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"INFORMATION AND BELIEF PLEADING UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995"

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Glen DeValerio and Kathleen M. Donovan-Maher
Berman, DeValerio & Pease LLP

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Introduction

Securities fraud class action complaints based on plaintiff's "information and belief" have generated extensive discussion on such issues as (i) whether allegations based on "investigation of counsel" are exempt from "information and belief" pleading requirements; (ii) whether plaintiffs must plead "all facts" which form the basis for their information and belief; and (iii) whether plaintiffs must disclose the names of confidential sources that support the basis of such information and belief. This article addresses these three issues and discusses the authority on each point. Sneak preview – two circuit courts and numerous district courts have addressed these issues with the result being conflicting judicial interpretation.

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[1] Glen DeValerio and Kathleen Donovan-Maher are both partners at Berman, DeValerio & Pease LLP in Boston, Massachusetts. Mr. DeValerio is a frequent lecturer in various continuing legal education seminars on complex securities litigation and is the past President of the National Association of Securities and Commercial Law Attorneys ("NASCAT").

I. THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

The Private Securities Litigation Reform Act of 1995 (the "PSLRA") requires that all allegations regarding false statements or material omissions that are made on information and belief must "state with particularity all facts on which that belief is formed." 15 U.S.C. § 78u-4(b)(1). In particular, a complaint

> shall specify each statement alleged to have been misleading, the reason or reasons why the statement is misleading, and, if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed.

Id.

When statutory language is clear and unambiguous on its face there is no need to resort to the legislative history for interpretation. See United States v. Oregon, 366 U.S. 643, 648 (1961) ("Having concluded that the [statute] provisions of § 1 are clear and unequivocal on their face, we find no need to resort to the legislative history of the Act."); Ex parte Collett, 337 U.S. 55, 61 (1949) ("there is no need to refer to the legislative history where the statutory language is clear. 'The plain words and meaning of a statute cannot be overcome by a legislative history which through strained processes of deduction from events of wholly ambiguous significance, may furnish dubious bases for inference in every direction.'" (citation omitted)). A district court in the Northern District of California relied extensively on legislative history, however, in applying the "information and belief" provision of the PSLRA. In re Silicon Graphics, Inc. Sec. Litig., 970 F. Supp. 746, 763-64 (N.D. Cal. 1997), aff'd, 183 F.3d 970, 983-84 (9th Cir. 1999).

According to Silicon Graphics, the legislative history on information and belief allegations comes from consideration of an amendment to H.R. 1058, the House of

Representatives' version of the PSLRA, proposed by Congressman John Bryant, D-TX.[2] Congressman Bryant expressed his concern that:

> [A]t the beginning of the case plaintiff would have to set forth "with specificity all information," they have to give all the information in advance that forms the basis for the allegations of the plaintiff, meaning any whistle-blower within a securities firm involved would have to be uncovered in the pleadings in the very, very beginning.

Id. at 763 (quoting 141 Cong. Rec. H2848 (Mar. 8, 1995)). Congressman John Dingell, D-MI, ranking minority member of the House Commerce Committee, agreed with Congressman Bryant and stated that H.R. 1058, if passed without the Bryant amendment, would require that plaintiffs "must literally, in [their] pleadings, include the names of confidential informants, employees, competitors, Government employees, members of the media, and others who have provided information leading to the filing of the case." Id. (quoting 141 Cong. Rec. H2849 (Mar. 8, 1995)).

The district court in Silicon Graphics, 970 F. Supp. at 763-64, aff'd, 183 F.3d 970, 983-84 (9th Cir. 1999), placed great emphasis on the fact that Congressmen Bryant and Dingell voiced these concerns, but the Bryant amendment nevertheless failed. The Silicon Graphics court drew the conclusion that the PSLRA requires plaintiffs to disclose

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[2] Section 4 of H.R. 1058 as introduced in the House would have added a new Section 10A to the Securities Exchange Act of 1934 to immediately follow Section 10.

Section 10A(a) would have defined a fraudulent statement for purposes of Section 10(b) and set forth the proof required to establish defendant made a fraudulent statement, including proof of intent "to deceive, manipulate, or defraud."

Section 10A(b) would require specific allegations "sufficient to establish scienter as to each defendant at the time the alleged violation occurred" and that an allegation made on information and belief "set forth with specificity all information on which that belief is formed."

Section 10A(c) provided for dismissal (with the right to one amendment at the discretion of the court) if the pleading requirements were not met and a stay a discovery pending consideration of the motion to dismiss.

The Bryant amendment would have deleted Sections 10A(b) and (c) as proposed and substituted the following: "(b) Pleading Requirement. – In any action arising under this title in which the plaintiff may recover money damages only if it proves that the defendant acted with scienter, the plaintiff must allege in its complaint facts suggesting that the defendant acted with that state of mind." See 141 Cong. Rec. H2848 (Mar. 8, 1995).

all sources of information, including, for example, the names of confidential informants. 970 F. Supp. at 763-64. In particular, the Silicon Graphics court stated:

> Because 'Congress does not intend sub silentio to enact statutory language that it has earlier discarded in favor of other language,' Immigration & Naturalization Serv. v. Cardoza-Fonseca, 480 U.S. 421, 442-43, 107 S. Ct. 1207, 1219, 94 L.Ed.2d 434 (1987) (internal quotation marks and citation omitted), the Court concludes that plaintiffs must plead the sort of information described by Reps. Bryant and Dingell to meet the requirements of the SRA [Securities Reform Act] as enacted.

970 F. Supp. at 764.

Courts and commentators, however, have criticized the Silicon Graphics court's interpretation of the legislative history. See, e.g., Novak v. Kasaks, 216 F.3d 300, 313 (2d Cir. 2000) ("[T]his rule is based on a misreading of the legislative history of the PSLRA. Specifically, the court in Silicon Graphics relied primarily on the hyperbolic statements of legislators attempting (unsuccessfully) to amend the proposed Act to lighten plaintiffs' pleading burden."), cert. denied, 121 S. Ct. 567, 148 L.E.2d 486 (2000); "Securities Reform Act Does Not Require Plaintiff to Name Sources", E.D. Pa. Rules, 4 No. 16 Andrews Sec. Litig. & Reg. Rep. 8 (April 28, 1999) (reviewing In re Aetna Inc. Securities Litigation, MDL 1219 n. 1 (E.D. Pa. March 24, 1999) and reporting that the court agreed with plaintiffs' argument that "the drafters of the Reform Act never intended to require plaintiffs to name vulnerable whistleblowers who could be subject to retaliation.").

Additionally, at least one commentator, in his securities law treatise, has devoted an entire section to the Silicon Graphics court's interpretation of the legislative history and has concluded that the analysis is flawed. Harold S. Bloomenthal, 3C Sec. & Fed. Corp. Law § 16:25.8 (1999). Bloomenthal supports his conclusion with the fact that the

bill the House adopted, H.R. 1058, was not the same bill that passed the entire Congress. H.R. 1058 was amended in the House and Senate Conference Committee. Id. Furthermore, Congressman Bryant's proposed amendment did not simply address the information and belief language but also would have lessened the standard for pleading scienter and eliminated the stay of discovery pending resolution of the motion to dismiss provision. Id. Further, according to Bloomenthal, "[a] fair reading of the debate over the Bryant amendment in its entirety makes clear that the debate primarily was over the standard for pleading scienter. A primary reason the House rejected the Bryant amendment was because it would have softened this aspect of H.R. 1058 as proposed and adopted by the House." Id.; see also 141 Cong. Rec. H2850 (Mar. 8, 1995) (stating view of Congressman Christopher Cox, R-CA: "Ironically the amendment is completely inconsistent with Federal Rules of Civil Procedure 9(b) because, while it requires that one pleads fraud or particularity, the Bryant amendment would let a costly lawsuit go ahead if the complaint only 'suggests that fraud may have occurred.'").

During the debate on the Bryant amendment, there was very limited reference to the information and belief language, and that isolated reference is what the Silicon Graphics court concentrated on when it ruled that plaintiff's complaint must provide detailed facts, including the names of confidential sources. Harold S. Bloomenthal, 3C Sec.& Fed. Corp. Law § 16:25.8 (1999). The Silicon Graphics court went so far as to hold that allegations referring to documents that support plaintiff's information and belief should include "the titles of the reports, when they were prepared, who prepared them, to whom they were directed, their content, and the sources from which plaintiffs obtained this information." 970 F. Supp. at 767.

Some courts have adopted the Silicon Graphics interpretation of the information and belief language and have concluded that the PSLRA raised the information and belief standard of Federal Rule of Civil Procedure 9(b) such that a plaintiff in a securities fraud action must now provide extremely detailed documentary and testimonial evidence. See In re Green Tree Fin. Corp. Stock Litig., 61 F. Supp. 2d 860, 871-2 (D. Minn. 1999) (one allegation of securities fraud complaint dismissed when basis for plaintiff's allegations was an admission made to an unnamed source); Novak v. Kasaks, 997 F. Supp. 425, 431-32 (S.D.N.Y. 1998), vacated, 216 F.3d 300, 313 (2d Cir. 2000); Chan v. Orthologic Corp., No. 96-1514 PHX RCV, 1998 WL 1018624, at *8, *16 (D. Ariz. Feb. 5, 1998) (the PSLRA "has strengthened the requirement of Rule 9(b)" – plaintiffs must "include all information about the source of any information if pleaded on information or belief"); Silicon Graphics, 970 F. Supp. at 763-64, aff'd, 183 F.3d at 983-84.

Some courts that have rejected the Silicon Graphics view have concluded that the information and belief provision of the PSLRA merely codifies the Rule 9(b) requirement as it existed before the PSLRA's enactment. See McNamara v. Bre-X Minerals, Ltd., 57 F. Supp. 2d 396, 405-06 (E.D. Tex. 1999) (discussing PSLRA "information and belief" language, noting that the Fifth Circuit has indicated that the statutory language is an adoption of the Second Circuit's requirement and concluding "the pre-Reform Act caselaw regarding the particularity requirements of Rule 9(b) is relevant."); In re Digi Int'l, Inc. Sec. Litig., 6 F. Supp. 2d 1089, 1095 n. 2 (D. Minn. 1998) ("Court finds that those allegations sufficient under Rule 9(b) are also sufficient under the Reform Act. Likewise, the Court concludes that the allegations that fail to meet the pleading standards under the Reform Act are also inadequate under Rule 9(b)."); cf. Hallwood Realty

Partners, L.P. v. Gotham Partners, L.P., 95 F. Supp. 2d 169, 178 (S.D.N.Y. 2000) ("Under long standing precedents in this circuit and under the PSLRA, a plaintiff making such an allegation on information and belief must set forth the factual basis on which it rests.").

Numerous other courts, however, including the Second Circuit, have rejected the Silicon Graphics view. See Novak, 216 F.3d at 313 (the PSLRA "does not require that plaintiffs plead with particularity every single fact upon which their beliefs concerning false or misleading statements are based"), vacating, 997 F. Supp. 425, at 431-32; In re Aetna, Inc. Sec. Litig., MDL No. 1219, at 1 (E.D. Pa. Mar. 24, 1999) (stating the PSLRA "did not require [p]laintiffs to name the 'human sources' that were consulted as part of counsel's investigation."); aff'd, No. 99-2019 (3d Cir. May 5, 1999); In re First Merchants Acceptance Corp. Sec. Litig., No. 97C2715, 1998 WL 781118, at *7 n. 3 (N.D. Ill. Nov. 4, 1998) ("The complaint sets forth detailed allegations of fraud and alleges substantially more than 'rumor or hunch.' The fact that Plaintiffs do not have all of the specific documents to support their claims at this time is not fatal to their complaint." (citations omitted)); In re Digi Int'l, Inc. Sec. Litig., 6 F. Supp. 2d 1089, 1096-97 (D. Minn. 1998) ("[T]he Court declines to adopt the view that the language of the Reform Act mandates that each and every 'information and belief' allegation must be supported by underlying documentary evidence."); In re Cephalon Sec. Litig., 96-CV-0633, 1997 WL 570918, at *2 (E.D. Pa. Aug. 29, 1997) ("[The PSLRA] does not require pleading of all evidence and proof thereunder supporting a plaintiff's claim.").

II. DOES "INVESTIGATION OF COUNSEL" EQUAL "INFORMATION AND BELIEF?"

The court in In re Equimed, Inc. Securities Litigation, 98-CV-5374 NS, 2000 WL 562909 (E.D. Pa. May 9, 2000) recognized "[t]here is no binding authority on whether plaintiffs must state with particularity all facts on which their belief is formed when the allegations are based on 'investigation of counsel.'" 2000 WL 562909, at *4. The Equimed court concluded, however:

> To distinguish between "information and belief" and "investigation of counsel" is meaningless; it would permit evasion of the clear intent of a statutory mandate. Plaintiffs must state with particularity those facts upon which their allegations are formed, even if made upon "investigation of counsel."

Id.

Some courts interpreting the PSLRA have agreed with defendants' argument that allegations based on the investigation of counsel are allegations based on information and belief. See In re Theragenics Corp. Sec. Litig., 105 F. Supp. 2d 1342, 1351 (N.D. Ga. 2000) ("allegations based on the investigation of counsel are the equivalent of allegations based on information and belief"); In re Green Tree Financial Corp. Sec. Litig., 61 F. Supp. 2d 860, 872 (D. Minn. 1999) ("because an attorney is required, under Rule 11 of the Federal Rules of Civil Procedure, to investigate claims before filing a complaint, plaintiffs should not be allowed to avoid the heightened pleading standard by claiming 'investigation of counsel.'"); In re 3Com Sec. Litig., No. C-97-21083 JW, 1999 WL 1039715, *4 (N.D. Cal. July 8, 1999) ("a complaint made 'upon investigation of counsel' is the same as a complaint made 'upon information and belief'"); Brady v. Anderson, 97-2154(SHx) 1998 U.S. Dist. LEXIS 20774, at *10-12 (C.D. Cal. May 27, 1998) (rejecting plaintiffs' argument that allegations based on "investigation of counsel" are different than

"information and belief" pleading); Silicon Graphics, 970 F. Supp. at 763 ("Because the sources … do not provide plaintiffs with personal knowledge, the complaint must be based on information and belief – that is the only alternative."), aff'd, 183 F.3d 970, 991 (9th Cir. 1999).

Alternatively, a number of courts have agreed with plaintiffs' argument that a distinction does exist so that the "all facts" requirement for information and belief allegations does not apply to allegations based on the investigation of counsel. See In re Cell Pathways, Inc. Sec. Litig., No. 99-725, 2000 WL 805221, at *9 n. 9 (E.D. Pa. June 20, 2000) (the PSLRA "does not specify whether this 'heightened pleading standard' applies to allegations which are based upon investigation of counsel."); Lister v. Oakley, No. SACV97-809GLTEEX, 1999 WL 816928, at *3 (C.D. Cal. Jan. 14, 1999) ("Because Plaintiffs' Complaint is based on the investigation of counsel, they need not state with particularity all facts on which their beliefs are formed."); In re Aetna Inc. Sec. Litig., MDL No. 1219, Order No. 8, n. 1 (E.D. Pa. March 24, 1999); In re Employee Solutions Sec. Litig., No. CIV 97545PHXRGS(OMP), 1998 WL 1031506, at *5 (D. Ariz. Sept. 22, 1998) ("complaint states that its allegations are based on an extensive investigation by plaintiffs' attorneys, and mentions the documents reviewed by the attorneys. That is sufficient."); Warman v. Overland Data, Inc., No. 97CV833 JM (JFS), 1998 WL 110018, at *3 (S.D. Cal. Feb. 20, 1998) ("as plaintiffs have pled their allegations based on investigation of the attorney and not upon information and belief, the complaint need not state with particularity all the facts on which the belief is formed"); Queen Uno Ltd. Partnership v. Coeur D'Alene Mines Corp., 2 F. Supp. 2d 1345, 1353-54 (D. Colo. 1998) (court held plaintiffs did not plead on information and belief where

plaintiffs stated "Plaintiffs have alleged the foregoing based upon the investigation of their counsel"); Howard Gunty Profit Sharing v. Quantum Corp., No. 96 20711 SW, 1997 WL 514993, at *3 (N.D. Cal. Aug. 14, 1997) (court draws a distinction between allegations based on "information and belief" and "investigation of counsel"); Zeid v. Kimberley, 973 F. Supp. 910, 915 (N.D. Cal. 1997) (complaint "does not state that any allegations are based on 'information and belief' but rather, it asserts that [p]laintiffs obtained the facts through 'investigation of counsel.'…As such, Plaintiffs need not state with particularity all facts on which their beliefs are formed.").

Courts unanimously agree, however, that a prefatory statement preceding paragraph 1 of a complaint clearly does not satisfy the PSLRA's information and belief pleading requirements. See e.g., Feeney v. Mego Mortgage Corp., 45 F. Supp. 2d 1356, 1357 (N.D. Ga. 1999) (prefatory paragraph that allegations are founded on information and belief and based upon investigation of counsel fails to comply with the PSLRA); In re Aetna, Inc. Sec. Litig., 34 F. Supp. 2d 935, 942 (E.D. Pa. 1999) (prefatory paragraph provided "little, if any, specificity about the foundation for their attorneys' allegations"); In re Health Management Systems, Inc. Sec. Litig., 97 CV 1865(HB), 1998 WL 283286 , at *3 (S.D.N.Y. June 1, 1998) (prefatory paragraph "insufficient because it does not indicate what publicly available articles, releases and filings the plaintiffs relied on, nor does it indicate what 'other matters' of public record plaintiffs reviewed."); Brady v. Anderson, 97-2154(SHx), 1998 U.S. Dist. LEXIS 20774, at *11, 20-, 25-26, 32-33 (C.D. Cal. May 27, 1998) (dismissing complaint for failure to plead false statements adequately despite prefatory paragraph stating the complaint was based on SEC filings, securities analysts' reports and advisories, press releases, media reports, discussions with

consultants, and even former officers and employees of the company); Silicon Graphics, 970 F. Supp. at 763 (finding prefatory paragraph language insufficient), aff'd, 183 F.3d 970, 983-84 (9th Cir. 1999).

The court in Lirette v. Shiva Corp., 999 F. Supp. 164 (D. Mass. 1998) not only rejected plaintiff's prefatory paragraph that the complaint allegations were founded on "information and belief" and "investigation of counsel" but ordered the plaintiff to specify:

> as to each particular allegation (i.e., every sentence or clause separated by a comma or conjunction), whether that allegation is made upon information and belief or is supported by some document or statement on personal knowledge by a potential witness. Sources need not be specified, but the Court needs to know which is which.

Id. at 165.

III. ARE PLAINTIFFS REQUIRED TO PLEAD "ALL FACTS?"

Defendants in In re Cell Pathways argued, with regard to information and belief pleading, that even if plaintiffs provided some bases for their beliefs, the PSLRA's requirement of "all facts" was not met. 2000 WL 805221, at *10. The Cell Pathways court criticized the defendants for apparently reading "In re Advanta [180 F.3d 525 (3rd Cir. 1999)] as requiring that a plaintiff plead 'all conceivable facts' which would support their beliefs, without the benefit of discovery." 2000 WL 805221, at *10. The Cell Pathways court recognized "it is difficult to imagine how any complaint could survive so narrow a reading of that holding." Id.

The Second Circuit Court of Appeals in Novak v. Kasaks, 216 F.3d 300 (2d Cir. 2000) addressed the issue of pleading "all facts" and noted:

> In our view, notwithstanding the use of the word "all," paragraph (b)(1) does not require that plaintiffs plead with particularity every single fact

> upon which their beliefs concerning false or misleading statements are based. Rather, plaintiffs need only plead with particularity *sufficient* facts to support those beliefs.

216 F.3d at 313-14 (emphasis in original).

The Second Circuit in Novak continued:

> Paragraph (b)(1) is strangely drafted. Reading "all" literally would produce illogical results that Congress cannot have intended. Contrary to the clearly expressed purpose of the PSLRA, it would allow complaints to survive dismissal where "all" the facts supporting the plaintiff's information and belief were pled, but those facts were patently insufficient to support that belief. Equally peculiarly, it would require dismissal where the complaint pled facts fully sufficient to support a convincing inference if any known facts were omitted. Our reading of the provision focuses on whether the facts alleged are sufficient to support a reasonable belief as to the misleading nature of the statement or omission.

216 F.3d at 314.

The court in In re Theragenics Corp. Securities Litigation, 105 F. Supp. 2d 1342 (N.D. Ga. 2000) "agree[d] with the approach of the Second Circuit in its recent Novak decision." 105 F. Supp. 2d at 1355. The court in In re Secure Computing Corp. Securities Litigation, 120 F. Supp. 2d 810 (N.D. Cal. 2000) also agreed that plaintiffs are not required "to state every fact that they possess that is in any way related to allegations that are plead on information and belief. The PSLRA requires them to 'state with particularity all facts on which that belief is formed.' 15 U.S.C. § 78u-4(b)(1)."). 120 F. Supp. 2d at 817. The Secure Computing court continued:

> For example, if Plaintiffs make an allegation that is based on a statement from a witness, they must reveal all facts about that witness that were material to the formation of their belief that the witness' statement is accurate. The precise amount of detail that they must reveal depends on the circumstances. If Plaintiffs relied on the witness' job position or relation to Secure in deciding to believe the witness, the witness' job position or relation to Secure must be disclosed in the complaint. If Plaintiffs make an allegation about information that is likely to be known only to a few individuals, the actual identity of the source may be material,

> in which case the identity of the source must be plead in the complaint in order to satisfy the PSLRA.

Id.

IV. MUST CONFIDENTIAL SOURCES BE NAMED?

The Ninth Circuit in Silicon Graphics, 183 F.3d 970 (9th Cir. 1999), although not ruling on the issue of whether confidential sources must be disclosed during the pleading stage, held that plaintiffs failed to meet the PSLRA's information and belief pleading requirement and stated:

> a plaintiff must provide, in great detail, all the relevant facts forming the basis of her belief. It is not sufficient for a plaintiff's pleadings to set forth a belief that certain unspecified sources will reveal, after appropriate discovery, facts that will validate her claim. In this case, [plaintiff]'s complaint does not include adequate corroborating details. She does not mention, for instance, the sources of her information with respect to the reports, how she learned of the reports, who drafted them, or which officers received them. Nor does she include an adequate description of their contents which we believe – if they did exist – would include countless specifics regarding ASIC chip shortages, volume shortages, negative financial projections, and so on. We would expect that a proper complaint which purports to rely on the existence of internal reports would contain at least some specifics from those reports as well as such facts as may indicate their reliability.
>
> In the absence of such specifics, we cannot ascertain whether there is any basis for the allegations that the officers had actual or constructive knowledge of SGI's problems that would cause their optimistic representations to the contrary to be consciously misleading. In other words, in the absence of such specifics, we cannot determine whether there is any basis for alleging that the officers knew that their statements were false at the time they were made – a required element in pleading fraud. [Plaintiff] would have us speculate as to the basis for the allegations about the reports, the severity of the problems, and the knowledge of the officers. We decline to do so.

183 F.3d at 985 (citation omitted).

In In re McKesson HBOC, Inc. Securities Litigation, 126 F. Supp. 2d 1248 (N.D. Cal. 2000) defendants argued that based on the Ninth Circuit's holding in Silicon

Graphics, plaintiffs are required, at a minimum, to name, not simply identify by job title, the 15 HBOC employees and customers who cooperated with lead counsel's investigation. 126 F. Supp. 2d at 1254, 1270. The McKesson court, however, agreed with plaintiffs that the complaint's allegations based upon information and belief were sufficient under Silicon Graphics, noting:

> Nowhere, however, did the Silicon Graphics court require naming (as opposed to identification) of sources. It is possible to identify sources and provide other corroborating details without disclosing the names of sources.

Id. at 1271.

In In re Engineering Animation Securities Litigation, 110 F. Supp. 2d 1183 (S.D. Iowa 2000) the court was troubled by plaintiffs' failure to state who informed them of an alleged company-wide teleconference during which one of the defendants admitted the company was not going to meet projected sales or earnings. Id. at 1192. The Engineering Animation court ruled that since the source was not given, the particularity requirement was not met with regard to the factual allegation. Id.

The only Court of Appeals to address directly the issue of naming sources, however, rejected the defendants' argument. The Second Circuit Court of Appeals in Novak v. Kasaks, 216 F.3d 300 (2d Cir. 2000), focused on whether plaintiffs must name anonymous sources who cooperated with plaintiffs' counsel. According to the Novak district court, in order to meet the information and belief pleading requirement, the plaintiffs needed to identify such confidential sources. Novak v. Kasaks, 997 F. Supp. 425, 431-32 (S.D.N.Y. 1998). The Second Circuit rejected the district court's findings and concluded that "[t]he district court's reasoning and conclusions were flawed in several respects." 216 F.3d at 312.

> For one thing, the complaint provides specific facts concerning the Company's significant write-off of inventory directly following the Class Period, which tends to support the plaintiffs' contention that inventory was seriously overvalued at the time the purportedly misleading statements were made. Specifically, the plaintiffs allege that: (1) in AnnTaylor's May 1995 reporting of its first quarter fiscal 1995 results, the Company "admitted to analysts that its inventories were too high" and that "inventory liquidation" would follow; (2) in AnnTaylor's July 29, 1995 10-Q filed with the SEC, it "admitted that the decrease in the Company's gross profit percentage was attributable to 'increased cost of goods sold as a percentage of net sales, *primarily resulting from markdowns*'"; and (3) a January 22, 1996 Weekly Report showed that even six months after the Class Period, substantial amounts of "Box and Hold" inventory still dated from 1993 and 1994, which supports the inference that inventory during the Class Period was similarly dated. Thus, the complaint identifies with particularity several documentary sources that support the plaintiffs' belief that serious inventory problems existed during the Class Period itself.

Id. at 312-13 (emphasis in original).

The Second Circuit in Novak also stressed that "there is nothing in the caselaw of this circuit that requires plaintiffs to reveal confidential sources at the pleading stage." Id. at 313.

> In fact, the applicable provision of the law as ultimately enacted requires plaintiffs to plead only facts and makes no mention of the sources of these facts. See 15 U.S.C. § 78u-4(b)(1).
>
> More fundamentally, our reading of the PSLRA rejects any notion that confidential sources must be named as a general matter.

Id.

In addressing defendants' argument that district courts outside the Second Circuit, In re Silicon Graphics Inc. Securities Litigation, 970 F. Supp. 746, 763 (N.D. Cal. 1997) and In re Aetna Inc. Securities Litigation, No. CIV. A. MDL 1219, 1999 WL 354527, at *4 (E.D. Pa. May 26, 1999), have held or implied that the PSLRA generally requires plaintiffs to include the names of their confidential sources, the Second Circuit noted:

> this rule is based on a misreading of the legislative history of the PSLRA. Specifically, the court in Silicon Graphics relied primarily on the hyperbolic statements of legislators attempting (unsuccessfully) to amend the proposed Act to lighten plaintiffs' pleading burden. See Silicon Graphics, 970 F. Supp. at 763-64. In fact, the applicable provision of the law as ultimately enacted requires plaintiffs to plead only facts and makes no mention of the sources of these facts. See 15 U.S.C. § 78u-4(b)(1).

216 F.3d at 313.

The Second Circuit further noted that the purpose of paragraph (b)(1) of the PSLRA "can be served without requiring plaintiffs to name their confidential sources as long as they supply sufficient specific facts to support their allegations." Id. at 314.

The Second Circuit also validated a point frequently stressed by plaintiffs that "[i]mposing a general requirement of disclosure of confidential sources serves no legitimate pleading purpose while it could deter informants from providing critical information to investigators in meritorious cases or invite retaliation against them." Id.

The Second Circuit concluded:

> Accordingly, where plaintiffs rely on confidential personal sources but also on other facts, they need not name their sources as long as the latter facts provide an adequate basis for believing that the defendants' statements were false. Moreover, even if personal sources must be identified, there is no requirement that they be named, provided they are described in the complaint with sufficient particularity to support the probability that a person in the position occupied by the source would possess the information alleged. In both of these situations, the plaintiffs will have pleaded enough facts to support their belief, even though some arguably relevant facts have been left out.

Id.

The Theragenics court, "[a]fter extensively reviewing the Reform Act, its legislative history, and more than 50 cases, … agree[d] with the approach of the Second Circuit in its recent Novak decision." 105 F. Supp. 2d 1342, 1355. The Theragenics court recognized that in practice the PSLRA information and belief pleading requirement

"may be easily satisfied by references to internal memoranda or other documents, press releases, news articles and government-mandated filings."

The Theragenics court concluded:

> A plaintiff at this stage of the litigation, however, need not provide the names of either corporate whistle-blowers, customers of the defendant, or even outside consultants who provided factual support for the allegations, provided that there are other facts that provide an adequate basis for believing that the defendants' statements were false. If there are no other sources of information, it is enough that the plaintiff cite human sources without providing their names, provided that enough information is given to assure the Court that the plaintiff is not seeking to use discovery merely as a fishing expedition in the hope that something will turn up.
>
> The Court believes that this interpretation comports with both the legislative history of the Reform Act and the policies that underlie it. … This Court believes, however, that if Congress had intended basically to abolish notice pleading that underlies the Federal Rules of Civil Procedure and instead reintroduce the previously rejected concept of code pleading in such an important area of federal law, Congress would have stated so more explicitly.

Id.

In Fitzer v. Security Dynamics Technologies, Inc., 119 F. Supp. 2d 12 (D. Mass. 2000) plaintiff relied "on two types of sources of information as the source material for her allegations: (1) press releases issued by Security Dynamics, its filings with the SEC, news reports, analyst reports, and other publicly available documents; and (2) statements from former employees of Security Dynamics employed during the class period." Id. at 20 (footnote omitted). The former employees were all unnamed, and only a general job description was given. Id. at 21.

The Fitzer court considered the reliance on unnamed sources to pose "serious questions" such as: "Were such former employees in a position in the company to learn of the facts they claim to know? Are they credible or do they, as former employees, hold

a grudge against the company?" 119 F. Supp. 2d at 21. Recognizing that such questions ultimately go to the weight of the evidence, the Fitzer court noted that the unnamed inside sources indicate plaintiff pled particularized allegations based on more than mere "information and belief." Id. Thus, the Fitzer court, "inclined to agree with the Second Circuit," ruled that "although Fitzer does not provide the names of her sources, she satisfies the Second Circuit's analysis by providing a 'sufficient general description of the personal sources of plaintiffs' beliefs.'" Id. at 22.

V. DEFENDANTS' UNIQUE ARGUMENT AND THE COURT'S REACTION

The defendants in In re Fine Host Corporation Securities Litigation, 25 F. Supp. 2d 61 (D. Conn. 1998) raised the unique argument that the PSLRA information and belief provision "applies not only to allegations about the statements themselves, but also to allegations about defendants' state of mind." Id. at 70. The Fine Host court rejected defendants' argument and noted:

> This interpretation is flatly contradicted by the structure of the statute. The language quoted is contained only in subsection 78u-4(b)(1), which is entitled "Misleading statements and omissions." The following subsection, entitled "Required state of mind," is devoid of any such language. Therefore, it would be incorrect to construe the PSLRA as having imposed on plaintiffs the burden to plead scienter by stating with particularity all facts on which allegations of scienter made on information and belief were formed. Rather, as explicitly stated in the statute, in order to plead scienter adequately, a plaintiff need only "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." 15 U.S.C. § 78u-4(b)(2).

Id. at 70-71.

Thus, the Fine Host court concluded defendant's "argument that plaintiffs have failed to plead fraud with particularity because they have failed to attribute the source of the information upon which the allegations are based is also without merit." Id. at 70.

VI. CONCLUSION

The issues relating to what satisfies the PSLRA "information and belief" pleading requirements have not reached any foregone conclusions. Jurisdictions disagree over the various points raised by the parties. A few trends seem clear, however. First, plaintiffs may not be able to avoid pleading with particularity by asserting allegations based on "investigation of counsel." Second, plaintiffs are not required to identify by name the human sources that support plaintiffs' information and belief. Finally, the "information and belief" pleading requirements apply solely to the reasons why a statement is misleading and not to allegations concerning defendants' state of mind.

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