

2013

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Recommended Citation

Marc I. Steinberg and Kelly Flanagan, Transnational Dealings - Morrison Continues to Make Waves (2012).
Available at SSRN: <https://ssrn.com/abstract=2205416>

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Transnational Dealings -- *Morrison* Continues to Make Waves

Marc I. Steinberg* and Kelly Flanagan**

Abstract

Morrison v. National Australia Bank Ltd. drastically altered the landscape for transnational securities litigation and the way that courts determine proper application of a statute concerning a transnational claim. The Supreme Court's characterization of extraterritoriality under the Securities Exchange Act as a merits-based inquiry has led to a reexamination of limitations under other federal statutes that were previously thought to be jurisdictional issues. Significantly, *Morrison* created a roadmap for courts to follow when the extraterritoriality of a statute is brought into question. The key to proper application of a statute is to decipher the minimum U.S. contacts required to state a transnational claim. The tests developed addressing this inquiry are critical in discerning the boundaries of U.S. law at a time when transnational dealings are prevalent.

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Introduction

The Supreme Court in *Morrison v. National Australia Bank Ltd.*,¹ significantly altered the treatment of transnational securities claims. This article explores *Morrison*'s impact, including trends that may emerge and questions that remain. The article commences with an analysis of this important decision. Thereafter, the widespread implications of *Morrison*'s merits-based characterization are addressed. The article then considers how *Morrison* affects extraterritorial claims under other federal laws. Lastly, there is a detailed analysis of the types of securities claims that endure after *Morrison*. The article's focus is that *Morrison* will have longstanding effects on both U.S. federal securities and non-securities law.

II. Making Waves – *Morrison v. National Australia Bank Ltd.*

A. Pre-*Morrison* – The Calm Before the Storm

Understanding the background of Section 10(b), which is the principal antifraud provision of the Securities Exchange Act, and its application to transnational securities fraud sets the stage for *Morrison*. Prior to *Morrison*, lower

¹ 130 S. Ct. 2869 (2010).

federal courts held that Section 10(b) was silent as to extraterritorial application.² When transactions with an international connection arose, courts considered whether there was subject matter jurisdiction under Section 10(b) to adjudicate the claim.³ In determining extraterritorial applicability, lower federal courts focused on policy matters such as the possible creation of a U.S. haven for those defrauding foreign investors and Congress's intent to establish a high standard of conduct in securities transactions.⁴ Also significant, the Second Circuit attempted to discern,

² See, e.g., *In re CP Ships Ltd. Secs. Litig.*, 578 F.3d 1306, 1313 (11th Cir. 2009); *Morrison v. Nat'l Austr. Bank Ltd.*, 547 F.3d 167, 170 (2d Cir. 2008); *Robinson v. TCI/US West Commc'ns Inc.*, 117 F.3d 900, 905 (5th Cir. 1997).

³ 15 U.S.C. § 78j(b). See, e.g., *In re CP Ships Ltd. Secs. Litig.*, 578 F.3d at 1312-13; *Morrison*, 547 F.3d at 176; *Robinson*, 117 F.3d at 904; *Zoelsch v. Arthur Anderson & Co.*, 824 F.2d 27, 31 (D.C. Cir. 1987); *Cont'l Grain (Austr.) Pty. Ltd. v. Pac. Oilseeds, Inc.*, 592 F.2d 409, 413-14 (8th Cir. 1979).

⁴ See, e.g., *MCG, Inc. v. Great W. Energy Corp.*, 896 F.2d 170, 174 (5th Cir. 1990) (discussing the policy considerations of the Second, Third, and Eighth Circuits where acts within the United States have affected foreign investors).

based on Section 10(b)'s underlying purposes,⁵ whether Congress desired to invoke the resources of U.S. courts in the transnational context.⁶

With these considerations in mind, federal appellate courts, most notably the Second Circuit, developed what became known as the “conduct” and “effects” test.⁷ The conduct analysis inquired “whether the wrongful conduct occurred in the

⁵ The underlying purpose of Section 10(b) was to “remedy deceptive and manipulative conduct with the potential to harm the public interest or the interests of investors.” *Morrison*, 547 F.3d at 170 (citing H.R. Rep. No. 1838, at 32-33 (1934)).

⁶ *Morrison*, 547 F.3d at 170 (referring to *Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974, 985 (2d Cir. 1975)).

⁷ See *Leasco Data Processing Equip. Corp. v. Maxwell*, 468 F.2d 1326, 1336-37 (2d Cir. 1972) (creating the conduct test); *Schoenbaum v. Firstbrook*, 405 F.2d 200, 206-09 (2d Cir. 1968) (creating the effects test). For the purposes of this article, the pre-*Morrison* approach will be referred to as the “conduct and effects test.” However, it should be noted that not all courts performed a joint assessment of conduct and effects. Compare *Itoba Ltd. v. LEP Group PLC*, 54 F.3d 118, 122 (2d Cir. 1995) (stating that a combination of the “conduct test” and “effects test” provides a better sense of whether sufficient U.S. contacts exist for a Section 10(b) claim) and *Kauthar SDN BHD v. Sternberg*, 149 F.3d 659, 665 n.8 (7th Cir. 1998) (finding that a comprehensive approach does a better job of measuring U.S. contacts), with *Robinson*, 117 F.3d at 905 (explaining that either the conduct test or the effects test may “independently establish jurisdiction”) and *Zoelsch*, 824 F.2d at 30 (offering the conduct and effects analyses as two instances where jurisdiction may be exercised over securities transactions that were not

United States.”⁸ The analysis applied to investors harmed abroad and varied depending on whether the investor was an American or a foreigner.⁹ When U.S. investors suffered losses abroad, the Second Circuit required that materially important acts performed in the United States “significantly contributed” to the harm.¹⁰ When foreigners suffered losses abroad, however, the acts occurring in the United States must have “directly caused” the harm.¹¹ In the latter instance, acts in

consummated in the United States). For a comparison of the regulatory systems in place in the world’s major markets, see Marc I. Steinberg and Lee Michaels, *Disclosure in Global Offerings: Analysis of Jurisdictional Approaches, Commonality and Reciprocity*, 20 Mich. J. Int’l L. 207 (1999).

⁸ See *In re CP Ships Ltd. Secs. Litig.*, 578 F.3d 1306, 1313 (11th Cir. 2009); *Morrison*, 547 F.3d at 170.

⁹ *Bersch*, 519 F.2d at 993.

¹⁰ *Id.* For instance, in *Bersch v. Drexal Firestone, Inc.*, the court concluded that jurisdiction existed where a prospectus emanating from the United States led to a fraudulent offering to U.S. investors abroad. *Id.* at 992.

¹¹ *Id.* See, e.g., *Psimenos v. E.F. Hutton & Co.*, 722 F.2d 1041, 1047-48 (2d Cir. 1983) (finding direct causation where the alleged fraud was completed through trades on U.S. commodities exchanges).

the United States that were “merely preparatory” did not satisfy the conduct test.¹² The Fifth,¹³ Seventh,¹⁴ and D.C. Circuits¹⁵ adhered to the Second Circuit’s approach, while the Third,¹⁶ Eighth,¹⁷ and Ninth¹⁸ Circuits embraced more relaxed standards.

¹² *Bersch*, 519 F.2d at 992 (“While merely preparatory activities in the United States are not enough to trigger application of the securities laws for injury to foreigners located abroad, they are sufficient when the injury is to Americans so resident.”).

¹³ *Robinson v. TCI/West Communications Inc.*, 117 F.3d 900, 906 (5th Cir. 1997) (referring to the presumption against extraterritoriality and stating that policy arguments may provide reason for Congress, but not the courts, to expand federal jurisdiction).

¹⁴ *Kauthar SDN BHD v. Sternberg*, 149 F.3d 659, 667 (7th Cir. 1998) (stating that the Second Circuit test provides an appropriate balance between the caution that should be exercised in finding extraterritorial application and the concern that the United States is not used as a base for fraudulent operations).

¹⁵ *Zoelsch v. Arthur Anderson & Co.*, 824 F.2d 27, 31-32 (D.C. Cir. 1987) (considering the presumption against extraterritorial jurisdiction and the “preserv[ation] of American judicial resources for adjudication of domestic disputes and enforcement of domestic law”).

¹⁶ *SEC v. Kasser*, 548 F.2d 109, 114 (3d Cir. 1977) (asking whether “at least some activity designed to further a fraudulent scheme occurs within this country”).

¹⁷ *Cont’l Grain (Austr.) Pty. Ltd. v. Pac. Oilseeds, Inc.*, 592 F.2d 409, 421 (8th Cir. 1979) (inquiring whether “defendants’ conduct in the United States was in furtherance of a fraudulent scheme and was significant with respect to its accomplishment”).

The effects analysis, on the other hand, asked “whether the wrongful conduct had a substantial effect in the United States.”¹⁹ The Second Circuit created the effects test based on the belief that Congress intended to protect U.S. investors who acquired foreign securities in the U.S. markets and to protect U.S. markets from improper foreign conduct impacting U.S. securities.²⁰ For instance, in *Schoenbaum v. Firstbrook*,²¹ a case involving securities of a Canadian corporation, the Second Circuit exercised jurisdiction where the transactions at issue had occurred in Canada but impacted the value of common shares trading on

¹⁸ *Grunenthal GmbH v. Hotz*, 712 F.2d 421, 425 (9th Cir. 1983) (adopting the Eighth Circuit’s test in *Continental Grain*).

¹⁹ *Morrison v. Nat’l Austr. Bank Ltd.*, 547 F.3d 167, 171 (2d Cir. 2008). *See also* *Robinson v. TCI/West Communications Inc.*, 117 F.3d 900, 905 (5th Cir. 1997); *Zoelsch*, 824 F.2d at 30. The Seventh and Eighth Circuits considered whether the effects were foreseeable and substantial. *See Kauthar SDN BHD*, 149 F.3d at 665; *Cont’l Grain (Austr.) Pty. Ltd.*, 592 F.2d at 416-17.

²⁰ *Schoenbaum v. Firstbrook*, 405 F.2d 200, 206 (2d Cir. 1968) (rejecting the district court’s conclusion that the Exchange Act did not apply to transactions outside of the territorial United States).

²¹ 405 F.2d 200 (2d Cir. 1968).

a U.S. exchange.²² The court asserted that application of Section 10(b) was “necessary to protect American investors.”²³

For over forty years, the conduct and effects test was applied and refined by the lower federal courts.²⁴ Not surprisingly, some commentators criticized the unpredictable and inconsistent application of Section 10(b) under the test.²⁵ In 2010, in *Morrison v. National Australia Bank Ltd.*, the Supreme Court altered the course of federal securities law concerning transnational securities fraud.²⁶

B. The Storm Strikes – The *Morrison* Decision

²² *Id.* at 208-09 (explaining that fraud upon the foreign corporation reduced its equity and resulted in decreased stock value on U.S. exchanges).

²³ *Id.* at 206.

²⁴ *See Morrison*, 130 S. Ct. at 2879-80 (detailing the history of the conduct and effects test).

²⁵ *See, e.g.*, Erez Reuveni, *Extraterritoriality as Standing: A Standing Theory of the Extraterritorial Application of the Securities Laws*, 43 U.C. DAVIS L. REV. 1071, 1075 (2010); Stephen J. Choi & Linda J. Silberman, *Transnational Litigation and Global Securities Class-Action Lawsuits*, 2009 WIS. L. REV. 465, 567-68 (2009); Kun Young Chuang, *Multinational Enforcement of U.S. Securities Laws: The Need for the Clear and Restrained Scope of Extraterritorial Subject-Matter Jurisdiction*, 9 FORDHAM J. CORP. & FIN. L. 89, 102 (2003); Margaret Sachs, *The International Reach of Rule 10b-5: The Myth of Congressional Silence*, 28 COLUM. J. TRANSNAT'L L. 677 (1990).

²⁶ 130 S. Ct. 2869 (2010).

Morrison was a “foreign-cubed” case, or rather – a case where foreign investors sued a foreign issuer under the U.S. securities laws for securities transactions on a foreign exchange.²⁷ In 1998, National Australia Bank Ltd. (National Australia) purchased HomeSide Lending, Inc. (HomeSide), a Florida-based mortgage servicing company that received fees for collecting mortgage payments. Since Homeside would not receive fees once a mortgage was fully paid, the value of HomeSide’s right to receive such fees diminished as mortgages were paid off early. Three years later, National Australia had to write down the value of Homeside’s assets by \$1.2 billion. National Australia explained that it had not anticipated the lowering interest rates and related refinancings. The prices of National Australia’s ordinary shares (which were listed on the Australian Stock Exchange Limited (ASX)) and its American Depositary Receipts (ADRs)²⁸ (which

²⁷ *Id.* at 2894 n.11 (Stevens, J., concurring in judgment).

²⁸ As stated by the Third Circuit:

An ADR is a receipt that is issued by a depositary bank that represents a specified amount of a foreign security that has been deposited with a foreign branch or agent of the depositary, known as the custodian. The holder of an ADR is not the title owner of the underlying shares; the title owner of the underlying shares is either the depositary, the custodian, or their agent. ADRs are tradeable in the same manner as any other registered American security, may be listed on any of the major exchanges in the United States or traded over the counter, and are subject to the Securities Act and the Exchange Act. This

were listed on the New York Stock Exchange (NYSE)) subsequently fell. Australian and American investors then sued National Australia, HomeSide, and their insiders, alleging violations of Section 10(b).²⁹ The plaintiffs claimed that the HomeSide defendants had manipulated the rates of early repayment as “unrealistically low” with the objective of inflating the ostensible value of the mortgage-servicing rights and that the National Australia defendants were aware of this deception.³⁰

The district court dismissed the claims by the American investor in National Australia’s ADRs for failure to allege damages.³¹ Since the American investor did

makes trading an ADR simpler and more secure for American investors than trading in the underlying security in the foreign market.

Pinker v. Roche Holdings, Ltd., 292 F.3d 361, 367 (3d Cir. 2005).

By purchasing ADRs, a U.S. investor can gain ownership in the shares of a foreign company without the cross-border and currency inconveniences that the investor would encounter if he instead purchased the shares on a foreign exchange. *See generally* Joseph Velli, *American Depositary Receipts: An Overview*, Symposium: Entering the U.S. Securities Markets: Opportunities and Risks for Foreign Companies, 17 *FORDHAM INT’L L.J.* S38, S39 (1994).

²⁹ *Morrison*, 130 S. Ct. at 2876.

³⁰ *Id.*

³¹ *In re Nat’l Austr. Bank Secs. Litig.*, No. 03 Civ. 6537 (BSJ), 2006 WL 3844465, at *8-9 (S.D.N.Y. Oct. 25, 2006).

not appeal, only claims by the Australian investors in National Australia's ordinary shares traded on the ASX were further considered.³² The district court then granted defendants' motion to dismiss for lack of subject-matter jurisdiction, reasoning that the acts in the United States were, "at most, a link in the chain of an alleged overall securities fraud scheme that culminated abroad."³³ The Court of Appeals for the Second Circuit affirmed, stating that the domestic acts did not "compris[e] the heart of the alleged fraud."³⁴ The Supreme Court granted certiorari.³⁵

As a threshold matter, the Court held that the extraterritorial reach of Section 10(b) with regard to National Australia's conduct was a "merits" question under Federal Rule of Civil Procedure (FRCP) 12(b)(6), not a subject-matter jurisdiction question under FRCP Rule 12(b)(1).³⁶ This "merits"-based approach constitutes a radical departure from the subject matter jurisdictional rationale that had been overwhelmingly embraced by the lower federal courts.³⁷ Perhaps equally as

³² *See Morrison*, 130 S. Ct. at 2876 n.1.

³³ *In re Nat'l Austr. Bank Secs. Litig.*, 2006 WL 3844465, at *8.

³⁴ *Morrison v. Nat'l Austr. Bank Ltd.*, 547 F.3d 167, 175-77 (2d Cir. 2008).

³⁵ *Morrison v. Nat'l Austr. Bank Ltd.*, 130 S. Ct. 783 (2009) (mem. op.).

³⁶ *Morrison*, 130 S. Ct. at 2876-77.

³⁷ *See* Jared L. Kopel et al., *42nd Annual Institute on Securities Regulation: Current Topics on Securities Litigation*, 1850 PLI/CORP 365, 391 (New York City, N.Y.) (Nov. 10-12, 2010)

("[T]he Court swiftly swept away a half-century of lower courts treating the issue of

significant, the Supreme Court rejected the conduct and effects test.³⁸

In determining whether the plaintiffs had stated a claim, the Supreme Court emphasized that unless Congress clearly expresses its affirmative intention “to give a statute extraterritorial effect,” then the statute has no such application.³⁹ The Court asserted that lower courts had disregarded this presumption against extraterritoriality by creating the conduct and effects test to “discern” whether Congress would have wanted a statute to apply.⁴⁰ The Court explained the difficulties of applying the conduct and effects test, such as having to decipher the degree of activity that transpired in the United States.⁴¹ After criticizing the unpredictable application of Section 10(b) to transnational cases under the conduct

extraterritorial reach of the securities law as a question of subject matter jurisdiction.”). *See, e.g., Morrison*, 547 F.3d at 171; *Robinson v. TCI/West Communications Inc.*, 117 F.3d 900, 906 (5th Cir. 1997); *Kauthar SDN BHD v. Sternberg*, 149 F.3d 659, 667 (7th Cir. 1998). For further discussion, see *infra* notes 65-109 and accompanying text.

³⁸ 130 S. Ct. at 2877-83.

³⁹ *Id.* at 2877 (commenting that various courts had been using this approach for decades).

⁴⁰ *Id.* at 2878.

⁴¹ *Id.* at 2879. *See, e.g., Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974, 986-87 (2d Cir. 1975) (distinguishing between U.S. and foreign investors); *IIT v. Vencap, Ltd.*, 519 F.2d 1001, 1017-18 (2d Cir. 1975) (stating that “mere preparatory activities” do not warrant extraterritorial application).

and effects test, the Court reasoned that applying the presumption against extraterritoriality in all cases provides stability moving forward.⁴²

Next, the Supreme Court considered whether Congress had legislated that Section 10(b) applies abroad.⁴³ The Court held that the “general reference to foreign commerce in the definition of ‘interstate commerce’ does not defeat the presumption against extraterritoriality.”⁴⁴ Congress’s observations, when setting forth the purposes of the Exchange Act, that “transactions in securities as conducted upon securities exchanges and over-the-counter markets are affected with a national public interest” and that the “prices established in such transactions are generally disseminated and quoted throughout the United States and foreign countries” also failed to overcome the presumption.⁴⁵ Lastly, the Solicitor General argued that Section 30(b) of the Exchange Act (which specifically authorizes the Securities and Exchange Commission (SEC) to promulgate regulations having

⁴² See *Morrison*, 130 S. Ct. at 2880-81 (criticizing “judicial-speculation-made-law-divining”); *id.* at 2887 (specifically disapproving *Leasco Data Processing Equipment Corp. v. Maxwell*, 468 F.2d 1326 (2d Cir. 1972), and *Schoenbaum v. Firstbrook*, 405 F.2d 200 (2d Cir. 1968), from which the Second Circuit developed its conduct and effects test).

⁴³ See *Id.* at 2881-83.

⁴⁴ *Id.* at 2882 (discussing the definition of “interstate commerce” in the Exchange Act, 15 U.S.C. § 78c(a)(17)).

⁴⁵ *Id.* (quoting 15 U.S.C. § 78b).

extraterritorial application in order “to prevent . . . evasion of the Exchange Act”) is evidence that the whole Exchange Act applies extraterritorially.⁴⁶ Disagreeing, the Court concluded that Section 30(b) appeared to be “directed at actions abroad that might conceal a domestic violation.”⁴⁷

As an example of “a clear statement of extraterritorial effect,” the Court focused on Section 30(a) of the Exchange Act.⁴⁸ That statute provides:

It shall be unlawful for any broker or dealer . . . to make use of the mails or of any means or instrumentality of interstate commerce for the purpose of effecting on an exchange not within or subject to the jurisdiction of the United States, any transaction in any security the issuer of which is a resident of, or is organized under the laws of, or has its principal place of business in, a place within or subject to the

⁴⁶ *Id.* (contending that “[this] exemption would have no function if the Act did not apply in the first instance to securities transactions that occur abroad” (Brief for the United States as *Amicus Curiae* 14)).

⁴⁷ *Id.* at 2882-83.

⁴⁸ *Id.* at 2883. The Court remarked that this provision providing for “a specific extraterritorial application would be quite superfluous if the rest of the Exchange Act already applied to transactions on foreign exchanges. . . .” *Id.*

jurisdiction of the United States, in contravention of such rules and regulations as the Commission may prescribe⁴⁹

The Court noted that even where a statute, such as Section 30(a), has some extraterritorial application, the presumption against extraterritoriality “operates to limit that provision to its terms.”⁵⁰ The Court concluded that there was not a sufficient basis to overcome the presumption against extraterritoriality for Section 10(b).⁵¹

Alternatively, plaintiffs argued that extraterritorial reach of Section 10(b) was immaterial in this instance, as they only sought domestic application concerning the alleged financial manipulations and public statements of HomeSide that occurred in Florida.⁵² In response, the Court commented:

For it is a rare case of prohibited extraterritorial application that lacks *all* contact with the territory of the United States. But the presumption against extraterritorial application would be a craven watchdog indeed

⁴⁹ 15 U.S.C. § 78dd(a) (2011).

⁵⁰ *Morrison*, 130 S. Ct. at 2883.

⁵¹ *Id.* (“In short, there is no affirmative indication in the [Exchange Act] that § 10(b) applies extraterritorially, and we therefore conclude that it does not.”).

⁵² *Id.* at 2883-84.

if it retreated to its kennel whenever *some* domestic activity is involved in the case.⁵³

The Court thus reasoned that the Exchange Act focuses on purchases and sales of securities in the United States, not on the location where the deception occurs.⁵⁴ If indeed Congress had intended for the Exchange Act to apply to conduct affecting transactions consummated abroad, the Court stated that it would have addressed the subject of prospective conflicts with foreign laws and procedures.⁵⁵

The Court thereupon enunciated the “transactional test” for the invocation of Section 10(b).⁵⁶ Under this test, for Section 10(b) to apply, “the purchase or sale [must be] made in the United States, or [must] involve[] a security listed on a domestic exchange.”⁵⁷ Since the plaintiffs in *Morrison* did not purchase or sell

⁵³ *Id.* at 2884 (emphasis in the original).

⁵⁴ *Id.* (applying the same mode of analysis used in *E.E.O.C. v. Arabian American Oil Co.*, 499 U.S. 244 (1991)).

⁵⁵ *Morrison*, 130 S. Ct. at 2884.

⁵⁶ *Id.* at 2886 (describing the test as a “clear test” that would not interfere with foreign securities regulation).

⁵⁷ *Id.* The Court explained that the prologue of the Exchange Act supported the significance of the domestic exchange with its goal of “provid[ing] for the regulation of securities exchanges.”

Id. at 2884. Moreover, the Court stated that it knew of no one who thought the Exchange Act

securities listed on a domestic exchange (and because the transactions at issue did

was meant to regulate foreign exchanges. *Id.* As for domestic purchases and sales, the Court referred back to Section 30(a) and (b), noting that, in each instance, the foreign location of the transaction “establishes (or reflects the presumption of) the Act’s inapplicability, absent regulations by the Commission.” *Id.* at 2885. The Court rejected the Solicitor General’s suggested test, which would have provided Section 10(b) coverage when the “fraud involves significant conduct in the United States,” primarily because the test lacked textual support. *Id.* at 2886. The Solicitor General stated that this test would “prevent[] the United States from becoming a ‘Barbary Coast’ for malefactors perpetrating frauds in foreign markets.” *Id.* In response, the Court stated that there is no evidence that the United States was on this path, though “some fear that [the United States] has become the Shangri-La of class-action litigation for lawyers representing those allegedly cheated in foreign securities markets.” *Id.*

Note that in certain circumstances, the SEC may be able to institute suit under Section 17(a) of the Securities Act when there are illegal offers to sell in the United States. Because Section 17(a) extends to both offers and sales, a domestic offer (even when the transaction is consummated abroad) comes within Section 17(a)’s coverage. *See SEC v. Goldman Sachs & Co.*, 790 F. Supp. 2d 147, 165 (S.D.N.Y. 2011). Significantly, Section 17(a) is solely a government enforcement tool. There is no private right of action under that statute. *See, e.g.*, *Finkel v. Stratton Corp.*, 962 F. 2d 169 (2d Cir. 1992); *Sears v. Likens*, 912 F. 2d 889 (7th Cir. 1990); *Landry v. All Am. Assurance Co.*, 688 F. 2d 381 (5th Cir. 1982). For analyses of Section 17 (a), see *Aaron v. SEC*, 446 U.S. 680 (1980); *United States v. Naftalin*, 441 U.S. 768 (1979); Marc I. Steinberg, *Section 17(a) of the Securities Act After Naftalin and Redington*, 68 Geo. L.J. 163 (1979).

not otherwise occur in the United States), the Court concluded that the plaintiffs had failed to state a claim and accordingly affirmed dismissal under Rule 12(b)(6).⁵⁸

⁵⁸ 130 S. Ct. at 2888. Justice Stevens, joined by Justice Ginsburg, concurred in the judgment only. *See generally id.* at 2888-95 (Stevens, J., concurring in judgment). Justice Stevens stated that the judge-made rules in U.S. securities law were invited by Congress when it deliberately created, and subsequently left intact, an open-ended statute. *Id.* at 2889-90. He contended that Second Circuit case law had been thoughtfully developed over several decades, had gained the “tacit approval of Congress and the Commission,” and thus, ought to be favored by the Court. *Id.* at 2890-91. Justice Stevens criticized Justice Scalia for limiting his search for an indication of extraterritorial application to statutory text. *Id.* at 2891 (explaining that “all available evidence about the meaning” of a provision should be considered to effectuate Congress’ will regarding extraterritorial application). In any case, Justice Stevens argued that it was not appropriate to discard the conduct and effects test based on the presumption against extraterritoriality because the test turns on the presence of sufficient *domestic* contacts in transnational securities fraud, not the complete absence of domestic contacts. *Id.* at 2892 (emphasis added). Justice Stevens found that the statutory text in § 10(b) and § 30(a) and (b) – which the majority held had no clear indication of extraterritorial application – offered strong indication that the Act covers at least some transnational frauds. *Id.* at 2893-94 n.9. Justice Stevens then stated that the real problem with the majority’s opinion is that its test for domestic application is based on the belief that transactions on domestic exchanges, rather than the interests of the public and investors, are the focus of the Exchange Act. *Id.* at 2894 (citing H.R. Rep. No. 1838, 73d Cong., 2d Sess., 32-33

Overall, *Morrison* contains three significant holdings: the abrupt characterization of extraterritoriality as a merits question; the determination that Section 10(b) does not overcome the presumption against extraterritoriality (with the related rejection of the conduct and effects test); and the creation of the transactional test. Before the impact of these holdings is examined, however, this article addresses Congress's response to the limitations pronounced in *Morrison*.

C. A Prescription for the Storm – The SEC-DOJ Dodd-Frank Amendment

One day after the Court released its *Morrison* decision, Congress enacted Section 929P of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) authorizing extraterritorial jurisdiction under the Exchange Act

(1934)). He pointed out that the transactional test created by the majority would leave an unsophisticated U.S. retiree who bought shares on a foreign exchange without a Section 10(b) remedy even if, on the basis of material misrepresentations, the purchase was induced in the United States by a U.S. subsidiary of the issuer. *Id.* at 2895. With regard to the facts in *Morrison* though, Justice Stevens concluded, “this case has Australia written all over it.” *Id.* See generally Genevieve Beyea, *Morrison v. National Australia Bank and the Future of Extraterritorial Application of the U.S. Securities Laws*, 72 OHIO ST. L.J. 537 (2011); Elizabeth Cosenza, *Paradise Lost: § 10(b) After Morrison v. National Australia Bank*, 11 CHI. J. INT’L L. 343 (2011).

for actions brought by the SEC and the U.S. government, such as the Department of Justice (DOJ).⁵⁹ Specifically, the statute provides:

Extraterritorial Jurisdiction. – The district courts of the United States and the United States courts shall have jurisdiction of an action or proceeding brought or instituted by the Commission or the United States alleging a violation of the antifraud provisions of this title involving –

- (1) Conduct within the United States that constitutes significant steps in furtherance of the violation, even if the securities transaction occurs outside the United States and involves only foreign investors; or
- (2) Conduct occurring outside the United States that has a foreseeable substantial effect within the United States.⁶⁰

According to floor comments made by the statute’s sponsor, Representative Paul Kanjorski, Section 929P sought to nullify the presumption against extraterritoriality of the antifraud provisions of the U.S. securities laws with regard to government-brought actions by codifying the conduct and effects test repudiated

⁵⁹ § 929P, Pub. L. No. 111-203, 124 Stat. 1376, 1865 (2010) (codified as amended at 15 U.S.C. §§ 77v(c), 78aa(b) (2011)).

⁶⁰ *Id.*

by *Morrison*.⁶¹ Additionally, the Dodd-Frank Act mandated that the SEC perform a study and report to Congress within eighteen months on whether the test set forth in Section 929P should be extended to private actions.⁶²

Congress therefore wrote a prescription to cure the ills of *Morrison* in the government enforcement setting. Whether Congress in fact prescribed the proper medicine is uncertain. In *Morrison*, the Supreme Court held that extraterritorial application was a matter of substantive law, not subject matter jurisdiction.⁶³ Ignoring this rationale, Congress framed Section 929P in terms of jurisdiction.

⁶¹ CONG. RECORD, at H5237 (June 30, 2010). Note that other criminal statutes may be invoked even if a subject transaction occurs abroad. For example, the federal wire fraud statute, 18 U.S.C. § 1343, extends liability to those who use U.S. interstate wires to execute a proscribed scheme or antifraud to defraud. *See Pascquantino v. United States*, 544 U.S. 349, 371 (2005).

⁶² § 929Y, Pub. L. No. 111-203, 124 Stat. 1376, 1871. The SEC request for comment considers international comity, as well as the economic costs and benefits of including private actions for transnational securities frauds. *Study on Extraterritorial Private Right of Actions*, SECS. & EXCHANGE COMMISSION, www.sec.gov/rules/other/2010/34-63174.pdf (last visited Feb. 16, 2012). The Commission issued its report to Congress in April 2012. *Study on the Cross-Border Scope of the Private Right of Action Under Section 10(b) of the Securities Exchange Act of 1934*, SECS. & EXCHANGE COMMISSION, <http://www.sec.gov/news/studies/2012/929y-study-cross-border-private-rights.pdf> (last visited June 20, 2012). See Part V of this article for a detailed discussion of the report and related public comments.

⁶³ *Morrison*, 130 S. Ct. at 2877.

Thus, it remains to be seen whether Congress's efforts regarding SEC and DOJ actions will be effective.⁶⁴ Section 929P is discussed further in the next section, which examines the consequences of treating extraterritoriality as a merits question and the implications of the abrupt departure from the historical treatment of this subject.

III. Divergent Waves – Subject Matter Jurisdiction and the Merits

Extraterritoriality has traditionally been dealt with as a matter of subject matter jurisdiction.⁶⁵ *Morrison*, however, held that this approach was not appropriate with regard to Section 10(b).⁶⁶ The Court explained that inquiring about extraterritorial reach is really to ask what conduct is prohibited under Section

⁶⁴ For a discussion on Section 929P as it relates to *Morrison*, see Richard Painter, Douglas Dunham, and Ellen Quackenbos, *When Courts and Congress Don't Say What They Mean: Initial Reactions to Morrison v. National Australia Bank and to the Extraterritorial Jurisdiction Provisions of the Dodd-Frank Act*, 20 Minn. J. Int'l L. 1 (2011).

⁶⁵ See, e.g., *Hartford Fire Ins. v. California*, 509 U.S. 764, 796 n.22 (1993) (the Sherman Act); *E.E.O.C. v. Arabian Am. Oil Co.*, 499 U.S. 244, 247, 258-59 (1991) (Title VII of the Civil Rights Act of 1964); *In re CP Ships Ltd. Secs. Litig.*, 578 F.3d 1306, 1311-13 (11th Cir. 2009) (Section 10(b) of the Exchange Act); *Morrison v. Nat'l Austr. Bank Ltd.*, 547 F.3d 167, 176 (2d Cir. 2008) (Section 10(b) of the Exchange Act).

⁶⁶ See *Morrison*, 130 S. Ct. at 2877.

10(b), which goes to the merits of the claim.⁶⁷ It stated that subject matter jurisdiction, on the other hand, concerns a court’s “power to hear a case.”⁶⁸ The differences between a jurisdictional and a merits challenge are discussed below, followed by an exploration of the implications of this change beyond Section 10(b).

A. Assessing the Storm – Consequences of Jurisdictional and Merit-Based Characterizations

Classifying an issue as jurisdictional or merit-based can impact when a challenge may be brought, who resolves the challenge, and the finality of the resolution.⁶⁹ For example, a motion based on subject matter jurisdiction may be raised at any time,⁷⁰ whereas a challenge based on the merits is forfeited if not

⁶⁷ *Id.*

⁶⁸ *Id.* One commentator defined the difference as: “Merits ask whether the defendant’s conduct was legally constrained (by the Constitution or by act of Congress); jurisdiction asks whether a federal court has the power to enforce that legal constraint on the defendant’s conduct.” Howard M. Wasserman, *Jurisdiction and Merits*, 80 WASH. L. REV. 643, 671 (2005).

⁶⁹ *See* *Arbaugh v. Y & H Corp.*, 546 U.S. 500, 514 (2006) (discussing the consequences of characterizing a requirement as a subject matter jurisdiction issue or a merits-based issue).

⁷⁰ *Id.* at 514.

brought to the court in a timely manner.⁷¹ An instance where this timing may affect the outcome of a case is where a defendant raises an issue for the first time on appeal.⁷² Such a challenge will likely be rejected as untimely if the court determines that the issue is based on the merits, rather than that of subject matter jurisdiction.⁷³

Additionally, courts have an independent obligation to determine that subject matter jurisdiction exists but have no such obligation regarding merit requirements.⁷⁴ Thus, a court must inquire into such jurisdictional issues on its own

⁷¹ *Union Pac. R.R. Co. v. Bhd. of Locomotive Eng'rs*, 130 S. Ct. 584, 596 (2009) (stating that a “claim-processing rule . . . is ordinarily ‘forfeited if the party asserting the rule waits too long to raise the point’”).

⁷² *See, e.g., Arbaugh v. Y & H Corp.*, 380 F.3d 219 (5th Cir. 2004), *rev'd* 546 U.S. 500 (2006) (affirming the district court’s decision to vacate a jury verdict for the plaintiff where the defendant raised an issue of subject matter jurisdiction for the first time after the trial).

⁷³ *See, e.g., Arbaugh*, 546 U.S. at 504 (rejecting a challenge based on the merits of a claim because the defendant had failed to raise the issue prior to the close of trial).

⁷⁴ *Id.* at 514; *also compare* Fed. R. Civ. P. 12(h)(3) (“If the court determines at any time that it lacks subject-matter jurisdiction, the court must dismiss the action.”), *with* Fed. R. Civ. P. 12(h)(2) (“Failure to state a claim upon which relief can be granted . . . may be raised: (A) in any pleading allowed or ordered under Rule 7(a); (B) by a motion under Rule 12(c); or (C) at trial.”). In determining that the ERISA requirement that an employer has fifteen or more employees was a merits rather than jurisdiction issue, the Supreme Court noted that the text of ERISA did not

accord. Characterization of an issue as jurisdictional or merit-based also influences whether a judge or a jury will resolve the dispute.⁷⁵ Particularly, a judge may weigh evidence concerning contested facts to resolve a dispute concerning subject matter jurisdiction, whereas a jury is the trier of contested facts where an element of the claim is at issue.⁷⁶

The finality of a resolution may also depend on characterization of an issue as jurisdictional or merit-based. A dismissal due to lack of subject matter jurisdiction typically is without prejudice, allowing a plaintiff to bring the claim in an appropriate court.⁷⁷ However, if a claim is dismissed on the merits, the plaintiff

indicate that “Congress intended courts, on their own motion, to assure that the employee-numerosity requirement is met.” *Id.*

⁷⁵ *See id.* (referring to Charles Wright and Arthur Miller, 5B Federal Practice & Procedure § 1350, pp. 243-49 (3d ed. 2004)).

⁷⁶ *Arbaugh*, 546 U.S. at 514.

⁷⁷ American Law Institute, Restatement (Second) of Judgments § 26(1) (2011) (providing an exception to claim preclusion where “[t]he plaintiff was unable to rely on a certain theory of the case or to seek a certain remedy or form of relief in the first action because of the limitations on the subject matter jurisdiction of the courts”).

would be precluded from arguing for a different outcome elsewhere.⁷⁸ Furthermore, the court's characterization of the issue may impact other claims. An appellate court must dismiss the entire complaint if subject matter jurisdiction is found lacking.⁷⁹ A motion to dismiss for failure to state a claim, on the other hand, allows the court discretion to exercise supplemental jurisdiction over pendant issues.⁸⁰

These differences can potentially impact the outcome of litigation. With the exception of potential claim preclusion, the characterization of an issue as merit-based appears to favor plaintiffs. When an issue is deemed a merits question, there is a limited time for challenges by defendants, no independent judicial obligation to ensure that merit requirements are met, and a jury to resolve disputes concerning contested facts. It should be noted, however, that a pretrial dismissal usually does not depend on characterization of an issue as jurisdictional or merit-based, as

⁷⁸ See *Allen v. McCurry*, 449 U.S. 90, 94 (1980) (“[A] final judgment on the merits of an action precludes the parties or their privies from relitigating issues that were or could have been raised in that action.”).

⁷⁹ *Arbaugh*, 546 U.S. at 514 (citing J. Moore et al., 15 Moore’s Federal Practice § 106.66[1], pp. 106-88 to 106-89 (3d ed. 2005)).

⁸⁰ *Id.* (explaining that this discretion stems from 28 U.S.C. § 1367).

evidenced in *Morrison*.⁸¹ National Australia raised the issue of extraterritorial reach of Section 10(b) before trial and therefore had not forfeited a challenge based on the merits. The Court found it unnecessary to remand the case based on the Second Circuit’s dismissal of the case for lack of jurisdiction under Rule 12(b)(1) instead of dismissal for failure to state a claim under Rule 12(b)(6), reasoning that the new labeling would result in the same outcome.⁸²

In *Morrison*, the Supreme Court abruptly overruled decades of history treating Section 10(b) extraterritoriality as an issue of subject matter jurisdiction. The impact of this change on extraterritorial securities litigation under Section 10(b) is monumental. As discussed next, *Morrison* is already influencing the characterization of statutory requirements of other federal statutes.

⁸¹ See *Morrison v. Nat’l Austr. Bank Ltd*, 130 S. Ct. 2869, 2877 (2010) (“Since nothing in the analysis of the courts below turned on the mistake, a remand would only require a new Rule 12(b)(6) label for the same Rule 12(b)(1) conclusion.”). See also *ABF Freight Sys., Inc. v. Int’l Bhd. of Teamsters*, 2011 WL 2623347 (8th Cir. July 6, 2011) (“It is true that an appellate court may treat a Rule 12(b)(1) issue as a Rule 12(b)(6) issue.”); *Daniels-Hall v. Nat’l Educ. Ass’n*, 629 F.3d 992, 997-98 (9th Cir. 2010) (finding that remand was unnecessary where the district court incorrectly discussed an ERISA matter for lack of subject matter jurisdiction, rather than failure to state a claim).

⁸² See, e.g., *Morrison*, 130 S. Ct. at 2877 (citing *Romero v. Int’l Terminal Operating Co.*, 358 U.S. 354, 359, 381-84 (1959)).

B. Riding the Waves – Implications Beyond Section 10(b)

The jurisdiction provision for the Exchange Act states:

The district courts of the United States . . . shall have exclusive jurisdiction of violations of [the Exchange Act] or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by [the Exchange Act] or the rules and regulations thereunder. . . .⁸³

There is thus no mention of extraterritoriality or any requirements regarding the scope of Section 10(b) in the foregoing statute. In *Morrison*, the Court stated that to establish subject matter jurisdiction, a plaintiff need only allege a violation of the Exchange Act.⁸⁴ Other federal statutes with similarly worded jurisdictional provisions⁸⁵ would be expected to yield results identical to *Morrison* in the future, that is – characterization of an issue regarding the statute’s scope as a merits question.

⁸³ Securities Exchange Act of 1934 § 27(a), 15 U.S.C. § 78aa(a) (2011).

⁸⁴ *See Morrison*, 130 S. Ct. at 2877 (quoting 15 U.S.C. § 78aa in finding that the District Court had jurisdiction to determine whether Section 10(b) applied to National Australia’s conduct).

⁸⁵ *See, e.g.*, 42 U.S.C. § 2000e-5(f)(3) (2011) (Title VII) (“Each United States district court and each United States court of a place subject to the jurisdiction of the United States shall have jurisdiction of actions brought under this subchapter.”).

Prior to *Morrison*, several circuit courts treated the requirements of the Foreign Trade Antitrust Improvement Act (FTAIA), which limits the extraterritorial reach of the Sherman Act, as a jurisdictional issue.⁸⁶ The Seventh Circuit noted that for six decades prior to enactment of the FTAIA, courts had treated application of the Sherman Act with regard to foreign markets as a matter of subject matter jurisdiction and that legislation should “be read to conform with Supreme Court precedent.”⁸⁷ Extraterritorial reach of the Sherman Act, without regard to the FTAIA, has also been characterized as a matter of subject matter jurisdiction.⁸⁸ Justice Scalia strongly dissented to this characterization in *Hartford Fire Insurance Company v. California*, insisting that, “the extraterritorial reach of the Sherman Act . . . has nothing to do with the jurisdiction of the courts. It is a question of substantive law turning on whether, in enacting the Sherman Act,

⁸⁶ See, e.g., *United States v. LSL Biotechnologies*, 379, F.3d 672, 679 (9th Cir. 2004); *United Phosphorus Ltd. v. Angus Chem. Co.*, 322 F.3d 942, 952 (7th Cir. 2003) (en banc); *Den Norske Stats Oljeselskap As v. HeereMac Vof*, 241 F.3d 420, 425 (5th Cir. 2001). Dissenting in *United Phosphorus Ltd. v. Angus Chemical Co.*, Judge Diane Wood argued that the FTAIA language that the Sherman Act “shall not apply” to certain foreign conduct did not speak to the court’s power to consider the case. 322 F.3d at 954-55.

⁸⁷ *United Phosphorus Ltd.*, 322 F.3d at 951.

⁸⁸ *Hartford Fire Ins. Co. v. California*, 509 U.S. 764, 796 n.22 (1993).

Congress asserted regulatory power over the challenged conduct.”⁸⁹ After *Morrison*, Justice Scalia’s approach may well emerge victorious.⁹⁰

Extraterritoriality is not the first issue to generate confusion over whether a decision based on jurisdiction or the merits is appropriate. Until the Supreme Court resolved the issue in *Arbaugh v. Y & H Corp.*,⁹¹ there was a deep circuit split regarding whether the definition of an employer under Title VII of the Civil Rights Act of 1964 was a jurisdictional or a merits issue.⁹² The Fifth Circuit in *Arbaugh* held that fifteen or more employees were necessary to establish subject matter jurisdiction of a Title VII claim.⁹³ The Supreme Court rejected this characterization and stated that the requirement was a merits question.⁹⁴

⁸⁹ *Id.* at 813 (Scalia, J., dissenting).

⁹⁰ Indeed, the Third Circuit recently held that the FTAIA is a merits-based limitation, rather than a jurisdictional one. *Animal Sci. Prods., Inc. v. China Minmetals Corp.*, 654 F.3d 462, 468-69 (3d Cir. 2011) (discussing *Morrison v. Nat’l Austr. Bank Ltd.*, 130 S. Ct. 2869 (2010), and *Arbaugh v. Y & H Corp.*, 546 U.S. 500 (2006)).

⁹¹ 546 U.S. 500 (2006).

⁹² Wasserman, *supra* note 68, at 657 n.65 (2005) (listing cases from eight different circuit courts over the past three decades).

⁹³ *Arbaugh v. Y & H Corp.*, 380 F.3d 219, 224 (5th Cir. 2004).

⁹⁴ *Arbaugh v. Y & H Corp.*, 546 U.S. 500, 510 (2006). Since the plaintiff moved for dismissal based on subject matter jurisdiction for the first time on appeal, characterization of the issue as a

Additionally, since *Morrison*, it has been contended that certain requirements under other statutes, such as ERISA⁹⁵ and the Alien Tort Statute (ATS),⁹⁶ should be characterized as merits questions.

All this is not to say that an issue that goes to the scope of the conduct covered under the statute can never be a jurisdictional issue. The Supreme Court has stated that Congress has the power to make a threshold limitation on a statute's scope jurisdictional by clearly identifying it as such.⁹⁷ To determine whether Congress has exercised this power, the Court has focused on whether the threshold appears in the jurisdictional provision of the statute or if it is accompanied by any jurisdictional language.⁹⁸ For example, the amount-in-controversy threshold for

merits question resulted in reinstatement of the jury's decision against the plaintiff because there was not a timely motion to dismiss on the merits. *See Arbaugh v. Y & H Corp.*, 2006 U.S. App. LEXIS 9279 (5th Cir. Apr. 13, 2006).

⁹⁵ *Daniels-Hall v. Nat'l Educ. Ass'n*, 629 F.3d 992, 997-98 (9th Cir. 2010) (regarding whether an employment plan was subject to ERISA).

⁹⁶ *Doe v. Exxon Mobil Corp.*, 2011 WL 2652384 (D.C. Cir. July 8, 2011); *Kiobel v. Royal Dutch Petroleum Co.*, 642 F.3d 268, 272 n.1 (2d Cir. 2011) (Circuit Judge Leval, dissenting).

⁹⁷ *Arbaugh*, 546 U.S. at 515.

⁹⁸ *See Union Pac. R.R. Co. v. Bhd. of Eng'rs*, 130 S. Ct. 584, 597-99 (2009) (analyzing the conferencing requirement under the Railway Labor Act); *Arbaugh*, 546 U.S. at 515 (considering the employee-numerosity requirement under Title VII).

diversity-of-citizenship jurisdiction under 28 U.S.C. § 1332 is an example of a requirement deemed jurisdictional by Congress.⁹⁹ By contrast, in *Union Pacific Railroad Co. v. Brotherhood of Locomotive Engineers*,¹⁰⁰ the Supreme Court held that a conferencing requirement under the Railway Labor Act (RLA) was not jurisdictional because it was “not moored” to the section of the RLA establishing jurisdiction.¹⁰¹

Had the conduct and effects test not been rejected in *Morrison* for substantive reasons, the Dodd-Frank amendment arguably would have been successful in converting the test into a jurisdictional requirement for cases brought by the SEC and DOJ. Notably, Section 929P speaks extensively in jurisdictional language.¹⁰² However, in light of the substantive limitations set forth in *Morrison*, it may well be that the amendment futilely attempts to grant jurisdiction beyond the substantive reach of the Exchange Act.¹⁰³

⁹⁹ *Arbaugh*, 546 U.S. at 514-15. 28 U.S.C. § 1332 provides: “The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceed the sum or value of \$75,000”

¹⁰⁰ 130 S. Ct. 584 (2009).

¹⁰¹ *Id.* at 597-99 (commenting that the two provisions were in separate sections).

¹⁰² *See supra* notes 59-64 and accompanying text.

¹⁰³ *See, e.g.,* Painter et al., *supra* note 64, at 4.

A similar argument was made with regard to the Alien Tort Statute (ATS)¹⁰⁴ in *Sosa v. Alvarez-Machain*.¹⁰⁵ The defendant argued that the ATS was “stillborn” since the jurisdictional grant did not have a corresponding cause of action.¹⁰⁶ The Supreme Court found that federal common law at the time the ATS was passed in 1789 provided substantive law to support the jurisdictional grant.¹⁰⁷ In its decision, the Court considered evidence that Congress intended the statute to have immediate effect upon enactment.¹⁰⁸

While *Morrison* clearly finds substantive law lacking for the conduct and effect test, courts may draw from *Sosa* and proceed based on Congress’s intent to overrule *Morrison*, taking into account the brief time frame in which Congress had to respond to *Morrison* and the lengthy history of courts treating extraterritorial application as a matter of jurisdiction. Given the uncertainty surrounding Section 929P though, Congress (at least in the government enforcement context) should

¹⁰⁴ 28 U.S.C. § 1350 (2011). In its entirety, ATS states: “The district courts shall have original jurisdiction of any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States.” *Id.*

¹⁰⁵ 542 U.S. 692 (2004).

¹⁰⁶ *Id.* at 714.

¹⁰⁷ *Id.* at 724.

¹⁰⁸ *Id.*

expand the substantive reach of Section 10(b) to help ensure that the law is interpreted as Congress intended.¹⁰⁹

All in all, a significant impact of the *Morrison* declaration that Section 10(b) extraterritoriality is a merits question is with respect to the characterization of the statutory requirements of other statutes. Future characterization of extraterritoriality appears particularly susceptible to the reasoning in *Morrison*, though Congress's ability to make a requirement jurisdictional means that courts cannot assume that a merits question under one statute is necessarily a merits question under another statute. As for the future of the Dodd-Frank amendment, the potential problems seem to lie in the substantive limitations of the Exchange Act, not with Congress's jurisdictional characterization of extraterritoriality. The impact of *Morrison*'s extraterritoriality analysis on other federal law is examined next.

IV. Wave Impact – Extraterritoriality with Regard to Other Federal Law

¹⁰⁹ Interestingly, the SEC has not relied on the Dodd-Frank amendment in post-*Morrison* cases. See *SEC v. Goldman Sachs & Co.*, 2011 WL 2305988 (S.D.N.Y. June 10, 2011); *SEC v. Credit Bancorp, Ltd.*, 738 F. Supp. 2d 376 (S.D.N.Y. 2010). Since the less strict conduct and effects test should make it easier for the SEC to bring Section 10(b) actions, perhaps the SEC harbors doubts about its effectiveness.

In *Morrison*, the Supreme Court stated that the presumption against extraterritoriality is a canon of construction that applies generally to the legislation of Congress.¹¹⁰ The Court explained that this presumption rests on the perception that Congress usually legislates with regard to domestic, rather than foreign, concerns.¹¹¹ Thus, unless Congress clearly indicates that a statute has extraterritorial reach, courts should presume the statute does not apply abroad.¹¹² While *Morrison* is definitely not the first Supreme Court case to promulgate that general concept,¹¹³ its outcome may unleash a new wave of defendants challenging the extraterritorial application of federal statutes. To gain an understanding of how *Morrison* might impact other federal law, this section examines the Racketeer Influenced and Corrupt Organization Act (RICO), a statute whose

¹¹⁰ *Morrison v. Nat'l Australia Bank Ltd.*, 130 S. Ct. 2869, 2877 (2010).

¹¹¹ *Id.*

¹¹² *Id.* at 2878.

¹¹³ *See, e.g.*, *Smith v. United States*, 507 U.S. 197, 204 (1993) and *E.E.O.C. v. Arabian Am. Oil Co.*, 499 U.S. 244, 248 (1991) (both quoting *Foley Bros. v. Filardo*, 336 U.S. 281, 285 (1949): “[L]egislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States.”).

extraterritoriality is unsettled, and the Lanham Act, a statute whose extraterritorial application was reinforced by *Morrison*.¹¹⁴

A. Rogue Wave – RICO

Prior to *Morrison*, several circuit courts adopted the conduct and effects test to determine the extraterritorial application of RICO.¹¹⁵ For example, the Ninth Circuit, upon finding that RICO is silent as to extraterritorial application, reasoned

¹¹⁴ These two statutes were chosen for discussion because each had case law discussing extraterritoriality prior to *Morrison*. Additionally, an analysis of RICO and the Lanham Act allows for comparison of a statute that likely does not overcome the presumption against extraterritoriality with one that does. For some of the other statutes whose extraterritoriality has been examined after *Morrison*, see *Sarei v. Rio Tinto, PLC*, Nos. 02-56256, 02-56390, 09-56381, 2011 WL 5041927, at *4--5 (9th Cir. Oct. 25, 2011) (Alien Tort Statute); *Tianrui Group Co. Ltd. v. Int'l Trade Com'n*, 661 F.3d 1322, 1328-32 (Fed. Cir. Oct. 11, 2011) (Tariff Act); *United States v. Elie*, No. S3 10 CRIM. 0336 LAK, 2012 WL 383403, at *2-3 (S.D.N.Y. Feb. 7, 2010) (Internet Gambling Business Act of 1970); and *Souryal v. Torres Advanced Enterprise Solutions, LLC*, No. 1:11CV643, 2012 WL 405048, at *5-7 (E.D. Va. Feb. 6, 2012) (Family and Medical Leave Act of 1993).

¹¹⁵ See *Poulos v. Caesars World, Inc.*, 379 F.3d 654, 663 (9th Cir. 2004); *Liquidation Com'n of Banco Intercontinental, S.A. v. Renta*, 530 F.3d 1339, 1351-52 (11th Cir. 2008); *United States v. Philip Morris USA Inc.*, 566 F.3d 1095, 1130 (D.C. Cir. 2009). See also *Kauthar SDN BHD v. Sternberg*, 149 F.3d 659, 671-72 (7th Cir. 1998) (opting to save determination on the extraterritorial scope of RICO for another day).

that the securities laws' conduct and effects test was useful in determining RICO's extraterritorial application.¹¹⁶ The Eleventh Circuit, after rejecting the assertion that RICO does not apply extraterritorially without an explicit statement to that effect, also adopted the conduct and effects test.¹¹⁷ In *United States v. Philip Morris USA Inc.*,¹¹⁸ the District of Columbia Circuit applied the effects test in determining that RICO applied where a British tobacco company was accused of deceiving U.S. consumers about the risks of smoking cigarettes.¹¹⁹ However, unlike the Ninth and Eleventh Circuits, the D.C. Circuit held that regulation of foreign conduct in such cases did not involve extraterritorial application, as the United States has a "legitimate interest in protecting its citizens within its borders."¹²⁰ The court stated that the presumption against extraterritoriality did not apply when a statute meets the effects test; rather, RICO would only have "true" extraterritorial reach if it were able to reach "foreign conduct that has *no* conduct on the United States."¹²¹

¹¹⁶ *Poulos*, 379 F.3d at 663.

¹¹⁷ *Liquidation Com'n of Banco Intercontinental, S.A.*, 530 F.3d at 1351-52.

¹¹⁸ 566 F.3d 1095 (D.C. Cir. 2009).

¹¹⁹ *Id.* at 1105-06, 1130.

¹²⁰ *Compare id.* at 1130, *with Poulos*, 379 F.3d at 663 *and Liquidation Com'n of Banco Intercontinental, S.A.*, 530 F.3d at 1351-52.

¹²¹ *Philip Morris USA Inc.*, 566 F.3d at 1130

These pre-*Morrison* analyses likely do not hold up today. In *Morrison*, the Supreme Court explained that the conduct and effects test stemmed from courts' misguided attempts to discern whether Congress would have wanted to apply Section 10(b) even though the statute was silent as to extraterritorial application.¹²² Without clear statutory indication that RICO was meant to apply extraterritorially, there is no reason to think that this test would be any more appropriate in a RICO case. Indeed, based on *Morrison* and the presumption against extraterritoriality, several courts have already concluded that RICO does not apply extraterritorially.¹²³ One district court, for example, specifically rejected the conduct and effects test with regard to RICO "for the same reasons" as in *Morrison*.¹²⁴

The D.C. Circuit's assertion that the effects test is a test for domestic, rather than extraterritorial, application is an interesting approach to RICO. While that

¹²² See *Morrison v. Nat'l Austr. Bank Ltd.*, 130 S. Ct. 2869, 2878-81 (2010).

¹²³ See, e.g., *Norex Petroleum Ltd. v. Access Indus., Inc.*, 631 F.3d 29 (2d Cir. 2010); *Sorota v. Sosa*, No. 11-80897-CV, 2012 WL 313530, at *4 (S.D. Fla. Jan. 31, 2012); *CGC Holdings Co., LLC v. Hutchens*, No. 11-CV-01012-RBJ-KLM, 2011 WL 5320988, at *14 (D. Colo. Nov. 1, 2011); *In re Toyota Motor Corp.*, 785 F. Supp. 2d 883, 913 (C.D. Cal. 2011); *U.S. v. Philip Morris USA, Inc.*, 783 F. Supp. 2d 23, 28-29 (D.D.C. 2011).

¹²⁴ See *In re Le-Nature's, Inc.*, No. 9-1445, 2011 WL 2112533, slip op. at *2 n.5 (W.D. Pa. May 26, 2011).

particular test may not survive *Morrison*, a workable test for domestic application of RICO involving foreign contacts might yet be developed. In *Morrison*, by creating the transactional test, the Supreme Court prescribed the domestic contacts necessary to establish a Section 10(b) claim.

The Court of Appeals for the Second Circuit recently had the opportunity to develop a minimum-domestic-contacts test for RICO claims but declined. In *Norex Petroleum Ltd. v. Access Industries, Inc.*,¹²⁵ Norex Petroleum Ltd. (Norex), a Canadian corporation, alleged that the primarily foreign group of defendants was involved in a widespread racketeering conspiracy aimed at taking over the Russian oil industry.¹²⁶ Norex claimed that defendants violated RICO by laundering money and committing other acts in furtherance of this scheme in the United States.¹²⁷ Defendants argued that Norex had failed to raise a RICO claim since the principal actions had taken place outside of the United States.¹²⁸ The Second Circuit held

¹²⁵ 631 F.3d 29 (2d Cir. 2010).

¹²⁶ *Id.* at 31. The defendants were primarily foreign actors, though several were U.S. citizens or conducted business in the United States. *Norex Petroleum Ltd. v. Access Indus., Inc.*, 304 F. Supp. 2d 570, 572 (S.D.N.Y. 2004), *rev'd*, 304 F.3d 29 (2010).

¹²⁷ *Norex Petroleum Ltd.*, 631 F.3d at 31. Specifically, Norex asserted that U.S. and foreign banking facilities concealed financial transactions to divert revenues on behalf of defendants. *Norex Petroleum Ltd.*, 304 F. Supp. 2d at 573.

¹²⁸ *Norex Petroleum Ltd.*, 631 F.3d at 31.

that, based on *Morrison*, RICO did not have extraterritorial application.¹²⁹ In its analysis, the court stated that *Morrison* created a “bright line rule” for determining a statute’s extraterritorial application: “[A]bsent a clear Congressional expression of a statute's extraterritorial application, a statute lacks extraterritorial reach.”¹³⁰

After noting that Second Circuit precedent held that “RICO is silent as to any extraterritorial application,” the court rejected each of Norex’s arguments to the contrary.¹³¹ Particularly, it found that: RICO’s broad language defining commerce¹³² did not indicate extraterritorial application;¹³³ the extraterritorial reach of RICO’s predicate acts such as wire fraud did not extend beyond the terms

¹²⁹ *Id.* at 33. The separate mail and wire fraud statutes have extraterritorial application, however, and should be available for criminal cases where a RICO claim is unavailable since RICO does not apply extraterritorially. Kopel et al., *supra* note 37, at 398.

¹³⁰ *Norex Petroleum Ltd.*, 631 F. 3d at 32 (citing *Morrison v. National Australia Bank Ltd.*, 130 S. Ct. 2869, 2877 (2010)).

¹³¹ 631 F. 3d at 33.

¹³² RICO prohibits the use or investment of racketeering proceeds affecting “interstate or foreign commerce.” 42 U.S.C. § 1962(a) (2011). The statute also prohibits a person from gaining or maintaining, through racketeering activities, an interest in an enterprise affecting “interstate or foreign commerce.” *Id.* § 1962(b).

¹³³ *Norex Petroleum Ltd.*, 631 F.3d at 33 (quoting *Morrison*, 130 S. Ct. at 2882) (“[W]e have repeatedly held that even statutes that contain broad language in their definitions of commerce do not apply abroad.”).

of those provisions to RICO as a whole;¹³⁴ and alleging some occurrence of domestic conduct was not enough to support domestic application of RICO.¹³⁵ Concluding that the slim domestic contacts alleged by Norex were not enough to support extraterritorial application of RICO, the court dismissed the claims under FRCP Rule 12(b)(6).¹³⁶ The court declined to discuss what domestic contacts would have supported RICO application despite the foreign contacts.

¹³⁴ *Id.* (quoting *Morrison*, 130 S. Ct. at 2882-83) (“[W]hile Section 30(b) of the Exchange Act . . . can be interpreted to apply abroad, ‘the presumption against extraterritoriality operates to limit that provision to its terms.’”).

¹³⁵ *Id.* (quoting *Morrison*, 130 S. Ct. at 2884) (“[I]t is a rare case of prohibited extraterritorial application that lacks all conduct with the territory of the United States.”).

¹³⁶ *Id.* Before the *Morrison* decision, the Second Circuit would have also engaged in an inquiry of whether Congress “would have intended that federal courts should be concerned with specific international controversies.” See *N. S. Fin. Corp. v. Al-Turki*, 100 F.3d 1046, 1051 (2d Cir. 1996), *overruled by* *Norex Petroleum Ltd.*, 631 F.3d 29 (2d Cir. 2010). Though the Second Circuit never settled on a specific test under this inquiry for the extraterritorial application of RICO, it indicated that it might have found a variation of the securities laws’ effects test appropriate. *Id.* at 1052 (commenting that the effects-oriented approach used in antitrust cases might be preferred in RICO cases as RICO’s substantive law and damages has similarities with parts of the Sherman Act).

Subsequently, as discussed below, a few district courts have considered this question.¹³⁷

In *Morrison*, the Supreme Court indicated that any test for domestic application should reflect the focus of the statute,¹³⁸ prompting several courts to perform a statutory analysis of RICO.¹³⁹ According to its statutory language, RICO does not criminalize racketeering activities standing alone – those are criminalized under other statutes; rather, the statute criminalizes racketeering activities in

¹³⁷ See, e.g., *In re Le-Nature's, Inc.*, No. 9-1445, 2011 WL 2112533, slip op. at *3 (W.D. Pa. May 26, 2011); *In re Toyota Motor Corp.*, 785 F. Supp. 2d 883, 914-15 (C.D. Cal. 2011); *European Cmty. v. RJR Nabisco, Inc.*, No. 02-CV-5771 (NGG)(VVP), 2011 WL 843957, at *5-6 (E.D.N.Y. Mar. 8, 2011) (mem. op.); *Cedeno v. Intech Group, Inc.*, 733 F. Supp. 2d 471, 472-73 (S.D.N.Y. 2010).

¹³⁸ See *Morrison v. Nat'l Austr. Bank Ltd.*, 130 S. Ct. at 2884 (examining the Exchange Act to identify the focus of congressional concern).

¹³⁹ See, e.g., *In re Le-Nature's, Inc.*, 2011 WL 2112533, slip op. at *3; *In re Toyota Motor Corp.*, 785 F. Supp. 2d at 914; *European Cmty.*, 2011 WL 843957, at *5-6; *Cedeno*, 733 F. Supp. 2d at 472-73.

connection with an enterprise.¹⁴⁰ This has led several courts to conclude that the focus of RICO is on the enterprise.¹⁴¹

The statute's purpose, which is stated as "the elimination of the infiltration of organized crime and racketeering into legitimate organizations operating in interstate commerce,"¹⁴² supports this conclusion. The reference to interstate commerce suggests that Congress's principal concern was focused on the corruption of domestic enterprises.¹⁴³ It can be argued that Congress would have

¹⁴⁰ 18 U.S.C. § 1962 (2011).

¹⁴¹ *See, e.g.*, *Sorota v. Sosa*, No. 11-80897-CV, 2012 WL 313530, at *4 (S.D. Fla. Jan. 31, 2012); *In re Le-Nature's, Inc.*, 2011 WL 2112533, slip op. at *3; *In re Toyota Motor Corp.*, 785 F. Supp. 2d at 914; *European Cmty.*, 2011 WL 843957, at *5; *Cedeno*, 733 F. Supp. 2d at 473. To determine the location of the enterprise in a RICO case, some courts have employed the "nerve center" test, which inquires as to where the decision-makers are. *See Mitsui O.S.K. Lines, Ltd. v. Seamaster Logistics, Inc.*, No. 11-2861 SC, 2012 WL 1657108, *4-5 (N.D. Cal. May 10, 2012); *European Cmty.*, 2011 WL 843957, at *5-6. Not all courts, however, have agreed that the enterprise is the focus of RICO. *See, e.g.*, *CGC Holding Co., LLC v. Hutchens*, No. 11-CV-01012-RBJ-KLM, 2011 WL 5320988, at *14 (D. Colo. Nov. 1, 2011) (finding that "racketeering activity" is the focus of RICO).

¹⁴² *Senate Comm. on the Judiciary, Report on Organized Crime Control Act of 1969*, S. REP. NO. 91-617, at 76.

¹⁴³ Additionally, in the prologue of the Organized Crime Control Act of 1970, the Act through which RICO was enacted, Congress published findings that organized criminal activities *in the*

addressed possible conflicts with foreign laws and procedures if RICO had been intended to apply to corruption abroad.¹⁴⁴ Thus, U.S. citizens harmed by a foreign enterprise may not have recourse under RICO.¹⁴⁵

Undoubtedly, *Morrison* will continue to be mentioned in discussions of statutes like RICO whose extraterritoriality is not yet settled.¹⁴⁶ A conclusion that a statute does not have extraterritorial reach is likely not enough to rule on a claim though, as shown by the creation of the *Morrison* transactional test for domestic application of Section 10(b). Next, an analysis of the Lanham Act reveals similar shortcomings where a statute has been deemed to have extraterritorial reach.

United States weaken the U.S. economy, “seriously burden interstate and foreign commerce, threaten the domestic security, and undermine general welfare” of the United States and its citizens. Pub. L. No. 91-452, 84 Stat. 922, 923, Statement of Findings and Purpose (emphasis added). In *Morrison*, the Court referred to the prologue of the Exchange Act as supporting the importance of the domestic exchange in § 10(b). *Morrison*, 130 S. Ct. at 2884-85.

¹⁴⁴ See *Morrison*, 130 S. Ct. at 2885 (refusing to find that the Exchange Act reaches foreign exchanges and transactions because Congress would have addressed conflicts with foreign laws and procedures if the statute were intended to apply abroad)

¹⁴⁵ This outcome would not be unlike the potential harsh realities of the § 10(b) transactional test. See *infra* notes 192-300 and accompanying text.

¹⁴⁶ See, e.g., *NewMarket Corp. v. Innospec, Inc.*, No. 3:10CV503-HEH, 2011 WL 1988073, at *6-8 (E.D. Va. May 20, 2011) (mem. op.) (discussing the extraterritoriality of the Robinson Patman Act, an anti-price discrimination statute).

B. Surfing the Waves – The Lanham Act

The extraterritorial application of the Lanham Act, which covers trademark infringement and unfair competition claims, was reinforced by *Morrison*.¹⁴⁷ It may be instructive in predicting the extraterritoriality of other federal laws after *Morrison* to understand the background supporting this finding of extraterritoriality. Furthermore, it is worth noting the tests that the federal appellate courts have developed limiting extraterritorial application of the Lanham Act.

In 1952, the Supreme Court held that jurisdiction existed in a Lanham Act case where the alleged trademark infringement was consummated outside the United States.¹⁴⁸ In *Steele v. Bulova Watch Co.*,¹⁴⁹ Bulova Watch Co. (Bulova), a New York corporation, sued Steele, a U.S. citizen, for stamping the name “Bulova” on watches that he assembled and sold in Mexico. The Court stated that international law did not prevent the United States from “governing the conduct of its own citizens . . . in foreign countries when the rights of other nations or their nationals are not infringed.”¹⁵⁰ Based on the Lanham Act’s “broad jurisdictional

¹⁴⁷ See *Morrison*, 130 S. Ct. at 2887 n.11.

¹⁴⁸ *Steele v. Bulova Watch Co.*, 344 U.S. 280, 281, 285 (1952). In deciding that jurisdiction existed, the Court did not find it necessary to pass on the merits of the claim. *Id.* at 283.

¹⁴⁹ 344 U.S. 280 (1952).

¹⁵⁰ *Id.* at 285.

grant,” which included “sweeping reach into ‘all commerce which may lawfully be regulated by Congress,’” the Court found legislative intent that the statute’s scope encompassed Steele’s activities abroad.¹⁵¹ The Court explained that Steele’s “operations and effects were not confined within the territorial limits of a foreign nation” – Steele bought some of the watch parts in the United States, and some of the watches made their way into the United States.¹⁵² Furthermore, the Court noted that affording Bulova relief would not impugn foreign law, as Mexico’s courts had nullified Steele’s trademark registration of “Bulova” in Mexico.¹⁵³ Significantly, in *Morrison*, the Supreme Court cited *Steele* for the proposition that the Lanham Act applies extraterritorially.¹⁵⁴

¹⁵¹ *Id.* at 286-87. The Court remarked, “[T]he United States is not debarred by any rule of international law from governing the conduct of its own citizens upon the high seas or even in foreign countries when the rights of other nations or their nationals are not infringed. With respect to such an exercise of authority there is no question of international law, but solely of the purport of the municipal law which establishes the duty of the citizen in relation to his own government.” *Id.* at 285 (citing *Skiriotes v. Florida*, 313 U.S. 69, 73 (1941)).

¹⁵² *Id.* at 286.

¹⁵³ *Id.* at 289.

¹⁵⁴ *Morrison v. Nat’l Australia Bank Ltd.*, 130 S. Ct. 2869, 2887 n.11 (2010) (rejecting the reading that *Steele* merely applied a nonextraterritorial statute based on U.S. conduct).

Lower courts subsequently created tests to determine when extraterritorial application was proper under the Lanham Act.¹⁵⁵ As in *Morrison*, settling the inquiry into extraterritoriality was not enough. Based on the Supreme Court’s analysis in *Steele*, the Second Circuit adopted a three-factor test that asks: (1) whether the subject defendant is a U.S. citizen; (2) whether such defendant’s conduct has a substantial effect on U.S. commerce; and (3) whether relief would create a conflict with foreign law.¹⁵⁶

¹⁵⁵ See, e.g., *McBee v. Delica Co., Ltd.*, 417 F.3d 107, 118-19 (1st Cir. 2005); *Reebok Intern., Ltd. v. Marnatech Enters., Inc.*, 970 F.2d 552, 554 (9th Cir. 1992); *Vanity Fair Mills, Inc. v. T. Eaton Co.*, 234 F.2d 633, 642 (2d Cir. 1956).

¹⁵⁶ *Vanity Fair Mills, Inc.*, 234 F.2d at 642. In *Steele*, the Supreme Court noted that the effects of Steele’s conduct reached the United States but never described the effects as “substantial.” See *Steele*, 344 U.S. at 285-87. That language appears to have been derived from the Fifth Circuit’s opinion in the case. See *id.* (citing *Bulova Watch Co. v. Steele*, 194 F.2d 567 (5th Cir. 1952)). The Fifth Circuit quoted commentary accompanying the Lanham Act that stated that the statute covers trademark uses in foreign, territorial, or interstate commerce, as well as uses in intrastate commerce that have a “substantial economic effect on interstate commerce.” *Bulova Watch Co. v. Steele*, 194 F.2d 567, 570 (5th Cir. 1952) (citing Daphne Robert, *Commentary on the Lanham Act*, 268-69 (1948)).

While the Fourth,¹⁵⁷ Fifth,¹⁵⁸ and Eleventh¹⁵⁹ Circuits have adopted the Second Circuit test with some variation, the First Circuit adheres to a standard based on the Supreme Court’s test for extraterritorial application under the antitrust laws.¹⁶⁰ That court explained that both antitrust and trademark law carry the risk that, absent some extraterritorial enforcement, violators who have harmed U.S. commerce may evade legal authority altogether.¹⁶¹ The First Circuit test requires a lesser showing of effects when the defendant is a U.S. citizen¹⁶² and disregards the

¹⁵⁷ See *Nintendo of Am., Inc. v. Aeropower Co., Ltd.*, 34 F.3d 246, 250 (4th Cir. 1994)

(requiring significant, rather than substantial, effects).

¹⁵⁸ See *Am. Rice, Inc. v. Producers Rice Mill, Inc.*, 518 F.3d 321, 327 (5th Cir. 2008); see also *id.* at 328 n.9 (suggesting that “some” effects might be sufficient).

¹⁵⁹ See *Int’l Café, S.A.L. v. Hard Rock Café Intern. (U.S.A.), Inc.*, 252 F.3d 1274, 1278 (11th Cir. 2001).

¹⁶⁰ *McBee*, 417 F.3d at 119-20 (allowing the test in *Hartford Fire Ins. Co. v. California*, 590 U.S. 764 (1993), to guide its analysis of the proper extraterritorial reach under the Lanham Act).

¹⁶¹ *Id.* at 119.

¹⁶² *Id.* at 118 (commenting that when the defendant is a U.S. citizen, “the domestic effect of the international activities may be of lesser importance and a lesser showing of domestic effects may be all that is needed”). Cf. *id.* at 120 (“We hold that the Lanham Act grants subject matter jurisdiction over extraterritorial conduct by foreign defendants only where the conduct has a *substantial effect* on United States commerce.”) (emphasis added).

conflict-of-law inquiry.¹⁶³ The Ninth Circuit similarly created a test based on antitrust law,¹⁶⁴ which it recently applied in *Love v. Associated Newspapers, Ltd.*,¹⁶⁵ making it the first federal appellate court to consider extraterritorial application of the Lanham Act since *Morrison*.

In *Love*, Mike Love, a band member of The Beach Boys,¹⁶⁶ claimed that the marketing and distribution of a CD in the United Kingdom and Ireland infringed on his limited exclusive right to use The Beach Boys trademark in live performances.¹⁶⁷ After acknowledging the requirement in *Morrison* for a “clear indication of an extraterritorial application,”¹⁶⁸ the Ninth Circuit distinguished the Lanham Act’s “sweeping language . . . expressly covering all commerce Congress can regulate” from the Exchange Act’s mere mention of “foreign commerce.”¹⁶⁹ The court found it unnecessary to reevaluate its case law concerning the Lanham

¹⁶³ *Id.* at 120. The court states that comity considerations should be analyzed as a prudential, rather than extraterritorial, question. *Id.* at 121.

¹⁶⁴ *Reebok Intern., Ltd. v. Marnatech Enters., Inc.*, 970 F.2d 552, 554 (9th Cir. 1992).

¹⁶⁵ 611 F.3d 601 (9th Cir. 2010).

¹⁶⁶ *The Beach Boys: The Complete Guide*, www.beachboys.com (last visited Feb. 16, 2012).

¹⁶⁷ *Love v. Assoc. Newspapers, Ltd.*, 611 F.3d 601, 612 (9th Cir. 2010). In a bit of humor, the court quipped, “Love wishes they could all be California torts.” *Id.* at 608.

¹⁶⁸ *Morrison v. Nat’l Austr. Bank Ltd.*, 130 S. Ct. 2869, 2878 (2010).

¹⁶⁹ *See Love*, 611 F.3d at 613 n.6.

Act's coverage of foreign activities.¹⁷⁰ Accordingly, the court turned to its three-factor test for proper extraterritorial application under that Act, which provides:

- (1) [T]he alleged violations must create some effect on American foreign commerce;
- (2) [T]he effect must be sufficiently great to present a cognizable injury to the plaintiffs under the Lanham Act; and
- (3) [T]he interests of and links to American foreign commerce must be sufficiently strong in relation to those of other nations to justify assertion of extraterritorial authority.¹⁷¹

Applying the test, the court found that “all relevant acts occurred abroad”¹⁷² and that Love failed to provide evidence of monetary injury in the United States caused by such acts.¹⁷³ The CD was conceived and manufactured overseas and was never sold or distributed in the United States.¹⁷⁴ Therefore, though the Lanham Act was

¹⁷⁰ *Id.*

¹⁷¹ *Id.* at 612-13. The Court noted that the test originated was originally developed for antitrust law. *Id.* at 613.

¹⁷² *Id.* at 613.

¹⁷³ *Id.* (refusing to find that Love's ticket sales in the United States suffered due to the CD since the alleged confusion would have occurred overseas).

¹⁷⁴ *Id.*

deemed to have extraterritorial application, the claims in *Love* were dismissed based on the Ninth Circuit’s test limiting the extent of that application.¹⁷⁵

A number of observations can be made concerning the courts’ treatment of the Lanham Act’s extraterritorial application. The *Love* decision offers a glimpse of a statute that has been deemed to have extraterritorial application in large part due to its definition of “commerce.”¹⁷⁶ When the petitioners in *Morrison* contended that Section 10(b) applied abroad because “interstate commerce” was defined to encompass “trade, commerce, transportation, or communication . . . between any foreign country and any state,” the Court responded that it has repeatedly held that statutes with broad language defining “commerce” do not have extraterritorial application, even in instances where “foreign commerce” was expressly included in the definition.¹⁷⁷ Yet, the Lanham Act has been deemed to

¹⁷⁵ *Id.*

¹⁷⁶ *See* *EEOC v. Arabian Am. Oil Co.*, 499 U.S. 244 252-53 (1991) (statutorily overruled by Civil Rights Act of 1991, § 109, 105 Stat. 1077, on other grounds).

¹⁷⁷ *Morrison v. Nat’l Australia Bank Ltd.*, 130 S. Ct. 2869, 2882 (2010) (quoting 15 U.S.C. §78c(a)(17)). For examples of statutes with broad language defining “commerce” not found to have extraterritorial application, see *EEOC v. Arabian American Oil Co.*, 499 U.S. 244, 252-53 (1991) (Title VII of the Civil Rights Act of 1964) (superseded by statute); *McCulloch v. Sociedad Nacional de Marineros de Honduras*, 372 U.S. 10, 19 (1963) (National Labor

have extraterritorial application based on its invocation of the Commerce Clause of the Constitution.¹⁷⁸ It is not readily apparent what areas of foreign commerce are covered under the Commerce Clause that would not also be covered by the Exchange Act’s definition of “commerce,” or any other statute’s similarly-worded definition of “commerce.”¹⁷⁹ Nonetheless, when considered together, *Morrison* and the extraterritorial findings of the Lanham Act suggest that a clear indication of extraterritorial application will not be found based on a statute’s definition of “commerce” unless the statute expressly calls upon the full extent of Congress’ power over commerce.

Additionally, the transactional test created in *Morrison* and the tests created by the federal circuit courts to determine the scope of the Lanham Act’s

Relations Act); and *New York Cent. R. Co. v. Chisholm*, 268 U.S. 29, 31 (1925) (Federal Employers’ Liability Act).

¹⁷⁸ See *Love*, 611 F.3d at 613 n.6.

¹⁷⁹ Compare, e.g., U.S. Constitution, Art. 1, § 8, Cl. 3 (“Congress shall have the power . . . [t]o regulate Commerce with foreign Nations, and among the several States, and with Indian tribes.”), with 15 U.S.C. 78c(a)(17) (“The term ‘interstate commerce’ means trade, commerce, transportation, or communication among the several States, or between any foreign country and any State, or between any State and any place or ship outside thereof. The term also includes intrastate use of: (A) any facility of a national securities exchange or of a telephone or other interstate means of communication, or (B) any other interstate instrumentality.”).

extraterritorial application indicate that proper application of a particular statute requires a more in-depth analysis than an inquiry into the statute's extraterritorial application.¹⁸⁰ *Morrison* sets the stage for a two-step analysis asking: (1) Does the subject statute contain a clear indication of extraterritorial application? And (2) what is the proper scope of its domestic (or extraterritorial) application?¹⁸¹ The second question, from which the *Morrison* transactional test¹⁸² and the tests developed by the federal circuit courts for the Lanham Act¹⁸³ emerged, really gets to the heart of the matter – proper application of the statute.

Stating that a statute has extraterritorial application when, in reality, that application is limited by considerations of U.S. connections may not be

¹⁸⁰ With regard to the Lanham Act though, practitioners should keep in mind that the Supreme Court has yet to hear a case involving the proper scope of extraterritorial application under the Act and therefore has not endorsed any of the federal appellate court tests.

¹⁸¹ A recent case on the extraterritoriality of RICO actually broke its discussion into two parts entitled: (1) “Whether RICO Applies Extraterritorially” and (2) “Whether [Defendant] Seeks Extraterritorial Application.” *See Sorota v. Sosa*, No. 11-80897-CV, 2012 WL 313530, at *2, *4 (S.D. Fla. Jan. 31, 2012).

¹⁸² *Morrison*, 130 S. Ct. at 2884-86 (inquiring into the proper domestic application of Section 10(b)).

¹⁸³ *Vanity Fair Mills, Inc. v. T. Eaton Co.*, 234 F.2d 633, 642 (2d Cir. 1956) (laying out the test for proper extraterritorial application of the Lanham Act).

significantly different than stating a statute does not have extraterritorial application when, in reality, so-called domestic application of the statute allows for foreign contacts so long as certain U.S. requirements are met.¹⁸⁴ In both instances, it is the specific degree and type of U.S. contacts necessary to state a claim that really matter.¹⁸⁵ Thus, the essential question is what are the minimum U.S. contacts, if any, necessary to state a claim under the applicable statute. The presumption against extraterritoriality would then only be applied once – in the court’s statutory analysis when answering this question.¹⁸⁶

¹⁸⁴ For instance, despite stating that the Lanham Act has extraterritorial reach, the Second Circuit looks for U.S. citizenship and effect on U.S. commerce when considering claims under the Act. *Vanity Fair Mills, Inc.*, 234 F.2d at 642. Additionally, the *Morrison* transactional test allows a claim under Section 10(b), a statute without extraterritorial reach, so long as the securities purchase or sale occurs on a domestic exchange or otherwise is a domestic transaction. *Morrison*, 130 S. Ct. at 2886.

¹⁸⁵ This is especially true in a time of globalization where an increasing number of cases involve both U.S. and foreign contacts. For a different perspective on extraterritorial application, see *United States v. Philip Morris USA Inc.*, 566 F. 3d 1095, 1130 (D.C. Cir. 2009), which defined “true” extraterritorial reach as “foreign conduct that has *no* conduct on the United States.”

¹⁸⁶ Compare *Morrison*, 130 S. Ct. at 2877-78, 2884 (applying the presumption against extraterritoriality when determining the extraterritorial reach of Section 10(b) and again when determining the domestic activity needed to state a Section 10(b) claim). In response to the plaintiff’s argument for domestic application of Section 10(b) in *Morrison*, Justice Scalia stated

Though the analysis in *Morrison* likely ensures that courts will first look to see if a statute has a clear indication of extraterritorial application, the more important battleground seems to be the second set of tests outlining proper application of a statute where both U.S. and foreign contacts are involved. Indeed, concurring in the judgment in *Morrison*, Justice Stevens commented, “[t]he real motor of the Court’s opinion, it seems, is not the presumption against extraterritoriality but rather the Court’s belief that transactions on domestic exchanges are ‘the focus of the Exchange Act’ and ‘the objects of [its] solicitude.’”¹⁸⁷

Overall, even though the presumption against extraterritoriality is not a new canon of statutory construction, *Morrison* has created a more difficult environment for plaintiffs to bring claims involving U.S. and foreign contacts. Defendants will bring more Rule 12(b)(6) challenges regarding extraterritorial application, asserting that either the statute at issue does not have extraterritorial reach or that the U.S. contacts are insufficient to state a claim. Indeed, in light of *Morrison*, use of the conduct and effects test in other areas of law that are not “textually

that the “presumption here (as often) is not self-evidently dispositive, but its application requires further analysis.” *Id.* at 2884.

¹⁸⁷ *Id.* at 2894 (Stevens, J., concurring in judgment).

plausible”¹⁸⁸ are susceptible to being overruled.¹⁸⁹ The future will likely be shaped by courts focusing on the language and objectives of a statute and developing tests therefrom.¹⁹⁰ An absence of statutory direction regarding conflicts with foreign

¹⁸⁸ *Id.* at 2884 n.9.

¹⁸⁹ It should be noted, however, that in determining if a clear indication of extraterritorial application exists, *Morrison* still allows courts to consult statutory context in deriving “the most faithful reading of the text.” *Id.* at 2883 (stating that a clear statement such as “this law applies abroad” is not necessary for a statutory finding of extraterritorial reach). For instance, in a post-*Morrison* decision, the Court of Appeals for the Eleventh Circuit stated that a clear expression of congressional intent that a statute apply abroad was needed to overcome the presumption against extraterritoriality and that “[s]uch an intention may appear on the face of the statute, but it may also be ‘inferred from . . . the nature of the harm the statute is designed to prevent,’ from the self-evident ‘international focus of the statute,’ and from the fact that ‘limit[ing] [the statute’s] prohibitions to acts occurring within the United States would undermine the statute’s effectiveness.’” *United States v. Belfast*, 611 F.3d 783, 811 (11th Cir. 2010) (internal citations omitted) (considering whether the Torture Act had extraterritorial application).

¹⁹⁰ One commentator concluded that *Morrison* “giv[es] courts total discretion to discern the ‘focus’ of any given statute.” Anthony J. Colangelo, *A Unified Approach to Extraterritoriality*, 97 VA. L. REV. 1019, 1044-45 (2011). As evidenced in *Morrison*, there is room to debate the focus of the congressional concern of a statute. *Compare Morrison*, 130 S. Ct. at 2884 (concluding that domestic exchanges and domestic transactions were the primary concern of Congress, *with id.* at 2894 (Stevens, J., concurring in judgment) (arguing, rather, that “public

laws will weigh in favor of a more limiting test.¹⁹¹

In addition to these broader statutory inquiries, *Morrison* generated specific concerns under the Exchange Act with respect to the effect of its new transactional test on Section 10(b) actions. The next section discusses the two prongs of the *Morrison* transactional test in detail, as well as the test's possible expansion in light of the recently completed Dodd-Frank study on Section 10(b) private rights of action.

V. The New Wave – Section 10(b) Transactional Test

After deciding in *Morrison* that Section 10(b) of the Exchange Act did not have extraterritorial application,¹⁹² the Supreme Court created a test to determine proper domestic application under the Act where foreign contacts are involved.¹⁹³ The *Morrison* transactional test requires either: (1) a purchase or sale of a security listed on a domestic exchange; or (2) a purchase or sale of a security made in the

interest” and the “interests of investors” were the focus of the Exchange Act). *See also* Sorota v. Sosa, No. 11-80897-CV, 2012 WL 313530, at *4 (S.D. Fla. Jan. 31, 2012) (focus of RICO is “enterprise”) and CGC Holding Co., LLC v. Hutchens, No. 11-CV-01012-RBJ-KLM, 2011 WL 5320988, at *14 (D. Colo. Nov. 1, 2011) (focus of RICO is “racketeering activity”).

¹⁹¹ *See id.* at 2885.

¹⁹² *Id.* at 2883.

¹⁹³ *Id.* at 2886 (referring to the adopted test as the “transactional test”).

United States.¹⁹⁴ While federal courts have already had occasion to interpret the *Morrison* transactional test in a variety of settings,¹⁹⁵ there are critical questions that remain unresolved. The analysis below begins with an examination of the first prong of the *Morrison* transactional test.

A. The First Wave – Purchase or Sale of a Security Listed on a U.S. Exchange

Under the first prong of the *Morrison* transactional test, a purchase or sale of a security listed on a domestic exchange is subject to Section 10(b).¹⁹⁶ The inquiry under this prong focuses on the circumstances in which the listing requirement is

¹⁹⁴ *Id.*

¹⁹⁵ *See, e.g.,* Quail Cruises Ship Mgmt Ltd. v. Agencia de Viagens CVC Tur Limitada, 645 F.3d 1307, 1310-11 (11th Cir. 2011) (over-the-counter purchase agreement designating the United States as the place of closing); *In re Vivendi Universal, S.A. Secs. Litig.*, 765 F. Supp. 2d 512, 530-31 (S.D.N.Y. 2011) (stock purchase on a foreign exchange); Plumbers’ Union Local No. 12 Pension Fund v. Swiss Reinsurance Co., 753 F. Supp. 2d 166, 178 (S.D.N.Y. 2010) (stock purchase by a U.S. resident); Elliott Assocs. v. Porsche Automobil Holding SE, 759 F. Supp. 2d 469, 472 (S.D.N.Y. 2010) (over-the-counter swap agreements).

¹⁹⁶ *Morrison*, 130 S. Ct. at 2886.

met.¹⁹⁷ In this respect, there are two ways that foreign companies seek to access capital markets through U.S. exchanges. First, ordinary shares, which are the foreign equivalent of common stock, may be listed on U.S. exchanges to trade as a U.S. company's stock normally would.¹⁹⁸ Second, ordinary shares of a foreign issuer may be represented on U.S. exchanges through American Depositary Receipts (ADRs),¹⁹⁹ which are securities that indicate ownership of ordinary shares but avoid the currency complications of foreign investments.²⁰⁰

¹⁹⁷ See generally Daniel Hemel, Comment, *Issuer Choice After Morrison*, 28 YALE J. ON REG. 471 (2011) (examining the courts' early interpretations of the first prong of the transactional test).

¹⁹⁸ For a listing of foreign companies with stock trading directly on NYSE, go to: *NYSE Listings Directory*, NYSE, http://www.nyse.com/about/listed/lc_ny_overview.html (go to "Issue Type" tab, select "Common Stock" from the Issue Type dropdown, and click on "NYSE-Listed Non-U.S. Companies").

For a listing of foreign companies with stock trading directly on NASDAQ, go to: NASDAQ INTERNATIONAL COMPANIES, <http://www.nasdaq.com/asp/nonUSoutput.asp> (click on "Download non U.S. company list" and then filter for non-ADR issuers). See sources cited *supra* note 28.

¹⁹⁹ For a listing of foreign companies with stock trading through ADRs on the NYSE, go to: *NYSE Listings Directory*, NYSE, http://www.nyse.com/about/listed/lc_ny_overview.html (go to "Issue Type" tab, select "ADS Common" from the Issue Type dropdown, and click on "NYSE-Listed Non-U.S. Companies").

After *Morrison*, plaintiffs have argued that so long as a company's shares are listed or represented on a U.S. exchange, a purchase or sale of stock on a foreign exchange satisfies the first prong of the transactional test.²⁰¹ Courts have

For a listing of foreign companies with stock trading through ADRs on NASDAQ, go to: NASDAQ INTERNATIONAL COMPANIES, <http://www.nasdaq.com/asp/nonUSoutput.asp> (click on "Download non U.S. company list" and then filter for ADR issuers).

²⁰⁰ See Velli, *supra* note 28, at S39. SEC requirements differ for each type of ADR, which include: Level I – unsponsored or sponsored, limited to over-the-counter trading; Level II – sponsored by the issuing company, listed on U.S. exchange; Level III – sponsored by the issuing company, listed on U.S. exchange, can conduct a public offering; Rule 144A – sponsored, limited to private placement with qualified institutional buyers. *DR Basics and Benefits*, BNY MELLON DEPOSITARY RECEIPTS, http://www.adrbnymellon.com/dr_edu_basics_and_benefits.jsp#11dr (last visited Feb. 16, 2012).

For an in-depth discussion of ADRs and *Morrison*, see Vincent M. Chiappini, *How American Are American Depositary Receipts? ADRs, Rule 10b-5 Suits, and Morrison v. National Australia Bank*, 52 B.C. L. Rev. 1795 (2011).

²⁰¹ See, e.g., *In re Royal Bank of Scotland PLC Secs. Litig.*, 765 F. Supp. 2d 327, 335-36 (S.D.N.Y. 2011) (ordinary shares represented by ADRs on NYSE); *In re Alstom SA Secs. Litig.*, 741 F. Supp. 2d 469, 471-72 (S.D.N.Y. 2010) (same); *Sglambo v. McKenzie*, 739 F. Supp. 2d 453, 487 (S.D.N.Y. 2010) (ordinary shares directly listed on NYSE).

consistently rejected this argument, explaining that such an outcome would undermine *Morrison*'s focus on domestic exchanges.²⁰²

For instance, in *In re Alstom SA, Securities Litigation*,²⁰³ class members had their Section 10(b) action dismissed where their purchases of a French company's shares occurred on a foreign stock exchange, despite the fact that the company's ADRs traded on the NYSE.²⁰⁴ The court explained that *Morrison* was "concerned

²⁰² See, e.g., *In re UBS Secs. Litig.*, No. 07 Civ. 11225(RJS), 2011 WL 4059356, at *4-7 (S.D.N.Y. Sept. 13, 2011); *In re Vivendi Universal, S.A. Secs. Litig.*, 765 F. Supp. 2d 512, 530-31 (S.D.N.Y. 2011); *In re Royal Bank of Scotland PLC*, 765 F. Supp. 2d at 336; *In re Alstom SA*, 741 F. Supp. 2d at 472-73. Note, however, that in this situation, plaintiffs may be able to institute suit under Section 18(a) of the Securities Exchange Act. 15 U.S.C. § 78r(a). Section 18(a) allows for a private right of action based on a materially false or misleading statement contained in any document filed with the SEC under the Exchange Act. The statute has strict reliance and loss causation requirements. Nonetheless, the statute should prove useful for investors who purchase (or sell) securities on a foreign exchange of a company whose shares also are listed on a U.S. stock exchange. Such issuers must file Exchange Act reports with the SEC. See Marc I. Steinberg, UNDERSTANDING SECURITIES LAW 300-01 (5th ed. 2009); Roger W. Kirby, *Access to United States Courts By Purchasers of Foreign Listed Securities in the Aftermath of Morrison v. National Australia Bank, Ltd.*, 7 HAST. BUS. L.J. 223, 262-63 (2011).

²⁰³ 741 F. Supp. 2d 469 (S.D.N.Y. 2010).

²⁰⁴ *In re Alstom SA*, 741 F. Supp. 2d at 471-72 (concerning ordinary shares purchased on the Euronext Paris Exchange).

with the territorial location where the purchase or sale was executed and the securities exchange laws that governed the transaction.”²⁰⁵ Similarly, in *Sglambo v. McKenzie*,²⁰⁶ where a Canadian company’s shares traded both on the Toronto Stock Exchange (TSE) and the American Stock Exchange (AMEX), the court summarily dismissed class members who had only purchased or sold common stock on the TSE.²⁰⁷ Overall, in determining whether a purchase or sale involves a security listed on a U.S. exchange, the lower courts uniformly have based their holdings on the territorial location of the exchange where the transaction at issue occurred.

²⁰⁵ *In re Alstom SA*, 741 F. Supp. 2d at 472-73 (quoting *Morrison v. National Australia Bank Ltd.*, 130 S. Ct. 2869, 2884 (2010)). *See also In re Vivendi Universal, S.A. Secs. Litig.*, 765 F. Supp. 2d at 527-34 (dismissing claims based on trades of a French company’s ordinary shares on the Paris Bourse exchange though shares were listed for non-trading purposes in support of ADRs on the NYSE).

²⁰⁶ 739 F. Supp. 2d 453 (S.D.N.Y. 2010).

²⁰⁷ *Sglambo v. McKenzie*, 739 F. Supp. 2d 453, 487 (S.D.N.Y. 2010). *See also In re Celestica Inc. Secs. Litig.*, No. 07 CV 312(GBD), 2010 WL 4159587, at *1 n.1 (S.D.N.Y. Oct. 14, 2010) (not reported) (disallowing purported class members who purchased Canadian defendant’s common stock on the TSE, though it also traded directly on the NYSE) *rev’d on other grounds*, *New Orleans Employees Ret. Sys. v. Celestica, Inc.*, No. 10-4702-cv, 2011 WL 6823204 (2d Cir. Dec. 29, 2011).

This territorial application is consistent with the directives expressed in *Morrison*, focusing on “purchases and sales of securities *in the United States.*”²⁰⁸ Indeed, if the transactional test could be met so long as stock that was purchased or sold on a foreign exchange had an identical or similar security listed on a U.S. exchange, one would have expected *Morrison*’s outcome to be different since National Australia had ADRs listed on the NYSE.²⁰⁹

Consistent with *Morrison*, courts have allowed purchases or sales of ADRs made on a U.S. exchange to proceed.²¹⁰ This is not to say all ADR purchases necessarily are within Section 10(b)’s scope. There has been some disagreement as to whether a purchase or sale of an ADR that trades over-the-counter satisfies the

²⁰⁸ *Morrison v. Nat’l Australia Bank Ltd.*, 130 S. Ct. 2869, 2884 (2010) (emphasis added) (“We know of no one who thought that the Act was intended to “regulat[e]’ *foreign* securities exchanges . . .”).

²⁰⁹ *Id.* at 2875-76.

²¹⁰ *See, e.g., In re Vivendi Universal, S.A. Secs. Litig.*, 765 F. Supp. 2d at 530-31 (allowing the Section 10(b) claim of both U.S. and foreign class members who purchased ADRs listed and traded on the NYSE to proceed); *Stackhouse v. Toyota Motor Co.*, Nos. CV 10-0922 DSF (AJWx), 2010 WL 3377409, at *1, *3 (C.D. Cal. July 16, 2010) (mem. op.) (analyzing *Morrison* and then appointing a pension fund as the lead plaintiff because the fund, which had purchased ADRs, suffered the largest loss).

Morrison transactional test.²¹¹ The next section, which discusses purchase or sales in the United States that do not occur on U.S. exchanges, will examine this situation further.

Overall, the listing of foreign stock directly, or the representation of foreign stock through ADRs, on a U.S. exchange alone is not enough to warrant Section 10(b) coverage under the *Morrison* transactional test. To satisfy the listing requirement of the first prong of the test, courts have required that the transaction *at issue* take place on a U.S. exchange. Purchases of ADRs on a domestic exchange come within Section 10(b) coverage. On the other hand, U.S. investors who purchase or sell securities outside of this country, whether on a stock exchange, over-the-counter, or in private transactions, are left without a Section 10(b) claim unless they can show that, pursuant to the second prong of the transactional test, the purchase or sale was made in the United States. The next section explores the scope of transactions covered by the second prong.

B. A More Tumultuous Wave – Purchase or Sale of Any Other Security in the United States

²¹¹ See, e.g., *In re Societe Generale Secs. Litig.*, No. 08 Civ 2495(RMB), 2010 WL 3910286, at *6-7 (S.D.N.Y. Sept. 29, 2010) (not reported) (noting in support of a Section 10(b) dismissal that the ADRs of a French company were not traded on a U.S. exchange).

The second prong of the *Morrison* transactional test raises a host of questions. In addressing this prong, the Supreme Court referenced to “purchases or sales made in the United States” as well as “domestic transactions.”²¹² Unfortunately, this terminology fails to provide sufficient light on the type of transactions that qualify under the second prong. Perhaps due to this lack of guidance, there is already a wealth of case law interpreting this terminology.²¹³

Many attempts by plaintiffs to satisfy the second prong of the *Morrison* transactional test have failed.²¹⁴ One of the arguments not surprisingly rejected by the courts is that a purchase of stock on a foreign exchange is a domestic

²¹² See *Morrison*, 130 S. Ct. at 2884, 2885-86.

²¹³ See, e.g., *Quail Cruises Ship Mgmt Ltd. v. Agencia de Viagens CVC Tur Limitada*, 645 F.3d 1307, 1310-11 (11th Cir. 2011); *Plumbers’ Union Local No. 12 Pension Fund v. Swiss Reinsurance Co.*, 753 F. Supp. 2d 166, 178-79 (S.D.N.Y. 2010); *Anwar v. Fairfield Greenwich Ltd.*, 728 F. Supp. 2d 372, 405 (S.D.N.Y. 2010); *Stackhouse*, 2010 WL 3377409, at *1.

²¹⁴ See, e.g., *Cascade Fund, LLP v. Absolute Capital Mgmt Holdings Ltd.*, No. 08-cv-01381-MSK-CBS, 2011 WL 1211511, slip op. at *14 (D. Colo. Mar. 31, 2011); *In re Royal Bank of Scotland Group PLC Secs. Litig.*, 765 F. Supp. 2d 327, 336 (S.D.N.Y. 2011); *Elliott Assocs. v. Porsche Automobil Holding SE*, 759 F. Supp. 2d 469, 474-76 (S.D.N.Y. 2010); *In re Societe Generale Secs. Litig.*, 2010 WL 3910286, at *6; *Plumbers’ Union Local No. 12 Pension Fund*, 753 F. Supp. 2d at 178; *Cornwell v. Credit Suisse Group*, 729 F. Supp. 2d 620, 625-26 (S.D.N.Y. 2010).

transaction because the purchase was made by a U.S. resident.²¹⁵ Clearly, nothing in *Morrison* indicates that for Section 10(b) purposes the location of a transaction turns on a purchaser's residency or citizenship.²¹⁶ As one court observed, “[a] foreign resident can make a purchase within the United States, and a United States resident can make a purchase outside the United States,” but Section 10(b) only reaches the former.²¹⁷ Indeed, ascertaining the reach of Section 10(b) based on the U.S. residency (or citizenship) of the complainant would inappropriately revive a primary component of the abandoned “effects” test.²¹⁸ As a consequence, under *Morrison*'s transactional test, Section 10(b) does “not extend to foreign securities trades executed on foreign exchanges even if purchased or sold by American investors.”²¹⁹

²¹⁵ See, e.g., *In re BP P.L.C. Secs. Litig.*, No. 4:10-MD-2185, 2012 WL 432611, at *16 (S.D. Tex. Feb. 13, 2011); *In re UBS Secs. Litig.*, No. 07 Civ. 11225(RJS), 2011 WL 4059356, at *7 (S.D.N.Y. Sept. 13, 2011); *Plumbers' Union Local No. 12 Pension Fund*, 753 F. Supp. 2d at 178; *Cornwell*, 729 F. Supp. 2d at 624.

²¹⁶ *Plumbers' Union Local No. 12 Pension Fund*, 753 F. Supp. 2d at 178.

²¹⁷ *Id.*

²¹⁸ *Cornwell*, 729 F. Supp. 2d at 624 (involving stock purchased on foreign exchange by a U.S. pension fund).

²¹⁹ *Id.* at 625-26 (rejecting the claim of a U.S. retirement fund that had bought Swiss stock on a Swiss exchange).

Place of injury has also been rejected as a basis for Section 10(b) coverage under *Morrison*.²²⁰ One court commented, “there is no textual or logical basis [in the Exchange Act] for making injury a sufficient condition for the statute's application without the existence of a domestic purchase or sale.”²²¹ After *Morrison*, therefore, a U.S. investor injured in the United States from a purchase or sale transacted abroad is without recourse under Section 10(b).

Next, consistent with *Morrison*'s rejection of the conduct test, courts have deemed the place of deceptive conduct irrelevant to the transactional test.²²² For

²²⁰ *In re UBS Secs. Litig.*, 2011 WL 4059356, at *8; *Plumbers' Union Local No. 12 Pension Fund*, 753 F. Supp. 2d at 178.

²²¹ *Id.*

²²² *See, e.g.*, *Basis Yield Alpha Fund (Master) v. Goldman Sachs Group, Inc.*, 798 F. Supp. 2d 533, 537 (S.D.N.Y. 2011) (noting that the Complaint includes “numerous instances of U.S.-based conduct” but fails to allege that a purchase or sale occurred in the United States); *SEC v. Goldman Sachs & Co.*, 790 F. Supp. 2d 147, 158 (S.D.N.Y. 2011) (“The shortcoming of all this U.S.-based conduct is precisely that—it is just conduct.”); *Plumbers' Union Local No. 12 Pension Fund*, 753 F. Supp. 2d at 179. In *Cornwell v. Credit Suisse Group*, the court discussed how, in *Morrison*, the Supreme Court: discarded the conduct and effects tests, which valued whether the harmed investor was American or foreign; did not place importance on the place where the deceptive conduct began; and referred to *E.E.O.C. v. Arabian American Oil Co.*, 499 U.S. 244 (1991), a case where extraterritorial application was rejected despite some domestic contacts. *Id.* at 626 (referring to *Morrison*, 130 S. Ct. at 2879, 2884-85).

example, in *SEC v. Goldman Sachs Group, Inc.*,²²³ the SEC referenced Goldman Sachs' actions in this country in an attempt to state Section 10(b) claims that involved purchases of notes by a German bank and sales of credit default swaps by a Netherland bank. The alleged deceptive conduct included transmission of false and misleading marketing materials and emails. The court dismissed the claims, explaining that domestic conduct is no longer the test for Section 10(b) liability.²²⁴ As *Morrison* reasons, "Section 10(b) does not punish deceptive conduct, but only transactions that take place in the United States that involve deceptive conduct committed 'in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered.'"²²⁵

Likewise, assertions that a transaction ought to be considered a domestic transaction where the decision to invest was made in the United States have proven futile.²²⁶ Concluding that an investment decision in the United States to purchase

²²³ 790 F. Supp. 2d 147 (S.D.N.Y. 2011).

²²⁴ *Goldman Sachs Group, Inc.*, 790 F. Supp. 2d at 158-61.

²²⁵ *Morrison v. Nat'l Australia Bank Ltd.*, 130 S. Ct. 2884 (2010). Of course, Section 10(b) also prohibits "manipulative" conduct. *See Santa Fe Indus., Inc. v. Green*, 430 U.S. 462 (1977); Marc I. Steinberg, *SECURITIES REGULATION* 414-25 (rev. 5th ed. 2009).

²²⁶ *See, e.g., Cascade Fund, LLP v. Absolute Capital Mgmt Holdings Ltd.*, No. 08-cv-01381-MSK-CBS, 2011 WL 1211511, slip op. at *6 (D. Colo. Mar. 31, 2011); *In re Royal Bank of Scotland Group PLC Secs. Litig.*, 765 F. Supp. 2d 327, 336 (S.D.N.Y. 2011) (U.S. pension and

stock has “no bearing on where the stock was ultimately purchased,”²²⁷ courts have rejected this argument.²²⁸ One court reasoned that allowing claims just because “some acts that ultimately resulted in execution of the transaction abroad [took] place in the United States” would only serve to revive the rejected conduct test.²²⁹

Several plaintiffs have advocated a seemingly more persuasive position that also has met with failure thus far, contending that purchase orders placed in the United States for stock listed on a foreign exchange are domestic transactions under *Morrison*.²³⁰ As one court reasoned, “the Exchange Act was not intended to

retirement funds bought British stock on British and Amsterdam exchanges); *Plumbers’ Union Local No. 12 Pension Fund*, 753 F. Supp. 2d at 178. In *In re Royal Bank of Scotland Group PLC Securities Litigation*, plaintiffs additionally noted that the decision was based on the advice of U.S.-based asset managers. 765 F. Supp. 2d at 336.

²²⁷ *Plumbers’ Union Local No. 12 Pension Fund*, 753 F. Supp. 2d at 178 (citing plaintiff’s rejected argument for Section 10(b) coverage in *Cornwell v. Credit Suisse Group*, 729 F. Supp. 2d 620, 622 (S.D.N.Y. 2010)).

²²⁸ See, e.g., *id.* at 178; *Cornwell*, 729 F. Supp. 2d at 622, 627.

²²⁹ *Cornwell*, 729 F. Supp. 2d at 624.

²³⁰ See, e.g., *Plumbers’ Union Local No. 12 Pension Fund*, 753 F. Supp. 2d at 178; *Stackhouse v. Toyota Motor Co.*, Nos. CV 10-0922 DSF (AJWx), etal. , 2010 WL 3377409, at *1 (C.D. Cal. July 16, 2010) (mem. op.). In *In re BP P.L.C. Securities Litigation*, plaintiffs unsuccessfully tried to rely on the trading rules of the LSE to establish a domestic transaction. No. 4:10-MD-2185, 2012 WL 432611, at *68-69 (S.D. Tex. Feb. 13, 2011). They explained that LSE’s electronic

regulate foreign exchanges” and that, due to the potential for conflicts with foreign law, “United States securities laws should defer to the law of the country where the security is exchanged.”²³¹ Based on *Morrison’s* rationale, therefore, it may well be that transactions effected on foreign exchanges can never be domestic transactions coming within Section 10(b) coverage.

After having gone through the rejected bases for defining a domestic transaction – that is, residency or citizenship, location where injury occurred, location of deceptive conduct, location of investment decision, and location where the purchase orders were placed – it is time to examine a basis that has yielded inconsistent responses from the courts. The theory that domestic transactions under the second prong of *Morrison* referred to “purchases and sales of securities explicitly *solicited* by the issuer within the United States” was first suggested and

trading network could pair a third-party market maker in the United States with a U.S. investor and argued that this type of transaction takes place in the United States, not in London. *Id.* at *68. The court replied, “carving out an exception for the purchase of securities on the LSE because some acts that ultimately result in the execution of a transaction abroad take place in the United States would be to reinstate the conduct test.” *Id.* at *69.

²³¹ *Stackhouse*, 2010 WL 3377409, at *1. See *Plumbers’ Union Local No. 12 Pension Fund*, 753 F. Supp. 2d at 179 (rejecting a Section 10(b) claim where a U.S. pension fund placed a purchase order in the United States for Swiss stock on a Swiss exchange)

adopted in *Stackhouse v. Toyota Motor Co.*,²³² a memorandum opinion designating a lead plaintiff for a securities class action suit.²³³ A decision from the Southern District of New York subsequently accepted this interpretation of the *Morrison* transaction test,²³⁴ but that district has declined to consistently follow it.²³⁵ To add to this division, the District Court for the District of Colorado found *Stackhouse*'s interpretation unpersuasive.²³⁶ In *Cascade Fund, LLP v. Absolute Capital Management Holdings, Ltd.*,²³⁷ the court pointed out that *Morrison* did not attribute any significance to the place of solicitation in reaching its holding.²³⁸ Indeed, it is questionable whether any part of the transactional test relies on

²³² Nos. CV 10-0922 DSF (AJWx), et al. , 2010 WL 3377409, at *1 (C.D. Cal. July 16, 2010) (mem. op.) (emphasis added).

²³³ *Stackhouse*, 2010 WL 3377409, at *1.

²³⁴ See *Elliott Assocs. v. Porche Automobil Holding SE*, 759 F. Supp. 2d 469, 476 (S.D.N.Y. 2010).

²³⁵ Compare *Elliott Assocs.*, 759 F. Supp. 2d at 476 (quoting *Stackhouse*), with *SEC v. Goldman Sachs & Co.*, 790 F. Supp. 2d 147, 158-61 (S.D.N.Y. 2011) (failing to key in on the alleged solicitation by Goldman Sachs and instead dismissing two Section 10(b) claims because the SEC failed to allege that “any party incurred ‘irrevocable liability’ in the United States”).

²³⁶ *Cascade Fund, LLP v. Absolute Capital Mgmt Holdings Ltd.*, No. 08-cv-01381-MSK-CBS, 2011 WL 1211511, slip op. at *6 (D. Colo. Mar. 31, 2011) (finding *Stackhouse* unpersuasive).

²³⁷ No. 08-cv-01381-MSK-CBS, 2011 WL 1211511 (D. Colo. Mar. 31, 2011).

²³⁸ *Cascade Fund, LLP*, 2011 WL 1211511, slip op. at *6.

solicitation, as this would rekindle aspects of the conduct test that the Supreme Court expressly overruled.²³⁹

More recently, the District Court for the Southern District of New York has focused on the notion of “irrevocable liability” rather than solicitation when considering domestic transactions under *Morrison*.²⁴⁰ This treatment stems from an analysis of case law and the statutory language of the Exchange Act performed by the court in *Plumbers’ Union Local No. 12 Pension Fund v. Swiss Reinsurance Co.*²⁴¹ There, the court determined that a purchase under the Exchange Act occurs when the parties incurred “irrevocable liability” to consummate the transaction.²⁴²

²³⁹ See *Morrison v. Nat’l Australia Bank Ltd.*, 130 S. Ct. 2869, 2887 (2010) (overruling *Leasco Data Processing Equipment Corp. v. Maxwell*, 468 F.2d 1326 (1972), the case involving fraudulent inducement from which the conduct test arose). See also *id.* at 2885 (“[W]e reject the notion that the Exchange Act reaches conduct in this country affecting exchanges or transactions abroad . . .”).

²⁴⁰ See, e.g., *Basis Yield Alpha Fund (Master) v. Goldman Sachs Group, Inc.*, 798 F. Supp. 2d 533, 537 (S.D.N.Y. 2011); *Goldman Sachs & Co.*, 790 F. Supp. at 157-58.

²⁴¹ 753 F. Supp. 2d 166 (S.D.N.Y. 2010).

²⁴² *Id.* at 177.

In April 2012, the Second Circuit adopted a similar test for domestic transactions under *Morrison*.²⁴³ The court stated in *Absolute Activist Value Master Fund Ltd. v. Ficeto*²⁴⁴ that a domestic transaction requires irrevocable liability to be incurred or title to be transferred within the United States.²⁴⁵ In discussing irrevocable liability, the court noted that the definitions of the terms “purchase” and “sale” in the Exchange Act include any contract for such undertaking.²⁴⁶ The court explained that the point at which parties contractually obligate themselves to

²⁴³ See *Absolute Activist Value Master Fund Ltd. v. Ficeto*, 677 F.3d 60 (2d Cir. 2012)

(Discussion, Part C).

²⁴⁴ 677 F.3d 60 (2d Cir. 2012).

²⁴⁵ *Id.*

²⁴⁶ *Id.* (discussing 15 U.S.C § 78c (13)-(14) (2011)). When construing the terms “purchase” and “sale” under the Exchange Act, courts have asked when the subject party became irrevocably bound” to buy or sell the securities such that “his rights and obligations became fixed.” *Portney v. Revlon, Inc.*, 650 F.2d 896, 898 (7th Cir. 1981). See also *DiLorenzo v. Murphy*, 443 F.3d 224, 229 (2d Cir. 2006) (stating that a purchase occurs under the Exchange Act once the purchaser “fully and irrevocably pa[ys]” for the securities); *Blau v. Ogsbury*, 210 F.2d 426, 427 (2d Cir. 1954) (explaining that a person is a purchaser under the Exchange Act when he “incur[s] an irrevocable liability to take and pay for stock”).

take and pay for a security or deliver a security can be used to determine the locus of that securities transaction.²⁴⁷

The facts needed to satisfy the irrevocable liability analysis for domestic transactions under *Morrison* are unresolved, as the post-*Morrison* cases using the analysis have either been dismissed for failure to allege sufficient facts²⁴⁸ or granted leave to amend the complaint with further facts.²⁴⁹ In *Absolute Activist Value Master Fund Ltd.*, the court suggested that facts regarding “the formation of contracts, the placement of purchase orders, the passing of title, or the exchange of money” would help to show that the parties became irrevocably bound or that the title passed in the United States.²⁵⁰ It is also instructive to make note of one of the instances where the alleged facts were found lacking.

In *SEC v. Goldman Sachs & Co.*,²⁵¹ the SEC alleged that the securities transaction at issue closed in New York. The court held, however, that there were

²⁴⁷ *Absolute Activist Value Master Fund Ltd.*, 677 F.3d at 60+.

²⁴⁸ *See, e.g.*, *Basis Yield Alpha Fund (Master) v. Goldman Sachs Group, Inc.*, 798 F. Supp. 2d 533, 537 (S.D.N.Y. 2011); *SEC v. Goldman Sachs & Co.*, 790 F. Supp. 2d 147, 157-61 (S.D.N.Y. 2011); *Plumbers’ Union Local No. 12 Pension Fund v. Swiss Reinsurance Co.*, 753 F. Supp. 2d 166, 178 (S.D.N.Y. 2010).

²⁴⁹ *See Absolute Activist Value Master Fund Ltd.*, 677 F.3d at 60+.

²⁵⁰ *Id.*

²⁵¹ 790 F. Supp. 2d 147 (S.D.N.Y. 2011).

no facts alleging that any party incurred irrevocable liability in the United States.²⁵²

It explained that, under *Morrison*, “the closing, absent ‘a purchase or sale . . . made in the United States,’ is not determinative.”²⁵³ Thus, it appears that courts will not presume that parties incurred irrevocable liability at the closing, even though that may often be the case.²⁵⁴

Other interpretations of “domestic transactions” under *Morrison* have considered the location where the subscription agreements were accepted.²⁵⁵ For instance, in *Anwar v. Fairfield Greenwich Ltd.*,²⁵⁶ a case brought by foreign investors against Bernie Madoff’s foreign feeder funds, the plaintiffs argued that

²⁵² *Goldman Sachs & Co.*, 790 F. Supp. 2d at 159-61.

²⁵³ *Id.* at 158-59.

²⁵⁴ See BLACK’S LAW DICTIONARY 291 (9th ed. 2009) (defining “closing” as when “the transaction is consummated”).

²⁵⁵ See, e.g., *Cascade Fund, LLP v. Absolute Capital Mgmt Holdings, Ltd.*, No. 08-cv-01381-MSK-CBS, 2011 WL 1211511, slip op. at *7 (D. Colo. Mar. 31, 2011) (granting defendant’s motion to dismiss after concluding that completion of the transaction did not occur until defendant accepted the subscription agreement in the Cayman Islands); *Anwar v. Fairfield Greenwich Ltd.*, 728 F. Supp. 2d 372, 405 (S.D.N.Y. 2010) (mandating further discovery before ruling on defendant’s motion to dismiss where plaintiff’s transactions were not on foreign exchanges and where the subscription agreements were allegedly accepted in New York).

²⁵⁶ 728 F. Supp. 2d 372 (S.D.N.Y. 2010) (a Bernie-Madoff feeder fund case).

the second prong of the *Morrison* transactional test was met because, though they sent their subscription agreements to foreign administrators, a transaction did not occur until the agreements were accepted in the defendants' New York offices.²⁵⁷ With no securities purchases or sales “executed on a foreign exchange,” the court stated that *Anwar* entailed a “novel and more complex application of *Morrison*'s transactional test.”²⁵⁸ The court concluded that, given the unique financial interests, transaction structures, and party relationships involved, more facts were needed to determine if plaintiffs' purchases occurred in the United States.²⁵⁹

Considering the location where the subscription agreement was accepted is consistent with the irrevocable liability analysis. Acceptance of an agreement presumably forms a contract that makes the parties liable to each other if they fail

²⁵⁷ *Id.* at 405.

²⁵⁸ *Id.* The court noted that the securities were “listed . . . [but] not actually traded” on a foreign exchange. *Id.*

²⁵⁹ *Id.* For another case brought by Madoff's feeder funds with similar results, see *In re Optimal U.S. Litigation*, No. 10 Civ. 4095(SAS), 2011 WL 1676067 (S.D.N.Y. May 2, 2011). In that case, the court denied a defendant's motion to dismiss, stating that a more fully-developed factual record was needed to establish “where all of Plaintiffs' shares were ‘issued,’ where they wired their subscription payments, what the statement ‘WE BOUGHT FOR YOUR ACCOUNT IN: NYS’ means, and where their subscription agreements were ‘accepted.’” *Id.* at *12.

to pay for or deliver the security as promised.²⁶⁰ Thus, under this approach, a plaintiff who pleads facts alleging that a private securities agreement was accepted in the United States may well satisfy the irrevocable liability analysis for demonstrating a domestic transaction under *Morrison*.

Arguably, there are instances where courts have interpreted *Morrison* too broadly to exclude certain privately placed securities transactions from Section 10(b) coverage.²⁶¹ For example, in *Elliott Associates v. Porsche Automobil Holding SE*,²⁶² the court considered whether there was a substantive distinction between the placement of a buy order in the United States for a security traded abroad, which it did not consider a “domestic transaction,” and the execution of a

²⁶⁰ See Restatement (Second) of Contracts § 1 (“A contract is a promise or set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty.”).

²⁶¹ See, e.g., *Elliott Assocs. v. Porsche Automobil Holding SE*, 759 F. Supp. 2d 469, 476 (S.D.N.Y. Dec. 30, 2010) (dismissing a Section 10(b) claim where the swap agreement was executed in the United States but the underlying shares traded on a foreign exchange); *In re Societe Generale Secs. Litig.*, No. 08 Civ. 2495(RMB), 2010 WL 3910286, slip op. at *5-7 (S.D.N.Y. Sept. 29, 2010) (dismissing Section 10(b) claims based on ADRs that were not traded on a U.S. exchange) .

²⁶² 759 F. Supp. 2d 469 (S.D.N.Y. 2010) (U.S. and foreign hedge funds, which were all managed from New York, sued foreign companies under the Exchange Act.).

swap agreement in the United States referencing foreign stock.²⁶³ Plaintiffs argued that, although the Volkswagen ordinary shares underlying their swap agreements traded on a German exchange, the agreements qualified as domestic transactions under *Morrison* since they were signed in the United States.²⁶⁴ The court determined that the economic reality was that the swap agreements were “essentially ‘transactions conducted upon foreign exchanges and markets,’ and not ‘domestic transactions’ that merit[ed] the protection of [Section] 10(b).”²⁶⁵ Referencing *Morrison*, the court relied on the presumption against extraterritoriality and that the Exchange Act was not intended to regulate foreign securities transactions.²⁶⁶ The court concluded that “transactions in foreign-traded securities – or swap agreements that reference them – where only the purchaser is located in the United States” are not covered by Section 10(b).²⁶⁷

²⁶³ *Elliot Assocs.*, 759 F. Supp. 2d at 474-76. A security swap agreement is a private contract that fluctuates in value based on the price of the shares referenced within; it is not traded on any exchange.

²⁶⁴ *Id.* at 474.

²⁶⁵ *Id.* at 476.

²⁶⁶ *Id.* (citing *Morrison v. National Australia Bank Ltd.*, 130 S. Ct. 2869, 2884 (2010)).

²⁶⁷ *Id.* The judge stated, “I am loathe to create a rule that would make foreign issuers with little relationship to the U.S. subject to suits here simply because a private party in this country entered into a derivatives contract that references the foreign issuer's stock. Such a holding

In a more expansive decision denying Section 10(b) coverage, *In re Societe Generale Securities Litigation*,²⁶⁸ the court held that a transaction involving over-the-counter ADRs was not a domestic transaction under *Morrison*.²⁶⁹ The court reasoned that “[t]rade in ADRs is considered to be a ‘predominantly foreign securities transaction.’”²⁷⁰ For further support, the court focused on the foreign

would turn *Morrison*’s presumption against extraterritoriality on its head.” *Id.* One commentary expressed concern this approach “would likely deny all purchasers of ADRs a remedy under Section 10(b).” Christian J. Ward, Esq., & J. Campbell Barket, Esq., Comment, *Morrison v. National Australia Bank: The Impact on Institutional Investors*, 27 No. 17 WL J. Corp. Officers & Dirs. Liability 1 (2012).

For another case that considered the economic reality of the transaction, see *Valentini v. Citigroup*, No. 11 Civ. 1355(LBS), 2011 WL 6780915, at *13-14 (S.D.N.Y. Dec. 27, 2011), which determined that convertible securities satisfied the second prong of the *Morrison* transactional test where the securities were notes that could, under certain circumstances, convert into domestically-traded stock.

²⁶⁸ *In re Societe Generale Secs. Litig.*, No. 08 Civ. 2495(RMB), 2010 WL 3910286 (S.D.N.Y. Sept. 29, 2010).

²⁶⁹ *Id.* at *6.

²⁷⁰ *Id.* at *4, *6 (quoting *Copeland v. Fortis*, 586 F. Supp. 2d 498, 506 (S.D.N.Y. 2010)).

However, *In re SCOR Holding (Switzerland) AG Litigation*, the case that *Copeland* derived this statement from, does not actually stand for this assertion. See *Copeland*, 685 F. Supp. 2d at 506 (citing *In re SCOR Holding (Switzerland) AG Litig.*, 537 F. Supp. 2d 556, 562 (S.D.N.Y. 2008)).

defendant's ADRs that were traded "in a less formal market [than a U.S. exchange] with lower exposure to U.S.-resident buyers."²⁷¹

Both *Elliott Associates* and *In re Societe Generale* unduly expand *Morrison's* scope. Since the second prong of the transactional test asks if "the purchase or sale is made in the United States," an execution of a swap agreement in the United States should satisfy *Morrison*.²⁷² Likewise, the focus with respect to over-the-counter ADRs should be on whether the ADR was purchased in the United States. By focusing instead on the foreign shares underlying these securities, the familiarity of the market where the ADRs are traded, and the number of U.S. resident purchasers, the court in *In re Societe Generale* misapplied the *Morrison* transactional test.

Prior to *Morrison*, the court in *In re SCOR Holding* merely stated, "Assuming that the purchase of [ADRs] on the NYSE . . . may be viewed as predominantly foreign securities transactions, it is not contested here that this Court has subject matter jurisdiction over claims arising out of such transactions under the effects test without consideration of the conduct test." 537 F. Supp. 2d at 562. Thus, since the jurisdiction of the ADRs was uncontested, the court had no occasion to make a determination that the ADRs *actually* were predominantly foreign securities.

²⁷¹ *In re Societe Generale Secs. Litig.*, 2010 WL 3910286, slip op. at *6. Thus, while Section 10(b) evidently covers purchases or sales of ADRs listed on U.S. exchanges, the statute may not cover ADRs traded over-the-counter.

²⁷² See *Morrison v. Nat'l Austr. Bank Ltd.*, 130 S. Ct. 2869, 2886 (2010) (transactional test).

After *Morrison*, parties may seek by contractual agreement to bring their transaction within Section 10(b) coverage. Hence, to what extent can parties use contractual language to satisfy *Morrison*'s "domestic transactions" prong? In *Quail Cruises Ship Management Ltd. v. Agencia de Viagens CVC Tur Limitada*,²⁷³ for example, a foreign corporation argued that the private purchase of foreign stock from another foreign corporation constituted a purchase or sale in the United States under *Morrison* because the share purchase agreement contained a forum selection clause providing for U.S. law and designated U.S. law offices as the place of closing.²⁷⁴ The court dismissed the claim, explaining that "[a]dopting a rule that permits the intent of parties located abroad and contracting from their home countries in a wholly off-shore transaction to apply United States securities law is inconsistent with *Morrison*."²⁷⁵

On appeal, the Eleventh Circuit vacated and remanded the decision.²⁷⁶ The appellate court observed that the plaintiffs had alleged that the closing "*actually*

²⁷³ 732 F. Supp. 2d 1345 (S.D. Fla. 2010).

²⁷⁴ *Id.* at 1347, 1349 (S.D. Fla. 2010).

²⁷⁵ *Id.* at 1350.

²⁷⁶ *See generally* *Quail Cruises Ship Mgmt Ltd. v. Agencia de Viagens CVC Tur Limitada*, 645 F.3d 1307 (11th Cir. 2011).

occurred in the United States.”²⁷⁷ The court then relied on the definition of “closing” in *Black’s Law Dictionary* to conclude that the transaction was consummated at closing.²⁷⁸ Lastly, the court found that the purchase agreement confirmed that the sale occurred at this domestic closing because the agreement stated that the title to the shares did not transfer until closing.²⁷⁹ This decision suggests that Section 10(b) coverage may be available for transactions where the parties bought or sold securities in accordance with contractual language mandating that the closing occur in the United States and that the title transfer at closing.

Beyond this perception, *Quail Cruises Ship Management Ltd.* presents an interesting contradiction between the *Morrison* transactional test and the policy underlying *Morrison* against interfering with foreign securities regulation.²⁸⁰ The

²⁷⁷ *Id.* (emphasis in original).

²⁷⁸ *Id.* (citing BLACK’S LAW DICTIONARY 291 (9th ed. 2009)).

²⁷⁹ *Id.* This comports with the Second Circuit’s decision in *Absolute Activist Value Master Fund Ltd.*, which considered the location where the title transferred in determining if a domestic transaction under *Morrison* had occurred. 677 F.3d 60 (2d Cir. 2012).

²⁸⁰ *See Morrison v. Nat’l Austr. Bank Ltd.*, 130 S. Ct. 2869, 2886 (2010). The Court states that it developed a “clear test” to avoid the interference with foreign securities regulation that application of § 10(b) abroad would produce. *Id.* It seems counterintuitive then that a foreign-cubed case would satisfy the transactional test.

Eleventh Circuit focused on applying the *Morrison* transactional test as literally adopted.²⁸¹ The district court below, on the other hand, looked to *Morrison*'s policy rationale, determining that allowing the Section 10(b) claim in this setting would undermine congressional intent concerning the regulation of foreign transactions.²⁸² By creating a test that ignores U.S. conduct and the U.S. connections of the parties, *Morrison* laid the groundwork for essentially foreign claims such as this to proceed.

Nonetheless, the interpretation of “domestic transactions” that seems to best comport with *Morrison* and the Exchange Act is the irrevocable liability analysis. That analysis takes into account the statutory meaning of the words “purchase” and “sale” and does not revive aspects of the rejected conduct and effects test, as a focus on “solicitation” would. Though the facts needed to establish proof of irrevocable liability in a given situation frequently may not be clear, mutual

²⁸¹ See *Quail Cruises Ship Mgmt Ltd.*, 645 F.3d at 1310-11 (examining the transaction to determine if the transaction “occurred in the United States” as required under the *Morrison* transactional test).

²⁸² See *Quail Cruises Ship Mgmt Ltd. v. Agencia de Viagens CVC Tur Limitada*, 732 F. Supp. 2d 1345 (S.D. Fla. 2010) (stating that even if the transaction closed in the United States, the purchase or sale occurred abroad because, under *Morrison*, it is Congress’s intent, not the parties’ intent, that is “dispositive of the application of federal securities law to foreign securities transactions”).

acceptance of the agreement's terms and conditions in the United States should be important. As for whether parties can invoke U.S. federal securities law based on contractual language alone, it appears they cannot. They may, however, be able to opt into Section 10(b) coverage if contractual language provides that the closing and title transfer occur in the United States and the parties then perform accordingly. With that possibility looming, it seems that the transactional test may produce results that *Morrison* did not foresee.

The last section considers private right of actions after *Morrison* and whether the emerging globalization of securities markets calls for action by Congress.

C. The Ultimate Wave – Private Right of Actions After *Morrison*

In response to the study called for in the Dodd-Frank Act, parties ranging from foreign governments to pension funds to law professors have weighed in on whether Congress ought to reinstate some form of the conduct and effects test for private right of actions under Section 10(b).²⁸³ Most foreign governments argue

²⁸³ See, e.g., California State Teachers' Retirement System et al., Comment in Response to SEC Release No. 34-63174 (Feb. 18, 2011) (group of sixteen pension funds); Jonathan Taylor, Managing Dir. Fin. Servs. & Stability, U.K., Comment in Response to SEC Release No. 34-63174 (Feb. 11, 2011) (United Kingdom government); Robert P. Bartlett, III et al., Comment in Response to SEC Release No. 34-63174 (Feb. 18, 2011) (group of forty-two law professors).

that expanding *Morrison* would create conflicts with foreign law.²⁸⁴ For instance, unlike the United States, many European countries have not adopted or have limited class actions, have limited discovery, do not allow contingency fees, and require the loser to pay litigation costs.²⁸⁵ Rather, these countries have made deliberate decisions not to provide the same remedies as are available in the United States. Additionally, the United Kingdom, France, Germany, and Switzerland argue that expansion of *Morrison* is not necessary because each country has

²⁸⁴ See, e.g., Taylor, *supra* note 283, at 9 (United Kingdom); Klaus Botzet, Legal Advisor and Consul General, F.R.G., Comment in Response to SEC Release No. 34-63174, at 2-3 (Feb. 18, 2011) (Germany); Catherine Bergeal, La Directrice des Affaires Juridiques, Fr., Comment in Response to SEC Release No. 34-63174, at 2-3 (Feb. 17, 2011) (France). See generally Marc I. Steinberg, INTERNATIONAL SECURITIES LAW (1998).

²⁸⁵ See Taylor, *supra* note 283, at 2-3 (United Kingdom); Bergeal, *supra* note 284, at 4 (France). The comment by France even provided, “French courts would almost certainly refuse to enforce a court judgment in the U.S. ‘opt out’ class action because such a judgment violates French constitutional principles and public policy.” *Id.* at 7. For a detailed comparison of U.S. and foreign securities law, see the appendix of a comment by several European banking federations. Mouvement des Entreprises de France et al., Comment in Response to SEC Release No. 34-63174, app. (Feb. 18, 2011).

remedies available to U.S. investors who invest in foreign markets.²⁸⁶ Several of the governments emphasize cooperation between regulating authorities as an effective way to deal with transnational securities.²⁸⁷ Overall, foreign governments advocate that the Section 10(b) private right of action should remain limited by *Morrison*.

U.S. pension funds, on the other hand, advocate that Section 10(b) ought to extend to all purchases and sales of securities by financial institutions located in the United States and by individuals and entities who reside in the United States.²⁸⁸

²⁸⁶ Taylor, *supra* note 283, at 8-9 (United Kingdom); Bergeal, *supra* note 284, at 6-7 (France); Botzet, *supra* note 284, at 2-3 (Germany); Manuel Sager, Ambassador, Switz., Comment in Response to SEC Release No. 34-63174, at 2 (Feb. 22, 2011) (Switzerland).

²⁸⁷ See, e.g., Taylor, *supra* note 283, at 7 (United Kingdom); Bergeal, *supra* note 284, at 8 (France); Sager, *supra* note 286, at 3 (Switzerland).

²⁸⁸ See California State Teachers' Retirement System et al., *supra* note 283, at 1 (sixteen public pension funds from eleven different states managing \$732 billion); Ohio Public Employees Retirement System et al., Comment in Response to SEC Release No. 34-63174, at 1-2 (Feb. 18, 2011) (five Ohio public pension funds managing \$162 billion); Thomas P. DiNapoli, State Comptroller, N.Y., Comment in Response to SEC Release No. 34-63174, at 1 (Feb. 18, 2011) (trustee of the \$141 billion New York State Common Retirement Fund). Cf. Robbins Gellar Rudman & Dowd LLP, Comment in Response to SEC Release No. 34-63174, at 4 (Feb. 18, 2011) (institutional investors of foreign pension funds worth \$134 billion urging Congress to reinstate the conduct and effects test).

Five Ohio pension funds assert that U.S. and European Union brokers are required by legislation to execute purchases and sales on the exchange that, under the circumstances, most benefits the client.²⁸⁹ Investors therefore have no idea which exchange(s) their orders will be directed through.²⁹⁰ Additionally, many states mandate that state pension funds engage in prudent diversification.²⁹¹ For some funds, this requires the purchase of securities on foreign exchanges.²⁹² Several

²⁸⁹ Ohio Public Employees Retirement System et al., *supra* note 288, at 7.

²⁹⁰ *Id.* at 7. *See also* National Association of Shareholder and Consumer Attorneys, Comment in Response to SEC Release No. 34-63174, at 21 (Feb. 18, 2011) (noting that the exchange used is not often under the investor's control).

²⁹¹ *See* Ohio Public Employees Retirement System et al., *supra* note 288, at 7-8; DiNapoli, *supra* note 288, at 2. As of December 31, 2010, about 29% of the New York State Common Retirement Fund's public equities were international, with most of them purchased on foreign exchanges. *Id.* at 2.

²⁹² *See* Ohio Public Employees Retirement System et al., *supra* note 288, at 8 (stating that "an investor seeking to have automotive industry representation simply cannot avoid buying Toyota or Volkswagon and cannot buy energy without purchasing BP or Royal Dutch Shell"). As an example of the potentially negative effects of *Morrison*, the trustee for the New York State Common Retirement Fund notes that the fund purchased BP shares on a foreign exchange and, thus, may not be able to continue its role as lead plaintiff against BP concerning misrepresentations about the recent oil spill in the Gulf of Mexico. DiNapoli, *supra* note 288, at 2-3. The trustee points out that 40% of BP's assets and workers are in North America, that 40%

funds contend that a private right of action for U.S. investors, regardless of where the affected securities transaction(s) are consummated, is essential to effectuate the Exchange Act's primary purpose of protecting investors.²⁹³

A comment by a group of forty-two law professors also supports extending Section 929P of the Dodd-Frank Act to private plaintiffs.²⁹⁴ The professors argued that, with the fluid and international nature of modern financial markets, the place of a trade is becoming increasingly arbitrary.²⁹⁵ For instance, they predicted that the proposed merger of the Deutsche Borse and NYSE Euronext (which subsequently was scuttled) would result in offshore trades that, in the past, would have been executed in the United States.²⁹⁶ Rather than focus on where a trade

of its ordinary shares are owned by U.S. investors, and that BP has two wholly-owned U.S. subsidiaries. *Id.* For a further discussion of *Morrison*'s impact on institutional investors, see Ward & Barket, *supra* note 267.

²⁹³ See California State Teachers' Retirement System et al., *supra* note 283, at 7-8, 14; Ohio Public Employees Retirement System et al., *supra* note 288, at 3-5.

²⁹⁴ Bartlett, III et al., *supra* note 283, at 5.

²⁹⁵ *Id.* at 7.

²⁹⁶ *Id.* at 5-6. European officials have since blocked this deal, and the parent company of the NYSE has decided not to pursue the merger. See Jacob Bunge, *NYSE-Deutsche Börse Joins Dead-Deal List*, WALL ST. J., Feb. 2, 2012, at C2; Aaron Smith et al., *NYSE-Frankfurt Stock*

occurs, the group urged Congress to focus on where an investor is induced to trade.²⁹⁷ Additionally, when foreign issuers list their stock in the United States and voluntarily subject themselves to U.S. securities laws, as National Australia did in *Morrison* by offering ADRs on the NYSE, the group argued that concerns about international comity are minimized.²⁹⁸ Lastly, the professors pointed to the numerous dismissals of securities fraud cases since *Morrison* as evidence of its shortcomings.²⁹⁹ By comparison, they claimed that the conduct and effects test

Exchange Merger Blocked, CNN MONEY (Feb. 1, 2012),

money.cnn.com/2012/02/01/markets/nyse_uronext_deutsche_boerse/index.htm.

²⁹⁷ *Id.* at 7 (arguing that “[i]f a person in the U.S. is approached by brokers in the U.S. and is led to execute a trade on a foreign exchange, surely that trade is territorial, not extraterritorial”). In urging the Commission to reflect on the benefits of reinstating the conduct and effects test, the professors suggest that the Commission consider “analogies to Regulation S’s ‘directed selling efforts’” and “the extent of trading in categories of economically equivalent instruments,” such as ADRs and swaps backed by foreign shares. *Id.* at 8.

²⁹⁸ *Id.* at 8-10. The group of professors remarked that plaintiffs in *Morrison* did not emphasize these facts before the Supreme Court. *Id.* at 13.

²⁹⁹ *See id.* at 13-18 (describing twelve cases dismissed or pending a motion to dismiss since *Morrison*). Many of the professors were also persuaded by the scenario painted by Justice Stevens in *Morrison*, where a retiree, after being sold doomed securities in a door-to-door sale by an executive of a foreign-owned U.S. subsidiary, might be barred from bringing a Section 10(b) action. *Id.* at 6.

“captures the potential complexity of the relationships among investors and issuers.”³⁰⁰

The Commission issued its report based on the Dodd-Frank study in April 2012.³⁰¹ Rather than recommend a particular course of action, the Commission put forth several alternatives regarding private right of actions for Congressional consideration.³⁰² These alternatives ranged from extending the conduct and effects test that Congress granted the Commission and DOJ in the Dodd-Frank Act,³⁰³ to supplementing and clarifying the second prong of the Morrison transaction test,³⁰⁴

³⁰⁰ *Id.* at 11. Note that one of the authors of this article, Marc I. Steinberg, joined this comment letter.

³⁰¹ *See generally Study on the Cross-Border Scope of the Private Right of Action Under Section 10(b) of the Securities Exchange Act of 1934, supra* note 62.

³⁰² *Id.* at 58-59.

³⁰³ *See id.* at 60-64. The Commission offered variations on the conduct and effects test for private rights of actions, such as an additional requirement that “the plaintiff’s injury resulted *directly* from conduct within the United States” or that a U.S. investor brought the complaint. *Id.* at 60 (emphasis in original).

³⁰⁴ *See id.* at 64-69. Options presented for consideration included:

1. Permit Investors to Pursue a Section 10(b) Private Action for the Purchase or Sale of any Security that Is of the Same Class of Securities Registered in the United States, Irrespective of the Actual Location of the Transaction

...

to taking no action at all.³⁰⁵ Issuing a dissenting statement on the report, SEC Commissioner Luis Aguilar expressed his “strong disappointment,” citing the report’s lack of any specific recommendations and its failure to accurately portray the “immense and irreparable investor harm” resulting from *Morrison*.³⁰⁶

2. Authorize Section 10(b) Private Actions Against Securities Intermediaries that Engage in Securities Fraud While Purchasing or Selling Securities Overseas for U.S. Investors

...

3. Permit Investors to Pursue a Section 10(b) Private Action if They Can Demonstrate that They Were Induced While in the United States to Engage in the Transaction, Irrespective of Where the Actual Transaction Occurred

...

4. Clarify that an Off-Exchange Transaction Takes Place in the United States if Either Party Made the Offer to Sell or Purchase, or Accepted the Offer to Sell or Purchase, While in the United States

....

Id. at 64-68.

³⁰⁵ See *id.* at 57-58 (noting that this approach would leave interpretation of *Morrison* to the courts).

³⁰⁶ See Luis A. Aguilar, *Statement by Commissioner: Defrauded Investors Deserve Their Day in Court*, SECS. & EXCHANGE COMMISSION,

<http://www.sec.gov/news/speech/2012/spch041112laa.htm> (Apr. 11, 2012)

In the SEC comments submitted by the various parties, the main disagreement appears to concern whether Section 10(b) coverage ought to be available to U.S. investors who purchased or sold securities of foreign issuers. In that situation, the United States has an interest in protecting U.S. investors, while a foreign government has an interest in policing issuers within its country. The American Law Institute’s Restatement (Third) of Foreign Relations Law observes that, with the increasing globalization of securities markets, territorial factors may become less relevant. Conversely, the place of representations and negotiations,³⁰⁷ the nationality and residency of the parties,³⁰⁸ and the effect of the transaction or conduct on U.S. markets and investors³⁰⁹ become more important.³¹⁰ Clearly, the locale of a transaction will become increasingly irrelevant if international exchange mergers become widespread. If the Exchange Act is to adequately protect U.S. investors and markets in the future, non-territorial factors, such as those set forth in the Restatement, must play a pivotal role in determining the scope of the Section

³⁰⁷ American Law Institute, Restatement (Third) of Foreign Relations Law § 416(2)(b).

³⁰⁸ *Id.* § 416(2)(c). This factor may be particularly important when seeking to protect members of the United States armed forces stationed abroad. *Id.* rptr. n.2.

³⁰⁹ *See id.* § 416(2)(a) (considering “whether the transaction or conduct has, or can reasonably be expected to have, a substantial effect on a securities market in the United States for securities of the same issuer or on holdings in such securities by United States nationals or residents”).

³¹⁰ *Id.* § 416 cmt.a.

10(b) private right of action.³¹¹ For these reasons, Congress needs to reconsider the substantive scope of Section 10(b) as applied to transactions consummated abroad.

VI. Conclusion

Morrison has significant ramifications. Overall, the decision (1) altered the longstanding treatment of extraterritoriality as a jurisdictional issue; (2) rendered it more difficult to overcome the presumption against extraterritoriality under federal law; and (3) dramatically narrowed the scope of Section 10(b) with respect to transnational frauds. The first two changes primarily have affected federal law outside of U.S. securities law. Statutory requirements are being scrutinized after *Morrison* to ensure that they are not incorrectly characterized as jurisdictional issues. Additionally, *Morrison*'s strict approach to the presumption against extraterritoriality is driving discussions where a statute's extraterritorial reach is unsettled. It is the creation of the transactional test, however, that will have the most lasting reverberations on the legal tapestry.

³¹¹ Under the Restatement, it would be reasonable for the United States to exercise jurisdiction based on representations made in the United States and for the protection of a U.S. investor. *See* Restatement (Third) of Foreign Relations Law § 416(2)(b)-(c), cmt. a. This is not to say that the application of foreign law would be inappropriate. As in blue sky law, the transaction may have sufficient connection to both U.S. and foreign law to warrant application of either law. *See* Joseph C. Long, 12 BLUE SKY LAW § 4.1 (2010).

Both securities law and non-securities law have been impacted by the transactional test, but in very different ways. The focus in securities law will be gaining an understanding of what it means to have a “domestic transaction” under *Morrison*. This may entail development of the irrevocable liability analysis and possibly some incorporation of contract law concepts. On the whole, with respect to private rights of action, it can be said that the transactional test sets a much higher threshold for Section 10(b) claims than the now defunct conduct and effects test ever did.

As for non-securities law, *Morrison* can be expected to guide the important development of the secondary tests that instruct courts as to the proper application of a statute. RICO is likely the first of many statutes to be examined by courts in accordance with the process set forth in *Morrison*. That is, the process of first identifying the focus of a statute based on its statutory language and legislative history and then creating a minimum-U.S.-contact test in accordance with that focus, all the while being mindful of the presumption against extraterritoriality. With the globalization of finance and business markets, ascertaining the requisite U.S. nexus under an applicable statute will become increasingly critical in discerning the boundaries of U.S. law.

