INTERNATIONAL FINANCE SPRING 2009

FIRST CLASS ASSIGNMENT

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We will begin by reading a case which raises issues about when domestic courts do and should exercise jurisdiction over fraud claims involving a mix of foreign and domestic elements.

Morrison v. National Australia Bank Ltd., 547 F.3d 167 (2nd. Cir. 2008) (Newman, Calabresi & B.D. Parker)**

This appeal requires us to revisit the vexing question of the extraterritorial application of the securities laws, Rule 10b-5 in particular. Founded in 1858, headquartered in Melbourne, and incorporated under Australian law, the National Australia Bank ("NAB") calls itself Australia's largest bank. In 2000, its Australian business accounted for roughly 55% of its assets and revenues, with its international operations responsible for the remainder. NAB's approximately 1.5 billion "ordinary shares" (the equivalent of American common stock) trade on the Australian Securities Exchange, the London Stock Exchange, the Tokyo stock exchange, and the New Zealand stock exchange. While NAB's ordinary shares do not trade on United States exchanges, its American Depository Receipts[1] ("ADRs") trade on the New York Stock Exchange.

In February 1998, NAB acquired HomeSide Lending Inc., an American mortgage service provider headquartered in Jacksonville, Florida, for $ 1.22 billion. HomeSide serviced mortgages in exchange for fees. By March of 2000, HomeSide, as a wholly owned subsidiary of NAB, held the rights to service $ 18 billion of mortgages, making it America's sixth biggest mortgage service company.

Following the acquisition, HomeSide's operations were profitable. In HomeSide's first year, it earned A$ 313 2 million in mortgage servicing fees, and contributed to NAB's net profits. In 1999, NAB announced A$ 153 million in profits from HomeSide, which accounted for approximately 5.4% of NAB's A$ 2.82 billion in profits for the year. For the 2000 fiscal year, NAB reported that HomeSide generated A$ 141 million in profits, 4.1% of its total profits of A$ 3.37 billion.

HomeSide's accounting practices spawned this litigation. HomeSide calculated

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** You can find the decision here: http://www.ca2.uscourts.gov:8080/isysnative/RDpcT3BpbnNcT1BOXDA3LTA1ODMtY3Zfb3BuLnBkZg==/07-0583-cv_opn.pdf

[1] ADRs are issued by U.S. depository banks and represent "one or more shares of foreign stock or a fraction of a share. If you own an ADR, you have the right to obtain the foreign stock it represents." U.S. Securities and Exchange Commission website at http://www.sec.gov/answers/adrs.htm

the present value of the fees it would generate from servicing mortgages in future years using a valuation model, booked that amount on its balance sheet as an asset called Mortgage Servicing Right ("MSR"), and then amortized the value of that asset over its expected life.

In 2001, NAB revealed that the interest assumptions in the valuation model used by HomeSide to calculate the MSR were incorrect and resulted in an overstatement in the value of its servicing rights. In July 2001, NAB disclosed that it would incur a $ 450 million write-down due to a recalculation in the value of HomeSide's MSR. NAB's ordinary shares and its ADRs both fell more than 5% on the news. In September 2001, NAB announced a second write-down of $ 1.75 billion of the value of HomeSide's MSR, causing NAB's ordinary shares to plummet by 13% and its ADRs to drop by more than 11.5% on the NYSE. In an amended Form 10-Q filed with the SEC in December 2001, NAB restated previously issued financial statements to reflect the July and September adjustments.

Plaintiffs, four individuals who purchased NAB shares, sued NAB, HomeSide, and various individual officers and directors (collectively "Defendants") in the Southern District of New York, alleging violations of Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934... and Rule 10b-5 promulgated thereunder ... The Plaintiffs claimed that "NAB's subsidiary HomeSide knowingly used unreasonably optimistic valuation assumptions or methodologies" and that various of the Defendants made materially false and misleading statements in SEC filings, annual reports and press releases regarding HomeSide's profitability, economic health, and its contribution to NAB. HomeSide allegedly falsified the MSR in Florida and then sent the data to NAB in Australia, where NAB personnel disseminated it via public filings and statements.

Three of the plaintiffs who purchased their shares abroad (Russell Leslie Owen, Brian Silverlock, and Geraldine Silverlock) ("Foreign Plaintiffs") sought to represent a class of non-American purchasers of NAB ordinary shares, while the fourth plaintiff, Robert Morrison ("Domestic Plaintiff"), who purchased ADRs, sought to represent a class of American purchasers during a proposed class period of April 1, 1999 through September 3, 2001.

Defendants moved to dismiss the complaint for lack of subject matter jurisdiction under Rule 12(b)(1), and for failure to state a claim under Rule 12(b)(6) of the Federal Rules of Civil Procedure... The district court .. granted the motion, and dismissed the claims of the Foreign Plaintiffs for lack of subject matter jurisdiction and those of the Domestic Plaintiff for failure to state a claim. This appeal followed.

DISCUSSION

I."Determining the existence of subject matter jurisdiction is a threshold inquiry and a claim is properly dismissed for lack of subject matter jurisdiction under Rule 12(b)(1) when the district court lacks the statutory or constitutional power to adjudicate it." ...”A plaintiff asserting subject matter jurisdiction has the burden of proving by a preponderance of the evidence that it exists."..."In reviewing a district court's dismissal of a complaint for lack of subject matter jurisdiction, we review factual findings for clear error and legal conclusions de novo."... "[T]he court must take all facts alleged in the complaint as true and draw all reasonable inferences in favor of plaintiff," ... but

"jurisdiction must be shown affirmatively, and that showing is not made by drawing from the pleadings inferences favorable to the party asserting it." ... In resolving a motion to dismiss for lack of subject matter jurisdiction under Rule 12(b)(1) a district court may consider evidence outside the pleadings. ..

"Only Congress may determine a lower federal court's subject-matter jurisdiction."... When Congress wrote the Securities Exchange Act, however, it omitted any discussion of its application to transactions taking place outside of the United States [4]... Therefore, when faced with securities law claims with an international component, we turn to "the underlying purpose of the anti-fraud provisions as a guide" to "discern 'whether Congress would have wished the precious resources of the United States courts and law enforcement agencies to be devoted to' such transactions."... The underlying purpose of Section 10(b) is "to remedy deceptive and manipulative conduct with the potential to harm the public interest or the interests of investors." ... Harm to domestic interests and domestic investors has not been the exclusive focus of the anti-fraud provisions of the securities laws. As our case law makes clear, we believe that it is consistent with the statutory scheme to infer that Congress would have wanted "to redress harms perpetrated abroad which have a substantial impact on investors or markets within the United States."...

We decided in Psimenos v. E.F. Hutton & Co.... (2d Cir. 1983), that .in determining the extraterritorial reach of Section 10(b) we look to whether the harm was perpetrated here or abroad and whether it affected domestic markets and investors. This binary inquiry calls for the application of the "conduct test" and the "effects test."... We ask: (1) whether the wrongful conduct occurred in the United States, and (2) whether the wrongful conduct had a substantial effect in the United States or upon United States citizens. ... Where appropriate, the two parts of the test are applied together because "an admixture or combination of the two often gives a better picture of whether there is sufficient United States involvement to justify the exercise of jurisdiction by an American court." ... In this case, however, Appellants rely solely on the conduct component of the test.

Under the "conduct" component, subject matter jurisdiction exists if activities in this country were more than merely preparatory to a fraud and culpable acts or omissions occurring here directly caused losses to investors abroad.... Our determination of whether American activities "directly" caused losses to foreigners depends on what and how much was done in the United States and on what and how much was done abroad...

Here, HomeSide allegedly manipulated its internal books and records and sent the falsely inflated numbers from Florida to NAB's headquarters in Australia. NAB, operating from Australia, created and distributed its public filings and related public statements from Australia. These public filings and statements included HomeSide's falsified numbers in two ways. NAB directly included some of the allegedly false HomeSide numbers as stand-alone numbers in public filings. NAB also incorporated

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[4] We respectfully urge that this significant omission receive the appropriate attention of Congress and the Securities and Exchange Commission.

allegedly false HomeSide numbers in company-wide figures (e.g., company-wide revenue, profit, and growth numbers), rendering them false to the extent that they depended on the artificially inflated numbers from HomeSide.

Appellants contended that the fraud occurred primarily in Florida because HomeSide was located there and the false numbers at issue were created there. The district court disagreed. In what it described as a "close call," the district court determined that HomeSide's knowing use of unreasonably optimistic assumptions to artificially inflate the value of its MSR could not serve as a predicate for subject matter jurisdiction because this conduct amounted to, at most, a link in the chain of a scheme that culminated abroad. The district court reasoned that there would have been no securities fraud "but-for (i) the allegedly knowing incorporation of HomeSide's false information; (ii) in public filings and statements made abroad; (iii) to investors abroad; (iv) who detrimentally relied on the information in purchasing securities abroad." ...Accordingly, the district court determined that "[o]n balance, it is the foreign acts -- not any domestic ones -- that 'directly caused' the alleged harm here." ... It concluded that the Plaintiffs failed to meet "their burden of demonstrating that Congress intended to extend the reach of its laws to the predominantly foreign securities transactions at issue here." ...

II. The district court believed that the difficulty of this case is heightened by its novelty. Here, a set of (1) foreign plaintiffs is suing (2) a foreign issuer in an American court for violations of American securities laws based on securities transactions in (3) foreign countries. This is the first so-called "foreign-cubed" securities class action to reach this Circuit.... But despite this unusual fact-pattern, the usual rules still apply. As we noted, subject matter jurisdiction exists over these claims only "if the defendant's conduct in the United States was more than merely preparatory to the fraud, and particular acts or culpable failures to act within the United States directly caused losses to foreign investors abroad." ...

Our Circuit's current standard for determining whether we possess subject matter jurisdiction over transnational securities fraud largely grew out of a series of opinions we issued between 1968 and 1983.[6] Two of these cases, Bersch v. Drexel Firestone,

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[6]A degree of confusion appears to exist in the other Circuits regarding our standard. In Zoelsch v. Arthur Andersen & Co...(D.C. Cir. 1987), the D.C. Circuit hypothesized that "[t]he Second Circuit's rule seems to be that jurisdiction will lie in American courts where the domestic conduct comprises all the elements of a defendant's conduct necessary to establish a violation of section 10(b) and Rule 10b-5: the fraudulent statements or misrepresentations must originate in the United States, must be made with scienter and in connection with the sale or purchase of securities, and must cause the harm to those who claim to be defrauded, even though the actual reliance and damages may occur elsewhere." The Fifth Circuit has since taken issue with that characterization. See Robinson v. TCI/US W. Communs. ... (5th Cir. 1997) ("Some courts, including the District of Columbia Circuit in Zoelsch, have suggested that the Second Circuit's test requires all elements of the alleged fraud to have occurred domestically. . . . [T]his is a bit of an overstatement: A close examination of the Second Circuit's caselaw reveals that the real test is simply whether material domestic conduct directly caused the complained-of loss."). To clear up any confusion, we reiterate that our "conduct test" requires that "the defendant's conduct in the United States [be] more than merely preparatory to the fraud, and [that] particular acts or culpable failures to act within

Inc.... and IIT v. Vencap, Ltd.... both written by Judge Friendly, are particularly helpful.

Bersch involved the offering of shares in IOS, a Canadian mutual fund, to non-Americans via a prospectus distributed outside of the United States, which the plaintiffs in the action asserted contained misleading statements and omissions... Of the six investment banks that underwrote the offering, two were headquartered in America, as was Arthur Andersen, IOS's primary accounting firm... IOS, the underwriters, and their attorneys and accountants met on many occasions in New York to initiate, organize, and structure the offering; parts of the prospectus were drafted in New York and read over the telephone to personnel at the main business office of IOS in Geneva, Switzerland; and the proceeds of the offering were deposited in New York before being distributed to IOS... We concluded that we did not have subject matter jurisdiction because the fraud itself consisted of the delivery of the fraudulent prospectus to investors and the final prospectus emanated from a foreign source (London, Brussels, Toronto, the Bahamas, or Geneva)... Despite the fact that meetings and work regarding the prospectus took place in New York, we concluded that those actions were "merely preparatory" or took the "form of culpable nonfeasance and are relatively small in comparison to those abroad." ...

In Vencap, which involved the allegedly fraudulent sale of foreign securities to a British investment trust, with certain actions taken in the United States, we determined that the findings of the district court did not provide enough information for us to determine subject matter jurisdiction. We did, however, observe that a fundamental consideration in determining whether conduct gives rise to subject matter jurisdiction is that the United States should not be "used as a base for manufacturing fraudulent security devices for export, even when these are peddled only to foreigners," as "[t]his country would surely look askance if one of our neighbors stood by silently and permitted misrepresented securities to be poured into the United States."...

Bersch and Vencap illustrate how to approach subject matter jurisdiction under the "conduct test": identify which action or actions constituted the fraud and directly caused harm -- in the case of Bersch, the act of placing the allegedly false and misleading prospectus "in the purchasers' hands,"... -- and then determine if that act or those actions emanated from the United States.... Since then we have repeatedly applied these principles...

We most recently applied them in SEC v. Berger... (..2003). There, the Manhattan Investment Fund, an offshore investment company organized under the laws of the British Virgin Islands and run by a single active director (Berger), suffered losses in excess of $ 300 million.... Instead of reporting these losses, Berger, working in New York, created fraudulent account statements that "vastly overstated" the market value of the Fund's holdings... Berger sent these fraudulent account statements to the fund administrator in Bermuda and ordered the administrator to send to investors the fraudulent statements rather than the accurate ones supplied by Bear Stearns.... We

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the United States directly cause [] losses to foreign investors abroad" for subject matter jurisdiction to exist. Alfadda, 935 F.2d at 478. We disavow the D.C. Circuit's characterization of our test as requiring the domestic conduct to comprise all the elements necessary to establish a violation of Rule 10b-5.

held that we had subject matter jurisdiction under the "conduct test" because the "fraudulent scheme was masterminded and implemented by Berger in the United States," ... even though the statements that ultimately conveyed the fraudulent information to investors were mailed from Bermuda. The critical factor was that the conduct that directly caused loss to investors -- the creation of the fraudulent statements -- occurred in New York.

Determining what is central or at the heart of a fraudulent scheme versus what is "merely preparatory" or ancillary can be an involved undertaking. Appellees and certain of the amici curiae urge us to eschew this analysis in favor of a bright-line rule. They urge us to rule that in so-called "foreign-cubed" securities actions, showing domestic conduct should never be enough and subject matter jurisdiction cannot be established where the conduct in question has no effect in the United States or on American investors. They contend that the general "presumption" against the extraterritorial application of American laws bars American courts from exercising subject matter jurisdiction over these types of claims.

In support of their position, Appellees and amici point to a parade of horribles that they claim would result if American courts exercised subject matter jurisdiction over such actions. They contend that this would, among other things, undermine the competitive and effective operation of American securities markets, discourage cross-border economic activity, and cause duplicative litigation. Their principal objection, though, is that entertaining such actions here would bring our securities laws into conflict with those of other jurisdictions. For instance, in Switzerland, no comprehensive federal legislation governs securities fraud, and private remedies are the only ones available. In Canada, securities class actions are recognized, but most provinces do not recognize the fraud on the market doctrine. In various other countries, class actions are either not available or the ability of class actions to preclude further litigation is problematic... In essence, Appellees argue that other countries have carefully crafted their own, individual responses to securities litigation based on national policies and priorities and that opening American courts to such actions would disrupt and impair these carefully constructed local arrangements.

However, the potential conflict between our anti-fraud laws and those of foreign nations does not require the jettisoning of our conduct and effects tests for "foreign-cubed" securities fraud actions and their replacement with the bright-line ban advocated by Appellees. The problem of conflict between our laws and those of a foreign government is much less of a concern when the issue is the enforcement of the anti-fraud sections of the securities laws than with such provisions as those requiring registration of persons or securities. The reason is that while registration requirements may widely vary, anti-fraud enforcement objectives are broadly similar as governments and other regulators are generally in agreement that fraud should be discouraged. As Judge Friendly pointed out in IIT, Int'l Inv. Trust v. Cornfeld ... "[t]he primary interest of [a foreign state] is in the righting of a wrong done to an entity created by it. If our anti-fraud laws are stricter than [a foreign state's], that country will surely not be offended by their application."

Furthermore, declining jurisdiction over all "foreign-cubed" securities fraud actions would conflict with the goal of preventing the export of fraud from America. As

the argument goes, the United States should not be seen as a safe haven for securities cheaters; those who operate from American soil should not be given greater protection from American securities laws because they carry a foreign passport or victimize foreign shareholders. A much stronger case would exist, for example, for the exercise of subject matter jurisdiction in a case where the American subsidiary of a foreign corporation issued fraudulent statements or pronouncements from the United States impacting the value of securities trading on foreign exchanges. Moreover, we are leery of rigid bright-line rules because we cannot anticipate all the circumstances in which the ingenuity of those inclined to violate the securities laws should result in their being subject to American jurisdiction. That being said, we are an American court, not the world's court, and we cannot and should not expend our resources resolving cases that do not affect Americans or involve fraud emanating from America. In our view, the "conduct test" balances these competing concerns adequately and we decline to place any special limits beyond the "conduct test" on "foreign-cubed" securities fraud actions.

The issue for us to resolve here boils down to what conduct comprises the heart of the alleged fraud. Appellants assert that the alleged manipulation of the MSR by HomeSide in Florida made up the main part of the fraud since those false numbers constituted the misleading information passed on to investors through NAB's public statements. According to Appellants, if HomeSide had not created and sent artificially inflated numbers up to its parent company, there would have been no fraud, no harm to purchasers, and no claims under Rule 10b-5. Appellants insist that NAB's creation and dissemination of the public statements in question consisted solely of the mechanical insertion of HomeSide's numbers into the statements and public filings and that the locus of the improper conduct (Florida) and not the place of compilation (Australia) should determine jurisdiction.

The Appellees, on the other hand, argue that the allegedly false and misleading public statements made by NAB constituted the fraud, since, without those statements, no misinformation would have been reported, no investors would have been defrauded, and no actionable claims would have existed under Rule 10b-5. Since NAB's public statements were compiled in Australia and disseminated from there, Appellees contend that the only conduct that directly caused harm to investors occurred in Australia.

We conclude that we do not have subject matter jurisdiction. The actions taken and the actions not taken by NAB in Australia were, in our view, significantly more central to the fraud and more directly responsible for the harm to investors than the manipulation of the numbers in Florida. HomeSide, as a wholly owned, primarily operational subsidiary of NAB, reported to NAB in Australia. HomeSide's mandate was to run its business well and make money. The responsibilities of NAB's Australian corporate headquarters, on the other hand, included overseeing operations, including those of the subsidiaries, and reporting to shareholders and the financial community. NAB, not HomeSide, is the publicly traded company, and its executives -- assisted by lawyers, accountants, and bankers -- take primary responsibility for the corporation's public filings, for its relations with investors, and for its statements to the outside world.

Appellants' claims arise under Rule 10b-5(b), which focuses on the accuracy of statements to the public and to potential investors. Ensuring the accuracy of such statements is much more central to the responsibilities of NAC's corporate

headquarters, which issued the statements, than to those of HomeSide, which did not. Liability under Rule 10b-5(b) requires a false or misleading statement. "Anything short of such conduct is merely aiding and abetting, and no matter how substantial that aid may be, it is not enough to trigger liability under Section 10(b)." ...NAB's executives possess the responsibility to present accurate information to the investing public and to the holders of its ordinary shares in accordance with a host of accounting, legal and regulatory standards. When a statement or public filing fails to meet these standards, the responsibility, as a practical matter, lies in Australia, not Florida.

Another significant factor at play here is the striking absence of any allegation that the alleged fraud affected American investors or America's capital markets. Appellants press their appeal solely on behalf of foreign plaintiffs who purchased on foreign exchanges and do not pursue the "effects" test. They do not contend that what Appellants allegedly did had any meaningful effect on America's investors or its capital markets. This factor weighs against our exercise of subject matter jurisdiction.

A third factor that weighs against jurisdiction is the lengthy chain of causation between the American contribution to the misstatements and the harm to investors. HomeSide sent allegedly falsified numbers to Australia. Appellants do not contend that HomeSide sent any falsified numbers directly to investors. If NAB's corporate headquarters had monitored the accuracy of HomeSide's numbers before transmitting them to investors, the inflated numbers would have been corrected, presumably without investors having been aware of the irregularities, much less suffering harm as a result. In other words, while HomeSide may have been the original source of the problematic numbers, those numbers had to pass through a number of checkpoints manned by NAB's Australian personnel before reaching investors. While HomeSide's rigging of the numbers may have contributed to the misinformation, a number of significant events needed to occur before this misinformation caused losses to investors. This lengthy chain of causation between what HomeSide did and the harm to investors weighs against our exercising subject matter jurisdiction. As the Supreme Court noted in Stoneridge, "deceptive acts [that] were not communicated to the public" do not suffice to "show reliance . . . except in an indirect chain that we find too remote for liability."...

This particular mix of factors -- the fact that the fraudulent statements at issue emanated from NAB's corporate headquarters in Australia, the complete lack of any effect on America or Americans, and the lengthy chain of causation between HomeSide's actions and the statements that reached investors -- add up to a determination that we lack subject matter jurisdiction.

III. CONCLUSION For all these reasons, the judgment of the district court is affirmed.

NOTES AND QUESTIONS:

The SDNY judgment in this case [1] includes a more informative note on ADRs than that reproduced above:

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[1] In re Nat'l Austl. Bank Sec. Litig., 2006 U.S. Dist. LEXIS 94162 (SDNY 2006).

"An ADR is a receipt that is issued by a depositary bank that represents a specified amount of a foreign security that has been deposited with a foreign branch or agent of the depositary, known as the custodian. The holder of an ADR is not the title owner of the underlying shares; the title owner of those shares is either the depositary, the custodian, or their agent. ADRs are tradable in the same manner as any other registered American security, may be listed on any of the major exchanges in the United States or traded over the counter, and are subject to the [federal securities laws.] This makes trading an ADR simpler and more secure for American investors than trading in the underlying security in the foreign market." Pinker v. Roche Holdings Ltd., 292 F.3d 361, 367 (3d Cir. 2002)...

The facts underlying this case involve different jurisdictions. National Australia Bank (NAB), headquartered in Melbourne, Australia, owned HomeSide, a mortgage service provider in Florida.[2] National Australia Bank Limited is the holding company for an international financial services group and is regulated in Australia.[3] NAB makes disclosures about its business in Australia, and also files reports with the SEC as a foreign issuer. NAB owned entities are also regulated in the jurisdictions where they carry on business.

The judgment tells us that “Three of the plaintiffs who purchased their shares abroad.. sought to represent a class of non-American purchasers of NAB ordinary shares, while the fourth plaintiff...who purchased ADRs, sought to represent a class of American purchasers...”[4] The SDNY’s judgment states that “The Lead Foreign Plaintiffs are residents of Australia, who purchased NAB's ordinary shares on an Australian exchange in 2001.” Why would non-US persons who purchased shares outside the US which were issued by a non-US issuer try to sue for securities fraud in the US? (The “foreign cubed” case).

We are told that NAB shares “trade on the Australian Securities Exchange, the London Stock Exchange, the Tokyo stock exchange, and the New Zealand stock exchange.” Do you think it should make a difference for fraud liability where an investor bought the shares? For example, should an investor who bought in Tokyo only be able to sue in Japan? Would it make a difference whether the investor were a Japanese citizen or resident?

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[2] Washington Mutual (whose assets were acquired by JP Morgan Chase in 2008) acquired HomeSide in 2002.

[3] NAB must comply with the provisions of two Commonwealth statutes in Australia: the Banking Act 1959 (Cth) and the Corporations Act 2001 (Cth). See NAB Annual Report *available at* http://idea.sec.gov/Archives/edgar/data/833029/000110465906083027/a06-25557_120f.htm. See also http://nab2008annualreports.textpacific.com.au/ .

[4] The reasoning in the 2nd Circuit applies to the Lead Foreign Plaintiffs. The Lead Domestic Plaintiff was dismissed by the SDNY because he failed to allege that he suffered any damages from the alleged fraud.

The Court states: “Our Circuit's current standard for determining whether we possess subject matter jurisdiction over transnational securities fraud largely grew out of a series of opinions we issued between 1968 and 1983.” Do you think there might be any difficulties in applying standards developed between 1968 and 1983 to acts carried out 20 and more years later? In footnote 4, the Court notes that “When Congress wrote the Securities Exchange Act, however, it omitted any discussion of its application to transactions taking place outside of the United States” and urges Congress to address the issue. Under what circumstances do you think that US rules should apply to transactions taking place outside the US?

The Second Circuit rejects the bright-line rule suggested by amici in favor of a fact based analysis. What are the advantages and disadvantages of this approach?

The Washington Legal Foundation reacted to this decision as follows:
On October 23, 2008, WLF scored a major victory when a three-judge panel of the U.S. Court of Appeals for the Second Circuit unanimously affirmed a ruling by the district court that United States securities laws do not have extraterritorial application to a foreign corporation. This ruling will have an impact on foreign corporations, especially those that have invested in U.S. businesses. In affirming the district court, the appeals court proclaimed, "We are an American court, not the world's court, and we cannot and should not expend our resources resolving cases that do not affect Americans or involve fraud emanating from America."[5]

Is this an accurate representation of the decision?

Another amicus brief was filed by the Securities Industry and Financial Markets Association (SIFMA), the Chamber of Commerce of the United States of America, the United States Council for International Business, and the Association Française des Entreprises Privées.[6] This amicus brief states:

> The rapid globalization of financial markets in recent years has given rise to new competitive challenges for the United States – challenges recognized not only by amici and their members as market participants, but also by respected scholars in law, economics and finance and by leaders at all levels of government, across the political spectrum. A central component of this ongoing and serious competitive threat to U.S. markets is the risk that securities class actions – litigation with abusive potential long acknowledged by the courts and Congress – will reduce cross-border investment and deter foreign companies from accessing U.S. markets.
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> This case presents a virtual “Exhibit A” for any foreign jurisdiction seeking to demonstrate, for its competitive advantage, the perils of coming into contact with the United States. An Australian company listed on an Australian exchange, with virtually all of its shareholders outside the United States, faces the possibility of protracted litigation in the U.S.

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[5] http://www.wlf.org/Litigating/casedetail.asp?detail=500 . The WLF Amicus Brief in the case is accessible from this page.

[6] http://www.sifma.org/regulatory/briefs/2007/NAB.pdf .

courts for alleged misstatements made to those non-U.S. investors. Perhaps even more damaging, plaintiffs principally rest this unprecedented attempt to expand U.S. jurisdiction, rightly rejected by the district court, on the Australian company's decision to invest in a U.S. subsidiary. In other words, plaintiffs seek to convert the decision to acquire a U.S. business into a securities litigation risk factor for non-U.S. companies – discouraging cross border economic activity even where that activity bears no relation to the interests protected by the U.S. securities laws.

The Supreme Court consistently has taught that courts must approach cases like this one with the "presumption that United States law governs domestically but does not rule the world." Microsoft, Inc. v. AT&T... (2007). This Circuit, as well, has recognized that it should not lightly devote the resources of U.S. courts to predominantly foreign matters and instead should leave the issue to foreign countries. Bersch v. Drexel Firestone, Inc.... (2d Cir. 1975). Moreover, as the Microsoft Court emphasized, it would be especially inappropriate to apply U.S. law to claims arising outside the United States in areas of law that "may embody different policy judgments." ... . There can be no question that this case involves just such an area of law – an area fraught with controversy and the potential for abuse even within the U.S. legal system – and where other countries can, and do, make fundamentally different policy decisions.

Whatever the merits of private securities class actions may be, the Supreme Court has recently reiterated that, "if not adequately contained, [they] can be employed abusively to impose substantial costs on companies and individuals whose conduct conforms to the law." Tellabs, Inc. v. Makor Issues & Rights, Ltd.... (June 21, 2007). The U.S.' securities-fraud class-action regime stands alone in the world, with its combination of the opt-out class-action procedure, tolerance of contingency fees, expansive and expensive discovery procedures, jury trials and potential for massive and devastating damage awards. Indeed, these very differences between the U.S. system and others have enticed plaintiffs whose claims rightfully belong in other countries to try to find a way into U.S. courts.

...of central importance to amici and their members, the application of domestic law to fundamentally foreign disputes raises a host of policy concerns, as courts and commentators have generally recognized for decades.

• It risks weakening core principles of comity – precluding foreign jurisdictions from establishing liability rules best suited to their markets in an area where U.S. courts and regulators have struggled for decades to strike an appropriate balance between plaintiffs and defendants.
• It risks deterring foreign companies from making acquisitions of U.S. companies – for fear of becoming subject to securities law liability if the target companies have prepared financials that arguably mislead the foreign company and its non-U.S. shareholders.
• It creates a reciprocal risk to U.S. companies – exposing them, should foreign courts adopt similar logic, to securities litigation in virtually any jurisdiction in which they have a subsidiary, even if their shares are traded exclusively by investors in the United States.
• It creates the risk of duplicative litigation – with various plaintiffs seeking out the class action regime most favorable to their case and the possibility of multiple "bites at the apple."
• Lastly, it creates the risk of arbitrariness and inequity – with different companies subject to different liability regimes dependent solely on tenuous factors arising out of the location of business operations or other considerations unrelated to the investor protection objectives of the U.S. securities laws...

Do you find these arguments persuasive?