
BARRACK BRIEF

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Where's The Money? From Handshake to Cash In Hand

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You have just read that the securities class action lawsuit against the company in which you invested, and subsequently lost, money has settled for a substantial amount of money. One of the first questions that comes to mind is "when will I receive my share of the settlement?" Typically it takes between eighteen and twenty-four months from the time the settlement is announced until a settlement fund is distributed. What takes so long?

Getting from the handshake between lawyers to a check in the mail to class members is a time-consuming and labor-intensive process. Mountains of paperwork, both for the lawyers and for the class members, approval and supervision by the court, in addition to the mundane task of calculating claims can cause the delay between the announcement of the settlement and the check in the mail to seem endless. So what actually happens?

The Settlement Itself

After hours or days of intensive negotiations, the lawyers representing the class and representing the defendants finally reached an agreement to settle the case. But the negotiating does not stop there. After the handshake, the agreement must be reduced to writing. A short version of the agreement, called a Memorandum of Understanding, or MOU, can be drafted and signed quickly, often within a week of the verbal agreement. The MOU contains the bare bones of the agreement, with the details left for the formal settlement agreement. Once an MOU is signed, and the court notified of the existence of the agreement, the real work on the full terms of the settlement begins. Corporations will often issue a press release announcing the settlement of the lawsuit after an MOU is signed.

Working out the details of a settlement does not have to be time-consuming, but can be. The parties often can draft and agree upon the language in a settlement agreement within a month of the actual agreement. However, with more complicated settlements, such as those involving the issuance of stock to the class, the process can go on for many months. In one case, a company issued a press release announcing a settlement in January of 1999, but the papers were not signed until November of that year.

The settlement agreement is only one part of the package of documents needed to finalize a settlement. The parties must also agree upon the language of the notice sent to members of the class describing the settlement and inviting class members to participate in, or object to, it; a summary notice for publication in the media; a proof of claim and release; and a proposed order for the court to sign to preliminarily approve the settlement. Two types of notice are needed to ensure that the class members receive actual notice of the settlement. Written notice of the settlement is sent to shareholders of record listed with a company's transfer agent. However, because the vast majority of securities are held in "street name" — held by nominees for their clients, the written notice is generally sent to the nominees, who are directed to disseminate the notice and claim forms to their clients. The summary notice, published in national financial press and on the internet, is designed to reach a wider audience than the written notices put in the mail. Although it lacks detail, the summary notice does contain instructions for obtaining a copy of the full notice and claim form.

Once the parties have approved all of the documents, the package is submitted to the court for its preliminary approval. In granting preliminary approval, the court sets important deadlines for final approval of the settlement, including the date of the fairness hearing and the dates by which the parties must submit their papers in support of the settlement and by which objections to the settlement must be filed. The court also sets the filing deadline for claim forms. All of these dates are included in the notices

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disseminated to class members. Time frames vary, but typically a fairness hearing will be scheduled approximately two months after the notice is sent. Claims deadlines are often two to three months after the date of the notice.

The fairness hearing can take fifteen minutes or a full day (or longer). A brief hearing is the norm in a simple matter where no one has objected to the settlement. The hearing could also take a full day or more if the settlement is complex or if there are objections to the settlement. If the court does approve the settlement (and in some rare cases, the court will not) the approval may come at the conclusion of the fairness hearing or some time later, usually no more than a week or two after the hearing.

Even when the settlement has been finally approved by the court (and assuming no appeal is taken from that approval), the settlement fund is still not distributed. What next?

Settlement Administration

Administration of the settlement begins when the first completed claim form arrives at the Claims Administrator's offices. But who is the Claims Administrator and what does he or she do?

Claims Administrators (sometimes called Settlement Administrators) are service organizations hired by the attorneys for the class to manage the flow of claim forms to and from class members entitled to make a claim on the settlement fund. These organizations, often accounting firms or outgrowths of accounting firms, have the staff and the technical know-how to manage the thousands of claim forms sent in by class members as well as the information submitted that form the basis for each individual claim. Class counsel delegates to the Claims Administrator the responsibility for handling the claims made by the class members. The Claims Administrator's job includes having the written notices and claim forms printed and mailed to class members; receiving completed claim forms; managing the information contained on the claim forms, as described below; and distributing the funds once the settlement administration is complete.

At the heart of claims administration is the claim form.

The claim form requires the claimant to provide detailed information about the transactions in the security in question during the class period. The claim form also requires the claimant to provide proof of the transactions in the form of confirmation slips, account statements, or portions of a tax return (if the claimant has claimed a loss on the transaction for tax purposes). Depending on how actively traded the stock was during the class period, the Claims Administrator could receive anywhere from 2,000 to 120,000 claim forms or more.

The Claims Administrator creates a specialized database for each case it administers. Typically, the claimant identification information on each claim form is entered into the database and the claimant is assigned a claim number. The transaction data contained in each claim form is then analyzed by the Claims Administrator's staff to verify the accuracy and authenticity of the information on the claim form, to determine whether a claim is deficient in any way and to calculate the claimant's allowed losses, if any. After the analysis is completed, the transaction, deficiency and loss data are entered into the database.

Once the database is complete, the Claims Administrator then contacts every claimant whose claim was rejected or found to be deficient. A claim will be rejected if the claimant purchased the securities in question outside of the class period or if, according to the plan of allocation approved by the court, a claimant suffered no loss attributed to the fraudulent actions alleged in the lawsuit. A claim is deficient if the claimant has not provided sufficient transaction information to verify the claim, has failed to provide other important information on the claim form, or has failed to sign the form. The deficient claimants have the opportunity to cure the deficiencies; the rejected claimants have the opportunity to demonstrate that the rejection was improper. If a deficiency is not cured, the claim is then rejected. Any claimant whose claim is rejected may seek the court's review of the administration of their claim. This process often takes many months to complete.

When the Claims Administrator has made a final determination with regard to each and every claim, including the deficient and rejected claims, it prepares a final report and recommendation containing detailed

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information about each claim made and its recommendations for the acceptance or rejection of the claims. Typically, nine to fifteen months elapse between the claim deadline and completion of the Claims Administrator's report. Still no distribution. What else has to happen?

The Final Step

Traditionally, class counsel have to request permission from the court to distribute the settlement fund in accordance with the Claims Administrator's recommendations. Class counsel would submit the report of the Claims Administrator to the court, and if there were any requests for court review of a rejected claim, class counsel would present these requests as well. Sometimes the court would hold a hearing on the matter. More typically, the court would order the distribution of the settlement fund based upon the papers. This could take a day or a month, depending, as with all requests submitted to the court, upon the court's schedule.

Once the court signs the distribution order, the settlement fund, including the principal contributed by the defendants plus all interest earned in the intervening months, can be distributed and only is delayed by the time it takes to print, assemble and mail the checks. If the settlement is not all cash, however, additional delays are typical. With a stock settlement, the issuance of stock certificates by a company's transfer agent adds an extra layer of administration that can delay distribution for months. Recently, some courts have incorporated permission to distribute the settlement fund into the final order approving the settlement (assuming no rejected claimants seek court review), thus eliminating this final step in the process.

So how long will it take? From handshake to final approval can take a few months or more, even up to a year. From the time claim forms are due to be filed (which typically occurs after the final approval hearing) until the settlement checks are mailed can stretch anywhere from nine to eighteen months. Getting from handshake to cash in hand, requires vigilance in filing a claim and patience in waiting for the check to arrive. ❖

Where's The Money?

At A Glance*

- Day 1: The handshake settles the case.
- Day 10: The lawyers sign the MOU.
- Day 45: The lawyers complete the Settlement Agreement and accompanying documents and submit them to the court for preliminary approval.
- Day 50: The court grants preliminary approval to the settlement.
- Day 55: Notice of the settlement is published and mailed.

2 months since handshake.

- Day 105: Fairness hearing.

4 months since handshake.

- Day 135: Claim forms due to be mailed.

1 year from claim form due date.

- Day 500: Claims administration completed. Claims administrator issues its report.

- Day 530: Lawyers for the class request permission to distribute the settlement fund based on the report of the claims administrator.

- Day 545: Court grants permission to distribute.

A year and a half from handshake.

- Day 560: Settlement fund distributed.

*Prepared for the Barrack Brief
by Leslie Bornstein Molder, Esquire*

* This time line is hypothetical. The actual length of time from an agreement to settle a securities class action case to the distribution of a settlement fund can vary significantly from this example.

Where the Numbers Come From

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One of most frustrating aspects of securities class action litigation for shareholders is when the check comes in the mail. Multi-million dollar settlements raise expectations that injured shareholders will be “made whole.” In reality, however, someone who lost thousands of dollars on their investment in a company that is the subject of a securities fraud class action may receive a check for a fraction of the out-of-pocket loss he suffered when he sold his stock in the company that is the subject of the lawsuit or the paper losses he has watched accumulate in his portfolio after the revelations of the fraud by the company. Many factors contribute to the disparity between the amount of money a shareholder actually lost on an investment and the amount of compensation that shareholder will receive as a result of a settlement in a securities fraud class action lawsuit.

The primary reason for the disparity is that a class member’s claim is not necessarily equal to the amount of money he lost on his investment. The securities laws are designed to compensate shareholders for the amount they overpaid for the stock as a result of the company’s fraud. A securities fraud lawsuit will not compensate a shareholder for the drop in price caused by other factors, such as general fluctuations in the stock market or parallel movements in the stock price of other companies in the same industry as the subject company. In fact, it is only when a securities fraud class action lawsuit is settled that the process of calculating class member claims begins.

Each class member’s claim is calculated in accordance with the Plan of Allocation described in the notice of settlement sent to potential members of the class when the court gives its preliminary approval to the settlement agreement between the parties. The formulas contained in the Plan of Allocation calculate how much a shareholder overpaid for the stock — due to the fraud by the company — on the day that he bought it. These formulas are created by experts on price movements in the stock market hired by the attorneys representing the class. The experts eliminate the effects of general market and industry stock price trends to isolate the effect that the fraud alone had on the price of the stock in question. The fraud — usually misinformation given to the investing public by

the company or adverse information known to the company but not disclosed to the investing public — inflates the price of the stock while it is ongoing and the experts determine what the “true” value of the stock would have been had the fraud not occurred.

The claims administration process, as described in the accompanying article, is designed to verify and calculate each class member’s claim. When the claims administrator has completed this process, and the court has approved the results of the administration, the claims administrator is then in a position to distribute the settlement funds. For an all cash settlement, the process is straightforward: the fund is distributed on a *pro rata* basis to the claimants. If a shareholder’s claim totals 1% of the total claims, then that shareholder is entitled to 1% of the fund to be distributed, whether the fund consists of all cash, a combination of cash and securities or all securities.

The analysis does not stop there because shareholders will not necessarily receive the full amount of their claim. If the settlement fund is insufficient to pay every claimant their full loss, then every claimant receives the same percentage of their claim. For example, if a settlement fund totals \$10 million and the claims total \$10 million, then every claimant will receive a check for 100% of their claim. If the claims total \$20 million, then every claimant will receive a check for 50% of their claim.

While waiting for the distribution to arrive in the mail, claimants often ask for a prediction of how much they will receive when the settlement fund is distributed. As shown above, until the end of the claims administration the answer is simply not available. ❖

About the Publisher...

Barrack, Rodos & Bacine is a boutique law firm that has been extensively involved in class and derivative actions alleging violations of securities laws for more than twenty-five years. The firm has attorneys in offices located in Philadelphia, San Diego, New York, and New Jersey. The *Barrack Bulletin*, edited by Leslie Bornstein Molder, Esquire, is published four times a year.

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