

# Should European institutions make the effort to see companies in court?

Scepticism of US lawyers and a reluctance to sue companies in which they invest, are two reasons European institutions avoid litigation over losses. But with €1.9bn going unclaimed and court action spurring good governance States-side, continental managers may have an obligation to take the legal route, writes Elizabeth Cripps

Given the frequent depiction of the US as a 'litigation culture', it should come as no surprise to those on this side of the Atlantic that US institutional investors have been quick to use legal action to recoup investment losses. More than 40 per cent of lead plaintiffs in class action cases are institutional investors, according to 2004 PricewaterhouseCoopers data cited by US securities litigation firms.

But could this level of involvement in American litigation ever take off in Europe, where the institutional arena is marked by a very different culture, and a decided mistrust of the US legal system?

With securities fraud cases continuing to make headlines, and increasingly global investment portfolios giving them an ever-growing stake in US companies, it seems that European institutions have at least to consider the possibility.

## Money for nothing

According to David Scott, managing partner at US securities litigation law firm Scott + Scott, many European institutions miss out even on the class action settlements to which they become automatically entitled: "Last year, the European investment community failed to collect on \$2.4bn (€1.9bn) in claims, out of total settlements of approximately

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Crispin Lace, Watson Wyatt



\$7bn (€5.5bn). This year, you have WorldCom and Enron, which in themselves far exceed the total of last year."

Dutch pension fund ABP is "automatically involved in a few hundred cases in the US", according to René Maatman, chief legal counsel of ABP Investments. He warns: "That's a number quite a few investors may not be aware of."

In the US, according to Mr Scott, this failure to fill in a claim form would amount to a breach of obligation to pension holders: "As a trustee, you have an obligation to make sure you know what's going on

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René Maatman, ABP Investments



with the status of litigation." The theory, he explains, is that a claim for security fraud against a company in which a pension fund has invested is, ultimately, an asset of that fund.

In Europe, attitudes are starting to change. "I do notice that more institutional investors, among them pension funds, are looking more closely at monitoring a whole 'portfolio' of class action cases in which they are involved," Mr Maatman says.

However, it is a big step from this to putting oneself forward as lead plaintiff, or opting out of class action and suing a company directly.

Crispin Lace, senior investment consultant at Watson Wyatt, who has worked with pension funds in the Nordic region, Germany and Austria, says: "I haven't really had much experience of any of them looking at this sort of class action." Mr Maatman confirms that the trend, as he has seen it, has been very much towards monitoring existing class action, "not so much to becoming lead plaintiff or opting out".

ABP itself made news earlier this year with its decision to opt out of class action against Royal Dutch/Shell, for mis-estimation of its oil reserves, and initiate its own suit. This the only case in which it has done so.

According to Mr Scott: "There have been several Dutch and German investors who have moved for appointment as lead plaintiff". And for fellow US attorneys Schiffrin & Barroway (S&B), an education campaign in Europe has been taking effect, particularly in Scandinavia.

According to head of investor relations Darren Check, S&B recently filed for lead plaintiff status in an options back-dating suit against United Health. As well as the Retirement Board of Allegheny County, three European names were put forward: Austrian fund company Erste Spar Invest, Danish pension fund PKA, and Swedish pension fund AP7. The firm also has four Swedish investors – two pension funds and two fund companies – on its books, who "will be bringing a direct action against a pharmaceutical company".

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Darren Check, Schiffrin & Barroway



## Why make the effort?

So why should European institutions get involved to the extent of becoming lead plaintiff, or even opting out of class action to sue a company directly? After all, as Mr Maatman puts it: "To become lead plaintiff in certain circumstances is burdensome. It is certainly more work than staying in the class."

Another deterrent is the perceived stigma of being involved in US litigation, according to Schiffrin & Barroway's Mr Check. He adds: "I have had clients who have said: 'I will be involved if you can bring another European institution to the table:'"

Mr Scott reports "a tremendous amount of scepticism about US lawyers" in his conversations with Nordic institutions. Another key factor is the fear that becoming lead plaintiff will be expensive.

European institutions also have a very different culture when it comes to shareholder activism. "If you look at what the European investment community does to effectuate corporate governance changes, it is more letter writing campaigns," says Mr Scott.

In the Nordic region in particular, Mr Lacey reports a tradition of en-

gagement with company management. Nordic institutions, he says, "come from a background where company management tends to listen to what they say, and things can be achieved through discussion".

In this context, taking legal action might seem aggressive, even counterproductive. The question for European institutions, is, to quote Mr Check: "Why would I want to sue a company I own stock in?"

The answer is that this, at least in the US environment, is often the way to achieve corporate governance change. "Class action," says Mr Check, "is no longer just a vehicle to get money back. Through class action securities litigation we can effectuate good corporate governance, and that is a key to the long-term sustainability of the investment."

European institutions, as they invest more in US firms, need to consider the US way of doing things, just as US pension funds investing in Europe can benefit from adopting the European approach.

But even in terms of getting money back, institutions have to ask whether a suit is more or less likely to succeed if it, the institution, is lead plaintiff. Some judges, notes Mr Maatman, might look more favourably on an institutional investor as lead plaintiff than on "some other parties that are active in that area".

European institutions are also mistaken, in assuming that they risk huge costs by becoming lead plaintiff. "We work strictly on a success fee basis," says Mr Scott. "We front all costs, then we make an application to the court for a payment of legal fees out of the settlement. The court decides if the fee request is fair and reasonable. The judge acts as gatekeeper to the class."

No win, no fee. A very American phrase, but perhaps European institutions can no longer afford to ignore it.

## The ABP experience: massive losses lead to close monitoring

Nordic pension funds could learn from the experience of European giant Stichting Pensioenfonds ABP. The €194bn pension fund for Dutch government and education workers has had US class action on its radar since 2001.

"We noticed that we might leave a lot of money on the table if we did not monitor the current cases," explains René Maatman, chief legal counsel of ABP Investments. This was timed with the high profile accounting fraud cases, which marked the start of the century. "We were, of course, confronted with giant losses in our portfolio."

Accordingly, ABP began to monitor all the class action cases in which it was involved. At the same time, Mr Maatman says: "We looked more closely at a few cases in particular – those with extraordinary losses or where the case was exceptionally strong in our view." Now, if a loss amounts to at least €20m, ABP makes an explicit evaluation as to whether to remain in the class or to opt out and start its own proceedings.

"You are automatically part of the class," points out Mr Maatman. "The decision is whether to be lead plaintiff, and whether to opt out. We make those decisions depending on the circumstances,

in particular our own losses and the quality of the case, but also who the other parties are that ask the judge to be lead plaintiff."

The fund has opted out on several occasions, starting its own case against Bristol Myers, Quest, AOL, Delphi Corporation and, of course, Shell. In a statement in January, ABP explained the decision to leave the class action and start its own suit against Shell.

Pointing out that other European institutions had made the same decision, the statement noted the risk that, "in due course, European investors could be excluded from the shareholders in the 'class' of the class action suit".

In general, according to Mr Maatman, various factors could determine whether it is optimal to opt out of a class action and act independently: "It could be that we think we have a better case than the lead plaintiff because we were in different circumstances. It might also be the case that we think we might be able to hire a better outside counsel."

It could also make a difference, he says, if the lead plaintiff is not "a generally respected institutional investor". Finally, the fee arrangement "could be a motive – we can maybe negotiate a better fee with the outside counsel than the lead plaintiff did".