# Opt-Out Cases in Securities Class Action Settlements

## 2012–2014 Update

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## Opt-Out Cases in Securities Class Action Settlements: 2012–2014 Update

### Introduction

This report updates our 2013 publication *Opt-Out Cases in Securities Class Action Settlements*, which provided for the first time a comprehensive quantitative analysis of publicly available lawsuits and settlements of so-called "opt-out" securities cases (cases in which at least one putative class member excludes itself from the class in order to pursue a separate lawsuit against the defendant). This publication supplements the prior study with publicly available information about the opt-outs from securities class action settlements reached between 2012 and 2014. Our database of 1,458 class action settlements now contains 48 opt-out cases from 1996 to 2014.[1]

### Key Findings

- Out of 186 securities class action settlements between January 1, 2012, and December 31, 2014, relying on publicly available data, we identified 10 cases in which at least one plaintiff opted out of the class action settlement and pursued a separate case against the defendant.[2]
- There is no publicly available information regarding dollar value opt-out settlement amounts in any of the 10 cases. However, in two of the 10 cases certain opt-outs recovered nothing—these cases were dismissed because they were time-barred under the reasoning of the 2013 ruling in *Police and Fire Retirement System of the City of Detroit v. IndyMac MBS Inc*. ("*IndyMac*").[3]
- Plaintiffs remain more likely to bring opt-out cases stemming from larger class action settlements: 75 percent of class actions with settlements of $500 million or greater reached between 2012 and 2014 had at least one related opt-out case, compared with 4 percent of class action settlements below $500 million. Across all the cases in our database, 58 percent of class actions with settlements of $500 million or greater reached between 1996 and 2014 had at least one related opt-out case, compared with 3 percent of class action settlements below $500 million.
- Almost 17 percent of cases with class action settlements over $20 million in 2012–2014 had associated opt-out cases.
- Among cases with information available, the average total value of opt-out settlements was $85.4 million, or almost 13 percent of the average class action settlement amount.
- Institutional investors such as pension funds, sovereign wealth funds, and hedge funds remain the most frequently observed type of opt-out, although small individual investors opted out in many cases.

The research for this report was conducted jointly by Cornerstone Research and Latham & Watkins.

## Analysis of Opt-Out Cases

As discussed in our 2013 report, the great majority of securities class actions result in either a dismissal or a settlement, with very few reaching a trial verdict.[4] After a settlement is agreed upon, potential class members have the ability to opt out of the settlement. Prior research had found that the most relevant predictor of opt-outs is the dollar amount recovered per class member.[5] Other research had reported that, after the adoption of the Private Securities Litigation Reform Act (PSLRA) in 1995, most plaintiffs who opted out did not do so in order to bring their own lawsuit.[6] Studies in the post-PSLRA period have found that the prevalence of opt-out cases—efforts to achieve a larger recovery through settlement or judgment outside the class—has increased relative to the pre-PSLRA period.[7] Our research builds on this by looking at the prevalence of recent opt-out cases, year by year, and analyzing salient available information about these cases.

We have identified 48 cases from 1996 to 2014 in which at least one party from the class opted out and filed a separate suit against the defendant, representing 3 percent of our sample of 1,458 cases.[8] Ten of these 48 opt-out cases occurred in 2012–2014, subsequent to our previous report.

We found no discernable increase in the preponderance of opt-outs over time. Between 1996 and 2014, both the number of opt-out cases and the percentage of those cases to class action settlements has fluctuated. The largest percentages in our data occurred in 1998 and 2013. The table below shows the number of opt-out cases per year based on our analysis, with the incremental additions to our original report boxed.

**Number of Securities Opt-Out Cases**
**1996–2014**

| Class Action Settlement Year | Number of Class Action Settlements | Number of Opt-Out Cases | Percentage of Opt-Out Cases to Class Action Settlements |
|---|---|---|---|
| 1996 | 1 | 0 | 0.0% |
| 1997 | 14 | 0 | 0.0% |
| 1998 | 29 | 3 | 10.3% |
| 1999 | 65 | 1 | 1.5% |
| 2000 | 90 | 1 | 1.1% |
| 2001 | 95 | 2 | 2.1% |
| 2002 | 111 | 6 | 5.4% |
| 2003 | 94 | 1 | 1.1% |
| 2004 | 110 | 5 | 4.5% |
| 2005 | 119 | 2 | 1.7% |
| 2006 | 90 | 6 | 6.7% |
| 2007 | 108 | 2 | 1.9% |
| 2008 | 97 | 1 | 1.0% |
| 2009 | 99 | 4 | 4.0% |
| 2010 | 85 | 4 | 4.7% |
| 2011 | 65 | 0 | 0.0% |
| **2012** | **57** | **3** | **5.3%** |
| **2013** | **66** | **7** | **10.6%** |
| **2014** | **63** | **0** | **0.0%** |
| **Total** | **1,458** | **48** | **3.3%** |

Source: *Bloomberg*; *Factiva*; *Law360*; *PACER*; Public Press; SEC Filings; Stanford Securities Class Action Clearinghouse Database

## Settlement Amount

In 21 of the 48 class action settlements with opt-out cases, the settlement or judgment amount for some or all of the opt-out cases was publicly available. The largest set of opt-out settlements related to a single case, in terms of total dollar value, was *AOL Time Warner Inc.*, where the $764 million of opt-out settlements was almost 31 percent of the size of the class action settlement.[9] The largest opt-out settlement amount as a percentage of the class action settlement was *Qwest Communications International Inc.*, where the $411 million opt-out settlement was 92 percent of the final class action settlement.[10]

Among cases with information available, the average total value of opt-out settlements was $85.4 million, or almost 13 percent of the average class action settlement amount. The average is heavily skewed by the larger opt-out settlements—the median value of opt-out settlements was only $3.9 million, or slightly less than 4 percent of the related class action settlement amount.

## Prevalence in Large Cases

While a large class action settlement does not guarantee opt-out cases, as class action settlements get larger the propensity of plaintiffs to bring an opt-out case also increases. Between 1996 and 2011, 11 percent of cases with class action settlements over $20 million had associated opt-outs. Over the 2012–2014 period analyzed in this update, almost 17 percent of cases with class action settlements over $20 million had associated opt-outs. Conversely, for class action settlements below $20 million, the opt-out case rate was only 1 percent in both periods.

Among the largest settlements, 11 of 19 cases with settlements over $500 million in 1996–2014 had associated opt-outs. Of the four cases with settlements over $500 million in 2012–2014, three had associated opt-outs. With the obvious caveat of a small sample size, this 75 percent rate in 2012–2014 represents an increase over the 53 percent opt-out rate for such large settlements in the 1996–2011 period analyzed in our original report.

While only 2 percent of all securities class action settlements between 2012 and 2014 were larger than $500 million, 30 percent of the cases involving opt-outs during the same period were associated with class action settlements larger than $500 million. In other words, large class action settlements represent a disproportionate percentage of the cases that ultimately face an opt-out. Based on our findings, if larger class action settlements are reached in the future, more opt-out cases may be expected to emerge.

## Plaintiffs

We obtained information about the identity of plaintiffs in 43 of the 48 opt-out cases in our sample:

- The most common plaintiffs in opt-out cases are pension funds. Pension funds were present in 21 of these 43 opt-out cases during 1996 to 2014.
- Other institutional investors, including mutual funds, hedge funds, and other investment companies, were involved in 20 opt-out cases.
- Eighteen opt-out cases involved individual shareholders, and four involved shareholders who obtained their holdings as a result of the defendant firm acquiring another company or entity.[11]

## Considerations for Opting Out Based on Recent Cases and Data

There are several issues opt-out plaintiffs must consider. Because opt-out cases tend to be smaller than the class action but may incur similar litigation expenses, the proportion of attorney's fees and other expenses (such as expert fees) that plaintiffs have to pay out of pocket may be higher than if the plaintiff had remained in the class. Individual plaintiffs may therefore not wish to bring an opt-out case unless their losses are sufficiently high to justify the subsequent legal costs.

One of the main reasons that class action participants nonetheless elect to opt out and pursue individual cases is the potential for financial improvement of the outcome despite the burden of legal fees.[12] The mere threat of an opt-out can be a powerful negotiating tool for plaintiffs. The higher dollar recovery sought for by plaintiffs, however, may not materialize. Many such reasons were discussed in our initial report. The Second Circuit's subsequent decision in *IndyMac* offers yet another cautionary reason (discussed below).

Another possible reason for opting out is the desire to bring a lawsuit in state court, which the opt-out plaintiffs might believe would provide a speedier trial process or a sympathetic local judge and jury pool.[13] As discussed below, however, a recent interpretation of the Securities Litigation Uniform Standards Act of 1998 (SLUSA) flags a potential complication to such calculus.

### Implications of IndyMac

In *IndyMac*, the Second Circuit held that the three-year statute of repose under the Securities Act of 1933 could *not* be tolled during a pending class action. Although the other circuits are not in unanimous agreement with this opinion, the *IndyMac* decision did have implications for opt-out case resolution in two of the 10 opt-out cases in the 2012–2014 period analyzed for this update.

In the *American International Group Inc. Securities Litigation*, a settlement of $725 million was granted final approval on February 2, 2012, and 25 shareholders opted out of the class. Seven of these shareholders are investment funds controlled by the same investment group. A lawsuit filed by six of these shareholders was dismissed in part because their claims under both the 1933 Act and the 1934 Act were time-barred under the reasoning of the ruling in *IndyMac*.[14]

In the *Bear Stearns Companies Inc. Securities Litigation*, SRM Global Master (SRM)—a hedge fund—opted out of a $275 million settlement to pursue a separate litigation against Bear Stearns. In the complaint, SRM alleged that it suffered $200 million in damages. The Second Circuit ruled that SRM filed its claim too late, dismissing the Securities Exchange Act of 1934 claims under the reasoning of *IndyMac*.[15]

### Implications of SLUSA

The U.S. District Court for the Southern District of New York's September 10, 2015, decision in *Kuwait Investment Office v. American International Group Inc. et al.* (KIO) suggests that opt-outs hoping for a more sympathetic or efficient venue may face an uphill battle. Citing SLUSA, the KIO court noted that opt-out plaintiffs' state law claims were precluded because they fell under the definition of a "covered class action," and per SLUSA, federal courts should be "the exclusive venue of, and federal law the exclusive remedy for, certain class actions." Although the opt-outs were not formally consolidated with the class, the KIO court reasoned that the two actions were "highly coordinated" and subject to similar case management orders.[16]

## Potential Cross-Border Issues

One of the 10 opt-out cases in 2012–2014 analyzed in this report suggests that cross-border considerations, especially for dual-listed shares (such as those listed in both the United States and Canada), might influence opt-out behavior. There were concurrent lawsuits filed against IMAX Corp. in both Canada and the United States, and the judge in Canada ruled that those who did not opt out of the U.S. proceeding would be excluded from the Ontario proceeding.[17] Whereas SLUSA may limit opt-outs from "venue shopping" in state court, for dual-listed companies "venue shopping" across borders might influence opt-out behavior.

## Blow Provisions

An increase in opt-out cases could impact class action settlements, causing them to fail by triggering so-called "blow-out" or "blow" provisions in the class action settlements. These provisions allow the termination or renegotiation of the class action settlement by the defendant if a large enough portion of the class opts out. Such provisions are designed to give defendants the option to consider opt-out claims that are ultimately made in order to protect against situations where opt-outs are so prevalent that settling the class action does not significantly reduce potential exposure or future legal costs. In other words, despite a class settlement agreement, a defendant may wish to terminate the class action settlement if remaining opt-out claims are significant enough that the litigation is not meaningfully discharged.

As noted in our 2013 study, if larger shareholders are expected to opt out of a settlement, then defendants may have less incentive to settle the class action or may offer less money to settle with the class, which could increase the likelihood of trials.[18] Blow provisions are one way to partially mitigate such incentives while managing the potential for future exposure.

There is no standard, boilerplate blow provision. Rather, the parameters of the provision are crafted by the settling parties, and there are numerous ways in which the terms of a blow provision can be structured. Because the purpose of a blow provision is to be able to terminate the settlement agreement if exposure to opt-out claims reaches a certain level, ideally the provision would directly relate to the dollar amount of potential exposure to opt-out claims. This potential exposure cannot be known with certainty, however, because opt-out plaintiffs may make different allegations than the class. Nonetheless, the more related a blow provision threshold is to the anticipated dollar amount of potential exposure to opt-outs, the more likely that a defendant will be able to terminate the class settlement agreement before the dollar exposure to opt-outs has exceeded the desired level. This is discussed in further detail in the forthcoming *Economic Considerations for Blow Provisions in Securities Class Action Settlements*, published by Cornerstone Research.

## Conclusion

This report updates our 2013 paper, which provided for the first time a comprehensive quantitative analysis of publicly available lawsuits and settlements of opt-out securities cases. This report supplements the prior paper with publicly available information about 10 opt-outs from securities class action settlements reached between 2012 and 2014. Out of 1,458 securities class action settlements in our database beginning on January 1, 1996, we identified 48 cases in which at least one plaintiff opted out.

Based on our analysis of these cases, it appears that defendants will need to continue to consider the potential for opt-out cases, and how to craft blow provisions to manage implications of opt-outs, as crucial issues for large securities class actions. Our research shows that over 50 percent of class actions with settlements above $500 million (and 75 percent of such cases in 2012 to 2014) had opt-outs.

Litigants in securities class actions should consider the impact of opt-out cases, as these settlements can add additional costs to the class action settlement. In the average case with an opt-out, an additional amount of almost 13 percent was paid to plaintiffs who opted out, and in six cases, more than 20 percent was paid to these plaintiffs. One additional factor to consider for the likelihood of opt-out cases is the portion of shares held by pension funds and other institutional investors, which continue to file a majority of opt-out cases.

## Endnotes

[1] Building off our prior study, the results presented throughout this report are based on a review of publicly available information from public press articles, U.S. Securities and Exchange Commission (SEC) filings, and court documents for 186 incremental securities class action settlements in 2012–2014. Potential settlement class opt-outs and subsequent related cases were identified by reviewing public press articles one year before and after the class action settlement hearing date, and company SEC Form 10-K and Form 10-Q filings two years before and after the class action settlement hearing date. An initial SEC filings and public press search was carried out for each company in the database. Key search terms included "opt-out," "exclude," and "individual action." Cases where key search terms were found were further reviewed based on a wider date range of public filings, public press, legal journal, and Internet searches. In those cases where search terms were found, if the list of plaintiffs was available in the court docket through PACER, the list of plaintiff names was searched in subsequent public filings, in order to find any future lawsuits filed by opt-out plaintiffs. Because opt-out information is not necessarily available until after the settlement, class action settlements in 2015 and 2016 were not considered at this point. While multiple parties may opt out and file lawsuits together or separately, for the purpose of this analysis we consider the collective opt-outs from a single case except where specifically noted. Similarly, while each case may have multiple defendants, we refer to them collectively as the defendant.

[2] Two of 10 incremental cases added in this update are related: the Zetia/Vytorin settlements with Schering-Plough and Merck & Co. Inc. After Schering-Plough's merger with Merck, the firms settled two similar cases involving defendant claims that the firms had delayed the release of unfavorable results of a clinical trial for the pharmaceuticals Zetia and Vytorin. The cumulative settlement amount was $688 million, of which $473 million was for the Schering-Plough settlement and $215 for the Merck settlement.

[3] Police and Fire Retirement System of the City of Detroit v. IndyMac MBS Inc., No. 11-2998-cv(L) (2d Cir. June 27, 2013).

[4] *Securities Class Action Filings—2012 Year in Review*, Cornerstone Research, 2013.

[5] Theodore Eisenberg and Geoffrey Miller, "The Role of Opt-Outs and Objectors in Class Action Litigation: Theoretical and Empirical Issues," *Vanderbilt Law Review* 57 (2004).

[6] John Coffee Jr., "Accountability and Competition in Securities Class Actions: Why 'Exit' Works Better Than 'Voice,'" *Cardozo Law Review* 30, no. 2 (2008). In these situations, the opt-outs typically increase the recovery to remaining class members.

[7] For example, *see* Kevin LaCroix, "Opt-Outs: A Worrisome Trend in Securities Class Action Litigation," *Oakbridge InSights* 2, no. 3 (April 2007): 1.

[8] Because our methodology entails reviewing publicly available information, and (as noted above) because opt-out information is not necessarily available until after the settlement, opt-outs in 2014 might exist but are not yet publicly reported.

[9] In re AOL Time Warner Inc. Securities Litigation. Complaint filed August 23, 2004. Settlement hearing date April 6, 2006.

[10] In re New England Health Care Employees Pension Fund et al. v. Qwest Communications International Inc. et al. Complaint filed February 6, 2004. Settlement hearing date September 29, 2006.

[11] Many cases involve multiple opt-outs among various types of plaintiffs.

[12] For example, *see* Kevin LaCroix, "Opt-Outs: A Worrisome Trend in Securities Class Action Litigation," *Oakbridge InSights* 2, no. 3 (April 2007): 1

[13] Because many opt-out cases are filed by government pension funds in their home state, against firms operating in other states, the "home-court advantage" of these cases may be substantial. *See* John Coffee Jr., "Accountability and Competition in Securities Class Actions: Why 'Exit' Works Better Than 'Voice,'" *Cardozo Law Review* 30, no. 2 (2008): 431–432.

[14] Kuwait Investment Office v. American International Group Inc. et al., No. 11-cv-8403 (S.D.N.Y. Sept. 10, 2015).

[15] SRM Global Master Fund Limited Partnership v. The Bear Stearns Companies LLC et al., ___ F.3d ___ (2d Cir. 2016).

[16] Kuwait Investment Office v. American International Group, Inc. et al., No. 11-cv-8403 (S.D.N.Y. Sept. 10, 2015), at 34–36.

[17] Wendy Berman, "In and Out: Ontario Superior Court of Justice Redefines Certified Global Class to Exclude Members of a Parallel U.S. Class Action," Cassels Brock & Blackwell, May 1, 2013, http://www.casselsbrock.com/CBArticle/In_and_Out__Ontario_Superior_Court_of_Justice_Redefines_Certified_Global_Class_to_Exclude_Members_of_a_Parallel_U_S__Class_Action.

[18] John Coffee Jr., "Accountability and Competition in Securities Class Actions: Why 'Exit' Works Better Than 'Voice,'" *Cardozo Law Review* 30, no. 2 (2008): 435.

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The views expressed herein are solely those of the authors, who are responsible for the content, and do not necessarily reflect the views of Cornerstone Research or Latham & Watkins. The authors acknowledge the research efforts and significant contributions of their colleagues at Cornerstone Research and Latham & Watkins.

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