

UNITED STATES DISTRICT COURT  
CENTRAL DISTRICT OF CALIFORNIA

CIVIL MINUTES -- GENERAL

Date: August 14, 2008

**CV 08-3261-JFW (RZx)** Waterford Township General Employees Retirement System, et al. -v- Downey Financial Corp, et al.

**CV 08-609-JFW (RZx)** Stephan J. Mihalacki -v- Downey Financial Corp., et al.

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**PRESENT:**

**HONORABLE JOHN F. WALTER, UNITED STATES DISTRICT JUDGE**

**Shannon Reilly**  
Courtroom Deputy

**None Present**  
Court Reporter

**ATTORNEYS PRESENT FOR PLAINTIFFS:**

None

**ATTORNEYS PRESENT FOR DEFENDANTS:**

None

**PROCEEDINGS (IN CHAMBERS):**

**ORDER GRANTING WATERFORD TOWNSHIP  
GENERAL EMPLOYEES RETIREMENT SYSTEM S  
MOTION FOR CONSOLIDATION PURSUANT TO  
FED.R. CIV.P. 42(a) [filed 7/22/08; Docket No. 17]**

On July 22, 2008, Plaintiff Waterford Township General Employees Retirement System ("Waterford") filed a Motion for Consolidation Pursuant to Fed.R. Civ.P. 42(a) ("Motion"). On August 4, 2008, Downey Financial Corp. ("Downey") and Brian E. Cote filed their Response and Objection to Waterford Township General Employees Retirement System's Proposed Order on Motion for Consolidation Pursuant to Fed.R. Civ.P. 42(a) ("Response"). On August 11, 2008, Waterford filed a Reply. Pursuant to Rule 78 of the Federal Rules of Civil Procedure and Local Rule 7-15, the Court finds that this matter is appropriate for decision without oral argument. The hearing calendared for August 18, 2008, is hereby vacated and the matter taken off calendar. After considering the moving, opposing, and reply papers and the arguments therein, the Court rules as follows:

**I. Factual and Procedural Background**

On May 16, 2008, Waterford filed a putative class action on behalf of all purchasers of Downey securities between October 16, 2006, and March 14, 2008, alleging claims for relief for (1) violation of Section 10(b) of the 1934 Act and Rule 10b-5; and (2) violation of Section 20(a) of the 1934 Act. In its Complaint, Waterford alleges that Downey and certain of its officers and/or directors engaged in improper behavior that harmed its customers and investors in both Downey's common stock and mortgage-backed securities. Waterford alleges this improper behavior includes

lending to borrowers with little ability to repay the amount loaned, pushing “solid” borrowers into sub-prime loans due to the higher fees generated, and pushing option adjustable-rate mortgages.

On June 2, 2008, Plaintiff Stephen J. Mihalacki (“Mihalacki”) filed a separate putative class action on behalf of all purchasers of Downey securities between October 16, 2006, and March 14, 2008, with virtually identical factual allegation, and alleging the same claims for relief, as the *Waterford* Complaint.

## II. Consolidation

The Private Securities Litigation Reform Act of 1995 (the “Reform Act”) requires the Court to hear motions to consolidate prior to appointing a lead plaintiff. 15 U.S.C. § 78u-4(a)(3)(B)(ii). A district court has broad discretion to consolidate actions involving “common issues of law or fact.” Fed.R.Civ.P. 42(a); *Investors Research Co. v. U.S. Dist. Ct. for Cent. Dist. of Cal.*, 877 F.2d 777, 777 (9th Cir. 1989). In exercising its broad discretion to order consolidation, a district court “weighs the saving of time and effort consolidation would produce against any inconvenience, delay, or expense that it would cause.” *Huene v. U.S.*, 743 F.2d 703, 704 (9th Cir. 1984).

As a preliminary matter, the Court notes that no party objects to the consolidation of the *Waterford* action and the *Mihalacki* action.<sup>1</sup> Furthermore having reviewed and compared the *Mihalacki* Complaint and the *Waterford* Complaint, the Court finds that the two cases involve virtually identical factual and legal issues. The class periods in both cases are identical. Each action involves the same defendants<sup>2</sup> and allege violations of sections 10(b) and 20(a) of the Exchange Act against Downey and certain of its current and former officers and directors. Both actions appear to be based on the same common facts and pose common questions of law: whether defendants issued materially false and misleading reports by failing to disclose and misrepresenting Downey’s financial well-being, business and prospects. Thus, these two actions are appropriate for consolidation under Fed. R. Civ. P. 42(a). Given these similarities, and the lack of any apparent inconvenience, delay or expense that would result from consolidating these cases, the Court finds that consolidation of these related actions is appropriate. Accordingly, the actions identified in the caption above are consolidated for all purposes pursuant to Fed R. Civ. P. 42(a).

## III. Appointment of Lead Plaintiff

Pursuant to the Reform Act:

th[is] presumption . . . may be rebutted only upon proof by a member of the purported plaintiff class that the presumptively most adequate

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<sup>1</sup> In their Response, Downey and Cote object to the form of Waterford’s proposed order, but explicitly state that they do “not object to Waterford’s Motion for Consolidation.” Response, p. 2.

<sup>2</sup> The named defendants are Downey, Brian E. Cote, Daniel D. Rosenthal, and Maurice L. McAlister (collectively “Defendants”).

plaintiff--

- (aa) will not fairly and adequately protect the interests of the class; or
- (bb) is subject to unique defenses that render such plaintiff incapable of adequately representing the class.

15 U.S.C. § 78u-4(a)(3)(B)((iii))(II).

The Reform Act “provides a simple three-step process for identifying the lead plaintiff” in a securities fraud case. *In re Cavanaugh*, 306 F.3d 726, 729 (9th Cir. 2002). “The first step consists of publicizing the pendency of the action, the claims made and the purported class period.” *Id.* The second step requires, “the district court [to] consider the losses allegedly suffered by the various plaintiffs,” and select as the “presumptively most adequate plaintiff” . . . the one who ‘has the largest financial interest in the relief sought by the class’ and [who] ‘otherwise satisfies the requirements of Rule 23 of the Federal Rules of Civil Procedure’.” *Id.* at 729-30. The third and final step, requires the court to “give other plaintiffs an opportunity to rebut the presumptive lead plaintiff’s showing that it satisfies Rule 23’s typicality and adequacy requirements.” *Id.* at 730.

The *Cavanaugh* court cautioned that “a straightforward application of the statutory scheme . . . provides no occasion for comparing plaintiffs with each other on any basis other than their financial stake in the case . . . So long as the plaintiff with the largest losses satisfies the typicality and adequacy requirements, he is entitled to lead plaintiff status, even if the district court is convinced that some other plaintiff would do a better job.” *Id.* at 732. *See also id.* at 739 (holding that the Reform Act was not meant to “authorize the district court to select as lead plaintiff ‘the most sophisticated investor available’”); *Ferrari v. Gisch*, 225 F.R.D. 599, 610 (C.D. Cal. 2004) (“Although the court may compare putative lead plaintiffs when assessing financial stake, once the statutory presumption has attached, it cannot be rebutted through relative comparison”).

In this case, there is no opposition to the appointment of Waterford as lead plaintiff. Moreover, upon review of the papers and evidence submitted by Waterford, the Court finds that Waterford is the “most adequate plaintiff” under PSLRA, 15 U.S.C. § 78u-4(a)(3). On May 16, 2008, counsel for Waterford, the plaintiff that filed the first action, published the requisite notice of the pendency of the *Waterford* action in Business Wire, a world-wide business-oriented wire service. The notice advised class members of the filing of the *Waterford* action and of the class period alleged. It stated that if class members wished to serve as lead plaintiff they were required to move for appointment no later than sixty days after the date on which the notice was published. *See* 15 U.S.C. § 78u-4(a)(3)(A)(i)(II) (stating that within “60 days after the date on which the notice is published, any member of the purported class may move the court to serve as lead plaintiff”). However, other than Waterford’s Motion, no motions for appointment of lead counsel were filed pursuant to the notice.

In addition, a review of the declarations and briefs submitted by Waterford demonstrate that it is the presumptive lead plaintiff because it has suffered an estimated loss of \$23,511, and has the largest financial stake in this litigation. The Reform Act “provides in categorical terms that the *only* basis on which a court may compare plaintiffs competing to serve as lead is the size of their financial stake in the controversy.” *See Cavanaugh*, 306 F.3d at 732 (emphasis in original). Because Waterford has the largest financial interest in the relief sought by the class, Waterford is the presumptive lead plaintiff. *See* 15 U.S.C. § 78u-4(a)(3)(B)(iii)(I). Accordingly, the Court must

consider whether Waterford satisfies the requirements of Rule 23(a) of the Federal Rules of Civil Procedure, and in particular, the requirements of “typicality” and “adequacy.” See *Cavanaugh*, 306 F.3d at 730 (emphasis in original) (stating that the “district court must compare the financial stakes of the various plaintiffs and determine which one has the most to gain from the lawsuit. It must then focus its attention on *that* plaintiff and determine, based on the information he has provided in his pleadings and declarations, whether he satisfies the requirements of Rule 23(a), in particular those of ‘typicality’ and ‘adequacy’”).

With respect to typicality and adequacy, “[a] wide ranging analysis . . . is not appropriate” to determine whether Waterford has made a prima facie showing that it satisfies the requirements of Rule 23, and such a wide ranging analysis “should be left for consideration on a motion for class certification.” *Fischler v. AmSouth Bancorp.*, 1997 WL 118429, \* 2 (M.D. Fla. 1997); see also *In re Cendant Corp. Litigation*, 264 F.3d 201, 263 (3d Cir. 2001) (emphasis in original) (stating that “[t]he initial inquiry (i.e., the determination of whether the movant with the largest interest in the case ‘otherwise satisfies’ Rule 23) should be confined to determining whether the movant has made a prima facie showing of typicality and adequacy”), cert. denied, 535 U.S. 929 (2002); *Gluck v. CellStar Corp.*, 976 F.Supp. 542, 546 (N.D. Tex. 1997) (“Evidence regarding the requirements of Rule 23 will, of course, be heard in full at the class certification hearing. There is no need to require anything more than a preliminary showing at this stage”); *Wenderhold v. Cylink Corp.*, 188 F.R.D. 577, 587 (N.D. Cal.1999) (noting that, at this stage of the litigation, “nothing more than a preliminary showing is required”). Moreover, “institutional investors and others with large losses will, more often than not, satisfy the typicality and adequacy requirements.” *Cendant*, 264 F.3d at 264.

“The typicality inquiry is intended to assess whether the action can be efficiently maintained as a class and whether the [Lead Plaintiffs] have incentives that align with those of absent class members so . . . that the absentees’ interests will be fairly represented.” *Takeda v. Turbodyne Technologies, Inc.*, 67 F.Supp.2d 1129, 1136 (C.D. Cal. 1999) (citation omitted). “Under [Rule 23’s] permissive standards, representative claims are ‘typical’ if they are reasonably co-extensive with those of absent class members; they need not be substantially identical.” *Hanlon v. Chrysler Corp.*, 150 F.3d 1011, 1020 (9th Cir. 1998). “Typicality [thus] entails an inquiry whether the named plaintiff’s individual circumstances are markedly different or . . . the legal theory upon which the claims are based differs from that upon which the claims of other class members will perform be based.” *Takeda*, 67 F.Supp.2d at 1136-37 (citations omitted).

Waterford’s claims are typical because, just like other class members, it: (1) purchased Downey securities during the Class Period, (2) suffered the same injuries as a result of the same course of conduct by Defendants, and (3) have claims that are based on the same legal issues. Accordingly, Waterford’s claims are substantially similar, if not identical, to those of other class members who invested in Downey securities during the Class Period and sustained losses resulting from the alleged false and misleading statements. Because a “preliminary showing” is all that is necessary, the Court concludes that Waterford has met its burden of establishing typicality. See *Cendant*, 264 F.3d at 265 (citations and internal quotation marks omitted) (“in inquiring whether the movant has preliminarily satisfied the typicality requirement, [the court] should consider whether the circumstances of the movant with the largest losses are markedly different or the legal theory upon which the claims of that movant are based differ from that upon which the claims of other class members will perform be based”); *Erikson v. Cornerstone Propane Partners*

*LP*, 2003 WL 22232387, \*3 (N.D. Cal. 2003) (noting that “[a]t this stage of litigation, all that is required is a ‘preliminary showing’ that the lead plaintiff group will satisfy the ‘typicality’ and ‘adequacy’ requirements . . . Lamphere purchased significant numbers of shares of CornerStone stock during the class period and incurred substantial losses allegedly attributable to CornerStone’s actions during that period . . . Lamphere thus satisfies the ‘typicality’ requirement”).

Rule 23(a) requires that the person representing a class be able fairly and adequately to protect the interests of all class members. Fed. R. Civ. P. 23(a)(4). Whether the class representative will adequately represent the class depends on the circumstances of each case. *McGowan v. Faulkner Concrete Pipe Co.*, 659 F.2d 554, 559 (5th Cir. 1981). In evaluating whether a class representative is adequate, courts assess whether he has interests antagonistic to the class, and whether his counsel have the necessary capabilities and qualifications. *In re Emulex Corp.*, 210 F.R.D. 717, 720 (C.D. Cal. 2002). Legal representation is “adequate” when counsel for the class is qualified and competent, the representative’s interests are not antagonistic to the interests of absent class members, and it is unlikely that the action is collusive. *In re Northern District of California, Dalkon Shield IUD Products Liability Litigation*, 693 F.2d 847, 855 (9th Cir. 1982). In addition, the class representative must have a sufficient interest in the outcome of the case to ensure vigorous advocacy. *See Riordan v. Smith Barney*, 113 F.R.D. 60, 64 (N.D.Ill. 1986). “Adequacy, for purposes of the lead plaintiff determination, is contingent upon both the existence of common interests between the proposed lead plaintiffs and the class, and a willingness on the part of the proposed lead plaintiff to vigorously prosecute the action.” *In re Milestone Scientific Securities Litigation*, 183 F.R.D. 404, 416 (D.N.J. 1998).

Waterford is an “adequate” plaintiff because it has suffered the greatest financial loss, ensuring vigorous advocacy, and Waterford has represented that it is willing and able to undertake the responsibilities of lead plaintiff. Moreover, Waterford’s interests are not antagonistic to those of other class members. To the contrary, Waterford’s interests are aligned with those of other class members because each member of the class purchased Downey securities in reliance on its allegedly false and misleading statements. Finally, there is no evidence that Waterford’s action is collusive. Based on the foregoing, Waterford has made the necessary prima facie showing that it satisfies both the typicality and adequacy requirements of Rule 23. Accordingly, the Court appoints Waterford as lead plaintiff in this consolidated action.

#### **IV. Appointment of Lead Counsel**

Once the court has designated a lead plaintiff, that plaintiff “shall, subject to the approval of the court, select and retain counsel to represent the class.” 15 U.S.C. § 78u-4(a)(3)(B)(v). A court may disturb the lead plaintiff’s choice of counsel only if it appears necessary to “protect the interests of the class.” 15 U.S.C. § 78u-(a)(3)(B)(iii)(II)(aa); *see also Vincent v. Hughes Air West, Inc.*, 557 F.2d 759, 774 (9th Cir. 1977) (quoting *MacAlister v. Guterma*, 263 F.2d 65, 69 (2d Cir. 1958)) (“The benefits achieved by consolidation and the appointment of general counsel, i. e. elimination of duplication and repetition and in effect the creation of a coordinator of diffuse plaintiffs through whom motions and discovery proceedings will be channeled, will most certainly redound to the benefit of all parties to the litigation.”).

In this case, Waterford wishes to retain Coughlin Stoia Geller Rudman & Robbins, LLP (“CSGRR”) as lead counsel. The Court has reviewed CSGRR’s firm resume, and is satisfied that it

is capable of serving competently in the role of lead counsel. CSGRR, a 200-lawyer firm, has substantial experience litigating securities fraud class actions on behalf of investors. In fact, CSGRR actively engages in a variety of complex litigation, emphasizing securities, consumer, and antitrust class actions. In addition, CSGRR has reportedly recovered billions of dollars on behalf of investors. Accordingly, the Court approves the appointment of CSGRR as lead counsel in this action.

**V. Conclusion**

For the foregoing reasons, the Court **GRANTS** Waterford's Motion. Accordingly, the Court also orders the following:

1. The Clerk shall consolidate the *Waterford* and *Mihalacki* actions such that the higher-numbered case, CV 08-3261-JFW (RZx), is designated the Master File. All documents filed hereafter shall bear the Master File case number CV 08-3261-JFW (RZx) and the following caption:

IN RE DOWNEY SECURITIES ) Case No. CV 08-3261-JFW (RZx)  
LITIGATION ) CLASS ACTION  
\_\_\_\_\_ )

2. The Court appoints Waterford as Lead Plaintiff.

3. The Court appoints CSGRR as Lead Counsel.

3. Lead Plaintiff Waterford shall file a consolidated derivative complaint no later than ten (10) days from the date of this Minute Order. The consolidated complaint shall be deemed the operative complaint, superseding all complaints filed in any of the actions consolidated hereunder. The consolidated complaint shall be treated as if it were the original complaint and filing deadlines shall be determined by the filing date of the consolidated complaint. The Court will dismiss the individual complaints after the filing of the consolidated complaint. Defendants shall respond to the consolidated complaint only.

IT IS SO ORDERED.

The Clerk shall serve a copy of this Minute Order on all parties to this action.