

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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IN RE WORLDCOM, INC. SECURITIES :
LITIGATION : MASTER FILE
 : 02 Civ. 3288 (DLC)
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This Document Relates to: : OPINION AND ORDER
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ALL ACTIONS :
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DENISE COTE, District Judge:

Defendants Salomon Smith Barney, Inc. ("SSB"), Citigroup, Inc. ("Citigroup"), and Jack Grubman ("Grubman") (collectively, the "SSB Group") have moved to sever three of the five claims against them in the Amended Consolidated Complaint filed on

October 11, 2002 ("Complaint") in this securities litigation ("Securities Litigation"). They request that the three claims be transferred to the Honorable Gerald E. Lynch of this district for consolidation with the many actions that have been brought against the SSB Group arising out of the recommendations made by SSB analysts to purchase nine telecommunications companies' stocks. For the following reasons, the motion is denied.

Background

The Complaint brings claims against certain former WorldCom executive officers, WorldCom's directors (and former directors), accountants, and eighteen underwriters ("Underwriter Defendants"), including SSB, as well as against Citigroup and Grubman. The claims in the Complaint arise from the alleged manipulation of the financial statements of WorldCom and the alleged false and misleading statements made to the investing public as a result of that manipulation.

The Complaint also alleges that an illegal quid pro quo relationship existed between the SSB Group and WorldCom in which SSB received investment banking business in return for agreeing to issue positive analyst reports about WorldCom, including false and misleading reports, to provide senior WorldCom executives with valuable IPO shares, and to loan WorldCom's Chief Executive Officer, Bernard J. Ebbers, several hundred million dollars. The Complaint contends that the registration statements issued in connection with certain of WorldCom's bond offerings were false and misleading in part because they failed to disclose conflicts

of interest that permeated the WorldCom/SSB relationship. Five counts in the Complaint state claims against members of the SSB Group.

Counts IV and V of the Complaint state claims against the Underwriter Defendants, including SSB, under Sections 11 and 12(a)(2) of the Securities Act of 1933, 15 U.S.C. §§ 77k and 77l(a)(2), for material misstatements in connection with the registration statements for, and sale of, public debt offerings by WorldCom. Among other claims, these Counts allege that the Underwriter Defendants failed to perform a reasonable investigation in connection with the public debt offerings and thus are liable for any material misrepresentations or omissions contained in the registration statements. In addition, Count IV alleges that SSB's conflicts of interest tainted its ability to handle certain public debt offerings as the lead underwriter, and that SSB and the other underwriters failed to disclose SSB's conflicts and to perform the requisite due diligence. SSB does not move to sever counts IV and V.

The claims that are the subject of this severance motion are Counts IX through XI. Count IX alleges a violation of Section 10(b) of the Securities Exchange Act of 1934 ("1934 Act"), 15 U.S.C. § 78(j) ("Section 10(b)"), against SSB and Grubman based in part on the same registration statements that are the subject of Counts IV and V. Among other claims, Count IX alleges that as part of their quid pro quo relationship, SSB, Grubman and WorldCom deceived investors and artificially inflated the price of WorldCom stock and debt. Count X alleges violations of

Section 10(b) by SSB and Grubman in connection with analyst reports regarding WorldCom. Among other things, Count X alleges that the analyst reports misrepresented or failed to disclose material facts regarding WorldCom and the nature of SSB's relationship with WorldCom. Count XI alleges violations of Section 20(a) of the 1934 Act, 15 U.S.C. § 78t, against Citigroup and SSB as control persons in connection with both the registration statements and the analyst reports.

The actions consolidated before Judge Lynch are referred to as the Analyst Actions. The Analyst Actions consist of over sixty actions that relate to SSB's analyst coverage of nine different telecommunications companies, including WorldCom, and that name as defendants two or more members of the SSB Group. Actions against SSB relating to its coverage of the telecommunications industry were filed in numerous venues, but the bulk of the analyst litigation against the SSB Group has been consolidated before Judge Lynch or is in the process of being consolidated before him. The common denominator in these Analyst Actions is the allegation that the recommendations of SSB's analysts to purchase these stocks lacked any reasonable factual basis, omitted material, neglected adverse information, and/or failed to disclose SSB's significant conflicts of interest arising from its effort to obtain investment banking business. The Analyst Actions do not name as defendants the telecommunications companies that were the subject of the analyst reports, their officers, directors, or auditors.

Prior to the transfer of the Analyst Actions to Judge Lynch, they had been before the Honorable Barbara S. Jones. On January 24, 2003, Judge Jones issued an order consolidating each of the actions according to the identity of the securities issuer. Thus, the analyst litigation against the SSB Group consists not of a single action, but of nine separately consolidated Analyst Actions. For example, the actions that relate to the recommendations to purchase WorldCom stock were consolidated into one action ("WorldCom Analyst Action").

The nine Analyst Actions are now proceeding before Judge Lynch. On March 20, 2003, Judge Lynch issued a case management order appointing lead plaintiffs for each of the nine consolidated Analyst Actions. The lead plaintiff in the Securities Litigation, New York State Common Retirement Fund, was appointed as lead plaintiff in the WorldCom Analyst Action. In addition to appointing lead plaintiff, the March 20 Order set schedules for the filing of consolidated complaints in each of the Analyst Actions. For the WorldCom Analyst Action, however, the Order provides that should this Court deny this severance motion, further proceedings in the WorldCom Analyst Action shall be stayed pending further order of the court.

Also before Judge Lynch is a securities action against various defendants associated with Global Crossing, In re Global Crossing, Ltd. Securities Litigation, No. 02 Civ. 910 (GEL) ("Global Crossing Securities"), an action that is similar to the Securities Litigation before this Court. Judge Lynch appointed as presumptive lead plaintiff for the Analyst Action concerning

Global Crossing the same plaintiff who had been appointed as lead plaintiff in Global Crossing Securities. Instead of allowing the plaintiffs to pursue Global Crossing-related claims against the SSB Group in both Global Crossing Securities and the Global Crossing Analyst Action, the March 20 Order ensures that such claims will continue in only one action. As with the WorldCom Analyst Action, the Order provides two alternatives for the Global Crossing Analyst Actions. The parties were directed to meet and confer and to advise the Court whether "plaintiff (a) agrees to stay proceedings in SSB Global Crossing [the Global Crossing Analyst Action] and to proceed with the claims against the Salomon Smith Barney defendants in the Global Crossing Securities matter; or (b) agrees to sever and dismiss the claims against those defendants in Global Crossing Securities and to proceed with those claims by filing a consolidated complaint" in the Global Crossing Analyst Action.

The Arguments

The SSB Group contends that the Court should exercise its discretion to sever Counts IX through XI and to transfer them to Judge Lynch to be consolidated with the WorldCom Analyst Action. The SSB Group argues that severing the claims is warranted because the inclusion of Counts IX through XI in the Complaint (1) is an effort to circumvent the division of business of this district court undertaken by the judges in this district and the Judicial Panel on Multidistrict Litigation ("MDL Panel"), (2) is an effort by the lead plaintiff before this Court to obtain

improperly appointment as the lead plaintiff in the WorldCom Analyst Action, and (3) will best serve the interest of judicial economy.

Plaintiff argues that the motion should be denied because the claims the SSB Group seeks to sever, and the underlying facts at issue with respect to each of those claims, are inextricably intertwined with the remainder of the Securities Litigation. Plaintiff contends that it is not barred from asserting Counts IX through XI in this action, and that judicial economy would best be served by retaining those counts in this action.

Discussion

Rule 21 of the Federal Rules of Civil Procedure provides that "any claim against a party may be severed and proceeded with separately." Fed. R. Civ. P. 21 ("Rule 21"). Rule 21, which addresses "misjoinder and non-joinder of parties," id., complements Rule 20, which sets forth the conditions for permissive joinder. Fed. R. Civ. P. 20(a). Rule 20 allows parties to be joined as defendants in a single action "if there is asserted against them jointly, severally, or in the alternative, any right to relief in respect of or arising out of the same transaction, occurrence, or series of transactions or occurrences and if any question of law or fact common to all defendants will arise in the action." Id. Rule 20 "permit[s] all logically related claims by or against different parties to be tried in a single proceeding." Epstein v. Kemper Ins. Co., 210 F. Supp. 2d 308, 320 (S.D.N.Y. 2002) (citation omitted).

District courts have broad discretion to determine whether or not to grant a motion to sever. Id.; cf. United States v. Zackson, 6 F.3d 911, 922 (2d Cir. 1993) (discretion standard in criminal case).

As discussed above, Counts IV and V, which are unchallenged by this motion, and Counts IX through XI, which the SSB Group seeks to sever, arise from the same series of transactions or occurrences: WorldCom's financial dealings and reporting, including alleged material misstatements which caused substantial losses to WorldCom's investors. Contrary to the SSB Group's contention, no clear line can be drawn between the allegations concerning the SSB Group's analyst reports and SSB's role as an underwriter -- in fact, the lead underwriter for at least two major WorldCom bond offerings. Instead, the Complaint alleges that the conflicts of interest that arose because SSB occupied these dual roles tainted WorldCom's actions, the underwriters' due diligence, and SSB's ability to handle certain debt offerings. It is simply inaccurate to classify, as the SSB Group does, the "center of gravity" for Counts IV and V as being the "financial" issues and for Counts IX through XI as being the "analyst" issues. Financial reporting and analyst issues permeate all five counts. In the event that Counts IV and V survive the motion to dismiss that has been filed by SSB, the litigation of this action will include the alleged conflict of interest and quid pro quo relationship that the registration statements and analyst reports failed to disclose. That means that even if Counts IX through XI were severed, the accuracy of

the analyst reports and registration statements and the circumstances surrounding their creation and promulgation, including SSB's role as lead underwriter, would remain an essential part of this litigation.

The SSB Group's argument that retaining Counts IX through XI in the Complaint is an impermissible circumvention of the division of business within this district is not persuasive. The MDL panel and this district have taken steps to centralize, coordinate, and efficiently proceed with actions arising from the collapse of WorldCom and the allegations of widespread misrepresentation in SSB's analysis of the telecommunications industry as a whole. Given the complex chains of connection between WorldCom, the WorldCom defendants in the Securities Litigation and the SSB Group, however, it is not surprising that overlap should occur between this action and the Analyst Actions. That overlap is due to the fact that the allegations regarding the SSB Group's analyst reports and those regarding its underwriting arise from the same set of alleged facts, not to an impermissible effort to bypass the MDL panel's decisions.

The MDL panel and the judges of this Court who have previously made decisions about the assignment of cases did so by applying their best judgment to the record before them. This Court must now do the same. On the record before this Court,¹

¹ Since the MDL panel issued its order, plaintiffs' counsel has been appointed in this action, and motions briefed and opinions issued addressing discovery, stays of the litigation regarding certain individual defendants, and remand or consolidation of certain actions. Motions to dismiss are now fully briefed as well. This history is set forth in greater

Counts IX through XI of the Complaint arise from the same alleged series of transactions or occurrences as the remainder of the Complaint and should not be severed.

The SSB Group's argument that inclusion of Counts IX through XI is an improper attempt by NYSCRF to secure appointment as lead plaintiff for the WorldCom actions before Judge Lynch can be swiftly rejected. For the reasons discussed above, in terms of a joinder analysis, pleading Counts IX through XI was appropriate, since they arise from and rely on the same set of transactions and occurrences that are at issue in the remainder of the Complaint. This inclusion provides no basis to find any improper motive. Moreover, as the recent argument before Judge Lynch illuminates, NYSCRF never has had any serious competition for lead plaintiff in the WorldCom Analyst Action, and was in fact appointed as such on March 20.

The final issue raised by the SSB Group is the important consideration of judicial efficiency. Judicial efficiency, however, counsels strongly against severing Counts IX through XI. Counts IX through XI arise from the relationships and dealings between WorldCom and the SSB Group that are at issue in the remainder of the Complaint. As already noted, if Counts IV and V survive the motions to dismiss, the propriety of SSB's actions as an underwriter and as lead underwriter, and the nature and extent of the quid pro quo relationship between the SSB Group and

detail in In re WorldCom, Inc. Securities Litigation, No. 02 Civ. 3288 (DLC), 2003 WL 716243 (S.D.N.Y. March 3, 2003), and familiarity with that opinion, and with all other opinions issued in the Securities Litigation is presumed.

WorldCom executives, if any, will be at issue in this action with or without Counts IX through XI. Although the SSB Group may prefer to have all claims related to SSB's analysis of the telecommunications industry consolidated before one judge, it will not achieve that even if Counts IX through XI are severed. In addition, it has failed to identify any prejudice it will suffer if Counts IX through XI remain in this action. Retaining Counts IX through XI in this action will help insure efficiency and fairness in motion practice, discovery and in the pre-trial handling of the litigation as a whole. If, at the time of trial, the SSB Group is still actively litigating this case, and believes that the WorldCom trial should be consolidated with the trial on claims related to one or more other issuers, it may bring a motion seeking such relief at that time.

The management of discovery illustrates the efficiencies to be gained by following the traditional organization of litigation, that is, by consolidating litigation by the identity of the issuer. While there may be some discovery of the SSB Group that will be common to the nine issuers involved in the SSB Analyst Actions, the overwhelming bulk of the discovery in each SSB Analyst Action will be specific to the issuer at the center of that action. Thus, while certain internal policies and practices of the SSB Group may have created or supported an environment that led to alleged wrongdoing in the case of more than one issuer, the liability of the SSB Group for both its WorldCom underwriting and its WorldCom analyst reports will rest principally on an investigation of the accuracy of the financial

reporting by WorldCom, SSB's knowledge about the accuracy of WorldCom's financials, SSB's reports about WorldCom, SSB's efforts to obtain the underwriting business from WorldCom, and any quid pro quo arrangements between the SSB Group and WorldCom or its principals.

At least at the pretrial stage, therefore, severance of Counts IX through XI would create, not eliminate, inefficiency. The SSB Group simply has not explained why it makes sense to sever some, but not all, of the claims against it.

One final word about efficiency is in order. The SSB Group is facing a significant number of lawsuits. Where possible, it is in the interest of all parties and the court system to avoid unnecessary duplication of effort. The SSB Group is represented by able counsel who will be in a position to suggest to the various courts before whom it is appearing economies that may be achieved without delaying or impeding a just resolution of the litigation. Such suggestions from all parties to the Securities Litigation and consultation and coordination with the other courts presiding over related litigation will continue to aid this Court as it strives to ensure that the Securities Litigation proceeds efficiently and fairly.

Conclusion

For the reasons stated above, the motion to sever Counts IX through XI of the Complaint is denied.

SO ORDERED:

Dated: New York, New York
March 24, 2003

DENISE COTE
United States District Judge