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## *Multinational Litigation*

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### **Belgian Accounting Firm Enjoined From Pursuing Action In Brussels To Halt United States Securities Fraud Action**

*By Michael J. Holland*

In *Quaak v. Klynveld Peat Marwick Goerdeler Bedrijfsrevisoren*, 361 F.3d 11 (1<sup>st</sup> Cir. 2004), the First Circuit Court of Appeals was faced with an issue on which the United States Supreme Court has been silent: When, in order to preserve its jurisdiction, should a United States Court enter an order enjoining a party from seeking relief in a foreign country? For those who want a quick answer, here it is: When the entry of such an order is necessary to preserve the United States Court's ability to do justice between the parties in cases that are legitimately before it.

How the First Circuit arrived at that decision, the twists and turns in the litigation, and the litigation chess match between the competing parties makes an interesting read for those involved in disputes among parties which spill across national and even continental borders.

The *Quaak* case arose out of the failure of Lernout & Haaspié ("L & H"), a Belgian corporation that developed and licensed speech technologies, including speech recognition software. Prior to its precipitous decline into bankruptcy in November of 2000, L & H was touted by some as the "Microsoft of Europe" and was listed on the NASDAQ Stock Exchange. The bankruptcy filing led to the predictable blizzard of shareholders' suits claiming that L & H had made false and misleading statements concerning its earnings, filed false documents with the SEC and engaged in deceptive accounting practices. L & H maintained its U.S. executive offices in Burlington, Massachusetts. L & H also had a subsidiary in Korea. The defendants snared in the net of the fallout from the L & H

bankruptcy included Klynveld Peat Marwick Goerdeler Bedrijfsrevisoren, (KPMG-B) a Belgian company that served as the auditor for L & H.

KPMG-B did not dispute that it was subject to personal jurisdiction in the District Court in Massachusetts, where it was a principal defendant in the securities fraud litigation. KPMG-B was also the target of a criminal investigation in Belgium arising out of the L & H debacle. The District Court found that the consolidated complaint brought by the plaintiffs in the securities fraud litigation satisfied the stringent pleading requirements in the Private Securities Litigation Reform Act of 1995 (PSLRA).

Having successfully negotiated these threshold hurdles of personal jurisdiction and pleading requirements, the securities fraud plaintiffs embarked on pretrial discovery, serving document requests for KPMG-B's work papers. KPMG-B objected, asserting that Belgian law prohibited it from divulging those documents. The securities fraud plaintiffs became civil co-prosecutors in the ongoing Belgian criminal investigation. By virtue of their status as civil co-prosecutors in the on-going criminal investigation, plaintiffs were able to view, but not copy, the documents they sought production of in the United States.

Their appetite whetted by the documents that they had seen but not copied, the securities fraud plaintiffs moved in the District Court to compel KPMG-B to turn over its work papers. The magistrate judge rejected KPMG-B's Belgian secrecy law argument and ordered production of the requested documents.

Four days before the deadline for production, KPMG-B filed an *ex parte* application in Brussels (probably not coincidentally, the filing was made on Thanksgiving Day in the United States) seeking to enjoin the securities fraud plaintiffs from

taking any steps to proceed with the requested discovery. KPMG-B also asked the Belgian court to impose a daily fine of 1,000,000 Euros for each violation of the proposed injunction of which they sought issuance. The Belgian court, while not acting on the *ex parte* application, directed that notice be given to the securities fraud plaintiffs and set a hearing in Brussels for December 16, 2003.

The next move in this international chess game was up to the securities fraud plaintiffs who promptly moved before the magistrate judge for an antisuit injunction which, when issued two days later, enjoined KPMG-B from proceeding with its Belgian action, ordered KPMG-B to withdraw the action, and ordered KPMG-B not to proceed with the scheduled hearing on December 16, 2003. The magistrate judge also denied KPMG-B's motion to stay the turnover order on the work papers. KPMG-B immediately appealed to the First Circuit Court of Appeals.

The First Circuit started its discussion by noting that "no aspect of the extension of the American legal system beyond the territorial frontier of the United States has given rise to so much friction as the requests for documents in investigation and litigation in the United States". *Quaak*, 361 F.3d at 13, citing Restatement (Third) of Foreign Relations Law of the United States § 442m Reporters' note 1 (1987).

The First Circuit began its analysis by articulating the basic principles: 1) Federal Courts have the power to enjoin those parties subject to their personal jurisdiction from pursuing litigation before foreign tribunals; 2) Parallel proceedings on the same *in personam* claim should generally be allowed to proceed simultaneously; and 3) There is a presumption in favor of concurrent jurisdiction.

While those basic principles have been consistently applied, the Courts of Appeals have differed as to their application of those principles in determining whether to enjoin an international

proceeding.

What has emerged from the decisions are two views: a “liberal approach,” which holds that an international antisuit injunction is appropriate whenever there is a duplication of parties and issues and the Court determines that the prosecution of simultaneous proceedings would frustrate the speedy and efficient determination of the case, and the “conservative approach” which holds that an antisuit injunction should be granted only when the foreign action either imperils the jurisdiction of the U.S. Court or threatens some strong national U.S. policy. The “conservative approach” accords greater weight to considerations of international comity, i.e., it is less restrictive on the jurisdiction of the foreign sovereign’s courts.

The First Circuit rejected the “liberal approach” which had been adhered to by the Fifth, Seventh, and Ninth Court of Appeals. Four Courts of Appeals (the Second, Third, Sixth, and District of Columbia Circuits) have espoused the “conservative approach” in determining whether to grant international antisuit injunctions.

In rejecting the “liberal approach,” the First Circuit said that approach gave “far too easy passage to international antisuit injunctions.” The First Circuit in *Quaak* favored the “conservative approach” since that approach recognizes the rebuttable presumption against issuing international antisuit injunctions. The “conservative approach” is more respectful of principles of international comity, and it compelled a Court to balance competing policy considerations when considering whether to grant an antisuit injunction. Issuing an international antisuit injunction suit “is a step that should be taken only with care and great restraint.” *Quaak*, 361 F.3d at 18.

The First Circuit did not uncritically accept the “conservative approach” and instead provided the following guidance for District Courts within the First Circuit in spelling out the

approach that would be taken by the First Circuit in reviewing a decision granting or denying an antisuit injunction. The guidelines are as follows:

1. Both suits must involve the same parties and issues. If that condition is not met, no injunction should be granted.
2. Given considerations of international comity, there is a rebuttable presumption against the issuance of an order that has the effect of halting foreign judicial proceedings.
3. The District Court should examine the totality of the circumstance in deciding whether a particular case warrants the issuance of an international antisuit injunction.

An analysis of the totality of the circumstances includes the nature of the two actions, the posture of proceedings in the two countries, the good faith or lack thereof in the parties’ conduct, the importance of the public policies at stake in the litigation and the extent to which the foreign action has the potential to undermine the United States Courts’ ability to reach a speedy and just result.

Against this articulated standard, the First Circuit in *Quaak* held that the District Court had acted correctly in enjoining KPMG-B from pursuing the Belgian litigation. The Court viewed KPMG-B’s attempt to impose a 1,000,000 Euro per violation sanction on the securities fraud plaintiffs (should they take any steps to enforce the District Court’s order requiring the turnover of the KPMG-B work documents) to be a chilling “*in terrorem*” tactic which was an effort to effectively strip the District Court of any power in the case. Finding that KPMG-B had instituted the Belgian action “in a blatant attempt to evade the rightful authority of the forum court.” *Quaak*, 361 F.3d at 20, the need for an antisuit injunction was

clear. The granting of the antisuit injunction was necessary to preserve the District Court's ability to do justice between the parties in cases that were legitimately before it.

The Court also found that the equities weighed in favor of affirming the District Court's order. The securities fraud plaintiffs were not engaged in some "fishing expedition;" rather, they had already been nominated as civil co-prosecutors in the on-going Belgian criminal investigation and had already seen the documents of which they now sought production. Accordingly, said the Court, the securities fraud plaintiffs were not "fishing in an empty stream." *Id.*

The *Quaak* Court suggested that KPMG-B would have been better off exhausting other options prior to filing the Belgian action attempting to enjoin the securities fraud plaintiffs from proceeding in the U.S. forum. KPMG-B could have appealed the Magistrate's order requiring the turnover of documents, or it could have sought clarification from the Belgian Courts as to whether the turnover of the documents would violate Belgian law. Having eschewed those options and having commenced an action that precipitated a direct conflict with the pending securities fraud action in the District Court in Massachusetts, KPMG-B was required to "pay the piper." *Quaak*, 361 F.3d at 21.

While not minimizing the potential difficulty of the situation in which KPMG-B found itself, the Court found that KPMG-B's election to maintain a major presence in the United States required the corporation to anticipate that it would be subject to suit in the United States and to the discovery rules of the United States judicial system. While the First Circuit emphasized that the District Court should take care to demonstrate due respect for any special problem confronted by a foreign litigant on account of its nationality, any foreign national that chooses to engage in business in the United States must demonstrate its respect for the operation of the American judicial system.

The *Quaak* case illustrates the difficulties that foreign corporations have in complying with the laws of their own countries as well as with the laws of the United States. The *Quaak* Court imposes a common sense approach for evaluating these legal problems but indicates that when a foreign action is commenced solely to thwart the jurisdiction of the United States Courts, the United States Courts are likely to grant an antisuit injunction prohibiting a party properly before it from going into the Courts of a foreign jurisdiction in an attempt to foreclose the progress of the United States lawsuit.