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The Price of Pay To Play in Securities Class Actions

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Abstract

This paper studies the effect of campaign contributions to lead plaintiffs—"pay to play''—on the level of attorneys' fees in securities class actions. We find that state pension funds generally pay lower attorneys' fees when they serve as lead plaintiffs in securities class actions than do individual investors serving in that capacity. This differential disappears, however, when we control for campaign contributions made to officials with influence over state pension funds. Thus, pay to play appears to increase agency costs borne by shareholders in securities class actions.

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1. Introduction

One of the main goals of the Private Securities Litigation Reform Act (PSLRA) was to "empower investors so that they, not their lawyers, control securities litigation."[1] Congress believed that individual investors who served as class representatives prior to the enactment of the PSLRA were largely figureheads dominated by class action lawyers. Because the interests of class action lawyers were typically much greater than those of the named class representatives, plaintiffs may have lacked the incentive to monitor class counsel adequately. To remedy that imbalance, the PSLRA creates a presumption that courts will appoint as lead plaintiff the class member seeking appointment with the largest financial interest in the relief sought.[2] Large shareholders, the theory went, would have more of an incentive to oversee lawyers who represent the class. Congress hoped that institutional shareholders serving as lead plaintiffs would better negotiate with class counsel over attorneys' fees, ensuring that a larger share of the recovery would accrue to the class members.

In some ways, it appears that the PSLRA's lead plaintiff provision has succeeded. After a slow beginning, institutional investors have stepped forward in large numbers to serve as lead plaintiffs. The PSLRA has changed the game for class action lawyers, who must now compete for the favor of institutional investors in order to be selected as counsel. There is evidence that this competition has played an important role in reducing the percentage of the class recovery that goes to paying the lawyers post-PSLRA.

[1] S. REP. NO. 104-98 (1995). *See also* H.R. CONF. REP. NO. 104-369, at 32 (1995).
[2] Securities Exchange Act of 1934 § 21D.

There have been rumors, however, of another form of competition to garner the favor of institutional lead plaintiffs. Most of the institutional investors that have agreed to serve as lead plaintiffs have been government-sponsored pension funds. Many of these funds are managed directly by politicians, such as state comptrollers, who must campaign to retain their current positions, or may have designs on higher offices. Alternatively, these funds are managed by political appointees, who typically owe their position to the state's governor. The presence of political influence over these funds naturally raises the question of whether law firms are making political contributions to the politicians who wield that influence in order to enhance their chances of being selected to represent the pension funds. Simply put, are law firms buying lead counsel status with campaign contributions, i.e., do class action lawyers pay to play? And do campaign contributions have any effect on the level of attorneys' fees paid in securities class actions? In other words, what is the price paid by class members if lawyers are paying to play?

This paper presents the results of an empirical study shedding light on that question. Looking at a sample of securities class actions filed between 2003 and mid-2007, we find that the presence of a state pension fund as lead plaintiff correlates with significantly lower attorneys' fees. That effect is confined, however, to state pension funds whose management has not received campaign contributions. Attorneys' fees in cases with state pension funds whose managers have received campaign contributions are statistically indistinguishable from attorneys' fees in cases with individual investors serving as lead plaintiffs. Thus, political contributions to lead plaintiffs appear to

undermine at least one of the objectives that Congress had in enacting the PSLRA's lead plaintiff provision.

We proceed as follows. Part 2 provides background on the lead plaintiff provision and develops hypotheses relating to political influence on pension funds serving as lead plaintiffs. Part 3 describes our sample and sources of data. Part 4 presents the results of our empirical tests of our hypotheses. Part 5 concludes with a discussion of the legal and policy implications of our findings.

2. Background and Hypotheses

2.1 Prior Literature

One of the abuses of securities class actions that Congress attempted to address in enacting the PSLRA was "the manipulation by class action lawyers of the clients whom they purportedly represent."[3] Congress found a potential solution to that problem in a proposal by Weiss and Beckerman (1995). Weiss and Beckerman argued that institutional investors, if placed in the lead plaintiff role, would act as effective monitors of plaintiffs' attorneys' actions in securities class action litigation. Congress acted on Weiss and Beckerman's proposal in adopting the PSLRA's lead plaintiff provision. That provision established a "rebuttable presumption . . . that the most adequate plaintiff . . . is the person or group of persons that . . . has the largest financial interest in the relief sought by the class."[4] The PSLRA also stated that the most adequate plaintiff will

[3] See H.R. Rep. No. 369, at 31 (1995), reprinted in 1996 U.S.C.C.A.N. 730, 1103.
[4] 15 U.S.C. § 78u-4(a)(3)(B)(iii)(I).

"select and retain counsel to represent the class."[5] The premise of the PSLRA's lead plaintiff provision is that larger investors, with larger stakes in the class recovery, will serve as more effective monitors of class counsel. By providing effective monitoring, the lead plaintiff will protect the interests of the absent class members.

Congress worried, however, about the potential for lead plaintiff monitoring to be undermined by side payments, which were rumored to have been an issue in securities class actions prior to the adoption of the PSLRA. The concern was that plaintiffs were being paid by lawyers for agreeing to serve as the class representative, and those payments undermined the class representative's incentive to look out for the interests of absent class members. To address the problem of side payments undermining monitoring, Congress included a provision in the PSLRA prohibiting non pro-rata payments to the lead plaintiff.[6] Congress's suspicion of possible side payments to individual lead plaintiffs appears to have been well-founded; several former partners of the Milberg Weiss law firm (now "Milberg") have gone to prison for hiding such payments from courts overseeing securities class actions (Selvin 2008).

Those side payments appear to have had an effect on monitoring by lead plaintiffs. One measure of lead plaintiff monitoring is attorneys' fees; vigilant monitors presumably would negotiate for lower fees, which would mean a greater net recovery to class members. Consistent with this theory, Perino (2008) finds that attorneys' fees were significantly higher for Milberg Weiss cases identified in the indictment against the firm where side payments to the lead plaintiffs were present than for those cases not

[5] 15 U.S.C. § 78u-4(a)(3)(B)(v).
[6] 15 U.S.C. § 78u-4(a)(4).

identified in the indictment.

There is considerable evidence that the lead plaintiff provision has led to improved monitoring of class counsel. Choi, Fisch and Pritchard (2005) report that public pension funds' participation as lead plaintiff increased significantly after the PSLRA's enactment. They also report that the presence of public pension funds correlates with high value settlements. Simmons and Ryan (2005) and Cox and Thomas (2006) also report that institutional lead plaintiffs correlate with increased settlement amounts. Cox, Thomas, and Bai (2008) similarly report that institutional investor lead plaintiffs, in particular public pension funds and labor unions, are positively related to larger settlement amounts. These studies suggest that institutional investors who serve as lead plaintiffs may be promoting larger recoveries for shareholder class members.

Choi, Fisch and Pritchard (2005) examine the relationship of lead plaintiffs and attorney fees. They report that attorney fees, measured as a percentage of recovery, if anything, are higher with private institutional lead plaintiffs after the enactment of the PSLRA compared with the pre-PSLRA period; they also report no significant correlation exists between fees and public pension funds post-enactment once they control for the size of the case. Their study looked only at cases filed from 1991 to 2000, so it antedates the time that institutional investors stepped forward in large numbers to serve as lead plaintiff. Perino (2006), looking at a larger sample of cases from 1995 to 2004, reports that attorney fees granted by a court are lower with public pension fund lead plaintiffs, even after controlling for the presence of accounting restatements and SEC investigations.

There has been anecdotal evidence for some time of political contributions to the lead plaintiff being linked to the plaintiff's lead counsel selection, but little systematic analysis. For example, *Fortune* magazine ran a story detailing political contributions received by former New York State Comptroller Carl McCall from the partners at Bernstein, Litowitz, Berger & Grossman (BLBG) (Weinberg & Fisher, 2004). McCall received these contributions shortly before McCall chose BLBG to serve as the New York public pension fund's counsel in the *WorldCom* securities class action. McCall was also involved in perhaps the most frequently cited example of pay to play in securities cases, *In re Cendant Corp. Litigation*. The district court in *Cendant* discovered that two law firms selected as lead counsel contributed nearly $200,000 to McCall's campaign, who was the sole director of the New York public pension fund that was a lead plaintiff in the case (Dewan 2002). The district court in *Cendant*, however, refused to find that pay to play took place, and this finding was affirmed by the Court of Appeals for the Third Circuit.[7]

Johnson-Skinner (2009) provides the first systematic effort to document pay to play. He presents summary statistics of law firm political contributions side-by-side with pension funds' selection of law firms as counsel in securities class actions from 2002 to 2006. He concludes, preliminarily, that there is substantial evidence of a connection between political contributions and selection as lead counsel. He does not, however, analyze the connection between contributions and attorneys' fees. This study fills that gap.

[7] *In re Cendant Corp. Litig.*, 264 F.3d 201, 269 (3d Cir. 2002).

2.2 Hypotheses

As discussed above, Congress believed that individual investors who served as lead plaintiffs were ineffective monitors and plaintiffs with larger stakes in the class recovery were likely to negotiate harder with class counsel over fees. The PSLRA's lead plaintiff provision encourages institutional investors to step forward to serve as lead plaintiffs. These institutional investors are quite varied in their size and sophistication. State level public pension funds—e.g., Calpers—are typically the largest and most sophisticated investors among those who have volunteered to serve as lead plaintiff. Smaller institutions, however, like local government and labor union pension funds, have also come forward to serve as lead plaintiffs. Finally, individuals continue to serve as lead plaintiffs in a substantial percentage of cases.

We postulate a continuum of investor types when it comes to negotiating over fees, with larger institutions, such as state pension funds, being the most effective in negotiating for lower fees, because they have the greatest leverage in being able to offer lawyers additional opportunities to serve as lead counsel in subsequent cases. Other institutions, such as local government pension funds and labor unions, may have greater stakes at issue than do individual investors, but they may lack the legal sophistication of the large state pension funds. We postulate that individuals will exercise the least influence in negotiating over attorneys' fees.

Hypothesis 1: State public pension funds will negotiate the lowest attorney fees, local government pension funds and labor unions will negotiate intermediate fees, and individual lead plaintiffs will negotiate the highest.

As noted above, the governing premise of the PSLRA's lead plaintiff provision is that investors with a larger stake in the class recovery will serve as better monitors of the class's interests. This incentive for better monitoring, however, may be undermined if the decisionmakers for the institutional lead plaintiff have been receiving a selective benefit—e.g., campaign contributions—not shared by other class members. Congress worried about the effect of selective benefits when it adopted the prohibition against non-pro rata payments to class members discussed above.

We use attorneys' fees as our measure of lead plaintiff monitoring. We hypothesize that political contributions to state pensions acting as the lead plaintiff—we call such plaintiffs "conflicted"—may lead to diminished monitoring and correspondingly higher attorneys' fees. Moreover, we postulate that attorneys' fees are likely to correlate with the size of the contributions to the state pension funds—the greater the contribution, the greater the fee. In other words, size matters.

> **Hypothesis 2: Attorneys' fees negotiated by conflicted state pension fund lead plaintiffs will be no different than attorneys' fees negotiated by individual plaintiffs.**
> **Hypothesis 2A: Attorneys' fees will correlate with the size of the political contributions made to the state pension fund lead plaintiffs.**

Hypothesis 2A postulates that the magnitude of contributions is one measure of the conflict created by political contributions. Another measure of that conflict is the pervasiveness of those contributions. Are the decisionmakers of the state pension fund frequent, or only occasional, recipients of contributions from securities class action

attorneys? Frequent recipients of political contributions may be signaling their tolerance of higher fees. Accordingly, we postulate that state pension fund lead plaintiffs who receive contributions from class counsel associated with a higher percentage of their cases are likely to agree to pay higher fees generally relative to those state pension funds that receive fewer contributions.

Hypothesis 3: Attorneys' fees will be higher in cases in which the state pension fund lead plaintiffs are frequent recipients of political contributions from securities class actions attorneys.

An additional area that we wanted to explore in this study is the role of local government pension funds, which have increasingly become involved as lead plaintiffs in securities class actions. Unfortunately, we were unable to locate data on political contributions for most of the decisionmakers for the local pension funds in our dataset. In the course of our investigation, however, we noted that most of the local pension funds in our sample were represented by one of two law firms ("Pension Counsel").[8] These firms appear to specialize in counseling local governments on pension and employment law issues. They also have appeared as co-counsel to one or more of the specialist securities class action firms in a handful of securities class actions, although this appears to be a sideline to their main legal work.

We surmise that these firms are steering their local pension fund clients to become involved as lead plaintiffs, but the effect of their influence on attorneys' fees in securities class actions is unclear. One hypothesis would be that these firms are

[8] The two firms are Klausner & Kaufman and VanOberbeke Michaud & Timmoney.

receiving referral fees from traditional class action firms for delivering their clients to serve as lead plaintiffs. That hypothesis would suggest that attorneys' fees should be higher in cases involving local government pension funds because the lead counsel firm would want to be compensated for the referral fee. The competing hypothesis would be that these firms are providing oversight of securities class action counsel on behalf of their clients. That oversight might include negotiating on behalf of the class for lower attorneys' fees. Given these plausible competing hypotheses, we do not have a predicted direction for the effect of the involvement of these two firms on attorneys' fees.

Hypothesis 4: Local government pension funds acting as lead plaintiff and represented by pension counsel will negotiate for higher/lower attorneys' fees.

3. Sample and Descriptive Statistics

3.1 Sample

To test our hypotheses, we use a sample of settlements for securities class actions filed from 2003 to mid-2007.[9] We obtain the suits from the Stanford Securities Clearinghouse. We exclude cases in which financial firms (SIC 6000 to 6999) are the primary defendant because of the different regulatory regime that applies to them.

[Insert Table 1 About Here].

Table 1 shows that the lawsuit filings were distributed relatively equally across our sample period, although there is some tapering off in 2006 and 2007, as many of the suits filed in those years remain unresolved. Looking at the frequency of lawsuit by

[9] The sample is based on the dataset in Choi (2009).

circuit, we find that the Second and Ninth Circuits are clearly head-and-shoulders above their peers with 19.2% and 25.5% of the lawsuits.

3.2 Control Variables

Descriptive statistics regarding the cases are presented in Table 2. We use the following set of variables in each of our multivariate models as controls (collectively referred as "Case Controls"). The controls are relevant to the strength of the case, which is likely to determine the difficulty of extracting a settlement. More difficult cases may generate higher attorneys' fees. We collect information on key aspects of the litigation from the last amended complaint available for each class action.[10]

From the complaints, we collect information about the causes of action alleged and use indicator variables for the cause of action. Over 95 percent of the cases alleged a Rule 10b-5 claim under the Securities Exchange Act of 1934; 19.3 percent of the cases alleged a § 11 claim under the Securities Act of 1933 (Section 11); 3.7 percent of the cases alleged a § 14(a) claim under the Securities Exchange Act of 1934. Section 11 is available only for material misstatements and certain omissions in the registration statement used in a public offering, but it allows for a substantially greater chance of surviving the motion to dismiss because § 11 does not require plaintiffs to plead fraudulent intent. Unlike the Rule 10b-5 cause of action, loss causation and due diligence are affirmative defenses, rather than elements of the claim. Claims under § 14

[10] As described in Choi (2009), the complaints and other securities-docket-related documents were collected from the PACER website.

of the Exchange Act relating to misstatements in a proxy statement also carry an easier standard for state of mind and loss causation (Section 14).

[Insert Table 2 About Here].

We also include as controls certain indicator variables based on the allegations in the complaint. These allegations are intended to satisfy the pleading standards, which are the principal barriers to recovery in securities class actions. We include in our Case Controls variables for SEC and other government investigations (Govt. Investigation) and accounting restatements (Restatement), each a high profile adverse event and the most common events triggering these suits. The presence of a government investigation or a restatement indicates a higher likelihood of wrongdoing and thus a stronger case for the plaintiffs. The overall strength of the case will also be bolstered if the firm has terminated a top officer, including the Chief Executive Officer, Chief Operating Officer, and Chief Financial Officer (Officer Term.) or its auditor (Auditor Term.), due to events relating to the fraud in question as described in the complaints. We also include whether the complaint alleges insider trading (Insider Trading Claim), which is relevant to fraudulent intent.

We also include variables in our Case Controls relating to the firm-specific characteristics of the defendant issuer, which correlate with the damages measure and the defendant's ability to pay a settlement. We include a measure of firm size, measured as market value of equity measured at the end of the fiscal year preceding the beginning of the class period (Market Capitalization). Larger firms may have greater resources to defend against a class action. On the other hand, larger firms may also be

better able to pay a settlement, leading to more vigorous prosecution of the case by plaintiffs' attorneys. We also include the share turnover during the class period (Turnover) and the minimum one-day stock return during the class period plus the day after the end of the class period (Minimum Return) for the company at issue in the complaint—both related to the potential damages available from the litigation. We also include the settlement amount because prior studies report a close relationship between settlement amount and the attorney fee award (e.g., Eisenberg & Miller, 2004).

We also include two industry controls that may relate to case strength and loss causation. Firms in the high technology sector (High Tech) – defined as SIC codes – may have stock prices that are particularly vulnerable to declines in sales or earnings. Firms in pharmaceuticals and medical devices may experience steep stock price declines if the Food and Drug Administration denies approval of their new products. To capture this effect, we include an indicator variable (FDA) equal to 1 if the last amended complaint for the class action contains allegations based on U.S. Food and Drug Administration-related disclosures and 0 otherwise. Finally, we include the log of the settlement amount; all else equal, larger settlements are likely to correlate with lower percentage fee requests.

3.3 Plaintiff Type

For each class action, we collect data from PACER, Westlaw, and the Securities Class Action Clearinghouse on the federal district court docket and the motions for lead

plaintiff. Lead plaintiffs usually are combined in a lead plaintiff group of several investors. Lead plaintiff groups typically are created to resolve disputes among class action firms competing to be named as counsel to the class.

Table 3, Panel A provides descriptive statistics regarding the type of investors selected as lead plaintiffs. Institutional investors appear as part of the lead plaintiff group in over half (55.8%) of the cases in our sample, confirming earlier work showing that institutional investors are important players securities class actions. Public pension funds appear in nearly eighteen percent of the cases in our sample; with slightly fewer state (8.3%) than local (9.1%) funds. State pension funds are the primary focus of our analysis.

[Insert Table 3 About Here]

Table 3, Panel B provides descriptive statistics comparing the assets under management and losses related to the class actions for the different types of institutions acting as lead plaintiff. As expected, the state pension funds are larger than their local counterparts and labor union funds. The average (median) state pension fund in our sample has nearly $15.0 billion ($6.1 billion) under management, while the local funds manage an average of $8.1 billion ($0.4 billion). The difference between the two means, however, is not significantly different from zero. State pension funds also had larger securities losses related to the class action. The average (median) state pension fund in our sample had $7.3 million ($1.8 million) losses in cases where they acted as lead plaintiff while the local funds manage an average of $0.6 million ($0.3 million). The difference between the two means is significant at the one percent level. Labor unions

manage the least in assets, with an average of $1.1 billion ($0.6 billion). Labor unions also had relatively low securities losses with an average of $0.8 million ($0.2 million).

3.4 Political Contributions

Having identified the lead plaintiffs in our sample, we collected data on contributions to politicians connected to state pension funds. We first identified the membership of the controlling boards of the plaintiff institutions at the time the case was filed. For board positions that were *ex officio*, we determined who held the relevant office at the time of filing of the complaint. For positions that were appointed by an elected official, we also determined what elected official was in office at the time of filing.

Next, we identified the plaintiff law firms that were selected as counsel by the funds in each case in the sample. If there was more than one plaintiff law firm for a given case, which was typically the case when more than one institution filed to be lead plaintiff, all the filers and all the firms were grouped together. For purposes of matching firms with plaintiff pension funds, we assumed that all funds and all counsel for a particular case were affiliated.

We then used state-level campaign finance filings to find instances of political contributions from the identified law firms to any of the elected officials associated with the pension funds that actually selected the firms.[11] Contributions from 1998 through 2008 were included in the search. The search allowed us to look for both contributions

[11] The source of this data is followthemoney.org. Puerto Rico was treated as a state for these purposes.

by the firm and by individuals who list the firm as their employer. Note that this method is underinclusive as it does not discover any donors who did not indicate their employer (for example, an attorney at Milberg Weiss who does not list Milberg Weiss as her employer). We also searched for contributions to the relevant elected officials' party committees in an attempt to find indirect contributions.[12]

Our data are underinclusive in another way because we were unable to locate systematic data for contributions to local, non-state level politicians affiliated with pension funds in our sample. We found press reports of such contributions in isolated cases, and handful of large municipalities have websites showing such contributions, but because we could not collect this data for all of the local government pension funds in our sample, we have not relied on any contributions to local politicians in our analysis. Thus, our findings are likely to understate the influence of pay to play, which appears to also affect local pension funds.

[Insert Table 4 About Here]

Table 4 presents descriptive statistics showing the results of this research into political contributions. Almost half (45.5%) of the state pension funds in our sample received campaign contributions. For these firms, the mean contribution was relatively small at $39,223 and the median contribution was $11,750. Aggregating all of the cases in our sample, state pension funds received a mean of $52,170.

[12] Note that we collect contribution data in part for a period of time after some of our securities class actions are resolved. We nonetheless conjecture that such contributions correlate with the overall flow of money to the specific state pension funds and thus reflect the influence of the plaintiffs' attorneys firms over the state pension funds in our sample.

4. Empirical Tests

4.1. Multivariate Analysis of Political Contributions and Attorney Fees

We estimate an ordinary least squares model with the log odds of the requested attorney fee percentage as the dependent variable (using case level data and robust standard errors). Panel A of Table 5 reports that the mean requested attorney fee is 26.7% of the settlement amount. Our main independent variable of interest is the fraction of the lead plaintiffs in a case that consist of a state pension fund (State Pension). We also include the fraction of the lead plaintiffs that consist of a local pension fund (Local Pension), or a labor union (Labor Union), and the fraction of lead plaintiffs that are institutions but not government pension funds or labor unions (Other Inst). The regression assesses the effect of these variables relative to our baseline category of individual lead plaintiffs, the type of plaintiff that Congress found wanting pre-PSLRA.

In our regressions, we include an indicator variable Low Loss defined as equal to 1 if the losses for the lead plaintiffs for the case are at the median losses or lower for all the lead plaintiffs in our sample or 0 otherwise. Plaintiffs with smaller losses at stake may have less incentive to monitor class counsel. We include the Case Controls described above. We also include indicator variables for those circuits with at least 20 class actions in the sample (Circuit Effects) and indicator variables for the resolution year (Year Effects).[13]

[13] The Circuit Effects include indicator variables for the 2nd, 3rd, 5th, 9th, and 11th circuits.

$$\ln(\text{Atty\_Fee}_i/1\text{-Atty\_Fee}_i) = \alpha + ß_{1i}\text{State Pension}_i + ß_{2i}\text{Local Pension} + ß_{3i}\text{Labor Union} + ß_{4i}\text{Other Institution} + ß_{5i}\text{Low Loss} + \text{Case Controls} + \text{Circuit Effects} + \text{Year Effects} + \varepsilon_i$$

The results are presented in Panel B of Table 5, Model 1. Negative coefficients for the independent variables correlate with lower attorneys' fees, suggesting more diligent monitoring by the lead plaintiff. Consistent with Hypothesis 1, we find that state pension fund lead plaintiffs request significantly lower attorneys' fees, as do local pension funds. Both coefficients are significant at the one percent level. Assessed at the mean of all independent variables, a fifty percentage point increase in the fraction of lead plaintiffs that consists of state pension funds correlates with a 2.8 percentage point decrease in the attorney fee request (or 10.6% of the mean requested attorney fees). Similarly, a fifty percentage point increase in the fraction of lead plaintiffs that consists of local pension funds correlates with a 2.6 percentage point decrease in the attorney fee request (or 9.8% of the mean requested attorney fees). The coefficients for Labor Union and Other Institution are negative, but considerably smaller in magnitude and statistically insignificant. Thus, these latter two categories of institutions appear to be indistinguishable from individual plaintiffs when it comes to negotiating attorneys' fees with counsel.

[Insert Table 5 About Here]

To assess the impact of lead attorney contributions to political officials in control of public pension funds, we replace the State Pension variable with two variables (reported in Model 2): the fraction of lead plaintiffs in the case that consists of state

pension funds with officials that received political contributions from the lead attorneys (State Pension—Contribution), and the fraction of lead plaintiffs in the case that consists of state pension funds with officials that did not receive political contributions from the lead attorneys (State Pension—No Contribution).

The results of Model 2 suggest that the correlation between state pension funds and lower attorneys' fee observed in Model 1 is driven largely by state pension funds that have not received campaign contributions. The coefficient for State Pension—Contribution is negative, but insignificant, while the coefficient for State Pension—No Contribution is negative and significant at the one percent level. Assessed at the mean of all independent variables, a fifty percentage point increase in the fraction of lead plaintiffs that consists of State Pension—No Contribution funds correlates with a 3.4 percentage point decrease in the attorney fee request (or 12.9% of the mean requested attorney fees). These findings, consistent with Hypothesis 2, suggest that campaign contributions seem to temper the zeal of state pension fund to squeeze lower fees out of their attorneys.

To assess the importance of the amount of campaign contributions by attorneys, we divide the State Pension—Contribution variable in Model 2 into two categories (reported as Model 3). State Pension—Contribution Above Median is the fraction of lead plaintiffs in a case that consists of state pension funds which received a contribution from the lead attorneys at the median or above for all state pension funds that received contributions in our sample. Conversely, State Pension—Contribution Below Median is the fraction of lead plaintiffs in a case that consists of state public

pensions with a contribution from the lead attorneys below the median for all state pension funds that received contributions in our sample.

Consistent with our prediction in Hypothesis 2A, the amount of the contributions does seem to matter. For the cases in which the contributions are above the median, the coefficient is actually positive, albeit insignificant. For the cases in which the contributions were below the median, the coefficient is negative and strongly significant. Assessed at the mean of all independent variables, a fifty percentage point increase in the fraction of lead plaintiffs that consists of State Pension—Contribution Below Median funds correlates with a 2.8 percentage point decrease in the attorney fee request (or 10.8% of the mean requested attorney fees). In fact, the coefficient for State Pension—Contribution Below Median is statistically indistinguishable from the coefficient for State Pension—No Contribution (F-test probability is equal to 0.697).[14]

[14] We estimated a number of robustness tests for the models in Panel B of Table 5. First, we re-estimated the models without the inclusion of the Low Loss variable (due to possible colinearity between greater losses and public pension funds). Unreported, the re-estimated models resulted in the same qualitative results as in Table 5.

Second, we re-estimated Model 1 replacing State Pension, Local Pension, Labor Union, and Other Institution with binary versions of each variable equal to 1 if the lead plaintiff group has at least one lead plaintiff of the type in question (e.g. State Pension is redefined to equal 1 if at least one lead plaintiff is a state pension fund) and 0 otherwise. For Model 2, we redefine State Pension—Contribution as equal to 1 if at least one lead plaintiff is a state pension fund and the state pension fund received political contributions from the lead attorneys and 0 otherwise. We redefine State Pension—Contribution as equal to 1 if at least one lead plaintiff is a state pension fund but the state pension fund did not receive political contributions from the lead attorneys and 0 otherwise. For Model 3, we redefine State Pension—Contribution Above Median as equal to 1 if at least one lead plaintiff is a state pension fund and the state pension fund received a contribution from the lead attorneys at or above the median for all public pension funds that received contributions in our sample. We redefine State Pension—Contribution Below Median as equal to 1 if at least one lead plaintiff is a state pension fund and the state pension fund received a contribution from the lead attorneys below the median for all public pension funds that received contributions in our sample. For each of the re-estimated model, we obtained the same qualitative results as in Table 5 with the following exceptions. The coefficient on Local Pension is negative but now significant at only the 5% level in Models 1 and 2 and the 10% level in Model 3.

Third, to control for selection effects, we re-estimate the models of Table 5 with a Heckman two-stage model. Stage two is the models from Table 5. Stage one is a model for settlement. For an

Only state pension funds that take in below the median level of contributions appear to negotiate for lower attorney fees.

4.2. Pension Fund Assets and Attorney Fees

Our next set of tests assesses the relation between assets under management and attorneys' fees. We postulate in Hypothesis 1 that larger pension funds will negotiate for lower fees. To test this hypothesis, we estimate an ordinary least squares model with the log odds of the requested attorney fee percentage as the dependent variable (using case level data and robust standard errors). Our main independent variables of interest are State Pension—Above Median Assets (the fraction of lead plaintiffs in a case that consists of state public pensions with total fund assets at the

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instrument, we use the total number of securities class actions filed in the dataset time period for the district court in which the specific class action is filed (Heckman 1979). We assume this variable is correlated with the decision to settle. A particular district court with large numbers of securities class action may face greater pressure to dismiss such actions to clear their docket, leading to fewer settlements. On the other hand, we assume this variable is not correlated directly with the number of attorney hours worked in a particular settled litigation. Unreported, the Heckman models returned the same qualitative results as in Table 5 with the following exceptions. The coefficient on Local Pension is negative but now significant at only the 10% level in Models 1 through 3. The coefficient on State Pension—Contribution Below Median in Model 3 is negative but now significant at only the 5% level.

Fourth, we examine the impact of contributions by plaintiffs' attorney firms to any state official for the state associated with a particular State Pension. It is possible that such donations may have an indirect effect on public pension funds decisions. For example, donations to the Governor of a state may lead the Governor to put pressure on the officials directly responsible for the public pension fund. We re-estimate Models 2 and 3 of Table 5 as follows. For Model 2, we replace State Pension—Contribution and State Pension—No Contribution with State Pension—Contribution Any Official and State Pension—No Contribution Any Official. Similar with Model 2of Table 5, the coefficient on State Pension—No Contribution Any Official is negative and significant at the 1% level. Unlike in Model 2 of Table 5, State Pension—Contribution Any Official is negative and now significant at the 5% level. The coefficient on State Pension—Any Contribution is nonetheless smaller in magnitude than the coefficient on State Pension—No Contribution Any Official. For Model 3, we replace State Pension—Contribution ≥ Median with State Pension—Contribution Any Official ≥ Median (defined based on the median for all state pensions in the sample that received a contribution for any official), State Pension—Contribution < Median with State Pension—Contribution Any Official < Median, and State Pension—No Contribution with State Pension—No Contribution Any Official. We obtain the same qualitative results as in Model 3 of Table 5.

median or above for state public pensions in our sample) and State Pension—Below Median Assets (the fraction of lead plaintiffs in a case that consists of state public pensions with total fund assets below the median for state public pensions in our sample). We also include two variables for Local Pension and Labor Union plaintiffs, each divided by asset size in the same manner as the division for State Pensions described above. We include a single Other Institution variable, as data on asset size is not available for these institutions. These variables are in comparison to the base category of individual lead plaintiffs. The other independent variables are the same as those used in the regressions presented in Table 5.

$$\begin{aligned} \ln(\text{Atty\_Fee}_i/1\text{-Atty\_Fee}_i) = \; & \alpha + \beta_{1i}\text{State Pension—Above Median Assets}_i \\ & + \beta_{2i}\text{State Pension—Below Median Assets}_i \\ & + \beta_{3i}\,\text{Local Pension—Above Median Assets}_i \\ & + \beta_{4i}\,\text{Local Pension—Below Median Assets}_i \\ & + \beta_{5i}\,\text{Labor Union—Above Median Assets}_i \\ & + \beta_{6i}\,\text{Labor Union—Below Median Assets}_i \\ & + \beta_{5i}\,\text{Other Institution} + \beta_{6i}\,\text{Low Loss} + \text{Case Controls} \\ & + \text{Circuit Effects} + \text{Year Effects} + \varepsilon_i \end{aligned}$$

We report the results in Table 6, Model 1. The results are mixed. The coefficient for Local Pension—Above Median Assets is negative and significant at the one percent level. Assessed at the mean of all independent variables, a fifty percentage point increase in the fraction of lead plaintiffs that consists of Local Pension—Above Median Assets funds correlates with a 4.2 percentage point decrease in the attorney fee request (or 15.6% of the mean requested attorney fees). Thus, it appears that larger local pension funds are more effective monitors than other types of investors who serve as lead plaintiffs. Larger institutions may have economies of scale in supervising their

attorneys or they may simply have greater bargaining leverage because of the advantages they have in seeking lead plaintiff status. Larger holdings are likely to correlate with larger losses, the relevant metric for awarding lead plaintiff status.

[Insert Table 6 About Here]

In Model 1, however, the coefficient on state pensions with below median assets is negative and significant at the one percent level while the coefficient on state pensions with above median assets, while negative, is not significantly different from zero. Thus, unlike local pensions, state pensions with larger assets do not correlate with lower attorney fees. We also find no distinction between labor unions with above and below the median assets for labor union lead plaintiffs in our sample, possibly because the variation in assets is less for labor unions. The standard deviation for fund assets is $3.2 billion for labor unions, compared to $22.9 billion for public pension funds.

One explanation for the anomalous result with regard to state pension funds in Model 1 might be campaign contributions. To assess whether attorney campaign contributions affect the attorneys' fees negotiated by larger state pension funds (and the lack of correlation between large state pension funds and attorney fees), we divide the State Pension—Above Median Assets variable in Model 1 into the following two variables. State Pension—Above Median Assets Contribution is the fraction of lead plaintiffs in a case that consists of state pension funds that received a contribution from one of the lead attorneys and that had total fund assets at the median or above for state pension funds in our sample. State Pension—Above Median Assets No Contribution is the fraction of lead plaintiffs in a case that consists of state pension

funds that did not receive a contribution from any of the lead attorneys and that had total fund assets at the median or above for state pension funds in our sample.

We report the results as Model 2 in Table 6. Once we control for campaign contributions, the results are generally consistent with Hypothesis 1. The coefficient for State Pension—Above Median Assets No Contribution is negative and strongly significant, and larger than the coefficient for State Pension—Below Median Assets. The coefficient for State Pension—Above Median Assets Contribution, in contrast, is positive and insignificant. Assessed at the mean of all independent variables, a fifty percentage point increase in the fraction of lead plaintiffs that consists of State Pension—Above Median Assets No Contribution funds correlates with a 4.1 percentage point decrease in the attorney fee request (or 15.2% of the mean requested attorney fees). In comparison, a fifty percentage point increase in the fraction of lead plaintiffs that consists of State Pension—Below Median Assets funds correlates with a 2.7 percentage point decrease in the attorney fee request (or 10.0% of the mean requested attorney fees). Greater state public pension size does correlate with greater monitoring of plaintiffs' attorneys, but only if the state public pension officials have not received contributions from the lead attorneys. Larger public pension funds that receive campaign contributions do not negotiate for lower fees relative to individual lead plaintiffs. Moreover, they pay considerably higher fees than do pension funds that are not the recipients of campaign contributions.[15]

[15] We estimated a number of robustness tests for the models in Table 6. First, we re-estimated the models without the inclusion of the Low Loss variable (due to possible colinearity between greater losses

4.3. State Receptivity to Contributions

We postulated with Hypothesis 3 that the pervasiveness of the conflict created by campaign contributions might influence attorneys' fees. Table 7, Panel A shows the state pension funds that received campaign contributions in the highest proportion of cases were those in Colorado, New Mexico, and Pennsylvania, which all received contributions from plaintiffs' attorneys in each case in our sample where they appeared.

To assess the impact of the prevalence of conflict, we again estimate an ordinary least squares model with the log odds of the requested attorney fee percentage as the dependent variable (using case level data and robust standard errors). We define a state pension fund as a having a frequent conflict if the state pension fund is associated with a lead attorney that made a contribution to fund officials in more than seventy-five percent of the cases in our sample where the public pension fund acts as lead plaintiff. For our main independent variables of interest we then define State Pension—Frequent Conflict as the fraction of lead plaintiffs in a case that consists of state pension funds with a frequent conflict. We define State Pension—Infrequent Conflict as the fraction of

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and public pension funds). Unreported, the re-estimated models resulted in the same qualitative results as in Table 6.

Second, we re-estimated the models in Table 6 replacing State Pension, Local Pension, Labor Union, and Other Institution with binary versions of each variable equal to 1 if the lead plaintiff group has at least one lead plaintiff of the type in question and 0 otherwise. For each of the re-estimated model, we obtained the same qualitative results as in Table 6 with the following exception. The coefficient on Local Pension—Above Median Assets is negative but now significant at only the 5% level in Model 3.

Third, to control for selection effects, we re-estimate the models of Table 6 with a Heckman two-stage model. Stage two is the models from Table 6. Stage one is a model for settlement. For an instrument, we use the total number of securities class actions filed in the dataset time period for the district court in which the specific class action is filed (as discussed above in the robustness tests for Table 5). Unreported, the Heckman version of Model 1 returned the same qualitative results as in Table 6 with the following exceptions. The coefficient on State Pension—Above Median Assets in Model 1 is negative and now significant at the 5% level. The results in Model 2 remain qualitatively the same.

lead plaintiffs in a case that consists of state pension funds which do not receive campaign contributions in more than seventy-five percent of the cases in our sample for which the pension fund acts as lead plaintiff. The other independent variables are the same as those used in the regressions presented in Table 5.

$$\begin{aligned} \ln(\text{Atty\_Fee}_i/1\text{-Atty\_Fee}_i) = \; & \alpha + ß_{1i}\text{State Pension—Frequent Conflict}_i \\ & + ß_{2i}\text{StatePension—Infrequent Conflict}_i \\ & + ß_{3i}\,\text{Local Pension} + ß_{4i}\text{Labor Union} \\ & + ß_{5i}\,\text{Other Institution} + ß_{6i}\,\text{Low Loss} \\ & + \text{Case Controls} + \text{Circuit Effects} \\ & + \text{Year Effects} + \varepsilon_i \end{aligned}$$

We present the results in Model 1 of Table 7, Panel B. Consistent with Hypothesis 3, we find that state pension funds that receive campaign contributions from attorneys in a high proportion of their cases are quite generous with fees for those attorneys. These funds negotiate attorneys' fees that are significantly *higher* than the fees negotiated by individual plaintiffs, while the funds with infrequent conflicts negotiated significantly lower fees. Assessed at the mean of all independent variables, a fifty percentage point increase in the fraction of lead plaintiffs that consists of State Pension—Frequent Conflict funds correlates with a 4.7 percentage point *increase* in the attorney fee request (or 17.7% of the mean requested attorney fees). In contrast, a fifty percentage point increase in the fraction of lead plaintiffs that consists of State Pension—Infrequent Conflict funds correlates with a 3.1 percentage point decrease in the attorney fee request (or 11.7% of the mean requested attorney fees).

[Insert Table 7 About Here]

To assess further the overall receptivity of a fund to attorney political

contributions, we replace the State Pension—Frequent Conflict and State Pension—Infrequent Conflict variables with the following two variables. We define State Pension—Large Total Contribution as the fraction of lead plaintiffs in a case that consists of state public pensions with total contributions from any plaintiffs' attorney firm above $100,000, and State Pension—Small Total Contribution as the fraction of lead plaintiffs in a case that consists of state public pensions with total contributions from any plaintiffs' attorney firm at $100,000 or below. The results are consistent with Model 1; recipients of large contributions pay significantly higher attorneys' fees than do individual plaintiffs, while recipients of smaller contributions pay significantly less. Assessed at the mean of all independent variables, a fifty percentage point increase in the fraction of lead plaintiffs that consists of State Pension—Large Total Contribution funds correlates with a 5.1 percentage point *increase* in the attorney fee request (or 19.1% of the mean requested attorney fees). In contrast, a fifty percentage point increase in the fraction of lead plaintiffs that consists of State Pension—Small Total Contribution funds correlates with a 3.2 percentage point decrease in the attorney fee request (or 12.0% of the mean requested attorney fees). In sum, it appears that the funds that receive the biggest campaign contributions are providing very little monitoring, at least with respect to attorneys' fees.[16]

[16] We estimated a number of robustness tests for the models in Panel B of Table 7. First, we re-estimated the models without the inclusion of the Low Loss variable (due to possible colinearity between greater losses and public pension funds). Unreported, the re-estimated models resulted in the same qualitative results as in Table 7.

Second, we re-estimated the models in Table 7 replacing State Pension, Local Pension, Labor Union, and Other Institution with binary versions of each variable equal to 1 if the lead plaintiff group has at least one lead plaintiff of the type in question and 0 otherwise. For each of the re-estimated model, we obtained the same qualitative results as in Table 7 with the following exceptions. The coefficient on

4.4. Pension Counsel

We examine the influence of pension counsel who appear to be steering their local pension fund clients into appearing as lead plaintiff. As noted above, we discovered that two firms specializing in providing legal advice relating to pension administration for local governments represented a substantial percentage of the local government pension funds appearing as lead plaintiffs in our sample. Those firms have also made occasional appearances as counsel in securities class actions, but always as co-counsel alongside traditional class action firms. We did not postulate a predicted direction for their influence in Hypothesis 4.

We estimate an ordinary least squares model with the log odds of the requested attorney fee percentage as the dependent variable (using case level data and robust standard errors). For our main independent variables of interest, we use the same independent variables as in Model 1 of Table 5 except that we replace Local Pension with two variables: Pension Counsel and No Pension Counsel. We define Pension Counsel as equal to the fraction of the lead plaintiff group that consists of local pensions where at least one of the local pensions has a relationship with one of the two pension

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State-Pension—Frequent Conflict, while positive, is now not significant. The coefficients on Local Pension are negative but now significant at only the 10% level in Models 1 and 2.

Third, to control for selection effects, we re-estimate the models of Table 7 with a Heckman two-stage model. Stage two is the models from Table 7. Stage one is a model for settlement. For an instrument, we use the total number of securities class actions filed in the dataset time period for the district court in which the specific class action is filed (as discussed above in the robustness tests for Table 5). Unreported, the Heckman version of the models in Table 7 returned the same qualitative with the following exceptions. The coefficient on State Pension—Large Total Contribution is positive but now significant at only the 10% level.

counsel firms. We define No Pension Counsel as equal to the fraction of the lead plaintiff group that consists of local pensions without that relationship.

$$\ln(\text{Atty\_Fee}_i/1\text{-Atty\_Fee}_i) = \alpha + ß_{1i}\text{State Pension}_i + ß_{2i}\text{Pension Counsel} + ß_{2i}\text{No Pension Counsel} + ß_{3i}\text{Labor Union} + ß_{4i}\text{Other Institution} + ß_{5i}\text{Low Loss} + \text{Case Controls} + \text{Circuit Effects} + \text{Year Effects} + \varepsilon_i$$

The results are presented in Table 8, Panel B. We find that lead plaintiffs represented by the two pension counsel firms we identified appear to play the monitoring role anticipated by Congress when it adopted the lead plaintiff provision. The coefficient for Pension Counsel is negative and significant at the one percent level. Assessed at the mean of all independent variables, a fifty percentage point increase in the fraction of lead plaintiffs that consists of Pension Counsel funds correlates with a 3.0 percentage point *decrease* in the attorney fee request (or 11.4% of the mean requested attorney fees). Thus, local pension funds represented by these firms appear to play the same monitoring role as do the larger state pension funds.[17]

[17] We estimated a number of robustness tests for the model in Panel B of Table 8. First, we re-estimated the models without the inclusion of the Low Loss variable (due to possible colinearity between greater losses and public pension funds). Unreported, the re-estimated models resulted in the same qualitative results as in Table 8.

Second, we re-estimated the model in Table 8 replacing State Pension, Local Pension (as used in the definition of Pension Counsel and No Pension Counsel), Labor Union, and Other Institution with binary versions of each variable equal to 1 if the lead plaintiff group has at least one lead plaintiff of the type in question and 0 otherwise. For each of the re-estimated model, we obtained the same qualitative results as in Table 8.

Third, to control for selection effects, we re-estimate the model of Table 8 with a Heckman two-stage model. Stage two is the models from Table 8. Stage one is a model for settlement. For an instrument, we use the total number of securities class actions filed in the dataset time period for the district court in which the specific class action is filed (as discussed above in the robustness tests for Table 5). Unreported, we obtained the same qualitative results as in Table 8.

[Insert Table 8 About Here]

4.5. Case Quality

One question raised by the apparent agency cost problems that we have identified with respect to campaign contributions is the effect that campaign contributions might have on case selection. Are state pension funds induced to bring frivolous suits by campaign contributions?

To assess this possibility, we estimate a logit regression with the same independent variables as Table 5. Our binary dependent variable is coded as a 1 for cases that produced a dismissal or settlement for nuisance value, which we define as less than $3 million. This is a conservative estimate of defense costs, so we presume that settlements for less than that amount had little merit.

[Insert Table 9 About Here]

The results are presented in Table 9. The only coefficient that is consistently significant in the three models is Labor Union, which is negative and significant at the five percent level. Thus, the presence of labor unions appears to correlate with suits of greater merit. The coefficients for state pension funds are consistently insignificant, whether or not we control for campaign contributions. We conclude that there is no evidence that campaign contributions induce state pension funds to appear as lead plaintiffs in cases of dubious merit. Rather, campaign contributions appear to be a tool that plaintiffs' lawyers use to gain advantage in the competition to be appointed class

counsel in cases that attract multiple plaintiffs' firms, which is likely to be the cases with the most obvious evidence of fraud and the greatest potential damages.[18]

5. Conclusion

Congress adopted the lead plaintiff provision of the PSLRA because members of Congress believed that individual investors were mere figurehead plaintiffs who did little to monitor plaintiffs' attorneys. Institutional investors, it was thought, would act as more active monitors. The evidence to date suggests that institutional investors have made a difference in bargaining for lower fees, which likely translates into greater net recovery for investors. Those findings are confirmed here with respect to state pension funds in general. We also find that local pension funds, while generally having smaller stakes in class action recoveries, appear to also act as active monitors.

Congress worried, however, that the benefits of the lead plaintiff provision could potentially be undermined by side payments from counsel to the lead plaintiffs. The PSRLA prohibits lead plaintiffs from obtaining more than their pro rata share. The political contributions received by state pension funds raise the question of whether these funds are receiving selective benefits from the class action recovery in violation of that provision.

[18] We estimated a number of robustness tests for the models in Table 9. First, we re-estimated the models without the inclusion of the Low Loss variable (due to possible colinearity between greater losses and public pension funds). Unreported, the re-estimated models resulted in the same qualitative results as in Table 9. The coefficient on Labor Union is negative and significant at the 1% level in all three models.

Second, we re-estimated the models in Table 9 replacing State Pension, Local Pension, Labor Union, and Other Institution with binary versions of each variable equal to 1 if the lead plaintiff group has at least one lead plaintiff of the type in question and 0 otherwise. For each of the re-estimated model, we obtained the same qualitative results as in Table 9.

Political contributions plainly have an impact. The evidence presented here shows that the greater monitoring produced by the lead plaintiff provision in general for state pension funds largely disappears when state pensions are the recipients of political contributions. When it comes to negotiating for fees, state pension funds that take political contributions are indistinguishable from the figurehead individual investors that Congress was targeting with the PSRLA.

This result is hardly surprising, but it has potentially important implications. Courts have generally been skeptical of allegations of pay to play in the selection of class counsel, with some suggesting that the problem is more theoretical than real. We have shown, however, that pay to play imposes a real cost on investors in class actions, who end up paying greater attorneys' fees. Courts may be justified in taking a closer look when state pension funds that have received political contributions come forward to seek lead plaintiff status. The evidence presented here suggests that such institutions should not be presumed to be the vigorous monitors that Congress anticipated when it adopted the PSLRA.

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Table 1: Sample Description

Full Sample

Outcome	Freq.	Percent
Settlement	271	49.72
Settlement ≤ $3 M.	81	14.86
Settlement > $3 M.	190	34.86
Trial Verdict or Judgment on Pleadings for Plaintiff	2	0.37
Dismissal	272	49.91
Total	545	100.00

Settlement Sample

Year of Filing	Freq.	Percent
2003	77	28.41
2004	87	32.1
2005	63	23.25
2006	38	14.02
2007	6	2.21
Total	271	100.00

Circuit Court	Freq.	Percent
1	17	6.27
2	52	19.19
3	28	10.33
4	10	3.69
5	23	8.49
6	9	3.32
7	8	2.95
8	10	3.69
9	69	25.46
10	17	6.27
11	27	9.96
DC	1	0.37
Total	271	100.00

Table 2: Summary Statistics for Settled Class Actions

	N	Mean	Std. Dev.
Low Loss	271	0.358	0.480
Rule 10b-5	269	0.955	0.207
Section 11	270	0.193	0.395
Section 14	271	0.037	0.189
Restatement	267	0.438	0.497
Govt. Investigation	271	0.273	0.446
Officer Termination	271	0.373	0.484
Auditor Termination	263	0.076	0.266
Insider Trading	266	0.549	0.499
Settlement Amount	268	20.963	84.399
Market Capitalization	261	3054.470	13097.150
Turnover	257	0.874	0.214
Minimum Return	258	-0.280	0.147
High Tech	271	0.159	0.366
FDA	267	0.026	0.160

Variable definitions are in the appendix.

Table 3: Lead Plaintiffs for Settled Class Actions

Panel A: Lead Plaintiff Types

Lead Plaintiff	Cases with at least One Lead Plaintiff of the Type	Percentage of Cases	Mean Fraction of Lead Plaintiffs Per Case
Institution	148	55.8%	
Public Pension	46	17.4%	0.126
State	22	8.3%	0.064
Local	24	9.1%	0.062
Pension Counsel	14	5.3%	0.043
Labor Union	65	24.5%	0.186
Other Institution	62	23.4%	0.137

Lead Plaintiff	Cases	Percentage of Cases
Individual Only	117	44.2%
Total Cases with Lead Plaintiff Information	265	100.0%

Panel B: Pension Fund Assets and Losses

		N	Mean	p25	p50	p75	Std. Dev.
Public Pension	Assets	43	11646.0	427.8	3666.4	10616.4	22900.2
	Losses	35	3.5	0.2	0.6	1.8	11.5
State	Assets	22	14996.3	3507.1	6119.4	16522.3	20392.3
	Losses	15	7.3	0.4	1.8	3.7	17.1
Local	Assets	21	8136.2	92.9	427.8	3666.4	25285.6
	Losses	20	0.6	0.1	0.3	0.7	0.8
Labor Union	Assets	64	1147.0	271.1	572.4	909.5	3188.5
	Losses	49	0.8	0.1	0.2	0.6	2.2

Pension fund assets are in millions of dollars, measured as of 2005.

Table 4: Campaign Contributions

Attorney Contribution to State Pension Fund Lead Plaintiffs

	Cases	Percentage	Mean Total Contribution - By Case (Median)	Std. Dev.	Mean Total Contribution - Aggregate (Median)	Std. Dev.
Contribution	10	45.5%	39,223 (11,750)	65,906	52,170 (28,350)	55,375
No Contribution	12	54.6%				

Table 5: Campaign Contributions and Attorneys' Fees

Panel A

	N	Mean	Std. Dev.
Requested Fee	238	0.267	0.335

Panel B

	Model 1	Model 2	Model 3
State Pension	-0.303**		
	(-3.50)		
State Pension—Contribution		-0.147	
		(-0.92)	
State Pension—Contribution ≥ Median			0.005
			(0.02)
State Pension—Contribution < Median			-0.313**
			(-3.19)
State Pension—No Contribution		-0.374**	-0.363**
		(-4.06)	(-3.95)
Local Pension	-0.280**	-0.276**	-0.265**
	(-3.11)	(-3.05)	(-2.91)
Labor Union	-0.076	-0.071	-0.063
	(-1.55)	(-1.48)	(-1.34)
Other Institution	-0.024	-0.024	-0.020
	(-0.46)	(-0.45)	(-0.37)
Low Loss	0.064*	0.071*	0.070*
	(1.99)	(2.16)	(2.13)
Constant	-0.747**	-0.743**	-0.709**
	(-5.54)	(-5.75)	(-5.78)
Case Controls	Yes	Yes	Yes
Circuit Effects	Yes	Yes	Yes
Year Effects	Yes	Yes	Yes
N	217	216	216
R^2	0.346	0.357	0.364

t statistics in parentheses (determined with robust standard errors); $^{+}$ $p < 0.10$, * $p < 0.05$, ** $p < 0.01$. Case Controls include the Section 11, Section 14, Govt. Investigation, Restatement, Officer Term., Auditor Term., Insider Trading Claim, ln(Settlement Amount), ln(Market Capitalization), Turnover, Minimum Return, High Tech, and FDA variables. Circuit Effects include indicator variables for the Second, Third, Fifth, Ninth, and Eleventh circuits. Year Effects are for the year the suit was resolved.

Table 6: Pension Fund Assets and Attorney Fees

	Model 1	Model 2
State Pension—Above Median Assets	-0.303	
	(-1.41)	
State Pension—Above Median Assets Contribution		0.085
		(0.20)
State Pension—Above Median Assets No Contribution		-0.444*
		(-2.57)
State Pension—Below Median Assets	-0.297**	-0.288**
	(-4.25)	(-4.20)
Local Pension—Above Median Assets	-0.457**	-0.449**
	(-3.58)	(-3.45)
Local Pension—Below Median Assets	-0.077	-0.060
	(-1.11)	(-0.90)
Labor Union—Above Median Assets	-0.107	-0.092
	(-1.60)	(-1.41)
Labor Union—Below Median Assets	-0.036	-0.029
	(-0.66)	(-0.55)
Other Institution	-0.019	-0.010
	(-0.38)	(-0.20)
Low Loss	0.055+	0.057+
	(1.68)	(1.74)
Constant	-0.740**	-0.697**
	(-5.60)	(-5.71)
Case Controls	Yes	Yes
Circuit Effects	Yes	Yes
Year Effects	Yes	Yes
N	217	216
R^2	0.368	0.385

t statistics in parentheses (determined with robust standard errors); + $p < 0.10$, * $p < 0.05$, ** $p < 0.01$. Case Controls include the Section 11, Section 14, Govt. Investigation, Restatement, Officer Term., Auditor Term., Insider Trading Claim, ln(Settlement Amount), ln(Market Capitalization), Turnover, Minimum Return, High Tech, and FDA variables. Circuit Effects include indicator variables for the Second, Third, Fifth, Ninth, and Eleventh circuits. Year Effects are for the year the suit was resolved.

Table 7: State Receptivity to Contributions

Panel A

State	Fraction of Cases with a Contributing Attorney
AR	0.50
CO	1.00
LA	0.58
NM	1.00
NY	0.00
OK	0.50
PA	1.00
PR	0.00
VA	0.00

Panel B

	Model 1	Model 2
State Pension—Frequent Conflict	0.467**	
	(3.79)	
State Pension—Infrequent Conflict	-0.341**	
	(-4.55)	
State Pension—Large Total Contribution		0.501**
		(4.81)
State Pension—Small Total Contribution		-0.347**
		(-4.66)
Local Pension	-0.255**	-0.257**
	(-2.79)	(-2.83)
Labor Union	-0.062	-0.062
	(-1.31)	(-1.31)
Other Institution	-0.016	-0.016
	(-0.31)	(-0.31)
Low Loss	0.067*	0.066*
	(2.08)	(2.04)
Constant	-0.684**	-0.689**
	(-5.78)	(-5.80)
Case Controls	Yes	Yes
Circuit Effects	Yes	Yes
Year Effects	Yes	Yes
N	217	217
R^2	0.383	0.385

t statistics in parentheses (determined with robust standard errors); $^{+}$ $p < 0.10$, * $p < 0.05$, ** $p < 0.01$. Case Controls include the Section 11, Section 14, Govt. Investigation, Restatement, Officer Term., Auditor

Term., Insider Trading Claim, ln(Settlement Amount), ln(Market Capitalization), Turnover, Minimum Return, High Tech, and FDA variables. Circuit Effects include indicator variables for the Second, Third, Fifth, Ninth, and Eleventh circuits. Year Effects are for the year the suit was resolved.

Table 8: Pension Counsel

Panel A: Incidence of Pension Counsel Relationship Among Local Pension Funds

	Number of Cases	Percentage
Pension Counsel	21	44.68%
No Pension Counsel	26	55.32%

Panel B

	Model 1
State Pension	-0.297**
	(-3.43)
Pension Counsel	-0.327**
	(-3.04)
No Pension Counsel	-0.120
	(-0.94)
Labor Union	-0.0763
	(-1.56)
Other Institution	-0.0204
	(-0.39)
Low Loss	0.0696*
	(2.15)
Constant	-0.745**
	(-5.49)
Case Controls	Yes
Circuit Effects	Yes
Year Effects	Yes
N	217
R^2	0.352

t statistics in parentheses (determined with robust standard errors); $^{+}$ $p < 0.10$, * $p < 0.05$, ** $p < 0.01$. Case Controls include the Section 11, Section 14, Govt. Investigation, Restatement, Officer Term., Auditor Term., Insider Trading Claim, ln(Settlement Amount), ln(Market Capitalization), Turnover, Minimum Return, High Tech, and FDA variables. Circuit Effects include indicator variables for the Second, Third, Fifth, Ninth, and Eleventh circuits. Year Effects are for the year the suit was resolved.

Table 9: Nuisance Outcome

	Model 1	Model 2	Model 3
State Pension	-0.555		
	(-1.06)		
State Pension—Contribution	0.0147	0.0185	0.00706
	(0.03)	(0.04)	(0.01)
State Pension—Contribution ≥ Median		-1.003	
		(-1.23)	
State Pension—Contribution < Median		-0.264	-0.276
		(-0.41)	(-0.43)
State Pension—No Contribution			-1.735
			(-1.21)
Local Pension			-0.595
			(-0.58)
Labor Union	-0.832*	-0.828*	-0.835*
	(-2.50)	(-2.48)	(-2.51)
Other Institution	-0.0363	-0.0156	-0.0224
	(-0.09)	(-0.04)	(-0.06)
Low Loss	0.412+	0.416+	0.416+
	(1.71)	(1.72)	(1.72)
Constant	-0.0141	-0.396	-0.497
	(-0.01)	(-0.32)	(-0.40)
Case Controls	Yes	Yes	Yes
Circuit Effects	Yes	Yes	Yes
Year Effects	Yes	Yes	Yes
N	458	454	454
R^2	0.166	0.164	0.165

z statistics in parentheses; + $p < 0.10$, * $p < 0.05$, ** $p < 0.01$. Case Controls include the Section 11, Section 14, Govt. Investigation, Restatement, Officer Term., Auditor Term., Insider Trading Claim, ln(Settlement Amount), ln(Market Capitalization), Turnover, Minimum Return, High Tech, and FDA variables. Circuit Effects include indicator variables for the Second, Third, Fifth, Ninth, and Eleventh circuits. Year Effects are for the year the suit was resolved.

Appendix: Variable Definitions

Key Independent Variables

Variable	Description
Public Pension	The fraction of lead plaintiffs in a case that consists of a public pension fund.
State Pension—Contribution	The fraction of lead plaintiffs in a case that consists of state pension funds with officials who received political contributions from the lead attorneys.
State Pension—Contribution Above Median	The fraction of lead plaintiffs in a case that consists of state pensions with a contribution from the lead plaintiffs at the median or above for all contributions in our sample.
State Pension—Contribution Below Median	The fraction of lead plaintiffs in a case that consists of state public pensions with a contribution from the lead plaintiffs below the median for all contributions in our sample.
State Pension—No Contribution	The fraction of lead plaintiffs in a case that consists of state pension funds with officials who did not receive political contributions from the lead attorneys.
State Pension—Above Median Assets	The fraction of lead plaintiffs in a case that consists of state pension funds with total fund assets at the median or above for state public pensions in our sample.
State Pension—Below Median Assets	The fraction of lead plaintiffs in a case that consists of state pension funds with total fund assets below the median for state public pensions in our sample.
State Pension—Frequent Conflict	The fraction of lead plaintiffs in a case that consists of state pension funds with a frequent conflict. Frequent conflict is defined to occur when a state pension fund is associated with a lead attorney who made a contribution to fund officials in more than 75% of the cases in our sample where the public pension fund acts as lead plaintiff.
State Pension—Infrequent Conflict	The fraction of lead plaintiffs in a case that consists of state pension funds without a frequent conflict. Frequent conflict is defined to occur when a state pension fund is associated with a lead attorney who made a contribution to fund officials in more than 75% of the cases in our sample in which the state pension fund acts as lead plaintiff.
Local Pension	The fraction of lead plaintiff in a case that consists of local government pension funds.
Pension Counsel	The fraction of lead plaintiffs in a case that consists of a local pension funds with a relationship with either the Klausner or Vanoverbeeke law firms.

No Pension Counsel	The fraction of lead plaintiffs in a case that consists of a public pension without a relationship with either the Klausner or Vanoverbeeke law firms.
Labor Union	The fraction of the lead plaintiffs that consists of a labor union.
Other Institution	The fraction of lead plaintiffs in a case that are institutions but not public pensions or labor unions.
Low Loss	Indicator variable defined as equal to 1 if the lead plaintiffs for the case are at the median or lower for all the lead plaintiffs in our sample or 0 otherwise.

Other Independent Variables

Case Control Variables	Description
Section 11	Indicator variable equal to 1 if the complaint for a particular class action alleged a Section 11 of the Securities Act of 1933 violation and 0 otherwise.
Section 14	Indicator variable equal to 1 if the complaint for a particular class action alleged a Section 14 of the Securities Exchange Act of 1934 violation and 0 otherwise.
Govt. Investigation	Indicator variable equal to 1 if the complaint indicated the presence of a SEC or other governmental investigation or enforcement action relating to the fraud at issue and 0 otherwise.
Restatement	Indicator variable equal to 1 if the complaint indicated that the company announced a restatement covering at least part of the class period and 0 otherwise.
Officer Term.	Indicator variable equal to 1 if the complaint indicated that a top officer of the defendant company resigned or was terminated during the class period and 0 otherwise.
Auditor Term.	Indicator variable equal to 1 if the complaint indicated that the auditor resigned or was terminated during the class period and 0 otherwise.
Insider Trading	Indicator variable equal to 1 if the complaint alleged insider trading and 0 otherwise.
Market Capitalization	Market value of a company's common equity (in $ millions) at the end of the fiscal year preceding the beginning of the class period.
Settlement Amount	The settlement amount for the class action.
High Tech	Indicator variable equal to 1 if the firm is in SIC codes 3570-3577 or 7370-7379 and 0 otherwise.
FDA	Indicator variable equal to 1 if the last amended complaint for a particular class action is based on U.S. Food and Drug Administration-related disclosures and 0 otherwise.