

CHOICE OF LAW RULES FOR INTERNATIONAL SECURITIES TRANSACTIONS?

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I. INTRODUCTION

Because global securities offerings, international takeovers, and the cross listing of securities are today common events, conflict of laws considerations have prominently invaded the arcane field of securities regulations. Professor Roberta Karmel's review of the takeover rules of the United States, United Kingdom, Germany, and Australia captures nicely the regulatory collage that faces one planning a transnational takeover.¹ No participant in the international takeover is immune to the effects of conflicting requirements. For example, the U.S. laws permit the bidder to purchase a significant block of the target corporation's shares before the public tender offer for shares is made without having to offer the same price to the other target shareholders in its upcoming tender offer.² Whereas, if the target of the takeover is subject to the British laws, any higher price paid for shares acquired during the three months preceding the public tender offer must be offered as well in the later public tender offer.³ Not the least of the concerns for the international bidder are the wide differences in substantive and procedural rules that apply to private litigation for disclosure violations arising in a takeover. Class actions, contingency fee arrangements, and liberal approaches to such substantive issues as

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1. See Roberta S. Karmel, *Transnational Takeover Talk—Regulations Relating to Tender Offers and Insider Trading in the United States, The United Kingdom, Germany, and Australia*, 66 U. CIN. L. REV. 1133 (1998).

2. See, e.g., *Kahn v. Virginia Retirement Sys.*, 783 F. Supp. 266, 270-71 (E.D. Va. 1992) (shares purchased after press release announcing intent to commence a tender offer but before formal commencement did not violate the best price provision). *But see Eptstein v. MCA, Inc.*, 50 F.3d 644, 655 & n.18 (9th Cir. 1995), *rev'd on other grounds*, 516 U.S. 367 (1996) (purchase of insider's shares moments before publication of commencement of tender violated best price rules because tender offer commences at 12:01 a.m. of the date of the publication).

3. See City Code on Take-overs and Mergers, Rule 6.1, in 2 WEINBERG & BLANK ON TAKE-OVERS AND MERGERS 7001, 7051 (Laurence Rabinowitz ed., 5th ed. 1989) [hereinafter City Code on Take-overs and Mergers].

materiality, recklessness, and causation, each are sobering considerations for bidders considering whether its bid should cross into U.S. regulatory waters.

It is not an uncommon practice for bidders to avoid unwanted takeover regulations and their accompanying liability regimes, most notably those of the United States, by excluding U.S.-based investors from its bid. Such a strategy then raises the issue whether the excluded investors are harmed by the very regulations that are intended for their benefit. Their possible injury has two sources. First, they are denied a chance to share equally with their foreign counterparts in the takeover premium offered to the target's shares. Second, investors who seek to overcome their exclusion by selling their shares in the market (most likely the target's home market) will incur nontrivial transactions costs. Not only will they bear a commission in disposing of their shares (in contrast those who tender to the bidder have no brokerage costs), but the price they receive for the shares will reflect the standard arbitrage discount. And, if the excluded target shareholder holds depositary receipts, there will necessarily be a delay and cost associated with converting the receipts into the underlying ordinary shares.

Professor Karmel also illustrates important differences that exist among the examined countries' insider trading laws—for example, the resources each country devotes to the detection of insider trading. In the case of insider trading, this is a far more important factor than the underlying definitions for proscribing unlawful insider trading. As discussed below, the laws of the United Kingdom, Germany, and Australia are each much more demanding in their proscription of tipping of inside information. Nevertheless, we find a fair number of tippers and their tippees are prosecuted in the United States more readily than in other countries because of the much more robust detection efforts that are carried out by the U.S. self-regulatory organizations and the Securities and Exchange Commission (SEC). Thus, differences among countries in their respective regulation of insider trading exist, as is the case with takeovers, because of different substantive and procedural considerations.

Significant substantive and procedural differences also exist among countries in their treatment of sales of securities and misrepresentations that occur in such transactions. Here we find that the differing definitions of what constitutes a security, the exemptions that apply for their sale and resale, and even what constitutes a misrepresentation pose sobering reminders to capital-hungry entrepreneurs to choose their markets with the wise advice of their securities lawyer.

International takeovers, cross border insider trading, and transnational sales of securities each invoke its own set of policy issues

relevant to its regulation. Indeed, nations are no different than commentators in disagreeing widely as to just what policy consideration is to be served by, for example, the regulation of takeovers or insider trading; further disagreements arise, of course, as to how best to fulfill a policy objective. Though these three types of securities transactions are quite different from one another, they do each share a common consideration relevant to the present investigation of how conflicting regulatory demands are best addressed when a securities transaction invokes the jurisdiction of more than one country. The issue simply is whether and to what extent securities regulations is public law or private law.

II. THE MOVEMENT FROM PUBLIC TO PRIVATE LAW

The reach of the U.S. securities laws is territorial. More frequently this is satisfied by focusing on the conduct of the parties, rather than the effects.⁴ In the case of the antifraud provision, most courts continue to be influenced by Judge Friendly's formulation in *Bersch v. Drexel Firestone, Inc.*⁵ whereby much more conduct must occur within the United States for foreign nationals to recover than if the aggrieved investors are U.S. citizens. Under this formulation, mere preparatory acts in the United States are insufficient for jurisdiction in a case involving foreign nationals where the fraudulent acts themselves occurred outside the United States.⁶

The territorial approach is also the cornerstone of the SEC's interpretation of the reach of the registration provisions of the federal Securities Act of 1933.⁷ The crucial determinant in deciding whether

4. The high water mark of the effects test is *Schoenbaum v. Firstbrook*, 405 F.2d 200 (2d Cir.), *rev'd in part en banc*, 405 F.2d 215 (2d Cir. 1968). The effects test is unsuccessful for invoking the jurisdiction of the U.S. securities laws when the complaint is that the off-shore conduct destabilized U.S. capital markets. *See, e.g.,* *Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974, 988-89 (2d Cir.), *cert. denied*, 423 U.S. 1018 (1975). The effects test may be successful where the effects are linked causally to stimulating investor behavior within the United States. *See id.* at 990-92; *see also* *Sloane Overseas Fund, Ltd. v. Sapiens Int'l Corp.*, 941 F. Supp. 1369, 1374 (S.D.N.Y. 1996) (fraudulent offering circular for the sale of convertible debt securities abroad could have an impact on common stock traded in the United States so that jurisdiction over suit was justified).

5. 519 F.2d 974 (2d Cir.), *cert. denied*, 423 U.S. 1018 (1975).

6. *See, e.g.,* *IIT v. Vencap, Ltd.*, 519 F.2d 1001, 1017-18 (2d Cir. 1975). In *Iloba Ltd. v. LEP Group, PLC*, this criterion was satisfied where the foreign purchasers established that the fraudulent representation was the failure to correct representations in a Securities and Exchange Commission (SEC) filing which was viewed as having facilitated further trading in London. 54 F.3d 118, 122-23 (2d Cir. 1995), *cert. denied*, 116 S. Ct. 702 (1996). For evidence that courts are most willing to characterize acts as being more than mere preparatory acts, *see Continental Grain (Australia) Pty., Ltd. v. Pacific Oilseeds, Inc.*, 592 F.2d 409, 419-420 (8th Cir. 1979).

7. Securities Act of 1933, 15 U.S.C. § 77a (1994).

securities must be registered is whether a security will be offered or sold "in interstate commerce."⁸ The latter is defined in the Act to include "trade or commerce in securities or any transportation or communication relating thereto . . . between any foreign country and any State."⁹ This definition is consistent with the narrow safe harbor from registration that is provided foreign issuers under the SEC's Regulation S,¹⁰ which requires that no offer or sale occur within the United States.¹¹

The U.S. approach toward the reach of its antifraud rule raises several interesting questions. As will be seen, courts have customarily taken an all-or-nothing approach. When there is sufficient conduct within the United States to justify applying the antifraud provision to the dispute, the courts have customarily assumed jurisdiction over the parties before it and applied the U.S. securities laws in resolving the dispute.¹² Conversely, the case is dismissed if the court finds there was insufficient U.S.-based conduct on the part of the defendant.¹³ Professor Robert Hillman has asked why there needs to be such an all-or-nothing approach.¹⁴ He counsels that it would be far more relevant to separate the inquiry into, on the one hand, the court's power, and its willingness to exercise that power over the parties, this being the historical question of jurisdiction, and on the other hand, its jurisdiction over the subject matter.¹⁵ Thus, it would be possible that the court could entertain the case, believing it had jurisdiction over the parties, but would resolve their dispute, not under U.S. law, but the law of the country with the most significant connection to the dispute. Recently a decision was reached that is consistent with this approach.

In *Robinson v. TCI/US West Cable Communications, Inc.*,¹⁶ the Court of Appeals for the Fifth Circuit held that the defendant had committed culpable failures within the United States that directly caused the foreign plaintiffs' losses.¹⁷ The substantial acts were a letter that the defendants had prepared in the United States which induced the

8. *Id.* § 77b(7).

9. *Id.* (emphasis added).

10. See Regulation S—Rules Governing Offers and Sales Made Outside the United States Without Registration Under the Securities Act of 1933, 17 C.F.R. §§ 230.901-904 (1997).

11. See *id.* § 230.901.

12. See, e.g., *Itoba Ltd. v. LEP Group, PLC*, 54 F.3d 118 (2d Cir. 1995), *cert. denied*, 116 S. Ct. 702 (1996).

13. See, e.g., *MCG, Inc. v. Great Western Energy Corp.*, 896 F.2d 170 (5th Cir. 1990).

14. See generally Robert W. Hillman, *Cross-Border Investment, Conflict of Laws, and Privatization of Securities Law*, 55 LAW & CONTEMP. PROB. 331 (1992).

15. See *id.* at 351.

16. 117 F.3d 900 (5th Cir. 1997).

17. See *id.* at 907.

plaintiffs to purchase the securities that later declined in value.¹⁸ Despite finding that the antifraud provision applied to the dispute, the court nevertheless dismissed the action, reasoning that England was the more convenient forum for resolving the dispute because all the facts and litigants were based there.¹⁹ The result is consistent with the bifurcated approach recommended by Professor Hillman,²⁰ provided the referent English courts apply the U.S. antifraud provision, as the Fifth Circuit believed ought to occur.

An important component in the courts' approach to deciding which country's law should apply to such a securities dispute is the inquiry into the competing social interests served by each choice facing the court. In the more typical securities case, the social interest is in the state preserving the integrity of its securities markets and protecting its residents from the harmful effects of a want of full disclosure in securities transactions. Though *Robinson* posed neither of these threats, there is a fairly well recognized social interest associated with avoiding the United States becoming something of a Barbary Coast from which the unscrupulous could launch their assaults on foreign investors.²¹ This objective, however, may well not be served by the conclusion reached in *Robinson*; the referent English court may well not apply U.S. law to the dispute. One may even imagine instances in which the foreign court applies its home-country law with the effect that investors are not protected to the same extent as they would be under U.S. securities laws.²² At the same time, *Robinson* was much influenced by established policy that litigation is better conducted on the soil of the country in which the evidence continues to be located.

The preceding well illustrates the important public character of the securities laws. As seen, the courts' willingness, indeed their power, to preside over securities-law claims is guided by the conducts test, which in turn reflects important public policy considerations. Simply put, the United States does not make its courts available to investors solely because the U.S. Marshall has served process on the defendant. In stark

18. *See id.*

19. *See id.* at 908-09.

20. *See Hillman, supra* note 14, at 333.

21. *See, e.g., Securities and Exch. Comm'n v. Kasser*, 548 F.2d 109, 116 (3d Cir.), *cert. denied*, 431 U.S. 938 (1977) ("We are reluctant to conclude that Congress intended to all the United States to become a 'Barbary Coast,' as it were, harboring international securities 'pirates.'").

22. On the subject of forum non conveniens in securities litigation, see Glenn R. Sarno, *Haling Foreign Subsidiary Corporations Into Court Under the 1934 Act: Jurisdictional Bases and Forum Non Conveniens*, LAW & CONTEMP. PROBS. Autumn 1992, 379. The criterion for deciding whether to dismiss a case on the basis of forum non conveniens is similar to that expressed in *M/S Bremen*, discussed in text at note 28, *infra*, because it focuses importantly on whether the plaintiff would be treated adversely in the alternative forum because of that forum's less favorable theories or remedies. *See Sarno, supra*, at 395.

contrast to such considerations is the heavy commitment most courts have made to parties entering into agreements setting forth not only the means (commonly arbitration) and venue (other than the United States) for resolving any dispute arising from their securities transaction, but also specifying the body of law through choice of law clauses by which any claim is to be decided.

There is now a substantial body of case law, most of it established by the Supreme Court, embracing the importance of enforcing agreements to arbitrate and forum selection clauses among private parties. As early as 1973, the Supreme Court dismissed an action under the antifraud provision, because the parties to that action had earlier agreed to arbitrate any dispute between them.²³ The suit arose from the sale of a foreign business to a U.S. buyer, and but for an agreement to arbitrate under Illinois law, only federal courts would have jurisdiction to entertain actions under the antifraud provision.²⁴ The Supreme Court's most sweeping commitment to such private arrangements occurred with its decision in *Shearson/American Express, Inc. v. McMahon*,²⁵ reversing four decades of precedent by upholding agreements to arbitrate between customers and their broker.²⁶ Indeed, the Supreme Court's acceptance of agreements to arbitrate and choice of law clauses is so sweeping, there appears to be no apparent limit on their use.²⁷

In the wake of this jurisprudence, the courts of appeal have enforced agreements to arbitrate securities claims under foreign law even though the securities transaction unquestionably occurred within the United States. Much of this law has been created in the wake of the financial difficulty experienced by the English insurer, the Society of Lloyds. Because of massive losses on asbestos and pollution liability claims for which Lloyds was the insurer, it became necessary for the first time in its history to call upon its members (Names) to fulfill their commitment to underwrite the risks insured by the syndicate. The agreement between the Names and Lloyds contained a forum selection clause, an agreement to arbitrate, and a choice of law clause. Several U.S. Names brought

23. *See* *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 519-20 (1973).

24. *See id.* at 508.

25. 482 U.S. 220 (1987).

26. *See id.* at 238. In its first treatment of the subject, the Supreme Court held that agreements to arbitrate claims under the federal Securities Act of 1933 violated the Act's antiwaiver provision. *See Wilko v. Swan*, 346 U.S. 427, 438 (1953). *McMahon*, though involving a claim under the Securities Exchange Act of 1934, nevertheless cast doubt regarding *Wilko's* continuing vitality due to *McMahon's* sweeping acceptance of arbitration. *See McMahon*, 482 U.S. at 232-33. *Wilko* was soon overruled. *See Rodriguez de Quijas v. Shearson/American Express Inc.*, 490 U.S. 477, 484 (1989).

27. For a wide-ranging critique of the Court's jurisprudence on this matter, see Paul D. Carrington & Paul H. Haagan, *Contract and Jurisdiction*, 1996 SUP. CT. REV. 331 (1997).

actions in the United States under the securities laws alleging material misrepresentations had been committed by Lloyds regarding the risks posed by the Names' investment in the insurance pools.

Relying on the Supreme Court's holding in *M/S Bremen v. Zapata Off-Shore Co.* that forum selection clauses are valid unless proven to be unreasonable,²⁸ most of the circuits²⁹ that have dealt with the various actions involving Names' suits against Lloyds have reviewed generally the rights Names would have under English law:

[F]orum selection and choice of law clauses are "unreasonable" (1) if their incorporation into the contract was the result of fraud, undue influence or overweening bargaining power; (2) if the selected forum is so "gravely difficult and inconvenient that [the complaining party] will for all practical purposes be deprived of its day in court"; or (3) if enforcement of the clauses would contravene a strong public policy of the forum in which the suit is brought, declared by statute or judicial decision.³⁰

Under this formulation, English law has not been found so lacking in protection as to overcome the presumptive validity of the choice of forum and law clauses.³¹

Forum selection and choice of law clauses such as those at issue in the Lloyds disputes always pose two quite independent questions. The threshold issue is always whether the clauses reflect a meeting of the minds between investor and issuer. In the Lloyds disputes this may well be answered affirmatively due to the presumed sophistication of the Names. Their dispute is not that of the parking patron who learns that the small print on the back of the ticket limits the garage's negligence in the bailment of the patron's automobile. By far the most fundamental question is the power of the parties to effectively remove their securities transactions from the reach of the U.S. securities laws by the fiat of their arms-length agreement. Arguments against their power to do so take two forms.

28. 407 U.S. 1, 15 (1972).

29. For cases upholding the clauses, see *Haynsworth v. Corp.*, 121 F.3d 956 (5th Cir.), *reh'g en banc denied*, 129 F.3d 956 (5th Cir. 1997); *Allen v. Lloyds of London*, 94 F.3d 923 (4th Cir. 1996); *Shell v. R.W. Sturge, Ltd.*, 55 F.3d 1227 (6th Cir. 1995); *Bonny v. Society of Lloyd's*, 3 F.3d 156 (7th Cir. 1993), *cert. denied*, 510 U.S. 1113 (1994); *Roby v. Corporation of Lloyds*, 996 F.2d 1353 (2d Cir.), *cert. denied*, 510 U.S. 945 (1993); *Riley v. Kingsley Underwriting Agencies, Ltd.*, 969 F.2d 953 (10th Cir.), *cert. denied*, 506 U.S. 1021 (1992).

30. *Bonny v. Society of Lloyd's*, 3 F.3d at 160 (citations omitted).

31. The most notable divergence from this line of cases was *Richards v. Lloyds of London*, which held that the clauses are unenforceable when the transaction has such substantial contact with the United States that public policy calls for the application of U.S. law and not foreign law to the subject matter. 107 F.3d 1422 (9th Cir. 1997), *withdrawn*, 135 F.3d 1289 (9th Cir. 1998) (*en banc*). However, the recent decision *en banc* by the Ninth Circuit brings that circuit in accord with other courts that have considered this question. *Richards v. Lloyds of London*, 135 F.3d 1289 (9th Cir. 1998) (*en banc*).

First, there is a need to protect investors from themselves. This concern applies equally to the sophisticated as well as the unsophisticated. Each are subject to the same pressures to take advantage of the offer before them which is not available absent the clauses requiring disputes be resolved in a foreign land under its laws. Importantly, from the securities perspective, the offending act—the offer of the securities with insufficient or misleading information—occurs before the investor agrees to resolve any dispute under another country's laws. Thus, the agreement can be seen as not a *waiver* of the protection of the U.S. securities laws, but a post-violation agreement about how the parties choose to resolve any claim arising from the violation. So viewed, the contract overcomes the orthodox interpretations of the antiwaiver provisions contained in both the Securities Act³² and the Exchange Act.³³ One obvious problem with this approach is it assumes the parties are aware a violation has occurred when they enter into the agreement. Such is not the case so that antiwaiver orthodoxy appears not to be satisfied in these cases. Absent knowledge that a violation has occurred, it is difficult to treat the forum selection and choice of law clauses as conscious substitutions of those rights for the manner of vindicating claims provided by the U.S. securities laws. This approach also is inconsistent with the very purpose for which the U.S. securities laws make private rights of action available to investors.

There is no doubt that the philosophy underlying the securities laws' express and implied causes of action are to assure compliance with the fundamental requirements of full and fair disclosure. The most extreme upholding of forum selection and choice of law clauses would be one that relegated U.S. investors to a foreign law when the issuer and its underwriters have offered a security for sale in the United States without seeking either its registration, or qualifying for an exemption from registration. Under U.S. laws, investors purchasing the security have an unqualified right to rescind their purchase.³⁴ Clearly the foreign land, even if it be England, would not demand the same level of disclosure or afford the same limited exemptions as exist under the Securities Act. Though this may well be the basis for concluding the investors would face "unreasonable" burdens in the foreign land, this is by no means clear in the examples of England or many other countries that provide reasonably comprehensive securities regulatory schemes. However, fundamental and unique policies are embedded in the Securities Act that are not replicated under the laws of, for example, England, and vice

32. Securities Act of 1933 § 14, 15 U.S.C. § 77n (1994).

33. Securities Exchange Act of 1934 § 29(a), 15 U.S.C. § 78cc(a) (1994).

34. *See* Securities Act of 1933 § 12(a)(1), 15 U.S.C. § 77l.

versa. It is in the fulfillment of those policies that the Securities Act provides sweeping rescission rights to investors who purchase securities that were neither registered, nor qualified for an exemption from registration. Similar policy rationales underlie assuring that investors enjoy protection under both the Securities Act and the Exchange Act when their sellers commit fraud in the sale of the security. The unknowing waiver of their rights through acceding to the demands of a forum selection and choice of law clause, therefore, can hardly be seen as fulfilling the policies sought to be served by providing investors with private causes of action when those underlying policies are violated.

A second basis for rejecting any sweeping acceptance of forum selection and choice of law clauses is the macroeconomic effects of doing so. The purpose of securities laws transcends the protection of widows, widowers, and orphans. The U.S. securities laws were enacted in the aftermath of the Great Depression and their history and content were much influenced by our experience and faith that fair and orderly markets are a cornerstone for not just economic stability, but social stability.

This grand vision is broader than the individual claims or needs of investors. For example, a major focus of capital market regulation is to enhance allocational efficiency within the economy. Thus, disclosure assumes importance not just because it will protect the investor from the unscrupulous issuer, but also because it protects other issuers who may be less favored in the marketplace because they choose to play by the rules, whereas those competing against it for capital do not. Thus, a major focus of disclosure is to provide a basic information package about issuers so that investors may wisely compare, if they choose, the promise of one against that of another. Similarly, sharp practices by promoters of securities are condemned because they raise the cost of capital for all issuers. This occurs in the now familiar scenario whereby investors cannot *ex ante* identify the scrupulous from the unscrupulous and so discount each security by the estimated cost of fraud averaged across all issuers. The securities laws seek to reduce the amount of this discount by reducing the number of unscrupulous promoters, issuers, and the like. Private arrangements that remove parties and transactions from the U.S. securities laws are very much in conflict with the purposes for which the securities laws were created. Such agreements balkanize U.S. capital markets so that some transactions are regulated with the more demanding standards of the U.S. securities laws while others are not. The consequence is much like that predicted by Gresham's Law—private agreements drive out wiser and more broadly formulated public law. It is hard to understand how any uniform judgment can thus be made of the integrity of such a market.

III. THE CHARACTERIZATION PROBLEM

A threshold consideration in the orthodox choice of law problems is that of characterization of the issue under review. We cannot resolve whether a problem involves the vindication of a public or private right until we first resolve what problem or goal is to be served by the laws or regulations that are competing to be applied to a transaction. This facet of the puzzle facing securities regulators is no better illustrated than in the instance of insider trading regulation. Here we may also see terrific tension in the choice between the "effects" and "conduct" approaches to application of the antifraud provision.

Securities law orthodoxy holds that the law of the country where the trade occurred applies to determine whether there is a violation of insider trading laws. Professor Merritt Fox argues that insider trading should be regulated exclusively by the country of the corporation's domicile, regardless of where the violation occurred.³⁵ He reasons that in the face of much disagreement over whether and why insider trading is harmful, any proscription is best reposed exclusively in the governments that represents those to be regulated.³⁶ Thus, in the Supreme Court's recent decision, *United States v. O'Hagan*,³⁷ Professor Fox would permit only the United Kingdom to prosecute Mr. O'Hagan for his wrongful use of information he misappropriated in the United States from his British client. The overall appeal of this approach depends on both the home country and the host market concurring on the purpose of proscribing insider trading.

Elsewhere I have examined closely the many rationales for insider trading regulation.³⁸ There we find that there are many possible justifications that can be invoked for insider trading regulation. Many of the justifications for insider trading regulation focus exclusively on perceived national interests served in protecting host markets from

35. See Merritt B. Fox, *Insider Trading in a Globalizing Market: Who Should Regulate What?*, LAW & CONTEMP. PROB. Autumn 1992, 263, 294-95.

36. See *id.* at 299.

37. 117 S. Ct. 2199 (1997). Such a standard may, of course, simply invite creative circumventions by eager U.S. courts and prosecutors who could be expected to reason, for example, that the abuse was not against the law firm's client, the British corporation Grand Metropolitan, but against the law firm such that the United States had sufficient interest to apply its insider trading laws.

38. See James D. Cox, *Insider Trading and Contracting: A Critical Response to the "Chicago School,"* 1986 DUKE L.J. 628. [hereinafter Cox, *Insider Trading and Contracting*]; James D. Cox, *Insider Trading Regulation and the Production of Information: Theory and Evidence*, 64 WASH. U.L.Q. 475 (1986).

abuses believed to accompany insider trading.³⁹ Under this view, insider trading regulation most assuredly would serve even the most restrictive view of the effects and conduct tests for the application of the host country's securities laws.⁴⁰ On the other hand, there are ample grounds to view insider trading regulation from a purely private perspective of policing the principal-agent relationship so that most certainly the law of the corporation's domicile should apply.⁴¹ To the extent that commentators vary so widely in their views regarding why insider trading should be regulated, such differences most assuredly will be repeated among national securities regulators so that it is unlikely that any consensus will develop that the sole regulator for insider trading should be the corporation's domicile and not a host market. Equally significant here is the important signaling that occurs by international corporations subjecting themselves to the more demanding scrutiny and regulation of U.S. capital markets. That is, issuers have multiple reasons for obtaining a secondary market for their shares; one such purpose is to provide, for example, in the case of obtaining a secondary listing on the New York Stock Exchange, greater protection from abusive market practices for investors seeking an ownership interest in the listed foreign company.

Insider trading regulation, though subject to a good deal of dispute regarding why there is any regulation, nevertheless is far simpler in the characterization issues it poses than in the case of takeover regulation. Professor Karmel reviews four countries' takeover regimes in which we find a rich mixture of regulatory provisions. There are disclosure rules that can best be understood as offering protection for the benefit of the target corporation's shareholders. Disclosure rules, as the rich history of the Williams Act well illustrates, also have a powerful secondary purpose, namely facilitating defensive steps by issuers.⁴² Thus, should

39. Professor Fox is dismissive of such concerns. See Fox, *supra* note 35, at 296 (reasoning that the sole conflict of interest that insider trading poses is that which can be addressed through home-country laws aimed at policing self-interested behavior). However, he fails to consider that insider trading can cause managers to engage in behavior that is harmful to trading markets such as delayed or misleading disclosure practices that are carried out to further the insider's trading agenda. See Cox, *Insider Trading and Contracting*, *supra* note 38, at 637 (reasoning that insider trading regulation can be justified as a meaningful prophylaxis to such misconduct).

40. See Donald C. Langevoort, Schoenbaum *Revisited: Limiting the Scope of Antifraud Protection in an Internationalized Securities Marketplace*, LAW & CONTEMP. PROBS. Autumn 1992, 241.

41. See Cox, *Insider Trading and Contracting*, *supra* note 38, at 653-55.

42. Here we will note the early warning disclosures compelled by § 13(d)(1) of the Securities Exchange Act of 1934, 15 U.S.C. § 78m(d)(1), which requires extensive disclosures by those whose ownership of a reporting company's shares exceeds five percent of that class. And when disclosures are made, they are also the subject of equitable actions by the target as well as other bidders who seek to gain a strategic advantage through the suit. See 15 U.S.C. § 78r(a) (1994).

we see such rules only as laws of the shareholders' domicile, or are they not also to be seen as conscious efforts by the target company to bring itself into another set of regulatory provisions by obtaining a secondary listing in the host country?⁴³ To ignore the latter appears to place undue emphasis on where the corporation obtained its first listing and does not place sufficient emphasis on the consideration of why it sought a secondary listing.

Takeover rules also announce a country's baseline policy for changes in control. Again, consider the various rules promulgated by the SEC under the Williams Act regarding the duration of tender offers,⁴⁴ withdrawal rights,⁴⁵ and pro rata acceptance rules.⁴⁶ Collectively, they embrace procedures that shape the process for the target's auction rather than to permit the swift "Saturday night specials" that coerce target shareholders and deny other suitors a chance to enter the bidding.⁴⁷ Again, we might ask whether the company that seeks a listing in the United States does not wish to have any future takeover regulated by a blend of the laws of its domicile as well as that of the United States. And, some rules exist for the fair treatment of shareholders such as the Williams Act's "all holders" rule⁴⁸ and the automatic bid rule imposed by the City Code of London.⁴⁹ These rules become an important component of the shareholders' contract with their corporation. It would seem that the contract is not less so if it appears to arise from two sets of rules, one in London and another in the United States.

Within each of the above characterizations of the protective provisions one finds in takeover laws, there is a good deal of freedom that one can achieve through self-help. Thus, securities regulatory practices that embrace, for example, an auction philosophy for transfers of control are subject to further change through either the issuer issuing "rights plans," which severely restrict the free conduct of an auction for

43. As should be clear from the reasoning employed above, the foreign issuer examined here is one who consciously brings itself within the scope of the securities laws by seeking a listing on an exchange or NASDAQ. Those who inadvertently are subject to SEC reporting provisions are excluded from my reasoning here primarily because they also are excluded from most of the Williams Act which only applies to companies that are subject to the reporting provisions of § 12. *Id.* § 78*l*. Inadvertent companies are exempt from this provision if they make their home-country filings. *See* Rules and Regulations Under the Securities Exchange Act of 1934, 17 C.F.R. § 240.12g3-(2)(b) (1997).

44. *See* 17 C.F.R. § 240.14c-2(a).

45. *See id.* § 240.14d-7.

46. *See id.* § 240.14d-8.

47. *See generally* Peter Cramton & Alan Schwartz, *Using Auction Theory to Inform Takeover Regulation*, 7 J.L. ECON. & ORG. 27 (1991); Lucian A. Bebchuck, *The Case for Facilitating Competing Tender Offers*, 95 HARV. L. REV. 1028 (1982).

48. *See* 17 C.F.R. § 240.14d-10.

49. *See* City Code on Take-overs and Mergers, Rule 9.1, *supra* note 3, at 7060.

control or incorporating in a jurisdiction with an effective antitakeover statute. It is generally understood that the impact of such a poison pill is to insert the target corporation's board of directors into the path of the bidder seeking to become an auctioneer. State law antitakeover statutes also illustrate that the law of the corporation's domicile, regardless of the country in which its shares are traded, can further qualify host market policies for the transfer of control.

There appears no reason to simply view the issuer's decision to seek a secondary listing as being other than a decision to subject itself and all those who trade in its securities to the policy choices of the host market. The variable characterizations that we can give to takeover provisions, with their conflicting policy objectives, the freedom of the target corporation to alter the rules for its acquisition, such as through the issuance of a poison pill, and the freedom of the bidder to circumvent burdensome requirements by how it chooses to structure its bid, do make the task of the international securities lawyer a more challenging one. We should at this stage be reluctant to simplify that task with a blind quest to apply a single law to a multi-market transaction.⁵⁰

IV. CONCLUSION

It would appear that a far wiser strategy than to embrace a simplifying choice of law rule that the law of the corporation's domicile should govern questions such as insider trading or takeover practices, for example, is to recognize that securities law is very much public law. Similarly, it is bad public policy to empower parties in their private securities transactions to choose the law of the country that will regulate their dealings. As seen above, a country's securities laws permit it to formulate important public policy about how capital shall be deployed within its borders. This is not an idle consideration; it very much relates to the capital formulation process within the host country as well as its own sense of values. Here we might point to the restrictive view held in the United States of who is a wrongful tipper. In *Dirks v. Securities and Exchange Commission*,⁵¹ the Supreme Court held that a tip is made improperly only when made to a relative, friend, or with the expectation of a pecuniary reward from the selective disclosure.⁵² None of the countries reviewed by Professor Karmel so restrict the scope of who is a tipper; the reason is that the United States values more so than do the

50. Such a single law approach is recommended in Merritt B. Fox, *Securities Disclosure in a Globalizing Market: Who Should Regulate Whom*, 95 MICH. L. REV. 2498, 2582-83 (1997).

51. 463 U.S. 646 (1983).

52. *See id.* at 663-64.

United Kingdom, Germany, or Australia the aggressive pursuit of confidential information by market analysts.⁵³ It affronts U.S. capital markets and more generally established U.S. policy to allow a foreign state to prosecute analysts who act lawfully in transmitting information their diligent investigative efforts have produced. This, however, would be the effect of conditioning insider trading regulation on the situs of the corporation's domicile, rather than the market in which the trading occurred.

What is the best regulatory approach is a matter over which great differences exist and will persist. And, this is a matter that is very much influenced not solely by local values, but values that are informed in turn by cultural and practical considerations which vary across countries. It appears far wiser to encourage an environment of regulatory competition with a healthy respect for the costs to local investors, securities issuers, and the national gross domestic product when regulations stray far from the practices that prevail in rival markets, as well as the freedom of businessmen to artfully structure transactions to avoid regulations they believe impose costs in excess of their benefits. This approach embraces not simply the hand of the regulator, but also the hand of businesses to choose their regulatory domicile. Those who reside in London do so with a healthy respect for the automatic bid rule. They can escape that rule by relocating their market to New York; they can also supplement that rule by choosing a secondary listing in the United States. It seems myopic to overlook this, as some would advise, by preferring a predictable and simple rule that only the law of the country's domicile should apply. Certainly the real world is not such a simple place.

53. *See id.* at 658.