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An Assessment of the SEC's Alternatives for Obtaining Evidence of Illicit Foreign-Originated Trading: The Key is Diplomacy

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COMMENTS

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I. INTRODUCTION

According to a recent study by the General Accounting Office, foreign-originated trades represented more than one-third of all cases of suspected insider trading referred to the United States Securities and Exchange Commission in 1987.¹ The same study indicated that foreign trading in U.S. equity markets has increased dramatically over recent years, totalling almost half a trillion dollars in 1987 or 18% of the total dollar value of all trades in this country.²

1. See *Problems With the SEC's Enforcement of the Securities Laws as to Suspicious Foreign Originated Trades: Hearings before the Subcomm. on Commerce, Consumer, and Monetary Affairs of the House Comm. on Government Operations, 100th Cong., 2nd Sess. (1988)* [hereinafter *Hearings*] (opening statements of Hon. Douglas Bernard, Jr. and Gary Montjoy).

2. See *id.*

The globalization of the securities markets has led to a growing concern about the SEC's ability to police trades originating from abroad.³ Although the SEC has been mindful of the need to prevent illicit foreign-originated trading, the central problem the Commission faces in this area is the collection of foreign-based evidence, *i.e.*, when evidence is located and controlled outside the U.S., the Commission must often defer to and work within the jurisdiction of another sovereign nation.⁴

This Comment assesses the effectiveness of the various alternatives available to the SEC for obtaining evidence from abroad. In order to provide a more objective assessment, Section II examines briefly the historical background of the problems associated with transnational discovery. The discussion in Section III explores in detail the various problems the SEC encounters when it attempts to obtain evidence from abroad under the federal securities laws; it also explores the problems that arise when the SEC attempts to obtain evidence which is subject to foreign secrecy laws or blocking statutes.⁵ In Section IV, this Comment examines the Commission's experience with the various international agreements for the production of evidence. Finally, the concluding discussion in Section V suggests that the most efficient alternative for obtaining evidence from abroad in cases involving illicit foreign-originated trading is not through unilateral judicial action by the U.S., but through diplomatic initiatives which serve to increase international cooperation among governments and their respective regulatory authorities.

3. *See id.*; *see also* U.S. SECURITIES AND EXCHANGE COMMISSION, INTERNATIONALIZATION OF THE SECURITIES MARKETS, ch. 1 (1987); *see generally* sources cited *infra* note 18.

4. *See Hearings* cited *supra* note 1 (testimony of David S. Ruder, Chairman, U.S. Securities and Exchange Commission); *see also* M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT (1989).

5. American litigants conducting discovery abroad may be adversely affected by official foreign acts. Generally, these include antisuit injunctions (orders from one court directing a party not to seek relief in another court or not to comply with orders of another court); blocking statutes (legislative enactments by foreign governments prohibiting distribution of sensitive information); secrecy laws (legislative rights given to individuals which allow them to require others to maintain specific information secret). For a more detailed discussion of the foregoing procedures and their effect on recent discovery efforts by the Commission, *see* M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT 42-47 (1989).

II. TRANSNATIONAL DISCOVERY IN PERSPECTIVE

After World War II, industrial nations experienced a dramatic increase in international trade.⁶ Not surprisingly, this increase in transnational trade resulted in occasional disagreements which invariably ended up in court.⁷ Unfortunately, the intricacies of international law were not understood by the American bar in the early part of this century.⁸ This misunderstanding created obstacles for Americans attempting to obtain evidence from abroad.⁹

The primary obstacle in transnational discovery continues to be the concept of territorial sovereignty, *i.e.*, although the United States and the other nations affected by a case may be friendly allies, they remain separate universal states which, having not yielded sovereignty to one central government or pledged full faith and credit to the judicial proceedings of each other, expect justice to be accomplished through their own respective judicial systems.¹⁰ In order to understand the roots of this conflict, the theories and values underlying judicial procedure in civil law countries must be examined.

In civil law countries, a fundamental precept is that the professionalism of the judiciary secures procedural justice.¹¹ The skill and experience of the judge in evaluating evidence is considered most likely to lead to the "truth."¹² The American discovery process — gathering voluminous quantities of factual information by attorneys who are then free to present or not to present such information and to manipulate its presentation to serve their own ends — is generally distrusted.¹³

Another fundamental precept of judicial procedure in civil law

6. Weis, *The Federal Rules and the Hague Conventions: Concerns of Conformity and Comity*, 50 U. PITT. L. REV. 903 (1989).

7. *See id.* at 903.

8. *See id.*

9. *See id.*

10. Oxman, *The Choice Between Direct Discovery and Other Means of Obtaining Evidence Abroad: The Impact of the Hague Evidence Convention*, 37 U. MIAMI L. REV. 733, 744 (1983).

11. *See Gerber, Extraterritorial Discovery and the Conflict of Procedural Systems: Germany and the United States*, 34 AM. J. COMP. L. 745, 768 (1986).

12. *See id.* at 768.

13. *See id.*

countries is that the litigation process should resolve disputes with maximum dispatch, with minimum interference of private rights, and with minimum costs to society.¹⁴ "Accordingly, the state is not allowed to interfere with privacy rights or to impose burdens on private citizens for the sake of [resolving] a private conflict unless there is a reasonable basis for believing that the result of such use of state power will be significant."¹⁵

Hence, the problems that Americans experience when attempting to obtain evidence from abroad in civil litigation emanate not only from the different historical concepts of procedural justice among civil and common law nations, but also from the different values attached to those concepts.¹⁶ Stated differently, procedures that are fundamental to fairness in the United States, e.g., adversary and full disclosure principles, if imposed on another sovereign state, might violate its fundamental notions of justice and fairness. Consequently, when American discovery rules are sought to be applied outside of the United States, a direct confrontation usually arises between the values and theories underlying the different systems of procedural justice. This confrontation gives rise to many of the problems discussed below.

III. DISCOVERY OBLIGATIONS OF A FOREIGN PARTY OR WITNESS SUBJECT TO U.S. JURISDICTION

The purpose of the discussion in this Section is to examine the problems that arise when the SEC attempts to obtain evidence from a foreign source which, although subject to U.S. jurisdiction, may be allowed or even required by foreign law to not cooperate with the Commission.¹⁷ It is not within the scope of this Comment to examine issues related to the extraterritorial application of U.S. jurisdiction under the federal securities laws.¹⁸ Rather, the discus-

14. *See id.*

15. *See id.* at 769.

16. *See id.*; see also Jones, *International Judicial Assistance: Procedural Chaos and a Program for Reform*, 62 YALE L.J. 515 (1953).

17. *See supra* note 5.

18. For a comprehensive discussion of arguments both in favor and against liberal application of extraterritorial jurisdiction under the federal securities laws, see Note, *American Adjudication of Transnational Securities Fraud*, 89 HARV. L. REV. 553 (1976); Comment, *Extraterritorial Application of United States Commodity and Securities Laws to*

sion in this Section focuses on the conflicts which the SEC experiences in transnational discovery after U.S. jurisdiction has been determined to exist.

A. Analytical Framework

In *Societe Internationale Pour Participations Industrielles et Commerciales, S.A. v. Rogers*,¹⁹ the Supreme Court addressed, *inter alia*, the issue of what, if any, sanctions are appropriate against a party who fails to produce foreign-based records. In that case, the defendant filed a request for production of documents under Rule 34 of the Federal Rules of Civil Procedure. The request was blocked, however, because the Swiss government, pursuant to a ruling by a Swiss Court stating that such disclosure would violate Swiss Penal Law, "constructively" seized the records which were actually being held in a Swiss bank.

Despite the action of the Swiss government, the United States Supreme Court held that, although the documents had been "constructively" confiscated by foreign government authorities, the plaintiff had actual control of the documents and was, thus, required to respond to the request for production.²⁰ However, the Court softened the impact of its holding by stating that, in the absence of *bad faith*,²¹ U.S. courts could not employ the ultimate sanction of dismissal with prejudice, but instead could use sanctions that would only offset any evidentiary advantage attained by the foreign litigant by reason of foreign law.²²

The Restatement (Second)²³ of the Foreign Relations Law of

Market Transactions in an Age of Intercontinental Trading Links, 7 NW. J. INT'L L. & BUS. 351 (1985); Comment, *The Transnational Reach of Rule 10b-5*, 121 U. PA. L. REV. 1363 (1973). For a perspective from abroad, see Hacking, *The Increasing Extraterritorial Impact of U.S. Laws: A Case for Concern Amongst Friends of America*, 1 NW. J. INT'L L. & BUS. 1 (1979).

19. 357 U.S. 197 (1958).

20. *See id.* at 211.

21. *See id.* at 212.

22. *See id.* at 213.

23. The American Law Institute has replaced the Restatement (Second) with the Restatement (Third) of the Foreign Relations Law of the United States (1987) [hereinafter Restatement (Third)]. The Restatement (Third) has been criticized for departing from the comity approach of the Restatement (Second) and for establishing strict, exhaustive, and unpredictable standards for the exercise of U.S. jurisdiction. *See* Goelzer, Stillman, Walter,

the United States (1965) [hereinafter Restatement (Second)] provides additional criteria for ascertaining the discovery obligations of a party, or a witness, subject to U.S. jurisdiction. Section 39 of the Restatement (Second) states that the mere existence of a foreign law which presents a conflict in an area of concurrent jurisdiction does not divest one state of jurisdiction. Instead, as set out in Section 40, both states must consider various factors when they exercise jurisdiction in areas where conflicts may arise. These factors include:

- a. vital national interests of each of the states;
- b. the extent and nature of the hardships that inconsistent enforcement actions would impose upon the person;
- c. the extent to which the required conduct is to take place in the territory of the other state;
- d. the nationality of the person; and
- e. the extent to which enforcement by action of either state can reasonably be expected to achieve compliance with the rule prescribed by that state.

B. *The Diverse Evolution of the Case Law*

The case law has focused on the first two factors of Section 40 of the Restatement (Second) as well as on the *bad faith* factor discussed in *Rogers*. For instance, in *In re Grand Jury Proceedings, United States v. The Bank of Nova Scotia*,²⁴ the District Court for the Southern District of Florida found the defendant/bank in civil contempt for failing to adequately produce documents pursuant to a subpoena.²⁵ The court, therefore, levied a fine which ultimately accrued to \$1,825,000.²⁶ On appeal, the bank argued that, with re-

Sullivan, Michael, *The Draft Revised Restatement: A Critique From a Securities Regulation Perspective*, 19 INT'L LAW. 431 (1985); see also Letter from the U.S. Attorney General to the American Law Institute (Nov. 26, 1985).

In view of the criticism which the Restatement (Third) has received, it is still an open question whether the courts will abandon the approach of the Restatement (Second), and its precedent, in favor of the Restatement (Third). See, e.g., *AVC Nederland B.V. v. Atrium Investment Partnership*, 740 F.2d 148, 150 (2d Cir. 1984); see also *Laker Airways, Ltd. v. Sabena, Belgian World Airlines*, 731 F.2d 909, 950 (D.C. Cir. 1984) (stating that the proposed criteria of the Restatement (Third) would delay international discovery requests).

24. 740 F.2d 817 (11th Cir. 1984), cert. denied, 469 U.S. 1106 (1985).

25. See *id.* at 819.

26. See *id.*

spect to the documents in the Cayman Islands, sanctions should not have been levied against it because compliance with the subpoena would have required the bank to violate the bank secrecy laws of the Cayman Islands.²⁷

The Eleventh Circuit rejected the argument and concluded that, in light of Section 40 of the Restatement (Second), the interest of the Cayman Islands in bank secrecy could not outweigh the interest of the United States in prosecuting criminal transactions.²⁸ Moreover, the court observed that the bank had chosen to operate in two jurisdictions with inconsistent laws and must, therefore, be willing to suffer the consequences of conflicting judicial demands.²⁹

A different judicial approach to a case with facts similar to those of *Bank of Nova Scotia* is found in *In re Sealed Case*.³⁰ In that case, the District Court for the District of Columbia found a bank, owned by the government of country X and a manager of a branch of that bank in country Y, in contempt for failing to respond to a grand jury subpoena.³¹ Both the bank and the manager argued that responding to the subpoena not only would violate the secrecy laws of country Y, but also would subject both the bank and the manager to criminal prosecution in country Y.³² The Circuit Court for the District of Columbia reversed the contempt finding as to the bank.³³

Unlike the ruling of the Eleventh Circuit in *Bank of Nova Scotia*, the Circuit Court for the District of Columbia in *In re Sealed Case* found, *inter alia*, that the defendant/bank could not be compelled to violate the laws of country Y. The court identified two important factors for reversing the civil contempt order against the bank. First, it stated that "these sanctions represent an attempt by an American court to compel a foreign person to violate the laws of a different foreign sovereign on that sovereign's own territory."³⁴

27. See *id.* at 825.

28. See *id.* at 827.

29. See *id.* at 831-32.

30. 825 F.2d 494 (D.C. Cir. 1987), *cert. denied*, 108 S. Ct. 451 (1987).

31. See *id.* at 495.

32. See *id.* at 495-96.

33. See *id.* at 499.

34. See *id.* at 497.

Second, the court stated that the bank "is not itself the focus of the criminal investigation in this case but is a third party that has not been accused of any wrong doing."³⁵

Two additional cases illustrate the reasoning of U.S. courts which are requested to compel production of foreign-based evidence. These cases are *SEC v. Banca Della Svizzera Italiana*³⁶ (hereinafter the *BSI* case) and *SEC v. Tome*.³⁷ In the *BSI* case, the SEC, in an effort to learn a bank customer's identity, moved for an order to compel discovery under Rule 37 of the Federal Rules of Civil Procedure.³⁸ The bank countered by arguing that such disclosure would subject the bank to civil and criminal liability in Switzerland for violating Swiss secrecy laws.³⁹ After a hearing, the District Court for the Southern District of New York granted the SEC's motion.⁴⁰

The opinion of the court in *BSI* is significant for several reasons. First, the court noted that, under *Rogers*, a foreign law prohibiting discovery is not decisive of how a U.S. court must rule on a motion for an order to compel discovery.⁴¹ Second, the court emphasized that the bank in *BSI* had acted in bad faith.⁴² Third, the court balanced the factors of Section 40 of the Restatement (Second) and found that the bank had made deliberate use of Swiss nondisclosure laws to evade U.S. securities laws on insider trading.⁴³ In this regard, the court stated:

The strength of the United States' interest in enforcing its securities laws to ensure the integrity of its financial markets cannot seriously be doubted. That interest is being continually thwarted by the use of foreign accounts. Congress, in enacting legislation on bank record-keeping, expressed its concern over the problem over a decade ago: 'Secret foreign bank accounts

35. See *id.* at 498.

36. 92 F.R.D. 111 (S.D.N.Y. 1981).

37. 638 F. Supp. 596 (S.D.N.Y. 1986), *aff'd*, 833 F.2d 1086 (2d Cir. 1987), *cert. denied sub. nom.*, *Lombardfin v. SEC*, 108 S. Ct. 1751 (1988).

38. See *BSI*, 92 F.R.D. at 113.

39. See *id.*

40. See *id.* at 119.

41. See *id.* at 114.

42. See *id.* at 118-19.

43. See *id.* at 114-17.

and secret foreign financial institutions have permitted the proliferation of "white collar" crime . . . [and] have allowed Americans and others to avoid the law and regulations concerning securities and exchanges The debilitating effects of the use of these secret institutions on . . . the American economy are vast⁴⁴

As a result of the information the SEC discovered in the *BSI* case, the SEC brought successful insider trading cases against several foreigners, including Guisepppe Tome.⁴⁵ In *SEC v. Tome*,⁴⁶ the court found that Tome, an Italian securities professional with substantial business ties to the U.S., had used a confidential relationship with Edgar Bronfman, the chairman and chief executive officer of Seagrams, to obtain and misuse material, nonpublic information concerning the planned takeover bid of St. Joe Minerals Corporation by Seagrams.⁴⁷ Based upon this nonpublic, material information, Tome and others bought large quantities of call options and common stock of St. Joe Minerals Corporation the day before the bid was announced.⁴⁸ The purchase orders were placed by the Swiss bank in the *BSI* case and were executed through foreign brokerage accounts maintained in the names of three Panamanian entities in which Tome had a beneficial interest.⁴⁹ Failure to grant the SEC's motion to compel discovery in the *BSI* case would perhaps have allowed Tome's illicit foreign-originated trading to go undetected.

In summary, the evolution of the international discovery cases demonstrates a tendency by the courts to scrutinize the peculiar facts of each case. The outcome is generally unpredictable⁵⁰ and differs from case to case, *e.g.*, in *Bank of Nova Scotia*, the Eleventh Circuit concluded that the interests of the United States in enforc-

44. *See id.* at 117.

45. *See* M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT 32 (1989).

46. *Tome*, 638 F. Supp. 596.

47. *Id.* at 599.

48. *See id.*

49. *See id.* at 608.

50. *Cf.* Note, *Court Ordered Violations of Foreign Bank Secrecy and Blocking Laws: Solving the Extraterritorial Dilemma*, 1988 U. ILL. L. REV. 563 ("Flaws in the current legal approaches have led to *ad hoc* balancing and frequent questionable findings of bad faith.").

ing its laws outweighed the interests of the Cayman Islands in enforcing its secrecy laws; on the other hand, in *In re Sealed Case*, a case with facts very similar to those of *Bank of Nova Scotia*, the Court of Appeals for the District of Columbia concluded that the interests of the United States did not justify compelling a foreign bank to violate the banking secrecy laws of a foreign country. These cases reflect the great uncertainty the SEC faces when it attempts to obtain foreign-based evidence in civil litigation.

More importantly, however, these cases highlight the need for greater diplomatic initiatives among international securities regulatory authorities in order to bridge the span of obtaining evidence from countries which have different values and theories underlying their respective procedural justice systems. The remainder of this Comment examines the diplomatic initiatives utilized by the SEC and considers whether these initiatives have improved the SEC's ability to obtain evidence from abroad.

IV. DIPLOMATIC INITIATIVES FOR THE PRODUCTION OF FOREIGN-BASED EVIDENCE

As discussed above, conflicting state policies among the sovereign nations of the world often produce gridlock and uncertainty in the gathering of evidence from abroad. During the last several years, however, the SEC has successfully used international agreements for the production of evidence in order to discover and settle several of the most significant insider trading cases in the Commission's history.⁵¹

A. *Bilateral Treaties*

The United States has entered into bilateral treaties which provide for mutual assistance in criminal actions with Switzerland, the Netherlands, Turkey, and Italy.⁵² It has also signed, but not yet ratified, bilateral agreements with the Commonwealth of the Baha-

51. See *infra* note 77 and accompanying text. See generally M. MANN AND J. MARI, CURRENT ISSUES IN INTERNATIONAL SECURITIES LAW ENFORCEMENT (1988).

52. See M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT 47 (1989).

mas, Colombia, Morocco, Canada, and the Cayman Islands.⁵³ To illustrate the advantages and disadvantages of these agreements, the following discussion focuses on the Swiss Treaty as it has served as a model for the negotiation of similar arrangements with other countries.

OPERATION, INTERPRETATION, AND EXPERIENCE UNDER THE
SWISS TREATY IN INSIDER TRADING CASES

The operative provisions of the Swiss Treaty,⁵⁴ which are relevant to civil discovery by the SEC, are found in Articles 3 and 5. Article 3 of the Swiss Treaty provides that the state granting assistance may refuse cooperation to the extent that the request is likely to prejudice its sovereignty, security or similar essential interests. Not surprisingly, banking secrecy under the Swiss Treaty is usually considered an essential Swiss interest. However, unless the person about whom the information is sought is unconnected with the offense, or the secret itself is of special importance to the Swiss economy, assistance generally will be forthcoming under the Treaty.⁵⁵

Article 5 of the Swiss Treaty provides that any evidence obtained pursuant to the Treaty, unless otherwise agreed by diplomatic channels, must be used in a criminal proceeding before it can be introduced in a civil proceeding. Additionally, assistance may also be denied if the purpose of the request is to prosecute a person for acts for which he has already been acquitted in the requested state. Finally, and perhaps most importantly, the Swiss Treaty is available for assistance only in cases that violate the criminal laws of both the U.S. and Switzerland.⁵⁶

In 1982, the SEC made its first request under the Swiss Treaty in *SEC v. Certain Unknown Purchasers of Common Stock of, and Call Options for the Common Stock of Santa Fe International Cor-*

53. *See id.*

54. Treaty on Mutual Assistance in Criminal Matters Between the Swiss Confederation and the United States, May 25, 1976, 27 U.S.T. 2019 (effective 1977).

55. *See infra* notes 58-62 and accompanying text.

56. Because, prior to July 1, 1988, Switzerland had no insider trading law, the dual criminality factor of the Swiss Treaty had created occasional discovery problems for the SEC. However, the recently enacted insider trading law of Switzerland solves most, if not all, of the SEC's former problems as it provides for substantial discovery in cases of insider trading which originate through Swiss banks. *See SWISS PENAL CODE ART. 161 (1988).*

poration⁵⁷ (hereinafter the *Santa Fe* case). In *Santa Fe*, the SEC sought to learn the identities of certain account holders who had directed purchases of Santa Fe International Corporation stock and options through Swiss banks immediately prior to the announcement of a merger. The Swiss Federal Court ruled that requests by the SEC could be processed under the Swiss Treaty, even though the SEC did not have the authority to bring criminal prosecutions.⁵⁸ As grounds for its decision, the Swiss Court reasoned that the requests of the SEC were in furtherance of an investigation and in advance of a possible criminal referral.

Despite its ruling, the Swiss Court concluded that the SEC had failed to allege the requisite violations of Swiss law and denied the SEC's evidentiary request.⁵⁹ Nevertheless, the opinion of the Court left open an avenue for a second request when it stated that, although an "insider" could trade while in possession of nonpublic information,⁶⁰ purchase of stock by a "tippee" would violate Swiss law. Accordingly, the SEC, on July 27, 1983, alleged the necessary additional facts.

After all appeals were exhausted by the defendants, the Swiss Federal Court ruled that the SEC's second request met the adequate requirements under the Swiss Treaty, and the identities of the unknown purchasers were finally revealed to the Commission. As a result of this ruling, the SEC, on February 26, 1986, disgorged approximately eight million dollars in profits from the previously unknown defendants.⁶¹ Since the *Santa Fe* case, the Swiss Federal Court has, on numerous occasions, affirmed the ability of the SEC to use the Swiss Treaty for investigations involving, among other things, insider trading.⁶²

Nevertheless, bilateral treaties pose several disadvantages to the SEC's efforts in obtaining foreign-based evidence. First, bilat-

57. 81 Civ. 6553 (WCC) (S.D.N.Y. Nov. 13, 1981).

58. Opinion of the Supreme Court of Switzerland Concerning Judicial Assistance in the *Santa Fe* Case, 22 I.L.M. 785 (1983).

59. *See id.*

60. *But see supra* note 56.

61. *See* M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT 53 (1989).

62. *See id.* at 53.

eral treaties require a lengthy negotiation and ratification process.⁶³ Second, evidentiary requests are usually not processed expeditiously. Third, as the *Santa Fe* case demonstrates, bilateral treaties usually are not tailored to the specific needs of the SEC and, consequently, consume enormous quantities of the Commission's resources.

B. *The SEC's Experience Under the Hague Evidence Convention*

The United States⁶⁴ and several other countries⁶⁵ are contracting states to the Hague Evidence Convention⁶⁶ (hereinafter the Convention). The Convention contains three of the most common devices for discovery of foreign-based evidence in transnational litigation: letters rogatory, evidence-taking by consular officials, and evidence-taking by appointed commissioners.⁶⁷ However, the internal foreign restrictions on the gathering of evidence, by all but four of the contracting states, have presented obstacles to the use of the

63. See *id.* at 61.

64. For a practical discussion of the procedures involved in processing foreign evidence requests in the United States under the Hague Evidence Convention, see Weiner, *In Search of International Evidence: A Lawyer's Guide Through the United States Department of Justice*, 58 NOTRE DAME L. REV. 60 (1982). For a pragmatic exposition of the procedures for the processing of evidence requests of American litigants in foreign countries, see Augustine, *Obtaining International Judicial Assistance Under the Federal Rules and the Hague Convention on the Taking of Evidence Abroad in Civil and Commercial Matters: An Exposition of the Procedures and A Practical Example: In Re Westinghouse Uranium Litigation*, 10 GA. J. INT'L & COMP. L. 102 (1980).

65. The following countries are parties to the Hague Evidence Convention: Barbados, Cyprus, Czechoslovakia, Denmark, Finland, France, Germany, Israel, Italy, Luxembourg, Monaco, the Netherlands, Norway, Portugal, Singapore, Sweden, United Kingdom, and United States. See U.S. DEP'T OF STATE, TREATIES IN FORCE 318 (1988).

66. Hague Convention on the Taking of Evidence Abroad in Civil or Commercial Matters, *opened for signature* Mar. 18, 1970, 23 U.S.T. 2555, T.I.A.S. No. 7444, 847 U.N.T.S. 231. It is outside the scope of this Comment to look deeply into the purpose or evolution of the Convention. For such a discussion, see Oxman, *The Choice Between Direct Discovery and Other Means of Obtaining Evidence Abroad: The Impact of the Hague Evidence Convention*, 37 U. MIAMI L. REV. 733 (1983). For an insightful look into the differing opinions of the various signatory countries regarding the purpose of the Convention, see *Amici Curiae* Briefs filed by France, Germany, Great Britain and Northern Ireland, Switzerland, United States and the Securities and Exchange Commission, *Societe Nationale Industrielle Aerospatiale v. United States District Court for the Southern District of Iowa*, 107 S. Ct. 2542 (1987) (No. 85-1695) (LEXIS, Genfed library, S. Ct. Briefs file).

67. See *id.* chs. I-II.

Convention by the SEC.⁶⁸

For instance, in England, which has one of the most liberal enabling provisions⁶⁹ under the Convention, internal restrictions direct courts to narrow discovery requests to specific documents. In addition, these internal restrictions allow the Secretary of State to abrogate cooperation for state security reasons. Thus, in *Rio Tinto Zinc Corp. v. Westinghouse Electric Corp.*,⁷⁰ the House of Lords refused to give any effect to language used in a request which it considered to be of a style routinely used in American discovery request, e.g., produce any and all memoranda, correspondence, or other documents relevant to this proceeding; the House of Lords referred to the request as a "fishing expedition."

However, in 1989, the House of Lords, in *In Re State of Norway*,⁷¹ found, *inter alia*,⁷² that a letter of request, which had been modified during the appeal process, could not be rejected as a "fishing expedition," as it was "in substance a request for what, by English law, would be regarded as assistance in obtaining evidence."⁷³ The decision in this case provides substantial support for the position that requests under the Convention can be drafted in a manner to avoid being labelled "fishing expeditions."

Despite *In Re State of Norway* and despite the fact that the SEC has generally obtained the evidence it has requested pursuant to the Convention, the expense and time expended by the Commission to obtain foreign-based evidence under the Convention has been substantial.⁷⁴ Therefore, whenever possible, the SEC has de-

68. See M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT 73 (1989).

69. See Evidence Act (Proceedings in Other Jurisdictions), 1975, ch. 34.

70. 1 All E.R. 434 (1978).

71. 2 W.L.R. 458 (1989) (Goff, M.R.).

72. The House of Lords decision also stands for the propositions that U.K. courts will consider an SEC proceeding a "civil or commercial" matter under the Convention. See *id.* at 471-75 (stating that the term "civil or commercial" matter under the Convention should be construed by reference to the respective laws of both countries in the evidentiary proceeding and that an English court should be prepared to accept the statement of the requesting court that the evidence which is required is for the purpose of a civil proceeding).

73. *Id.* at 479.

74. See M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT 73 (1989).

ferred⁷⁵ to the use of bilateral treaties, to memoranda of understanding, or, where appropriate, to the Federal Rules of Civil Procedure.⁷⁶ The discussion that follows demonstrates that, of the foregoing alternatives, the memoranda of understanding, when combined with other diplomatic initiatives,⁷⁷ provide the SEC with the most expedient and least costly alternative for obtaining foreign-based evidence.

C. *Memoranda of Understanding Between the SEC and Foreign Governments or Authorities*

A memorandum of understanding (hereinafter MOU) is a nonbinding agreement between international financial regulators.⁷⁸

75. The ability of the SEC to defer to other international discovery alternatives was validated in *Societe Nationale Industrielle Aerospatiale v. United States District Court for the Southern District of Iowa*, 107 S. Ct. 2542 (1987) (holding, *inter alia*, that the Convention is not the exclusive means for obtaining evidence located within the territory of a signatory country and that the Convention does not require that its procedures be utilized first). "The SEC, as amicus, opposed both the exclusivity and [the] first use requirement because, among other reasons, its experience has shown that resort to the Hague Convention's procedures can be costly and time consuming." M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT 74 (1989). For a detailed presentation of the arguments of the United States and the SEC in *Aerospatiale*, see *Amici Curiae* Brief for the United States and the Securities and Exchange Commission, *Aerospatiale*, 107 S. Ct. 2542 (1987) (LEXIS, Genfed library, S. Ct. Briefs file).

Recently, however, scholars have suggested an "analytical model" which facilitates as well as reduces the cost of obtaining evidence from abroad under the Convention. See Youngblood & Welsh, *Obtaining Evidence Abroad: A Model for Defining and Resolving the Choice of Law Between the Federal Rules of Civil Procedure and the Hague Evidence Convention*, 10 U. PA. J. INT'L BUS. L. 1 (1988).

76. See M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT 73 (1989).

77. Some of the largest insider trading cases in the Commission's history have been successfully settled as a result of informal, yet responsible, diplomatic initiatives. Perhaps the most notorious case is the action brought against Dennis Levine which ultimately resulted in successful actions being brought against Ivan F. Boesky, Michael R. Milken, and the investment banking firm of Drexel Burnham Lambert, Inc. In *SEC v. Levine*, 86 Civ. 3726 (S.D.N.Y. 1986), Bank Lue International, Ltd., a Swiss financial institution located in the Bahamas, initially refused to disclose Levine's identity and trading activities, arguing that, under Bahamian law, such a disclosure would subject the bank to criminal penalties. The bank, however, turned over the information after the SEC provided it with written assurances from the Bahamian Attorney General that the securities transactions effected through it were not banking transactions and, therefore, not subject to prosecution under Bahamian law. The written assurances from the Bahamian Attorney General were secured through informal diplomatic channels.

78. See M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT 61 (1989).

The regulatory authorities which enter into MOUs usually share the common goal of integrity in the transnational securities markets. An MOU provides for the sharing of information and assurances of cooperation between the SEC and its respective foreign counterpart. Specifically, this arrangement formalizes the methods to request and provide information in connection with international efforts to administer and enforce securities laws.⁷⁹

To date, the SEC has entered into five MOUs. These include agreements with Switzerland;⁸⁰ with the United Kingdom⁸¹ Department of Trade and Industry; with the Japanese Ministry of Finance; with the securities commissions of the Canadian provinces of Ontario, Quebec and British Columbia; and with the Brazil Comissao de Valores Mobiliarios.⁸² It is important to note that, unlike the bilateral treaties discussed above, MOUs do not require that the subject matter of the request involve offenses under the laws of both countries.⁸³ In effect, most MOUs provide the SEC with direct access to information held by a counterpart in a foreign country. This diplomatic approach for obtaining international assistance usually results in the expeditious processing of an SEC

79. *See id.*

80. The Swiss MOU is no longer in effect as its purpose vanished when the Swiss insider trading law went into effect. *See supra* note 56. Nevertheless, bank secrecy remains an integral part of the banking industry not only in Switzerland, but also in other civil law countries; therefore, as elaborated throughout this Comment, a comprehensive historical exploration of the "values" underlying the laws of financial privacy in civil and common law countries is necessary in order to understand and overcome the barriers which keep them apart, especially for the purpose of transnational discovery in complex cases of financial fraud. For such an exploration, see Meyer, *Swiss Banking Secrecy and Its Legal Implications in the United States*, 14 *NEW ENG. L. REV.* 18 (1978); Note, *The Effect of Swiss Bank Secrecy on the Enforcement of Insider Trading Regulations and the Memorandum of Understanding Between the United States and Switzerland*, 7 *B.C. INT'L & COMP. L. REV.* 541 (1984); Comment, *Swiss Banking Secrecy*, 5 *COLUM. J. TRANSNAT'L L.* 128 (1966); Comment, *The Conflict Between United States Securities Laws on Insider Trading and Swiss Bank Secrecy*, 7 *NW. J. INT'L L. & BUS.* 318 (1985). For a discussion of the recent progress in this area, see Capitani, *Banking Secrecy Today*, 10 *U. PA. J. INT'L BUS. L.* 57 (1988).

81. For a recent and comprehensive discussion of the problems associated with the enforcement of insider trading laws in Great Britain, see Comment, *Recent Developments in Insider Trading Laws and Problems of Enforcement in Great Britain*, 12 *B.C. INT'L & COMP. L. REV.* 265 (1989).

82. *See* M. MANN AND J. MARI, *DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT* 74 (1989).

83. *See Id.*

evidentiary request.⁸⁴

THE CANADIAN MEMORANDUM OF UNDERSTANDING

The most comprehensive MOU entered into by the SEC to date is the one with the Canadian provinces⁸⁵ (hereinafter the Canadian MOU). It builds upon the SEC's previous experiences with the Swiss and U.K. MOUs and provides that assistance will be available in cases involving:

- (i) insider trading;
- (ii) misrepresentation of the use of fraudulent, deceptive or manipulative practices in connection with the offer, purchase or sale of any security;
- (iii) the duties of persons to comply with periodic reporting requirements or requirements relating to changes in corporate control;
- (iv) the duties of persons, issuers, or investment businesses to make full and fair disclosure of information relevant to investors;
- (v) the duties of investment businesses and securities processing businesses pertaining to both their financial, operational or other requirements and their duties of fair dealing in the offer and sale of securities and execution of transactions; and
- (vi) the financial and other qualifications of those engaged in, or in control of, issuers investment businesses or securities processing businesses.⁸⁶

Perhaps the most efficient aspect of the Canadian MOU is its simplicity. All that a request for assistance must allege is that the requesting authority is investigating to determine whether a violation of one of the foregoing subjects has occurred. After the required allegations are made, and providing that the information is located within the jurisdiction of the other authority, assistance is generally made available.

84. *See Id.*

85. Memorandum of Understanding Between the United States Securities and Exchange Commission and the Ontario Securities Commission, the Commission de Valuers Mobiliere du Quebec and the British Columbia Securities Commission, Jan. 7, 1988, 27 I.L.M. 412.

86. *See id.*

Prior to the implementation of MOUs, enforcement efforts aimed at cross-border violations of securities laws had required the voluntary cooperation of witnesses or the initiation of costly and often time-consuming litigation. Regulatory authorities usually were unable to compel witnesses located abroad to testify or even to produce documents. However, under the Canadian MOU, securities regulators have agreed to investigate, using subpoena power where necessary, in order to ensure that the requested information is obtained.⁸⁷

If the SEC continues its diplomatic efforts and negotiates additional MOUs which are similar in scope to the Canadian MOU, the enforcement and regulatory capabilities of the SEC will be immensely strengthened. The result will be increased confidence by both institutional and individual investors in U.S. equity markets as they will believe that securities laws are being equally applied. History has demonstrated that this confidence is essential to strong, stable, prosperous, and solid financial markets.⁸⁸

V. CONCLUSIONS AND RECOMMENDATIONS

This Comment recommends diplomatic initiatives as the best alternative for implementing internationally tolerable discovery methods among countries with different theories of procedural justice. Moreover, this Comment suggests that greater cooperation among regulatory agencies has developed because diplomatic efforts, rather than unilateral judicial actions, have facilitated the evolution of the various systems of procedural justice. Furthermore, this Comment demonstrates that, despite inherent differences in the procedural justice systems of sovereign nations, attitudes of countries *can* beneficially evolve by more frequent use of diplomatic channels.⁸⁹

In addition, this Comment demonstrates that diplomatic initiatives provide the Commission with the most pragmatic alternative to the recurring conflicts that arise when it attempts to obtain

87. See M. MANN AND J. MARI, DEVELOPMENTS IN INTERNATIONAL SECURITIES LAW ENFORCEMENT 67 (1989).

88. See generally L. LOSS, FUNDAMENTALS OF SECURITIES REGULATION (1988).

89. Cf. Hearings cited *supra* note 1 (statement by Harvey L. Pitt).

foreign-based evidence. First, the evolution of the case law indicates that, without international agreements, the SEC would face great uncertainty in its international discovery efforts. Second, the experience of the SEC in procuring foreign-based evidence through diplomatic initiatives demonstrates that the Commission is spared considerable time and expense. Third, diplomatic negotiations resulted in the Commission's having successfully settled some of the largest insider trading cases in its history.

Finally, this Comment demonstrates that the globalization of the securities markets makes enforcement of federal securities laws more complex. Barriers based on rigid notions of procedural justice are a severe impediment to obtaining foreign-based evidence. However, this Comment proposes a solution. It suggests that international cooperation among securities regulatory authorities can substantially improve the SEC's law enforcement efforts as well as those of foreign nations. More importantly, this Comment recommends responsible diplomatic initiatives as the key to aligning the conflicting values which keep sovereign nations apart.

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