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Abstract:

This Article seeks what may be the holy grail of securities law scholarship - the role of the "merits" in securities class actions - by investigating the relationship between settlements and D&O insurance. Drawing upon in-depth interviews with plaintiffs' and defense lawyers, D&O claims managers, monitoring counsel, brokers, mediators, and testifying experts, we elucidate the key factors influencing settlement and examine the relationship between these factors and notions of merit in civil litigation. We find that, although securities settlements are influenced by some factors that are arguably merit-related, such as the sex appeal of a claim's liability elements, they are also influenced by many that are not, including, most obviously, the amount and structure of D&O insurance. The virtual absence of adjudication results in payment to the plaintiffs' class for every claim surviving the motions stage and, as importantly, a lack of authoritative guidance about merit at settlement. Without such adjudication, the weight of various factual patterns is untested, and the validity of competing damages models remains unknown. Parties structure their settlement by reference to other settlements, but these are opaque and subject to the same set of distortions. In this murky environment, plaintiffs and defendants collude to pressure the D&O insurer to settle on terms that may not reflect the ultimate merits of the claim. More adjudication, we argue, would be the best solution to the problem, but barring that, disclosure of D&O insurance and settlement terms would offer some improvement.

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