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For all of the attention brought to bear on global financial regulation, relatively little scholarly energy has been directed towards thinking through the mechanics of how national regulators govern international pools of capital via their domestic rulemaking authority. This Article responds to this weak link in the literature by providing a short conceptual overview of the operationalization of supervisory power by national regulatory authorities. It argues that "territorial" authority in financial regulation—commonly considered both a source and limitation of control over local firms—in practice constitutes a diverse array of tactics employed by national authorities to exert authority over mobile market participants. As such, it can facilitate the projection of regulatory power beyond national borders, especially for countries enjoying large capital and customer markets.

This Article then contextualizes territoriality against the backdrop of financial globalization and shows how the "rise of the rest" changes the international regulatory order as other countries have developed their own liquid financial centers and means of (extra)territorial influence. Specifically, this Article argues that as emerging markets have become more important, the costs of unilateral territorialism and non-cooperation by traditionally dominant countries have increased, which has helped spur new efforts at international coordination, as well as innovative initiatives aimed at leveraging hard and soft power to promote national policy preferences abroad. Nevertheless, this Article concludes that territoriality remains a central element in international coordination and the bargaining process.

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INTRODUCTION

The global financial crisis has brought unprecedented attention to the need for heightened international coordination and cooperation among regulators. As the repercussions of the financial crisis have moved from the United States to Europe and the rest of the world, policymakers now largely acknowledge the economic risks that arise where large financial institutions transact across the globe as investors, insurers, and counterparties.[1] And recent financial scandals have once again highlighted with painful clarity the increasingly international repercussions of fraud and bad acts by financial firms and their management.[2] It is not surprising that the demand for greater collective action among regulators has grown exponentially since the crisis first upended the global economy undermined investors' faith in financial markets.

Yet for all of the attention brought to bear on global financial regulation, relatively little scholarly attention has been directed toward thinking through the mechanics of how *national* regulators govern *international* pools of capital via their domestic rulemaking authority.[3] Specifically, although scholars have long recognized the extraterritorial

1. *See, e.g.*, Declaration, Group of Twenty, Summit on Financial Markets and the World Economy Nov. 15, 2008), *available at* http://www.g20.org/Documents/g20_summit_declaration.pdf (noting the need for achieving greater transparency internationally for complex securities and financial instruments in order to promote investor protection).

2. *See* Martha Brannigan, *SEC Accuses Stanford Group Owner of Massive Ongoing Fraud*, MIAMI HERALD, Feb. 17, 2009, at 1 (reporting the alleged worldwide fraud perpetrated by Robert Allen Stanford's investment company, especially in Latin America); Joanna Chung, *Half of Madoff Loss Borne by Foreigners*, FIN. TIMES, Jan. 12, 2009, at 16 (detailing the global nature of Bernie Madoff ponzie scheme); Richard A. Oppel Jr. & Riva D. Atlas, *Enron's Collapse: The Overview; Hobbled Enron Tries to Stay on Its Feet*, N.Y. TIMES, Dec. 4, 2001, at C1 (noting that Japanese money market funds took a "beating" because of their Enron holdings); Reuters, *Parmalat Is Sued on Behalf of U.S. Investors*, L.A. TIMES, Jan. 6, 2004, at C3 (reporting that Parmalat, though headquartered in Italy, allegedly caused $1.5 billion in losses for U.S. investors).

3. This is not to say, however, that scholars have failed to identify the challenges regulators face when attempting to carry out their domestic regulatory mandates. For just a sampling of the writing on the subject, see William W. Bratton & Lawrence A. Cunningham, *Treatment Differences and Political Realities in the GAAP–IFRS Debate*, 95 VA. L. REV. 989, 1007 (2009); Howell E. Jackson, *Toward a New Regulatory Paradigm for the Trans-Atlantic Financial Market and Beyond: Legal and Economic Perspectives*, EUR. BUS. ORG. L. REV. (forthcoming 2011), *available at* http://www.law.harvard.edu/faculty/workshops/open/papers0708/jackson.paper.pdf; Donald C. Langevoort, *U.S. Securities Regulation and Global Competition*, 3 VA. L. & BUS. REV. 191 (2008); Joel Trachtman, *Regulatory Competition and Regulatory Jurisdiction*, 3 J. INT'L ECON. L. 331 (2000). Indeed, perhaps Claire Kelly and Roberta Karmel have most consistently addressed regulatory export in their analysis of transatlantic securities regulation, though even they do not provide a theoretical framework for assessing the issue generally. *See* Roberta S. Karmel, *The EU Challenge to the SEC*, 31 FORDHAM INT'L L.J. 1692, 1711 (2008) (noting that European integration has given the European Union more power in influencing Securities and Exchange Commission decisionmaking).

effects of various financial rules, the extraterritorial exertion of authority is rarely examined as a regulatory technique. Instead, extraterritoriality is analyzed in the context of the extensive "conflicts of law" literature that focuses on how courts determine which law is to be applied where different governments assert jurisdiction.[4] Though critical to understanding the international reach of national rules, this back-end focus on judicial decisionmaking overlooks the strategic front-end considerations and tactics of national regulatory agencies where achieving domestic policy objectives requires actions with international import.

This Article, prepared for the 2010 Corporate Law Symposium sponsored by the University of Cincinnati College of Law, responds to this under-explored issue in legal scholarship. It provides a typology of dominant regulatory techniques employed by financial regulators and then contextualizes these strategies by exploring their implications in the aftermath of the 2008 financial crisis. In doing so, this Article provides a framework for viewing the role of national regulators as sources of international financial law and provides an assessment for unilateral regulatory power in the wake of the recent global financial turmoil.

To carry out its analysis, this Article scrutinizes the legal means by which regulators unilaterally exert their influence. It argues that "territorial" authority in financial regulation—routinely considered both a source and limitation of control over *local* firms—in practice constitutes a diverse array of tactics employed by national authorities to exert authority over mobile market participants. As such, it can facilitate the projection of regulatory power beyond national borders, especially for countries enjoying large capital and customer markets. This Article also argues, however, that territoriality faces significant challenges in the wake of financial globalization, both in practical and political terms as previously marginal or developing countries have developed their own liquid financial centers and (extra)territorial influence. These challenges, which have only been exacerbated in the wake of the crisis, have spurred new efforts at international coordination and innovative initiatives among traditional regulatory leaders aimed at leveraging their residual hard and soft power to promote their national policy preferences abroad. Nevertheless, territoriality remains an

4. For an overview of the diverse approaches used by U.S. courts, see, for example, Hannah L. Buxbaum, *The Private Attorney General in a Global Age: Public Interests in Private International Antitrust Litigation*, 26 YALE J. INT'L L. 219, 225–26 (2001); Philip J. McConnaughay, *Reviving the "Public Law Taboo" in International Conflict of Laws*, 35 STAN. J. INT'L L. 255, 262 (1999); Symeon C. Symeonides, *Choice of Law in the American Courts in 2000: As the Century Turns*, 49 AM. J. COMP. L. 1 (2001); Donald T. Trautman, *The Role of Conflicts Thinking in Defining the International Reach of American Regulatory Legislation*, 22 OHIO ST. L.J. 586, 617 (1961).

important strategic factor informing the coordination process.

In an effort to demonstrate the importance of territoriality, Part I of this Article provides an overview of the diverse mechanisms of territorial regulation and pinpoints what can be considered the three primary modes of territorial oversight. Part II problematizes the exercise of territorial authority and explores how financial globalization and the financial crisis have altered the strategic calculus underpinning its use. Finally, Part III examines the regulators' recent responses to the changing political economy and predicts a lingering importance for the territorial technique in financial regulatory affairs.

I. THREE MODES OF REGULATORY AUTHORITY

A. Domestic Territoriality

Financial authorities, like most regulators, exercise the lion's share of their power through the supervision of persons, businesses, and activities within their borders. As organs of the state, they wield a long acknowledged power over "territory" largely considered the hallmark of a country's sovereignty under international law.[5]

Defining geographic borders for regulatory purposes is not always a straightforward matter.[6] Instead, jurisdiction over financial matters often arises through what can be described as territorial proxies. In countries with national banking regulators, jurisdiction is generally asserted (and thus territorial contact made) where an institution or branch takes deposits from persons in that jurisdiction.[7] Meanwhile, in

5. Sovereignty is generally conceptualized as the "exercise [of] supreme authority over a territory carved on the physical map of the world." Hannah L. Buxbaum, *Conflict of Economic Laws: From Sovereignty to Substance*, 42 VA. J. INT'L L. 931, 933 n.3 (2002) (citing JARROD WIENER, GLOBALIZATION AND THE HARMONIZATION OF LAW 8 (1999)). *See also* Daniel Philpott, *Sovereignty: An Introduction and Brief History*, 48 J. INT'L AFF. 353, 356–57 (1995) (noting that "Sovereignty is authority within a discrete land, bounded by borders. . . . [and the] legitimate authority within a territory." (emphasis omitted)).

6. This observation holds true not only to the regulation of financial transactions, but also (and even especially) to corporate governance more generally. For example, under the real seat doctrine, the authority over a company's internal affairs belongs to the state in which the company's central management decisions are implemented on a day-to-day basis. Werner F. Ebke, *The "Real Seat" Doctrine in the Conflict of Corporate Laws*, 36 INT'L LAW 1015, 1015 (2002). Meanwhile, under the incorporation theory, the state in which companies are incorporated trigger jurisdiction, thereby granting promoters choice of law as to what principles should govern the internal affairs of the firm. *Id.* at 1016.

7. Here the U.S. serves as a partial exception to this rule. To be sure, where a bank takes deposits in the U.S., it will become subject to regulation by a government entity. However, precisely which entity will regulate turns in part on the form of charter that a bank selects (e.g., state or national), though in either case federal regulation applies at least indirectly under Federal Deposit Insurance Corporation deposit insurance supervision.

the case of securities law, territoriality is largely conceived of through sale of securities to the "public" in a particular jurisdiction or through the use of an instrumentality associated with securities transactions that are physically in a jurisdiction like stock exchanges or other centralized trading venues.[8] Once jurisdiction applies, certain regulatory requirements take effect. In the case of banks and insurance regulation, this has meant that foreign banks must comply with capital adequacy requirements and periodic inspections. Securities firms, meanwhile, along with issuers, must register with the host country's national securities regulator or, in the absence of a national regulator, with the relevant stock exchange authorities, and periodic disclosures must be made.

Domestic territoriality is the dominant mode through which financial risk is regulated. It inherently recognizes the principle that countries have authority over actions that take place within their borders. To the extent that any speculative market activities potentially undermine the welfare of the state, national authorities are well within their right to patrol, govern, and oversee transactions to ensure that they promoted national economic objectives. It is as such in its purest form—where domestic authorities regulate domestic market participants—uncontroversial from the standpoint of public international law.

Additionally, domestic territorially has historically provided a simple mode of exerting dispositive regulatory authority. Following much of the last two centuries, the objects of financial regulation—banks, the buyers, sellers of securities, and insurance companies—were in large part domestic actors, and the bulk of the risks their activities generated were local. By attaching to geographic proxies like branches, stock exchanges, and the investing public, financial regulations could achieve a deep geographic coverage touching virtually all "transactions that occur within its borders, or that have substantial effects within its territory."[9]

In this way, national regulatory authorities have at least historically enjoyed what some commentators have described as a "regulatory monopoly" over the conduct of financial activities in their relevant jurisdictions.[10] By law, domestic companies would have to comply with domestic regulations. Similarly, foreign firms would become subject to

8. *See* Chris Brummer, *Stock Exchanges and the New Markets for Securities Laws*, 75 U. CHI. L. REV. 1435, 1441 (2008) (describing jurisdiction of U.S. securities regulation).

9. Frederick Tung, *From Monopolists to Markets?: A Political Economy of Issuer Choice in International Securities Regulation*, 2002 WIS. L. REV. 1363, 1371.

10. Brummer, *supra* note 8, at 1440 (discussing presumption of regulatory monopoly in the literature).

local laws. As a matter of practice, this has meant that foreign firms are generally afforded national treatment, which means that foreign firms are treated no differently from local firms and must comply with the same rules as their local counterparts.

B. "Extraterritorial" Territoriality

Territorial laws need not necessarily be domestic in effect, a point that the conflicts of law literature and judges have long pointed out. As we have seen, at the most basic level, foreign firms operating in a country will often have to comply with that country's domestic rules, and thus internalize the costs and benefits of the relevant regulatory regime. In such cases, firms may have to make disclosures that are not usually required under their home regulatory regimes and follow various capital, corporate governance, and procedural requirements.

Additionally, territorial laws may require not only that foreign companies be required to comply with the host country's rules, but also that their parent companies do so as well. For example, the U.S. Financial Services Modernization Act of 1999 has required that all foreign banks seeking to be licensed as financial holding companies satisfy risk-based capital standards on a global basis and satisfy the Federal Reserve (the Fed) that its global operations are well capitalized.[11] This consolidated form of supervision confers to the Fed the power to evaluate the operations of international regulators as well as to conduct inspections of foreign affiliates and foreign regulatory agencies.[12] Similarly, the European Union's (EU) Financial Conglomerate Directive and draft Alternative Investment Fund Managers Directive only permit operations and access to customers where the companies and their parent companies either comport with EU rules or are subject to regulation deemed to be equivalent to that exercised by federal European regulators.[13]

Importantly, extraterritoriality need not be operationalized as de jure rules "upstreamed" to parent companies and affiliates. For example,

11. KERN ALEXANDER, RAHUL DHUMALE & JOHN EATWELL, GLOBAL GOVERNANCE OF FINANCIAL SYSTEMS: THE INTERNATIONAL REGULATION OF SYSTEMIC RISK 27 (2005).

12. Other countries are empowered to impose similar restrictions. *Id.* at 47.

13. Michael Gruson, *Supervision of Financial Conglomerates in the European Union* (2004), http://www.imf.org/external/np/leg/sem/2004/cdmfl/eng/gruson.pdf (describing consolidated supervision under the EU Financial Conglomerate Directive); *Commission Proposal for a Directive of the European Parliament and of the Council on Alternative Investment Fund Managers and Amending Directives 2004/39/EC and 2009/…/EC*, at 10, COM (2009) 207 final (Apr. 30, 2009), *available at* http://ec.europa.eu/internal_market/investment/docs/alternative_investments/fund_managers_proposal_en.pdf.

where a regulator imposes a rule applicable throughout its territory, and a foreign firm establishes a subsidiary in a country to carry out operations, compliance by the subsidiary can be up-streamed to the parent company or other international affiliates such that they, too, adopt the stricter rule. Firm managers may prefer to transact under one set of rules in order to minimize the transaction costs of operating in multiple jurisdictions. For example, instead of operating in a country where standard "x" requires a stricter disclosure standard tied to an offering, and then hiring a different set of lawyers to facilitate compliance with standard "y," a more permissive set of disclosures, in another country, a firm will merely abide by "x" in order to minimize compliance costs.

This particular kind of de facto internationalization of national standards is possible where one country imposes certain kinds of national corporate governance requirements. Take, for example, the Sarbanes–Oxley Act of 2002[14] and the EU's rules on credit rating agencies promulgated in 2009.[15] Both initiatives would impose on their respective targets (either issuers of securities under Sarbanes–Oxley or credit rating agencies under the EU initiative) a requirement the firms monitor their internal controls and possibly institute new governance structures and committees. Although both initiatives were directed at local market participants, their effects are potentially international in scope because some regulated entities could find it rational to change all of their operations to reflect these requirements. In that way, common legal processes and administrative structures can be developed to harmonize functions across the firms. Companies may be able to minimize the transaction costs associated with undertaking new compliance procedures in each jurisdiction. Furthermore, by operating along the lines of the highest common denominator, legal risk can be minimized where operations are deeply international, and where multiple subsidiaries often work across borders.

Similar forms of de facto internationalization of national standards occurs where a national authority applies rules to its own firms that are then "passed on" indirectly to foreign clients. For example, as part of its credit rating agency regulations, the EU has considered and adopted a

14. Sarbanes–Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745.

15. *Commission Proposal for a Regulation of the European Parliament and of the Council on Credit Rating Agencies*, at 8, COM (2008) 704 final (Nov. 12, 2008), *available at* http://ec.europa.eu/internal_market/securities/docs/agencies/proposal_en.pdf (describing proposed transparency and independence requirements for credit rating agencies operating in Europe); Press Release, Council of the European Union, Financial Services: New Rules on Credit Rating Agencies, Bank Capital Requirements, Cross-Border Payments and E-Money, and a Programme to Support the Effectiveness of EU Policies (July 27, 2009), *available at* http://register.consilium.europa.eu/pdf/en/09/st12/st12380.en09.pdf.

range of reforms that would impose elevated capital requirements on banks, insurance firms, and other financial institutions that enter into financial transactions whose risk assessments rely in part on credit rating agencies that have not been registered by EU authorities.[16] The idea is, at least in theory, born of regulatory policy concerns in the wake of the credit crisis insofar as authorities wish to ensure that credit rating agencies are properly supervised and regulated given the extent to which ratings are used for investment and regulatory purposes. In practice, however, it also helped the European Union export its preferred policy approaches by forcing credit rating agencies to register and comply with its rules if they wished to access and provide competitive services for European banks and financial institutions.

These examples illustrate that as a regulatory concept, "territoriality" best describes not so much the effect or scope of law, but instead the means by which it is generated. Territorial regulation need not be entirely domestic in its reach. By operating as a gateway to investors, consumers, and capital, territoriality can be leveraged in a way that can affect foreign firms—at a minimum those operating in the country—and potentially, the conduct by foreign regulators as even some parent firms and affiliates adopt the rules or standards of the exporting state.

Even more importantly from the regulator's standpoint, territoriality can potentially afford extraterritorial prudential and supervisory power. In an age of globalized financial transactions, the appeal of extraterritorial regulation is obvious. As business activity has become increasingly cross-border, strong extraterritorial regulation permits regulators to reach beyond their territories to affect the conduct of foreign market participants and occasionally foreign regulators.

C. "Direct" Extraterritoriality

As a third regulatory strategy, authorities can adopt purer forms of extraterritorial regulation that apply more directly to international actors and activities. This subpart addresses three possibilities, in particular. First, regulators can apply laws directly and exclusively addressed to foreign firms. Second, jurisdiction can be structured in a way such that even the most inconsequential contact with the state triggers its authority. Finally, jurisdiction can arise wherever foreign acts have an "effect" on the regulating country.

In the first case, a country could simply pass laws that apply directly to foreign firms. For example, a country could pass a law that outlaws

16. Council Regulation 1060/2009, On Credit Rating Agencies, 2009 O.J. (L 302) 1.

any bank in the world from engaging in fraudulent conduct with any of that country's nationals—even where the depositors are themselves overseas when transacting with the firm. Such cases of extraterritoriality are virtually non-existent in the financial world, in part because courts themselves are reluctant to take on cases where such little national interest exists. However, they are at least theoretically possible, as demonstrated by the Alien Tort Claim statutes and its international progeny, which permit foreigners to sue for human rights violations that occur abroad, as well as under the Foreign Corrupt Practices Act, which among other things bars the bribery of foreign government officials by U.S. persons.[17]

As a second course, regulators can assert jurisdiction extraterritorially wherever foreign companies engage in conduct that has effects in the country asserting jurisdiction. In practice, this kind of extraterritorial strategy has been used to most spectacular effect in antitrust actions, such as where the European Commission, largely on the basis of the anti-competitive implications the deal would have for European markers, blocked a merger between General Electric and Honeywell after the U.S. Department of Justice sanctioned it.[18] Effects-driven jurisdiction has also at times been applied by courts in amplifying the reach of U.S. securities laws. For example, in *Des Brisay v. Goldfield Corp.*, a court ruled for plaintiffs where they alleged that an issue of stock in Canada to insiders of a Canadian company at an unfairly low price adversely affected the value and price of the company's shares listed on the American Stock Exchange.[19] Although fraud was perpetrated by a Canadian company and the foreign defendant never entered the United States in connection with the fraud, the Second Circuit found in part because of the adverse effect on the equity of U.S. shareholders was sufficient to support jurisdiction.[20]

A final subspecies of direct extraterritoriality, similar to effects-based jurisdiction (and indeed often employed in conjunction with it), arises through the implementation of what can be considered tenuous contacts with even territorial proxies. As such, it is best explained through example, again with reference to the United Stats, which remains the country most likely to exert extraterritorial financial law. The Securities

17. For a description of the Alien Tort Claims Act, see Harold J. Berman, The Alien Tort Claims Act and the Law of Nations, 19 EMORY INT'L L. REV. 69 (2005). *See also* Tara Elliott, Note, *Risky Business: The Alien Tort Claims Act and the Foreign Corrupt Practices Act Expand the Reach of U.S. Courts in a Global Economy*, 62 RUTGERS L. REV. 211 (2009).

18. *See* Michael Elliott, *The Anatomy of the GE-Honeywell Disaster*, TIME, July 9, 2001, at 5.

19. Des Brisay v. Goldfield Corp., 549 F.2d 133 (9th Cir. 1981).

20. *See id.* at 135.

Act of 1933 provides that it is unlawful to offer or sell any security without registering it where there is use of any "means or instruments of transportation or communication in interstate commerce or of the mails."[21] Meanwhile, "interstate commerce" is defined in the statute to include "trade or commerce in securities or any transportation or communication relating thereto . . . between any foreign country and any State, Territory, or the District of Columbia."[22] As a result, the statute is silent as to the scope of registration requirements, and it can be construed to encompass virtually any offering of securities made by a U.S. corporation to foreign investors wherever say, a telephone call to the United States is made in connection with the sale of a security abroad, and exclusively to foreign investors.[23] The rulemaking authority of the Securities and Exchange Commission (SEC) has, consequently, had potentially broad, international implications.

Direct extraterritorial jurisdiction has several clear advantages over domestic and extraterritorial territoriality. Territorialism's inherent limitation—that authority it is tied to certain geographic markers—is at least theoretically overcome. A regulator can directly address foreign activities without having to substantiate significant contacts with its domestic territorial borders. In this way, activities that have repercussions for financial markets or a regulator's national economy, but that might be consummated entirely overseas, can be addressed through domestic prudential and supervisory regulation. Consequently, direct extraterritorial regulation may be able to more significantly affect the behavior of foreign firms. Additionally, the very promulgation of international standards or rules could have a deterrence effect with regards to the possible conduct of overseas actors. And like classic territorial regulation, it can be wielded unilaterally with no cooperation required from a foreign counterpart with regards to the promulgation of the rules, but must, at most, be verified or upheld by domestic judicial authorities.[24]

21. *See* Securities Act of 1933, § 5(a), 48 Stat. 74, 77 (1933) (codified at 15 U.S.C. § 77e (2006)).

22. *See* 15 U.S.C. § 77b(a)(7) (2006).

23. *See* Schoenbaum v. Fistbrook, 405 F.2d 200, 206 (2d Cir. 1968) (explaining the extraterritorial application of federal securities laws), *rev'd en banc*, 405 F.2d 215 (2d Cir. 1968). For a detailed discussion of the effects test in securities regulation, see generally Symposium, *Oversight by the U.S. Securities and Exchange Commission of U.S. Securities Markets and Issues of Internalization and Extraterritorial Jurisdiction*, 29 INT'L LAW. 731 (1995).

24. Courts may, of course, themselves impose strict limitations on the power of regulators, the subject of the conflicts of law literature. *See generally* Buxbaum, *supra* note 5, at 941. Indeed, often considerations will involve a balancing of interests between countries. Yet even here, there is a focus on territorial power that at least historically has often upheld the exercise of extraterritorial authority.

II. THE DIFFICULTY OF EXTRATERRITORIAL EXPORT

Despite the advantages catalogued above, the unilateral "exportation" of regulation by national authorities to other jurisdictions—both in its indirect territorial guise and in its more explicit form—is difficult. Ultimately, two challenges stymie regulators from acting unilaterally. The first is what can be considered a "political economy" problem: regulators, in short, do not act in a vacuum, and where their actions have negative consequences for foreign regulators, they may punish the regulatory exporter. The second is the increasingly diverse sources of finance, a product of financial globalization, which not only exacerbate the political and possibly economic costs of unilateralism, but also make extraterritoriality less practical and weaken the incentives for tough domestic territorial rules.

A. The Political Economy Problem: Reputation and Retaliation

The political economy problem of extraterritorial regulation stems from the fact that extraterritorial export can spark reactions, some retaliatory, from other regulators that can imperil a regulator's ability to achieve its own long-term strategic objectives.

As perhaps the most basic consequence of extraterritorial regulation, consider how it can undermine a regulator's image among its international peers. The international system generally frowns upon unilateral extraterritorial conduct, in part because it often implies the violation of longstanding principles of international law. The very notion of sovereignty, as discussed *supra*, demands that states have full authority over their respective territories, whereas principles of comity, though not formally public international law, have long required that governments give effect to the executive, legislative, and judicial acts (and authority) of other countries.[25] As a result, either directly or indirectly, extraterritorial legislation is generally found to be an acceptable practice only where it can be justified by significant interests of the intervening regulator.

Yet here as well, extraterritorial conduct can have serious controversial qualities. Even where a regulator has significant interests, its interests may not necessarily be superior to those of other regulators. Moreover, even if it believes they are, other regulators may not necessarily agree, or they may perceive its regulatory response as not

25. Comity encourages restraint and the limited interference by sovereigns in extraterritorial affairs. Note, *Offshore Funds and Rule 10b-5: An International Law Approach to Extraterritorial Jurisdiction Under the Securities Exchange Act of 1934*, 8 FORDHAM INTL L.J. 396, 410 (1985).

being tailored narrowly enough to speak to those interests. Conflicts of law under such circumstances can generate, as Chief Justice Rehnquist once mildly noted, "international discord."[26]

Extraterritorial regulation, even when justifiable, generates costs that are not internalized by the officious regulatory authority or its local firms, but are instead born by unwitting foreign regulators and market participants. The assertion of regulatory authority often accompanies costs for foreign firms that must adjust to new standards or move to other jurisdictions to avoid a law's regulatory effect. It also potentially infringes on the ability of foreign regulators to oversee and supervise firms the way in which they wish. Firms in an affected jurisdiction may have to change their corporate governance structure, disclosure requirements, or register with another national authority, all of which could undermine the authority of the national regulator. Extraterritorial regulation can also send signals as to a regulator's views of another's regime, and implies that foreign law is less sound than those practiced domestically.

As a result, the decision by a regulator to engage in extraterritorial regulation often erodes its reputation in the international community. For example, a regulator may appear self-interested and insensitive to the costs and consequences that its laws may have for other regulators and firms. Furthermore, the regulator can develop a reputation as less willing to respect the doctrine of comity and perhaps even international laws of sovereignty.

A poor reputation can have a variety of adverse consequences. Perhaps most obvious, as a regulator gains a reputation as self-interested or uncooperative, other regulators may decide to refrain from cooperating with it or helping it achieve its strategic objectives.[27] How would this passive retaliatory conduct look in practice? At a minimum, a regulator could decide not to help the extraterritorial regulator enforce its extraterritorial rules when it seeks help prosecuting a violation where witnesses or the proceeds of misconduct are located abroad in its jurisdiction.[28] In more dramatic circumstances, a regulator could pull back from cooperation more generally. It could decide not to engage in joint regulatory projects—unless, of course, it was directly in its own

26. EEOC v. Arabian Am. Oil Co., 499 U.S. 244, 248 (1991).

27. This idea has been articulated by a variety of theorists, but for a comprehensive assessment see ANDREW T. GUZMAN, HOW INTERNATIONAL LAW WORKS 71–111 (2008).

28. John D. Kelly, Note, *Let There Be Fraud (Abroad): A Proposal for a New U.S. Jurisprudence with Regard to the Extraterritorial Application of the Anti-Fraud Provisions of the 1933 and 1934 Securities Acts*, 28 LAW & POL'Y INT'L BUS. 477, 478 (1997) (discussing how countries frustrated with extraterritorial laws are often reluctant to enforce judgments).

interest to do so—as well as could refrain from robust information sharing and enforcement cooperation.

Additionally, a regulator can respond by making its own extraterritorial rules.[29] In some rare situations, a response might take on an explicitly retaliatory character aimed at disciplining the extraterritorial regulator, while in others it may merely take place as a reciprocal breach in related areas from established principles of comity. More frequently, extraterritorial conduct may also serve as a kind of "precedent" justifying extraterritorial regulation in unrelated financial matters. For example, consider the promulgation of the Sarbanes–Oxley Act, where many European regulators protested what many believed was Congress's lack of respect for comity, and complained that the wide reaching extraterritorial effects would require many firms to reconstitute their corporate governance fundamentally to meet U.S. standards that were poorly suited to the way in which firms evolved abroad.[30] Ultimately, their protests were largely ignored and few reforms to the legislation were made. This event, however, created a precedent for similar territorial rules enacted by the European Commission when it enacted stiff corporate governance requirements for (primarily American) credit rating agencies. And after previously promulgating its own rules, the SEC was in a weakened position to argue against such extraterritorial exerts of power.

As a result, the mode of jurisdictional authority asserted by regulators can be important. It is conceivable, and indeed likely, that traditional territorial regulation generates fewer political costs than direct extraterritorial legislation. Extraterritorial legislation challenges international law more obviously than even aggressive territoriality insofar as it is either addressed directly to actions that take place overseas or at least implicitly does not limit the application of rules domestically. There are also fewer obvious justifications for it. Extraterritorial territoriality can at least be justified on the basis that it is applied domestically, addressing local actors or transactions. Moreover, where territorial regulation is promulgated, regulators can argue that, from a fairness perspective, foreign companies voluntarily subject themselves to host country regulation by coming to the country to do business. Arguably, firms "opt-in" to the regulatory regime of the host state. No such justifications are usually available where extraterritorial

29. *See* GUZMAN, *supra* note 27, at 42–49 (discussing retaliation and reciprocity as disciplinary responses in international relations).

30. For an analysis of the difficulties for European companies, especially in Europe, see Lawrence A. Cunningham, *From Convergence to Comity in Corporate Law: Lessons from the Inauspicious Case of SOX*, 1 INT'L J. DISCLOSURE & GOVERNANCE 269, 272 (2004).

laws are explicitly addressed to foreign companies and actions taking place abroad.

B. Financial Globalization's Brave New (and Larger) World

Regulatory export is also increasingly difficult due to the increasing diversification of international sources of finance. To understand why, it is necessary to recognize that regulatory export largely relies on a regulator's authority over large, liquid capital markets. Simply put, the bigger the capital market, the greater the influence of regulators. Larger capital markets are more indispensable sources of capital for capital or client-hungry multinationals. As a result, large capital markets amplify the power of local regulatory authorities. If a capital market is significant enough to the global economy, its rules can become *lex financiaria*—not necessarily the formal international law of finance per se, but international financial law complied with by firms.

In practice, only the United States has consistently wielded such authority over the last sixty years. Its securities markets largely dwarfed those in other countries, and thus most multinational companies seeking financing beyond their own shores came to the United States to raise capital on its world-class exchanges. This migration gave the U.S. national securities authority, the SEC, indirect influence over the provision of both domestic and global securities rules. Similarly, for nearly three decades, the country has been able to directly shape and inform global banking regulations. In order to access U.S. depositors and serve companies operating in the U.S., foreign banks were compelled to establish branch offices as a source of dollar funding. In the process of setting up their outposts, they became subject to U.S. regulatory jurisdiction and rules on bank entry and operations could be leveraged to export American banking regulations.[31]

However, over the last two decades, globalization has weakened American financial dominance. Perhaps most notably, the unification of the Eurozone, notwithstanding the current monetary turmoil in Greece and other periphery nations, created the world's largest common market. And to the extent to which the European Union has established federal authority over the relevant issue area, it can be an important player in the international regulatory arena.[32] As previously demonstrated, by

31. William F. Kroener, III, *Towards Interdependence: A Decline in U.S. Dominance?*, 24 LAW & POL'Y INT'L BUS. 1135, 1136 (1993).

32. *See* Gregory C. Shaffer & Mark A. Pollack, *Hard vs. Soft Law: Alternatives, Complements, and Antagonists in International Governance*, 94 MINN. L. REV. 706, 766 (2010) (noting that where regulation is harmonized at the EU level, it can play an increasingly important entrepreneurial role in

pooling sovereignty, consumer markets, and financial markets, EU countries have been able to project policy preferences in ways once reserved for U.S. financial authorities. Indeed, the European Union has frequently been able to prod U.S. authorities to change their own domestic regulatory course—from credit rating agencies, hedge fund oversight, and accounting rules—by threatening to wield expansive forms of oversight in their own markets.

Advances in information and computer technologies have additionally spurred cross-border investment. Innovations in information technology have enabled the transmission of up-to-date data concerning securities traded on capital markets.[33] Earnings reports, government filings, and market developments can be disseminated via the web pages of issuers, financial advisors, the government, and online news services—along with instantaneous quotations on most publicly traded securities. Equally important, "[t]he new information technologies have brought instantaneous transmission, interconnectivity, and speed to the financial markets."[34] After searching for opportunities online, they can execute transactions with the click of a mouse or have financial advisors execute trades on their account, with less concern for the successfulness of execution or the distance that the trader is from the market. Advances in communications now make possible the trading on this information from anyone in the world in a matter of milliseconds. Consequently, money can instantly flow anywhere regardless of national origin and boundaries.[35]

Initially, these advances helped U.S. financial markets, largely by enabling the migration of companies to U.S. borders, especially during the tech boom of the 1990s.[36] With advances in information technology, foreign countries have been able to develop liquid capital markets and stock exchanges on their own to service capital hungry firms. This development has, by extension, enabled even large foreign multinationals to raise capital outside of the United States. This is

global governance, including in financial regulation); *see also* Karmel, *supra* note 3, at 1711 (noting that "changing economics, and in particular the migration of many international issuers to the London markets, has given the EU more power in influencing the SEC").

33. Brummer, *supra* note 8, at 1459–60 (describing changes in stock market microstructure).

34. SASKIA SASSEN, LOSING CONTROL?: SOVEREIGNTY IN AN AGE OF GLOBALIZATION 43 (1996).

35. *Id.* at 40. Indeed, as a conceptual matter, capital has always had a high "exit" potential when compared to other potential objects of regulation. Christian Tietje & Matthias Lehmann, *The Role and Prospects of International Law in Financial Regulation and Supervision*, 12 J. INT'L ECON. L. 663, 669 (2010).

36. *See* Steven M. Davidoff, *Rhetoric and Reality: A Historical Perspective on the Regulation of Foreign Private Issuers*, 79 U. CIN. L. REV. 619, 626– 27 (2010) (describing the tech boom of the 1990s).

perhaps most evident in the securities space when examining the initial public offerings of companies on exchanges outside their respective countries of domicile—so called global Initial Public Offerings (IPOs). Here, the United States has experienced a dramatic decline in its market share from 44.5% in 1996 to just 10.1% in the first nine months of 2007. It has also experienced a decline in global IPOs in terms of value, as its share has declined from 58.8% in 1996 to just 7.7% through the first nine months of 2007. And in 2007, none of the twenty largest global IPOs were done in the United States. Many of these losses over the last decade have flowed to London, which since the 1980s (and the introduction of various technological and deregulatory programs) has hosted well over three times the foreign companies than the New York Stock Exchange (NYSE). Furthermore, London exchanges have increasingly attempted to attract not only foreign listings, but also U.S. domiciled companies. In this respect, the London Stock Exchange's Alternative Investment Market (AIM) was particularly successful over the last decade, attracting thirty-seven of the forty-three U.S. companies listing solely on overseas exchanges between 2002 and 2008.[37] Increasingly, exchanges in South America and Asia are becoming players in the industry. In 2007, Brazil, Russia, India, and China (BRIC) accounted for $106.5 billion of the total $255 billion raised in IPOs worldwide.[38]

Though less data is available on the issue, economic theory suggests that globalization could similarly impair the traditional dominance of the United States with regard to banking. Although the dollar has periodically strengthened (and weakened) at different times during the crisis, financial activity continues to migrate overseas to emerging markets.[39] And with this migration, U.S. banks have followed the

37. Chris Brummer, *Corporate Law Preemption in an Age of Global Capital Markets*, 81 S. CAL. L. REV. 1067, 1093–95 (2008) ("This data becomes all the more salient when one takes into account a simultaneous decline in cross-listings in the United States. Even companies that do IPOs abroad may still cross-list their securities and in the process become subject to the country's reporting requirements and antifraud regimes. As a result, even where the United States does not capture IPOs, it could possibly capture securities transactions through secondary trading. Available data suggest[], however, that foreign markets have not only been more successful in attracting IPOs, but have also kept cross-listings from migrating to the United States. The share of U.S. cross-listings since 2000 . . . has declined dramatically. Only twelve new cross-listings were transacted on the major U.S. exchanges in 2003, the lowest number of new cross-listings since 1989. Furthermore, [the most popular forms of cross-listings were in 2004 and 2005] at their lowest level since 1992. This trend, along with the overall decline in the United States's global share of IPOs, strongly suggests a decline in both the U.S. share of securities transactions and, by extension, its market as a provider for securities laws." (internal citations and quotations omitted)).

38. *See* Olesya Dmitracova, *Emerging Markets to Boost IPO Activity in 2008—E&Y*, REUTERS, Dec. 16, 2007, *available at* http://www.reuters.com/article/idUSL1526789720071217.

39. Valentine V. Craig, *China's Opening to the World: What Does It Mean for U.S. Banks?*, 17

money and consequently are subject to foreign regulatory supervision.[40] Equally important, U.S. current account deficits have both stoked fears for the currency and calls by foreign governments and creditors to diversify out of the currency, and over time, replace it.[41]

At a minimum, the changes wrought by globalization and changing economic dynamics portend a range of important strategic implications for territorially based regulation, both for the United States and the world. First, the development of foreign capital markets has made the evasion of any one country's rules easier for many actors. Not only is there greater technical ability for capital and market participants to transact in foreign locales, but there is also greater reason to do so. More financial centers offer greater liquidity, reliable expertise, speed, and a global array of market participants. Plus customers and clients can themselves move and transact in foreign markets. As a result, territoriality as a technique has more limited repercussions than ever before. Instead of acting as an outright determinant for firms and investors, prohibitions and rules often can be evaded by moving cross-border, which, though not costless, can create a "choice of law" for market participants.[42] Thus, in response to both the United Kingdom's (UK) 2009 decision to levy higher taxes on investment bank profits, and the EU's new draft legislation on hedge funds, some have reportedly moved from the UK (and the Eurozone) altogether, to Switzerland.[43]

Additionally, financial globalization has strained the practicability of extraterritorial export. Globalization implies that more transactions are taken in more places by more individuals and firms. As a result, as it accelerates, increasing resources must be devoted to both the monitoring and enforcement of territorial rules. Enforcement in such a world becomes increasingly difficult. Often, resources will have to be devoted to the adjudication of claims and the potential explosion of cases to be settled in domestic courts. Furthermore, in order to prosecute (or sue)

BANKING REV. No. 3, at 6 n.24, Nov. 2005, *available at* http://www.fdic.gov/bank/analytical/banking/2005nov/article1.pdf (noting that foreign banks had established over 200 representative offices in China by mid-2004).

40. As recently as 2004, for example, foreign banks in China operated under licenses that restricted them to specific clients and to certain geographical areas. And even there they have been restricted to provide financial services in nonlocal currencies to foreign firms. *Id.*

41. *See, e.g.*, Jeremy Gaunt, *U.N. Panel Urges Replacing Dollar with Currency Basket*, REUTERS, Mar. 18, 2009, *available at* http://www.gata.org/node/7280 (describing calls by different governments and a United Nations panel to explore replacing the dollar with a synthetic currency).

42. *See generally* ERIN A. O'HARA & LARRY E. RIBSTEIN, THE LAW MARKET (2009).

43. Matthew Lynn, *Bankers Will Follow Hedge Funds to Switzerland*, BLOOMBERG, Oct. 13, 2001, http://www.bloomberg.com/apps/news?pid=20601039&sid=ap19tV54PWuE; Zachery Kouwe, *Europe Moves Ahead with Tough PE/Hedge Fund Regulation*, DEALBREAKER, May 7, 2010, http://dealbreaker.com/2010/05/europe-moves-ahead-with-tough-pehedge-fund-regulation/.

violators of extraterritorial laws, the assistance of foreign regulators will be needed where violators or witnesses are located abroad. Assistance may not be forthcoming because foreign counterparts may not accept or agree with the merits of the substantive rules seeking to be enforced. Such difficulties recently emerged where Germany sought to institute a ban on naked short selling of various investment instruments, and the British Financial Services Authority, declared that such a (unilateral) ban would not apply to branches of German institutions outside the country.[44]

Finally, financial globalization has helped spur greater regulatory competition and a burgeoning "market" for financial regulation.[45] This development has led to weakening of territoriality in some regards from the inside out. Thus a variety of rules, including exemptions for private placements (transactions between sophisticated investors) and offshore transactions from certain procedural and disclosure requirements, have been implemented in most developed countries explicitly to avoid the extraterritorial application of domestic securities laws. Instead, only those functions considered most key to regulatory missions are pointedly exterritorial.[46] Meanwhile, wherever financial authorities assert

44. Clara Ferreira-Marques, *FSA-German Short Ban Does Not Cover UK*, REUTERS, May 19, 2010, http://uk.reuters.com/article/idUKTRE64I1SX20100519?feedType=RSS&feedName=domesticNews.

45. *See* Brummer, *supra* note 8 (describing the "market" for securities laws enabled by financial market globalization); *see also* Eric J. Pan, *Why the World No Longer Puts Its Stock in Us* 9 (Benjamin N. Cardozo Sch. of Law, Jacob Burns Inst. for Advanced Legal Studies, Working Paper No. 176, 2006), *available at* http://papers.ssrn.com/abstract_id=951705. *See also* Jeffrey L. Dunoff & Joel P. Trachtman, *Economic Analysis of International Law*, 24 YALE J. INT'L L. 53 (1999) (noting the increasing importance of regulatory competition issues in international relations).

46. In this case, § 10(b) of the Securities Exchange Act of 1934 provides that it is "unlawful for any person . . . by the use of any means or instrumentality of interstate commerce . . . [t]o . . . employ, in connection with the purchase or sale of any [unregistered security] any manipulative or deceptive device." Securities Exchange Act of 1934, § 10(b), 48 Stat. 881, 891 (1934) (codified at 15 U.S.C. § 78j(b) (2006)). Section 3(a)(17) of the Act then defines "interstate commerce" broadly to encompass "commerce, transportation, or communication . . . between any foreign country and any State." Securities Exchange Act of 1934, § 13(a)(17), 48 Stat. 881, 882, 884 (1934) (codified at 15 U.S.C. § 78c(a)(17) (2006)). Thus any minimum contact with the U.S. "in connection with" a foreign transaction would bring the transaction within the jurisdictional scope of § 10(b) and under the jurisdiction of U.S. authorities. Because of the flexibility and potential scope of § 10(b), U.S. courts at times have been enablers of expansive extraterritorial jurisdiction by the U.S. government. For example, in *Schoenbaum v. Firstbrook*, a U.S. court held that U.S. securities laws were intended to have extraterritorial application to protect domestic investors who have purchased foreign securities on American exchanges and to protect domestic securities markets from effects of improper foreign transactions in American securities. 405 F.2d 200, 206 (2d Cir. 1968), *rev'd en banc*, 405 F.2d 215 (2d Cir. 1968). In the case, the court permitted U.S. shareholders to bring a derivative suit against a Canadian corporation for damages to the corporation resulting from the sales, in Canada, of stock to foreign purchasers under the theory that the directors and defendants conspired to defraud Banff by making Banff sell treasury shares at below their true value. *Id.* at 208. Similarly, in *United States v. Tarkoff*, U.S. courts tried a lawyer for processing illicit funds even though the violation occurred in

extraterritorial rules, either directly or indirectly, foreign firms are often excused from some of the most burdensome or costly compliance requirements.

C. The Impact of the Financial Crisis on Territorial Power: A Global Perspective

At least initially in the wake of the 2008 financial crisis, some question arose as to the sustainability of the "rise of the rest" and the continued growth of non-U.S. (and indeed, non-Western) financial centers. This is because although the 2008 crisis originated in mature markets, and exchanges in New York and London fell to historic lows, the financial fallout from the crisis quickly spread around the world. The McKinsey Global Institute recently reported that in emerging markets, the total value of financial assets fell $5.8 trillion in 2008, a loss of 15%.[47] Meanwhile, capital flows to developing countries, both in the form of portfolio investment and foreign direct investment, plunged 39%.[48] As foreign lending flows reversed, and debt and equity flows diminished, the cost of fund-raising skyrocketed in many emerging economies.[49] For this reason, it was at least theoretically possible that countries would suffer long-term capital flow reversals reminiscent of those arising in the wake of the Asian and South American financial crises of the 1990s.

However, the year 2009 brought about wholesale reversals in these trends. After a weak first quarter, private capital flows to emerging markets resumed and quickly gathered pace in the second, third, and fourth quarters.[50] Much of this investment took the form of portfolio investment, with emerging market mutual funds attracting a record $80 billion during the year.[51] Meanwhile, global IPO activity picked up, especially in Asia, where the Shanghai and Hong Kong exchanges have been important gateways to capital for Chinese corporations seeking relatively low cost, low disclosure venues for offerings. As a result, in 2009, China was the world's largest IPO market,[52] just as BRIC

Israel with an Israeli bank and the only connection with the U.S. was that the Israeli bank transactions required telephone communication between Israel and Miami, Florida, and between Miami, Florida and Curacao, to arrange for the transfer of funds from Curacao to Israel. 242 F.3d 991, 995 (11th Cir. 2001).

47. MCKINSEY GLOBAL INST., GLOBAL CAPITAL MARKETS: ENTERING A NEW ERA 27 (2009).

48. *Id.*

49. *Id.*

50. J. Alex Tarquinio, *Emerging Markets Make a Comeback*, NY TIMES, Oct. 11, 2009, at 14; Conrad de Aenlle, *Emerging Markets Regain Footing*, NY TIMES, July 12, 2009, at 14.

51. Tim Gray, *How to Gauge the Rush to Emerging Markets*, NY TIMES, Jan. 10, 2010, at 14.

52. *See* Vivian Wai-yin Kwok, *China: The World's Biggest IPO Market*, FORBES, Sept. 29,

countries accounted for 76% of global IPO activity during the first month of 2010.[53]

The flow of money back to emerging markets is explained by a general lack of confidence in the economies of developed countries, specifically in the United States and Europe, causing investors to seek greener pastures in less traditional locales. In short, emerging markets exhibit better growth prospects given their advantageous economic fundamentals. Due to global trade imbalances, many emerging countries have larger foreign reserves, less sovereign indebtedness, and superior household finances and savings rates than their more developed counterparties.[54] As a result, global investors are more confident in emerging markets' ability to grow in spite of economic malaise in the United States and Europe, an optimism grounded in both real and expected growth in the Gross Domestic Product (GDP) of emerging economies.[55]

Additionally, the maturation of many foreign financial centers has appealed to some investors, who previously viewed emerging markets only as risky or speculative investment locales. Most commentators agree that Asian securities markets, though far from perfect, have come a long way in regards to disclosure and regulatory supervision. For instance, since 1998, China has created a central securities regulator, promulgated its first securities law, reduced the number of non-tradable, state-owned shares in its equity markets, and relaxed restrictions on foreign institutional investors seeking to invest in its markets. Brazil has also taken steps to strengthen the reputation of its financial markets: In 2001, the World Bank announced a $14.46 million loan to Brazil to help it strengthen its Central Bank and Securities Commission, and the country has also been working to improve corporate governance and investor voting rights in connection with a set of priority initiatives promulgated by the Organisation for Economic Co-Operation and Development (OECD).

These regulatory reforms in the securities law coincide with ostensibly well-keeled regulatory supervision of banking sectors in some emerging markets. In Asia, in particular, depositary institutions have thus far fared well in the wake of the crisis, even as some question their

2009.

53. *See* Sujata Rao, *BRIC IPOs See Record January at $6.7 Billion*, REUTERS, Jan. 27, 2010.

54. *See* John Stepek, *Emerging Markets Will Be the Winners From This Crisis*, MONEYWEEK, June 15, 2009, *available at* http://www.moneyweek.com/news-and-charts/economics/emerging-markets-will-be-the-winners-from-this-crisis-15672.aspx.

55. David Oakley & Christopher Brown-Humes, *Emerging Market Debt Benefits From Greek Woes*, FIN. TIMES, Apr. 29, 2010, *available at* http://www.ft.com/cms/s/0/04129faa-53bb-11df-aba0-00144feab49a.html.

domestic banking practices.[56] With presumably more conservative lending standards and lessons learned from the Asian financial crisis, banks in the region are asserting themselves as more prudent than their Western counterparts. Only 5% of the approximately $500 billion write-off by banks globally from January to August 2008 were done so by Asian banks.[57] Instead, banks in North America accounted for half of the total write-offs; according to Bloomberg, banks in the United States accounted for half, and European banks accounted for 45%.[58] This success has helped lend a veneer of credibility and stability to the entire financial system and have helped encourage capital flows to the region as well as Asia's increasing influence as an international lender. Not surprisingly, many industry observers expect this trend to continue into 2010, with net private capital flows to emerging markets expected to exceed $670 billion, and even more over the next decade helping to fuel dramatic growth in emerging market GDP.[59]

Assuming this track record remains untarnished, which at the time of this writing is unknown, these developments will likely serve to only exacerbate changes in the global political economy previously outlined.[60] On the one hand, mobile market participants will continue to have expanded choice as to where they seek capital, and in some instances, what rules govern their transactions. Furthermore, countries that were once only remote destinations for capital now wield more regulatory clout and are better positioned to check extraterritorial exertions of influence by traditionally leading countries. Thus, for example, the United States now imposes regulatory standards on foreign companies by means of its own capital market activity; regulators in not

56. *See* Chia-Peck Wong, *China Property Prices Jump, Highlighting Bubble Risk*, BLOOMBERG, Mar. 10, 2010, *available at* http://www.bloomberg.com/apps/news?pid=20601206&sid=aO9xOGXjsJUo.

57. *See* Capital Guardian Trust Co., *Asian Financials: Time to Shine in China and Hong Kong*, TO THE POINT, Oct. 2009, *available at* https://server.capgroup.com/capgroup/action/getContent/file/GIG/North_America/Market_Insights/Capitals_Views/TTP_AsiaChina_1009_CG.pdf.

58. *Id.*

59. *See, e.g.*, INST. OF INT'L FIN., CAPITAL FLOWS TO EMERGING MARKET ECONOMIES (2009), *available at* http://www.iif.com/press/press+119.php; Gillian Tett, *Bankers Sense Shift in Capital Flows*, FIN. TIMES, Jan. 22, 2010, at 6, *available at* http://www.ft.com/cms/s/0/bd0cb8e6-06f5-11df-b058-00144feabdc0.html.

60. It is after all notable that China in particular may face significant write-offs with regard to its own imprudent domestic lending in real estate, much like the U.S. Vishesh Kumar, *China Curbs Bank Loans as Asset Bubble Worries Grow*, DAILYFINANCE, Jan. 20, 2010, *available at* http://www.dailyfinance.com/story/china-curbs-bank-loans-amid-bubble-worries/19324151/. Some experts contend, however, that even in the event of such bubbles "bursting," the domestic fallout would be considerably less than that in the 2008 crisis in the U.S. Katie Benner, *What Happens if China's 'Bubble' Pops?*, FORTUNE, Feb. 5, 2010, *available at* http://money.cnn.com/2010/02/05/news/international/china_bubbles.fortune/index.htm.

only Europe, but also Asia and even South America increasingly enjoy their own exterritorial reach through their domestic capital and consumer markets and can affect the operations of U.S. multinationals to a historically unprecedented extent.[61] As a result, greater reflection is required by regulators of the traditionally dominant financial centers when they attempt to unilaterally solve global capital markets challenges—and indeed even domestic capital market challenges.

III. THE FUTURE OF TERRITORIAL REGULATION

Multipolarity in the international system will have important implications for the regulatory strategies pursued by national authorities. First, it will generate pressures for greater international coordination, which will reflect a new democratic distribution of economic and territorial power. Second, national authorities will draw on new strategies that help leverage both their historical prestige and residual financial power. Yet even with both developments, territoriality will remain an important factor informing regulatory export.

A. Greater International Coordination

Perhaps most obviously, there will be a greater dependence on international regulatory coordination. Administrative agencies, once content with largely domestic regulatory strategies, have hired personnel with not only market know how, but also foreign policy expertise as foreign policy analysts, experts and area-specialists often work alongside traditional regulators and enjoy civil service tenure. Moreover, the general trend of technocratic control has accelerated via further specialization by and in regulatory agencies. Virtually every regulatory agency charged with domestic supervisory responsibilities—whether it be financial ministries, securities regulators or banking authorities—has instituted an "office of international affairs" of some sort to spearhead cooperation efforts with international homologues. A key aspect of such work involves the promotion of national policy preferences abroad, a charge that often involves both persuading homologues to regulate in ways that are consonant with the policy

61. As in other forms of extraterritoriality, the policy consequences have been most obvious in the antitrust space, where China is increasingly blocking international deals with only secondary implications for its markets. Editorial, *Antitrust in China*, FIN. TIMES, May 4, 2009 (noting that China's Ministry of Commerce imposed restrictions on the $1.6 billion takeover by Japan's Mitsubishi Rayon of the UK's Lucite international, forcing the latter to sell half of its production of one polymer at cost, as well as restrictions on InBev's $52 billion acquisition of Anheuser-Busch).

preferences of the respective administrative agency.

Regulators have also revamped efforts aimed at achieving broader, global forms of international coordination. In 2008, just as the U.S. financial crisis blossomed into a cross-border, international economic event, regulators undertook a variety of efforts to revive and reorganize the global financial architecture. For example, the G-20 has been christened the primary body for international financial decisionmaking, in effect superseding the erstwhile dominance of the G-7 and expanding the number of countries with input on the global regulatory agenda.[62] Meanwhile, the Financial Stability Forum has been reorganized as the Financial Stability Board to promote international financial stability through better information exchange and international cooperation.[63] The mandate of the new organization focuses on monitoring potential risks in the economy, especially those involving the biggest firms, and will conduct periodic reviews of firms to spot potential trouble and report possible threats to the stability of the global financial system to the G-20 finance ministers, the IMF, and central bank governors. It will also act as a clearing house for information-sharing and contingency planning for the benefit of its members.[64]

Greater international coordination is envisioned to help achieve a range of international regulatory goals. First, it helps achieve better information sharing among regulators. In that way, greater trust can be achieved as well as points of common interest.[65] Second, international organizations can help craft norms that can help influence the norms and expectations of investors as to what practices market participants should be complying with. Finally, to the extent coordination is institutionalized, new reputational and institutional disciplines can be generated that provide new incentives for regulators and markets alike to comply with high international standards.

B. The Strategic Redeployment of Soft and Hard Power

Regulatory authorities are also seeking to leverage their soft and hard power more strategically than ever before. To heighten their powers of

62. What is the G-20, http://www.g20.org/about_what_is_g20.aspx (last visited Sept. 29, 2010) (describing the G-20's mandate).

63. *See* Eilís Ferran & Kern Alexander, *Soft Institutions and Hard-Edged Power: What Role for the European Systemic Risk Board?* (2010) (unpublished manuscript) (on file with author).

64. Fin. Stability Bd., Mandate, http://www.financialstabilityboard.org/about/mandate.htm (last visited Sept. 1, 2009).

65. *See* Rolf H. Weber, *Multilayered Governance in International Financial Regulation and Supervision*, 13 J. INT'L. ECON. L. 683, 696 (2010) (noting that international laws help mitigate potential conflicts between national regulators and increase the potential for mutual reliance).

persuasion, they have, for example, increased outreach efforts with developing and emerging markets. In this regard, technical assistance programs have been particularly successful instruments of soft power. By providing guidance to other, usually less developed, counterparts in developing markets on issues relating to financial sector development, regulatory authorities have enhanced their ability to promulgate policy preferences in less confrontational low-level forums. They are also able to bolster the prestige of their agency in the international community of regulators.

Some regulators are also seeking to exercise extraterritorial influence in ways more amenable to foreign jurisdictions. For example, consider the SEC's "mutual recognition" program launched as a direct regulatory response to financial globalization.[66] This program—formally initiated in 2008 as a pilot project with Australia, though stalled in the wake of the credit crisis—works, in ways akin to "extraterritorial territoriality," to affect the behavior of both market participants and their regulators. It works against a deregulatory backdrop, instead of as a new and potentially unwelcome extraterritorial projection of power: as opposed to imposing stricter guidelines on firms and exporting them abroad, the purpose of the program is to offer relevant market participants ways to escape U.S. territorial control.

Specifically, instead of being subject to direct SEC supervision, foreign stock exchanges and foreign broker–dealers would apply for an exemption from SEC registration based on their compliance with foreign regulations deemed to be comparable to those in the United States. To establish a framework for such exemptions, the SEC would, along with its foreign counterpart, sign a non-binding mutual recognition "arrangement" laying out in basic terms their intent to liberalize market integration. At the same time, memoranda of understanding would be signed allowing for enhanced enforcement cooperation and information-sharing.[67] This arrangement would also contain an undertaking by the foreign regulator "describing in detail how certain regulatory preconditions required by the SEC are met, and a similar undertaking by the SEC providing for reciprocity."[68] Once the SEC blessed the laws of their home jurisdictions, stock exchanges and broker–dealers in those countries would then be permitted to apply for exemption from SEC registration based on their compliance with their home state laws, and

66. For a description of the mutual recognition program, see generally Ethiopis Tafara & Robert J. Peterson, *A Blueprint for Cross-Border Access to U.S. Investors: A New International Framework*, 48 HARV. INT'L L.J. 31 (2007).

67. *Id.* at 32.

68. *Id.* at 56.

shares traded on or through them, could be marketed and sold to U.S. investors without complying with U.S. disclosure and corporate governance rules.[69]

Although the SEC's mutual recognition program could, if ultimately implemented, significantly liberalize U.S. markets, the architects of the program ultimately view the program as providing key incentives for foreign counterparts to adopt U.S.-style regulations. Despite the fact that convergence in some instances might be costly or involve the adoption of rules that are contrary to a regulator's traditions or philosophy, the regulator's domestic market participants could potentially enjoy a range of important competitive advantages, especially over other market participants in non-participating jurisdictions. They would not have to register their securities to access capital markets in the United States. Instead, only compliance with their home state regulator would be required. Furthermore, exchanges in the complying jurisdiction could also potentially enjoy greater liquidity. Regulators hope these advantages would change the net payoffs for regulators such that the importation of U.S. law is the preferred policy choice.

Whether, by itself, capital market access can comprise a meaningful lever for change is far from clear. As a policy strategy, it will only work in a finite number of circumstances. First, mutual recognition likely works best on a bilateral basis where a regulator of a big, capital rich market, offers a mutual recognition policy with the regulator of a smaller market with capital hungry firms seeking to raise money from overseas markets. In such circumstances, the regulator of the smaller market will likely find it acceptable that its firms make some adjustments in order to access clients, customers, and investors abroad. Agreements between regulators of large or rapidly growing markets may be difficult, given the aggregate adjustment costs of firms in the adjusting regulator's market.

Otherwise, mutual recognition programs will only be feasible where adjustment costs for the target regulator are low. This will be the case either where standards by the rules-exporting regulator are softened, or where (as with Australia's mutual recognition agreements with New Zealand and the United States) jurisdictions already share largely similar regulatory regimes and thus requiring only small adjustment costs. In either scenario, the use value of capital markets incentives weakens. The fewer the requirements for mutual recognition, the fewer the number of required regulatory concessions an exporting jurisdiction

69. Brummer, *supra* note 8, at 1454.

must make. Meanwhile, if countries are already similar, then the value derived from mutual recognition as a leverage instrument is limited and should be better recognized and understood as a mechanism for market liberalization, and potentially, the decline of state intervention.

C. "Conserved" Territoriality

The limitations of even regulatory suasion returns us to the basic observations outlined at the outset of this Section: unilateral, territorially based regulatory export is increasingly difficult—both practically and politically. As emerging economies grow and as the global distribution of economic and financial power evolves, the reputational costs of export become more significant just as enforcement of territorial rules abroad becomes more difficult.

Nevertheless, territoriality remains a key factor of regulatory power—and indeed international regulatory affairs. Nation–states—and by extension, regulatory agencies—still wield total formal authority over resources and capabilities in their territories. As a result, international or global standards must be agreed upon domestic members and implemented on a national basis. Indeed, for this reason, in the wake of the crisis, new reforms reflect an emphasis not so much on strengthening formal international organizations, but instead on the "softer" process of international coordination and cooperation.[70]

Moreover, the evolving allocation of financial capital and resources merely changes the calculus of regulatory power as others come to wield influence in their own right. In many ways, the burgeoning, multipolar world of financial regulation operates along what can be considered a "conservation theory" of international financial law insofar as regulatory power is not so much destroyed, but transferred. In practical terms, this means that although some actors, like the United States and the EU, may experience diminished powers of extraterritorial export, others will be able to enjoy greater national economic sovereignty insofar as perceived interference or intermeddling by other national authorities are reduced. Furthermore, new regulatory capabilities are becoming available to other countries and regions that allow them to project power and influence in ways that were once only enjoyed by the United States

Changes in the global financial economy can shift the burden of non-cooperation. To the extent to which agreement cannot be reached between regulators, the costs of discensus, once at least partially evaded

70. Mario Giovanoli, *The Reform of the International Financial Architecture After the Global Crisis*, 42 N.Y.U. J. INT'L L. & POL. 81, 90–91 (2009).

by traditional regulatory superpowers like the United States, who could export de jure or de facto their preferences with few repercussions, are now internalized as independent responses by other regulators and can increasingly affect the welfare and profitability of domestic firms. As a result, territoriality helps reshape the incentives and bargaining power of regulatory actors on the international stage.

Globalization does not, however, necessarily mean that interests between regulatory authorities are themselves becoming "polarized." In some instances, the development of domestic markets and stakeholders may drive countries towards a convergence of interests, especially with regards to the regulation of practices that hold broadly negative economic or financial consequences. Furthermore, as financial centers develop and gain breadth, the interests of regulators and market participants may change as countries transition to more broadly accepted standards in order to enhance their legitimacy or to improve the reputation of domestic financial services. On the other hand, where regulatory practices diverging from international standards are viewed as the primary drivers to a financial center's success, its regulators may resist standards more rigorously.

Yet financial globalization highlights in stark terms, especially in the wake of the crisis, that no one regulator can singlehandedly impose its will globally on all actors, all the time. Territoriality can help project power, but ultimately it, like extraterritoriality itself, does not ensure it. This is because territoriality both defines and is defined by financial power. Regulators exercise through their markets capabilities that are checked directly and indirectly by the regulatory power engendered by the strength of other foreign markets. As a result, regulators across national boundaries are increasingly interdependent not only from the standpoint of affirmative regulatory governance, but also from the perspective of strategic deference from one another—both with regards to their territorial and directly extraterritorial activities—so as not to unduly undermine one another's supervisory activities or the activities of regulated firms.

CONCLUSION

Territoriality is a remarkably complex regulatory strategy in an age of financial globalization. Long employed to describe the confinement of regulatory power to national borders, territoriality actually constitutes a diverse array of strategies used by national regulators to exert regulatory authority over often mobile market participants. It is not only a limit of state power, but can also operate as the means by which regulatory power is projected beyond national borders, especially for countries enjoying large capital and customer markets. This Article argues that the implications of territoriality are rapidly evolving. Formerly dominant regulatory powers are witnessing the weakening of the territorial approach to both domestic and international influence, whereas others are discovering within their borders more meaningful and significant levers of global regulatory power. These challenges, which have only accelerated in the wake of the crisis, have spurred new efforts at international coordination and innovative initiatives among traditional regulatory leaders aimed at leveraging their residual hard and soft power to promote their national policy preferences abroad. Yet even here territoriality will remain an important factor informing the coordination process.