The NAPPA Report

Direct Actions: A Path to Recovery for Foreign Purchases of Securities

By Serena P. Hallowell, Rachel A. Avan, and Thomas W. Watson

October 2017

Seven years on, the Supreme Court's opinion in *Morrison v. National Australia Bank*, 561 U.S. 247 (2010), continues to complicate the ways investors can recover for securities fraud. The holding of *Morrison* is by now well known: that the U.S. securities laws only provide a cause of action for securities purchased on a national exchange or in a domestic transaction. While this test may seem like a simple way to, as Justice Scalia put it, ensure the securities laws only apply to "domestic, not foreign matters," what *Morrison* doesn't grapple with is the truly global nature of corporations and securities markets. Institutional investment strategies have kept pace with this global trend, and institutional investors are increasingly finding themselves seeking to recover for fraud-related losses on foreign purchased securities. *Morrison* holds that, no matter the other connections to the U.S., the federal securities laws cannot be used for this purpose.

As *Morrison* takes one recovery tool away, investors must find others to take its place. One common approach post-*Morrison* has been to participate in foreign class actions, or where impossible, to pursue group or individual actions abroad. While an important recovery strategy, foreign litigation can have its drawbacks. For example, the relevant country may have procedures and laws that make recovery difficult or risky to pursue. Or, where an investor has exposure to *both* U.S. *and* foreign-purchased securities, a foreign litigation creates additional administrative burdens and could result in an investor needing to pursue recovery opportunities in more than one litigation—an inefficient process at best. This makes it vital for investors also to consider whether their foreign securities-related losses can be recovered in the United States.

Notwithstanding *Morrison*, it can be done. Where securities fraud involves U.S. conduct, investors may be able to seek recovery for losses on non-U.S. purchases in a direct action asserting state and/or foreign law claims in the United States. For reasons described further below, this strategy could be especially attractive for state pension plans.

Morrison should not affect this strategy. In *Morrison*, the Court applied a federal cannon of construction to determine that Congress did not express an intent for the federal securities laws to apply extraterritorially—that is, outside the United States. The opinion does not purport to restrict the reach of state claims, or the power of the courts to adjudicate disputes that have foreign elements. Rather than *Morrison* itself, a major hurdle that investors have faced when considering state law claims has been the Securities Litigation Uniform Standards Act of 1998 ("SLUSA"). SLUSA precludes "covered class actions" from asserting securities claims under state law. Because many investors rely on class actions to recover their losses due to corporate malfeasance, the interaction of *Morrison* (which forbids federal law claims for foreign purchases) and SLUSA (which forbids state law claims for *any* securities purchases) has left class actions with few, if any, U.S. recovery options for these losses.[1] But SLUSA has not only affected class actions— it can also affect opt-out litigants who litigate in the same court as the related class action. Under a broad reading of SLUSA, some courts have held that opt-out litigants are part of the same "covered class action" as the related class case, and have extinguished their state law claims.

Public pension plans do not face these restrictions. SLUSA explicitly exempts state agencies and retirement plans from its operation, leaving them free to pursue state law claims alongside the related class action.[2] By asserting state law claims, investors can free courts from *Morrison's* strict transaction test, allowing them to make more common sense determinations about whether a case should be adjudicated in a U.S. forum.

U.S. courts are actually well-versed in adjudicating disputes that involve some foreign conduct. Indeed, they do it all the time, and have devised several doctrines to determine whether to hear a case, and how such cases should proceed. These analyses include *forum non conveniens*, personal jurisdiction, and choice of law. These doctrines will vary by jurisdiction, and specific research is vital to crafting a successful claim. But the broad strokes of these doctrines, especially *forum non conveniens* and personal jurisdiction, provide a good framework for evaluating whether it is possible to bring a state or foreign law securities suit in the United States. A brief overview will demonstrate that, under these doctrines, even though a security was purchased abroad, other connections to the United States can provide access to U.S. courts.

Forum Non Conveniens

Forum non conveniens is a discretionary common law doctrine allowing courts to decline jurisdiction when they believe the court "is a seriously inconvenient forum for the trial of the action provided that a more appropriate forum is available to the plaintiff."[3] Restatement (Second) of Conflict of Laws § 84 (1971). Because it is the doctrine that courts have long used to determine whether a case should be resolved in U.S. courts, it provides a good guide when crafting a securities claim involving foreign transactions.

In general courts defer to the plaintiff's choice of forum, unless there are "weighty reasons" for declining jurisdiction.[4] *Id.* To determine whether the forum is so inconvenient as to upset the plaintiff's choice of forum, courts consider the interests of the private parties and the public. The private factors consider the practicality of hearing the case—are the parties, witnesses, and evidence in the jurisdiction? The public interest factors consider more generally whether the jurisdiction should expend resources adjudicating the case—would the subject matter be of little interest to the public or the jury? Would the trial have to be conducted under completely foreign laws? Then, even if the court finds that the factors favor adjudication elsewhere, it will still ask whether another more appropriate forum is available.

Personal Jurisdiction

Under *forum non conveniens*, a court may still determine to hear a controversy with very little conduct in the forum. Therefore, investors must still ask whether the forum has personal jurisdiction over the company. A court may gain jurisdiction either through general, "all purpose," jurisdiction, which allows the court to exercise jurisdiction for any suit, or through specific jurisdiction, which allows the exercise of jurisdiction only over suits which arise out of the defendants contact with the forum.[5] In *Daimler AG v. Baumen*, the U.S. Supreme Court adopted a more restrictive view of general personal jurisdiction, limiting it in most cases to the place a company is incorporated and its principal place of business.[6] Given the restrictions imposed by the *Daimler* case, unless the company is incorporated or primarily headquartered in the United States, investors should consider whether it is possible to assert specific jurisdiction over the company. Like *forum non conveniens*, the specific jurisdiction analysis provides a good litmus test for whether a particular case is well-suited to a U.S.-based recovery strategy.

Conflict of Law

Unlike some of the other doctrines, the conflict of law analysis informs less whether a claim can be brought in the United States, and more how that claim should be crafted. This is because conflict of law affects a potential suit in indirect ways. For example, different jurisdictions may apply different limitations periods, or impose different elements. It is very important, therefore, to consider which laws a court may apply, and tailor claims such that they can succeed under as many as possible.[7]

The current individual actions against BP related to the Deepwater Horizon disaster illustrate how a court may determine to hear foreign purchase claims under the above doctrines. In the *BP* litigation, a number of investors opted out of the securities class action to bring individual common law fraud claims against BP, some for common stock purchased on the London Stock Exchange (the "LSE"). In a series of opinions, the district court performed an exhaustive analysis under *forum non conveniens* to determine whether U.S. and foreign plaintiffs could litigate claims for purchases on the LSE.[8] In both cases, the court determined to retain jurisdiction of the claims, and, after conducting a choice-of-law analysis, determined to apply English law.[9]

As the above demonstrates, state and foreign law claims asserted in individual actions in the U.S. may provide an important tool for recovering investor losses that involve foreign transactions.

This is particularly true under fact patterns where the conduct and the parties are domestic, but the transaction was abroad. This is a fact pattern that has become increasingly possible in recent years, as U.S. corporations seek to access foreign capital markets, or explore different corporate structures to lessen their U.S. tax obligations, such as corporate inversions. In a corporate inversion, a U.S. corporation enters into a complex merger transaction to relocate its legal domicile to a foreign jurisdiction, but often maintains its headquarters and management in the U.S.[10]

Conclusion

As institutional investors find themselves seeking to recover for fraud-related losses on foreign-purchased securities, U.S.-based direct actions are an underutilized recovery tool that should be considered. While there are limitations on when these actions can be successfully brought, under the right facts, U.S.-based direct actions can provide investors with an important and viable opportunity to recover for losses stemming from foreign purchases of securities, without some of the challenges they may face abroad.

Serena Hallowell *is a Partner and head of the Direct Action Litigation Practice,* ***Rachel Avan*** *is Of Counsel, and* ***Thomas Watson*** *is an Associate in the New York office of Labaton Sucharow.*

ENDNOTES:

[1]A few courts have held that SLUSA does not preclude bringing securities claims under foreign law. *See, e.g., LaSala v. Bordier et Cie*, 519 F.3d 121, 143 (3d Cir. 2008) (holding that SLUSA does not preclude claims under Swiss law); *In re BP p.l.c. Sec. Litig.*, 109 F. Supp. 3d 946, 960 (S.D. Tex. 2014) (finding same with regard to English law claims). This means that class actions can potentially assert foreign law claims, and there have been recent attempts to do so. That, however, is a topic worthy of its own article.

[2]15 U.S.C. §§ 78bb(f)(3)(B); *see Merrill Lynch, Pierce, Fenner & Smith Inc. v. Dabit*, 547 U.S. 71, 87 (2006) ("The statute carefully exempts from its operation . . . actions brought by a state agency or state pension plan[.].").

[3]Restatement (Second) of Conflict of Laws § 84 (1971).

[4]*Id.*

[5]*See Daimler AG v. Baumen*, 134 S. Ct. 746 (2013).

[6]*Id.* at 761 n.19.

[7]For claims that sound in fraud, a court may look to Restatement of the Conflicts of Laws (Second) § 148, which puts the most weight on the plaintiff's place of reliance and where the misstatement was made or originated. If the plaintiff's reliance and the misstatement occurred in the same state, then that state's law is presumed to apply. If the plaintiff's reliance was in a different state, then § 148 provides a multi-factored analysis for determining which state's law to apply. Restatement of the Conflict of Laws (Second) § 148.

[8]*In re BP p.l.c. Sec. Litig.*, No. 4:12-CV-1256, 2013 WL 6383968, at *52–55 (S.D. Tex. Dec. 5, 2013) (retaining jurisdiction over U.S. plaintiffs' English law claims); *In re BP p.l.c. Sec. Litig.*, 109 F. Supp. 3d 946, 961–65 (S.D. Tex. 2014) (retaining jurisdiction over foreign plaintiffs' English law claims).

[9]*Id.*

[10]In some instances, these mergers result in the company's securities being cross listed on non-U.S. exchanges. In such instances, though the company is domestic in nearly every respect, an investor defrauded on a security purchased abroad would have no recourse under the federal securities laws.