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CLIENT ALERT

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Second Circuit Rejects "Listing Theory," Finds That Cross-Listing on a US Exchange Is Insufficient to Justify an Exception Under *Morrison*

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In a case of first impression, the US Court of Appeals for the Second Circuit recently held in a published opinion that the Supreme Court's decision in *Morrison v. National Australia Bank Ltd.*, 561 US 247 (2010), precludes Securities Exchange Act of 1934 ("Exchange Act") claims brought by a putative class of foreign and domestic purchasers of shares of UBS AG—a foreign issuer listed on a foreign exchange—even where those shares were cross-listed on a US exchange. *City of Pontiac Policemen's and Firemen's Retirement System v. UBS AG*, No. 12-4355-cv, 2014 US App. LEXIS 8533 (2d Cir. May 6, 2014). This ruling, which affirmed Judge Richard Sullivan's dismissal with prejudice of all claims in plaintiffs' amended complaint, further demonstrates that the focus of US securities laws is on domestic transactions and not the location of the securities exchange or the citizenship of the purchaser. The ruling also establishes that foreign issuers will not incur liability under the Exchange Act simply by cross-listing on a US exchange. Separate from its holdings on *Morrison*, the court affirmed the dismissal of the remaining securities claims under the Securities Act of 1933 ("Securities Act") and the Exchange Act, finding that UBS's alleged general statements regarding corporate policies, regulatory compliance, risk management, and portfolio valuation are

immaterial and do not establish scienter. The Second Circuit also affirmed the district court's decision to deny plaintiffs further leave to amend their complaint.

Reading *Morrison* As A Whole

"Foreign Cubed" Claims — The Court Rejects The "Listing Theory" As An Exception To Morrison

A "foreign cubed" claim involves claims by foreign plaintiffs suing a foreign issuer based on securities transactions in foreign countries. In *Morrison*, the Supreme Court rejected the assertion that Section 10(b) of the Exchange Act provides a private cause of action for foreign-cubed claims; instead, the Court held that US securities laws only apply to "transactions in securities listed on a domestic exchange" and to "purchases and sales of securities in the United States." *Morrison*, 561 US at 267. The *City of Pontiac* plaintiffs argued, however, that *Morrison*'s preclusive effect was limited to claims relating to securities "*[not] listed*" on a domestic exchange. Op. at 11-12 (emphasis and alteration in original) (citing *Morrison*, 561 US at 273). Under this "listing theory," plaintiffs argued that they could bring Section 10(b) claims against a foreign issuer based on foreign transactions, because the relevant shares were cross-listed on the New York Stock Exchange. Op. at 11-12.

The Second Circuit firmly rejected plaintiffs' argument, holding that the listing theory is "irreconcilable with *Morrison* read as a whole." *Id*. Instead, the court reiterated *Morrison*'s emphasis that the Exchange Act is focused on "*purchases and sales*" of securities in the United States, which demonstrates a concern with the location of the securities transaction and not with the location of the exchange. *Id*. (emphasis in original). In supporting its reasoning, the court pointed out that the Supreme Court's analysis in *Morrison* was not affected by the fact that the *Morrison* defendant's American Depository Receipts (ADRs)—which represented the right to receive a specified number of its ordinary shares—had been listed on the NYSE. *Id*. at 13. Further, the court recognized *Morrison*'s rejection of the Second Circuit's "conduct and effects" test, pursuant to which the Circuit had previously applied the Exchange Act to "transactions regarding stocks traded in the United States which are effected outside the United States." *Id*. at 13-14. The court therefore found that *Morrison*'s bar is not lifted simply because the shares at issue are also listed on a domestic exchange.

"Foreign Squared" Claims — The Mere Placement Of A "Buy Order" Does Not Establish "Irrevocable Liability"

In contrast to "foreign cubed" claims, "foreign squared" claims involve claims asserted by domestic investors who purchased securities of foreign issuers on foreign exchanges. In another issue of first impression, the Second Circuit addressed whether the placement of a buy order in the United States for the purchase of foreign securities on a foreign exchange is sufficient to allege that the purchaser incurred "irrevocable liability" in the United States, such that the purchase is governed by US securities laws. Op. at 15. The Section 10(b) claims at issue were asserted by the Oregon Public Employees Board ("OPEB"), a domestic entity that purchased UBS shares by placing a "buy order" in the United States. Although this order was later executed on a Swiss Exchange, OPEB asserted that the placement of its order in the United States was sufficient to satisfy *Morrison*'s second prong as a "purchase[] . . . of securities in the United States." *Id*. at 14.

In dismissing OPEB's Section 10(b) claims, the Second Circuit relied on its decision in *Absolute Activist Value Master Fund Ltd. v. Ficeto*, 677 F.3d 60 (2d Cir. 2012), to conclude that the mere placement of a buy order in the United States is too tenuous a connection to confer US securities laws jurisdiction over those securities. Op. at 15. *Absolute Activist* defined a domestic securities transaction for purposes of *Morrison* as one where "the parties incur irrevocable liability to carry out the transaction within the United States or when title is passed within the United States." *Absolute Activist*, 677 F.3d at 69. The Second Circuit rejected OPEB's argument that, when the purchaser is a domestic entity, "irrevocable

liability" is incurred in the United States where the order is placed and not when the security is actually purchased on a foreign exchange. Op. at 15-16. In so doing, the Circuit pointed to its own prior holdings that a purchaser's citizenship or residency does not affect where a transaction occurs. *Id*.

Looking Forward

City of Pontiac, while not addressing *Morrison*'s application to Securities Act claims, presents a major victory for foreign issuers facing potential Exchange Act claims involving cross-listing on US exchanges, as the decision's holistic approach to *Morrison* appears to definitely dispose of the "listing theory"—at least in the Second Circuit. Following this decision, the fact that a foreign issuer might cross-list a foreign security on a US exchange should not affect the limitations imposed by *Morrison* on Exchange Act claims. Similarly, the Second Circuit appears to have made clear that merely placing a buy order in the United States is not sufficient to make the purchase a "domestic transaction" for purposes of *Morrison*'s second prong, although the opinion leaves open the question of what more could be pleaded to sufficiently state a Section 10(b) claim. While these *Morrison* issues have yet to be addressed by other circuit courts, the Second Circuit's decision offers persuasive precedent.

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