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COVER STORY

Securities litigators find opportunities with China

By Eli Wolfe / Daily Journal Staff Writer

Two recent, back-to-back victories for Skadden, Arps, Slate, Meagher & Flom LLP and Affiliates have highlighted the unique market potential in securities litigation defense work for Chinese-based issuers.

The firm successfully dismissed two securities class action suits brought against Chinese clients — ChinaCache International Holdings Ltd. and Jumei International Holding Ltd. — on Jan. 9 and 10. Peter B. Morrison, a Los Angeles-based Skadden partner who defended ChinaCache against a claim of making misleading statements to the market, noted that the firm has built a strong presence in Asia to handle these kinds of securities cases. He said it's been "highly successful over the years."

Bradly A. Klein, a Hong Kong-based Skadden partner who defended ChinaCache and Jumei, said that he's represented Asia-based clients in at least 14 securities cases since moving to China several years ago. There has been a general increase in securities class action filings against foreign companies in recent years, he noted.

But there is an especially strong demand among Chinese-based issuers for securities defense work, according to several attorneys who have specialized in this niche field.

"The Chinese economy is the second largest in the world now and Chinese companies are expanding," said William K. Pao, a partner at O'Melveny & Myers LLP. "A lot of them are coming to the U.S. primarily because of the prestige of listing in the U.S. and the access to the capital here, and, in addition to that, it may actually be more difficult for them to list in China."

Pao said that there was a rash of securities class action litigation against Chinese-based issuers starting around late 2010 and 2011, when the Securities and Exchange Commission raised the listing standards for reverse merger companies. Prior to this, reverse mergers had been a relatively easy way for Chinese companies to get listed on the U.S. stock exchange.



Juliane Backmann / Special to the Daily Journal

Peter B. Morrison, a Los Angeles-based partner at Skadden, Arps, Slate, Meagher & Flom LLP and Affiliates, is one of a growing number of attorneys who've found success in defending Chinese clients in securities cases.

Chinese-based issuers are now more familiar with the SEC's rigorous reporting standards, but Pao said there are still a large number of securities cases affecting issuers because China's economy is still growing, which means more companies are trying to enter foreign markets, including the U.S.

China-based issuers today face fewer meritless attacks by plaintiffs eager to short their stock, thanks to changes in the requirements for bringing securities cases to court, according to David M. Furbush, a partner with Pillsbury Winthrop Shaw Pittman LLP.

"I'm seeing fewer cases because I think the plaintiffs' bar has realized the challenges of bringing these cases," Furbush said. "They can't just file a suit based on suspicion [anymore]."

At the same time, there is no shortage of demand for defense work in legitimate securities cases. Scott D. Musoff, a partner with Skadden, said that with the increase in securities filings over the past two years, public companies are increasingly the target of litigation. He added that in the future there will likely continue to be many investigations related to the Foreign corrupt Practices Act and cases brought against technology and life sciences companies, which by

their nature tend to be more volatile in the market. He added that the new presidential administration could also potentially affect litigation.

"We'll be watching the new administration's actions in terms of trade with China and Asia in general, and the impact that could have on certain China-based companies that are public in the U.S.," Musoff said.

Attorneys are also paying close attention to economic and regulatory changes going on in China. According to Skadden's Klein, there has been more enforcement by Chinese authorities against local and multinational companies in the anti-corruption space. Thomas M. Shoesmith, a partner at Pillsbury, observed that some Chinese-based issuers are discovering that they can get better valuation for their companies in their own country, where capital is far more accessible than it was even several years ago.

"For companies whose principal focus is China, the Chinese domestic markets are pretty attractive," Shoesmith said. "In fact, we're seeing a fair amount of activity in Chinese companies or private equity firms acquiring assets in the U.S. with the intent of listing them on the Chinese markets, which is the inverse of what

was happening five years ago."

Attorneys speculated that this trend has also been propelled by the significant decrease in IPOs by dollars and volume in the U.S. over the past year, which, combined with intense scrutiny and litigation, has persuaded some companies to try their chances at home.

"I think it's true that Chinese companies are revisiting the issue of whether they should list in China, and thinking long and hard about that before they list in the U.S.," Pao said.

A relatively small group of U.S. firms are well-positioned to defend Chinese-based issuers facing securities litigation, Pao said. That requires a combination of expertise in securities, boots on the ground in China, and a deep understanding of Chinese companies.

Klein commented that many kinds of client interaction, including the development of the factual aspects of the cases and document preservation, are made more convenient by having Mandarin-fluent litigators in China to work with clients in person. He also noted that it's necessary to explain basic concepts of a class action to some Chinese clients who are under the impression that they're being sued by a particular person, versus a class of shareholders.

Peter Morrison said that the inverse can also be true, requiring attorneys to explain the reasoning behind common Chinese laws and customs.

"Sometimes it even runs the other way: You're dealing with a complex corporate structure that's undertaken for completely legitimate reasons based on Chinese restrictions and Chinese laws, and you have to explain that to a U.S. audience that is not necessarily familiar with those arrangements and structures," said Morrison.

Having an experienced securities attorney in China to meet with clients has been a critical component in developing business, Musoff said.

"It's a huge value-add to have Brad [Klein] on the ground to help clients who aren't used to U.S. or class action litigation navigate the process," he said.