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# Extraterritorial Application of United States Commodity and Securities Laws to Market Transactions in an Age of Intercontinental Trading Links

## I. INTRODUCTION

The recently operational<sup>1</sup> trading link between the Chicago Mercantile Exchange ("CME") and the Singapore International Monetary Exchange ("SIMEX")<sup>2</sup> is one of the most significant developments to occur in the securities industry in recent memory. While the initial phase of this intermarket, intercontinental link involves only the trading of Eurodollar, Deutsche mark, and Japanese yen futures contracts,<sup>3</sup> the prospects for the trading of additional contracts,<sup>4</sup> and the further expansion of trading hours, ultimately to round-the-clock trading, appear favorable.

The internationalization of both foreign and domestic futures markets is clearly the order of the day.<sup>5</sup> A trading link connecting the futures exchanges of two separate nations, however, represents a new and truly experimental phenomenon, one which has prompted concern

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<sup>1</sup> Trading over the CME-SIMEX link commenced on Friday, September 7, 1984. See, N.Y. Times, Sept. 7, 1984, at D1, col. 3; Wall St. J., Sept. 6, 1984, at 2, col. 3.

<sup>2</sup> Formerly the Gold Exchange of Singapore, the SIMEX was created in response to the desire of the Monetary Authority of Singapore to enter into the trading of financial futures. Three officials of the CME were invited to consult with Singapore Monetary Authority officials as to how the desired expansion of SIMEX into a full-scale financial futures marketplace might be accomplished. While originally intended to spur the growth and development of the SIMEX, the consultations between CME and SIMEX officials led instead to a feasibility study of a trading link joining the trading floors of the CME and the newly constituted SIMEX. Thus, the potential for expansion of the CME's market activities came into being as well.

<sup>3</sup> The decision to commence trading with only three contracts was based upon research which demonstrated the significant average change in the dollar value of one Eurodollar or Japanese yen futures contract during non-United States trading hours. See *infra* note 14.

<sup>4</sup> The CME has petitioned the Commodity Futures Trading Commission for permission to begin trading a gold futures contract identical to that which has been trading on SIMEX since July 5, 1984. Chicago Mercantile Exchange, Market Perspectives (Sept. 1984) (the monthly bulletin of the exchange).

<sup>5</sup> As a result of rapid advances in communications technology, traders worldwide currently enjoy almost instantaneous access to the price quotations and trading floors of futures markets anywhere in the world. See, 16 Sec. Reg. & L. Rep. (BNA) 169 (1984).

among regulators and members of the investment community inasmuch as the once abstract regulatory and jurisdictional issues raised by an international trading link have now presented themselves as realities for the first time.

Utilization of the CME-SIMEX link creates substantial opportunities both for the commercial hedger as well as the individual or institutional speculator by expanding trading flexibility and lowering transaction costs.<sup>6</sup> Increased opportunity, however, is likely to spawn difficulty in situations where, for instance, a SIMEX trader in Singapore using the trading link alleges some act of fraud or misrepresentation prohibited under United States laws and then seeks to employ the federal judicial forum in an effort to recover damages or such other remedies as are authorized by statute.

The issue of at what point fraudulently induced market activity initiated abroad becomes justiciable in this country has received considerable attention in the field of securities law.<sup>7</sup> Growth and interest in the trading of commodity and financial futures contracts have resulted more recently in an examination of the extraterritorial application of the anti-fraud provisions of the Commodities Exchange Act ("CEA").<sup>8</sup> Predictably, United States courts have thus far analogized from the existing body of securities law to the futures field in order to afford traders claiming to have been defrauded abroad the protections and remedies available under our laws for violations of the Commodities Exchange Act.<sup>9</sup>

Part I of this Comment will fully explore the novel concept embodied by the CME-SIMEX trading link. Next, Part II will analyze the most recent judicial decision—one not involving the trading link—concerning the extraterritorial application of federal commodities statutes to illegal acts alleged to have been committed abroad. And finally, in Part III, this Comment will examine the arguments in favor of and against extraterritorial application of the Securities and Commodities Exchange Acts to claims of predominantly foreign fraud in an era of increasing internationalization of world financial markets. The conclusion reached is that existing judicial doctrines used in dealing with the determination of extraterritorial jurisdiction, while fashioned over a decade ago, are now, more than ever, appropriately applied to protect domestic interests

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<sup>6</sup> Illustrations of increased trading flexibility and evidence of lowered transaction costs are presented *infra* at notes 15 and 18 respectively.

<sup>7</sup> See *infra* notes 105-10 and accompanying text.

<sup>8</sup> Commodity Exchange Act, 7 U.S.C. § 6(b) (1982).

<sup>9</sup> See *infra* note 40 and accompanying text.

from the effects of fraudulent conduct exported, in any degree, to the United States.

The analysis set forth herein is equally applicable to other trading links which have either been undertaken or are rumored to be under consideration between foreign and domestic exchanges<sup>10</sup> or as other exchanges are added to the CME-SIMEX link in furtherance of the concept of round-the-clock futures trading.

## II. THE TRADING LINK

### A. The Concept

Commodity and financial futures contracts are among the most volatile of investment vehicles<sup>11</sup> as their market prices are determined on the basis of any number of international events which can occur at any hour. Natural disasters in one corner of the world quite frequently will affect the price of such "soft" commodities as wheat, cocoa, or sugar throughout the rest of the world.<sup>12</sup> Similarly, political and economic uncertainties the world over are often responsible for a strengthening or weakening in the value of world currencies.<sup>13</sup> Whether or not futures markets in

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<sup>10</sup> At this writing, other links presently operational in the securities field include links between the Boston and Montreal Stock Exchanges, the Toronto and American Stock Exchanges and the London Stock Exchange and the National Association of Securities Dealers, Inc. ("NASD") in the Over the Counter Market. See N.Y. Times, Sept. 22, 1986, at D1, col. 3. Links currently being contemplated but not yet operational include a possible link between the Chicago Board of Trade and the London International Financial Futures Exchange, see *FUTURES*, Sept. 1984, at 55; a link between the American Stock Exchange Options Exchange and the European Options Exchange and a joinder between the Philadelphia Stock Exchange and the London Stock Exchange is also proposed. Conversation with William Brodsky, President, Chicago Mercantile Exchange (Apr. 30, 1986).

While more and more of such links are contemplated and become operational, only the link between SIMEX and the CME offers futures traders substantial opportunities in the areas of limitation of oversight trading risk and a lengthening of the actual trading day.

<sup>11</sup> Of course, it is not the futures contract itself which results in the instrument's extraordinary volatility but rather the value of the commodity or currency underlying the contract. Because many underlying commodities and currencies represent foodstuffs, raw materials, fuels and means of exchange, futures contracts tend to be extremely volatile due to the sensitivity of the financial community to the slightest shifts in crop or production forecasts and currency stabilities.

<sup>12</sup> The citrus canker outbreak in Florida in 1984, which resulted in dramatic increases in orange futures contract prices, is an example of a natural phenomenon which had an enormous impact upon "soft" commodity prices.

<sup>13</sup> Mexico's recent economic crisis provides a useful illustration. Mexico sought to take full advantage of what seemed to be an insatiable worldwide demand for oil during the 1970s. Unfortunately, the world's industrial nations soon found themselves trapped in a recession and Mexico, in turn, found itself with a foreign debt in excess of \$48 billion which it had assumed in expectation of continued worldwide demand for oil. President de la Madrid's bold economic austerity program drastically devalued the peso, a measure which shook world currency markets. For a more detailed account of Mexico's troubles, see *TIME*, June 13, 1983, at 48.

any given part of the world will be open when such events take place is purely a matter of chance.

The CME-SIMEX link was instituted in response to the vicissitudes of the world economy and the resultant risk an investor in futures contracts used to have to bear during the sixteen hours futures exchanges were closed each day.<sup>14</sup> The three futures contracts initially involved in the CME-SIMEX link (Eurodollars, Deutsche marks, and Japanese yen) are currently traded on the CME from 7:30 am (CST) until roughly 2:00 pm (CST). With the trading of these contracts on SIMEX, additional trading hours from roughly 6:30 pm (CST) to 1:00 am (CST) have become effective.<sup>15</sup> Thus, the CME-SIMEX trading link allows for almost a doubling in the length of the trading day and a concomitant decrease in the degree of overnight risk traders are forced to bear between an exchange's closing and its opening the following morning.

### B. The Mutual Offset System

The real benefit to be gained as the result of the extended trading hours made possible by the CME-SIMEX link derives from what has been termed the Mutual Offset System ("MOS").<sup>16</sup> Until recently, if a trader took a position in ninety-day Eurodollar futures in Chicago during the day and then, after the CME had concluded its trading day, international events suddenly required the liquidation of that Eurodollar posi-

<sup>14</sup> A study conducted jointly by Data Resources, Inc. and the CME during the period December 10, 1982 to August 1, 1983 demonstrates the significance of the average change in the dollar value of Japanese yen and Eurodollar futures contracts during hours when United States futures markets are closed. The study further illustrates the average change in the dollar value of yen and Eurodollar contracts during the United States trading day and the total average change in dollar value over a 24-hour period.

<sup>15</sup> A comparison of Chicago trading hours (cst) with Singapore trading hours displaying actual Singapore time and equivalent Chicago (cst) time is illustrated below:

<u>Commodity</u>	<u>CME Trading Hours (cst)</u>	<u>SIMEX Trading Hrs. Singapore Time</u>	<u>Corresponding (cst)</u>
DM	7:30am-1:20pm	8:35am-2:50pm	6:35pm-12:50am
Eurodollar	7:30am-2:00pm	9:00am-3:00pm	7:00pm- 1:00am
¥	7:30am-1:22pm	8:30am-2:45pm	6:30pm-12:45am

The seemingly random close of trading for the mark and yen can be explained by the fact that for operational reasons, the CME has chosen to stagger the closings of its currency futures at two-minute intervals. Not only do staggered closings allow for a more orderly conclusion of trading but traders who trade more than one financial futures contract are afforded an opportunity to be present at the close of each currency traded.

<sup>16</sup> The Mutual Offset System is defined as, "the system established pursuant to this Agreement whereby certain Clearing Members of either Exchange may liquidate or establish positions on one Exchange through the execution of trades on the other Exchange." The Agreement for the Creation of a Mutual Offset System Between the Chicago Mercantile Exchange and the Singapore International Monetary Exchange, Ltd. (June 28, 1984) [hereinafter the Agreement]. A copy of the Agreement is available at the Chicago Mercantile Exchange, Chicago, Illinois.

tion, in order to limit losses a trader would have to sell (go short) a corresponding number of Eurodollar contracts on another futures exchange open for trading during what would be evening hours in the United States.<sup>17</sup> The following day, in order to close out the two separate market positions, the trader would have to sell out the long position in Chicago and cover the short sale on the foreign exchange.

The MOS substantially reduces the chances that four transactions will have to be executed in the event that exigent market circumstances or investor decisions necessitate trading at hours during which a trader's original marketplace is closed. Assuming that SIMEX is open when the Chicago trader needs to liquidate a market position opened on the CME, the MOS will permit a position (purchase or short sale) to be offset by a corresponding, but opposite, transaction on SIMEX. Trades initiated on SIMEX can likewise be offset by transactions on the CME. Not only is the number of orders a trader has to place cut in half, resulting over time in considerable commissions savings,<sup>18</sup> but the trader is required to pay only one bid-ask spread<sup>19</sup> rather than the two such spreads required when closing out a market position on an exchange different from where the position originated. Along these same lines, the CME-SIMEX link is characterized by a single margin structure,<sup>20</sup> thus eliminating the need

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<sup>17</sup> This predicament should not be confused with a similar situation, in fact a strategy which a trader may choose to adopt, called "spreading." Spreading is defined as "[t]he purchase of one futures contract and the sale of another, in the expectation that the price relationships between the two will change so that a subsequent offsetting sale and purchase will yield an amount as profit." See Chicago Board of Trade, *Commodity Trading Manual* 283 (1933).

<sup>18</sup> While commissions are no longer fixed but are instead negotiable, brokerage houses still publish commission schedules which act as a point of departure for individual brokers wishing to provide customers with some sort of discount. For example, Paine Webber's basic commission rate for future trading provides for a \$90 commission on the purchase or sale of one Eurodollar futures contract, a \$900 commission on the purchase or sale of 10 Eurodollar contracts and a \$2250 commission for the purchase or sale of 25 Eurodollar contracts. These rates may be discounted up to 50% depending upon the agreement struck between broker and client. Quoted by Paine Webber, Inc. (Nov. 1, 1984) (all trades based upon CME execution). Where traders are forced to cover market positions on other exchanges these transaction costs will be at least doubled due to increased commissions where executions take place on a foreign market.

<sup>19</sup> The "bid-ask" spread is the difference between the price a trader is prepared to bid (pay) for a particular futures contract and the price other traders are asking in exchange for those same contracts. In a strong market, buyers will often raise their bids to meet sellers' asking prices and, conversely, in a weak market sellers will often lower their asking prices in order to meet buyers' bids.

<sup>20</sup> Futures trading normally involves greater sums of money than ordinary securities transactions due to the sizable contract specifications involved—i.e. one Japanese yen contract represents 12.5 million yen. As a result of the dollar amounts at stake as well as the potential for considerable volatility, trading accounts are settled each day with accounts credited or debited at the conclusion of daily trading to reflect the current market value of a trader's position. A margin account is an account which a trader is required to maintain in order to absorb debits made at the end of a trading session or to accumulate credits as market conditions on any given day may dictate.

Heretofore a trader would have had to maintain at least two separate margin accounts (tying up

for a trader to maintain more than one margin account<sup>21</sup> in anticipation of having to offset a market position on a second market.

### C. Inter-Exchange Transfers

The operational functioning of the MOS is considerably more difficult to comprehend than is the conceptual functioning of the system. For example, offsetting a position assumed on the CME by an opposite transaction executed on SIMEX is made possible by the result of "inter-exchange transfers."<sup>22</sup> The parties involved in these inter-exchange transfers are referred to as "originating clearing members"<sup>23</sup> and "executing clearing members."<sup>24</sup> An originating clearing member is a member of one of the linked exchanges which initiates orders for execution on the other linked exchange on which the originating firm is not a clearing member, i.e., a CME member firm for purposes of trades to be executed on SIMEX. Conversely, an executing clearing member is an exchange

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twice as much cash) in order to preserve the flexibility to liquidate a position on a second market if such a transaction became necessary. As has been stated, a trader employing the CME-SIMEX link can enjoy trading flexibility while maintaining only one margin account.

<u>Currency</u>	<u>U.S. Overnight Risk</u>	<u>U.S. Trading Risk</u>	<u>Total Risk</u>
Eurodollar	\$225	\$350	\$400
¥	\$212	\$188	\$288

Although United States overnight risk is not as great as United States trading day risk in the case of Eurodollars, exposure remains considerable—Eurodollar overnight risk is 9 basis points or 64% of the 14 basis point daytime risk. Overnight risk is actually greater in the case of the Japanese yen futures contract than is the case during the United States trading day because events likely to affect the value of the yen most often occur during Japan's business day which coincides with evening hours in the United States. United States overnight risk for the yen trader is (in United States financial market terms) 17 basis points or 113% of the 15 basis point risk during United States daytime trading hours. See Chicago Mercantile Exchange, *Market Perspectives* 1 (Sept. 1983).

The study included comparable data for SIMEX's one ounce gold futures contract but CME and SIMEX officials decided, at least initially, to substitute the trading of a Deutsche mark contract for the gold contract based upon the former's generally recognized status as the primary commercial currency of Europe and the latter's recent sluggish market performance. Interview with William Brodsky, President of the Chicago Mercantile Exchange (Oct. 28, 1984).

<sup>21</sup> As opposed to the generic meaning of a margin account when applied to securities trading, a margin account in the case of futures trading is "the amount deposited as a guarantee for the fluctuations of a futures purchase or sale. If the contract fluctuates against the holder of the contract, he is required to provide for the difference between his contract price and the current market price by paying 'variation margin' differences. Thus, the original margin continues to guarantee fully the performance of the contract at any market price level." GUIDE TO WORLD COMMODITY MARKETS 367 (E. de Keyser ed. 1979).

<sup>22</sup> Terminology adopted by the Agreement but which may not be used by traders, the popular press or others not strictly familiar with the trading link's contractual underpinnings. An "Inter-Exchange Transfer" is defined in the Agreement as a "transfer pursuant to the Mutual Offset System to one Exchange of a position established as a result of a trade executed on the other Exchange . . . ." See Agreement, *supra* note 16, at 4.

<sup>23</sup> *Id.*

<sup>24</sup> *Id.* at 3.

member firm which accepts and executes orders initiated by originating clearing members.<sup>25</sup> Facilitated by these market participants, the inter-exchange transfer process is comprised of two separate procedures: "matching"<sup>26</sup> and "clearing."<sup>27</sup>

Once an executing clearing member has executed a trade received from an originating clearing member, that trade must initially be "matched" by the clearing house of the executing exchange. Matching simply entails a comparison of the trading information submitted by both sides of a trade to the clearing house. Where the trading information of both parties to a transaction is identical, the buy and the sell orders are deemed to have been matched.<sup>28</sup> The second step in the inter-exchange transfer is the "clearing" process. Clearing a trade is the procedure undertaken at the close of trading each day in which the price at which a given execution took place is compared with the closing price ("settlement price") of that futures contract for that day.<sup>29</sup> The amount of variation between the price at which the trade took place and the price at which the contract closed for the day is computed and then collected by the clearing house from one clearing member and paid to another.<sup>30</sup>

The MOS requires the complete cooperation of the participating exchanges and their clearing houses to facilitate the smooth operation of inter-exchange transfers. In an effort to ensure as trouble-free a transfer process as is possible, the agreement between the CME and SIMEX provides for an Inter-Exchange Administrator<sup>31</sup> whose chief responsibility is to preside over and to clarify the matching and clearing of inter-exchange

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<sup>25</sup> While all present clearing members of both the CME and SIMEX are potentially eligible to place and/or execute orders over the trading link, only clearing members who are specifically authorized by their parent exchange may actually facilitate their own trades over the link. In addition to authorization by the parent exchange to participate in the transaction of business over the link, CME firms may apply to SIMEX for membership and SIMEX firms may seek membership on the CME to obviate the need for agreements between the authorized clearing members of different exchanges providing that one member will execute the orders initiated by the other and vice-versa. According to *Law and Compliance Reporter*, a monthly publication of the Futures Industry Association, as of September 1984 some 20 domestic futures commission merchants had become members of SIMEX and over 80 CME member firms had been designated to participate as authorized clearing members for MOS trades. See LAW & COMPLIANCE REP., Sept. 1984, at 1.

<sup>26</sup> "Matching" is a term used industry-wide and is not peculiar to the trading link's operations or the MOS.

<sup>27</sup> "Clearing" is likewise a generic term.

<sup>28</sup> For a more detailed discussion of this facet of the operational process of futures trading, see 1 T. RUSSO, REGULATION OF THE COMMODITIES, FUTURES AND OPTIONS MARKET § 2.02 (1983); 1 P. JOHNSON, COMMODITIES REGULATION 97-100, §§ 1.31, 1.32 (1982).

<sup>29</sup> An order so processed is termed "marked-to-market," a process performed industry-wide.

<sup>30</sup> For a more detailed discussion of this aspect of the operations process, see T. RUSSO, *supra* note 28, and P. JOHNSON, *supra* note 28.

<sup>31</sup> See Agreement, *supra* note 16, at 3.



orders immediately prior to their transfer from executing exchange to originating exchange, the final step in the inter-market transfer process.

#### D. A Summary

To recapitulate the inter-exchange transfer process briefly, the procedure follows these general steps: 1) an originating clearing member transmits a customer order to an executing clearing member for execution; 2) the executing clearing member executes the order which is then processed by the executing exchange's clearing house; 3) the executing exchange's clearing house matches the trade between executing floor brokers; 4) the trade is then submitted to the originating exchange's clearing house MOS to match the trade between exchanges and to settle the trade among clearing members; and finally 5) the Inter-Exchange Administrator certifies the transaction and the trade is then transferred to the books of the originating clearing member as if the transaction had taken place on the originating clearing member's exchange.<sup>32</sup>

One last, but not unimportant, advantage accruing to those employing the CME-SIMEX link is that the link makes possible the trading of identical futures contracts on more than one exchange.<sup>33</sup> Heretofore, the trader who was forced to cover a market position on a second market often assumed an added element of risk by having to offset an already existing market position with a new contract of different specifications resulting in some market exposure and ultimately requiring one last transaction to extinguish the remaining position. Since the CME-SIMEX link has made possible the trading of identical contracts in Chicago and Singapore, the trading link provides both for the offset of opposite market transactions undertaken on either the CME or SIMEX and, for offset to be exact, the elimination of yet another previously unavoidable element of risk with which traders were forced to deal.

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<sup>32</sup> For a more complex, if more exact, summary of the operational procedures of the MOS, see Chicago Mercantile Exchange Perspectives 4 (Sept. 1984), or any of the CME or SIMEX publicity materials directly obtainable from the respective exchanges.

<sup>33</sup> For example, while Japanese yen futures contracts have the exact same specifications on both the CME and the New York Mercantile Exchange (12.5 million yen) and both the Chicago Board of Trade and the Kansas City Board of Trade trade an identical wheat futures contract (5,000 bushels), the simultaneous existence of identical futures contracts in this country is of no use to a trader seeking to insure against overnight risk on those market positions.

At this point, with the exception of the CME-SIMEX trading link, no foreign futures exchange involves contracts with specifications identical to those possessed by contracts traded on domestic exchanges. The London International Financial Futures Exchange ("LIFFE") trades contracts nearly identical to those traded on the Chicago Board of Trade ("CBT"), with whom LIFFE is soon to be affiliated; but regardless of how closely the CBT and LIFFE contracts resemble one another, they will not be completely fungible as are the contracts traded over the CME-SIMEX trading link.

An expanded trading day making possible a tremendous increase in trading flexibility, an elimination of wasteful commissions charges, and an ability to trade with perfect symmetry between two marketplaces separated by half a world, all account for the very real significance of this new intermarket, intercontinental trading link.

### III. CASE LAW

#### A. The Issues

Regardless of the manner in which the CME-SIMEX link reduces both overnight trading risk and market transaction costs, trading over the link will not be problem-free. Traders employing the trading link are certain to bring actions against brokers and brokerage houses alleging the same violations of the anti-fraud provisions of the CEA<sup>34</sup> as have been increasingly invoked since the formation of the Commodities Futures Trading Commission ("CFTC")<sup>35</sup> and the advent of more stringent regulation of the commodity futures industry.<sup>36</sup>

To the extent that fraudulent conduct is alleged by a complainant to have been committed in this country by a commodity futures broker (foreign or domestic), United States courts have unhesitatingly asserted subject matter jurisdiction and proceeded under the CEA.<sup>37</sup> In contrast, the exercise of jurisdiction over extraterritorial CEA claims is not as simple a matter. Federal courts have thus turned to the more developed body of law dealing with securities fraud under the Securities Acts of 1933 and 1934<sup>38</sup> for guidance as to when United States jurisdiction should be exercised over violations of the CEA alleged to have taken place abroad.<sup>39</sup> The United States courts' application of the CEA to this species of extraterritorial claim is complicated not only by an analysis of the materiality

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<sup>34</sup> The anti-fraud provisions of the CEA consist primarily of § 4 and § 6 of the Act. 7 U.S.C. §§ 4, 6 (1982).

<sup>35</sup> Congress established the CFTC in the Commodity Futures Trading Commission Act of 1974 ("CFTCA"), Pub. L. No. 93-463, 88 Stat. 1389 (1974).

<sup>36</sup> Public criticism of commodity markets, congressional concern over the increased use of futures markets for speculative purposes, and the widespread perception that the regulatory system established by the CEA was wholly inadequate to meet the demands facing it, prompted the revision in 1974 of the CEA by the Commodity Futures Trading Commission Act. For a history of the events leading up to the adoption of the CFTCA and an analysis of its provisions, see *Modernizing the Regulation of the Commodity Futures Markets*, 13 HARV. J. LEGIS. 35 (1975).

<sup>37</sup> See *infra* notes 47-68 and accompanying text.

<sup>38</sup> The Securities Act of 1933, 15 U.S.C. § 77a-bbbb (1982); The Securities Exchange Act of 1934, 15 U.S.C. § 78a-111 (1982).

<sup>39</sup> See, e.g., *Mormels v. Girofinance, S.A.*, 544 F. Supp. 815, 817 n.8 (S.D.N.Y. 1982) ("Securities cases and principles are used as persuasive aids to interpretation of the CEA."); *Miller v. New York Produce Exchange*, 550 F.2d 762, 769 n.2 (2d Cir.), *cert. denied*, 434 U.S. 823 (1977); *CFTC v. J.S. Love Assoc. Options*, 422 F. Supp. 652, 660 (S.D.N.Y. 1976).

of the conduct alleged to have taken place within this country, but also by more delicate issues involving United States foreign relations and the reach of United States laws. The ability now to trade futures contracts in Singapore with offset possible through MOS in Chicago has caused concern among traders, brokers, and regulators over whether individuals utilizing the trading link will be entitled to the same protections afforded traders who trade exclusively on United States futures exchanges.<sup>40</sup>

## B. The Law

*Tamari v. Bache & Co. (Lebanon)*<sup>41</sup> is the most recent case concerning the extraterritorial application of the anti-fraud provisions of the CEA. *Tamari* involved a claim by citizens and residents of Lebanon, three brothers, that defendant Bache & Co. (Bache Lebanon), a Lebanese corporation and wholly-owned subsidiary of Bache & Co., Inc., a Delaware corporation, committed acts of fraud and misrepresentation in violation of Sections 4b and 4c of the CEA<sup>42</sup> which resulted in losses to the plaintiffs in excess of two million dollars. In particular, the defendant was alleged by the Tamaris to have made misrepresentations regarding

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<sup>40</sup> See, e.g., N.Y. Times, Aug. 29, 1984, at D1, col. 1; Wall St. J., Sept. 6, 1984, at 2, col. 2; *The Link Felt 'Round the World*, FUTURES, Sept. 1984, at 54-56.

<sup>41</sup> 730 F.2d 1103 (7th Cir. 1984).

<sup>42</sup> Section 4(b) provides in pertinent part:

It shall be unlawful for any member of a contract market, or for any correspondent, agent or employee of any member, in or in connection with any order to make, or the making of, any contract of sale of any commodity in interstate commerce, made, or to be made, on or subject to the rules of any contract market, for or on behalf of any other person . . .

(A) to cheat or defraud or attempt to cheat or defraud such other person;

(B) willfully to make or cause to be made to such other person any false report or statement thereof, or willfully to enter or cause to be entered for such person any false record thereof;

(C) willfully to deceive or attempt to deceive such other person by any means whatsoever in regard to any such order or contract or the disposition of any such order or contract, or in regard to any act of agency performed with respect to such order or contract for such person; or

(D) to bucket such order, or to fill such order by offset against the order or orders of any other person, or willfully and knowingly and without the prior consent of such person to become the buyer in respect to any selling order of such person, or become the seller in respect to any buying order of such person.

Section 4(c) states:

(a) Meretricious transactions

It shall be unlawful for any person to offer to enter into, enter into, or confirm the execution of, any transaction involving any commodity, which is or may be used for (1) hedging any transaction in interstate commerce in such commodity or the products or byproducts thereof, or (2) determining the price basis of any such transaction in interstate commerce in such commodity, or (3) delivering any such commodity sold, shipped, or received in interstate commerce for the fulfillment thereof—

(A) if such transaction is, is of the character of, or is commonly known to the trade as, a "wash sale," "cross trade," or "accommodation trade," or is a fictitious sale; or

(B) if such transaction is used to cause any price to be reported, registered, or recorded which is not a true and bona fide price.

its expertise in the management of commodity futures accounts, to have given false advice concerning market conditions, to have mismanaged plaintiffs' accounts, and to have breached its fiduciary duty.<sup>43</sup>

Bache Lebanon responded to the Tamaris' allegations by moving in district court for a judgment on the pleadings or, in the alternative, for summary judgment in its favor. The grounds upon which Bache Lebanon sought summary disposition of the complaint were three: lack of subject matter jurisdiction,<sup>44</sup> collateral estoppel,<sup>45</sup> and no right of action under the CEA and its associated rules and regulations.<sup>46</sup> The district court disposed of Bache Lebanon's collateral estoppel and right of action arguments without difficulty. The issue of the court's subject matter jurisdiction over the cause of action brought by plaintiffs was the basis of the district court's denial of defendant's motion for summary judgment.

Bache Lebanon moved unsuccessfully for the district court to reconsider its denial of summary judgment; however, the district court did certify for appeal that part of its order dealing with the court's exercise of subject matter jurisdiction over the claims presented. The United States Court of Appeals for the Seventh Circuit permitted an interlocutory appeal to be taken on the narrow issue of federal subject matter jurisdiction, characterizing the precise legal issue to be considered as, "[w]hether the district court has subject matter jurisdiction under the CEA over a dispute between nonresident aliens when the trading of commodity futures contracts giving rise to the suit took place on United States exchanges but the contacts between the parties occurred in Lebanon."<sup>47</sup> Ultimately, the Seventh Circuit affirmed the district court's denial of Bache Lebanon's motion for summary judgment, holding that subject matter jurisdiction, did, in fact, exist.

The undisputed facts giving rise to this litigation are relatively straightforward but because the question presented concerned federal jurisdiction, a brief recapitulation of the events at issue, where they took

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<sup>43</sup> *Tamari v. Bache & Co. (Lebanon)*, 547 F. Supp. 309, 310 (N.D. Ill. 1982).

<sup>44</sup> *Id.*

<sup>45</sup> Bache Lebanon asserts that the issues raised by the Tamaris were collaterally estopped by an arbitrator's decision in favor of Bache & Co., Inc. (Delaware). The district court found, however, that since Bache Lebanon was not a party to the arbitration it would have to show that it was entitled to rely on the arbitration decision under principles of collateral estoppel. In the opinion of the district court, Bache Lebanon failed to make such a showing. *Id.* at 316.

<sup>46</sup> The district court rejected Bache Lebanon's argument that the Tamaris had no private right of action under § 4(b) and § 4(c) of the CEA stating, "[p]rior to the 1974 amendments to the CEA, federal courts had routinely recognized a private cause of action under the statute, and in the recent case of *Merrill, Lynch, Pierce, Fenner & Smith v. Curran* . . . the Supreme Court held that a private cause of action survived the 1974 amendments." *Id.* (citation omitted).

<sup>47</sup> 730 F.2d at 1104.

place, their whereabouts, and the locations of the parties involved is appropriate. Plaintiffs, Lebanese citizens and residents, maintained commodity futures trading accounts with the defendant Lebanese corporation. In trading for plaintiffs' accounts, Bache Lebanon would receive orders from plaintiffs at its office in Beirut and would then transmit them to Bache & Co., Inc. in the United States for execution on either the CME or the Chicago Board of Trade. All conversations between the plaintiffs and the defendant prior to the opening of plaintiffs' accounts and regarding what later were alleged to be fraudulently induced trades resulting in plaintiffs' loss in excess of two million dollars, took place in Lebanon. Only the execution of plaintiffs' orders occurred in the United States.

### C. The District Court

In its analysis of the facts in *Tamari*,<sup>48</sup> the district court looked to the analogous body of securities law dealing with the transnational scope of the Securities Exchange Acts of 1933 and 1934.<sup>49</sup> Courts grappling with the transnational application of the Securities Exchange Acts fashioned two distinct but related tests in an effort to ascertain whether the particular facts surrounding a fraudulent scheme warranted application of United States statutes or whether such a scheme should instead be dealt with under the laws of the jurisdiction in which the fraud had been perpetrated. These tests, to which the district court turned initially for guidance and which eventually formed the basis of the court's denial of defendant's motion, are termed the "conduct test" and the "effects test."

#### 1. The Conduct Test

First fashioned by the Second Circuit in *Leasco Data Processing Equipment Corporation v. Maxwell*,<sup>50</sup> the conduct test arose out of a case brought under Section 10b of the Securities Exchange Act of 1934<sup>51</sup> in which plaintiffs, United States citizens, alleged fraud surrounding their purchase, through British brokers on the London Stock Exchange, of

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<sup>48</sup> 547 F. Supp. 309 (N.D. Ill. 1982).

<sup>49</sup> *Id.* at 311.

<sup>50</sup> 468 F.2d 1326 (2d Cir. 1972).

<sup>51</sup> Section 10(b) provides in relevant part:

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

(b). To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

shares in a British corporation whose stock was not registered or traded on United States exchanges.<sup>52</sup> Reversing the district court's dismissal of the case for lack of subject matter jurisdiction, the Second Circuit in *Leasco* upheld jurisdiction, finding that "abundant misrepresentations in the United States"<sup>53</sup> had taken place and that such domestic conduct was sufficient to enable federal courts to apply the Securities Exchange Act of 1934 to the case at bar even though the sale of securities took place on the London Stock Exchange.<sup>54</sup> The doctrinal basis of the conduct test can be traced to section seventeen of The Restatement (Second) of Foreign Relations Law of the United States.<sup>55</sup> The essence of section seventeen of the Restatement was distilled by the court of appeals in *Leasco* into a rule providing that, "the nation where the conduct has occurred has jurisdiction to displace foreign law and to direct its courts to apply its own."<sup>56</sup>

Formulation of the conduct test in *Leasco* has resulted in attempts by the judiciary to define more precisely what types of conduct will be sufficient to justify the exercise of United States jurisdiction over extra-territorial Securities Exchange Act claims. The district court in *Tamari* traced the progeny of *Leasco*, which limited the reach of the conduct test in the field of securities fraud, and settled upon the standard of conduct established in another securities fraud case, *Travis v. Anthes Imperial, Ltd.*:<sup>57</sup> "significant conduct with respect to the alleged violation [of the Securities Exchange Act] in the U.S."<sup>58</sup> Similarly, in *Bersch v. Drexel Firestone, Inc.*,<sup>59</sup> the Second Circuit further narrowed its own holding in *Leasco* when it stated: "We see no reason to extend it [satisfaction of the conduct test] to cases where the U.S. activities are merely preparatory . . . and are relatively small in comparison to those abroad."<sup>60</sup> Finally, in *IIT v. Vencap*,<sup>61</sup> the Second Circuit made plain that only material conduct in furtherance of a fraudulent scheme would satisfy the conduct

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<sup>52</sup> 468 F.2d at 1330-33.

<sup>53</sup> *Id.* at 1335.

<sup>54</sup> *Id.* at 1339.

<sup>55</sup> Section 17 provides:

A state has jurisdiction to prescribe a rule of law

(a) attaching legal consequences to conduct that occurs within its territory, whether or not such consequences are determined by the effects of the conduct outside the territory, and

(b) relating to a thing located, or a status or other interest localized, in its territory.

RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 17 (1965).

<sup>56</sup> 468 F.2d at 1339.

<sup>57</sup> 473 F.2d 515 (8th Cir. 1973).

<sup>58</sup> *Id.* at 524.

<sup>59</sup> 519 F.2d 974 (2d Cir.), *cert. denied*, 423 U.S. 1018 (1975).

<sup>60</sup> *Id.* at 987.

<sup>61</sup> 519 F.2d 1001 (2d Cir. 1975).

test. The *Vencap* court held that: “[J]urisdiction is limited to the perpetration of fraudulent acts themselves and does not extend to mere preparatory activities or the failure to prevent fraudulent acts when the bulk of the activity was performed in foreign countries.”<sup>62</sup>

Sensitive to the interpretations of the conduct test which had evolved, the district court in *Tamari* articulated the focus of the inquiry involved in the conduct test as not “the residence or citizenship of the parties and the foreign or domestic nature of the securities involved,”<sup>63</sup> but instead, “the relative importance of activities within the U.S. to the success of the alleged scheme to defraud.”<sup>64</sup> Structuring its inquiry to determine initially whether Bache Lebanon’s conduct constituted conduct within the United States and secondly to examine the “relative importance” of any domestic conduct found to have been committed in furtherance of defendant’s alleged fraudulent scheme, the district court concluded that conduct within the United States had taken place<sup>65</sup> and that the conduct was “substantial”<sup>66</sup> or “significant”<sup>67</sup> when viewed “in relation to its importance to the success of the alleged scheme to defraud.”<sup>68</sup>

In support of its conclusion with respect to the conduct test, the district court found that the transmission by Bache Lebanon of the Tamaris’ orders from Beirut to Chicago constituted conduct within the United States.<sup>69</sup> The conclusion that the domestic conduct was both substantial and significant was buttressed by the finding that “Bache Lebanon’s writing of the Tamaris’ orders to Chicago and the execution of those orders on the Chicago exchanges were the final steps in the alleged scheme.”<sup>70</sup> The execution of plaintiffs’ orders in this country proved of particular importance to the district court, as evidenced by its characterization of the execution as “a necessary and foreseeable step in a scheme to defraud and thus substantial conduct within the U.S.”<sup>71</sup> Despite the

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<sup>62</sup> *Id.* at 1018.

<sup>63</sup> 547 F. Supp. at 313.

<sup>64</sup> *Id.* at 313-14.

<sup>65</sup> *Id.* at 315.

<sup>66</sup> *Id.*

<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> The district court premised this conclusion on the findings of several other courts that “making phone calls or sending mail to the United States should be deemed conduct within the United States for jurisdictional purposes in transnational cases.” *Id. See, e.g., Continental Grain (Australia) Pty., Ltd. v. Pacific Oilseeds, Inc.*, 592 F.2d 409, 420 n.18 (8th Cir. 1979) (“Both the place of sending and the place of receipt constitute locations in which conduct takes place when the mails or instrumentalities of interstate commerce are used to transmit communications.”)

<sup>70</sup> 547 F. Supp. at 315.

<sup>71</sup> *Id.*

limitations placed on *Leasco* by its progeny, the district court in *Tamari* found material conduct in furtherance of Bache Lebanon's alleged fraudulent scheme had occurred in this country and thus the conduct test was deemed satisfied by virtue of defendant's domestic activities.

## 2. The Effects Test

Like the conduct test, the effects test was also first fashioned by the Second Circuit in a case dealing with an alleged violation of Section 10b of the 1934 Securities Exchange Act, but in the context of a different factual situation with an entirely different focus. The effects test grew out of *Schoenbaum v. Firstbrook*,<sup>72</sup> a case in which an American shareholder in a Canadian corporation brought a derivative suit alleging fraud under the Securities Exchange Act of 1934 where the challenged transaction took place in Canada but involved Canadian stock registered on the American Stock Exchange.<sup>73</sup> Once again, the Second Circuit found itself reversing a district court which had granted summary judgment in favor of the defendant on the basis of a lack of jurisdiction. The Second Circuit in *Schoenbaum* held instead that the Securities Exchange Act of 1934 could be applied extraterritorially, "in order to protect domestic investors who have purchased foreign securities on American exchanges and to protect the domestic securities market from the effects of improper foreign transactions in American securities."<sup>74</sup>

The foundation for the effects test is section eighteen of the Restatement (Second) of Foreign Relations Law of the United States.<sup>75</sup> While the use of the effects test was intended to protect United States investors from the adverse effects of fraudulent schemes concocted abroad and executed on domestic exchanges, the question arose as to what type of showing of an adverse effect on United States investors or domestic markets would be necessary to satisfy the effects test. As was the case in *Leasco*, a period of judicial retrenchment followed *Schoenbaum* during which the

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<sup>72</sup> 405 F.2d 200 (2d Cir.), *rev'd on other grounds*, 405 F.2d 215 (2d Cir. 1968) (en banc) (affirming previous decision as to jurisdiction), *cert. denied*, 395 U.S. 906 (1969).

<sup>73</sup> *Id.* at 204-05.

<sup>74</sup> *Id.* at 206.

<sup>75</sup> RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 18 (1965). Section 18 provides:

A state has jurisdiction to prescribe a rule of law attaching legal consequences to conduct that occurs outside its territory and causes an effect within its territory, if either

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



effects test was refined. The result of this scrutiny was an effects test calculated to be triggered only by bona fide threats to the integrity of United States markets.<sup>76</sup> Hereafter, when the securities at issue in a particular case are not registered on American exchanges and no showing of a particularized harm to domestic interests is made, any "general" adverse effect claimed by a plaintiff will be found to be too hypothetical or indirect.<sup>77</sup>

The district court in *Tamari* interpreted the primary inquiry involved in the effects test to be whether foreign conduct occurring abroad causes foreseeable and substantial harm to interests within the United States or whether, as the court stated more succinctly, "there is a substantial impact on domestic investors or on the domestic market."<sup>78</sup> Applying the effects test to the facts in *Tamari*, the district court concluded that since the transactions at issue "directly involved domestic futures exchanges"<sup>79</sup> no particularized harm had to be proven by plaintiffs.<sup>80</sup> Harm could be presumed to have befallen domestic exchanges in the instant case, the court found, because the fraud alleged by the Tamaris directly implicated the integrity of an American marketplace.<sup>81</sup> Thus, although all of the alleged fraudulent misrepresentations made by Bache Lebanon had taken place abroad and even though plaintiffs could demonstrate no adverse effect to a domestic market as the direct result of the executions of their orders in this country, the protection of the integrity of domestic exchanges was found to be of such paramount importance that adverse effects were presumed to have occurred simply by

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<sup>76</sup> The efforts by the judiciary to constrict the limits of the effects test were prompted by a concern that affidavits by economists or other experts might persuade courts to accept "general" adverse effects of market manipulation as sufficient to satisfy the effects test. Therefore, the attempted refashioning of the effects test sought to have courts require a more substantial causal link between the fraudulent activity complained of and any adverse effects on domestic markets alleged. See *Bersch*, 519 F.2d 974, in which plaintiffs claimed that jurisdiction existed under the effects test on account of the adverse general effect the collapse of an international corporation would have on United States stock exchanges even though the demised company's shares were not traded on United States exchanges. The Second Circuit in *Bersch* rejected such "general" adverse impact stating:

[W]e do not doubt that the collapse of IOS after the offering had an unfortunate financial effect in the United States. Nevertheless we conclude that the *generalized* effects described by Prof. Mendelson would not be sufficient to confer subject matter jurisdiction over a damage suit by a foreigner under the anti-fraud provisions of the securities laws.

*Id.* at 988 (emphasis added).

See also *Recaman v. Barish*, 408 F. Supp. 1189, 1199 n.11 (E.D. Pa. 1975) (study showing general adverse impact on economy in case where securities were not traded on domestic exchanges held to be insufficient under the effects test).

<sup>77</sup> 547 F. Supp. at 313.

<sup>78</sup> *Id.* at 311.

<sup>79</sup> *Id.* at 313.

<sup>80</sup> *Id.*

<sup>81</sup> *Id.*

virtue of potentially fraudulent trading on a United States futures market.

Having decided that both the conduct and the effects tests had been satisfied by the facts presented in *Tamari*, the district court held that subject matter jurisdiction existed, and defendant's motion for summary judgment was denied.

#### D. The Court of Appeals

On appeal,<sup>82</sup> Bache Lebanon asserted that the district court had failed to consider whether Congress had intended the CEA to apply to alleged illegal acts committed abroad by foreign citizens and also that the conclusions of the district court as to the satisfaction of the conduct and effects tests were mistaken.<sup>83</sup>

The Court of Appeals for the Seventh Circuit agreed with Bache Lebanon's initial assertion and undertook an examination of the legislative history of the CEA. While recognizing the paucity of evidence germane to the issue of the Act's extraterritorial application,<sup>84</sup> the court was able to discern that one of Congress' fundamental purposes in enacting the CEA was "to ensure fair practice and honest dealings on commodity exchanges, for the protection of the market itself as well as those who could be injured by unreasonable fluctuations in commodity prices."<sup>85</sup> The court found that specific congressional intent relevant to whether nonresident aliens could be held subject to the CEA's provisions when the conduct proscribed had been committed abroad was nowhere expressly evident in the Act's text.

The absence of specific legislative guidance on the matter of the transnational scope of the CEA left to the court's consideration both the overarching aims of the CEA's legislative scheme and the interpretation put forward by the Commodity Futures Trading Commission ("CFTC") as *amicus curiae*. The position adopted by the CFTC stressed that congressional reports on the CEA in 1974<sup>86</sup> and 1982<sup>87</sup> as well as the

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<sup>82</sup> 730 F.2d 1103.

<sup>83</sup> *Id.* at 1106.

<sup>84</sup> *Id.* at 1106-07.

<sup>85</sup> *Id.* at 1106 (citing S. Rep. No. 93-1131, 93d Cong., 2d Sess. 14 (1974), reprinted in 1974 U.S. CODE CONG. & AD. NEWS 5843, 5856).

<sup>86</sup> See H.R. REP. NO. 93-975, 93d Cong., 2d Sess. (1974). Known as the Commodity Futures Trading Commission Act, *supra* notes 33, 34, the Act expressly established the CFTC to strengthen the regulation of futures markets.

<sup>87</sup> See S. REP. NO. 97-384, 97th Cong., 2d Sess. (1982). The further amendment of the CEA by the Futures Trading Act of 1982, Pub. L. No. 97-444, 96 Stat. 2294 (1982), specifically § 204, added a new subsection (b) to § 4 of the CEA which provides:

The Commission [CFTC] may adopt rules and regulations proscribing fraud and requiring min-

CFTC's own rules and regulations dealing with the increased foreign participation on domestic commodity futures exchanges<sup>88</sup> evinced an attitude on the part of Congress to allow the application of the CEA to nonresident aliens employing United States markets.<sup>89</sup> Conversely, Bache Lebanon placed great reliance upon the CFTC's own decision to exclude "foreign associated persons of domestic firms"<sup>90</sup> from the CFTC's registration requirements<sup>91</sup> and asserted that this decision indicated a purposeful policy decision to limit the reach of the CEA and the rules and regulations promulgated thereunder.<sup>92</sup>

Its examination of the CEA's legislative history having failed to prove dispositive, the court admitted that no conclusive evidence existed to indicate that Congress did or did not intend the CEA to apply to foreign commodity dealers or brokers when their fraudulent activities occurred outside of the United States.<sup>93</sup> The court, therefore, settled upon the conduct and the effects tests, borrowed by the district court in *Tamari* from the analogous body of securities law, as the appropriate analytical tools with which to fashion standards controlling the extraterritorial application of the CEA.<sup>94</sup>

Given the Court of Appeals' reading of the CEA's *raison d'être*, "to ensure the integrity of the domestic commodity markets,"<sup>95</sup> it followed logically that the Court of Appeals should affirm the district court's ap-

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imum financial standards, the disclosure of risk, the filing of reports, the keeping of books and records, the safeguarding of customers' funds and the registration with the Commission by any person located in the United States, its territories or possessions, who engages in the offer or sale of any contract of sale of a commodity for future delivery that is made or to be made on or subject to the rules of a board of trade, exchange or market located outside the United States, its territories or possessions. . . .

<sup>88</sup> See, e.g., 17 C.F.R. §§ 17.00, 21.02 (1983) (requiring foreign brokers and traders to comply with CFTC reporting procedures and "special calls" for information regarding their market positions); 17 C.F.R. § 30.02 (1983) (prohibiting fraud in the domestic offer and sale of foreign futures contracts).

<sup>89</sup> 730 F.2d at 1107.

<sup>90</sup> *Id.*

<sup>91</sup> 17 C.F.R. § 3.12 (1983) (rescinding registration requirements for foreign associated persons of domestic firms).

<sup>92</sup> 730 F.2d at 1107. However, no doubt in response to the issues raised by Bache Lebanon in *Tamari*, the CFTC has published an "Advance Notice of CFTC Rulemaking on Foreign Futures" to determine whether rules in addition to Rule 30.02 (prohibiting fraud in the domestic offer or sale of foreign futures contracts) are needed. See 16 Sec. Reg. L. Rep. (BNA) 1272 (1984). Reasons given by the CFTC for considering additional rules and regulations include:

[the] growing volume of foreign futures contracts; a projected increase in the number of foreign futures contracts that closely parallel contracts offered in the United States or that may be of particular interest to U.S. citizens [and] the development of proposed links between foreign and U.S. exchanges. . . .

*Id.*

<sup>93</sup> 730 F.2d at 1103.

<sup>94</sup> *Id.*

<sup>95</sup> *Id.* at 1108.

plication of the conduct and effects tests to the facts in *Tamari*. The Court of Appeals held that only by extending the reach of the anti-fraud provisions of the CEA to foreign traders who choose to transact business on domestic exchanges could the fullest protection of domestic markets be achieved.<sup>96</sup>

Bache Lebanon filed a petition for certiorari with the United States Supreme Court on May 21, 1984<sup>97</sup> and on October 2, 1984<sup>98</sup> the Court denied the petition.

#### IV. PAROCHIALISM OR PRUDENT REGULATORY POLICY

##### A. The Extent of Internationalization

As if the evolution of a transnational trading link were not enough evidence of the increasing internationalization of world financial markets, it is a fact that while United States private investment in foreign securities totalled \$19.6 billion in 1971,<sup>99</sup> by 1981 the same figure eclipsed \$62 billion.<sup>100</sup> Not surprisingly, foreign investment in United States securities other than Treasury securities also exploded during the decade of the seventies growing from \$25.6 billion in 1971<sup>101</sup> to \$74 billion in 1981.<sup>102</sup> Preliminary figures indicate that, as of 1983, United States private investment in foreign securities reached \$84.8 billion<sup>103</sup> while foreign investments in non-United States Treasury Securities exceeded \$114.6 billion<sup>104</sup>—increases over the 1982 totals of roughly twelve percent and twenty-two percent respectively. Securities and Exchange Commissioner Barbara Thomas has offered the following explanation of what she terms the “meteoric rise” in international financial transactions:

As global commerce has expanded, multinational corporations have flourished, and technology has advanced, transnational securities transactions have increased dramatically. In this connection, it is now commonplace for issuers to cross their national borders to raise capital in foreign

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<sup>96</sup> The court of appeals reasoned that: “Congress would have wished domestic markets and domestic investors to be protected from improper foreign transactions.” *Id.* The court concluded by speculating as to what acceptance of the position espoused by Bache Lebanon would eventually entail; “[w]ere we to construe the CEA as inapplicable to the foreign agents of commodity exchange members when they facilitate trading on domestic exchanges, the domestic commodity futures market would not be protected from the negative effects of fraudulent transactions or originating abroad.” *Id.*

<sup>97</sup> 730 F.2d 1103, *petition for cert. filed*, 52 U.S.L.W. 2575 (U.S. May 21, 1984) (No. 83-1904).

<sup>98</sup> 730 F.2d 1103, *cert. denied*, 53 U.S.L.W. 3240, (U.S. Oct. 2, 1984) (No. 83-1904).

<sup>99</sup> See U.S. Dept. of Commerce, 53 SURV. CURRENT BUS. 21 (Aug. 1973).

<sup>100</sup> See U.S. Dept. of Commerce, 61 SURV. CURRENT BUS. 56 (Aug. 1981).

<sup>101</sup> See *supra* note 96.

<sup>102</sup> See *supra* note 97.

<sup>103</sup> See U.S. Dept. of Commerce, 64 SURV. CURRENT BUS. 75 (June 1984).

<sup>104</sup> *Id.*

markets, and consequently, the commercial interface between corporations and foreign parties through securities transactions has become a frequent occurrence. In addition, sophisticated electronics and data processing systems have enabled investors to purchase and sell securities, and transfer money, virtually instantaneously in any part of the world. Thus, no longer encumbered by geographical limitations, investors have increasingly sent their money abroad to invest in foreign securities, seeking higher profits and less risk through diversified investment portfolios.<sup>105</sup>

It is in response to the internationalization of securities and futures markets that the extraterritorial application of United States regulatory statutes has become a primary concern of government regulators and the securities industries of both this country as well as those countries whose foreign capital and capital markets are most closely tied to domestic investment instruments and markets.<sup>106</sup> The advent of transnational trading links<sup>107</sup> provides a new framework within which to analyze the difficulties, potential conflicts and policy arguments which have accompanied attempts to extend the application of United States law to transactions originating abroad and executed on United States securities or futures markets. Given the truly international composition of today's market participants<sup>108</sup> and the seemingly unending variety of sophisticated schemes devised to capitalize upon the unsuspecting investor or the loosely-regulated marketplace,<sup>109</sup> the extension of United States laws to police the execution of foreign transactions on domestic markets should be viewed as less objectionable than has heretofore been the case.<sup>110</sup>

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<sup>105</sup> Thomas, *Extraterritoriality in an Era of Internationalization of the Securities Market: The Need to Revisit Domestic Policies*, 35 RUTGERS L. REV. 453 (1983).

<sup>106</sup> See, e.g., Thomas, *Internationalization of the Securities Markets: An Empirical Analysis*, 50 GEO. WASH. L. REV. 155 (1982). Thomas illustrates the remarkable interconnectedness of world securities markets and considers how various United States regulatory policies may have a positive or adverse impact on foreign activity in United States markets. For a foreign perspective of the impact of United States extraterritorial jurisdiction in securities and antitrust matters, see David Lord Hacking, *The Increasing Extraterritorial Impact of U.S. Laws: A Case for Concern Amongst Friends of America*, 1 NW. J. INT'L L. & BUS. 1 (1979).

<sup>107</sup> See *supra* note 10.

<sup>108</sup> See, e.g., Thomas, *supra* note 106, and the statistical breakdown of United States investment abroad and foreign investment in the United States cited *supra* notes 96-101. See also *Proposed Duties of Futures Comms. Merchants Towards Accounts of Foreign Brokers and Traders*, [1980-1982 Transfer Binder] Comm. Fut. L. Rep. (CCH) § 21,028 (CFTC May 14, 1980); Interview with CFTC Chairman Susan Phillips in 16 Sec. Reg. & L. Rep. (BNA) 169 (Jan. 27, 1984); *CFTC Rulemaking on Foreign Futures*, 16 Sec. Reg. & L. Rep. (BNA) 1272 (July 27, 1984).

<sup>109</sup> See references made to enforcement matters in: SEC DOCKET; SEC NEWS DIGEST; and U.S. SECURITIES AND EXCHANGE COMMISSION ANNUAL REPORT.

<sup>110</sup> See, e.g., Thomas, *supra* note 105; David Lord Hacking, *supra* note 106; Note, *American Adjudication of Transnational Securities Fraud*, 89 HARV. L. REV. 553 (1976); Sandberg, *The Extraterritorial Reach of American Economic Regulation: The Case of Securities Law*, 17 HARV. INT'L L.J. 315 (1976); Comment, *The Transnational Reach of Rule 10b-5*, 121 U. PA. L. REV. 1363 (1973).

## B. The Debate

### 1. Arguments Against Liberal Extraterritorial Jurisdiction

The securities and futures industries have advanced a number of arguments opposing liberal extraterritorial application of domestic laws to suits alleging fraud in transactions emanating from abroad. Initially, industry representatives claim that broadened United States jurisdiction would further overload crowded federal court calendars and leave the "precious resources" of United States courts and enforcement agencies stretched beyond the breaking point.<sup>111</sup> Another charge leveled at attempts to expand United States extraterritorial jurisdiction concerns the likelihood that the exercise of such jurisdiction will chill the trading activity of foreign market participants who might fear that their foreign customer-broker relationships will be governed by unfamiliar and unusually restrictive United States laws.<sup>112</sup> And finally, there is the complaint that, under the present tests for determining the existence of United States jurisdiction, no consistent standards have yet been fashioned to adequately characterize and put market participants on notice as to exactly what degrees of "conduct" and what quantum of "effect" are sufficient to trigger the exercise of extraterritorial application of United States law.<sup>113</sup>

Even the CFTC and the SEC, which have generally supported the slow but steady expansion of extraterritorial jurisdiction<sup>114</sup> in furtherance of their mandates to protect the interests of United States investors and the integrity of United States markets, have acknowledged the possibility of a conflict between United States laws and the laws of other nations from which extraterritorial claims may originate.<sup>115</sup> The potential

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<sup>111</sup> This reasoning was put forward by Bache Lebanon in its petition for certiorari to the United States Supreme Court and is taken directly from the opinion of the Second Circuit in *Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974, 985, *cert. denied*, 423 U.S. 1018 (1975). See also *Fidenas AG v. Compagnie Internationale*, 606 F.2d 1001 (2d Cir. 1975).

<sup>112</sup> See Amicus Brief in Support Of Petition For Writ of Certiorari filed by the Futures Industry Association, Inc. and ten United States futures exchanges in *Tamari v. Bache & Co. (Lebanon)*, at ix.

<sup>113</sup> See, e.g., Note, *Extraterritorial Application of the Federal Securities Laws: The Need for Reassessment*, 14 J. INT'L L. & ECON. 529 (1980); Norton, *Extraterritorial Jurisdiction of U.S. Antitrust and Securities Laws*, 28 INT'L & COMP. L.Q. 575 (1979); Thomas, *supra* note 105.

<sup>114</sup> For example, the CFTC filed an amicus brief with the Seventh Circuit urging affirmance of the result reached in *Tamari v. Bache & Co. (Lebanon)* in the district court. See *supra* text accompanying notes 86-87. Both the CFTC and the SEC submitted amicus briefs urging the result reached by the Second Circuit in *Psimenos v. E.F. Hutton & Co.*, 722 F.2d 1041 (2d Cir. 1983) (foreign initiated trading activities on United States commodities markets are significant acts and are sufficient to establish subject matter jurisdiction in United States courts).

<sup>115</sup> See, e.g., Report of the Division of Trading and Markets and the Division of Economic Analysis of the Commodity Futures Trading Commission on the Proposed Mutual Offset System between

for continued extension of United States jurisdiction over allegations of foreign securities and commodities fraud culminating in execution on a United States exchange could, the agencies maintain, interfere with the regulatory practices and governmental policies of foreign nations which demonstrate an interest in prosecuting for themselves offenses allegedly perpetrated within their national borders.<sup>116</sup>

## 2. *Arguments Favoring Liberal Extraterritorial Jurisdiction*

As has already been stressed, however, the inherent nature of an international trading link—its active courtship of the virtual dependence upon an international clientele—affords a timely opportunity to reevaluate many of the traditional criticisms and concerns surrounding the extraterritorial application of United States securities and commodities laws. For example, the argument that the continued transnational application of United States securities and commodities laws to allegations of fraud occurring abroad will result in an all but unbearable and legislatively-unintended burden being placed upon United States courts and enforcement agencies is largely undercut by the exacting administrative scrutiny and governmental regulation without which a trading link could never have commenced operation. It cannot be seriously asserted that the CFTC and the congressional committees charged with its oversight<sup>117</sup> did not foresee that a trading link between a domestic and a foreign futures exchange would result in the creation of a single entity—for purposes of mutual offset—over which both the United States and Singapore could be called upon to exercise jurisdiction.

Increased governmental involvement in the regulation and operation of such ventures as the CME-SIMEX trading link as well as a clearly discernible pattern on the part of United States courts to apply extraterritorial jurisdiction to claims arising abroad,<sup>118</sup> manifest a common concern for the stringent policing of United States markets and the vigilant protection of market participants.<sup>119</sup> No branch of government is more keenly aware than the judiciary of the congestion which plagues its dock-

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the Chicago Mercantile Exchange and the Singapore International Monetary Exchange 120-24 (Aug. 28, 1984).

<sup>116</sup> *Id.*

<sup>117</sup> As a result of the historical association between agriculture and commodities trading, congressional oversight of the regulation of domestic commodity markets has been vested in the House Agriculture Committee and the Senate Committee on Agriculture and Forestry.

<sup>118</sup> See *supra* notes 50-81 and accompanying text.

<sup>119</sup> The source of the judiciary's concern for the protection of market participants as well as the integrity of the markets themselves is found in: S. REP. NO. 93-1131, 93d Cong., 2d Sess. 18-24 (1974); S. REP. NO. 97-384, 97th Cong., 2d Sess. (1982); H.R. REP. NO. 93-975, 93rd Cong., 2d Sess. (1974). See *supra* notes 85-89 and accompanying text.

ets; nevertheless, the judicial circuits in which extraterritorial securities and commodities claims have been brought<sup>120</sup> have felt compelled to apply United States laws in order to comply with the legislative schemes codified in Section 10(b) of the Securities Exchange Act of 1934 and Section 4(b) of the Commodities Exchange Act. Congress, for its part, while possessing the ability to adopt legislation to curtail what critics charge is an unwarranted extension of United States jurisdiction, has, without comment, permitted the continued evolution of case law supporting the extraterritorial application of United States laws to foreign claims involving some conduct within or some effect upon investors or markets in this country.<sup>121</sup> Thus, the arguments that the judiciary is being overrun by a "steady flow into the federal courts of disappointed foreign speculators in commodities futures and financial futures"<sup>122</sup> and that such an insufferable burden was never the intent of Congress in passing securities and commodities legislation are belied both by history and legislative inaction suggesting the contrary.

The charge that extraterritorial application of United States laws to United States market activity initiated abroad will result in a chilling of such activity with a concomitant decrease in both overall market liquidity and total foreign investment in United States markets is similarly untenable in a world where national economies have grown increasingly intertwined. Once again, the development of the CME-SIMEX trading link provides an interesting case in point. Presumably, those choosing to execute transactions utilizing the trading link will have based their choice of market upon the distinct advantages an international trading link has to offer.<sup>123</sup> Irrespective of ample judicial precedent,<sup>124</sup> logic alone should put all market participants on notice that jurisdiction over claims of fraud precedent to CME-SIMEX execution could be exercised in either the United States or Singapore in furtherance of a legitimate national interest in policing the integrity and ensuring the viability of the trading

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<sup>120</sup> The issue of extraterritorial application of United States securities and commodities statutes has been litigated in the Second, Third, Seventh, Eighth, and Ninth Circuits.

<sup>121</sup> Although Congress clearly possesses the authority to clarify its legislative intent with respect to the extraterritorial application of United States securities and commodities statutes, no legislation has been forthcoming to modify the case law which has overwhelmingly favored extension of applicable United States laws.

<sup>122</sup> See *Bache Lebanon's Petition For A Writ Of Certiorari To The United States Court of Appeals for the Seventh Circuit* (May 21, 1984).

<sup>123</sup> See *supra* text accompanying notes 15-33.

<sup>124</sup> See *Tamari v. Bache & Co. (Lebanon)*, 547 F. Supp. 309 (N.D. Ill. 1982) (summarizing the growing body of case law).



link.<sup>125</sup> Moreover, notions of equity argue for the proposition that one seeking to benefit by use of the trading link (in effect, the markets of another country) must bear any burden which might result from the application of United States or Singapore law instead of the laws of the transgressor's own nation.<sup>126</sup> The application of United States law to a claim with origins abroad cannot be viewed fairly as a penalty or as a protectionist barrier to international commerce, but rather should be understood as a risk willingly assumed by those seeking the advantages of the markets of a foreign nation, a nation with a vital interest in the lawful conduct of its markets' participants.

Finally, the criticisms leveled by members of the securities and futures industry at the standards currently employed by United States courts to determine the existence of their jurisdiction seem increasingly unpersuasive in the context of such bold new international ventures as transnational trading links. Whereas in *Tamari*,<sup>127</sup> the district court struggled to evaluate and characterize the nature of the conduct performed in the United States by Bache & Co. as agent for Bache Lebanon,<sup>128</sup> parties wishing to execute some part of their transactions abroad must be made to appreciate the necessity of abiding by the laws of the foreign forum whose commercial benefits they seek to enjoy. Rather than attempting to characterize a species of conduct or effect as "preparatory," "significant," or "important,"<sup>129</sup> an inherently subjective task,<sup>130</sup> the interest that the United States has in assuring the integrity of its marketplaces for the sake of both domestic as well as international economic stability should now be sufficient to give jurisdiction to a United States court when a complainant so chooses and the facts so warrant. Similarly, the virtual impossibility of demonstrating a nexus between a defendant's fraudulent conduct and discernible effect upon a United States

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<sup>125</sup> See Sections 17 and 18, the RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW OF THE UNITED STATES §§ 17-18 (1965).

<sup>126</sup> Not only do notions of equity argue that one seeking the benefits of transacting commerce in a foreign forum should be subject to the laws of that forum but an analogy to the doctrine of assumption of risk also seems appropriate. In effect, one who knowingly undertakes to transact business in or on the markets of another nation may be assumed to have implicitly consented to bear any burden or absorb any injury resulting from the application of the laws of the foreign forum.

<sup>127</sup> 547 F. Supp. 309 (N.D. Ill. 1982).

<sup>128</sup> See *supra* text accompanying notes 49-71.

<sup>129</sup> *Id.*

<sup>130</sup> Much of the criticism leveled at the conduct test has centered around the extent to which characterizing degrees of alleged fraudulent conduct is really a metaphysical exercise, as concerned with the semantics as with principles of law. See, e.g., Note, *supra* note 113, at 549; Thomas, *supra* note 105, at 459 (the conduct and effects tests are, "too simple and mechanistic to adequately express the important considerations of policy that should precede assertion of jurisdiction over international transactions.")

marketplace<sup>131</sup> would disappear as a prerequisite to establishing jurisdiction where use of the trading link, in and of itself, would constitute an acknowledgement of probable United States jurisdiction.

### C. A Proposed Rationale for United States Extraterritorial Jurisdiction

Of considerably greater importance than the arguments voiced by private commercial interests against a policy of liberal United States extraterritorial jurisdiction in securities fraud cases is a growing concern among our allies and trading partners that:

agencies of the United States government, over an everwidening field of international commerce, are persistently making more and more attempts to impose domestic laws on persons and corporations who are not U.S. nationals and who are acting outside the territory of the United States.<sup>132</sup>

There can be little doubt that some in the international community see the extraterritorial application of United States securities and commodities laws as an attempt, in Chief Justice Burger's words: "[to] have trade and commerce in world markets and international waters exclusively on our terms, governed by our laws and resolved in our courts."<sup>133</sup> The application of domestic laws to securities transactions either executed on or having some effect upon United States markets, however, should not be confused with the extraterritorial application of United States anti-trust and business disclosure statutes which possess a far greater likelihood of interfering with the economic policies and regulatory practices of our partners in commerce.<sup>134</sup>

Crucial at the outset is a realization that both Section 10(b) of the Securities Exchange Act of 1934 and Section 4(b) of the CEA require some dealing in interstate commerce before a violation of either Act's anti-fraud provision can occur.<sup>135</sup> Thus, before any attempt to exercise United States jurisdiction in an action brought under Section 10(b) of the Securities Exchange Act of 1934 or Section 4(b) of the CEA, some conduct within the United States must have taken place. As the constitutionally designated regulator of interstate commerce,<sup>136</sup> the federal government and its statutes are, a fortiori,<sup>137</sup> properly employed to police

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<sup>131</sup> For a discussion of the effects test, see *supra* notes 72-81 and accompanying text.

<sup>132</sup> See David Lord Hacking, *supra* note 106, at 2.

<sup>133</sup> *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 9 (1972).

<sup>134</sup> See Grossfeld & Rogers, *A Shared Values Approach to Jurisdictional Conflicts in International Economic Law*, 32 INT'L & COMP. L.Q. 931 (1983); Toms, *The French Response to the Extraterritorial Application of U.S. Antitrust Laws*, 15 INT'L L.J. 585 (1981).

<sup>135</sup> See 15 U.S.C. § 78j (1976); 7 U.S.C. § 6(b) (1976).

<sup>136</sup> U.S. CONST. art. I, § 8, cl. 3.

<sup>137</sup> U.S. CONST. art. VI, cl. 2.

the use of the means of interstate commerce whether by United States or foreign citizens.<sup>138</sup> Rather than attempting to categorize different degrees of conduct within this country in order to satisfy the "conduct test" fashioned in *Leasco Data Processing Equipment Corporation v. Maxwell*,<sup>139</sup> Congress' constitutional mandate to regulate and to police the use of interstate commerce justifies what has been termed a "minimal conduct approach"<sup>140</sup> to extraterritorial jurisdiction over transnational securities and commodities fraud cases. The minimal conduct approach, simply put, would allow for the application of United States law to an allegation of transnational securities fraud where *any* use of interstate commerce was employed and not merely where foreign sponsored activity or conduct in the United States was "significant" or "important."<sup>141</sup>

In addition to a conduct-based rationale for the extraterritorial application of United States securities and commodities laws, several policy reasons argue for the proposition, that, in an era of international financial markets, the extension of United States jurisdiction to transnational claims of fraud protects not only United States investors but also foreign participants in United States markets.<sup>142</sup> Clearly, the primary purpose of Section 10(b) of the Securities Exchange Act of 1934 and Section 4(b) of the CEA is to protect domestic investors from becoming the objects of schemes to defraud perpetrated either in this country or from abroad.<sup>143</sup> However, in *IIT v. Vencap*,<sup>144</sup> the Second Circuit concluded: "We do not think Congress intended to allow the United States to be used as a base for manufacturing fraudulent security devices for export, even where these are peddled only to foreigners."<sup>145</sup> The Second Circuit's acknowledgement of the interests of foreign market participants in *Vencap* forcefully demonstrates the fallacy of claims by other nations that extraterritorial application of United States securities laws is intrusive, meddlesome, and overtly protectionist where fraudulent misrepresentations occur abroad and only market execution takes place in the United States. The extraterritorial application of United States securities laws is aimed equally at protecting the interests of domestic investors and at foreclosing the use of United States markets to those who would employ

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<sup>138</sup> See *supra* note 125.

<sup>139</sup> 468 F.2d 1326 (2d Cir. 1972).

<sup>140</sup> See Note, *Expanding the Jurisdictional Basis for Transnational Securities Fraud Cases: A Minimal Conduct Approach*, 6 FORDHAM INT'L L.J. 308 (1983).

<sup>141</sup> See *supra* notes 57-68 and accompanying text.

<sup>142</sup> See, e.g., Note, *supra* note 140.

<sup>143</sup> See *supra* note 119.

<sup>144</sup> 519 F.2d 1001 (2d Cir. 1975).

<sup>145</sup> *Id.* at 1017.

them in furtherance of schemes to defraud investors abroad.<sup>146</sup>

Deterrence of fraudulent market activity and, concurrently, the affirmative encouragement of lawful market conduct is the goal of the anti-fraud provisions of the Securities Exchange Act of 1934 and the CEA.<sup>147</sup> To the extent that an international claim must, by definition, have an impact upon the jurisdiction of another nation, the exercise of United States jurisdiction will appear intrusive. Nonetheless, the aim of such a judicial determination is by no means a desire to bring international commerce within the exclusive domain of United States tribunals. One need look no farther than the protestations of the securities industry<sup>148</sup> for evidence that the threatened application of United States anti-fraud statutes is a powerful deterrent to potential illicit conduct.<sup>149</sup> The Third Circuit in *SEC v. Kasser*<sup>150</sup> addressed the importance of deterrence as a rationale for extending the reach of United States securities laws to claims arising from international transactions:

From a policy perspective, and it should be recognized that this case in large measure calls for a policy decision, we believe that there are sound rationales for asserting jurisdiction. First, to deny such jurisdiction may embolden those who wish to defraud foreign securities purchasers or sellers to use the United States as a base of operations. By sustaining the decision of the district court as to the lack of jurisdiction, we would, in effect create a haven for such defrauders and manipulators. We are reluctant to conclude that Congress intended to allow the United States to become a "Barbary Coast," as it were, harboring international securities "pirates."<sup>151</sup>

As a final response to international criticism of United States securities regulatory policy, nations which insist that extraterritorial application of United States securities laws will result in the creation of formidable obstacles which will have an adverse impact upon efforts to raise capital in the United States,<sup>152</sup> fail to consider that, instead of discouraging investment abroad, the extraterritorial application of United

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<sup>146</sup> *Id.* See also *Psimenos*, 722 F.2d at 1041 ("... Congress did not want the U.S. to be used as a base for manufacturing fraudulent securities devices, irrespective of the nationality of the victim...").

<sup>147</sup> See *supra* note 119.

<sup>148</sup> See *supra* notes 110-33 and accompanying text.

<sup>149</sup> The degree to which the securities industry has fought the extension of United States anti-fraud statutes to extraterritorial transactions constitutes persuasive evidence that such statutes are a necessary and efficacious way to police international securities transactions executed in this country.

<sup>150</sup> 548 F.2d 109 (3d Cir.), *cert. denied*, 431 U.S. 938 (1977).

<sup>151</sup> *Id.* at 116.

<sup>152</sup> For a thorough discussion of the effects of extraterritorial application of United States anti-fraud statutes on foreign capital formation, see Bloomenthal, *Extraterritorial Application of United States Securities Laws—Recent Developments*, 2 Sec. & Fed. Corp. L. Rep. (Clark Boardman) 114 (1980).

States laws may actually facilitate foreign capital formation.<sup>153</sup> Unlike the exportation of United States antitrust policy,<sup>154</sup> it remains to be proven that application of United States securities laws pose a threat, where their application is deemed warranted, to the economies of any foreign nation. Moreover, insofar as foreign capital formation is often largely dependent upon offerings in the United States,<sup>155</sup> United States investors may well be more willing to invest in foreign securities with the knowledge that there will be a lesser risk of fraud where foreign broker-dealers are held accountable for their conduct under United States securities statutes. Thus, more likely than not, the strict enforcement and appropriate extraterritorial application of United States securities laws will encourage rather than impede the investment of United States capital in fledgling as well as established foreign enterprises.

One need not be extremely well-versed in the intricacies of securities law to realize how the exercise of United States jurisdiction over transnational securities fraud cases might be taken as an affront by foreign nations. Similarly, the perception of the securities industry that application of United States statutes to fraudulent conduct occurring predominantly outside the United States will discourage foreign participation in domestic markets is an understandable, albeit groundless, concern. Neither the complaints of our trading partners nor the cries of the financial community, however, should be permitted to interfere with the strict regulation, including extraterritorial United States jurisdiction, of securities transactions when the integrity of United States markets or the protection of United States investors are genuinely at stake.

The exercise of extraterritorial jurisdiction in securities and commodities fraud cases by the United States is aimed simply at protecting United States financial marketplaces and those conducting business there. The fact that United States markets are now formally linked with the markets of other nations unavoidably extends the legitimate sphere of United States regulatory policy, but, at the same time, the powerful deterrent force of United States law is brought to bear to discourage the perpetration of fraud through the use, no matter how limited, of United States securities and commodities markets and their affiliates.

## V. CONCLUSION

While the complexity of investment instruments and investment

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<sup>153</sup> See Thomas, *supra* note 109 and sources cited therein. See also figures cited in the Commerce Department's monthly *Survey of Current Business*, *supra* notes 99-104.

<sup>154</sup> See *supra* note 134.

<sup>155</sup> See *supra* note 152.

strategies has increased considerably over the past few years, world financial markets have become truly international in membership. The desire to manage more effectively the overnight trading risk involved in futures trading has given birth to the concept of the intercontinental trading link making possible the offset of market positions, and thus the limiting of risk, during hours when markets would ordinarily be closed. An unavoidable consequence of this increased internationalization of financial markets, however, has been the problem of how and by whom such ventures as international trading links will be regulated.

Case law involving United States securities and commodities statutes has gone to great lengths to devise the proper tests and criteria in an effort to limit extraterritorial application of United States jurisdiction to those cases in which fraudulent conduct initiated abroad and exported to this country, to *any* extent, poses a real danger to domestic interests. Neither hairsplitting semantic distinctions between degrees of "conduct" or "effect" or trading bloc rivalries aggravated as the result of the extraterritorial application of United States jurisdiction should be allowed to divert attention away from what is ultimately at stake—the strict regulation and smooth functioning of international as well as internationally-linked financial markets.

At present, United States courts will only apply domestic regulatory statutes to cases in which some aspect of fraudulent conduct or some step in furtherance of a scheme to defraud takes place in the United States. However, for better or worse, many of the world's most important and complex financial transactions occur in domestic securities markets or are facilitated by the means and instrumentalities of interstate commerce. The extraterritorial application of United States jurisdiction to transnational securities and commodities fraud cases, while concededly an increasingly frequent phenomenon, is primarily a reflection of United States prominence in the financial world, a prominence largely acquired due to the integrity of United States financial markets. The United States must continue to maintain the integrity of its financial markets, in part through a judicious policy of appropriate extraterritorial application of United States anti-fraud statutes for the sake of both domestic investors, investors abroad, as well as for the good of the world economy.

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