

## Securities

# Rare Securities Fraud Jury Verdicts Test High-Stakes Strategy

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The high risks and potential benefits—to both companies and investors—of taking securities fraud class actions to a jury were on full display in three rare trials that concluded over two recent months.

Verdicts left Vaxart Inc. investors empty-handed in their suit against a hedge fund that sold its majority stake in the vaccine developer, and denied recovery to Exxon Mobil Corp. shareholders over accounting disclosures. On the other side of the ledger, a jury ordered Elon Musk to pay Twitter Inc. investors their losses—still to be assessed but potentially topping \$2 billion—attributed to a pair of social media posts he made before acquiring the company. Musk has vowed to appeal.

These highly variable outcomes—where plaintiffs end up with either nothing or big potential paydays—are very different from the single-digit percentages investors often recover in settlements. Despite the risk, litigants on both sides may develop more appetite for class trials.

“The perception that securities class actions are somehow unsuitable for a jury trial is quickly fading,” Mark Molumphy of Cotchett, Pitre & McCarthy LLP, an attorney for the Twitter investors, said in an email.

The cases also put a fresh lens on companies’ new flexibility to conduct public offerings that require securities claims to go to individual arbitration following a Trump administration policy shift.

“The recent verdicts cut against the rationale for leaving the court system,” said Mohsen Manesh, a business law professor at the University of Oregon. Arbitrating disputes “would probably be worse for corporate defendants than today’s class-action system, which screens weak claims early and offers class-wide finality that arbitration cannot,” he said by email.

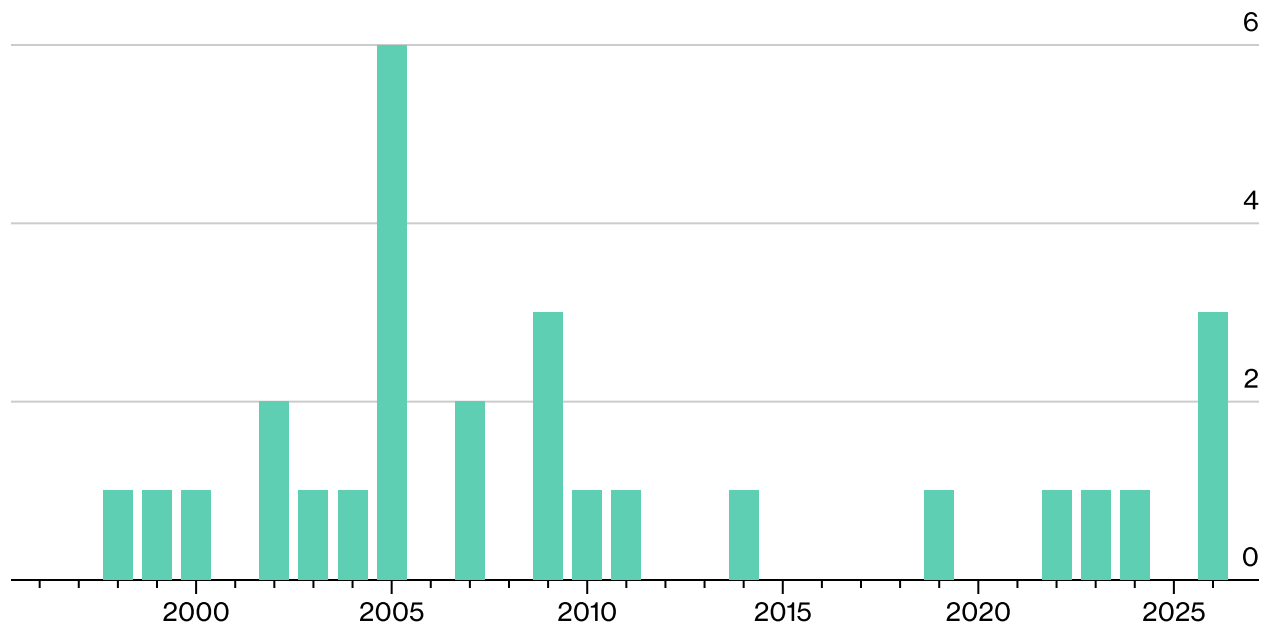
### Rarities

Securities fraud class actions have rarely gone to trial since the passage of the 1995 Private Securities Litigation Reform Act, which transformed the practice area and prompted researchers to collect lawsuit data.

Out of about 7,500 such cases filed in those three decades—as tallied in a January NERA report—fewer than 30 have gone to trial, according to NERA data in a 2017 report, a Bloomberg Law review of cases, and an email from Cornerstone Research.

## Federal Securities Class Actions Rarely Go to Trial

### Cases reaching trial since 1995 Private Securities Litigation Reform Act



Sources: NERA, Bloomberg Law review

Only about 22 reached a verdict—including the three this year.

About two-thirds of the verdicts were at least partially for plaintiffs, and the potential size of a class award helps explain why trials are so rare. Shareholders of an HSBC Holdings Plc unit won a \$2.46 billion judgment in 2013 following a verdict establishing liability. That award was reversed on appeal and the parties settled before a new trial.

There are a few reasons some cases go to trial, said Michael Canty, a plaintiffs' attorney with Labaton Keller Sucharow LLP. "If the right case presents itself, several factors can come together: good jury appeal, strong facts, and an adversary that does not want to meet you in the middle or at mediation."

"I learned early in my career that slam-dunk cases are not the ones that go to trial," Canty said. "Difficult cases go to trial."

### **Trial Wave?**

The recent defense wins highlight the burden on plaintiffs to prove their case by a preponderance of the evidence.

"In a lot of these cases, there's not a smoking gun," said Jimmy McBirney of Scott + Scott Attorneys at Law, who represented the Vaxart investors at trial against hedge fund Armistice Capital LLP. "There's not an email you can point to where the defendant is clearly directing something to happen for an improper purpose and then trading on it or whatnot."

But conversations with the Vaxart jurors after the verdict showed the case was fairly close, McBirney said. "And that's on a case that needed to bridge some really difficult evidence gaps," he said.

Attorneys for Armistice declined to comment for this story. Chuck Connolly, a partner at Akin Gump Strauss Hauer & Feld LLP, called the April 28 verdict an "exoneration" for Armistice and two of its executives.

Attorneys for Musk and the parties in the Exxon case didn't respond to emailed requests for comment.

Despite his clients' loss in the Vaxart case, McBirney said it will "make plaintiffs more inclined to take even just slightly stronger cases to trial."

"I do foresee more of these cases going to trial as attorneys and judges see the benefits of the process," said Molumphy. "As a trial lawyer, if you have a strong case, you want a jury to look the key witness in the eye when they testify. That's true whether you represent a class or a corporate defendant."

Canty said he commends the Exxon investors. "By going the distance, even in a loss, the plaintiffs sent a broader message to the defense bar: plaintiffs' firms are not afraid to take these cases to trial," he said.

### **Arbitration Option**

"The more consequential question is whether companies will stay in the court system at all," Manesh said.

The Securities and Exchange Commission announced last September that it would permit clauses in registration statements that would force investors to resolve claims through arbitration. Plaintiffs' attorneys and investor advocates have criticized the shift as diminishing accountability. Some attorneys see significant downsides for businesses as well. To date, no large companies have adopted such clauses.

But Musk's SpaceX is considering a mandatory arbitration provision as a fallback to a Texas Business Court venue in its forthcoming initial public offering, according to the company's prospectus.

The effect would be to eliminate class actions like the three that went to trial, Manesh said. Smaller investors, "least able to afford arbitration, would lose their remedy," he said. And companies would lose the benefits of the court system, he said.

Molumphy said the jury system works as well for securities class actions as for other cases, citing the three "unanimous verdicts after relatively short, two to three week trials."

"At the end of the day, these are common fraud cases and we found that jurors are well equipped to assess credibility, even in billion dollar cases," he said.

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