TRANSNATIONAL LITIGATION AND GLOBAL SECURITIES CLASS-ACTION LAWSUITS

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The U.S. securities laws often apply extraterritorially. Courts apply a number of doctrines, including the conduct and effects tests, to determine how far to extend jurisdiction in securities class-action lawsuits involving transnational securities fraud. In determining both jurisdiction and the propriety of a class-action lawsuit, courts often focus on whether foreign jurisdictions will recognize a U.S. class-action judgment and whether there are effective alternative remedies abroad. We focus our analysis on the present extraterritorial regime as applied to securities class-action lawsuits involving foreign issuers and, at least in part, foreign investors transacting abroad (often referred to as *f-cubed litigation*). We argue that the conduct and effects tests, as well as court inquiries into whether foreign jurisdictions will recognize U.S. judgments and the presence of alternative remedies abroad, are uncertain in their application and as a result, unpredictable. We propose instead that courts adopt a uniform, bright-line exchange-based presumptive rule in determining the applicable class in a rule 10b-5 class-action lawsuit. Courts should presume jurisdiction over all investors trading in a company's securities within the United States, and presume no jurisdiction for rule 10b-5 lawsuits for foreign investors trading outside the United States. Under this approach, private plaintiffs' attorneys have equivalent incentive to file a class-action lawsuit under rule 10b-5 against foreign issuers, compared with domestic issuers with a similar level of U.S. investor ownership and trading volume, and thus an equal level of private deterrence against the negative effects of fraud on the U.S. markets.

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INTRODUCTION

In this increasing era of globalization, American litigation has also "gone global." Of course, many aspects of the legal effects of cross-border conduct and transactions are not new. Questions about the reach of American law have been around since *American Banana Co. v. United Fruit Co.*[1] in the early twentieth century.[2] But the answers to questions about the territorial reach of U.S. law—whether it be discrimination law, antitrust law, or securities law—are different from the "territorial presumption" that prevailed in earlier times, even if the contemporary "answers" are not always consistent. Both the Supreme Court of the United States and lower courts have emphasized that when there is no express statutory directive on the question of territorial reach, ambiguous statutes are to be construed to "avoid unreasonable interference with the sovereign authority of other nations."[3] Such concerns have surfaced even more dramatically in the context of transnational class-action lawsuits, in particular securities class-action lawsuits involving claims against foreign defendants brought by foreign investors trading outside the United States—a paradigm often referred to as an *f-cubed case*.[4]

In this Paper, we review how courts in the United States have dealt with the extraterritorial application of U.S. securities laws to f-cubed

1. 213 U.S. 347 (1909).

2. *Id.* at 357–58.

3. *F. Hoffman-La Roche Ltd. v. Empagran S.A.*, 542 U.S. 155, 164 (2004).

4. We concern ourselves solely with jurisdictional issues involving class-action lawsuits with foreign defendants and at least some degree of trading outside of the United States. As Professor Buxbaum observes, U.S. courts are consistent in applying jurisdiction to U.S. investors transacting on U.S. markets as well as foreign investors also transacting in U.S. markets. Hannah L. Buxbaum, *Multinational Class Actions Under Federal Securities Law: Managing Jurisdictional Conflict*, 46 COLUM. J. TRANSNAT'L L. 14, 55–56 (2007).

cases[5] and offer our own prescription for dealing with such cases. Concerns about the extraterritorial reach of the U.S. securities laws have been addressed in a variety of contexts. Courts have exercised prescriptive jurisdiction in the securities context for rule 10b-5 actions under the so-called conduct and effects tests, and have used concepts of reasonableness[6] or other doctrines to consider the relative efficiency and desirability of extending jurisdiction abroad.[7] Extraterritorial concerns have also arisen in securities class-action lawsuits in determinations about whether foreign investors in these f-cubed cases can be members of a U.S. class-action lawsuit as well as whether foreign investors can serve as lead plaintiffs. The answers often depend on whether a U.S. class-action judgment or settlement will be recognized abroad, and/or whether there are alternative remedies available elsewhere. Both of these issues affect not only the question of jurisdiction to prescribe, but the particular inquiries that must be made on a class-certification motion with respect to "superiority."

Unfortunately, much uncertainty surrounds the consideration of extraterritorial issues within securities class-action lawsuits. The individual doctrines applied within the courts—such as the conduct and effects tests—are often ambiguous and difficult to predict. Uncertainty also arises from the many different factors that can enter into the calculus of prescriptive jurisdiction, including the question of whether or not 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. Not all courts approach the extraterritoriality issue in the same manner; often, whether foreign

5. The term *f-cubed* is found in Stuart M. Grant & Diane Zilka, *The Role of Foreign Investors in Federal Securities Class Actions*, *in* PLI CORPORATE LAW AND PRACTICE HANDBOOK SERIES, NO. B-1442, at 91, 96 (2004); *see also* Buxbaum, *supra* note 4, at 14; John C. Coffee, Jr., *Securities Policeman to the World? The Cost Of Global Class Actions*, N.Y. L.J., Sept. 18, 2008, at 5.

6. *See* RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES §§ 402, 403, 416 (1986); *see, e.g.*, *Europe and Overseas Commodity Traders, S.A. v. Banque Paribas London*, 147 F.3d 118 (2d Cir. 1998) ("[T]he exercise of prescriptive jurisdiction by Congress would be unreasonable within the meaning of the Restatement of Foreign Relations . . . and is particularly so when the transaction is clearly subject to the regulatory jurisdiction of another country with a clear and strong interest in redressing any wrong."). Courts often perceive the question of the extraterritorial reach of a statute as one of "subject matter jurisdiction," but it is probably more accurate to characterize the issue as one of "legislative" or "prescriptive" jurisdiction. For further discussion on the point, see RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 401, cmt. c (1986) as well as Justice Scalia's dissenting opinion in *Hartford Fire Insurance Co. v. California*, 509 U.S. 764, 813–14 (1993).

7. If a U.S. court is not considered the appropriate forum for the case, a dismissal on forum non conveniens may be in order. Courts have also used a comity analysis as a basis for dismissing a case.

investors will ultimately have a remedy within a federal court turns on that court's selection of a specific doctrinal framework in which to consider extraterritoriality.

We propose reform to the application of extraterritorial jurisdiction for f-cubed cases involving foreign plaintiffs (investors), foreign defendants (often including the issuer), and foreign transactions in the context of securities-fraud class-action lawsuits under rule 10b-5. We argue for a clear bright-line rule tracking the exchange on which the transaction is executed for when U.S. prescriptive jurisdiction is appropriate.[8] Under an exchange-based rule, foreign investors who transact in foreign securities on an exchange outside the United States would be presumptively excluded from rule 10b-5 litigation. Such a rule allows those who wish to avoid the U.S. regime to do so; although it may be unlikely that they will do so, parties who wish to opt into the U.S. regime are able to do so predictably. Such a rule also reduces the role of judges as decision makers on individual determinations of jurisdictional issues. Our proposal offers only a default rule; it leaves the Securities and Exchange Commission (SEC) with the regulatory authority to determine ex ante for which countries U.S. jurisdiction should extend extraterritorially because the SEC stands in a better position to make that determination. Centralizing the decision within the SEC will provide uniformity in how jurisdiction is applied, as well as give other nations a single source with which to negotiate to accommodate issues arising from jurisdictional conflicts.

I. JURISDICTIONAL UNCERTAINTY FOR FOREIGN INVESTORS

A. Jurisdiction to Prescribe

In the past ten years, the Supreme Court has decided two cases on jurisdiction to prescribe, both in the antitrust field. In *Hartford Fire Insurance Co. v. California*,[9] the Supreme Court invoked the *Restatement (Third) of Foreign Relations Law* with the five-person Court majority indicating that, because there were significant effects in the United States and other factors that made the exercise of jurisdiction reasonable, the antitrust laws could be applied.[10] The second case, *F. Hoffman-La Roche Ltd. v. Empagran S.A.*,[11] involved a class-action lawsuit on behalf of

8. With respect to the small number of transactions that do not take place on an exchange, we advocate a rule that looks to the primary location where the transaction takes place.
9. 509 U.S. 764 (1993).
10. *Id.* at 795–96.
11. 542 U.S. 155 (2004).

foreign and domestic purchasers of vitamins who claimed that foreign and domestic vitamin manufacturers and distributors had engaged in a global price-fixing conspiracy, raising the price of vitamin products to customers in the United States and foreign countries.[12] Defendants moved to dismiss the suit as to foreign purchasers who bought the vitamins for delivery outside the United States.[13] The Supreme Court decided 8-0 that the Sherman Act, as limited by the Foreign Trade Antitrust Improvement Act (FTAIA), did not encompass foreign purchasers to the extent that the foreign injuries were independent of domestic effects.[14] While technically the Court was interpreting a statute (the FTAIA), it went further in noting that to exercise jurisdiction over foreign conduct whose foreign harms were independent of domestic harms would have been "an act of legal imperialism."[15]

Whether the philosophy of *Empagran* will carry over to the securities area is not yet clear. The Supreme Court has never taken a prescriptive-jurisdiction case in the context of securities litigation, and it has been the lower courts—in both class and nonclass contexts—that have so far defined the parameters of the extraterritorial reach of the securities laws' antifraud provisions.[16] The federal courts have adopted two judicially created tests with respect to the extraterritorial reach of the antifraud provisions of the Securities Exchange Act of 1934. One test is the "conduct" test, which assesses the relationship between the appellees' domestic conduct and the specific securities fraud at issue before the court. The other is the "effects" test, which measures the foreseeability and magnitude of the effect of the fraud on American investors and markets. Usually these tests are applied independently—that is, they are alternative tests and there is a threshold for each—but at least one United States Court of Appeals (the Second Circuit) has used those tests collectively to determine whether there is sufficient U.S. interest in the transaction at hand to justify application of the U.S. securities law.[17]

With respect to any of the tests, foreign investors who purchase shares of a U.S. corporation on a U.S. exchange will usually satisfy the requirements of prescriptive jurisdiction. That is also true for a foreign investor who purchases American Depositary Receipts (ADRs) of a foreign corporation through a transaction on a domestic exchange. This

12. *Id.* at 155.
13. *Id.*
14. *Id.* at 175.
15. *Id.* at 169.
16. Certain provisions of the securities laws have been determined by SEC regulations not to apply to overseas transactions. *See, e.g.*, 17 C.F.R. § 230.901–.905 (2008).
17. *See Itoba Ltd. v. Lep Group PLC*, 54 F.3d 118, 121–22, 124 (2d Cir. 1995).

view reflects the strong U.S. interests in the regulation of its securities markets.[18] The more difficult issue arises with respect to the "f-cubed" securities class-action case—involving a class consisting at least partially of foreign investors who purchase securities of a foreign corporation on a foreign securities exchange. The question is whether such cases should be regulated according to U.S. standards, and if so, in what circumstances.

1. CONDUCT TEST

When f-cubed securities class-action lawsuits come within U.S. regulatory authority, it is usually the result of application of the conduct test. In the relatively early case *Bersch v. Drexel Firestone, Inc.*,[19] Judge Henry Friendly identified the conduct test in terms of whether enough of the fraudulent behavior occurred in the United States to grant the plaintiff a cause of action under the federal securities laws.[20] He further stated that there was no reason to extend prescriptive jurisdiction to include cases "where the United States activities are merely preparatory or take the form of culpable nonfeasance and are relatively small in comparison to those abroad."[21] Interpretation of this test in both class and nonclass contexts has left much to be desired. In a leading case in the United States Court of Appeals for the Third Circuit, *SEC v. Kasser*,[22] which was not a class or even a private action, the Court of Appeals held that U.S.-based conduct could suffice to extend application of the securities law to a

18. *Cf. Schoenbaum v. Firstbrook*, 405 F.2d 200 (2d Cir. 1968). *Schoenbaum* was a derivative suit brought by a U.S. shareholder on behalf of a Canadian oil company against management, alleging that it had sold treasury stock to another Canadian corporation that was a controlling shareholder of the company. *Id.* at 204–05. The transaction had been carried out entirely in Canada, but the shares of the corporation were registered and traded on the American Stock Exchange. *Id.* The district court dismissed the suit, but the United States Court of Appeals for the Second Circuit held that the Securities Act of 1933 applied when necessary to protect American investors. *Id.* at 204–08.

19. 519 F.2d 974 (2d Cir. 1975).

20. *Id.* at 977, 986–87.

21. *Id.* at 987. The court offered the following analogy:

> The fraud, if there was one, was committed by placing the allegedly false and misleading prospectus in the purchasers' hands. Here the final prospectus emanated from a foreign source . . . . Not only do we not have the case where all the misrepresentations were communicated in the nation whose law is sought to be applied . . . or the case where a substantial part of them were . . . but we do not even have the oft-cited case of the shooting of a bullet across a state line where the state of the shooting as well as of the state of the hitting may have an interest in imposing its law. At most the acts in the United States helped to make the gun whence the bullet was fired from places abroad.

Id.

22. 548 F.2d 109 (3d Cir. 1977).

Canadian investor, even where there were no effects on the U.S. market.[23] In colorful language, the Third Circuit in *Kasser* explained its reasoning: prescriptive jurisdiction should not be exercised in so lax a manner as to turn the United States into a "'Barbary Coast' . . . harboring international securities 'pirates.'"[24] Interestingly, cases decided by the courts of appeals interpreting the conduct test have generally been outside the class-action context,[25] and thus it has been the lower federal district courts that so far have attempted to outline the contours of that test within the class-action setting.

Two current cases are of particular interest in that regard. The first is a district court case, *In re Vivendi Universal, S.A. Securities Litigation*,[26] where a French corporation was sued in the United States by foreign buyers of foreign securities for ascertaining and disseminating fraudulent statements and financial data about the corporation.[27] Notwithstanding the fact that the relevant statements of data were initiated, organized, and approved in France, the court found that other conduct in the United States justified application of the securities laws. First, Vivendi had acquired numerous U.S. companies, the acquisition of which was the cause of the debt at the center of the fraudulent information. Because the acquisition of the companies was the predicate for false statements, these acquisitions were found to be a "cause" of the fraudulent scheme. Second, Vivendi had targeted the U.S. market; Vivendi's top two officers resided in and operated out of the United States, which enabled them to more effectively promote misleading perceptions on Wall Street. It could reasonably be inferred that the alleged fraud on the U.S. exchange was a

23. *Id.* at 116; *see also Straub v. Vaisman and Co.*, 540 F.2d 591 (3d Cir. 1976).

24. *Kasser*, 548 F.2d at 116.

25. *See, e.g.*, *SEC v. Berger*, 322 F.3d 187 (2d Cir. 2003) (finding jurisdiction to prescribe under the securities laws in an action by the SEC against the defendant and his offshore investment company established in the British Virgin Islands, and determining that although most of the investors were foreign and the information was disseminated outside the United States, the fraudulent account statements created by the defendant in the United States were sufficient to satisfy the conduct test); *Europe & Overseas Commodity Traders, S.A. v. Banque Paribas London*, 147 F.3d 118, 129 (2d Cir. 1998) (finding exercise of prescriptive jurisdiction over a Panamanian corporation's suit against a French bank, its London account manager, a Canadian citizen, and other foreign defendants would be "unreasonable" even though the Canadian defendant made an offer to sell securities from the United States, and that the transaction was clearly subject to the regulatory jurisdiction of another country with a clear and strong interest in redressing any wrong); *Kasser*, 548 F.2d at 111, 114 (holding that federal securities laws applied in an action by the SEC against U.S. and foreign defendants who acted largely in Canada and caused harm to a Canadian investor).

26. 381 F. Supp. 2d 158 (S.D.N.Y. 2003).

27. *Id.* at 164, 169–70.

"substantial cause" of foreign investors' decisions to purchase Vivendi's stock abroad.

The second case, in potential tension with the first, is *Morrison v. National Australia Bank Ltd.*,[28] which was the first and only f-cubed securities class-action lawsuit to reach the United States Court of Appeals for the Second Circuit.[29] *Morrison* is a prime example of the difficulty of distinguishing "substantial conduct" from "preparatory conduct," and it offered an opportunity for the court to provide guidance on dealing with these f-cubed cases. In *Morrison*, defendant National Australia Bank (NAB) reported purportedly fraudulent statements concerning a U.S. mortgage service provider that NAB had acquired.[30] The statements were transmitted to shareholders outside the United States, but the data collection that ultimately resulted in the fraudulent conduct occurred in the United States. A class-action lawsuit was filed on behalf of both U.S. domestic plaintiffs who purchased ADRs on the New York Stock Exchange (NYSE) and foreign plaintiffs who purchased NAB shares on Australian and other foreign exchanges. On a motion to dismiss the foreign plaintiffs for lack of prescriptive jurisdiction, the district court found no significant conduct or effects in the United States.[31] The district court characterized the conduct of the U.S.-based mortgage service provider as "at most, a link in the chain of an alleged overall securities fraud scheme that culminated abroad," and held jurisdiction to prescribe lacking.[32]

On appeal, the Second Circuit affirmed the dismissal.[33] Attempting to establish the parameters of the conduct test for prescriptive jurisdiction, the Second Circuit explained that jurisdiction attaches only if the defendant's conduct in the United States was "*more than merely prepatory to a fraud* and culpable acts or omissions here *directly caused losses* to investors abroad."[34] Pointing to the earlier Second Circuit cases, *Bersch v. Drexel Firestone, Inc.*[35] and *IIT v. Vencap, Ltd.*,[36] which the court in *Morrison* characterized as illustrating the approach to prescriptive jurisdiction under the conduct test, the court undertook to "identify which action or actions constituted the fraud and directly caused harm . . . and

28. 547 F.3d 167 (2d Cir. 2008).

29. *Id.* at 172.

30. *In re Nat'l Austl. Bank Sec. Litig.*, No. 03 Civ. 6537 (BSJ), 2006 WL 3844465, at *1 (S.D.N.Y. 2006).

31. *Id.* at *9.

32. *Id.* at *8.

33. *See Morrison*, 547 F.3d at 177.

34. *Id.* (emphasis added).

35. 519 F.2d 974 (2d Cir. 1975).

36. 519 F.2d 1001 (2d Cir. 1975).

then determine if that act or those actions emanated from the United States."[37] The court viewed its inquiry as follows:[38]

> 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.[39]

In affirming the district court's conclusion that prescriptive jurisdiction was lacking, the Second Circuit relied on three factors that helped to localize the conduct that it perceived as the "heart of the alleged fraud."[40] First, the actions taken in Australia were "significantly more central to the fraud and more directly responsible for the harm to investors" than the conduct in Florida, and "as a practical matter," the "responsibility" for ensuring the accuracy of disclosures and public statements rested in Australia rather than in Florida.[41] Unlike in the *Vivendi* case, the court in *Morrison* made a qualitative distinction based on the location of the party who ultimately had the responsibility for issuing the misleading statements.[42] Despite the origin of the fraud in the United

37. *Morrison*, 547 F.3d at 173.

38. In cases similar to *National Australia Bank*, other district courts have found jurisdiction to prescribe. In *In re Alstom SA Sec. Litig.*, 406 F. Supp. 2d 346 (S.D.N.Y. 2005), the court applied the U.S. securities laws to claims by a class of foreign plaintiffs who alleged that accounting improprieties at the French conglomerate defendant's U.S. subsidiary were incorporated into the financial statements and distributed abroad. *Id.* at 370. In *In re Gaming Lottery Securities Litigation*, 58 F. Supp. 2d 62 (S.D.N.Y. 1999), prescriptive jurisdiction was sustained over a class of foreign plaintiffs where a Canadian defendant had acquired a U.S. subsidiary without regulatory approval and made false representations with respect to it. *Id.* at 73–76. The court there observed that efficiencies of market pricing and the ever-present possibility of arbitrage generally caused stock prices across markets to move "in tandem," such that fraud in one market will almost certainly have an effect on purchasers of securities of the same company on another market. *Id.* at 75. *But cf. In re Scor Holding (Switz.) AG Litig.*, 537 F. Supp. 2d 556, 560–69 (S.D.N.Y. 2008) (finding that a federal court did not have prescriptive jurisdiction over the claims of foreign persons who purchased shares of a Swiss company on a Swiss exchange, and determining that filing documents with the SEC, having a meeting in the United States, and conducting conference calls with Wall Street analysts was insufficient to establish conduct that directly caused the losses claimed by the foreign plaintiffs).

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

40. *Id.* at 175.

41. *Id.* at 176.

42. *See id.*

States, the *Morrison* court found such actions as merely preparatory because the responsibility for the statements ultimately lay abroad.[43] Second, there were no meaningful domestic effects on either U.S. investors or U.S. capital markets.[44] And third, the "chain of causation"[45] from the domestic acts to the eventual securities violation was too attenuated.[46]

The court in *Morrison* rejected an alternative formulation of the conduct test presented by the SEC in its amicus brief. The SEC suggested that the prior case law had "set forth a series of 'diverse formulations' of the applicable legal standard" and it sought to offer its own clarification of a conduct test.[47] It proposed that the antifraud provisions of the securities law "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."[48] In the SEC's view, materiality is satisfied when domestic conduct is "an integral—not incidental or ancillary—link in the chain of events in the transnational fraud."[49] Once domestic conduct is deemed material, the inquiry then turns to "substantiality," which the SEC argued could be satisfied by demonstrating a "sufficient quantum of conduct" in the United States to warrant application of the antifraud provisions, or even a showing of more limited conduct in the United States where the particular domestic conduct was "highly significant to the fraud."[50]

Responding to defendant and amici concerns about international comity and an overextension of U.S. securities laws to foreign corporations whose shares trade overseas that would discourage investment in the United States, the SEC brief noted that it was articulating its conduct test only for SEC enforcement action and private suits by named foreign plaintiffs.[51] As for class-action lawsuits, the SEC brief noted that the Second Circuit had suggested on several occasions that

43. *Id.*

44. *Id.*

45. *Id.*

46. The court in *Morrison* also took pains to explain what it was not saying. Noting that courts in other circuits had misunderstood the test of the Second Circuit as requiring the "domestic conduct [to comprise] all the elements of a defendant's conduct necessary to establish a violation of section 10(b) and Rule 10b-5," the court expressly disavowed such a characterization. *Id.* at 172 n.6.

47. Brief of the Securities and Exchange Commission as Amicus Curiae, in Response to the Court's Request at 2, *Morrison v. Nat'l Austl. Bank*, 547 F.3d 167 (2d Cir. 2008) (No. 07-0583-cv).

48. *Id.* at 22.

49. *Id.* at 23.

50. *Id.* at 24.

51. *Id.* at 4 n.1, 29.

class-action lawsuits presented unique considerations, and that a "more jurisdictionally restrictive standard may be warranted in the class-action context."[52]

2. EFFECTS TEST

The other primary test courts use to extend federal jurisdiction extraterritorially in securities-fraud cases is the effects test. In *Schoenbaum v. Firstbrook*,[53] an U.S. plaintiff and shareholder of Banff Oil Ltd., a Canadian corporation, alleged a violation of section 10(b) of the Securities Exchange Act of 1934, claiming that the company's controlling shareholders had arranged to purchase shares from the corporation for a price below fair market value.[54] While the securities transaction involved in *Schoenbaum* took place in Canada, the Second Circuit held:

> [T]he district court has subject matter jurisdiction over violations of the Securities Exchange Act although the transactions which are alleged to violate the Act take place outside the United States, at least when the transactions involve stock registered and listed on a national securities exchange, and are detrimental to the interests of American investors.[55]

According to the Second Circuit in *Schoenbaum*, the sale of undervalued stock in Canada would negatively affect the price of Banoff stock trading on an U.S. securities exchange. This negative effect on price provided enough of an effect to justify the extension of U.S. jurisdiction.[56] The effects test as outlined in *Schoenbaum* has been followed in several other cases.

Not all effects rise to the level required in *Schoenbaum* to trigger the effects test. Where the issuer's securities do not trade in the United States and the plaintiff argues that the issuer's fraudulent activities have a general effect on the U.S. economy, the businesses of U.S. companies, or more generally on U.S. securities trading as a whole, courts are unlikely to find the effects test met. The Second Circuit in *Bersch* held that "an adverse effect on this country's general economic interests or on American security prices" did not generate enough of an

52. *Id.* at 4 n.1.
53. 405 F.2d 200 (2d Cir. 1968).
54. *Id.* at 204.
55. *Id.* at 208.
56. *See id.* at 206.

effect to result in the extraterritorial application of rule 10b-5 to foreign defendants.[57]

Whether the effects test could be developed to include the f-cubed cases is an interesting question. The Second Circuit in *Morrison*, addressing the question of jurisdiction in the f-cubed situation, explicitly stated that a court should 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."[58] When a corporation's shares are traded on an U.S. exchange as well as a foreign exchange, it might be argued that there is a harmful domestic effect if prices fall abroad, since falling prices abroad may cause securities traded on the U.S. exchange to fall as well. Such a domestic effect could be said to be the result of a global and efficient securities market.[59] On the other hand, we know of no court that has used the effects test to apply extraterritorial jurisdiction in an f-cubed case. In refusing to apply the effects test for f-cubed plaintiffs, courts have rejected the view of a worldwide market for securities.[60] Similarly, courts have rejected extending jurisdiction under the conduct test for foreign plaintiffs trading outside the United States under a theory that world securities markets are interconnected and that conduct (in the form of SEC filings in the United States) is significant for trading abroad.[61]

57. 519 F.2d 974, 989 (2d Cir. 1975).

58. *Morrison v. Nat'l Aust. Bank Ltd.*, 547 F.3d 167, 171 (2d Cir. 2008). The *Morrison* court went on to say: "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." *Id.* at 175 (emphasis added). Despite this language, *Morrison* did not apply the effects test because the appellants "rely solely on the conduct component of the test." *Id.* at 171.

59. *Cf.* Ronald J. Gilson & Reinier H. Kraakman, *The Mechanism of Market Efficiency*, 70 VA. L. REV. 549, 549–52 (1984).

60. *See, e.g.*, *In re Baan Co. Sec. Litig.*, 103 F. Supp. 2d 1, 11 (D.D.C. 2000) ("[P]laintiffs argue that the defendants' acts had an effect in the United States because Baan shares trade in tandem on the world's markets, and therefore the value of Baan's shares owned by United States residents was affected. More specifically, the shares owned by the American plaintiffs were affected. However, the *Bersch* court rejected the idea that generalized effects in the United States are sufficient to confer subject matter jurisdiction. The effects test only extends jurisdiction as to those American plaintiffs who are affected."). For an argument that both the conduct and effects test should have broader transnational impact, see Hannah L. Buxbaum, *Transnational Regulatory Litigation*, 46 VA. J. INT'L L. 252, 275–78 (2006).

61. *See In re Bayer AG Sec. Litig.*, No. 03 Civ. 1546 (WHP), 2004 U.S. Dist. LEXIS 19593, at *55 (S.D.N.Y. Sept. 30, 2004) ("Although plaintiffs rely in part on the 'fraud on the market' doctrine to show causation and reliance, that doctrine cannot be used to satisfy the conduct test."); *Tri-Star Farms Ltd. v. Marconi, PLC*, 225 F. Supp. 2d 567, 579 (W.D. Pa. 2002) (rejecting the plaintiffs' argument that there

B. "Transnational Issues" Complicating the Inquiry

Courts do not rely solely on the conduct and effects tests in limiting jurisdiction in f-cubed litigation. Courts often turn to other doctrines to restrict application of a rule 10b-5 remedy in the federal courts, particularly in the class-action context. Concerns about comity are captured by the *Restatement (Third) of Foreign Relations Law*, which imposes a reasonableness test in determining whether prescriptive jurisdiction is to be exercised. Moreover, invocation of forum non conveniens may result in dismissal of the suit in favor of an alternative forum. Also, the propriety of certification of a class-action lawsuit that includes foreign investors involves the question of whether the class-action mechanism is a "superior" method of proceeding, and may depend on how foreign courts will treat a class-action judgment. These transnational issues thus complicate any f-cubed case.

1. RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW

Even when there is a conduct jurisdictional hook in these f-cubed cases, courts, particularly those looking at the *Restatement (Third) of Foreign Relations Law*, are likely to look at the reasonableness of the exercise of jurisdiction.[62] Reasonableness is a multifactored test that considers the links and connections to the various countries, as well as the competing regulatory interests, the existence of justified expectations, and the likelihood of conflict with regulation by another country.[63] Thus, we have seen courts in the class-action context take account of whether (1) a judgment in the U.S. class proceeding will be recognized abroad, such that a prevailing defendant will not face a multiplicity of suits; and (2) there are alternatives available in the plaintiffs' home state to remedy these securities violations, and if so, whether such remedies conflict with an exercise of U.S. jurisdiction.[64]

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was a "seamless, worldwide market" and instead holding that "[e]mploying the 'fraud-on-the-market' doctrine to satisfy the conduct test in this type of class action lawsuit involving overwhelmingly foreign transactions would extend the jurisdictional reach of the securities laws too far.").

62. *See, e.g.*, *Europe and Overseas Commodity Traders, S.A., v. Banque Paribas London*, 147 F.3d 118, 129 (2d Cir. 1998) ("[T]he exercise of prescriptive jurisdiction by Congress would be unreasonable within the meaning of the Restatement of Foreign Relations . . . and is particularly so when the transaction is clearly subject to the regulatory jurisdiction of another country with a clear and strong interest in redressing any wrong.").

63. *See* RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 403(2) (1987).

64. On the initial motion to dismiss in *In re Royal Dutch/Shell Transport Securities Litigation*, 380 F. Supp. 2d 509, 548 (D.N.J. 2005), the court characterized

2. FORUM NON CONVENIENS

Foreign defendants sued by a class that includes foreign plaintiffs in a multinational securities action may seek to dismiss the complaint on a forum-non-conveniens motion. On a forum non conveniens motion, courts generally require that defendants show that (1) there is an adequate alternative jurisdictional forum available outside the United States, and (2) private- and public-interest factors balance strongly toward dismissal.[65] Courts have applied forum non conveniens in transnational securities actions where the alternative forum is a foreign forum[66] and unlikely to apply U.S. securities laws.[67]

A few courts have used the concept of comity rather than forum non conveniens to dismiss where a present proceeding exists in a foreign forum and concerns relating to "international cooperation" weigh strongly in favor of deferring to the foreign jurisdiction's proceedings.[68]

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the issue of alternative remedies in the plaintiffs' home state as an element of "international comity." For further discussion on this case *infra* Part I.B.5.b.

65. The leading Supreme Court case, *Gulf Oil Corp. v. Gilbert*, 330 U.S. 501 (1947), set forth this test in a domestic context where the alternative forum was another U.S. court. *Id.* at 503. With respect to the private interests, the Court in *Gulf Oil* looked to considerations such as the relative ease of access to sources of proof, the availability of compulsory process, the cost of obtaining attendance of witnesses, and other issues directed to an expeditious and inexpensive trial. *Id.* at 508. Other concerns relate to the enforceability of a U.S. judgment abroad. *Id.* With respect to public interests, the Court expressed its concerns about the burdens, including jury service, imposed upon the people of a community that has no relation to the litigation, as well as the difficulties for courts in untangling problems in conflict of laws and foreign law itself. *Id.* at 508–09. Although the *Gulf Oil* analysis is applied in transnational cases, *see Howe v. Goldcorp Invs., Ltd.*, 946 F.2d 944 (1st Cir. 1991), that test may not fully consider some of the unique aspects of transnational litigation.

66. *See Howe*, 946 F.2d at 945; *Alfadda v. Fenn*, 935 F.2d 475 (2d Cir. 1991). *See generally* Buxbaum, *supra* note 4, at 35–38.

67. Laws classified as "public" or "regulatory" are generally thought not to be enforceable in the courts of other countries. For a history and critique of the doctrine, particularly when claims are brought by private plaintiffs, see William S. Dodge, *Breaking the Public Law Taboo*, 43 HARV. INT'L L.J. 161 (2002).

68. *See, e.g.*, *Paraschos v. YBM Magnex Int'l, Inc.*, 130 F. Supp. 2d 642, 645 (E.D. Pa. 2000) ("The rationale for dismissals based on comity is . . . deference to the foreign country's legal, judicial, legislative, and administrative system of handling disputes over which it has jurisdiction, in a spirit of international cooperation."). Interestingly, unlike some continental systems, the United States does not have a formal *lis pendens* doctrine to stay a case when prior proceedings have been instituted elsewhere. Some courts in the United States have relied upon forum non conveniens to dismiss such cases, whereas others have invoked "international abstention" or comity. *See* Linda Silberman, *A Proposed* Lis Pendens *Rule for Courts in the United States: The International Judgments Project of the American Law Institute*, *in* INTERNATIONAL

3. CLASS CERTIFICATION

Transnational securities class-action lawsuits often pose special issues for courts considering applications for class certification. Specifically, courts face the question of whether a class of foreign investors is "superior to other available methods for the fair and efficient adjudication of the controversy" pursuant to Federal Rule of Civil Procedure (FRCP) 23(b)(3). In assessing "superiority," courts often look to whether (1) a judgment in the U.S. class proceeding will be recognized abroad, and (2) there are alternative remedies available in the plaintiffs' home country. The answers to these questions may be a double-edged sword that often keeps these foreign plaintiffs out of the class in any case. On the one hand, if the foreign country has a class-action-like remedy, courts in that country may be more likely to recognize a class-action judgment that includes opt-out class members. But at the same time, the availability of an alternative remedy may mean that there is a more appropriate alternative in that country and plaintiffs need not be part of a U.S. class-action lawsuit.

4. LEAD PLAINTIFF

Another place the recognition-of-judgment issue has emerged is at the selection of lead plaintiff in a securities class-action lawsuit under the Private Securities Litigation Reform Act of 1995 (PSLRA). Although the PSLRA imposes a presumption that the plaintiff seeking lead-plaintiff status with the "largest financial interest" in the litigation will be the lead plaintiff (so long as the other requirements of FRCP 23 are fulfilled), the possible lack of prescriptive jurisdiction in the f-cubed case may rebut that presumption. The issue surfaced in *In re Royal Ahold N. V. Securities and ERISA Litigation*,[69] a case in which a German investment fund was in competition with other U.S. plaintiffs for lead status. Royal Ahold had overstated its earnings, and certain transactions in one of its units were legally suspect. Although the fund was one of the largest institutional investors, the court found that it could not serve as an adequate class representative because it would need to devote a large portion of its time and effort to the issue of prescriptive jurisdiction.

COOPERATION THROUGH PRIVATE INTERNATIONAL LAW 341, 350–51 (Talia Einhorn & Kurt Siehr eds., 2004).

69. 219 F.R.D. 343 (D. Md. 2003).

5. COMMON CONSIDERATIONS

Each of the doctrinal theories set forth above affect the viability of transnational securities actions in U.S. courts. Cutting across these various doctrines are certain common threads that are generally important in transnational litigation. The first is whether U.S. judgments will be respected in foreign jurisdictions; the second is the availability of alternative remedies in foreign jurisdictions for investors.

a. Recognition of U.S. class-action judgments

Consider first the recognition of the U.S. class-action judgment factor. Why—and in what contexts—should it be relevant? The argument of defendants in resisting class-action lawsuits that include foreign investors is that if they, as defendants, are successful, they may still face a potential lawsuit in a foreign jurisdiction brought by the absent class plaintiffs. Normally, even class plaintiffs who have never formally consented to suit would be bound—at least as a matter of U.S. law—to the extent they failed to opt out of the class. That type of jurisdiction or "binding effect" is not known or generally accepted by many countries, supporting the argument that the judgment will not have any preclusive effect outside the United States. In one sense, the concern may be more hypothetical than real, since it is unlikely that the "absent member" of the U.S. class would ever relitigate such a claim in a foreign court. Nonetheless, several courts have expressed concern with that issue, and the result has been elaborate expert reports (and subsequent law-review articles by those experts) detailing the likelihood of enforcement of such a judgment in various countries.

The background to the concern for judgment recognition can be traced to language by Judge Friendly in *Bersch*, where he first raised the point in a context where it was clear from "uncontradicted affidavits" that a judgment would not bind the foreign plaintiffs.[70] Judge Friendly continued: "[W]hile an American court need not abstain from entering judgment simply because of a possibility that a foreign court may not recognize or enforce it, the case stands differently when this is a near certainty."[71] Defendants have attempted to show in a number of foreign

70. 519 F.2d 974, 996 (2d Cir. 1975).

71. *Id.* at 996. The question of whether a foreign jurisdiction would recognize a U.S. class-action judgment by a foreign country arose in a slightly different context in the *Bersch* case. The court was considering whether it should extend the doctrine of pendent jurisdiction to include in the class action lawsuit a group of foreign purchasers who might have claims against the defendants under state or foreign law. *Id.* The court found that it would be an abuse of discretion to do so, given the myriad choice-of-law

investor class-action lawsuits in the United States that a U.S. class-action judgment would not be binding in a foreign jurisdiction and that an absent-class foreign investor, unhappy with the result in the U.S. class-action lawsuit, would be able to pursue a multiplicity of actions. As noted above, the issue can arise in a variety of contexts.

Concerns about nonrecognition of an eventual U.S. class-action judgment or settlement were highlighted recently on a motion for class certification in *Vivendi.* As discussed above, a securities-fraud action under rule 10b-5 was brought against Vivendi for making false and misleading statements leading to artificially inflated prices for Vivendi stock.[72] Plaintiff sought certification of a worldwide class consisting of all persons who purchased or otherwise acquired Vivendi's common stock or American Depository Shares (ADSs) during the proposed class period.[73] A significant number of the proposed class were foreign investors (37 percent of the ordinary shares were held by citizens of France who purchased them on the Bourse; U.S. investors held 25 percent of Vivendi shares in the form of ADSs purchased on the NYSE).[74] On the class-certification motion, defendants argued that the foreign plaintiffs should be excluded from the class because there would be no preclusion bar in France or other European countries, and thus certification should be denied because such a class would not meet the requirement of "superiority" in FRCP 23(b)(3).

Voluminous expert declarations were introduced and the court proceeded to examine the recognition issue at length.[75] It first turned to a discussion of recognition of a U.S. class-action judgment in France. France requires a "characteristic link" with the forum before a judgment will be recognized and the federal district court concluded that there was such a link with the United States, although it focused on the connection with Vivendi rather than the link with the French investor plaintiffs who were the relevant parties to be bound. Moreover, the court did not believe that a U.S. class-action judgment would be found to be a violation of public policy in France. The court also reviewed the law on recognition of judgments in England, the Netherlands, Germany, and Austria. Choosing to evaluate the possibility of recognition along a continuum, the district

issues and the fact that it was a "near certainty" that foreign courts would not recognize a class-action judgment for either party or a settlement deemed to be inadequate. *Id.*

72. *See supra* notes 26–27 and accompanying text (discussing the *Vivendi* opinion).

73. *In re Vivendi Universal, S.A. Sec. Litig.*, 242 F.R.D. 76, 92 (S.D.N.Y. 2007).

74. *Id.* at 81.

75. For a more general discussion of foreign recognition of U.S. judgments, see Linda J. Silberman, *Some Judgments on Judgments: A View from America*, 19 K.C.L.R. 235 (2008).

court determined that France, England, and the Netherlands would "more likely than not" recognize the judgment.[76] By contrast, the plaintiffs did not establish a "likelihood" that German or Austrian tribunals would do so.[77] Using that standard, the court decided that the French, English, and Dutch investors were "in" but the German and Austrian plaintiffs were "out."[78] Defendants sought to appeal the certification issue via an FRCP 23(f) motion, requesting clarification of the appropriate standard for assessing the relationship between the requirement of res judicata and the determination of class-action superiority under FRCP 23(b)(3). Specifically, defendants challenged the "more likely than not" standard and argued that the lack of "preclusion protection" amounted to a due process violation. The Second Circuit refused to hear the appeal, and defendants then sought certiorari in the Supreme Court which was denied.[79]

The question of recognition of a class-action judgment was also raised on an early motion to dismiss in *In re Royal Dutch/Shell Transport Securities Litigation*,[80] but there the issue was part of the inquiry as to whether prescriptive jurisdiction was proper.[81] The defendants "retained eight 'expert jurists or legal scholars' . . . who 'raised serious concerns about whether their courts would recognize or enforce an 'opt out' class-action judgment with respect to claims by foreign nationals who purchased shares on foreign exchanges.'"[82] The thrust of those opinions was that any judgment could "*probably not* be used by [the defendant, Royal Dutch Shell] to forestall new lawsuits against it in foreign jurisdictions."[83] Plaintiffs' experts, on the other hand, "opine[d] that there [was] no consensus about whether the European courts in question would recognize a [class-action] judgment" in this case, and believed that there were "credible arguments" in favor of recognition and enforcement.[84] The district court, applying the test of a "near certainty" that a judgment would not be enforced, found that this threshold had not been met and that the securities laws extended to the foreign investors.[85] In addition, the

76. *See Vivendi*, 242 F.R.D. at 95–105.

77. *See id.*

78. *See id.* at 105.

79. *In re Vivendi*, 128 S. Ct. 391 (2007).

80. 380 F. Supp. 2d 509 (D.N.J. 2005).

81. *Id.* at 546–47.

82. *Id.* (quoting Royal Dutch/Shell Defendants' Memorandum in Support of Their Motion to Dismiss in Part for Lack of Subject Matter Jurisdiction at 33, *In re Royal Dutch*, 380 F. Supp. 2d at 509 (Civil No. 04-374 (JWB))).

83. *Id.* at 547.

84. *Id.*

85. *Id.*

court rejected[86] the contention of the defendant (who relied on *Empagran*) that the case posed a "serious risk of interference with a foreign nation's ability independently to regulate its own commercial affairs."[87] But subsequently, after further discovery and additional developments, a different judge dismissed the action for lack of a sufficient connection with the United States.[88]

Lead-plaintiff status to a foreign investor has also turned on the court's consideration of whether a U.S. class-action judgment would be recognized abroad. In the *Royal Ahold* case, lead-plaintiff status was denied to a German institutional investor because there was a possibility that a U.S. judgment might not be recognized in Germany and as a result, the German institutional investor as well as other foreign purchasers might be eliminated from the class.[89] In a subsequent ruling, however, the court found that there was jurisdiction to hear the claims of foreign purchasers based on conduct by Royal Ahold in the United States, and without reference to how a foreign court might treat a U.S. judgment.[90] Nonetheless, the German institutional investor was denied lead-plaintiff status.

In *Borochoff v. Glaxosmithkline PLC*,[91] another German institutional investor failed to obtain lead-plaintiff status despite having suffered the largest loss on the basis of similar res judicata concerns.[92] Although the court refused to conclusively decide the prescriptive-jurisdiction issue, it found that there was a substantial risk that the plaintiff would be excluded from the class, and that "it would be improvident to appoint that German [investor group] as lead plaintiff at this point."[93] Of course, when it appears likely that the court will indeed have prescriptive jurisdiction over the claims of foreign plaintiffs, lead-plaintiff status may indeed be granted to a large foreign investor. For example, in *Mohanty v. BigBand Networks, Inc.*,[94] the argument was made that a U.S. class-action judgment would not be enforceable in Cyprus, and thus the Cypriot

86. *Id.* at 548.

87. Royal Dutch/Shell Defendants' Memorandum in Support of Their Motion to Dismiss in Part for Lack of Subject Matter Jurisdiction at 40, *In re Royal Dutch*, 380 F. Supp. 2d at 509 (Civil No. 04-374 (JWB)).

88. *In re Royal Dutch/Shell Transport Sec. Litig.*, 522 F. Supp. 2d 712, 723 (D.N.J. 2007).

89. *In re Royal Ahold N.V. Sec. & ERISA Litig.*, 219 F.R.D. 343, 352 (denying lead-plaintiff status to Union Asset Management Holding AG).

90. *See In re Royal Ahold N.V. Sec. & ERISA Litig.*, 351 F. Supp. 2d 334, 353–54, 355–57, 362 (D. Md. 2004).

91. 246 F.R.D. 201 (S.D.N.Y. 2007).

92. *Id.* at 205.

93. *Id.*

94. No. C 07-5101 SBA, 2008 WL 426250 (N.D. Cal. Feb. 14, 2008).

plaintiff should not be accorded lead-plaintiff status.[95] One of the plaintiffs competing for lead-plaintiff status relied on a link to a Web site that purportedly contained translations of assorted Cypriot laws.[96] The court was not impressed, noting that "the versions of the rules on this website appear to use idiomatic phraseology that is literally Greek to this Court."[97]

b. Availability of alternative remedies and class-action analogues

Unlike the recognition-of-judgments concern that has surfaced in various contexts as explained above, the inquiry with respect to the availability of remedies elsewhere is less common. That may be partly due to the fact that only a few other countries have adopted class-action mechanisms for securities violations. But the landscape in Europe and elsewhere is changing,[98] and the result is that the case for rejecting both U.S. jurisdiction and worldwide classes and allowing other countries to remedy violations in the f-cubed cases is likely to grow stronger.

The availability of an alternative remedy abroad did seem to affect the decision on prescriptive jurisdiction in the *Dutch Shell* case. There, the question arose in the context of a decision as to whether it was reasonable for a U.S. court to exercise prescriptive jurisdiction under the securities laws. As noted above, the issue arose in *Dutch Shell* on a motion to dismiss, not on class certification. *Dutch Shell* was a class-action lawsuit brought in the United States District Court for the District of New Jersey by the lead plaintiffs (Pennsylvania State Employees' Retirement System and the Pennsylvania Public School Employees' Retirement System) and class representative Peter M. Wood, a British citizen and resident/domiciliary of Andorra, on behalf of themselves and all persons who had purchased the securities of the Royal Dutch Petroleum Co. The gravamen of the complaint was false and misleading statements by Shell in reporting its proven oil and gas reserves. Shell settled other proceedings brought by the SEC in the United States and by the Financial Services Authority in the United Kingdom, and subsequently a class-action lawsuit was filed against Shell on behalf of all shareholders worldwide based on Shell's fraudulent scheme of improperly booking and reporting its proven oil and gas reserves.

In a 2005 district-court opinion, Judge John Bissell found that Shell had "engaged in material and substantial fraudulent conduct in the United

95. *Id.* at *8.

96. *Id.*

97. *Id.*

98. *See generally* Richard A. Nagareda, *Aggregate Litigation Across the Atlantic and the Future of American Exceptionalism*, 62 VAND. L. REV. 1 (2009) (comparing mechanisms for aggregate litigation in Europe and the United States).

States" and that there was "a sufficient interest in the claims of the foreign investors" to support the exercise of jurisdiction.[99] Also, the judge largely dismissed the need to examine the remedial scheme in other countries so long as the United States had a sufficient interest in the claims of the foreign investors. However, in April 2007, the lead plaintiffs were informed that Shell had negotiated a contract for settlement with the foreign Individual Plaintiffs[100] as well as other foreign purchasers who purchased their shares outside the United States. The settlement was made pursuant to the 2005 Dutch Act on Collective Settlement of Damages (Dutch Collective Settlement Act) that permits mass settlement of claims but does not permit class-action litigation. During this time, the parties were engaged in extensive discovery, revealing further evidence (or lack thereof) with respect to U.S. activity. Judge Bissell had retired and a further hearing was referred to a special master. In light of the additional facts that were put forward, the special master and the new judge, Judge Joel Pisano, concluded that there was not sufficient conduct in relation to the non-U.S. purchasers to justify application of the U.S. securities laws.[101] The court buttressed its decision by noting that the non-U.S. purchasers can seek recovery through the settlement agreement entered into before the Amsterdam Court of Appeals or through procedures available within their respective jurisdictions.[102]

The availability of an alternative remedy may be a factor not only with respect to prescriptive jurisdiction, but also on the question of class certification in a case where the connections with the case are largely foreign. Whether a class-action lawsuit is a superior method of proceeding

99. *In re Royal Dutch/Shell Transp. Sec. Litig.*, 380 F. Supp. 2d 509, 548 (D.N.J. 2005). For a discussion of this case see *supra* Part I.B.5.a.

100. In January 2006, several non-U.S. purchasers (and would-be putative class members in the class-action lawsuit), consisting of twenty-five Dutch pension funds, two German pension funds and one Luxembourg fund (the foreign Individual Plaintiffs) filed individual actions in the New Jersey federal district court. The actions were consolidated with the class-action lawsuit.

101. *In re Royal Dutch/Shell Transp. Sec. Litig.*, 522 F. Supp. 2d 712, 724 (D.N.J. 2007).

102. Not all courts have been moved by the existence of alternative remedies or even a parallel suit. In *DiRienzo v. Philip Servs. Corp.*, 294 F.3d 21 (2d Cir. 2002), the proposed class involved all purchasers of stock and call options in a suit against a Canadian defendant for massive fraud with respect to stock traded on both U.S. and Canadian exchanges. *Id.* at 26. Related litigation had been initiated in Canada by a class of Canadian plaintiffs. *Id.* at 27. The district court granted defendant's motion to dismiss on grounds of forum non conveniens, but the Second Circuit reversed (2-1). *Id.* at 33–34. The court held that the Canadians who bought their stock in Canada were a small minority of the proposed class, and thus the United States had a greater interest in hearing the case. *Id.* at 31. The court also stated that a U.S. court would likely apply Canadian law to claims by nonresident class members based on the purchase of securities outside the United States. *Id.*

may depend in part on what procedures for settlement or adjudication exist in the foreign forum.

The *Vivendi* and *Dutch Shell* cases reveal the significance of the context in which the questions of "recognition" or "alternative remedy" arise. In *Dutch Shell*, the lack of prescriptive jurisdiction meant that no foreign investors—neither large institutional investors on their own nor small investors as part of a class—could bring a federal lawsuit under the U.S. securities laws. By contrast, in *Vivendi*, the issue of recognition of a U.S. class-action judgment arose on a motion for class certification in the context of whether the foreign investors were to be part of a worldwide class. Because the court concluded that a class-action judgment would not be recognized in Germany, the court found lack of superiority for purposes of FRCP 23(b)(3) and determined that certain foreign investors—for example, the German investors—could not be part of any class. However, since in the earlier *Vivendi* decision the court held that there was prescriptive jurisdiction, it was still possible for large German or Austrian institutional investors to bring their own individual suits in the United States. Of course, another doctrine, such as forum non conveniens, might still be used to dismiss such a case in favor of an alternative forum.

Perhaps we read too much into the *Royal Dutch Shell* case, but certainly one has to see the Dutch settlement as influencing the court in its decision about the extraterritorial reach of the securities laws. Plaintiffs, of course, view the settlement as an end-run around securities-fraud class-action lawsuits and merely a transnational "reverse auction" that we have often seen in the domestic context.[103] And, of course, since the effect of the Dutch Settlement Act is not to settle a Dutch proceeding but rather a U.S. proceeding, there is something to that claim. On the other hand, whether one speaks of prescriptive comity as did the Supreme Court in *Empagran* or of the reasonableness factors in the *Restatement (Third) of Foreign Relations Law*, the availability of an alternative remedy has implications for the exercise of prescriptive jurisdiction as well as for the FRCP 23(b)(3) superiority on a motion for class certification.

It is interesting, therefore, to look at some of the mechanisms in other countries. For example, in 2005, Germany passed the Capital Investors' Model Proceeding Law (KapMuG), which provides for designation of a "model case" in actions by investors for false,

103. *See* John C. Coffee, Jr., *Class Wars: The Dilemma of the Mass Tort Class Action*, 95 COLUM. L. REV. 1343, 1354 (1995) ("[S]uspect settlements result in large measure because of the defendants' ability to shop for favorable settlement terms, either by contacting multiple plaintiffs' attorneys or by inducing them to compete against each other. At its worst, this process can develop into a reverse auction, with the low bidder among the plaintiffs' attorneys winning the right to settle with the defendant.").

misleading, or omitted public capital-markets information or shareholder actions for specific performance in actions brought under the Securities Acquisition and Takeover Act.[104] The model case proceeds and then all individual cases are decided on the basis of the model-case decision.

A mechanism similar to a model case was introduced in England in 2000,[105] enabling a court to issue a Group Litigation Order (GLO) for claims arising out of related issues of fact or law. Parties who want to join the group litigation must affirmatively opt in to the litigation, and thus a claimant who wishes to participate in a group action must register or be registered by the court. Moreover, if the group loses, a group member is liable to pay an equal proportion of common costs as well as costs pursuant to any cost-shifting in the English "loser-pays" system.[106] But, it is unclear what the efficacy of the GLO procedure will be in securities litigation.[107]

Several other countries have class-action mechanisms closer to those in the United States, but still different in significant ways. A Swedish act went into effect in January 2003 that allows individual class-action lawsuits by a plaintiff class member for both injunctive and monetary relief.[108] The Swedish legislation requires that the class be "appropriately defined," that there be common factual circumstances, and that the action be manageable and superior to other alternatives such as joinder and separate "actions by the members of the group."[109] But in contrast to the American class-action lawsuit, under the Swedish procedure, class

104. *See* Kapitalanleger-Musterverfahrensgesetz [KapMuG] [Act on the Initiation of Model Case Proceedings in Respect of Investors in the Capital Markets], Aug. 2005, BGBI. I S. 2437 at 16, *available at* http://www.bmj.bund.de/files/-/1110/KapMuG_english.pdf. The legislation was sparked by the large settlement of the U.S. shareholder class-action lawsuit in favor of U.S. shareholders brought against Deutsche Telekom, whereas German claimant shareholders had no such redress.

105. *See* CIVIL PROCEDURE RULES (U.K.) 19.10–.12 (2008) (providing a set of rules to deal with group litigation). Some mechanism for the consolidation of common claims was thought necessary since the traditional "representative action" in England, *see id.* at 19.6, is construed very narrowly such that "the interests of the representatives and represented [must be] virtually the same." ADRIAN ZUCKERMAN, ZUCKERMAN ON CIVIL PROCEDURE: PRINCIPLES OF PRACTICE 511 (2d ed. 2006).

106. *See* ZUCKERMAN, *supra* note 105, at 525–27.

107. The GLO was held inappropriate as a means to seek redress for the misselling of investments by financial advisers. Press Release, Reynolds Porter Chamberlain LLP, High Court Judgment Kills Hopes of US Style Class Actions for Split-cap Mis-selling (Mar. 17, 2006), *available at* http://www.rpc.co.uk/Default.aspx?sID=755&cID=17&ctID=43&lID=0.

108. Group Proceedings Act (Svensk författningssamling [SFS] 2002:599) (Swed.), *available at* http://www.sweden.gov.se/content/1/c6/02/77/67/bcbe1f4f.pdf.

109. *Id.* § 8 (noting special preconditions for proceedings).

members must opt in to be a member of the class.[110] Both Canada, specifically in Ontario,[111] and Australia[112] have class-action lawsuits generally as well as particular provisions for securities class-action lawsuits.[113] The standards of liability are slightly different from those in the United States, and the loser-pays rules may discourage litigation.[114]

The European collective-action mechanisms are substantially different from the U.S. class-action lawsuit, but they do suggest a different model of adjudication for multiple claims. They may also affect how courts in the United States evaluate whether they should extend their laws to basically foreign transactions and whether to allow class suits embracing investors and shareholders who may have a remedy, albeit a more limited one. It is also interesting to note that the European Commission has been looking at options for introducing collective-action mechanisms for Europe, one relating to the enforcement of consumer protection and the other to enforcement of competition law.[115] Concern about investor fraud and shareholder litigation may not be far behind.

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110. Under Sweden's opt-in system, group members are not parties unless they have intervened as parties. Only parties are liable for costs. *See* HENRIK LINDBLOM, NATIONAL REPORT: GROUP LITIGATION IN SWEDEN 13 (Dec. 6, 2007) (presented at The Globalization of Class Actions, a conference held in Oxford, England from December 12–14, 2007), available at http://globalclassactions.stanford.edu/PDF/Sweden_National_Report.pdf.

111. Securities Act, R.S.O., 1990, ch. S.5 (as amended by Bill 198, effective Jan. 1, 2006), *available at* http://www.ontla.on.ca/bills/bills-files/37_Parliament/Session3/b198ra.pdf.

112. Australian Securities and Investment Commission Act, 2001 § 12GM, *available at* http://www.austlii.edu.au/au/legis/cth/consol_act/asaica2001529/s12gm.html.

113. For further discussion of these provisions, see Gary L. Gassman & Perry S. Granof, *Global Issues Affecting Securities Claims at the Beginning of the Twenty-First Century*, 43 TORT TRIAL & INS. PRAC. L.J. 85, 87–94 (2007).

114. *See, e.g.*, *Kerr v. Danier Leather, Inc.*, [2007] 286 D.L.R. 601 (Can.), *available at* http://csc.lexum.umontreal.ca/en/2007/2007scc44/2007scc44.html (upholding a lower court's award of costs against the representative plaintiff under section 31(1) of the Ontario Class Proceedings Act, 1992 and stating, "[P]rotracted litigation has become the sport of kings in the sense that only kings or equivalent can afford it. Those who inflict it on others in the hope of significant personal gain and fail can generally expect adverse cost consequences.").

115. *See* COMM'N OF THE EUR. CMTYS., WHITE PAPER ON DAMAGES ACTIONS FOR BREACH OF THE EC ANTITRUST RULES 4 (April 2, 2008), *available at* http://ec.europa.eu/competition/antitrust/actionsdamages/files_white_paper/whitepaper_en.pdf (suggesting representative actions brought by certain qualified entities and opt-in collective actions in the area of antitrust law); JULES STUYCK ET AL., CTR. FOR EUR. ECON. LAW, AN ANALYSIS AND EVALUATION OF ALTERNATIVE MEANS OF CONSUMER REDRESS OTHER THAN REDRESS THROUGH ORDINARY JUDICIAL PROCEEDINGS 260–321 (2007), *available at* http://ec.europa.eu/consumers/redress/reports_studies/comparative_report_en.pdf (assessing whether collective action for damages for consumers is "practical and effective").

II. AN EXCHANGE-BASED RULE

The Introduction and Part I of this Paper highlight the uncertainty that has characterized the U.S. approach to prescriptive jurisdiction in transnational securities cases. The conduct and effects tests themselves are complicated, and the introduction of other transnational issues, such as concerns about recognition of judgments and the availability of alternative remedies, have led to even more confusion and lack of predictability. The proliferation of class-action lawsuits in the foreign cases and the issue of whether there should be a heightened jurisdictional showing in f-cubed class-action lawsuits introduce yet another complication. Our own approach argues for greater clarity and certainty, and is directed to the regulatory authority over the exchange.

Of course, easy cases do exist for determining U.S. prescriptive jurisdiction. Consider a foreign issuer with solely foreign investors buying and selling securities entirely in a foreign marketplace. Suppose the issuer's management releases inflated revenue numbers (prepared outside the United States), which harms solely foreign investors purchasing the issuer's now overinflated securities. In this case, no reason exists to apply U.S. securities protections. No conduct takes place in the United States, and no effects occur that directly impact U.S markets.[116] The interest of the United States in regulating such transactions is at a minimum; the interests of the home countries of the issuer and the foreign investors to regulate the transaction are at a maximum. Now consider a U.S. issuer with solely U.S. investors buying and selling securities entirely on the NYSE. In this case, when the issuer's management releases inflated revenue numbers (prepared inside the United States), the conduct and effects tests both point toward applying jurisdiction. The U.S. interest in regulating the transaction is at a maximum; correspondingly, the interests of other countries are at a minimum.

Not all transactions are so clearly cut. A U.S. issuer may disclose misleading information that affects foreign investors trading in a foreign marketplace. Similarly, a foreign issuer may disclose information in the United States that affects investors trading in the United States as well as abroad. How should the U.S. antifraud liability under rule 10b-5 apply to these varied transactions? In particular, we ask in the f-cubed case of a foreign issuer with securities trading both in and outside the United States whether the class should include not only investors who

116. As discussed below, indirect effects are possible. For instance, U.S. companies in competition with a foreign issuer may be affected by the foreign issuer's fraud.

trade in the United States, but also foreign investors who trade outside the United States.

A. An Exchange-Based Jurisdictional Rule

Class-action lawsuits aggregate large numbers of transactions. The aggregation allows plaintiffs to bring claims that otherwise would be too small to justify the costs of litigation. Without a class-action lawsuit, many individual investors would likely not litigate their rule 10b-5 claims at all. Because of the collective aspect of class-action lawsuits, the effectiveness of class-action lawsuits as a device to deter fraud for one subset of investors (investors trading domestically) may be tied to whether another subset of investors (foreign investors trading abroad) have prescriptive jurisdiction.

The present conduct test for extraterritorial jurisdiction ignores the collective aspect of class-action deterrence. Instead, decisions under the conduct test have justified the extension of securities extraterritorial jurisdiction as a means of protecting the reputation of the U.S. capital markets among foreign investors. Without the extension of U.S. jurisdiction, foreign investors will come to view the United States as a safe haven for fraud,[117] reducing the ability of U.S. companies (tainted by their association with the United States) to raise capital abroad. In addition, other countries may choose not to deter fraud within their own borders that may affect the United States if the United States adopts a lax attitude toward fraudulent conduct that takes place, at least in part, on U.S. soil.

The fraud safe-haven argument depends on the assumption courts make about how foreign investors and others abroad form their views as to who is responsible for committing fraud (and failing to regulate to deter fraud). It is unclear why investors would associate the United States and its regulatory regime with fraud perpetrated by a foreign issuer solely because some conduct relating to a foreign issuer's fraud occurs within the United States. Even if the degree of conduct in the United States is significant, if investors (and others) attribute the fraudulent statements to a foreign-based issuer, we argue that a reasonable assumption (but only an assumption as we discuss below) is that foreign investors and others abroad will not associate the fraud with the U.S. regime, but instead with the home regime governing the foreign issuer. If a French company makes a misleading statement that

117. In *IIT v. Vencap, Ltd.*, for example, the Second Circuit wrote that the United States should not be "used as a base for manufacturing fraudulent security devices for export, even when these are peddled only to foreigners." 519 F.2d 1001, 1017 (2d Cir. 1975).

affects French investors in France, investors will focus on the responsibility of the French regulatory regime in failing to police the French issuer, even if some of the conduct behind the French company's disclosure occurred in the United States. Under this view of what constitutes conduct, who the public views as speaking (making the misleading statement) is qualitatively more important than other forms of conduct, and determinative of whether extraterritorial jurisdiction should apply under the conduct test.

The Second Circuit in *Morrison*, as discussed above, adopted a similar view of conduct and the importance of who makes the fraudulent statements to the public. The *Morrison* court wrote:

> 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 [National Australia Bank]'s corporate headquarters, which issued the statements, than to those of [the U.S. subsidiary], 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)."[118]

Although a U.S. subsidiary of the National Australia Bank (a foreign issuer) hatched the scheme and initiated the fraudulent conduct in the United States that directly resulted in overstated revenues, the Second Circuit in *Morrison* labeled the conduct as "merely preparatory" because National Australia Bank, and not the U.S. subsidiary, was responsible for and made the misleading statement to the investing public. Under this view of the conduct test, so long as a foreign issuer is responsible for the misleading statement at issue (and engages in the ultimate decision to release misleading information to the public abroad), the conduct test will point toward not extending rule 10b-5 jurisdiction even if other decisions occurred in the United States that led up to the fraud. *Morrison* viewed those other decisions as not giving rise to rule 10b-5 liability, even if they were deceptive and a necessary causal factor behind the fraud. The *Morrison* court stressed that the actions of the U.S.-based subsidiary were too remote in the chain of causation. In doing so, *Morrison* imported the views expressed by the Supreme Court in *Stoneridge Investment Partners, LLC v.*

118. *Morrison v. Nat'l Aust. Bank Ltd.*, 547 F.3d 167, 176 (2008) (quoting *Wright v. Ernst & Young LLP*, 152 F.3d 169, 175 (2d Cir. 1998)). 519 F.2d 974, 989 (2d Cir. 1975).

Scientific-Atlanta, Inc.,[119] on the separate issue of who can be a proper defendant in a rule 10b-5 class-action lawsuit (depending heavily on the notion of reliance on a statement by investors) into the conduct test of extraterritorial prescriptive jurisdiction.

Of course, *Morrison* is only one case (albeit a significant one). Another court, analyzing the same facts, might have decided the case differently and found prescriptive jurisdiction because the initial decision to commit fraud originated in the U.S. subsidiary and took place in Florida. Importantly, how a court will decide the conduct test in the future turns on the court's specific assumptions about how foreign investors and others outside the United States make determinations on who is ultimately responsible for fraud. If a court believes, as the Second Circuit apparently does, that foreign investors hold the actual party making the fraudulent statement (the foreign issuer in the *Morrison* case) responsible even if some conduct occurs in the United States, then the conduct test of extraterritorial jurisdiction focuses on the location and actions of the ultimate speaker. In the typical case where the foreign issuer makes the decision to disclose abroad and then disseminates misleading information abroad, no jurisdiction will apply under *Morrison* regardless which precursor steps took place in the chain of causation in the United States. On the other hand, if a court believes that foreign investors will hold a U.S.-based party who engages in significant conduct in the United States responsible, even for a foreign issuer's statements (such as making the initial decision to commit fraud as did the U.S. subsidiary of the foreign issuer in *Morrison*), then the conduct test will point to extending jurisdiction extraterritorially to cover the foreign issuer. Because the conduct test turns so much on assumptions on how foreign investors and others abroad form views on fraud responsibility, the amount and importantly the qualitative type of conduct that must occur in the United States to trigger the conduct test is uncertain. Because such assumptions lack empirical support and are simply ad hoc on the part of specific courts, litigants face difficulty in predicting the application of the conduct test.

Given the deficiencies of the conduct test, we instead start directly from a U.S.-investor-welfare perspective. Our focus is on ensuring adequate deterrence where necessary to prevent negative effects on U.S. investors and markets. Using this perspective, we argue for jurisdiction based on the country that regulates the exchange on which

119. 128 S. Ct. 761 (2008). *Morrison* itself cites *Stoneridge*. *See Morrison*, 547 F.3d at 177.

the transaction takes place: an exchange-based rule.[120] Under such a regime, courts should presumptively exclude all foreign investors who engage in transactions on exchanges other than U.S. exchanges from U.S. class-action lawsuits.[121] Compared with the existing conduct or effects tests, an exchange-based presumptive rule for prescriptive jurisdiction provides a more certain method of applying jurisdiction that better protects the interests of U.S. investors and markets.

Applying the traditional effects test to determine whether to apply U.S. jurisdiction is problematic for class-action lawsuits. As with the conduct test, courts lack clear guidance in how to apply the effects test. As discussed above, courts, such as in *Morrison*, at least make reference to the possibility of the effects test as a means for extraterritorial jurisdiction for f-cubed plaintiffs.[122] On the other hand, many courts simply refuse to accept the possibility that information that affects prices for a company's securities in an overseas market may have an effect on the prices for the same company's securities in a trading market within the United States.[123] This refusal results from a desire to restrict extraterritorial jurisdiction and rests on the increasingly untenable fiction that markets are separate—despite the growing linkages between worldwide securities markets and the presence of arbitrageurs ready to profit from price discrepancies across different markets. Rather than perpetuate this fiction, we argue that the decision to extend (or not extend) extraterritorial jurisdiction should explicitly address the issue of effects on U.S. investors and markets.

So what types of effects are substantial enough to trigger U.S. jurisdiction? We argue that the answer should derive from the underlying goal of applying the securities laws: to protect U.S. markets and investors. To determine the effect on U.S. investors, we argue, courts should look at the degree to which U.S. investors are directly harmed by a foreign issuer's misleading statement. In an f-cubed case, if no U.S. investors are present in the class, then it is unlikely that the misleading statements had much direct effect on U.S. markets. In

120. In an earlier article, one coauthor argued for such an approach to rule 10b-5 prescriptive jurisdiction for the general, non-class-action situation. *See* Stephen J. Choi & Andrew T. Guzman, *The Dangerous Extraterritoriality of American Securities Law*, 17 NW. J. INT'L L. & BUS. 207, 208 (1996).

121. For purposes of this Paper, we do not address the issue of whether U.S. investors who trade the securities of foreign issuers in foreign markets should also be excluded from rule 10b-5 class-action lawsuits. While strong arguments exist that an exchange-based approach to jurisdiction should also apply for U.S. investors (resulting in exclusion), we leave this analysis for future work.

122. *See supra* notes 28–46 and accompanying text (discussing the *Morrison* opinion).

123. *See supra* notes 60–61.

contrast, if a significant proportion of U.S. investors is present in an f-cubed class, then a foreign issuer's misleading statement is much more likely to have a greater effect on the U.S. markets. However, once we measure effects based on the degree to which U.S. investors are present in the class, extraterritorial jurisdiction is generally not needed to protect the interests of U.S. investors. In a class-action lawsuit, a large U.S. investor presence (sufficient to trigger jurisdiction under an effects test) may in and of itself generate incentives for private plaintiffs' attorneys to bring a class-action lawsuit, irrespective of the presence of foreign investors in the class. The larger the U.S. effects, in other words, the less need for extraterritorial jurisdiction in a class-action lawsuit because private plaintiffs' attorneys will be more likely to bring a class-action lawsuit to directly enforce the interests of U.S. investors.

Plaintiffs' attorneys are profit motivated and will only bring a class-action lawsuit where the expected benefits outweigh the costs. The presence of a subset of U.S. investors with prescriptive jurisdiction—even if an exchange-based rule of jurisdiction excludes foreign investors trading abroad—will give plaintiffs' attorneys incentives to file a class-action lawsuit. Of course, the incentive will not be as great as if the class includes both foreign investors trading abroad and domestic investors. To assess the incentive for private deterrence if only investors transacting within a U.S. securities exchange are allowed in an f-cubed class-action lawsuit, we need to establish a baseline of comparison. As our baseline of comparison we use the level of private liability, and thus deterrence against fraud, available through the U.S. securities regime for domestic issuers with an equivalent volume of U.S.-located trading.

Consider two publicly traded and well-followed companies. The common stock of domestic Company *A* is traded solely inside the United States by U.S. investors and has a market capitalization of $1 billion. The common stock of foreign Company *B*, in contrast, is traded both in the United States and outside the United States. Assume that 25 percent of the trading volume for Company *B* stock occurs inside the United States (involving securities of Company *B* with a market capitalization of $1 billion), and 75 percent outside the United States by foreign investors (involving securities with a market capitalization of $3 billion). Assume also that Company *B*'s total trading volume is four times the total trading volume for Company *A* (due to the larger total market capitalization for Company *B*'s shares). The CEOs of companies *A* and *B* both make decisions to allow their respective companies to disclose overinflated historical earnings through a public press release. Assume that the CEOs of both companies approve the fraudulent disclosures as a means to increase the stock prices of their respective companies, resulting in greater stock option compensation for the CEOs.

While the global impact of fraud on investors is greater in the case of foreign Company *B* (due to its higher market capitalization and corresponding total trading volume), the U.S.-specific impact is approximately the same magnitude as for domestic Company *A*. If the fraud overvalues the stock of both companies by 10 percent, U.S. investors of both companies *A* and *B* are harmed by $100 million: an equivalent effect on U.S. investors and markets. Excluding the investors who transact outside the United States from a class-action lawsuit brought against Company *B* thus equalizes the size of the class, the amount of potential damages, and the incentives of plaintiffs' attorneys to bring a class-action lawsuit in the first place against companies *A* and *B*. Indeed, providing for extraterritorial jurisdiction would perversely lead to a much greater level of private class-action deterrence against fraud for a foreign issuer, compared with a domestic issuer with an equal level of effect on U.S. markets.[124]

A jurisdictional rule that presumptively excludes foreign investors transacting abroad results in a class-action lawsuit brought solely for the direct effects on U.S. investors and the U.S. capital markets. Unlike the more uncertain effects test, an exchange-based rule would precisely vary the private incentives for securities class-action lawsuits based on the level of U.S.-located trades in the foreign issuer. The greater the U.S.-based investor interest, the larger the class size and the greater the corresponding incentive of plaintiffs' attorney to file a class-action lawsuit. Moreover, the incentive is matched with the incentive for a domestic company with an equivalent U.S. investor base, leading to a similar level of deterrence from securities class-action lawsuits in the United States (at least with respect to U.S. companies with an equal level of investor transactions that occur in the United States).

Several criticisms can be directed at an exchange-based jurisdictional rule that presumptively excludes foreign investors who carry out their transaction outside the territorial United States in f-cubed class-action lawsuits. First, the private securities class-action regime that applies for U.S. domestic issuers and investors—used as the baseline for our analysis—may not be the right or optimal level of private liability to deter fraud. Nonetheless, assessing whether jurisdictional choices involving f-cubed foreign investors achieve at

124. In our numerical example, if a class-action lawsuit included all investors of Company *B* (representing a market capitalization of $4 billion), the potential damages from a class-action lawsuit would be four times that for domestic Company *A* (with a market capitalization of only $1 billion and an assumed one-fourth trading volume of Company *B*). Even though the effect on U.S. investors is the same due to the equal level of U.S.-based market capitalization and trading, plaintiffs' attorneys would have four times greater incentive to bring a class-action lawsuit against Company *B* compared with Company *A* (to obtain higher fees), all other things being equal.

least the same level of private deterrence under the U.S. regime as for domestic U.S. issuers with a similar level of U.S. investor ownership allows us to determine whether these jurisdictional choices adversely affect (or do not affect) the welfare of U.S. investors. Using this baseline, we argue that applying an exchange-based rule provides certainty and an equivalent level of deterrence for U.S. investors of foreign issuers as domestic-issuer companies with the same quantity of U.S.-based investor holdings. If the level of private enforcement is not optimal from a societal perspective, due for example to the presence of frivolous litigation,[125] Congress should address this concern with a reform that affects both domestic and foreign issuers equally.

Second, not all harms to U.S. investors in f-cubed situations will lead plaintiffs' attorneys to file suit (or even if they file suit, pursue the case vigorously), particularly where the amount of U.S.-investor trading volume is small. But, this is the case for domestic U.S. issuers as well. U.S. domestic issuers with a small market capitalization that provides only limited potential damages rarely face securities class-action lawsuits. Evidence exists that private plaintiffs' attorneys do not bring suit against smaller U.S. issuers where the potential damages are lower, irrespective of the possibility of fraud.[126] Private enforcement is not the only mechanism of fraud deterrence in the United States. Just as the SEC should focus on U.S. issuers with small market capitalization (because of the dearth of private enforcement), under our proposed territorial rule of jurisdiction, the SEC may also wish to focus its public enforcement efforts on foreign issuers with relatively small U.S.-based trading.

Third, the level of private deterrence incentives under an exchange-based rule of jurisdiction for an f-cubed class-action lawsuit may not always be equivalent to a domestic-issuer class-action lawsuit with a similar U.S-investor base. To the extent a U.S. domestic issuer also has a significant foreign investor base transacting abroad, and class-action lawsuits in the United States include such foreign investors, excluding foreign investors from f-cubed litigation will no longer generate an equivalent level of private deterrence. If our domestic

125. Many have written on the possibility of frivolous lawsuits. *See, e.g.*, Janet Cooper Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STAN. L. REV. 497, 501 (1991); Stephen J. Choi, *Do the Merits Matter Less After the Private Securities Litigation Reform Act?*, 23 J.L. ECON. & ORG. 598, 612 (2007); Marilyn F. Johnson et al., *Do the Merits Matter More? The Impact of the Private Securities Litigation Reform Act*, 23 J.L. ECON. & ORG. 627, 627 (2007).

126. For evidence that smaller-sized firms face a lower incidence of securities class-action lawsuits, see James Bohn & Stephen Choi, *Fraud in the New-Issues Market: Empirical Evidence on Securities Class Actions*, 144 U. PA. L. REV. 903, 928–45 (1996); Choi, *supra* note 125, at 606–13.

Company *A*, in the example above, also has $10 million of common stock trading abroad, then the total amount of Company *A* securities that may potentially come within a class-action lawsuit ($1.01 billion) will exceed the U.S.-investor-only component of the foreign issuer Company *B* (equal to $1 billion) eligible for a class-action lawsuit under a territorial rule, despite the equal amount of U.S. market interest in both companies. It is unclear, however, the magnitude of this difference. The difference only exists for U.S. companies with significant foreign trading in their securities.[127] Another divergence between the private deterrence incentives under an exchange-based rule lies with the expense of litigation. Even if the potential damages are the same for a domestic and foreign issuer with an equivalent amount of U.S.-based trading, plaintiffs' attorneys may find it more costly to prosecute a class-action lawsuit against foreign issuers due to language translation, transport, and other costs of litigating against a distant, foreign defendant. Such costs may result in a lower degree of private deterrence against foreign issuers under our exchange-based jurisdictional rule, compared with a U.S. issuer with a similar U.S. investor base, all other things being equal. As plaintiffs' attorney firms go global, such cost concerns will become minimized.[128]

Fourth, even if the level of private incentives on the part of plaintiffs' attorneys to bring a class-action lawsuit are equivalent under an exchange-based rule for U.S. and foreign issuers with equal levels of U.S.-based trading, excluding foreign-based investors from a class-action lawsuit for foreign issuer Company *B* may still result in lower levels of fraud deterrence for the foreign issuer (negatively affecting U.S. investors trading in the securities of the foreign issuer). In particular, the incentives to commit fraud for managers at Company *B* will be greater than those for managers at domestic issuer Company *A* due to the larger non-U.S. market capitalization in the hands of foreign investors of Company *B*. While the benefit of committing fraud to managers is not directly linked to the size of the trading market, indirect benefits tied to overall, global market capitalization nonetheless exist. Insiders interested in insider trading will be better able to hide their insider trades the greater the size

127. One could argue that under a territorial rule of jurisdiction, we should exclude foreign transactions from class-action lawsuits involving even domestic issuers. Because our focus in this Paper is on f-cubed litigation, we leave this analysis for future work.

128. For example, Labaton Sucharow LLP, a plaintiffs' attorney firm, has entered into alliances and "cooperation relationships" with law firms in Germany, Italy, the Netherlands, France, England, Canada, and Australia with the goal of creating "a truly international law practice." *See* Labaton.com, International Presence, http://www.labaton.com/en/about/international/International-Presence.cfm (last visited Mar. 10, 2009).

of the trading markets for the company's securities. The ability of a company to use its stock for acquisition purposes will also depend on the liquidity of the company's secondary markets. A company with a small secondary market will have a more difficult time using its stock as consideration than a company with a much larger secondary market. Thus, the incentive to commit fraud will be lower for the domestic issuer (Company *A*) compared to a foreign issuer with an equivalent level of U.S. trading plus additional non-U.S.-based trading (Company *B*).[129] An exchange-based jurisdictional rule that excludes the investors engaged in non-U.S. trading from a rule 10b-5 class-action lawsuit may therefore underdeter foreign-issuer managers from committing fraud.

Despite the theoretical possibility that an exchange-based rule of jurisdiction may result in incrementally lower deterrence for foreign issuers compared with domestic issuers with the same level of U.S.-market interest, this effect typically will not justify extending jurisdiction to those investors who transact outside the United States. Where a foreign issuer has the same U.S.-trading volume as a domestic issuer, the level of private incentives to bring a class-action lawsuit under an exchange-based jurisdictional rule will be, at a first-order level, roughly equivalent. As discussed above, differences in private deterrence may exist due to greater expenses on the part of plaintiffs' attorneys to sue foreign issuers, the possibility of foreign-investor class members for domestic issuers, and greater incentives for managers of foreign issuers to commit fraud where the U.S. market interest is equivalent but the foreign issuer has a greater worldwide market capitalization.

Such differences, however, are likely only second-order differences. In particular, including foreign investors in an f-cubed class-action lawsuit may not be necessary for adequate deterrence. For secondary-market fraud, the measure of damages under a rule 10b-5 lawsuit is not tied to the benefit to those committing the fraud. Instead, the damages turn on the amount of secondary-market trading that takes place during the class period, as well as the stock-price drop attributable to the fraud in question. An insider, for example, may decide to overstate a company's revenues to profit from insider sales of the company's securities. Suppose these insider-trading profits equal $10 million based on sales of one million shares. The rule 10b-5

129. For example, a manager of foreign Company *B* (discussed as an example above in the text) will have a much easier time engaging in insider trading because of the overall larger market capitalization of Company *B* (which will make it harder for outsiders to detect relatively small amounts of insider trading) compared with domestic Company *A*, even though both companies have a similar U.S.-based market capitalization.

damages, however, will not be limited to this $10 million profit. Instead, if fifty million shares change hands (mostly from one outside investor to another outside investor) during the class period, then the insider and company may face rule 10b-5 damages of $500 million. The rule 10b-5 damage measure for secondary-market fraud is not tied precisely to the benefit of the wrongdoer—and typically far exceeds the benefit—resulting in overdeterrence.[130] Removing foreign investors from the class is therefore unlikely to reduce deterrence appreciably (since the level of deterrence is already likely excessive) where U.S. investors still are present in the class.[131]

Moreover, where effective alternative remedies exist in other countries, deterrence may not require the application of U.S. class-action-style private enforcement for foreign investors (and indeed, doing so may result in greater deterrence against fraud for foreign issuers compared with domestic issuers with a similar U.S. investor base). Lastly, if achieving an exact level of deterrence equivalent between foreign issuers and domestic U.S. issuers is important, we argue below that the SEC can take such considerations into account in making exceptions to the general exchange-based jurisdictional presumption we argue that courts should apply.

130. Because not all fraud is detected, damages for fraud should exceed the benefit to the wrongdoer for "optimal" deterrence. *See* Gary S. Becker, *Crime and Punishment: An Economic Approach*, 76 J. POL. ECON. 169, 198–99 (1968). The disconnect between secondary-market damages and the benefit to wrongdoers is so large (and uncertain), however, that overdeterrence is likely.

131. For a discussion of securities damages under rule 10b-5, see Janet Cooper Alexander, *Rethinking Damages in Securities Class Actions*, 48 STAN. L. REV. 1487 (1996). Of course, if private litigation tends to reach settlements where individual officers and directors do not pay much (if anything) out of their personal resources into the settlement fund, rule 10b-5 may not result in overdeterrence (and may actually underdeter fraud). However, this problem is not unique to f-cubed litigation—but rather affects all private class actions under rule 10b-5. Congress or the SEC should devise a more general solution that addresses this problem for all types of rule 10b-5 class-action litigation (such as increasing public enforcement against directors and officers).

Primary market fraud (involving sales directly by an issuer to investors) poses a different situation. Unlike secondary-market fraud, in a purely primary-market rule 10b-5 class-action lawsuit, the damages paid by the issuer will correspond to the trading losses of investors who purchase from the issuer. Few rule 10b-5 class-action lawsuits, however, are brought solely for primary-market fraud. Even if a primary-market fraud component is present, the class typically also includes those who transact in the secondary market in the period immediately following the primary offering. Moreover, given the incentive already in place for plaintiffs' attorneys to bring a lawsuit to the extent primary-market purchases occur inside the United States and the uncertainty facing issuers and investors of not taking a bright-line-rule approach, we argue for an exchange-based jurisdictional presumption even if a rule 10b-5 class-action lawsuit includes a primary-securities-transaction component.

B. Other Considerations

Looking beyond the traditional conduct and effects doctrines of prescriptive jurisdiction, an exchange-based rule of jurisdiction provides several other benefits. Using the regulatory authority over the exchange as a proxy for the application of rule 10b-5 provides an easily understandable and, importantly, intuitively appealing rule for investors. The trigger for the exclusion is a transaction outside the United States. This trigger is likely to comport with most investors' a priori views on when the U.S. laws apply (i.e., primarily inside the United States). If an investor travels to Japan to purchase securities on the Tokyo Stock Exchange, the typical investor will expect that Japanese law applies to the transaction (much like Japanese law applies to other actions the investor may take in Japan, such as driving above the speed limit). Because of the clarity of an exchange-based rule, the chance for confusion is minimized.[132]

A clear exchange-based jurisdictional rule will also facilitate choice among issuers and investors. Not all regulatory protections are value-increasing for issuers and investors. A clear exchange-based rule of jurisdiction will allow issuers and investors to structure their transactions to apply rule 10b-5 where the benefit to both parties jointly from rule 10b-5 (in the form of increased deterrence against fraud) outweighs the cost of applying rule 10b-5 (including, for example, the possibility of frivolous lawsuits). Issuers that desire to avoid rule 10b-5, for example, may issue securities solely outside the United States. The choices issuers make will place competitive pressure on U.S. regulators to provide antifraud protections that maximize the joint welfare of issuers

132. Securities transactions, on the other hand, are becoming increasingly fragmented. An investor in London may place a purchase order for a company's securities; the order may get executed in any number of possible securities markets, including markets in the United States. Fragmentation may make it difficult to trace the exchange where a particular transaction occurs with a specific foreign investor. It is unclear nonetheless how far markets will become fragmented. Liquidity benefits exist from having large amounts of securities all within one market. Even where tracing is a problem, courts could shift the burden to the plaintiffs to demonstrate tracing. If the possibility of securities enforcement is valuable to investors, the market will respond to such a burden with a greater paper trail for transactions to enable tracing. Note also that fragmentation is a potential problem not only for our exchange-based proposal but also for the present conduct and effects tests. The application of the conduct and effects tests also relies on distinctions between transactions that occur inside and outside the United States. Whether a transaction is an f-cubed or non-f-cubed situation turns in part on the location of the transaction. *See* Donald C. Langevoort, *U.S. Securities Regulation and Global Competition*, 3 VA. L. BUS. REV. (forthcoming 2009) (arguing that increased fragmentation of securities order flow will diminish the incentives of any single national regulator to "devote precious resources to policing issuer disclosure simply based on the fact that some (varying) percentage of issuer stock is traded there").

and investors. With a clear rule, issuers and investors may structure their transactions to apply the level of regulatory protection they desire. Foreign issuers who wish to avoid U.S. securities-fraud class-action lawsuits may either choose not to list on a U.S. securities exchange or, alternatively, limit the amount of trading in the issuers' securities that takes place in the United States.[133] As issuers and investors shift their transactions to account for the level of regulatory protection, regulators will come under competitive pressure to cater protections toward maximizing the joint welfare of issuers and investors.[134]

Second, adopting an exchange-based presumption such as the one we suggest limits the role of judges as decision makers. Rather than have courts attempt to identify those situations where the conduct in question has directly caused the losses abroad and then balance that factor along with concerns of comity, preclusive effect of judgments, and the availability and adequacy of other remedies, an exchange-based rule gives courts a simple rule of thumb to follow in determining prescriptive jurisdiction. The present varied doctrines governing whether U.S. courts should hear rule 10b-5 claims arising out of transnational securities transactions makes it difficult for parties to predict whether U.S. jurisdiction will apply in any given transaction.

Moreover, the current regime where additional transnational concerns enter into the calculus may lead to a result where different judges are likely to arrive at inconsistent jurisdictional determinations based on their own assessments as to whether a country will recognize a U.S. class-action judgment with respect to absent-class members. In *Vivendi*, for example, the district judge found that it was "more likely than not" that a French court would recognize a U.S. judgment and bind absent French class members, thus keeping French investors in the class.[135] In contrast, in a later case, *In re Alstom SA Securities Litigation*,[136] a different district judge—applying the same standard—

133. A foreign issuer, for example, may limit the proportion of securities the issuer raises inside the United States. To the extent the U.S. market is not the main market for the issuer's securities, the trading volume within the United States will likely not increase beyond the proportion of securities issued in the United States.

134. For a more detailed argument on the benefits of regulatory competition under the securities laws, see Stephen J. Choi & Andrew T. Guzman, *Portable Reciprocity: Rethinking the International Reach of Securities Regulation*, 71 S. CAL. L. REV. 903, 922 (1998); Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L.J. 2359, 2419 (1998). For an argument against regulatory competition in securities regulation, see Merritt B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice Is Not Investor Empowerment*, 85 VA. L. REV. 1335, 1395–96 (1999).

135. *In re Vivendi Universal, S.A. Sec. Litig.*, 242 F.R.D. 76, 102 (S.D.N.Y. 2007); *see also supra* Part I.A.1.

136. 253 F.R.D. 266 (S.D.N.Y. 2008).

opined that it was more likely than not that opt-out U.S. class-action judgments would not be recognized in France, and thus excluded French investors from the class.[137] The same inconsistency may occur where a judge in one case concludes that the lack of available remedies in France dictates that French investors be included in the U.S. class, and a different judge may determine that French remedies, even if different, are completely adequate. Relying on judges to make such decisions on a case-by-base basis will result in a varied application of U.S. jurisdiction to French investors without any principled reasons to justify such variations.[138] An exchange-based jurisdictional presumption would bring certainty and predictability to the application of U.S. jurisdiction to securities-fraud class-action lawsuits involving transnational securities transactions.

Lastly, the United States simply lacks the ability to extend its jurisdiction across the world.[139] A rule based on the regulatory authority

137. The district court in *Alstom* distinguished *Vivendi* in that Alstom's articles of association included a forum-selection clause that provided that any dispute between shareholders and the company were to be submitted to the exclusive jurisdiction of the courts where Alstom's registered office was located (i.e., the courts of France), whereas there was no such jurisdiction clause in Vivendi's articles of association. Thus, the district court believed that a French court would view its jurisdiction over French investors' claims as exclusive, and "French courts would likely not recognize any judgment rendered by [the U.S. court] with regard to absent French investors against Alstom." *Id.* at 285. As to the defendants other than Alstom—where there was no forum-selection clause—the district court did find that there was an adequate "characteristic link," but that it was more likely than not that opt-out class-action judgments would not be recognized in France because they would violate French public policy. Thus, the French purchasers were excluded from the class as against the other defendants as well. In distinguishing *Vivendi*, which had rejected the argument that there was a violation of French public policy in light of an "ongoing debate in legal and business sectors" about opt-out class-action lawsuits, the district court in *Alstom* called attention to later developments in France that rejected the concept of such a framework. *Id.* at 287 n.11.

138. Professor Buxbaum, for example, examined a dataset of multinational securities class-action lawsuits filed from 1996 to 2005. She found forty-five f-cubed complaints that included claims based on foreign transactions. Among those cases where foreign claims were excluded from the U.S. litigation, she reported that courts employed a variety of mechanisms to reach their exclusion decision. No one uniform approach was taken. *See* Buxbaum, *supra* note 4, at 40 ("In sixteen cases, all foreign-cubed claims were excluded from the U.S. litigation. Courts used a variety of procedural mechanisms to achieve this result. In several cases, jurisdiction was decided on a 12(b)(1) motion to dismiss the foreign claims for lack of subject-matter jurisdiction. In some cases, the court considered jurisdiction at the certification stage, choosing to certify classes that included only claims based on U.S. market transactions. One case was dismissed on the basis of *forum non conveniens*, and another on the basis of comity.").

139. *See, e.g.*, *Morrison v. Nat'l Aust. Bank*, 547 F.3d 167, 175 (2d Cir. 2008) ("[W]e are an American court, not the world's court, and we cannot and should

of a country over its securities-market would limit the United States to applying the securities laws where it has the power to enforce its laws. The U.S. securities laws already take such an approach to jurisdiction in other areas. For example, under Regulation S, the rules governing public offerings only apply to offerings that take place inside the United States (with various exceptions). Applying a similar rule for rule 10b-5 jurisdiction would provide consistency as to the extraterritorial scope of the U.S. securities regime.

C. Rebutting the Presumption

Our arguments in favor of an exchange-based jurisdictional presumption that excludes foreign investors in f-cubed class-action litigation do not apply uniformly to all foreign issuers. In some cases, for example, the positive spillover effect on U.S. investors from extending jurisdictional protection to foreign investors (in the form of increased deterrence against company fraud) may be of sufficiently large magnitude to warrant extension of rule 10b-5 jurisdiction. This may particularly be the case for issuers who are based in countries without effective protections for investors. Indeed, most countries lack a class-action regime. Even where countries do employ formal class-action mechanisms, few class-action lawsuits are brought.

To take into account the varying strength of the territorial-jurisdiction presumption, we propose that the presumption be rebuttable. We propose that the SEC have the ability to make ex ante determinations about which countries lack effective protections against fraud and therefore may argue for (if comity and other factors warrant) an expansion of U.S. jurisdiction for investors trading in those countries. Taking a country-by-country approach, the SEC may use its resources to investigate whether specific countries respect U.S. judgments involving securities class-action lawsuits. Similarly, the SEC can determine the effectiveness of the securities regime of other countries in providing a remedy for investors trading in those countries. The SEC's determination can also be based on the potential for the preclusive effect and the availability of remedies in the other country. For example, if a country already has a well-functioning class-action system that will not recognize a U.S. settlement or judgment, then the SEC may find no reason to reverse the presumption that investors trading outside the United States should not have rule 10b-5 jurisdiction.

not expend our resources resolving cases that do not affect Americans or involve fraud emanating from America.").

We would only allow the SEC—and not judges—to make ex ante determinations to rebut the exchange-based jurisdictional rule. While judges deciding jurisdictional issues are dispersed and may generate inconsistent results across different cases, the SEC is a centralized decision maker with expertise on securities-enforcement issues. Rather than have judges in disparate courts reinvent the wheel, the SEC can make the determination once and apply this determination consistently for investors trading the securities of a foreign issuer in a particular country.

Importantly, rebutting the exchange-based jurisdictional rule turns primarily on country-level factors. Such country-level factors include the precise amount of risk facing issuers from a lack of preclusion based on a U.S. judgment for the specific countries in which foreign transactions take place. Moreover, whether investors have an alternative remedy in other countries and other comity concerns will also vary based on country-level factors, and not on the facts of a specific case. Of course, some case-level factors are possible. Large numbers of U.S. investors in a specific class-action lawsuit may opt-out, leaving insufficient class members to provide a financial incentive for plaintiffs' attorneys to pursue a rule 10b-5 class-action lawsuit absent the inclusion of foreign investor class members. These case-level factors, however, are difficult to quantify and likely not worth the uncertainty and expense of allowing judges to make case-by-case determinations.

Precedent exists for the SEC making determinations about particular foreign securities markets. The SEC already designates particular organized securities markets as "designated offshore securities markets" for purposes of determining "offshore transactions" under Regulation S (the territorial-based exemption from the public-offering requirements of the U.S. securities laws).[140] Unlike courts, the SEC may also negotiate with regulators in other countries. Leaving it to the SEC to determine the reach of U.S. class-action lawsuits provides one agent with which foreign governments can negotiate. Rather than leave determinations of extraterritorial jurisdiction to unilateral actions by countries, allowing the SEC to respond to rebuttals of the presumptive rule of jurisdiction will encourage bilateral negotiations over jurisdiction. The United States may have better success entering into explicit agreements regarding information sharing and enforcement efforts with countries concerned about fraudulent conduct occurring in

140. *See* 17 C.F.R. § 230.902(b)(2) (2008). At the time of the writing of this Paper, these markets included the London Stock Exchange, the Stock Exchange of Hong Kong Limited, the Bourse de Luxembourg, and the Tokyo Stock Exchange, among others.

the United States that may affect other countries. Such agreements would allow other countries concerned about fraudulent conduct occurring in the United States that affects the other countries to bring their own enforcement against the fraudulent parties.

CONCLUSION

Courts in the United States wrestle with how far to extend jurisdiction in securities class-action lawsuits involving transnational securities fraud. Courts may allow foreign investors transacting abroad to join the class of investors litigating a rule 10b-5 claim under either a conduct or effects test of jurisdiction. Courts also may examine the reasonableness of applying U.S. jurisdiction and whether an alternative forum would provide better relief. Courts also look to comity issues. These varied doctrines often turn on the availability of remedies in other countries and/or whether these other countries will respect a U.S. judgment.

We argue that the conduct and effects tests as applied to securities class-action lawsuits involving foreign issuers and (at least in part) foreign investors transacting abroad are uncertain in their applications (and as a result, unpredictable). Wherever a foreign issuer is involved in a transaction, litigants may argue that the key conduct relating to the fraud occurred outside the United States, and that any U.S.-based conduct was merely preparatory. The conduct test requires courts to draw lines in determining exactly what type and extent of U.S.-based conduct is required for jurisdiction. Lacking empirical evidence on how foreign investors view who is responsible for fraud, courts are left without any principled method of drawing such lines, leaving the doctrine littered with assumption-driven analysis. Similarly, many events that occur abroad may have an effect on U.S. markets; whether a court will accept such effects for jurisdictional purposes however is uncertain. Most courts adopt the fiction that effects in an overseas securities market will not have an effect on a U.S. securities market despite arbitrage and the substantial links across worldwide securities markets that undermine this fiction.

Because the line-drawing assumptions relating to conduct and fictions adopted regarding effects can vary across judges and courts, what applies in one case may not apply in another case. Making such decisions on a case-by-case basis, judges may be poor decision makers in applying the conduct and effects tests (and making reasonableness and comity determinations) to decide extraterritorial jurisdictional issues in the securities context.[141]

Given these concerns, we propose that courts adopt a uniform, bright-line exchange-based presumptive rule in determining the applicable class in an f-cubed rule 10b-5 class-action lawsuit. Courts should presume jurisdiction over all investors trading in a foreign issuer's securities within the United States, and presume no jurisdiction over rule 10b-5 suits for foreign investors trading in the securities of a foreign issuer outside the United States. Applying an exchange-based presumption provides greater certainty to issuers and investors regarding the application of rule 10b-5 class-action lawsuits. The presumption also protects the interests of investors trading in the United States without unduly interfering with the jurisdiction of foreign regimes. Under this approach, private plaintiffs' attorneys have equivalent incentive to file a class-action lawsuit under rule 10b-5 against U.S. investors, compared with domestic issuers with a similar level of U.S. investor ownership and trading volume, and thus an equal level of private deterrence against the negative effects of fraud on the U.S. markets. Not all countries and investors will fit neatly into our presumption. We therefore also suggest that the SEC—but not individual courts—take an active role in providing ex ante determinations where the application of U.S. jurisdiction for investors of particular countries involved in f-cubed litigation may be necessary.

141. Indeed, the Second Circuit in *Morrison*, perhaps recognizing the deficiencies in the conduct and effects tests, called for Congress and the SEC to pay attention to the question of the extraterritorial reach of the Securities Exchange Act. *See Morrison*, 547 F.3d at 171 n.4 ("We respectfully urge that this significant omission receive the appropriate attention of Congress and the Securities and Exchange Commission.").