SECURITIES PIRATES: WHY A MORE EXPANSIVE BASIS FOR JURISDICTION OVER TRANSNATIONAL SECURITIES FRAUD WILL PREVENT THE UNITED STATES FROM TURNING INTO THE BARBARY COAST

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INTRODUCTION

In an ever-expanding global economy where securities are being purchased in domestic and foreign markets, questions regarding the scope of regulations are particularly ripe. The regulation of a particular subset of transnational securities, known as "foreign cubed" securities, has garnered a great deal of attention.[1] Foreign cubed securities litigation generally entails actions against foreign issuers by a class of foreign plaintiffs who purchased securities on a foreign exchange and now wish to bring those actions in United States courts based upon United States securities laws.[2] The jurisdictional issues involved in foreign cubed securities affect both class actions by foreign plaintiffs and the Securities and Exchange Commission's (SEC's) ability to regulate the market for fraudulent acts.

Under SEC rule 10b-5, it is "unlawful for any person . . . by the use of any means or instrumentality of interstate commerce,[3] or of the mails or of any facility of any national securities exchange, [t]o employ any device, scheme, or artifice to defraud."[4] Additionally, the rule prohibits the use of interstate commerce "[t]o 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."[5] Lastly, the rule also prohibits a person from "engag[ing] 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."[6] The difficulty with transnational securities fraud cases lies in the fact that neither Congress nor the Supreme Court has addressed the extent of rule 10b-5's jurisdictional reach in its oversight of fraud on the market. Rule 10b-5 does not specify a limitation on its application because it applies to any transaction connected to the purchase or sale of a security.[7] The Securities Act of 1933 and the Securities Exchange Act of

1. *See* Stuart M. Grant & Diane Zilka, *The Role of Foreign Investors in Federal Securities Class Actions*, *in* SECURITIES LITIGATION & ENFORCEMENT INSTITUTE 2004, at 91, 96 (PLI Corp. Law & Practice, Course Handbook Series No. B-1442, 2004) (explaining the colloquially coined term *foreign cubed* as actions involving plaintiffs who are "foreign investors who have purchased foreign securities on foreign exchanges").

2. *See* Morrison v. Nat'l Austl. Bank Ltd., 547 F.3d 167, 172 (2d Cir. 2008) (explaining the general elements of a foreign cubed securities action).

3. *See* 15 U.S.C. § 78c(a)(17) (2006) (defining *interstate commerce* as "trade, commerce, transportation, or communication among the several States, or between any foreign country and any State, or between any State and any place or ship outside thereof").

4. 17 C.F.R. § 240.10b-5(a) (2009).

5. 17 C.F.R. § 240.10b-5(b).

6. 17 C.F.R. § 240.10b-5(c).

7. *See* 15 U.S.C. § 78c(a)(14) (defining *sale* as "any contract to sell or otherwise dispose of [securities]"); Hannah L. Buxbaum, *Multinational Class Actions Under Federal Securities Law: Managing Jurisdictional Conflict*, 46 COLUM. J. TRANSNAT'L L. 14, 19 (2007) (explaining that the broad reach of rule 10b-5 means that it applies whenever U.S.

1934 (the Acts), however, both contain language indicating congressional intent that they apply to both interstate and foreign commerce.[8] Unfortunately, Congress has not set forth the scope of this jurisdiction, thus leaving the difficult task for the Judiciary.[9]

This Comment will examine the treatment of jurisdictional issues in transnational securities fraud cases by various circuits and will discuss how each varying test affects the SEC's ability to regulate the securities market for fraudulent actions. Part I provides background information regarding the judicially developed conduct and effects tests for determining transnational securities fraud jurisdiction and describes how the application of these tests has varied from one circuit to another. Part II of this Comment compares the different judicial tests to the test proposed by the SEC and discusses which of these tests will afford the SEC the broadest ability to pursue its mandate of regulating the market for fraudulent activity. Part III explores the importance of choosing a solid standard for courts to apply and the reason the Supreme Court should clarify the standard for jurisdiction. Lastly, this Comment will argue that the Supreme Court should consider adopting two sets of rules for determinations of extraterritorial jurisdiction: one for SEC enforcement against fraud, which is quintessential to preventing rampant fraudulent activity in the United States, and another for private-plaintiff class actions, which are remedial and have fueled some of the main contentions against the broader reading of the jurisdictional tests. For SEC enforcement, the Supreme Court should adopt the test proposed by the SEC because it will allow for more-efficient monitoring of foreign fraudulent activity without overdeterring foreign commerce with the United States while contemporaneously limiting the possible abuses of United States securities laws by foreign class actions.[10]

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mail or phone service is used, and that this situation is present in virtually every case involving some contact with the United States, and presenting the major question of how to limit the application of U.S. law in cross-border cases, especially when weighing the varying concerns the courts have, which range from policy reasons for deterring fraud to judicial economy).

8. *See* SEC v. Kasser, 548 F.2d 109, 114 & n.21 (3d Cir. 1977) (stating that the term *interstate commerce* in both Acts entails any trade, commerce, transportation, and communication with "any foreign country" and is thus not restricted to merely commerce within the United States).

9. *See id.* at 114 (explaining how the Acts use relatively broad language when addressing the scope of jurisdiction).

10. *See* Phyllis Diamond, *High Court Seeks SG's Views in "Foreign-Cubed" Securities Controversy*, SEC. L. DAILY, June 2, 2009, http://news.bna.com/sdln/SDLNWB/split_display.adp?fedfid=12894533&vname=sldbulallissues&fcn=1&wsn=503234000&fn=12894533&split=0 (explaining that the United States Chamber of Commerce and the Securities Industry and Financial Markets Association argued in amicus briefs that allowing jurisdiction over transnational securities cases would create a "virtual 'Exhibit A' for any foreign jurisdiction seeking to demonstrate, for its competitive advantage," that doing business with the United States would be detrimental,

I. JUDICIAL ATTEMPTS AT CREATING A TEST FOR TRANSNATIONAL SECURITIES JURISDICTION

A. Development of Jurisdiction for Transnational Securities Fraud

The determination of a test that would impose United States laws upon foreign companies inherently requires a discussion of policy.[11] The major policy concern is the balance between preventing the United States from becoming a haven for fraudulent activity by foreign companies and the effect a United States court judgment would realistically have upon foreign countries.[12] Judge Friendly and subsequent judges have found that if the test for jurisdiction were too strict or were a bright-line rule against jurisdiction, it would lead to a situation where foreign companies would view the United States as a country that fosters the deception of investors abroad.[13] If the test for jurisdiction were too lenient and allowed

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and that heavy regulation would discourage foreign companies from bringing their business into the United States due to fear of overregulation). *See generally* Margaret V. Sachs, *The International Reach of Rule 10b-5: The Myth of Congressional Silence*, 28 COLUM. J. TRANSNAT'L L. 677 (1990) (arguing that Congress understood the international nature of the times from the 1920s onward and that their subsequent enactment of the Securities Act of 1933 and the Securities Exchange Act of 1934 would reflect whether Congress felt these Acts should extend beyond the borders of the United States or if the Acts were designed solely to combat fraud committed against American investors trading on U.S. stock exchanges).

11. *See Kasser*, 548 F.2d at 116 (asserting that policy must come into discussion when determining transnational securities cases because rule 10b-5 is silent on the extent of jurisdiction, thus the court must weigh multiple United States policies to make a proper assessment).

12. *See* Bersch v. Drexel Firestone, Inc., 519 F.2d 974, 987 & n.29 (2d Cir. 1975) (limiting the application of its holding to suits by the SEC or by named foreign plaintiffs, thus potentially excluding class action lawsuits due to additional problems that would arise in judgments for class actions as opposed to regulation within United States borders); IIT v. Vencap, Ltd., 519 F.2d 1001, 1018 n.31 (2d Cir. 1975) (noting that class actions may stand differently primarily due to the likelihood that "a very small tail may be wagging an elephant" which leads to doubt that a judgment in an American court would protect defendants elsewhere since defendants who win a judgment in the United States may ultimately be sued multiple times in the courts of other countries applying their securities laws instead of United States securities laws, thus creating the possibility of conflicting judgments in different countries); *see also* Stephen J. Choi & Linda J. Silberman, *Transnational Litigation and Global Securities Class-Action Lawsuits*, 2009 WIS. L. REV. 465, 466–68 (discussing the uncertainty that arises from the calculus of prescriptive jurisdiction due to whether a U.S. class action judgment or settlement will be recognized abroad and consideration of the type of alternative remedy that would otherwise be available to the foreign investors since a judgment found in favor of a claimant would have to be enforced either by the foreign country in which the business operates or an injunction of the business that is being conducted in the United States, which may only afford a claimant a minimal recovery of the damages that may be caused by the fraudulent action).

13. *See Kasser*, 548 F.2d at 116 (concluding that a determination of jurisdiction that is too strict would turn the United States into a "Barbary Coast" that harbors international securities "pirates" since there would be a strong incentive to place subsidiaries in the United States to do the dirty work while having the business headquarters in another foreign

jurisdiction to apply too often, then foreign companies, even those not intending to commit fraud, would be significantly discouraged from bringing their business to the United States as the costs and risks of doing business would be too great.[14] Thus, the Judiciary drew a fine line to prevent the wasting of American judicial resources on judgments that would not be honored and, at the same time, to protect the global economy by fostering an environment where the United States would serve as an example for its neighbors by preventing global-scale securities fraud.

Two of the earliest judicial opinions attempting to develop a test for transnational securities subject-matter jurisdiction came from Judge Friendly of the Second Circuit Court of Appeals. These two cases, decided on the same day, led to the development of a case-by-case examination of subject-matter jurisdiction.[15] Subsequent cases eventually refined Judge Friendly's theories and formulated the test for transnational securities fraud jurisdiction—these tests are the conduct and effects tests.

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country where United States securities laws do not apply); *see also Bersch*, 519 F.2d at 987 (explaining that "Congress did not mean the United States to be used as a base for fraudulent securities schemes even when the victims are foreigners" because allowing a fraudulent base would ultimately lead to fraud in the global economy); *IIT*, 519 F.2d at 1017–18 (positing a comparison of how the United States "would surely look askance if one of [its] neighbors stood by silently and permitted misrepresented securities to be poured into the United States" as those securities would quite likely be out of the reach of the United States court system).

14. *See generally* Diamond, *supra* note 10 (describing consequences to foreign investments within the United States if foreign cubed securities regulation was allowed to proceed and how careful consideration must be made before expanding rule 10b-5 to the expanses of foreign securities fraud).

15. *See Bersch*, 519 F.2d at 977, 992–93 (holding that in the case where defendants were part of a Canadian corporation, federal securities laws apply to losses from sales of securities to American residents in the United States, whether or not acts or culpable failures to act of material importance occurred in the United States, while limiting its application of jurisdiction to situations where Americans are injured when the fraudulent activities within the United States were merely preparatory); *IIT*, 519 F.2d at 1003, 1017–18 (explaining that in this case, where an international investment trust organized under the laws of Luxembourg defrauded an international investment group, the application of securities laws should be extended to transnational transactions beyond prior decisions because "[if] there would be subject matter jurisdiction over a suit by the SEC to prevent the concoction of securities frauds in the United States for export, there would also seem to be jurisdiction over a suit for damages or rescission by a defrauded foreign individual"). *See generally* Buxbaum, *supra* note 7, at 18–21 (explaining the background and development of transnational securities subject-matter jurisdiction through an examination of congressional intent when writing the Securities Act of 1933 and the Securities Exchange Act of 1934, the wording of rule 10b-5, and the attempts by the district courts in establishing a workable test for determining subject-matter jurisdiction for transnational securities fraud); Choi & Silberman, *supra* note 12, at 468–72 (discussing the development of subject-matter jurisdiction for transnational securities cases specifically in regard to class actions brought by foreign plaintiffs under United States securities laws including a comparison of the two most recent cases in the Second Circuit that have applied the conduct test and the effects test for the determination of transnational securities fraud jurisdiction).

B. Effects Test

The effects test questions whether the wrongful conduct had a substantial effect in the United States or upon United States citizens.[16] The United States has a strong incentive to protect its own citizens from fraudulent investments regardless of where the securities are located. This test was developed initially to protect domestic investors who had purchased foreign securities on American exchanges and to protect the domestic securities market from the effects of improper foreign transactions in American securities.[17] Generally, the effects test is a strong basis for jurisdiction over transnational securities; however, it is limited to the extent that the effects must be detrimental to specific interests within the United States—the mere claim of a general reduction of confidence in United States markets is not enough.[18]

C. Conduct Test

The conduct test focuses on whether the activities in the United States were more than merely preparatory to a fraud.[19] Additionally, the test questions whether the culpable acts or omissions occurring in the United

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16. *See* Morrison v. Nat'l Austl. Bank Ltd., 547 F.3d 167, 171 (2d Cir. 2008) (explaining that the effects test was generally applied together with the conduct test 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") (quoting Itoba Ltd. v. Lep Group PLC, 54 F.3d 118, 122 (2d Cir. 1995)).

17. *See* Schoenbaum v. Firstbrook, 405 F.2d 215 (2d Cir. 1968) (en banc) (developing the effects test); *see also* Buxbaum, *supra* note 7, at 21–22 (stating that "[t]he effects test was first fully articulated in *Schoenbaum*" and was developed due to the United States' prerogative in protecting its citizens from fraudulent transactions including those from foreign companies and also to remove the incentive of moving fraudulent activity into the United States by foreign businesses).

18. *See* Buxbaum, *supra* note 7, at 22–23 (explaining that courts do not allow a broad interpretation for fear that securities laws would be used for litigating general market conditions instead of specific harm suffered by some U.S. party).

19. *See, e.g.*, SEC v. Berger, 322 F.3d 187, 194–95 (2d Cir. 2003) (finding that Berger's actions were not merely preparatory because his creation of false financial information, transmission of that false financial information overseas, and approval of the resulting false financial statements prior to the statements being sent to advisors showed that his actions in the United States were material actions constituting fraud); Itoba Ltd. v. Lep Group PLC, 54 F.3d 118, 124 (2d Cir. 1995) (holding that the continued nondisclosure of the fraudulent statements had a deleterious effect and played as much of a role in the plaintiff's purchases of the stock as the price listings on the London Exchange and NASDAQ, and thus could not be described as incidental or merely preparatory); Psimenos v. E.F. Hutton & Co., 722 F.2d 1041, 1046 (2d Cir. 1983) (explaining the similarity of merely preparatory activity to conduct far removed from the consummation of the fraud and that establishing jurisdiction requires that conduct within the United States directly cause the loss); SEC v. Princeton Econ. Int'l Ltd., 84 F. Supp. 2d 452, 454 (S.D.N.Y. 2000) (explaining that "merely preparatory" fraudulent behavior means that the behavior was an insubstantial or insignificant contributing cause to the losses).

States directly caused losses to investors abroad.[20] Recently, the Second Circuit applied both the conduct test and effects test in *Morrison v. National Australian Bank Ltd.*,[21] in which it reaffirmed the possibility of subject-matter jurisdiction for foreign cubed securities cases if either test were met.[22] The case itself focused primarily on the conduct test, as there was no showing of any effects on American investors based on the actions of National Australian Bank and its subsidiary.[23] The conduct test generally requires a demonstration that the application of United States law to the claims will serve a legitimate United States regulatory interest. Specifically, the conduct test's basis lies with preventing the United States from becoming an area that fosters fraud.[24]

The conduct test has been difficult to apply as multiple circuits have created competing standards regarding the quantity of local conduct necessary to create jurisdiction over predominantly foreign transactions. Currently, the primary standard for the conduct test, reaffirmed in *Morrison*, is whether there was conduct in the United States that directly caused the claimant's losses and whether such conduct was more than merely preparatory to securities fraud conducted elsewhere.[25] Due to competing standards, the Second Circuit requested the SEC's opinion as to the basis for transnational securities jurisdiction. The Second Circuit examined this SEC standard alongside the conduct and effects tests it had traditionally followed. Although these tests have been created to determine the reach of rule 10b-5's provision against fraud, courts have applied these tests inconsistently, which has caused significant confusion as to whether the SEC can regulate.[26] The Seventh Circuit explained the varying

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20. *See Morrison*, 547 F.3d at 171 (explaining that the "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").

21. *Id.*

22. *Id.* at 175.

23. *See id.* at 171 (stating that the appellants were relying solely on the conduct component of the test as there was no contention that National Australia Bank's conduct caused any loss to the United States securities market).

24. *See* SEC v. Kasser, 548 F.2d 109, 116 (3d Cir. 1977) (explaining general United States policy in encouraging proper securities regulation as a model in hopes that other countries will follow the example and set up their own regulatory systems to fight fraudulent securities transactions, thus encouraging the global economy through reciprocal transnational securities regulation and cooperation); Buxbaum, *supra* note 7, at 56–59 (explaining that in addition to deterring fraud in the United States, the conduct test also helps to achieve efficient resolution of disputes that touch multiple jurisdictions, thereby fostering a more conducive environment for transnational securities and commerce).

25. *See Morrison*, 547 F.3d at 171 (examining whether the particular acts or culpable failures to act within the United States directly caused losses to foreign investors abroad); *see also In re* Vivendi Universal, S.A. Sec. Litig., 381 F. Supp. 2d 158, 169 (S.D.N.Y. 2003) (reaffirming the narrow application of the conduct test used by the Second Circuit).

26. *See* Buxbaum, *supra* note 7, at 18–20 (discussing that because Congress and the Supreme Court have not addressed the subject-matter jurisdiction of transnational securities

applications of the conduct test in *Kauthar SDN BHD v. Sternberg*,[27] noting that the predominant difference among the circuits was the degree to which the American-based conduct must be causally related to the fraud and the resultant harm to justify the application of American securities law.[28] The Seventh Circuit divided the different approaches into a restrictive approach, a broad approach, and a balance approach.[29] This confusion has spawned the development of the SEC's proposed rule, which was designed to embody the concepts from the conduct and effects tests while being broader and more consistent in application.[30]

1. Restrictive Approach

In *Zoelsch v. Arthur Andersen & Co.*,[31] the D.C. Circuit used the restrictive approach to interpret the Second Circuit's conduct test.[32] Under the restrictive approach, plaintiffs must prove that the conduct in the United States satisfies the prima facie elements of a securities fraud case under rule 10b-5.[33] A plaintiff must show that "the fraudulent statements or misrepresentations originate[d] in the United States, [were] made with scienter and in connection with the sale or purchase of securities, and . . . cause[d] the harm to those who claim to be defrauded, even though the actual reliance and damages may occur [outside the United States]."[34] The restrictive approach was the narrowest of the conduct tests because its

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litigation, lower courts have inconsistently and unpredictably applied the conduct test and the effects test, leading to added confusion across multiple jurisdictions where some jurisdictions are very expansive in their application while others, i.e., the Second Circuit, apply the tests very narrowly to limit extraterritorial jurisdiction).

27. 149 F.3d 659 (7th Cir. 1998).

28. *See id.* at 665–66 (explaining that the conduct "test" and the effects "test" should really be termed "approaches" for flexibility since the different circuits have been applying the tests inconsistently). The Seventh Circuit then explained that the difficulty with a conduct "test" was that there had not been a sufficiently precise description of the conduct occurring within the United States that ought to be adequate to trigger American regulation of the transaction. *See id.*

29. *See id.*; *see also* Michael J. Calhoun, Comment, *Tension on the High Seas of Transnational Securities Fraud: Broadening the Scope of United States Jurisdiction*, 30 LOY. U. CHI. L.J. 679, 696–98 (1999) (listing various circuit approaches to the conduct test).

30. *See* Brief of the SEC as Amicus Curiae, in Response to the Court's Request, Morrison v. Nat'l Austl. Bank, Ltd., 547 F.3d 167 (2d Cir. 2008) (No. 07-0583-cv) (discussing the inconsistent application of the conduct test and the effects test across circuits, and even within the same circuits, and arguing that the Second Circuit should adopt the SEC's proposed rule).

31. 824 F.2d 27, 30 (D.C. Cir. 1987).

32. *See id.* at 30–32; *see also* Calhoun, *supra* note 29, at 698 n.133 (stating that the U.S. Court of Appeals for the District of Columbia Circuit was the only circuit to use the restrictive analysis to construe the conduct approach).

33. *Zoelsch*, 824 F.2d at 30–31.

34. *Id.* at 31 (citing IIT v. Vencap, 519 F.2d 1001, 1018 (2d Cir. 1975)) (explaining that finding jurisdiction is limited to the perpetration of fraudulent acts themselves).

objective was to ensure the principles of international comity,[35] to avoid waste of judicial economy, and to prevent the creation of numerous cumbersome jurisdictional tests.[36] Ultimately, this approach implies the possibility that American courts should never assert jurisdiction over domestic conduct that causes losses to foreign investors.[37]

2. *Broad Approach*

The Third, Eighth, and Ninth Circuits have adopted the broad approach to the conduct test.[38] Under this approach, courts hold that if there is some conduct in the United States meant to perpetuate fraud, the conduct is sufficient to confer jurisdiction over the fraudulent transaction.[39] The conduct must be material and not mere preparation.[40] The Eighth Circuit suggested that courts must examine the transaction as a whole to determine whether the conduct is significant enough to allow a federal court to exercise jurisdiction because the essential elements of a scheme to defraud may slowly unfold over time and across national borders.[41] In *SEC v. Kasser*,[42] the Third Circuit found that if at least some activity pertaining to

35. *See* Calhoun, *supra* note 29, at 688 (defining *international comity* as "the practice of courtesy and good will that one nation shows for the national interests of another nation"). *International comity* is also defined as "the recognition which one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citizens or of other persons who are under the protection of its laws." Hilton v. Guyot, 159 U.S. 113, 164 (1895).

36. *See Zoelsch*, 824 F.2d at 32 ("When . . . a court is confronted with transactions that on any view are predominantly foreign, it must seek to determine whether Congress would have 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." (quoting Bersch v. Drexel Firestone, Inc., 519 F.2d 974, 985 (2d Cir. 1975))). *See generally* Calhoun, *supra* note 29, at 687–90, 698–700 (explaining the reasoning behind international comity and the presumption against extraterritoriality and how these principles have shaped the support for the restrictive approach).

37. *See Zoelsch*, 824 F.2d at 32 (explaining that if not for the Second Circuit's preeminence in the field of securities law and the court's desire to avoid a multiplicity of jurisdictional tests, the court may have been inclined to never assert jurisdiction over domestic conduct that causes losses to foreign investors because Congress did not think about conduct that contributes to losses abroad in enacting the Securities Exchange Act of 1934).

38. *See* Kauthar SDN BHD v. Sternberg, 149 F.3d 659, 666 (7th Cir. 1998) (explaining that the Third, Eighth, and Ninth Circuits "generally require some lesser quantum of conduct" (citing Robinson v. TCI/US W. Commc'ns, Inc., 117 F.3d 900, 906 (5th Cir. 1997))). *See generally* Calhoun, *supra* note 29, at 700–08 (discussing thoroughly the development and adoption of the broader approach by the Third, Eighth, and Ninth Circuits).

39. *See, e.g.*, SEC v. Kasser, 548 F.2d 109, 114 (3d Cir. 1977).

40. *See id.* at 114–15 (citing IIT v. Vencap, 519 F.2d 1001, 1018 (2d Cir. 1975)).

41. Travis v. Anthes Imperial Ltd., 473 F.2d 515, 523–24, 26 (8th Cir. 1973).

42. 548 F.2d 109 (3d Cir. 1977).

the advancement of a transnational fraud scheme occurs within the United States, then a United States federal court has jurisdiction to hear the case.[43]

3. The Balance Approach

The Second, Fifth, and Seventh Circuits follow the balance approach developed by the Second Circuit. Under the balance approach, a court must weigh the competing interests of market integrity and constitutional limits on judicial jurisdiction.[44] The balance approach requires that the fraudulent conduct in the United States amount to substantial acts relating to the fraud.[45] The domestic conduct must directly cause the plaintiff's loss to establish jurisdiction.[46] The Fifth Circuit found that when conduct in the United States is of material importance to the fraud or directly causes the fraud, then American courts could have jurisdiction to preside over a case of transnational securities fraud.[47] The Seventh Circuit requires that the fraudulent conduct occurring in the United States be a substantial part of the fraud and material to its success.[48]

II. EXAMINATION OF THE SEC'S PROPOSED RULE

A. SEC Proposed Rule from Morrison v. National Australia Bank, Ltd.

The SEC submitted an amicus curiae brief in response to the Second Circuit panel's request for clarification on the SEC's position regarding the extent to which jurisdiction should be extended for transnational securities cases.[49] In its brief, the SEC formulated a standard guarding against

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43. *See id*. at 114 (holding that the court has jurisdiction over an American party even where the only victim of the alleged fraud was a foreign corporation).

44. *See* Calhoun, *supra* note 29, at 708–09 (suggesting that the balancing approach is a middle ground between the two extremes of the restrictive and broad approaches) (citing Kauthar SDN BHD v. Sternberg, 149 F.3d 659, 666 (7th Cir. 1998)).

45. Psimenos v. E.F. Hutton & Co., 722 F.2d 1041, 1045–46 (2d Cir. 1983) (citing IIT v. Vencap, Ltd., 519 F.2d 1001 (2d Cir. 1975)).

46. *See* Bersch v. Drexel Firestone, Inc., 519 F.2d 974, 993 (2d Cir. 1975) (concluding that antifraud provisions of federal securities laws do not apply to losses from sales of securities to foreigners unless the acts within the United States directly caused such losses); *see also* Morrison v. Nat'l Austl. Bank Ltd., 547 F.3d 167, 171 (2d Cir. 2008) (explaining that the determination of whether American activities "directly" caused losses to foreigners is made by comparing "what and how much was done in the United States and . . . what and how much was done abroad").

47. *See* Robinson v. TCI/US W. Commc'ns, Inc., 117 F.3d 900, 903, 907 (5th Cir. 1997) (adding that when the events occurring in the United States are "key events," a United States court may properly exercise its jurisdiction).

48. Kauthar SDN BHD v. Sternberg, 149 F.3d 659, 667 (7th Cir. 1998); *see also supra* notes 11–15 and accompanying text.

49. Brief of the SEC as Amicus Curiae, in Response to the Court's Request, *supra* note 30, at 1–2.

transnational securities fraud, stating that "antifraud provisions of the securities laws apply to transnational frauds that result exclusively or principally in overseas losses if the conduct in the United States is material to the fraud's success and forms a substantial component of the fraudulent scheme."[50] The SEC has pointed out that the inconsistent application of the conduct test and the effects test is based significantly on the Second Circuit's slow deviation into the use of a "substantial portion" or "material" test, which moves away from the "very fine distinctions" required by the rigid conduct and effects tests.[51]

Under the "material" test, antifraud provisions of the securities law apply "when the conduct occurring in the United States directly causes the plaintiff's alleged loss in that the conduct forms a substantial part of the alleged fraud and is material to its success."[52] The SEC asserts that the materiality inquiry would ensure that the domestic conduct would be an integral, thus not an incidental or ancillary, link in the chain of events in the transnational fraud that led to the foreign investor's losses.[53] The materiality test was designed to filter out litigation based upon conduct far removed from the consummation of the fraud.[54]

If materiality is determined, the test then examines the totality of the circumstances to determine if there was a sufficient quantum of conduct that occurred in the United States to "reasonably warrant application of the antifraud provisions in light of the competing policy concerns."[55] Substantiality would be satisfied even where there is limited conduct within the United States if the conduct is "highly significant to the fraud."[56] The SEC believes this test would be a synthesis of the prior Second Circuit decisions discussing transnational securities jurisdiction as well as a

50. *Id*. at 2.

51. *See id*. at 25–27 (observing the district courts' confused application of the controlling test).

52. *See Kauthar*, 149 F.3d at 667 (adopting the Second Circuit conduct test but incorporating "substantial portion" and "material" within the test); *see also* Brief of the SEC as Amicus Curiae, in Response to the Court's Request, *supra* note 30, at 23 (discussing *Kauthar* and noting the Second Circuit's prior use of "material to the completion of the fraud" and "substantial acts in furtherance of the fraud" tests).

53. *See* Brief of the SEC as Amicus Curiae, in Response to the Court's Request, *supra* note 30, at 23–24 (elaborating upon the benefits of clarity and uniformity provided by adoption of the materiality standard).

54. *See* Psimenos v. E. F. Hutton & Co., 722 F.2d 1041, 1046 (2d Cir. 1983) (avoiding the extension of transnational securities fraud jurisdiction to situations where the majority of the fraudulent activity occurred in foreign countries such as what happened in *Bersch*).

55. Brief of the SEC as Amicus Curiae, in Response to the Court's Request, *supra* note 30, at 24.

56. *Id*. (suggesting that "communicating the misrepresentations to foreign investors in or from the United States, masterminding the scheme here, or using the United States as a base to consummate schemes concocted abroad" are potential examples of conduct highly significant to the fraud (citations omitted)).

slightly more expansive test that would allow the court to have a broader ability to find jurisdiction for transnational securities fraud cases.[57]

The SEC's proposed test falls in between the broad approach of the Third, Eighth, and Ninth Circuits and the Second, Fifth, and Seventh Circuits' balance approach. The proposed test borrows the broad approach's overarching concept of requiring some fraudulent conduct within the United States that is not merely preparatory and narrows the test so that it conforms more to the preeminent balance approach test by requiring that the conduct be both material and substantial.[58] By mixing the broader approach with the balance approach, the test becomes an expansive test with well-defined elements necessary to establish jurisdiction.[59]

B. *Brief Facts of* Morrison *and the Second Circuit's Holding*

In *Morrison*, National Australia Bank (NAB), an Australian corporation, traded its ordinary shares exclusively on the London Stock Exchange, Tokyo stock exchange, and the New Zealand stock exchange.[60] NAB did, however, trade its American Depositary Receipts (ADRs) on the New York Stock Exchange.[61] In 1998, NAB acquired HomeSide Lending, an American mortgage service provider located in Florida.[62]

In the first year after the acquisition, HomeSide Lending earned A$313 million[63] in mortgage servicing fees.[64] In 1999, HomeSide Lending earned A$153 million, which contributed about 5.4% of NAB's profits.[65] In 2000, HomeSide Lending earned A$141 million, contributing 4.1% of NAB's profits.[66] In 2001, NAB disclosed that HomeSide Lending's valuation model of mortgage servicing rights (MSRs) had been significantly overstated and NAB would have to adjust[67] the MSRs by $450 million.[68]

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57. *See id*. at 14–19 (examining relevant Second Circuit case law to develop a test that "both addresses the concerns reflected in the Circuit's decisions and offers more uniformity of analysis and predictability of results").

58. *See supra* notes 39–49 and accompanying text (discussing the broad and balancing approaches to the conduct test).

59. *See* Brief of the SEC as Amicus Curiae, in Response to the Court's Request, *supra* note 30, at 23 (explaining that the SEC's formulation builds upon the Second Circuit's balance approach but brings the approaches together in a unified standard that will provide greater guidance to lower courts in resolving future cases).

60. Morrison v. Nat'l Austl. Bank Ltd., 547 F.3d 167, 168 (2d Cir. 2008).

61. *Id*.

62. *Id*. at 168–69.

63. A$ signifies Australian dollars.

64. *Morrison*, 547 F.3d at 169.

65. *Id*.

66. *Id.*

67. *See id*. at 169 (explaining that NAB's "write-down" was a recalculation of its mortgage servicing rights (MSRs), which ultimately restated the amount that the MSRs

By the end of that year, NAB had disclosed an additional $1.75 billion write down of HomeSide Lending's MSRs, resulting in a 13% decline in NAB's ordinary shares and an 11.5% decline in NAB's ADRs.[69] Due to the massive write-downs from the misstatements of HomeSide Lending's MSRs, NAB was required to file an amended 10-Q with the SEC restating its previously issued financial statements in light of its prior adjustments.[70]

The Second Circuit ultimately found that since the claimants did not assert that there was an effect on the U.S. market, the court would only apply the conduct test.[71] The court concluded that there was no subject-matter jurisdiction because although HomeSide Lending was acting in a fraudulent manner by sending misstated accounting information to NAB, ultimately the accounting data was to be filtered by NAB in Australia before being disseminated to its investors.[72] HomeSide Lending's operations were found to be merely preparatory to the fraud that was actually committed outside of the United States because HomeSide Lending did not file financial statements with the United States but sent all of its financial data to NAB to be checked.[73] Thus, NAB was the actual entity committing fraud, as it was their duty to discover the fraudulent misrepresentations of their subsidiaries.[74]

C. *Application of SEC's Proposed Rule to* Morrison

Under the SEC's proposed rule as applied to the facts in *Morrison*, the SEC recommended that there was a basis for jurisdiction.[75] The two main components of the SEC's proposed rule are materiality and substantiality.[76]

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were worth as they had been overvalued as compared to a more accurate market price that was available for its determination).

68. *Id.* (explaining that HomeSide Lending used faulty interest assumptions in calculating its MSRs resulting in NAB incurring a $450 million write-down).

69. *Id.*

70. *Id.* 10-Qs are quarterly filings required by the Securities Exchange Act of 1934 meant to accurately and fairly reflect the transactions and dispositions of the assets of the securities issuer. *See* 15 U.S.C. § 78m(a)(2)–(b)(2)(A) (2006) (requiring the submission of quarterly reports).

71. *Morrison*, 547 F.3d at 170–71, 176.

72. *Id.* at 176–77.

73. *Id.* at 176 (concluding that "actions taken and the actions not taken by NAB in Australia were . . . central to the fraud and more directly responsible for the harm to investors than the manipulation of the numbers in Florida").

74. *See id.* (explaining that due diligence should have been performed at NAB's Australian corporate headquarters because it had the responsibility of overseeing operations, including subsidiary operations, and was a publicly traded parent company whose executives bore ultimate responsibility).

75. *See* Brief of the SEC as Amicus Curiae, in Response to the Court's Request, *supra* note 30, at 30–31 (arguing that "the defendants' domestic conduct was both material to the scheme's success and a substantial part of the alleged fraud").

76. *See supra* notes 50–60 and accompanying text (explaining the requirements of

An examination of the materiality of HomeSide Lending's actions shows that due to its misrepresentations NAB wrote down its profits by approximately $2.2 billion,[77] which resulted in a 13% drop in the price of NAB's ordinary shares.[78] Within the United States, the restatement of its prior earnings caused an 11.5% drop in the ADR price.[79] These price drops demonstrate that HomeSide Lending's omissions constituted a direct link in investor losses.[80]

Additionally, HomeSide Lending's activities in the United States were a substantial, if not pivotal, component of the fraudulent misrepresentations to the foreign investing public. The bulk of the initial misrepresentation occurred within the United States, with the ancillary collection and distribution of the financial information in Australia.[81] The actual location where the fraud and misrepresentation occurred would likely make it a substantial component in the commission of fraud.[82] Even if the information was ultimately disseminated from another country, an integral piece of the fraud was committed within U.S. territory.

III. THE COURTS SHOULD ADOPT THE SEC'S PROPOSED RULE

In June 2009, the *Morrison* investors filed a petition for certiorari with the Supreme Court.[83] The Solicitor General has been invited to submit a brief discussing the United States' position regarding the test for transnational securities jurisdiction.[84] If certiorari is granted, the Supreme Court will be able to examine the circuit splits in the application of the

materiality and substantiality).

77. *See Morrison*, 547 F.3d at 169 (recalling the $450 million and $1.75 billion write-downs in the values of HomeSide's MSRs).

78. *Id*.

79. *Id*.

80. *See* Brief of the SEC as Amicus Curiae, in Response to the Court's Request, *supra* note 30, at 30–31 (explaining that "[w]ithout this domestic misconduct, there would have been no fraudulent release of information in Australia nor a resulting inflation of NAB's stock" and that the scheme was allegedly conceived in Florida where HomeSide Lending "took numerous steps in the United States to perpetrate that scheme by manipulating the assumptions in HomeSide Lending's MSR valuation modes"). Through this manipulation, HomeSide Lending was able to fraudulently value its models and incorporate this information in its Australian parent's financial statements.

81. *Morrison*, 547 F.3d at 171.

82. *See* SEC v. Berger, 322 F.3d 187, 193–95 (2d Cir. 2003) (finding subject-matter jurisdiction under the conduct test where the defendant prepared false statements in the United States, sent those statements to an offshore administrator for calculation, and then disseminated the statements to domestic and foreign investors).

83. *See* Diamond, *supra* note 10.

84. *See* Morrison v. Nat'l Austl. Bank, Ltd., 129 S. Ct. 2762, 2762 (2009) (stating that the Supreme Court had invited the Solicitor General to submit a brief explaining the United States' position regarding jurisdictional issues involved in transnational securities fraud cases).

conduct test and the effects test and weigh the traditional tests with the proposed test set forth by the SEC. If the Supreme Court were to adopt the SEC's proposed rule, it would significantly deter foreign companies from conducting fraudulent activities within the United States. Second, adoption of the SEC's rule would embrace the "materiality" test, which would keep the test consistent with the rules set forth for securities fraud under rule 10b-5. Lastly, adoption of the SEC's proposed rule would solve the inconsistent application of the conduct and effects tests that has spawned cases with very similar factual patterns but yielded completely opposite results.

A. Deterring Fraudulent Activities Within the United States by Foreign Companies

Deterrence of fraudulent activity is a primary and major concern of extending subject-matter jurisdiction to transnational securities fraud cases. As a matter of policy, the Second Circuit's application of the conduct and effects tests and its subsequent holding that there was no basis for jurisdiction creates an incentive for foreign corporations to open subsidiaries within the United States to commit fraud but, at the same time, incorporate in a country that has more-relaxed standards for securities regulation.[85] The narrow reading of the conduct and effects tests would actually create an incentive to defraud within the United States, which undermines the creation of a rule allowing jurisdiction in the first place.[86]

The SEC's more expansive rule would bring more cases within its ability to regulate as its primary function is to effectuate the laws created by the Securities Act of 1933 and the Securities Exchange Acts of 1934. Without this expansive rule, more financial frauds will be perpetuated against investors around the world, and the United States may one day find itself with the same reputation as Antigua.[87] Lenient regulations are generally a double-edged sword in that less regulation may promote an influx of businesses, but those businesses may not be of the type that are

85. *See* SEC v. Kasser, 548 F.2d 109, 116 (3d Cir. 1977) (discussing concerns that an overly strict requirement for subject-matter jurisdiction in transnational securities cases would create an incentive to set up fraud within the United States but may also induce reciprocal responses on the part of other nations who will not regulate against fraud within their own countries).

86. *Id.*

87. *See* Alison Fitzgerald & Michael Forsythe, *Stanford Coaxed $5 Billion as SEC Weighed Powers*, BLOOMBERG.COM, Apr. 16, 2009, http://www.bloomberg.com/apps/news?pid=20670001&sid=aVCxRFrq1FPU# (quoting Jonathan Winer, a State Department official, who stated that being in Antigua should be a "supremo indicator" of fraud and that "[t]here's no reason for somebody to be located there, except to take advantage of bank secrecy laws and lax regulation" much like Berger operating out of Bermuda and possibly Kasser operating out of Canada).

ultimately beneficial.

B. SEC's Materiality Test Maintains Consistency with the Elements for Securities Fraud Under Rule 10b-5

The SEC's use of the word *material* allows for a more consistent application of securities laws. Since domestic securities fraud cases also use "materiality" to determine whether there was fraud, this would provide more guidance for applying the rule. The extension of rule 10b-5's materiality element for fraud to determinations of transnational securities jurisdiction would be consistent with existing U.S. securities laws, which require a showing of materiality.[88] For example, the Supreme Court has found that when pleading a securities fraud case, the claimant must show that the defendant had misrepresented or omitted a "material" fact.[89]

There has been a significant amount of litigation in the domestic securities fraud field, many proceeding to the Supreme Court, where the term *material* has been fleshed out and its meaning clarified.[90] This is unlike the use of the conduct test where the term *preparatory* has not been fully explained, thus causing significant confusion in its application across circuits.[91] The use of materiality essentially embodies the overall purpose

88. Buxbaum, *supra* note 7, at 24–29.

89. *See* Dura Pharm., Inc. v. Broudo, 544 U.S. 336, 341 (2005) (explaining that rule 10b-5 forbids making any untrue statement of material fact or omission of any material fact necessary to ensure the statements made are not misleading). Although private securities litigation is not the main focus of this Comment, it does help to develop a clearer understanding of the differing issues that a private litigant faces as opposed to what the SEC faces when regulating the securities market.

90. *E.g.*, *id.*; *see also In re* Time Warner Inc. Sec. Litig., 9 F.3d 259, 267–68 (2d Cir. 1993) (explaining that undisclosed information is material if there is a substantial likelihood that "disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information available"). Materiality is also used in insider trading cases where insider trading occurs when a corporate insider buys or sells his corporation's securities using material, nonpublic information. *See* United States v. O'Hagan, 521 U.S. 642, 651–52 (1997); *see generally* BLACK'S LAW DICTIONARY 450 (9th ed. 2009) (defining *material* as "having some logical connection with consequential facts").

91. *See* Zoelsch v. Arthur Andersen & Co., 824 F.2d 27, 31 (D.C. Cir. 1987) (explaining that the Third, Eighth, and Ninth Circuits appear to have relaxed the Second Circuit's test by interpreting "conduct that directly causes losses" to mean either domestic conduct that was in furtherance of a fraudulent scheme and was significant with respect to its accomplishment, or the even more permissive Third Circuit test, where *conduct* is defined as significant activity within the United States designed to further a fraudulent scheme); Brief of the SEC as Amicus Curiae, in Response to the Court's Request, *supra* note 30, at 14–15 (explaining that the Second Circuit's conduct test has proven to be problematic to apply as difficulty arises from an apparent shift in emphasis from a test of strict causation to one of materiality of the domestic acts, which lends support for the SEC's proposed rule as there seems to be a difference between the stated conduct test and effects test and the ultimate application of the rules); *see also* Russell J. Weintraub, *The Extraterritorial Application of Antitrust and Securities Laws: An Inquiry into the Utility of a "Choice-of-Law" Approach*, 70 TEX. L. REV. 1799, 1812–13 (1992) (describing the Second

of expanded jurisdiction, as the United States policy for securities regulation is to prevent fraudulent activity within the country.[92]

C. Inconsistent Application of Conduct Test

The SEC's most recent case dealing with transnational securities fraud was *SEC v. Berger*,[93] where the Second Circuit found that under the conduct test there was a sufficient basis for subject-matter jurisdiction.[94] In *Berger*, the defendant was located within the United States but selling securities to foreigners.[95] The defendant's fund, the Manhattan Investment Fund, was located partially within the United States, but all financial statements were sent out to foreign investors from Bermuda.[96] The Second Circuit found that Berger's conduct was not preparatory because the creation and transmission of the false financial information, and approval of the resulting false financial statements later sent to investors, all took place "materially" within the United States.[97]

The fact patterns in *Berger* and *Morrison* are very similar as the fraud in both cases was committed within the United States but the fraudulent financial information was transmitted from the United States to a foreign country to be processed and distributed to investors.[98] In *Berger*, the Second Circuit applied the conduct test and found that although the information was being disseminated from a foreign location, the fraudulent acts originated in the United States—thus the court had subject-matter jurisdiction.[99] In *Morrison*, the court applied the conduct test to NAB and HomeSide Lending and found that since it was NAB's duty to review HomeSide Lending's financial statements under Australian securities laws before distributing the information, the fraudulent conduct in the United

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Circuit's greater impact on transnational securities fraud subject-matter jurisdiction due to its location within the financial center of the country, while other jurisdictions have not been in "lock-step" with the Second Circuit's application of the conduct test and the effects test).

92. *See Zoelsch*, 824 F.2d at 29–30 (providing a historical analysis of the Acts' purposes through an examination of the language of select provisions and congressional intent).

93. 322 F.3d 187 (2d Cir. 2003).

94. *Id*. at 193–94.

95. *Id*. at 188.

96. *Id*. at 189.

97. *See id*. at 189, 195 (explaining that the fraudulent scheme was masterminded and implemented by Berger in the United States even though the business had its headquarters in Bermuda, which was where Berger sent out his fraudulent financials).

98. *See* Morrison v. Nat'l Austl. Bank Ltd., 547 F.3d 167, 169 (2d Cir. 2008) (explaining that statements were prepared in the United States and sent to Australia for distribution); *Berger*, 322 F.3d at 189 (explaining that statements were prepared in the United States and sent to Bermuda for distribution).

99. *Berger*, 322 F.3d at 194–95.

States was only "preparatory."[100] These two scenarios had similar fraudulent conduct yet yielded completely different results because the Second Circuit's balancing approach was ambiguous in its definition and application of the elements necessary to confer jurisdiction.[101]

The balance approach's fact-intensive inquiry cannot provide clear procedural standards for jurisdiction, and this ultimately increases the number of jurisdictional standards in transnational securities cases.[102] The Seventh Circuit's renaming of the conduct "test" to an "approach" is testament to the balance approach's inefficiency at establishing clear procedural standards for circuits to follow.[103] The D.C. Circuit went so far as to say that the balance approach, or any approach that is heavily fact dependent, should not be adopted because experience from extraterritorial application of antitrust laws has demonstrated that fact-dependent jurisdiction tests are difficult to apply and inherently unpredictable.[104] Under the balance approach, the merits of the case will be decided during the determination of jurisdiction because so many facts must be plead in order to establish that any particular case is eligible for jurisdiction in American courts.[105]

Besides the ambiguity of the balance approach, another possible reason for this variation in results derives from a major distinction between these two cases. *Morrison* involved a class action[106] while *Berger* involved SEC regulatory enforcement.[107] Securities class actions present an additional concern for the courts, especially with the added layer that the claimants are entirely foreign.[108] With class actions, additional concerns include whether a judgment by an American court will actually be enforceable in another country and also, if the defendants were to win, whether an

100. *Morrison*, 547 F.3d at 176.

101. *See supra* notes 44–48 and accompanying text (explaining the Second Circuit's balance approach).

102. *See* Calhoun, *supra* note 29, at 724 (arguing why the broader approach should be adopted over the balance approach).

103. *See supra* notes 27–30 and accompanying text (explaining the Seventh Circuit's rationale for choosing "approach" instead of "test").

104. Zoelsch v. Arthur Andersen & Co., 824 F.2d 27, 32 n.2 (D.C. Cir. 1987).

105. *See id*. (stating that balancing tests "present powerful incentives for increased litigation on the jurisdictional issue itself").

106. *See* Morrison v. Nat'l Austl. Bank Ltd., 547 F.3d 167, 169 (2d Cir. 2008) (describing the claimants as a class of foreign investors who purchased NAB's ordinary shares in foreign markets, thus excluding the claimants who had purchased the ADR shares on the New York Stock Exchange).

107. *See* SEC v. Berger, 322 F.3d 187, 189 (2d Cir. 2003) (explaining that the SEC brought this civil enforcement action against Berger alleging violations of various provisions of the federal securities laws).

108. *See* IIT v. Vencap, Ltd., 519 F.2d 1001, 1017 (2d Cir. 1975) (raising concerns about United States courts exercising jurisdiction over extraterritorial schemes that defraud only a small number of United States investors).

American judgment would actually protect the defendants in another country.[109] This opposes the SEC's purpose of enforcing United States securities law.[110] According to Judge Friendly, there may be reason to treat SEC enforcement differently than a foreign securities class action because the SEC is a responsible government agency and will take into account in framing its enforcement actions any foreign policy concerns communicated by the Department of State.[111] Because this Comment addresses only SEC enforcement, a distinction should be made between governmental regulation of securities and private securities class actions, which would exist within the same realm as rule 10b-5 regulations that restrict private securities litigation as opposed to SEC enforcement.

CONCLUSION

The SEC should generally be governed by a distinct set of rules as opposed to private securities class actions. With *Morrison* awaiting a decision regarding certiorari from the Supreme Court, there should be discussion of how to encourage SEC enforcement in the current financial environment, which has shown that the SEC's regulatory powers are, if anything, too limited for effective regulation.[112] As the SEC is hamstrung in its powers, more financial fraud will occur within the borders of the United States while protected by the relaxed regulatory schemes of other countries that may not have the same incentive as the United States in protecting its citizens and reputation from harm.[113]

Ultimately, should the Supreme Court grant certiorari, there is a strong argument to be made that the SEC's proposed rule should be adopted for SEC enforcement if not for private litigation. By adopting the "material" and "substantial component" test, the SEC would be better able to effect the United States' policy against harboring those who wish to defraud. A quick examination of the current financial climate shows that a clear rule needs to be established for the SEC to follow as uncertainties about the extent of its regulatory power have led to a plethora of frauds that have

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109. *Id.* at 1018 n.31.

110. 15 U.S.C. § 78b (2006).

111. *See* Zoelsch v. Arthur Andersen & Co., 824 F.2d 27, 33 n.3 (D.C. Cir. 1987) (stating that a court may feel more comfortable asserting jurisdiction if it knows that foreign policy concerns can be accommodated by the plaintiff and are not left entirely to the court's untutored evaluation).

112. *See* Fitzgerald & Forsythe, *supra* note 87 (explaining how the SEC's time spent weighing whether it had the power to regulate mutual funds that were depositing in offshore accounts led to a four-year period where the Stanford Group was unregulated even though signs of fraudulent activity had emerged which perpetuated into the SEC, also missing the Bernard Madoff Ponzi scheme as regulatory schemes have been unclear for the SEC).

113. *See id*. (stating that the SEC currently has authority to regulate U.S. activities but has no jurisdiction over offshore banks).

only recently surfaced.[114] A clearer rule for the SEC may have allowed it to regulate HomeSide Lending earlier, which could have potentially prevented the 13% price fall and the avoidance of a $2 billion write-down.

114. *See id*. (discussing the SEC's failure to prevent recent frauds perpetrated by Bernard Madoff and Allan Stanford). With the increasing number of massive Ponzi schemes being uncovered, it would seem that increased regulation of hedge funds is underway. Since the Ponzi schemes currently in the media are not truly within the discussion of transnational securities fraud, the implications have not been fully examined. A possible result of the increased regulation of Ponzi schemes in the United States may lead to increased transnational securities regulation as Ponzi schemers will move out of the United States into countries with relaxed regulations but may continue to work out of the United States.