

## Second Circuit: Vacates Class Action Dismissal Concluding That the District Court Misinterpreted the Scope of a Forum Selection Clause and Attributed Undue Weight to a Foreign Country's Interest (Securities Law Alert)

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On August 26, 2022, the Second Circuit vacated and remanded a district court's dismissal of a lawsuit, on the ground of forum non conveniens, challenging a going-private merger involving the defendant e-commerce company and the purchase of its outstanding publicly-traded American Depositary Shares ("ADSs") by the company's controlling shareholders. *Fasano v. Guoqing Li*, 47 F.4th 91 (2d Cir. 2022) (Kearse, J.). The Second Circuit held that the district court gave the forum selection clause<sup>[1]</sup> at issue an unwarrantedly narrow interpretation causing it to undercount the defendants who should be covered by it and that the district court erred in weighing the public interest factors.

### Background and Procedural History

The company, incorporated in the Cayman Islands, became publicly traded in 2010 with its shares trading as ADSs on the NYSE, covered by a deposit agreement containing a forum selection clause requiring arbitration of certain disputes. In 2015, the company's CEO/founder led a group of allegedly controlling shareholders<sup>[2]</sup> that proposed a going-private merger by offering to buy out the company's minority shareholders. The going-private merger closed in 2016. Subsequently, plaintiff former owners or holders of the company's ADSs commenced a putative class action against the company and its controlling shareholders challenging the merger and alleging negligent misrepresentation, breach of fiduciary duty, and federal securities claims under Sections 10(b), 13(e), and 20(a) of the Exchange Act. The Southern District of New York determined that the forum selection clause only applied to the claims "relating to or based upon" federal securities law—not the negligent misrepresentation and breach of fiduciary duty claims—and that only the company was a signatory to the deposit agreement, therefore, many of the codefendants were not subject to the forum selection clause. The district court further held that the public interest factors favored dismissal on the ground of forum non conveniens because the forum selection clause was applicable to only half of plaintiffs' claims and to only five of the 13 named defendants.

### It Was Reasonably Foreseeable That the "Buyer Group" Would Be Bound by the Forum Selection Clause

On appeal, the Second Circuit concluded that the district court erred: (i) by giving the forum selection clause an unwarrantedly narrow

interpretation, thereby undercounting the non-signatory defendants who should be covered by the forum selection clause; and (ii) in weighing the public interest factors.

As to the district court’s conclusion that certain defendants could not have foreseen being bound by the forum selection clause, the court stated that the lower court’s “unduly narrow” focus on the issuance of the company’s ADSs (rather than the ADSs themselves or their alleged confiscation) “infected its conclusion as to what parties the Forum Selection Clause covers.” Weighing defendants’ connection to the subject matter of the action, and the propriety of finding the forum selection clause was applicable to them, the Second Circuit found it persuasive that these defendants were in the buyer group that caused plaintiffs’ ADSs to be eliminated and that the proxy statement repeatedly stated that they would be subject to the deposit agreement’s terms and conditions. The court concluded that “it was reasonably foreseeable to any member of the ‘Buyer Group’ that they would be subject to the underlying deposit agreement, and therefore its Forum Selection Clause.”

**The Public Interest Factors Did Not Justify a Forum-Non-Conveniens Dismissal**

The Second Circuit also concluded that the public interest factors could not justify a forum-non-conveniens dismissal. As to the district court’s conclusion that dismissal was warranted because only half of plaintiffs’ claims were covered by the forum selection clause, the Second Circuit indicated that it appeared that the district court was seeking to avoid bifurcation of the case. However, the Second Circuit stated that it was not possible to avoidance bifurcation if plaintiffs insisted on their rights under the deposit agreement to have their federal securities claims litigated in court because the deposit agreement required all of their other claims to be submitted to arbitration.

**Cayman Islands Has No Genuine Interest In Adjudicating U.S. Federal Securities Claims**

The Second Circuit also concluded that while plaintiffs’ common-law claims were likely governed by Cayman Islands law because the company was incorporated there, a forum-non-conveniens dismissal could not serve the Cayman Islands’ interest in having those claims “decided at home” because the deposit agreement required those claims to be submitted to arbitration in New York. The court reasoned that because plaintiffs’ common-law claims could only be pursued in a New York arbitration, if the forum-non-conveniens dismissal stood then the only claims to be determined in the Cayman Islands would be the federal securities claims. The Second Circuit stated that it could not see any genuine interest of the Cayman Islands in adjudicating such claims, in contrast to the U.S., which the court stated has a vital interest in having its own courts decide an unsettled securities law question (namely, whether Section 13(e) implies a private right of action).

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[1] The forum selection clause provides, in relevant part, “Any controversy, claim or cause of action brought by any party hereto against the Company arising out of or relating to the Shares or other Deposited Securities, the American Depositary Shares, the Receipts or the Deposit Agreement, or the breach thereof shall be settled by arbitration . . . however, that any such controversy, claim or cause of action relating to or based upon the provisions of the Federal securities laws of the United States . . . shall be submitted to arbitration if, but only if, so elected by the claimant.”

[2] Aside from the company’s CEO/founder, this group included certain officers or directors of the company, its parent company, and three British Virgin Island entities that were controlled by the CEO/founder.

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