Extraterritoriality as Standing:
A Standing Theory of the Extraterritorial Application of the Securities Laws

Erez Reuveni*

This Article contends that the current treatment of the extraterritorial scope of the 1934 Securities Exchange Act as a question of subject matter jurisdiction is wrong. Although the Act is silent as to its extraterritorial application, for over forty years, courts have analyzed the Act’s extraterritorial scope as a question of subject matter jurisdiction, relying on the so-called “conduct” and “effects” tests. Because courts apply these tests in an ad hoc, case-by-case manner, they are inherently unpredictable and unnecessarily complicated. This state of affairs has become particularly troublesome in recent years, as so-called “foreign-cubed” securities fraud lawsuits — lawsuits filed by foreign plaintiffs against

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foreign defendants, alleging fraud in connection with the sale or purchase of shares in foreign markets — have proliferated in federal courts. This Article argues that contrary to current practice, the extraterritorial reach of section 10(b) and Rule 10b-5 of the Act is really a question of statutory standing. Under the analysis developed here, the appropriate question for courts to ask is not whether they have jurisdiction over foreign claims, but whether Congress intended for the statutory scheme to provide a remedy to foreign plaintiffs. As this Article shows, only foreign investors who purchase or sell stock in the United States have standing to invoke the securities laws. This approach resolves the problems inherent in jurisdictional analysis and provides a simple, easily understood bright-line rule whose predictive value and procedural benefits ensure an optimal enforcement regime against foreign fraud affecting American interests.

TABLE OF CONTENTS
INTRODUCTION ................................................................................. 1073
I. SUBJECT MATTER JURISDICTION UNDER THE CONDUCT AND EFFECTS TESTS ................................................................ 1081
   A. Jurisdiction Based on the Effects Test .................................... 1083
   B. Jurisdiction Based on the Conduct Test ................................... 1084
      1. Early Cases ...................................................................... 1084
II. A NEW FOREIGN-CUBED STANDING ANALYSIS FOR RULE 10b-5 ...................................................................................... 1096
   A. Distinguishing Legislative and Subject Matter Jurisdiction ....... 1096
   B. Determining the Scope of the Rule 10b-5 Implied Cause of Action .......................................................... 1103
      1. Cort v. Ash and Implied Rights of Action Generally ............... 1104
      2. The Contours of the Rule 10b-5 Implied Right of Action .......... 1105
III. APPLYING THE EXTRATERRITORIALITY AS STANDING FRAMEWORK ............................................................ 1110
   A. The 1934 Act’s Legislative Purpose ........................................... 1111
   B. Rule 10b-5 Policy Considerations and Empagran .................. 1117
      1. Deterrence ....................................................................... 1118
      2. Practical Consequences ..................................................... 1121
IV. FOREIGN-CUBED RULE 10B-5 STANDING ................................ 1122
   A. The Test ............................................................................. 1122
   B. Benefits .............................................................................. 1124
CONCLUSION..................................................................................... 1133
INTRODUCTION

The globalization of financial markets has made the world an exceedingly small place for securities issuers. In recent years, this has been particularly true in the context of so-called foreign-cubed1 litigation — transnational securities lawsuits involving claims against foreign defendants brought by foreign investors trading in foreign markets.2 The rate of such claims has increased dramatically in the past decade3 as the American plaintiffs’ bar has sought to cultivate foreign investors and expand the scope of securities class actions on a global scale.4 This explosion of foreign-cubed litigation presents federal courts with the unenviable task of managing class actions alleging securities fraud in foreign countries whose regulatory regimes and securities laws do not mirror American law.5 These claims require courts to address head-on the extraterritorial application of American securities laws, which in turn raises numerous jurisdictional and class certification issues absent from the run-of-the-mill securities suit.

Considering the financial stakes,6 one might expect that the question of the extraterritorial reach of the securities laws would be clearly established by now. But that is not the case. The 1934

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2 See Morrison v. Nat’l Austl. Bank Ltd., 547 F.3d 167, 172 (2d Cir. 2008) (defining foreign-cubed lawsuit as one in which “(1) foreign plaintiff[] is suing (2) a foreign issuer in an American court for violations of American securities laws based on securities transactions in (3) foreign countries”).

3 2008 saw more foreign-cubed suits than in any previous year, and 2009 is on pace to break that record. See STANFORD LAW SCH., SECURITIES CLASS ACTION CLEARINGHOUSE & CORNERSTONE RESEARCH 6-7 (2009), available at http://securities.stanford.edu/clearinghouse_research/2009_YIR/Cornerstone_research_Filings_2009_MidYear_Assessment.pdf.

4 See Buxbaum, supra note 1, at 62; see also Mary Jacoby, For the Tort Bar, A New Client Base: European Investors, WALL ST. J., Sept. 2, 2005, at Al; Andrew Longstreth, Coming to America, AM. LAW., Nov. 1, 2006, at 553.


Securities Exchange Act (the “1934 Act”), which governs the secondary trading of securities, is silent as to its extraterritorial reach. The Act’s central antifraud provision, section 10(b), and Rule 10b-5, promulgated by the Securities and Exchange Commission (“SEC”) pursuant to authority granted by section 10(b), and which provides litigants an implied cause of action, are also silent on this issue. To date, Congress has not enacted legislation addressing the question, and the Supreme Court has not yet answered it. Instead, the issue has been left for the lower federal courts to decide.

For over forty years, those courts have viewed the question of the extraterritorial application of the securities laws to foreign transactions as a question of subject matter jurisdiction, analyzed using the so-called conduct and effects tests. Given the absence of any express guidance in the 1934 Act or its legislative history, courts have turned to policy considerations extrinsic to the statute to delimit its scope.

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7 See discussion infra Part I.
9 Rule 10b-5, adopted pursuant to section 10(b) of the 1934 Act, provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

12 See discussion infra Part I.
13 Id.
14 Id.
Having its basis in policy, rather than congressional edict, the jurisdictional inquiry is judge-made and assumption-driven. Courts analyze the issue on an ad hoc basis, eschewing any bright-line rule.\textsuperscript{15} As a result, jurisdiction is highly unpredictable and the case law is inconsistent. In the words of one exasperated district court, “[A]ny notion that a single precedent or cohesive doctrine may be found which may apply to dispose of all jurisdictional controversies in this sphere is bound to prove as elusive as the quest for a unified field theory explaining the whole of the physical universe.”\textsuperscript{16}

The jurisdictional inquiry’s unpredictability exacerbates already existing uncertainty when foreign-cubed litigation involves a class action, rather than just an individual litigant. Foreign-cubed class actions raise additional threshold questions, including whether foreign investors can be members of a U.S. class action and whether they may serve as lead plaintiffs. The answers often depend on similarly unpredictable tests that ask whether a U.S. class action judgment or settlement would be recognized abroad or whether alternative remedies exist elsewhere for foreign class members. Both of those questions in turn affect many of the requirements for class certification. In recent years courts analyzing virtually identical factual situations have produced wildly divergent rulings on motions for class certification in foreign-cubed cases,\textsuperscript{17} further complicating an already discordant jurisdictional analysis.

A growing consensus is emerging in legal and business circles regarding the drawbacks of the current jurisdictional regime.\textsuperscript{18} The

\textsuperscript{15} Id.


absence of a predictable and uniform body of law articulating the extraterritorial scope of the securities laws seriously constrains a multinational corporation’s ability to forecast which sovereign’s laws will govern its conduct, an important factor in a company’s decision to enter new markets.19 A foreign company conducting a small percentage of its business or issuing a small number of its shares in the United States cannot predict with any certainty whether its small American presence exposes all of its securities worldwide to U.S. liability, creating a significant disincentive for foreign businesses to conduct business or raise capital in the United States.20 Consequently, foreign issuers increasingly choose to list elsewhere rather than face uncertain liability in American markets.21 This in turn has led to a withdrawal of foreign capital from American markets and even caused foreign issuers to delist from American stock exchanges.22 This state of affairs has further caused American equity markets to lose competitiveness with foreign markets, harming both American markets and investors.23

Moreover, the ad hoc nature of the jurisdictional inquiry intrudes upon the prerogatives of the legislative and executive branches, which are best suited to determine whether the regulatory policies of the United States should interfere with a foreign sovereign’s regulation of

19 INTERIM REPORT, supra note 18, at 11 (citing unpredictability of U.S. class action as reason against listing in U.S. markets); see also U.S. CHAMBER OF COMMERCE, supra note 18, at 30 (observing that U.S. legal and regulatory environment is critical factor discouraging companies from accessing U.S. markets).

20 INTERIM REPORT, supra note 18, at 11; U.S. CHAMBER OF COMMERCE, supra note 18, at 1 (determining that “[t]he perception, if not the reality, of burdensome and duplicative regulatory schemes and an inefficient and unfair legal system [are] making U.S. capital markets increasingly less attractive to foreign and domestic companies alike’); Coffee, Law and the Market, supra note 18, at 303-04 (noting that foreign issuers are deterred from cross-listing as “it is not worth risking potential liability in the billions”).

21 INTERIM REPORT, supra note 18, at 29; BLOOMBERG & SCHUMER, supra note 18, at ii, 5, 12, 43-54; Coffee, Law and the Market, supra note 18, at 303; see U.S. CHAMBER OF COMMERCE, supra note 18, at 1, 18.

22 China Staff, Hong Kong Poses Threat to New York as Global Financial Service Leader, EUROMONEY INSTITUTIONAL INVESTOR, Nov. 1, 2006, at 49 (noting trend among Asian companies); Gordon Platt, NYSE Lists Carbon Allowances Fund, GLOBAL FIN., Apr. 1, 2009, at 70, available at 2009 WLNR 7911228; see BLOOMBERG & SCHUMER, supra note 18, at 12-13, 73-75 (noting that foreign issuers are increasingly looking to move to markets in London, whose legal environment is less fraught with uncertainty); PRICEWATERHOUSECOOPERS, 2008 SECURITIES LITIGATION STUDY 1 (2009), available at http://10b5.pwc.com/PDF/ny-09-089%20SECURITIES%20LIT%20STUDY%20FINAL.PDF (noting that foreign listings declined in 2008 for third consecutive year).

23 See sources cited supra note 21.
its internal affairs. That intrusion affects American diplomacy and jeopardizes cross-border cooperation in numerous regulatory areas, including securities fraud, and interferes with the SEC's ability to encourage foreign investment in American markets. Indeed, the interference with foreign sovereigns' regulatory prerogatives may even lead to foreign retaliation against American companies in the form of lawsuits or protective legislation.

Given these complications, recent scholarship has proposed alterations to the jurisdictional analysis under the conduct and effects tests. But what if courts and scholars have been asking the wrong

24 Buxbaum, supra note 1, at 17.

25 The SEC has attempted to assuage foreign concerns regarding the risks of entering American markets by exempting them from certain American regulatory requirements. See Termination of a Foreign Private Issuer's Registration of a Class of Securities, 72 Fed. Reg. 65, 16,934-37 (Apr. 5, 2007). Private enforcement of the securities laws, particularly foreign-cubed class actions, undermines these efforts, sending the opposite message to foreign companies and issuers.


question for forty years? What if the question of the securities laws’
natrerritorial scope is not a question of jurisdiction at all? The late
Judge Henry Friendly, widely recognized as the author of the
foundational opinions addressing the extraterritorial scope of the
securities laws,28 wondered as much in his last authored opinion on
the subject,29 and for good reason — the Supreme Court has never
analyzed the question of the scope of the Rule 10b-5 cause of action as
a question of subject matter jurisdiction. Rather, the Court routinely
views the question as a matter of statutory standing to sue,30 meaning
whether Congress intended for a specific statutory scheme to provide
a remedy to a specific class of plaintiffs.31

Moreover, recent Supreme Court precedent addressing
extraterritoriality in other contexts does not view the extraterritorial
scope of American law as a question of subject matter jurisdiction.32
Both the Supreme Court and lower federal courts acknowledge that
the question of a court’s subject matter jurisdiction is analytically
distinct from the question of the extraterritorial scope of a federal

Rev. 1799, 1799-1801 (1992); Note, American Adjudication of Transnational Security
Fraud, 89 Harv. L. Rev. 553, 571 (1976); Note, Predictability and Comity: Toward
Common Principles of Extraterritorial Jurisdiction, 98 Harv. L. Rev. 1310, 1314-16
(1985).

28 See, e.g., Adena Exploration, Inc. v. Sylvan, 860 F.2d 1242, 1252 (5th Cir.
1988) (making this observation); Bruce A. Ackerman et al., In Memorium: Henry J.

29 AVC Nederland B.V. v. Atrium Inv. P’ship, 740 F.2d 148, 153 (2d Cir. 1984)
(noting that if issue of 1934 Act’s extraterritorial scope “were arising here for the first
time,” appropriate question may not be subject matter jurisdiction, but concluding
that because “every one of this court’s seven major decisions regarding the application
of the securities laws to transactions carried out in part in the United States and in
part abroad has regarded the issue as one of subject-matter jurisdiction,” court felt
“constrained to do likewise”).

30 See discussion infra Part II.

31 See Steel Co. v. Citizens for a Better Env’t, 523 U.S. 83, 96-97, 97 n.2 (1998);
Kohen v. Pac. Inv. Mgmt. Co., 571 F.3d 672, 676 (7th Cir. 2009). Statutory standing
is also referred to as “non-constitutional standing,” Cetacean Cnty v. Bush, 386 F.3d
1169, 1175 (9th Cir. 2004), and is distinct from the “zone of interests” standing
analysis performed in administrative law cases. See Procter & Gamble Co. v. Amway
Corp., 242 F.3d 539, 563 n.49 (5th Cir. 2001); Conte Bros. Auto., Inc. v. Quaker
State-Slick 50, Inc., 165 F.3d 221, 226 (3d Cir. 1998).

32 See Microsoft Corp. v. AT&T Corp., 550 U.S. 437, 453-54 (2007); F. Hoffman-
Act’s employee-numerosity requirement was jurisdictional and holding that “when
Congress does not rank a statutory limitation on coverage as jurisdictional, courts
should treat the restriction as nonjurisdictional in character”).
statute. The former question addresses a federal court’s prescriptive jurisdiction, that is, the court’s power to adjudicate a dispute under the Constitution. A court has such power so long as a plaintiff invokes a nonfrivolous federal cause of action. The latter question addresses legislative jurisdiction, that is, whether Congress intended the relevant statute to reach extraterritorial conduct, and focuses on whether a plaintiff has statutory standing to sue or whether a cause of action exists in the first place, both inquiries decidedly nonjurisdictional in character.

This Article contends that, contrary to current federal court practice, the extraterritorial reach of the 1934 Act is really a question of statutory standing. Statutory standing is nonjurisdictional in nature, meaning it has nothing to do with the court’s constitutional or statutory power to adjudicate a case. However, like jurisdictional questions, statutory standing can be resolved as a threshold issue. The distinction is more than a semantic dispute. The “jurisdiction” and “statutory standing” labels carry with them a distinct set of procedural and substantive benefits and drawbacks. Viewing the extraterritoriality of the 1934 Act as a question of statutory standing rather than a question of jurisdiction is more consistent with Supreme Court precedent addressing the implied cause of action under Rule 10b-5 and the 1934 Act’s text and legislative history. Additionally, doing so also provides numerous procedural advantages over jurisdictional analysis in terms of providing an optimal Rule 10b-5 enforcement regime. Perhaps most importantly, the analysis developed here provides a predictable, bright-line rule governing when a foreign-cubed plaintiff may sue in an American court. That rule avoids many of the complexities of jurisdictional and class certification analysis present under the current analytical framework. Moreover, unlike


34 Arbaugh, 546 U.S. at 513; Steel, 523 U.S. at 89; Hartford, 509 U.S. at 813 (Scalia, J., dissenting).

35 Arbaugh, 546 U.S. at 513 n.10; Steel, 523 U.S. at 89.

36 EEOC, 499 U.S. at 248; Hartford, 509 U.S. at 813 (Scalia, J., dissenting); Litecubes, 523 F.3d at 1368-69; see discussion infra Part II.

37 Steel, 523 U.S. at 89-97, 97 n.2; Hartford, 509 U.S. at 813.

38 Ortiz v. Fibreboard Corp., 527 U.S. 815, 831 (1999); Steel, 523 U.S. at 96-97, 97 n.2.

39 See discussion infra Part IV.
other recent proposals for reform, the statutory standing analysis requires no new legislation or reversal of prior federal court practice.40

The Article proceeds in four parts. Part I reviews the evolution of jurisdictional analysis under the 1934 Act, beginning with the Second Circuit’s decisions in Schoenbaum v. Firstbrook41 and Leasco Data Processing Equipment v. Maxwell,42 and ending with the Second Circuit’s most recent decision in Morrison v. Natational Australian Bank Ltd.43 As Part I demonstrates, the jurisdictional analysis as originally conceived conferred jurisdiction over foreign plaintiffs only when the complaint alleged that fraud in foreign markets affected American investors or markets. Although these early cases effectively applied a standing inquiry without saying so, modern cases do not, analyzing the issue purely as a matter of jurisdiction. The modern construction of the jurisdictional test is the source of much of the confusion and unpredictability plaguing foreign-cubed litigation today.

Part II sketches the contours of the standing analysis that courts should apply in foreign-cubed cases, drawing on two related, but distinct bodies of Supreme Court precedent addressing legislative and judicial jurisdiction and the creation and scope of implied causes of action. Part III explicitly applies this framework to section 10(b) and Rule 10b-5, paying special attention to the 1934 Act’s purpose, structure, and legislative history, and articulates a simple, bright-line test for Rule 10b-5 standing in foreign-cubed cases. As Part III shows, federal courts’ present application of the conduct test does not establish foreign-cubed standing. Rather, only foreign plaintiffs suffering a loss in connection with the purchase or sale of securities in the United States have standing to sue. The approach applies equally to class actions and precludes the certification of any class that includes foreign-cubed plaintiffs who purchased foreign shares abroad.

Part IV concludes by highlighting the benefits of the standing analysis over subject matter jurisdiction and rebutting perceived criticisms of the approach. This analysis permits early dismissal of nonmeritorious suits and avoids the costs associated with jurisdictional discovery. The analysis also facilitates the SEC’s regulation of American-based fraud affecting foreign sovereign interests, and ensures that the SEC, rather than private litigants,
determines whether the regulatory policies of the United States should interfere with a foreign sovereign’s regulation of its internal affairs.

I. SUBJECT MATTER JURISDICTION UNDER THE CONDUCT AND EFFECTS TESTS

The 1934 Act is famously silent regarding its extraterritorial application, as are both section 10(b) and Rule 10b-5. Since at least 1968, however, courts have read the 1934 Act as reaching some international transactions, analyzing the issue as a question of subject matter jurisdiction over the underlying dispute. Generally, a federal court has subject matter jurisdiction over a federal cause of action so long as the plaintiff’s claim is “colorable,” meaning the claim is not “so immaterial and made solely for the purpose of obtaining jurisdiction” or is “wholly insubstantial and frivolous.” This is a generous standard for plaintiffs, as a court has jurisdiction over the underlying dispute so long as “the right of the petitioners to recover under their complaint will be sustained if the Constitution and laws of the United States are given one construction and will be defeated if they are given another.”

However, courts analyzing jurisdiction under section 10(b) and Rule 10b-5 do not apply this jurisdictional test. Instead, federal courts have adopted two judicially created tests, the so-called conduct and effects tests, which are premised on judicial guesses as to whether federal courts should exercise jurisdiction over foreign-cubed cases. Because of the supposed absence of any guidance from the 1934 Act’s text, structure, or legislative history, federal courts must determine for themselves whether Congress conferred them with jurisdiction over foreign-cubed cases. Rather than ask whether a plaintiff alleges a colorable securities fraud claim, courts must — in the words of an influential early case — divine what “Congress would have wished” had it considered the question of extraterritoriality.

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44 See id. at 170.
47 See Schoenbaum v. Firstbrook, 405 F.2d 200, 208 (2d Cir. 1968).
49 Steel, 523 U.S. at 89.
Courts readily concede that this act of divination is premised on policy considerations found nowhere in the 1934 Act.\textsuperscript{51} Thus, in determining what Congress “would have wished,” the courts have relied on three distinct, but related policy concerns. First, courts invoke the notion of the United States as a safe haven for securities fraud.\textsuperscript{52} Under this rationale, Congress could not have intended for the 1934 Act to permit the United States to serve as a base for the sale of fraudulent securities to foreigners,\textsuperscript{53} because a good neighbor does not allow fraudulent schemes to be perpetrated within its borders, even where those schemes are directed solely at foreign individuals.\textsuperscript{54} Second, courts ask whether Congress would have wished for the limited resources of U.S. courts and law enforcement agencies to be devoted to predominantly foreign transactions.\textsuperscript{55} Under this rationale, courts should not find jurisdiction over “predominantly foreign” transactions if jurisdiction might hamper “the adjudication of domestic disputes and the enforcement of domestic law.”\textsuperscript{56} Third, some courts hold that one purpose of the securities laws is to achieve “a high standard of business ethics in the securities industry.”\textsuperscript{57} Under this rationale, jurisdiction over cases involving foreign transactions is appropriate where it may encourage Americans involved in securities transactions “to behave responsibly.”\textsuperscript{58}

As discussed in the following sections, invocation of these policy concerns has led to the expansion of the effects and conduct tests far beyond their original bounds, causing much of the confusion, inconsistency, and lack of predictability inherent in modern jurisdictional analysis of the 1934 Act.

\textsuperscript{51} Zoelsch, 824 F.2d at 32; Cont’l Grain (AustL) Pty. Ltd. v. Pac. Oilseeds, Inc., 592 F.2d 409, 421 (8th Cir. 1979); SEC v. Kasser, 548 F.2d 109, 116 (3d Cir. 1977); Bersch, 519 F.2d at 993; accord Kauthar SDN BHD v. Sternberg, 149 F.3d 659, 664 & n.6 (7th Cir. 1998); Robinson v. TCI/US W. Commc’ns Inc., 117 F.3d 900, 906 (5th Cir. 1997); Grunenthal GmbH v. Hotz, 712 F.2d 421, 424 (9th Cir. 1983).

\textsuperscript{52} See Butte Mining PLC v. Smith, 76 F.3d 287, 290 (9th Cir. 1996); Cont’l Grain, 592 F.2d at 421; Kasser, 548 F.2d at 116; IIT v. Vencap, 519 F.2d 1001, 1017 (2d Cir. 1975).

\textsuperscript{53} Vencap, 519 F.2d at 1017; see Kasser, 548 F.2d at 116 (“We are reluctant to conclude that Congress intended to allow the United States to become a ‘Barbary Coast,’ as it were, harboring international securities ‘pirates.’ ”).

\textsuperscript{54} Vencap, 519 F.2d at 1017; see Kasser, 548 F.2d at 116.

\textsuperscript{55} Zoelsch, 824 F.2d at 32; Bersch, 519 F.2d at 985.

\textsuperscript{56} Zoelsch, 824 F.2d at 32; see Bersch, 519 F.2d at 985.

\textsuperscript{57} Grunenthal GmbH v. Hotz, 712 F.2d 421, 425 (9th Cir. 1983); see Cont’l Grain, 592 F.2d at 421; Kasser, 548 F.2d at 116.

\textsuperscript{58} Butte Mining PLC v. Smith, 76 F.3d 287, 291 (9th Cir. 1996).
A. Jurisdiction Based on the Effects Test

Under the effects test, courts have jurisdiction over foreign activity where that activity has “a substantial effect in the United States or upon United States citizens.”59 This language tracks the more general proposition that Congress may regulate conduct abroad where that conduct has significant effects in the United States.60 The test was first articulated in the securities context by the Second Circuit in Schoenbaum v. Firstbrook,61 a derivative action brought by an American shareholder of a Canadian corporation, alleging that the company’s controlling shareholders had arranged to purchase shares from the corporation for a price below fair market value.62 Emphasizing both that the shares were listed and traded on an American exchange, and the 1934 Act’s legislative history, the court held that “Congress intended the Exchange Act to have extraterritorial application in order to protect domestic investors who have purchased foreign securities on American exchanges and to protect the domestic securities market from the effects of improper foreign transactions in American securities.”63 Accordingly, under the 1934 Act a court may exercise jurisdiction over securities transactions occurring outside the United States when the transactions “involve stock registered and listed on a national securities exchange, and are detrimental to the interests of American investors.”64

Courts have subsequently limited the effects test, at least where the issuer’s securities do not trade on a U.S. market and plaintiffs do not allege a detrimental effect on a specific interest within the United States. In that situation, “an adverse effect on this country’s general economic interests or on American security prices” is insufficient for

61 See 405 F.2d 200, 206 (2d Cir. 1968) (“We believe that Congress intended the Exchange Act to have extraterritorial application in order to protect domestic investors who have purchased foreign securities on American exchanges and to protect the domestic securities market from the effects of improper foreign transactions in American securities.”), overruled on other grounds by Schoenbaum v. Firstbrook, 405 F.2d 215 (2d Cir. 1968) (en banc).
62 Id. at 204.
63 Id. at 206.
64 Id. at 208.
jurisdictional purposes. Likewise, where Americans hold a fraction of the total shares in a foreign company, the effect on American interests does not satisfy the effects test. These subsequent cases, however, continue to emphasize the 1934 Act’s policy purpose of protecting American investors and markets. That purpose remains the overriding concern of the effects test under any formulation.

In foreign-cubed cases, the effects test is only invoked where defendants list shares on American markets by way of American Depositary Receipts or sell shares in over-the-counter markets. Most often, foreign-cubed cases are analyzed under the conduct test. As the next section will show, the original version of the conduct test is really just a variation of the effects test.

B. Jurisdiction Based on the Conduct Test

1. Early Cases

Under the conduct test, courts have jurisdiction over foreign securities fraud where a substantial portion of the fraud occurred in the United States and directly caused the harm abroad. The conduct test was first articulated by Judge Henry Friendly in *Leasco Data Processing Equipment Corp. v. Maxwell.* In *Leasco,* the plaintiff alleged that foreign defendants had engaged in fraudulent misrepresentations in the United States in order to induce the American plaintiff to purchase securities in London. The securities were neither listed nor traded in the United States, distinguishing the case from *Schoenbaum.*

The Second Circuit nevertheless found jurisdiction, emphasizing the court’s understanding of the 1934 Act’s purpose — the

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66 IIT v. Vencap, Ltd., 519 F.2d 1001, 1016 (2d Cir. 1975) (finding no jurisdiction where Americans held only 0.2% of total shares).
67 See *Zoelsch v. Arthur Andersen & Co.*
68 See *In re Nat’l Austl. Bank Sec. Litig.,* No. 03 Civ. 6537 (BSJ), 2006 WL 3844465, at *1 (S.D.N.Y. 2006); Choi & Silberman, supra note 5, at 469-70, 476.
69 See *Morrison v. Nat’l Austl. Bank Ltd.,* 547 F.3d 167, 171 (2d Cir. 2008); Choi & Silberman, supra note 5, at 476 (“[W]e know of no court that has used the effects test to apply extraterritorial jurisdiction in an f-cubed case.”).
70 Choi & Silberman, supra note 5, at 470.
71 *See Morrison,* 547 F.3d at 171.
72 468 F.2d 1326 (2d Cir. 1972).
73 Id. at 1330-31.
74 Id. at 1334.
protection of American investors.\textsuperscript{75} Thus, where a foreigner makes misrepresentations in the United States intending to induce an American to purchase stock abroad, a court has jurisdiction under the conduct test.\textsuperscript{76}

The court emphasized the point by distinguishing a situation where American investors are harmed from a situation where neither party is American or transacting in American securities.\textsuperscript{77} Thus, U.S. conduct is insufficient to warrant jurisdiction where that conduct consists of a foreigner inducing another foreigner to purchase non-American shares on a foreign securities exchange.\textsuperscript{78} This distinction suggests that the court was really applying an effects test at this point. Just as in Schoenbaum, the misrepresentations caused the diminution in the value of an American’s stock portfolio. Indeed, in the court’s words, “[T]he New Yorker who is the object of fraudulent misrepresentations in New York is as much injured if the securities are of a mine in Saskatchewan as in Nevada.”\textsuperscript{79} Accordingly, under the conduct test announced in \textit{Leasco}, while the nationality of the issuer is irrelevant,\textsuperscript{80} the defrauded purchaser or seller must be American.\textsuperscript{81}

Subsequent early cases in the Second Circuit echoed this reading of the conduct test.\textsuperscript{82} For example, in \textit{Bersch v. Drexel Firestone, Inc.},\textsuperscript{83} the court declined to exercise jurisdiction over foreign members of a putative class action alleging fraudulent misrepresentations as part of a public share offering made by a foreign fund manager whose shareholders were primarily foreign but whose fund invested in American companies. Indeed, the court distinguished between American and non-American class members. According to the court, “[A]ssuming that there were no American purchasers and that the underwriting related, for example, to a large foreign industrial

\textsuperscript{75} \textit{Id}. at 1337 (“Still we must ask ourselves whether, if Congress had thought about the point, it would not have wished to protect an American investor if a foreigner comes to the United States and fraudulently induces him to purchase foreign securities abroad.”).

\textsuperscript{76} \textit{Id}.

\textsuperscript{77} \textit{Id}. at 1338.

\textsuperscript{78} \textit{Id}. (“[W]here 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.”).

\textsuperscript{79} \textit{Id}. at 1336.

\textsuperscript{80} \textit{Id}.

\textsuperscript{81} \textit{Id}. at 1336-38.

\textsuperscript{82} See \textit{IIT v. Vencap, Ltd.}, 519 F.2d 1001, 1016 (2d Cir. 1975); \textit{Bersch v. Drexel Firestone, Inc.}, 519 F.2d 974, 986-87 (2d Cir. 1975).

\textsuperscript{83} 519 F.2d 974.
company clearly identified with a foreign country rather than with the United States . . . we do not believe the activities in the United States, would justify an American court in taking jurisdiction in a suit for damages by foreign plaintiffs. 84 In contrast, if Americans had purchased the shares, an American court would have jurisdiction, regardless of where the statements were made. 85

Bersch, also authored by Judge Friendly, is often cited as the seminal articulation of the conduct test. There, the court stated that the “anti-fraud provisions of the federal securities laws . . . [do not] apply to losses from sales of securities to foreigners outside the United States unless acts (or culpable failures to act) within the United States directly caused such losses.” 86 Bersch’s “direct causation” requirement serves as the basis for the conduct test in every federal appellate court that has considered the issue. 87

Bersch should be read in conjunction with IIT v. Vencap, Ltd. 88 A companion case issued the same day as Bersch, which Bersch references and which Judge Friendly also authored. Doing so shows that Bersch’s “conduct test” is really a variation of the effects test premised on the unique factors present in Bersch and Vencap. In other words, as originally conceived, the conduct test requires harm to American investors or markets.

In Vencap, the plaintiff IIT, an investment trust based in Luxembourg, and three individuals alleged that the defendant Vencap, a foreign venture capital fund, had committed fraud in connection with a complicated series of transactions, part of which unfolded within the United States. 89 The majority stakeholder and controlling principal of Vencap was an American citizen, and 0.2 percent of IIT’s

84 Id. at 986-87.
85 Id. at 993. Although the court identified an intermediate category of American, one who purchases shares of a foreign company abroad, rather than on an American exchange, id., the Second Circuit subsequently rejected the distinction between Americans and foreigners who purchase foreign shares abroad, focusing instead on the U.S. residence of individual investors. See Europe & Overseas Commodity Traders, S.A. v. Banque Paribas London, 147 F.3d 118, 129 & n.12 (2d Cir. 1998).
86 Bersch, 519 F.2d at 993.
88 519 F.2d 1001 (2d Cir. 1973).
89 Id. at 1016.
fundholders — 300 individuals — were also Americans. IIT alleged that Vencap had fraudulently induced IIT to invest in it by misrepresenting its financial health, and that thereafter Vencap’s controlling stakeholder funneled most of Vencap’s funds into separate entities that he controlled. IIT alleged that the funneling occurred in New York, where Vencap’s law firm was based.

The Second Circuit rejected jurisdiction premised solely on the controlling principal’s American citizenship or the fact that the 300 Americans who owned shares in the fund were affected by the fraud. However, the court identified a third, novel rationale for jurisdiction based on conduct within the United States: “We do not think Congress intended to allow the United States to be used as a base for manufacturing fraudulent security devices for export, even when these are peddled only to foreigners. This country would surely look askance if one of our neighbors stood by silently and permitted misrepresented securities to be poured into the United States.”

Although the rationale seems sweeping at first, the court cabinied its holding in three important ways. First, the court noted that its holding was based in part on the fact that the case was “sui generis.” Indeed, the plaintiffs provided 99.9 percent of the funding to a fund controlled by an American citizen who likely would have been beyond the reach of any other jurisdiction. This fact weighed so heavily that Judge Friendly referred to defendant’s acts as “wicked.” Second, the court seemed concerned with ensuring the SEC’s authority to prosecute

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90 Id.
91 Id. at 1005-09.
92 Id.
93 Id. at 1016. As to the majority stakeholder’s nationality, the court stated that “[i]t is simply unimaginable that Congress would have wished the anti-fraud provisions of the securities laws to apply if, for example, [defendant] while in London had done all the acts here charged and had defrauded only European investors.” Id.
94 Id. at 1016-17.
95 Id. at 1017; see also SEC v. United Fin. Group, Inc., 474 F.2d 354, 357 n.7 (9th Cir. 1973) (finding jurisdiction because of sales to American investors, and “finding it unnecessary to render an opinion as to the appropriateness of asserting jurisdiction on the ground of a national interest in protecting this country’s reputation abroad”).
96 Vencap, 519 F.2d at 1019.
97 Id.; see also Coffee, Securities Policeman, supra note 1, at 5 (observing that court was concerned primarily with fact that “American principal defendant would have been likely beyond the reach of other jurisdictions”).
98 Vencap, 519 F.2d at 1018 (remanding for “further findings as to the wickedness of underlying transactions”).
such cases, even if private plaintiffs might be unable to. 99 Immediately after announcing its haven rationale, the court stated, “[B]y the same token it is hard to believe Congress meant to prohibit the SEC from policing similar activities within this country.” 100 Thus, by providing jurisdiction in this sui generis case, the court made sure that the SEC was not hamstrung in its regulatory efforts. Last, the court unequivocally limited jurisdiction based on the haven rationale to situations where “the perpetration of fraudulent acts themselves” occurred in the United States, and stated that jurisdiction “does not extend to mere preparatory activities or the failure to prevent fraudulent acts where the bulk of the activity was performed in foreign countries.” 101 That is, the actions in the United States themselves could constitute a 10b-5 cause of action. 102

Vencap, though sui generis, is thus an effects test of a different sort, to be applied in specific, limited circumstances, but easily reconciled with Schoenbaum and Leasco’s policy concern of protecting American investors and markets. In Schoenbaum and Leasco, the courts were protecting American investors. 103 In Vencap, the court sought to protect the reputation of American capital markets, so that foreign companies would continue to list on American markets and invest in American companies. 104 However, the Vencap safe haven rationale was cabined by the facts of the case. Indeed, while referencing Vencap, Bersch expressly referred to Vencap’s specific, sui generis circumstances, acknowledging that Vencap “itself goes beyond any case yet decided.” 105 And while Bersch found no jurisdiction over the

99 See Coffee, Securities Policeman, supra note 1, at 5. It is well accepted that the SEC’s authority under Section 10(b) goes beyond the text of Rule 10b-5, and this permits the SEC to file fraud suits that private plaintiffs may not be able to. See Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit, 547 U.S. 71, 85 (2006); SEC v. Berger, 322 F.3d 187, 193 (2d Cir. 2003); see also discussion infra Part IV.

100 Vencap, 519 F.2d at 1017.

101 Id. at 1018.


103 Leasco, 468 F.2d at 1333, 1337; Schoenbaum v. Firstbrook, 405 F.2d 200, 206 (2d Cir. 1968).

104 Choi & Silberman, supra note 5, at 490 n.117.

105 Bersch, 519 F.2d at 987.
foreign plaintiffs in that case, Bersch acknowledged Vencap’s concern with enforcement by implying that the SEC could have prophylactically brought suit against the defendants, even if private class action plaintiffs could not.\textsuperscript{106} Bersch also imported the same “merely preparatory” language from Vencap, holding that “we see no reason to extend [Vencap] to cases where the United States activities are merely preparatory or take the form of culpable nonfeasance and are relatively small in comparison to those abroad.”\textsuperscript{107} Thus, Bersch’s “direct causation” test cannot be understood without reference to Vencap and the specific fraud at issue there.

Dozens of cases following Bersch and Vencap cite them for their safe haven and good neighbor rationales. But none exhibited the sui generis facts in Vencap. Indeed, while some cases continued to require some effect on American markets or investors,\textsuperscript{108} many more decoupled the safe haven rationale from the policy of protecting American investors and markets found in Schoenbaum, Leasco, Bersch, and Vencap. Two years after Vencap, the Third Circuit, in SEC v. Kasser,\textsuperscript{109} greatly expanded the scope of the conduct test, holding that American-based conduct satisfied the test even where there were no effects on American investors or markets, so long as “some activity designed to further a fraudulent scheme occurs within this country.”\textsuperscript{110} Kasser expressly invoked Vencap’s haven rationale but did not mention, let alone analyze, the sui generis nature of Vencap’s facts.\textsuperscript{111} Taking Vencap’s haven rationale one step further, the court stated that it was “reluctant to conclude that Congress intended to allow the United States to become a ‘Barbary Coast,’ as it were, harboring international securities ‘pirates.’ ”\textsuperscript{112} Kasser also added an entirely new rationale, that the 1934 Act was “designed to insure high standards of conduct in securities transactions within this country in addition to

\begin{footnotesize}
\begin{enumerate}
\item[106] Id. In the court’s view, “At most the acts in the United States helped to make the gun whence the bullet was fired from places abroad; alternatively proper action in the United States would have prevented the gun’s ever being sent abroad.” Id.
\item[107] Id. Vencap expresses similar sentiment, noting “the line has to be drawn somewhere if the securities laws are not to apply in every instance where something has happened in the United States.” Vencap, 519 F.2d at 1018.
\item[109] 548 F.2d 109 (3d Cir. 1977).
\item[110] Id. at 106, 114.
\item[111] Id. at 114-15.
\item[112] Id. at 116. The court also invoked Vencap’s good neighbor/reciprocity rationale.
\end{enumerate}
\end{footnotesize}
protecting domestic markets and investors from the effects of fraud.\textsuperscript{113}

Kasser perhaps can be understood as an SEC action, and indeed, Kasser cited Vencap's concern that the SEC retain the power to regulate where private litigants might not be able to sue.\textsuperscript{114} But post-Kasser cases invoking Vencap's safe haven rationale were not SEC enforcement actions. The Second Circuit endorsed Kasser's rationale in \textit{IIT v. Cornfeld},\textsuperscript{115} another opinion by Judge Friendly, going so far as to suggest that because all countries share an interest in combating securities fraud, foreign countries would “surely not be offended” by an American court's application of stricter American law to foreign nationals and corporations.\textsuperscript{116} \textit{Cornfeld} also did not discuss Vencap's sui generis nature. The Eighth and Ninth Circuits likewise subsequently adopted Kasser's expansive conduct test, similarly invoking the safe haven rationale with no mention of the unique context in which the rationale arose.\textsuperscript{117} Both courts also invoked Kasser's “standards of conduct” rationale.\textsuperscript{118} Subsequent appellate courts in the Second,\textsuperscript{119} Fifth,\textsuperscript{120} Seventh,\textsuperscript{121} Ninth,\textsuperscript{122} and Eleventh\textsuperscript{123} Circuits, as well as dozens of district courts, have similarly invoked

\textsuperscript{113} Id.
\textsuperscript{114} Id. at 114 (quoting \textit{IIT v.Vencap}, 519 F.2d 1001, 1017 (2d Cir. 1975)); see id. at 116 (extending jurisdiction because it "will enhance the ability of the SEC to police vigorously the conduct of securities dealings within the United States"). Judge Bork, writing for the D.C. Circuit, viewed Kasser this way as well. See Zoelsch v. Arthur Andersen & Co., 824 F.2d 27, 33 n.3 (D.C. Cir. 1987).
\textsuperscript{115} 619 F.2d 909, 921 (2d Cir. 1980).
\textsuperscript{116} In the court's words: "The primary interest of [a foreign state] is in the righting of a wrong done to an entity created by it. If our anti-fraud laws are stricter than [a foreign state's], that country will surely not be offended by their application." \textit{Id.}
\textsuperscript{118} \textit{Grunenthal}, 712 F.2d at 425; \textit{Cont'l Grain}, 592 F.2d at 421.
\textsuperscript{119} Morrison v. Nat'l Austl. Bank Ltd., 547 F.3d 167, 175 (2d Cir. 2008); Europe & Overseas Commodity Traders, S.A. v. Banque Paribas London, 147 F.3d 118, 125 (2d Cir. 1998); Itoba Ltd. v. Lep Group PLC, 54 F.3d 118, 122 (2d Cir. 1995); Psimenos v. E.F. Hutton & Co., 722 F.2d 1041, 1045 (2d Cir. 1983); \textit{Cornfeld}, 619 F.2d at 919; Arthur Lipper Corp. v. SEC, 547 F.2d 171, 179 (2d Cir. 1976).
\textsuperscript{120} Robinson v. TCI/US West Commc'n's Inc., 117 F.3d 900, 905 (5th Cir. 1997); MCG, Inc. v. Great W. Energy Corp., 896 F.2d 170, 174-75 (5th Cir. 1990).
\textsuperscript{121} Kauthar SDN BHD v. Sternberg, 149 F.3d 659, 667 (7th Cir. 1998).
\textsuperscript{122} Butte Mining PLC v. Smith, 76 F.3d 287, 290-91 (9th Cir. 1996).
\textsuperscript{123} \textit{In re CP Ships Ltd. Sec. Litig.}, 578 F.3d at 1313 (11th Cir. 2009). The Eleventh Circuit's predecessor court did so in \textit{United States v. Cook}, 573 F.2d 281, 284 (5th Cir. 1978).
these rationales without any discussion of their original contexts or purposes. Only the D.C. Circuit has expressly rejected them.\textsuperscript{124}

Unmoored from the policies that the conduct test was intended to effectuate, the conduct test has evolved into an expansive and fragmented doctrine with diverse formulations across the circuits. Under the standard generally applied by the Second, Fifth, Seventh, and Eleventh Circuits, a court has subject matter jurisdiction under the conduct test if (1) conduct in the United States directly caused the claimant’s losses, and (2) the conduct was more than merely preparatory to a securities fraud conducted elsewhere.\textsuperscript{125} However, under the standard applied by the Third, Eighth, and Ninth Circuits, courts have jurisdiction where (1) some activity designed to further a fraudulent scheme occurs within the United States, or (2) activity in the United States was in furtherance of a fraudulent scheme and was significant with respect to its accomplishment.\textsuperscript{126} Only the D.C. Circuit appears to have remained true to the conduct test as first articulated, requiring, as Vencap did, that the fraudulent acts occurring in the United States themselves be actionable securities violations.\textsuperscript{127} Still other cases apply some mix of the conduct and effects tests,\textsuperscript{128} while others expressly eschew that approach.\textsuperscript{129} Yet others look for “tipping factors,” meaning some additional connection to the United States beyond the alleged fraudulent acts,\textsuperscript{130} or view identical acts as capable of characterization “as either conduct or effects in the United States.”\textsuperscript{131}

Thus, the conduct test has evolved from a quasi-effects test meant to effectuate Congress’s goal of protecting American investors and markets\textsuperscript{132} into a multiheaded hydra applied without reference to its

\textsuperscript{125} In re CP Ships, 578 F.3d at 1312-15; Morrison v. Nat’l Austl. Bank Ltd., 547 F.3d 167, 171 (2d Cir. 2008); Kauthar, 149 F.3d at 667; Robinson, 117 F.3d at 905.
\textsuperscript{126} Grunenthal GmbH v. Hotz, 712 F.2d 421, 424-25 (9th Cir. 1983); Cont’l Grain, 592 F.2d at 420-21; SEC v. Kasser, 548 F.2d 109, 114-16 (3d Cir. 1977).
\textsuperscript{127} Zoelsch, 824 F.2d at 30-32.
\textsuperscript{128} Itoba Ltd. v. Lep Group PLC, 54 F.3d 118, 121-22 (2d Cir. 1995).
\textsuperscript{131} Id. at 128 & n.13.
\textsuperscript{132} As recently as 1998, at least one Second Circuit panel viewed the conduct test in this way, requiring some effect in the United States, be it a “transaction on a U.S. exchange, economic activity in the U.S., harm to a U.S. party, or activity by a U.S. person or entity meritng redress.” Id. at 130.
original purposes. Instead, the conduct test now effectuates policy considerations found nowhere in the 1934 Act and created entirely by judicial guesswork. Although recent decisions have attempted to simplify the analysis, they have only caused more uncertainty, resulting in confusion in the lower courts and an absence of any consistency in the test’s application.


The Second Circuit’s most recent ruling on the subject, *Morrison v. National Australia Bank Ltd.*, complicates the conduct test further. In *Morrison*, plaintiffs brought suit against National Australia Bank ("NAB"), alleging that NAB’s wholly owned American subsidiary, Homeside Lending Inc. ("Homeside"), manipulated its internal books and records to inflate its earnings. Homeside, based in Florida, transmitted its cooked financial information to NAB’s Australian headquarters, whose executives then incorporated the numbers into public statements disseminated from Australia. Reasoning that the NAB executives with primary responsibility for ensuring the accuracy of NAB’s statements operated out of Australia, the court ruled that it lacked jurisdiction under the conduct test.

The court sought to clarify the conduct test, holding that the test is only satisfied where “the defendant’s conduct in the United States [was] more than merely preparatory to the fraud, and that particular acts or culpable failures to act within the United States directly caused losses to foreign investors abroad.” However, in applying this test, the *Morrison* court created a new concept, which it called the “heart of

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133 The most recent examples are *In re CP Ships Ltd. Securities Litigation*, 578 F.3d 1306, 1313-16 & nn.10-11 (11th Cir. 2009) and *Morrison v. National Australia Bank Ltd.*, 547 F.3d 167, 176 (2d Cir. 2008). Although both cases shared strikingly similar facts, the *Morrison* court declined to find jurisdiction, 547 F.3d at 176, while the *In re CP Ships* court did, 578 F.3d at 1313-16 & n.10. Plaintiffs in *Morrison* cited these two cases in support of certiorari before the Supreme Court. See Supplemental Brief for Petitioners, *Morrison v. Nat’l Austl. Bank Ltd.*, No. 08-1191 (U.S. Aug. 27, 2009), 2009 WL 2759747.

134 547 F.3d 167.

135 As of this writing, *Morrison* is pending before the Supreme Court, with oral argument scheduled for March 29, 2010. At issue is whether and to what extent the 1934 Act covers foreign-cubed fraud. See supra note 11.

136 *Morrison*, 547 F.3d at 169, 171.

137 *Id.* at 171.

138 *Id.* at 176.

139 *Id.* at 172, 173 n.6.
the fraud” test.\textsuperscript{140} Under \textit{Morrison}, whether an act is “merely preparatory” depends on where “what is central or at the heart of a fraudulent scheme” occurred.\textsuperscript{141} That, in turn, depends on at least three factors, including whether conduct abroad was “significantly more central to the fraud and more directly responsible for the harm to investors,” whether the fraud caused any meaningful effects in the United States, and whether the “lengthy chain of causation” was “too remote for liability.”\textsuperscript{142}

For this last factor, \textit{Morrison} cited 	extit{Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.},\textsuperscript{143} a Supreme Court case holding that third parties who did not themselves communicate to the public the fraudulent statements on which plaintiffs relied cannot be defendants in a private Rule 10b-5 action. \textit{Stoneridge} held that “deceptive acts [that] were not communicated to the public” do not suffice to “show reliance . . . except in an indirect chain that we find too remote for liability.”\textsuperscript{144} Although cases preceding \textit{Morrison} never applied the concept, \textit{Morrison} imported the concept of Rule 10b-5 reliance into the jurisdictional analysis. In the court’s view, the alleged fraud in Florida was not communicated to the public.\textsuperscript{145} Rather, the fraud was communicated to NAB headquarters in Australia, who then disseminated the misrepresentations to the public.\textsuperscript{146} Accordingly, because the plaintiffs could not have relied on any statement made in Florida, but instead relied on statements that emanated from NAB in Australia, the court lacked jurisdiction.\textsuperscript{147}

This analysis complicates more than it simplifies, unnecessarily injecting new problems into an already convoluted and confusing area of law.\textsuperscript{148} Indeed, both the Eleventh Circuit and the Solicitor General

\begin{itemize}
\item \textsuperscript{140} \textit{Id.} at 174, 175.
\item \textsuperscript{141} \textit{Id.} at 174.
\item \textsuperscript{142} \textit{Id.} at 176-77.
\item \textsuperscript{143} 552 U.S. 148, 158 (2008).
\item \textsuperscript{144} \textit{Id.}
\item \textsuperscript{145} \textit{Morrison}, 547 F.3d at 176-77.
\item \textsuperscript{146} \textit{Id.}
\item \textsuperscript{147} \textit{Id.}
\item \textsuperscript{148} It is settled law that where the merits of an action are intertwined with the jurisdictional determination, courts may not resolve a motion to dismiss for lack of subject matter jurisdiction prior to discovery. See Gulf Oil Corp. v. Copp Paving Co., 419 U.S. 186, 203 n.19 (1974); MCG, Inc. v. Great W. Energy Corp., 896 F.2d 170, 176 & n.6 (5th Cir. 1990); Thornhill Publ’g Co. v. Gen. Tel. & Elecs. Corp. 594 F.2d 730, 733-34 (9th Cir. 1979). Because reliance is an element of a Rule 10b-5 action, requiring plaintiffs to demonstrate reliance as part of a jurisdictional analysis may require courts to defer ruling on the jurisdictional issue until summary judgment or even trial, injecting greater delay and uncertainty into foreign-cubed litigation.
\end{itemize}
have recently criticized Morrison on this point. Moreover, Morrison’s reliance on Stoneridge conflicts with earlier Second Circuit precedent applying the concept of “derivative reliance” as part of the conduct test. When applicable, plaintiffs do not have to rely on statements disseminated to the public in order to satisfy the conduct test. Rather, they need only rely on statements made by individuals, who themselves relied on fraudulent misrepresentations. Indeed, that is precisely what happened in Morrison. However, Morrison does not discuss derivative reliance when applying Stoneridge.

Morrison also directly conflicts with F. Hoffmann-La Roche Ltd. v. Empagran S.A., a recent Supreme Court case addressing the extraterritorial application of American law where such application interferes with foreign regulatory regimes. Relying on Empagran, defendants and amici in Morrison argued that the conduct test should account for the regulatory interests of foreign states when those interests conflict with American regulatory interests. Morrison rejected the argument. Invoking ITT v. Cornfeld, the Morrison court suggested that any conflict between American and foreign regulatory objectives was not a problem because “governments and other regulators are generally in agreement that fraud should be discouraged.”

149 See In re CP Ships Ltd. Sec. Litig., 578 F.3d 1306, 1316 & nn.10-11 (11th Cir. 2009); Brief for the United States as Amicus Curiae at *11-12, Morrison, No. 08-1191 (U.S. Oct. 27, 2009), 2009 WL 3460233. In In re CP Ships, the parties agreed that the relevant jurisdictional test was Morrison’s iteration of the conduct test. Id. However, the court expressly declined to adopt Morrison as the law of the Eleventh Circuit, noting that not only was Morrison “more stringent” than previous Second Circuit opinions, but also that Morrison may have incorrectly focused on the location of the publicly disseminated fraudulent statements, given that “the false numbers at issue there were actually created in Florida.” Id. The Solicitor General echoed this criticism in a filing before the Supreme Court. Brief for the United States as Amicus Curiae, supra, at *11-12.

150 See Itoha Ltd. v. Lep Group PLC, 54 F.3d 118, 122 (2d Cir. 1995).

151 Id.


154 619 F.2d 909, 921 (2d Cir. 1980).

155 Morrison, 547 F.3d at 175. The court reasoned: “The problem of conflict
However, *Empagran* expressly rejected this reasoning. *Empagran* involved a class action on behalf of foreign and domestic purchasers of vitamins who claimed that foreign and domestic vitamin manufacturers and distributors engaged in a global price-fixing conspiracy, raising the price of vitamin products in the United States and foreign countries. Defendants sought the dismissal of the foreign purchasers who bought vitamins outside the United States. In a unanimous decision, the Supreme Court held that the Sherman Act, as modified by the Foreign Trade Antitrust Improvement Act, did not encompass foreign purchasers, at least where their foreign injuries were independent of any domestic effects.

*Empagran*’s conclusion rested on the notion of “prescriptive comity” — a rule of statutory construction requiring courts to construe “ambiguous statutes to avoid unreasonable interference with the sovereign authority of other nations.” Applying that rule, the Court rejected the plaintiffs’ argument — the same argument endorsed by *Morrison* — that because foreign countries have adopted antitrust laws similar to American antitrust laws, the practical likelihood of interference with the relevant interests of other nations was minimal. As the Court observed, “[E]ven where nations agree about primary conduct . . . they disagree dramatically about appropriate remedies.” Thus, because each country involved had its own regulatory framework that carefully balanced competing considerations relevant to its domestic antitrust enforcement, applying American law to foreign conduct would serve as an “act of legal imperialism.”

It is difficult to reconcile *Empagran*’s admonition against imposing American law on foreign countries as an act of “legal imperialism” between our laws and those of a foreign government is much less of a concern when the issue is the enforcement of the anti-fraud sections of the securities laws than with such provisions as those requiring registration of persons or securities. The reason is that while registration requirements may widely vary, anti-fraud enforcement objectives are broadly similar as governments and other regulators are generally in agreement that fraud should be discouraged. . . . [T]he primary interest of [a foreign state] is in the righting of a wrong done to an entity created by it. If our anti-fraud laws are stricter than [a foreign state’s], that country will surely not be offended by their application.”

156 *Empagran*, 542 U.S. at 159.
157 Id. at 159-60.
158 Id. at 175.
159 Id. at 164.
160 Id. at 167.
161 Id.
162 Id. at 169.
with Morrison’s statement that all countries share common regulatory interests. Perhaps future courts can avoid the issue entirely because Morrison’s observation is dicta, unrelated to its holding. But Empagran adds yet another layer of complexity to an already confusing jurisdictional analysis. Regardless of whether Morrison can be reconciled with Empagran, Morrison serves as the most recent example of how unpredictable and convoluted the conduct test is.

II. A NEW FOREIGN-CUBED STANDING ANALYSIS FOR RULE 10B-5

With so much confusion and unpredictability inherent in foreign-cubed jurisdictional analysis, it is worth asking whether the jurisdictional analysis is the correct analysis at all, especially given the conduct test’s ever-burgeoning scope and complexity. As this Part contends, courts have been incorrectly analyzing the extraterritorial scope of the securities laws as a question of subject matter jurisdiction for over forty years. Instead, the correct analysis should ask whether foreign-cubed plaintiffs have statutory standing under the 1934 Act to invoke the private Rule 10b-5 remedy.

As the following discussion demonstrates, this conclusion follows from a review of two distinct but related bodies of Supreme Court precedent addressing legislative and subject matter jurisdiction — the creation and scope of implied rights of action generally and the implied Rule 10b-5 cause of action specifically. Indeed, the Supreme Court has routinely treated both the question of a statute’s extraterritorial scope and the question of the contours of the Rule 10b-5 implied right of action as matters of statutory construction, rather than jurisdictional issues, and the extraterritorial scope of the 1934 Act should be no different.

A. Distinguishing Legislative and Subject Matter Jurisdiction

Writing his last opinion addressing the extraterritorial scope of the 1934 Act, Judge Friendly observed that if the “issue were arising here for the first time,” the court would not analyze it as a question of

163 See, e.g., sources cited supra note 60.
subject matter jurisdiction. Instead, Judge Friendly suggested that *Bell v. Hood*, a Supreme Court case which none of his earlier opinions cited, would conceivably control the inquiry. *Bell* and its progeny addressed “the court’s statutory or constitutional power to adjudicate the case.” The power to adjudicate—a court’s subject matter jurisdiction—exists so long as the plaintiff “pleads a colorable claim ‘arising under’ the Constitution or laws of the United States.” Thus, “[a] claim invoking federal-question jurisdiction” may be dismissed if it is “immaterial and made solely for the purpose of obtaining jurisdiction” or is “wholly insubstantial and frivolous.”

Judge Friendly presaged subsequent Supreme Court cases addressing the tendency of courts to conflate dismissal based on jurisdiction—the absence of a court’s statutory or constitutional power to adjudicate—with other bases for dismissal. The Court recently stated that jurisdiction “is a word of many, too many, meanings,” and is often used inappropriately, even by the Supreme Court. For example, the Court in *Arbaugh v. Y&H Corp.*, addressing the issue of the propriety of labeling a dismissal as jurisdictional, observed that “[j]udicial opinions . . . often obscure the issue by stating that the court is dismissing ‘for lack of jurisdiction’” when in fact the court is dismissing on some other non-jurisdictional basis. *Arbaugh* viewed these dispositions as “‘drive-by jurisdictional rulings’

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166 See AVC Nederland B.V. v. Atrium P’shp, 740 F.2d 148, 153 (2d Cir. 1984); see also United Phosphorus, Ltd. v. Angus Chem. Co., 322 F.3d 942, 950 (7th Cir. 2003) (en banc) (making same observation in antitrust context, but following precedent).

167 327 U.S. 678 (1946). *Bell* involved a motion to dismiss for subject matter jurisdiction which asserted an absence of jurisdiction because plaintiffs failed to state a cause of action. *Id.* at 680. The Court, observing that the merits may not be addressed as a question of subject matter jurisdiction, held that when the contested basis of federal jurisdiction is also an element of the plaintiff’s asserted federal claim, the claim should not be dismissed on jurisdictional grounds except when it “appears to be immaterial and made solely for the purpose of obtaining jurisdiction or where such a claim is wholly insubstantial and frivolous.” *Id.* at 682-83.

168 *Nederland*, 740 F.2d at 153.


170 *Arbaugh* v. *Y&H Corp.*, 546 U.S. 500, 513 (2006); *Steel*, 523 U.S. at 89.

171 *Arbaugh*, 546 U.S. at 513 n.10.

172 *Id.; Steel*, 523 U.S. at 89.

173 *Arbaugh*, 546 U.S. at 511.

174 *Id.* (quoting Da Silva v. Kinsho Int’l Corp., 229 F.3d 358, 361 (2d Cir. 2000)); see also Romero v. Int’l Terminal Operating Co., 358 U.S. 354, 359 (1959) (“[F]requently . . . where jurisdiction depends on subject matter, the question whether jurisdiction exists [becomes] confused with the question whether the complaint states a cause of action.”).
that should be accorded 'no precedential effect' on the question whether the federal court had authority to adjudicate the claim in suit."175 Indeed, as the Court has stressed, a court's power to adjudicate depends only on whether Congress or the Constitution confers upon the courts the authority to adjudicate the underlying dispute.176 Subject matter jurisdiction in this sense depends only on whether a complaint raises a federal question or invokes diversity, and whether the complaint is a live "case or controversy under Article III," thus conferring constitutional standing on a plaintiff.177 By the same token, Congress can strip a court of jurisdiction already conferred by statute, but this too is addressed under the rubric of whether a court has constitutional or statutory authority to adjudicate the dispute.178

Thus, subject matter jurisdiction properly understood is distinct from the question of the substantive or extraterritorial scope of an act of Congress, which is a matter of "legislative jurisdiction," also called "jurisdiction to prescribe."179 Legislative jurisdiction "refers to the

175 Arbaugh, 546 U.S. at 511 (quoting Steel, 523 U.S. at 91); see United States v. Cotton, 535 U.S. 625, 630 (2002) (reversing Ex parte Bain, 121 U.S. 1 (1887), and holding that that case's "elastic concept of jurisdiction is not what the term 'jurisdiction' means today, i.e., 'the courts' statutory or constitutional power to adjudicate the case' " (quoting Steel, 523 U.S. at 89)).


177 Steel, 523 U.S. at 89-93.


Extraterritoriality as Standing

authority of a state to make its law applicable to persons or activities.\textsuperscript{180} Although Congress can prescribe conduct abroad so long as it has some constitutional basis for doing so and it complies with the Due Process Clause,\textsuperscript{181} Congress is generally presumed not to extend the reach of its laws “to the full extent permitted.”\textsuperscript{182} Absent some legislative intent to the contrary, legislation is likewise presumed “to apply only within the territorial jurisdiction of the United States.”\textsuperscript{183}

Whether Congress has in fact exercised its legislative jurisdiction to extend the scope of American law to actions abroad is a question of statutory construction.\textsuperscript{184} If a plaintiff fails to show that Congress intended to reach extraterritorial conduct, the court does not dismiss the claim for want of subject matter jurisdiction.\textsuperscript{185} Rather, it either decides the claim, ruling on the merits that the plaintiff has failed to state a cause of action under the relevant statute,\textsuperscript{186} or dismisses on the basis of the plaintiff’s failure to establish statutory standing without reaching the merits.\textsuperscript{187}

\textsuperscript{180} Hartford, 509 U.S. at 813 (Scalia, J., dissenting); Restatement (Third) of the Foreign Relations Law of the United States § 401 & cmt. a; see EEOC, 499 U.S. at 253; see also Howard M. Wasserman, Jurisdiction and Merits, 80 Wash. L. Rev. 643, 684-85 (2005) (distinguishing “jurisdictional elements” which “are about congressional jurisdiction — substantive congressional constitutional power or authority — to regulate particular real-world conduct through legislation” from “judicial jurisdiction — judicial power or authority — to adjudicate a case or controversy between parties under that statute”).

\textsuperscript{181} Zoelsch v. Arthur Andersen & Co., 824 F.2d 27, 30 (D.C. Cir. 1987); Bersch, 519 F.2d at 985; Leasco, 468 F.2d at 1334; see EEOC, 499 U.S. at 248 (“Congress has the authority to enforce its laws beyond the territorial boundaries of the United States.”).

\textsuperscript{182} Bersch, 519 F.2d at 985; Leasco, 468 F.2d at 1334; see Steele v. Bulova Watch Co., 344 U.S. 280, 282-83 (1952); Zoelsch, 824 F.2d at 30.


\textsuperscript{184} Hartford, 509 U.S. at 813 (Scalia, J., dissenting); EEOC, 499 U.S. at 248; Steele, 344 U.S. at 282-83; see Litecubes, 523 F.3d at 1363.


\textsuperscript{186} See Steel, 523 U.S. at 89, 91-92; Hartford, 509 U.S. at 813 (Scalia, J., dissenting); Litecubes, 523 F.3d at 1363; United Phosphorus, Ltd. v. Angus Chem. Co., 322 F.3d 942, 955-59, 961-62 (7th Cir. 2003) (Wood, J., dissenting).

\textsuperscript{187} See Steel, 523 U.S. at 89, 92, 96-97; Warth v. Seldin, 422 U.S. 490, 500 (1975); see also Piper v. Chris-Craft Indus., Inc., 430 U.S. 1, 38 (1977); Kohen v. Pac. Inv.
Admittedly, the two concepts are related and often overlap. But neither is an issue that goes to a federal court's power to adjudicate — the sole inquiry of subject matter jurisdiction. While Judge Friendly felt constrained to follow established Second Circuit precedent addressing the issue as jurisdictional, as a matter of first principles, the extraterritoriality of the securities laws is decidedly not a question of the court's power to adjudicate. Indeed, the Supreme Court's recent decisions addressing the extraterritorial scope of the antitrust and patent laws do not treat extraterritoriality as a matter of subject matter jurisdiction. Instead, they view the question as a matter of statutory interpretation regarding whether Congress intended to exercise its legislative jurisdiction to the maximal extent permitted.

The Court's decisions predating Schoenbaum and Leasco do so as well.

In fact, the early Second Circuit cases addressing section 10(b) implicitly recognized that the issue of the statute's extraterritorial scope is a matter of legislative jurisdiction. For example, in Vencap, Judge Friendly observed that “[a]lthough the United States has power to prescribe the conduct of its nationals everywhere in the world, Congress does not often do so and courts are forced to interpret the statute at issue in the particular case.” Thus, “[r]esolution of the jurisdictional issue . . . depends on construction of exercised congressional power, not the limitations upon that power itself.”

Likewise, in Leasco, Judge Friendly invoked the concept of “jurisdiction to prescribe,” noting that it would be “erroneous to assume that the legislature always means to go to the full extent permitted” in exercising its power to extend its laws abroad. Thus, the extent of a statute's extraterritorial reach is a question of the

Mgmt. Co., 511 F.3d 672, 676-77 (7th Cir. 2009); cf. Arbaugh v. Y&H Corp., 546 U.S. 500, 516 (2006) (“[W]hen Congress does not rank a statutory limitation on coverage as jurisdictional, courts should treat the restriction as nonjurisdictional in character.”).

188 Steel, 523 U.S. at 89-93; Piper, 430 U.S at 24, 38.


190 Microsoft Corp. v. AT&T Corp., 550 U.S. 437, 455-56 (2007).

191 Id.; Empagran, 542 U.S. at 164.


194 Id. (quoting Steele, 344 U.S. at 282-83).

interpretation of the particular statute." And in Bersch, the court cited Leasco, similarly invoking the concept of jurisdiction to prescribe and stated that whether Congress intended for section 10(b) to apply to the maximum extent permitted by the due process clause is a question of statutory interpretation. Many other early cases similarly conflate the concept of legislative jurisdiction with the court's power to adjudicate.

These early cases performed precisely the “drive-by jurisdictional rulings” that the Supreme Court rejected in Arbaugh. Consequently, the label “subject matter jurisdiction” came to replace the legislative jurisdiction analysis that the courts were actually performing. With time, courts dropped any reference to prescriptive or legislative jurisdiction, and simply analyzed the issue as a question of subject matter jurisdiction.

Indeed, this is the analysis the Morrison court conducted in its dicta dismissing the defendant and amici’s invocation of Empagran and prescriptive comity, and it is also the analysis district courts apply when addressing whether foreign plaintiffs can

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196 Id.
197 Vencap, 519 F.2d at 985.
200 Zoelsch v. Arthur Andersen & Co., 824 F.2d 27, 29 (D.C. Cir. 1987), is a good example of this process. There, Judge Bork cited Leasco for the proposition that “Congress can, of course, prescribe the extent of federal jurisdiction over actions to enforce the federal securities laws, so long as it does not overstep the broad limits set by the due process clause.” Of course, Leasco used the term “prescribe” to mean legislative jurisdiction, not adjudicative jurisdiction, as Zoelsch did. 468 F.2d at 1334; see also Litecubes, LLC v. N. Light Prods., Inc., 523 F.3d 1353, 1363 (Fed. Cir. 2008) (“[T]here has been a particular tendency among courts and litigants to label limitations on the extraterritorial reach of a statute as ‘jurisdictional.’ ”).
201 See Morrison v. Nat'l Austl. Bank Ltd., 547 F.3d 167, 175 (2d Cir. 2008); SEC v. Berger, 322 F.3d 187, 193 (2d Cir. 2003); Kauthar SDN BHD v. Sternberg, 149 F.3d 659, 667 (7th Cir. 1998); Robinson v. TCI/US W. Commc'n's Inc., 117 F.3d 900, 905 (5th Cir. 1997); Itoba Ltd. v. Lep Group PLC, 54 F.3d 118, 122 (2d Cir. 1995); MCG, Inc. v. Great W. Energy Corp., 896 F.2d 170, 174-75 (5th Cir. 1990); Grunenthal GmbH v. Hotz, 712 F.2d 421 (9th Cir. 1983).
202 See Morrison, 547 F.3d at 175-76.
rely on the fraud-on-market presumption of reliance to satisfy the conduct test.\footnote{American plaintiffs are entitled to a rebuttable presumption of reliance so long as they can show that the shares they purchased or sold trade on an efficient market. See Basic Inc. v. Levinson, 485 U.S. 224, 246-47 (1988). Many district courts refuse to permit foreign plaintiffs to rely on the presumption in establishing direct causation under the conduct test because it would extend the application of American law too far. See \textit{In re AstraZeneca Sec. Litig.}, 559 F. Supp. 2d 453, 465-66 (S.D.N.Y. 2008); \textit{In re China Life Sec. Litig.}, No. 04 Civ. 2112 (TG), 2008 WL 4066919, at *9 (S.D.N.Y. Sept. 3, 2008); \textit{In re Bayer AG Sec. Litig.}, 423 F. Supp. 2d 105, 113 n.2 (S.D.N.Y. 2005); Burke v. China Aviation Oil (Singapore) Corp. Ltd., 421 F. Supp. 2d 649, 653 (S.D.N.Y. 2005); Tri-Star Farms Ltd. v. Marconi, PLC, 225 F. Supp. 2d 567, 578-79 (W.D. Pa. 2002); \textit{In re Baan Co. Sec. Litig.}, 103 F. Supp. 2d 1, 10 (D.D.C. 2000). However, while labeling their analysis jurisdictional, these courts perform a legislative jurisdiction analysis, declining to recognize the presumption of reliance because it is inconceivable that “Congress intended such a result.” \textit{Tri-Star}, 225 F. Supp. 2d at 579; see \textit{In re AstraZeneca}, 559 F. Supp. 2d at 466 (noting such result would extend reach of American law “too far”); \textit{In re Baan}, 103 F. Supp. 2d at 10 (same). For more discussion on the presumption of reliance, see Buxbaum, \textit{supra} note 1, at 26-41; Choi & Silberman, \textit{supra} note 5, at 477-88.}

As the foregoing makes clear, the extraterritorial scope of federal law is not properly deemed a question of subject matter jurisdiction. The real question is whether and to what extent Congress exercised its legislative jurisdiction. Guided by the principle of prescriptive comity as articulated most recently in \textit{Empagran}, the court “construes ambiguous statutes to avoid unreasonable interference with the sovereign authority of other nations” because Congress is presumed not to have intended to intrude upon the sovereign prerogatives of foreign nations.\footnote{F. Hoffmann-La Roche Ltd. v. Empagran S.A., 542 U.S. 155, 164 (2004); see also United States v. Aluminum Co. of Am., 148 F.2d 416, 443 (2d Cir. 1945).} In other words, prescriptive comity requires courts to “assume that legislators take account of the legitimate sovereign interests of other nations when they write American laws.”\footnote{\textit{Empagran}, 542 U.S. at 164.} However, unlike the statute that the Court analyzed in \textit{Empagran}, where Congress in fact addressed the issue of extraterritoriality, albeit ambiguously, Congress not only was silent as to section 10(b)’s extraterritorial scope, but also never actually “wrote” a law creating a private Rule 10b-5 cause of action. Indeed, the private Rule 10b-5 cause of action is entirely a creature of judicial creation.\footnote{See Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, 552 U.S. 148, 163-64 (2008); Musick, Peeler & Garrett v. Employers Ins. of Wausau, 508 U.S. 286, 294 (1993); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 737 (1975).} In this sense, Congress was doubly silent about the extraterritorial reach of
the securities laws. Thus, the prescriptive comity canon of construction only goes so far in the securities context.

B. Determining the Scope of the Rule 10b-5 Implied Cause of Action

Crafting an appropriate analytical framework addressing the extraterritorial scope of the securities laws requires examining another related body of law — the Supreme Court’s treatment of implied rights of action generally and the Rule 10b-5 cause of action specifically. The first, more general inquiry focuses on whether the text, structure, purpose, and legislative history of a specific statute permit inferring an implied right of action, focusing on legislative intent.207 The second, more specific inquiry, seeks to define “the contours of”208 the Rule 10b-5 cause of action by, in the Court’s words, “attempt[ing] to infer how the 1934 Congress would have addressed the issue had the Rule 10b-5 action been included as an express provision in the 1934 Act.”209

If the inquiry seems familiar, it should be. It is precisely the inquiry the federal appellate courts undertake when analyzing the extraterritorial reach of the securities laws under the guise of subject matter jurisdiction.210 Yet the Supreme Court has never analyzed the scope of implied rights of action as a question of jurisdiction. Instead, as with the legislative jurisdiction analysis, the Court refers to the analysis as either a question of statutory standing to sue211 or a question of the merits.212 The distinction is not merely a theoretical exercise. Its resolution determines whether a court can dismiss a case early in the proceedings or must wait until after discovery or even trial to dismiss the case,213 and therefore drastically affects the costs and benefits of Rule 10b-5 litigation and whether private enforcement of alleged Rule 10b-5 violations achieves optimal deterrence.214 As the

209 Musick, 508 U.S. at 294.
210 Compare Musick, 508 U.S. at 294 (“[C]ourt attempt[s] to infer how the 1934 Congress would have addressed the issue had the 10b-5 action been included as an express provision in the 1934 Act.”), with Bersch v. Drexel Firestone, Inc., 519 F.2d 974, 993 (2d Cir. 1975) (basing jurisdiction on court’s “best judgment as to what Congress would have wished if these problems had occurred to it”).
213 See discussion infra Part IV.
following discussion shows, the most appropriate treatment of the subject is under the rubric of statutory standing.

1. Cort v. Ash and Implied Rights of Action Generally

Historically, the Supreme Court has readily implied private rights of action where a statute is silent on the issue.\(^{215}\) This view reached its most generous expression in \textit{J.I. Case Co. v. Borak},\(^{216}\) where the Court held that “it is the duty of the courts to be alert to provide such remedies as are necessary to make effective the congressional purpose” expressed by a statute.\(^{217}\) The Court abandoned that understanding of implied rights in \textit{Cort v. Ash},\(^{218}\) articulating instead a four-part test focusing on congressional intent to “especial[ly] benefit” a particular class of plaintiffs,\(^{219}\) but also examining whether an implied federal right would conflict with existing state causes of action.\(^{220}\) Thus, in order to determine whether a private remedy is implicit in a statute not expressly providing one, courts consider (1) whether the plaintiff “is one of the class for whose especial benefit the statute was enacted”; (2) whether legislative intent, explicit or implicit, supports creating or denying an implied remedy; (3) whether implying a remedy is consistent with the underlying purposes of the legislative scheme; and (4) whether the putative cause of action is one traditionally relegated to state law, in an area basically the concern of the States, such that “it would be inappropriate to infer a cause of action based solely on federal law.”\(^{221}\)

In subsequent cases, the Court has emphasized the inquiry’s focus on Congress’s intent.\(^{222}\) Thus, where Congress has not expressly indicated whether private plaintiffs may sue under a statute, courts are tasked with interpreting the statute “to determine whether it displays

\(^{215}\) Alexander, 532 U.S. at 287 (discussing J.I. Case Co. v. Borak, 377 U.S. 426, 433 (1964)).
\(^{216}\) 377 U.S. 426, 433 (1964).
\(^{217}\) Id.
\(^{218}\) 422 U.S. 66, 67 (1975).
\(^{219}\) Id. at 78.
\(^{221}\) Cort, 422 U.S. at 78 (citations omitted).
an intent to create not just a private right but also a private remedy.”223 The inquiry seeks to divine statutory intent, focusing on the text, structure, purpose, and if necessary, the legislative history of the relevant statute.224 Absent evidence of an intent to create a private remedy, “a cause of action does not exist and courts may not create one, no matter how desirable that might be as a policy matter, or how compatible with the statute.”225

2. The Contours of the Rule 10b-5 Implied Right of Action

The implied rights analysis answers the question of whether a statute implicitly provides a cause of action. That is a question addressing the merits of the case — the existence of a valid cause of action — and therefore courts dismiss on the basis of a failure to state a claim where the relevant statute does not support an implied cause of action.226 But that is only half the inquiry for section 10(b) and Rule 10b-5 purposes, as the Supreme Court has already affirmed the lower courts' creation of an implied right of action under Rule 10b-5.227 The other question is the scope of the implied right. Put another way, while the Court has accepted the proposition that section 10(b) and Rule 10b-5 imply a general antifraud cause of action, the class of plaintiffs that may invoke the implied right of action remains an open and evolving question. As the Court has made clear, unlike the question of whether an implied right exists at all, the question of who specifically may invoke that right is a matter of statutory standing.228

223 *Alexander*, 532 U.S. at 286; *see also* Gonzaga Univ. v. Doe, 536 U.S. 273, 283-84 (2002) (“[T]he question whether Congress intended to create a private right of action is definitively answered in the negative where a statute by its terms grants no private rights to any identifiable class. For a statute to create such private rights, its text must be phrased in terms of the persons benefited.”) (citations, internal quotation marks, and alteration marks in original omitted).
224 *Alexander*, 532 U.S. at 286; *Touche*, 442 U.S. at 578.
225 *Alexander*, 532 U.S. at 286-87; *see Touche*, 442 U.S. at 575-76; *Cort*, 422 U.S. at 78.
226 *Alexander*, 532 U.S. at 286; *Steel Co. v. Citizens for a Better Env’t*, 523 U.S. 83, 89-97, 97 n.2 (1998); *see Touche*, 442 U.S. at 568.
228 *Steel*, 523 U.S. at 89-97, 97 n.2 (distinguishing question of “whether this plaintiff has a cause of action under [a] statute” from the “question whether any plaintiff has a cause of action,” and labeling former statutory standing question and latter merits question); *see Stoneridge*, 552 U.S. at 165-66 (framing scope of 10b-5 inquiry as “determination of who can seek a remedy,” rather than determination of whether any remedy exists at all).
The Court’s analysis of the question of who may sue under Rule 10b-5 mirrors the analysis that courts undertake under the conduct test. As with the conduct test, the Rule 10b-5 right and its contours are entirely a judicial creation.229 Likewise the Court concedes that it cannot “divine from the language of § 10(b) the express ‘intent of Congress’ as to the contours of a private cause of action under Rule 10b-5.”230 However, because the Court has implied the private right of action, and because Congress has not intervened,231 the courts have retained primary responsibility for delimiting the contours of the Rule 10b-5 cause of action.232 In defining those contours, the court’s task is to “attempt to infer how the 1934 Congress would have addressed the issue had the 10b-5 action been included as an express provision in the 1934 Act.”233 That inquiry, in turn, is guided by Congress’s objectives in enacting the securities laws, such that the court may not expand the scope of a right where doing so “detracts from the effectiveness of the 10b-5 implied action or interferes with the effective operation of the securities laws.”234

The chief means of inferring congressional intent is by comparing section 10(b) to other provisions of the 1934 Act, particularly those that provide express causes of action,235 as well as to sections of the 1933 Securities Act, a legislative companion to the 1934 Act which

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229 Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 737 (1975) (“[W]e deal with a judicial oak which has grown from little more than a legislative acorn.”).
231 Musick, 508 U.S. at 292-93; Va. Bankshares, Inc. v. Sandberg, 501 U.S. 1083, 1104-05 (1991); see Blue Chip Stamps, 421 U.S. at 749 (stating that Rule 10b-5 right must be “judicially delimited one way or another unless and until Congress” gets around to it).
232 Musick, 508 U.S. at 292 (“[T]o now disavow any authority to allocate it on the theory that Congress has not addressed the issue would be most unfair to those against whom damages are assessed.”).
234 Musick, 508 U.S. at 298; id. at 295 (“[O]ur goals in establishing limits for the 10b-5 action have remained the same: to ensure the action does not conflict with Congress’ own express rights of action, to promote clarity, consistency, and coherence for those who rely upon, or are subject to, 10b-5 liability, and to effect Congress’ objectives in enacting the securities laws.”); see Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 477 (1977) (“[A] private cause of action under the antifraud provisions of the Securities Exchange Act should not be implied where it is ‘unnecessary to ensure the fulfillment of Congress’ purposes’ in adopting that Act.”).
governs the registration of securities for sale and requires certain disclosures prior to sale. Indeed, the Court has emphasized this mode of interpretation over others because of the need to “ensure that the rules established to govern the 10b-5 action are symmetrical and consistent with the overall structure of the 1934 Act and, in particular, with those portions of the 1934 Act most analogous to the private 10b-5 right of action that is of judicial creation.” Where extending the implied right of action would conflict with an express provision of the Act, the express provision takes precedence, and the extension of the implied right must be rejected.

The Court routinely frames the inquiry in terms of whether Congress, if it had expressly legislated a private right of action, would have intended for certain plaintiffs to be able to invoke that right. For example, in Blue Chip Stamps v. Manor Drug Stores, the Court addressed whether Congress would have wished to provide a remedy under Rule 10b-5 to stockholders who did not purchase or sell their stocks in connection with alleged fraud. The Court observed that because Congress had not spoken on the issue expressly, it was appropriate to rely on “policy considerations” when articulating the scope of the 10b-5 right. Invoking those considerations, the Court reasoned that standing under Rule 10b-5 should be limited to purchasers or sellers because “a widely expanded class of plaintiffs under Rule 10b-5” would raise the specter of “vexatious litigation” by

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237 Musick, 508 U.S. at 294. The Court has observed that Sections 9 and 18 of the 1934 Act are analogous to Section 10(b), as both sections “target the precise dangers that are the focus of § 10(b), and the intent motivating all three sections is the same — to deter fraud and manipulative practices in the securities markets, and to ensure full disclosure of information material to investment decisions.” Id. at 296 (citations omitted).
238 Stoneridge, 552 U.S. at 161-63; Central Bank, 511 U.S. at 180; Musick, 508 U.S. at 297; cf. Alexander, 532 U.S. at 290 (“The express provision of one method of enforcing a substantive rule suggests that Congress intended to preclude others.”).
239 Stoneridge, 552 U.S. at 165-66 (framing Rule 10b-5 inquiry as “determination of who can seek a remedy”); Central Bank, 511 U.S. at 180 (asking whether Congress intended “to expand the plaintiff class” who may invoke Rule 10b-5); Va. Bankshares, 501 U.S. at 1099 (analyzing “the class of plaintiffs eligible to sue under § 14(a)’”); Piper v. Chris-Craft Indus., Inc., 430 U.S. 1, 38 (1977) (analyzing implied right under Section 14(e) as question of standing, and asking whether “Congress intended standing under § 14(e) to encompass tender offerors’); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 740 (1975) (analyzing effects of “widely expanded class of plaintiffs under Rule 10b-5”).
240 421 U.S. 723.
241 Id. at 728.
242 Id. at 737.
encouraging speculative claims and creating procedural intractability.\textsuperscript{243} Accordingly, mere holders, rather than purchasers or sellers, lack standing to sue under Rule 10b-5.\textsuperscript{244}

The Court’s more recent treatment of implied causes of action under the 1934 Act confirms that standing is the correct analytical rubric. In \textit{Virginia Bankshares, Inc. v. Sandberg},\textsuperscript{245} the Court addressed whether minority shareholders could invoke the implied right of action under section 14(a) of the 1934 Act as a basis for challenging a shareholder vote.\textsuperscript{246} Plaintiffs in that case alleged that proxy statements on which they relied in voting in favor of a proposed merger contained fraudulent misrepresentations.\textsuperscript{247} The Court understood its inquiry as “defin[ing] the class of plaintiffs eligible to sue under § 14(a).”\textsuperscript{248} That inquiry in turn required the Court to determine whether the facts alleged, as a matter of law, could satisfy the causation requirements of a section 14(a) claim, namely whether plaintiffs could establish “a chain of causal connection in which the proxy statement is claimed to have been an ‘essential link’ ” in securing “votes legally required to authorize the action proposed.”\textsuperscript{249} Invoking \textit{Blue Chip Stamps}'s policy concerns, the Court reasoned that “expand[ing] the class of plaintiffs entitled to bring” a section 14(a) claim to include those relying on the plaintiffs’ “hazy” theory of causation would encourage “speculative claims and procedural intractability.”\textsuperscript{250} Accordingly, the Court held that the plaintiffs were not among the class of plaintiffs the section 14(a) implied right of action was intended to benefit.\textsuperscript{251}

Applying a similar analysis in \textit{Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.},\textsuperscript{252} the Court addressed whether plaintiffs could allege an aiding and abetting cause of action under Rule 10b-5. Relying on the statutory text, the Court held that section

\textsuperscript{243} Id. at 740.
\textsuperscript{244} Id. at 755.
\textsuperscript{247} Va. Bankshares, 501 U.S. at 1097-98. The minority shareholders’ votes were not required by law or corporate bylaw. Id. at 1099.
\textsuperscript{248} Id.
\textsuperscript{249} Id. at 1102.
\textsuperscript{250} Id. at 1102, 1103.
\textsuperscript{251} Id. at 1107-08.
\textsuperscript{252} 511 U.S. 164 (1994).
10(b) did not permit plaintiffs to sue under an aiding and abetting theory.253 However, in dicta, the Court also analyzed the issue, assuming that the statute did not resolve it explicitly.254 Observing that none of the express causes of action under the 1933 and 1934 Acts permitted aiding and abetting liability, the Court reasoned that Congress would therefore not have provided for aiding and abetting liability under section 10(b) had it provided an express cause of action.255 According to the Court, it would be “anomalous to impute to Congress an intention to expand the plaintiff class for a judicially implied cause of action beyond the bounds it delineated for comparable express causes of action,” particularly where to do so would permit suit by a class of plaintiffs who could not as, a matter of law, show reliance on the aider and abettor’s statements.256

The Court again addressed the scope of Rule 10b-5 and aiding and abetting liability in Stoneridge Investment Partners, LLC v. Scientific-Atlanta.257 Noting that Congress had amended the 1934 Act to permit the SEC — but not private plaintiffs — to enforce section 10(b) against aiders and abettors, the Court rejected plaintiffs’ aiding and abetting claim under Rule 10b-5, holding that plaintiffs could not show reliance.258 The Court then addressed the plaintiffs’ argument that aiders and abettors could be held liable as primary violators because their misrepresentations to the issuer caused the issuer to make misrepresentations to the public.259 The Court rejected the argument for similar reasons — a failure to allege causation — and further noted that permitting the plaintiffs to “seek a remedy” would undermine congressional intent in amending the 1934 Act.260 Indeed, the Court retreated from its earlier holdings that the Court retained power to shape the contours of Rule 10b-5 causes of action, holding instead that “[t]he decision to extend the cause of action is for Congress, not for us,” and that therefore the class of plaintiffs who may invoke Rule 10b-5 “should not be extended beyond its present boundaries.”261

253 Id. at 173-78.
254 Id. at 178.
255 Id. at 179-80.
256 Id. at 180.
258 Id. at 156.
259 Id. at 157-58. The Court referred to this as “scheme liability.” Id. at 159.
260 Id. at 160.
261 Id. The Court went so far as to suggest that the scope of Rule 10b-5 may not be expanded beyond its contours in 1995, when Congress amended the 1934 Act. See id. ("It is appropriate for us to assume that when § 78u-4 was enacted, Congress accepted..."
III. APPLYING THE EXTRATERRITORIALITY AS STANDING FRAMEWORK

As the foregoing demonstrates, the Supreme Court addresses the scope of the implied right of action under section 10(b) and Rule 10b-5 as a question of statutory standing and addresses the extraterritorial application of federal law as a question of legislative jurisdiction and prescriptive comity. Both ask, much like the conduct test, what Congress would have done had it expressly contemplated the issue, and both provide tools of interpretation meant to divine congressional intent. Taken together, the two related doctrines of legislative jurisdiction and implied rights provide a simple framework for addressing the extraterritorial scope of the securities laws as a question of standing.

Although the Court now emphasizes congressional intent over other factors discussed in *Cort*, the case provides a workable template for foreign-cubed standing analysis. Recall that *Cort* articulated a four-part test for determining whether a statute provides an implied cause of action, focusing on statutory purpose and whether the implied cause would conflict with existing state law. The legislative purpose inquiry outlined in *Cort* is precisely the analysis the Court applies to Rule 10b-5 standing questions. Thus, the Court looks to legislative text, structure, purpose, and if necessary, legislative history, to determine how the 1934 Congress would have delimited the scope of the Rule 10b-5 implied cause of action had it legislated an express cause of action.

While less obvious, *Cort*’s reference to state law tracks the legislative jurisdiction analysis. In *Cort*, the Court cautioned that implying a cause of action may be inappropriate if the “cause of action [is] one traditionally relegated to state law, in an area basically the concern of the States.” *Cort*’s concern for preexisting state remedies can be viewed as a version of the statutory presumption, oft-repeated by the Supreme Court, that absent an express intent to the contrary, Congress is presumed not to preempt state law causes of action.

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265 Cort, 422 U.S. at 78.
Extraterritoriality as Standing

2010

Seen in that light, Cort's fourth factor is analogous to Empagran's “prescriptive comity” rule of construction. That is, just as Congress is presumed not to intrude upon state prerogatives, absent a showing of contrary congressional intent, Congress is also presumed not to intrude on the legitimate sovereign interests of other nations, absent some indication to the contrary.267

Cort, as modified by Empagran, Musick, and Central Bank, provides the analytical framework for foreign-cubed standing. As with the conduct test, the Court must determine what the 1934 Congress would have done had it thought about the issue. That inquiry focuses on the 1934 Act's legislative purpose,268 as dictated by its text, structure, and legislative history.269 Absent contrary congressional intent, the statutory canon of prescriptive comity cabins that purpose, such that the Act cannot be read to unreasonably intrude upon the sovereign prerogatives of foreign countries.270 Distilled to its core, the inquiry simply asks whether the plaintiff alleges an injury that the securities laws are designed to remedy.271

As the remainder of this Part demonstrates, this analysis does not permit a cause of action where the conduct test would. Rather, the standing inquiry advocated here tracks the effects test as originally articulated in Schoenbaum.272 Thus, a foreign-cubed plaintiff only has standing to sue where he or she alleges an effect on American investors or markets. For foreign investors, that effect must involve the purchase or sale of shares within the United States. This approach has significant procedural advantages over the jurisdictional approach currently applied by the federal courts.

A. The 1934 Act's Legislative Purpose

As discussed, the text of the 1934 Act is silent as to its extraterritorial reach. A single passage addresses foreign transactions explicitly. Section 30(b) states that the 1934 Act does not apply to “any person” who “transacts a business in securities without the jurisdiction of the United States.”273 The courts have read this on its

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269 Musick, 506 U.S. at 204; Cort, 422 U.S. at 78.
270 Empagran, 542 U.S. at 164-75.
271 Of course, the Court would still apply Blue Chip Stamps's purchaser-seller standing rule. See Dabit, 547 U.S. at 84-88.
272 Schoenbaum v. Firstbrook, 405 F.2d 200, 206-07 (2d Cir. 1968).
273 15 U.S.C. § 78dd(b) (2006). That statute also grants the SEC the power to issue
face, reasoning that it applies to broker-dealers and allows them to buy or sell securities abroad without having to make the same disclosures as an issuer. Beyond this, the text makes no express reference to extraterritoriality.

Although courts analyzing the extraterritorial scope of the securities laws have invoked policy rationales found nowhere in the text or legislative history of the 1933 and 1934 Acts, the Supreme Court has never endorsed these rationales. Rather, the Court has held that the 1933 and 1934 Acts serve two fundamental, general purposes. First, the 1934 Act was “intended principally to protect investors against manipulation of stock prices through regulation of transactions upon securities exchanges and in over-the-counter markets, and to impose regular reporting requirements on companies whose stock is listed on national securities exchanges.” Second, the 1933 Act “was designed to provide investors with full disclosure of material information concerning public offerings of securities in commerce, to protect investors against fraud and, through the imposition of specified civil liabilities, to promote ethical standards of honesty and fair dealing.” These purposes focus on American markets and investors. Indeed, many courts applying the conduct and effects tests readily concede

regulations governing these transactions if “necessary or appropriate to prevent the evasion of this chapter.” Id. The SEC has not issued any regulations under this subsection.

274 Kauthar SDN BHD v. Sternberg, 149 F.3d 659, 664 (7th Cir. 1998); Robinson v. TCI/US W. Commc’ns, Inc., 117 F.3d 900, 904-05 (5th Cir. 1997); Zoelsch v. Anderson & Co., 824 F.2d 27, 30 (D.C. Cir. 1987); Schoenbaum, 405 F.2d at 206.

275 See supra notes 51-58 and accompanying text.


277 Ernst, 425 U.S. at 195 (citing H.R. REP. NO. 73-85, at 1-5 (1933)); see Herman & MacLean v. Huddleston, 499 U.S. 373, 388-89 (1983); SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186 (1963). It is important to note that while cases like Kasser have suggested that the 1934 Act was intended to promote “high standards of conduct,” see discussion supra notes 114-19 and accompanying text, the Court here articulated this “honesty and fair dealing” rationale in the context of the 1933 Act.

278 Ernst, 425 U.S. at 195; Robinson, 117 F.3d at 906; Zoelsch, 824 F.2d at 31; Des Brisay v. Goldfield Corp., 549 F.2d 133, 135 (9th Cir. 1977); Schoenbaum, 405 F.2d at 206; cf. Interbrew v. Edperbrascan Corp., 23 F. Supp. 2d 425, 429 (S.D.N.Y. 1998) (“A proper analysis should focus on the policy considerations that led to the extraterritorial application of these laws in the first place — protecting or punishing U.S.-parties and markets.”).
that the legislative history of the 1934 Act evinces a clear purpose of protecting American investors and markets.\textsuperscript{279}

Although courts of appeals have considered the 1934 Act’s legislative history barren on the subject of extraterritoriality, suggesting that Congress could not have foreseen the globalization of securities markets,\textsuperscript{280} in truth, the legislative history suggests Congress knew about foreign markets and investors, but excluded them from the Act’s coverage anyway.\textsuperscript{281} Several sections of the legislative history bear this out. First, section 30(b)’s legislative history strongly suggests that Congress intended to cover only American investors and markets.\textsuperscript{282} As the Second Circuit observed in Schoenbaum and Leasco, section 30 was “intended to prevent evasion of the Act through transactions on foreign exchanges”\textsuperscript{283} and was driven by the fear, articulated by the bill’s principal draftsman, that the 1934 Act’s “enactment would drive American securities to foreign exchanges.”\textsuperscript{284} Accordingly, as the Schoenbaum court observed, section 30 grants the SEC the power to issue rules and regulations governing conduct abroad when “necessary to prevent the evasion of the domestic regulatory scheme.”\textsuperscript{285} Section 30 therefore contemplates jurisdiction in SEC actions over American

\textsuperscript{279} See Robinson, 117 F.3d at 906; Zoelsch, 824 F.2d at 31 (citing Des Brisay, 549 F.2d at 135, S. REP. NO. 792, at 1-13 (1934), and H.R. REP. NO. 1383, at 1-16 (1934)); Leasco Data Processing Equip. v. Maxwell, 468 F.2d 1326, 1336-37 (2d Cir. 1972); Schoenbaum, 405 F.2d at 206 (citing H.R. REP. NO. 1383 (1934), 78 CONG. REC. 7922 (1934) (statement of Rep. Hapes), and 78 CONG. REC. 7861 (1934) (statement of Rep. Lea)).

\textsuperscript{280} See Zoelsch, 824 F.2d at 30; Bersch v. Drexel Firestone, Inc., 519 F.2d 974, 993 (2d Cir. 1975).

\textsuperscript{281} See James D. Cox et al., Securities Regulation 1201 n.1 (2d ed. 1997) (noting that “most of the capital used to fund last century’s railroad expansion in the United States came from bonds floated in Europe”). See generally Margaret V. Sachs, The International Reach of Rule 10b-5: The Myth of Congressional Silence, 28 Colum. J. Transnat’l L. 677, 677-712 (1990) (“[T]he securities markets of the 1920’s were highly international, as Congress was well aware when it enacted the 1933 and 1934 Acts. . . . Congress nevertheless chose to protect only those investors whose trades occur inside the United States — ‘domestic traders’ — regardless of whether the securities traded are domestic or foreign.”).

\textsuperscript{282} See Zoelsch, 824 F.2d at 32; Leasco, 468 F.2d at 1336 n.6; Schoenbaum, 405 F.2d at 207-08.

\textsuperscript{283} Schoenbaum, 405 F.2d at 207 (citing Hearings on S. Res. 89, and S. Res. 56 and S. Res. 97 Before the S. Comm. on Banking and Currency, 73d Cong. 6569, 6578-79 (1934)).

\textsuperscript{284} Leasco, 468 F.2d at 1336 n.6 (citing Hearings on S. Res. 84 and S. Res. 97 Before the S. Comm. on Banking and Currency, 73d Cong. 6569, 6578-79 (1934)).

\textsuperscript{285} Schoenbaum, 405 F.2d at 207; see Zoelsch, 824 F.2d at 32 (stating same); see also 15 U.S.C. § 78dd(a) (2006).
issuers should they try to avoid the 1934 Act's reporting requirements by issuing their shares abroad,\textsuperscript{286} which suggests, as Judge Bork observed in Zoelsch, that “Congress was concerned with extraterritorial transactions only if they were part of a plan to harm American investors or markets.”\textsuperscript{287} Likewise, the express reference to foreign exchanges and the domestic regulatory scheme shows that the 1934 Act's drafters plainly contemplated foreign exchanges, but chose to leave them outside the ambit of the 1934 Act.\textsuperscript{288}

In addition to explaining the purpose of section 30, the legislative history repeatedly emphasizes the need to protect the American public and American markets from worthless foreign and domestic securities.\textsuperscript{289} Conversely, in the sole instance where the legislative history mentions foreign traders, it expressly distinguishes them from American traders.\textsuperscript{290} Relatedly, the legislative history makes clear what Congress meant when it defined “interstate commerce,” as used in the 1933 and 1934 Acts, to mean commerce between states and “between

\textsuperscript{286}  Leasco, 468 F.2d at 1336 n.6 (citing Hearings on S. Res. 84 and S. Rec. 56 and S. Res. 97 before the S. Comm. on Banking and Currency, 73d Cong. 6569, 6578-79 (1934)).

\textsuperscript{287}  Zoelsch, 824 F.3d at 32.

\textsuperscript{288}  See id.; Leasco, 468 F.2d at 1336 n.6; Schoenbaum, 405 F.2d at 207-08.

\textsuperscript{289}  See Sachs, supra note 281, at 693-96 (discussing Hearings on H.R. 7852 and H.R. 8720 Before the H. Interstate and Foreign Commerce Comm., 73d Cong. 1st Sess. (1934), reprinted in 2 LEGISLATIVE HISTORY OF THE SECURITIES ACT OF 1933 AND SECURITIES EXCHANGE ACT OF 1934, item 20, at 85 (1973), S. REP. NO. 73-1445 (1933), S. REP. No. 73-47 (1934), and 77 CONG. REC. 2951-52 (1933)).

\textsuperscript{290}  Id. In colloquy with a Commerce Department official during hearings on the 1933 Act, Representative Wolverton suggested the Act was intended to protect Americans from the sale of foreign securities in America, and not intended to protect foreign purchasers of American securities abroad:

REP. WOLVERTON: Suppose there is a security . . . here in America, and there is a desire to float them in France or England. Could . . . you . . . tell what the modus operandi would be to get that stock on the market over there, and whether there is any provision of law in those countries that would prevent the free sale of such over [t]here?

COMMERCE DEPARTMENT OFFICIAL: It would have to be sold through one of the 5 or 6 houses over there, which act as distributors for the whole country. As I understand it, those few houses of issue, or bond houses, are controlled informally by the British Government. . . .

REP. WOLVERTON: Maybe this is only academic, as to our securities over there. The great danger is from foreign securities over here. I am trying to provide against that danger.

any foreign country and any State.” 291 The early versions of the 1933 Act defined “interstate commerce” without reference to foreign countries, 292 and discussions between Congressmen and the bill’s drafters indicated that this was because the 1933 Act was limited to the U.S. and its territories. 293 The language “between any foreign country and any State” was subsequently inserted into the Act in response to Representative Wolverton’s concern that the absence of such language would jeopardize statutory coverage of foreign securities trading in the United States. 294 Subsequent 1933 Act bills overwhelmingly defined “interstate commerce” to include commerce “between any foreign country and any State” for this reason, 295 as did

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293 2 LEGISLATIVE HISTORY, supra note 292, item 20, at 54-55, 210-11, 220; Sachs, supra note 281, at 700-01.

294 2 LEGISLATIVE HISTORY, supra note 292, item 20, at 210-11, 220; Sachs, supra note 281, at 700-01.

295 See Sachs, supra note 281, at 700-01 (citing H.R. 5480, 73d Cong. (1st Sess. 1933) (introduced May 10, 1933), reprinted in 3 LEGISLATIVE HISTORY, supra note 292, item 27, at 41; H.R. 5480, 73d Cong. (1st Sess. 1933) (introduced May 3, 1933), reprinted in 3 LEGISLATIVE HISTORY, supra note 292, item 26, at 4; H.R. 5480, 73d Cong. (1st Sess. 1933) (introduced May 4, 1933), reprinted in 3 LEGISLATIVE HISTORY, supra note 292, item 25, at 4; H.R. 5480, 73d Cong. (1st Sess. 1933) (introduced May 3, 1933), reprinted in 3 LEGISLATIVE HISTORY, supra note 292, item 24, at 4; and S. REP. NO. 73-47 (1933), reprinted in 3 LEGISLATIVE HISTORY, supra note 292, item 29, at 31 (Apr. 27, 1933)); see also H.R. 4500, 73d Cong. (1st Sess. 1933) (introduced Mar. 30, 1933), reprinted in 3 LEGISLATIVE HISTORY, supra note 292, item 23, at 5 (defining “trade or sale of securities in interstate commerce” to include “trading or dealing in, in any State or Territory of the United States, any securities issued in another State or in a foreign country”).
the 1933\textsuperscript{296} and 1934\textsuperscript{297} Acts, as enacted. Thus, to the extent the legislative history provides any evidence of congressional intent, it shows that Congress chose to protect only American markets and investors.\textsuperscript{298}

Beyond demonstrating the 1934 Act’s focus on American investors and markets, the legislative history also suggests that Congress intended for section 30(b) to ensure that American securities laws did not interfere with foreign markets or investors. As the Second Circuit in \textit{Schoenbaum} observed after reviewing the Act’s legislative history, section 30 is “designed to take the Commission out of the business of regulating foreign security exchanges unless the Commission deems regulation necessary to prevent evasion of the domestic regulatory scheme.”\textsuperscript{299} Put another way, section 30(b) serves as a dividing line between domestic and foreign issuers, “releiv[ing] the Commission of the impossible task of enforcing American securities law upon persons whom it could not subject to the sanctions of the Act for actions upon which it could not bring its investigatory powers to bear.”\textsuperscript{300} Thus, some seventy years before the Supreme Court’s decision in \textit{Empagran}, section 30(b) functions as a built-in prescriptive comity mechanism\textsuperscript{301}, placing the responsibility of regulating foreign securities in the hands of the SEC, where, as the \textit{Zoelsch} court noted, such “extraterritorial transactions . . . were part of a plan to harm American investors or markets.”\textsuperscript{302}

\textsuperscript{296} See Sachs, \textit{supra} note 281, at 699-701.


\textsuperscript{298} For further analysis of the legislative history, see Sachs, \textit{supra} note 281, at 689-708.

\textsuperscript{299} Schoenbaum v. Firstbrook, 405 F.2d 200, 207 (2d Cir. 1968).

\textsuperscript{300} Id. at 207-08.


\textsuperscript{302} Zoelsch v. Anderson & Co., 824 F.2d 27, 32 (D. Cir. 1987). Indeed, it would be rather bizarre to recognize that section 30(b) excludes foreign markets and investors from the SEC’s regulatory scope, but at the same time somehow permits foreign plaintiffs to sue in American courts alleging foreign misrepresentations. Such a result provides private plaintiffs more regulatory power than the SEC itself.
Indeed, at least one other express provision of the securities laws supports reading section 30(b) as a prescriptive comity mechanism. The Foreign Bondholders Act, enacted as Title II of the 1933 Act, established a process by which the President could create an independent governmental corporation empowered to negotiate and sue on behalf of American “holders of defaulted foreign securities issued, sold or owned in the United States.” Thus, rather than establish a private right of action for U.S.-based holders of foreign securities, Congress expressly contemplated an administrative body that, like the SEC under section 30(b), would be better situated to balance comity concerns with the needs of private compensation.

The existence of section 30(b) of the 1934 Act and Title II of the 1933 Act, both express provisions establishing administrative bodies whose responsibilities include regulating foreign issuers and pursuing claims on behalf of American holders of foreign issuers where an effect on American markets or investors is realized, strongly suggests that the 1934 Congress did not intend a private right of action reaching the same. In the Court’s words, “[T]he express provision of one method of enforcing a substantive rule suggests that Congress intended to preclude others,” particularly where granting private plaintiffs standing “would undermine Congress’ determination that [a] class of defendants should be pursued by the SEC and not by private litigants.”

At a minimum, then, the text, structure, and legislative history of the 1933 and 1934 Acts not only show that Congress was concerned with American investors and markets, but also that where foreign issuers affected American investors or markets in some way, Congress intended for administrative agencies, rather than private litigants, to enforce the securities laws. The 1934 Act, contrary to years of federal court holdings, is therefore decidedly not silent as to whether Congress intended to provide a cause of action for foreign-cubed plaintiffs.

B. Rule 10b-5 Policy Considerations and Empagran

The failure of the text, structure, and legislative history to show a congressional intent to create a cause of action for foreign-cubed plaintiffs should end the inquiry. However, the Court’s recent Rule
10b-5 case law and the fourth Cort factor, as modified by Empagran, provide further compelling reasons for limiting the class of plaintiffs who can sue under a Rule 10b-5 cause of action to plaintiffs who can allege an injury that the securities laws are designed to remedy, meaning an injury to American investors or markets.

The Supreme Court’s Rule 10b-5 case law provides that in addition to determining whether the 1934 Congress would have extended standing to foreign-cubed plaintiffs by examining the 1934 Act’s text, structure, and history, courts should also look to “policy considerations” in determining the scope of the Rule 10b-5 cause of action. In doing so, courts should focus on whether “a widely expanded class of plaintiffs under Rule 10b-5” would conflict with the overall “effective operation of the securities laws,” whose purpose is to protect American investors and markets. Under this policy analysis, expanding or limiting the class of plaintiffs who may invoke the Rule 10b-5 right of action depends on whether that expansion or limitation enhances U.S. investor welfare and the strength of American markets. The focus is on deterrence and the practical consequences of extending or limiting Rule 10b-5 standing.

1. Deterrence

The deterrence question primarily focuses on the effectiveness of private litigation, particularly class action litigation, as a means of deterring fraud. Under an effects-based standing framework, incentives to sue will depend on the size of the effect of fraud in the United States — the larger the U.S. effect, the greater the likelihood that private plaintiffs’ attorneys will file a class-action lawsuit to directly enforce the interests of investors trading in the United States. Indeed, because private plaintiffs’ attorneys are profit-motivated, they

307 Id. at 740.
308 Musick, Peeler & Garrett v. Employers Ins. of Wausau, 508 U.S. 286, 298 (1993); see also James Keenley, Comment, How Many Injuries Does It Take?: Article III Standing in the Class Action, 95 CAL. L. REV. 849, 851-52, 873-74 (2007) (arguing that it is particularly appropriate to consider class standing before jurisdiction in securities context).
309 See Stoneridge, 552 U.S. at 163-64; Choi & Silberman, supra note 5, at 492.
310 See Stoneridge, 552 U.S. at 163-64; Blue Chip Stamps, 421 U.S. at 737-40; Choi & Silberman, supra note 5, at 492.
311 See Choi & Silberman, supra note 5, at 490.
will only file suit where the expected benefits outweigh the costs. The presence of a subset of plaintiffs harmed in connection with the purchase or sale of stock in the United States in any class will encourage suit, although admittedly, that incentive will be less than if the class includes both foreign-cubed purchasers and domestic investors. That observation, however, itself shows why limiting foreign-cubed class actions to domestic traders in fact provides optimal deterrence.

Consider the example of two publicly traded companies, A and B.312 Company A trades exclusively in the United States, and has a market capitalization of $1 billion. Company B trades both in the United States and abroad. Assume that 25 percent of Company B’s trading volume, valued at $1 billion, occurs in the United States, and 75 percent, valued at $3 billion, occurs abroad. The CEOs of both companies intentionally issue false press releases inflating their historical earnings as part of a fraudulent scheme. While the global impact of fraud is greater in the case of Company B, the U.S.-specific impact is roughly equal for both companies. If the fraud overvalues the stock of both companies by 10 percent, investors at both companies who executed trades in the United States are harmed by $100 million. Excluding the foreign-cubed investors from a class-action lawsuit brought against Company B equalizes the size of the class, the amount of potential damages, and the incentives of plaintiffs’ attorneys to bring a class action in the first place against either company.

However, if the class includes foreign-cubed purchasers, the incentive to file suit will be greater than in the purely domestic context. Indeed, given the larger class and possible damages award, foreign-cubed suits encourage a suboptimal level of private class-action deterrence by encouraging lawsuits that are not necessary to properly vindicate American interests. Limiting standing to litigants who can demonstrate injury to American markets and investors therefore mirrors precisely the incentives that plaintiffs’ attorneys have to file suit in the run-of-the-mill domestic securities fraud context.313 In other words, permitting class action suits to include foreign-cubed purchasers is not necessary to ensure that plaintiffs’ attorneys will have appropriate incentives to file private suits vindicating the securities laws’ purpose of protecting American markets and investors. Instead, such suits may overdeter.314

312 This example is adapted from Choi & Silberman, supra note 5, at 494-95.
313 Id. at 495.
314 To the extent that plaintiffs’ attorneys may lack incentive to sue where harm to
One could argue that excluding foreign-cubed purchasers decreases deterrence by virtue of the fact that in an increasingly connected world, fraud by foreign managers can affect American investors and markets indirectly.\textsuperscript{315} For example, where a foreign company has both American and foreign investors, that company's managers might have a greater incentive to commit fraud than managers at a purely American company because its foreign shareholders will not be governed by the American securities regime in the event of a lawsuit unless they executed their trades in the United States. Similarly, foreign managers may be better able to hide insider trades in foreign markets, which may indirectly harm American shareholders in the company.\textsuperscript{316}

The short response is that because most Rule 10b-5 litigation in the United States addresses fraud in the secondary market, rather than primary markets, the decrease in deterrence is marginal if nonexistent.\textsuperscript{317} This is because in secondary market fraud cases, damages are not tied to the benefit to the wrongdoer, but rather to the amount of secondary market trading that takes place during the class period and the stock-price drop attributable to the fraud. This measure of damages typically greatly exceeds the benefit to the wrongdoer, resulting in overdeterrence.\textsuperscript{318} Thus, removing foreign-cubed investors

U.S. investors is too small, particularly where trading volume is minimal, it is worth noting that the very same is true for domestic issuers with low trading volume or market capitalization. Whether or not the domestic regime itself is optimal remains an open and hotly debated question and is beyond the scope of this Article. See Janet Cooper Alexander, Rethinking Damages in Securities Class Actions, 48 STAN. L. REV. 1487, 1503-04 (1996); Choi & Silberman, supra note 5, at 496-97; John Coffee, Jr., Reforming the Class Action, 106 COLUM. L. REV. 1534, 1556-66 (2006) [hereinafter Coffee, Reforming]; Frank H. Easterbrook & Daniel R. Fischel, Optimal Damages in Securities Cases, 52 U. CHI. L. REV. 611, 641 (1985); Amanda Rose, Reforming Securities Litigation Reform: Restructuring the Relationship Between Public and Private Enforcement of Rule 10b-5, 108 COLUM. L. REV. 1301, 1312 (2008). If that regime is in fact suboptimal, Congress should address this concern with a reform aimed at both domestic and foreign issuers equally.

\textsuperscript{315} See Choi & Silberman, supra note 5, at 493.

\textsuperscript{316} Id. at 497-98.

\textsuperscript{317} Id. at 498-99, 499 n.131; Coffee, Reforming, supra note 314, at 1556-61.

\textsuperscript{318} Choi & Silberman, supra note 5, at 499; see Fox, supra note 27, at 43-50. Indeed, recent scholarship suggests that damages in Rule 10(b)(5) fraud-on-the-market cases really just transfer shareholder wealth from one subset of shareholders to another, resulting in a zero-sum game in which shareholders do not in fact receive compensation for their losses because the shareholders at the time suit is filed are the ones who will inevitably pay out any damages award. See Coffee, Reforming, supra note 314, at 1556-66; Fox, supra note 27, at 43-44; Rose, supra note 314, at 1313. For a detailed discussion of why foreign-cubed class actions do not vindicate the
from a class action is unlikely to reduce deterrence where investors who purchased or sold shares in the United States remain in the class. In short, limiting the class of foreign plaintiffs who can sue under Rule 10b-5 to foreign investors who can show a direct effect in the United States does not underdeter fraud, and if anything, helps to better calibrate deterrence incentives so as to avoid overdeterrence to the point of harming American markets.\footnote{Such overdeterrence can also affect foreign activities which have beneficial effects on American markets. See Andrew T. Guzman, Choice of Law: New Foundations, 90 GEO. L.J. 883, 908 (2002).}

2. Practical Consequences

The Supreme Court's cases addressing the practical consequences of an expansion of the class of plaintiffs who may sue under Rule 10b-5 caution against expansion of the Rule 10b-5 right. Both securities scholars and recent economic studies have noted the declining competitiveness of the American securities markets caused by fears of exposure to massive securities class action judgments.\footnote{See sources cited supra notes 18-21; see also Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, 552 U.S. 148, 163-64 (2008) ("Overseas firms with no other exposure to our securities laws could be deterred from doing business here. This, in turn, may raise the cost of being a publicly traded company under our law and shift securities offerings away from domestic capital markets."); Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Dabit, 547 U.S. 71, 80 (2006) (noting that "litigation under Rule 10b-5 presents a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general") (quoting Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 739 (1975)).}

Because most foreign-cubed cases are class action cases, foreign defendants face enormous pressure to settle rather than litigate, so as to avoid the potential for large judgments as well as the costs of extensive discovery under American laws different from and more permissive than foreign law.\footnote{Stoneridge, 552 U.S. at 148-52, 163-67.} Overseas firms with no other exposure to American securities laws are deterred from doing business in the United States, which in turn, raises the cost of being a publicly traded company under American law and shifts securities offerings away from domestic capital markets.\footnote{\textit{Id.} at 163-67.} More recently, foreign firms have been delisting entirely from American markets, rather than risk uncertain exposure to global liability in an American lawsuit.\footnote{See supra notes 18-21.}
These empirical realities are precisely the policy concerns that the Supreme Court routinely considers in Rule 10b-5 cases and strongly cautions against permitting foreign-cubed class actions, absent a showing of direct injury in the United States. The Court has repeatedly indicated that where such policy issues are present, Congress, not the courts, should expand the class of plaintiffs who may invoke the Rule 10b-5 remedy further. This is particularly so where an expanded class of plaintiffs affects not just American markets, but also American policy with foreign nations. It is in the latter scenario where Empagran comes into play just as the fourth Cort factor would if an expanded class of plaintiffs would affect regulation traditionally left to the states. Indeed, the Supreme Court's most recent Rule 10b-5 case, Stoneridge, implicitly integrated Empagran's prescriptive comity concerns into the Rule 10b-5 analysis by relying on the fact that expanding the class of plaintiffs who had standing to sue would affect American markets and interfere with foreign investment in the United States.

Under both approaches, the Court must assume that Congress did not intend to create standing for foreign-cubed plaintiffs where expanding the class of plaintiffs who do have standing to sue would harm American markets and intrude upon the diplomatic prerogatives of Congress and the Executive Branch.

IV. FOREIGN-CUBED RULE 10B-5 STANDING

A. The Test

Distilling the foregoing analytical framework, a simple, predictable test emerges for statutory standing that is applicable equally to both private individual foreign plaintiffs and foreign-cubed class actions. Under this test in order to have standing to sue, a foreign-cubed plaintiff must allege an injury that the securities laws are designed to protect. That injury must be a direct effect in the United States on American markets or investors. Accordingly, only foreign plaintiffs suffering a loss caused by the purchase or sale of securities in the

326 Stoneridge, 552 U.S. at 163-66.
United States would have standing to sue.\textsuperscript{327} By definition, then, foreign-cubed plaintiffs lack standing because they neither purchased nor sold shares in the United States.

The test similarly prevents any class action consisting of foreign plaintiffs relying on the conduct test. A plaintiff who lacks statutory standing may not serve as class representative.\textsuperscript{328} Therefore, under the analysis developed in this Article, no foreign plaintiff can serve as lead plaintiff in a foreign-cubed lawsuit.\textsuperscript{329} However, irrespective of whether a lead plaintiff has statutory standing, whether the class action device itself may be employed to vindicate a right is itself a question of statutory standing.\textsuperscript{330} Just as class representatives must themselves have statutory standing to sue before a class may be properly certified, so too must the class itself.\textsuperscript{331} In other words, the

\textsuperscript{327} Although beyond the scope of this Article, arguably, under the analysis developed here, Americans purchasing shares on foreign exchanges should also lack standing to sue. Indeed, as discussed, the 1933 Act expressly provides for the creation of an administrative agency to negotiate the resolution of American claims premised on the fraudulent purchase or sale foreign securities to Americans. See supra note 303 and accompanying text. However, I leave that analysis for another day.

\textsuperscript{328} See Harzewski v. Guidant Corp., 489 F.3d 799, 803 (7th Cir. 2007); Coan v. Kaufman, 457 F.3d 250, 256 n.3 (2d Cir. 2006).

\textsuperscript{329} A class may not be certified if any class members lack Article III standing. See Ortiz v. Fibreboard Corp., 537 U.S. 815, 831 (1999); Denney v. Deutsche Bank AG, 443 F.3d 253, 264 (2d Cir. 2006); Adashunas v. Negley, 626 F.2d 600, 604 (7th Cir. 1980). Sometimes courts certify a class action containing class members who themselves would not satisfy statutory standing, so long as the lead plaintiff does. See Hohider v. United Parcel Serv., Inc., 574 F.3d 169, 181 n.14 (3d Cir. 2009); Kohen v. Pac. Inv. Mgmt. Co., 571 F.3d 672, 677-78 (7th Cir. 2009); Bates v. United Parcel Serv., Inc., 465 F.3d 1069, 1077 (9th Cir. 2006); Denney, 443 F.3d at 267-68.

\textsuperscript{330} See Ortiz, 527 U.S. at 831 (stating that “the class certification issues” are “logically antecedent to Article III concerns” and “themselves pertain to statutory standing”); Payton v. Kane, 308 F.3d 673, 680 (7th Cir. 2002); see also Linda S. Mullenix, Standing and Other Dispositive Motions After Amchem and Ortiz: The Problem of “Logically Antecedent” Inquiries, 2004 Mich. St. L. Rev. 703, 730-31. See generally CHARLES A. WRIGHT ET AL., FEDERAL PRACTICE AND PROCEDURE § 1785.1 n.10 (3d ed. 2009) (collecting cases).

\textsuperscript{331} Bates, 465 F.3d at 1077-78 (discussing “showing . . . necessary to establish the class's statutory standing to bring a lawsuit under the ADA’’); Payton v. County of Kane, 308 F.3d 673, 680-81 (7th Cir. 2002) (“[O]nce a class is properly certified, statutory and Article III standing requirements must be assessed with reference to the class as a whole, not simply with reference to the individual named plaintiffs.’’); Conte Bros. Auto., Inc. v. Quaker State-Slick 50, Inc., 165 F.3d 221, 226 (3d Cir. 1998) (holding that in class action context question of class’s “statutory standing” to sue depends on whether Congress intended to provide remedy to that class); 13A WRIGHT ET AL., supra note 330, § 3531.9.6 n.16 (discussing courts that “address directly a concept of ‘class standing’’).
court must analyze “class standing.” Put in terms of the Supreme Court’s Rule 10b-5 implied rights jurisprudence, a class composed of foreign-cubed plaintiffs would lack statutory standing to sue as the 1934 Congress would not have extended standing to foreign-cubed plaintiffs where “a widely expanded class of plaintiffs under Rule 10b-5” would conflict with express provisions of the 1934 Act, SEC regulation of foreign issuers, and the overall “effective operation of the securities laws.”

Understood in this light, a court may reject the class as a whole when it includes foreign-cubed class members, regardless of whether the class representatives are themselves American or may otherwise file suit under Rule 10b-5, because the class itself fails the statutory standing analysis outlined in this Article. Only a class consisting of individuals who purchased or sold shares within the United States, whether American or foreign, would satisfy that analysis, thus necessarily excluding all foreign-cubed plaintiffs from class actions.

The result is a simple, mechanical test, which not only follows from the Supreme Court’s Rule 10b-5 and comity case law, but also, as the next subpart shows, has the virtue of putting the conduct test and all its complications and uncertainties to bed.

B. Benefits

Beyond its simplicity, analyzing the question of the extraterritorial application of the securities laws as a question of statutory standing has numerous benefits that the current jurisdictional analysis lacks.

First, the standing analysis provides a predictable, consistent, and easily understood test that has intuitive appeal for both investors and issuers. By definition, the conduct test does not satisfy the standing analysis, providing a bright-line rule that is easily applied. The trigger is a direct effect in the United States, which requires the purchase or sale of shares in the United States. Not only does that trigger comport with investor expectations, but it also provides predictability for foreign issuers deciding whether to expose themselves to Rule 10b-5’s liability and disclosure regime.

332 See 13A WRIGHT ET AL., supra note 330, § 3531.9.6 n.16 (collecting cases).
335 See discussion of Section 30 of the 1934 Act, supra Part III.A.
336 Musick, 508 U.S. at 298.
Second, relying on standing limits the role of judges as decision makers in areas that touch on foreign relations and American economic policy. Rather than have courts attempt to ascertain the quantum of conduct necessary to invoke federal jurisdiction while also balancing comity concerns and the procedural complexities of the class certification process, an extraterritoriality standing analysis provides courts with a simple roadmap to follow when determining whether foreign plaintiffs may invoke the Rule 10b-5 remedy. That simple rule, which forecloses conduct test analysis, eliminates the uncertainty caused by courts reaching different results in cases that share essentially the same exact facts.

Third, the standing analysis permits the early dismissal of suits, just like a jurisdictional analysis, but without its procedural pitfalls. Early dismissal of securities class actions is crucial for optimizing the deterrent effect of private securities litigation. The uniquely vexatious nature of securities class actions, which often result in forced settlements rather than trial, means that an early vehicle for dismissing nonmeritorious suits is necessary. Similarly, the potential for foreign-cubed suits to interfere with international relations and American business interests and competitiveness also militates in favor of an early dismissal of nonmeritorious suits.

Statutory standing facilitates early dismissal of suits because it is a threshold question that may be decided before jurisdictional issues.

337 Because the standing analysis advocated here avoids all these issues, the intricacies of class certification in the foreign-cubed context are beyond the scope of this Article. These complexities most often revolve around the question of whether a class action lawsuit is superior in light of the possibility that a foreign court will not recognize a judgment as preclusive, whether foreign plaintiffs can serve as lead plaintiffs, and whether foreign plaintiffs can rely on a presumption of reliance available to American investors. See Choi & Silberman, supra note 5, at 477-88; Fox, supra note 27, at 44-54. For more in-depth discussion of the issues arising in the class action context, see Buxbaum, supra note 1, at 26-41; Choi & Silberman, supra note 5, at 477-88.


340 Ortiz v. Fibreboard Corp., 527 U.S. 815, 831 (1999); Ruhrgas AG v. Marathon Oil Co., 526 U.S. 574, 585 (1999); Steel Co. v. Citizens for a Better Env’t, 523 U.S. 83,
including Article III standing and subject matter jurisdiction,\textsuperscript{341} class certification,\textsuperscript{342} or the merits.\textsuperscript{343} Statutory standing thus permits the earliest possible dismissal of the case by virtue of a motion to dismiss on the pleadings or for failure to state a claim.\textsuperscript{344} Moreover, statutory standing permits dismissal on a motion to dismiss for lack of jurisdiction. Indeed, courts sometimes refer to statutory standing as jurisdictional, even though it has nothing to do with the court’s statutory or constitutional power to adjudicate a case.\textsuperscript{345} As such, some courts incorrectly analyze the issue as a Rule 12(b)(1) motion to dismiss for lack of subject matter jurisdiction.\textsuperscript{346} Although the result is often the same as if analyzed under Rule 12(b)(6), this adds another layer to the confusion engendered by misuse of the “jurisdictional” label.\textsuperscript{347} In any event, the doctrine is flexible. Unlike true jurisdictional issues, the court can assume statutory standing and decide the case on the merits if the exigencies of the case favor resolution on the merits.\textsuperscript{348}

Moreover, the dismissal is on a purely legal basis, and thus avoids jurisdictional discovery. Given the context-specific nature of the

\textsuperscript{341} Steel, 523 U.S. at 97 n.2; cf. 13A CHARLES A. WRIGHT ET AL., FEDERAL PRACTICE AND PROCEDURE § 3531.15 (2d. ed. Supp. 2002) (“[T]he court has an extensive discretion to deny standing if that course is easier, or more clearly right, than to rule on constitutional grounds first.”).

\textsuperscript{342} Ortiz, 527 U.S. at 831; Payton v. County of Kane, 308 F.3d 673, 682 (7th Cir. 2002).

\textsuperscript{343} Ortiz, 527 U.S. at 831; Steel, 523 U.S. at 97 n.2; see also Potter v. Hughes, 546 F.3d 1051, 1055 (9th Cir. 2008); Lerner v. Fleet Bank, N.A., 318 F.3d 113, 129 (2d Cir. 2004); cf. Bruce v. United States, 759 F.2d 755, 757-58 (9th Cir. 1985) (addressing statutory standing as “a threshold jurisdictional question in every federal case,” and noting that plaintiff “may have a valid claim on the merits and nonetheless lack standing”).

\textsuperscript{344} See Sinochem, 549 U.S. at 431; Steel, 523 U.S. at 97 n.2; Cetacean Cmty. v. Bush, 386 F.3d 1169, 1175 (9th Cir. 2004).

\textsuperscript{345} See Loren v. Blue Cross & Blue Shield of Mich., 305 F.3d 598, 606 (6th Cir. 2007); Coan v. Kaufman, 457 F.3d 250, 256 (2d Cir. 2006); Lerner, 318 F.3d at 129; Bruce, 759 F.2d at 757-58.

\textsuperscript{346} See Lerner, 318 F.3d at 129; Bruce, 759 F.2d at 757-58.

\textsuperscript{347} See Harris v. Amgen, Inc., 573 F.3d 728, 732 n.3 (9th Cir. 2009); In re Parmalat Sec. Litig., 497 F. Supp. 2d 526, 528-29 (S.D.N.Y. 2007); see also Canyon County v. Syngenta Seeds, Inc., 519 F.3d 969, 975 n.7 (9th Cir. 2008) (criticizing cases that view statutory standing as jurisdictional).

\textsuperscript{348} See Steel, 523 U.S. at 97 n.2; Coan, 457 F.3d at 256.
conduct test, subject-matter-jurisdiction analysis inevitably requires the resolution of questions of fact. Those questions often cannot be resolved at the motion to dismiss stage, requiring jurisdictional discovery. Such discovery may eventually lead to dismissal, or it may devolve into a long, confusing, and expensive process that both plaintiffs and defendants can invoke as reason to defer settlement, given the possibility of dismissal. This distorts litigation incentives and encourages plaintiffs and defendants alike to overestimate the strength of their hand, causing further wasted litigation expenditures. A standing analysis avoids these procedural complications and delays without encouraging gamesmanship or distorting settlement incentives, and also leaves factual disputes where they belong — as summary judgment challenges to the merits of the case.

A standing analysis also sidesteps the potentially thorny issue created by importing Stoneridge's logic into the conduct test. Recall that Morrison injected the concept of Rule 10b-5 reliance into its conduct test analysis. But if Rule 10b-5 reliance is an element of the conduct test, the conduct test cannot be resolved on a motion to dismiss. This is because where the merits of an action are intertwined with the jurisdictional determination, courts may not resolve a motion to dismiss for lack of subject matter jurisdiction prior to discovery on the merits. Thus, foreign-cubed cases would not be resolvable until summary judgment, at the earliest, injecting far greater uncertainty into an already unpredictable jurisdictional analysis.


350 Indeed, such inquiries may devolve into full-blown mini-trials on the merits. Given that the conduct test requires an analysis of direct causation, and, after Morrison, possibly reliance, the “arising under” formulation of 28 U.S.C. 1331’s grant of federal question jurisdiction cannot be resolved simply by reviewing the complaint. These mini-trials frontload litigation costs and further exacerbate the inefficiency of the jurisdictional approach. See also Itoba Ltd. v. Lep Group PLC, 54 F.3d 118, 122 (2d Cir. 1995) (applying concept of “derivative reliance” to conduct test).

351 See Fox, supra note 27, at 42.

352 Viewing the inquiry as a legal question also facilitates de novo review by courts of appeals, thus facilitating less deferential appellate review of questions of comity and congressional intent. Conversely, if the inquiry is jurisdictional, the inquiry is also factual, requiring deferential appellate review of facts related to the inquiry.

353 See Morrison, 547 F.3d at 175; supra Part I.B.2.


355 See Gulf Oil, 419 U.S. at 204 n.19. This may also be a problem given the “direct causation” requirement of the conduct test, which is also an element of the Rule 10b-5
statutory standing, which is not inextricably intertwined with the merits of a Rule 10b-5 case, can be decided before any discovery.\textsuperscript{356}

Statutory standing also optimizes the efficiencies of Rule 10b-5 litigation. Objections for lack of subject matter jurisdiction can never be waived, and a court can raise the issue at any time on its own even if the parties do not.\textsuperscript{357} This makes sense where the issue is in fact jurisdictional, as a judgment issued by a court lacking the statutory or constitutional power to enter that judgment would be unconstitutional — a harm worth avoiding. Even so, at some point in the litigation process, dismissing on jurisdictional grounds and forcing the parties to relitigate from scratch becomes less efficient than deciding the case on the merits.\textsuperscript{358} This is particularly so when both parties actively seek

\textsuperscript{356} This follows from the fact that statutory standing is a legal question, and therefore can be resolved before the merits, see Steel Co. v. Citizens for a Better Env’t, 523 U.S. 83, 92 (1998); Assoc. Gen. Contractors of Cal. v. Cal. State Council of Carpenters, 459 U.S. 519, 539 (1983), and from the fact that reliance is not an element of statutory standing as developed in this Article. As such, discovery is unnecessary. See, e.g., Harris v. Amgen, Inc., 573 F.3d 728, 732 (9th Cir. 2009) (noting that “a dismissal for lack of statutory standing is properly viewed as a dismissal for failure to state a claim”); Lerner v. Fleet Bank, N.A., 318 F.3d 113, 129 (2d Cir. 2004) (noting that court can address statutory standing before merits if not inextricably linked with merits); Miller v. Rite Aid Corp., 334 F.3d 335, 341 (3d Cir. 2003) (observing that question of whether plaintiff has statutory standing to sue under Section 502 of Employee Retirement Income Security Act of 1974 may be determined before addressing merits of the claim). To the extent that the parties dispute plaintiff’s pleadings regarding the location of the trade at issue, courts should require plaintiffs to submit some documentation, most likely an affidavit, stating the location of the relevant trade, but no more. Sanctions pursuant to Federal Rule of Civil Procedure 11 should be sufficient to deter frauds on the court by litigants.\textsuperscript{357} See Arbaugh v. Y&H Corp., 546 U.S. 500, 506 (2006); Kontrick v. Ryan, 540 U.S. 443, 455 (2004); United States v. Cotton, 535 U.S. 625, 630 (2002).

\textsuperscript{358} For example, a large cost imposed on defendants in securities litigation is discovery. However, once discovery is completed, that harm has been fully realized. Consider also a trial adjudicated on the merits, taken up on appeal, and then dismissed, some five years down the line, on the basis of subject matter jurisdiction. That decision is binding on the facts adjudicated as to jurisdiction, but has no binding effect on the merits, meaning that the issues can easily be relitigated again, at cost to both parties. See Da Silva, 229 F.3d at 362; 18 Wright et al., supra note 330, § 4436. The efficiency value in finality of judgments is therefore undermined.
a final judgment or settlement, and have invested years’ worth of time and litigation expenses into reaching that conclusion on the merits or settlement, only to have a court hit the reset button by dismissing on jurisdictional grounds. Statutory standing avoids this problem entirely because it is a waivable objection. Thus, if the parties want to litigate a final judgment or settle a case to secure res judicata effects against future litigation, the parties may elect simply not to contest the statutory standing issue.

Fourth, and perhaps most importantly from the perspective of American economic competitiveness, statutory standing facilitates an optimal deterrence regime by calibrating the balance between private and public enforcement. Private Rule 10b-5 litigants are motivated by self-interest and are ill-suited to temper their litigation motives in favor of broader systemic concerns, like international regulatory cooperation, foreign policy, and diplomatic relations. The SEC, on the other hand, is well situated to take into account any such concerns. Using the statutory standing analysis outlined here to exclude foreign purchasers of foreign securities from Rule 10b-5 class actions allows SEC regulation to serve as the primary enforcement mechanism where those frauds affect American interests in some way. This follows from the fact that the statutory standing analysis would not govern SEC actions, as private plaintiff standing is a separate and distinct concept

359 This follows from the fact that statutory standing is not a prerequisite for a court’s exercise of judicial power. See Craig v. Boren, 429 U.S. 190, 193-94 (1976); Bd. of Natural Res. v. Brown, 992 F.2d 937, 945-46 (9th Cir. 1993); MacLauchlan v. Prudential Ins. Co. of Am., 970 F.2d 357, 359 n.1 (7th Cir. 1992); Rite Research Improves the Env’t, Inc. v. Castle, 650 F.2d 1312, 1320 (5th Cir. 1981); see also Steel Co. v. Citizens for a Better Env’t, 523 U.S. 83, 95, 97 (1998) (observing distinction between statutory standing which depends on “text of the statute relied upon” and Article III standing, which does not, but is nonetheless prerequisite for exercise of “judicial power of the United States”); Valley Forge Christian Coll. v. Ams. United for Separation of Church & State, Inc., 454 U.S. 464, 474-75 (1982) (noting distinction between Article III standing, requirement for exercise of judicial power, and prudential standing, which is not); In re Literary Works in Elec. Databases Copyright Litig., 509 F.3d 116, 134 (2d Cir. 2007) (Walker, J., dissenting) (noting “distinction between constitutional standing, the absence of which deprives the court of authority to redress harm to that plaintiff, and statutory standing, the absence of which may be waived”); Max Huffman, A Standing Framework for Private Extraterritorial Antitrust Enforcement, 60 SMU L. Rev. 103, 141 (2007).

from the general statutory and regulatory prohibition on fraud in connection with the purchase or sale of securities. Indeed, the SEC’s statutory role is to enforce the remedial and preventive terms of the securities laws in the public interest, and not merely to police those whose plain violations have already caused demonstrable loss or injury. Therefore, unlike private plaintiffs, the SEC can act prophylactically to protect American investors and markets before a securities violation actually occurs, and it need not plead standing or allege investor reliance or causation in connection with a fraud it seeks to regulate. The SEC, therefore, retains broader regulatory and enforcement tools otherwise unavailable to Rule 10b-5 plaintiffs and can better balance competing policy concerns where international relations or regulation is involved when using those tools.

The standing analysis thus permits the SEC, rather than private plaintiffs, to serve as the regulatory vehicle for the safe haven and good neighbor rationales espoused by courts applying the conduct test. To that effect, the standing analysis facilitates the SEC’s use of section 30 of the 1934 Act to issue regulations governing extraterritorial conduct where that conduct affects American investors or markets. The SEC may choose to exempt foreign issuers, as it has done in other contexts under the registration provisions of the 1933 Act, or it may negotiate with other regulatory sovereigns to create a system in which foreign companies could opt into the American regulatory scheme, if a company concludes that such opting-in is beneficial to the company. Likewise, the SEC could cooperate with foreign regulatory bodies to pursue transnational frauds. Regardless,

362 See Berko v. SEC, 316 F.2d 137, 143 (2d Cir. 1963).
363 Berger, 322 F.3d at 193.
364 Dabit, 547 U.S. at 85.
366 Indeed, courts applying the conduct test have suggested that the SEC can rely on a lesser quantum of conduct under the conduct test because of its regulatory and enforcement role. See Berger, 322 F.3d at 193; Zoelsch v. Arthur Andersen & Co., 824 F.2d 27, 30 (D.C. Cir. 1987).
367 See discussion supra Part III.
369 See Choi & Silberman, supra note 5, at 504; Fox, supra note 27, at 54.
370 Such cooperation is facilitated by so-called “positive comity” agreements, by which the affected regulatory authority can request that a regulatory authority that is party to the agreement initiate enforcement activities. See Joseph P. Griffin, Extraterritoriality in U.S. and EU Antitrust Enforcement, 67 Antitrust L.J. 159, 183 (1999).
the standing analysis strengthens the SEC’s role in regulating American fraud with effects abroad and removes private plaintiffs from the equation. 371 Given the legislative history’s explanation of section 30(b)’s purpose, it is the SEC who should be enforcing the securities laws where foreign issuers are involved in the first place. 372 Moreover, the standing analysis eliminates the perverse incentives that currently exist for defendants to resist cooperating with the SEC and other regulatory bodies. The present regime unintentionally encourages inverse deterrence. 373 Defendants who may otherwise cooperate with regulatory authorities may decline to do so given that the likelihood they will face a private civil lawsuit in addition to whatever regulatory penalty the SEC negotiates with them. 374 This, in turn, limits the SEC’s ability to negotiate criminal or civil settlements that American investors or markets may benefit from. Indeed, where defendants risk civil liability in addition to any regulatory settlement, they may simply choose to hide fraud harmful to shareholders, rather than risk a civil suit. Because shareholders are better off in a world where defendants disclose harmful information, the problem of inverse deterrence undermines the 1934 Act’s overall goals. Under a standing analysis, the problem of inverse deterrence is minimized, as private lawsuits against foreign issuers absent an American-based investor or injury are no longer possible.

Finally, unlike other recent scholarly proposals aimed at modifying the jurisdictional analysis, 375 the standing analysis outlined here is

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371 The standing analysis therefore minimizes any concern that American actors may somehow externalize the costs of their wrongdoing on foreign jurisdictions and avoid the consequences. See Guzman, supra note 319, at 886, 927-30.
372 See discussion supra Part III.A-B.
373 See generally Huffman, supra note 359, at 115-16, 140 (discussing concept of inverse deterrence).
374 In recent years, self-reporting to or cooperation with administrative agencies has often been followed by private lawsuits against the same party addressing the same underlying misconduct. See Jackson & Roe, supra note 360, at 7.
375 Professors Choi and Silberman would limit jurisdiction based on whether a foreign plaintiff purchased shares on an American market. See Choi & Silberman, supra note 5, at 468, 490-500. Professor Buxbaum offers a similar proposal, as does Professor Coffee. Buxbaum, supra note 1, at 56-69; Coffee, Law and the Market, supra note 18, at 303. Professor Fox takes a different tack, arguing that no plaintiff should be allowed to file suit against a foreign company unless its “economic center of gravity” was in the United States. Fox, supra note 27, at 54. All four proposals would require legislative action or, at the very least, judicially overruling the validity of the conduct test for jurisdictional analysis. As of this writing, news reports suggest that the SEC may seek to abolish the conduct test outright. See Rich Edson, SEC Gives “Wish List” of 42 Changes It Wants in Securities Law, FOX Bus., July 16, 2009, http://www.foxbusiness.com/story/markets/industries/government/sec-gives-wish-list--
entirely within the power of the courts to implement. No legislative amendment is needed, and no sweeping reversal of forty years of federal practice is required. Of course, this Article contends that the Supreme Court or the courts of appeals should expressly rule that the issue of extraterritoriality is a question of statutory standing, but courts could nevertheless apply the analysis even if they feel constrained by earlier precedent. Indeed, adopting the analysis advocated here would harmonize the Rule 10b-5 statutory standing doctrine with other areas of federal law, most notably antitrust and the Racketeer Influenced and Corrupt Organizations Act ("RICO"), which also treat extraterritoriality as a statutory standing question. 376

Conceivably, one could argue that Congress has acquiesced to the lower courts' treatment of the issue as jurisdictional, thus preventing a subsequent lower court from analyzing the issue as statutory standing. 377 The short response is that the Supreme Court has held that where the Court expressly reserves an issue, rather than deciding it, Congress cannot by inaction legislatively affirm the practice of the

376 Although beyond the scope of this Article, the statutory standing analysis discussed here is almost indistinguishable from the statutory standing framework that the Supreme Court has articulated for both private antitrust and RICO lawsuits. In both those contexts, plaintiffs must allege that they suffered a direct injury the antitrust or RICO laws were designed to remedy, and that the violating conduct directly caused that injury. See Bridge v. Phoenix Bond & Indem. Co., 128 S. Ct. 2131, 2141-42 (2008) (discussing RICO); Holmes v. Sec. Investor Prot. Corp., 503 U.S. 258, 272 (1992) (same); Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 496 (1985) (same); Assoc. Gen. Contractors of Cal. v. Cal. State Council of Carpenters, 459 U.S. 519, 532-33 (1983) (discussing antitrust lawsuits); Brunswick Corp. v. Pueblo Bowl-O-Mat, 429 U.S. 477, 486-87 (1977) (same). And in the antitrust context, courts also ask whether permitting suit would conflict with the underlying policies the antitrust laws were designed to promote. See Associated Gen., 459 U.S. at 532-33; Brunswick, 429 U.S. at 486-87; Huffman, supra note 359, at 108-13. Both doctrines have been applied in the extraterritorial context. See, e.g., Liquidation Comm'n of Banco Intercontinental, S.A. v. Renta, 330 F.3d 1339, 1352 (11th Cir. 2008) (discussing RICO); Empagran S.A. v. F. Hoffman-LaRoche Ltd., 315 F.3d 338, 357-59 (D.C. Cir. 2003) (antitrust); Kruman v. Christie's Int'l PLC, 284 F.3d 384, 403 (2d Cir. 2002) (same); Den Norske Stats Oljeselskap As v. HeercMac V.O.F., 241 F.3d 420, 426 (5th Cir. 2001) (same); see also Edward D. Cavanagh, The FTAIA and Empagran: What Next?, 58 SMU L. Rtv. 1419, 1433-51 (2005); Huffman, supra note 359, at 141.

lower courts. The Court expressly reserved the issue of the extraterritorial scope of the securities laws in Scherk v. Alberto-Culver Co. Accordingly, congressional inaction in the face of divided lower federal court practice cannot legislatively affirm that practice or require courts to follow that practice. In any event, as a general matter, Congress can only amend a duly enacted statute by express action. Moreover, the Court has repeatedly noted that while Congress has acquiesced to the private Rule 10b-5 right generally, it has left defining the contours of that right to the courts. If anything, then, the acquiescence argument cuts against any claim that Congress has acquiesced to the conduct test or the treatment of the Act’s extraterritoriality as a question of subject matter jurisdiction. Thus, nothing stands in the way of the federal courts applying the standing analysis outlined here.

CONCLUSION

For over forty years, courts have analyzed the question of the extraterritorial application of section 10(b) and Rule 10b-5 of the 1934 Securities Exchange Act as a question of subject matter jurisdiction under the so-called conduct and effects tests. Courts apply these tests in an ad hoc, inconsistent manner, eschewing any bright-line rule. As a result, jurisdiction under either test is highly unpredictable. This state of affairs leaves litigants uncertain as to their legal obligations, discourages foreign issuers from entering American markets, and places American economic and foreign policy in the hands of private litigants and the judiciary, rather than with Congress or the SEC. Most recently, the Second Circuit in Morrison v. National Australia Bank Ltd. complicated the analysis further by crafting yet another version of the conduct test.

However, as this Article demonstrates, the extraterritorial scope of the securities laws has nothing to do with a court’s subject matter jurisdiction, meaning its power to adjudicate a dispute under the Constitution. Instead, the extraterritorial scope of the securities laws, like any law, depends on whether Congress intended for the relevant

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378 Cent. Bank, 511 U.S. at 186.
380 Cent. Bank, 511 U.S. at 186.
381 Id.
383 See supra Part I.B.2.
statute to reach extraterritorial conduct. That analysis is decidedly not jurisdictional and focuses on Congressional intent. In the particular context of the implied Rule 10b-5 cause of action, the Supreme Court has routinely analyzed the question of who may invoke the cause of action as a matter of statutory standing. Applying that analysis in light of the 1934 Act’s text, structure, and legislative history readily answers the question of extraterritoriality — only foreign plaintiffs who bought or sold stock within the United States have standing to invoke American securities laws.

The standing analysis developed in this Article provides courts with a simple, bright-line rule that eliminates the unpredictability of the present jurisdictional regime and facilitates the early dismissal of nonmeritorious lawsuits. That, in turn, encourages an optimal level of private litigation without deterring beneficial economic activity and leaves the delicate work of regulating transnational frauds that implicate foreign relations to the SEC. And, unlike recent proposals for reform that continue to view the issue as jurisdictional, the standing analysis that this Article proposes does not require new legislation. With so much at stake, the time has come to correct the error of analyzing extraterritoriality as a question of subject matter jurisdiction.