

Comments

Carnero v. Boston Scientific Corporation: Interpreting the Extraterritorial Effect of the Civil Whistleblower Protection Provision of the Sarbanes-Oxley Act

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EVERY YEAR, PEOPLE THROUGHOUT THE WORLD invest trillions of dollars in the United States securities markets.¹ In 2001, investor confidence was shaken when Enron, the seventh largest company on Fortune Magazine's list of the top 500, filed for Chapter Eleven bankruptcy in United States Bankruptcy Court.² To restore public confidence in the safety of the United States securities markets, Congress hastily enacted the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley Act").³ A key component of this legislation was the civil whistleblower protection provision⁴ ("Whistleblower Provision"), which created a federal cause of action for employees of publicly-traded companies,

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1. See NEW YORK STOCK EXCHANGE EDUCATIONAL SERVICES DEPARTMENT, A GUIDE TO THE NYSE MARKETPLACE (2006), available at http://www.nyse.com/pdfs/nyse_bluebook.pdf. As of June 30, 2006, the shares listed on the New York Stock Exchange represented a total global market capitalization of over \$22.6 trillion. *Id.*

2. J. Michael Anderson, Enron: A Select Chronology of Congressional, Corporate, and Government Activities, at Summary (Congressional Research Service Report for Congress RL31364, 2002); see also Corinne A. Falencki, Note, *Sarbanes-Oxley: Ignoring the Presumption Against Extraterritoriality*, 36 GEO. WASH. INT'L L. REV. 1211, 1212-13 (2004).

3. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002) (codified in scattered sections of 11 U.S.C., 15 U.S.C., 18 U.S.C., and 28 U.S.C.). See *infra* Part II.A.2 for further discussion of the purpose of the Sarbanes-Oxley Act.

4. 18 U.S.C.A. § 1514A (West 2005).

like Enron, who were fired in retaliation for “blowing the whistle” on fraudulent accounting practices and other corporate wrongdoing.⁵ By offering employees of publicly-traded companies the same protections afforded government whistleblowers, Congress sought to decrease the chances that another Enron-like scandal would threaten investor confidence in the United States securities markets.⁶

In drafting the Whistleblower Provision, Congress failed to consider potential complications arising from an increasingly interconnected world. The provision does not explicitly protect, nor does it explicitly exempt from protection, employees working abroad for foreign subsidiaries of United States corporations. Absent explicit statutory language, the courts must employ other methods to determine whether extraterritorial application is appropriate. Should the protection of the Whistleblower Provision apply to employees retaliated against for reporting the corporate fraud of subsidiary companies, allowing such employees to bring suit against the United States parent company? In an increasingly global economy, can the intent of the provision be effectuated without such application? The First Circuit was called upon to answer these questions in *Carnero v. Boston Scientific Corp.*⁷

The action in *Carnero* stemmed from an employment dispute between plaintiff Ruben Carnero and defendant Boston Scientific Corporation (“BSC”).⁸ Carnero alleged that BSC terminated his employment in retaliation for whistleblowing when he informed BSC that a number of its Latin American subsidiaries had created false invoices and inflated sales figures.⁹ Carnero filed suit in the United States District Court for the District of Massachusetts under the Whistleblower Provision of the Sarbanes-Oxley Act.¹⁰ BSC argued that Carnero, as an Argentinean citizen working for its Latin American subsidiaries in Brazil, was not entitled to file suit under the Whistleblower Provision.¹¹

In deciding that the Whistleblower Provision did not have extraterritorial effect, the First Circuit employed a presumption against ex-

5. *Id.*

6. 148 CONG. REC. S1788 (daily ed. Mar. 12, 2002) (statement of Sen. Leahy).

7. 433 F.3d 1 (1st Cir. 2006).

8. *See id.* at 2.

9. *Id.*

10. *Carnero v. Boston Scientific Corp.*, No. 04-10031-RWZ, 2004 U.S. Dist. LEXIS 17205, at *1 (Mass. Dist. Ct. 2004) (denying Carnero’s petition for certiorari).

11. *Id.* at *3.

tratorritorial application of congressional action.¹² However, this territoriality presumption is only one of the recently applied approaches for deciding if legislation should have extraterritorial effect—there was nothing to prevent the First Circuit from employing an effects-based analysis in deciding this issue.¹³ At the time *Carnero* was decided, the Supreme Court had embraced both the presumption against extraterritoriality and an effects test without providing guidance as to which approach should govern legislation in the field of securities regulation.¹⁴ This Comment will show that, had the First Circuit employed the effects test, the court could have logically reached the conclusion that the Whistleblower Provision of the Sarbanes-Oxley Act should have extraterritorial effect.

The choice between these two possible approaches has serious implications for the outcome of a case. The territoriality presumption is unnecessarily limiting in many contexts and often does not allow the court to facilitate the underlying congressional intent behind the legislation. In contrast, the effects test allows the court more flexibility and is better suited to deal with unforeseen international applications of legislation. This flexibility allows the court system to uphold congressional intent even when extraterritorial effect is not expressly provided for. The effects test analysis refocuses the inquiry by looking to the location of an action's effect rather than fixating on the physical location of that action.

The existence of competing analyses for determining the extraterritorial effect of United States legislation will inevitably give rise to conflict. Although the First Circuit chose to apply the territoriality presumption, the other circuit courts are free to adopt a competing approach. The Supreme Court's failure to embrace one approach leaves the door open for confusion in the lower courts and will likely lead to conflicting case law. In declining to hear this case, the Supreme Court missed an important opportunity to set the standard for extraterritoriality analysis of legislation in the field of securities regulation.¹⁵ Given the global economy, in which companies routinely operate in numerous countries around the world, the Court must recognize the need to adopt a standard for analyzing the extraterrito-

12. *Carnero*, 433 F.3d at 7.

13. See GARY B. BORN, INTERNATIONAL CIVIL LITIGATION IN UNITED STATES COURTS 595 (John Berger ed., 3d ed., Kluwer Law Int'l 1996).

14. *Id.* See *infra* Part II for a discussion of these two approaches recently adopted by the Supreme Court to analyze the extraterritorial effect of congressional legislation.

15. *Carnero v. Boston Scientific Corp.*, No. 05-1397, 2006 U.S. LEXIS 4956, at *1 (2006).

riality of legislation in the field of securities regulation. In recognition of the complexity of securities regulation, the Court should embrace the flexible approach of the effects test.

Part I of this Comment presents the circumstances of Ruben Carnero's employment with BSC, the termination of his employment, and the ensuing litigation. Part II introduces the territoriality presumption and the effects test, both of which were recently employed by the Supreme Court in analyzing the extraterritorial effect of congressional action. The facts of *Carnero* will be analyzed under each of these approaches to illustrate the limitations of the territoriality presumption and the benefits of the effects test analysis for determining the extraterritorial effect of the Whistleblower Provision. Part III concludes by encouraging the Supreme Court to adopt the effects test analysis to determine the extraterritorial effect of the Whistleblower Provision or, alternatively, to adopt the test as a standard for the analysis of the extraterritorial effect of legislation enacted in the field of securities regulation.

I. *Carnero v. Boston Scientific Corporation: The First Circuit's Decision Not to Protect Those Who "Blow the Whistle" Outside the United States*

Ruben Carnero, a citizen of Argentina, resided in Brazil at the time of the First Circuit's decision.¹⁶ Between 1997 and 2003, he was employed by two Latin American subsidiaries of BSC, a Delaware corporation headquartered in Massachusetts.¹⁷ In 1997, Carnero began working for Boston Scientific Argentina S.A. ("BSA"), the Argentinian subsidiary of BSC.¹⁸ He entered into an employment agreement with BSA in Argentina, although the agreement was negotiated in many countries, including the United States.¹⁹ The agreement was governed by the laws of Argentina and specified BSA's headquarters in Buenos Aires as Carnero's place of work.²⁰ In 2001, Carnero accepted concurrent employment with the Brazilian subsidiary of BSC, Boston Scientific Do Brasil Ltda. ("BSB").²¹ In the course of his employment, Carnero discovered that BSA and BSB were involved in creating false invoices and improperly inflating sales figures, and he

16. *Carnero*, 433 F.3d at 2.

17. *Id.*

18. *Id.*

19. *Id.*

20. *Id.*

21. *Id.*

reported this accounting misconduct to BSC.²² Carnero asserted that he was terminated from BSB in August 2002 and BSA in April 2003 in retaliation for reporting the accounting misconduct of BSB and BSA to supervisors at BSC.²³

Following the termination of his employment, Carnero initiated three actions, including an administrative complaint against BSC with the United States Department of Labor.²⁴ In the administrative complaint, Carnero alleged retaliatory termination and other instances of discrimination in violation of the Whistleblower Provision.²⁵ In December 2003, the Department of Labor issued a preliminary decision dismissing the administrative complaint after finding that the Whistleblower Provision did not apply to employees, such as Carnero, working outside of the United States.²⁶ Carnero then filed a complaint in the United States District Court for the District of Massachusetts, seeking de novo judicial review of the claim.²⁷ Carnero brought suit under the Whistleblower Provision, which creates both the administrative complaint procedure with the Department of Labor and “a federal civil cause of action, designed to protect the ‘employees of publicly traded companies’ who lawfully ‘provide information . . . or otherwise assist in an investigation regarding any conduct which the employee believes constitutes a violation’ . . . of any rule or regulation of the Securities and Exchange Commission” (“SEC”) or any other fraud-related provision of federal law.²⁸ The district court dismissed

22. *Id.* at 2–3.

23. *Id.*

24. *Carnero v. Boston Scientific Corp.*, No. 04-10031-RWZ, 2004 U.S. Dist. LEXIS 17205, at *1 (Mass. Dist. Ct. 2004). The other actions initiated by Carnero at this time included a conciliation proceeding in Argentina seeking statutory severance and an eight-count complaint against BSC in the United States District Court for the District of Massachusetts that was dismissed for lack of jurisdiction. *Carnero*, 433 F.3d at 3.

25. *Carnero*, 433 F.3d at 3.

26. *Id.*

27. *Id.* at 3–4.

28. *Id.* at 5 (quoting 18 U.S.C.A. § 1514(A)(a) (West 2005)). The full text of the Whistleblower Provision provides:

Whistleblower protection for employees of publicly traded companies. No company with a class of securities registered under section 12 of the Securities Exchange Act of 1934 (15 U.S.C. § 781), or that is required to file reports under section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. § 78o(d)), or any officer, employee, contractor, subcontractor, or agent of such company, may discharge, demote, suspend, threaten, harass, or in any other manner discriminate against an employee in the terms and conditions of employment because of any lawful act done by employee—

(1) to provide information, cause information to be provided, or otherwise assist in an investigation regarding any conduct which the employee reason-

Carnero's Whistleblower Provision claim.²⁹ The court held that Carnero, as an Argentinean citizen who resided and worked in Brazil for the Latin American subsidiaries of BSC, could not sue BSC under the Whistleblower Provision for allegedly retaliatory conduct that took place outside the United States because the provision was without extraterritorial effect.³⁰

On appeal, the First Circuit was called upon to decide if the Whistleblower Provision should be interpreted to have extraterritorial effect, extending its protection to cover foreign employees complaining of misconduct abroad by overseas subsidiaries.³¹ If such extraterritorial effect were found, covered employees in foreign countries, such as Carnero, would be permitted to bring suit under the Whistleblower Provision against the United States parent company in response to retaliatory termination by a foreign subsidiary.³² The First Circuit assumed, without deciding, that Carnero was a covered employee for the purposes of the Whistleblower Provision and that there was evidence that his employment was terminated in retaliation for protected conduct.³³

ably believes constitutes a violation of section 1341, 1343, 1344, or 1348 [18 U.S.C. §§ 1341, 1343, 1344, or 1348], any rule or regulation of the Securities and Exchange Commission, or any provision of Federal law relating to fraud against shareholders . . . ; or

(2) to file, cause to be filed, testify, participate in, or otherwise assist in a proceeding filed or about to be filed (with any knowledge of the employer) relating to an alleged violation of section 1341, 1343, 1344, or 1348 [18 U.S.C. §§ 1341, 1343, 1344, or 1348], any rule or regulation of the Securities and Exchange Commission, or any provision of Federal law relating to fraud against shareholders.

18 U.S.C.A. § 1514A(a) (West 2005).

29. *Carnero*, 433 F.3d at 4.

30. *Id.*

31. *Id.* at 6–7.

32. *Id.* at 6. See generally John B. Chiara & Michael D. Orenstein, Note, *Whistler's Nocturne in Black and Gold—The Falling Rocket: Why the Sarbanes-Oxley Whistleblower Provision Falls Short of the Mark*, 23 HOFSTRA LAB. & EMP. L.J. 235 (2005) for a discussion of the requirements to maintain an action under the Whistleblower Provision. The plaintiff must prove his or her prima facie case by showing “by a preponderance of the evidence that (1) she engaged in protected activity; (2) the employer knew of the protected activity; (3) she suffered an unfavorable personnel action; and (4) circumstances exist to suggest that the protected activity was a contributing factor to the unfavorable action.” *Id.* at 260 (citing *Collins v. Beazer Homes, USA, Inc.*, 334 F. Supp. 2d 1365, 1375 (N.D. Ga. 2004)). If the plaintiff meets this burden, the burden shifts to the defendant to show that they would have taken the unfavorable personnel action even if the protected activity had not occurred. *Id.*

33. *Carnero*, 433 F.3d at 6. In *Carnero*, the court discussed two theories under which Carnero may have been an “employee” of BSC for the purposes of seeking relief under the Whistleblower Provision. *Id.* Carnero first claimed that he was supervised by BSC personnel

In deciding whether the Whistleblower Provision applied extraterritorially, the First Circuit considered the text of the Sarbanes-Oxley Act, the legislative history surrounding its enactment, past precedent in which legislation had been determined not to have extraterritorial effect, and the policies both in favor and against extending the effect of the Whistleblower Provision.³⁴ After a detailed analysis, the court determined that the Whistleblower Provision did not reflect the “necessary clear expression of congressional intent” to extend the reach of the provision to foreign employees working outside of the United States.³⁵

II. Imparting Extraterritorial Effect to the Whistleblower Provision: Should Legislation in the Field of Securities Regulation Be Limited by the Presumption Against Extraterritorial Effect?

In recent decisions, the Supreme Court has embraced two different approaches to analyze the extraterritorial effect of congressional legislation. In 1991, the Supreme Court decided *Equal Employment Opportunity Commission v. Arabian American Oil Co.* (“*Aramco*”).³⁶ The Court applied the traditional territoriality presumption analysis under which congressional legislation is assumed to apply only within the United States unless Congress expressly provides for the legislation to apply extraterritorially.³⁷ The Court determined that Title VII of the Civil Rights Act of 1964³⁸ did not apply to regulate the employment practices of a United States company that employed a United States citizen to work in Saudi Arabia.³⁹ A short two years later, the Supreme Court decided *Hartford Fire Insurance Co. v. California*,⁴⁰ in which the

working at the company’s Massachusetts headquarters, and that this interaction made him an employee of BSC as well as an employee of the company’s foreign subsidiaries. *Id.* In addition, the First Circuit also recognized, in dicta, that Carnero’s employment with BSA and BSB may qualify him as an employee of BSC under the Department of Labor regulations defining “employee” for the Whistleblower Provision as those “presently or formerly working for a [publicly-traded] company or company representative.” *Id.* (quoting 29 C.F.R. § 1980.101 (2005)). The court opined that “[i]f BSA and BSB were agents of BSC, as seems quite possible, their own employee would fit this definition of the parent’s ‘employee.’” *Id.* This Comment will adopt the First Circuit’s assumptions on this point.

34. *Id.* at 9–18.

35. *Id.* at 18.

36. 499 U.S. 244 (1991).

37. *Foley Bros., Inc. v. Filardo*, 336 U.S. 281, 285 (1949).

38. The Civil Rights Act of 1964, Pub. L. No. 88-352, tit. VII, 78 Stat. 241 (1964) (codified as amended in pertinent part at 42 U.S.C. §§ 2000e to 2000e-17 (2000)).

39. *Aramco*, 499 U.S. at 259.

40. 509 U.S. 764 (1993).

Court adopted an effects test approach to hold that provisions of the Sherman Act could be applied extraterritorially if they were meant to affect and did produce an effect in the United States.⁴¹ In deciding *Hartford Fire Insurance*, the Supreme Court made no reference to the territoriality presumption that it embraced in *Aramco* just two years earlier.⁴² In declining to hear *Carnero* and, thereby, declining to clarify which of these competing approaches should be used to determine the extraterritorial effect of legislation in the field of securities regulation, the Supreme Court opened the door for confusion among lower courts and litigants.⁴³ This potential confusion can be demonstrated through an analysis of *Carnero* under both the territoriality presumption, as employed by the First Circuit, and the effects test, which remains a viable alternative method of analysis.

A. Analysis #1: The Territoriality Presumption as Applied to the Whistleblower Provision

The territoriality presumption is based on two recognized principles of law in the United States. The first principle sets forth Congress's undisputed authority to enforce its laws beyond the territorial jurisdiction of the United States.⁴⁴ However, this principle is tempered by the equally accepted principle that "legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States."⁴⁵ This second principle is the foundation of the territoriality presumption.

Determining whether Congress intended to exercise its recognized authority to grant legislation extraterritorial effect is a matter of statutory interpretation.⁴⁶ Where congressional action is silent as to its territorial reach and Congress manifests no intent to extend its reach beyond domestic borders, the territoriality approach employs a presumption against extraterritorial effect.⁴⁷ This presumption assumes that Congress is primarily concerned with enacting legislation to deal with domestic conditions.⁴⁸ The territoriality presumption also "reflects the principle of international comity, under which the United

41. *Id.* at 796.

42. BORN, *supra* note 13, at 595.

43. *Id.*

44. *Aramco*, 499 U.S. at 248.

45. *Foley Bros., Inc. v. Filardo*, 336 U.S. 281, 285 (1949).

46. *Aramco*, 499 U.S. at 248.

47. *Id.*

48. *Foley Bros.*, 336 U.S. at 285.

States should avoid interference with the laws of another sovereign over conduct occurring within its territory.”⁴⁹

Although the territoriality presumption typically operates to limit the reach of legislation to application only within the territorial boundaries of the United States unless Congress has expressly conferred extraterritorial authority, there are cases in which the requisite intent has been implied.⁵⁰ As the First Circuit points out in *Carnero*, “in appropriate circumstances Congress’s extraterritorial intent has on occasion been implied without explicit statement in the text or even history.”⁵¹ In determining if implied intent is appropriate, courts typically look to the “context and structure” of a statute as well as “its purpose and ‘all available evidence.’”⁵²

In *Foley Brothers, Inc. v. Filardo*,⁵³ an early case dealing with the presumption against extraterritorial effect and the method of evaluating implied congressional intent, the Supreme Court was called upon to determine if the Federal Eight Hour Law⁵⁴ was applicable to an employment contract in a foreign country.⁵⁵ In *Foley Bros.*, the plaintiff, an American citizen, was employed by the defendant on behalf of the United States in Iran and Iraq.⁵⁶ The plaintiff alleged that he frequently worked more than eight hours per day and filed suit claiming he was entitled to one and one-half times the basic rate of pay for those excess hours under the provisions of the Federal Eight Hour Law.⁵⁷

In deciding *Foley Bros.*, the Supreme Court employed a three-part statutory interpretation analysis to determine if the Federal Eight

49. *Denty v. SmithKline Beecham Corp.*, 907 F. Supp. 879, 882 (E.D. Pa. 1995).

50. Examples of such implied intent include *Hartford Fire Ins. Co. v. California*, 509 U.S. 764, 796 (1993) (holding that the Sherman Act applied to anti-competitive conduct abroad that was “meant to produce and did in fact produce some substantial effect in the United States”), *Schoenbaum v. Firstbrook*, 405 F.2d 200, 208 (2d Cir. 1968) (holding that the Securities Exchange Act had extraterritorial effect “at least when the transactions involve stock registered and listed on a national securities exchange, and are detrimental to the interests of American investors”), and *Vermilya-Brown Co., Inc. v. Connell*, 335 U.S. 377, 390 (1948) (extending the protections of the Fair Labor Standards Act to contractors engaged in construction for the United States government on naval bases located in Bermuda and leased from Great Britain upon determining that the term possession was intended to include such bases).

51. *Carnero v. Boston Scientific Corp.*, 433 F.3d 1, 8 (1st Cir. 2006).

52. *Id.*

53. 336 U.S. 281 (1949).

54. *See id.* at 282 (discussing 27 Stat. 340, as amended, 40 U.S.C. §§ 321–26, *repealed by* Work Hours Act of 1962, Pub. L. No. 87-581, title II § 203, 76 Stat. 360 (1962)).

55. *Id.* at 283–84.

56. *Id.* at 283.

57. *Id.*

Hour Law should have extraterritorial effect.⁵⁸ The three-part test employed by the *Foley Bros.* court consisted of: (1) a textual analysis of the language, (2) an examination of the legislative history, and (3) an examination of the administrative interpretations throughout the development of the Federal Eight Hour Law.⁵⁹ After conducting this statutory analysis, the *Foley Bros.* court held that the Federal Eight Hour Law did not have extraterritorial effect.⁶⁰

As *Carnero* raised a similar question of statutory interpretation, the First Circuit used a similar analysis to the one employed by the Supreme Court in *Foley Bros.* to determine if, under the territoriality presumption, the Whistleblower Provision should have extraterritorial effect.⁶¹ In addition to analyzing the three factors addressed by the *Foley Bros.* court, the First Circuit considered policy and precedent in its ultimate determination that the Whistleblower Provision did not demonstrate the requisite congressional intent to endorse extraterritorial application.⁶²

1. The Text of the Whistleblower Provision Does Not Demonstrate Intent to Impart Extraterritorial Effect

The first step in statutory interpretation is to conduct a close reading of the statute in question.⁶³ *Carnero* filed suit under the Whistleblower Provision, which provides “a federal civil cause of action, designed to protect the ‘employees of publicly traded companies’ who lawfully ‘provide information . . . or otherwise assist in an investigation regarding any conduct which the employee believes constitutes a violation’ . . . of any rule or regulation of the Securities and Exchange Commission” or any other fraud-related provision of federal law.⁶⁴

58. *Id.* at 285–91.

59. *Id.*

60. *Id.* The Court held that the text of the Eight Hour Law did not provide the Court with a showing that Congress intended extraterritorial application of the provision. *Id.* at 285. Additionally, the Court held that the legislative history demonstrated that Congress was primarily concerned with domestic labor conditions when it enacted the Eight Hour Law. *Id.* at 286. The Court also found that, despite one Executive Order which seemed to acknowledge the possibility of extraterritorial application, the administrative interpretations of the Eight Hour Law did not support a finding of extraterritorial application. *Id.* at 288.

61. 433 F.3d 1, 9–15 (1st Cir. 2006).

62. *Id.* at 15–18.

63. See, e.g., *Foley Bros.*, 336 U.S. at 285.

64. *Carnero*, 433 F.3d at 5 (quoting 18 U.S.C.A. § 1514A(a) (West 2005)). See *supra* note 28 for the full text of the Whistleblower Provision.

Judicial construction of congressional action should start “with the assumption that the legislative purpose is expressed by the ordinary meaning of the words used.”⁶⁵ Although the Whistleblower Provision is silent as to its territorial reach, two textual aspects of the Sarbanes-Oxley Act can be read to provide insight into Congress’s intent regarding extraterritorial application of the provision. First, Congress failed to consider problems arising from overseas application of the Whistleblower Provision. This is especially persuasive in light of the fact that such difficulties were considered in other sections of the Sarbanes-Oxley Act. Second, Congress expressly provided for the extraterritorial application of a criminal whistleblower statute elsewhere in the Sarbanes-Oxley Act (“Criminal Whistleblower Provision”).⁶⁶

In enacting the Sarbanes-Oxley Act, Congress recognized the difficulties that its application to persons abroad would present and expressly dealt with those difficulties in several sections of the Act.⁶⁷ One such instance is the accounting provision contained in section 106 of the Sarbanes-Oxley Act.⁶⁸ In recognition of the difficulties of enforcing United States regulatory statutes abroad, this section permits the SEC to exempt foreign accounting firms from the Sarbanes-Oxley Act as it “determines necessary or appropriate in the public interest or for the protection of investors.”⁶⁹ The inclusion of this exemption demonstrates that Congress recognized the need to explicitly provide for the extraterritorial application of the provisions of the Sarbanes-Oxley Act and to deal with any difficulties that might arise from applying those provisions abroad.

Congress did not exhibit any such concern over application of the Whistleblower Provision abroad and notably failed to address the difficulties likely to arise from extraterritorial application of the provision. Congress also failed to provide any mechanism that would allow for extraterritorial enforcement of the Whistleblower Provision.⁷⁰ Additionally, Congress did not grant the Department of Labor, the agency charged with receiving and investigating whistleblower claims under the administrative complaint procedure, any powers that would permit extraterritorial investigation of claims.⁷¹ Congressional failure to address administrative issues likely to arise from extraterritorial ap-

65. *Richards v. United States*, 369 U.S. 1, 9 (1962).

66. 18 U.S.C.A. § 1513 (West 2005).

67. *Carnero*, 433 F.3d at 14–15.

68. 15 U.S.C. § 7216(c) (2000).

69. *Id.*

70. *Carnero*, 433 F.3d at 15.

71. *Id.*

plication of the Whistleblower Provision may demonstrate a lack of congressional intent that the provision be granted extraterritorial effect.

Another textual illustration of Congress's intent that the Whistleblower Provision not apply extraterritorially is the *express* grant of extraterritorial jurisdiction in the Criminal Whistleblower Provision.⁷² In interpreting congressional action, it is logical to presume that when "Congress includes particular language in one section of a statute but omits it in another section of the same Act, . . . Congress acts intentionally and purposely in the disparate inclusion or exclusion."⁷³ The Criminal Whistleblower Provision provides an express grant of extraterritorial federal jurisdiction for criminal sanctions against anyone who "takes any action harmful to any person, including interference with the lawful employment or livelihood of any person."⁷⁴ The inclusion of this express grant of extraterritorial jurisdiction demonstrates that Congress considered the possibility that the Sarbanes-Oxley Act would have international implications. Knowing that international issues were likely to arise, Congress constructed statutory language to deal with the problems of extraterritorial jurisdiction and addressed those problems explicitly in the language of the Criminal Whistleblower Provision. This explicit grant of territorial jurisdiction in the Criminal Whistleblower Provision is significant as it transforms the silence of the Whistleblower Provision as to its territorial reach into a *conspicuous* silence under the territoriality presumption and may indicate a lack of intent that the civil provision be granted extraterritorial effect.

Although the Whistleblower Provision is silent as to its territorial reach, the textual construction of both the Whistleblower Provision and the Sarbanes-Oxley Act in general may counsel in favor of finding that Congress did not intend the Whistleblower Provision to apply extraterritorially. Congressional failure to consider the problems arising from extraterritorial application of this provision (when such consid-

72. 18 U.S.C.A. § 1513(d) (West 2005).

73. *Russello v. United States*, 464 U.S. 16, 23 (1983) (citing *United States v. Wong Kim Bo*, 472 F.2d 720, 722 (5th Cir. 1972)).

74. 18 U.S.C.A. § 1513(d)-(e) (West 2005). This section of the Act expressly provides that "[t]here is extraterritorial Federal jurisdiction over an offense under this section." 18 U.S.C.A. § 1513(d). An offense under this section is committed by anyone who "knowingly, with intent to retaliate, takes any action harmful to any person, including interference with the lawful employment or livelihood of any person, for providing to a law enforcement officer or any truthful information relating to the commission or possible commission of any Federal offense . . ." 18 U.S.C.A. § 1513(e).

erations informed the drafting of other provisions of the Sarbanes-Oxley Act) demonstrates a lack of congressional intent that the Whistleblower Provision have extraterritorial effect. Additionally, the explicit provision of extraterritorial effect for the Criminal Whistleblower Provision shows that Congress was concerned with extraterritorial application of certain provisions of the Sarbanes-Oxley Act and legislated to facilitate such application where appropriate.

A close reading of the Whistleblower Provision itself, silent as to its territorial reach, does not provide an answer to whether the provision has extraterritorial effect. However, one is left to question whether this silence was intentional or merely a legislative oversight. Although the text of other sections of the Sarbanes-Oxley Act may be read to support the proposition that the Whistleblower Provision's silence limits its extraterritorial application, it is dangerous to read silence as an affirmative expression of a statute's provisions. When basing a decision on a textual analysis of statutory language, reading textual silence to imply limitations on the statute's application may frustrate congressional intent in enacting the statute.

2. The Legislative History of the Whistleblower Provision Does Not Demonstrate Intent to Impart Extraterritorial Effect

Textual analysis is only the first step in determining if congressional action should be granted extraterritorial effect under the territoriality presumption. When there is no express grant of extraterritorial jurisdiction, a court may also consider the legislation's "purpose and all other available evidence."⁷⁵ The legislative history of the congressional action in question is a key part of this inquiry.

Congress passed the Sarbanes-Oxley Act as a reaction to the sudden collapse of the Enron Corporation in December 2001.⁷⁶ In early 2001, Enron was one of the most prestigious corporations in the United States, with assets totaling over \$49 billion and a ranking by Fortune Magazine as the seventh largest corporation in the United States.⁷⁷ On December 2, 2001, Enron unexpectedly filed for Chapter Eleven bankruptcy in United States Bankruptcy Court.⁷⁸ The next day, Enron announced the layoff of 4000 employees.⁷⁹ In the wake of the filing, the stock price of Enron plummeted, decimating the invest-

75. *See, e.g., Carnero*, 433 F.3d at 8.

76. Falencki, *supra* note 2, at 1211.

77. Anderson, *supra* note 2, at Summary.

78. *Id.* at CRS-18.

79. *Id.*

ments and retirement savings of families throughout the United States.⁸⁰ The ultimate collapse of Enron was largely attributable to individual Enron executives who chose to ignore questionable accounting practices that, temporarily and with disastrous consequences, caused the overvaluation of Enron stock.⁸¹ The investigation following the collapse of Enron brought Arthur Andersen, Enron's accounting firm, into the scandal after it was revealed that the firm destroyed "a significant but undetermined number" of documents relating to its dealings with Enron.⁸²

The collapse of Enron and the subsequent scandal involving Arthur Andersen peaked congressional interest in enacting legislation to combat corporate fraud and regulate corporate financial accounting practices.⁸³ Legislative focus was heightened when over one hundred companies corrected financial results that had already been announced for the first half of 2002.⁸⁴ This nearly doubled the number of corrections averaged in previous decades.⁸⁵ Concerns about the United States securities markets were not limited to domestic investors; the reaction abroad to these scandals led many international investors to be wary of investing on the New York Stock Exchange.⁸⁶ Congress hastily enacted the Sarbanes-Oxley Act in this post-scandal environment both to restore public confidence in the United States securities markets and to monitor and investigate possible acts of corporate fraud and violations of securities regulations.⁸⁷

Senator Leahy introduced the Whistleblower Provision on March 12, 2002.⁸⁸ Senator Leahy emphasized, on behalf of himself and the bill's co-sponsors, the importance of restoring confidence in the integrity of United States markets and the role that the proposed Whistleblower Provision would play in achieving that goal.⁸⁹ His remarks focused, in part, on changes necessary to provide meaningful

80. Falencki, *supra* note 2, at 1213. During the 2001 fiscal year, the value of a share of Enron stock fell from eighty-five dollars to thirty cents. Chiara & Orenstein, *supra* note 32, at 236.

81. Chiara & Orenstein, *supra* note 32, at 236.

82. Anderson, *supra* note 2, at CRS-17.

83. Falencki, *supra* note 2, at 1213. *See also* Mark Jickling, Accounting Problems Reported in Major Companies Since Enron (Congressional Research Service Report for Congress RS21269, 2003).

84. Jickling, *supra* note 83, at CRS-1.

85. *Id.*

86. Falencki, *supra* note 2, at 1213.

87. 148 CONG. REC. S1786 (2002) (statement of Sen. Leahy).

88. *Id.* at S1785.

89. *Id.* at S1786.

whistleblower protection within the United States.⁹⁰ Two perceived problems at the center of the discussion were: (1) the lack of federal protection for employees of publicly-traded companies coming forward to report corporate wrongdoing and (2) the inconsistencies of state law in providing protection for whistleblowers working for publicly-traded companies.⁹¹ The first of these perceived problems stemmed from the fact that federal law protected many government employees from retaliation if they reported wrongdoing, but provided no similar protection for employees of publicly-traded companies who acted in the public interest by reporting fraud or other wrongdoing by the corporation.⁹² The second perceived problem that the Whistleblower Provision was intended to combat was the “patchwork and vagaries of current State laws” that failed to provide consistent protections across state lines.⁹³ Congress designed the Whistleblower Provision to alleviate both of these problems by providing a federal cause of action for employees of publicly-traded companies who were retaliated against after they “blew the whistle” on a company’s fraudulent behavior or other wrongdoing.⁹⁴

Despite the lack of expressed intent to imbue the Whistleblower Provision with extraterritorial effect, the legislative history demonstrates a strong intent that the Sarbanes-Oxley Act, generally, and the Whistleblower Provision, specifically, sweep broadly to protect markets from fraudulent activity that is damaging to investors.⁹⁵ On January 29, 2003, Senator Leahy again addressed the Senate regarding the Whistleblower Provision.⁹⁶ He spoke about a change in the White House’s interpretation of the Whistleblower Provision.⁹⁷ In keeping

90. *See id.* at S1787–S1788.

91. *Id.* at S1788.

92. *Id.*

93. *Id.* The Congressional Record includes an email from one of Enron’s lawyers written in response to a request for legal advice after an Enron employee attempted to report accounting irregularities in August, 2001. *Id.* at S1791. The email reads:

You also asked that I include in this communication a summary of the possible risks associated with discharging (or constructively discharging) employees who report allegations of improper accounting practices: 1. Texas law does not currently protect corporate whistleblowers. The supreme court [sic] has twice declined to create a cause of action for whistleblowers who are discharged

Id. at S1792.

94. *See id.* at S1788.

95. *See generally* 149 CONG. REC. S1725 (2003) (statement of Sen. Leahy); 148 CONG. REC. S1786 (2002) (statement of Sen. Leahy); Chiara & Orenstein, *supra* note 32; Falencki, *supra* note 2.

96. 149 CONG. REC. S1725 (2003).

97. *Id.* Initially, the executive branch narrowly interpreted the Whistleblower Provision to protect only those disclosures made to a congressional committee already con-

with the previously stated purpose, Senator Leahy said that “[t]he law was intentionally written to sweep broadly, protecting any employee of a publicly traded company who took such reasonable action to try to protect investors and the market.”⁹⁸

The Senate discussions regarding the Whistleblower Provision were limited to the benefits of enacting the provision *within* the United States.⁹⁹ Concerns expressed included the domestic problems that led to the collapse of Enron and subsequent scandal involving Arthur Andersen and the need to restore confidence in the United States securities markets.¹⁰⁰ The problems discussed included those relating to disparities among state laws.¹⁰¹ Even the quoted statement above, regarding the intent that the legislation “sweep broadly,” was made in connection with an executive interpretation that would have prevented individual whistleblowers from “[s]imply picking up the phone and calling [his or her] local Senator or Representative to report a case of securities fraud,” but made no reference to application of the provision abroad.¹⁰² The context of Senator Leahy’s statements illustrates the decidedly domestic focus of language that could be interpreted to imply extraterritorial effect. The First Circuit found that these discussions of the Whistleblower Provision were domestic in nature and did not support implying a congressional intent to grant the provision extraterritorial effect.¹⁰³

Limiting the Whistleblower Provision to apply only within the United States, based on legislative inattention to the potential interna-

ducting an authorized investigation. *Id.* Leahy addressed the Senate on January 29, 2003 to report that the executive interpretation had been changed to protect whistleblowers who disclosed information regarding corporate fraud to any member of Congress. *Id.*

98. *Id.*

99. *See* *Carnero v. Boston Scientific Corp.*, 433 F.3d 1, 12–13 (1st Cir. 2006).

100. 148 CONG. REC. S1785–S1786 (2002).

101. 148 CONG. REC. S1788.

102. 149 CONG. REC. S1725 (2003).

103. *Carnero*, 433 F.3d at 14–15. After determining that the legislative history did not support extraterritorial application of the Whistleblower Provision, the First Circuit examined the few administrative decisions dealing with the extraterritorial application of the provision. The Occupational Safety and Health Administration’s regional administrator and the Department of Labor’s Administrative Law Judges held, on at least three occasions, that the Whistleblower Provision did not apply extraterritorially. *Id.* at 17–18 (referencing the three earlier decisions: *Carnero v. Boston Scientific Corp.*, 2004-SOX-22 (OSHA Reg’l Adm’r) (Dec. 19, 2003); *Concone v. Capital One Fin. Corp.*, 2005-SOX-6 (ALJ) (Dec. 3, 2004); *Ede v. Swatch Group*, 2004-SOX-68, 2004-SOX-69 (ALJ) (Jan. 14, 2005)). The Department of Labor, the agency responsible for receiving and investigating administrative whistleblower complaints under the Whistleblower Provision, did not issue a statement of policy on the extraterritorial application of the Whistleblower Provision. *Id.* at 17.

tional implications of the provision, seems troubling and counterintuitive in light of the important policy concerns raised by the Enron scandal and Congress's stated purpose in crafting the legislation. Congress intended to enact broadly-sweeping legislation to protect employees of publicly-traded companies who served the public interest by reporting corporate improprieties. Although the lack of explicit congressional attention to the extraterritorial application of the statute is undeniable, it is less clear whether this inattention was purposeful or merely a congressional oversight. Nonetheless, the lack of expressed congressional intent makes this troubling outcome proper under the territoriality presumption.

3. The Lingering Questions of Policy: When, if Ever, Can the Territoriality Presumption Be Overcome?

a. The Overarching Purpose of the Whistleblower Provision Will Not Be Accomplished Without Extraterritorial Effect

As previously discussed, the Sarbanes-Oxley Act was enacted as a means of investor protection, guarding against fraud in order to protect investors and the integrity of the United States securities markets.¹⁰⁴ The Whistleblower Provision serves this purpose by preventing retaliation against employees who come forward to provide information and participate in investigations of frauds committed by their employers.

In *Schoenbaum v. Firstbrook*,¹⁰⁵ the Second Circuit recognized the importance of such policy concerns regarding United States securities markets.¹⁰⁶ The court found that Congress intended the Securities Exchange Act of 1934¹⁰⁷ to have extraterritorial reach, regulating transactions outside the United States, at least when the transactions involve stocks listed on a United States securities market and are detrimental to the interests of American investors.¹⁰⁸ The court based its decision on policy concerns and cited the importance of extraterritorial application of the Securities Exchange Act to protect domestic investors purchasing foreign securities and to "protect the domestic securities market from the [negative] effects of improper foreign

104. *Id.* at 11. See also SEC Release No. 33-8177 (Jan. 31, 2003).

105. 405 F.2d 200 (2d Cir. 1968).

106. *Id.* at 206.

107. Securities Exchange Act of 1934, Pub. L. No. 73-291, 48 Stat. 881 (1934) (codified as amended at 15 U.S.C. §§ 78a-78mm (2000)).

108. *Schoenbaum*, 405 F.2d at 208.

transactions in . . . [United States] securities.”¹⁰⁹ The court stated that “neither the usual presumption against extraterritorial application of legislation nor the specific language . . . show Congressional intent to preclude application of the Exchange Act . . . when extraterritorial application of the Act is necessary to protect American investors.”¹¹⁰

The reasoning employed by the court in *Schoenbaum* supports finding implied congressional intent for extraterritorial effect of the Whistleblower Provision because the protection of United States investors and markets cannot be fully accomplished without extraterritorial application of the provision.¹¹¹ In the global economy, many United States parent companies have spawned fully functioning foreign subsidiaries beyond the traditional territorial reach of congressional legislation. There can be little doubt that frauds uncovered by whistleblowers employed by these foreign subsidiaries present a threat to the integrity of United States securities markets comparable to the threat created by frauds committed domestically by the United States parent company.¹¹² To the same extent that extraterritorial application of the Securities Exchange Act of 1934 was necessary to protect investors in *Schoenbaum*, extraterritorial application of the Whistleblower Provision is required to protect United States investors and securities markets. Without such effect, investors and markets will be more vulnerable to frauds committed by foreign subsidiaries of United States parent companies.

In deciding *Schoenbaum*, the Second Circuit inverted the typical inquiry by focusing not on whether Congress *intended* to extend jurisdiction, but rather on whether they *intended to preclude* jurisdiction.¹¹³ This outcome-determinative approach was presumably adopted in order to effectuate the protection of American investors, but it is not the inquiry mandated by the territoriality presumption. The court may have taken this more liberal approach to finding implied intent based

109. *Id.* at 206.

110. *Id.*

111. *Carnero v. Boston Scientific Corp.*, 433 F.3d 1, 8 (1st Cir. 2006).

112. The First Circuit recognized the impact frauds against foreign subsidiaries could have on the United States parent company, but did not find this sufficiently persuasive to deviate from the presumption against extraterritorial application of the Whistleblower Provision. *Id.* at 8. See *infra* Part II.B.1.a for a discussion of the impact foreign subsidiaries of companies listed in the United States securities markets have on the performance of the parent company.

113. See *supra* note 110 and accompanying text (discussing the court’s view that the presumption against extraterritorial effect and the text of the Act do not “show Congressional intent to *preclude* [extraterritorial] application” *Schoenbaum*, 405 F.2d at 206 (emphasis added)).

on specific language included in section two of the Securities Exchange Act,¹¹⁴ which states that “transactions in securities . . . are affected with a national public interest which makes it necessary to provide for regulation and control of such transactions and of practices . . . and to impose requirements necessary to make such regulation and control *reasonably complete and effective*.”¹¹⁵ A textual analysis of section two of the Securities Exchange Act could lead to the reasonable conclusion that Congress intended all provisions of that Act to have the necessary territorial jurisdiction to further the “national public interest” in regulating transactions in securities.¹¹⁶ This interpretation of other language in the Securities Exchange Act could provide the basis for the inverted inquiry employed by the *Schoenbaum* court.¹¹⁷

The purpose of the Sarbanes-Oxley Act—to provide comprehensive protection for United States investors and guard the integrity of United States securities markets—may be frustrated unless the Whistleblower Provision is granted extraterritorial effect. As previously discussed, Congress enacted the Sarbanes-Oxley Act in the wake of one of the most devastating corporate scandals in recent history. Thus, it is reasonable to conclude that legislators would have wanted to uphold the purpose of the act by granting the Whistleblower Provision the necessary territorial reach to fully protect investors in the United States securities markets. However, under the territoriality presumption, the purpose of the Sarbanes-Oxley Act is but one consideration, and it is not sufficient to overcome the presumption against finding extraterritorial effect when Congress has not expressly granted such broad territorial reach.

b. Congress Is Capable of Crafting Legislation that Has Extraterritorial Effect

Before implying a congressional intent where one is not clearly expressed, the courts should consider that Congress is aware of the need to make a clear statement that it intends legislative action to apply extraterritorially. As discussed in *Aramco*, congressional recognition of the need to make a clear statement that a statute is intended to

114. 15 U.S.C. § 78b (2000).

115. *Id.* (emphasis added).

116. *Id.*

117. The *Schoenbaum* court may also have been influenced by a line of cases involving antitrust litigation and employing the effects test approach to analyzing extraterritoriality. *See infra* Part II.B.

apply to foreign conduct is demonstrated by the numerous occasions in which legislation contains an express grant of extraterritorial jurisdiction.¹¹⁸ If, through some act of legislative oversight, a statute that is intended to apply extraterritorially does not contain an express grant, Congress is free to amend the legislation to clarify and expressly impart extraterritorial effect.¹¹⁹ This was the case with the Age Discrimination in Employment Act¹²⁰ (“ADEA”) discussed in *Aramco*.¹²¹ After several courts held that the ADEA did not apply overseas, Congress amended the ADEA to provide for extraterritorial effect.¹²² Thus, it is wise for courts to generally assume, absent evidence to the contrary, that Congress is aware of the intricacies of passing legislation and refrain from implying intent in most circumstances.

4. The Territorial Presumption: The Whistleblower Provision Will Not Be Granted Extraterritorial Effect

Under the statutory interpretation analysis mandated by the territoriality presumption, the Whistleblower Provision does not have the characteristic markers of intended extraterritorial effect. Without the express earmarks of congressional intent to impart extraterritorial effect, the policy considerations behind the Whistleblower Provision—specifically, the desire to protect United States investors and markets against fraud—will not sustain the expansion of its reach simply because such an expansion would provide another means of accomplishing this goal. As the First Circuit stated, “whatever help to investors its overseas application might in theory provide is offset . . . by the absence of any indication that Congress contemplated extraterritoriality.”¹²³ Under the territoriality presumption, the First Circuit correctly held that the Whistleblower Provision was not intended to reach foreign employees working outside the United States.¹²⁴

However technically proper this holding may be under the territoriality presumption, it is troubling when one considers the devastating impact of the Enron scandal and the concerns driving the enactment of the Whistleblower Provision. This counterintuitive result subverts, rather than upholds, the actual intent of Congress in crafting

118. *Equal Employment Opportunity Comm’n v. Arabian Am. Oil Co. (Aramco)*, 499 U.S. 244, 258 (1991).

119. *See id.* at 258–259.

120. 29 U.S.C. §§ 621–34 (2000).

121. *Aramco*, 499 U.S. at 258–259.

122. *Id.*

123. *Carnero v. Boston Scientific Corp.*, 433 F.3d 1, 7 (1st Cir. 2006).

124. *Id.* at 18.

the Whistleblower Provision. To combat troubling outcomes of this nature, another approach for analyzing the extraterritorial effect of legislation in the field of securities regulation must be employed.

B. Analysis #2: The Effects Test as Applied to the Whistleblower Provision

The territoriality presumption analysis is only one of the methods used by the Supreme Court to determine the extraterritorial effect of congressional legislation.¹²⁵ As previously mentioned, the Supreme Court has also embraced an effects test analysis of extraterritorial effect.¹²⁶ This analysis departs from the rigid approach of the territoriality presumption and refocuses the inquiry on the effect that an action taken abroad has within the United States.

In evaluating the benefits of adopting an effects test approach for analyzing the extraterritorial effect of legislation in the field of securities regulation, a comparison to the field of antitrust, with its equally compelling international concerns, is informative. The Supreme Court initially adopted the territoriality presumption when it considered the extraterritorial effect of the Sherman Act,¹²⁷ one of the most often invoked provisions in antitrust legislation.¹²⁸ Over the next several decades, a series of cases involving the international application of the Sherman Act challenged this limited view of the Act's territorial reach.¹²⁹ Judge Learned Hand was the first to fully depart from the traditional territoriality presumption with his 1945 decision, *United States v. Aluminum Company of America* ("Alcoa").¹³⁰

In *Alcoa*, the United States government filed an antitrust complaint alleging the unlawful pursuit of exclusionary market practices and monopolization of the production and sale of aluminum ingot.¹³¹

125. See BORN, *supra* note 13, at 595. Until the First Circuit adopted the territoriality presumption in *Carnero*, the presumption had never been applied to securities regulation. *Carnero v. Boston Scientific Corp.*, 433 F.3d 1 (1st Cir. 2006), *petition for cert. filed* (U.S. May 3, 2006) (No. 05-1397).

126. See, e.g., *Hartford Fire Ins. Co. v. California*, 509 U.S. 764 (1993).

127. 15 U.S.C. § 1 (2000).

128. *Am. Banana Co. v. United Fruit Co.*, 213 U.S. 347, 357 (1909) (holding that the Sherman Act did not reach the allegedly anti-competitive behavior of a United States corporation if that behavior took place outside the territorial jurisdiction of the United States).

129. See BORN, *supra* note 13, at 578. The shortcomings of the territoriality presumption, when applied to fields that require participation in international conduct, may have prompted a shift away from the territoriality presumption and towards the effects test, in the field of antitrust. *Id.*

130. 148 F.2d 416 (2d Cir. 1945). See also BORN, *supra* note 13, at 578.

131. *Alcoa*, 148 F.2d at 423.

The government alleged that agreements entered into by the defendant violated section one of the Sherman Act, which makes illegal “[e]very contract, combination . . . or conspiracy, in restraint of trade or commerce.”¹³² The general character of the agreements was that “[n]o shareholder was to ‘buy, borrow, fabricate or sell’ aluminum produced by anyone not a shareholder except with the consent of the board of governors, but [the consent] must not be ‘unreasonably withheld.’”¹³³ Neither of the agreements explicitly included imports into the United States.¹³⁴ As the agreements allegedly violating section one of the Sherman Act were not entered into in the United States,¹³⁵ the court was called upon to evaluate the extraterritorial application of the Sherman Act.

In deciding the case, Judge Hand crafted a new approach for determining the extraterritorial reach of legislation. Judge Hand’s formulation of an effects test provided that the Sherman Act would cover conduct occurring outside the United States if two requirements were satisfied: (1) the conduct was intended to affect United States imports, and (2) the conduct actually had an effect in the United States.¹³⁶ The court held that the agreements at issue were unlawful under the Sherman Act because the “agreements would clearly have been unlawful, had they been made within the United States; and it follows from what we have just said that both were unlawful, though made abroad, if they were intended to affect imports and did affect them.”¹³⁷

The effects test was most recently applied by the Supreme Court in *Hartford Fire Insurance Co. v. California*.¹³⁸ In *Hartford Fire Insurance*, the Court considered the extraterritorial application of the Sherman Act to London-based reinsurers.¹³⁹ The complaint alleged that the defendants conspired in violation of section one of the Sherman Act to force primary insurers to change the terms of their insurance policies to conform with the policies of the defendant insurance companies.¹⁴⁰ Writing for a narrow majority of five justices, Justice Souter

132. BORN, *supra* note 13, at 577 (citing section 1 of the Sherman Act, 15 U.S.C. § 1 (2000)).

133. *Alcoa*, 148 F.2d at 442.

134. *Id.* at 442–43. Imports into the United States were discussed during the preparation of one of the agreements and the shareholders agreed that imports into the United States should be included in the quotas. *Id.*

135. *Id.* at 444.

136. *Id.*

137. *Id.*

138. 509 U.S. 764 (1993).

139. *Id.* at 794–95.

140. *Id.* at 770–71.

reaffirmed the effects test in finding that the London defendants' actions were meant to produce and did produce substantial effects in the United States, and the principles of international comity did not counsel against exercising extraterritorial jurisdiction over the foreign defendants.¹⁴¹

1. The Effects Test: Recognizing that an Effect Within the United States Should Extend the Reach of Legislation in the Field of Securities Regulation

Although the effects test has been used primarily in antitrust cases, its application is not limited. Legislation in the field of securities regulation, including the Sarbanes-Oxley Act, is comparable to anti-trust in that it is the type of legislation that must be interpreted with an eye toward the interconnected global economy. To be wholly effective, the territorial reach of legislation dealing with securities regulation must extend to foreign conduct that "was meant to produce and did in fact produce some substantial effect"¹⁴² on United States securities markets.

The purpose of the Sarbanes-Oxley Act, passed in the wake of the Enron scandal, is to protect United States investors and the integrity of the United States securities markets by regulating against corporate accounting impropriety, particularly corporate fraud.¹⁴³ In a global economy, accomplishing this purpose will necessarily involve dealing with commercial transactions on an international level. This requires that courts look beyond the territorial boundaries of the United States and interpret the Sarbanes-Oxley Act to apply to *all* transactions that are intended to produce and actually do produce some substantial effect on the United States securities markets.

The Whistleblower Provision was designed to further the goals of the Sarbanes-Oxley Act by fighting a corporate culture in which employees who report corporate fraud and impropriety are vulnerable to retaliation.¹⁴⁴ The provision is an important measure in eradicating the widespread accounting improprieties revealed in the wake of the Enron scandal. In his introduction of the bill, Senator Leahy discussed a letter from the National Whistleblower Center proclaiming the Whistleblower Provision to be "the single most effective measure pos-

141. *Id.* at 798–99.

142. *Id.* at 796.

143. See 148 CONG. REC. S1786 (2002) (statement of Sen. Leahy); Falencki, *supra* note 2, at 1213–14.

144. 148 CONG. REC. S1792.

sible to prevent recurrences of the Enron debacle and similar threats to the nation's financial markets."¹⁴⁵ Although the Whistleblower Provision has characteristics of both employment legislation, which is traditionally not applied extraterritorially,¹⁴⁶ and securities regulation, it plays an integral role in accomplishing the goals of the Sarbanes-Oxley Act. To uphold the purpose and objectives of the Sarbanes-Oxley Act, the extraterritorial effect of the Whistleblower Provision should be analyzed in light of its function as legislation in the field securities regulation.

The effects test affords a court more flexibility to consider both policy concerns and implied congressional intent in deciding if the effect produced in the United States will support a finding that the Whistleblower Provision applies extraterritorially. This flexibility allows the court to examine the potential benefits realized by imparting extraterritorial effect in light of the legislation's purpose. The court is no longer constrained by the presumption that ambiguous and incomplete statutory language or legislative history requires a restriction on the legislation's territorial reach that will subvert, rather than uphold, the legislation's purpose. In the case of the Whistleblower Provision, a court employing the effects test would have more leeway to examine the benefits of protecting whistleblowers abroad, taking into account ambiguously-stated congressional intent that the legislation "sweep broadly." The deciding court would have more latitude to determine if, although not expressly prohibited by the legislation, the behavior such whistleblowers protect against produces the type of effect in the United States that Congress intended to protect against. The court would also have the ability to consider the practical application of the statute in the real world and to respond to unforeseen international implications of the legislation.

145. *Id.*

146. Dating back to the *Foley Brothers* decision in 1948, the Court has recognized the uniquely local implications of employment regulations. *Foley Brothers*, 336 U.S. at 286. The Court in *Aramco* also recognized the difficulty of exporting employment legislation and, without clear evidence of congressional intent, the Court was "unwilling to ascribe . . . a policy which would raise difficult questions of international law by imposing this country's employment-discrimination regime upon foreign corporations operating in foreign commerce." *Equal Employment Opportunity Comm'n v. Arabian Am. Oil Co. (Aramco)*, 499 U.S. 244, 255 (1991). Applying the Whistleblower Provision extraterritorially to allow foreign employees working abroad at the foreign subsidiaries of United States parent companies, thereby allowing the foreign employee to bring suit against the United States parent company, does not raise the same concerns as regulating corporations operating entirely outside the borders of the United States.

a. Foreign Subsidiary Conduct: The Intended and Actual Effects of Retaliatory Termination of Employment in the United States

The first inquiry mandated by the effects test is whether the conduct to be regulated was intended to produce an effect in the United States.¹⁴⁷ An employee of a foreign subsidiary filing suit against a United States parent company under the Whistleblower Provision must establish the intended effect of the alleged retaliatory conduct based on the individual circumstances of his or her case. Under the first prong of the effects test, the alleged retaliatory conduct would only merit extraterritorial application of the Whistleblower Provision if the conduct itself was intended to have an effect in the United States.¹⁴⁸

One situation in which foreign subsidiary conduct could be intended to affect the United States is in the case of ongoing corporate fraud. Logic dictates that whistleblowers fired in retaliation for reporting corporate fraud are fired because they pose a threat to the continuation of that fraud. Fraudulent subsidiary activities, including creating false invoices and inflating sales figures, may be intended to increase the net income of the parent company. If the firing of the subsidiary whistleblower is intended to facilitate the continued corporate impropriety at the subsidiary, and if that impropriety is intended to affect the financial statements of the United States parent company, it could be argued that the retaliatory firing was intended to produce an effect in the United States. Although such an effect in the United States is indirect, if an Enron-like scandal involving the United States parent company were to occur, it is likely that investors in the parent company would have preferred early disclosure of the corporate fraud regardless of whether the disclosure was made by a whistleblower in the United States or at a foreign subsidiary.

Carnero alleges that he was fired in retaliation for “blowing the whistle” on the accounting misconduct of BSC’s Latin American subsidiaries.¹⁴⁹ Although the First Circuit made no findings regarding the intended effect of firing Carnero, a court could reasonably find that the alleged retaliatory firing was intended to facilitate the continuation of the fraudulent activity, thereby affecting the financial statements of BSC, the parent company listed in the United States on the

147. *United States v. Aluminum Co. of America (Alcoa)*, 148 F.2d 416, 444 (2d Cir. 1945).

148. *See Alcoa*, 146 F.2d at 444.

149. *Carnero v. Boston Scientific Corp.*, 433 F.3d 1, 2–3 (1st Cir. 2006).

New York Stock Exchange. If the alleged improprieties of the Latin American subsidiaries were meant to artificially increase the stock price of BSC or in any other way defraud American investors or undermine the integrity of the United States securities markets, then the court could find that the subsidiaries intended to produce an effect in the United States. This would support extraterritorial application of the Whistleblower Provision if the court further determined that Carnero was fired in retaliation for reporting the fraudulent activity, and to ensure that the impropriety continued. These findings would be commensurate with the expressed congressional intent that the legislation “sweep broadly” to protect any employee who acted to “protect investors and the market.”¹⁵⁰

If it is established that the alleged retaliatory conduct was intended to produce an effect in the United States, the court will then determine if the impropriety actually produced an effect in the United States.¹⁵¹ As the territoriality presumption is not concerned with the negative effect an action abroad may have in the United States, the First Circuit did not inquire as to the actual effects produced by the alleged impropriety at BSA and BSB. However, a previous instance of fraud perpetrated by a Japanese subsidiary of BSC indicates that subsidiary fraud at BSA and BSB is likely to produce an actual effect in the United States.¹⁵²

In *In re Boston Scientific Corp.*, the SEC found that between March 1997 and June 1998 Boston Scientific Japan, KK (“BSJ”) recorded false sales and earnings data and reported the data to BSC.¹⁵³ The fraudulent reports by BSJ caused BSC to overstate net income in 1997 and the first two quarters of 1998 by a total of nearly fifty million dollars.¹⁵⁴ Although BSC discovered the fraudulent activity in the fall of 1998 and restated its financial filings to reflect the impact of the fraud, the reports filed with the SEC in 1997 and the first two quarters of 1998 contained material misstatements of income and losses in vio-

150. 149 CONG. REC. S1725 (2003) (statement of Sen. Leahy).

151. *Alcoa*, 148 F.2d at 444. The magnitude of effect required to satisfy this prong of the effects test is somewhat disputed. Many lower courts refuse to grant extraterritorial effect when the effects within the United States are merely speculative. *See, e.g.*, *Montreal Trading v. Amax, Inc.*, 661 F.2d 864, 870 (10th Cir. 1981). *Hartford Fire Insurance* implicitly adopts a “substantial effects” threshold in its holding. 509 U.S. at 796.

152. *See In re Boston Scientific Corp.*, Securities Exchange Administrative Proceeding File No. 3-10272, 2000 SEC LEXIS 1705, at *1 (S.E.C. Aug. 21, 2000).

153. *Id.* at *2–3. The total amount of misstated revenue was later determined to be in excess of seventy-five million dollars. *Id.* at *6.

154. *Id.* at *7.

lation of the Exchange Act of 1934.¹⁵⁵ The SEC accepted an offer of settlement by BSC¹⁵⁶ and entered an order that BSC cease and desist from committing or causing the violations.¹⁵⁷

Under the effects test approach, extraterritorial application is proper when conduct is both intended to affect the United States and actually produces an effect within the United States.¹⁵⁸ Fraudulent activities perpetrated by a foreign subsidiary of a United States parent company may be intended to increase the net income, or decrease the net losses, of the parent company. As illustrated in *In re Boston Scientific Corp.*, foreign subsidiary fraud can result in significant problems with the accuracy of SEC filings mandated by the Exchange Act of 1934, thereby producing an actual effect within the United States.¹⁵⁹ If later revealed, the subsidiary's improprieties are likely to have a significant impact on public confidence in the parent company and may well affect the performance of the parent company in the United States securities market.¹⁶⁰ Retaliation against a whistleblower who serves the public interest by reporting foreign subsidiary fraud perpetrated with an eye toward affecting the United States parent company merits extraterritorial application of the Whistleblower Provision under the effects test analysis when it can be shown that the retaliation perpetuated the fraud and produced an actual effect within the United States.

155. *Id.* at *9–12. The fraudulent activity of BSJ caused BSC to materially misstate net income and losses in its annual report for 1997 and quarterly reports filed in 1997 and 1998, which placed BSC in violation of several sections of the Exchange Act. The misstatements were a violation of section 13(a) of the Exchange Act, which requires that information filed pursuant to the Exchange Act must be accurate and complete, because the financial reports contained materially inaccurate information. *Id.* at *9. The misstatements also violated section 13(b)(2)(A) of the Exchange Act, which requires that an issuer of securities must keep books and records that accurately and fairly reflect its transactions, and section 13(b)(2)(B) of the Exchange Act, which requires that issuers maintain internal accounting controls to prevent transactions from being improperly recorded. *Id.* at *10–12.

156. The commission accepted BSC's offer of settlement in light of the remedial action taken by BSC and the company's cooperation with the commission. *Id.* at *12–13.

157. *Id.* at *13.

158. *See Alcoa*, 146 F.2d at 444.

159. *See supra* note 155 (illustrating the actual effects produced in the United States by a Japanese subsidiary of BSC).

160. *See, e.g.*, Scott Reckard, *Syncor Seeks SEC Filing Extension*, L.A. TIMES, NOV. 14, 2002, at C3 (reporting that a disclosure by Syncor International Corporation that it was investigating possible bribes to foreign officials made by its foreign subsidiaries "cut its stock price in half"); Travis Purser, *Syncor Rebounds but Credibility Issues Remain*, L.A. BUS. J., NOV. 18, 2002, at 14 (noting that, although stock prices had rebounded from the trading low of \$16.90 to \$25.69, experts believed that Syncor's biggest problem would be repairing the damage that the disclosure of bribes to foreign officials had done to its credibility).

b. When Do the Principles of Comity Counsel Against Extraterritorial Application in the Effects Test Analysis?

Hartford Fire Insurance reached the Supreme Court following a long line of cases holding that the Sherman Act applied to foreign conduct that “was meant to produce and did in fact produce some substantial effect in the United States.”¹⁶¹ Therefore, the Court did not focus on congressional intent regarding extraterritorial effect, but instead asked whether the district court should have declined to exercise jurisdiction based on the principles of international comity.¹⁶² In deciding this question, the majority sought to determine whether there was a “true conflict between domestic and foreign law.”¹⁶³ The Court found that, because the London reinsurers were not required by British law to act in some manner prohibited by the United States and that compliance with the laws of both countries was not impossible, no true conflict of laws existed.¹⁶⁴ As there was no conflict of laws, the Court found that the principle of international comity did not counsel against exercising extraterritorial jurisdiction over the London-based reinsurers.¹⁶⁵

If a district court finds that the alleged retaliatory conduct supports extraterritorial application of the Whistleblower Provision, it should only decline to exercise jurisdiction based on the principle of international comity if there is a true conflict of laws between the protections afforded by the Whistleblower Provision and the laws of the other country. In *Hartford Fire Insurance*, the Court stated that “[n]o conflict exists . . . ‘where a person subject to regulation by two states can comply with the laws of both.’”¹⁶⁶ Under the standard enunciated by the majority in *Hartford Fire Insurance*, this would not have been a problem in *Carnero* unless BSA and BSB presented evidence sufficient

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

162. *Id.* at 798.

163. *Id.* (quoting *Société Nationale Industrielle Aérospatiale v. United States District Court*, 482 U.S. 522, 555 (1987)).

164. *Id.* at 799.

165. *Id.*

166. *Id.* (quoting RESTATEMENT (THIRD) FOREIGN RELATIONS § 403, Comment e). This is a somewhat controversial understanding of international comity. The majority in *Hartford Fire Insurance* focused on only one factor in the section 403 test—the likelihood of conflict with regulation by another state—to determine if the exercise of jurisdiction is reasonable and treated that factor as dispositive without conducting a balancing of the other seven factors. RESTATEMENT (THIRD) FOREIGN RELATIONS § 403(2)(a)–(h). See Robert C. Reuland, *Hartford Fire Ins. Co., Comity, and the Extraterritorial Reach of United States Antitrust Laws*, 29 TEX. INT’L L.J. 159, 204–09 (1994) for a discussion of the controversy surrounding Justice Souter’s interpretation of international comity.

to satisfy the court that compliance with both the laws of their respective countries and the anti-fraud provisions violated by the alleged improper accounting practices was impossible.

2. The Effects Test: The Whistleblower Provision May Be Granted Extraterritorial Effect

Under the effects test, a court will find that the Whistleblower Provision should have extraterritorial effect when: (1) the alleged retaliatory conduct was intended to have an effect in the United States, and (2) the conduct actually had such an effect. This expansion of extraterritorial application addresses many of the policy concerns that make the limited notion of extraterritorial effect under the territoriality presumption so troubling. Under the effects test, the deciding court has more flexibility to determine if the conduct to be regulated has significant impact within the United States and is, therefore, the type of conduct to which the legislation should apply.

Congress enacted the Whistleblower Provision to combat a corporate culture in which employees who report impropriety are vulnerable to retaliation.¹⁶⁷ Whistleblowers are less likely to come forward with reports of corporate fraud and impropriety at foreign subsidiaries of United States parent companies if they fear losing their jobs or suffering other retaliation.¹⁶⁸ If foreign subsidiary whistleblowers are less likely to come forward, subsidiary fraud is less likely to be exposed. Such subsidiary fraud can cause a United States parent company to overstate net income, or understate net losses, in reports filed with the SEC.¹⁶⁹ This misstatement has the potential to wipe out investments in the parent company, listed in the United States securities markets, if and when the subsidiary fraud is revealed.¹⁷⁰ This is the impact on United States investors and securities markets that Congress sought to prevent when the Whistleblower Provision was enacted.

167. 148 CONG. REC. S1792 (2002) (statement of Sen. Leahy).

168. In his brief to the First Circuit, Carnero detailed the retaliation he experienced after reporting that BSA and BSB created false invoices and inflated sales figures, but before his eventual termination. Brief of Petitioner-Appellant at 10–12, *Carnero v. Boston Scientific Corporation*, Nos. 04-2291 and 04-1801 (consolidated) (1st Cir. Dec. 17, 2004). After reporting the alleged impropriety, Carnero learned that other BSC employees made false allegations accusing him of “unethical conduct.” *Id.* at 11. Carnero requested an investigation into the allegations made against him, but BSC was unresponsive. *Id.*

169. See *In re Boston Scientific Corp.*, Securities Exchange Administrative Proceeding File No. 3-10272, 2000 SEC LEXIS 1705, at *1 (S.E.C. Aug. 21, 2000).

170. See Chiara & Orenstein, *supra* note 32, at 236 (discussing the role misstatements in financial filings played in the Enron scandal).

The effects test analysis refocuses the inquiry on the location of the effect rather than on the location of the action against which Congress sought to legislate. If the effect in the United States is substantial, it is not unreasonable to consider the action as within the scope of domestic concerns Congress presumably has in mind when enacting legislation.¹⁷¹ In such situations, the substantial effect within the territorial bounds of the United States supports this assumption regardless of the action's physical location. When granted extraterritorial effect, the Whistleblower Provision more effectively upholds congressional intent that the legislation "protect[] any employee . . . who took such reasonable action to try to protect investors and the market."¹⁷² In this era of increasing globalization, the important interests motivating the enactment of the Sarbanes-Oxley Act—specifically the protection of United States investors and the integrity of the United States securities markets—are better served if certain provisions of the Sarbanes-Oxley Act, such as the Whistleblower Provision, reach beyond the physical territory of the United States. In the absence of a clear statement of extraterritorial reach, it is only through application of the effects test that courts are allowed the flexibility to determine if the overarching purpose of legislation is best served by allowing an intended and actual effect in the United States to support extraterritorial effect.

III. Conclusion

In the increasingly global economy where many United States corporations operate numerous foreign subsidiaries, it is likely that the courts will again be called upon to decide if the Whistleblower Provision should be granted extraterritorial effect. The granting of extraterritorial effect would allow covered employees working abroad for a foreign subsidiary to bring suit against the United States parent company for allegedly retaliatory conduct that took place outside the territorial boundaries of the United States. When the issue is raised, the court faced with the decision may choose to follow the First Circuit's lead and employ the territoriality presumption. However, as this Comment has illustrated, an analysis of the Whistleblower Provision under the territoriality presumption is likely to result in a finding that the provision is without extraterritorial effect. This undercuts the purpose of the Sarbanes-Oxley Act by limiting the protection that the Whistleblower Provision provides. Such a decision has the potential to

171. See *Foley Bros., Inc. v. Filardo*, 336 U.S. 281, 285 (1949).

172. 149 CONG. REC. S1725 (2003) (statement of Sen. Leahy).

discourage employees working overseas for foreign subsidiaries of United States parent companies from coming forward to report corporate fraud that will eventually make its way back to the United States. If the next court to confront the issue employs the territoriality presumption, its restrictive approach and inability to fully respond to important policy considerations will likely lead to the troubling result reached by the First Circuit—that the Whistleblower Provision does not apply extraterritorially.

Without a decision by the Supreme Court declaring that the extraterritorial effect of the Whistleblower Provision should be governed by the territoriality presumption, the next court to decide the issue may forego its restrictive approach in favor of the more flexible effects test analysis. The flexibility of the effects test allows a court to consider the application of legislation in an international context as it arises and to uphold the goals of the legislation, even when congressional intent that the provision be granted extraterritorial effect is not explicitly stated. The effects test better upholds the purpose of the Whistleblower Provision by extending its protections to employees of foreign subsidiaries who are retaliated against if the retaliation was intended to produce an effect in the United States and actually produced such an effect. Extending the Whistleblower Provision to cover these employees will encourage reporting of foreign subsidiary fraud that is intended to affect the United States securities markets, thereby protecting both investors and the integrity of the markets.

This Comment seeks to expose the inherent difficulty in allowing competing analytical approaches for determining the extraterritorial effect of congressional action to exist simultaneously: the results reached under the two approaches will not always be the same. In declining to hear this case, the Supreme Court missed an opportunity to either clarify the analysis of extraterritorial effect of the Whistleblower Provision or to set the standard for the analyzing the extraterritoriality of legislation in the field of securities regulation. Without such guidance, there will likely be confusion among lower courts and litigants when dealing with the potential extraterritorial application of both the Whistleblower Provision and other provisions of the Sarbanes-Oxley Act that are silent as to their territorial reach. Should another opportunity arise, the Court should adopt the flexibility of the effects test to analyze legislation enacted in the field of securities regulation as it is better suited to deal with ambiguously-stated congressional intent and the likelihood that such legislation will have unanticipated international implications.

