

# International Group Securities Litigation

*Morrison V. National Australia Bank Changes Global Landscape*

## Summary

The Morrison v. National Australia Bank case has changed the global landscape for class action recoveries and the likely result is an increase in the time and attention investors will have to pay to potential litigation in non-US jurisdictions. In June, 2010, the U.S. Supreme Court ruled that securities traded outside the U.S. are no longer within U.S. jurisdiction, effectively barring investors who purchase securities on a foreign exchange from filing U.S. class actions.

As a result, investors must now seek out foreign jurisdictions as a venue for their complaints and bring suits under non-US law in foreign courts. This requires a comprehensive understanding of the different legal mechanisms for handling group actions in foreign jurisdictions, a task that is proving challenging for investors to do on their own. Each country has its own set of rules that are still evolving, and cases are not as widely publicized as they are in the U.S.

Cases outside the U.S., however, are becoming more prevalent. Therefore, to maximize international group action opportunities — or even to simply perform their fiduciary obligations — investors need information gathering and case monitoring capabilities that reduce the risk of missing potentially significant international recoveries.

They also need expertise and guidance in navigating through the complexity of the group action mechanisms employed in different regions of the world.

While the majority of the world's securities class action settlements still occur in the United States, the international scope of class actions continues to expand. Many countries other than the U.S. routinely experience group securities litigation, while other

countries are new to group litigation. Mexico, for example, began allowing class actions for the first time in March 2012, and India introduced a bill last year to allow opt-in class actions.

Outside of the U.S., the bulk of class actions occur in Canada and Australia, with Asian and European countries beginning to implement systems similar to what exists in the U.S. Each country and jurisdiction has its own set of rules that are constantly evolving. In fact, with the Morrison v. National Australia Bank decision, even the U.S. has recently changed its own policies regarding international securities class actions.

In the case Morrison v. National Australia Bank, the U.S. Supreme Court ruled in June, 2010, that securities traded outside the U.S. are no longer within U.S. jurisdiction, effectively forcing actions against securities traded on foreign exchanges to be pursued outside of the United States.

Prior to the Morrison decision, the U.S.'s jurisdiction over securities class actions was so broadly defined that complaints were frequently filed in U.S. courts on behalf of foreign companies, trading foreign securities, on foreign exchanges (so-called f-cubed cases). Only the most tenuous connection to the U.S. was required to grant U.S. jurisdiction. This opened the door for international investors to seek recoveries for their damages in U.S. courts, which historically have been more sympathetic to investors than some other countries. As a result of the Morrison ruling however, investors must now seek out foreign jurisdictions as a venue for their complaints and bring suits under non-US law in foreign courts.

Accordingly, the number of foreign group actions is on the rise. A recent report released by NERA Economic Consulting revealed that there were a record 15 new securities class actions filed in Canadian

**For more information:**

Sales: 781.306.3866  
info@frtservices.com  
www.frtservices.com

One Cabot Road  
4th Floor  
Medford, MA 02155

courts in 2011, representing \$24.2 billion in outstanding claims. Similarly in Australia, settlements in shareholder class actions topped \$500 million for the first time in 2011, according to a report from the law firm King & Wood Mallesons. European group actions have likewise become more common with high profile cases like Convergium, Vivendi and Parmalat affecting millions of investors. High profile non-U.S. group actions include a \$200 million settlement with Centro Properties in Australia, a \$1.14 billion settlement with Nortel in Canada, and a \$376 million settlement with Royal Dutch Petroleum in the Netherlands.

### ***Mechanisms Used in Foreign Courts***

Successfully navigating class actions outside the U.S. requires a comprehensive understanding of the legal mechanisms for handling group actions in foreign jurisdictions. Depending on the jurisdiction, a variety of different mechanisms for group litigation are employed to address investors' concerns. The primary mechanisms, however, can be broken down into the following categories:

**Opt-out Class Action:** This is the US-style class action in which investors — as described by the court-approved plan of allocation which accompanies each settlement — are bound by any settlement unless they explicitly opt-out, regardless of whether they file for a claim with the administrator. This approach requires investors to explicitly opt-out of the class before they are able to bring their own private suit.

**Example:** Atlas Cold Storage Income Trust in Canada

**Pros:** Opt-out class actions provide investors - even individual (non-institutional) investors - with recourse in the event of corporate fraud or other misconduct affecting share prices. This type of behavior would otherwise, due to the small size of each individual claim, go unmitigated. By aggregating the damages across all affected investors, the repercussions become a legitimate corrective force, and a deterrent to future misconduct.

**Cons:** There is general distrust of US-Style class actions, particularly in Europe, because many are uncomfortable with the idea that, in a class action, the defendant cannot face their accusers, given that the class represents an unidentified and very large body of people. Class members often feel that they should not be bound by a settlement in which they did not actively choose to participate. Many think the US is too litigious with a system that is open to abuse. They believe plaintiff lawyers use the system to force securities issuers into settlements, even when they have done nothing wrong, and cite the tendency of plaintiff lawyers to sue for large damage amounts that are often viewed as disproportionate to the real effects of the misconduct as evidence of this abuse.

### **Opt-in Class Action:**

Investors are not bound by the settlement until they have explicitly opted into a class prior to settlement. In some instances, the risk associated with such an endeavor is underwritten by a litigation funding company, which fronts any legal retainers in exchange for a contingency fee collected in the event of a settlement. Australian Group Actions are still largely based on an “opt-in” mechanism, as opposed to the “opt-out” mechanism in US class actions.

**Example:** Nufarm Securities Litigation in Australia

**Pros:** The opt-in mechanism is typically a privately-organized solution in which a litigation-funding company underwrites the risks associated with taking on legal fees. They do so on contingency in the event of a settlement. The benefit is that in smaller jurisdictions where lead plaintiffs (institutional investors) are not easy to come by, many cases come to fruition which would otherwise be discarded. Although it is not *always* necessary to opt into the class beforehand to be included in the settlement, it is usually beneficial for investors to do so. If there is not enough support for the action, it will not be profitable for the litigation funders, who will be forced to drop the case before it has even started.

**Cons:** The flip-side of having a litigation funder underwrite the legal retainer is that they take a significant contingency fee in the event of a recovery, as much as 40%.

#### **Collective Action:**

This type of case is employed in a number of jurisdictions to avoid having an unknown body of complainants. In a collective action, investors must join as members of a representative organization—typically an investor-protection association, which can represent a large body of complainants. Typically, rules govern which organizations are eligible to lodge a complaint. For example, in Germany an organization must have already existed for at least three years in order to be considered eligible.

**Example: Vivendi Group – A collective action was brought against Vivendi in 2008 when the court ordered compensation to more than 200 small shareholders for a total of 1.2 million euros.**

**Pros:** A collective action alleviates certain concerns, particularly in Europe, around being sued by an unknown body of claimants by grouping claimants into a single organizational entity with a membership roster. By limiting the size of the action, it also serves to limit the extent of the damages being sought.

**Cons:** The downside of a collective action is that, in most jurisdictions, an organization cannot be created *as a response* to corporate misconduct. Instead, the collective entity must have pre-dated the event that initiated the group action. This limits the recourse available to investors if an appropriate organization does not already exist. It also requires a high level of awareness on the part of investors, who must actively participate in the litigation by opting into the collective organization before a settlement has been reached. In doing so, they also absorb the risk that any fees associated with joining the group will be lost or insufficiently covered by the outcome of the litigation.

#### **Test Case:**

A test case is a non-representative mechanism where the verdict from a prior case can be applied to similar complaints that arise in the future. Variations on this mechanism include:

- The KapMuG multi-party process in Germany, in which a model case is chosen from individual claims and then the ruling is applied to all other analogous complaints going forward.
- The Group Litigation Order (GLO) rule in England and Wales provides broad authority to the courts to manage a particular set of claims. Often a group register is set up for claimants to apply to be a part of the litigation. A representative claim is then chosen from the registry and the verdict is applied to all registered claimants.

### Example: Hypo Real Estate KapMuG Case

Pros: Like collective actions, test cases alleviate certain concerns, particularly in Europe, around being sued by an unknown body of claimants. Unlike collective actions, however, they have the added benefit of giving the individual investor the option to put forth their own evidence and to have a real influence over the course of the litigation.

Cons: The downside of the Test Case mechanism is the significant level of participation required by the complainant. Unlike class and collective actions, participants must actively engage in the legal process in order to show that their own situation is not contrary to that of the model claimant.

#### **Joinders-of-Claim:**

A non-representative mechanism where several similar complaints are joined into one case with all plaintiffs listed individually. These tend to be small actions with limited press attention, however, they are prevalent on the global scale (including in the US) because they circumvent many of the concerns associated with larger group actions. In fact, many such suits are derived from existing class actions when class members actively opt-out of a settlement. This enables them to bring their own suit, usually because they feel that their recovery from the settlement is insufficient.

### **International Class Action Landscape**

By “international class action” we mean group litigation that has been filed in jurisdictions outside of the U.S. The distinction should be made between cases involving shares traded on

foreign exchanges that are tried in foreign jurisdictions and foreign securities that are traded on U.S. exchanges in the form of American Depositary Receipts (ADRs). Since ADRs are traded on U.S. exchanges, they are treated as domestic cases and are litigated in U.S. courts.

The majority of the countries outside of the U.S. currently lack definitive procedural law for class actions, although international courts are shifting to provide investors with legitimate recourse in the event of securities fraud. In many jurisdictions, particularly in Europe, there exists a backlash against the idea of a class action. These countries are uncomfortable with idea that defendants in a class action cannot face their accuser and are effectively being sued on behalf of an undefined group of people.

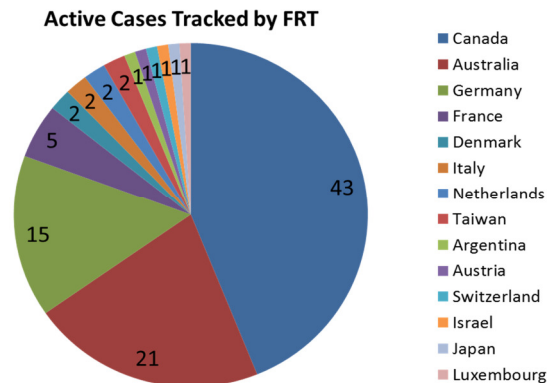
Even more importantly, there is fear that the system will be abused. Many see the U.S. as being too litigious, with plaintiff lawyers taking advantage of the system to force securities issuers into settlements, even when they have done nothing wrong.

On the other hand, it is widely recognized that investors have very few options for recourse in the event of financial misconduct by securities issuers. Class actions have proven an effective mechanism for recovering damages for harmed investors.

Until class action laws are enacted in these jurisdictions, recovery attempts generally require working with a local law firm to bring an action against a specific firm. In non-English speaking countries where securities group actions are currently active (such as Japan), this often requires partnering with a local intermediary to facilitate filings, handle translation needs, and address any procedural issues. Some jurisdictions do not allow third-party providers to file on behalf of an investor, and in those cases,

investors must work directly with the local legal firm.

**Non-US Countries with the Most Active Cases**



Note: FRT is currently tracking approximately 100 "active" international cases. In Canada, that means a case has already settled and a claims administrator is actively taking claims. In Australia, this means that a plaintiff law firm is accepting new registrants to determine if the suit should be filed.

**Canada**

Canada follows the U.S.-style opt-out approach, however, certain cases can be restricted to residents of a particular province, whereas other cases are open to all investors, both Canadian and international.

Active cases in Canada include:

*Canadian Superior Energy*  
Related to concerns that its shares were undervalued during its acquisition by Sonde Resources.

*Bear Lake Gold*  
The Action arose from the discovery in July 2009 of inconsistencies in the exploration results for its Larder Lake Property.

*Atlas Cold Storage Income Trust*  
This action is settled in the Ontario courts and is accepting claims. The Lawsuit alleges that Atlas Cold

Storage Income Trust's net income for the fiscal years ending 2001 and 2002 was overstated, thereby causing the Atlas Trust Units to trade at artificially high prices. The statement of claim also alleges that some of the Defendants breached section 130 of the Securities Act and that the defendants were negligent.

**C.P. Ships**

This action is settled in the Ontario courts and is accepting claims. The company made material misrepresentations of its financial state in 2003 and 2004 and did not follow GAAP principles in its internal accounting controls.

**Australia**

Australia employs opt-in class actions as its primary group litigation mechanism and allows classes to be organized and represented by third party litigation funding groups, which front the retainer fee and then take a contingency on settlement.

In Australia, plaintiff law firms typically release press alerts seeking investors meeting the criteria they believe best captures the damages caused by the proposed defendant. If the plaintiff lawyers choose to go forward with the case, they will often coordinate with a litigation funding company to fund the suit. In some instances, registration for the class may still be accepted even after this point.

Because these alerts are issued so early in the investigation, plaintiff lawyers may refine certain aspects of the case – such as the class period and the relevant securities – based on the submissions they receive.

Active cases in Australia include:

*Transpacific Industries*



This action is open for registration in Australia, but investors must contact IMF to participate. The cause of action relates to alleged misleading or deceptive conduct and alleged breaches by TPI of its “continuous obligations” in terms of financial reporting.

#### *Nufarm*

When several Chinese manufacturers of Glyphosate, the primary ingredient in Roundup Weed Killer, closed down during the Beijing Olympics, prices of Roundup skyrocketed. Nufarm had a large inventory of Roundup and forecast their sales based on the artificially high prices during the Olympics. Ultimately, they were forced to sell their inventory at a loss when the market readjusted after the Olympics. The lawsuit arose because the company allegedly engaged in misleading and deceptive conduct by forecasting net debt of \$450 million on July 14, 2010, when—as the plaintiff law firm has claimed—Nufarm should have been aware that the actual figure would be significantly higher. Class Period: between September 28, 2009 and August 31, 2010.

#### **Germany**

Germany has struggled with promoting a single group litigation mechanism. Its law includes provisions for class actions, however, these were essentially superseded in 2005 by the KapMuG process wherein the results from one case can be applied to other complainants that are similarly situated. Unfortunately, KapMuG cases have invariably proven ineffective given the significant procedural challenges associated with allowing thousands of interested parties to make their cases individually. In addition, settlements are nearly impossible to achieve because

KapMuG requires all interested parties to agree on its terms.

The KapMuG procedure is expected to undergo a significant overhaul in the coming months. Otherwise the procedure’s sunset clause will be invoked in October 2012, preventing it from becoming a permanent part of German Law. In either case, it will be worthwhile to keep a close eye on how the laws of group actions evolve in Germany.

Active cases in Germany include:

#### *Hypo Real Estate*

Reason for the lawsuit is that HRE misled participants in the capital markets about the risks of their investments in so-called collateralized debt obligations (CDOs). This case was accepting registrants until December 31, 2011 and employed the model of using prior Test Cases.

#### *Euroventa AG*

Many German investors did not realize that they were investing in an English Ltd. as opposed to a stock corporation incorporated under German law and that they were exposed to particularly high risk securities. It is now clear that the “Shareholder Certificates” issued to investors were worthless.

#### ***Conclusion: Best Practices in International Class Action Recovery***

International filings are on the rise, however, taking advantage of these settlement opportunities can be complex and time-consuming given the different mechanisms used in each country. As different countries figure out what recourse they want to give to investors, they are enacting legal changes to accommodate class actions or other similar mechanisms. ***So staying on top of this evolving landscape is crucial to maximizing their opportunities.***

In addition, many of these cases are not widely publicized as they are in the U.S. For example, in Europe, since group actions are private litigations between plaintiff and defendant, there is no place where information on pending legal actions is publicly available. ***This emphasizes to the need for adequate information gathering and case monitoring abilities.***

Lastly, since there are many local players involved – from plaintiffs’ attorneys to litigation funders – it is important to ***know who to talk to in each jurisdiction and to develop appropriate channels for communication and information flow.***

In closing, the Morrison case has changed the landscape for international group action recoveries. Investors need to stay informed on the latest developments in securities group actions across a wide range of global jurisdictions. They need a monitoring system that helps reduce the risk of missing potentially significant recovery opportunities outside the U.S., and they need expertise and guidance in navigating through the complexity of the group action mechanisms employed in different regions of the world. Armed with this information, investors can make informed decisions on their level of participation in these actions.

### **About Financial Recovery Technologies**

Financial Recovery Technologies is a technology-based services firm that helps institutional investors identify eligibility, file claims and collect funds made available in securities class action settlements. Offering the most comprehensive range of claim filing services available, the firm excels by providing best-in-class eligibility analysis, disbursement auditing and client reporting, and by delivering the highest level of accuracy, accountability and transparency available.

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