

Post-Morrison:

The Global Journey Towards Asset Recovery



NAPPA

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Public Pension Attorneys

By the NAPPA *Morrison* Working Group
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INTRODUCTION

Six years ago the Supreme Court of the United States, by its decision in *Morrison v. National Australia Bank, Ltd.*, 561 U.S. 247 (2010), launched the institutional investor's odyssey into the developing world of non-U.S. securities law and regulation. Understanding the implications of *Morrison* on an investor's ability to recover assets lost due to the malfeasance of others, NAPPA membership began to develop the tools and identify the resources necessary to conduct appropriate risk/reward analysis with respect to the uncharted waters of foreign securities litigation. NAPPA's working group: Securities Litigation, Including Remedies Outside the U.S. published, "Living in a Post-*Morrison* World: How To Protect Your Assets Against Securities Fraud" in June of 2012, which served as a first of its kind guide (the "*Morrison* White Paper").

As institutional investors continue to look for opportunities to invest globally, and given the post-*Morrison* world, it is critical for institutions -- particularly those of us who are fiduciaries and consider a litigation to be an asset of the fund to be treated just like any other asset of the fund in terms of risk, cost and return -- to have a plan in place to consider how best to approach recovery of assets in the event of a loss. Institutional investors have witnessed an increase in foreign group actions abroad for purposes of asset recovery. A number of NAPPA members have participated in these cases. With the first of the post-*Morrison* foreign cases announcing settlements in very recent times, the working group thought this would be a good time to update the *Morrison* White Paper.

The Working Group has created this paper, which provides the current state of various courts' interpretation of *Morrison*; practical considerations for institutional investors when considering foreign actions, the current state of securities laws of 15 foreign jurisdictions; and select foreign case studies, which show how some of the first foreign cases have been resolved and highlight those cases to watch. We hope that this paper will be a useful and educational tool.

As co-chairs of the Working Group, we would like to thank each member of the *Morrison* sub-committee for their efforts over the last several months. Their research, tremendous work and dedication to this project has produced a paper that is extraordinarily valuable and instrumental in helping institutions and practitioners to better understand the state of the securities laws in the post-*Morrison* world.

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***Editorial Support**

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The Shifting Global Landscape Of Securities Fraud Cases





A. LEGAL LANDSCAPE

The *Morrison* Decision

In 2010, the U.S. Supreme Court issued the landmark decision *Morrison v. National Australia Bank Ltd.*, 561 U.S. 247 (2010). *Morrison* has revolutionized the way federal courts interpret the territorial scope of the anti-fraud provisions of the federal securities laws.¹ In *Morrison*, the Supreme Court rejected the “conduct” and “effects” tests for assessing jurisdiction over fraud claims involving foreign exchange-traded securities. Rather than focusing on whether a foreign issuer’s alleged fraudulent conduct occurred or had a substantial effect in the United States, the Supreme Court applied a “transactional test” that examines where the securities are listed, or where the transactions at issue occurred. In doing so, *Morrison* has restricted U.S. lawsuits involving securities listed and traded on foreign exchanges.

The specific question considered by the Court in *Morrison* was whether a claim under Section 10(b) of the Securities Exchange Act of 1934 (the “Exchange Act”) can be brought by foreign plaintiffs suing a foreign issuer for alleged fraud concerning securities traded on a foreign exchange (a so-called “foreign-cubed” case).² In its ruling, the Court noted that Section 10(b) of the Exchange Act does not apply extraterritorially, finding that the Act does not focus on the place where the deception originated, but rather upon “purchases and sales of securities in the United States.”³ Accordingly, the Supreme Court held that Section 10(b) applies only to domestic securities transactions, *i.e.*, “transactions in securities listed on domestic exchanges, and domestic transactions in other securities.”⁴

The impact of *Morrison* has been significant for investors seeking to recover foreign investment losses caused by alleged misconduct. Most obviously, *Morrison* prohibited claims under the anti-fraud provisions of the Exchange Act involving securities listed on foreign exchanges, or for securities transactions executed overseas. This eliminates any Exchange Act recourse for foreign-cubed scenarios, and “foreign-squared” cases (*i.e.*, U.S. investors of foreign securities listed on a foreign exchange), both of which were potentially actionable before *Morrison*. Since *Morrison*, certain lower courts have interpreted the decision broadly to even prohibit actions involving securities cross-listed on U.S. and foreign exchanges.⁵

These courts have generally found such “listing theories” to be overly technical and “contrary to the spirit of *Morrison*.⁶ Other courts have restricted cases involving “domestic transactions” in securities listed on a foreign exchange by focusing on the locus of the *transaction*, rather than the investor’s location or the site of the injury.⁷

Notwithstanding these limitations, the *Morrison* decision has surprisingly not reduced the number of U.S. securities class actions filed against foreign issuers. Such filings have actually increased since the decision was issued in 2010. Specifically, the percentage of U.S. securities class action filings against

¹ George T. Conway, III, *Morrison at Four: A Survey of its Impact on Securities Litigation*, in FEDERAL CASES FROM FOREIGN PLACES, HOW THE SUPREME COURT HAS LIMITED FOREIGN DISPUTES FROM FLOODING U.S. COURTS (U.S. Chamber Institute for Legal Reform, Nov. 2014).

² “Foreign-cubed” actions involve claims in which: (1) foreign plaintiffs are suing (2) a foreign issuer in a U.S. court for violations of U.S. securities laws, (3) based on securities transactions in foreign countries. See *Morrison*, 561 U.S. 247, 271 n.11 (2010).

³ *Id.* at 266.

⁴ *Id.* at 267.

⁵ See *infra* Section I.A.3.



foreign issuers was 21% in 2012, 18% in 2013, 20% in 2014, and 19% in 2015. This represents an increase from the historical average of 11% from 1997-2013.⁸ However, almost all of the lawsuits filed during this period have involved foreign issuers with U.S. listed securities. Accordingly, the *Morrison* decision has necessarily forced U.S. investors to carefully consider alternative jurisdictions when fraudulent conduct adversely affects their foreign exchange-traded securities.

Evolution of Class and Group Actions Abroad – The Rise in Filings in Foreign Jurisdictions: 2010 to 2016

One consequence of the *Morrison* decision has been an increase in the filing of group actions abroad.⁹ The increase in such filings is likely to lead to a further development of group action procedures and remedies in those countries. Indeed, courts in both Canada and The Netherlands (which previously had class or group action mechanisms) have specifically noted that, after *Morrison*, claimants need to have a means of redress in their home countries for securities fraud.¹⁰ Given the extraterritorial limitations of the U.S. securities laws under *Morrison* and its progeny, investors are now required to develop a comprehensive understanding of these alternative mechanisms for group actions in foreign jurisdictions.

It is apparent that investor interest in jurisdictions outside of the United States has increased in the past several years. For instance, in Canada, 11 securities class actions were filed in 2013, 13 were filed in 2014 and seven were filed in 2015.¹¹ By the end of

⁸ Securities Class Action Filings: 2015 Year in Review, CORNERSTONE RESEARCH, 15 (2015), <https://www.cornerstone.com/GetAttachment/c8a2df79-cde2-4494-b771-39fd3fa55ad9/Securities-Class-Action-Filings-2015-Year-in-Review.pdf>.

⁹ Kevin LaCroix, *Morrison v. National Australia Bank: An Important Decision About the Reach of the U.S. Securities Laws*, LXBN (Dec. 18, 2015), <http://www.lxbn.com/2015/12/18/morrison-v-national-australia-bank-an-important-decision-about-the-reach-of-the-u-s-securities-laws/>.

10 *Id.* at 1.

¹¹ *Trends in Securities Class Actions: 2015 Update*, NERA ECONOMIC CONSULTING, (Feb. 11, 2016), <http://www.nera.com/publications/archive/2016/trends-in-canadian-securities-class-actions--2015-update.html>.

2014 there were 60 securities cases pending in Canada, representing more than twice the number of pending actions in 2007. Australia has also experienced a rise in the number of securities class action cases filed recently. Between 2014 and 2015, at least ten such cases were filed, with further actions still anticipated.¹² Moreover, the increase in private third-party litigation funding in Australia also suggests a likely expansion of class action securities litigation in that country. There has also been growing investor enthusiasm to pursue securities class actions in the United Kingdom, where litigation funding has developed and a new class action regime has been introduced (pursuant to the Consumer Rights Act of 2015, which took effect on 1 October 2015).¹³ In addition, the Netherlands has become a venue more frequently considered by plaintiffs seeking relief on a class-wide basis, as well as defendants interested in a binding resolution for global investor claims.¹⁴

There are a variety of alternatives to the U.S. class action system in certain foreign jurisdictions. For instance, Canada utilizes a U.S.-style “opt-out class action,” where investors are bound by a court-approved settlement unless they explicitly opt-out.¹⁵ Australia utilizes group actions that are similar to an “opt-in” system, where investors must explicitly opt into a settlement on behalf of a plaintiff group before they are bound by the settlement terms.¹⁶ Other alternatives

¹² King & Wood Mallesons, *The Review: Class Actions in Australia 2014/2015* (Aug. 18, 2015).

¹³ Herbert Smith Freehills LLP, *UK Class Action Market Heating Up in 2016*, LEXOLOGY (Apr. 13, 2016), <http://www.lexology.com/library/detail.aspx?g=978dfaf9-1ac6-418c-8b40-94ce27128606>. See also *infra* Section III (England & Wales).

¹⁴ Joni Jacobsen et al., *US \$1.3 Billion Fortis Settlement Ushers in New Era in Globalization of Securities Laws*, BUS. ADVISOR (Mar. 21, 2016), <http://www.jdsupra.com/legalnews/us-1-3-billion-fortis-settlement-ushers-55928/> (discussing global settlement of securities claims against Belgium-based Fortis Bank using Dutch collective settlement procedures).

¹⁵ FINANCIAL RECOVERY TECHNOLOGIES, *Morrison v. National Australia Bank Changes Global Landscape*, 2 (2012), <http://frtservices.com/wp-content/uploads/2012/09/FRT-International-Group-Securities-Litigation-White-Paper-2012.pdf>. See also *infra* Section III (Canada).

¹⁶ *Id.* (citing *Hadchiti v. Nufarm Ltd.* [2011] FCA VID24/2011 (Austl.); *Verbatt Pty Ltd. v. Nufarm Ltd.* [2010] FCANSID1847/2010 (Austl.)). See also *infra* Section III (Australia).



include: (i) collective actions, where investors must join as members of a pre-existing representative organization (*i.e.*, an investor protection association) that can represent a large body of complainants (used in Germany); and (ii) joinder of claims, a non-representative mechanism where similar complainants are joined into one case with all plaintiffs listed individually (a prevalent device used in Japan).¹⁷

In addition, the United Kingdom, Australia, Canada, Germany, South Korea, Mexico, The Netherlands, and Taiwan have all adopted procedures that allow for the adjudication of multiple securities fraud claims at once.¹⁸ Litigation in these jurisdictions may now present a viable alternative to filing suit in U.S. courts.¹⁹

Recent Applications of the *Morrison* Test by the Courts

Some recent court decisions have provided additional guidance on *Morrison* and its application to Section 10(b) claims.

Absolute Activist Value Master Fund Ltd. v. Ficeto

In *Absolute Activist Value Master Fund Ltd. v. Ficeto*, the Second Circuit Court of Appeals defined what constitutes a “domestic securities transaction” of non-U.S. listed securities under *Morrison*.²⁰ The district court in *Absolute Activist* considered whether there were actionable Section 10(b) claims for plaintiffs who purchased penny stocks traded on U.S. over-the-counter (“OTC”) markets. The district court found *Morrison* barred an Exchange Act claim for these purchases because the securities were not listed on a U.S. exchange, and plaintiffs purchased directly from the foreign issuers.

On appeal, the Second Circuit clarified that Section 10(b) applies to “domestic transactions” of securities that are not listed on a U.S. exchange only if: (i) an irrevocable liability to purchase or sell the security is incurred in the United States; *or* (ii) title to the security was transferred in the United States. First, the court found that purchasing or selling a security is equal to entering into a binding contract to purchase or sell. Thus, a domestic transaction exists only if the “purchaser incurred irrevocable liability in the United States to take and pay for a security, or the seller incurred irrevocable liability within the United States to deliver a security.”²¹ Second, the court found that a “sale” consists of the passing of title from the seller to the buyer for a price. Accordingly, the court held that a securities transaction is considered “domestic” if title to that security was transferred within the United States.²² If either prong of the *Absolute Activist* test is satisfied, an investor may bring a Section 10(b) claim in the Second Circuit even if the underlying security is not listed on a U.S. exchange.

In re Petrobras Securities Litigation

Another court within the Second Circuit has recently applied the *Absolute Activist* test to provide further clarification on the “domestic transaction” prong of *Morrison*. In *In re Petrobras Securities Litigation*, the district court examined Exchange Act claims involving the purchase of debt securities (“Notes”) of a Brazilian oil company, Petróleo Brasileiro S.A., or Petrobras (“Petrobras”).²³ Plaintiffs argued that the Notes were traded on the OTC “bond market,” and thus satisfied the second prong of the *Morrison* test (*i.e.*, a “domestic transaction” in securities not listed on a U.S. exchange). Judge Jed Rakoff of the U.S. District Court for the Southern District of New York found that two U.S. pension fund plaintiffs (North Carolina Department of State Treasurer and the Employees’ Retirement System of the State of Hawaii) adequately pled that irrevocable liability was incurred in the United

¹⁷ Fin. Recovery Techs., *supra* n. 15, 3-4. See also *infra* Section III (Japan).

¹⁸ William F. Sullivan *et al.*, *A Global Concern: The Rise of International Securities Litigation*, BLOOMBERG LAW (Apr. 8, 2013), <http://www.bna.com/a-global-concern-the-rise-of-international-securities-litigation/>. See also *infra* Section III (The Netherlands).

¹⁹ See *infra* Section III.

²⁰ 677 F.3d 60, 66 (2d Cir. 2012).

²¹ *Id.* at 67-68.

²² *Id.*

²³ No. 14-cv-9662 (JSR), 2015 WL 9266983 (S.D.N.Y. Dec. 20, 2015).



States because they purchased the Notes from New York-based underwriters.

However, the court rejected the claims of certain non-U.S. funds who only alleged that their Note transactions took place in the United States without any factual detail. The district court also dismissed the claims of a U.K.-based fund that merely alleged that the Notes were transferred from its U.S.-based affiliate. Here, the court found that irrevocable liability was actually incurred in the United Kingdom, where these plaintiffs were located.²⁴ The court also rejected plaintiffs' argument that the *Absolute Activist* test was satisfied because beneficial ownership, rather than legal title, was transferred in the United States. Plaintiffs asserted that title was effectively transferred in the United States because their Note purchases were settled through the Depository Trust Company ("DTC") in New York. Judge Rakoff found this argument unpersuasive, noting that "[t]he mechanics of DTC settlement . . . involve neither the substantive indicia of a contractual commitment necessary to satisfy *Absolute Activist*'s first prong nor the formal weight of a transfer of title necessary for the second."²⁵

Lastly, two of the non-U.S. plaintiffs argued that irrevocable liability was incurred in the United States because they purchased the Notes "on the offering date and at the offering price," and all underwriters who sold in the initial offerings only did so in the United States. The court disagreed. Although the supplemental offering prospectuses indicated that some Notes were initially offered in the United States, they did not state that they were *exclusively* offered in the United States. Instead, the court found the prospectuses actually implied that some underwriters initially offered the Notes outside of the United States. Therefore, even if plaintiffs only purchased the Notes in the initial offerings, this was still insufficient to satisfy the "domestic transaction" test in *Morrison*.²⁶

In re UBS Securities Litigation

Other recent court decisions have provided additional guidance on the "cross-listing" theory for satisfying *Morrison*. For example, in *In re UBS Securities Litigation*, the district court dismissed claims brought by foreign plaintiffs who purchased UBS stock on foreign exchanges.²⁷ Plaintiffs argued that their "foreign-cubed" claims were actionable under *Morrison* because the securities purchased on foreign exchanges were also cross-listed on a U.S. exchange (the NYSE).

Plaintiffs argued that transactions in securities registered on a U.S. exchange fell within the purview of Section 10(b) of the Exchange Act, regardless of where the trade was actually executed. The district court disagreed. In rejecting the cross-listing theory, the court held that plaintiffs selectively quoted from *Morrison*, and ignored its main "spirit," namely, a focus on the location of the securities *transaction*, and not the location of an exchange where the security may be dually listed.²⁸ The court also noted that *Morrison* clearly intended to limit the extraterritorial reach of Section 10(b), not expand it as plaintiffs' approach would do.

The Second Circuit later affirmed in *City of Pontiac Policemen's and Firemen's Retirement System v. UBS AG*, holding that Plaintiffs' "listing theory" may be supported when viewed in isolation, but is irreconcilable with *Morrison* as a whole.²⁹ The circuit court reiterated that *Morrison* concerned the location of the securities transaction itself, and not the location of an exchange where the security may be dually listed. Moreover, the Second Circuit emphasized that the Supreme Court's focus in *Morrison* was on domestic transactions, thereby rejecting the notion "that the *national* public interest pertains to transactions conducted upon *foreign* exchanges and markets."³⁰ The *City of Pontiac* decision has confirmed that cross-

²⁴ *Id.*

²⁵ *Id.* at *4.

²⁶ See *infra* Section IV for discussion on foreign litigation adverse Petrobras.

²⁷ No. 07-Civ-11225 (RJS), 2011 WL 4059356 (S.D.N.Y. Sept. 13, 2011).

²⁸ *Id.* at *5.

²⁹ 752 F.3d 173, 180 (2d Cir. 2014).

³⁰ *Id.* (citing *Morrison*, 561 U.S. at 263).



listing theories are unlikely to be cognizable under *Morrison*.

Parkcentral Global Hub Ltd. v. Porsche Automobile Holdings SE

Another recent interpretation of *Morrison* by the Second Circuit is its decision in *Parkcentral Global Hub Ltd. v. Porsche Automobile Holdings SE*.³¹ In *Parkcentral*, more than thirty international hedge fund plaintiffs invested in “securities-based swap agreements” linked to the ordinary stock of Volkswagen AG (“VW” or “Volkswagen”), which traded on foreign exchanges.³² The plaintiffs (whose investment managers were located in the United States) sued Porsche Automobile Holding SE (“Porsche”) for misrepresenting its intention to acquire a controlling interest in VW stock. The fraudulent statements were made primarily in Germany, and the foreign defendants had no involvement in the plaintiffs’ swap transactions. While the plaintiffs alleged that they entered into the swap agreements in the United States, the VW shares referenced in the swaps appeared to trade only on foreign exchanges.

The Second Circuit affirmed dismissal of the plaintiffs’ claims under *Morrison*, holding that while a domestic securities transaction is necessary, it is insufficient, standing alone, to state a domestic claim under Section 10(b) of the Exchange Act. The court focused on where the alleged fraudulent conduct occurred (Germany), and, accordingly, found this nexus insufficient under *Morrison*.³³ The Second Circuit further noted that its decision does not foreclose future litigation regarding domestic swap transactions in foreign securities where the foreign defendants are alleged to have sufficiently subjected themselves to Section 10(b).

Atlantica Holdings, Inc. v. BTA Bank JSC

The decision in *Atlantica Holdings, Inc. v. BTA Bank JSC* provides an additional gloss on the “domestic

securities transaction” prong of the *Morrison* test.³⁴ The plaintiffs in *Atlantic Holdings* were Panamanian corporations that purchased subordinated debt securities relating to the restructuring of defendant BTA Bank JSC, a bank in Kazakhstan. Plaintiffs argued that, under *Absolute Activist*, irrevocable liability was incurred or title was transferred in the United States because they “communicated their commitment to participate in [defendant’s] restructuring by sending . . . completed ‘Electronic Instruction Forms’ [‘EIFs’] to their brokers in the Miami, Florida, Office of UBS Financial Services.”³⁵ More specifically, plaintiffs explained that once they agreed to purchase the debt securities, the UBS Miami Office transferred the funds to the UBS back office in Connecticut, where the order was filled and the transactions were completed.

The court agreed. In doing so, it distinguished these facts from *City of Pontiac*, where the securities order was placed in the United States, but executed on a foreign exchange. By contrast, the initial purchases in *Atlantica* were not executed on a foreign exchange, and the secondary market transactions were executed in Connecticut. Likewise, the court distinguished *Parkcentral* on grounds that the debt securities at issue were fundamentally different from the securities-based swaps present in *Parkcentral*.³⁶ The court in *Atlantica* also rejected defendant’s argument that the EIFs were likely sent from Panama, where plaintiffs were located, and thereby demonstrating that irrevocable liability was incurred abroad (*i.e.*, the “mailbox rule”). The court found no indication that the EIFs became binding when sent, as opposed to when plaintiffs’ brokers in Miami sent them to UBS in Connecticut. In sum, the *Atlantica* court found that plaintiffs had satisfied *Morrison* and *Absolute Activist*.

United States v. Georgiou

The Third Circuit Court of Appeals’ decision in *United States v. Georgiou* provided a notable recent analysis of *Morrison* in the criminal context.³⁷

³¹ 763 F.3d. 198 (2d Cir. 2014).

³² *Id.* at 201.

³³ *Id.* at 216.

³⁴ *Id.* at *7.

³⁵ *Id.*

³⁶ No. 13-CV-5790 (JMF), 2015 WL 144165 (S.D.N.Y. Jan. 12, 2015).

³⁷ 777 F.3d 125, 131 (3d Cir. 2015).



In *Georgiou*, the Third Circuit held that the purchase and sale of securities issued by U.S. companies, through U.S. market makers acting as intermediaries, constituted a “domestic transaction” under *Morrison*. In the case, defendant and his co-conspirators were convicted under Section 10(b) for scheming to manipulate the markets of four U.S.-issued stocks that were traded on OTC markets. To do so, the co-conspirators opened brokerage accounts in foreign jurisdictions through U.S. market makers to give the false impression that there was an active market in each of the stocks.³⁸ While the co-conspirators were able to sell their shares at artificially inflated prices, the accounts experienced severe trading losses over time.

The defendant argued that his securities fraud conviction was improperly based on the extraterritorial application of Section 10(b) because there was no evidence that any of the subject securities transactions occurred in the United States. However, the Third Circuit found that because some of the fraudulent transactions were executed through U.S.-based market makers, irrevocable liability was incurred in the United States.³⁹ This ruling suggests that OTC trades executed through U.S. entities acting as intermediaries for foreign entities may well be cognizable under *Morrison*.⁴⁰

Mark Stoyas, et al. v. Toshiba Corporation

The *Toshiba* decision provides another recent judicial interpretation of the *Morrison* test. On May 20, 2016, the United States District Court for the Central District of California dismissed class action claims against the Japanese company, Toshiba Corporation (“Toshiba”), alleging violations of Sections 10(b) and 20(a) of the Exchange Act, as well as claims under Japan’s Financial Instruments & Exchange Act (“FIEA”).⁴¹ The complaint alleged that defendants sold stock, including American Depository Shares, or ADSs, at an inflated price caused by defendants’ false

profit reports. Defendants allegedly used improper accounting methods for over six years to inflate pre-tax profits by more than \$2.6 billion, and conceal losses of at least \$1.3 billion. After Toshiba restated more than six years of reported financial results that eliminated approximately a third of the profits it reported from 2008 to 2014, the price of Toshiba securities declined by more than 40%, resulting in a loss of \$7.6 billion. The class included: (i) all persons who acquired Toshiba ADSs between May 8, 2012 and November 12, 2015 (“Class Period”); and (ii) all citizens and residents of the United States who otherwise acquired shares of Toshiba common stock during the Class Period.

Defendants argued that plaintiffs’ claims did not meet the *Morrison* test, as plaintiffs could not show that they purchased a Toshiba security listed on a U.S. exchange, or that Toshiba was involved in any domestic securities transaction, such as trading ADSs in the U.S. In addressing the first prong in *Morrison*, defendants argued that the ADSs at issue were not listed on a national stock exchange, but rather, on an OTC market, a distinction noted in *Georgiou*. Defendants cited to a recent Third Circuit decision which noted that because the Exchange Act explicitly references both OTC markets and securities exchanges separately, the statute recognizes a distinction between the two.⁴² Accordingly, the court found that OTC markets were not the domestic exchanges contemplated by *Morrison*, and thus concluded that Toshiba did not list securities on a domestic exchange.

Defendants also asserted that plaintiffs’ claims did not meet the second prong of the *Morrison* test because Toshiba was not involved in any domestic transaction of ADSs in the U.S. Instead, a depositary bank purchased the underlying Toshiba common stock on a foreign exchange, and then sold the ADSs to plaintiffs in the U.S. Because Toshiba was not involved in this transaction, Defendants argued that the claims should be dismissed under *Morrison*. The district court agreed. In reaching its conclusion, the court held that it is ultimately the depositary bank that holds the underlying security and sells the ADS, and

³⁸ *Id.* at 131.

³⁹ *Id.* at 136.

⁴⁰ Dan Gold, *et al.*, *Guest Post: Year in Review: Securities Litigation*, D&O DIARY (Feb. 29, 2016), <http://www.dandodairy.com/2016/02/articles/securities-litigation/guest-post-year-in-review-securities-litigation/>.

⁴¹ *Mark Stoyas, et al. v. Toshiba Corporation*, No. 15-cv-04194 (C.D. Cal.).

⁴² *Georgiou*, 777 F.3d at 134-35 (noting that the Exchange Act “refers to ‘securities exchanges’ and ‘over-the-counter markets’ separately, which suggests that one is not inclusive of the other”).



thus the bank has the rights indicative of ownership. Furthermore, the sales of the ADSs by the depositary bank were made without any connection to Toshiba, and the securities were not listed on domestic exchanges. Therefore, the court concluded that the transactions at issue did not fall under the second prong of *Morrison*. The court found that permitting Section 10(b) claims based on the independent actions of depositary banks selling on OTC markets would create limitless liability, which is inconsistent with the spirit of *Morrison*.

Lastly, the district court dismissed claims asserted under Japanese law. Applying the principle of comity, the court found that Japan's interest in adjudicating the dispute outweighed the United States' interest. The court noted that the public statements and omissions were made in Japan by a Japanese corporation, that Toshiba's executives are overwhelmingly citizens and residents of Japan, that the majority of Toshiba stockholders are Japanese citizens, and that the Japanese government has spoken publicly about the ramifications of Toshiba's accounting revelations. Additionally, there are at least three pending lawsuits against Toshiba pursuant to Article 21-2 of the Japanese Exchange Act.⁴³

B. THE EFFECT OF MORRISON ON ADRS

The most common method for U.S. investors to purchase foreign securities in the United States is through American Depository Receipts, or ADRs.

ADRs Generally

An ADR is a negotiable instrument issued by a depositary bank representing beneficial ownership in a certain number of ordinary shares of a foreign stock that trades on a U.S. exchange. The underlying shares of the foreign issuer, which are represented by the ADR in the United States, are referred to as American Depository Shares, or ADSs, and are held by a custodian bank in the issuer's home country.⁴⁴

ADRs simplify the purchase and sale of foreign securities for U.S. investors by eliminating foreign regulatory and currency exchange issues inherent in trading foreign-registered securities overseas. ADRs can be freely traded between U.S. investors through depositary banks in the same manner as other U.S. securities (*i.e.*, trades are settled and cleared in the United States). This avoids inconvenient foreign securities transfer procedures and varying registration requirements present in many foreign countries. ADRs are also quoted and traded in U.S. dollar denominations, and dividends and the underlying foreign shares are paid in dollars and transmitted by the depositary banks directly to ADR holders. The depositary banks also inform ADR holders of the foreign company's recapitalization plans, security exchange offers, proxy voting matters, and other significant company developments.

Generally, there is no difference between owning an ADR and owning the underlying shares of a foreign issuer. U.S. investors should exercise caution, however, when purchasing ADRs, as ADRs do not eliminate the currency, economic and political risks for the underlying shares in the foreign country. Further, the laws of the foreign issuer's home country may affect various shareholder rights, including voting rights and proxy limitations. An additional element of risk stems from the fact that each ADR is subject to the terms of a depositary agreement between the foreign issuer and the U.S. depositary bank.

Overall, ADRs have allowed U.S. investors to diversify their portfolios through increased international investments without the expense of using a foreign broker or depositary. As ADR programs continue to grow, they will become increasingly important investments for U.S. pension systems and other institutional investors. Accordingly, their treatment under *Morrison* and its progeny is an important issue going forward.

Types of ADRs

ADRs fall into two basic categories: (i) “unsponsored”; and (ii) “sponsored.” Each category has different characteristics and regulatory requirements

⁴³ See *infra* Section III.J.

⁴⁴ Each ADR generally represents one or more ADS, and each ADS represents a number or fraction of underlying shares in the foreign company.



under U.S. securities laws, which are briefly discussed below.

Unsponsored ADRs

Unsponsored ADRs are issued by a depositary bank without the participation or consent of the foreign issuer of the underlying securities. ADRs (both unsponsored and sponsored), however, cannot be issued unless the foreign company is either: (i) subject to the periodic reporting requirements of the Exchange Act; or (ii) exempt from such reporting requirements under Rule 12g3-2(b) of the Exchange Act.⁴⁵

Unsponsored ADRs are not listed on U.S. securities exchanges, and only trade on the OTC market. The U.S. OTC market consists of a large network of broker-dealers that hold securities inventories to buy and sell for their own accounts or their customers' accounts. There are usually several broker-dealers making a market in a given OTC-traded ADR at a given time. Company information and prices for OTC-traded ADRs can be found in the National Quotation Bureau's "pink sheets," or the OTC Bulletin Board. Both provide wholesale price quotes for OTC stocks listed by market makers in individual securities.

Often more than one depositary bank issues the same unsponsored ADR because they are created without the consent of the foreign issuer of the underlying securities. The unilateral ability of depositary banks to issue unsponsored ADRs (assuming the above requirements are satisfied) allows them to quickly respond to increased U.S. investor/broker demand for a particular foreign issuer's equity securities. However, depositary banks issuing unsponsored ADRs have no obligation to provide investors with information or shareholder communications from the foreign issuers

of the underlying securities. There are also no additional reporting requirements under U.S. securities laws for unsponsored ADRs traded on the OTC market.

The foreign issuer has no formal agreement with a U.S. depositary bank; foreign issuers may, however, maintain informal relationships with a number of depositary banks. As a result, any number of depositary banks can create ADRs for the foreign issuer and they do so based on market demands (if there is demand for a specific ADR, the depositary bank can purchase shares of the foreign issuer on its home exchange, transfer them to its local custodian, and issue corresponding ADRs in the United States). It is important to note, though, that each ADR is specific to the depositary bank that issued it, so an unsponsored ADR issued by BNY Mellon is not interchangeable with an unsponsored ADR issued by Citibank. This lack of interchangeability can often make trading more cumbersome (a problem that does not exist with sponsored ADRs, which all come from the same depositary bank).

As of May 2016, there are over 1,500 unsponsored ADRs traded on U.S. OTC markets, including unsponsored ADRs for China Construction Bank, L'Oreal SA, LVMH Moet Hennessy Louis Vuitton SA, and Bayerische Motoren Werke AG (commonly known as BMW). Ultimately, unsponsored ADRs may be considered less favorable to U.S. investors given the lack of information and control by the foreign issuers.

Sponsored ADRs

Sponsored ADRs are issued by a depositary bank pursuant to an agreement with the foreign issuer of the underlying equity securities ("deposit agreement"). Sponsored ADRs are issued by a single depositary bank, often with the financial assistance and at the direction of the foreign securities issuer. There are three levels of sponsorship. Levels I and II relate to foreign shares already issued, and are designed to create a U.S. trading market for these outstanding foreign shares. Level III ADRs concern new offerings of foreign securities. Each level involves varying registration and reporting requirements under U.S. securities laws.

⁴⁵ 17 C.F.R. § 240.12g3-2(b). Rule 12g3-2(b) of the Exchange Act provides an automatic exemption from the registration and reporting requirements of the Exchange Act if the foreign private issuer: (i) has not publicly offered or listed securities in the United States; (ii) has a class of securities traded in a non-U.S. jurisdiction representing over 55% of the issuer's worldwide trading volume; and (iii) has electronically published English translations of material information made public or filed with securities exchanges under the laws of its home country (e.g., annual reports, interim financial statements, and press releases).



Level I ADRs are not listed on U.S. exchanges and are traded on the OTC market only. Consequently, Level I ADRs are not required to be registered under Section 12(b) of the Exchange Act. There is also no requirement to register Level I ADRs under Section 12(g) of the Exchange Act, assuming the requirements of Rule 12g3-2(b) are met. Level I ADRs also have minimal U.S. Securities and Exchange Commission (“SEC”) reporting requirements, *i.e.*, the foreign issuer is not required to issue quarterly or annual reports in compliance with U.S. Generally Accepted Accounting Principles (“GAAP”).

Notwithstanding these exemptions, the depositary bank issuing Level I ADRs must still register the ADRs under the Securities Act of 1933 (the “Securities Act”). This registration statement (“SEC Form F-6”) does not require comprehensive information regarding the foreign company and is usually limited to a copy of the deposit agreement and ADR certificate.

Level I ADRs are appealing to foreign companies that want to introduce their securities to U.S. capital markets without subjecting themselves to the listing and registration requirements involved in an initial public offering in the United States.

Level II ADRs are listed and traded on U.S. securities exchanges (*i.e.*, the NYSE or the NASDAQ). A foreign company issuing Level II ADRs must meet the registration requirements of both the Exchange Act and the Securities Act. Specifically, Level II ADRs require the filing of a Form F-6 and the more comprehensive annual registration statement under Form 20-F of the Exchange Act. Form 20-F requires essentially the same level of detailed information as an annual report on Form 10-K for a U.S. company. A foreign company sponsoring Level II ADRs is also required to follow either U.S. GAAP or International Financial Reporting Standards (“IFRS”) in its reported financial statements. In addition, the foreign company must comply with the financial reporting requirements of the Sarbanes-Oxley Act of 2002 (“Sarbanes-Oxley”).

Level II ADRs have the advantage of being traded on the more widely accessible U.S. securities exchanges, and provide greater disclosures about a

foreign company to U.S. investors. Level II ADRs traded on U.S. exchanges do not involve any newly issued common stock of the foreign company (*i.e.*, they are limited to the currently issued and outstanding stock of the foreign company).

Level III ADRs are listed and traded on U.S. securities exchanges, but unlike Level II ADRs, they represent new shares of the foreign company that are being publicly offered to raise capital in the United States. Thus, a foreign company issuing Level III ADRs is not simply allowing outstanding shares from its home market to be deposited (and traded) with a depository bank in the United States; it is issuing new shares into the U.S. market.

Accordingly, Level III ADRs have more stringent reporting and registration requirements than Level II ADRs. Level III ADRs require the filing of a Securities Act registration statement under Form F-1, which provides detailed company information akin to an offering prospectus for new shares. The filing of a Form F-6 under the Securities Act is also required for Level III ADRs. In addition, the foreign company must file a Form 20-F under the Exchange Act and must comply with the accounting standards of U.S. GAAP or IFRS. Any material company information provided to shareholders under relevant securities regulations in the foreign market must also be filed with the SEC through Form 6-K under the Exchange Act. Level III ADRs also require compliance with Sarbanes-Oxley.

Level III ADRs tend to generate greater interest by U.S. investors given the more regulated nature of these securities and the fact that they involve raising new capital by foreign securities issuers.

As of May 2016, over 2,100 sponsored ADRs were traded on U.S. exchanges and OTC markets. Among them were such foreign powerhouses as Toyota Motor Corp., Samsung Electronics Co. Ltd, HSBC Holdings PLC, and Royal Dutch Shell PLC.

Surviving the Jurisdictional Hurdle of Morrison’s Transactional Test

ADRs may prove to be an institutional



investor's best tool for circumventing the jurisdictional limits imposed by *Morrison*'s transactional test when investing in foreign companies. Most post-*Morrison* courts have treated sponsored ADRs favorably, largely excluding them from their jurisdictional analysis.⁴⁶ Given their varied forms though, it is not surprising that some lower courts have struggled to properly apply *Morrison*'s transactional test to certain classes of ADRs. For example, in September 2010, the U.S. District Court for the Southern District of New York dismissed the Section 10(b) claims of purchasers of unlisted ADRs *sua sponte* in *In re Societe General Securities Litigation*, despite engaging in only limited analysis and applying a questionable understanding of the ADRs at issue.⁴⁷

There is little dispute regarding whether Level II and III sponsored ADRs satisfy the *Morrison* transactional test. Such transactions plainly meet the first prong of the test because they involve securities "listed on an American stock exchange." While no reported decision has yet specifically applied the *Morrison* transactional test to Level II and III ADRs, the absence of such case law should not be interpreted to suggest that the question remains open. Rather, litigants already recognize that Level II and III ADR purchases satisfy the first prong of the *Morrison* transactional test and have refrained from seeking dismissal of claims related to such securities.

For example, in *In re BP p.l.c. Securities Litigation*, defendants successfully raised a *Morrison* defense against claims by individuals who had purchased BP shares on the London Stock Exchange. The *In re BP* defendants, however, raised no such

⁴⁶ See, e.g., *Alstom*, 741 F. Supp. 2d at 471 (excluding ADRs from *Morrison* analysis); *Cornwell v. Credit Suisse Grp.*, 729 F. Supp. 2d 620, 622 (S.D.N.Y. 2010) (same); *Stackhouse v. Toyota Motor Co.*, No. CV 10-0922, 2010 WL 3377409, at *2 (C.D. Cal. July 16, 2010) (appointing ADS investor lead plaintiff in a post-*Morrison* case).

⁴⁷ See *In re Societe Generale Sec. Litig.*, No. 08 CIV. 2495 (RMB), 2010 WL 3910286, at *6 (S.D.N.Y. Sept. 29, 2010).

defense against individuals who had purchased BP's ADRs listed on U.S. exchanges.⁴⁸

Divining whether Level I sponsored ADRs or unsponsored ADRs – neither of which are "listed on an American stock exchange" – satisfy the *Morrison* transactional test presents a greater challenge. The answer will likely hinge on how courts characterize the securities at issue.

Two decisions discussed in Section I.A.3 above provide important guideposts for predicting the treatment of Level I sponsored ADRs and unsponsored ADRs. Taken together, they suggest that Level I sponsored ADRs should satisfy *Morrison*, but unsponsored ADRs will not.

ADRs may prove to be an institutional investor's best tool for circumventing the jurisdictional limits imposed by Morrison's transactional test when investing in foreign companies.

As discussed in more detail above, in *Absolute Activist*, the Second Circuit addressed the circumstances under which "the purchase or sale of a security that is not listed on a domestic exchange should be considered 'domestic' within the meaning of *Morrison*."⁴⁹ The court determined that securities transactions are domestic when, within the United States, the parties incur irrevocable liability to conduct transactions or when title is passed.⁵⁰

In *Parkcentral*, also discussed above, the Second Circuit found that securities-based swap agreements executed in the United States did not satisfy *Morrison*'s transactional test because the agreements at issue were private contracts executed by the plaintiffs and a third party. While the swaps related to the price of VW stock traded on foreign exchanges, VW was not a party to the contract and had no connection to the transaction. Moreover, no shares of VW stock exchanged hands between the parties to the swap agreement. Under these facts, the Second Circuit held that the *Morrison*

⁴⁸ *In re BP p.l.c. Sec. Litig.*, 843 F. Supp. 2d 712, 794 (S.D. Tex. 2012).

⁴⁹ *Absolute Activist Value Master Fund Ltd. v. Ficeto*, 677 F.3d at 60, 66-67 (2d Cir. 2012).

⁵⁰ See *id.* at 69.



transactional test was *necessary*, but not *sufficient*, to trigger the application of U.S. securities laws to foreign issuers. Specifically, the court found:

If the domestic execution of the plaintiffs' agreements could alone suffice to invoke § 10(b) liability with respect to the defendants' alleged conduct in this case, then it would subject to U.S. securities laws conduct that occurred in a foreign country, concerning securities in a foreign company, traded entirely on foreign exchanges, in the absence of any congressional provision addressing the incompatibility of U.S. and foreign law nearly certain to arise. That is a result *Morrison* plainly did not contemplate and that the Court's reasoning does not, we think, permit.⁵¹

Accordingly, the court determined that it must also examine the “character” of the security at issue to properly assess whether the application of the U.S. securities laws is “appropriately domestic or impermissibly extraterritorial.”⁵²

It is likely that transactions involving Level I ADRs will satisfy the *Morrison* transactional test when viewed through the prism of *Absolute Activist* and *Parkcentral*. Specifically, Level I ADRs meet the standard set forth in *Absolute Activist* because they are issued by a U.S. depository bank and traded in the United States on the OTC market. Provided the purchaser is located in the United States, the parties will invariably “incur irrevocable liability to carry out the transaction within the United States” or pass title within the United States.⁵³

In addition, in light of *Parkcentral*, transactions involving Level I ADRs are arguably sufficiently domestic to warrant the application of U.S. securities laws. First, the foreign sponsors at issue have affirmatively sought out the U.S. market by sponsoring Level I ADRs through a U.S. depository

bank. Second, the U.S. depository bank must register the securities with the SEC. Level I ADRs, therefore, exhibit all the hallmarks of a domestic security and have been created with the consent and participation of the foreign sponsor. As a result, the foreign sponsors of Level I ADRs are precisely the sort of entities to which extraterritorial application of the U.S. securities laws is appropriate.

Moreover, applying the U.S. securities laws to the sponsors of Level I ADRs would not undercut the Supreme Court’s rationale for creating the transactional test. As discussed above, in applying *Morrison*, courts have stressed the legal concerns and priorities that underpin the Supreme Court’s decision.⁵⁴ Notably, post-*Morrison* courts have given great weight to the various goals espoused by the Supreme Court, including respect for international comity.⁵⁵ In part, the Supreme Court cautioned that extraterritorial application of U.S. securities laws to foreign companies had the potential for wreaking havoc on foreign regulatory regimes by creating a morass of competing laws.⁵⁶

None of the Supreme Court’s concerns, however, are implicated by providing U.S. courts with extraterritorial jurisdiction over the foreign sponsors of ADRs because they have affirmatively sought out access to U.S. capital markets and U.S. investors.⁵⁷

⁵⁴ See, e.g., *Morrison*, 561 U.S. at 268-70; *In re Banco Santander Sec.–Optimal Litig.*, 732 F. Supp. 2d 1305, 1317 (S.D. Fla. 2010) (citing the concerns underpinning *Morrison*), aff’d sub nom. *Inversiones Mar Octava Limitada v. Banco Santander S.A.*, 439 F. App’x 840 (11th Cir. 2011); *Stackhouse*, 2010 WL 3377409, at *1 (same).

⁵⁵ See *Morrison*, 561 U.S. at 268-70.

⁵⁶ See *id.*

⁵⁷ See *Stackhouse*, 2010 WL 3377409, at *1 (interpreting *Morrison*’s definition of “domestic transactions” to include “purchases and sales of securities explicitly solicited by the issuer within the United States”). The U.S. District Court for the Southern District of New York recently provided similar analysis:

When a foreign issuer decides to access U.S. capital markets by listing and trading ADRs, it subjects itself to SEC reporting requirements, and it would not be illogical to subject that company to the antifraud provisions of the Exchange Act at least where there is a sufficient nexus to the United States.

In re Vivendi Universal, S.A. Sec. Litig., 765 F. Supp. 2d 512, 529 (S.D.N.Y. 2011).



Such calculated decisions have significant consequences, among which is that the foreign sponsor must comply with U.S. securities laws and should be expected to submit to the jurisdiction of U.S. courts when called to account for wrongdoing. Exempting foreign sponsors from the jurisdiction of U.S. courts would only serve to undermine U.S. securities laws and the U.S. regulatory regime, effectively voiding U.S. law in the name of international comity.

By contrast, this rationale likely would not apply to unsponsored ADRs because unsponsored ADRs exhibit traits that gave the Second Circuit pause when examining the swaps at issue in *Parkcentral*. Specifically, much like the *Parkcentral* swaps, unsponsored ADRs are created without the consent or involvement of the foreign company.

Subjecting a foreign company to U.S. securities laws simply because an unrelated depositary bank sold ADRs of its shares in the United States appears to be inconsistent with *Morrison*'s jurisdictional limitations. Plainly, if a transaction involving an unsponsored ADR were sufficient to trigger liability in the United States, no company – no matter how remote its connections to the United States – would be exempt from U.S. securities laws. Such a result seems to fly in the face of *Morrison*.

C. ALTERNATIVES TO FOREIGN LITIGATION - BRINGING STATE LAW CLAIMS ON AN INDIVIDUAL BASIS

Since the *Morrison* decision in 2010, entities have explored alternatives to bringing Section 10(b) claims. This section provides an overview of some of these new strategies.

Bringing State Law Claims on an Individual Basis

While *Morrison* significantly limits the jurisdictional reach of the federal securities law, it is still an open question of whether *Morrison* does—and should—have the same preclusive effect on claims in connection with alleged violations of state securities laws. Plaintiffs have attempted to circumvent *Morrison*'s holding by bringing state law claims for purchases of

securities occurring outside the U.S. against foreign defendants. There are, however, numerous issues that must be carefully considered before pleading state law claims.⁵⁸

SLUSA Preemption

Any mention of a state law securities action should raise concerns of possible preemption by the Securities Litigation Uniform Standards Act of 1998 (“SLUSA”). SLUSA prohibits the use of a class action to bring state law claims alleging securities fraud.⁵⁹ As the court stated in *In re Worldcom, Inc. Sec. Litig.*, “SLUSA was enacted to close the [state class action] loophole by mandating federal courts as the exclusive venue for class actions alleging fraud in the sale of certain covered securities and by mandating that such class actions be governed exclusively by federal law.”⁶⁰ SLUSA is not meant to prevent plaintiffs from asserting state law causes of action in state or federal court in individual actions; it is only meant to prevent a securities class action exodus from federal court, where the more restrictive Private Securities Litigation Reform Act (“PSLRA”) applies.⁶¹ Specifically, the statute provides:

No covered class action based upon the statutory or common law of any State or subdivision thereof may be maintained in any State or Federal court by any private party alleging—

(A) a misrepresentation or omission of a material fact in connection with the purchase or sale of a covered security; or

⁵⁸ The two most obvious types of state law claims that could apply to securities transactions are common law fraud claims and claims under state's “Blue Sky” laws. Other possibilities include other varieties of common law claims, such as negligent misrepresentation and unjust enrichment.

⁵⁹ See 15 U.S.C. § 78bb(f)(1).

⁶⁰ *In re Worldcom, Inc. Sec. Litig.*, 308 F. Supp. 2d 236, 242 (S.D.N.Y. 2004) (citation and quotation omitted).

⁶¹ *Dabit*, 547 U.S. at 87 (“[SLUSA] does not deny any individual plaintiff, or indeed any group of fewer than 50 plaintiffs, the right to enforce any state-law causes of action that may exist.”); see also *Kircher v. Putnam Funds Trust*, 547 U.S. 633, 636 n.1 (2006).



(B) that the defendant used or employed any manipulative or deceptive device or contrivance in connection with the purchase or sale of a covered security.⁶²

Is the Subject Security a “Covered Security?”

One question to consider is whether the foreign securities at issue in your case are “covered securities” under SLUSA. If not, SLUSA might not preempt the state law class action.⁶³ SLUSA defines “covered security” by referencing section 18(b) of the Securities Act, which states in part:

[T]he following are covered securities:

(1) Exclusive Federal registration of nationally traded securities. A security is a covered security if such security is—

(A) listed, or authorized for listing, on the New York Stock Exchange or the American Stock Exchange, or listed, or authorized for listing, on the National Market System of the Nasdaq Stock Market (or any successor to such entities);

⁶² *Id.*

⁶³ In some cases, SLUSA could preempt a claim even if the securities purchased by the plaintiff are not “covered securities.” SLUSA preempts a claim as long as the complaint pleads fraud in connection with covered securities – even if the covered security is not the security on which the claims are based. For example, in *U.S. Mortgage, Inc. v. Saxton*, 494 F.3d 833, 845 (9th Cir. 2007), *abrogated on other ground by Proctor v. Vishay Intertechnology Inc.*, 584 F.3d 1208 (9th Cir. 2009), the Ninth Circuit held that state-law fraud claims alleging misrepresentations in a publicly traded company’s regulatory filings were precluded by SLUSA—although plaintiffs’ claims arose from transactions in privately negotiated debt securities that were not “covered securities.” The court concluded that “the alleged harm stems from misrepresentations in [defendant’s] public filings and public statements,” which “undoubtedly ‘coincide’ with the purchase or sale of [defendant’s] publicly traded shares, and those shares are clearly ‘covered securities’ under SLUSA.” *Id.*

(B) listed, or authorized for listing, on a national securities exchange (or tier or segment thereof) that has listing standards that the Commission determines by rule (on its own initiative or on the basis of a petition) are substantially similar to the listing standards applicable to securities described in subparagraph (A); or

(C) is a security of the same issuer that is equal in seniority or that is a senior security to a security described in subparagraph (A) or (B).⁶⁴

Subparagraphs (A) and (B) consider whether a security is “listed” or “authorized for listing” on certain U.S. exchanges or “on a national securities exchange” with comparable listing standards. The statute does not define the term “national securities exchange,” but the structure of the statute makes clear that the phrase “national securities exchange” includes only domestic securities exchanges.⁶⁵

Therefore, a stock listed on a foreign exchange would not normally be considered a “covered security.”

⁶⁴ 15 U.S.C. § 77r(b).

⁶⁵ Specifically, Section 77r falls within a part of the code titled “domestic securities” while a separate part of the code deals with “foreign securities.” Also, there is a separate section titled “Foreign securities exchanges,” the existence of which suggests that “national securities exchanges” does not include foreign securities exchanges. See 15 U.S.C. § 78dd; see also *Roth v. Fund of Funds, Ltd.*, 279 F. Supp. 935, 936 (S.D.N.Y. 1968) (“The heading of [15 U.S.C. § 78dd] refers to ‘foreign securities exchanges’ and obviously refers to activities on such exchanges.”). Finally, there are several regulations that apply to “national securities exchanges” which would not conceivably apply to foreign exchanges. See, e.g., 15 U.S.C. § 78f (providing for the registration with the SEC of national securities exchanges and otherwise regulating such exchanges); see also 15 U.S.C. §§ 78g, 78i, 78k.



However, there are certain limited circumstances under which stock listed on a foreign exchange could be considered a “covered security,” so caution must be exercised when analyzing SLUSA. For example, foreign shares are sometimes listed on a U.S. exchange in connection with a foreign company’s ADR program. The foreign shares are considered “covered securities” even though they are not actually traded on the U.S. exchange. In *In re BP p.l.c.*, the class-action plaintiffs asserted New York common law fraud claims based on purchases of BP ordinary shares, which trade on the London Stock Exchange.⁶⁶ The court held that SLUSA preempted the claim, because the ordinary shares were technically “listed” on the New York Stock Exchange in connection with BP’s ADR program.⁶⁷ The court rejected the argument that a security must also be traded—not merely listed—in order to be subject to SLUSA.⁶⁸

One must also consider subparagraph (C) of the “covered securities” definition, which states that a security is a covered security if it “is a security of the same issuer that is equal in seniority or that is a senior security to a security described in subparagraph (A) or (B).”⁶⁹ A senior security is one that has “priority over another class as to the distribution of assets or the payment of dividends.”⁷⁰ Therefore, if the issuer of the foreign shares also issues other securities that trade on a U.S. exchange, the foreign shares would be considered “covered securities.”

If the foreign shares at issue do not qualify as “covered securities” (and if the complaint does not allege that the defendants made misrepresentations in connection with the purchase or sale of any other covered security), it does not appear that SLUSA will bar a class action based on state law claims alleging securities fraud.

Is the Action a “Covered Class Action?”

Notably, SLUSA applies only to “covered class actions.” The definition not only includes formal class actions, but also “any group of lawsuits filed in or pending in the same court” involving common questions of law or fact, and are “joined, consolidated, or otherwise proceed as a single action for any purpose.”⁷¹

Normally, if you bring an action on behalf of 50 or fewer investors, SLUSA will not apply. Some courts, however, have held that SLUSA preemption applies to individual actions that have been consolidated with a separate class action.⁷² Moreover, state law claims in an individual action may still be preempted by SLUSA even when the action is not formally joined or consolidated with other class actions bringing similar claims.⁷³

Thus, SLUSA preempts any “related” individual action proceeding with other actions “as a single action ‘for any purpose.’”⁷⁴ Also, Defendants may seek to remove a state court action to federal court where the action could potentially be consolidated with similar actions and dismissed under SLUSA.⁷⁵ Thus, despite plaintiff’s efforts to the contrary, there are still mechanisms available to preempt an individual action’s state law claims under SLUSA.

SLUSA’s State Pension Plan Exemption

Importantly, SLUSA excludes cases brought by states or state pension plans from its definition of

⁷¹ 15 U.S.C. § 78bb(f)(5)(b).

⁷² See *In re Fannie Mae Sec. Litig.*, 503 F. Supp. 2d 25, 32-33 (D.D.C. 2007); see also *In re Enron Corp. Sec., Derivative & MDL-1446 “ERISA” Litig.*, No. 01-3624, 2006 U.S. Dist. LEXIS 90526 (S.D. Tex. Dec. 12, 2006); *WorldCom*, 308 F. Supp. 2d at 247 (holding that ten individual actions collectively seeking damages on behalf of more than fifty plaintiffs formed a covered class action).

⁷³ See *In re Citigroup Inc. Sec. Litig.*, 987 F. Supp. 2d 377, 388 (S.D.N.Y. 2013) (plaintiff’s state law claims for fraud and negligent misrepresentation preempted under SLUSA, even where plaintiff “did not purposefully direct his lawsuit to this Court, nor is his complaint a verbatim copy of the other complaints, nor is he represented by the same counsel as other plaintiffs”) (citing *Instituto De Prevision Militar v. Merrill Lynch*, 546 F.3d 1340, 1347 (11th Cir.2008)).

⁷⁴ *Id.*

⁷⁵ *WorldCom*, 308 F. Supp. 2d 241.

⁶⁶ *In re BP p.l.c.*, 843 F. Supp. 2d at 792.

⁶⁷ *Id.* at 796-97.

⁶⁸ *Id.* at 797.

⁶⁹ 15 U.S.C. § 77r(b)(1)(C).

⁷⁰ *In re Metro. Secs. Litig.*, 532 F. Supp. 2d 1260, 1298 (E.D. Wash. 2007).



“covered class actions.” Specifically, SLUSA provides:

Notwithstanding any other provision of this section, nothing in this section may be construed to preclude a State or political subdivision thereof or a State pension plan from bringing an action involving a covered security on its own behalf, or as a member of a class comprised solely of other States, political subdivisions, or State pension plans that are named plaintiffs, and that have authorized participation, in such action.⁷⁶

“State pension plan” is specifically defined as “a pension plan established and maintained for its employees by the government of a State or political subdivision thereof, or by any agency or instrumentality thereof.”⁷⁷

Under the plain meaning of SLUSA, any pension fund established by a state, its agencies and instrumentalities for their employees may claim the exception.⁷⁸ As noted above, it seems clear that a state pension plan can proceed with state law claims under the state action exception and without fear of SLUSA preemption.

Such an action, however, cannot be brought as a class action. Significantly, the complaint must be drafted to clearly articulate that the state-entity plaintiff is proceeding on its own behalf and that it does not seek to assert claims on behalf of additional, similarly-situated state entities unless they have specifically authorized the suit. As such, any recovery sought must only go directly to the fund and not its members.

Because actions by state entities are immune from SLUSA, an unlimited number of state entities may join their claims in a single suit, provided each has specifically authorized the action. “The effect of the state-actions exception (as its plain language indicates) is to bring only those suits that are brought on behalf of fifty or more states, political subdivisions, or state pension plans that are named plaintiffs outside of

SLUSA’s otherwise broad preclusive reach under this grouping provision.”⁷⁹

The following cases are examples of how the State pension plan exception has been applied.

City of Chattanooga, Tennessee v. Hartford Life Ins. Co.

In *City of Chattanooga*, the sponsor of the City of Chattanooga, Tennessee Deferred Compensation Plan, brought state law claims in federal court for breach of fiduciary duty and unjust enrichment in connection with its investments in variable annuity contracts made through defendants.⁸⁰ The City styled its complaint as a class action “on behalf of its pension plan and all other similarly-situated pension plans[.]”⁸¹

Defendants moved to dismiss, claiming SLUSA preemption. The court found that all the elements for SLUSA preemption were met and dismissed the complaint without prejudice to repleading in line with the state action exception.⁸²

The court rejected the plaintiff’s initial invocation of the state action exception because it brought its claims as a class action. Instead, the court accepted defendants’ argument that “the exception applies only where the class is composed of named plaintiffs that have authorized participation.”⁸³

The court reached its conclusion based on its “plain language” analysis of the statute and rejected Chattanooga’s argument that the state action exception operated as an “opt-in” provision by which other state entities could join the action.⁸⁴ While the court granted the motion to dismiss, it also granted Chattanooga leave to amend in order to bring its complaint within the state action exception (presumably by recasting the

⁷⁹ *Demings v. Nationwide Life Ins. Co.*, 593 F.3d 486, 494 (6th Cir. 2010).

⁸⁰ *City of Chattanooga, Tenn. v. Hartford Life Ins. Co.*, No. 3:09cv516, 2009 U.S. Dist. LEXIS 119930, at *4-5 (D. Conn. Dec. 15, 2009).

⁸¹ *Id.* at *1.

⁸² *Id.* at *7-8.

⁸³ *Id.* at *9.

⁸⁴ *Id.* at *10 (“SLUSA . . . indicates that the state entity must have ‘authorized’ its participation at the time the action is brought.”) (citation omitted).

⁷⁶ 15 U.S.C. § 77p(d)(2)(A).

⁷⁷ 15 U.S.C. § 78bb(f)(3)(B)(ii).

⁷⁸ 15 U.S.C. § 78bb(f)(3)(B)(ii).



complaint as an individual action, as opposed to a class action).⁸⁵

In re Hollinger International, Inc.

In *Hollinger*, three plaintiffs filed an eight-count class action complaint in federal district court.⁸⁶ Two plaintiffs were pension plans (the Teachers' Retirement System of Louisiana ("Teachers") and the Washington Area Carpenters Pension and Retirement Fund ("Washington Carpenters")) and one was a private individual ("Carlson"). Three of the alleged causes of action were founded on Illinois state law: (i) breach of fiduciary duty; (ii) violations of Illinois Securities Law; and (iii) aiding and abetting breach of fiduciary duty. The remaining claims arose out of the Exchange Act.

Defendants moved to dismiss the state law claims on SLUSA preemption grounds. The court rejected defendants' argument that the Illinois Securities Law claim did not fall within the state action exception, holding that "the complaint fairly allege[d] that Teachers and Washington Carpenters are state pension plans."⁸⁷ The court nevertheless dismissed that claim under the Illinois Securities Law, but with leave to amend. It admonished the plaintiffs to "exclude any plaintiffs [i.e., Carlson] who are not state pension plans" when amending their complaint on behalf of the named plaintiffs, stating that "Plaintiffs may replead as to the named plaintiffs in this case."⁸⁸

Demings v. Nationwide Life Ins. Co.

In *Demings*, the Sixth Circuit rejected an attempt by a county sheriff, on behalf of a deferred compensation plan, to claim the state action exception.⁸⁹ The complaint was brought in federal court in Ohio and

styled as a class action on behalf of "all others similarly situated as sponsors of [deferred compensation] plans."

The *Demings* court found that the class mechanism invoked by the "all others similarly situated" language destroyed the state action exception.⁹⁰

Under the state action exception, "only classes of named plaintiffs that specifically authorized participation in the underlying suit" may belong to a class under the state action exception.⁹¹ Congress crafted the state action exception in this manner to avoid creating a loophole for class actions "on behalf of pension funds and municipalities that had no interest in bringing suit."⁹²

Instituto de Prevision Militar v. Merrill Lynch

Similar to the sheriff in *Demings*, the plaintiff in *Instituto de Prevision Militar v. Merrill Lynch* characterized its suit as one on behalf of "a large class of Guatemalan military pensioners."⁹³ The court found the claim to be preempted under SLUSA and not exempted by the state action exception for two reasons.

First, the claim was pled on behalf of a class of pensioners and not the fund itself—something expressly disallowed by the exception.⁹⁴

Second, the fund was foreign, and the "exception only applies to pension plans of states in the United States."⁹⁵ The court reached the same conclusion in a related case brought by the same foreign pension fund plaintiff.⁹⁶ Thus, foreign pension funds may not claim the protection of the state action exception under the SLUSA, as "this individual exception is addressing the preservation of U.S. state court causes of action in U.S.

⁸⁵ *Id.*

⁸⁶ *In re Hollinger Int'l, Inc., Sec. Litig.*, No. 04C-0834, 2006 U.S. Dist. LEXIS 47173, at *5-6 (N.D. Ill. June 28, 2006).

⁸⁷ The court conducted no analysis beyond this and did not remark on the fact that one of the pension plans appears not to be a state entity, but a union pension fund (Washington Carpenters). The court also did not directly address whether the plaintiffs could assert class claims on behalf of similarly-situated pension plans, although it ostensibly granted leave to amend on behalf of the named plaintiffs only.

⁸⁸ *Id.* at *71.

⁸⁹ *Demings*, 593 F.3d at 489.

⁹⁰ *Id.* at 493.

⁹¹ *Id.* at 494 (citing H.R. 1689, 105th Cong. § 16(d)(2) (July 21,

1998)).

⁹² This rationale was a secondary one for the court, which rejected the assertion of the state action exception because the sheriff, not the plan itself, was asserting the claim, which was at odds with the statute. *Id.* at 492 (citing 15 U.S.C. § 77p(d)(2)(A)).

⁹³ *Instituto de Prevision Militar v. Merrill Lynch*, 2007 U.S. Dist. LEXIS 31066, at *8.

⁹⁴ *Id.* at *7.

⁹⁵ *Id.* at *15.

⁹⁶ *Instituto de Prevision Militar v. Lehman*, 485 F. Supp. 2d at 1346.



state courts for the U.S. state pension funds.”⁹⁷

Extraterritorial Application of State Laws

Because *Morrison* held that federal securities laws do not have extraterritorial application, it is important to consider whether state laws apply to conduct occurring—and plaintiffs residing—outside a given state or outside the U.S. In other words: when do a particular state’s laws control the conduct of a foreign defendant? This issue overlaps with the choice-of-law question – when an investor sues a defendant for common law fraud, which state’s law applies?

Most of the cases on this issue address whether a particular state’s law can be applied to an out-of-state (not out-of-country) defendant. But from a state’s perspective, it should not matter whether the defendant is a citizen of a different state or a different country; the party is an out-of-state defendant in either scenario. Therefore, the following cases – discussing out-of-state but domestic defendants – are relevant to the question of whether a state’s laws can be applied to a foreign defendant.

Law of the Plaintiff’s Residence

One option is to apply the law of plaintiff’s state of residence, which is often the same location as where the plaintiff initiated its securities purchase. This is akin to the pre-*Morrison* Effects test. There are several cases in which investors have brought suit under the law of their state of residence. In many of these cases, there is no indication that the defendant engaged in any wrongful conduct within the state. These decisions do not directly address whether it is permissible for an investor to sue a non-resident defendant under a particular state’s law when the only connection to the state is that the plaintiff resides there and the plaintiff initiated the purchase there.⁹⁸

⁹⁷ *Id.*

⁹⁸ There is dicta in some cases that suggests this is appropriate. See, e.g., *Simms Investment Company v. E.F. Hutton & Co. Inc.*, 699 F. Supp. 543 (M.D. N.C. 1988) (“Blue Sky laws protect two distinct policies. First, the laws protect resident purchasers of securities, without regard to the origin of the security. Second, the laws protect legitimate resident issuers by exposing illegitimate resident issuers to liability, without regard to the markets of the issuer.”) (emphasis added); *Rousseff v. Dean Witter & Co.*, 453

Rather, these decisions portray how plaintiffs have successfully applied their home state’s law in certain situations.

- *In re Fannie Mae Sec. Litig.*:⁹⁹ The plaintiffs filed individual actions after opting out of the federal securities class action. Plaintiffs were residents of Massachusetts and California and sued under their respective state laws. A review of defendants’ brief in support of their motion to dismiss shows that they argued for SLUSA preemption but did not argue that the state laws did not apply to them.
- *Booth v. Verity*:¹⁰⁰ The plaintiffs were two individual Kentucky residents that bought stock in the defendant, a California company. Plaintiffs filed suit under Kentucky’s blue sky law. The court held that there was no personal jurisdiction over the individual defendants because they had not committed any act purposefully directed at Kentucky. After dismissing the claims against the individual defendants, the court proceeded to analyze the merits of the claim against the company, while implicitly assuming that Kentucky law could properly be applied to the company.¹⁰¹
- *In re Marsh & McLennan Companies, Inc. Sec. Litig.*:¹⁰² The class action plaintiffs asserted various state law claims, including blue sky law claims, on behalf of a pension fund subclass. The court seemed to assume that either the law of the residences of the plaintiffs or the defendant would control, stating: “Where applicable, citations are provided for Ohio, New Jersey, and New York, the respective residences of the Co-Lead Plaintiffs and [the defendant].”¹⁰³ The blue sky law claim in the complaint stated: “This Count is brought

F. Supp. 774, 778 n.7 (N.D. Ind. 1978) (“Indiana’s securities law is designed to protect investors who operate within the State of Indiana”).

⁹⁹ *In re Fannie Mae Sec. Litig.*, 503 F. Supp. 2d 25 (D. D.C. 2007).

¹⁰⁰ *Booth v. Verity*, 124 F. Supp. 2d 452 (W.D. Ky. 2000).

¹⁰¹ *Id.* at 459 n.2.

¹⁰² *In re Marsh & McLennan Companies, Inc. Sec. Litig.*, 501 F. Supp. 2d 452 (S.D.N.Y. 2006).

¹⁰³ *Id.* at 495 n.19.



pursuant to those state securities laws that have a private right of action of each of the states in which the members of the Municipal and State Pension Fund Subclass Plaintiffs are located.” In their brief, the defendants did not argue that the various state statutes did not apply to them, just that “[a] proper choice of law analysis might dictate that New York law applies to all the claims.”

- *Beightol v. Navarre Corp., Inc.*:¹⁰⁴ The plaintiff, a Mississippi resident, sued the defendant, a Minnesota company, under the Mississippi Securities Act and for Mississippi common law fraud. The plaintiff conceded that the statute required privity between the plaintiff and defendant, which he had not alleged, but the defendant never argued that it was not otherwise subject to the Mississippi statute. The court found that the plaintiff had adequately pled the negligent misrepresentation and common law fraud claims under Mississippi law.¹⁰⁵
- *In re Enron Corp. Sec.*:¹⁰⁶ Ohio pension funds sued in state court and asserted “claims for common law fraud and deceit, aiding and abetting common law fraud, conspiracy to commit fraud, and negligent misrepresentation under Ohio law, as well as violation of the Texas Securities Act[.]”
- *In re Worldcom, Inc. Sec. Litig.*:¹⁰⁷ The plaintiffs were a group of New York City pension funds suing under federal and state law. The court applied New York law to the common law fraud claims based on the parties’ consent to its application.

None of these cases specifically analyze the question of whether state law can be applied extraterritorially. It is, however, encouraging that multiple plaintiffs have sued defendants under their

own state’s blue sky law where there was no obvious connection to the state other than the plaintiff’s residence and the fact that the purchase was initiated there. It is also encouraging that the defendants in these cases did not argue that the law could not be applied to them.

One complication is that a class action typically includes the claims of investors from many different states. While there are some favorable pre-SLUSA decisions applying one state’s law to a nationwide class of investors, post-SLUSA decisions on this point are rare because SLUSA essentially eliminated securities fraud class actions arising under state law.¹⁰⁸

Wrongful Acts Within a Particular State

Another option is to apply the law of the particular state where the defendant’s wrongful acts occurred. Both federal and state courts have determined that state law is applicable to claims involving securities transactions based on defendants’ actions within that state. At its core, this is an application of the pre-*Morrison* Conduct test to state law.

¹⁰⁴ *Beightol v. Navarre Corp., Inc.*, 2009 U.S. Dist. LEXIS 6590 (S.D. Miss. Jan. 26, 2009).

¹⁰⁵ *Id.* at *13.

¹⁰⁶ *In re Enron Corp. Sec.*, 465 F. Supp. 2d 687, 692 (S.D. Tex. 2006).

¹⁰⁷ *In re Worldcom, Inc. Sec. Litig.*, 382 F. Supp. 2d 549 (S.D.N.Y. 2005).

¹⁰⁸ See, e.g., *Barkman v. Wabash, Inc.*, 674 F. Supp. 623, 634 (N.D. Ill. 1987) (rejecting defendants’ argument that the “court must apply the law of each class member’s residence because the law of the state where each individual member of the class transacted his purchase would govern the common law fraud claim”; instead Illinois applies the “most significant contacts” test in determining choice of law issues); *In re Activision Sec. Litig.*, 621 F. Supp. 415, 430 (N.D. Cal. 1985) (despite differences in elements of common law fraud claims, defendants had not shown why California law would not apply to all claims); *In re Victor Technologies Sec. Litig.*, 102 F.R.D. 53, 59-60 (S.D. Cal. 1984) (certifying nationwide class of stock purchasers alleging federal securities and state statutory and common law claims because the “court will most likely apply California law to all pendent state law claims”); *In re Saxon Sec. Litigation*, 1984 U.S. Dist. LEXIS 19223, at *11 (S.D.N.Y. Feb. 23, 1984) (“Although we have no specific information on the law governing common law fraud in different states, we doubt whether there are significant variations. Therefore, it may well be reasonable to apply the law of New York to all of the non-residents’ claims, or to allow both sides to explore the possibility of picking another state’s law to be applied uniformly[.]”) (internal citation omitted); *Dekro v. Stern Brothers & Co.*, 540 F. Supp. 406, 418 (W.D. Mo. 1982) (refusing to decertify a class alleging violations of the federal securities laws and common law fraud because “[i]t is conceivable that defendant’s conduct should be evaluated under the law of that state with the most significant contacts to the underlying transaction”).



In *Dandong v. Pinnacle Performance Ltd.*,¹⁰⁹ the plaintiffs, Singapore investors, filed an action against Morgan Stanley in the Southern District of New York alleging New York state law claims relating to their purchases of credit-linked notes issued by Pinnacle Performance Limited.¹¹⁰ Plaintiffs alleged that Morgan Stanley deliberately invested plaintiffs' principal in risky collateralized debt obligations ("CDOs") created by Morgan Stanley. Plaintiffs asserted that Morgan Stanley knowingly designed the CDOs to fail, and that Morgan Stanley took a short position on the collateral pool of assets underlying the CDOs.¹¹¹ Even though the notes were bought from various independent distributors in Asia, the conduct at issue took place in New York.¹¹²

In rejecting defendants' argument that a forum selection clause required that the litigation take place in Singapore, the court found that "the vast majority of actions that Plaintiffs' allege were fraudulent occurred in New York and London."¹¹³ These actions included Morgan Stanley's creation of the CDOs (New York), their selection of the assets underlying the CDOs (New York), their selection of the assets underling the notes (London), and their drafting of the offering materials (New York). And because Morgan Stanley did not demonstrate that Singapore law differed from New York law, the court applied New York law to the merits issues as well.¹¹⁴

Then, in 2012, Singapore financial company Hong Leong Financial ("HLF") filed an action in the Southern District of New York against Morgan Stanley alleging state claims and a federal claim arising from the same set of facts present in *Dandong*.¹¹⁵ The court dismissed the federal claim under the Lanham Act, which was the basis for the court's subject matter jurisdiction, and declined to extend supplemental jurisdiction over the remaining state law claims. Because the district

court dismissed the federal case without ruling on the merits of the state claims, HLF filed an action in New York state court against Morgan Stanley alleging state law claims in 2014.¹¹⁶ As the federal court did in *Dandong*, the New York state court applied New York state law because plaintiffs showed that the "alleged fraud was devised in New York, through the actions of Morgan Stanley and MS Capital, and that the situs of the transaction, as well as the availability of the evidence and witnesses, favors HLF's choice of New York."¹¹⁷

Additionally, plaintiffs have also been successful—albeit on a limited basis and only at the trial court level—by bringing state-specific common law claims in state court after initially failing in federal court with U.S. securities law claims. For example, in *Viking Global Equities, LP v. Porsche Automobil Holding SE*,¹¹⁸ a group of hedge funds claimed they sustained losses as a result of misrepresentations made by Porsche with regards to its expressed intention not to acquire shares in Volkswagen. The Southern District of New York determined that the plaintiffs' investments—security-based swap agreements based on foreign shares—were insufficient to form a jurisdictional nexus and, thus, were barred by *Morrison*.¹¹⁹

Undeterred, the plaintiffs then brought New York state law claims of fraud and unjust enrichment in New York state court. Specifically, plaintiffs alleged that they were fraudulently induced into short selling VW stock in reliance on defendant's public and private assurances that it had no present intention to acquire a 75% stake in Volkswagen. When defendant unveiled its takeover plan, it triggered a "short squeeze" that spiked VW's stock price and forced plaintiffs to cover their positions at losses of more than a billion dollars.¹²⁰

¹⁰⁹ *Dandong v. Pinnacle Performance Ltd.*, 2011 U.S. Dist. LEXIS 126552 (S.D.N.Y. Oct. 31, 2011).

¹¹⁰ *Id.* at *1-2.

¹¹¹ *Id.* at *5-6.

¹¹² *Id.* at *2, 5-6.

¹¹³ *Id.* at *15.

¹¹⁴ *Id.*

¹¹⁵ *Hong Leong Finance Ltd. (Singapore) v. Pinnacle Performance Ltd.*, 2013 WL 5746126 (S.D.N.Y Oct. 23, 2013).

¹¹⁶ *Hong Leong Fin. Ltd. (Singapore) v. Morgan Stanley*, 998 N.Y.S.2d 306 (Sup. Ct. 2014).

¹¹⁷ *HLF v. Morgan Stanley*, 998 N.Y.S.2d at 306.

¹¹⁸ 960 N.Y.S.2d 53 (New York Sup. Ct. Aug. 6, 2012).

¹¹⁹ *Elliott Associates v. Porsche Automobil Holding SE*, 759 F.Supp.2d 469, 476 (S.D.N.Y. Dec. 30, 2010). The Second Circuit ultimately affirmed the district court. See *Parkcentral*, 763 F.3d at 198.

¹²⁰ *Viking Global Equities, LP v. Porsche Automobil Holding SE*, 960 N.Y.S.2d 53 (New York Sup. Ct. Aug. 6, 2012).



Defendants again argued that the character of the securities at issue precluded jurisdiction in U.S. courts. The New York Supreme Court rejected defendants' argument, explaining that "[a]t the core of plaintiffs' claims are whether New York courts may hold responsible a foreign entity, who conducts business globally, for fraudulent misrepresentations purportedly aimed at New York plaintiffs. New York clearly has a vested interest in such an action."¹²¹ The appellate court, however, reversed the lower court's decision after finding that the email and phone records—the communications containing the alleged misrepresentations—were inadequate on their own to establish jurisdiction.¹²²

Finally, the use of state law as an alternative is underscored by another case, *Basis Yield Alpha Fund v. Goldman Sachs Group, Inc.*,¹²³ brought by an Australian hedge fund against Goldman Sachs. Although this case concerns a foreign plaintiff rather than a foreign defendant, *Basis Yield* addresses the same issue as *Viking Global*: whether *Morrison* precludes jurisdiction of state law claims. Plaintiffs alleged that defendant Goldman Sachs made false and misleading statements concerning its sales of a security based upon a collateralized debt obligation arising from subprime residential home mortgages and two credit default swaps. Plaintiffs' claims for fraud, negligent misrepresentation, and unjust enrichment were sustained and largely affirmed by the New York appellate court.¹²⁴ Another interesting point in the *Basis Yield* opinion is that the Court acknowledged that provisions in the securities documents called for the application of English law, but the parties stipulated that the English and New York fraud analysis would be largely the same. However, the Court found that since English law does not recognize the covenants of good faith and fair dealing, certain of plaintiffs' contract-based claims failed.¹²⁵ From a practical view, this

demonstrates that relying on foreign law for both fraud and contract claims is a double-edge sword.

Issues with State Law Claims

There are various obstacles that arise when pleading state law claims which do not present themselves with traditional federal law claims. In particular, while Oregon was the first—and, thus far, only—state to adopt the fraud-on-the-market theory in 2012,¹²⁶ the overwhelming majority of state law fraud claims do not recognize the fraud-on-the-market presumption of reliance.¹²⁷

¹²⁶ *State v. Marsh & McLennan Co. Inc.*, 292 P.3d 525 (Or. 2012).

¹²⁷ See *Peil v. Speiser*, 806 F.2d 1154, 1163 n.17 (3d Cir. 1986) ("While the fraud on the market theory is good law with respect to the Securities Acts, no state courts have adopted the theory, and thus direct reliance remains a requirement of a common law securities fraud claim"); *In re Ford Motor Co. Vehicle Paint Litig.*, 182 F.R.D. 214, 221 (E.D. La. 1998) ("[T]he vast majority of states have never adopted a rule allowing reliance to be presumed in common law fraud cases, and some states have expressly rejected such a proposition."); *Marsh & McLennan*, 501 F. Supp. 2d at 496 ("[I]n Ohio, securities plaintiffs must allege their reliance on false representations."); *In re WorldCom, Inc. Sec. Litig.*, 2006 U.S. Dist. LEXIS 11679, at *18 (S.D.N.Y. Mar. 22, 2006) ("In interpreting their common law, however, courts have declined to create a presumption of reliance for securities' claims where it would not otherwise exist for common law fraud claims"); *Gaffin v. Teledyne, Inc.*, 611 A.2d 467, 474 (Del. 1992) ("A class action may not be maintained in a purely common law . . . fraud case since individual questions of law or fact, particularly as to the element of justifiable reliance, will inevitably predominate over common questions of law or fact"); *Antonson v. Robertson*, 141 F.R.D. 501, 508 (E.D. Kan. 1991) ("[W]ith respect to plaintiffs' common law fraud claims, in the absence of an analogous state law doctrine of fraud on the market, each individual plaintiff would be required to prove his or her individual reliance, causing individual questions of fact to predominate in the case."); *Mirkin*, 5 Cal. 4th at 1100-01 (California common law requires pleading actual reliance); *Gavron*, 115 F.R.D. at 325 (declining to certify class of Pennsylvania common law fraud claims because "each plaintiff must demonstrate his individual reliance upon the defendants' misstatements"); *Keyser v. Commonwealth Nat. Financial Corp.*, 121 F.R.D. 642, 649 (M.D. Pa. 1988) (fraud on the market claim unavailable in common law). There are some hints that the fraud-on-the-market presumption could be invoked under New York law, although most New York cases have refused to apply the presumption. *Pfizer*, 584 F. Supp. 2d at 643 (while there is an "open question" as to whether the fraud-on-the-market theory can be used for New York common law fraud claims, courts in the Southern District of New York "have generally refused to allow plaintiffs to use the fraud-on-the-market theory to support

¹²¹ *Id.* at *4.

¹²² *Viking Global Equities, LP v. Porsche Automobil Holding SE*, 101 A.D.3d 640, 640 (New York App. Div. Dec. 27, 2012).

¹²³ No. 652996/2011, 961 N.Y.S.2d 356 (N.Y. Sup. Ct. Oct. 18, 2012).

¹²⁴ *Id.*; see *Basis Yield Alpha Fund (Master) v. Goldman Sachs Group, Inc.*, 115 A.D.3d 128 (N.Y. App. Div. Jan. 30, 2014).

¹²⁵ 2012 WL 5187653, at *9.



In contrast to common law fraud claims, “[m]any state securities statutes have been . . . interpreted to include a presumption of reliance, or to eliminate the reliance requirement altogether.”¹²⁸

However, the state securities statutes present their own unique obstacles. Many of these statutes require privity between the plaintiff and the defendant. For example, the Pennsylvania equivalent to Section 10(b) is Section 1-401 of the Pennsylvania Securities Act.¹²⁹ Section 1-501 provides a private cause of action for violations of Section 1-401.¹³⁰ However, Section 1-501 contains a privity requirement.¹³¹ In most securities fraud cases, the plaintiffs did not purchase their shares directly from the defendant company, but rather purchased them on the open market. These purchasers would, hence, not be able to use statutes requiring privity.¹³²

common law fraud claims”).

¹²⁸ *In re WorldCom, Inc. Sec. Litig.*, 2006 U.S. Dist. LEXIS 11679, at *17-18 (S.D.N.Y. Mar. 22, 2006) (citing *Mirkin v. Wasserman*, 858 P.2d 568, 579-80 (Cal. 1993); *Conn. Nat'l Bank v. Giacomi*, 699 A.2d 101, 120 n.37 (Conn. 1997); *Allyn v. Wortman*, 725 So. 2d 94, 101 & n.3 (Miss. 1998); *Kaufman*, 754 A.2d at 1197; *Everts v. Holtmann*, 667 P.2d 1028, 1033 (Or. Ct. App. 1983); *Gohler v. Wood*, 919 P.2d 561, 566 (Utah 1996); *Esser Distributing Co. v. Steidl*, 437 N.W.2d 884, 887 (Wis. 1989)). Some state securities laws do require a plaintiff plead actual reliance. For example, Section 517.301 of the Florida Securities Act, Florida’s analogue to Section 10(b) of the Exchange Act, includes reliance as an element. See *Camden Asset Mgmt., L.P. v. Sunbeam Corp.*, 2001 U.S. Dist. LEXIS 11022 (S.D. Fla. July 3, 2001) (“Similarly, for the Florida Securities Act claim, the Eleventh Circuit . . . has found that justifiable reliance is an essential element of a claim under § 517.301 of the Florida Securities Act”). “Unlike under federal law . . . a presumption of reliance based on a ‘fraud on the market theory’ is unavailable in Florida.” *In re Sahlen & Assoc., Sec. Litig.*, 773 F. Supp. 342, 371 (S.D. Fla. 1991).

¹²⁹ *GFL Advantage Fund, Ltd. v. Colkitt*, 272 F.3d 189, 214 (3d Cir. 2001).

¹³⁰ See *Kronenberg v. Katz*, 872 A.2d 568, 597 (Del. Ch. 2004).

¹³¹ See *Biggans v. Bache Halsey Stuart Shields, Inc.*, 638 F.2d 605, 610 (3d Cir. Pa. 1980) (Section 1-501 “only gives the seller or buyer the right to sue the person purchasing or selling the security”); *Sowell v. Butcher & Singer, Inc.*, 1987 U.S. Dist. LEXIS 3788 (E.D. Pa. May 12, 1987) (“The Pennsylvania securities statute however, grants a private remedy to a buyer only against a seller and requires strict privity between the parties”).

¹³² See also *Kaufman v. I-Stat Corp.*, 165 N.J. 94, 112 (N.J. 2000) (New Jersey does not require reliance, but it does require privity between the plaintiff and defendant, which excludes purchases on the secondary market).

California’s securities fraud statute, Section 25400(d) of the California Corporations Code, does not require privity.¹³³ The statute does, however, contain a different obstacle – pleading and proof of the involvement of each defendant in the purchase or sale of the security:

The principal limitation of section 25400(d) as a general remedy for securities fraud appears to be the requirement that the party making the misrepresentation be a “broker-dealer or other person selling or offering for sale or purchasing or offering to purchase the security.” To satisfy this requirement, the plaintiff must prove that the defendant was engaged in market activity at the time of the misrepresentations.¹³⁴

D. FOREIGN LAW CLAIMS

Some plaintiffs have pled claims based on foreign law in an attempt to avoid the limitations of *Morrison*. So far, many of these claims have not been successful.¹³⁵ However, at least one federal court has allowed foreign law claims despite the policy arguments stemming from *Morrison*.¹³⁶

Jurisdiction

The threshold issue when pleading foreign law claims is whether the court will have subject matter

¹³³ *Mirkin v. Wasserman*, 5 Cal. 4th 1082, 1104 (Cal. 1993).

¹³⁴ *Mirkin*, at 1123; see also *Kamen v. Lindly*, 94 Cal. App. 4th 197, 206 (Cal. App. 6th Dist. 2001) (“[W]e conclude that civil liability pursuant to Corporations Code section 25500 applies only to a defendant who is either a person selling or offering to sell or buying or offering to buy a security”); *California Amplifier, Inc. v. RLI Ins. Co.*, 94 Cal. App. 4th 102, 111-14 (Cal. App. 2d Dist. 2001) (liability under Section 25500 requires that the defendant personally violate Section 25400). The plaintiff need not have purchased from the defendant but must have been “affected by such act or transaction for the damages sustained by the latter as a result of such act or transaction.” Cal. Corp. Code § 25500.

¹³⁵ See *In re Toyota Motor Corp. Secs. Litig.*, 2011 U.S. Dist. LEXIS 75732, at *17-21 (C.D. Cal. July 7, 2011) (dismissing claims under Japanese law); *In re BP P.L.C.*, 2012 843 F. Supp. 2d 712, 798-99 (S.D. Tex. Feb. 13, 2012) (dismissing claims under English law).

¹³⁶ *In re BP p.l.c. Secs. Litig.*, MDL No. 10-md-2185, No. 4:12-cv-1837 (S.D. Tex. Sept. 30, 2013).



jurisdiction over the claims. In both *Toyota* and *BP* (“*BP I*”), the plaintiffs sought to establish original jurisdiction over the foreign law claims under the Class Action Fairness Act (“CAFA”).¹³⁷ In both cases, the courts applied CAFA’s carve-out for “any class action that solely involves a claim . . . concerning a covered security.”¹³⁸ CAFA uses the same definition of “covered security” as is used by SLUSA, so the discussion above regarding whether foreign securities are considered covered securities is also relevant here. If Toyota and BP did not have ADR programs in the U.S., their ordinary shares would not have been “listed” on the NYSE and would not be considered “covered securities.” In that situation, the courts would have had original jurisdiction over the foreign law claims.

Even though the *Toyota* and *BP I* courts concluded that they lacked original jurisdiction over the foreign law claims, they nevertheless had discretion to exercise supplemental jurisdiction over those claims. Both courts declined to exercise this discretion.¹³⁹ In declining jurisdiction, the *Toyota* court expressly relied on *Morrison*, holding that the “clear underlying rationale of” *Morrison* “is that foreign governments have the right to decide how to regulate their own securities markets.”¹⁴⁰ According to the court, “[t]his respect for foreign law would be completely subverted if foreign claims were allowed to be piggybacked into virtually every American securities fraud case, imposing American procedures, requirements, and interpretations likely never contemplated by the drafters of the foreign law.”¹⁴¹

However, in an extraordinarily rare ruling, the Texas District Court in a later *BP* case (“*BP Ohio*”) held that some state law claims were not precluded under *Morrison* because they were capable of proceeding under English law.¹⁴² In considering the motion to dismiss, the court addressed the jurisdictional law

issues governing the claims. By applying Texas choice of law principles and the Restatement (Second) of Conflicts of Laws, the court determined that English law has the “most substantial relationship” to the plaintiffs’ claims.¹⁴³ The court then proceeded to “map” three of the plaintiffs’ claims to English law: i) state statutory claims map to statutory securities fraud under the Financial Services and Markets Act of 2000 (“FSMA”); ii) claims for common law fraud map to the English action for “deceit;” and, iii) claims for common law negligent misrepresentation map to the English action for “negligent misstatement.”¹⁴⁴ While numerous factors influenced the court’s decision, many of which were extremely fact-specific (notably, the large number of related cases simultaneously pending in the same court), the *BP Ohio* case nonetheless represents a successful attempt to establish jurisdiction for claims under state and comparable foreign law in a U.S. court against a foreign company.

Forum Non Conveniens

Even if a U.S. court has jurisdiction over foreign law claims, it may still dismiss those claims under the *forum non conveniens* doctrine. The *forum non conveniens* doctrine recognizes a court’s discretion to decline to exercise jurisdiction over a suit if the convenience of the parties and the court, and the interests of justice point toward adjudication in another forum.¹⁴⁵ A party seeking dismissal on this basis must show that (i) an adequate alternative forum exists and (ii) the balance of the public and private factors favors dismissal.¹⁴⁶

The question of *forum non conveniens* is very fact-specific. Some courts have dismissed foreign claims under the *forum non conveniens* doctrine. The Third Circuit has held that “[o]nly quite unusual” cases raising foreign securities law claims will be appropriate for adjudication in U.S. courts, because plaintiffs must show both that the U.S. court is “the most appropriate

¹³⁷ See 28 U.S.C. § 1332(d).

¹³⁸ 28 U.S.C. § 1332(d)(9); see *Toyota*, 2011 U.S. Dist. LEXIS 75732, at *17-18; *BP*, 2012 U.S. Dist. LEXIS 17788, at *237-38.

¹³⁹ *Toyota*, 2011 U.S. Dist. LEXIS 75732, at *19-21; and *BP*, 2012 U.S. Dist. LEXIS 17788, at *238-39.

¹⁴⁰ *Toyota*, 2011 U.S. Dist. LEXIS 75732, at *20.

¹⁴¹ *Id.* at *20-21

¹⁴² *In re BP p.l.c. Secs. Litig.*, MDL No. 10-md-2185, No. 4:12-cv-1837, 2013 WL 6383968 (S.D. Tex. Sept. 30, 2013).

¹⁴³ *In re BP p.l.c. Secs. Litig.*, MDL No. 10-md-2185, No. 4:12-cv-1837, 2013 WL 6383968 (S.D. Tex. Sept. 30, 2013).

¹⁴⁴ 2013 WL 6383968, at *37.

¹⁴⁵ *Koster v. (Am.) Lumbermens Mut. Cas. Co.*, 330 U.S. 518, 527 (1947); and *Karim v. Finch Shipping Co.*, 265 F.3d 258, 268 (5th Cir. 2001).

¹⁴⁶ *Karim*, 265 F.3d at 268-69.



forum” and that a U.S. court “is the most convenient forum, which, particularly for foreign-law claims asserted against foreign entities, is rarely an easy task.”¹⁴⁷

The *BP Ohio* case represents one of the quite unusual and rare cases appropriate for adjudication in the U.S. In holding that the defendants did not surmount “the high bar for disturbing Plaintiffs’ choice of forum” and that “the Court is certainly capable of applying English law,” the court considered the unique factors surrounding the BP Deepwater Horizon oil spill.¹⁴⁸ In conducting its analysis, the court noted that “the nature of the controversy is unquestionably local” and that “it would be inefficient to send these claims to England, when nearly the same issues will be adjudicated here” in multiple other BP actions.¹⁴⁹ Based on these factors, the court declined to conclude that an English court was a more appropriate forum.

The court’s reasoning was extremely fact specific and may not easily lend itself for use in other cases. Nevertheless, *BP Ohio* is an excellent example of how to use case specific facts to overcome a *forum non conveniens* argument in a motion to dismiss.

SLUSA

Investors should be cognizant that one court has held (in two separate decisions) that SLUSA bars securities fraud class actions brought under foreign law.¹⁵⁰ These decisions are directly contrary to SLUSA’s plain language, which states that the statute applies only to class actions “based upon the statutory or common law of any State.”¹⁵¹ The term “State” is defined as “any State of the United States, District of Columbia,

Puerto Rico, the Virgin Islands, or any other possession of the United States.”¹⁵² Consistent with the statutory text, the Third Circuit, on the other hand, has held that SLUSA does not apply to foreign law claims.¹⁵³

A distinguishing factor worth noting, SLUSA did not bar the claims in *BP Ohio* because the case was not brought on behalf of a class. A group of nine pension funds had large enough holdings to make it worth their while to pursue as an individual action. However, had the case been brought as a class action, the outcome would have likely been very different.

E. RICO CLAIMS

Another possibility is to file suit pursuant to the Racketeer Influenced and Corrupt Organizations Act (“RICO”) to recover for fraud in connection with the purchase of foreign securities. There are a couple of significant hurdles to this approach.

First, the PSLRA “removed securities fraud as a predicate act under RICO.”¹⁵⁴ Specifically, the PSLRA modified the RICO statutory text so that it now reads, in part: “no person may rely upon any conduct that would have been actionable as fraud in the purchase or sale of securities to establish a violation of [the section prohibiting racketeering activities].”¹⁵⁵ An argument could be made that because fraud in connection with the purchase or sale of a foreign security is no longer actionable under Section 10(b), the RICO carve-out does not apply to fraud in connection with foreign securities. There is some authority to support this

¹⁴⁷ *LaSala v. Bordier Et Cie*, 519 F.3d 121, 142-43 (3d Cir. N.J. 2008); see also *In re Alcon S’holder Litig.*, 719 F. Supp. 2d 263, 275 (S.D.N.Y. 2010) (dismissing shareholder claims on *forum non conveniens* grounds where “core events, operative facts, applicable law, and associated public policy interests at issue are predominantly” foreign); and *LaSala v. UBS, AG*, 510 F. Supp. 2d 213, 234 (S.D.N.Y. 2007) (dismissing Swiss law claim on *forum non conveniens* grounds).

¹⁴⁸ 2013 WL 6383968, at *54.

¹⁴⁹ *Id.* at *54-55.

¹⁵⁰ See *LaSala v. UBS, AG*, 510 F. Supp. 2d 213, 238 (S.D.N.Y. 2007); and *LaSala v. Lloyds TSB Bank*, 514 F. Supp. 2d 447, 472 (S.D.N.Y. 2007).

¹⁵¹ 15 U.S.C. §78bb(f)(1)(A).

¹⁵² 15 U.S.C. §78c(a)(16).

¹⁵³ See *LaSala*, 519 F.3d at 142-43 (“This conclusion [that SLUSA does not preempt foreign-law claims] flows directly from the text of SLUSA, which by its terms only affects claims based upon the laws of a state or territory of the United States”).

¹⁵⁴ *Anza v. Ideal Steel Supply Corp.*, 547 U.S. 451, 472 (2006).

¹⁵⁵ 18 U.S.C. § 1964(c); see also *In re Enron Corp. Sec., Derivative & ERISA Litig.*, 284 F. Supp. 2d 511, 618 (S.D. Tex. 2003) (“Before the RICO Amendment, a plaintiff could allege a private civil RICO claim for securities laws violations sounding in fraud because ‘fraud in the sale of securities’ was listed as a predicate offense”).



argument.¹⁵⁶ However, other courts have held that the RICO carve-out applies even when the plaintiff could not bring a federal securities fraud claim.¹⁵⁷

Even assuming that courts would allow plaintiffs to allege a foreign securities fraud, such as a racketeering act, a separate issue of whether the RICO claim would be barred as an extraterritorial application of the statute, would arise. Since *Morrison*, multiple courts have held that RICO lacks extraterritorial application.¹⁵⁸ Despite these rulings, RICO is presumably still available when there is sufficient conduct in the U.S.¹⁵⁹

To summarize, there may be a narrow path to a successful RICO claim. A successful claim would require a court to hold (i) that acts of foreign securities fraud may be used as predicate racketeering acts (because those acts are no longer actionable as securities fraud); and (ii) the conduct at issue has sufficient connection to the U.S. to be considered a domestic application of RICO.

¹⁵⁶ See *OS Recovery, Inc. v. One Groupe Int'l, Inc.*, 354 F. Supp. 2d 357, 368-71 (S.D.N.Y. 2005) (holding that RICO claims based on purported aiding and abetting securities violation were not barred by RICO Amendment because they were not actionable by the same plaintiff who brought the RICO claims).

¹⁵⁷ See, e.g., *MLSMK Inv. Co. v. JP Morgan Chase & Co.*, 651 F.3d 268, 277 (2d Cir. 2011) (“[T]he PSLRA bars civil RICO claims alleging predicate acts of securities fraud, even where a plaintiff cannot itself pursue a securities fraud action against the defendant”); *Thomas H. Lee Equity Fund V. L.P. v. Mayer Brown, Rowe & Maw LLP*, 612 F. Supp. 2d 267, 283 (S.D.N.Y. 2009) (“[T]he RICO Amendment bars claims based on conduct that could be actionable under the securities laws even when the plaintiff, himself, cannot bring a cause of action under the securities laws”).

¹⁵⁸ See, e.g., *Norex Petroleum Ltd. v. Access Industries, Inc.*, 631 F.3d 29, 33 (2d Cir. 2010); *United States v. Philip Morris USA, Inc.*, 783 F. Supp. 2d 23, 27 (D.D.C. 2011); *Cedeno v. Intech Group, Inc.*, 733 F. Supp. 2d 471, 473-74 (S.D.N.Y. 2010).

¹⁵⁹ See *Philip Morris*, 783 F. Supp. 2d at 29 (noting, and not disagreeing with the premise of, the plaintiffs’ argument that domestic conduct can still give rise to RICO claim even though some conduct also occurs abroad); *Picard v. Kohn*, 2012 U.S. Dist. LEXIS 22083, at *15 n.3 (S.D.N.Y. 2012) (recognizing that RICO “has its own extraterritorial limitations” and noting, but not deciding, the plaintiff’s argument that the alleged RICO “enterprise has sufficient contacts with the United States to support a RICO claim”).



Practical Considerations For Institutional Investors Interested In Foreign Asset Recovery Actions





A. EVALUATING WHETHER TO PARTICIPATE IN A FOREIGN ASSET RECOVERY ACTION

Monitoring and Identifying Securities Actions That Impact Your Portfolio

Following *Morrison*, an investor that has purchased ordinary shares of a foreign company on a foreign exchange only has an available remedy for a federal securities fraud violation through an action in a foreign jurisdiction. Given the new realities of global securities litigation after *Morrison*, public pension funds must adapt to the new challenges of monitoring their off shore portfolios to ensure that they are able to take full advantage of opportunities to recover assets in jurisdictions outside the U.S.

While most of the world's securities class action litigation occurs in the U.S., there has been a significant expansion in investor recovery actions around the globe. Securities actions are now occurring in Canada, Australia, Brazil, and across Europe and Asia. An analysis of select jurisdictions is found in Section Three of this paper. The number of actions and the number of countries where actions are being pursued will likely continue to increase, and the various actions which allow for recovery are evolving during this process.

Finding and tracking litigation on a global scale can be difficult for U.S. institutional investors to accomplish on their own. Even devoting substantial internal resources to the process may leave significant gaps in monitoring a global portfolio. The identification process is complex because there is no central registry or single source for finding actions outside the United States. Moreover, unlike the U.S. opt-out class action process, where investors can remain passive, receive notice of a settlement, and then decide to make a claim or opt-out of the class case, most foreign actions (exceptions being Canada, Australia and, on occasion, The Netherlands), require investors to "opt-in" to foreign proceedings at the time of filing.

This "opt-in" process forces investors to make affirmative decisions early in the process to join a case in order to recover anything on their losses or be

left with no remedy. In many cases, investors may be required to make these decisions before a foreign action is even filed. Therefore, in most instances, a legal and risk analysis should be conducted for each and every action (including competing versions of the same action) to help ensure that when an institutional investor joins a foreign action it makes sense both legally and economically.

Considering the complexity of the varying laws and rules for each country and jurisdiction, investors need comprehensive information with regard to each foreign jurisdiction's legal mechanisms for handling investor actions. As a result, it is critical to have a robust and timely mechanism for identifying and analyzing potential foreign actions and negotiating the economic terms and associated risks. As explained in Section C, outsourcing that function to domestic law firms or monitoring companies may be the most efficient use of resources for pension funds to monitor these issues.

In addition to the opt-in and timing issues, there are significant challenges posed by the funding mechanisms used in foreign jurisdictions. Many

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jurisdictions do not allow the typical contingency fee arrangements that are commonly used in the U.S. Rather, the cases are funded by groups that are called “litigation funders.” The litigation funders are third parties (typically corporate entities or U.S.-based law firms) who finance the cases, register investors, and generally manage the cases. Without such funding, foreign counsel would have to bill clients directly as the case progresses, and the clients would be required to pay substantial attorneys’ fees regardless of the outcome and recovery (if any) in the case.

The litigation funder takes on the risk of loss if the case is not successful (because it is the funder, rather than counsel, that underwrites the litigation’s costs and must pay the attorneys’ fees regardless of the outcome). In return for taking on this risk, the litigation funder earns a percentage of the proceeds if the case is successful, much like contingency fee arrangements in the U.S. In order to offset the risk assumed, litigation funders require a sufficient number of investors to register with them before they will commit to bringing the case. For this reason, institutional investors may have the ability to negotiate the funding agreements. This can be mutually beneficial if a fund brings sufficient losses to help the litigation funder reach the minimum level needed to file. In these cases, it may be beneficial for multiple funds to join together to negotiate favorable terms. Finally, it is also important to note that once a litigation funder closes its group and files the case, it is often too late to join the action, but sometimes the funder will reopen the group to allow more investors to join depending on the case.

Notwithstanding the monitoring challenges and the issues related to dealing with foreign jurisdictions, institutional investors may be at risk if they simply ignore foreign actions after *Morrison* because inaction could result in the institutional investors being barred from recovery while other investors with identical trading histories attain significant recoveries. This issue raises the question of whether institutional investors have a fiduciary duty to participate in foreign actions and whether they are breaching that duty by not participating in such actions. The risk of a breach of fiduciary duty is increased when an investor chooses to simply ignore foreign actions without knowing when

investments abroad have been impacted and without analyzing the economics and risks associated with legal procedures and substantive laws in these foreign jurisdictions. But on the other hand, an institutional investor must analyze whether joining the action will expose it to unacceptable levels of risk (e.g., in a loser-pays jurisdiction, whether there is sufficient indemnity or insurance coverage of the potential adverse costs). A list of potential factors for an institutional investor to consider is found in the section below.

Determining Whether To Participate In A Foreign Action

As discussed above, investors must confront the difficulties in identifying and tracking foreign actions, evaluating the differences in various overseas legal procedures and substantive laws, and they must do so in a timely fashion, before the opt-in period for a foreign action closes. If a U.S. fund wants to ensure that it capitalizes on all recoveries in both domestic and foreign actions, it must develop a protocol to stay informed and make prudent decisions relating to its involvement in foreign actions which, unlike domestic cases, require a proactive strategy to ensure timely registration for meritorious cases.

First, institutional investors should determine whether they want to establish a loss threshold and only consider participation in foreign actions when losses equal or exceed that amount. Loss thresholds may be established by weighing the amount of losses against factors like the amount of work that will be involved in participating in the action, the anticipated duration of the litigation, and the likelihood of recovery. It may make sense for the loss threshold to differ depending on the jurisdiction. For example, although Australia generally requires an investor to “opt-in” to an action before it is filed, once an investor has “opted-in” the investor’s role in the litigation is similar to being a passive class member in the United States. The limited amount of work involved in Australian actions may lead a public pension plan to establish a low or minimal loss threshold for evaluating Australian actions.



When determining whether a loss meets or exceeds an established threshold, it is important to consider how losses are calculated in the particular jurisdiction. First-In/First-Out (“FIFO”) and Last-In/First-Out (“LIFO”) calculations of losses are not always translatable to recoverable damages in foreign jurisdictions. Where case precedent or other guiding framework exists, care should be taken to estimate losses based on a method that will likely be used in the jurisdiction. On the other hand, it may be that there is limited or no case precedent in a given jurisdiction, in which case FIFO or LIFO may be the best methods for estimating a fund’s losses.

If a U.S. fund wants to ensure that it capitalizes on all recoveries in both domestic and foreign actions, it must develop a protocol to stay informed and make prudent decisions relating to its involvement in foreign actions which, unlike domestic cases, require a proactive strategy to ensure timely registration for meritorious cases.

After assessing the amount of losses and determining whether a loss meets or exceeds an established threshold, it is important to further analyze the action in order to determine whether to participate or, conversely, in order to be able to explain at a later stage why the fund decided it was not prudent to participate. Some of the key questions to keep in mind when evaluating foreign actions include:

1. Is the jurisdiction where the action is being brought and the law in that jurisdiction favorable? What are the potential risks, including adverse party cost orders and discovery, of being involved in a case there? What are the merits of the case and the likely defenses in light of the law in that jurisdiction? Is there any precedent at all for the legal theory or is it the first application of a new statute?
2. How is the action being funded? Who are the funders (including their investors) and are the funders reliable? Are the funders providing insurance or indemnification for the benefit of the investors? Will the funder agree to apply the fund’s home state law for the resolution of any dispute? What fee is the funder taking from the case and how is it calculated? Is this percentage fee the entire fee, or is the funder also entitled to reimbursement of expenses and any costs? Are these items negotiable?
3. What are the terms of the litigation funder’s rights of termination? Does the funder have to provide notice? Does your fund have termination rights? What are the costs associated with termination? What rights does your fund have to attorney work-product after termination?
4. What is the process and cost for opting in and is there a cost or subscription fee for doing so?
5. Who is the foreign counsel, what is their experience and reputation, do they have



U.S. offices, and how are they being paid? What are the requirements for powers of attorney?

6. What are the financial risks (*i.e.*, is there a possibility that your fund could be asked to pay the legal costs of the defendant if an action is not successful, as is normally the case in the U.K.)? Are financial risks capped by statute or otherwise limited? If there are financial risks, are the funders offering indemnification or litigation insurance and are the indemnitors or carriers properly funded, reputable and reliable?
7. What are the corporate governance terms; what role will your fund play or be allowed to play? No role, active role? How are the decisions made in the case? Do you have any say in anything? Will the litigation funder and/or lawyers agree to provide regular updates and copies of pleadings translated into English? Do you have approval rights over settlement decisions?
8. What is the size of your recoverable loss? How are losses calculated in this jurisdiction? Did the alleged wrongdoing cause the loss?
9. What time and resources will your fund have to devote to the foreign litigation? Will participation require staff to travel to the foreign jurisdiction?
10. What other investors are in the group and how large is the total expected claim to be brought on behalf of the entire group? What are the potential discovery burdens?
11. What are the real deadlines to join and can your fund comply with the appropriate deadlines?

These are just some questions funds will need to answer in determining both whether to act and how best to act in foreign jurisdictions.

B. ANALYSIS OF POTENTIAL ASSET RECOVERY ACTIONS (EVALUATING PARTICIPATION AGREEMENTS/FUNDING AGREEMENTS FROM COMPETING GROUPS)

Over the past several years, there has been both an overall increase in the number of foreign actions and an increase in the number of competing actions or potential actions announced against one particular company that alleges the same or substantially similar facts and legal claims. For example, in the recent case against *Fortis* there were at least four competing actions, three of which proceeded in The Netherlands and one of which proceeded in Belgium. And the case against *Fortis* was not unique. More recently, in the claims against *Volkswagen* there were at least seven competing groups, some of which are proceeding in Germany and some in The Netherlands. In *Olympus*, there were two competing groups that brought separate actions. Serious allegations of fraud or corporate malfeasance almost always lead to an announcement of more than one competing action. Complicating matters is the fact that in most jurisdictions outside the United States, investors are required to “opt-in” or file their own individual or group claim—there is no class action procedure that ensures that only one case may proceed or that all investors can recover a portion of any settlement or judgment. Not all competing actions are created equal and it is important to understand how to decide in which foreign action to participate when there are competing actions. Some factors that should be evaluated when assessing competing actions are:

- The experience of the law firms/funders that are pursuing a given action. In many jurisdictions, a case may be a case of first impression or there may be limited precedent. In that case, it is important to consider the funders’ experience organizing and funding other actions outside the United States as well as the experience and expertise of the local counsel.
- The proposed class period. Do the facts and claims support the proposed class period?



Different groups may propose different class periods and a fund should analyze its own trading under each option.

- The participation deadline. Is the advertised deadline based on a legal limitation period? Or is the deadline based on the attorneys' case strategy? Or is the deadline a "false" deadline that may be extended or may the fund join provisionally, with rights to drop out within a certain deadline?
- The method for calculating losses and damages. Is there known case precedent or a known legal basis for the method that the action is using to calculate estimated losses and damages? Different groups sometimes utilize different damages theories.
- Eligibility to participate. Some litigation funders require certain loss thresholds or other criteria to join the action. It is important to ask whether the action is available to the fund and if the funder is imposing reasonable criteria. Some funders may offer "early mover" discounts to entice funds to join in return for rights to share the fact that the fund joined with other funds. Other funders may offer group joinder discounts, allowing funds to join together to achieve lower pricing.
- Jurisdiction. Various groups may propose filing in different jurisdictions. Is there a strong legal basis for all the proposed jurisdictions? Does the fund have standing in all proposed jurisdictions? If all jurisdictions likely have a legal basis to hear the dispute, what are the procedural differences? What are the differences in the legal claims that will be pursued? What will be required of the fund in order to proceed in each of the jurisdictions (evidence, paperwork, testimony, etc.)? Are all the jurisdictions "loser pays" jurisdictions and is there a risk that the fund might be responsible for paying the defendants' costs and fees in the event that the action is not successful? What is the likely timeframe

in which the litigation will be resolved (the judicial system in some countries is much slower than in others)?

- The funding arrangements. Litigation funders charge either a percentage of any recovery or a multiple of the amount the funders spend on the prosecution of the case. Fees premised on the percentage of recovery can range from 10% to 40% depending on several factors such as the amount of the overall recovery and the timing of the recovery. Fees based on a multiple of the amount expended can range from 1.5 to 6 times the amount of the funding costs. Public pension funds, in order to best protect the interests of their members and fulfill their fiduciary duties, must not only consider the least expensive funding option, but take care to evaluate both the economic terms and other factors, such as the proposed legal strategy of the funders/group and the funder's experience. A lower cost option that results in a lower (or no) recovery in many cases is not in the best interest of the investor/litigant. Below are some of the factors to evaluate:
 - a. Are litigation expenses included in the funding fee or does the funding agreement call for reimbursement of expenses plus the funding fee? If expenses are to be reimbursed from the recovery, is there a cap on the amount of expenses that can be recovered? Is the funding fee based on the net recovery (after expenses are deducted) or the gross?
 - b. Is there an ability to negotiate a lower fee? Is there an ability to join together with other funds to negotiate a lower funding fee? Are all participants in the action paying the same fee (either as a percentage or a multiple)? Can the fund secure most favored nation pricing arrangement?
 - c. What is the funding group's legal strategy



and what is included in the funding fee? Is this group proposing to actively litigate a case, or merely to attempt to negotiate a settlement, or follow other proceedings? Does the requested fee structure adequately address the expected costs of the strategy?

- d. Will the funders indemnify the fund from any risk of adverse costs? Or has the funder obtained insurance to protect against adverse cost risk? What are the *bona fides* and financials of the source of that risk protection?
- e. Does the funder require a minimum loss threshold in order for an investor to be eligible to participate in that action? Minimum loss thresholds vary greatly depending on the jurisdiction, the case, and the funders involved.
- f. Can you withdraw from participation in the action? If you withdraw, will the funder require the fund to reimburse any of the costs or expenses and what happens to attorney work-product?
- g. Who has the discretion to settle the case? Who has the discretion to appeal?
- h. What protections are in place if the funder decides to stop funding the action?

It can be challenging to decide between competing actions but by conducting adequate due diligence and evaluating the proposed legal strategy, investors can ensure that they make a prudent decision and join an action that best protects the fund.

C. THE ROLE OF DOMESTIC LAW FIRMS/MONITORING COMPANIES IN FOREIGN LITIGATION (REFERRAL FEES EXPECTATIONS)

Use of a domestic law firm or monitoring company to assess and monitor foreign litigation can be an efficient way to exercise a pension fund's fiduciary

obligations to maximize recoveries in the event of securities law violations. In some instances, a pension fund may not have the time, resources, or background and expertise to undertake this process. A domestic law firm or monitoring company can provide a variety of services that the pension fund would otherwise have to perform itself.

Domestic Law Firms

A domestic law firm can provide services to a fund that include analyzing the case and the relevant law to determine whether participation is feasible for a particular fund, acting as a liaison with foreign litigation attorneys, and monitoring the case on an ongoing basis, including providing guidance regarding strategy and settlement.

First, the domestic law firm can analyze particular cases and jurisdictions for a fund, including competing actions. Funds have different loss thresholds and goals when getting involved in foreign litigation and a domestic law firm can provide an in-depth analysis for the individual funds. For example, cases like *Volkswagen* are brought in multiple jurisdictions—in that case, the jurisdictions include actions in The Netherlands under a Dutch settlement foundation and as active litigation in Germany. Although it may make sense for one fund to join the Dutch settlement foundation for a myriad of reasons, another pension fund may seek to join the active litigation in Germany for other reasons. A domestic law firm can provide guidance as to which action (if any) is most appropriate for the fund's goals.

Second, once the fund determines to join a particular case, the domestic law firm can act as a liaison to foreign litigation attorneys. Given the growing field of foreign securities litigation, qualified domestic law firms will have or will seek to obtain connections to foreign attorneys who will ultimately be responsible for litigating the case. These relationships allow the domestic firms to have confidence in selecting competent foreign counsel for a particular litigation. Without the use of a domestic law firm as a liaison, a pension fund would otherwise need to evaluate the capabilities of foreign attorneys in circumstances where



the fund might not have sufficient information to make that evaluation.

Finally, by retaining a domestic law firm to oversee foreign litigation, a fund can rely on the litigation being attended to by knowledgeable attorneys who will manage the fund's obligations in the foreign action. A qualified and experienced domestic law firm will have extensive experience in the resolution of complex securities actions. The domestic law firm can leverage this experience in engaging with foreign firms and defendants in the resolution of claims. While U.S.-style class actions have begun to spread around the globe, there are still relatively few non-U.S. firms with substantial experience in handling complex securities class actions. Accordingly, a well-qualified domestic law firm can provide substantial guidance both to clients and foreign attorneys regarding litigation strategies, valuation of claims, and settlement negotiations. Using a retained domestic law firm can also ensure that any foreign recovery is actually obtained, and that a fund's claim in a foreign action is properly submitted. Because most foreign actions require some level of active participation or are "opt-in" proceedings, having a domestic law firm guide and manage this unfamiliar process may be a prudent undertaking.

In selecting a domestic law firm to analyze and coordinate foreign litigation, care should be taken in assessing the firm's experience in handling foreign litigation, as well as evaluating the firm's relationships with foreign lawyers in the relevant jurisdictions. Additionally, funds should review the method by which the firm will be paid for its services.

Many domestic law firms will assess and monitor foreign litigation on a contingency basis. In those cases, there will typically be little or no out-of-pocket up-front expense to participating in a foreign litigation or claim process. Generally, the fee that goes to the domestic firm will typically be in the form of a referral fee paid out of any recovery obtained by the foreign litigators. Depending on the level of activity and oversight provided by the firm, these fees can vary. As a general matter, the fees will be higher in actions where the firm plays an active role in litigating the action. A fund should request disclosure of the referral

fee and an understanding from the domestic law firm as to the role of the domestic firm in litigating the case. Further, a fund should request information about the litigation funders for a particular case and whether the domestic law firm has a financial interest in the litigation funder which may create a potential conflict of interest.

Alternatively, some domestic law firms will agree to assess and monitor foreign litigation on an hourly or fixed fee basis, with fees paid directly by the fund as work is completed. Using this approach may be more costly to the fund in the short term, but provides a separation between the firm and the foreign litigation funder by which the fund may command better terms in the fee agreement negotiations and an additional layer of independence in evaluating competing options for recovery.

Domestic Monitoring Companies

A number of private companies in the U.S. offer monitoring and claims filing services for both domestic and foreign actions. These companies maintain

A domestic law firm can provide services to a fund that include analyzing the case and the relevant law to determine whether participation is feasible for a particular fund, acting as a liaison with foreign litigation attorneys, and monitoring the case on an ongoing basis, including providing guidance regarding strategy and settlement.



databases of pending, current, and past securities class actions or group action lawsuits and settlements, monitor all class action activity, and match actions with institutional investors' historical transaction data.

The companies that offer foreign monitoring services have generally developed relationships with attorneys in various countries and are able to identify and evaluate a client's exposure in cases that are being investigated (pre-filing) as well as pending cases. These companies do all or some of the following: (i) monitor securities actions being considered and brought in non-U.S. jurisdictions ("Foreign Actions"); (ii) perform electronic portfolio screening and loss calculations for Foreign Actions; (iii) identify and notify clients of Foreign Actions in which the client has an interest ("Relevant Foreign Actions"); (iv) register the client for Relevant Foreign Actions; (v) provide ongoing monitoring of Relevant Foreign Actions where appropriate; (vi) provide full claims recovery services in Relevant Foreign Actions that settle or otherwise result in a recovery; and (vii) provide quarterly reports of monitoring and claims-recovery activities for Foreign Actions. These companies are often able to provide these services on an a la carte basis or provide the full array of services, depending on the goals of the fund.

If a fund decides to utilize a monitoring company to monitor its global portfolio, it is important to perform due diligence to ensure that the provider has the ability to protect the portfolio internationally. Some questions for funds to ask include:

1. Which countries do you provide services for, and what types of services are offered for each?
2. What is your process for identifying potential and/or existing foreign (whether class, or more likely, individual) securities actions? How do you receive the information about foreign cases and, typically, when are you notified of the cases?
3. What advice and information are you able to provide to your clients regarding participation

in foreign cases, including the legal process in each jurisdiction?

4. How do you handle "opt-in" cases? What services do you provide for such cases?
5. Do you work with third parties to provide any of your foreign litigation services? If so, which types?
6. What are your fees? Some foreign monitoring services charge on a contingency, net of what the litigation funder charges. Other companies charge a flat fee for some of these services and funds should consider whether these fees are prudent given the potential size of recoveries and the services provided.

D. EVALUATION OF FOREIGN COUNSEL

Evaluation of counsel is of the utmost importance in all legal actions. Legal counsel plays an important role not only in appropriately advising the fund(s), but in many cases will be a decisive factor in the ultimate success of an action. Evaluating and selecting foreign counsel poses unique challenges. Although the number of foreign actions is increasing, the number of actions pursued in any single jurisdiction is still small. Given the limited number of actions pursued in any given foreign jurisdiction, it is not likely to be feasible to issue RFPs or to select foreign counsel on the basis of a pre-approved roster. Evaluation of foreign counsel is more likely to occur on an ad hoc basis, but should still be thorough and consider factors like:

1. Prior experience handling securities/shareholder litigation. If there is limited past precedent, then consideration of the size and complexity of an attorney's or law firm's prior cases may also provide valuable insight.
2. Past results in settlements and overall success rates.
3. Reputation of the attorney or the law firm in the local community and/or in the international legal community. Was the attorney or law firm ranked in publications like Chambers



and Partners? Was the attorney or law firm recommended by anyone?

4. The English-language ability of the attorney or law firm. Although it is more important that the attorney or law firm be able to zealously represent the fund in the courts in the local jurisdiction, it is also beneficial if the attorney or law firm can explain the legal proceedings and developments to you.
5. Relationship with a third-party funder or domestic law firm.
6. Availability to pursue an action and advise investors. In many jurisdictions outside the United States, attorneys do not specialize as plaintiff's attorneys or defendant's attorneys, but instead will represent clients on either side of a dispute. It can, therefore, be very important to determine whether an attorney or law firm has any conflict with potential defendants.
7. Limitations on liability. Foreign counsel may require clients to agree to a limitation on liability for the action pursued. It is important to understand what any limitations are, and how they apply to the fund individually as well as to the group as a whole.

Thoroughly evaluating potential local counsel can ensure both that the fund has a better chance of recovering investment losses and that it is receiving proper advice and making the best decisions for the fund.



Survey Of Countries



A. AUSTRALIA

Overview

Class actions have been available in the Federal Court of Australia since March 1992.¹⁶⁰ Australia was one of the first countries outside of the United States to introduce comprehensive class action regimes, which was achieved through the enactment of Section IVA (“Representative Proceeding Act” or the “Act”) of the *Federal Court of Australia Act 1976* (Cth), on March 4, 1992.¹⁶¹ In passing the Representative Proceeding Act,

the Australian Parliament hoped to provide access to the courts to those in the community who had been effectively denied legal redress because of the high cost of taking action. The general philosophy underpinning the policy goal of modern class action regimes, commonly known as the judicial economy goal, is the efficient use of finite judicial resources.¹⁶² Group actions or representative proceedings may also be conducted in the state Supreme Courts of Victoria¹⁶³ and New South Wales¹⁶⁴

¹⁶⁰ Brief of the Government of The Commonwealth of Australia as Amicus Curiae in Support of the Defendant-Appellees attached to Australian Government Submission to the SEC, February 18, 2011 at 17, available at <http://www.sec.gov/comments/4-617/4617-34.pdf>.

¹⁶¹ Jane Caruana and Vince Morabito, Australian Unions—the

Unknown Class Action Protagonists, *Civil Justice Quarterly*, Issue 4, 2011 at 382.

¹⁶² *Id.* at 384.

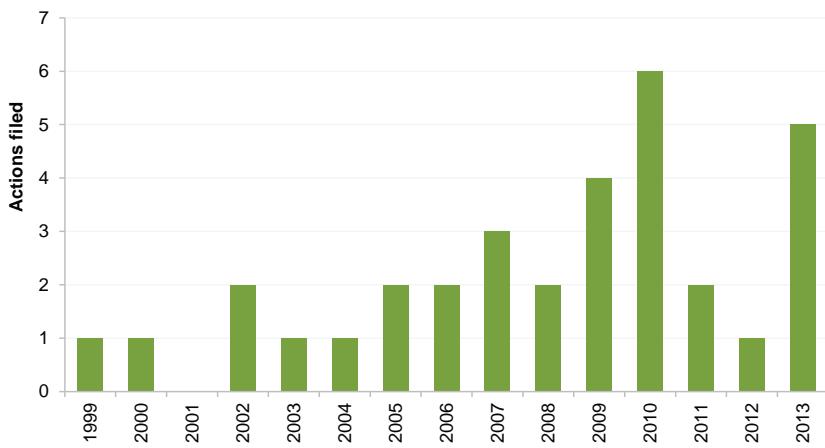
¹⁶³ Part 4A of the *Supreme Court Act 1986* (Vic).

¹⁶⁴ Part 10 of the *Civil Procedure Act 2005* (NSW).



but other states and territories have yet to introduce their own class action procedures.

The first securities class action was filed in Australia in 1993. The second, and first successful one, was filed in 1999. About one per year was filed thereafter until 2004, at which point the number increased steadily through 2009 when six were filed.¹⁶⁵ Shareholder class actions have increased in the past 11 years, but not significantly so, as demonstrated in the graph below:



Data Source: Allens (2014) displayed as it appears in the Productivity Commission's report, 2014, figure 18.3, 620.

Shareholder Class Actions Filed

Over the last 21 years, class actions comprised only about 0.4 percent of federal actions, (or about 0.1 percent of all actions). On average, about 14 class actions are commenced per year.¹⁶⁶ According to one study, only 9.9 percent of all class actions commenced between 1992 and 2009 were shareholder claims.¹⁶⁷

¹⁶⁵ National Economics Research Associates, Inc. “NERA” Economic Consulting, Trends in Australian Securities Class Actions: 1 January 1993-31 December 2009, available at <http://www.nera.com/publications/archive/2010/trends-in-australian-securities-class-actions-1-january-1993-.html>.

¹⁶⁶ Morabito V, *An Empirical Study of Australia’s Class Action Regimes*, First Report (December 2009), at 11.

¹⁶⁷ Ibid at 3.

Basics of Filing a Claim and Litigation

A proceeding under the Representative Proceeding Act may be commenced where: (a) seven or more persons have claims against the same person; (b) the claims of all those persons are in respect of, or arise out of, the same, similar or related circumstances; and (c) the claims of all those persons give rise to a substantial common issue of law or fact.¹⁶⁸

The Act states that it is irrelevant: (a) whether or not the relief sought: (i) is, or includes, equitable relief; or (ii) consists of, or includes, damages; or (iii) includes claims for damages that would require individual assessment; or (iv) is the same for each person represented; and (b) whether or not the proceeding: (i) is concerned with separate contracts or transactions between the respondent in the proceeding and individual group members; or (ii) involves separate acts or omissions of the respondent done or omitted to be done in relation to individual group members.¹⁶⁹

Unlike the U.S. system, no initial class certification filing is required in Australia. Specifically, the burden is placed on the respondent to show that it is *not* appropriate for the claims of the plaintiffs to be pursued by way of the class action.¹⁷⁰ The counterbalancing factor to the absence of initial class briefing in Australia is the presence of a “loser pays” cost rule.¹⁷¹ Another difference is that, although Rule 23(b)(3) of the U.S. Federal Rules of Civil Procedure requires that the issues common to the class must “predominate” over the individual issues, the Australian statute requires only that there exist a “substantial common issue of law or fact.”¹⁷²

¹⁶⁸ The Act Part IVA, Sec. 33C, http://www.austlii.edu.au/au/legis/cth/consol_act/fcoaa1976249/s33c.html.

¹⁶⁹ *Id.*

¹⁷⁰ Australian Government Submission to SEC, February 18, 2011, at 10; see also Act, Part IVA, Sec 33N http://www.austlii.edu.au/au/legis/cth/consol_act/fcoaa1976249/s33n.html.

¹⁷¹ Act, Sec 43 http://www.austlii.edu.au/au/legis/cth/consol_act/fcoaa1976249/s43.html.

¹⁷² *Id.*



To start the process, an application commencing a representative proceeding, or a document filed in support of such an application, must, in addition to any other matters required to be included: (a) describe or otherwise identify the group members to whom the proceeding relates; (b) specify the nature of the claims made on behalf of the group members and the relief claimed; and (c) specify the questions of law or fact common to the claims of the group members. In describing or otherwise identifying group members for the purposes of application, it is not necessary to name, or specify the number of group members.¹⁷³ A group member may file an application to substitute another member as a representative party upon a showing that the current representative is not able to adequately represent the interest of the group members.¹⁷⁴ Trials are without a jury unless the Court orders otherwise.¹⁷⁵

Loser Pay Model

The representative party who brings the action has the formal responsibility for running the case and for complying with any orders made by the court and is liable for any costs awarded in favor of the class action defendant.¹⁷⁶ Costs may not be awarded against absent group members.¹⁷⁷

Opt-In vs. Opt-Out

Consent is not required to be a group member in a representative proceeding.¹⁷⁸ A member may opt-out using written notice by a date fixed by the Court. Except with leave of the Court, the hearing of the representative proceeding may not be commenced before that date.¹⁷⁹ In reality, due, in part, to the “loser pays” rule and the lack of contingent fees, most cases have involved “opt-in” sub-classes comprising group

members who have entered into a funding arrangement with commercial litigation funders before the action is filed. However, opt-out, or “open,” class actions have become increasingly popular because defendants are demanding the full release that an opt-out action can provide.

Extraterritorial Jurisdiction

Australia filed both an *amicus* brief in *Morrison* and a comment letter for the Study on Extraterritorial Private Rights of Action conducted by the SEC pursuant to Section 929Y of the Dodd-Frank Wall Street Reform and Consumer Protection Act.¹⁸⁰ In those submissions, the Government of the Commonwealth, not the Australian judiciary, took the position that *Morrison* is the proper interpretation of the reach of securities anti-fraud law based on issues of comity and the strict statutory interpretation of the U.S. securities laws. Australia pointed out that laws differ in Australia with different incentives and awards. For instance, as noted above, in Australia the general rule is that the loser pays the winner’s costs. Australia also pointed out that there were well-developed remedies available in Australia for U.S. investors to use. Therefore, it is clear that Australia was not taking a “hard line approach” to extraterritoriality. Rather, the Commonwealth acknowledged that, in fact, Australia explicitly provides for extraterritoriality under the “conduct and effects test” in its own law:

The Extraterritorial Jurisdictional Scope of Australia’s Legislative Regime Is Expressly Provided For

The market misconduct provisions in Part 7.10 of the Corporations Act apply to certain acts or omissions outside of Australia, but only when they are tied to conduct and effects in Australia. These include:

- manipulating a financial market in Australia;*

¹⁷³ Act, Sec. 33H, http://www.austlii.edu.au/au/legis/cth/consol_act/fcoaa1976249/s33h.html.

¹⁷⁴ Act, Sec. 33T, http://www.austlii.edu.au/au/legis/cth/consol_act/fcoaa1976249/s33t.html.

¹⁷⁵ Act, Sec 39.

¹⁷⁶ Jane Caruana and Vince Morabito at 387; Act, Sec 43.

¹⁷⁷ Act, Sec. 43(1A).

¹⁷⁸ Act, Sec. 33E, http://www.austlii.edu.au/au/legis/cth/consol_act/fcoaa1976249/s33e.html.

¹⁷⁹ Act, Sec 33J, http://www.austlii.edu.au/au/legis/cth/consol_act/fcoaa1976249/s33j.html.

¹⁸⁰ Australian Government Submission to SEC, February 18, 2011, attaching Brief of the Government of The Commonwealth of Australia as Amicus Curiae in Support of the Defendant-Appellees. <http://www.sec.gov/comments/4-617/4617-34.pdf>.



- *false trading on a financial market in Australia;*
- *dissemination of information about illegal transactions on a financial market in Australia; and*
- *making materially false or misleading statements that are likely to have the effect of increasing, reducing or maintaining the prices on a financial market in Australia.*¹⁸¹

*The ASIC Act also has provisions that reflect an Australia-focused approach to extraterritoriality. Section 12AC(1) extends various of the Act's prohibitions to conduct engaged in outside of Australia by: "(a) bodies corporate incorporated or carrying on business within Australia; or (b) Australian citizens; or (c) persons ordinarily resident within Australia." Thus, the Corporations Act and the ASIC Act differ from the approach taken by the U.S. Congress in the Securities Exchange Act of 1934, which was silent on the issue of extraterritorial application.*¹⁸²

Funding The Litigation - Contingent Fee Arrangements

Australia prohibits damages-based contingency fees, though it permits “no-win no-fee” arrangements and in some jurisdictions permits an “uplift” on professional fees of up to 25%.¹⁸³ The lack of a fee incentive for the lawyers, as well as the threat of adverse costs, also impacts the low number of securities suits filed since the passage of the group action device. However, as discussed below, litigation funding rules in many Australian jurisdictions are gradually easing.

¹⁸¹ See *Corporations Act*, §§1041B, 1041C, 1041D, 1041E; see especially §1041E(1)(b)(iii).

¹⁸² Brief of the Government of The Commonwealth of Australia as *Amicus Curiae* in Support of the Defendant-Appellees attached to Australian Government Submission to the SEC, February 18, 2011 at 11-12. <http://www.sec.gov/comments/4-617/4617-34.pdf>.

¹⁸³ “The push to reform class action procedure in Australia: evolution or revolution,” Melbourne University Law Review, Vol. 32 No. 3, December 2008.

As in the U.S., historically, litigation funding was prohibited in Australia as encouraging litigation (maintenance) and profiting from it (champerty).¹⁸⁴ That began to change with laws abolishing litigation funding as a crime or as a tort in Australia’s states and territories. In 1995, insolvency practitioners were allowed to contract for the funding of lawsuits, if the contract was characterized as property of the insolvent company---such as actions by the insolvent company against former officers and directors.¹⁸⁵ The funder paid the costs of litigation (which included attorneys’ fees) and accepted the risk of paying the defendants’ costs in the event of a loss, and indemnified the plaintiff for the same. In that context, fees ran between one and two thirds.¹⁸⁶

In *Campbells Cash and Carry Pty Limited v Fostif Pty Ltd.*,¹⁸⁷ Australia’s highest court considered the legality of litigation funding for the first time. The High Court held that litigation funding was not an abuse of process or contrary to public policy---existing doctrines of abuse of process and the courts’ ability to protect their processes would be sufficient to deal with a funder conducting themselves in a manner ‘inimical to the due administration of justice.’¹⁸⁸ The Court did not decide the position for those states where legislation had not abolished maintenance and champerty as crimes and torts (Western Australia, Queensland, Tasmania and the Northern Territory).¹⁸⁹

The closed model, opt-in, class action addresses the concern that the class action regime as an “opt-out” process would inevitably result in “free riders,” i.e. claimants who chose not to sign a funding agreement but who would benefit from the outcome of the class action without having to contribute towards its cost.¹⁹⁰ In *Multiplex Funds Management Ltd v. P. Dawson*

¹⁸⁴ Michael Legg, Louisa Travers, Edmond Park, and Nicholas Turner, *Litigation Funding in Australia*, University of New South Wales Faculty of Law Research Series, 2010 -12 at 3, available at <http://www.austlii.edu.au/journals/UNSWLRS/2010/12.html>.

¹⁸⁵ *Id.* at 4.

¹⁸⁶ *Id.* at 4.

¹⁸⁷ *Campbells Cash and Carry Pty Limited v Fostif Pty Ltd*, (2006) 229 CLR 386.

¹⁸⁸ Legg, Travers, Park and Turner at 6.

¹⁸⁹ *Id.* at 7.

¹⁹⁰ *Id.* at 2.



Nominees Pty. Ltd.,¹⁹¹ the Full Federal Court of Australia rejected respondents' attack on the "closed class" and permitted the use of a "limited group" or "closed class" that existed at the time the suit was commenced and provided that members could opt-out. The "sub-group" would be identified as those who entered into the funding agreement.¹⁹²

Other evolving issues include privilege, security for costs, and regulation of litigation funding, which has previously been held to constitute a form of managed investment scheme¹⁹³ for the purposes of the *Corporations Act 2001* (Cth).¹⁹⁴ It is likely more regulation will develop to protect investors and consumers.¹⁹⁵

Fraud On The Market Theory

A recent decision of the New South Wales Supreme Court involving HIH Insurance Limited has held that the principle of "indirect causation" or "market-based causation," which is similar to the fraud on the market theory, applies to the proof of causation in shareholder claims.¹⁹⁶ This is the first trial court decision on the merits to accept market-based causation in a shareholder suit. Prior to that decision the Full Federal Court of Australia had also considered 'indirect causation' in a strike-out context¹⁹⁷ (*i.e.*, similar to motion to dismiss proceedings),¹⁹⁸ where the Court held that indirect causation can be pleaded in shareholder actions. Prior to these decisions, there had been several significant settlements in Australia in shareholder class actions. In each of those cases, the shareholder claimants had sought to argue for 'indirect

causation' being a version of the "fraud on the market" theory, as it was said that causation could be an issue common to all members of the class where it could be demonstrated that the effect of the alleged misconduct was to cause the market as a whole to inflate the price of traded securities.¹⁹⁹

The court's acceptance of market-based causation in the HIH Insurance case, and rejection of the requirement to prove individual reliance as to the misleading conduct, may have important consequences. Some in the Australian legal community predict that plaintiffs will be more likely to demand larger settlements, or will push their cases farther to trial, rather than settling at a discount in recognition of the risks of proving individual reliance.²⁰⁰

The decision in *HIH Insurance*, however, is likely to be tested on appeal. Until the appellate courts weigh in on the issue, uncertainty as to the application of indirect causation to shareholder suits will remain.

Quantification of Damages

Like issues of causation and reliance, the proper approach to quantifying damages has been an area of uncertainty for class action litigators in Australia. Plaintiffs have generally employed several damages models, given that they do not know which one the court will ultimately accept.²⁰¹ Three main models include: (1) the "what's left in the hand" approach, which compares the share purchase price to the market price on a particular date (if the shares are held) or to the sale price (if sold), but any factors that may have affected the share price beyond the unlawful conduct are ignored; (2) an attempt to determine the effect on

¹⁹¹ *Multiplex Funds Management Ltd v. P. Dawson Nominees Pty Ltd*, (2007) 164 FCR 275.

¹⁹² Legg, Travers, Park and Turner at 14 -16.

¹⁹³ *Brookfield Multiplex Ltd v. International Litigation Partners Pte Ltd* [2009] FCAFC 147.

¹⁹⁴ The Australian Federal Government has since enacted the *Corporations Amendment Regulation 2012* (No.6)(Cth) to effectively exempt litigation funding from all forms of regulation, save for a requirement to have adequate processes in place to manage conflicts of interest.

¹⁹⁵ *Id.* at 17-43.

¹⁹⁶ *HIH Insurance Limited (In Liquidation) and others* [2016] NSWSC 482.

¹⁹⁷ *Caason Investments Pty Ltd v. Cao* [2015] FCAFC 94.

¹⁹⁸ *Caason Investments Pty Ltd v Cao* [2015] FCAFC 94.

¹⁹⁹ Andrew Watson and Jacob Varghese, *The Case for Market-Based Causation* (2009) 32 University of New South Wales Law Journal 948, available at http://www.unswlawjournal.unsw.edu.au/sites/default/files/49_watson_2009.pdf.

²⁰⁰ See Mariana Papadakis, HIH court decision means companies face more risks in shareholder actions, *The Australian Financial Review*, Apr. 21, 2016, at <http://www.afr.com/business/legal/hih-court-decision-means-companies-face-more-risks-in-shareholder-actions-20160421-gobs9r>.

²⁰¹ Rachel Nickless and Hannah Low, "Class actions adrift in uncertain waters," *The Australian Financial Review*, Mar. 5, 2010, at <http://www.afr.com/business/legal/class-actions-adrift-in-uncertain-waters-20100304-ivwze>.



an omission on the valuation of the company had the omitted information been disclosed at the proper time; and (3) the event study approach employed in U.S. shareholder actions.²⁰²

The court in *HIH Insurance* adopted its own approach to quantifying damages (somewhat akin to the second method mentioned above), despite a different analysis proffered by the plaintiffs. In that case, shareholders of HIH Insurance alleged that the company had improperly accounted for certain reinsurance arrangements. A proper accounting would have reduced HIH Insurance's profits and net assets. In the court's view, the damages had to relate specifically to the unlawful conduct, and not to any other additional matters that may have affected the "true value" of the shares. In making this calculation, the court observed that "[p]recisely how the market would have responded had the [reinsurance arrangements] been properly accounted for cannot realistically be the subject of precise proof, and necessarily involves hypothesis and a degree of speculation."²⁰³ Ultimately, the court determined that HIH Insurance's book value was "the single most important indicator of value," and it held that "the impact of the contravening conduct is represented by the difference between the price at which HIH shares actually traded on the market, and the hypothetical price achieved by applying the price to book value at which they traded to an adjusted book (adjusting for the [improperly accounted for reinsurance arrangements])."²⁰⁴ As applied by the court, during one time period the adjusted book value was 9.5% lower than the reported book value, so investors that acquired shares during that period were entitled to damages equivalent to 9.5% of the purchase price paid.²⁰⁵

Notably, the *HIH Insurance* decision included no discussion of *Dura*-type loss causation issues.

Causes Of Action In Securities Litigation

Most securities class actions in Australia are heard by the Federal Court of Australia, which has

jurisdiction over matters concerning Commonwealth legislation, including legislation that serves as the basis for most securities class action claims. Such actions typically arise out of the *Corporations Act 2001* (Cth), the *Competition and Consumer Act 2010* (Cth) (which, prior to January 2011, was the *Trade Practices Act 1974* (Cth)), and/or the *Australian Securities and Investments Commission Act 2001* (Cth), all of which provide specific legislation mechanisms to enable aggrieved shareholders to seek redress arising from corporate misconduct.²⁰⁶

More specifically, many claims allege that the respondent violated the disclosure rules imposed on listed companies²⁰⁷ and/or they allege violations of the Corporations Act 2001 prohibition on misleading or deceptive conduct in connection with securities. Additionally, allegations often include breaches of fiduciary trust.²⁰⁸

Chapter 7.10 of the Corporations Act contains prohibitions relating to insider trading, market manipulations, and various other types of fraudulent and misleading conduct. Prohibited conduct includes: (i) market manipulation (s.1041A); (ii) false trading and market rigging (creating a false or misleading appearance of active trading) (s.1041B); (iii) artificially maintaining trading price (s.1041C); (iv) dissemination of information about illegal transactions (s.1041D); (v) false or misleading statements (s.1041E); (vi) inducing persons to deal (s.1041F); (vii) dishonest conduct (s.1042G); and (viii) misleading or deceptive conduct (s.1041H). With the exception of misleading or deceptive conduct (s.1041H), for which there is civil liability only, these types of conduct are all criminal offenses and breaches are subject to both criminal prosecutions and civil actions. The Corporations Act also provides statutory backing for the continuous disclosure requirements imposed on listed entities by

²⁰⁶ *Corporations Act 2001* (Cth), § 674 (continuous disclosure), §1041H (misleading conduct); *Australian Securities and Investments Commission Act 2001* (Cth), §12(DA)(misleading conduct); *Trade Practices Act 1976* (Cth) § 52 (misleading conduct); *Competition and Consumer Act 2010* (Cth); and Australian Consumer Law § 18 (misleading conduct).

²⁰⁷ ASX Listing Rules, Rule 3.1, <http://www.asx.com.au/documents/rules/Chapter03.pdf>.

²⁰⁸ Luke Green, *supra*.



securities markets (s.674) and enables courts to order compensation in relation to breaches (s.1317HA).²⁰⁹

Australia laid out the availability of the private rights of action of investors in its *amicus* brief in *Morrison*:

Civil remedies that may apply to a claim of the type alleged in this case are found in Part 7.10. In that Part, § 1041I makes available private civil actions for those injured by (i) false and misleading conduct (§ 1041E); (ii) improperly inducing someone to deal (§ 1041F); (iii) dishonest conduct (§1041G); or (iv) misleading or deceptive conduct (§1041H).

A contravention of the continuous disclosure requirements in Chapter 6CA of the Corporations Act that are applicable to listed entities may also give rise to civil damages. By §674, such entities are required to comply with the continuous disclosure requirements in the listing rules of the financial markets on which their securities are traded.... Section 1317HA empowers a court to order the payment of compensation for damages suffered as a result of a contravention of § 674.

The [Australian Securities and Investments Commission, (“ASIC”)] Act also provides a private civil action in § 12GF for those injured by: (i) unconscionable conduct (§§ 12CA-CC); (ii) misleading or deceptive conduct (§ 12DA); or (iii) false or misleading representations (§ 12DB).

*Civil actions under the Corporations Act and the ASIC Act can be brought in a federal court or the courts of an Australian state or territory having jurisdiction over the defendant(s). Appellate review is available in each jurisdiction.*²¹⁰

²⁰⁹ Australian Government Submission to SEC, February 18, 2011, at 9-10.

²¹⁰ Brief of the Government of The Commonwealth of Australia as Amicus Curiae in Support of the Defendant-Appellees attached

Regulatory Environment for Securities Litigation

The Australian Securities and Investments Commission (“ASIC”) is responsible for overseeing corporations and market integrity, including disclosure standards and consumer protection. ASIC regulates Australian companies, financial markets, financial services organizations, and professionals who deal and advise on investments, superannuation (*i.e.*, retirement pension), insurance, deposit taking, and consumer credit. ASIC is also responsible for registering and supervising the operation of managed investment schemes.²¹¹

The level of foreign investment in Australia increased by A\$220.5 billion (US\$159.4 billion) in 2015 to reach A\$3,024.4 billion (US\$2.2 trillion). Portfolio investment accounted for A\$1,622.7 billion (US\$1,173.3 billion or 54%), direct investment for A\$ 735.5 billion (US\$531.8 billion or 24%), other investment liabilities for A\$485.6 billion (US\$351.1 billion or 16%), and financial derivatives for A\$180.6 billion (US\$130.6 billion or 6%). Of the portfolio investment liabilities, debt securities accounted for A\$1,162.3 billion (US\$840.4 billion or 38%) and equity securities for A\$460.4 billion (US\$332.9 billion or 15%).²¹²

According to the Australian government in its *amicus* brief in *Morrison*, it welcomes and embraces the new class action regime:

Senior ASIC officials have also welcomed the creation of this type of action. In 2005, ASIC’s Deputy Chairman explained that “[t]he increase in shareholder vigilance, coupled with the emergence of shareholder class actions, means that ASIC is better able to focus on its surveillance and enforcement functions while shareholders

to Australian Government Submission to the SEC, February 18, 2011 at 15-16. <http://www.sec.gov/comments/4-617/4617-34.pdf>.

²¹¹ U.S. Department of State, Bureau of Economic, Energy and Business Affairs, 2011 Investment Climate Statement—Australia (March 2011), available at <http://www.state.gov/e/eb/rls/othr/ics/2011/157234.htm>.

²¹² Australian Bureau of Statistics, available at <http://www.abs.gov.au/ausstats/abs@.nsf/mf/5352.0>.



*play a proactive role in protecting their interests.... "(footnote omitted)*²¹³

ASIC is also, purportedly, very active in enforcing investor rights:

Finally, ASIC, using its statutory power to institute civil actions on behalf of injured investors, has brought class actions in circumstances where it believed that the victims lacked the financial resources to pursue the case themselves. To date, ASIC has brought at least nine securities class actions on behalf of victims. 42 were filed in 2006, five were filed in 2007, eight were filed in 2008, and at least nine were filed in 2009. In the still-pending Westpoint related financial products cases, ASIC has already recovered for investors some \$A100 million of the \$A388 million invested. (footnotes omitted.)²¹⁴

Both the Australian Competition and Consumer Commission (“ACCC”) and ASIC have supported the role of class actions as private enforcement complements to their own regulatory role.²¹⁵ ASIC Chairman Greg Medcraft recently endorsed class action litigation, saying it was “very good at equaling up the tables” and was “a good market-driven solution,” but with the proviso that the class actions needed to be “done responsibly.”²¹⁶

²¹³ Amicus Brief at 18.

²¹⁴ *Id.* at 20-21.

²¹⁵ See, e.g., ASIC backs private litigation, Money Management, 25 June 2014.

²¹⁶ <http://www.theaustralian.com.au/business/opinion/asics-nod-to-class-actions-may-backfire/story-e6frg9if-1226324318161>.

B. BELGIUM



Class Actions - Extraterritorial Jurisdiction

The Act of 28 March 2014 on Claims for Collective Redress (“Collective Redress Act”) introduced the possibility of launching class actions in Belgium.²¹⁷ This class action procedure was enacted after various bills circulated among Belgium’s legislative branches and within academic circles, seeking to establish the legal right to commence a class action.²¹⁸ In 2011, the federal government led by Prime Minister Elio Di Rupo determined that it wanted to strengthen consumers’ rights by introducing proceedings for collective redress. Two proposals were submitted in Parliament in 2014. The Collective

Redress Act is part of a European trend: in this respect, the preparatory works of the Act of 28 March 2014 explicitly refer to the recommendation of the European Commission of 11 June 2013, but does not comply with it in all its aspects.

The principal hurdles to bringing class action claims in Belgium were Articles 17 and 18 of the Belgian Code of Civil Procedure (“BCCP”), which require that every party to a proceeding in a Belgian court have a *personal interest* and *capacity* in the claims asserted in order to have standing to prosecute those claims. The requirement that a plaintiff have a *personal interest* in the claims means that class actions were excluded under Belgian law because one plaintiff cannot file a claim on behalf of others. This principle also applies to corporate entities (a corporation cannot file a claim on behalf of its constituent members). Thus, claims introduced by consumer associations with the aim of protecting the general interest of claimants lacked standing under Belgian law.

²¹⁷ The Collective Redress Act is inserted in title 2 of book XVII of the Code of Economic Law Belgian Official Gazette 29 April 2014. The Act entered into force on 1 September 2014 (Royal Decree of 4 April 2014 on the entry into force of certain books of the code of Economic law, Belgian Official Gazette 29 April 2014)

²¹⁸ Proposal of 16 August 2007, Doc Parl. 52/0109/001; Proposal of 22 February 2008, Doc. Parl. 52/0872/001; Proposal of 17 March 2008, Doc Parl. 52/0978/001; Proposal of 29 May 2009, Doc Parl. 52/2019/001.



Importantly, there are other statutory exceptions to Articles 17 and 18 which allow certain associations to collectively act before the court. For example, the following associations can seek injunctions:

- Associations defending consumers' interests with legal personality can request a cease and desist order with respect to unfair trade practices (Art. 98 of the Law on Trade Practices); and
- Associations defending the professional interests of members of a specific profession (*e.g.*, lawyers, doctors, architects...).²¹⁹

However, actions brought under this statute, especially for misleading practices, are rare primarily due to lack of funding and the fact that plaintiffs cannot seek damages.²²⁰

Another potential avenue for redress for defrauded investors is Belgium's criminal courts. Under Belgian law, any party that has suffered damages due to a defendant's tortious conduct – which also constitutes a criminal wrong – can join any criminal proceeding instituted by a government prosecutor. Defrauded investors can appear (*i.e.* join) the criminal proceeding as "civil parties"²²¹ and have their claims (for damages, restitution, etc.) adjudicated by the criminal court.²²²

These exceptions and alternative forms of redress, however, do not entitle parties to bring actions for damages before the courts.²²³ Thus, any of the cases in Belgium prior to the introduction of the Collective Redress Act involving multiple claimants represented by an association were not traditional class actions, but are more aptly described as mass (or collective) actions, in which each claimant has a demonstrable interest in the claims asserted and is appearing by proxy through

²¹⁹ See Law on Trade Practices and Consumer Information and Protection of 14 July 1991, Official Gazette of Belgium.

²²⁰ Matthias E. Strome & Evelyne Terryn, *Belgian Report on Class Action*, at 10-11 (2007).

²²¹ Denis Waelbroeck, Kelly Cherrette, and Aurelie Garth, *Belgium Report*, 4 (2004), available at http://ec.europa.eu/competition/antitrust/actionsdamages/national_reports/belgium_en.pdf.

²²² Matthias E. Strome & Evelyne Terryn, *Belgian Report on Class Actions*, at 3 (2007).

²²³ See March 1898 Act on professional organizations and the 5 December 1968 Act on unions.

the association. These group actions comply with Articles 17 and 18 because each claimant is itself either personally appearing or represented by proxy.

Examples of group actions include the *Lernout & Hauspie* ("L&H") and *Citibank Belgium* cases. A group action was commenced in Belgium in 2001 against L&H (a speech technology company) in the wake of its worldwide accounting fraud. The L&H case was brought by an investor protection association known as Société Anonyme Deminor ("Deminor"),²²⁴ which represented 13,000 claimants who suffered \$500 million in damages as the result of L&H's fraud. The limitations of the group were acutely demonstrated when Deminor, who had accepted claimants from September 2001 to April 2007, was forced to stop accepting additional claimants because each claim had to be individually analyzed and the service costs had become significant.²²⁵ Interestingly, in the L&H case, 5,000 victims filed their "civil party" claims in a criminal proceeding against L&H's founders and other defendants, as opposed to joining the group action. The court convicted eight of the 21 defendants in September 2010. The "civil party" claims are still pending.

In the *Citibank Belgium* case, Deminor commenced a group action against Citibank Belgium in 2008 in the Brussels Commercial Court as a result of the collapse of Lehman Brothers. Citibank Belgium had sold financial products issued and guaranteed by Lehman Brothers. After Lehman's collapse, 4,100 Citibank Belgium clients lost their savings (approximately 130 million Euros). Within 15 months, Deminor announced a settlement whereby investors received 68 percent of the face value of the Lehman notes. Notably, the Belgian Government filed a criminal complaint against Citibank Belgium and secured a conviction based on the misrepresentations made to investors. Sixty-three investors of Citibank Belgium filed "civil party" claims with the Criminal Court. Instead of accepting the proposed settlement

²²⁴ Deminor is a law firm that specializes in minority shareholder claims and is a "leading European company focusing on services to investors in Continental-European companies." See <http://www.deminor.com>.

²²⁵ Allen & Overy, *Belgium: Class & Group Actions 2010*, at 3 (Dec. 2009).



offer, the Criminal Court imposed fines on Citibank Belgium and awarded full (100 percent) compensation to all 63 investors.

Since September 1, 2014, consumers have had the right to file class actions. The Collective Redress Act is solely applicable to events that have occurred after its entry into force. The Constitutional Court of Belgium has ruled that the limitation of the Collective Redress Act to damages caused after the date on which the Act came into force does not violate articles 10 and 11 of the Belgian Constitution.²²⁶

Scope of the Collective Redress Act

The Collective Redress Act aims to deal with the claims of numerous aggrieved consumers in a global and efficient manner. The class action is only available to *consumers*, who are defined as natural persons acting for purposes that fall outside their trade, business, craft or professional activity.²²⁷

The defendants are limited to *companies*, which are natural or legal persons, pursuing an economic purpose in a sustainable manner, including associations.²²⁸ Autonomous state enterprises (such as bpost, Belgium's postal operator and universal services provider) can be defendants in a class action.

Only *violations of either contractual obligations or of a limited list of 31 Belgian and European legislative acts*, mainly focused on consumer protection, give rise to the right to initiate a class action, such as competition law, market practices and consumer protection,²²⁹ payment and credit services, safety of products and services, intellectual property, travel, energy, financial services regulations, privacy law, protection of electronic data as well as EU legislation on the rights of train passenger and airplane passengers.

The following financial law provisions, as well as their implementing regulations, are included in the list²³⁰:

- provisions on payment services and consumer credit (including consumer mortgage credit) (Chapter VII of the Code of Economic Law) (including compliance with the license and registration requirements);
- prohibition against the manipulation of reference;
- provisions setting out certain disclosure requirements, including the requirement to provide correct, clear and non-misleading information when offering or providing financial products or financial services (including the requirement to clearly identify marketing materials as marketing materials) to (potential) clients, this also includes certain MiFID disclosure requirements (information regarding the firm, the financial instruments and the proposed investment strategies, the places of execution and the costs);
- specific requirements regarding savings accounts offered to consumers;
- regulations with respect to: (i) product ban, (ii) product label and (iii) the use of the reference question lists: the Financial Services and Markets Authority (FSMA) has the power to ban the marketing of financial products to retail consumers conducting regulated activities without the appropriate license or registration;
- offering of collective investment funds (including AIFs) in breach of the relevant fund marketing regulations;
- public solicitation of funds without the appropriate licenses or registrations;
- regulations regarding certain financial sureties

²²⁶ Constitutional Court nr. 41/2016, 17 March 2016.

²²⁷ Article I,1, second bullet of the Code of Economic Law.

²²⁸ Article I,1, first bullet of the Code of Economic Law.

²²⁹ Book VI of the Code of Economic Law regarding market practices and consumer protection applies to the offering of financial services and financial products, including the public offer of securities (subject to certain specific implementing provisions).

²³⁰ <http://www.allenavery.com/publications/en-gb/european-finance-litigation-review/northern-europe/Pages/Introduction-of-the-Belgian-Collective-Redress-Act-and-Impact-on-the-Financial-Sector.aspx>.



- (granted without specific considerations); and
- regulations with respect to dormant accounts and safes.

Claims on the basis of tort are excluded, as well as disputes between shareholders and companies.²³¹

Finally, the class action will only be admissible if its use is deemed ***more expedient*** than initiating a claim in accordance with common judicial law.²³² This will be assessed by the court based on various elements such as the potential size of the group, the existence of individual damages that originate from the same cause, the complexity and the efficiency of the class action and the legal certainty for the consumers. The individual amount of damages is not a decisive element.²³³

Group Representative

The Collective Redress Act stipulates that the individual consumers themselves are not parties in the legal proceedings, but are represented by a group representative. This may either be a consumer protection association with legal personality that is represented in the Council for Consumption (*Raad voor Verbruik/Conseil de la Consommation*) or is recognized by the Minister, or an association that has had legal personality for more than three years, with a corporate purpose directly related to collective damages suffered by the group, which does not pursue an economic purpose in a sustainable manner and that is recognized by the Minister.

As discussed below, the Act establishes phases of class proceedings. Notably, the court will furthermore determine if the group representative is suitable as part of the “admissibility phase.” During the “negotiations phase,” the consumers can also be represented by the Federal Ombudsman.

²³¹ Note that claims for missellings are included in the scope of the Collective Redress Act, that refers to violations of Article 27 (2) and (3) of the Act of 2 August 2002 on the supervision of the financial sector and the financial services.

²³² Article XVII.36, first bullet Code of Economic Law.

²³³ Memorie van toelichting Parl. St. Kamer 2013-14, nr. 53K3300/001 and nr. 53K3301/001, p.8-9 and 21.

In its decision rendered on March 17, 2016, the Constitutional Court annulled article XVII.39 of the Code of Economic Law insofar that it did not allow representative entities established in other EU member States that meet the conditions set out in article 4 of the Commission Recommendation of 11 June 2013 on common principles for injunctive and compensatory collective redress mechanisms in the Member States concerning violations of rights granted under Union Law to act as group representative.

Phases of Proceedings

The Act sets out proceedings in four stages, if no settlement is reached before the claim is filed at the court. An amicable settlement obtained prior to the formal initiating of legal proceedings can be submitted to the court in order to have it ratified.

Admissibility Phase

First, the court assesses the admissibility of the claim within a period of two months after the complete request has been filed. If the claim is declared admissible, the court will have to include various elements in its decision such as a description of the collective damages and their cause, a description of the group of consumers and an estimate that is as accurate as possible of the number of aggrieved persons.

Furthermore, the court will determine whether the case will be governed by an opt-in system or an opt-out system when: (i) the consumer either has to make the explicit choice to join the proceedings (without becoming an actual party); or (ii) it will have the possibility to distance itself from the proceedings, in which case it will not be bound by its outcome. In principle, the court will decide at its discretion which mechanism will apply. However, in some cases, the opt-in system is compulsory (e.g. in case of bodily injury or moral collective damages). Opting-out is only applicable to Belgian residents.

Compulsory Negotiation Phase

If the claim is declared admissible, the group representative and the defendant have to enter into



negotiations on a possible settlement. The negotiation period starts after the term granted to opt in or out of the proceedings has expired and its duration varies between three and six months. Parties can involve a professional mediator.

An amicable settlement has to be ratified by the court, which may refuse to do so in four cases: The agreed-upon redress is apparently unreasonable; The period within which members of the group must address the clerk of the court to obtain individual redress is apparently unreasonable in case of an opt-out system; The additional publication measures are apparently unreasonable; and the compensation for the group representative exceeds the actual costs borne.

Litigation

If a settlement is not reached, the parties will litigate the case on its merits, within the boundaries of traditional court proceedings under Belgian judicial law.

Implementation Phase: Loss Administrator

A loss administrator is appointed (i) to carry out the ratified settlement; or (ii) if the claimants are successful on the merits. The loss administrator is entrusted with the task of distributing the compensation paid by the defendant to the claimants.

Both the settlement and the judgment will contain the content and the modalities of the redress. The purpose of the claim is to obtain individual redress. Punitive damages are not permitted.

Class Actions

Test-Aankoop, a Belgian consumer protection organization that meets the criteria to act as a group representative, has introduced two class actions. The first action was directed against Thomas Cook: compensation was sought for damages suffered by travelers who were delayed on a flight to Brussels from Tenerife. The other action was filed against the Belgian National Rail Company, to obtain damages for travelers due to the amount of strikes between December 2014 and October 2015.

Funding The Class Action - Contingent Fee Arrangements

Limitations Grounded in Belgium's Rules Of Civil Procedure

Belgian rules of civil procedure prohibit a lawyer from being paid solely on the outcome of a case.²³⁴ Strict no-win, no-fee agreements are prohibited.²³⁵ Success fee agreements, however, are permitted and can be added to a lawyer's main fees.²³⁶ Furthermore, the law on the recovery of attorneys' fees and expenses provides that the losing party must be ordered to pay a nominal amount called 'procedural indemnity' (i.e. a lump sum intended to cover a part of the lawyers' fees). The amount of the procedural indemnity, with a maximum of EUR 30,000, depends upon the value of the claim and the parties' financial situation.

Funding The Class Action

The Collective Redress Act does not contain any general rules on funding of the class action, the compensation or remuneration of the group representative. Compensation cannot be dependent on the outcome of the class action. Belgian doctrine defends the possibility for the group representative to obtain compensation for the actual costs incurred. In case of an amicable settlement, any compensation exceeding the actual costs can result in the refusal by the court to ratify the settlement. The lack of legislative clarification and the risk of funding a class action that is declared inadmissible by the court form important hurdles for an effective use of the Collective Redress Act.

Fraud on the Market Theory

Belgium does not recognize the fraud on the market theory.²³⁷

²³⁴ See Article 446ter of the Code of Civil Procedure.

²³⁵ Mathias Reimann, *Cost and Fee Allocation in Civil Procedure*, 84 (2012).

²³⁶ *Id.*

²³⁷ See *Warlop v. Lernout*, 05-Civ.-12058 (PBS)(D. Mass. Feb. 12, 2007) (in dismissing action and deeming Belgium an adequate forum, the court recognized that "[t]here are much more difficult hurdles for plaintiffs in Belgium, who do not have the class action mechanism or the ability to use a 'fraud on the market' theory to assist in recovery").



Jurisdiction and Pleading Standards

Jurisdiction: General

The civil court system in Belgium has courts of general jurisdiction and specialized courts including a Commercial Court. Under Article 573 of the Judicial Code, the Commercial Court hears disputes between parties to commercial transactions which do not fall under the general jurisdiction of the justice of the peace or under the power of the police courts. The Commercial Court has jurisdiction over any actions involving the purchase or sale of securities. The *Citibank Belgium* group action was commenced in the Commercial Court, as well as the group action instituted against Fortis, as a result of alleged misrepresentations in the Fortis-ABN AMRO transaction in 2008.

Jurisdiction: Collective Redress Act

The Collective Redress Act grants exclusive jurisdiction to the Brussels courts. Class actions have to be introduced either before the Court of First Instance, which is the court of general jurisdiction, or the Commercial Court, in accordance with the applicable provisions of the Judicial Code. The Constitutional Court has had to rule on the compliance of this exclusive jurisdiction with the Belgian Constitution, as class actions could possibly be introduced by German-speaking consumers, who are unable to conduct the legal proceedings in German before the Brussels court, taking into account the applicable language regulations. The Constitutional Court declared the appeal unfounded.²³⁸

Pleading Standards

With respect to causation, the Prospectus Act of 16 June 2006 provides a rebuttable presumption of a causal link between the absence of information or misleading or inaccurate information in a prospectus, and the damage incurred by investors when such absence or misleading or inaccurate information is likely to have a positive influence on the purchase price of the financial instrument or to create a positive feeling in the market.

²³⁸ Constitutional Court no. 137/2015, 1 October 2015.

Government Regulation

On April 1, 2011, Belgium implemented a new regulatory structure to supervise its financial system.²³⁹ Known as the “Twin Peaks model,” Belgium’s financial system is now regulated by two entities: the National Bank of Belgium and the Financial Services and Markets Authority (“FSMA”), formerly known as the CBFA (*Commissie voor het Bank, Financie- en Assurantiewezen/Commission Bancaire, Financière et des Assurances*). The FSMA is responsible for:

supervising the financial markets and listed companies, authorizing and supervising certain categories of financial institutions, overseeing compliance by financial intermediaries with codes of conduct and supervising the marketing of investment products to the general public, as well as for the ‘social supervision’ of supplementary pensions. The Belgian government has also tasked the FSMA with contributing to the financial education of savers and investors.²⁴⁰

Under Belgian law, listed companies must provide the markets with up-to-date information about the state of their affairs. Such information must be provided periodically in the annual or interim statements or, as a rule, without delay each time the company is aware of information of a sufficiently precise nature and which is likely to have a significant effect on the prices of its listed financial instruments. In addition, a prospectus must be published when securities are offered to the public or admitted to trading on a regulated market. The FSMA is responsible for the supervision of the compliance by issuers of these regulations.

²³⁹ See FSMA website available at <http://www.fsma.be/en/About%20FSMA/Powers.aspx>. (visited on May 10, 2016).

²⁴⁰ See <http://www.fsma.be/en/About%20FSMA/Powers.aspx>.



C. BRAZIL

Brazil is the largest securities market in Latin America, but investor recourse to individual damages is limited despite a number of possible mechanisms.

Brazil's Bolsa de Valores, Mercadorias & Futuros de São Paulo ("BM&F BOVESPA") is the largest securities exchange in Latin America. At the end of 2015, it had a market capitalization of \$624 billion.²⁴¹

Securities trading is regulated by the Comissão de Valores Mobiliários ("CVM"), which is the Brazilian equivalent of the United States Securities and Exchange Commission.

The responsibilities of the CVM are contained in two laws. Law 6.385/76²⁴² ("Brazilian Securities

Act") established the CVM and Law 6.404/76²⁴³ ("Corporation Law") governs the structure, organization and responsibilities of corporations. The CVM has the power to issue regulations and interpretive guidance consistent with Laws 6.385 and 6.404. CVM Instructions are regulations of general applicability in specific areas of responsibility. The concepts of financial fraud, price manipulation and other unfair trade practices are defined in CVM Instruction No. 8. The requirements of disclosure of material events are set out in Instruction 358. Sanctions applicable to such practices are set out in the Brazilian Securities Act.²⁴⁴

The practice of financial fraud price manipulation and other unfair trade practices may result

²⁴¹ BM&F BOVESPA, Annual Report 2015 (2016), available at http://ir.bmbovespa.com.br/enu/2737/RA2015_EN.PDF. (U.S. dollar value calculated as of May 2016.).

²⁴² Lei No. 6.385/76, de 7 de Dezembro de 1976, Diário Oficial da União de 7.12.1976, available at http://www.planalto.gov.br/ccivil_03/LEIS/L6385original.htm.

²⁴³ See Alexei Bonamin, Antonio Felix de Araujo Cintra, Fabiola Augusta Cavalcanti, Kenneth Antunes Ferreira, Rodrigo de Campos Vieira and Cláudio Coelho de Souza Timm, *Capital Markets 2016 – Brazil*, Latin Lawyer, (March 16, 2016), <http://latinlawyer.com/reference/topics/49/capital-markets>.



in administrative, civil or criminal sanctions, including fines of up to 50 percent of the consideration associated with the wrongdoing, or three times the economic advantage or loss derived from the illegal trading and imprisonment from one to eight years.²⁴⁵

Private rights to recover damages for securities fraud, however, are limited to individual actions, arbitration, class actions brought by regulators or associations, and new “repetitive action” procedures. Brazil’s New Code of Civil Procedure 2005 (NCPC) Law No. 13.105/15 went into effect on March 16, 2015.²⁴⁶ It creates a new process for the “resolution of repetitive actions.” The aim is to assure that lawsuits with the same subject matter receive identical solutions, thus providing uniformity and coherence to decisions. Precedent will now have to be followed by judges and parties, who must indicate the applicable precedents to the case at the moment of filing the lawsuit. The NCPC includes a special procedure that allows parties, judges, the public attorney and the public defender, among others, to request the Appellate Court to judge the legal controversy in the abstract, establishing its understanding about the legal issue, then applying it to other analogous cases.²⁴⁷ This proceeding commences with the selection of one or more of the pending lawsuits which represent the issue of law requiring a unanimous decision. After this selection, all other pending lawsuits involving the same issue of law will be suspended until the judge issues a decision in the representative case.²⁴⁸

While Brazil also has separate statutes creating collective actions, they do not allow individuals to bring claims. For example, the Public Civil Suit Law (Law No. 7.347/85) covers environmental protection matters, consumer goods issues, rights related to artistic, aesthetic, historical, tourism and landscaping,

²⁴⁵ *Id.*

²⁴⁶ Lei No. 13.105/15, de 16 de Marco de 2015, Diário Oficial da União de 16.3.2015, available at http://www.planalto.gov.br/ccivil_03/Ato2015-2018/2015/Lei/L13105.htm.

²⁴⁷ See Carlos Roberto Siqueira Castro & Daniela Soares Domingues, *Litigation 2016 – Brazil*, Latin Lawyer (November 6, 2016), <http://latinlawyer.com/reference/topics/60/litigation>.

²⁴⁸ See Fabio Ozi & Isabela Vidigal, *Brazil – Class and Group Actions 2016* ICLG, October 28, 2015, available at <http://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/brazil>.

infringement of the economic or urban order, and certain issues involving racial, ethnic or religious bias, as well as matters related to public property. The Consumer Protection Code (Law No. 8.078/90)²⁴⁹ permits class action lawsuits to solve matters related to collective but diffuse rights, collective rights in its strict sense, or individual but similar rights, as long as they do not involve a challenge to any taxation. Individual but similar rights are specific rights of individuals that stem from the same facts.²⁵⁰ The collective actions must be brought by a “legitimate party,” which includes the public prosecutor, regulators and consumer protection claims, but not individuals.²⁵¹

Basics of Filing a Claim and Litigation

Brazilian law offers the same judicial remedies to foreign entities as to Brazilian companies and citizens, such as injunctions, declaratory actions, collection procedures, actions for damages (compensation or indemnification) and actions for exhibition, among others. However, the NCPC requires a party who resides outside Brazil to post a bond, related to the payment of the legal costs and of the attorney’s fees of the other party.²⁵²

Private investors may file lawsuits to recover any losses they have suffered based on the general civil responsibility rules contained in the Brazilian Civil Code.²⁵³ But mandatory arbitration may be pushing out some investor suits from the courts. In 2001, Brazil amended its Corporate Law (Article 109) to allow companies to include mandatory arbitration clauses in their by-laws. Companies appear to be taking advantage of the law. For example, in 2002, Petrobras adopted just such a by-law.²⁵⁴ The by-law states that

²⁴⁹ Lei No. 8.078/90, de 11 de Setembro de 1990, Diário Oficial da União de 11.9.1990, available at http://www.planalto.gov.br/ccivil_03/Leis/L8078.htm.

²⁵⁰ See Ozi & Vidigal, *supra* note 241.

²⁵¹ A good analysis of the limitations of the Brazilian class action mechanism and history can be found in *Class Action Evolution, Improving the Litigation Climate in Brazil*, U.S. Chamber Institute for Legal Reform, August, 2014, available at http://www.instituteforlegalreform.com/uploads/sites/1/Brazil_v10.pdf.

²⁵² See Castro & Domingues, *supra* note 240.

²⁵³ See Bonamin, *supra* note 2374, at 1.

²⁵⁴ See *infra* Section IV.



“disputes . . . involving the Corporation, its shareholders, managers and members of the Audit Board regarding ‘the rules issued . . . by the Brazilian Securities and Exchange Commission . . . as well as in all further rules applicable to the operation of the capital market in general . . . shall be resolved according to the rules of the Market Arbitration Chamber.’” As a result, in the U.S. *Petrobras* ADR litigation, the court held that investors needed to arbitrate any claims for transactions in Brazil under Brazilian law.

In addition, some of the Brazilian exchange listings now require that companies adopt arbitration clauses for disputes with shareholders. While this may arguably conflict with the Brazilian constitutional right to seek legal recourse, or even Article 54 of the Consumer Protection Act, some commentators believe otherwise.²⁵⁵

Loser Pay Model

Brazil follows the loser pay model. The court may award between ten and twenty percent of the amount in controversy.²⁵⁶ There is no loser pays for class actions.²⁵⁷ Under the Brazilian Arbitration Act, the arbitrators have discretion to allocate costs and fees between the parties. However, the parties may also agree as part of the preliminary negotiations at the commencement of arbitration) to waive any “loser pays” provisions.²⁵⁸

Opt-In vs. Opt-Out

Brazilian collective actions are neither opt-in nor opt-out. In general, the effects of decisions in class action suits will apply to all members of a class or

²⁵⁵ Baker & McKenzie, The Baker & McKenzie International Arbitration Yearbook 389-392 (1999), available at https://books.google.com/books?id=ISblXalfLzcC&pg=PA389&lpg=PA389&dq=Article+109+of+the+Brazilian+Corporate+Law&source=bl&ots=zO_u_tQnA&sig=c83MSuUjejNa4Fr8A9E3yV4neCw&hl=en&sa=X&ved=0ahUKEwjh6YD-6vb_MAhVR_mMKHeNHCh8Q6AEIIzAB#v=onepage&q=Article%20109%20of%20the%20Brazilian%20Corporate%20Law&f=false.

²⁵⁶ See Castro & Domingues, *supra* note 240.

²⁵⁷ Lei No. 8.078/90, *supra* note 242, Art. 87.

²⁵⁸ See <http://www.iclg.co.uk/practice-areas/international-arbitration-international-arbitration-2015/brazil - para 13.3>.

group as long as they are beneficial to them.²⁵⁹ There is however an opt-in and opt-out procedure for pre-existing individual cases.²⁶⁰

Extraterritorial Jurisdiction

Whether or not Brazilian laws can extend to acts outside of Brazil is a complicated question and attorneys opining on the subject cannot yet provide a consensus.

Generally, Brazilian courts can exercise jurisdiction extraterritorially whenever the defendant is domiciled in Brazil, the obligation is performed in Brazil, or the cause of action is based on a fact that occurred in Brazil.²⁶¹

The Brazilian Criminal Code also provides for the extraterritorial application of Brazilian law with regard to crimes committed against the property or legal authority of the Union, Federal District, States, Territories or Municipalities, state-owned companies, mixed-economy companies, government entities or state-controlled foundations. The Administrative Misconduct Law applies to any individual, resident in Brazil or not, who induces, assists in, or is involved in any of the acts proscribed by the law.²⁶²

The U.S. *Petrobras* litigation provides topical application of these principles. Professor Paulo Borba Casella (on the behalf of defendant Petrobras) opined that plaintiffs may not pursue claims under the Brazilian Statutes for Petrobras securities (ADRs) registered and offered in the United States because under Brazilian choice-of-law principles, the laws of the United States and/or its constituent states, not Brazilian law, would govern. Brazil’s choice-of-law rule, set forth in Article 9 of *Lei de Introdução às Normas de Direito Brasileiro* (Law on the Introduction to Norms of Brazilian Law) (“Article 9”), reflects the policy of Brazil to look to the facts of each transaction and to defer to the laws of the

²⁵⁹ See Ozi & Vidigal, *supra* note 241.

²⁶⁰ Lei No. 8.078/90, *supra* note 242, Art. 103.

²⁶¹ Lei No. 13.105/15, *supra* note 239, Art. 21.

²⁶² See Adriana Dantas, Barbosa Müssnich & Aragão, *Anti-Corruption 2016 –Brazil*, Latin Lawyer, October 14, 2015, available at <http://latinlawyer.com/reference/topics/74/jurisdictions/6/brazil>.



place where obligations are constituted, whether it be Brazil or a foreign country.²⁶³

Similarly, Professor Luiz Leonardo Cantidiano (also on behalf of Petrobras) opined that plaintiffs may not pursue claims under the CVM Regulations because they do not apply to securities registered and offered for sale outside of Brazil.²⁶⁴

Funding the Litigation- Contingent Fee Arrangements

The Brazilian Bar association allows contingent fees. There are no specific provisions relating to third party funding.²⁶⁵

Pleading Standards

A party is required to submit all fact arguments and supporting evidence with the initial pleading.²⁶⁶

Causes of Action in Securities Litigation

Brazilian Corporate Law (Article 159 paragraph 7) provides that shareholders directly harmed by acts of officers and board members have the right of legal action against them.²⁶⁷ Also, the Brazilian Civil Code (Article 927) states that anyone who causes damages to others by committing illicit acts, is liable for damages to the aggrieved party. Such liability shall be limited to the extent of the damages suffered (Article 944).²⁶⁸

²⁶³ Expert Report of Paulo Borba Casella, *In re Petrobras Secs. Litig.*, No. 14-cv-9662 (S.D.N.Y. Aug. 21, 2015), ECF No. 198-4.

²⁶⁴ Expert Report of Luiz Leonardo Cantidiano (“Cantidiano Report”), *In re Petrobras Secs. Litig.*, No. 14-cv-9662 (S.D.N.Y. Aug. 21, 2015), ECF No. 198-2.

²⁶⁵ Rogério Carmona Bianco, Fábio Peixinho Gomes Corrêa & Maria Beatriz Rizzo, *Litigation and Enforcement in Brazil: Overview*, Practical Law, August 1, 2015, available at <http://us.practicallaw.com/9-502-2479>; Octávio Aronis, *Litigation in Brazil – The Difficulties and Alternatives*, Stellar Risk Report and Journal, <http://www.stellarisk.com/litigation-in-brazil-the-difficulties-alternatives/> (last accessed May 5, 2015).

²⁶⁶ See Castro & Domingues, *supra* note 240.

²⁶⁷ Lei No. 6.404/76, *supra* note 236. Links to most Brazilian laws regulating public corporations can be found on the website of the CVM at http://www.cvm.gov.br/subportal_ingles/menu/investors/regulation.html. The English version of the Brazilian Corporation Act is available at http://www.cvm.gov.br/export/sites/cvm/subportal_ingles/menu/investors/anexos/Law-6.404-ing.pdf.

²⁶⁸ Lei No. 10.406/02, de 10 de Janeiro de 2002, Diário Oficial da União de 10.1.2002, available at http://www.planalto.gov.br/ccivil_03/Leis/2002/L10406.htm.

Article 26 Paragraph 2 of the Brazilian Securities Act (Law 6.385/76) provides that independent auditors or auditing firms shall be subject to civil liability for any losses caused to third parties as a result of negligence or fault (scienter) in the exercise of the functions provided for in this article.²⁶⁹

In the ongoing U.S. *Petrobras* litigation, the plaintiffs identified several possible causes of action under Brazilian law, including:

1. Violations for duties owed to shareholders under Brazilian Corporate Law Article 158, (Law 6.404/76). Article 158 provides that officers and directors are civilly liable to shareholders for damages caused to the corporation by virtue of negligence or willful misconduct, even within their powers; and for actions carried out beyond their authority, that is, exceeding the powers granted to them, or contrary to the provisions of the law or the company's by-laws.
2. Violations of the Brazilian Securities and Exchange Commission (“Comissão de Valores Mobiliários or “CVM”) Instructions No. 358/02, which regulates the duties to report material acts and facts.²⁷⁰
3. General Tort, Violation of Good Faith and Customs and Negligence. Claims based on Article 186, 187 and 927 of the Brazilian Civil Code which provides that anyone, by action or voluntary omission, negligence or imprudence, violates rights and causes damages to others, even though exclusively moral, commits an illicit act and has an obligation to indemnify.²⁷¹
4. Auditor Negligence. Claims based on Brazilian Securities Act (Law 6.385/76), Article 26 provides that only audit firms or independent auditors which are registered with CVM may audit the financial statements of publicly held corporations

²⁶⁹ Lei No. 6.385/76, *supra* note 235.

²⁷⁰ Regulations of Interest to Foreign Investors, CVM Instructions 358 (January 3, 2002), available at http://www.cvm.gov.br/export/sites/cvm/subportal_ingles/menu/investors/anexos/CVM-Instruction-358.pdf.

²⁷¹ Lei No. 10.406/02, *supra* note 261.



and institutions, companies or corporations which compose the securities distribution and intermediation system.

In *Petrobras*, Professor Luiz Leonardo Cantidiano provided an expert opinion stating that the Brazilian Civil Code causes of action were superseded by the Corporate Law. He also opined that the Brazilian Corporate Law causes of action were infirm because Brazilian law only recognizes “effective” losses – meaning that the securities had to have been sold; his opinions were uncontested and did not cite to any authority other than his personal view of the text.²⁷² With Brazil’s NCPC requiring adherence to precedent, interpretation of Brazilian law should become more reliable.

(directors and executives) of public companies can be brought by minority shareholders, similar to U.S.-style derivative lawsuits. However, the effectiveness of these lawsuits is impaired by the fact that they must be approved by the shareholders meeting (not the board as in the U.S.). Controlling shareholders are thus able to block such actions. As a result, lawsuits against directors are rare. Moreover, injured investors can file a complaint before the BSM Bovespa Investor Compensation Mechanism (MCR) for compensation of losses suffered as a result of actions or omissions of market intermediaries in connection with a Bovespa security. The maximum compensation is 70,000BR. The IMF concluded that the availability of private litigation options in Brazil could be improved.²⁷⁴

Regulatory Environment for Securities Litigation

Securities litigation in Brazil appears to be nearly non-existent, and the enforcement capabilities of the regulators have been criticized. Moreover, arbitration provisions in corporate by-laws may make it impossible to institute litigation in court. Although corporate bylaws may make it impossible for an investor to commence litigation in the Brazilian courts, arbitration may allow investors to seek a more expedient resolution. Arbitration may also allow investors the opportunity to more adequately control costs (e.g. parties can agree to waive “loser pays” provisions) and to have input regarding the appointment of the arbitrators, evidentiary rules, etc.²⁷³

According to the June 013 IMF Financial Sector Assessment Program for Brazil conducted by the former Secretary of the U.S. SEC, Jonathan Katz, the CVM is underfunded and does not have adequate control over allocation of its budget; and there is an important gap in regulatory authority for investor protection and secondary market trading in government securities. While the CVM can require a violator to recompense defrauded persons as a condition to a negotiated settlement, it cannot impose this requirement in a litigated action. Private lawsuits against administrators

²⁷² Cantidiano Report, *supra* note 257.

²⁷³ See <http://www.iclgs.co.uk/practice-areas/international-arbitration/international-arbitration-2015/brazil>.

²⁷⁴ International Monetary Fund, Financial Sector Assessment Program – Brazil, IOSCO Objectives and Principles of Securities Regulation, Detailed Assessment of the Implementation, (June, 2013), available at <https://openknowledge.worldbank.org/bitstream/handle/10986/15973/807280ESW0Braz00Box379814B00Public0.pdf?sequence=1&isAllowed=y>.



D. CANADA

Securities Class Actions Exist In Many Canadian Provinces

Canada has no nationwide securities class action system akin to the federal securities laws in the United States. In Canada, matters involving securities relate to “property and civil rights within the province,” and are thus governed by the legislature of each province and territory.²⁷⁵ The superior courts in each province and territory have inherent and general jurisdiction to deal with securities claims for their jurisdictions.²⁷⁶ Similarly, each province and territory has jurisdiction to establish procedures for class proceedings.

Canadian securities class actions really developed in the aftermath of a series of high-profile frauds carried out by publicly-traded companies in the 1990s.²⁷⁷ After these events, Ontario became the

first province to adopt a new civil liability regime for secondary market purchases in its securities laws, and it was also one of the first²⁷⁸ to enact class action legislation, the Class Proceedings Act (“CPA”).²⁷⁹

available to investors lacking and recommended the creation of a statutory civil liability system to help investors sue issuers, directors and officers who violated their statutory disclosure obligations. *See Canadian Imperial Bank of Commerce v. Green (CIBC v. Green)*, 2015 SCC 60, [2015] 3 S.C.R. 801, paras. 63-65 (Can.); *Theratechnologies Inc. v. 121851 Canada Inc.*, 2015 SCC 18, [2015] 2 S.C.R. 106, paras. 29-31 (Can.). These recommendations were then adopted by the Canadian Securities Administrators, an umbrella organization of Canada’s provincial and territorial securities regulators. 2015 SCC 18, para. 30. Since then various provinces have enacted laws to implement certain of these recommendations.

²⁷⁵ See *Reference re Securities Act*, 2011 SCC 66, [2011] 3 S.C.R. 837 (Can.).

²⁷⁶ The Federal Court in Canada is a statutory court and its jurisdiction is limited generally by the *Federal Court Act* and other federal legislation that confers jurisdiction on that court. Generally, the Federal Court deals with such matters as claims against the Government of Canada, intellectual property, maritime and admiralty claims and national security.

²⁷⁷ Following these incidents, the Toronto Stock Exchange created the Allen Committee to examine the disclosure rules governing secondary market purchases. The Committee found the remedies

²⁷⁸ Quebec has had representative actions since 1978.

²⁷⁹ 1992, S.O. 1992, c. 6. By way of background, the Ontario class action mechanism is similar to that in the U.S. with several important differences, including that: (i) there is no typicality requirement so the representative plaintiff need not have claims against all defendants; (ii) an Ontario court does not consider the merits when assessing whether to certify a class; and (ii) there is no requirement that common questions predominate over individual questions (it is sufficient if there are common questions that can be resolved through a class action). Other important procedural differences in securities class actions are that (i) there is no right to a jury trial in Canada; and (ii) formal discovery is still far more limited in Ontario than in the U.S.



Since then, most provinces have enacted similar civil liability laws for securities fraud and all but one province has adopted a class action statute.²⁸⁰ The confluence of the enactment of both a statute for secondary market purchases and procedures governing class actions triggered a burgeoning of securities litigation in Canada.²⁸¹

With the exception of British Columbia, provincial class action statutes provide for opt-out classes, thus operating similarly to U.S. class actions.²⁸² Moreover, as discussed below, these often involve global classes. Accordingly, U.S. pension funds should ensure that, where eligible, they are submitting proofs of claims in Canadian class actions.

Securities class actions are filed primarily in Ontario, British Columbia, Quebec²⁸³, Alberta and

²⁸⁰ (British Columbia) Class Proceedings Act (“CPA”), R.S.B.C. 1996, c 50; (Saskatchewan) The Class Actions Act (“CAA”), S.S. 2001, c C-12.01; (Newfoundland and Labrador) CAA, S.N.L. 2001, c C-18-1; (Manitoba) CPA, C.C.S.M., c C130; (Alberta) CPA, S.A., c C-16.5; (New Brunswick) CPA R.S.N.B. 2011, c 125; (Nova Scotia) CPA S.N.S. 2007, c 28; (Quebec) An Act Respecting the Fonds d'aide aux actions collectives, C.Q.L.R., c F-3.2.0.1.1, Code of Civil Procedure, C.Q.L.R. c C-25.01, arts. 571-604.

²⁸¹ NERA Economic Consulting reports that, as of the end of 2015, it had identified 129 cases that have been filed in Canada since 1997, more than half of which were filed since 2009. See Bradley A. Heys and Mark L. Berenblut, *Trends in Canadian Securities Class Actions: 2015 Update, Are We In Bear Territory?*, NERA Economic Consulting (Feb. 5, 2016) (“NERA 2015”), at 3, http://www.nera.com/content/dam/nera/publications/2016/2015_Recent_Trends_Canada.pdf.

²⁸² Prince Edward Island (“PEI”) does not have any class action statute. Although there is no legislation regarding class actions in PEI, the courts may have jurisdiction to certify class actions under existing rules of practice related to representative proceedings. In British Columbia, class actions operate on an opt-out basis for B.C. residents and an opt-in basis for non-residents. (British Columbia) CPA, R.S.B.C. 1996, c 50, ss. 6, 16.

²⁸³ Unlike the rest of Canada, in Quebec, civil matters are based on the French civil law, not the English common law. Much of the laws governing civil issues are found in the Quebec Civil Code and Code of Civil Procedure. In January 2016, a newly revised Code of Civil Procedure went into effect, which included important changes to Quebec class action procedures. See Code of Civil Procedure, CQLR c. C-25.01, arts. 571-604. Moreover, it should be noted that Quebec’s test for certifying a class actions appears to be less rigorous than the test in other provinces. See, e.g., *Vivendi Canada Inc. v. Dell’Aniello*, 2014 SCC 1, [2014] 1 SCR 3, para. 57 (Can.) (“[T]he Quebec approach to authorization [of a class

Saskatchewan).²⁸⁴ However, Ontario is, by far, the most active jurisdiction.²⁸⁵ This is not surprising since it was the first to implement these statutory civil liability provisions and the main stock exchange, the Toronto Stock Exchange (the “TSX”), is located in Ontario.²⁸⁶

Claims Under Ontario Law

Common Law

Ontario has long recognized common law remedies stemming from the disclosure of misleading information, including misrepresentations made in connection with open market purchases.²⁸⁷ However, as the Allen Committee concluded, the “common law remedies available to aggrieved investors for misleading disclosure in secondary trading markets were so onerous that they were ‘as a practical matter largely academic.’”²⁸⁸ Most notably, courts hold that reliance cannot be presumed on a class-wide basis.²⁸⁹ Today, common law claims are still prosecuted, and Ontario courts will certify class actions for fraud in connection with open market purchases when such claims are coupled with the statutory claims discussed below. But, the common law claims are typically certified for common issues of liability only, with each investors’ reliance being subject to individual proof.²⁹⁰

action] is more flexible than the one taken in the common law provinces, ...”).

²⁸⁴ See, e.g., NERA 2015 at 5; Bradley A. Heys, Mark L. Berenblut and Jacob Dwhyte, *Trends in Canadian Securities Class Actions: 2014 Update*, NERA Economic Consulting (Feb. 10, 2015) (“NERA 2014”), at 4, http://www.nera.com/content/dam/nera/publications/2015/PUB_Recent_Trends_Canada_0115.pdf.

²⁸⁵ *Id.*

²⁸⁶ The major equity exchange in Canada is the Toronto Stock Exchange. The other exchanges include (i) Montreal Exchange – an options exchange (co-owner of the Boston Options Exchange); (ii) ICE Futures Canada – the Winnipeg Commodity Exchange; (iii) Nasdaq Canada; (iv) CNQ – Canada’s newest stock exchange for trading equities of emerging companies; and (v) NGX – the natural gas exchange. See <http://www.world-stock-exchanges.net/canada.html>; http://www.osc.gov.on.ca/en/Marketplaces_cnsx_index.htm.

²⁸⁷ See *CIBC v. Green*, 2015 SCC 60, para. 128.

²⁸⁸ *Id.* at para. 64.

²⁸⁹ *Abdula v. Canadian Solar, Inc.*, 2015 ONSC 53, paras. 26-27 (Can. Ont. Sup. Ct. J.).

²⁹⁰ See, e.g., *CIBC v. Green*, 2015 SCC 60, para. 128; *Abdula v. Canadian Solar, Inc.*, 2015 ONSC 53, paras. 26-27, 61-63, 66.



Statutory Liability for Primary and Open Market Purchases

The Ontario Securities Act (“OSA”), has long provided a claim for *primary* market purchases—*e.g.*, purchases made in public offerings.²⁹¹ However, it was only in recognition of the concerns outlined by the Allen Committee that, in 2005, the Ontario legislature provided a statutory claim for secondary market (a.k.a. open market) purchases (“Secondary Liability Provisions”).²⁹² Specifically, Section 138.3 creates a “statutory cause of action [for a misrepresentation made in a document or oral statement] for the benefit of those who acquired or disposed of a responsible issuer’s securities between the time a document containing a misrepresentation is released by the responsible issuer and the time of its correction.”²⁹³ Importantly, the statute expressly states that plaintiffs need not prove reliance on the misrepresentation.²⁹⁴

Whereas the Exchange Act requires that the plaintiff prove “scienter” to obtain damages for open market purchases, the OSA generally does not require scienter for misrepresentations *made in core documents* (such as annual or interim financial statements).²⁹⁵ It merely provides for a due diligence defense. Another notable distinction is that the Ontario law caps each defendants’ liability unless they acted with scienter—with the caps varying depending on the role of the particular defendant.²⁹⁶ For example, an issuer’s potential liability in a secondary market fraud case (*i.e.*, a § 10(b) open market type case) is capped at the greater of \$1 million or 5% of the issuer’s market

²⁹¹ R.S.O. 1990, c. S.5 (Can.).

²⁹² As the Ontario Court of Appeals recently held, this claim was “intended to be remedial legislation with the twin goals of a) facilitating and enhancing access to justice for investors, and b) deterring corporate misconduct and negligence.” *Green v. Canadian Imperial Bank of Commerce*, 2014 ONCA 90, [2014] 118 O.R. 3d 641, para. 36 (Can. Ont. C.A.). Since its enactment, at least 68 Statutory Secondary Market cases have been filed. NERA 2015 at 2. Of these 68 cases, by the end of 2015, 33 remained unresolved and 30 have settled for \$463 million. *See id.*

²⁹³ *Goldsmith v. National Bank of Canada*, 2016 ONCA 22, para. 8 (Can. Ont. C.A.).

²⁹⁴ *CIBC v. Green*, 2015 SCC 60, para. 11; s. 138.3(3).

²⁹⁵ R.S.O. 1990, c. S.5, ss. 138.1 & 138.4.

²⁹⁶ *Id.* at ss. 138.1 & 138.7.

capitalization.²⁹⁷ In its 2015 Report, NERA states that “[a]lmost all settlements in Statutory Secondary Market Cases to date appear to have been less than the damage limit for issuers set out in the provincial securities acts.”²⁹⁸ Settlements involving smaller companies, however, have “tended to be closer to the statutory damage limit than have settlements involving larger companies.”²⁹⁹

One hallmark of this secondary market statute is that the legislature requires that investors seek leave of the court to bring these claims.³⁰⁰ This statutory claim supplements the common law rather than replaces it.³⁰¹

Since the secondary market claim is still in its infancy, there are numerous disputes regarding its application. In the past few years, Canadian appellate courts have clarified three such disputes.

First, a main area of dispute has been the question of what is required for “leave” to bring a statutory securities fraud claim. The Canadian Supreme Court has addressed this question in two recent cases and has, arguably, raised the evidentiary threshold for plaintiffs to obtain leave to file claims under the Secondary Liability Provisions of the OSA.

In the first case, the Canadian Supreme Court addressed the same leave provision under the Quebec law, which provides that the court should grant leave to file the statutory claims “if it deems that the action is in good faith and there is a reasonable possibility that it will be resolved in favour of the plaintiff.”³⁰² The Supreme Court held that a “reasonable possibility” of success “requires the claimant to offer both a plausible analysis of the applicable legislative provisions, and some credible evidence in support of the claim.”³⁰³ The

²⁹⁷ *Id.* at s. 138.1.

²⁹⁸ NERA 2015 at 9.

²⁹⁹ *Id.* at 10.

³⁰⁰ R.S.O. 1990, c. S.5, s. 138.8(1). This provision reads: “No action may be commenced under section 138.3 without leave of the court granted upon motion with notice to each defendant. The court shall grant leave only where it is satisfied that, (a) the action is being brought in good faith; and (b) there is a reasonable possibility that the action will be resolved at trial in favour of the plaintiff.”

³⁰¹ *Abdula v. Canadian Solar, Inc.*, 2015 ONSC 53, paras. 41, 44.

³⁰² Securities Act, CQLR, c. V-1.1, s. 225.4.

³⁰³ *Theratechnologies*, 2015 SC 18, para. 39.



Supreme Court warned, however, that:

The authorization stage ... should not be treated as a mini-trial. A full analysis of the evidence is unnecessary. If the goal of the screening mechanism is to prevent costly strike suits and litigation with little chance of success, it follows that the evidentiary requirements should not be so onerous as to essentially replicate the demands of a trial.... What *is* required is sufficient evidence to persuade the court that there is a reasonable possibility that the action will be resolved in the claimants' favor.³⁰⁴

Since then, the Supreme Court has confirmed that this same threshold test applies to a leave motion under Section 138.8 of the OSA.³⁰⁵

The lower courts are interpreting the rule as very stringent and denying leave motions. Recently, in *Goldsmith v. National Bank of Canada*, the Ontario Court of Appeal upheld an order denying leave, holding that there must be a “more stringent” evaluation and that courts must scrutinize the competing evidence.³⁰⁶ On March 31, 2016, in *Bradley v. Eastern Platinum Ltd.*,³⁰⁷ the superior court reaffirmed the position that the test for statutory leave to bring a secondary market securities class action “is not a low bar.”³⁰⁸ While the statute provides a mechanism by which plaintiffs are entitled to limited discovery, there appears to be much concern in the investor community that the Ontario courts are allowing defendants to constrain the limited discovery to evidence helpful to their cause.

³⁰⁴ *Id.*

³⁰⁵ *CIBC v. Green*, 2015 SCC 60, para. 122.

³⁰⁶ 2016 ONCA 22, para. 34 (to obtain leave, one must “offer both a plausible interpretation of the applicable legislative provisions and credible evidence sufficient to convince the court that there is a reasonable possibility that the action will be resolved at trial in the claimant’s favor”).

³⁰⁷ 2016 ONSC 1903 (2016).

³⁰⁸ See, e.g., *Coffin v. Atlantic Power Corp.*, 2015 ONSC 3686 (Can. Ont. Sup. Ct. J.) (denying leave based on affidavits submitted by defendants).

Second, courts have opined on whether underwriting investment banks may be held liable for misleading secondary market disclosures. Section 138.3(1) enumerates certain actors that can be held liable for misleading disclosures pursuant to these Secondary Liability Provisions. While underwriters are not enumerated, investors have argued that underwriters are liable as either “experts” or “promoters,” both of which are enumerated. However, two courts have recently rejected these efforts to hold underwriters liable for secondary market purchases. In *LBP Holdings v. Allied Nevada Gold Corp.*, the Superior Court of Ontario held that the term “expert” in section 138.3(1) is not intended to include underwriters.³⁰⁹ Moreover, in *Goldsmith v. National Bank of Canada*, the Court of Appeal held that the underwriters were not “promoters.” While that Court left open the possibility that an underwriter could be a “promoter,” it held that the investment banker must be something more than a professional adviser – it must have knowingly influenced the release of the misleading information.

Third, in 2015, the Canadian Supreme Court issued its much anticipated ruling regarding the statute of limitations for seeking leave to bring a secondary market claim under Section 138.1 of the OSA.³¹⁰ Under Section 138.8 of the OSA, a secondary market claim may be *commenced only with leave* of the court and within the three-year limitation period set forth in Section 138.14, which provides that claims are time-barred three years after the date of the alleged misrepresentation. Lower courts were, however, divided about whether this limitation period was tolled by the *filing* of an action notifying defendants of the *intent to seek leave* pursuant to Section 28 of the CPA. Section 28 provides that “a cause of action asserted in a class proceeding” suspends the limitations period.³¹¹ Thus, the practical question was ultimately whether a plaintiff had to actually seek and be granted leave to file the statutory claim prior to the end of the limitations period, or whether filing the action and notifying defendants of the intent to seek leave was enough.

³⁰⁹ 2016 ONSC 1629, para. 63 (Can. Ont. Sup. Ct. J.).

³¹⁰ See *CIBC v. Green*, 2015 SCC 60 (answering the question raised in a trilogy of Ontario court of appeal decisions).

³¹¹ S.O. 1992, c 6, s. 28 (emphasis added).



In a trilogy of cases (the “*Green Trilogy*”), the Ontario Court of Appeal held that pleading a statutory claim under Section 138.3 was sufficient to trigger the suspension of the limitation even though leave had not yet been granted. After this opinion, the Ontario legislature added Section 138.14(2) to the OSA, specifying that the limitation period is suspended from the date of the filing of a notice of motion for leave under Section 138.8. This new rule applies to newly-filed cases.

Because Section 138.14(2) did not have retroactive effect, the Canadian Supreme Court issued a ruling to address the interplay between the tolling provision and the leave requirement for the *Green Trilogy* of cases. Although the Court was deeply divided, a majority held that Section 28 of the CPA operates to suspend the limitation in Section 138.3 of the OSA only after leave has been actually granted. However, the Court held that courts have the inherent jurisdiction to issue orders *nunc pro tunc* to allow plaintiffs to proceed with an action where leave is sought—but not granted—prior to the expiration of the limitation period.³¹²

Carriage Motions—Canadian Lead Plaintiff/Lead Counsel Motions

The decision about who should lead a class action is evaluated quite differently in Canada. Unlike the U.S., there is no uniform test for determining who should be the lead plaintiff and lead counsel in Ontario. Notably, Ontario courts apply no presumption in favor of appointing the investor with the largest losses as lead plaintiff. Ontario courts entertain fulsome motions, called “carriage motions,” when multiple class actions are filed on the same matter. Based on these motions, courts analyze many factors to determine which plaintiff, as well as which law firm, should be appointed as the representative plaintiff and class counsel, respectively.³¹³

Over the years, different judges have engaged in different analyses. In the *Sino-Forest* case, the court engaged in an extensive merits-based analysis and considered the characteristics of the plaintiffs and how each firm alleged its complaint. Specifically, the court considered the definition of class membership, the theory of the case, the causes of action, joinder of defendants and prospects of certification to assess which firm’s theory it preferred. The size of the plaintiffs’ losses was considered but the court clearly did not view the fact that one shareholder had the largest loss necessarily as dispositive. While the court did think appointing institutional investors as lead plaintiffs could be beneficial, it favored a group that included both institutional investors and individuals. As time progresses, the number of cases involving competing carriage motions have increased.

Extra-Territorial Reach of Ontario’s Statute

In Canada, plaintiffs often bring securities fraud claims on behalf of a global class of investors including domestic or foreign investors who purchased securities on either its domestic exchanges or even on foreign exchanges. Canadian courts have certified such classes, and cases have been settled on this basis.³¹⁴

Global Classes Are Allowed

Several reported opinions address the extraterritorial scope of the OSA, and Ontario courts seem to broadly interpret the territorial application of Ontario law. In particular, based on the language of the OSA, Ontario courts have adopted a test that considers whether there are substantial connections to Ontario as opposed to a *Morrison*-style test that focuses on the exchange where the securities were purchased.³¹⁵ Accordingly, Canadian firms file cases even where the issuer does not trade securities in Ontario. Rather, they focus on cases whether the company in question

³¹² See, e.g., *Abdula v. Canadian Solar, Inc.*, 2015 ONSC 53, paras. 59-60.

³¹³ See, e.g., *Smith v. Sino-Forest Corp.*, 2012 ONSC 24 (Can. Ont. Sup. Ct. J.) (a recent ruling on a carriage motion by an Ontario court considering applications by both Canadian and U.S. institutional and individual movants).

³¹⁴ See, e.g., *Abdula v. Canadian Solar Inc.*, 2011 ONSC 5105 (Can. Ont. Sup. Ct. J.) (holding that the Ontario Securities Act applies to a company that chooses to be incorporated in Canada, has its principal office in Ontario, and carries on business in Ontario), affirmed on appeal, 2012 ONCA 211, [2012] O.R. 3d 256 (Can. Ont. C.A.).



has a significant tie to Canada. In fact, they have filed cases where the company in question is not even listed on a Canadian exchange but is effectively a Canadian company.³¹⁶ One such example involved Canadian Solar Inc., a company registered in Canada but operated in China, whose shares traded only on the NASDAQ.³¹⁷

Recently, the Court of Appeal of Ontario addressed the extraterritoriality of the Securities Act in the securities class action against B.P. plc, which concerned alleged misrepresentations related to the Deepwater Horizon oil spill disaster in the United States. Defendants argued that the Securities Act should not apply because BP, a UK corporation headquartered in London, does not own property in Canada, does not conduct business in Canada and its stock does not trade on any Canadian exchange. However, the Court of Appeal upheld the lower court's ruling that the Securities Act claims could be pursued in connection with shares purchased on foreign exchanges because it was a "reporting issuer" for a short period when its ADS traded on the TSX and, afterwards, BP continued to send relevant investor documents to its shareholders in Canada.³¹⁸ In an interesting turn, despite this ruling, the Court of Appeal ultimately dismissed the BP case on *forum non conveniens* grounds.

U.S./Canada Cross-Border Issues

In many instances, similar class actions against the same defendants are litigated simultaneously in the U.S. and Canada. According to NERA, "of the 68 Statutory Secondary Market cases brought to date, 29 (43%) have also involved parallel U.S. class actions."³¹⁹ NERA also reports that, since 2006, approximately half of all U.S. filings against Canadian companies have seen a corresponding parallel claim in Canada.³²⁰

³¹⁶ Since there are few examples where Canadian companies do not trade on a Canadian exchange, this is not likely to occur frequently.

³¹⁷ See *Abdula v. Canadian Solar, Inc.*, 2011 ONSC 5105.

³¹⁸ *Kaynes v. BP plc*, 2014 ONCA 580, [2014] 122 O.R. 3d 162 (Can. Ont. C.A.). There, plaintiffs defined the proposed class to encompass only Canadian investors. Plaintiffs also chose to expressly exclude all investors who purchased on the NYSE and to not exclude themselves from the U.S. BP class action.

³¹⁹ NERA 2015 at 5.

³²⁰ *Id.*

One key issue stemming from these parallel cross-border actions is how to handle class definitions that overlap between the Canadian and U.S. class actions. While Canadian attorneys have often limited their cases to exclude class members covered by U.S. cases, that is not always the case. In practice, at the settlement stage, U.S. and Canadian law firms often have cooperated to avoid problems with settling a case on behalf of a class that may include residents of the other country. However, problems can arise when there is a lack of cooperation. For example, in one case, the U.S. court approved a settlement of a class action involving Canadian residents but the Canadian court refused to enforce the U.S. class action judgment on grounds that the U.S. court failed to meet the due process and procedural fairness requirements for notice to absent class members.³²¹

Another important example of conflicts between Canadian and U.S. class actions is the *IMAX Corporation* litigation, which involved significant cross-border disputes spanning over six years. In the Ontario class action, the Ontario Superior Court initially certified a global class in 2009, which included all persons who purchased on either the TSX or the NASDAQ.³²² Because approximately 85% of the securities traded on NASDAQ, the Ontario judge was fully aware that this decision might later give rise to a "day of reckoning" if a settlement were reached in the related U.S. class action. When the U.S. class action later settled for \$12 million on behalf of investors who purchased shares on the NASDAQ, Canadian counsel intervened to object to the scope of the release.³²³ The U.S. settlement notice described how the "day of reckoning" had arrived, and told investors that they must choose whether to participate in the U.S. settlement and waive their rights in the Canadian class action, or opt out of the U.S. settlement. The U.S. settlement was conditioned on an order from the Ontario court excluding from the

³²¹ See, e.g., *Currie v. McDonald's Restaurants of Canada Ltd.* (2005), 74 O.R. 3d 321, [2005] O.J. No. 506 (QL) (Can. Ont. C.A.).

³²² *Silver v. Imax Corp.*, 2009 CanLII 72334 (Can. Ont. Sup. Ct. J.); *Silver v. Imax Corp.*, 2009 CanLII 72342 (Can. Ont. Sup. Ct. J.).

³²³ See *In re IMAX Corp. Sec. Litig.*, No. 1:06-cv-6128 (NRB) (S.D.N.Y.).



definition of the Canadian case all investors who did not opt out of the U.S. settlement. Concluding that the U.S. court had jurisdiction to approve the U.S. settlement and that the notice issued to investors was fair, the Ontario court acquiesced and amended its certification order to exclude from the definition of the Canadian class all persons who did not opt out of the U.S. settlement.³²⁴ Ontario counsel appealed, arguing, among other things, that a determination of the issues in Ontario would result in a far more substantial award for the class, but the appeal was denied.³²⁵

Because of potential difficulties arising from cases on both sides of the border, there have been some efforts to set up class action protocols for cross-border class actions.³²⁶ On August 14, 2011, the Council of the Canadian Bar Association: (i) approved as best practices the Canadian Judicial Protocol for the management of Multi-Jurisdictional Class Actions; and (ii) endorsed the ABA “Protocol on Court-to-Court Communications in Canada – U.S. Cross-Border Class Actions” and “Notice Protocol: Coordinating Notice(s) to the class(es) in Multijurisdictional Proceedings.” On August 8-9, 2011, the American Bar Association issued a resolution adopting as best practices the *Protocol on Court-to-Court Communications in Canada-U.S. Cross-Border Class Actions* and *Notice Protocol: Coordinating Notice(s) to the Class(es) in Multijurisdictional Class Proceedings* (together, the “Protocols”).

With respect to Canada-U.S. cross-border cases, the Protocols provide: (i) standardized mechanisms to notify counsel, parties and the courts of overlapping actions, and to conduct settlement proceedings with the goal of ensuring that notice to class members is provided in a meaningful way that will be understood by all affected persons in the differing jurisdictions

(the “Notice Protocol”); and (ii) that courts should communicate with other courts where there is commonality among substantive or procedural issues (a “Communication Protocol”). The purported objective of the Protocols is to ensure that U.S.-Canada cross-border class actions be prosecuted in a coordinated and efficient manner. However, the Protocols are non-binding. Before a court applies the Protocols (with or without modifications), counsel must be given notice and an opportunity to be heard regarding what sections of the protocol to apply.

Provincial Cross-Border Issues

While most Canadian cases are filed in Ontario, a certain percentage of cases involve multiple actions in different provinces.³²⁷ Because each province broadly interprets the territorial application of its respective laws and because there is no equivalent mechanism to the U.S. multidistrict litigation procedures, Canadian attorneys routinely struggle with the problem of class cases being filed in multiple jurisdictions, each purporting to represent classes with overlapping members.³²⁸

As a practical matter, parties in the various provinces will often work cooperatively. Sometimes, the class action in one province will be limited to expressly exclude investors covered by a related class action in a different province.³²⁹ To the extent a global

³²⁴ *Silver v. IMAX Corp.*, 2013 ONSC 1667, [2013] 36 C.P.C. 7th 254, para. 190 (Can. Ont. Sup. Ct. J.).

³²⁵ *Silver v. IMAX Corp.*, 2013 ONSC 6751, [2013] 117 O.R. 3d 616 (Can. Ont. Sup. Ct. J.).

³²⁶ Several years ago, several groups were created to tackle such cross-border issues including: (i) the ABA Canada/U.S. Class Action Protocol Project; (ii) the Canadian Bar Association National Task Force; and (iii) the International Bar Association’s Task Force on International Procedures and Protocols for Class Actions.

³²⁷ NERA reports that “[a]pproximately 23% of all cases involve claims filed in more than one province.” NERA 2015 at 5. NERA also notes that, “[h]istorically, approximately 78% of all new securities class actions involve a filing in Ontario and 25% involve a filing in Quebec. Only 12% of all cases do not involve a filing in least Ontario or Quebec.” *Id.*

³²⁸ See *Tiboni v. Merck Frosst Canada Ltd.* (2008), 295 D.L.R. 4th 32, [2008] O.J. No. 2996 (QL) (Can. Ont. Sup. Ct. J.), and *Wuttunee v. Merck Frosst Canada Ltd.* (2008), 312 Sask. R. 265, [2008] S.J. No. 324 (QL) (Can. Sask. Q.B.), *rev’d* (2009), 324 Sask. R. 210, [2009] S.J. NO. 179 (QL) (Can. Sask. C.A.). See also Scott Maidment, *Exclusive Forum Selection In National Class Actions: A Common Issues Approach*, 5 Canadian Class Action Review 133 (Irwin Law, Canada, Aug. 2009). In *Canada Post Corp. v. Lépine*, 2009 SCC 16, [2009] 1 S.C.R. 549 (Can.), at para. 57, the Supreme Court urged the provincial legislatures to develop a legislative framework for national class actions.

³²⁹ See, e.g., Order (Settlement Approval), *The Trs. of The Labourers’ Pension Fund of Cent. & E. Canada v. Sino-Forest Corp.*, No. CV1143115300CP (Can. Ont. Sup. Ct. J. Mar. 29, 2016).



settlement is reached, the parties often present the settlement for approval in their respective provinces with an understanding that the court in each province must approve the settlement for it to take effect. In some instances, the parties will agree that one or more judges can sit together to supervise nationwide settlement proceedings.³³⁰

Currently pending before the Canadian Supreme Court is a case that Canadian attorneys hope will result in an order providing guidance on dealing with inter-province cases. In what is known as the “tainted-blood” case, the parties in all provinces except British Columbia (“B.C.”) and Quebec agreed to defer to the jurisdiction of the Ontario courts to resolve nationwide settlements. However, rather than approving the settlements while physically present in their respective provinces, the Ontario, B.C. and Quebec judges all sat together in Alberta to exercise their supervisory oversight, as they were already in Alberta for other reasons. The Attorney General of Ontario argued that the Ontario judge lacked jurisdiction to sit outside Ontario and appealed its rulings.³³¹ The Ontario Court of Appeal dismissed the appeal and the matter is now before the Canadian Supreme Court.³³²

Monitoring of Canadian Cases and Potential Scope Of Class

Unlike the U.S., there are no services tracking all Canadian securities class action filings. This is in

part because there is no nationwide scheme, the court filing systems are not all electronic and there are far fewer cases brought in Canada. There is a nationwide class action database held by the Canadian Bar Association.³³³ However, except for Ontario cases, it is a voluntary pilot project and, thus, is not comprehensive. The website states that “[t]he database will list all class actions filed in Canada after January 1, 2007 that are sent to the CBA. Once posted, a class action proceeding will remain on the database unless and until it is dismissed as a class action by the court. Counsel can request that proceedings filed prior to January 1, 2007 be posted on the CBA website. These ‘archived’ class actions will be posted as soon as time permits.” However, since Canadian securities class actions are increasing in number, there may be increased tracking of securities cases.

Hiring Counsel

All provinces that allow class actions also permit lawyers to be paid by a contingency fee in such cases.³³⁴ That is, attorneys can advance all fees and expenses in a class action and plaintiffs are not liable for any payment of fees and reimbursement of expenses if there is no recovery in the case.

Usually, Ontario firms will enter into retention agreements that provide for contingent fees comprising 20 to 30 percent of recovery in any class action or, alternatively, for fees based on a specific multiplier of lodestar. Retention agreements are generally the same for all types of class actions, including securities class actions. The attorneys must file a motion for attorneys’ fees to receive payment from a settlement.

Canadian courts have not established a specific standard for assessing the reasonableness of an award of fees and reimbursement of expenses in class actions.³³⁵ In Ontario, courts will review counsel’s fee

³³⁰ Interestingly, one of the recent amendments to the Quebec civil procedure code may affect inter-province cases. Article 577 of Quebec’s newly revised Code of Civil Procedure now provides that “[t]he court cannot refuse to authorize a class action on the sole grounds that the class members are part of a multi-jurisdictional class action already under way outside Quebec. If asked to decline jurisdiction, to stay an application for authorization to institute a class action or to stay a class action, the court is required to have regard for the protection of the rights and interests of Quebec residents.” Article 577 further gives the court the right to authorize a plaintiff to “institute a class action involving the same subject matter and the same class if it is convinced that the class members’ interests would thus be better served,” despite the threat of duplicative litigation.

³³¹ See *Parsons v. The Canadian Red Cross Society*, 2013 ONSC 3053, [2013] 363 D.L.R. 4th 352 (Can. Ont. Sup. Ct. J.).

³³² *Parsons v. Ontario*, 2015 ONCA 158, [2015] 125 O.R. 3d 168 (Can. Ont. C.A.).

³³³ See <http://www.cba.org/Publications-Resources/Class-Action-Database>.

³³⁴ See, e.g., the *Solicitors Act*, R.S.O. 1990, c S.15 and *Contingency Fee Agreements*, Ont. Reg. 195/04; see also Erik S. Knutson & Janet Walker, *Litigation Funding and Costs in Canada*, 7 (July 2009), available at <http://docplayer.net/918116-Litigation-funding-and-costs-in-canada.html>.

³³⁵ Courts apply the same standard for all class actions, securities



request to determine whether it is “fair and reasonable,” and the Class Proceedings Act expressly adopts the lodestar plus multiplier metric.³³⁶ Similar to the U.S., some Ontario courts consider both reasonableness of a percentage award and the lodestar approach. The courts consider essentially the same factors that U.S. courts consider, such as: (i) the results achieved; (ii) the risks undertaken; (iii) the time expended; (iv) the complexity of the matter; (v) the degree of responsibility assumed by counsel; (vi) the importance of the matter to the client; (vii) the quality and skill of counsel; (viii) the ability of the class to pay; (ix) the client and class expectation; (x) avoiding inconsistencies with awards in similar cases in other jurisdictions; and (xi) fees in similar cases. With respect to the lodestar approach, a 2007 report indicates that the average multiplier applied is 2.5.³³⁷

Loser Pays Provisions Apply

For the most part, Canada traditionally has been a “loser pays” regime. Canadian courts have considerable discretion to award costs and will only assess an award based on what is “fair and reasonable” for that person to pay.³³⁸ In addition to the “fair and reasonable” requirement, Ontario recently revised its Rules of Civil Procedure to provide that the court must consider proportionality when making a costs award:

In applying these rules, the court shall make orders and give directions that are proportionate to the importance and complexity of the issues, and to the amount involved, in the proceeding.³³⁹

or other.

³³⁶ S.O. 1992, c 6, s. 33(7).

³³⁷ See Benjamin Alarie, *Rethinking the Approval of Class Counsel’s Fees in Ontario Class Actions*, The Canadian Class Action Review, Vol. 4, No. 1 (July 2007), pp. 15-46.

³³⁸ See *Celanese Canada Inc. v. Canadian National Railway Co.* (2005) 196 O.A.C. 60, [2005] O.J. No. 1122 (Can. Ont. C.A.) (costs fixed by a court must be fair and reasonable); R.S.O. 1990, c. C.43, s. 131(1) (“Subject to the provisions of an Act or rules of court, the costs of and incidental to a proceeding or a step in a proceeding are in the discretion of the court, and the court may determine by whom and to what extent the costs shall be paid”).

³³⁹ Ontario Rules of Civil Procedure, R.R.O. 1990, Reg. 194, r. 1.4(1.1). In an effort to encourage settlement, Ontario has implemented special cost rules related to offers of settlement. *Id.*,

Even when “loser pays” applies, it is very rare for the court to order the unsuccessful party to pay the full amount of the prevailing party’s costs. Rather, the courts award costs on different scales, such as partial indemnity, substantial indemnity and full indemnity.³⁴⁰ Courts typically award costs based on partial indemnity, which generally ranges from 40 to 75 percent of the actual, reasonable fees.³⁴¹ Substantial and full indemnity awards are rare and are reserved for situations in which the unsuccessful party conducted itself in a manner deserving of sanctions.³⁴² Substantial indemnity awards are typically 90 percent of the actual legal costs, and full indemnity is 100 percent of the actual costs, as the name implies.³⁴³ The wide discretion of the courts has left litigants unable to predict their exposure to adverse costs awards.

Over the years, however, some provinces have shifted away from this regime in the context of class actions. The following Canadian provinces are “no-way costs” jurisdictions in class actions; that is, generally each party bears its own costs (unless there is vexatious, frivolous or abusive conduct): British Columbia, Manitoba and Newfoundland. Nevertheless, in certain instances, costs will be assessed even in these jurisdiction—for example, for certain motions in the pre-certification stage.

The following Canadian provinces are “loser pays” jurisdictions even in the class action context: Alberta, Ontario, New Brunswick, Nova Scotia and Saskatchewan. In most of these provinces, the legislature provides the many factors that go into the cost award determination, including the stage of the litigation, the context of the case (*i.e.*, novel issues of law) and the conduct of the parties.³⁴⁴ Moreover, as discussed more fully below, an Ontario court recently

r. 49.10.

³⁴⁰ Erik S. Knutsen, *The Cost of Costs: The Unfortunate Deterrence of Everyday Civil Litigation in Canada*, 116, 36 Queen’s L.J. 113, 122 (2010).

³⁴¹ *Id.* at 123.

³⁴² *Id.* at 124.

³⁴³ *Id.*

³⁴⁴ See, e.g., Ontario CPA, 1992, S.O. 1992, s. 31(1); Alberta Rules of Court, Alta Reg. 124/2010, r. 10.32; Saskatchewan CAA, S.S. 2001, c C-12.01, s. 40(2); Nova Scotia CPA S.N.S. 2007, c 28, s. 40.



considered the source of funding in assessing what costs to order against a losing plaintiff.³⁴⁵ The level and nature of the costs vary across each province. These costs are evaluated and awarded on a motion by motion basis.

Costs awards to the prevailing party are not inconsequential. In *Kerr v. Danier Leather Inc.*,³⁴⁶ the court awarded costs in excess of \$1 million against the plaintiff. In a more recent decision *McCracken v. Canadian National Railway Co.*,³⁴⁷ the plaintiff was awarded over \$750,000 for costs of the certification motion. Funding agreements are, thus, an integral part of Ontario cases.

Funding Of Cases

There are three main sources of funding for class proceedings in Ontario: (i) indemnities given by class counsel; (ii) quasi-public funding; and (iii) funding supplied by professional funders. While Ontario firms do fund some of their cases, they also embrace the use of funders.

Quasi-Public Funding

Several provinces, most notably Ontario, have an approved non-private, quasi-public funding source, which is quite unusual by U.S. standards.³⁴⁸ The Ontario source is administered through the Class Proceedings Committee (“CPC”). The CPC provides financial support for disbursements and indemnity against costs through the Class Proceedings Fund (“CPF” or “Fund”).

In 1992, the *Law Society Amendment Act* established the CPC and the CPF to provide financial support to class action plaintiffs in Ontario Class Actions.³⁴⁹ The Fund was first established with a \$500,000 grant from the Law Foundation of Ontario, which is a grant-making organization that promotes

and enhances justice for Ontarians. The CPC’s current sources of funding are: (i) a levy of 10 percent of any awards or settlements in favor of plaintiffs in funded proceedings; and (ii) a return of any funded disbursements after settlement or award.³⁵⁰

Plaintiffs’ applications for CPC funding (including oral submissions) are confidential. The CPC may seek the applicants’ permission to request written submissions from defendants. Any defense submission is not confidential and plaintiffs may receive a copy of it. If accepted: (i) plaintiffs must fulfill reporting requirements (*i.e.*, they need to provide advance notice of motions and copies of documents filed with the court); (ii) all costs, including “loser pays” costs, are covered; and (iii) 10 percent of any recovery is paid back to the Fund.

The CPC “determines whether applicants will receive funding based upon a number of considerations including the merits of the plaintiff’s case, the extent to which the issue in the proceeding affects the public interest, the plaintiff’s efforts to raise funds, the likelihood of certification and the amount of money in the Fund.”³⁵¹ The CPC summarizes its financials as well as statistics regarding applications, such as total number of hearings held and applications approved, in its annual reports.³⁵² The Law Commission of Ontario published a report in 2013 indicating that, “[s]ince its inception, the CPF has considered more than 130 applications for funding and has approved 82 of them, 30 of which have resulted in settlements or awards.”³⁵³ The Law Commission of Ontario Report highlights what it refers to as “frailties” of the existing CPF structure.³⁵⁴

As alluded to earlier, in the fall of 2012, a court issued an adverse cost award of \$1,766,000 in the matter of *Smith v. Inco Limited* (a non-securities

³⁴⁵ See discussion of *Smith v. Inco, infra*.

³⁴⁶ 2007 SCC 44, [2007] 3 S.C.R. 331 (Can.).

³⁴⁷ 2010 ONSC 6026, [2010] O.J. No. 4650 (QL) (Can. Ont. Sup. Ct. J.).

³⁴⁸ Quebec also has a provincial public fund, the Fonds d’aide aux recours collectif. <http://www.faac.justice.gouv.qc.ca/>.

³⁴⁹ See <http://www.lawfoundation.on.ca/who-we-are/history/>.

³⁵⁰ See <http://www.lawfoundation.on.ca/class-proceedings-fund/how-to-apply/>.

³⁵¹ Defense attorneys have served on the committee evaluating whether to fund a case under this scheme.

³⁵² See <http://www.lawfoundation.on.ca/who-we-are/history/>.

³⁵³ See *Review of Class Actions in Ontario: Issues to be Considered*, Law Comm’n of Ontario, Nov. 2013, at 7, <http://www.lco-cdo.org/class-actions-issues-to-be-considered.pdf> (hereinafter “Law Commission of Ontario Report”).

³⁵⁴ See *id.* at 7.



class action) against plaintiffs in a CPC funded case.³⁵⁵ However, the amount ordered was half that requested by the defendant because, as the court explained, the CPC “is available for the purpose of facilitating access to justice for large groups of the population who may wish to pursue a class proceeding. However, the Fund is not bottomless and a costs order that would cripple the Fund should not be made as it could unduly stifle subsequent claims.” Law Commission of Ontario Report at 7.

Private Funding

Ontario law firms are also increasingly using private funders. In *Metzler Investment GMBH v. Gildan Activewear Inc.*, the Ontario court determined that third-party agreements are not inherently champertous, but can become so in the presence of an improper purpose (for example over-compensation, improper motive or the potential for “officious intermeddling” in the litigation).³⁵⁶ Shortly thereafter, in *Dugal v. Manulife Financial Corporation*, (“Dugal”) Justice Strathy held that a foreign litigation funding company could indemnify the plaintiffs from their exposure to a potential adverse cost award in exchange for a cut of any money recovered from litigation.³⁵⁷ In the Order, the court noted that litigation funding was a necessity given the loser-pays model in effect in Ontario.³⁵⁸ However, in approving the agreement, it was important to the court that the private funder had not “stirred up, incited or provoked this litigation,” and that the private funder was charging a “reasonable” (7 percent) commission with a “reasonable” commission cap (\$5 million pre-trial and \$10 million thereafter).³⁵⁹ Additionally, the funding agreement left control of the litigation in the hands of the representative plaintiff as long as the funder received appropriate information about the progress of the case.³⁶⁰

³⁵⁵ 2011 ONCA 628 [2011] 107 O.R. (3d) 321 (Can. Ont. C.A.).

³⁵⁶ See *Metzler Investment GMBH v. Gildan Activewear Inc.*, [2009] O.J. No. 3315 (QL) (Can. Ont. Sup. Ct. J.).

³⁵⁷ See *Dugal v. Manulife Financial Corp.*, 2011 ONSC 1785, [2011] 105 O.R. 3d 364 (Ont. Sup. Ct. J.) (provides outline of terms of retention agreements).

³⁵⁸ *Id.* at para. 28.

³⁵⁹ *Id.* at para. 33.

³⁶⁰ *Id.*

Third-party financing has been approved in several cases since *Dugal* including in *Kinross Gold and Smith v. Sino-Forest Corp.* (“Sino-Forest”).³⁶¹ Courts in other Canadian provinces have approved funding agreements as well.³⁶²

A key difference between obtaining third-party funding and funding through the Class Proceedings Fund is that the third-party funding must be approved by the court.

If an application is made to the Class Proceeding Fund, the court does not need to approve the arrangement, as it is made pursuant to the legislation set out above. In *Dugal*, Justice Strathy considered the specific facts of the case and determined that the private funding agreement was neither “champertous” nor illegal under Ontario law. Justice Strathy did require further information on two issues regarding the arrangement: (i) further evidence regarding the capacity of the funder to satisfy any costs award that may be made; and (ii) further information about the reasonable controls on the provision of information to the funder. Once this further evidence was given, Justice Strathy approved the agreement.

One advantage to obtaining third-party funding is that the amount paid as a levy can be negotiated. In contrast, with the Class Proceedings Fund, the levy is always 10 percent. In *Dugal*, as noted above, the plaintiffs were able to negotiate an agreement where the funder would receive 7 percent of any money recovered.

³⁶¹ 2012 ONSC 24, paras. 141-142 (Can. Ont. Sup. Ct. J.).

³⁶² See *Hobshaw v. Atco Gas and Pipelines Ltd.* (May 14, 2009), Action 0101-04999 (Can. Alta. Q.B.) (approving a third party funding agreement in the Alberta Court of Queen’s Bench); *MacQueen v. Sydney Steel Corporation* (October 19, 2010), Action 218010 (N.S.S.C.) (approving a third party funding agreement in the Supreme Court of Nova Scotia).

E. DENMARK



The Trends in Securities Litigation in Denmark

The Danish Administration of Justice Act (“Danish Act”) became effective on January 1, 2008, and provides for both opt-in and opt-out class actions.³⁶³ But since that time, relatively few class actions have been brought under the law.

While the Danish Act provides for opt-out class actions, private plaintiffs may only bring opt-in class actions, and the class representative may be required to pay legal costs as a security and potentially additional legal costs up to the amount they stand to recover. Opt-out class actions, on the other hand, may only be brought by public bodies, primarily the Danish Consumer Ombudsman (*Forbrugerombudsmanden*), and such actions will only be deemed appropriate when the damages per class member is small.

The Danish Act required a “sunset” review of the regime after three years. The review was planned to be undertaken in 2012, but the review has been postponed. A key reason for including a review provision in the Act was to address fears, principally voiced by the

business community, that Danish class actions would exponentially increase as a result of the Danish Act and create what opponents to the Act termed the “American situation” in Denmark.³⁶⁴ But that has not been the case, as Danish class actions remain relatively rare.

Opt-In and Opt-Out Actions Under the Danish Act

After significant debate and a recommendation by the Standing Committee on Procedural Law (*Retsplejerådet*), the Danish Parliament enacted the Danish Act in February 2007. Effective as of January 1, 2008, this law provides for two types of class actions: (i) an opt-in class action, and (ii) a representative action (i.e., an opt-out class action). Class actions may only be brought when the class members have “uniform claims” based on the “same factual circumstances” as well as the “same legal basis,” and Denmark must be the proper legal venue for all asserted claims. The court must determine that a class action is the best way of examining the claims. Finally, court approval is required for settlement.

³⁶³ Administration of Justice Act, pt. 23, Act No. 181. Feb. 28, 2007 (Den.) (in force Jan. 1, 2008).

³⁶⁴ Dan Terkildsen & David Frolich, *New Possibilities for and First Experiences with Class Actions in Denmark*, The Int’l Litig. Quarterly, Am. Bar Ass’n (Summer 2010).



In opt-out class actions, only a public entity, such as the Danish Consumer Ombudsman, may serve as a class representative. This requirement reflects the fact that an opt-out class action was believed, by at least some, to be foreign to Danish legal tradition. In addition, the amount of each member's claim must typically be no more than 2,000 Danish kroner or 270 euros because opt-out proceedings are only considered appropriate if the claims are "unmarketable." Whether proceedings will take place on an opt-in or opt-out basis lies within the judge's discretion.

According to the legislative history, examples of cases that might be suitable for a class action include:

- homes with roof materials that crumbled;
- hemophiliacs that had been treated with HIV infected blood in public hospitals;
- compensation claims for flight tickets;
- unlawful fees collected by banks;
- cases on unlawful price trusts;
- a prospectus with material omissions; and
- a large number of subscribers of a telecommunications company claiming that the company collected rates that were higher than authorized.

Interestingly, the Danish Standing Committee on Procedural Law that recommended the law acknowledged the possibility that a small minority of class members might not become aware of an opt-out notice, but concluded that this issue did not give rise to due process concerns.

Given these limitations, securities class actions tend to be opt-in. Private parties may bring opt-in class actions. After receiving notice, parties that want to opt-in must register with the court. The parties may be required to pay money to register as security as well as pay additional legal costs up to the amount that they might be able to recover. The class representative may

be changed when at least half of members of the group make the request.

Attorneys' Fees, Costs, and Third-Party Funding

In Denmark, under the general rules of the Administration of Justice Act on legal costs, the losing party is normally ordered to pay at least a proportion of the costs which the other party has to pay to his lawyer. This rule applies to opt-in class actions. Moreover, the court may require the class representative to provide security for legal costs as well as pay outstanding costs not covered by the group. In class actions, if there is a risk of very high legal costs, security is generally required.

The maximum costs to be covered by group members are decided at the beginning of proceedings. In opt-out class actions, however, participating members cannot be ordered to provide security for legal costs, and they may only be ordered to pay legal costs that do not exceed the maximum amount the group member may receive as a result of the action.

Interestingly, contrary to many foreign countries, Denmark bar rules allow lawyers to bring cases on a contingent basis. That is, lawyers may contract with their clients to advance all costs and only seek fees if they obtain a recovery. The one significant limitation is that it is unlawful for lawyers to agree to take a contingent fee that is fixed as a certain portion of the damages awarded. Thus, while the lawyer's fee may still be contingent on the outcome of the case, the amount of the fee must be dictated by some metric other than as a percentage of recovery. For example, a lawyer may agree to take nothing, or 50% of his or her hourly rate, when an action is unsuccessful, but seek to be paid an hourly rate plus a multiplier if the action is successful.

While third-party funding is permitted, such funding may have tax implications or be questionable if made with an illegal purpose. To date, third-party funding has not yet been employed in Denmark to fund class actions. Rather, the attorneys have funded the cases themselves.



Danish Securities Laws

The OMX Nordic Exchange Copenhagen is the Danish center for trade of listed securities such as stock, bonds, notes, derivatives and money market instruments. The OMX Nordic Exchange Copenhagen is a part of OMX Nordic Exchange, which consists of two divisions: (i) OMX Exchanges, which operates seven stock exchanges in the Nordic and Baltic countries (including the OMX Nordic Exchange Copenhagen); and (ii) OMX Technology, which develops and markets systems for financial transactions that are used by the OMX Exchanges and other stock exchanges. Securities listed at the OMX Nordic Exchange Copenhagen are carried out electronically and registered with the VP Securities Services (*Værdipapircentralen*).

The most important securities laws are: (i) the Danish Securities Trading Act (*Værdipapirhandelsloven*); (ii) the Danish Financial Businesses Act (*LovomFinansielVirksomhed*); and (3) the Rules Governing Securities Listing on the Nasdaq OMX Copenhagen.³⁶⁵ These acts and rules are supplemented by derivative regulation issued through a number of executive orders setting forth detailed provisions on particular subjects such as issuers' disclosure duties. In addition, the Danish Financial Supervisory Authority ("the DFSA") has issued a number of guidelines on the interpretation of the executive orders. Finally, the EU Transparency Directive provides the framework for issuers of securities admitted to trading on a regulated market within a member state (listed companies).

Notably, these securities statutes do not provide a specific private right of action for securities fraud.

Recent Cases

Since the Act became effective in 2008, there have only been a few class actions brought in Denmark concerning financial misconduct, with one additional case likely to be brought in the future.

Bank Trelleborg

The case involving Bank Trelleborg was the first class action of any kind brought under the Danish Act. The case arose out of Bank Trelleborg's financial troubles that resulted in a forced acquisition of the bank by Sydbank. A group representing nearly 5,000 minority investors of Bank Trelleborg sued Sydbank, a group of majority shareholders that had requested the compulsory acquisition, and the Danish Financial Supervisory Authority on the basis that the compulsory acquisition and redemption of shareholders' shares was unlawful. Notably, Denmark's Eastern High Court eventually ruled that the compulsory redemption was unlawful, but determined that the minority shareholders suffered no damages.³⁶⁶ Despite this setback, Sybank ultimately settled with the minority shareholders in 2013 by agreeing to pay 135 million Danish kroner (about US\$20.2 million).³⁶⁷

Jyske Bank

Denmark's second class action involved a hedge fund administered by Jyske Bank (Jyske Invest Hedge Markedsneutral - Obligationer), which had lost 80% of its value. 1,100 investors brought a class action under the Danish Act alleging misrepresentations and omissions in the fund's prospectus materials. Ultimately, through settlement, investors recovered approximately 300 million Danish kroner (about US\$45 million).³⁶⁸

Pandora

In July 2014, a group of 36 mostly institutional investors sued Danish jewelry manufacturer and retailer Pandora A/S and its CEO for issuing a late profit warning. On August 2, 2011, Pandora slashed

³⁶⁶ See *The Eastern High Court finds compulsory acquisition unlawful*, Dec. 8, 2010, at <http://www.mwblaw.dk/en/Nyheder/Nyheder%202010/2010-12-07%20Oestre%20Landsret%20finder%20tvangsindebetegnelse%20ulovlig.aspx>.

³⁶⁷ Press Release, Sydbank, Settlement of bankTrelleborg claims (Aug. 7, 2013), at <https://globenewswire.com/news-release/2013/08/07/565081/0/en/Settlement-of-bankTrelleborg-claims.html>.

³⁶⁸ See *LETT in brief – highlights from 2015 at LETT Law Firm*, at 7, at http://www.lett.eu/media/1841791/aarsrapport-2015_uk_20pages/www.pdf.

³⁶⁵ Portions of this section are from <http://www.mwblaw.dk/Doing%20Business%20in%20Denmark/Securities%20law.aspx>.



its previous profit guidance from 30% down to zero, prompting a 65% one-day drop in its share price. The investor-plaintiffs seek damages ranging from €20 million to €50 million.³⁶⁹ The case is ongoing.

Vestas Wind Systems

In August 2013, a group of 87 institutional investors sued Danish wind turbine maker Vestas Wind Systems A/S for losses resulting from the company's misleading statements about its revenues and other financial matters. A related class action filed in U.S. federal court on behalf of ADR purchasers settled for \$5,000,000 in 2014.³⁷⁰ The Danish litigation remains ongoing.

OW Bunker

Investors are currently joining together with the view of initiating a class action against Danish fuel supplier OW Bunker, which filed for bankruptcy only eight months after its IPO in March 2014.

The claims asserted in these cases typically originate from (a) statutes regarding generalized torts or breaches of contract that are applied in the securities fraud context, or (b) violations of certain financial regulations. Denmark does not have a particular securities fraud statute, like Section 10(b) of the Exchange Act and Rule 10b-5, upon which plaintiffs' claims are consistently brought.

³⁶⁹ Investors in Denmark's Pandora sue over 2011 profit warning, Reuters, July 31, 2014, available at <http://www.reuters.com/article/pandora-lawsuit-idUSL6N0Q643Z20140731>.

³⁷⁰ Press Release, Vestas Wind Systems, Vestas – Court approval of proposed settlement of US class action, Dec. 9, 2014, at <https://globenewswire.com/news-release/2014/12/09/689912/0/en/Vestas-Court-approval-of-proposed-settlement-of-US-class-action.html>.

F. ENGLAND & WALES



Overview

The combined jurisdiction of England and Wales does not presently have an American style class action system for securities litigation. There are, however, other methods of multi-party actions available. In England and Wales, there are presently two types of collective actions available, including: (i) representative actions; and (ii) the Group Litigation Order (“GLO”).³⁷¹

Representative actions are the most similar to the American class action. In a representative action, one claimant can represent other parties with the same interest.³⁷² Representative actions, however, are rarely used because they are not available where members of the class have different remedies or defenses.³⁷³

³⁷¹ Scotland has a different legal system and has not introduced a group action procedure.

³⁷² The Civil Procedure Rules, 2016, Part 19.II. (U.K.). <https://www.justice.gov.uk/courts/procedure-rules/civil/rules/part19>.

³⁷³ Alison Brown & Ian Dodds-Smith, *England & Wales: Class and Group Actions 2016*, available at <http://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/>

Any action where damages must be proved cannot be brought as a representative action. The strict limitations on representative actions led to the development of the GLO mechanism.³⁷⁴

The GLO, introduced in 1999, is a mechanism created by the courts for managing multiple claims, “which give rise to common or related issues of fact or law (the ‘GLO issues’).”³⁷⁵ Before the court grants a GLO, it must determine that it will be the most appropriate means of resolving the claims and must establish:

- A group register on which details of the claims to be managed under the GLO must be entered;

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³⁷⁴ Dr. Christopher Hodges, *Global Class Actions Project Country Report: England and Wales*, 3 (2010), available at http://globalclassactions.stanford.edu/sites/default/files/documents/England_Country%20Report.pdf.

³⁷⁵ The Civil Procedure Rules, 2016, Part 19.10. (U.K.). <https://www.justice.gov.uk/courts/procedure-rules/civil/rules/part19>.



- The GLO issues, which will identify the claims to be managed under the GLO; and
- The “management court” responsible for managing the claims.³⁷⁶

A GLO is not considered a representative action because it covers individual claims. It is possible, however, that a lead or test case may be selected for decision on a certain issue before other GLO participants.³⁷⁷ So-called “lead actions” allow for a determination of law or fact that can then be applied in other GLO cases to allow the other actions to focus on any remaining individual issues. The rules of estoppel require that any judgment on one GLO issue be binding on all other claims on the group register, unless otherwise ordered by the court.³⁷⁸

There are several steps that must be taken to initiate a GLO. First, either a plaintiff or defendant in a claim may apply to the court for a GLO. The application should summarize the litigation, including the nature and number of claims, parties, and the common issues to the litigation. The applicant should also specify whether there are issues that distinguish any sub-groups. There is no predominance requirement in the GLO criteria, which allows the mechanism to operate as a more flexible case management tool. Once the application is approved, the group litigation is assigned to a judge who has specialized GLO experience. After the GLO has been granted, the judge can order that a group of specific lawyers represent parties in the group so as to ensure more effective coordination. In some of the more complex cases, a “steering group” of lawyers may be appointed.³⁷⁹

³⁷⁶ Alison Brown & Ian Dodds-Smith, *England & Wales: Class and Group Actions 2016*, <http://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/england-and-wales>.

³⁷⁷ Dr. Christopher Hodges, *Global Class Actions Project Country Report: England and Wales*, 1 (2010), http://globalclassactions.stanford.edu/sites/default/files/documents/England_Country%20Report.pdf.

³⁷⁸ Alison Brown & Ian Dodds-Smith, *England & Wales: Class and Group Actions 2016*, <http://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/england-and-wales>.

³⁷⁹ Dr. Christopher Hodges, *Global Class Actions Project Country Report: England and Wales*, 14, 17 (2010), http://globalclassactions.stanford.edu/sites/default/files/documents/England_Country%20Report.pdf.

There is no oversight by the courts regarding the fairness and reasonableness of settlements.³⁸⁰

GLO proceedings still remain relatively uncommon in England and Wales. Since 2000 the courts have only managed 92 GLOs and, of those, 14 have been commenced since 2012.³⁸¹

Loser Pay Model

Similar to the “loser pay” model, England and Wales follow a “cost shifting” rule that requires the losing party to pay the prevailing party’s court fees and legal costs. Such fees also include costs for expert witnesses and other incidental expenses. It is up to the court to make a determination on the appropriate fees to be paid. In determining the appropriateness of the fees, the court may consider a party’s success on a particular issue and/or the parties’ conduct in the litigation. Costs are often significantly discounted upon assessment by the court. Thus, England and Wales does not operate under a full “loser pay” model.³⁸²

If one party offers a settlement that meets certain requirements, called a “Part 36 offer,” and the opposing party does not accept, the opposing party may be liable for all costs incurred after refusal of the offer unless the opposing party achieves a better result at trial.

Opt-In vs. Opt-Out

Claimants to an opt-in collective action only join collective proceedings when they actively assert membership to a class action. Whereas claimants to an opt-out collective action will automatically fall within globalclassactions.stanford.edu/sites/default/files/documents/England_Country%20Report.pdf.

³⁸⁰ *Id.* at 15, 25.

³⁸¹ Alison Brown & Ian Dodds-Smith, *England & Wales: Class and Group Actions 2016*, <http://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/england-and-wales>.

³⁸² David H. Kistenbroker, Alyx S. Pattison, Patrick M. Smith, *Recent Developments in Global Securities Litigation*, 1904 PLI Corp. 607, 13 (2011); http://www.kattenlaw.com/files/upload/Recent_Developments_in_Global_Securities_Litigation_2011.pdf Alison Brown & Ian Dodds-Smith, *England & Wales: Class and Group Actions 2016*, <http://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/england-and-wales>.



a ‘class’ for the purposes of the proceedings unless they take steps to opt-out. The GLO system requires claimants to opt in and for individual claims to be managed together. In order to be coordinated under the GLO, a claimant must have issued its proceedings in the management court (or had them transferred there) and be named on the group register.³⁸³

The U.K. Government has considered introducing a generic right to a collective action on a sector-specific basis. The only sector-specific rule for litigation currently available is for cases regarding competition laws.³⁸⁴ The Consumer Rights Act 2015, which came into force on 1 October 2015, makes it easier for companies who have suffered harm as a result of an infringement of competition law both to bring a damages claim and obtain compensation. Under the previous system only opt-in collective actions were permitted but, under the Consumer Rights Act regime, opt-out collective actions are now also allowed. The U.K.’s Competition Appeal Tribunal is the main forum in which to bring such claims. One notable difference from individual proceedings is that exemplary damages are not available in collective proceedings.³⁸⁵ Also, contingency fee type arrangements are not permitted in these opt-in proceedings.

GLO Costs

Costs incurred under a GLO are usually divided into individual costs and common costs. Individual costs are costs associated with the defense or pursuit of an individual claim and common costs are those costs incurred in defending or pursuing the GLO issues. Additional common costs are incurred by a firm acting for the claimants who are appointed by the court as the Lead Solicitor in order to administer the group litigation, performing tasks such as keeping the group register and preparing court bundles and transcripts.

³⁸³ Alison Brown & Ian Dodds-Smith, *England & Wales: Class and Group Actions 2016*, <http://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/england-and-wales>.

³⁸⁴ *Id.*

³⁸⁵ Lucy Cass, Consumer Rights Act 2015: Promoting collective proceedings in competition damages claims <http://www.olswang.com/articles/2015/04/consumer-rights-act-2015-promoting-collective-proceedings-in-competition-damages-claims/>.

Unlike normal multi-claimant or multi-defendant actions where liability for costs is joint and several, GLOs have a specific costs regime. The default rule under GLOs is that each claimant will be liable for its individual costs and severally liable for an equal share of common costs of pursuing the group action (and a several and equal share of any adverse costs awarded where the action does not succeed). This means an individual claimant’s contribution to his own costs and adverse costs risk is limited and often small where there are many claimants.

In securities actions, the court has recognized that the economic interest of each claimant may be very different and so may vary the default GLO position to provide that each claimant’s contribution to common costs and adverse costs risk, while still several, is pro-rata to the size of its economic interest (such as the size of its shareholding or claim) [*Trustees of Mineworkers Pension Scheme Limited and Ors v Royal Bank of Scotland Group plc*, 2014 EWHC 227 (Ch)].³⁸⁶ Such orders are perceived to be fairer as between institutions and individual shareholders in securities actions.

Jurisdiction

Foreign claimants may bring proceedings in England against English corporations or persons domiciled in England as of right under the Brussels Regulation 1215/2012 save in certain circumstances such as an exclusive jurisdiction clause in a prospectus in favor of another jurisdiction.³⁸⁷ Proceedings may also be brought in England based on conduct in England and the conduct of English subsidiaries outside of the UK. For example, South African citizens successfully brought an action against an affiliate of an English company for exposure to asbestos in South Africa.³⁸⁸

³⁸⁶ *Pension Scheme Limited and Ors v. Royal Bank of Scotland Group plc* 2014 EWHC 227, available at <http://www.bailii.org/ew/cases/EWHC/Ch/2014/227.html>.

³⁸⁷ Office Journal of the European Union: *Regulation (EU) No 1215/2012 of The European Parliament And of The Council* <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:351:0001:0032:en:PDF>.

³⁸⁸ *Lubbe v. Cape Plc*, [2000] 1 WLR 1545; Alison Brown & Ian Dodds-Smith, *England & Wales: Class and Group Actions 2016*, <http://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/england-and-wales>.



Funding the Litigation - Own Costs and Adverse Costs Risk

There are a number of options for funding litigation in England. While claimants may pay for the litigation themselves, usually at an hourly rate, the relatively high cost of group actions means that this may not be the preferred option in group litigation.³⁸⁹

There is a highly developed and well-resourced market for third party funding in England. Third party funders will typically fund some or all of the costs of litigation on a non-recourse basis in return, on a successful action, for a multiple of the funding provided or a percentage of the damages awarded. While the English courts used to have rules against champerty, these no longer apply and third party funding is recognized as contributing to access to justice.

Another method of funding a case in England is through a conditional fee agreement (“CFA”) with the law firm acting on behalf of the claimants. CFAs are commonly referred to as “no win no fee” agreements. They typically take two forms: (i) the law firm takes no fee unless the action succeeds in which case the firm receives its full fees on the basis of hours worked at its full rate along with a success fee; or more typically in commercial actions (ii) the law firm charges a discounted hourly rate and, if the action is successful, it receives an uplift to its full hourly rate along with a success fee.³⁹⁰ Success fees are calculated as a percentage of the law firm’s full fees and that percentage cannot exceed 100%. Since a change in the costs rules for actions started on or after 1 April 2013 through a series of provisions known as the Jackson Reforms,³⁹¹ success fees cannot be recovered against the defendant

³⁸⁹ Dr. Christopher Hodges, *Global Class Actions Project Country Report: England and Wales*, 26 (2010), http://globalclassactions.stanford.edu/sites/default/files/documents/England_Country%20Report.pdf.

³⁹⁰ Alison Brown & Ian Dodds-Smith, *England & Wales: Class and Group Actions 2016*, <http://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/england-and-wales>.

³⁹¹ The Jackson Reforms, implemented on April 1, 2013, are the result of Lord Justice Jackson’s wide-ranging review of the civil litigation costs system, and include his recommendations to promote access to justice.

on a successful action and must be paid by the claimant or out of damages (although the law firm’s fees on the basis of its full hourly rate can still be recovered).

Since 1 April 2013, it has been possible for English law firms to act on a contingent basis (known as a damages based agreement or “DBA”) where the law firm agrees to take a percentage of damages in lieu of its fee. In commercial cases, the percentage of damages that the law firm can take is limited to 50% of damages recovered (as opposed to awarded). The initial uptake of DBAs was low due to early issues with the regulatory regime governing them but they are becoming more common.

In terms of covering adverse cost risk, there is a mature and sophisticated market in England for After-The-Event (“ATE”) legal expenses insurance which, in return for a premium, will cover costs payable to the defendant in the event that the claim is unsuccessful. Premiums can be payable upfront, deferred and contingent (meaning that they are only payable in the event that the litigation is successful) or a mixture of the two with part of the premium payable upfront and part deferred and contingent. Since 1 April 2013, ATE premiums are not recoverable on a successful action from the defendant and must be paid out of damages.

Before-The-Event (“BTE”) legal expense insurance has recently become more popular in England. If this method of funding is used, the insurer will usually select the lawyer and there will be a financial limit. Such insurance is, however, typically focused on consumer and employment cases and is unlikely to cover group cases.³⁹²

Large commercial actions such as securities actions may often be funded by a combination of the above. For example, a third party funder may fund the discounted fees of a law firm working on a CFA and the upfront part of a partly deferred ATE premium in return for a multiple of the funding it has put in on the action being successful. In this way, the commercial effect for

³⁹² Dr. Christopher Hodges, *Global Class Actions Project Country Report: England and Wales*, 26 (2010), http://globalclassactions.stanford.edu/sites/default/files/documents/England_Country%20Report.pdf.



the claimant is similar to a U.S.-style contingent action where the claimant pays no money up front and has no adverse costs risk but will pay out a proportion of damages on a successful action.

Fraud on the Market Theory

Where securities claims rely on a fraud cause of action (see below), English law does not currently recognize the doctrine of fraud on the market. As such, claims for deceit and misrepresentation in theory require proof of actual reliance:

In bringing a claim for deceit, “[t]he claimant must in fact rely on the statement, as part of which requirement the claimant would have to be aware of the statement. This requirement is taken to rule out the theory of ‘fraud on the market,’ whereby a misstatement which has an effect on the market price can be said to cause an investor loss, even though that particular investor was not aware of the misstatement.”³⁹³

There are as yet no decided cases on how the courts will require multiple claimants to prove reliance in securities fraud cases. However, the balance of legal opinion is that the English courts will not adopt a fraud on the market theory in the same manner as the U.S. courts.

Pleading Standards

The English common law system has pleading standards that are relatively similar to the American requirements. Pleading standards are regulated in England using the Civil Procedure Rules (“CPR”) and their associated practice directions. According to CPR 7.2 -7.4, proceedings are commenced when the Claim Form, which contains basic information about the claimant and defendant along with a brief summary of the claim, is issued in court. The Claim Form is usually accompanied or followed shortly by Particulars of Claim setting out a concise statement of the facts on which the claimant relies. Particulars of Claim may also refer to points of law and witnesses intended to be called.

³⁹³ Paul Davies, *Davies Review of Issuer Liability: Liability for Misstatements to the Market*, 16 (2007), www.treasurers.org/system/files/daviesdiscussion260307.pdf.

Once the Claim Form and the Particulars of Claim have been served on the defendant, the defendant must then serve a Defense stating which of the allegations in the Particulars of Claim it denies, admits or intends to put forward a different version of events of from that given by the claimant. The defendant must state his or her own version of events in the contents of the Defense and bare denials are not permitted. A claimant is then given the opportunity to reply to the Defense.

The Particulars of Claim and Defense may be amended and such amendment is common in large cases, particularly in securities cases to take account for discovered documents which will generally all come from the Defendant.

CPR 22 also requires documents to be verified by a statement of truth. A statement of truth is a statement, to be included in any statement of case, witness statement, expert's report and certain other documents which confirm that the facts stated in the document are true. The statement of truth must be signed by the litigant (or his legal representative on instructions) or the witness or expert as the case may be. Knowingly signing a false statement of truth can be punished by sanctions for contempt of court.

Discovery

Discovery is known as disclosure in English proceedings. While not as wide-ranging as U.S. style discovery, each party is entitled to disclosure of all documents which are relevant to the case *i.e.* that might support or harm the cases of either party. Litigants are also obliged to apply document holds from the earliest time litigation is contemplated.

The current procedural rules governing disclosure attempt to reign in the costs of the disclosure process by applying the relevance standard set out above (no “train of enquiry” disclosure is permitted) and a proportionality test. However, disclosure exercises will still generally result in production of most, if not all, documents essential to the case.



All parties are generally obliged to give disclosure. However, in securities litigation, other than transaction documentation relating to the purchase of securities it is usual that claimants have few disclosable documents and all the key documents will come from the defendant. In a recent non-fraud case, it was ordered that the claimants did not have to give any disclosure [*Trustees of Mineworkers Pension Scheme Limited and Ors v Royal Bank of Scotland Group plc*, 2015 EWHC C740 (Ch)].

Depositions do not form part of English procedure. Witness evidence is given by exchange of written statements of evidence in chief on which witnesses may be cross-examined at trial.

Causes of Action in Securities Litigation

In England, as set out below, the primary causes of action for securities claims are statutory. While English law recognizes common law theories including fraud, deceit, and negligent misrepresentation, they require the relevant representation to be directed to the claimant with the intention that it relies on that representation. Documents such as prospectuses and periodic accounts are considered to have been published to the public and, as such, do not meet the common law tests. That said, where a specific representation is made to a claimant to induce it to purchase securities, such as at a road show to investors, actions in deceit and negligent misrepresentation may be available (although the claimant must prove that it relied on the misrepresentation).

The two key statutory provisions under which securities claims may be brought are Section 90 of the Financial Services Markets Act of 2000³⁹⁴ relating to non-fraud prospectus liability and Section 90A of the Financial Services Markets Act of 2000 relating to liability for fraudulent statements in certain publications by listed companies.

Section 90 of FSMA

Section 90 introduced a statutory liability regime for untrue or misleading statements contained in – or

omissions from – a prospectus or listing particulars. This updated the existing legislation applicable to listing particulars to meet the requirements of the European Prospectus Directive.³⁹⁵ It provides that any person responsible for a prospectus is liable to pay compensation to a person who has acquired securities offered by the prospectus and suffered loss as a result of any untrue or misleading statement or omission from the prospectus of matters that should be included by Section 87A. Section 87A requires that a prospectus must include the information necessary to enable investors to make an informed assessment of the issuer and the rights attaching to the securities.³⁹⁶

Similar to claims brought under Sections 11 and 12 of the Securities Act, 15 U.S.C. §§77k and l, claims brought under Section 90 do not require proof of reliance on the alleged misstatement. This is considered to be a non-reliance cause of action and claimants need not prove that they relied upon the prospectus or that they even read it, merely that the prospectus was misleading or omitted necessary information and they suffered loss as a result.

Persons responsible for the prospectus will always include the issuer and the directors of the issuer but may also include others such as the investment banks sponsoring the prospectus.

To date, there has only been one Section 90 claim brought under a GLO against an issuer – *Trustees of Mineworkers Pension Scheme Limited and Ors v Royal Bank of Scotland Group plc* (the “RBS” case). The RBS case is due to go to trial in March 2017 at the High Courts in England.³⁹⁷

In the RBS case, shareholders are claiming approximately £4 billion in damages pursuant to allegations that during RBS’ £12 billion investor cash call in 2008, which was launched just prior to the bank’s near collapse, RBS issued material misstatements to the market.³⁹⁸ Solicitors in the United Kingdom will be

³⁹⁵ Directive 2003/71/EC <http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX:32003L0071>.

³⁹⁶ Savitt, W. *The Securities Litigation Review*, Law Business Research Ltd (2015) First Edition.

³⁹⁷ See *infra* Section IV (Royal Bank of Scotland (the United Kingdom)).

³⁹⁸ See Kirstin Ridley, *British judge delays trial of RBS shareholder*



closely following the status of the RBS case throughout 2016 and 2017 as it is a test case for group/collective securities litigation in the United Kingdom. For example, an action is set to be filed against Tesco PLC (“Tesco”) by the company’s shareholders, who believe they sustained significant damages due to Tesco’s admitted overstatement of profits.³⁹⁹ The results of the RBS action will likely affect the strategy undertaken by Tesco investors.

A Section 90 claim differs from and avoids issues confronting common law actions on prospectuses arising from the case of *Derry v Peek* [(1889) 14 App. Cas. 337] which held that directors of a company were not liable in an action for deceit for untrue statements made in a prospectus unless it could be demonstrated that those directors had acted fraudulently.⁴⁰⁰

Section 90A of FSMA

Section 90A was introduced to comply with the European Transparency Directive⁴⁰¹ and was substantially updated in 2010. It provides that an issuer of securities is liable to pay compensation to persons who have suffered loss as a result of an untrue or misleading statement in – or omission from – certain publications made by the issuer or dishonest delay in publishing such information. Such publications include not only periodic financial reports but any information published by a recognized information service or information whose availability (e.g. on a website) is announced by means of a recognized information service. Persons entitled to compensation include those who bought, continued to hold or sold the securities in reasonable reliance on the publication and so include those in the open market.

However, this is a fraud cause of action and, as such, claimants must prove that persons with managerial

lawsuit to 2017, Reuters, (Nov. 26, 2015), <http://uk.reuters.com/article/uk-rbs-lawsuit-shareholders-idUKKBN0TF1Y420151126>.

³⁹⁹ See Alan Tovey, *Tesco faces £100m damages claim over accounting black hole*, The Telegraph, (Jan. 26, 2016), <http://www.telegraph.co.uk/finance/newsbysector/retailandconsumer/12121817/Tesco-faces-100m-damages-claim-over-accounting-black-hole.html>.

⁴⁰⁰ Hudson, A. *Securities Law*, Sweet & Maxwell (2013) Second Edition

⁴⁰¹ 2004/109/EC <http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX:32004L0109>.

responsibility within the issuer (generally the directors) knew that the statement was untrue or misleading (or were reckless as to whether it was) or that an omission was a dishonest concealment of a material fact and that the claimant relied on the relevant information. The fact that the claimant must also prove that it relied on the information at a time, and in circumstances, when it was reasonable for it to do so means that the reliance threshold is more exacting than the test for reliance in a common law deceit claim where reasonableness is not relevant.

Under the U.K. Companies Act of 2006, shareholders may also bring derivative suits for breach of duty, breach of trust, and director negligence.⁴⁰²

Regulatory Body for Securities

Since the 2006-08 financial crisis, the U.K. has undergone significant reform of its regulatory bodies. New reforms were published in February 2011 to be overseen by the Financial Policy Committee, the Prudential Regulation Committee and the Financial Conduct Authority. The Financial Policy Committee is assigned to oversee and regulate the entire U.K. financial system. The Prudential Regulation Committee regulates the financial institutions that carried the greatest balance sheet risk. The Financial Conduct Authority is the successor to the U.K. Financial Services Authority (“FSA”), which was the U.K.’s version of the SEC.⁴⁰³ According to the reform papers, the goal of the Financial Conduct Authority is to “protect and enhance the confidence of all consumers of financial services.”⁴⁰⁴

⁴⁰² Companies Act, 2006, c. 46 (U.K.); Robert F. Carangelo, Paul A. Ferrillo and Catherine Y. Nowak, *Designing a New Playbook for the New Paradigm: Global Securities Litigation and Regulation*, 3 (2011), <http://www.dandodiary.com/2011/12/articles/securities-litigation/designing-a-new-playbook-for-the-new-paradigm-global-securities-litigation-and-regulation/>.

⁴⁰³ Robert F. Carangelo, Paul A. Ferrillo and Catherine Y. Nowak, *Designing a New Playbook for the New Paradigm: Global Securities Litigation and Regulation*, 4 (2011), <http://www.dandodiary.com/2011/12/articles/securities-litigation/designing-a-new-playbook-for-the-new-paradigm-global-securities-litigation-and-regulation/>.

⁴⁰⁴ HM Treasury, *A New Approach to Financial Regulation: Building a Stronger System*, at 60 (Feb. 20, 2011).



G. FRANCE

Overview

Class actions do not presently exist under French law. While there has been significant debate and discussion in France over the implementation of class actions, such a system has not yet been accepted by the French government. There are, however, limited restrictive methods for bringing representative actions that are discussed below.

Under French law, there is an “adversarial principle” (“principe du contradictoire”) that provides that each person involved in a lawsuit must have the right to appear in court and be heard. Those who oppose the introduction of an opt-out class action system argue that this principle would be violated if one claimant was able to represent the interests of a class.⁴⁰⁵ Another important principle in French law that does not support class actions is that “no one shall plead by proxy” (“Nul ne plaide par procureur”) meaning that no one may

represent the interests of other persons. Each plaintiff must set forth his own individual claims.⁴⁰⁶

The law does allow for a more restrictive form of collective representation called “action en representation conjointe,” or a common representation action.⁴⁰⁷ French law allows for consumer associations with governmental approval to take action in the collective interest of consumers. The approval must be granted by The Ministry of Economy and Finance. Even approved consumer associations may only bring collective actions when several consumers have sustained individual injuries caused by the same actor and have a “common origin.”⁴⁰⁸

⁴⁰⁵ Dominique de Combles de Nayves and Benoit Javaux, *The International Comparative Legal Guide to: Class & Group Actions 2011: A Practical Cross-Border Insight Into Class and Group Actions Work*, Global Legal Group, 83 (2011), www.iclg.co.uk/khadmin/Publications/pdf/3976.pdf.

⁴⁰⁶ David H. Kistenbroker, Alyx S. Pattison, Patrick M. Smith, *Recent Developments in Global Securities Litigation*, 1904 PLI Corp. 607 at 13 (2011).

⁴⁰⁷ CODE MONÉTAIRE ET FINANCIER [C.M.F.] arts. L. 452-1 & L. 452-2 (Fr.) available at <https://www.legifrance.gouv.fr/af-fichCodeArticle.do?cidTexte=LEGITEXT000006072026&idArticle=LEGIArticle000006654264&dateTexte=&categorieLien=cid> Dominique de Combles de Nayves and Benoit Javaux, *The International Comparative Legal Guide to: Class & Group Actions 2011: A practical cross-border insight into class and group actions work*, Global Legal Group, 83 (2011),

⁴⁰⁵ Veronique Magnier, *Class Actions, Group Litigation & Other Forms of Collective Litigation Protocol for National Reports: France*, 3(2007), available at http://globalclassactions.stanford.edu/sites/default/files/documents/France_National_Report.pdf.



French law allows for investor actions to be brought as common representation actions. Article L. 452-2 of the Monetary and Financial Code allows for an opt-in action “stipulating that if ‘in their capacity as investors, several . . . persons have suffered individual damage having a common origin through the actions of the same person . . . [a properly declared investor defense association] may, if it has been instructed by at least two of the investors concerned, sue for damages . . . on behalf of those investors.’”⁴⁰⁹ In order to qualify as an approved association for investor claims, the association must have an express purpose of representing investors in matters relating to investment products.

When bringing a collective action on behalf of investors, investor associations are prohibited from soliciting via television, radio or personalized letters. If an approved association brings an investor action, the judge may allow for the group to solicit powers of attorney from the investors to allow them to act on their behalf. If approved by the judge, the association may pursue advertising through the above-listed means.⁴¹⁰

If a common representation action is unsuccessful, the consumers or investors lose their right to sue on those claims. If the defendant is found liable, the award is divided among the injured claimants “since the only purpose of these actions is to get compensation for their individual injuries.”⁴¹¹

Prevalence of Investors’ Associations

It is unclear how widespread such associations are, or how often they bring the types of lawsuits authorized in Article L. 452-1. However, based on the dearth of press reports on such associations, it seems they do not play nearly as large a role in regulating

the French securities market as do securities class actions in the U.S.

A 2002 article in The Guardian profiles one such association, called Association pour la Défense des Actionnaires Minoritaires (“ADAM”), or Association for the Defense of Minority Shareholders.⁴¹² Founded in 1991 by an economist, ADAM’s mission is to protect the interests of minority shareholders, including through legal action. The article describes one of ADAM’s major successes as obtaining a court-ordered increase of the purchase price for minority non-voting preference shares in connection with a corporate takeover, after ADAM challenged the price as being unreasonably low.⁴¹³ Although such challenges are routine in the U.S., based on the article, it appears that ADAM’s lawsuit and subsequent victory were unprecedented in France. This suggests that such associations are not widespread, and that private, collective lawsuits on behalf of shareholders are relatively uncommon.

Loser Pays Model

France operates under the “loser pays” rule. Under French law, costs of litigation “shall be borne by the losing party.”⁴¹⁴ Throughout the course of the action, each party is responsible for its own attorney and expert fees. Under Article 700 of the French Code of Civil Procedure (CPC), the judge may order the losing party to pay for at least part of the successful party’s legal fees. In making this determination, the court will consider the financial resources of the losing party. Courts very rarely require individual plaintiffs or consumer associations to pay such fees when they have been unsuccessful in a case against a corporation. In practice, the “loser pays” rule is usually only applied to corporate defendants.⁴¹⁵

available at www.iclg.co.uk/khadmin/Publications/pdf/3976.pdf.

⁴⁰⁹ David H. Kistenbroker, Alyx S. Pattison, Patrick M. Smith, *Recent Developments in Global Securities Litigation*, 1904 PLI Corp. 607 at 13 (2011), citing to, CODE MONÉTAIRE ET FINANCIER [C.M.F.] arts. L. 452-1 & L. 452-2 (Fr.) available at http://www.kattenlaw.com/files/upload/Recent_Developments_in_Global_Securities_Litigation_2011.pdf.

⁴¹⁰ Veronique Magnier, *Class Actions, Group Litigation & Other Forms of Collective Litigation Protocol for National Reports: France*, 10 (2007).

⁴¹¹ *Id.*, 11.

⁴¹² The Guardian, *Collette, Adam and Goliath*, April 12, 2002, available at <http://www.theguardian.com/money/2002/apr/13/shares.moneyinvestments> (last visited April 29, 2016).

⁴¹³ *Id.*

⁴¹⁴ Combles de Nayves and Javaux, *The International Comparative Legal Guide to: Class & Group Actions 2011*, 88 (2011), available at <http://www.iclg.co.uk/khadmin/Publications/pdf/3976.pdf>.

⁴¹⁵ *Id.*



Opt-In vs. Opt-Out

French common representation actions require individual plaintiffs to opt in. In order for an association to bring an action on behalf of consumers or investors, each plaintiff must authorize the representation in writing.⁴¹⁶

As noted in the amicus brief filed by the European Aeronautic Defense & Space Co., N.V., Alstom SA, Lagardere Group SCA, Thales SA, Technip SA and Vivendi SA in *Morrison*, French opponents of an opt-out class action system argue that French constitutional principles of individual notice, consent, and party autonomy would be violated if absent class members were bound by an opt-out class judgment.⁴¹⁷

Jurisdiction

Article 42 of the French Code of Civil Procedure allows defendants to be sued where they are domiciled.⁴¹⁸ Thus, an action against a French company may be brought in France. As an alternative, defendants may also be sued where a contract is performed or a tort is committed.⁴¹⁹ The French Code Civile, under Articles 14 and 15, includes a specific provision for foreigners bringing actions in France. These Articles allow jurisdiction before French courts when a French citizen or company is a party to the action – whether plaintiff or defendant.⁴²⁰

Funding the Litigation - Contingent Fee Arrangements

Pure contingency fee arrangements, *i.e.*, having 100% of the fee contingent upon success, are illegal in France. The traditional form of payment to lawyers is based on either a fixed sum or an hourly rate

⁴¹⁶ *Id.* at 84.

⁴¹⁷ “Brief for the European Aeronautic Defense & Space Co., N.V., Alstom SA, Lagardere Group SCA, Thales SA, Technip SA and Vivendi SA,” *Morrison v. National Australia Bank Limited*, 2010 WL 719336 (U.S.), 28 (U.S., 2010).

⁴¹⁸ CODE DE PROCEDURE CIVILE {C. PROC. CIV.} art.42 (Fr.).

⁴¹⁹ C. PROC. CIV. art.46 (Fr.).

⁴²⁰ C. CIV. art. 14 (Fr.); C. CIV. art. 15 (Fr.); Andrew L. Strauss, Beyond National Law: The Neglected Role of the International Law of Personal Jurisdiction in Domestic Courts, 36 Harv. Int'l L.J. 373, 388 (1995).

basis. However, arrangements that permit otherwise acceptable fee structures, such as hourly or flat fees, to be adjusted based on outcome, are permitted.⁴²¹ Such fees are strictly monitored by French judges and can only represent a portion of the total fees.⁴²²

Third party funding is another possible method available in French litigation. Although Article 11.3 of the National Bar Association Rules requires that a lawyer be paid only by his client or client's agent, it is possible that third-party funding would be permitted if there is a contract with the plaintiff governing the funding and the plaintiff ultimately makes payments to his lawyers.⁴²³

Fraud on the Market Theory

There does not appear to be a definitive statute or ruling regarding the viability of the fraud-on-the-market theory in France. In *Morrison*, French companies submitted an *amicus brief* suggesting that it is not viable, citing *Société Eurodirect Marketing v. Pfeiffer*, no. 03-20600 (Cass. Com. Nov. 22, 2005). However, the theory was not actually discussed or even asserted in that case. Nevertheless, defendants argued that the plaintiff failed to show causation, and specifically, actual reliance (*i.e.* what would be called “transaction causation” in the U.S.), and there was no dispute that actual reliance was required.⁴²⁴ However,

⁴²¹ European Commission, Competition, Antitrust, Actions for Damages, Executive summary and overview of the national report for France, available at http://ec.europa.eu/competition/antitrust/actionsdamages/executive_summaries/france_en.pdf (last accessed May 2, 2016).

⁴²² Veronique Magnier, *Class Actions, Group Litigation & Other Forms of Collective Litigation Protocol for National Reports: France*, 21 (2007).

⁴²³ Article 11.3 of the National Bar Association Rules; Dominique de Combles de Nayves and Benoit Javaux, *The International Comparative Legal Guide to: Class & Group Actions 2011: A practical cross-border insight into class and group actions work*, Global Legal Group, 89 (2011), www.iclg.co.uk/khadmin/Publications/pdf/3976.pdf.

⁴²⁴ The French version of the affirmance is available at <https://www.legifrance.gouv.fr/affichJuriJudi.do?idTexte=JURITEXT000007498096> (last accessed April 29, 2016). The French version of the lower court's judgment is available at <https://www.legifrance.gouv.fr/affichJuriJudi.do?idTexte=JURITEXT000006943092> (last accessed May 5, 2016).



the court upheld the lower court's decision *in favor of the plaintiff*. The case does not affirmatively reject the fraud-on-the-market theory, and whether a French court would accept it appears to be a question that has not been squarely addressed by the French courts.

Pleading Standards

French pleading standards require that claims contain more factual support than the general pleading standards in America, and are more analogous to the pleading requirements for a Section 10(b) case under the Private Securities Litigation Reform Act. The emphasis is on informing the defendant of the claims against him. In France, the statement of claim must make an "*exposé des moyens*" or a "statement of the methods by which the claims will be proved."⁴²⁵ This statement should include any facts on which the plaintiff relies in stating his claim. A properly pled statement of claim must also include copies of all written evidence referred to by plaintiff. French pleading rules also state that the statement of the claim "*vaut conclusions*," or "merits conclusions," meaning that the allegations in the claim must be conclusive.⁴²⁶

Causes of Action in Securities Litigation

French shareholders may bring private securities actions. As "parties civiles," shareholders may bring or join criminal claims for securities violations. When the trial for criminal securities violations concludes, the judgment will include an award for both criminal and civil liability.⁴²⁷

As discussed above, there is no French equivalent to the American class action where private parties can bring securities claims on an aggregate basis. Because of the limitations on securities actions, including the lack of a fraud on the market theory and

the risk of an unsuccessful party's liability of legal fees, it is difficult for plaintiffs to bring individual securities actions. Such restrictions incentivize plaintiffs to allow regulatory bodies to bring their claims to first establish violation before any private action is brought.⁴²⁸

Regulatory Body for Securities

In France, securities regulation is governed by the *Autorité des Marchés Financiers ("AMF")* (*the "Financial Markets Authority"*). The AMF is France's equivalent to the U.S. Securities and Exchange Commission. It is responsible for "safeguarding investments, ensuring that issuers disclose material information, and supervising financial markets."⁴²⁹ The AMF also has created rules for securities of publicly-traded companies and reviews all disclosures by issuers of securities to verify that adequate information has been provided. The enforcement powers of the AMF include investigations of alleged securities fraud and sanctions for violations of AMF rules.⁴³⁰

Most recently, the French regulators have pursued investigation and enforcement charges for insider trading. The AMF brought insider-trading charges against French hedge fund, B&G, in July 2010. In February 2011, the AMF again filed insider trading charges against France's largest publisher.⁴³¹ From the perspective of many in France, regulatory bodies such as the AMF adequately regulate securities traded on French exchanges and interference by the United States regulators is unnecessary.⁴³²

⁴²⁸ "Brief for the European Aeronautic Defense & Space Co., N.V., Alstom SA, Lagardere Group SCA, Thales SA, Technip SA and Vivendi SA," *Morrison v. National Australia Bank Limited*, 2010 WL 719336 (U.S.), 28 (U.S.,2010).

⁴²⁹ *Id.* at 19.

⁴³⁰ *Id.* at 22 n. 20.

⁴³¹ Robert F. Carangelo, Paul A. Ferrillo and Catherine Y. Nowak, *Designing a New Playbook for the New Paradigm: Global Securities Litigation and Regulation*, 4 (2011).

⁴³² See, e.g., "Brief for the European Aeronautic Defense & Space Co., N.V., Alstom SA, Lagardere Group SCA, Thales SA, Technip SA and Vivendi SA," *Morrison v. National Australia Bank Limited*, 2010 WL 719336 (U.S.), 22 n. 20 (U.S.,2010) (asserting that "European nations have bristled at the idea that investors purchasing stocks on foreign exchanges will not be adequately protected from corporate fraud unless U.S. courts extend jurisdiction over their claims").

⁴²⁵ Peter F. Schlosser, Lectures on Civil-Law Litigation Systems and American Cooperation with Those Systems, 45 U. Kan. L. Rev. 9, 13 (1996) citing to Noveau Code de proc dure civile [N.C.P.C] art. 56(1), Nr. 2 (Fr.).

⁴²⁶ *Id.*

⁴²⁷ "Brief for the European Aeronautic Defense & Space Co., N.V., Alstom SA, Lagardere Group SCA, Thales SA, Technip SA and Vivendi SA," *Morrison v. National Australia Bank Limited*, 2010 WL 719336 (U.S.), 22 (U.S.,2010).



Recent Developments: The Aristophil Scandal

A recent French investment scandal sheds light on potential legal avenues for defrauded investors. Originating in the early 2000s, the scheme involved a collection of old manuscripts acquired by an organization called the “Aristophil Society,” with investors paying a fee of €1500 on the promise of 8% annual returns, ostensibly generated by rising manuscript values. In 2014, it was revealed to be a Ponzi-like scheme.

The French government seized approximately €100 million in assets, and defrauded investors were given a few months to file claims. However, there appear to be at least two other avenues of private action being pursued.

One is the Association de Défense des Investisseurs en Lettres et Manuscrits (ADILEMA), an Investors’ Defense Association under the regime described above.⁴³³ ADILEMA was created on March 4, 2015. Membership in ADILEMA costs €40, with retention of a law firm costing an additional €300.⁴³⁴ According to reports, it represents between 400 and 500 investors.⁴³⁵ It is unclear, however, what specific legal actions ADILEMA is currently pursuing.

Another potential avenue is an “*action conjointe*,” or “joint action,” specifically through a website created by the Paris Bar called “*Avocats Actions Conjointes*,” or Joint Action Lawyers.⁴³⁶ The legal authority for such actions appears to be rooted in traditional legal principles.⁴³⁷ However, technology has made it significantly easier for litigants to coordinate and connect with each other and with lawyers, and

thus easier for such actions to be conducted on a large scale.⁴³⁸

The Aristophil scandal is one of the listed cases on the website.⁴³⁹ According to the website, 1,639 individuals signed up to join before the March 31, 2016 deadline, at a cost of €3600 in attorneys’ fees, with an additional 15% of any monies recovered to be awarded to the attorneys.⁴⁴⁰

The joint action, which seeks €150 million in damages, is being brought not against Aristophil, but against two banks, Société Générale (SG) and Crédit Industriel et Commercial (CIC), for allegedly facilitating the fraud.⁴⁴¹ On February 29, 2016, the Paris court overseeing the €100 million in seized assets was reported to have partially denied a claim filed by SG to recover collateral on a loan it made to Aristophil in March of 2014, reportedly on the grounds that the court had doubts about SG’s good faith at that time, in part because of evidence that SG by then had knowledge that the scheme was fraudulent.⁴⁴² This presumably improves the prospects of the joint action.

⁴³³ ADILEMA’s website is <http://scandalearistophil.fr>.

⁴³⁴ See <http://scandalearistophil.fr/comment-recuperer-mon-argent/>.

⁴³⁵ See <http://www.ouest-france.fr/societe/justice/aristophil-floues-apres-avoir-investi-dans-des-manuscrits-3697327>.

⁴³⁶ <http://www.avocats-actions-conjointes.com>.

⁴³⁷ See <http://www.avocats-actions-conjointes.com/quest-ce-quune-action-conjointe> (explaining that joint actions are based on longstanding legal principles and statutes).

⁴³⁸ See Les Echos Business, *Avocats Actions Conjointes, quand l’Ordre facilite l’accès aux contentieux de masse*, Nov. 17, 2015, available at <http://business.lesechos.fr/directions-juridiques/avocats-et-conseils/choisir-son-avocat/avocats-actions-conjointes-quand-l-ordre-facilite-l-acces-aux-contentieux-de-masse-204753.php> (last accessed May 2, 2016)(profiling the website).

⁴³⁹ <http://www.avocats-actions-conjointes.com/affaire-aristophil>.

⁴⁴⁰ See *id.*

⁴⁴¹ See L’OBS, *Affaire Aristophil: des banques rattrapées par le scandale?*, October 29, 2015, available at <http://tempsreel.nouvelobs.com/justice/20151028.OBS8466/affaire-aristophil-des-banques-rattrapees-par-le-scandale.html> (last accessed May 2, 2016).

⁴⁴² cBanque, *La « bonne foi » de la Société Générale mise en doute dans l’affaire Aristophil*, March 10, 2016, available at <http://www.cbanque.com/actu/56930/la-bonne-foi-de-la-societe-generale-mise-en-doute-dans-affaire-aristophil> (last accessed May 2, 2016).



H. GERMANY

Overview

Germany has a civil law system. It does not provide for class action lawsuits or comprehensive discovery rules. However, over the past years Germany has slowly started to develop first signs of a mass litigation culture.

Since the late 1990's there has been a growing awareness, particularly in securities law, that mass litigation requires specific regulations.⁴⁴³ This and the frustration of plaintiffs and courts over the Deutsche Telekom litigation has led to the Capital Markets Model Case Act or *Kapitalanleger-Musterverfahrensgesetz*⁴⁴⁴ (the "KapMuG").⁴⁴⁵ The KapMuG was initially adopted in 2005 to allow quasi-class actions for securities fraud cases only. The law was originally expressly intended as an experiment in class action lawsuits and included a sunset provision with an expiration of 2012, unless it was renewed.⁴⁴⁶ Since then, the KapMuG has been renewed through 1 November 2020. Further, it has been improved in several ways.⁴⁴⁷ The most significant improvements are:

⁴⁴³ Hess, in: Kölner Kommentar zum KapMuG, 2nd Ed. 2014, Introduction rec. 1.

⁴⁴⁴ *Id.* rec. 19.

⁴⁴⁵ An English translation of the KapMuG is available here: http://www.gesetze-im-internet.de/englisch_kapmug/index.html.

⁴⁴⁶ Hess *supra* at note 435, Introduction rec. 1. rec. 2.

⁴⁴⁷ Peter Bert, *KapitalanlegerMusterverfahrensgesetz: Looks As Though It's Here To Stay*, Dispute Resolution in Germany, October 15, 2011, available at <http://www.disputeresolutiongermany.com/2011/10/kapitalanlegermusterverfahrensgesetz-looks-as-so-it%e2%80%99s-here-to-stay/> (last accessed May 13, 2016).

(1) The extension of the scope of claims that fall under the KapMuG; now including claims against certain intermediaries such as brokers and investment advisers, who use incorrect capital market information, *e.g.* in a prospectus;⁴⁴⁸

(2) Lower requirements for collective settlements (see below addressing the "Basics of Filing a Claim and Litigation" and "Collective Settlement");

(3) Easier participation by mere registration of claims; and

(4) The shifting of jurisdiction from the Regional Courts (where the individual cases are tried) to the Higher Regional Court (where the model case proceeding take place).⁴⁴⁹

However, the KapMuG still is not a "class action" as in the U.S. system and it is limited in scope to certain claims made by investors.

According to the electronic Federal Gazette (*Elektronischer Bundesanzeiger*), as of May 2015, there have been over 40 model case proceedings since the introduction of the KapMuG in 2005. The figures

⁴⁴⁸ Hess *supra* at note 435., Introduction rec. 22.

⁴⁴⁹ For an overview of the development of the KapMuG, see Burkhard Schneider and Heiko Heppner, *KapMuG Reloaded – das neue Kapitalanleger-Musterverfahrensgesetz*, Betriebsberater 2012, 2703, *et seq.*; Hess, in: Kölner Kommentar zum KapMuG, 2nd Ed. 2014, Introduction rec. 21, *et seq.*



for the most recent years show the growing acceptance of model proceedings under the KapMuG, particularly after the renewal and amendment in 2012. Amongst the most prominent cases are the *Deutsche Telekom* case and the case against Daimler AG (both initiated 2006). As of Spring 2016, the applications for model proceedings against Volkswagen AG relating to the alleged emissions testing manipulations are at the center of German media attention.⁴⁵⁰

Furthermore and irrespective of the KapMuG, it has become more and more common in Germany to conduct mass proceedings by bundling a large number of claims against one defendant into one action.

Punitive damages in civil cases are still not permitted by German law. Generally, German law only compensates a plaintiff for the economic loss he has actually suffered.⁴⁵¹

Basics of Filing a Claim and Litigation

The KapMuG is designed to streamline securities litigation proceedings in cases with a large number of individual claims. It provides for identical issues of law and fact to be extracted from these individual claims in order to be finally determined in a single model case proceeding before the Higher Regional Court. During the model case proceeding, all individual proceedings concerning the same subject matter are stayed. The legal and factual findings in the model case proceedings are binding not only on the model plaintiff but on all plaintiffs in the respective complex of disputes who either filed a claim (with or without applying for model case proceedings) or registered later under the new Sec. 10 Para 2 KapMuG. Hence, if a model claim proceeding is initiated in a series of disputes, all plaintiffs will be impacted by the rulings.

Model case proceedings under the KapMuG operate in three stages: (i) the initiation of the model case proceedings; (ii) the actual model case

proceedings at the Higher Regional Court; and (iii) the subsequent continuation of the individual proceedings. Furthermore, the KapMuG stipulates the possibility of a collective settlement.

Initiation of Model Case Proceedings

KapMuG proceedings are based on individual securities litigation claims filed with the court of first instance. A party wishing to initiate a model case proceeding must apply to this court of first instance for the establishment of a model case. This application can be filed by the plaintiff or by the defendant (the plaintiff, however, can already combine such application with the filing of the claim). The application must set out the legal and factual issues to be determined by way of the model case proceeding as well as the underlying facts and the supporting evidence. Furthermore, it must demonstrate that these issues may have significance for other similar cases beyond the individual dispute concerned.⁴⁵² The court shall then decide on the admissibility of any model case application within 6 months and publish any admissible applications in a claims register.⁴⁵³

Once a total of ten applications referring to the same complex of disputes have been published in the claims register, the determination of the legal and factual issues included in applications is transferred to the Higher Regional Court by way of a court order.⁴⁵⁴ Once this court order is published in the claims register, all individual proceedings in this complex of disputes are stayed.⁴⁵⁵

The Model Case Proceeding at the Higher Regional Court

In a first step, the Higher Regional Court designates the model plaintiff upon its own discretion. However, it shall consider the following points in its decision:⁴⁵⁶

- The suitability of the plaintiff to consider the in-

⁴⁵⁰ See *infra* Section IV (Volkswagen AG (Germany, the United States, and the Netherlands)).

⁴⁵¹ Oetker, in: *Münchener Kommentar zum BGB*, 7th Edition

2016, Sec. 249 rec. 8, *et seq.*

⁴⁵² Sect. 2 KapMuG.

⁴⁵³ Sect. 3 KapMuG.

⁴⁵⁴ Sect. 6 KapMuG.

⁴⁵⁵ Sect. 8 KapMuG.

⁴⁵⁶ Sect. 9 KapMuG.



terests of all similarly-situated plaintiffs in the conduct of the model case proceedings;⁴⁵⁷

- Agreements among several plaintiffs on who shall be the model plaintiff (if applicable); and
- The amount in dispute as filed for by the (potential) model plaintiff.

Upon designation of the model plaintiff, the Higher Regional Court shall publicly announce, among other things, the model plaintiff, the model defendant and the file number of the model case proceeding. Within a period of six months after this public announcement, any plaintiff who has not already filed an individual claim, can register its claim in writing with the Higher Regional Court.⁴⁵⁸ However, the six month period for claims registration does not toll any applicable limitations periods. In other words, it is possible that the model case proceedings will be publicly announced with less than six months available for would-be claimants to act before the expiration of the statute of limitations that would bar the claimant from pursuing claims. If a claimant “registers” a claim instead of filing a complaint, the registration will toll the statute of limitations but the claimant must convert the registration to an active case (by filing a complaint) before the KapMuG reaches a conclusion if the claimant wants to be bound by the result.⁴⁵⁹

While the model claim proceeding is conducted by the model plaintiff, plaintiffs not selected as model plaintiff, are not excluded from acting in the model case proceeding. Rather, they can participate as a so-called “interested party.” As such, they have a position similar to a co-plaintiff and can generally plead their own case in the model case proceeding,⁴⁶⁰ for more details, please see below under “Opt-In vs. Opt-Out”). There are no particularities with respect to the taking of evidence in the model case proceeding. And, as noted above, there are no provisions for discovery.

⁴⁵⁷ However, the model plaintiff acts neither as representative of the other plaintiffs nor on their behalf, cp. Hess, in: Kölner Kommentar zum KapMuG, 2nd Ed. 2014, Sec. 9 rec. 70.

⁴⁵⁸ Sect. 10 KapMuG.

⁴⁵⁹ <https://www.expertguides.com/articles/collective-redress-in-germany/collec14>.

⁴⁶⁰ Sect. 14 KapMuG.

The legal and factual issues brought before the Higher Regional Court for determination can be expanded in the course of the model case proceeding.⁴⁶¹

The Higher Regional Court’s final decision by which it determines the relevant legal and factual issues is made by way of a court order which is called the model case ruling.⁴⁶² The model case ruling can be challenged by an appeal to the Federal Supreme Court only as to points of law.⁴⁶³

Continuation of the Individual Proceedings

Once the model case ruling is final, the individual proceedings are recommenced as soon as one party has submitted the final model case ruling to the court of first instance. From that point on, the case is tried by the first instance court based on the findings set out in the model case ruling (except, as discussed below, with respect to plaintiffs who pleaded adversely to the model plaintiff).

Collective Settlements

A major point of criticism with respect to the old KapMuG centered on the regulations on settlement. They required consent of all interested parties. Commentators pointed out that this made it virtually impossible to settle a case.⁴⁶⁴ In the course of the last amendment of the KapMuG, these regulations have been changed.⁴⁶⁵ Now, non-model plaintiffs can opt-out of any settlement agreed between the model plaintiff and the model defendant (and approved by the court). However, the approved settlement shall

⁴⁶¹ Sect. 15 KapMuG.

⁴⁶² Sect. 16 KapMuG.

⁴⁶³ Sect. 20 KapMuG.

⁴⁶⁴ Louise Moher and Lynda Morgan, in: *Germany: Multi-Party Litigation In Germany: The KapMuG In Action*, Class Actions, Federal Press., Spring 2008, last updated January 10, 2012, available at <http://www.mondaq.com/x/160298/Class+Actions/MultiParty+Litigation+In+Germany+The+KapMuG+In+Action> (last accessed May 13, 2016); Carl Karlsgodt, *Notes from the 5th Annual Conference on the Globalization of Class Actions and Mass Litigation, Session 3 – Managing the Mass*, ClassActionBlawg, December 27, 2011, available at <http://classactionblawg.com/2011/12/27/notes-from-the-5th-annual-conference-on-the-globalization-of-class-actions-and-mass-litigation-session-3-managing-the-mass> (last accessed May 13, 2016).

⁴⁶⁵ Sect. 17, *et. seq.* KapMuG.



take effect if less than 30 per cent of the participants in the model case proceeding opt-out. If the settlement becomes effective, the cases of any withdrawing plaintiffs continue in first instance in their individual proceedings.⁴⁶⁶

Loser Pay Model

The losing party must pay all litigation costs, including court costs and the opposing party's attorney fees.⁴⁶⁷ Costs are distributed proportionally if a party partially wins.⁴⁶⁸

Particularly in large cases, court fees and adverse cost risk in German proceedings are limited and rather predictable:

- (1) While clients and attorneys may agree to different pricing models for attorney fees (negotiated hourly rates being the most common pricing model), the reimbursement of attorney fees is limited to statutory attorney fees under the Law on the Remuneration of Attorneys (*Rechtsanwaltsvergütungsgesetz*).
- (2) Both court fees and statutory attorney fees are
 - Flat fees based on the amount in dispute; and
 - The amount in dispute applicable for fee calculation is capped at EUR 30 million.

Accordingly, bundling claims can be a cost efficient way to pursue Securities Litigation in Germany. The aforementioned cap is generally also applicable if several claims of different plaintiffs are bundled into one action. Still, it needs to be analysed how the bundling of several claims might affect the prospects of success and/or the time line for each individual case.

For an action with a value in dispute of EUR 30 million or more, in the first instance

- The court fees are approx. EUR 330,000 (payable in advance by plaintiff); and
- The adverse cost risk with respect to attorney fees is approximately EUR 230,000 (plus 19% VAT) for a case involving one defendant where the parties are required to participate in an oral hearing.

Non-EU plaintiffs have to provide a security for the defendant's possible claim for reimbursement of costs for at least two instances if the defendant makes an application for cost security. In a model case proceeding, the adverse cost liability is distributed among all the plaintiffs (even those whose cases are stayed) on a pro-rata basis.

Opt-In vs. Opt-Out

The KapMuG is neither "opt-in" nor "opt-out." Plaintiffs do not have a choice whether they want to *join* the model case or not. Rather, once an individual plaintiff has filed a lawsuit on which a model case proceeding has already been established, all other plaintiffs are statutorily included as an "interested party" to the model case. Those plaintiffs are automatically bound by the model case ruling regardless of whether they decide to participate in the model case proceeding or not.

However, KapMuG provides limited measures to release plaintiffs from the binding effect of the model case ruling. In order to take these measures, plaintiffs have to participate in the model case proceeding. By doing so, they get a position similar to a co-claimant which enables them to plead their own case. For example, they can

- File their own briefs;
- Bring forward their own evidence; and
- Attend the oral hearing and plead in front of the court.

This generally includes pleading adversely to the model plaintiff. In the model case proceedings, such adverse pleadings will not be heard and the

⁴⁶⁶ If the settlement becomes effective, the cases of any withdrawing plaintiffs continue in first instance in their individual proceedings.

⁴⁶⁷ Zivilprozeßordnung [ZPO] (German Civil Procedure Code), Sec. 91.

⁴⁶⁸ *Id.* Sec. 92.



positions of the model plaintiff will prevail. However, with respect to the model case ruling, it results in a kind of a partial opt-out. Any issues to which a plaintiff pleaded adversely will be determined in the plaintiff's subsequent individual proceedings regardless of the findings in the model case ruling on these issues.

Apart from that, the effects of the model case proceedings can only be avoided if the model claimant and the model defendant have agreed on a settlement. Since the latest revision of the KapMuG, any plaintiff can opt-out of such settlement and proceed with his claim individually.

This demonstrates that despite the lack of a general opt-out provision, the KapMuG allows for the protection of the non-model plaintiffs' individual interests. In order to ensure that non-model plaintiffs make best use of their rights under the KapMuG, it seems advisable for any plaintiff to seek individual representation in KapMuG proceedings. This is particularly the case for plaintiffs with very high losses.

Extraterritorial Jurisdiction

The extraterritorial jurisdiction for claims for compensation of damages appears to be limited. The various statutes under which a claim may be made under the KapMuG usually refer to securities traded on a German stock exchange, traded on the free market, or admitted to trading on an organized market in another Member State of the European Union or in another of the Contracting States to the Agreement on the European Economic Area.⁴⁶⁹

Funding the Litigation – Contingent Fee Arrangements

Contingent fees are generally prohibited under German law. The only and very limited exception are cases in which the client otherwise would be inhibited from taking legal actions due to its economic situation (Sec. 4a Law on the Remuneration of Attorneys (*Rechtsanwaltsvergütungsgesetz*)).

⁴⁶⁹ Securities Trading Act (*Wertpapierhandelsgesetz* – WpHG), available at https://www.bafin.de/SharedDocs/Aufsichtsrecht/EN/Gesetz/WpHG_en.html (last accessed May 13, 2016); see also cp; Fuchs, in: Fuchs, WpHG, rec. 89, *et seq.*

In contrast, litigation funding is allowed in Germany, and without regulation. In its latest 2014 overview, the German Bar Association listed 17 providers and their main terms.⁴⁷⁰ German litigation funders usually cover all costs of the proceedings, including the liability for adverse costs, since, under the German statutory fee schedules, these can be predicted with great accuracy in most cases (see above regarding the "Loser Pay Model"). In larger cases, the fee of the German funders usually ranges between 20 to 30 percent of the proceeds from the claim. Recently, also Anglo-American funders have started to be more visible in the German market in particular in large scale security litigations cases.

Fraud On The Market Theory

Germany does not yet recognize a "fraud-on-the-market" theory. However, under Sections 37(b) & (c) of the German Securities Trading Act (WpHG), an investor does not need to prove individual reliance in order to be eligible to recover damages from issuers of financial instruments who make false or misleading ad-hoc announcements or who fail to disclose inside information by way of a mandatory ad-hoc announcement.⁴⁷¹

In order to be eligible for damages, an investor must be economically affected by such incorrect or omitted ad-hoc announcements. For example, in case of failure to publish inside information which has an adverse effect on the issuer's share price (Sec. 37(b) Para. 1 no. 1 WpHG), the issuer is liable to an investor if

- The investor acquired the issuer's shares after the issuer's obligation to make an ad-hoc announcement existed; and

⁴⁷⁰ Overview of litigation funders in Germany, German Bar Association, September 2014, available at <http://anwaltverein.de/files/anwaltverein.de/downloads/praxis/Verguetungsrecht/Uebersicht%20Prozessfinanzierer-Stand%20209%2009%2014.pdf> (last accessed May 17, 2016).

⁴⁷¹ Sec. 37(b) and (c) WpHG only apply to ad-hoc announcements; Sec. 826 German Civil Code (BGB) is applicable for other incorrect or misleading statements; the requirements of Sec. 826 BGB are considerably stricter than those under Sec. 37(b) and (c) WpHG; e.g., according to the Federal Supreme Court Sec. 826 BGB requires reliance.



- The investor was still holding the shares when negative insider information later became public.

In such case, the investor has acquired the shares at an inflated price and later suffered a loss from the correction in the share price when the negative insider information became public. Accordingly, the investor is entitled to damages in the amount of the difference between

- The price actually paid for the shares; and
- The hypothetical correct share price if the ad-hoc announcement had duly been made.

According to the German Supreme Court, such a damage claim does not require reliance.⁴⁷² Although individual reliance is not required, it is disputed among German commentators whether the investor must still prove loss causation.

However, the German Supreme Court furthermore set out that under Sec. 37(b) Para. 1 no. 1 WpHG, an investor can alternatively claim for rescission of the acquisition of the shares. In this case however, reliance is required.⁴⁷³

Finally, under the recently amended regime for the statute of limitation, claims under Sec. 37(b) and (c) WpHG are time-barred after three years. This limitation period starts at the end of the year in which (i) the claim came into existence; and (ii) the investor obtained knowledge of the circumstances giving rise to the claim and of the identity of the obligor, or would have obtained such knowledge if he had not been grossly negligent.

Pleading Standards

German pleading standards are strict. In Germany, the initial statement of claim occupies a place of central importance. Generally, it is an extensive and detailed paper as the German system requires specific

fact pleading and also requires a party to designate the means of proof for each factual assertion in the pleadings (for example, by identifying documents and witnesses). As a result, German litigation is rather front loaded with most of the fact finding taking place prior to the filing of the initial statement of claim.

Standard of Proof

German law has a subjective standard of proof. In order to prove a factual allegation in a German court, the judge has to be convinced that the allegation is true.⁴⁷⁴ In making this determination, the judge has to evaluate all pleadings and all evidence presented in the proceedings and must not ignore the laws of logic, physics and thought.

Causes of Action in Securities Litigation

The scope of the KapMuG is expressly set out in Sec. 1 KapMuG.

In general terms, the causes of actions that fall under the KapMuG are:

- (1) Claims for compensation of damages due to

- False, misleading or omitted public capital markets information;
- The use of such information; and
- The failure to clarify such information.

The most common claims comprised by this regulation are (i) claims under Sec. 37(b) and (c) of WpHG (communication of insider information); (ii) tort claims under Sec. 826 of the German Civil Code in relation to the communication of capital markets information; and (iii) prospectus liability claims under the Securities Prospectus Act and the Capital Investment Act.

- (2) Claims to fulfilment of a contract, which is based on an offer under the Securities Acquisition and Takeover Act.

⁴⁷² Cp. German Supreme Court in: NJW 2012, 1800-1807; decision dated 13 Dec 2011, File-No. XI ZR 51/10, recitals 47 to 58.

⁴⁷³ Cp. German Supreme Court in: NJW 2012, 1800-1807; decision of 13 Dec 2011; File-No. XI ZR 51/10; recitals 67.

⁴⁷⁴ Cp. Greger, in: Zöller, 31st Ed. 2016, before Sec. 284, recital 1; and Sec. 286 recital 17, *et seq.*



In practice, these kinds of claims have not been of any relevance among the KapMuG proceedings initiated so far.

Regulatory Environment for Securities Litigation

On May 1, 2002, the Federal Banking Supervisory Office (*Bundesaufsichtsamt für das Kreditwesen* – BAKred) was merged with the then Federal Securities Supervisory Office (*Bundesaufsichtsamt für den Wertpapierhandel* – BAWe) and Federal Insurance Supervisory Office (*Bundesaufsichtsamt für das Versicherungswesen* – BAV) to become the Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht* – BaFin). The BaFin is responsible for the supervision of Banking, Insurance and Securities.⁴⁷⁵

The basis for the fledgling Securities Supervisory Office's duties was the Securities Trading Act (*Wertpapierhandelsgesetz* – WpHG)⁴⁷⁶ – an important element of the Second Financial Market Promotion Act – most of which became effective on 1 January 1995. Under this Act the Supervisory Office was charged with ensuring the integrity and transparency of the German capital market – by combating and preventing insider trading, by monitoring ad hoc disclosure by listed companies and the disclosure requirements applying to changes in voting rights in listed companies and by monitoring compliance with the codes of conduct applying to investment services firms – all in the name of improved investor protection.

Almost all of the provisions of the Securities Trading Act are based on European Directives. The Act has therefore been amended and adapted to take into account developments in the securities markets on a number of occasions by now. For instance, the Third Financial Market Promotion Act, which came into force in 1998, increased BAWe's existing rights to obtain information in connection with investigations

into insider trading and extended the notification requirements applying to holders of voting rights in listed companies. In January 2002 the Securities Acquisition and Takeover Act (*Wertpapiererwerbs- und Übernahmegesetz* – WpÜG)⁴⁷⁷ gave the Supervisory Office the job of monitoring company takeovers for the first time ever. Another change was brought in by the Fourth Financial Market Promotion Act of 2002. For instance, since then the securities regulator has also been responsible for monitoring the prohibition on price and market manipulation and oversees the notification and disclosure of directors' dealings. In addition, the provisions relating to the misuse of ad hoc announcements for advertising purposes and the publication of false information have been strengthened.

However, under the WpHG and the WpÜG, the BaFin not only monitors (and, in cases of indications of irregularities, investigates) but also has regulatory responsibilities in another important field relating to securities litigation: in Germany, securities and other investment products generally require a prospectus in order to be offered to the public for sale. The mandatory approval procedure for these prospectuses is again carried out by the BaFin.

From 1 January 2016, large parts of the BaFin are being reorganised, partly as a result of new duties in areas such as consumer protection. However, apart from consumer protection, another main task of the Federal Financial Supervisory Authority is anti-money laundering. This will be based in the Banking Supervision directorate since it has a large area of connection with anti-money-laundering.

⁴⁷⁵ History of BaFin, available at http://www.bafin.de/EN/DieBaFin/AufgabenGeschichte/Wertpapieraufsicht/securitiessupervisionassetmanagement_node.html (last accessed May 13, 2016).

⁴⁷⁶ The Securities Trading Act (WpHG) is available at http://www.bafin.de/SharedDocs/Aufsichtsrecht/EN/Gesetz/WpHG_en.html (last accessed May 24, 2016).

⁴⁷⁷ Securities Acquisition and Takeover Act (WpÜG) is available at <https://www.voeb.de/de/publikationen/fachpublikationen/publikation-wertpapiererwerbsgesetz.pdf> (last accessed June 14, 2016).

I. INDIA



Overview

Class action suits were introduced into Indian law in August 2013 with the passage of Section 245 of the Companies Act of 2013 (the “Companies Act”).⁴⁷⁸ The Companies Act is administered by the Ministry of Corporate Affairs in India.⁴⁷⁹ Under the Companies Act, shareholders are permitted to file an application with the National Company Law Tribunal stating that the management of the affairs of a company are being

carried out in a way that is harmful to a company’s interests.⁴⁸⁰ Shareholders may bring suit for damages against the company or directors for fraudulent or unlawful acts or omissions.⁴⁸¹ A class action suit may also be brought against an auditor or expert seeking damages for improper or misleading statements contained within their respective professional reports.⁴⁸² Similar to the United States, India has adopted a procedure to consolidate similar cases and appoint a lead applicant.⁴⁸³

⁴⁷⁸ The Companies Act, 2013, § 245, Acts of Parliament, 2013 (India).

⁴⁷⁹ Satwinder Singh, Rupa Radhakrishnan, and Rankika Kapoor, *Securities Law In India, International Securities Law Handbook* (World Law Group 2010).

⁴⁸⁰ Siddharth Acharya, *Class Action Suits: Shareholder activism or wolf pack activism?*, available at <http://indiaincorporated.com/item/4401-class-action-suits-shareholder-activism-or-wolf-pack-activism.html> (last accessed May 1, 2016).

⁴⁸¹ Companies Act § 245(g)(i).

⁴⁸² *Id.* § 245(g)(ii and iii).

⁴⁸³ *Id.* § 245(5)(b).



Paying for the Litigation

In India, attorneys are barred from accepting cases on a contingency fee basis.⁴⁸⁴ However, third-party funding of litigation is not prohibited.⁴⁸⁵ Indian courts may also direct costs against a party for filing a frivolous or vexatious claim or defense.⁴⁸⁶

Securities Litigation in India: The Satyam Scandal

Prior to the Companies Act of 2013, Indian law lacked a definition for securities fraud.⁴⁸⁷ The definition of securities fraud was borrowed from contract law (specifically, the Indian Contract Act of 1872); however, this legislation failed to discuss the intricacies of securities transactions.⁴⁸⁸ In the 1990s, there was a booming corporate sector in India that brought with it a rise in corporate fraud. An instance of corporate fraud that necessitated more legislation to address securities fraud in India involved Satyam Computer Services Ltd. (“Satyam” or the “Company”). Satyam was a rapidly growing company in the 1990s that offered IT and business outsourcing services in India and other countries.⁴⁸⁹ In January 2009, Satyam’s Chairman and Founder, Mr. B. Ramalinga Raju, revealed that the Company’s accounting had been manipulated for years.⁴⁹⁰ Mr. Raju admitted to overstating the Company’s assets by approximately U.S. \$1.47 billion and underreporting liabilities on the Company’s balance sheet.⁴⁹¹ Investors lost

approximately U.S. \$2.82 billion as a result of the Satyam scandal.⁴⁹²

Cases were filed against the Company and officers and directors in the United States on behalf of purchasers of Satyam common shares traded in India as well as purchasers of American Depository Shares on the New York Stock Exchange.⁴⁹³ In India during this time, there existed no mechanism for investors to seek recovery of damages incurred as a result of securities fraud. The Securities and Exchange Board of India (“SEBI”), an entity responsible for protecting investors’ interests in the securities markets,⁴⁹⁴ brought claims against Satyam in India.⁴⁹⁵ On July 15, 2014, SEBI issued an order against Satyam’s founder that forced him to return over U.S. \$306 million (as well as U.S. \$201 million in interest) and prevented many of Satyam’s executives from trading securities for a period of 14 years as a result of the scheme to defraud the Company.⁴⁹⁶

Following the revelation of fraud at Satyam and the aftermath of other incidents of corporate fraud in India dating back to the 1990s, the Indian legislature passed the Companies Act. Section 37 of the Companies Act introduced an avenue for filing a securities claim by persons “affected by any misleading statement or the inclusion or omission of any matter in the prospectus.”⁴⁹⁷

Corporate Governance in India

Historically, Indian law lacked strong corporate governance principles. Following the fallout in *Satyam*, in 2009, the Ministry of Corporate Affairs addressed many corporate governance issues, including the independence of directors, the roles and responsibilities of audit committees and the boards of companies, and whistleblower policies. The Companies Act imposed

⁴⁸⁴ Bar Council of India Rules of the Advocates Act 1961, Rule 20 ch. II pt. IV, available at <http://www.barcouncilofindia.org/wp-content/uploads/2010/05/BCIRulesPartVonwards.pdf> (last accessed May 6, 2016).

⁴⁸⁵ *Third Party Funding In Asia* (Nov. 8, 2015), available at <https://international-arbitration-attorney.com/third-party-funding-in-asia/>.

⁴⁸⁶ Companies Act § 245(5).

⁴⁸⁷ Pritha Chatterjee, *Securities Fraud and Class Action Suits in India: Need for Legislative Riders In Clause 216 of the Companies Amendment Bill 2009*, 284 Co. Law. (2011).

⁴⁸⁸ *Id.*

⁴⁸⁹ Madan Lal Bahasin, *Corporate Accounting Fraud: A Case Study of Satyam Computers Limited*, 2 Sci. Res. Open J. of Acct., 26, 29 (2013).

⁴⁹⁰ *Id.* at 30.

⁴⁹¹ *Id.*

⁴⁹² *Id.* at 32.

⁴⁹³ The claims relating to common shares were ultimately dismissed after the U.S. Supreme Court’s ruling in *Morrison*. See *In re Satyam Comput. Servs. Ltd. Sec. Litig.*, 915 F. Supp. 2d 450 (S.D.N.Y. 2013).

⁴⁹⁴ Singh, et al., *supra* note 479.

⁴⁹⁵ Bahasin, *supra* note 480, at 33.

⁴⁹⁶ Order in the matter of *Satyam Computer Services Ltd.*, WTM/RKA/SRO/64-68, dated July 15, 2014.

⁴⁹⁷ Companies Act, § 37.



strict regulations on companies including, among other things, a mandate for independent directors, who do not have a material or pecuniary relationship with the company;⁴⁹⁸ a provision that requires that the board of a company must consist of at least one-third of independent directors;⁴⁹⁹ and a requirement that a majority of the directors on a public company's audit committee must be independent directors.⁵⁰⁰

Liability for Securities Fraud

India imposes civil and criminal liability for securities fraud relating to the issuance of a prospectus that contains untrue statements.⁵⁰¹ For example, under the Companies Act, a company and every person who knowingly issues a prospectus “without the consent of an expert who is connected with formation or management of the company”⁵⁰² can receive a fine of up to INR 50,000 (approximately U.S. \$740). Criminal penalties can include imprisonment for up to two years or fines up to INR 50,000, or both for any person who “authorizes the issue of a prospectus containing a misstatement or an untrue statement.”⁵⁰³

Expansion of Insider Trading Regulations Under Indian Law

In May 2015, India expanded its securities regulations with respect to insider trading through its adoption of the SEBI Prohibition of Insider Trading Regulations (the “Insider Trading Regulations”).⁵⁰⁴ Pursuant to the Insider Trading Regulations, individuals and entities that have access to a company’s unpublished financial information are prohibited from trading in that company’s stock.⁵⁰⁵

Listed companies in India are responsible for adopting the Insider Trading Regulations.⁵⁰⁶

Through the Insider Trading Regulations, the definition of “insider” was broadened to include persons connected on the basis of being in any contractual, fiduciary, or employment relationship that allows such people access to unpublished price sensitive information (“UPSI”).⁵⁰⁷ Companies are now required to disclose UPSI on a regular basis before trading.⁵⁰⁸

Foreign Investment Procedures in India

Historically, investment procedures in India made it more difficult for institutional investors to gain access to Indian markets and investment vehicles than it was for local investors. To address the issues faced by foreign institutional investors, the Working Group on Foreign Investment in India (the “Working Group”) was created in November 2009.⁵⁰⁹ The Working Group made several recommendations to the Indian Government to address the concerns of foreign institutional investors, including the implementation of single window registration, the elimination of the practice of classifying foreign institutional investors, foreign venture capital investors, or non-resident Indians as separate investor classes, and the general elimination of investment regulations that distinguish between investor classes.⁵¹⁰ In 2013, SEBI approved the recommendations and later implemented the regulations.⁵¹¹

⁴⁹⁸ *Id.* § 149(6)(c).

⁴⁹⁹ *Id.* § 149(4).

⁵⁰⁰ *Id.* § 177.

⁵⁰¹ Singh, et al., *supra* note 479.

⁵⁰² *Id.*

⁵⁰³ *Id.* at 302.

⁵⁰⁴ Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015

⁵⁰⁵ Nishant Singh & Vaibhar Ganjlwale, *New insider trading regulations: wouldn’t be more*, May 21, 2015, available at <http://www.vccircle.com/news/others/2015/05/21/new-insider-trading-regulations-wouldn%E2%80%99t-be-more> (last accessed May 24, 2016).

⁵⁰⁶ Kenneth A. Cutshaw & Rohit Kochhar & Co., *Corporate Counsel’s Guide to Doing Business in India* § 8:30 (3d, 2014-2015 ed. 2014).

⁵⁰⁷ Firstpost, *SEBI tightens insider trading rules, expands definition of ‘insider’*, Nov. 20, 2014, available at http://www.firstpost.com/printpage.php?idno=1996881&sr_no=0 (last accessed May 24, 2016).

⁵⁰⁸ *Id.*

⁵⁰⁹ Nikhil Suresh Pareek & Soham Banerjee, *Streamlining of foreign portfolio investment in India: policy regime of SEBI (Foreign Portfolio Investors) Regulations*, I.C.C.L.R., 360 (2014).

⁵¹⁰ *Id.*

⁵¹¹ *Id.* at 363.



REITs: Investment Vehicle for Institutional Investors

Real Estate Investment Trusts (“REITs”) have been used for years as investment vehicles in countries such as the United States and Australia. In India, REITs have only recently been permitted.⁵¹² REITs are funds that purchase and manage real estate and mortgages.⁵¹³ The money is pooled from investors into various investment categories. Investors obtain units in the REIT and their returns are based on the proportion of units held by each investor.⁵¹⁴ Some advantages of REITs include that they are significantly liquid as opposed to ordinary real estate, they allow for participation in non-traditional residential properties, such as hotels, and they do not require a minimum investment.⁵¹⁵

In the past, investments in India’s real estate assets were outside the reach of the financial markets.⁵¹⁶ In the last several years, however, India has seen a significant growth in its real estate market, which has set the stage for REITs as a viable investment vehicle.⁵¹⁷ REITs have become a flourishing foreign investment in India particularly in light of the recent implementation of new regulations including the Real Estate Investment Trusts SEBI Regulations of 2014⁵¹⁸ and tax incentives that have reduced tax burdens.⁵¹⁹ For example, in February 2016, the finance minister of India removed the dividend distribution tax on REITs, which will facilitate REIT investment.⁵²⁰

⁵¹² Abhirup Ghosh & Amit Kumar, *Institutionalizing Real Estate Investments: The Emerging REIT Regime in India*, 5 Asian Bus. L. 77, 79 (2010).

⁵¹³ *Id.* at 79.

⁵¹⁴ *Id.* at 81.

⁵¹⁵ *Id.* at 80.

⁵¹⁶ *Id.* at 81.

⁵¹⁷ Kailash Babar, *Budget 2016 clears DDT hurdle in making REITs reality in India*, Feb. 29, 2016, available at <http://economictimes.indiatimes.com/wealth/real-estate/budget-2016-clears-ddt-hurdle-in-making-reits-reality-in-india/articleshow/51193793.cms?prtpage=1>.

⁵¹⁸ Securities and Exchange Board of India (Real Estate Investment Trusts) Regulations, 2014.

⁵¹⁹ Conventus Law, *Real Estate Investment Trusts In India* (Feb. 24, 2016), <http://www.conventuslaw.com/report/real-estate-investment-trusts-in-india/>.

⁵²⁰ Babar, *supra* note 508.

J. ISRAEL



Overview

Israel has a class action system that, in many ways, follows the American principles and procedures of class litigation.

Under Israeli law, a class action is an action initiated by a representative claimant, brought on behalf of a group of persons (who themselves did not authorize the claimant to do so), which raises substantive questions of fact and law common to all members of the group.⁵²¹

Class actions in Israel may be brought on a wide variety of subject matters including securities, consumer, banking, antitrust and environmental claims all as expressly permitted by Schedule 2 of Israel's Class Actions Law.

Basics of Filing a Claim and Litigation

The claimant files his own claim, based on his own individual cause of action, together with an application requesting judicial approval for his claim to become a class action and to serve as a representative claimant, on behalf of the putative class. The representative claimant must demonstrate an ascertainable class. He is not required to locate or identify potential class members. Once the Court reviews and approves the application for class action status, the claim can proceed as a class action. Determination of class status precedes meaningful consideration of the individual claim.

With some exceptions, class action litigation, including the application for class approval, are filed in civil court. Most monetary claims (where the aggregate amount claimed by the class is greater than NIS 2.5 million (approximately \$650,000) are filed in Israeli district courts. (If the aggregate damage is more modest, the claim is filed in magistrate court).

⁵²¹ Class Actions Law, 5766-2006, s. 2.(Isr.).



However, securities class cases must be submitted to the Economic Department of the Tel Aviv District Court.⁵²²

Section 8(a) of the Class Actions Law sets out the following list of conditions for approval, all of which must be met:

The action raises material questions of fact or law, which are common to all members of the class, and there is a “reasonable possibility” that these questions would be determined in favor of the class;

A class action is the most efficient and fair way to settle the dispute, given the circumstances of the matter; and

There is a reasonable basis to assume that the class members’ interests will be represented and conducted in an appropriate manner, and in good faith.

These conditions are cumulative. That said, the court may deviate from these requirements under certain circumstances mentioned in the Class Actions Law. Or, the court may approve the class action even if the last condition is not fulfilled, if the court concludes that the other conditions can be met by adding or replacing a representative claimant or class counsel. Moreover, even where the requirements have been met, the court may decide not to grant approval in cases where the application is brought against the state or a body established by law, or against a body that provides an essential service to the public, if conducting the claim as a class action is expected to cause severe harm to the public.⁵²³

In addressing these questions, the courts balance between two competing considerations: providing an opportunity for the main issues in the case to be heard and decided while also protecting a defendant from

incurring large costs needlessly to defend or settle baseless litigation.

If the court determines not to certify the application, the claimant is still allowed to conduct his own personal action against the defendant.

A court decision not to certify a class action may be appealed by the representative claimant. A court decision to approve a class action may be appealed by the defendant only if the court that granted the approval or the appellate court has authorizes such an appeal.

The court may define a class by using the opt-out model (the default option) or the opt-in model (only in special circumstances). In any event, in an opt-in class action, the representative claimant must identify and locate the class members, and notify them of the approval.

If the court decides to approve the application, the defendant may submit a statement of defense within 45 days following receipt of the decision, or at another time as determined by the court.

The Class Actions Law does not determine any specific notice mechanism. It provides that the court may order different methods of publication notice to different class members taking into account several considerations, such as the costs involved or the estimated number of class members.

Class action standing is codified by the Class Actions Law⁵²⁴ and is principally a function of the subject matter at issue. In addition to individual claimants, a public agency and authorities, (approved by the Israeli Ministry of Justice) may be approved by the Court so long as the Court determines that to do so is necessary for the efficient and fair conduct of the class action.⁵²⁵

If the Court determines that the proposed class action is baseless or unfit to qualify as a class action, it may assess significant but reasonable costs on the claimants.

⁵²² Other exceptions are claims relating to labor laws which must be filed at the Labor Tribunal and those against a state agency for return of unlawfully collected mandatory payments which are filed at the Court of Administrative Affairs.

⁵²³ *Supra* at note 521, s. 8(b).

⁵²⁴ *Supra* at note 521, 5766-2006, s. 4.

⁵²⁵ *Supra* at note 521, 5766-2006, s. 15.



After approving the class action application, the Court will determine the scope of the class to ensure that material questions of fact or law are common to all members. The requirement is that material – not *all* – factual or legal questions be common to the class. The Court may also consider whether sub-classing the claimants or the claims is appropriate, even at the damage calculation phase.

Extraterritorial Jurisdiction

There are no special rules when dealing with class actions where claimants are outside Israel. The regular rules on jurisdiction apply. Jurisdiction of the Israeli courts is obtained by due service of a claim. There are no special restrictions on foreign claimants applying for approval of class actions in the Israeli courts.

Foreign parties may bring class action proceedings in Israel. No additional jurisdiction requirements are required so long as service of the claim has been properly effected.

Funding the Litigation

In instances where the class action addresses questions of “public and social importance,” potential class representatives may be eligible for state funding of the class litigation.⁵²⁶ Class actions may be funded by the state-sponsored public fund. The public fund is managed by a board appointed by the Justice Ministry and includes members of governmental agencies, including the Attorney General, the Restrictive Trade Practices Commissioner and the Supervisor of Banks. The Class Actions Aid Regulations list the criteria for funding a class action, for example, the specific circumstances of the matter, the social and public importance of the class action and its contribution to the values it aims to protect. The fund is expressly restricted from funding specific types of class actions,

which the Israeli Securities Authority is authorized to fund.⁵²⁷

The courts are generally unwilling to permit private third-party litigation funding for class actions in Israel.

Fees and Costs

The Class Actions Law deals with both costs awards to representative claimants⁵²⁸ and class counsel.⁵²⁹ The court has the sole discretion to set the level of remuneration, to be awarded at the end of the proceedings. There are no maximum or minimum thresholds in this regard.

In setting the amount of remuneration for the representative claimant, the court considers, among other things, the work done by the representative claimant; the litigation risk, the class benefits, the public importance of the class action. The remuneration should provide a meaningful incentive to file meritorious class actions though the amount awarded must be reasonable.

The class counsel’s remuneration is decided, among others, on the basis of the following the complexity of the case, the costs paid out by class counsel, the quality of representation, the difference between the remedies originally requested in the application for approval, and those finally awarded by the court.

Normally, the remuneration is awarded when the court rules in favor of the class. However, in exceptional cases, the court may order remuneration to the representative claimant even if the action was not approved as a class action, or if the class action was not decided in favor of the group.

When the class action is settled, the costs and fees will be determined by the court according to the same considerations.⁵³⁰ However, their level would

⁵²⁷ *Supra* at note 521, s. 27(g) and Securities Law, 5728-1968, s. 55c(a).

⁵²⁸ *Supra* at note 521, s. 27.

⁵²⁹ *Supra* at note 521, s. 23.

⁵³⁰ *Supra* at note 521, s. 19.



be much lower than in a case where the court ruled in favor of the class.

Damages

Israeli Class Action law⁵³¹ provides that the Court has discretion to award damages on a per class member basis or to the class itself pending a subsequent damage analysis. Class-wide basis either pending individual proof of claims or defer calculation. If class-wide damages are impractical, the Court has discretion to grant any other remedy to the class, or to the public.

In determining the relief, the Court may balance the costs to the public as a whole resulting from the defendant's outlay in meeting the damage award against the class or public benefits of the class relief. There is no cap to the award that the Court may order.

Punitive damages are only available in limited circumstances set out in section 9 of Schedule 2 of the Class Actions Law.

The claimant may request – and the Court may award – declaratory and/or monetary relief. The Court may also award interim relief, especially an interim injunction.

Settlement Rules

A settlement involving a class action requires court approval. To ensure class members' interests are protected and the settlement is fair, the Class Action Law requires that the proposed settlement be thoroughly examined, including support from an expert opinion, prior to Court approval. The expert should examine the advantages (and disadvantages) to the class of the proposed settlement. Further, the proposed settlement must be reviewed by the Israeli Attorney General's office. Class members must also receive notice of the proposed settlement.

⁵³¹ *Supra* at note 521, s. 20.



K. JAPAN

Securities Law in Japan

There has been an increase in the number of securities actions filed in Japan over the last several years.⁵³² Much of this litigation is a direct result of the passage of Article 21-2 of the Financial Instruments and Exchange Act (the “FIEA”) in 2004. Article 21-2 is a provision of the FIEA that outlines an issuer’s statutory liability to investors in the secondary securities market in Japan.

To prevail on a claim for damages under Article 21-2, plaintiffs must prove: (i) there was a material misrepresentation in an issuer’s public disclosure documents enumerated under Article 25 of the FIEA; (ii) that the acquired⁵³³ securities were issued by the person or entity who submitted the disclosure documents; and (iii) the securities were acquired from such person or entity (rather than in a public offering) after the document was disclosed to the public.⁵³⁴ Material misrepresentations include both affirmatively false statements and omitted statements regarding “important matters.” The applicable disclosure documents listed in Article 25 include, but are not limited to: annual reports, semi-annual reports, quarterly reports, and

internal control reports. Interestingly, Article 21-2 is not applicable to misrepresentations made in disclosures required by stock exchanges or in voluntary disclosures by an issuer.

A fraud-on-the-market theory like that utilized in the U.S. is generally applicable to claims under Article 21-2. Accordingly, plaintiffs need not prove actual reliance on the challenged disclosure as a result of a 2014 amendment enacted as part of Japan’s recent reform of the FIEA. Under this amendment, the standard of liability was changed from strict liability to negligence, with the burden of proof for demonstrating non-negligence on the defendant issuer.⁵³⁵ Importantly, investors in Japan need not demonstrate a defendant’s scienter as required in the U.S. under Section 10(b) of the Exchange Act. However, defendants still have the ability to rebut a showing of negligence in connection with their alleged misrepresentations and omissions.⁵³⁶

There is also the equivalent of a “statute of limitations” to assert claims under Article 21-2. Claims are extinguished if not exercised: (i) within two years from the time the claimant becomes aware of the misrepresentation (or should be aware through the exercise of reasonable care); or (ii) within five years from the date the challenged disclosure document is filed.⁵³⁷

Under FIEA, there is a statutory rebuttable presumption of damages caused by a defendant’s

⁵³² Gen Goto, *Growing Securities Litigation against Issuers in Japan: Its Background and Reality*, at 1 (Jan. 13, 2016), <http://ssrn.com/abstract=2714252>.

⁵³³ Pursuant to the 2014 amendment discussed *infra*, Article 21-2 was expanded to also include investors who disposed of the issuer’s securities during a misrepresentation. However, the presumption of damages under Article 21-2 is still limited to those who *acquired* the issuer’s securities during a misrepresentation. See Goto *supra* note 532, at 29 n. 79.

⁵³⁴ See Goto *supra* note 532, at 6.

⁵³⁵ FIEA Art. 21-2, ¶ 2 (as amended).

⁵³⁶ See Goto *supra* note 532, at 29-30.

⁵³⁷ FIEA Art. 21-3 and Art. 20.



material misrepresentations. Specifically, damages are presumed to be the difference between the average market price in the one-month period before and after a corrective disclosure.⁵³⁸ This presumption only applies to investors who acquired the issuer's shares within one year prior to the corrective disclosure date, and who continued to hold the shares on the day of the disclosure. Moreover, recoverable damages under Article 21-2 are limited to the difference between the amount paid by plaintiff to acquire the security, and the market value of that security when plaintiff claimed damages.⁵³⁹ Issuer defendants are also not liable for damages stemming from a decline in stock price not caused by a defendant's alleged misrepresentation.

In addition to private litigation, public securities enforcement under Article 21-1 is carried out by Japan's Securities and Exchange Surveillance Commission ("SESC"). The SESC typically pursues this public enforcement by issuing: (i) administrative fines; or (ii) criminal sanctions for misrepresentations or omissions in the offering of securities.⁵⁴⁰ As in the U.S., a private litigant's burden of proof under Article 21-1 is eased if he can point to an SESC recommendation for an administrative fine, or request for criminal prosecution.

The *Olympus*, *Seibu Railway* and *Livedoor* Cases

The *Olympus* action represents a significant securities case litigated in Japan since *Morrison*. In *Olympus*, numerous institutional investors and pension funds filed suit in Japan because they had purchased Olympus-issued ADRs in the U.S.⁵⁴¹ The company was alleged to have engaged in fraudulent accounting practices, which resulted in a claim for damages against both the company's directors and auditors.⁵⁴²

In the *Seibu Railway Co., Ltd.* litigation, executives were accused of falsifying financial statements by incorrectly reporting the number of shares in the possession of its parent company, Kokudo Corporation and its affiliated companies in the annual securities reports from 1997 through 2004.⁵⁴³ In addition, one executive, Yoshiaki Tsutsumi, pleaded guilty for falsifying financial reports to hide the extent of his ownership in the company.⁵⁴⁴ After the false reporting schemes were announced on October 13, 2004, the price of Seibu shares declined significantly, and the Tokyo Stock Exchange (on which the shares were listed) decided to delist the company's stock.⁵⁴⁵ The Supreme Court found liability under Japan's general tort law, given that Article 21-2 could not be applied at the time. More than ten shareholder lawsuits were filed against the company seeking damages, and 30.9 billion JPY (\$271 million USD) has been paid by the company.⁵⁴⁶

Another prominent example of a Japanese securities case under Article 21-2 is the *Livedoor* action. Various investors separately sued Livedoor, an internet portal and services company, alleging they suffered losses from the company's 2006 share price collapse. This drop in stock price occurred after a disclosure of false profits in the company's financial statements, and other fraud. Because the parallel regulatory investigation by the SESC established material misrepresentations and omissions, the private plaintiffs were not required to make a separate showing of materiality. As a result, Japanese courts in the four major *Livedoor* cases awarded a total of 19 billion JPY in damages (approximately \$250 million).

⁵³⁸ FIEA Art. 21-2, ¶ 3. Recessionary damages are also available for plaintiffs who can prove that they would not have purchased the securities but for the alleged misrepresentation.

⁵³⁹ FIEA Art. 21-2, ¶ 5 and 6.

⁵⁴⁰ Goto, *supra* note 532, at 16-17.

⁵⁴¹ Alix Partners, *Recent Trends in Japanese Securities Litigation: 2000-2012* (Jul. 25, 2013), http://www.alixpartners.com/en/LinkClick.aspx?fileticket=vpr_GIK924%3d&tabid=2087.

⁵⁴² See *infra* Section IV (Case Study-Olympus (Japan)).

⁵⁴³ Munehisa Wada, *Supreme Court Judgment in the Seibu-Railway Corporation Case*, Waseda University Institute of Comparative Law (Mar. 8, 2012), available at http://www.waseda.jp/hiken/en/jalaw_inf/topics2011/010wada.html.

⁵⁴⁴ Todd Zaun, *Guilty Plea in big Financial Scandal in Japan*, N.Y. Times, June 17, 2005, available at http://www.nytimes.com/2005/06/17/business/worldbusiness/guilty-plea-in-big-financial-scandal-in-japan.html?_r=0.

⁵⁴⁵ Wada, *supra* note 534.

⁵⁴⁶ Nikkei Asian Review, *Former Execs to Repay Seibu's Damages in Shareholder Suits* (Feb. 11, 2016), available at <http://asia.nikkei.com/Business/Companies/Former-execs-to-repay-Seibu-s-damages-in-shareholder-suits>.



Different Mechanisms for Group Proceedings in Japan

There are a number of different legal mechanisms available to investors in Japan seeking collective redress for fraud in connection with securities transactions: joint proceedings, appointed party proceedings, consumer organization proceedings, the new class action system, quasi-class actions, and individual or institutional investor suits.

Joint Proceedings

Article 38 of the Code of Civil Procedure of Japan (“CCP”) allows joinder of parties or claims, known as “Joint Proceedings.” Such proceedings are permissible if claims: (i) are common to the parties; (ii) arise from the same facts or law; or (iii) are of the same kind and arise from the same kind of cause.⁵⁴⁷ In Japan, most group disputes are resolved by utilizing this established system of joinder,⁵⁴⁸ which involves the appointment of the same attorneys as plaintiffs’ counsel. There are various remedies available through Joint Proceedings, such as monetary, injunctive, specific performance and declaratory relief.

Under the CCP, there is no set time limit when a proceeding must be filed. Rather, rights and obligations will lapse after certain intervals as set forth in Japan’s substantive law.⁵⁴⁹ Therefore, the “statute of limitations” varies depending on the type of claim, but generally, claims subject to the CCP will extinguish ten years after the time that the claims became exercisable.⁵⁵⁰

Appointed Party Proceedings

The CCP also allows appointed group representatives to file lawsuits on behalf of group members, known as “Appointed Party Proceedings.” Similar to “opt-in” actions in the United States, a

decision of the court only binds parties to the litigation, *i.e.*, the group representative, the defendants and the parties appointing the representative. The following requirements must be met to file an Appointed Party Proceeding in Japan: (i) a group of persons must share common interest in the case; (ii) the representative must be selected from the same group; and (iii) an organized group that qualifies as an unincorporated association may commence a procedure under its own name.⁵⁵¹ The relief provided includes monetary, injunctive, specific performance and declaratory relief. Payment of court fees will be arranged between the parties appointing the group representative.

Consumer Organization Proceedings

This special procedure allows consumer organizations licensed by the government, a “Qualified Consumer Organization,” to pursue litigation to resolve consumer disputes pursuant to: (i) the Consumer Contract Act (“CCA”); (ii) the Act Against Unjustifiable Premiums and Misleading Representations (“AUPMR”); and (iii) the Specified Commercial Transactions Act (“SCTA”). Only injunctive relief is available in Consumer Organization Proceedings under these Acts. In addition, a court decision on collective claims under these Acts does not preclude consumers from advancing individual claims. While the conduct at issue must be related to consumer disputes (*i.e.*, false advertising and solicitation), such conduct includes “false representations, provision of conclusive evaluations on uncertain matters or willful omissions of disadvantageous facts.”⁵⁵² It is at least conceivable that this language could be applied to consumer contracts in the securities industry.

New Class Action System

On December 11, 2013, the Japanese government enacted the Act on Special Rules of Civil Procedure for Collective Recovery of Consumers’ Property Damage, thereby introducing a new class action system that will take effect in December 2016.⁵⁵³ Under this Act, Specified Qualified Consumer Organizations (“SQCO”)

⁵⁴⁷ International Comparative Legal Guides (“ICLG”), *Japan: Class and Group Actions 2016*, at 2 (Oct. 28, 2015), available at <https://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/japan>.

⁵⁴⁸ Michael Maddera, *The New Class Actions in Japan*, 23 *Pac. Rim L. & Pol'y J.* 795 at 803 (June 3, 2014).

⁵⁴⁹ ICLG, *supra* note 538, at 9.

⁵⁵⁰ CCP, Articles 166 and 167.

⁵⁵¹ CCP, Articles 29 and 30.

⁵⁵² ICLG, *supra* note 538, at 3.

⁵⁵³ See Maddera, *supra* note 539, at 803.



licensed by the government can pursue litigation for the collective recovery of consumers' monetary claims.⁵⁵⁴

Because claims brought under this new class action system are essentially limited to claims concerning consumer contracts (*i.e.*, product defects and harmful business practices), such relief would appear to be unavailable to investors in the secondary market who suffer damages through misrepresentations.⁵⁵⁵ It remains to be seen whether investors or attorneys in Japan will opt to use this in the securities law context.

Quasi-Class Actions

Given that U.S.-style securities class actions are unavailable for Japanese investors, Japanese attorneys must seek different means to replicate the U.S. mechanism. It is therefore not uncommon for several law firms to file quasi-class actions on behalf of plaintiff investors, and persuade a large group of investors to become plaintiffs in such lawsuits by opening websites for "victim shareholders."⁵⁵⁶ These lawsuits can be seen as quasi-class actions because although the scale of such litigation tends to be much smaller than U.S. class actions, they still involve numerous investor plaintiffs filing collectively.

The quasi-class action mechanism appears to be growing in Japan. The *Seibu Railway, Livedoor, and Olympus* cases were all quasi-class actions filed in Japan.⁵⁵⁷ Some of these actions are filed on behalf of investors by a group of law firms, and some are brought by just a single firm. The number of plaintiffs in these suits is mostly in the hundreds, but some have exceeded that amount, such as the *Livedoor* case where a group of over 3,000 investor plaintiffs brought suit.

Suits Filed by Institutional or Individual Investors

Some institutional investors opt for alternatives to the quasi-class action, such as seeking individual representation by a single law firm in Japan.

The amounts claimed in these lawsuits are large, even up to the hundreds of millions to tens of billions in Japanese Yen (equivalent to hundreds of millions in USD). A number of individual investor suits are also being filed without attorney representation.⁵⁵⁸ The claims in these suits tend to be small, often less than 100 million JPY (approximately 1 million USD), in contrast to the larger amounts sought by institutional investors filing individually, or investor groups suing in quasi-class actions.

Costs and Attorneys' Fees

Pursuant to Article 61 of the CCP, court fees and other litigation costs are paid by the losing party unless otherwise allocated by the court.⁵⁵⁹ There is no CCP provision that specifically requires a court to impose a cap on court fees, so the court can use its discretion to allocate such fees. In joint proceedings, the joint parties generally pay court fees in equal amounts, but the court can order a different allocation. Specifically, in Appointed Party Proceedings, the distribution of court fees will be decided by an arrangement between the appointing group members. In Consumer Organization Proceedings, court fees are paid by the Qualified Consumer Organization litigating these claims. Under the new class action statute, plaintiff SQCOs will generally incur court fees, but may also recover their fees from consumers who opt-in to the class. If a party withdraws a lawsuit or otherwise abandons a claim, that party will pay the court fees relating to that claim.⁵⁶⁰

Attorneys' fees are not considered costs under the CCP. In Japan, as in the U.S., parties are generally responsible for their own legal fees. Therefore, a party does not have to pay the other party's attorneys' fees even if it loses the case (*i.e.*, no loser pays system). In addition, there is no *per se* limit on contingency fees, which are permissible in Japan.⁵⁶¹

⁵⁵⁴ ICLG, *supra* note 538, at 3.

⁵⁵⁵ See Goto, *supra* note 532, at 11; see also, Maddera, *supra* note 539, at 796.

⁵⁵⁶ Goto, *supra* note 532, at 11.

⁵⁵⁷ *Id.* at 21.

⁵⁵⁸ *Id.* at 25.

⁵⁵⁹ ICLG, *supra* note 538, at 11.

⁵⁶⁰ *Id.* at 11-12.

⁵⁶¹ Goto, *supra* note 532, at 12.

L. MEXICO



Overview

The Mexican Stock Exchange (Bolsa Mexicana de Valores or “BMV”) is now part of the Mercado Integrado Latinamericano (the “MILA”), which integrates with the exchanges of Chile, Colombia, and Peru. Combined, the MILA is larger than Brazil’s Bolsa de Valores, Mercadorias & Futuros de São Paulo (BM&F BOVESPA), and has over 780 issuers.⁵⁶²

The Mexican Securities Market Law (Ley del Mercado de Valores or “LMV”) governs companies which have their securities listed on the Mexican Stock Exchange. Damages and lost profits are recoverable for violations of the law, which include the release of

misleading information.⁵⁶³ However, there is little in the public record regarding the use of such actions, and it is still unclear whether the law would permit private investor suits.

Mexico has been developing class action laws and procedures, similar to the United States and Brazil. On July 29, 2010, the Mexican Constitution was amended to require the Federal Congress to pass laws allowing exclusively federal class actions. The

⁵⁶² Jude Webber, *Mexico exchange names Sacristán as new head*. *FIN. TIMES* (Jan. 9, 2015), available at <http://www.ft.com/intl/cms/s/0/4ef088e4-7a43-11e4-a8e1-00144feabdc0.html#axzz498wOktJC>.

⁵⁶³ Ley Del Mercado de Valores, 30-12-2005, translated, <http://www.banxico.org.mx/disposiciones/circulares/leyes/%7BB4D02177-3630-E75F-A12B-E93E1AEE94F5%7D.pdf>; Martinez, Alga, Estrella, DeHaro y Galvan-Duques, S.C., *Comments to the New Securities Law* (Feb. 2006), http://www.iln.com/articles/pub_302.pdf-f; Hans P Goebel Caviedes and Diego Sánchez Villarreal Nader, Hayaux y Goebel SC, *Capital Markets 2016, Mexico, Latin L.* (Mar. 16, 2016), <http://latinlawyer.com/reference/topics/49/jurisdictions/16/mexico/>.



most important amendment was the addition of Articles 578 through 625 of the Federal Civil Procedural Code (“CFPC”), which provides the specific procedures for group or class actions in Mexico.⁵⁶⁴ The amendments limit the types of claims that can be brought as class actions to consumers, users of goods or public and private services, the environment, or violations of the competition laws.⁵⁶⁵ On March 12, 2012, these changes went into effect, allowing “collective actions” in which private individuals, non-profits, and government agencies may prosecute claims representatively on behalf of a group of people. Book Five of Mexico’s Federal Code of Civil Procedure codifies these collective action procedures. While the Mexican legal framework shares several similarities with Rule 23 of the U.S. Federal Rules of Civil Procedure (“FRCP 23”), there are notable differences. For example, Mexico’s laws and procedures do not explicitly provide for collective actions for securities fraud. To date, there are no reported securities fraud or equivalent class actions. If such a claim were allowed, it would be an opt-in action.

Basics of Filing a Claim and Litigation

Under Mexican law, a collective action allows a common representative, a non-profit association, or a government agency to file a claim to protect a right

⁵⁶⁴ These articles, (Código Federal de Procedimientos Civiles [CFPC], arts 578-625, Diario Oficial de la Federación [DOF] 30-08-2011 (Mex.)), which Google Translate will automatically translate to English can be found here: http://dof.gob.mx/nota_detalle.php?codigo=5206904&fecha=30/08/2011.

⁵⁶⁵ Juan Francisco Vazquez Lavista & Jorge Arturo Pérez Dominguez, Gardere, Arena y Asociados, S.C., *Mexico Class and Group Action 2016*, International Comparative Legal Guides, <http://www.iclg.co.uk/practice-areas/class-and-group-actions/class-and-group-actions-2016/mexico> (last visited Apr. 26, 2016) (“ICGL”); Adrián Magallanes and Rodrigo Barradas, Von Wobeser y Sierra, S.C., *Class/Collective actions in Mexico: Overview*, Practical Law, Thomson Reuters (Aug. 1, 2015), <http://us.practicallaw.com/9-618-1165#top>; *New Class Action Rules in Mexico Create Significant Risks for Companies Doing Business in Mexico*, Jones Day (Mar. 2012), http://www.jonesday.com/new_class_action_rules_in_mexico/. (“Jones Day”); Neal R. Marder and Andrew S. Jick, Winston & Strawn LLP, *Collective Actions in Mexico: Similarities, Differences, and Implications*, BNA, Bloomberg L. (Oct. 26, 2012), <http://cdn2.winston.com/images/content/1/3/v2/1313/marderjickcollectiveactionsmexico.pdf> (referenced hereafter as “Marder”).

or interest that belongs to a community or group of individuals, united by a common cause or circumstance, the judgment of which affects all the members of the community or group. Standing for bringing the action, the procedures to follow, and the remedies available depend on the type of rights the action seeks to protect. The three types, largely borrowed from Brazilian law, are:

- **Diffuse actions.** These actions are indivisible and belong to an undetermined group. An example is a violation of the environmental laws where the relief sought is general, such as injunctive relief and the cost of clean-up.⁵⁶⁶ These claims are similar to claims made pursuant to FRCP 23(b)(1) and (2).⁵⁶⁷
- **Collective actions “in the strict sense.”** A group, composed of 30 or more individuals, whose members’ rights are determined by common circumstances arising from some sort of legal relationship. An example is a products liability claim resulting in a recall and an award of individual damages to each purchaser.⁵⁶⁸ If allowed, securities fraud class action claims based on misrepresentations or omissions by a company would likely fit into this category. These claims fit under the rubric of FRCP 23(b)(1) through (3).⁵⁶⁹
- **“Individual Homogenous” actions.** A group, composed of 30 or more individuals, whose members’ rights are divisible but with a common origin in contract.⁵⁷⁰ These claims are most analogous to FRCP 23(b)(3) class actions. If allowed, a claim similar to a claim under Section 11 or 12(a)(2) of the Securities Act based on a registration statement or prospectus might fit into this category.

⁵⁶⁶ Jones Day, *supra* note 556.

⁵⁶⁷ Marder, *supra* note 556.

⁵⁶⁸ Jones Day, *supra* note 556.

⁵⁶⁹ Marder, *supra* note 556.

⁵⁷⁰ Jones Day, *supra* note 556; Marder, *supra* note 556.



Loser Pays Model

Mexico has no “loser pays” model. Pursuant to Article 617 of the CFPC, each party shall bear its own legal expenses and costs during the process of class actions, as well as their own representative’s fees. The judge determines whether the losing party must pay the expenses and costs in the final judgement.

Expenses and costs may be paid from a public fund created with proceeds obtained from diffuse actions where there is a social interest that justifies it and to the extent the proceeds are available.⁵⁷¹ This may also be true of individual homogenous actions.⁵⁷²

There are caps on attorney’s fees in collective actions, which range from 3% to 20% depending on the amount of damages.⁵⁷³

Opt-In vs. Opt-Out

As referenced within the discussion of diffuse actions above, Mexican class actions are opt-out only in diffuse actions, which would not apply to securities fraud class actions. They are opt-in for actions that would recover individual damages, such as individual homogenous actions. In such actions, once the defendant’s liability is established, individuals may opt-in within 18 months of the entry of judgment.⁵⁷⁴

Extraterritorial Jurisdiction

Pursuant to Article 24-IV of the CFPC, class actions have to be filed before the competent court of the domicile of the defendant by any affected plaintiff with legal standing.⁵⁷⁵

Funding the Litigation – Contingent Fee Arrangements

There is no statutory provision regarding funding. The CFPC provides a tariff for the collection of representatives’ fees. If the judgment does not

include a quantifiable amount, the judge must take into consideration the work done by the representatives and its complexity, the number of members, the benefit to the community, and other circumstances deemed relevant.⁵⁷⁶

There are no reports of third-party institutional funding.

Causes of Action in Securities Litigation

Under the LMV, it is forbidden to disclose false or misleading information about securities or information related to an issuer’s financial, economic, or legal position.⁵⁷⁷ No one in possession of material undisclosed information is permitted to trade on that information or pass that information to anyone else.⁵⁷⁸ While it is clear that these laws are enforceable by the company, 5% shareholders,⁵⁷⁹ or regulators, it is not clear whether there exists a private right to sue.

Regulatory Environment for Securities Litigation

In 2012, the International Monetary Fund (the “IMF”)⁵⁸⁰ issued an assessment on Mexico’s implementation of the International Organization of Securities Commissions Objectives and Principles of Securities Regulation (IOSCO Principles).⁵⁸¹ It found a high level of implementation, but many gaps, which should concern investors.

The main regulator of the securities markets in Mexico is the National Banking and Securities Commission (Comisión Nacional Bancaria y de Valores, or CNBV). However, the IMF found that there are “significant weaknesses in the protections afforded

⁵⁷⁶ See *id.*

⁵⁷⁷ Ley del Mercado de Valores [LMV], arts 36, 368, Diario Oficial de la Federación [DOF] 30-12-2005, última reforma DOF 10-01-2014 (Mex.).

⁵⁷⁸ *Id.* art 364.

⁵⁷⁹ *Id.* art 38.

⁵⁸⁰ The IMF is an organization of 189 countries working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world.

⁵⁸¹ Mexico, *The IOSCO Objectives and Principles of Securities Regulation, Detailed Assessment of Implementation*, IMF (Mar. 2012), <https://www.imf.org/external/pubs/ft/scr/2012/cr1268.pdf>.

⁵⁷¹ See ICLG, *supra* note 556.

⁵⁷² See Practical Law, *supra* note 556.

⁵⁷³ See *id.*

⁵⁷⁴ See ICLG and Jones Day, *supra* note 556.

⁵⁷⁵ See ICLG, *supra* note 556.



members of the Board of Governors and staff and with the resources of the Commission that lead to concerns about its independence and ability to carry out its mandate fully.” Moreover, while there is a consumer protection agency for users of financial services – the National Commission for the Protection and Defense of the Users of Financial Services (Comisión Nacional para la Protección y Defensa de los Usuarios de Servicios Financieros, or CONDUSEF) – this commission does not seem to have a mandate to protect investors, and it appears to have no power to order compensation for damages. The IMF concluded: “The weakness of this agency is of concern as gaps in the consumer protection regime may have a negative effect on investors and undermine confidence in the system as a whole.”⁵⁸²

Prerequisites for a Collective Action

In order to certify a collective action under Mexican law, familiar prerequisites must be satisfied. The CFPC contains provisions that roughly correspond to FRCP 23’s requirements that the class size be sufficiently numerous, common questions of fact or law exist among class members, and absent class members be adequately represented.⁵⁸³ While there is no formal requirement that a representative’s claims be typical of those of the class, there exist in the CFPC provisions requiring adequate representation, as well as a determination as to whether there are common facts, whether the class definition is appropriate, and whether the appropriateness of collective action versus an individual action has been established.⁵⁸⁴

Certification and Notice During the Collective Action

Perhaps the most dramatic difference between the CFPC and FRCP 23 is that the CFPC contains a highly expedited approach to class certification. This contrasts sharply with class certification in the United States, where class certification is vigorously contested and may take an extended period of time to secure in complex cases.⁵⁸⁵

⁵⁸² *Id.* at 6.

⁵⁸³ See ICGL, *supra* note 556; see also Jones Day, *supra* note 556.

⁵⁸⁴ See Jones Day, *supra* note 556.

⁵⁸⁵ See *id.*

The CFPC requires that the court, after issuing orders certifying a collective action, provide proper notice to the collective group (*i.e.*, notice must be “economic, efficient and wide” under the circumstances).⁵⁸⁶ These requirements are similar to FRCP 23(c)’s class notice requirements for FRCP 23(b)(3) actions.⁵⁸⁷ In addition, similar to FRCP 23(d), under the CFPC the court may require the collective group representative to provide periodic status updates to the group and to alter or amend the collective action allegations in the complaint when warranted.⁵⁸⁸

Settlement

Similar to the requirements of FRCP 23, the CFPC encourages settlement and mandates that parties may only settle a collective action with court approval.⁵⁸⁹ Under both legal systems, the court must ensure that the settlement is fair and that the interests of absent class members are protected. In addition, both systems require that notice of the proposed settlement be provided to the collective group and that the court conduct a hearing at which the parties and any objecting members of the collective group may be heard.⁵⁹⁰ However, under the CFPC, in contrast to FRCP 23, the court is authorized to propose settlement terms and encourage the parties to reach a settlement.⁵⁹¹

Attorneys’ Fees and Costs

By contrast to FRCP 23(h)’s provision that the court may award “reasonable” attorneys’ fees and costs, the CFPC sets a maximum fee schedule for compensation of the collective group’s legal representative.⁵⁹² This fee schedule provides a sliding scale based on the amount of the settlement or judgment.⁵⁹³ If the parties

settle, the amount of the fee is determined during negotiations, subject to the statutory maximum; but if plaintiffs obtain a judgment, the court determines

⁵⁸⁶ See ICGL, *supra* note 556; see also Jones Day, *supra* note 556.

⁵⁸⁷ See Jones Day, *supra* note 556.

⁵⁸⁸ See ICGL, *supra* note 556; see also Jones Day, *supra* note 556.

⁵⁸⁹ See ICGL, *supra* note 556; see also Jones Day, *supra* note 556.

⁵⁹⁰ See ICGL, *supra* note 556; see also Jones Day, *supra* note 556.

⁵⁹¹ See Jones Day, *supra* note 556.

⁵⁹² See ICGL, *supra* note 556.

⁵⁹³ See Jones Day, *supra* note 556.



the amount of attorneys' fees, subject to the statutory maximum, giving consideration to the quality of work performed, the complexity of the case, the size of the collective group, the benefit received by the collectivity, and other relevant factors.⁵⁹⁴

Class Counsel

Unlike FRCP 23(g), the CFPC does not require the court to appoint counsel for the collective group.⁵⁹⁵ Instead, the court's supervisory powers are limited to overseeing the representative of the collective group to ensure that the common representative provides adequate representation throughout the proceedings.⁵⁹⁶ If the original representation of the group becomes inadequate, the court has the authority to appoint a substitute representative.⁵⁹⁷

⁵⁹⁴ See ICGL, *supra* note 556.

⁵⁹⁵ See Marder, *supra* note 556.

⁵⁹⁶ See *id.*

⁵⁹⁷ See *id.*

M. THE NETHERLANDS



Trends in Securities Litigation in the Netherlands

The Netherlands has become an increasingly popular forum for plaintiffs seeking monetary relief on behalf of investors in multiple jurisdictions, as well as defendants seeking a binding opt-out settlement on securities claims against them. In 2012, the Amsterdam Court of Appeal declared an international collective settlement involving Converium Holding AG (“Converium”) to be binding on members of the class who did not opt out even though the defendants and most of the plaintiffs were not located in the Netherlands. The court utilized a class settlement procedure known as the Dutch Act on the Collective Settlement of Mass Claims (*Wet Collectieve Afwikkeling Massaschade*, or

“WCAM”).⁵⁹⁸ In principle, the settlement should be recognized in all European Union member states, as well as Switzerland, Iceland and Norway.

More recently, on March 14, 2016, Belgium-based Ageas SA/NV (formerly Fortis SA/NV) announced it had reached a settlement agreement using Dutch collective settlement procedures for €1.204 billion (\$1.3 billion) to settle claims brought by several shareholder foundations. The settlement was brought before the Amsterdam Court of Appeal to be declared legally binding on all shareholders.

⁵⁹⁸ The WCAM is set forth in Articles 907-910 of Book 7 of the Dutch Civil Code (“DCC”) and Articles 1013-18a of the Dutch Code of Civil Procedure (“DCCP” or *Wetboek van Burgerlijke Rechtsvordering*.



Opt-In vs. Opt-Out

The Netherlands is both an opt-in and opt-out jurisdiction and has two collective redress mechanisms:

- A representative collective action seeking declaratory or injunctive relief (a “liability foundation or stichting”); and
- A collective settlement mechanism based on WCAM (a “settlement foundation or stichting”).

Collective actions in the Netherlands are governed by Article 3:305a of the Dutch Civil Code (“DCC”). This law allows collective actions to be filed by a representative organization or foundation with legal authority to sue on behalf of a group of injured individuals or entities that have opted in to the foundation. The court must approve the foundation’s lawsuit and find that the interests of the individuals in the foundation are sufficiently similar so that they can be handled in a single declaratory action. A collective action to obtain monetary damages is prohibited presently, but the representative entity can submit a claim for declaratory relief establishing the liability of the defendants or seek injunctive relief. Judgments entered under this provision are only binding on members of the foundation – *i.e.*, it is an opt-in mechanism. This type of collective action is often used as a stepping stone for subsequent individual or group actions seeking a recovery in Netherlands courts, which cite judgments on liability as precedent.

The WCAM allows the representative party to reach an opt-out settlement with defendants on behalf of class members outside of the foundation. Class settlements under WCAM can be declared binding exclusively by the Amsterdam Court of Appeal. The parties may request the court approve a settlement before any suit has been filed. WCAM settlements may also stem from collective actions brought under the DCC.

The Dutch legislature drafted WCAM with the U.S. class action system in mind, which shares certain features, including the opt-out mechanism. The parties can only settle their claims under WCAM, however.

The WCAM cannot be used as a basis to assert claims for damages. Another key difference is that the party that represents the interests of the class members must be a foundation and cannot be an individual plaintiff. The primary features of WCAM’s settlement provisions include:

- Parties negotiate an out-of-court settlement of mass claims;
- Claimants are represented by one or more foundations and associations;
- Representative organizations may be preexisting or established for the purpose of negotiating a settlement;
- Settling parties jointly petition court for settlement approval;
- Court-approved notice;
- Opportunity for objectors to be heard;
- Court reviews and approves settlement;
- Notice of settlements and opt-out period; and
- Settlement administration by private foundation.

Once the Amsterdam Court of Appeal holds that the settlement agreement is binding, the settlement binds all class members unless a person decides to opt out within a certain time period. Class members are allowed to stay in the class, object, and may opt out after the court approves the settlement. There is no right of appeal for class members after the court approves the settlement. Settlements are administered by private foundations established specifically for this purpose.

WCAM was amended in July 2013 to enlarge the WCAM’s applicability and make it more attractive for parties to reach a settlement. The amended WCAM enables parties to involve a judge at an early stage for assistance in the negotiation of the collective settlement agreement (a pre-trial hearing). The amendments also make it possible to use the WCAM procedure



in bankruptcy cases. In July 2014, a draft bill was submitted to amend the collective action under the DCC to abolish the current prohibition against seeking damages and introduces a procedure for a collective damages action before the Dutch District Courts to allow parties to reach a settlement agreement.⁵⁹⁹

The Amsterdam Court of Appeal has issued several decisions involving settlements under WCAM since the Act entered into force in July 2005, including:

- DES (2006) (Product Liability): 34,000+ members, €38 million
- Dexia (2007) (Financial services): 300,000 members, €1 billion
- Vie d'Or (2009) (Insurance): 11,000 members, €45 million
- Shell (2009) (Securities): 500,000 members, \$352.6 million
- Vedior (2009) (Securities): 2,000 members, €4.25 million
- Converium (2012) (Securities): 12,000 members, \$58.4 million

While the first three settlements followed a decision in a Dutch collective action proceeding, the latter three settlements did not. The latter three settlements involved securities claims and were cross-jurisdictional in scope.

As noted above, on March 14, 2016, Belgium-based Ageas (formerly Fortis) announced it reached an agreement to settle shareholder claims brought by several shareholder foundations for €1.204 billion (\$1.3 billion). The case is currently pending before the Amsterdam Court of Appeal.

Securities Settlements Under WCAM

The Amsterdam Court of Appeal has issued three decisions involving international securities settlements. First, in May 2009, the court declared an international settlement to be binding on an international class in the “Shell Reserves” case under WCAM. In that case, shareholders were allegedly harmed by false statements about Shell’s oil and gas reserves that were made by the company and various officers beginning in 1999. In January of 2004, the stock price dropped after Royal Dutch/Shell announced a re-categorization and reduction in its oil reserves and the resignation of three Shell executives. One of the Shell entities was in the Netherlands, while the other was in the United Kingdom. Most shareholders lived outside of the Netherlands.

Investors brought securities class actions in the United States. However, before the U.S. court issued a final ruling, Shell reached a collective settlement with non-U.S. investors and applied to the Dutch court to have it declared binding on all non-U.S. investors. Shell agreed to pay a total of \$381 million to non-U.S. investors.

Shell has also agreed to request that the SEC distribute to shareholders the \$120 million paid by Shell in 2004 under a consent agreement resolving the SEC’s investigation into Shell. Finally, the law firms representing the foundation and two Dutch pension funds reportedly negotiated a fee of \$47 million for their role in negotiating the settlement.

The parties jointly filed a petition under WCAM seeking approval of the international settlement. On November 20, 2008, the petition was heard by Amsterdam Court of Appeal. On May 29, 2009, the court held that it had jurisdiction to hear the case and to issue a decision that bound non-U.S. claimants, even those not residing in the Netherlands, in order to prevent contradictory rulings. The *Shell* settlement resolved the claims of all investors in 100 jurisdictions worldwide, except for those investors residing in the United States who purchased their shares on U.S. stock exchanges.

⁵⁹⁹ Dutch Consultation on a draft bill on Redress of Mass Damages in a Collective Action, Dutch Ministry of Sec. and Justice (July 2014), <https://www.internetconsultatie.nl/motiedijksma/document/1177>.



Second, in July 2009, the Amsterdam Court of Appeal approved and declared binding the €4.25 million settlement for losses allegedly suffered by investors who sold their Vedior stock prior to a suspension in trading at a time when allegations were spreading that Vedior was about to be acquired. The foundation representing the class alleged that Vedior violated Dutch securities laws that required it to release certain information earlier. The settlement is significant because it was the first settlement under WCAM to include North American investors.

Third, on January 17, 2012, the Amsterdam Court of Appeal held that an international settlement was binding in a case where none of the defendants and only a limited number of the investors resided in the Netherlands. The case involved Converium Holding AG, a Swiss reinsurance company (now known as SCOR Holding AG). Converium was a wholly owned subsidiary of Zürich Financial Services Ltd. (“ZFS”).

In 2001, ZFS sold all its Converium shares in an IPO and Converium shares were listed on the SWX Swiss Exchange. Converium American Depository Shares were listed on the New York Stock Exchange. The price of Converium stock declined after the company announced increases in its loss reserves in the period from 2002 through 2004.

Investors brought a class action in the United States, and the court certified a class consisting of all U.S. persons who had purchased Converium securities on any exchange, as well as all persons—regardless of their residence—who had purchased Converium securities on a U.S. exchange. The U.S. court excluded from the class all non-U.S. persons who had purchased Converium securities on any non-U.S. exchange. The U.S. action then settled with the court’s approval.

The Amsterdam Court of Appeal’s reasoning in *Converium* largely followed the same line of reasoning as *Shell*. However, the *Converium* settlement had fewer connections with the Netherlands than the *Shell* settlement. The court emphasized the significance of a Dutch foundation representing the interested persons and having to distribute the settlement relief under the settlement agreement.

The more recent *Fortis* settlement agreement has been submitted to the Amsterdam Court of Appeal, and the parties have jointly requested the court to declare the settlement legally binding on all shareholders. The history of the *Fortis* case goes back to October 22, 2008, when U.S. shareholders filed a securities class action lawsuit in the U.S. District Court for the Southern District of New York against Fortis for violations of Sections 10(b) and 20(a) of the Exchange Act for misrepresentation and failure to disclose material information concerning Fortis’ worsening financial condition. On February 18, 2010, the securities class action was dismissed with prejudice under *Morrison*.

A specially formed foundation representing investors in the U.S., Europe, the Middle East, and Australia filed suit in Utrecht Civil Court in the Netherlands on January 10, 2011 seeking declaratory relief against Fortis for defrauding investors through a 2007 rights issue to acquire ABN AMRO. Additional Dutch shareholder foundations were organized, and a separate group independently filed actions in Belgium. The *Fortis* settlement agreement includes the Dutch shareholder foundations and the Belgian actions.

Questions remain regarding the true enforceability of an opt-out settlement such as this, given that many European Union member states have opt-in class structure. All member states of the European Union, Switzerland, Iceland and Norway, in principle, had to recognize the *Converium* decision. Whether other countries outside of the EU will also recognize it depends on local law. Nonetheless, after *Converium*, the Netherlands has certainly become the most popular forum in Europe for facilitating international settlements in securities actions.

Jurisdiction

A threshold issue in *Converium* was whether the Court had jurisdiction. Jurisdiction is, in principle, governed by the Brussels *Ibis* Regulation and the Lugano Convention, depending on whether the person to be sued is domiciled in a member state of the EU, or in Norway, Switzerland or Iceland (the “Lugano” countries). The Brussels *Ibis* Regulation and the Lugano



Convention apply if the litigation concerns a civil or commercial matter. In both *Shell* and *Converium*, the court ruled that it was a civil and commercial matter. The court also relied on Article 3 of the Dutch Code of Civil Procedure, which provides that Dutch courts have jurisdiction if at least one of the parties requesting the binding declaration, or one of the defendants, is domiciled in the Netherlands. The court's decision on international jurisdiction in *Converium* implies that even if the case is substantively not connected to the Netherlands, but a minority of the parties are domiciled in the Netherlands, and one of the parties to the settlement is a Dutch entity (*i.e.*, the foundation), the court will assert jurisdiction. The court also held as a separate and autonomous ground for jurisdiction that the settlement agreement to be declared binding had to be executed in the Netherlands.

Regulatory Environment for Securities Litigation

The Authority for the Financial Markets (*Stichting Autoriteit Financiele Markten* or “AFM”) has principal responsibility for the enforcement and administration of most securities laws in the Netherlands under the main Dutch securities statute, the Financial Supervision Act (*Wet op het financieel toezicht* or “WFT”). The Dutch Minister of Finance is responsible for most securities regulations. The Dutch Central Bank (De Nederlandsche Bank N.V. or “DNB”) is responsible for the supervision of investment undertakings, investment firms and credit institutions.

Section 6:194 of the DCC provides that anyone who issues a statement about products or services is acting wrongfully towards another party who is acting in the course of his business, if such statement is misleading in any way, such as in representations concerning the material characteristics of the securities offered.⁶⁰⁰ Claims arising from prospectus liability are based on this rule.⁶⁰¹ The unfair commercial practices rules are the basis for prospectus liability claims initiated by investors who are not acting in the course of their business.⁶⁰²

⁶⁰⁰ Marcel C. A Nieuwenhuijzen, *Financial Law in the Netherlands*, 492 (2010).

⁶⁰¹ *Id.*

⁶⁰² *Id.*, 498; Sections 6:193a – 193j *et seq.* DCC.

Fraud on the Market Theory

Under Dutch law, investors do not have to show scienter to recover damages, as Dutch law presumes that if the misrepresentations were made in the company’s public filings and the directors, executive management, and the supervisory board members are responsible for them (likewise, Dutch tort rules do not pose a scienter requirement). The burden shifts to the director or supervisory board member to disprove that the statement is not attributable to him or her.

Proving causation under Dutch law is similar to proving causation under U.S. law. A theory similar to U.S. fraud-on-the-market doctrine applies when showing reliance on the public misstatement. Plaintiffs must also must show loss causation, *i.e.*, that the damage was related to the event giving rise to the liability.

The Dutch Supreme Court established a presumption of reliance/causation for cases involving prospectus liability in its *World Online* decision.⁶⁰³ The court recognized that investors are guided by a multitude of considerations in making an investment decision and that proving reliance and causation leading to an investment decision because of a misleading statement in a prospectus could be near impossible.⁶⁰⁴ The court established a presumption of a causal connection between the misleading statement in the prospectus and the investment decision given the problems with causality and reliance and recognizing that the Prospectus Directive⁶⁰⁵ envisioned investor protection as one of its

⁶⁰³ Wulf A. Kaal & Richard W. Painter, *Forum Competition and Choice of Law Competition in Securities Law After Morrison v. National Australia Bank*, 97 MINN. L. REV. 132, 182 (2012); see also Bas J. de Jong, *Liability for Misrepresentation—European Lessons on Causation from the Netherlands*, 8 EUR. COMPANY & FIN. L. REV. 352, 364–65 (2011) (discussing the *World Online* decision and its implications); Shelley Thompson, *The Globalization of Securities Markets: Effects on Investor Protection*, 41 INT’L LAW 1121, 1139–41 (2007) (explaining the differences between the Dutch and U.S. systems of securities litigation and underscoring the attractiveness of the Dutch rules).

⁶⁰⁴ Kaal, *supra* at 182; see de Jong, *supra* at 356.

⁶⁰⁵ Directive 2010/73, of the European Parliament and of the Council of 24 November 2010 Amending Directives 2003/71/EC on the Prospectus to Be Published When Securities Are Offered to the Public or Admitted to Trading and 2004/109/EC on the Harmonisation of Transparency Requirements in Relation to Information About Issuers Whose Securities Are



core objectives.⁶⁰⁶ Under the holding in *World Online*, plaintiffs do not have to show actual reliance on a fraudulent statement in prospectus liability cases.⁶⁰⁷

Damages

Damages under Dutch law are awarded on the basis of the actual harm suffered by the claimant⁶⁰⁸ to the extent that the harm can reasonably be attributed to the wrongful conduct of the defendant(s).⁶⁰⁹ The courts have broad discretion to estimate the damages.⁶¹⁰

Damages under Dutch law are determined by the amount of artificial inflation in the stock price caused by the misrepresentations. However, recovering damages may be more favorable in the Netherlands because the Dutch court has the authority to assess damages in the manner it considers most appropriate. Thus, investors may raise any plausible damage theory that can be supported and the Dutch court has the freedom to estimate the damage if it cannot be determined precisely.

In class settlement proceedings using WCAM, a “damage scheduling” approach is often applied, under which compensation is awarded to claimants based on the characteristics of the group of which the particular claimant is a member, rather than on the basis of the claimant’s individual characteristics. The court scrutinizes the reasonableness of the compensation offered and refuses to declare the settlement binding if it finds that the compensation is not reasonable.

Loser Pays Rule

The loser pays rule applies in the Netherlands, but in practice, the compensation for legal representation is fixed at a fraction of its actual cost.⁶¹¹ Legal costs consist of court fees and attorneys’ fees.⁶¹² The losing party is potentially liable for a portion of the prevailing party’s legal fees and expenses, as well as court costs. However, the winning party does not recover the actual costs of the litigation. Costs are based on certain standard amounts for certain standard activities and the amount of the claim, and costs for legal representation are awarded on the basis of fixed amounts, which usually do not cover the real costs.⁶¹³

Funding the Litigation - Contingent Fee Arrangements

In the Netherlands, Dutch attorneys are barred by the rules of ethics from taking cases on a contingency fee basis,⁶¹⁴ but the prohibition on contingency fees is not absolute. Article 3 of the Code of Conduct for the Dutch Bar (“CCDB”) states that settling a dispute

⁶¹¹ Jeroen S. Kortmann & Miriam C. Buieten, *Private Enforcement and Collective Redress in European Competition Law*, FIDE 2016 Questionnaire, 5 (Nov. 2015), available at <http://static1.squarespace.com/static/5574a2fae4b0083487121509/t/56425f98e4b07a45a8606924/1447190424368FIDE+concept+privaatrechtelijke+handhaving+%28finaal+november+2015%29.pdf>.

⁶¹² *Id.*

⁶¹³ See Access to Civil Procedure Abroad § 8.9.3 (Henk J. Snijders ed., 1996).

⁶¹⁴ Articles 25(2) and 25(3) of the Code of Conduct for the Dutch Bar (CCDB); Kortmann, *supra* at 22; see also Article 7.7 of the Dutch Regulation of the legal profession. For a report (in Dutch, but with an English summary) on European practices regarding attorneys’ fees, see Michael G. Faure, Ton Hartlieb, Niels Philipsen Resultaatgerelateerdebeloningssystemenvooradvocaten:Eenvergelijkendebeschrijving van beloningssystemenvooradvocaten in een aantal landen van de Europese Unie en Hong Kong [Result-Related Remuneration Systems for Lawyers: A Comparative Law Description of Remuneration Systems for Lawyers in a Number of E.U. Member States and in Hong Kong] (2006), available at <http://www.wodc.nl/onderzoeksdatabase/internationale-vergelijking-beloningssystemen-advocatuur.aspx>. Resultaatgerelateerdebeloningssystemenvooradvocaten:Eenvergelijkendebeschrijving van beloningssystemenvooradvocaten in een aantal landen van de Europese Unie en Hong Kong [Result-Related Remuneration Systems for Lawyers: A Comparative Law Description of Remuneration Systems for Lawyers in a Number of E.U. Member States and in Hong Kong] (2006), available at <http://www.wodc.nl/onderzoeksdatabase/internationale-vergelijking-beloningssystemen-advocatuur.aspx>.

Admitted to Trading on a Regulated Market, 2010 O.J. (L 327) 1, available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:327:0001:0012:EN:PDF>.

⁶⁰⁶ Kaal, *supra* at 182; de Jong, *supra* at 364.

⁶⁰⁷ Kaal, *supra* at 182; de Jong, *supra* at 364.

⁶⁰⁸ Articles 6:95 , 109 DCC; Jeroen S. Kortmann & Miriam C. Buieten, *Private Enforcement and Collective Redress in European Competition Law*, FIDE 2016 Questionnaire, 11 (Nov. 2015) available at <http://static1.squarespace.com/static/5574a2fae4b0083487121509/t/56425f98e4b07a45a8606924/1447190424368FIDE+concept+privaatrechtelijke+handhaving+%28finaal+november+2015%29.pdf>.

⁶⁰⁹ Article 6:98 DCC; Kortmann, *supra* at 11.

⁶¹⁰ Article 6:97 DCC; Kortmann, *supra* at 12.



is often preferable to litigation, and, as a general rule, lawyers' remuneration should always be reasonable taking into account all the circumstances of the case.⁶¹⁵

In the *Converium* case, the Amsterdam Court of Appeal dismissed an objection that U.S. class counsel would receive fees out of the settlement amount based on a contingency fee arrangement. The court pointed out that in the context of determining the fairness of a class settlement, the court can take into account customary U.S. fee practices, when U.S. law firms are involved and the legal services provided by them took place predominantly in the U.S. The court held that a fee amounting to 20% of the settlement amount was not unreasonable.

Similarities and Differences Between Group Action Mechanisms in the Netherlands and United States

In addition to the similarities concerning reliance and causation pleading standards described above, there are several other parallels between group actions in the Netherlands and class actions in the United States. Indeed, in some ways it appears that the Netherlands' expansive recovery regime hearkens back in spirit to the regime in the United States pre-*Morrison*. However, as discussed below, the proposed draft bill on Redress of Mass Damages in a Collective Action includes jurisdictional features similar to U.S. procedures post-*Morrison*.

Global Recovery and Settlement Procedures

Prior to *Morrison*, the United States functioned as an unofficial clearinghouse for the claims of investors injured by securities fraud no matter where they purchased their investments. Actions in the United States, once granted court approval, were opt-out in nature and binding on all class members, and class definitions were expansive, covering purchases of a defendant company's securities around the world. In the aftermath of *Morrison*, which dramatically limited the scope of the federal securities laws to only securities purchased on a U.S. exchange, investors who

purchased shares abroad were forced to seek recoveries in other jurisdictions.

The Netherlands settlement stichting regime has filled the void created by *Morrison* for investors, and appeals also to defendants given its potential for achieving "global peace." Like the old U.S. procedure, through a settlement stichting, claims may be settled regardless of where a company is based or incorporated and regardless of where investors purchased their securities. Indeed, the settlement stichting procedure has proven increasingly popular since 2010 (when *Morrison* was decided), as reflected above in the increase in settlement stichting actions and several more proposed settlement stichtings (including against Royal Imtech N.V., Vestas Wind Systems A/S, Tesco plc, and ABN AMRO Bank N.V.).

The U.S. and Netherlands settlement procedures also resemble one another. Similar to U.S. class action procedures, the terms of a settlement negotiated by a settlement stichting: (i) require court approval; (ii) offer an opportunity for shareholders to opt out; and (iii) are binding on shareholders who do not opt out. In addition, in determining if a settlement should be declared binding, the Amsterdam Court of Appeal considers the ability of the foundation to adequately represent the interested persons as well as the reasonableness of the settlement.⁶¹⁶ These considerations are similar to the factors considered by U.S. courts in approving a class action settlement.⁶¹⁷

However, unlike the U.S. procedure, the WCAM settlement mechanism relies solely on the voluntary participation of the parties in negotiating a settlement.

⁶¹⁶ Ruud Hermans & Jan de Bie Leuveling Tjeenk, *International Class Action Settlements in the Netherlands Since Converium*, Int'l Comparative Legal Guide to Class & Group Actions 2016, 8th ed., at 5.

⁶¹⁷ See, e.g., *In re Fuqi Int'l, Inc. Sec. Litig.*, No. 10-cv-2515, 2016 WL 736649, at *4 (S.D.N.Y. Feb. 19, 2016) (considering the typicality and adequacy of class representative pursuant to Rule 23 of the Federal Rules of Civil Procedure in considering the final certification of a settlement class); and *City of Detroit v. Grinnell Corp.*, 495 F.2d 448, 463 (2d Cir. 1974) (setting forth factors courts consider in evaluating substantive fairness of proposed class action settlements).

⁶¹⁵ Article 25(10) CCDB; Kortmann, *supra* at 22.



Normal jurisdictional rules apply in the context of actions to establish liability or damages. Dutch courts do not necessarily have jurisdiction when a company that is not domiciled or incorporated in the Netherlands or the injury or wrong did not occur there.

Differing Claims and Treatment for Investors

The settlement foundation regime in the Netherlands allows for a more expansive recovery than that available currently through a U.S. action also with regard to the types of investment transactions for which damages may be sought. Whereas claims pursuant to the Exchange Act are limited to investors who purchase or sell securities,⁶¹⁸ through a settlement stichting, investors who held securities during the relevant period and refrained from selling their investments due to alleged corporate misrepresentations may also seek a recovery. For example, the recently announced Fortis settlement provides for compensation for purchasers *and* holders of Fortis shares, though noting that their compensation amounts will differ.⁶¹⁹ So-called “holder claims” have long been rejected by U.S. courts.⁶²⁰

In addition, unlike in the United States where all class members recover on an equal, pro rata basis, the Netherlands permits different recoveries depending on the degree of involvement of settlement stichting class members. Specifically, the announcement of the Fortis settlement specifies that “the settling parties here ‘have agreed to take into account within the

compensation principles the concept of ‘Active’ and ‘Non-active’ Claimants,’” meaning claimants who initiated legal action and were involved in establishing the settlement stichting, “enduring membership, legal and/or administrative expenses,” and those who were merely absent members of the class.⁶²¹ This approach goes beyond the provision in the U.S. Private Securities Litigation Reform Act of 1995 allowing lead plaintiffs to seek the award of reasonable costs and expenses incurred while representing the class.⁶²²

The Proposed Bill to Expand the Scope of Liability Foundations

As noted above, the Netherlands Parliament is considering a bill that would enable a liability stichting to seek not just injunctive or declaratory relief concerning a defendant’s liability but also the recovery of damages. The vision for this new liability stichting framework is that it will be used in instances in which parties are unwilling to enter into negotiations or when negotiating parties fail to reach an agreement. The ability to seek damages will allow investors to increase pressure on defendants to settle an action.

Although a liability stichting is a form of collective opt-in action, if the bill is approved and certain prerequisites are met, as discussed below this device could yield a similar result to a U.S. opt-out class action. The bill also features an extraterritoriality provision that may have been inspired by *Morrison*.⁶²³

Prerequisites for Seeking a Damages Ruling

Pursuant to the proposed bill, a liability stichting must have a sufficient number of members to justify a damages proceeding.⁶²⁴ In addition, those group members “must not have other efficient and effective

⁶¹⁸ See *In re Citigroup Inc. Sec. Litig.*, 987 F. Supp. 2d 377, 383 (S.D.N.Y. 2013)(explaining that “one asserting a claim for damages based on the violation of [the Exchange Act] must be either a purchaser or seller of securities”) (quoting *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 749 (1975)); *see also id.*

⁶¹⁹ See Ageas Press Release, *Regulated information – Ageas, Deminor, Stichting Fortis Effect, SICAF and VEB reach agreement aiming at settling all Fortis civil legacies*, at p. 5 (Mar. 14, 2016), <https://www.ageas.com/en/press-release/ageas-deminor-stichting-fortiseffect-sicaf-and-veb-reach-agreement-aiming-settling-all>. (providing “compensation for both buyers and holders”).

⁶²⁰ See, e.g., *In re Citigroup*, 987 F. Supp. 2d at 380 (S.D.N.Y. 2013)(dismissing holder claims with prejudice “because [they] are not cognizable under the Exchange Act”); and *In re Bear Stearns Cos., Inc. Sec., Deriv., and ERISA Litig.*, 995 F. Supp. 2d 291, 314-15 (S.D.N.Y. 2014)(dismissing holder claims based on precedent barring such claims under New York law).

⁶²¹ See Ageas Press Release, *id.*

⁶²² 15 U.S.C.A. § 78u-4 (a)(4).

⁶²³ The proposal has been heavily criticized and may not be implemented in its current form if it receives approval. Hermans *supra*, at 5.

⁶²⁴ Dutch Consultation, *supra* (“The group of persons on whose behalf the entity brings the action must be of a size justifying the use of the collective damages action”).



means to get redress” and are required to have sought “to obtain redress from the person held liable amicably.”⁶²⁵

Potential for Results Similar to U.S. Actions

The proposed change to the liability stichting framework would empower investors to seek a ruling on liability and a determination of damages. Any settlement achieved as part of this opt-in litigation process could then be certified through WCAM procedures, transforming it into an opt-out settlement⁶²⁶ akin to the outcome achieved through a U.S. securities class action.

This proposed procedure would provide stichting members with the sort of leverage U.S. classes have in seeking a recovery from public companies. One commentator has called this change “radical” in that, defendants will no longer have the option of declining to settle after a liability ruling in favor of facing individual lawsuits by stichting members; defendants will now face a damages ruling if they refuse to settle with a liability stichting, forcing a resolution with class-wide implications.⁶²⁷

Notably, however, the bill would impose several hurdles on liability stichting members prior to allowing them to seek a damages ruling from the court.⁶²⁸ The steps include several opportunities for court-directed settlement discussions and mediation.⁶²⁹ The inclusion of these many preconditions in the process reflects an intent to prevent abusive claims and balance the burdens on the parties.⁶³⁰

Under the proposed regime, a damages ruling will only be delivered as a last resort.⁶³¹

Extraterritoriality Provision

The proposed bill contains a limitation on extraterritorial application that echoes *Morrison*. In order for a liability stichting to pursue a damages claim, there must be a nexus to the Netherlands, either: (1) the defendant should have its domicile or residence in the Netherlands; (2) the majority of the interested parties in the stichting should be residents of the Netherlands; or (3) the events that give rise to claim should have occurred in the Netherlands.⁶³²

This provision limits the ability of foreign parties to seek collective compensatory relief in the Netherlands and backpedals from the broad extraterritorial jurisdiction approach endorsed by the WCAM procedure, which has been the subject of much criticism.⁶³³ Indeed, the bill’s explanatory memorandum prohibits a Dutch court from exercising jurisdiction over a damages action brought by a liability stichting even when both parties have agreed that Dutch law is controlling in the dispute—a prohibition that recalls the U.S. Supreme Court’s ruling in *Morrison*.⁶³⁴

⁶²⁵ *Id.*

⁶²⁶ *Hermans, supra*, at 5.

⁶²⁷ Brechje van der Velden, *Radical changes proposed to Dutch class action system* (July 7, 2014), <http://www.allenoverby.com/publications/en-gb/european-finance-litigation-review/northern-europe/Pages/Radical-changes-proposed-to-Dutch-class-action-system.aspx>.

⁶²⁸ See Dutch Consultation, *supra* (outlining five steps to the proposed framework for seeking a damages ruling from a court).

⁶²⁹ *See id.*

⁶³⁰ *See id.*

⁶³¹ A damages ruling in a collective action is considered particularly complex as an analysis of damages may involve questions that can often only be answered on an individual basis. See Xandra E. Kramer, *Securities Collective Action and Private International Law Issues in Dutch WCAM Settlements: Global Aspirations and Regional Boundaries*, 27 Pac. McGeorge Global Bus. & Dev. L.J. 2014, 240 (Mar. 1, 2014).

⁶³² Xandra Kramer, *Dutch draft bill on collective action for compensation – a note on extraterritorial application*, Conflict of Laws.net (Nov. 20, 2014), <http://conflictflaws.net/2014/dutch-draft-bill-on-collective-action-for-compensation-a-note-on-extraterritorial-application/>.

⁶³³ *Id.*

⁶³⁴ *Id.*

N. SOUTH KOREA



Overview

Korea enacted new legislation providing for class actions against relatively large companies commencing on January 1, 2005 (and other companies from January 1, 2007).⁶³⁵ The Securities Related Class Action Act (the SRCAA) was enacted to improve transparency in corporate management as well as to protect the interests of minority shareholders. Such improvements were thought to be especially needed after the Asian financial crisis of 1997-1998 revealed significant weaknesses in the government-backed, family-dominated conglomerates known as “chaebols” that are a distinct feature of Korea’s post World War II economy.⁶³⁶ These weaknesses included a lack of concern for minority shareholders’ rights, which the SRCAA is meant to address.⁶³⁷

As described in more detail below, class actions under the SRCAA are available for a limited number of statutorily prescribed causes of action. In terms of certification requirements, the action must consist of 50 or more class members holding in aggregate 0.01 percent or more of the issued and outstanding shares of the defendant company, and the claims of the class members must involve common questions of law or fact.

The first reported securities fraud class action suit was filed in April 2009 by 1,700 shareholders against Jinsung, a KOSDAQ-listed maker of machine parts, for losses allegedly caused by accounting fraud. The case settled out of court in January 2010 for approximately \$2.5 million.⁶³⁸

Since then, only six additional cases have been brought under the SRCAA. The most recent

⁶³⁵ Stephen J. Choi, The Evidence on Securities Class Actions, University of California At Berkeley School of Law, Public Law and Legal Theory Research Paper Series, 2004.

⁶³⁶ Dae Hwan Chung, Introduction to South Korea’s New Securities-Related Class Action, 30 J. Corp. L. 165, 166-67 (2005) (“Dae”).

⁶³⁷ *Id.*

⁶³⁸ U.S. Department of State, Bureau of Economic, Energy and Business Affairs, 2011 Investment Climate Statement—South Korea (March 2011), available at <http://www.state.gov/e/eb/rls/othr/ics/2011/157359.htm>.



reported case was filed in 2014, against embattled chaebol Tong Yang Group, in connection with sales of fraudulent corporate bonds to approximately 40,000 retail investors. (Tong Yang Group's former chairman was sentenced to seven years in prison for pressuring his staff to sell the bonds, and one employee even committed suicide in the wake of the massive losses suffered by her customers.)⁶³⁹ Interestingly, the lawsuit also names financial regulators as defendants, for failing to prevent the losses despite knowledge that Tong Yang Group was not creditworthy.⁶⁴⁰

Financial Investment Services and Capital Markets Act

In 2007, Korea enacted the Financial Investment Services and Capital Markets Act (FSCMA) to replace separate regulations governing securities, derivatives and asset management. Further reforms are underway that would apply to hedge funds, private equity funds and other private funds. This Act has been called a deregulatory move that consolidates power of several agencies and laws into one. The law has been repeatedly amended since. The FSCMA repeals the long-standing Securities and Exchange Act of 1962 ("SECA").⁶⁴¹ Many of the same liabilities are found in FSCMA, but with modifications such as those found in the U.S. Private Securities Litigation Reform Act of 1995 relating to forward looking statements.⁶⁴² Other sections of the FSCMA refer back to the older SECA as still applying. For example, Section 197 of the SECA still applies to auditors. The term "protection of investors" is scattered throughout the FSCMA.

⁶³⁹ See, e.g., The Korea Times, *Tongyang investors to take fall*, Oct. 4, 2013, available at http://www.koreatimes.co.kr/www/news/biz/2013/10/123_143789.html (last accessed April 29, 2016); The Korea Times, *Tongyang deceived customers on bonds*, Dec. 12, 2013, available at http://www.koreatimes.co.kr/www/news/biz/2013/12/488_147740.html (last accessed April 29, 2016); Yonhap News Agency, *Tong Yang victims sue firm, gov't over losses*, Jan. 21, 2014, available at <http://english.yonhapnews.co.kr/national/2014/01/21/6/0302000000AEN20140121006200315F.html> (last visited April 29, 2016).

⁶⁴⁰ News Agency, *Tong Yang victims sue firm, gov't over losses*, Jan. 21, 2014, available at <http://english.yonhapnews.co.kr/national/2014/01/21/6/0302000000AEN20140121006200315F.html> (last visited April 29, 2016).

⁶⁴¹ See Article 2 FSCMA Addenda.

⁶⁴² See Article 162 (Liability for Damages due to Misstatements)

However, it appears that Presidential Decree can override the FSCMA in many instances "when taking into account the balance between the confidentiality, including corporate management, etc. and the protection of investors." This exception creates the dangerous possibility of watering down the FSCMA on a whim.

Possible Causes of Action Under the SRCAA

The SRCAA limits class actions to certain causes of action (which are themselves set forth in the above-described FSCMA):

Misrepresentation in a registration statement or prospectus;⁶⁴³

Misrepresentation in an annual, bi-annual, or quarterly report;⁶⁴⁴

Insider trading, market price manipulation, or other unfair trading practices;⁶⁴⁵

Fraudulent audits.⁶⁴⁶

Elements of a Claim Under the FSCMA

As for the underlying causes of action, there does not appear to be a "catch-all" provision similar to Section 10(b)/Rule 10b-5 in the U.S. Rather, the enumerated causes of action are more akin to the

⁶⁴³ SRCAA Article 3(1)1 (including claims under Article 125 of the FSCMA, which covers false statements made in registration statements and prospectuses). An English translation of the FSCMA is available on the Korean government website at: <http://www.fsc.go.kr/eng/lr/list03.jsp> (last visited April 29, 2016).

⁶⁴⁴ SRCAA Article 3(1)2 (including claims under Article 162 of the FSCMA, which covers false statements made in annual, bi-annual, and quarterly filings [or "business reports"], but excluding claims under Article 161 of the FSCMA, which covers business reports on material facts, similar to Form 8-K filings).

⁶⁴⁵ SRCAA Article 3(1)3 (including claims under Articles 175, 177, and 179 of the FSCMA, which cover insider trading, market price manipulation, and unfair trading respectively).

⁶⁴⁶ SRCAA Article 3(1)4 (including claims under Article 170 of the FSCMA, which covers auditor liability).



Securities Act of 1933, in that they largely apply to statements made in prescribed contexts.⁶⁴⁷ Like Securities Act claims, they do not appear to require a plaintiff to demonstrate scienter, and provide for due diligence, knowledge, and negative causation defenses.⁶⁴⁸ Also like the Securities Act, liability is limited to enumerated statutory defendants.⁶⁴⁹

The text of Article 162, one of the possible causes of action, is reproduced at the end of this section.

Opt-In vs. Opt-Out, and Other Notable Procedural Considerations

Securities-related class actions are opt-out. The following is a summary of the procedure.⁶⁵⁰

After a complaint is filed with a court, the court should make a public announcement of the lawsuit and, thereafter, approve a lead plaintiff on behalf of the class. If the representative party does not adequately represent the interests of the class as a whole, or should there be any other relevant cause, the court may, according to its authority or on application by the other party, prohibit the furtherance of the suit by the lead plaintiff. Any lead plaintiff or lead counsel who has

served as lead plaintiff or lead counsel three or more times in the last three years may not act as lead plaintiff or lead counsel.

The court must notify individual class members and also publish in a national newspaper any decision to approve a securities-related class action, any modification to the range of class members, any withdrawal of appeal, or any final judgment. Prior to making decisions related to withdrawal of suit, settlement, or relinquishment of a damage claim, the court must notify the class members and provide an opportunity to testify.

The judgment of the court will bind the lead plaintiff and those who are members of the class, but any class member who wishes to be excluded from the judgment must file a written declaration of exclusion with the court.

A class member, within the designated period, should report his or her claim with the distributor. Any class member who is not able to report the claim with the distributor within the designated time period may report the claim within one month after the event that caused the failure to report has been concluded, but only if the failure to report is not imputable to the member's own fault.

Notably, it appears that class members can only opt-out pursuant to an “opt-out notice” published in the period of time after a class has been certified (or a class definition has been modified by the court).⁶⁵¹ There does not appear to be a mechanism for opting out after settlement or judgment.⁶⁵² Another notable procedural consideration is that the class-certification order is immediately appealable as of right, creating the

⁶⁴⁷ The broadest cause of action would seem to be for “unfair trading” under Articles 178 and 179 of the FSCMA. Article 178 makes it a violation to (1) use an “unfair means, scheme, or trick,” or (2) to “attempt[] to earn money or any interest in property, by using a document containing” material misstatements or omissions, or (3) use “an inaccurate market price with an intention to attract another” into a transaction. It also makes it a violation to “disseminate a rumor … with an intention to trade or make any other transaction in financial investment securities or attempt to cause a fluctuation in the market price.”

⁶⁴⁸ See, e.g., Article 162 of FSCMA, providing that “a person … shall not be liable if he/she proves that he/she was unable to know such fact although he/she exercised reasonable care, or that the [plaintiff] knew the fact at the time he/she acquired or disposed of the securities,” and that “a person … shall not be liable for partial damages, if he/she proves that all or part of the damages sustained by the claimant were not caused by” the misstatement.

⁶⁴⁹ See, e.g., FSCMA Articles 125, 162.

⁶⁵⁰ Dae Hwan Chung, Introduction to South Korea’s New Securities-Related Class Action, 30 Iowa J. Corp. L. 165, 171-172 (2004).

⁶⁵¹ See SRCAA Articles 18, 27, and 28 (specifying opt-out procedures).

⁶⁵² See generally SRCAA, Chapter IV Distribution Procedure (no mention of opt-out procedures).



potential for substantial delay before merits proceedings can begin.⁶⁵³

In general, it takes several months to obtain certification of a class, a prerequisite for initiating a class action in South Korea. Because class certification decisions by the trial court can be appealed to an appellate court, it is possible that several years will pass before proceedings begin on the merits.⁶⁵⁴ Once a class is certified, the case process is similar to other civil actions.⁶⁵⁵ Typically, it takes one to two years for the court to complete the proceedings and issue its orders on disputes involving securities claims.⁶⁵⁶

Similar to class litigation in the U.S. and other common law jurisdictions, there must be a certifiable class with claims involving common questions of law and fact.⁶⁵⁷ The suit must involve 50 or more class members, and the class needs to be certified by the court.⁶⁵⁸ As for the degree of commonality required, the SRCAA merely states that “[a]s a claim for compensation of loss under [the enumerated causes of action], the legally or actually material counts shall be common to all members of the class.”⁶⁵⁹ It is unclear whether this standard merely requires the class members to have the same cause of action, a relatively low bar, or whether it requires a higher degree of commonality, like the predominance requirement of Rule 23(b)(3).

Also, the SRCAA provides that no attorney may serve as lead counsel or lead plaintiff on a class action suit if he or she has served as lead counsel or lead plaintiff on three or more class action suits in the prior three years, unless the court makes an express finding that the prohibition should not apply.⁶⁶⁰

⁶⁵³ SRCAA Article 15(4) (“An immediate appeal may be raised” of the court’s rulings regarding the permission of a securities-related class action lawsuit).

⁶⁵⁴ See Chung/Seo/Kim, *supra*.

⁶⁵⁵ *See id.*

⁶⁵⁶ *See id.*

⁶⁵⁷ See Jin-Yeong Chung, Sungjean Seo, and Dong-Wook Kim, Class/collective actions in South Korea: overview, Practical Law: Global Guide 2015/16 – Class Actions, <http://us.practicallaw.com/5-617-3110?source=relatedcontent> (“Chung/Seo/Kim”).

⁶⁵⁸ *See id.*

⁶⁵⁹ SRCAA Article 12(1)2.

⁶⁶⁰ SRCAA Article 11.

Basics of Filing a Claim and Litigation

The following are the basic steps for filing a claim and litigation:⁶⁶¹

File a written complaint with a district court with the following documents attached: (i) power of attorney properly notarized and translated; and (ii) If you and/or Defendant are corporations, commercial registry extracts of Defendant corporation and a “certificate as to corporate nationality,” properly notarized and translated.

Pay a court stamp fee to file a lawsuit. The amount is usually around 0.5 percent of the claim amount, and you can pay this amount by affixing revenue or payment stamps (a stamp showing the amount you paid to file a lawsuit) in the required amount to the Complaint document.

If you have no address, office, or other place of business in Korea, (and the Defendant requests it), the court will order that you provide security for litigation costs. The purpose of this security amount is to secure the Defendant’s claim for reimbursement of the litigation costs expended by Defendant should you lose the case.

Loser Pays Model

The basic rule in South Korea is that losing parties (whether plaintiffs or defendants) are compelled to pay the litigation costs for both parties.⁶⁶² However, the amount that a losing party must reimburse a winning party for legal fees is capped by a formula that depends on the amount of money won in the lawsuit; thus, for

⁶⁶¹ Hoon Lee, Jipyong & Jipyong, Filing a Lawsuit in Korea: Overview, Korealaw.com http://www.korealaw.com/sub/information/boardView.asp?brdId=litigation&brdIdx=43&gotopage=1&search=&search_string=_.

⁶⁶² Gyooho Lee, Cost and Fee Allocation Rules in Korean Civil Procedure, 10 J. KOREAN L. 65, 69 (2010).



lawsuits involving very small sums, a winning party can seek reimbursement for attorneys' fees not in excess of 8 percent of the amount in controversy, while in very large lawsuits, a winning party can seek reimbursement for attorneys' fees not in excess of 0.5 percent of the amount in controversy.⁶⁶³ Losing parties are also responsible for paying the filing fees of the winning party. A losing party must also pay the winning party's expenses in collecting evidence.⁶⁶⁴

Extraterritorial Jurisdiction

The Financial Investment Services and Capital Markets Act (FSCMA), which incorporates the old regulations governing securities, derivatives and asset management, including the SECA, applies extraterritorially so long as there are effects on Korea-traded securities:⁶⁶⁵

Article 2 (Application to Foreign Activities): This Act shall apply to any activity conducted in the foreign jurisdiction where such activity affects the domestic market.

Funding the Litigation – Contingent Fee Arrangements

Contingency fee arrangements are allowed and common in civil cases in South Korea, including family law cases.⁶⁶⁶ (They are also allowed even in criminal cases, unless the arrangements are judged by

the court to be unfair).⁶⁶⁷ Perhaps because of the low ratio of lawyers-to-population, pure contingency fee arrangements are not common; lawyers are usually paid retainer fees before commencing a lawsuit.⁶⁶⁸ The usual range of contingency fees is between 5 and 10 percent of the amount won or settled for.⁶⁶⁹

Notably, the SRCAA requires that an “agreement on lawyers’ fees” be included with the application for class certification.⁶⁷⁰ The SRCAA authorizes the court to reduce lawyers’ fees, and also makes such a reduction immediately appealable.⁶⁷¹

Fraud on the Market Theory

There is no published information suggesting that Korea has adopted a fraud-on-the-market theory for securities class actions. And, although reliance is not an explicit element of the SRCAA-eligible misstatement-related causes of action, causation is. For instance, Article 162 of the FSCMA provides that “persons shall be liable for damages sustained by a person who acquired or disposed of securities … *due to a* false description or representation of a material fact” in a required business report.⁶⁷² Further, unless the SRCAA requires “predominance,” the lack of a fraud-on-the-market theory may not be that problematic, given that whatever individualized causation issues may exist, the question of whether defendants made material false statements will be common to the class, potentially satisfying the commonality requirement found in SRCAA Article 12(1)2.

Given the statutory language, defendants may raise arguments that plaintiffs’ losses were not “due to” defendants’ misstatements on any number of theories,

⁶⁶³ *Id.* at 70–71.

⁶⁶⁴ *Id.* at 73.

⁶⁶⁵ See Kun Young Chang, *Extraterritorial Application of the Korean Capital Markets Act: Lessons from Securities Regulations in the United States*, Abstract, 23 Asia Pacific L. Rev. 1 (2015) (“The Capital Markets Act of Korea has a provision expressly recognizing the extraterritoriality of the Act. However, the question still remains how far the reach of the Act extends to cover overseas activities. ... [T]his article proposes a two-tiered approach for discerning the extraterritorial scope of the antifraud rules under the Capital Markets Act. Although the Capital Markets Act has various categories of antifraud provisions, it is still unclear to what extent these provisions may be applicable in the context of transnational securities fraud. Through consideration of the merits of the current regulatory structure in the United States, this article suggests that a more restrictive view be taken toward suits initiated by private claimants, but that a more permissive view be taken toward enforcement proceedings by public regulators.”).

⁶⁶⁶ Gyooho Lee, *Cost and Fee Allocation Rules in Korean Civil Procedure*, 10 J. KOREAN L. 65, 85 (2010).

⁶⁶⁷ *Id.*

⁶⁶⁸ *Id.*

⁶⁶⁹ *Id.* at 86.

⁶⁷⁰ SRCAA Article 9(1)7.

⁶⁷¹ SRCAA Article 44(3)-(4).

⁶⁷² FISCMA Article 162(1) (emphasis added). The English translation of Article 125 of the FISCMA, covering registration statements, is grammatically confusing; it provides that persons shall be liable for “damages inflicted upon any person as a result of acquiring securities by including a false description or representation of any material fact.” Nevertheless, a causal link seems required.



including that they would have transacted regardless of defendants' misstatements, or that plaintiffs did not rely on the market price, or that the market was inefficient and therefore did not incorporate defendants' misstatements.

Regulatory Environment for Securities Litigation

During the last decade, Korea has taken to restructuring its financial laws and institutions. Liabilities to market participants, including auditors and financial institutions that audit public companies and sell their securities have been enacted. Currently, Korean policy seeks to strengthen confidence in Korea's capital markets and, therefore, investors may expect support from regulatory agencies.

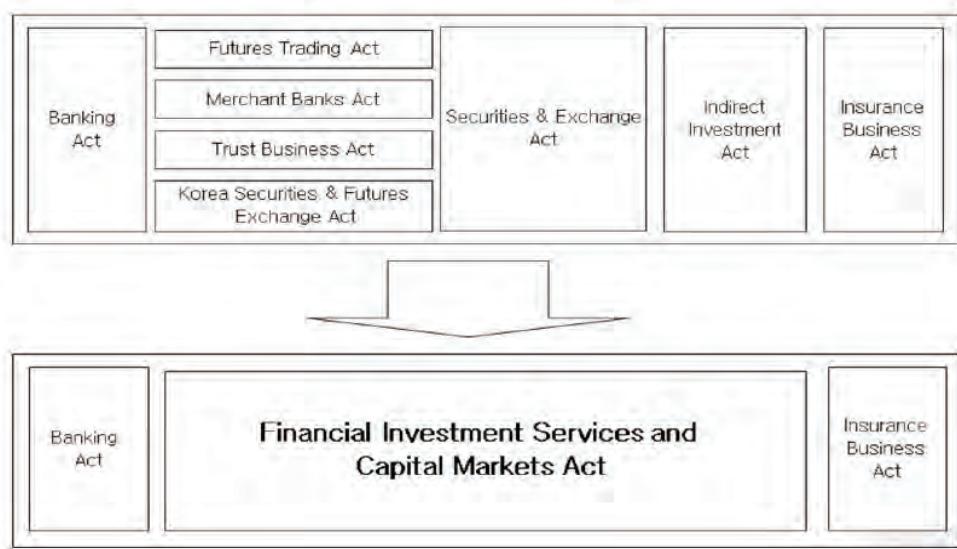
When the FSCMA was implemented on February 4, 2009, securities companies under the Securities and Exchange Act, futures companies under the Futures Trading Act, asset management companies, investment advisory companies, and discretionary investment companies under the Act on Business of Operating Indirect Investment and Assets, and trust companies under the Trust Business Act were consolidated into Financial Investment Business Entities under the FSCMA, which governs entry and business activities.⁶⁷³ In addition to the provisions on financial investment businesses, FSCMA provides for disclosure of financial investment instruments issuers and the functions and the roles of financial investment entities, such as the Korea Exchange (KRX) and the Korea Financial Investment Association (KFIA), to ensure fair and equitable pricing and trading of financial investment instruments. Companies listed on the KRX are required to file annual and quarterly reports with the FSC/FSS and the KRX as

well as ongoing disclosures on any transaction or event

that has material impact on their business soundness or financial conditions.⁶⁷⁴

The Act on External Audit of Stock Companies (AEASC) provides for accounting and auditing regulations. Specifically, AEASC authorizes the FSC/FSS to establish accounting and auditing standards and to enforce filing of financial statements in compliance with the accounting standards and audit in accordance with the auditing standards. AEASC requires auditors to maintain client confidentiality and to report fraud to shareholders. Auditors are liable for any damages caused by negligence in performing audits or failure to disclose material information.⁶⁷⁵

Financial Investment Services and Capital Markets Act



According to the State Department's 2014 Investment Climate Statement, these new reforms were long overdue and, in fact, may not have yet proven effective:

Corporate Governance and Investment Decision-Making:

Investors and financial markets remain wary of corporate governance in Korea despite significant improvements since the 1997-98 Asian financial crisis.

⁶⁷³ Financial Supervisory Service, Financial Supervisory System in Korea, 16 (December 2008).

⁶⁷⁴ *Id.* at 16-17.

⁶⁷⁵ *Id.* at 17.



Concerns about corporate governance often reduce the price to earnings ratios to levels lower than comparable companies elsewhere. Korean policy makers acknowledge that foreign investors often exact a “Korea Discount” when

dealing with Korean companies or in making investment decisions. Large gaps continue to exist between the ownership and control of a significant number of firms in Korea, with many of Korea’s conglomerates (*chaebol*) still controlled by their founding families, despite the family’s relatively small ownership stakes. Increasing participation by foreign investors and stockholders, requiring more independent boards of directors, modernizing business-government relations, and infusing professionalism in the corporate culture would greatly help improve corporate governance.⁶⁷⁶

The Financial Supervisory Service, along with delegation to the Securities and Futures Commission supervises, examines and investigates financial institutions upon matters delegated to the Service by the new Financial Services Commission (FSC). More information about the Financial Supervisory Service is available at <http://www.fsc.go.kr/eng/>.

Similarities to and Differences with U.S. Class Action System

There are several aspects of the system of securities class actions under the SRCAA that are similar to the U.S. class action system. As in the U.S., following *Morrison*,⁶⁷⁷ claimants in South Korean securities matters may reside outside the country, but their losses must be related to securities traded on the Korean Securities Exchange.⁶⁷⁸ As noted above, the

claims permitted by the SRCAA are similar to those provided in the Securities Act, and the Korean statute of limitations also resembles that of the Securities Act—one year from the date the claimant became aware of the unlawful act, and three years from the date of the unlawful act.⁶⁷⁹ In addition, because there are no special rules regarding costs or contingency fees, contingency fee arrangements for claimants’ counsel are permitted.⁶⁸⁰

Another similarity between South Korean collective actions and U.S. class actions is that claimants’ damages are calculated as the difference between the price paid for the security and the price at time of sale or at the time the proceedings are resolved.⁶⁸¹ Furthermore, as in the United States, before a South Korean class action settlement may be approved, the court must notify the class to allow for any objections and the opportunity for class members to opt-out.⁶⁸²

However, there are notable differences in South Korea’s class action system under the SRCAA. Document discovery is only permitted in South Korean collective actions once the complaint has been filed and requires leave of court.⁶⁸³ Often in collective actions in South Korea, plaintiffs must rely on the documents obtained by government prosecutors or other governmental authorities.⁶⁸⁴ Second, class certification is a necessary prerequisite for a South Korean collective action to proceed.⁶⁸⁵ Third, unlike in U.S. securities litigation, parties to South Korean securities actions may request that the court appoint experts to advise the court and to establish pertinent facts.⁶⁸⁶ Finally, the South Korean approach to litigation costs differs from the U.S. approach. Unlike in the United States, South Korean courts typically order the losing party to bear the costs of the litigation, with such costs being subject to a statutory scale set by the court.⁶⁸⁷ Significantly, plaintiffs would be liable for these costs if they fail to

⁶⁷⁶ See *id.*; see also 15 U.S. Code § 77(m).

⁶⁷⁸ See *id.*; see also 15 U.S. Code § 78(u)-4.

⁶⁷⁹ See *id.*

⁶⁸⁰ See *id.*; see also Hannuri, *supra*.

⁶⁸¹ See Chung/Seo/Kim, *supra*.

⁶⁸² See Hannuri, *supra*.

⁶⁸³ See *id.*

⁶⁸⁴ See Chung/Seo/Kim, *supra*.

⁶⁸⁵ See *id.*

⁶⁸⁶ See Chung/Seo/Kim, *supra*.

⁶⁸⁷ See Chung/Seo/Kim, *supra*.



establish loss causation even if the court found their claims meritorious.⁶⁸⁸

Text of FSCMA Article 162 (Liability for Damages due to Misstatements)

(1) Any person falling under the following subparagraphs shall be liable for damages where a person who has acquired or disposed of the securities (including securities deposit receipts related to such securities and other securities prescribed by the Presidential Decree; hereafter in this Article, the same shall apply) issued by a reporting corporation sustains damages because an annual report, semi-annual report, quarterly report, or report on material matters (hereinafter referred to as "annual reports, etc.") under Article 159 (1) and accompanying documents thereof (excluding an audit report prepared by an accounting auditor) contains any misstatement or omission of material matters: provided that the same shall not apply to cases where a person who is liable for the compensation proves that he/she could not have known such misstatement or omission despite his/her due diligence, or where the person who has acquired or disposed of such securities knew the fact at the time of the acquisition or disposal: <Amended on Feb. 3, 2009>

1. A person who has submitted the annual reports, etc., and directors of the reporting corporation at the time of the submission thereof;
2. A person falling under any subparagraph of Article 401-2 (1) of the Commercial Act, who has [been] instructed to prepare or has been in charge of the annual reports, etc.;
3. A person prescribed by the Presidential Decree as certified public accountant, appraiser, credit-

rating specialist, etc. (including any organization to which each of them belongs) who has agreed to prove the authenticity or accuracy of the entries of the annual reports, etc. or accompanying documents thereof and [bears] a signature; and

4. A person who has agreed to enter his/her opinion on the assessment, analysis, and confirmation in the entries of the annual reports, etc. and accompanying documents and has verified the entries thereof.

(2) Notwithstanding paragraph (1), any person falling under the subparagraphs of paragraph (1) shall not be liable for damages where forward-looking information is entered or indicated pursuant to each of the following subparagraphs: provided, that the same shall not apply to cases where the person who has acquired or disposed of the securities concerned has been unaware of the misstatement or omission of material matters at the time of the acquisition and disposal and cases where it has proven that any person falling under each subparagraph of paragraph (1) is responsible for the misstatement or omission by intention or by recklessness:

1. The entry or indication is required to be specified as forward-looking information;
2. The grounds for the assumptions or judgments of the predictions or forecasts are required to be specified;
3. The entry or indication is required to have reasonable grounds or assumptions; and
4. Bespeaks cautions that the projections may differ from the actual result are required to be specified.

⁶⁸⁸ See Hannuri, *supra*.



(3) *The amount to be compensated pursuant to paragraphs (1) and (2) shall be the difference between the amount actually paid or received by the claimant for the acquisition or disposal of the securities concerned and the amount (limited to paragraph (1) in the case of the disposal) falling under either of the following subparagraphs:*

1. *The market price (where no market price is available, referring to an estimated price at which the securities would be disposed of) of the securities concerned when the argument to make claims for compensation pursuant to paragraphs (1) and (2) is concluded; or*
2. *Where the disposal is made before the conclusion of the argument under subparagraph 1, the price at which the securities is disposed of.*

(4) *Notwithstanding paragraph (3), where a person liable for the damages pursuant to paragraphs (1) and (2) proves that a claimant has sustained any or all of the damages without regard to any misstatement or omission of material matters, the person is not bound to compensate for the damages of such part.*

(5) *The claims for damages under paragraphs (1) and (2) shall be extinguished unless the claimant exercises his/her right of claim within the one year from the date on which he/she has discovered the fact or within the three years from the date when the annual reports, etc. have been submitted.*

O. SPAIN



Overview

In Spain, collective actions are limited to proceedings for the protection of consumers. Since 2000, the Spanish Law of Civil Procedure has provided mechanisms whereby groups and certain legal entities may bring actions on behalf of consumers where a number of individuals have suffered losses due to the same event.⁶⁸⁹

The remedies available by means of collective redress are damages.⁶⁹⁰

Two types of collective action may be brought in Spain. For the first type, actions to protect the collective interest (“collective actions”), groups representing a majority of the pool of consumers may bring collective actions whenever the members of such groups are identified or are easily identifiable.⁶⁹¹ In those cases, collective actions can be brought by consumer associations and certain authorized legal

⁶⁸⁹ In 2000, the *Ley de Enjuiciamiento civil* (Civil Procedure Act or “LEC”) introduced a specific litigation procedure granting standing for the protection of rights and interests of consumers and users in Art. 11 LEC. Prior to 2000, collective actions were mainly named by Art. 7.3 of the *Ley Orgánica 6/1985, de Julio 6, del Poder Judicial* (Organic Law 6/1985, of July 6th, of Judicial Powers; LOPJ). María Paz García Rubio & Marta Otero Crespo, Report II on collective redress, Collective redress in Spain in light of the EC Recommendation, British Institute of International & Comparative Law (Nov. 2014), available at <http://www.collectiveredress.org/collective-redress/reports/spain/overview>.

⁶⁹⁰ Quantification of damages is mandatory. Prof. C. Van Heerden, University of Pretoria (South Africa), *Redress for Consumers in terms of the Consumer Protection Act 68 of 2008: A Comparative Discussion*, JICLT (2011) 6(2): 131-144.

⁶⁹¹ Linklaters, *Collective actions across the globe – a review*, at 20 (2011) available at: http://www.linklaters.com/pdfs/mkt/london/1103_Collective_actions.pdf. See also Csóngor István Nagy, Comparative Collective Redress From a Law and Economics Perspective: Without Risk There is No Reward!, 19 Colum. J. Eur. L. 469, 488 (2013).



entities.⁶⁹² The second type of collective action, actions for the protection of widespread or diffuse interests of consumers, may be brought if the members of the group are unknown or difficult to identify and must be filed by a sufficiently representative consumer association (such as the Spanish Council of Consumers).⁶⁹³

The Spanish Civil Procedure Act (Ley 1/2000, de 7 de enero, de Enjuiciamiento Civil or “LEC”) provides procedures for the protection of consumer collective interests based on groupings of specialties, such as telecommunications services, financial services, and product liability. The LEC has been criticized because of an absence of systemic and consistent parameters.⁶⁹⁴ There is a lack of harmonized and methodical approach to collective redress mechanisms in Spain due to the contradictions and inconsistencies among the rules of the LEC.⁶⁹⁵

Opt-In vs. Opt-Out

Spain cannot be defined as either an opt-in or opt-out jurisdiction. Individual consumers will be bound by the court decision no matter what they do.⁶⁹⁶ There is no need for individuals to agree to participate in collective actions brought by groups, associations or legal entities. If individuals choose to opt in, they will be able to claim their damages within a certain time, depending on the type of collective action. If individuals remain out of the proceedings, they will still be bound by the decision and able to benefit from it by filing a claim for damages with the court enforcing the judgment.

⁶⁹² *Id.*

⁶⁹³ *Id.*

⁶⁹⁴ Prof. C. Van Heerden, University of Pretoria (South Africa), *Redress for Consumers in terms of the Consumer Protection Act 68 of 2008: A Comparative Discussion*, JICLT (2011) 6(2): 131-144; see also Csongor István Nagy, *Comparative Collective Redress From a Law and Economics Perspective: Without Risk There is No Reward!*, 19 COLUM. J. EUR. L. 469, 488 (2013); María Paz García Rubio & Marta Otero Crespo, *Report II on collective redress, Collective redress in Spain in light of the EC Recommendation*, British Institute of International & Comparative Law (Nov. 2014), available at <http://www.collectiveredress.org/collective-redress/reports/spain/overview>.

⁶⁹⁵ *Id.*

⁶⁹⁶ Linklaters, *Collective actions across the globe – a review*, 20 (2011), available at http://www.linklaters.com/pdfs/mkt/london/1103_Collective_actions.pdf.

For this reason, Spanish law attempts to guarantee that individual consumers are aware of the proceedings and have the opportunity to join, support the position of the claimant, and seek their individual damages. This is achieved by giving notice (usually in newspapers) and in cases where the members of the group are identifiable, by requiring the claimant to send a letter to all affected consumers prior to filing the claim. Once proceedings have commenced, individual claimants can join the case. In cases where the members of the group are not easily identifiable, the proceedings will be stayed for two months while the claim is publicized. Potential claimants will only be able to come forward and join the claim during that period. Where the members of the group are identifiable, individuals can join the proceedings at any time.

If the court upholds the claim, it must determine which individuals are entitled to benefit from the award regardless of whether they joined the proceedings or remained out of the proceedings.⁶⁹⁷ The court will rule on the individual claims filed by affected consumers who joined the proceedings, and also hold whether other members of the group of affected consumers can benefit from the relief obtained by the claimant. If it is not possible to identify the beneficiaries of the award with sufficient certainty, the court will need to establish requirements that individuals must fulfill in order to be entitled to participate.

If the court rejects the collective action, all affected consumers will be bound by that decision whether they joined the proceedings or not. This determination will have a *res judicata* effect, as affected consumers will not be able to bring new actions against the defendant arising from the same claims.⁶⁹⁸

⁶⁹⁷ *Id.*

⁶⁹⁸ *Id.*



Possible Strategies to Bring Collective Actions in Spain

One strategy to bring a collective action in Spain is to obtain a court ruling on a few individuals that are representative of the class. This ruling will bind the class, and future claims can be brought under the original ruling.⁶⁹⁹ A good example of this is the *Bankia* case.

Bankia was formed in 2010 by consolidating seven regional savings banks, or cajas. During the consolidation, troubled loans were allegedly transferred to a separate government-controlled holding company. Bankia went public in July 2011, and more than 350,000 individual and institutional investors bought shares.⁷⁰⁰ In early 2012, Bankia stock dropped significantly after it required a government bailout and restructuring.

Two small investors filed suit against the directors and officers for failing to disclose the loan problems. The cases went up to the Tribunal Supremo de España (Supreme Court), which ordered Bankia in January 2016 to reimburse the investors for misleading them during its 2011 IPO. Under the ruling, the bank must pay one investor nearly €10,000 and the other nearly €21,000.⁷⁰¹ The Supreme Court held that Bankia's prospectus for its public stock offering in 2011 had contained "serious inaccuracies."⁷⁰²

Shareholders may recover all of their investment plus legal interest and the costs of the proceedings. With the Supreme Court's ruling, all of the shareholders who

file a claim will recover their losses.⁷⁰³ Following the Supreme Court's ruling, a collective action was filed by 660 Spanish investors seeking €6.3 million (about \$7 million), and more are expected to join.⁷⁰⁴ The bank is aware of €819 million of potential claims by affected investors.⁷⁰⁵

Another strategy to bring a collective action in Spain is to file a criminal complaint on behalf of the victims and join a civil action for damages to it. In Spain, the judicial system allows a prosecution to be filed by both the Public Prosecutor and by private persons.⁷⁰⁶ Criminal proceedings can be initiated *ex officio* (by the Public Prosecutor's Office, State Counsel, police or courts themselves) or by a party filing a formal complaint or criminal complaint.⁷⁰⁷ The court then decides if, on the basis of the relevant facts, the acts in question constitute an offence.⁷⁰⁸ A civil action may be joined to the criminal action.

Regulatory Environment for Securities Litigation

The Comisión Nacional del Mercado de Valores (CNMV) regulates the securities market in

⁶⁹⁹ 1/2000, January 7, Civil Procedure Act (Spain), Articles 11, 221, 222.3, 519; Linklaters, *Collective actions across the globe – a review*, 20 (2011), available at http://www.linklaters.com/pdfs/mkt/london/1103_Collective_actions.pdf.

⁷⁰⁰ *White Smoke for Bankia's Shareholders*, International Financial Litigation Network, available at <http://www.ifl-network.com/white-smoke-for-bankia-s-shareholders.html>.

⁷⁰¹ Kevin LaCroix, *Spanish Class Action is the Latest Collective Investor Action Filed Outside U.S.*, International D&O (Feb. 7, 2016), available at <http://www.dandodairy.com/2016/02/articles/international-d-o/spanish-class-action-is-the-latest-collective-investor-action-filed-outside-u-s/>; *White Smoke for Bankia's Shareholders*, International Financial Litigation Network, available at <http://www.ifl-network.com/white-smoke-for-bankia-s-shareholders.html>.

⁷⁰² Raphael Minder, *Spanish Supreme Court Orders Bankia to Repay 2 Investors in Its I.P.O.*, THE NEW YORK TIMES (Jan. 27, 2016), available at <http://www.nytimes.com/2016/01/28/business/spanish-supreme-court-orders-bankia-to-repay-2-investors-in-its-ipo.html?r=0>; see also, *Misled shareholders file class action lawsuit against Bankia*, THE LOCAL (Feb. 5, 2016), available at <http://www.thelocal.es/20160205/spains-bankia-sued-by-misled-shareholders-in-class-action-lawsuit>.

⁷⁰³ Business Crime 2016, International Comparative Legal Guides, available at <http://www.iclg.co.uk/practice-areas/business-crime/business-crime-2016/spain>.

⁷⁰⁴ *Id.*

⁷⁰⁵ *Id.*



Spain. The Securities Market Act creates liability “for any damages that may be caused to the owners of the securities acquired as a result of false information or omissions of relevant data from the prospectus or any other document that the guarantor must draw up.”⁷⁰⁹ The Securities Market Act provides that certain acts or omissions constitute very serious violations, including

- Launching public offerings for sale or subscription or listing without complying with the basic conditions set forth in the prospectus, where a prospectus is required, or omitting material data or including in the prospectus inaccuracies or false or misleading information where the amount of the offering or listing or the number of investors affected is material.⁷¹⁰
- Breach of the disclosure duties with intent to conceal or gross negligence, where the missing disclosure and the delay which occurred was material.⁷¹¹

The statute of limitations is five years for serious or very serious violations and two years for minor violations.⁷¹²

Spanish financial institutions are regulated by the Bank of Spain (Banco de España) under Act Number 26/1988 of 29 July, on Discipline and Intervention of Credit Institutions.

Criminal prosecution of misconduct resulting in counterfeiting the balance sheet or the books which caused damages to the company, to stakeholders or to third parties is available under Article 290 of the Spanish Criminal Code.

In Spain, civil liability may be claimed in criminal proceedings by the Public Prosecutor or by the

⁷⁰⁹ Act 24/1988, of 28 July, on the Securities Market, Article 28(3) (Spain). Consolidated unofficial English translation text provided by the CNMV (Last update July 2012), available at: http://www.cnmv.es/docportal/legislacion/leymercado/LMV_May2012_EN.pdf.

⁷¹⁰ Act 24/1988, of 28 July, on the Securities Market, Article 99(n) (Spain).

⁷¹¹ Act 24/1988, of 28 July, on the Securities Market, Article 99(p) (Spain).

⁷¹² Act 24/1988, of 28 July, on the Securities Market, Article 101 bis (Spain).

victims, who must act under the same representation, according to Article 103 of the Criminal Procedural Law.⁷¹³

Loser Pays Model

In Spain, the losing party will pay the costs (“loser pays” or English rule).⁷¹⁴ Legal costs in Spain are the resulting expenses from the proceedings and include lawyers and solicitors fees; publication of announcements that must be published during the proceedings; and experts’ fees.⁷¹⁵ The amount in legal fees that the losing party has to pay cannot exceed one-third of the amount claimed in the proceeding.⁷¹⁶ The losing party may allege that the costs are excessive or improper, and the court will decide the exact amount that has to be paid.⁷¹⁷

Funding the Litigation - Contingent Fee Arrangements

Lawyers and their clients can freely agree on the amount of legal fees, subject to ethical and unfair competition rules.⁷¹⁸ Contingency fees agreements are available.⁷¹⁹

⁷¹³ Marta Requejo, *Securities Class Actions and Extraterritoriality: a View from Spain*, Conflict of Laws (July 2, 2010), available at <http://conflictflaws.net/2010/securitiesclassactionsandextraterritorialityaviewfromspain/>.

⁷¹⁴ Fernando Gomez & Marian Gili, Country Report Spain, in EVALUATION OF THE EFFECTIVENESS AND EFFICIENCY OF COLLECTIVE REDRESS MECHANISMS IN THE EUROPEAN UNION, 8 (2008), available at http://ec.europa.eu/consumers/redress_cons/sp-country-report-final.pdf.

⁷¹⁵ *Id.*

⁷¹⁶ *Id.* at 9. Section 394.3 LEC.

⁷¹⁷ *Id.*

⁷¹⁸ *Id.*, Limits of legal fees are established by Section 394.3 LEC.

⁷¹⁹ Decision of the Supreme Court of 4 November 2008; see also the Decisions of the Supreme Court 357/2004, 13 May (RJ 2004, 2739) and 446/2008, 29 May (RJ 2008, 4164); María Paz García Rubio & Marta Otero Crespo, Report II on collective redress, Collective redress in Spain in light of the EC Recommendation, British Institute of International & Comparative Law (Nov. 2014), available at <http://www.collectiveredress.org/collective-redress/reports/spain/overview>.

Case Studies





Securities litigation outside the United States is on the rise. Prior to the U.S. Supreme Court’s decision in *Morrison*, only a handful of securities cases had been pursued outside the United States – most notably of which was the case against *Royal Dutch Shell*. Post *Morrison*, more and more cases have been filed and are being filed in various countries around the globe. A number of the earliest post-*Morrison* cases that were filed have now been resolved, providing important legal precedent and helping to further enlighten the investor community about their recovery options in a post-*Morrison* world. Below are brief overviews of the seminal cases that have been, or that are currently being, pursued either outside the United States or within the United States but utilizing state law or other creative strategies. The case studies of resolved cases appear first (in chronological order) followed by case studies of some ongoing litigation that will be interesting to watch over the next few years.

A. RESOLVED AND SETTLED CASES

Royal Dutch Shell (The Netherlands)

Royal Dutch Shell plc (“Shell”), one of the world’s largest petroleum production companies, is headquartered in the Netherlands and incorporated in the U.K. On January 9, 2004, Shell announced that it would have to reduce its “proved” oil and gas reserves by nearly 4 billion barrels – 20% of its proved reserves.⁷²⁰ The oil portion of the write-down alone represented \$135 billion in potential future revenue. Over the next three months Shell cut its reserves three more times. In total, by February 3, 2005 Shell had announced cuts to its previously announced proved reserves by approximately 6 billion barrels. Shell also twice restated its financial results for 2001 and 2002, and once for 2003, reducing its net income by hundreds of millions of dollars.

Numerous securities fraud actions were filed against Shell in 2004 in the U.S. District Court for the District of New Jersey. The action proceeded on behalf of Shell purchasers worldwide until a special master concluded based on an extensive evidentiary

record that the Court did not have subject matter jurisdiction over the claims of non-US investors. However, in April 2007, prior to that ruling becoming final, Shell announced that it had entered into a settlement of non-U.S. investor claims with a special purpose foundation under Dutch law. Ultimately, U.S. purchaser claims settled in the United States, while non-US purchaser claims were resolved through the Dutch legal proceedings. Foreign investors covered by the Stichting Shell Reserves Compensation Foundation shared in a \$352.6 million settlement, while domestic purchasers recovered an additional \$89.5 million. In addition, Shell also agreed to ask the SEC to distribute the \$120 million it had paid the SEC to investors.

The Shell settlement was a landmark development in global securities law. As discussed previously, the Dutch Act on Collective Settlement of Mass Damages (“WCAM”) was enacted in July 2005, giving Shell and European investors an ability to settle claims “on their home turf.”⁷²¹ The Settlement was ultimately approved by the Amsterdam Court of Appeal in May 2009. This was the first time that a Dutch court had declared a large settlement binding and approved an opt-out settlement similar to a U.S. class action; although at least one smaller settlement had been approved prior to the Shell settlement.

The settlement procedure did not actually provide investors with collective damage claims. The WCAM only provided a mechanism for the Dutch court to approve the settlement of the damage claims based upon Shell’s willingness to do so. For a collective settlement to be a viable option, the defendant must have a reason to be willing to agree to a collective settlement. That is most likely to occur when damage claims have been instituted (or reasonably threatened) in another jurisdiction (or in the Netherlands alleging violations that arise under separate Dutch laws). It is the threat of potentially expensive and ever growing litigation

⁷²¹ Kevin LaCroix, Does the Royal Dutch Shell Settlement Approval Portend a Rush of European Collective Actions? The D&O Diary (June 3, 2009), available at <http://www.dandodairy.com/2009/06/articles/securities-litigation/does-the-royal-dutch-shell-settlement-approval-portend-a-rush-of-european-collective-actions/>.

⁷²⁰ See <http://shellsettlement.com/index.php?page=history>.



that likely would provide the greatest motivation for a defendant to agree to a collective settlement. Litigation that is unlikely to be capable of being expanded (because of the expiration of a statute of limitations or for other reasons) to include many plaintiffs in most cases will not likely provide a sufficient incentive to cause a defendant to want to engage in a class-wide settlement.

Converium (The Netherlands)

Converium Holding (Switzerland) AG (now called SCOR Holding (Switzerland) AG) is a Swiss reinsurer, with common shares trading on the SWX Swiss Exchange and with ADRs listed on the NYSE. In October 2004, investors brought suit in the Southern District of New York alleging that the defendants had misrepresented the sufficiency of the company's loss reserves, which were hundreds of millions of dollars less than needed to cover Converium's exposure to reinsurance claims.

The claims of non-U.S. investors who had purchased their shares on the Swiss exchange were denied class certification (for lack of subject matter jurisdiction under the "conducts and effects" test in a pre-*Morrison* decision). After the dismissal, a Dutch foundation consisting of both non-U.S. investors and non-U.S. shareholder rights groups was established to pursue and to consummate a global resolution of the non-U.S. claims. The Dutch foundation was able to negotiate a \$58.4 million settlement on behalf of all shareholders in July 2010 and the settlement was effectuated using the Dutch WCAM procedure. As discussed above, the WCAM allows for collective resolution of claims on a global basis, but only once a settlement has been reached; but it does not provide a mechanism for establishing corporate (or other) liability or for assessing damages.

The settlement was preliminarily approved by the Amsterdam Court of Appeal on November 12, 2010. Final approval was granted on January 17, 2012.

The Converium settlement is notable because it was one of the earlier and more prominent uses of the WCAM mechanism. It is also notable for the Dutch

court's reasoning in approving the settlement, which, among other things, recognized that the Netherlands is the only EU legal system that allows for opt-out collective settlements, and expressly referred to the inability of U.S. courts to secure global relief due to the *Morrison* decision. Also significant is the fact that it was approved despite the fact that—as the Dutch Court recognized—the case had only a limited connection to the Netherlands. Indeed, the settlement was approved even though Converium's shares were traded on a Swiss stock exchange and not on a Dutch exchange; only a very small number of the investors in Converium, both in absolute terms and as a percentage of all of the investors in Converium were Dutch; and Converium was a Swiss corporation and had limited activity in the Netherlands. Some interpreted the decision to be a signal from the Dutch judicial system of its view of the extraordinarily broad applicability of the WCAM to settle litigation on a global basis.

One of the lingering questions after the Converium settlement was the extent to which the decision, and others like it, will be recognized in the rest of the EU, as well as European countries that are not part of the EU, such as Switzerland, Iceland, and Norway. As of this writing, no challenges appear to have been made by European courts, and the question remains unanswered.⁷²²

⁷²² See, e.g., Xandra E. Kramer, *Securities Collective Action and Private International Law Issues in Dutch WCAM Settlements: Global Aspirations and Regional Boundaries*, *Global Business & Development Law Journal*, Volume 27, Issue 2, pp. 235-279, 2014 (noting both praise and criticism for Converium and WCAM but not identifying any challenge from other European courts); see also Axel Halfmeier, *Recognition of a WCAM settlement in Germany*, *Nederlands Internationaal Privaatrecht* (NIPR), Issue 2, pp. 176-184, 2012, available at <http://www.nipr-online.eu/pdf/2012-265.pdf> (last accessed May 4, 2016) (arguing that German courts should recognize WCAM settlements).



Leighton Holdings (Australia)

Leighton Holdings is an Australian construction company. In April 2011, it announced more than A\$1.1 billion in write-downs relating to construction projects, causing it to project an A\$427 million loss for the year, despite having forecasted a net profit of A\$480 million just two months prior. Shares fell 14% on the news.⁷²³

Litigation funders and law firms specializing in representing plaintiffs immediately began investigating a potential securities fraud claim.⁷²⁴ In September 2011, an Australian law firm announced that it was seeking Leighton investors to join a proposed lawsuit.⁷²⁵

A lawsuit was commenced in October 2013 on behalf of approximately 2,400 investors. According to reports, the lawsuit had been ready to file months prior, but its filing was delayed in light of settlement discussions.⁷²⁶ On May 16, 2014, an A\$69 million (approximately \$52 million USD) settlement was reached. It was approved by the Federal Court of Australia on August 25, 2014. From the perspective of U.S. observers, numerous aspects of the case, and the settlement, are interesting. In particular, the facts that settlement discussions began *before* the formal class-action lawsuit was filed, and that the lawsuit was filed more than two years *after* the last “corrective disclosure,” are noteworthy. These facts contrast sharply with the process that is typical in U.S. securities class action, where customarily an investor class must survive a motion to dismiss before defendants will even begin to discuss settlement. Also notable is the fact that the law firm leading the litigation represented over 2,000 investors *before* filing the suit.

⁷²³ Gareth Hutchens, The Sydney Morning Herald, *New class action hit for Leighton* (Oct. 31, 2013), <http://www.smh.com.au/business/new-class-action-hit-for-leighton-20131030-2whfv.html>.

⁷²⁴ Tracy Lee, The Australian, *Leighton investors consider class action against the company* (Apr. 20, 2011), <http://www.theaustralian.com.au/business/leighton-investors-consider-class-action-against-the-company/story-e6frg8zx-1226041807649>.

⁷²⁵ Drew Cratchley, The Courier-Mail, *Lawsuit targets Leighton* (Sept. 2, 2011), <http://www.couriermail.com.au/ipad/lawsuit-targets-leighton/story-fn6ck2gb-1226127571231>.

⁷²⁶ Gareth Hutchens, The Sydney Morning Herald, *New class action hit for Leighton* (Oct. 31, 2013), <http://www.smh.com.au/business/new-class-action-hit-for-leighton-20131030-2whfv.html>.

Again, this sharply contrasts with U.S. practice, where class action law firms typically only represent one or just a handful of clients, who then vie for leadership of the case on behalf of the class.

These differences seem attributable at least in part to the fact that despite a statutory opt-out regime, Australian courts have apparently “allow[ed] classes to be defined in such a way that only those claimants who have retained a particular law firm and/or entered into an arrangement with a particular litigation funder are able to be members of the class,” creating so-called “closed” classes, which are in effect opt-in.⁷²⁷ Whatever impact this shift has had on class actions, however, observers nonetheless describe the Australian regime one of the most plaintiff-friendly in the world.⁷²⁸

SINO-FOREST (CANADA)

Sino-Forest is the largest securities fraud class action in Canada, in which investors suffered over \$7 billion in damages. Although Sino-Forest Corp. quickly sought insolvency protection, plaintiffs in the Ontario securities case were still able to achieve substantial settlements with auditors, underwriters, and other secondary actors.

Claims

Sino-Forest Corp. was a forestry company organized and headquartered in Canada, but with most of its forestry assets and operations in China. In 2011, Sino-Forest became embroiled in controversy after a short-seller released a report accusing

⁷²⁷ Class Actions in Australia, Ashurst Law Firm, 2013, available at https://www.ashurst.com/doc.aspx?id_Resource=8181 (last accessed May 6, 2016).

⁷²⁸ Indeed, so long as relatively low numerosity and commonality thresholds are met, there is no requirement that a class action proceeding be judicially certified as appropriate for class treatment. Nor is there a predominance requirement. See, e.g., Quinn Emanuel Urquhart & Sullivan, LLP, Business Litig. Reports, Article: Overview of the Class Action Regime in Australia, <http://www.quinnemanuel.com/the-firm/news-events/article-february-2014-overview-of-the-class-action-regime-in-australia/>; see also Stuart Clark, Who’s Who Legal, *Is Australia the New Class Action Frontier?* (June 2013), <http://whoswholegal.com/news/features/article/30562/is-australia-new-class-action-frontier>.



Sino-Forest of being a multi-billion dollar Ponzi scheme, grossly overstating its forestry assets by hundreds of millions of dollars. At that time, Sino-Forest traded on the Toronto Stock Exchange (“TSX”) and its market capitalization was over \$6 billion. Amid the fraud allegations, the Ontario Securities Commission and the Royal Canadian Mounted Police instituted investigations, with the Commission soon issuing a cease-trade order as to Sino-Forest’s stock.

Investors filed several class actions in Ontario, Quebec and Saskatchewan against Sino-Forest, certain of its officers and directors, its auditors, its underwriters and a consultant. In the Ontario case, after an extensive carriage motion proceeding, the plaintiffs asserted claims under the Ontario Securities Act, as well as common law claims for negligence, negligent misrepresentation and unjust enrichment.

Procedural Posture

Within months after investors filed their lawsuits, however, Sino-Forest initiated insolvency proceedings in Canada under the Companies’ Creditors Arrangement Act (“CCAA”), the equivalent of American bankruptcy proceedings. The CCAA proceedings temporarily stayed the actions as to Sino-Forest, and the court extended the stay as to Sino-Forest’s auditors, underwriters and other third-party defendants.

Nevertheless, class counsel was able to successfully negotiate several settlements, including settlements with Ernst & Young, several underwriters, a consulting company and certain officers and directors. The Ernst & Young settlement, totaling \$117 million, is the largest securities fraud settlement ever achieved with an auditor in Canada. In total, class counsel recovered over \$153 million for class members residing both in Canada and elsewhere, including the U.S.⁷²⁹

Non-Opt-Out Settlements With Non-Issuer Defendants Approved Through Insolvency Proceedings

The manner in which class plaintiffs in the Ontario case were able to achieve significant settlements in the face of an insolvent issuer offer important insights on Canadian law.

First, unlike U.S. law, where open market fraud claims against secondary actors are limited to specific instances where they personally and intentionally issued misleading statements to investors,⁷³⁰ Ontario law allows negligence-based claims against secondary actors. Thus, solvent defendants such as Ernst & Young and various underwriters faced claims under Ontario securities laws and common law claims for negligence and unjust enrichment. This is good news for investors who might otherwise have little recourse against insolvent issuers.

Second, the defendants required that most of the settlements be approved through the Canadian CCAA proceedings. The CCAA court temporarily stayed the class action litigation as to all defendants, including the auditor and underwriter defendants. Class plaintiffs appeared in the CCAA proceeding and were able to negotiate inclusion of a mechanism in Sino-Forest’s plan of reorganization for approval of so-called “named third party defendants” in the Ontario class action. Through this mechanism, which was approved by Sino-Forest’s creditors and the CCAA court, the settlements would be approved in the context of the CCAA proceeding, and class members would be afforded no opportunity to opt-out.

A small number of investors did not like the fact that by proceeding in the CCAA court, the settlements provided no opportunity for opting out.⁷³¹ These investors objected to the settlements, claiming that the CCAA court had no authority to dispense with the

⁷²⁹ As noted above, this Ontario action proceeded on behalf of all investors regardless of residence for all securities that traded on the TSX and on behalf of Canadian residents who purchased any Sino-Forest securities (with the exception that investors covered by the Quebec class action were excluded).

⁷³⁰ See *Janus Capital Group, Inc. v. First Derivative Traders*, 131 S. Ct. 2296 (2011). See also *CentralBank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994).

⁷³¹ The objectors represented investments comprising approximately 1.6% of Sino-Forest’s shares.



investors' opt-out rights that are explicitly provided by the Ontario Class Proceedings Act ("CPA").

In its decision approving the Ernst & Young settlement, the CCAA court rejected the objectors' argument that settlement of class action litigation was required to be approved under the CPA, explaining: "I do not accept that the class action settlement should be approved solely under the CPA. The reality facing the parties is that [Sino-Forest] is insolvent; it is under CCAA protection, and stakeholder claims are to be considered in the context of the CCAA regime."⁷³² The court cited precedent indicating that it was "well-established that class proceedings can be settled in a CCAA proceeding,"⁷³³ and further that "third-party releases are not an uncommon feature of complex restructurings under the CCAA."⁷³⁴

In approving the settlement under the CCAA, the court assessed: "(a) whether the settlement is fair and reasonable; (b) whether it provides substantial benefits to other stakeholders; and (c) whether it is consistent with the purpose and spirit of the CCAA."⁷³⁵ In deciding whether it was appropriate for the settlement to release third-party claims, the court applied a "nexus" test, assessing "whether there is 'a reasonable connection between the third party claim being compromised in the plan and the restructuring achieved by the plan to warrant inclusion of the third party release in the plan.'"⁷³⁶

The court ultimately found that plaintiffs' claims against Ernst & Young were intertwined with the Sino-Forest CCAA proceedings. The court appeared especially concerned with Ernst & Young's own claims against Sino-Forest and its subsidiaries for indemnity with respect to the class plaintiffs' claims, and the court deemed it helpful to the CCAA restructuring to have those claims released as well.

⁷³² *Labourers' Pension Fund of Central and Eastern Canada v. Sino-Forest Corp.*, 2013 ONSC 1078, ¶ 72 (O.S.C.J. Mar. 20, 2013).

⁷³³ *Id.*, ¶37.

⁷³⁴ *Id.*, ¶46.

⁷³⁵ *Id.*, ¶49.

⁷³⁶ *Id.*, ¶50 (quoting *ATB Financial v. Metcalf and Mansfeld Alternative Investments II Corp.*, 2008 ONCA 587, ¶ 70).

The objectors appealed the lower court's order approving the Ernst & Young settlement, but to no avail. The Ontario Court of Appeal denied leave for appeal, finding no basis to disturb the ruling.

Notably, the settlements also covered U.S. investors. Although there was a parallel U.S. class action that covered members of the Canadian settlement class, the U.S. plaintiffs approved the Ernst & Young settlement and agreed to the process of seeking approval through the CCAA proceeding and thereafter seeking enforcement of the settlement approval orders through the U.S. bankruptcy court. The plaintiffs in the U.S. action specifically sought and obtained orders from the U.S. bankruptcy court for enforcement of the settlements. The U.S. bankruptcy court found that the settlements were enforceable and that the release would apply to U.S. investors despite the absence of opt-out rights.

Olympus (Japan)

Olympus Corporation is a manufacturer of optics and reprography products that is headquartered in Japan. In 2011, the former CEO of Olympus Corporation, Michael Woodford, blew the whistle on one of the largest accounting frauds in Japan. From the late 1990s to 2011, Olympus had covered up losses by writing off acquisitions and paying exorbitant advisory fees.⁷³⁷

Three former Olympus executives pled guilty to accounting fraud in a Japanese court in 2012 after Olympus admitted to concealing more than \$1.7 billion in losses and fees through a series of sham transactions, including a \$687 million payment it made for financial advice on its \$2 billion takeover of Gyrus Group PLC in 2008. The executives received suspended sentences and Olympus paid a fine of \$7 million (\$700 million yen). The company did not appeal the fine. Olympus was also required to restate five years of financial

⁷³⁷ Floyd Norris, THE NEW YORK TIMES, Deep Roots of Fraud at Olympus, (Dec. 8, 2011), http://www.nytimes.com/2011/12/09/business/deep-roots-of-fraud-at-olympus.html?_r=0, quoting The Third Party Committee, Olympus Corp., Investigation Report Summary (Dec. 6, 2011), at <http://www.olympus-global.com/en/info/2011b/if111206corpe.pdf>.



statements in order to remain listed on the Tokyo Stock Exchange. In addition, the whistleblower (Michael Woodford) filed and settled claims (reportedly for 10 million pounds) that Olympus had fired him in retaliation for questioning its accounting.

Section 10(b) and 20(a) claims were asserted in the United States in the Eastern District of Pennsylvania as to Olympus ADRs only. That action, filed in Allentown, Pennsylvania, settled for \$2.6 Million in May 2014.

For claims based upon purchases of Olympus' common stock, several actions were brought in Japan by groups that included both Japanese and foreign (U.S., European and Asian) investors, including some of the world's largest pension and sovereign wealth funds and mutual fund complexes. Misstatements were alleged pursuant to Japan's FIEA. Amendments to FIEA in 2004 reduced the burden of proof for plaintiffs and introduced a presumptive rule for damages—the difference in the one-month average of a stock price before and after the disclosure in question. FIEA stipulates no-fault liability on the part of corporations for their misstatements. There is no class action mechanism in Japan.

In March 2015, the action in Japan brought by one of the groups of investors (sponsored by three U.S. law firms and composed for more than 100 investors) was settled for ¥11 billion (approximately \$92 million) as the result of a mediation proceeding conducted by an Australian mediator and a Japanese mediator. The second action, sponsored by a European-based law firm, has not yet settled (or at least there has been no public report of such a settlement).

The Olympus action was the first major litigation in Japan to be initiated by foreign institutional investors. In prior years, plaintiffs had been mostly domestic.

Fortis (The Netherlands)

Fortis⁷³⁸ was the largest financial services provider in the Netherlands and Belgium and in 2007, it was the 20th largest company in the world by revenue.⁷³⁹ Fortis' attempt to acquire ABN Amro⁷⁴⁰ and the bank's exposure to collateralized debt obligations and subprime mortgage-backed securities led to the bank's collapse in the fall of 2008. As a result of the bank's collapse, investors lost as much as ninety percent (90%) of the value of their investments. Investors commenced various legal actions in the Netherlands and in Belgium⁷⁴¹ alleging that the company and its executives misrepresented the company's financial condition. Shareholders first initiated proceedings before the Dutch Enterprise Chamber⁷⁴²

⁷³⁸ Fortis operated under a dual set-up headed by two companies: Fortis S.A./N.V., a company incorporated in Belgium and with registered offices in Brussels, and Fortis N.V., a company incorporated under the laws of the Netherlands with registered offices in Utrecht. Both companies shared the same executive directors and shares of Fortis N.V. and Fortis S.A./N.V. traded in tandem.

⁷³⁹ Fortune Global 500 (2007), at <http://fortune.com/global500/2007/>.

⁷⁴⁰ Clara Ferreira-Marques, *Reuters*, RBS-led group says gets 86 pct of ABN shares (Oct. 8, 2007), <http://www.reuters.com/article/idUSWLB303420071008>.

⁷⁴¹ The four largest actions included an action filed in the Netherlands by a Dutch Foundation the *Stichting Investor Claims Against Fortis* on behalf of 150 institutional investors from around the world, an action filed in the Netherlands on behalf of Dutch retail investors by the Dutch shareholder association the *VEB*, an action filed in the Netherlands on behalf of Belgian and Dutch retail investors by the Dutch foundation *Stichting FortisEffect*, and an action filed on behalf of Belgian retail and some Benelux and international institutional investors in Belgium. See Ageas, *Agreement on settlement Fortis events in 2007 & 2008, Announcement* at 8 (Mar. 14, 2016), <https://www.ageas.com/en/presentation/settlement-fortis-events-2007-2008>, p. 8.

⁷⁴² The Dutch Enterprise Chamber is an independent division within the Amsterdam Court of Appeals and it is responsible for investigating companies and determining whether any wrongdoing has occurred and whether companies have implemented and adhered to proper internal policies. The Enterprise Chamber cannot determine liability or damages. Labor unions, the public prosecutor, and shareholders have the right to submit a request for an investigation of a particular company by the Enterprise Chamber.



and on April 5, 2012 the Enterprise Chamber found that Fortis was mismanaged during the period of 2007 and 2008.⁷⁴³ Fortis appealed the judgment but on December 6, 2013, the Dutch Supreme Court rejected Fortis' arguments and upheld the Enterprise Chamber's findings.⁷⁴⁴

Investors also commenced various legal actions in the Netherlands and Belgium to establish liability and damages. In March 2016, Ageas⁷⁴⁵ and the four largest group shareholder actions announced that they reached a settlement for €1.204 billion.⁷⁴⁶ The settlement is a global settlement and will utilize the Dutch WCAM procedure to be declared binding on all eligible shareholders who do not opt-out.⁷⁴⁷ The Fortis securities settlement is not only notable for its size, but also because global investors are utilizing WCAM procedures to create a binding settlement in the absence of any U.S. settlement.

At the time this paper was written, the settlement was pending approval by the Amsterdam Court of Appeal. If approved, all eligible shareholders who do not opt-out will have an opportunity to file a claim and obtain a portion of the settlement proceeds.⁷⁴⁸ Those shareholders who actively litigated the action will receive a larger amount of compensation than those shareholders who did not participate in any proceedings, but who choose to now file a claim.⁷⁴⁹

B. ONGOING CASES

Vivendi S.A. (France)

Vivendi S.A. is a mass media company headquartered in Paris, France. In December 2013, an action was commenced in France against Vivendi on behalf of investors who purchased Vivendi securities between October 12, 2000 and August 14, 2002 on the Paris Bourse (the "French Action").⁷⁵⁰ The plaintiffs in the French Action allege that Vivendi engaged in improper accounting practices and misled the market regarding Vivendi's financial health. It is alleged that, from 2000 to 2001, Vivendi spent approximately €600 billion on several acquisitions to expand its size. Vivendi issued press releases in early 2002 that portrayed its cash flows as "excellent" and reported operating earnings as better than projections. However, in July 2002, Vivendi acknowledged a loss of €13.6 billion for calendar year 2001 and accumulated debts of €37 billion. For fiscal year 2001-2002, Vivendi reported losses of €23.3 billion, the largest reported loss in French corporate history.

At the time this paper was published, the French Action was in the "expertise phase," during which the parties meet with experts designated by the Court to ascertain the amount of damages suffered by investors. The parties' experts are in the process of reviewing relevant documents, requesting any necessary additional material, and preparing to submit their conclusions to the Court. This phase of the proceedings will continue for much of 2016, after which time the Court will turn to issues of liability.

⁷⁴³ Ben Deighton, Reuters, *Fortis guilty of mismanagement before breakup-court* (Apr. 5, 2012) <http://www.reuters.com/article/ageas-court-idUSL6E8F59V320120405>.

⁷⁴⁴ <http://finance.yahoo.com/news/dutch-supreme-court-fortis-mismanaged-153649984--finance.html>.

⁷⁴⁵ Ageas is the successor entity to Fortis.

⁷⁴⁶ <http://hugin.info/134212/R/1993901/734150.pdf>.

⁷⁴⁷ Ageas, *Agreement on settlement Fortis events in 2007 & 2008, Announcement* at p. 3, 7 (Mar. 14, 2016), <https://www.ageas.com/en/presentation/settlement-fortis-events-2007-2008>.

⁷⁴⁸ Ageas, *Agreement on settlement Fortis events in 2007 & 2008, Announcement* at p. 7 (Mar. 14, 2016), <https://www.ageas.com/en/presentation/settlement-fortis-events-2007-2008>.

⁷⁴⁹ Ageas Press Release, *Ageas, Deminor, Stichting Fortis Effect, SICAF and VEB reach agreement aiming at settling all Fortis civil Legacies*, at p. 5 (Mar. 14, 2016), http://www.fortissettlement.com/EN_Fortissettlement_14032016_014.pdf

⁷⁵⁰ Claims against Vivendi were initially filed in 2002 when a securities class action was commenced in the U.S. District Court for the Southern District of New York alleging violations of U.S. securities laws, *In re Vivendi Universal, S.A. Securities Litigation*, No. 02-cv-5571 (S.D.N.Y.). After a three-month trial that concluded in 2010, a jury found that Vivendi had violated U.S. securities laws by recklessly disseminating materially misleading information. However, soon after the jury verdict, the U.S. Supreme Court limited the scope of the U.S. securities laws to claims by investors who purchased shares on U.S. exchanges in *Morrison v. National Australia Bank*, 561 U.S. 247 (2010). Thereafter, Vivendi filed a motion to dismiss all claims related to Vivendi securities traded on a foreign exchange, which was granted.



The merits of the French Action are strong in light of: (i) a finding of Vivendi's misconduct by the French Autorité des marchés financiers (Financial Markets Authority); (ii) the verdict by a U.S. jury that Vivendi was liable for numerous instances of issuing false or misleading statements; and (iii) the conviction of Jean-Marie Messier, Vivendi's Chief Executive Officer during all relevant periods, for criminal misrepresentations. However, despite the strength of the French Action, the fact that this case must be prosecuted post-*Morrison* within the French legal system (not in the United States) presents obstacles for aggrieved investors seeking relief from Vivendi.

For example, the method of calculating damages for defrauded shareholders is not well defined under French law. French courts have significant discretion in determining damages. While such discretion could lead to substantial recoveries for shareholders, it could also result in disappointing results. The French Action will provide a noteworthy test case for the level of damages investors may expect to recover in securities fraud claims asserted in France going forward.

BP p.l.c. (Southern District of Texas, United States)

BP p.l.c. ("BP") is a British multinational company headquartered in London, England and it is one of the world's largest oil and gas companies. In April 2010, an oil rig owned by BP suffered an explosion in one of its wells. The rig was located off the coast of Louisiana and the incident, which came to be known as the "Deepwater Horizon Oil Spill of 2010," killed 11 people and caused massive environmental damage. BP initially underestimated the amount of oil being discharged by the resulting leak, and failed to disclose similar past safety issues relevant to the Deepwater Horizon incident. BP eventually pled guilty to felony counts and paid a fine of \$4.5 billion to the U.S. government. BP also settled claims for violating the Clean Water Act, and settled over 100,000 claims with private plaintiffs for spill-related damages.

Shareholders brought a securities class action against BP in the Southern District of Texas⁷⁵¹ alleging

that numerous statements made by BP about its safety and maintenance procedures regarding its deepwater drilling operations were false and misleading. The shareholders also alleged that BP materially misrepresented the spill amount following the Deepwater Horizon explosion.

In light of *Morrison*, the Court found that putative class members who purchased BP common shares on the London Stock Exchange had no standing under U.S. securities laws.⁷⁵² The Court reasoned that the transaction of foreign-listed shares in a foreign company could not qualify, irrespective of the locus of the transactions or domicile of the plaintiffs.⁷⁵³

However, a related action filed by individual investors reached a different result.⁷⁵⁴ The action was originally filed in the Western District of Louisiana, but was transferred to the Southern District of Texas MDL proceeding. Plaintiffs in this action were referred to as the "Ludlow Plaintiffs" and represented a subclass within the putative class. In a subsequent opinion addressing the Ludlow Plaintiffs, the Court found that the Ludlow Plaintiffs – including ordinary

The Southern District of Texas' acceptance of the Ludlow Plaintiffs' arguments – specifically as to their ability to bring common law fraud claims against BP – was a promising inroad, especially against the categorical exclusions of claims under Morrison by other jurisdictions.

Specifically, plaintiffs brought claims under the Exchange Act, § 10(b), 15 U.S.C.A. § 78j(b). The putative class consisting of American Depository Share purchasers and Ordinary Share Purchasers advanced New York common law and English common law claims, in addition to their section 10(b) claims. BP announced on June 2, 2016, that a settlement was reached on behalf of a class of ADS purchasers for the "post-spill class" in the amount of \$175 million.

⁷⁵² *Id.* at 794.

⁷⁵³ *Id.* at 795-96.

⁷⁵⁴ *In re BP p.l.c. Securities Litigation*, 843 F.Supp.2d 712 (S.D. Tex. Feb. 13, 2012).

⁷⁵¹ *In re BP p.l.c. Securities Litigation*, MDL No. 10-md-2185, 4:10-2185, 843 F.Supp.2d 712 (S.D.Tex. Feb. 13, 2012).



share purchasers – could pursue common law claims against BP. First, the Court found that, under Texas choice of law principles and the Restatement (Second) of Conflicts of Laws, English law applied.⁷⁵⁵

The Court then determined that, under English law, claims under the Financial Services and Markets Act of 2000 would be available to plaintiffs, and that the allegations were sufficient under the requisite elements.⁷⁵⁶ Despite this, defendants argued that the Court should dismiss the claims on *forum non conveniens* grounds. The Court rejected this argument, confirming that all of the Ludlow Plaintiffs' claims would be litigated in U.S. courts. While the circumstances in *BP p.l.c.* are unique, the case demonstrates that *Morrison* does leave open some possibility for recovering losses on foreign shares against a foreign company in U.S. courts.

The Southern District of Texas' acceptance of the Ludlow Plaintiffs' arguments – specifically as to their ability to bring common law fraud claims against BP – was a promising inroad, especially against the categorical exclusions of claims under *Morrison* by other jurisdictions. This development was notable because it opened up a potentially innovative strategy for plaintiffs in the Fifth Circuit – invoking choice of law principles to assert fraud claims that may otherwise be precluded by *Morrison*. This approach is, of course, dependent on the substantive law of the foreign jurisdiction in question. Another takeaway from the decision is defendants' failure to advance dismissal arguments on *forum non conveniens* grounds. Defendants argued that it would be more appropriate to litigate English law in an English forum. By rejecting this argument, the Court established a helpful guidepost for future plaintiffs. One of the critical issues in a *forum non conveniens* analysis is efficiency, and the Court

importantly held that efficiency would best be served by not sending any portion of the case overseas. There are still several considerations for a BP-like scenario, one of which is that other districts may not be as willing to take the approach to common law fraud on a class-wide basis, given the more complicated class structure in BP (the Ludlow Plaintiffs were treated as a subclass thus the Court was not faced with allowing common law claims on behalf of the entire class).

Royal Bank of Scotland (the United Kingdom)

Between 2001 and 2007, The Royal Bank of Scotland plc (“RBS”), a banking and insurance holding company based in Edinburgh, Scotland, began a series of acquisitions that transitioned RBS from a small national bank to one of the largest financial conglomerates in the world.

In 2007, as concerns about subprime exposure became manifest throughout the financial markets, RBS assured investors that its subprime exposure was limited. But RBS had accumulated billions of dollars in subprime exposure. One of RBS's investment banks had been selling mortgage debt as asset-backed securities (“ABS”) and packaging them together into collateralized debt obligations (“CDO”). The underlying assets in the ABS and CDO transactions were mortgage-backed securities (“MBS”), including securities backed by subprime and other high-risk residential mortgages.

When liquidity in the subprime market weakened, RBS was forced to retain interest in several CDOs and assume the risks associated with them. As a result, RBS's subprime exposure reached at least £34 billion (\$68 billion) by 2007.

In April 2007, RBS announced that it was submitting a proposal for the acquisition of ABN AMRO Bank N.V., one of the largest financial institutions in the Netherlands. A three member consortium that included RBS purchased ABN AMRO in October 2007 for approximately \$38 billion. Shortly thereafter, in December 2007, it was announced that RBS and ABN AMRO would be taking write-downs of £950 million and £300 million, respectively, attributable to their exposure

⁷⁵⁵ *In re BP p.l.c. Securities Litigation*, 4:12-cv-1837, 2013 WL 6383968 (S.D. Tex. Sep. 30, 2013) (amended Dec. 5, 2013).

⁷⁵⁶ The Court mapped the claims to English law categorically. 2013 WL 6383968, at *37. The elements of a FSMA claim are: (1) purchase of Defendant's securities; (2) in actual and justifiable reliance on (i) any untrue or misleading statement in a publication to which the law applies or (ii) omission of any matter required to be included in such a publication; (3) scienter regarding the misstatement or omission by a person with responsibility for it; and (4) loss as a result.



to U.S. subprime mortgage markets. Nevertheless, RBS continued to claim that the risks were minimal. In April 2008, RBS announced an additional asset write-down of £5.9 billion (nearly \$12 billion) attributable mainly to RBS's exposure to subprime assets. On that same date, RBS also announced a £12 billion (nearly \$24 billion) rights issue to increase RBS's capital base. Despite these announcements, RBS continued to assert that its business would be healthy going forward. However, six months later, RBS disclosed that it would receive a bailout from the British government. In January 2009, RBS admitted that its subprime exposure had resulted in a loss of £28 billion (\$41.3 billion) for 2008.

In 2009, investors filed a securities class action in the United States against The Royal Bank of Scotland Group plc, its executives and board members, and numerous underwriters alleging that investors had been defrauded as a result of Defendants' failure to disclose RBS's substantial holdings in subprime and other mortgage-related assets.⁷⁵⁷ Notably, the court-appointed lead plaintiffs had purchased common shares of RBS, which traded on the London Stock Exchange and Euronext Amsterdam stock exchange, not the ADRs trading on the NYSE.

Citing *Morrison*, the Court concluded that this group of investors could not invoke U.S. securities laws to seek recovery because their purchases were not "domestic" securities transactions.⁷⁵⁸ The Court emphasized that a foreign company is not automatically subject to U.S. securities laws simply because it lists some of its securities in U.S.-based stock exchanges.

⁷⁵⁷ Specifically, Plaintiffs alleged claims for violations of claims for violations of 10 Section (b) and 20(a) of the Exchange Act, 15 U.S.C. §§ 78j(b) and 78t(a), Rule 10b-5 promulgated thereunder; and Sections 11, 12(a)(2), and 15 of the Securities Act, 15 U.S.C. § 771(a)(2), 15 U.S.C. §§ 77k, 771(a) (2), and 77o, concerning RBS's statements that it held strong capital reserves, a balanced risk portfolio, and extensive internal controls relating to its exposure to credit risk.

⁷⁵⁸ *In re Royal Bank of Scotland Group PLC Securities Litigation*, 765 F.Supp.2d 327, 336 (S.D.N.Y. Jan. 11, 2011). The Court sustained claims on behalf of investors who bought some of an estimated \$5 billion of preferred securities that RBS sold in the United States. *Id.*

As the plaintiffs had purchased common shares of RBS trading in European stock exchanges, the Court determined that U.S. securities laws were inapplicable.

Investors precluded from recovery in the U.S. were left with the option of joining one of several actions against RBS that were brought before the High Court of Justice (Chancery Division) in London. The claims being pursued in the High Court of Justice are being brought only on behalf of investors who purchased shares in the April 2008 Rights Offering, and are based upon Section 90 of The Financial Services and Markets Act 2000. Section 90 creates a private right of action for monetary claims by shareholders who incurred losses in a rights offering, pursuant to a prospectus. As Section 90 does not extend to open market purchases and the analogous provision of U.K. law dealing with open market purchases has many complexities that have never been addressed by the U.K. courts, none of the groups pursuing claims against RBS have sought to include open market purchases of RBS securities. Thus, investors in RBS who did not purchase in the April 2008 Rights Offering had no effective redress for the losses they suffered.

The RBS litigation is being pursued by three main groups (two represent only institutional investors while a third represents some institutions and tens of thousands of individuals) and all three groups assert that their investor members were misled into signing up to the £12 billion rights issue months before RBS failed in October 2008. The three groups collectively are seeking approximately £4 billion in damages.

The central claim of the investor groups is that RBS's 2008 rights issue prospectus contained untrue or misleading statements about certain issues, including the bank's capital and true purpose of the offering. RBS has claimed that it was diligent and truthful in its preparation of the offering, and point to market volatility as the real culprit behind RBS's near-collapse.

The U.K. litigation is still ongoing. While RBS may at some point seek to settle all claims, or at least certain claims of the largest institutional class members, at this point it appears that the U.K. litigation is likely headed for a civil trial.



The RBS lawsuit is the largest, and potentially the most expensive, in the history of the U.K., with RBS's legal fees estimated to exceed £90 million before the end of a merits trial (currently scheduled to begin in March 2017). A High Court judge recently criticized RBS and its legal advisors for being "unfocused" and inundated by over 25 million documents. The judge urged RBS to take tighter control of its production of documents after noting that the disclosure process had been unfocused. Although securities litigation is still finding its place in the U.K., the trend seems to be moving towards a more open understanding and acceptance of group actions. Scholars and pundits will be paying close attention to the RBS proceedings, as many predict that the outcome will have substantial implications on the future of group actions in the U.K.

The BC Capital Group S.A. (Panama and the United States)

Beginning in January 2003, Nikolai S. Battoo and his agents began soliciting pool participants to invest in a series of portfolios set to engage in the trading of commodities, futures contracts, and equities. Battoo operated BC Capital Group S.A. ("BC Panama"), BC Capital Group Limited ("BC Hong Kong"), and BC Capital Group Holdings S.A. ("BC Switzerland") (collectively, "BC Common Enterprise"), and it was through the BC Common Enterprise that he solicited pool participants to invest in his Private International Wealth Management and Private International Wealth Management-Insurance portfolios (collectively, "PIWM Portfolios"). As a result of these solicitations, a minimum of 250 U.S. pool participants invested at least \$140 million in Battoo's investment portfolios.

Between April and October 2008, the PIWM Portfolios suffered significant losses—potentially as high as \$140 million—which Battoo and his agents failed to disclose to pool participants. Moreover, in December 2008, Battoo and the BC Common Enterprise lost tens of millions of dollars investing in Bernie Madoff "feeder funds." Rather than disclosing these losses to investors, Battoo assured the pool participants that their exposure to the Madoff Ponzi scheme was nominal, leading many pool participants to invest additional funds. In an attempt to reassure his clients

that their investments were performing adequately, Battoo provided his clients with asset verifications in September 2009 that grossly overstated the net asset value of their investments.

In October 2011, Battoo, in an attempt to disguise his prior investment losses, misrepresented to the pool participants that several investment portfolios had suffered significant losses as a result of MF Global Inc.'s ("MF Global") collapse. On November 11, 2011, Battoo and the BC Common Enterprise suspended valuations and redemptions, and informed pool participants that a significant amount of investments held in the PIWM Portfolios were in "underlying managed accounts at MF Global, along with CTA and hedge fund investments that cleared through MF Global." Battoo claimed that all investment portfolios were affected by MF Global's collapse, and informed pool participants that each portfolio's exposure ranged from 17% to 39%. In truth, the PIWM Portfolios had relatively small exposure to MF Global.

On September 6, 2012, the SEC and U.S. Commodity Futures Trading Commission ("CFTC") (collectively, the "Government") filed parallel actions in the U.S. District Court for the Northern District of Illinois against Battoo and several entities under his control seeking permanent injunctions, civil penalties, and restitution.⁷⁵⁹ The Government accused Battoo of running a Ponzi scheme that defrauded over 250 U.S. pool participants which had invested at least \$140 million in the PIWM Portfolios.

The district court in the CFTC action entered a default judgment order against Battoo and the BC Common Enterprise, all of which failed to answer the complaint, after determining that defendants had violated numerous anti-fraud provisions of the Commodity Exchange Act. Specifically, the district court concluded that defendants knowingly or recklessly made material misrepresentations and omissions to pool participants regarding the PIWM Portfolios' losses, the value and location of assets allegedly held in the PIWM Portfolios,

⁷⁵⁹ See *U.S. Commodity Futures Trading Commission v. Battoo*, Case No. 12-cv-7127, 2016 WL 3059856 (N.D. Ill. Jan. 11, 2016); *U.S. Securities and Exchange Commission v. Battoo*, Case No. 12-cv-7125 (N.D. Ill. Sept. 30, 2014).



and the PIWM Portfolios' exposure to the MF Global bankruptcy. On January 11, 2016, the District Court ordered defendants to pay approximately \$294 million in restitution, \$49 million in disgorgement, and \$147 million in civil penalties.

Similarly, a default judgment was also entered against Battoo, BC Capital Group S.A. (Panama) and BC Capital Group Limited (Hong Kong) in the SEC's enforcement action. Pursuant to the district court's Order dated September 30, 2014, defendants were ordered to pay disgorgement and prejudgment interest of approximately \$290 million and a civil penalty in the amount of \$68 million.

The parallel proceedings against Battoo and the BC Common Enterprise in the Northern District of Illinois provided defrauded investors with an opportunity to recover their losses. Although Battoo and the BC Common Enterprise were based outside of the United States, the court determined that defendants had violated U.S. federal law because the transactions at issue were domestic in nature. This holding paves the way for defrauded investors to recover their losses in instances where the transactions at issue were domestic in nature even if the defendants were based outside of the United States.

Tesco (the United Kingdom and the Netherlands)

Tesco PLC ("Tesco") is a U.K.-based and LSE-listed retailer with stores in 12 countries worldwide and average annual sales of £68.5 billion and average annual group profits of £3.6 billion over the past 5 years. The Tesco case centers on an accounting scandal involving more than £263 million in overstated profits, the resignation of both Tesco's CFO and CEO, the loss of £10 billion in market capitalization, and several investigations by the U.K. government, including a criminal investigation by the U.K. Serious Fraud Office.

A number of potential actions, including litigation in the U.K. and the establishment of a Dutch foundation, have been announced against Tesco. As of this writing, no lawsuit had been filed nor a global settlement reached.⁷⁶⁰

⁷⁶⁰ A US securities class action was settled for \$12 million for

A case against Tesco in the U.K. will likely involve allegations that Tesco and its officers violated Section 90A of the Financial Services and Markets Act 2000 (FSMA 2010 version). There is a six-year statute of limitations to bring claims under Section 90A and the statute of limitations for claims arising from Tesco's accounting scandal will therefore not expire until late 2020. Furthermore, as of April 2016 the U.K. Serious Fraud Office's investigation is ongoing.⁷⁶¹ Given the lengthy statute of limitations and the ongoing government investigation, it will likely be a while before a case is filed or there are major developments to report.

Toshiba (Japan)

Toshiba is a multinational conglomerate corporation headquartered in Tokyo, Japan. Its shares are listed on the Tokyo and New York Stock Exchanges. The case against Toshiba stems from the 2015 disclosures that Toshiba had uncovered a scandal involving seven years of fraudulent accounting that led to a staggering \$1.2 billion in overstated profits. Toshiba's stock price declined approximately 40% over several months following the revelation.⁷⁶²

In December 2015, 50 Japanese investors brought suit in a Tokyo court against three of Toshiba's former presidents and two former CFOs, seeking approximately \$2.4 million in damages.⁷⁶³ The investors argued they would not have purchased Toshiba stock had they known of the fraud. The investors' individual claims ranged from approximately \$1,500

purchasers of ADRs. See Julia Kollewe, *The Guardian*, *Tesco agrees \$12 m payout to US shareholders over accounting scandal* (Nov. 26, 2015), <http://www.theguardian.com/business/2015/nov/26/tesco-makes-12m-payout-to-us-shareholders-over-accounting-scandal>.

⁷⁶¹ James Davey, *Reuters*, *Despite sales growth, UK's Tesco cautions recovery to be bumpy* (Apr. 13, 2016), <http://uk.reuters.com/article/us-tesco-results-idUKKCN0XA1T6>.

⁷⁶² Makiko Yamazaki, *Reuters*, *Toshiba shareholders sue in Tokyo for \$2.45 million after stock plunge* (Dec. 6, 2015), <http://www.reuters.com/article/us-toshiba-accounting-idUSKBN0TQ0D020151207>

⁷⁶³ Equities.com, *Japan Economic Newswire*, *Toshiba shareholders sue ex-management over falsified accounting* (Dec. 6, 2015), <https://www.equities.com/news/toshiba-shareholders-sue-ex-management-over-falsified-accounting>; <http://www.reuters.com/article/us-toshiba-accounting-idUSKBN0TQ0D020151207>.



to \$100,000.⁷⁶⁴ It was the first lawsuit filed in Japan over the scandal on behalf of a group of investors.⁷⁶⁵ In January 2016, a second lawsuit was brought in an Osaka court by 45 additional investors seeking approximately \$1.6 million in damages from the defendants in the Tokyo lawsuit as well as Toshiba itself.⁷⁶⁶ According to reports, additional lawsuits are expected to be filed in Japan throughout 2016, with the total number of plaintiffs expected to be around 1,000.^{767,768} At the time of writing, at least one group of international institutional investors were preparing to commence litigation in Japan. Additionally, an unnamed investor was reported to have threatened to sue 28 current and former executives, including current CEO Masashi Muromachi, who was a director during much of the fraud, unless Toshiba brought suit itself.⁷⁶⁹ Toshiba did bring suit, but only against five former executives (seeking approximately \$2.4 million in damages).⁷⁷⁰

In addition to shareholder litigation, the scandal has prompted calls for more corporate governance reform within Japan.⁷⁷¹ Along those lines, in December

⁷⁶⁴ Makiko Yamazaki, Reuters, *Toshiba shareholders sue in Tokyo for \$2.45 million after stock plunge* (Dec. 6, 2015), <https://www.equities.com/news/toshiba-shareholders-sue-ex-management-over-falsified-accounting>.

⁷⁶⁵ Equities.com, Japan Economic Newswire, *Toshiba shareholders sue ex-management over falsified accounting* (Dec. 6, 2015), <https://www.equities.com/news/toshiba-shareholders-sue-ex-management-over-falsified-accounting>.

⁷⁶⁶ Jiji, The Japan Times, *Toshiba shareholders in western Japan sue former executives* (Dec. 14, 2015), <http://www.japantimes.co.jp/news/2015/12/14/national/crime-legal/toshiba-shareholders-western-japan-sue-former-executives/>.

⁷⁶⁷ Makiko Yamazaki, Reuters, *Toshiba shareholders sue in Tokyo for \$2.45 million after stock plunge* (Dec. 6, 2015), <http://www.reuters.com/article/us-toshiba-accounting-idUSKBN0TQ0D020151207>.

⁷⁶⁸ A U.S. securities class action over Toshiba ADRs, which are unsponsored, *i.e.* issued without Toshiba's involvement or participation, is pending in the Central District of California. See *Stoyas et al. v. Toshiba Corp.*, No. 15-cv-04194-DPP-JC (C.D. Cal.). As of this writing, a motion to dismiss relying heavily on *Morrison* has been filed and is being contested.

⁷⁶⁹ Makiko Yamazaki, Reuters, *Toshiba lawsuit highlights Japan governance reform still lacking: lawyers* (Nov. 12, 2015), <http://www.reuters.com/article/us-toshiba-lawsuit-idUSKCN0T10AA20151112>.

⁷⁷⁰ *Id.*

⁷⁷¹ Anna Kitanaka, The Japan Times, *Toshiba case points to whistleblower law's shortcomings* (July 24, 2015), <http://www.japantimes.co.jp/news/2015/07/24/national/crime-legal/toshiba-case-points-to-whistleblower-laws-shortcomings/>.

2015, Japanese regulators announced they would be seeking a record fine of approximately \$60 million.⁷⁷² Regulators are also reportedly considering criminal complaints.⁷⁷³

Vestas (Denmark, the United States, and the Netherlands)

Vestas Wind Systems A/S is the world's largest wind turbine manufacturer. The company is headquartered in Denmark but has manufacturing operations in Australia, China, Denmark, Germany, India, Italy, Norway, Romania, the U.K., the U.S., Spain, and Sweden. In a pending lawsuit based in Denmark, 87 investors claim that Vestas Wind Systems A/S ("Vestas" or the "Company"), the world's largest wind turbine manufacturer, released false and misleading statements related to expected and realized 2010 earnings.

On October 27, 2009, Vestas issued a financial report claiming strong order volume would result in \$7 billion in 2010 earnings. Less than a year later, on August 18, 2010, Vestas cut their 2010 fiscal year outlook by \$1 billion, causing Vestas stock to drop 23%. On October 26, 2010, Vestas announced its failure to implement 2010 international accounting standards, causing a further 10% stock drop.

In May of 2011, a U.S. plaintiff class sued Vestas for violations of §§10(b) and 20(a) of the Exchange Act, claiming the Company's false and misleading statements caused Vestas stock to trade at artificially inflated prices. In December of 2014, the parties agreed

[case-points-whistleblower-laws-shortcomings/](#); Noriyuki Suzuki, The Japan Times, *Toshiba scandal highlights need for diversity in corporate Japan* (Aug. 14, 2015), <http://www.japantimes.co.jp/news/2015/08/14/business/corporate-business/toshiba-scandal-highlights-need-diversity-corporate-japan/>.

⁷⁷² Atsuko Fukase, The Wall Street Journal, *Toshiba Accounting Scandal Draws Record Fine From Regulators* (Dec. 7, 2015), <http://www.wsj.com/articles/toshiba-accounting-scandal-draws-record-fine-from-regulators-1449472485>.

⁷⁷³ Jiji, The Japan Times, *Toshiba employees grilled by securities watchdog officials over accounting scandal* (Jan. 11, 2016), <http://www.japantimes.co.jp/news/2016/01/11/national/crime-legal/toshiba-employees-grilled-securities-watchdog-officials-accounting-scandal/>.



to a \$5 million settlement for investors who purchased Vestas ADR and common stock in U.S. transactions.

Shortly after the U.S. action began, numerous international law firms attempted to organize a Stichting, or Foundation, in order to represent the potential class of international injured investors. The Foundation route was eventually abandoned. Instead, a more traditional action is currently being pursued in Denmark. The ongoing case is not a collective action, but rather 87 individual claims bundled into the same legal procedure.

Though unresolved, the Vestas case provides a glimpse at the limitations of using a Foundation outside of the Netherlands. Furthermore, the case shows the opportunity the Danish judicial system provides for U.S. investors otherwise barred by *Morrison*. Although collective actions in Denmark have been allowed since 2008 under the Danish Administration of Justice Act, Chapter 23a (the “Act”) Sections 254a-k, the litigants in Vestas chose to pursue 87 individual claims. This method was likely used because the Act proscribes fairly specific requirements for class certification, prohibits contingency fee arrangements, and mandates loser pay rules, making collective actions unpopular in Denmark.

Petrobras (Brazil, the United States, the Netherlands, and Spain)

Petróleo Brasileiro S.A. (“Petrobras”) is a semi-public oil and gas company headquartered in Rio de Janeiro, Brazil. Petrobras is alleged to have engaged in an enormous money laundering and bribery scheme dating back for many years. It is alleged that Petrobras inflated the value of construction contracts by incorporating bribes into the value of the contracts on its financial statements. Beginning in September 2014, the prices of Petrobras’ New York Stock Exchange-traded ADSs and debt securities significantly declined following the arrests of members of senior management and the Company’s admission that it may have to restate its historical financial statements to account for the overpricing of construction contracts. The investigation involves former Petrobras executives, some of Brazil’s largest construction companies, and a group of money

launderers that allegedly colluded to inflate the cost of Petrobras contracts, and then pocketed the difference.

Claims were brought in the United States under the federal securities laws on behalf of common and preferred ADS purchasers. U.S. Plaintiffs also asserted claims under Brazilian law. The District Court sustained the federal securities claims arising out of purchases on U.S. markets, but dismissed the claims arising out of purchases made on the BOVESPA, the Brazilian Exchange, holding that “as a matter of Brazilian law, purchasing Petrobras shares on the [BOVESPA] indicates the purchaser’s consent to be bound by the arbitration clause in the company’s bylaws.”⁷⁷⁴ The District Court subsequently granted certification of two classes of U.S. purchasers: (1) open market purchasers of ADSs and (2) purchases or acquisitions of debt securities on various U.S. public offerings.

In addition to the U.S. class action, and criminal proceedings in Brazil, efforts are underway to recover for losses arising out of purchases made on the BOVESPA. Based on the arbitration clause on Petrobras’ by-laws, damages resulting from investments in Petrobras Brazilian securities are being sought in arbitration in front of the Market Arbitration Chamber of the BOVESPA. A Dutch Foundation and a potential action in Spain have also been announced.

Volkswagen AG (Germany, the United States, and the Netherlands)

Volkswagen AG (“Volkswagen”) is a German automobile manufacturer. A September 2015 notice from U.S. environmental authorities revealed that Volkswagen had utilized an illegal “defeat device”—software that temporarily reduces emissions during government testing—in many of its diesel vehicles.⁷⁷⁵ The revelation of this conduct resulted in sharp declines in the prices of Volkswagen securities, which primarily trade on the Frankfurt exchange and in a much smaller volume in the United States through ADSs.

⁷⁷⁴ *In re Petrobras Sec. Litig.*, 116 F. Supp. 3d 368, 389 (S.D.N.Y. 2015).

⁷⁷⁵ California Environmental Protection Agency Air Resources Board, *ARB Volkswagen Investigation*, http://www.arb.ca.gov/msprog/vw_info/vw-diesel-info/vw-diesel-info.htm.



In the wake of these investment losses, retail and institutional investors are pursuing recovery from Volkswagen in the United States, as well as in the Netherlands and Germany. Investors allege that Volkswagen caused investment losses by misrepresenting its diesel vehicle business and failing to disclose the enormous financial risks resulting from the implementation of the illegal defeat devices. Investor actions charge statutory violations as well as tort and other common law claims.

A number of investor lawsuits have been filed against Volkswagen in Braunschweig, Germany. The investor lawsuits have been filed in the district court in Braunschweig, Germany, which, under Section 32b of the German Code of Civil Procedure, has exclusive jurisdiction to hear the disputes.⁷⁷⁶ Additional investor lawsuits will likely be filed in Germany in the coming months. In conjunction with the complaints, motions have been filed to open model case proceedings for these actions pursuant to the German Capital Markets Model Case Act of 2012 (“KapMuG”). It is expected that a German court will initiate a KapMuG proceeding for the Volkswagen litigation in Germany.

Once the model case proceeding is initiated, the court will stay all individual actions and select a model plaintiff to lead the model case against Volkswagen through which common issues will be heard and tried. After the higher court issues the model ruling, either the parties will negotiate a settlement or all the individual actions will be resumed in the trial courts for adjudication of the remaining individual issues of fact or law.

In addition to the shareholder litigation in the U.S. and in Germany, a couple Dutch Foundations have been established in an attempt to convince Volkswagen to settle the actions without litigation and then utilize the Dutch WCAM procedure to make the settlement binding.

⁷⁷⁶ §32b Zivilprozeßordnung (ZPO), English translation available at http://www.gesetze-im-internet.de/englisch_zpo/englisch_zpo.html.



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