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Rules Committee Support Office
Administrative Office of the United States Courts
One Columbus Circle, NE
Washington, D.C. 20544

Dear Sir:

Please consider the enclosed article as a suggestion for the Rules Advisory Committee. The article presents the results of a study of fee awards in settled securities fraud class actions. In the last section, my coauthors and I present a reform proposal that would help federal judges size fee award more accurately and objectively, and that would also make the process more transparent.

Sincerely,

Charles Silver

"I am Charlie"

Papers posted on SSRN: http://papers.ssrn.com/Author_id=164490
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IS THE PRICE RIGHT?
AN EMPIRICAL STUDY OF FEE-SETTING IN SECURITIES CLASS ACTIONS

Lynn A. Baker,* Michael A. Perino** and Charles Silver***

Every year, fee awards enable millions of people to obtain access to justice and strengthen the deterrent effect of the law by motivating lawyers to handle class actions. But the process by which judges decide how much to pay lawyers remains a black box. Settlements go in one side; fee awards come out the other. The inputs and outputs have been studied, but the actual operation of the fee-setting mechanism has not. Consequently, it is difficult to know why judges award the amounts they do or whether they size fee awards correctly.

Both numerically and in terms of dollars recovered, securities cases dominate the federal courts' class action docket. We therefore undertook to peer into the fee-setting black box by studying in detail all of the 434 securities class actions that settled in federal district courts from 2007 through 2012. We examined the actual court filings in each case to create an original, comprehensive dataset of information on all points at which federal judges are likely to consider issues relating to fees. These data enable us to paint a picture of the fee-setting process that is unusually detailed and nuanced and that falsifies many common beliefs.

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Among our major findings are that: (1) federal judges often deviate from the path Congress laid out in the Private Securities Litigation Reform Act (PSLRA), which requires lead plaintiffs to set the terms of class counsel's retention and federal judges to serve as backstops against abuses; (2) fees tend to be lower in federal districts that see a high volume of securities class actions than in districts that handle these cases less often; (3) fee cuts are significantly more likely among judges that see a high volume of securities class actions than among low volume judges; (4) the well-known "decrease-increase" rule, according to which fee percentages decline as settlements become larger, operates mainly in high-volume districts; and (5) judges appear to cut fees randomly, that is, on the basis of their own predilections rather than the merits of fee requests. Finally, we learn that so-called "lodestar cross-checks," which require judges to consider the "time and labor expended by counsel" and other factors to ensure against excessive fees, accomplish nothing. Actual fee awards reflect something closer to a pure "percentage of the fund" approach.

In sum, we found little evidence that the actions currently taken by the courts in securities class actions move class counsel's fees closer to the "right price." We therefore propose a set of procedural reforms which courts could easily adopt that would make fee-setting in securities class actions more transparent, more compatible with the normative goals of the PSLRA, and more predictable. The reforms would encourage lawyers to invest optimally in class actions, with salutary effects for investors seeking compensation and the integrity of the financial markets.

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I. INTRODUCTION

Every year, class action settlements bring $10-$20 billion into federal courts.[1] And every year, federal judges award billions of these dollars to plaintiffs' attorneys in payment of fees and reimbursement of expenses.[2] The payments are essential. But for these awards, the incentive to wage class actions—which entail enormous commitments of time and financial resources—would disappear. One can say, without exaggeration, that federal judges enable millions of people to obtain access to justice each year by rewarding lawyers for litigating class actions successfully.

Yet, the process by which fee and cost awards are set is a black box. Settlements go in; awards come out. Little is known about the mechanism that earmarks dollars for attorneys.[3] Consequently, it is difficult to know why fee

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[1] *See* Brian T. Fitzpatrick, *An Empirical Study of Class Action Settlements and Their Fee Awards*, 7 J. EMPIRICAL LEGAL STUD. 811, 825 (2010) (hereafter "Fitzpatrick 2010") (studying all class actions that settled in federal courts in 2006 and 2007 and reporting total recoveries of $22 billion and $11 billion, respectively).

[2] *Id.* at 831 (reporting $2.9 billion in fee and expense awards in 2006 and $2.1 billion in 2007).

[3] The empirical literature on fee awards in class actions is large, but only one study to date has looked at fee award procedures in any detail. *See* Lynn A. Baker, Michael A. Perino, and Charles Silver, *Setting Attorneys' Fees in Securities Class Actions: An Empirical Assessment*, 66 VAND. L.

awards are sized as they are. Studies have shown that more dollars flow to lawyers when settlements are larger; that, in percentage terms, awards tend to decline as recoveries rise; and that investors get more "bang for the buck" in securities fraud class actions when public pension funds serve as lead plaintiffs.[4] But the causes of these phenomena remain hidden from view because researchers have not peered inside the fee-setting mechanism.

The reason for this is simple: It takes work—a lot of it—to study fee-setting processes in action. In securities fraud cases, which account for about 40 percent of all federal class actions and over 70 percent of all federal class action recoveries, the mechanism first cranks up when the court appoints the lead plaintiff and lead counsel at the start of litigation.[5] To study just this part of the process, one must review the pleadings, motions, and declarations filed by the parties and lawyers seeking control of the case, along with the order entered by the court. With seventy to eighty settlements per year and two or more parties per case seeking appointment as the lead plaintiff, it takes substantial effort just to determine which parties and lawyers sought control, who won, and whether judges considered compensation terms when selecting the winners.[6] To make

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REV. 1677 (2013) (hereinafter "Baker et al. 2013") (examining fee setting practices in three district courts). All of the other studies focus solely on inputs (settlements), outputs (fee and cost awards), and case characteristics (subject matter of the litigation, named plaintiff type, duration, etc.). *See, e.g.,* Brian T. Fitzpatrick, *An Empirical Study of Class Action Settlements and Their Fee Awards*, 7 J. EMPIRICAL LEGAL STUD. 811 (2010) (finding that fees vary with the size of the settlement, the age of the case, and where the case is litigated); Theodore Eisenberg & Geoffrey P. Miller, *Attorney Fees and Expenses in Class Action Settlements: 1993–2008*, 7 J. EMPIRICAL LEGAL STUD. 248 (2010); Robert H. Lande & Joshua P. Davis, *Benefits from Private Antitrust Enforcement: An Analysis of Forty Cases*, 42 U.S.F. L. REV. 879 (2008) (reporting data on the size of fee awards in antitrust cases); Eric Helland & Jonathan Klick, *The Effect of Judicial Expedience on Attorney Fees in Class Actions*, 36 J. LEG. STUD. 171 (2007) (finding that class action fee awards are positively correlated with measures of court congestion); Theodore Eisenberg & Geoffrey P. Miller, *Attorney's Fees in Class Action Settlements: An Empirical Study*, 1 J. EMPIRICAL LEG. STUD. 27 (2004) (documenting a strong correlation between fees and settlement size and noting inter-circuit variations in fee awards); William J. Lynk, *The Courts and the Plaintiff's Bar: Awarding the Attorney's Fee in Class-Action Litigation*, 23 J. LEG. STUD. 185, 195-204 (finding that lodestar amounts better explain actual fee awards than percentage of recovery methods).

[4] Perino, *supra* note __, at 369.

[5] Fitzpatrick 2010, *supra* note __, at 818, 825.

[6] Although most existing studies of fee awards in securities class actions control for the type of investor that served as lead plaintiff, *see, e.g.,* Perino, *supra* note __, at 384, no study quantifies

matters more challenging, the relevant documents must often be obtained directly from courts because they are not available electronically. The process must then be repeated for each case at the settlement stage, where the items to be collected and reviewed include motions for settlement approval and fee awards, supporting affidavits, objections, responses to objections, and the court's various orders.

Do the stakes justify the effort needed to peer inside the black box? We think so. More than just billions of dollars in compensation and access to justice for millions of people are at issue. The law's ability to influence conduct outside the courthouse also hangs in the balance. By setting fees too high or too low, judges would incentivize lawyers to bring too many class actions or too few. Excessive litigation would over-deter primary conduct that is desirable; insufficient litigation would under-deter primary conduct that is unwanted. These consequences will occur in all areas where class actions are brought: antitrust, civil rights, consumer protection, labor and employment, employee benefits, RICO, and, of course, financial fraud. The deep reason for opening the black box is to learn whether the procedural system operates in ways that are reasonably thought to advance the goals of substantive laws.

The need is especially acute in the securities area, both because securities fraud cases dominate the federal class action docket and because Congress instructed judges legislatively how to handle fee awards in these cases. In 1995, Congress adopted the Private Securities Litigation Reform Act (PSLRA) because it viewed the securities class action system as dysfunctional and abusive.[7] One problem was that the litigants who served as representative plaintiffs were often

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the frequency with which lead plaintiffs and the lawyers they hire bargain over fees, describes the fee terms that such arms' length bargaining produces, or documents the frequency with which privately negotiated fee agreements are offered into the record for judges to review and consider when ruling on class counsel's motion for attorneys' fees at the end of the case. Any belief that the documented reduction in agency costs under the PSLRA is due to lead plaintiffs who aggressively negotiate *ex ante* fee agreements with the attorneys they hire is only a surmise.

[7] It is certainly possible to debate the accuracy of that description. *See* Myriam Gilles & Gary B. Friedman, *Exploding the Class Action Agency Cost Myth: The Social Utility of Entrepreneurial Lawyers*, 155 U. PA. L. REV. 103 (2006); Joel Seligman, *The Merits Do Matter: A Comment on Professor Grundfest's "Disimplying Private Rights of Action under the Federal Securities Laws: The Commission's Authority*, 108 HARV. L. REV. 438 (1994).

small investors who would not or could not monitor class counsel effectively.[8] They were figureheads for lawyers who financed the cases, ran them as they wished, and, for all important purposes, were the real parties in interest.[9]

Another problem was that federal judges had failed to police the conduct of class actions on their own. Although charged by the rules to act as guardians for absent class members, judges were at least as interested in getting cases off their dockets as they were in rooting out abuses.[10] Judges lacked the means to police abuses too. They could not rely on the parties who proposed settlements to bring problems to their attention, and they could not (always) rely on objectors to do so either. Objectors only appeared in some cases, and their agendas were often suspect. Many objectors were hold-up artists bent on extorting payments.

By enacting the PSLRA, Congress gave class action procedure a complete overhaul.[11] Seeking to rely less on judges and objectors and more on incentives, it put class actions under the control of sophisticated investors with large financial stakes.[12] The hope was that these investors would seek to maximize their own net

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[8] H.R. REP. NO. 104-369, at 32 (1995) (Conf. Rep.), reprinted in 1995 U.S.C.C.A.N. 730, 731. Among other abuses, lawyers paid kickbacks to individuals who held a few shares of likely litigation targets who were willing to serve as the needed representative plaintiff. Those individuals obviously could not be expected to vigorously monitor class counsel, particularly with respect to attorneys' fees requests. Kickbacks were often a percentage of the lawyers' fee and, therefore, the representative plaintiff would have an incentive to maximize rather than minimize fees. *See* MICHAEL A. PERINO, THE MILBERG WEISS PROSECUTION: NO HARM, NO FOUL? (AEI 2008).

[9] Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1, 7-8 (1991); John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of law Through Class and Derivative Actions*, 86 COLUM. L. REV. 669 (1986).

[10] See Janet C. Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STAN. L. REV. 497 (1991).

[11] Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (codified in scattered sections of 15 U.S.C.); see 15 U.S.C. §§ 77z-1(a)(3), 78u-4(a)(3) (2006) (establishing procedural guidelines for determining lead plaintiffs).

[12] *See, e.g.,* H.R. REP. NO. 104-369, at 32 (1995) (Conf. Rep.), reprinted in 1995 U.S.C.C.A.N. 730, 731 (noting Congress's intent to "increase the likelihood that parties with significant holdings in issuers, whose interests are more strongly aligned with the class of shareholders, will participate in the litigation and exercise control over the selection and actions of plaintiffs counsel").

recoveries by maximizing the net recoveries for everyone.[13] They would use contingent fee arrangements to incentivize excellent attorneys to obtain good results, while using competition among lawyers to obtain bargain rates. Sophisticated investors would also evaluate settlements, reducing the burden on judges, who are poorly placed to figure out whether proposed deals are good or bad.

Empirical studies of inputs and outputs suggest that the PSLRA has been a reasonable success. Although many of the most sophisticated private investment funds still refuse to serve as lead plaintiffs,[14] public pension funds have volunteered in numbers, and their use of the mechanisms created by the PSLRA appears to be reducing agency costs.[15] Cases led by public pension funds tend to have higher recoveries and lower attorneys' fees than other securities class actions, controlling for important case characteristics.[16] Even in cases led by other kinds of plaintiffs, attorneys' fees have declined significantly over time.[17]

Without looking inside the black box, however, it is impossible to know whether the credit for these successes belongs to the PSLRA or to other aspects of the fee-setting mechanism. The documented reduction in attorneys' fees and other agency costs could be the result of hard bargaining between institutional

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[13] *See* Elliott J. Weiss & John S. Beckerman, *Let the Money Do the Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions*, 104 YALE L.J. 2053, 2105 (1995). *See also Elliot J. Weiss, The Lead Plaintiff Provisions of the PSLRA after a Decade, or "Look What's Happened to My Baby,"* 61 VAND. L. REV. 543 (2008).

[14] *See* Michael A. Perino, *Have Institutional Fiduciaries Improved Securities Class Actions? A Review of the Empirical Literature on the PSLRA's Lead Plaintiff Provision*, in HANDBOOK OF INSTITUTIONAL INVESTMENT AND FIDUCIARY DUTY (Cambridge University Press 2013).

[15] *See, e.g.*, Stephen J. Choi, A. C. Pritchard & Jill E. Fisch, *Do Institutions Matter? The Impact of the Lead Plaintiff Provision of the Private Securities Litigation Reform Act*, 83 WASH. U. L.Q. 869, 879 (2005); James D. Cox & Randall S. Thomas, *Does the Lead Plaintiff Matter? An Empirical Analysis of Lead Plaintiffs in Securities Class Actions*, 106 COLUM. L. REV. 1587, 1588–93 (2006); James D. Cox, Randall S. Thomas & Lynn Bai, *There Are Plaintiffs and . . . There Are Plaintiffs: An Empirical Analysis of Securities Class Action Settlements*, 61 VAND. L. REV. 355, 367 (2008); C.S. Agnes Cheng *et al.*, *Institutional Monitoring through Shareholder Litigation*, 95 J. FIN. ECON. 356 (2010); Michael Perino, *Institutional Activism through Litigation: An Empirical Analysis of Public Pension Fund Participation in Securities Class Actions*, 9 J. EMPIRICAL LEGAL STUD. 368, 369–70 (2012).

[16] Perino, *supra* note __, at 369.

[17] *Id.* at 370.

lead plaintiffs and class counsel.[18] But the credit could, at least in part, also belong to federal judges, who may use the fees awarded in cases with public pension lead plaintiffs as the model for fees in other cases. The fact that fees have fallen in securities class actions of all types since the enactment of the PSLRA, including those led by other investors, suggests that judges are playing an important role.[19]

To learn how fee awards in class actions are set and whether the PSLRA is working as Congress intended, we created an original database with information on all of the 434 securities class action settlements that were announced between January 1, 2007 and December 31, 2012 in the federal district courts in the United States. Our database is uniquely rich because it contains details gathered from the actual court filings in each of the cases, in addition to the settlement amounts and fee awards on which other studies rely. We know the number and type of plaintiffs who sought control of class litigation, the terms of any agreements regarding fees and costs that were disclosed to the courts, the amounts requested as fees, the formulas for calculating fees that judges were asked to employ, the presence and number of objectors, and many other details. This information enables us to shine a powerful light inside the black box.

Our granular approach to analyzing the fee setting process yields a picture that is far more nuanced than—and significantly different from—that suggested by the conventional wisdom, which is that institutional investors are solely

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[18] This has been suggested by Professor Weiss, for example, who has contended that the mechanism he co-conceived is working as it should. In an article reflecting on developments in the post-PSLRA era, he wrote:

> Consistent with our expectations, institutional investors that have sought appointment as lead plaintiff generally have negotiated fee arrangements with the law firms they have retained that provide for percentage fees far lower than had been the norm prior to passage of the PSLRA. Many institutional lead plaintiffs also have actively monitored class actions in which they have served as lead plaintiff and have pushed for larger settlements, recoveries from individual defendants responsible for corporate frauds, and governance reforms directed at preventing corporate wrongdoing from recurring.

Weiss, *supra* note __, at 552-553. Professor Weiss could be right, but the studies on which he relies shed no light on how the observed reduction in attorneys' fees and other agency costs has been obtained.

[19] *See* Perino, *supra* note __, at 385-89.

responsible for recent improvements in the operation of securities class actions. Many of our findings show that the PSLRA has not worked as hoped. For example, although the statute was supposed to encourage lead plaintiffs to bargain over fees with class counsel at the start of litigation, we find that cases with *ex ante* fee agreements are the exception rather than the rule. And although courts are making smaller fee awards, in the vast bulk of cases that does not appear to be because they are explicitly choosing to abide by fee agreements negotiated between lead plaintiffs and their chosen counsel. The truth appears to be that, instead of enforcing (and requiring) such *ex ante* fee agreements, the courts in most cases set fees in precisely the same manner they did before passage of the PSLRA—*ex post*, after a settlement has already been reached.

Equally troubling is our finding that the market for attorneys' fees may be even more imperfect than previously suspected.[20] Our data reveal that the market for attorneys' fees is geographically segmented. Judges from high volume districts (those that see securities class actions more frequently) set fees that are significantly different from those set by judges from low volume districts. Our data also suggest that plaintiffs' attorneys may be aware of and may seek to exploit these market imperfections by asking courts for significantly higher fees in low volume districts than in high volume ones.

Perhaps most contrary to the goals of the PSLRA are our findings regarding courts' current handling of fee requests in the minority of cases (about 15 percent) in which courts cut the requested fee. Our regression analyses show

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[20] It is certainly true that some judges in securities class actions have complained that they find it difficult to set fees *ex post* because they lack data on what an actual client would agree to pay an attorney *ex ante* to litigate a securities class action. *See* Taubenfeld v. AON Corp., 415 F.3d 597, 599 (7th Cir. 2005) ("Although is it impossible to know ex post exactly what terms would have resulted from arm's-length bargaining ex ante, courts must do their best to recreate the market by considering factors such as actual fee contracts that were privately negotiated for similar litigation, information from other cases, and data from class-counsel auctions."); Goldberger v. Integrated Resources, Inc., 209 F.3d 43, 52 (2d Cir. 2000) ("we cannot know precisely what fees common fund plaintiffs in an efficient market for legal services would agree to, given an understanding of the particular case and the ability to engage in collective arm's-length negotiation with counsel."). That problem is less severe in the post-PSLRA period because judges can now look to the fees that public pension funds have negotiated *ex ante*. Indeed, it seems possible that the overall decline in fees since passage of the Act is attributable to the influence the public pension cases may have had on fee setting in other cases. *See* Perino, *supra* note __, at 385-89.

that judicial fee cuts are effectively random events, which we speculate are driven more by judges' predilections and biases than the merits of the fee requests. The unpredictability of fee cuts necessarily creates uncertainty on the part of class counsel, who cannot reliably estimate the returns on effort. This likely discourages lawyers from investing time and resources optimally in class cases, to the detriment of investors who will lose compensation in particular cases and be victimized by frauds too often. Fee-related uncertainty weakens the law's power to discourage wrongdoing.

Taken as a whole our findings suggest that the current system of *ex post* fee setting in securities class actions is deeply flawed. We therefore propose a mechanism that, in our judgment, would both work better and be more consonant with Congress' intent, as expressed in the PSLRA. The cornerstone for our proposal is the belief that attorneys' fees in securities class actions should be set *ex ante*. The lead plaintiff should negotiate a fee when retaining counsel to handle the case. The lead plaintiff should be required to disclose the terms of the negotiated fee agreement to the district court when offering a law firm for appointment as class counsel. The district court should review the negotiated fee terms before appointing class counsel and should approve those terms unless they are clearly unreasonable or not the products of arm's length negotiations. And when reviewing class counsel's request for a fee award at the end of litigation, the district court should apply the agreed and previously approved terms unless unforeseen developments have rendered those terms clearly excessive or unfair. Among the advantages of our proposal are that it respects the PSLRA's preference for private ordering, and it creates superior incentives for attorneys to invest the optimal amount of time and resources in the litigation, thereby maximizing the recovery to the class.

The Article begins in Part II by briefly discussing the lead plaintiff and lead counsel selection mechanisms contained in the PSLRA. Part III sets out the design of our six-year nationwide study and discusses our empirical findings in greater depth. Part IV discusses the normative implications that we think flow from these findings. It also considers several procedural reforms that we believe would make fee-setting in securities class actions more transparent and compatible with the PSLRA by enhancing the flow of information to judges. Part V contains brief concluding remarks.

II. THE PSLRA'S MECHANISMS FOR SELECTING THE LEAD PLAINTIFF AND CLASS COUNSEL AND FOR SETTING ATTORNEYS' FEES

Under the PSLRA, the court chooses the lead plaintiff through a straightforward procedure. The party that is first to file a securities class action provides notice of the lawsuit to all investors by publication in a "widely circulated national business-oriented publication or wire service."[21] Interested investors then have sixty days to file a motion nominating themselves for the position of lead plaintiff.[22] Upon review of the timely submitted applications, the court is to appoint the "most adequate plaintiff" as the lead plaintiff.[23] The PSLRA imposes on the court a presumption that the most adequate plaintiff is the applicant which has "the largest financial interest in the relief sought by the class" and which "otherwise satisfies the requirements of Rule 23 of the Federal Rules of Civil Procedure."[24] The PSLRA further specifies that the lead plaintiff is obligated, "subject to the approval of the court, [to] select and retain counsel to represent the class."[25]

In practice, when an investor files its application to be appointed lead plaintiff it typically has already chosen the law firm that it will recommend that the court appoint as class counsel. Indeed, that chosen law firm usually serves as counsel-of-record for the investor in the process of applying for lead plaintiff status and in requesting that the investor's chosen counsel be appointed counsel for the class.

The PSLRA's mandate that the lead plaintiff "select and retain" counsel to represent the class suggests that a lead plaintiff candidate will *hire* its chosen law firm, including negotiating the terms of its compensation (subject to judicial review). As we have previously written,

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[21] 15 U.S.C. §§ 77z-1(a)(3)(A), 78u-4(a)(3)(A) (2006).

[22] *Id.*

[23] 15 U.S.C. §§ 77z-1(a)(3)(B)(i), 78u-4(a)(3)(B)(i).

[24] 15 U.S.C. §§ 77z-1(a)(3)(B)(iii)(I), 78u-4(a)(3)(B)(iii)(I).

[25] 15 U.S.C. §§ 77z-1(a)(3)(B)(v), 78u-4(a)(3)(B)(v). The statute also explicitly limits the total attorneys' fees and expenses that may be awarded to "a reasonable percentage of the amount of any damages and prejudgment interest actually paid to the class." §§ 77z-1(a)(6), 78u-4(a)(6).

> This assignment of responsibility makes sense because a sophisticated lead plaintiff with a large financial stake in the case and substantial experience in securities litigation should have good information about both the identity of the "right" lawyer for the case and the "right" fee for the lawyer to be paid. To obtain the best combination of quality and price, a plaintiff must evaluate the facts and bargain with attorneys. Sophisticated lead plaintiffs can do both because law firms compete openly for their business. This competitive process enables institutional investors to evaluate lawyers' track records and credentials, assess the "fit" between lawyer and client, compare requested compensation terms, and use the prospect of future business to extract concessions.[26]

The hope and expectation of Professors Elliott Weiss and John Beckerman, who conceived of the lead-plaintiff mechanism, were that institutional investors would apply to be appointed lead plaintiffs and, when given control of class actions, "would act as reasonably diligent litigation monitors, negotiating arm's length fee arrangements with plaintiffs' attorneys and overseeing the prosecution and settlement of the actions in which they were involved."[27] In other words, unlike passive small investors, institutional investors were supposed to be active participants in the litigation. They were expected to drive hard bargains with lawyers competing for the opportunity to earn fees by representing investor classes and to demand zealous representation from the lawyers they retained.

Consistent with above analysis, the Third Circuit requires district court judges to consider fee agreements when appointing lead plaintiffs.[28] The trial judge's job, according to the Third Circuit, is to ensure that the lead plaintiff "fairly and adequately represent[s] the interest of the class."[29] And "one of the best ways" a trial judge can do this is by "inquir[ing] whether [a lead plaintiff candidate] has demonstrated a willingness and ability to select competent class counsel and to negotiate a reasonable retainer agreement with that counsel."[30]

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[26] Baker, Perino & Silver, *supra* note __, at ___.

[27] Weiss, *supra* note ___, at 551. See also Weiss & Beckerman, *supra* note ___, at ___.

[28] *In re* Cendant Corp. Litig., 264 F.3d 201 (3d. Cir. 2001).

[29] *Id.* at 266.

[30] *Id.* at 265. There are a handful of cases outside the Third Circuit that take a similar approach. *See In re* Quintus, 201 F.R.D. 475 (N.D. Cal. 2001) (noting that "the best way for the court to assess a potential lead plaintiff's adequacy is to consider the manner in which he has retained counsel and negotiated an attorney's fee for the class.").

The reported cases, however, suggest that this *ex ante* approach is infrequently employed. Judges outside the Third Circuit rarely examine fee agreements when appointing lead plaintiffs, and even within the Third Circuit many district courts do not seem to do so.[31] Prior to our study, however, there was no systematic, comprehensive information about the extent to which district courts' existing practices comport with Congress's intent in enacting the PSLRA. In brief, there was no systematic information available about: the frequency with which lead plaintiffs negotiate *ex ante* fee agreements with class counsel; the frequency with which courts consider such agreements when appointing lead plaintiffs; the frequency with which class counsel invokes an *ex ante* fee agreement when seeking an award of fees from the court at the end of the litigation; or the frequency with which the court invokes (and enforces the terms of) class counsel's *ex ante* fee agreement with the lead plaintiff when awarding attorneys' fees at the end of the litigation. We also did not know how often or to what extent judges overrule lead plaintiffs when awarding fees. Finally, we did not even know whether, on average, judges or institutional investors with large financial stakes tended to be more parsimonious with regard to attorneys' fees or whether there are systemic differences across courts with respect to fee awards.

Before turning in the next Part to the details of our study, it is worth pausing briefly to illustrate, for those unfamiliar with the process, how fees are

[31] *See* Steamfitters Local 449 Pension Fund v. Cent. European Distribution Corp., No. 11-6247 (JBS/KMW), 2012 U.S. Dist. LEXIS 118693, at *4 (D.N.J. Aug. 22, 2012) (accepting the magistrate judge's recommendation to approve the lead plaintiff's choice of counsel without a discussion of fee arrangements when the motion to appoint counsel was unopposed); Blake Partners, Inc. v. Orbcomm, Inc., No. 07-4517, 2008 U.S. Dist. LEXIS 43061, at *21–26 (D.N.J. June 2, 2008) (noting that the Third Circuit requires courts to consider "whether the movant has demonstrated a willingness and ability to . . . negotiate a reasonable retainer agreement with that counsel" but neglecting to discuss the movant's fee arrangement); *In re* Sterling Fin. Corp. Sec. Class Action, No. 07-2171, 2007 U.S. Dist. LEXIS 93708, at *15–16 (E.D. Pa. Dec. 21, 2007) (determining without describing the fee arrangement that the proposed lead plaintiff "has demonstrated a willingness and ability to select competent class counsel and to negotiate a reasonable retainer agreement with that counsel"); Lowrey v. Toll Bros., No. 07-1513, 2007 U.S. Dist. LEXIS 99501, at *10 (E.D. Pa. June 29, 2007) (appointing lead plaintiff and expressing confidence that it "will endeavor to negotiate a reasonable fee arrangement with counsel"); *In re* Able Labs. Sec. Litig., 425 F. Supp. 2d 562, 573–74 (D.N.J. 2006) (approving the lead plaintiff's choice for counsel when the plaintiff described the negotiated fee arrangement to the court).

typically set in class actions of all types.[32] When submitting a proposed settlement for judicial review, class counsel also submits an application for an award to cover attorneys' fees and litigation costs. More often than not, class counsel requests a percentage of the common fund as fees, and judges calculate fees on this basis.[33] When setting the fee percentage or determining fees on another basis, judges enjoy broad discretion. Federal Rule of Civil Procedure 23(h) and the PSLRA specify only that fee awards be "reasonable."[34]

In the vast majority of cases, plaintiffs' law firms, in order to establish the reasonableness of their fee request, provide information on the number of hours their attorneys worked on the case multiplied by the hourly rates common for attorneys in that district. Indeed, some courts mandate that attorneys provide detailed information on this figure—known as the "lodestar." Lodestar amounts are usually below the fee requested.[35] The multiplier applied to adjust the lodestar amount to the percentage requested is supposed to compensate attorneys for the risks associated with handling the case on a contingency basis. In cases where the multiplier is unusually high (or, theoretically, unusually low), the court has the ability to adjust the percentage award.[36] The literature on the lodestar methodology is vast,[37] and although it has been subject to withering judicial and

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[32] The process described in this paragraph is also employed in many class actions not involving the securities laws. *See, e.g.*, Sullivan v. DB Investments, Inc., 667 F.3d 273, 330 (3d Cir. 2011) (antitrust case); Vizcaino v. Microsoft Corp., 290 F.3d 1043 (9th Cir. 2002) (employee benefits claim); McDaniel, 595 F.3d at 421-22 (civil rights claim).

[33] Boeing Co. v. Van Gemert, 444 U.S. 472 (1980).

[34] Fed. R. Civ. Proc. 23(h) ("In a certified class action, the court may award reasonable attorney's fees and nontaxable costs that are authorized by law or by the parties' agreement."); 15 U.S.C. § 78u-4(a)(6) ("Total attorneys' fees and expenses awarded by the court to counsel for the plaintiff class shall not exceed a reasonable percentage of the amount of any damages and prejudgment interest actually paid to the class.").

[35] In a non-trivial number of cases, however, the lodestar exceeds the fee request. *See, e.g.*, *In re* Heartland Payment Sys., Inc. Customer Data Sec. Breach Litig., 851 F. Supp. 2d 1040, 1088 (S.D. Tex. 2012) ("The record and law support reducing the lodestar by a negative multiplier to avoid a windfall to class counsel, given the value of the settlement obtained.").

[36] We are aware of no instance in which a court declared class counsel's multiplier to be too small and adjusted it upwards.

[37] *See, e.g.*, *Court Awarded Attorney Fees, Report of the Third Circuit Task Force*, 108 F.R.D. 237 (1985).

academic criticism,[38] the approach is still commonly used by courts[39] (and therefore also by class counsel in their fee requests[40]) as a "cross-check" on the reasonableness of the percentage fee requested.

In most cases, this process occurs in a largely non-adversarial setting. Defendants are typically indifferent to fee awards because in a common fund case the fee is deducted from the settlement and therefore simply involves the allocation of an already fixed sum between class counsel and class members.[41] A larger fee costs a defendant no more and a smaller fee saves a defendant no money. The primary challenges to excessive fees are supposed to come from class members, but prior studies show that objections to fee requests are rare.[42]

III. THE DATA ON FEE-SETTING IN SECURITIES CLASS ACTIONS

A. The Sample

Using lists of case names and docket numbers provided by the Stanford Securities Class Action Clearinghouse, we identified every securities class action filed in every federal district court in which the parties announced a settlement

[38] *See Goldberger*, 209 F.3d at 48 (lodestar methodology creates "a temptation for lawyers to run up the number of hours for which they could be paid."); *Court Awarded Attorney Fees,* 108 F.R.D. at 248 (concluding that lodestar methodology "creates a disincentive for the early settlement of cases" because it places a premium on the hours worked). For academic critiques of the lodestar approach, see Charles Silver, *Due Process and the Lodestar Method: You Can't Get There from Here*, 74 TUL. L. REV. 1809 (2000); Charles Silver, *Unloading the Lodestar: Toward a New Fee Award Procedure*, 70 TEXAS L. REV. 865 (1992).

[39] *See, e.g.*, In re AT&T Corp. Sec. Litig., 455 F.3d 160, 164 (3d Cir. 2006). In our sample, 43.36% of the judicial fee orders explicitly reference the percentage method with a lodestar cross-check. Virtually all of the remaining cases used the percentage method alone.

[40] In our data set, 92.16% of the fee applications used the percentage method with a lodestar cross-check. Virtually all of the remaining cases used the percentage method alone

[41] A more adversarial process is likely where the statutory cause of action provides that defendants are liable to compensate plaintiffs for the attorneys' fees they have incurred in successfully pursuing the action in addition to any damages. *See, e.g.*, 15 U.S.C. § 15(a) (successful plaintiffs suing under the Clayton Act are permitted to recover a "reasonable attorney's fee" from defendants); Civil Rights Attorney's Fees Awards Act of 1976, Pub. L. No. 94-559, 90 Stat. 2641 (codified at 42 U.S.C.A. § 1988(b) (providing that court, in its discretion, may allow the prevailing party, other than the United States, a reasonable attorney's fee as part of the costs").

[42] *See* Theodore Eisenberg & Geoffrey P. Miller, *The Role of Opt-Outs and Objectors in Class Action Litigation: Theoretical and Empirical Issues*, 57 VAND. L. REV. 1529 (2004) (finding that the median number of objectors to a securities class action settlement was zero).

from January 1, 2007 through December 31, 2012.[43] We then hand collected comprehensive data for each of these 434 cases by examining the following documents in the court record for each case: (1) all motions for appointment of lead plaintiff and lead counsel, along with all supporting memoranda, affidavits, declarations, and other documents; (2) court orders appointing lead plaintiffs and approving lead counsel; (3) all motions and supporting memoranda, affidavits, declarations, and other documents requesting an award of attorneys' fees; (4) any filed objections to the settlement, including objections to the proposed attorneys' fees; (5) any filed responses to the objections, and any related court orders; (6) court orders granting final approval to the settlement; and (7) court orders awarding attorneys' fees.

In these documents for each case we looked for evidence that the lead plaintiff candidates had negotiated fee agreements with their chosen counsel at the outset of the litigation. We also examined whether judges considered the existence or terms of an *ex ante* fee agreement when appointing the lead plaintiff, approving a lead plaintiff's proposed class counsel, or awarding fees to class counsel at the end of the litigation. We coded the characteristics of the parties that were ultimately chosen as lead plaintiffs. Finally, we looked at the arguments lawyers offered to justify their fee requests, the bases for any objections to the fee request, and the explanations judges gave for their decisions.

B. Empirical Findings

1. Descriptive Statistics

Descriptive statistics for our nationwide data set appear in Tables 1 and 2. We discuss various aspects of these descriptive statistics below.

[43] These cases were filed between October 1998 and August 2011. In some cases, the court's order awarding attorneys' fees and/or granting final approval for a settlement announced during our study period was not filed until 2013. We included these cases in the sample. Some cases with multiple partial settlements had announced settlements that occurred prior to our study period. In order to make the data analysis as complete as possible, we included these earlier partial settlements in the sample as well.

a. The Lead Plaintiff Selection Process

We began the analysis by looking for cases in which proposed lead plaintiffs offered the court proof of the *ex ante* fee agreements they negotiated. Although Congress and the drafters of the lead plaintiff mechanism seemed to anticipate that such agreements would be the norm, we found little evidence that they play a significant role in a court's selection of the lead plaintiff. There were very few cases—just 10.62%—in which the lead plaintiff candidate or the court discussed an *ex ante* agreement during the appointment process.[44] We then looked at whether lawyers vary their approach to obtaining the lead plaintiff position for their clients, such as by referencing an *ex ante* fee agreement in the motion to be appointed lead plaintiff, depending on the frequency with which courts handle securities class actions. We analyze that question in several ways. First, we segmented our sample using an indicator variable (*High Volume*) that was assigned a value of 1 if the case was litigated in one of the three districts that see the largest number of securities class actions—the Central and Northern Districts of California and the Southern District of New York—and a value of 0 otherwise.[45] Overall, lead plaintiff candidates discuss *ex ante* fee negotiations in 10.62% of cases—12.57% of the cases litigated in high volume districts and 9.23% in other districts. Although this difference suggests the possibility that counsel for lead plaintiff candidates use court-specific strategies in the lead plaintiff application process, the difference is not statistically significant.[46]

Next, we looked at judges' experience with securities class actions. Because we have collected data on all settlements during our six-year study period, the frequency with which any individual judge appears in our sample

[44] Of the 386 cases for which we were able to obtain lead plaintiff moving papers, only 41 discussed the presence of an *ex ante* fee agreement. In the remaining 48 settlements, the lead plaintiff moving papers were not available electronically.

[45] We chose these three districts because in our nationwide sample of settlements, these courts collectively accounted for 48.16% of the settlements. The Northern District of California heard the fewest (42 cases) of these three districts, but that was more than twice the number of cases as the next nearest court (the Northern District of Illinois).

[46] Pearson chi-square = 1.107; probability = 0.293.

provides a rough measure of judicial experience with these cases.[47] Our sample contains 247 individual judges; 161 of those judges contributed a single fee decision, but the number of decisions per judge ranged from one to eight. On average, each judge contributed 2.78 decisions to the data set, with a standard deviation of 1.95. Based on these data, we created a variable (*High Volume Judge*) that takes a value of 1 if a judge had four or more fee decisions in our sample and 0 otherwise. Discussion of fee arrangements in the lead plaintiff application process is significantly more frequent in cases handled by high volume judges (14.66%) than in cases handled by other judges (8.89%),[48] suggesting that lawyers may modify their strategy for obtaining lead counsel positions depending on the judge who hears the case.

We also analyzed the relationship between competition for the lead plaintiff position and the frequency with which lead plaintiff candidates discuss *ex ante* fee agreements. Overall, there is a good deal of competition to capture the lead plaintiff position. Nearly 71% of the cases had more than one motion to be appointed lead plaintiff, with a mean (median) of 3.21 (3) motions per case. One case had seventeen (17) different applications for appointment as lead plaintiff. Not surprisingly, the cases with competition turn out to yield significantly larger settlements, suggesting that prospective lead counsel may have the ability to identify the more lucrative or otherwise higher quality cases at the earliest stages of the litigation. Cases with multiple lead plaintiff motions had mean (median) settlements of $62.1 million ($11.7 million), compared to only $26.9 million ($7.5 million) for the cases with only one motion.[49] Competition for the lead plaintiff position is also correlated with a higher frequency of discussion of an *ex ante* fee agreement in the lead plaintiff moving papers. Where there was no competition, fee arrangements were discussed in only 3.77% of the cases, compared to 15.97%

[47] To be sure, this measure is not perfect. It does not account for cases that were dismissed or otherwise terminated prior to a settlement. Nor does it include cases that a judge may have handled prior to our study period.

[48] Pearson chi-square = 2.841; probability = 0.092.

[49] The difference in means is significant at less than 5 percent (t = -2.019; probability = 0.044).

of the cases with competition.[50] We found no evidence that competition for the role of lead plaintiff is more frequent in high volume districts.

While evidence of *ex ante* fee agreements in the moving papers was sparse, we found even less evidence that judges actually considered *ex ante* fee agreements when awarding the lead counsel position. In only 5.19% of the cases did the court's order appointing the lead plaintiff and class counsel make any mention of such an agreement. There were no significant differences between high and low volume districts, but high volume judges were twice as likely (7.41% to 3.68%) as other judges to mention *ex ante* agreements in their selection decisions.[51] Judges are much more likely to focus on fee arrangements when the lawyers have raised them, but discussion in the moving papers is by no means a guarantee that courts will address fees when appointing the lead plaintiff. Nearly thirty percent of the orders appointing lead plaintiff (29.27%) mentioned fee arrangements in cases where fees were discussed in the lead plaintiff motion papers compared to only 1.47% of fee orders in the remaining sample.[52] Thus, in the vast majority of cases, courts seemingly did not consider the presence of a negotiated fee arrangement to be pertinent to the lead plaintiff and lead counsel appointment decisions. We speculate that this result may be the product of the PSLRA, which explicitly makes the size of the lead plaintiff's stake in the case the overwhelming consideration for the court when appointing the lead plaintiff.[53]

While the courts in only a few cases discussed such *ex ante* fee agreements,[54] those that did emphasized that the presence of such an agreement is relevant, either with respect to whether the lead plaintiff satisfies the adequacy prong of Rule 23 or to whether the court should approve lead plaintiff's proposed lead counsel. For example, the judge in *Taubenfeld v. Career Education*

[50] While this difference is statistically significant (Pearson chi square = 8.326; probability = 0.004), it is worth emphasizing that this finding does not imply that increased competition causes lawyers to compete on price. After all, the presence of multiple lead plaintiff applications increases the likelihood that at least one of those applications will mention fees.

[51] This difference in frequencies is significant, but only at the 10% level.

[52] This difference is significant (Pearson chi square = 66.322; probability < 0.001),

[53] *See* 15 U.S.C. §§ 77z-1(a)(3)(B)(iii)(I), 78u-4(a)(3)(B)(iii)(I).

[54] *See infra* notes __ through __ and accompanying text.

Corporation[55] appointed the candidate with the largest financial interest as lead plaintiff, but noted that the plaintiff's moving papers did not discuss the proposed fee structure. As this was "significant information that the court would like to review prior to making a determination on lead counsel," the court reserved its decision appointing lead counsel until the law firm submitted the requested fee information.[56] Unfortunately, there are too few instances of this kind of judicial demand for additional information in our data set to determine whether they are correlated with lower fee requests or awards. The simple fact is that most courts, perhaps because of time or other constraints, appear to be indifferent to such evidence when they make their lead plaintiff selections.

b. Fee Requests and Awards

We found that *ex ante* fee agreements are more frequently invoked when the lead counsel applies for a fee award than when they seek appointment as lead counsel. Overall, in 17.54% of the cases, lead counsel argued that the presence of a negotiated *ex ante* agreement with the lead plaintiff justified its requested fee.[57] The frequency of this argument was virtually identical in the high volume versus the low volume districts (17.82% versus 17.27%), but lead counsel was significantly more likely to make this argument in front of a high volume judge (22.31%) than a low volume judge (15.41%). Consistent with the view that sophisticated institutional investors would make the best monitors of class counsel, evidence in the record of an *ex ante* fee agreement is most prevalent when a public pension fund is the lead plaintiff. Evidence of such an agreement was present in 26.21% of the cases with public pension lead plaintiffs compared to just 12.30% of cases with other lead plaintiff types. This difference was significant.[58]

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[55] 03-CV-884 (N.D. Ill. March 19, 2004); *see also* In re Motorola Sec. Litig., 2003 WL 21673928, at *7 (N.D. Ill. July 16, 2003) (appoint lead counsel where proposed fees did "not appear unreasonable"); Johnson v. Tellabs, Inc., 214 F.R.D. 225, 229 (N.D. Ill. 2002) (approving proposed lead counsel because the proposed fees did not appear unreasonable).

[56] *Taubenfeld*, at 10-11; *see also* Mayo v. Apropos Tech., Inc., 2002 WL 193393, at *5-6 (N.D. Ill. Feb. 7, 2002) (requesting potential lead plaintiff to submit information on, among other things, the "agreed fees").

[57] That is, 74 of 422 cases.

[58] The Pearson chi-square statistic was 11.487 (probability = 0.001).

Somewhat more frequently (specifically in 34.68% of the cases), attorneys noted in their fee request filings that the lead plaintiff supported the requested fee, often without any discussion of whether that support was premised on an *ex ante* fee agreement. In many cases, the lead plaintiff's support came solely as a result of an *ex post* evaluation of the fairness of the fee. In such a case, the lead plaintiff or its representative would typically file a supporting declaration indicating that it thought the requested fee was fair based on the work performed and the result achieved.[59]

It is possible that the variables in our regressions (discussed below) for *ex ante* fee agreements and public pension plaintiffs might not be measuring separate effects. Plaintiffs' attorneys told us in informal interviews that, in their experience, some form of *ex ante* fee agreement is present in virtually all cases with public pension funds.[60] For that reason, we have speculated that these variables may be "measuring some variation of the same thing—the impact that a sophisticated and engaged lead plaintiff has on fee requests."[61]

Some evidence from our current, nationwide study, however, is at odds with that anecdotal evidence. In cases with both public pension lead plaintiffs and evidence of an *ex ante* fee agreement, the average fee request is 13.76%. By contrast, in cases with a public pension lead plaintiff but no evidence of an *ex ante* fee agreement, requests are significantly higher, averaging 22.19%.[62] These data suggest that fee agreements negotiated at the beginning of cases have a substantial moderating effect on fee requests, even when cases are under the control of sophisticated institutional investors. To put the matter another way, public pension funds may come in two types—those that act aggressively to reduce agency costs and those that do not—and the presence of an *ex ante* fee agreement may help distinguish one from the other. Relatedly, the absence of an *ex ante* agreement may also correlate with instances of pay-to-play, a practice known to

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[59] See, e.g., [cites to specific declarations].

[60] Baker, Perino & Silver, *supra* note __, at 1694, 1701.

[61] *Id.* at 1701.

[62] The t statistic for the means comparison test is 6.4803 (probability < 0.0001).

weaken the enthusiasm of public pension funds for bargaining hard with attorneys over fees.[63]

Overall, the mean (median) fee request in our sample of cases is 24.62% (25.00%). In cases without *ex ante* agreements, overall fee requests are 25.92% compared to 18.29% in cases with evidence of *ex ante* agreements. These differences are significant.[64] The same pattern exists with respect to fee awards. In cases without an *ex ante* agreement, fee awards averaged 24.94% compared to 17.92% in cases with evidence of an *ex ante* agreement.[65] Of course, these simple comparisons cannot tell us whether it is the presence of an *ex ante* fee agreement that is driving this result. Inflation-adjusted settlements, for example, are significantly larger in the cases with *ex ante* agreements ($137 million) than in the cases without such agreements ($34.4 million). Fee requests and awards measured as a percentage of settlement tend to decline as settlement size increases, so it is possible that the difference in the size of the settlements explains the difference in fees.

To get a better sense of how settlement size and the presence of an *ex ante* fee agreement might be correlated with fee requests and awards, Figure 1 depicts fee requests and awards as a percentage of the settlement. Figure 1 shows that the majority of fee requests are clumped into one of three values—25%, 30%, or 33.33%. A 25% fee request is the mode for the sample (occurring in 26.93% of the cases), a not terribly surprising result given the number of courts, particularly in the Ninth Circuit, that explicitly use 25% as a benchmark for awarding fees.[66] The vast majority (73.97%) of fee requests in cases with *ex ante* agreements, however, are below 25%. The slopes for the predicted values in cases with and without agreements are close to parallel, which suggests that the effect of an *ex ante* fee agreement does not vary with the settlement size.

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[63] Stephen J. Choi, Drew T. Johnson-Skinner & A. C. Pritchard, *The Price of Pay to Play in Securities Class Actions*, 8 J. EMPIRICAL LEGAL STUD. 650 (2011).

[64] The t statistic for the means comparison test is 9.1212 ($p < 0.0001$).

[65] Here, too, the differences are significant. The t statistic for the means comparison test is 8.1315 ($p < 0.0001$).

[66] *See, e.g.*, Hanlon v. Chrysler Corp., 150 F.3d 1011, 1029 (9th Cir. 1998); Camden I Condominium Ass'n, Inc. v. Dunkle, 946 F.2d 768 (11th Cir. 1991).

There is substantial evidence that the court's familiarity with securities class actions makes a difference not only with respect to fee awards, but also with respect to fee requests. Experience, in other words, matters both in terms of what lawyers ask for and what courts give them. These differences become particularly pronounced if we look jointly at both judicial experience and settlement size. As settlement size increases, lawyers ask for and are awarded significantly larger fees in those districts that see fewer securities class actions. Fee requests averaged 26.21% in the low volume districts compared to just 22.90% in the high volume districts.[67] Overall, fee awards were significantly higher (25.67%) in the low volume districts than in the high volume ones (21.79%).[68] In the top quartile of settlements in our nationwide study, average fee requests in the low volume districts were 23.03% compared to 18.18% in the high volume districts.[69] Fee awards for those cases average 22.58% in the low volume districts versus 17.68% in the high volume districts. These differences are also significant.[70]

Figure 2 provides a starker illustration of how fee request practices vary between high and low volume districts. To understand the significance of these results, it is important to emphasize that one of the most robust findings of existing empirical research is that awards of attorneys' fees exhibit scale effects—as settlement size increases, fee percentages decline.[71] Until now, most commentators simply assumed that these scale effects were uniform across districts and judges. But as Figure 2 illustrates, that is simply not the case. Fee requests and awards are again shown as a percentage of the settlement. In low volume districts, Figure 2 shows that, on average, fee requests are less sensitive to settlement size, with requests declining only slightly as settlements increase. There are, to be sure, some low fee requests (defined as requests below 20%) in the low volume districts, but those cases overwhelmingly have either a public pension lead plaintiff (71.43% of the cases) or evidence of an *ex ante* fee

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[67] The t statistic for the means comparison test is 4.9428 (probability < .0001).

[68] The t statistic for the means comparison test is 5.7984 (probability < .0001).

[69] The t statistic for the means comparison test is 3.739 (probability = 0.0003).

[70] The t statistic for the means comparison test is 3.788 (probability = 0.0003).

[71] *See, e.g.*, Fitzpatrick, *supra* note __, at ___; Eisenberg and Miller, *supra* note __, at ___; Perino, *supra* note __, at 388. This proposition is also generally accepted by courts. *See* Silverman v. Motorola Solutions, Inc., 739 F.3d 956, 959 (7th Cir. 2013) (noting that "negotiated fee agreements regularly provide for a recovery that increases at a decreasing rate.").

agreement (53.58% of the cases). In low volume districts, there were 130 cases that had neither a public pension fund lead plaintiff nor evidence of an *ex ante* fee agreement. Only five of those cases (3.85%) had fee requests below 20 percent.

By contrast, in high volume districts, the downward slope of the fitted values line is steeper. In these districts, lawyers ask for substantially lower percentage fees as settlement size increases than in the low volume districts. Again, however, these simple comparisons of means cannot tell one whether this effect is really associated with the *volume* of securities cases settled in the high volume districts or is instead the result of the *kinds* of securities cases that are brought in those districts. For example, it remains possible that sophisticated lead plaintiffs and *ex ante* fee agreements are driving this result. Two-thirds of the cases in high volume districts with fee requests below 20% involved public pension lead plaintiffs. More than 44% of such cases had evidence of an *ex ante* fee agreement.

We see a similar pattern when we compare high volume judges to low volume judges (Figure 3). In both sub-samples, there are scale effects, but the rate of decline is much sharper for both requests and awards when a high volume judge hears the case. Here too, we need to exercise care because other case characteristics could be driving these results. Nonetheless, the picture that is beginning to emerge is one that is far more nuanced than indicated in previous studies. In a result that should be surprising to no one, it appears that lawyers behave strategically based on where they are and who they are appearing before. We have certainly known for years that courts[72] and judges are not monolithic when it comes to their fee awards. Some judges have earned reputations for vigorously scrutinizing fee requests and for awarding relatively low fees.[73] What is new, however, is that we cannot chalk up those differences solely to the idiosyncrasies of individual judges (although as we note below in our discussion of fee cuts, we continue to believe these personal characteristics remain important in understanding the fee-setting process). The more experience courts or judges

[72] *See* Eisenberg, Miller and Perino, *supra* note __, at ___ (identifying significant inter-circuit variation in fee award practices); Helland and Klick, *supra* note __, at ___ (attributing differences in fees to differences in court congestion).

[73] *See In re* HPL Technologies, Inc. Sec. Litig., 366 F. Supp. 2d 912 (N.D. Cal. 2005) (Walker, J.).

have with securities class actions, the more parsimonious they appear to become. But the phenomena we observe are not simply the product of experienced courts or judges slashing fee requests more than their less experienced counterparts (a point we address in more detail below). Lawyers appear to be anticipating what the court is likely to do, asking for lower fees (particularly as cases get larger) when they appear in courts with large numbers of class actions or before high frequency judges and asking for higher fees in other situations.

The fee request-award dynamic thus appears to be a complex version of the Ultimatum Game, a classic of behavioral economics in which two players decide how to divide a fixed sum of money. In the standard form of the game, the Proposer is asked to allocate a sum of money between herself and the other player, the Responder. The Responder may either accept the offer (in which case the money is split as proposed) or reject it. In the latter case, neither player receives anything.[74] Under the traditional assumptions of classical economics, the Proposer should offer the Responder the smallest sum of money possible and the Responder should accept it because she will be better off than with the alternative (which is nothing). But repeated experiments have shown that Responders tend to reject offers that are too far outside what might be considered the objectively fair outcome, an even split. In the majority of studies, offers tend to average between 40 to 50 percent of the fixed total sum, with responders usually rejecting offers below 30 percent.[75] Proposers, in other words, appear to anticipate these reactions and so tend to offer divisions that fall within the likely acceptable range.[76]

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[74] *See* Christine Jolls, Cass Sunstein & Richard Thaler, *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471, 1489-90 (1998); Richard H. Thaler, *The Ultimatum Game*, 2 J. ECON. PERSPECTIVES 195, 195-96 (1988).

[75] Ernst Fehr & Klaus M. Schmidt, *A Theory of Fairness, Competition & Cooperation in* ADVANCES IN BEHAVIORAL ECONOMICS (Colin F. Camerer, et al., eds.) 271, 277 (2004); Ernst Fehr & Simon Gächter, *Fairness and Retaliation: The Economics of Reciprocity in* ADVANCES IN BEHAVIORAL ECONOMICS, *supra*, 510, 512.

[76] Jolls, Sunstein & Thaler, *supra* note __, at 1490-97. The reason why Proposers make offers larger than what would be predicted under the classic economic model remains something of a mystery. They might "have a taste for fairness' or they might simply be acting strategically to avoid the possibility that low offers will be rejected. Thaler, *supra* note __, at 197; Richard A. Posner, *Rational Choice, Behavioral Economics, and the Law*, 50 STAN. L. REV. 1551, 1564-65 (1998). We suspect that the latter explanation is the better one.

An attorney's decision about what fee to request in a class action shares some basic characteristics with the Ultimatum Game.[77] There are two key differences. The first is that in the absence of an *ex ante* fee agreement the court rather than the lead plaintiff will play the role of the Responder, although in doing so it is supposed to be acting in the best interests of the class.[78] The second is that the court has the final decision about how the pot will be split. But the existence of an accepted range of fair values—in this case the existing precedents regarding fee awards—will tend to constrain the attorney's decision about what fee to propose. Indeed, in variations on the Ultimatum Game in which Proposers have information about which offers have been accepted in the past, offers tend to converge toward those demonstrably acceptable values.[79] Rather than run the risk that a court will respond to a high demand by awarding an especially low fee, lawyers appear to make proposals that are within a range of values deemed to be fair, given the precedents in the relevant jurisdiction. The difference between high volume and low volume districts is that in the former there are likely to be more precedents and a tighter range of "fair values," which constrain class counsel's ability to request as much as might be wanted. In low volume districts and with judges who handle these cases infrequently, there are fewer precedents, allowing attorneys to pitch their requests at the higher end of the perceived "fair value" range. In layman's terms, lawyers ask for as much as they think they can reasonably get, but what they think they can get will vary depending on where and before whom a case is pending.

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[77] For a discussion of the application of the Ultimatum Game to contingent fees more generally, see Eyal Zamir & Ilana Ritov, *Notions of Fairness and Contingent Fees*, 74 L. & CONTEMP. PROBS. 1, 9-10 (2011).

[78] In the Ultimatum Game, the Responder bears a cost for rejecting the proposed allocation because she gets nothing under those circumstances. The judge can also be thought to bear a cost when it rejects a fee request because it will now have to write an opinion explaining why the proposed fee was unreasonable. The willingness to accept such costs is important for judges in high volume districts because it will allow them to develop a reputation for accepting only fair fee requests. *See* Martin A. Nowak, Karen M. Page & Karl Sigmund, *Fairness Versus Reason in the Ultimatum Game*, 289 Science 1773, 1774 (2000) ("individuals who accept low offers run the risk of receiving reduced offers in the future" whereas "the costly act of rejecting a low offer buys the reputation that one accepts only fair offers.").

[79] *See id.* at 1774 (where information on past offers is available and the game is repeated "evolutionary dynamics tend to favor strategies that demand and offer a fair share of the prize.").

This dynamic changes when a sophisticated institutional investor serves as the lead plaintiff. Particularly where that lead plaintiff negotiates fee terms *ex ante* with retained counsel, the lead plaintiff has the ability to engage in real arm's-length negotiations, rather than simply responding to the lawyer's fee proposal. As we discuss in Part IV, there are substantial reasons to believe that, given the dynamics and uncertainties inherent in class action litigation, sophisticated lead plaintiffs who negotiate fees with their counsel at the start of the case are better suited to setting fees appropriately—that is, to paying the "market rate"—than are judges who simply respond to fee requests after the substantive aspects of the case are complete.

c. Judicial Fee Reductions

If we anticipate that lawyers will moderate their fee requests when they appear in high volume districts or before high volume judges, then it is difficult to predict the frequency with which different courts will cut requested fees. On one level, fee cuts might in general be quite infrequent. This would be so if lawyers accurately anticipate the amounts judges are willing to award and tailor their fee requests accordingly. One might also expect fee cuts to be less frequent among experienced judges and in experienced courts because lawyers' predictions will be better informed. Alternatively, because a low volume court has comparatively little basis for comparison when presented with a given fee request, it might be inclined to find reasonable a fee request that a high volume court would consider "high" or "too high." As we noted previously, fee requests are typically non-adversarial. Defendants are indifferent to fee awards because they are paid out of the common fund and objectors tend to be infrequent. As a result, lawyers requesting fees have little reason not to skew their briefs toward the higher end of the range of perceived "fair values." Under these circumstances, a court that sees securities class actions infrequently might cut fees only rarely.

As it turns out, fee cut decisions do present something of a mixed bag. In 14.62% of cases, the court awarded a smaller fee than lead counsel requested.[80] Put another way, in six out of seven cases, plaintiffs' counsel received precisely the fee requested. From this perspective courts seem to take a light touch, but that

[80] That is, in 62 of the 424 cases for which the documents were available online.

conclusion needs to be placed in context. When Congress created the PSLRA, it gave the lead plaintiff primary responsibility for fees, with the courts providing a protective backstop against excessive compensation. Given the role assigned to lead plaintiffs, and the fact that fee requests are always made with their (explicit or implicit) support, the 15% fee cut rate provides striking evidence that the PSLRA is not working as intended. Judges are far more active than one might have expected them to be. Moreover, their aggressiveness often comes from within. In only 19 of the 62 cases in which fees were reduced (30.65% percent) did an objector formally challenge the size of the requested fee.[81] Thus, in seven out of ten cases in which the court cut the requested attorneys' fees, the court did so *sua sponte*, without the lead plaintiff or any other class member questioning the size of the fee request.

Indeed, the willingness of judges to cut fees appears to be unrelated to actual objections from class members to proposed fees. If we measure the ratio of award to request, we find that for the overall sample the mean (median) is 0.9676 (1.000). On average, lawyers could expect to get 97 cents on the dollar in fee awards, or 100 cents if we rely on the median. In the subset of cases where the court cut fees, the ratio of award to request is actually higher when there is an objection to the fee request (0.8035) than when there is no objection (0.7711), although the difference is not statistically significant. The requested fees in the 62 fee cut cases ranged from 6.54% to 33.33%, with the fee awards ranging from 6.29% to 30.0%. The mean (median) ratio of award to request in these cases was 0.7810 (0.7900), with a range from 0.2533 to 0.9908.

Our data also provide mixed evidence about the deference that courts show to large institutional lead plaintiffs. Based simply on broad descriptive statistics, we found that fee cuts were neither more prevalent when an individual was the lead plaintiff in the case nor less prevalent when a public pension fund was the lead plaintiff, two relationships that might be expected given that the PSLRA encourages courts to defer to institutional investors. Individuals were lead plaintiffs in 46.40% of the settlements and accounted for 43.54% of the cases with

[81] The objection rate was, to be sure, higher in the cases where the court cut the requested fee. Overall, objections occurred in only 21.93% of the cases we examined. But the difference between the frequency of objections between the cases where the court cur requested fees and they cases where it did not was insignificant (Pearson chi-square statistic was 2.660, probability = 0.103).

fee cuts.[82] Cases with public pension fund lead plaintiffs were not significantly less likely to have fee cuts than cases with other kinds of lead plaintiffs.[83] We did find, however, some relationship between the type of lead plaintiff and the *size* of the fee cut. The mean ratio of award to request is significantly higher in cases with a public pension lead plaintiff (0.9811) than in cases with other lead plaintiff types (0.9607),[84] indicating that courts cut fees less in cases with public pension funds.

We also found limited evidence, again based on simple frequency comparisons, that courts show greater deference to fee requests that were the product of *ex ante* fee agreements. Judges did not award the requested fee in about 8 percent of the settlements with *ex ante* fee agreements compared to about 16 percent of the cases without such agreements. Although fee cuts were twice as likely in cases without *ex ante* agreements, the difference in frequencies was not statistically significant. Within the fee cut cases, there was virtually no difference in the ratio of award to request for cases with *ex ante* fee agreements (0.7927) and those without (0.7726). The same was true across the entire sample. Overall, lawyers were awarded 98.30% of their requested fees in cases with *ex ante* fee agreements compared to 96.41% in cases without such agreements. Nor is there evidence that the lead plaintiff's expressed support of the requested fee made a difference in the likelihood of a judicial fee cut. Cuts were about as likely in the cases with such support (12.5%) as in those without it (15.33%).[85]

As in the other aspects we have examined, however, there is some evidence of inter-court and inter-judge variations. High volume districts appear to scrutinize fee requests somewhat more vigorously than low volume districts. To be sure, the overall level of judicial scrutiny remains quite low. The average ratio of award to request in high volume districts (0.9575) is significantly lower than in low volume districts (0.9787).[86] Most striking is the fact that fee cuts are almost

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[82] The other lead plaintiffs in these fee-cut cases were public pension funds (25.81%) and other institutions, including union funds and private institutions (30.64%).

[83] The chi-square statistic was 2.1537 (probability = 0.142).

[84] The t statistic is -2.0948 (probability = 0.0368).

[85] These slight differences were not statistically significant (Pearson chi-square = 0.6143; probability = 0.433).

[86] The t statistic for the means comparison test is 2.5137 (probability = 0.0123).

twice as likely in the high volume districts (occurring in 19.12% of cases) as in the low volume districts (10.45%).[87] A similar pattern emerges for the judges who most frequently rule on fee requests. Fee cuts are significantly more likely among high volume judges (19.08%) than among low volume judges (12.63%). High volume judges also have significantly lower ratios of award to request (0.9573) than low volume judges (0.9722), although, on average, neither group reduces fees by very much. Indeed, in the sub-sample of cases with fee cuts, there are no significant differences in the *size* of cuts among high volume and low volume districts or among judges who see these cases more or less frequently.

There does appear to be some difference, however, between the deference that high volume judges give to *ex ante* fee agreements compared to their low volume counterparts. In only one of 27 cases (3.70%) in which a high volume judge was evaluating a fee request that was the product of an *ex ante* agreement did that judge reduce the requested fee. By comparison, low volume judges reduced requested fees in five of 45 cases with *ex ante* fee agreements (11.11%). Although the numbers are too small to demonstrate statistical significance, they suggest the possibility that judges who see more securities class actions may defer more readily to negotiated fee agreements.

Finally, we examined the rationales courts offered for their decisions to reduce the requested fees. Given that fee awards raise significant policy concerns regarding the structure of the civil litigation system and its deterrent effects, and given the importance of fee awards to lawyers and class members, one might hope that judges would give some explanation for their decisions to cut the requested fees. That is simply not the case. In one-third (21) of the fee-reduction cases, the court gave no reason or justification at all for its decision to cut the fee. In the remaining cases, the court gave one or more reasons for the fee reduction, which are summarized in Table 3. For the most part, judges offered only the most cursory explanations for their decisions. In 40.32% of the cases, courts simply expressed the opinion that the requested fee was "too large," with no explanation whatsoever about why. Although courts often offered other explanations, such as the low risk the case entailed, the quality or excessive quantity of the work performed by the attorneys, in most cases these discussions were cursory at best.

[87] Pearson chi-square = 6.3630; p = 0.012).

The typical decision was an unpublished order only a few pages in length. While hardly adequate, these decisions were often an improvement over the cases in which the court awarded the requested fee without any reduction. In many of those cases, courts simply signed a conclusory proposed order that class counsel had submitted with its fee application. In those cases, it is difficult to avoid the inference that the court simply rubber-stamped the requested fee with little if any independent evaluation or analysis.

Courts' unwillingness or inability to explain why they award the fees they do leave important questions unanswered. Are fee awards random or is there a pattern to the data? What factors do courts really consider in determining whether a fee request is reasonable? Do courts actually apply the factors they claim to consider? Are there systematic differences among courts or among judges in awarding fees? Do lawyers know about these differences and exploit them in their fee requests? What, if any role do *ex ante* fee agreements play in fee awards? What factors explain judicial decisions to cut requested fees? We now examine these questions in greater depth.

2. Regression Analyses

To better understand how *ex ante* fee agreements, the participation of public pension funds, and judicial experience with securities class actions are correlated with fee requests and awards, we constructed a series of linear regressions with either the fee request or the fee award as the dependent variable. We included indicator variables for: (1) evidence of an *ex ante* fee agreement (*Ex Ante*); (2) whether there was competition for the lead plaintiff position (*Competition*); (3) the presence of a public pension fund (*Public Pension*) or other institutional investor (*Other Institution*) as lead plaintiff; (4) the age of the case in years from filing until the date the court awarded attorneys' fees (*Case Age*); (5) whether the case was litigated in a high volume district for securities class actions (*High Volume*); and (6) whether the case was litigated in front of a high volume judge (*High Volume Judge*). As an alternative way of measuring judicial experience with securities class actions, we created an additional variable (*Judge Frequency*) which measures the actual number of fee decisions a judge has in our data set. In our regressions for fee awards, we also included indicator variables for: (1) whether an objection to the fee was filed (*Fee Objection*), and (2) whether the court cut the requested fee (*Cut*). All models include as an independent

variable the log-transformed, inflation-adjusted settlement in the case. To give a clear sense of the magnitude of the effects these variables have, we centered the regressions at the mean settlement size in the database ($51.8 million).[88]

To analyze the circumstances in which courts reduce the requested fee, we also constructed a logit model which takes *Cut* as a dependent variable. This regression employs independent variables that are largely observable by case participants when the fee request is made. The use of these variables enables us to determine whether class counsel can make reliable predictions as to when fee cuts are likely. To a large extent, the variables are the same ones we use in our regressions for fee awards and requests.

a. Fee Requests

Model 1 in Table 4 shows that, even controlling for other relevant variables, the effect of an *ex ante* fee agreement on a fee request is negative and significant, both statistically and economically. At the mean settlement value, the average fee request in a case without an *ex ante* agreement is 30.7% (or $15.9 million). By contrast, the mean fee request in cases with an *ex ante* agreement was 25.0% (or $12.95 million), a 19% reduction in the fee requested. The presence of a public pension fund has similar effects. Cases with public pension fund lead plaintiffs have fee requests that average 25.9%, a reduction of about $2.5 million at the mean settlement amount. Other types of lead plaintiffs, including union-affiliated pension funds and other kinds of private institutional investors, have no statistically significant correlation with fee requests, a result that is consistent with prior studies.[89]

Competition for the lead plaintiff position is also correlated with lower fee requests, although the effect is smaller than for either *ex ante* fee agreements or the presence of a public pension fund. On average, the fee requests in cases with such competition decline from 30.7% to 29.3%. Competition seems not to influence fee award size directly, however, because compensation terms do not

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[88] To account for potential variation among circuits, the regressions we report here use robust standard errors, clustered by circuit. *See* Michael Perino, *Institutional Activism through Litigation: An Empirical Analysis of Public Pension Fund Participation in Securities Class Actions*, 9 J. EMPIRICAL LEG. STUD. 368, 389 (2012) (using a similar methodology).

[89] *See* Perino, *supra* note __, at 389.

influence judges' decisions to appoint lead plaintiffs. Instead, competition may be a proxy for case quality. Higher quality encourages lawyers to seek control of class actions because it implies lower risk, and it induces them to compete on price for the same reason.[90]

Perhaps the most significant finding in Model 1 is that plaintiffs' attorneys appear to adjust their fee requests based on the volume of securities class actions settled in the district court where a case is pending. The variable *High Volume* is negative and significant. All else being equal, fee requests in the Northern and Central Districts of California and in the Southern District of New York (which collectively see roughly half of all securities class actions) are, on average, 2.8% lower than requests in other districts. At the mean settlement value, the lead counsel in a case in a high volume district asks for about $1.45 million less in fees than in a case filed in a low volume district.[91]

To further examine this relationship, Model 2 includes two interactions—(1) between *Mean Settlement* and *High Volume* and (2) between *Ex Ante* and *Public Pension*—in order to test the combined effects of those variables on fee

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[90] Model 1 also suggests that the age of the case has a minor impact on the fee request, but not in the predicted direction. Although one might expect the requested fee to be higher in cases that take longer, *Case Age* is actually negatively correlated with fee requests. For every additional year the case is litigated, the fee request declines by 0.3%. This association, however, is only significant at the 10 percent level.

[91] In an unreported model, we replaced the *High Volume* variable with indicator variables for each circuit, with the Second Circuit as the reference circuit. The results are consistent with the analysis in Model 1. In eight of the remaining eleven circuits, fee requests were higher than in the Second Circuit. In five of those cases (the Third, Fourth, Eighth, Tenth, and D.C. Circuits) those differences were significant. For the most part, these are the circuits that see the fewest securities class actions. *See* Stanford Securities Class Action Clearinghouse, http://securities.stanford.edu/circuits.html (last visited Jan. 29, 2015) (reporting that since 1996, the Fourth, Eighth, Tenth, and D.C. Circuits have the lowest levels of securities class action filings).

The only circuits with significantly lower fee requests were the Seventh (1.5% lower fee requests on average) and the Ninth Circuit (1.8% lower). Again, these results are largely consistent with our *High Volume* variable. Two of the three districts we defined as high volume districts were within the Ninth Circuit. While the Seventh Circuit does not see a large number of class actions, it has developed a reputation for scrutinizing closely fee requests in other types of class actions. *See In re* Synthroid Marketing Litig., 325 F.3d 974, 975 (7th Cir.2003); *In re* Synthroid Marketing Litig., 264 F.3d 712 (7th Cir. 2001); *In re* Continental Illinois Sec. Litig., 962 F.2d 566 (7th Cir. 1992). It also contains the district court (the Northern District of Illinois) that saw the fourth largest number of securities class action settlements in our sample.

requests. With these interactions, the constant in Model 2 (0.307) represents the average fee request in a case litigated in a low volume district without either an *ex ante* fee agreement or a public pension lead plaintiff.[92] As noted previously, one of the most consistent results in studies of attorneys' fees in class actions generally is that settlement size is strongly correlated with fee requests and awards. As settlements increase, fee requests (measured as a percentage of the settlement) have been found to decrease.[93] The overwhelming empirical support for this proposition makes one result in Model 2 particularly notable. With an interaction term between settlement size and high volume districts, the variable *Mean Settlement* is now negative but insignificant. What does this result mean? In districts that see few securities class actions, fee requests do not appear to vary significantly with the size of the settlement. In other words, regardless of settlement size, when a lead counsel in a low volume district is not constrained by either a negotiated *ex ante* fee agreement or an active public pension lead plaintiff, the counsel requests fees of around 30% of the settlement.

By contrast, in high volume districts fee requests are significantly lower, averaging 27.9% at the mean settlement value, about a $1.45 million reduction in the requested fee. It is important to emphasize that this reduction in fee requests occurs even in the absence of a public pension fund lead plaintiff or an *ex ante* fee agreement, suggesting that it is the court with relatively greater experience handling securities class actions that is providing this moderating influence. This finding substantially modifies the existing understanding of the relationship between fee requests and settlement size in class action settlements. Previously, most scholars have concluded that class action fee requests declined uniformly across courts as settlement size increased.[94] But the results here suggest both imperfect information (by courts and plaintiffs) in the market for fees and plaintiffs' attorneys who seemingly seek to exploit that information asymmetry.[95]

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[92] The 95% confidence interval for the constant is 0.2916 to 0.3233.

[93] *See* Eisenberg & Miller, *supra* note __, at ___; Perino, *supra* note __, at 389; Fitzpatrick, *supra* note __, at ___.

[94] *Id.*

[95] One could construe this finding as evidence of a bifurcated or stratified market for class action attorneys, rather than as imperfect information by courts, if there were market-based reasons for the same law firm to charge a different percentage of the recovery when prosecuting a class action in one district court rather than another. But we are aware of no such justifications.

The decline in fee requests associated with increasingly large settlements is driven entirely by the requests made to the subset of courts that see these cases most frequently. Outside of that handful of districts, lawyers ask for uniform fees, regardless of settlement size.

How big is the difference in fee requests in high versus low volume districts when the settlements involved are substantially larger than average? This relationship can be seen in the interaction between *Settlement* and *High Volume*, which we found to be negative and significant. This result indicates that as settlement values increase the distance between fee requests in low versus high volume districts continues to widen. To understand the magnitude of this effect, consider a one-standard-deviation increase in the size of the settlement, which would mean a settlement of approximately $216.8 million. In the absence of either a public pension lead plaintiff or an *ex ante* fee agreement, the average fee request in a low volume district is 30.06%, virtually unchanged from the fee request for an average settlement. In the same case in a high volume district, the average fee request is only 26.01%. At these averages, class counsel could be expected to ask for fees of nearly $10 million more in the case litigated in the low volume district. These differences suggest substantial, previously undocumented inefficiencies in the market for attorneys' fees in securities class actions. Lawyers, who naturally act in accordance with their own financial best interests, appear to be aware of these inefficiencies and strategically adjust their fee requests to take advantage of them.

The question that naturally arises concerns the mechanism though which high volume courts can have this moderating influence on fee requests. What prevents an attorney (at least in the absence of an *ex ante* fee agreement or a sophisticated public pension fund) from asking for the same fees in both high volume and low volume districts? One obvious way courts might influence fee requests is through their fee award precedents. For example, the Ninth Circuit explicitly uses a benchmark fee of 25% in securities class actions,[96] a percentage that is similar to the nationwide average fee request we report. A benchmark, of course, works uniformly, regardless of settlement size, but precedents need not be so precise to have a moderating influence on fee requests. The Second Circuit, for

[96] *See* Hanlon v. Chrysler Corp., 150 F.3d 1011, 1029 (9th Cir. 1998).

example, does not explicitly use such a benchmark, but in numerous cases district courts there have awarded fees that are substantially below 25% and the Court of Appeals has suggested that fees in securities cases are too high.[97] As we indicated earlier, a judge in a high volume district is also more likely to have ready access to, or feel obliged to seek out and consider, the body of unpublished fee decisions from the same district. Those decisions may affect published decisions within the district, ultimately making it more difficult for class counsel to request fees that are substantially out of line with the fees other judges from the same court have awarded in larger cases.

The final question that Model 2 addresses is whether the effects that public pension lead plaintiffs and *ex ante* agreements have on fee requests are conditional, or are simply two different ways of measuring the same thing—the influence that an active, sophisticated lead plaintiff has on fee requests.[98] With the interaction between *Public Pension* and *Ex Ante* included in the regression, the two separate individual variables now represent partial effects—the effect of a public pension lead plaintiff without an *ex ante* agreement and vice versa at mean settlement values. Both individual variables remain negative and significant in Model 2, with magnitudes that are identical. In the presence of either a public pension lead plaintiff or an *ex ante* agreement, fee requests average just under 26.4%, all else being equal. The interaction term in Model 2, while negative, is insignificant. In other words, there is no evidence of any greater effect on fee requests when the class action has both a negotiated *ex ante* fee agreement and a public pension fund lead plaintiff. Consequently, it appears that each of these two variables is indeed measuring the influence of an active, sophisticated lead plaintiff on fee requests. Together they suggest that this aspect of the PSLRA is working largely as Congress intended. In cases where a real plaintiff plays a meaningful role in selecting and retaining counsel, some of the agency costs typically associated with securities class actions are reduced.

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[97] *See* Goldberger v. Integrated Resources, Inc., 209 F.3d 43, 52 (2d Cir. 2000); *In re* Bristol-Myers Squibb Sec. Litig., 361 F. Supp. 2d 229 (S.D.N.Y. 2005) (awarding an attorneys' fee of 4% of the settlement).

[98] *See* Baker, Perino & Silver, *supra* note __, at ___.

Models 3 through 6 supplement the analysis of high volume districts by looking at whether attorneys' moderate their fee requests when they appear before judges with significant experience handling securities class actions. The descriptive statistics for the sample suggested precisely this kind of strategic behavior, and these regressions confirm those results. Whether judicial experience is measured as the total number of decisions the judge has in the data set (Models 3 and 4) or if instead we pool high volume judges (Models 5 and 6), we see the same dynamic at work. The more experience an individual judge has with securities class actions, the lower the fees that class counsel requests. This phenomenon, however, appears to be limited to experienced judges in high volume districts. In models with an interaction for high volume districts and judges, the interaction is negative and significant while the variable that measures judicial experience is insignificant. This result suggests that lawyer put a great deal of care into structuring their fee requests. For the most experienced judges in high volume districts, fee requests average 1.7% less than requests made to less experienced judges in low volume districts. Experienced judges in low volume districts (now represented by the *Judge Frequency* or *High Volume Judge* variables) see fee requests that are statistically indistinguishable from their colleagues who have seen fewer such cases.

Plaintiffs' lawyers in securities class actions do not appear to take lightly the decision to lower their fee requests. They certainly do so in the presence of a public pension lead plaintiff or an *ex ante* fee agreement. But in situations where the lead plaintiff does not appear to be monitoring their behavior, they ask for uniformly high fees regardless of settlement size. As we will see in the next section, experienced judges from districts that see these cases frequently award lower fees. Attorneys appear to anticipate these awards and moderate their requests when they appear before these judges.

One way to see how limited the situations are in which attorneys will independently reduce their fee requests is to flip the analysis around to focus on the least experienced judges. Model 7 includes a variable (*One Opinion*) that takes a value of 1 if a judge has only one fee decision in the data set and 0 otherwise. Since that opinion must come from the same case, the lawyers

effectively have no information about how that particular judge might award fees.[99] As in previous models, Model 7 interacts this variable with the *High Volume* district variable. The fee requests made to judges from low volume districts with only one decision are indistinguishable from the average fee request of just under 31% made in a low volume district. For experienced judges in high volume districts, fee requests are on average 3.01% lower than fee requests in low volume districts. For judges without an established track record in high volume districts, however, fee requests are 1.57% higher than more experienced judges in those districts. Fee requests remain lower for inexperienced judges in high volume districts than for judges in low volume districts (presumably because of the abundance of precedents from other judges in the district supporting lower fees), but not as low as for judges from the high volume district with a more established record. These findings support the hypothesis that plaintiffs' attorneys adjust their fee requests according to both the relevant judge's individual experience and the collective experience of the relevant court in litigating securities class actions.

b. Fee Awards

The models in Table 5 examine how the same variables we analyzed with respect to fee requests affect fee awards. The descriptive statistics suggest that in a typical case the judge displays a relatively light touch when it comes to reducing the requested fees. Fee cuts occur in a minority of cases. While such cuts can be large when they occur, on average lawyers get the vast majority of the fees they request. The higher fee *requests* we observe in low volume districts suggest that attorneys might anticipate higher fee *awards* when their cases are litigated in those districts.

As we did in in the models for fee requests, Model 1 in Table 5 begins without interaction terms. At mean settlement values, fee awards in low volume districts average 29.9%. In high volume districts, fee awards average 26.8%. In either kind of district, *ex ante* fee agreements and public pension lead plaintiffs have a significant moderating influence on fees. Average fees in all cases with an *ex ante* fee agreement are 24.5% at mean settlement values. For cases with public

[99] As noted previously, such information may be available to the extent that a judge issued fee decisions before our study period.

pension lead plaintiffs, fee awards average 25.6%. When judges cut fees, we observe reductions of similar magnitude: fee cuts average about 3.8%.

It is noteworthy that when courts award a fee that is lower than the requested amount they apparently pay little heed to objectors. We found no evidence that objections to fee requests have any significant relationship to fee awards. There are several potential explanations for this result. One is that objections are infrequent. Objections to the fee request were filed in only about one-fifth of the cases (21.93%), and nearly half of the cases with objections (45.08%) had only a single objection. Of the 122 cases with any kind of objection, only 19 (15.57%) had five or more objections. Most courts consider a low rate of objections to be support for the proposed settlement and fee,[100] although the strength of such an inference seems dubious given the collective action problems facing class members. Many plaintiffs' lawyers complain about the presence of "professional objectors," who file *pro forma* objections to proposed class settlements simply in an attempt to extract a greater share of the settlement or to garner attorneys' fees for providing what they contend are independent benefits to the class.[101] If courts believe that these professional objectors predominate (and there is some evidence that they do),[102] it is not surprising that courts pay little attention to objectors when awarding fees.

Competition for the lead plaintiff position at the start of the case is also correlated with lower fee awards at the end of the case. On average, fee awards

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[100] *See, e.g., In re* AT&T Corp. Sec. Litig, 455 F.3d 160, 165 (3d Cir. 2006) (court should consider presence or absence of substantial objections in evaluating fee request); *In re* Tyco Int'l, Ltd. Sec. Litig. 535 F. Supp. 2d 249, 269 (D. N.H. 2007) (fact that only eleven objections were filed to proposed fee out of more than 2.4 million class members who received notice of the settlement supported proposed fee).

[101] *See* In re Initial Pub. Offering Secs. Litig., 721 F. Supp. 2d 210, 215-16 (S.D.N.Y. 2010); Barnes v. FleetBoston, No. 01 Civ. 10395, 2006 U.S. Dist. LEXIS 71072, at *3 (D. Mass. Aug. 22, 2006) ("Repeat objectors to class action settlements can make a living simply by filing frivolous appeals and thereby slowing down the execution of settlements. The larger the settlement, the more cost-effective it is to pay the objectors rather than suffer the delay of waiting for an appeal to be resolved (even an expedited appeal)."). For a discussion of this phenomenon, see Brian T. Fitzpatrick, *The End of Objector Blackmail?* 62 VAND. L. REV. 1623 (2009).

[102] *See* O'Keefe v. Mercedes-Benz United States, LLC, 214 F.R.D. 266, 295 n.26 (E.D. Pa. 2003) ("Federal courts are increasingly weary of professional objectors: some of the objections were obviously canned objections filed by professional objectors who seek out class actions to simply extract a fee by lodging generic, unhelpful protests.") (citation omitted).

are about 1 percent less in cases with that kind of competition. While it is possible that competition signals the court that the case is more lucrative and perhaps less risky, leading to a reduction in fees, this does not appear to be the case. Instead, the magnitude of the decline in fee awards is about the same as the decline in fee requests in these cases. In other words, courts appear to be awarding lower fees in cases with competitors for the lead plaintiff position because attorneys are asking for lower fees in those cases. This result, along with the general ineffectiveness of objections to fee requests, underscores the importance of focusing on *ex ante* versus *ex post* strategies for addressing fees, a matter which we will return to in more detail in Section IV.

Unlike in models for fee requests, which showed a weak (negative) correlation with *Case Age*, Model 1 shows no statistically significant correlation between the number of years the case was litigated and fee awards. The lack of any significant relationship between these variables is interesting, given the standards courts typically employ in awarding fees. For example, *Johnson v. Georgia Highway Express, Inc.*,[103] one of the leading class action fee precedents, adopts a twelve-part test for evaluating fee requests. Two elements of that test—"the time and labor required" to reach the settlement and the opportunity costs associated with taking a particular case—relate to the length of time a case has been litigated. The duration of the case is also correlated, albeit imperfectly, to the hours an attorney has devoted to a case. Indeed, consistent with appellate court precedent in the Ninth,[104] the Second,[105] and other circuits,[106] a majority of courts in our nationwide data set (56.64 percent) used a lodestar cross-check to evaluate the requested fee. The prevalence of these time-based factors in legal doctrine and the insignificance of *Case Age* in our findings suggest a substantial disconnect between what these courts say they do and what they actually do when awarding fees. Instead, courts in practice seem to follow something closer to a pure percentage approach to fee awards.[107]

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[103] 488 F.2d 714,717-18 (5th Cir. 1975).

[104] *See* Vizcaino v. Microsoft Corp., 290 F.3d 1043, 1047 (9th Cir. 2002).

[105] *See* Goldberger v. Integrated Resources, 209 F.3d 43, 50 (2d Cir. 2000).

[106] *See In re* Rite Aid Corp. Sec. Litig., 396 F.3d 294, 305 (3d Cir. 2005).

[107] Several circuit court decisions have adopted just such an approach. *See* Swedish Hosp. Corp. v. Shalala, 1 F.3d 1261, 1271 (D.C. Cir. 1993); Camden I Condominium Ass'n v. Dunkle,

Given the prevalence among courts of using a lodestar cross-check to justify fee awards,[108] we investigated whether there is any evidence that this procedure has any meaningful impact on fees. Although we do not report the results separately in Table 5, we ran a regression that included as an explanatory variable whether the court stated in its fee order that it had used a lodestar cross-check in arriving at its fee award. If this approach by courts was useful, we would expect to see systematic differences between those courts that use a cross-check versus those courts that award fees on a simple percentage basis. That is not the case. There was no statistically significant difference between fee awards using a lodestar cross-check and fee awards under the percentage of the recovery approach. This result supports previous academic criticisms of the lodestar methodology.[109] It also suggests that the time and resources lawyers devote to tracking lodestar amounts and the enormous number of hours that some judges spend reviewing firm billing records is largely a waste of time.

As we did when we analyzed fee requests, Model 2 adds interaction terms between settlement size and high volume districts and between *ex ante* agreements and public pension lead plaintiffs. We continue to see very similar results. On average in a low volume district, courts award attorneys' fees of about 29.8% in cases without either a public pension lead plaintiff or an *ex ante* fee agreement. There is no evidence that those fees vary with settlement size. In a high volume district, by comparison, courts in similar cases award, on average, only 26.7% in attorneys' fees. The interaction term *Mean Settlement x High Volume* also remains significant in Model 2. On average, fee awards in districts that see securities class actions frequently decline as settlement size increases. For a settlement one standard deviation above the mean ($216.8 million), fee awards in low volume districts average about 29.4% compared to 24.8% in high volume districts. This is an average difference of about $10 million per fee award, an amount that is both statistically and economically significant.

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946 F.2d 768, 774 (11th Cir. 1991). The pure percentage approach was also the second most common approach in our sample, occurring in 44.05 percent of the fee awards we examined.

[108] Indeed, some judges have argued that conducting such a cross-check is an ethical imperative. See Vaughn R. Walker & Ben Horwich, *The Ethical Imperative of A lodestar Cross-Check: Judicial Misgivings about "Reasonable Percentage" Fees in Common Fund Cases*, 18 GEO. J. LEGAL ETHICS 1453 (2005).

[109] *See supra* note ___.

Put another way, the significance of the interaction between settlement values and high volume districts with regard to fee awards, as opposed to fee requests, suggests that plaintiffs' attorneys are able to exploit imperfections in the market for attorneys' fees. That is, class counsel request larger fees in districts that are more likely to award them. If that were not the case, then fee awards in low volume districts would match fee awards in high volume districts, regardless of the size of the fee requests.

If the PSLRA were working as intended, one would not expect to find inter-court variations like these. Both the plaintiffs' securities bar and the investment markets operate nationwide; any plaintiffs' law firm can appear in a securities class action in any federal district court. If lead plaintiffs consistently shopped for lawyers and drove hard bargains when negotiating *ex ante* fee agreements, one would expect to find fairly uniform fee terms and fee awards across courts after controlling for relevant case characteristics.

We surmise that judges in low volume districts are operating in a comparatively lower information environment than their counterparts in high volume districts. Because they see these cases less frequently and because so many fee awards are unpublished,[110] they have a smaller pool of precedents on which to base their decisions. As noted above, judges seem to generally disregard objectors, perhaps because they deem them an unreliable signal of excessive fee requests.[111] Defendants are indifferent to fee requests because the fees are paid out the common fund.[112] In such a non-adversarial setting, it is hardly surprising that a time-constrained federal judge would be inclined simply to sign the proposed fee order that class counsel has drafted.

The effects on fee awards associated with *ex ante* fee agreements and public pension funds remain the same in Model 2. Individually, both variables are negative and significant, with magnitudes that are roughly similar. The interaction

[110] Fees are typically awarded via a court order which is filed and is public, but which is not a published opinion of the court.

[111] *See supra* ___.

[112] In our nationwide data set, there was not one instance in which a defendant objected to a proposed fee. Furthermore, it is common practice for settlement agreements to state that the defendant "agrees not to oppose a fee request by class counsel of X dollars/percent or less."

term remains negative, but insignificant. At this stage, there is no evidence of any greater effect on fee awards when there is both an *ex ante* agreement and a public pension lead plaintiff. The variables *Cut* and *Fee Objection* are similar to what we found in the previous model. Judicial fee cuts average about 3.9%. There is no evidence that objections are correlated with fee awards.

Models 3 through 7 in Table 5 examine the impact on fee awards of individualized judicial experience with securities class actions. The results mirror those found in our regressions on fee requests. Overall, experienced judges award lower fees than less experienced judges, but this appears to be true only for experienced judges in districts that see substantial securities class action filings. To illustrate this point, consider Models 5 and 6, in which we include an indicator variable for judges who contributed four or more decisions to our data set. Viewed in isolation (Model 5) all such judges appear to award fees that are, on average, 1.7% lower than those awarded by less experienced judges. But when we interact that indicator variable with high volume districts, we see that all of that reduction comes from the most experienced judges in the highest volume districts. Contrast that result with judges from high volume districts with the least amount of experience (Model 7). The fees that the less experienced judges award are lower than those awarded by their counterparts in low volume districts, but not nearly as low as the awards by more experienced judges in their own districts. These results suggest that the more judges see securities class actions, the less willing they are to award fees to the attorneys who bring them.

c. Judicial Fee Reductions

In order to evaluate the relative impact of *ex ante* and *ex post* approaches to attorneys' fees, it is useful to consider the variables correlated with judicial fee reductions. To do that, we created a logit model with *Cut* as the dependent variable. We used the same variables we employed in our fee regressions because we wanted to see whether these variables could also predict the cases in which fee cuts occurred. What is noteworthy about these variables is that, with the exception of *Objection*, they are readily observable to case participants prior to any fee application. The coefficients for the logit model we report in Table are the marginal effects of each independent variable when the other independent variables are set to their means.

Table 6 shows that there are some variables that increase or decrease the probability of a fee cut. For example, there is evidence that courts do in fact defer to the fee arrangements negotiated by public pension funds and to *ex ante* agreements. Indeed, the effect on the probability of these two variables is nearly identical. In the presence of either one, the probability of a fee cut declines by about 13 percentage points. As with our regressions for fee awards, there also appears to be significant inter-court variation—in a high volume district fee cuts are about 12 percentage points more likely than in a low volume district.

Table 6 also shows that, all else being equal, the probability that the judge will reduce the requested fee is related to the settlement size. A closer look at those probabilities, however, shows a seemingly anomalous result. The likelihood of a fee cut increases in low volume districts (represented here by the *Settlement* variable). By contrast, in high volume districts (*Settlement x. High Volume*), the probability of a fee cut decreases with settlement size. The explanation for this counter-intuitive result most likely lies in our findings with respect to fee requests. On average, as settlement size increased, plaintiffs sought lower fees in high volume versus low volume districts. With lower fee requests, there was likely less need for high volume courts to cut fees. A similar dynamic occurs with high volume judges. Outside the high volume districts, judges with more experience with securities class actions are more likely to cut fees. In high volume districts, because the most experienced judges see lower fee requests, they are less likely to cut the requested fees. In other words, *ex ante* steps to reduce fee requests reduce the likelihood that judges will make *ex post* adjustments in their fee awards.

While these results are consistent with our linear regressions for requests and awards, it is important to recognize the limitations in this analysis. Perhaps the best way to evaluate the utility of a logit model is to see how well it classifies cases. In other words, do the model's predictions for which cases will have fee cuts match up with what actually happened in the cases in the sample? Overall, we find that the model correctly predicted 85.17% of the cases. In the abstract that sounds like a powerful predictive tool, until one realizes that there were no fee cuts in 85.38% of the cases in the database. We would have achieved virtually identical results if we had simply guessed that there were no fee reductions in any of our sampled cases. A closer examination reveals just how poorly the model performs. It correctly predicted all but three of the 358 cases without fee cuts, but

identified only one of the sixty cases in which reductions actually occurred. In other words, when it came to identifying the situations in which judges did cut fees, the model was wrong more than 98% of the time.

Notwithstanding the model's low predictive power, it does illustrate that *ex ante* fee agreements, public pension lead plaintiffs, and judicial experience are all associated with the probability of a fee cut. The real lesson of the analysis, however, is that these variables tell only a small part of the story. Logically, that realization suggests two possible alternatives. The first is that judicial fee reductions are, for all intents and purposes, random events. The second is that other unobserved (or perhaps unobservable) case or judicial characteristics play the dominant role in determining whether the court will cut fees.

Either scenario raises serious questions about how fees are set in securities class actions (and in class actions of other types). Some judges may believe they have the ability to identify and accurately reduce "excessive" fee requests, but if they do they are relying on criteria other than those we have tested here. The standards that courts explicitly employ also contemplate that judges have the ability to assess *ex post* a vast array of factors, including how hard the attorneys worked, how much risk they faced, the quality of the results they obtained, and the relationship of the fee request to similar cases.[113] Perhaps long experience with any given case or with securities class actions more generally provides judges information that is more nuanced than we can capture here. Indeed, that might partially explain why fees in high volume districts differ so dramatically from fees in low volume districts.

But we suspect that something more is going on. We speculate that the unpredictability of fee cuts derives from the fact that fee reductions are primarily the product of subjective assessments by judges based on their own idiosyncrasies, biases, and heuristics rather than the objective facts of any given case. Temperament, judicial philosophy, experience with class action litigation, personal wealth, pre-judicial work history, personal earnings history, political ideology, and other individual and largely unobservable judicial characteristics may well—consciously or unconsciously—drive judges' decisions about whether and how much to reduce fees. Indeed, the importance of such variables might

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[113] *See Johnson*, 488 F.2d at 717-19; City of Detroit v. Grinnell Corp., 495 F.2d 448, 470 (2d Cir. 1974).

partially explain our finding that in one-third of the fee-reduction cases the court offered no justification or explanation at all for its decision.[114] When courts do offer an explanation, the most common one is simply that the requested fee is "too large."[115]

Our data show that class counsel can expect some kind of fee reduction in about one out of every seven cases, and experience suggests that some judges may be more likely than others to cut the requested fees.[116] But whether fees will be cut in any particular case will likely be impossible to determine at the time the fee request is made. And little more is likely to be known after a given court's fee ruling because the courts' fee opinions offer no reliable explanations for those decisions.

The inability to account for fee cuts in securities class actions on the basis of objective factors raises a broader concern for class actions of all types. The unpredictability of fee cuts implies that, to a significant extent, fee awards are unpredictable too. This is likely true for all class actions, because the doctrines and procedures that govern fee awards are largely trans-substantive. If anything, fee awards in other types of federal lawsuits may be more uncertain than those in securities fraud class actions because the PSLRA applies only to the latter. In cases of other types, fee awards are governed by federal common law, which places only the weakest of constraints on the discretion of district court judges. Uncertainty regarding fees can be expected to discourage lawyers from investing optimally in class actions by creating downside risks that lawyers will avoid. This uncertainty ultimately harms both class members (by impairing the quality of the representation they receive) and the general public (by weakening the deterrent effect of the law).

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The picture that emerges from these nationwide data is both nuanced and significantly different from much conventional wisdom regarding attorneys' fees

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[114] *See supra* __.

[115] *See supra* __.

[116] For example, one district judge in the Southern District of New York, Shira Scheindlin, cut requested fees in three of the five decisions in our sample in which she was the judge.

in securities class actions. We found that some lead plaintiffs do seem to take seriously the responsibility Congress bestowed on them, carefully choosing their lawyers, aggressively negotiating fees with them upfront, and actively monitoring them throughout. But such plaintiffs are in the minority. In most cases, lead plaintiffs appear passive, seemingly agreeing at the time of settlement to whatever fees their attorneys deem appropriate.

Even more troubling are our findings regarding the role of the courts in the fee-setting process. We found no evidence that the actions taken by the courts move class counsel's fees closer to the "right price." Instead, we found that the courts facilitate, rather than prevent, the exploitation of market imperfections by class counsel, enabling them systematically to obtain higher fees from courts and judges that see securities class actions less frequently than from more experienced courts. And although judges do sometimes cut class counsel's fees, we found those decisions to be unpredictable. That is, judicial fee cuts are as likely to result in fees that are further from the "right price" as they are to move them closer to that ideal.

In sum, there is little to celebrate in the current state of affairs, and reason to think that even small improvements in the fee-setting process might yield significantly better results.

IV. SHOULD COURTS SET FEES *EX ANTE*? A PROPOSAL

In this section we consider some possible improvements to the current process by which class counsel's fees are determined under the PSLRA. We begin by examining previous reform proposals. We go on to offer our own reforms, which we believe improve upon those prior efforts.

A. Prior Reform Proposals

In 2002, a Task Force convened by the Third Circuit issued a report on the manner of selecting and compensating lawyers who handle class actions.[117] It encouraged judges presiding over securities cases to base fee awards on negotiated agreements between lead plaintiffs and class counsel. After observing

[117] Third Circuit Task Force Report, *Selection of Class Counsel,* 208 F.R.D. 340 (2002) ("2002 Task Force Report").

that "[t]he PSLRA establishes a model of client control that extends ... to ... negotiation of the fee," the Task Force "conclude[d] ... that strict scrutiny of the fee agreement [would be] inconsistent with the client-driven litigation model established in the PSLRA." Instead, it urged district court judges to "presume that the fee is reasonable when it is the result of an agreement between the 'most adequate' plaintiff and chosen counsel." Judges should override this presumption only when the agreed compensation is "clearly excessive", "has been rendered unfair by unforeseen developments", or "was not reached by arm's-length negotiation between the lead plaintiff and counsel".[118]

The Task Force issued its proposal on the heels of the Third Circuit's decision in *Cendant* and its recommendation hews closely to the approach endorsed in that case, which also encouraged district court judges to defer to negotiated fee agreements. As the Third Circuit explained:

> We [] believe that, under the PSLRA, courts should accord a presumption of reasonableness to any fee request submitted pursuant to a retainer agreement that was entered into between a properly-selected lead plaintiff and a properly-selected lead counsel. This presumption will ensure that the lead plaintiff, not the court, functions as the class's primary agent vis-a-vis its lawyers. Further, by rendering *ex ante* fee agreements more reliable, it will assist those agreements in aligning the interests of the class and its lawyers during the pendency of the litigation.[119]

The Third Circuit also agreed that judges could properly override the presumption when "unusual and unforeseeable changes, i.e., those that could not have been adequately taken into account in the negotiations," arose and when "the (properly submitted) retainer agreement fee is clearly excessive." The Court thought it

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[118] *Id.* at 425-426. *See also* RESTATEMENT (THIRD) OF LAW GOVERNING LAWYERS § 125 (2000) (stating that in class actions "[a] more appropriate arrangement" for reducing settlement-related conflicts in class actions "is for the lawyer's fee to be negotiated initially by the client and lawyer at the outset of the relationship, it being understood and disclosed to the client that the ultimate award may be scrutinized by the opposing party and approved by the court").

[119] In re Cendant Corp. Litig., 264 F.3d 201, 282 (3d Cir. 2001). In support of this recommendation, the Third Circuit cited Weiss & Beckerman, *supra* note ___, at 2105, which observed that "a court might well feel confident in assuming that a fee arrangement an institutional investor had negotiated with its lawyers before initiating a class action maximized those lawyers' incentives to represent diligently the class's interests, reflected the deal a fully informed client would negotiate, and thus presumptively was reasonable."

unlikely that "candidates for [the] lead plaintiff designation [would] be deterred by the understanding that their retainer fee arrangement [sic] with Lead Counsel will be subject to judicial review for clear excessiveness."[120]

Clearly, the Task Force's recommendation is compatible with the holding of *Cendant*. Both place great weight on *ex ante* fee agreements between lead plaintiffs and class counsel, and both set out similar grounds for overriding the terms of *ex ante* agreements on *ex post* judicial review. But the Task Force did not simply follow the Third Circuit's jurisprudence down the line. Its recommendation differs from *Cendant*'s holding in a key respect: the former, but not the latter, encouraged judges to set preliminary fee terms early in the litigation. In other words, the Task Force followed *Cendant* in recommending deference to fee agreements negotiated *ex ante* between attorneys and lead plaintiffs but added that judges should set fee terms when appointing class counsel instead of addressing fees for the first time when litigation concludes, as they usually do. Although the Task Force agreed that judges had to review fee awards for reasonableness at the end of litigation, it emphasized that the terms of class counsel's compensation should be addressed at the appointment stage as well.[121]

The Task Force is far from the only authority to encourage judges to set preliminary fee terms when appointing class counsel. Successive editions of the *Manual for Complex Litigation* advise judges to establish ground rules for fee awards and cost reimbursements at this juncture.[122] A series of guides for judges published by the Federal Judicial Center since the 1980s also endorses this

[120] *Id.* at 282-283.

[121] See 2002 Task Force Report, supra note ___, at 420-421 ("[T]he topic of attorney fees should be addressed at the early stages of the case as well as throughout the prosecution of the case. At the outset of the case, the court may be well-advised to direct counsel to propose the terms for a potential award of fees; the potential fees might be established within ranges, with the court making it clear to the parties that the fee remains open for further review for reasonableness. A preliminary fee arrangement may provide a helpful structure for the court when it conducts its reasonableness review at the end of the case.").

[122] *See* MANUAL FOR COMPLEX LITIGATION (THIRD) § 24.21 (entitled "Setting Guidelines and Ground Rules"); MANUAL FOR COMPLEX LITIGATION (FOURTH) § 14.211 (entitled "Selecting Counsel and Establishing Fee Guidelines").

approach.[123] Other appellate courts have expressed a preference for *ex ante* fee agreements in class litigation.[124] Setting attorneys' fees *ex ante* was one of the primary motivations for the now-abandoned experiments in some courts to auction the role of class counsel.[125] One can also find a strong hint in this direction in the report a prior Third Circuit Task Force issued in 1986. The earlier Task Force recommended "that in the traditional common-fund situation ..., the district court, on motion or its own initiative and at the earliest practicable moment, should attempt to establish a percentage fee arrangement agreeable to the Bench and to plaintiff's counsel."[126] Although members of the 1986 Task Force disagreed as to when the "earliest practicable moment" was likely to arrive, the report noted that "high management judges will want to settle the fee question at the outset of the case" and that "[a]ll lawyer members of the Task Force ... desired early clarification of the fee issue."[127] Finally, some judges have set fees

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[123] *See* THOMAS E. WILLGING AND NANCY A. WEEKS, ATTORNEY FEE PETITIONS: SUGGESTIONS FOR ADMINISTRATION AND MANAGEMENT 5-8 (1985); ALAN HIRSCH AND DIANE SHEEHEY, AWARDING ATTORNEYS' FEES AND MANAGING FEE LITIGATION 109 (1994); ALAN HIRSCH AND DIANE SHEEHEY, AWARDING ATTORNEYS' FEES AND MANAGING FEE LITIGATION 113-114 (2nd ed. 2005); BARBARA J. ROTHSTEIN & THOMAS E. WILLGING, MANAGING CLASS ACTION LITIGATION: A POCKET GUIDE FOR JUDGES 33 (3d ed. 2010); BARBARA J. ROTHSTEIN & CATHERINE R. BORDEN, MANAGING MULTIDISTRICT LITIGATION IN PRODUCTS LIABILITY CASES, A POCKET GUIDE FOR TRANSFEREE JUDGES 14 (2011).

[124] *See Silverman*, 739 F.3d at 958 ("establishing a fee structure at the outset of a suit is desirable; unlike auctions, which private markets in legal services do not use, ex ante fee structures are common and beneficial to clients."); *In re Synthroid*, 264 F.3d at 718 ("Only ex ante can bargaining occur in the shadow of the litigation's uncertainty; only ex ante can the costs and benefits of particular systems and risk multipliers be assessed intelligently."); *Swedish Hospital Corp.*, 1 F.3d at 102 ("Mechanisms which may facilitate a judge in more closely approximating the market include: encouraging class counsel to enter into preliminary non-binding fee agreements with class members").

[125] *See In re* Auction Houses Antitrust Litig., 197 F.R.D. 71, 85 (S.D.N.Y. 2000); *In re* Bank One Shareholders Class Actions, 96 F. Supp. 2d 780, 784-90 (N.D. Ill. 2000); *In re* Lucent Techs., Inc., Sec. Litig., 194 F.R.D. 137, 155-58 (D.N.J. 2000); *In re* Oracle Sec. Litig., 131 F.R.D. 688, 697 (N.D. Cal. 1990). For a critique of auctions, see Jill E. Fisch, *Lawyers on the Auction Block: Evaluating the Selection of Class Counsel by Auction*, 102 COLUM. L. REV. 650 (2002).

[126] *Report of the Third Circuit Task Force, Court Awarded Attorney Fees*, 108 F.R.D. 237, 255 (1986) ("1986 Task Force Report").

[127] *Id.* at 274, n. 62.

up front,[128] and others have encouraged lawyers to bring the matter of fees to their attention early on.[129]

While there is thus considerable support for negotiating fees *ex ante*, substantial problems remain in the way that courts have handled these issues. As we have noted, it is only a minority of cases that have actually adopted this approach explicitly, whereas we believe that this should be the universal approach to fee-setting in class actions.[130] Courts often discuss in general terms that they will respect retainer agreements, but do not specify the precise process they will follow in reviewing those agreements. In many cases, review of the retention agreement seems to come only at the end of the case when the court is awarding fees rather than when it selects the lead plaintiff and lead counsel. Courts also tend to be frustratingly vague when it comes to specifying the circumstances under which they will choose not to defer to such agreements. For example, in *In re AT&T Corp. Sec. Litigation*, the Third Circuit emphasized that:

> the presumption of reasonableness set forth in *Cendant* does not diminish a court's responsibility to closely scrutinize all fee arrangements to ensure fees do not exceed a reasonable amount. We caution against affording the presumption too much weight at the expense of the court's duty to act as "a fiduciary guarding the rights of absent class members."[131]

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[128] Most famously, Judge John F. Grady did so in *In re* Continental Illinois Securities Litigation, 572 F. Supp. 931 (N.D. Ill. 1983). Judge Grady's order is discussed in detail in Thomas E. Willging, JUDICIAL REGULATION OF ATTORNEYS' FEES: BEGINNING THE PROCESS AT PRETRIAL (1984).

[129] See *In re* First Fid. Bancorporation Securities Litig., 750 F. Supp. 160, 163 (D.N.J. 1990) ("Unfortunately, counsel did not avail themselves of the procedure outlined in the [1986] Task Force Report, wherein the contingent fee is to be negotiated and approved at the outset of the litigation.") (*citing 1986 Task Force Report,* 108 F.R.D. at 255–258).

[130] *See, e.g., In re* Global Crossing Sec. & ERISA Litig., 225 F.R.D. 436, 466 (S.D.N.Y. 2004) (noting that "courts presume fee requests submitted pursuant to a retainer agreement negotiated at arm's length between lead plaintiff and lead counsel are reasonable."); *In re* Cardinal Health Inc. Sec. Litig., 528 F. Supp. 2d 752. 758 (S.D. Ohio 2007).

[131] 455 F.3d 160, 168-69 (3d Cir. 2006) (citing Cendant, 264 F.3d at 231); *see also In re* Bristol-Myers Squibb Sec. Litig., 361 F. Supp. 2d 229, 237 (S.D.N.Y. 2005) ("fact that the 7.5% fee was negotiated with institutional Lead Plaintiffs ... should not and, here, does not, lead to the conclusion that this percentage is presumptively fair.").

Vague statements such as these create too much uncertainty over whether and to what extent the court will actual defer to a vigorously negotiated *ex ante* fee agreement.

We address all of these concerns in the following proposal.

B. Our Proposal

We believe that, as a general matter, the authorities discussed in the preceding section are on the right track. All support a shift from the traditional end-of-litigation approach currently taken by courts to set fees in most class actions to a start-of-litigation regime in class actions governed by the PSLRA. Having considered the details of those prior recommendations, which vary, we tentatively propose the following set of arrangements:

1. The lead plaintiff should negotiate a fee when retaining counsel to handle the case;
2. The lead plaintiff should disclose the terms of the negotiated fee to the district court when offering a law firm for appointment as class counsel;[132]
3. The district court should review the negotiated fee terms before appointing class counsel and should uphold them unless they are clearly unreasonable or not the products of arm's length negotiations; and
4. When reviewing class counsel's request for a fee award at the end of litigation, the district court should apply the agreed terms unless unforeseen developments have rendered those terms clearly excessive or unfair.

Our nationwide data, discussed in the preceding sections, suggest that these proposed procedures will require most courts, lead plaintiffs, and law firms that represent plaintiffs in securities class actions to change their current practices. But these changes should be relatively simple to make. And, as the following sections explain, the result should be fee awards that more closely approximate the "right price" as envisioned by the PSLRA.

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[132] Plaintiffs have legitimate reasons for wanting to prevent defendants from acquiring information about their fee terms. We therefore propose that fee agreements be submitted under seal for *in camera* review by the district court. The 2002 Task Force made a similar proposal for dealing with bids submitted in connection with fee auctions. 2002 Task Force Report, *supra* note __, at 393-394.

1. *Our Proposal Respects the PSLRA's Preference for Private Ordering*

In keeping with the purpose of the PSLRA, our proposal treats the lead plaintiff as the bargaining agent for the class, with the district court judge serving as a backstop in case the lead plaintiff fails to do its job.[133] This arrangement makes sense because many lead plaintiffs, especially sophisticated institutional investors with large financial stakes, can be relied upon to demand appropriate terms when hiring attorneys. They have good information about the market for fees because lawyers compete for opportunities to represent them. They have considerable bargaining leverage over attorneys, for the same reason. They know that price and quality matter, not just price alone, so they will offer higher fees when, in their judgment, higher fees are likely to generate larger net recoveries. Lastly, they have incentives to save money. By promising supra-market rates for legal services, they would needlessly diminish their own recoveries. These effects are not just theoretical. Our empirical analyses show that cases with public pension lead plaintiffs and *ex ante* fee agreements have fees that are materially different from those in other cases.

Not all lead plaintiffs are likely to bargain hard over fees, however. Even today, many class actions are led by individual investors with fairly small stakes in the litigation. Our data showed that the fees in cases led by union-affiliated institutional investors are statistically indistinguishable from the fees in cases led by individual investors. These plaintiffs may have little incentive to bargain, limited access to counsel, and little information. Other lead plaintiffs are pension funds whose mangers may favor particular lawyers as a result of past campaign contributions or other relationships.[134] They may agree to pay higher fees than they should because their agents have been corrupted. *Ex ante* review of fee agreements enables judges to distinguish lead plaintiffs who are doing their jobs from those who are not, before litigation proceeds very far.

To make this assessment, judges will need evidence. We therefore expect lead plaintiff candidates to submit materials showing that they acted as zealous

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[133] See Charles Silver, *Reasonable Attorneys' Fees in Securities Class Actions: A Reply to Mr. Schneider*, 20 THE NAPPA REPORT 7, 7 (Aug. 2006) (arguing that "judges should intercede only when there is good reason to believe that lead plaintiffs failed to set fees at market rates").

[134] *See* 2002 Task Force Report, *supra* note __, at 402-403 & 411-412.

agents for the absent investors they seek to represent. For example, a pension fund's general counsel might prepare an affidavit describing the number of law firms that monitor the fund's portfolio for signs of fraud, the number of firms that bid for the opportunity to represent the fund in the current litigation, the range of the competing bids, and the reason(s) supporting the choice of the law firm offered to the court as counsel for the class. The affidavit might also describe the relationship between the fund and the law firm, including any political contributions that lawyers associated with the firm may have made to anyone associated with the fund, along with the fees the fund agreed to pay outside counsel when suing on its own in other matters.

Over time, the body of evidence bearing on the reasonableness of *ex ante* fee contracts would grow, and judges' initial fee assessments would become increasingly reliable. In cases with competing lead plaintiff candidates, judges could require all contenders to submit their fee agreements. This would increase the amount of information available and pressure all lawyers involved to offer market rates. Judges would also have a firm basis for disciplining lead plaintiffs who failed to bargain hard by referencing fees negotiated in comparable cases. If this evidence were readily available, it is reasonable to expect that it would have the greatest impact on, and utility for, judges in low volume districts or judges with little or no prior experience with securities class actions. As we have shown, it is in those cases that lawyers have the greatest ability to exploit the existing imperfections in the market for attorneys' fees. Making these data readily available to all judges may help to reduce the current information asymmetries we believe underlie our empirical findings.

When reviewing negotiated fee terms, district court judges would either uphold them or find them clearly unreasonable. Both findings would require an evidentiary basis. A visceral reaction by the judge that a proposed fee arrangement promises too much money to lawyers would not suffice; nor would other unsubstantiated concerns. Rather, when striking down a fee negotiated *ex ante*, a judge would have to show that the lead plaintiff failed to act as a zealous agent for the class or that the proposed fee deviates from the market rate so greatly as to be unacceptable.

Even so, the fee setting process would be simpler than it is today. For the initial review, a judge would need only the lead plaintiff's evidence and

information about prevailing market rates, which could be obtained from an expert report. For the final review, a judge would require evidence of unforeseen developments, if any, that rendered the previously approved, negotiated fee terms clearly excessive or unfair. For example, a defendant may have offered to settle immediately after the lead plaintiff was appointed, so that the result obtained could not possibly be attributed to class counsel's work. Ordinarily, such evidence, when it exists, will be within the court's judicial cognizance or could readily be obtained by questioning the parties.

By comparison, the existing fee setting process is inefficient and unprincipled. When petitioning for fees, lawyers may feel pressure to inflate their hours, billing rates, and lodestar multipliers. Objectors scour fee filings for errors and improper charges, accuse class counsel of being greedy, and attempt to extract payments by filing appeals. Judges approve fees without knowing how the requested fees compare with those prevailing in the market for legal services. And they cut fees randomly, for reasons that are often unspecified or unclear. By tying fees to the market and eliminating lodestar cross-checks on the back end, our proposal would reduce the burden on judges and all but eliminate opportunities for extortionate objections.

2. Our Proposal Creates Superior Incentives to Invest in Litigation

By setting class counsel's fees at the appointment stage, courts would strengthen class counsel's incentives to devote resources to the litigation, while also compensating them appropriately for incurring risks. When fees are first addressed at the end of litigation, lawyers' rights are under-specified.[135] They know what they will receive if they lose—nothing—but they can only guess at what they will be paid if they win. Because class actions require lawyers to bear large, undiversified risks in terms of both time and cash outlay, uncertainty surrounding their compensation terms likely inclines them toward parsimony. This predictably harms investors by reducing their recoveries.

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[135] John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter is Not Working*, 42 MD. L. REV. 215, 233 (1983).

a. Lawyers Currently Have Difficulty Predicting Fees

Within broad limits, fee awards in securities class actions are predictable. Indeed, the evidence compiled here suggests that plaintiffs' lawyers, particularly when they are dealing with an experienced judge from a high volume district, adjust their requests based on their assessments of what the judge is likely to award in fees. Still, the limits on judicial discretion remain broad, the outliers among fee awards are not trivial, and the variables that ultimately will be most relevant to the court's fee determination are unknowable at the commencement of the case.[136]

At the most general level, in the 145 securities fraud cases led by public pension funds in our nationwide data set, mean fee awards were 19.7% with a standard deviation of 7.8%. This implies that in about two-thirds of the cases the fee award fell within the 11.9%-27.5% range, while awards in the remaining cases were above or below these extremes. Settlement size is by far the best predictor of fee awards (explaining more than 90 percent of the variation in fee awards[137]), but at the outset of a litigation lawyers cannot predict settlement size with any degree of precision. And even if they could, the lawyers would still have difficulty predicting their eventual fees because courts often deviate from prevailing norms, usually by awarding less than settlement size alone would lead one to expect. With little ability to predict the cases in which such reductions will occur and given a predictable downward bias from courts, a rational plaintiffs' attorney might well choose to under-invest in the average case in order to guard against a substantial reduction in fees in any given case.

Fee awards also vary in response to other factors whose impact, in the absence of reliable *ex ante* fee terms, can only be guessed. For example, in percentage terms, fees and recoveries vary inversely. A larger recovery may imply a smaller percentage fee, although our data have shown that relationship to

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[136] *See* Samuel R. Berger, *Court Awarded Attorneys' Fees: What is "Reasonable"?* 126 U. PA. L. REV. 284 (1977) (leading class action lawyer arguing that to a great extent the outcome of fee requests depends "upon 'the roll of the dice'—from court to court and from case to case.").

[137] *See* Eisenberg and Miller, *supra* note __, at ___.

prevail only in the high volume districts.[138] But in any given case, the relationship is poorly specified. Judges exercise broad discretion and they vary in their generosity toward plaintiffs' lawyers, with substantial differences, as we have seen, in courts that see securities class actions more or less frequently. Class counsel in a case in a high volume district can be confident that greater success will cause their fee percentages to decline, but they cannot predict the magnitude of the effect. Long-term trends also matter. Perino found that "[m]ean fees in cases settled after 2002 were 24.9 percent, significantly lower than the period prior to 1999 (28.1 percent) or the period 1999–2002 (27.1 percent)."[139] Lawyers who file cases today can only guess whether the trend toward lower fees will stop, continue, or accelerate.

b. Uncertainty over Fees Harms Class Members

Although we know of no empirical study that shows that the class of investors does better when its counsel's fees are set *ex ante* rather than *ex post*, it seems safe to infer that the failure to specify lawyers' rights in advance discourages them from investing optimally in cases. When sophisticated clients hire lawyers in private market transactions, which are presumably efficient, they routinely set fee terms up front. Consider patent lawsuits. When Professor David L. Schwartz studied contingent fee patent representations, he found highly structured working arrangements and consistent *ex ante* bargaining over fee percentages and responsibility for costs.[140] *Ex ante* bargaining also occurs in securities lawsuits when sophisticated clients opt out of class actions and hire

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[138] See Jordan Milev, Robert Patton, Svetlana Starykh, and John Montgomery, Recent Trends in Securities Class Action Litigation: 2011 Year-End Review 21 (Dec. 14, 2011) (studying post-PSLRA cases and reporting that "the median plaintiffs' attorney[s'] fees [were] a third of the settlement amount [for settlements below $5 million], while for settlements of over $500 million, fees [fell] to below 10%.".

[139] Perino, *supra* note ___, at 389.

[140] See, e.g., David L. Schwartz, *The Rise of Contingent Fee Representation in Patent Litigation*, 64 ALA. L. REV. 335, 360 (2012) (reporting that lawyers and clients always fix fee percentages and responsibility for expenses up front in patent representations); Stephen D. Susman, Fee Agreements in Technology Litigation: Harmonizing Client and Attorney Interests, presented at 20th Annual Technology and Computer Law Conference (May 23-25, 2007) (providing sample terms used in fee agreements in patent representations, including terms governing contingent percentages and responsibility for litigation expenses).

lawyers to pursue tag-along suits.[141] In fact, to the best of our knowledge, class actions comprise the only area of contingent fee practice in which compensation terms are currently fixed when litigation ends.[142]

Why do clients and lawyers normally set contingent percentage fees when representations begin? Many reasons are apparent. First, it is usually easier to negotiate fees *ex ante* than *ex post*. At the start of litigation, there is no money to divide. There is only the prospect of forming a joint venture between a client and a lawyer that seeks to maximize the parties' joint wealth by offering the lawyer compensation terms that will motivate the lawyer to work hard on behalf of the client.

When fees are set at the end of litigation, by contrast, the amount to be recovered is already known. This heightens the conflict between the client and the attorney because every additional dollar for one means a dollar less for the other. This is why judges, who sit as absent class members' guardians, may think fee-setting is a zero-sum game, and also may think they are protecting class members when they set fees as close to zero as possible. They may see no upside to class members from paying higher fees because they are setting fees at a time when lawyers' services are no longer required.

Second, lawyers and clients should want to set compensation terms early on because this encourages lawyers to bear beneficial risks. Principals hire agents because agents can perform certain tasks more efficiently than principals can themselves. (Otherwise, principals would be better off acting directly.) In contexts where lawyers work on contingency, efficient working arrangements saddle lawyers with risks they can bear more readily than clients. This includes risks associated with the deployment of legal services. Lawyers pay for these

[141] *See In re* Synthroid Mktg. Litig, 264 F.3d 712, 720–22 (7th Cir. 2001) (looking to securities "benchmarks for determining legal fees"); *see also* Kevin LaCroix, *Ohio Joins the Time Warner Opt-Out Settlement Parade*, THE D&O DIARY (March 7, 2007), http://www.dandodiary.com/2007/03/articles/optouts/ohio-joins-the-time-warner-optout-settlement-parade/ (reporting that the State of Ohio agreed to pay "a 17.5% contingency fee to Lerach Coughlin" for representation in an opt-out securities case).

[142] State bar disciplinary rules require contingent fee arrangements to be set out in writings that expressly address compensation percentages, responsibility for litigation costs, and other matters. But these rules do not require the terms to be written down at the outset of litigation. *See, e.g.*, Model Rule of Professional Conduct 1.4.

services initially, by lending their time and bearing costs. Compensation and reimbursement come, when they do, from recovered funds. Under common arrangements, lawyers are reimbursed for expenses dollar-for-dollar.[143] Their profit comes entirely from the percentage fee.[144] This compensation structure creates a strong, though still imperfect, alignment of interests because it encourages lawyers to bear the costs and risks associated with litigation activities that are likely to benefit clients. It also reduces the monitoring burden on clients, who can usually trust lawyers to exercise good judgment when delivering services, incurring expenses, and evaluating settlement offers.

In contingent fee relationships, then, the fee percentage does the heavy lifting. It motivates lawyers to help clients by making good decisions that maximize joint gains. This is why clients and lawyers both benefit from fixing lawyers' compensation in advance. Leaving the core fee term unsettled creates uncertainty about compensation, causing lawyers to decline some risks that clients would rationally want them to take. The predictable result will be sub-optimal recoveries that leave clients and lawyers both poorer than they might have been.

Third, when contingent fee percentages are set *ex ante*, the risks associated with litigation are palpable because no one knows how they will play out. Will the class recover? If so, how large will the settlement be? The answers can only be estimated at the start of litigation. By contrast, when judges set fees *ex post*, everything is known. This creates significant potential for the hindsight bias to poison judges' assessments of litigation risks. The predictable result is that fee percentages will be set too low.

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[143] The reimbursed expenses do not usually include the law firm's general "overhead." The overhead expenses are ultimately borne by the lawyers (out of the "fees" portion of their award), consistent with standard practice in other contingent fee arrangements. See, e.g., ABA Formal Op. 93-379, Billing for Professional Fees, Disbursements and Other Expenses (Dec. 6, 1993) (stating that "A lawyer may not charge a client for overhead expenses generally associated with properly maintaining, staffing and equipping an office; however, the lawyer may recoup expenses reasonably incurred in connection with the client's matter for services performed in-house, such as photocopying, long distance telephone calls, computer research, special deliveries, secretarial overtime, and other similar services, so long as the charge reasonably reflects the lawyer's actual cost for the services rendered.").

[144] Of course, attorneys may have incentives to inflate their costs as an alternative way to profit from a case. Indeed, in the minority of cases in which there are objections to the settlement or fee request, allegations that attorneys are inflating their costs are a common theme.

Hindsight bias is a defect in human reasoning that causes people who know actual outcomes to misestimate *ex ante* odds. It specifically leads people to over-estimate the *ex ante* probability of the outcomes they observe. To document the impact of hindsight bias on federal judges, researchers gave more than 150 federal magistrates a statement describing a case in which a prisoner appealed after being sanctioned by a trial judge for filing a frivolous complaint.[145] One-third of the statements indicated that the appellate court affirmed the sanction; another third indicated that the appellate court imposed a lesser sanction; and the last third indicated that the appellate court vacated the sanction entirely. The judges were then asked to "go back in time" and identify the result that was most likely to occur on appeal. The estimates reflected the information that the magistrates received about the actual outcomes. "[T]he judges exhibited a predictable hindsight bias; when they learned that a particular outcome had occurred, they were much more likely to identify that outcome as the most likely to have occurred."[146]

The parties to real client-lawyer relationships would fare poorly if they allowed hindsight bias to influence their assessments of lawyers' compensation. Knowing that litigation produced a recovery, they would over-estimate the *ex ante* odds of winning and set lawyers' fee percentages too low. This would discourage lawyers from taking risks when they should. The problem is avoided by setting fees up front and enforcing *ex ante* fee agreements.

When fees are set *ex post*, the outcomes of all litigation risks are known and hindsight bias has many opportunities to distort judges' estimates of *ex ante* odds. Judges know, for example, that the complaint survived the motion to dismiss, instead of failing it as complaints often do. They know whether a class was certified, which can be a significant hurdle. They know the class obtained a recovery, which not all class actions do. They may also know that the recovery was large, which is a rarer accomplishment still. Predictably, this information will cause judges to over-estimate the lawyers' likelihood of success and underestimate the risk the lawyers' bore when they began the litigation, thereby

[145] Chris Guthrie, Jeffrey J. Rachlinski and Andrew J. Wistrich, *Inside the Judicial Mind*, 86 CORNELL L. REV. 777 (2001).

[146] *Id.* at 803.

exerting downward pressure on the judges' assessments of appropriate fees. Case law expressly ties fees percentages to the risks lawyers incur. Judges who are convinced that litigation risks were low cannot be expected to award high fees.

If courts lower fees based on these *ex post* assessments of risk, they also run the risk of awarding fees that are too low for another reason illustrated in our empirical data. Plaintiffs' lawyers are likely to have the greatest expertise in evaluating *ex ante* the potential risks and rewards of any potential case. Our data suggest that attorneys consider these risks in their fee requests. Case competition (our proxy for case quality) is negatively correlated with fee requests, i.e., lawyers already ask for lower fees in what appear to be higher quality cases. If judges acting *ex post* were to reduce fees even further, they run a substantial risk of setting fees that are too low given the risks the case entails.

Our proposal prevents hindsight bias from distorting judges' risk assessments by mimicking what normally occurs outside the class action context when clients hire lawyers on contingency. Fees are set at the outset of litigation, before any actual results are known. "For counsel to seek a contingent fee after the matter has been resolved is akin to placing a wager after the outcome of the event is known or playing poker with everyone's cards face up. The percentage of recovery should be negotiated and fixed while the risks and amount of recovery are still unknown."[147]

The theoretical case in favor of setting contingent fees *ex ante* is thus straightforward. Fee arrangements that motivate lawyers to maximize recoveries serve clients best. The market pressure that would likely exist if our proposal is adopted should therefore encourage lawyers to offer fee arrangements that have this effect. These arrangements will reduce uncertainty about lawyers' compensation to efficient levels, because higher levels of uncertainty would harm clients by discouraging lawyers from investing optimally. Actual transactions in all market sectors, including transactions involving sophisticated clients, show that efficient arrangements set lawyers' compensation terms at or near the start of litigation. Consequently, the current judicial practice of setting fees *ex post* in securities class actions is presumably inefficient and makes investors worse off.

[147] *In re First Fidelity Bancorporation Securities Litig,*, 750 F. Supp. 160, 163 (D.N.J., 1990).

c. Our Proposal Restores Objectivity and Reduces Arbitrariness

Finally, under our proposal, an *ex ante* fee contract would give class counsel considerable protection from a court's subsequent, arbitrary fee reduction by establishing a presumption of reasonableness following initial review. By accepting a lead plaintiff's recommendation of class counsel without complaint, a judge would establish that the lead plaintiff was a zealous bargaining agent and that the proposed fee terms set out in the *ex ante* fee agreement were reasonable given everything that was then known about the litigation and the prevailing market for attorneys' services. Because few grounds would exist for a court to revise this assessment *ex post*, the negotiated fee terms would be reliable and lawyers' incentives would be secure. A lawyer who challenged an *ex post* fee cut on appeal would also look like any other lawyer who sues to enforce a contractual right to payment.[148] By comparison, when appealing a low fee award today, class counsel must establish that a trial judge abused his or her discretion.[149] Because some evidence providing a basis for a low fee award can likely be found in every record, this is a very hard showing for class counsel to make.

Wal-Mart Stores, Inc. v. Visa U.S.A., Inc.,[150] an antitrust class action, provides an excellent example of arbitrary fee-setting. There, the Second Circuit affirmed a $220 million fee award on a settlement that provided for about $3.4 billion in compensatory relief. The Second Circuit agreed with the district court judge that the low fee percentage—6.511%—was proper because the recovery was enormous.[151] When litigation started a decade earlier, of course, no one knew that even $1 would be recovered. It was therefore a question of fact whether the parties would have given the remote possibility of a mega-fund recovery much weight when negotiating the lawyers' compensation *ex ante*. Because "five of the nation's largest merchants" agreed to pay more than 18 percent of their recoveries in fees, a negative answer enjoyed considerable support. In other words, there was reason to doubt that a sophisticated representative of the entire class would

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[148] In addition, a lawyer appealing a fee cut will be less likely to be accused of acting adversely to his/her clients in making such an appeal.

[149] *See In re* Nortel Networks Corp. Sec. Litig., 539 F.3d 129, 134 (2d Cir. 2008).

[150] 396 F.3d 96 (2d Cir. 2005)

[151] *Id.* at 122.

have used the possibility of a mega-fund recovery to bargain for a 6.5 percent fee.[152] (One might similarly doubt that experienced attorneys would ever have agreed to so low a contingent fee *ex ante*.)

The appellate court could have suggested, with greater plausibility, that a sophisticated bargaining agent would have insisted on a sliding scale of fees. This happened in the *Enron* litigation, in which the Regents of the University of California agreed *ex ante* to a scale that entitled class counsel to 10 percent of the first billion dollars recovered, 9 percent of the second billion, and 8 percent of any larger amount.[153] The plausibility of a fee scale being readily admitted, it is nonetheless true that we know of no scale that would have reduced the *Wal-Mart* fee into the $220 million range. The *Enron* scale would have generated a $302 million fee had it been applied to the $3.4 billion recovery in *Wal-Mart*. The fee awarded was almost $80 million less.

Neither the Second Circuit nor the district court connected the *Wal-Mart* fee award to the contingent percentage fee paid by any real client in any actual case. Both plucked the 6.511% figure out of thin air. Worse, the Second Circuit downplayed the importance of getting lawyers' incentives right. It remarked that "[i]n this case, the district court's decision in favor of protecting the instant class from an excessive fee award militates against awarding attorneys' fees based purely on economic incentives."[154] Plainly, both the Second Circuit and the district court missed the seemingly obvious point that fee awards based on terms that motivate lawyers to maximize recoveries cannot be excessive insofar as class members are concerned. Rather, such fees are precisely the ones that class

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[152] *Id.* at 123,

[153] *In re Enron Corp. Securities, Derivative & "ERISA" Litig.*, 586 F. Supp. 2d 732 (S.D. Tex. 2008). Given the eventual $7.2 billion recovery, the contractual fee scale entitled class counsel to $688 million. Judge Easterbrook has noted that sliding scales like these make sense in securities class actions: "Awarding counsel a decreasing percentage of the higher tiers of recovery enables them to recover the principal costs of litigation from the first bands of the award, while allowing the clients to reap more of the benefit at the margin (yet still preserving some incentive for lawyers to strive for these higher awards)." *See Silverman*, 739 F.3d at 959.

[154] Wal-Mart Stores, Inc. v. Visa U.S.A., Inc., 396 F.3d at 123.

members would willingly and rationally agree to pay *ex ante* when hiring lawyers directly.[155]

The analysis just presented appears to have altered the thinking of Judge Gleeson, who was the district court judge in the *Wal-Mart* case that settled in 2003.[156] When awarding fees ten years later in the *Payment Card Interchange Fee* litigation, which settled for $5.7 billion in 2013, he repeatedly emphasized the need for "concrete guideposts" that would secure lawyers' financial incentives, and he explicitly took market rates into account.[157] Thus, he adopted a declining scale of marginal percentages because "sophisticated clients often require counsel to accept a smaller percentage of a recovery as the size of the recovery increases."[158] He also set the percentages at levels that, in his assessment, resembled those sophisticated clients employ, starting with 33% of the first $10 million recovered and declining steadily across identified ranges until reaching a low of 6% on the last $1.7 billion.[159] Summing the marginal increments, Judge Gleeson concluded that a 9.56% fee was warranted, a percentage very close to the agreement-based fee approved in *Enron*.[160]

Judge Gleeson in his 2014 opinion also twice endorsed the principle of setting fees in class actions in advance. In the first passage on this subject, he noted that "[i]n PSLRA litigation, a lead plaintiff may bargain with lead counsel

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[155] A source of arbitrariness that is hard to document but unquestionably important is the vast difference between federal judges' meager salaries and the enormous amounts lawyers earn when class actions yield mega-fund recoveries. How can federal district court judges, who earn less than $200,000 per year, not be envious when lawyers whose credentials may be no better than theirs, and who may work no harder than they do, pocket tens or hundreds of millions in fees in a single case?

[156] In re Visa Check/Mastermoney Antitrust Litigation, 297 F.Supp.2d 503 (E.D.N.Y. 2003). The $5.7 billion is after reductions for opt outs. *Id.* at ___.

[157] *In re* Payment Card Interchange Fee and Merchant Discount Antitrust Litigation, 991 F.Supp.2d 437 (E.D.N.Y. 2014) (awarding fees in connection with settlement given final approval in 986 F.Supp.2d 207 (E.D.N.Y. 2013)). Judge Gleeson mentioned "concrete guideposts" in 991 F.Supp.2d at 442 ("The law sets only minimal constraints on fee awards. Within those constraints, it offers no concrete guideposts."); and at 444 ("Despite the absence of concrete guideposts . . . ."). See also *id.* at 446 ("In my view, a guidepost is solely needed.").

[158] *Id.* at 444.

[159] *Id.* at 445.

[160] *Id.* at 445. *See also* In re Enron Corp. Securities, Derivative & "ERISA" Litig., 586 F. Supp. 2d 732, __ (S.D. Tex. 2008).

over fees."[161] Then, after adding that in the Second Circuit "a district court need not defer to such a bargain when actually making the award at the end of litigation," he observed that "[i]t would be helpful to have a negotiated benchmark from which to work" and said that "in a future case, [he would] consider employing [his] authority under Rule 23(d) to require such negotiation – perhaps with court-appointed counsel to represent a cross-section of the plaintiffs for the purposes of the fee negotiation."[162]

Obviously, we agree that a negotiated benchmark set by the lead plaintiff and its chosen counsel at or near the start of a securities class action would both make the court's eventual fee award more objective and give class counsel better incentives during the litigation. We dissent, however, from Judge Gleeson's proposal to appoint counsel to negotiate on behalf of the class, partly because the PSLRA vests lead plaintiffs with this responsibility and partly because appointed, temporary counsel would have no obvious interest in obtaining fee terms that are optimal for a class.

The second time Judge Gleeson discussed *ex ante* fee setting in his 2014 opinion, he zeroed in on lawyers' incentives:

> A final reason to employ the schedule methodology advanced here is for the benefit of counsel in future cases. If plaintiffs' lawyers know in advance (that is, at the start of a case) that such a schedule will be used, it will alter their thinking for the better. A graduated schedule ensures that the greater the settlement, the greater the fee, and it therefore avoids certain incentive problems that come from simply scaling an overall percentage down as the size of the fund increases. *See In re Synthroid Mktg. Litig.*, 264 F.3d 712, 721 (7th Cir. 2001) (citing cases, and noting that the graduated schedule ensures that "attorneys' fees never [go] down for securing a larger kitty, and counsel always [have] an incentive to seek more for their clients"). Using such a schedule as a guideline for future cases – from which departures based on case-specific circumstances may of course be warranted – will permit counsel to make reasonable decisions *ex ante* in those future cases.[163]

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[161] *Id.* at 443.

[162] *Id.*

[163] 991 F.Supp.2d at 446 (footnote omitted).

This is both exactly right and a significant improvement on the lack of concern about attorney incentives expressed in the *Wal-Mart* opinions.[164] When setting fees, judges should keep uppermost in their minds that they are creating incentives for attorneys. Realizing this, their only object should be to select fee terms that motivate lawyers to maximize net recoveries for claimants. Choosing a fee arrangement for any other reason would disserve class members by discouraging their lawyers from representing them zealously, thereby creating a serious risk that class members would be denied due process of law.

In our nationwide study, we found that judges usually grant fee requests in full and are somewhat more deferential when requests are based on *ex ante* agreements. Readers may therefore wonder why we think the current fee-setting process lacks objectivity and is rife with arbitrariness. Don't judges mostly do what we think they should do, by regularly approving fee requests supported *ex post* by lead plaintiffs? No—we are concerned that judges currently act improperly both when they grant fee requests and when they cut them. In most of the 85 percent of cases where judges awarded the fees that class counsel requested, they neither set fees up front, made any effort to determine whether lead plaintiffs bargained zealously on behalf of the investors they represented, nor compared requested fee percentages to prevailing market rates. Consequently, in these cases it is hard to know whether fee awards were too large, too small, or about right. The only thing one can be confident of is that, while the lawsuits were on-going, the lawyers' incentives were deficient because their compensation terms were vague. In the remaining 15 percent of the cases where judges cut fee requests, the same three problems were present. Fee reductions only made the fact of arbitrariness clearer by highlighting defects in the way judges think about fee regulation. And, as our data show, those fee reductions were random.

In nearly all cases in our nationwide six-year study, judges appear to have misunderstood the role that *ex ante* fee agreements between lead plaintiffs and lawyers should play in the fee-setting process under the PSLRA. Usually, judges displayed no interest in the content or existence of such *ex ante* agreements. Judges did not require lead plaintiff candidates to submit them as part of the

[164] In re Visa Check/Mastermoney Antitrust Litigation, 297 F.Supp.2d 503 (E.D.N.Y. 2003), *aff'd* Wal-Mart Stores, Inc. v. Visa U.S.A., Inc., 396 F.3d 96 (2d Cir. 2005).

application process, and the candidates rarely volunteered them. Similarly, only a handful of judges expressed interest in these agreements when evaluating class counsel's request for fees at the time of settlement. We are left to surmise that most federal district court judges have failed to grasp that the core implication of the PSLRA is that a lead plaintiff is supposed to act as a zealous bargaining agent for a class, and that Congress therefore assigned lead plaintiffs weightier responsibilities than named plaintiffs in other class actions are normally required to bear.[165] To ensure that lead plaintiffs do the job they sign up for, judges should obtain and evaluate *ex ante* fee agreements routinely at the outset of the case.

V. CONCLUSION

Every year, federal judges presiding over securities class actions award hundreds of millions of dollars in attorneys' fees. Until now, little has been known about how these awards are actually made. Our nationwide, six-year empirical study is the first to peer carefully, comprehensively, and systematically inside the black box of the fee award process. Sadly, our findings suggest that the current practice of *ex post* fee setting is both deeply flawed and not consistent with Congress's goals when adopting the PSLRA twenty years ago. We have therefore proposed a set of procedural reforms that courts can easily adopt and that we believe will make fee-setting in securities class actions more transparent, more compatible with the normative goals of the PSLRA, and ultimately more beneficial for class members, class counsel, and the general public.

In the meantime, we hope this Article will encourage potential lead plaintiffs and the attorneys who represent them to privately resolve fee-related matters when litigation begins, and to present their *ex ante* fee agreements to courts for *in camera* review when requesting control of class litigation. Doing so should result in fee awards at the time of settlement that are more predictable and

[165] Even so, one could argue (1) that judges should also consider *ex ante* fee agreements when deciding whether a lead plaintiff candidate and proposed class counsel are adequate under Rule 23(a) of the Federal Rules of Civil Procedure, and (2) that judges should make more frequent use of the power to set fees up front recognized in Rule 23(g).

more likely to be grounded in prevailing market rates than in the predilections and biases of individual judges.

Finally, we hope that our findings will cause judges who undertake to award attorneys' fees (or to review such fee awards on appeal) in securities cases and class actions of other types to think more deeply and carefully about how best to perform this task. We also hope that academic researchers will contribute to this important judicial work by undertaking empirical studies along the lines of the one presented here.

Table 1

Summary Statistics (Continuous Variables)

	Obs.	Mean	Std. Dev.	Median	Min.	Maximum
Fee Request	427	0.246	0.071	0.250	0.000	0.340
Fee Award	430	0.238	0.072	0.250	0.000	0.340
Settlement (Millions)	431	51.800	165.000	10.600	0.352	2,420.000
Case Age (Years)	430	4.000	2.120	3.511	1.006	13.778
Judge Frequency	434	2.779	1.955	1.000	1.000	8.000

Note: Settlement data are in constant 2012 dollars.

Table 2

Summary Statistics (Categorical Variables)

	Obs.	Yes	Percent	No	Percent
LP Competition	431	305	70.77%	126	29.23%
Ex Ante Agreement LP Motion	386	41	10.62%	345	89.38%
Ex Ante Agreement LP Order	405	21	5.19%	384	94.81%
Ex Ante Agreement Fee Request	422	74	17.54%	348	82.46%
Ex Ante Agreement Fee Award	428	27	6.31%	401	93.69%
Public Pension LP	431	146	33.87%	285	66.13%
Other Institution LP	431	152	35.27%	279	64.73%
Individual LP	431	200	46.40%	231	53.60%
High Volume District	434	209	48.16%	225	51.84%
Objection	424	93	21.93%	331	78.07%
Fee Cut	424	62	14.62%	362	85.38%
High Volume Judge	434	135	31.11%	299	68.89%
One Opinion	434	161	37.10%	273	62.90%

Note: The frequencies for lead plaintiff types exceed 100% because cases often feature more than one type of lead plaintiff.

Table 3

Rationales for Judicial Fee Reductions

Rationale	Number (Frequency)
The requested fee is "too large"	25 (40.32%)
The requested fee is "too large given the work performed by the attorneys"	22 (35.48%)
The requested fee is "too large given lead counsel's actual risk of non-recovery"	19 (30.65%)
Requested fee is "out of line with fees in similar cases"	20 (32.26%)
Requested fee fails a lodestar cross-check	21 (33.87%)
The court cannot rely on the market for setting attorneys' fees	3 (4.84%)
Requested fee not the result of arm's length bargaining	1 (1.61%)

Table 4
Regressions for Fee Requests

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Settlement	-0.007**	-0.001	-0.001	-0.001	-0.001	-0.001	-0.001
	(0.003)	(0.004)	(0.005)	(0.004)	(0.004)	(0.004)	(0.005)
Competition	-0.014***	-0.013***	-0.013***	-0.013***	-0.013***	-0.014***	-0.014***
	(0.002)	(0.002)	(0.002)	(0.002)	(0.002)	(0.002)	(0.002)
Public Pension	-0.048***	-0.043***	-0.048***	-0.048***	-0.048***	-0.048***	-0.048***
	(0.008)	(0.011)	(0.009)	(0.008)	(0.009)	(0.009)	(0.008)
Other Institution	-0.001	-0.003	-0.002	-0.003	-0.002	-0.002	-0.002
	(0.004)	(0.004)	(0.004)	(0.004)	(0.004)	(0.004)	(0.004)
Ex Ante Agreement	-0.057***	-0.043***	-0.054***	-0.054***	-0.056***	-0.056***	-0.056***
	(0.014)	(0.011)	(0.012)	(0.012)	(0.013)	(0.013)	(0.014)
Case Age (Years)	-0.003*	-0.003*	-0.003**	-0.003**	-0.003**	-0.003**	-0.003**
	(0.001)	(0.002)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
High Volume District	-0.028***	-0.028***	-0.022***	-0.011**	-0.024***	-0.019***	-0.030***
	(0.005)	(0.005)	(0.006)	(0.004)	(0.006)	(0.004)	(0.006)
Settlement x High Volume		-0.011**	-0.011**	-0.010**	-0.011**	-0.011**	-0.011**
		(0.004)	(0.004)	(0.004)	(0.004)	(0.004)	(0.004)
Public Pension x Ex Ante		-0.029					
		(0.032)					
Judge Frequency			-0.005***	-0.002			
			(0.001)	(0.002)			
High Vol. x Judge Freq.				-0.004*			
				(0.002)			
High Volume Judge					-0.015***	-0.004	
					(0.005)	(0.006)	
High Vol. Judge x. High Vol.						-0.017*	
						(0.009)	
One Opinion							0.005
							(0.007)
One Opinion x High Vol.							0.016*
							(0.007)
Constant	0.307***	0.307***	0.318***	0.313***	0.312***	0.311***	0.309***
	(0.003)	(0.007)	(0.004)	(0.005)	(0.004)	(0.004)	(0.006)
Observations	419	419	419	419	419	419	419
R-squared	0.414	0.434	0.441	0.444	0.436	0.439	0.434

Robust standard errors (clustered by Circuit) are in parentheses.

*** p<0.01, ** p<0.05, * p<0.1

Table 5
Regressions for Fee Awards

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Settlement	-0.007**	-0.002	-0.002	-0.002	-0.001	-0.002	-0.002
	(0.003)	(0.004)	(0.005)	(0.004)	(0.005)	(0.004)	(0.005)
Competition	-0.009**	-0.008***	-0.008***	-0.009***	-0.009***	-0.009***	-0.010***
	(0.003)	(0.002)	(0.002)	(0.002)	(0.003)	(0.003)	(0.003)
Public Pension	-0.043***	-0.037***	-0.043***	-0.043***	-0.043***	-0.043***	-0.043***
	(0.008)	(0.010)	(0.008)	(0.008)	(0.009)	(0.009)	(0.008)
Other Institution	-0.001	-0.003	-0.003	-0.003	-0.002	-0.003	-0.003
	(0.004)	(0.004)	(0.004)	(0.004)	(0.004)	(0.004)	(0.004)
Ex Ante Agreement	-0.054***	-0.038***	-0.051***	-0.051***	-0.053***	-0.053***	-0.053***
	(0.014)	(0.011)	(0.013)	(0.012)	(0.014)	(0.013)	(0.014)
Objection	-0.004	-0.003	-0.006	-0.006	-0.006	-0.006	-0.005
	(0.007)	(0.008)	(0.008)	(0.008)	(0.007)	(0.007)	(0.008)
Fee Cut	-0.038***	-0.039***	-0.039***	-0.040***	-0.039***	-0.040***	-0.039***
	(0.006)	(0.005)	(0.006)	(0.006)	(0.006)	(0.006)	(0.005)
Case Age (Years)	-0.002	-0.002	-0.003*	-0.003*	-0.003*	-0.003*	-0.003*
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
High Volume District	-0.031***	-0.031***	-0.025***	-0.014***	-0.027***	-0.022***	-0.033***
	(0.005)	(0.005)	(0.005)	(0.004)	(0.005)	(0.004)	(0.006)
Settlement x High Volume		-0.010**	-0.009*	-0.009*	-0.010**	-0.009*	-0.009*
		(0.004)	(0.004)	(0.004)	(0.004)	(0.004)	(0.004)
Public Pension x Ex Ante		-0.033					
		(0.031)					
Judge Frequency			-0.004***	-0.002			
			(0.001)	(0.002)			
High Vol. x Judge Freq.				-0.004*			
				(0.002)			
High Volume Judge					-0.017***	-0.006	
					(0.004)	(0.006)	
High Vol. Judge x. High Vol.						-0.017*	
						(0.008)	
One Opinion							0.004
							(0.007)
One Decision x High Vol.							0.016**
							(0.007)
Constant	0.299***	0.298***	0.310***	0.305***	0.305***	0.303***	0.301***
	(0.003)	(0.006)	(0.004)	(0.005)	(0.003)	(0.003)	(0.006)
Observations	417	417	417	417	417	417	417
R-squared	0.398	0.415	0.420	0.423	0.418	0.420	0.415

Robust standard errors (clustered by Circuit) in parentheses.

*** p<0.01, ** p<0.05, * p<0.1

Table 6

Logit Regression for Judicial Fee Reductions

	Cut
Settlement	0.074***
	(0.021)
Competition	-0.029
	(0.036)
Public Pension	-0.130***
	(0.045)
Other Institution	-0.023
	(0.037)
Ex Ante Agreement	-0.126**
	(0.056)
High Volume District	0.120***
	(0.043)
Case Age (Years)	-0.014
	(0.009)
Objection	0.026
	(0.041)
Settlement x High Volume	-0.038*
	(0.022)
High Volume Judge	0.138**
	(0.057)
High Vol. Judge x High Vol.	-0.159**
	(0.071)
Observations	418
Pseudo R-squared	0.113

Table 5 reports average marginal effects for the independent variables with delta-method standard errors in parentheses.

*** p<0.01, ** p<0.05, * p<0.1

FIGURE 1

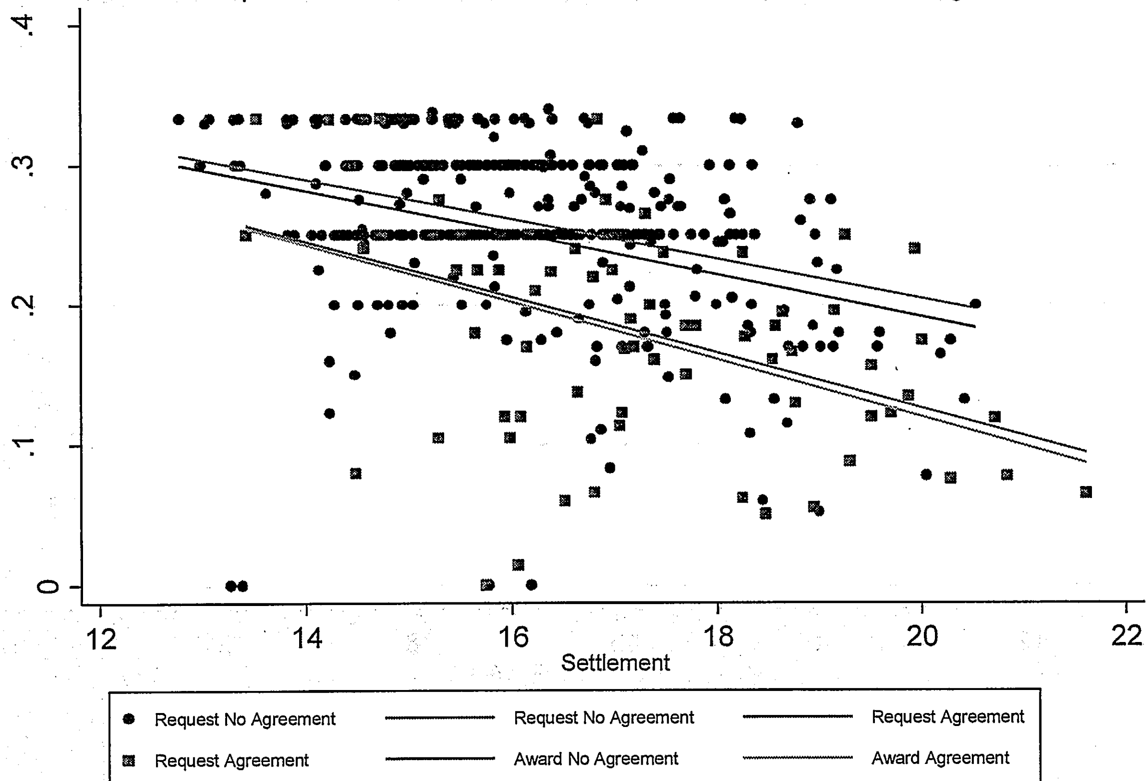
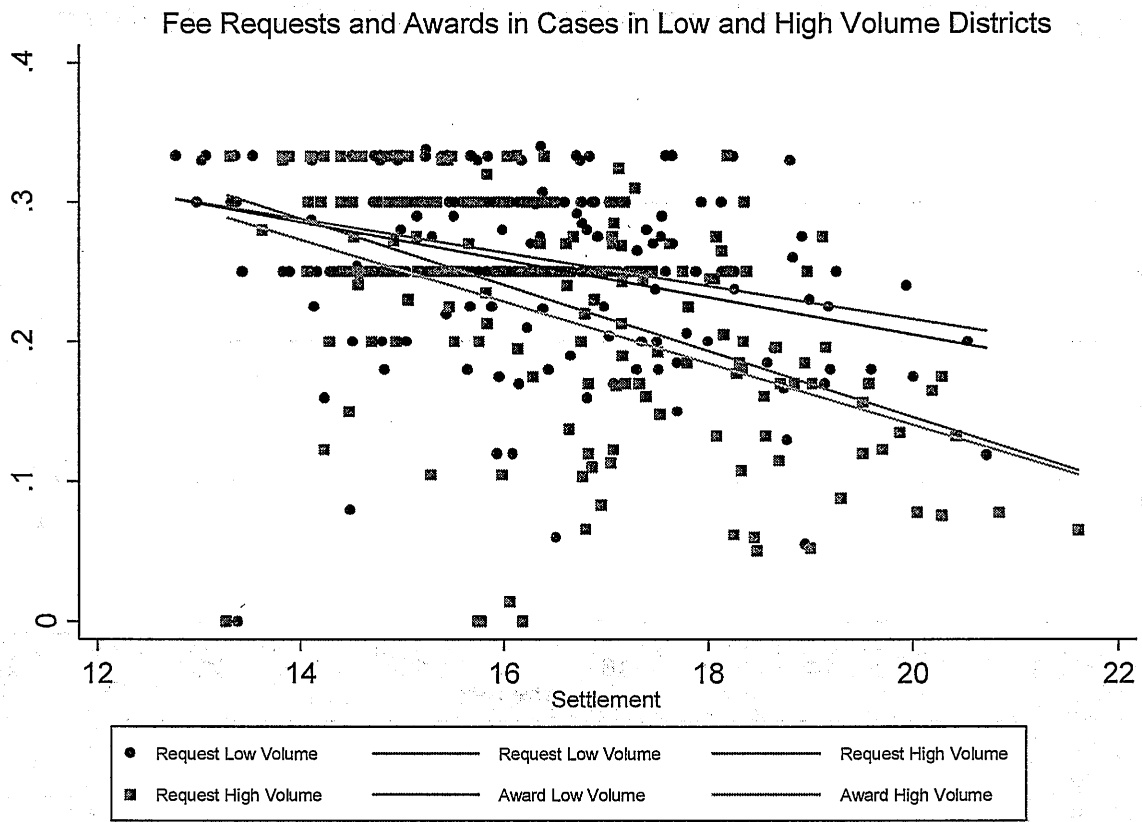
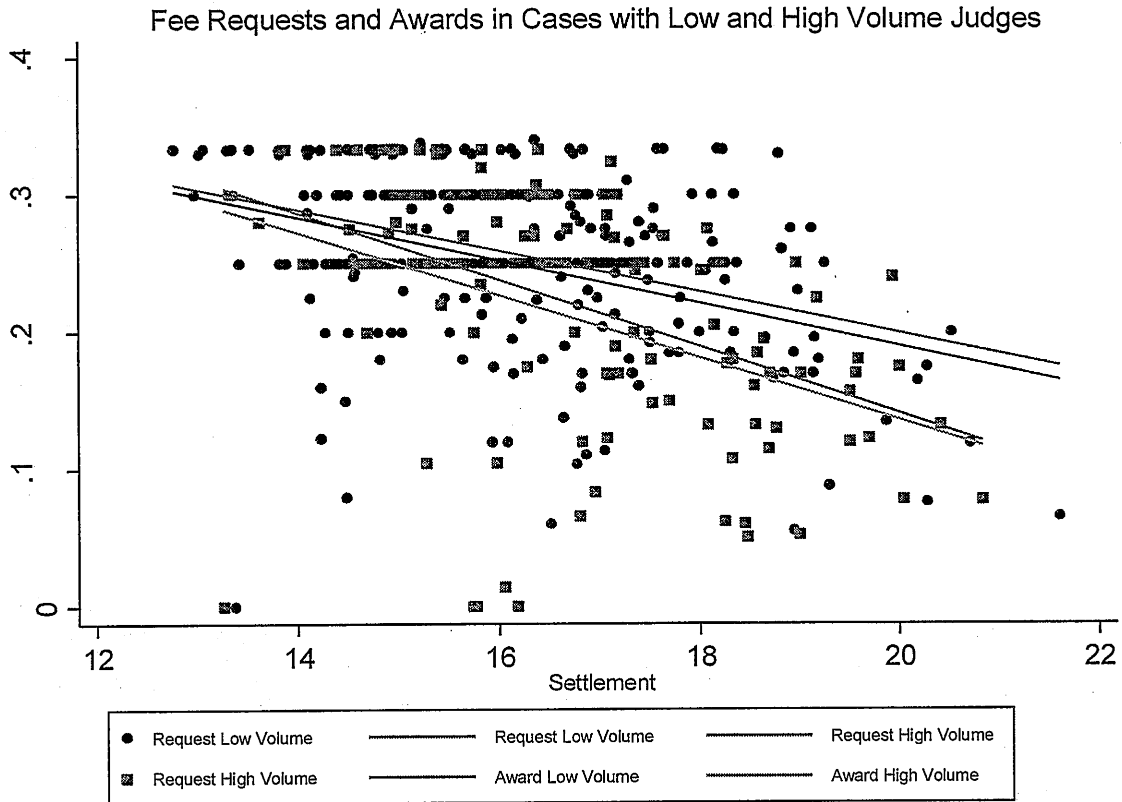


Figure 2



Settlements are log-transformed and in constant 2012 dollars.

Figure 3



Settlements are log-transformed and in constant 2012 dollars.