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SOUTHERN DISTRICT CIVIL PRACTICE ROUNDUP

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'Worldcom': Jurisdiction, Case Management in Complex Litigation

THE PROSPECT of being drawn into a complex multidistrict litigation is often daunting for the plaintiff seeking to assert an individual claim. The pace of a multidistrict litigation may be slower than the pace at which the plaintiff could litigate a claim independently, and the plaintiff's attorney will have to surrender considerable control over the direction of the litigation if compelled to coordinate with other plaintiffs' counsel. But for defendants faced with multiple litigations in multiple fora, consolidation into a single litigation under 28 USC §1407(a) offers enormous economies and the chance to coordinate the defense of related cases. Most importantly, consolidation of complex multidistrict litigation promotes judicial economy by vesting authority to control pretrial proceedings in a single judge who can manage the schedule and oversee and resolve discovery disputes and pre-trial motions in a coordinated fashion.

The 'Worldcom' Case

In re Worldcom, Inc. Securities Litigation, a multidistrict proceeding

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pending before Southern District Judge Denise L. Cote, provides a road map of some of the substantive and procedural issues facing parties to potential multidistrict litigation. That litigation grew out of Worldcom's announcement that it would have to restate financial statements for several years as a result of its improper treatment of billions of dollars in ordinary costs as capital expenditures. In addition to criminal, regulatory and congressional investigations, numerous individual and class-action lawsuits were filed in federal and state court, alleging common-law, ERISA (Employee Retirement Income Security Act) and state and federal securities laws violations. In addition to Worldcom, the defendants in those actions include its former executives, directors, underwriters, accountants and financial analysts who issued reports regarding Worldcom. Those cases that were filed in New York were consolidated by order of the district court. Those that were filed in other federal jurisdictions were centralized in

the U.S. District Court for the Southern District of New York by order of the Judicial Panel on Multi-District Litigation, pursuant to 28 USC §1407.

Some plaintiffs went to great lengths to avoid being caught up in the multidistrict litigation. They chose to forgo customary securities fraud claims under the Securities Exchange Act of 1934 as well as class-action claims, which would have had to be filed in, or would be subject to removal to, federal court. Instead, they limited themselves to individual claims under the Securities Act of 1933 (for false statements in connection with Worldcom bond offerings and controlling person liability for various officers and directors) as well as common-law fraud claims. In so doing, they sought to benefit from §22(a) of the 1933 Act, which provides that except for class-action claims, "no case arising under [the 1933 Act] and brought in any State court of competent jurisdiction shall be removed to any court of the United States."¹

The carefully crafted efforts of these plaintiffs to proceed in state court were thwarted, however, by Worldcom's decision to file for bankruptcy. Not only did the automatic stay halt pursuit of claims against Worldcom itself, but the bankruptcy removal statute, 28 USC §1452, provided a new and independent basis for removal to federal court of the claims against the remaining defendants. Judge Cote denied the state court plaintiffs' motions to remand their cases

back to the state courts in which they were filed. She held that their claims fell within the bankruptcy removal statute and that the 1933 Act's limitation on removal must give way to the broader interests of bankruptcy removal jurisdiction.²

Bankruptcy Removal

Section 1452(a) provides that a party may remove any civil claim or cause of action to the federal district court where that action is pending if the district court has jurisdiction over that claim pursuant to §1334. Section 1334 in turn provides that “[n]otwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.” The only exceptions to §1452's bankruptcy-removal provision are for actions before the U.S. Tax Court or those brought by a governmental unit to enforce its police or regulatory power. In contrast to §1441, the general removal statute, any party, including a plaintiff, may remove a case under §1452, and may do so without the consent of any other party.

In removing the state court actions under §1452, the Worldcom defendants did not contend that the claims against them arose under or in the Worldcom bankruptcy. Instead, they asserted that those claims were subject to bankruptcy removal as “related to” that bankruptcy — a claim contested by the plaintiffs on their motion for remand. Judge Cote held that the plaintiffs' claims did qualify as “related to” the bankruptcy, noting, in reliance on *Celotex Corp. v. Edwards*,³ that the comprehensive grant of jurisdiction to the bankruptcy courts requires that “related to” jurisdiction “encompass ‘more than simply proceed-

ings involving the property of the debtor or the estate.’ ” She explained that the dominant standard for “related to” jurisdiction was articulated by the U.S. Court of Appeals for the Third Circuit in *In re Pacor, Inc.*,⁴ which held that a civil proceeding is related to a bankruptcy if “the outcome of that proceeding could conceivably have any effect on the estate being administered in bankruptcy.” Applying that expansive standard to the plaintiffs' claims, she concluded that indemnification and contribution claims that the defendants could potentially assert against Worldcom brought the claims within the “related to” jurisdiction of the court.

Judge Cote observed that substantial authority within and outside of the U.S. Court of Appeals for the Second Circuit supports the finding of “related to” jurisdiction where there is a “reasonable legal basis” for either indemnification or contribution claims. Here, she found that the defendants' statutory rights to contribution from Worldcom under 15 USC §77k(f)(1) (based on joint and several liability), coupled with the fact that any finding of liability against the defendants would be entirely dependent on a finding that Worldcom had engaged in wrongful conduct, provided a reasonable basis for the claims giving rise to the assertion of “related to” jurisdiction.⁵

Conflict With 1933 Act

The plaintiffs opposing federal court jurisdiction also argued that the 1933 Act's express bar on removal of actions filed in state court trumped the federal court's bankruptcy jurisdiction and removal authority. As Southern District Judge Gerald E. Lynch recently noted in *In re Global Crossing, Ltd. Securities Litigation*,⁶ a case raising many of the same issues as the Worldcom litigation, the bankruptcy removal statute and the 1933 Act removal bar are in direct conflict on the specific issue of removal

under bankruptcy jurisdiction of 1933 Act suits filed in state court. He observed that “[e]ach of the statutes states a general rule, and each enumerates one or more exceptions, but neither excepts cases covered by the other's general rule.”

The Worldcom and Global Crossing courts both resolved this conflict in favor of bankruptcy removal. Adopting similar reasoning, they relied first on the fact that §1452(a) supplements the general federal question removal statute by adding specific authorization to remove any action within the bankruptcy jurisdiction subject to only two, explicit and narrow exceptions for tax court actions and those enforcing governmental police or regulatory powers. Under the canon of statutory construction *inclusio unius est exclusio alterius* (the inclusion of one is the exclusion of another), Judge Cote and Judge Lynch both concluded that the absence of an exclusion for securities law claims meant that such claims fell within bankruptcy removal jurisdiction. Both judges also stressed that the bankruptcy statute was enacted much later than the removal limitation in the 1933 Act and that Congress' purpose in enacting §1452 was to broaden, not narrow federal jurisdiction. Both judges concluded that the bankruptcy removal statute took priority over the 1933 Act's deference to the plaintiff's choice of forum and that removal was thus proper.

The Worldcom plaintiffs also sought remand based on various abstention and equitable remand provisions contained in the bankruptcy jurisdiction statute. In certain cases, abstention is mandatory, notwithstanding the existence of federal subject-matter jurisdiction. Section 1334(c)(2) provides that “[u]pon timely motion of a party in a proceeding based upon a State law claim or State law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with

respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a State forum of appropriate jurisdiction." Even where abstention is not mandatory, §1334(c)(1) provides that a court may always abstain from hearing a particular proceeding "in the interest of justice, or in the interest of comity with State courts or respect for State law." In addition, §1452(b) provides that the district court may remand a claim removed pursuant to §1334 "on any equitable ground."

Judge Cote found that remand was unwarranted under any of these provisions. She held that the cases before her did not qualify for mandatory remand because they failed to meet two of the statutory requirements set forth in §1334(c)(2). First, plaintiffs' claims under the 1933 Act could have been brought in federal court without reference to the court's bankruptcy jurisdiction. Second, in light of the size of the Worldcom bankruptcy, the close connection between the defendants and Worldcom and the complexity of the litigation, Judge Cote concluded that a remand to state court "could slow the pace of litigation dramatically." She further held that discretionary remand was not appropriate because the plaintiffs had not identified any unique or unsettled issues of state law, and the presence of federal claims counseled against abstention. Finally Judge Cote held that "it is beyond cavil" that judicial economy and efficiency would be best served by keeping the cases in federal court so that they could be administered along with all the other cases consolidated before her. She concluded that "[w]ith the consolidation of the litigation in one court, the motion practice and discovery process can be

managed to protect the rights of all parties and to preserve, to the extent possible, the maximum amount of assets for recovery. ..."

Case Management

In a subsequent decision setting forth a detailed case-management plan for the consolidated proceedings, Judge Cote again stressed preservation of assets as a primary objective.⁷ She held that to the extent that "attorney's fees are incurred because of wasteful, duplicative litigation, that is a disservice to the victims and a failure of the court system." Among the other important objectives she identified in formulating a "sensible structure" for the pre-trial process were to provide all plaintiffs, whether individuals or members of a class, with a full and fair opportunity for discovery and meaningful participation in settlement discussions.

Judge Cote ordered that there would be no separate discovery taken in the individual actions without a showing of some issue unique to one or more individual plaintiffs. She directed that all discovery taken in the securities litigation would apply to, and upon execution of appropriate confidentiality agreements, be made available to all plaintiffs in the individual actions. She further ordered that discovery by all plaintiffs in the consolidated securities actions be conducted by lead counsel and that any contact with defense counsel was to be channeled through lead counsel. Counsel in the individual actions were required to select one law firm to serve as liaison counsel between the court and the securities action lead counsel. Liaison counsel was charged with conveying any discovery requests or litigation strategy concerns of any attorney for an individual plaintiff to lead counsel. Judge Cote's order provided that the attorneys for any individual plaintiff could seek the court's interven-

tion if they believed that liaison counsel was not sufficiently presenting their views or that lead counsel was not incorporating their views into the discovery process.

By setting up strict lines of communication and vesting at least the initial authority for conducting discovery with one lead counsel, Judge Cote has streamlined what might otherwise have been a litigation free-for-all. But in the interests of preserving assets for the plaintiffs, she has significantly reduced the role that plaintiffs' counsel can play in conducting the litigation. It remains to be seen whether this allocation of responsibility will give rise to its own universe of litigation squabbles.



(1) 15 USC §77v(a). In 1998, Congress enacted the Securities Litigation Uniform Standards Act (SLUSA), which carved out an exception to the removal bar on state court 1933 Act claims, by providing for mandatory removal to federal court of covered class actions. 15 USC 77p(c).

(2) *In re Worldcom, Inc. Securities Litigation*, 293 B.R. 308 (SDNY 2003).

(3) 514 US 300 (1995).

(4) 743 F2d 984 (3d Cir. 1984).

(5) Judge Cote acknowledged some contrary authority, including Southern District Judge Laura Taylor Swain's decision in *General Elec. Cap. Corp. v. Pro-Fac Coop.*, 2002 WL 1300054 (SDNY June 11, 2002), which found indemnification and contribution claims insufficient for related to jurisdiction, as well as the Third Circuit's recent decision in *In re Federal-Mogul Global, Inc.*, 300 F3d 368 (3d Cir. 2002), which took a narrower view of its earlier decision in *Pacor* than have most other courts. *Federal-Mogul* held that related-to jurisdiction exists only where the impact on the bankruptcy proceeding would not require the intervention of another lawsuit.

(6) 2003 WL 21659360 (SDNY July 15, 2003). *Disclosure*: The author represents one of the parties in this litigation.

(7) 2003 WL 21219037 (SDNY May 22, 2003).

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