LATIN LAWYER INSIGHT

The Guide to Corporate Crisis Management

Second Edition

Editors
Sergio J Galvis, Robert J Giuffra Jr and Werner F Ahlers

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Publisher's Note

Latin Lawyer is delighted to publish *The Guide to Corporate Crisis Management*.

Edited by Sergio J Galvis, Robert J Giuffra Jr and Werner F Ahlers of Sullivan & Cromwell LLP, and containing the knowledge and experience of over 40 leading practitioners from a variety of disciplines, it provides guidance that will benefit all practitioners when an unexpected crisis hits.

Corruption investigations, expropriation, industrial accidents: corporate crises take many forms, but each can be equally dangerous for companies in Latin America. Covering the impact of political instability, the role of communications in crisis response, approaches to bribery investigations and game plans in response to financial stress, this book is designed to assist key corporate decision-makers and their advisers in effectively planning for and managing corporate crises in the region.

We are delighted to have worked with so many leading firms and individuals to produce *The Guide to Corporate Crisis Management*. If you find it useful, you may also like the other books in the Latin Lawyer series, including our *Guide to Infrastructure and Energy Investment* and jurisdictional references.

My thanks to the editors for their vision and energy in pursuing this project and to my colleagues in production for achieving such a polished work.

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Securities Litigation After a Crisis: What Latin American Companies Can Expect in a US Court Proceeding

Brendan P Cullen[1]

The term 'securities fraud' likely brings to mind the sort of financial manipulations that, when exposed, have resulted in some of the United States' largest and highest-value class action lawsuits – think *Enron*, *WorldCom* and *Tyco*. But the United States' securities laws do not outlaw purely financial misdeeds. As numerous domestic and foreign issuers of securities in the United States have learned the hard way, nearly any sort of corporate crisis that negatively impacts an issuer's stock price can give rise to a securities class action lawsuit. And those lawsuits can impose substantial costs in terms of litigation costs, costs to resolve the lawsuits, and impositions on manager time and energy.

In the past decade, several large companies have been the subject of high-profile US securities class actions arising out of corporate crises in Latin America, including environmental disasters and corruption cases. These cases should serve as a warning to Latin American companies that issue securities in the United States that – in the event they face a corporate crisis – they may be hauled into US courts to defend themselves against a resulting securities class action lawsuit.[2] In this chapter, we outline the steps involved in defending against a securities class action lawsuit, from the filing of a complaint through motion to dismiss briefing to discovery and, finally, to trial (or, more likely, settlement). And we offer some guidance for increasing the chances of avoiding becoming a defendant in such a lawsuit (and for increasing the chances of prevailing in one).

1 Brendan P Cullen is a partner at Sullivan & Cromwell LLP. The author would like to thank Duncan C Simpson LaGoy and Rebekah T Raybuck, associates at Sullivan & Cromwell LLP, for their thoughtful contributions to this chapter.

2 The number of securities class action lawsuits filed against foreign filers (i.e., companies based outside the United States but listed on a United States exchange) has increased substantially over the last 10 years, with every region, including Latin America, experiencing a jump. Jane Njavro, 'Why D&O Costs Are Soaring For Foreign Filers', Woodruff Sawyer (14 August 2019, 1:23 PM), https://woodruffsawyer.com/do-notebook/do-costs-soaring-foreign-filers.

Complaint

As soon as news of a corporate crisis breaks that results in a meaningful drop in the value of that corporation's US securities (including common stock, ADRs or ADSs, or bonds), a cadre of US-based law firms that specialise in representing plaintiffs in US securities actions will begin investigating the incident and issue a public notice asking investors in the (allegedly) affected securities to join their securities class action lawsuit. Plaintiffs commence a securities lawsuit by filing a complaint in a US federal court. The complaint typically purports to be brought on behalf of a potential class of all purchasers of the defendant's securities during the period of the alleged fraud. Securities complaints are rarely brought as anything less than a class action. Alone or in small groups, it would be uneconomical for securities holders to assert their claims. As a class, they typically can allege damages of magnitudes that attract qualified plaintiffs' counsel and can justify the costs of a multi-year litigation.

Most post-crisis securities class actions are brought pursuant to Section 10(b) of the Securities Exchange Act of 1934 (the 1934 Act),[3] which prohibits material misstatements or omissions made by a company or its executives in the company's periodic filings with the US Securities and Exchange Commission (e.g., a Form 20-F) or in other public statements. To establish liability under this statute, a plaintiff must show that:

- the defendant made a material misrepresentation or omission;
- the defendant acted with scienter (i.e., the intent to defraud);
- there was a connection between the misrepresentation or omission and the plaintiff's purchase or sale of a security;
- the plaintiff relied upon the misrepresentation or omission;
- the plaintiff suffered economic loss (i.e., damages); and
- the plaintiff's losses were caused by the fraud.

Typically, plaintiffs will attempt to plead violations of the securities laws based on the theory that the company or its executives made false or misleading statements in connection with the sale of its securities (i.e., that the false or misleading statements caused the company's securities to trade at artificially inflated prices, and that plaintiffs would not have paid those prices had they known the truth about the company). In a complaint arising from a crisis, plaintiffs typically scour the issuer's prior public statements (including in SEC filings and during investor or analyst calls) for statements that appear inconsistent with what the crisis supposedly revealed about the issuer. So, for example, in the recently settled *Petrobras Securities Litigation*,[4] plaintiffs alleged that Petrobras and its executives touted the company's commitment to transparent and appropriate business conduct while concealing high levels of corruption from investors, thereby inflating Petrobras's share price, and that the 'truth was revealed' when several senior-level Petrobras managers were arrested on corruption-related charges.

3 15 U.S.C. § 78a et seq.

4 Case No. 14-cv-9662 (JSR) (S.D.N.Y. 2014).

Similarly, in *In re BHP Billiton Limited Securities Litigation*,[5] shareholders brought suit under the 1934 Act following the failure of a tailings dam operated by a Brazilian non-operated joint venture between BHP's Brazilian subsidiary and another company, which caused 19 fatalities and environmental damage. Plaintiffs alleged that BHP was aware of structural problems with the dam before it failed and had made misleading statements about the company's commitment to health and safety and the adequacy of its safety and risk management protocols.

The securities litigation arising out of the Deepwater Horizon incident, *In re BP p.l.c. Securities Litigation*,[6] followed the same pattern. In May 2010, there was a catastrophic explosion on one of BP's mobile offshore drilling rigs (known as Deepwater Horizon) located in the Gulf of Mexico. The price of BP's securities tumbled in the wake of the crisis. Plaintiffs alleged that BP and its senior executives violated the 1934 Act by misrepresenting that the company was committed to safe operations at its drilling units in the Gulf of Mexico and had adequate internal risk management practices, when in fact it had been cutting spending on safety to reap maximum profits.[7]

Lead plaintiff selection and the amended complaint

In securities fraud class actions, the initial complaint is typically not intended as an operative complaint, but rather as a placeholder for the law firm that filed the complaint, which hopes to be appointed lead counsel for the class. Plaintiffs' law firms and shareholders have 60 days from the date the first complaint was filed to apply to the court to be named 'lead plaintiff/lead counsel.' Often several plaintiffs and law firms vie for the roles of lead plaintiff and lead counsel. Usually, courts appoint the applicant with the largest claimed losses as lead plaintiff, which is typically a state or municipal pension fund.

Once appointed, the lead plaintiff typically files an amended complaint that contains more detailed allegations of securities violations than the initial complaint. Whereas an initial complaint usually is several dozen pages in length, the amended complaint regularly exceeds a hundred pages and quotes heavily from news reports and public statements by government officials, including officials investigating the crisis, and other third parties who were affected by the crisis. In preparation of the amended complaint, lead plaintiff may contact defendant's former employees and consultants and seek their cooperation in developing the allegations of the amended complaint. Amended complaints sometimes include quotes from these individuals, who are identified in the amended complaint as 'confidential witnesses'. Plaintiffs are not required to disclose the identities of these witnesses unless the case is allowed to proceed to discovery (discussed below).

5 Case No. 16-cv-1445 (S.D.N.Y. 2016).

6 Case No. 4:10-md-02185 (S.D. Tex. 2011).

7 Sullivan & Cromwell LLP represented BP and BHP in these securities litigations, and the author of this chapter represented BHP.

Motion to dismiss

Overview

After a lead plaintiff has been selected and has filed an amended, operative complaint, a defendant has the opportunity to file, and nearly always files, a motion to dismiss the action on the basis that the pleadings fail adequately to allege the elements of their securities fraud claim.[8] Not only is discovery typically stayed during the pendency of these motions – allowing the defendant time to consider the plaintiffs' claims against them without the pressure of document collection and threat of depositions – they are the most common way that defendants defeat a securities action short of settlement.

The standard the court applies to decide a motion to dismiss favours the plaintiff: a court 'must accept as true all of the factual allegations set out in plaintiff's complaint, draw inferences from those allegations in the light most favorable to plaintiff, and construe the complaint liberally'.[9] To the benefit of defendants, however, the US Private Securities Litigation Reform Act (PSLRA) requires that plaintiffs plead their claims with 'particularity', meaning that plaintiffs must identify in their complaint 'each statement alleged to have been misleading' and 'the reason or reasons why the statement is misleading', as well as the facts that plaintiffs allege give rise to 'a strong inference that the defendant acted with the required state of mind'.[10]

If the plaintiffs' complaint does not specifically identify the allegedly fraudulent statements and explain why they were misleading and why defendants had the requisite state of mind, the court will dismiss the complaint (likely without prejudice to amend the complaint at least one more time). By requiring plaintiffs to set forth their allegations with particularity, the PSLRA helps defendants to understand plaintiffs' allegations and to put forth explanations for why they fail to state a claim under US securities laws.

Under a typical briefing schedule, a defendant has 60 days to move to dismiss the amended complaint, the lead plaintiff has 60 days to oppose the motion and the defendant has 45 days to reply. If the court holds a hearing, it will typically follow the reply brief by two or so weeks. The court may then take a period of weeks or months to decide the motion. The court can grant the entire motion or can dismiss only certain claims. Even if the motion is granted, the court will usually dismiss the complaint with leave to amend, permitting the lead plaintiff another 60 days to amend the complaint to address, if possible, whatever deficiencies the court identified. That second amended complaint will then become subject to another round of motion to dismiss briefing, which process can be repeated multiple times. Between 1997 and 2016, 43 per cent of all securities class actions were eventually dismissed with prejudice.[11]

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8 Fed. R. Civ. Proc. 12(b)(6). Depending on the circumstances, a Latin American company or a non-resident individual defendant may be able to file a motion to dismiss for lack of personal jurisdiction – i.e., that the defendant does not have sufficient contacts with the United States that it could be subject to a lawsuit in the United States.

9 *Roth v. Jennings*, 489 F.3d 499, 510 (2d Cir. 2007).

10 15 U.S.C. § 78u-4(b)(1)-(2).

11 Cornerstone Research, 'Securities Class Actions, 2017 Year in Review', at 15 (28 January 2018), available at https://www.cornerstone.com/Publications/Reports/Securities-Class-Action-Filings-2017-YIR.

Typical arguments

Typically only three elements of a securities fraud claim are susceptible to a motion to dismiss: falsity, materiality and scienter. Additionally, depending on the circumstances, a non-American corporate defendant also may be able to argue that the court lacks jurisdiction because the securities at issue did not trade on a US securities exchange.

Falsity

At the most basic level, a plaintiff must allege that a company made statements that were false when they were made. After a crisis has occurred, securities class action plaintiffs may point to prior statements by the company that were accurate when made but, in hindsight, appear misleading because they do not disclose details which, post-crisis, seem important. For example, a lead plaintiff may point to (accurate) statements regarding historical production capacity for a plant that suffered a catastrophe and stopped production, arguing that the historical information was misleading because it did not predict that the plant would need to be closed. But a defendant may be able to dismiss these types of claims where it can demonstrate that the lead plaintiff failed to allege that the statements were in fact inaccurate when made.[12]

Materiality

In addition to being false, for an omission or misstatement to be actionable under Section 10(b), it must be 'material' to a reasonable investor, that is, there must be a 'substantial likelihood that the disclosure of the [relevant information] would have been viewed by the reasonable investor as having significantly altered the "total mix" of information made available'.[13] But, 'where the alleged misstatements are so obviously unimportant to a reasonable investor that reasonable minds could not differ on the question of their importance, a court may find the misstatements immaterial as a matter of law.'[14] A common category of statements that are 'immaterial as a matter of law' is so-called 'puffery', which refers to 'an optimistic statement that is so vague, broad, and non-specific that a reasonable investor would not rely on it'.[15] Examples of statements that courts have held to be puffery include alleged misstatements about being 'committed to safely producing the energy we all need' and 'preserving the environment',[16] and statements about a company's 'commitment to quality, safety, and corporate citizenship'.[17]

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12 *Boca Raton Firefighters & Police Pension Fund v. Bahash*, 506 F. App'x 32, 39 (2d Cir. 2012) ('[A] violation of federal securities law cannot be premised upon a company's disclosure of accurate historical data.') (citation omitted).

13 *Matrixx Initiatives, Inc. v. Siracusano*, 131 S. Ct. 1309, 1318 (2011).

14 *Feinman v. Dean Witter Reynolds, Inc.*, 84 F.3d 539, 540–41 (2d Cir. 1996).

15 *In re General Elec. Co.* Secs. Litig., 857 F. Supp. 2d 367, 384 (S.D.N.Y. 2012).

16 *In re Anadarko Petroleum Corp.* Class Action Litig., 957 F. Supp. 2d 806, 820 (S.D. Tex. 2013).

17 *In re Ford Motor Co.* Sec. Litig., 381 F.3d 563, 570 (6th Cir. 2004).

Scienter

Scienter often is one of the more difficult elements of a Section 10(b) claim for a plaintiff to allege because, as discussed, the PSLRA requires that plaintiffs 'state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind'.[18] In practice, plaintiffs typically try to plead scienter with allegations tending to show that company executives who were responsible for the allegedly misleading statements were aware of contemporaneous facts inconsistent with those statements. These contemporaneous facts must be pleaded specifically and it must be demonstrated credibly that those facts were known (or must have been known) to the specific company executives accused of having made misstatements. Under US Supreme Court precedent, courts typically conduct searching reviews of these allegations and only permit a complaint to survive a motion to dismiss if, based on the facts alleged in the complaint taken collectively, 'a reasonable person would deem the inference of scienter cogent and at least as compelling as any opposing inference [of non-fraudulent intent].'[19]

Extraterritoriality

Latin American (and other non-US) companies may have an additional basis on which to dismiss a securities fraud complaint if their securities do not trade on US exchanges. In *Morrison v. National Australia Bank Ltd.*, the Supreme Court held that US securities laws do not apply 'extraterritorially' and limited Section 10(b) claims to 'transactions in securities listed on domestic [US] exchanges, and domestic [US] transactions in other securities'.[20] Practically, this means that if a company's securities do not trade directly on a US securities exchange (e.g., the New York Stock Exchange) and only trade on secondary markets, a plaintiff will need to plead facts showing that it purchased the securities in a 'domestic' US transaction. Specifically, a plaintiff must include facts 'suggesting that [plaintiff] became irrevocably bound' in the United States or 'that title was transferred within the United States, including, but not limited to, facts concerning the formation of the contracts, the placement of purchase orders, the passing of title, or the exchange of money'.[21]

Even if a US-based investor purchases securities on exchanges outside the United States, it likely will not be able to bring Section 10(b) claims against the company.[22]

These arguments have been successful in the US District Court for the Southern District of New York, where a disproportionate number of securities actions are filed. For example, a court in the Southern District of New York recently dismissed a securities lawsuit brought by 'a Brazilian/Cayman Island plaintiff against Brazilian defendants regarding Brazilian bonds and claims which relate to a Brazilian catastrophe' in which the 'bonds [at issue] were never listed on a U.S. exchange and were principally offered and sold outside the United States'.[23]

18 15 U.S.C. § 78u-4(b)(2)(A).

19 *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 324 (2007).

20 561 U.S. 247, 267 (2010).

21 *Absolute Activist Value Master Fund Ltd. v. Ficeto*, 677 F.3d 60, 70 (2d Cir. 2012).

22 *In re UBS* Secs. Litig., 2011 WL 4059356, at *5 (S.D.N.Y. Sept. 13, 2011) (holding that claims asserted by US investors who purchased UBS stock on a foreign exchange were barred, even though the orders were placed from the United States).

23 *Banco Safra S.A. – Cayman Islands Branch v. Samarco Mineração S.A.*, 2019 WL 2514056, at *2, 4–6 (S.D.N.Y. 18 June 2019).

Extraterritoriality requires, however, a fact-intensive inquiry that may be applied differently depending on the court in which the action is proceeding.

Discovery

Overview

For Latin American companies that are defendants in US securities actions, US-style discovery is often one of the most surprising and disconcerting aspects of the litigation. Discovery refers to the pretrial process by which each party to a lawsuit can obtain information from the other party or third parties related to the issues in the case. Under the US Federal Rules of Civil Procedure (the Federal Rules), discovery is very broad: parties 'may obtain discovery regarding any non-privileged matter that is relevant to any party's claim or defense and proportional to the needs of the case'.[24] Parties may withhold documents and other information based on certain privileges, the most common of which is attorney–client privilege, which protects from disclosure confidential attorney–client communications. In practice, however, defendants are expected to have preserved, and to provide plaintiffs with equal access to, large volumes of non-privileged documents and other information in defendants' possession or control that are relevant to the parties' claims and defences, even where the relevance of the materials is limited and the burden on defendants of collecting and producing that information is substantial and disproportionate to the burden on plaintiffs. To preserve these materials, one of the first steps that a company should take following the filing of a complaint is to issue a notice to its employees to preserve email and any other documents that may be within the scope of discovery.

Before parties produce any documents or information in discovery, the parties will negotiate a confidentiality agreement and ask the court to enter the agreement as a protective order to ensure that confidential information exchanged by the parties is not shared with third parties. Stipulated protective orders typically permit the producing party to unilaterally designate certain information or documents as 'confidential', limit the individuals or entities that can access the protected materials, prohibit protected information from being used for any purpose other than prosecuting the action, and forbid parties from filing confidential materials in public court documents (instead requiring the filing to be done 'under seal' or with appropriate redactions).

There are four primary devices for obtaining pretrial discovery: requests for production of documents; interrogatories; requests for admissions; and depositions. In a typical US litigation, discovery can begin almost immediately after a complaint is filed. Securities actions in federal court are subject to a different rule, and, absent extraordinary circumstances, discovery is stayed by the PSLRA until any motion by the defendants to dismiss the complaint is finally denied – sometimes not until after the court has required the plaintiff to amend its complaint multiple times.[25] To facilitate the discovery process, the parties are required by the Federal Rules to exchange initial disclosures that, among other things, identify

24 Fed. R. Civ. P. 26(b)(1).

25 See 15 U.S.C. § 78u-4(b)(3)(B).

individuals who would likely have information relating to plaintiffs' surviving claims and defendants' defences to those claims.[26]

Discovery in US securities class actions typically takes at least one year, sometimes several. Courts expect the parties to work out discovery disputes among themselves, but if the parties cannot resolve a dispute, they may raise it with the court.[27] The party seeking discovery may move to compel disclosure or discovery; the party from whom discovery is sought may move for a protective order.[28]

Discovery in securities class actions is much more burdensome for defendants than it is for plaintiffs because most of the information concerning the major factual issues in the case (e.g., whether company executives knowingly made false or misleading statements in periodic filings) will be in the defendants' possession. Plaintiffs therefore typically seek as much information as possible, both to seek information for use in resisting summary judgment or in prevailing at trial and as a tactic to increase the costs and burdens to defendants and encourage settlement.

Document production

Discovery typically begins with requests for the production of documents, which identify broad categories of documents relevant to a party's claims (e.g. 'All documents concerning BP's operation of the Deepwater Horizon Drilling Platform'). In complex securities class actions, defendants may be required to produce electronic data equivalent to millions of pages of documents. Even documents located outside the United States may be discoverable if the defendant has control over the documents. Cross-border discovery can present complications; counsel should be aware of foreign countries' privacy laws or 'blocking statutes' restricting the transfer of documents to the United States.

Within 30 days of receiving the document requests (or some other time period to which the parties have agreed), the responding party must serve written responses and objections to the requests. Once the responses and objections have been served, the parties' respective counsel will typically participate in a series of meetings, during which they will discuss plaintiffs' requests and negotiate a joint document production protocol covering, for example, the individuals whose documents should be searched (referred to as 'custodians'), the relevant time period and the search terms to be applied to the custodians' documents. Once the parties have agreed on a document production protocol, the responding party must begin the costly process of collecting documents from custodians, running the agreed-upon searches over those custodians' documents, reviewing the documents for responsiveness and privilege, and producing non-privileged documents that are responsive to plaintiffs' requests. Privileged documents redacted or withheld on that basis must generally be noted in a log, which the responding party will provide to the propounding party. The propounding party may move to compel the production of documents it believes were inappropriately withheld, including those claimed by the responding party to be privileged.

26 Fed. R. Civ. P. 26(a)(1)(A).

27 See Fed. R. Civ. P. 37(a)(1).

28 See Fed. R. Civ. P. 26(c), 37(a).

Written discovery

In addition to document production requests, parties may serve written discovery requests through two methods: interrogatories and requests for admission. Interrogatories are written questions about factual matters at issue in the lawsuit that are propounded by one party to be answered by the opposing party. For example, plaintiffs in a securities class action might ask the company to identify those of its employees who were involved with drafting the filings that are alleged to contain misstatements or who were responsible for the aspect of the defendants' business involved in the crisis. Requests for admission are written requests to the opposing party to admit the truth of any factual matters within the scope of allowable discovery. For example, in a securities case alleging that the company misrepresented that it was committed to safety, plaintiffs might ask defendants to admit that the company reduced spending on safety during the fiscal years leading up to the disaster.

Depositions

In the United States, depositions are a mechanism for obtaining testimony from an individual or an entity under oath prior to trial. Deposition testimony may be used to support pretrial motions or as evidence at trial (subject to any hearsay or other evidentiary objections the parties may raise before trial). The Federal Rules of Civil Procedure provide for a maximum number of depositions in a federal case of 10 per side (i.e., 10 for the plaintiffs as a group; 10 for the defendants as a group). In complex cases, however, defendants should expect courts to grant additional depositions, and plaintiffs often request 20 or more (sometimes many more) depositions.

Plaintiffs may seek depositions of defendants' current and former directors, officers and employees, and consultants and other third parties. Counsel for the parties will generally negotiate the number of depositions and identities of the deponents. Counsel also will negotiate the timing and location of depositions to try to limit the inconvenience to both witnesses and counsel. In addition to taking the depositions of individuals, US rules permit the deposition of an entity or organisation itself, in which circumstance the entity must nominate one or more individuals to testify on the company's behalf and must educate the witness about the topics of the deposition.

If the witness named in the deposition notice is an officer, director or 'managing agent' of a corporate party, the corporation is required to produce that witness for a deposition, even if he or she is located abroad.[29] A corporate employee or agent who does not qualify as an officer, director or managing agent is not subject to deposition by notice, and the deposing party must use some other means to compel the witness's attendance (such as a subpoena under Rule 45 of the Federal Rules). Because defendants often wish to be involved in the preparation of even non-officer employees for their depositions, counsel for defendants frequently agree to make those employees available for deposition without a subpoena.

For witnesses located outside the United States, depositions may occur in the witness's home jurisdiction or other locations outside the United States, but such depositions may

29 Fed. R. Civ. P. 37(d)(1)(A)(i); see, e.g., *Dubai Islamic Bank v. Citibank*, N.A., 2002 WL 1159699, at *5-6 (S.D.N.Y. 31 May 2002) (managing agent located abroad subject to deposition notice).

be subject to additional procedures and costs. The court may also require witnesses located abroad to travel to the United States to be deposed when the witnesses regularly travel to the United States or legal or practical considerations make taking the deposition in a foreign country difficult, such as when the witness's home country does not allow for depositions.[30] The court can also order recalcitrant witnesses located outside the United States to be questioned prior to trial, including through treaties, such as the Inter-American Convention on Letters Rogatory.

Witnesses typically spend several hours (or more) with counsel before their depositions to review documents, refresh their recollections of significant events, and prepare for the sorts of questions they are likely to be asked by plaintiffs' counsel. Depositions are recorded by audio, video or stenographic means and typically take place in a law firm conference room. These recordings can be admissible at trial (though trials are exceedingly rare in securities actions, as discussed below) in place of live witness testimony or to impeach a witness who testifies at trial.

While the Federal Rules presumptively limit depositions to seven hours, that is testimony time and the deposition itself (including breaks) can take as long as 10 hours from start to finish. Because preparing for depositions is expensive and time-consuming, plaintiffs will use often them as a litigation tactic to increase the burden on defendants and as a pressure point for settlement negotiations. In fact, plaintiffs will commonly ask to depose senior executives (the CEO included). They often do so in part because senior executives usually will have made some or all of the alleged misstatements in question or certified the disclosures that contained the statements, and therefore their testimony is relevant to plaintiffs' allegations. They also do so, however, to exert pressure on defendants, which often would prefer to avoid the cost, inconvenience and potential embarrassment of having their senior executives sit for depositions.

The parties will receive a transcript of the deposition after it is completed. Because deposition transcripts are not filed with the court as a matter of course, deposition testimony ordinarily will not be within the scope of public access until it is submitted as evidence in support of a motion or at trial. Counsel should specify procedures in the stipulated protective order (see 'Discovery: Overview') for protecting sensitive or confidential material in a deposition transcript from public disclosure.

Expert discovery

Once the parties have completed fact discovery, they will typically engage in expert discovery regarding damages calculations or any other topic upon which testimony from a subject-matter expert might be helpful to the judge or jury in deciding the case. Expert

30 *See Fausto v. Credigy Servs. Corp.*, 251 F.R.D. 427 (N.D. Cal. 2008) (ordering depositions of four Brazilian nationals to occur in the United States because Brazilian law prohibited US lawyers from taking depositions in Brazil, and defendant often hosted Brazilian employees in the US). 'Brazilian authorities do not permit persons, such as American attorneys, to take depositions for use in a court in the United States before a US consular officer, with the assistance of a Brazilian attorney, or in any other manner.' US Department of State, Brazil (14 August 2019, 1:48 PM), https://travel.state.gov/content/travel/en/legal/Judicial-Assistance-Country-Information/Brazil.html. Other countries impose similar restrictions on the taking of depositions of their nationals.

discovery typically includes the exchange of lengthy written reports setting forth the opinions of each potential expert that either party intends to offer (including to rebut the opinions of the other side's experts) and the depositions of such experts. Plaintiffs typically do not allege potential damages until expert discovery (except they often will provide preliminary settlement calculations in relation to settlement discussions), and even then they may attempt to avoid specifying damages until trial.

To maximise their alleged damages, plaintiffs often calculate damages by asserting that most, if not all, of the amount of the post-crisis stock drop is attributable to the revelation of the alleged fraud, and multiplying that amount against an estimation of the number of securities that were purchased in the United States during the period of the alleged fraud and held until after the stock drop. In anticipation of or in response to criticism from defendants, plaintiffs will sometimes temper their calculations by conceding, among other things, that portions of the stock drop cannot be attributed to the revelation of the alleged fraud or the price of the securities in question could not have been inflated by the same amount throughout the period of the alleged fraud. It can, however, be challenging to prove and oppose damages calculations, and, as discussed below, on the rare occasion that a case proceeds to trial, damages typically turn on the credibility of the parties' competing expert witnesses rather than hard facts.

Class certification

In a securities class action, a single lead plaintiff (or sometimes several plaintiffs) asks the court to allow it to represent the interests of a large group of individuals or institutions known as the class that were allegedly injured in the same way by defendants' actions. For the action to be certified as a class action, the lead plaintiff must demonstrate that the action meets four prerequisites: the class is numerous (generally over 40 members); there are at least some questions of law or fact that are common to the class; the lead plaintiff is 'typical' of the class; and the lead plaintiff (and lead counsel) will fairly and adequately protect the interests of the class.[31] Additionally, securities class actions must generally meet an additional requirement, that the questions of law or fact that are common to the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for resolving the dispute.[32]

Class certification is often difficult for a defendant in a securities action to oppose because securities class actions typically involve many class members with the same claims that are represented by well-qualified law firms that frequently litigate class actions. Only around 15 per cent of cases reach a decision on class certification, as most cases will either be dismissed or will settle before they reach the class certification stage.[33] But of the cases that reach a decision, courts grant class certification around 89 per cent of the time.[34]

31 Fed. R. Civ. P. 23(a).

32 Fed. R. Civ. P. 23(b)(3).

33 Stefan Boettrich and Svetlana Starykh, NERA Economic Consulting, Recent Trends in Securities Class Action Litigation: 2018 Full-Year Review, at 21 (29 January 2019).

34 id.

Settlement

Settlement discussions may occur at any time. In the majority of cases, however, settlement discussions typically occur after document discovery and at least some depositions have been completed. This level of discovery allows the parties some insight into whether the factual record supports plaintiffs' allegations. Additionally, parties are often wary of suggesting earlier settlement negotiations lest they appear to their adversary to be unusually eager to settle (and thus potentially agreeable to a settlement their adversary would find unusually favourable). Further, because in class actions the court determines whether to approve settlements and plaintiffs' counsels' legal fees (which are paid from the settlement proceeds), plaintiffs' counsel typically prefer to engage in some discovery prior to settlement to demonstrate that they have done sufficient work to understand the value of plaintiffs' claims and therefore the reasonableness of the settlement, and to justify a higher fee award.

In the course of settlement discussions, plaintiffs often provide at least an indication of the damages they anticipate asserting at trial. Typically, cases settle at a substantial discount to plaintiffs' damages calculations, but the size of that discount varies widely. Settlement discussions typically involve an in-person mediation before a mediator selected by the parties. If the case is not settled during the mediation itself, as often is the case, the discussions typically continue after the mediation, often over several weeks or months, and involve multiple rounds of offers and counter-offers brokered by the mediator. With the assistance of counsel, defendants typically keep directors and officers insurance carriers updated on developments in settlement discussions, including the selection of a mediator (if the parties agree to retain one), and seek their carriers' approval of any settlement offers to ensure that, to the greatest possible extent, the carriers pay the costs of any eventual settlement.

Securities class action settlements can vary widely depending on the estimated damages, whether there are related proceedings (e.g., criminal or regulatory charges brought against the company) and other underlying factual circumstances (e.g., unhelpful documents or witness testimony that arise during discovery). In 2017, 51 per cent of securities class actions settled for US$5 million or less, while several cases settled for over US$100 million.[35] In one of the largest securities class action settlements to date, the Petrobras Securities Litigation settled for US$3 billion.[36]

Summary judgment and trial

As a practical matter, nearly 100 per cent of US securities class actions are either dismissed by the court or settled prior to trial. If a case does not settle, however, defendants have two additional opportunities to defeat plaintiffs' claims.

35 Bulan, Ryan and Simmons, Cornerstone Research, Securities Class Action Settlements, 2017 Review and Analysis, at 8 (13 March 2018), available at http://securities.stanford.edu/research-reports/1996-2017/Settlements-Through-12-2017-Review.pdf.

36 Memorandum of Law In Support of Class Plaintiffs' Motion for Final Approval of Settlement and Plan of Allocation at 1, In re Petrobras Secs. Litig., 317 F. Supp. 3d 858 (S.D.N.Y. 2018). This settlement also represents the largest single payout by a foreign issuer in the history of securities class actions. id. at 2.

First, after fact and expert discovery are completed, defendants can move the court for summary judgment on plaintiffs' claims. To prevail, defendants must demonstrate that, based on the documents and deposition testimony produced in discovery, there is no material issue of disputed fact that remains to be resolved and that defendants are entitled to a judgment as to some or all of the plaintiffs' surviving claims.[37] It can be difficult to win a summary judgment motion because in deciding the motion, the court must make all inferences in favour of the non-moving party (typically the plaintiff), and must find that there is no dispute about any facts necessary to make its decision. Once filed, the court may not issue a decision on a motion for summary judgment for several months or longer.

Second, a company can defeat a lead plaintiff's claims at trial. In a trial, a lead plaintiff must convince a jury selected from members of the public (or, in some cases, a judge) that the evidence it has compiled proves that it is more likely than not that the defendants violated US securities laws. The parties will each have an opportunity to introduce documents and to call witnesses, and the jury or judge will decide whether lead plaintiff has met its burden. Trials of securities class actions are exceedingly rare because they are expensive – it can take hundreds or thousands of hours to prepare for and try a case – and because they are risky – defendants could be found liable for the full amount of lead plaintiff's alleged damages, or they could be found not liable at all.

How to avoid a securities lawsuit or minimise its impact

Some Latin American companies that issue securities in the United States view securities class actions as an unavoidable cost of raising capital in the United States. There are, however, practices that companies can adopt to avoid a securities action and to minimise the impact once an action has been filed.

How to avoid a lawsuit

The essential ingredients of a securities action are a crisis and resulting stock drop, and disclosures that can be alleged to be misleading. While crises cannot always be avoided, Latin American companies can take steps to make their disclosures less susceptible to securities actions. First, companies should not make broad but definitive statements such as 'accountability, safety or efficient capital allocations is our top priority'. While these statements have the feel of immaterial statements or puffery on which investors could not reasonably rely, some US courts have found the potential materiality of statements like these to be sufficient to survive a motion to dismiss. Further, statements of this kind are sufficiently broad that creative plaintiffs' counsel can use them as hooks for claims in relation to a wide variety of crises that correlate with stock drops. From a litigation perspective, a better approach to statements like these is to reframe them in less definitive terms, such as that 'sustainability' (for example) is 'a priority' rather than 'our top priority'.

Second, companies should be careful to explain accurately in their disclosures their relationships with subsidiaries, joint ventures and other entities. The more entities to which

37 The lead plaintiff can also move for summary judgment, and occasionally will – typically on discrete issues where they believe they can show that there are no factual disputes.

a company's disclosures can be construed to apply, the more opportunities plaintiffs have to link the company to a crisis. If a company does not intend for portions of its disclosures to apply to certain entities, the company should make that clear. The company's disclosures should state clearly that specific sections of the disclosure or certain topics do not apply to the entities in question (e.g., 'statements regarding our values and operations do not apply to our non-operated assets'). Likewise, when describing actions taken by other entities to which the company's disclosures do not apply, the company's disclosures should not attribute those actions to the company by using words such as 'we', 'our' and 'us' to describe who took those actions.

Finally, companies should take care to ensure the accuracy of their disclosures both pre- and post-crisis. In the high-pressure environment that exists post-crisis, where good news is at a premium and companies can experience an all-too-understandable desire to assuage the concerns of investors, customers, regulators, employees and others, companies sometimes exacerbate the situation by issuing disclosures that are too positive. While these disclosures may bring momentary relief from post-crisis scrutiny, when these disclosures are shown to have been too rosy, they often become the subject of a securities action.

In fact, many securities actions allege both pre- and post-crisis misstatements. In the BP securities litigation arising from the Deepwater Horizon incident, some of the most difficult allegations for the company to defeat were plaintiffs' allegations that some of BP's post-incident statements regarding the volume of petroleum leaking into the Gulf of Mexico were misleading. An awareness of this tendency and vigilant policing of post-crisis statements is critical. 'I don't know' is a difficult thing to say when answers are demanded, but it is often a far better response than a bold pronouncement that proves inaccurate.

How to minimise the impact of an action

The impacts of a securities litigation on a company can be myriad, ranging from bad press to distracting senior executives and other personnel to the cost of defending and settling (if necessary) the case. Once a litigation has been filed, some of these impacts cannot be avoided, and others can be mitigated through close coordination between the company's officers and in-house counsel, and experienced outside counsel. There are, however, steps that a company can take pre-incident to minimise the potential impact of an action.

Maintaining a clear corporate structure and well-defined reporting lines, and observing corporate formalities, can reduce the burden of discovery. Clarity on these issues pre-litigation allows the company to negotiate the scope of discovery with plaintiffs with a clear view of which entities within its corporate structure were involved in the underlying issues, which employees may have relevant documents, and what rights the company may have in order to obtain documents from those entities and their employees. This clarity can reduce the number of potential sources of discovery and therefore the disruption to company officers and employees, and the cost of the discovery process. It also may help to reduce the likelihood for discovery disputes with plaintiffs, which can be time consuming and costly, and result in negative press if the parties bring their disputes to the court.

Similarly, having well-defined company-wide document retention policies and practices can greatly reduce the burden of discovery by facilitating the document collection process. Absent these policies and practices, document collection can be disruptive to company officers, who must provide information on where documents they use or create are housed, and stress internal legal and technology departments, which must divert resources to the collection process. Further, it is in the company's best interests to ensure that the documents it will need to defend its conduct are preserved and reasonably accessible.

Finally, the impact of litigation can be mitigated by purchasing directors and officers insurance pre-litigation, and maintaining a collaborative relationship with the insurance carriers throughout the litigation. Most obviously, insurance can reduce the costs of defending the litigation and paying a resulting settlement or judgment if necessary. Carriers, as repeat players in securities actions, also have a wealth of information about aspects of securities litigations. Carriers can be a useful sounding board for defences, and a source of advice on, among other things, potential mediators, plaintiffs' counsel's negotiating habits and style, and historical settlements in other cases.

Conclusion

Each year, investors file hundreds of securities class actions in US federal courts accusing companies that have issued securities in the United States of committing fraud in relation to the sale of those securities. These actions arise from myriad types of corporate crises. Some companies are repeatedly defendants in these lawsuits. The costs of defending these suits – in terms of money, time and public relations – can be high. It is not, however, a foregone conclusion that all issuers will someday defend a securities class action. Nor are defendants defenceless to plaintiffs' claims or the burdens of these cases. With careful planning, companies that issue securities in the United States can reduce their exposure to securities litigation, and, if sued, adopt defence strategies that lower defence costs and increase the likelihood that the case will be resolved in a positive manner.

Appendix 1

About the Authors

Brendan P Cullen

Sullivan & Cromwell LLP

Brendan Cullen is a partner at Sullivan & Cromwell LLP's litigation group and serves as coordinator of the firm's appellate practice. Mr Cullen has litigated a broad range of matters, including complex securities, commercial, intellectual property and competition litigation, frequently with a substantial technological element. He has advised and represented clients in arbitrations, in cases in state and federal trial courts and on appeals before state and federal appellate courts, including the US Supreme Court. He also has conducted numerous confidential internal investigations, including investigations related to issues of corporate governance, securities matters and Foreign Corrupt Practices Act compliance, and involving numerous countries throughout Asia, Europe, the Middle East and Latin America.

Sullivan & Cromwell LLP

125 Broad Street
New York, NY 10004-2498
United States
Tel: +1 212 558 4000
Fax: +1 212 558 3588
cullenb@sullcrom.com
www.sullcrom.com

Corruption investigations, expropriation, industrial accidents: corporate crises take many forms, but each can be equally dangerous for companies in Latin America.

Published by *Latin Lawyer*, edited by Sergio J Galvis, Robert J Giuffra Jr and Werner F Ahlers of Sullivan & Cromwell LLP, *The Guide to Corporate Crisis Management* is designed to assist key corporate decision-makers and their advisers in effectively planning for and managing corporate crises in the region. More than 40 leading practitioners from a variety of disciplines have contributed their knowledge and insights from their experience.

Covering the impact of political instability, the role of communications in crisis response, approaches to bribery investigations and game plans in response to financial stress, this book provides guidance that will benefit all practitioners when an unexpected crisis hits.

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