I. INTRODUCTION

As a securities case approaches trial, the court confronts the question whether plaintiffs can aggregate damages at trial so that the jury can make a single determination of damages applicable to all plaintiffs in the class, notwithstanding the fact that damages may vary widely across the class. Plaintiffs argue in favor of aggregating damages because doing so can simplify their damages proof and facilitate administrative management of the case. Defendants argue in favor of calculating damages on an individualized plaintiff level, rather than in the aggregate.

For this reason, the United States District Court for the Western District of Pennsylvania has held that, under the PSLRA, damages cannot be calculated on an aggregate basis.

This article discusses aggregate securities damages. It analyzes the differing approaches to the issue taken by the Western District of Pennsylvania and the Southern District of New York. It also discusses the implications of this issue for the parties to the case and for insurance carriers.

II. DECISIONS CONCERNING AGGREGATE DAMAGES IN SECURITIES CASES

Bell v. Fore Systems, Inc.

In Bell v. Fore Systems, Inc., the United States District Court for the Western District of Pennsylvania considered the use of aggregate damages when granting a motion in limine by defendants to exclude testimony from the plaintiffs' expert witness on damages in a Section 10(b) securities fraud action. The plaintiffs' expert witness used a damages model that calculated "aggregate damages" by multiplying the estimated number of shares traded by the estimated artificial inflation for each day of the class period.

At the same time, however, while aggregate damages calculations may be simpler, they are less precise because they do not take into account variations among the plaintiff class that will likely reduce damages, potentially by a large amount. In addition, in cases under Section 10(b) of the Securities Exchange Act of 1934, the use of aggregate damages may run afoul of the Private Securities Litigation Reform Act of 1995 (the "PSLRA").

The provision recognizes that investors may overreact to the disclosure of adverse information about a company, thereby causing the stock price of the company to drop excessively immediately following disclosure. The PSLRA therefore requires that any damages calculation in a Section 10(b) case "look back" in order to take into account the increase in the stock price that often takes place in the 90-day period following a disclosure of adverse information.

In a Section 10(b) case, the PSLRA also addresses the possibility that some members of the plaintiff class may have sold their shares during the 90-day look-back period. It provides that if the plaintiff sells or repurchases the stock during that period, then "the award of damages to the plaintiff shall not exceed the difference between the purchase or the sale price paid or received, as appropriate, by the plaintiff for the subject security and the mean trading price of that security during the 90-day period beginning on the date on which the information correcting the misstatement or omission that is the basis for the action is disseminated to the market.

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In a Section 10(b) case, the PSLRA also addresses the possibility that some members of the plaintiff class may have sold their shares during the 90-day look-back period. It provides that if the plaintiff sells or repurchases the stock during that period, then "the award of damages to the plaintiff shall not exceed the difference between the purchase or the sale price paid or received . . . and the mean trading price of the security during the dissemination of information correcting the misstatement or omission and ending on the date on which the plaintiff sells or repurchases the security."
Third, the Bell court reasoned that subsection (e) establishes a formula for determining damages that cannot be applied class-wide. The court explained that in order to properly calculate damages for a plaintiff, the fact finder would need to determine the purchase price actually paid and sale price actually received on a plaintiff-specific basis. The Bell court concluded that "the Limitation on Damages cannot be imposed on the class as a whole, but must be applied to the circumstances of each plaintiff." As a result, it held that the trial would need to be bifurcated. During the first "class action" phase, the jury could decide liability as well as, assuming liability was established, the amount of inflation per share for various time segments potentially at issue. During the second phase, plaintiff-specific issues would be resolved. These issues could include whether plaintiffs purchased shares during the class period, whether defendants could rebut "fraud on the market" presumptions as to particular plaintiffs and the actual amount of damages as a result of the look-back calculations.

The court acknowledged inefficiencies in individual determinations of damages as well as bifurcation and recognized that an appellate court may deem aggregate class damages acceptable. The court also acknowledged that its interpretation of the PSLRA "is at odds with current litigation practices" and "forthrightly admits that its proposed bifurcation of issues is based on practicalities rather than precedent." The court therefore certified its order for interlocutory appeal sua sponte, but the parties did not pursue an appeal in the case, which the parties ultimately settled.

In re Oxford Health Plans, Inc. Securities Litigation

Less than a year later, in In re Oxford Health Plans, Inc. Securities Litigation, the United States District Court for the Southern District of New York rejected the Bell court's approach and held that plaintiffs are permitted, notwithstanding the PSLRA, to present aggregate damages calculations to the jury. In that case, the plaintiff class representatives in a Section 10(b) securities fraud class action sought the award of a common fund of damages based on an aggregate damages analysis by their expert witness. The defendants contended that the PSLRA barred such an award and instead required bifurcation.

The Oxford Health court disagreed that subsection (e) of the PSLRA in any way distinguished between the "class" and "individual" plaintiffs for purposes of damages, as Bell had concluded. Rather, according to the court, the only change enacted by the passage of subsection (e) of the PSLRA was the addition of the 90-day look-back period. In all other respects, the court opined, subsection (e) "represents no significant change from the law as it previously existed." As a result, it held that the trial would need to be bifurcated. During the first "class action" phase, the jury could decide liability as well as the amount of damages. The court awarded damages for a plaintiff, the fact finder would need to determine the purchase price actual cost and sale price actual cost received on a plaintiff-specific basis.

In re WorldCom, Inc. Securities Litigation

Most recently, the United States District Court for the Southern District of New York addressed the issue of aggregate damages in two opinions In re WorldCom Securities Litigation. In those decisions on motions in limine, the court addressed the use of aggregate damages in a Section 11 case and in two WorldCom bond offerings, relying heavily on the reasoning of Oxford Health.

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The defendants sought to exclude testimony by plaintiffs' expert concerning the aggregate damages, arguing that the aggregated damages analysis failed to consider the magnitude of the opt-outs from the class, the various conclusions a jury might reach regarding liability on the various alleged omissions and misstatements, the receipt of money by class members through the bankruptcy settlement, and the success that the defendants might have in proving the affirmative defense that an individual class member actually knew of the alleged misrepresentations and omissions when purchasing the bonds.

The court rejected the defendants' arguments, relying on the reasoning of Oxford Health, and noting that "[a]ggregate damages awards are a 'standard practice' in securities cases." It held that "[t]he trial of Securities Act claims, with their special formulae for calculating damages embodied in Section 11(e), alongside Exchange Act claims should not change that practice." In addressing the defendants' concern regarding overcompensation to absent class members, the Court held that an aggregate damages award would not overcompensate a class member because, following trial, the individualized damages would be paid out in the claims process following the plenary trial. Moreover, to the extent that the established fund turned out to exceed the amount to be distributed to class members, the court noted that the defendants could receive the excess funds.

The WorldCom court also relied on practical concerns previously identified in Oxford Health to support the use of aggregate damages. The court explained that entry of an award by a jury permits entry of a final judgment, which in turn facilitates prompt appellate review. In addition, the court reasoned that entry of an award by the jury creates a common fund to pay the litigation expenses and administrative costs associated with the claims process.
decisions by two district court judges do not constitute binding precedent in the Southern District of New York,18 let alone outside of that court. Thus, defendants and their insurers can take into account that they may still be able to challenge the use of aggregate securities damages.

In that regard, as a practical matter, the use of aggregate damages gives plaintiffs another tool to inflate artificially the calculations in an effort to try to extract high damages. Aggregate damages calculations represent a best-case scenario for plaintiffs and do not take into account the factors likely to bring the number down.

The Southern District of New York seems untroubled by the fact that defendants may have numerous plaintiff-specific arguments that will reduce the amount of damages. Under its approach, everything will work out in the end because these issues will be addressed before damages are finally paid out, and the defendants "are entitled to a refund of any parts of the common fund not actually expended or distributed."19 The court in WorldCom determined, for example, that such individualized determinations "will be pursued in the individual proceedings that will follow the plenary trial,"20 although it did not outline in any detail the form or process for those individual proceedings. This approach disregards the low probability that the end point will ever be reached.

Instead, as in WorldCom, the odds are high that most or all of the case will be settled. Plaintiffs may be able to use a high aggregate damages number to extract a larger settlement from defendants (and their insurers) even though the aggregate damages do not take into account all of the factors that will ultimately drive the number down at the end of the day.

At least in the Southern District of New York, where the use of aggregate damages remains viable, defendants and their carriers should recognize when negotiating settlements that the aggregate damages number may be reduced by a number of factors, including:

- **In Section 10(b) cases**, the actual sales and purchase price of the members of the class required for the look-back analysis of subsection (e) of the PSLRA;
- **In Section 11 cases**, trading data to show when, and at what prices, plaintiffs sold their bonds;
- Evidence that some plaintiffs, particularly institutional investors, knew the facts alleged by misrepresentation at the time they purchased the securities;
- Receipt of money by class members from other sources (e.g., bankruptcy); and
- Opt-outs from the class.

Cumulatively, these factors may drive the damages calculation down substantially. For example, in WorldCom, defendants' brief in opposition to the use of aggregate damages argued that the aggregate damages calculation potentially overstated damages by more than $3 billion.

Defendants and their insurers should therefore recognize that, as with other elements of plaintiffs-style damages, the damages numbers put forward by plaintiffs likely overstate damages to a large degree and should not be a factor, let alone the starting point, in any settlement discussions for a securities class action lawsuit.21

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FOOTNOTES

5. See In re Oxford Health Plans, Inc. Sec. Litig., 244 F. Supp. 2nd, 270-51 (S.D.N.Y. 2003) ("Common sense suggests that the sudden revelation of a fraud may cause a momentary overcorrection in market price, and a dearth of potential buyers may exist for a longer period while whatever cloud the revelation placed on the issuer, dissipates."); Baruch Lev & Meiring vs. Villiers, Stock Price Crashes and 10(b)(5) Damages: A Legal, Economic and Policy Analysis, 47 Stan. L. Rev. 7 (1994) (analyzing same).
7. Bell, 2002 WL 3209754, *2 (citing Pennsylvania Dept. of Corrections v. Yeskey, 524 U.S. 206 (1998)) (the title of a statute cannot limit a title’s plain meaning, but can be used for interpretive purposes to shed light on some ambiguous word or phrase).
12. 244 F. Supp. 251; see also id. ("The statute merely modifies slightly the means by which actual damages are determined. Its enactment should not be deemed to effect such a drastic change in the conduct of class action litigation as now claimed.").
17. Gasperini v. Center for the Humanities, 518 U.S. 415, 430 n.10 ("If there is a federal district court standard, it must come from the Court of Appeals, not from the over 40 district court judges in the Southern District of New York, each of whom sits alone and renders decisions not binding on the others.").
20. See also David H. Topol, Attacking Plaintiffs-Style Damages During Mediation of Securities Cases in the May & June 2004 issues of the PLUS Journal.