

SARBANES-OXLEY ACT OF 2002: ARE MULTI-NATIONAL CORPORATIONS UNDULY BURDENED?

“Sarbanes-Oxley is the most important piece of legislation in the securities area since the New Deal.”¹

- SEC Commissioner Harvey Goldschmid, 2004

I. INTRODUCTION

The Sarbanes Oxley Act (SOX) was signed into law on July 30, 2002.² SOX was enacted in an effort to “restore confidence to the US capital markets.”³ The frauds of Enron, WorldCom, and other companies prompted Congress to pass legislation to end corruption in American markets.⁴ President Bush, in his speech before signing SOX, stated Corporate America would not be held to a different ethical standard than the rest of the United States.⁵ Even though SOX was enacted to deter corruption in the United States, the impact of the legislation was global.⁶ “Relevant legal developments in the United States . . . never go unnoticed in foreign jurisdictions.”⁷

¹ Harvey Goldschmid, Comm’r, Sec. Exch. Comm’n, Address at Columbia Business School: The Sarbanes Oxley Act: Too Little, Too Far, or Just Enough? (September 17, 2004), *available at* <http://www0.gsb.columbia.edu/leadership/news?&global.now=09-01-2004&main.id=592069&main.ctrl=contentmgr.detail&main.view=news.detail>.

² Bonnie K. Levitt, *Sarbanes-Oxley Insider Trading Prohibitions Affect Insiders Outside the US*, 14 INT’L CO. & COM. LAW REV. 293, 293 (2003).

³ Tom O’Neill, Bertrand Cardi, & Simon Charbit, *Conflicts between French Law and Practice and the US Sarbanes-Oxley Act of 2002*, 31 INT’L BUS. LAW. 59, 59 (2003).

⁴ Larry E. Ribstein, *International Implications of Sarbanes-Oxley: Raising the Rent on U.S. Law 2* (Illinois Law and Economics Working Paper Series, Paper No. LE03-005, 2003), *available at* http://papers.ssrn.com/pape.tar?abstract_id=401660. [hereinafter *Raising the Rent*].

⁵ George W. Bush, President of the U.S., Address at the signing of the Sarbanes-Oxley Act of 2002 (July 30, 2002), *available at* <http://www.whitehouse.gov/news/releases/2002/07/20020730-1.html>.

⁶ Jonathan Shirley, Comment, *International Law and the Ramifications of the Sarbanes--Oxley Act of 2002*, 27 B.C. INT’L & COMP. L. REV. 501, 511 (2004).

⁷ Felix R Ehrat, *Sarbanes-Oxley – A View from Outside*, 31 INT’L BUS. LAW. 75 (2003).

SOX has implications for companies and corporations doing business in the United States and abroad. Firms listed on the New York Stock Exchange are subject to the regulation under United States securities laws.⁸ Approximately fifteen percent of firms listed on the New York Stock Exchange are domiciled outside of the United States.⁹ These companies include the Nokia Corporation domiciled in Finland,¹⁰ DaimlerChrysler Corporation domiciled in Germany,¹¹ and Siemens Corporation also domiciled in Germany.¹² This is a large group of firms controlled not only by United States securities laws, but also by regulations in their countries of domicile. Problems arise when the regulations under SOX and other United States securities regulations conflict with international corporate governance standards and regulations of individual countries.

This comment examines the conflicts between SOX and corporate governance regulations outside of the United States, specifically in the European Union (emphasizing France and Germany), International Corporate Governance Regulations, and regulations under the World Trade Organization. Section II provides an overview of SOX, the provisions effecting multinational companies, its' background, and the reasoning behind the provisions. Section III discusses the conflicts between the provisions of SOX and international corporate governance. Section IV discusses enforcement issues of both SOX and international corporate governance

⁸ *Raising the Rent*, *supra* note 4, at 2.

⁹ Jordan Siegel, *Can Foreign Firms Bond Themselves Effectively by Renting U.S. Securities Laws?*, J. OF FIN. ECON., Feb. 2004, at 2, 2, available at <http://www.afajof.org/pdfs/2003program/articles/siegel.pdf>. This is a chart of the volume of foreign stocks on the New York Stock Exchange. http://www.nysedata.com/factbook/viewer_edition.asp?mode=chart&key=16&category=6.

¹⁰ New York Stock Exchange: Listed Company Directory, <http://www.nyse.com/about/listed/6.html> (last visited Nov. 6, 2005).

¹¹ New York Stock Exchange: Listed Company Directory <http://www.nyse.com/about/listed/6.html?&ListedComp=All&start=21&startlist=1&item=2&next=clicked&firsttime=done&default=2> (last visited Nov. 6, 2005).

¹² New York Stock Exchange: Listed Company Directory, <http://www.nyse.com/about/listed/6.html?&ListedComp=All&start=41&startlist=1&item=3&next=clicked&firsttime=done&default=2> (last visited Nov. 6, 2005).

regulations, including the extraterritorial jurisdiction of the United States as a matter of law and international comity concerns. Section V discusses which form of governance has been more successful and the reasons for success. Section VI is the conclusion.

II. OVERVIEW OF SOX AND ITS PROVISIONS

A. Background of SOX

SOX was enacted in the wake of Enron, WorldCom, and other business scandals in the United States.¹³ Politicians feared the scandals would cripple American markets.¹⁴ The scandals had already resulted in billions of dollars of corporate losses and deeply harmed investor trust.¹⁵ Congress realized if they did not take swift action, the problem would spread throughout every sector of the economy.¹⁶ Congress felt most of the links in the chain, such as managerial controls for disclosure and between auditors and officers of a company, had failed and companies failed to deliver clean and honest information to investors.¹⁷

The Bush Administration was under immense pressure to push for a tough response of regulation after the Enron scandal.¹⁸ The explosion of the Enron scandal in the media led to over thirty “Enron-inspired” bills being contemplated on by Congress.¹⁹ By July 25, 2004, a final bill was passed by Congress and was signed into law by President Bush five days later.²⁰

¹³ Michael A. Perino, *American Corporate Reform Abroad: Sarbanes-Oxley and the Foreign Private Issuer*, 4 EUR. BUS. ORG. L. REV. 213 (2003), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=439501.

¹⁴ *Id.*

¹⁵ Information Guide to the Sarbanes Oxley Act of 2002, <http://www.sarbanes-oxley-101.com/sarbanes-oxley-faq.htm> (last visited Nov. 6, 2005) [hereinafter Information Guide].

¹⁶ Perino, *supra* note 13.

¹⁷ DAVID E. HARDESTY, PRACTICAL GUIDE TO CORPORATE GOVERNANCE AND ACCOUNTING: IMPLEMENTING THE REQUIREMENTS OF THE SARBANES-OXLEY ACT xvi (2005 ed.) [hereinafter PRACTICAL GUIDE].

¹⁸ Shirley, *supra* note 6, at 505.

¹⁹ *Id.*

²⁰ *Id.*

The scandals occurred because monitoring failed at several levels, including the monitoring of directors and at prominent accounting and law firms.²¹ SOX requires all publicly-traded companies, domestic and multinational companies, to comply with regulations set out in the Act.²² SOX regulations try to improve corporate governance and corporate accountability by requiring honesty in financial reporting.²³

B. Provisions of SOX

SOX includes provisions to “restore integrity to financial markets and confidence in corporate conducts, financial reports and related audit functions.”²⁴ It creates new rules to “protect auditor independence and address conflicts of interest faced by securities analysts.”²⁵ The provisions range from accounting procedures and enhanced disclosure to criminal sanctions for violating the regulations of SOX.²⁶ These provisions have the goal of trying to get honest and detailed information to investors, without the taint of corruption or deceit.

1. Title III: Corporate Responsibility²⁷

Sections 301 to 308 lay out the requirements for corporate responsibility under SOX.²⁸ There are four relevant provisions under Title III: (1) the establishment of audit committees of public companies;²⁹ (2) CEO and CFO certifications;³⁰ (3) insider trades during pension fund blackout periods;³¹ and (4) the rules of professional conduct for attorneys.³²

²¹ *Raising the Rent*, *supra* note 4, at 2.

²² Information Guide, *supra* note 15.

²³ Pankaj K. Jain & Zabihollah Rezaee, Professors, U. of Mem., 2003 Financial Management Association Meeting, Denver, Colorado: Have the Sarbanes Oxley Act of 2002 and CEO Certifications Made the Markets More Informed? (Oct. 8, 2003), *available at* http://207.36.165.114/Denver/Papers/sarbanes_spread.pdf.

²⁴ *Id.*

²⁵ William H. Donaldson, Chairman, Sec. Exchange Comm’n, Address at London School of Economics: U.S. Capital Markets in the Post-Sarbanes-Oxley World: Why Our Markets Should Matter to Foreign Issuers (Jan. 25, 2005).

²⁶ Ehrat, *supra* note 7, at 75

²⁷ Sarbanes--Oxley Act of 2002, Pub. L. No. 107--204, § 307, 116 Stat. 745 (2002) (codified as amended in 15 U.S.C.A. §§ 7201-7266 and scattered sections of 11,18,28, and 29 U.S.C.A. (West Supp. 2003), *available at* <http://news.findlaw.com/hdocs/docs/gwbush/sarbanesoxley072302.pdf> [hereinafter The Act].

²⁸ PRACTICAL GUIDE, *supra* note 17, at 301.

a. Section 301: Public Company Audit Committees³³

The audit committees of public companies must be made up of independent directors.³⁴

The requirements for the directors include taking charge of corporate audits and overseeing the auditors, resolving accounting disputes between auditors and management, and hearing and acting on complaints regarding accounting or internal control issues.³⁵ The members of the audit committee must be independent; this means that the members cannot receive any kind of compensation for advising or consulting from the issuer and must not be affiliated with the issuer.³⁶

The purpose of this provision is to ensure the independence of auditors from management.³⁷ Congress realized before the enactment of SOX that many problems were due to “close ties between audit committee members and management.”³⁸ The audit committee cannot owe their loyalty to the management of the company; it must be loyal to the company as a whole and the committee.³⁹

b. Section 302: Corporate Responsibility for Financial Reports⁴⁰

Chief Financial Officers (CFOs) and Chief Executive Officers (CEOs) are required to certify that the financial statements are truthful and contain no material misstatements.⁴¹ The statement shows the company has the required internal control over financial reporting and

²⁹ PRACTICAL GUIDE, *supra* note 17, at 301.

³⁰ *Id.* at 311.

³¹ *Id.* at 327.

³² *Id.* at 339.

³³ The Act, *supra* note 27, § 301.

³⁴ PRACTICAL GUIDE, *supra* note 17, at 301.

³⁵ *Id.*

³⁶ *Id.* at 305.

³⁷ *Id.* at 302.

³⁸ *Id.* at 301.

³⁹ *Id.* at 302.

⁴⁰ The Act, *supra* note 27, § 302.

⁴¹ PRACTICAL GUIDE, *supra* note 17, at 311.

disclosure procedures.⁴² Statements that must be certified under this section are forms 10-Q, 10-K, 20-F, and 40-F.⁴³

The 10-Q is a report filed quarterly to the Securities and Exchange Commission (SEC).⁴⁴ It includes an unaudited financial statement and shows the financial status of the firm.⁴⁵ The report must be filed for the first three fiscal quarters and is due within 45 days of the end of the quarter.⁴⁶ The 10-K provides a comprehensive outline of the firm's business.⁴⁷ The report must be filed within 90 days of the end of the fiscal year.⁴⁸ The 20-F is the form for foreign private issuers to register with the SEC under Section 12(b) or 12(g) of the Securities Exchange Act of 1934.⁴⁹ It is also the form used for annual and transition reports for firms under Sections 13 and 15(d) of the Securities Exchange Act of 1934.⁵⁰ The 40-F is a registration statement under Section 12 of the Securities Exchange Act of 1934 or an annual report under Section 13(a) or 15(d) of the Securities Exchange Act of 1934.⁵¹

Section 302 of SOX requires CEOs and CFOs to certify financial reports and requires officers to review and verify that the reports are honest and do not contain misleading or false statements.⁵² This section requires certification to cover "review of the report, its material accuracy, the fair presentation of financial information, disclosure controls, and internal

⁴² PRACTICAL GUIDE, *supra* note 17, at 311.

⁴³ *Id.* at 312.

⁴⁴ Definition of 10-Q, <http://www.accounting-career-opportunity.com/accounting-terms-and-definition.html> (last visited Nov. 6, 2005).

⁴⁵ *Id.*

⁴⁶ *Id.*

⁴⁷ Definition of 10-K, <http://www.accounting-career-opportunity.com/accounting-terms-and-definition.html> (last visited Nov. 6, 2005).

⁴⁸ *Id.*

⁴⁹ Security Lawyer's Deskbook, <http://www.law.uc.edu/CCL/34forms/form20-F.html> (last visited Nov. 6, 2005).

⁵⁰ *Id.*

⁵¹ *Id.*

⁵² PRACTICAL GUIDE, *supra* note 17, at 311.

accounting controls.”⁵³ CEOs and CFOs are held accountable for the financial statements and must sign the reviewed financial documents.⁵⁴

c. Section 306: Insider Trades During Pension Fund Blackout Periods⁵⁵

Corporate officers and directors are not allowed to trade in company stock during a “blackout period.”⁵⁶ A blackout period is a “period of at least three days during which at least half of the company’s U.S. individual account plan participants are not permitted to trade the company stock within their plans.”⁵⁷ Participants also receive at least 30 days notice prior to a blackout period.⁵⁸

This provision emerged directly from the Enron scandal, where it was alleged that “employees held Enron stock in their individual retirement account plans and were prevented from selling the stock on account of a ‘blackout’”, and during that time their stock lost value.⁵⁹ This provision only applies to issuers who maintain individual account plans.⁶⁰

d. Section 307: Rules of Professional Responsibility for Attorneys⁶¹

Attorneys are required to report evidence of securities violations and any other fraudulent act to a company’s chief counsel or the CEO.⁶² The attorney must take the evidence to the board of directors if appropriate action is not taken.⁶³ This process is known as “up-the-ladder

⁵³ GUY P. LANDER, WHAT IS SARBANES-OXLEY? 4 (2004).

⁵⁴ PRACTICAL GUIDE, *supra* note 17, at 311.

⁵⁵ The Act, *supra* note 27, § 306.

⁵⁶ PRACTICAL GUIDE, *supra* note 17, at 327.

⁵⁷ *Id.*

⁵⁸ *Id.*

⁵⁹ *Id.*

⁶⁰ *Id.* at 328.

⁶¹ The Act, *supra* note 27, § 307.

⁶² PRACTICAL GUIDE, *supra* note 17, at 339.

⁶³ *Id.*

reporting.”⁶⁴ The attorney has discretion to decide whether or not the company has appropriately responded to the report.⁶⁵

The purpose of this provision is to hold attorneys accountable to the same standards as officers of a company.⁶⁶ The attorney “owes his or her professional and ethical duties to the company as an organization, rather than to the company’s officers, directors, or employees.”⁶⁷ Congress felt that previous regulations on attorneys were ineffective and did not deter attorney wrongdoing.⁶⁸ This provision requires attorneys to report any material violation and be held accountable for not reporting violations.⁶⁹

There is also a provision in this section labeled the “noisy withdrawal” regulation.⁷⁰ This provision arises when the attorney does not receive a timely response to a report citing a material violation.⁷¹ The procedure differs for external attorneys working on a matter for a corporation and in-house attorneys working directly for the corporation. An external attorney must withdraw from representing the corporation and notify in writing that the withdrawal is based on professional considerations.⁷² An in-house attorney must stop working on the matter concerning the violation and notify the corporation in writing that there has not been an adequate response to their report.⁷³

2. Title IV: Enhanced Financial Disclosures⁷⁴

⁶⁴ PRACTICAL GUIDE, *supra* note 17, at 340.

⁶⁵ *Id.* at 340.

⁶⁶ *Id.* at 339.

⁶⁷ LANDER, *supra* note 53, at 91.

⁶⁸ PRACTICAL GUIDE, *supra* note 17, at 339.

⁶⁹ *Id.* at 340.

⁷⁰ *Id.* at 345.

⁷¹ *Id.*

⁷² *Id.*

⁷³ *Id.*

⁷⁴ The Act, *supra* note 27, § 400.

Sections 401 to 409 lay out the requirements for financial disclosures under SOX.⁷⁵

There are three relevant sections under Title IV: (1) the management assessment of internal controls;⁷⁶ (2) the code of ethics for senior financial officers;⁷⁷ and (3) real-time issuer disclosures.⁷⁸

a. Section 404: Management Assessment of Internal Controls⁷⁹

Annual reports of a public company are to be accompanied by a report on the effectiveness of internal control.⁸⁰ Auditors are required to attest to management's assessment of internal control.⁸¹ Management is responsible for ensuring that the internal control meets the requirements under SOX.⁸² These requirements include designing a system of internal control, supervised operation of the system, continuous monitoring of the system, and documentation of the internal controls implemented.⁸³ The independent auditor of a company must also report on the company's internal control over financial reporting.⁸⁴ If the auditors cannot express an overall opinion about the effectiveness of a company's internal control over financial reporting, the auditors must explain why.⁸⁵ The management assessment of internal controls and also the auditor's assessment must be included in the annual report.⁸⁶

The purpose of this provision is to assure investors that companies have an effective internal control system.⁸⁷ Before SOX, it was rare for companies to report on internal control.⁸⁸

⁷⁵ PRACTICAL GUIDE, *supra* note 17, at 401.

⁷⁶ *Id.* at 418.

⁷⁷ *Id.* at 427.

⁷⁸ *Id.* at 436.

⁷⁹ The Act, *supra* note 27, § 404.

⁸⁰ PRACTICAL GUIDE, *supra* note 17, at 418.

⁸¹ *Id.*

⁸² *Id.* at 421.

⁸³ *Id.* at 1603.

⁸⁴ *Id.* at 423.

⁸⁵ LANDER, *supra* note 53, at 19.

⁸⁶ Amey Stone, *Hardly Ready for Sarbanes-Oxley*, BUS. WK., Sept. 20, 2004.

⁸⁷ PRACTICAL GUIDE, *supra* note 17, at 419.

⁸⁸ *Id.*

This section holds management accountable for the internal control of a company and makes it public knowledge so investors know there is an internal control mechanism in place.⁸⁹ It also places a burden on the auditors of a company to report on the internal control procedures and their effectiveness.⁹⁰

b. Section 406: Code of Ethics for Senior Financial Officers⁹¹

Companies must disclose whether it has adopted a code of ethics for financial officers.⁹² For purposes of the provision, a code of ethics must be a written set of standards deterring violations and promoting honest conduct.⁹³ Companies must include the code of ethics in their annual report.⁹⁴

This provision shows investors whether a company has a written set of rules for financial officers.⁹⁵ A company may also have different codes of ethics for different types of employees.⁹⁶ The code may be part of a larger code addressing other issues and applying to additional persons.⁹⁷ If a company does not have a code of ethics for financial officers, the company must state the reasons why they have not adopted a code.⁹⁸ Also, if a company's code of ethics is defective, they may not affirm that it has the required code.⁹⁹ A company must also report any change to the code and keep it updated.¹⁰⁰

c. Section 409: Real-time Issuer Disclosures¹⁰¹

⁸⁹ PRACTICAL GUIDE, *supra* note 17, at 420.

⁹⁰ *Id.* at 423.

⁹¹ The Act, *supra* note 27, § 406.

⁹² PRACTICAL GUIDE, *supra* note 17, at 427.

⁹³ *Id.* at 428.

⁹⁴ *Id.*

⁹⁵ *Id.* at 427.

⁹⁶ LANDER, *supra* note 53, at 66.

⁹⁷ *Id.*

⁹⁸ PRACTICAL GUIDE, *supra* note 17, at 427.

⁹⁹ LANDER, *supra* note 53, at 65.

¹⁰⁰ PRACTICAL GUIDE, *supra* note 17, at 427.

¹⁰¹ The Act, *supra* note 27, § 409.

The SEC is “required to issue rules requiring ‘real-time’ disclosure of a number of key occurrences and transactions, which may be of importance to investors.”¹⁰² Issuers are required to disclose, in real-time, material changes and transactions.¹⁰³ Events prompting the disclosure requirements have to be reported within two business days.¹⁰⁴ The disclosure must also be in English, it cannot be submitted in any other language even if a corporation is domiciled outside of the United States.¹⁰⁵

The purpose of this provision is to disclose information of material changes of the financial condition of the company in a timely fashion.¹⁰⁶ This leads to a constant flow of current information. This provision is “necessary . . . for the protection of investors and in the public interest.”¹⁰⁷

3. Title VIII: Corporate and Criminal Fraud Accountability¹⁰⁸

Sections 801 to 807 lay out the punishment for violation of other provisions of SOX.¹⁰⁹ A relevant provision under Title VIII deals with protection for employees who provide evidence of fraud.¹¹⁰

a. Section 806: Protection for Employees of Publicly Traded Companies Who Provide Evidence of Fraud¹¹¹

This provision encourages “whistleblowing” by employees who report any violation of SOX.¹¹² It also prohibits companies from retaliating against employees who have reported

¹⁰² PRACTICAL GUIDE, *supra* note 17, at 436.

¹⁰³ *Id.* at 438.

¹⁰⁴ *Id.* at 436.

¹⁰⁵ *Id.*

¹⁰⁶ *Id.*

¹⁰⁷ *Id.*

¹⁰⁸ The Act, *supra* note 27, § 800.

¹⁰⁹ PRACTICAL GUIDE, *supra* note 17, at 801.

¹¹⁰ *Id.*

¹¹¹ The Act, *supra* note 27, § 806.

¹¹² PRACTICAL GUIDE, *supra* note 17, at 811.

securities law violations.¹¹³ This section can be implemented under Section 301, which requires audit committees to hear and act on reports of violations.¹¹⁴ The audit committee must have procedures to receive complaints regarding internal accounting measures and auditing issues.¹¹⁵ The committee must also set up a system to receive anonymous submissions by employees concerning question accounting and auditing procedures.¹¹⁶ All reports of violations are kept confidential.¹¹⁷

The purpose of this provision is to protect employees from being wrongfully terminated or disciplined for reporting violations.¹¹⁸ The employee has recourse if the company does take retaliatory action. The employee can file a complaint with the Department of Labor and if the matter is not resolved within 80 days, the employee may file a suit against the company in federal court.¹¹⁹

4. Title IX: White-Collar Crime Penalty Enhancements¹²⁰

Sections 901 to 906 describe the criminal sanctions imposed on individuals within corporations who ignore the regulations of SOX.¹²¹ A relevant provision under Title IX of SOX deals with corporate responsibility for financial reports.¹²²

a. Section 906: Corporate Responsibility for Financial Reports¹²³

CEOs and CFOs are required to certify financial statements to comply with SOX.¹²⁴ This provision requires “that financial statements comply with SEC reporting rules and that the

¹¹³ *Id.*

¹¹⁴ PRACTICAL GUIDE, *supra* note 17, at 811. Each audit committee must “establish procedures for: (1) the receipt, retention, and treatment of complaints received by the listed issuer . . . and (2) the confidential, anonymous submission by employees . . . of concerns regarding questionable accounting or auditing matters.” *Id.* at 308.

¹¹⁵ *Id.* at 308.

¹¹⁶ *Id.*

¹¹⁷ *Id.* at 811.

¹¹⁸ *Id.* at 812.

¹¹⁹ *Id.* at 811.

¹²⁰ The Act, *supra* note 27, § 900.

¹²¹ PRACTICAL GUIDE, *supra* note 17, at 901.

¹²² *Id.* at 904.

¹²³ The Act, *supra* note 27, § 906.

statements fairly present, in all material respects, the financial condition and results of operations of the company.”¹²⁵ This section states the penalties for not complying with section 906 and also Section 302.¹²⁶ The penalty imposed for certification of statements that officers know to be inaccurate includes imprisonment and monetary fines.¹²⁷

The certification must accompany periodic financial statements submitted to the SEC.¹²⁸ The periodic statements included under this section are forms 10-K, 10-Q, 20-F, and 40-F, which were defined earlier.¹²⁹ Section 906 also makes it easier for prosecutors to build a case against executives who issue false or misleading financial statements.¹³⁰ Section 906 is called the “criminal” certification for CEOs and CFOs.¹³¹

III. SOX: CONFLICTS WITH INTERNATIONAL LAW

SOX has implications for companies doing business in the United States and abroad.¹³² However, only companies listed on United States exchanges are affected.¹³³ “More than 1300 foreign corporations that list securities on U.S. exchanges are affected.”¹³⁴ Not all provisions of SOX conflict with international corporate governance, but there are many provisions that do.

A. Sections of SOX Conflicting with International Law

¹²⁴ PRACTICAL GUIDE, *supra* note 17, at 904.

¹²⁵ PRACTICAL GUIDE, *supra* note 17, at 904.

¹²⁶ *Id.*

¹²⁷ *Id.* A person who certifies a financial statement knowing that the report accompanying the financial statement does not comply with the regulations under this provision will be fined no more than 1 million dollars and imprisoned for not more than 10 years, or both. *Id.* at 905. A person who willfully certifies a financial statement knowing the report does not comply with the requirements under this provision will be fined no more than 5 million dollars or imprisoned for not more than 20 years, or both. *Id.* at 905.

¹²⁸ LANDER, *supra* note 53, at 8.

¹²⁹ *Id.*

¹³⁰ PRACTICAL GUIDE, *supra* note 17, at 904.

¹³¹ LANDER, *supra* note 53, at 8.

¹³² Shirley, *supra* note 6, at 511.

¹³³ *Id.*

¹³⁴ *Id.*

Section 301 of SOX deals with the formation of public company audit committees and who comprises them.¹³⁵ This provision makes it difficult for foreign companies, most of who are controlled by few shareholders.¹³⁶ The audit committee must be staffed by completely independent members.¹³⁷

This requirement of independent members on the audit committee raises problems for many companies. For companies who are controlled by a few large shareholders, SOX excludes major shareholders who may insist on more of a voice in the audit committee.¹³⁸ In a foreign company, one member may represent majority shareholders as an observer.¹³⁹

The formation of an audit committee may also lead to unnecessary expenses for firms with only one or a few controlling shareholders.¹⁴⁰ In this type of firm, the main problem is “controlling shareholders’ oppression of minority shareholders rather than managerial agency costs.”¹⁴¹ The independent audit committee is valuable in helping shareholders judge management by ensuring quality auditing of the firm.¹⁴² Differences in the quality of auditing are likely to be ineffective against shareholder opportunism.¹⁴³ These additional decision-making costs are likely to outweigh the benefits in multinational firms.¹⁴⁴ The costs are based on the increased amount of time it takes to file the relevant forms and also firms who accrue additional outside professional costs.¹⁴⁵

¹³⁵ PRACTICAL GUIDE, *supra* note 17, at 301.

¹³⁶ *Raising the Rent*, *supra* note 4, at 28.

¹³⁷ *Id.*

¹³⁸ *Id.* at 9.

¹³⁹ *Id.*

¹⁴⁰ *Id.* at 10.

¹⁴¹ *Id.* at 10.

¹⁴² *Raising the Rent*, *supra* note 4, at 10.

¹⁴³ *Id.* at 10.

¹⁴⁴ *Id.* at 10.

¹⁴⁵ Estelle M. Sohne, *The Impact of Post-Enron Information Disclosure Requirements Imposed Under U.S. Law on Foreign Investors*, 42 COLUM. J. TRANSNAT’L L. 217, 230 (2003).

Section 301 can directly conflict with laws of many countries, especially those countries who have a civil law system.¹⁴⁶ Many countries with civil law systems, including France and Germany, require “two-tier” boards.¹⁴⁷ The “upper” board (supervisory board) must be at least half comprised of labor managers and the “lower” board (managing board) is typically comprised of insider executives.¹⁴⁸ The requirement also creates conflicts with the status of internal and external auditors.¹⁴⁹ In Italy, Japan, and Brazil, the local laws provide “for a statutory board of auditors that must be independent of the board of directors itself (thus precluding an audit committee comprised of ‘independent directors’).”¹⁵⁰ French companies are regulated by “two independent institutes, the *Ordre des Experts-Comptables* (National Institute for Chartered Accountants) and the *Compagnie Nationale des Commissaires aux Comptes* (National Institute for Statutory Auditors).”¹⁵¹ French companies wonder why they have to abide by the regulations of SOX and also regulations under French oversight boards.¹⁵² It is standard practice in most European countries for shareholders to directly appoint outside auditors, not by a special committee of independent directors.¹⁵³

Civil law corporations have generally resisted giving the supervisory board important substantive responsibilities, because employee representatives serve on the board.¹⁵⁴ Under SOX, labor representatives would be given great responsibility, because “the audit committee

¹⁴⁶ Kenji Taneda, *Survey: Sarbanes-Oxley, Foreign Issuers and United States Securities Regulation*, 2003 COLUM. BUS. L. REV. 715, 739 (2003).

¹⁴⁷ *Id.* at 739.

¹⁴⁸ *Id.*

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ John Paul Lucci, *Enron – The Bankruptcy Heard Around the World and the International Ricochet of Sarbanes-Oxley*, 67 ALB. L. REV. 211, 240 (2003).

¹⁵² *Id.* at 240.

¹⁵³ Taneda, *supra* note 146, at 739.

¹⁵⁴ Minodora D. Vancea, *Exporting U.S. Corporate Governance Standards through the Sarbanes-Oxley Act: Unilateralism or Cooperation?*, 53 DUKE L. J. 833 (2001), available at <http://www.law.duke.edu/journals/dlj/articles/dlj53p833.htm>.

must be staffed with members of the supervisory committee, including labor representatives.”¹⁵⁵

The conflict between SOX and a civil system of government also makes it impossible for companies in those countries to “comply with both the codetermination requirement imposed by their country of incorporation and the independence requirement imposed by the Sarbanes-Oxley Act.”¹⁵⁶ Most members of the supervisory board, required under codetermination, are not considered independent under United States law.¹⁵⁷ The SEC does have an exemption for this circumstance, but foreign companies are uneasy about increasing labor representatives’ bargaining power.¹⁵⁸

Section 302 of SOX ensures corporate responsibility by requiring CEOs and CFOs to certify financial statements published by a company.¹⁵⁹ This provision has caused immediate concern, especially in European companies.¹⁶⁰ There are no corresponding requirements in English or Swiss law.¹⁶¹ In French law, it is only the CEO who certifies financial statements and not the CFO.¹⁶² In Germany, corporations have the governance structure of two tiers consisting of a management board, Vorstand, and a supervisory board, Aufsichstrat.¹⁶³ The executive with responsibilities most analogous to the CEO of an American company is a member of the

¹⁵⁵ Vancea, *supra* note 154, at 841.

¹⁵⁶ *Id.*

¹⁵⁷ 17 C.F.R. § 240.10A-3(b)(1), *available at*

http://a257.g.akamaitech.net/7/257/2422/12feb20041500/edocket.access.gpo.gov/cfr_2004/aprqrtr/pdf/17cfr240.10A-3.pdf. “Each member of the audit committee must be a member of the board of directors of the listed issuer.” *Id.*

“An affiliate of the company is not independent for audit committee purposes.” Vancea, *supra* note 154, n.47. “An affiliate is defined as someone that ‘controls, or is controlled by, or is under common control with’ the company.” *Id.*

¹⁵⁸ Vancea, *supra* note 154, at 842. The exemption is that foreign employee representatives on the supervisory board are allowed to be part of the audit committee, even though they are not independent of the company’s executives. *Id.*

¹⁵⁹ PRACTICAL GUIDE, *supra* note 17, at 311.

¹⁶⁰ Mark Walsh & Thomas Thesing, *Extraterritorial Application of US Corporate Governance Standards in Europe*, 14 INT’L CO. & COM. L. REV. 165, 165 (2003).

¹⁶¹ *Id.* at 165.

¹⁶² Tom O’Neill, Bertrand Cardi, & Simon Charbit, *Conflicts between French Law and Practice and the US Sarbanes-Oxley Act of 2002*, 31 INT’L BUS. LAW. 59, 59 (2003).

¹⁶³ Letter from Cleary, Gottlieb, Steen, & Hamilton Law Firm, to Jonathan G. Katz, Secretary, Sec. Exch., Comm’n (August 19, 2002) (on file with the Sec. Exch. Comm’n), *available at* <http://www.sec.gov/rules/proposed/s72102/cleary1.htm>.

management board.¹⁶⁴ There is also not a member of the management board who all other employees and executives report to and are subordinate to.¹⁶⁵ The members of the management board represent the company equally.¹⁶⁶

The requirement of CEO and CFO certification creates problems with firms operating outside of the United States, primarily because the process of certification can be time consuming.¹⁶⁷ Executives of many foreign issuers are greatly disadvantaged, because they are not accustomed to United States disclosure standards and practices.¹⁶⁸ An example of the disadvantage can be seen in the “materially accurate” standard for certification of financial statements under section 302.¹⁶⁹ Materiality is a concept central to United States securities laws, but foreign firms are unsure of the standard and if it has been met.¹⁷⁰ In countries of the European Union (EU), the term “price sensitive” is used, but this is only a similar standard, not an exact one.¹⁷¹ The SEC has made an exception for foreign firms so they only have to make this certification once annually.¹⁷² This provision is not burdensome for sophisticated foreign firms, but for all others it can be very burdensome.¹⁷³

Section 306 regulates insider trades during pension fund blackout periods.¹⁷⁴ “When blackouts affect a significant percentage of US participants in certain retirement plans, than all

¹⁶⁴ Letter from Cleary, Gottlieb, Steen, & Hamilton Law Firm to Jonathan G. Katz, *supra* note 163.

¹⁶⁵ *Id.*

¹⁶⁶ *Id.*

¹⁶⁷ Michael P. Kelley, *The Impact of Sarbanes-Oxley on Foreign Private Issuers, Private Equity Funds and Their Counsel*, VA. L., April 2003, at 24, 25, available at <http://www.vsb.org/publications/valawyer/apr03/kelley.pdf>.

¹⁶⁸ Tod Ackerly, *The Global Impact of U.S. Corporate Governance Initiatives*, COVINGTON & BURLING, Oct. 2002, available at <http://www.cov.com/publications/download/oid43940/314.pdf>.

¹⁶⁹ Ackerly, *supra* note 168. See 15 U.S.C.A § 78a; 17 C.F.R. Section 240.18a (West, Westlaw through Sept. 2005 amendments).

¹⁷⁰ Ackerly, *supra* note 168.

¹⁷¹ Ackerly, *supra* note 168. See Council Directive 98/34, art. 21.7.98, 1998 O.J. (L 204) (EC), available at http://europa.eu.int/comm/enterprise/tris/98_34_ec/index_en.pdf.

¹⁷² Ackerly, *supra* note 168.

¹⁷³ Kelley, *supra* note 167, at 25.

¹⁷⁴ PRACTICAL GUIDE, *supra* note 17, at 327.

trading by insiders, including insiders of the non-US issuer, is prohibited.”¹⁷⁵ This provision specifically applies to multinational corporations as well as domestic corporations. Foreign private issuers, for the purposes of this section, are defined as any foreign private issuer other than a foreign government and having more than fifty per cent of the issuer’s outstanding voting securities directly or indirectly held by residents in the United States.¹⁷⁶ The test applied to a foreign issuer is more stringent than the test applied to domestic corporations.¹⁷⁷

The test applied to corporations under this provision is the fifty per cent test.¹⁷⁸ This test is applied by comparing “the number of affected participants and beneficiaries located within the United States and its territories who will be restricted with the total number of participants and beneficiaries in all of the issuer’s relevant US individual account plans.”¹⁷⁹ Foreign corporations are also subjected to an additional test. The additional test is a calculation made to confirm either that at least fifteen per cent of the beneficiaries and participants in the corporation’s relevant worldwide individual account plans are affected by the blackout and more than 50,000 United States plan participants are affected.¹⁸⁰ Also, for the purpose of foreign corporations, the definition of a “director” is limited to directors who are also management employees.¹⁸¹

Section 307 requires attorneys to report any security violations to the company, so that the situation may be resolved.¹⁸² This provision affects attorneys practicing in the United States, but also applies to any attorney outside the United States working for multinational firms falling under SOX regulations, unless the attorney falls under any of the exceptions listed in the

¹⁷⁵ Levitt, *supra* note 2, at 293.

¹⁷⁶ *Id.* at 294.

¹⁷⁷ *Id.* at 295.

¹⁷⁸ *Id.*

¹⁷⁹ *Id.*

¹⁸⁰ *Id.*

¹⁸¹ Levitt, *supra* note 2, at 295.

¹⁸² PRACTICAL GUIDE, *supra* note 17, at 339.

section.¹⁸³ The SEC, after receiving many complaints from multinational firms, included a definition for “non-appearing foreign attorney” which excludes most lawyers who do not practice in the United States.¹⁸⁴ Non-appearing foreign attorneys are attorneys who are admitted to practice law outside of the United States, do not hold themselves out as giving advice on or practicing American law, and conduct activities that are incidental to a foreign law practice or in consultation with United States counsel.¹⁸⁵ The rule, however, does not apply when foreign attorneys are rendering their advice when consulting with counsel practicing in the United States.¹⁸⁶

The provisions for regulating attorneys under SOX may conflict with international rules and rules of individual countries.¹⁸⁷ In Germany, secrecy is mandated not only by the professional rules but also by the penal code.¹⁸⁸ Another problem faced by attorneys of multinational corporations is that attorneys that practice law outside of the United States may be unfamiliar with violations of United States securities laws.¹⁸⁹ How can the SEC expect foreign attorneys to report material violations of United States securities laws if they lack expertise in that area of law?¹⁹⁰ Foreign firms also argue the “noisy withdrawal” provision may constitute a breach of attorney-client privilege.¹⁹¹ The SEC does try to alleviate some of the concerns of multinational corporations and foreign issuers by excluding most foreign attorneys, not licensed

¹⁸³ PRACTICAL GUIDE, *supra* note 17, at 340.

¹⁸⁴ Walsh & Thesing, *supra* note 160, at 170.

¹⁸⁵ Robert D. Strahota, Assistant Dir., Off. of Int’l Aff., Sec. Exch. Comm’n, Address at the Fourth South Eastern Europe Corporate Governance Roundtable: Recent Governance Developments in the United States (March 7, 2003), available at <http://www.oecd.org/dataoecd/46/54/2506071.ppt>.

¹⁸⁶ Walsh & Thesing, *supra* note 160, at 170.

¹⁸⁷ Detlev F. Vagts, *Extraterritoriality and the Corporate Governance Law*, 97 AM. J. INT’L L. 289 (2003).

¹⁸⁸ *Id.* at 293.

¹⁸⁹ Ethiopos Tafara, Acting Dir., Off. of Int’l Aff., Sec. Exch. Comm’n., Address before the American Chamber of Commerce in Luxembourg: Addressing International Concerns under the Sarbanes-Oxley Act (June 10, 2003), available at <http://www.sec.gov/news/speech/spch061003et.htm>.

¹⁹⁰ *Id.*

¹⁹¹ *Id.*

to practice law in the United States, from its coverage.¹⁹² “As a general matter, only foreign attorneys who provide advice regarding US securities law may still be subject to the rule.”¹⁹³

Section 404 regulates management’s assessment of internal controls.¹⁹⁴ SOX makes no distinction between corporations that are completely domestic and multinational corporations doing business in the United States and abroad.¹⁹⁵ There is a later compliance date for multinational corporations, but that is the only dissimilarity in the rule.¹⁹⁶ Many executives of multinational firms are unhappy with Section 404 of SOX. According to a survey conducted by PricewaterhouseCoopers in June of 2003, only thirty percent of executives of multinational corporations had a favorable opinion of the provision.¹⁹⁷

This provision has many implications for multinational corporations. Before SOX, management was not required to have extensive internal control expertise.¹⁹⁸ The business environments in certain regions are less focused on controls; examples include Asia, Latin America, and Europe.¹⁹⁹ This lack of expertise and focus leads to an increase in the amount of work needed to comply with Section 404 of SOX.²⁰⁰

Another problem for multinational corporations is the form of the organization. Multinational corporations have a “decentralized organizational model.”²⁰¹ This type of corporation may only receive financial statements from their subsidiaries once or twice a year

¹⁹² Tafara, *supra* note 189.

¹⁹³ *Id.*

¹⁹⁴ PRACTICAL GUIDE, *supra* note 17, at 418.

¹⁹⁵ SEC. EXCH. COMM’N, FINAL RULE: MANAGEMENT’S REPORTS ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND CERTIFICATION OF DISCLOSURE IN EXCHANGE ACT PERIODIC REPORTS (2003).

¹⁹⁶ *Id.*

¹⁹⁷ WARREN GORHAM & LAMONT, HOW MULTINATIONAL COMPANIES ARE RESPONDING TO THE SARBANES-OXLEY ACT (2003).

¹⁹⁸ DELOITTE & TOUCHE LLP, SARBANES-OXLEY SECTION 404: COMPLIANCE CHALLENGES FOR FOREIGN PRIVATE ISSUERS 5, *available at* <http://www.iasplus.com/dttpubs/0502soxfpi.pdf>.

¹⁹⁹ *Id.* at 5.

²⁰⁰ *Id.*

²⁰¹ *Id.* at 4. Multinational corporations usually have subsidiaries in different countries. *Id.*

making it very difficult for these corporations to report to the SEC in a timely fashion.²⁰² There are also language barriers to consider when having to report to the SEC.²⁰³ Many corporations have found that the English language is not always an effective medium of communication.²⁰⁴

SOX also requires corporations to use Generally Accepted Accounting Principles (GAAP).²⁰⁵ Section 108 of SOX requires corporations to use GAAP standards when preparing financial statements.²⁰⁶ Traditionally, multinational firms used United States GAAP specialists to conform financial statements to comply with SOX regulations.²⁰⁷ Section 404 requires reports filed by companies under the provisions of SOX must conform to GAAP standards.²⁰⁸ Corporations are required to demonstrate that they have the appropriate experience ; they cannot rely on external sources to “fix” financial statements to conform to GAAP standards.²⁰⁹ “The independent auditor’s independence is impaired if they are considered to be a part of the company’s system internal control.”²¹⁰

This provision can be especially burdensome for foreign issuers and multinational corporations whose principal place of business is outside of the United States.²¹¹ In many jurisdictions outside of the United States, there are a limited amount of audit partners that possess the requisite knowledge of GAAP standards.²¹² In addition, most large multinational

²⁰² DELOITTE & TOUCHE, *supra* note 198, at 4.

²⁰³ *Id.* at 5.

²⁰⁴ *Id.*

²⁰⁵ *Id.* at 3. GAAP are the common set of “accounting principles, standards and procedures that companies use to compile their financial statements.” Generally Accepted Accounting Principles, <http://www.investopedia.com/terms/g/gaap.asp> (last visited Oct. 7, 2005).

²⁰⁶ PRACTICAL GUIDE, *supra* note 17, at 132.

²⁰⁷ DELOITTE & TOUCHE, *supra* note 198, at 3.

²⁰⁸ *Id.*

²⁰⁹ *Id.*

²¹⁰ *Id.* at 5.

²¹¹ Mélanie Lambelet, *The Extraterritorial Effects of the Sarbanes-Oxley Act of 2002*, MÉMOIRE MBL, Oct. 2003, at 28, available at http://www.unige.ch/droit/mbi/upload/pdf/MEMOIRE_Melanie_Lambelet.pdf.

²¹² Letter from Deloitte and Touche LLP to Jonathan Katz, Secretary, SEC (Jan. 10, 2003) (on file with the SEC), available at <http://www.sec.gov/rules/proposed/s74902/deloitte1.htm>.

corporations require “line” partners to complete their audits.²¹³ Developing “line” partners, who can maintain the level of experience needed by the corporation, is “costly, difficult, and time consuming.”²¹⁴ Audit firms are also severely limited in their ability to fill critical partner roles for these clients.²¹⁵ This could decrease the quality of work done by these firms and defeat the purpose for implementing this provision.²¹⁶

Section 406 requires corporations to adopt a code of ethics or to state why they have not adopted a code of ethics.²¹⁷ This provision applies to domestic firms and foreign private issuers.²¹⁸ The distinction between domestic firms and foreign private issuers under this section is that foreign private issuers do not have to provide a current report of a change in the issuer’s code of ethics.²¹⁹ A foreign private issuer only has to disclose changes once a year in its annual report.²²⁰

The Organization for Economic Co-Operation and Development (OECD) has provisions for a code of ethics to build public trust.²²¹ It is not mandated that corporations adopt a code of ethics, but the code will aid the process of corporate governance and encourage the reporting of

²¹³ *Id.*

²¹⁴ *Id.*

²¹⁵ *Id.*

²¹⁶ *Id.*

²¹⁷ PRACTICAL GUIDE, *supra* note 17, at 427.

²¹⁸ *Id.*

²¹⁹ Holme Roberts & Owen, *Final Rules: Code of Ethics*, HRO ALERT, Feb. 7, 2003, 1, 2, available at <http://www.hro.com/pubs/FRethics.pdf>.

²²⁰ *Id.*

²²¹ OECD, *Principles of Corporate Governance* (2004), available at <http://www.oecd.org/dataoecd/47/50/4347646.pdf>. The OECD groups:

30 member countries sharing a commitment to democratic government and the market economy. With active relationships with some 70 other countries, NGOs and civil society, it has a global reach. Best known for its publications and its statistics, its work covers economic and social issues from macroeconomics, to trade, education, development and science and innovation.

OECD, http://www.oecd.org/about/0,2337,en_2649_201185_1_1_1_1_1,00.html.

unethical behavior.²²² Almost all of the countries in the OECD also use training programs to raise awareness of ethical issues.²²³

Section 409 requires “real-time” disclosure of a number of key occurrences and transactions, which may be of importance to investors.²²⁴ This presents a complication for foreign issuers and multinational corporations.²²⁵ Time zone differences could affect the disclosure by corporations headquartered outside of the United States.²²⁶ The requirement that all disclosed documents must be in English presents a unique problem for foreign issuers whose first language is not English.²²⁷ This provision could lead to increased costs for document translation and other factors arising from the language barrier.²²⁸

Section 806 prohibits employers from taking adverse action against an employee when they take “lawful actions to disclose information or otherwise assist criminal investigators, federal regulators, Congress, supervisors . . . or parties in a judicial proceeding in detecting and stopping fraud.”²²⁹ There are many implications for multinational corporations under this section. The differences of corporate culture in America and other countries can lead to conflicts

²²² OECD, *Principles of Corporate Governance* (2004), available at <http://www.oecd.org/dataoecd/47/50/4347646.pdf>.

²²³ OECD Public Management Policy Brief, *Building Public Trust: Ethics Measures in OECD Countries*, Sept. 2007, available at www.oecd.org/dataoecd/60/43/1899427.pdf. The OECD is comprised of the following countries:

Republic of Austria, the Kingdom of Belgium, Canada, the Kingdom of Denmark, the French Republic, the Federal Republic of Germany, the Kingdom of Greece, the Republic of Iceland, Ireland, the Italian Republic, the Grand Duchy of Luxembourg, the Kingdom of the Netherlands, the Kingdom of Norway, the Portuguese Republic, Spain, the Kingdom of Sweden, the Swiss Confederation, the Turkish Republic, the United Kingdom of Great Britain and Northern Ireland, and the United States of America.

Convention on the Organisation for Economic Co-operation and Development, Dec. 14, 1960, available at http://www.oecd.org/document/7/0,2340,en_2649_201185_1915847_1_1_1_1,00.html.

²²⁴ PRACTICAL GUIDE, *supra* note 17, at 436.

²²⁵ Kelley, *supra* note 167, at 25.

²²⁶ *Id.*

²²⁷ *Id.*

²²⁸ *Id.*

²²⁹ PRACTICAL GUIDE, *supra* note 17, at 811.

in reporting misconduct.²³⁰ There are many countries where whistleblowing is seen as a return to the government intruding on the business practices of corporations.²³¹ In countries such as Italy and France, it sparks memories of experiences with collaborators during World War II.²³² Even with this section of SOX, many employees outside of the United States will be hesitant to report violations.²³³

The whistleblowing provision of SOX conflicts with the EU Data Protection Law.²³⁴ In complying with SOX, many corporations have established telephone hotlines or even a complaint system where employees can make anonymous complaints on the internet.²³⁵ The submissions may contain information about fellow employees and management.²³⁶ The EU data protection laws are very strict in the circumstances for the collection and disclosure of personal information.²³⁷

Article 26, Section 2 of the 1995 European Parliament Directive on the protection of individuals with regard to the processing of data, states:

Without prejudice to paragraph 1, a Member State may authorize a transfer or a set of transfers of personal data to a third country which does not ensure an adequate level of protection within the meaning of Article 25 (2), where the controller adduces adequate safeguards with respect to the protection of the privacy and fundamental rights and freedoms of individuals and as regards the exercise of the corresponding rights; such safeguards may in particular result from appropriate contractual clauses.²³⁸

²³⁰ Curtis C. Verschoor, *Is This the Age of Whistleblowers?*, STRATEGIC FIN., Jan. 2005, at 17, 18, available at <http://www.imanet.org/ima/docs/2900/2849.pdf>.

²³¹ *Id.* at 18.

²³² *Id.*

²³³ *Id.*

²³⁴ Hunton & Williams, *Conflict between Sarbanes-Oxley Whistleblower Provisions and EU Data Protection Law*, CLIENT ALERT, June 2005, at 1, 1.

²³⁵ *Id.*

²³⁶ *Id.*

²³⁷ *Id.*

²³⁸ Council Directive 1995/46, 1995 O.J. (L 281) 46 (EC), available at http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexapi!prod!CELEXnumdoc&lg=EN&numdoc=31995L0046&model=guichett.

This article lays out the protection for individuals in the EU and the restrictions of processing information and sending it to non-EU countries.²³⁹ The directive also requires that “the processing of personal information must not adversely affect the personal freedom of individuals, and imposes consent and disclosure requirements.”²⁴⁰

The SOX whistleblowing provision conflicts with laws outside of the United States and these conflicts can be seen in a German labor court decision and a decision by the French National Commission for Data Protection and the Liberties.²⁴¹ The French decision was based on the French data protection law.²⁴² The decision prohibited two companies, McDonald’s and CEAC Exide Technology, from setting up anonymous reporting systems.²⁴³ The reporting systems, “hotlines”, were deemed to be illegal in France.²⁴⁴ The Commission Nationale de L’informatique et des Libertes (CNIL) found there to be a lack of transparency due to the fact a whistleblower’s allegations against another employee may not be accessible to the target of the allegations.²⁴⁵ The commission also found the hotlines to be a breach of ethics and unfair to employees accused, because they would not have the means to defend themselves or oppose proceedings which may involve criminal sanctions.²⁴⁶ This result creates a legal bind for companies: how can you implement SOX when it conflicts with local laws of countries where

²³⁹ Hunton & Williams, *supra* note 234, at 2.

²⁴⁰ *Id.*

²⁴¹ Mark E. Schreiber & Jeffrey M. Held, *Anonymous Sarbanes Oxley Hotlines in the E.U.: Practical Compliance Guidance for Global Companies*, WORLD DATA PROTECTION REPORT, Aug. 2005, available at <http://www.theworldlawgroup.com/db30/cgi-bin/pubs/SOX%20Hotlines.doc>. The English translation of the French case may be found here. www.theworldgroup.com/newsletter/details.asp?ID=1246367122005. The English translation for the German case may be found at this website. www.theworldgroup.com/newsletter/details.asp?ID=745557282005.

²⁴² Commission Nationale de L’informatique et des Libertes, Act n°78-17 of 6 January 1978 on Data Processing, Data Files and Individual Liberties, available at <http://www.cnil.fr/fileadmin/documents/uk/78-17VA.pdf>.

²⁴³ Schreiber & Held, *supra* note 241.

²⁴⁴ *Id.*

²⁴⁵ *Id.*

²⁴⁶ *Id.*

business is being done?²⁴⁷ Christopher Kuner, an attorney with the Hunton & Williams law firm based in Brussels, made this conflict clear when he stated companies are being told “I either have to chop off my left hand or my right hand.”²⁴⁸

The German case was a decision handed down by the Fifth Division of the Wuppertal Labor Court on June 15, 2005.²⁴⁹ The court held Wal-Mart had to discontinue use of an employee complaint hotline for German employees until an agreement could be reached.²⁵⁰ The court also held provisions of the code of conduct implemented by Wal-Mart were invalid under German law.²⁵¹ The court found Wal-Mart did not request consent of the works council of Wal-Mart.²⁵² The court also founded their decision on German data protection laws.²⁵³ German data protection law “does not recognise an intra-group privilege for the transfer of data.”²⁵⁴ “Where the data is ultimately transferred to the United States, either the EC Commission standard contractual clauses have to be implemented or the U.S. company has to certify according to the Safe Harbor regulations.”²⁵⁵

²⁴⁷ David Reilly & Sarah Nassauer, *Tip-line bind: Follow the law in U.S. or EU?*, WALL ST. J., Sept. 6, 2005, available at <http://www.post-gazette.com/pg/05249/566468.stm>.

²⁴⁸ *Id.*

²⁴⁹ Schreiber & Held, *supra* note 241.

²⁵⁰ *Id.*

²⁵¹ *Id.*

²⁵² *Id.* This finding was made under a German labor law titled the Works Council Constitution Act. *Id.* The Act stipulates “works councils must be established in all companies that have five or more regular employees.” *Id.* The function of the works council under this law is “to protect the ‘collective labor rights’ of the employees of the company.” *Id.* The Works Council Directive created a works council for Wal-Mart in the European Union. 2002 O.J. (L 80) 29. The purpose of the Works Council Directive is “to establish a general framework setting out minimum requirements for the right to information and consultation of employees in undertakings or establishments within the Community.” 2002 O.J. (L 80) 29, 31.

²⁵³ Schreiber & Held, *supra* note 241.

²⁵⁴ *Id.*

²⁵⁵ *Id.* Use of the Contractual Clauses “should be considered whenever there is an intention to transfer personal data from within the EC to a country outside the European Economic Area that has not been recognized as providing adequate protection to personal data.” Goodwin Procter, *European Commission Approves Standard Contractual Clauses for Personal Data Transfers*, IP / TECH ADVISOR, July 2001, available at http://www.goodwinprocter.com/publications/IPA_personaldatatransfers_8_01.pdf. “Certifying to the safe harbor will assure that EU organizations know that your company provides ‘adequate’ privacy protection, as defined by the Directive.” U.S. Dept. of Com., Safe Harbor Overview, http://www.export.gov/safeharbor/sh_overview.html (last visited Nov. 6, 2005).

Section 906 imposes criminal sanctions on CEOs and CFOs who file misleading or false financial statements.²⁵⁶ This provision seems to conflict or overlap with regulations imposed by the International Organization for Standardization (ISO).²⁵⁷ Under the ISO provisions, dishonest reports and fraudulent quality systems are criminalized.²⁵⁸ With this level of regulation, it might be viewed as creating too much of a burden of suspicion on top management and seems to put a magnifying glass to companies who are registered under the ISO and are also subject to SOX regulations.²⁵⁹

IV. ENFORCEMENT ISSUES OF SOX

SOX affects all companies listed on any stock exchange in the United States.²⁶⁰ The Act directly affects “management, audit committees, public company auditors, attorneys, and brokerage firms.”²⁶¹ SOX affects companies operating domestically in the United States and also multinational companies, including foreign companies cross-listing on the United States stock exchanges.²⁶² Harvey L. Pitt, Chairman of the SEC, has spoken on the issue of the extraterritoriality.²⁶³ He stated ““We are aware of the fact that [many of the Act’s] requirements . . . can conflict with internal corporate structures and legal requirements in home

²⁵⁶ PRACTICAL GUIDE, *supra* note 17, at 904.

²⁵⁷ William A. Stimson, *Sarbanes-Oxley and ISO 9000*, QUALITY PROGRESS, March 2005, at 24, 28, available at <http://sqp.asq.org/pub/qualityprogress/past/0305/qp0305stimson.pdf>. The ISO only affects companies who are registered under the ISO. *Id.* A list of countries following the ISO standards can be found here. International Organization for Standardization, <http://www.iso.org/iso/en/aboutiso/isomembers/MemberList.MemberSummary?MEMBERCODE=10> (last visited Nov. 6, 2005).

²⁵⁸ Stimson, *supra* note 257, at 28. The provisions can be found in the ISO 9001, which is a set of managed and applied procedures. *Id.*, at 25. The certain provisions criminalizing dishonest reports and fraudulent quality systems are clauses 4.2.3, 4.2.4, and 8.0. *Id.*, at 28. An English translation of the ISO 9001 can be found here. ISO 9001, <http://praxiom.com/iso-9001.htm> (last visited Nov. 6, 2005).

²⁵⁹ *Id.* at 29.

²⁶⁰ *Raising the Rent*, *supra* note 4, at 28.

²⁶¹ PRACTICAL GUIDE, *supra* note 17, at xxi. SOX not only affects public companies, but also affects private companies indirectly. *Id.* Once private companies see SOX raising the public expectations for good corporate governance, they will also have to conform or lose business. *Id.* Nonprofit organizations and accountants who do not audit public companies will also feel the indirect effects of SOX. *Id.* at xxii.

²⁶² *Raising the Rent*, *supra* note 4, at 3.

²⁶³ Ackerly, *supra* note 168.

jurisdictions.”²⁶⁴ He urged any effected party to “let us know when our proposals conflict with local law or local stock exchange requirements. . . . [W]e do promise to listen, . . . and do our best to harmonize the application of our rules with foreign sovereign requirements.”²⁶⁵

A. Extraterritoriality Problems of SOX

The United States assertion of SOX in the global forum has created controversy all over the world.²⁶⁶ SOX was applauded domestically but was greatly criticized internationally.²⁶⁷ SOX was criticized for “being made applicable to all foreign issuers listed on a U.S. exchange, even though some of the behavior the Act targeted was either a non-issue in foreign countries or was already efficiently regulated.”²⁶⁸

1. Statutory Enforcement Power under SOX

The statutory enforcement language of SOX can be found in Section Three of the Act.²⁶⁹ Section Three is entitled “Commission Rules and Enforcement.”²⁷⁰ It covers both regulatory actions of the commission and enforcement powers.²⁷¹ The term “commission” means the SEC.²⁷² Under this provision, the SEC “shall promulgate such rules and regulations, as may be necessary or appropriate in the public interest or for the protection of investors, and in furtherance of this Act.”²⁷³

²⁶⁴ Ackerly, *supra* note 168.

²⁶⁵ *Id.*

²⁶⁶ Vancea, *supra* note 154, at 839.

²⁶⁷ Cheryl Jerome Moore, *Current Issues Regarding Corporate Governance and Multinational Corporations*, <http://library.findlaw.com/2004/Oct/27/133621.html> (last visited Nov. 6, 2005).

²⁶⁸ Vancea, *supra* note 154, at 839.

²⁶⁹ The Act, *supra* note 27, at § 3.

²⁷⁰ *Id.*

²⁷¹ PRACTICAL GUIDE, *supra* note 17, at 3004.

²⁷² *Id.* at 3003. This definition can be found in the definitions section of SOX at Section 2. *Id.* at 3002.

²⁷³ *Id.* at 3004.

The enforcement provision can be found in Section Three of SOX.²⁷⁴ The enforcement provision states,

A violation by any person of this Act, any rule or regulation of the Commission issued under this Act, or any rule of the Board shall be treated for all purposes in the same manner as a violation of the Securities Exchange Act of 1934 (15 U.S.C 78a et seq.) or the rules and regulations issued thereunder, consistent with the provisions of this Act, and any such person shall be subject to the same penalties, and to the same extent, as for a violation of that Act or such rules or regulations.²⁷⁵

This provides a broad grant of jurisdictional authority for the SEC and Department of Justice to impose criminal and civil sanctions under the requirements contained in SOX.²⁷⁶

2. United States Assertion of Extraterritorial Jurisdiction

The assertion of extraterritorial jurisdiction by the United States has been criticized by the international community.²⁷⁷ Extraterritorial jurisdiction is defined as:

. . . the operation of a U.S. law so as to encompass activities where (1) the conduct at issue occurs within the U.S., but its effects take place abroad; (2) the conduct occurs abroad, but its effects take place in the U.S.; or (3) both the conduct and its effect occur abroad.²⁷⁸

²⁷⁴ PRACTICAL GUIDE, *supra* note 17, at 3004.

²⁷⁵ *Id.* The Securities Exchange Act of 1934 regulates securities exchanges and corporate responsibility. 15 U.S.C.A § 78a (West, Westlaw through Sept. 2005 amendments).

²⁷⁶ Stephen M. Kohn, *The Sarbanes-Oxley Act ("SOX"): Legal Protections for Corporate Whistleblowers*, <http://www.whistleblowers.org/html/sarbanes-oxley.htm> (last visited Nov. 6, 2005).

²⁷⁷ Vancea, *supra* note 154, at 833.

²⁷⁸ *Id.* The principles of extraterritorial jurisdiction can be found in §402 of the Restatement (Third) of the Foreign Relations Law of the United States. RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 402 (1987) [HEREINAFTER RESTATEMENT]. *See also id.* at §403 (1987) (Factors assessing the reasonableness of asserting jurisdiction to prescribe over a matter are:

(1) Even when one of the bases for jurisdiction under § 402 is present, a state may not exercise jurisdiction to prescribe law with respect to a person or activity having connections with another state when the exercise of such jurisdiction is unreasonable.

(2) Whether exercise of jurisdiction over a person or activity is unreasonable is determined by evaluating all relevant factors, including, where appropriate:

(a) the link of the activity to the territory of the regulating state, i.e., the extent to which the activity takes place within the territory, or has substantial, direct, and foreseeable effect upon or in the territory;

(b) the connections, such as nationality, residence, or economic activity, between the regulating state and the person principally responsible for the activity to be regulated, or between that state and those whom the regulation is designed to protect;

(c) the character of the activity to be regulated, the importance of regulation to the regulating state, the extent to which other states regulate such activities, and the degree to which the desirability of such regulation is generally accepted.

(d) the existence of justified expectations that might be protected or hurt by the regulation;

(e) the importance of the regulation to the international political, legal, or economic system;

SOX is concerned with the conduct that takes place in the United States, but the effects are felt abroad.²⁷⁹ The Restatement (Third) of the Foreign Relations Law of the United States describes the link between territoriality and nationality:

International law recognizes links of territoriality, Subsection (1), and nationality, Subsection (2), as generally justifying the exercise of jurisdiction to prescribe. But these links are not sufficient in all cases: not all activities within a state's territory, nor all activities of a state's nationals, may reasonably be subjected to its legislation.²⁸⁰

However, this is a rule stated in a Restatement of the law and does not bind any court until it adopts the rule.²⁸¹

Jurisdiction is the “power of a sovereign to affect the rights of persons, whether by legislation, by executive decree, or by the judgment of a court.”²⁸² This definition lays out the principle that a “State has the right to exercise jurisdiction within the limits of its sovereignty, but is not entitled to encroach upon the sovereignty of other States.”²⁸³ International law imposes “limits on the ability of states to encroach on the sovereignty of other states by delineating the acceptable bases for asserting jurisdiction.”²⁸⁴

There are two types of limitations used by the United States courts in determining the extent of jurisdiction.²⁸⁵ The limitations applied by the courts are the subject matter test and

(f) the extent to which the regulation is consistent with the traditions of the international system;

(g) the extent to which another state may have an interest in regulating the activity; and

(h) the likelihood of conflict with regulation by another state).

²⁷⁹ Vancea, *supra* note 154, at 835.

²⁸⁰ RESTATEMENT, *supra* note 278, at §402.

²⁸¹ Shirley, *supra* note 6, at 521.

²⁸² Joseph H. Beale, *The Jurisdiction of a Sovereign State*, 36 HARV. L. REV. 241, 241 (1923).

²⁸³ James D. Cox, *Regulatory Duopoly in U.S. Securities Markets*, 99 COLUM. L. REV. 1200, 1240 n.130 (1999).

²⁸⁴ Vancea, *supra* note 154, at 846.

²⁸⁵ *Id.* at 848.

prescriptive test to determine jurisdiction.²⁸⁶ These limitations are in addition to the limitations set by international law.²⁸⁷

The subject matter test for United States extraterritoriality is based on two presumptions.²⁸⁸ The first presumption is that acts of Congress are not to be construed in violation of international law.²⁸⁹ This presumption is known as the *Charming Betsy* presumption.²⁹⁰ The presumption recognizes the potential for international conflict created by violations of international law and is used to determine vague congressional intent.²⁹¹ The second presumption is imposed under a canon of construction stating “legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States.”²⁹² This presumption is known as the *Foley Bros.* presumption.²⁹³ To discern Congressional intent the Supreme Court relied upon three factors: (1) the absence of an expressed intent that the statute apply to foreign companies;²⁹⁴ (2) the legislative history of the statute;²⁹⁵ (3) administrative decisions.²⁹⁶

3. Extraterritoriality of Securities Regulation before SOX

²⁸⁶ Vancea, *supra* note 154, at 848.

²⁸⁷ *Id.* The Supreme Court laid out the appropriate sources of international law when it stated international law “may be ascertained by consulting the works of jurists, writing professedly on public law; or by the general usage and practice of nations; or by judicial decisions recognizing and enforcing that law.” *Filartiga v. Pena-Irala*, 630 F.2d 876, 880 (quoting *United States v. Smith*, 18 U.S. (5 Wheat.) 153, 160-61 (1820)).

²⁸⁸ Vancea, *supra* note 154, at 848.

²⁸⁹ *Murray v. Schooner Charmin Betsy*, 6 U.S. 64, 118 (1804). “[A]n act of Congress ought never to be construed to violate the law of nations if any other possible construction remains.” *Id.* This case was a controversy over a vessel sold in a Danish island and whether it was liable to seizure under the non-intercourse law of February 27, 1800. *Id.* at 65.

²⁹⁰ Vancea, *supra* note 154, at 849.

²⁹¹ *Id.*

²⁹² *Foley Brothers v. Filardo*, 336 U.S. 281,285 (1949). This case dealt with a controversy concerning overtime wages due to an employee under the Federal Eight Hour Law. *Id.* at 281. *See also* *American Banana Company v. United Fruit Company*, 213 U.S. 347 (1909) (holding that when a statute is silent on jurisdiction, it should be construed to only apply to conduct occurring in the territory of the United States).

²⁹³ Vancea, *supra* note 154, at 849.

²⁹⁴ *Foley Brothers*, 336 U.S. at 285.

²⁹⁵ *Id.* at 286.

²⁹⁶ *Id.* at 288.

The extraterritoriality of securities regulations is not a drastic or new idea; corporations outside of the United States have been subjected to United States securities regulations for quite some time.²⁹⁷ The first case examining the scope of Securities regulation outside of the United States was in *Schoenbaum v. Firstbrook*, a case that was filed in 1968.²⁹⁸ Schoenbaum was a controversy over whether the Securities Exchange Act of 1934 applied to a Canadian oil company, listed on an American stock exchange that was engaging in insider trading.²⁹⁹ The district court granted summary judgment to defendants on the grounds that the complaint failed to state a claim under section 10(b) of the Securities Exchange Act of 1934.³⁰⁰ The Court of Appeals reversed in part and affirmed in part. The Court of Appeals stated:

. . . plaintiff stockholder's allegations that majority stockholder, knowing true value of corporation's stock, used its control over corporation to acquire 500,000 shares at a vastly inadequate price shortly before public announcement of corporation's oil discovery required that plaintiff be permitted through discovery to develop evidence to counter defense affidavits, but that where it appeared that negotiations for purchase of treasury stock by other defendant were at arm's length and that purchaser, and those whom it represented, were unable to bring any pressure on corporation to sell its stock at price below its true value, purchaser was entitled to dismissal of action against it.³⁰¹

The court reversed on the issue of extraterritoriality, but decided that the insiders had not engaged in illegal insider trading regardless of their decision on the extraterritoriality argument.³⁰² This decision found the Securities Exchange Act of 1934 applied extraterritorially.³⁰³ The case also created the “effects” test under federal securities laws.³⁰⁴

²⁹⁷ Shirley, *supra* note 6, at 515.

²⁹⁸ *Schoenbaum*, 405 F.2d at 215.

²⁹⁹ Siegel, *supra* note 9.

³⁰⁰ *Schoenbaum*, 405 F.2d at 215. Section 10(b) of the Securities Exchange Act of 1934 deals with manipulative and deceptive devices. 15 U.S.C.A. § 78j (West 2000). This provision is used to protect the public interest and also the investors of corporations. *Id.*

³⁰¹ *Schoenbaum*, 405 F.2d at 215.

³⁰² Siegel, *supra* note 9.

³⁰³ Vancea, *supra* note 154, at 850. *See also* Kohn v. American Metal Climax Inc., 489 F.2d 262 (New York based insiders of a Zambian firm, who listed on and American stock exchange, had violated disclosure laws; court found jurisdiction); *Derensis v. Coopers & Lybrand Chartered Accountants*, 930 F.Supp. 1003 (Canadian company listed on an American stock exchange was charged with securities fraud; court found jurisdiction); *Landry v. Price Waterhouse Chartered Accountants*, 715 F. Supp. 98 (Canadian company listed on an American stock exchange was charged with financial fraud; court found jurisdiction); *In Re Baan Company Securities Litigation*, 284 F.Supp.2d 62

4. International Comity Considerations

Comity is a term used in international law when dealing with relations between the United States and other nations.³⁰⁵ It is described as an “informal principle that nations will extend certain courtesies to other nations, particularly by recognizing the validity and effect of their executive, legislative, and judicial acts.”³⁰⁶ This issue is most frequently raised by the courts, which should not “act in a way that demeans the jurisdiction, laws or judicial decisions of another country.”³⁰⁷ The courts have adopted multiple balancing tests to address questions of comity and extraterritoriality desiring to avoid undue intrusion into the business and affairs of other countries.³⁰⁸

An important case in setting out the United States view of comity is the Supreme Court decision of *Hartford Fire Insurance Company v. California*.³⁰⁹ This case involved the

(Dutch company listed on United States stock exchange sued for making financial misstatements; court found jurisdiction).

³⁰⁴ *United States v. Aluminum Company of America*, 148 F.2d 416, 444 (2d Cir. 1945) (Judge Learned Hand adopted the “effects” test; the court held the Sherman Act applied to foreign firms if their conduct affected the United States). For the “effects” test you must look “whether the transaction or conduct has, or can reasonably be expected to have, a substantial effect on a securities market in the United States for securities of the same issuer or on holdings in such securities by United States nationals or residents.” RESTATEMENT, *supra* note 278, §416.

³⁰⁵ Comity, <http://en.wikipedia.org/wiki/Comity> (last visited Oct. 14, 2005).

³⁰⁶ *Id.*

³⁰⁷ *Id. But see Societe Nationale Industrielle Aerospatiale v. United States Dist. Court* 482 U.S. 522, 553 (Blackmun J., concurring in part and dissenting in part) (arguing that interest balancing is more appropriately considered by the Executive and Congress because judges lack experience with foreign legal systems, misapprehend foreign procedural rules, inaccurately assess foreign responses to particular acts, and are likely to exhibit a pro-forum basis), Vancea, *supra* note 237, n. 136.

³⁰⁸ Patton Boggs, LLP, *Current Issues Regarding Corporate Governance and Multinational Corporations*, <http://library.findlaw.com/2004/Oct/27/133621.html> (last visited Nov. 6, 2005). When dealing with balancing the interests of multiple countries, you must ask the question “Does the need for a U.S. rule of law, in this instance, outweigh the likelihood of conflict with foreign laws and practices?” Nanda, Ved P. et al., 1 *Litigation of International Disputes in U.S. Courts* §5:1 (2004).

³⁰⁹ *Hartford Fire Insurance Co. v. California*, 509 U.S. 764 (1993). *Compare SEC v. Banca Della Svizzera Italiana*, 92 F.R.D. 111, 117-18. (S.D.N.Y 1981) (expressing concern that “secret foreign financial institutions . . . have allowed Americans and others to avoid the law and regulations concerning securities and exchanges”) *with United States v. Nippon Paper Indus. Co.*, 109 F.3d 1, 8 (1st Cir. 1997) (refusing to dismiss criminal antitrust charges on comity grounds since to do so “would create perverse incentives for those who would use nefarious means to influence markets in the United States, rewarding them for erecting as many territorial firewalls as possible between cause and effect”).

jurisdiction of the Sherman Antitrust Act over foreign reinsurers.³¹⁰ The Supreme Court held that the Sherman Act did have extraterritorial jurisdiction over foreign reinsurers under principles of international comity.³¹¹ The main issue the court struggled with was whether the provisions of the Sherman Act were in direct conflict with foreign law.³¹² Reinsurers from London argued that the Sherman Act conflicted with British Law.³¹³ It was well settled law before this case was decided that the Sherman Act applied to conduct by foreign parties that produced a substantial effect in the United States.³¹⁴ The court found that there was no conflict with British law.³¹⁵ The court also found that “where a person subject to regulation by two states can comply with the laws of both.”³¹⁶

5. Extraterritoriality of SOX

SOX regulations apply to all companies listed on any United States exchange regardless of whether it is a domestic or foreign company.³¹⁷ In some instances, however, SOX makes it impossible to comply with laws in countries outside the United States.³¹⁸ A good example is Australia; under Australian corporate law, shareholders select the auditor instead of a committee like required under SOX.³¹⁹ This is a situation where the regulation under SOX directly conflicts

³¹⁰ *Hartford Fire Insurance Co.*, 509 U.S. at 764. The Sherman Antitrust Act was passed in 1980 to disband existing monopolies and not let any more arise in their place. 15 U.S.C. §§ 1-7.

³¹¹ *Hartford Fire Insurance Co.*, 509 U.S. at 764.

³¹² *Id.* at 798.

³¹³ *Id.* at 798.

³¹⁴ *Id.* at 795. See also *Matsushita Elec. Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574, 582, n. 6 (1986) (American television manufacturers could not recover antitrust damages against Japanese television manufacturers for any conspiracy by the Japanese manufacturers since such conduct could not injure the American manufacturers who stood to gain from any such conspiracy); *United States v. Aluminum Co. of America*, 148 F.2d 416 (2d Cir. 1945) (Judge Learned Hand adopted the “effects” test; the court held the Sherman Act applied to foreign firms if their conduct affected the United States); RESTATEMENT § 415 (Any agreement in restraint of United States trade that is made in the United States, and any conduct or agreement in restraint of such trade that is carried out in significant measure in the United States, are subject to the jurisdiction to prescribe of the United States, regardless of the nationality or place of business of the parties to the agreement or of the participants in the conduct).

³¹⁵ *Hartford Fire Insurance Co.*, 509 U.S. at 798.

³¹⁶ *Id.* at 798 (citing RESTATEMENT § 403).

³¹⁷ Information Guide, *supra* note 15.

³¹⁸ Patton Boggs, LLP, *supra* note 308.

³¹⁹ *Id.*

with the law of a host country, and falls specifically under the comity concerns raised in *Hartford Fire Insurance Co.*³²⁰

SOX specifically regulates all firms listing on a United States exchange regardless of whether they are a domestic or foreign company.³²¹ SOX regulates these companies by using specific language out of the Act. Extraterritoriality can be found under the language of SOX, by using the specific language of enforcement provisions, which make no distinction between domestic and foreign firms.³²² This can be analogized to the Supreme Court's holding in *Hartford Fire Insurance Co.*³²³ The court talks about a type of jurisdiction relevant to the extraterritorial reach of a statute known as "legislative jurisdiction" or "jurisdiction to prescribe".³²⁴ When deciphering the jurisdiction issue, look to the intent of the legislature for guidance.³²⁵ The courts have consistently held that the legislation of Congress, unless a contrary intent appears, is meant to only apply in the territory of the United States.³²⁶ The enforcement language under SOX³²⁷ would seem to indicate that Congress meant for the Act to apply to all companies listed on a United States Exchange, both foreign and domestic.³²⁸

To discern the Congressional intent behind SOX, look to the legislative history behind the Act.³²⁹ Members of Congress were very reluctant in imposing SOX regulations on countries whose corporate responsibility frameworks were adequate or superior to the corporate

³²⁰ *Hartford Fire Insurance Co.*, 509 U.S. at 798. If the British law would have been in direct conflict with the Sherman Act, then a comity issue would have arisen. *Id.*

³²¹ The Act, *supra* note 27, at § 3.

³²² The Act, *supra* note 27, at § 3.

³²³ *Hartford Fire Insurance Co.*, 509 U.S. at 798.

³²⁴ *Id.* (citing *E.E.O.C. v. Arabian American Oil Co.*, 499 U.S. at 253). This case held that Title VII of the Civil Rights Act does not apply extraterritorially. *E.E.O.C.*, 499 U.S. at 244.

³²⁵ *Hartford Fire Insurance Co.*, 509 U.S. at 798.

³²⁶ *Id.* at 798 (quoting *E.E.O.C. v. Arabian American Oil Co.*, 499 U.S. at 248).

³²⁷ The Act, *supra* note 27, at § 3.

³²⁸ *Raising the Rent*, *supra* note 4, at 3.

³²⁹ *Foley Brothers*, 336 U.S. at 286.

responsibility framework of the United States.³³⁰ Senator Enzi, during a discussion on the Senate floor, stated:

While foreign issuers can be listed and traded in the U.S. if they agree to conform to GAAP and New York Stock Exchange rules, the SEC historically has permitted the home country of the issuer to implement corporate governance standards. Foreign issuers are not part of the current problems being seen in the U.S. capital markets, and I do not believe it was the intent of the conferees to export U.S. standards disregarding the sovereignty of other countries as well as their regulators.³³¹

Senator Enzi's opinion shows that at least some of the lawmakers behind the passage of SOX desired the legislation to only regulate companies in the United States, because foreign companies were not part of the scandals leading up to the passage of this bill.³³²

V. SUCCESS OF SOX

The question asked by companies both in the United States and abroad is whether SOX has had a positive effect on securities markets around the world or if it has imposed too great of a regulation. When SOX was implemented in 2002, an international outcry from many multinational corporations and foreign firms rang out claiming that SOX was ineffective and that Congress "rushed" the legislation.³³³ Multinational firms all across the world have clamored for exemptions from the regulations imposed by SOX.³³⁴ These firms requested exemptions from certain provisions of SOX such as prohibitions on foreign loans³³⁵ and forfeitures by certain officers of compensation and securities-related profits.³³⁶ Multinational corporations have formed the Reciprocity in International Accounting Coalition to "push for changes that affect

³³⁰ 148 Cong. Rec. S 7350, 7356 (2002).

³³¹ *Id.* at 7356 (2002). Mike Enzi is a senator from Wyoming. Senator Mike Enzi, <http://enzi.senate.gov/> (last visited Nov. 9, 2005).

³³² 148 Cong. Rec. S at 7356 (2002).

³³³ Lucci, *supra* note 151, at 219.

³³⁴ *Id.* at 219 (citing Fiona Buffini, *Multinationals Seek Exemption from Act*, AUSTL. FIN. REV., Sept. 2, 2002, at 16).

³³⁵ The Act, *supra* note 27, at § 402.

³³⁶ *Id.* at § 304. The multinational firms are part of the Organization for International Investment (OFII). Letter from OFII, to Jonathan G. Katz, Secretary, Sec. Exch., Comm'n (August 19, 2002) (on file with the Sec. Exch. Comm'n), available at http://www.ofii.org/SEC_Letter_081902.pdf. OFII is the "leading business association in the United States representing the interests of U.S. subsidiaries of nearly 100 international companies." *Id.*

international companies and their corporate officers.”³³⁷ A concern for the United States securities market is whether the regulation of SOX will have an effect on companies cross-listing on a United States exchange and also the influence SOX has on foreign and multinational firms when creating models of corporate governance regimes in their respective countries of domicile.³³⁸

A. *The Decision to Cross-List*

Cross-listing is the practice where foreign and multinational firms list their companies on a United States stock exchange.³³⁹ These companies usually cross-list with the aid of American Depository Receipts (ADRs), which are a form of derivative securities.³⁴⁰ United States depository banks hold foreign securities in custody in the country of origin and convert all payments into United States dollars to receipt holders in the United States. Investors bear all the currency risk and pay fees to the depository banks. Foreign companies must also satisfy two requirements to list on a United States exchange.³⁴¹ The first requirement is to arrange for a precise reproduction of settlement facilities as domestic securities with a transfer agent and registrar.³⁴² The firm must also register with the SEC.³⁴³ To accomplish this, a firm must file a

³³⁷ Judy Sarasohn, Coalition Targets Accounting Law, Wash. Post, Oct. 24, 2002, at A33, available at <http://www.washingtonpost.com/ac2/wp-dyn?pagename=article&contentId=A8481-2002Oct24¬Found=true>.

³³⁸ Craig Doidge et al., Private Benefits of Control, Ownership, and the Cross-Listing Decision 1 (European Corp. Governance Inst., Working Paper No. 77/2005, 2005), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=668424.

³³⁹ John C. Coffee Jr., *Racing Towards the Top?: The Impact of Cross-Listings and Stock Market Competition on International Corporate Governance*, 102 COLUM. L. REV. 1757, 1757 (2002).

³⁴⁰ Cally Jordan, International Cross-Listing and Bonding: The Chameleon Effect 1 (Sept. 13, 2004) (unpublished manuscript, on file with University of Florida College of Law). ADRs were developed by JP Morgan in 1927. Stephen R. Foerster & G. Andrew Karolyi, *The Effects of Market Segmentation and investor Recognition on Asset Prices: Evidence from Foreign Stocks Listing in the United States*, 54 J. FIN. 981, 983 (1999), available at <http://www.cob.ohio-state.edu/fin/faculty/karolyi/papers/JF1999.pdf>. They were created as a method for investors to register and earn dividends on non - United States stock. *Id.*

³⁴¹ Foerster & Karolyi, *supra* note 340.

³⁴² *Id.*

³⁴³ *Id.*

registration statement and supply an annual report on a Form 20-F with a reconciliation of financial accounts performed under the requirements of GAAP.³⁴⁴

1. Benefits of Cross-Listing

The benefits of foreign and multinational companies cross-listing include “the increased ability to raise equity, growth of the firm’s shareholder base, increased liquidity, lower cost of capital, and greater visibility and prestige.”³⁴⁵ Another potential benefit for a firm cross-listing could be that United States investors would identify which new and innovative firms are likely to succeed.³⁴⁶ The cost of listing in the United States, according to reports by managers, is very small when compared to the benefits.³⁴⁷ Some scholars contend that “the primary benefit of cross listing involves voluntary submission to the U.S. disclosure and liability regimes, which may send a signal of firm quality and thereby reduce capital costs.”³⁴⁸ The number of foreign and multinational companies cross-listing on a United States exchange has increased tremendously since the early 1990’s.³⁴⁹ For example, the number of firms cross-listing on the New York Stock Exchange (NYSE) had more than quadrupled to 471 firms as of October, 2002.³⁵⁰

2. Costs of Cross-Listing

³⁴⁴ *Id.*

³⁴⁵ Doidge et al., *supra* note 338, at 1 (citing surveys done by Karolyi in 1998 and 2004; Claessens, Klingebeit, and Schmukler in 2002; Benos and Weisbach in 2004; these surveys evaluate over one hundred and fifty studies that examine the decision to cross-list shares on a foreign market).

³⁴⁶ Christopher Woo, The Effects of Sarbanes-Oxley on Foreign Private Issuers 4 (unpublished manuscript, on file with Harvard Law School), *available at* http://www.law.harvard.edu/programs/pifs/pdfs/christopher_woo.pdf.

³⁴⁷ Craig Doidge et al., Why are foreign firms listed in the U.S. worth more? 1 (National Bureau of Economic Research, Working Paper No. 8538, 2003), *available at* <http://jfe.rochester.edu/02367.pdf>.

³⁴⁸ Perino, *supra* note 10 (Citing Oren Fuerst, A Theoretical Analysis of Investor Protection Regulations: Argument for Global Listing of Stocks (Sept. 10, 1998) (unpublished paper, on file with author)).

³⁴⁹ Kees G. Koedijk & Mathijs A. van Dijk, The Cost of Capital of Cross-Listed Firms 2 (Erasmus Research Institute of Management, Working Paper No. ERS-2002-99-F&A, 2002), *available at* http://www.business.uts.edu.au/qfrc/conferences/qmf2002/VanDiji_M.pdf.

³⁵⁰ *Id.* at 2.

Major costs of listing include “the disclosure standard, the requirement of accounting reconciliation, the direct cost in time and money associated with a United States listing, and the fear of liability.”³⁵¹ Whenever the firm wants to buy another company it must follow the United States disclosure and procedural rules, rather than the law of their respective country of domicile.³⁵² There are costs to list on a United States exchange including a listing fee for registration with the SEC and other associated costs for the necessary paperwork.³⁵³ Additional costs also include “increases in directors’ and officers’ liability insurance, accounting and legal fees, and board compensation (as board members are given increased responsibility and may be subjected to higher risk).”³⁵⁴ One recent study estimated that “public companies as a group would spend \$2.5 billion on information technology and related consulting in order to comply with the Act’s internal control requirements.”³⁵⁵

3. Effect of SOX on Cross-Listing

SOX has had an effect on the decision of foreign and multinational firms to cross-list on a United States exchange.³⁵⁶ There are many companies that are hesitant to cross-list due to the regulations imposed by SOX.³⁵⁷ Porsche has decided not to list, citing “problems with Sarbanes-Oxley, and has announced that it will not change its decision even after the proposed exemptions.”³⁵⁸ Companies such as the Benfield Group have chosen to list in London instead of listing on a United States exchange stating that the “London Stock Exchange has been quite openly using the regulatory hurdles associated with the Sarbanes-Oxley Act as a marketing

³⁵¹ Woo, *supra* note 346, at 7 (citing James A. Fanto & Roberta S. Karmel, *A Report on the Attitudes of Foreign Companies Regarding a U.S. Listing*, 3 STAN. J.L. BUS. & FIN. at 64, 69 (1997)).

³⁵² Siegel, *supra* note 9.

³⁵³ Foerster & Karolyi, *supra* note 340, at 984.

³⁵⁴ Perino, *supra* note 10.

³⁵⁵ *Id.* (quoting Eileen Colkin Cuneo, *Y2K Again? Say It Ain't So*, INFORMATIONWEEK.COM, May 19, 2003, at 20).

³⁵⁶ Woo, *supra* note 346, at 19.

³⁵⁷ *Id.*

³⁵⁸ *Id.*

wedge against U.S. registration and listing.”³⁵⁹ The letter, written by the Benfield Group to the SEC, also stated that SOX has led to “foreign regulators, companies and media questioning the right of Congress to change the rules for non-U.S. listed companies ‘in the middle of the game.’”³⁶⁰ William Donaldson, Chairman of the SEC, made the following statement in a speech in London:

We also seek to have a listing in the U.S. to signify to investors throughout the world that this company is willing to make the investment needed to meet these standards. Companies who choose not to come to the United States may meet those same standards – but our registrants have taken the extra step of telling the world that they are up to the challenges that accompany a U.S. listing.³⁶¹

In that same speech, however, he also states “the SEC has worked from its earliest days to accommodate foreign issuers” and “The SEC remains committed to a level playing field for all its issuers, foreign and domestic alike.”³⁶²

B. Influence of SOX on Corporate Governance Standards Worldwide

The success of Sarbanes-Oxley can also be seen in the influence which the Act has had on corporate governance standards abroad. Many countries are using Sarbanes-Oxley as a model for implementing their own regulations.³⁶³ South Korea has implemented regulations for CEO certifications of company financial reports.³⁶⁴ Companies in South Korea must get “CEOs to swear to the accuracy of their company's financial statements, to present consolidated financial sheets of affiliated firms, and to set up a ‘firewall’, separating auditing and consulting businesses.”³⁶⁵ Australia, even after rejecting it at first glance, is now considering using SOX as

³⁵⁹ Letter from Darla Stuckey, Corp. Secretary, NYSE, to Jonathan G. Katz, Secretary, Sec. Exch., Comm’n (Feb. 21, 2003) (on file with the Sec. Exch. Comm’n), *available at* <http://www.sec.gov/rules/proposed/s70203/dcstuckey1.htm>.

³⁶⁰ Stuckey, *supra* note 359.

³⁶¹ Donaldson, *supra* note 25.

³⁶² *Id.*

³⁶³ Patton Boggs, LLP, *supra* note 308.

³⁶⁴ *Id.*

³⁶⁵ Lucci, *supra* note 151, at 244.

a model and holding executives liable for the credibility of financial statements.³⁶⁶ Canada introduced a bill with very similar terms as SOX but the regulations imposed by the bill are not nearly as comprehensive.³⁶⁷ A commentator from the United Kingdom even stated that SOX “looks certain to become the benchmark against which every other jurisdiction’s corporate governance rules are tested.”³⁶⁸

VI. CONCLUSION

In conclusion, SOX is a very controversial act that has many companies, foreign and multinational, asking for relief. SOX was enacted to deter corporate corruption in the United States, but has had a global impact. There are many regulations imposed by SOX that conflict with international corporate governance standards and also regulations of individual countries outside the United States.

The extraterritoriality of SOX is a hotly debated topic. It will continue to be until either the SEC decides to exempt all foreign and multinational companies listing on a United States exchange from regulation or there is a convergence of SOX and international corporate governance regulations. Companies can only look to the legislative history of SOX and past decisions to see how SOX may affect them in the future.

The SEC has the power to grant exemptions to foreign and multinational firms, but doing so may invoke an outcry from domestic firms. If the SEC is not applying the same rules, it will destroy the even playing field that the SEC desired to create by enacting SOX. The effectiveness of SOX will be greatly weakened if firms will be exempted from certain regulations, just because

³⁶⁶ *Id.*

³⁶⁷ See Julius Melnitzer, *Sarbanes-Oxley Creeps Across Border: Canada Debates Need for SEC-Type Governance Rules and Regulations*, 2/03 CORP. LEGAL TIMES 33 (COL. 1), Feb. 2003. It imposes rule on attorneys to report violations, but it is not as stringent as SOX. *Id.* The measures were introduced to stimulate the amount of investment to Canadian Capital markets. *Id.*

³⁶⁸ Patton Boggs, LLP, *supra* note 308 (quoting Andrew Sawers, *Company Law, Act Brings Greater Accountability*, FIN. DIRECTOR (U.K.), Oct, 1, 2002).

they move their headquarters outside of the United States or move a majority of their operations outside of the United States.

Legislation will not be enough, by itself, to swing the pendulum in the right direction. Companies, both foreign and domestic, must take personal responsibility in restoring investor confidence in the United States securities and capital market and also the global securities market. SOX is a step in the right direction, but companies must do everything in their power to deter corruption and restore confidence in markets where there is none.