Approved Claims Rates in Securities Class Actions

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"Plaintiff-style" aggregate damages are commonly calculated for securities class actions. These estimates provide a plaintiffs' view of the defendant's potential dollar exposure assuming the plaintiffs prevail on the merits of their case. Despite criticisms of typical plaintiff-style aggregate damages, including those made by several courts, they, along with aggregate damages estimates incorporating defendant adjustments (typically concerning class period and inflation) can play an important role throughout the life cycle of a case, in particular when it comes to settlement negotiations.

It is therefore useful to have information on the extent to which these estimates may exceed the dollar amount of damages claims submitted and approved to be paid if a case settles or if the plaintiffs prevail on their allegations at trial. Such data are limited, however, because data for securities class actions that settle are generally not publicly available and very few cases reach trial and result in a verdict in favor of plaintiffs such that damages are ultimately awarded.

This study identifies and analyzes two securities class actions that relatively recently reached trial and resulted in a verdict in favor of plaintiffs: *In re Vivendi Universal, S.A. Securities Litigation* (*Vivendi*) and *In re Household International, Inc.* (*Household*).[1] The data from these cases shows the extent to which aggregate damages estimates can exceed approved damages claims, excluding the effect of differences between plaintiffs' allegations and the jury's findings. In *Vivendi*, the "approved claims rate" was 20 percent and for *Household*, the "approved claims rate" was 38 percent.[2] When applied to aggregate damages estimates for other cases, these approved claims rates can provide an indication of the potential damages exposure, which may be of interest to securities litigators, their clients, and directors and officers (D&O) insurers.

		Vivendi	*Household*
Total Dollar Amount of Approved Claims	[a]	$41 million	$1,476 million
Aggregate Damages Estimate	[b]	$202 million	$3,880 million
Approved Claims Rate	[c] = [a] / [b]	20%	38%

CALCULATION OF APPROVED CLAIMS RATES

Aggregate damages estimates are likely to differ from the total amount of approved claims resulting from any judgment in favor of plaintiffs for a number of reasons. As a foundational matter, plaintiff-style aggregate damages estimates assume the plaintiffs prevail on their initial allegations regarding class period and the amount of inflation in the defendant company's shares during the class period.[3] For this study, this difference is removed by using the class period and amount of inflation from the jury verdicts in *Vivendi* and *Household* in the calculation of aggregate damages.[4]

Differences between aggregate damages estimates and total approved claims are also likely to occur because:

1. The trading models used in aggregate damages estimates are unreliable in that they do not provide an accurate estimate of damaged shares;
2. Not all damaged investors submit damages claims;
3. Some claims may be rejected (e.g., because defendants successfully rebut the presumption of reliance on the market price); and
4. There can be differences in damages methodologies attributable to the court's determination of how damages will be calculated for individual investors.[5]

The analysis in this study measures the effect of these four items by using publicly available information to calculate "approved claims rate" as the ratio of approved damages claims to aggregate damages estimates based on the jury verdicts.

VIVENDI AND *HOUSEHOLD*

The total dollar amount of approved claims for *Vivendi* and *Household*, according to judgments issued was $41,082,476 and $1,476,490,844, respectively.[6]

For the aggregate damages estimates, as noted above, the class period and amount of inflation in the defendant company's shares at issue were based on the jury verdicts.

In *Vivendi*, the jury ruled that Vivendi's American Depository Shares (ADS) (1) bought during the class period, between October 30, 2000, and August 13, 2002, and (2) held over the corrective disclosure, August 14, 2002, are eligible for damages. The jury determined that the amount of inflation in Vivendi's ADS for each day in the Vivendi class period ranged from $0.00 to $11.00 per ADS.[7]

In *Household*, the jury ruled that (1) shares bought during the class period, between March 23, 2001, and October 11, 2002, and (2) sold during, or after, the start of the corrective disclosure period, beginning November 15, 2001, and ending October 10, 2002, were eligible for damages. The jury determined that the amount of inflation in Household's shares for each day in the Household class period reached a high of $23.94 per share.[8]

The aggregate damages estimates for each matter are otherwise calculated using methodologies typically applied by plaintiffs.[9] Plaintiff-style aggregate damages are usually estimated using publicly available information—such as the number of shares available to be traded (float) during the class period and the volume of shares traded each day—along with a number of assumptions and related adjustments.

Float is typically calculated for each day during the class period as the number of shares outstanding less shares held by company officers and directors. Other common adjustments include subtracting estimated long-term holdings by larger institutional investors[10] and adding the number of shares comprising short interest.[11] Float was calculated for both *Vivendi* and *Household* in accordance with these typical calculations and adjustments.[12]

Plaintiffs commonly use the calculated float as an input into trading models, along with trading volume for the shares at issue.[13] Trading models purportedly estimate how many of the shares that comprise daily trading volume are purchased for the first time during the class period (and therefore become eligible for damages) and whether and/or when those shares were sold.

One model commonly used by plaintiffs—sometimes referred to as the 80/20 two-trader model—assumes that 20 percent of the trading volume is attributable to 80 percent of shares, and the remaining 80 percent of the trading volume is attributable to the remaining 20 percent of shares. While simplifying assumptions such as these generally render aggregate damages estimates unreliable, as noted by various courts,[14] these estimates are commonly used in the context of settlement negotiations.

Using the calculated float, trading volume, the 80/20 two-trader model, and the class period and amount of inflation per the jury verdicts, aggregate damages estimates are calculated.[15] Comparing the total dollar amount of approved claims for each case to the aggregate damages estimates results in approved claims rates of 20 percent for *Vivendi* and 38 percent for *Household*.[16]

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ENDNOTES

1. Analysis of these cases is associated with the January 29, 2010, verdict for *Vivendi* and the May 7, 2009, verdict for *Household* and the claims process that followed these verdicts. After the verdicts, litigation has continued for both cases with implications for the amounts ultimately received by plaintiffs. In *Vivendi*, in February 2017 the U.S. Supreme Court granted Vivendi SA an extension to appeal the jury's 2010 verdict. *See*, *e.g.*, C. Germaine, "Vivendi Gets More Time for High Court Bid in Investor Suit," *Law360*, February 7, 2017, http://www.law360.com/securities/articles/889288. In *Household*, the verdict was remanded on appeal on May 21, 2015, for a new trial to address, in part, damages issues related to loss causation. On June 17, 2016, prior to the new trial, the parties settled for $1.575 billion, approximately 64 percent of the initial verdict amount of $2.463 billion ($1.476 billion plus prejudgment interest). *See*, *e.g.*, J. Corsco, "Historic $1.6B HSBC Securities Settlement Gets Final Nod," *Law360*, October 20, 2016, https://www.law360.com/articles/853868/historic-1-6b-hsbc-securities-settlement-gets-final-nod.
2. These approved claims rates appear consistent with a February 2015 article by Rust Consulting which noted "claims rates" for securities class actions range from 20 percent to 35 percent. *See* S. Wheatman and T. Janowicz, "Estimating Claims – What Every Attorney Should Know," Rust Consulting, February 2015, available through http://rustconsulting.com/Insights/Insights-All. The Rust Consulting article does not mention how the cited claims rates were calculated, for example, whether they were calculated based on plaintiff-style aggregate damages estimates and, if so, how those estimates were calculated. Prior publications from other authors that include claims rates calculations for securities class actions were published anywhere from over 10 years ago to as far back as 1994. Further, these prior publications focus on discrediting various trading models used in the calculation of plaintiff-style aggregate damages estimates, or only provide estimates of the percentage of damaged shares for which claims are ultimately submitted, as opposed to the percentage of a damages dollar amount. The purpose of this paper is not to analyze the reliability of various trading models, which courts have generally found to be unreliable (*see*, *e.g.*, *Kaufman v. Motorola Inc*., 2000 U.S. Dist. LEXIS 14627 (N.D. Ill. 2000) and *In re Broadcom Corporation Securities Litigation*, 2005 U.S. Dist. LEXIS 12118 (C.D. Cal. 2005)), but to provide two relatively recent approved claims rate calculations based on publicly available information.
3. The class period is the time period over which the defendant company's stock was allegedly inflated. The amount of inflation in the defendant company's stock over the course of the class period would take into account changes in inflation, such as when any additional inflation was introduced and/or when any alleged inflation was removed via corrective disclosures.
4. The jury findings on the merits may differ substantially from original plaintiff claims, as was the case in both *Vivendi* and *Household*.
5. Individual investors may have a number of trades at issue, whereas trading models can only estimate damages associated with particular trades. Specifically, damages claims in a judgment take into account the aggregation of trades for a particular investor and related matching of trades (First In First Out (FIFO) or Last In First Out (LIFO)), offsets (*e.g.*, offsetting damages with gains from inflation from sales during the class period), and/or limits on damages (*e.g.*, limiting recognized losses per share to the nominal loss (purchase price less sales price)). *See* C. Galley et al., *Limiting Rule 10b-5 Damages Claims*, Cornerstone Research, 2014, https://www.cornerstone.com/Publications/Reports/Limiting-Rule-10b-5-Damages-Claims, for additional discussion.
6. *In re Vivendi Universal, S.A. Securities Litigation*, Exhibit A to Final Judgment Pursuant to Federal Rule of Civil Procedure 54(b), filed December 22, 2014. *In re Vivendi Universal, S.A. Securities Litigation*, Exhibit B to Final Judgement, filed July 24, 2016. *Lawrence E. Jaffe Pension Plan v. Household International, Inc., et al*., Exhibit A to Final Judgment Pursuant to Federal Rule of Civil Procedure 54(b), filed October 17, 2013. These amounts do not include prejudgment interest.
7. *In Re Vivendi Universal, S.A. Securities Litigation*, Verdict Form, filed February 2, 2010 ("Vivendi Verdict Form").
8. Notice of Verdict in Favor of Plaintiff Class and Against Household International, Inc., William Aldinger, David Schoenholz, and Gary Gilmer, filed January 6, 2011 ("Household Verdict Form"), Exhibit A. Despite it being part of the class period, the jury deemed there was no inflation on October 11, 2002. Therefore, investors that purchased Household stock on this day would not be damaged. The jury indicated in its decision "[f]or Household common stock that was purchased or acquired from March 23, 2001 through October 10, 2002, and: … sold from November 15, 2001 through October 10, 2002, the Recognized Loss per share is the difference between: (i) the inflation on the date of purchase as shown on Exhibit A less (ii) the inflation on the date of sale as shown on Exhibit A…" *See* Household Verdict Form. The jury also determined that on certain dates, Household's shares were purchased with as much as $4.66 of "negative inflation" per share, resulting in a benefit from the misstatements to investors that purchased Household shares on these dates. For purposes of this analysis, on these days, Household's shares are assumed to have zero inflation. This is consistent with the damages calculations applied by the claims administrator. *See* Report of Gilardi & Co. LLC Regarding Claims Administration *In re Household*, filed December 22, 2011.
9. Where assumptions were required, they were made such that the aggregate damages estimates would be smaller, and thus any calculated approved claims rate would be higher. (All else equal, this results in a higher potential approved damages claim amount when applied to any plaintiff-style aggregate damages estimate.) Assuming the plaintiffs prevail on their allegations, calculating actual potential aggregate damages requires share purchase and sale data from each potentially damaged investor. This information, however, is not publicly available (and remains unknown until each investor submits a claim for damages, either as part of the settlement proceedings or after a trial verdict). When submitting a claim, investors are typically also required to provide information on their defendant company share holdings as of the beginning of the class period. These holdings can affect the amount of a damages claim, depending upon the purchase and sale matching assumption employed (e.g., FIFO or LIFO) and whether any shares purchased prior to the class period were sold during the class period while the stock was allegedly inflated. In such an instance, the investor may have benefited from any alleged inflation. In some cases, these benefits may be used to offset any alleged damages from other share purchases. *See* Galley et al., *supra* note 5.
10. Certain institutional investors are required to report their public company holdings quarterly via SEC Form 13-F. A commonly used assumption, which is also used here, is that over the class period, an institutional investor continuously held the minimum number of shares that it reported as having owned over the class period. Since investor holdings data are reported on a quarterly basis, the number of shares held on any date other than the start or end of a quarter is commonly linearly interpolated based on daily trading volume during the quarter.

11. Short interest refers to the number of shares at any given point in time that have been sold by an investor but not yet purchased, which effectively increases the number of shares eligible for damages. The assumption that short interest increases the number of shares eligible for damages is commonly used in plaintiff-style aggregate damages estimates and is also used here. The amount of short interest is estimated for each day during the class period using bimonthly short interest provided by FINRA and assuming changes in short interest on each date between reporting dates occur proportionally to the trading volume over that same period.
12. Other commonly seen float adjustments include seasoned equity issuances and/or share buybacks. No such adjustments were made here because such events did not occur, or there were insufficient data available to reliably or conservatively model the adjustments.
13. Daily trading volume is commonly reduced, depending upon which exchange the shares at issue traded on, to account for intraday trading and/or market maker activity. A 20 percent volume reduction is typically used for shares traded on the NYSE to account for specialist activity and intraday trading. The securities at issue in both *Vivendi* and *Household* traded on the NYSE.
14. *See, e.g.*, *Motorola* and *Broadcom*, *supra* note 2.
15. Damages associated with shares held as of the end of the class periods are calculated by applying the PSLRA look-back provision through 90 days following the class period end date.
16. Using a one-trader model, whereby each share is assumed equally likely to trade, aggregate damages estimates are higher: $298 million for *Vivendi* and $5,307 million for *Household*. Using these estimates, approved claims rates are accordingly lower: 14 percent for *Vivendi* and 28 percent for *Household*.

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