International Securities Regulation—Absorption of the Shock

As with so many other facets of our economic and social life, the securities industry has undergone and continues to undergo its own form of "future shock." The internationalization of the world's securities markets is a phenomenon of the past 15 years. While rarely consistent, the dynamics of that movement have kept a pace with which not even the most modern and flexible laws and institutions could hope to cope effectively. Even the United States, with the most comprehensive regulatory scheme in the world, has been kept at bay in massive international securities frauds and at the same time criticized for an overzealous extra-territorial application of its laws. Other countries have adopted or strengthened securities laws and regulations, providing an unprecedented potential for uncertainty, conflict and inconsistency for those enterprises which would venture to tap the world's capital markets. Technological advances, primarily in transportation and communication, the growth of the multinational enterprise (MNE) and a number of related factors, such as the rapid internationalization of money and capital markets, have provided the environment for offshore securities frauds and have caused a myriad of complex neuroses. One such neurosis is that the world soon will be controlled by the MNEs. The rise of many developing nations and a concomitant surge of nationalism indicate that the MNE may not be entirely the master of its own or our destiny.¹

Regardless of the role of the MNE, each country and each person and enterprise are part of an international world where no one, including the United States, can revert successfully to an isolationist role. The book value of United States investment abroad is well in excess of one hundred billion dollars and foreign investment in the United States, attracted at least in part by the decreased international value of the dollar, has increased significantly in recent

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years. The answer to the breakdown of national boundaries does not rest with restrictive measures limiting the foreign ownership of local enterprise, such as have been adopted in many developing nations. Rather, the answer lies in increased communication, understanding and occupation in a number of areas which transcend national boundaries, such as antitrust, export and import controls, and securities regulation. With respect to securities, effective regulation is needed which can reach all transactions when participants are in need of protection, regardless of where the transaction occurs, yet which will be mindful of differences in attitude and approach in different countries which potentially render compliance by MNEs expensive, time-consuming and frustrating.

If this is the goal for international securities regulation, it makes little difference whether it is achieved through the immediate establishment of a supranational body or through accommodation and flexibility on a national level with respect to disclosure and reporting and a judicious extra-territorial application of national laws with respect to enforcement. Perhaps a beginning would be an international body composed of representatives from public and private institutions concerned with securities transactions and their regulation. While the ultimate goal of this body might be to develop a framework for the regulation of international transactions by qualifying MNEs, in effect preempting national regulation of these transactions, the more immediate and attainable goal should be the development of exemptions within national regulatory schemes for international transactions where the issuer is subject to "effective regulation" in its domicile. There is abundant precedent for such an approach, perhaps the most striking example being the "blue sky" laws of the various states. Almost all states exercise jurisdiction over an initial public offering within their borders, regardless of the domicile of the issuer. Once the securities of an issuer are listed on a major national securities exchange, however, most states exempt further offerings within their boundaries in reliance on the regulatory surveillance of the exchange and the SEC.

This article will summarize the status of securities regulation throughout the industrialized world and examine its application to transactions which cross national boundaries, and, with this foundation, will explore what has been and can be done to secure effective international regulation without impeding the free flow of capital.

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3Such measures are part of the Andean Investment Code and have been adopted in a number of other South American countries. Similar restrictive legislation has been before Congress. There is some question whether such restrictions could withstand constitutional attack in the United States. See Fenton, Proposed Limitations on Alien Purchases of United States Securities, 9 J. INT. LAW & ECON. 267 (1974).

4When securities are listed on an exchange, they must also be registered under Section 12(b) of the Securities Exchange Act of 1934, thereby subjecting the issuer to the periodic reporting, proxy solicitation and insider trading rules of this Act.
Securities Regulation in General

Despite the emergence of the institutional investor and its impact in the marketplace, the United States remains committed to a system of regulation where individuals can invest with some degree of protection against abusive practices. The primary ingredients of this system are (1) the comprehensive requirements for disclosure (a) when a firm makes an appeal to the public market for funds and (b) periodically thereafter in order to ensure an effective secondary trading market, and (2) the public and private remedies when inadequate disclosure attends a securities transaction.

In most other parts of the industrialized world, regulation of securities markets and firms issuing securities has developed on different premises. In Europe, the truly "public" company has been a rarity; capital markets have operated on a different basis, with banks (prohibited from engaging in the securities business in the United States by the Glass-Steagall Act\(^4\)) playing a predominant role in the purchase and distribution of securities; most securities are in bearer form so that ownership is difficult to trace; and an over-the-counter market, so well developed in the United States, does not exist. These are but a few of the many differences. Indeed, investing and trading in securities, particularly common stocks, have been regarded in Europe as an economic function of a tightly knit and restricted business community where those individuals who participate can make independent, informed judgments. The European traditions of family-controlled companies and "secrecy" have allowed, even required, that data be transmitted informally in a way not possible in the anonymity of the American economy. European businessmen have viewed "disclosure" as an unfair aid to their competitors. In fairness to this view, until a greater degree of uniformity in regulation is achieved in countries in close proximity to each other, firms in those countries will not be able to take comfort in the fact that their competitors are subject to the same or similar requirements.

While the differences in attitude and approach to securities regulation are thus natural and understandable, they tend to frustrate the hope for international accord leading to international regulation on anything other than a lowest common denominator basis. Nonetheless, the past ten years have witnessed vast increases in the scope and sophistication of securities laws in countries other than the United States. As this process continues, the differences in attitude and approach should dissipate. Those which remain as real will be crystalized and become proper subjects for international discourse.

Securities Regulation in the United States

The Basic Regulatory Scheme

The primary foundations of the federal securities laws are the Securities Act of 1933\(^{4}\) (the "1933 Act"), the Securities Exchange Act of 1934\(^{6}\) (the "1934 Act") and the Investment Company Act of 1940\(^{7}\) (the "1940 Act"). In brief, the 1933 Act requires disclosure in connection with the public offer and sale of securities and provides administrative and private remedies for failure to disclose and for material inaccuracies in disclosure; the 1934 Act regulates brokers and dealers, contains requirements with respect to periodic reporting, solicitation of proxies and insider trading, and provides for the now omnipresent private remedy of "10b-5" when "fraud" attends the purchase or sale of a security\(^{8}\); and the 1940 Act regulates certain operations of collective investment institutions, commonly known in the United States as mutual funds. The Securities and Exchange Commission ("SEC"), which administers all aspects of the federal securities laws, has embellished these statutes with regulations and other pronouncements which together form a regulatory framework well beyond that of any other country.

Extra-territorial Application of the United States Securities Laws

For the most part, the federal securities laws apply equally to foreign and domestic firms desiring to offer securities within the United States. For the non-United States firm, this has created many conflicts with laws and practices in its home country, particularly in the areas of accounting and financial reporting. In particular, it is usually burdensome for a foreign firm, once having sold its securities in the United States, to be required to comply to the same extent as domestic firms with the reporting, proxy solicitation and insider trading requirements of the 1934 Act. This burden on foreign firms unfamiliar with such regulation and the conflict with laws and mores of other countries led to an international outcry when the 1964 amendments to the 1934 Act rendered these requirements applicable to foreign issuers with a certain number of United States shareholders. International discourse and fact-gathering by the SEC led to the granting of exemptions which softened the impact on foreign firms and demonstrated that the SEC could accommodate its interest in protecting American investors and securities markets to the exigencies of international commerce. The final result was the adoption of Rule 3a12-3, which exempts the securities of foreign issuers from Sections 14 and 16 of the 1934 Act even though

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\(^{7}\) U.S.C.A., §§ 80a-1 to -52.

\(^{8}\) Section 10(b) of the 1934 Act and Rule 10b-5 promulgated thereunder.
the securities are registered under Section 12(g), provided that less than 50 percent of the voting stock of the issuer is held of record by United States residents. With respect to periodic reporting requirements, the SEC has required most foreign issuers to submit only that information which they must make public under the laws of their domicile or the regulations of stock exchanges on which their securities are listed. There are numerous other examples where the SEC, acting on ad hoc basis, has permitted foreign issuers desiring to offer securities in the United States to deviate from United States standards, particularly in the accounting area.9

There are also examples of accommodations of the federal securities laws with respect to domestic issuers offering securities outside the United States. Even with the repeal of the Interest Equalization Tax, the SEC has allowed United States issuers (other than mutual funds) to make foreign offerings without registration where reasonable steps were taken to ensure that the securities would not be sold to citizens or residents of the United States and would come to rest outside the United States. To assist domestic companies in complying with Japanese requirements, the SEC adopted Rule 434C under the 1933 Act. Japanese regulation requires some additional information in the prospectus and a different format of presentation than is required by the 1933 Act, and Rule 434C permits the use of a prospectus for the Japanese market so long as it is not provided to United States nationals or residents.

Requirements as to disclosure which constitute a condition precedent to offering securities in a given jurisdiction and continuing regulation thereafter are certainly the topics of critical concern to MNEs and all others who participate in the world's capital markets. Nonetheless, most of the focus of scholars has been on the extension to international settings of the private remedy afforded by Rule 10b-5.10 While the 1934 Act and the SEC have provided no parameters for the transnational reach of Rule 10b-5, the courts have clarified the essential elements to jurisdiction and for the most part have done so without offending the sense of justice in other interested countries. When a security traded on a United States exchange is involved in a "fraud-

9For a number of such cases, see INTERNATIONAL SECURITIES REGULATION 1975, Practicing Law Institute, pages 200-213.

10A discussion of cases involving the extra-territorial reach of 10b-5 and the various bases in international law for asserting extra-territorial jurisdiction is beyond the scope of this article. These subjects have been examined in a number of recent articles, including Comment, The Transnational Reach of Rule 10b-5, 121 UNIV. PA. LAW REV. 1363 (1973); Comment, Extra-territorial Application of the Securities Acts, 1974 WASH. UNIV. LAW Q. 859; Mizrack, Recent Developments in the Extra-territorial Application of Section 10(b) of the Securities and Exchange Act of 1934, 30 BUS. LAW. 367 (1975). Some of the leading cases discussed in these articles are Schoenbaum v. Firstbrook, 405 F.2d 200 (2d Cir. 1968), Leasco Data Processing Equip. Corp. v. Maxwell, 468 F.2d 1326 (2d Cir. 1972), Travis v. Anthes Imperial Ltd., 473 F.2d 515 (6th Cir. 1973), Scherck v. Alberto-Culver Co., 417 U.S. 506 (1974), Borsch v. Drexel Firestone, Inc., 519 F.2d 974 (1975), and ITT v. Vencap, Ltd., and Blackman, 519 F.2d 1001 (1975).
ulent” transaction and there is an adverse effect on a United States interest, there probably will be jurisdiction based on the Schoenbaum case even though the actionable conduct occurred entirely outside the United States.\textsuperscript{11} If there is substantial conduct within the United States forming an “essential link” with a total scheme to defraud, together with a harmful effect on a United States interest, there will be jurisdiction under Leasco\textsuperscript{12} and cases following, even if listing on a United States exchange is absent. Standards such as these, while by no means precise, should not provide a stumbling block to the vast majority of MNEs, especially in the light of the United States Supreme Court’s decision in Scherk\textsuperscript{13}, which recognizes that arbitration and venue selection bring orderliness and predictability to international transactions and avoid conflict of laws problems when courts of several countries might otherwise attempt to exercise jurisdiction over such transactions.\textsuperscript{14}

Certainly enforcement and private remedies are important in a discussion of international securities regulation. On the other hand, the cases which have been decided and have received such notoriety in the past several years highlight securities frauds; these, however, comprise but a small segment of international securities transactions. There is little question that MNEs have learned that remedies exist for inadequate disclosure in the sale of securities. What is needed, however, is a means for MNEs to tap the capital markets of more than one country without being subjected to conflicting and burdensome regulation, resulting in delays and exorbitant costs which are paid for in the long run by the MNE’s shareholders.

\textit{Accommodation of United States Securities Laws to Transactions with Foreign Elements}

It is unlikely that meaningful international securities regulation administered by a central body and subscribed to by a majority of nations will be achieved in the 1970s. Nonetheless, this is a logical if not mandatory outgrowth of the direction currently being taken by the world’s capital markets and their participants. The questions are the traditional ones of when, how and on what basis. In the interim, and as an important part of the road toward uniformity and centralization, there must be some reasonable accommodation of domestic securities laws when they conflict with legitimate laws and practices of other countries and when rigid application is not necessary for the protection of legitimate domestic interests.

\textsuperscript{11}Schoenbaum v. Firstbrook, \textit{supra} note 10.
\textsuperscript{12}Leasco Data Processing Equip. Corp. v. Maxwell, \textit{supra} note 10.
\textsuperscript{13}Scherk v. Alberto Culver Co., \textit{supra} note 10.
\textsuperscript{14}See Bremen v. Zapata Off-Shore Co., 407 U.S. 1 (1971), holding that forum selection clauses in international contracts are prima facie valid.

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Domestic laws have had little opportunity to catch up with the rapid internationalization of securities transactions and the world securities markets. They thus remain concerned primarily with domestic markets and the parochial interests of local citizens and residents. The words of the Supreme Court in *Bremen v. Zapata* apply not only to the United States but to each country which would participate in the modern world economy:

The expansion of American business and industry will hardly be encouraged if, notwithstanding solemn contracts, we insist on a parochial concept that all disputes must be resolved under our laws and in our courts. . . . We cannot have trade and commerce in world markets and international waters exclusively on our terms, governed by our laws, and resolved in our courts.\(^{15}\)

The 1933 and 1934 Acts do not differentiate between foreign and domestic private issuers and accountants, yet insistence on strict compliance with United States laws and regulations would effectively deny many foreign issuers access to United States capital markets. Despite the spread of major United States based auditing firms as the MNEs of the accounting profession, there remains much lack of uniformity in different countries on accounting principles and procedures and financial statement presentation and disclosure. A full discussion of accounting differences is beyond the scope of this article but brief reference to the nature of these differences may bring some appreciation of the task which lies ahead. In some industrialized countries, consolidated financial statements are not the accepted method of financial reporting; inventory is carried at replacement or current value and arbitrary write-downs are permitted (note that the recent change in the United States to the use of LIFO in valuing inventory is a step toward replacement value accounting); depreciation is continued even after the asset has been fully depreciated for book purposes so long as it is still usable; fixed assets can be written up to current values, often on the basis of a coefficient established by the home government; contingency reserves unknown in the United States are allowed or required; and confirmation of accounts receivable and observation of physical inventories are not normal auditing procedures. Independence of accountants, a highly sensitive issue in the United States, can be a problem for companies in some foreign countries where accountants are expected to own shares of their clients' stock.

Several examples of flexibility by the SEC in the application of the federal securities laws have been cited above. The United States has not always been so successful, however. Rights offerings to existing shareholders must be registered under the 1933 Act but are subject to little or no regulation in most countries. There have been numerous rights offerings by United Kingdom companies, notably the Rank Organization, where the companies refused to cope with the time-consuming and costly registration process and restricted the

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\(^{15}\)Id. at 8-9.
offerings to shareholders not resident in North America. The result was not protection of United States shareholders, but rather financial loss to those shareholders, because they could not participate in a favorable offering.

Despite statutory authorization permitting foreign investment companies to register under the 1940 Act, only a few have registered. In fact, the SEC has registered foreign investment companies only if it considered that the 1940 Act could be enforced against the foreign company both from a legal and practical point of view. In this regard, the SEC has not shown any propensity to follow the German example of adopting a set of standards to govern foreign investment companies more lenient than those with which domestic companies must comply. The obvious fear of such a dual standard is that domestic companies will reincorporate in a country where investment companies are subject to little or no regulation in an effort to take advantage of the more lenient standards applicable to foreign companies.

Indeed, the answer is not a dual standard system; rather, pending true international regulation, each situation can be examined on an ad hoc basis to determine whether certain aspects of the United States securities laws and regulations should be accommodated to legitimate conflicts affecting the foreign issuer. Major considerations in analyzing each case should be the scope and degree of regulation in the issuer's home country as well as the true ownership and locus of control of the issuer. If a foreign issuer is domiciled in a country with no effective regulation, then there would be no legitimate conflict among national laws, and countries in which the securities of such a foreign issuer are sold should exercise the control and regulation lacking in the issuer's home country. In such a case, uniformity and harmonization may be less important than some form of effective regulation. While the possibility exists that a foreign issuer will thus be subjected to different regulations in different countries where it desires to offer its securities, these are conflicts which can be resolved only as we approach a structure for supranational regulation.

The enforcement of public and private remedies does not present the same potential for conflict as do disclosure and reporting requirements. While unharnessed extra-territorial application of those remedies is certain to create international ill will, the availability of a meaningful remedy to an injured investor who otherwise may have no opportunity for redress is critical to the maintenance of an orderly securities market and investor confidence and is unlikely to offend international comity. In deciding whether to give extra-territorial application to Rule 10b-5 and other remedies available under the United States securities laws, the courts have considered a number of factors in addition to the underlying purposes of the United States securities laws, the most important of which are the impact of the transaction on United States and

foreign securities markets, the legitimate expectations of the parties and the need for certainty and predictability in business transactions, the nature and extent of domestic conduct and effect, and the relevant policies of other interested countries and the relative interests of those countries in the determination of the particular issue. The last factor, of course, is of utmost importance when there is another interested jurisdiction, i.e., one in which some significant part of the transaction occurred, where a market for the securities is located, or where the issuer or some party to the transaction is domiciled.

It is doubtful that many have been offended by the extra-territorial application of remedies under the United States securities laws in situations where the United States was an interested jurisdiction and where there was not a bargained-for arbitration or choice of law clause. Certainly MNEs based in other countries have not been affected significantly. Although Rule 10b-5 differs from the concepts of fraud in most other countries in that the standards of conduct are higher and the requirements of proof somewhat easier under 10b-5, the differences probably are not so substantial that the application of Rule 10b-5 in most international securities transactions would offend or conflict with foreign policies and laws. Nonetheless, there may be instances where the existence of remedies under the laws of interested foreign countries would support a United States court's deferral to a proceeding brought in a court of that foreign country. The goals of sound transnational securities markets and harmonious international relations require that United States courts not be overzealous in extending the protection of United States laws to cases in which some meaningful protection is available under applicable foreign law nor reticent in extending the protection of United States laws to cases in which no adequate alternative protection or remedy exists. The collapse of the IOS companies illustrates the harms which can occur when the SEC and United States courts refuse to fill a regulatory vacuum that works to the detriment of foreign investors.

While remedies for fraud are universally recognized, the United States securities laws provide at least one remedy which is neither recognized nor understood in most countries. Section 16(b) of the 1934 Act, which authorizes recovery by a corporation of any profit made by an insider on the purchase and sale of shares within six months, is based on absolute liability. Such a remedy should be applied cautiously, if at all, in international settings and should not

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1 Many of these considerations are not dissimilar to those outlined in the Restatement (Second) Conflicts, § 6(3).

14 See Wagmein v. Astle, CCH Fed. Sec. L. Rep., ¶ 94,783 (S.D.N.Y. 1974) (no recovery under 16(b)); but see, Roth v. Fund of Funds, Ltd., 405 F.2d 421 (2d Cir. 1968) (recovery allowed under 16(b)). Article 82 of the Statute on European Stock Companies, proposed by the EEC Commission in 1970, is similar to Sections 16(a) and (b) of the 1934 Act. Also, in 1970 the German Commission
burden international discourse and efforts at harmonization on other issues which are far more relevant to the effort of fostering international securities transactions while preserving the integrity of domestic regulation.

The real effort at harmonization is needed less in the area of enforcement than in disclosure and other requirements that are conditions precedent to entering or remaining in a given domestic capital market. Yet even Tentative Draft No. 3 of the Federal Securities Code\(^9\) fails to address the real issue. Section 1604, entitled "Relation to Other Countries," provides that the code applies to sales, purchases, offers, inducements, proxy solicitations or tender offers occurring within the United States although initiated outside that country; simply an attempt at statutory formulation of one of the rules of international law with respect to the extra-territorial application of domestic law. The emphasis appears to be a codification of some of the elements of the Leasco and Schoenbaum cases; again, these are remedies rather than requirements for entry. The draft gives some hint on the latter point by providing that the code does not apply to sales or offers initiated in the United States but directed abroad. Left unanswered is the situation of the MNE desiring to raise capital in several foreign capital markets; it is relieved from regulation at home but potentially is subject to conflicting and duplicative regulation in those countries where its securities are offered.

Securities Regulation Outside the United States

As noted at the outset, the capital markets and their participants in most parts of the world are different from the United States situation. The rapid internationalization of these markets has tended to narrow the gap, but new markets are continually emerging and important differences remain. These must be understood and reconciled if international securities regulation is to proceed on a basis which will satisfy the needs of MNEs and the world business community.

In general, securities regulation in Europe and other industrialized countries is much less developed than in the United States, primarily because it has responded to capital markets with a different structure and different participants. Offerings in Europe of equity securities in what would be a public distribution by United States standards have never been and are not now common. Aside from the great difference between "private" offerings in Europe and the United States, little additional access to the public in Europe would be gained through the true "public" offering. Domestic exchange control restric-
tions often inhibit the purchase by individuals of foreign securities. For instance, British residents cannot acquire non-sterling securities without Bank of England approval and payment of the foreign currency investment premium, twenty-five percent of which must be forfeited on resale. As a result, purchasers in England usually are institutions which are exempt from the exchange control restrictions and which may invest on behalf of non-residents and holders of discretionary accounts. Furthermore, the prospectus requirements of the Companies Act 1948 do not apply to an offer to any person whose ordinary business is to buy or sell shares, whether as principal or agent: an additional incentive to offer only to institutions. From the United States point of view, the most vivid examples of the liberal private placement doctrines extant in most of Europe have been the Eurobond and Eurocurrency offerings in recent years. These offerings were certainly public by United States standards, but were made by underwriters and dealers so as to comply with local private placement standards in Europe.

We cannot hope for meaningful international securities regulation unless those who would develop such regulation have a complete understanding and appreciation of the regulatory differences, large and small, in the participating nations. A detailed survey of the status of securities regulation throughout the world is well beyond the scope of this article, but a few examples are necessary to place in perspective the broader issues of how and on what basis to achieve international regulation.¹⁰

Some forms of securities regulation have existed for some time in several European countries. Unlike the United States, however, there are usually not separate securities laws. Prospectus requirements may be found in a companies act or commercial code and remedies for fraud or deception are almost certain to be found in the basic civil code. These requirements and remedies have not developed to the same extent as in the United States for the simple reason that there has been no need. Europeans have never traded in securities to any appreciable degree and local business enterprises either did not require large amounts of capital or obtained it through normal bank loans. The emergence of MNEs and international capital markets, however, has disrupted these traditional structures, with the result that securities regulation outside the United States has developed significantly in the past ten years.

Securities regulation in France really began in 1966 and the Commission des Opérations de Bourse, which administers the French securities laws and supervises the French stock exchanges, was created only in 1967. French regulation

¹⁰For a detailed analysis of securities regulation in several countries, see International Securities Project, 30 Bus. Law 585 (1975). For a concise tabulation of the reporting, disclosure, insider trading and proxy regulations of the major European exchanges, see INTERNATIONAL SECURITIES REGULATION 1975, Practicing Law Institute, pages 160-165.
nonetheless remains quite different from that in the United States, in large part due to the practice and consensus of the French financial community. Witness the distinction between public and private offerings: public offering in France involves "public appeals for savings," a concept without further definition. The verbally expressed position of the Ministry of Economy and Finance is that, if no public advertisement appears prior to completion of the distribution, French banks may be solicited as underwriters or selected dealers and they may in turn place foreign securities abroad, in discretionary accounts or to fill unsolicited orders. Secondary offerings are not regulated unless a listing of the securities is involved, and rights offerings to shareholders in France are not deemed to involve a public offering and accordingly no approval is required. As a guard against potential misuse of inside information with most shares in bearer form, insiders or listed companies now must put their shares in registered form or deposit them with a bank.

Most significant to securities regulation in the United Kingdom are the extra-legal requirements of The London Stock Exchange and The City Code on Take-Overs and Mergers. Probably no other stock exchange outside the United States has such comprehensive requirements, and the "tender offer" regulations are among the most sophisticated in the world. On the other hand, there is little in the way of statutory securities regulation. Inasmuch as there is no over-the-counter market in the United Kingdom, however, a company desiring a public market for its shares of necessity will be involved in a listing on The Stock Exchange and thus will become subject to its rules. Among other requirements, The Stock Exchange approves all proposed materials to be sent to shareholders, the United Kingdom thus being one of the few countries with anything resembling the proxy rules promulgated under the 1934 Act.

There is no central body in the Federal Republic of Germany which has primary jurisdiction over the interpretation and enforcement of the various provisions of West German law which deal with securities, and with the exception of mutual funds, West Germany has no comprehensive statute which regulates the distribution of securities. A prospectus is required only in connection with the sale of mutual fund shares or the listing of securities, and even if the listing follows a public distribution of shares in Germany, the offering generally will be completed before the listing prospectus is required to be prepared. Civil liabilities are at the early stages of development, mergers and tender offers are subject to little regulation, and reporting and disclosure requirements are at a minimum level. On the other hand, there is a provision similar to Section 13(d) of the 1934 Act which requires notification to a company when a business enterprise acquires more than 25 percent of its capital stock. Until the notice is given, the rights to vote and receive dividends are suspended.
With respect to mutual funds, West Germany does have a comprehensive statute which regulates funds established in West Germany. In regulating foreign mutual funds, however, West Germany rejected its own 1957 statute, because its supervisory authority could not conduct the same examination of quality to which the management and operations of domestic funds were subjected and because adherence to its domestic statute might be burdensome or impossible if it conflicted with the laws of the fund's home country. Thus, while domestic funds are subject to a regulatory law in the true sense of the word, foreign funds are governed by a statute which more closely resembles a disclosure law.

Unlike the European countries, Japan does have a separate securities law. In fact, regulation in Japan is modeled after that in the United States, and the fundamental law, the Securities Exchange Law of 1948, is patterned on the 1933 Act and the 1934 Act and regulates both the issuing and trading markets. The Ministry of Finance has broad rule-making powers for the implementation of the securities regulation policy, but little judicial interpretation exists due to the Japanese reluctance to engage in litigation. In 1970, the internationalization of the previously insulated Japanese securities market began, and the principal recent developments in securities regulation have related to permitting issuances of securities in Japan by foreign issuers and the listing of such securities on the Tokyo Stock Exchange. The similarities of regulation in Japan and the United States should provide a strong base for accommodation and the elimination of conflicting or duplicative requirements.

The need to accommodate domestic regulation to transactions with foreign elements increases in direct proportion to the scope and extent of the domestic regulation itself. The greater the regulation, the greater the potential for conflict with laws and practices in a foreign issuer's home country. Companies based in the United States have proved that they can tap European capital markets with a minimum of regulation due to liberal private placement doctrines and the operation of those markets themselves which renders it unnecessary for the offer to be made directly to the "public." The same is not true for companies based in Europe which would raise capital in the United States. Thus, the burden of accommodation in a real sense rests with the SEC. Nonetheless, the United States is not alone in the necessity to accommodate domestic laws to foreign companies subject to conflicting regulation at home. Possibly the most interesting example is presented by the West German statute governing foreign investment companies. In general, this is significantly weaker in regulatory impact than either the West German statute governing domestic

investment companies or the 1940 Act. Nonetheless, the West German statute carries over the strong policy which exists in several European countries that expert fiduciaries are better able to protect investors than investors themselves, a basic difference from the attitude and regulatory approach in the United States. The statute thus contains certain provisions with respect to the powers and duties of custodian banks which are not found in the 1940 Act and which are not customary practices of United States based mutual funds and investment companies. Nonetheless, West Germany has waived compliance with these provisions in recognition that the security for investors which it finds in the powers and duties of custodian banks can be supplied by the alternative means of the total regulatory structure provided by the 1940 Act with respect to registered investment companies.

In late 1973, the Tokyo Stock Exchange decided to permit the listing and trading of certain foreign securities. Standards for listing were designed to insure that only foreign-based MNEs and major "blue chip" corporations could be listed and traded. At approximately the same time, two regulations on requirements for financial statements of foreign companies were amended. The first allows foreign companies to prepare financial statements for use in Japan on the basis of the standards in their home country unless the Ministry of Finance finds such standards to be inadequate. The second amendment allows foreign companies to report on a consolidated or separate company basis depending on how they regularly report their operations and those of their subsidiaries in their home country. These are important examples of accommodation leading to a freer flow of capital without forsaking domestic regulation.

Areas of International Cooperation

Cooperation on an international level in securities regulation and enforcement is an essential adjunct to national restraint and accommodation and will be an additional catalyst to the eventual development of some form of supranational regulation. Even with respect to enforcement of private remedies, the judicial mechanism, whether in the United States or elsewhere, is not capable of developing national securities policy or balancing the competing policies and interests of different nations. Meaningful international study, discourse and cooperation should not only harmonize standards that are in direct conflict but also eliminate those which are ineffectual or unnecessary. It is important to focus attention on the real differences of opinion as to the efficacy of alternative methods of securities regulation and enforcement, and to do so on an empirical rather than an intuitive basis.

Indeed, there is precedent for this form of international cooperation. The United Nations Convention on the Recognition and Enforcement of Foreign
Arbitral Awards is adhered to not only by almost all countries of the Western industrialized world but also by most of the Eastern European countries. Officials of the antitrust agencies of almost all European countries, Canada, Japan and the United States utilize the Business Practices Committee in the OECD as a focal point for periodic meetings and exchange of views.

There has been progress as well in some areas of securities regulation. The SEC has established an Office of International Corporate Finance, the duties of which include supervising offerings of United States securities abroad and offerings of foreign securities in the United States, and resolving the problems which arise from the need to meet the accounting and disclosure requirements of more than one nation. Efforts are being made to standardize the regulation of stock exchanges, and the EEC is attempting harmonization among the Common Market countries in a number of areas related to securities regulation. With respect to the difficult area of accounting principles and standards, in 1973 the International Accounting Standards Committee was formed by 31 professional accounting bodies from 22 countries. The task of this committee is to formulate and publish basic standards and to promote worldwide acceptance of those standards. International Accounting Standard No. 1 was issued in January 1975 on the disclosure of accounting policies. Other standards have been issued as exposure drafts or are on the agenda for future consideration, including valuation of inventories, consolidation of financial statements, and equity accounting, depreciation, and inflation accounting.

In the area of enforcement of securities laws, the best example of international cooperation involves the myriad of Vesco-controlled corporations and offshore funds. Significantly, in granting a preliminary injunction requested by the SEC, the district court judge noted that related proceedings were being carried on in several foreign countries and emphasized the importance of working in harmony with the governmental authorities of those countries. Most of the corporate defendants were domiciled in Canada, Luxembourg, the Bahamas and the Netherlands Antilles. In mid-1973 there was a meeting in Luxembourg attended by representatives of the SEC, the Luxembourg regulatory authorities, the Canadian federal government, and the Quebec and Ontario Securities Commissions. The decision was made to seek the liquidation of the IOS entities under the supervision of the domiciliary governments. What emerged was real coordination of effort among the SEC, the United States receivers, foreign governments and foreign liquidators. There have been quarterly meetings among all receivers and liquidators, and the courts and regulatory officials of the countries concerned have for the most part cooperated in

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22 International Controls Corp. v. Vesco, 490 F.2d 1334 (2d Cir. 1974), cert. denied 41 L.Ed.2d 236 (1974); see also Hutchison, Vesco, Praeger Publishers, Inc. (New York 1974).
ceding jurisdiction and responsibility in a way to avoid conflict and duplication. The lesson of Vesco is a persuasive argument for the creation of some form of international securities commission to coordinate and supplement the efforts of national regulatory agencies and courts in cases which involve several countries. The existence of such a commission would enable interested countries to coordinate their efforts quickly when speed is critical to preserve remaining liquid assets.

The examples of cooperation cited above, while not to be belittled, fall far short of the mark. To be realistic, however, modern history is replete with failures of attempts at international regulation and agreement. Since World War II, there have been any number of public and private attempts to establish multinational conventions for the safeguarding of private foreign investments, most of which aborted because of the divergent underlying interests of the investing and receiving countries. Proposals for a supranational authority to administer an international companies law are not news, but again little has been accomplished and recent nationalistic trends in the developing countries have a twofold effect: they render the task of structuring an international companies law even more difficult if not impossible, and they erode the so-called dominant position of the MNEs which prompted many of the suggestions for a supranational authority. As a result, MNEs now find themselves subject to a myriad of restrictions in such countries, such as exchange controls on dividend and royalty remittances, imposition of new and higher taxes on earnings, and restrictions on the percentage of foreign ownership of local companies. The difficulty of structuring an effective international companies law perhaps is most vividly demonstrated by the experience of the EEC in its attempts to formulate a company law for the members of the Community. The concept was first proposed in 1960 and, although a draft statute has been prepared, agreement has not been reached and the EEC now faces the task of integrating British institutions and common law traditions within the framework of civil law institutions and practices.

Certainly the development of an international companies law for the regulation of MNEs is more difficult than the structuring of some form of international securities regulation. Nonetheless, proposals for international cooperation or regulation of a more limited scope than companies law have met with considerable difficulty. Two examples are the attempts at harmonization of standards, inspections and certifications with respect to the importation of products and the International Center for the Settlement of Investment Dis-

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24Witness the ill-fated 1948 Havana Charter of the International Trade Organization.
putes, neither of which has been particularly successful. Nor have attempts been much more successful in the securities field. The OECD Standard Rules with respect to investment companies, although substantially adopted in Japan, are the product of disagreement and compromise among the 23 member nations. This inability to agree is the product of divergent attitudes toward the regulatory role itself and a design of each member's representatives that their own country's current regulatory scheme be able to meet the OECD Standard Rules with minimal strain. Thus the forces of negotiation and compromise molded the Standard Rules into a framework which is based upon the lowest common denominator of acceptable regulation and falls far short of providing comprehensive regulation of investment companies.

The Future—Can It Absorb the Shock?

The design of a supranational structure for international securities regulation is indeed a prodigious task. As noted earlier, at least until recently public shareholders and active trading have been minor factors in the European securities markets. There has thus been little pressure for public disclosure and other developments which have occurred in the United States. To some extent, the MNE caused the break-up of the traditional European family corporation and increased the need to raise substantial amounts of equity to grow and compete effectively. The experience of the United States and the United Kingdom in creating investor confidence and attracting savings has persuaded many foreign bankers and enterprises that disclosure and protection of investors are necessary to the successful tapping of public funds. Nonetheless, most securities markets and thus most systems of securities regulation continue to have basic differences from those in the United States. Moreover, even in the United States there is no consensus on all points. To the contrary, there is continuous re-examination and change; witness the substantial amendments to the 1934 Act in 1964, the "Wheat Report" and consequent changes, and the 1970 amendments to the 1940 Act. With the increase in the number of MNEs and the emergence of potential new capital markets, new systems of regulation are under study almost everywhere and there are likely to be a myriad of viewpoints and proposed solutions. It would seem critical to establish some form of international forum for disclosure before systems and viewpoints become cast in the proverbial concrete. It is also important not to lose sight of the fact that a supranational regulatory scheme, at least at the outset, need cover only a small portion of what is encompassed by total domestic regulation.

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As usual, it is easier to agree on what should not be done, i.e., no country should attempt, through unharnessed extra-territorial application of its own laws, to impose a supranational regulatory structure on others, and it would be equally wrong to regulate internationally on a lowest common denominator basis. Similarly, it would be shortsighted to assume that the problem is only for non-United States MNEs on the basis that United States MNEs are subject to such a comprehensive regulatory scheme that they should be able to comply elsewhere and, in any event, heretofore have been able to tap most foreign capital markets by taking advantage of liberal private placement doctrines. First, the past ten years have witnessed a tremendous growth in economic interdependence, and the next ten years are likely to see the trend continue, possibly with a multiplier effect. Therefore, it is important that non-United States based MNEs be able to tap United States capital markets if this is necessary for them to remain viable participants in a world economy where failure of any major segment cannot help but impact the whole. Second, if the United States restricts access to its capital markets, it is not unlikely that other nations will take steps to control access by foreign-based MNEs. European investors cannot have forgotten the losses they sustained in convertible Eurobond offerings by United States based MNEs and their Netherlands Antilles subsidiaries in the late 1960s and early 1970s. In many cases, these securities have been repurchased by the United States company for less than 50 percent of face amount.

Possibly the most important economic force over the next ten years will be the result of MNEs and other companies increasing business activities with developing nations in the Middle East, Africa and South America. Here the problem is twofold—nationalism is high and securities regulation is embryonic. Companies are thus faced with requirements that their subsidiaries have a local majority and be financed locally, possibly through a stock issue rather than bank loans. Unless some form of international cooperation is obtained, the potential for conflicting and burdensome regulations is even greater than it has been in recent years.

As noted earlier, there have been many examples of effective accommodation and of international cooperation and efforts at harmonization of conflicting laws and regulations. But aside from being inadequate to what is needed, these efforts have been disjointed and could profitably be brought together in a forum which would be designed to assemble securities scholars and experts from around the world to discuss ideas and issues on a noncrisis basis. Especially with the emergence of developing nations and thus new capital markets, an understanding of the workings of the various market systems and an appreciation of the real problems in securities regulation are essential. Efforts thus could be directed at those problems rather than being diverted to issues (such as a 16(b) type absolute liability) where there may be great disagreement among nations but where there is little impact on international securities transactions.
Perhaps many countries could agree to the formation of an international securities commission with a limited charter at first but the ability to expand that charter through common accord as mutual understanding and respect increased. Such a charter might include:

1. The forum, mentioned above, for international study and discourse and coordination of the presently diffused efforts at cooperation and accommodation.

2. Coordination of enforcement efforts when international securities frauds are uncovered and speed is necessary to find and preserve remaining liquid assets. This aspect could be particularly important in view of the difficulty, often encountered, of the courts of one country obtaining personal jurisdiction over potential defendants.

3. Examination of ways in which domestic regulation can be accommodated to foreign issuers which are subject to meaningful regulation at home. The problem, of course, is what constitutes "meaningful regulation." The SEC is unlikely to relinquish jurisdiction when a non-United States issuer enters the United States capital market in a manner which results in a significant number of United States shareholders. Nonetheless, United States mutual funds can sell securities in West Germany even though United States regulations do not impose the duties on custodians which are imposed under West German law. The SEC, possibly through an international securities commission, should begin to examine modes of regulation outside the United States which are sufficiently acceptable to warrant exemption from United States requirements. For instance, any company with securities listed on The Stock Exchange in London might qualify for such an exemption so long as the company complied with all requirements of the Exchange vis-à-vis its United States shareholders.

The long-term goal of such a commission should be the development of a registration process for MNEs of sufficient size and with a proven earnings history which desire to offer their securities. In the United States, there is some precedent in the tests of eligibility for use of the simplified Form S-7 in lieu of the more burdensome S-1. Perforce there will be difficulty in establishing the tests of eligibility, the registration requirements and the degree of preemption over national laws, particularly in the areas of enforcement and private remedies. But one must begin somewhere, and the establishment of an international commission with a limited charter seems a reasonable first step likely to attract enough participants to be an effective forum and eventually to provide the foundation for true supranational regulation.