11-0397-cv(L),

11-0403-cv(CON), 11-0416-cv(CON), 11-0418-cv(CON),
11-0428-cv(CON), 11-0447-cv(CON)

United States Court Of Appeals

for the

Second Circuit

VIKING GLOBAL EQUITIES LP, VIKING GLOBAL EQUITIES II LP, VGE III PORTFOLIO LTD., PARCENTRAL GLOBAL HUB LIMITED, ELLIOTT INTERNATIONAL, L.P., THE LIVERPOOL LIMITED PARTNERSHIP, ELLIOTT ASSOCIATES, L.P.,

(caption continued on inside cover)

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF OF THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION AND THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICI CURIAE* SUPPORTING DEFENDANTS-APPELLEES

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Plaintiffs-Appellants,

– versus –

PORSCHE AG WENDELIN WIEDEKING,

Defendant,

PORSCHE AUTOMOBILE HOLDINGS SE, FKA Dr. ING. H.C. F. PORSCHE AG, WENDELIN WIEDEKING, HOLGER P. HAERTER,

Defendants-Appellees.

RULE 26.1 CORPORATE DISCLOSURE STATEMENT

Amici curiae the Securities Industry and Financial Markets Association and the Chamber of Commerce of the United States of America state that they are not subsidiaries of any corporation, and no publicly held corporation owns more than 10% of their stock.

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TABLE OF AUTHORITIES

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The Securities Industry and Financial Markets Association ("SIFMA") and the Chamber of Commerce of the United States of America (the "Chamber") respectfully submit this brief as *amici curiae* in support of affirmance of the District Court's order dismissing appellants' third amended complaint for failure to state a claim.

STATEMENT OF INTEREST OF THE *AMICI CURIAE*[1]

SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit www.sifma.org. SIFMA has long played an active advocacy role in addressing the potential extraterritorial application of private rights of action under Section 10(b), including in *amicus* briefs submitted in *Morrison v. National Australia Bank Ltd.*, No. 07-0583 (2d Cir. 2008), *Morrison v. National Australia Bank Ltd.*, No. 08-1191 (U.S. 2010), and other cases and in comment letters to the U.S. Securities and

[1] Under Fed. R. App. P. 29(c)(5), SIFMA and the Chamber certify that no party's counsel authored this brief in whole or in part; no party or party's counsel contributed money intended to fund the preparation or submission of the brief; and no person other than SIFMA and the Chamber contributed money intended to fund the preparation or submission of the brief.

Exchange Commission (the "SEC"). As a leading advocate in this field, SIFMA has a perspective that the parties to this appeal do not represent.

The Chamber is the world's largest business federation, directly representing 300,000 members and indirectly representing the interests of over three million business, trade, and professional organizations of every size, in every business sector, and from every region of the country. The Chamber regularly files *amicus curiae* briefs in cases, such as this one, that raise issues of importance to the business community. The Chamber's members transact business around the globe. To that end, the Chamber has filed numerous amicus briefs addressing extraterritorial application of U.S. laws, including amicus briefs jointly submitted with SIFMA in *Morrison v. National Australia Bank Ltd.*, No. 07-0583 (2d Cir. 2008) and *Morrison v. National Australia Bank Ltd.*, No. 08-1191 (U.S. 2010).

As advocates for global securities and business interests, SIFMA and the Chamber bring a unique perspective to the proceeding, including an assessment of the ramification of the Court's decision on national and transnational capital transactions and business relations.

PRELIMINARY STATEMENT

This case presents a critical challenge to the Supreme Court's recent decision in *Morrison v. National Australia Bank*, 130 S. Ct. 2869 (2010). That decision expressly prohibited extraterritorial application of implied rights of action

under Section 10(b) of the Securities Exchange Act (the "Exchange Act"). Plaintiffs in this case, however, bring an action against a *foreign* person for alleged misstatements and omissions regarding securities of a *foreign* issuer traded on a *foreign* securities exchange – based merely on allegations that plaintiffs signed confirmations of swap transactions with unnamed third parties in the United States.

The District Court properly rejected this effort to skirt the Supreme Court's holding in *Morrison*, a holding grounded in the text of the federal securities laws, longstanding principles of comity, and well-recognized policy dangers associated with overbroad application of U.S. private rights of action. Authorizing private rights of action based merely on "references" in swap agreements against foreign entities *not party to those swap agreements* would effectively extend Section 10(b)'s extraterritorial scope beyond that permitted for purchases and sales of the underlying foreign securities, with adverse consequences for U.S. and international capital markets.

Nothing in the Exchange Act supports adopting a broader territorial scope for actions under Section 10(b) based on swap agreements than for actions based on transactions in the underlying securities. On the contrary, when Congress enacted legislation to apply Section 10(b) rules and precedents to securities-based swap agreements, it made explicit that it was doing so only "to the same extent as they apply to securities." In other words, as in the case of the securities

transactions addressed in *Morrison*, "there is no affirmative indication in the Exchange Act that §10(b) applies extraterritorially" to swap agreements – and the presumption against extraterritorial application must prevail.

Moreover, extension of private rights of action under Section 10(b) extraterritorially based on mere "references" in swap agreements would pose particularly acute and heightened policy concerns, given the magnitude and arbitrariness of the potential litigation exposure. Non-U.S. defendants have no ability to control – or even to be aware of – the number or size of the swap agreements that hedge funds or other market participants may execute, with unnamed third parties, involving foreign securities. The transactions are not public and their "notional amount" (which is theoretically unlimited) may well exceed the market value of all of a company's outstanding shares. Non-U.S. issuers would have to assume that U.S. laws would apply to their conduct in any securities market, and that the only way to protect themselves against potentially massive liability would be to keep themselves (and their investments and access to capital markets) wholly outside the United States. In other words, the likelihood that private rights of action will conflict with foreign regulatory regimes and U.S. economic interests is even greater here than in the case of the securities transactions addressed in *Morrison*.

The imposition of U.S. policy choices regarding private rights of action on activities outside the United States will deter foreign investment in the United States and threaten international comity and regulatory cooperation, as recognized in numerous submissions by foreign governments and others in *Morrison* and other contexts. Congress, not the courts, has the responsibility to assess the important and sensitive policy ramifications of altering *Morrison*'s limitations on extraterritorial application of the securities laws. Indeed, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") has specifically called upon the SEC to conduct a study and make recommendations regarding the need for legislation on those very issues – and it is only through that process, not creative litigation theories, that *Morrison*'s holding may be altered.

ARGUMENT

POINT I

EXPANDING SECTION 10(b)'S EXTRATERRITORIAL APPLICATION BASED ON "REFERENCES" IN SWAP TRANSACTIONS WOULD HAVE SERIOUS ADVERSE POLICY IMPLICATIONS AND FALLS SOLELY WITHIN THE AUTHORITY OF CONGRESS

The novel extraterritorial application of Section 10(b) sought in this action would have adverse policy ramifications for the U.S. economy and would deter foreign investment in the United States. Expanding private litigants' ability to bring claims in U.S. courts for activities involving foreign securities beyond the limits set in *Morrison* would substantially increase the risk of expensive and

potentially abusive litigation for foreign companies – and thereby discourage cross-border economic activity involving the United States.

This action represents just such an effort to exceed *Morrison*'s limits. It tries to recover losses resulting neither from "transactions in securities listed on domestic exchanges [nor] domestic transactions in other securities." *Morrison* at 2884. Rather, it seeks to assert a claim against a foreign company, Porsche, to recover losses relating to shares of another foreign company, Volkswagen, traded on a foreign exchange – based simply on the allegation that plaintiffs signed confirmations in the United States for swap transactions that "refer" to those foreign securities. This action thus risks precisely the harm to the U.S. economy and foreign investment that proper application of *Morrison* would preclude.

A. Extraterritorial Application of Securities Laws Threatens International Investment in the U.S. Economy.

The U.S. Supreme Court, foreign governments, U.S. governmental authorities, academics and industry leaders have all recognized the dangers of extraterritorial application of U.S. securities laws. European companies have ranked "fear of legal action" as the second-largest barrier to investing in the United States. *See* U.S. Dep't of Commerce, Int'l Trade Admin, Assessing Trends and Policies of Foreign Direct Investment in the U.S., 7 (2008). Exposure to U.S. securities litigation, it is well understood, could cause "[o]verseas firms with no other exposure to our securities laws [to] be deterred from doing business here."

Stoneridge Inv. Partners, LLC. v. Scientific-Atlanta, Inc., 552 U.S. 148, 164 (2008).

Specifically, exposure to the risk of U.S. private securities actions "discourag[es] foreign investment in United States businesses[,] inhibit[s] cross-border capital flows[,] . . . raises the cost of doing business in the U.S. and could deter corporations from operating within the U.S. or participating in U.S. financial markets." Br. of the United Kingdom of Great Britain and Northern Ireland as *Amicus Curiae* in Supp. of Resp'ts at 25-26, *Morrison v. National Australia Bank Ltd.*, 130 S. Ct. 2869 (2010) (No. 08-1191) ("U.K. *Morrison Amicus* Br."); *see also* Comments from Australian Gov't to SEC ¶ 24 (Feb. 18, 2011) (on file with SEC), *available at* http://www.sec.gov/comments/4-617/4617-34.pdf ("Australia Comments") (extraterritorial application "will inevitably lead to higher compliance costs for Australian firms with even a minimal nexus that might establish personal jurisdiction in the United States."). For these reasons, extraterritorial application of U.S. securities laws "will cause [foreign] companies to reduce their U.S. contacts further, such as by terminating (or declining to establish) sponsored ADR programs, or limiting their investor communications programs in the United States." Letter from Susannah Haan, Sec'y Gen., EuropeanIssuers, to Elizabeth M. Murphy, Sec'y, SEC at 3 (Feb. 18, 2011) (on file with SEC), *available at* http://www.sec.gov/comments/4-617/4617-10.pdf.

Private securities actions present a unique potential for vexatious litigation, including "strike suits, and protracted discovery, with little chance of reasonable resolution by pretrial process," *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 1105 (1991), such that "if not adequately contained, [the private right of action] can be employed abusively to impose substantial costs on companies and individuals whose conduct conforms to the law." *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*, 551 U.S. 308, 313 (2007). Private securities action "disruptively expos[e] foreign corporations to a litigation environment in which plaintiffs arguably have undue leverage." John C. Coffee, Jr., *Global Class Actions*, Nat'l Law J., June 11, 2007, at 12. For example, U.S. plaintiffs can impose substantial discovery burdens on defendants, use opt-out class action mechanisms, and face low fee risks as they are not subject to a "loser-pays" rule and can make contingency fee arrangements with their attorneys; none of these advantages are available to securities plaintiffs in most other jurisdictions. *See Morrison*, 130 S. Ct. at 2885-86; Australia Comments ¶ 20; Letter from Catherine Bergeal, Dir. of Legal Affairs, Ministry of the Econ., Fin., and Indus. of Fr., to Mary L. Schapiro, Chairman, SEC at 4 (Feb. 17, 2011) (on file with SEC), *available at* http://www.sec.gov/comments/4-617/4617-29.pdf ("France Comments").[2]

[2] *See also* City of London Law Soc'y & The Law Soc'y of Eng. and Wales, Extra-Territorial Application of Securities Fraud Provisions at 3 (February 2011) (on file with SEC), *available at* http://www.sec.gov/comments/4-617/4617-35.pdf

Additionally, the "unpredictable specter of private litigation in U.S. courts" can undermine the "effectiveness of any action by a foreign regulator." U.K. *Morrison Amicus* Br. at 24.

B. Extraterritorial Application of Section 10(b) Creates the Risk of Potentially Massive and Arbitrary Liabilities, Unforeseeable by Foreign Defendants.

Extension of Section 10(b) private actions extraterritorially based on "references" to foreign securities in swap agreements poses particularly acute and heightened policy concerns, given the magnitude and arbitrariness of the potential litigation exposures. The risk of liability based on references in swap agreements far exceeds the exposure for transactions in the underlying securities – and, indeed, is theoretically unlimited. The "notional amount" of swap agreements is unconstrained by the actual number of the issuer's outstanding shares. Swap

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("English Law Societies Comments") ("Private litigation in the US in this context has in the past resulted in conflicting and inconsistent decisions that frustrate informed decision-making and the efficient allocation of capital resources. The differences in the legal and regulatory environment of the issuer and the markets in which its securities are traded relative to US norms serves only to magnify the risk posed by potential litigation."); Letter from David S. Hirschmann, President and CEO of Ctr. for Capital Mkts. Competitiveness and Lisa A. Rickard, President of U.S. Chamber Inst. for Legal Reform, to Elizabeth M. Murphy Sec'y, SEC at 2 (Feb. 18, 2011) (on file with SEC), *available at* http://www.sec.gov/comments/4-617/4617-37.pdf ("The vast majority of other nations—many of them our closest allies—have declined to adopt the U.S. model of private securities litigation, and in particular our country's authorization of 'opt-out' securities class actions. . . . Significantly, the doubts that other nations have expressed about the wisdom of the U.S.'s litigation system are consistent with a growing body of empirical evidence about the inefficacy of that system as applied in our country—and its harmful consequences.").

market participants thus can enter into transactions with "notional" exposures of billions of dollars, potentially far exceeding any exposures arising out of ordinary capital raising or trading activities in the underlying shares. These massive additional exposures are entirely unpredictable and completely outside the control of potential defendants.

Swap transactions reflect unilateral trading decisions of hedge funds and other private market participants. Foreign issuers have no way to know, much less to limit, the extent to which U.S. persons may wish to enter into swaps "referencing" their foreign securities. Market participants may enter into swap agreements – and thus create potential litigation exposure – even where a foreign issuer makes no effort at all to access U.S. securities markets. Indeed, the potential for liability extends even more broadly to non-U.S. persons who, as in this case, are not even the issuers of the securities "referenced" in the swap agreement, nor even alleged to have made any statements about a security traded in the United States.

The massive and arbitrary exposures that would arise from Section 10(b)'s extraterritorial application based on "references" in swap agreements would create a substantial disincentive to U.S. investment by foreign companies. As appellants acknowledge, defendants could only protect themselves against liability by remaining wholly outside the personal jurisdiction of the United States.

Appellants' Br. at 28-29. In other words, the price of opening U.S. factories, investing in U.S. subsidiaries and accessing U.S. capital markets (through stock market listings or otherwise) would be the risk of potentially unlimited liability to unrelated private actions, with a widely recognized potential for abuse, arising out of swap transactions wholly outside the non-U.S. parties' awareness and control. Not only is it hard to imagine that Congress could have intended this result – particularly without a word of debate – but *Morrison* expressly prohibits that conclusion absent a legislative statement sufficiently clear to rebut the longstanding presumption against extraterritorial application of U.S. law. *Morrison*, 130 S. Ct. at 2881-82.

The result appellants seek, in fact, is exactly that which the *Morrison* court abhorred – creating a global "Shangri-La" for securities class actions in which anyone operating in any securities market worldwide would need to act as if U.S. securities law applies, *id.* at 2886, because it is unforeseeable whether a private party will enter into a swap agreement with unnamed third parties that could create very substantial and indeterminate liabilities in relation to the underlying foreign security.

C. Congress Alone Has Authority to Make the Policy Determination to Expand Extraterritorial Application of the Section 10(b).

Congress, not the courts, has responsibility for making the sensitive and important policy determination of whether to extend extraterritorial application of

the private right of action beyond *Morrison*'s bounds. *See id.* at 2881. Notably, under the Dodd-Frank Act, Congress has specifically called for the SEC to conduct a study and make recommendations regarding the extraterritorial scope of the private right of action under Section 10(b). Dodd-Frank Act, Pub. L. 91-190, § 929Y, 124 Stat. 1376, 1871 (2010). Consistent with its statutory mandate, the SEC has solicited public input regarding this issue, including seeking information on the implications of extraterritorial application on international comity and "the costs . . . to domestic and international financial systems and securities markets." Study on Extraterritorial Private Rights of Action, Exchange Act, Release No. 63,174, 75 Fed. Reg. 66,822, 66,824 (Oct. 25, 2010). To date, the SEC has received over sixty comments from foreign governments, foreign trade associates and scholars, among others. The SEC must report its recommendations to Congress by January 21, 2012. Dodd-Frank Act § 929Y.

It is through the legislative process, in this case Congress acting with the benefit of informed study by an expert agency, and not creative litigation theories that the issue of whether to extend liability beyond *Morrison* should be addressed – particularly given the magnitude of the potential exposures and economic impact at a time of major challenges to U.S. and global markets.[3]

[3] The potential damage from extraterritorial application of U.S. securities laws is amplified by current economic trends showing that foreign direct investment in the United States is on the decline and U.S. capital markets have become less

POINT II

EXTRATERRITORIAL APPLICATION OF PRIVATE RIGHTS OF ACTION UNDER SECTION 10(b), BASED ON MERE "REFERENCES" IN SWAP AGREEMENTS, CANNOT BE RECONCILED WITH *MORRISON* OR PRINCIPLES OF COMITY ESSENTIAL TO EFFECTIVE INTERNATIONAL REGULATORY COOPERATION

A. *Morrison* Established a Bright-Line Rule Against Extraterritorial Application of Securities Laws.

Applying the "longstanding principle . . . that legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States," *Morrison* reviewed the Exchange Act and concluded, unambiguously: "there is no affirmative indication in the Exchange Act that §10(b) applies extraterritorially, and we therefore conclude that it does not." *Morrison*, 130 S. Ct. at 2877, 2883 (internal quotation marks omitted). The Court

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competitive globally. *See* Letter from Kevin M. Carroll, Managing Dir. and Assoc. Gen. Counsel of Secs. Indus. and Fin. Mkts. Ass'n, and Lorraine Carlton, Managing Dir. and Gen. Counsel of Ass'n for Fin. Mkts. in Eur., to Elizabeth M. Murphy Sec'y, SEC at 8 (Feb. 18, 2011) (on file with SEC), *available at* http://www.sec.gov/comments/4-617/4617-15.pdf ("Although there was a slight improvement in 2008 and 2009, 'by nearly all measures, the U.S. capital market today remains 'much less competitive than it was historically.' For example, the U.S. percentage of global IPOs – widely viewed as an indicator of the relative competitiveness of capital markets – has rapidly decreased in the last 10 years, with the United States capturing a paltry 2.7% of global IPO activity in the first quarter of 2010. The United States' position as the most attractive destination for foreign investment has also eroded since the late 1980s: foreign investment in the United States 'in 2009 totaled $152.1 billion, down by more than 50 percent compared to the $319.7 billion in 2008.'") (internal citations omitted).

summarized, "When a statute gives no clear indication of an extraterritorial application, it has none." *Id.* at 2878.

Building on principles of international comity, the Court expressly rejected "the notion that the Exchange Act reaches conduct in this country affecting exchanges or transactions abroad." *Id.* at 2885. The Court expressed concern with "the interference with foreign securities regulation that application of § 10(b) abroad would produce." *Id.* at 2885-86 ("[T]he regulation of other countries often differs from ours as to what constitutes fraud, what disclosures must be made, what damages are recoverable, what discovery is available in litigation, what individual actions may be joined in a single suit, what attorney's fees are recoverable, and many other matters."). Therefore, "[t]he probability of incompatibility with the applicable laws of other countries is so obvious that if Congress intended such foreign application it would have addressed the subject of conflicts with foreign laws and procedures." *Id.* at 2885 (internal quotation marks omitted).

Relying on the presumption against extraterritorial application and in deference to comity concerns, *Morrison* created a bright-line rule prohibiting the application of private rights of action to foreign-traded securities: "Section 10(b) reaches the use of a manipulative or deceptive device or contrivance *only* in connection with the purchase or sale of a security listed on an American stock

exchange, and the purchase or sale of any other security in the United States." *Id.* at 2888 (emphasis added).

B. Extraterritorial Application of U.S. Securities Laws Based on "References" in Swap Agreements Cannot Be Squared with the *Morrison* Rule.

This case presents an unprecedented attempt, contrary to *Morrison*'s mandate, to extend the Exchange Act to conduct *outside* the United States "affecting exchanges or transactions abroad." *Id.* at 2885. The complaint seeks relief arising out of statements made by a *foreign* person regarding securities traded on a *foreign* exchange. Specifically, appellants allege that Porsche, a German company, made fraudulent statements about its intentions regarding the shares of another German company, Volkswagen, which are traded on the German securities market. Dist. Ct. Op. at 4-6, 12. The only connection to the United States was a transaction unrelated to Porsche or the Volkswagen shares: appellant hedge funds allege that they signed confirmations for swap agreements in the United States that used the price of the Volkswagen shares as a "reference." *Id.* at 1-2, 3-4. These swap agreements were "privately negotiated" and, in their complaint, appellants did not identify the specific swap agreements on which they base their claims or disclose the counterparties to the swap agreements. *Id.* at 3, 4.

As the District Court recognized, application of the Exchange Act in these circumstances would have Section 10(b) govern all statements made by anyone

anywhere in the world regarding a foreign security listed and traded outside the United States – based merely on a U.S. person's unilateral decision to enter into a swap transaction that "refers" to the foreign security. Dist. Ct. Op. at 10 (adopting appellants' theory "would extend extraterritorial application of the Exchange Act's antifraud provisions to virtually any situation in which one party to a swap agreement is located in the United States."). But "*Morrison*'s presumption against extraterritoriality" and its "strong pronouncement that U.S. courts ought not interfere with foreign securities regulation without a clear Congressional mandate" made the District Court wary of "creat[ing] a rule that would make foreign issuers with little relationship to the U.S. subject to suits here simply because a private party in this country entered into a derivatives contract that references the foreign issuer's stock." *Id.* at 13 (internal citations omitted).

There is no question that, had appellants entered into transactions in Volkswagen shares directly on the "referenced" German market, *Morrison* would preclude their action under Section 10(b). *See In re Royal Bank of Scot. Grp. plc Sec. Litig.*, 765 F. Supp. 2d. 327, 337 (S.D.N.Y. 2011) (investor's U.S. residence is irrelevant); *Cornwell v. Credit Suisse Grp.*, 729 F. Supp. 2d 620, 625-26 (S.D.N.Y. 2010) (investor's U.S. citizenship is irrelevant); *Plumbers' Union Local No. 12 Pension Fund v. Swiss Reinsurance Co.*, 753 F. Supp. 2d 166, 179 (S.D.N.Y. 2010) (purchaser's U.S. citizenship and residence are irrelevant). There plainly would be

no "transactions in securities listed on domestic exchanges [nor] domestic transactions in other securities." *Morrison* at 2884. Yet appellants contend that their unilateral decision to enter into a private swap agreement "referencing" Volkswagen shares should produce a different result – rendering Porsche (and every other non-U.S. defendant) potentially subject to suit under Section 10(b) despite the longstanding doctrines against extraterritorial application of U.S. law cited in *Morrison*. If anything, however, the extraterritorial application of U.S. law under the circumstances of this case creates even greater risk to international comity than under the facts of *Morrison* itself.

C. Extraterritorial Application of Private Actions Based on Mere "References" in Swap Agreements Cannot Be Reconciled with the Principles of International Comity Recognized in *Morrison*.

Exporting private rights of action to all foreign activities based on mere "references" in U.S. agreements would, as in the case of transactions in the underlying securities in foreign markets, undermine foreign governments' ability to make independent policy choices regarding the regulatory and enforcement remedies available in their securities markets. *Id.* at 2885-86. As numerous foreign governments have noted in submissions to the SEC for purposes of its Dodd-Frank Act study and to the Supreme Court as *amici* in *Morrison*, the U.S. regulatory regime is not the sole global remedy for fighting securities fraud. Different jurisdictions can and do offer alternative private and other remedies to

aggrieved investors, many of which are viewed as preferable to the private right of action under Section 10(b), which has proven highly controversial even in the United States. *See, e.g.*, Letter from Klaus Botzet, Legal Advisor and Consul Gen., Embassy of the Fed. Republic of Ger., to Elizabeth M. Murphy, Sec'y, SEC at 2 (Feb. 18, 2011) (on file with SEC), *available at* http://www.sec.gov/comments/4-617/4617-12.pdf ("Germany now fears that" the "extraterritorial application of U.S. private rights of action" may "potentially seriously hamper Germany's proven and internationally well-balanced regulatory system."); France Comments at 4 ("allowing private plaintiffs to sue for securities fraud that takes place outside the United States would interfere with the ability of foreign nations to regulate their own securities markets and manage their economies."); Australia Comments ¶ 6 ("private legal actions in the United States seeking to impose liability on foreign companies for actions outside the United States that allegedly injured foreign investors risk[] undermining the legal and regulatory regimes established by foreign governments.").[4]

[4] *See also, e.g.*, English Law Societies Comments at 2-3 ("The fact that all governments recognise that greater regulation is essential for the smooth functioning of financial markets does not mean that it must be uniform or under the surveillance of one body in order to function. Extraterritorial application of US law has the potential to damage international relations irreparably by ignoring the sovereignty of other states and sending the message that other states' legislation is inferior or inadequate.").

Considerations of comity are particularly important, moreover, in light of the increasingly international nature of challenges facing global securities markets and economies more generally. The need for effective international regulatory cooperation requires particular care in respecting the policy determinations of other jurisdictions rather than unilateral imposition of U.S. rules on securities markets around the world. In the view of foreign sovereigns, "U.S. judicial interference in [their securities regulatory] decisions risks damaging the mutual respect that comity is meant to protect and could be perceived as an attempt to impose American economic, social and judicial values," ultimately "undermining . . . global regulatory cooperation." U.K. *Morrison Amicus* Br. at 22-24; *see also Morrison*, 130 S. Ct. at 2886 (foreign governments and trade associations "all complain of the interference with foreign securities regulation that application of § 10(b) abroad would produce.").

These concerns with comity and effective international regulatory cooperation, recognized by the *Morrison* court and foreign governments, do not arise solely in the context of purchases and sales of securities in non-U.S. markets. Indeed, they are exacerbated in the context of swap transactions "referencing" foreign securities, since extraterritorial application of U.S. law would turn solely on unilateral decisions by U.S. persons outside the knowledge or control of non-

U.S. persons, including non-U.S. regulatory authorities.[5] Further, there would be nothing that potential foreign defendants or their regulators could do to prevent U.S. litigation (short of avoiding general jurisdiction over the defendants), thereby depriving non-U.S. authorities of any ability to ensure the viability of competing remedial and regulatory regimes.

POINT III

NOTHING IN THE EXCHANGE ACT SUPPORTS EXTRATERRITORIAL APPLICATION OF SECTION 10(b) IN THE CONTEXT OF SWAP TRANSACTIONS

The Exchange Act offers no basis for construing Section 10(b) more broadly in the context of swaps than in the context of purchases and sales of foreign securities. Under *Morrison*, as noted above, plaintiffs could not bring an action under Section 10(b) for short sales of the foreign securities whose price allegedly was affected by the foreign defendants' statements or omissions in this case. *Morrison*, 130 S. Ct. at 2888. Indeed, appellants here dismissed their claims for short sales of Volkswagen securities that they allege were subject to Porsche's fraud. Appellants' Br. at 5. Nonetheless, appellants seek to proceed with an action that would not be permitted with respect to their short sales, based merely on their

[5] Even apart from concerns regarding international comity, "[e]lementary considerations of fairness dictate that individuals should have an opportunity to know what the law is and to conform their conduct accordingly." *Caiola v. Citibank, N.A.*, 295 F.3d 312, 327 (2d Cir. 2002).

having entered into swap transactions that "refer" to the same foreign securities. Their theory is advanced without any allegation that the foreign defendants – or indeed that any foreign person – had any involvement with those swap transactions.

Nothing in Section 10(b) supports this effort to expand the Exchange Act's territorial reach beyond *Morrison* based on the unilateral decision of a U.S. person to enter into transactions through a swap rather than to execute directly in the foreign market. On the contrary, both the text of the Commodity Futures Modernization Act ("CFMA") – the statute adding swap agreements to Section 10(b) – and its legislative history demonstrate that Congress intended parties to swap agreements to stand in a position no better than those transacting in the underlying securities.

A. The CFMA's Text Makes Clear That No Broader Extraterritorial Application Was Intended for Swap Agreements than for Securities.

The CFMA amended Section 10(b)'s antifraud provisions, which previously had not applied to swap agreements, to provide that "[r]ules promulgated under subsection (b) of this section that prohibit fraud . . . and judicial precedents decided under subsection (b) of this section and rules promulgated thereunder that prohibit fraud . . . shall apply to security-based swap agreements . . . *to the same extent as*

they apply to securities." 15 U.S.C. § 78(j) (emphasis added).[6] Not only does the statutory language give no "clear indication of an extraterritorial application," as would be required under *Morrison*, 130 S. Ct. at 2878, it expressly confirms that Congress intended the scope of liability to be no greater than for the underlying securities.

B. The CFMA's Legislative History Further Evidences the Lack of Any Intent to Extend Extraterritorial Swap Liability More Broadly than for Securities.

Consistent with the amended text of the Exchange Act, the legislative history of the CFMA confirms the lack of any Congressional intent to expand extraterritorial liability for swap agreements more broadly than for the underlying securities. Rather, Congress intended the CFMA to prevent circumvention of existing rules applicable to securities transactions through the use of swap agreements referencing those securities. One of the CFMA's architects, Senator Paul Sarbanes, explained that under the CFMA "current and future anti-fraud rules will apply to swap agreements to the same extent as they do to securities . . . [to] enhance protection for investors and for the financial markets, and [to] permit the SEC to respond as necessary to developments in these markets." 146 Cong. Rec. 11,947 (daily ed. Jan. 2, 2001).

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[6] "Security-based swap agreement[s]" include "a swap agreement . . . of which a material term is based on the price, yield, value, or volatility of any security or any group or index of securities, or any interest therein." CFMA § 301(a).

Congressional testimony on prior versions of the CFMA, which excluded over-the-counter derivatives from regulation under the federal securities laws, further confirms this legislative intent. The Secretary of the Treasury explained that it should not be possible for an individual "who would be legally prohibited [under Section 10(b)] from buying a stock or buying an option to be able to engage in a total return swap that was the functional equivalent of buying that stock."[7] He specifically noted, in response to questions, the need to "craft the minimal set of provisions that assures that there will not be circumvention of the existing regulatory protections with respect to the factors that we have enumerated – insider trading, manipulation, fraud, and protection of retail investors." *Id.* at 31.

This Congressional objective – preventing the use of swaps "referencing" securities to engage in misconduct that would be prohibited in transactions involving the securities themselves – is wholly consistent with the extraterritorial limitation adopted by the District Court. There is no risk that the prohibitions of Section 10(b) could be circumvented through the use of a swap agreement if the Section 10(b) did not apply to the underlying securities transactions. Moreover, the CFMA amendments apply only to *security-based* swaps – not swaps on

[7] Joint Hearing before the Committee on Agriculture, Nutrition and Forestry, United States Senate, and the Committee on Banking, Housing and Urban Affairs, One Hundred Sixth Congress, Second Session, on S. 2697, The Commodity Futures Modernization Act of 2000, 106th Cong. 14 (2000).

commodities or other financial instruments not already governed by Section 10(b) – thereby further belying any suggestion that the amendments were intended to expand the scope of Section 10(b) based on mere "references" to foreign or other instruments in the contracts of private parties.

CONCLUSION

For the foregoing reasons, the *amici* respectfully submit that the decision of the District Court dismissing this action for failure to state a claim should be affirmed.

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Respectfully submitted,

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CERTIFICATE OF COMPLIANCE WITH RULE 32(a)

This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) as modified by Fed. R. App. P. 29(d) because it contains 5,554 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word version 2007 in 14-point Times New Roman.

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