The Shareholder Wealth Effects of Delaware Litigation*

Adam B. Badawi † and Daniel Chen ‡

† School of Law, Washington University in St. Louis

‡ Toulouse Institute for Advanced Study

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Abstract

We collect data on the record of every action in over one thousand cases involving public companies from 2004 to 2011 in the Delaware Court of Chancery, which is the leading court for corporate law disputes in the United States. We use these data to estimate how markets respond to Delaware litigation events and characteristics such as case initiations, procedural motions, case quality, and judge identity. We find that negative abnormal returns are associated with the filing of derivative and contract cases, but we observe little effect associated with the filing of the average merger challenge. When we include measures of case quality, we see that higher quality cases increase the expected impact of derivative and contract litigation on firm value. We also develop evidence that tactics associated with multijurisdictional litigation are associated with a weakened impact of litigation on firm value. This evidence is consistent with the belief that the presence of litigation in another jurisdiction allows defense lawyers to bid down competing groups of plaintiffs' lawyers during settlement negotiations. Finally, we show

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that abnormal returns are not associated with information on judicial assignment at the time of case filing, nor are they associated with judge identity at case resolution. These results suggest that the judicial impact on shareholder wealth at the time of judicial assignment and the time of case termination is too small to be statistically detected.

1 Introduction

The effects of litigation on firm value has long been a central focus for scholars of law and business. These inquiries have been limited by the difficulty of collecting large, uniform samples and the lack of detailed information about the type of cases, motions, announcements, and key milestones that constitute the lifetime of a case. In this study, we significantly expand the depth of the information available by collecting electronic docket data from the Delaware Court of Chancery, which is the leading court for corporate disputes in the United States.[1] The granular nature of the docket data allow us to specify event windows with precision and it allows us to extract information about procedural tactics, litigation intensity, and judicial assignment in these cases. We use this additional information to analyze how these case features affect firm value.

We develop three primary results about the impact of Delaware corporate litigation on shareholder wealth. First, we examine how the filing of different types of complaints affects shareholder wealth. Our evidence shows that market participants appear to draw stronger inferences from the filing of corporate law cases that have high initial barriers to moving forward. For example, we demonstrate a negative effect on firm value associated with the filing of a derivative case. These cases, in which shareholders sue directors on behalf of the firm, require that plaintiffs show at the outset that directors are too conflicted to investigate the alleged wrongdoing. Overcoming this threshold is particularly difficult in an era where the majority of directors on public company boards are independent. Indeed, in the absence of a compelling showing that a majority independent board was complicit in the alleged wrongdoing,

[1] More than 50% of all public firms are incorporated in Delaware, while New York, the state with the second highest share, attracts fewer than 5% of public firms (Daines, 2001). The judges of the Chancery Court are well-versed in corporate law and their speed and effectiveness is one of the reasons that has been credited for Delaware's success in attracting incorporations (Kahan, 2006).

Delaware courts will typically dismiss the suit. We hypothesize that this high initial barrier should lead plaintiffs to conduct more pre-suit investigation. This investigation may uncover information that is not known to the market as a whole and, as a consequence, the filing of the suit may alert market participants that the case may have merit. Derivative cases with merit have the potential to be costly and disruptive as there have been a number of historically large damage awards–and related attorney fee awards– in stock option backdating and insider trading derivative cases during our sample period (Cheffins et al., 2012). Our evidence of a negative effect associated with derivative case filings supports this account. We buttress this claim by showing that the negative effect increases with our proxies for case quality, which include the appearance of out-of-state counsel in the matter and the total number of cases filed.

Acquisition-related cases, which are another important segment of Chancery Court corporate disputes, tell another story. These disputes are, at this point, automatic in the wake of a merger or acquisition (Cain and Davidoff, 2012). Unlike derivative suits, merger cases do not have the high initial threshold to proceeding. Defendant boards will typically settle these suits rather than fight them because, even in cases with little merit, it is difficult to obtain a dismissal prior to the closing of the transaction. As a consequence, the average case filing of this sort is unlikely to provide new information to the market. Our data confirm this expectation as we show that the average merger case filing produces no statistically detectable abnormal return.

Our second primary result develops evidence on the consequences of multijurisdictional litigation. Scholars debate whether this type of competition sharpens the effectiveness of corporate litigation or blunts it by creating a race to settle. Litigating a single matter across multiple jurisdictions can create a "reverse auction," (Coffee, 1995) which allows defendant firms to bid competing groups of plaintiffs down in an effort to obtain a relatively cheap global settlement. Evidence consistent with this mechanism would suggest other contexts, such as the ability to file multiple class action suits, e.g., in Australia in the context of third-party litigation funding, for the same action can also result in less deterrence than policymakers might think (Chen, 2015).

We use the presence of a motion to expedite–a tactic that we show correlates with the existence of a case in another jurisdiction–to assess the impact of this type of litigation. The analysis suggests that multijurisdictional liti-

gation may dilute the impact of derivative cases and and acquisition-related cases. This evidence supports the concern that litigating a single matter across multiple jurisdictions creates a "reverse auction."

Our final question builds on the econometric investigations of decision maker assignment. We seek to examine if judges in cases most closely followed by markets have direct effects the moment they are assigned rather than the moment when the decisions are revealed. This kind of analysis is typically not possible in other settings. (Belloni et al., 2012; Chen and Yeh, 2014; Chen and Lind, 2014; Chen and Sethi, 2011). The structure of the Court of Chancery–which has a large corporate docket, a small number of judges, and faces significant scrutiny from the business press, equity analysts, and merger arbitrageurs–presents an ideal environment for this type of analysis. We find little evidence that the market accounts for judicial identity either at the time of filing or at the time of case resolution.

While the focus of the paper is on Delaware, this study offers some insights potentially capable of greater generalization. Haslem (2005) is the only paper with a comparable sample size that we are aware of that also examines the effects of litigation on firm value. In that paper, he collects 737 cases from across the U.S. and finds that the market views settlement as a negative outcome on average. He suggests that firms with weak corporate governance settle litigation more quickly, and the market reacts more negatively to settlements involving firms with higher agency costs. We find some evidence consistent with this hypothesis.

The paper proceeds as follows. Part II reviews the literature on corporate litigation and draws on that literature to develop our hypotheses. Part III describes the sample used in this study and reports descriptive statistics. Part IV examines the wealth effects associated with the litigation and analyzes the potential determinants of those effects. Part V concludes. Appendix A provides the definitions of the variables used in the regressions and Appendix B details our investigation of the association between motions to expedite and multijurisdictional litigation.

2 Background and Hypothesis Development

In this section we discuss our expectations about the effect of case types and case features on firm value. We develop these hypotheses by drawing on the

existing literature on corporate litigation. Before doing so, however, we provide some brief comments on the Delaware Chancery Court's docket. The equitable jurisdiction of the Chancery Court means that certain types of cases filed by and against firms that are incorporated in Delaware have the option of being litigated in the Chancery Court. Most of the that involve public corporations fall into one of three categories: (1) derivative lawsuits; (2) shareholder class actions that challenge an acquisition; and (3) inter-firm contract disputes (Badawi, 2013). We limit our data to cases that fall into these categories.

2.1 Case Types and Expectations

Among our three categories of lawsuits— derivative cases, merger class actions, and contract cases—the likelihood of a lawsuit when circumstances might produce one varies substantially. We discuss our hypotheses for each of type of these cases below.

2.1.1 Derivative Lawsuits

Studies from 1980s and early 1990s find little relationship between the filing of derivative lawsuits and firm value. A pioneering paper by Romano (1991) shows no significant effect on stock price associated with the filing of a derivative lawsuit in 66 lawsuits.[2] Likewise, she finds no significant effect when the lawsuit gets reported in the Wall Street Journal, which occurs, on average, two weeks after filing. This null effect may be due to the small monetary awards that went to shareholders in derivative suits at that time. She finds that derivative settlements are, on average, only 0.5 percent of firm assets. A related study by Fischel and Bradley (1985) looks at the effect of court rulings on motions to dismiss in derivative suits. They find a significant negative effect associated with dismissals and an insignificant positive effect when courts decline to dismiss suits, but do not find a significant effect around the filing date and conclude that any aggregate effect is likely to be negligible. As Bhagat and Romano (2002) point out, this finding is consistent with the negligible effects that Romano finds in her 1991 study. The conventional wisdom at the time was consistent with these studies: derivative lawsuits were thought to be largely meritless and involve small recoveries (Armour, Black,

[2]West (2001) conducts a more recent investigation of derivative lawsuits in Japan. Like the other studies, he finds no stock market effect associated with the filing of these cases.

Cheffins, 2012). To put this another way, the ease of showing demand futility at this time allowed meritless suits to produce a settlement for plaintiffs' lawyers. Consequently, these cases got filed even when they were meritless.

In the time since these studies, however, there have been sizable shifts in the makeup of boards and those changes have had an impact on the expected value of filing a derivative lawsuit. To understand why this is so, it is helpful to provide some brief background on the demand futility requirement. To move forward in a derivative lawsuit, the plaintiffs must show either that they made a demand on the board that it investigate the alleged wrongdoing or that such a demand would be futile. A board's refusal to investigate a demand is subject to the extreme deference of the business judgment rule. In practice, this approach means that the lawsuit will fail unless there is a plausible claim that demand is futile (Bainbridge, 2004). To show that futility the plaintiffs must show that a majority of the directors were implicated in the alleged wrongdoing or that they cannot otherwise act independently. As the percentage of independent directors on boards grows, it becomes more difficult to show that demand would be futile.

There has been a marked increase in the use of independent directors over the past few decades. Some of the reasons for this shift include regulatory mandates such as the requirement under the Sarbanes-Oxley Act that public companies have audit committees comprised of only independent directors and NYSE and NASDAQ regulations that require that the majority of board members be independent (Davis Jr, 2008). As Thompson and Thomas (2004) suggest, the trend towards an increasing number of independent directors on corporate boards has likely made it made it more difficult to sustain a derivative lawsuit. As compared to the earlier era, it is substantially easier for the defendant directors to get a case dismissed quickly on the basis of demand futility. In order to get past this requirement, plaintiffs will typically need to make a substantial showing that the independent directors were complicit in the alleged wrongdoing. This evidence is likely to require investigation of information that is not available to the broader public. The filing of a derivative suit may thus signal the existence of a strong case and that information may be new for market participants. These stronger cases are, all else equal, likely to result in larger damages and larger attorney fee awards (Armour, Black, Cheffins, 2012). Moreover, the filing may also signal an undisclosed problem with existing management or the board's oversight over management. We

thus expect the filing of a case to bring new (and negative) information to the market.

H0A: *The filing of derivative lawsuits should, on average, result in a decrease in firm value.*

2.1.2 Merger Class Actions

Merger class actions are lawsuits filed by an individual or institutional shareholder on behalf of all shareholders. In the most typical scenario, a plaintiff alleges that the directors of the target company breached their fiduciary duties to the shareholders by failing to obtain a sufficiently high price for the target firm.[3] Over the course of our sample, the likelihood of a lawsuit in the wake of acquisition has increased from probable to a near certainty. Cain and Davidoff (2012) show that roughly 45% of mergers were the subject of lawsuits in 2005 to over 95% of mergers in 2011. Significant settlements or awards are quite rare in these cases–a large majority of these cases result in a settlement that involves additional disclosures about the merger to shareholders and a payment of relatively small fees to the plaintiffs' lawyers (Davidoff et al., 2015). Given the high frequency of these lawsuits and the low likelihood of a highly adverse result, we thus expect the filing of merger lawsuits to have little effect on firm value.

H0B: *Merger lawsuits are unlikely to have an effect on firm value at the time of filing.*

2.1.3 Contract Lawsuits

Contract lawsuits are probably even more difficult to anticipate than derivative lawsuits. Derivative claims often piggyback on government investigations. While that public information may not inform market participants of everything that would go into the decision whether to file a derivative lawsuit, there is some indication of the factual basis for the claim. That type of information about contract disputes is probably less likely to be public as disclosure requirements typically do not get triggered until after the commencement of

[3]These lawsuits will often have a higher chance of success if there is some degree of self-dealing in the transaction, such as a management-led buyout or the involvement of a controlling shareholder.

litigation. And even then, the firm must only disclose material litigation matters. For this reason, the announcement of a contract case is likely to bring new information to the market. The degree of the impact should, then, turn on the amount of expected liability and legal costs. For defendants both the expected liability and the legal costs should lead to a negative impact on firm value. For plaintiffs in these lawsuits, the possibility of a positive judgement and the likelihood of legal costs should have countervailing effects. While a rational firm would only pursue litigation if the costs outweighed the benefit, it is possible that the market may make a negative inference about the larger consequences that stem from the dispute such as the disruption of a long-term supply relationship that involves a number of firm-specific investments. For these reasons, we refrain from making a prediction about the effect of filing a contract lawsuit on firm value. We note, however, that previous research has not found an effect related to bringing a contract lawsuit (Bhagat et al., 1998).

H0C: *Contract lawsuits filed against a firm should result in negative abnormal returns.*

2.2 Indications of Lawsuit and Lawyer Quality

The filing of a lawsuit can provide new information that goes beyond the existence of the action. The complaint can allege information that may not be widely known or suspected. The identity of the lawyers bringing the case can signal the strength or weakness of the underlying allegations. And, should multiple cases get filed at approximately the same time, that fact can send a signal about the quality of the case. Some of these indicia of quality, such as the credibility of the allegations made in the complaint, would be very difficult to standardize and measure. Others, like the effect on stock price of each additional case that gets filed could, in theory, be captured given a broad enough window of time. The potential problem with such a metric is one that is well-known in event study methodology: expanding the length of event windows to capture the filing of an additional case—or some other indication of quality—makes it more difficult to attribute the abnormal return to any specific event.

Rather than expanding event windows, we assume that some measure of lawsuit and lawyer quality are observable upon filing. We assume that these observable measures are likely to manifest themselves in events—such as the

filing of additional lawsuits and the appearance of out-of-state counsel—that occur after the filing of the case. We expect that higher quality lawsuits will tend to increase the likelihood of plaintiff success. In the case of mergers, this prospect may increase share price because there is a higher expectation of an award to target shareholders (that would likely be paid by the acquirer). In the derivative and contract contexts, higher quality should lead to larger chances of liability and, hence, a decrease in share price.

In our analysis, we use two indicators of potential quality. The first of these indicators is the number of cases filed in response to the same set of facts as a measure of case quality. We expect this variable to have a positive relationship with case quality. The more likely there is to be a substantial recovery–which should be a function of both the underlying facts and the amount at stake–the more interest a case should draw from plaintiffs' attorneys. Indeed, Cain and Davidoff (2013) use the number of cases to control for case quality but they do not do so in the context of an event study. Note that we do not expect this variable to be a perfect proxy for the strength of a case. Lawyers could base the decision to file a case, in part, on media coverage of the underlying facts and that coverage may have little relationship with case quality. Nevertheless, we expect that, on average, the decision to file will be driven by expected recovery and that potential for recovery should have a positive relationship with the quality of a case.

H1A: *The number of complaints filed in response to a similar set of facts should have a positive relationship with the prospect of liability.*

Our second measure is more novel. We code whether the case involves at least one motion for an out-of-state lawyer to appear. This procedural device, known as a pro hac vice motion, allows a lawyer who is not admitted in Delaware to be admitted for the purpose of a single case. The Chancery grants these motions as a matter of course in nearly all cases (Armour et al., 2012). We speculate that the presence of an out-of state lawyer is an indication of the difficulty of the case. While a firm can mount a high-quality defense by relying on the deep expertise of the Delaware defense bar, a complex case will typically include the involvement of a firm's regular counsel and that counsel is usually from out of state. That regular counsel may be actively involved in the case or may only be an observer, but our review of the dockets suggests that an intensely litigated case almost always involves at least one motion to

admit an out-of-state counsel.[4] This observation is borne out in the docket data. Cases that include at least one motion to admit out-of-state counsel average about 163 docket entries over the course of litigation. Cases without such a motion, however, average roughly 30 docket entries.

There is substantial variation in the use of pro hac vice motions. At least one of these motions gets filed in about three-quarters of merger cases and two-thirds of derivative cases. We hypothesize that the cases without such a motion are likely to be of particularly poor quality and we speculate that this quality is observable at the time of filing. Market participants may be able to infer this quality from the identity of the lawyers that file the case or from the underlying allegations. This observation is consistent with existing evidence that stock prices react to the reputation of the plaintiffs' lawyers in merger class actions (Badawi and Webber, 2015).

H1B: *The eventual filing of at least one pro hac vice motion should have a positive relationship with the prospect of liability at the time of filing.*

2.3 Indications of Multijurisdictional Litigation

Representative lawsuits, such as acquisition-related class actions and derivative cases, sometimes involve competing litigation in multiple jurisdictions.[5] Litigation in another forum creates the risk that a settlement in the alternative jurisdiction will have a preclusive effect on all other cases. Corporate law scholars have suggested that this dynamic can create incentives for a "reverse auction" among plaintiffs' attorneys (Coffee, 1995; Griffith and Lahav, 2013). As these different groups negotiate with the defendant, they may be willing to make lower offers with respect to damage and attorneys' fees in order to ensure that they get something for their effort. All else being equal, the terms of these settlements should be lower than if the litigation were proceeding in a single jurisdiction.[6]

[4]Because there are many high quality lawyers in Delaware, we choose not to use the total number of pro hac vice motions in a case as an explanatory variable. A high quality case where a Delaware firm leads the defense may involve a relatively small number of pro hac vice motions, while a medium quality case directed by an out-of-state firm may involve a high number of these motions. As we explain below, we expect cases where no out of state counsel appear at all, to be of especially low quality.

[5]For corporate law claims, plaintiffs may usually file a case in the state where firm locates its headquarters or in the state of incorporation.

[6]One might object that there is an inconsistency between our prediction that multiple cases will tend to increase the potential for liability while multijurisdictional cases may

Complete data on the existence of multijurisdictional litigation is difficult to collect because parties do not always disclose these lawsuits in their securities filings. As a proxy for the existence of multijurisdictional litigation, we use the presence of a motion to expedite in the docket. If a court grants this motion, discovery will begin quickly and the court may issue rulings in relatively short order. Progression of a case on an expedited basis can make judges elsewhere reluctant to approve a settlement and may thus diminish incentives for a reverse auction. Conversations with Delaware attorneys suggest that plaintiffs often use motions to expedite for this precise purpose.[7] There is some empirical evidence to support this association. Badawi (2013) shows that, in the years where there is an increase in multijurisdictional merger litigation, there is also an increase in motions to expedite in Delaware merger cases. To further confirm this connection, we verify whether there is related litigation occurring in another jurisdiction for a subset of the cases of our sample. We present those results in Appendix B, which documents a very strong positive association between multijurisdictional litigation and motions to expedite in merger litigation and a relatively strong positive association in derivative cases.

We observe substantial variation in the use of motions to expedite. In merger litigation, the cases involve a motion to expedite in about 57% of cases and in derivative cases, plaintiffs file a motion to expedite in roughly one quarter of the cases. To the degree these motions are indications of lawsuits going on elsewhere, that competing litigation should be observable to the market. We thus expect the relationship between the effect on firm value at the time of filing and the presence of a motion to expedite to be a measure of the effect of multijurisdictional litigation. Simultaneous disputes in multiple jurisdictions should tend to dilute the expected effect of the lawsuit. In the case of deriva-

decrease the prospect of liability. If cases in multiple jurisdictions produce a reverse auction, shouldn't that also happen when multiple cases get filed in the same jurisdiction? This is unlikely to occur because, within each jurisdiction, there is a designated group of lead counsel that has the authority to control the case on behalf of all plaintiffs who have filed a case in that jurisdiction. The lead plaintiffs' counsel controls the negotiations with the defendants and thus the non-lead counsel cannot undercut the lead counsel by making a lower offer to the defendant.

[7]To be sure, there are other reasons why a party might a motion to expedite. Perhaps the leading alternative motivation is that the closing date of a merger is approaching and expedited proceedings will enhance the credibility of a plaintiffs' attempt to enjoin the merger. We do not, however, expect the market to be able to predict this dynamic at the time of lawsuit filing. The presence of litigation elsewhere should, however, be observable.

tive litigation, this would mean less negative effect on firm value to reflect the chance of a lower judgement. For merger-related litigation, the effect should be a less positive effect due to the diminished chance of a significant payment to the shareholders of the target firm, who are typically the plaintiffs in these cases and are suing the board of the target firm.[8]

H2: *The presence of a motion to expedite in representative cases should dilute the expected consequences of a finding of liability.*

2.4 Judicial Identity

The docket includes information on the Chancellor or Vice-Chancellor assigned to the case. We use this information to assess the wealth effect of a particular judge being assigned to a case at the time the judge is revealed and at the time the case is decided. The theory that motivates this analysis is the possibility that the market prices expectations about the effect a judge will have on a case. For example, if a judge has a reputation for being particularly sympathetic to shareholder plaintiffs in merger suits, all else being equal, one should expect the stock price to reflect the expectation that the merger price will be adjusted upward.

Our ability to use this dataset to measure the stock market effect of judicial assignment appears to be novel. There is, however, a related literature that attempts to develop empirical measures of judicial quality and prestige. Perhaps the most prominent of these measures is the degree to which judges get cited in other jurisdictions. Choi, Gulati, Holman, and Posner (2009; 2011) have used this metric to rank judges. These authors sometimes use citations to courts outside the home state, district, or circuit as the relevant measure on the theory that these citations are a better measure of influence because, by definition, the courts citing the opinions are not bound by them. These same authors have also used productivity and judicial independence–measured by the willingness of a judge to disagree with judges nominated by a President or governor of the same political party–as alternative metrics to rank judges (Choi and Gulati, 2005; Choi et al., 2011, 2009).[9]

[8]Recall that a successful resolution in a merger-related case is an increase in merger consideration to the class of shareholder plaintiffs. This payment is typically funded by the buyer. That prospect should, all else equal, increase abnormal returns. The presence of multijurisdictional litigation should mute that effect and thus be associated with a decrease in abnormal returns.

[9]It is tempting to infer judicial quality from the equity price effects of judicial assignment.

H3: *To the degree there are perceived differences in the manner individual judges decide cases, those differences should be reflected in firm value upon assignment of the judge.*

3 Data and Summary Statistics

This paper uses a dataset that begins with every docket entry in the Delaware Court of Chancery for cases categorized as "Civil" from the beginning of 2004 through the end of 2011. The Court of Chancery's jurisdiction over equitable cases means that it hears corporate matters, trust and estate cases, questions relating to purchases of real estate, and contract cases. Any firm incorporated in Delaware is subject to the jurisdiction of the Chancery Court when a case falls within these subjects. Given that over 50% of public companies have incorporated in Delaware, this court frequently settles inter and intra corporate disputes and has a national reputation for expertise in these matters.

We obtain the data from Westlaw's electronic coverage of the Chancery Court's docket. This coverage began in October, 2003, but because the 2003 entries largely involve cases that were in progress we begin with 2004 cases. The 2004 to 2011 window includes 7418 unique case numbers that involve a total of 43441 parties. From this initial dataset, we extract a subset of cases that involve publicly traded companies. To do so, we use a "fuzzy" matching algorithm that compares the names of parties from the docket with the names of publicly available companies extracted from the US Stock database put together by the Center for Research in Security Prices (CRSP). The results of the fuzzy matches are then hand-checked to confirm actual matches.

The resulting subset should be regarded as a large sample of public company litigation in the Chancery Court over the span of 8 years.[10] The resulting

While there are competing definitions of what judicial quality is, in the context of trial-level corporate cases, we would expect one of the most important measures of ability to be the minimization of Type I (a finding of liability when the underlying facts support no liability) and Type II (a finding of no liability when the facts support liability) errors. If a judge is more prone to these mistakes, the effect on equity price would depend on whether a Type I or Type II error is likely. We presume that this sort of inference is not possible at the time of case filing. Moreover, if judges make correct assessments on average and differ only with respect to the variance of their decisions, a difference in ability should not, on average, affect equity prices. For these reasons, we expect any judge-specific effects to reflect the different beliefs they have about how to best characterize the alleged wrongful conduct before them in an average case.

[10]There does not, however, appear to be any compelling reason to believe that the matching method would bias the sample in a discernible way. This sort of bias may be possible

dataset includes a total of 876 publicly traded companies that appear in 1379 cases.[11] We distinguish between "lead" cases and "follow-up" cases. Lead cases are the first-filed actions that relate to a given set of facts. If additional plaintiffs file additional cases based on the same set of facts, we designate them as follow-up cases. We base the coding for lead and follow-up cases on an examination of the complaint in each case. We also base the categorization of each case on a reading of the complaint. We retain all cases that can be categorized as derivative, merger-related, or contract, which is the vast majority of the cases involving public companies. [12]

We search the text of the docket entries to code the presence of certain procedural events and motions in the docket. The text is standardized so that frequent procedural occurrences get described is highly similar ways. This feature of the docket allows us to have a high degree of confidence that our searches are capturing the correct events. To ascertain whether a pro hac vice motion has been filed—which typically allows a lawyer from out of the state to appear in the case—we search for "pro hac vice" and code whether the docket for a particular case contains that term. For motions to expedite we search whether the docket has the term "expedite," "expedited," and/or "expedition." We randomly select cases with both positive and negative hits for both terms and find no miscodings.

The merger cases, which mostly involve lawsuits against the board members of the target, benefit from controls for the amount of the premium paid by the acquirer and the timing of the lawsuit relative to the announcement of the transaction. From the SDC Platinum database we obtain information on premium and announcement dates. We use the same "fuzzy" matching algorithm used to match the docket data to CRSP to match the cases to SDC data and hand check each match. To be useable, the SDC data must include the transaction date and the merger premium. Our final matched dataset includes 279 "lead" merger case filings. We report some statistics based on the

if the cases involving public company subsidiaries, which are sometimes difficult to pick up through fuzzy matching, tend to differ in important ways from the cases that involve the parent companies.

[11]Some cases involve multiple publicly traded companies as defendants and some cases involve public companies suing each other.

[12]Some cases involve both derivative and merger-related claims. We allow those categories to overlap. We do, however, confine the merger-related cases that involve contract claims to the merger category. Our rationale for doing so is that the contract claims almost always center on the merger agreement.

more complete, unmatched merger sample, but many of the regressions based on merger case filings use the SDC controls.

[Insert Table 1 here]

Table 1 provides summary statistics for party status, case type, judicial assignment, and case and firm characteristics. Figure 1 shows the annual trends for the case types and party status for those cases categorized as "Lead." Several trends are evident. First, the numbers of publicly listed plaintiffs and the numbers of derivative and contract suits stay relatively steady over the course of the sample. The variables that fluctuate the most appear to be the number of publicly listed companies appearing as defendants and the number of merger-related cases. There has, since 2008, been a large increase in both those numbers. The increase in merger-related cases may be due both to a secular increase in the number of those cases as well as a return of these cases to Delaware after an apparent exodus.[13]

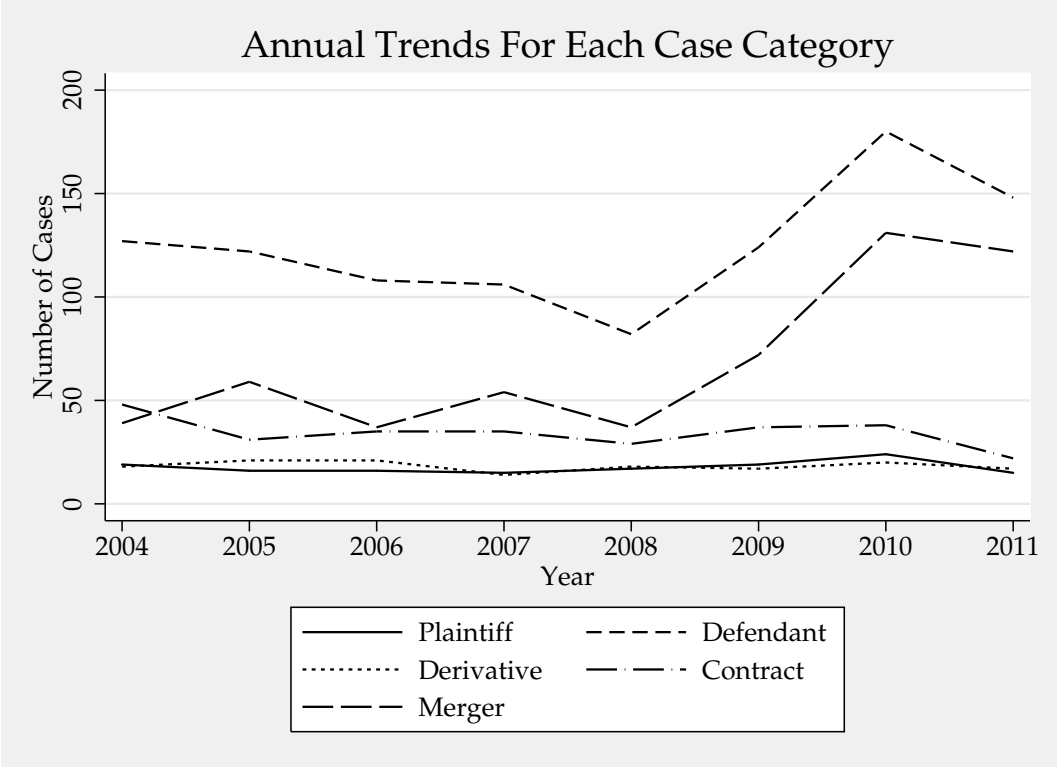


Table 2 summarizes annual trends on the termination of cases for all cases. We group terminations into four categories: stipulated dismissals, dismissals

[13]Armour, Black, and Cheffins (2012) have documented the exit of merger cases from Delaware that occurred from the mid-90s until 2009. There is some evidence, however, that these cases have returned (Cain and Davidoff, 2011; Badawi, 2013).

by the court, settlement hearings, and consolidations. When a case ends in a dismissal or a settlement hearing, we define the date of the dismissal or the hearing as the termination date. We drop lead cases where the most recent event is a consolidation. Those cases are still ongoing so it is not appropriate to treat them as terminated. It is worth noting that the docket data runs until the middle of 2012. We code for all cases that have terminated by that point, but drop those that have yet to resolve.

[Insert Table 2 here]

For each year, Table 2 shows the totals for these different categories of terminations for both lead and follow-up cases. The column for stipulated dismissals suggests that there is not a tremendous amount of variation for these types of terminations. For all years other than 2011 the number of stipulated dismissals is between 44 and 54. In 2011, the number is only 31, but that may reflect that some cases have not yet terminated. Likewise, settlement hearings do not vary that much, with a low of 9 in 2008 and a high of 20 in 2009. There is, however, substantial change in the number of consolidations each year. These numbers are likely a reflection of the number of follow-up cases that plaintiffs file; the similarity of cases determines whether consolidation is appropriate (Badawi, 2013). There are a large number of consolidations in 2005, 2010, and 2011. Relatedly, the average time to termination is relatively low in those years, which is likely due to the fact that consolidations happen early on in a case.

As in other courts of equity, there are no juries in the Court of Chancery. Each case is decided by either the Chancellor, the equivalent of the chief judge, or one of the Vice-Chancellors [collectively referred to as judges for convenience]. The Chancellor and the Vice-Chancellors are nominated by the Governor and are confirmed by the Delaware Senate for twelve-year terms. The Chancellor has responsibility for assigning the cases to individual Vice-Chancellors or to himself.[14] For most of the period in the sample William B. Chandler III served as the Chancellor. On June 22, 2011, Vice-Chancellor Leo Strine was elevated to the position of Chancellor. This means that Chancellor Chandler served as the Chancellor for the entire sample, except for roughly the last five months of it.

[14]Some cases get assigned to Case Masters, which are the equivalent of magistrates. We keep these cases in the dataset for most of the analysis we perform, but we omit them when we perform the judge-focused regressions.

We must be cautious in making inferences because the assignment process in the Court of Chancery is not randomized. Instead, the Chancellor assigns cases as they arrive. Chancellor Chandler has suggested that he sought to balance caseloads in assigning cases Marcus (2011). Fortunately, our data allow some assessment of the degree to which the assignment process is significantly non-random. First, to test the distribution of cases, we regress the market capitalization, plaintiff, pension fund, total cases, motion to expedite, pro hac vice, and the industry fixed-effects variables against the judge fixed effects controlling for year and case-type fixed effects. We then run a joint test of the judge fixed effects. In these unreported regressions, none of 16 joint tests is significant at even the 10% level. Consequently, we are unable to reject the null hypothesis (i.e. as a statistical matter, the cases appear to be randomly assigned across judges).

4 The Wealth Effects of Litigation

This section details the event study methodology that we use and it then discusses the results of applying that methodology to the Delaware data.

4.1 Estimating Cumulative Abnormal Returns

We use standard event study methodology to analyze the effect of Delaware litigation on equity prices. This approach assumes that stock returns follow a market model,

$$r_t = \alpha + \beta r_t^m + \varepsilon_t \tag{1}$$

where r_t is the return on a particular stock at time t, r_t^m is the compounded return on a market portfolio, and ϵ_t is a stochastic error. If an event, such as a lawsuit filing or case termination, occurs on day T, then there may be an "abnormal return" to the particular stock on that day. This can be captured by first calculating the predicted return during the event period, which we call r_t^*, using the constant and coefficient calculated in equation (1). To calculate the cumulative abnormal returns for firm i we subtract the actual cumulative return during the event window from the predicted return during the event window: $CAR_i = r_t - r_t^*$. We use event periods of varying lengths, as detailed below, and a 255-day pre-event window consisting of $T - 300$ to $T - 46$.

We want to obtain a representative estimate of the abnormal returns from lawsuit filings for multiple stocks, under the assumption that these represent independent events and that they share the same underlying "true" mean. We use a weighted mean to estimate the "average abnormal return," where the weight for each observation is the inverse of the variance of the predictive residual used in the calculation of the abnormal return.

We also conduct a number of analyses relating the abnormal return to the characteristics of the lawsuit being filed. To do so we conduct weighted least squares (WLS) regressions with the cumulative abnormal return in the event window as the dependent variable and firm and lawsuit characteristics and the independent variables. The WLS approach helps to correct for hetereoskedasticity. (Shahrur, 2005; Dutordoir and Van de Gucht, 2007) For weights we use the inverse of the variance of the predictive residual.

4.2 Case-Type Regressions

This subsection discusses the stock price reaction to the three major types of case type in the sample: derivative lawsuits, acquisition-related lawsuits, and contract disputes. We analyze both the filing and the termination of cases. We define the date the plaintiff filed the complaint as the date of filing indicated on the docket. For terminations, we record the date of termination as the date of the terminating event (as explained in Section 3). Table 3 reports the regression results and in every case, except for the noted column, the regressions do not include controls (i.e. the abnormal return is the constant, as is standard in litigation event studies), where observations are weighted by the inverse of the variance associated with estimate of the cumulative abnormal return. Each coefficient is the constant term from a separate regression.

4.2.1 Derivative Lawsuits

We begin our analysis with derivative lawsuits. As noted in Section 2, we have reason to believe that the earlier studies, which find no result related to these cases, may not reflect more recent use of the derivative lawsuit. Our primary reason for this hypothesis is the screening effect that the increased difficulty of showing demand futility is likely to have. When a lawsuit does make it through the screen—meaning that the plaintiffs think it is worth bringing—that may bring new information to the market. Figure 2 provides some support for this

hypothesis—it shows the running weighted abnormal returns for the ten days prior to filing and the ten days after filing. There is a substantial drop just prior to and, on the day of, filing.

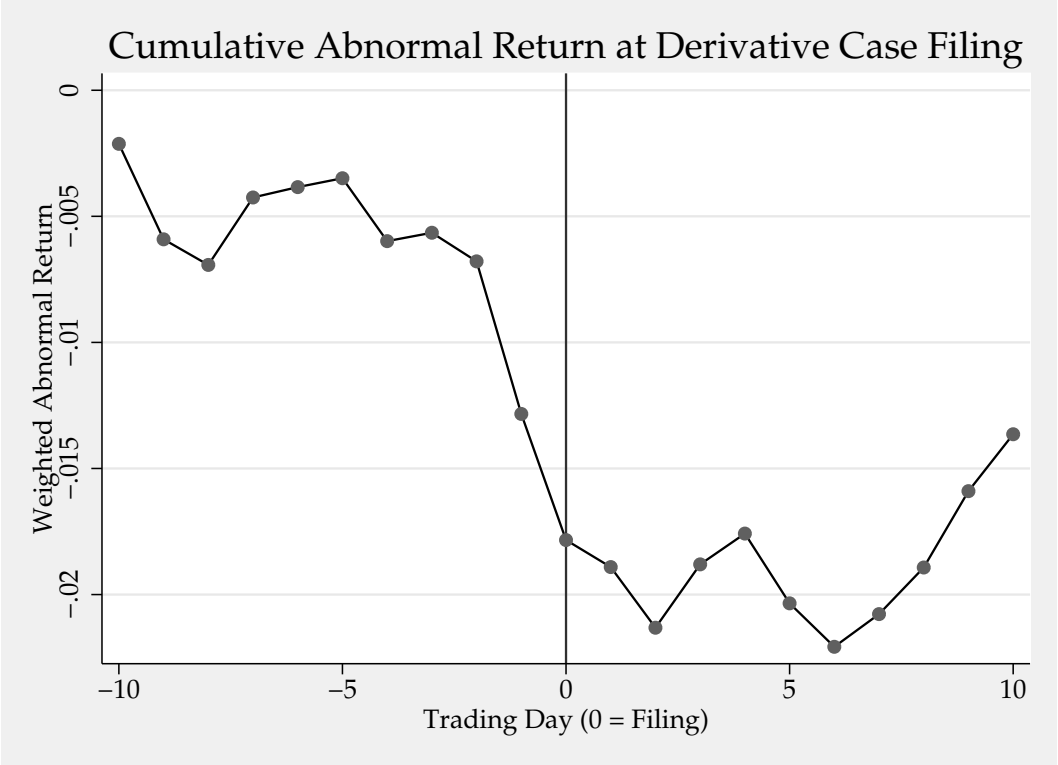


Table 3 provides further evidence that the cumulative abnormal returns of derivative cases are negative. The [-1,0], [0,+1], and [-1,+1] windows have negative CARs that are significant at the ten-percent level and the [-2, +2] window has a negative effect that is significant at the five-percent level. The significant coefficients range from -.0060 to -.0157, which suggests a loss of 0.60% to 1.57% of firm value.[15] Figure 2 shows that there are negative abnormal returns associated with every day that spans from two days before filing to two days after filing.

[Insert Table 3 here]

It can, of course, be difficult to disaggregate the effect of an expected lawsuit from the other negative effects associated with the release of the news that gives rise to the derivative suit. It could be, for instance, that the prospect of government investigation and subsequent fines may be the reason for the

[15]Twenty-two of the derivative cases also involve acquisition-related claims. When we exclude these cases in unreported regressions, we find highly similar results with respect to the sign, size, and statistical significance of the CARs.

decline in stock price. Nevertheless, the negative effects in the event windows closer to the filing date provide some evidence that the filing of the derivative lawsuit itself has a negative impact on firm value.

There are at least two potential interpretations of the evidence of a negative effect associated with derivative lawsuits. One is that the filing of derivative lawsuits provides a negative signal about the quality of management and/or board oversight and the market is punishing the firm accordingly. If, indeed, a firm faces the prospect of losing value, this effect may inhibit the type of wrongdoing that derivative lawsuits target. Alternatively, the loss may just be a transfer of wealth from the firm to plaintiffs' attorneys through attorneys' fees.[16] The difference between these two interpretations depends on the underlying merits of the lawsuit and the dynamic effects associated with derivative actions. As we discuss in the section below on indicators of case quality, it does appear that higher quality cases increase the negative effect associated with derivative lawsuits.

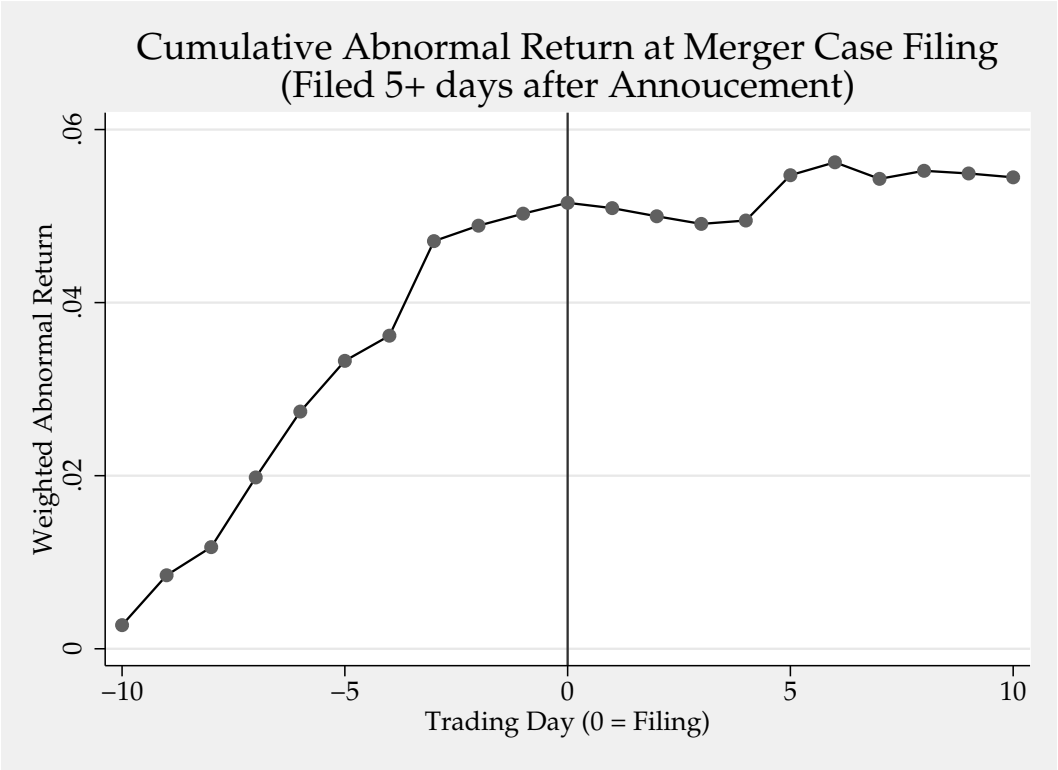
4.2.2 Acquisition-Related Cases

Acquisition-related lawsuits have been the subject of extensive recent research. Researchers have examined how multijurisdictional dynamics may affect litigation (Cain and Davidoff, 2013), whether there has been an increase in the number of challenges as opposed to the percentage of mergers challenged (Thomas and Thompson, 2012), and how the presence of institutional parties affects features of these cases Webber (2013). But the effect of this litigation on equity prices has not yet been subject to analysis.

Conducting merger litigation event studies poses some difficulty because plaintiffs often file cases right after the announcement of a merger (Fletcher et al., 2012). We address these concerns in two ways. First, we conduct an analysis of cases filed five or more trading days after the announcement of the merger. At that time, the abnormal return associated with the price paid by the acquirer should be fully incorporated into the stock price in a way that does

[16]Insurance policies may cover attorneys' fees in these cases, which might mute the effect of an award on firm value. (see, e.g., XL Spec. Ins. Co. v. Loral Space & Comm., Inc., 011 WL 537161 (N.Y. App. Div. Feb. 17, 2011) (holding that a directors and officers' insurance policy covered the attorneys' fees in a derivative action)). That said, insurers usually adjust rates to reflect experience. Significant derivative liability may lead to a large increase in premiums and that change may have an adverse effect on firm value. The market may anticipate this increase in premiums upon filing of the lawsuit and that effect could produce negative abnormal returns.

not overlap with the event windows. For these cases, results are insignificant in all event windows except for the [-1,0] CAR and that result is significant only at the ten-percent level. This evidence provides some support for our hypothesis that the average merger lawsuit is uninformative to the market. Figure 3 further supports this finding—the cumulative weighted AR is quite flat around the window of filing for those cases filed five or more trading days after announcement.



There are several potential objections to this first approach. One is that the cases filed quickly are different from those filed less than five trading days after announcement of the deal. For example, higher quality cases may get filed more quickly than lower quality cases. Another potential problem is that the additional time may allow the market to incorporate both the expected lawsuit and the expected effect of the lawsuit into stock price.

To address these concerns our second type of analysis includes acquisition cases filed at any time after announcement. We include controls for deal timing and the premium paid. Specifically, we use indicator variables for cases filed the same day as the announcement (sameday) or the day after the announcement (nextday), the merger premium, and interactions between sameday and the premium and nextday and the premium. These controls

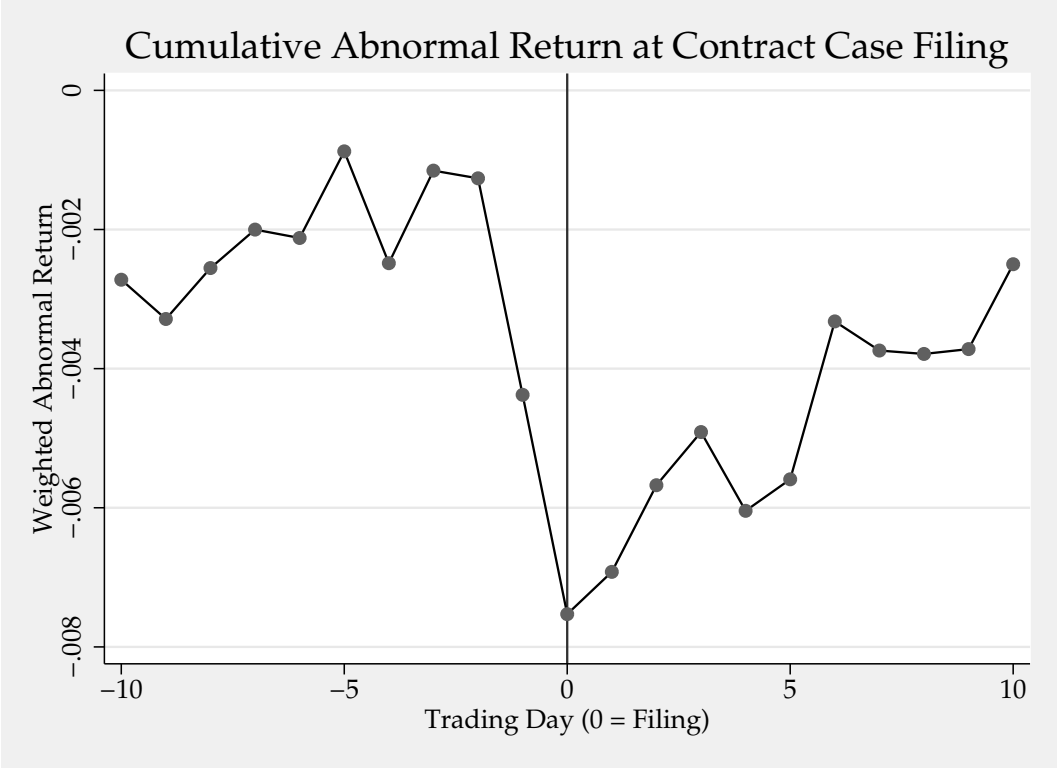
should account for the premium's effect on stock price, albeit at the cost of restricting our sample size because we do not have this information for all cases.

The regressions with the merger controls indicate that there is no significant abnormal return associated with case filing. The sole exception is the [-2,+2] window, which is straightforward to explain. Because we only use sameday and nextday controls, this regression does not control for cases filed two days after the announcement of the deal. Deal announcements typically bring large increases in price, which indicates why the coefficient for that window is substantially larger than the estimated abnormal returns for the shorter windows.

We view this evidence as largely consistent with our hypothesis. Merger litigation is almost a foregone conclusion, especially toward the end of our sample period. Market participants should expect this litigation to occur and should factor the average effect of this litigation into the target's equity price. If the lawsuit provides some indication that there is likely to be a recovery for shareholders, the market may reflect that fact, but that is an above average result in these cases (Davidoff et al., 2015). We attempt to control for some of these factors in the analysis below, but the evidence developed in the present analysis does suggest that the average case has no effect on firm value at the time of filing.

4.2.3 Contract Cases

Contract disputes are the final type of case that we analyze. Figure 4 shows the abnormal return in the ten days before and after case filing. We find some evidence that the filing of these cases negatively affects firm value. The magnitude of the abnormal loss appears to be relatively modest. We find negative effects in the [-2, 0] and [-1,0] windows that are significant at the five-percent level. The potential for experiencing this loss in firm value may have the effect of encouraging compliance with contracts. The results also suggest that the occurrence of these lawsuits is not completely expected by the market. This possibility supports our prediction that contract (and derivative) lawsuits are more difficult to anticipate than merger lawsuits.



4.2.4 Case Terminations

Table 3 also includes information on the termination of cases. We expect terminations to have little systematic effect on firm value. Information should be coming to the market about the case as it proceeds, and equity prices should reflect continual updating of the expected resolution.[17] Our evidence is consistent with that expectation.[18] None of our case types is associated with

[17]Haslem (2005) shows a negative effect associated with settlement as opposed to judicial resolution of a case. He attributes this effect to a signal that management would rather keep the underlying facts confidential rather than subject them to further litigation. To try and discern whether this effect holds for Delaware litigation, we run specifications based on the type of termination. In these unreported regressions, we find that only settlement hearings result in a negative effect. This result is consistent with Haslem's findings.

[18]We do not include the weights in our merger termination regressions because we believe that they distort the data. The weights reflect the volatility in stock price during the pre-event period. For cases where the merger termination announcement occurred during or before the pre-event period there is likely to be little volatility in the stock price because the target firm will be trading at a slight discount to the merger price. This lack of volatility will increase the weights for cases that take more time to resolve. Cases that resolve quickly, however, will have smaller relative weights because the pre-event window includes the pre-announcement volatility. The large relative weights is the likely reason why using the weights for merger termination cases produces results that are extremely sensitive to the inclusion of single outliers (i.e. when we remove the observations with the largest weights, the coefficients are no longer statistically significant). None of our other results show this type of sensitivity to outliers.

a statistically significant abnormal return.

4.3 Case Covariates

This subsection examines the inclusion of case covariates in the estimates of abnormal returns. As discussed in Section 2, these covariates include indications of case quality and the potential presence of cases in other jurisdictions. Tables 4 and 5 present these results.

4.3.1 Indications of Case Quality

The first regression in Table 4 reports the results for derivative filings. Both measures of case quality—the presence of a pro hac vice motion and the number of cases filed—are negative, large, and statistically significant. The coefficients are also economically significant. The average market capitalization of firms that are the targets of derivative suits in the sample is approximately $2.19 billion at the time of filing. The 1.92 percent drop in firm value implied by the pro hac vice coefficient implies a loss of value of approximately $420 million. This estimate is far larger than the average attorneys' fees in Delaware derivative cases (Webber, 2013). The coefficient for the number of cases filed is also sizable at roughly -1.2 percent per case.

[Insert Table 4 here]

This evidence suggests that, at least in those cases with indicia of higher quality, the decline in firm value goes beyond what the company can expect to pay in attorneys' fees. To put it another way, the data suggest that the filing of a Delaware lawsuit provides a negative signal about the firm that the market punishes. To the degree that managers respond to these types of declines in equity prices, one could read this finding as corroborative evidence that derivative lawsuits do have the power to deter managerial wrongdoing.

We do not find associations between our case quality variables and the filing of merger cases. The pro hac vice and the number of cases variables have insignificant coefficients when we control for premium and timing and when we restrict cases to those filed five or more trading days after the announcement of the deal. One might explain the apparent difference that case and attorney quality have as an indication that derivative cases are, on average, more difficult to understand and litigate than merger lawsuits. Accordingly, the known or expected early involvement of high quality counsel in derivative

cases may give the market a signal that there is something to the case. In contrast, if merger cases are relatively straightforward to litigate, the known or expected involvement of high quality counsel may not have as much of a consequence for the possibility of increasing the amount of consideration paid by the target.

We do find a positive abnormal expected return associated with the termination of merger cases that involve pro hac vice motions.[19] This result is surprising insofar as market participants should be aware of the quality of counsel representing the parties and should incorporate those assessments into the stock price. At the same time, a number of studies show abnormal positive returns to merger arbitrage (Jindra and Walkling, 2004; Baker and Savaşoglu, 2002; Mitchell and Pulvino, 2001). Some of these studies suggest that the returns from this arbitrage come from the substantial risk associated with failed deals. This pro hac vice result supports this account insofar as higher quality lawyers imply that the underlying cases are more complex.[20] These harder cases may increase the risk that the deal will fail either through court action or because the underlying deal is complicated. If market participants are not willing to fully bear that risk—as the research on merger arbitrage suggests—that would explain the positive abnormal return when the case terminates.

We find the expected associations with attorney and case quality in the filing of contract cases. One would expect companies to bring in better lawyers in cases that are more problematic and one would expect cases with better lawyers to have a larger impact on firm value. While we cannot tease apart these separate effects, Table 4 shows that there is a significant negative effect associated with cases where the parties bring in out-of-state lawyers. Likewise, where the lawsuit draws multiple cases there is a significant and negative effect on equity prices. We note that in the representative cases, it is much more likely that a dispute will draw multiple cases due to the competition to become lead counsel. Contract cases rarely involve aggregate litigation and,

[19]This effect is robust to a variety of specifications. As we note above, we do not use weights for the merger termination analysis. If we include these weights, the result remains positive and statistically significant. The result is not sensitive to outliers (with respect to weights) and it endures both with and without the use of controls for type of resolution and judicial identity.

[20]This pro hac vice result could be a proxy for case length rather than for complexity (i.e. the longer the case stretches on, more likely it is to involve a lawyer from another jurisdiction). To test for this effect we include a variable for time to termination in unreported regressions. The pro hac vice coefficient remains positive and statistically significant and the time to termination variable is not statistically significant.

consequently, it is relatively rare for parties to file multiple, related cases. Nevertheless, when a contractual dispute spurs the filing of more than one complaint the data suggest that it will have a quite large effect on firm value.

4.3.2 Indications of Multijurisdictional Litigation

Turning to motions to expedite, we find a large, positive stock price effect (1.92%) that is significant at the five-percent level upon the filing of a derivative case that involves an eventual motion to expedite. Note that the magnitude of this effect is potentially large enough to wipe out the decline in stock price–and thus the deterrent effect–associated with higher quality cases. We view this result as a potential indication that competition among plaintiffs undermines incentives to pursue derivative cases with vigor. If an eventual motion to expedite signals that a case is proceeding in another forum, the large positive effect on stock price may reflect that the potential for a reverse auction will dilute the effect of the derivative lawsuit. We note, however, that our the confirmation exercise that we carry out in Appendix B does not show as strong an association between motions to expedite and multijurisdictional litigation in derivative lawsuits as we observe in merger litigation. For that reason, we interpret this result with more caution than we do our more robust results.

Analyzing the role of motions to expedite in merger cases turns out to be somewhat complex due to the shift in the amount of multijurisdictional litigation over the course of the sample. As Cain and Davidoff document, the number of merger challenges that involved cases filed in different states increased from 8.5% in 2005 to 25.8% in 2006. By 2011, 47.4% of merger challenges involved claims in multiple states. Badawi (2013) shows that motions to expedite in these sorts of cases have increased in Delaware over the same time period. These changes mean that the reasons for filing a motion to expedite in a merger case may have changed. Early in the sample–when it was less likely that litigants were competing with related cases in other jurisdictions–the motivation for a motion to expedite may have been to increase leverage over the defendant directors. In cases where these motions are likely to be successful, this leverage should allow plaintiffs to secure a larger increase in merger consideration. But later in the sample, filing a motion to expedite may be a response to a group of attorneys litigating in other states. When a motion to expedite is expected in these cases, one may expect a negative effect on stock price because the potential for a reverse auction substantially decreases the

leverage that plaintiffs' attorneys have over the defendant directors.

To account for this potential change in the effect of a motion to expedite we interact the expedite variable with the year fixed effects. The results suggest that the meaning of an expected motion to expedite has shifted over the span of the sample. Table 5 reports these results in three separate windows for merger filings with the SDC controls and merger cases filed 5 or more trading days after the deal announcement. In three out of the six regressions the baseline effect of a motion to expedite is positive, large, and significant at either the five or one-percent level. This implies that during 2004, which is the omitted year for the interactions, the expectation of a motion to expedite signaled that the attorneys might gain leverage over the board. But the effects of the interaction show that this effect began to disappear. For many of the years after 2004, the effect of the interaction is large, negative, and statistically significant.[21] To the degree that the expectation of a motion to expedite later in the sample signals that there is litigation going on in another forum, these results provide some evidence that this sort of competition has a negative effect for shareholders that is consistent with the reverse auction concern.[22]

[Insert Table 5 here]

4.4 Wealth Effects and Judicial Assignment

The docket includes information on the Chancellor or Vice-Chancellor assigned to the case. We use this information to assess the wealth effect of a particular judge being assigned to a case at the time the judge is revealed and at the time the case is decided.[23]

[21] To check the robustness of these findings, we run similar, unreported regressions for the derivative cases. We expect that the interaction variables will not be significant because there is no evidence that the meaning of a motion to expedite has shifted in the same way that it has for the acquisition-related cases. The results largely confirm this expectation insofar as only two of the year-expedite interaction variables are significant (one at the ten-percent level and another at the five-percent level).

[22] Note that the coefficients on the interaction terms are roughly in the same range. We do not place much weight on the difference between each of the coefficients because those differences are not that large. Rather our emphasis is on the difference between 2004, when there was little multijurisdictional litigation, and the following years when that litigation increased substantially.

[23] Some cases get assigned to Case Masters, which are roughly the equivalent of magistrates. We keep these cases in the dataset for all of the analysis above, but we limit the analysis in this section to cases assigned to the Chancellor and Vice-Chancellors. Vice Chancellor Glasscock was the only new judge that came into the sample during the analysis period. He was confirmed in 2011, near the end of the sample. Because he appears in so few cases, we omit him from the analysis.

Tables 6 and 7 show the results for these regressions. Columns 1 and 2 include all acquisition-related cases, Columns 3 and 4 include all non-acquisition-related contracts cases, and Columns 5 and 6 include all non-acquisition-related derivative cases. We focus on the [+1, +4] event window for case filing because the assignment of a judge to a case usually does not occur until several business days after filing. We run the regressions both with controls for party status, market capitalization, plaintiff status, pension fund involvement, total cases, motions to expedite, pro hac vice, and industry and without those controls. The merger regression includes the premium and timing controls used in the earlier analysis.

[Insert Table 6 here]

As Table 6 shows, we find no significant effects associated with the identity of the judge near filing.[24] This is the case both when we omit case controls and when we include them. There are two ways to interpret these results. The first is that the market places little or no weight on the identity of the judge deciding the case. This could be because judges have little impact on how litigants resolve case, because they decide in a similar manner, or because any differences are not valued by the market. A second possibility is that there are substantive differences between judges, but we are unable to discern them with our data. One methodological difficulty is the variation in the time of judicial assignment. The docket does not provide information about the date that the judge assigned to the case became public. Conversations with Delaware lawyers suggests that the average time between filing and assignment is roughly two to three days, but we cannot verify that claim. As a consequence, we must use a relatively long window (four days) and that makes the analysis more imprecise.

[Insert Table 7 here]

Table 7 reports the results for case terminations. While the filing regressions attempt to measure the reaction to judicial assignment, the market, of course, knows the judge at the time of termination (barring an extremely quick stipulated dismissal). We view these regressions as a measure of the degree to which the termination of the case differs from market expectations. The results show little direct effect associated with the judge variables.

[24] As noted above, we omit the cases assigned to Case Masters and to Vice Chancellor Glasscock. This accounts for the different number of observations in this table and in those that use the complete sample.

As with the filing regressions, there are two potential interpretations. One is that the market anticipates the effect of the judge on the termination of the case and incorporates that effect into the stock price prior to termination. The second possibility is that our data are not robust enough to pick up an effect. This is, of course, a possibility, but we have more confidence that the lack of significant effects are meaningful relative to the judicial filing regressions. We use a narrow two-day window for these results so we do not have as many problems with imprecision. In addition, the market has much more time—in some cases years—to develop expectations about what is likely to happen in these cases. The notion that market participants will be able to impound the judge's likely effect on the resolution of the case at the time of that resolution does not strike us as far-fetched.

5 Conclusion

This study provides evidence that answers three open questions about corporate litigation. First, the event studies suggest that the filing of derivative lawsuits have a negative effect on firm value. The magnitude of these effects suggests that the loss of shareholder wealth exceeds the direct costs associated with litigation. This effect suggests that market participants make a negative inference about firms that are the subject of derivative suits.

Second, the data suggest that multijurisdictional litigation may dilute the effect of shareholder litigation. Insofar as motions to expedite are an indicator that litigation is going on elsewhere, we show that these procedural moves mitigate the negative effect of derivative litigation and may diminish prospects of a shareholder recovery in acquisition-related litigation. We view this evidence as providing some confirmation of the reverse auction hypothesis. If firms have a competing group of plaintiffs in multiple jurisdictions, they may be able to settle for less than they would if they were dealing with plaintiffs in a single jurisdiction.[25]

Third, we find little evidence that judicial identity affects firm values either at assignment or at the time of termination. This evidence provides some indication that any judicial effects at the time that judges are revealed are too small to detect statistically.

[25]We take no position, on what the "right" amount of shareholder litigation is. Our data only allow us to make relative inferences about the effects of shareholder litigation.

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Appendix A: Variable Definitions

Variable	Definition
ln(Market Cap.)	Natural logarithm of the market capitalization as reported in Compustat at the end of the quarter in which the complaint was filed.
Pension Fund	Pension fund appears as one of the parties.
Pro Hac Vice Motion Filed	The docket shows that at least one pro hac vice motion was filed during the course of the litigation.
Motion to Expedite Filed	The docket shows that at least one motion to expedite proceedings filed during the course of litigation.
Total Complaints Filed	The total number of complaints filed that allege a similar claim based on a similar set of facts.
Plaintiff	The public company in the case is the plaintiff.
Chandler	The case was initially assigned to Chancellor Chandler.
Laster	The case was initially assigned to Vice Chancellor Laster.
Noble	The case was initially assigned to Vice Chancellor Noble.
Strine	The case was initially assigned to then-Vice Chancellor Strine.
Lamb	The case was initially assigned to Vice Chancellor Lamb.

Appendix B:
Motions to Expedite and Multijurisdictional Litigation

As discussed in Section 2.3, conversations with Delaware lawyers and some empirical evidence suggests that competing litigation in other jurisdictions may motivate a motion to expedite. We investigate that relationship in this appendix by ascertaining whether cases that involved a motion to expedite were, in fact, being litigated on multiple fronts. To do so, we examine the sued or suing firm's 10-Q, 10-K, and related securities filings for the period after the filing of the Delaware case. We obtain these filings from the SEC's EDGAR database. Firms are required to disclose "material" information, including lawsuits, and most 10-Q and 10-K filings have a subsection labeled "Litigation," or something similar. We proceed on the assumption that if the company discloses the Delaware case, it will disclose related litigation elsewhere. But if the company does not disclose the Delaware case, it will not disclose other similar cases in other jurisdictions. The company may not disclose these cases because it deems them not "material."

We randomly select a subsample of the merger and derivative cases and read the related securities filings. For the merger cases, we limit the subsample to cases where the shareholders sue the directors of the target in an active deal because there is almost always an attorney's fee to be had in these cases (Cain & Davidoff, 2012). Cases involving failed mergers and those suing bidders have far worse prospects and are unlikely to produce the fee that drives multijurisdictional competition. Of the 76 merger cases we examined, we were unable to find a disclosure of the Delaware case for 21 of them. For the remaining 55 cases, the Pearson correlation coefficient for the presence of multijurisdictional litigation and a motion to expedite is .558. More concretely, of the 38 cases that involve a motion to expedite, 31 of them have a similar case proceeding in another jurisdictions. Of the 17 cases without a motion to expedite, only 4 involve litigation in another jurisdiction.

For derivative cases, we examine 26 cases and are able to locate disclosures of the Delaware case in 17 of them. The Pearson correlation coefficient for the presence of multijurisdictional litigation and the filing of a motion to expedite in the Delaware case is .311. Of the 9 cases without a motion to expedite, only 1 of those cases involves multijurisdictional litigation. Of the remaining 8 cases, 3 of them involve multijurisdictional litigation.

Table 1: Summary Statistics for Case Filings and Case Terminations

	Filings		Terminations	
	Percentage (or Mean)	SD	Percentage	SD
Chancellor or Vice-Chancellor				
Parsons	0.146		0.171	
Laster	0.0733		0.112	
Noble	0.131		0.122	
Strine	0.277		0.238	
Lamb	0.136		0.129	
Chandler	0.225		0.205	
Party Type				
Defendant	0.884		0.878	
Plaintiff	0.116		0.122	
Case Type				
Derivative	0.130		0.167	
Merger	0.505		0.433	
Merger (SDC matched)	0.256		0.116	
Contract	0.270		0.286	
ln(Market Cap)	7.483	2.266	7.801	2.310
Pension Fund	0.144		0.141	
Total Complaints Filed	1.427	1.166	1.362	1.011
Motion to Expedite Filed	0.411		0.347	
Pro Hac Vice Motion Filed	0.675		0.626	
Industry				
Consumer Non-Durables	0.0485		0.0483	
Consumer Durables	0.0165		0.0190	
Manufacturing	0.0778		0.0741	
Oil, Gas, Coal	0.0513		0.0534	
Business Equipment	0.214		0.207	
Telephone and Television	0.0696		0.0776	
Wholesale	0.0815		0.0879	
Healthcare	0.116		0.112	
Utilities	0.0266		0.0328	
Other	0.298		0.288	
Observations	1092		580	

Table 2: Case Resolutions by Year of Filing

Year	Stip. Dismissal	Settlement Hearing	Consolidated	Court Dismissal	Mean Days to Resolution
2004	50	15	28	19	355.5
2005	44	14	65	21	256.9
2006	46	9	17	15	325.8
2007	44	11	31	10	251.0
2008	43	10	10	5	315.4
2009	50	20	28	9	246.7
2010	54	12	75	2	145.6
2011	31	18	108	3	93.4

Table 3: Abnormal Return to Case Filing and Termination

	Derivative		Merger			Contract	
	Filing	Termination	Filing (filed 5 or more days after announcement)	Filing (with SDC controls)	Termination	Filing	Termination
(-1,0) CAR	-0.0111	-0.00390	0.00265	0.00901	-0.00167	-0.00628	0.000603
	(0.00650)*	(0.00335)	(0.00148)*	(0.00641)	(0.00324)	(0.00319)**	(0.00200)
(0,+1) CAR	-0.00610	-0.00258	0.000646	0.00264	-0.000963	-0.00255	-0.00180
	(0.00358)*	(0.00215)	(0.00148)	(0.00403)	(0.00269)	(0.00252)	(0.00244)
(-1,+1) CAR	-0.0121	-0.00455	0.00203	0.00943	-0.000657	-0.00567	0.000405
	(0.00692)*	(0.00360)	(0.00192)	(0.00664)	(0.00360)	(0.00390)	(0.00280)
(-2,+2) CAR	-0.0156	-0.00217	0.00287	0.0282	-0.00638	-0.00453	0.000941
	(0.00771)**	(0.00443)	(0.00234)	(0.00914)***	(0.00499)	(0.00436)	(0.00346)
Observations	144	98	435	282	198	279	163

This table presents results from WLS regressions that use the cumulative abnormal return in the indicated window as the dependent variable. The value reported is the value of the constant. Other than the merger regressions described below the regressions include no independent variables. Day zero is the day the first complaint is filed against the target firm. The first merger filing regression includes all cases filed five or more trading days after the announcement of the merger. The second merger filing regression includes controls for the merger premium, indicator variables for whether the plaintiffs filed the lawsuit on the same day as the announcement of the transaction (sameday), the day after the transaction (nextday), and interaction variables for premium*sameday, and premium*nextday. Each observation is weighted by the inverse of the variance associated with estimate of the cumulative abnormal return. The standard errors are reported in parentheses. ***, **, and * denote significance at the 1%, 5%, and 10% confidence levels, respectively.

Table 4: Cumulative Abnormal Return and Case Characteristics in the [0,+1] Window

	Case Filings				Case Terminations		
	Derivative	Merger (SDC)	Merger (5+ days)	Contract	Derivative	Merger	Contract
ln(Market Cap)	-0.00156	0.00358	0.000293	-0.00102	-0.000639	0.000181	0.00286
	(0.00201)	(0.00210)*	(0.000767)	(0.00115)	(0.00163)	(0.00131)	(0.00123)**
Pension Fund	0.0131	0.00625	0.00268	-0.0103	-0.00113	0.00486	0.00189
	(0.0102)	(0.00758)	(0.00396)	(0.0187)	(0.00776)	(0.00717)	(0.0295)
Pro Hac Vice Motion Filed	-0.0192	0.00936	-0.000727	-0.0120	0.00438	0.0196	-0.00497
	(0.00949)**	(0.00756)	(0.00402)	(0.00532)**	(0.00653)	(0.00753)***	(0.00493)
Motion to Expedite Filed	0.0192	-0.00518	0.00343	0.00910	-0.00306	-0.00512	0.00297
	(0.00957)**	(0.00640)	(0.00336)	(0.00587)	(0.00735)	(0.00657)	(0.00576)
Total Complaints Filed	-0.0122	-0.00162	0.000769	-0.0283	0.00395	0.00277	0.00493
	(0.00496)**	(0.00196)	(0.00140)	(0.00558)***	(0.00331)	(0.00342)	(0.00613)
Plaintiff		-0.160	0.0130	0.00186		0.0342	-0.00283
		(0.0717)**	(0.00841)	(0.00535)		(0.0126)***	(0.00536)
Constant	-0.0166	-0.0300	-0.00660	0.0730	-0.00657	0.0115	-0.0508
	(0.0386)	(0.0324)	(0.0126)	(0.0351)**	(0.0262)	(0.0298)	(0.0302)*
Observations	144	282	435	279	98	198	163
R^2	0.225	0.645	0.084	0.202	0.210	0.165	0.386
Year Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Industry Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes	Yes

This table presents results from WLS regressions that use the cumulative abnormal return in the indicated window as the dependent variable. Day zero is the day the first complaint is filed against the target firm. The first merger filing regression includes controls for the merger premium, indicator variables for whether the plaintiffs filed the lawsuit on the same day as the announcement of the transaction (sameday), the day after the transaction (nextday), and interaction variables for premium*sameday, and premium*nextday. The second merger filing regression includes all cases filed five or more trading days after the announcement of the merger. Each observation is weighted by the inverse of the variance associated with estimate of the cumulative abnormal return. The standard errors are reported in parentheses. ***, **, and * denote significance at the 1%, 5%, and 10% confidence levels, respectively.

Table 5: Abnormal Return to Merger Case Filing and with Expedite Interactions

	CAR 0,+2		CAR -1,0		CAR 0, +1	
	SDC Controls	Five+ Days	SDC Controls	Five+ Days	SDC Controls	Five+ Days
Plaintiff	-0.171	0.00315	-0.110	0.00316	-0.165	0.0131
	(0.0716)**	(0.00951)	(0.119)	(0.00821)	(0.0709)**	(0.00848)
Pension Fund	0.00311	0.00265	-0.00252	0.00314	0.00165	0.00256
	(0.00774)	(0.00463)	(0.0129)	(0.00399)	(0.00769)	(0.00413)
ln(Market Cap)	0.00334	0.000452	0.00117	0.0000800	0.00413	0.000302
	(0.00214)	(0.000891)	(0.00355)	(0.000767)	(0.00213)*	(0.000794)
Pro Hac Vice Motion Filed	0.0138	-0.000594	0.0152	-0.00454	0.0167	-0.000710
	(0.00787)*	(0.00457)	(0.0131)	(0.00394)	(0.00782)**	(0.00407)
Motion to Expedite Filed	0.0546	0.00851	-0.00643	0.0666	0.0489	0.0125
	(0.0206)***	(0.0154)	(0.0342)	(0.0133)***	(0.0204)**	(0.0138)
Total Complaints Filed	-0.00113	0.00156	0.00278	-0.00113	-0.000506	0.000820
	(0.00206)	(0.00159)	(0.00342)	(0.00137)	(0.00205)	(0.00142)
2005 * Expedite	-0.0853	-0.0228	0.00989	-0.0667	-0.0783	-0.0176
	(0.0288)***	(0.0182)	(0.0477)	(0.0157)***	(0.0285)***	(0.0163)
2006 * Expedite	-0.0939	-0.0220	0.0283	-0.0745	-0.0994	-0.0254
	(0.0286)***	(0.0223)	(0.0475)	(0.0192)***	(0.0284)***	(0.0199)
2007 * Expedite	-0.0578	-0.00365	0.0164	-0.0597	-0.0597	-0.00950
	(0.0256)**	(0.0186)	(0.0425)	(0.0160)***	(0.0254)**	(0.0166)
2008 * Expedite	-0.0432	0.0164	-0.00905	-0.0501	-0.0428	0.00433
	(0.0338)	(0.0206)	(0.0561)	(0.0177)***	(0.0336)	(0.0184)
2009 * Expedite	-0.0538	0.00442	0.0173	-0.0594	-0.0482	-0.00173
	(0.0370)	(0.0237)	(0.0614)	(0.0204)***	(0.0367)	(0.0211)
2010 * Expedite	-0.0589	-0.00756	-0.00495	-0.0629	-0.0514	-0.0110
	(0.0241)**	(0.0168)	(0.0400)	(0.0145)***	(0.0239)**	(0.0150)
2011 * Expedite	-0.0671	-0.00148	0.000848	-0.0702	-0.0591	-0.00684
	(0.0246)***	(0.0169)	(0.0409)	(0.0145)***	(0.0244)**	(0.0150)
Observations	282	435	282	435	282	435
R^2	0.659	0.092	0.705	0.156	0.664	0.094
Year Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
Industry Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes

This table presents results from WLS regressions that use the cumulative abnormal return in the indicated window as the dependent variable. Day zero is the day the first complaint is filed against the target firm. The first regression in each window includes controls for the merger premium, indicator variables for whether the plaintiffs filed the lawsuit on the same day as the announcement of the transaction (sameday), the day after the transaction (nextday), and interaction variables for premium*sameday, and premium*nextday. The second regression in each window includes all cases filed five or more trading days after the announcement of the merger. Each observation is weighted by the inverse of the variance associated with estimate of the cumulative abnormal return. The standard errors are reported in parentheses. ***, **, and * denote significance at the 1%, 5%, and 10% confidence levels, respectively.

Table 6: Abnormal Returns to Filing in the [+1,+4] Window
with Judicial Controls (relative to Parsons)

	Derivative		Merger		Contract	
Chandler	-0.000123	0.0382	0.00480	-0.000880	0.00860	0.0142
	(0.0229)	(0.0300)	(0.00631)	(0.00721)	(0.00855)	(0.00914)
Laster	0.0112	0.0349	-0.00244	-0.00569	-0.00530	-0.00813
	(0.0329)	(0.0428)	(0.00819)	(0.00860)	(0.0133)	(0.0151)
Noble	0.00246	0.0135	0.00718	0.00611	-0.00116	-0.000216
	(0.0297)	(0.0338)	(0.00706)	(0.00738)	(0.00923)	(0.00978)
Strine	0.0128	0.0488	0.00749	0.00191	-0.00471	-0.00382
	(0.0243)	(0.0294)	(0.00583)	(0.00665)	(0.00817)	(0.00933)
Lamb	0.00493	0.0374	0.00454	0.00556	-0.00119	0.00784
	(0.0258)	(0.0337)	(0.00646)	(0.00813)	(0.00950)	(0.0108)
Observations	142	142	277	277	250	250
R^2	0.006	0.109	0.011	0.112	0.014	0.147
Controls	No	Yes	No	Yes	No	Yes

This table presents results from WLS regressions that use the cumulative abnormal return in the indicated window as the dependent variable. Day zero is the day the first complaint is filed against the target firm. The standard errors are reported in parentheses. The controls include the same as those in Table 4 (whether the party is a plaintiff, the presence of pension funds, whether a pro had vice motion or motion to expedite was filed in the case, and the total number of complaints. The merger regression control add controls for the merger premium, indicator variables for whether the plaintiffs filed the lawsuit on the same day as the announcement of the transaction (sameday), the day after the transaction (nextday), and interaction variables for premium*sameday, and premium*nextday. Each observation is weighted by the inverse of the variance associated with estimate of the cumulative abnormal return. The standard errors are reported in parentheses. ***, **, and * denote significance at the 1%, 5%, and 10% confidence levels, respectively.

Table 7: Abnormal Returns to Termination in the [0,+1] Window with Judicial Controls (relative to Parsons)

	Derivative		Merger		Contract	
Chandler	-0.0142	-0.0146	0.00584	0.00598	-0.00747	-0.00778
	(0.0136)	(0.0136)	(0.00933)	(0.00956)	(0.00874)	(0.00885)
Laster	-0.0165	-0.0157	0.00908	0.00885	0.00729	0.00857
	(0.0137)	(0.0142)	(0.0106)	(0.0108)	(0.00914)	(0.00947)
Noble	-0.0256	-0.0225	-0.00605	-0.00700	0.00378	0.00520
	(0.0181)	(0.0186)	(0.0106)	(0.0109)	(0.00856)	(0.00906)
Strine	-0.00390	-0.00416	0.00378	0.00400	0.00737	0.00793
	(0.0137)	(0.0143)	(0.00926)	(0.00948)	(0.00784)	(0.00805)
Lamb	-0.0116	-0.0124	0.00619	0.00634	0.0142	0.0141
	(0.0151)	(0.0151)	(0.0124)	(0.0126)	(0.0101)	(0.0102)
Observations	91	91	194	194	136	136
R^2	0.231	0.278	0.183	0.187	0.554	0.560
Case Controls	Yes	Yes	Yes	Yes	Yes	Yes
Resolution Controls	No	Yes	No	Yes	No	Yes

This table presents results from WLS regressions that use the cumulative abnormal return in the indicated window as the dependent variable. Day zero is the day the first complaint is filed against the target firm. The standard errors are reported in parentheses. The case controls include the same as those in Table 4 (whether the party is a plaintiff, the presence of pension funds, whether a pro had vice motion or motion to expedite was filed in the case, and the total number of complaints. The resolution controls provide indicator variables for whether the case ended through a consolidation, settlement hearing, or a judicial dismissal (stipulated dismissals are the omitted category). Each observation is weighted by the inverse of the variance associated with estimate of the cumulative abnormal return. The standard errors are reported in parentheses. ***, **, and * denote significance at the 1%, 5%, and 10% confidence levels, respectively.