Janet Cooper Alexander posits that the merits in securities fraud litigation do not affect settlement amounts at all.[21]

Second, the first-in-time rule created incentives for lawyers to seek out prospective plaintiffs rather than waiting for disgruntled investors to approach them.[22] Accordingly, lawyers relied on repeat or professional plaintiffs who owned a token number of shares in many companies.[23] These professional

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13. *See, e.g.,* Alexander, *supra* note 2, at 576.

14. *See, e.g., In re* Time Warner, Inc., Sec. Litig., 9 F.3d 259 (2d Cir. 1993).

15. *Id.* at 267.

16. *Id.*

17. *Id.* at 271.

18. Elliott J. Weiss & John S. Beckerman, *Let the Money Do the Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions,* 104 YALE L.J. 2053, 2087 (1995).

19. *Id.* (quoting a confidential source).

20. *See Time Warner,* 9 F.3d at 270.

21. Alexander, *supra* note 2, at 523.

22. Fisch, *Complex Litigation, supra* note 1, at 57.

23. S. REP. NO. 104-98, at 5–6 (1995) (describing three goals of PSLRA: "to encourage the voluntary disclosure of information by issuers"; "to empower investors so that they, not their lawyers, control securities litigation"; "to encourage

plaintiffs regularly lent their names to lawsuits.[24] Because they had little economic interest in the litigation, these plaintiffs lacked the incentive to wrest control of the litigation from their attorneys and hold out for larger class recovery. Studies show that investors recovered "only 7 to 14 cents for every dollar lost as a result of securities fraud."[25]

Third, the first-in-time rule caused courts to appoint lead counsel without thoroughly analyzing attorneys' qualifications.[26] As a result, lesser-qualified lawyers could control significant securities fraud litigation. This could lead to smaller recoveries for plaintiffs with legitimate claims deserving greater compensation.

Thus, the first-in-time rule disadvantaged both plaintiffs and defendants while creating advantages for lawyers. Congress needed to fix a fundamental flaw of securities fraud class action litigation. The PSLRA was Congress's attempt to do so.

B. The PSLRA Goals

Some argue that in enacting the PSLRA, Congress aimed to eliminate private securities litigation, while others contend that Congress intended to "curry favor with particular groups of constituents or with past or potential campaign contributors."[27] Still others argue that the PSLRA sought to reduce "the number of frivolous securities class actions that were filed simply to extort settlements from defendant corporations."[28] The legislative history of the PSLRA, however, indicates that Congress hoped to discourage plaintiffs' lawyers from acting in

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plaintiffs' lawyers to pursue valid claims for securities fraud and to encourage defendants to fight abusive claims").

24. *Id.* at 6.

25. *Id.*

26. Fisch, *Complex Litigation*, *supra* note 1, at 57 (citing H.R. REP. NO. 104-369, at 33 (1995)) (noting that because "courts traditionally appoint counsel in class action lawsuits on a 'first come, first serve' basis[,]" they "often afford insufficient consideration to the most thoroughly researched, but later filed, complaint").

27. *Weiss*, *supra* note 9, at 562.

28. Julia C. Kou, *Closing the Loophole in the Private Securities Litigation Reform Act of 1995*, 73 N.Y.U. L. REV. 253, 254 (1998). The *Time Warner* litigation discussed above illustrates this phenomenon.

their own pecuniary interests rather than in the best interests of their clients.[29]

1. A Distrust of Plaintiffs' Attorneys

Congress's distrust of plaintiffs' attorneys in securities fraud cases arose from a system in which the lawyers had large economic interests relative to their clients'. Because strike suits allowed attorneys to seek out plaintiffs when stock prices dropped dramatically, the motives of these attorneys were more suspect than in other class action suits. Additionally, plaintiffs' lawyers possessed both the primary decision-making authority in litigation and incentives to make decisions according to their own economic interests.[30] This system forced plaintiffs' attorneys to choose between maximizing their own income and maximizing the recovery for the plaintiff class.[31] A quick settlement meant less time spent in litigation and therefore more profit for the lawyer, but little recovery for the plaintiff class. Conversely, winning the case at trial meant more time and less profit for the lawyer, but full recovery for the plaintiff class.[32] Thus, the structure created an incentive for plaintiffs' lawyers to maximize their fees relative to the amount of work they invested in the case, not "to the size of the recovery to class members."[33]

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29. Richard H. Walker, David M. Levine & Adam C. Pritchard, *The New Securities Class Action: Federal Obstacles, State Detours*, 39 ARIZ. L. REV. 641, 642 (1997) (finding that the "central theme of the legislative history is that plaintiffs' lawyers, rather than faithfully representing investors, were acting for their own benefit"). *But Cf.* H.R. CONF. REP. NO. 104-369, at 31 (1995), stating that PSLRA was designed to combat:

> (1) the routine filing of lawsuits against issuers of securities and others whenever there is a significant change in an issuer's stock price, without regard to any underlying culpability . . . ; (2) the targeting of deep pocket defendants . . . who may be covered by insurance, without regard to their actual culpability; (3) the abuse of the discovery process to impose costs so burdensome that it is often economical for the victimized party to settle; and (4) the manipulation by class action lawyers of the clients whom they purportedly represent.

One suggestion that closely connects the ownership and control of class action litigation is the judicial auctioning of lawsuits. Thomas & Hansen, *supra* note 2, at 424.

30. Fisch, *Class Action Reform*, *supra* note 4, at 536.

31. Weiss & Beckerman, *supra* note 18, at 2057.

32. *See id.*

33. Fisch, *Class Action Reform*, *supra* note 4, at 536.

The media exclaimed that the whole system of filing, litigating, and settling class action lawsuits had become a "cynical and highly profitable game played by and for lawyers" with little regard for the shareholder plaintiffs.[34] For instance, in 1984, John W. Kluge, the founder of Metromedia Inc., bought the company from shareholders and proceeded to sell off its divisions and assets at a profit of about $3.3 billion. When Kluge announced his management buyout, almost a dozen different law firms quickly challenged the deal in a series of class action suits alleging Kluge's offer was far too low and violated a host of securities laws.[35] Less than four months later, the plaintiffs settled for an extra sixty-nine cents per share. Describing this slightly higher price as a "benefit" to the plaintiff class, the lawyers applied for and received just under $1 million in fees.[36] In other words, the offer that was originally far too low only increased sixty-nine cents per share, while the attorneys received almost one million dollars. This case is but one common example of plaintiffs' attorneys receiving an exorbitant profit for a meager class recovery. In fact, critics of class actions claim that when plaintiffs' attorneys settle class actions, which they usually do, they "*often* shortchange the plaintiff class."[37] The securities fraud class action system thus creates objectionable incentives for lawyers that many of them take advantage of. Given the plaintiff's lawyers' incentives, Congress likely enacted the PSLRA to transfer the control of securities litigation back to the plaintiffs.[38]

2. Back to the Plaintiff Class

To this end, Congress first established certain requirements for parties applying for lead plaintiff, as the PSLRA's language demonstrates. First, a prospective lead plaintiff must provide "[e]arly notice to class members . . . of the pendency of

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34. Steve Coll & David A. Vise, *Shareholder Lawsuits: Profitable New Path for Attorneys; As Takeovers and Buyouts Boom, Class-Action Litigation is Becoming a Frequent, Cynical Tactic, Critics Say*, WASH. POST, July 24, 1988, at H1.

35. *Id.*

36. *Id.*

37. Weiss & Beckerman, *supra* note 18, at 2055 (emphasis added).

38. Fisch, *Class Action Reform*, *supra* note 4, at 533. *Cf.* H.R. CONF. REP. NO. 104-369, at 31 (1995) (noting the PSLRA was designed to combat "the manipulation by class action lawyers of the clients whom they purportedly represent").

the action" and the opportunity for "any member of the purported class [to] move the court to serve as lead plaintiff."[39] The first plaintiff to file no longer receives the lead plaintiff designation, so that plaintiff's counsel does not necessarily qualify for lead counsel status. This language not only prevents the first lawyer to file the claim from automatically thwarting others seeking lead counsel status, but also forces lawyers to notify lead counsel hopefuls of the claim.

Because Congress assumed that the most appropriate lead plaintiff is the class member with the largest interest in the litigation, the PSLRA mandates two presumptions regarding the selection of lead plaintiff.[40] First, the court must presume that the most adequate plaintiff "has either filed the complaint or made a motion in response to a notice [by the party who originally filed the action] . . . ."[41] This presumption relies on the premise that notwithstanding the race to the courthouse, the first plaintiff to file sometimes is a diligent investor who first observes potential securities fraud. If a court appoints that investor as lead plaintiff, the PSLRA assumes that the chances of that investor remaining diligent throughout litigation increase. This result serves Congress's goal of transferring control back to the plaintiff class.

Second, the PSLRA instructs courts to presume that the plaintiff best fit to serve as lead plaintiff is the party who, "in the determination of the court, has the largest financial interest in the relief sought by the class . . . ."[42] This language strongly suggests Congress sought to restrict the use of professional plaintiffs.[43] If the lead plaintiff must have a great financial interest in the litigation, as the PSLRA now requires, attorneys cannot keep a few stockholders with token stock in a few corporations waiting in the wings until a securities fraud occurs in the hopes of a lead counsel appointment. Instead, attorneys must wait until those with large financial interests seek them out as attorneys. Therefore, the plaintiff with the "strongest financial interest will pursue the claims with the

39. 15 U.S.C. § 78u-4(a)(3)(A) (2000).

40. For an argument that this presumption encourages participation by institutional investors as lead plaintiffs, see H.R. CONF. REP. NO. 104-369, at 34 (1995).

41. 15 U.S.C. § 78u-4(a)(3)(B)(iii)(I)(aa).

42. *Id.* at § 78u-4(a)(3)(B)(iii)(I)(bb).

43. Fisch, *Class Action Reform*, *supra* note 4, at 536.

greatest vigor and will have both the interest and the clout to engage qualified counsel at the best rate for the class."[44]

Finally, a plaintiff seeking lead plaintiff status must satisfy "the requirements of Rule 23 of the Federal Rules of Civil Procedure."[45] Imposing these traditional requirements of class action litigation in the securities fraud litigation environment also prevents a race to the courthouse. Rule 23 of the Federal Rules of Civil Procedure requires that a member of a class may sue as a representative of that class if the "representative part[y] will fairly and adequately protect the interests of the class."[46]

Courts use the common law interpretations of this Rule in evaluating prospective lead plaintiffs.[47] Hence, this additional requirement also serves the PSLRA's two overarching purposes. First, it returns control of the litigation to the plaintiff class. This is done by requiring a plaintiff to show that she will fairly protect the interest of the class if she seeks the role of lead counsel, even if she is first to file. This process eliminates the abuses that accompanied the first-in-time rule.[48] Second, it provides trial court judges with criteria as to how to select lead plaintiff, including the traditional rules governing class actions.

II. ENTER THE AUCTION PROCESS

Although Congress ended the race to the courthouse by replacing the first-in-time rule with the PSLRA lead plaintiff requirements, it failed to provide the courts with a formula for appointing lead counsel in securities litigation. Absent explicit statutory guidance, courts have developed the auction process. Gradually, courts have modified the auction to include mean-

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44. *In re* Cendant Corp. Litig., 182 F.R.D. 144, 145-46 (D.N.J. 1998).

45. 15 U.S.C. § 78u-4(a)(3)(B)(iii)(I)(cc).

46. FED. R. CIV. P. 23.

47. *See* Kriendler v. Chem. Waste Mgmt., Inc. 877 F. Supp. 1140, 1159 (N.D.Ill. 1995) (stating three requirements to satisfy Rule 23: "(1) [t]he chosen class representative cannot have . . . conflicting claims with other members of the class . . .; (2) the named representative must have a 'sufficient interest in the outcome to ensure vigorous advocacy' . . . . (quoting Riordan v. Smith Barney, 113 F.R.D. 60, 64 (N.D. Ill. 1986)); and (3) counsel for the named plaintiff must be competent, qualified, experienced, and able to vigorously conduct the proposed litigation").

48. Indeed, "initial research suggests that the race to the courthouse has slowed since the enactment of PSLRA." *See* Walker, *supra* note 29, at 650.

ingful selection criteria other than mere price. By returning control of securities litigation to the plaintiff class, the auction process has thus far fulfilled the goal of the PSLRA.

A. How Congress Failed

Though it was intended to encourage deliberation in the selection of lead counsel, the PSLRA does not provide criteria to the court in reviewing the lead plaintiff's choice of counsel. Additionally, the PSLRA fails to explain what happens when the court rejects the plaintiff's selection.[49] The absence of statutorily created criteria has forded courts to develop a process of review for the choice for lead counsel. Yet courts have exhibited a reluctance to impose meaningful selection criteria.[50] No published cases in any federal district describe parameters regarding appointment of lead counsel. Indeed, courts often fail to carefully scrutinize the qualifications of class counsel.[51]

Furthermore, appellate courts may not be able to review the process of selecting the lead plaintiff and appointing lead counsel on appeals by non-selected attorneys because review must wait until the case ends.[52] In *Metro Services Inc. v. Wiggins,* the trial court had issued an order appointing lead counsel.[53] The Second Circuit Court of Appeals found that the order did not meet the finality requirement of the collateral order test, and thus disallowed the appeal. [54] Specifically, because the district court had reserved the right to reconsider its lead plaintiff determination, the appellate court found that the disputed question had not been conclusively determined.[55] Ac-

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49. Fisch, *Complex Litigation*, *supra* note 1, at 64.

50. Walker, *supra* note 29, at 658 (citing Joint Amended Motion of the Micro Warehouse Plaintiffs' Group to be Appointed Lead Plaintiffs at 1, Payne v. Micro Warehouse, Inc. Civil Action No. 3:96 CV 01920 (DJS) (D. Conn. Dec. 20, 1996)) (listing the actions). Walker concludes that these filings "are somewhat curious as the [PSLRA] allows any plaintiff to simply move to be named lead plaintiff after an initial complaint is filed, thereby making the filing of additional (and costly) complaints unnecessary." Walker, *supra* note 28, at 658–59 n116.

51. Fisch, *Class Action Reform*, *supra* note 4, at 549.

52. Metro Servs., Inc. v. Wiggins, 158 F.3d 162, 165 (2d. Cir. 1998).

53. *Id.*

54. *Id.*

55. *Id.* (quoting Richardson-Merrell, Inc. v. Koller, 472 U.S. 424, 431 (1985)); *see also In re* Cendant Corp. Litig., ("[r]ecognizing that the [PSLRA] affords [the] opportunity to lead plaintiffs to choose counsel subject to the approval of the Court, the Court maintains the same in the auction process").

cording to the Second Circuit Court of Appeals, since the appellate court cannot review the appointment of lead counsel until the case is over, the PSLRA strips appellate courts of their already limited ability to review a determination as to which attorney will best serve as lead counsel. Although this issue has not been decided conclusively, it appears that the statute not only fails to explicitly guide trial courts in choosing lead counsel, but it also prevents appellate courts from providing them with instruction. As a result, United States District Courts are left to formulate their own selection processes.

Further, by dictating that "[t]otal attorneys' fees and expenses awarded by the court to counsel for the plaintiff class shall not exceed a reasonable percentage of the amount of any damages and prejudgment interest actually paid to the class, "the PSLRA assumes an inherent cost-benefit analysis in securities litigation." [56] This provision falsely presupposes that courts can and do determine the reasonable value of the services attorneys provide.[57] Yet judges have rarely reviewed the relevant evidence in the actions in any detail and thus rarely independently evaluate either party's claims or defenses, or how much work the claims and defenses require.[58] Additionally, judges know even less about "how diligently or effectively the plaintiffs' attorneys have prosecuted the action."[59]

B. How the Courts Responded

The PSLRA's deficiencies regarding lead counsel selection criteria and assumptions regarding costs and benefits led courts to appoint lead counsel using price as a primary criterion. The resulting auction process rests on the assumption that, given the "opportunity, absent class members would select the most qualified representation at the lowest cost."[60] The courts correctly believe that since the lead plaintiff's choice of counsel is subject to their approval, the statute instructs them to rely on something more than the plaintiff's own judgment.[61] Rather, judicial selection of counsel should use the mechanisms

56. 15 U.S.C. § 77z-1(a)(6) (2000).
57. Raftery v. Mercury Fin. Co., No. 97-624, 1997 U.S. Dist. LEXIS 12439, at *6 (N.D. Ill. Aug. 15, 1997).
58. Weiss & Beckerman, *supra* note 18, at 2066.
59. *Id.*
60. *In re* Cendant Corp. Litig., 182 F.R.D. 144, 150 (D.N.J. 1998).
61. *Id.*

of a competitive market.[62] The *In re Continental Illinois Securities Litigation* court noted:

> [T]he object [in determining fee awards] is to simulate the market where a direct market determination is infeasible. It is infeasible in a class action because no member of the class has a sufficient stake to drive a hard—or any—bargain with the lawyer. So the judge has to step in and play surrogate client.[63]

Thus, courts believe that determining attorneys' fees depends on a simulation of a competitive market.

The idea behind the auction process—obtaining highly qualified counsel that will maximize recovery best serves the class—necessarily implies that attorneys' fees should be relatively low.[64] Therefore, the PSLRA directs courts to review the lead plaintiff's lead counsel selection and then determine whether that attorney would have been selected in an open, competitive market, based on counsel's stated fees. This rationale explains the "emerging trend in common fund class actions for courts to simulate the free market in the selection of class counsel."[65] Thus, courts have recognized that marketplace competition is the most effective way to establish reasonable attorneys' fees.[66]

First among those cases to use the auction process, *In re Oracle Securities Litigation* began when Oracle Systems Corporation announced disappointing earnings for the first quarter of 1990, and the stock price dropped drastically the next day.[67] In the ensuing securities class action, Judge Vaughn R. Walker of the U.S. District Court for the Northern District of California decided first that lead counsel would be awarded according to a bidding process. He discussed the lodestar method, by which judges fix attorneys' fees according to the time and effort they put into the litigation. Judge Walker rejected the lodestar approach calling it unworkable since it "abandons the adversary

62. *In re* Oracle Sec. Litig., 131 F.R.D. 688, 693 (N.D. Cal. 1990).
63. 962 F.2d 566, 572 (7th Cir. 1992).
64. Raftery v. Mercury Fin. Co., No. 97-624, 1997 U.S. Dist. LEXIS 12439 at *5 (N.D. Ill. Aug. 15, 1997).
65. *In re* Cendant Corp. Litig., 182 F.R.D. at 150.
66. *Id.*
67. *In re* Oracle Sec. Litig., 131 F.R.D. at 690.

process upon which our judicial system is based."[68] He reasoned that because lawyers are paid according to their time, and thus may be drawn to lengthy and complex litigation, the loadstar approach promotes "wasteful litigiousness.".[69] Judge Walker then attacked the benchmark method, by which judges rely on a set percentage of the total class recovery to fix attorneys' fees.[70] Because both lawyers and judges rarely agree upon that percentage, and because it can be adjusted upward or downward for virtually any reason, Judge Walker also rejected the benchmark method as too faulty to determine attorneys' fees.[71]

Judge Walker finally concluded that the bidding process would be the most appropriate way to determine attorneys' fees since it fosters the natural competition of the market.[72] Even in this first auction for lead counsel, Judge Walker required lawyers to submit both their qualifications to serve as lead counsel and the percentage of the recovery they would charge as fees.[73] Judge Walker also reserved the right to request additional information from the attorneys.[74]

Using variations on the model first employed in the *Oracle* case,[75] other judges have directed firms seeking appointment as lead counsel to submit bids to the court.[76] These bids require the attorneys to propose a fee structure for conducting the litigation.[77] Judges consider the bids, as well as a number of other factors, in selecting lead counsel.[78] These additional factors include the attorneys' respective "qualifications, experience, malpractice coverage, and willingness to post a completion bond."[79] In some cases, firms must "demonstrate that they evaluated the case and specify the range and likelihood of recovery."[80]

In a more sophisticated auction, the court in *In re Cendant Corporation Litigation* followed a similar process to determine

68. *Id.* at 689.
69. *Id.*
70. *Id.* at 695.
71. *Id.*
72. *Id.* at 690.
73. *Id.* at 697.
74. *Id.*
75. *See generally In re* Oracle Sec. Litig., 136 F.R.D. 639 (N.D. Cal. 1991).
76. Fisch, *Complex Litigation*, *supra* note 1, at 80.
77. *Id.*
78. *Id.*
79. *Id.* at 81.
80. *Id.*

the lowest qualified bidder to represent the class as counsel.[81] Here Cendant's predecessor and a second corporation formed Cendant late in 1997.[82] Cendant later announced substantial accounting irregularities that resulted in previously misstated earnings.[83] When Cendant later corrected the earnings, its stock price fell sharply.[84] Fifteen plaintiffs or groups of plaintiffs filed motions for appointment as lead plaintiff after the court merged the ensuing flurry of derivative suits.[85] Each of those plaintiffs also moved to have its counsel appointed lead counsel for the class.[86]

After appointing a lead plaintiff based on its application of the PSLRA, the *Cendant* court faced the task of appointing lead counsel. First, the court noted its discretion under the PSLRA to determine whether lead plaintiff's choice of lead counsel would best suit the needs of the class.[87] The court then explained that it would be "reasonable to assume that given the opportunity, absent class members would try to secure the most qualified representation at the lowest cost."[88]

> [T]he ultimate goal in class action litigation—that is, for the members of the plaintiff class—is to maximize the benefit to the class members if the litigation proves successful . . . and there can be no doubt that the class is best served by obtaining highly qualified class counsel who are prepared to undertake the representation on a basis that will maximize that recovery (something that necessarily implicates what counsel will charge for their services).[89]

As had the court in *Oracle*, this court acknowledged that its selection of lead counsel should reflect a strong consideration of price.

The court agreed with the reasoning in *Oracle* that the most effective way to establish reasonable attorneys' fees is to

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81. *In re* Cendant Corp. Litig., 182 F.R.D. 144, 146 (D.N.J. 1998).
82. *Id.*
83. *Id.*
84. *Id.*
85. *Id.*
86. *Id.*
87. *Id.* at 150.
88. *Id.*
89. *Id.* (quoting Raftery v. Mercury Fin. Co., No. 97-624, 1997 U.S. Dist. LEXIS 12439 at *4–5(N.D. Ill. Aug. 15, 1997)).

simulate market competition.[90] Accordingly, it conducted an auction to determine the lowest qualified bidder to represent the class as counsel. The Court required bidders to submit their personal qualifications, relevant history of involvement in securities or similar litigation, the results of any such litigation, and their ability to undertake the current litigation.[91] The court also insisted that bidders indicate the predicted attorneys' fee award. Finally, the court ordered the bidders to submit their bids in good faith and without any assistance or collusion.[92] It appears, then, that courts that have experimented with auctions are motivated to provide a more objective way of selecting lead counsel and a better way of determining an appropriate fee award.[93]

III. PROBLEMS WITH AND SOLUTIONS TO THE AUCTION PROCESS

Because of the novelty of the auction process and because few cases get to this point, judicial experience with it is lim-

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90. *Id.*

91. *Id.* at151.

92. *Id.* The court's list of applicable factors follows.

1. Each bidder shall submit his, her, or their professional qualifications to be lead counsel. Among anything else deemed relevant, this shall include a history of involvement in similar litigation, case titles, docket numbers, relevant dates, courts involved, the result, whether by trial or appeal, settlement or resolution and the time during litigation when such resolution or settlement occurred.

2. Bidders shall indicate their ability to undertake and maintain all costs of this litigation, and should express their readiness to post a performance bond and its amount, if required by the Court.

3. Bidders shall indicate how costs are to be deducted in the event of resolution favorable to the plaintiffs.

4. Applicants shall state their percentage fee bids according to one or both of the following 'litigation milepost' grids: [grid omitted].

5. Each bidder shall certify that its bid is made in good faith and has been formulated, determined, prepared and forwarded to the Court without any assistance, revelation or collusion, direct or indirect, with any other party or competing law firm before submission to the Court.

6. Payment of the fees and costs of any lawyers or firms assisting the lead counsel, if any, will be the responsibility of lead counsel.

7. The Court reserves the right to reject any and all bids it deems not to have been made in good faith or which are contrary to the interests of the consolidated plaintiffs. In its discretion, the Court may solicit additional bids from any source.

93. Fisch, *Complex Litigation*, *supra* note 1, at 80–81; *See, e.g., In re* Cendant Corp. Litig. 182 F.R.D. 144 (D.N.J. 1998); *In re* Oracle Sec. Litig., 131 F.R.D. 688 (N.D. Cal. 1990).

ited.[94] Yet despite this inability to truly evaluate the process, for some commentators, the initial experience already suggests practical problems that have yet to be addressed by the courts.[95] Courts must answer the fundamental question underlying these practical problems: Does an auction constitute an appropriate means to select lead counsel?[96] As the following discussion posits, the auction process is the most appropriate means to select lead counsel in accordance with the goals of the PSLRA.

A. Overcoming the Focus on Price

Some commentators strongly disagree that the auction appropriately appoints lead counsel, and usually cite either the preoccupation with price or the court's inability to calculate a fair price.[97] Most critics cite to the former argument and claim that the focus on price does not direct a court to the attorney who can best serve the plaintiff class.[98] Recently, when Judge Walker employed the auction to determine lead counsel in *In re Quintus Securities Litigation* and in *In re Copper Mountain Networks Securities Litigation,*[99] the attorneys not selected as lead counsel appealed, arguing that the judge "compared fees and he picked the lowest fee and that's wrong."[100]

Indeed, the selection of class counsel solely on the basis of price, without consideration of qualitative factors and the costs of poor performance, may shut out effective lawyers from the bidding process.[101] Because many experienced, qualified securities fraud lawyers often charge higher fees than some lesser-qualified attorneys, they will be ousted by the very system that

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94. Fisch, *Complex Litigation*, *supra* note 1, at 82.

95. *Id.*

96. *Id.*

97. *See generally, e.g.* Fisch, *Complex Litigation*, *supra* note 1; Fisch, *Class Action Reform*, *supra* note 4; Henry Gottlieb, *Study Frowns on Class Action Auctions: 3rd Circuit task force says judges should significantly limit their use of competitive bidding for class action counsel* , LEGAL TIMES, Feb. 4, 2002, at 6; Weiss, *supra* note 9, at 568–69; Karen Gullo, *Milberg Weiss Fights Ruling on Securities Suits Fees*, BLOOMBERG NEWS, Feb. 15, 2002.

98. *See* Gottlieb, *supra* note 97, at 6.

99 148 F. Supp. 2d 967 (N.D. Cal. 2001).

100. Gullo, *supra* note 97, at ¶ 6 (finding the "case may shape the way securities firms jockey for millions of dollars in fees" against corporations such as Enron).

101. *In re* Oracle Sec. Litig., 136 F.R.D. 639, 648 (N.D. Cal. 1991).

is trying to best serve the plaintiff class. The Third Circuit Task Force on the Selection of Class Counsel concluded that when courts primarily consider price in the selection of counsel, they create the risk of "low quality representation."[102]

Emphasizing price also creates the problem that courts may not be able to characterize a fair price. Courts may not know what contingent fees "sophisticated members of the plaintiff class would be prepared to pay and that competent and experienced securities lawyers would be prepared to accept."[103] In response to *Copper Mountain*, lawyers from a firm whose bid was rejected charged that "judges have no business rejecting lead plaintiffs on the basis that they think the lawyers are charging too much."[104] Critics conclude that courts cannot know precisely what fees plaintiffs in an efficient market would agree to "given an understanding of the particular case and the ability to engage in collective arms-length negotiation with counsel."[105]

Uncertainty has always plagued the world of class actions. Courts have never known what fees plaintiffs or lawyers would agree to. Courts traditionally have made fee awards "in a partial vacuum, looking only at the fees that plaintiffs' attorneys have requested and [that] courts have awarded in other, more or less comparable cases."[106] Far from exacerbating the problem, the auction process may in fact enhance the judge's perspective in making the fee award decision. By having the opportunity at the onset of litigation to carefully review the requested fees, courts can compare the data and determine what fees appear reasonable to the attorneys. With that information, courts can better evaluate the choices available to plaintiffs and how those plaintiffs would select counsel.[107]

Still, many point to an imbalance between attorneys' fees and individual class member recoveries and argue that the

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102. *Third Circuit Task Force Report on the Selection of Class Counsel* 45 (Jan. 2002) [hereinafter *Third Circuit Task Force*], *available at* http://www.ca3.uscourts.gov/classcounsel/final%20report%20of%20third%20circuit%20task%20force.pdf.

103. Weiss, *supra* note 9, at 568.

104. Gullo, *supra* note 97, at ¶ 8.

105. Goldberger v. Integrated Res., Inc., 209 F.3d 43, 52 (2d Cir. 2000).

106. Weiss, *supra* note 9, at 568.

107. For an argument that Judge Vaughn Walker actually demonstrated a sophisticated grasp of agency-cost issues in *In Re Oracle Sec. Litig.*, 136 F.R.D. 639 (N.D. Cal. 1991), *see* Weiss & Beckerman, *supra* note 18, at 2072.

court's focus on price does not correct this imbalance.[108] The *Cendant* court addressed this problem by considering factors other than just price in the bidding process.[109] For example, the court required each bidder to submit its qualifications, including prior experience.[110] The court also required bidders to state their ability to undertake the costs of the litigation.[111] Additionally, the court reserved the right to reject any bids not made in good faith.[112] In light of the *Cendant* case, courts obviously recognize focusing solely on price may prove insufficient in selecting counsel, since the *plaintiff* himself is likely to consider factors in addition to price in selecting counsel.

B. Introducing New Factors: Criticisms Without Merit

Nevertheless, even the introduction of factors other than price has drawn criticism, which usually falls into one of two categories. First, some critics concern themselves not with the introduction of other factors necessarily, but with how the auction process incorporates these factors into the bidding. A multi-factor bidding structure that weighs each of the non-monetary factors more heavily than the current process does may satisfy these critics. The second kind of criticism is that multi-factor auctions are improper methods of selecting lead counsel because, in reality, courts do not look at the factors but make decisions based on price. This criticism simply overlooks the sophistication and concern with which judges have appointed lead counsel for plaintiff classes. Each type of criticism, however, could be quelled by an act from Congress dictating how the many factors relevant to lead counsel selection are to be weighed by courts.

1. Implementation, Implementation, Implementation

Critics concerned about how courts incorporate non-monetary factors in the bidding process argue that courts do not adhere to a consistent model of what weight each factor will

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108. Fisch, *Class Action Reform*, *supra* note 4, at 553.

109. 182 F.R.D. 144, 151 (D.N.J. 1998). *See supra* note 92 for the court's list of applicable factors.

110. *Id.*

111. *Id.*

112. *Id.*

carry.[113] Perhaps a uniform approach to weighing the factors, dictated by Congress, may pacify critics concerned with the implementation of the auction process as a multi-factor process. Courts appear to give great weight to seemingly unimportant facts, while altogether ignoring important ones. For example, although a bidder might reasonably assume that a firm's size and location as well as its litigation experience within the circuit would weigh in its favor, one court concluded that precisely the opposite was true.[114] That court held that a smaller firm with no local offices and no "litigation experience in the circuit would give it greater incentives to succeed."[115]

Similarly, critics are concerned about how trial experience will weigh in the multi-factor bidding structure. Because securities fraud class actions rarely reach the trial stage, courts potentially might give insufficient weight to trial experience in analyzing a firm's qualifications to serve the plaintiff class.[116] With the PSLRA, however, Congress sought to deter early settlement when that settlement is based on the plaintiff's lawyer's desire to maximize profits. Therefore, if fewer cases settle early and progress closer to trial, trial experience may become increasingly important to a court's selection of lead counsel. It remains unclear, then, whether or not trial experience should weigh heavily in a firm's favor. These concerns regarding the implementation of the auction process could be addressed by a Congressional mandate directing courts how to weigh the multiple factors relevant to selecting lead
counsel.

2. Sophistication

Other critics of the multi-factor auction process assume that the amorphous nature of the multi-factor auction process really allows judges to disguise their price-based choices of lead counsel. These critics fail to see the sophistication with which judges appoint lead counsel. Again, these critics may be quieted by a Congressional mandate dictating how the multiple factors will be weighed in an auction for lead counsel.

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113. Fisch, *Complex Litigation*, *supra* note 1, at 84.
114. *Id.*
115. *Id.*
116. Fisch, *Complex Litigation*, *supra* note 1, at 84.

For example, the Third Circuit Task Force suggested that the lack of information at the early stages of litigation may distort bids.[117] This concern assumes that bidding will reduce the investigation of claims since law firms will only expend resources they can recover after winning the bid.[118]

This concern, however, fails to consider two facts. First, even before the PSLRA, attorneys did not engage in early investigation, but instead filed sloppy claims.[119] Second, this concern fails to consider that the auction process has already accounted for the amount of time and energy spent in this early investigation of claims in their decisions regarding lead counsel. Additionally, the fact that a court evaluates a firm's early investigative efforts in reaching its decision will not deter but will increase the investigation of claims. This creates the possibility that a firm engaging in this investigation may uncover helpful information, which may lead to a larger award than that which would have resulted without the auction process's added incentive to engage in early investigative efforts.

Another criticism of the multi-factor auction process as a method of lead counsel selection stems from *Sherleigh Associates v. Windmere-Durable Holdings, Inc.*, where the judge decided to evaluate bid proposals on a price-quality continuum [120] Here, the judge introduced quality considerations—i.e., factors based on firm quality—into the bid structure, including the firm's experience in securities litigation, the firm's qualifications to complete the work, and evidence that the firm had evaluated the case.[121] The court, however, gave no indication as to how it would evaluate these factors.[122] By not specifying which factors demonstrated firm quality, the court vindicated critics who argue that "quality considerations" simply rationalize the court's selection.[123] One critic suggested that in *Oracle*, Judge Walker exclusively based his selection of lead counsel on

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117. *Third Circuit Task Force*, *supra* note 102, at 46–47.

118. Gottlieb, *supra* note 97, at ¶ 17. *See also* Fisch, *Complex Litigation*, *supra* note 1, at 93 (concluding that those engaging in early investigation "face a risk that they will not be compensated").

119. Fisch, *Complex Litigation, supra* note 1, at 57.

120. 184 F.R.D. 688 (S.D. Fla. 1999).

121. *Id.* at 696.

122. Fisch, *Complex Litigation*, *supra* note 1, at 84 (discussing *Sherleigh Assocs.*, 184 F.R.D. 688). This, of course, suggests the first category of criticisms, i.e., that the implementation of a multi-factor auction process is flawed.

123. *Id.*

price, rather than the other factors he purported to weigh, since he appointed the lowest-bidding attorney.[124] Not only is there no evidence to suggest this has occurred—or that any other method of selecting lead counsel would not result in the same alleged abuse—but this criticism seems to dismiss that it was the distrust of lawyers—and not judges—that led to the PSLRA and, subsequently, the auction process.

In fact, in *Copper Mountain*, Judge Walker rejected the lowest bid.[125] After bidding higher than another firm, the losing firm achieved a new low bid when it "hastily established its fee in a hallway meeting with clients, rather than conducting 'meaningful arms-length bargaining,' according to court papers."[126] In rejecting the lowest bid as illgotten, Judge Walker appears not to have focused on price but on the access of the plaintiff class to fair market negotiations. Critics who argue that courts ignore factors other than price in auctions overlook the sophistication and concern with which judges have appointed lead counsel for plaintiff classes.

C. Keeping Lead Plaintiff Satisfied with Lead Counsel

Some commentators are disenchanted with the auction process because the lead plaintiff could be disappointed by the court's selection of lead counsel. First, the lead plaintiff may have had no prior connection to or association with the court's chosen lead counsel. This, the critics argue, may "weaken the relationship between the lead plaintiff and class counsel and specifically reduce the ability of the lead plaintiff to exert control over litigation decision-making."[127] Although the auction process has neither created nor exacerbated this problem, it does have the ability to address it.

Two possible solutions exist. First, a judge can consider the plaintiff's chosen counsel in the bidding calculations. The plaintiff's choice for lead counsel will then have a weighted bid in her favor. Since courts have already demonstrated a willingness to look at factors beyond the price, they appear recep-

124. *Id.* at 83.
125. 148 F. Supp. 2d 967 (N.D. Cal. 2001).
126. Gullo, *supra* note 97, at ¶ 13.
127. Fisch, *Complex Litigation*, *supra* note 1, at 95.

tive to this new factor as well.[128] Second, the judge could allow the plaintiff's original choice of counsel to match the winning bid. Arguably, whomever the plaintiff originally selected as lead counsel should have the opportunity to reenter a bid with attorneys' fees set the same as that of the winning bid. This would fulfill the purpose of the auction process—the simulation of an open market—as well as the benefits of a lead plaintiff familiar with lead counsel for the litigation.

Although it appears that if a court applies both of these solutions, plaintiff's choice of counsel would receive the advantage of both a weighted bid and the opportunity to match the winning bid, these advantages do not operate simultaneously. That is, if the plaintiff's choice of counsel wins the bid in the first instance, she will thus have no need to match the winning bid, so there is no double benefit. Should counsel lose, her weighted bid will not change the outcome because only her willingness to lower her fees to match the winning bid matters.

The *Cendant* court implemented this second option. The judge there instructed that if the lead plaintiff's designated counsel were the lowest qualified bidder, the court would appoint that attorney.[129] If the lowest qualified bidder were some other firm, the court gave the lead plaintiff's present counsel, "if otherwise qualified," the opportunity to agree to the terms of the lowest qualified bid.[130] If the lead plaintiff's counsel accepted those terms, the court granted lead counsel status.[131] If counsel did not exercise this right of first refusal, the court appointed the lowest qualified bidder to serve the plaintiffs.[132] This method appropriately assured that the lead plaintiff's choice of counsel had the opportunity to serve as lead counsel.

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128. For cases looking at factors other than price in a bid, see, e.g., *In re* IBP, Inc., Sec. Litig., No. 01-4031, 2001 U.S. Dist. LEXIS 7898 (D.S.D. June 7, 2001); *In re* Razorfish, Inc. Sec. Litig., 143 F. Supp. 2d 304 (S.D.N.Y. 2001); *In re* Auction Houses Antitrust Litig., 197 F.R.D. 71 (S.D.N.Y. 2000); *In re* Lucent Techs., Inc., Sec. Litig., 194 F.R.D. 137 (D.N.J. 2000); Sherleigh Assocs. v. Windmere-Durable Holdings, Inc., 184 F.R.D. 688 (S.D. Fla. 1999); *In re* Cendant Corp. Litig., 182 F.R.D. 144 (D.N.J. 1998); Wenderhold v. Cylink Corp., 188 F.R.D. 577 (N.D. Cal. 1999); *In re* Bank One S'holders Class Actions, 96 F. Supp. 2d 780 (D. Ill. 2000); *In re* Amino Acid Lysine Antitrust Litig., 918 F. Supp. 1190, 1193 (N.D. Ill. 1996) (competitive proposals may be beneficial "provided that the selection criteria include qualitative factors affecting representation of the class . . .").

129. *In re* Cendant Corp. Litig., 182 F.R.D. at 151.

130. *Id.*

131. *Id.*

132. *Id.*

In fact, this process may better situate the lead plaintiff, and the plaintiff class generally, with regard to recovery and still give plaintiffs the counsel of their choice.

Another argument suggests that questioning a plaintiff's choice of lead counsel by using an auction process may discourage institutional investors from seeking the role of lead plaintiff. The Third Circuit Task Force found that the PSLRA aimed to put plaintiffs, not lawyers, in control of class actions and to ensure that the "most adequate" plaintiff will choose counsel and negotiate a reasonable fee.[133] Although this purpose may be furthered by having institutional investors as lead plaintiffs, the auction process discourages institutional-investor participation by focusing on price and not these plaintiffs' selection of counsel.[134]

Three arguments, however, contradict this theory. First, most scholars agree that before the PSLRA, lead plaintiffs had no real role in securities class action litigation.[135] Even since the enactment of the PSLRA, the role of lead plaintiff remains insubstantial. Thus, the presence of an institutional investor as lead plaintiff may make little difference in the litigation. Second, the purpose of appointing a lead plaintiff stems from the idea that the person with the greatest interest at stake in the litigation should take the lead role.[136] If an institutional investor truly is the plaintiff with the most at stake, the lack of lead counsel choice will not deter this investor from protecting its substantial assets.[137] Third, if a court allows the lead plaintiff's choice of counsel to match the winning bid, the lead plaintiff may work with its choice of counsel, provided that its choice of counsel exercises the right of first refusal. Therefore, the proposed modification of the auction process and the PSLRA itself answer the concern that institutional investors will be deterred from seeking appointment as lead plaintiffs.

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133. *Third Circuit Task Force*, *supra* note 102, at 75.

134. Gottlieb, *supra* note 97, at ¶ 13.

135. *See, e.g.*, Fisch, *Class Action Reform*, *supra* note 4; Thomas & Hansen, *supra* note 2; Weiss, *supra* note 9; Alexander, *supra* note 2.

136. *See* S. REP. NO. 104-98, at 6 (1995).

137. *See* H.R. CONF. REP. NO. 104-369, at 34 (1995).

D. More Advantages to the Auction Process

A positive result of the auction process is that "the court simultaneously selects lead counsel and determines counsel's fee."[138] This saves the time spent at the close of litigation when attorneys normally apply to the court for their fees. It also reduces the incentive during the litigation for the attorneys to settle early to receive a greater profit. The result in *In re Amino Acid Lysine Antitrust Litigation*,[139] in which the court ordered the filing of competitive bids for lead counsel, illustrates this benefit. That decision employed the auction process because it found that "[c]ompetitive bid proposals to serve as lead counsel for the plaintiff class may be beneficial to the plaintiff class in this antitrust action provided that the selection criteria include qualitative factors affecting representation of the class, as well as attorneys' fees that would be charged by proposed lead class counsel."[140] Again, the court believed factors other than price were vital in determining who would best serve as lead counsel. In *Lysine*, the successful bidder ultimately received

> something in the range of just 6% of the total class recovery of well over $50 million—meaning that the class members realized about 94% of what the defendants had ultimately paid in settlement. That meant the plaintiff class was somewhere between $5 million and $10 million better off in pocket than would have been true in the typical lead counsel–liaison counsel-counsel committee arrangement, with scads of lawyers feeding at the trough.[141]

Here, the selection of lead counsel through an auction resulted in qualified representation based on a competitive market simulation and a better class recovery than would have been had in the absence of an auction.

Finally, the auction process may better determine the lead counsel than other traditional methods because of how it formulates the award of attorneys' fees. Both the lodestar method

138. Fisch, *Complex Litigation*, *supra* note 1, at 80.
139. 918 F. Supp. 1190, 1192 (N.D. Ill. 1996).
140. *Id.* at 1193.
141. *In re* Bank One S'holders Class Actions, 96 F. Supp. 2d 780, 785 n.5 (D. Ill. 2000).

and the benchmark approaches present problems.[142] The lodestar approach allows the trial judge to base the attorneys' fees on the number of hours the attorneys spent in litigation.[143] This creates an incentive for the attorneys to spend exhaustive hours on relatively simple cases in order to report as many hours as possible. The benchmark approach allows the trial judge to set a percentage of the plaintiff class recovery as the attorneys' fees, often subject to adjustment based on performance or the complexity of the litigation.[144] Under this approach, judges rarely review the work done by the attorneys.

The lodestar and benchmark approaches magnify the potential for poor selection of lead counsel for at least two reasons. First, the "uncertain game of assessing fees under the lodestar calculation ... discourages well qualified but risk-averse lawyers from class action practice."[145] The lodestar calculation only pays well if the plaintiffs succeed. Second, the monitoring of a "class counsel's performance is impeded by restricting judicial review to class counsel's fee application."[146] Setting attorneys' fees in advance of trial may be better for two reasons. First, under the benchmark of lodestar approaches, attorney performance has already been good, bad, or indifferent when courts get around to evaluating it.[147] Second, at the end of trial, the judge has little incentive to effectively review attorney performance.[148]

In contrast, under the auction process, "[a] court must evaluate the quality of a competitive bid at the time of bidding and thereafter monitor class counsel's performance during the

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142. Most courts have traditionally used one of these two methods for awarding attorney fees in class action cases. For a circuit-by-circuit survey see 3 HERBERT B. NEWBERG & ALBERT CONTE, NEWBERG ON CLASS ACTIONS 105 (3d. ed. Supp. 2002).

143. *See, e.g.*, Hanlon v. Chrysler Corp., 150 F.3d 1011 (9th Cir. 1998) (approving lodestar method for determining fee award).

144. *See, e.g.*, Camden I Condominium Ass'n, Inc. v. Dunkle, 946 F.2d 768, 774 (11th Cir. 1991) ("Henceforth in this circuit, attorneys' fees awarded from a common fund shall be based upon a reasonable percentage of the fund established for the benefit of the class."); Swedish Hosp. Corp. v. Shalala, 1 F.3d 1261, 1272 (D.C. Cir. 1993) (concluding that percentage of the fund method "is the proper method for awarding attorney fees in common fund class actions").

145. Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiff's Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 54 (1991).

146. *In re* Oracle Sec. Litig., 136 F.R.D. 639, 648 (N.D. Cal. 1990).

147. *Id.*

148. *Id.*

litigation."[149] Already this improves upon both of the previous approaches, as it eliminates inappropriate incentives those approaches create. Furthermore, "[c]ompetitive selection does not make price supreme and determinative, but forces the lawyers and courts to deal with the *quality* of class counsel's services."[150] As a result, plaintiff classes have the opportunity for better representation because courts directly evaluate the quality of the representation. The auction process then becomes a much more appropriate means of determining attorneys' fees than either the lodestar or benchmark approaches. These benefits over the two traditional approaches are likely what attracted judges to this solution originally.

The auction process may have another potentially positive effect since "disappointed bidders are likely to be on the lookout for shortcomings in the performance of the winner."[151] With disappointed bidders reviewing their work, lead counsel will have additional incentive to apply best efforts to the plaintiff's case. Even Professor Fisch, a well-respected *and* virulent critic of the auction process, concedes that auctions can allow courts to avoid a number of problems traditionally associated with the selection of class counsel, [152] and that auctions at least appear "no more problematic than the [benchmark] or lodestar methods of determining counsel fees."[153]

CONCLUSION

Generally, class action attorneys perform a public service to protect innocent investors.[154] By offering representation on a contingent fee basis, class action attorneys allow small shareholders to file claims for securities frauds. The system that initially attempted to protect these investors, however, has transformed into a system in which the shareholders and their representatives do not share the same goals. As a result, plaintiffs' attorneys have profited greatly in a system that may no longer serve the public.

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149. *Id.* at 648.
150. *Id.* at 649.
151. *Id.*
152. Fisch, *Complex Litigation*, *supra* note 1, at 82.
153. *Id.* at 91.
154. Weiss & Beckerman, *supra* note 18, at 2055.

The PSLRA attempts to maintain this public service, but also limits opportunities for attorneys to abuse the process. The PSLRA eliminates the race to the courthouse that had plagued securities litigation prior to its enactment. Those seeking appointment as lead plaintiff cannot simply be the first to file suit. The PSLRA requires a lead plaintiff to have a large stake in the outcome of the litigation and fulfill the requirements of Rule 23. The provision for appointment of lead counsel subject to judicial approval aims to eliminate abuse of the securities litigation system. Indeed, Congress, through the PSLRA sought to transfer securities fraud litigation back into the hands of the injured plaintiffs from the hands of opportunistic attorneys.

The extent to which the procedural reforms of the PSLRA, including the lead plaintiff provisions, will transfer control of securities class actions from lawyer to client remains unclear.[155] The auction process, however, does nothing to interfere with that goal, and if appropriately used, can further it. No longer can plaintiffs' attorneys rush their clients into deals in courthouse hallways. Judges may consider many factors other than price, including experience, time spent investigating the claim, and the plaintiff's choice of counsel. Additionally, Congress should consider mandating a multi-factor auction process incorporating many of the factors discussed above, as well as mandating what weight each factor should receive, in order to satisfy the critics of the auction process. The evidence demonstrates that PSLRA has succeeded in preventing many abuses of securities class actions. The uniform auction process stands alone in its ability to maximize the benefit to the plaintiff class by minimizing grotesquely large fee awards.

Finally, the auction process directly results from the PSLRA and from Congress's desire to transfer litigation control back to the plaintiff class. Courts interpret that to give plaintiffs the opportunity to engage in a fair market evaluation. Until Congress lists the criteria by which to appoint lead counsel, it has entrusted the final decision to trial courts. Thus far, the decision has remained safe in their hands.

155. Fisch, *Class Action Reform*, *supra* note 4, at 550.