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Cozen O'Connor (United States)
Vivendi The Multi-Billion Dollar Impact Of Morrison On Foreign-Cubed Securities Litigation
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By Mr Angelo Savino and Abby J. Sher

On February 17, 2011, U.S. District Judge Richard J. Holwell in the Southern District of New York entered an order in *In re Vivendi Universal, S.A. Securities Litigation*, 02-5571 (S.D.N.Y. Feb. 22, 2011), that dramatically reduced the potential amount of a plaintiff's jury verdict in a securities class action under section 10(b), originally estimated at approximately $9 billion. This decision vividly demonstrates the effect of Justice Antonin Scalia's recent opinion for the U.S. Supreme Court in *Morrison v. National Australia Bank, Ltd.*, 139 S. Ct. 2869 (2010). In *Morrison*, the Court held that section 10(b) cannot be applied to securities actions involving claims of foreign investors against foreign issuers to recover losses from purchases on foreign securities exchanges, so-called foreign-cubed litigation. In applying the principles announced in*Morrison*, the *Vivendi* court struck down approximately 80 percent of the jury's verdict, which related to claims of foreign and domestic class members who purchased their securities on foreign exchanges.

Vivendi: The Background

In 2002, United States and foreign shareholders brought suit against Vivendi Universal, S.A., its former CEO, Jean- Marie Messier, and its former CFO, Guillaume Hannezo, for violations of sections 10(b) and 20 (a) of the Securities Exchange Act of 1934. The shareholders alleged that between October 30, 2000 and August 14, 2002 (the Class Period) the defendants made material misrepresentations and omissions and, in reliance on those statements or omissions, the shareholders purchased ordinary shares or American Depositary Receipts (ADRs) at artificially inflated prices. The ordinary shares were traded primarily on the Paris Bourse, but not in the U.S. The ADRs, in contrast, were traded on the New York Stock Exchange (NYSE).

In February 2003, the defendants moved to dismiss the case on the ground that the court lacked subject matter jurisdiction over the claims brought by the foreign-cubed class members. The Southern District of New York applied the Second Circuit's pre-*Morrison* conduct and effects tests, considering whether the conduct occurred in the United States or had a substantial effect on United States markets or citizens. The court found that subject matter jurisdiction existed because "activities in this country were more than merely preparatory to a fraud and culpable acts or omissions occurring here directly caused losses to investors abroad." Messier and Hannezo engaged in significant conduct in the United States related to the fraud,

including moving Vivendi's headquarters to New York and splitting time between the United States and France during the Class Period. Accordingly, the court also certified a class consisting of all persons from the United States, France, England and the Netherlands who purchased or otherwise acquired ordinary shares or ADRs of Vivendi during the class period.

After a four month jury trial, the jury returned a verdict that Vivendi violated 10(b) and acted recklessly with respect to each of the 57 allegedly misleading statements set forth on the verdict form, but that Messier and Hannezo did not violate sections 10(b) or 20(a) with respect to any of the statements.

In its post-trial motions, Vivendi renewed its request for judgment as a matter of law or alternatively moved for a new trial. Before those motions could be addressed, the Supreme Court issued its opinion in *Morrison v. National Australia Bank*, holding that section 10(b) cannot be applied extraterritorially to foreign-cubed securities lawsuits.

Morrison v. National Australia Bank

In *Morrison*, Australian citizens brought suit in the United States against the National Australian Bank (NAB) under section 10(b), alleging that a Florida-based subsidiary of NAB had falsified financial data that was disseminated by NAB as part of its public filings. The Australian citizens had purchased ordinary shares of NAB on foreign exchanges. The ordinary shares were traded on the Australian stock exchange and other foreign exchanges, but not on any exchange in the United States. NAB listed its ADRs (representing rights to receive ordinary shares) on the NYSE.

The defendants argued, and both the Southern District of New York and Second Circuit agreed, that the case by the foreign plaintiffs should be dismissed for lack of subject matter jurisdiction. Under the conduct and effect tests, the court lacked subject matter jurisdiction because the actions at NAB in Australia -- the preparation and dissemination of the financial statements - -were more central to the fraud than was the alleged falsification of financial data that occurred at the Florida-based subsidiary and the alleged fraud did not have an effect in the U.S. or on U.S. citizens. (The claim of a U.S. purchaser of ADRs had also been dismissed by the District Court for failure to state a claim, but had not been appealed.)

As a threshold matter, the Supreme Court rejected as erroneous the Second Circuit's analysis of the extraterritorial application of section 10(b) as a question of subject matter jurisdiction under the cause and effect tests. Instead, the Court held that the applicability of section 10(b) presented a merits question -- whether plaintiffs had stated a cause of action.

In addressing this question, the Court applied the longstanding presumption against extraterritoriality, ruling that, because there was "no affirmative indication in the Exchange Act that 10(b) applies extraterritorially... it does not." The Court then formulated a bright-line transactional test: "Section 10(b) reaches the use of a manipulative or deceptive device or contrivance only in connection with the purchase or sale of a security listed on an American stock exchange, and the purchase or sale of any security in the United States." Because the plaintiffs had purchased their NAB [ordinary] shares on foreign exchanges, the Court dismissed the suit for failure to state a claim upon which relief may be granted.

The Vivendi Decision

The parties agreed that *Morrison* had no impact on the Vivendi ADRs, which were listed and traded on the NYSE. They hotly disputed, however, whether purchases of Vivendi's ordinary shares on foreign exchanges could nonetheless be considered domestic transactions under *Morrison*. Vivendi's ADRs were sold in the United States as part of a public offering in 2000. To sell those ADRs through a public offering in the United States, Vivendi was required to register a corresponding number of ordinary shares with the SEC. Vivendi registered about 500 million ADRs with the SEC. It also listed an equivalent number of the ordinary shares on the NYSE to satisfy the above-mentioned requirement but did not make those shares available for trading purposes.

Plaintiffs therefore argued that because the ordinary shares underlying the ADRs were listed with a domestic exchange, all of Vivendi's ordinary shares should be considered to be so listed for purposes of the *Morrison* transactional test. In*Morrison*, Justice Scalia had echoed the statutory language when he explained that section 10(b) could be applied to securities*listed* on a domestic stock exchange.

The District Court, however, rejected the plaintiffs' "listing" argument as inconsistent with*Morrison*. Judge Holwell stated: "[t]here is no indication that the *Morrison* majority read section 10(b) as applying to securities that may be cross-listed on domestic and foreign exchanges, *but where the purchase and sale does not arise from the domestic listing*, particularly where (as here) the domestic listing is not even for trading purposes." (Emphasis added). Under this reading, the location of the trade must be in the U.S. to comply with *Morrison*. Accordingly, all foreign-cubed plaintiffs in *Vivendi* did not possess claims.

Judge Holwell also held that *Morrison* required the court to dismiss the claims of American purchasers of Vivendi's ordinary shares, so-called foreign-squared plaintiffs. American citizenship of the purchaser or seller does not bring the case within the ambit of 10(b) when the transactions involve foreign securities on foreign exchanges. "Though the Supreme Court in*Morrison* did not explicitly define the phrase 'domestic transactions' [in the second part of its test,] there can be little doubt that the phrase was intended to be a reference to the location *of the transaction*, not to the location of the purchaser and that the Supreme Court clearly sought to bar claims based on purchases and sales of foreign securities on foreign exchanges, even though the purchasers were American."

Thus, Judge Holwell dismissed the claims of all domestic and foreign purchasers of Vivendi ordinary shares -- estimated to be about 80 percent of the class -- and amended the class certification to include only those class members from the United States, France, England and the Netherlands who purchased or otherwise acquired Vivendi ADRs during the Class Period because those trades necessarily occurred on the NYSE.

In an attempt to sustain some of the claims of the class, the plaintiffs argued that the disqualified class members should be entitled to recovery under common law fraud. The court rejected this notion because the lower court's holding that Vivendi was liable for securities fraud could not be transformed into common law fraud due to the higher burden of proof applicable to the common law claim.

Denial of Vivendi's Motion for Judgment as a Matter of Law and Motion for a New Trial

With one significant qualification, the court upheld the jury's verdict as to what remained of Plaintiffs' case after *Morrison*. The court denied Vivendi's motions for judgment as a matter of law and for a new trial on most grounds. Vivendi argued that there was insufficient evidence to sustain the jury finding of liability. The court provided a lengthy recital of the evidence presented and disagreed with Vivendi's assertion. It found that there was sufficient evidence on the issues of whether Vivendi omitted material information and/or made misrepresentations, whether Vivendi acted with scienter and whether plaintiffs proved loss causation. Further, the court rejected Vivendi's other evidentiary and procedural arguments. It also concluded that the verdict against Vivendi, but in favor of the individual defendants, was not inconsistent because certain evidence that had been admitted as to the company was not admitted for use against the individuals.

Vivendi did prevail on an issue involving the jury's finding that on nine days during the Class Period, only one class of Vivendi's shares traded, and that, without support in the trial record, there was zero inflation in the price of the traded shares. Nevertheless, the court concluded that although this error indicated either confusion on the part of the jury or a clerical error in filling out the verdict form, it is not a "miscarriage of justice." Thus, it was not so egregious so as to justify a new trial and did not suggest that Vivendi was entitled to judgment as a matter of law. Rather, this problem could be cured if and when shareholders who purchased and sold shares on the nine days in question submitted claims.

Significantly, the court also agreed with Vivendi that the plaintiffs' request for entry of a final judgment was premature because Vivendi is entitled to rebut the presumption of reliance on the market price of its stock on an individual basis with respect to particular class members. The class members are not yet identified and Vivendi has not yet had the opportunity for this individualized assessment.

Conclusion

Vivendi is yet another in a string of recent decisions demonstrating the significant impact *Morrison* has had on securities litigation and its ability, so far, to withstand all attempts to limit its scope. Notably, *Vivendi* rejected the plaintiffs' "listing" argument and dismissed not only all foreign-cubed claims, but all foreign-squared claims as well.

As a result of Judge Holwell's decision, the*Vivendi* claims will proceed, albeit with significantly decreased class damages. The class will consist only of those shareholders who purchased ADRs because those securities were listed on a domestic exchange. Although a significant amount of claims remain, the effect of this ruling will be to reduce what was projected to be a $9.0 billion recovery by as much as 80 percent or more. This drastic reduction in the potential amount of this rare jury verdict illustrates the significant effect of the*Morrison* decision.

Vivendi also illustrates the tremendous litigation risks facing securities class action plaintiffs, even after the exceptionally rare achievement of a jury verdict. The court and the parties now face individualized issues of reliance by each ADR purchaser before any judgment may be entered, or any appeal of this decision taken.

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