LEAD PLAINTIFF PRIMER

An overview of U.S. federal securities laws, class action procedure, and the role of lead plaintiff in securities class action litigation pursuant to the Private Securities Litigation Reform Act of 1995.
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2 Introduction

The role of lead plaintiff is vital in United States (U.S.) securities class action litigation. A lead plaintiff is a class representative vested with significant privileges and responsibilities to recover damages for itself and similarly situated investors. While the goal is simple, achieving it can be complex. This primer is intended to simplify some of the complexity by providing an overview of: (i) the U.S. federal securities laws; (ii) class action litigation procedure; and (iii) the role of lead plaintiff in this type of lawsuit.

3 Creation of Federal Securities Laws

In the early 1900s, the U.S. stock market was largely unregulated. In 1929, the U.S. experienced an unprecedented stock market crash followed by a severe economic depression. Many investors lost everything with no means of recovery. Lawmakers responded by creating federal laws governing the offering and trading of securities. Those laws would become known as the Securities Act of 1933 (Securities Act) and the Securities Exchange Act of 1934 (Securities Act). In the following decades, courts defined how these laws would be interpreted and applied.

Years later, U.S. federal securities laws were significantly reformed by legislation called the Private Securities Litigation Reform Act of 1995 (PSLRA). Changes included creating a more structured process for lead plaintiffs participating in securities class action litigation. The PSLRA, and court rulings that interpret and apply it, governs the modern process for how most federal securities class actions are litigated.

3.1 Securities Act

The Securities Act established that securities offered to the public must be registered with the U.S. Securities and Exchange Commission (SEC). Registration materials must provide truthful and accurate information about an issuer’s corporate governance, finances, and operations. The law recognizes that investors rely on material information to make informed investments decisions. Accordingly, deceit, misrepresentations, and other fraud in the offering of securities are prohibited. If such wrongdoing occurs, the Securities Act permits investors to file lawsuits against the issuers and related parties who violated the law.
3.2 Exchange Act
While the Securities Act regulates new offerings, the Exchange Act regulates securities after they have been offered. Issuers and other persons in the secondary securities markets are likewise regulated under the Exchange Act. The Exchange Act details disclosure requirements for periodic financial statements (such as quarterly and annual financial reports) and other corporate actions that must be filed with the SEC. Material information must be promptly and truthfully reported. Accordingly, false and misleading statements, or the omission of material information, is prohibited. The Exchange Act also prohibits illicit insider trading. Importantly, the Exchange Act permits investors to file lawsuits against wrongdoers who have violated these provisions.

The Exchange Act and Securities Act have provisions that provide for joint and several liability for persons who aid or control securities law violators. This means if an employee violates securities laws, the employer (e.g., an issuer) could be held liable. Similarly, if an individual encourages another to violate securities laws, the individual could be held liable. For these reasons, securities class actions often name the corporation as well as senior officers as defendants.

3.3 PSLRA
The PSLRA made substantive changes to the federal securities laws. Amendments included changes to standards for pleadings, discovery, liability, class representation and compensation. A major effect of the changes was an increased burden on plaintiffs to obtain evidence of wrongdoing before filing a lawsuit and without the benefit of pretrial discovery. The PSLRA also created rules for selecting the most appropriate plaintiff to serve as a class representative and gave courts greater discretion to scrutinize attorneys handling of the lawsuit. Lead plaintiff responsibilities and procedure are discussed in detail further below.

Note 1: Private versus Government Enforcement
Investors and the SEC have very different rights and powers under federal securities laws. But both may bring lawsuits for certain violations of securities laws. Private rights of actions brought by investors can be complementary to or overlap with SEC enforcement actions. Investor actions can also be critical for enforcing matters that the SEC lacks resources for, delays in prosecuting, or overlooks.
4 Class Action Litigation Benefits

Lawsuits claiming violations of federal securities laws are often litigated as a class action. A class action is a type of lawsuit allowing a similarly situated group (class) to be represented collectively by a member of that group (lead plaintiff). Investors can use a class action to effectively litigate against violators of federal securities laws. A class action allows for investors to receive recoveries for claims that might, individually, be too costly to litigate. A class action can empower investors by creating greater liability for defendants. Such litigation can force defendants to take seriously the claims and work to expeditiously resolve the matter.

A class action is usually a more efficient alternative for courts and defendants who would otherwise have to manage thousands of separate lawsuits over the same issue. A class action can reduce court congestion by limiting unnecessary court filings and dockets. Reducing the number of cases can allow judges to focus more on the merits of an action. A class action also binds absent class members, which can provide finality for defendants who may not desire to repeatedly litigate the same issue.

<table>
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<tr>
<th>Potential Plaintiff Benefits</th>
<th>Potential Court Benefits</th>
<th>Potential Defendant Benefits</th>
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<tr>
<td>• Strength in numbers</td>
<td>• Reduce docket congestion</td>
<td>• Easier to manage</td>
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<tr>
<td>• Less costly to litigate</td>
<td>• Easier to manage</td>
<td>• Finality</td>
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<td></td>
<td>• More time to focus on merits</td>
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5 Lead Plaintiff Benefits and Considerations

A lead plaintiff has many responsibilities and privileges. A lead plaintiff is a representative of the proposed class of injured investors and oversees the lawsuit on their behalf. A lead plaintiff moves the case forward through its chosen attorneys (lead counsel). A lead plaintiff selects lead counsel, oversees the litigation, and must agree to any settlement offer on behalf of the class. As a representative plaintiff, a lead plaintiff must cooperate in a way that serves the best interest of the class. A lead plaintiff should expect to participate in discovery, including gathering information related to its claims and being deposed. A lead plaintiff may also need or want to attend hearings, trials, and other court proceedings.

A lead plaintiff may be entitled to an incentive award for any costs and expenses dedicated to the successful resolution of a securities class action. An incentive award is usually requested when a settlement is submitted to the court for approval. An incentive award is separate compensation from any recovery a lead plaintiff would receive as part of the class.

5.1 Lead Plaintiff Groups

The PSLRA permits one movant or a group of movants to serve as lead plaintiff. Size and cohesiveness are two factors courts often scrutinize when considering the appropriateness of a lead plaintiff group. Moving as a group can be advantageous when it increases a lead plaintiff’s abilities and resources.

5.2 Significance of Institutional Investors

Both individual and institutional investors can serve as lead plaintiff. Historically, individuals have participated at a greater rate than institutional investors. Although, when drafting the PSLRA, lawmakers identified institutional investors as ideal class representatives and entrusted that enactment of the legislation would encourage their participation as lead plaintiff. Legislators believed that increasing the role of institutional investors in class actions would ultimately benefit shareholders and assist courts by improving the quality of representation in securities class actions. A limited number of empirical studies suggest institutional investor leadership in securities class actions can result in lower dismissal rates and higher settlement values for resolved cases. Regardless, time has shown the value of both individual and institutional participation.
6 Securities Class Action Procedure

The selection of lead plaintiff is one of several critical events for a class action filed pursuant to the PSLRA. In fact, federal securities class action litigation can be viewed as having nine progressive phases: (1) case assessment; (2) initial complaint and notice; (3) lead plaintiff motion; (4) additional pleadings and overcoming the motion to dismiss; (5) discovery; (6) class certification; (7) mediation; (8) overcoming summary judgment; and (9) settlement or trial. Accordingly, each phase has important considerations and responsibilities for a lead plaintiff and its counsel.

6.1 Case Assessment

The assessment of whether securities litigation is merited typically occurs weeks or months before the filing of a securities class action complaint. A securities class action often originates from an investigation of a company after a corrective disclosure has occurred. A corrective disclosure is a specific public announcement or event uncovering a past false statement, misrepresentation, or omission. A surprise announcement of a restatement of earnings is a classic corrective disclosure, but any number of issues could be a triggering event. The negative news must also cause a decline in the price of a related security for it to be a true corrective disclosure. At that time, the matter may be analyzed by attorneys for the scope of the wrongdoing and affected class of investors. An investigation may lead to the drafting of an initial class action complaint on behalf of a certain group of investors during a specific time period. Many investors hire law firms to actively monitor the markets for such events. Such law firms might then alert its clients when they have suffered a fraud-related loss.
6.2 Initial Complaint and Class Notice

The initial securities class action complaint is filed by the first plaintiff to propose a class action on behalf of injured investors. A typical initial complaint includes the major allegations against the defendants but may lack detailed background information and other specifics. A more comprehensive complaint, usually called an amended complaint, is usually later filed by the lead plaintiff after it has been appointed.

Notice of the proposed class action must be published by the plaintiff in a widely-circulated business periodical within 20 days after the initial complaint is filed. A common practice is for a plaintiff’s counsel to publish the notice concurrently with the filing the initial complaint. If more than one plaintiff files a complaint during this period, only the plaintiff of the first filed action is required to file a notice. Moreover, a court can later consolidate all related actions into one action if multiple complaints are filed.

The notice contains a summary of the claims asserted in the complaint, a description of the class of impacted investors, and an explanation of how interested investors can participate in the action. Under the PSLRA, the initial plaintiff and all other similarly harmed investors have the same opportunity to make a motion for appointment as lead plaintiff.

Example class action notice excerpt

USMA LAW GROUP ANNOUNCES FILING OF SECURITIES CLASS ACITON LAWSUIT AGAINST ABC CORP.

WASHINGTON, DC, June 01, 2018 (NEWSWIRE) -- U.S Market Advisors Law Group PLLC announces the filing of a class action lawsuit on behalf of purchasers of ABC Corporation (“ABC”) securities from January 1, 2018 through May 30, 2018, inclusive (the “Class Period”). The lawsuit seeks to recover damages for ABC investors under the federal securities laws. If you wish to serve as lead plaintiff, you must move the Court no later than July 31, 2018....
6.3 Lead Plaintiff Motion

The PSLRA provides that any investor seeking appointment as lead plaintiff must make a motion within 60 days of the proposed class action notice publication. If multiple motions are made, movants typically file subsequent briefs in support of their motion and/or in opposition to competing motions.

It is not uncommon for courts to appoint a lead plaintiff based on the motion briefing documents. But a court may schedule a hearing on the appointment of lead plaintiff allowing the movants’ counsels to argue why their respective clients should be appointed. In any event, a court should appoint a lead plaintiff generally within 90 days of the proposed class action notice publication.

6.3.1 Lead Plaintiff Criteria

The lead plaintiff motion process can be competitive. When multiple investors are seeking appointment as lead plaintiff, they must not only meet the PSLRA’s standards, but show how they are the best choice among the competing applicants.

The PSLRA establishes a rebuttable presumption that the movant or movant group with the largest financial interest shall be the lead plaintiff. The presumptive lead plaintiff must have also timely filed a motion and be otherwise sufficient to represent the putative class. The presumption may only be rebutted upon proof by a member of the purported class that the presumptive plaintiff will not fairly and adequately represent the class or has unique defenses making it incapable of adequately representing the class. Following is more detailed information on financial interest and other requirements of the lead plaintiff.
6.3.1.1 Financial Interest

The PSLRA does not define how a proposed lead plaintiff’s financial interest should be measured. But courts tend to measure financial interest by the approximate losses suffered by the movant. Other financial interest considerations might include: (1) the total number of shares purchased by the movant during the relevant period; (2) the number of net shares purchased by the movant during the relevant period; and (3) the net funds expended by the movant during the relevant period. Once the movant with the largest financial interest has been determined, that movant is the presumed lead plaintiff. But it cannot be appointed lead plaintiff until it is also found to be typical and adequate to represent the proposed class.
6.3.1.1 Losses
Because financial interest is such an important issue, a proposed lead plaintiff should be keenly aware of its losses. Most actions are filed on behalf of purchasers of a security who suffered losses after a securities fraud was disclosed. But securities class actions can be filed on behalf of purchasers or sellers of a security. For investors purchasing the relevant security during the class period, losses are generally calculated by taking the difference between the purchase price and the 90-day average price after the end of the class period. If a purchaser sold shares during the class period, those sales are matched against any pre-class period holdings or class period purchases. In that regard, losses are typically calculated using a first-in-first-out or a last-in-first-out (“LIFO”) accounting method. LIFO has grown as the preferred method in many jurisdictions.

<table>
<thead>
<tr>
<th>Example transactional data used in a loss calculation</th>
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<tbody>
<tr>
<td>Class Period: 01/1/17 - 01/31/17</td>
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<tr>
<td>Shares Held Before Class Period Start: 5</td>
</tr>
<tr>
<td>Class Period Purchases:</td>
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<td>01/06/17</td>
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<td>01/20/17</td>
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<td>Class Period Sales:</td>
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<tr>
<td>Date</td>
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<tr>
<td>01/05/17</td>
</tr>
<tr>
<td>01/10/17</td>
</tr>
<tr>
<td>90-day Avg. Stock Price After Class Period End: 05/01/17</td>
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</table>

6.3.1.2 Typicality
The lead plaintiff movant possessing the largest financial interest must be typical to represent the proposed class. Typicality can be evidenced by showing a movant’s claim arises from the same course of events impacting other members of the class. A movant might evidence typicality by showing it purchased the relevant securities during the relevant time period, and that this investment has suffered damages similar to other class members.

6.3.1.3 Adequacy
The lead plaintiff movant with the largest financial interest must be adequate to represent the proposed class. Adequacy can be evidenced by the absence of any hindrances that would keep a movant from fairly protecting the interests of the class. Adequate representation will be found if the movant has the ability and incentive to vigorously represent the class’ claims, with no fundamental conflicts of interest with the interests of the class. A movant’s retention of competent and experienced counsel is a factor that can be used to support adequacy.
6.4 Additional Pleadings

Generally, when a plaintiff files a complaint, defendants have a limited number of days to respond (answer) to it. But for federal securities class actions, courts generally stay (pause) the complaint and answer (pleadings) period until after a lead plaintiff is appointed. After such time, the parties typically ask the court to approve a new pleading schedule for filing an amended complaint and responsive briefs.

6.4.1 Amended Complaint

Depending on the court approved briefing schedule, the lead plaintiff often has between 30 and 60 days after the appointment of lead plaintiff to file an amended complaint. During this time, the lead plaintiff’s counsel will take what it has been learned from its investigation to file a comprehensive complaint (as compared to the initial complaint). And if allowed by the court, additional amendments to the comprehensive complaint might be made as the case progresses.

6.4.2 Motion to Dismiss

A lead plaintiff should expect that a defendant will make a motion for the court to dismiss the amended complaint. The motion to dismiss and other responsive briefs will follow the lead plaintiff’s filing of an amended complaint. The securities class action moves forward when the motion to dismiss is denied.

6.5 Discovery

Upon the denial of a defendant’s motion to dismiss, the PSLRA’s mandated stay on discovery will be lifted. The parties will begin negotiating the exchange of documents and other responsive information that will be used to help support their respective positions. A lead plaintiff is responsible for producing relevant documents and may be deposed. A lead plaintiff is often questioned about its organizational structure (if any) and how or why it made the relevant investment. Accordingly, a lead plaintiff is likely to be asked for documents and other information supporting its answers, to the extent they exist. Competent counsel will aid, defend, and guide a lead plaintiff through discovery to make the process as easy as possible.

**Note 2: Litigation Hold**

The lead plaintiff should safeguard any documents related to the action in order to build the strongest possible case against the defendant. Accordingly, counsel for the lead plaintiff should aid and advise it to take affirmative steps to preserve relevant documents. This means that relevant documents that might be destroyed in the normal course of business should be preserved until otherwise advised by counsel. Some of the preserved documents may be provided to the defendants as part of discovery. Some documents may not be provided. Competent counsel will work zealously to protect privacy and prevent undue burdens.
6.6 Class Certification

After a defendant’s motion to dismiss has been denied by the court, a lead plaintiff will often make a motion to officially certify the class. The class certification motion includes a brief detailing why the action is appropriately litigated as a class and how the lead plaintiff is an appropriate class representative.

Federal rules require that the claims of a lead plaintiff and other class representatives meet four criteria: (1) the class is so numerous that it is impracticable for each class member to separately litigate the same issues (numerosity); (2) there are questions of law or fact common to the class (commonality); (3) the claims or defenses of the class representatives are typical of those of the class (typicality); and (4) the class representatives will fairly and adequately protect the interests of the class (adequacy). Like the amended complaint, a defendant will typically oppose the motion for class certification. An action can proceed towards trial after class certification has been granted.

6.7 Mediation

The relevant parties may mediate a class action in an effort to prevent the costs and risks associated with trial. Mediation is a method to settle the action without a trial by using a neutral third party to aid them in the resolving the parties’ disagreement. Mediation allows each party to gain insight on the other party’s strengths and weaknesses of their claims and defenses. The mediator is often a former judge experienced in presiding over securities actions.

Mediation is a common, if not mandated, practice in most court jurisdictions. Mediation can occur at any time during the litigation, but commonly take places after class certification and before trial. The opportunity for meaningful mediation tends to increase as the action gets closer to a trial date. At this stage, the parties are more knowledgeable of the risks involved with allowing a judge or jury determine the outcome.
6.8 Summary Judgment

After the parties have a sufficient understanding of the other parties’ legal theories and strengths and weaknesses, a defendant will likely file a motion for summary judgment. The motion for summary judgment is effectively a request that the court dismiss the action. It is a claim that there is no dispute as to the *material facts* of the action. Therefore, no trier of fact (judge or jury) is needed. The case can be resolved simply using the what the law states without the need for a trial. A motion for summary judgment can be made at almost any time during the litigation, but is often withheld until close to a trial date.

6.9 Settlement or Trial

Settlement or trial are two very different ways of resolving a securities class action. The overwhelming majority of actions that resolve favorably for plaintiffs end in settlement. Less than one percent of securities actions filed since the enactment of the PSLRA have gone to trial. The risks and costs associated with trial often make settlement a much more attractive option for all parties.

The lead plaintiff has great power in the settlement process. Specifically, it must give authority before a case can settle. When all parties have agreed on the terms of resolution, the settlement agreement will be submitted for court approval. The court will then scrutinize the agreement to ensure it is fair, particularly to class members. A settlement agreement will typically include: (1) a summary of the claims alleged/denied; (2) reasons for settling; (2) procedural history; (3) important terms such as the amount of the settlement fund and the definition of the class eligible to file a claim; (4) any exclusions and releases of liability; and (5) the proposed claims administration process for distributing the settlement fund.

A trial is a formal examination of evidence before a judge or jury to decide if wrongdoing occurred. A trial is a final resolution to the litigation (although it is possible for a party to appeal the ruling to a higher court). In the rare instance that a case goes to trial, it is possible the lead plaintiff or a lead plaintiff representative will be asked to provide testimony.

Even though trials are rare, competent counsel should litigate a class action as if it were going to trial. This can have the effect of providing the most zealous representation for the lead plaintiff and class.

*Less than one percent of securities actions filed since the enactment of the PSLRA have gone to trial.*
7 Glossary

Below are common terms used in securities litigation pursuant to the PSLRA. Term definitions are only intended to be general explanations.

**Adequacy.** The state of a plaintiff or movant meeting the requirement of being legally able to serve as a lead plaintiff or class representative.

**Answer.** A defense in writing, made by a defendant, to the allegations contained in a complaint filed by the plaintiff.

**Appointment.** The designation by a court to serve as a lead plaintiff or class representative.

**Artificial inflation.** An increase in the price of the security caused by, then unknown to the market, false or misleading statements.

**Class Certification.** Upon the motion of the lead plaintiff, a court’s certification that an action has met the criteria of proceeding as a class action.

**Class representative.** A plaintiff or movant representing the interests of all class members who have been affected by the conduct challenged in a lawsuit.

**Complaint.** A pleading on the part of the plaintiff in a securities class action that details the allegations against the defendant and its claims for relief.

**Control-person liability.** Any person who directly or indirectly controls another person found liable for a violation of the Securities Exchange Act or any regulation thereunder is jointly and severally liable, to the same extent as the controlled person, to any person to whom the controlled person is liable.

**Corrective disclosure.** A specific public announcement or event that reveals a past false statement, misrepresentation, or omission and causes a decline in value of a related security.

**Consolidation.** The act of uniting several similar actions into one action by order of a court.

**Deposition.** An out-of-court testimony of a witness intended to be used at trial.

**Discovery.** A pre-trial procedure in which each party can obtain evidence from the other party or parties by means of devices such as a request for answers to interrogatories, request for production of documents, request for admissions and depositions. Discovery can also be obtained from non-parties using subpoenas.
**EDGAR.** The Electronic Data Gathering, Analysis, and Retrieval system. EDGAR performs automated collection, validation, indexing, acceptance, and forwarding of submissions by companies and others who are required by law to file forms with the U.S. Securities and Exchange Commission.

**Federal.** Relating to the jurisdiction of the central government of the US (not state jurisdiction).

**Financial Interest.** A plaintiff’s or movant’s economic reason for participating in a securities class action. Dollar losses suffered is a popular measure of financial interest.

**Fraud.** A deceitful practice or willful device intended to deprive the right of another, or in some manner cause an injury.

**Interrogatories.** A series of formal written questions served on a party or witness to obtain evidence during discovery.

**Issuer.** A legal entity that develops, registers, and sells securities to finance its operations. Issuers may be corporations, investment trusts, or domestic or foreign governments.

**Joint and Several Liability.** When two or more parties are each independently liable for the full extent of the injuries stemming from a fraudulent act.

**Lead Counsel.** An attorney or law firm selected by a lead plaintiff and approved by a court charged with the responsibility of litigating an action.

**Lead Plaintiff.** A movant or plaintiff appointed by a court as a representative of the members of a class. A lead plaintiff is responsible for overseeing counsel and the lawsuit in general.

**Litigation Hold.** A written directive to preserve potentially relevant documents and information in anticipation of litigation.

**Mediation.** An out-of-court proceeding overseen by a neutral facilitator with the goal of finding an appropriate settlement of the dispute.

**Movant.** A party making a motion, such as a motion for appointment as lead plaintiff.

**Notice.** A required publication to make potential class members aware of a proposed action affecting their rights, obligations or duties.

**Plaintiff Certification.** A sworn declaration affirming a plaintiff meets the criteria to for serving as a lead plaintiff or class representative.

**Pleadings.** A plaintiff’s complaint (or amended complaint) and a defendant’s answer.
**Private Right of Action.** A legal right allowing private parties (as opposed to the government) to bring a lawsuit.

**Pro Rata Share.** A relative proportion of an entire amount. Claimants often receive their respective pro rata share of a settlement fund as permitted in a settlement plan of allocation.

**PSLRA.** The Private Securities Litigation Reform Act of 1995. The PSLRA contains legislative amendments to federal securities laws and governs the procedure for securities class action litigation.

**Rebuttable Presumption.** An assumption that is deemed as a fact unless rebutted by reliable conflicting evidence.

**Request for Admission.** A procedure where a party requests that the adverse party admit certain facts are true and if the adverse a party fails to respond in a timely manner or concedes, the facts are deemed to be true at trial.

**Request for Production.** A discovery procedure to compel the opposing party to provide a list of related documents requested by the movant.

**Scienter.** Intent or knowledge of wrongdoing. An offending party has knowledge of the fraudulence of an act or event prior to committing it.

**Securities Act of 1933.** Comprehensive federal legislation regulating the offer or sale of securities.

**Securities Act of 1934.** Comprehensive federal legislation governing the secondary trading of securities.

**SEC.** U.S. Securities and Exchange Commission. An independent U.S. federal agency primarily responsible for enforcing the federal securities laws, proposing securities rules, and regulating the securities industry and markets.

**Security.** A fungible, negotiable financial instrument that represents some type of financial value.

**Settlement.** The resolution of a lawsuit by the parties without pursuing the matter through a trial.

**Stay.** The act of temporarily stopping a judicial proceeding through the order of a court. Discovery is stayed for actions filed pursuant to the PSLRA.
Strict Liability. Absolute legal responsibility for an injury that can be imposed on the wrongdoer without proof of carelessness or fault. Certain provisions of the Securities Act provide strict liability for violators.

Summary Judgment. A judgment rendered by the court prior to a verdict because no material issue of fact exists and one party or the other is entitled to a judgment as a matter of law.

Trial. A proceeding in which opposing parties in a dispute present evidence and make arguments on the application of the law before a judge or jury.

Typicality. The state of a plaintiff or movant meeting the requirement that it has the claims or defenses of those of everyone else in the class, enabling it to serve as a lead plaintiff or class representative.
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