II. EXTRATERRITORIAL APPLICATION OF THE SECURITIES ACTS

In the traditional view of jurisdiction, both in American[243] and international law,[244] a nation's regulatory laws are enforceable only if the constituent elements of the violation occurred within the regulating nation's territory.[245] This view has been liberalized to permit extraterritorial application of regulatory laws in appropriate cases.[246] American courts generally follow the *Restatement (Second) of Foreign Relations Law of the United States* and accept subject matter jurisdiction either if there is illegal conduct within the territory of the United States, even if the harmful effects of the conduct occur outside that territory,[247] or if illegal conduct occurs outside United States territory, but causes substantial harmful effects that are direct and foreseeable within the United States.[248] The *Restatement* also permits jurisdic-

243. *See* Blackmeer v. United States, 284 U.S. 421, 437 (1932); American Banana Co. v. United Fruit Co., 213 U.S. 347 (1909).

244. *See generally* Note, *Limitations on the Federal Judicial Power to Compel Acts Violating Foreign Law*, 63 COLUM. L. REV. 1441, 1473-85 (1963).

245. This view was also reflected in the field of conflicts of law during the reign of the first *Restatement of Conflict of Laws* (1934) "vested rights" doctrine. It was considered that a state's laws could not be applied to a wrong whose critical element occurred in another state. *See generally* Trautman, *The Role of Conflicts Thinking in Defining the International Reach of American Regulatory Legislation,* 22 OHIO ST. L.J. 586 (1961).

246. *See* Case of the S.S. "Lotus," [1927] P.C.I.J., ser. A, No. 9. *See also* Note, *supra* note 244, at 1473-85. This trend parallels the current trend toward "interest analysis" in conflicts thinking. *See generally* Reese, *Choice of Law: Rules or Approach,* 57 CORNELL L. REV. 315 (1972); Sedler, *The Contracts Provisions of the Restatement (Second): An Analysis and a Critique,* 72 COLUM. L. REV. 279 (1972).

247. RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 17 (1965) [hereinafter cited as RESTATEMENT (SECOND) OF FOREIGN RELATIONS] provides:

> A state has jurisdiction to prescribe a rule of law
>
> (a) attaching legal consequences to conduct that occurs within its territory, whether or not such consequences are determined by the effects of the conduct outside the territory, and
>
> (b) relating to a thing located, or a status or other interest localized, in its territory.

248. *Id.* § 18 provides:

> A state has jurisdiction to prescribe a rule of law attaching legal consequences to conduct that occurs outside its territory and causes an effect within its territory, if either
>
> (a) the conduct and its effect are generally recognized as constituent elements of a crime or tort under the law of states that have reasonably developed legal systems, or

tion to be exercised over the forum's nationals regardless of effect or the location of the national's illegal conduct.[249]

The federal securities laws, and the 1934 Act in particular, have only recently been applied to transactions that are substantially extraterritorial.[250] During the last ten years, however, the courts have increasingly accepted jurisdiction over securities violations that involve small amounts of local "conduct" or "effect." Between the relatively clear situations in which both significant conduct and effect occur either domestically or outside the United States, the courts have struggled to develop a workable and predictable standard for imposing American jurisdiction to protect both American investors and the integrity of laws regulating domestic securities transactions, without violating principles of international law. The result has been, in general, to focus on the degree of conduct within this country and the role of that conduct within the overall transaction giving rise to a securities claim. Yet, the courts have been reluctant to abandon a requirement of at least some domestic effect.

A. *The Persistent Requirement of Domestic Effect*

The 1934 Act predicates jurisdiction in secondary trading on the use,

---

> (b) (i) the conduct and its effect are constituent elements of activity to which the rule applies; (ii) the effect within the territory is substantial; (iii) it occurs as a direct and foreseeable result of the conduct outside the territory; and (iv) the rule is not inconsistent with the principles of justice generally recognized by states that have reasonably developed legal systems.

See also Strassheim v. Daily, 221 U.S. 280, 285 (1911); United States v. Aluminum Co. of America, 148 F.2d 416, 443 (2d Cir. 1945).

The current extraterritorial approach may cause conflict between countries, especially where two countries' laws require inconsistent conduct. Factors for each country to consider in deciding whether to exercise its jurisdiction are set out in RESTATEMENT (SECOND) OF FOREIGN RELATIONS § 40:

> (a) vital national interests of each of the states,
>
> (b) the extent and the nature of the hardship that inconsistent enforcement actions would impose upon the person,
>
> (c) the extent to which the required conduct is to take place in the territory of the other state,
>
> (d) the nationality of the person, and
>
> (e) the extent to which enforcement by action of either state can reasonably be expected to achieve compliance with the rule prescribed by that state.

249. RESTATEMENT (SECOND) OF FOREIGN RELATIONS § 30.

250. The first case in which a federal securities statute was considered in an extraterritorial situation was Kook v. Crang, 182 F. Supp. 388 (S.D.N.Y. 1960). *See* notes 271-73 *infra* and accompanying text. The first successful extraterritorial application of the securities acts was not until 1963 in SEC v. Gulf Intercont'l Fin. Corp., 223 F. Supp. 987 (S.D. Fla. 1963). *See* notes 252-54 *infra* and accompanying text.

direct or indirect, of "any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange."[251] This language would appear to permit the exercise of jurisdiction when only incidental use of interstate facilities in furtherance of a securities transaction occurred, without regard to its effect. Yet most decisions have depended, at least in part, on a finding of domestic effect.

An extreme example is *SEC v. Gulf Intercontinental Finance Corp.*[252] in which the SEC sought to enjoin a Canadian corporation from offering or selling its notes in violation of the antifraud provisions of the 1933 and 1934 Acts.[253] The court had little difficulty finding substantive domestic conduct in furtherance of the scheme to defraud: the corporation was controlled by Americans, who conceived the plan in Florida and directed the offer and sale of the notes (and received the invested money in the form of salaries and unsecured loans) by the use of telephones and the mails. Yet the court struggled and found domestic effect as well by taking judicial notice of the circulation in the United States of Canadian newspapers in which the notes were advertised and reasoning that this constituted a domestic offer of securities.[254]

---

251. 1934 Act § 10, 15 U.S.C. § 78j (1970). Jurisdiction over the activities of broker-dealers is based on their participation in the securities industry, as defined in various provisions of § 3 of the Act, 15 U.S.C. § 78c (1970). *See, e.g.*, 1934 Act § 7(c), 15 U.S.C. § 78g(c) (1970) (margin requirements) ("any member of a national securities exchange or any broker or dealer"). *See generally* Note, *United States Taxation and Regulation of Offshore Mutual Funds*, 83 HARV. L. REV. 404, 442-43 & nn.102-04 (1969).

252. 223 F. Supp. 987 (S.D. Fla. 1973).

253. 1933 Act § 17(a), 15 U.S.C. § 77q(a) (1970); 1934 Act § 10(b), 15 U.S.C. § 78j(b) (1970).

254. Despite an absence of proof that any actual offer or sale of the securities was made to an American, the court also found it necessary to take judicial notice of the practice of Canadians to vacation in the United States (where they might be expected to read their hometown newspapers) and of widespread American investment in the Canadian securities market. The opinion is confusing on the importance of these facts. Since domestic conduct was clear—and the court went further by characterizing the Canadian corporation as a "conduit" through which the "true issuers," the American promoters and domestic subsidiaries which they controlled, extended the illegal offer—apparently the court took sweeping judicial notice of these facts in order to show domestic effect. Yet it also characterized the domestic "offer," thus established, as a requisite of local conduct:

> It is sufficient for subject matter jurisdiction under the Acts that such offers be made within the United States without a showing that such offers were accepted by actual sale, or that the alleged misrepresentations were in fact successful in inducing the sale of such securities by reliance thereon.

In *Roth v. Fund of Funds, Ltd.*[255] the Second Circuit found subject matter jurisdiction in a stockholder's derivative action under section 16(b) of the 1934 Act[256] against a Canadian corporation to recover short-swing profits made by that corporation in a purchase and sale of the common stock of a domestic corporation on the New York Stock Exchange. Again, domestic conduct was clear; the securities were bought and sold on an American exchange through local brokers and payment was made through a New York bank. But the court devoted considerable attention to the domestic effect of the transaction and compared the injury to "outside" stockholders caused by the trading of both foreign and domestic "insiders."[257]

A third example of judicial concern with effect despite significant domestic conduct is *SEC v. United Financial Group, Inc.*,[258] a rule 10b-5[259] case. After finding "very substantial activity" in the United States in furtherance of an allegedly fraudulent offer to exchange the stock of two foreign mutual funds, the court went on to find that "at

223 F. Supp. at 994-95 (footnotes omitted). Later, however, the court reasoned that any use of interstate facilities in furtherance of the scheme satisfied the conduct requirement:

> It would appear that where the scheme is one which necessarily must be accomplished in part by use of the mails or interstate facilities within the limits of our federal jurisdiction that even though the offer were made entirely outside the nation that the remedial protection of these sections may be invoked.

Id. at 995. *Cf.* Hooper v. Mountain States Sec. Corp., 282 F.2d 195 (10th Cir. 1960); United States v. Cashin, 281 F.2d 669 (5th Cir. 1960).

255. 405 F.2d 421 (2d Cir. 1968), *cert. denied,* 394 U.S. 975 (1969).

256. 1934 Act § 16(b), 15 U.S.C. § 78p(b) (1970).

257. *Roth* is one of several cases in which a defense under the § 30(b) exemption, 15 U.S.C. § 78dd(b) (1970), is raised. The argument is that § 30(b) exempts from the provisions of the 1934 Act any person who "transacts a business in securities without the jurisdiction of the United States"; since the insider profits were made by a foreign corporation "without the jurisdiction of the United States" in the securities of an American corporation, the section should apply. The *Roth* court answered this argument by pointing out that the effect of insider trading on the American investing public is the same regardless of whether the insider is itself an American. Further, the insider's use of domestic facilities to transact its purchase and sale meant that it no longer transacted business "without the jurisdiction of the United States." 405 F.2d at 422.

The § 30(b) exemption has also been judicially interpreted to apply not only to broker-dealers in foreign securities or exchanges, but also to individual, occasional transactions. *See* Schoenbaum v. Firstbrook, 405 F.2d 200, 207 (2d Cir.), *rev'd on rehearing on other grounds,* 405 F.2d 215 (2d Cir. 1968) (en banc), *cert. denied,* 395 U.S. 906 (1969). *See generally* Goldman & Magrino, *Some Foreign Aspects of Securities Regulation: Towards a Reevaluation of Section 30(b) of the Securities Exchange Act of 1934,* 55 VA. L. REV. 1015 (1969).

258. 474 F.2d 354 (9th Cir. 1973).

259. 17 C.F.R. § 240.10b-5 (1974).

least three" American investors had been offered and sold the securities involved in the scheme.[260] The court specifically identified "the impact . . . upon American investors" as an element of jurisdiction, and declined to rule on the SEC's alternative theory that jurisdiction could be entertained solely on the use of facilities of interstate commerce.[261]

The necessity of a finding of domestic effect is difficult to isolate in the cases because most involve transactions with at least some aspects of both conduct and effect in the United States. Thus, in a typical case involving alleged violation of the antifraud provisions of the securities laws, some activity in furtherance of the effort to offer or sell securities requires the use of domestic interstate facilities and almost necessarily affects Americans, by reason of their equity ownership of the corporation whose securities are involved, their "exposure," however tenuous,

---

260. 474 F.2d at 357. The court noted that the "relative percentage" of American investors involved was not determinative, citing McGee v. International Life Ins. Co., 355 U.S. 220 (1957), in which personal jurisdiction over a Texas insurance company in a California court on the basis of a single California policyholder was held not to violate due process.

261. The SEC's "interstate commerce facilities use" theory has never been adopted as the sole basis for extraterritorial application of the securities laws. The theory is that the United States has an interest in the use to which its facilities are put, and therefore has plenary power over that use. Thus, Congress has power to regulate even incidental use of interstate facilities connected with securities fraud. Since the *United Financial* court found both domestic effect and more than incidental use of interstate facilities, it did not have to consider the theory, although the court remarked that it had "some merit." 474 F.2d at 358.

The "interstate commerce facilities use" theory, if adopted, would be enormously expansive of American jurisdiction in light of decisions construing the "jurisdictional means" provisions of the securities acts in purely domestic transactions. As recently as 1959, a federal court stated that a sale of securities consummated

> while traveling from one state to another in an automobile for the express purpose of selling those securities does not establish a violation of the [1933] Act . . . . Nor is there a use of an instrument of interstate commerce when . . . checks were sent back to the drawee bank in [another state] in the usual course of business.

Repass v. Rees, 174 F. Supp. 898, 902-03 (D. Colo. 1959). Only five years later, in Lennerth v. Mendenhall, 234 F. Supp. 59 (N.D. Ohio 1964), it was held that an intrastate telephone call was sufficient to invoke federal jurisdiction, the "character of the instrument used" being determinative. *Accord*, Levin v. Marder, 343 F. Supp. 1050 (W.D. Pa. 1972) (local calls sufficient if they play "material role in the transaction"); Ingraffia v. Belle Mead Hosp., Inc., 319 F. Supp. 537 (E.D. La. 1970). *Contra*, Burke v. Triple A Mach. Shop, Inc., 438 F.2d 978 (9th Cir. 1971). Since the phrase "interstate commerce" is defined in § 3(a)(17) of the 1934 Act, 15 U.S.C. § 78c(a)(17) (1970), as "trade, commerce, transportation, or communication among the several States, or between any foreign country and any State, or between any state and any place or ship outside thereof," acceptance of the SEC's theory would arguably bring with it an adoption of the expanded means test.

to the offer, or by some other means. Only one case, *Schoenbaum v. Firstbrook*,[262] has held that such effect by itself will support jurisdiction. In *Schoenbaum*, another 10b-5 action, an American shareholder in Banff Oil, a Canadian corporation, sued Banff's directors for consipiring to defraud the corporation by causing it to sell its treasury shares at a price they knew, on the basis of undisclosed inside information, to be artificially low. The Second Circuit identified no domestic conduct in furtherance of the scheme to defraud, but found jurisdiction on the basis of the domestic effect of depressing the market price of Banff's common stock, which was sold on an American exchange and owned by American investors.[263]

The Second Circuit recently indicated in dictum that it would not extend *Schoenbaum*'s "effect" doctrine to permit jurisdiction over purely extraterritorial transactions whose only connection with the United States was their effect on an American corporation whose stock was traded on an American exchange. In *Leasco Data Processing Equipment Corp. v. Maxwell*[264] the court found jurisdiction for a 10b-5 claim by an American investor who was fraudulently induced in the United States to buy stock in an English corporation on an English exchange. The corporation's securities were not traded domestically, and consequently the *Schoenbaum* holding was not in point. But the *Leasco* court declined to premise jurisdiction solely on domestic fraudulent conduct. Defendants argued that the securities were purchased in the name of a foreign subsidiary of an American corporation, and thus, since no American investor had standing to sue as a "purchaser" of securities under section 10(b), there was no jurisdiction. Rather than look solely at defendants' domestic conduct, the court reasoned

---

262. 405 F.2d 200 (2d Cir.), *rev'd on rehearing on other grounds*, 405 F.2d 215 (2d Cir. 1968) (en banc), *cert. denied*, 395 U.S. 906 (1969). *Schoenbaum* is criticized in Becker, *Extraterritorial Dimensions of the Securities Exchange Act*, 2 N.Y.U.J. INT'L L. & POL. 233 (1969).

263. 405 F.2d at 208-09:

> A fraud upon a corporation which has the effect of depriving it of fair compensation for the issuance of its stock would necessarily have the effect of reducing the equity of the corporation's shareholders and this reduction in equity would be reflected in lower prices bid for the shares on the domestic stock market. This impairment of the value of American investments by sales by the issuer in a foreign country, allegedly in violation of the [1934] Act, has in our view, a sufficiently serious effect upon United States commerce to warrant assertion of jurisdiction for the protection of American investors and consideration of the merits of plaintiff's claim.

264. 468 F.2d 1326 (2d Cir. 1972).

that the subsidiary was an alter ego of its American parent, and that the latter had been recognized by the parties to the transaction as being "intimately involved." The court then distinguished the situation in which "a German and a Japanese businessman met in New York for convenience, and the latter fraudulently induced the former to make purchases of Japanese securities on the Tokyo Stock Exchange."[265]

The effect of the *Leasco* opinion is two-fold. First, insofar as cases without significant domestic conduct are concerned, it restricts the validity of *Schoenbaum* to situations involving fraud in foreign securities sold on American exchanges.[266] Second, in cases not involving securities traded domestically, it requires both domestic conduct and domestic effect.[267] Thus, to use the court's Japanese illustration,

---

265. *Id.* at 1338.

266. The *Leasco* court first identified *Schoenbaum*'s narrow holding that jurisdiction would lie despite an absence of domestic conduct where the transaction involved stock sold domestically and harmed American investors. Then, viewing that holding as resolving part of the question raised by § 18 of the *Restatement*, namely, under what circumstances will American courts entertain jurisdiction over conduct occurring outside American territory that causes domestic effect, the *Leasco* court expressed

> most serious doubt whether, despite . . . *Schoenbaum*, § 10(b) would be applicable simply because of the adverse effect of the fraudulently induced purchases in England of securities of an English corporation, not traded in an organized American securities market, upon an American corporation whose stock is listed on the New York Stock Exchange and its shareholders.

Id. at 1334, *citing* Vanity Fair Mills, Inc. v. T. Eaton & Co., 234 F.2d 633 (2d Cir.), *cert. denied*, 352 U.S. 871 (1956). The court concluded that "[w]hen no fraud has been practiced in this country and the purchase or sale has not been made here, we would be hard pressed to find justification for going beyond *Schoenbaum*." 468 F.2d at 1334.

267. This conclusion is implicit in the court's treatment of the defense that the purchaser of the securities was not American. Had the *Leasco* court intended to hold that substantial local conduct was in itself an adequate basis for jurisdiction, it could have dismissed the argument as irrelevant. The court, however, after first arguing that it was the American parent corporation which had a beneficial interest in the purchase, went on to reason that even if the foreign subsidiary were the beneficial owner, "it would be elevating form over substance to hold that this entails a conclusion that the purchases did not have a *sufficient effect in the United States* to make § 10(b) apply." 468 F.2d at 1338 (emphasis added). Finally, a pure conduct analysis would have made discussion of the situation involving the German and Japanese businessmen superfluous. For further discussion of the *Leasco* case, see Becker, *supra* note 262, 67 AM. J. INT'L L. 554 (1973); 6 VAND. J. TRANSNAT'L L. 687 (1973).

In Selas of America (Nederland) N.V. v. Selas Corp. of America, 365 F. Supp. 1382 (E.D. Pa. 1973), an American corporation reached an agreement in the United States with employees of its wholly owned Dutch subsidiary to sell 60% of the shares of the subsidiary to a second Dutch corporation to be organized by the employees. As a part of the agreement, the parent was to receive the retained earnings of the subsidiary as of a certain date and to acquire noncancellable preferred shares in the subsidiary. When a

even where every material element of a 10b-5 action occurred in the United States, if the transaction had no effect on either the American investing public (through its impact on the security's price in a domestic market) or an American purchaser, the requisite effect would be absent and jurisdiction would not lie.

This analysis is supported by *United States v. Clark*,[268] a recent case decided in the Southern District of New York, which confirmed the validity of effect considerations in all but the specialized *Schoenbaum* situation. The *Clark* court, after discussing *Leasco* and *Schoenbaum*, concluded that their "cumulative effect" was that section 10(b) "cover[s] at least charges of fraudulent conduct in the United States resulting in sales of securities abroad which have a substantial detrimental effect upon the interests of American investors."[269] Thus, despite the apparent existence of substantial conduct in the United States in fraudulently inducing the overseas sale of debentures in a foreign subsidiary corporation, the *Clark* court found it necessary also to find domestic effect in the form of the artifical inflation of the domestic market price of the parent corporation as a result of the sale of the subsidiary's securities overseas. The effect in *Clark* is less direct than the effect in *Leasco*, where the beneficial purchaser of the securities was an American corporation, but *some* effect was deemed requisite to jurisdiction.[270]

---

dispute arose about the amount of earnings, the parent sued the subsidiary in the Netherlands to establish the primacy of its audit of the subsidiary's earnings and to reacquire full control of the subsidiary. The subsidiary thereafter sued in the United States, alleging that the parent had made fraudulent misrepresentations in the United States in connection with both the original sale of the subsidiary's shares to the other Dutch corporation and the acquisition of the preferred shares. The parent urged that no jurisdiction should attach to a foreign transfer of securities in a foreign corporation to a foreign purchaser, and invited the court to find that *Schoenbaum*, *Leasco*, and *Travis* require some form of domestic effect, either on the American securities markets or an American investor. The *Selas* court declined to decide whether domestic conduct alone was sufficient to invoke jurisdiction by finding that "the transaction . . . ha[d] significant impact on American securities markets." *Id.* at 1386. The court characterized the domestic conduct as "sufficient" and cited the effect of the transactions on the earnings of the parent, whose stock is publicly owned and registered on the American Stock Exchange.

268. 359 F. Supp. 131 (S.D.N.Y. 1973).

269. *Id.* at 134.

270. *Clark*, like *United Financial*, *see* notes 258-61 *supra* and accompanying text, involved illegal conduct by a foreign subsidiary which was directed by the subsidiary's domestic parent. Neither the *Clark* nor the *United Financial* court specified much conduct occurring within the geographical boundaries of the United States that was an integral part of the scheme to defraud. Rather, the courts evaluated the series of acts, including

B. *The Meaning of "Domestic Conduct"*

A second consideration of courts faced with the question of extraterritorial application of the securities acts is *what* domestic conduct is sufficient to invoke jurisdiction. Generally, a court's primary concern in analyzing the facts is with conduct. Those few courts that have dismissed cases for lack of jurisdiction have done so because domestic conduct was either absent or insignificant. Thus, in *Kook v. Crang*,[271] in which an American investor sued his Canadian broker for violation of the margin requirements of section 7(c) of the 1934 Act[272] when extending credit to the investor for a Canadian investment, the court held that, although the broker was registered with the SEC and made use of the mails, jurisdiction would not lie without domestic conduct that was "necessary and substantial." Since the broker's American activities were not closely related to the extension of credit, which was the basis for the investor's section 7(c) action, the court dismissed the action.[273]

---

the parents' implementation of the plans, as a unified scheme and considered the fraudulent acts of the subsidiaries to be attributable to their parents—and thus "domestic." In this fashion, the definition of illegal or substantial domestic conduct has itself been expanded.

271. 182 F. Supp. 388 (S.D.N.Y. 1960).

272. 1934 Act § 7(c), 15 U.S.C. § 78g(c) (1970), declares it unlawful for "any broker or dealer, directly or indirectly, to extend credit or arrange for the extension or maintenance of credit to or for any customer" on non-exempted securities in violation of the regulations established by the Board of Governors of the Federal Reserve System.

273. 182 F. Supp. at 390-91:

> The question here is not whether there are contacts with the United States sufficient to give this Court jurisdiction, no one questions that, but rather whether Congress intended to make the statute applicable to these transactions. We hold that such was not the intention of the legislature and that "jurisdiction" as used in Section 30(b) contemplates some necessary and substantial act within the United States.

Specifically, *Kook* required a showing of some domestic act directly or indirectly in furtherance of the extension or maintenance of credit.

Only two other cases have been dismissed for lack of subject matter jurisdiction. In Finch v. Marathon Sec. Corp., 316 F. Supp. 1345 (S.D.N.Y. 1970), an Englishman alleged that he was fraudulently induced to purchase the interest of a Bermudian corporation in an English corporation in violation of rule 10b-5. Both the misleading statements alleged and the sale took place in England; the Bermudian corporation was a closed investment company whose securities were not traded in the United States. The *Finch* court held that a number of American contacts, including substantial American control of the Bermudian corporation and the signing of a preliminary agreement to purchase the shares (later re-executed, with some changes and the requisite formalities, in England), were not sufficient to give it subject matter jurisdiction. The court found *Schoenbaum* "dispositive," yet based its holding on both the fact that the "substance"

That courts will not grant jurisdiction merely on the basis of establishing *some* conduct and effect is illustrated by *Ferraioli v. Cantor*,[274] a pre-*Schoenbaum* case. In *Ferraioli* an American shareholder in General Baking, an American corporation, brought a 10b-5 class action against a Canadian corporation for selling its controlling shares in General Baking to a second Canadian corporation at a price above the market value on the basis of inside information, without informing the American investor of the information or making the same offer available to him. As a part of the transfer of control between the two Canadian corporations, the seller, by using the mails, caused its proxies to be voted on its behalf and caused its designated directors in the United States to resign. Rather than simply find that a minimum of domestic conduct (use of the mails) had occurred or focus on the considerable impact on American investors, the court found jurisdiction by characterizing the directors' resignations as an integral part of the transfer of control in the target corporation, part of the course of conduct that gave rise to the 10b-5 claim, and ignored considerations of effect.[275]

Similarly, in a recent Eighth Circuit case, *Travis v. Anthes Imperial Ltd.*, the court found jurisdiction in a 10b-5 case involving foreign securities that were "neither registered nor traded on an organized United States market."[276] The court purported to make a pure conduct analysis, stating that the "essential issue is whether the defendants' conduct in the United States was of such significance to subject them to . . . jurisdiction," and even went so far as to say that "subject matter

---

of the fraudulent conduct occurred outside the United States and that there was "no showing of any domestic injury." *Id.* at 1349.

In Manus v. Bank of Bermuda, Ltd., [1971-1972 Transfer Binder] CCH FED. SEC. L. REP. ¶ 93,299 (S.D.N.Y. 1971), the court dismissed a 10b-5 claim for failure to state a cause of action—noting that a suit for breach of a fiduciary duty cannot be "bootstrapped" into 10b-5 without a showing of scienter, citing Shemtob v. Shearson, Hammill & Co., 448 F.2d 442 (2d Cir. 1971)—but added that the action also lacked subject matter jurisdiction since the parties were all aliens, the principal transactions took place outside the United States, and no detriment to American investors or markets resulted.

274. 259 F. Supp. 842 (S.D.N.Y. 1966).

275. The court's analysis reflects, at least in part, its concurrence in the parties' assumption that the 1934 Act "presumptively" applies only to acts committed in the United States. The question of "extraterritoriality" was not briefed or argued. *Id.* at 845. Perhaps because of this presumption, the *Ferraioli* court was preoccupied with characterizing some part of the defendants' course of conduct as "domestic," instead of emphasizing the policy of the Act of protecting American investors in American securities against fraudulent acts, whether foreign or not. *See generally* Note, *Extraterritorial Application of the Securities Exchange Act of 1934*, 69 COLUM. L. REV. 94 (1969).

276. Travis v. Anthes Imperial Ltd., 473 F.2d 515 (8th Cir. 1973).

jurisdiction attaches whenever there has been significant conduct with respect to alleged violations in the United States."[277] Such a position would support jurisdiction in *Leasco*'s hypothetical of the two foreign businessmen and would, thereby, implicitly eliminate the effect requirement. Since the plaintiffs in *Travis* were, however, defrauded American investors, effect was present, and the court's attempted confinement of the jurisdictional question to conduct alone is not as significant as it appears at first blush.[278]

It is doubtful that any analysis based primarily on consideration of the quantity of domestic "conduct" or "effect" is satisfactory. Conduct analysis runs the risk of preoccupation with jurisdictional "means," a consideration more appropriate to questions of federal and state jurisdiction than to extraterritoriality.[279] Further, such an analysis may

---

277. *Id.* at 524.

278. Both *Leasco* and *Travis* based a conduct analysis on their interpretation of § 17 of the *Restatement* which, on its face, appears to require domestic conduct "relating to a thing located, or a status or other interest localized," in the nation's territory. The *Leasco* court examined one of the section's official illustrations to conclude that, despite the quoted qualification, "[c]onduct within the territory alone would seem sufficient from the standpoint of jurisdiction to prescribe a rule." 468 F.2d at 1334. The illustration is this:

> *X* and *Y* are in State *A*. *X* makes a misrepresentation to *Y*. *X* and *Y* go to State *B*. Solely because of the prior misrepresentations, *Y* delivers money to *X*. *A* has jurisdiction to prescribe a criminal penalty for obtaining money by false pretenses.

RESTATEMENT (SECOND) OF FOREIGN RELATIONS § 17, Illustration 2. Nevertheless the court reasoned that while this may permit jurisdiction to attach purely to conduct, the actual extent of jurisdiction must be determined by statutory construction. It was at this point that the court distinguished the hypothetical of the foreign businessmen and discussed domestic effect. 468 F.2d at 1337-38.

The *Travis* court, to support its statement that jurisdiction attaches "whenever" there is significant local conduct, cited both § 17 and the *Leasco* court's treatment of it, but confused the matter by remarking that "[m]oreover, clause (b) of § 17 [requiring effect] is met here because the defendants' conduct in the United States was directly related to and affected the interests of [American] shareholders." 473 F.2d at 524 n.15.

279. The expanded jurisdictional means test, *see* note 261 *supra*, may be acceptable as a rationale for widespread SEC involvement in domestic securities practices. By triggering federal mechanisms for registration, disclosure, and antifraud protection on the least "interstate" activity imaginable, courts have provided domestic investors and markets with protection and confidence, largely without upsetting state regulation and philosophy through enforcement of the blue sky laws. Involving the SEC and the full panoply of federal securities legislation in largely extraterritorial matters on the basis of the use of interstate facilities is another matter. To use the *Leasco* hypothetical, it makes little sense to require representatives of two foreign businesses, whose activities and securities transactions have no domestic impact, to comply with the securities laws of the United States or in effect to write into their understanding potential liabilities for viola-

overlook the effect of conduct on domestic investors and the domestic securities markets. Effect analysis more accurately reflects the congressional policy of protecting American investors, but it runs the risk of ignoring principles of international law and comity by focusing on what may be only a minor part of a transaction that is best supervised or adjudicated elsewhere.[280] Both analyses raise difficult problems of comity and enforcement,[281] and may, the more expansive they become, interfere with other congressional aims such as encouraging foreign in-

---

tions of local law solely because their agreement to sell securities was reached in this country.

280. This problem is dealt with in § 40 of the *Restatement, see* note 248 *supra,* but is ignored for the most part by the courts. In a recent case, however, the Supreme Court indicated that the policy of affording protection to purchasers of securities will not always override other considerations in international transactions. In Scherk v. Alberto-Culver Co., 417 U.S. 506 (1974), an American corporation which had purchased three foreign corporations from a German seller brought a 10b-5 action for misrepresentations that allegedly occurred in the United States. Although the sales contract between the parties called for arbitration of disputes before a tribunal in France, the buyer obtained an injunction against the seller from proceeding further with arbitration.

On appeal, the Court was thus faced with a conflict between the policy of the securities acts to permit the plaintiff his choice of forum, and the arbitration agreement. The Court had previously held, in Wilko v. Swan, 346 U.S. 427 (1953), that the antiwaiver provision of the 1933 Act, 15 U.S.C. § 77n (1970); *see* 1934 Act § 29(b), 15 U.S.C. § 78cc(b) (1970), renders an arbitration agreement void. The *Scherk* Court, however, distinguished *Wilko* on the ground that it involved a purely domestic transaction, and held that in international transactions, the arbitration agreement is controlling for two reasons: (1) the advantage to the plaintiff of selecting his forum is "chimerical" because the defendant may avail himself more quickly of remedies in foreign tribunals; and (2) advance determination of a forum is "an almost indispensable precondition to achievement of the orderliness and predictability essential to any international business transaction." 417 U.S. at 516 (Stewart, J.). *Cf.* Bremen v. Zapata Off-Shore Co., 407 U.S. 1 (1972).

Scherk is significant to the issue of extraterritorial jurisdiction for two reasons. First, the case suggests that, so long as a transaction is international in character, American jurisdiction can be prevented by the existence of an arbitration agreement. Second, in determining which transactions are governed by *Wilko* and which by *Scherk,* courts must determine whether they are "international," and *Scherk* implies a more conservative test than the jurisdiction cases. *See* 417 U.S. at 521 (Douglas, J., dissenting). The *Scherk* majority acknowledged that there may be cases in which the international "contacts" are "insignificant" or "attenuated," *id.* at 517 n.11 and thus would come within *Wilko;* but in *Scherk* virtually the entire impact was domestic, since the defrauded buyer was an American corporation, owned by American shareholders and traded publicly in the United States, and the fraudulent misrepresentations, although only a part of discussions that were conducted for the most part in Europe, occurred in the United States.

281. *See* Lauritzen v. Larsen, 345 U.S. 571 (1953) (discussing the possibility of retaliation by foreign governments against what they view as unwarranted interference by the United States in their internal affairs).

vestment in the United States to benefit the American balance of payments.[282] As a result, the question of jurisdiction over international transactions in securities should not be entrusted to piecemeal adjudication, but rather should be directed by SEC regulations under the guidance of Congress. The role of the courts would then be limited to determinations of whether imposing jurisdiction in particular cases violates due process.

---

282. This policy was the motivation for the Interest Equalization Tax Act, Pub. L. No. 88-563, 78 Stat. 809 (1964), *as amended,* INT. REV. CODE OF 1954, §§ 4911-22, which taxes American investment in foreign securities, and the Foreign Investors Tax Act of 1966, Pub. L. No. 89-809, 80 Stat. 1541, *as amended,* INT. REV. CODE OF 1954. §§ 1248-49, which broadened favorable tax treatment for foreign investors in United States securities by including large-scale foreign investment organizations and ended the tax on dividend distributions by investment companies not engaged in domestic business but dealing in American securities. *See generally* S. ROBERTS & W. WARREN, FOREIGN INVESTORS TAX ACT (1967); Note, *supra* note 251, at 407-26; Note, *Offshore Financing for United States Business Ventures,* 48 IND. L.J. 43 (1973). As a result of a more favorable balance of payments picture and to reduce the limitation on foreign investments by Americans, the interest equalization tax rate was recently reduced to zero. *See* Exec. Order No. 11,766, 39 Fed. Reg. 3807 (1974).

For a discussion of the rather complex interrelationship between securities policy and tax policy, see BNA SEC. REG. & L. REP. No. 257, at D-1 (June 19, 1974) (address by SEC Chairman Ray Garrett to the Financial Times Conference). Mr. Garrett indicates, for example, that because of the removal of the interest equalization tax, the SEC will reevaluate its position on exempting securities that have "come to rest" abroad, that is, securities resold to American investors by the foreign purchaser of a foreign issue. *Id.* at D-3.