Prospectus Regulation and Prospectus Liability

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Prospectus Liability

Competent Courts of Jurisdiction and Applicable Law

*Matteo Gargantini**

I. Why do Jurisdiction and Applicable Law Matter? An Introduction

This chapter addresses the European legal framework for cross-border disputes arising from alleged violations of prospectus rules. It deals with the identification of both jurisdiction and applicable law in cases where litigation involves transnational elements, so that a conflict may arise about who is the judge having jurisdiction and what law is this judge bound to apply.[1] Crucial in both respects are, in the first place, the connecting factors to which EU law refers (see sections II 'The Default Jurisdictional Regime for Prospectus Liability', para. 19.10 and III 'The Default Regime on Applicable Law for Prospectus Liability', para. 19.30) and, in the second place, the rules concerning issuers' and investors' ability to deviate from such rules (see section V 'Deviating from Default Rules: The Issuer Choice Regime', para. 19.50). The importance of these rules can hardly be overestimated. Obviously, not all courts are equal, and neither are national laws. **19.01**

* The author wishes to thank Tomas Arons and Burkhard Hess. All errors remain the sole responsibility of the author.

[1] The two may not coincide, of course, so that judges may have to apply foreign laws. See e.g. Andrew Scott, 'The Scope of Non-Contractual Obligations', in: John Ahern and William Binchy (eds), *The Rome II Regulation on the Law Applicable to Non-Contractual Obligations* (Leiden: Brill–Nijhoff, 2009), 63 (jurisdictional issues and choice-of-law issues have no necessary connection; cases where the European Court of Justice (ECJ) has expressed preference for a coincidence of jurisdiction and applicable law are exceptional).

19.02 Let us take jurisdiction first. Certain judicial systems may facilitate specialization, *de jure* or *de facto*, or can ensure a high level of predictability, especially when courts may rely on a sufficiently broad and consistent case law. Other judicial systems may lack one or the other feature, or both, thus increasing the costs of the uncertainty that surrounds disputes. This equally applies to the notorious fact that some jurisdictions are quicker than others in reaching *res judicata*. Not only does judicial inefficiency inflate litigation costs in some countries, but it also increases the risk of strategic exploitation by litigants that have an interest in postponing the outcome of the dispute—typically the prospective defendants.

19.03 For instance, a well-known litigation strategy by prospective defendants consists in filing a request for negative declaratory relief, thus assuming the formal role of plaintiffs. This action—sometimes referred to as 'torpedo'—is normally brought before a convenient court, such as the one at the plaintiff's domicile, or in a jurisdiction that has notoriously lengthy proceedings. This technique exploits the strict priority principle of the *lis pendens* rule of Article 29, Regulation (EU) 1215/2012 (Brussels I-*bis*), which requires the court where the subsequent affirmative action is filed to stay its proceeding. By filing this kind of action, the potential defendant can either try to establish jurisdiction in the desired forum, especially when the location of jurisdiction is not clear-cut,[2] or delay the potential plaintiff's action for the large amount of time the seized court needs to decline jurisdiction.[3]

19.04 In the field of prospectus liability, this strategy may also rely on the European Court of Justice (ECJ) case law, which facilitates it to some extent. First, the effectiveness of a torpedo action crucially depends on the extent to which two different actions may be regarded as overlapping, so that the second proceeding is stayed. To avoid conflicting judgments (Art. 45(1)(c), Brussels I-*bis* Regulation), the ECJ applies an autonomous and broad interpretation of the 'same cause of action',[4] which is deemed to exist whenever the central issue in the two proceedings is the same. As a consequence, pendency is deemed to occur if the claim for specific performance, on the one side, and the contrasting negative action for a declaratory judgment, on the other, are in opposition to each other.[5] The role of the parties as claimant or defendant in the proceedings is irrelevant in this respect. The fact that a plaintiff in one proceeding is the defendant in the

[2] The stratagem is far from exceptional in practice. For instance, it was used in the Porsche SE/Volkswagen dispute. By lodging a negative declaratory action in Stuttgart, Porsche pre-empted a parallel claim by investors in London. The UK court suspended as per (now) Article 29, Brussels I-*bis* Regulation, and later on dismissed the trial as soon as the court in Stuttgart retained jurisdiction. Thomas Möllers, 'The Takeover Battle Volkswagen/Porsche: The Piëch-Porsche Clan-Family Acquires a Majority Holding in Volkswagen', *Capital Markets Law Journal* (2015) 10, 410, 427.

[3] A frequent form of this second version of the strategy is the so-called 'Italian torpedo', due to the sadly proverbial slowness of some Italian courts.

[4] *Gubisch*, ECJ, C-144/86, 8 December 1987, paras 11, 16, 18–19; *Tatry*, C-406/92, 6 December 1984, paras 45, 48; *Gasser*, C-116/02, 9 December 2003, paras 41–2; *Folien Fischer and Fofitec*, C-133/11, 25 October 2012, para. 49; *Nipponkoa Insurance Co.*, C-452/12, 19 December 2013, para. 42.

[5] Negative declarations are also used to prevent collective claims, see *McGraw Hill International (UK) Ltd v Deutsche Apotheker und Arztebank eG* [2014] EWHC 2436. The announcement of bringing (a future) action may trigger an action for a negative declaration against (potential) lead plaintiffs.

other and vice-versa, does not preclude *lis pendens*. Second, the ECJ case law allows bringing actions for a negative declaration before the court of the place where the alleged tort was committed.[6] In the case of prospectus litigation, this will easily be the issuer domicile.

19.05 Identifying the applicable national law is equally crucial, of course. To begin with, different laws can bring along different qualifications of prospectus liability as contractual or tortious. This has broad implications in terms of available remedies, liability standards, and scope of liable persons. But even when the law or the case law of different jurisdictions adopts the same label—for instance, by referring to non-contractual liability—these elements may diverge. As for the remedies, some national regimes on tortious liability allow plaintiffs to claim compensation for the loss they suffered,[7] some others enable rescission (or restitution),[8] and yet other ones allow for both.[9] As for the standard of liability, some jurisdictions deem negligence sufficient, while others require gross negligence.[10] Finally, in spite of the (admittedly limited) harmonization under Article 11, Prospectus Regulation, countries diverge not only on the choice of whether corporate bodies or issuers (or both) should be liable, but also on the extension of their regimes for prospectus liability to other entities, such as underwriters.[11]

19.06 As this brief introduction demonstrates, determining the competent court of jurisdiction and the applicable law is a crucial precondition for legal certainty. Clear and efficient rules on cross-border prospectus disputes may reduce the cost of private enforcement, to the benefit of issuers and investor alike. However, this chapter will show that the legal framework for jurisdiction and applicable law in the context of prospectus liability is rather complex. This depends in part on the highly technical nature of conflict-of-law rules, and in part on the fact that those rules leave room for interpretation when applied to securities offerings. As the drafters of those rules do not seem to have had primary market transactions in mind, the ECJ plays a fundamental role in providing clarifications. However, many questions remain on the proper interpretation of EU law, and even the available answers—however well grounded on the existing rules—do not always deliver a predictable outcome.

19.07 These issues may affect a broad range of securities disputes, and they have different consequences, depending on the disputed matter. With some inevitable simplifications, one can distinguish four different settings, only one of which is addressed here. In the

[6] *Folien Fischer and Fofitec*, C-133/11, 25 October 2012, paras 21 and 52.

[7] This is the case with the UK: Paul Davies, 'Damages Actions by Investors on the Back of Market Disclosure Requirements', in: Danny Busch et al. (eds), *Capital Markets Union in Europe* (Oxford: OUP, 2018), 325–9.

[8] This is the case with Germany; ibid.

[9] This is the case with Italy; ibid.

[10] While the UK and Italy adopt a negligence standard, in Germany plaintiffs normally have to demonstrate gross negligence: ibid.; Martin Gelter, 'Global Securities Litigation and Enforcement', in: Pierre-Henri Conac and Martin Gelter (eds), *Global Securities Litigation and Enforcement* (Cambridge: CUP, 2019), 74–5. See also Eilís Ferran, 'Cross-Border Offers of Securities in the EU: The Standard Life Flotation', *European Company and Financial Law Review* (2007) 4, 461, 476–82.

[11] Both the UK and Italy, for instance, extend liability to underwriters: Davies (n. 7).

first scenario, litigation may concern the allocation of securities' ownership, as is the case when two parties claim incompatible rights on a share, or when they litigate about the existence of a lien on the share or about whether such lien is effective against third parties. These disputes concerning the 'proprietary' aspects of securities normally involve the negotiable character thereof.[12] In a second scenario, litigation may concern the contract whereby a party acquired the relevant securities, and may, for instance, address the validity of such transfer between the two parties of that contract or the voidability of the same contract.[13] In the third setting, the plaintiff may claim that the issuer is not complying with the security's terms and condition, and may file an action to enforce her rights vis-à-vis the issuer.[14] This kind of litigation is particularly relevant in claims arising from frauds, and in particular when these involve debt instruments, because the issuer or the offeror that allegedly provided false or misleading information will have violated the issuance terms and conditions as well.[15] The fourth and last setting is the one where one or more investors claim restitution and damages for an allegedly false or misleading prospectus.[16] In the remainder of the chapter, reference will be made, unless otherwise specified, to this last setting alone.[17]

19.08 In practice, litigation may involve a number of defendants, including the issuer, any other responsible person identified as such in the prospectus, the auditors that audited the financial information, members of banking syndicates, global coordinators, lead managers and, in some countries, financial supervisors that vetted and approved the information (Art. 11(1), Prospectus Regulation; see also e.g. Annex I, section 2, Regulation (EU) 2019/980).[18] However, issuers are most often challenged in this kind of dispute, so we will consider them as the archetypical defendants. Furthermore, the analysis will refer, unless otherwise specified, to individual or multiple claims that do not fall into the scope of collective redress tools (such as class actions and others), as these raise specific problems that cannot be dealt with in this chapter.

[12] It is in this sense that, for instance, Regulation (EC) 593/2008 (**Rome I Regulation**) is made inapplicable to negotiable instruments, 'to the extent that the obligations under such (. . .) negotiable instruments arise out of their negotiable character' (Art. 1(2)(d)). See e.g. Matthias Lehmann, 'Financial Instruments', in: Jurgen Basedow et al. (eds), *Encyclopedia of Private International Law* (Cheltenham: Edward Elgar, 2017), 742.

[13] In this respect, for instance, the Rome I Regulation clarifies that when a contract is concluded on a trading venue, the law governing that contract is the law that governs such trading venue (Art. 4(1)(h)). For an example involving jurisdictional issues see, instead, *Profit SIM*, ECJ, C-366/13, 20 April 2016.

[14] The dispute concerns, in this case, the 'rights and obligations which constitute a financial instrument and rights and obligations constituting the terms and conditions governing the issuance or offer to the public' of a financial instrument (see e.g. Art. 6(4)(d), Rome I Regulation, which excludes applicability of the general consumer regime).

[15] See e.g. *Kolassa*, ECJ, C-375/13, 28 January 2015, where the claim involved both contractual and non-contractual claims.

[16] This is the setting to which Article 11, Prospectus Regulation refers.

[17] For a broader analysis of litigation concerning claims based on securities' terms and conditions (the third setting sketched out in the text), see Matteo Gargantini, 'Jurisdictional Issues in the Circulation and Holding of (Intermediated) Securities: The Advocate General's Opinion in *Kolassa v Barclays*', *Rivista di diritto internazionale private e processuale* (2014) 50, 1095; Matteo Gargantini, 'Capital Markets and the Market for Judicial Decisions: In Search of Consistency', MPILux Working Paper Series (2016).

[18] Supervisors' liability is in any event subject to the law of the home Member State (Art. 20(9), Prospectus Regulation).

The remainder of the chapter is organized as follows. Sections II 'The Default Jurisdictional Regime for Prospectus Liability' (para. 19.10) and III 'The Default Regime on Applicable Law for Prospectus Liability' (para. 19.30) deal with the default regimes for jurisdiction and, respectively, applicable law. Section IV 'Taking Stock of Default Rules: A System in Need of Reform' (para. 19.39) highlights the shortcomings of such regimes, and section V 'Deviating from Default Rules: The Issuer Choice Regime' (para. 19.50) explores to what extent private ordering solutions may address them. Section VI (para. 19.66) concludes. **19.09**

II. The Default Jurisdictional Regime for Prospectus Liability

This section addresses the default jurisdictional regime for matters pertaining to prospectus liability. It first summarizes the applicable legal framework (section II.1 'Cross-Border Prospectus Liability and the Brussels I-*bis* Regime', para. 19.11) and then moves on to analyse the most relevant judicial decisions pertaining to the localization of financial damages (section II.2 'An Overview of the European Court of Justice Case Law', para. 19.18). **19.10**

1. Cross-Border Prospectus Liability and the Brussels I-*bis* Regime

To put the analysis in context, one should first consider that the general connecting factor for establishing international jurisdiction in cross-border disputes on civil and commercial matters is the defendant's domicile (Art. 4 Brussels I-*bis*). **19.11**

In the most typical setting of an alleged prospectus fraud, the issuer will play the role of defendant, shareholders or other investors being the plaintiff instead.[19] The general rule of Article 4 would therefore, as a matter of principle, facilitate some concentration of litigation in a single country,[20] with a partial[21] limitation due to the fact that, for the purposes of Article 4, issuers could alternatively be sued, depending on the plaintiff's choice, in the country where the issuer has either its registered office, or its central administration, or the principal place of business (Art. 63 Brussels I-*bis*). However, the relevant head of jurisdiction in prospectus litigation is rarely the defendant's domicile, because plaintiffs often refer to other criteria. **19.12**

[19] Exceptions are the so-called torpedo actions (para. 19.05 above) and the Dutch system for collective redress (paras 19.48 and 19.49 below).

[20] As opposed to other jurisdictional rules (see e.g. Art. 18 on consumers), Article 4, Brussels I-*bis* refers to the courts of a Member State, rather than to the courts of a specific place, thus apparently leaving to each Member State the identification of the competent court within its territory.

[21] The three connecting factors will often be located in the same Member State, although issuers may decide to have the real seat and the legal seat in different countries when their company law allows it—typically as a consequence of the incorporation doctrine: see e.g. Frank Wooldridge, 'Uberseering: Freedom of Establishment of Companies Affirmed', *European Business Law Review* (2003) 14, 227; Justin Borg-Barthet, *The Governing Law of Companies in EU Law* (Oxford: OUP, 2012), 50.

19.13 The most common legal basis for determining jurisdiction (and applicable law[22]) in cross-border disputes involving issuer prospectus liability is indeed tortious (or non-contractual) liability (Art. 7(2)). This also applies when legal qualifications may diverge under national substantive laws,[23] because tortious liability is normally regarded as the relevant criterion under the autonomous interpretation of Brussels I-*bis*.[24]

19.14 The reasons why prospectus liability qualifies as non-contractual under EU law are manifold.[25] In the first place, this seems to be the most common qualification among EU Member States.[26] Second, it is a widely shared view that the prospectus as such is not addressed to each investor individually, but rather to the market as a whole, so that a fraud would breach the general trust of market participants. To some extent, this approach seems to echo the 'fraud on the market theory', which is grounded on the assumption that misstatements affect investors because they primarily distort pricing mechanisms.[27] Third, while a contractual relationship may occur between issuers and investors on the primary market, this is often not deemed to be the case on the secondary market and—so the argument goes—there is no reason not to treat investors equally in the two cases. While not all these justifications seem equally convincing, it seems indeed reasonable to qualify prospectus liability as tortious under the Brussels I-*bis* Regulation.

19.15 From the plaintiff's perspective, grounding a claim on tortious liability gives the opportunity of bringing action before the courts where the harmful event has occurred.[28] Moving jurisdiction away from the defendant's domicile may in this case, according to the traditional view, facilitate sound administration of justice and the efficacious conduct of proceedings,[29] in particular for the taking of evidence.[30] Under the ECJ case law, the place of the harmful event can be either the place where the wrongful conduct took

[22] See section III 'The Default Regime on Applicable Law for Prospectus Liability' (para. 19.30) below.

[23] See para. 19.05 above. On the effects of the autonomous interpretation of the Brussels I-*bis* Regulation on contractual and non-contractual basis for jurisdiction, see *Tacconi*, ECJ, C-334/2000, 17 September 2002, para. 19 (where a dispute based on contractual liability under national law is qualified as non-contractual under Brussels I-*bis*).

[24] This qualification is quite undisputed. For jurisdictional matters, see e.g. Matthias Lehmann, 'Where Does Economic Loss Occur?', *Journal of Private International Law* (2011) 7, 527, 529 (although referring to secondary market purchases alone); Matthias Lehmann, 'Prospectus Liability and Private International Law—Assessing the Landscape after the CJEU's *Kolassa* Ruling (Case C-375/13)', *Journal of Private International Law* (2016) 12, 318, 325–6 (more broadly) ; Gelter (n. 10), 100.

[25] For a more extensive analysis of the following reasons, see Francisco Garcimartín, 'The Law Applicable to Prospectus Liability in the European Union', *Law and Financial Markets Review* (2011) 5, 449, 451 (referring to applicable law, but with statements that can equally apply to jurisdictional issues).

[26] This seems also justified by the ECJ (autonomous) interpretation of Brussels I-*bis* concerning the violation of the duty to act in good faith during the negotiations: *Tacconi*, ECJ, C-334/00, 17 September 2002, paras 25 ff. Supporting such interpretation, Matthias Lehmann, 'Special Jurisdiction', in: Andrew Dickinson and Eva Lein (eds), *The Brussels I Regulation Recast* (Oxford: OUP, 2015), 146 (also in the light of Art. 12 and Recital (30), Rome II Regulation: see para. 19.36 below); critically Peter Mankowski, 'Art. 5', in: Ulrich Magnus and Peter Mankowski (eds), *Brussels I Regulation* (Munich: Sellier, 2012), 138–9.

[27] e.g. Jonathan Macey and Geoffrey Miller, 'Good Finance, Bad Economics: An Analysis of the Fraud on the Market Theory', *Stanford Law Review* (1990) 42, 1059, 1060.

[28] Article 7(2) refers to the courts 'for the place where the harmful event occurred', thus apparently restricting Member States' discretion on the identification of the competent court within their territories.

[29] *Henkel*, ECJ, C-167/00, 1 October 2002, para. 46; *Coty Germany*, C-360/12, 5 June 2014, para. 47.

[30] *Universal Music*, ECJ, C-12/15, 16 June 2016, para. 27.

place (*Handlungsort*) or, at the choice of the plaintiff, the place where the damage itself occurred (*Erfolgsort*).[31] While the wrongful conduct may easily have occurred in the Member State where the issuer is established,[32] the place of the damage may facilitate the establishment of jurisdiction in the country where the plaintiff has her domicile.[33]

19.16 Unfortunately, these criteria have proven unable to ensure legal certainty. To be sure, the ECJ has conveniently curtailed the possibility that jurisdiction be established in places where only indirect damages are suffered. For this reason, the plaintiff cannot establish jurisdiction at her domicile on the mere basis that this is where her financial assets are concentrated.[34] However, it remains quite unclear, in the light of the EJC case law, where exactly the place of the damage should be located. Plaintiffs have invoked multiple connecting factors in this respect, sometimes combining them in variable fashions. On its turn, the ECJ has progressively clarified its interpretation as long as it dealt with specific requests for a preliminary ruling, but it also inevitably fell short of providing a clear set of criteria that issuers and investors can rely upon in future disputes.

19.17 The most recurring connecting factor in the ECJ case law on disputes involving tortious liability in securities frauds is the investor's account. However, this criterion seldom appears on its own, being often combined with other connecting factors. Furthermore, what is exactly meant by 'investor's account' might also be quite uncertain, in particular as regards the alternative between the securities account where the financial instruments are registered or the bank account where the invested money originates. A brief overview of the most important ECJ decisions will clarify these aspects.

2. An Overview of the European Court of Justice Case Law

19.18 This subsection provides a synthetic overview of ECJ decisions on cross-border disputes concerning securities liability. While not all the cases reported deal with prospectus frauds, they all contribute to clarifying what the connecting factors are for the identification of the place where a financial damage occurred. At the same time, the analysis omits other cases where the claimant invoked prospectus liability, to the extent that such cases did not address issues on the localization of financial damages.

19.19 The leading case of our analysis is *Kronhofer*.[35] This dispute originated from a claim filed with an Austrian court by an Austrian investor against a group of German defendants. The investor sought to recover damages for financial losses he suffered because of his investment in some call options having shares as their underlying asset. In the

[31] *Mines de Potasse d'Alsace*, ECJ, 21-76, 30 November 1976, para. 17.
[32] See e.g. *Kolassa*, ECJ, C-375/13, 28 January 2015, para. 53; Gelter (n. 10), 100.
[33] For this reason, plaintiffs tend to refer to the place where the damage occurred. This is not without exceptions, however: see *Melzer*, ECJ, C-228/11, 16 May 2013, para. 19.
[34] *Marinari*, ECJ, C-364/93, 19 September 1995; see also *Dumez*, C-220/88, 11 January 1990.
[35] *Kronhofer*, ECJ, C-168/02, 10 June 2004.

plaintiff's view, the defendants (all employees of a German investment firm) had failed to warn him of the risks of option trading. To pursue its investments, the investor had opened an 'investment account' with the same German investment firm, while the call options were bought on the London Stock Exchange. In the plaintiff's view, the place where the damage occurred had to be located at his domicile. However, the Austrian courts stayed proceedings and referred a request for a preliminary ruling to the ECJ with a view to ascertaining whether the 'place where the harmful event occurred' also includes the place where the injured party is domiciled, even if the investment was carried out in another Member State.

19.20 The ECJ ruling in *Kronhofer* was consistent with the previous case law, as it deemed insufficient for the plaintiff to refer, to establish jurisdiction at his domicile, to the place where his assets were concentrated. In the Court's view, referring to the plaintiff's domicile would undermine predictability of jurisdiction. Rather, the ECJ considered that Germany was the place where both the event giving rise to the damage and, most importantly, the place where the damage occurred were located.

19.21 While not expressly stating that the 'investment account' was to be regarded as the key connecting factor, the ECJ decision was quite clear in considering this account as the relevant criterion for the identification of the place where the financial damage occurred. What remained unclear, however, was the precise meaning of the expression 'investment account', as this might have referred to either the bank account opened with a view to performing the specific investment on call options (brokerage account)[36] or to the security account where these options were subsequently registered.[37] Furthermore, one could perhaps infer from the Court's reasoning that the investor's bank account where the invested money originally came from was irrelevant, instead, as the investor had apparently opened his investment account in Germany in the vicinity of the disputed investment, with the specific purpose to buy the call options. Not all these doubts have been dispelled by subsequent case law, as the remainder of this subsection demonstrates.

19.22 An important ECJ decision that took up again these questions on the determination of the place where financial damages occur was *Kolassa*. The dispute in *Kolassa* arose out of a financial scam uncovered in Germany in 2009. In 2005, a large British bank allotted through its German branch some certificates—qualified as bearer securities under paragraphs 793 ff. of the German BGB (Civil Code)—to a limited number of institutional investors. These sold the certificates on to the public at large through a base prospectus—which shows the non-equity nature of such securities.[38] The prospectus was approved by the national competent authority in Germany and subsequently

[36] See e.g. Lehmann, 'Where Does Economic Loss Occur?' (n. 24), 545. Apparently, A. G. Opinion, *Melzer*, case C-228-11, 29 November 2012, paras 31–2; Matthias Haentjens and Dorine Verheij, 'Finding Nemo: Locating Financial Losses after *Kolassa/Barclays Bank* and *Profit*', *Journal of International Banking Law and Regulation* (2016) 31, 346, 347.

[37] See e.g. Garcimartín (n. 25), 452–3.

[38] Article 5(4), Directive 2003/71/EC.

published in other countries, including Austria, under the passport regime of Directive 2003/71/EC. A German bank bought some of the certificates and endorsed them in favour of its Austrian subsidiary. In turn, this subsidiary entered into a contract with a retail investor domiciled in Austria, who thereby had the right to receive payments based on the certificates' cash flow. The Austrian subsidiary held the certificates in its own name on a securities account opened in Munich, operating as a trust in favour of the Austrian investor, who had the right to receive the securities' cash flow.

19.23 As the value of the assets underlying the bearer securities plummeted, the Austrian investor filed a lawsuit in Austria against the British bank, claiming damages on the basis of both contractual and tort liability. In this analysis, we will only focus on prospectus liability, which in the plaintiff's view resulted from false information and breach of control obligations. Once again, the plaintiff sought to establish jurisdiction at his own domicile, on the basis that this was the place where the damage had occurred under Article 7(2) Brussels I-*bis*. The ECJ answered that the courts where the plaintiff has his domicile can have jurisdiction only when this is the place where the loss occurred, and 'in particular when that loss occurred itself directly in the applicant's bank account held with a bank established within the area of jurisdiction of those courts'.[39] To strengthen this result, the ECJ also stressed that this interpretation of Article 7(2) Brussels I-*bis* Regulation enables the issuer to foresee in which court it may be sued, because the decision to notify a prospectus in a certain Member State allows such issuer to anticipate the risk of being sued in that Member State by investors that, having incurred a loss, may claim they have not been adequately informed.[40]

19.24 *Kolassa* generically referred to the investor's 'bank accout' when locating financial damages, bit it did not openly address whether this was to be considered as the bank account (in a narrow sense) where the invested money originated from or the account where the purchased securities were registered (a securities account). However, as the ECJ seems to have conceded that Austrian tribunals had jurisdiction, one can assume that the bank account in a narrow sense was the relevant one, as the securities were held in a German securities account while the money paid for consideration was probably transferred out of an Austrian bank account.[41] Unfortunately, *Kolassa* fell short of providing other key answers, and possibly raised new questions that the subsequent case law could only partially address. As opposed to *Kronhofer*, nothing in *Kolassa* hints to the fact that a distinction existed between the generic bank account of the retail investor and a separate brokerage account.[42] Is *Kolassa* then to be regarded as a partial

[39] *Kolassa*, ECJ, C-375/13, 28 January 2015, paras 55 and 57.
[40] ibid., para. 56.
[41] This is far from clear, as some authors suggested, at the time the decision in *Kolassa* was released, that the expression 'bank account' might just be an inaccurate wording for 'securities account': Tomas Arons, 'On Financial Losses, Prospectus, Liability, Jurisdiction (Clauses) and Applicable Law', *Nederlands Internationaal Privaatrecht* (2015) 377, 380; Gargantini, 'Capital Markets' (n. 17); Haentjens and Verheij (n. 36), 352.
[42] In the case of *Kolassa*, the Austrian bank formally held the securities in a trustee-like position in a German securities account on behalf of the retail investor, who only had claims against the Austrian banks and did not formally qualify as the owner of those securities (*Kolassa*, ECJ, C-375/13, 28 January 2015, para. 15). For this reason, no specific brokerage account needed to be opened in Germany.

revirement of *Kronhofer* in this respect, due to its focus on the investor's generic bank account as a basis for jurisdiction? Furthermore, the ECJ itself seemed to consider the bank account alone as a weak legal basis for jurisdiction. Not only did the Court pay some consideration to the claimant's domicile (perhaps due to the way the referring judge framed the question[43]), but it also added the further requirement of the passport notification in the Member State of the investor—this last requirement being, remarkably, the only reason why the head of jurisdiction was deemed predictable. What would then happen if an investor domiciled in a country not included in the offer decided to purchase the relevant securities?

19.25 Shortly after *Kolassa*, another dispute was brought before the ECJ that involved the identification of the place where financial damages occur. In the *Universal Music* case,[44] a Dutch court submitted a request for a preliminary ruling addressing the distinction between the initial (or direct) financial damage and the consequential (or derived) financial damage. In the facts of the case, a Dutch company had committed to purchase a controlling stake in a Czech company, but due to a clerical error by a law firm in the Czech Republic the contract eventually signed reported an inflated price for the Czech company's shares. The buyer and the seller settled the dispute out of court, for a price that fell in between the original price and the price actually appearing in the signed contract. The Dutch company then claimed redress from the Czech lawyers (and apparently the Dutch)[45] on the basis of non-contractual liability, and tried to establish jurisdiction in the Netherlands on the basis that it had suffered a financial damage at its domicile.[46] Although the buyer of the shares brought action only against the law firm, and therefore the dispute involved neither the issuer nor the seller directly, the ruling is based on Article 7(2) Brussels I-*bis* and is therefore important for prospectus liability as well.

19.26 The Court's decision in *Universal Music* is remarkable in many respects. First, the ECJ stressed that the whole series of events leading to the final damage—the precontractual negotiations, the signing of the contract, the subsequent out-of-court settlement—occurred in the Czech Republic. Interestingly enough, some of these events would seem to pertain to the place of the wrongful conduct, rather than to the place where the damage occurred, but the Court seemed to consider them as relevant to assess whether, overall, establishing jurisdiction in the Netherlands might have made the collection of evidence more complex. Second, the ECJ confirms that *Kolassa* made reference to the bank account of the claimant from which the investment was made—as opposed, therefore, to the securities account.

[43] 'Is the wording "the place where the harmful event occurred or may occur" in Article 5(3), Regulation No. 44/2001 to be interpreted as meaning that, when a security is purchased on the basis of deliberately misleading information, the place where the damage occurred is taken to be the domicile of the person suffering the loss, being the place where his assets are concentrated?' (ECJ, *Kolassa*, ECJ, C-375/13, 28 January 2015, para. 19(3)(b)).

[44] *Universal Music*, ECJ, C-12/15, 16 June 2016.

[45] It remains unclear why the applicant did not try to establish jurisdiction in the Netherlands also on the basis of the domicile of codefendants (Art. 8(1), Brussels I-*bis* Regulation).

[46] It was undisputed that the place of the alleged wrongful conduct was the Czech Republic (ibid., para. 29).

However, and most importantly, *Universal Music* pointed out in the third place that, in *Kolassa*, other circumstances (such as the notification of prospectus) contributed to establishing jurisdiction at the claimant's domicile, so that the place of the bank account cannot, on its own, be considered as a relevant connecting factor under Article 7(2) Brussels I-*bis* Regulation.[47] Grounding jurisdiction on the sole basis of the bank account—so the Court's reasoning goes—would make the outcome unpredictable, as claimants could have accounts in different countries with no special connection with the facts of the dispute. As a consequence, the place where the bank account is located plays a role in defining jurisdiction only when accompanied by other concurring circumstances.[48]

19.27 To some extent, the *Universal Music* strengthened what one may define a 'holistic approach' to the identification of jurisdiction in non-contractual matters. Just like in *Kolassa*, but this time more openly, the ECJ considered the relevant facts as a whole, rather than focusing on a single connecting factor, with the aim of establishing jurisdiction in the most convenient forum in the light of the specific circumstances. This approach was later confirmed by the last case we consider in our analysis: *Löber*.

19.28 The dispute in *Löber*[49] originated from the same fraud that triggered the trial in *Kolassa*, and was equally (but this time exclusively) based on prospectus liability. Unsurprisingly, the outcome of the case is also aligned with *Kolassa*, as the ECJ deemed Austria to be the country of jurisdiction. What is relevant, however, is the reasoning of the Court, which stresses once again that the applicant's bank account where the financial losses materialize does not suffice, on its own, to establish jurisdiction. Other factors to be considered include the clearing accounts intended for the execution of the transaction, the place where the secondary market purchase of the securities occurred, the place where the investment contract is signed and—what the ECJ particularly emphasizes for its ability to ensure predictability[50]— the notification of prospectus in the country of the defendant's domicile.[51]

19.29 This is perhaps the most complete list of relevant factors the ECJ has fleshed out, to date, when deciding on the place where purely financial damages occurred under Article 7(2) Brussels I-*bis* Regulation. Remarkably, the ECJ clearly states that these factors should be 'taken as a whole'[52] to determine jurisdiction, which confirms that the approach of the Court is to consider the global features of each specific case, in line with the 'holistic approach' sketched out above.

[47] *Universal Music*, ECJ, C-12/15, 16 June 2016, para. 38.
[48] ibid., para. 39.
[49] *Löber*, ECJ, C-304/17, 12 September 2018.
[50] ibid., para. 35.
[51] ibid., paras 32–3.
[52] ibid., para. 31.

III. The Default Regime on Applicable Law for Prospectus Liability

19.30 Just like under the Brussels I-*bis* legal framework on international jurisdiction, prospectus liability equally qualifies as tortious under the European regime on the determination of applicable law, and is therefore subject to the Rome II Regulation (Regulation (EC) 864/2007), whether the securities have been acquired on the primary or on the secondary market.[53] This qualification is substantially undisputed in the literature and it hinges upon reasons that largely overlap with those recollected in paragraph 19.14 for jurisdiction, with the addition of the policy-oriented argument that labelling prospectus liability as 'contractual' would drag along the regime of the Rome I Regulation (Regulation (EC) 593/2008). This regime is normally deemed to be too permissive for investor protection needs, as it would in principle enable issuers to select the applicable law.[54] Furthermore, even pre-contractual liability falls into the scope of Rome II, which further contributes to reducing the relevance of the Rome I framework (Art. 1(2)(i) Rome I Regulation; Art. 12 Rome II Regulation).[55]

19.31 As opposed to the tortious liability regime in Brussels I-*bis* regulation, which offers the claimant the opportunity of suing the alleged tortfeasor before the court of the place where the wrongful conduct occurred or before the court of the place where the damage occurred, the legal framework on the law applicable to non-contractual obligation relies only on the place where the damage occurred (Art. 4(1) Rome II Regulation).[56]

19.32 While this principle has been applied discontinuously, most scholars agree that Brussels I-*bis* and the Rome I and II Regulation should be interpreted in parallel, so that equivalent statements should be given equivalent meanings in all those statutes (see also, to this effect, Recital (7), Rome II Regulation). As a consequence, the case law summarized in section II.2 'An Overview of the European Court of Justice Case Law' (para. 19.18) above inevitably influences the interpretation of the regime on the applicable law.[57]

19.33 Defining the law applicable to prospectus liability on the basis of the place where the damage occurred, as interpreted under the ECJ case law summarized above, is widely considered a suboptimal outcome. The reason is quite intuitive, as that interpretation determines the applicability of as many national laws[58] as are the places where jurisdiction can be established. However, there is no evident reason why investors should

[53] See e.g. Garcimartín (n. 25), 451. This does not exclude that contractual claims may arise from primary market transactions (such as a request to rescind the purchase agreement: ibid.), but these claims fall out of the scope of this chapter (nn. 13 and 14 above, and accompanying text).

[54] Garcimartín (n. 25).

[55] This is relevant, of course, to the extent that one believes that Article 1(2)(i), Rome I Regulation applies in the absence of individual bargaining, which is far from being a unanimous interpretation: see para. 19.36 below.

[56] To further clarify that the country of the place where the damage occurred has no alternative, the same provision states that that connecting factor applies 'irrespective of the country in which the event giving rise to the damage occurred and irrespective of the country or countries in which the indirect consequences of that event occur'.

[57] Lehmann, 'Prospectus Liability' (n. 24), 336–7.

[58] Note that 'national laws' may include laws of non-EU Member States (Art. 3, Rome II Regulation).

enjoy different levels of protection, when they have all subscribed or purchased securities within the same issuance, nor why issuers should be subject to an equally broad number of divergent regimes.[59] As section II.2 has shown, the ECJ has recently emphasized the importance of prospectus notification in establishing the place of damage, which may partially make the interpretation of conflict-of-law rules more predictable. While this might make some concerns less pressing, the fact remains that making the same issuance subject to different tortious law inevitably increases complexity.

19.34 For this reason, scholars have made various attempt to streamline the identification of the applicable law, and to possibly concentrate the applicable regimes into one, and one only, national law. Remarkably, while the majority of scholars have explored alternative interpretations *de lege lata* or have submitted proposals *de lege ferenda*, no solution has individually emerged as dominant. Out of the many hypotheses that have been tested in the literature, four are worth mentioning here. All of them have their merits and their drawbacks, of course, but what is important to highlight is that they altogether show an overall lack of satisfaction with the current system, combined with the inability to agree on how an ideal system should look like.

19.35 The first alternative interpretation that is meant to determine the applicable law without referring to the place where the damage occurred relies on the so-called 'escape clause' of Article 4(3) Rome II Regulation. Under this rule, when the facts of the case clearly show that the tort is 'manifestly more closely connected' with a country other than that where the damage occurred, then the law of such country should apply. This provision provides potentially valuable room for flexibility, and has been considered by some scholars as the legal basis for various proposals. For instance, some suggest that the applicable law should be the law of the country where the issuer has its registered office.[60] Others recommend applying the law of the place where the relevant market is located.[61] And still others refer to the home country as defined under the rules for prospectus approval.[62] While most scholars consider the escape clause of Rome II Regulation as having a lot of potential to deliver an efficient outcome, the very fact that so many divergent opinions exist as to the applicable law demonstrates how problematic it might be to identify a 'manifest' close connection to a specific country.

19.36 The second alternative that scholars have explored is the qualification of prospectus liability as precontractual liability (*culpa in contrahendo*; Art. 12 Rome II Regulation).[63] This interpretation would lead to determining the applicable law on the basis of the

[59] Lehmann, 'Prospectus Liability' (n. 24), 337.

[60] Wolf-Georg Ringe and Alexander Hellgardt, 'The International Dimension of Issuer Liability—Liability and Choice of Law from a Transatlantic Perspective', *Oxford Journal of Legal Studies* (2011) 23, 31, 33.

[61] Tomas Arons, '"All Roads Lead to Rome": Beware of the Consequences! The Law Applicable to Prospectus Liability Claims under the Rome II Regulation', *Nederlands Internationaal Privaatrecht* (2008) 26, 481, 485.

[62] For a synthesis of these opinions see Lehmann, 'Prospectus Liability' (n. 24), 338–9.

[63] An extensive analysis in Michel Tison and Fran Ravelingien, 'Roma Locuta, Causa Finita? Conflictenrechtelijke Capita Selecta Inzake Bancaire Aansprakelijkheid Na De Rome II-Verordening', in: Johan Erauw and Piet Taelman (eds), *Nieuw Internationaal Privaatrecht: Meer Europees, Meer Globaal* (Mechelen: Kluwer, 2009), 239.

rules for contractual obligations, an outcome that even some authors that are sceptical on its viability deem positive.[64] To some extent, Recital (30), Rome II would seem to support precontractual liability, as this latter is said to include the violation of disclosure duties. However, the majority of scholars believe that reference to 'dealing' in Article 12 Rome II restricts its application to precontractual bargaining, and therefore exclude that such provision may address standardized communications like prospectuses.[65] Furthermore, applicability of Article 12 may be questionable between issuers and secondary market investors, as no contacts occurred between them during the period preceding the publication of the prospectus.[66]

19.37 The third alternative relies on the Rome II regime on 'rules of safety and conduct' (Art. 17). The rule, whose wording may appear obscure at first sight, in practice requires that once a certain law has been deemed applicable on the basis of the place where the damage occurred, account should nonetheless be taken of the rules of conduct that were applicable in the place where the harmful behaviour occurred (Recital (34), Rome II). This provides a remedy to the risk of conflicting requirements between the applicable tortious law and the conduct-of-business regime to which the alleged tortfeasor is subject in its own jurisdiction. However, in the field of prospectus liability, Article 17 is less relevant than it might appear at first sight. First, harmonization of the prospectus regime has reduced the divergences among Member States on the standards of conduct issuers have to comply with when drafting a prospectus. Second, Article 17 does not address the remaining building blocks of tortious liability regimes, such as the burden of proof, the negligence standard, the quantification of damages, and so on. Third, the same provision applies only 'as a matter of fact' and 'in so far as is appropriate', which inevitably makes the court assessment a matter of discretion and consequently reduces legal certainty and predictability.

19.38 Fourth and final, consideration has been given to the possibility that the prospectus regime may pre-empt the Rome II framework according to the principle '*lex specialis derogat legi generali*', which also applies to conflict-of-law rules on non-contractual obligations (Art. 27, Rome II Regulation). This might be the case if the prospectus regime contained its own conflict-of-law rule(s), which some authors identified in (what is now) Article 11(2), Prospectus Regulation. This requires Member States to ensure that their national provisions on civil liability apply to those responsible for the information given in a prospectus. Some authors consider this to be a conflict-of-law rule, which would make civil (tortious) liability subject to the same connecting factors that are applicable to the identification of the home Member State (and the national competent authority) under the Prospectus Regulation (Art. 2(m)). After all—so the argument goes—Article 27, Rome II is meant to safeguard instruments aimed at fostering

[64] Lehmann, 'Prospectus Liability' (n. 24), 338.

[65] ibid.; Ivo Bach, 'Art. 12 Rome II', in: Peter Huber (ed.), *Rome II Regulation* (Munich: Sellier, 2011), 318 (also for further references).

[66] ibid.; Andrew Dickinson, *The Rome II Regulation. The Law Applicable to Non-Contractual Obligations* (Oxford: OUP, 2008).

the 'proper functioning of the internal market' (Recital (35(2)), Rome II), which is precisely the ambition of Prospectus Regulation (Recitals (3) and (4)). As a consequence, the applicable law would be, in a nutshell, that of the Member State of the issuer registered office for non-equity securities whose face value is below EUR 1,000 and for all equity securities, and either the state of the issuer's registered office or the state where admission to trading is sought or where the offer is made—at the choice of the issuer—for the other non-equity securities. While this would allow having one single applicable rule for all the tortious claims, most scholars tend to disagree with this interpretation, mainly because they do not consider Article 11(2), Prospectus Regulation as a conflict-of-law provision.

IV. Taking Stock of Default Rules: A System in Need of Reform

19.39 The brief overview of the ECJ case law on the identification of the place where financial damages occur should have made clear that predicting jurisdiction and applicable law may be a difficult exercise for investors and issuers alike. As the ECJ does not rely on a single connecting factor, gauging the relative weight of the relevant circumstances may easily become a matter of discretional assessment. Take the list of connecting factors in *Löber*, for instance. While these elements offer perhaps the full menu of potential criteria that a court might want to adopt when interpreting Article 7(2), Brussels I-*bis* (and, consequently, Art. 4(1), Rome II), they do not appear to be hierarchically coordinated, so that the question remains what the identification of jurisdiction (and of applicable law, respectively) should look like in case one or more of these factors were missing, or were pointing to a different direction.

19.40 The divergent outcomes in *Kolassa* and *Löber*, on the one hand, and in *Universal Music*, on the other, are a case in point. The cases led to opposite results, as jurisdiction was established at the claimants' domicile in *Kolassa* and *Löber*, and at the defendant's domicile in *Universal Music*. The reasons for this differential treatment can be understood as a consequence of the overall stronger connection of the disputed facts with the investors' domiciles in *Kolassa* and *Löber*, while in *Universal Music* all the relevant activities on the side of both the claimant and the defendant took place in the defendant's country of domicile.

19.41 Overall, these decisions seem to strike a fair balance between the interest of the disputants. For instance, the ECJ recognizes that grounding jurisdiction and applicable law on the sole basis of the investors' bank accounts would not ensure predictability. As a matter of fact, adopting bank accounts as the exclusive connecting factors might disperse jurisdiction and may lead to establishing litigation even in Member States where issuers carried out no activity whatsoever.[67]

[67] See more broadly Gargantini, 'Capital Markets' (n. 17).

19.42 In spite of these attempts to foster predictability, it remains difficult on the basis of the case law to date, to draw a precise dividing line that could shed light on future litigation.[68] To some extent, the plaintiff's conduct in the facts that led to the dispute seems to play a role in the assessment, as a more active behaviour of this party in the defendant's Member State—including wiring money to such Member State[69]—could facilitate the determination of jurisdiction and applicable law at the defendant's domicile. However, the ECJ also attaches great importance to the defendant's conduct, and in particular to the decision to take advantage of the prospectus passport with a view to offering financial instruments in the investors' country. Absent such a notification, one may doubt that the ECJ would determine jurisdiction and applicable law at the defendant's domicile, even if the defendant did not directly transfer money abroad to purchase securities (as in *Kolassa* and *Löber*).

19.43 Furthermore, whether an investment requires a direct transfer of money in the defendant's country of domicile may depend on the technical devices adopted to perform the investment—out of the issuer's control and likely unbeknownst to retail investors like the plaintiffs in *Kolassa* and *Löber*. In these two disputes, for instance, no such direct transfer occurred for the mere reason that in both cases—not coincidentally originating from Austria[70]—the intermediaries located in the investors' Member State were acting in a trustee-like capacity on behalf of their clients. But what if the investors held securities abroad in direct form (as in *Kronhofer*), after having purchased them with the intermediation of national investment firms?

19.44 On the basis of these concerns, one may consider anchoring jurisdiction to the securities account where the investor's securities are registered.[71] This would avoid some drawbacks that arise from the need to 'follow the money' used to pay the securities, but an agreement should first be found on the place where securities accounts should be located. Absent a special regime,[72] this place might be difficult to determine, as securities are usually held in an immobilized or dematerialized form. Normally, such place is considered to be the place where the first intermediary from the point of view of the investor is located, a criterion known as 'place of the relevant intermediary approach' (PRIMA) or, with some slight variations, 'Place of the relevant account approach' (PRACA).[73] However, many uncertainties remain as to whether this criterion can apply across the board, and as to its implications in specific circumstances.

[68] Financial law is not the only area struggling with these issues. See the dispute recently brought before the ECJ on the localization of the place of the harmful event in connection with the German emission scandal: *Verein für Konsumenteninformation*, ECJ, C-343/19, still pending.

[69] See in this sense Johannes Ungerer, 'Pure Financial Loss and International Jurisdiction for Tort under the Brussels I (Recast) Regulation', *Maastricht Journal of European and Comparative Law* (2017) 24, 448, 452.

[70] On the role of the Austrian holding system for foreign securities see Gargantini, 'Jurisdictional Issues' (n. 17).

[71] In favour of establishing jurisdiction on the basis of the place where securities accounts are held, Arons, 'On Financial Losses' (n. 41), 380; Haentjens and Verheij (n. 36), 352; Giorgio Risso, 'Financial Torts and Investor Protection: Is the Europeanisation of Third State Cases a Viable Solution?', *Netherlands International Law Review* (2016) 63, 313, 322. Contra Lehmann, 'Where Does Economic Loss Occur?' (n. 24).

[72] For examples of special regimes, see e.g. Article 9(2), Directive 98/26/EC (on settlement finality) and Article 9(1), Directive 2002/47/EC (on financial collaterals).

[73] Matthias Haentjens, *Harmonisation of Securities Law* (Alphen aan den Rijn: Kluwer Law International 2007) 38–9 and 240; Philip Paech, 'Market Needs as Paradigm—Breaking Up the Thinking on EU Securities

19.45 While the analysis looks quite intricate for jurisdiction, uncertainties are even worse for the identification of the applicable law. On top of the concerns that surround the localization of financial damages, the debate on prospectus liability under Rome II shows that, in this case, there is no agreement even on the proper EU provision that should determine applicable law.

19.46 For both jurisdiction and applicable law, a thorough reflection should be undertaken on the role of the general principle that enables claimants to bring action where the alleged damaged occurred. This principle is usually justified on the basis that it may favour proximity between the judge and the evidence concerning occurrence and magnitude of the damage.[74] However, ascertaining the size of the damage occurring as a consequence of securities' depreciation does not normally require physical proximity, as a certificate by the relevant bank or securities custodian will often suffice.

19.47 Various proposals have been devised to solve these issues. For instance, some authors have suggested adopting as connecting factor the place of the venue where securities are admitted to trade or offered to the public.[75] Most of these proposals are submitted *de lege ferenda* and rely on policy considerations that are inevitably subjective. However, they shed light on another drawback of the current regime: its lack of centralization, which is perceived to be problematic, especially for jurisdiction. Remarkably, this fragmentation is at odds with one of the main reasons why scholars deem prospectus liability as tortious, namely that prospectus frauds affect the market as a whole rather than each investor individually.[76]

19.48 Concentration of litigation is particularly relevant for collective redress, as the former is a precondition for the latter. Whether the Brussels I-*bis* regime is compatible with collective redress is a long-debated topic that cannot be addressed here. However, it is worth mentioning that some attempts have been made, at national level, to foster concentration and attract collective litigation. The most famous example is the Dutch Act on Collective Settlements (WCAM), which provides a particularly attractive mechanism for collective actions.[77] The WCAM relies on an opt-out system for binding settlement agreements approved by the courts. When granting such approval, Dutch judges have adopted a generous approach in retaining jurisdiction, as shown by the prominent *Shell*[78] and *Converium*[79] cases. This case law relies on Articles 4(1) and

Law', in: Pierre-Henri Conac, Ulrich Segna, and Luc Thévenoz (eds), *Intermediated Securities* (Cambridge: CUP, 2013), 36–7.

[74] *Zuid-Chemie*, ECJ, C-189/08, 16 July 2009.

[75] Garcimartín (n. 25), 453; Arons, '"All Roads Lead to Rome"' (n. 61), 486. See also Mankowski (n. 26), 255 (market values may be considered as the primary damage).

[76] See text accompanying n. 27 above.

[77] Ianika Tzankova and Deborah Hensler, 'Collective Settlements in the Netherlands: Some Empirical Observations', in: Christopher Hodges and Astrid Stadler (eds), *Resolving Mass Disputes. ADR and Settlement of Mass Claims* (Cheltenham: Edward Elgar, 2013), 91.

[78] *Shell Petroleum N.V. v Dexia Bank Nederland N.V*, Amsterdam Court of Appeal, 29 May 2009, NJ 2009, 506.

[79] *Scor Holdings AG (f/k/a Converium Holdings AG)*, Amsterdam Court of Appeal, 12 November 2010, NJ 2010/683, LJN: BO3908 and 17 January 2012, LJN: BV1026.20.

8(1), Brussels I-*bis* Regulation, which link jurisdiction to the defendant's domicile and, respectively, allow suing multiple defendants in the courts for the place where any one of them is domiciled whenever separate proceedings may deliver irreconcilable judgments.

19.49 Article 4(1) plays a role in the Dutch system for collective settlements because class members qualify as defendants in a procedure initiated by the (alleged) debtor with the aim of binding all the interested counterparties to give away their rights to initiate an individual claim. Article 8(1), at the same time, ensures that action can be brought in the Netherlands for all the parties, to the extent that at least one among the co-defendants has a Dutch domicile.[80] Hence, those who hold a substantial claim play the defendant's role, while potential debtors take on the plaintiff's position. This system resembles a request for a negative declaratory relief, whose legitimacy—including its ability to switch plaintiff's and defendant's positions—has been recognized by the ECJ.[81] At the same time, this mechanism substantially allows for taking jurisdiction away from consumer's domicile, which is at odds with Articles 17 and 18, Brussels I-*bis* Regulation.[82] On this basis, for instance, the ECJ has denied that assignments of claims from one consumer to another can move jurisdiction from the transferor's to the transferee's domicile.[83]

V. Deviating from Default Rules: The Issuer Choice Regime

19.50 The previous analysis has shown that the EU legal framework for the determination of jurisdiction and applicable law does not always ensure predictability. Nevertheless, issuers and investors might manage these drawbacks if they were allowed to contract out of default rules and devise contractual clauses that best suit them.

19.51 However, no optional regime is in principle available for the determination of the law applicable to tortious liability. The Rome II system only allows to tailor the applicable law regime after the dispute has arisen or where all the parties involved are pursuing a commercial activity, but in this second case the requirement that the agreement be 'freely negotiated' does not seem to fit standardized transactions, as those involving a prospectus (Art. 14, Rome II Regulation).[84] At the same time, restrictions to parties' freedom of choice are one of the reasons why scholars tend to classify prospectus

[80] For an analysis, see Xandra Kramer, 'Securities Collective Action and Private International Law Issues in Dutch WCAM Settlements: Global Aspirations and Regional Boundaries', *Global Business & Development Journal* (2014) 27, 235.

[81] See n. 4 above.

[82] Burkhard Hess, 'Collective Redress and the Jurisdictional Model of the Brussels I Regulation', in: Arnaud Nuyts and Nikitas Hatzimihail (eds), *Cross-Border Class Actions. The European Way* (Munich: Sellier, 2014), 65.

[83] *Schrems II*, ECJ, C-498/16, 25 January 2018, para. 49. The decision follows the Opinion rendered by the Advocate General (14 November 2017, paras 121–3, observing that the Brussels I-*bis* regulation is an insufficient basis for cross-border EU collective actions).

[84] See text accompanying n. 94 below on the necessity to have a genuine consent for jurisdiction agreements.

liability as non-contractual. The remainder of this section therefore concentrates on the regulatory framework for choice-of-court agreements.

1. Jurisdictional Agreements in Securities Litigation

19.52 In Brussels I-*bis*, jurisdiction agreements are a particularly powerful tool. Their effects go beyond contractual relationships, as they involve 'any disputes which have arisen or which may arise in connection with a particular legal relationship' (Art. 25, Brussels I-*bis*)—and for this reason they are also relevant for tortious liability such as that stemming from prospectus frauds.[85] Furthermore, jurisdictional agreements grant priority to the selected court, even in cases where the validity or the scope of the agreement is challenged (Art. 31(2) and (3); Recital (22)),[86] which incidentally reduces the likelihood of torpedo actions that issuers might instrumentally bring before other courts of their own choice.[87]

19.53 However, and perhaps because of these significant effects, jurisdiction agreements are also subject to some stringent limits. First, they face severe limitations when involving consumers (Art. 19, Brussels I-*bis*). Second, even when they are not addressed to consumers, they still require an agreement, subject to special formal requirement, between the parties (Art. 25, Brussels I-*bis*).

19.54 For consumers, prorogation of jurisdiction may deviate from the special protection regime by way of an agreement entered into after the dispute has arisen (Art. 19, Brussels I-*bis*), which makes preventive choice-of-court agreements of little help. For this reason, classifying investors as consumers may have an impact on the effects, towards them, of jurisdiction agreements within a company's charter (if shareholders) or securities terms and conditions (if bondholders or parties to derivative contracts). Whether investors can qualify as consumers under Article 17, Brussels I-*bis* when holding financial instruments outside their trade or profession remains partially an open question. However, with some simplifications, one can conclude, in the light of the scholarly literature and the case law to date, that as a matter of principle shareholders are not consumers,[88] while holders of

[85] Haentjens and Verheij (n. 36), 355.

[86] This regime was introduced in the Brussels I recast as a remedy to the opposite stance taken by the ECJ in its previous case law, which confirmed jurisdiction of the court first seized on the existence of a choice-of-court agreement (*Gasser*, ECJ, C-116/02, 9 December 2003) and excluded anti-suit injunction could interfere with the decision of such court (*Turner*, ECJ, C-159/02, 27 April 2004): see Ilaria Queirolo, 'Prorogation of Jurisdiction in the Proposal for a Recast of the Brussels I Regulation', in: Fausto Pocar et al. (eds), *Recasting Brussels I* (Padua: Cedam, 2012), 191.

[87] See Xandra Kramer and Erlis Themeli, 'The Party Autonomy Paradigm: European and Global Developments on Choice of Forum', in Vesna Lazić and Steven Stuij (eds), *Brussels Ibis Regulation. Changes and Challenges of the Renewed Procedural Scheme* (The Hague/Heidelberg: Asser Press–Springer, 2019), 27. A proper use of jurisdiction agreement could therefore protect investors (including, ironically, consumers). This would depend, of course, on the bargaining power of larger investors on the primary market: Gargantini, 'Capital Markets' (n. 17).

[88] Peter Mülbert, 'Gerichtsstandsklauseln als materielle Satzungsbestandteile', *Zeitschrift für Zivilprozess* (2005), 118, 313, 332; Rainer Hausmann and Ilaria Queirolo, 'Art. 23', in: Thomas Simons, Rainer Hausmann and Ilaria

securities other than shares may qualify as such, as long as they satisfy all the other requirements.[89]

19.55 The question therefore arises whether a contractual relationship exists and the required formalities are satisfied for investors that are not consumers (Art. 25, Brussels I-*bis*). For shareholders, the ECJ case law provides a sufficiently solid ground for jurisdictional agreements. In *Powell Duffryn*, the ECJ qualified company's charters as contracts,[90] and stated that jurisdiction clauses inserted in the company's charter bind shareholders.[91] In the Court's view, when investors decide to become (and, subsequently, to remain) shareholders, they agree to be subject to all the provisions appearing in the statutes of the company (and to their subsequent amendments), which include jurisdictional agreements.

19.56 Things are more complex for bondholders (and in general for those who have invested in securities other than shares) that do not qualify as consumers.[92] As the protective measures for consumers do not apply, these investors may be bound by jurisdiction agreements that predate litigation, but only to the extent that these arise out of an agreement that is either in writing (or evidenced in writing, including in electronic form through a durable medium) or in a form which complies with international trade usages (Art. 25(1)(a) and (c)).[93] The source of complexity lies with the common understanding that these formal requirements are a legal device aimed at ensuring an actual and genuine agreement between the parties.[94] As a consequence, the standard the ECJ has traditionally applied is stricter than—for instance—the standard normally deemed sufficient for establishing jurisdiction in contractual matters (Art. 7(1), Brussels I-*bis*), where an obligation 'freely assumed' by the defendant is normally deemed sufficient.[95] Therefore, limitations may occur either because there is no agreement whatsoever between an issuer and its investors, or because an agreement lacks the required formalities (and might consequently not be genuine).

19.57 In its decision on *Kolassa* summarized in para. 19.22, the ECJ excluded that the Austrian investor had a contractual relationship with the issuer, as the formal bearer of

Queirolo (eds), *Regolamento 'Bruxelles I'* (Munich: IPR Verlag, 2012), 481. Overall, the reason behind this interpretation seems to rely on the residual nature of the claims shareholders are entitled to, and on the powers they enjoy in the company's governance.

[89] See *Kolassa*, ECJ, C-375/13, 28 January 2015, paras 23–4.

[90] *Powell Duffryn*, ECJ, C-214/89, 10 March 1992, paras 16 and 19. See also *Martin Peters*, ECJ, 34/82, 22 March 1983, para. 13.

[91] *Powell Duffryn*, ECJ, C-214/89, 10 March 1992, paras 17 ff.

[92] Note that a prospectus is necessary when the offer is not limited to qualified investors, provided that it is addressed to at least 150 non-qualified investors (Art. 1(4), Prospectus Regulation). As not all retail investors under the Prospectus Regulation are consumers under the Brussels I-*bis* regime (Art. 2(e), Prospectus Regulation, which refers to the MiFID II classification), jurisdiction agreements retain their utility in prospectuses accompanying offerings of securities other than shares. This also applies to listing prospectuses in general.

[93] Less relevant for this analysis is the possibility for the parties to set, by way of a framework contract, the form for future jurisdiction agreements (Art. 25(1)(b), Brussels I-*bis* Regulation).

[94] *Elefanten*, ECJ, C-150/80, 24 June 1981. Hausmann and Queirolo (n. 88), 480–1; Ulrich Magnus, 'Art. 23', in: Magnus and Mankowski (eds) (n. 26), 480.

[95] See e.g. *Kolassa*, ECJ, C-375/13, 28 January 2015, para. 41.

the bonds was indeed the Austrian bank of which the investor was a client. In spite of some uncertainties,[96] the decision is based on the holding technique typically adopted by Austrian banks for foreign securities, which is a sufficient (albeit formalistic) reason to exclude applicability of Article 17, Brussels I-*bis*.[97] While in some countries intermediaries holding securities on behalf of the account holder often operate as mere custodians without any property interest in the registered securities, in other jurisdictions they may have some legal entitlements on securities held on behalf of investors, so that the holding chain creates multi-tiered entitlements on the same financial instruments. This latter is especially the case when the legal regime governing the relationship between custodians (or between the investor and a custodian) follows the rules of trust as inspired by the common law tradition.[98] In this context, while the beneficial owner retains the equitable interest linked to her economic exposure, the custodian at the top of the chain has the formal legal ownership vis-à-vis third parties, including the issuer (indirect holding system[99]). Although the custodian model prevails in continental Europe, the holding-in-trust model may also be adopted in civil law countries on a case-by-case basis, as *Kolassa* shows. For this reason, the ECJ deemed that there was no legal obligation freely consented to by the issuer with respect to the Austrian investor.[100]

19.58 When accountholders qualify as the holders of securities vis-à-vis their issuers (direct holding system), the question remains whether a jurisdictional agreement fulfils the formalities required by Article 25, Brussels I-*bis*. The ECJ has recently tried to clarify this matter in *Profit SIM*, a decision originating from a request for preliminary ruling that concerned, among other matters, whether a choice-of-court agreement included in the terms and conditions of non-equity financial instruments could be binding on investors.[101] In the facts that led to the dispute, a German bank had issued, in the form of notes, credit derivatives linked to underlying bonds issued by an entity incorporated in Luxembourg. An Italian investment firm purchased such credit linked notes through a UK-based investment firm.[102] The terms and conditions of the notes contained a clause stating that the UK court had jurisdiction over every dispute concerning, or arising out

[96] See in particular the Opinion of the Advocate General in *Profit SIM*, ECJ, C-366/13, 20 April 2016, para. 56, that reads *Kolassa* in the sense that a direct contact be needed between issuers and investors for a contract to arise between them, and states that transfers taking place on the secondary market prevent such a direct contact, even when investors do not hold financial instruments in an (intermediated and) indirect form. For a critique, see Gargantini, 'Capital Markets' (n. 17); Donny Surtani, 'Prospectus Liability: Bracing for Parallel Claims in Multiple Jurisdictions', *Butterworths Journal of International Banking and Financial Law* (2015) 30, 284–5. The ECJ did not follow the Opinion (*Profit SIM*, ECJ, C-366/13, 20 April 2016, paras 32–4).

[97] European Commission, 'EU Clearing and Settlement. Legal Certainty Group—Questionnaire. Horizontal Answers', Brussels (2006) 458.

[98] For an analysis of the UK system, see Eva Micheler, *Property in Securities. A Comparative Study* (Cambridge: CUP, 2007), 119.

[99] See in general Philip Paech, 'Market Needs as Paradigm— Breaking Up the Thinking on EU Securities Law', in: Pierre-Henri Conac et al. (eds), *Intermediated Securities* (Cambridge: CUP, 2013) 50–1.

[100] *Kolassa*, ECJ, C-375/13, 28 January 2015, para. 40.

[101] See more broadly Matteo Gargantini and Verity Winship, 'Private Ordering of Shareholder Litigation in the EU and the US', in: Sean Griffith et al. (eds), *Research Handbook on Representative Shareholder Litigation* (Cheltenham: Edward Elgar, 2018), 451–2.

[102] The description of the facts does not clearly determine whether the Italian investment firm was operating as a broker or as a dealer.

of, the notes themselves. Following the default of the Luxembourg-based vehicle, the Italian investment firm challenged before the Milan court the validity of the notes for lack of consideration. The German bank contested that such court had jurisdiction, and invoked the choice-of-court agreement. The seized judge stayed the proceeding and referred a request for a preliminary ruling to the ECJ in order to ascertain whether the requirement that a jurisdiction agreement be in written form (Art. 25(1)(a), Brussels I-*bis*) is satisfied where such an agreement is inserted into an offering document unilaterally created by a bond issuer, so that the prorogation of jurisdiction be made applicable to disputes involving future purchasers. The same court also asked whether, in case this question was answered in the negative, the insertion of a choice-of-court agreement into the offering document can be considered as a form which accords with usages in international trade or commerce under Article 25(1)(c), Brussels I-*bis*.

19.59 To answer these questions, *Profit SIM* distinguishes between primary and secondary market. As for primary market transactions, a jurisdictional clause written in a prospectus is binding on investors (under Art. 25(1)(a), Brussels I-*bis*) if the contract between the issuer and the underwriter 'expressly mentions the acceptance of that clause or contains an express reference to that prospectus'.[103] As for the secondary market, such clause is binding for subsequent buyers if all the three following conditions are met: (i) the clause was valid between the issuer and its counterparty on the primary market (underwriter or first buyer); (ii) the subsequent buyers succeeded to the primary market counterparty's position under the applicable law, thereby acquiring the rights and obligations of that party; (iii) the subsequent buyers had 'the opportunity to acquaint' themselves with the prospectus containing the jurisdiction clause, 'which implies that the prospectus is readily accessible.'[104]

19.60 When one or more of these requirements are missing, jurisdiction agreements retain validity only if they accord with a usage in international trade or commerce (Art. 25(1)(c), Brussels I-*bis*) This is in turn subject to strict requirements, namely that (i) such conduct is regularly followed by market participants for that specific kind of contract; and that either (ii.a) the parties had previously had commercial relations between themselves or with other parties operating in the sector in question, or (ii.b) recourse to jurisdiction agreements is sufficiently well known to be considered an established practice.[105]

2. Remaining Issues in Issuer Choice Regime

19.61 In the light of the intricacies of the choice-of-court legal framework, it comes as no surprise that the current regime is widely deemed as inadequate.[106] To begin with, one

[103] *Profit SIM*, ECJ, C-366/13, 20 April 2016, para. 29.
[104] ibid., paras 36–7.
[105] ibid., paras 48–50.
[106] See e.g. Gargantini, 'Capital Markets' (n. 17); Haentjens and Verheij (n. 36).

may wonder whether the distinction between direct and indirect securities holding systems—which *Kolassa* implicitly relies upon—justifies a different regime for jurisdiction agreements. The technicalities of holding systems are highly dependent on legal qualifications under the applicable law and might therefore cause jurisdiction to be established along different criteria, depending on the national context. Not only does this prevent equal treatment of substantially identical situations, but it also jeopardizes the autonomous interpretation of the Brussels I-*bis* Regulation, together with the need for uniformity it reflects.

19.62 As for the effectiveness of jurisdiction agreements in cases where a contractual relationship can be established, the requirements set out in *Profit SIM* also raise some concerns. The requirement that the clause be valid between the parties on the primary market (i) seems to neglect that syndicates of financial intermediaries often facilitate securities placement by way of firm commitment, which entails underwriting (or buying) securities from the issuer (or the seller) and subsequently reselling them to the investors that have placed their orders on the primary market.[107] These securities are therefore reaching their final purchasers after subsequent resales in the proximity of the primary market transactions, as is the case with retail cascades (Art. 5, Prospectus Regulation). Distinguishing between primary and secondary markets, as *Profit SIM* does, increases the legal risk for investors on the secondary market, as one does not see why bondholders' rights and obligations should depend on the validity of a clause that they are not able to ascertain.

19.63 As for the need that subsequent buyers succeed to the primary market counterparty's position under the applicable law (ii), the ECJ position has the merit of getting rid of interpretations that excluded enforceability of choice-of-courts clauses on the secondary market, but the reference to national laws in order to ascertain whether the initial bondholders' rights and obligations pass on to subsequent buyers may be problematic. In some jurisdictions, rights on securities are originally created when credited on the purchaser's account rather than derived from the previous owner and, even in the same jurisdiction, whether the one or the other form of transfer applies may depend on the circumstances.[108] There is no evident reason, however, not to enforce jurisdiction agreements against new bondholders, whichever is the case. Finally, accessibility of prospectus (iii) is a vague concept, and it might remain under the control of the issuer (Art. 21, Prospectus Regulation).

19.64 One wonders whether these limitations are always justified. Securities are structurally aimed at allowing assignment of legal entitlements with no requirement of further approval by their issuers. As the ECJ puts it in *Tilly Russ* (a case referring to bills of lading), allowing the holder of the bill to remove herself from the compulsory jurisdiction as

[107] Stefano Lombardo, 'The Stabilisation of the Share Price of IPOs in the United States and the European Union', *European Business Organization Law Review* (2007) 8, 526 ff.
[108] European Commission, 'EU Clearing and Settlement' (n. 97), 165–71.

established by the same document would be alien to the purpose of Article 25, Brussels I-*bis*, which is to neutralize jurisdiction clauses that might pass unnoticed in contracts. Therefore, the ECJ correctly states that holders of bills of lading become vested with all the rights and subject to all the obligations mentioned in the document, including those relating to the agreement on jurisdiction.[109] The reason why an identical reasoning should not apply to jurisdiction agreements within securities' terms and conditions is unclear.

19.65 Relying on usages will not help too much either. First, ascertaining whether the form expressing a contractual clause corresponds to a well-established usage may not be easy.[110] Although the ECJ has stated that repeated challenges to the validity of such forms do not necessarily mean a usage is no longer in force,[111] assessing through litigation whether a practice is regularly observed would easily be prone to circularity. Second, market usages are not a reliable source: they do not favour incorporation by reference of jurisdiction agreements in securities[112] and, unsurprisingly, are rarely referred to in international market practices.[113]

VI. Conclusion

19.66 This chapter has analysed the current EU regime for the determination of courts of jurisdiction and applicable law in cross-border disputes concerning prospectus liability. In doing so, it has described the connecting factors EU law and case law refer to when identifying jurisdiction and applicable law in disputes on non-contractual matters involving financial damages, and has highlighted the drawbacks of the current regime. Overall, relying on the place where the damage occurred as an anchor leads to fragmentation of litigation and reduces predictability. The recent ECJ efforts to adopt a more flexible ('holistic') approach have ensured fair results in specific disputes, but have not yet delivered clear guidelines for future cases. The chapter has then considered whether the EU regime on choice of law and jurisdiction may help address some of these drawbacks. While issuers (and investors) can have no choice on the applicable law, jurisdiction agreements offer some room for flexibility. However, the requirements these agreements are made subject to are not meeting issuers' (and investors') needs.

[109] *Tilly Russ*, ECJ, 71/83, 19 June 1984, paras 24 ff.

[110] *Mainschiffharts-Genossenschaft eG (MSG)*, ECJ, C-106/95, 20 February 1997.

[111] *Castelletti*, ECJ, C-159/97, 16 March 1999, para. 29. Remarkably, the case concerned jurisdiction clauses in bills of lading, and the Italian Court of Cassation held, on reconsideration of the case after the ECJ decision, that no international market practice could be invoked because there was no evidence that the parties regarded the relevant jurisdictional clauses as binding (Alexander Layton and Hugh Mercer, *European Civil Practice* (London: Sweet & Maxwell, 2004), 732).

[112] Incorporation by reference is not deemed sufficient for jurisdictional agreements to circulate with bills of lading in international market practices: Hausmann and Queirolo (n. 88), 505–6.

[113] Gilles Cuniberti, 'Three Theories of Lex Mercatoria', *Columbia Journal of Transnational Law* (2014) 52, 101 (modern lex mercatoria hardly meets the needs of international merchants, and empirical evidence shows that these rarely choose its application).