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Some Thoughts on Securities Litigation Trends From Either Side of the Bar

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In yesterday's column, we ran through some key takeaways from the latest annual tally of securities class action filings from Cornerstone Research. Today, as previously promised, we'll chew on the Cornerstone numbers with a pair of practitioners from opposite sides of the securities bar: Jerry Silk of Bernstein Litowitz Berger & Grossmann and Scott Musoff of Skadden, Arps, Slate, Meagher & Flom.

First, a quick review of what jumped out in this year's numbers: The overall volume of new filings ticked up slightly in 2023 to 215 from 208 in 2022—the first increase after three consecutive years of decline. This uptick occurred despite a slowdown in three significant lines of cases Cornerstone has tracked over the past few years: New filings involving claims tied to COVID and SPACs both fell by 39% last year and there were 50% fewer cryptocurrency cases than in 2022. Part of what was driving the overall increase, however, was an emerging line of nine cases that sprang out of last year's regional bank failures, including eight new cases filed in 2023.

Courtesy photos

Scott Musoff, left, of Skadden, and Gerald H. Silk, right, of Bernstein Litowitz Berger & Grossmann.

Where cases were being filed also underwent an interesting shift. The Second Circuit, the perennial leader in securities class actions activity, saw the number of new filings drop for the second consecutive year, falling to 50 in 2023 from 73 in 2022 after seeing a peak of 82 in 2021. The Ninth Circuit, meanwhile, significantly outpaced the Second Circuit last year in terms of new filings with 67.

Silk of Bernstein Litowitz said he "wasn't terribly surprised" to see the shift in cases toward the Ninth Circuit. For one, he said what seems to be driving the securities practice right now are cases against technology, media and telecom companies and biotech companies that are largely located on the West Coast. He added that the Second Circuit is usually home to a lot of cases involving financial services cases, but this latest wave of bank failures has been confined largely to regional banks on the West Coast, including Silvergate Bank, Silicon Valley Bank, and First Republic, all banks headquartered in California, where his firm is serving as lead or co-lead counsel in the follow-on securities suits.

Skadden's Musoff agreed with Silk's observation about the West Coast nature of the recent regional bank crisis driving some of the shift in filings to the Ninth Circuit. But he added that there had been a significant dropoff in 1933 Act filings, especially Section 11 suits brought in the wake of initial public offerings. Those cases, he noted, often end up in the Second Circuit because that is where many of the banks underwriting those IPOS are located.

As to the dropoff in COVID, SPAC and crypto cases, neither Musoff nor Silk was surprised. As to SPACs, Silk said, "We've all seen that this stock vehicle is no longer one favored by Wall Street." Fewer SPAC deals means fewer SPAC securities suits. Simple enough. In cryptocurrency cases, Silk said there have been some issues that have popped up around offshore entities and opaque business structures that have made recoverability an issue for plaintiffs in some of those cases. "That's probably one reason that you've seen a slowing pace on those cases," he said.

Looking at the numbers with Silk and Musoff made me realize that securities litigation is clearly a lagging economic indicator. Fewer IPOs mean fewer IPO suits. And with fewer Section 11 suits, where strict liability attaches to material misrepresentations in company registration statements, that leaves the plaintiffs bar working on more 10b-5 where the intent of the speaker making the alleged misleading statement comes into play.

I asked Silk if this sort of economic environment makes it more difficult for lawyers practicing on the plaintiffs' side of the securities bar. He pointed out that the S&P 500 was up 24% in 2023. He said the IPO market, with interest rates sitting where they were, was largely "closed for business." He said his clients understand the significance of Section 11 claims and the history of the securities laws building "extra protections for investors in the IPO setting."

"I'm not gonna say it's more challenging, but we're seeing less of that for sure," he said. Silk added that another aspect of having the stock market on an overall upward trajectory is that sometimes, when a company discloses something potentially damaging, the market doesn't quite react as it might otherwise. All the other positive news in the market can have the effect of driving the stock prices upward, he said.

To that, Musoff noted that while you can look at what the S&P 500 or any other index does over the whole year, interim stock price declines at individual companies are what drive many 10b-5 suits. A rising market means higher valuations. "If there is something that causes more volatility, we may see declines that end up with higher market cap losses, which will attract securities litigation," Musoff said.

We'll see about that next year.

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