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of Securities Law in Haven Jurisdictions Palm Trees Hide More than Sunshine: The Extraterritorial Application

Howard S. Eberstein

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Palm Trees Hide More Than Sunshine: The Extraterritorial Application of Securities Laws in Haven Jurisdictions

Howard S. Erbstein*

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SECURITIES LAWS IN HAVEN JURISDICTIONS

I. Introduction

The year 1986 did not bode well for investment banker Dennis Levine. In a civil injunctive action¹ the Securities and Exchange Commission (SEC) alleged that Levine, through an insider trading scheme, violated several antifraud provisions of the Securities Exchange Act of 1934.² Without admitting or denying that he obtained over \$12 million in illicit profits from secretly trading in the securities of fifty-four companies, the brazen Levine settled the SEC action and was ordered to disgorge over \$10 million to the court.³

Ostensibly, this judgment is a footnote to 1980s avarice. A more critical look, however, reveals legally-sanctioned instruments that threaten the integrity of securities markets everywhere. Levine executed his unlawful trades through two Panamanian shell companies and a Bahamian bank account.⁴ For some time, these nondisclosure instruments provided Levine with access to U.S. securities markets and anonymity from U.S. securities regulators.⁵

More disturbing is the fact that if the offshore bankers had not destroyed various documents in their attempt to scuttle the initial SEC inquiry, Levine might never have been incarcerated.⁶ By destroying documents, the bank made itself vulnerable to U.S. prosecution for obstruction of justice. The destruction of evidence placed the bankers in a legal *cul-de-sac*. Had the bankers avoided this cloak and dagger episode, they would have done nothing illegal and at the very least, the SEC would have been tied up for years in the Bahamian courts trying to force disclosure of Levine's name. Levine was apprehended because a variety of circumstances fermented and not through any comprehensive regulation of haven⁷ jurisdictions. Serendipity was a prominent element in Levine's ultimate apprehension.

This anecdote represents the potential bottleneck that U.S. securities regulators face when investigating insider trading violations commenced in haven jurisdictions. When an alleged securities law violation is being investigated, the SEC typically requests trading information from the

1. SEC v. Levine, Fed. Sec. L. Rep. (CCH) ¶ 92717 (S.D.N.Y. 1986), *rev'd and remanded on other grounds*, 881 F.2d 1165 (2d Cir. 1989).

2. 15 U.S.C. §§ 77a-80c-3 (1988).

3. See SEC v. Levine, Fed. Sec. L. Rep. (CCH) ¶ 92717 (S.D.N.Y. 1986), *rev'd and remanded on other grounds*, 881 F.2d 1165 (2d Cir. 1989).

4. *Id.*

5. *Id.*

6. J. STEWART, DEN OF THIEVES 242 (1991).

7. The terms "haven" and "offshore" will be used interchangeably throughout this article.

broker involved and its customer. Yet, where the customer is a bank located in a foreign country — that is, where the bank trades on behalf of an investor for whom it acts as custodian — the request is often denied on the ground that disclosure would violate bank secrecy laws.⁸

The purpose of this article is to analyze bank secrecy and regulatory disclosure, two conflicting objectives that arise in the situation where voluntary compliance with an SEC request for customer information is refused by reason of bank secrecy law. Part II, through an analysis of the relevant case law, illustrates how offshore courts actively resist U.S. attempts to undermine their sovereignty on the issue of bank secrecy. Given this reluctance to release information, Part III critically evaluates litigation, one of the principal methods U.S. authorities have used to extract information. In light of the internationalization of markets, Part IV concludes by initiating discussion on how the competing objectives of preserving customer confidentiality and disclosing offshore trading information should be resolved.

II. Barriers to Regulation

A. Overview

U.S. case law generously supports the assertion that bank secrecy laws inhibit the supervision of securities markets.⁹ The preponderance of academic literature examines the offshore problem from the view of the frustrated securities regulator. When the literature does examine the problem from the perspective of the haven jurisdiction, it often entails an analysis of civil law provisions.¹⁰ The purpose of this section, however, is to illustrate, using the Bahamas as a case study, how a common law secrecy haven justifies the primacy of the banker's duty of secrecy over a foreign subpoena to produce documents in a foreign court. For the sake of clarity, this section divides its discussion into six substantive subsections. Subpart B examines the common problem faced by haven banks that execute transactions on U.S. securities markets, namely an

8. Bank secrecy laws protect the confidentiality of information held by financial institutions. These laws prohibit the disclosure of bank customer identity, business records, and other details relating to a customer's bank account. EXCHANGE ACT RELEASE NO. 21186 (July 30, 1984), reprinted in [1983-1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 86,980.

9. See, e.g., *Bank of Nova Scotia v. United States*, 691 F.2d 1384 (11th Cir. 1982), cert. denied, 462 U.S. 1119 (1983); *SEC v. Levine*, Fed. Sec. L. Rep. (CCH) ¶ 92717 (S.D.N.Y. 1986), rev'd and remanded on other grounds, 881 F.2d 1165 (2d Cir. 1989); *SEC v. Banca Della Svizzera Italiana*, 92 F.R.D. 111, 117 (S.D.N.Y., 1981).

10. See, e.g., Bernhard F. Meyer, *Swiss Banking Secrecy and its Legal Implications in the United States*, 14 NEW ENG. L. REV. 18 (1978).

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exposure to U.S. court orders and liability to civil and criminal penalties in the haven. Subpart C identifies the institutional rationales for bank secrecy. Against this backdrop, subparts D through G offer a clinical analysis of common law bank secrecy in the Bahamas, specifically demonstrating how offshore courts negatively respond to the thinly-veiled attempts of U.S. authorities to undermine their sovereignty on the issue of bank secrecy with investigative subpoenas.

B. The Problem: Jurisdictional Conflict

The international marketplace dictates that multinational enterprises must necessarily function in at least two sovereign states to remain competitive. When the laws of those two or more states conflict, the enterprise's legal responsibilities become more onerous.¹¹ This conflict is apparent in bank secrecy laws, insofar as many banks maintain offices in countries around the world. Frequently, issues involving the affairs of a customer arise in state A concerning his transactions in the offshore jurisdiction of state B. For example, the New York office of a U.S. bank may be asked by a U.S. court to supply customer information kept at its Nassau office. This information, however, enjoys privileged status under Bahamian secrecy laws. Operating under two jurisdictions, — the U.S. jurisdiction, under which the bank maintains its headquarters and the Bahamian jurisdiction, where the requested information is kept — the bank is in a most unenviable position. In short, the bank is caught between Scylla and Charybdis.

Hence, jurisdictional questions, coupled with issues of sovereignty, vex multinational banking enterprises. It is worthwhile, therefore, to begin by considering some of the theoretical aspects of jurisdiction and sovereignty before an analysis is undertaken of their practical implications.

It is said that sovereignty constitutes the supreme authority in an independent political society.¹² The related concept of jurisdiction can be defined as the capacity of a state under international law to govern people and property by its municipal law.¹³ It includes both the power to make laws (prescriptive jurisdiction) and the power to ensure compliance with them (enforcement jurisdiction).¹⁴ The question of jurisdiction was addressed by the Permanent Court of International Justice

11. Henry Harfield, *The Implications of U.S. Extraterritorial Discovery Proceedings Against Multinational Corporations for the Judiciary*, 16 N.Y.U. J. INT'L L. & POL. 973, 974 (1984).

12. WILLIAM W. BISHOP, *CASES AND MATERIALS ON INTERNATIONAL LAW* 11 (1971).

13. D.J. HARRIS, *CASES AND MATERIALS ON INTERNATIONAL LAW* 250 (4th ed. 1991).

14. *Id.*

in the *Lotus Case*.¹⁵ Here, the court determined that "the first and foremost restriction imposed by international law upon a state is that . . . it may not exercise its power in any form in the territory of another state."¹⁶

Orthodox positions on jurisdiction and sovereignty have, to some extent, been realigned in light of more recent concepts such as the effects doctrine. This doctrine is characterized by the approach that, irrespective of where the conduct in question occurs, if it sufficiently affects a state's trading markets, jurisdictional assertion is justified.¹⁷ The United States has aggressively employed this doctrine. The classic statement of the American doctrine is found in *United States v. Aluminum Company of America*,¹⁸ in which the court claimed that "any state may impose liabilities, even upon persons not within its allegiance, for conduct outside its borders that has consequences within its borders which the state reprehends."¹⁹ While other grounds for claiming jurisdiction can be advanced, the effects doctrine remains the most prevalent basis used by the United States to justify the extraterritorial application of its laws.²⁰

Notwithstanding any theoretical objections that could be advanced against the effects doctrine, the practical implications are that it largely ignores the concerns of other jurisdictions. A cursory examination of the definition of extraterritoriality emphasizes the point. Extraterritoriality may be defined as "[a] legal fiction by which certain persons and things are deemed for the purpose of jurisdiction and control to be outside the territory of the State in which they really are and within that of some other State."²¹ It should come as no surprise, then, that extraterritorial reach is often viewed as an assault on the other state's sovereignty. As implied above, inherent in the definition of enforcement jurisdiction is that a state's judicial reach is limited by its territorial boundaries. The effects doctrine operates as an exception to this principle. In matters of economic significance, however, states are simply unwilling to concede elements of their sovereignty to another state.

The issue of Bahamian sovereignty in the financial services sphere, for example, has been jealously guarded by the Bahamian judiciary. The most recent decision of the Bahamian Supreme Court, *Re Bank of*

15. 1927 P.C.I.J. (ser. A) No. 10 (1927).

16. M.I. DIXON, *TEXTBOOK ON INTERNATIONAL LAW* 115 (1990).

17. *Id.* at 443-44.

18. *United States v. Aluminum Company of America*, 148 F.2d 416 (2d Cir. 1945).

19. *Id.* at 443.

20. Donald K. Charter & Stanley M. Beck, Q.C., *Problems of Enforcement in the Multinational Securities Market*, 9 U. PA. J. INT'L L. 467, 469 (1987).

21. R. BIRD, *OSBORN'S CONCISE LAW DICTIONARY* 142 (7th ed. 1983).

America,²² illustrates the commitment of the judiciary to bank secrecy laws. Here, the court embraced the principles of economic sovereignty attested to by James Smith, Governor of the Central Bank of the Bahamas.²³ Smith argued that the banking industry was one of the largest and most important sectors of the economy and if the industry's success was to continue, it was imperative that bank secrecy be maintained.²⁴ In particular, Smith believed that "[t]he country's success in providing offshore financial services has been impaired by seriously increased competition internationally during the last decade. To engender investments in the offshore financial sector and remain competitive, the confidentiality of financial transactions must be preserved."²⁵

Based on the foregoing, it is clear that the question of jurisdiction is complex. It attempts to assimilate the conflicting principles of state sovereignty, equality of states, and non-intervention in the domestic affairs of other states. The extent to which states police financial fraud will necessarily be based on their willingness to do so, as well as their practical capabilities. Although international law concepts of jurisdiction assist in supplying a new classification of potential theories, in practice, it is the actions states pursue that provide the critical insight.²⁶ For this reason, Subparts D through G provide a clinical assessment of Bahamian practice in dealing with U.S. subpoenas and Part III discusses actual SEC practices.

C. Institutional Justifications for Bank Secrecy

Apart from the common law duty of secrecy,²⁷ institutional or entrenched justifications for bank secrecy are rooted in civilian jurisprudence. For analytical purposes, the justifications can be grouped into three categories: (1) the preservation of confidential relationships; (2) the protection of financial assets; and (3) the enhancement of the domestic banking industry.²⁸

22. Civ. No. 923 (Bah. Sup. Ct. 1993) (unreported) (copy on file with author).

23. *See id.*

24. *Id.*

25. *Id.*

26. J. Breslin, *Extraterritorial Control of Securities Fraud* 14 (1989) (unpublished Ph.D. thesis, on file at the University of Cambridge) (copy on file with author).

27. *See infra* part II.F.

28. Harvey L. Pitt et al., *Problems of Enforcement in the Multinational Securities Market*, 9 U. PA. J. INT'L BUS. L. 315, 405-06 (1987); *see also* J. SUTER, *THE REGULATION OF INSIDER DEALING IN BRITAIN* 356 (1989).

Principles of bank secrecy originated in early Roman and Germanic law as an aspect of the right to privacy.²⁹ Many civil law jurisdictions have since considered financial privacy to be a central tenet of individual liberty and freedom. The Swiss Civil Code and the Code of Obligations, for example, recognize that every individual is entitled to *Geheimsphäre* (a sphere of secrecy) that is protected against public disclosure.³⁰ One of the individual rights within the *Geheimsphäre* is bank secrecy.³¹

Financial security is among the most important reasons advanced for bank secrecy laws.³² Because there is generally no taxation or exchange control in the Gulf states, two prevailing reasons for the use of bank secrecy jurisdictions, one could assert that financial security is the only explanation for the considerable flow of funds both to and through Switzerland from the Middle East.³³

The skeptic, however, would argue that although bank secrecy historically has been a legitimate response to the sanctity of individual rights, the enduring vitality of bank secrecy can be attributed to economic factors.³⁴ The leaders of developing countries need only perform a brief study of Switzerland to see that its bank secrecy laws have made it one of the world's leading financial centers. Understandably, many countries would like to emulate Switzerland's success.

D. Case Study of Common Law Bank Secrecy Haven: The Bahamas

A number of bank secrecy havens permeate the globe. In order to effect a detailed analysis of common law bank secrecy *per se*, rather than execute a descriptive survey of the various bank secrecy havens that exist, this article will focus on one jurisdiction. The Bahamas is salient for three reasons. First, a number of U.S. cases suggests that the jurisdiction has played a notable role in both the concealment of insider trading and

29. See, e.g., EDOUARD CHAMBOST, A WORLD GUIDE TO CONFIDENTIALITY (1983). Chambost is a French lawyer who has written extensively on offshore banking.

30. J. Lifin, *Our Playing Field, Our Rules: An Analysis of the SEC's Waiver by Conduct Approach*, 11 BROOK. J. INT'L L. 530 (1985).

31. *Id.*

32. CHAMBOST, *supra* note 29, at 10.

33. See CHAMBOST, *supra* note 29. Cf. SEC v. Banca Della Svizzera Italiana, 92 F.R.D. 111 (S.D.N.Y. 1981). This case demonstrated that Kuwaiti businessmen indeed found stability in Swiss banks. However, they also found anonymity to purchase call options with inside information. Accordingly, Chambost's affirmation must be questioned.

34. In 1983, over 425 banks were operating in the Cayman Islands. Their initial and annual licensing fees accounted for 20% of the colony's budget. In 1964, the Cayman Islands had two local banks and practically no offshore business. Ostensibly, the change in fortunes is due to the 1966 enactment of bank secrecy legislation. STAFF OF PERMANENT SUBCOMMITTEE ON INVESTIGATIONS OF SENATE COMMITTEE ON GOVERNMENTAL AFFAIRS, CRIME AND SECRECY: THE USE OF OFFSHORE BANKS AND COMPANIES 30-31, app. 3 (1983).

the laundering of illicit funds.³⁵ Second, the Bahamas is strategically placed to offer offshore financial services. Geographically, the Bahamas is situated between two affluent continents, with Canada and the United States to the north and Central and South America, with their petrodollars and emerging securities markets to the south.³⁶ On a temporal plane, the Bahamas falls within the eastern time zone, home to the New York Stock Exchange. Third, the financial services industry is the *cause célèbre* of the Bahamian economy.³⁷ Indeed, the Bahamian financial services industry is committed to entrench bank secrecy, as it is perceived to be a pillar of financial development.³⁸ The view of many in the Bahamian financial services industry is perhaps best summarized by analogy to the Swiss position, explained by Alfred Sarasin, former President of the Swiss Association of Bankers: "The Swiss financial position is not a product of banking secrecy. *But if it did not exist, our country would no longer be a serious competitor in the international competition between the financial centres of the world.*"³⁹ The same

35. See, e.g., SEC v. Levine, Fed. Sec. L. Rep. (CCH) ¶ 92717 (S.D.N.Y. 1986), *rev'd and remanded on other grounds*, 881 F.2d 1165 (2d Cir. 1989); Bank of Nova Scotia v. United States, 691 F.2d 1384 (11th Cir. 1982), *cert. denied*, 462 U.S. 1119 (1983); United States v. Becker, 569 F.2d 951 (5th Cir. 1978); United States v. Sand, 541 F.2d 1370 (9th Cir., 1976).

36. R. JOHNS, TAX HAVENS AND OFFSHORE FINANCE 191 (1983).

37. In the late 1980s, Prime Minister Pindling initiated a program of new financial legislation aimed at winning back customers lost to rival offshore jurisdictions. To oversee the program, a Financial Services Secretariat was established within the Ministry of Finance to, among other things, identify and encourage all types of financial services available within the Bahamas — whether in banking law, accounting, insurance, corporate and trust services and tax avoidance.

38. Confidentiality, the foundation of bank secrecy, permeates Nassau's -Bay Street, the Bahamian equivalent of the Square Mile. The Bahamian attitude is conveniently summarized in a 1977 speech given by Donald Fleming, former president of the Bank of Nova Scotia Trust Company, to the Bahamian Chamber of Commerce:

The secrecy attached to relations and transactions between financial institutions and their clients has been another factor essential in the attraction of financial business. . . . Any lessening of this guarantee would harm the interests of the Bahamas, and any strengthening of it would bolster them.

Donald Fleming, Former President of the Bank of Nova Scotia Trust Company of the Bahamas, Address Before the Bahamian Chamber of Commerce (1977).

Recent legislative evidence of the commitment to secrecy is found in the International Business Companies Act of 1990 [hereinafter IBC Act]. GOVERNMENT OF THE COMMONWEALTH OF THE BAHAMAS, INTERNATIONAL BUSINESS COMPANIES OF THE BAHAMAS 7 (1990). An IBC is a Bahamian-incorporated company that does not carry on business in the Bahamas. *Id.* There are two main aspects of an IBC that afford the members of a company a high degree of confidentiality: (1) There is no requirement for the filing of annual returns, and thus, the names of shareholders are not registered for public inspection; and (2) The actual records that the company is required to keep by the IBC Act may be kept at a company's registered office — shielded from public inspection. *Id.*

39. Alfred Sarasin, Former President of the Swiss Association of Bankers, Address at Bankers' Day in the Kursaal in Berne (Sept. 22, 1978) (copy on file with author).

rationality could be asserted on behalf of the Bahamian judicial approach to the banking industry.

Apart from the institutional justifications for bank secrecy offered above, it is necessary to examine in greater detail the two-pronged machinery utilized by the Bahamas to maintain the vitality of their haven jurisdiction. The haven status is perpetuated through Bahamian statutory guidelines and a robust judicial approach to preserving banker/customer confidentiality. Case law will be interpreted within the context of the four *Tournier* qualifications outlined below.

E. Bahamian Statutory Duty of Bank Secrecy

Banks doing business in the Bahamas are governed by the Banks and Trust Companies Regulations Act of 1965 [hereinafter the Bank Act].⁴⁰ Section 10, the substantive secrecy provision of the Bank Act, provides that banks must maintain as secret, information concerning their affairs.⁴¹ Section 10 is the only legislative enactment of the Bahamas preserving a duty of confidence in banker/customer relationships.

Specifically, under section 10(1), disclosure is prohibited by any person who has "acquired information in his capacity as director, officer, employee or agent of any licensee or former licensee."⁴² In addition to forbidding a bank employee from disclosing "information relating to the identity, assets, liabilities, transactions, and accounts of a customer's bank account,"⁴³ the Bank Act equally prohibits the release of information after employment is terminated.⁴⁴

Every person who violates the section 10(1) duty of secrecy "shall be guilty of an offense against this Act and shall be liable on summary conviction to a fine not exceeding fifteen thousand dollars or to a term of imprisonment not exceeding two years or to both such fine and imprisonment."⁴⁵ In addition to the criminal penalties for disclosure, the bank is exposed to the possibility of a lawsuit for breach of contract.⁴⁶ If, however, a bank is contemplating disclosure only for the purpose of answering a subpoena in a foreign court, the customer can obtain an injunction.⁴⁷ Thus, the rational banker will balk at disclosure because

40. Banks and Trust Companies Regulations Act, 1965 (amended 1980) (Bah.).

41. *Id.* s. 10.

42. *Id.* s. 10(1)(a).

43. *Id.* s. 10(1)(e).

44. *Id.* s. 10(1)(a).

45. Banks and Trust Companies Regulations Act, 1965, s. 10 (amended 1980) (Bah.).

46. *Id.*

47. *See, e.g., F.D.C. Co. Ltd. v. Chase Manhattan Bank, N.A.*, [1990] 1 H.K.L.R. 277 (H.K.).

of the threat of penalties, civil liability, and, of course, potential damage to his reputation.

A banker can, however, avoid liability for disclosure if (1) he has the consent of the customer concerned;⁴⁸ (2) the performance of his duties or the exercise of his functions under the Bank Act mandate disclosure;⁴⁹ (3) it is required for the performance of his duties within the scope of his employment;⁵⁰ (4) he is lawfully required to make disclosure by any court of competent jurisdiction within the Bahamas,⁵¹ or (5) it is required pursuant to the Bahamian common law, as qualified by the Bank Act.⁵² Although these statutory exceptions included in section 10(1) appear broad, it is doubtful that any one of them would authorize a bank employee to disclose information for the purposes of a foreign court's subpoena.

F. Bahamian Common Law Duty of Bank Secrecy

The Bahamian common law position is similarly guarded about the information banks may surrender. It appears that the tenets of the common law are very much a part of Bahamian law.⁵³ Indeed, appeals are no longer taken from the Supreme Court of the Bahamas to the Judicial Committee of the Privy Council.⁵⁴ Yet, English case law has great persuasive, if not binding, effect in the Bahamas. Several English and Commonwealth cases are useful in illustrating not only the approach of the Bahamian courts, but also the various approaches to addressing bank secrecy by other common law haven jurisdictions. Although the cases cited are principally investigations into tax fraud, similar questions can arise in relation to securities law violations.⁵⁵

At first sight, the legal relationship between banker and customer can be characterized as that of debtor and creditor.⁵⁶ A more critical look,

48. Banks and Trust Companies Regulations Act of 1965, s. 10 (amended 1980) (Bah.).

49. *Id.* s. 10(1)(e)(i).

50. *Id.* s. 10(1)(e)(ii).

51. *Id.* s. 10(1)(e)(iii).

52. *Id.*

53. *Barclay's Bank v. McKinney*, Civ. No. 474 (Bah. Sup. Ct. 1979) (unreported) (copy on file with author). In this judgment of the Supreme Court, it was stated that "[t]he general law of the Bahamas as to the circumstances in which a bank is justified in disclosing a customer's account is the same as the common law of England." *Id.*

54. This Committee has the power to hear appeals from any Dominion or Dependency of the Crown in any matter, civil or criminal, except where its jurisdiction has been excluded as regards a particular country.

55. L. Collins, *Banking Secrecy and the Enforcement of Securities Legislation*, in CONFLICTS OF INTEREST IN THE CHANGING FINANCIAL WORLD 84-85 (R. Goode ed., 1986).

56. *Joachimson v. Swiss Bank Corporation*, [1921] 3 K.B. 110 (Eng.); *Foley v. Hill*, 9 Eng. Rep. 1002 (1849) (Eng.). No duty of confidentiality is attached to the normal relationship of debtor

however, reveals that the banker's duty to keep secret the affairs of his customer is well-established in English jurisprudence.⁵⁷ To appreciate this duty of secrecy, it is important to note that it indeed comprises elements of agency.⁵⁸ As a general rule, an agent is obligated to offer loyalty and confidentiality to his principal.⁵⁹ Although the scope of the agent's duty varies according to the nature of the relationship,⁶⁰ it is settled law that a banker owes a duty of secrecy to his customer.⁶¹

It has been suggested that the banker's agency relationship and his corresponding duty of confidentiality can be explained on the basis of sensible economic policy.⁶² Through its role as paymaster and receiver of amounts due, the bank has access to intimate details regarding its customers' financial transactions. A banker must not abuse this access, or trust,⁶³ by revealing his customers' financial affairs.

Notwithstanding the historical and economic basis of the obligation to keep bank transactions confidential, the duty of secrecy is not absolute, but qualified. *Tournier v. National Provincial and Union Bank of England*⁶⁴ is the *locus classicus* on common law bank secrecy.⁶⁵ Recently, in *Lipkin Gorman v. Karpnale Ltd.*⁶⁶ the House of Lords asserted that "the correctness of the principles of law stated by the majority in *Tournier's* case has not been doubted since the case was decided."⁶⁷ *Tournier* was a customer of the defendant bank.⁶⁸ In April 1922, his account was approximately £10 overdrawn.⁶⁹ Accordingly, *Tournier* reached a repayment agreement with the bank.⁷⁰ On the agreement, *Tournier* provided the name and address of his employer, Kenyon.⁷¹ When *Tournier* defaulted on the agreement, the bank

and creditor. Accordingly, the *Tournier* judgment is of considerable importance because it held that a banker does indeed owe a duty of confidentiality, although qualified, to his customer.

57. *Hardy v. Veasey*, [1868] 3 Ex. 107 (Eng.); *Foster v. Bank of London*, [1862] 3 F. & F. 214 (Eng.); *Tassel v. Cooper*, [1850] 9 C.B. 509 (Eng.).

58. E. ELLINGER, *MODERN BANKING LAW* 96 (1993).

59. *Boardman v. Phipps*, [1967] 2 A.C. 46 (Eng.).

60. Unlike the company director who may be ordered by a court to testify against his company, a solicitor has an absolute duty to maintain his client's confidences, see *Minter v. Priest*, 1930 A.C. 558 (Eng.); *O'Rourke v. Darbishire*, 1920 A.C. 581 (Eng.).

61. See *Parry Jones v. Law Society* [1969] 1 Ch. 1, 9 (Eng.).

62. See ELLINGER, *supra* note 58, at 97.

63. R. POWELL, *LAW OF AGENCY* 25-26 (2d ed. 1961).

64. [1924] L.K.B. 461 (Eng.).

65. M. HAPGOOD, *PAGET'S LAW OF BANKING* 254 (10th ed. 1990).

66. 1989 W.L.R. 1340 (Eng.).

67. *Id.* at 1357.

68. *Tournier v. Nat'l Provincial and Union Bank of England*, [1924] 1 K.B. 461 (Eng.).

69. *Id.*

70. *Id.*

71. *Id.*

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manager telephoned Kenyon to find out Tournier's home address.⁷² In conversations with two of Kenyon's directors, the bank manager revealed the following: (1) Tournier's account was overdrawn; (2) Tournier was not honoring the repayment agreement; and (3) The bank traced a check passing from Tournier to a bookmaker and in turn suggested that he was a gambling addict.⁷³ Following the conversations, Kenyon refused to renew Tournier's employment contract.⁷⁴ Tournier brought an action against the bank for, among other things, breach of an implied term of the contract between he and the bank, namely that the contract provided that the bank would not reveal to third parties the state of his account or transactions relating to it.⁷⁵

At first instance, Mr. Justice Avory and the jury rendered judgment in favor of the bank.⁷⁶ Tournier appealed and the Court of Appeal, in allowing the appeal, held that there was an implied term in the contract between bank and customer whereby a bank should not divulge to third parties either the state of a customer's account, any of the customer's transactions with the bank, or any information relating to the customer acquired by the bank in the keeping of the customer's account.⁷⁷ Additionally, in his famous judgment, Lord Justice Bankes stated that there were circumstances where a bank would be justified in disclosing its customers' transactions:

At the present day I think it may be asserted with confidence that the duty [of secrecy] is a legal one arising out of contract, and that the duty is not absolute but qualified. It is not possible to frame any exhaustive definition of the duty. The most that can be done is to classify the qualification and to indicate its limits On principle I think that the qualifications can be classified under four heads: (a) Where disclosure is under compulsion by law; (b) where there is a duty to the public to disclose; (c) where the interests of the bank require disclosure; (d) where the disclosure is made by the express or implied consent of the customer.⁷⁸

Through a framework constructed by the four *Tournier* exceptions, the following subpart will examine the relevant case law. In so doing, it will become evident that: (1) It is unlikely that the foreign securities regulator

72. *Id.*

73. *Tournier v. Nat'l Provincial and Union Bank of England*, [1924] 1 K.B. 461 (Eng.).

74. *Id.*

75. *Id.*

76. *Id.*

77. *Id.*

78. *Tournier v. Nat'l Provincial and Union Bank of England*, [1924] 1 K.B. 461 (Eng.).

will be able to successfully place his request for trading information within the ambit of any of the four heads; and (2) Although these qualifications could be interpreted as providing banks subject to a duty of secrecy with a justification for disclosure, they have nevertheless been narrowly construed by British and offshore courts.⁷⁹ Moreover, the extent to which these four common law qualifications modify the duty of secrecy imposed by section 10(1) of the Bank Act is still the subject of developing jurisprudence. According to the Bank Act, "nothing contained in section [10(1)] shall prejudice or derogate from the rights and duties subsisting at common law between a licensee and its customer."⁸⁰

G. *Exceptions to the Bahamian Duty of Bank Secrecy*

1. *Disclosure Under Compulsion by Law.*—In the Bahamas, bankers' have common law and statutory duties of nondisclosure, to the extent disclosure is not compelled by other domestic laws.⁸¹ Note that compulsion of disclosure by law means a foreign court's compulsion order is inapplicable. This was decided in *Re Standard Chartered Bank*⁸² and affirmed again in *Re Bank of America*.⁸³ A similar view was expressed by the Court of Appeal of Hong Kong in *F.D.C. Co. v. Chase Manhattan Bank*.⁸⁴

Both of these latter cases cited and affirmed Lord Denning's view in *R. v Grossman*.⁸⁵ In *Grossman*, Denning asserted that the Nassau or Hong Kong Branch of a multijurisdictional bank must be considered a separate entity from the head office in New York.⁸⁶ Anyone opening an account in either of these two havens must have confidence that in the ordinary course of business, the records of his account will be kept and processed entirely at a local level.⁸⁷ As stated by the Hong Kong Court of Appeal in *F.D.C. Co. v. Chase Manhattan Bank*:

There is no reason for [a customer] to suspect that the extent of such confidentiality might vary from bank to bank depending on where its head office is located. What we are concerned with here is not . . . the relationship between a foreign bank operating in Hong Kong and

79. See Pitt et al., *supra* note 28, at 408.

80. Bank and Trust Companies Regulations Act, 1965, s. 10 (amended 1980) (Bah.).

81. See *supra* parts II.E, II.F.

82. Civ. No. 852 (1986) (unreported) (Bah.) (copy on file with author).

83. Civ. No. 923 (1993) (unreported) (Bah.) (copy on file with author).

84. [1990] 1 H.K.L.R. 283 (H.K. Ct. App. 1990) (H.K.).

85. [1981] 73 CR. APP. R. 302 (Eng.).

86. *Id.*

87. *Id.*

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its customer. The relationship under consideration is between a bank registered in Hong Kong and a customer in Hong Kong, their relationship being governed by Hong Kong Law.⁸⁸

Similarly, in *Re Bank of America*, Chief Justice Gonsalves-Sabola noted: "I can find no warrant for regarding compulsion of law in the alien [U.S.] jurisdiction of the Head Office as being comprehended in the compulsion of law which *Tournier* recognised as constituting an exception to the duty of confidentiality owed by a local [Bahamas] bank to its customer."⁸⁹

In practical terms, disclosure under compulsion by law often entails disclosure through compulsion by statute. In England, the *Jack Committee Report*⁹⁰ identified nineteen statutory provisions that permit the disclosure of confidential bank account information without the consent of the customer. Of immediate relevance is section 177 of the Financial Services Act of 1986.⁹¹ Under this provision, the Secretary of State can instruct inspectors to investigate whether a contravention of the Company Securities (Insider Dealing) Act of 1985⁹² has occurred. Notwithstanding the common law duty of confidentiality, the Act specifically vests the Secretary of State with the power to compel a bank to disclose customer information.⁹³

No similar statutory provision exists in the Bahamas. It is suggested, however, that the U.S. Justice Department could make use of a combination of treaty and statutory provisions to compel Bahamian bankers to disclose account information. In 1987, under the Mutual Legal Assistance Treaty⁹⁴ [hereinafter MLAT], the United States and the Bahamas agreed to assist one another in the investigation, prosecution, and suppression of certain offenses.⁹⁵ Conduct punishable as a crime

88. [1990] 1 H.K.L.R. 283, 286 (H.K. Ct. App. 1990) (H.K.).

89. Civ. No. 923 (1993) (unreported) (Bah.) (copy on file with author).

90. The Jack Committee, a parliamentary committee, recommended the update and statutory codification of the *Tournier* exceptions to the banker's duty of confidentiality, and the establishment of a standard of best practice among banks clearly explaining the rules of this duty to customers. The Report concluded with an "earnest appeal" for no further statutory exceptions to this duty, which it viewed as a pillar of the banking system's integrity. See THE REPORT OF THE REVIEW COMMITTEE ON BANKING SERVICES: LAW AND PRACTICE 1992, CMND. 622 (1992).

91. See Financial Services Act, 1986, s. 177(8)(b) (Eng.).

92. Company Securities Act (Insider Dealing) Act, 1985 (Eng.).

93. Financial Services Act, 1986, s. 177(8)(b) (Eng.).

94. Treaty Between the United States of America and the Commonwealth of the Bahamas on Mutual Assistance in Criminal Matters, Feb. 4, 1988, U.S.-Bah., S. TREATY DOC. 100-17, 100th Cong. (1989) [hereinafter MLAT]. In August 1990, The Mutual Legal Assistance (Criminal Matters) Act 1988 came into operation in the Bahamas. The Act had the effect of domesticating the 1987 treaty so that the treaty became part of the municipal law of the Bahamas and directly applicable in Bahamian courts.

95. MLAT, *supra* note 94, art. 1(1).

under the laws of both countries qualifies as an offense under the MLAT.⁹⁶

Insider trading is a crime in the United States⁹⁷ and has been a crime in the Bahamas since June 1992.⁹⁸ Once the element of dual criminality has been established, the Attorney-General of the Bahamas⁹⁹ can initiate assistance, including, among other things: (1) taking the testimony of persons;¹⁰⁰ (2) providing documents;¹⁰¹ (3) serving documents;¹⁰² and (4) exchanging information in relation to the investigation prosecution and suppression of offenses.¹⁰³ The treaty further stipulates that all requests for information must comply with the domestic laws of the solicited state.¹⁰⁴ Notwithstanding the Bahamian statutory and common law duties of bank secrecy, the Attorney-General could, under the *Tournier* qualification of disclosure by compulsion of law, make an application to the court citing the Bank Act.¹⁰⁵

It must be noted that this proposal is, at best, tentative. First, under article 3(1)(a) of the MLAT, the Bahamas may deny a request to the extent that the request would prejudice its essential public interests.¹⁰⁶ Arguably, the Bahamas view bank secrecy as tantamount to economic development and any weakening of it threatens "essential public interest." Second, the preamble of the MLAT states that:

The Government of the United States of America and The government of The Commonwealth of The Bahamas, Desiring to provide more effective cooperation between the two States in the investigation, prosecution, and suppression of *serious crimes* [emphasis added], such as narcotics trafficking; and Desiring to

96. *Id.* art. 2(1)(a).

97. Willful violations of the securities laws or the rules promulgated under them are prohibited by fines and imprisonment.

98. Section 302(1) of the Bahamian Companies Act provides:

A person being an insider who . . . makes use of any material confidential information for his own benefit or advantage shall be guilty of an offense and shall be liable on conviction on information to a fine of fifty thousand dollars or to imprisonment for two years or to both such fine and imprisonment.

Companies Act, 1992, s. 302(1) (Bah.).

99. MLAT, *supra* note 94, art. 4(3).

100. *Id.* art. 1(2)(a).

101. *Id.* art. 2(b).

102. *Id.* art. 1(2)(c).

103. *Id.* art. 1(2)(g).

104. MLAT, *supra* note 94, art. 1(4).

105. See Banks and Trust Companies Regulations Act, 1965, s. 10(1)(e)(iii) (amended 1980 (Bah.)).

106. MLAT, *supra* note 94, art. 3(1)(a).

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improve coordination and mutual assistance in law enforcement matters in general; have agreed as follows . . .¹⁰⁷

Indeed, there are a multiplicity of factors that could arise which negate the use of the MLAT for insider trading applications. Any further discussion of the mechanics of the MLAT are, however, outside the scope of the present analysis. It is sufficient to note that legal creativity is essential to successful investigations into transborder securities fraud.¹⁰⁸

One instance of legal creativity that reaped reward for the SEC was the litigation involving Dennis Levine.¹⁰⁹ The unique approach in the Levine case developed from previous unsuccessful attempts to obtain client information. The *Re Guaranty Trust Co.*¹¹⁰ case illustrates such a failed attempt. In *Re Guaranty Trust Co.*, the SEC argued before the Bahamian courts that securities transactions were not equivalent to banking transactions.¹¹¹ It followed that Bahamian bank secrecy laws would not be breached if the client's name was revealed.¹¹² Before this line of reasoning could be evaluated, the Court of Appeal dismissed the case on the basis that the SEC lacked standing to seek a declaratory judgment.¹¹³

Having learned the error of its ways in *Guaranty Trust*, the SEC adopted a different approach in the Levine investigation. Here, the SEC directly approached the Attorney-General of the Bahamas for assistance.¹¹⁴ Again, the SEC lawyers contended that disclosure of Levine's name would not violate Bahamian secrecy laws, given that it was a "securities" transaction rather than a "banking" transaction.¹¹⁵ This time, however, the Attorney-General condoned what no Bahamian court would. It is suggested that Bahamian compliance with the SEC's request for information in the Levine investigation was unorthodox and is unlikely to be repeated. This conclusion is based on the fact that

107. *Id.* pmb1. Perhaps insider trading is not a serious crime at all and would not fall within the treaty. See BARRY RIDER & T.M. ASHE, *INSIDER CRIME — THE NEW LAW* v (1993) ("Contrary to what some people may think . . . we do not consider insider dealing as the most serious of the 'white collar' offences, let alone criminal offences."); H. MANNE, *INSIDER DEALING AND THE STOCK MARKET* 131-45 (1966).

108. S. Cass Weiland, *The Use of Offshore Institutions to Facilitate Criminal Activity in the United States*, 16 N.Y.U. J. INT'L L. & POL. 1115 (1984).

109. See *supra* part I.

110. Civ. No. 19 (1986) (unreported) (Bah.) (copy on file with author).

111. *Id.*

112. *Id.*

113. *Id.*

114. *SEC v. Levine*, Fed. Sec. L. Rep. (CCH) ¶ 92717 (S.D.N.Y. 1986), *rev'd and remanded on other grounds*, 881 F.2d 1165 (2d Cir. 1989).

115. See *id.*

shortly after the Attorney-General's ruling, the Bahamian government publicly announced that (1) the ruling turned on its own special facts; and (2) notwithstanding any implication to the contrary, the government was committed to the preservation of bank-related information.¹¹⁶

2. *Disclosure Under Public Duty.*—In *Tournier*, Lord Justice Bankes summarized the disclosure under the public duty exception with reference to Lord Finlay's judgment in *Weld-Blundell v. Stephens*.¹¹⁷ In *Weld-Blundell*, Lord Finlay spoke of cases where a higher duty than private duty is involved, as where danger to the state may supersede the duty of the agent to his principal.¹¹⁸ Construed broadly, this exception could include disclosing information that helps alleviate fraud on securities markets. Once again, however, it is important to note that this qualification is only an exception to the duty of secrecy where the disclosure is owed to the public of the Bahamas. It is submitted that foreign court proceedings do not fall within this qualification.

3. *Disclosure Under Bank Duty.*—The interests of the bank require some disclosure of the customer's transactions whenever there is litigation between the bank and its customer. In Bahamian jurisprudence, conflicting authority exists as to whether a Bahamian bank can reveal information to a foreign court when served with a subpoena *duces tecum*. This notion has been reflected in two recent cases. First, in *Re Standard Chartered Bank*,¹¹⁹ the appellant bank was incorporated under the laws of England with a branch network throughout the world. Branch locations specifically included Nassau and New York.¹²⁰ Three of the bank's customers were under investigation for tax fraud and thus, the New York branch was served with a subpoena *duces tecum* requiring the production of confidential bank documents located in the Bahamas.¹²¹ The bank applied for a declaration that it be at liberty to produce subpoenaed records before the grand jury.¹²² The Bahamian Court refused the declaration sought and rejected the proposition that the interest of the bank in disclosing information to the New York Grand Jury in compliance with a subpoena directed to it, operated as an

116. GOVERNMENT OF THE COMMONWEALTH OF THE BAHAMAS STATEMENT (Sept. 4, 1986).

117. 1920 A.C. 956, 965 (Eng.).

118. [1924] 1 K.B. 473 (Eng.).

119. Civ. No. 852 (1986) (Bah.) (unreported) (copy on file with author).

120. *Id.*

121. *Id.*

122. *Id.*

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exception to the prohibition contained in section 10(1) of the Bank Act.¹²³

Contrary authority, however, is provided by *Royal Bank of Canada v. Apollo Development Ltd.*¹²⁴ In that case, a subpoena *duces tecum* was served on the plaintiff in New York requiring the production of confidential bank documents located at its Bahamian branch.¹²⁵ The court held that the interest of the bank in disclosing such documents in answer to the subpoena was sufficient to constitute an exception to the prohibition otherwise provided by section 10(1) of the Bank Act.¹²⁶

Although these judgments represent a divergence of approach, it is more likely that *Re Standard Chartered Bank* is the preferred approach, as it represents the most recent approach of the Bahamian Supreme Court in *Re Bank of America*.¹²⁷ In *Re Bank of America*, the applicant's head office was in the United States, with local branches in the Bahamas.¹²⁸ The Internal Revenue Service (IRS) served U.S. federal district court orders on the head office to produce bank records of customers at the Nassau branch.¹²⁹ Not wanting to violate either the U.S. court summons or the bank secrecy laws of the Bahamas, Bank America and its subsidiary, Bahamas Trust, joined to seek a declaration from the Supreme Court of the Bahamas that they would be able to comply with the IRS summons.¹³⁰ The Court returned a wholesale refusal of the bank's application.¹³¹

In refusing the application, Chief Justice Gonsalves-Sabola respectfully criticized the reasoning in *The Royal Bank of Canada* case. He stated that it either was a case that turned on its own facts or that Chief Justice Georges decided the case without considering Lord Justice Atkins's judgment in *Tournier*:

It is difficult to hit upon a formula which will define the maximum of the obligation which must necessarily be implied. But I think it is safe to say that the obligation not to disclose information such as I have mentioned is subject to the qualification that the bank have the right to disclose such information when, and to the extent to which it is reasonably necessary for the protection of the bank's interests,

123. *Id.* See *supra* part II.E.

124. 1985 L.R.C. (Comm.) 66 (Bah.).

125. *Id.*

126. *Id.*

127. Civ. No. 923 (1993) (unreported) (Bah.) (copy on file with author).

128. *Id.*

129. *Id.*

130. *Id.*

131. *Id.*

either as against their customer or as against third parties in respect of transactions of the bank for or with their customer, or for protecting the bank or persons interested or the public against fraud or crime.¹³²

In Gonsalves-Sabola's estimation, disclosure by the bank to save itself from the threatening behavior of third persons who are entirely outside the privity of the contract with the bank's customers, falls outside any of the *Tournier* categories. Accordingly, as a matter of contract law, the bank could not assert any legal right vis-a-vis the customer, to make disclosure to a third party.¹³³ Portions of Gonsalves-Sabola's judgment provide further elucidation:

Since the relationship between a bank and its customer is born out of contract and governed throughout by that law or principle, if a bank and its customer did not expressly or implicitly contract out of their reciprocal common law duties, the bank cannot unilaterally relieve itself of that most sensitive of its contractual obligations — non-disclosure without the customer's consent — for reasons not sounding in the law of contract. If the banker needed to secure for himself the liberty to disclose his customer's affairs under compulsion of foreign law he could have procured that inclusion of a term to that effect in the contract. Subsequent events which show that the banker may have benefitted from the inclusion of suitably protective terms in the contract do not justify a court coming to the banker's protection in order to save him from his own lack of foresight and to the prejudice of his customer's rights.¹³⁴

Two final cases further enhance the *Re Bank of America* position of nondisclosure for foreign sovereigns. First, in *X.A.G. v. A Bank*¹³⁵ the English judiciary demonstrated that national interest will take precedence over the policies of the United States. In *X.A.G.*, a group of oil companies maintained an account at the London branch of Citibank, a U.S. bank.¹³⁶ The group's U.S. subsidiary had dealings in the U.S. oil markets.¹³⁷ In an investigation into the crude oil business, the U.S. Justice Department sought information concerning all the companies in the group.¹³⁸ Accordingly, the Justice Department served a subpoena on Citibank's U.S. office to produce documents located at its London

132. Civ. No. 923 (1993) (unreported) (Bah.) (copy on file with author).

133. *Id.*

134. *Id.*

135. [1983] 2 All E.R. 464 (Eng.).

136. *Id.*

137. *Id.*

138. *Id.*

branch.¹³⁹ When the bank made it clear that it intended to provide the documents, the group obtained an interim injunction in the High Court.¹⁴⁰ When the U.S. District Court issued another order commanding disclosure, Mr. Justice Legatt continued the injunction.¹⁴¹ Consistent with the views expressed by Mr. Justice of Appeals Yang in *F.D.C. Co.* and Chief Justice Gonsalves-Sabola in *Re Bank of America*, Mr. Justice Legatt made it clear that the group of companies opened their account in London and could expect that the proper law of the contract was English law.¹⁴² Moreover, disclosure by the bank would not be justified on the ground that it had to comply with the subpoena of a U.S. court.¹⁴³

Second, in *F.D.C. Co.*, the Hong Kong Court of Appeal affirmed an injunction to constrain the defendants from complying with a U.S. subpoena to supply local Hong Kong bank account information to U.S. revenue authorities.¹⁴⁴ Here again, the plaintiffs, who maintained an account with the Hong Kong branch of Chase instituted local proceedings to enjoin the bank from releasing documents pursuant to a U.S. subpoena.¹⁴⁵ Again the court continued the injunction stating that the duty of secrecy was not constrained by territorial limits.¹⁴⁶ Although the orders of the U.S. court were addressed to Chase at its New York offices, they were "aimed unashamedly"¹⁴⁷ at information that was within the jurisdiction of the Hong Kong courts and they were therefore intended to have extraterritorial effect. As stated by V.P. Huggins:

The Hong Kong Courts could enjoin the Bank against disclosing the information to the US Government in Hong Kong and I am satisfied that they can restrain a transfer which is nothing more nor less than a device to avoid the enforcement in Hong Kong of the orders of a foreign court [W]e are not bound to hold back from enforcing the law of Hong Kong at the dictate of a foreign power All persons opening accounts with banks in Hong Kong, whether foreign or local banks, are entitled to look to the Hong Kong Courts to enforce any obligation of secrecy which, by the law of Hong Kong, is implied by virtue of the relationship of banker and customer.¹⁴⁸

139. *Id.*

140. [1983] 2 All E.R. 464 (Eng.).

141. *Id.*

142. *Id.*

143. *Id.*

144. 1 H.K.L.R. 283 (1990) (H.K. Ct. App. 1990) (H.K.).

145. *Id.*

146. *Id.*

147. *Id.* at 278.

148. *Id.* at 284.

All these cases demonstrate that English, Hong Kong, and Bahamian courts are keen to protect the secrecy laws. There is consistency in the application of the *Tournier* qualifications and the reasoning of the variety of judges. Haven courts that are governed by the common law will resist attempts by the United States to infringe upon respective jurisdictions' bank secrecy laws. Therefore, it is unlikely that a bank employee, served with a subpoena *duces tucem*, would be entitled to disclose information otherwise required to be held confidentially.

4. *Disclosure Under Express or Implied Consent of the Customer.*—In this analysis, it is assumed that under the fourth exception, a banker could not obtain the express consent of a customer to disclose information to securities regulators. Indeed, it is rare for the suspected offender to knowingly relinquish incriminating evidence. Consensual access can be acquired, however, from the bank account holder who fears no punishment for any wrongdoing.¹⁴⁹ A frequent example of implied consent is where the customer authorizes a reference to his banker. Nothing in the Bank Act can prevent a bank from providing information on a customer's general credit rating upon a legitimate request in the normal course of business.¹⁵⁰ This disclosure provision, however, is of little use to the securities regulator.

In *Re ABC Ltd.*,¹⁵¹ the Grand Court of the Cayman Islands evaluated the position of a Cayman Island bank that had been served with a consent signed by a client in accordance with a U.S. court order. The bank applied for a direction under the Confidential Relations (Preservation) Law of 1976¹⁵² as to whether it should act on the consent it had received, and Chief Justice Summerfield held that it should not, stating that:

Although in form the consent directive purports to be a consent and direction given by the client of the bank, it is in substance a direction given by the foreign court. It is not a real consent at all. In reality it is the foreign court directing the bank to disclose confidential information.¹⁵³

The significance of this decision to offshore jurisprudence is its suggestion that although *Tournier* contemplates an express or implied

149. Bradley O. Field, *Improving International Evidence Gathering Methods*, 15 LOY. L.A. INT'L & COMP. L.J. 691, 698 (1993).

150. Bank and Trust Companies Regulations Act, 1965, s. 10(2) (amended 1980) (Bah.).

151. 1985 F.L.R. 159 (Cayman Islands).

152. Confidential Relations (Preservation) Law, 1976 (Cayman Islands).

153. 1985 F.L.R. 159, 163 (Cayman Islands).

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waiver, a court must be satisfied that the waiver was voluntarily given. A foreign court's order of "compelled consent" is an oxymoron that cannot force disclosure.

H. Summary

The cases cited on bank secrecy demonstrate that a principal interest of the courts involved was to preserve the confidential relationship between banker and customer. The sanctity of this relationship was upheld both to maintain the sovereignty of the haven and to engender economic sustenance. Indeed, bank secrecy laws embody important national interests arising from circumstances wholly apart from securities regulation. Despite these valid goals, bank secrecy laws provide undue protection to those persons committing fraud on U.S. markets.¹⁵⁴ The SEC believes that bank secrecy laws have a broad capacity to impede investigations of a variety of securities violations, including: (1) acquisitions of securities in violation of beneficial ownership and tender offer provisions of the Exchange Act; (2) stock manipulations; (3) violations of margin requirements; (4) misappropriation of corporate assets; and (5) laundering of funds generated by illegal activities.¹⁵⁵ Indeed, the *Tournier* rules remain law. It is time, however, to reassess these rules in light of the requirements of modern transnational commerce. World trade based on free markets demands the strict regulation of market participants. As bank secrecy is incompatible with this goal, the reaction of the SEC to offshore havens has not been hospitable.

III. U.S. Response

A. Overview

While the U.S. Securities and Exchange Commission (SEC) has an enviable record of policing transactions domestically, its current tools are too unwieldy and time-consuming to deal effectively with haven jurisdictions. According to one former SEC Commissioner, prevailing methods of investigating foreign initiated transactions are ". . . slow, cumbersome, unpredictable and often unproductive."¹⁵⁶ The purpose

154. See, e.g., J. Fedders, *Policing Trans-Border Fraud in the United States Securities Markets: The Waiver by Conduct Concept — A Possible Alternative or Starting Point for Discussion*, 11 BROOK. J. INT'L L. 480 (1985).

155. EXCHANGE ACT RELEASE NO. 21186 (July 30, 1984), reprinted in [1983-1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 86,980.

156. See Fedders, *supra* note 154, at 480.

of this part is to evaluate the SEC's use of litigation to obtain requested information. For the sake of clarity, Part III is divided into six substantive subparts. Subpart B initiates the discussion with a summary of the goals of the SEC's enforcement program. Taking into account these goals, Subpart C explains how the enforcement program is obstructed by bank secrecy laws. Subparts D and E evaluate the methods by which U.S. courts assert jurisdiction over offshore initiated transactions. Finally, through an analysis of three of the leading U.S. cases involving bank secrecy laws, Subpart F assesses the SEC's success with litigation.

B. Goals of Regulation

The primary objective of the SEC's enforcement program is to preserve investor confidence in the integrity, fairness, and efficiency of the securities market.¹⁵⁷ To further this objective, the Commission, in recent years, has focused attention on a number of problem areas. One of the most prominent areas of focus has been insider trading.

The antifraud provisions of the federal securities laws aim to (1) maintain the integrity of the securities market; and (2) guarantee that people trading in securities will not be disadvantaged by insiders or those who misuse their access to material nonpublic corporate information.¹⁵⁸ If the SEC fails to pursue aggressive policing of these markets, investors essentially accept a double standard of law enforcement, one standard for individuals who trade from within the United States and a second standard for individuals trading outside the United States. Offshore investors cannot be allowed to contravene U.S. laws with impunity, while domestic investors are accountable for the same violations.¹⁵⁹

Although two schools of thought reach opposing conclusions as to whether insider trading should be prohibited, an evaluation of this debate is superfluous here. For present purposes, it is accepted that the practice of insider trading must be banned.¹⁶⁰ Sufficient concern has been

157. Sandra N. Hurd, *Insider Trading and Foreign Bank Secrecy*, 24 AM. BUS. L.J. 25, 26 (1986).

158. W. McLucas et al., *Protection from International Fraud — Legal and Enforcement Developments: Part I*, 13 COMPANY LAW. 206-07 (1992).

159. Fedders, *supra* note 154, at 488.

160. On numerous occasions, courts have found that insider trading is simply dishonest. See *Chiarella v. United States*, 445 U.S. 222, 245 (1980) (Burger, C.J., dissenting) ("Chiarella . . . misappropriated — stole to put it bluntly — valuable nonpublic information entrusted to him in the utmost confidence . . . [and] then exploited his ill-gotten informational advantage by purchasing securities in the market."). See also *SEC v. Tome*, 638 F. Supp. 596, 599 (S.D.N.Y. 1986), modified 638 F. Supp. 638 (S.D.N.Y. 1986) ("case reveals a crass abuse and betrayal of a personal and professional relationship of trust and confidence for personal gain").

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expressed that securities markets could suffer harm if public confidence in their fairness were eroded, as investors may be deterred from participating in the market if they know that others are trading on information legally prohibited from the investing public.

C. How Enforcement Activities are Impeded by Bank Secrecy Laws

Domestically, the SEC's enforcement objectives have been achieved through its statutory ability to conduct investigations into alleged securities violations. Under express provisions of the Securities Exchange Act, the SEC is entitled to obtain full and complete trading records from any broker or dealer located within the United States or transacting business in securities through a registered broker or dealer.¹⁶¹ This information necessarily includes the identity of any customers of the broker on whose behalf the suspicious trades were executed, the amounts of stock purchased and the time of the transactions.

When attempting to gather information located in haven jurisdictions, the SEC frequently encounters barriers in the form of local nondisclosure laws. These obstacles vary depending on the country. Often, the prohibitions are in the form of statutes or as judicially-constructed nondisclosure principles. The Bahamas case study was illustrative of the prohibitions invoked by offshore banks when SEC requests for information are received.

The internationalization of securities markets and corresponding increase in haven initiated transactions challenges the existing enforcement structure. The regulations described above were designed to maintain the integrity of national markets. Domestically-oriented regulations, however, are proving ineffective in the face of securities transactions originating in bank secrecy jurisdictions.

D. Litigation

Indeed, the SEC can avail itself of numerous statutory and treaty-based mechanisms to extract information shielded by bank secrecy laws.¹⁶² A wholesale evaluation of these mechanisms, however, is outside the scope of the current analysis. Given that most attempts by the SEC to obtain information located in haven jurisdictions have resulted in

161. Securities Exchange Act, 15 U.S.C. §§ 77a-80c-3 (1988).

162. Other methods include (1) through informal cooperation between regulators, as demonstrated by the time the SEC notified United Kingdom authorities about the Guinness Affair and (2) through bilateral and multilateral agreements, for example, the Hague Convention on the Taking of Evidence Abroad in Civil or Commercial Matters. See L. GOWER, *BIG BANG AND CITY REGULATION* (1988).

litigation, it will be the primary focus here.¹⁶³ Notwithstanding its shortcomings, litigation has been a useful tool in effecting changes in how countries with nondisclosure laws address SEC requests for information.

If sufficient information obtained during the SEC's initial inquiry indicates that a violation of the federal securities laws has occurred, the SEC can initiate an action in federal court.

E. Jurisdiction

The following two jurisdictional thresholds must be satisfied before a U.S. court will adjudicate a dispute involving the extraterritorial application of securities laws: (1) subject matter jurisdiction; and (2) personal jurisdiction.¹⁶⁴ The following two subsections confirm that haven banks that trade on U.S. securities markets are within the ambit of the U.S. judicial process.

1. Subject Matter Jurisdiction.—U.S. jurisprudence has well-established that the courts have subject matter jurisdiction over securities purchases initiated offshore and executed on U.S. markets.¹⁶⁵ From the U.S. perspective, asserting jurisdiction over a foreign country's territory can be substantiated on the basis of both the conduct and effects doctrines of prescriptive jurisdiction under international law.¹⁶⁶ Under the former doctrine, the United States can attach legal consequences to conduct that occurs within its territory.¹⁶⁷ *Tamari v. Bache & Co. (Lebanon) S.A.L.*¹⁶⁸ held that the execution of trades on U.S. markets constitutes sufficient conduct to come within the scope of U.S. securities laws. Accordingly, where a haven bank initiates securities transactions on a U.S. market, it will be within the jurisdiction of U.S. courts.

Under the effects doctrine, it is permissible to apply U.S. law if conduct beyond its territorial limits has a substantial, direct, and foreseeable effect within the United States.¹⁶⁹ Arguably, initiating

163. R. Ferrara & J. Mackintosh, *Legal Representation and the International Securities Market*, 10 COMPANY LAW. 103 (1989). Given the SEC's access to litigation, these authors argue that the primary concern of the practitioner must be the ability to settle claims prior to a courtroom visit.

164. Edward F. Greene et al., *Problems of Enforcement in the Multinational Securities Market*, 9 UNIV. PA. J. INT'L BUS. L. 325, 343 (1987).

165. Derek J.T. Adler & Marco E. Schnabl, *Reaffirmation of Availability of Antifraud Provisions of U.S. Securities Law to Foreign Litigants Suing in U.S. Courts*, 20 INT'L BUS. LAW. 29, 30 (1992).

166. See *supra* notes 17-21 and accompanying text (discussing the effects doctrine).

167. RESTATEMENT (SECOND) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 17 (1965) [hereinafter RESTATEMENT].

168. 730 F.2d 110 (7th Cir. 1984).

169. RESTATEMENT, *supra* note 167, § 18.

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insider trades offshore encourages such an effect. As the Court in *Tamari* noted:

[w]hen transactions initiated by agents abroad involve trading on United States exchanges, the pricing and hedging functions of the domestic markets are directly implicated, just as they would be by an entirely domestic transaction. If the transactions are the result of fraudulent representations, unauthorized trading, or mismanagement of trading accounts, prices and trading volumes in the domestic marketplace will be financially influenced and public confidence could be undermined.¹⁷⁰

2. *Personal Jurisdiction*.—Personal jurisdiction entails the ability of a court to effect service of notice on a party. It is usually based on a finding that a party has sufficient minimum contacts with the forum. This notion of sufficient minimum contact is complemented by the due process requirement that “traditional notions of fair play and substantial justice”¹⁷¹ be satisfied. In effect, where a haven bank is part of a multinational institution with offices in the United States, the haven bank will be within the personal jurisdiction of U.S. courts. The fact that documents identifying the beneficiary of a bank account are outside the territorial boundaries of the United States does not impede the service of process. For example, the New York office of a bank can be compelled to produce documents located in Nassau. In *Re Marc Rich*,¹⁷² the court stated that “the witness [may not] resist the production of documents on the grounds that the documents are located abroad The test for the production of documents is control, not location.”¹⁷³

Even in the unlikely situation that a haven bank exists independently of any branch network, the bank will still be within the personal jurisdiction of U.S. courts if it executes transactions on U.S. markets. According to one former SEC commissioner, “the cases go very far in subjecting anyone who effects transactions in US securities directly or indirectly through a US financial institution to the [personal] jurisdiction of a US court.”¹⁷⁴ In *SEC v. Tome*,¹⁷⁵ for example, the Commission received the court’s approval to serve process through newspaper advertisements in several European cities. This was an insider trading

170. *Tamari*, 730 F.2d at 1108.

171. *International Shoe Co. v. Washington*, 326 U.S. 310, 316 (1945).

172. 707 F.2d 663 (2d Cir. 1983).

173. *Id.* at 667.

174. R.I. Karmel, *The Second Circuit’s Role in Expanding the SEC’s Jurisdiction Abroad*, 65 ST. JOHN’S L. REV. 765 (1991).

175. 833 F.2d 1086 (2d Cir. 1987), *cert. denied*, 486 U.S. 1014, 1015 (1988).

case, based on circumstantial evidence, where the identity of the fraudulent dealers was unknown. The SEC exercised similar creativity in another insider trading case, *SEC v. Unifund S.A.L.*¹⁷⁶ Here, the service of process was initially delivered by overnight courier to the New York office of the broker who executed the stock purchase with instructions to forward the papers to Unifund in Beirut.¹⁷⁷ Again, the court ruled that service was effective.¹⁷⁸

Thus, jurisdiction over securities transactions initiated offshore gives the SEC settled ability to make use of the U.S. judicial system.

F. Rule 37 of the Federal Rules of Civil Procedure

Once an action has been filed and the court's jurisdiction has been verified, the SEC may start discovery procedures under the United States' Federal Rules of Civil Procedure [hereinafter FRCP]. If a court subpoena has been effectively served and the recipient bank does not comply, the SEC can request the court to issue an order compelling discovery under Rule 37 of the FRCP.¹⁷⁹ If the bank fails to comply with this court order, Rule 37 gives the court the power to impose sanctions against the bank, including contempt proceedings, monetary fines and other adverse measures.¹⁸⁰

Despite the existence of wide subject matter and personal jurisdiction, U.S. courts nevertheless exercise perfunctory discretion when encroaching on the sovereignty of other jurisdictions and occasionally refrain from doing so. The three cases discussed below examine the methods by which U.S. courts resolve the conflict of laws in the absence of information sharing agreements on insider trading. U.S. courts dealing with the problem of exercising the right to enforce U.S. laws extraterritorially have usually applied one or more of three tests: (1) international comity,¹⁸¹ (2) balancing of interests,¹⁸² and (3) good faith.¹⁸³ These tests will be assessed in more detail within the framework created by the three cases.

176. 910 F.2d 1028 (2d Cir. 1990), *petition for reh'g denied*, 917 F.2d 98 (2d Cir. 1990).

177. *Id.*

178. *Id.*

179. FED. R. CIV. P. 37. See also J. Fedders, *Policing Internationalized U.S. Capital Markets: Methods to Obtain Evidence Abroad*, 18 INT'L L. 96-97 (1984).

180. FED. R. CIV. PROC. 37. See also Martin Radvan, *The Hague Convention on Taking of Evidence Abroad in Civil or Commercial Matters: Several Notes Concerning its Scope, Methods, and Compulsion*, 16 N.Y.U. J. INT'L L. & POL. 1031 (1984).

181. *Ings v. Ferguson*, 282 F.2d 149, 152-53 (2d Cir. 1960); *SEC v. Banca Della Svizzera Italiana*, 92 F.R.D. 111, 117 (S.D.N.Y. 1981).

182. RESTATEMENT, *supra* note 167, § 40.

183. *Société Internationale v. Rogers*, 357 U.S. 197, 204-05 (1958).

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1. *The St. Joe Case*.—*SEC v. Banca Della Svizzera Italiana*¹⁸⁴ [hereinafter *St. Joe Case*], involved an attempt by the SEC to obtain information protected by Swiss bank secrecy laws. BSI was a Swiss bank that maintained a subsidiary in the United States.¹⁸⁵ The SEC alleged that BSI and its principals had traded on inside information.¹⁸⁶ During the course of its investigation, the SEC requested the identity of individuals who had conducted certain securities transactions through BSI.¹⁸⁷ BSI argued that under Swiss law, it would be unable to identify such customers because it was shielded by bank secrecy law.¹⁸⁸

Following BSI's refusal to divulge such information, a New York District Court granted the SEC's application for a temporary restraining order to freeze BSI's New York bank account.¹⁸⁹ More significantly, the District Court ordered BSI to comply fully with the SEC's request for information.¹⁹⁰ BSI subsequently obtained a waiver from its customers and satisfied the SEC's request.¹⁹¹ What is of interest is the approach of the U.S. court in determining that BSI should comply with the SEC request, obliquely requiring BSI to breach Swiss secrecy laws.

The issue of comity was not addressed by the *St. Joe* court. This is a departure from the earlier approach of the Court of Appeals for the Second Circuit.¹⁹² Previous judgments stressed that production of requested information would not be required if such production would disturb the relationships enjoyed with a neighboring state. This course of action was supported by the belief that diplomatic channels were best suited for such endeavors. The situation today, however, differs markedly. Courts continue to recognize the legitimate interests of haven jurisdictions, but it is almost unheard of to defer on the basis of international comity. According to Harvey Pitt, former General Counsel to the SEC, two elements chronicle the demise of the international comity test: (1) It fails to recognize any interest the United States might have in the outcome other than maintaining good relations in the international theater; and (2) It provides haven jurisdictions with an incentive to retain

184. 92 F.R.D. 111 (S.D.N.Y. 1981) [hereinafter *St. Joe Case*].

185. *Id.*

186. *Id.*

187. *Id.*

188. *Id.*

189. *St. Joe Case*, 92 F.R.D. at 113; D. Newcomb, *Policing Trans-Border Fraud*, 11 BROOK. J. INT'L L. 562 (1985).

190. *St. Joe Case*, 92 F.R.D. at 113.

191. *Id.* at 113.

192. See, e.g., *Re Chase Manhattan Bank*, 297 F.2d 611 (2d Cir. 1962); *Ings v. Ferguson*, 282 F.2d 149 (2d Cir. 1960); *First Nat'l City Bank v. Commissioner*, 271 F.2d 616 (2d Cir. 1959).

virile bank secrecy laws secure in the knowledge that the United States will defer to their legislation.¹⁹³

The Court of Appeals for the Second Circuit¹⁹⁴ jettisoned the comity standard with its 1968 adoption of the American Law Institute's balancing of interests test. This test evolved into the principal judicial instrument by which the competing interests would be assessed. The balancing test entails numerous criteria. Principal among them are: (1) the vital national interests of each of the states; and (2) the extent and the nature of the hardship that inconsistent enforcement actions would impose.¹⁹⁵

In the present case, the court concluded that the United States had a vital national interest in maintaining the integrity of its securities markets. Haven-initiated transactions threatened the strength of U.S. markets and affected U.S. economic interests.¹⁹⁶

District Judge Pollack then considered the second factor in the balancing of interests test, namely the extent of the hardship that inconsistent enforcement actions would impose on BSI. While conceding that BSI could be subject to monetary and criminal penalties under Swiss law, Judge Pollack determined that that same Swiss law contained a "state of necessity" exception that operated to relieve an individual of criminal liability in these circumstances.¹⁹⁷

The court further considered whether BSI approached the proceedings in good faith. From the Supreme Court judgment in *Société Internationale v. Rogers*¹⁹⁸ the Court elicited that if a party acted in good faith but was unable to comply because of foreign law, it was possible for the party to avoid sanctions being imposed for non-compliance. In *Société Internationale*, the Court articulated a two-step test for deciding if the party in question acted in good faith. First, the party must make efforts "to the maximum of its ability" to achieve compliance. Second, the party must not "deliberately court legal impediments."¹⁹⁹ The significance of this test, however, must be questioned. Subsequent cases in the federal appellate courts generally

193. Pitt et al., *supra* note 28, at 419.

194. The Second Circuit Court of Appeals has had and continues to have a profound effect on securities law. It is known as the "mother court." Its judgments bind the courts in the southern district of New York within the scope of New York's financial center. R. Karmel, *The Second Circuit's Role in Expanding the SEC's Jurisdiction Abroad*, 65 ST. JOHN'S L. REV. 743 (1991).

195. See, e.g., *Garpeg Ltd. v. United States*, 583 F. Supp. 789, 795 (2d Cir. 1984).

196. See *St. Joe Case*, 92 F.R.D. at 117-18.

197. *Id.* at 118-19.

198. 357 U.S. 197 (1958).

199. *Id.* at 208-09, 211-12.

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imposed sanctions for non-compliance with subpoenas and narrowly construed the holding decided in *Société Internationale*.²⁰⁰

Here, the court determined that the Bank failed to bring itself within the ambit of *Société Internationale*.²⁰¹ The Bank had not pursued good faith efforts to comply with the SEC subpoena.²⁰² BSI was found to have deliberately taken advantage of Swiss bank secrecy laws in an effort to eschew U.S. securities regulations.²⁰³ Moreover, BSI had profited from its conduct.²⁰⁴ The court asserted that:

It would be a travesty of justice to permit a foreign company to invade American markets, violate American laws if they were indeed violated, withdraw profits and resist accountability for itself and its principals for the illegality by claiming their anonymity under foreign law.²⁰⁵

The approach of the *St. Joe* court illustrates the conflict between the good faith standard and the primary interests of the United States in discovery. While U.S. courts will consider factors such as international comity in jurisdictional disputes, the tendency, as represented by this case, is to find that U.S. interests supersede all other nations' interests. The preponderance of U.S. case law concludes that in the interests of international comity, it is best if the United States' needs are satisfied first.²⁰⁶ Indeed, the good faith test is "intended to do justice in the individual situation and to provide a less offensive approach from the international perspective."²⁰⁷ Contemporary judgments indicate, however, that a party basing its conduct on a foreign secrecy law will inevitably be at odds with U.S. law and therefore act in bad faith. Predictably, such an approach diminishes principles of international comity.

In a broader context, the *St. Joe* case illustrates how the threat of sanctions and court orders compelling compliance with SEC investigations can be successful. Nevertheless, litigation is a questionable

200. See, e.g., *United States v. Vetco, Inc.*, 644 F.2d 1324 (9th Cir. 1981); *Civil Aeronautics v. Deutsche Lufthansa Aktiengesellschaft*, 591 F.2d 951 (D.C. Cir. 1979); *Ohio v. Arthur Andersen & Co.*, 570 F.2d 1370 (10th Cir. 1978).

201. *St. Joe Case*, 92 F.R.D. at 117-18.

202. *Id.*

203. *Id.*

204. *Id.*

205. *Id.* at 119.

206. See, e.g., *United States v. First Nat'l City Bank*, 396 F.2d 897 (2nd Cir. 1986); *In re Chase Manhattan Bank*, 297 F.2d 611 (2d Cir. 1962); *First Nat'l Bank v. IRS*, 271 F.2d 616 (2d Cir. 1959).

207. *Strict Enforcement of Extraterritorial Discovery*, 38 STANFORD L. REV. 871 (1986).

long term solution to the SEC's international problems for three reasons.²⁰⁸ First, litigation is an inherently ad hoc approach for resolving barriers created by bank secrecy laws. Inconsistent results and increasing volumes of litigation mandate an approach which guarantees greater uniformity. A case-by-case method for analyzing whether production of information will be compelled does not provide the most effective deterrent against securities law violators.²⁰⁹ Second, obtaining a Rule 37 court order is difficult, as the case must be pending before a U.S. District Court. As a result, for the SEC investigation to proceed to this stage, the SEC must engage in time-consuming and costly litigation. Moreover, there is an opportunity cost in that other, possibly more important, enforcement activities are forsaken. Third, litigation creates friction between states. Ultimately, this could impair U.S. foreign relations, as well as damage other investigations.

2. *The Bank of Nova Scotia Case.*—*United States v. Bank of Nova Scotia*²¹⁰ is relevant for its insight into litigation's costly effect on the financial intermediary. First, however, it is necessary to assess the mechanics of the court's judgment.

In this case, the Bank of Nova Scotia, a Canadian bank, maintained branches in approximately forty-five countries, including the United States and the Bahamas.²¹¹ A customer of the Bahamas branch was being tried in the United States for tax and narcotics violations.²¹² During the trial, the U.S. court issued a subpoena *duces tecum* requesting information on transactions initiated by the customer.²¹³ When the Bank refused to comply, citing Bahamian bank secrecy law, the court found the Bank in contempt, noting that a mere assertion of illegality would be insufficient to evade sanctions.²¹⁴

The Bank asserted, among other things, that comity between countries precluded the enforcement of the subpoena.²¹⁵ Specifically, the Bank argued that the U.S. government "could avoid rather than provoke disrespect for the sovereignty of a friendly nation" by pursuing

208. R. Kauffman, *Secrecy and Blocking Laws: A Growing Problem as the Internationalization of Securities Markets Continues*, 18 VAND. J. TRANSNAT'L L. 831-33 (1985).

209. STAFF OF PERMANENT SUBCOMMITTEE ON INVESTIGATIONS OF SENATE COMMITTEE ON GOVERNMENTAL AFFAIRS, CRIME AND SECRECY: THE USE OF OFFSHORE BANKS AND COMPANIES 325 (1983).

210. 691 F.2d 1384 (11th Cir. 1982).

211. *Id.* at 1386.

212. *Id.*

213. *Id.*

214. *Id.* at 1387.

215. *Bank of Nova Scotia*, 691 F.2d at 1389-91.

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the alternative of applying for an order of judicial assistance permitting disclosure from the Supreme Court of the Bahamas.²¹⁶ The court rejected this argument, and under the rubric of comity,²¹⁷ contended that the judicial assistance procedure would not provide due deference to the interests of the United States.²¹⁸

The U.S. court conceded that enforcement of such a subpoena could potentially result in a deterioration of relations between the two countries. Nevertheless, the court concluded that:

While it is true courts should not impinge upon the political prerogatives of the government in the sensitive area of foreign relations (*Chicago and Southern Air Lines v. Waterman Steamship Corp.*), accepting the Bank's position would be a greater interference with foreign relations than the procedures employed here. In essence, the Bank would require the government to choose between impeding the grand jury's investigation and petitioning the Supreme Court of the Bahamas for an order of disclosure.²¹⁹

The court further considered whether the Bank approached the proceedings in good faith. Briefly, the court asserted that the Bank failed to bring itself within the ambit of *Société Internationale*.²²⁰ The Bank had not pursued good faith efforts to comply with the SEC subpoena.²²¹ As a consequence of the Bank's failure to release customer information, civil contempt sanctions were imposed.²²² By the time the Bank completely complied with the subpoena to produce offshore documents, its \$25,000 per day fine totaled \$1,825,000.²²³

This case, like the *St. Joe Case*, exhibits that the SEC can achieve results with litigation. Notwithstanding these pyrrhic victories, it is submitted again that litigation remains an untenable long term solution.

216. *Id.* at 1390.

217. Although the court couched its reasoning under the rubric of comity, in fact, it is submitted, they engaged in a balancing of interests test.

218. "In essence, the Bank asks the court to require our government to ask the courts of the Bahamas to be allowed to do something lawful under US law. We conclude such a procedure to be contrary to the interests of our nation and outweigh the interests of the Bahamas." *Bank of Nova Scotia*, 691 F.2d at 1391.

219. *Id.* at 1388.

220. *Id.* at 1388-89.

221. *Id.* In later litigation on the same issue the same court held that "[t]he Bank had voluntarily elected to do business in numerous foreign countries and has accepted the incidental risk of occasional inconsistent governmental actions. It cannot expect to avail itself of the benefits of doing business here without accepting the concomitant obligations." *Re Grand Jury Proceedings Bank of Nova Scotia*, 740 F.2d 817 (11th Cir. 1984).

222. *Grand Jury Proceedings*, 740 F.2d at 819.

223. *Id.* at 824.

Elaborating on the shortcomings discussed above, this case demonstrates the intolerable dilemma for third party multinational banks that hold confidential information as fiduciaries for others.²²⁴ The frequency of conflicting jurisdictional problems for the multinational bank only seems to be increasing. The United States' resort to litigation, while satisfying for short-term objectives, proves to be no more acceptable for either the securities regulator or the financial institution. Confrontation between the bank and securities regulator often results in the diversion of the investigation, as resources are expended on the debate over disclosure rather than on the primary objectives of the investigations.²²⁵ Further, despite the drain on the bank's resources, the securities regulator encounters an opponent willing and capable of bearing the costs involved in such litigation.

In a wider context, *Bank of Nova Scotia* equally reveals that the continued assertion of extraterritorial jurisdiction serves to irritate relationships with other countries. Both Canada and the Bahamas filed *amicus curiae* briefs with the court to emphasize their dissatisfaction with the U.S. approach. In effect, U.S. investigative efforts are capable of alienating otherwise friendly nations. The attempt also weakens a critical foundation of international law, namely, the sovereign equality of all states. This principle of international law dictates that the conflicting authorities of two sovereign states be given equal weight. It would seem to follow that a private party should not be penalized for choosing to obey one state at the other's expense. However, this is precisely what happens to the multinational bank.

3. *The Santa Fe Case*.—This case may be distinguished from the two cases above because in *Sante Fe*, an information sharing agreement, while not specifically on insider trading, was tested. In the *Santa Fe* case,²²⁶ the SEC brought civil proceedings in New York alleging that insider trading had occurred prior to the takeover of Santa Fe by Kuwait Petroleum. The SEC contended that Swiss banks with branch offices in the United States had unknowingly acted as conduits through which the prohibited trading had occurred.²²⁷ Accordingly, the SEC requested the names of the banks' customers involved in the transactions in issue.²²⁸

224. Douglas E. Rosenthal & Stephen Yale-Loehr, *Two Cheers for the ALI Restatement's Provisions on Foreign Discovery*, 16 N.Y.U. INT'L L. & POL 1075, 1081 (1984).

225. Newcomb, *supra* note 189, at 564.

226. 23 I.L.M. 511 (1984).

227. *See id.*

228. In this case, the SEC was unaware of the identity of the purchaser for whom the Swiss bank executed the transaction. Accordingly, it filed a "John Doe" complaint naming the "unknown

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The U.S. court granted the SEC's request for an order to produce the relevant information.²²⁹ Once again, the Swiss banks initially refused to comply with the court order, citing Swiss bank secrecy law and customer confidentiality.²³⁰

The SEC could have opted to pursue a course of action similar to the successful one employed in the *St. Joe Case*. However, the SEC, acting through the Justice Department, applied for Swiss assistance under the 1977 United States-Switzerland Treaty for Mutual Assistance in Criminal Matters, ratified in 1977.²³¹ This treaty established assistance measures that were specifically developed to allow a requesting country to obtain necessary information for investigations of offenses committed within the requesting country's jurisdiction.²³² In accordance with the Treaty, the matter was heard before the Swiss Federal Tribunal, where the SEC request was initially rejected. Following a second request by the SEC, the Swiss Federal Tribunal granted the SEC's application. Forty-one months after the initiation of litigation, the Swiss delivered the requested information to the SEC. This case reveals that the Treaty was not helpful to the SEC in its goal of rationalizing securities investigations with an international element.

In spite of the protracted proceedings, the *Santa Fe* case demonstrates that the SEC received the information it requested. More important, the case substantiates the claim that litigation has the capacity to induce bank secrecy jurisdictions to enter into specific insider trading information sharing agreements with the United States. Forcing disinterested havens to the bargaining table is the genuine benefit of litigation.

In August 1982, after the *St. Joe Case* and during the *Sante Fe* litigation, the United States and Switzerland agreed on a Memorandum of Understanding which declared the commitment of both countries to improve measures established by the 1977 Treaty for use in insider trading investigations.²³³ Moreover, these two cases awakened the Swiss insider trading bill, which had rested idle since its introduction

purchaser" as the principal defendant and the Swiss bank as a nominal defendant. *Id.*

229. *Id.*

230. *Id.* See 22 I.L.M. 785 (1983) (Swiss decision of the *Sante Fe* case).

231. Treaty for Mutual Assistance in Criminal Matters, U.S.-Switz., May 25, 1973, 27 U.S.T. 2019 [hereinafter U.S.-Swiss Treaty for Assistance in Criminal Matters].

232. *Id.* art. 4(1).

233. Memorandum of Understanding to Establish Mutually Acceptable Means for Improving International Law Enforcement Cooperation in the Field of Insider Trading, United States-Switzerland, Nov. 3, 1993, 22 I.L.M. 1.

some ten years earlier.²³⁴ Although the Swiss legislation machine operates at a slow pace, this bill was given priority. The result was the prohibition of insider trading under article 161 of the Swiss Penal Code which came into effect in July 1988.²³⁵

Interestingly enough, a number of countries enacted or modified insider trading legislation in the 1980s in the wake of *St Joe* and *Sante Fe* cases and the villainous yet fantastic set of insider trading cases involving Levine and friends. Jurisdictions that took legislative action include: (1) Canada; (2) France; (3) Hong Kong; (4) Japan; (5) Switzerland; (6) the Netherlands; and (7) the United Kingdom.²³⁶ The hypothesis could be advanced that the United States provided the impetus for these changes. In effect, the U.S. government vicariously effected an international policy goal, namely universal opprobrium of insider trading, through the legislative bodies of foreign countries-extraterritoriality *par excellence*.

The same hypothesis could be proposed regarding the U.S. capacity to conclude numerous information sharing agreements in an attempt to achieve a domestic policy goal, namely, the maintenance of fair and efficient U.S. securities markets in the wake of increased transborder securities trading. With Switzerland, the traditional haven, neutered, it is maintained that the *Bank of Nova Scotia* litigation forced numerous haven jurisdictions in the Caribbean basin to reassess how they deal with foreign requests for information. Arguably, *Bank of Nova Scotia* prompted mutual assistance treaties between the United States and each of the Bahamas, the Cayman Islands, and Jamaica. The Cayman Islands mutual assistance treaty makes specific provision for releasing information relating to insider trading offenses. As argued earlier, the Bahamas MLAT potentially could address insider trading requests. The Jamaican mutual assistance treaty has no requirement of dual criminality.²³⁷ Conceivably, then, it is irrelevant to inquire if Jamaica has outlawed insider trading.

Indeed, the hypothesis that the United States unilaterally controls the executive and legislative organs of foreign countries is contestable. One could argue that two or three cases could not categorically prompt an international review of insider trading legislation or the stimulus to sign

234. W. de Capitani, *Banking Secrecy Today*, 10 U. PA. J. INT'L BUS. L. 65 (1988).

235. M. Mann & L. Lustgarten, *Internationalization of Insider Trading Enforcement — A Guide to Regulation and Co-operation in EUROPEAN INSIDER DEALING* 362 (K. Hopt & E. Wymeersch eds., 1991).

236. *Id.* at 362-73.

237. *Id.*

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information sharing agreements. However, it is conceivable that litigation as a tool of the securities regulator has the capacity to force all countries to evaluate how they view securities regulation and how they deal with the SEC.

G. Summary

In Subpart A, it was stated that the success of the SEC's litigation efforts would be evaluated. Success is a malleable concept. If success entails efficiency or economy then the SEC's approach has been unsuccessful. All three cases were time-consuming and expensive. If success can be measured by the ability of U.S. courts to render consistent judgments against offshore banks that refuse to divulge customer identity, again, the SEC's approach has been unsuccessful. *Société Internationale* held that a bank bound by foreign secrecy law, which nevertheless acts in good faith, may avoid sanctions. In contrast, appellate court judgments narrowly confine this Supreme Court holding to the particular facts of the case. The resulting absence of judicial clarity creates manifest inconvenience for the potential litigant. Justice demands certainty. If, however, success is equated with the ability of the SEC to further its agenda of increasing international cooperation in insider trading investigations, then, a degree of success has been achieved.

IV. Conclusion

Three short sentences identify the crux of the problem discussed in this article: "Securities regulation is local. But securities trading is international. It is inevitable, therefore, that there may be collision between high and low-regulated states."²³⁸ In seeking a solution to the challenges of international law and foreign relations that emerge from this conflict of laws, a degree of parochialism and rigidity emerges from both the disclosure-oriented United States and the secrecy-oriented haven jurisdictions. In essence, opposing societal values fill the gap between disclosure and secrecy. The United States, for example, regards bank secrecy laws as the hallmark of fraud. In contrast, the haven believes bank secrecy laws are the hallmark of freedom, insofar as financial privacy begets freedom. As a number of concluded international agreements attest, however, there is a middle ground on which to cooperate.

238. P. Wood, *Financial Conglomerates and Conflicts of Interest in CONFLICTS OF INTEREST IN THE CHANGING WORLD* 74 (R. Goode ed., 1986).

The internationalization of securities markets occupies this middle ground. Through the rapid growth of formerly insignificant securities markets, as well as the emergence of new securities markets, a plethora of jurisdictions are now confronted with the issue of transactions shielded by bank secrecy laws. Moreover, with the integration of securities markets, insider trading has the potential to affect linked exchanges. Thus, the concerns of the U.S. regulator have become the concerns of many regulators. Inevitably, this induces cooperation.

U.S. regulators are equally concerned about the negative effect of internationalization on domestic markets. Obscure jurisdictions like Rarotonga and Vanuatu are all too willing to initiate the transactions that other havens will not. As stated by one scholar: "There has always been and always will be a huge quantity of international money, owing allegiance to no particular country, looking for a home where secrecy is guaranteed."²³⁹ Securities regulators must be responsive to the dynamics of internationalization if markets are to keep fraud in abeyance. Litigation, as demonstrated in this article, is not the long term answer. Although it peeled back the leaves of the palm tree, it was a costly and inefficient exercise. Cooperation is the way forward. It uproots the tree.

239. F. Neate, *Introduction in BANK CONFIDENTIALITY* xviii (F. Neate & R. McCormick eds., 1990).