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# SECURITIES REGULATION AND THE FOREIGN ISSUER EXEMPTION: A STUDY IN THE PROCESS OF ACCOMMODATING FOREIGN INTERESTS

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This article has three aims. It describes, in the minimum detail needed to make the matter clear to nonspecialists, the regime created by statute and administrative action governing securities regulation and the foreign issuer;<sup>1</sup> it essays a few critical comments on that regime; and it explores the administrative process by which the current arrangement was created. From such a process study we may learn about the ways, values and dangers of subjecting transnational financial and commercial activity to local regulation.

The regulation of business enterprises whose activities interest more than one state is not easily reducible to general legal norms. One common but somewhat sterile preliminary characterization of transnational regulation concerns the nature of the hold the regulating

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<sup>1</sup> A detailed but not always clear resumé of the present SEC regulation of foreign issuers subject to § 12(g) of the Securities Acts Amendments of 1964, 15 U.S.C. § 78C(g) (Supp. 1967), amending 15 U.S.C. § 78C (1964), Exchange Act of 1934, added by 78 Stat. 566 (1964), 15 U.S.C. § 78C(g) (1964) is contained in Goldman & Magrino, *Foreign Issuers and Section 12(g) of the Securities Exchange Act of 1934*, 23 Bus. Law. 135 (1967) [hereinafter cited as Goldman & Magrino]. The current situation can best be understood when viewed against the legislative history of the 1964 Amendments and the originally proposed regulation; see Phillips & Shipman, *An Analysis of The Securities Acts Amendments of 1964*, 1964 DUKE L.J. 706, 754-62 [hereinafter cited as Phillips & Shipman].

A brief overview of the current picture is also found in H. STEINER & D. VAGTS, *TRANSNATIONAL LEGAL PROBLEMS* 967-73 (1968). This, however, concentrates upon the "extraterritoriality" of the regulation, as do the earlier comments (on the first proposed regulatory scheme) of Stevenson, *The Effect of the New SEC Registration Requirements on Foreign Issuers*, in N.Y.S. BAR ASS'N, *ADDRESSES AT MEETING OF BANKING, CORP'N & BUS. L. SECTION 8* (Feb. 3, 1966) [hereinafter cited as Stevenson]; The Committee on International Law of the Ass'n of the Bar of the City of N.Y., *The 1964 Amendments to the Securities Exchange Act of 1934 and the Proposed Securities and Exchange Rules—International Law Aspects*, 21 RECORD 240 (1966). See also Note, *The Proposed SEC Regulations for Foreign Over-the-Counter Securities: A Delicate Step Forward in the Evolution of Disclosure*, 6 VA. J. INT'L L. 326 (1966); W. Kronstein, *Publizitätspflicht ausländischer Aktiengesellschaften in USA*, 11 AUSSENWIRTSCHAFTSDIENST DES BETRIEBS-BERATERS 432 (1965). The former is a detailed, the latter a summary review of the proposed regulation before its modification.

state attempts to obtain over such activities. To use Anglo-American concepts, there is a superficial distinction between attempts to gain jurisdiction over the person in order to force obeisance to orders of omission or commission, and attempts to obtain and destroy the "thing" that is causing harm to protectible interests.<sup>2</sup> At times this distinction may suggest the propriety or impropriety of a given response. If inflammable textiles are imported by a State Regulating dealer buying from a State Transacting enterprise, their seizure under a health and safety regulation of and in the former state would be generally accepted; an attempt to impose sanctions upon the exporting enterprise might not be. The power to achieve the latter step is not questioned in Anglo-American law,<sup>3</sup> even if service of process limitations force use of quasi-in-rem jurisdictional principles to allow the seized goods to substitute for the enterprise in matters of judgment satisfaction. The propriety of attempting to hold the person, however, depends not upon abstract principles of jurisdiction but upon such substantive questions as the extent and directness of the enterprise's efforts to exploit the State Regulating market with defective wares. In any event, the suggested distinction is often meaningless for quite a different reason. The seizure of the "thing"—amounting finally to a closing of the foreign market to the enterprise—may well be so painful to the enterprise that it will accept personal orders of omission or commission as the preferable alternative.<sup>4</sup>

It is also difficult to categorize transnational activities on the basis

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<sup>2</sup> For a thorough review and analysis of these jurisdictional concepts, see Trautman, *The Role of Conflicts Thinking in Defining the International Reach of American Regulatory Legislation*, 22 OHIO ST. L.J. 586 (1961). See also, in the domestic context, von Mehren & Trautman, *Jurisdiction To Adjudicate: A Suggested Analysis*, 79 HARV. L. REV. 1121 (1966).

<sup>3</sup> This statement assumes that in the area of economic regulation the defensive territorial, or protective, principle applies, and that current customary rules of public international law do not prohibit municipal legislation of the sort discussed in the text. See RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 18(b) (1965). See also the limited reach of § 33, *Id.*

It is possible, however, to argue that an excessively aggressive use of this legislation is wrong; whether wrong as a matter of comity or as an "abuse of right" (and thus illegal as a matter of international law) is a matter of some doubt. See note 44 *infra*. I do not believe, however, that more protection of legitimate foreign interests is available through such concepts than through the "open process" approach discussed in the following text.

<sup>4</sup> See Magnusson, *The Need for International Agreement on Obtaining Evidence From Foreign Countries*, 26 FED. B.J. 232 (1966) for examples of "hard line" reactions to regulatory conflicts that would be unimpeachable under traditional legal concepts. A recent example is the pronouncement of directly conflicting regulatory orders involving the North Atlantic Westbound Freight Association (production of documents); see *Financial Times*, Aug. 30, 1968, at 8, col. 6.

of their factual distinctions. Yet one might usefully define three types of transnational operations in the expectation that the legal principles applicable in guiding efforts at supervision will vary depending on which of the three types of operations best characterizes the activities to be supervised: (1) An enterprise of State Transacting is present in State Regulating and acts there in ways legally analogous to the ways it acts in State Transacting, although not necessarily with the same degree of intensity. An example is the creation of a manufacturing and sales subsidiary in State Regulating. (2) An enterprise of State Transacting carries on activities from which it expects profits to be generated out of State Regulating in a reasonably direct fashion. For example, the enterprise sells goods to State Regulating importers or merchants (perhaps through a sales subsidiary there, perhaps directly), or it seeks to raise capital on the State Regulating financial market. (3) An enterprise of State Transacting, as a result of essentially local activities, indirectly and inadvertently affects interests that the law of State Regulating wishes to protect. For example, products whose quality is dubious enough to generate products liability in State Regulating but not in State Transacting may be sold by the enterprise to local third parties who independently export them to State Regulating. A second example would be the investment by State Regulating brokers in securities of a State Transacting enterprise, made originally through purchases in the latter state but eventually resulting in trading in those securities by State Regulating investors.

At times the transnational nature of the conflict will benefit the dealing parties; State Regulating for overriding "political" reasons may soften its position if State Transacting prohibits the commission of acts State Regulating deems desirable.<sup>5</sup> This heightened confrontation, however, only confirms that it is in the evaluation of the relative importance of substantive interests that most of the conflicts find their resolution.

In the arena of state resolution of transnational financial and commercial activity the role of the lawyer is to identify material interests, to evaluate arguments of the legitimacy of those interests, and to rank them in making arguments for honest and defensible policy decisions. In an ideal world, inductively generalized principles would give the policy maker the tools for doing this work efficiently. But in this field—where events are sporadic, relatively rare, enormously dif-

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<sup>5</sup> Good examples are the hassles over the production of documents familiar from antitrust cases, and the occasional disputes over certain restrictive practices (or acts corrective thereof) in antitrust litigation.

ferentiated and complicated, involve high stakes, and as a result of all this are highly politicized—generalizations have a habit either of being uselessly vague or of hiding direct, conclusory positions. If generalizations can ever be useful, they will at least have to be derived from the study of events such as the one here to be described.

## I

### THE PROBLEM

The Securities Act of 1933 and the Securities Exchange Act of 1934 govern the issuance of securities, the trade in securities (including the functioning of the various markets and the professionals acting therein) and certain aspects of the continuing relationship between issuers and their security holders. The regulatory scheme is stringent and complex and, at least so far as trading in securities is concerned, of growing and uncertain scope, particularly because of the expanding role of civil liability for fraudulent trading. From the standpoint of an issuer of securities, the important provisions are those imposing a number of registration and reporting requirements, a set of duties involving the solicitation of proxies from shareholders, and automatic civil liability for short-swing trading in securities by certain "insider" groups.<sup>6</sup> All these burdens, however, only arise following one or the other of two controllable events: A primary distribution of the issuer's stock on the American capital market in order to raise capital here, or the voluntary listing of a class of the issuer's stock on a national exchange in order to enjoy an orderly trading market in the United States.

With the passage of the Securities Acts Amendments of 1964,<sup>7</sup> this situation changed. The mentioned burdens were thereby imposed upon issuers with gross assets of at least one million dollars and with at least one class of equity securities held by five hundred or more shareholders. The decision of coverage is no longer directly within the control of any issuer, and thus the obligations mentioned are imposed rather than accepted. The original acts and the 1964 amendments apply to foreign as well as domestic issuers. The reasons for extending coverage, however, are not necessarily the same for the two groups. In recognition of this consideration, in 1964 the Securities and Ex-

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<sup>6</sup> Securities Exchange Act of 1934, § 13, 15 U.S.C. § 78m (1964); § 14, 15 U.S.C. § 78n (1964); § 16, 15 U.S.C. § 78p (1964).

<sup>7</sup> 78 Stat. 565 (1964), 15 U.S.C. §§ 77b-77h, 78c-78s (1964).

change Commission was again given almost unlimited power to create exemptions for foreign issuers.<sup>8</sup>

## II

### THE EXEMPTION STORY

Immediately after the passage of the 1964 legislation, the SEC granted foreign issuers an exemption from the requirement of an initial section 12(g) registration until November 30, 1965;<sup>9</sup> during 1965 this exemption was extended to November 30, 1966.<sup>10</sup> Since the registration obligation, under the statutory system, only arises 120 days after conclusion of a fiscal year, it became effective no earlier than April 1, 1967. In the meantime the SEC issued its regulations as to substantive coverage and exemptions. It did this by publishing "proposed regulations" in November 1965,<sup>11</sup> following approximately one year of informal but intensive discussions with interested foreign parties, ranging from personal interchanges at the SEC offices to diplomatic notes.<sup>12</sup> Such activity continued during 1966 and substantial changes were discussed during that year as well.<sup>13</sup> The modified regulations went into effect on April 28, 1967, slightly late but with a dispensation for any company forced into late disclosure as a result of the delay.<sup>14</sup>

These regulations, which cover only the registration process, provide that registration is not required if there are less than three hundred shareholders (of a world-wide total of at least five hundred shareholders) of a class of securities resident in the United States. If the foreign securities are not directly owned but are deposited in exchange for American Depositary Receipts, no registration duty is

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<sup>8</sup> Securities Exchange Act of 1934, § 12(g)(3), 15 U.S.C. § 78C(g)(3) (1964). For a full review of the history of this exemption and its legislative road, see Phillips § Shipman, *supra* note 1, at 754-55.

<sup>9</sup> SEC Securities Exchange Act Release No. 7427 (Sept. 15, 1964); Rule 12g3-1, 17 C.F.R. § 240.12g3-1 (1968).

<sup>10</sup> SEC Securities Exchange Act Release No. 7867 (Apr. 21, 1966).

<sup>11</sup> SEC Securities Exchange Act Releases Nos. 7746-49 (Nov. 16, 1965); Proposed rule 12g3-2 was the most important of the rules and forms suggested for adoption.

<sup>12</sup> See Goldman & Magrino, *supra* note 1, at 137.

<sup>13</sup> The SEC has available for inspection at its headquarters a large file, "Letters Of Comment On Proposed Rules And Forms Relating To Foreign Issuers," containing comments upon the proposed rules (invited by the Commission in Nov. 1965 Releases that followed an October meeting with industry representatives), dated late 1965 and early 1966.

<sup>14</sup> SEC Securities Exchange Act Release No. 8066, at 2 (Apr. 28, 1967).

imposed upon the latter as such, consonant with earlier established practice,<sup>15</sup> but individual holdings of ADRs are counted with holdings of foreign share certificates in calculating the three hundred shareholders in those cases where both forms co-exist.<sup>16</sup>

Registration is the event that normally triggers the other obligations and liabilities already mentioned: Periodic financial and operational report requirements, proxy solicitation requirements, and insider trading sanctions. In addition, failure to register when required could give rise to sanctions not only against the issuer but, more importantly, against the securities themselves in the sense of outlawing their trade and subjecting dealers therein to separate sanctions. These results, which need not automatically follow, are the subject of later discussion.

A full accommodation to foreign interests has been reached as to the proxy solicitation requirements and the insider trading disabilities. The effect of the SEC regulation is simply to exempt those foreign issuers and insiders putatively subject to registration from the operation of sections 14 and 16 of the 1934 Act which impose those burdens.<sup>17</sup>

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<sup>15</sup> See note 67 *infra* and accompanying text. If there are 300 ADRs, however, the underlying shares are to be "registered." For a description of the American Depository Receipt, see in addition to authority cited in notes 35 & 37 *infra*, Moxley, *The ADR: An Instrument of International Finance and a Tool of Arbitrage*, 8 VILL. L. REV. 19 (1962).

<sup>16</sup> Rule 12g3-2(a)(1), 17 C.F.R. § 270.12g3-2(a)(1) (1968). Although rule 12g3-2(c) separately exempts ADRs from § 12(g), the provision of (a)(1), counting as separate "holders" each separate customer account of a dealer who holds nominal title to the foreign security can be read as including ADRs. The practical consequences of reading the rule to include ADR holders may not be too important, since a foreign issuer usually authorizes an ADR operation whenever the volume of domestic trading warrants it; nevertheless, the same issue is occasionally found in both ADR and normal form.

The lower numbers-count for foreign issuers, compared with the domestic minimum of 500, has been criticized as discriminatory. Reh binder, *Publizität Und Auslandsbeziehungen*, in *DAS UNTERNEHMEN IN DER RECHTSORDNUNG—FESTGABE FÜR HEINRICH KRONSTEIN* 203, 210 (1967) [hereinafter cited as Reh binder]. It derives from § 12(g)(4), which maintains § 12(g) status for a domestic company once caught (*i.e.*, once having met the 500 shareholder test) until the count drops below 300, but is patently, if not significantly, discriminatory when compared with that domestic scheme. Proving that the 300 holder requirement has been reached may be difficult, especially in the case of bearer shares. Phillips & Shipman, *supra* note 1, at 756-57.

<sup>17</sup> This was achieved in 1966 through the adaptation of the earlier identical exemption, available to foreign issuers since 1935, to the new § 12(g) scheme. Rule 3a12-3, 17 C.F.R. § 240.3a12-3 (1968). Technically, the exemption is available to issuers registering under § 12(g) (authorized to file on Form 20, 17 C.F.R. § 249.220 (1968), the § 12(g) form). Presumably, the shift of the SEC, detailed below, to an exemption in lieu of, rather than upon, registration obviates the need to order specifically the further exemptions from §§ 14 and 16, under which the issuers and insiders involved would otherwise fall. Query, whether the failure of such issuers to comply with the below-described conditions for obtaining the § 12(g) exemption will also subject them to the

This result was in a sense dictated by history, as the SEC has long granted the same dispensation to voluntary foreign registrants and issuers seeking national exchange listing, groups whose subjection to these sections would seem a fortiori required before section 12(g) companies should be so treated.<sup>18</sup> In consequence, foreign issuers subject to section 12(g) at the outset have faced only the duty of disclosing the information required by the registration statement and by the periodic reporting obligations. Even here a major accommodation has been made. Section 12(g) companies are now by rule exempted from that section if they furnish the Commission certain initial and recurrent information.<sup>19</sup> These pseudo-registration disclosures are to some extent patterned after those required for voluntary registration of securities upon application for issue permits or for trading on a national exchange. Although these filings normally include a large amount of relevant financial and operational information, submissions required of foreign issuers under the 1964 Amendments are limited to information the issuer: (1) Is by the law of its domicile required to make public there, (2) files with any stock exchange on which its securities are traded if that exchange makes the information public, or (3) voluntarily distributes to its security holders.<sup>20</sup> Even these submissions, since they

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reach of §§ 14 and 16, and more relevantly, to the private action exposure that their presumed violations of these provisions will create. The doubt centers upon the wording of rule 3a12-3: "Securities for which the filing of registration statements on Form 20 . . . is authorized shall be exempt from the operation of Section 14 and 16 of the [Securities Exchange] Act. . . ." Miscreant issuers only lose the exemption from § 12(g). See rule 12g3-2(b)(1), 17 C.F.R. § 270.12g3-2(b)(1) (1968). If they then file, do they and their insiders still enjoy the exemption of rule 3a12-3? If, as is likely, they do not file, have they taken themselves out of the exemption?

<sup>18</sup> As to both, see rules 3a12-3, 17 C.F.R. § 240.3a12-3 (1968), and rule 14a-2(d), 17 C.F.R. § 240.14a-2(d) (1968); 2 L. LOSS, *SECURITIES REGULATION* 794 n.30, 874, 1110 (2d ed. 1961). A recent explanation of the purposes of these exemptions is found in *Hearings on H.R. 6789 Before a Subcomm. of the House Comm. on Interstate and Foreign Commerce*, 88th Cong., 1st Sess., pt. II, at 179 (1963).

<sup>19</sup> Rule 12g3-2(b)(1), 17 C.F.R. § 240.12g3-2(b)(1) (1968).

<sup>20</sup> *Id.* The major procedural difference between the originally proposed rule (SEC Securities Exchange Act Release No. 7746 (Nov. 16, 1965)) and that finally adopted is the elimination of a filing requirement under § 12(g) in favor of an exemption from § 12(g)'s filing requirement once certain information is "furnished to" the Commission. The substantive change in terms of information required is minor. Originally, at least a balance sheet and profit-and-loss statement of the latest fiscal year, a description of the issuer's business, and a review of holders' rights under the registered securities were to be filed, in addition to the information still required, described in the text. Why the minor safeguard entailed in ensuring that so much was included in the "home country standard" was dropped is not clear; there was no significant objection to the originally framed substantive scope of the registration requirement. See Stevenson, *supra* note 1, at 12; Rehinder, *supra* note 16, at 210.

might include a flood of trivia, are further reduced by a definition of relevant information.

The periodic reporting obligations under section 13 of the 1964 Act, which for a domestic issuer are triggered by the involuntary initial registration, are eliminated entirely for the foreign issuer. Normally section 13 (as implemented by SEC rules) requires annual and semi-annual reports, and current reports upon the happening of such events as changes in the control of the registrant, major asset changes, changes in the terms of securities or increase or decrease thereof, and the like. So far as involuntarily "registering" foreign issuers are concerned, the current report requirement has been dropped by the SEC in favor of a simplified approach requiring annual reporting of otherwise covered events only to the extent required for initial "registration."<sup>21</sup> At least equally important, neither "registration" nor "reporting" is subject to the rigorous American accounting format imposed by Regulation S-X.<sup>22</sup> Failure of a foreign issuer to meet these requirements will, of course, trigger the applicability of section 12(g), and with it the applicability of section 13 (reporting requirements), and perhaps of sections 14 (proxy solicitation) and 16 (insider trading). How these swords, and the one penalizing a failure to register, are to fall upon foreign issuers is not clear. It is not clear that the exemption from sections 14 and 16, granted by rule 3a12-3, ends when section 12 has been violated;<sup>23</sup> nor is it clear how these consequences are to be brought home to the foreign issuer.

The benefits of this modified regulatory scheme, after much pulling and hauling, have also been extended to other North American foreign issuers. The historical discrimination against Canadian issuers rested as much upon the extensive participation of United States capital in Canadian enterprise as it did upon the freewheeling nature of the Canadian investment market.<sup>24</sup> The improvement of regulatory

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<sup>21</sup> Rule 12g3-2(b)(1), 17 C.F.R. § 240.12g3-2(b)(1) (1968). Originally, an annual balance sheet and profit-and-loss statement were required; again it is unlikely that these will not be forthcoming under the basic reporting requirement (which is identical with the basic "submission") and equally puzzling why the safeguard nonetheless assuring their availability was dropped.

<sup>22</sup> 17 C.F.R. § 210 (1968). For the details of the varied and partial exemptions from its requirements that have been available to some foreign issuers, see RAPPAPORT, *SEC ACCOUNTING PRACTICE AND PROCEDURE* 26.25-42 (2d rev. ed. 1966); see also 1 L. Loss, *supra* note 18, at 366-68.

<sup>23</sup> See note 17 *supra*.

<sup>24</sup> See 3 L. Loss, *supra* note 18, at 1995-2004; Cohen & Throop, *Investment of Private Capital in Foreign Securities*, in *A LAWYER'S GUIDE TO INTERNATIONAL BUSINESS TRANSACTIONS* 519, 594-96 (W. Surrey & C. Shaw eds. 1963); Note, *Enforcing United States Securities Regulation Against Canadians: Conflict of Laws Problems*, 66 *HARV. L. REV.* 1081 (1953).

controls at the provincial and to some extent the federal level has changed the latter situation; and this may account for the SEC's decision to drop the original proposal, which required full compliance with registration and reporting duties and imposed the proxy solicitation and insider trading sanctions.<sup>25</sup> Some of the remaining slack may be taken up by the new provision that precludes enjoyment of the modified scheme in the case of "essentially United States" issuers—companies the stock of which is more than fifty per cent in United States hands and the business of which is administered principally in the United States or by United States directors.<sup>26</sup> All such issuers remain section 12(g) companies, and are subject to sections 13, 14, and 16.

Finally, a description of the sanction mechanism is in order. The exemption from the onerous (and United States-system oriented) proxy solicitation requirements and insider trading disabilities has already been mentioned. The only statutory civil liability for false disclosures in the registration and reporting statements is that of section 18 of the 1934 Act, which imposes liability upon the maker for damages suffered by any person who relied upon a false and misleading statement, contained in a registration statement or other filed document, in purchasing or selling a security at a price that was affected by such statement.<sup>27</sup> As weak as the section 18 weapon is, the SEC has attempted to remove even this basis for liability by the ingenious step of proclaiming that the documents submitted by the involuntary foreign registrant shall be deemed not filed for section 18 purposes.<sup>28</sup> Well-considered doubt was expressed as to the validity of this exemption when the proposed regulation still required a section 12(g) registration but on a form calling for less than normally required information.<sup>29</sup> The 1964 Amendments permit the SEC to exempt foreign

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<sup>25</sup> The rationale of the SEC in originally proposing continued full application of its requirements to Canadian issuers was not designed to achieve that purpose and is, if anything, more consonant with the final result:

"This policy is based upon the similarity between business and accounting practices in those countries [Canada, Mexico and Cuba] and those in the United States, as well as upon the greater familiarity of nationals of such countries with United States requirements." Securities Exchange Act of 1934 Release No. 7746 (Nov. 16, 1965).

<sup>26</sup> Rule 12g3-2(e), 17 C.F.R. § 240.12g3-2(e) (1968).

<sup>27</sup> 48 Stat. 897, as amended, 15 U.S.C. § 78r (1964).

<sup>28</sup> Rule 12g3-2(b)(4), 17 C.F.R. § 240.12g-2(b)(4) (1968). That such statutory provisions can sometimes be rejuvenated, see *Heit v. Weitzen*, 402 F.2d 909 (2d Cir. 1968), and more generally, *Escott v. Barchris Constr. Corp.*, 283 F. Supp. 643 (S.D.N.Y. 1968).

<sup>29</sup> Shipman, *Two Current Questions Concerning Implied Private Rights of Action Under the Exchange Act: Authority of the Administrative Agency to Negate; Existence for Violation of Self-Regulatory Requirements*, 17 CASE W. RES. L. REV. 925, 937-39, 948-60 (1966).

issuers from the entire registration-with-sequels scheme of section 12,<sup>30</sup> but do not seem to permit alteration of the regime of the basic 1934 Act once registration, with or without sequels, is imposed by the agency. Thus it may still be an open question whether these objections remain valid under the new "information in lieu of registration" scheme.

The legal justification (as distinguished from the business justification) for the SEC exemption from sections 14 and 16 is more clearly legitimate, since these sections are in the main statements of affirmative duties of issuers and "insiders" which the Commission has decided are not appropriate to the policing of foreign issuers. The private rights of action created by the two sections enforce these affirmative duties and can only arise if the affirmative duties are imposed and then not honored.<sup>31</sup> Section 18, however, is purely a private right of action, declared by law to arise whenever sections 12 and 13 are affirmatively violated. It does not seem likely that the SEC, by a regulation not based upon specific delegation of authority to do so, can negate an express statutory right of private action. In any event the issue is almost academic, given the unsuitability of section 18 as a weapon of private recovery.<sup>32</sup> Lurking in the background is the more menacing and not wholly imaginary horror of rule 10b-5, whose uncertain reach may extend to the trade in foreign securities,<sup>33</sup> even granting the power of the SEC to preclude this result by promulgating specific regulatory exemptions from the rule.

There are, of course, other sanctions available under the overall

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<sup>30</sup> Section 12g(3), its original reverse reading (statutory exemption with power in the SEC to revoke it) and its significance in this respect are discussed in Phillips & Shipman, *supra* note 1, at 754-55.

<sup>31</sup> See Shipman, *supra* note 29, at 945-48.

<sup>32</sup> See 3 L. Loss, *supra* note 18, at 1751-54.

<sup>33</sup> Compare Schoenbaum v. Firstbrook, 268 F. Supp. 385 (S.D.N.Y. 1967), and Kook v. Crang, 182 F. Supp. 388 (S.D.N.Y. 1960), with Ferraioli v. Cantor, 259 F. Supp. 842 (S.D.N.Y. 1966), and SEC v. Gulf Intercont'l Fin. Corp., 223 F. Supp. 987 (S.D. Fla. 1963). The cases are not directly comparable, treating respectively substantive and procedural jurisdiction (see Ferraioli v. Cantor, *supra*, at 845 n.4), but are nevertheless revealingly different in their attitude toward the problem. See Note, 69 COLUM. L. REV. 94 (1969); Note, *supra* note 24, at 1089 n.65. See also Roth v. Fund Of Funds, Ltd., 279 F. Supp. 935 (S.D.N.Y. 1968); Fontaine v. SEC, 259 F. Supp. 880 (D.P.R. 1966); Order Accepting Offer of Settlement, SEC Securities Exchange Act Release No. 8083 (May 23, 1967), reprinted in 6 INT'L LEGAL MAT'L 412 (1967). In the domestic context, see Mansfield Hardwood Lumber Co. v. Johnson, 268 F.2d 317 (5th Cir.), cert. denied, 361 U.S. 885 (1959) (law of forum governs scope of foreign corporation's directors' duty of disclosure where forum was seat of many corporate transactions); Note, *Conflict of Laws—Duty of Director of Foreign Corporation to Shareholder Held Governed by Law of Forum When Corporate Activity Centers in Forum*, 108 U. PA. L. REV. 742 (1960).

regulatory system presently in effect. The SEC may sue to prevent violations of the Act, or to enforce duties imposed by the Act and its regulations. The procurement of in personam jurisdiction over the necessary foreign parties, assuming the substantive reach of the law, should not be more difficult than obtaining in personam jurisdiction over foreign parties generally. The more potent weapon available to the SEC is its potential jurisdiction over the trade and traders in foreign securities or in American Depository Receipts whose issuers, whether as non-feasants or malfeasants, are not performing the above-described duties. In particular, dealers in these securities, under pain of disciplinary proceedings and the concomitant creation of private damage actions, can be forced to desist from handling such securities or at least to disclose the deficiencies and violations as a condition of trading.<sup>34</sup> Indeed, the SEC has the power to order dealers to warn investors that they are buying securities the information on which does not reach "American" standards even when the issuer thereof is in full compliance with the statutory and regulatory requirements.<sup>35</sup> Finally, of course, there is the intangible but effective sanction of public disclosure of violations. SEC regulations in particular and American practice in general permit the citation of chapter and verse to an extent unknown in most European countries. What of all this panoply the SEC has in fact decided to use will be discussed later. All in all, however, an evaluation of the accommodation reached can for the moment assume that methods exist to assure that the accommodation will be honored and can concentrate upon its substance.

### III

#### CRITIQUE

Such a review should consider both the substantive interests involved on each side and the process by which these interests are identified and weighed.

Although there is no uniform "foreign issuer" position, particularly if United States trade in Canadian securities is included under

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<sup>34</sup> Securities Exchange Act of 1934, § 15, as amended, 15 U.S.C. § 78o(c)(1) (1964); see 3 L. Loss, *supra* note 18, at 1791-92.

<sup>35</sup> See Proposed Rule 15c1-10, SEC Securities Exchange Act Release No. 7746 (Nov. 16, 1965). It was, "at the present time," not adopted; SEC Securities Exchange Act Release No. 8066, at 3 (Apr. 28, 1967). For a narrative review of the SEC attitude toward the problem, see Brownell, Cohen, Heller, Loss & Stevenson, *Legal Problems of Issuing and Marketing Foreign Securities in the United States*, in *INTERNATIONAL FINANCING AND INVESTMENT* 430, 447-50 (J. McDaniels ed. 1964).

that label, the arguments of agents of the German companies affected by the 1964 Amendments seem representative enough for discussion.<sup>36</sup> Their major claim was that the issuers were not voluntarily entering the United States securities market for purposes of primary distribution, but were caught by the 1964 Amendments because of independent transactions by unrelated investors or dealers.<sup>37</sup> This point is central to any discussion of the obligations that such issuers seek to avoid. As a result it is important to differentiate between those obligations that affect the issuer at its foreign domicile and those that affect American-based trading in its securities. That the latter obligations may make trading sufficiently unattractive to keep the securities from the market is of no real moment; indeed, it is a consequence accepted in principle once the inadvertency of the issuer's connection with the regulating state is asserted. This point becomes particularly important in discussing the SEC's regulation of the American dealer in foreign securities.

Given this involuntary connection, certain of the burdens imposed by the 1964 Amendments may lose their justification in the foreign context, quite apart from the problem of the unsuitability of transposing some of these burdens into that context. But a decision as to the justifiability of a particular obligation is not so easy as may appear at first glance. For example, the fact that the proxy solicitation process is "domestic" in its detail does not make its imposition abroad factually impossible or normatively outrageous. Before an annual meeting, a foreign issuer can legally send its American shareholders information of the sort rule 14-A requires, whether or not it submits the same information to its domestic shareholders. Further, given that what the shareholder wants is not a knowledgeable minority position but a knowledgeable shareholder family,<sup>38</sup> the issuer can be "required"—in the sense of making this a condition of opening the American market to its securities—to send the same detail even to its domestic shareholders. Even something like a ban on short-swing insider trading can be imposed, not because in personam jurisdiction can occasionally be

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<sup>36</sup> Komitee für Fragen der Securities Acts Amendments of 1964 [Gierlichs Committee], Memorandum über die Publizität deutscher Aktiengesellschaften im Hinblick auf den Schutz der Investoren, Apr. 28, 1965, and accompanying letter to Manuel F. Cohen, Esq., May 6, 1965. See also Komitee für Fragen der Securities Acts Amendments of 1964, Memorandum über die Publizität deutscher Aktiengesellschaften im Hinblick auf den Schutz der Investoren, July 5, 1965, bringing the Apr. 28 memorandum up to date following the passage of the Aktiengesetz of 1965.

<sup>37</sup> Letter to Manuel F. Cohen, Esq., *supra* note 36, at 8.

<sup>38</sup> See *J.I. Case Co. v. Borak*, 377 U.S. 426 (1964).

obtained over the insider in the United States, but because the issuer can be forced—by the simple expedient of stopping United States trading as a sanction—to consider taking internal preventive measures of a contractual nature against the practice.

The matter of choice is stressed because it places emphasis upon the substantive considerations: The importance of protecting local interests weighed against the burdens thus imposed upon the foreign business. Of course, procedural and mechanical considerations have their place in choosing the least onerous satisfactory regulation. Experience shows that using conceptual considerations as to the “extra-territorial” character of the regulation, or worse, abstractions such as “public international law limits on extraterritorial regulation,” in reaching solutions only renders the underlying struggle of material interests unprincipled. Law is better served where we insist upon disclosure of the substantive considerations involved and weigh them directly. If a given regulation can be imposed only through disproportionately burdensome efforts at enforcement or compliance, the benefits thereof may not be worth the bother. But that is a policy matter.<sup>39</sup>

Seen in this light, what are the issues that should have been joined? Returning to the initial classification,<sup>40</sup> as to all burdens affecting the foreign issuer directly a distinction can be drawn between those incompatible with domestic procedure and the rest. If the proxy solicitation requirements are arguably incompatible, then it is not because American procedure requires unique disclosures prohibited locally, but because meaningful solicitation would impose on the foreign issuer use of the burdensome American standard vis-à-vis all shareholders. This incompatibility is not a legal one, however, since foreign law presumably does not forbid disclosures of the kind required by rule 14A. It is, strictly speaking, not an incompatibility at all. It hardly differs analytically from the safety requirements newly imposed upon foreign cars exported to the United States.<sup>41</sup> Only these, of all foreign cars produced, need conform to the requirements. Yet Volkswagenwerk AG might have to conform its entire production to these standards if its assembly line did not segregate United States-bound production from the rest. This comparison forcefully suggests that “unfairness” is the problem.

Further, the sanction for violating an otherwise reasonable obliga-

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<sup>39</sup> See pp. 373-75 *infra*.

<sup>40</sup> See p. 360 *supra*.

<sup>41</sup> National Traffic and Motor Vehicle Safety Act of 1966, 15 U.S.C. §§ 1381-1409 (Snp. II, 1966).

tion may also trigger the "disproportionate burden" complaint.<sup>42</sup> Consideration of the Volkswagen analogy at greater length may be helpful. If Volkswagenwerk AG were directly interested in export to the United States, imposing local standards might be acceptable even though, due to unsegregated production lines, the standards are imposed for all cars it produces. If the company's competitive cost position in its other markets is so jeopardized thereby as to force it to abandon United States exports, however, the "detriment" side of the scale would weigh more heavily. This might tip the decision, but that is all.

If VW exports occur despite the producer's lack of interest in them, the propriety of imposing American standards might depend more upon the particular sanction. The cars might be barred at entry, or local alterations required, to the financial detriment of the trading parties. American law might impose absolute tort liability in the event of accidents—but against the American importer or dealer. All of these sanctions at most go to inhibit United States imports. If by definition these are uninteresting to the foreign producer, the sanctions presumably would be of no concern to it. If VW were interested, then the "foreign detriment" element in the scale must be given more weight.

If, however, absolute tort liability were imposed upon Volkswagenwerk AG despite its lack of interest in, and worse, inability to prevent, exports to the United States, a different situation results—one which can be judged by a more stringent notion of "unfairness."<sup>43</sup> This is a qualitative difference. When applied to proxy solicitation it suggests the need to look at the sanction involved, rather than at the solicitation requirement. If it is assumed that ownership of shares by American residents cannot be prevented, and the sanction operates to punish the foreign issuer for what it cannot prevent, the sanction should be discarded. If on the other hand the sanction acts against trading operations only, it can be evaluated as part of the described weighing process. This process can be used when the regulation is essentially administrative and equally well when it is an abstract command coupled with civil sanctions.<sup>44</sup>

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<sup>42</sup> Another less obvious but perhaps equally important factor would be the burden upon the regulating state of creating the administrative apparatus to process compliance and pursue non-compliance, especially given the relatively inefficient channels and means available to achieve the latter purpose.

<sup>43</sup> As a practical matter, this would be a rare case in light of the difficulties of procuring in personam jurisdiction over the foreign company. Consider, however, that the manufacturer may be present in the jurisdictional sense through other commercial activities.

<sup>44</sup> Some commentators, however, would distinguish between abstract obligation and sanction simply on the basis that a particular sanction was too harsh an expression of

The short-swing profit ban requires a more extended analysis, as here an additional "burden" exists: the unavailability under the foreign law of such a recoupment action. The inability of Volkswagenwerk AG to accept American safety requirements and remain competitive in the United States market is a factual barrier. The inability of a foreign issuer to accept an obligation to police a short-swing ban at its domicile is a matter of foreign law. Even though the issuer has no interest in a United States market for its securities, this is a situation where fairness—perhaps sanctified by the magic label "comity," as an apparent conflict in obeisance exists—might dictate an exemption. The fact that the sanction involved is not one comparable to absolute tort liability might, in this case, be ignored—a result dictated all the more, of course, if the sanction is penal rather than a mere ban on American trade in the securities.<sup>45</sup> Of course, this is typological discussion only; the actual justification for the section 16 exemption is not thus proved. As mentioned, section 16 imposes duties and liabilities not upon the issuer but upon the insider. If there is no obligation upon the issuer to police the ban, the consequences of a violation fall only upon the insider, who is held accountable only if subject to the jurisdiction of American courts.<sup>46</sup> Such an insider's reluctant acceptance of the burden of refraining from short-swing transactions might be an important factor in deciding upon the exemption, but since his abstention from trading is not forbidden by the law governing his transactions, no unique element of comity is added to the factors properly considered.

From this discussion it should be clear that most of the issues involved in deciding on the application of securities trading standards to foreign securities can be handled in a straightforward fashion. A look at the one obligation the SEC retained, the quasi-registration requirement, may confirm this point.

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"extraterritoriality." See, e.g., S. KLAUE, UNTERNEHMENSZUSAMMENSCHLÜSSE NACH § 23 DES [GWB] MIT UND ZWISCHEN AUSLÄNDISCHEN UNTERNEHMEN 75-78 (n.d. 1967); E. REHBINDER, EXTRATERRITORIALE WIRKUNGEN DES DEUTSCHEN KARTELLRECHTS 87-88 (1965).

<sup>45</sup> The possibility that a penal sanction might be visited upon the American dealer in the issuer's securities is probably irrelevant, since such a dealer has the option of abstaining from this business.

<sup>46</sup> Since the provision calls for recovery by the corporation of these profits, the possibility that it may be found in the United States for jurisdictional purposes is by definition irrelevant. Such esoterica are but alter ego allegations seeking to reach the insider through the corporation. *But see* Empire Steel Corp. of Texas v. Superior Court, 56 Cal. 2d 823, 366 P.2d 502, 17 Cal. Rptr. 150 (1961). The enforcement of American regulatory statutes, such as this one, by foreign courts in private actions based directly on the statute is not a likely prospect; see 3 L. Loss, *supra* note 18, at 1855-60.

The demand for information adequate to protect American shareholders has been tailored to the convenience of the foreign issuer. The "registration" need contain only information released by such issuers either voluntarily or under their domestic requirements. In addition, the SEC is willing to police this requirement by relying on apparently harmless administrative sanctions, which involve some unspecified pressures on trading by American dealers.<sup>47</sup> Indeed, the whole weight of regulation has shifted to a mere request of disclosure of the violation, because the SEC does not presently intend to ban trading in the securities of non-complying issuers. On the other hand, dealers who do not disclose an issuer's failure to comply with the registration requirement may in the future be found guilty of a "fraudulent device" with attendant administrative and civil sanctions.<sup>48</sup> Further, the SEC plans to publish a "grey list" of the names of non-complying issuers, on which dealers may rely in advising customers.<sup>49</sup>

#### IV

#### THE RELEVANT QUESTIONS

If the process of reaching accommodation is viewed as a battle, victory would seem to lie with the foreign issuers. Thus it is now ap-

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<sup>47</sup> If on that much. SEC Securities Act of 1933 Release No. 8066 (Apr. 28, 1967), states:

While no sanction will attach to any broker or dealer by reason of its transactions in the securities of an issuer solely because it is listed as neither registered nor exempt, the Commission expects that brokers and dealers will consider this fact in deciding whether they have a reasonable basis for recommending these securities to customers.

*Id.* at 3.

In fairness, however, the dissonance between such dealer sanctions and the ultimate aim of investor protection should be noted; the current investor is the victim, not beneficiary, of driving traders out of the market. See Note, *supra* note 1, at 339.

<sup>48</sup> Note, *supra* note 1, at 339.

<sup>49</sup> One such release was published during the interim period. SEC Securities Exchange Act of 1934 Release No. 7934 (Aug. 10, 1966).

Interesting side issues concern the standing of foreign issuers to be heard in court on complaints against placement on such lists, fairness of any procedure for attempting removal therefrom, and the power (statutory in the case of the SEC) to subject persons to whatever detriment initial publicity imposes. See *Kukatash Mining Corp. v. SEC*, 309 F.2d 647 (D.C. Cir. 1962). The suggested distinction, in *Rehbinder*, *supra* note 16, at 211 n.26, between the Canadian Restricted List involved in *Kukatash* and the "grey list" now at issue, however, is not entirely convincing. While the former case involves the dealer and thus only indirectly harmed the complaining issuer, later cases have rejected similar suits even though the complainant was the very party harmed by the disclosure. See *FTC v. Cinderella Career & Finishing Schools, Inc.*, CCH TRADE REG. REP. ¶ 72,385 (D.C. Cir. 1968); *Lemov*, *Administrative Agency News Releases: Public Information Versus Private Injury*, 37 GEO. WASH. L. REV. 63 (1968).

propriate to turn to the critical questions: Is the result reached a sound result and how does one tell? These questions can only be answered if certain subsidiary facts are known, because the questions are directed at the weighing process and require quantitative data as well as some subsidiary subjective judgments.

The data needed to judge the local benefits of extending the Amendments to foreign issuers would provide answers to questions like these: (1) Is there less need for regulation of foreign securities than American securities? In other words, is this type of investment substantially limited to sophisticated investors? (2) Assuming the minimum of three hundred local shareholders, what is the volume of the local market in foreign issues (whether securities or ADRs) and what is the number of issues traded? (3) Are the answers to the foregoing questions uniform or is there significant variation depending upon the nature or size of the issue, the country of issue, and the issuer's business? Once this side of the scale is quantified, the data needed to determine the detriment of possible regulation upon the issuer become important: (4) How closely do the already required foreign disclosures approximate American requirements? (5) Can the foreign issuer legally comply with American requirements under the foreign law?

Another issue is that of the inadvertency of the connection with the American market: (6) Does the American marketmaker (especially in ADRs) obtain issuer approval for its actions? Is it responsive to persuasion from the issuer, and why? (7) At least in the past, have ADR markets been succeeded by full scale issues on the United States capital markets, or by decisions to list on a national exchange?

Finally, there are what might be called the negative costs of the regulatory effort: (8) How expensive in terms of money and energy is the regulatory and enforcement mechanism to the regulating state? (9) What are the risks to present United States investors of imposing the regulation with its sanctions? Will the market available to them thin out, subjecting their investment to greater dangers than those already posed? Would a grandfather clause be feasible?

The SEC procedure that led to the promulgation of the described regulatory scheme did not allow the eliciting of such information, at least not in any public way.<sup>50</sup> A public notice of its intention to

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<sup>50</sup> Many comments relevant to the above questions can be found in various releases and other communications, but the source, mode and evidentiary detail of their elicitation are not clear. *See, e.g.*, SEC Securities Exchange Act Release No. 8066, at 1-2 (Apr. 28, 1967):

[T]he Commission made an extensive study of the disclosure and reporting requirements and practices in many of the countries whose issuers have securities traded in the United States. . . .

The Commission also asked . . . foreign issuers . . . to furnish to the

promulgate rules was given by the SEC; interested parties, mainly foreign companies and ad hoc groups thereof, and American dealers in foreign securities made representations to the SEC on aspects of the proposed rules; thereafter definitive rules were issued. No rule-making hearings were held (or requested) and no public record as such was made, although most of the industry and interested-party representations are available for inspection at the SEC's headquarters.<sup>51</sup> As a result, there was no public joining of issues to highlight relevant policy choices embedded in the new regulations. Instead, the presentations range from assertions concerning international law and extra-territoriality to detailed legal reviews of particular provisions and problems posed thereunder. At no time, however, with the occasional exception of a glancing blow at the motives presumed to underlie differentiated treatment of Canadian issuers, are questions framed or problems suggested relating to the described material issues.<sup>52</sup> That material justifications, in terms of investor protection, are not reviewed is understandable, given the interest positions and thus the concern of most persons responding. That problems of foreign "burden" are reviewed only assertively rather than in evidentiary detail is perhaps more surprising. This situation—and I suspect other case studies would yield similar proof—suggests that private unilateral monologues are no substitute for a public airing of the issues in the traditional open, and if necessary, adversary, format. In that format the agency suggesting a proposed regulatory scheme can reveal its concerns, and can obtain reactions from two sources. On the one hand, the interests to be regulated, assuming they have a common interest position, can challenge substantively unfounded assertions, and can in turn be challenged on substantively unfounded reactions. On the other hand, such a process affords concurrent challenge of the administrative position by third parties who stand, so to speak, to the left of the agency's initial position—be they interested economic parties, journalists, pro-

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Commission certain information which they made public abroad. . . . During its first study, the Commission noted the improvement in the reporting of financial information . . . and voluntary disclosure by the companies . . . has re-enforced the Commission's initial conclusions as to the quality of the information.

Compare the SEC's recent concern with publicity for staff interpretative and no-action letters. SEC Securities Act of 1933 of Release No. 4924 (Sept. 20, 1968).

<sup>51</sup> Compare the record made by the SEC when the treatment of ADR issuers was discussed in 1955. CONFERENCE ON AMERICAN DEPOSITARY RECEIPTS, OFFICIAL REPORT OF PROCEEDINGS BEFORE THE SECURITIES AND EXCHANGE COMMISSION (1955). As the author has not read this report, reliance for the preceding comment on the evaluation is found in Note, *SEC Regulation of American Depositary Receipts: Disclosure, Ltd.*, 65 YALE L.J. 861 (1956).

<sup>52</sup> Compare the order of priorities in Phillips & Shipman, *supra* note 1, at 761.

fessors, or crackpots.<sup>53</sup> Similarly, such a process permits later examination and, if the passage of events warrants, later criticism and "advice."

Such openness of the regulatory process may not always be a virtue. Delay and expense may dictate shortcuts in the case of trivial situations. Very important problems (financial matters traditionally seem to enjoy this aura) may occasionally suggest a need to rise above principles of participatory democracy. Indeed, the agency's governmental position gives color to its claim of representing the public interest, and any mere private efforts to shape its position on a given problem must therefore be limited to personal supplication.<sup>54</sup> It is no secret, however, that the supplicants have begun to reject this role, and that halting but unmistakable judicial approbation of their new demands is being signaled.<sup>55</sup> On balance, the costs of this trend are not fearsome. Situations wherein costs would be too high—where the only good decision can be a quiet one—will not lack announcers, nor will the relevant interests lack their guardians.<sup>56</sup>

The pervasiveness of regulation and the paradoxical dependence of the regulators upon their respondents—not so much in terms of financial or political inferiority as in terms of access to relevant material for decisions<sup>57</sup>—have made the efficient yet democratic achievement of regulatory goals problematical to the point of theoretical crisis.<sup>58</sup> The

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<sup>53</sup> It may also be required by the Administrative Procedure Act, 5 U.S.C. § 553 (1964). I do not claim that the law requires hearings to be held (*see* K. DAVIS, *ADMINISTRATIVE LAW* § 7.06 (1958)), but that, the constraint of § 553(1) apart, good policy would often so dictate. For a related recent critique, *see* Forte, *Fair Hearing in Administrative Rule-Making: A Recent Experience Under the Federal Food, Drug and Cosmetic and Fair Packaging and Labeling Acts*, 1968 DUKE L.J. 1.

<sup>54</sup> *See* the comments of Donald Turner, then Assistant Attorney General in charge of the Antitrust Division, replying to Congressman Celler's proposal that private parties be granted intervention rights, reported in BNA ANTITR. & TRADE REG. REP. No. 297, at A-15 to A-16, X-1 to X-3 (Mar. 21, 1967); *but see* In The Matter of Applications by American Broadcasting, Inc., 9 P&F RADIO REG. 2d 12, 48 (FCC 1966) (Johnson, Comm'r, dissenting). *See generally* Flynn, *Consent Decrees in Antitrust Enforcement: Some Thoughts and Proposals*, 53 IOWA L. REV. 983, 1008-10, 1016-17 (1968); Shapiro, *Some Thoughts on Intervention Before Courts, Agencies, and Arbitrators*, 81 HARV. L. REV. 721, 740-48 (1968).

<sup>55</sup> *See* *Cascade Natural Gas Corp. v. El Paso Natural Gas Co.*, 386 U.S. 129 (1967); *but see* *United States v. Blue Chip Stamp Co.*, 272 F. Supp. 432 (D.C. Cal. 1967), *aff'd sub nom.* *Thrifty Shoppers Scrip Co. v. United States*, 389 U.S. 580 (1968).

<sup>56</sup> *See* Buxbaum, *Antitrust Policy in Modern Society: Dilemmas and Needs*, in *DAS UNTERNEHMEN IN DER RECHTSORDNUNG—FESTGABE FÜR HEINRICH KRONSTEIN* 345, 364-66 (1967).

<sup>57</sup> *See* L. JAFFE, *JUDICIAL CONTROL OF ADMINISTRATIVE ACTION* 13 (1965).

<sup>58</sup> In lieu of the variety of dispassionate or tendentious comments available upon this subject, *see* the wide-ranging review, as satisfying negatively as it is disappointing

transnational dimension reveals an additional reason to challenge the old system. At first glance one might argue that accommodations here are best reached informally. If American economic policy dictates the tapping of foreign markets by American-owned foreign subsidiaries,<sup>59</sup> dependence upon foreign governments' willingness to allow this may dictate caution in taking a hard line against unregulated foreign issues that reach these shores in presumably secondary trading.<sup>60</sup> While it is not suggested that this lies behind the accommodation described, it is a useful hypothetical example. What may happen, and how easily, when the political reasons for a given regulatory approach change? The conclusory decision—the regulation that dispenses with a justifying record—is particularly susceptible to politically expedient manipulation along arbitrary or discriminatory lines.<sup>61</sup> Foreign interests can be vulnerable to that danger in a manner not applicable to domestic ones. The latter's manifold traditional channels of influence, frontdoor and backdoor, create a web of constraints that can usually hold against flagrant abuse or outrageous experiment. The channels available to foreign interest are generally few and crude. Accordingly, the harmony of challenge and counter-challenge is often missing. Stresses that ought to be accommodated informally can instead lead to clumsy overreaction at the international political level,<sup>62</sup> if not to the resurgence of national autarchy in an international society that can less and less afford it.

In a sense, the foreign issuer exemption from the 1964 Amendments is not the best case from which to extrapolate these general comments. For one thing, as has been briefly suggested, there is some history in the way, which while it is not itself immune from critical review of the sort here sketched, nevertheless explains many of the current exemption details. Sections 14 and 16 have not been applied

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in its proposals, in Loewi, *The Public Philosophy: Interest-Group Liberalism*, 61 AM. POL. SCI. REV. 5 (1967).

<sup>59</sup> See the prevalence of Eurodollar debt and equity flotations at present, coupled with the reverse barrier of the Interest Equalization Tax of 1963, INT. REV. CODE OF 1954 §§ 4911-20.

<sup>60</sup> See Phillips & Shipman, *supra* note 1, at 761-62.

<sup>61</sup> For one example see C. EDWARDS, TRADE REGULATIONS OVERSEAS 563, 573 (1966); the recent debate over allowing accession to the proposed European Patent Convention by the United States is another. See generally Buxbaum, *Incomplete Federalism: Jurisdiction Over Antitrust Matters in the European Economic Community*, 52 CALIF. L. REV. 56, 57 (1964).

<sup>62</sup> An instructive recent example is reviewed in Walker, *Dispute Settlement: The Chicken War*, 58 AM. J. INT'L L. 671 (1964), though he can point to relatively smooth resolution through the GATT machinery. Rougher fights are those mentioned in notes 4 and 5 *supra*. See generally I A. CHAYES, T. EHRLICH & A. LOWENFELD, INTERNATIONAL LEGAL PROCESS 249-575 (1968).

to foreign issuers potentially subject thereto since the inception of the regulatory scheme in 1934.<sup>63</sup> Sections 12 and 13 have been more generally applied to issuing and listed companies, but with due consideration to the less rigorous accounting and certification practices under which many foreign issuers operate.<sup>64</sup> The ADR market was essentially liberated from even these registering and reporting obligations due to what, with all respect to the contrary view of Professor Loss,<sup>65</sup> I am constrained to call an unnecessary technical preoccupation of the SEC.<sup>66</sup> (Even if correct, however, the reasons for the ADR exemption from a reasonable disclosure obligation do not dictate a similar result for section 12(g) issuers.<sup>67</sup>) It is proper to be concerned with even the traditional practice, especially given the new congressional concern inherent in the 1964 legislation; but at the same time it is important to recognize that the only substantial material change from prior practice lies in the abandonment of the special regime for Canadian issuers.

Perhaps more important than history in justifying this anticlimactic disclaimer is the well-deserved faith of the legal community in the essential good judgment of the SEC. Yet an agency whose substantive record engenders such reliance should be among the first to wish its processes open to verification. Of all our regulatory superstructure, it is the SEC that can best claim that it helped this society to reach the point at which open processes are no longer idealistic and no longer dangerous, but achievable and necessary.

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<sup>63</sup> Note 17 *supra*.

<sup>64</sup> Note 20 *supra*.

<sup>65</sup> 1 L. Loss, *supra* note 18, at 463.

<sup>66</sup> This opinion is developed in detail in Note, *supra* note 51, at 866-72; it is shared in a conclusory fashion by Rehbinder, *supra* note 16, at 206 n.9.

<sup>67</sup> The chapter and verse on this problem of ADR coverage is fully explained in Note, *supra* note 51, at 868-71. It involves a technical problem concerning an exemption of securities issued or guaranteed by a bank (banks being the customary source of ADRs) from registration under § 3(a)(2) of the Securities Act of 1933, 15 U.S.C. § 77c(a)(2) (1964). Obviously, this has no relevance to the legality of subjecting the foreign securities themselves to registration.