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Trend in Southern District of New York to Disclose Identity of Confidential Witnesses in Securities Class Action Complaints

Three recent decisions from the Southern District of New York mark a trend toward requiring plaintiffs in securities cases to identity any "confidential witnesses" cited in a complaint. While the case law had been mixed, these recent decisions will make it more difficult for plaintiffs to evade this discovery obligation.

Confidential witnesses, also referred to as confidential informants, are typically former employees of a defendant company. Securities plaintiffs – who must adequately allege scienter in order to survive a motion to dismiss, but must do so without the benefit of discovery from defendants – often contact and interview ex-employees in search of useful information or, ideally, direct quotes to bolster the allegations in the complaint. Courts in the Second Circuit and elsewhere have held that plaintiffs need not name such sources in the complaint to satisfy their pleading burden. Thus, in recent years, as pleading standards have ratcheted up, so too has plaintiffs' reliance on these confidential witnesses.

If plaintiffs survive the motion to dismiss, defense counsel will seek to discover the identities of confidential witnesses, both to investigate the substantive allegations in the complaint and to assess whether plaintiffs have misquoted or exaggerated confidential witness statements in trying to clear the motion to dismiss hurdle. Such misuse of confidential sources is all-too common and, indeed, the case law records numerous incidents in which confidential witnesses recanted, disavowed, or disagreed with statements attributed to them in the complaint.[1] In perhaps the most dramatic example, a federal district court in Illinois dismissed a securities class action on a motion for reconsideration in part because it was discovered that plaintiffs' counsel never met with a key witness cited in the complaint and "never verified the hearsay reports of their investigators."[2]

Plaintiff's counsel, for their part, typically resist such discovery. Plaintiffs argue that identification of the confidential witnesses would reveal work product because it would provide insight on which witnesses plaintiff's counsel considered important, and how plaintiff's counsel evaluated information during an investigation. Further, plaintiffs maintain, so long as they do not intend to call the confidential witnesses at trial--and, when pressed, plaintiffs often concede this point--defendants cannot show a substantial need for the information that would allow them to overcome the work product protection. Plaintiffs also typically claim that the

[1] *See, e.g., In re Bankatlantic Bancorp., Inc. Sec. Litig.*, No. 07-61542-CIV, slip op. at 15-16, 22-24 (S.D. Fla. Aug. 3, 2011).

[2] *City of Livonia Emp. Ret. Sys.* v. *Boeing Co.*, No. 09 CV 7143, slip op. at 4 (N.D. Ill. Mar. 7, 2011).

witnesses might face retaliation if their identities were disclosed, or that disclosing their identities would deter future witnesses from coming forward.

Procedurally, the issue typically arises in connection with Rule 26 initial disclosures, which require plaintiffs to supply the names of any individuals with discoverable information.[3] Plaintiffs will supply a list with possibly hundreds of names, including the names of the confidential witnesses, but will refuse to identify which of the listed individuals were the confidential witnesses cited in the complaint. Educated guesswork on the part of defendants may not be enough to winnow the list--particularly when the disclosure contains hundreds of names--while deposing everyone on the list would be impractical and unduly expensive. Defendants must therefore move to compel.

Courts have ruled both for and against requiring specific identification of confidential witnesses.[4] As recently as February 2011, a federal district court in New York agreed that confidential witness identities are protected work product.[5] "While the identities of witnesses with relevant information are discoverable," the Court wrote, "Defendants are not automatically entitled to know which of those witnesses Plaintiffs consider important."[6] The case law, however, is now turning decidedly in favor of requiring plaintiffs to disclose the identities of confidential witnesses.

First, in *Plumbers and Pipefitters Local Union No. 630 Pension-Annuity Trust Fund* v. *Arbitron, Inc.*, No. 08 Civ. 4063 (PAE), 2011 WL 5519840 (S.D.N.Y. Nov. 14, 2011) ("*Arbitron*"), Judge Paul Engelmayer granted a defendant's motion to compel confidential witness identities. Judge Engelmayer expressed skepticism about plaintiff's claim of work product,[7] and held that the work product protection could not stand where the plaintiffs had used confidential witnesses statements offensively in the complaint: "In the Court's view, where a party has attempted to satisfy the pleading requirements of the [Private Securities Litigation Reform Act] by showcasing statements from a limited number of confidential witnesses, it may not thereafter refuse to disclose who they are on grounds of work product."[8] Confidential witness statements, in other words, cannot be used as both sword and shield.

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[3] *See* Fed. R. Civ. P. 26(a)(1)(A). The issue may also arise in response to specific discovery requests from defendants. *See* Fed. R. Civ. P. 26(b)(1).

[4] *See generally In re Marsh & McLennan Cos., Inc. Sec. Litig.*, MDL 1744, slip op. at 3 (S.D.N.Y. July 30, 2008) (comparing cases and noting that "[t]here is no binding authority on the question of whether the identities of the C[onfidential] W[itnesse]s in a securities class action are discoverable." (quoting *Miller* v. *Ventro Corp.*, 01 Cv. 1287 (SBA) (EDL), slip op. at 1 (N.D. Cal. Apr. 21, 2004)).

[5] *See, e.g., In re SLM Corp. Sec. Litig.*, No. 08-CV-1029 (S.D.N.Y. Feb. 15, 2011).

[6] *Id*. Slip op. at 1.

[7] Judge Engelmayer wrote: "It is difficult to see how syncing up the 11 [confidential witnesses] with these already disclosed names would reveal Plaintiff's counsel's mental impressions, opinions, or trial strategy." Slip op. at 9.

[8] Slip op. at 10 (quoting *Ross* v. *Abercrombie & Fitch Co.*, No. 05-CV-0819, slip op. at 3 (S.D. Ohio Mar. 24, 2008)).

In recent weeks, two other decisions from the Southern District of New York have followed *Arbitron*'s lead. First, in *In re Bear Stearns Companies, Inc. Securities, Derivative, and ERISA Litigation*, 1:08 MDL No. 1963 (RWS), 2012 WL 259326 (S.D.N.Y. Jan. 27, 2012) ("*Bear Stearns*"), Judge Robert Sweet granted a motion to compel the identity of seven confidential witnesses who were quoted in a complaint regarding the collapse of Bear Stearns.[9] Notwithstanding Lead Plaintiff's statement that it would not call the seven confidential witnesses at trial, Judge Sweet held that, "based upon this District's most recent jurisprudence and the circumstances presented here, the work product doctrine cannot be employed to protect the identities of [Lead Plaintiff's] confidential witnesses."[10]

Most recently, in *In re American International Group, Inc. 2008 Securities Litigation*, No. 08 Civ. 4772 (LTS) (DF) (S.D.N.Y., Mar. 6, 2012), Magistrate Judge Debra Freeman ordered plaintiffs to disclose the names of three confidential witnesses whose statements about AIG's financial products were cited by the Court in denying the defendants' motion to dismiss. Magistrate Judge Freeman cited *Arbitron* and *Bear Stearns*, and wrote that even if some minimal work product protection attached to the confidential witness identities, "the difficulty Defendants would face in trying to ascertain the identity of these witnesses from otherwise available information is a burden that overcomes Plaintiffs' need for protection."[11]

The Second Circuit has yet to address the identification of confidential witnesses, so the issue remains open. But defendants now have a formidable body of case law from which to argue that the identification of confidential witness should be required, and there is no mistaking the trend in favor of that view.

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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[9] The Bear Stearns Companies Inc. was represented by Paul, Weiss, Rifkind, Wharton & Garrison LLP.

[10] Slip op. at 9.

[11] Slip op. at 7.

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