

The Multiple Stages of Securities Litigation

What is the number one question we are asked by investors who contact our firm when a new securities case is filed? Why do securities class actions take so long to reach a settlement or reach some other type of resolution? Therefore, we decided to write this article to explain the lengthy process each and every securities lawsuit goes through before it ever reaches the point of a possible settlement.

The Initial Stages

In a typical securities class action, one or more shareholders who held or currently hold stock in a particular company will commence a class action by filing a complaint (most often in federal court). More often than not, multiple lawsuits are filed by multiple law firms, who each have their own plaintiff. When the **first** securities lawsuit is announced (pursuant to a press release required under the Private Securities Litigation Reform Act of 1995), this date triggers a 60-day deadline for any individual, pension fund or entity to file paperwork with the Court asking to be considered as a lead plaintiff in what eventually will be one consolidated action. When multiple actions are filed during a similar time frame, investors who choose to file documents with the Court within that 60-day window are asking the Court to consolidate all cases filed up to that point and appoint one lead plaintiff to represent the entire class, with their choice of attorney to be appointed as lead counsel representing the class. There are no extensions allowed – all parties must file their documents asking for consideration of appointment of lead plaintiff within 60 days of the first press release announcing the first filed securities class action.

Once the 60-day deadline has passed, the judge has two choices – he or she can review all pleadings filed by all parties in great detail and then enter a Court order consolidating the actions and appointing a lead plaintiff and lead counsel. Or, more often, the judge will schedule a hearing for all attorneys to appear on behalf of their clients and give oral arguments in support of their client(s) being best suited as lead class representative. These hearings are generally set within 30-45 days from the lead plaintiff deadline. At the scheduled hearing, the attorneys will present any additional arguments they have to support their client's appointment of lead plaintiff. The judge can then either make a ruling during this hearing, but most often takes the matter under advisement and issues an order at a later date in time. There is no way to determine how long a judge may take to enter an order of consolidation and appointment of lead plaintiff and counsel. This time frame can range from a few days to a few months.

As you can see from this scenario, more than 4 months have now passed just to consolidate the cases and appoint a class representative. In some instances, this time frame may be extended 6-9 months if the judge handling the case is backed up and does not have the time to review the briefs and testimony until several months after the lead plaintiff hearing. Once consolidated, all cases will move forward as one action, with one entity or group as the class representative(s), with their respective attorneys appointed as lead counsel.

Once consolidated, the judge will then enter what is typically called a scheduling order setting forth future deadlines for filing of: 1) plaintiffs' consolidated amended complaint (combining the allegations and findings from all plaintiffs, with any new allegations found by plaintiffs' lead counsel); 2) the deadline for defendants to file their motion to dismiss; and, 3) all response and reply deadlines to defendants motion to dismiss. At times, the attorneys for lead plaintiffs and defense counsel will develop their own stipulation and scheduling order and submit to the Court for approval. Either way, the scheduling order sets off the next chain of events in securities cases.

Stage Two

Plaintiffs' counsel generally has 60-90 days (pursuant to the Scheduling Order) to file their Amended Consolidated Complaint. The defendants (which include the company, as well as all named officers and/or directors) then have a deadline to file their motion to dismiss. A motion to dismiss is essentially an argument by the defendants that, even if all of the facts alleged in the complaint were assumed to be true, those facts would not be sufficient to give rise to liability under SEC Rule 10b-5. Rule 10b-5 "prohibits any act or omission resulting in fraud or deceit in connection with the purchase or sale of any security"). Once the defendants file their motion to dismiss, class plaintiffs have a deadline to file their response in opposition to defendants' motion, with defense counsel having one final opportunity to file a final reply in support of its motion to dismiss. This "briefing" period generally lasts 60-90 days. Once concluded, the court will either: 1) schedule a hearing for oral arguments on the motion to dismiss; or, 2) will take the briefs filed under advisement and file an order approving or denying the defendants' motion to dismiss. By this stage in the litigation, typically more than one year has passed since the commencement of the first lawsuit, and in busier courts, the time frame to reach this stage could approach 2 years.

If the court determines that the facts alleged in plaintiffs' complaint **are sufficient** to uphold a Rule 10b-5 claim, the court will enter an order denying the motion to dismiss, which then gives class plaintiffs the right to obtain "discovery" from the defendants -- which is the right to demand documentary evidence in defendants' possession concerning the facts at issue, and the right to require officers of the company, as well as any experts or other third parties, to sit for depositions. The discovery process is protracted and very expensive, often involving production of millions of pages of documents and depositions of multiple witnesses. Thus, it is extremely important to the litigants whether a motion to dismiss is granted or denied, as costs of the litigation will increase substantially when defendants' motion to dismiss is denied. However, when a motion to dismiss is denied by the Court, there is now a much greater chance of a recovery on behalf of the class. If defendants' motion to dismiss is granted, the case is over and will be closed by the court. This also means there will be no recovery on behalf of the class. Thus, the outcome of a motion to dismiss in a Rule 10b-5 case essentially determines whether the case gets dismissed or whether it proceeds to discovery and, very often, results in class certification and a large settlement. Because the motion to dismiss is a pivotal stage in the course of a Rule 10b-5 case, the attorneys for class plaintiffs and defendants argue fiercely over the rules that govern motions to dismiss, whether in writing or through oral argument in the courtroom.

Stage Three

By now, the lawsuit has progressed through consolidation, appointment of lead plaintiffs, and the briefing stages of a motion to dismiss – which has most likely taken 1 ½ to 2 years. If the litigation survived the motion to dismiss, then most likely discovery will be conducted. This can involve requests for document production, requests for admissions and even subpoenas to third parties for documents, etc. Often, class counsel will schedule depositions of officers, employees, experts and third parties. This process typically takes several months, depending on the number of documents to be exchanged and reviewed and the number of depositions conducted).

Once discovery is completed, class plaintiffs must seek class certification under Rule 23 of the Federal Rules of Civil Procedure. If the court grants plaintiffs' motion for class certification, the case officially becomes a securities fraud class action. At this point, the defendants can face great liability if the case goes to trial and the jury was to render a verdict against the defendants. Hypothetically, if the investor class is comprised of 50,000 shareholders who each own an average of 1,000 shares, and each shareholder claims to have sustained losses of \$10 per share because of the fraud committed by the defendants, the potential damages are \$500 million. Therefore, as a matter of practicality, when a securities case is not dismissed and is certified as a class action, the

defendants will face much pressure to settle the case to avoid the possibility of a significantly higher award by a jury verdict in class plaintiffs' favor.

The Final Stage - Settlement

It is possible that 2 ½ to 3 years have now passed since inception of the first lawsuit. However, at this point almost all securities fraud class actions result in settlement, which involves a 4-step process, *i.e.*, 1) negotiating a settlement; 2) seeking preliminary court approval; 3) obtaining final court approval; and 4) the claims administration process. Often, a mediator may be hired to assist the parties in reaching a compromise of settlement terms. Agreeing on settlement terms can occur fairly quickly or take months of negotiations. Once settlement terms have been agreed upon by both sides, a Memorandum of Understanding ("MOU") is drafted to memorialize the agreements by all parties. Once in place, a Stipulation of Settlement, and all documents needed to finalize a settlement, are drafted and filed with the court. The court then schedules a preliminary approval hearing, where the judge reviews the settlement terms and all settlement documents filed with the Court. The judge will then most likely sign an Order preliminarily approving the proposed settlement.

A final approval hearing is then scheduled, at which time the attorneys finalize all documents approved at the preliminary hearing, and hiring a third party Claims Administrator to administrate the settlement fund. If the parties implemented all required notice requirements, properly drafted final settlement documents, etc., then the judge will most likely approve the settlement for distribution at the final approval hearing. At this point in time, the Claims Administrator takes over and the attorneys step out of the picture. The Administrator receives the settlement fund, sends out court approved notices to the investor class, receives the claims from investors, processes the claims and distributes the settlement funds. If the settlement fund is large with thousands of shareholders submitting claims, the claims process could take up to one year or more. After filing some final documents by the Administrator and a dismissal of the lawsuit – the case is finally over, sometimes take 3-4 years to reach this resolution. Many of the larger securities fraud class actions, *i.e.*, Tyco, Enron, etc., took years and years to resolve.

We hope this detailed scenario will give shareholders some idea of the time involved in each and every securities lawsuit filed, and that all of them do not result in a recovery for the class. If you like this article and want to share it with someone, visit our Facebook page, "like" this article and share it.