



# Securities Litigation

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Fifth Annual Capital Matters: Managing Labor's Capital Conference (Pensions and Capital Stewardship Project, Harvard Law School)

Professor Michael A. Perino  
St. John's University School of Law



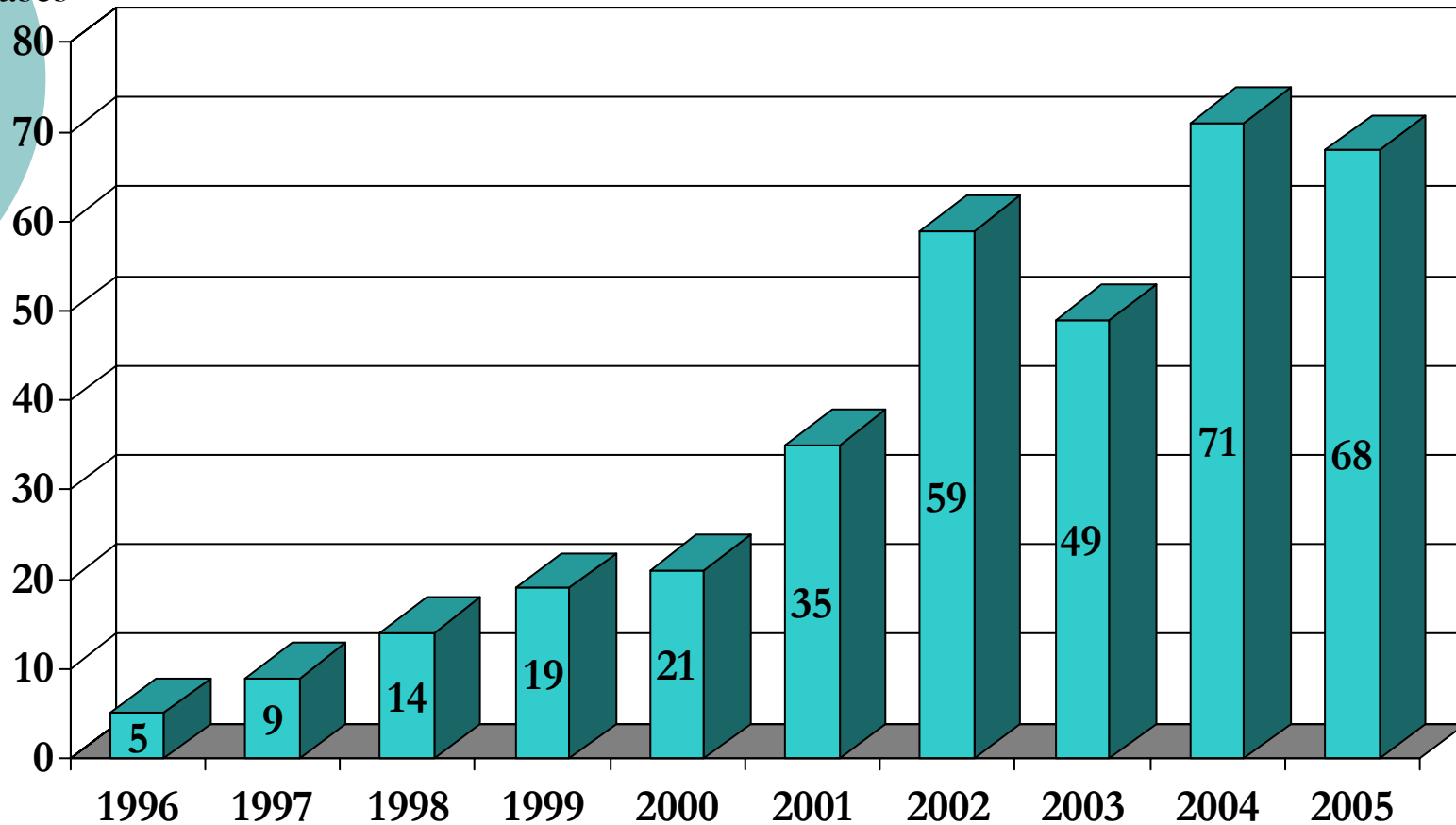
# The PSLRA and the Institutional Investor

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- Congress created lead plaintiff provision to encourage institutional investors to monitor class counsel
- Are institutional investors effective monitors?

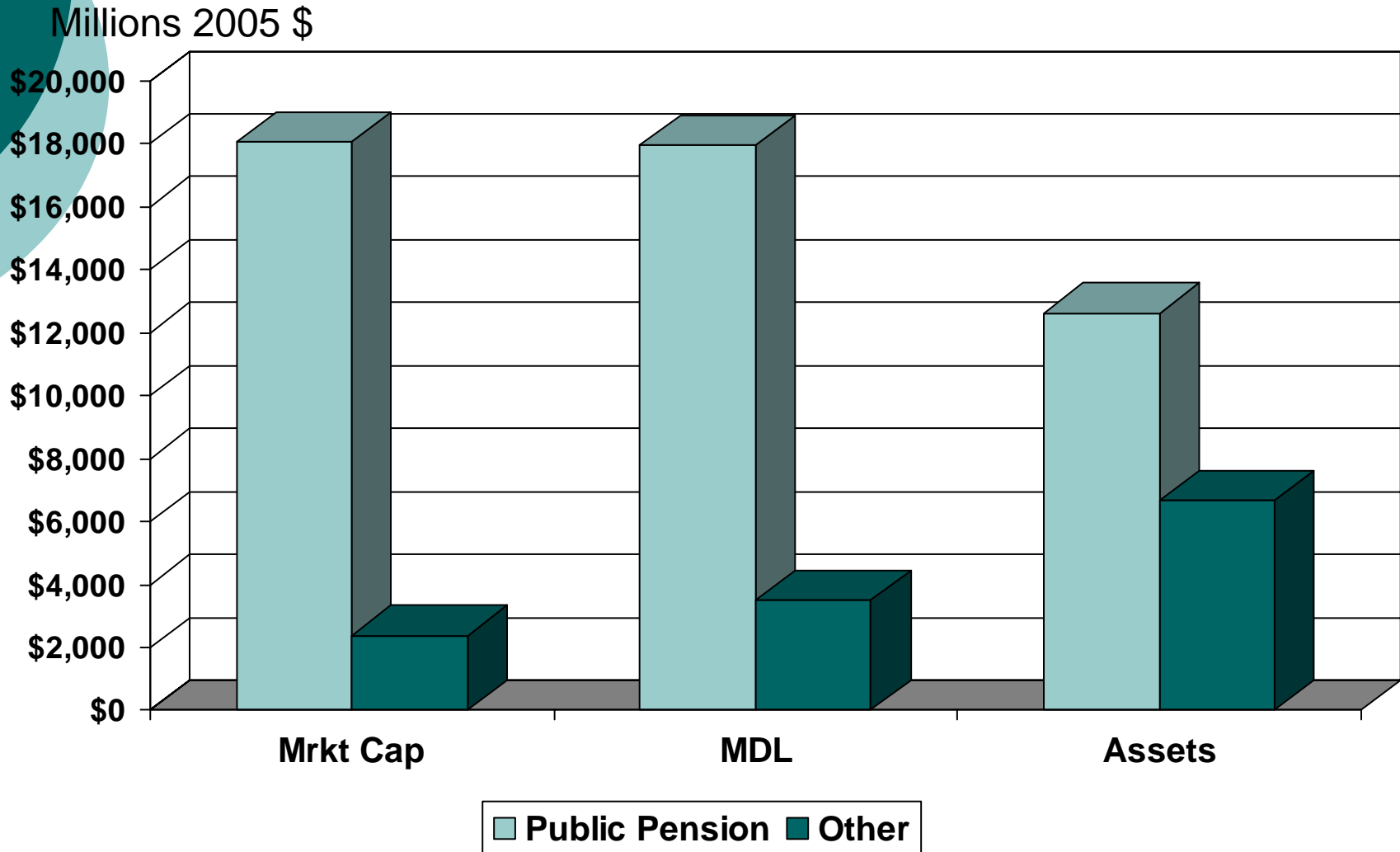
# Cases with Public Pension Funds or Unions as Lead Plaintiffs

No. Cases

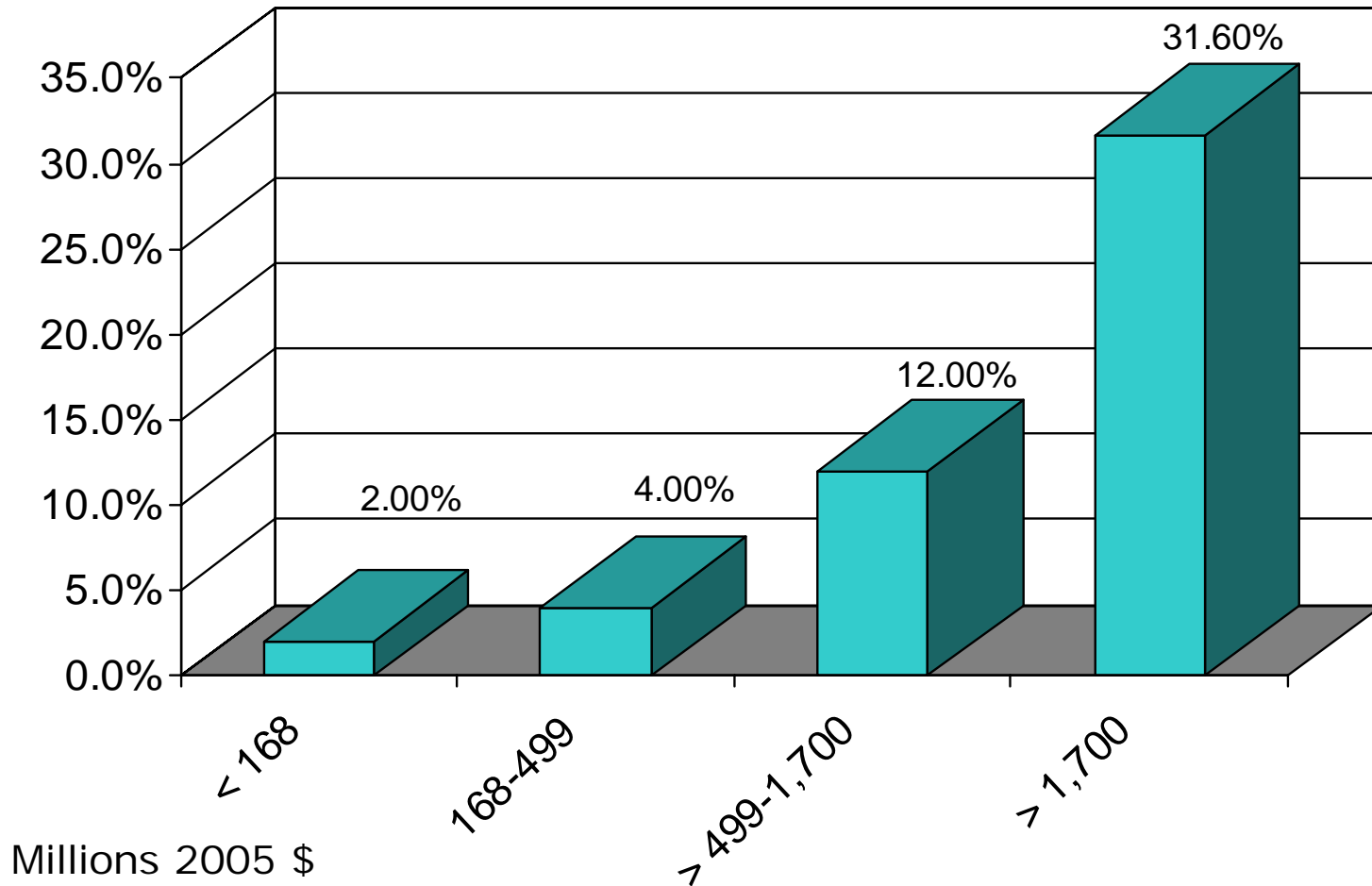


Source: PricewaterhouseCoopers

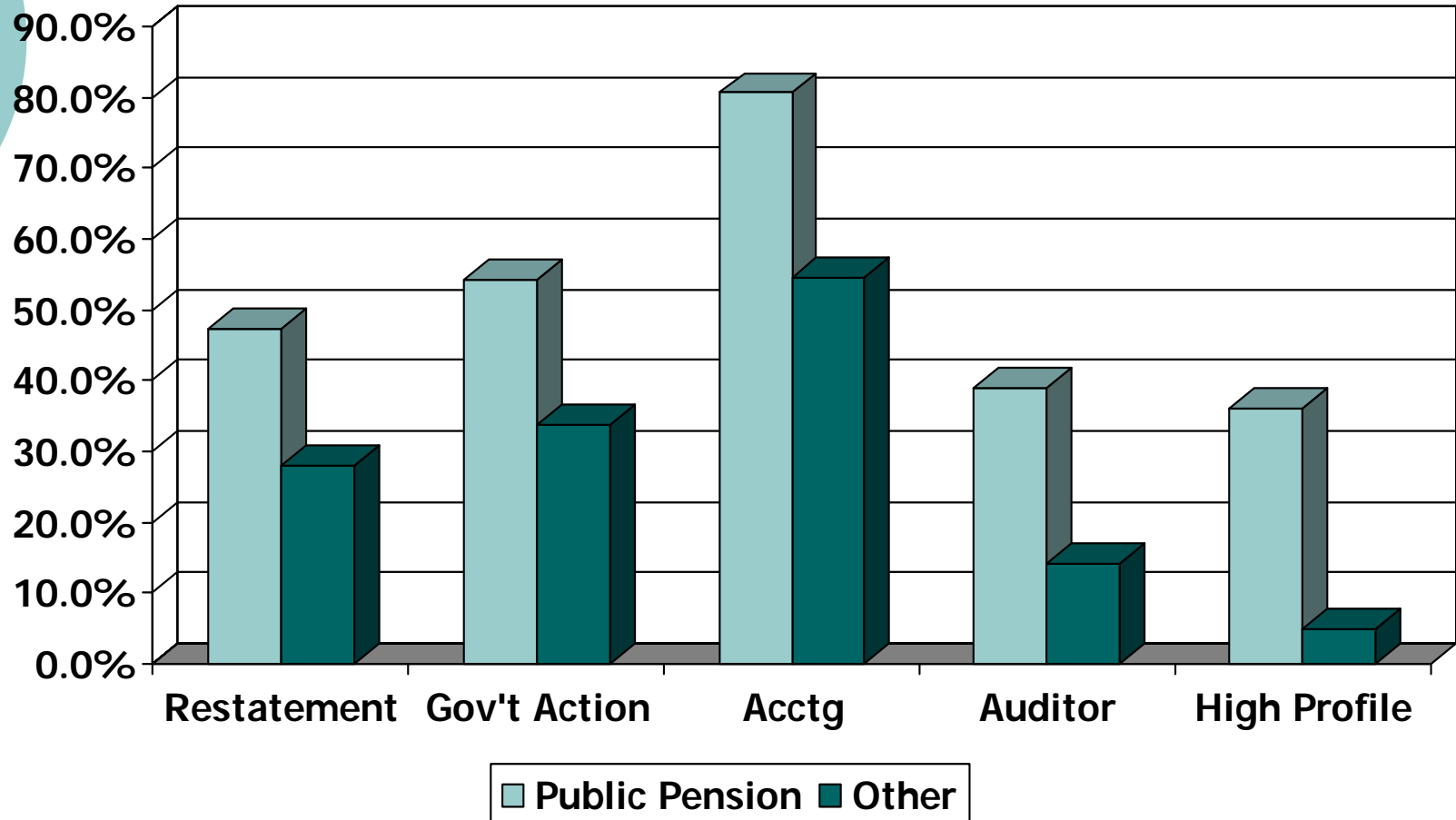
# Institutional Self-Selection



# Percentage of Public Pension Participation by MDL



# Institutional Self-Selection



# Settlement Outcomes

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- Inflation-adjusted settlements are significantly larger in cases with public pension versus other lead plaintiff types (\$376.37 million versus \$21.01 million)
- Remains significant if 5 outlying settlements > \$1 billion are excluded (\$108.30 million versus \$21.01 million)

Is that simply a byproduct of the larger cases in which public pensions assume lead plaintiff role?

# Settlement Outcomes

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- Dependent variable =  $\log(\text{settlement})$

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	<i>Full Sample</i>	<i>Settlements &lt; \$1B</i>
<b>Public Pension</b>	<b>.241 (.060)***</b>	<b>.222 (.061)***</b>
MDL	.226 (.032)***	.228 (.032)***
Class Period Length	.049 (.020)*	.042 (.020)*
Government Action	.079 (.041)*	.076 (.041)
Restatement	.127 (.045)**	.118 (.045)**
High Profile	.148 (.072)*	.151 (.073)*

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\* Significant at .01; \*\* significant at .01; \*\*\* significant at .001.

# Ratio Settlement to MDL

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- Ratio is virtually identical in cases with public pension versus other lead plaintiff types (.069 versus .070)
- Difference remains insignificant settlements < \$1 billion (.030 versus .070)

# Ratio Settlement to MDL

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	<i>Full Sample</i>	<i>Settlements &lt; \$1B</i>
<b>Public Pension</b>	<b>.185 (.072)**</b>	<b>.166 (.072)*</b>
Market Capitalization	-.721 (.044)***	-.720 (.045)***
Total Assets	.247 (.035)***	.241 (.035)***
Government Action	.107 (.048)*	.103 (.048)*
Restatement	.177 (.054)**	.168 (.054)**
Bankruptcy	-.216 (.051)***	-.207 (.051)***
Underwriter	.161 (.055)**	.143 (.055)**

\* Significant at .01; \*\* significant at .01; \*\*\* significant at .001.

# Attorney Effort

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- Total Docket Entries (TDE) is a rough proxy for litigation effort
- TDE are significantly larger in cases with public pension versus other lead plaintiff types (420.35 versus 140.10)
- Remains significantly larger for settlements < \$1 billion (315.93 versus 140.10)

# Attorney Effort: Total Docket Entries

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	<i>Full Sample</i>	<i>Settlements &lt; \$1B</i>
<b>Public Pension</b>	<b>.200 (.037)***</b>	<b>.190 (.036)***</b>
MDL	.075 (.018)***	.068 (.019)***
High Profile	.109 (.044)*	.092 (.044)*
Government Action	.054 (.025)*	.054 (.024)*
Auditor	.153 (.030)***	.146 (.030)***
Underwriter	.073 (.028)**	.050 (.028)
Case Age	.571 (.047)***	.586 (.046)***

\* Significant at .01; \*\* significant at .01; \*\*\* significant at .001.

# Attorney Fee Requests

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- Mean fee requests are significantly smaller ( $< .001$ ) in cases with public pension versus other lead plaintiff types (.212 versus .307)
- Difference remains significant for settlements  $< \$1$  billion (.222 versus .307)

# Attorney Fee Requests

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	<i>Full Sample</i>	<i>Settlements &lt; \$1B</i>
<b>Public Pension</b>	<b>-.055 (.006)***</b>	<b>-.052 (.006)***</b>
MDL	-.012 (.003)***	-.011 (.003)***
PSLRA	-.017 (.005)***	-.018 (.005)*
Auction	-.108 (.014)***	-.110 (.014)***
Bernstein Litowitz	-.016 (.007)*	-.014 (.007)*
Milberg Weiss	.011 (.004)**	.011 (.004)**

\* Significant at .01; \*\* significant at .01; \*\*\* significant at .001.

# Attorneys' Fees

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- Mean fees are significantly smaller ( $< .001$ ) in cases with public pension versus other lead plaintiff types (.200 versus .273)
- Remain significant if 5 outlying settlements  $> \$1$  billion are excluded (.207 versus .273)

# Attorneys' Fees

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	<i>Full Sample</i>	<i>Settlements &lt; \$1B</i>
<b>Public Pension</b>	<b>-.039 (.009)***</b>	<b>-.038 (.009)***</b>
MDL	-.019 (.005)***	-.018 (.005)***
PSLRA	-.002 (.008)	-.003 (.008)
Auction	-.090 (.019)***	-.083 (.019)***
Bernstein Litowitz	-.009 (.010)	-.004 (.010)
Milberg Weiss	.008 (.005)	.008 (.005)

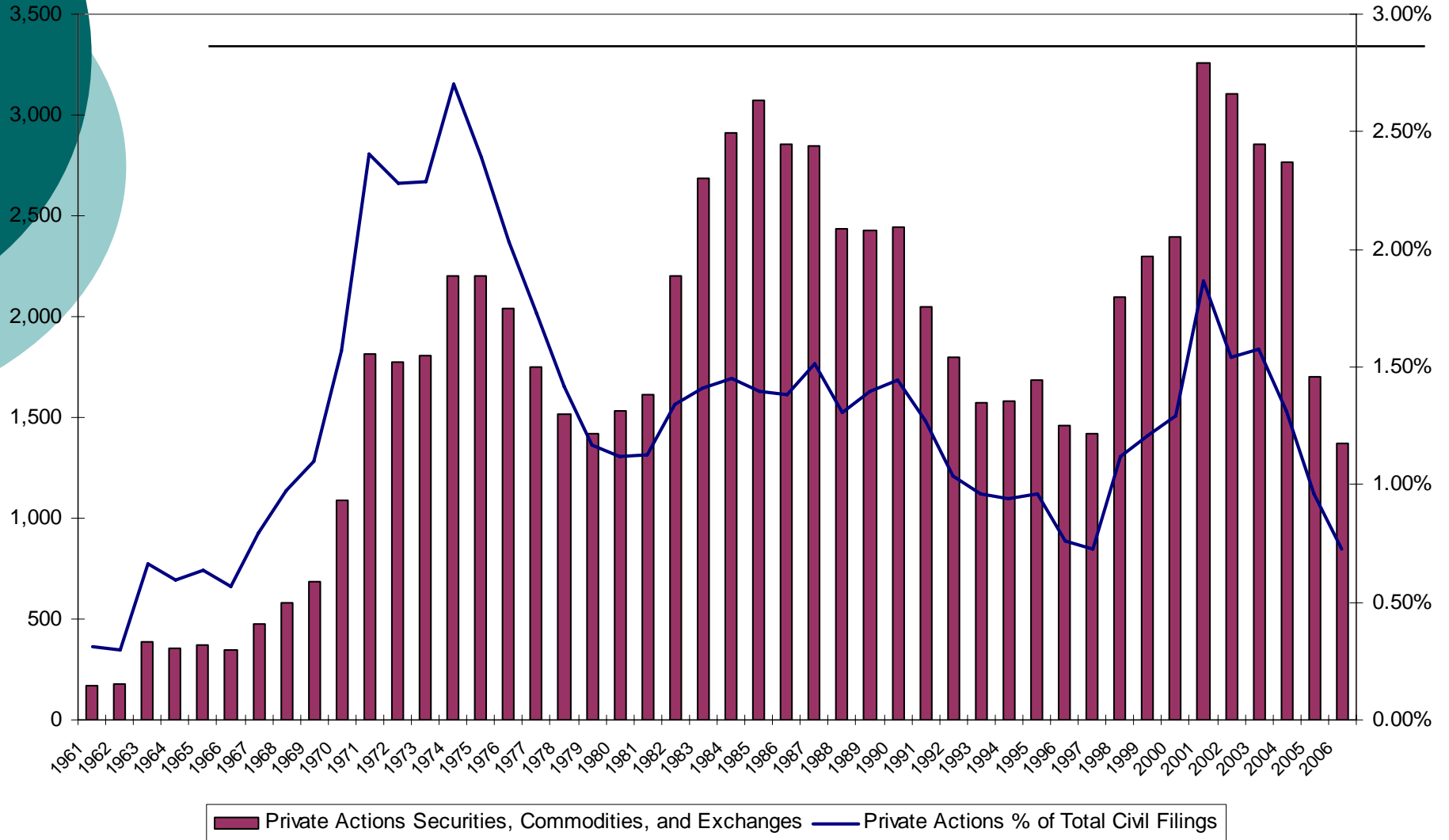
\* Significant at .01; \*\* significant at .01; \*\*\* significant at .001.



# Class Actions and International Competition

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## Private Securities Actions in Federal Courts (1961-2006)



## Johnson, Nelson & Pritchard (2007)

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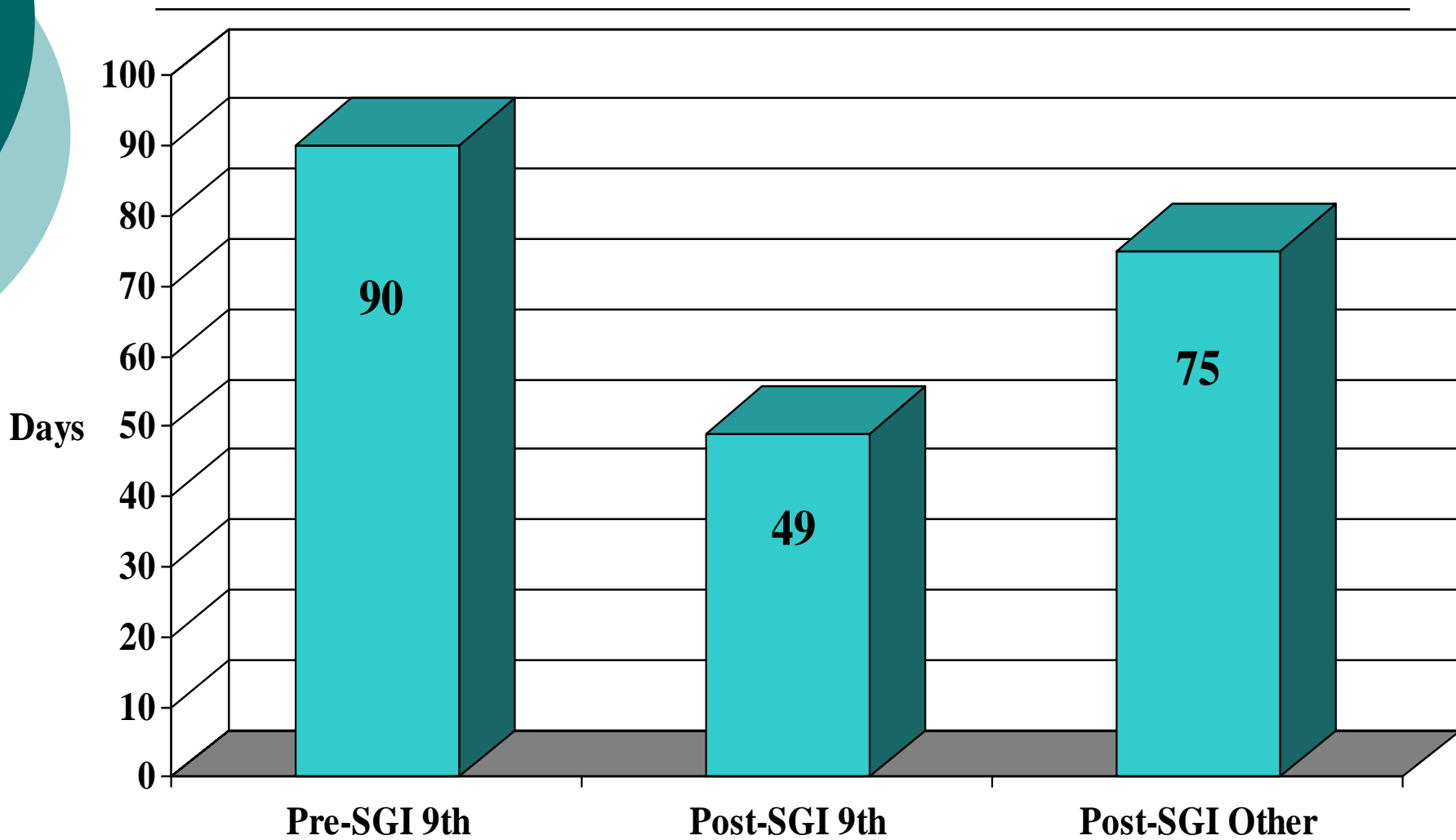
- Analyze sample of 114 computer hardware and software firms sued in securities fraud actions from 1991-2000
- Risk of lawsuit is significantly *higher* in the post-PSLRA period for firms restating class period earnings, for firms with abnormal insider stock sales, and for firms with unusually large single-day stock price drops
- Risk of lawsuit is significantly *lower* in the post-PSLRA period for firms issuing earnings warnings
- Restatements are significantly more likely to result in a settlement in the post-PSLRA period

# Choi, Nelson & Pritchard (2007)

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- Nuisance value claims are less likely to be filed in post PSLRA period
- Concludes that to compensate for extra risk under PSLRA plaintiff's lawyers shifted from low- to high-value claims
- Plaintiff's lawyers increasingly focus on cases with hard evidence (restatements and/or SEC investigations)
- Meritorious claims lacking such evidence are less likely to be filed post-PSLRA and have greater likelihood of being dismissed or of receiving low-value settlement

# The Pleading Standard and Pre-Filing Investigation



Source: Perino (2003)



## The PSLRA Paradox

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- The Act appears to reduce the incidence of non-meritorious suits
- Attorneys reduce the risk of dismissal by pursuing more obvious cases of fraud
  - The same cases that public enforcers are most likely to bring
- This undermines the rationale for private enforcement because private attorneys duplicate rather than supplement governmental action



# Is Private Enforcement Worth the Cost?

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- More criminal prosecutions, larger SEC fines, and other enforcement tools have enhanced deterrent value of government actions
- SOX Fair Funds provision (§308) gives SEC greater role in providing compensation to investors
- Helland (2006): Officers and directors do not suffer reputational penalty in average securities class action