# International Securities Regulations

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## I. Multilateral and Bilateral Securities Agreements

Several multilateral and bilateral international agreements were signed by the United States Securities and Exchange Commission and the Commodities Futures Regulatory Commission in 1996.

### A. COMMODITY FUTURES TRADING COMMISSION AND NEW ZEALAND SECURITIES COMMISSION

The Commodity Futures Trading Commission and the New Zealand Securities Commission signed a memorandum of understanding (MOU) on September 16, 1996. This MOU will facilitate the exchange of data needed to oversee the global futures and options industry in both countries. The MOU is designed to improve enforcement of the Commodities futures and options markets in each country.

> Under the MOU, . . . the CFTC and NZSC have arranged to provide each other with "the fullest mutual assistance" permitted by U.S. and New Zealand law in response to requests each authority may make concerning futures and options matters.

Each signatory agrees to provide the other "access to information in the files of the requested authority, tak[e] testimony and statements, obtain[] information and documents, and conduct[] compliance inspections or examinations of futures transactions and futures businesses."[1]

### B. DECLARATION ON COOPERATION AND SUPERVISION OF INTERNATIONAL FUTURES EXCHANGES AND CLEARING ORGANIZATIONS

Perhaps the most significant effort towards international cooperation amongst futures markets regulators was the "Declaration on Cooperation and Supervision of International Futures Exchanges and Clearing Organizations." This agreement was signed on March 15, 1996, by futures market regulators representing 14 countries. The agreement establishes a multilateral

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1. *CFTC, New Zealand Securities Agency Sign Memorandum of Understanding*, 28 Sec. Reg. L. Rep. (BNA) No. 37, at 1156 (Sept. 20, 1996).

mechanism for bilateral information exchange. The agreement will facilitate the exchange of information in situations where "local concerns or law may necessitate the involvement of a governmental authority."[2]

The signatories include: the U.S. Commodities Futures Trading Commission (CFTC); the United Kingdom Securities and Investments Board (SIB); the Australian Securities Commission; the Austrian Ministry of Finance; the French Commission des Operations de Bourse; Germany's Bundesausichtsamt fur der Wertpapierhandel; Hong Kong's Securities and Futures Commission; the Central Bank of Ireland; Italy's Commissione Nazionale per le Societa e la Borsa; the Securities Board of Netherlands; the Commission des Valeurs Mobilieres du Quebec; the Monetary Authority of Singapore; the Financial Services Board of South Africa; and Spain's Comision Nacional del Mercado de Valores.

This agreement is part of a larger international regulatory effort signed by 49 securities and futures regulators. The agreements have their origin in the recommendations and endorsements established at the May 1995 Windsor, England, meeting of international futures regulators. The new mechanisms are designed to establish cooperation and the exchange of information in situations where signatories' financial resources or positions may be effected. "The trigger levels are designed to facilitate the identification of large exposures by firms that could have a potentially adverse effect on markets," the CFTC stated.[3]

Then CFTC Acting Chairman John Tull asserted that the declaration and MOU constituted "an unprecedented exercise in cooperation that will significantly enhance the international safety net for financial markets. In an era where exchange member firms typically trade on multiple exchanges, an individual regulator or market authority alone may not have the information necessary to evaluate the risks to its markets."[4]

"The newly created mechanisms for sharing large exposure data, along with effective internal controls, 'add an important new protection which significantly advances international efforts to address systemic risk which may result from the failure of a major firm,' Tull advised. 'I hope that other exchanges, clearing organizations and their governmental authorities will embrace this partnership between markets and regulators,' he added."[5]

### C. International Information Sharing Agreement

On March 15, 1996, 49 futures exchanges and clearing entities signed the "International Information Sharing Agreement and Memorandum of Understanding." The agreement is designed to facilitate the exchange of market and financial data information among signatory exchanges and clearinghouses regarding the financial condition of international brokerage firms and banks. As part of this agreement signatories agreed to exchange data required to protect the integrity of global exchange traded markets. Signatories include futures exchanges and clearinghouses from America, Africa, Europe, and the Asia-Pacific.[6]

The most notable provision of the MOU is the "triggering mechanism." Under this mechanism a "triggering" event allows a signatory to the agreement to seek information from other

2. *Information Sharing Accord Signed Among 14 Futures Regulators*, Sec. Reg. & L. Rep. (BNA) No. 12, at 421 (March 22, 1996).

3. *Id.*

4. *Id.*

5. *Id.*

6. *Global Futures Marts, Clearing Entities Sign Memorandum of Understanding*, Sec. Reg. & L. Rep. (BNA) No. 12, at 423 (March 22, 1996).

signatories regarding an international financial services firm or ban. Triggering events would include: a substantial decline in a member firm's financial resources; large cash flows in a proprietary or customer account of a member firm; and a high concentration of positions in a particular futures or options contract.

Any decisions made on the basis of the information exchange is required to be provided to the originating exchange or clearinghouse. Furthermore, information provided to a signatory is done so on a strictly confidential basis.

The following exchanges and clearinghouses are signatories to the MOU: the CBT; the BTCC; the Canadian Derivatives Clearing Corp.; the CME; the Citrus Associates of the New York Cotton Exchange Inc.; the Coffee, Sugar & Cocoa Exchange Inc.; the Comex Clearing Association Inc.; the Commodity Clearing Corp.; the Commodity Futures Clearing Corp. of New York; the Deutsche Terminborse; the Deutsche Borse AG; the European Options Exchange; the EOCC Clearing Corp. B.V.; the FUTOP Clearing Centre; the HKFE; the Hong Kong Futures Exchange Clearing Corp.; the International Petroleum Exchange of London Ltd.; the Irish Futures and Options Exchange; the Kansas City Board of Trade; the Kansas City Board of Trade Clearing Corp.; the LIFFE Administration and Management; the London Clearing House Ltd.; MATIF; the Marche des Options Negociables de Paris; MEFF Holding; the Mid America Commodity Exchange; the Minneapolis Grain Exchange; the Montreal Exchange; the New York Cotton Exchange; the New York Futures Exchange Inc.; Nymex; the New Zealand Futures and Options Exchange Ltd.; the Norwegian Futures and Options Clearing House; the N.V. Nederlandse Liquidatie Kas; OM Stockholm; the OMLX Exchange; the Oslo Stock Exchange; OTAB AG—the Austrian Futures and Options Exchange; SIMEX; the South African Futures Exchange; SAFEX Clearing Co. (PTY) Ltd.; the Swiss Exchange and its subsidiary, the Swiss Options and Financial Futures Exchange Ltd.; the Sydney Futures Exchange Ltd.; the Sydney Futures Exchange Clearing House PTY. Ltd.; the Toronto Futures Exchange; the Winnipeg Commodity Exchange; the Winnipeg Commodity Clearing Ltd.; the Vancouver Stock Exchange; and the London Metal Exchange.

## D. SEC MOUs

### 1. *Israel*

Memoranda of Understanding were also entered into by the Securities and Exchange Commission and foreign securities regulators in 1996. On February 13, 1996, SEC Chairman Arthur Levitt and Israel Securities Authority Chairman Arie Mientkavich signed a memorandum of understanding. Under the terms of this MOU the signatories agree to provide mutual assistance in enforcement of the respective securities laws of each nation. The two regulators agreed to utilize "their best efforts to coordinate cross-border securities offerings by U.S. and Israeli issuers and to provide mutual assistance in enforcement and administrative matters."[7]

### 2. *Egypt*

The MOU between the United States SEC and Israel was the 20th MOU entered into by the United States. Two days earlier the United States Securities and Exchange Commission signed a Memorandum of Understanding with its Egyptian counterpart. The MOU with Egypt "formalizes a cooperative and consultative relationship between U.S. and Egyptian authorities."

7. *SEC, Israeli Regulator Announce Signing of Mutual Assistance MOU*, 28 Sec. Reg. & L. Rep. (BNA) No. 7, at 217 (Feb. 16, 1996).

The SEC also agreed to "consult with, and provide technical assistance to, the CMA concerning the development of the Egyptian securities-regulatory system." Pursuant to the MOU, the two parties established a framework for cooperation for consultation "regarding other matters of mutual interest . . ., including regulatory and enforcement issues." This MOU was the first of its kind entered into by the SEC and an emerging capital market in the Middle East.[8]

3. *Germany*

The U.S. Securities and Exchange Commission and Germany's Bundesaufsichtsamt fur das Kreditwesen (Federal Bank Supervisory Authority) agreed in January 1996 to the establishment of a supervisory framework. This framework will allow German bank affiliates of U.S. broker-dealers to utilize the data processing centers of their U.S. parent banks. U.S. broker-dealers will now be able to consolidate their data processing yet still satisfy German banking authorities' supervisory and inspection requirements.[9]

### E. International Organization of Securities Commissions (IOSCO)

The International Organization of Securities Commissions (IOSCO) held its twenty-first annual meeting in Montreal in September 1996. At this meeting securities regulators from 136 countries agreed to a series of 20 recommendations to promote client asset protection.[10]

An earlier IOSCO meeting in May 1996 resulted in an agreement by international securities regulators to establish five common securities offenses under the criminal laws of their respective countries. By adopting common criminal securities laws member states can cooperate and not become havens for illegal securities activities.

The five agreed upon common securities offenses are: insider trading, disseminating inaccurate information, divulging professional secrets, misleading clients (intentionally or otherwise), and market manipulation. The members still differ widely in enforcement and investigatory authority including rights of inspection of financial records of broker dealers.[11]

## II. International Securities Issues—Judicial Opinions

### A. U.S. Supreme Court

In 1996, the U.S. Supreme Court granted *certiorari* in *Dunn and Delta Consultants, Inc. v. Commodity Futures Trading Commission*. This action tests the jurisdiction of the Commodity Futures Trading Commission over foreign currency options not traded on the "regular" exchanges.[12] A customer of Delta Consultants alleges a loss of $189 million due to fraudulent activities in foreign currency option trading. Delta Consultants Inc. maintains that the CFTC lacks jurisdiction to bring the enforcement action.[13]

8. *SEC Announces MOU with Egypian Authorities*, 28 Seg. Reg. & L. Rep. (BNA) No. 7, at 217 (Feb. 16, 1996).

9. *Framework Set Between SEC and Germany's Banking Authority*, 9 Int'l Sec. Reg. Rep. (Buraff) No. 3 (Jan. 15, 1996).

10. *IOSCO Comes of Age*, Financial Regulation Report, Oct. 1996, *available in* Lexis News Library, FRR File.

11. *Warsaw Meeting Focuses on "Common Offenses," Increasing Police Powers*, 9 Int'l Sec. Reg. Rep. (Buraff) No. 14 (June 17, 1996).

12. 117 S. Ct. 290 (1996).

13. *Id.*

The U.S. Supreme Court declined to grant *certiorari* to a challenge of the global jurisdiction of the United States courts over securities fraud in United States markets. The court refused to disturb the decision of the Second Circuit Court of Appeals in securities fraud claims arising from London Stock Exchange transactions in the stock of a London-based conglomerate, *LEP Group PLC v. Itoba Ltd.*[14]

### B. Second Circuit

In May 1995 the Second Circuit reinstated the complaint of Itoba Ltd. Itoba Ltd is an off-shore subsidiary of A.D.T. Ltd., a subsidiary of A.D.T. Securities Systems Inc. Plaintiffs assert that they purchased shares in LEP Group PLC on the London Stock Exchange. As part of a plan to create a U.S. market for common stock, LEP deposited approximately 13 million of 136 million shares in an American depository in 1988. This depository then issued an American Depository Receipt for each five shares of LEP common stock on deposit. The American Depository Receipts (ADRs) were traded on the National Association of Securities Dealers Automated Quotation System (NASDAQ) and exposed LEP to the U.S. securities laws.

Itoba asserted that the defendants failed to disclose in its securities filings with the SEC that LEP was engaged in high risk investments and speculative businesses and thereby violated Section 10b of the 1934 Securities and Exchange Act. Plaintiff also asserted that LEP director William Berkley, a U.S. citizen, had engaged in insider trading in LEP securities in the United States the same day that Itoba had purchased a large block of shares in London. Itoba maintained it would not have made the purchase if Berkley had complied with his duty to disclose material nonpublic information before trading.[15]

The Second Circuit held that "inevitably, there was a direct linkage between the prices of the ADRs representing five ordinary shares and the prices of the single ordinary shares themselves. If the ordinary share price fell on the London Exchange, the market price of an ADR would decrease in similar manner, and visa [*sic*] versa."[16]

## III. International Securities Enforcement Actions

### A. Gillette–Duracel Merger

There was limited international securities enforcement activity in 1996. One of the most notable involved insider trading relating to the Gillette acquisition of Duracell. The SEC alleged that the defendants purchased Duracell call options while in possession of material nonpublic information concerning a proposed merger between The Gillette Company ("Gillette") and Duracell. The insider trading was executed in accounts held by Banca della Svizzera Italiana (BSI), of Lugano, Switzerland, at the Pershing Division of Donaldson, Lufkin & Jenrette Securities Corp. and Nominees (Bahamas) Ltd. of Nassau, Bahamas, at Prudential Securities Incorporated.[17]

### B. Gitano Group

Another insider trading investigation involving trading via foreign accounts involved corporate officers of Gitano Group. In *SEC v. Dabab*,[18] the defendants were accused of trading securities

14. 58 F.3d 50 (2d Cir. 1995), *cert. denied*, 116 S. Ct. 702 and 116 S. Ct. 703 (1996).
15. *Id.*
16. *Itoba, Ltd., v. LEP Group PLC*, 54 F.3d 118 (2d Cir. 1995).
17. *Id.*
18. *Certain Purchasers of the Call Options of Duracell Int'l, Inc.*, No. 96 Civ. 7017, 1996 WL 559938 (S.D.N.Y. Oct. 2, 1996).

of Gitano via accounts in foreign banks in early 1992. The material, nonpublic information concerned the company's earnings, and disclosure of a threat to a material line of credit. In December 1996 the defendants agreed to pay the SEC over $1 million in disgorgement, interest, and penalties while neither admitting nor denying their guilt.

### C. Daiwa Bank

The investigation of Japan-based Daiwa Bank securities violations continued in 1996. In February 1996, the United States Attorney's Office for the Southern District of New York announced its decision to drop four counts from its original criminal indictment against Daiwa Bank Ltd. over the institution's alleged coverup of $1.1 billion in losses. The losses stem from the allegedly unauthorized government bond trading of a trader in the New York branch office of Daiwa.[19] Prosecutors moved to have the four counts dismissed, including charges of filing false records, because the counts were all based on alleged misconduct of the bank that occurred before November 1991. The statute was not applicable to U.S. branches of foreign banks prior to that date. Daiwa still faces criminal charges of conspiracy to defraud the Federal Reserve Board; mail and wire fraud; obstruction of bank examinations; falsifying bank records; and misprision of felonies.

## IV. International Securities Litigation—*Allen v. Lloyd's of London*

One of the most hotly contested international securities disputes of 1996 stemmed from the reorganization efforts of international insurer Lloyd's of London. In 1995, Lloyd's of London announced a $22 billion "Plan for Reconstruction and Renewal" to restructure the Lloyd's market's reinsurance needs and to revitalize the market. The Plan included an offer by Lloyd's managers to settle, for $4.8 billion, all intra-market disputes, including existing and potential lawsuits by "Names," members of the Lloyd's market who underwrite insurance there. Ninety-three American Names filed an action in the Eastern District of Virginia under United States securities laws to compel Lloyd's to disclose more financial information about its proposed plan. The Names also sought a preliminary injunction prohibiting Lloyd's from forcing American Names to make "an irrevocable election respecting their investment" by an August 28, 1996, deadline established by Lloyd's.[20]

The plaintiff(s)'s motion for a preliminary injunction was granted on August 23, 1996. The district court ordered Lloyd's to make additional disclosures to comply with Section 14(a) of the Securities Exchange Act of 1934 by September 23, 1996, and prohibited Lloyd's from taking steps to collect any amounts from American Names pending completion of the disclosure.

A panel of the Fourth Circuit Court of Appeals reversed the opinion of the district court. The Circuit Court held that "the contractual provisions among the parties selecting the law of and a forum in the United Kingdom should be enforced." Those contractual provisions specify that "any dispute and/or controversy of whatsoever nature arising out of or relating to" Names' participation in Lloyd's be submitted to the exclusive jurisdiction of the British courts and that British law govern all matters referred to in the General Undertaking, including the parties' "rights and obligations . . . arising out of or relating to" the Names' participation in Lloyd's."[21]

19. S96 Civ. 9498 (S.D.N.Y. December 17, 1996).
20. *United States v. Daiwa Bank Ltd.* (S.D.N.Y.), 95 CR 947, February 9, 1996.
21. *Allen v. LLoyd's of London*, 94 F.3d 923 (4th Cir. 1996).

The court concluded that enforcement of the parties' forum selection and choice of law provisions in this case would not subvert the United States securities laws' policy of prohibiting fraud. They determined that British law afforded adequate protection to American investors and that the policies of the United States securities laws do not override the parties' choice of forum and law for resolving disputes in this case.

In remanding the case to the district court, the Fourth Circuit announced, "Moreover, we do not believe that Congress intended that the disclosure requirements of the United States securities law be exported and imposed as governing principles on markets conducted entirely in other countries simply because membership in such markets is solicited in the United States."[22]

The Fourth Circuit held that Lloyd's settlement offer was not subject to the disclosure requirements of Section 14(a) and that Lloyd's Plan for Reconstruction and Renewal was neither a security nor a solicitation in respect of a security. Therefore, the plan was not subject to the United States securities laws.

22. *Id.*