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Do Differences in Pleadings Standards Cause Forum Shopping in Securities Class Actions?: Doctrinal and Empirical Analyses

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DO DIFFERENCES IN PLEADING STANDARDS CAUSE FORUM SHOPPING IN SECURITIES CLASS ACTIONS?: DOCTRINAL AND EMPIRICAL ANALYSES

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Federal appellate courts have promulgated divergent legal standards for pleading fraud in securities fraud class actions after the Private Securities Litigation Reform Act (PSLRA). Recently, the Supreme Court of the United States issued a decision in *Tellabs, Inc. v. Makor Issues & Rights, Ltd.* that could have resolved these differences, but did not do so. This Paper provides two significant contributions. We first show that *Tellabs* avoids deciding the hard issues that confront courts and litigants daily in the wake of the PSLRA's heightened pleading standard. As a consequence, the opinion keeps very much alive the circuits' disparate interpretations of the PSLRA's fraud pleading standard. To be sure, *Tellabs* might ultimately be applied by lower courts to narrow the range of permissible approaches to satisfying the strong inference standard, but leaves a good deal of room within which wide variations in approach will continue. Our second contribution is empirical in that we seek to answer the question: do plaintiffs' attorneys take advantage of the differences among the circuits' interpretation of the pleading standard to select more favorable venues to file their cases, as some scholars have claimed? We find that 85 percent of the securities fraud class actions in our sample are filed in the home circuit of the defendant corporation. While we find that the differences in the circuits' pleading standards do not have a statistically significant impact on the plaintiffs' choice of venue, we find that plaintiffs are more likely to file low-value cases in jurisdictions other than the one in which the defendant's headquarters is located.

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INTRODUCTION

Access to justice has long been a feature not only of American civil procedure, but also American society. We find its impact nearly everywhere we look in the law, whether it be permissive class-action procedures, contingency-fee arrangements, or the American rule on who pays for the costs of a misdirected lawsuit. Even the dry subject of pleading reflects our belief that plaintiffs should not be hobbled in getting their grievance before the judge and jury. Thus, in 1938, Federal Rule of Civil Procedure (Rule) 8 broke with the common law's fact-specific pleading requirements so as to "ensure litigants have their day in court."[1] Simply stated, notice pleading's primary function is to alert the opposing party of the incident upon which a claim is being asserted. In its seminal pleading decision *Conley v. Gibson*,[2] the Supreme Court of the United States observed, "The Federal Rules reject the approach that pleading is a game of skill in which one misstep by counsel may be decisive to the outcome and accept the principle that the purpose of pleading is to facilitate a proper decision on the merits."[3]

But even in this plaintiff-friendly environment, limits on otherwise acceptable bald allegations were imposed where abuses were seen most likely to occur. Thus, Rule 9(b) has long called for allegations of "fraud or mistake" to be set forth with "particularity."[4] More recently,

1. Christopher M. Fairman, *The Myth of Notice Pleading*, 45 ARIZ. L. REV. 987, 990 (2003). Rule 8 requires a "short and plain statement of the claim showing that the pleader is entitled to relief." FED. R. CIV. P. 8. *See also* Charles E. Clark, *Simplified Pleadings*, 2 F.R.D. 456, 462–73 (1943) (describing the then-new rules and procedures to reach merit determinations).

2. 355 U.S. 41 (1957).

3. *Id.* at 48.

4. FED. R. CIV. P. 9(b). We find heightened requirements for particularity in other areas as well, for example discrimination claims filed under Title VII of the Civil Rights Act of 1964. *See, e.g.*, *Swierkiewicz v. Sorema N.A.*, 534 U.S. 506, 509 (2002). *See generally* Fairman, *supra* note 1 (reviewing various legal areas for which there is a heightened pleading requirement).

in *Bell Atlantic Corp. v. Twombly*,[5] the Supreme Court held that at least in antitrust cases alleging a conspiracy to restrain trade, *Conley*'s permissive standard was to be replaced by a "plausible grounds" standard whereby the plaintiff must plead "enough facts to raise a reasonable expectation that discovery will reveal evidence of illegal agreement."[6] Congress too has entered these retrenchment efforts. In response to efforts by the "big five" accounting firms and Silicon Valley executives, who joined forces believing they had been on the nuisance end of a bit too much access to justice, Congress enacted the Private Securities Litigation Reform Act of 1995 (PSLRA).[7] The PSLRA has as one of its cornerstones[8] a heightened pleading

5. 127 S. Ct. 1955 (2007).

6. *Id.* at 1965. The Court justified, and perhaps thus cabined to some extent, its holding by there being significant costs flowing from discovery in antitrust cases, particularly antitrust class actions, which may "push cost-conscious defendants to settle even anemic cases." *Id.* at 1967.

7. Pub. L. No. 104-67, 109 Stat. 737 (1995). We do not believe a compelling case has been made that the PSLRA, and particularly the heightened pleading requirement, was a significant cause in the wide-spread reporting abuses that caused the collapse of U.S. securities markets in 2002. Some commentators point toward the reforms introduced by the PSLRA, and particularly the heightened pleading requirement, as contributing to the environment that fostered the numerous financial reporting scandals that came to light in 2001 and 2002. *See, e.g.*, André Douglas Pond Cummings, *"Ain't No Glory in Pain": How the 1994 Republican Revolution and the Private Securities Litigation Reform Act Contributed to the Collapse of the United States Capital Markets*, 83 NEB. L. REV. 979, 1028–29 (2005) (arguing that the PSLRA stripped away important investor protections that facilitated abuses that ensued in the late stages of the 1990s bull market); Daniela Nanau, *Analyzing Post-Market Boom Jurisprudence in the Second and Ninth Circuits: Has the Pendulum Really Swung Too Far in Favor of Plaintiffs?*, 3 CARDOZO PUB. POL'Y & ETHICS J. 943, 946–47 (2006) (suggesting prodefendant substantive and procedural developments contributed to unabashed conflicts of interest, reporting violations, and manipulative practices in public offering of securities). We believe this gives too much credit to the reforms introduced in 1995 and too little credit to the ability of lawyers to meet the heightened pleading requirement. On this point, it is relevant that Congress's response to the frauds was not to repeal any provision of the PSLRA. On the contrary, Congress's response was the enactment of the Sarbanes-Oxley Act of 2002, with multiple provisions intended to strengthen the financial reporting system, not facilitate the conduct of securities class actions.

8. Two other PSLRA innovations that have significantly impacted the conduct of securities class actions were enacted to reduce the likelihood of strike suits. Adding a catch-22 feature to the heightened pleading requirement is the PSLRA's bar to the plaintiff gaining discovery when a motion to dismiss is pending. *See* 109 Stat. 737, 747 (codified as amended at 15 U.S.C. § 78u-4(b)(3)(B) (2006)). Thus, not only must the plaintiff set forth with particularity facts establishing the defendant's knowledge or recklessness in committing a misrepresentation, the plaintiff must rely on means other than the pre-PSLRA practice of fishing through the defendant's records to gather the required facts. It has been suggested that "constrained and targeted discovery" focused on filling gaps in the complaint that were surfaced through the lens of the heightened

requirement for securities class actions. Pursuant to the PSLRA, allegations regarding the defendant's state of mind must be set forth not only with particularity, but more significantly the facts pleaded should give "rise to a *strong inference* that the defendant acted with the required state of mind" in committing the disclosure violation.[9]

Several puzzles arise from the PSLRA's "strong-inference" standard. First, just how persuasive or compelling is a strong inference? Is this to be judged by the standard that applies in civil litigation generally—the more-likely-than-not standard[10]—or is it some more demanding standard, such as a "high likelihood" or some variation on that formulation? Since this determination involves testing

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pleading requirement would eliminate this catch-22 problem. *See* Elliott J. Weiss & Janet E. Moser, *Enter Yossarian: How to Resolve the Procedural Catch-22 that the Private Securities Litigation Reform Act Creates*, 76 WASH. U. L.Q. 457, 506–07 (1998).

The other cornerstone of the PSLRA is a mechanism by which the court selects a lead plaintiff from competing petitioners. *See* § 21D(a)(3), 109 Stat. at 743 (codified as amended at 15 U.S.C. § 78u-4(a)(3)). Pursuant to the latter provision, after a securities lawsuit is filed on behalf of a class, notice is given to the class inviting interested parties to petition to be named the suit's lead plaintiff. The statute provides a rebuttable presumption that the petitioner with the largest loss from the alleged violation is the "most adequate" plaintiff. 15 U.S.C. § 78u-4(a)(3)(B)(iii). Among the selected lead plaintiff's tasks is to recommend to the court who should be counsel for the suit. By enacting the lead plaintiff provision, Congress sought the participation of institutional investors, believing they might reduce the frequency of misguided suits while in other cases assuring that settlements were fair to the class members. Empirical evidence supports Congress's belief as to the latter, as the presence of an institutional plaintiff yields statistically significant greater returns. *See* James D. Cox & Randall S. Thomas, *Does the Plaintiff Matter? An Empirical Analysis of Lead Plaintiffs in Securities Class Actions*, 106 COLUM. L. REV. 1587 (2006) [hereinafter *Does the Plaintiff Matter?*]. Institutional investors also appear to moderate the fees awarded to the suit's counsel such as through presuit negotiations. *See* Michael A. Perino, *Markets and Monitors: The Impact of Competition and Experience on Attorneys' Fees in Securities Class Actions* 2 (St. John's University Sch. of Law Legal Studies Research, Working Paper No. 06-0034, 2006), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=870577. However, not all the news regarding institutions is positive. *See* James D. Cox & Randall S. Thomas, *Letting Billions Slip Through Your Fingers: Empirical Evidence and Legal Implications of the Failure of Financial Institutions to Participate in Securities Class Action Settlements*, 58 STAN. L. REV. 411, 424 (2005) (finding that in 118 securities class-action settlements, 72 percent of institutions that could participate in a settlement do not submit a claim once the suit is settled even though their mean loss was almost $850,000); *see also* James D. Cox & Randall S. Thomas, *Leaving Money on the Table: Do Institutional Investors Fail to File Claims in Securities Class Actions?*, 80 WASH. U. L.Q. 855, 875–77 (2002) (revealing similar findings in a small pilot study).

9. Private Securities Litigation Reform Act of 1995, § 21D(b)(2), 109 Stat. at 747 (codified as amended at 15 U.S.C. § 78u-4(b)(2)) (emphasis added).

10. The Supreme Court had held that the governing standard of proof in private securities suits is the preponderance-of-the-evidence standard. *See Herman & MacLean v. Huddleston*, 459 U.S. 375, 390 (1983).

the plaintiffs' pleadings, it is a decision that of necessity is made by the presiding judge.

There is yet another difficult question, to wit, whether in enacting the PSLRA Congress intended to alter the prevailing standard for evaluating motions to dismiss as set forth in Rule 12(b), namely that any reasonable inference from the plaintiff's allegations are to be drawn in favor of the plaintiff.[11] But drawing inferences poses another tricky question. If factual inferences are to be drawn both for and against the plaintiff, does this so involve the judge in factual issues that it invades the province of the jury[12] and violates the Seventh Amendment guarantee of a jury trial? Not surprisingly, the PSLRA's legislative history is bereft of insights on each of these questions. As a result, in the ten years after the PSLRA, variations developed among the federal circuits in their approach to the strong-inference standard so that when the Supreme Court granted review of the United States Court of Appeals for the Seventh Circuit's decision in *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*,[13] there was optimism that clarity in this area would be restored. As we will see in the discussion that follows, *Tellabs* answers many issues surrounding the application of the strong-inference standard, but leaves many significant issues unresolved.

This Paper provides two significant contributions. We first show that *Tellabs* avoids deciding the hard issues that confront courts and litigants daily in the wake of the PSLRA's heightened pleading standard. As a consequence, the opinion keeps very much alive the circuits' disparate interpretations of the PSLRA's fraud-pleading standard. To be sure, *Tellabs* might ultimately be applied by lower courts to narrow the range of permissible approaches that satisfy the strong-inference standard, but leaves a good deal of room within which wide variations in approach will continue.

Our second contribution is empirical in that we seek to answer the question, do plaintiffs' attorneys take advantage of the differences among the circuits' interpretations of the pleading standard to select

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11. In a Rule 12(b)(6) motion to dismiss, defendants admit all well-pleaded allegations and all inferences the jury can reasonably draw in the plaintiff's favor. In this way, the motion to dismiss tests the plaintiff's best case to determine whether, as a matter of law a claim has been stated. *See Scheuer v. Rhodes*, 416 U.S. 232, 236 (1974).

12. *See, e.g., Pirraglia v. Novell, Inc.*, 339 F.3d 1182, 1188 (10th Cir. 2003) (professing its unwillingness to weigh inferences for fear it would "invade the traditional role of the factfinder").

13. 127 S. Ct. 2499, 2506 (2007) ("[G]rant[ing] certiorari to resolve the disagreement among the Circuits on whether, and to what extent, a court must consider competing inferences in determining whether a securities fraud complaint gives rise to a 'strong inference' of scienter.").

more favorable venues to file their cases?[14] The securities laws provide fairly broad venue options for private litigants. Suit can be brought in any federal district court where "the defendant is found or is an inhabitant or transacts business," and service of process is equally broad.[15] Such broad venue options invite our examination of whether counsel in securities class actions choose a forum based on the proximity of the forum to the defendants, or instead select a forum opportunistically to gain a substantive advantage such as a more favorable pleading standard.[16] The forum-shopping thesis is

14. *See, e.g.*, Michael A. Perino, *Did the Private Securities Litigation Reform Act Work?*, 2003 U. ILL. L. REV. 913, 947–48.

15. Securities Exchange Act of 1934, ch. 404, sec. 27, 48 Stat. 881, 902–03 (codified as amended at 15 U.S.C. § 78aa (2006)); Securities Act of 1933, ch. 38, sec. 22(a), 48 Stat. 74, 86–87 (codified as amended at 15 U.S.C. § 77v(a)). The great distinction between these two acts is that the federal courts enjoy exclusive jurisdiction with respect to violations of the Securities Exchange Act of 1934, but have concurrent jurisdiction with the states with respect to private suits brought under the Securities Act of 1933.

16. In addition to the common considerations related to convenience to the plaintiff who favors a suit near the plaintiff counsel's office, due to a number of circuit splits, there are a host of substantive issues that can cause counsel to select a more remote forum for the securities class action. A threshold consideration is whether the suit is barred by the statute of limitations. The standard limitations period is that suit must be brought within one year of discovery, and in no case longer than three years after the violation. The Sarbanes-Oxley Act of 2002 extended these lengths to two years and five years, respectively, for suits premised on fraud (as contrasted with negligent violations). Pub. L. No. 107-204, § 804, 116 Stat. 745, 801 (codified as amended at 28 U.S.C. § 1658). Circuits vary not only in their interpretation of what level of awareness constitutes "discovery," but also in whether, even after such discovery, the statute is tolled for that period of time that upon notice of a possible violation, the investor through reasonable diligence would have discovered the facts underlying the fraud. *See* JAMES D. COX ET AL., SECURITIES REGULATIONS CASES AND MATERIALS 798–99 (5th ed. 2006) (collecting cases illustrating different approaches).

An important consideration in securities class actions is finding a culpable defendant with sufficient resources to make the suit worth prosecuting. Following the Supreme Court's rejection of aiding-and-abetting liability in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994), implicating such a person has become not only challenging, but also invites forum shopping. To be so liable, the defendant must either be a primary participant or a control person. Circuits vary in their approach to defining who is a *primary violator*. To illustrate, consider the so-called bright-line test followed in the United States Court of Appeals for the Second Circuit. In a leading case, the court held that an accounting firm that falsely assured management that its 1995 results were accurate was not liable to investors who relied on reports released by management. *Wright v. Ernst & Young LLP*, 152 F.3d 169, 175–76 (2d Cir. 1998). Reasoning that investor reliance upon a false statement made by the defendant is an essential aspect for liability, the court concluded that, since the accountants were not identified in the reports, the reports could not thereby be connected to the accountants such that the investors could be deemed to have relied on any representation attributable to the accountants. Just the opposite result would occur had the suit been maintained in the United States Court of Appeals for the Ninth

straightforward. Litigants, and their attorneys, want to maximize their overall recoveries in securities fraud class actions. If they have a portfolio of cases that they are considering filing over a broad range of different venues (which the securities laws' liberal venue provisions permit them to do),[17] they are more likely to file their highest-value cases in jurisdictions where they perceive the odds of winning are the best. Since nearly all securities class actions that survive motions to dismiss are settled, economically rational plaintiffs' lawyers will deduce that the applicable pleading standard by which the case must pass to reach a settlement should impact their choice of where to file it. That is, if court *A* can be expected to apply a more stringent threshold for

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Circuit, which adheres to the more liberal "substantial participant" standard whereby liability attaches to accountants who knowingly draft, edit or review reports they know are false and will be released to the public. *See, e.g., In re Software Toolworks, Inc. Sec. Litig.*, 50 F.3d 615, 627, 629 (9th Cir. 1994). Divisions among the circuits also exist with respect to defining a *control person.* Both the Securities Act and the Exchange Act impose liability on those who directly or indirectly control a primary violator. In addition to reaching the firm's controlling stockholder, this provision also extends liability to senior managers, audit committee chairmen, and in some cases outside directors. However, a distinct minority of the circuits follow the lead of the Second Circuit in holding that control-person liability extends only to control persons who were "culpable participants" in the primary violator's misbehavior. *See, e.g., Boguslavsky v. Kaplan*, 159 F.3d 715, 720 (2d Cir. 1998) (determining that a control person must in "some meaningful sense" act culpably (quoting *SEC v. First Jersey Sec., Inc.*, 101 F.3d 1450, 1472 (2d Cir. 1996))); *Sharp v. Coopers & Lybrand*, 649 F.2d 175, 185 (3d Cir. 1981) (holding that the plaintiff must prove that a control person's action or inaction "'was deliberate and done intentionally to further the fraud'" (quoting *Rochez Bros., Inc. v. Rhoades*, 527 F.2d 880, 890 (3d Cir. 1975))). Most circuits are like the Ninth Circuit and do not premise control-person liability on a showing of complicity by the control person. *See Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1575 (9th Cir. 1990) (en banc); *see also Harrison v. Dean Witter Reynolds, Inc.*, 974 F.2d 873, 880–81 (7th Cir. 1992); *Metge v. Baehler*, 762 F.2d 621, 630 (8th Cir. 1985); *Herm v. Stafford*, 663 F.2d 669, 684 (6th Cir. 1981); *G.A. Thompson & Co., Inc. v. Partridge*, 636 F.2d 945, 957–58 (5th Cir. 1981).

Even questions of proving the materiality of a misrepresentation elicit differences between the circuits. For example, the Ninth Circuit does not require an observable change in a firm's security price to support an allegation that the representation was materially misleading. *See No. 84 Employer-Teamster Joint Council Pension Trust Fund v. Am, W. Holding Corp.*, 320 F.3d 920 (9th Cir. 2003) (determining that other events in the market may muffle or distort prices on the day the allegedly false report was released). In contrast, the United States Court of Appeal for the Third and Fourth Circuits require this type of evidence. *Glaser v. Enzo Biochem, Inc.*, 464 F.3d 474, 479 (4th Cir. 2006); *In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410 (3d Cir. 1997). In sum, there are numerous circuit splits that prevent the federal securities remedies available to investors from being uniform so that class counsel can be expected to take into account these considerations in determining where to file suit.

17. *See* Securities Exchange Act of 1934, ch. 404, sec. 27, 48 Stat. 881, 902–03 (codified as amended at 15 U.S.C. § 78aa) (providing that suit can be brought in any federal district court "wherein the defendant is found or is an inhabitant or transacts business").

pleadings than court *B*, then all other things being equal, the plaintiffs' counsel will choose to file cases in court *B* where they have the greater likelihood of survival. Stringent pleading standards might thus be an important factor in plaintiffs' counsels' choice of forum.

An alternative hypothesis is that defendants are not without recourse should the selected forum place them at a substantive disadvantage or visit serious practical inconvenience to them. The well-established doctrine of forum non conveniens, now subsumed in the statutory change of venue provision in 28 U.S.C. § 1404,[18] is available to defendants who believe the plaintiff's initial choice of forum poses substantial burdens on them. Moreover, when multiple complaints are filed, as is frequently the case, and one plaintiffs' attorney selects an inconvenient forum for the corporation while a second plaintiffs' attorney files in the corporation's home district, the multi-district-litigation (MDL) panel can address opportunism via its authority to transfer the two cases to "any district for coordinated or consolidated pretrial proceedings."[19] While consolidated cases are supposed to be returned to their home jurisdiction after they finish pretrial motions and discovery, securities fraud cases rarely go to trial so they are effectively decided in the court where they are referred by the MDL system. Our conversations with several well-known plaintiffs' counsels consistently reflected their view that it is impractical for them to engage in forum shopping due to the strong likelihood that their choice of a venue that is

18. Section 1404 is a statutory recognition of the common-law doctrine and provides "[f]or the convenience of parties and witnesses, in the interest of justice, a district court may transfer any civil action to any other district or division where it might have been brought." 28 U.S.C. § 1404. Of interest in the class-action context is that convenience to the class representative carries less weight than in nonrepresentative suits. *See, e.g.*, *In re Nematron Corp. Sec. Litig.*, 30 F. Supp. 2d 397, 400, 405–07 (S.D.N.Y. 1998) (giving a securities class action's lead plaintiff's choice of forum little a weight in decision to relocate suit to another state).

19. 28 U.S.C. § 1407. Pursuant to section 1407, the Judicial Panel on Multidistrict Litigation can temporarily transfer two or more civil actions "involving one or more common questions of fact" to a single "district for coordinated or consolidated pretrial proceedings." *Id.* If the defendant moves for the transfer to the MDL panel, the defendant has the burden of persuasion that the transfer meets the criteria of section 1407. *See In re Advantage Investors Mortgage Corp. Mortgage Fund Litig.*, 268 F. Supp. 2d 1379, 1380 (J.P.M.L. 2003). An earlier study found that most transferred actions are terminated in the transferee court by some form of pretrial disposition. *See* Patricia D. Howard, *A Guide to Multidistrict Litigation*, 124 F.R.D. 479, 480 (1989) (reporting that only about 18 percent of the cases were ultimately remanded to their original court). While there is some uncertainty whether section 1407 permits the transferee court to rule on forum-non-conveniens issues, the transferee courts do, from time to time, grant motions pursuant to section 1404. *See, e.g.*, *In re Gen. Instrument Corp. Sec. Litig.*, No. 96 C 1129, 1999 U.S. Dist. LEXIS 11147, at *24–25 (D. Ill. June 17, 1999) (granting a section 1404(a) motion to transfer seven securities class actions after they were consolidated for pretrial proceedings).

removed from the defendant firm's principal place of business will be immediately followed by a successful (not to mention expensive and time consuming) defendant's motion to relocate the suit. Hence, rather than engage in a futile act, they file suit initially in the defendant company's home district.

Our empirical analysis examines a large number of settlements in securities class actions, dividing the settlements into discrete groups according to the applicable approach to satisfying the strong-inference requirement that was followed in the circuit in which the settled case was litigated. We examine whether settled cases are filed in forums that are geographically remote to the defendant company's principal place of business. We find that 85 percent of the securities fraud class actions in our sample are filed in the home circuit of the defendant corporation. In the remainder of cases, those that are filed outside the defendant's home jurisdiction, our analysis shows that differences in the pleading standards do not explain a statistically significant amount of the reason for that decision.

While the differences in the circuits' pleading standards do not have a statistically significant impact on the plaintiffs' choice of venue, we find that plaintiffs are more likely to file low-value cases in jurisdictions other than the one in which the defendant's headquarters is located. Further, we find that cases with smaller provable losses and without an accompanying Securities and Exchange Commission (SEC) investigation are statistically significantly more likely to be filed in circuits other than where the defendant's principal place of business is located. We interpret the former result as consistent with the hypothesis that in lower-value cases, plaintiffs' counsel is more likely to select jurisdictions that are convenient to themselves rather than to the defendant. It may also reflect defendants' reluctance to engage in costly forum selection motions in cases where it is cheaper to settle the case. Conversely, when an SEC investigation is proceeding on the basis of the same operative facts, our results are consistent with the claim that plaintiffs' counsel will avoid filing outside of the defendant corporation's home jurisdiction to avoid procedural delays. Overall, we conclude that our findings support the view that the federal circuits' differing approaches to interpreting the PSLRA's pleading standard do not contribute to forum shopping by plaintiffs' counsel.

These results provide important background information for evaluating the social-welfare implications of *Tellabs*. Our data is consistent with the view that *Tellabs* should be evaluated largely on the technical basis of whether it leads to a more uniform interpretation of the federal securities laws. We argue that *Tellabs* should be viewed as gently nudging the judicial system in the direction of a more uniform

interpretation of the federal securities laws, while at the same time not announcing a single standard, let alone a clarion one.

The organization of our analysis is straightforward. In Part I, we provide a close examination of *Tellabs* as well as the quilt of case law that the PSLRA spawned with respect to the federal courts' approaches to applying the strong-inference pleading requirement. In Part II we examine filing, dismissal, and settlement patterns for federal securities class actions. We next turn, in Part III, to determining whether plaintiffs' attorneys in these cases engage in any forum shopping, and if so, whether the more stringent pleading standards applied by some circuits appear to affect plaintiffs' decisions about where to file these cases. The full implications of our findings on *Tellabs* and the future conduct of securities litigation are set forth in the concluding section.

I. THE PLEADING MÉLANGE

Even before the PSLRA, circuits varied in their approaches to applying Rule 9(b)'s requirements that "[i]n alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake," and that "[m]alice, intent, knowledge, and other conditions of a person's mind may be alleged generally."[20] For example, prior to the PSLRA, Rule 9(b)'s particularity requirement enjoyed at best a drive-by quality in the United States Court of Appeals for the Ninth Circuit since its approach required only that the plaintiff set forth a description of the facts or circumstances alleged to constitute fraud, coupled with a conclusory statement that the facts and circumstances were fraudulent.[21] This essentially permitted complaints in the Ninth Circuit to survive motions to dismiss without setting forth any particular facts regarding the defendant's state of mind. In contrast,

20. Fed. R. Civ. P. 9(b). The 1937 advisory committee notes on Rule 9(b) are limited to: "See *English Rules Under the Judicature Act* (The Annual Practice, 1937) O. 19, r.22." *See* 2 JAMES WM. MOORE ET AL., MOORE'S FEDERAL PRACTICE 9 app. 02 (3d ed. 2008). The text of Rule 9(b) has remained unchanged by subsequent amendments. *See* Christopher M. Fairman, *An Invitation to the Rulemakers—Strike Rule 9(b)*, 38 U.C. DAVIS L. REV. 281, 286–87 (2004) (finding the history of Rule 9(b) to be scant and quoting the English Rules Under the Judicature Act: "'Wherever it is material to allege malice, fraudulent intention, knowledge, or other condition of the mind of any person, it shall be sufficient to allege the same as a fact without setting out the circumstances from which the same is to be inferred . . . . Fraud must be distinctly alleged and proved. The acts alleged to be fraudulent must be stated otherwise no evidence in support of them will be received,'" and quoting the architect of the Rules, Judge Clark's explanation for Rule 9(b): "'While useful, this rule probably states only what courts would do anyhow and may not be considered absolutely essential.'")

21. *See, e.g.*, *In re GlenFed, Inc. Sec. Litig.*, 42 F.3d 1541, 1546–49 (9th Cir. 1994) (en banc).

the United States Court of Appeals for the Second Circuit maintained the most demanding approach under Rule 9(b), requiring that not only could fraud not be alleged via conclusory allegations, but that the complaint's specific allegations of fraud must create a "'strong inference' of fraudulent intent."[22] This interpretation was later refined when the Second Circuit embraced two broad alternative means by which a complaint could plead a strong inference of scienter; the complaint could either plead facts alleging a "motive and opportunity" on the part of the defendant to commit a misrepresentation, or plead "facts that constitute strong circumstantial evidence of conscious misbehavior or recklessness."[23]

In enacting the PSLRA, Congress opted for the Second Circuit's strong-inference standard, believing this was necessary to curb the frequency of baseless securities class actions that were being filed to extort recoveries as a consequence of lax procedural protections of defendants. However, the PSLRA's legislative history was at best equivocal as to whether Congress intended to adopt the Second Circuit's judicial approach, namely motive and opportunity, in applying the new pleading standard, or instead believed that the strong-inference standard should be applied with even greater rigor than it had been applied by the Second Circuit. For example, on the one hand, the Senate Banking Committee's report accompanying the PSLRA states "courts may find . . . [the Second Circuit] law instructive" in construing the new pleading requirement.[24] On the other hand, the Conference Committee Report appears to reject the Second Circuit's interpretation by observing, "Because the Conference Committee intends to strengthen existing pleading requirements, it does not intend to codify the Second Circuit's case law interpreting this pleading standard."[25] The report proceeds, "For this reason, the Conference Report chose not to include in the pleading standard certain language relating to motive, opportunity, or recklessness."[26] President Bill Clinton's veto of the bill was in response to his concern that Congress intended the pleading standard to be more rigorous than the Second Circuit's approach.[27] In the debate leading up to the successful override

22. *In re Time Warner Inc. Sec. Litig.*, 9 F.3d 259, 268 (2d Cir. 1993) (quoting *O'Brien v. Nat'l Prop. Analysts Partners*, 936 F.2d 674, 676 (2d Cir. 1991)).

23. *Shields v. Citytrust Bancorp, Inc.*, 25 F.3d 1124, 1128–30 (2d Cir. 1994).

24. S. REP. NO. 104-98, at 15 (1995).

25. H.R. REP. NO. 104-369, at 41 (1995) (Conf. Rep.).

26. *Id.* at 41 n.23.

27. *See* 141 CONG. REC. H15215 (daily ed. Dec. 20, 1995) (showing that President Clinton expressed his desire for a high pleading standard and found the balance struck in the Second Circuit optimal, but believed that the standard embraced in

of the president's veto, the Senate managers professed their admiration for the Second Circuit's standard;[28] their new found affinity for the Second Circuit's standard may well have reflected the political necessity for moderation, since the Senate ultimately overrode the veto with only a two-vote margin.[29] What emerged in the ensuing decade from this politically expedient ambiguity were three distinct approaches to interpreting the strong-inference standard: the Ninth Circuit standard, the Second Circuit standard, and an intermediate standard.

Reflecting a complete reversal from its pre-PSLRA position, the Ninth Circuit adopted the most demanding standard by which the securities class-action complaint must set forth facts creating a strong inference of fraud. After its 1999 decision in *In re Silicon Graphics Inc. Securities Litigation*,[30] the court determined the plaintiff needed to plead facts that created a strong inference that the defendant knew the statements were false, or that the defendant was consciously or deliberately reckless in disregarding the truth or falsity of the statements.[31] No other circuit has joined the Ninth Circuit in this

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the PSLRA would "raise the standard even beyond that level" with the consequence that meritorious cases would not be heard).

28. *See, e.g.*, 141 CONG. REC. S19150 (daily ed. Dec. 22, 1995) (statement of Sen. Domenici) (stating that the PSLRA's pleading standard "is the Second Circuit's pleading standard"); 141 CONG. REC. S19068 (daily ed. Dec. 21, 1995) (statement of Sen. Dodd) (asserting that the PSLRA met the Second Circuit's standard and that courts could be expected to look to the Second Circuit opinions for guidance in interpreting the PSLRA's pleading standard); *see also* 141 CONG. REC. H15219 (daily ed. Dec. 20, 1995) (statement of Rep. Lofgren) (stating that the Second Circuit's standard was embodied in the PSLRA). These professions are at odds with the earlier adoption by the Senate of an amendment sponsored by Senator Specter expressly incorporating the Second Circuit's criteria into the PSLRA. *See* 141 CONG. REC. S9222 (daily ed. June 28, 1995). This provision was, however, removed in the ensuing conference between the differing House and Senate versions. *See* H.R. REP. NO. 104-369, at 1-30 (showing that the bill emerging from the Conference Committee did not include the provision sponsored by Senator Specter). In place of the Specter amendment was the Conference Committee's statement that "[b]ecause the Conference Committee intends to strengthen existing pleading requirements, it does not intend to codify the Second Circuit's case law interpreting this pleading standard." *Id.* at 41. For a close review of the PSLRA's legislative history, see Michael B. Dunn, Note, *Pleading Scienter After the Private Securities Litigation Reform Act: Or, a Textualist Revenge*, 84 CORNELL L. REV. 193, 243-44 (1998) (concluding that Congress did not intend to address whether recklessness could give rise to liability, but rather wished to address only the pleading issue).

29. Professors Grundfest and Pritchard cogently develop the view that not just the Congress but the courts benefit from ambiguity, finding something of a symbiotic relationship each has in adhering to the necessity of ambiguity of outcome as often the necessity for reaching legislative consensus. *See* Joseph A. Grundfest & A.C. Pritchard, *Statutes with Multiple Personality Disorders: The Value of Ambiguity in Statutory Design and Interpretation*, 54 STAN. L. REV. 627, 649 (2002).

30. 183 F.3d 970 (9th Cir. 1999).

31. *See, e.g.*, *id.* at 974.

approach, and, as we shall see, the Ninth Circuit itself appears to be backing away from this standard after the *Tellabs* decision.

The Second Circuit, believing its earlier position had been codified by the PSLRA, continues to follow its prior approach,[32] joined by the United States Court of Appeals for the Third[33] and Eighth[34] Circuits. Most circuits position themselves between the Ninth and Second Circuit positions, hence embracing an intermediate standard, embracing what can be understood as a motive-and-opportunity-plus approach.[35] Under this intermediate standard, motive and opportunity alone do not necessarily suffice to establish a strong inference of fraudulent behavior; they customarily require factual allegations that bear on matters other than motive and opportunity for a complaint to withstand a motion to dismiss.

There were several reasons for expecting that the PSLRA's pleading standard would find its way to the Supreme Court. For one, a split among circuits on an important legal issue always makes a grant of certiorari more likely. But even more compelling to some justices may have been the oft-stated view that the PSLRA's fundamental objective of curbing the frequency of securities class actions had been impeded by the lower courts' misapplication of the pleading standard.[36] Indeed, a

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32. *See, e.g., Press v. Chem. Inv. Servs.*, 166 F.3d 529, 537–38 (2d Cir. 1999) (citing support from case law adopted before the passage of the PSLRA).

33. *See In re Advanta Corp. Sec. Litig.*, 180 F.3d 525, 534–35 (3d Cir. 1999).

34. *See Fla. State Bd. of Admin. v. Green Tree Fin. Corp.*, 270 F.3d 645, 659–61 (8th Cir. 2001).

35. *See Makor Issues & Rights, Ltd. v. Tellabs Inc.*, 437 F.3d 588, 601 (7th Cir. 2006); *Ottman v. Hanger Orthopedic Group, Inc.*, 353 F.3d 338, 344–45 (4th Cir. 2003); *Nathenson v. Zonagen Inc.*, 267 F.3d 400, 406–11 (5th Cir. 2001); *City of Philadelphia v. Fleming Cos., Inc.*, 264 F.3d 1245, 1249, 1259, 1261–62 (10th Cir. 2001); *Greebel v. FTP Software, Inc.*, 194 F.3d 185, 188, 194–95, 198–200 (1st Cir. 1999); *In re Comshare, Inc. Sec. Litig.*, 183 F.3d 542, 549 (6th Cir. 1999); *Bryant v. Avado Brands, Inc.*, 187 F.3d 1271, 1283, 1287 (11th Cir. 1999).

36. *See, e.g.*, Perino, *supra* note 14, at 915–16, 929, 942–47 (reviewing 1499 securities class actions filed between 1996 and 2001 and concluding that the Second Circuit and intermediate standards contributed to there being as many, or even more, filings after the PSLRA's enactment than were filed before). This is not to say that the pleading standard has not had its impact. The rate of dismissals of securities fraud cases has nearly doubled since the passage of the PSLRA. *Compare* RONALD I. MILLER ET AL., NERA ECON. CONSULTING, RECENT TRENDS IN SHAREHOLDER CLASS ACTION LITIGATION: BEYOND THE MEGA-SETTLEMENTS, IS STABILIZATION AHEAD? 4 (Apr. 2006), *available at* http://www.nera.com/image/bro_recenttrends2006_sec979_ppb-final.pdf (reporting a dismissal rate of 40.3 percent for securities class actions filed from 1998 to 2003), *with* ELAINE BUCKBERG ET AL., NERA ECON. CONSULTING, RECENT TRENDS IN SHAREHOLDER CLASS ACTION LITIGATION: ARE WORLDCOM AND ENRON THE NEW STANDARD? 3 (July 2005) (finding a dismissal rate of 20.3 percent for securities class actions filed from 1991 to 1995).

high-level theoretical debate continues to rage over whether one of the contributing forces to the feared lack of competitiveness of U.S. capital markets is the serious risk of securities class actions faced by public companies.[37] The Supreme Court's disposition of *Tellabs* was therefore anticipated, and eagerly so, in many quarters.

Tellabs was litigated under the intermediate standard adopted by the Seventh Circuit. The complaint focused on a series of misstatements committed by the CEO of Tellabs, Inc., Richard C. Notebaert. The misstatements ran the gamut from claims of high consumer demand for its flagship product, assertions of growing demand for a new product that was represented to be available, and statements of present and prospective revenue.[38] None of the statements were correct so that when, in early spring 2001, Tellabs announced that consumer demand had diminished and that revenues would not be as forecast, its shares dropped from $67.125 to $15.87. The district court twice dismissed the plaintiffs' suit on the ground that the complaint failed to meet the strong-inference pleading requirement with respect to Notebaert's state of mind. The district court believed that the plaintiffs' allegations that Notebaert attended numerous meetings and participated in phone calls concerning the status of Tellabs's products did not establish scienter since no details of the meetings or calls were alleged.[39]

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37. *See* COMM. ON CAPITAL MKTS. REGULATION, INTERIM REPORT OF THE COMMITTEE ON CAPITAL MARKETS REGULATION 11–15, 18 (Nov. 30, 2006), *available at* http://www.capmktsreg.org/pdfs/11.30Committee_Interim_ReportREV2.pdf (calling for a variety of substantive reforms in the antifraud rule to provide greater clarity and fewer private suits, including the introduction of alternative-dispute mechanisms such as arbitration). One need look no further than a recent Supreme Court decision to find similar expressions of the harm securities litigation does to U.S. global competitiveness. *See Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 128 S. Ct. 761, 766, 773–74 (2008) (rejecting a scheme-liability approach to reach third-party vendors who knowingly participate in a plan to inflate their vendee's revenues).

38. Specifically, the plaintiffs set forth four principal misstatements. First, the plaintiffs stated that demand for the company's existing flagship product, the TITAN 5500, was continuing to grow, when in fact it was declining. Second, they stated that the new-generation TITAN 6500 was available for delivery and was experiencing strong demand; in fact, the product was not available and demand was weak. Third, Notebaert's representations regarding fourth-quarter performance were misleading by failing to disclose they entailed "channel stuffing" practices whereby product shipments did not represent true sales of the quarter. Fourth, Notebaert overstated revenue projections by failing to reflect in his estimates the weakening demand for the TITAN 5500 and the delays in introducing the TITAN 6500.

39. *Johnson v. Tellabs, Inc.*, 303 F. Supp. 2d 941, 968 (N.D. Ill. 2004) (finding that plaintiffs' allegations that Notebaert attended a late April meeting in which he explained that Tellabs's SALIX technology was outdated failed to even support an inference of negligence or recklessness because it was consistent with an early-April public disclosure announcing the termination of the SALIX product line).

The Seventh Circuit reversed,[40] stating that the strong-inference standard called on the court to review all the inferences that could be drawn from the complaint and to deny a motion to dismiss "if it alleges facts from which, if true, a reasonable person could infer that the defendant acted with the required intent."[41] The panel reasoned, in part, that in light of the flagship product's significance to Tellabs and the number of internal reports that the product was experiencing problems, it could be reasonably inferred that Notebaert knew his optimistic statements were false.[42] The court reached similar conclusions with the false representations of availability and demand for the next-generation product.[43] As for the false representation of revenues, the panel believed sufficient facts had been alleged to establish that Notebaert was aware that the firm engaged in "channel stuffing" to inflate revenues.[44] Finally, Notebaert's scienter with respect to revenue projections was also believed to have been sufficiently pled since future performance was dependent upon success of the flagship and next-generation products, and facts circumstantially suggested he knew these facts were contrary to his optimistic projections.[45]

The Supreme Court reversed, holding that the Seventh Circuit had applied too low a standard. It reasoned that a strong inference required the strength of the inference to be "powerful or cogent,"[46] and not merely "reasonable" or "permissible."[47] The Court elaborated that "a

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40. *Makor*, 437 F.3d at 605.

41. *Id.* at 602 (asserting that when a court is "'[f]aced with two seemingly equally strong inferences, one favoring the plaintiff and one favoring the defendant, it is inappropriate for [a judge] to make a determination as to which inference will ultimately prevail'" because that would "'invade the traditional role of the factfinder.'" (quoting *Pirraglia v. Novell, Inc.*, 339 F.3d 1182, 1188 (10th Cir. 2003))).

42. *Id.* at 603 (finding that internal reports in March 2001 indicated the market for the TITAN 5500 was drying up, "[y]et in April 2001, Notebaert told financial analysts that 'everything we hear from the customers indicates that our in-user demand for services continues to grow.'").

43. *Id.* at 604–05 (finding that plaintiffs pleaded sufficient facts to support a strong inference that Notebaert knowingly lied when he informed investors that the TITAN 6500 was available and being shipped, when in fact the product was not ready for deployment).

44. *Id.* (relying on the plaintiffs' evidence suggesting that Notebaert knew about the channel stuffing and even allegedly "'worked directly with Tellabs's sales personnel' to effect the channel stuffing" and determining that the plaintiffs' "complaint contain[ed] enough detail to establish a strong inference that Notebaert knew of the channel stuffing and therefore knew Tellabs had exaggerated its fourth quarter 2000 revenues.").

45. *Id.* at 605.

46. *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 127 S. Ct. 2499, 2502, 2510 (2007).

47. *Id.*

court must consider plausible nonculpable explanations for the defendant's conduct, as well as inferences favoring the plaintiff"[48] so that the allegations of scienter "must be cogent and compelling, thus strong in light of other explanations."[49] To be noted here is that it is not enough that the facts more likely than not support an inference of scienter; what the court also requires is that the inference meet a standard of persuasion, which the Court stated required an inference of scienter that was "cogent and compelling," not just "reasonable and permissible."[50] Whether the complaint meets this requirement is to be determined based on the totality of the allegations.[51] While acknowledging that the defendant's motive, such as personal gain, is a relevant consideration, the particular significance of motive in supporting an allegation of scienter "depends on the entirety of the complaint."[52] Most importantly, the Court disagreed with the Seventh Circuit's conclusion that this evaluation by the presiding judge would violate the plaintiffs' Seventh Amendment guarantee to a jury trial.[53] The Court held that the PSLRA did not change the procedures for treating motions to dismiss pursuant to Rule 12(b)(6) whereby the plaintiff's allegations are assumed to be true.[54] Thus, the evaluation engaged in by the judge is merely to assure that the plaintiff has met the conditions for properly lodging a complaint with the court, a matter it believed was within Congress's constitutional authority, and not a disposition on the merits for which there is a constitutional right to a jury trial.[55]

It is difficult to fully assess *Tellabs*'s likely impact on the future conduct of securities litigation.[56] One inescapable conclusion is that a bare allegation of motive and opportunity will not meet *Tellabs*'s call for a cogent and compelling inference, potentially casting doubt on the

48. *Id.* at 2502.

49. *Id.*

50. *Id.* at 2502, 2510. On this point, consider the Court's statement: "When the allegations are accepted as true and taken collectively, would a reasonable person deem the inference of scienter at least as *strong* as any opposing inference?" *Id.* at 2511 (emphasis added). Note the Court's earlier construction of *strong*.

51. *Id.* at 2509, 2511.

52. *Id.* at 2511.

53. *Id.* at 2511-12.

54. *Id.* at 2502, 2504, 2512-13.

55. *Id.* at 2512-13.

56. On remand, Judge Posner reversed the order of considering "cogent" and "compelling," reasoning that the latter being a quantitative standard should be considered first as in many instances (particularly when there are but two possible inferences, the one favoring the plaintiffs' version of the facts being more persuasive), that which is compelling will be also cogent. *See Makor Issues & Rights, Ltd. v. Tellabs Inc.*, 513 F.3d 702, 705, 707, 710 (7th Cir. 2008).

continued viability of the Second Circuit standard. But a close review of Second Circuit decisions reveals that motive and opportunity were far from an automatic talisman for meeting the strong-inference standard.[57] Thus, if this were to be *Tellabs*'s contribution, it would have minimal effect. We believe *Tellabs*'s salience within securities litigation will come from its call for courts to focus on *all* aspects of the complaint, its requirement that inferences are to be drawn both for and against the plaintiff, and its enunciation of a somewhat malleable meaning for *strong*. In the end, the impact of each of these innovations depends heavily on not just the facts of the individual case but equally so on the particular perspective of the presiding judge.

Moreover, *Tellabs*'s call to examine the entire pleadings before the court appears at this time to impact the somewhat narrower, categorical considerations of factors that preceded *Tellabs*. This conclusion is no clearer than its impact on the Ninth Circuit, where in *South Ferry L.P., #2 v. Killinger*,[58] the Ninth Circuit correctly interpreted *Tellabs*'s call for considering all reasonable inferences to be drawn from the facts to permit general allegations related to the overall operations of the defendant firm to satisfy pleading scienter on the part of the firm's officers.[59] Indeed, *Killinger* reverses the Ninth Circuit's earlier *Silicon Graphics* decision's approach of not considering allegations that were viewed as either vague or ambiguous, relying on *Tellabs*'s call that the pleadings be considered in their totality.[60]

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57. *See Ganino v. Citizens Utils. Co.*, 228 F.3d 154, 170 (2d Cir. 2000) (asserting that with respect to motive, "[g]eneral allegations that the defendants acted in their economic self-interest are not enough"); *Fishbaum v. Liz Claiborne, Inc.*, No. 98-9396, 1999 WL 568023, at *4 (2d Cir. 1999) ("[N]o inference of scienter should be drawn from insider trading activity unless that activity is unusual."); *Chill v. Gen. Elec. Co.*, 101 F.3d 263, 268 (2d Cir. 1996) (stating that the alleged motive must entail concrete benefits that could be realized by one or more of the alleged false statements or wrongful nondisclosures, and additionally that "[t]he motive to maintain the appearance of corporate profitability, or of the success of an investment, will naturally involve benefit to a corporation, but does not 'entail concrete benefits'" (quoting *Shields v. Citytrust Bancorp, Inc.*, 25 F.3d 1124, 1130 (2d Cir. 1994))).

58. 542 F.3d 776 (9th Cir. 2008).

59. *Id.* at 783–84.

60. *Id.* at 784. According to *Killinger*:

> [A]llegations regarding management's role in a company may be relevant and help to satisfy the PSLRA scienter requirement in three circumstances. First, the allegations may be used in any form along with other allegations that, when read together, raise an inference of scienter . . . . Second, such allegations may independently satisfy the PSLRA where they are particular and suggest that defendants had actual access to the disputed information . . . . Finally, such allegations may conceivably satisfy the PSLRA standard in a more bare form, without accompanying particularized allegations, in rare circumstances where the nature of the relevant fact is of such

While the question of whether it is appropriate to draw inferences against, not just for, the plaintiff is new to the case law,[61] we suspect that the rather recent development of this idea by courts was merely bringing to the foreground what had been occurring all along; judges considering motions to dismiss regularly evaluated *sub silentio* the permissible inferences against the inferences the plaintiff proposed, drawing from the pled facts.[62] Thus, we are not at all persuaded that, post-*Tellabs*, all three of the earlier purportedly different approaches will not persist. Indeed, since *Tellabs* deftly avoided choosing from among the three competing approaches, clothing the standard with malleable expressions such as cogency and compelling while inviting consideration of all factual allegations and asking for inferences to be drawn both for and against the plaintiff, the opinion does not provide a clear method for choosing among the mélange of tests currently employed by the different circuits.

The implication of this is it is even more important today to empirically assess whether securities class-action litigation involves opportunistic forum shopping. We therefore turn next to this important issue.

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prominence that it would be "absurd" to suggest that management was without knowledge of the matter.

Id. at 785–86.

61. Lower courts divided on this issue along the same lines as they did on the role that motive and opportunity should play. Thus, courts falling into the intermediate-standard position held that the approach to competing inferences is to select the "most plausible" of the competing inferences. *See In re Credit Suisse First Boston Corp.*, 431 F.3d 36, 49 (1st Cir. 2005); *Fidel v. Farley*, 392 F.3d 220, 227 (6th Cir. 2004) (holding that a strong inference of scienter exists when the guilty inference is more credible than an innocent inference); *Ottman v. Hanger Orthopedic Group, Inc.*, 353 F.3d 338, 350 (4th Cir. 2003). This language also is similar to the approach taken in the Ninth Circuit pursuant to its most demanding pleading standard. *See Gompper v. VISX, Inc.*, 298 F.3d 893, 896–97 (9th Cir. 2002). Somewhat related to this most-plausible-inference standard is the more generalized guidance that the strength of the inference is to be determined from the "overall context" of the facts alleged. *See Pirraglia v. Novell, Inc.*, 339 F.3d 1182, 1187 (10th Cir. 2003); *In re K-tel Int'l, Inc. Sec. Litig.*, 300 F.3d 881, 889 n.6 (8th Cir. 2002). These various approaches appear to involve insignificant differences among them, and each appears consistent with the general statements announced by the Supreme Court in *Tellabs*. The Seventh Circuit adopted none of these approaches in its decision and substituted a weaker test of whether "a reasonable person could infer that the defendant acted with the required intent." *Makor Issues & Rights, Ltd. v. Tellabs Inc.*, 437 F.3d 588, 602 (7th Cir. 2006).

62. *See, e.g., In re Credit Suisse First Boston Corp.*, 431 F.3d at 51 (finding that Rule 12(b)(6) "does not require the court, in a PSLRA case, to turn a blind eye to the universe of possible conclusions stemming from a given fact or set of facts"); *Pirraglia*, 339 F.3d at 1187 ("Whether an inference is a strong one cannot be decided in a vacuum.").

II. DO PLAINTIFFS' LAWYERS ENGAGE IN FORUM SHOPPING?

Tellabs leaves us in a world where different circuits will apply different standards to resolve federal securities law cases. Given these differences, economically rational plaintiffs' attorneys might try to maximize the value of the cases they file by selecting the most favorable jurisdiction for their cases. Given the liberal venue provisions of the federal securities laws, plaintiffs' counsel has essentially unlimited choices of where to file, subject to the previously described governors of the forum-non-conveniens doctrine and the consolidation authority of the MDL panel.

Prior scholarship has hypothesized that a plaintiffs' attorney has a portfolio of cases that he or she will file in one of a number of jurisdictions across the country, taking advantage of the liberal venue provisions of the federal securities laws.[63] If true, there would be several important considerations that bear on this filing decision: location of the defendant company, location of the law firm, location of witnesses and documents, and perhaps most importantly, the attorney's perception of how receptive a court is to securities fraud cases.[64] The pleading standard of fraud employed by a particular court undoubtedly bears heavily in weighing this final factor. In simple economic terms, if the attorney can select any venue, then she will choose, on an ex ante basis, the jurisdiction where the expected value of the suit is highest. Stricter pleading standards should increase the likelihood of dismissal of the case, all other things being equal, so that plaintiffs should seek to file in jurisdictions with the weakest fraud-pleading standards. The key to settlement is to survive a motion to dismiss and the odds of doing so may be much better in some circuits than in others.

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63. *See* Perino, *supra* note 14, at 947–48. One commentator on this Paper suggested that it would be interesting to examine the decision to file suit in the first place. While on a theoretical basis we agree that this would add some interesting insights, as a practical matter we have no way of counting the number of suits that were not filed.

64. We are not writing on a blank slate. The president who appointed the judge to the court and the frequency of securities class actions in that jurisdiction are among the variables Professors Grundfest and Pritchard found in the courts' choice of pleading standard. *See* Grundfest & Pritchard, *supra* note 29, at 635. Professors Pritchard and Sale find that the nature of the misrepresentation, for example, a forward looking statement, is correlated with the likely success of a motion to dismiss. *See* A.C. Pritchard & Hillary A. Sale, *What Counts as Fraud? An Empirical Study of Motions to Dismiss Under the Private Securities Litigation Reform Act*, 2 J. EMPIRICAL LEGAL STUD. 125, 146 (2005) (analyzing cases from the Second and Ninth Circuits to conclude that allegations of accounting violations are more likely to survive the pleading requirements in the former than the latter).

However, this thesis neglects a very important institutional feature of the federal judicial system: the MDL panel and change-of-venue provisions in section 1404. As we discussed in Part I, if multiple class actions are filed in different jurisdictions all alleging securities fraud arising out of the same set of operative facts, the MDL panel will determine which court will handle all of these cases. This process will result in significant delays and costs for plaintiffs' counsel, and most likely lead to all of the cases being consolidated in the defendant corporation's home jurisdiction. Similarly, if only one suit is filed, but it is filed outside of the defendant's home circuit, the defendant will likely file a motion for change of venue on the grounds that it will be most efficient to litigate the case where all of the main witnesses, the defendant's officers, and most of the documents are located.

This leads us to our alternative hypothesis: that plaintiffs file in the defendant corporation's home circuit in order to avoid having their cases transferred into the MDL-panel system or having to face the company's motion for a change of venue. If this is correct, then we should see that a high percentage of cases are filed in the corporation's home circuit, and that the differences in pleading standards have little effect on the choice of where to file. However, the general tendency may be offset in some cases by other considerations, such as the convenience of the plaintiffs' counsel, or the cost-benefit ratio for the plaintiffs' law firm in litigating a low-value case far from their own home.

We begin by trying to provide some empirical background on the scope of the differences between circuits so as to provide a general overview of where securities fraud class actions are filed, how the different circuits generally treat motions to dismiss, and the likelihood of settlement of the case if it survives a motion to dismiss. Table 1 provides a general overview of the filing, dismissal, and settlement of securities fraud class actions for all circuits. We constructed this table using data from the RiskMetrics (formerly Institutional Shareholder Services) database on securities fraud class-action settlements.[65] We note that the data for 1993 are incomplete as many cases were not entered into the RiskMetrics database at that time

65. We would like to thank RiskMetrics for providing us with access to this database. We would also like to thank NERA Economic Consulting for providing similar data on class-action filings from their database of securities fraud class-action settlements. We choose to use the RiskMetrics data in this Paper because we had more complete access to its data. We note, however, that the NERA data on case filings, while not identical to the RiskMetrics data, are quite similar.

Table 1: Securities Fraud Class Actions Filed, Settled or Dismissed 1993-2006												
Panel A: Number of Cases Filed												
Year	1st	2nd	3rd	4th	5th	6th	7th	8th	9th	10th	11th	Total
1993	2	16	5	1	2	0	3	3	18	1	4	55
1994	15	50	18	9	12	13	7	12	63	6	13	218
1995	10	34	14	3	16	14	7	3	72	8	15	196
1996	11	14	14	4	7	3	2	2	31	5	14	107
1997	8	34	12	2	7	7	9	8	56	3	24	170
1998	14	51	23	8	25	12	6	5	59	7	25	235
1999	12	32	18	11	25	10	11	10	54	11	24	218
2000	17	39	21	15	13	10	13	6	51	7	22	214
2001	12	31	19	8	7	9	10	7	61	9	16	189
2002	14	81	22	6	17	15	15	17	44	5	21	257
2003	18	58	19	11	18	14	11	8	43	8	21	229
2004	10	56	23	21	17	7	12	9	68	5	22	250
2005	9	46	17	7	13	12	9	12	35	7	9	176
2006	8	35	13	5	8	6	4	6	29	3	14	131
Total	160	577	238	111	187	132	119	108	684	85	244	2645

Panel B: Number of Cases Settled												
Year	1st	2nd	3rd	4th	5th	6th	7th	8th	9th	10th	11th	Total
1993	2	14	4	1	2	0	1	3	18	1	4	50
1994	11	35	16	4	7	8	7	9	48	6	10	161
1995	9	25	13	3	10	13	3	3	55	8	11	153
1996	8	8	12	1	6	1	2	1	19	3	8	69
1997	8	24	6	1	5	6	8	6	38	1	14	117
1998	6	33	18	3	15	12	4	3	35	4	12	145
1999	9	15	11	6	13	5	5	4	26	11	17	122
2000	9	22	13	9	7	6	10	1	30	7	12	126
2001	8	19	13	2	2	2	8	6	38	8	10	116
2002	7	45	9	1	9	10	7	9	22	3	9	131
2003	5	16	9	3	8	7	2	4	17	4	12	87
2004	6	15	4	4	5	1	4	4	24	3	9	79
2005	3	10	4	1	3	1	2	3	6	3	2	38
2006	2	1	1	0	2	0	0	0	1	0	0	7
Total	93	282	133	39	94	72	63	56	377	62	130	1401

Panel C: Number of Cases Dismissed												
Year	1st	2nd	3rd	4th	5th	6th	7th	8th	9th	10th	11th	Total
1993	0	2	1	0	0	0	2	0	0	0	0	5
1994	4	12	2	5	5	4	0	3	13	0	3	51
1995	1	8	1	0	6	1	4	0	15	0	3	39
1996	3	5	2	3	1	2	0	1	12	2	6	37
1997	0	10	6	1	2	0	1	2	16	1	10	49
1998	8	10	5	5	9	0	2	2	23	3	13	80
1999	3	14	5	5	11	5	6	6	27	0	6	88
2000	5	14	8	6	6	4	2	2	17	0	10	74
2001	3	5	3	6	2	4	1	1	18	1	3	47
2002	6	19	7	4	4	4	4	6	12	1	9	76
2003	8	18	1	5	7	2	4	4	15	1	5	70
2004	1	15	6	3	5	6	3	2	25	1	6	73
2005	3	12	3	2	8	3	3	6	20	1	2	57
2006	0	2	2	1	0	1	1	2	1	0	3	13
Total	45	146	52	46	60	36	33	37	214	11	79	759

The most salient feature of these data is the large number of cases filed, dismissed, and settled in the Ninth and Second Circuits. These two jurisdictions are disproportionately important, with more than half of all securities fraud class actions being filed in them collectively. Table 1 reveals that the dismissal rate for cases filed in the Ninth Circuit in 1995, prior to the PSLRA, was 20.8 percent, it climbed to 34.9 percent by 2003, and in 2005, it stood at 57.1 percent. This suggests that the pleading standard matters, and likely a lot. The dismissal rate in the Second Circuit prior to the PSLRA (when it applied a more rigorous interpretation of the "particularity" requirement than the Ninth Circuit) was 23.5 percent, followed by 31 percent for cases filed in 2003, and in 2005, it was 26 percent. Thus, these back-of-the-envelope calculations suggest that dismissal rates in the Ninth Circuit are significantly higher, by more than a factor of two, than in the Second Circuit. All things being equal, the plaintiffs' counsel should look more warmly on filing in the Second Circuit than the Ninth Circuit. But as our data reflect, there are serious institutional forces that retard such opportunistic behavior.

Table 2 illustrates the division of all of the cases in our sample into the five categories mentioned above. The first three groups contain the cases in our sample that were filed (and later settled) in courts under the three pleading standards for fraud: the *Silicon Graphic* standard, the intermediate standard, or the Second Circuit standard. We have approximately one hundred cases in the latter two categories and slightly fewer in our sample from the Ninth Circuit after it decided the

Silicon Graphics case. The remaining cases in our sample consist of 269 cases that were filed (and settled) after the passage of the PSLRA at the end of 1995, and 139 cases that were filed prior to the enactment of PSLRA.

Table 2: Number of Cases in Sample Subject to Different Pleading Standards

Types of Pleading Standard	# of Cases	Percent of Total
(1) *Silicon Graphics* Standard	88	12.5
(2) Intermediate Standard	101	14.4
(3) Second Circuit Standard	105	15.0
(4) Post-1995, But Before Circuit Ruled on Pleading Standard	269	38.3
(5) Pre-PSLRA Cases (Filed Before 1996)	139	19.8
Total	702	100.0

With this general overview of the sample in mind, we begin our analysis of forum shopping by examining how frequently plaintiffs' counsel seeks to file securities fraud class actions in jurisdictions other than the one where the corporation's headquarters is located. Table 3 contains three panels: Panel A presents data on the pre-PSLRA cases in our sample, Panel B covers the post-PSLRA cases, and Panel C reports the cases in our sample that were decided by one of the circuits after it issued a post-PSLRA decision selecting a fraud-pleading standard for securities fraud class actions. We explain the construction of this panel below.

Table 3: Cases Filed in/out of Defendant Corporation's Home Circuit

Panel A: Pre-PSLRA Cases

	# of Cases	Percent of Total
Cases Filed in Circuit of Incorporation	91	84.3
Cases Filed Outside Circuit of Incorporation	17	15.7
Total	108	100.0

Panel B: Post-PSLRA Cases

	# of Cases	Percent of Total
Cases Filed in Circuit of Incorporation	398	82.2
Cases Filed Outside Circuit of Incorporation	86	17.8
Total	484	100.0

Panel C: Post-Circuit Decision on Pleading Standard

	Cases Filed Away from Home Circuit	Percent
Home Circuit with *Silicon Graphics* Standard	11	13.4
Home Circuit with Intermediate Standard	14	13.9
Home Circuit with Second Circuit Standard	9	14.1
Total	34	13.8

Beginning with Panels A and B of Table 3, we see that the overwhelming percentage of cases is filed in the defendant corporation's home circuit, both pre- and post-PSLRA. In fact, we find no statistically significant differences between the two sets of data.[66] This is consistent with anecdotal evidence that we have heard from plaintiffs' attorneys who tell us that they rarely seek to file in other jurisdictions because they do not want to have their case transferred to the MDL panel and subjected to lengthy delays resulting from motions to transfer the litigation back to the corporation's home circuit. Overall, it does not appear that the PSLRA had any significant effect on this trend.

Even though most cases are filed in the corporation's home circuit, it is possible that the pleading standards in different jurisdictions matter for those cases that are filed in other jurisdictions. In order to determine if the pleading standards matter in this choice, we divide our

66. Applying a Pearson chi-square test to the difference in percentage of cases filed away from home jurisdictions during pre- and post-PSLRA periods results in a chi-square value of 0.25, and p value of 0.61. These numbers do not reject the null hypothesis of equality between the two time periods.

sample into five groups according to the pleading standard applied by the circuit where the suit was filed. In particular, we code cases that were filed in the Ninth Circuit after July 2, 1999, when that court adopted this pleading standard, as the "*Silicon Graphics* Standard"; all cases filed in the United States Court of Appeals for the First, Fourth, Fifth, Sixth, Seventh, Tenth, and Eleventh Circuits after their respective adoption date of this pleading standard[67] as the "Intermediate Standard"; and all cases filed in the United States Court of Appeals for the Second, Third, and Eighth Circuits after their respective adoption date of this standard,[68] as the "Second Circuit Standard." The remaining cases are placed into two other categories, the first containing all cases that were filed after 1995 (i.e., post-PSLRA) but before the presiding circuits had formally adopted a pleading standard, and the second one with all cases that were filed during the pre-PSLRA period (prior to January 1, 1996).

In Panel C of Table 3, we divide the cases filed outside of the corporation's home jurisdiction according to the pleading standards adopted by the home circuits. On average, we find about 14 percent of these cases are filed in other jurisdictions with minor (and insignificant) deviations among the different groupings.[69]

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67. The adoption dates are October 8, 1999, for the First Circuit, *see Greebel v. FTP Software, Inc.*, 194 F.3d 185, 197 (1st Cir. 1999); December 22, 2003, for the Fourth Circuit, *see Ottmann v. Hanger Orthopedic Group, Inc.*, 353 F.3d 338, 344 (4th Cir. 2003); September 25, 2001, for the Fifth Circuit, *see Nathenson v. Zonagen Inc.*, 267 F.3d 400, 409–10 (5th Cir. 2001); May 31, 2001, for the Sixth Circuit, *see Helwig v. Vencor, Inc.*, 251 F.3d 540, 551 (6th Cir. 2001); January 25, 2006, for the Seventh Circuit, *see Makor Issues & Rights, Ltd. v. Tellabs Inc.*, 437 F.3d 588 (7th Cir. 2006); September 7, 2001, for the Tenth Circuit, *see City of Philadelphia v. Fleming Cos., Inc.*, 264 F.3d 1245, 1261–62 (10th Cir. 2001); and September 3, 1999, for the Eleventh Circuit, *see Bryant v. Avado Brands, Inc.*, 187 F.3d 1271, 1282–83 (11th Cir. 1999).

68. The adoption dates are June 21, 2000, for the Second Circuit, *see Novak v. Kasaks*, 216 F.3d 300, 310 (2nd Cir. 2000); June 17, 1999, for the Third Circuit, *see In re Advanta Corp. Sec. Litig.*, 180 F.3d 525, 534–35 (3d Cir. 1999); and October 25, 2001, for the Eighth Circuit, *see Fla. State Bd. of Admin. v. Green Tree Fin. Corp.*, 270 F.3d 645, 659–60 (8th Cir. 2001).

69. For Part C of Table 3, applying a Pearson chi-square test for the difference in percentage of cases filed away from home jurisdiction reveals a chi-square value of 0.014, and p value of 0.99. These numbers do not suggest that the percentage of cases filed away from the home jurisdiction is significantly different among home jurisdictions with different pleading standards.

III. EMPIRICAL FINDINGS: EVIDENCE THAT CLASS-ACTION LAWYERS ARE NOT LEMMINGS

Of course, the pleading standards for fraud are not the only variables that influence filing venue choices. We need to also consider a range of other variables that might potentially influence this decision, such as the magnitude of the losses suffered by the class, the presence of a parallel SEC investigation into the violation alleged in the class action, and the presence of an institutional lead plaintiff. We obtained information relevant to these variables from a variety of sources. To obtain the identity of the suit's plaintiff, and whether there was a parallel SEC enforcement action, we used court filings, the federal courts' electronic filing service (PACER), and Lexis-Nexis databases. We then estimated the amount of damages suffered by the class during the class period, which we call *provable losses*, using the methodology that was in our earlier analysis of provable losses in securities class actions.[70]

An especially important variable is whether the suit's plaintiff is a financial institution. As mentioned above, one innovation in the PSLRA was the introduction of a mechanism whereby the court selects a lead plaintiff from competing petitioners. We coded the cases according to their lead plaintiff types; we coded any financial institution in the classic sense of an insurance company, bank, pension fund, mutual fund, endowment, or foundation as "Institutional Investors." The largest group of institutional lead plaintiffs in our sample are pension funds (including labor-union pension funds).

A. Descriptive Statistics for Control Variables

Table 4 provides information about the distribution of institutional lead plaintiffs in our sample. Several studies have found that institutional lead plaintiffs correlate with greater settlement sizes.[71] This means that we need to determine if institutional lead plaintiffs are more likely to have appeared in some of the categories within our sample. In fact, it seems that institutional lead plaintiffs appear in a greater percentage of the more recent cases in our sample, namely those captured in categories 1, 2, and 3. The Ninth Circuit cases have the

70. *See* James D. Cox & Randall S. Thomas, *SEC Enforcement Heuristics: An Empirical Inquiry*, 53 DUKE L.J. 737 (2003).

71. *See* Stephen J. Choi et al., *Do Institutions Matter? The Impact of the Lead Plaintiff Provision of the Private Securities Litigation Reform Act*, 83 WASH. U. L.Q. 869, 885 (2005); Cox & Thomas, *Does the Plaintiff Matter?*, *supra* note 8, at 1624, 1630–32; Perino, *supra* note 7, at 14.

highest percentage of institutional lead plaintiffs appearing in them, while the Intermediate Standard cases show the lowest of these three categories. The disparity in institutional presence in different categories will be controlled for in our subsequent regression analysis.[72]

Table 4: Cases with Institutional Lead Plaintiffs

Types of Pleading Standard	# of Cases	Percent
(1) *Silicon Graphics* Standard	44	50.0
(2) Intermediate Standard	35	34.7
(3) Second Circuit Standard	46	43.8

Next, we look at the presence of a parallel SEC investigation. A substantial number of the defendants in the private securities fraud class actions in our sample were also subject to a parallel SEC enforcement action over the same allegations. Earlier research found that the presence of a parallel SEC action results in greater settlements in private actions against the same defendant.[73] This may lead plaintiffs' counsel to seek to file in the defendant corporation's home jurisdiction because it does not wish to see higher-valued cases tied up in the MDL-panel process. Therefore, we examine whether there are significant differences in the presence of these enforcement actions across our sample. Table 5 outlines the data on this question for our sample.

Table 5: Cases with Parallel SEC Actions

Types of Pleading Standard	# of Cases	Percent
(1) *Silicon Graphics* Standard	21	23.9
(2) Intermediate Standard	22	21.8
(3) Second Circuit Standard	22	21.0

72. Again, there is only one observation to compare in each category, so we cannot run significance tests on these differences.

73. Cox & Thomas, *supra* note 70, at 763.

In terms of SEC investigations, categories 1-3 have roughly the same percentages of cases, with parallel private and SEC actions, with all of them within the range of 21-24 percent.

Next, we turn to estimated provable losses. Larger provable losses, our surrogate for the possible losses suffered by the class, have been found to be correlated with bigger cash settlements in earlier research.[74] Intuitively, this result makes sense, as we would expect larger investor losses to lead to bigger settlements by defendant firms if the merits of securities fraud class actions matter.

Table 6 presents our data on estimated provable losses for the cases in our sample. The differences between the means and medians of categories 1, 2, and 3 are not statistically significant.[75]

Table 6: Estimated Provable Loss ($ Million)

Types of Pleading Standard	Mean	Median	# of Cases
(1) *Silicon Graphics* Standard	948	150	84
(2) Intermediate Standard	1,409	158	97
(3) Second Circuit Standard	2,041	190	99
All Cases	1,526	162	280

Summarizing these preliminary statistics, we find that there are no significant differences between the cases in our sample in categories 1, 2, and 3. In other words, the descriptive statistics in Tables 1-6 do not generally show large differences in the cases decided under the three different pleading standards adopted by the different circuits. To try to better determine why plaintiffs' counsel may seek to file cases outside of the defendant corporation's home jurisdiction, we must resort to multiple regression analysis.

B. Multivariate Analysis

We turn next to multiple regression analysis to examine why plaintiffs' counsel may seek to file securities fraud class actions outside of the defendant's home jurisdiction. We are particularly interested in

74. Cox & Thomas, *Does the Plaintiff Matter?*, *supra* note 8, at 1631.

75. A t-test for difference in the mean and Wilcoxon Rank Sum test for difference in the median failed to reject the null hypothesis of equivalence.

determining whether differences in the pleading standards for fraud lead to more forum shopping. As we discussed earlier, the Ninth Circuit has the most stringent standard during the time period that we are investigating. Thus, if it is true that the pleading standards are an important influence on the choice of venue, we would expect to see more forum shopping in the Ninth Circuit as compared to the most lenient pleading standard in the Second Circuit. Similarly, the intermediate standard for pleading scienter is stricter than that used in the Second Circuit, once again leading us to expect relatively greater forum shopping in that jurisdiction than in the Second Circuit if pleading standards are an important determinant of venue.

To test this hypothesis, we use multiple regression analysis where the dependent variable is whether the plaintiffs have filed their complaint away from the home jurisdiction of the defendant corporation.[76] This is a logit regression as the dependent variable can take only two values: 1 if it is filed outside the defendant corporation's home circuit, and 0 otherwise. Because the Second Circuit standard for pleading fraud is the most lenient of the three possible standards, we use it as the default standard. This means that the coefficients on the two independent variables for different pleading standards—the *Silicon Graphics* Standard (pleading standard 1) and the Intermediate Standard (pleading standard 2)—should tell us the effect on forum selection of these higher pleading standards. A positive and significant coefficient on one of these variables would be interpreted as indicating that the pleading standard did lead to an increased likelihood that the plaintiffs' counsel would file the case in another jurisdiction. We also include several independent variables in order to control for factors that have been found to affect, or theorized to affect, settlement values. The importance of including this set of independent variables is to control for other factors, such as estimated damages, that might affect forum choice. Table 7 below shows these results.

76. For statistical reasons, we use a log transformation of some of the independent variables. This helps to reduce the impact of outliers in the data on the results of the estimation.

Table 7: Multivariate Regression on Forum Shopping

Parameter	Coefficient	Standard Error	Wald Chi-Square	Pr > ChiSq
Intercept	0.74	1.35	0.30	0.58
Home Circuit with *Silicon Graphics* Standard	-0.09	0.58	0.02	0.88
Home Circuit with Intermediate Standard	0.28	0.55	0.25	0.61
Log (Provable Loss)	-0.24	0.11	4.47**	0.03
Parallel SEC Action	-1.08	0.64	2.80*	0.09
Institutional Lead Plaintiff	0.28	0.46	0.36	0.55

* Significant at 10% level.
** Significant at 5% level. The Cox and Snell R-square statistic for goodness of fit is 0.036.[77]

The coefficients on both the independent variables "Home Circuit with *Silicon Graphics* Standard" and "Home Circuit with Intermediate Standard" are insignificant. This is consistent with the hypothesis that the fraud-pleading standards are not an important factor in plaintiffs' counsel's decision about when to file cases in jurisdictions other than the corporation's home circuit. However, we do see negative and significant coefficients on the variables for estimated losses and the presence of an SEC enforcement action. The former result is consistent with the possibility that plaintiffs' counsel is more likely to file low-value cases outside of the defendant corporation's home jurisdiction when the stakes in the case are relatively small, perhaps reflecting a cost-benefit analysis in favor of litigating the case where it is more convenient to the plaintiff or her counsel. In this regard, of the thirty-four cases shown in Table 3 Panel C that were filed outside of the defendant's home jurisdiction, fourteen were filed in jurisdictions in which at least one of the plaintiffs' law firms was headquartered. Convenience for the plaintiffs in legal representation appears to be an

77. The relatively low value for the goodness of fit in this equation suggests that the regression results would benefit from the inclusion of further control variables such as proxies for case quality. Unfortunately, to date we and other researchers in the field have been unable to come up with good proxy variables for case strength. For further discussion of the Cox and Snell R-square statistic, see D.R. COX & E.J. SNELL, ANALYSIS OF BINARY DATA (2d ed. 1989).

important factor in forum selection for these cases, as nine out of fourteen cases were filed in the jurisdiction in which the home office of the lead law firm was located. We would also suspect that for low-value cases, defendants might be more reluctant to engage in costly jurisdictional battles because the legal fees involved might well exceed the costs of a small settlement. Thus, the defendants might have financial incentives to concede the venue battle in the expectation of a quick and easy settlement of the case.

The presence of an SEC investigation reduces the likelihood of filing the case in a different jurisdiction. Since prior research has shown that cases with parallel SEC investigations are likely to result in higher settlements,[78] we interpret this result as consistent with plaintiffs choosing to file high-value cases in the defendant corporation's home jurisdiction to avoid any delays associated with procedural litigation over forum choice and thereby speed the process toward a potentially favorable resolution.

CONCLUSION

Our data supports the conclusion that differences across pleading requirements do not support significant forum shopping. Overall, we find very little forum shopping in the filing of federal securities class actions, with almost 85 percent of cases being brought in the circuit of the defendant firm's principal place of business. Therefore, it seems unlikely that *Tellabs* will have much impact in reducing forum shopping because there is very little of it going on. The data does, however, raise questions whether other factors, specifically estimated losses and the presence of an SEC enforcement action, have, at the margins, some impact on the profile of cases that find their way into a particular circuit.

We further conclude that *Tellabs*' s requirement that the inferences are to be drawn not solely from the plaintiffs' allegations may lead to greater uniformity across circuits in their individual applications of the strong-inference standard. We have already seen some movement in this direction by the Ninth Circuit in *South Ferry L.P. # 2*, discussed above. Nevertheless, *Tellabs* in some ways was a missed opportunity for the Supreme Court to bring uniformity into the interpretation of the PSLRA. We began this Paper acknowledging the incantation of access to justice and identifying some of the many ways that our laws further this aspiration. Indeed, we can add to this brief list allowing, in the first instance, that the plaintiff forum selection is a mechanism for providing

78. *See* Cox & Thomas, *supra* note 70, at 763; Perino, *supra* note 14, at 962–63.

the aggrieved access to a court.[79] To be noted here is that *forum selection* is the kinder, gentler expression for *forum shopping*. Courts conveniently move between the two characterizations, supporting the former and chastising those who engage in the latter. The reasons for abhorring decisions that are deemed forum shopping are many: it undermines substantive law, overburdens jurisdictions with the most plaintiff-friendly approach, tends to place the suit in a locale that is removed from the source of the contest so that the litigants' expenses are greater, and perpetuates a negative perception of the fairness of the legal system.[80] While we find varying levels of persuasiveness with each of these concerns, our focus is the first. In enacting the PSLRA, Congress clearly sought not just a higher pleading standard, but one that would be more uniform than existed in 1995 under the Rule's particularity requirement, which, as pointed out earlier, elicited wide-ranging approaches among the circuits. Moreover, just a few years after enacting the PSLRA, Congress was sufficiently disturbed by fears that the PSLRA's heightened pleading requirement and the act's other innovations were being circumvented by suits being filed in state rather than federal courts, that it enacted the Securities Litigation Uniform Standards Act of 1998,[81] empowering the defendant to remove any

79. *See* Debra Lyn Bassett, *The Forum Game*, 84 N.C. L. REV. 333, 337, 364–68 (2006) (discussing forum selection in the context of a federal system that anticipates that states will reflect in their laws different social choices, a rationale that is greatly weakened when forum selection is driven by differing interpretations of a *federal* statute); *see, e.g.*, *Keeton v. Hustler Magazine, Inc.*, 465 U.S. 770, 779 (1984) (upholding prosecution in a libel suit in the only possible state where the statute of limitations had not run, reasoning, "Petitioner's successful search for a State with a lengthy statute of limitations is no different from the litigation strategy of countless plaintiffs who seek a forum with favorable substantive or procedural rules or sympathetic local populations"). For the view that appointed judges may be as susceptible as elected judges to creating and nurturing procedural and substantive opportunities for forum shopping, see Todd Zywicki, *Is Forum Shopping Corrupting America's Bankruptcy Courts?*, 94 GEO. L.J. 1141, 1156–57 (2006).

80. *See* George D. Brown, *The Ideologies of Forum Shopping—Why Doesn't a Conservative Court Protect Defendants?*, 71 N.C. L. REV. 649, 651 (1993) (pointing out that forum shopping not only is counter to the reasoning of *Erie Railroad Co. v. Tompkins*, 304 U.S. 64 (1938), but threatens a variety of conservative values such as multiplicity of suits and manipulation of the judicial system); Note, *Forum Shopping Reconsidered*, 103 HARV. L. REV. 1677, 1695 (1990) (arguing that forum shopping is but part of a continuum of activities within the legal system that crosses into the impermissible area where it entails the plaintiff's manipulation of rules to defeat what is perceived as the "correct" legal result).

81. Pub. L. No. 105-353, 112 Stat. 3227 (codified as amended at 15 U.S.C. § 78bb(f) (2006)). That uniformity of result that was sought is underscored by *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit*, 126 S. Ct. 1503 (2006), which upholds removal and subsequent dismissal of a suit on behalf of a class that alleged it was duped into not selling its shares by the defendants' false representations. Due to the fact that

securities class action to federal court. The lack of uniformity in the circuits' constructions of the PSLRA's pleading standard flaunts Congress's clear mandate for uniformity. For these reasons, it was incumbent upon the Supreme Court to deal definitively with the pleading standard by, for example, identifying which of the three disparate approaches it believed was consistent with the intent of Congress. *Tellabs* did not do this. As a result, not only are the substantive demands of the law frayed at the edges, but so is the likely intent of Congress.

the class of defrauded investors were not actual sellers of shares, their suit could not have been brought in federal court although a limited number of states recognized under their laws suits by such "frustrated" sellers.

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