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Transnational Investment in Securities and Extraterritoriality: Materials for Class on Monday April 1 2024

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Money and financial claims are transferred easily across territorial boundaries, but the rules which regulate these claims are mostly fixed in particular geographic locations.[2] Financial firms need to be licensed to carry on business by the regulators in the jurisdictions in which they do business.[3] Issuers of securities may choose to sell their securities in more than one jurisdiction,[4] to increase the pool of prospective investors, and may list their securities on exchanges based in more than one jurisdiction,[5] but if they do so they become subject to rules in force in the different jurisdictions in which they sell the securities. A company that decides to list its securities outside its home jurisdiction may find that its securities are ineligible for inclusion in indices, which means that the issuer is not able to benefit from passive investment by funds

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[2] Even where there is transnational harmonization of standards the rules that affect financial market participants are those which are promulgated in domestic legal systems.

[3] *See, e.g.*, SEC Charges Four India-Based Brokerage Firms with Violating U.S. Registration Requirements (Nov. 27, 2012) at http://www.sec.gov/news/press/2012/2012-241.htm.

[4] The China Securities Regulatory Commission recently introduced a revised review mechanism for Chinese companies wishing to list securities outside China. *See*, *e.g.*, Chinese Companies Listed on Major U.S. Stock Exchanges (updated Jan. 8, 2024) at https://www.uscc.gov/sites/default/files/2024-01/Chinese_Companies_Listed_on_US_Stock_Exchanges_01_2024.pdf.

[5] Shell plc shares are listed in Amsterdam, London and, as American Depositary Receipts (ADRs) in New York. 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. ADRs may be listed on a US exchange or traded over the counter. See, e.g., Pinker v. Roche Holdings Ltd., 292 F. 3d 361, 365(3rd Cir. 2002) ("American Depositary Receipts ("ADRs") are financial instruments that allow investors in the United States to purchase and sell stock in foreign corporations in a simpler and more secure manner than trading in the underlying security in a foreign market.")

that focus on index investments.[6]

Jurisdictions compete with each other to attract economic activity, including financial activity.[7] New York has for a long time been an attractive place for issuers to list securities, either at the New York Stock Exchange or on NASDAQ, and recently it seems that this attractiveness has only increased.[8] However, Shein, a fast-fashion company headquartered in Singapore recently suggested it would consider a London listing if it were prevented from listing in the US because of its links with China.[9] Financial competition with other jurisdictions is affected by other political considerations.

Sometimes even selling securities outside a particular jurisdiction raises issues of compliance with that jurisdiction's securities laws: the US is concerned that sales of securities to "US persons" should be carried out in conformity with US rules. The development of offshore US dollar denominated markets in Europe (the euromarket), which involved issues of US dollar denominated debt securities outside the US, suggested to the Securities and Exchange Commission (SEC) that there was a risk that US investors might come to hold securities which had not been issued with the disclosure required within the US. Such offerings were always accompanied by US legal opinions with respect to the risks of the applicability of US securities registration requirements (the risk being that US$ denominated securities would be attractive to US investors). Beginning in 1990 the SEC developed safe harbors with respect to registration and these are now set out in Regulation S.[10] Offers to non-US persons carried out in compliance with the requirements of the Regulation do not require registration. But a US person includes a foreign citizen who is a US permanent resident, and other foreign citizens may also be considered to be US persons.[11] Regulation S is designed to ensure that such securities come to rest outside the US,

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[6] *See*, *e.g.*, James Mackintosh, VinFast, Arm and Other Index Orphans Miss Out on Billions From Passive Investors, Wall Street Journal (Aug. 25, 2023).

[7] *Cf.* https://www.visualcapitalist.com/top-global-financial-centers-in-2023/ .

[8] *See*, *e.g.*, Philip Augar, *How the Us Is Crushing Europe's Domestic Exchanges*, Financial Times (Sep. 25, 2023) ("They are the markets of choice because they are the largest. US equities account for nearly 70 per cent of the MSCI World index; the next five largest — in Japan, UK, France, Canada and Germany — total less than 20 per cent. The top 10 constituent equities of the MSCI World index, which are all US companies including Apple at number one and ExxonMobil at number 10, aggregate to more than 20 per cent."); Ian Johnston & Jonathan Wheatley, Indivior Aims to Move Primary Listing from London to New York, Financial Times (Feb. 22, 2024).

[9] Eleanor Olcott, Mercedes Ruehl, Jim Pickard & Lucy Fisher, Shein Considers London Listing If US IPO Blocked over Ties to China, Financial Times (Feb. 27, 2024); Julia Kollewe, UK's Jeremy Hunt Met Shein Boss in Attempt to Lure Firm's IPO to London, The Guardian (Feb. 27, 2024).

[10] 17 CFR § 230.901- 203.905.

[11] See SEC Guidance at https://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm#276.01. The guidance states "Other individuals without permanent resident status may also be residents of the U.S. for purposes of these provisions. In

and in a Final Rule published in 1998 the SEC expressed concerns that abuses had arisen and tightened some of the rules.[12] The Regulation S safe harbors relate to registration and not to fraud liability. Later in the semester we will look at some issues raised by Fintech, including cryptocurrencies, and we will see that issuances of cryptocurrencies may be caught by the Federal securities laws. A coin that would be considered under US law to be a security must either be registered under the Securities Act 1933 or benefit from an exemption from registration. The SEC's recent enforcement action relating to Binance charged Binance and its founder with secretly allowing US based customers to trade on the Binance.com platform while publicly claiming that this was not possible, and with the unregistered sale of Binance's own crypto assets.[13]

In addition to investing in securities issued by foreign issuers whose securities are available on domestic markets in the US, usually as ADRs,[14] US investors have increasingly been investing in securities in markets outside the US.[15] Often this is accomplished through investments in mutual funds or exchange-traded funds which invest in international securities, and some brokers offer brokerage accounts which allow investors to trade in foreign securities in foreign markets.[16]

In this class we are going to focus on the definition of the territorial scope of application of rules relating to fraud liability in the context of cross-border financial activity. Financial activities that involve multiple jurisdictions raise questions about what law should apply. This may be a normative question, but it is also a question of interpretation of domestic rules. What sorts of connections between acts and persons and a particular territory are and should be treated as providing the basis for the application of law, and jurisdiction, with respect to frauds? There

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these circumstances, an issuer must decide what criteria it will use to determine residency and apply them consistently without changing them to achieve a desired result. Examples of factors an issuer may apply include tax residency, nationality, mailing address, physical presence, the location of a significant portion of their financial and legal relationships, or immigration status."

[12] Securities and Exchange Commission, Offshore Offers and Sales, 63 Fed. Reg. 9632, 9632 (Feb. 25, 1998) ("Regulation S has been used as a means of perpetrating fraudulent and manipulative schemes, especially schemes involving the securities of thinly capitalized or ''microcap'' companies. These types of securities are particularly vulnerable to fraud and manipulation because little information about them is available to investors.")

[13] SEC Files 13 Charges Against Binance Entities and Founder Changpeng Zhao (Jun. 5, 2023).

[14] *See*, *e.g.*, Charles Schwab, 4 Ways to Invest Internationally (Aug. 14, 2023) at https://www.schwab.com/learn/story/4-ways-to-invest-internationally .

[15] The Growing Importance of Cross-Border Securities Holdings for the US Economy (Nov. 15, 2022) at https://www.sifma.org/resources/news/the-growing-importance-of-cross-border-securities-holdings-for-the-u-s-economy/.

[16] *See*, *e.g.*, Charles Schwab, 4 Ways to Invest Internationally (Aug. 14, 2023) at https://www.schwab.com/learn/story/4-ways-to-invest-internationally .

could be circumstances where regulators in more than one jurisdiction would like to take enforcement action with respect to the same circumstances, leading to a risk of over-enforcement.

In recent years the US Supreme Court has developed a presumption that US Federal statutes do not have extraterritorial application.[17] Congress may choose to enact legislation that applies extraterritoriality, but the Court will generally apply a presumption against extraterritoriality. Some version of this presumption has existed in American law since the 19th century, but it has evolved over time.[18] And it is a general presumption which does not only apply in the context of financial transactions, although this is the context where we will examine it.

From an international perspective, we should notice that the issue of the appropriateness of states exercising extraterritorial jurisdiction has also evolved. The US willingness to apply its anti-trust and securities laws with extraterritorial effects led to other jurisdictions enacting blocking legislation to prevent these effects.[19] More recently, the EU was concerned to address US sanctions against Iran and amended its blocking rules to deal with this issue.[20] At the same

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[17] *See*, *e.g.*, Julie Rose O'Sullivan, *The Extraterritorial Application of Federal Criminal Statutes: Analytical Roadmap, Normative Conclusions, and a Plea to Congress for Direction*, 106 Georgetown Law Journal 1021, 1026 (2018) ("The presumption against extraterritoriality means that the Court assumes that Congress intends its statutes to apply only to conduct within the territory of the United States unless it says otherwise. This exclusive emphasis on conduct within the territory of a State reflects the subjective territorial principle under the international law of prescriptive jurisdiction.")

[18] *See*, *e.g.*, William S. Dodge, *The New Presumption Against Extraterritoriality*, 133 HARV. L. REV. 1582, 1584-5 (2020) ("The presumption against extraterritoriality is a prime example of a canon that has changed substantially over time. The presumption began in the nineteenth century as an application of the Charming Betsy canon, requiring that statutes be construed to avoid violations of international law. When international law evolved to permit greater extraterritorial regulation, the Supreme Court kept the presumption but articulated new rationales — first, international comity and then Congress's primary concern with domestic conditions. The American Banana version of the presumption that the Court applied during the first half of the twentieth century turned entirely on the location of the conduct. When this approach would have led to results that seemed inconsistent with Congress's intent, the Court distinguished or ignored the presumption. After 1949, the presumption fell into disuse for four decades. It was reborn in the 1991 case EEOC v. Arabian American Oil Co.13 (Aramco) and was applied regularly, if somewhat inconsistently, thereafter. The Aramco version of the presumption purported to be a clear statement rule, and, like American Banana's version of the presumption, it turned entirely on the location of the conduct." (footnotes omitted)).

[19] For example, the UK's Protection of Trading Interests Act 1980, 1980 Ch.11.

[20] *See, e.g.*, Commission Implementing Regulation(EU) 2018/1101 laying down the criteria for the application of the second paragraph of Article 5 of Council Regulation (EC) No 2271/96 protecting against the effects of the extra-territorial application of legislation adopted by a third country, and actions based thereon or resulting therefrom, OJ No. L199I/7 (Aug. 7, 2018). See also, Commission Communication, The European Economic and Financial System: Fostering Openness, Strength and Resilience, COM(2021) 32 final (Jan. 19, 2021) at p. 18 ("The EU considers that the extra-territorial application by third countries of measures against EU operators is contrary to international law.").

time jurisdictions other than the US now appreciate the complexities of reconciling jurisdiction based on ideas of territoriality with the facts of globalization.[21]

The materials here focus primarily on civil liability under the US Federal securities laws, and in particular, s10(b) of the Securities Exchange Act 1934[22] and Rule 10b-5,[23] which give rise to an implied private right of action for investors.

In **Morrison v National Australia Bank**,[24] the US Supreme Court was faced with an f-cubed securities claim: claims of securities fraud brought in the Southern District of New York by investors outside the US who had purchased shares in a foreign issuer, National Australia Bank, outside the US. [25] I am providing you with excerpts from the judgments in the 2nd Circuit and the Supreme Court in this case. Which approach do you find to be more persuasive? Under what circumstances do you think that US rules should apply to transactions taking place outside the US?

The Second Circuit Court of Appeals applied the test it had developed and applied for many years to the facts of the case, concluding that there was no jurisdiction over the case based

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[21] *See generally, e.g.*, *Developments in the Law: Extraterritoriality*, 124 HARV. L. REV. 1226, 1233 (2011) ("there is no simple descriptive theory of the patterns of American extraterritorial exertion and the international community's response. Congress eagerly legislates beyond American borders — at least in cases of protecting competitive markets and curbing state-sponsored terrorism. Courts have restrained that legislative impulse. But these institutional roles are curiously inconsistent in cases of individual rights. Courts have narrowed statutory remedies for foreign human rights violations but serve as guardians of constitutional protections that Congress has sought to limit beyond U.S. borders. The European Union's posture toward American extraterritorial law is equally inconsistent. Together, these aspects of extraterritoriality do not point to one clear path for global politics and legal theory. Rather, they reflect a continuing search for solutions to a common problem: how to reconcile the premises underlying the Westphalian, state-based order with an increasingly integrated world.")

[22] 15 USC § 78j(b): "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange–...(b). To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered ... any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors...."

[23] 17 C.F.R. § 240.10b-5: "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange, 1. To employ any device, scheme, or artifice to defraud, 2. To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or 3. To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security."

[24] 130 S. Ct. 2869 (S.Ct. 2010).

[25] Foreign investors, issuer, transactions.

on an examination of how much conduct there had been in the US and effects of the alleged fraud in the US (an approach developed in the 2nd Circuit by Judge Friendly). Here is an excerpt from **Morrison v. National Australia Bank Ltd. (2d. Cir. 2008)**:[26]

"   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 ("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... HomeSide's accounting practices spawned this litigation. HomeSide calculated 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.

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[26] 547 F.3d 167 (2nd. Cir. 2008) (Newman, Calabresi & B.D. Parker).

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... 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... This appeal followed....

"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[27]... 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

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

public filings. NAB also incorporated 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."...

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."...

... in SEC v. Berger... (..2003)... 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 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."

The approach in the Supreme Court was quite different. Rather than characterizing the relevant issue as one of jurisdiction, the Supreme Court focused on the territorial reach of the statute. Here are excerpts from the decision in **Morrison v. National Australia Bank Ltd. (Supreme Court 2010):**[28]

Justice Scalia: Before addressing the question presented, we must correct a threshold error in the Second Circuit's analysis. It considered the extraterritorial reach of § 10(b) to raise a question of subject-matter jurisdiction, wherefore it affirmed the District Court's dismissal under Rule 12(b)(1)... In this regard it was following Circuit precedent... The Second Circuit is hardly alone in taking this position..

But to ask what conduct § 10(b) reaches is to ask what conduct § 10(b) prohibits, which is a merits question. Subject-matter jurisdiction, by contrast, "refers to a tribunal's '"power to hear a case."'.. It presents an issue quite separate from the question whether the allegations the plaintiff makes entitle him to relief... The District Court here had jurisdiction.. to adjudicate the question whether § 10(b) applies to National's conduct...

It is a "longstanding principle of American law 'that legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States.'"... This principle represents a canon of construction, or a presumption about a statute's meaning, rather than a limit upon Congress's power to legislate.. It rests on the perception that Congress ordinarily legislates with respect to domestic, not foreign matters.. Thus, "unless there is the affirmative intention of the Congress clearly expressed" to give a statute extraterritorial effect, "we must presume it is primarily concerned with domestic conditions.".. The canon or presumption applies regardless of whether there is a risk of conflict between the American statute

[28] 130 S. Ct. 2869 (S.Ct. 2010).

and a foreign law... When a statute gives no clear indication of an extraterritorial application, it has none.

Despite this principle of interpretation, long and often recited in our opinions, the Second Circuit believed that, because the Exchange Act is silent as to the extraterritorial application of § 10(b), it was left to the court to "discern" whether Congress would have wanted the statute to apply...

This disregard of the presumption against extraterritoriality did not originate with the Court of Appeals panel in this case. It has been repeated over many decades by various courts of appeals in determining the application of the Exchange Act, and § 10(b) in particular, to fraudulent schemes that involve conduct and effects abroad. That has produced a collection of tests for divining what Congress would have wanted, complex in formulation and unpredictable in application.

As of 1967, district courts at least in the Southern District of New York had consistently concluded that, by reason of the presumption against extraterritoriality, § 10(b) did not apply when the stock transactions underlying the violation occurred abroad... Schoenbaum v. Firstbrook... involved the sale in Canada of the treasury shares of a Canadian corporation whose publicly traded shares.. were listed on both the American Stock Exchange and the Toronto Stock Exchange. Invoking the presumption against extraterritoriality, the court held that § 10(b) was inapplicable (though it incorrectly viewed the defect as jurisdictional)... The decision in Schoenbaum was reversed, however, by a Second Circuit opinion which held that "neither the usual presumption against extraterritorial application of legislation nor the specific language.. show Congressional intent to preclude application of the Exchange Act to transactions regarding stocks traded in the United States which are effected outside the United States....".. It sufficed to apply § 10(b) that, although the transactions in treasury shares took place in Canada, they affected the value of the common shares publicly traded in the United States.. Application of § 10(b), the Second Circuit found, was "necessary to protect American investors"..

The Second Circuit took another step with Leasco Data Processing Equip. Corp. v. Maxwell,... which involved an American company that had been fraudulently induced to buy securities in England. There, unlike in Schoenbaum, some of the deceptive conduct had occurred in the United States but the corporation whose securities were traded (abroad) was not listed on any domestic exchange. Leasco said that the presumption against extraterritoriality applies only to matters over which the United States would not have prescriptive jurisdiction... Congress had prescriptive jurisdiction to regulate the deceptive conduct in this country, the language of the Act could be read to cover that conduct, and the court concluded that "if Congress had thought about the point," it would have wanted § 10(b) to apply...

With Schoenbaum and Leasco on the books, the Second Circuit had excised the presumption against extraterritoriality from the jurisprudence of § 10(b) and replaced it with the inquiry whether it would be reasonable (and hence what Congress would have wanted) to apply the statute to a given situation. As long as there was prescriptive jurisdiction to regulate, the Second Circuit explained, whether to apply § 10(b) even to "predominantly foreign" transactions became a matter of whether a court thought Congress "wished the precious resources of United States courts and law enforcement agencies to be devoted to them rather than leave the problem to foreign countries." Bersch v. Drexel Firestone, Inc....

The Second Circuit had thus established that application of § 10(b) could be premised upon

either some effect on American securities markets or investors (Schoenbaum) or significant conduct in the United States (Leasco). It later formalized these two applications into (1) an "effects test," "whether the wrongful conduct had a substantial effect in the United States or upon United States citizens," and (2) a "conduct test," "whether the wrongful conduct occurred in the United States." SEC v. Berger... These became the north star of the Second Circuit's § 10(b) jurisprudence, pointing the way to what Congress would have wished. Indeed, the Second Circuit declined to keep its two tests distinct on the ground that "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." Itoba Ltd. v. Lep Group PLC... The Second Circuit never put forward a textual or even extratextual basis for these tests. As early as Bersch, it confessed that "if we were asked to point to language in the statutes, or even in the legislative history, that compelled these conclusions, we would be unable to respond"..

As they developed, these tests were not easy to administer. The conduct test was held to apply differently depending on whether the harmed investors were Americans or foreigners: When the alleged damages consisted of losses to American investors abroad, it was enough that acts "of material importance" performed in the United States "significantly contributed" to that result; whereas those acts must have "directly caused" the result when losses to foreigners abroad were at issue.. And "merely preparatory activities in the United States" did not suffice "to trigger application of the securities laws for injury to foreigners located abroad."... This required the court to distinguish between mere preparation and using the United States as a "base" for fraudulent activities in other countries.... But merely satisfying the conduct test was sometimes insufficient without "'some additional factor tipping the scales'" in favor of the application of American law... District courts have noted the difficulty of applying such vague formulations... There is no more damning indictment of the "conduct" and "effects" tests than the Second Circuit's own declaration that "the presence or absence of any single factor which was considered significant in other cases... is not necessarily dispositive in future cases." IIT v. Cornfeld...

Other Circuits embraced the Second Circuit's approach, though not its precise application...

At least one Court of Appeals has criticized this line of cases and the interpretive assumption that underlies it...

Commentators have criticized the unpredictable and inconsistent application of § 10(b) to transnational cases... Some have challenged the premise underlying the Courts of Appeals' approach, namely that Congress did not consider the extraterritorial application of § 10(b) (thereby leaving it open to the courts, supposedly, to determine what Congress would have wanted).... Others, more fundamentally, have noted that using congressional silence as a justification for judge-made rules violates the traditional principle that silence means no extraterritorial application...

The criticisms seem to us justified. The results of judicial-speculation-made-law -- divining what Congress would have wanted if it had thought of the situation before the court -- demonstrate the wisdom of the presumption against extraterritoriality. Rather than guess anew in each case, we apply the presumption in all cases, preserving a stable background against which Congress can legislate with predictable effects.

..Rule 10b-5, the regulation under which petitioners have brought suit, was promulgated under § 10(b), and "does not extend beyond conduct encompassed by § 10(b)'s prohibition.".. Therefore,

if § 10(b) is not extraterritorial, neither is Rule 10b-5...
On its face, § 10(b) contains nothing to suggest it applies abroad... Subsection 30(a) contains what § 10(b) lacks: a clear statement of extraterritorial effect. Its explicit provision for a specific extraterritorial application would be quite superfluous if the rest of the Exchange Act already applied to transactions on foreign exchanges -- and its limitation of that application to securities of domestic issuers would be inoperative. Even if that were not true, when a statute provides for some extraterritorial application, the presumption against extraterritoriality operates to limit that provision to its terms... No one claims that § 30(a) applies here.
The concurrence claims we have impermissibly narrowed the inquiry in evaluating whether a statute applies abroad, citing for that point the dissent in Aramco... But we do not say, as the concurrence seems to think, that the presumption against extraterritoriality is a "clear statement rule,".. if by that is meant a requirement that a statute say "this law applies abroad." Assuredly context can be consulted as well. But whatever sources of statutory meaning one consults to give "the most faithful reading" of the text.. there is no clear indication of extraterritoriality here... In short, there is no affirmative indication in the Exchange Act that § 10(b) applies extraterritorially, and we therefore conclude that it does not.
.. Petitioners argue that the conclusion that § 10(b) does not apply extraterritorially does not resolve this case. They contend that they seek no more than domestic application anyway, since Florida is where HomeSide and its senior executives engaged in the deceptive conduct of manipulating HomeSide's financial models; their complaint also alleged that Race and Hughes made misleading public statements there. This is less an answer to the presumption against extraterritorial application than it is an assertion -- a quite valid assertion -- that that presumption here (as often) is not self-evidently dispositive, but its application requires further analysis. For it is a rare case of prohibited extraterritorial application that lacks all contact with the territory of the United States. But the presumption against extraterritorial application would be a craven watchdog indeed if it retreated to its kennel whenever some domestic activity is involved in the case. The concurrence seems to imagine just such a timid sentinel,... but our cases are to the contrary. In Aramco,[29] for example, the Title VII plaintiff had been hired in Houston, and was an American citizen... The Court concluded, however, that neither that territorial event nor that relationship was the "focus" of congressional concern.. but rather domestic employment....
Applying the same mode of analysis here, we think that the focus of the Exchange Act is not upon the place where the deception originated, but upon purchases and sales of securities in the United States. Section 10(b) does not punish deceptive conduct, but only deceptive conduct "in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered."... Those purchase-and-sale transactions are the objects of the statute's solicitude. It is those transactions that the statute seeks to "regulate,"... it is parties or prospective parties to those transactions that the statute seeks to "protec[t],"... And it is in our

[29] In EEOC v. Arabian American Oil Co., 499 U.S. 244 (1991) the US Supreme Court was presented with a claim by a naturalized United States citizen born in Lebanon and working in Saudi Arabia, that his termination by his employer, Arabian American Oil Company, a Delaware corporation violated Title VII of the Civil Rights Act of 1964. The Court held that Tile VII did not apply extraterritorially to regulate the employment practices of United States firms employing US citizens abroad.

view only transactions in securities listed on domestic exchanges, and domestic transactions in other securities, to which § 10(b) applies.

The primacy of the domestic exchange is suggested by the very prologue of the Exchange Act, which sets forth as its object "[t]o provide for the regulation of securities exchanges... operating in interstate and foreign commerce and through the mails, to prevent inequitable and unfair practices on such exchanges...." We know of no one who thought that the Act was intended to "regulat[e]" foreign securities exchanges -- or indeed who even believed that under established principles of international law Congress had the power to do so. The Act's registration requirements apply only to securities listed on national securities exchanges...

With regard to securities not registered on domestic exchanges, the exclusive focus on domestic purchases and sales is strongly confirmed by § 30(a) and (b)... The former extends the normal scope of the Exchange Act's prohibitions to acts effecting, in violation of rules prescribed by the Commission, a "transaction" in a United States security "on an exchange not within or subject to the jurisdiction of the United States.".. And the latter specifies that the Act does not apply to "any person insofar as he transacts a business in securities without the jurisdiction of the United States," unless he does so in violation of regulations promulgated by the Commission "to prevent evasion [of the Act]."... Under both provisions it is the foreign location of the transaction that establishes (or reflects the presumption of) the Act's inapplicability, absent regulations by the Commission.

The same focus on domestic transactions is evident in the Securities Act of 1933.. enacted by the same Congress as the Exchange Act, and forming part of the same comprehensive regulation of securities trading... That legislation makes it unlawful to sell a security, through a prospectus or otherwise, making use of "any means or instruments of transportation or communication in interstate commerce or of the mails," unless a registration statement is in effect... The Commission has interpreted that requirement "not to include... sales that occur outside the United States."..

Finally,.we reject the notion that the Exchange Act reaches conduct in this country affecting exchanges or transactions abroad for the same reason that Aramco rejected overseas application of Title VII to all domestically concluded employment contracts or all employment contracts with American employers: The probability of incompatibility with the applicable laws of other countries is so obvious that if Congress intended such foreign application "it would have addressed the subject of conflicts with foreign laws and procedures."... Like the United States, foreign countries regulate their domestic securities exchanges and securities transactions occurring within their territorial jurisdiction. And the regulation of other countries often differs from ours as to what constitutes fraud, what disclosures must be made, what damages are recoverable, what discovery is available in litigation, what individual actions may be joined in a single suit, what attorney's fees are recoverable, and many other matters... The Commonwealth of Australia, the United Kingdom of Great Britain and Northern Ireland, and the Republic of France have filed amicus briefs in this case. So have (separately or jointly) such international and foreign organizations as the International Chamber of Commerce, the Swiss Bankers Association, the Federation of German Industries, the French Business Confederation, the Institute of International Bankers, the European Banking Federation, the Australian Bankers' Association, and the Association Francaise des Entreprises Privees. They all complain of the interference with

foreign securities regulation that application of § 10(b) abroad would produce, and urge the adoption of a clear test that will avoid that consequence. The transactional test we have adopted -- whether the purchase or sale is made in the United States, or involves a security listed on a domestic exchange -- meets that requirement.
.. The Solicitor General suggests a different test, which petitioners also endorse: "[A] transnational securities fraud violates [§]10(b) when the fraud involves significant conduct in the United States that is material to the fraud's success."... Neither the Solicitor General nor petitioners provide any textual support for this test. The Solicitor General sets forth a number of purposes such a test would serve: achieving a high standard of business ethics in the securities industry, ensuring honest securities markets and thereby promoting investor confidence, and preventing the United States from becoming a "Barbary Coast" for malefactors perpetrating frauds in foreign markets... But it provides no textual support for the last of these purposes, or for the first two as applied to the foreign securities industry and securities markets abroad. It is our function to give the statute the effect its language suggests, however modest that may be; not to extend it to admirable purposes it might be used to achieve.
If, moreover, one is to be attracted by the desirable consequences of the "significant and material conduct" test, one should also be repulsed by its adverse consequences. While there is no reason to believe that the United States has become the Barbary Coast for those perpetrating frauds on foreign securities markets, some fear that it has become the Shangri-La of class-action litigation for lawyers representing those allegedly cheated in foreign securities markets....
The Solicitor General points out that the "significant and material conduct" test is in accord with prevailing notions of international comity. If so, that proves that if the United States asserted prescriptive jurisdiction pursuant to the "significant and material conduct" test it would not violate customary international law; but it in no way tends to prove that that is what Congress has done....
Section 10(b) reaches the use of a manipulative or deceptive device or contrivance only in connection with the purchase or sale of a security listed on an American stock exchange, and the purchase or sale of any other security in the United States. This case involves no securities listed on a domestic exchange, and all aspects of the purchases complained of by those petitioners who still have live claims occurred outside the United States...

Justice Stevens, with whom Justice Ginsburg joins, concurring in the judgment:
While I agree that petitioners have failed to state a claim on which relief can be granted, my reasoning differs from the Court's. I would adhere to the general approach that has been the law in the Second Circuit, and most of the rest of the country, for nearly four decades.
.. Today the Court announces a new "transactional test,".. for defining the reach of § 10(b)... and SEC Rule 10b-5..: Henceforth, those provisions will extend only to "transactions in securities listed on domestic exchanges... and domestic transactions in other securities,".. If one confines one's gaze to the statutory text, the Court's conclusion is a plausible one. But the federal courts have been construing § 10(b) in a different manner for a long time, and the Court's textual analysis is not nearly so compelling, in my view, as to warrant the abandonment of their doctrine.
The text and history of § 10(b) are famously opaque on the question of when, exactly, transnational securities frauds fall within the statute's compass. As those types of frauds became

more common in the latter half of the 20th century, the federal courts were increasingly called upon to wrestle with that question. The Court of Appeals for the Second Circuit, located in the Nation's financial center, led the effort. Beginning in earnest with Schoenbaum v. Firstbrook,.. that court strove, over an extended series of cases, to "discern" under what circumstances "Congress would have wished the precious resources of the United States courts and law enforcement agencies to be devoted to [transnational] transactions,"... Relying on opinions by Judge Henry Friendly, the Second Circuit eventually settled on a conduct-and-effects test. This test asks "(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.".. Numerous cases flesh out the proper application of each prong.

The Second Circuit's test became the "north star" of § 10(b) jurisprudence.. not just regionally but nationally as well. With minor variations, other courts converged on the same basic approach... Neither Congress nor the Securities Exchange Commission (Commission) acted to change the law. To the contrary, the Commission largely adopted the Second Circuit's position in its own adjudications..

In light of this history, the Court's critique of the decision below for applying "judge-made rules" is quite misplaced.. This entire area of law is replete with judge-made rules, which give concrete meaning to Congress' general commands. "When we deal with private actions under Rule 10b-5," then-Justice Rehnquist wrote many years ago, "we deal with a judicial oak which has grown from little more than a legislative acorn." Blue Chip Stamps v. Manor Drug Stores... The "'Mother Court'" of securities law tended to that oak.. One of our greatest jurists -- the judge who, "without a doubt, did more to shape the law of securities regulation than any [other] in the country"[30] -- was its master arborist.

The development of § 10(b) law was hardly an instance of judicial usurpation. Congress invited an expansive role for judicial elaboration when it crafted such an open-ended statute in 1934. And both Congress and the Commission subsequently affirmed that role when they left intact the relevant statutory and regulatory language, respectively, throughout all the years that followed... Unlike certain other domains of securities law, this is "a case in which Congress has enacted a regulatory statute and then has accepted, over a long period of time, broad judicial authority to define substantive standards of conduct and liability," and much else besides...

This Court has not shied away from acknowledging that authority. We have consistently confirmed that, in applying § 10(b) and Rule 10b-5, courts may need "to flesh out the portions of the law with respect to which neither the congressional enactment nor the administrative regulations offer conclusive guidance.".. And we have unanimously "recogniz[ed] a judicial authority to shape... the 10b-5 cause of action," for that is a task "Congress has left to us.".... Indeed, we have unanimously endorsed the Second Circuit's basic interpretive approach to § 10(b) -- ridiculed by the Court today -- of striving to "divin[e] what Congress would have wanted," "Our task," we have said, is "to attempt to infer how the 1934 Congress would have addressed the issue."...

Thus, while the Court devotes a considerable amount of attention to the development of the case law.. it draws the wrong conclusions. The Second Circuit refined its test over several decades and

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[30] This is a reference to Judge Friendly.

dozens of cases, with the tacit approval of Congress and the Commission and with the general assent of its sister Circuits. That history is a reason we should give additional weight to the Second Circuit's "judge-made" doctrine, not a reason to denigrate it. "The longstanding acceptance by the courts, coupled with Congress' failure to reject [its] reasonable interpretation of the wording of § 10(b),... argues significantly in favor of acceptance of the [Second Circuit] rule by this Court."..

.. The Court's other main critique of the Second Circuit's approach -- apart from what the Court views as its excessive reliance on functional considerations and reconstructed congressional intent -- is that the Second Circuit has "disregard[ed]" the presumption against extraterritoriality... It is the Court, however, that misapplies the presumption, in two main respects.

First, the Court seeks to transform the presumption from a flexible rule of thumb into something more like a clear statement rule. We have been here before. In the case on which the Court primarily relies,.. Aramco, Chief Justice Rehnquist's majority opinion included a sentence that appeared to make the same move.... Justice Marshall, in dissent, vigorously objected...

Yet even Aramco -- surely the most extreme application of the presumption against extraterritoriality in my time on the Court -- contained numerous passages suggesting that the presumption may be overcome without a clear directive... And our cases both before and after Aramco make perfectly clear that the Court continues to give effect to "all available evidence about the meaning" of a provision when considering its extraterritorial application, lest we defy Congress' will... Contrary to Justice Scalia 's personal view of statutory interpretation, that evidence legitimately encompasses more than the enacted text. Hence, while the Court's dictum that "[w]hen a statute gives no clear indication of an extraterritorial application, it has none,".. makes for a nice catchphrase, the point is overstated. The presumption against extraterritoriality can be useful as a theory of congressional purpose, a tool for managing international conflict, a background norm, a tiebreaker. It does not relieve courts of their duty to give statutes the most faithful reading possible.

Second, and more fundamentally, the Court errs in suggesting that the presumption against extraterritoriality is fatal to the Second Circuit's test. For even if the presumption really were a clear statement (or "clear indication,"..) rule, it would have only marginal relevance to this case. It is true, of course, that "this Court ordinarily construes ambiguous statutes to avoid unreasonable interference with the sovereign authority of other nations,".. and that, absent contrary evidence, we presume "Congress is primarily concerned with domestic conditions,"... Accordingly, the presumption against extraterritoriality "provides a sound basis for concluding that Section 10(b) does not apply when a securities fraud with no effects in the United States is hatched and executed entirely outside this country." Brief for United States as Amicus Curiae. But that is just about all it provides a sound basis for concluding. And the conclusion is not very illuminating, because no party to the litigation disputes it. No one contends that § 10(b) applies to wholly foreign frauds.

Rather, the real question in this case is how much, and what kinds of, domestic contacts are sufficient to trigger application of § 10(b). In developing its conduct-and-effects test, the Second Circuit endeavored to derive a solution from the Exchange Act's text, structure, history, and purpose. Judge Friendly and his colleagues were well aware that United States courts "cannot and

should not expend [their] resources resolving cases that do not affect Americans or involve fraud emanating from America."..

The question just stated does not admit of an easy answer. The text of the Exchange Act indicates that § 10(b) extends to at least some activities with an international component, but, again, it is not pellucid as to which ones. The Second Circuit draws the line as follows: § 10(b) extends to transnational frauds "only when substantial acts in furtherance of the fraud were committed within the United States,".. or when the fraud was "'intended to produce'" and did produce "'detrimental effects within'" the United States, Schoenbaum..

This approach is consistent with the understanding shared by most scholars that Congress, in passing the Exchange Act, "expected U.S. securities laws to apply to certain international transactions or conduct."... It is also consistent with the traditional understanding, regnant in the 1930's as it is now, that the presumption against extraterritoriality does not apply "when the conduct [at issue] occurs within the United States," and has lesser force when "the failure to extend the scope of the statute to a foreign setting will result in adverse effects within the United States."... And it strikes a reasonable balance between the goals of "preventing the export of fraud from America," protecting shareholders, enhancing investor confidence, and deterring corporate misconduct, on the one hand, and conserving United States resources and limiting conflict with foreign law, on the other..

Thus, while § 10(b) may not give any "clear indication" on its face as to how it should apply to transnational securities frauds... it does give strong clues that it should cover at least some of them.. And in my view, the Second Circuit has done the best job of discerning what sorts of transnational frauds Congress meant in 1934 -- and still means today -- to regulate. I do not take issue with the Court for beginning its inquiry with the statutory text, rather than the doctrine in the Courts of Appeals.. I take issue with the Court for beginning and ending its inquiry with the statutory text, when the text does not speak with geographic precision, and for dismissing the long pedigree of, and the persuasive account of congressional intent embodied in, the Second Circuit's rule.

Repudiating the Second Circuit's approach in its entirety, the Court establishes a novel rule that will foreclose private parties from bringing § 10(b) actions whenever the relevant securities were purchased or sold abroad and are not listed on a domestic exchange. The real motor of the Court's opinion, it seems, is not the presumption against extraterritoriality but rather the Court's belief that transactions on domestic exchanges are "the focus of the Exchange Act" and "the objects of [its] solicitude.".. In reality, however, it is the "public interest" and "the interests of investors" that are the objects of the statute's solicitude.... And while the clarity and simplicity of the Court's test may have some salutary consequences, like all bright-line rules it also has drawbacks.

Imagine, for example, an American investor who buys shares in a company listed only on an overseas exchange. That company has a major American subsidiary with executives based in New York City; and it was in New York City that the executives masterminded and implemented a massive deception which artificially inflated the stock price -- and which will, upon its disclosure, cause the price to plummet. Or, imagine that those same executives go knocking on doors in Manhattan and convince an unsophisticated retiree, on the basis of material misrepresentations, to invest her life savings in the company's doomed securities. Both of these investors would, under the Court's new test, be barred from seeking relief under § 10(b).

The oddity of that result should give pause. For in walling off such individuals from §10(b), the Court narrows the provision's reach to a degree that would surprise and alarm generations of American investors -- and, I am convinced, the Congress that passed the Exchange Act. Indeed, the Court's rule turns §10(b) jurisprudence (and the presumption against extraterritoriality) on its head, by withdrawing the statute's application from cases in which there is both substantial wrongful conduct that occurred in the United States and a substantial injurious effect on United States markets and citizens...
Some cases involving foreign securities transactions have extensive links to, and ramifications for, this country; this case has Australia written all over it.

Notes and Questions After Morrison

Congress enacted Section 929P of the Dodd-Frank Act soon after the decision in Morrison by amending the Securities Act 1933 and the Securities Exchange Act 1934 providing for "extraterritorial jurisdiction" for federal courts in cases brought by the US or the SEC involving "(1) conduct within the United States that constitutes significant steps in furtherance of the violation, even if the securities transaction occurs outside the United States and involves only foreign investors; or (2) conduct occurring outside the United States that has a foreseeable substantial effect within the United States." The provision suggests that Congress wanted to reverse the decision in cases of official enforcement but the reference to jurisdiction, rather than to the substantive reach of the statutes raises some questions. In the same statute Congress mandated the SEC to study extraterritorial private rights of action.

Justice Stevens saw the majority opinion in Morrison as part of a more general effort to limit litigation under §10(b) and Rule 10b-5, and other cases which rely on the presumption against extraterritoriality also seem to be influenced by similar questions about whether courts in the US should hear cases involving acts outside the US. The US Chamber of Commerce in an amicus brief in the case invoked the idea of increasing litigation in US courts by foreign investors, attracted by features of the US system that made this litigation attractive, and by the efforts of the plaintiffs' bar.

Justice Scalia's opinion states that §10(b) and Rule 10b-5 apply to "transactions in securities listed on domestic exchanges, and domestic transactions in other securities."

Subsequent case law has defined domestic transactions as transactions where the parties incur irrevocable liability in the US, or where title is transferred within the US.[31] But, the irrevocable liability test is not itself a bright-line test, as it "depends on the governing law and the details of the parties' transaction and therefore fails to provide clear answers in some cases."[32] William

[31] Absolute Activist Value Master Fund Ltd. v. Ficeto, 677 F.3d 60 (2d Cir. 2012).

[32] William S. Dodge, *Extraterritorial Application of Federal Securities Law: What Hath Morrison Wrought?* (April 20, 2023). New York University Journal of International Law and Politics (Forthcoming),

Dodge writes:

> Morrison's "transactional test," and Absolute Activist's "irrevocable liability" gloss, have not produced a clear, bright-line rule for unlisted securities. The problem with the rule is not just its fuzziness but also the randomness of its results. For listed securities—on which Choi, Silberman, and Scalia all focused—tying section 10(b) to the location of the exchange makes sense because it coincides with the expectations of the parties and allows them to choose a level of antifraud protection they desire. For unlisted securities, however, there seems to be no good reason why the applicability of section 10(b) should turn on where the buyer signs the subscription agreement or where orders for futures on a foreign stock exchange are matched. Indeed, as Hannah Buxbaum has noted, sellers of securities can manipulate the place of acceptance in ways that are not transparent to buyers, depriving them of the protection of U.S. law without their knowledge or consent.[33]

Even where there are domestic transactions in securities the 2nd Circuit has found that other geographic factors may take those transactions outside the scope of the statute and the Rule.[34] The Parkcentral case involved transactions in security-based swaps relating to shares in Volkswagen and the plaintiffs tried to sue in the US over Porsche's statements disclaiming any intention to acquire VW, which turned out to be false. The Second Circuit found that the VW shares appeared to trade only on foreign exchanges, and the deceptive conduct alleged occurred primarily in Germany, and held that whereas a domestic transaction was necessary to invoke §10(b) and Rule 10b-5, it was not sufficient:

> ... a rule making the statute applicable whenever the plaintiff's suit is predicated on a domestic transaction, regardless of the foreignness of the facts constituting the defendant's alleged violation, would seriously undermine Morrison's insistence that § 10(b) has no extraterritorial application. It would require courts to apply the statute to wholly foreign activity clearly subject to regulation by foreign authorities solely because a plaintiff in the United States made a domestic transaction, even if the foreign defendants were completely unaware of it. Such a rule would inevitably place § 10(b) in conflict with the regulatory laws of other nations... If the domestic execution of the plaintiffs' agreements could alone suffice to invoke § 10(b) liability with respect to the defendants' alleged conduct in this case, then it would subject to U.S. securities laws conduct that occurred in a foreign country, concerning securities in a foreign company, traded entirely on

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Available at SSRN: https://ssrn.com/abstract=4437497, at p 2.

[33] *Id.* at 7.

[34] Parkcentral Global HUB Ltd. v. Porsche Automobile Holdings SE, 763 F.3d 198 (2d Cir. 2014).

> foreign exchanges, in the absence of any congressional provision addressing the incompatibility of U.S. and foreign law nearly certain to arise. That is a result Morrison plainly did not contemplate and that the Court's reasoning does not, we think, permit.[35]

The Parkcentral approach has been rejected by other federal courts,[36] creating a circuit split,[37] which provides an invitation to forum shopping. In addition to raising doctrinal questions about the appropriate interpretation of the Morrison decision, the case raises some normative questions. Where derivative securities transactions are entered into in the US, in circumstances where the issuer of the referenced securities had no involvement in the US transactions, should the issuer be subject to liability for breach of US rules? This issue arises with respect to security based swap transactions as in Parkcentral where the contracting parties agree to make payments based on changes in value of the referenced securities, but also with respect to unsponsored ADRs. ADRs may be issued in the US with the involvement of the issuer of the linked securities, but it is also possible for ADRs to be put on the market in the US without any involvement of the issuer of the underlying securities.

In the Toshiba securities litigation the California District Court denied class certification on the basis that the transaction in which the investors acquired their ADRs involved a triggering event causing irrevocable liability in Japan, when plaintiffs acquired the underlying Toshiba stock there before conversion into ADRs.[38] Purchases of ADRs can happen in two ways: either through purchases of existing ADRs on a US stock exchange or on the over-the-counter market or, as in the Toshiba case, by acquiring shares on a foreign exchange and arranging for the issuance of new ADRs by depositing the foreign-bought shares with a depositary bank.[39] In this second situation, where the Toshiba court focused on where the investors acquired irrevocable liability, it would also make sense to focus on where the seller of the ADRs acquired irrevocable liability, and/or, as Morrison suggests, where title to the ADRs was transferred.[40]

A decision that sought clarity and a simple approach to the question of application of the statute turns out not to work well in a financial context where transactions are complex, rather than

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[35] *Id.* at 215-16.

[36] Stoyas v. Toshiba Corp., 896 F. 3d 933 (9th Cir. 2018).

[37] *Cf.* Laydon v. Coöperatieve Rabobank U.A. 51 F. 4th 476 (2nd Cir. 2022)(holding the Commodity Exchange Act does not apply to futures contracts traded on U.S. exchanges that are tied to the values of foreign commodities).

[38] Stoyas v. Toshiba Corp., No. 2:15-cv-04194 DDP-JC, 2022 WL 80469, at *3 (C.D. Cal. Jan. 7, 2022).

[39] Sheet Metal Workers National Pension Fund v. Aktiengesellschaft (ND California 2023).

[40] *Id*.

simple, and when it is hard to identify what is and is not a domestic transaction.

A 2019 article argued that Morrison did not change the litigation environment for foreign issuers and should really be seen as a decision on standing rather than on extraterritoriality.[41] The authors said that Morrison may have prevented global class actions, but these were rare in any case before Morrison.

[41] Robert P. Bartlett, Matthew D. Cain, Jill E. Fisch & Steven Davidoff Solomon, *The Myth of Morrison: Securities Fraud Litigation Against Foreign Issuers* (2019). Business Lawyer, Vol. 74, p. 1967, 2019, UC Berkeley Public Law Research Paper, U of Penn, Inst for Law & Econ Research Paper No. 18-34, Available at SSRN: https://ssrn.com/abstract=3283527 or http://dx.doi.org/10.2139/ssrn.3283527 .