

CORNERSTONE RESEARCH

ECONOMIC AND FINANCIAL CONSULTING AND EXPERT TESTIMONY

Securities Class Action Settlements

2013 Review and Analysis



TABLE OF CONTENTS

Highlights	1
Developing Trends.....	2
Number and Size of Settlements.....	3
Total Settlement Dollars	3
Mega Settlements.....	4
Settlement Size	5
Damages Estimates and Market Capitalization Losses.....	7
“Estimated Damages”	7
Disclosure Dollar Loss.....	10
Tiered Estimated Damages	11
Analysis of Settlement Characteristics	12
Nature of Claims.....	12
Accounting Allegations	13
Third-Party Codefendants.....	14
Institutional Investors.....	15
Derivative Actions	16
Corresponding SEC Actions	17
Comparison of Settlement Characteristics by Size	18
Time to Settlement.....	19
Litigation Stages	20
Industry Sectors	21
Federal Court Circuits.....	22
Cornerstone Research’s Settlement Prediction Analysis	23
Research Sample.....	24
Data Sources	24
Endnotes	25
About the Authors.....	26

TABLE OF FIGURES

Figure 1: Settlement Statistics	1
Figure 2: Total Settlement Dollars.....	3
Figure 3: Mega Settlements	4
Figure 4: Cumulative Ten-Year Settlement Distribution	5
Figure 5: Settlement Percentiles	6
Figure 6: Median and Average “Estimated Damages”	7
Figure 7: Median Settlements as a Percentage of “Estimated Damages”	8
Figure 8: Median Settlements as a Percentage of “Estimated Damages” by Damages Ranges.....	9
Figure 9: Median and Average Disclosure Dollar Loss.....	10
Figure 10: Tiered Estimated Damages.....	11
Figure 11: Settlements by Nature of Claims.....	12
Figure 12: Median Settlements as a Percentage of “Estimated Damages” and Accounting Allegations.....	13
Figure 13: Median Settlements as a Percentage of “Estimated Damages” and Third-Party Codefendants	14
Figure 14: Median Settlement Amounts and Public Pensions	15
Figure 15: Frequency of Derivative Actions.....	16
Figure 16: Frequency of SEC Actions	17
Figure 17: Comparison of Settlement Characteristics by Size.....	18
Figure 18: Median Settlements by Duration from Filing Date to Settlement Hearing Date	19
Figure 19: Litigation Stages.....	20
Figure 20: Settlements by Select Industry Sectors.....	21
Figure 21: Settlements by Federal Court Circuit	22

HIGHLIGHTS

- Total settlement dollars in 2013 increased substantially—46 percent over 2012 and 60 percent above the average for the prior five years. [\(page 3\)](#)
- There were 67 settlements in 2013 (up from 57 in 2012), the first year-over-year increase since 2009. [\(page 3\)](#)
- Mega settlements pushed settlement dollars up in 2013, accounting for 84 percent of total settlement dollars, the second highest proportion in the last decade. [\(page 4\)](#)
- While mega settlements drove up the 2013 average settlement amount, the median settlement amount declined, reflecting a reduction in the size of more typical cases. [\(page 5\)](#)
- For 2013, the median “estimated damages” declined 48 percent from 2012 and is 17.5 percent lower than the median for post-Reform Act settlements in the prior five years. Since “estimated damages” are the most important factor in determining settlement amounts, this decline was likely a major factor contributing to the substantially lower median settlement in 2013 compared with 2012. [\(page 7\)](#)
- The proportion of settled cases in 2013 involving accounting allegations dipped to a ten-year low, but the settlement as a percentage of “estimated damages” for these cases was much higher than for cases not involving such allegations. [\(page 13\)](#)
- The median settlement in 2013 for cases with a public pension as a lead plaintiff was \$23 million, compared with \$3 million for cases without a public pension as a lead plaintiff. [\(page 15\)](#)
- New analyses reveal that settlements of \$50 million or lower are far less likely to involve accompanying SEC actions or a public pension as a lead plaintiff. [\(page 18\)](#)

FIGURE 1: SETTLEMENT STATISTICS

(Dollars in Millions)

	2013	1996–2012
Minimum	\$0.7	\$0.1
Median	\$6.5	\$8.3
Average	\$71.3	\$55.5
Maximum	\$2,425.0	\$8,358.2
Total Amount	\$4,773.9	\$73,740.2

Note: Settlement dollars adjusted for inflation; 2013 dollar equivalent figures used.

DEVELOPING TRENDS

The year 2013 saw the highest total dollar value of settlements approved over the last six years. This was due in part to an uptick in the number of cases settled (compared with the prior two years), as well as the relatively high average shareholder losses associated with cases settled in 2013 (the second highest in the last six years). The surrounding economic events are an important backdrop to understanding the settlement trends.

Settlement sizes in 2013 were affected by the resolution of a number of credit crisis cases, which tend to involve relatively large settlement amounts and related investor losses. Pharmaceutical industry sector settlements also contributed to the overall increase.

At the opposite end of the settlement spectrum were settlements of Chinese reverse merger cases. These matters tend to be relatively small. According to *Securities Class Action Filings—2013 Year in Review* released earlier this year by Cornerstone Research, the majority of these cases were filed in 2011 and thus, not surprisingly, a relatively large number (14 cases) were settled in 2013. All but one of these settlements were for amounts less than \$10 million.

Despite record enforcement activity by the SEC in the last couple of years, there has not been an increase in securities class action settlements accompanied by SEC actions. This is due in part to the potential lag between the underlying class action settlement and resolution of activity commenced by the SEC. Furthermore, the SEC's enforcement activity includes matters outside the scope of this research. Nevertheless, it is possible there will be an increase in securities class actions accompanied by disclosure-related SEC enforcement actions in the future.

In addition, securities class action filings (i.e., new cases) involving Rule 10b-5, Section 11, and/or Section 12 allegations have been relatively high over the last few years, including a surge in the second half of 2013 (see *Securities Class Action Filings—2013 Year in Review*). Thus, it is unlikely there will be any significant decline in the overall number of cases settled in upcoming years.

Looking ahead, it would be remiss not to mention the *Halliburton Co. v. Erica P. John Fund* matter currently before the U.S. Supreme Court. As has been widely discussed, the case challenges the fraud-on-the-market presumption that was established in 1988 through *Basic Inc. v. Levinson*. The suit has the potential to dramatically affect the entire landscape surrounding securities class actions, including issues that are the focus of this report, such as the damages associated with securities cases, the progression of these cases through the litigation process, and ultimately, the settlement amounts involved.

This report analyzes a sample of securities class actions filed after passage of the Private Securities Litigation Reform Act of 1995 (Reform Act) and settled from 1996 through year-end 2013, and explores a variety of factors that influence settlement outcomes. This study focuses on cases alleging fraudulent inflation in the price of a corporation's common stock (i.e., excluding cases with alleged classes of only bondholders, preferred stockholders, etc., and excluding cases alleging fraudulent depression in price). See page 24 for a detailed description of the research sample.

NUMBER AND SIZE OF SETTLEMENTS

TOTAL SETTLEMENT DOLLARS

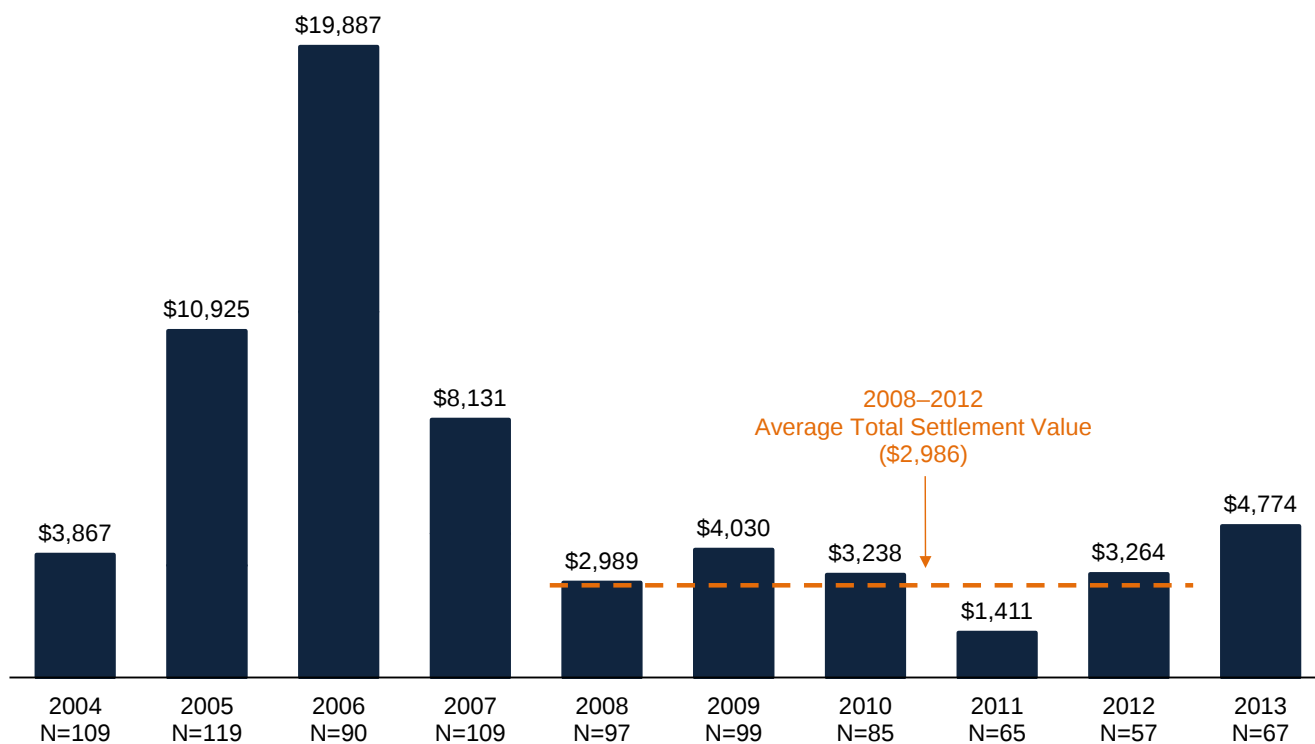
- In 2013, there were 67 court-approved settlements, a 17.5 percent increase from 2012 and a reversal of the year-over-year decline in the number of settlements observed since 2009.
- The increase in the number of settlements is likely due, in part, to increased securities class action filings during 2010 through 2012.¹ (See page 19 for a related discussion of time from filing to settlement.)
- The increase in total settlement dollars in 2013 was largely driven by six mega settlements (settlements at or above \$100 million).

Total settlement dollars in 2013 increased 46 percent over 2012.

FIGURE 2: TOTAL SETTLEMENT DOLLARS

2004–2013

(Dollars in Millions)



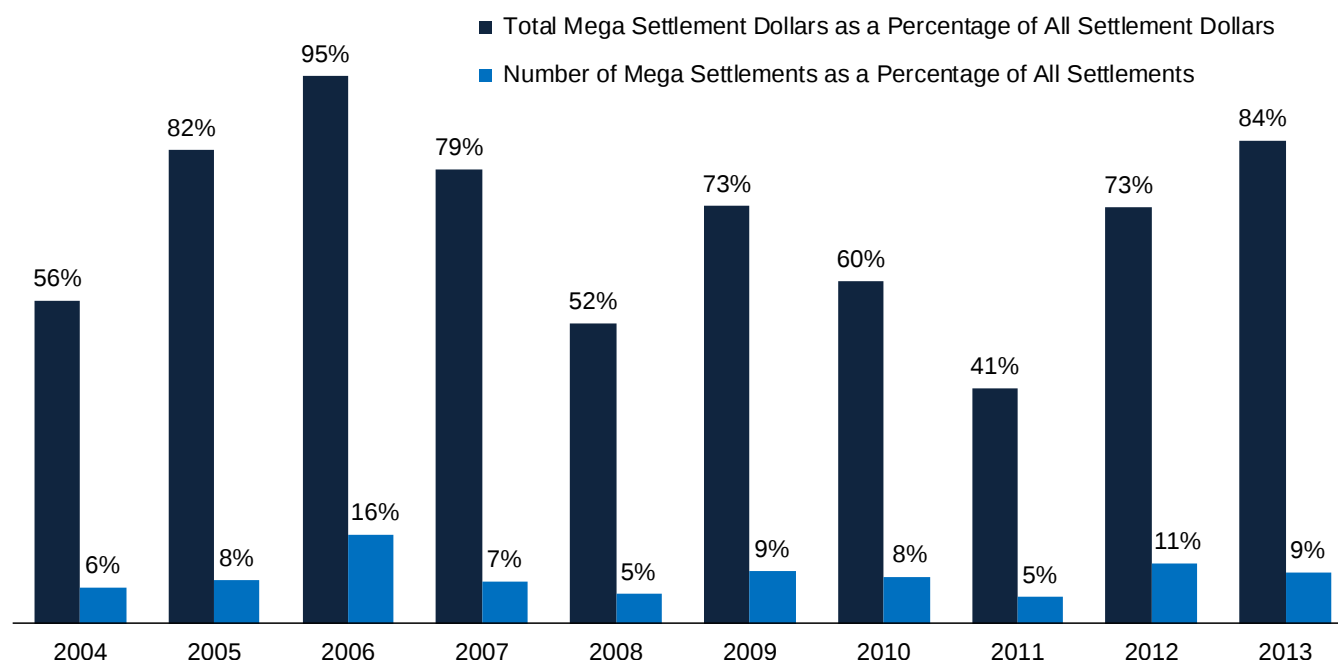
Note: Settlement dollars adjusted for inflation; 2013 dollar equivalent figures used.

MEGA SETTLEMENTS

- The percentage of settlement dollars from mega settlements (settlements at or above \$100 million) was the second highest proportion in the last ten years.
- As noted, there were six mega settlements in 2013, including one settlement for more than \$2 billion. The remaining five cases settled for between \$150 million and \$600 million.
- Three mega settlements involved pharmaceutical companies, and three involved financial institutions.

In 2013,
six settlements
accounted for
84 percent of total
settlement dollars.

FIGURE 3: MEGA SETTLEMENTS
2004–2013

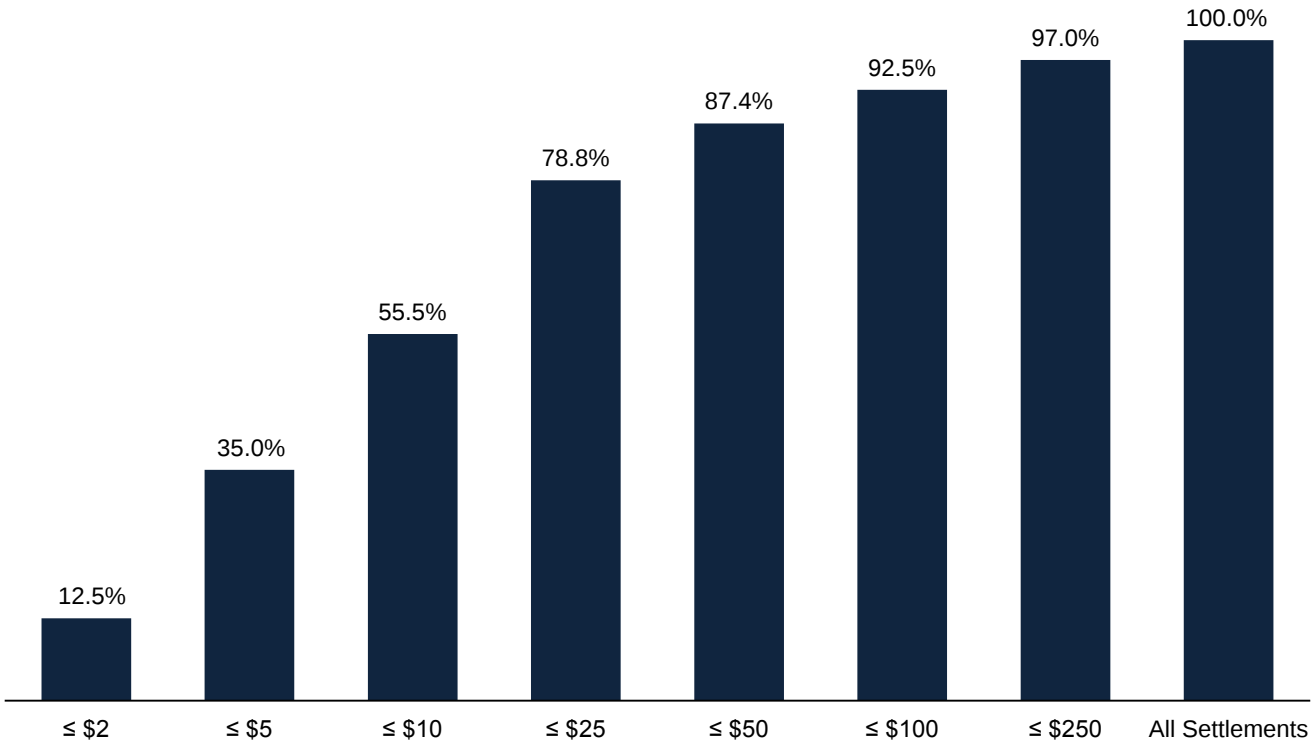


SETTLEMENT SIZE

- In 2013, the settlement size in approximately 60 percent of settled cases was \$10 million or less, slightly higher than the cumulative ten-year percentage of about 56 percent.
- This high number of smaller settlements contributed to a 37 percent decline in the median settlement size in 2013 compared with 2012 (\$6.5 million in 2013 versus \$10.3 million in 2012).
- Roughly 32 percent of settlements less than \$10 million in 2013 were for cases involving Chinese reverse mergers.²
- A total of 44 cases related to the subprime credit crisis are included in this study.³ The median settlement for credit crisis–related cases was \$30 million and the average settlement was over \$140 million. These cases generally settle for higher amounts compared to cases not associated with the credit crisis.

The vast majority of securities class actions settle for less than \$50 million.

FIGURE 4: CUMULATIVE TEN-YEAR SETTLEMENT DISTRIBUTION
2004–2013
(Dollars in Millions)



Note: Settlement dollars adjusted for inflation; 2013 dollar equivalent figures used.

SETTLEMENT SIZE *continued*

- Overall, 50 percent of post–Reform Act cases have settled for between \$3.6 million and \$20.6 million.
- Despite recent swings in annual median settlements, the range of settlement values between the 25th and 75th percentiles, with few exceptions, has fluctuated moderately with no discernible trend.

Annual median settlement values have ranged between \$6 and \$12 million in recent years.

FIGURE 5: SETTLEMENT PERCENTILES*(Dollars in Millions)*

Year	Average	10th	25th	Median	75th	90th
1996–2013	\$42.0	\$1.7	\$3.6	\$8.1	\$20.6	\$70.6
2013	\$71.3	\$1.9	\$3.0	\$6.5	\$21.5	\$79.5
2012	\$57.3	\$1.3	\$2.8	\$10.3	\$35.5	\$110.6
2011	\$21.7	\$1.9	\$2.6	\$6.0	\$18.6	\$43.3
2010	\$38.1	\$2.1	\$4.5	\$12.0	\$26.7	\$85.0
2009	\$40.7	\$2.6	\$4.2	\$8.7	\$21.7	\$72.1

Note: Settlement dollars adjusted for inflation; 2013 dollar equivalent figures used.

DAMAGES ESTIMATES AND MARKET CAPITALIZATION LOSSES

“ESTIMATED DAMAGES”

For purposes of this research and prior Cornerstone Research reports on securities class action settlements, these analyses use simplified calculations of shareholder losses, referred to as “estimated damages.” Application of this consistent method allows for the identification and analysis of potential trends. “Estimated damages” are not necessarily linked to the allegations included in the associated court pleadings.⁴ Accordingly, damages estimates presented in this report are not intended to be indicative of actual economic damages borne by shareholders.

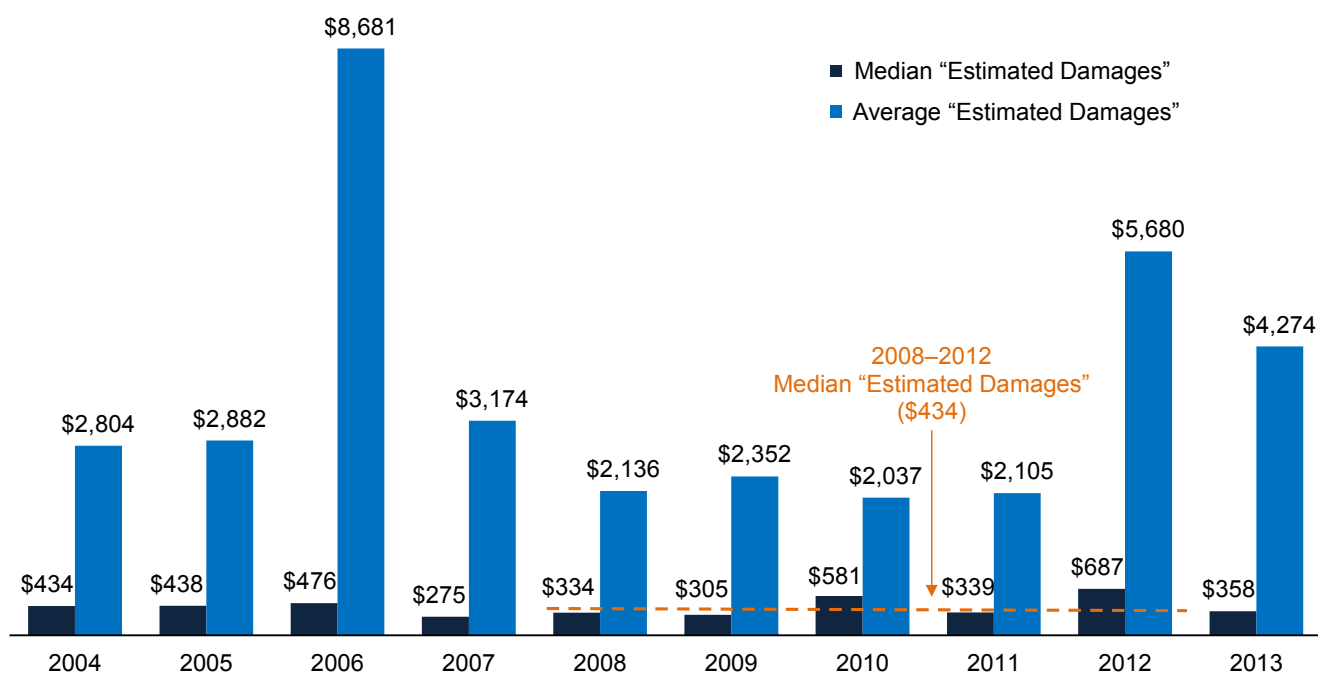
- Average “estimated damages” for 2013 were the third highest in the post-Reform Act era, due in part to a small number of extremely large cases, two of which related to the credit crisis.
- The decline in median “estimated damages” was likely a major factor contributing to the substantially lower median settlement in 2013 relative to 2012.⁵

Median “estimated damages” for 2013 declined 48 percent from 2012.

FIGURE 6: MEDIAN AND AVERAGE “ESTIMATED DAMAGES”

2004–2013

(Dollars in Millions)



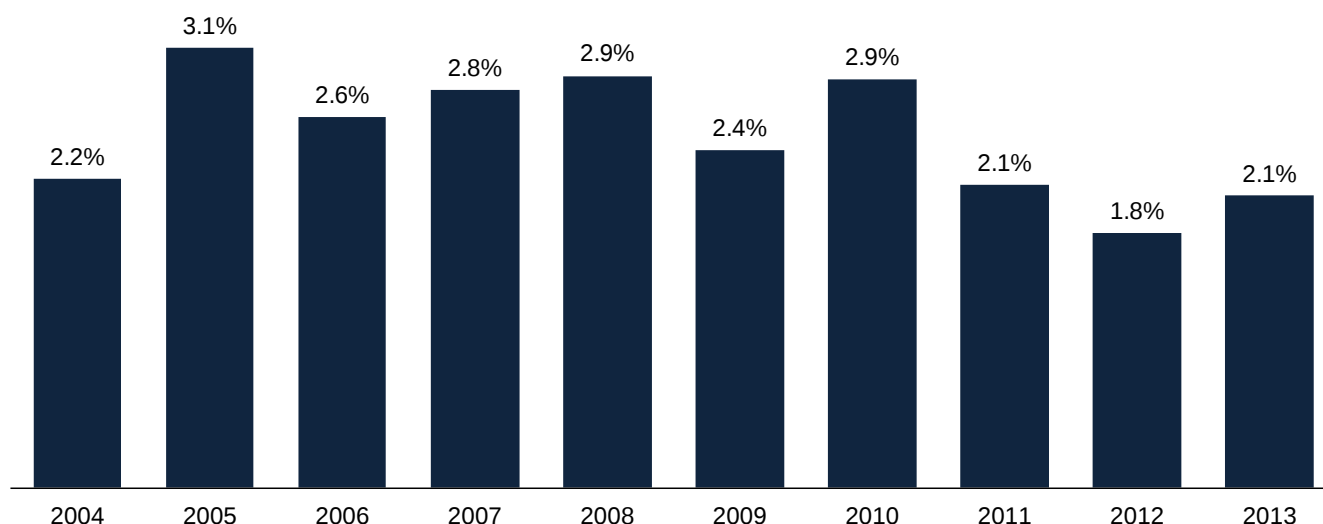
Note: “Estimated damages” are adjusted for inflation based on class period end dates.

“ESTIMATED DAMAGES” *continued*

- In 2013, the median settlement as a percentage of “estimated damages” rebounded slightly from a historic low of 1.8 percent in 2012.
- Median settlements as a percentage of “estimated damages” remained relatively low compared to levels observed over the past decade. Two factors contributed to this: the increased number of extremely large cases and the presence of credit crisis cases.
 - Traditionally, cases with large “estimated damages” have settled for a smaller proportion of those damages.
 - For credit crisis cases settled in 2013, the median settlement as a percentage of “estimated damages” was 0.7 percent, compared with 2.3 percent for all other cases settled in 2013.

Settlements as a percentage of “estimated damages” observed over the last three years are the lowest in the past decade.

FIGURE 7: MEDIAN SETTLEMENTS AS A PERCENTAGE OF “ESTIMATED DAMAGES” 2004–2013



“ESTIMATED DAMAGES” continued

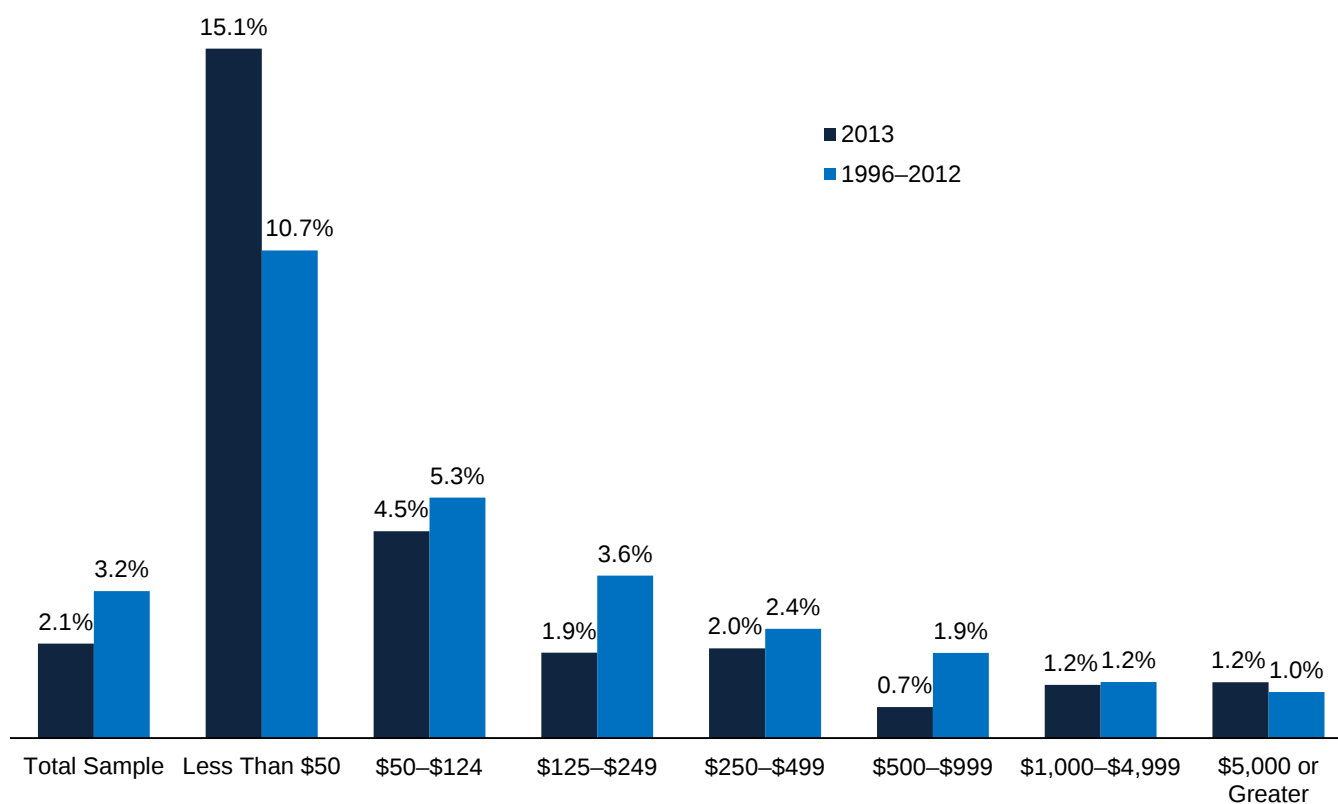
- Settlement amounts are generally larger when “estimated damages” are larger. Yet, as previously mentioned, settlements as a percentage of “estimated damages” tend to be smaller when “estimated damages” are larger.
- In 2013, relatively small cases—those with “estimated damages” of less than \$50 million—had a median settlement as a percentage of “estimated damages” of 15.1 percent, compared with 2.1 percent for all 2013 settlements.

In 2013, smaller cases settled at a much higher percentage of “estimated damages.”

FIGURE 8: MEDIAN SETTLEMENTS AS A PERCENTAGE OF “ESTIMATED DAMAGES” BY DAMAGES RANGES

1996–2013

(Dollars in Millions)



DISCLOSURE DOLLAR LOSS

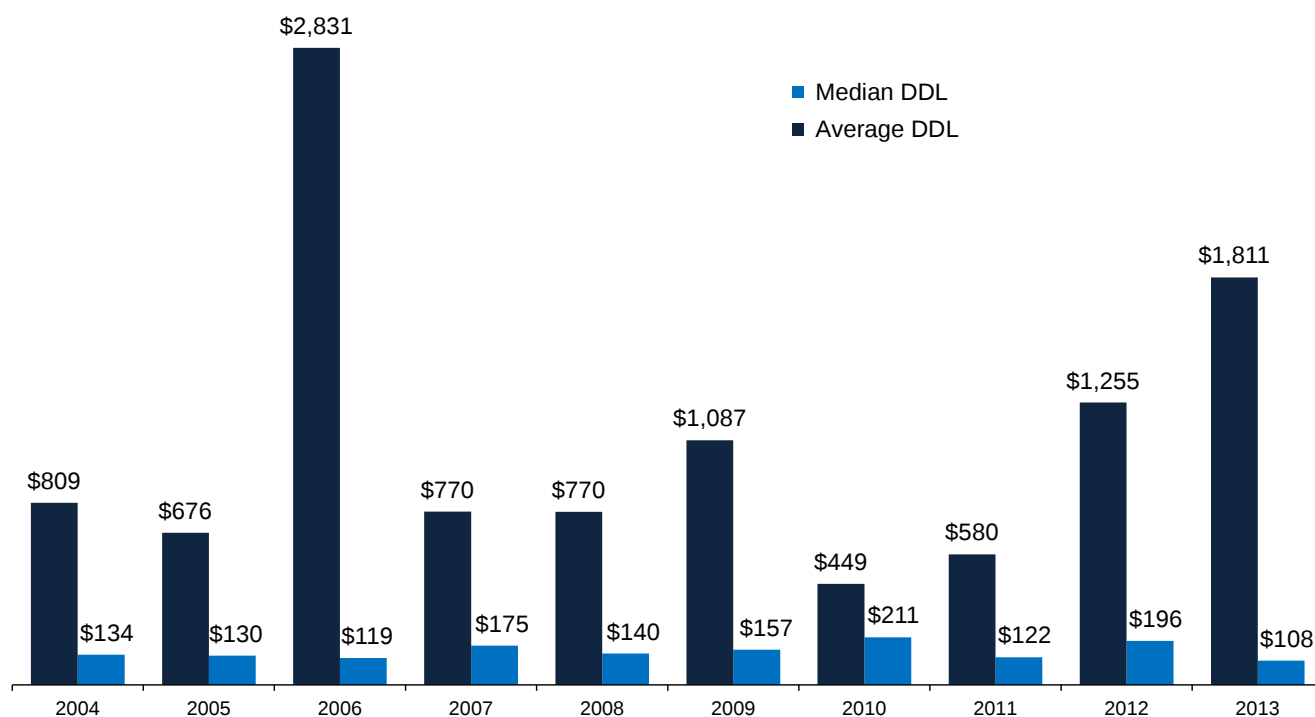
Disclosure Dollar Loss (DDL) is another simplified measure of shareholder losses and an alternative measure to “estimated damages.” DDL is calculated as the decline in the market capitalization of the defendant firm from the trading day immediately preceding the end of the class period to the trading day immediately following the end of the class period.⁶

- In contrast to the median DDL, average DDL increased 44 percent from 2012 to \$1.8 billion, reflecting the influence of a few very large cases.
- The median market capitalization at the time of settlement for issuers in the top 10 percent of DDL was dramatically higher than the median market capitalization for the next tier of DDL (\$133.8 billion compared with \$9.2 billion).
- The relationship between settlements and DDL is similar to that between settlements and “estimated damages”—settlements are larger when DDL is larger, yet settlements as a percentage of DDL are generally smaller when DDL is larger.

The median DDL associated with settled cases in 2013 decreased 45 percent from 2012.

FIGURE 9: MEDIAN AND AVERAGE DISCLOSURE DOLLAR LOSS 2004–2013

(Dollars in Millions)



Note: DDL adjusted for inflation based on class period end dates.

TIERED ESTIMATED DAMAGES

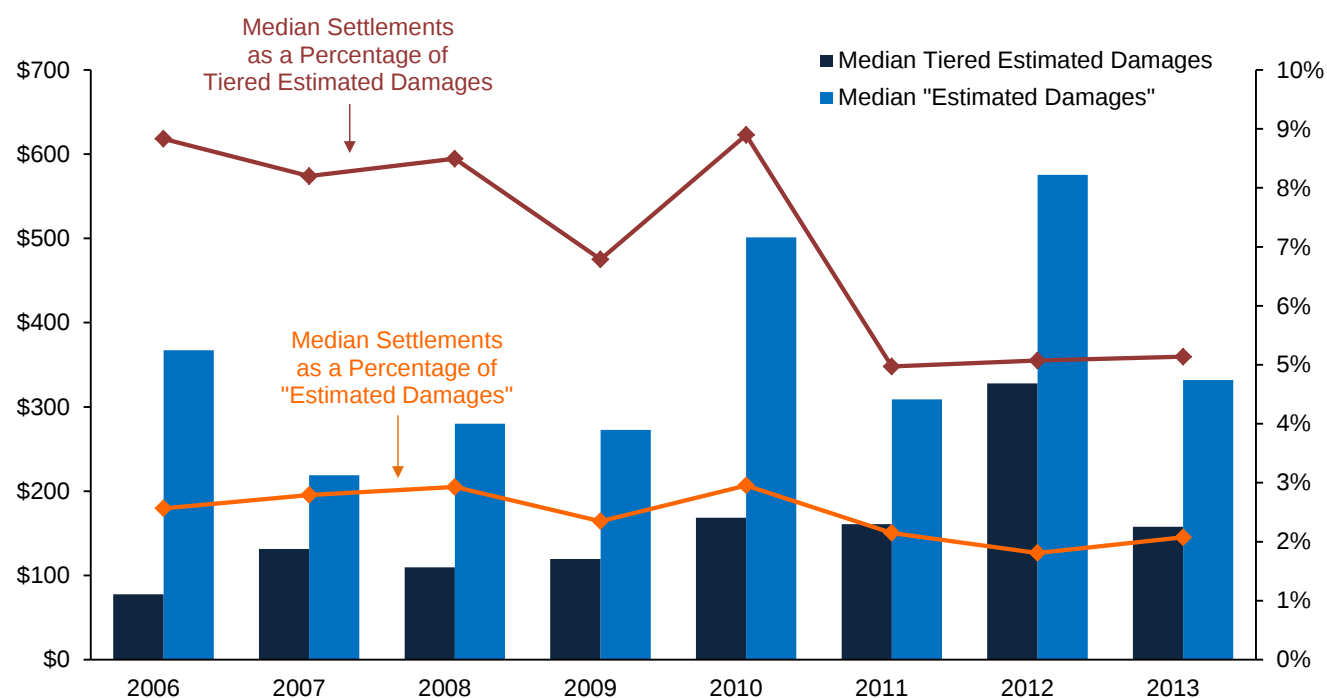
The landmark decision in 2005 by the U.S. Supreme Court in *Dura Pharmaceuticals Inc. v. Broudo* (*Dura*) determined that plaintiffs must show a causal link between alleged misrepresentations and the subsequent actual losses suffered by plaintiffs. As a result of this decision, damages cannot be associated with shares sold before information regarding the alleged fraud reaches the market. Accordingly, this report considers the influence of *Dura* on securities class action damages calculations by exploring an alternative measure of damages in settlements research. This alternative measure, referred to here as tiered estimated damages, is based on the stock-price drops on alleged corrective disclosure dates as described in the plan of allocation for the settlement.⁷ It utilizes a single value line when there is only one alleged corrective disclosure date (at the end of the class period) or a tiered value line when there are multiple alleged corrective disclosure dates.

This alternative measure has been calculated for a subsample of cases settled after 2005. As noted in past reports, tiered estimated damages has not yet surpassed the traditional measure of “estimated damages” used in this series of reports in terms of its power as a predictor of settlement outcomes. However, it is highly correlated with settlement amounts and provides an alternative measure of investor losses for more recent securities class action settlements.

FIGURE 10: TIERED ESTIMATED DAMAGES

2006–2013

(Dollars in Millions)



ANALYSIS OF SETTLEMENT CHARACTERISTICS

NATURE OF CLAIMS

- The number of cases settled in 2013 involving only Section 11 and/or Section 12(a)(2) claims is consistent with the increased activity in the U.S. IPO market in recent years.⁸ There were eight such cases in 2013 compared with only four in 2012.
- The median settlement as a percentage of “estimated damages” is higher for cases involving only Section 11 and/or Section 12(a)(2) claims compared with cases involving only Rule 10b-5 claims.

“Estimated damages” are typically smaller for cases involving only Section 11 and/or Section 12(a)(2) claims.

FIGURE 11: SETTLEMENTS BY NATURE OF CLAIMS

1996–2013

(Dollars in Millions)

	Number of Settlements	Median Settlements	Median "Estimated Damages"	Median Settlements as a Percentage of "Estimated Damages"
Section 11 and/or 12(a)(2) Only	80	\$3.4	\$46.7	7.4%
Both Rule 10b-5 and Section 11 and/or 12(a)(2)	246	\$11.7	\$402.3	3.4%
Rule 10b-5 Only	1,049	\$6.8	\$272.2	2.9%
All Post-Reform Act Settlements	1,376	\$7.0	\$257.1	3.1%

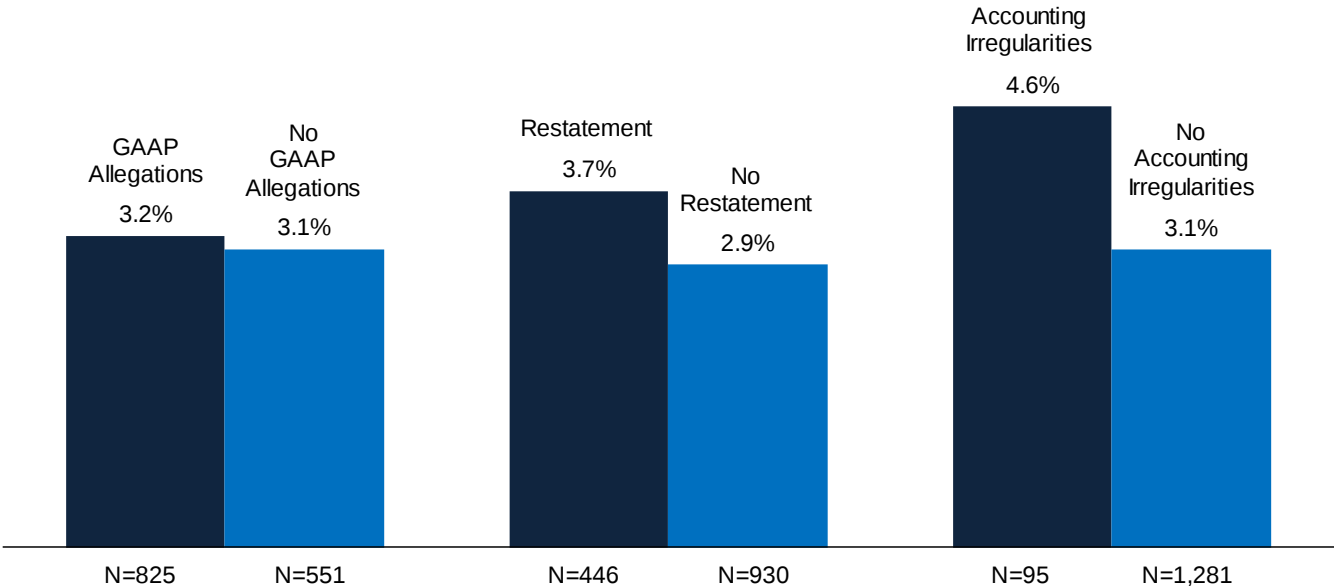
ACCOUNTING ALLEGATIONS

This research examines three types of accounting allegations among settled cases: (1) alleged GAAP violations, (2) restatements, and (3) reported accounting irregularities.⁹

- Cases involving accounting allegations are typically associated with higher settlement amounts and higher settlements as a percentage of “estimated damages.”
- Cases alleging GAAP violations settled for only a slightly higher percentage of “estimated damages” than cases not alleging GAAP violations.
- Restatement cases settled for a higher percentage of “estimated damages” compared with GAAP cases not involving restatements.
- In 2013, 55 percent of settled cases alleged GAAP violations, 21 percent were associated with restatements, while only 4 percent involved reported accounting irregularities.
- Although relatively few settlements in 2013 involved reported accounting irregularities, these cases settled for a much larger percentage of “estimated damages” compared with cases not involving accounting irregularities.

The proportion of settled cases in 2013 involving accounting allegations dipped to a ten-year low.

FIGURE 12: MEDIAN SETTLEMENTS AS A PERCENTAGE OF “ESTIMATED DAMAGES” AND ACCOUNTING ALLEGATIONS 1996–2013

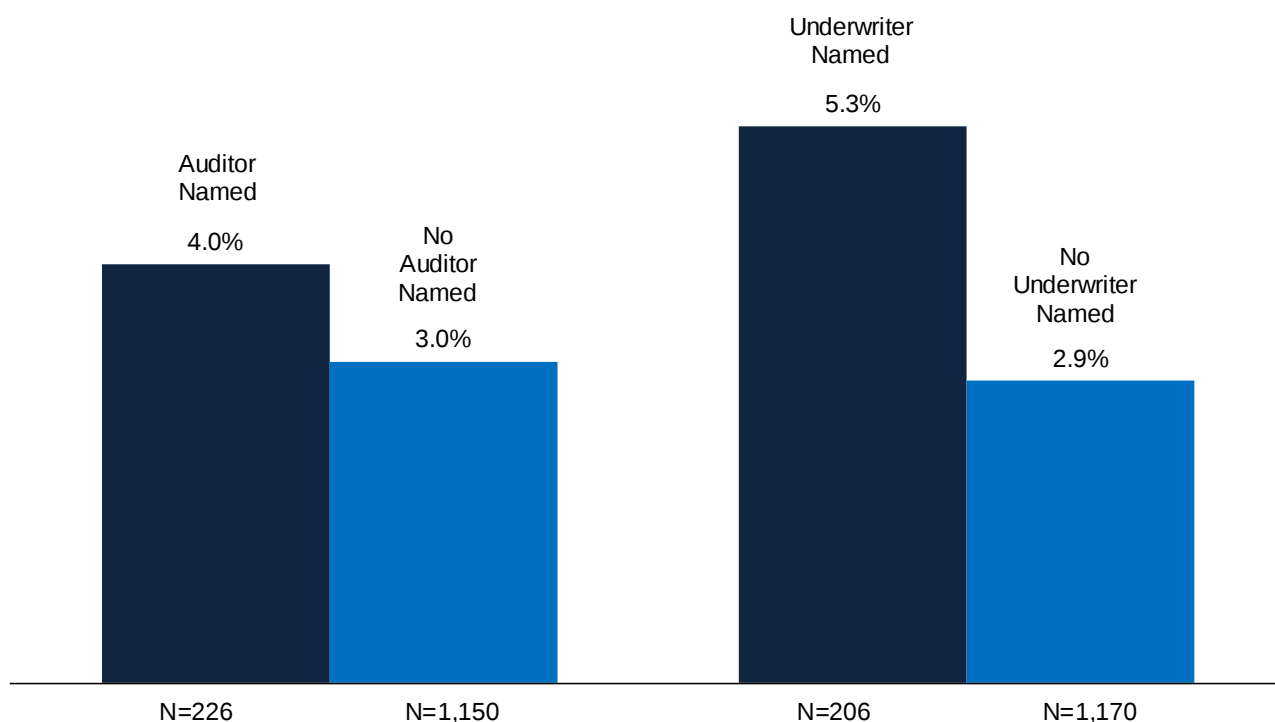


THIRD-PARTY CODEFENDANTS

- Third parties, such as an auditor or an underwriter, are often named as codefendants in larger, more complex cases and provide an additional source of settlement funds.
- Outside auditor defendants are often associated with cases involving restatements of financial statements or alleged GAAP violations, while the presence of underwriter defendants is highly correlated with the inclusion of Section 11 claims.
- In 2013, 32 percent of accounting-related cases had a named auditor defendant, while 76 percent of cases with Section 11 claims had a named underwriter defendant.

Cases with third-party codefendants have higher settlements as a percentage of “estimated damages.”

FIGURE 13: MEDIAN SETTLEMENTS AS A PERCENTAGE OF “ESTIMATED DAMAGES” AND THIRD-PARTY CODEFENDANTS 1996–2013



INSTITUTIONAL INVESTORS

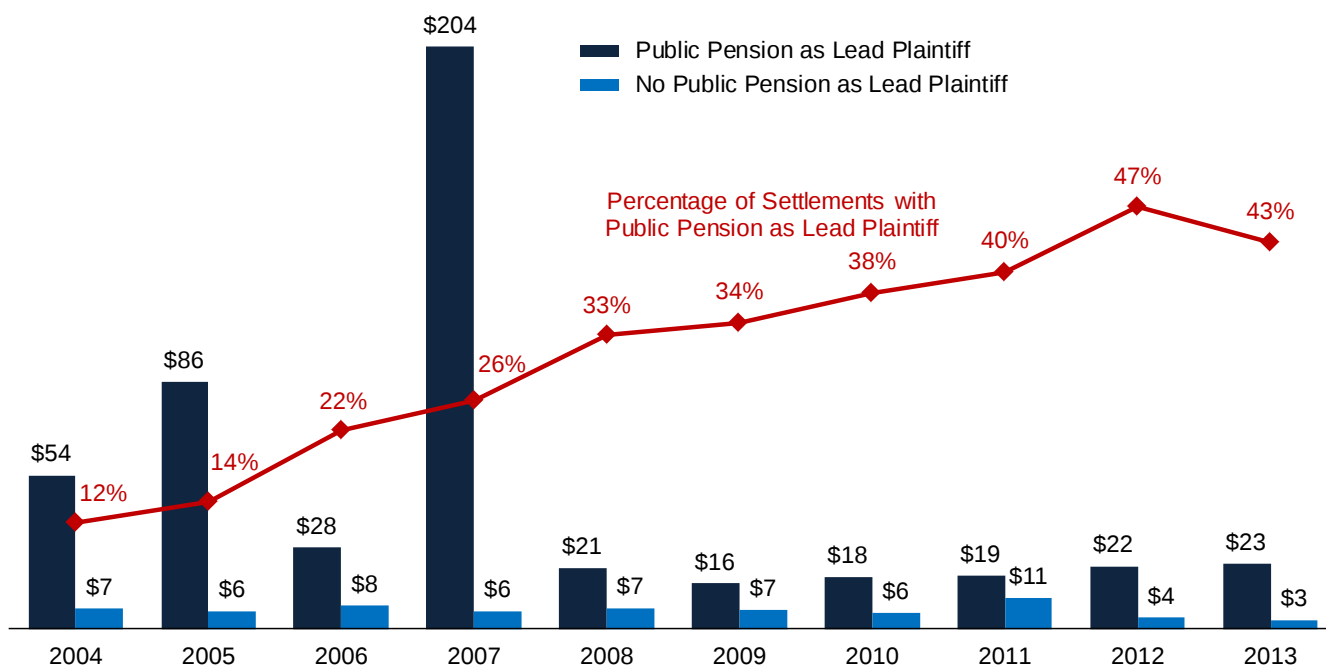
- Since 2006, more than half of the settlements in any given year have involved institutional investors as lead plaintiffs.
- Among institutional investors, public pensions are the most active, involved as lead plaintiffs in over 55 percent of settlements with an institutional investor lead plaintiff since 2006.
- In 2013, public pensions served as a lead plaintiff in 43 percent of settled cases, slightly lower than in 2012 (47 percent), but nearly four times the 2004 figure (12 percent).
- The median settlement in 2013 for cases with a public pension as a lead plaintiff was \$23 million, compared with \$3 million for cases without a public pension as a lead plaintiff.

The presence of a public pension as a lead plaintiff is associated with higher settlements.

FIGURE 14: MEDIAN SETTLEMENT AMOUNTS AND PUBLIC PENSIONS

2004–2013

(Dollars in Millions)



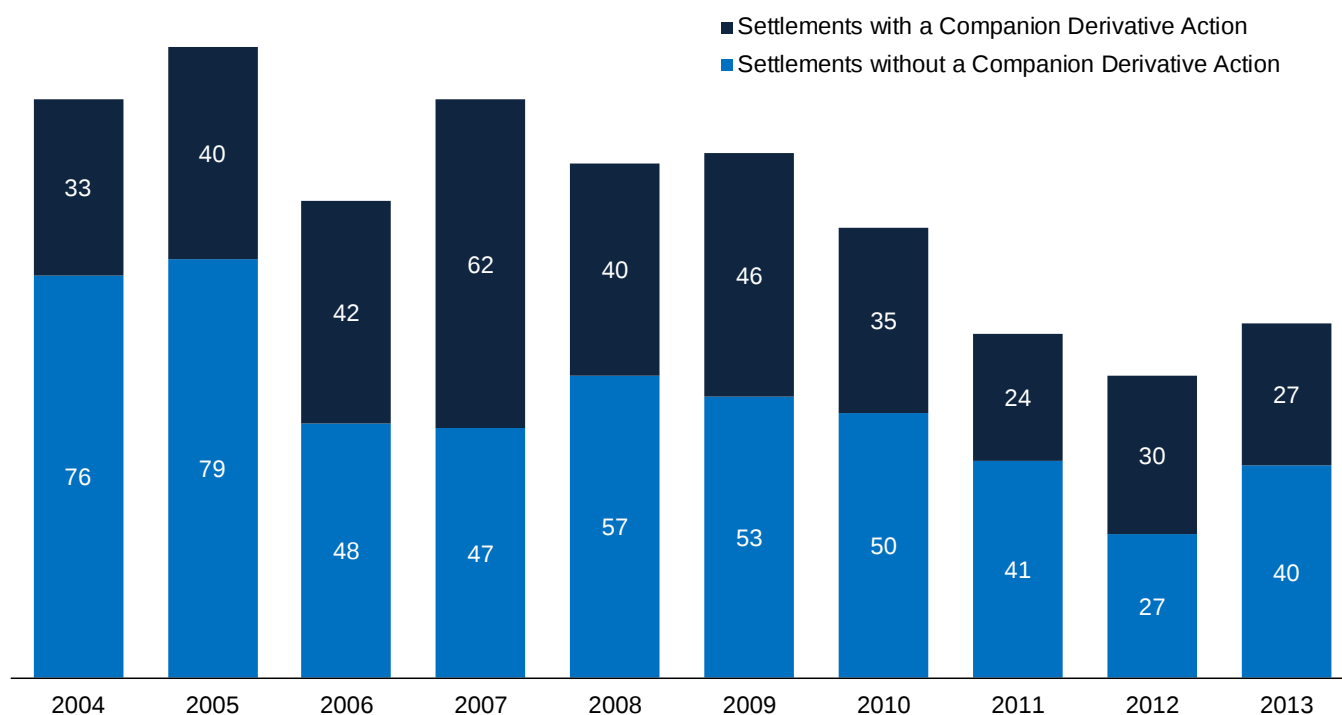
Note: Settlement dollars adjusted for inflation; 2013 dollar equivalent figures used.

DERIVATIVE ACTIONS

- “Estimated damages” for cases with accompanying derivative actions are typically higher compared to cases with no identifiable derivative action.¹⁰
- In 2013, 40 percent of settled cases were accompanied by derivative actions, compared with 53 percent of settled cases in 2012, and 32 percent of settled cases in prior post-Reform Act years.
- In recent years, cases in the sample have included far fewer simultaneous class and derivative settlements than in prior years.¹¹ In fact, during 2013, only two securities class actions settled simultaneously with the related derivative action.

Settlement amounts for class actions accompanied by derivative actions are significantly higher.

FIGURE 15: FREQUENCY OF DERIVATIVE ACTIONS
2004–2013



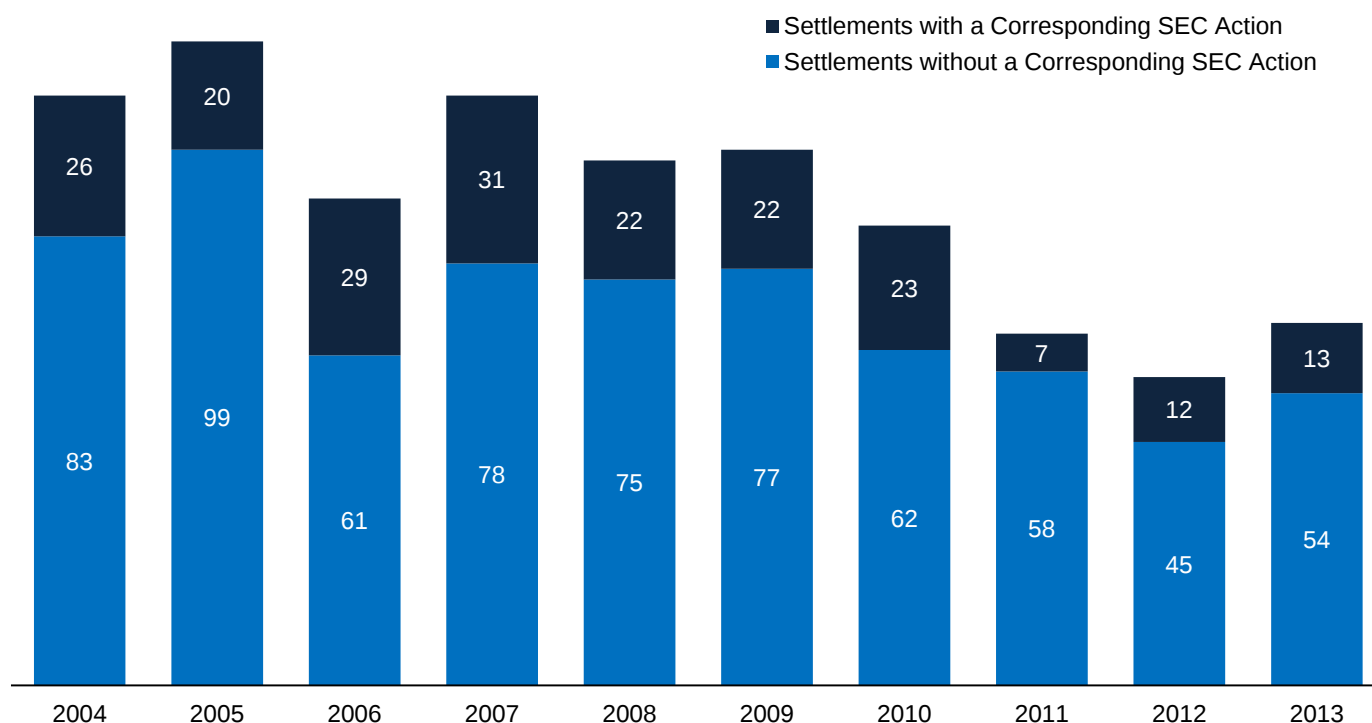
CORRESPONDING SEC ACTIONS

Cases that involve a corresponding SEC action (evidenced by the filing of a litigation release or administrative proceeding prior to the settlement of the class action) are associated with significantly higher settlement amounts and have higher settlements as a percentage of “estimated damages.”¹²

- In 2013, 19 percent of settled cases involved a corresponding SEC action, compared with 21 percent in 2012, and 23 percent of settled cases in prior post-Reform Act years.
- The median settlement for cases with an SEC action among all post-Reform Act years (\$12.9 million) was more than two times the median settlement for cases without a corresponding SEC action.
- Record enforcement activity by the SEC in 2011 and 2012 was followed by a modest decrease in 2013.¹³ SEC enforcements focus on a large scope of allegations, beyond those that may be included in the types of cases examined in this report. However, the SEC is placing sufficient emphasis on disclosure-related fraud and securities offerings such that the rate of securities class action settlements with corresponding SEC actions may increase.¹⁴

The recent decline in corresponding SEC actions may result from the reported slowdown in financial fraud investigations by the SEC during 2008–2010.

FIGURE 16: FREQUENCY OF SEC ACTIONS
2004–2013



COMPARISON OF SETTLEMENT CHARACTERISTICS BY SIZE

Several of the characteristics highlighted in this report are more prevalent for larger cases than smaller cases. For example, among the small proportion of post-Reform Act cases that settled for more than \$50 million, 63 percent had a companion derivative action and 52 percent involved a third party as a codefendant. However, for the vast majority of cases in the sample that settled for less than \$50 million, only 29 percent had a companion derivative action and only 24 percent involved a third-party as a codefendant.

- In addition, 57 percent were associated with GAAP allegations, compared with 79 percent for larger cases.
- 16 percent had a public pension as a lead plaintiff, compared with 62 percent for larger cases.

Settlements of \$50 million or lower are far less likely to involve corresponding SEC actions or public pensions as lead plaintiffs.

FIGURE 17: COMPARISON OF SETTLEMENT CHARACTERISTICS BY SIZE
2004–2013

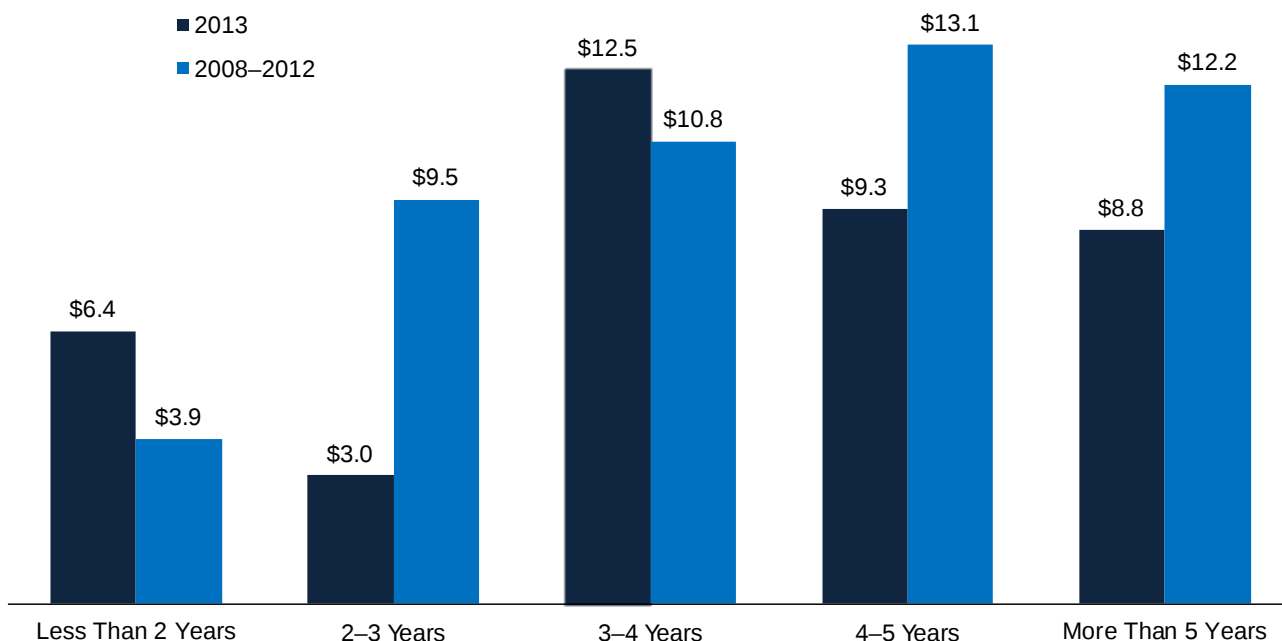
	Corresponding SEC Action	Accompanying Derivative Action	GAAP Allegations	Named Third-Party Codefendant	Public Pension as Lead Plaintiff
\$50 Million or Less	19%	29%	57%	24%	16%
More Than \$50 Million	54%	63%	79%	52%	62%

TIME TO SETTLEMENT

- Overall, the average time to reach settlement (as measured by the settlement hearing date) has been higher in recent years compared with the early post-Reform Act period.
- However, despite the longer settlement resolutions in recent years, in 2013, a substantial portion of settlements (37 percent) were resolved within 30 months of filing, the highest proportion in the past decade.
- Larger cases (as measured by “estimated damages”) and cases involving larger firms tend to take longer to reach settlement.

In 2013, the median time to settlement was 3.2 years.

**FIGURE 18: MEDIAN SETTLEMENTS BY DURATION
FROM FILING DATE TO SETTLEMENT HEARING DATE
2008–2013**
(Dollars in Millions)



LITIGATION STAGES

Advancement of cases through the litigation process may be considered an indication of the merits of a case (e.g., surviving a motion to dismiss) and/or the time and effort invested by the plaintiff counsel. This report studies three stages in the litigation process:

Stage 1: Settlement before the first ruling on a motion to dismiss

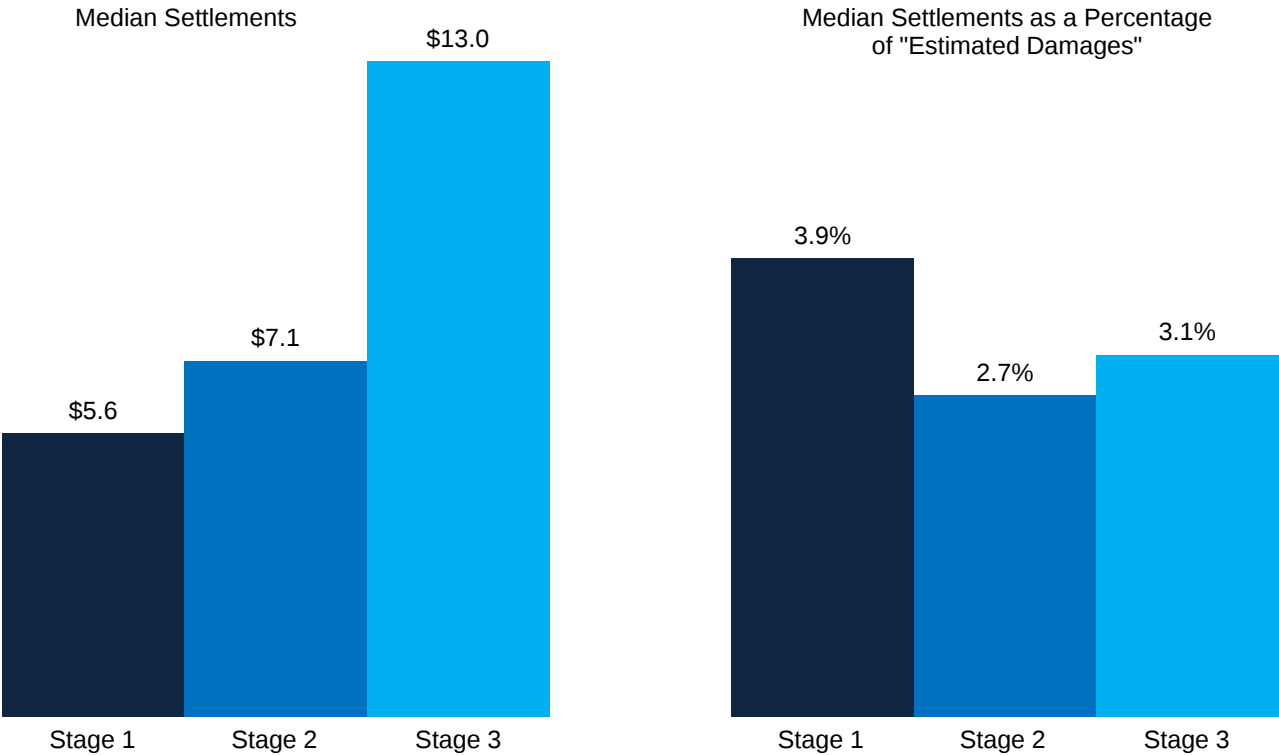
Stage 2: Settlement after a ruling on motion to dismiss, but before a ruling on motion for summary judgment

Stage 3: Settlement after a ruling on motion for summary judgment¹⁵

- Settlement amounts tend to increase as litigation progresses.
- Cases settling in Stage 1 settled for the highest percentage of “estimated damages,” while there was only a small difference in the percentage between cases settling in Stage 2 versus Stage 3.
- Larger cases tend to settle at more advanced stages of litigation and tend to take longer to reach settlement. Through 2013, cases reaching Stage 3 had median “estimated damages” of more than three and a half times the median “estimated damages” of cases settling in Stage 1.

Settlements occurring early in the litigation process have smaller “estimated damages.”

FIGURE 19: LITIGATION STAGES
1996–2013
(Dollars in Millions)



INDUSTRY SECTORS

The financial industry continues to rank the highest in median settlement value across all post-Reform Act years. However, industry sector is not a significant determinant of settlement amounts when controlling for other variables that influence settlement outcomes (such as “estimated damages,” asset size, and the presence of third-party codefendants).

- Resolution of credit crisis–related cases has comprised a large portion of settlement activity in the financial sector in recent years—22 percent of settlements in 2013, 30 percent in 2012, and 18 percent in 2011.
- The next most prevalent sectors, in terms of the number of cases settled in 2013, were pharmaceuticals (18 percent) and technology (9 percent). In comparison, pharmaceuticals and technology comprised 6 percent and 24 percent, respectively, of cases settled during 1996 through 2012.
- The shift of settled cases to the pharmaceutical sector is consistent with the larger share of filing activity in the consumer non-cyclical sector (which includes healthcare, biotechnology, and pharmaceutical companies, among others) observed in recent years.¹⁶

The proportion of settled cases involving pharmaceutical firms was higher in 2013 relative to prior years.

FIGURE 20: SETTLEMENTS BY SELECT INDUSTRY SECTORS
1996–2013
(Dollars in Millions)

Industry	Number of Settlements	Median Settlements	Median "Estimated Damages"	Median Settlements as a Percentage of "Estimated Damages"
Financial	169	\$12.5	\$575.4	3.1%
Telecommunications	141	8.0	340.6	2.4%
Pharmaceuticals	94	8.1	434.0	2.2%
Healthcare	56	6.3	212.1	3.5%
Technology	324	6.0	236.7	3.0%
Retail	117	5.8	171.0	4.3%

FEDERAL COURT CIRCUITS

- The highest concentration of settled cases in the Ninth Circuit in 2013 was in the technology and pharmaceutical sectors, each representing 9 percent of all cases. In prior post-Reform Act years, 38 percent of cases in this circuit involved technology firms, while only 6.5 percent related to pharmaceuticals.
- The number of docket entries can illustrate the complexity of a case and is correlated with the length of time from filing to settlement. Interestingly, the Second Circuit, one of the most active circuits, reports a median number of docket entries that ranks among the lowest.
- Generally, settlement approval hearings are held within four to seven months following the public announcement of a tentative settlement.

The Second and Ninth Circuits continue to lead the other circuits in number of settlements.

FIGURE 21: SETTLEMENTS BY FEDERAL COURT CIRCUIT 2009–2013

(Dollars in Millions)

Circuit	Number of Settlements	Median Number of Docket Entries	Median Duration from Tentative Settlement to Approval Hearing (in months)	Median Settlements	Median Settlements as a Percentage of "Estimated Damages"
First	11	104	7.3	\$6.0	2.7%
Second	95	123	6.5	\$11.4	2.4%
Third	34	144	5.8	\$10.1	2.4%
Fourth	14	183	4.3	\$8.8	1.8%
Fifth	19	168	5.2	\$6.5	1.6%
Sixth	16	116	4.0	\$13.6	4.1%
Seventh	22	158	4.8	\$6.2	2.5%
Eighth	8	178	5.9	\$6.5	4.0%
Ninth	110	167	6.0	\$8.0	2.3%
Tenth	9	180	6.4	\$7.5	3.4%
Eleventh	19	154	5.5	\$6.3	2.1%
DC	2	603	4.9	\$83.3	3.7%

CORNERSTONE RESEARCH'S SETTLEMENT PREDICTION ANALYSIS

Characteristics of securities cases that may affect settlement outcomes are often correlated. Regression analysis makes it possible to examine the effects of these factors simultaneously. As part of this ongoing analysis of securities class action settlements, regression analysis was applied to study factors associated with settlement outcomes. Based on this research sample of post-Reform Act cases settled through December 2013, the variables that were important determinants of settlement amounts included the following:

- “Estimated damages”
- Disclosure Dollar Loss (DDL)
- Most recently reported total assets of the defendant firm
- Number of entries on the lead case docket
- The year in which the settlement occurred
- Whether the issuer reported intentional misstatements or omissions in financial statements
- Whether a restatement of financials related to the alleged class period was announced
- Whether there was a corresponding SEC action against the issuer, other defendants, or related parties
- Whether the plaintiffs named an auditor as codefendant
- Whether the plaintiffs named an underwriter as codefendant
- Whether a companion derivative action was filed
- Whether a public pension was a lead plaintiff
- Whether noncash components, such as common stock or warrants, made up a portion of the settlement fund
- Whether the plaintiffs alleged that securities other than common stock were damaged
- Whether criminal charges/indictments were brought with similar allegations to the underlying class action
- Whether Section 11 claims accompanied Rule 10b-5 claims
- Whether the issuer traded on a nonmajor exchange

Settlements were higher when “estimated damages,” DDL, defendant asset size, or the number of docket entries were larger. Settlements were also higher in cases involving intentional misstatements or omissions in financial statements reported by the issuer, a restatement of financials, a corresponding SEC action, an underwriter and/or auditor named as codefendant, an accompanying derivative action, a public pension involved as lead plaintiff, a noncash component to the settlement, filed criminal charges, or securities other than common stock alleged to be damaged. Settlements were lower if the settlement occurred in 2004 or later, and if the issuer traded on a nonmajor exchange.

While the primary approach of these analyses is designed to better understand and predict the total settlement amount, these analyses also are able to estimate the probabilities associated with reaching alternative settlement levels. These probabilities can be useful analyses for clients in considering the different layers of insurance coverage available and likelihood of contributing to the settlement fund. Regression analysis can also be used to explore hypothetical scenarios, including but not limited to the effects on settlement amounts given the presence or absence of particular factors found to significantly affect settlement outcomes.

RESEARCH SAMPLE

- The database used in this report focuses on cases alleging fraudulent inflation in the price of a corporation's common stock (i.e., excluding cases with alleged classes of only bondholders, preferred stockholders, etc., and excluding cases alleging fraudulent depression in price).
- The sample is limited to cases alleging Rule 10b-5, Section 11, and/or Section 12(a)(2) claims brought by purchasers of a corporation's common stock. These criteria are imposed to ensure data availability and to provide a relatively homogeneous set of cases in terms of the nature of the allegations.
- The current sample includes 1,396 securities class actions filed after passage of the Reform Act (1995) and settled from 1996 through 2013. These settlements are identified based on a review of case activity collected by Securities Class Action Services LLC (SCAS).¹⁷
- The designated settlement year, for purposes of this report, corresponds to the year in which the hearing to approve the settlement was held.¹⁸ Cases involving multiple settlements are reflected in the year of the most recent partial settlement, provided certain conditions are met.¹⁹

DATA SOURCES

In addition to SCAS, data sources include Dow Jones Factiva, Bloomberg, Center for Research in Security Prices (CRSP) at University of Chicago Booth School of Business, Standard & Poor's Compustat, court filings and dockets, SEC registrant filings, SEC litigation releases and administrative proceedings, LexisNexis, and public press.

ENDNOTES

- ¹ See *Securities Class Action Filings—2013 Year in Review*, Cornerstone Research, 2014. This report, *Securities Class Action Settlements—2013 Review and Analysis*, excludes merger and acquisition cases since those cases do not meet the sample criteria.
- ² See *Investigations and Litigation Related to Chinese Reverse Merger Companies*, Cornerstone Research, 2011; and *Securities Class Action Filings—2013 Year in Review*, Cornerstone Research, 2014.
- ³ For further discussion and case details for subprime credit crisis matters, see the *D&O Diary* at www.dandodiary.com.
- ⁴ The simplified “estimated damages” model is applied to common stock only. For all cases involving Rule 10b-5 claims, damages are calculated using a market-adjusted, backward-pegged value line. For cases involving only Section 11 and/or Section 12(a)(2) claims, damages are calculated using a model that caps the purchase price at the offering price. Volume reduction assumptions are based on the exchange on which the issuer’s common stock traded. Finally, no adjustments for institutions, insiders, or short sellers are made to the underlying float.
- ⁵ Twenty settlements out of the 1,396 cases in the sample were excluded from calculations involving “estimated damages” due to stock data availability issues. The WorldCom settlement was also excluded from these calculations because most of the settlement in that matter related to liability associated with bond offerings (and this research does not compute damages related to securities other than common stock).
- ⁶ DDL captures the price reaction—using closing prices—of the disclosure that resulted in the first filed complaint. This measure does not incorporate additional stock price declines during the alleged class period that may affect certain purchasers’ potential damages claims. Thus, as this measure does not isolate movements in the defendant’s stock price that are related to case allegations, it is not intended to represent an estimate of investor losses. The DDL calculation also does not apply a model of investors’ share-trading behavior to estimate the number of shares damaged.
- ⁷ The dates used to identify the applicable inflation bands may be supplemented with information from the operative complaint at the time of settlement.
- ⁸ See *Securities Class Action Filings—2013 Year in Review*, Cornerstone Research, 2014. Annual U.S. IPO activity in 2010–2012 was significantly higher than in 2008–2009.
- ⁹ The three categories of accounting allegations analyzed in this report are: (1) GAAP violations—cases with allegations involving Generally Accepted Accounting Principles (GAAP); (2) restatements—cases involving a restatement (or announcement of a restatement) of financial statements; and (3) accounting irregularities—cases in which the defendant has reported the occurrence of accounting irregularities (intentional misstatements or omissions) in its financial statements.
- ¹⁰ This is true whether or not the settlement of the derivative action coincides with the settlement of the underlying class action, or occurs at a different time.
- ¹¹ Typically, the resolution of derivative suits lags settlement of an accompanying class action. The common practice of seeking a stay in a parallel derivative suit contributes to this lag in the resolution of derivative suits when compared with accompanying class actions.
- ¹² It could be that the merits in such cases are stronger, or simply that the presence of an accompanying SEC action provides plaintiffs with increased leverage when negotiating a settlement.
- ¹³ “SEC Announces Enforcement Results for FY 2013,” SEC press release, December 17, 2013, http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370540503617#.UrCA_tJUeul.
- ¹⁴ See Sara E. Gilley and David F. Marcus, Cornerstone Research, “The Changing Nature of SEC Enforcement Actions,” *Law360*, October 8, 2013.
- ¹⁵ Litigation stage data obtained from Stanford Law School’s Securities Class Action Clearinghouse. Sample does not add to 100 percent as there is a small sample of cases with other litigation stage classifications.
- ¹⁶ See *Securities Class Action Filings—2013 Year in Review*, Cornerstone Research, 2014.
- ¹⁷ Available on a subscription basis.
- ¹⁸ Movements of partial settlements between years can cause differences in amounts reported for prior years from those presented in earlier reports. Additionally, four cases, omitted from 2012 settlements, were added to the data sample.
- ¹⁹ This categorization is based on the timing of the settlement approval. If a new partial settlement equals or exceeds 50 percent of the then-current settlement fund amount, the entirety of the settlement amount is recategorized to reflect the settlement hearing date of the most recent partial settlement. If a subsequent partial settlement is less than 50 percent of the then-current total, the partial settlement is added to the total settlement amount and the settlement hearing date is left unchanged.

ABOUT THE AUTHORS

Laarni T. Bulan

Ph.D., Columbia University; M.Phil., Columbia University; B.S., University of the Philippines

Laarni Bulan is a manager in Cornerstone Research's Boston office, where she specializes in finance. She has consulted on cases related to financial institutions and the credit crisis, municipal bond mutual funds, merger valuations, insider trading, asset-backed commercial paper conduits, and credit default swaps. Dr. Bulan has published several academic articles in peer-reviewed journals. Her research covers topics in dividend policy, capital structure, executive compensation, corporate governance, and real options. Prior to joining Cornerstone Research, Dr. Bulan was an assistant professor of finance at the International Business School and in the economics department of Brandeis University.

Ellen M. Ryan

M.B.A., American Graduate School of International Management; B.A., Saint Mary's College

Ellen Ryan is a manager in Cornerstone Research's Boston office, where she works in the securities practice. Ms. Ryan has consulted on economic and financial issues in a variety of cases, including securities class actions, financial institution breach of contract matters, and antitrust litigation. She also has worked with testifying witnesses in corporate governance and breach of fiduciary duty matters. Prior to joining Cornerstone Research, Ms. Ryan worked for Salomon Brothers in New York and Tokyo. Currently she focuses on post-Reform Act settlement research as well as general practice area business and research.

Laura E. Simmons

Ph.D., University of North Carolina at Chapel Hill; M.B.A., University of Houston; B.B.A., University of Texas at Austin

Laura Simmons is a senior advisor in Cornerstone Research's Washington, DC, office. She is a certified public accountant (CPA) and has more than twenty years of experience in accounting practice and economic and financial consulting. She has focused on damages and liability issues in litigation, as well as on accounting issues arising in a variety of complex commercial litigation matters. She has served as a testifying expert in cases involving accounting analyses, securities case damages, research on securities lawsuits, and other issues involving empirical analyses.

Dr. Simmons's research on pre- and post-Reform Act securities litigation settlements has been published in a number of reports and is frequently cited in the public press and legal journals. She has spoken at various conferences and appeared as a guest on CNBC addressing the topic of securities case settlements. She has also published in academic journals, with recent research focusing on the intersection of accounting and litigation. Dr. Simmons was previously an accounting faculty member at the Mason School of Business at the College of William & Mary. From 1986 to 1991, she was an accountant with Price Waterhouse.

The authors acknowledge the research efforts and significant contributions of their colleagues at Cornerstone Research. Please direct any questions and requests for additional information to the settlement database administrator at settlement.database@cornerstone.com.

Many publications quote, cite, or reproduce data, charts, or tables from Cornerstone Research reports. The authors request that you reference Cornerstone Research in any reprint, quotation, or citation of the charts, tables, or data reported in this study, and include a link to the report: <http://www.cornerstone.com/Publications/Research/Post-Reform-Act-Settlements>

The views expressed in this report are solely those of the authors, who are responsible for the content, and do not necessarily represent the views of Cornerstone Research.

Boston

617.927.3000

Chicago

312.345.7300

Los Angeles

213.553.2500

Menlo Park

650.853.1660

New York

212.605.5000

San Francisco

415.229.8100

Washington

202.912.8900

www.cornerstone.com

