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Extraterritoriality and the Regulatory Power of the United States: Featured Issues of Sovereignty, Legitimacy, Accountability, and Democracy

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Abstract

Extraterritoriality is a negative form of transnationalism. It creates a paradox among state regulatory power because extraterritoriality can both govern the conduct of the state and also constrain the state in reacting to future transnational changes. In governing the state, extraterritoriality provides the state with the power to impose standards to control the activities within its borders. On the other hand, extraterritorialty constrains the state by hindering multi-state progression towards more efficient transnational developments. States have traditionally captured their autonomy in sovereignty, but extraterritorialty challenges this notion. This was an inevitable result, as extraterritoriality became a natural consequence that resulted from globalization and technological advancements. In this study, the criminal extraterritorial enforcement mechanisms of the U.S. Exchange Act of 1934 will be offered as an example of state extension within the broader context of the transnational world. However, there is one problem with the current predicament and trend: since a state's borders are blurred in modern securities transactions, the state – the United States – is excessively expanding its reach due to this form of transnationalism – extraterritoriality. This extension of U.S. law abroad is unfortunate. While extraterritoriality is a legal way to regulate conduct via prescriptive jurisdiction, it creates problems relating to (1) sovereignty, (2) legitimacy, (3) accountability, and (4) democracy. Regarding state sovereignty, the very definition of extraterritoriality comprises the extension of a state's law upon the foreign conduct of another state's nationals. Current uses of extraterritoriality by the United States are arbitrarily applied without the consent of those affected and, because of this, pose a severe threat to both the territorial and economic sovereignty and integrity of other states. Analyses into legitimacy reveal that people are uncomfortable with this process because of the degree of coercion that results from

the judiciary's ability to formulate additional standards in its case holdings. This use is also counter-productive in that it diverts the focus away from victims and perpetrators and instead redirects attention on methods of enforcement. With extraterritoriality, the United States is gaining different regulatory constituents, namely foreigners; however, the United States is not accountable to these foreign actors. This may include the U.S. adjudication of claims with little to no connection to the United States. Furthermore, extraterritoriality hinders a state's right to self-determination since its basic notion is the imposition of another state's law upon it with no consent. It also undermines the structure of the United States' democracy, including its system of government by creating complications between the U.S. branches regarding the separation of powers. Additionally, even though extraterritorial applications by the United States depict the state as a purported strong player in the international sphere, it instead produces a transformed state that risks foreign infringement through this form of regulatory power. A better approach is one that transcends state public law, abandons the over-reliance on U.S. extraterritoriality, and comports with modern objectives of international cooperation and development, such as forms of either procedural and substantive harmonization.

Introduction

Illustrating the Problem

As globalization meets technological advancements, transnational criminal activity is perpetrated by new opportunities and with innovative capabilities, resulting in a perplexing challenge for the modern state in regulation and enforcement mechanisms. Exacerbating this challenge is the legal exercise of the reliance on the extraterritoriality of U.S. public regulatory statutes to solve transnational crimes. However, despite its legality, specific issues have arisen that challenge the utilization of extraterritorial application of criminal statutory provisions to reach foreign nationals, such as concerns as to state sovereignty, legitimacy, accountability, and democracy. The United States has, in recent decades, used its authority to apply criminal statutes to substantively reach foreign activity. The blame for this is usually given to the "complexities, inventions, and limitations of our modern, transient world" that tend to include "the velocity and capacity of individuals to commit criminal acts while finding ways to avoid

capture."[1] Nevertheless, the question remains as to how the state *should* respond to these challenges.

As an illustration, the U.S. Exchange Act of 1934, specifically Section 10(b), provides for criminal liability if certain elements are met, including willfulness. As will be discussed, although it has recently been held that the presumption against extraterritoriality applies to criminal statutes, the judiciary has nevertheless found ways to evade its scope and formulate new standards to reach foreign conduct. Thus, this study concludes that extraterritoriality is a negative form of transnationalism. It creates a paradox[2] among the regulatory power of the United States by virtue of its ability to both govern and constrain the state. As a state-based driver of transnational law, extraterritoriality empowers the state with the power – not necessarily the international authority – to formulate novel standards/tests to determine the propriety of extending domestic law abroad. And, as these practices to govern regulatory conduct expand and become excessive, its use was tempered by judicial and political-imposed restraints, such as the presumption, comity considerations, interest-balancing, or deference. Whether these restraints are effective tools is a debated topic; however, its function has been to bestow and to acknowledge the obligation of United States to regulate their borders and control the activities within it.

On a similar, slightly contradictory note, the overreliance on extraterritoriality constrains the state by hindering further transnational developments and efforts towards multi-lateral agreements. This constraint includes the reluctance and inability to respond to global changes, which can be a necessity in reacting to a transnational

1. *See* Christopher L. Blakesley & Dan E. Stigall, *The Myopia of U.S. v. Martinelli: Extraterritorial Jurisdiction in the 21st Century*, 39 Geo. Wash. Int'l L. Rev. 1, 15 (2007).

2. *See* Dan E. Stigall, *Ungoverned Spaces, Transnational Crime, and the Prohibition on Extraterritorial Enforcement Jurisdiction in International Law*, 3 Notre Dame J. Int'l L. 1, 2, 5 (2013) (Professor Stigall traces the evolution of transnational criminal activities and observes the "increased need by domestic law enforcement agencies to conduct extraterritorial law enforcement operations" in areas where there is no governmental counterpart willing to take on such a task. In referring to the basic principles of statehood, sovereignty, and territory, Stigall observes how a scheme of sovereign functions with limited external interferences can "mitigate[] conflict in certain respects" (for example, assist in governing the state) but can also "give[] rise to problems associated with transnational crime" (for example, constraining the regulatory power of the state). This is the paradox described above).

world. Through the unilateral expansion of its domestic laws abroad, the United States can inject its presence in the international sphere with little to no accountability to those who are affected by the reach of its laws.[3] This form of hegemonic power has the logical consequence of creating a desire in the United States to dominate internationally and, as a result, deters the willingness of the United States towards progressing in transnational developments. As the proceeding parts will demonstrate, this trend impedes transnationalism.

Outline

This study will reveal how, why, and to what extent the over-reliance on extraterritoriality – particularly when utilized by the United Sates – impedes transnational law developments and efforts at promoting and responding to global changes. It proceeds in the following order. Part II utilizes the criminal provisions of the U.S. Exchange Act as an example of a public regulatory statute and discusses its initial implications in a transnational world. It proceeds to describe the *Morrison*, *Vilar*, and *Bowman* Trilogy as specific illustrations of opinions in U.S. jurisprudence discussing extraterritoriality and the extension from the civil to criminal context.

Part III gives a background on extraterritoriality and the restraints developed to regulate states, such as the presumption against extraterritorialty. It then outlines the purpose and consequences of this practice by the United States, including the motivations behind the actions of the United States and reactions by foreigners. Part IV examines extraterritoriality in a transnational world and discusses the main critiques of current practices that relate to the following four principles: (1) sovereignty, (2) legitimacy, (3) accountability, and (4) democracy. Within each respective sub-part, the criminal provisions of the Exchange Act will be used to further demonstrate how such critiques of a U.S. public regulatory statute operate in a transnational world.

Part V considers the negative implications from this trend, such as the complications with foreign relations matters and the politi-

3. *See* Austen L. Parrish, *Kiobel, Unilateralism, and the Retreat from Extraterritoriality*, 28 Md. J. Int'l L. 208, 220 (2013) [hereinafter, Parrish, *Kiobel, Unilateralism*] (observing how extraterritoriality "became a way to expand the sphere of American influence without having to worry about the constraints that international treaties impose").

cal/economic considerations that make it difficult for the United States to conceive of alternative solutions. It then discusses how to plan for a transnational solution and the possibilities within the criminal enforcement mechanisms of securities laws. Part VI provides the conclusion to this study; namely, that global extraterritorial regulation by the United States impairs transnationalism.

Criminal Provisions under Section 10(b) of the U.S. Exchange Act as A Form of Public Law

Introduction

Public law is defined as "the law of relationships between a government and those whom it governs."[4] Examples of pubic law are most easily illustrated through fields of law such as constitutional law, administrative law, procedural law, and criminal law. This study utilizes the criminal provisions of Section 10(b) of the Exchange Act as an example of a public regulatory statute enacted by the United States to govern the conduct of those within its control. This example is utilized to effectively place its effects within the modern, transnational world. The purpose of this sub-part is to provide background definitions and context that are necessary for understanding the dangerous implications of extraterritorialty in a transnational world. The context is confined to our above illustrated example of criminal provisions of Section 10(b) of the Exchange Act.

Though linked to a state-based driver of transnational law, extraterritoriality has emerged as a form of transnationalism. Transnational law is not easily susceptible to a commonly accepted definition. However, Professor Roger Cotterrell notes that transnational law often "refers to extensions of jurisdiction across nation-state boundaries, so that people, corporations, public or private agencies, and organizations are addressed or directly affected by regulation originating outside the territorial jurisdiction of the nation-state in which they are situated, or interpreted or validated by authorities external to it."[5] It is in the interest of dominant states, such as the United States, to assist in the development of transnational law to assert

4. *See* Michal Tamir, *Public Law as a Whole and Normative Duality: Reclaiming Administrative Insights in Enforcement. Review*, 12 TEX. J. C.L. & C.R. 43, 44 (2006).

5. *See* Roger Cotterrell, *What Is Transnational Law?*, 37 Law & Soc. Inquiry 500, 501 (2012).

its presence in the global sphere. For example, in utilizing the extra-territorial application of its own laws, the United States is unilaterally extending its state's reach upon foreign states/nationals, resulting in a system of blurred borders and, consequently, altered sovereignty of the affected states. Though state extension has the added benefits of familiarity due to its ties to a recognized state, its practice by the United States is seen as politically hegemonic and as an inappropriate solution for transnational developments because transnational law is something distinct from domestic and international law, requiring different solutions. However, its use continues simply because the United States has decided that it wants to extend its power in this field of law – specifically within the securities law context. In other words, the United States – via its criminal public regulatory statute, Section 10(b) of the Exchange Act – can respond to new developments of transnationalism in one of two ways: (1) extending the state, or (2) transcending the state. It chose to extend.

The Morrison, Vilar, and Bowman Trilogy

Morrison, *Vilar*, and *Bowman* have one thing in common: they highlight the significance of the presumption against extraterritorialty – whether implicitly or explicitly – in an attempt to limit foreign infringements. This sub-part aims to provide a brief summary of these opinions and their implications. Its purpose is to reinforce this paper's conclusion that extraterritorialty hinders transnationalism with specific examples from U.S. caselaw.

To begin, criminal law was traditionally confined within the territorial borders of the enacting state.[6] Extraterritoriality challenged this tradition. Due to the "increased [] potential for transnational criminal securities fraud" from technological advancements, the concept of extraterritoriality was developed as "an immediate response to such challenges."[7] Section 10(b) forbids "any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in

6. *See* Edgardo Rotman, *Extraterritorial Criminal Enforcement of Securities Fraud Regulations after United States v. Vilar*, 70 U. Miami L. Rev. 53, 58 (2015) (describing criminal law as the "stronghold of territoriality").

7. *Id.* at 59; *see also* Blakesley & Stigall, *supra* note 1, at 45 (noting the parallel between the "greater willingness to extend the extraterritorial effects of domestic criminal law" and the "social changes and technological advances").

the public interest or for the protection of investors."[8] Section 32(a) provides that "[a]ny person who *willfully* violates any provision of this chapter . . . or any rule or regulation thereunder" shall be criminally liable.[9] In all cases, it is the state that regulates the underlying provisions of the Exchange Act, including the cause of action, remedies, enforcement procedures, etc.

Within the securities context, extraterritorial application of U.S. securities law soon became commonplace. From *Schoenbaum*[10] to *Leasco*[11] and *Bersch*/*Vencap*[12] to *Kasser*,[13] the willingness of the United States in utilizing extraterritorial application sharply increased. Cases from *Hartford Fire*/*Empagran*[14] to *Morrison*,[15] on the other hand, demonstrated a purported cut-back in its over-reliance. *Morrison*, decided in 2010, was a monumental decision in that it held, in a majority opinion by Justice Scalia, that the extraterritorial application of the Exchange Act reach is a merits question, not one of subject matter jurisdiction and that "[w]hen a statute gives no clear indication of an extraterritorial application, it has none."[16] After concluding the "focus" of the statute to be upon the purchases and sales of securities in the United States," the "transactional test" was formu-

8. *See* 15 USC § 78j (Section 10(b), Manipulative and deceptive devices).
9. *See* 15 U.S.C. § 78ff(a) (Section 32(a), Penalties) (emphasis added); *see also* Steve Thel, *Taking Section 10(b) Seriously: Criminal Enforcement of SEC Rules*, 2014 Colum. Bus. L. Rev. 1, 12 (2014) (noting how Section 10(b) can "trigger[] criminal sanctions under section 32, which apply to rules whose violation is made 'unlawful' by the Exchange Act").
10. *See Schoenbaum v. Firstbrook*, 405 F.2d 200, 206 (2d Cir. N.Y. 1968) (developing the "effects" test).
11. *See Leasco Data Processing Equip. Corp. v. Maxwell*, 468 F.2d 1326, 1336 (2d Cir. N.Y. 1972) (developing the "conduct" test).
12. *See Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974, 992 (2d Cir. N.Y. 1975); *see also IIT v. Vencap, Ltd.*, 519 F.2d 1001, 1018 (2d Cir. N.Y. 1975) (decided on the same day concluding that more than "merely preparatory activities" is needed, though the "perpetration of fraudulent acts" is sufficient).
13. *See SEC v. Kasser*, 548 F.2d 109, 116 (3d Cir. N.J. 1977) (justifying extraterritoriality based on policy reasons and to prevent the United States form becoming a "Barbary Coast" for harboring defrauders).
14. *See Hartford Fire Ins. Co. v. Cal.*, 509 U.S. 764, 818-20 (1993); *see also F. Hoffmann-La Roche Ltd v. Empagran S.A.*, 542 U.S. 155, 159 (2004) (finding extraterritorial application in Sherman Act despite strong dissent by Justice Scalia only to change positions entirely about ten years later to hold that the Act did not apply extraterritorially in an attempt to limit infringements with other sovereigns).
15. *See Morrison v. Nat'l Austl. Bank Ltd.*, 561 U.S. 247 (2010).
16. *Id.* at 254-55.

lated, which holds that Section 10(b) applies only to "securities listed on domestic exchanges, and domestic transactions in other securities . . . ."[17] The implications of *Morrison* have shown to be far-reaching, as the transactional and domestic "focus" test deny relief to anything foreign. This is not to imply that extraterritorial application in certain situations needs to be extended further; instead, it lends credence to the assertion that the solution – a transnational solution – does not necessarily depend upon extraterritorialty. However, one thing these cases do have in common is that they are all confined civilly. This changed in 2013 with the *Vilar* decision in the Second Circuit.[18]

The *Vilar* opinion is often cited for its extension of the presumption against extraterritoriality to the criminal context. What is seldom mentioned is its reference, reliance, and subsequent incorporation of a 1922 Supreme Court opinion, *United States v. Bowman*.[19] *Bowman* concerned the application of a criminal statute to foreign conduct. In *Bowman*, as re-emphasized in *Vilar*, the Supreme Court held that the requirement of an explicit statement from Congress regarding extraterritoriality "should not be applied to *criminal* statutes which are, as a class, *not logically dependent on their locality* for the Government's jurisdiction, but are enacted because of the right of the Government to defend itself against obstruction, or fraud . . . ."[20] Like *Morrison*, *Bowman* was also a case of statutory construction.

Since *Bowman*, courts have found "implied extraterritoriality"[21] for many offenses. It is this "implied" qualifier that forms the bases of many problems concerning foreign infringement and judicial arbitrary decision-making. Furthermore, adding *Vilar* into the trilogy produces the holding that the presumption, as reinvigorated from *Morrison*, extends to criminal statutes.[22] Its justification was to avoid the "dangerous principle" that allows the judiciary to give the same statutory provision – Section 10(b) – different meanings in different contexts.[23]

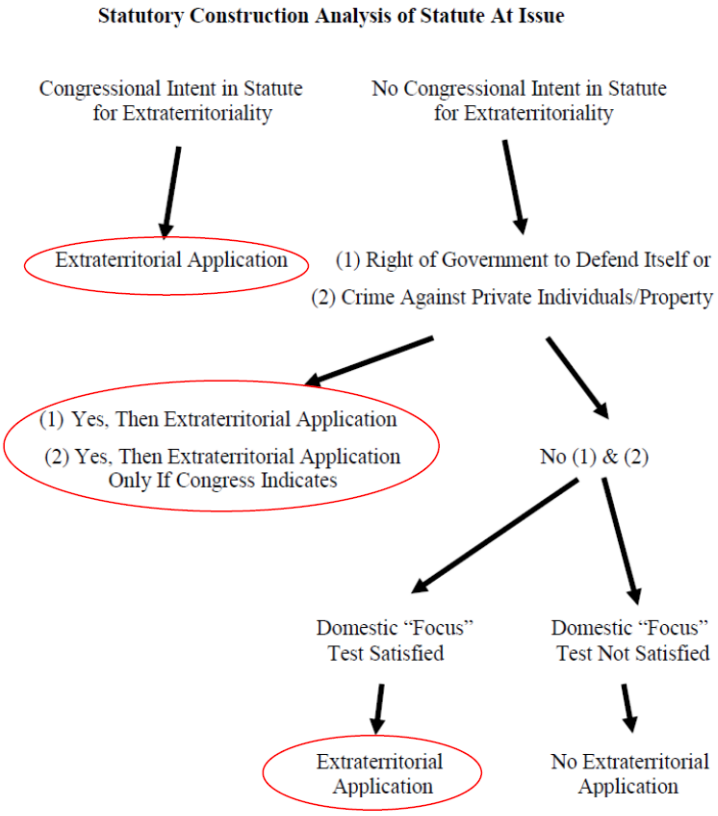
17. *Id.* at 266-67.
18. *See United States v. Vilar*, 729 F.3d 62 (2d Cir. 2013).
19. *See United States v. Bowman*, 260 U.S. 94 (1922).
20. *Id.* at 98 (emphasis added).
21. *See* Blakesley & Stigall, *supra* note 1, at 35.
22. *Vilar*, 729 F.3d at 74.
23. *Id.* at 75.

Thus, we now have a multi-part test when analyzing the extraterritoriality of a criminal statute. First, if statute gives a clear indication that it applies extraterritorially, then it will be extended abroad (*Morrison*).[24] Second, when there is no clear indication, the next step turns on whether the statute at issue prohibits (1) a crime against the government such as the right of the government to defend itself against obstruction or fraud or (2) a crime against private individuals or their property (*Bowman*).[25] Regarding the first option, statutes that prohibit crimes against the government may be applied extraterritorially, even in the absence of clear congressional intent. On the other hand, for the second option, statutes that prohibit crimes against private persons or their property are not applied extraterritorially, unless Congress clearly indicates otherwise.

If the answer to the first two questions is "no," then the statute has no extraterritorial application. Liability can then only be found where the "focus" of the statute is construed by the courts to be on domestic conduct (*Morrison*).[26] As the presumption also applies to criminal statutes, "Section 10(b) is no exception" since the same statute provides for both civil and criminal liability (*Vilar*).[27] A graphical representation of this multipart test is represented directly below.

24. *Morrison*, 561 U.S. at 255.
25. *Bowman*, 260 U.S. at 98.
26. *Morrison*, 561 U.S. at 266.
27. *Vilar*, 729 F.3d at 74.

The *Morrison*, *Vilar*, *Bowman Trilogy* (criminal statutes, excluding Dodd-Frank)



As demonstrated above, the courts as well as lawyers must now use the legacy of *Morrison*, *Vilar*, and *Bowman* in determining whether a federal criminal statute can reach foreign nationals and/or foreign conduct. But the problem remains, as stated at the beginning of this paper: these holdings can and do vary depending on the text of the statute and the interests the court decides that the statute is intended to protect. Thus, this process gives the claimant in these criminal statutory cases not two, but *three* chances of proving that U.S. law should apply to their case (as shown in red above).

A Brief Background on Extraterritoriality of Criminal Provisions under the U.S. Exchange Act

Definition: Extraterritoriality and the Presumption Against Extraterritoriality

This sub-part provides additional background information into extraterritoriality and its restraints. Extraterritoriality involves "the application of federal and state law to conduct that takes place at least partially outside the territory of the United States . . . ."[28] Its application is undertaken in one of three ways: prescriptive (legislative) jurisdiction, adjudicative jurisdiction, or enforcement jurisdiction.[29]

In an attempt to limit the blatantly excessive effects of extraterritoriality, several safeguards were established, such as the presumption against extraterritoriality,[30] an interest-balancing approach,[31] or comity considerations.[32] The most important of these safeguards has been the *presumption against extraterritoriality*, which instructs courts to begin with the presumption that "Congress is primarily concerned with domestic conditions."[33]

However, this presumption is easily rebuttable; for example, the Restatement (Fourth) of Foreign Relations Law, Tentative Draft No. 3, mandates that the presumption be applied unless there is a *clear*

28. *See* Curtis A. Bradley, International Law in the U.S. Legal System 169 (Oxford University Press) (2d ed. 2015); *see also Austen L. Parrish, Evading Legislative Jurisdiction, 87 Notre Dame L. Rev.* 1673, 1679 (2013) [hereinafter Parrish, *Evading Legislative Jurisdiction*] ("[W]hen Congress uses a basis of jurisdiction other than territorial jurisdiction, Congress has regulated extraterritorially").

29. *See* Anthony J. Colangelo, *What Is Extraterritorial Jurisdiction?*, 99 Cornell L. Rev. 1303, 1348-49 (2014) [hereinafter Colangelo, *What Is Extraterritorial Jurisdiction?*] (noting that jurisdiction "comprises at least three different aspects, ordinarily referred to as *prescriptive* jurisdiction, *adjudicative* jurisdiction, and *enforcement* jurisdiction") (emphasis added).

30. *Foley Bros., Inc. v. Filardo*, 336 U.S. 281, 285 (1949) (The presumption is a canon of construction which declares that "legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States" and "is based on the assumption that Congress is primarily concerned with domestic conditions").

31. *See* Cedric Ryngaert, Jurisdiction in International Law 76 (2d ed., 2015) (noting that, in addition to overcoming the presumption against extraterritoriality as a "threshold requirement," further tools of judicial restraint, such as interest-balancing, may also need to be overcome).

32. *See New York C. R. Co. v. Chisholm*, 268 U.S. 29, 31-32 (1925) (In this Supreme Court decision, Justice McReynolds took care to note that to subject a person to the laws of another state where he did not commit any acts "not only would be unjust, but would be an interference with the authority of another sovereign, contrary to the *comity of nations*, which the other state concerned justly might resent") (emphasis added).

33. *Foley Bros., Inc.*, 336 U.S. at 285.

indication from Congress to the contrary.[34] But a clear *indication* is not the same as a clear *statement*, implying that courts over time gained more discretion to discern congressional intent,[35] such as the ability to use context, rely on policy considerations, or promote a purported U.S. interest. It is this discretion that creates many problems in enforcing U.S. criminal securities laws in transnational cases adjudicated in U.S. courts.

Purpose and Consequences

The above sub-part provided a general definition of extraterritoriality; however, it did little to shed light on the damaging effects of the true nature of extraterritorial implications on states. This sub-part will elaborate upon the purposes and developments of extraterritoriality and delineate the major consequences that have resulted.

To start, Professor Jay Lawrence Westbrook instead characterizes extraterritoriality as a form of "sovereign regulation" because these "circumstances always involve multinational conduct of some kind."[36] Professor Austen Parrish, in agreement, notes that extraterritorialty is a "matter of convenience" that is used in lieu of international law-making because it is "politically more expedient."[37] But why did this happen? Among the reasons as to why this practice gained force are because conduct today more likely "materially implicates the territories of more than one state."[38] Because there is no overarching transnational authority to regulate and enforce transnational activity, the task falls to the states to regulate this conduct. In noting this, it appears to be the dominant states that will take on this

34. *See* Restatement (Fourth) of Foreign Relations Law: Jurisdiction § 203, pt. II, ch. 1 (Am. Law Inst., Tentative Draft No. 3, 2017) (noting that federal statutes are to apply only with the territory of the United States unless congressional intent says otherwise).

35. *See* Parrish, *Evading Legislative Jurisdiction*, *supra* note 28, at 1674 (noting that instead of engaging in statutory construction of statutes, "some courts have sidestepped the issue of legislative jurisdiction entirely" and have "redefin[ed] extraterritoriality itself"); *see also* Anthony J. Colangelo, *A Unified Approach to Extraterritoriality*, 97 Va. L. Rev. 1019, 1046 (2011) [hereinafter Colangelo, , *A Unified Approach*] (observing that a rule based on location "may unintentionally sideline the political branches even more by giving total discretion to judges to discern the statutory "focus" and thereby circumvent the presumption altogether").

36. *See* Jay Lawrence Westbrook, *Extraterritoriality, Conflict of Laws, and the Regulation of Transnational Business*, 25 Tex. Int'l L. J. 71, 74 (1990).

37. *See* Parrish, *Kiobel, Unilateralism*, *supra* note 3, at 220.

38. *See* Westbrook, *supra* note 36, at 76.

challenge, either by regulating this conduct by agreement or regulating unilaterally, according to Westbrook.[39] If not, "the conduct will not be regulated at all."[40]

As an easily predictable respondant, the United States became the leader in utilizing extraterritorial application. In gaining power and control in the international sphere to develop transnational movements, several problems emerged. For example, the reliance on extraterritoriality made "Congress gr[o]w generally indifferent to foreign concerns" and resulted in a "new legal orthodoxy that disfavored international law and promoted unilateral domestic regulation."[41] Foreigners grew resentful of this practice, as U.S. cases throughout the decades displayed an increase in the use of extraterritoriality[42] that revealed inconsistent practices.[43] In addition to these inconsistent practices, extraterritoriality has been utilized to serve the best interests of the United States, such as finding such application appropriate where it promote the U.S. government's interests but refusing to find it where the U.S. government harms others.[44]

Despite the above assertions, modern extraterritorial application of U.S. securities laws has been at times characterized by a somewhat

39. *Id.* at 77.
40. *Id.*
41. *See* Parrish, *Kiobel, Unilateralism*, *supra* note 3, at 221.
42. *See* Austen Parrish, Chapter 12, *The Interplay Between Extraterritoriality, Sovereignty, and the Foundations of International Law*, in Standards and Sovereigns: Legal Histories of Extraterritoriality 6 (2017) [hereinafter Parrish, *The Interplay Between Extraterritoriality*] (noting that the "1990s and 2000s witnessed a dramatic increase in the number of national laws applied to foreign conduct").
43. *See* Mark P Gibney, *The Extraterritorial Application of U.S. Law: The Perversion of Democratic Governance, the Reversal of Institutional Roles, and the Imperative of Establishing Normative Principles*, 19 B. C. Int'l & Comp. L. Rev. 297, 301 (1996) (tracing the "vast majority of legislative and executive enactments" and, due to the ambiguous language, noting how "the task of interpreting extraterritoriality from this has fallen on the courts . . . ." who have "been no more consistent, on the surface at least, than Congress").
44. *See* Branislav Hock, *Transnational Bribery: When is Extraterritoriality Appropriate?*, 11 Charleston L. Rev. 305, 307 (2017) (observing how "literature indicates that extraterritorial enforcement might also serve national self-interests, thus destabilizing markets, principles of international order, or international relations between states"); *see also* Gibney, *supra* note 43, at 316 (noting that "while the United States has been very quick to regulate a myriad of phenomena in the world that have, or are perceived as having, a negative effect on U.S. interests, the United States has tended to ignore those situations where its government or corporate entities have had a negative effect on others").

cautionary approach that considers the relationship of U.S. extraterritoriality on foreign affairs. For example, these different forms of foreign infringement in asserting criminal jurisdiction resulted in the development of jurisdictional restraints, as discussed above – such as the limitations on a government's jurisdiction to prescribe, to adjudicate, and to enforce – that operate in order to "regulate[] particular types of juridical behavior on the part of states."[45] But upon closer examination, recent restraints have proven ineffective. For example, since this concept involves unilateral action, there is no consent of other states; there is just the continued action of the United States "in the political realm" with the "superficial veneer of legality."[46] Similarly, Parrish makes this notation as well, claiming that courts have tended to "[e]vad[e] legislative jurisdiction" and to do this represents "an approach that privileges and fosters unilateralism while undermining traditional international law-making . . . ."[47] This failure of the restraints and persistent abuse of extraterritoriality are among the many factors that hinder further developments at transnationalism.

The Concept of Extraterritoriality in A Transnational World
Extraterritoriality as An Attack on State Sovereignty

Extraterritorialty challenges sovereignty because it transgresses a state's borders and results in an unnecessary and arbitrary expansion of the state's reach. The presumption against extraterritoriality developed when principles of sovereignty were strongly adhered to, even internationally.[48] This implies that territorial sovereignty plays a role today; however, the opposite is true. While the critique in this sub-part does not intend to imply that the loss of sovereignty is either completely good or completely bad, it does intend to assert that extraterritorial applications by the United States inappropriately attack

45. *See* Stigall, *supra* note 2, at 11.
46. *Id.* at 10 (concluding that extraterritoriality "enables the U.S. to create law, without being bound by it" and provides "evidence of a hegemonic state seeking to exempt itself from the world system").
47. *See* Parrish, *Evading Legislative Jurisdiction*, *supra* note 28, at 1707.
48. *See* Zachary D. Clopton, *Replacing the Presumption Against Extraterritoriality*, 94 B.U. L. Rev. 1, 8 (2014) ("The presumption against extraterritoriality has its historical roots in the emphasis on territorial sovereignty in international law"); *see also* William S. Dodge, *Understanding the Presumption against Extraterritoriality*, 16 Berkeley J. Int'l Law. 85, 113 (1998) [hereinafter Dodge, *Understanding the Presumption*] ("The original justification for the presumption against extraterritoriality was based in international law").

state sovereignty by infringing upon foreign states in an attempt to regulate the conduct of other states' nationals.

The Treaty of Westphalia in 1648 is credited as bestowing the notion of state sovereignty and stands for the proposition that "the world is divided into discrete territories that are controlled in their entirety by individual and co-equal sovereign authorities" and "implies the absolute authority" to enforce laws within its own territorial boundaries.[49] As additional states were formed, sovereignty was recognized as a form of state independence.[50] However, this traditional definition no longer guarantees the equal authority of the state as the center source of power due to the rise of extraterritoriality. For instance, when we speak of extraterritorial applications of criminal provisions of securities fraud within the Exchange Act, several normative issues arise such "non-intervention, comity, and sovereign equality."[51] These concepts are interrelated in that they all refer to the need for respect and deference of other sovereigns under international law principles.

However, with transnational activities, such as cross-border security transactions, "decisionmakers are doomed to step on some sovereign's toes either by regulating or by not regulating."[52] The most damaging infringements identified are those that relate to the "domestic legal processes and control of its criminal justice apparatus"[53] such as extraterritorial application by a dominant state upon foreign nationals.

However, because it is usually a foreign national – not the foreign state itself – that is aggrieved in these situations, the state's rights under international law are not infringed. Instead, the resentment by the affected state against the dominant state exerting extraterritorial application "represents more a desire to prevent economic harm to its nationals or corporations than an assertion of the rights of

49. *See* Stigall, *supra* note 2, at 8-9; *see also* Alan M. Simon; Spencer Weber Waller, *A Theory of Economic Sovereignty: An Alternative to Extraterritorial Jurisdictional Disputes*, 22 Stan. J. Int'l L. 337, 345 (1986) (noting that sovereignty "directly focuses on the rights of individual states in an international system based upon the equality of states").
50. *See* Simon & Waller, *supra* note 49, at 346.
51. *See* Rotman, *supra note* 6, at 59.
52. *See* Westbrook, *supra* note 36, at 90.
53. *See* Stigall, *supra* note 2, at 10.

the state."[54] For this reason, and because the traditional understanding of sovereignty has been rendered slightly outdated,[55] a more appropriate notion to sovereignty may include the recognition of *economic* sovereignty, as opposed to the traditional territorial sovereignty.[56] Alan Simon advanced this theory to "acknowledge the increased significance of economic forces," "facilitate necessary economic transactions between and among states," and "preserve economic activities closely linked to the existence of the state."[57]

As applied to criminal enforcement mechanisms under the Exchange Act, the economic sovereignty of foreign states is also encroached. This is because, as the law currently stands under the *Morrison*, *Vilar*, and *Bowman* Trilogy, the transactional test causes a severe reduction in foreign capital flow. In denying relief to foreign transactions, U.S. investors are less likely to invest in foreign security markets and thereby less likely to diversify their portfolios internationally to reduce risk.[58] Furthermore, foreign investors are less likely to transact in U.S. securities due to the United States' arbitrary and inconsistent decision-making that are perceived as unfair and contrary to self-governance.[59] Thus, current practices of extraterritoriality by the United States appear to attack both the territorial and economic sovereignty of other states.

Problems of Legitimacy in Utilizing Extraterritorial Application

Enforcement mechanisms must be legitimate, especially when crossing state boundaries and when dealing with transnational activities. Before proceeding, it is necessary to note that there is nothing in

54. *See* Simon & Waller, *supra* note 49, at 344.
55. *Id.* at 347 ("As the nature of the international order changed, so too did the use of the term sovereignty. The definition of breach of sovereignty expanded to include economic concerns").
56. *Id.* at 348 (emphasis added) (Simon and Waller draw an important distinction between territorial sovereignty and economic sovereignty. "Many examples blur the distinction between the territorial and economic rights of states" and "the realities of the modern international economic system often render the distinction between territorial and economic rights meaningless").
57. *Id.*
58. *See* Stephen J. Choi & Andrew T. Guzman, *The Dangerous Extraterritoriality of American Securities Law*, 17 Nw. J. Int'l L. & Bus. 207, 226 (1996).
59. *See* Parrish, *Evading Legislative Jurisdiction*, *supra* note 28, at 1701 ("[L]aws that regulate foreign conduct are often perceived to be antithetical to basic notions of fairness and self-governance").

and of itself prohibited with extraterritoriality; it is a legally recognized form of transnationalism. However, while extraterritoriality is a legal way to regulate conduct via prescriptive jurisdiction, it creates legitimacy and structural concerns. A critique of legitimacy in utilizing extraterritoriality leads us to one fundamental question: are we comfortable with this process? This is the focus of this sub-part. To answer this question requires a consideration of the degree of coercion present and what this practice is creating.

First, the United States – as the dominant nation in utilizing extraterritoriality – exhibits forms of coercive and competitive power. For example, even though the presumption against extraterritoriality has been reinvigorated in an attempt to curb excessive extraterritorialty, the ability of the judiciary to formulate additional standards and exceptions renders the purpose of the presumption meaningless, thus depriving future litigants of consistency and predictability in case holdings. This is also illustrated by the anxiety that foreigners have from the fear of being subject to U.S. law.[60] In concluding the same, Professor Austen Parrish observes the relationship between extraterritorialty and "empire-building and the unseemly bullying of smaller nations by great powers."[61]

Second, Parrish notes how extraterritorialty "runs the risk of being counter-productive." [62] For instance, among the many consequences associated with extraterritorialty by the United States include "turning the focus away from the victims and the perpetrators . . . and instead redirect[ing] global attention to the methods of enforcement."[63] Thus, extraterritorial regulation is viewed as something "illegitimate" with deep-seated foreign resentment.[64] It is these features that make us anti-internationalists and undermine multilateral cooperation.

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60. *See* Harold G. Maier, *Interest Balancing and Extraterritorial Jurisdiction*, 31 Am. J. Comp. L. 579, 582 (1983) (noting the coercive effects of extraterritorialty by those "who might believe themselves likely later to become subject to judicial jurisdiction in United States courts").
61. *See* Parrish, *Kiobel, Unilateralism*, *supra* note 3, at 216.
62. *Id.* at 233.
63. *Id.*
64. *See* Austen L. Parrish, *Morrison, The Effects Test, and the Presumption Against Extraterritoriality: A Reply to Professor Dodge*, American Society of International Law 105th Annual Meeting Proceedings, 16 (2012) [hereinafter Parrish, *Morrison, The Effects Test*].

Accountability Issues of Public Regulatory Statutes Abroad

With extraterritoriality, the United States has gained additional constituents: *foreigners*. However, the United States is not accountable to these foreign actors nor have these foreigners consented to the imposition of its laws. This is the key to an accountability critique, as this sub-part demonstrates. As discussed, current application of U.S. criminal securities laws extraterritorially raises issues of American exceptionalism, unilateral decision-making, excessive judicial discretion as well as creates foreign friction, breaches of comity, and harm to foreign investors/markets. These problems stem from the simple inability of foreign nationals to exert an influence in the political process.[65]

Using the criminal provisions of Section 10(b) as our example demonstrates the self-interested nature of the United States. For example, the inconsistent case holdings and arbitrary standards for determining the propriety of extraterritoriality have comported with U.S. interests only.[66] This creates a lack of accountability of the United States to foreign investors.[67]

The Democracy Concerns in Enforcement Proceedings Using Extraterritorialty

The power of the state in passing legislation that may [not] have extraterritorial application or the ability of the courts to formulate standards and/or restraints in transnational cases creates issues concerning the democratic nature of its process. Such issues relate mainly to the notions that extraterritorialty is characterized by (1) controlling the unconsented, (2) hindering a state's right to self-determination, and (3) undermining the structure of the United States'

65. *Id.* (observing that extraterritoriality can "impose obligations on individuals and groups who have no formal voice in the political process and who have not consented to those laws"); *see* Gibney, *supra* note 43, at 306 (noting how foreigners are "not consulted about the application of foreign law to them, nor do they have the ready means to change the law if it is not consistent with their own domestic standards and norms").

66. *See* Gibney, *supra* note 43, at 304 (concluding that "U.S. law has been applied extraterritorially when that has served the national interest of the United States").

67. *Id.* at 311 (noting the accountability issue between the state enacting the laws and the affected people in the other states).

system of government. This sub-part will analyze the above criticisms of extraterritorialty in relation to principles of democracy.

First, extending the state's criminal statutes to foreign activity creates problems regarding democracy that "impose national laws on foreign legal subjects who did not participate in their enactment."[68] In fact, extraterritorial applications are in sharp contrast with the principles of democracy. For example, Professor Mark Gibney notes that the basic notion of the democratic rule rests in "the consent of the governed."[69] However, extraterritoriality fails to satisfy this standard since it is merely a system whereby the United States is in a position to "pick and choose"[70] which statutory provisions will have extraterritorial application.

Second, this also impacts a state's right to self-determination because the dominant state is arguably imposing its own law on unwilling participants. Using the Exchange Act as our example, Professor Edgardo Rotman observes that "[t]he most damaging effects of securities fraud . . . are that they create distrust toward the system and its healthy components."[71] The purposes of the Exchange Act are "to protect U.S. investors and the integrity of the U.S. capital markets."[72] However, after considering *Morrison*'s new transactional and domestic "focus" test and *Vilar*'s added complexities regarding criminal provisions, it is unlikely these goals are fulfilled. For example, while it has been noted that *Morrison*/*Vilar* deny relief to American investors purchasing foreign shares, it has yet another harmful consequence: the self-determination of foreign states is obstructed since it is possible for its nationals to be increasing captured by U.S. criminal law.

Lastly, extraterritorial application by the United States attacks its democratic structure, such as the separation of powers. Under this critique, Gibney asserts that its use is perpetrated "without any semblance of a system of checks and balances."[73] The unpredictable interaction between the judiciary and political branches is an example of this, as seen in the newly formulated transactional test by the judi-

68. *See* Rotman, *supra* note 6, at 59.
69. *See* Gibney, *supra* note 43, at 305.
70. *Id.*
71. *See* Rotman, *supra* note 6, at 63.
72. *See* Choi & Guzman, *supra* note 58, at 224.
73. *See* Gibney, *supra* note 43, at 307.

ciary in *Morrison* followed by the subsequent, contradictory enactment of Section 929P(b) of Dodd-Frank.[74] Gibney sees instances such as this as the over-devotion of the judiciary in promulgating U.S. law abroad with scant attention to the interests of those bound "who lack the protections of U.S. law or the Constitution."[75]

These arguments are closely intertwined with the issues of legitimacy and accountability discussed above: extraterritoriality is in essence not democratic because "the lawmakers in the country promulgating laws that will be enforced in other countries are not *accountable* to 'the people' in these other lands," as they are "not consulted about the application of foreign law to them, nor do they have the ready means to change the law if it is not consistent with their own domestic standards and norms,"[76] making people question its *legitimacy*.

Future Implications on the Regulatory Power of the United States

Considering the Implications from This Trend

Excessive extraterritorial applications have hegemonic implications that both stifle international cooperation and foreign capital flow. Another dangerous consequence is that this practice has the ability to *influence*. What is referred to here is the ability of the United States to create an example in utilizing extraterritoriality that other states may wish to use themselves to apply their own laws abroad – laws that do not comport with the values and legal system of the United States.[77] For instance, Professor Austen Parrish notes that the practice of extraterritoriality is not limited to the United States; in fact, its use by other states is "hardly surprising," he asserts, as it was the United States that created the "precedent" or "sense of righteousness" in other states.[78] Thus, the question to be explored in this subpart is as follows: How does this concept impact the regulatory power

74. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, § 929P(b), Pub. L. No. 111-203, 124 Stat. 1376, 1865 (2010).
75. *See* Gibney, *supra* note 43, at 307.
76. *Id.* at 305-06.
77. *See* Austen L. Parrish, *Reclaiming International Law from Extraterritoriality*, 93 Minn. L. Rev. 815, 867 (2009) [hereinafter, Parrish, *Reclaiming International Law*] (noting that other nations applying their domestic law extraterritorially is "problematic" because "[l]ittle reason exists to believe that foreign laws necessarily will be consistent with Western concepts of justice").
78. *Id.* at 855.

of the United Sates in today's modern transnational world? The main replies to this inquiry include the adverse implications on foreign relation matters and political/economic considerations which indoctrinates a reluctance within the United States to conceive of different mechanisms to regulate foreign conduct.

Because extraterritoriality involves the application of U.S. law as applied to foreign subjects, it connects to "foreign relations issues that have consequences for the United States."[79] These foreign relations issues can negatively affect the United States' reputation internationally and in the eyes of its own citizens. Regarding international consequences, an increase in the United States' power is likely correlated with a reduction in cooperation for international agreements; thus, this "often reflects an inability or unwillingness to engage multilaterally" and depicts the United States as an "isolationist."[80]

In addition, extraterritorial applications by the United States relate "not merely the question of moral values, but they also have important political and economic consequences."[81] The morality concerns are easy, as extraterritoriality involves the regulation of other states' nationals by a government who is not accountable to these people; it is plainly an unfair process. The political and economic consequences include dampened relationships with other states regarding transnational cooperation and reduced foreign capital flow within the United States. Furthermore, these considerations may create a reluctance within the United States to change their current practices. Professor Gibney elaborates upon the implications of this trend and notes that the increase in its use "will not change, and if anything, the desire to apply U.S. law in other countries will only continue to grow."[82] While this is a regrettable situation, scholars have fortunately noted steps that can be taken to help reverse this trend, as the next part demonstrates.

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79. *See* Clopton, *supra* note 48, at 3.
80. *See* Parrish, *The Interplay between Extraterritoriality*, *supra* note 42, at 11; *see also* Parrish, *Reclaiming International Law*, *supra* note 77, at 874 (noting that the United States' withdrawal from international law occurred at relatively the same time as the dramatic increase in U.S. extraterritorialty and that this results in domestic law replacing international law").
81. *See* Hock, *supra* note 44, at 312.
82. *See* Gibney, *supra* note 43, at 307.

Planning A Solution

In planning the appropriate course of action, due consideration must be given as to whether that solution should continue to utilize extraterritoriality or instead whether a different mechanism should be explored. This sub-part elaborates upon the preparation to be involved at this stage.

As a starting point, Professor Gibney notes how current extraterritoriality practice "does not come close to resembling law-making in the domestic sphere."[83] This is because, as Gibney asserts, there is a gap in the United States' "constitutional balance" that needs to be restored; specifically, it is the political branches that need to be responsible for creating the law and the judicial branch that must serve as the "check against governmental abuses."[84] In addition to the "establishment of normative principles," this "attempt at balance" is needed to prevent the United States from fostering a system of applying its laws extraterritorially and enforcing them upon foreigners without any protection of the law.[85]

Additionally, because the United States is a powerful dominant state in the global community, it has considerable influence in shaping future transnational developments in how to best regulate foreign conduct in a way that reduces foreign infringement and respects international comity. What it currently lacks is the motivation and willingness to initiate these changes.

As a last note to keep in mind, Professor Parrish advances an interesting possibility, which is what this study also intends to promote: "No clear reason exists why global regulation cannot be achieved through multilateral means."[86] For instance, he observes first how most scholarly literature asserts that extraterritorial regulation is necessary in today's world. However, he rebuts this majority view by explaining that the reasons for this are "unclear" and supports this conclusion by noting a contradiction in U.S. history: "We have seen periods where the world's economy was highly integrated, and yet domestic law remained strictly territorially prescribed. And conversely, we have seen nations use extraterritorial laws aggressively,

83. *Id.* at 315.
84. *Id.*
85. *Id.* at 315, 319.
86. *See* Parrish, *Kiobel, Unilateralism*, *supra* note 3, at 239.

even during times of isolation."[87] Thus, it appears extraterritoriality is not dependent on the degree of globalization at stake. In turn, we can conclude that its use is not necessarily needed nor desirable in a transnational, interconnected community.

Possibilities

In considering the above, how should the state respond to this practice? Shall it be the continued extension of the United States abroad or a transcended form of public law? While the former has the appeal of being tied to a state, this study has concluded that the notions of territory and sovereignty are becoming less important in our modern world or, simply, our focus is shifting to include new interests. Furthermore, the idea that extraterritoriality is linked to state-based law is irrelevant in terms of predictability and comfort, as U.S. practice demonstrates several inconsistencies with this concept as well as arbitrary decision-making. The appeal of transnationalism or some form of harmonization recognizes that transnational law is a novel concept deserving of novel approaches. In considering the above ideas, this sub-part serves to elaborate upon the several examples of the next steps our globalized community can take regarding extraterritoriality, as applied to criminal enforcement of securities laws.

Professor Harold Maier begins by concluding that these matters are "most appropriately carried out by diplomatic exchange, not by judicial decisions in which a forum balances its own interest against the competing interests of other states."[88] As we can see, the judicial system has been overly active in formulating standards and tests to determine the propriety of extraterritoriality in the securities context. This is illustrated by the judicially-formulated conduct tests, effects test, and even the transactional with domestic "focus" test. Restraints such as the presumption or comity considerations are nothing more than creations by the United States to appease foreign resentment. Thus, the regulation of transnational activities and transnational conduct, according to Maier, must be based on the "fundamental premise that a state's bona fide territorial interests will be recognized as legit-

87. *Id.* at 238-39.
88. *See* Maier, *supra* note 60, at 581.

imate by the other members of the international community."[89] In other words, legitimacy and comity are the key elements advocated by Professor Maier that "validates the exercise of state power."[90]

Professor Westbrook asserts that "the only acceptable solution to regulation of transnational economic activity in the long run is international agreement . . . ."[91] However, this is complicated to apply to criminal enforcement mechanisms of securities laws across states due to the inherent differences in market structures, sophistication in markets, disclosure requirements, individual cultures, etc. Perhaps the more critical question is whether domestic regulation is a good start towards achieving this "international agreement" goal. Westbrook argues that "only national regulation of multinational conduct will produce the necessary impetus to international agreement."[92] This is because national regulation, he concludes, provides "an incentive to agreement;" nevertheless, before this goal is achieved, the "values of transnational regulation" should always be considered.[93]

Other forms of solutions, though overlapping with the above approaches, include efforts that transcend state borders – such as harmonization. These are more drastic measures, as they involve greater departures from state sovereignty. For instance, Professor Hannah Buxbaum identifies two trends as forms of transnational solutions that have been circulating scholars for decades: a form of *substantive harmonization* or a form of *procedural harmonization*. These can be accomplished via multilateral agreements and are promoted for their lack of unilateralism.[94] Buxbaum states that the first is a form of unification and perhaps constitutes "the most fundamental disturbance" of sovereignty since it will literally replace domestic laws of individual states.[95] On the other hand, the second form, Buxbaum asserts,

89. *Id.* at 584-85.
90. *Id.* at 585.
91. *See* Westbrook, *supra* note 36, at 92.
92. *Id.* at 93.
93. *Id.* at 95.
94. *See* Parrish, *Kiobel, Unilateralism*, *supra* note 3, at 235-36 (Parrish notes that multilateral approaches are "longer-lasting," "avoid fragmentation," and "are more consistent with other international law principles and mechanisms." This is because such approaches, such as treaties, "contain a degree of legitimacy that unilateral approaches lack because multilateral agreements are more egalitarian and democracy reinforcing").
95. *See* Hannah L. Buxbaum, *Conflict of Economic Laws: From Sovereignty to Substance*, 42 Va. J. Int'l L. 931, 947-48 (2002).

are a set of harmonized rules for use in cross-border transactions that will not replace domestic law but nevertheless still constitute a "move away from sovereignty-based conflicts analysis . . . ."[96] Whether these approaches can be effectively implemented depend on their desirability and feasibility. Thus, the overall implementation remains to be seen.

Conclusion

When analyzing the conditions and applicability of the extraterritoriality of U.S. criminal securities law provisions, it is obvious that its current use is unrestrained, arbitrary, and abusive. Thus, it is a negative form of transnationalism. Its use creates a paradox by giving the state to power to govern the activities within its borders but also constraining the state from developing potential transnational solutions to criminal enforcement measures of securities laws. The state's public regulatory provisions can respond to this predicament by either extending the state or transcending it; the United States has chosen to extend.

The current trajectory places the United States on a dangerous path that creates anxieties about future implications such as other states applying their laws extraterritorially. The current uses of extraterritorial applications of the criminal enforcement provisions of the U.S. Exchange Act was provided as an example of this trend. The anxieties noted relate to notions of sovereignty, legitimacy, accountability, and democracy. The critiques of these four preceding principles concluded the following regarding extraterritorial application: (1) it is an unconsented form of global regulation and infringes state *sovereignty*; (2) it makes people uncomfortable with its *legitimacy* because it is coercive and diverts attention away from its victims; (3) it is a process by which the United States is not *accountable* to those that are affected by its regulatory reach; and (4) it undermines the self-determination of states as well as the *democracy* of the United States, such as the separation of powers.

This study thus concluded that this practice by the United States was unfortunate and risks foreign infringement. The practice of extraterritorial applications has little benefits and the global community

96. *Id.* at 948.

would be better off abandoning this process in its entirety as it relates to criminal enforcement mechanisms of cross-border securities transactions. The optimal approach should focus on developments and solutions that transcend state borders, abandons the over-reliance on extraterritoriality, and promotes transnational cooperation, such as efforts at harmonization.