Most Foreign Investors Are Now Banned from Class Actions, Must Act as Lead Plaintiff or Opt Out

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A large group of foreign investors can no longer ride out U.S. class actions passively – as so-called 'absent' class members – and enjoy the recoveries that other investors and their counsel secured for them without actively taking part in the lawsuit. The federal court of appeals in Manhattan (the Second Circuit) recently affirmed a district court decision to exclude from the class *all foreign investors from countries that are unlikely to recognize the court's judgment or the court-approved settlement as the final resolution for all class members*. The rule, which has already been followed by other courts in the United States, affects investors from around the world, including the Gulf States, Germany, France, Austria, Switzerland, Luxembourg, Japan, South Korea, and Taiwan. Banned from playing merely a passive role, such investors' sole remaining recovery options are now to act as lead plaintiff or opt out. The new rule does ***not*** affect investors from Canada, the Netherlands, the United Kingdom, and most of Latin America.

The *Vivendi* Rule

The root of the issue is foreign countries' relative lack of familiarity with U.S. class actions. Accordingly, under their more traditional rules of civil procedure based on the two-party model (one plaintiff, one defendant), court judgments are binding only on those who were parties to it, and cannot accrue to the benefit or detriment of those who had no part in the litigation. If the two-party model is all that a country has, its legal doctrine could reject as against due process a judgment that purports to be binding on anyone who is part of a class because they merely failed to opt out (*i.e.*, an 'opt-out' class), rather than affirmatively *chose* to be party (an 'opt-in' class). Due process, it could argue, requires that a party had actual knowledge of the lawsuit and affirmatively consented to being bound by it. In that case, if a foreign plaintiff merely failed to opt out, it will not be a valid defense for a defendant to argue that the claim at hand was already decided in litigation abroad (*res judicata*), and such foreign opt-out collective action judgment will not be recognized or provided an *exequatur*. This would be so, even if the collective action was ostensibly to the plaintiffs' benefit and redress would have been impossible to achieve if the plaintiffs were forced, under traditional doctrines, to act in their own names.

In *In re Vivendi Universal, S.A. Sec. Litig.*, 242 F.R.D. 76 (S.D.N.Y. 2007), the court held that if a U.S. class action judgment is given no effect against a foreign plaintiff in his own country, this plaintiff could simply file a claim there and start all over again (*id*. at 106-107). This could happen if the class case was lost and the plaintiff thinks he can do better a second time around, or if the plaintiff was simply unaware of the U.S. litigation or missed the deadline to participate in a settlement. The court reasoned that class actions go both ways and should provide finality for plaintiffs and defendants alike. If they do not, they cannot be said to satisfy the prerequisites of Rule 23, which requires, *inter alia*, that a class action present a method for adjudicating the dispute that is 'superior' to other methods (such as a joinder of parties or consolidation of actions). Thus, the court held that if foreign plaintiffs cannot prove that their courts will likely recognize the *res judicata* effect of the U.S. class action judgment, certification of a class that includes those foreign claimants will be denied for lack of superiority (*id*. at 95, 107).

The Second Circuit's Affirmance of the *Vivendi* Rule

This new exclusion rule has been followed by other district courts, including in the federal district court in Manhattan in *Anwar v. Fairfield Greenwich.*, 289 F.R.D. 105 (S.D.N.Y. 2013), where it was used to wipe out the claims of Madoff fraud victims from no less than 25 countries. But it was never applied beyond the district court level or endorsed by any appellate court.

The Second Circuit Court of Appeals had only once stated, 40 years ago, that foreign investors may be excluded from a class if it is a 'near certainty' that the class action judgment would have no effect in the foreign court anyway. *See Bersch v. Drexel Firestone*, 519 F.2d 974, 996 (2d Cir. 1975). That statement was innocuous because it suggested a standard that was nearly impossible for defendants to satisfy because in most countries there was no clear case law on the issue, at most some general doctrinal views about first principles.

Moreover, *Bersch* was expressly abrogated by the Supreme Court in *Morrison v. National Australia Bank*. Although *Morrison* involved extraterritorial application of U.S. securities law, which is a different issue, at least one federal judge in Manhattan has held that *Morrison*'s elimination of extraterritoriality 'materially lessen[ed]' the *Bersch/Vivendi res judicata* concerns. *In re Petrobras Sec. Litig.*, 312 F.R.D. 354 (S.D.N.Y. 2016) (Rakoff, J.). Such concerns, *Petrobras* held, 'are not a bar to the superiority of a class action' (*id*. at 363).

On appeal from the *Vivendi* decision, the Second Circuit has now held the opposite: 'Concerns about foreign recognition of our judgments are reasonably related to superiority.' *In re Vivendi, S.A. Sec. Litig.*, 838 F.3d 223, 264 (2d Cir. 2016). While it expressly declined to decide *how likely* recognition must be to meet Rule 23's superiority requirement, the appellate court did recognize that plaintiffs have the burden to establish the requirements of Rule 23 'by a preponderance of the evidence' (*id*.). Thus, it is clear that foreign investors must make at least some showing that their respective home courts do not consider opt-out classes to violate domestic public policy and recognize U.S. class action judgments, including court-approved settlements, when they purport to be binding on absent class members who did not opt out of the U.S. case.

So Who Is In, and Who Is Out?

In the wake of the now-affirmed *Vivendi* decision, district courts have applied the *Vivendi* rule and reviewed foreign expert opinion evidence and case law to determine, with analytical rigor, which countries will more likely than not recognize U.S. class judgments, so that their citizens should be allowed to participate in U.S. class actions as absent members of the class. These courts have found either an absence of evidence (so that plaintiffs could not meet their burden) or evidence against recognition in a host of countries around the world. U.S. courts have now excluded from U.S. class actions foreign investors from Europe (Andorra, Austria, Bosnia, France,Germany, Liechtenstein, Luxembourg, Monaco, San Marino, Switzerland), Asia (China, Japan, Mongolia, North Korea, South Korea), the Middle East (Israel, Kuwait, Oman, Qatar, Saudi Arabia, United Arab Emirates), Africa (Namibia, South Africa), and Oceania (Pitcairn Islands, Tokelau). *See Anwar*, 289 F.R.D. at 121; *In re Alstom SA Sec. Litig.*, 253 F.R.D. 266 (S.D.N.Y. 2008); *Borochoff v. Glaxosmithkline*, 246 F.R.D. 201, 203 (S.D.N.Y. 2007).

By contrast, the courts have permitted participation by foreign investors from the rest of Europe (Belgium, Denmark, Finland, Greece, Italy, Malta, Netherlands, Norway, Portugal, Spain, Sweden), common law jurisdictions (Canada, United Kingdom), and Central or South America (Argentina, Bolivia, Brazil, Chile, Colombia, Curaçao, Dominican Republic, Ecuador, El Salvador, Mexico, Peru, Uruguay, Venezuela). *Anwar*, 289 F.R.D. at 120-21. With respect to investors from most other countries the question has not yet been adjudicated.

Remaining Avenues to Recovery for Foreign Investors

What do these developments mean for investors from 'excluded countries'? The answer is that they will no longer be able to passively await the outcome of a class action and, if there is a favorable judgment or a settlement, limit themselves to filing a proof of claim to obtain their share of the recovery. German, Japanese, Kuwaiti, and other excluded investors cannot be 'absent class members.'

They can, however, still take action against fraud and recover losses in one of two ways: opt out or act as lead plaintiff. U.S. courts routinely appoint foreign investors as lead plaintiffs, and they have continued to do so after *Vivendi* and *Morrison* limited the rights of absent class members and purchasers on foreign exchanges. In several instances, courts have permitted foreign investors to serve as lead plaintiffs in class actions without regard for *res judicata* concerns. *See, e.g., Foley v. Transocean Ltd.*, 272 F.R.D. 126 (S.D.N.Y. 2011); *Teran v. Subaye, Inc.*, 2011 WL 4357362 (S.D.N.Y. Sept. 12, 2011). In others, courts have noted that due process concerns that cause foreign courts to require actual acknowledge and/or affirmative consent are not an issue for lead plaintiffs, who are not 'absent' members. Lead plaintiffs necessarily give their informed consent, and will be bound by the judgment. *OFI Risk Arbitrages v. Cooper Tire & Rubber Co.*, 63 F. Supp. 3d 394, 406 (D. Del. 2014); *see Takeda v. Turbodyne Techs., Inc.*, 67 F. Supp. 2d 1129, 1139 (C.D. Cal. 1999). As *OFI* makes clear, the same French plaintiff that would be excluded under *Anwar* and *Alstom* (if it remained an absent class member) was able to serve as lead plaintiff without foreign recognition concerns.

Foreign investors from excluded countries who cannot serve as lead plaintiff, or are not selected by the court to act as such, ***must*** opt out if they wish to preserve their rights to recovery in the United States. Those who opt out of a class are not subject to Rule 23's requirements for certification of a class and therefore not affected by *Vivendi*'s superiority analysis. Because opt-out plaintiffs are not absent class members but active parties who consent to be bound by the court's judgment, foreign due process rules do not raise the same *res judicata* concerns. An opt-out action is usually coordinated or consolidated with the corresponding class action, especially for discovery purposes, and the court's determination of liability questions generally will apply to both the class action and any opt-out actions to the extent relevant. However, opt-out plaintiffs retain the ability to settle their claims independently of the class (often for a proportionally higher recovery) and without a need for court approval.

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