

# Securities Class Action Settlements

## 2014 Review and Analysis



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## HIGHLIGHTS

In 2014, total settlement dollars in securities class actions hit their lowest mark in 16 years. There was also a dramatic decrease in the average settlement amount, which reached its lowest level since 2000. At the same time, the number of settlements remained largely unchanged.

- Total settlement dollars in 2014 declined 78 percent compared to 2013 and were 84 percent below the average for the prior nine years. (page 3)
- There were 63 settlements in 2014, largely unchanged compared to the 66 settlements in 2013. (page 3)
- At \$265 million, the largest settlement in 2014 was substantially smaller than in 2013 and 2012. (page 4)
- The average settlement size dropped to \$17.0 million from \$73.5 million in 2013, while the median settlement amount (representing the typical case) declined only slightly to \$6.0 million from \$6.6 million in 2013. (page 6)
- Average “estimated damages” declined 60 percent from 2013. Since “estimated damages,” the simplified calculation analyzed for purposes of this research, are the most important factor in predicting settlement amounts, this decline contributed to the substantially lower average settlement amounts in 2014. (page 7)
- Historically, cases with third-party codefendants have settled for substantially higher amounts as a percentage of “estimated damages.” In 2014, however, cases with and without third-party defendants settled for similar percentages of “estimated damages.” (page 15)
- Average docket entry numbers fell substantially among 2014 settlements involving public pensions as lead plaintiffs. (page 19)

### FIGURE 1: SETTLEMENT STATISTICS

(Dollars in Millions)

	1996–2013	2013	2014
Minimum	\$0.1	\$0.7	\$0.3
Median	\$8.3	\$6.6	\$6.0
Average	\$57.2	\$73.5	\$17.0
Maximum	\$8,493.6	\$2,464.3	\$265.0
Total Amount	\$79,786.1	\$4,847.9	\$1,068.0

Settlement dollars adjusted for inflation; 2014 dollar equivalent figures used.

## 2014 FINDINGS: PERSPECTIVE AND DEVELOPING TRENDS

There was a dramatic decrease in average size among settlements approved in 2014, while the median settlement amount remained relatively constant. This decrease reflected a drop-off in particularly large settlements. The most important factor in explaining settlement amounts is the associated shareholder losses, referred to in this report as “estimated damages” (see page 7). Average “estimated damages” dropped sharply in 2014, while median “estimated damages” experienced an increase.

In 2014, there were fewer settlements involving “estimated damages” greater than \$1 billion and similarly, a reduced number involving “estimated damages” greater than \$5 billion, compared to prior years. Understanding the decrease in the number of large settlements requires consideration of the causes of the decline in large-damage cases.

The level of “estimated damages” depends on several factors, including the length of the associated class periods and the stock market volatility during the relevant time period. In 2014, on average, the class period length was not substantially different than prior years. However, the volatility of the stock market in recent years has been declining when compared to earlier years, which may have contributed to the smaller average “estimated damages” for cases settled in 2014.

Qualitative factors also contributed to the reduction in large settlements. A smaller proportion of large cases involved third-party defendants or public pension plans as lead plaintiffs. These factors are associated with higher settlements. Moreover, the average size of the defendant firms involved in securities class actions with large “estimated damages” (i.e., damages in excess of \$500 million) was considerably smaller than the average in recent years.

The number of securities class action filings (i.e., new cases) involving Rule 10b-5, Section 11, and/or Section 12(a)(2) allegations increased in 2014 for the second year in a row.<sup>1</sup> If there is not a marked change in case dismissal rates, it is possible there will be an increase in the overall number of cases settled in upcoming years. However, a reduction in filings of cases with large market capitalization losses in 2014<sup>2</sup> may mean that the lower level of large settlements will persist in the future.

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“Lower ‘estimated damages’ may stem from the reduced stock price volatility during the years when many of these cases were filed.”

Dr. Laura Simmons  
Cornerstone Research  
Senior Advisor

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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 2014, 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 2014, there were 63 court-approved settlements, largely unchanged from 2013.
- While the year-over-year change was small, when comparing the total number of settled cases from 2010 to 2014 to the prior five-year period (2005 to 2009), the number of settled cases declined approximately 35 percent.
  - Since cases tend to take about two to four years from filing to settlement, the reduced number of settlements over the last five years can be traced to an earlier decrease in related filings.<sup>3</sup>
  - Below-average filing rates and increasing dismissal rates in recent years have likely impacted the total number of settled cases.<sup>4</sup>
- The total value of settlements approved by courts in 2014 was \$1.1 billion, compared to an annual average of \$6.6 billion for the prior nine years.
- The low level of total settlement dollars was primarily due to fewer very large settlements compared to the prior year, rather than a shift in the typical settlement size (see Mega Settlements on page 4).

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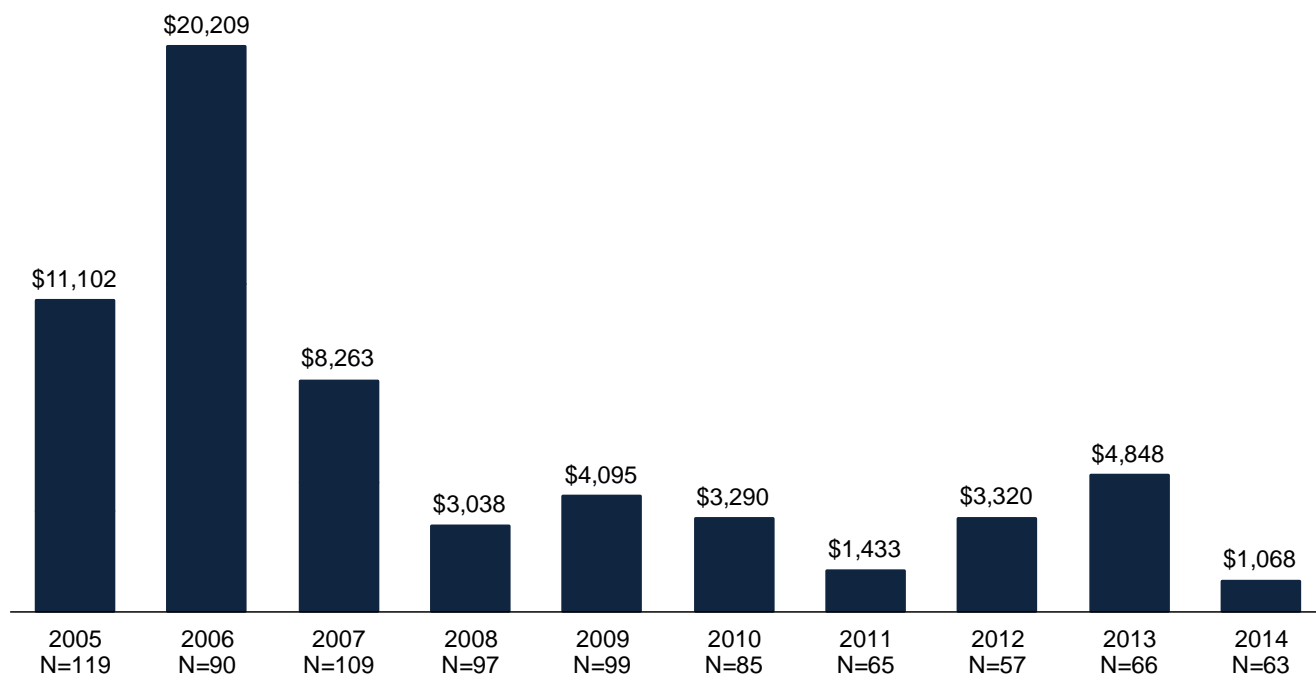
Total settlement dollars in 2014 were the lowest in 16 years.

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**FIGURE 2: TOTAL SETTLEMENT DOLLARS**

**2005–2014**

*(Dollars in Millions)*



Settlement dollars adjusted for inflation; 2014 dollar equivalent figures used.

## MEGA SETTLEMENTS

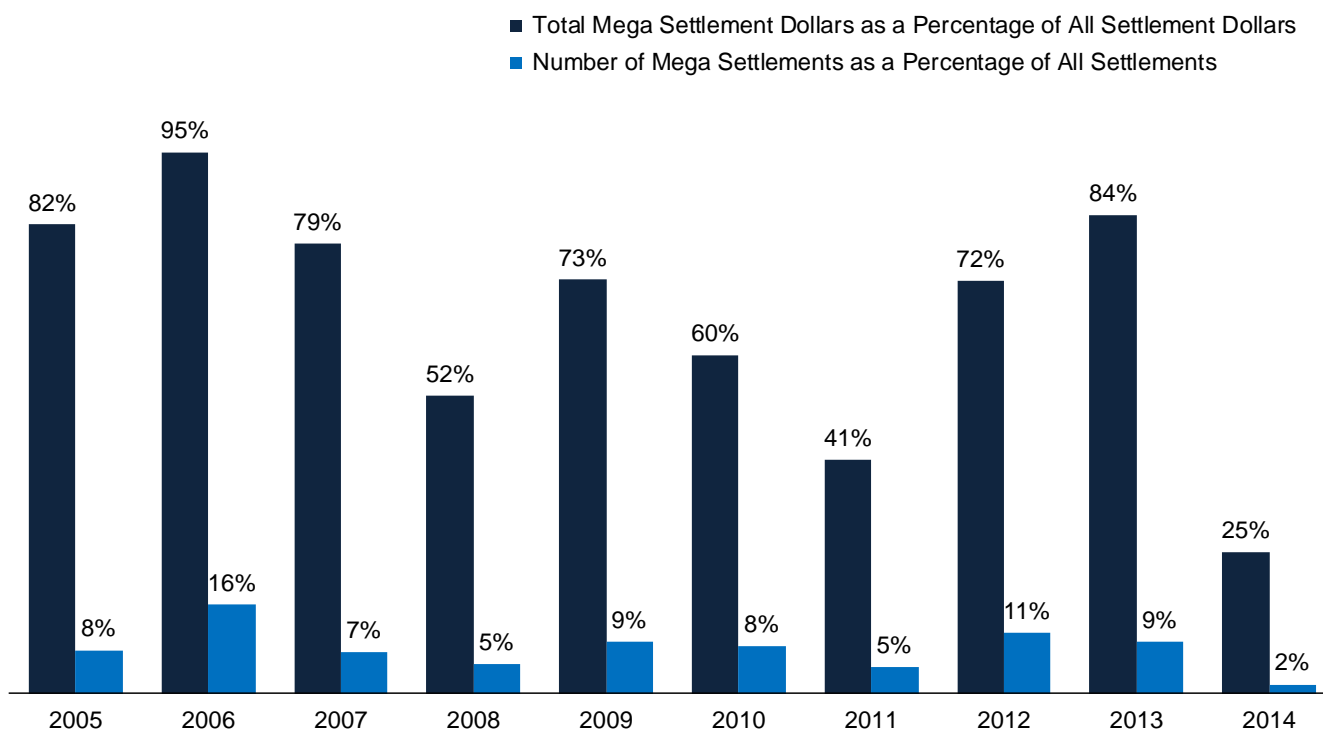
- In many years, a substantial proportion of total settlement dollars are attributable to mega settlements (settlements at or above \$100 million). In contrast, there was only one mega settlement in 2014, accounting for 25 percent of total settlement dollars, compared with six mega settlements in 2013 accounting for 84 percent of total settlement dollars.
- In the last decade, 2014 is one of only three years in which there were no cases settling for amounts in excess of \$500 million.

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In 2014, the percentage of settlement dollars from mega settlements was the lowest in 16 years.

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**FIGURE 3: MEGA SETTLEMENTS**  
2005–2014



## SETTLEMENT SIZE

- As highlighted in prior reports, the vast majority of securities class actions settle for less than \$50 million.
- In 2014, all but one of the 63 cases (98 percent) settled for less than \$100 million.
- The proportion of cases settling for \$2 million or less (often referred to as “nuisance suits”) in 2014 was 11 percent, similar to the prior nine-year period.

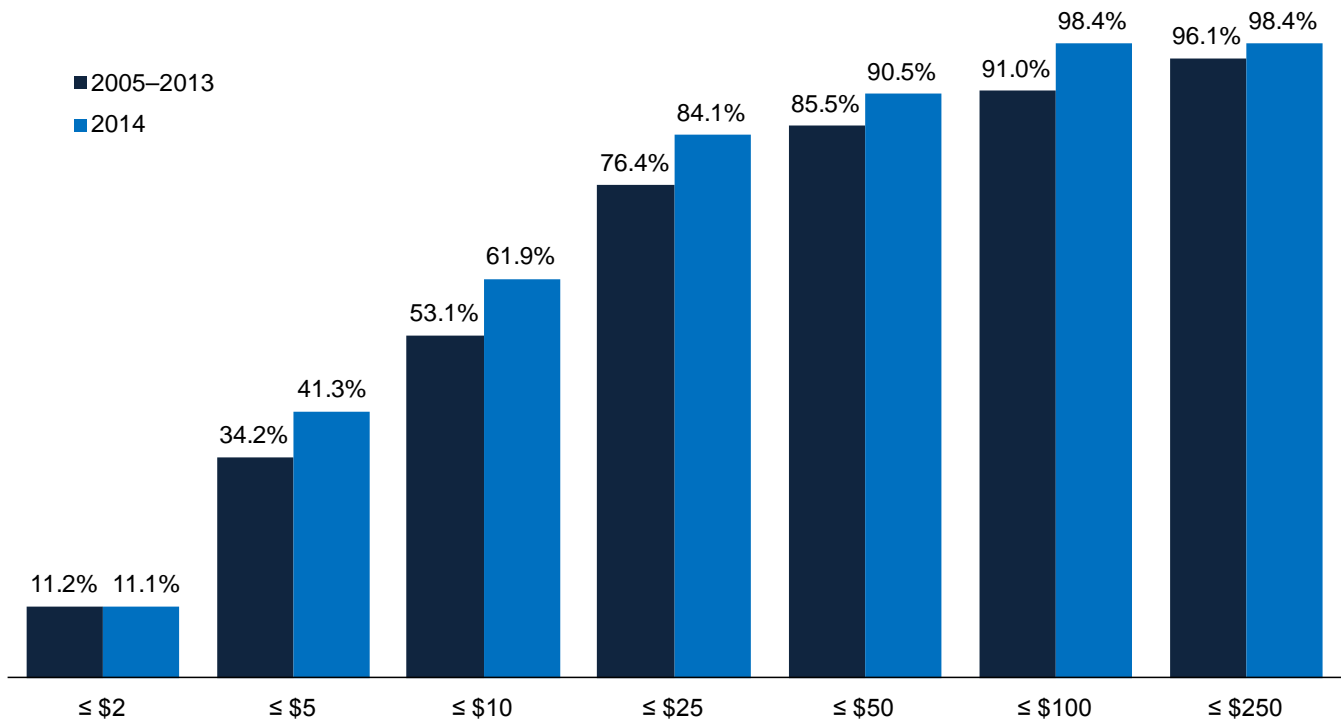
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Over 90 percent of cases in 2014 settled for less than \$50 million.

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**FIGURE 4: CUMULATIVE SETTLEMENT DISTRIBUTION 2005–2014**

*(Dollars in Millions)*



Settlement dollars adjusted for inflation; 2014 dollar equivalent figures used.



**SETTLEMENT SIZE** *continued*

- At \$17 million, the average settlement amount in 2014 was 64 percent lower than the average for all prior post–Reform Act years.
- In 2014, not only was there a sharp drop-off in the proportion of very large settlements, but there was also an increase in the proportion of settlements of \$10 million or less.
  - Approximately 62 percent of settlements in 2014 were for \$10 million or less, compared to 53 percent for 2005–2013.
  - This increase in small settlements occurred despite the fact that the proportion of settlements related to Chinese reverse merger cases dropped by half in 2014 (to 15 percent of settlements for amounts less than \$10 million). Chinese reverse merger cases have tended to settle for relatively small amounts.<sup>5</sup>

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The average settlement amount was 77 percent lower than in 2013.

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**FIGURE 5: SETTLEMENT PERCENTILES****2005–2014***(Dollars in Millions)*

Year	Average	10th	25th	Median	75th	90th
2014	\$17.0	\$1.7	\$2.9	\$6.0	\$13.2	\$39.9
2013	\$73.5	\$1.9	\$3.1	\$6.6	\$22.5	\$83.8
2012	\$58.2	\$1.3	\$2.8	\$10.5	\$36.1	\$112.4
2011	\$22.1	\$1.9	\$2.6	\$6.1	\$18.9	\$44.0
2010	\$38.7	\$2.2	\$4.6	\$12.2	\$27.1	\$86.4
2009	\$41.4	\$2.6	\$4.2	\$8.8	\$22.1	\$73.3
2008	\$31.3	\$2.2	\$4.1	\$8.8	\$20.9	\$55.4
2007	\$75.8	\$1.7	\$3.4	\$10.3	\$20.0	\$91.1
2006	\$131.6	\$2.0	\$3.7	\$8.2	\$27.3	\$268.2
2005	\$30.4	\$1.8	\$4.0	\$9.0	\$23.2	\$91.0

Settlement dollars adjusted for inflation; 2014 dollar equivalent figures used.

## DAMAGES ESTIMATES AND MARKET CAPITALIZATION LOSSES

### “ESTIMATED DAMAGES”

For purposes of this research, simplified calculations of potential shareholder losses are used, referred to here as “estimated damages.” Application of this consistent method allows for the identification and analysis of possible trends. Notably, this measure of damages is the most important factor in predicting settlement amounts. “Estimated damages” are not necessarily linked to the allegations included in the associated court pleadings.<sup>6</sup> Accordingly, the damages estimates presented in this report are not intended to be indicative of alleged economic damages incurred by shareholders.

- Average “estimated damages” in 2014 were the lowest in 12 years.
- In 2014, there were only five settlements with “estimated damages” greater than \$5 billion, compared to an annual average of nine cases for 2005–2013.
- Even after lowering the “estimated damages” threshold to \$1 billion, there was still a 24 percent decline in the number of cases in 2014 when compared to the prior nine years.
- Only three credit crisis cases settled in 2014, compared to seven in 2013 and 13 in 2012. Credit crisis cases have tended to be associated with larger “estimated damages,” and the limited number of credit crisis settlements likely contributed to the lower “estimated damages” in 2014.

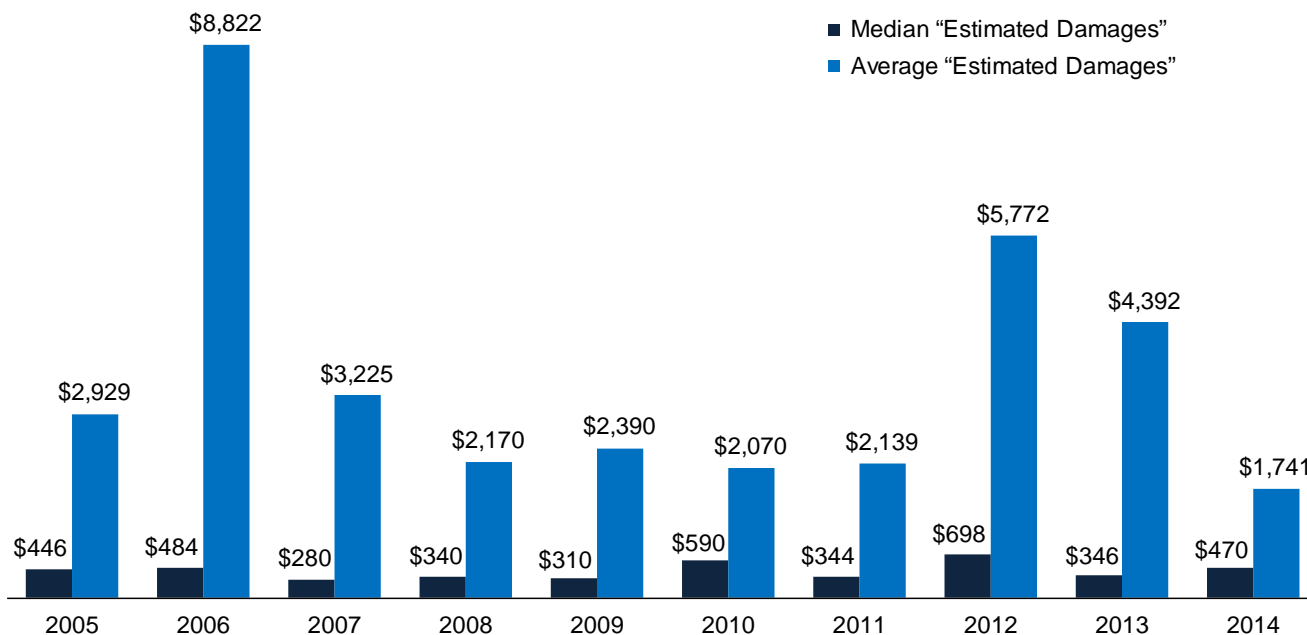
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Average “estimated damages” for 2014 declined 60 percent from 2013.

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**FIGURE 6: MEDIAN AND AVERAGE “ESTIMATED DAMAGES” 2005–2014**

(Dollars in Millions)



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

**“ESTIMATED DAMAGES”** *continued*

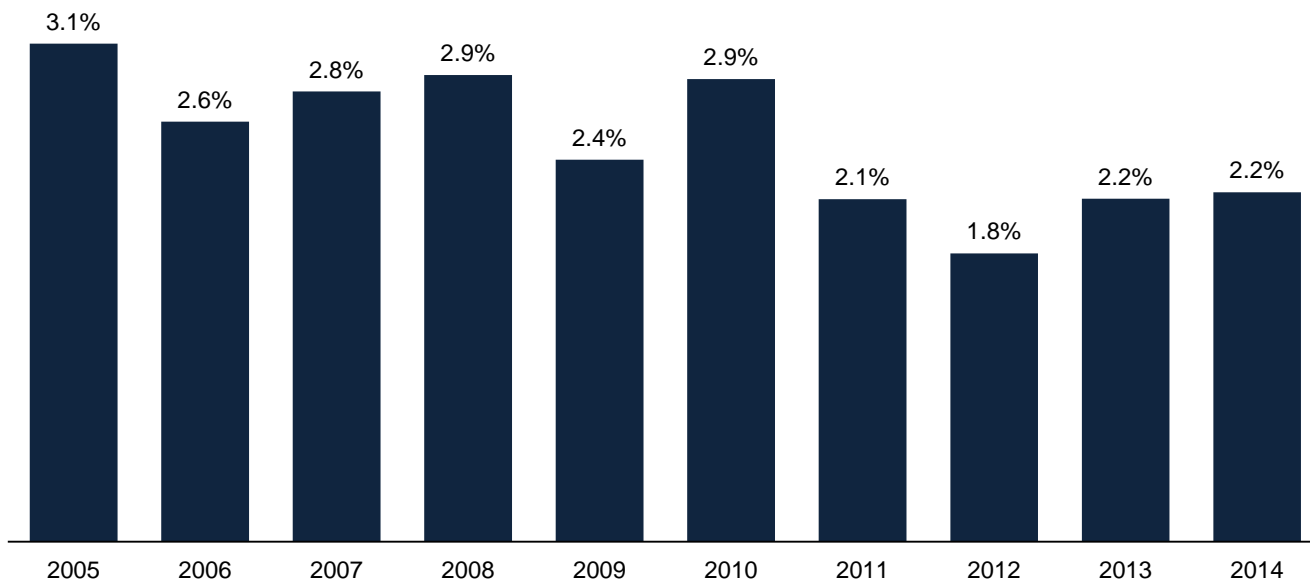
- Settlements as a percentage of “estimated damages” tend to be smaller when “estimated damages” are larger; thus, when overall “estimated damages” increase, settlements as a percentage of “estimated damages” typically decrease. In 2014, however, median “estimated damages” increased 36 percent while median settlements as a percentage of “estimated damages” were essentially flat compared to the prior year.
- These results suggest that other factors, including those discussed in the following pages, influenced median settlements as a percentage of “estimated damages” in 2014.

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Median settlements as a percentage of “estimated damages” hit a historic low in 2012, but have risen over the past two years.

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**FIGURE 7: MEDIAN SETTLEMENTS AS A PERCENTAGE OF “ESTIMATED DAMAGES” 2005–2014**



“ESTIMATED DAMAGES” *continued*

- In 2014, smaller cases continued to settle for substantially higher percentages of “estimated damages.”
- Very small cases—those with “estimated damages” of less than \$50 million—had a median settlement as a percentage of “estimated damages” of 9.9 percent, compared with 2.2 percent for all 2014 settlements.
- Among cases settled in the last 10 years, 57 percent have “estimated damages” below \$500 million and 43 percent have “estimated damages” above \$500 million.

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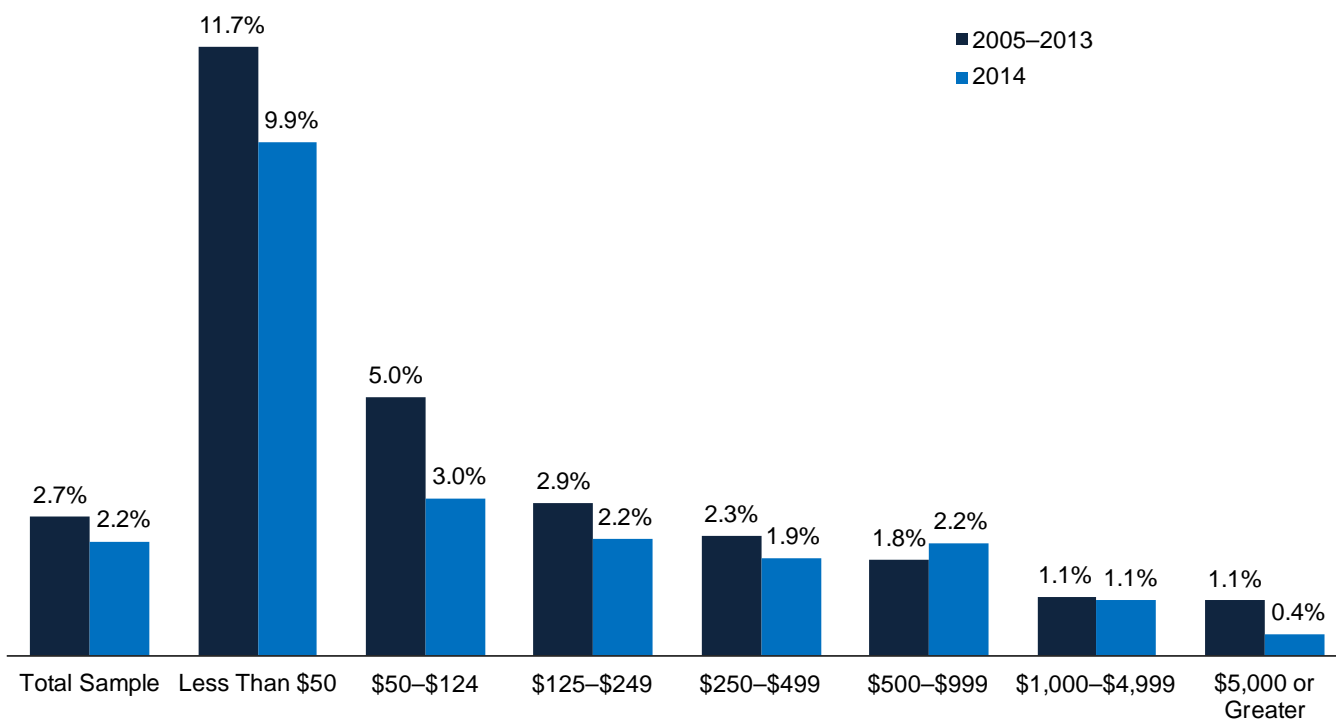
Settlements as a percentage of “estimated damages” remained below the 2005–2013 median.

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

2005–2014

(Dollars in Millions)



**“ESTIMATED DAMAGES”** *continued*

- New analysis included in this year’s report shows that for settled cases, the amount of “estimated damages” is correlated with market volatility around the time of case filing, which tends to be two to four years prior to settlement.
- NYSE and NASDAQ volatility most recently peaked in 2008. Consistent with this, “estimated damages” for settled cases filed in 2008 and 2009 were the highest since 2002.
- In recent years, market volatility has generally been trending downward, which may have contributed to the reduction in average “estimated damages” and Disclosure Dollar Loss (DDL) for cases settled in 2014 (see page 11).

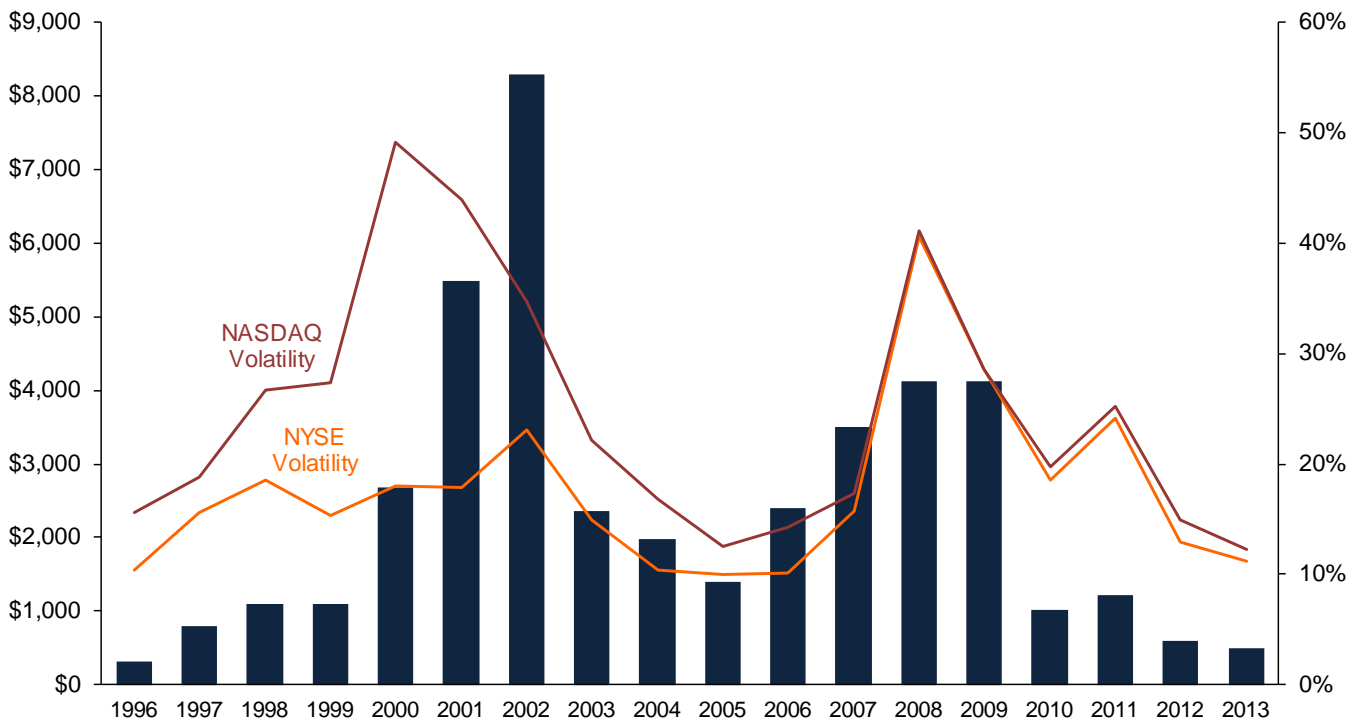
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Continued low market volatility in 2014 suggests that lower “estimated damages” may persist.

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**FIGURE 9: AVERAGE “ESTIMATED DAMAGES” FOR SETTLED CASES BY FILING YEAR 1996–2013**

(Dollars in Millions)



Note: “Estimated damages” adjusted for inflation; 2014 dollar equivalent figures used. Volatility is calculated as the annualized standard deviation of daily market returns. Chart shows filing years for settled cases through December 2014.

## DISCLOSURE DOLLAR LOSS

Disclosure Dollar Loss (DDL) is another simplified measure of potential 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.<sup>7</sup>

- Similar to the pattern observed with “estimated damages,” the average DDL declined substantially in 2014 while the median DDL increased slightly.
- In 2014, there were only three cases (5 percent) with DDL above \$2.5 billion, compared to nine (14 percent) in 2013.
- Consistent with the lower shareholder losses, as another measure of case size, issuer firms of cases settled in 2014 also had lower average assets compared to firms involved in 2013 settlements.

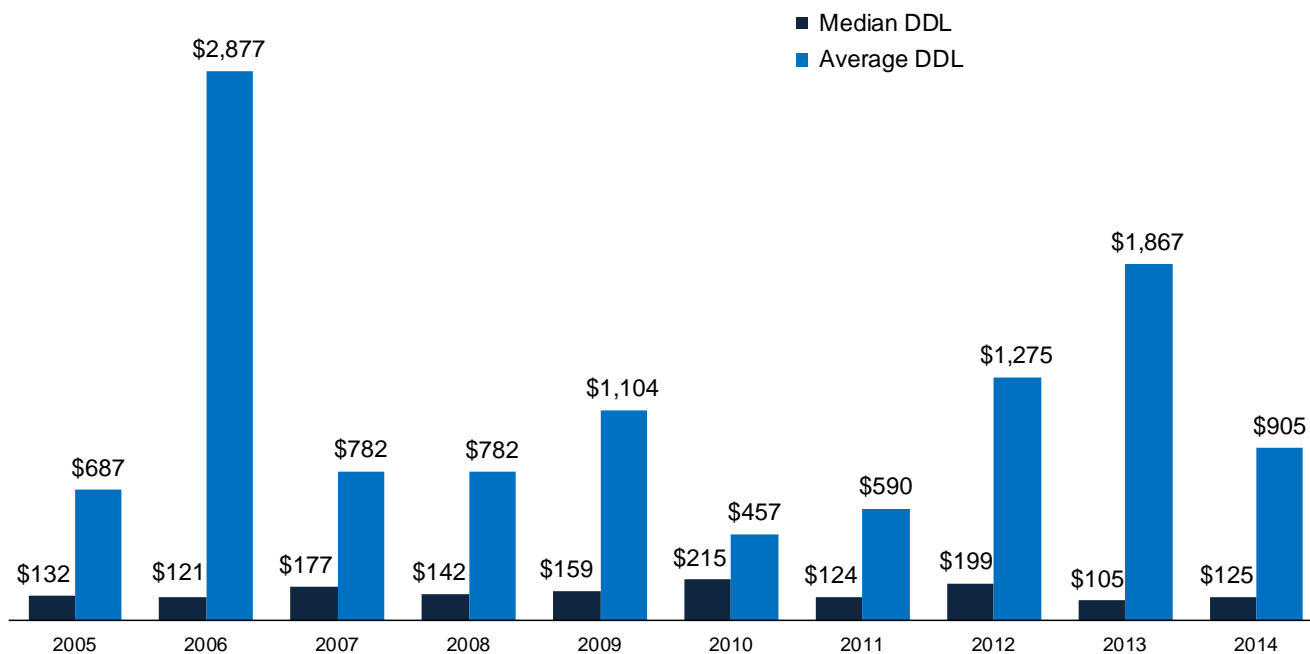
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The average DDL associated with settled cases in 2014 decreased 52 percent from 2013.

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**FIGURE 10: MEDIAN AND AVERAGE DISCLOSURE DOLLAR LOSS 2005–2014**

(Dollars in Millions)



DDL is adjusted for inflation based on class period end dates.

## TIERED ESTIMATED DAMAGES

To account for the U.S. Supreme Court's 2005 landmark decision in *Dura*, this report considers an alternative measure of damages.<sup>8</sup> This measure reflects the fact that damages cannot be associated with shares sold before information regarding the alleged fraud reaches the market.<sup>9</sup> This alternative damages measure is referred to as tiered estimated damages and is based on the stock-price drops on alleged corrective disclosure dates as described in the settlement plan of allocation.<sup>10</sup>

As noted in past reports, this measure has not yet surpassed “estimated damages” 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.

- Median settlements as a percentage of tiered estimated damages are higher than median settlements as a percentage of “estimated damages,” as tiered estimated damages are typically smaller than “estimated damages.”<sup>11</sup>
- Although the difference between the two damages measures can be substantial, their year-to-year directional trends are generally similar.

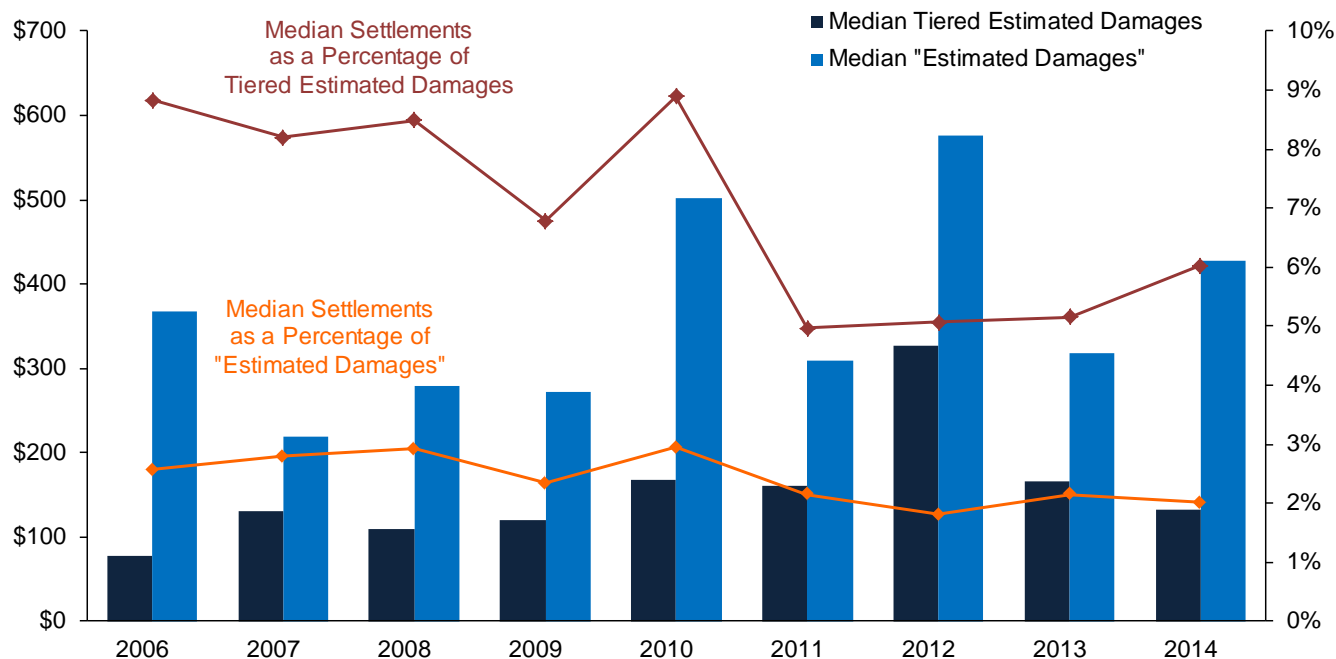
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Median tiered estimated damages are substantially lower than “estimated damages.”

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**FIGURE 11: TIERED ESTIMATED DAMAGES 2006–2014**

(Dollars in Millions)



## ANALYSIS OF SETTLEMENT CHARACTERISTICS

### NATURE OF CLAIMS

- In 2014, there were only three cases involving Section 11 and/or Section 12(a)(2) claims that did not involve Rule 10b-5 allegations. There were seven cases in 2014 that involved Section 11 and/or Section 12(a)(2) claims, in addition to Rule 10b-5 claims.
- Intensified activity in the U.S. IPO market in recent years has occurred in tandem with the increase in filings involving Section 11 claims.<sup>12</sup> This suggests that settlements of cases involving these claims are likely to be more prevalent in future years.
- 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.

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

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### FIGURE 12: SETTLEMENTS BY NATURE OF CLAIMS

1996–2014

(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	83	\$3.9	\$60.4	7.3%
Both Rule 10b-5 and Section 11 and/or 12(a)(2)	253	\$13.8	\$529.9	3.4%
Rule 10b-5 Only	1,102	\$8.0	\$368.3	2.8%
All Post-Reform Act Settlements	1,438	\$8.2	\$336.6	3.1%

Settlement dollars and “estimated damages” adjusted for inflation; 2014 dollar equivalent figures used. “Estimated damages” are adjusted for inflation based on class period end dates.



## ACCOUNTING ALLEGATIONS

This research examines three types of accounting allegations among settled cases: (1) alleged GAAP violations, (2) restatements, and (3) reported accounting irregularities.<sup>13</sup>

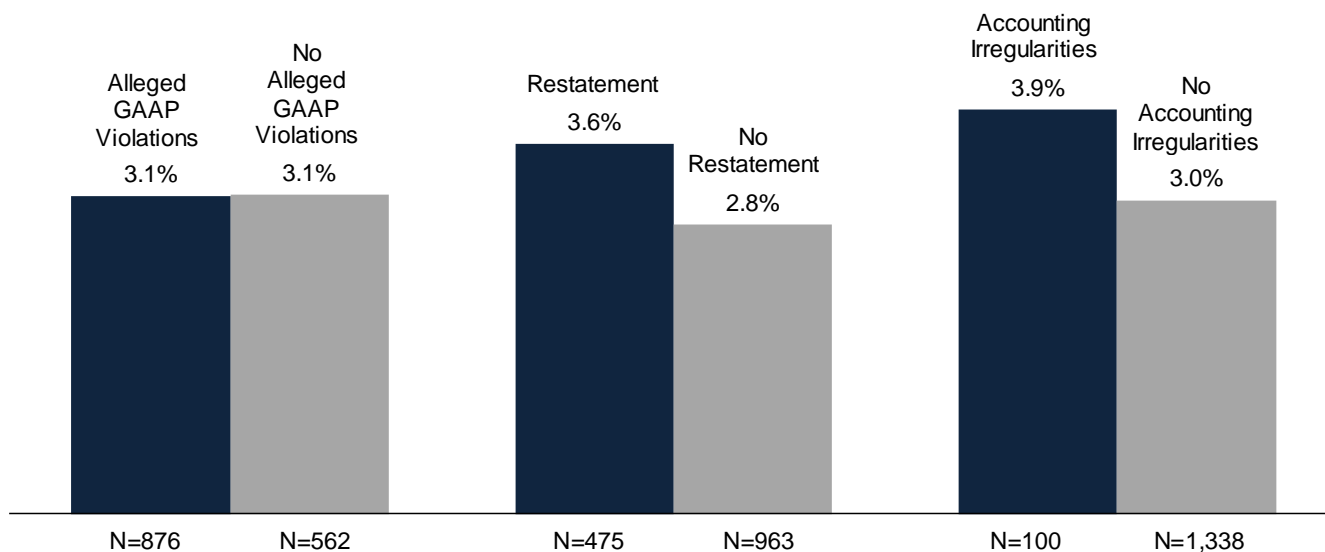
- In 2014, 67 percent of settled cases alleged GAAP violations, representing a slight increase over the rate of 61 percent for all prior post-Reform Act years.
- The median class period length for cases with GAAP allegations is nearly twice as long as for cases without such allegations.
- Restatements were involved in 29 percent of cases settled in 2014 and were associated with higher settlements as a percentage of “estimated damages” compared to cases not involving restatements.
- Of the cases approved for settlement in 2014, 8 percent involved reported accounting irregularities, which is within the range of previous years. These cases continued to settle for the highest amounts in relation to “estimated damages.”

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Cases involving accounting allegations are generally associated with higher settlement amounts and higher settlements as a percentage of “estimated damages.”

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**FIGURE 13: MEDIAN SETTLEMENTS AS A PERCENTAGE OF “ESTIMATED DAMAGES” AND ACCOUNTING ALLEGATIONS 1996–2014**



### THIRD-PARTY CODEFENDANTS

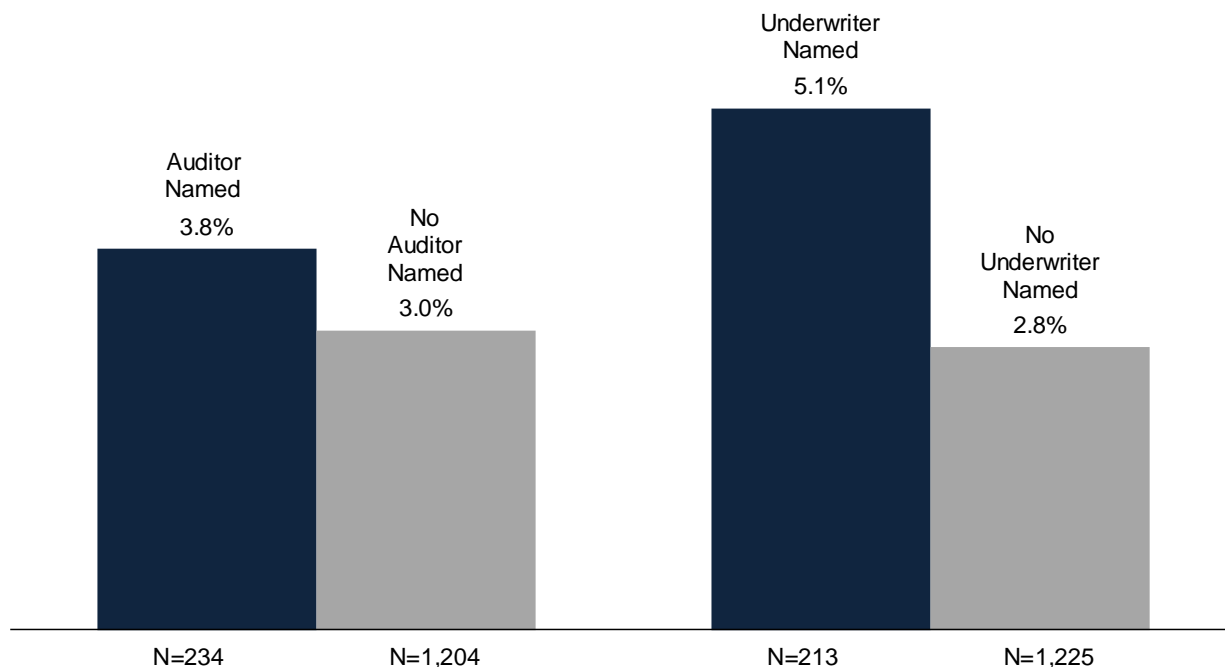
- Third parties, such as an auditor or an underwriter, are often named as codefendants in larger, more complex cases and can provide an additional source of settlement funds.
- Historically, cases with third-party codefendants have settled for substantially higher amounts as a percentage of “estimated damages.” In 2014, however, cases with and without third-party defendants settled for similar percentages of “estimated damages.”
- In 2014, 21 percent of cases with alleged GAAP violations had a named auditor defendant, while 70 percent of cases with Section 11 claims had a named underwriter defendant.

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Outside auditor defendants are typically associated with cases involving GAAP violations; underwriter defendants are highly correlated with Section 11 claims.

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**FIGURE 14: MEDIAN SETTLEMENTS AS A PERCENTAGE OF “ESTIMATED DAMAGES” AND THIRD-PARTY CODEFENDANTS 1996–2014**



## INSTITUTIONAL INVESTORS

- Since 2006, more than half of the settlements in any given year have involved institutional investors as lead plaintiffs. In 2014, 63 percent of cases approved for settlement had lead plaintiffs that were institutional investors.
- The median settlement in 2014 for cases with a public pension as a lead plaintiff was \$13 million, compared with \$5 million for cases without a public pension as a lead plaintiff.
- In 2014, 52 percent of settlements with “estimated damages” greater than \$500 million involved a public pension plan as lead plaintiff, compared to 24 percent for cases with “estimated damages” of \$500 million or less.

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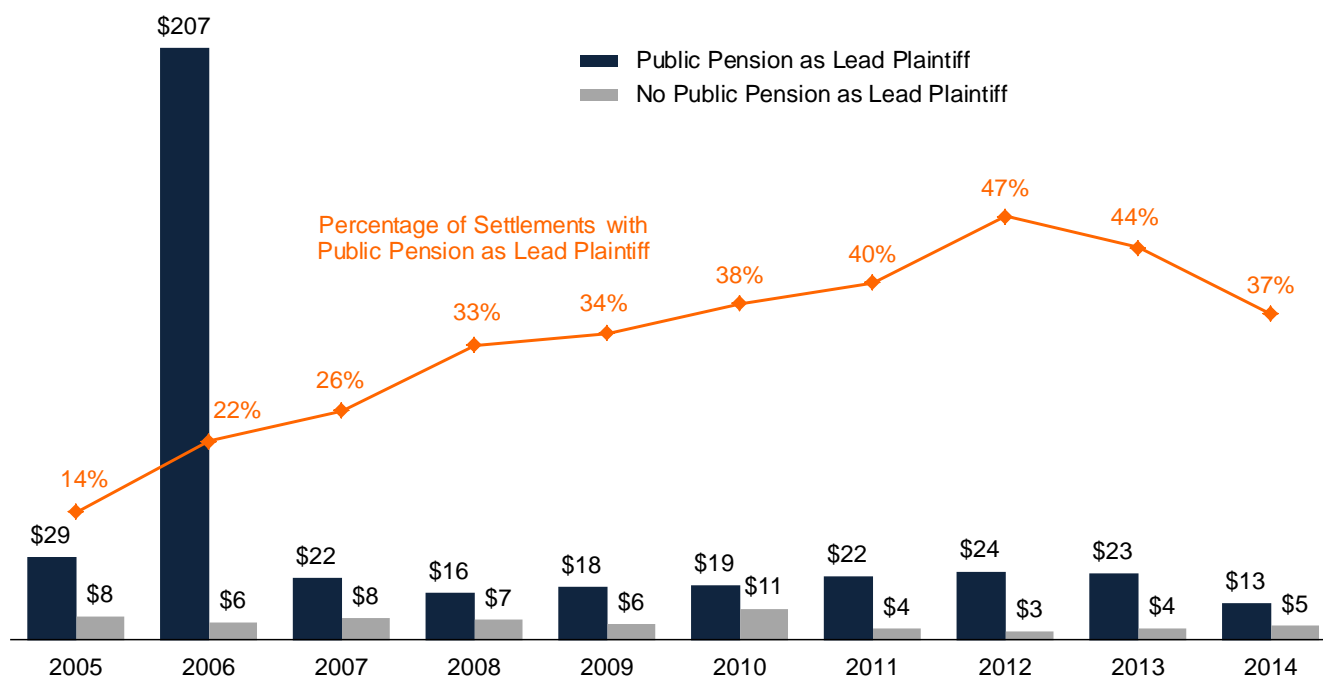
The increasing involvement of public pensions as lead plaintiffs reversed in 2013 and further declined in 2014.

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**FIGURE 15: MEDIAN SETTLEMENT AMOUNTS AND PUBLIC PENSIONS**

2005–2014

(Dollars in Millions)



Settlement dollars adjusted for inflation; 2014 dollar equivalent figures used.

## DERIVATIVE ACTIONS

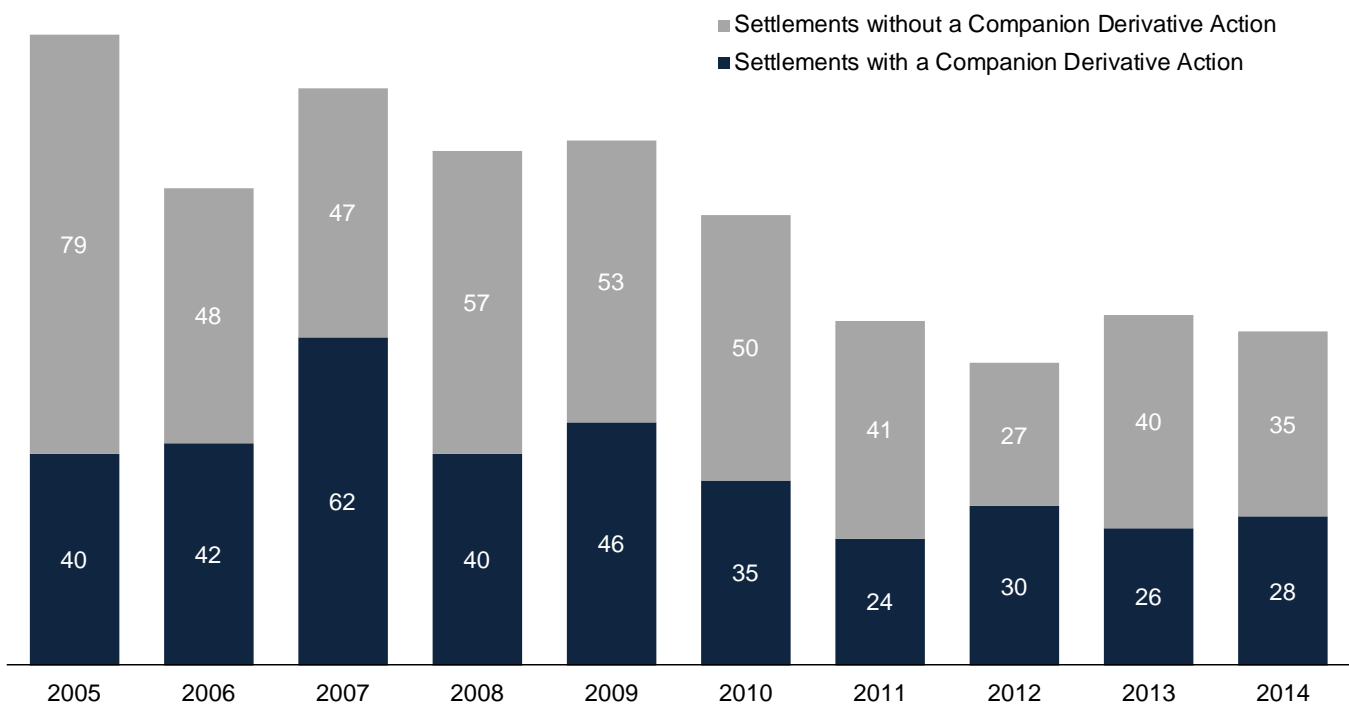
- Historically, accompanying derivative actions have been associated with larger securities class actions compared to smaller cases.<sup>14</sup> In 2014, this gap narrowed—48 percent of cases with “estimated damages” of more than \$500 million involved a companion derivative action, compared to 41 percent for cases with damages of \$500 million or less.
- In 2014, the median settlement for cases with an accompanying derivative action was 31 percent higher than for cases without an accompanying derivative action. In 2013, this difference was 78 percent while in 2012, it was 387 percent.
- Overall, 44 percent of settled cases in 2014 were accompanied by derivative actions—similar to prior years.

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Companion derivative actions continued to be associated with higher class action settlements.

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**FIGURE 16: FREQUENCY OF DERIVATIVE ACTIONS 2005–2014**



## CORRESPONDING SEC ACTIONS

Cases that involve a corresponding SEC action (evidenced by the filing of a litigation release or administrative proceeding prior to settlement) are associated with significantly higher settlement amounts and have higher settlements as a percentage of “estimated damages.”<sup>15</sup>

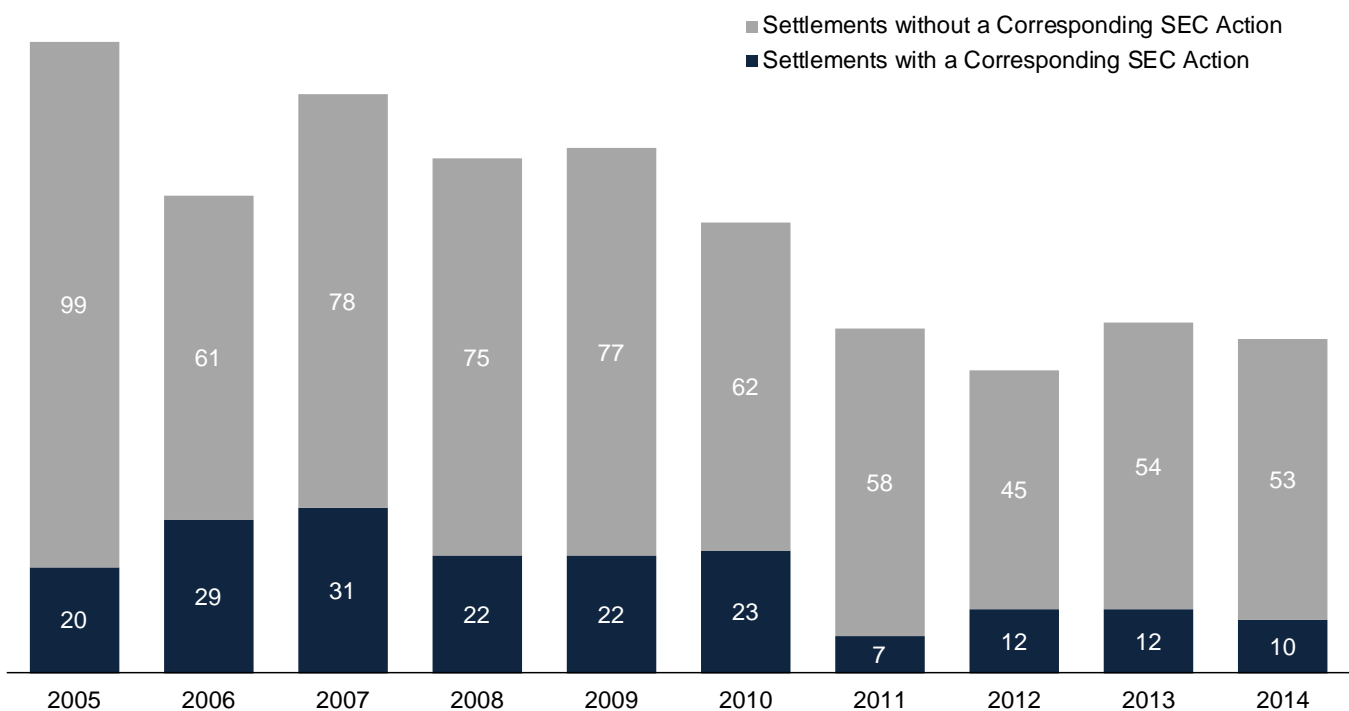
- In 2014, 16 percent of settled cases involved a corresponding SEC action, compared with 18 percent in 2013 and 21 percent in 2012.
- The median settlement for all post–Reform Act cases with an SEC action (\$12.9 million) was more than twice the median settlement for cases without a corresponding SEC action.
  - In 2014, the median settlement for cases with an SEC action was \$9.4 million, while cases without an associated SEC action had a median settlement of \$5.5 million.
  - In 2014, institutional investors were involved as lead plaintiffs in seven of the 10 cases with a corresponding SEC action.
- The higher settlement amounts for cases involving corresponding SEC actions are, in part, due to the fact that among securities cases that have settled, SEC actions more frequently accompany larger cases, as measured by issuer asset-size and higher “estimated damages.”

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The number of settlements with corresponding SEC actions remained relatively low in 2014.

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**FIGURE 17: FREQUENCY OF SEC ACTIONS  
2005–2014**



## TIME TO SETTLEMENT AND CASE COMPLEXITY

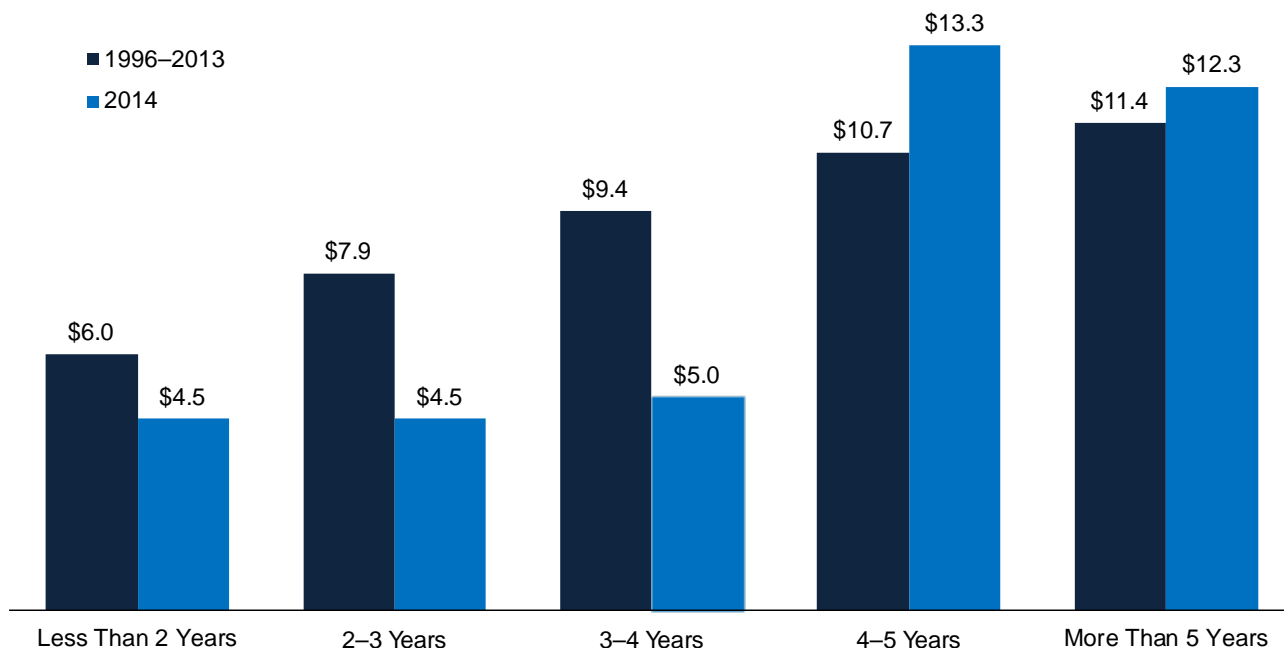
- In 2014, the median and average time to settlement was three years.
- Larger cases (as measured by “estimated damages”) and cases involving larger firms tend to take longer to reach settlement.
- The length of time from filing to settlement is correlated with the number of docket entries—a measure of the complexity of a case and the case’s progression through the litigation process.
  - In 2014, the average number of docket entries (both in absolute figures and scaled by the time from filing to settlement) was among the lowest in 10 years. In other words, even controlling for the length of time that cases were outstanding prior to settlement, the number of docket entries dropped in 2014, indicating reduced activity for cases prior to settlement.
  - For cases involving a public pension as a lead plaintiff, average docket entries were down approximately 40 percent in 2014 when compared to the prior nine years.
  - Despite the observable decline in docket entries, fewer cases in 2014 settled in very early stages of the litigation process.

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Approximately 70 percent of settlements in 2014 occurred two to four years after the filing date.

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**FIGURE 18: MEDIAN SETTLEMENT BY DURATION FROM FILING DATE TO SETTLEMENT HEARING DATE 1996–2014**  
 (Dollars in Millions)



## LITIGATION STAGES

This report studies three stages in the litigation process that 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 plaintiff counsel:

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 judgment<sup>16</sup>

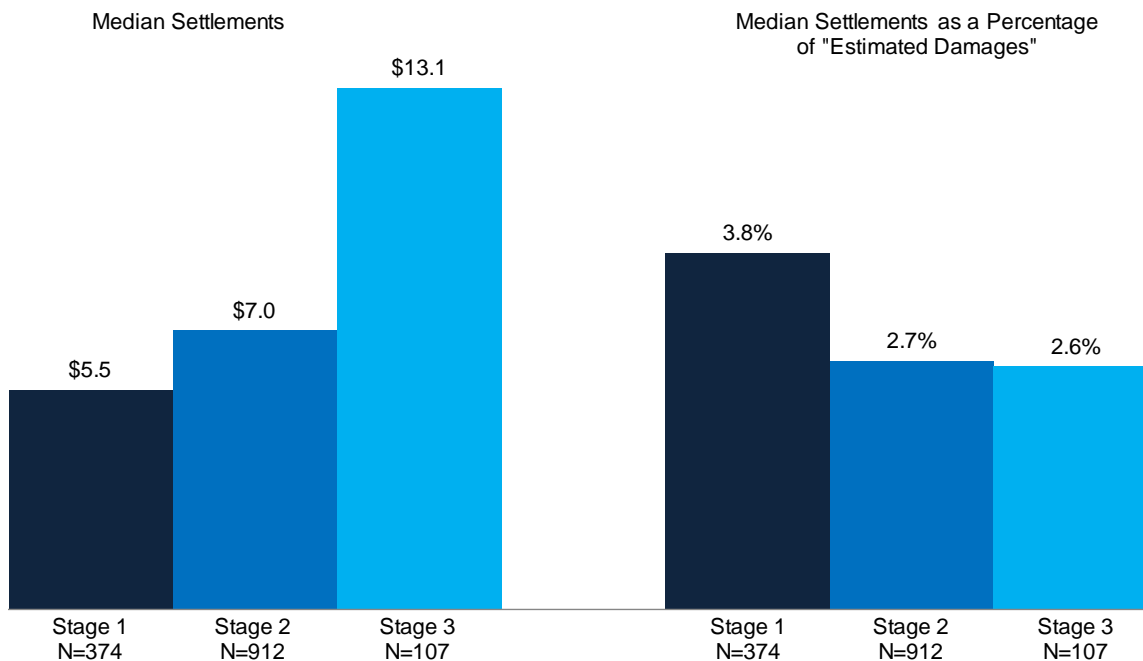
- In 2014, only 19 percent of settlements occurred in Stage 1, compared to 27 percent for cases settled in 1996–2013.
- Although smaller in total settlement dollar amounts, cases settling in Stage 1 have settled for the highest percentage of “estimated damages.”
- Larger cases tend to settle at more advanced stages of litigation and tend to take longer to reach settlement. Through 2014, cases reaching Stage 3 had median “estimated damages” that were 75 percent higher than the median “estimated damages” of cases settling in Stage 1.

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Settlement amounts tend to increase as litigation progresses.

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**FIGURE 19: LITIGATION STAGE**  
**1996–2014**  
*(Dollars in Millions)*



## INDUSTRY SECTORS

Resolution of credit crisis–related cases has constituted a large portion of settlement activity in the financial sector in recent years. However, filing of securities class actions involving credit crisis issues essentially ceased by 2012.<sup>17</sup> Accordingly, the majority of these cases have now progressed through the litigation process, resulting in a reduction in settlements involving financial firms in 2014.

- Only seven settled cases (11 percent) in 2014 involved financial firms compared to 15 (23 percent) in 2013 and 17 (30 percent) in 2012.
- Reflecting their larger “estimated damages,” cases in the financial sector have settled for the highest amounts.
- The proportion of settled cases involving pharmaceutical firms declined to 9.5 percent in 2014 from a historic high of 18 percent in 2013.
- 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 other factors discussed on page 23).

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The proportion of settled cases in 2014 involving financial firms is the lowest in seven years.

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**FIGURE 20: SELECT INDUSTRY SECTORS**

**1996–2014**

*(Dollars in Millions)*

Industry	Number of Settlements	Median Settlements	Median "Estimated Damages"	Median Settlements as a Percentage of "Estimated Damages"
Technology	332	\$7.7	\$323.3	3.0%
Financial	176	\$13.2	\$742.0	3.0%
Telecommunications	143	\$9.4	\$494.9	2.4%
Retail	123	\$6.8	\$237.7	4.1%
Pharmaceuticals	100	\$9.4	\$591.4	2.2%
Healthcare	59	\$7.9	\$282.1	3.5%

Settlement dollars and “estimated damages” adjusted for inflation; 2014 dollar equivalent figures used. “Estimated damages” are adjusted for inflation based on class period end dates.



## FEDERAL COURT CIRCUITS

- In 2014, the Second and Ninth Circuits continued to lead other circuits in the number of settlements.
- While activity levels have stayed relatively constant in the Second and Ninth Circuits over the last decade, other federal court circuits have experienced a decline of more than 50 percent in the number of securities class action settlements.
- Although it varies across court circuit, settlement approval hearings are generally held within four to eight months following the public announcement of a tentative settlement.

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**48 percent of settlements occurred in the Second or Ninth Circuits in 2014.**

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**FIGURE 21: SETTLEMENTS BY FEDERAL COURT CIRCUIT 2005–2014**

(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	38	131	6.4	\$7.1	2.8%
Second	197	108	6.5	\$11.9	2.6%
Third	77	123	6.1	\$8.9	2.8%
Fourth	29	127	4.3	\$8.6	2.0%
Fifth	62	112	5.3	\$6.5	2.3%
Sixth	41	142	4.4	\$18.2	2.7%
Seventh	42	151	5.2	\$10.5	2.2%
Eighth	29	165	5.9	\$14.6	3.6%
Ninth	217	162	6.3	\$8.2	2.4%
Tenth	28	170	7.6	\$8.2	2.0%
Eleventh	67	132	5.5	\$5.7	2.6%
DC	4	190	6.5	\$31.1	3.7%

Settlement dollars adjusted for inflation; 2014 dollar equivalent figures used.

## CORNERSTONE RESEARCH'S SETTLEMENT PREDICTION ANALYSIS

Regression analysis was applied to examine which characteristics of securities cases were associated with settlement outcomes. Based on the research sample of post-Reform Act cases settled through December 2014, the factors 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 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 this regression analysis is designed to better understand and predict the total settlement amount given the characteristics of a particular securities case, the probabilities associated with reaching alternative settlement levels can also be estimated. These probability estimates can be useful 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 M&A cases).
- 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 1,458 securities class actions filed after passage of the Reform Act (1995) and settled from 1996 through 2014. These settlements are identified based on a review of case activity collected by Securities Class Action Services LLC (SCAS).<sup>18</sup>
- The designated settlement year, for purposes of this report, corresponds to the year in which the hearing to approve the settlement was held.<sup>19</sup> Cases involving multiple settlements are reflected in the year of the most recent partial settlement, provided certain conditions are met.<sup>20</sup>

## DATA SOURCES

In addition to SCAS, data sources include the Stanford Law School Securities Class Action Clearinghouse, 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—2014 Year in Review](#), Cornerstone Research, 2015.
- 2 *Ibid.*
- 3 “Related filings” refers to case types covered in the scope of this report as described on page 24.
- 4 See [Securities Class Action Filings—2014 Year in Review](#), Cornerstone Research, 2015.
- 5 See [Investigations and Litigation Related to Chinese Reverse Merger Companies](#), Cornerstone Research, 2011
- 6 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.
- 7 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.
- 8 Tiered estimated damages are calculated for cases that settled after 2005.
- 9 Tiered estimated damages utilize a single value line when there is 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.
- 10 The dates used to identify the applicable inflation bands may be supplemented with information from the operative complaint at the time of settlement.
- 11 Tiered estimated damages apply inflation bands to specific date intervals during the alleged class period. As such, this measure does not capture all declines during the alleged class period as “estimated damages” does.
- 12 See [Securities Class Action Filings—2014 Year in Review](#), Cornerstone Research, 2015.
- 13 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.
- 14 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.
- 15 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.
- 16 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.
- 17 See [Securities Class Action Filings—2014 Year in Review](#), Cornerstone Research, 2015.
- 18 Available on a subscription basis.
- 19 Movements of partial settlements between years can cause differences in amounts reported for prior years from those presented in earlier reports.
- 20 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 senior 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, real estate markets, credit default swaps, and foreign exchange. 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 had a joint appointment at Brandeis University as an assistant professor of finance in its International Business School and in the economics department.

### **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 20 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](mailto:settlement.database@cornerstone.com).

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**Boston**

617.927.3000

**Chicago**

312.345.7300

**London**

+44.20.3655.0900

**Los Angeles**

213.553.2500

**Menlo Park**

650.853.1660

**New York**

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**San Francisco**

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