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Regulating Offshore Finance

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From the Panama Papers to the Paradise Papers, massive document leaks in recent years have exposed trillions of dollars hidden in small offshore jurisdictions. Attracting foreign capital with low tax rates and environments of secrecy, a growing number of offshore jurisdictions have emerged as major financial havens hosting thousands of hedge funds, trusts, banks, and insurance companies.

While the prevailing account has examined offshore financial havens as "tax havens" that facilitate the evasion or avoidance of domestic tax, this Article uncovers how offshore jurisdictions enable

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business entities to opt out of otherwise mandatory domestic regulatory laws. Specifically, recent U.S. Supreme Court cases restricting the geographic scope of federal statutes create a space for commercial actors to circumvent regulation by incorporating in offshore jurisdictions. Under this jurisprudence, financial transactions completed through offshore commercial entities are often, albeit not categorically, seen as "extraterritorial" transactions beyond the reach of federal statutes. This makes it increasingly difficult for private litigants to bring statutory claims designed to protect the workings of the market, even in cases that are predominantly connected to the United States. After documenting how offshore jurisdictions enable commercial entities to opt out of federal regulatory statutes, this Article critiques the Supreme Court's recent extraterritoriality jurisprudence that risks breeding a cottage industry of private regulatory evasion.

INTRODUCTION

By some accounts, more than $2.6 trillion in untaxed profits of U.S. companies are held in offshore jurisdictions.[1] These jurisdictions—typically small, sun-drenched islands with minimal permanent workforce—have transformed in recent years into major financial havens hosting hedge funds, trusts, insurance companies, and banks.[2] Bermuda, a famous vacation destination in the Atlantic Ocean with a tiny permanent population, is now the world's largest provider of captive insurance—a form of sophisticated self-insurance.[3] The Cayman Islands, located in the Western Caribbean, is estimated to be home to upward of sixty percent of the world's hedge fund assets,[4] and reportedly the third-largest holder of U.S. government debt.[5] This is a phenomenon engineered at least in part by lawyers, judging by the emergence of "offshore magic circle" law firms in recent years that purport to provide full-service law practice ranging from offshore mergers and acquisitions to offshore fund formations.[6]

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1. *See* Lynnley Browning, *Trump's Offshore Tax Plan May Mean Perk for Apple, Pfizer*, BLOOMBERG (June 12, 2017), http://www.bloomberg.com/news/articles/2017-06-12/trump-s-offshore-tax-plan-may-mean-extra-perk-for-apple-pfizer [https://perma.cc/XTM5-BLLN].

2. *See* RONEN PALAN, RICHARD MURPHY & CHRISTIAN CHAVAGNEUX, TAX HAVENS: HOW GLOBALIZATION REALLY WORKS 8–10 (2010).

3. CHRISTOPHER BRUNER, RE-IMAGINING OFFSHORE FINANCE: MARKET DOMINANT SMALL JURISDICTIONS IN A GLOBALIZING FINANCIAL WORLD 59 (2016).

4. Jan Fichtner, *The Anatomy of the Cayman Islands Offshore Financial Center: Anglo-America, Japan, and the Role of Hedge Funds*, 23 REV. INT'L POL. ECON. 1034, 1034 (2016) ("About 60% of global hedge fund assets are legally domiciled in Cayman . . . .").

5. Eliza Ronalds-Hannon, *Hedge Funds' Misery Exposed as Caribbean Proxies Dump Treasuries*, BLOOMBERG (June 21, 2016), https://www.bloomberg.com/news/articles/2016-06-21/hedge-funds-misery-exposed-as-caribbean-proxies-dump-treasuries [https://perma.cc/2TD3-UFCP].

6. *See, e.g.*, *Corporate*, APPLEBY, http://www.applebyglobal.com/services/corporate.aspx (last visited Jan. 19, 2018) [https://perma.cc/GX23-N24H]; Will Fitzgibbon, *Appleby, the Offshore Law Firm With a Record of Compliance Failures*, IRISH TIMES (Nov. 5, 2017), https://www.irishtimes.com/business/appleby-the-offshore-law-firm-with-a-record-of-compliance-failures-1.3280860 [https://perma.cc/YG76-HB6M]; *see also* Matthew Valencia, *Storm Survivors*,

The visual paradox of tiny islands transforming into hubs of modern finance has attracted the scrutiny of lawmakers and academics alike, most prominently in efforts to curtail tax evasion or avoidance.[7] The United States famously levies corporate tax based on a corporate entity's place of incorporation, incentivizing corporations operating within the United States to "migrate" offshore by forming entities incorporated in offshore jurisdictions.[8] Permutations are endless, but some of the most successful offshore financial havens typically levy no corporate or capital gains tax, enabling corporate entities to purchase legal status at a reasonable cost with little or no economic activity in the "host" states.[9]

But tax is only part of the story. As this Article will show, offshore corporate structure enables commercial entities to evade domestic regulatory laws, particularly under recent U.S. Supreme Court case law strengthening the presumption against applying federal statutes in cases with both domestic and foreign facts.[10] Under this

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ECONOMIST (Feb. 16, 2013), http://www.economist.com/news/special-report/21571549-offshore-financial-centres-have-taken-battering-recently-they-have-shown-remarkable [https://perma.cc/HR4H-ZF2K] (assessing that offshore financial havens grew "often with help from lawyers based in Wall Street or the City of London").

7. Scholars typically distinguish tax evasion, a set of illicit activities aimed at reducing taxes, from tax avoidance, which includes various forms of *legal* maneuvering. *See, e.g.*, Conor Clarke, *What Are Tax Havens and Why Are They Bad?*, 95 TEX. L. REV. 59, 68 (2016) (reviewing GABRIEL ZUCMAN, THE HIDDEN WEALTH OF NATIONS: THE SCOURGE OF TAX HAVENS (2015)) ("Tax evasion usually refers to the illegal failure to report income. Tax avoidance usually refers to legal . . . forms of tax planning that reduce tax liability." (footnote omitted)).

8. Throughout this Article, I use the terms "offshore financial havens" and "tax havens" interchangeably to describe sovereign nation states (e.g., the Bahamas) or semisovereign states (e.g., the Cayman Islands) with lawmaking authority that attract foreign capital predominantly through offering a combination of light regulation and low tax rates. There is no consensus around which jurisdictions constitute "tax havens" or "offshore financial havens." For general definitions, see BRUNER, *supra* note 3, at 19–25.

9. *Id.* at 19–23.

10. This line of jurisprudence is doctrinally guided by a canon of statutory interpretation known as the presumption against extraterritoriality. *See infra* Section II.A. Recent Supreme Court cases strengthening the presumption against extraterritoriality include *RJR Nabisco, Inc. v. European Community*, 136 S. Ct. 2090 (2016); *Kiobel v. Royal Dutch Petroleum Co.*, 133 S. Ct. 1659 (2013); and *Morrison v. National Australia Bank Ltd.*, 561 U.S. 247 (2010). The trio of blockbuster decisions in *Morrison*, *Kiobel*, and *Nabisco* may be a reflection of the current Supreme Court's aversion to adjudicating transnational cases. *See* Pamela K. Bookman, *Litigation Isolationism*, 67 STAN. L. REV. 1081, 1097–99 (2015) (considering the presumption a means for "transnational litigation avoidance"). Or it may be part of an agenda to rein in private litigants run amok. *See* Paul B. Stephen, *Private Litigation as a Foreign Relations Problem*, 110 AJIL UNBOUND 40, 40 (2016) (proposing that *Morrison*, *Kiobel*, and *Nabisco* represent the Court's willingness to constrain civil litigants' ability to reach foreign actors); Carlos M. Vázquez, *Out-Beale-Ing Beale*, 110 AJIL UNBOUND 68, 72 (2016) (considering *Morrison*, *Kiobel*, and *Nabisco* illustrative of the Court's hostility to private rights of action generally). Regardless of the motives, there seems to be a consensus around the idea that recent Supreme Court jurisprudence has strengthened the presumption against applying federal statutes extraterritorially. *See infra* Section II.B.

jurisprudence, financial transactions completed through offshore commercial entities are often, albeit not categorically, seen as "extraterritorial" transactions outside the reach of federal statutes.[11] The legal residence of commercial entities matters particularly in cases arising out of modern financial transactions that appear to defy or simply transcend territorial borders.[12]

The result is an increasing difficulty faced by private litigants bringing claims involving commercial entities registered in offshore jurisdictions—even in cases that are predominantly connected to the United States. Thus, for instance, in *Cascade Fund, LLLP v. Absolute Capital Management Holdings Ltd.*, an investment fund registered in the Cayman Islands was able to dodge federal securities fraud claims on grounds that the transaction was nondomestic, even while soliciting U.S. investors within U.S. territory.[13]

Cascade Fund is hardly an unusual case. In addition to intimately playing a role in the largest Ponzi scheme ever recorded in U.S. history,[14] the footprints of offshore financial havens are readily apparent in a significant number of disputes spanning U.S. bankruptcy law,[15] the civil Racketeer Influenced and Corrupt Organizations ("RICO") Act,[16] the Employee Retirement Income Security Act

11. *See infra* Section II.B.

12. The domicile of commercial entities matters particularly in these cases because they serve as tangible markers available to impute location to transactions that lack clear-cut territorial connections to a particular jurisdiction. *See infra* Section II.B.3. As Professor Hannah Buxbaum explains, many financial transactions "touch[ ] . . . multiple countries or are executed by electronic or other means to which it is difficult to assign a location at all." Hannah L. Buxbaum, *Remedies for Foreign Investors Under U.S. Federal Securities Law*, 75 L. & CONTEMP. PROBS. 161, 167–68 (2012) [hereinafter Buxbaum, *Remedies*]. For instance, swap transactions, a form of contracts involving the exchange of financial instruments, "can be between participants in two different countries, booked in a third country, and risk-managed in a fourth country." John C. Coffee, Jr., *Extraterritorial Financial Regulation: Why E.T. Can't Come Home*, 99 CORNELL L. REV. 1259, 1274 (2014).

13. Cascade Fund, LLLP v. Absolute Capital Mgmt. Holdings Ltd., No. 08-CV-01381-MSK-CBS, 2011 WL 1211511, at *7 (D. Colo. Mar. 31, 2011).

14. *See* Sec. Inv'r Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC, No. AP 08-01789, 2016 WL 6900689, at *2 (Bankr. S.D.N.Y. Nov. 22, 2016) (identifying feeder funds formed in the British Virgin Islands and the Cayman Islands as part of "the largest Ponzi scheme ever discovered").

15. *See, e.g.*, *In re* Gerova Fin. Grp., Ltd., 482 B.R. 86, 88, 89 (Bankr. S.D.N.Y. 2012) (deferring to insolvency proceeding in Bermuda notwithstanding the acknowledgement that "Gerova may have had significant assets in the United States").

16. *See, e.g.*, Absolute Activist Value Master Fund Ltd. v. Devine, 233 F. Supp. 3d 1297, 1305 (M.D. Fla. 2017) (dismissing civil RICO claim involving Cayman Islands funds notwithstanding the alleged schemes taking place in Florida by a Florida resident).

("ERISA"),[17] excise tax,[18] and securities fraud.[19]

Alarmingly, the restrictive form of extraterritoriality jurisprudence devised by recent Supreme Court cases facilitates various forms of regulatory arbitrage,[20] converting otherwise mandatory laws of the United States into default rules under the pretense of being governed by the laws of offshore financial havens.[21]

Regulatory evasion of this kind is problematic because the mandatory nature of certain statutes that typically forbid private entities from contractually waiving compliance with these laws may indicate that there are costs associated with certain forms of private misconduct that are not being fully internalized by the private parties.[22] Moreover, regulatory statutes can be designed to advance certain social policies, even when doing so conflicts with private preferences.[23] It gives little comfort that the laws of offshore financial havens are often straightforward cases of legislative capture, whereby laws can literally

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17. *See, e.g.*, *In re* Meridian Funds Grp. Sec. Litig., 917 F. Supp. 2d 231, 237 (S.D.N.Y. 2013) (discussing extraterritorial application of ERISA relating to a fund organized in the Cayman Islands).

18. *See, e.g.*, Validus Reinsurance, Ltd. v. United States, 786 F.3d 1039, 1041 (D.C. Cir. 2015) (declining to apply federal excise tax under 26 U.S.C. § 4371 to a Bermudan reinsurance company selling "reinsurance to insurance companies that sell policies covering risks, liabilities, and hazards within the United States").

19. *See, e.g.*, *In re* Banco Santander Sec.-Optimal Litig., 732 F. Supp. 2d 1305, 1317 (S.D. Fla. 2010) (dismissing a claim brought under Rule 10b-5 reasoning that "[t]he funds at issue in this case are registered under the laws of the Bahamas, and the Plaintiffs purposefully went off-shore to invest").

20. *See infra* Section III.B; *see also* Sean J. Griffith, *Substituted Compliance and Systemic Risk: How to Make a Global Market in Derivatives Regulation*, 98 MINN. L. REV. 1291, 1293 (2014) ("In the context of derivatives, if U.S. authorities impose a harsh clearing regime, banks may shift their derivatives operations to London or, if European and American regulation converge, to Hong Kong or Singapore or some less highly regulated jurisdiction.").

21. Consider, for instance, the Securities Exchange Act of 1934. The statute expressly prohibits parties from avoiding liability for securities fraud through direct contractual waiver. *See* Securities Exchange Act of 1934, 15 U.S.C. § 78cc(a) (2012) ("Any condition, stipulation, or provision binding any person to waive compliance with any provision of this chapter or any rule or regulation thereunder, or of any rule of an exchange required thereby shall be void."). But sellers of security products soliciting U.S. investors have been able to opt out of securities fraud suits by structuring transactions through offshore commercial entities, thereby appearing to complete transactions offshore. *See infra* Section II.B.3.

22. *See* William W. Bratton & Joseph A. McCahery, *The New Economics of Jurisdictional Competition: Devolutionary Federalism in a Second-Best World*, 86 GEO. L.J. 201, 231–32 (1997) (explaining that "individual actions have external effects . . . whenever one's actions impact on the interests of others and one fails to account for such impact"); Joel P. Trachtman, *Economic Analysis of Prescriptive Jurisdiction*, 42 VA. J. INT'L L. 1, 17 (2001) (explaining that a state may be less likely to apply a law if its violation "has adverse effects in other jurisdictions and lacks adverse effects in the regulating jurisdiction").

23. Ralf Michaels, *Economics of Law as Choice of Law*, 71 L. & CONTEMP. PROBS. 73, 79 (2008).

be written by interested private actors.[24] The policy danger, at its extreme, is the emergence of a regulatory lacuna where no sovereign regulates forms of misconduct that could have substantial impact on society at large.

This Article strips away the largely presupposed notion that a foreign sovereign interest is triggered by virtue of a corporate entity maintaining its juridical residence in a foreign jurisdiction—an assumption that is currently constraining federal courts from applying federal statutes in cases involving offshore commercial entities.[25]

Importantly, prescriptive jurisdiction, a jurisdictional principle allocating interjurisdictional authority,[26] concerns lawmakers' authority "to regulate conduct—namely, the location of the conduct."[27] A claim to regulate conduct based solely on the location of a commercial entity is a claim bootstrapped in legal fiction that reveals little to nothing about the location of the conduct that the law would seek to regulate. While domicile is a concept used to impute location for the purposes of determining the laws governing the "internal affairs" of corporate entities,[28] it need not align with the location of the actors that the law would seek to regulate.

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24. *See infra* Section III.C.

25. Federal courts recognize foreign sovereign interests through a variety of comity doctrines, including the presumption against extraterritoriality, the act of state doctrine, prescriptive and judicial comity, and foreign sovereign immunity. *See* William S. Dodge, *International Comity in American Law*, 115 COLUM. L. REV. 2071, 2079, 2099–2119 (2015) [hereinafter Dodge, *International Comity*] (extensively detailing the "many doctrines of American law [that] manifest the principle of international comity"); Eric A. Posner & Cass R. Sunstein, Chevron*izing Foreign Relations Law*, 116 YALE L.J. 1170, 1179–80 (2007) (reviewing comity doctrines that "must be justified in different terms because they promote American interests at the expense of comity"). The focus of this Article is on the presumption against extraterritoriality doctrine (and prescriptive comity to the extent that the doctrine is not already woven into the presumption against extraterritoriality doctrine). *See infra* Section III.A.

26. Trachtman, *supra* note 22, at 2–3 ("Prescriptive jurisdiction (and its private law cognate, choice of law) is the term used to refer to the critical question of allocation of public authority in a horizontal interstate system.").

27. Anthony J. Colangelo, *What Is Extraterritorial Jurisdiction?*, 99 CORNELL L. REV. 1303, 1305 (2014).

28. *See* Edgar v. MITE Corp., 457 U.S. 624, 645 (1982) ("The internal affairs doctrine is a conflict of laws principle which recognizes that only one State should have the authority to regulate a corporation's internal affairs . . . because otherwise a corporation could be faced with conflicting demands."); Frederick Tung, *Before Competition: Origins of the Internal Affairs Doctrine*, 32 J. CORP. L. 33, 33–34 (2006); *see also* Curtis Alva, *Delaware and the Market for Corporate Charters: History and Agency*, 15 DEL. J. CORP. L. 885, 887 n.6 (1990):

> The location of the corporate domicile is important because state corporation codes vary significantly and the internal affairs of a corporation (such as what powers belong to the board of directors, what limitations can be placed on their compensation, what kinds of self-interested transactions can members of the board of directors enter into, what duties must directors and officers perform, and in what ways can directors and officers be found liable for breaches of those duties) are governed by the general corporation law

This metaphysical assertion becomes more concrete when we unpack what the concept of corporate domicile entails.[29] Unlike domicile of a natural person, which typically entails an individual establishing her "headquarters" through an overwhelming territorial relationship with a particular jurisdiction,[30] domicile of commercial entities is a form of private contract aimed at opting out of a bundle of rules imposed by one legal regime in favor of another.[31] Offshore financial havens typically have no plausible claim to prescribe conduct underlying financial transactions completed through offshore commercial entities because the decisionmaking authority of relevant commercial entities lies not in the place of incorporation but in "nerve centers" located in "onshore" jurisdictions, including the United States.[32]

Indeed, a very high percentage of corporate entities registered in offshore financial havens are "exempted" or "excepted" entities under

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> of the state of incorporation—even if the corporation's principal office, all of its physical assets, and its principal place of business are in other states . . . .

Courts also impute situs to intangibles like corporate stock as if they are sited at the domicile of the corporation. Aaron D. Simowitz, *Siting Intangibles*, 48 N.Y.U. J. INT'L L. & POL. 259, 279 (2015).

29. A brief word on terminology may be useful here. By "corporate domicile," I primarily (but not exclusively) refer to a corporate entity's place of incorporation. I say "not exclusively" because firms operating in certain sectors of finance are able to (or at least claim to) locate their headquarters in offshore financial havens without physically moving offshore. *See infra* Section I.B. I use the term generically to capture the instances where corporate entities use offshore financial havens to establish juridical residence, while leaving the nerve center—where officers or managers direct, control, and coordinate the corporation's activities, *see infra* note 32—elsewhere. While there will inevitably be blurry lines, relatively few corporate entities incorporated in offshore financial havens currently have significant physical presence in those jurisdictions. *See infra* Section III.B.

30. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 16 (AM. LAW INST. 1971); *see also* Jack L. Goldsmith III, Note, *Interest Analysis Applied to Corporations: The Unprincipled Use of a Choice of Law Method*, 98 YALE L.J. 597, 603 (1989) [hereinafter Goldsmith, *Interest Analysis*] ("The model of a person having one and only one permanent and specific residence correlates fairly well with reality.").

31. As Professors Henry Hansmann and Reinier Kraakman explain, commercial legal entities are "simply standard-form contracts among the parties who participate in an enterprise—including, in particular, the organization's owners, managers, and creditors." Henry Hansmann & Reinier Kraakman, *The Essential Role of Organizational Law*, 110 YALE L.J. 387, 390 (2000).

32. The term "nerve center" should sound familiar to teachers of civil procedure. The term is used to determine a corporation's principal place of business for diversity jurisdiction purposes. *See* Hertz Corp. v. Friend, 559 U.S. 77, 78 (2010) ("The phrase 'principal place of business' in § 1332(c)(1) refers to the place where a corporation's high level officers direct, control, and coordinate the corporation's activities . . . ." (quoting 28 U.S.C. § 1332(c)(1) (2012))). As I will show in Section III.A, the location of actors with decisionmaking authority is significant in deducing the reach of a jurisdiction's lawmaking authority. I am in no way suggesting that prescriptive jurisdiction should generally be conflated with judicial (adjudicative) jurisdiction, the latter of which concerns the authority over subjecting parties to a judicial process. *See* Colangelo, *supra* note 27 (analyzing the scope of extraterritorial jurisdiction).

the laws of those jurisdictions, formed for the express purpose of doing business *outside* of those jurisdictions.[33] For instance, approximately ninety-six percent of corporate entities registered to a popular registration office in the Cayman Islands are "exempt companies, exempt limited partnerships, and exempt trusts,"[34] meaning that they are "generally prohibited from trading within the Cayman Islands."[35] The status of these entities is important, for it reveals that a vast array of financial dealings involving offshore entities do not implicate actual conduct or decisionmaking taking place in offshore jurisdictions.

This is a subject that deserves wider scrutiny.[36] While small offshore jurisdictions have received sustained scrutiny by tax scholars, they are relatively unexamined hotbeds of transnational disputes laden with high financial stakes and fundamental theoretical questions. Rather than seeking to give a comprehensive accounting, this Article presents a broad sketch that future research can build on to further shed light on the topic.

The remainder of this Article is organized in three parts. Part I documents the dramatic rise of offshore financial havens in facilitating private financial transactions in recent decades, becoming a central feature of the modern economy. It frames this discussion by drawing on tax and regulatory arbitrage scholarship and identifies an important

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33. Tony Heaver-Wren & Jeremy Walton, *Cayman Islands*, *in* CROSS-BORDER INSOLVENCY: A COMMENTARY ON THE UNCITRAL MODEL LAW 87, 87 (Look Chan Ho ed., 2009) ("Most companies incorporated in the Cayman Islands are registered as 'exempted' companies. Such companies are prohibited from trading in the Cayman Islands except in furtherance of their business outside the Cayman Islands."); *see also* CONYERS DILL, BERMUDA EXEMPTED COMPANIES 5 (2016), https://www.conyersdill.com/publicationfiles/2016_12_BDA_Bermuda_Exempted_Companies.pdf [https://perma.cc/F6MB-FBLJ] ("Bermuda law distinguishes between those companies which are owned predominantly by Bermudians ('local companies') and those which are owned predominantly by non-Bermudians ('exempted companies'). Only local companies are permitted to carry on and compete for business which is in Bermuda.").

34. U.S. GOV'T ACCOUNTABILITY OFFICE, CAYMAN ISLANDS: BUSINESS AND TAX ADVANTAGES ATTRACT U.S. PERSONS AND ENFORCEMENT CHALLENGES EXIST 12 (2008), http://www.gao.gov/new.items/d08778.pdf [https://perma.cc/X3MV-EZGP] [hereinafter GAO REPORT].

35. *Id.*

36. This is a topic that will increasingly become important, both from practical and theoretical standpoints. For most of the last two centuries, extraterritorial financial regulation was hardly a prominent issue because the objects of financial regulation were "in large part domestic actors, and the bulk of the risks their activities generated were local." Chris Brummer, *Territoriality as a Regulatory Technique: Notes from the Financial Crisis*, 79 U. CIN. L. REV. 499, 503 (2010). Needless to say, this is no longer the case in today's globally interconnected financial economy. *See* David Zaring, *Finding Legal Principle in Global Financial Regulation*, 52 VA. J. INT'L L. 685, 689 (2012) (explaining the import of "globalization of the financial economy" for regulators); David Zaring, *The Legal Response to the Next Financial Crisis*, 24 GEO. MASON L. REV. 533, 537–38 (2017) (describing the varied forms and processes that have been attempted for international financial regulation).

gap left in the prevailing account. Part II contains the descriptive contribution of this piece, uncovering the previously undetected relationship between corporate form and the extraterritorial reach of federal regulatory statutes. In particular, this Part highlights recent cases that predominantly (albeit not categorically) favor delimiting federal statutes in "offshore" cases, critically assessing the impact of the Supreme Court's recent federal extraterritoriality jurisprudence. Part III develops an account conceptualizing offshore corporate structure as a species of transnational private contract, revealing the limited utility of a corporation's juridical home in identifying a sovereign's authority to regulate conduct. This Part also identifies policy considerations that counsel against a doctrinal framework that renders domestic regulatory statutes amenable to private choice.

I. INCORPORATION, TAXES, AND OFFSHORE CORPORATE MIGRATION

By now, most people at least have a vague intuition of what tax havens are all about. It is, after all, a topic that has catapulted the seemingly dry academic subject of taxation into a staple headliner of the *New York Times*.[37] While the earliest forms of tax havens can be traced to the late nineteenth century,[38] U.S. corporations started experimenting with tax havens in the years following World War II,[39] with their use accelerating in pace and scope in recent decades.[40] This Part explains the rise of offshore financial havens and identifies an important gap left in the existing academic treatment of the subject.

A. Offshore Incorporation

At the heart of the various tax avoidance strategies available to business entities today is the U.S. tax rule known as the "place of

37. *See, e.g.*, Scott Shane, Spencer Woodman & Michael Forsythe, *How Business Titans, Pop Stars and Royals Hide Their Wealth*, N.Y. TIMES (Nov. 7, 2017), https://nyti.ms/2jaqe61 [https://perma.cc/2C9L-AGNP]; Andrew Ross Sorkin, *When It Comes to Tax Avoidance, Donald Trump's Just a Small Fry*, N.Y. TIMES (Oct. 4, 2016), https://nyti.ms/2klNZ6E [https://perma.cc/E3RX-6GUG].

38. Ronen Palan, *Tax Havens and the Commercialization of State Sovereignty*, 56 INT'L ORG. 151, 153 (2002) [hereinafter Palan, *Commercialization*] (tracing the "emergence of the first modern tax havens" to "the last years of the nineteenth century").

39. *See* William W. Park, *Fiscal Jurisdiction and Accrual Basis Taxation: Lifting the Corporate Veil to Tax Foreign Company Profits*, 78 COLUM. L. REV. 1609, 1613 (1978) ("In the years following World War II, many American companies established foreign subsidiaries in countries with little or no income taxation. American insurance companies were among the greatest offenders in the use of such 'tax havens.' ").

40. BRUNER, *supra* note 3, at 1–5.

incorporation" rule.[41] This rule determines the corporation's legal location as a purely formal criterion based on the entity's place of incorporation,[42] permitting firms headquartered or managed in the United States to avoid U.S. taxpayer status by reincorporating in foreign jurisdictions.[43]

While the more elaborate tax planning tactics span multiple continents around the world in complex legal structuring going by names like "the double Irish Dutch sandwich,"[44] the most basic form of corporate tax planning involves a domestic entity forming an affiliate entity in an offshore financial haven to reduce its effective tax rate. For instance, Houston-headquartered Cooper Industries, Inc. moved its place of incorporation from Ohio to Bermuda, touting that it would "reduce its effective tax rate from about 35% to 18-23%."[45] It is no surprise, then, that the dominant offshore jurisdictions attracting corporate relocation levy nil to zero corporate income tax.[46] Incorporating in offshore jurisdictions enables corporations operating worldwide to pay "only on U.S.-source income and offers other opportunities to shelter U.S. income through transfer pricing, income stripping, and other techniques."[47]

The widespread practice of corporate inversion—a series of complex transactions undergone by a U.S. corporation to reincorporate in a foreign jurisdiction—suggests that the trend toward offshore corporate migration will continue.[48] In my count of recently announced inversion transactions tracked by Professor Eric Talley,[49] Bermuda and

41. *See* I.R.C. § 7701(a)(4) (West 2018). This need not be the rule. Several prominent jurisdictions around the world peg corporate residency to the location of corporate headquarters for tax purposes. *See* ROBERT COUZIN, CORPORATE RESIDENCE AND INTERNATIONAL TAXATION 25 (2002).

42. *See* Omri Marian, *Home-Country Effects of Corporate Inversions*, 90 WASH. L. REV. 1, 3 (2015) ("[U]nder the Internal Revenue Code (IRC) corporate tax residence is determined based on the place of incorporation . . . .").

43. Eric J. Allen & Susan Morse, *Tax-Haven Incorporation for U.S.-Headquartered Firms: No Exodus Yet*, 66 NAT'L TAX J. 395, 395–96 (2013); Daniel Shaviro, *The Rising Tax-Electivity of U.S. Corporate Residence*, 64 TAX L. REV. 377, 378 (2011).

44. Daniel J. Hemel, *The President's Power to Tax*, 102 CORNELL L. REV. 633, 662–64 (2017).

45. Cathy Hwang, *The New Corporate Migration: Tax Diversion Through Inversion*, 80 BROOK. L. REV. 807, 827 (2015) (citing Cooper Indus., Ltd., Registration Statement (Form S-4), at 13–14 (June 11, 2001)).

46. This includes the usual suspects, including the Cayman Islands, the Isle of Man, Jersey, Vanuatu, Bermuda, and the British Virgin Islands. *See* PALAN ET AL., *supra* note 2, at 30–33.

47. Victor Fleischer, *Regulatory Arbitrage*, 89 TEX. L. REV. 227, 246 (2010).

48. Gregory Day, *Irrational Investors and the Corporate Inversion Puzzle*, 69 SMU L. REV. 453, 454 (2016).

49. *See* Eric L. Talley, *Corporate Inversions and the Unbundling of Regulatory Competition*, 101 VA. L. REV. 1649, 1651 (2015) ("analyz[ing] the current inversion wave (and reactions to it) from both practical and theoretical perspectives").

the Cayman Islands together accounted for a staggering forty percent of U.S.-based companies legally migrating to foreign jurisdictions.[50] The figure jumps to sixty-four percent when adding four additional well-known tax havens to the mix—Antigua, the British Virgin Islands, the Marshall Islands, and Ireland.[51] While various legislative and regulatory actions have reacted to the alarming rates of what one commentator has described as "the new corporate migration,"[52] it is too early to determine whether these efforts will accomplish their intended goals.[53]

B. Offshore "Headquarters"

While incorporating in an offshore tax haven remains the primary method employed in tax planning strategies, business entities in certain financial sectors have set up their headquarters in offshore jurisdictions too. This may surprise anyone who studies the demographics of some of the most successful offshore financial havens. For instance, the Cayman Islands, with a total land mass about 1.5 times the size of Washington, D.C., and a permanent population of 58,441 people,[54] is said to house thousands of investment funds.[55]

But perhaps the problem is our overly myopic intuition that corporate activities ought to have extensive territorial contact with a particular jurisdiction. Financial instruments that constitute the bread

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50. *Id.* at 1748–51 app. B.

51. *Id.*

52. Hwang, *supra* note 45, at 807.

53. *Compare Trump to Keep Obama Rule Curbing Corporate Tax Inversion Deals*, REUTERS (Oct. 4, 2017), https://www.reuters.com/article/us-usa-tax-inversions/trump-to-keep-obama-rule-curbing-corporate-tax-inversion-deals-idUSKBN1C92RQ [https://perma.cc/KCR5-HZPV] ("A 2011-2015 wave of inversion deals prompted Treasury to take a series of actions that culminated in an April 2016 rule release and the collapse of a $160-billion deal between U.S. drugmaker Pfizer Inc (PFE.N) and Ireland's Allergan Plc (AGN.N), which would have been the largest inversion ever."), *with* Richard Waters, *Tax Havens Retain Allure for US Tech*, FIN. TIMES (Jan. 24, 2018), https://www.ft.com/content/bcf50bfc-ffd4-11e7-9650-9c0ad2d7c5b5 [https://perma.cc/2U8U-7JDQ] ("The US tax overhaul will not prompt the country's big tech companies to drop their reliance on overseas tax avoidance strategies or create more jobs at home, according to tax experts."); *see also* Day, *supra* note 48, at 461–65 (describing recent regulatory measures aimed to prevent U.S. corporations from migrating to foreign jurisdictions for tax purposes).

54. *The World Factbook: Cayman Islands*, CENT. INTELLIGENCE AGENCY, https://www.cia.gov/library/publications/the-world-factbook/geos/cj.html (last updated Sept. 26, 2018) [https://perma.cc/74HV-PXKS].

55. DAVID CAY JOHNSTON, FREE LUNCH: HOW THE WEALTHIEST AMERICANS ENRICH THEMSELVES AT GOVERNMENT EXPENSE 253 (2007) ("Hedge funds are legally organized offshore, the favorite spot being the Cayman Islands. . . . Most hedge-fund managers have never even been to the Cayman Islands, making the headquarters arrangement a farce."); *see also infra* note 280 (reporting a total of 11,061 funds registered in the Cayman Islands as of June 2015).

and butter of the financial sector are in essence contracts that rely on legal systems to enforce rights.[56] Unlike industries that rely on productive activities tied to an identifiable parcel of territory (think, for instance, automobile manufacturing in Detroit), financial transactions are *legally constituted*.[57] Because finance is built and constituted by systems of rules, the industry need not be territorial at all.[58] This is particularly true for entities like hedge funds or mutual funds that do not serve direct customers.[59]

It is for this reason that firms in several important sectors of finance have been able to structure their operations to locate "the head office in an offshore center with the onshore activities organized into affiliates of the offshore headquarters."[60] Although examples abound, this Section will focus on two salient contemporary illustrations of how commercial entities can be headquartered in offshore jurisdictions without (for the most part) physically moving their operations offshore: hedge funds in the Cayman Islands and insurance companies in Bermuda.

1. Hedge Funds in the Cayman Islands

Hedge funds are investment funds that pool capital from individual and institutional investors aiming to make a positive market return through investing in securities and other assets.[61] To understand how the Cayman Islands, with a tiny permanent workforce, became the world's largest host of hedge funds,[62] one needs to

56. Katrina Pistor, *A Legal Theory of Finance*, 41 J. COMP. ECON. 315, 315 (2013) ("Financial assets *are* contracts the value of which depends in large part on their legal vindication . . . .").

57. *Id.* at 316–18.

58. William J. Moon, *Tax Havens as Producers of Corporate Law*, 116 MICH. L. REV. 1081, 1089–90 (2018) [hereinafter Moon, *Tax Havens*] (reviewing BRUNER, *supra* note 3). This is because finance is "legally constructed" in the sense that financial assets are simply "contracts the value of which depends in large part on their legal vindication." Pistor, *supra* note 56, at 315.

59. Edward D. Kleinbard, *Competitive Convergence in the Financial Services Markets*, 81 TAXES 225, 230–31 (2003).

60. PHILIP R. LANE & GIAN MARIA MILESI-FERRETTI, CROSS-BORDER INVESTMENT IN SMALL INTERNATIONAL FINANCIAL CENTERS 5–6 (2010). As Professor William Magnuson explains, the unprecedented mobility of capital has allowed "companies to operate on a global basis from headquarters in the Cayman Islands or the Seychelles, countries recognized as tax havens." William Magnuson, *Unilateral Corporate Regulation*, 17 CHI. J. INT'L L. 521, 537 (2016).

61. William W. Bratton, *Hedge Funds and Governance Targets*, 95 GEO. L.J. 1375, 1382–83 (2007) ("Some specialize in securities of distressed firms, while others make directional bets on the movement of currency exchange or interest rates. Still others pursue convertible arbitrage, going long in a convertible bond and shorting the underlying common stock."); John Morley, *The Regulation of Mutual Fund Debt*, 30 YALE J. ON REG. 343, 347–48 (2013).

62. Houman B. Shadab, *Hedge Fund Governance*, 19 STAN. J.L. BUS. & FIN. 141, 155 (2013). Some estimate that "around [eighty-five] percent of the world's hedge funds are domiciled in the

understand the basic legal structure of hedge funds. A hedge fund typically consists of three basic entities: "the fund itself, the fund's management company, and the fund's equity investors."[63] In a typical offshore design, the fund's management company is composed of investment professionals who operate "onshore," while the hedge fund itself is in one of the offshore financial havens.[64]

Managers based in the United States typically set up stand-alone business entities called "feeder funds" in offshore jurisdictions principally to cater to two clients: tax-exempt U.S. entities (like university endowments and pension funds) and foreign investors.[65] Feeder funds are important because they help funds avoid triggering U.S. tax liability for both U.S. tax-exempt entities and foreign investors.[66] As an added benefit, Cayman Islands law enables investors to set up opaque financial structures that provide a degree of anonymity from U.S. regulators.[67] These are among the key incentives for offshore funds to keep the *appearance* of foreign territorial operations.[68] As a

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Cayman Islands." *The Cayman Islands: A Guide for Hedge Fund Managers*, MOURANT OZANNES 1 (2017), https://www.mourant.com/file-library/media—-2017/2017-guides/the-cayman-islands—-a-guide-for-hedge-fund-managers.pdf [https://perma.cc/CSR2-98MB].

63. Shadab, *supra* note 62, at 150.

64. *See, e.g.*, SEC v. Gruss, 859 F. Supp. 2d 653, 658 (S.D.N.Y. 2012) (describing a typical offshore fund structure, where the fund was "incorporated, administered, registered, domiciled and regulated in the Cayman Islands" whereas "the actual 'operational and investment decisions for the Offshore Fund were all made by the Offshore Fund's manager, DBZCO, primarily in DBZCO's New York office' " (quoting Complaint ¶ 20, *Gruss*, 859 F. Supp. 2d 653)).

65. Summer A. Lepree, *Taxation of United States Tax-Exempt Entities' Offshore Hedge Fund Investments: Application of the Section 514 Debt-Financed Rules to Leveraged Hedge Funds and Derivatives and the Case for Equalization*, 61 TAX LAW. 807, 815 (2008).

66. *See* DOUGLAS L. HAMMER ET AL., U.S. REGULATION OF HEDGE FUNDS 361 (2005) (discussing the U.S. tax considerations for offshore hedge funds). U.S. tax-exempt entities, for instance, may face domestic tax liability on "unrelated business taxable income," commonly referred to as "UBTI." Offshore feeder funds, also known as blocker corporations, help avoid triggering this tax liability. *See Offshore Hedge Funds vs. Onshore Hedge Funds*, FUND ASSOCIATES 4 (2008), http://fundassociates.com/pdfs/Offshore_vs_Onshore_Funds_Whitepaper.pdf [https://perma.cc/5SEQ-LNSQ]. Similarly, while a foreign investor may possibly trigger tax liability by being considered to be engaged in a U.S. business, investing through an offshore feeder fund "blocks" this potential exposure at the offshore level. *See A Practical Guide to U.S. Tax Compliance Issues for Hedge Fund of Funds*, PEPPER HAMILTON, LLP 4 (2008), http://www.pepperlaw.com/uploads/files/fundoffunds_schneidman_1008.pdf [https://perma.cc/5FZM-CC5N].

67. Fichtner, *supra* note 4, at 1037.

68. *See* Michael Brocard & François-Serge Lhabitant, *A Primer on the Tax Framework of Offshore and Onshore Hedge Funds*, EDHEC BUS. SCH. 23 (2016), https://www.edhec.edu/sites/www.edhec-portail.pprod.net/files/publications/pdf/edhec-working-paper-a-primer-on-the-tax-framework-f_1467203960443-pdfjpg [https://perma.cc/E87T-EJSJ] (discussing hedge funds' complex legal and operational structures that lend themselves to complicated tax structures, particularly in the Cayman Islands). The offshore structure allows the hedge fund to accomplish tax benefits as well. As a widely cited *New York Times* piece explained in 2007, Cayman Islands tax laws help "American fund managers legally defer domestic taxes on their personal profits by

hedge fund consultant based in the Cayman Islands explained in a *Forbes* spread, "In order to ensure that your fund is not seen as being run within the U.S., it's common practice to have a majority of non-U.S. directors on the board of the fund itself."[69] Indeed, several offshore jurisdictions legally require foreign-based funds to establish some form of contact with the jurisdiction, including retaining local directors who play little or no role in the management of the funds.[70]

Absent this legal structure, offshore funds are run by U.S.-based managers no differently than typical onshore funds. As Professor Houman Shadab explains, "[M]anagement companies enjoy the same general plenary powers over offshore funds' investments and other operations as they do with onshore funds."[71]

2. Insurance Companies in Bermuda

Bermuda, a tiny island in the Atlantic Ocean familiar to Americans as a tourist destination, is now the "third largest insurance market in the world."[72] The island boasts its status as the largest supplier of both "reinsurance business" (essentially insurance for insurers) as well as the "captive insurance market" (a sophisticated form of self-insurance of a parent company through a subsidiary insurer).[73]

To understand how Bermuda became a magnet for insurance companies—particularly the ones that focus on providing coverage to U.S.-based risks—one must first understand the structure of the insurance industry. Unlike territory-reliant industries, parts of the insurance industry do not require "significant fixed assets and

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channeling them offshore through their funds." Lynnley Browning, *Offshore Tax Breaks Lure Money Managers*, N.Y. TIMES (July 1, 2007), http://www.nytimes.com/2007/07/01/business/yourmoney/01cay.html [https://perma.cc/4266-2KA7].

69. Ky Trang Ho, *Why Hedge Funds Love to Go Offshore*, FORBES (May 9, 2015), https://web.archive.org/web/20150516100546/http://www.forbes.com:80/sites/trangho/2015/05/09/why-hedge-funds-love-to-go-offshore/3 [https://perma.cc/AS3H-8XT2]; *see also* Shadab, *supra* note62, at 156 ("From a governance point of view, the most distinguishing aspect of offshore hedge funds is that, unlike most of their U.S.-based peers, offshore hedge funds typically have a board of directors . . . . In practice, the oversight role hedge fund directors play is likely not substantial.").

70. *See* John Morley, *The Separation of Funds and Managers: A Theory of Investment Fund Structure and Regulation*, 123 YALE L.J. 1228, 1253 (2014) [hereinafter Morley, *Investment Fund*] (explaining the pattern of separating funds and managers for the purpose of limiting fund investors' control rights to obtain greater profits).

71. Shadab, *supra* note 62, at 155.

72. CHRISTOPHER BICKLEY, BERMUDA, BRITISH VIRGIN ISLANDS AND CAYMAN ISLANDS COMPANY LAW 3 (2013).

73. BRUNER, *supra* note 3, at 59.

enormous workforce."[74] As explained by Professor Edward Kleinbard, "[A] reinsurer can in fact have a commercial presence in the primary insurer's jurisdiction through the retention of an agent of independent status, thereby facilitating its reinsurance business in respect of risks in that jurisdiction."[75]

Through this process, U.S. insurance companies owned by Bermuda parent companies reduce the tax burden on their insurance activities without bringing the foreign parent companies into the U.S. net income tax system.[76] Thus, the parent entities can "minimize taxation on passive portfolio income such as interest and dividends, in part because of the low or zero tax-haven rate."[77] The result is the ability to provide coverage to U.S.-based risks operating in the United States while maintaining minimal physical presence in Bermuda.

C. The Prevailing Scholarly Account

Until fairly recently, the study of offshore financial havens in legal scholarship was almost completely monopolized by tax scholars.[78] The important body of work by these scholars demonstrates the vast impact that offshore jurisdictions can have in the global economy, ultimately affecting domestic policy. In a seminal work, for instance, Professor Reuven S. Avi-Yonah documented how tax havens allow "large amounts of capital to go untaxed, depriving both developed and developing countries of revenue and forcing them to rely on forms of taxation less progressive than the income tax."[79] Against this backdrop, Avi-Yonah proposed the "coordinated imposition of withholding taxes on international portfolio investment,"[80] as well as the taxing of multinational corporations "initially in the jurisdictions where their goods and services are consumed."[81] Recent works continue the

74. Kleinbard, *supra* note 59, at 235.

75. *Id.* at 236.

76. *Id.*

77. Allen & Morse, *supra* note 43, at 412.

78. For one of the earliest accounts, see Walter W. Bruno, *Tax Considerations in Selecting a Form of Foreign Business Organization*, 13 VAND. L. REV. 151 (1959). Outside of legal scholarship, offshore jurisdictions have long been studied both by economists and political scientists. *See* RONEN PALAN, THE OFFSHORE WORLD: SOVEREIGN MARKETS, VIRTUAL PLACES, AND NOMAD MILLIONAIRES 8–9 (2003) (reviewing existing accounts).

79. Reuven S. Avi-Yonah, *Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State*, 113 HARV. L. REV. 1575, 1575 (2000).

80. *Id.* at 1579.

81. *Id.* at 1575.

tradition of investigating unilateral and multilateral solutions to reduce tax evasion or avoidance.[82]

Within the past two decades, legal scholars have increasingly turned attention to the interrelationship between corporate law and tax law. According to Professors Mitchell Kane and Ed Rock, while offshore incorporation is "unabashedly all about tax reduction,"[83] it also concerns corporate law because it requires corporate entities to opt into "a different, possibly inferior, corporate law regime."[84] This view is now fairly well accepted. As Professor Victor Fleischer observes, "In some circumstances, managers will opt to minimize taxes by choosing a tax haven or tax-friendly jurisdiction, even if that jurisdiction is suboptimal from the standpoint of corporate law."[85]

Others are more optimistic about the virtues of offshore financial havens, relying on the corporate charter competition experience in the United States. In the United States, corporate law—the body of law governing relations between firm managers and shareholders—is largely a matter of state law.[86] Corporate entities can choose to be governed by a particular state's laws simply by electing to incorporate in that state.[87] Privately selected corporate governance rules are said to be welfare enhancing and encourage jurisdictional competition between

82. *See, e.g.*, Andrew Blair-Stanek, *Intellectual Property Law Solutions to Tax Avoidance*, 62 UCLA L. REV. 2, 4 (2015) (proposing a change in intellectual property law rather than tax law to combat tax avoidance); Samuel D. Brunson, *Repatriating Tax-Exempt Investments: Tax Havens, Blocker Corporations, and Unrelated Debt-Financed Income*, 106 NW. U. L. REV. 225, 229 (2012) (discussing a proposal to repeal the unrelated debt-financed income regime and instead police tax-exempt entities through reportable transaction rules); Mark P. Gergen, *How to Tax Capital*, 70 TAX L. REV. 1, 4–6 (2016) (suggesting a securities tax to reduce incentives for tax avoidance and evasion); Tracy A. Kaye, *Innovations in the War on Tax Evasion*, 2014 BYU L. REV. 363, 365 (offering global transparency and a multilateral information exchange platform as solutions for international offshore tax evasion).

83. Mitchell A. Kane & Edward B. Rock, *Corporate Taxation and International Charter Competition*, 106 MICH. L. REV. 1229, 1230 (2008).

84. *Id.*; *see also* Orsolya Kun, *Corporate Inversions: The Interplay of Tax, Corporate, and Economic Implications*, 29 DEL. J. CORP. L. 313, 314 (2004) ("The conversion of a U.S.-based multinational into a foreign corporation not only alters the tax exposure of the corporate group, but also changes the laws that govern intra-corporate relations.").

85. Fleischer, *supra* note 47, at 276.

86. Tung, *supra* note 28, at 3335.

87. *See* Edgar v. MITE Corp., 457 U.S. 624, 645 (1982) (holding that a state does not have an interest in regulating the internal affairs of foreign corporations and therefore can only regulate corporations incorporated within it). Historically, this was not the case. Prior to the late nineteenth century, corporate activities were primarily local, and corporate law was largely monopolized by the state where the corporation conducted its business. Capital mobility and the growth of interstate business effectively broke this monopoly, for "[l]egislatures could not afford to . . . driv[e] business out of state to the detriment of local interests." Tung, *supra* note 28, at 46.

states, resulting in innovative corporate governance rules.[88] This competition is enabled by private entities' ability to choose the corporate law of any state without establishing territorial presence in the chosen state.[89]

Scholars have extended this framework to the international jurisdictional competition context in areas tertiary to corporate law. Offshore financial havens purportedly provide an array of differentiated regulatory rules unavailable in the United States.[90] This typically includes the absence of accounting rules and disclosure rules—along with other "regulatory-compliance" costs—that an entity would be subjected to when operating in a purely domestic context.[91] Professor Jonathan Macey and attorney Anna Manasco Dionne, for instance, argue that competition introduced by offshore jurisdictions leads to financial and regulatory innovation.[92] Some proponents of interjurisdictional competition readily acknowledge the dark sides of offshore jurisdictions that manifest in the form of money laundering, financial fraud, terrorism financing, and tax evasion.[93] But they counsel

88. ROBERTA ROMANO, THE GENIUS OF AMERICAN CORPORATE LAW 1–5 (1993). *But see* Lucian Arye Bebchuk, *Federalism and the Corporation: The Desirable Limits on State Competition in Corporate Law*, 105 HARV. L. REV. 1435, 1437 (1992) (arguing that "the presence of managerial opportunism and externalities may lead states to adopt undesirable corporate law rules").

89. *See* Roberta Romano, *Law as a Product: Some Pieces of the Incorporation Puzzle*, 1 J.L. ECON. & ORG. 225, 225–27 (1985) (evaluating, from an empirical perspective, the relation between corporate migration patterns and the rationale for reincorporating and testing the level of states' responsiveness to private-sector preferences). Delaware is widely regarded as the winner of this competition. The advantages of Delaware corporate law are well known. In addition to the state legislature enacting cutting-edge corporate law, the Delaware Court of Chancery, staffed with renowned business law jurists, is famous for producing a refined body of corporate law that reduces uncertainty, ultimately benefiting both managers and shareholders. *See, e.g.*, Jill E. Fisch, *The Peculiar Role of the Delaware Courts in the Competition for Corporate Charters*, 68 U. CIN. L. REV. 1061, 1064 (2000) (attributing Delaware's success in attracting corporate charters to "the unique lawmaking function of the Delaware courts"); Ralph K. Winter, Jr., *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251 (1977); Lewis S. Black, Jr., *Why Corporations Choose Delaware*, DEL. DEP'T STATE 1–7 (2007), https://corpfiles.delaware.gov/whycorporations_web.pdf [https://perma.cc/NT2L-95WU].

90. *See* BRUNER, *supra* note 3, at 10–11.

91. Marco Becht, Colin Mayer & Hannes F. Wagner, *Where Do Firms Incorporate? Deregulation and the Cost of Entry*, 14 J. CORP. FIN. 241, 242 (2008); *see also* Magnuson, *supra* note 60, at 527 n.17 ("There is strong evidence that corporations choose their country of incorporation based on regulatory costs, including minimum capital requirements and setup costs.").

92. Jonathan Macey & Anna Manasco Dionne, *Offshore Finance and Onshore Markets: Racing to the Bottom, or Moving Toward Efficient?*, *in* OFFSHORE FINANCIAL CENTERS AND REGULATORY COMPETITION 8–10 (Andrew P. Morriss ed., 2010).

93. Andrew P. Morriss, *Introduction* to OFFSHORE FINANCIAL CENTERS AND REGULATORY COMPETITION, *supra* note 92, at 7.

against "the welfare-enhancing baby from being thrown out with the money-laundering bathwater."[94]

While insightful in many regards, these discussions are largely limited to the relative merits of firms opting out of "internal" corporate governance rules, along with regulatory compliance requirements.[95]

Largely overlooked are the collateral consequences that can be attributable to transnational corporate structuring on the back-end litigation side. Offshore corporate migration, as I show in the next Part, impacts the applicability of important federal regulatory statutes.

II. OFFSHORE FINANCIAL TRANSACTIONS AND THE EXTRATERRITORIAL REACH OF FEDERAL STATUTES

This Part uncovers how offshore corporate form can render predominantly "domestic" transactions outside the reach of federal regulatory statutes. It is worth noting up front that Congress typically enacts statutes that are "geoambiguous,"[96] giving only "cryptic clues as to their territorial scope."[97] It is for this reason that courts are often called upon to constructively assess the spatial reach of federal statutes, employing a canon of statutory construction known as the presumption

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94. *Id.*

95. Fleischer, *supra* note 47, at 230 (defining regulatory arbitrage as "the manipulation of the structure of a deal to take advantage of a gap between the economic substance of a transaction and its regulatory treatment"). The "regulatory arbitrage" literature, for instance, identifies the sorts of regulatory gamesmanship that involve legal planning techniques used to avoid taxes and other regulatory costs. *Id.* at 229. In a seminal work, Professor Ronald Gilson identified the important ways that private entities make decisions that take into consideration both regulatory costs and ordinary Coasian transactional costs. *See* Ronald J. Gilson, *Value Creation by Business Lawyers: Legal Skills and Asset Pricing*, 94 YALE L.J. 239, 255 (1984). In a more recent work, Victor Fleischer identified how regulatory arbitrage arises when private entities identify "gaps between legal form and economic substance." Fleischer, *supra* note 47, at 239. While some scholars have recognized the arbitrage opportunities that arise when multiple sovereigns are at play, the discussion is generally limited to costs internalized by corporate entities in the form of taxes and regulatory compliance costs. *Id.* at 246:

> The ability to choose one's planning of incorporation provides planning opportunities in the international context as well, of course. U.S. companies sometimes consider re-incorporating in a tax-haven jurisdiction. Incorporating abroad allows multinationals to pay U.S. tax only on U.S.-source income and offer other opportunities to shelter U.S. income through transfer pricing, income stripping, and other techniques.

(footnotes omitted).

96. Judge Jeffrey Meyer uses this term to describe federal statutes that "proscribe or regulate conduct but that remain silent about whether they apply to acts that occur outside of the United States." Jeffrey A. Meyer, *Dual Illegality and Geoambiguous Law: A New Rule for Extraterritorial Application of U.S. Law*, 95 MINN. L. REV. 110, 114 (2010).

97. Russell J. Weintraub, *The Extraterritorial Application of Antitrust and Securities Laws: An Inquiry into the Utility of A "Choice-of-Law" Approach*, 70 TEX. L. REV. 1799, 1800 (1992).

against extraterritoriality.[98] While this canon traces its roots to the early nineteenth century,[99] the Supreme Court substantially rewrote the canon recently through a series of blockbuster decisions. Labeled as "rigidly territorialist" by Professor Carlos Vázquez,[100] the Court's recent jurisprudence is described by Professor Hannah Buxbaum as a "continuing quest to identify categorical, territory-based rules" to govern "messy and often unpredictable patterns of transnational economic activity."[101] Section A provides an up-to-date primer on the Supreme Court's extraterritoriality jurisprudence. Section B illustrates how this line of jurisprudence has produced rulings in the lower courts delimiting federal statutes from applying to cases involving offshore commercial entities that are substantially connected to the United States.

*A. Extraterritoriality in the Post-*Morrison *World*

The Supreme Court's recent reshaping of its federal extraterritoriality jurisprudence started in 2010 with *Morrison v. National Australia Bank Ltd.*, involving three Australian investors who bought stock in Australia's largest bank listed on the Australian Securities Exchange.[102] The investors filed a suit in the U.S. District Court for the Southern District of New York under the antifraud provision of the Securities and Exchange Act of 1934("Exchange Act"), alleging that the bank manipulated the financial models of a U.S. mortgage-service company it purchased to make its business appear more valuable.[103] The critical issue was whether Congress intended the Exchange Act to cover this sort of action by a company whose stock was traded on foreign exchanges.[104]

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98. *See* Lea Brilmayer & Charles Norchi, *Federal Extraterritoriality and Fifth Amendment Due Process*, 105 HARV. L. REV. 1217, 1228–33 (1992). As the *Morrison* Court reminds us, the presumption is a "canon of construction . . . rather than a limit upon Congress's power to legislate." Morrison v. Nat'l Austl. Bank Ltd., 561 U.S. 247, 255 (2010).

99. *See* William S. Dodge, *Understanding the Presumption Against Extraterritoriality*, 16 BERKELEY J. INT'L L. 85, 85 (1998) (noting the Supreme Court's early use of the presumption to limit the reach of federal customs and piracy laws).

100. Vázquez, *supra* note 10, at 68.

101. Hannah L. Buxbaum, *The Scope and Limitations of the Presumption Against Extraterritoriality*, 110 AJIL UNBOUND 62, 62 (2016).

102. 561 U.S. at 249. One might argue that it started earlier, when Justice Scalia penned a scathing dissent in the seminal case of *Hartford Fire Insurance Co. v. California* concerning the extraterritorial reach of the Sherman Act. *See* 509 U.S. 764, 800 (1993) (Scalia, J., dissenting). The dissent arguably set the intellectual groundwork for *Morrison*. *See id.* at 800–02.

103. *Morrison*, 561 U.S. at 249–50.

104. *Id.* at 247–49.

Justice Antonin Scalia, writing for the majority, held that civil actions for securities fraud under Section 10(b) of the Exchange Act cannot be based on a sale that took place on a foreign exchange. This conclusion was based on the Court's observation that there is "no affirmative indication in the Exchange Act that §10(b) applies extraterritorially,"[105] coupled with the finding that the focus of the Exchange Act "is not upon the place where the deception originated, but upon purchases and sales of securities in the United States."[106]

While the outcome of the case was relatively unremarkable,[107] *Morrison* is remarkable for rewriting the presumption against extraterritoriality canon into a two-step test.[108] Under this test, a court must first ask "whether the statute gives a clear, affirmative indication that it applies extraterritorially."[109] If the statute does not, the court must then determine whether the case involves a permissible "domestic application of the statute by looking to the statute's 'focus.' "[110] Under the second step, "if the conduct relevant to the focus occurred in a foreign country, then the case involves an impermissible extraterritorial application regardless of any other conduct that occurred in U.S. territory."[111] Employing this test, the *Morrison* Court concluded that the Exchange Act did not apply to the facts at hand because it applies only to "transactions in securities listed on domestic exchanges, and domestic transactions in other securities."[112]

Since *Morrison*, the Supreme Court has invoked the presumption at a rapid pace by historical standards.[113] In *Kiobel v. Royal Dutch Petroleum*, decided in 2013, the Court invoked the

105. *Id.* at 265.

106. *Id.* at 266.

107. The case involved the fairly controversial topic of applying U.S. securities law to the so-called "f-cubed" transactions, where foreign shareholders purchase stock of a foreign issuer on a foreign exchange. The Court was merely affirming the U.S. Court of Appeals for the Second Circuit's holding, albeit overturning the lower court's long-standing doctrinal test. For an excellent discussion on "f-cubed" securities litigation, see Elizabeth Cosenza, *Paradise Lost: § 10(b) after* Morrison v. National Australia Bank, 11 CHI. J. INT'L L. 343, 344–45 (2010).

108. For a general critique of how the *Morrison* Court reshaped the presumption against extraterritoriality, see Lea Brilmayer, *The New Extraterritoriality:* Morrison v. National Australia Bank*, Legislative Supremacy, and the Presumption Against Extraterritorial Application of American Law*, 40 SW. L. REV. 655 (2011) [hereinafter Brilmayer, *New Extraterritoriality*].

109. *Morrison*, 561 U.S. at 248.

110. RJR Nabisco, Inc. v. European Cmty., 136 S. Ct. 2090, 2101 (2016) (quoting *Morrison*, 561 U.S. at 249).

111. *Id.*

112. *Morrison*, 561 U.S. at 249.

113. Maggie Gardner, RJR Nabisco *and the Runaway Canon*, 102 VA. L. REV. 134, 136 ("[T]he presumption against extraterritoriality fell into disuse after the 1940s. The Restatement (Third) of Foreign Relations Law, published in 1987, did not even bother to include it." (footnotes omitted)).

presumption to hold that alleged human rights violations committed by the Royal Dutch Shell Company in the Ogoni region of Nigeria could not be brought under the Alien Tort Statute because "all the relevant conduct" regarding those violations "took place outside the United States."[114] In its most recent opinion on the topic, *RJR Nabisco, Inc. v. European Community*, the Court extended the presumption to a suit involving U.S. corporations that allegedly directed a racketeering activity from the United States to launder drug-trafficking money through cigarette purchases, resulting in harm to European state-owned cigarette businesses.[115] The Court declined to apply the Racketeer Influenced and Corrupt Organizations Act to the facts of the case, reasoning that private litigants bringing a RICO claim must establish "domestic injury" and not "domestic conduct."[116]

The Supreme Court's new extraterritoriality jurisprudence has dramatically impacted plaintiffs attempting to bring private suits with a transnational fact pattern.[117] Importantly, the first step virtually prohibits a federal judge from finding congressional intent to apply statutes outside of the U.S. territory absent express instructions—something that rarely exists in the world of federal statutes.[118] While the second step leaves the door open, an attempt to decipher the "focus" of a particular statute frequently serves as a screening mechanism eliminating the type of connecting factors that could overcome the

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114. 569 U.S. 108, 124 (2013). For an introduction to the scope of the Alien Tort Statute, see William J. Moon, *The Original Meaning of the Law of Nations*, 56 VA. J. INT'L L. 51, 57–61 (2016).

115. 136 S. Ct. at 2098. Importantly, the Supreme Court held that the provision conferring the plaintiff's right of action could not overcome the presumption against extraterritoriality, while holding that the substantive provision of RICO applied extraterritorially. Carlos M. Vázquez & Ingrid Wuerth, *Introduction to Agora: Reflections on* RJR Nabisco v. European Community, 110 AJIL UNBOUND 37, 37 (2016).

116. *RJR Nabisco*, 136 S. Ct. at 2111.

117. *See* Bookman, *supra* note 10, at 1097–99 (discussing the cases that comprise the Court's extraterritoriality jurisprudence); Patrick J. Borchers, *How "International" Should A Third Conflicts Restatement Be in Tort and Contract?*, 27 DUKE J. COMP. & INT'L L. 461, 461 (2017) (describing the Exchange Act and RICO as being construed by the Supreme Court "in implausibly narrow fashions to limit their impact abroad"); Katherine Florey, *State Law, U.S. Power, Foreign Disputes: Understanding the Extraterritorial Effects of State Law in the Wake of* Morrison v. National Australia Bank, 92 B.U. L. REV. 535, 542 (2012) (describing the *Morrison* opinion as adhering to an old-fashioned and formalistic view of territory).

118. Brilmayer, *New Extraterritoriality*, *supra* note 108, at 655 (assessing that the first step instructs "lower courts to turn a deaf ear to indications of congressional intent any subtler than the proverbial meat axe"). This much is clear from the Supreme Court's blunt admission in *Nabisco* that the new extraterritoriality test does not actually concern what Congress would want but whether Congress explicitly gave indication on a statute's geographic scope. *See RJR Nabisco*, 136 S. Ct. at 2100 ("The question is not whether we think 'Congress would have wanted' a statute to apply to foreign conduct 'if it had thought of the situation before the court,' but whether Congress has affirmatively and unmistakably instructed that the statute will do so." (quoting Morrison v. Nat'l Austl. Bank Ltd., 561 U.S. 247, 261 (2010))).

presumption against extraterritoriality. Thus, for instance, in *Nabisco*, the overwhelming facts connecting the case to the United States—"[a]ll defendants are U.S. corporations, headquartered in the United States, charged with a pattern of racketeering activity directed and managed from the United States, involving conduct occurring in the United States"[119]—were insufficient to trigger the RICO statute because the "focus" of the statute was determined by the majority of the Justices to be the regulation of "domestic injury" and not "domestic conduct."[120] And in *Morrison*, even though the relevant fraudulent conduct took place in the United States, this was insufficient because congressional focus was not to punish deceptive conduct alone but "deceptive conduct 'in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered.' "[121]

Below, I illustrate the impact of this line of jurisprudence on the offshore context by examining recent cases involving the extraterritorial application of the U.S. Bankruptcy Code, the RICO Act, and the Exchange Act.

B. Offshore Application

1. "Domestic" Fraudulent Transfers Under the U.S. Bankruptcy Code

Securities Investor Protection Corp. v. Bernard L. Madoff Investment Securities LLC is one of the dozens of high-stakes bankruptcy litigations stemming from the infamous Madoff Ponzi scheme.[122] Madoff, a former chairman of the NASDAQ, pleaded guilty to eleven counts of federal crimes in 2009 after running a $50 billion Ponzi scheme through his fund, Bernard L. Madoff Investment Securities ("BLMIS").[123] Madoff did not actually engage in any securities transactions on behalf of his customers, but "sent them bogus customer statements and trade confirmations showing fictitious trading activity and profits."[124] Investors in this scheme included both

119. 136 S. Ct. at 2114 (Ginsburg, J., dissenting).

120. *Id.* at 2111 (majority opinion).

121. *Morrison*, 561 U.S. at 266 (quoting 15 U.S.C. § 78j(b) (2012)).

122. 513 B.R. 222, 225 (Bankr. S.D.N.Y. 2014).

123. Amir Efrati, Tom Lauricella & Dionne Searcey, *Top Broker Accused of $50 Billion Fraud*, WALL ST. J. (Dec. 12, 2008), https://www.wsj.com/articles/SB122903010173099377 [https://perma.cc/7HTW-9X4F]; Robert Frank, Amir Efrati, Aaron Lucchetti & Chad Bray, *Madoff Jailed After Admitting Epic Scam*, WALL ST. J. (Mar. 13, 2009), https://www.wsj.com/articles/SB123685693449906551 [https://perma.cc/Y9Y3-BFB9].

124. Sec. Inv'r Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC, No. AP 08-01789 (SMB), 2016 WL 6900689, at *2 (Bankr. S.D.N.Y. Nov. 22, 2016).

domestic and foreign investors that invested in Madoff's fund through feeder funds formed in the British Virgin Islands and the Cayman Islands.[125] Prior to the collapse of Madoff's fund, the feeder funds withdrew proceeds from BLMIS's commingled bank account that included other customers' investments along with "fake" profits and distributed them to "their customers, managers, and the like."[126] Following the commencement of BLMIS's liquidation, the court-appointed trustee sued the feeder funds, as well as the investors who invested in BLMIS through the feeder funds, in order to recover the transferred funds.

The relevant laws here are fraudulent transfer laws,[127] codified in the U.S. Bankruptcy Code.[128] The Code allows the trustee to recover—or to use the statute's term, "avoid"—fraudulent transfers in order to spread the loss among defrauded creditors. In a typical bankruptcy proceeding, a trustee is appointed to oversee a fair distribution in accordance with the priority rules.[129] The defendants in *Security Investor Protection Corp.*, who were recipients of the proceeds from the feeder funds, moved to dismiss, arguing that the Bankruptcy Code "does not apply extraterritorially and therefore does not reach subsequent transfers made abroad by one foreign entity to another."[130]

In determining whether the transfer occurred "extraterritorially," Judge Jed Rakoff, applying *Morrison*, assessed that

125. *Sec. Inv'r Prot. Corp.*, 513 B.R. at 225.

126. *Id.*

127. Fraudulent transfer laws trace their origin to legislation passed in 1571 in England making "illegal and void any transfer made for the purpose of hindering, delaying, or defrauding creditors." Douglas G. Baird & Thomas H. Jackson, *Fraudulent Conveyance Law and Its Proper Domain*, 38 VAND. L. REV. 829, 829 (1985). This statute, commonly known as the Statute of 13 Elizabeth, was designed to curb what was thought to be a widespread practice of debtors avoiding creditors through entering and living in sanctuaries unreachable by the King's writ—including the interior of a church and certain precincts defined by custom or royal grant. *Id.*

128. Section 548(a)(1) permits avoidance of fraudulent transfers that were executed "with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted." 11 U.S.C. § 548(a)(1)(a) (2012). Section 550(a) permits the trustee to recover the transfer avoided under Section 548. 11 U.S.C. § 550(a) (2012).

129. The particular case at hand involved the trustee proceeding pursuant to the Securities Investor Protection Act of 1970 ("SIPA"). *See* 15 U.S.C. § 78fff(b) (2012). SIPA "merely engrafts special features onto the familiar framework of a liquidation proceeding under Chapter 7 of the Bankruptcy Code . . . to address the concerns peculiar to the orderly liquidation of a brokerage." Picard v. Fairfield Greenwich Ltd., 762 F.3d 199, 212 (2d Cir. 2014). An ordinary clawback action involving a Ponzi scheme is not particularly difficult given that transfers in connection with a Ponzi scheme are presumed to be fraudulent transfers. *See, e.g.*, Drenis v. Haligiannis, 452 F. Supp. 2d 418, 429 (S.D.N.Y. 2006) ("[T]he defrauding defendants [were] alleged elsewhere in the complaint to be perpetrators of a Ponzi scheme. In such cases, courts have found that the debtor's intent to hinder, delay or defraud is presumed to be established.").

130. *Sec. Inv'r Prot. Corp.*, 513 B.R. at 226.

the "focus" of the relevant sections of the Bankruptcy Code was on the "property transferred [and] the fact of its transfer, not the debtor."[131] Under this analysis, the transfer at issue was extraterritorial and thus outside the reach of the U.S. Bankruptcy Code because "the relevant transfers and transferees are predominantly foreign: foreign feeder funds transferring assets abroad to their foreign customers and other foreign transferees."[132]

Importantly, Judge Rakoff's analysis elevates the domicile of the feeder funds—essentially glorified paperwork[133]—as the central factual input of the extraterritoriality analysis.[134] This is apparent as the court's analysis necessarily downplays the importance of the fact that "the chain of transfers originated with Madoff Securities in New York."[135] Judge Rakoff's "focus" also glances over the fact that many of the feeder funds were controlled and operated from the funds' related entities located in the United States. For instance, one major feeder fund, Fairfield Cayman, maintained its principal place of business in New York, operated out of a parent entity's New York headquarters, and "never had employees or an office in the Cayman Islands."[136]

The decision's narrow (and peculiar) construction of the Bankruptcy Code's geographic reach is perhaps best illustrated in an example provided by Professor Ed Morrison in his critique of the decision: "If Madoff wires funds from his New York account to London-based investors, the Trustee can bring suit against those investors. But if Madoff carries a briefcase full of cash to London and then hands the

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131. *Id.* at 227.

132. *Id.* Rather than ruling on each claim before him, Judge Rakoff remanded the cases for the bankruptcy judge to decide each of the trustee's avoidance claims within the parameters he set forth. *Id.* at 232.

133. *See* Moon, *Tax Havens*, *supra* note 58, at 1095 ("[L]egal formalities may permit a juridical center of operations appear to be in a particular jurisdiction using little more than glorified paperwork.").

134. It is important to remember that feeder funds themselves exist principally as a tax avoidance tool. Recall that foreign investors typically invest in U.S.-managed funds not directly, but through feeder funds formed in offshore jurisdictions for tax purposes. *See supra* Section I.B.1. Absent this corporate structure, a foreign creditor withdrawing from a domestic fund would likely fall within the reach of U.S. bankruptcy law. *See* Edward R. Morrison, *Extraterritorial Avoidance Actions: Lessons from* Madoff, 9 BROOK. J. CORP. FIN. & COM. L. 268, 283 (2014) [hereinafter Morrison, *Extraterritorial Avoidance*] ("The trustee's (or debtor's) authority to recover the fraudulent transfer does not disappear because the initial transferee is located abroad."). Arguably these foreign customers would have a "good faith" defense on grounds that they could not expect their funds to be invested in a U.S.-based entity. *See id.* at 282; *see also* 11 U.S.C. §§ 548(c), 550(b) (2012) (offering defenses to a transferee "that takes for value" and "in good faith"). But this is a separate question from the geographical reach of U.S. bankruptcy law.

135. *Sec. Inv'r Prot. Corp.*, 513 B.R. at 228.

136. Sec. Inv'r Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC, No. AP 08-01789 (SMB), 2016 WL 6900689, at *31 (Bankr. S.D.N.Y. Nov. 22, 2016).

cash to his investors, the Trustee apparently cannot bring suit because the cash handoff was a 'purely foreign transfer.' "[137]

2. "Domestic" Racketeering Under the RICO Act

The impact of the Supreme Court's recent decision in *Nabisco* has already made shockwaves of confusion in the lower courts adjudicating civil RICO cases.[138] The recent case of *Absolute Activist Value Master Fund Ltd. v. Devine* illustrates how courts have imputed the location of the injury—the "focus" of the RICO statute under *Nabisco*—based on the domicile of corporate entities.[139]

In *Devine*, eight hedge funds—all formed under the laws of the Cayman Islands—sued Susan Devine, a long-term resident of Naples, Florida. Devine was a former wife of Florian Homm, a chief investment officer and investment manager for mutual funds who allegedly caused more than $200 million in losses by inflating the prices of virtually worthless U.S. microcap companies.[140] After learning that the scheme was at risk of being publicly disclosed, Devine allegedly formed a criminal enterprise with Homm to conceal and transfer proceeds from the scheme. This elaborate scheme encompassed:

> [A] strategic divorce; the creation of a network of entities in far-flung locales, including known bank secrecy havens; the use of accounts for which the Homm children were the nominal beneficiaries to shield assets; the fabrication of records; the use of aliases; difficult-to-trace transactions in cash, gold, and fine art; and innumerable bank transfers.[141]

While the complaint alleged that the money-laundering scheme was "directed, controlled, and participated in" by Devine in Florida,[142] the court dismissed the RICO claim, reasoning that any alleged economic injuries were suffered by the plaintiffs in "the only location where the plaintiffs were located—in the Cayman Islands."[143] The court reached this decision because the "focus" of RICO, under the Supreme

137. Morrison, *Extraterritorial Avoidance*, *supra* note 134, at 270 (quoting *Sec. Inv'r Prot. Corp.*, 513 B.R. at 232).

138. This much was predicted by Justice Alito's majority opinion in *Nabisco*. As the *Nabisco* Court explains, the application of the rule that a civil RICO plaintiff "allege and prove a domestic injury to business or property . . . will not always be self-evident, as disputes may arise as to whether a particular alleged injury is 'foreign' or 'domestic.' " RJR Nabisco, Inc. v. European Cmty., 136 S. Ct. 2090, 2111 (2016).

139. Absolute Activist Value Master Fund Ltd. v. Devine, 233 F. Supp. 3d 1297, 1326 (M.D. Fla. 2017).

140. Complaint ¶¶ 1–2, 12, *Devine*, 233 F. Supp. 3d 1297 (No. 15-00328).

141. *Id.* ¶ 3.

142. *Id.*

143. *Devine*, 233 F. Supp. 3d at 1326.

Court's *Nabisco* decision, is the "geographic location of the injury to plaintiffs, not the location of a defendant's wrongful acts."[144]

It is important to note here that the court's analysis neglects to consider the source of the funds: as alleged in the complaint, the fund operated by Homm invested "on behalf of hundreds of investors in the United States and around the world."[145] Moreover, plaintiffs had alleged that Devine directed the scheme, transferring wrongfully obtained proceeds "while residing in Naples, Florida."[146] Whether these facts constitute a sufficient nexus to the United States and whether the alleged actions amounted to a RICO violation are separate questions. What stands out is the formalistic line drawn by the court based on the domicile of the fund, turning a blind eye to the significant U.S. connection to the case.

3. "Domestic" Securities Under the Exchange Act

In *Morrison*, the Supreme Court limited application of Section 10(b) of the Exchange Act to either (i) "the purchase or sale of a security listed on an American stock exchange," or (ii) "the purchase or sale of any other security in the United States."[147] The *Morrison* Court provided little guidance on what constitutes a domestic purchase or sale for a security not listed on an exchange like the NASDAQ or the New York Stock Exchange.[148] *Morrison* simply held that the provision applies to nonexchange-based transactions when "the purchase or sale is made in the United States."[149]

Cascade Fund, LLLP v. Absolute Capital Management illustrates how the offshore fund structure aids those engaging in securities transactions with fairly substantial connections to the United States to opt out of U.S. securities law. In *Cascade Fund*, a Colorado-based company invested in Absolute Capital Management ("ACM"), a fund organized and registered under the laws of the Cayman Islands. ACM contended that *Morrison* precluded the application of Section 10(b) claims because "the funds are not traded on any domestic stock exchange and because the transaction . . . occurred in the Cayman Islands, not the United States."[150] Cascade alleged four facts to

144. *Id.*

145. Complaint, *supra* note 140, ¶ 9.

146. *Id.* ¶ 146.

147. Morrison v. Nat'l Austl. Bank Ltd., 561 U.S. 247, 273 (2010).

148. Absolute Activist Value Master Fund Ltd. v. Ficeto, 677 F.3d 60, 69 (2d Cir. 2012).

149. *Morrison*, 561 U.S. at 269–70.

150. Cascade Fund, LLLP v. Absolute Capital Mgmt. Holdings Ltd., No. 08-CV-01381-MSK-CBS, 2011 WL 1211511, at *5 (D. Colo. Mar. 31, 2011).

establish that the transaction was plausibly domestic in nature: "(i) the Offering Memoranda and other investment materials were disseminated to Cascade in the United States; (ii) . . . ACM executives traveled to the United States to solicit American investors; (iii) Cascade made its decision to invest while in the United States; and (iv) the money for the purchase was wired to a bank in New York."[151]

The court dismissed the case at the motion to dismiss stage, reading *Morrison* as making "clear that the test of §10(b)'s reach is not dependent on the fact that domestic investors in foreign securities were harmed by fraud."[152] Interestingly, the court focused on the language of the Subscription Agreement (the contract at issue), which made it "clear that simply sending money to New York was not sufficient to complete the transaction."[153] Thus, the court assessed that the transaction could not have occurred in the United States because "the transaction was not completed until ACM finally accepted an application—presumably in its Cayman Islands offices."[154]

Cascade Fund is indicative of post-*Morrison* jurisprudence that has elevated the domicile of corporate entities as an important factual input for determining the extraterritorial reach of federal statutes.[155] More specifically, courts often refuse to apply federal securities law to transactions completed through offshore entities because they view these transactions as taking place outside the territory of the United States.[156] This is a particularly ill-advised method for determining

151. *Id.* at *7.

152. *Id.* at *5.

153. *Id.* at *7.

154. *Id.*

155. Consider the case of *In re Banco Santander Securities-Optimal Litigation*, 732 F. Supp. 2d 1305, 1340–41 (S.D. Fla. 2010), brought by investors in Bahamian feeder funds that were established to invest in Madoff's assets in New York. Observing that "[t]he funds at issue in this case are registered under the laws of the Bahamas," the court dismissed the claim, reasoning that applying U.S. securities fraud law to the case would amount to interfering "with foreign securities regulation that *Morrison* sought to avoid." *Id.* at 1317. In other cases, U.S. securities law claims are dismissed because an offshore jurisdiction's regulatory approval is the condition precedent of a contract completed through an offshore commercial entity. For instance, in *Adderley v. Dingman*, a U.S. citizen's securities fraud claim against a Bahamian corporation was dismissed, notwithstanding the fact that the CEO of the Bahamian corporation made a number of misrepresentations over a series of lunch meetings in Manhattan. *See* No. 15 Civ. 9935, 2017 U.S. Dist. LEXIS 54610, at **6–9 (S.D.N.Y. Mar. 29, 2017). The court reasoned that approval of the Bahamian regulator was needed to complete a transaction through a Bahamian corporation, essentially removing the transaction from the reach of U.S. securities law. *Id.* at *26.

156. *See, e.g.*, MVP Asset Mgmt. (USA) LLC v. Vestbirk, No. 2:10-CV-02483-GEB, 2013 WL 1726359, at *7 (E.D. Cal. Mar. 22, 2013) (dismissing a Section 10(b) claim because plaintiffs failed to identify the location of defendants when the parties entered into the "valid, binding and enforceable agreement"); *In re* Merkin, 817 F. Supp. 2d 346, 357 n.10 (S.D.N.Y. 2011) (dismissing a Section 10(b) claim against a Cayman Islands hedge fund because there was no allegation any

whether U.S. securities laws ought to govern a particular transaction because "[m]arkets are moving to a point where the 'site' of a trade is happenstance," such that there is little "connection between the place of trade and the injury."[157] To the extent that securities laws are designed in part to deter local injury, limiting the reach of these laws based on the place of trade makes little sense where the place of injury does not align with the place of trade.

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To recap, offshore financial havens have become virtual spaces where the juridical residence of corporate entities plays a significant role in delimiting the application of federal statutes. Perhaps more importantly, the "focus" test developed by the *Morrison* Court invites endless permutations of loopholes that allow commercial entities to avoid the application of federal regulatory statutes. In the securities regulation context, the new jurisprudence allows private entities, with essentially a well-drafted contract and incorporation paperwork, to opt out of Section 10(b) even while soliciting U.S. investors within U.S. territory.[158] And consider the implications of Judge Rakoff's *Madoff* ruling. As Professor Ed Morrison explains, under the *Madoff* decision, "[a] transfer can be immunized from recovery simply by interposing a foreign-based transferee between the debtor and the ultimate foreign beneficiary."[159] This is not mere academic speculation. As Judge Shira Scheindlin forewarned in a pre-*Morrison* case: "[A] creditor—be it foreign or domestic—who wished to characterize a transfer as extraterritorial could simply arrange to have the transfer made overseas, a result made all too easy in the age of the multinational company and information superhighway."[160] The next Part takes a step

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shares at issue were traded on a domestic exchange or purchased in a domestic transaction); Basis Yield Alpha Fund (Master) v. Goldman Sachs Grp., Inc., 798 F. Supp. 2d 533, 537 (S.D.N.Y. 2011) (dismissing Section 10(b) claims related to transactions by a Cayman Islands entity when plaintiff "fail[ed] to provide sufficient facts that allow the Court to draw the reasonable inference that the purchase or sale was made in the United States").

157. Comments by Forty-Two Law Professors, Comment Letter on Release No. 34-63174, Study on Extraterritorial Private Rights of Action, at 7 (Feb. 18, 2011), http://www.sec.gov/comments/4-617/4617-28.pdf [https://perma.cc/262V-T96C].

158. This should give some reason for concern. As Hannah Buxbaum explains, the territorialist jurisprudence in the securities regulation context enables transactions that are "not only manipulable but can be non-transparent to the other party." Buxbaum, *Remedies*, *supra* note 12, at 173.

159. Morrison, *Extraterritorial Avoidance*, *supra* note 134, at 269–70.

160. *In re* Maxwell Commc'n Corp., 186 B.R. 807, 816 (S.D.N.Y. 1995), *aff'd*, 93 F.3d 1036 (2d Cir. 1996).

back and interrogates the purported reasons that underlie this line of jurisprudence.

III. CORPORATE DOMICILE AND TERRITORIAL SOVEREIGNTY

This Part assesses whether the foreign status of offshore commercial entities alone should convert otherwise domestic transactions into "extraterritorial" transactions outside the reach of federal statutes. Section A introduces readers to the traditional and modern conceptions of territorial sovereignty that underlie the federal extraterritoriality jurisprudence. Section B shows the implausibility of a jurisdiction asserting an authority to regulate conduct based on corporate domicile alone. While a good argument can be made that federal and state judges ought to defer to foreign law when it comes to corporate governance rules over the "internal affairs" of business entities formed in foreign nations, foreign incorporation alone should not cause an authority to regulate conduct arising out of or related to that entity. Viewed in this light, the recent extraterritoriality jurisprudence discussed in Part II represents domestic regulatory laws ceding to privately curated juridical rules under the doctrinal framework of judicial modesty and international comity. Section C raises several important policy considerations challenging the wisdom of jurisdictional competition and regulatory arbitrage facilitated by the Supreme Court's recent extraterritoriality jurisprudence. Section D offers sensible doctrinal solutions to regulate modern financial transactions that refuse to be captured in traditional notions of space and time.

A. Territorial Sovereignty Under Domestic and International Law

The presumption against extraterritoriality is a method of statutory interpretation deployed to accomplish two goals. This includes, first, effectuating Congress's general practice of legislating with "domestic concerns in mind,"[161] and second, avoiding "international discord that can result when U.S. law is applied to conduct in foreign countries."[162] While the U.S. Supreme Court described this "international discord" rationale as the "most notabl[e]"[163] reason for employing the presumption in *Nabisco*, the

161. RJR Nabisco, Inc. v. European Cmty., 136 S. Ct. 2090, 2100 (2016) (quoting Smith v. United States, 507 U.S. 197, 204 n.5 (1993)) (internal quotation marks omitted).

162. *Id.*

163. *Id.*

Court has not stayed consistent on this point. In *Morrison*, for instance, the Court stated that the presumption applies "regardless of whether there is a risk of conflict between the American statute and a foreign law,"[164] leading an early commentator to conclude that the international comity rationale embodied in the presumption was dead.[165] This did not turn out to be the case, as *Nabisco* in 2016 reaffirmed the international discord rationale as central to the presumption.[166]

Regardless of whether comity concerns are already folded into the presumption, it is worth reviewing the theoretical building blocks underlying any given nation state's authority to legislate in the first place. This is important, because where there is no possible foreign sovereign interest attributable to a particular transnational case, the rationale underlying the presumption (and the related concept of comity) becomes moot, resulting in nonapplication of federal law in a vast range of transnational cases where application would advance U.S. interests without clashing with foreign law.[167] Moreover, a case substantially connected to the United States would presumably involve "domestic concerns" that federal statutes are designed for.[168] Below, I review the concept of territorial sovereignty as it relates to a sovereign's authority to legislate and apply the principle to the case of offshore financial transactions.

1. Traditional Conceptions of Territorial Sovereignty

Territorial sovereignty is a concept that traces its intellectual origin to the historical legacy of the Westphalian sovereign state.[169] Nation states, in the aftermath of the Peace of Westphalia in 1648, were principally defined by territorial borders under the premise that the

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164. Morrison v. Nat'l Austl. Bank Ltd., 561 U.S. 247, 255 (2010).

165. *See, e.g.*, William S. Dodge, Morrison*'s Effects Test*, 40 SW. L. REV. 687, 689 (2012) [hereinafter Dodge, *Effects Test*] ("The first justification became difficult to maintain after the Court applied the presumption in situations presenting no risk of conflict with foreign law, and *Morrison* officially jettisoned it. Thus, the presumption now rests solely 'on the perception that Congress ordinarily legislates with respect to domestic, not foreign matters.' " (quoting *Morrison*, 561 U.S. at 255)).

166. *RJR Nabisco*, 136 S. Ct. at 2101.

167. Larry Kramer, *Vestiges of Beale: Extraterritorial Application of American Law*, 1991 SUP. CT. REV. 179, 215–17.

168. *See, e.g.*, Foley Bros. v. Filardo, 336 U.S. 281, 285 (1949).

169. Kal Raustiala, *The Geography of Justice*, 73 FORDHAM L. REV. 2501, 2508 (2005) ("The importance of place to legal rules and protections—the belief that law derives from land—has deep historical roots. Defining law in spatial terms accords with the traditional conception of the Westphalian sovereign state.").

world was divided into separate, equal, and independent states.[170] Influenced by the work of seventeenth-century Dutch jurist Ulrich Huber,[171] Justice Joseph Story is credited with transplanting this concept of territoriality to the U.S. legal discourse. In a celebrated treatise, *Commentaries on the Conflict of Laws*, published in 1834, Story explained that "every nation possesses an exclusive sovereignty and jurisdiction within its own territory."[172]

Because statehood was articulated in terms of a particular parcel of territory, "jurisdiction, in the sense of a sovereign's authority over persons or events, was also referenced to their location within that territory."[173] This historic legacy of the Westphalian state informed the U.S. Supreme Court's early extraterritoriality jurisprudence in federal customs and piracy law disputes in the early nineteenth century.[174] The presumption against extraterritoriality made its modern appearance as a canon of statutory interpretation in the early twentieth century.[175] In the seminal case of *American Banana Co. v. United Fruit Co.*, Justice Oliver Wendell Holmes famously noted that "all legislation is prima facie territorial," declining to extend the reach of the Sherman Act to activities in Colombia.[176]

Strict territorialism was the principle that also influenced the doctrinal development of a wide body of law at the time, including

170. It is for this reason that statehood is often conceptualized as an entity monopolizing the use of legitimate authority in a particular territory. Territorial sovereignty, in both law and political science, is generally understood as a nation exercising principal means of authority within a given territory. *See* Jack L. Goldsmith, *The Internet and the Abiding Significance of Territorial Sovereignty*, 5 IND. J. GLOBAL LEGAL STUD. 475, 476 (1998).

171. Geoffrey C. Hazard, Jr., *A General Theory of State-Court Jurisdiction*, 1965 SUP. CT. REV. 241, 259 ("Story borrowed from Huber the idea of the exclusivity of sovereign authority.").

172. JOSEPH STORY, COMMENTARIES ON THE CONFLICT OF LAWS § 18 (Edmund H. Bennett ed., Little, Brown & Co. 7th ed. 1872) (1834).

173. *See* Hannah L. Buxbaum, *Territory, Territoriality, and the Resolution of Jurisdictional Conflict*, 57 AM. J. COMP. L. 631, 632 (2009) [hereinafter Buxbaum, *Territoriality*].

174. *See, e.g.*, The Apollon, 22 U.S. (1 Wheat.) 362, 370 (1824); United States v. Palmer, 16 U.S. (3 Wheat) 610, 630–32 (1818).

175. *See* Dodge, *Effects Test*, *supra* note 165, at 687. Of course, the presumption against extraterritoriality traces its doctrinal roots to the *Charming Betsy* canon, which teaches that statutes should be construed not to violate international law. *See* David L. Sloss, Michael D. Ramsey & William S. Dodge, *International Law in the Supreme Court to 1860*, *in* INTERNATIONAL LAW IN THE SUPREME COURT: CONTINUITY AND CHANGE 7, 37–38 (David L. Sloss, Michael D. Ramsey & William S. Dodge eds., 2011).

176. 213 U.S. 347, 356–57 (1909) (quoting *Ex Parte* Blain (1879) 12 Ch D 522 at 528 (Eng.)), *overruled as recognized in* W.S. Kirkpatrick & Co. v. Envtl. Tectonics Corp., Int'l, 493 U.S. 400, 407–08 (1990). The opinion reflects strict territorialism that enjoyed its heyday around the time. *See id.* at 356 ("[T]he general and almost universal rule is that the character of an act as lawful or unlawful must be determined wholly by the law of the country where the act is done.").

judicial jurisdiction and conflict of laws.[177] Judicial jurisdiction, or the sovereign's authority over persons or events, for instance, could be determined by ascertaining the location of the persons or events within that territory.[178] The familiar case of *Pennoyer v. Neff* held that territorial presence was a precondition for a court to exercise personal jurisdiction.[179] Professor Joseph Beale has had the most significant and enduring impact as the intellectual leader of the traditional "territorial" thought in conflict of laws. To Beale, law had to "apply to everything and must exclusively apply to everything within the boundary of its jurisdiction."[180] This is the famous "vested" rights theory, prominently codified in the Restatement (First) of Conflict of Laws. For instance, the Restatement primarily determined applicable tort law based on "where the last event necessary to make an actor liable for an alleged tort [took] place,"[181] while determining applicable contract law principally based on where the contract was accepted.[182]

2. Modern Conceptions of Territorial Sovereignty

A comprehensive theory in line with strict territorialism began to crack in the early twentieth century with the acceleration of cross-border activities that forced territorially tethered laws to produce results that were "undeniably arbitrary and verged on the bizarre."[183] The rise of legal realism, in particular, exposed the formalistic account as intellectually rotten and practically infeasible, setting up an intellectual vacuum for modern conceptions of territorial sovereignty to take shape.[184]

Against this backdrop, strictly territorial rules were gradually relaxed over the course of the twentieth century in favor of more flexible

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177. Allgeyer v. Louisiana, 165 U.S. 578, 588 (1897) (rejecting application of Louisiana law to a contract "made and to be performed within the State of New York").

178. Buxbaum, *Territoriality*, *supra* note 173, at 632 ("Statehood is articulated by reference to a particular geographic territory; jurisdiction, in the sense of a sovereign's authority over persons or events, by reference to their location within that territory.").

179. 95 U.S. 714, 720 (1877).

180. 1 JOSEPH BEALE, A TREATISE ON THE CONFLICT OF LAWS § 4.12 (1935); *see also* Kermit Roosevelt III, *The Myth of Choice of Law: Rethinking Conflicts*, 97 MICH. L. REV. 2448, 2455 (1999) ("Law, for Beale, was fundamentally territorial, supreme within a jurisdiction but generally powerless outside it.").

181. RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 377 (AM. LAW INST. 1934).

182. KERMIT ROOSEVELT, CONFLICT OF LAWS 10 (2d ed. 2015).

183. Roosevelt, *supra* note 180, at 2458.

184. Lea Brilmayer, *Rights, Fairness, and Choice of Law*, 98 YALE L.J. 1277, 1282–84 (1989).

conceptions of territoriality.[185] Various modern strands of territorial sovereignty rejected categorical rules derived solely from raw territorial contact and embraced a more flexible approach taking into account the location of the harm.[186]

Strict territoriality's demise in judicial jurisdiction is a story familiar even to scholars with no particular love for personal jurisdiction. The Supreme Court in 1945 relaxed the personal jurisdiction standard to a flexible "fair play and substantial justice" test in *International Shoe v. Washington*,[187] laying the theoretical groundwork for *Shaffer v. Heitner* to formally overturn *Pennoyer v. Neff*.[188]

A revolution swept across the field of conflict of laws as well, accommodating a theory of "state interest" that could exist outside of strict territorial connection between the state and the individual. Moving away from the First Restatement's teachings, "modern" conflicts scholars embraced "a flexible, case-by-case approach to choice-of-law problems that focused on state interests."[189]

Various strands of federal extraterritoriality doctrines developed in the middle of the twentieth century similarly repudiated raw territorial contact as the sole basis to determine the reach of law. The movement had already started in 1927, when the Supreme Court distinguished *United States v. Sisal Sales Corp.* from *American Banana* despite nearly identical facts.[190] A full-scale abandonment of strict territorialism can be traced to the U.S. Court of Appeals for the Second Circuit's 1945 decision in *Alcoa*, where Judge Learned Hand dispensed with the *American Banana* test and, in its place, articulated an "effects" test: conducts occurring outside the territory of the United States were prohibited by the Sherman Act "if they were intended to affect imports

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185. Buxbaum, *Territoriality*, *supra* note 173, at 636; Dodge, *International Comity*, *supra* note 25.

186. William S. Dodge, *Extraterritoriality and Conflict-of-Laws Theory: An Argument for Judicial Unilateralism*, 39 HARV. INT'L L.J. 101, 124–27 (1998).

187. Int'l Shoe Co. v. Washington, 326 U.S. 310, 316 (1945) (holding that a state court can exercise personal jurisdiction over a defendant if he has "certain minimum contacts with it such that the maintenance of the suit does not offend traditional notions of fair play and substantial justice"). For a commentary reflecting on the impact of *International Shoe*, see Linda J. Silberman, *"Two Cheers" for* International Shoe *(and None for* Asahi*): An Essay on the Fiftieth Anniversary of* International Shoe, 28 U.C. DAVIS L. REV. 755, 758 (1995).

188. Shaffer v. Heitner, 433 U.S. 186, 206 (1977); *see also* Linda J. Silberman, Shaffer v. Heitner*: The End of an Era*, 53 N.Y.U. L. REV. 33, 62–79 (1978) (explaining the doctrinal shift leading up to *Shaffer*).

189. Hillel Y. Levin, *What Do We Really Know About the American Choice-of-Law Revolution?*, 60 STAN. L. REV. 247, 251 (2007) (reviewing SYMEON C. SYMEONIDES, THE AMERICAN CHOICE-OF-LAW REVOLUTION: PAST, PRESENT AND FUTURE (2006)).

190. United States v. Sisal Sales Corp., 274 U.S. 268, 275–76 (1927).

and did affect them."[191] This more flexible conception of territoriality is reflected in the influential Restatement (Third) of Foreign Relations Law's five bases for the exercise of legislative jurisdiction: "territorial, national, protective, passive personality, and universal jurisdiction."[192] It is under this rubric in the next Section that I evaluate a possible territorial sovereignty claim that offshore financial havens may raise.

B. Could Corporate Domicile Trigger an Authority to Legislate?

Of the five bases to exercise legislative jurisdiction recognized by the Restatement (Third) of Foreign Relations Law, only two potentially implicate the issue at hand: national and territorial.[193]

Territorial theory allows a nation state to exercise jurisdiction over any conduct committed in whole or in part within the state's borders and any action taking place outside the territory that has a local impact.[194] While the offshore financial haven's territorial contact with a corporate entity—ranging from the physical filing of the incorporation documents to maintaining a mailbox within the physical territory of the jurisdiction—may provide a possible claim under this theory, this argument is unavailing because the relevant entity's contact with the jurisdiction is largely metaphysical in the sense that the conduct potentially giving rise to a legal claim does not physically take place in offshore jurisdictions. While the territorial theory recognizes a right to legislate based on the effects felt within the jurisdiction,[195] this doctrine also does little work here given that corporate domicile is irrelevant for tracking the location of potential harm arising out of corporate

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191. United States v. Aluminum Co. of Am. (Alcoa), 148 F.2d 416, 444 (2d Cir. 1945); *see also id.* at 443 ("[A]ny 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.").

192. Brilmayer & Norchi, *supra* note 98, at 1244 (citing RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 402 (AM. LAW INST. 1987)).

193. Universal jurisdiction concerns jurisdiction over heinous crimes. *See* Brilmayer & Norchi, *supra* note 98, at 1244; Kenneth C. Randall, *Universal Jurisdiction Under International Law*, 66 TEX. L. REV. 785, 839 (1988). Protective jurisdiction generally concerns national security. *See* Brilmayer & Norchi, *supra* note 98, at 1245. Finally, passive personality concerns protection of the state's nationals abroad and is generally inapplicable outside of certain criminal law contexts. *See* RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 402 cmt. g(AM. LAW INST. 1987) (noting that passive personality jurisdiction "has not been generally accepted" for ordinary torts or crimes); Brilmayer & Norchi, *supra* note 98, at 1245.

194. *See* Lea Brilmayer, *Liberalism, Community, and State Borders*, 41 DUKE L.J. 1, 7 (1991) (illustrating the broad exercise of jurisdiction under the territorial theory by using U.S. antitrust law as an example).

195. Brilmayer & Norchi, *supra* note 98, at 1245. The impact theory of territoriality, also referred to as the "effects principle" of jurisdiction, most famously underpins the extraterritorial application of U.S. antitrust laws.

activities.[196] For instance, a U.S. retiree that invested in a fraudulent investment package sold by a Bahamian fund managed by investment managers in San Francisco will presumably still have the loss felt in the United States, because that is where the capital and persons interested are located.

Nationality theory is trickier.[197] The theory holds that a nation state may exercise jurisdiction respecting "any actions committed beyond its territory by one of its own nationals."[198] Corporate entities domiciled in offshore financial havens may be understood as "nationals" of those jurisdictions, similar to how a nation state may regulate the conduct of its citizens for conduct committed outside of its territory.

This view would impute nationality to corporate entities based on the entity's place of incorporation. The obvious advantage of this method is the creation of a bright-line rule.[199] Enhanced predictability, indeed, is one of the principle arguments that underlie the internal affairs doctrine, which instructs courts to apply the law of the state of the entity's place of incorporation to govern "internal" affairs between the entity's shareholders and the managers.[200] It is also important to acknowledge that corporations were once conceptualized as if they were natural persons based on their places of incorporation. Classically, a corporation was conceived as "an artificial person, coming into existence through creation by a sovereign power."[201] This early Anglo-American conception of corporate entities dominated court cases during the nineteenth century. As explained by the Massachusetts Supreme Court

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196. As Professor Curtis Bradley notes, the territorial category allows a nation to regulate "conduct within its territory as well as foreign conduct that has substantial effects or intended effects in its territory." Curtis A. Bradley, *Universal Jurisdiction and U.S. Law*, 2001 U. CHI. LEGAL F. 323, 323.

197. This is particularly the case because the nationality principle as applied to corporate entities has been unsettled for decades. *See* William Laurence Craig, *Application of the Trading with the Enemy Act to Foreign Corporations Owned by Americans: Reflections on* Fruehauf v. Massardy, 83 HARV. L. REV. 579, 589 (1970) ("The international law principles for determining the nationality of corporations are unsettled.").

198. Brilmayer & Norchi, *supra* note 98, at 1245.

199. As recognized by the U.S. Supreme Court, it would be difficult to structure internal corporate governance rules without the certainty afforded by a bright-line standard like incorporation. *See* Edgar v. MITE Corp., 457 U.S. 624, 645 (1982):

> The internal affairs doctrine is a conflict of laws principle which recognizes that only one State should have the authority to regulate a corporation's internal affairs—matters peculiar to the relationships among or between the corporation and its current officers, directors, and shareholders—because otherwise a corporation could be faced with conflicting demands.

200. Deborah A. DeMott, *Perspectives on Choice of Law for Corporate Internal Affairs*, 48 L. & CONTEMP. PROBS. 161, 161–63 (1985).

201. Adolf A. Berle, Jr., *The Theory of Enterprise Entity*, 47 COLUM. L. REV. 343, 343 (1947).

in the seminal case of *Bergner & Engel Brewing Co. v. Dreyfus*, "[A] corporation has its domicile in the jurisdiction of the state which created it, and, as a consequence, that it has not a domicile anywhere else."[202]

But those were also the days when the place of incorporation "was indicative of a real and meaningful connection between the corporation and the authorizing state."[203] This is no longer the case, as the dominance of the internal affairs doctrine in the twentieth century rendered the place of incorporation largely irrelevant for deducing an actual territorial relationship between the corporation and the state.[204] Absent some level of real economic activity taking place in offshore financial havens,[205] it is difficult to support the proposition that offshore jurisdictions can exercise prescriptive jurisdiction over matters "external" to the corporate form.[206]

This principle is easy enough to appreciate when comparing the difference between a natural person's domicile and a corporation's domicile. Domicile of a natural person is a territorial relationship between the state and the individual.[207] Generally speaking, the domicile concept establishes an individual's legal "headquarters" that in turn regulates a host of bundled rights between the individual and the government unit, including state taxes, voting rights, and education.[208] Domicile of natural persons generally requires extended

202. 51 N.E. 531, 532 (Mass. 1898); *see also* Tung, *supra* note 28, at 54 ("Corporate law had only a territorial effect, and a corporation existed only within the borders of the sovereign that created it."). This understanding is also reflected in the Restatement (First) of Conflicts of Laws, largely mirroring the views of its author, Joseph Beale. *See* RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 41 (AM. LAW INST. 1934); 1 BEALE, *supra* note 180, § 41.1.

203. Linda A. Mabry, *Multinational Corporations and U.S. Technology Policy: Rethinking the Concept of Corporate Nationality*, 87 GEO. L.J. 563, 587 (1999).

204. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 11 cmt. l (AM. LAW INST. 1971); Goldsmith, *Interest Analysis*, *supra* note 30, at 602 n.32; *see also* Julian Arato, *Corporations as Lawmakers*, 56 HARV. INT'L L.J. 229, 275 (2015) (explaining in the international investment law context that "the corporation's flexible form affords the multinational business enterprise significant leeway to acquire treaty protection for its contracts with foreign sovereigns"); Tung, *supra* note 28, at 33–36 (explaining the rise of the internal affairs doctrine). Indeed, as others have argued, the internal affairs doctrine is said to be the foundation of jurisdictional competition in U.S. corporate law. *See* Vincent S.J. Buccola, *States' Rights Against Corporate Rights*, 2016 COLUM. BUS. L. REV. 595, 636.

205. I am not suggesting that this would be impossible. The point, rather, is that offshore financial havens are currently used precisely to "provide protection from national regulation and taxation *without* the need to physically relocate to the host country." Palan, *Commercialization*, *supra* note 38, at 163.

206. *Cf.* Frederick A. Mann, *The Doctrine of Jurisdiction in International Law*, 111 RECUEIL DES COURS 1, 97 (1964) ("No country could so provide without contravening the paramount principle of international jurisdiction, i.e. the requirement of a close connection between the legislating State and the subject-matter of the legislation.").

207. Goldsmith, *Interest Analysis*, *supra* note 30, at 600.

208. *Id.* at 600.

physical presence in the place and specific intent to make that jurisdiction home.[209] It is because of this unique relationship between the individual and the government unit that state courts principally deduce "state interest" in terms of the domicile of noncorporate litigants in domestic choice of law cases.[210] Indeed, in a large number of domestic choice of law disputes, a court "simply determines the domicile of the plaintiff and the defendant and then assigns to each party the law of that domicile in ascertaining each state's interest in applying its laws."[211]

Corporate domicile, by contrast, is a contract used to establish the legal relations between members "internal" to corporate entities.[212] Indeed, mainstream corporate law scholars conceptualize corporate law as standard-form default rules produced by states.[213] It is for this reason that while half of Fortune 500 companies call Delaware their *juridical* home, only two of them operate their physical headquarters in the state.[214] As visitors to Wilmington, Delaware will quickly realize, the

209. RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 16, 18 (AM. LAW INST. 1971).

210. *See, e.g.*, John Bernard Corr, *Interest Analysis and Choice of Law: The Dubious Dominance of Domicile*, 1983 UTAH L. REV. 651, 653 ("[I]nterest analysis assumes that states have special interests in litigation that affects persons who are domiciled or residing within their borders."). State interest is a loaded term. In domestic choice of law cases, state interest refers to a prima facie claim that a state's law (e.g., New York law) should apply in a case connected to more than one state (e.g., New York and Connecticut). *See* Lea Brilmayer, *Interest Analysis and the Myth of Legislative Intent*, 78 MICH. L. REV. 392, 394 (1980) [hereinafter Brilmayer, *Legislative Intent*]. Interest analysis, a related term developed by Professor Brainerd Currie, is one intimately familiar to modern conflict of laws teachers. *See* BRAINERD CURRIE, SELECTED ESSAYS ON THE CONFLICT OF LAWS (1963). I use the term not because I follow all of Currie's theoretical approaches, many of which have been thoroughly discredited. *See* Lea Brilmayer, *What I Like Most About the Restatement (Second) of Conflicts, and Why it Should not be Thrown out With the Bathwater*, 110 AJIL UNBOUND 144, 145 n.5 (2016); John Hart Ely, *Choice of Law and the State's Interest in Protecting its Own*, 23 WM. & MARY L. REV. 173, 175 (1981). But the term captures an important theoretical advancement—that law is not an objectively existing entity deduced by territorial postulates, as Joseph Beale had his contemporaries believe in the early twentieth century, but rather that the law is a tool of social policy. *See* Roosevelt, *supra* note 180, at 2461. I share this premise with more modern writers. *See, e.g.*, Larry Kramer, *The Myth of the "Unprovided-For" Case*, 75 VA. L. REV. 1045 (1989).

211. Goldsmith, *Interest Analysis*, *supra* note 30, at 601; *see* Corr, *supra* note 210, at 654 ("[T]he interest of a state other than that in which a party is domiciled may prevail, but it is far more common for the interest of a domiciliary state to dominate.").

212. Tung, *supra* note 28, at 35–36.

213. FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 2 (1991) ("The corporate code in almost every state is an 'enabling' statute. An enabling statute allows managers and investors to write their own tickets, to establish systems of governance without substantive scrutiny from a regulator.").

214. *See* BRUNER, *supra* note 3, at 181.

juridical home of corporate entities can look like nothing more than a small mailbox in a warehouse-like building.[215]

Incorporating in an offshore jurisdiction is not so different. Ugland House, an unassuming building located in Georgetown, Cayman Islands, is home to nearly nineteen thousand corporate entities, often "participants in investment activities, such as those related to hedge funds or private-equity funds, and structured finance activities, such as securitization or aircraft finance."[216] The house drew international headlines in 2008 with then-presidential candidate Barack Obama's assessment that the building was "either the biggest building or the biggest tax scam on record."[217] A U.S. government investigative report later revealed that the sole occupant of Ugland House is a law firm that serves as a registration office. Ninety-six percent of the entities registered in the office were classified as exempted entities under Cayman Islands law, meaning that they are generally prohibited from carrying out domestic business within the Cayman Islands.[218] This account is confirmed by other sources, as well. For instance, a recent study found that of the 25.5 percent of hedge funds legally registered in the Cayman Islands, only 0.3 percent of the funds were physically managed from the Cayman Islands.[219]

The fact that "exempted" or "excepted" entities are involved in an offshore financial transaction should matter considerably when a judge decides whether U.S. regulatory law ought to apply to a case with both a domestic and a foreign fact pattern. For instance, if a securities transaction's only nondomestic connection is the fact that it was offered by an exempt entity registered in the Bahamas, there is little reason why the judge should decline to apply federal securities law on grounds that the transaction was completed "extraterritorially" and thus outside

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215. A small humdrum office on North Orange Street in Wilmington, Delaware is the legal headquarters to 285,000 separate businesses, including American Airlines, Apple, Bank of America, and Wal-Mart, among thousands of other entities. *See* Leslie Wayne, *How Delaware Thrives as a Corporate Tax Haven*, N.Y. TIMES (June 30, 2012), http://www.nytimes.com/2012/07/01/business/how-delaware-thrives-as-a-corporate-tax-haven.html [https://perma.cc/FRS2-9QXP].

216. GAO REPORT, *supra* note 34, at 3.

217. KOEN BYTTEBIER, TOWARDS A NEW INTERNATIONAL MONETARY ORDER 264 (2017) (citation omitted).

218. GAO REPORT, *supra* note 34, at 3, 12–13. It is perhaps for this reason that courts in the interstate conflicts cases did not accord weight to corporate domicile as triggering state interests, even as courts were willing to accept domicile of natural persons as triggering state interests. *See* Goldsmith, *Interest Analysis*, *supra* note 30, at 609–16.

219. *See* Michael Brocard & Francois-Serge Lhabitant, *A Primer on the Tax Framework of Offshore and Onshore Hedge Funds*, EDHEC BUS. SCH. 3–4 (June 13, 2016), https://www.edhec.edu/sites/www.edhec-portail.pprod.net/files/publications/pdf/edhec-working-paper-a-primer-on-the-tax-framework-f_1467203960443-pdfjpg [https://perma.cc/QR6L-HACZ].

of the reach of the Exchange Act. To rule otherwise would be to enable private entities to contractually opt out of securities fraud—something expressly prohibited by the language of the statute that bars any "condition, stipulation, or provision binding . . . to waive compliance" with the regulation.[220]

It is perhaps because the legal residence of business entities need not align with where those entities actually operate that federal legislation aimed at regulating corporate entities traditionally looked to the control and ownership of the entities as opposed to where the entity was formed. This method of imputing corporate nationality traces its origin to early twentieth-century federal statutes enacted to establish a jurisdictional basis for subjecting corporations to U.S. law.[221] Thus, for instance, national security laws adopted by Congress during and after World War I established restrictions on foreign ownership of firms in key strategic industries, defining corporate nationality "primarily by reference to the nationality of a firm's shareholders, and in some cases, its officers and directors."[222] Moreover, the Export Administration Act of 1979, which prohibited U.S. companies from participating in the Arab boycott of Israel, defined U.S. companies broadly to include foreign affiliates that are "controlled in fact" by U.S. persons.[223] These cases, of course, do not necessarily indicate a uniform approach adopted by Congress. Rather, they show that laws enacted to regulate the conduct of corporate entities are often "determined by the place from which the corporation is controlled."[224]

To be sure, there is an inherent difficulty in imputing "interest" on a juridical entity—the nation state. While it is easy to anthropomorphize the state to advance one's view on what types of sovereign interest ought to count, such an effort is bound to break down under serious intellectual pressure. This is not necessarily because

220. *See* Securities Exchange Act of 1934, 15 U.S.C. § 78cc(a) (2012).

221. Mabry, *supra* note 203, at 582, 584–86.

222. *Id.* at 586. A paradigmatic example is the Radio Act of 1927, ch. 169, § 12, 44 Stat. 1167 (repealed 1934) (requiring the licensing of all radio station owners and limiting the award of licenses to U.S. citizens, with corporate citizenship being defined as corporate entities whose officers or directors were U.S. nationals and that had eighty percent of their stock owned by U.S. citizens).

223. Export Administration Act of 1979, Pub. L. No. 96-72, § 16, 93 Stat. 503 (1979) (expired 1994); Mabry, *supra* note 203, at 582 n.78. These tests, of course, are not without downsides. For instance, as Mabry suggests, "Discerning the identity and nationality of persons or entities that have the power to influence key corporate decisions is becoming increasingly difficult." Mabry, *supra* note 203, at 590.

224. Craig, *supra* note 197, at 589.

state interest is purely objective[225] but because there are underlying international norms and enforcement constraints that define the current world order.[226]

Similarly, my argument does not hinge on whether an offshore jurisdiction would subjectively assess that it has an interest in applying its law to a range of disputes external to the corporate entity domiciled in that jurisdiction. After all, it is no secret that the earliest forms of modern tax havens deliberately adapted strategies aimed to attract incorporation business to increase local government revenue.[227] Such an argument is unpersuasive.[228] Consider an analogy from the domestic context. In the United States, Delaware derives a substantial portion of its government revenue from competing (successfully) in the market for corporate registration.[229] But very few would argue that this revenue interest requires applying Delaware law for state regulatory law (e.g., state antitrust law) involving Delaware corporations. Delaware's requirement that corporations wishing to opt into Delaware corporate law possess a physical mailbox within the state does not alter this equation.[230] Unbridled subjective interest of sovereigns in the international arena should be reined in not because sovereign interest is necessarily objective but because it is functionally constrained by a multijurisdictional system.

To be clear, my goal here is not to be the jury in resolving "conflicts" when at least two competing jurisdictions can assert legitimate authority to prescribe the same conduct. The transnational nature of modern commerce necessarily produces instances where

225. For a discussion on the subjective and objective ways to construct the concept of state interest, see LEA BRILMAYER, CONFLICT OF LAWS: FOUNDATIONS AND FUTURE DIRECTIONS 98–103 (1991); Lea Brilmayer, *The Other State's Interests*, 24 CORNELL INT'L L.J. 233, 240–43 (1991); Roosevelt, *supra* note 180, at 2481, 2485–86.

226. For a general discussion, see Oona Hathaway & Scott J. Shapiro, *Outcasting: Enforcement in Domestic and International Law*, 121 YALE L.J. 252, 272 (2011).

227. R.A. JOHNS, TAX HAVENS AND OFFSHORE FINANCE: A STUDY OF TRANSNATIONAL ECONOMIC DEVELOPMENT 20 (1983).

228. It is entirely possible that offshore financial havens, when asked, would express an interest in governing particular cross-border transactions. At least theoretically, this increases the fees that the governments of these jurisdictions can extract from entities attempting to evade assortments of otherwise applicable laws by their home jurisdictions.

229. Indeed, Roberta Romano's seminal work on corporate charter competition between states depends on the assumption that franchise taxes represent a substantial source of state revenue. Romano, *supra* note 89, at 280. This assumption may not universally hold. *See* Marcel Kahan & Ehud Kamar, *The Myth of State Competition in Corporate Law*, 55 STAN. L. REV. 679 (2002).

230. Under Delaware law, a corporate entity need not conduct its business in the state to call Delaware its legal domicile. Rather, it need only file paperwork, pay a franchise tax, and hire a registered agent who "must have a physical street address in Delaware." *How to Form a New Business Entity*, DEL. DIVISION CORPS., https://corp.delaware.gov/howtoform.shtml (last visited Sept. 10, 2018) [https://perma.cc/YCR5-6XPP].

conduct in one jurisdiction affects more than one jurisdiction. For instance, the seminal case of *Hartford Fire Insurance Co. v. California* involved the extraterritorial application of the Sherman Act to various reinsurance companies in the United Kingdom that allegedly conspired to harm U.S. consumers.[231] Similarly, it is entirely conceivable that some form of economic activity occurs in offshore jurisdictions for certain forms of cross-border commercial transactions. These are situations where an extraterritorial application of federal regulatory statutes may affect other jurisdictions' interests in regulating their own, which can generate the types of regulatory retaliation that the presumption against extraterritoriality is designed to help avoid.[232]

Regulatory litigation involving corporate entities domiciled in offshore financial havens, on the other hand, are often situations that may appear at first to involve the interest of multiple jurisdictions in which only one jurisdiction actually has the authority to prescribe a particular conduct.

C. Jurisdictional Competition and Regulatory Arbitrage: A Reassessment

Even disregarding foreign sovereign interests, arguments in favor of international regulatory competition facilitated by territorially tethered domestic rules do not completely lose their intellectual appeal. When viewing laws as "products,"[233] the source of those "products" does not necessarily alter the efficiency gain envisioned by these accounts.[234] That is, whether a rule governing a financial transaction is produced entirely by a private organization (e.g., International Swaps and Derivatives Association),[235] a state (e.g., New York law), or a foreign sovereign (e.g., Cayman Islands law), private choice enables private entities to make welfare-enhancing transactions between consenting parties.

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231. 509 U.S. 764, 769–80 (1993).

232. Roger P. Alford, *The Extraterritorial Application of Antitrust Laws: A Postscript on* Hartford Fire Insurance Co. v. California, 34 VA. J. INT'L L. 213, 215, 220 (1993); Weintraub, *supra* note 97, at 1800.

233. Romano, *supra* note 89, at 225–27.

234. Although the term "efficiency" is often used in unmoored and inconsistent ways in legal scholarship, I use the term generically to refer to the concept of "achieving a maximum value of output from a given value of inputs." George J. Stigler, *Law or Economics?*, 35 J.L. & ECON. 455, 458 (1992).

235. For an excellent primer on the transnational private regulation of over-the-counter derivatives, see Gabriel V. Rauterberg & Andrew Verstein, *Assessing Transnational Private Regulation of the OTC Derivatives Market: ISDA, the BBA, and the Future of Financial Reform*, 54 VA. J. INT'L L. 9 (2013).

Theoretically, therefore, offshore corporate form delimiting the application of federal statutes can be conceptualized as an emerging virtual space built by transnational private contracts enabling private entities to opt out of otherwise mandatory rules.[236] These spaces are in part built by domestic legal rules enabling private entities to accrete growing influence over cross-border economic transactions, under the doctrinal framework of judicial modesty and international comity.[237]

Indeed, functionally, allowing private entities to opt out of mandatory domestic laws through offshore incorporation mirrors "legal regime shopping" through the insertion of choice of law clauses in private contracts.[238] The latter, which is now a ubiquitous companion to cross-border commercial transactions and increasingly enforced by both national courts and private arbitration houses, effectively allows private entities to "legal regime shop" without establishing any territorial connection with the preferred jurisdiction.[239] Importantly, recent U.S. court jurisprudence in many cases allows private entities to opt out of a range of otherwise mandatory statutes by contractually stipulating to be governed by foreign law.[240] Both mechanisms—offshore corporate domicile and private contracts—allow private entities to opt out of bundles of local rules without physically exiting that jurisdiction. Theoretically, the supporters for this line of "private choice" approaches tend to reason that choice enables private entities

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236. Corporate structuring in the transnational context, to a certain extent, may be intellectually grounded in neoliberalist thought that tends to support "particular market imperatives" against "political intervention." David Singh Grewal & Jedediah Purdy, *Introduction: Law and Neoliberalism*, 77 L. & CONTEMP. PROBS. 1, 1 (2014). As Professor David Grewal explains, neoliberalism, in both domestic and transnational contexts,

> privileges relations of sociability and mistrusts those of sovereignty, since (on its own account at least) the latter are distorted and corrupted by power in a way the former are not. Instead, neoliberals place their faith in those activities that people undertake as individuals choosing to participate in broader structures of social life.

DAVID SINGH GREWAL, NETWORK POWER: THE SOCIAL DYNAMICS OF GLOBALIZATION 247 (2008).

237. *See, e.g.*, Brilmayer, *New Extraterritoriality*, *supra* note 108, at 656 (critiquing the Supreme Court's opinion in *Morrison* as being littered with "pretensions to judicial modesty"). Interestingly, the contemporary private governance of transnational commercial activities has also been expressly conceptualized as "offshore" or "virtual spaces." *See* ALEC STONE SWEET & FLORIAN GRISEL, THE EVOLUTION OF INTERNATIONAL ARBITRATION: JUDICIALIZATION, GOVERNANCE, LEGITIMACY 35 (2017) (describing a transnational private arbitral governance of transnational business as a "space" that makes "no sovereignty claims over people or territory").

238. *See* ERIN A. O'HARA & LARRY E. RIBSTEIN, THE LAW MARKET 1–12 (2009); Erin A. O'Hara & Larry E. Ribstein, *From Politics to Efficiency in Choice of Law*, 67 U. CHI. L. REV. 1151, 1152–57 (2000).

239. *See* Erin O'Hara O'Connor & Larry E. Ribstein, *Preemption and Choice-of-Law Coordination*, 111 MICH. L. REV. 647, 692 (2013) ("For many types of contracts today, courts routinely and nearly uniformly enforce choice-of-law clauses.").

240. *Id.* at 691–92.

to be governed by law that best suit their needs. As an added benefit, it may encourage competition between jurisdictions to produce innovative law.[241]

I am skeptical of these views because normative accounts that focus on effectuating private choice and efficiency—a predominant focus of private law scholarship[242]—are often dependent on the view that regulatory laws serve no social purpose.[243] At the very least, there are reasons to cast doubt on this viewpoint, given that private benefits and costs may not necessarily align with social benefits and costs.[244] Tax incentives, for instance, may induce private entities to opt into an offshore jurisdiction's legal regime, even when this structure may not be desirable from the general public's standpoint.[245]

Even assuming efficiency gains attributable to private entities' ability to opt out of a set of otherwise mandatory laws, the jurisdictional competition theory holds less persuasion when private transactions tend to impose externalities on third parties.[246] The lack of externalities, fatally, is an assumption largely shared by proponents of jurisdictional competition, who owe their intellectual roots to the Tiebout model. The model, developed by economist Charles Tiebout in a 1956 article,[247] posits that competition among cities for mobile individuals results in the efficient supply of local public goods by those

241. O'HARA & RIBSTEIN, *supra* note 238, at 5–12. The private choice rationale is also prominently advocated in the field of securities regulation. For seminal accounts, see Stephen J. Choi & Andrew T. Guzman, *Portable Reciprocity: Rethinking the International Reach of Securities Regulation*, 71 S. CAL. L. REV. 903 (1998); Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L.J. 2359 (1998).

242. *See* Grewal & Purdy, *supra* note 236, at 15 ("[P]rivate-law scholarship has largely organized itself around the concept of efficiency, whether devising efficiency-enhancing reforms or debating the correct definition of efficiency and the appropriate scope of efficiency concerns.").

243. Professor Joel Trachtman makes this observation in the securities law context. Trachtman, *supra* note 22, at 25–26 (arguing that issuer choice-based theories to securities regulation "are dependent on an assumption that securities regulation serves no social purpose: that there is no externality worthy of being internalized by regulation").

244. Proponents for leaving private commercial transactions entirely to private bargaining tend to underappreciate that there are social impacts of private transactions that are not necessarily internalized by contracting parties. *See* RICHARD R.W. BROOKS & CAROL M. ROSE, SAVING THE NEIGHBORHOOD: RACIALLY RESTRICTIVE COVENANTS, LAW, AND SOCIAL NORMS 58 (2013) (explaining in the racial restrictive covenants context that "social impacts . . . are not necessarily internalized by the initial contracting parties").

245. *See* Moon, *Tax Havens*, *supra* note 58, at 1093–94.

246. Externalities is a loaded concept in both economics and law. For my purposes, I refer to the range of costs and benefits borne by society at large, other than those engaged in private transactions. For a seminal account of externalities, see Harold Demsetz, *Toward a Theory of Property Rights*, 57 AM. ECON. REV. 347, 348 (1967).

247. *See* Charles M. Tiebout, *A Pure Theory of Local Expenditures*, 64 J. POL. ECON. 416 (1956). Under the Tiebout model, the threat of physical exit from the state incentivizes states to provide public goods, including the bundle of laws imposed on its subjects.

cities. While advancing the debate considerably, the Tiebout model, like many economic theories, unrealistically presupposes the absence of externalities.[248]

Thus, even from an efficiency standpoint, the gains envisioned by proponents of international regulatory competition are empirically unproven.[249] In regulatory theory, the mandatory nature of certain statutes[250]—including antitrust, most securities regulation, and practically all criminal law—exists "where the regulated person does not absorb all of the effects, adverse or beneficial, of his or her action."[251] As explained by Professor Joel Trachtman, "[T]he mandatory nature of a law is an indicator, and is perhaps the best evidence, that the law addresses externalities in the private sector that would ordinarily be expected to translate into interstate externalities."[252] Indeed, as

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248. *See* William W. Bratton & Joseph A. McCahery, *The New Economics of Jurisdictional Competition: Devolutionary Federalism in a Second-Best World*, 86 GEO. L.J. 201, 231–32 (1997) ("The Tiebout model unrealistically assumes the absence of externalities . . . . [I]ndividual actions often have external effects. This occurs whenever one's actions impact on the interests of others and one fails to account for such impact."); Trachtman, *supra* note 22, at 27 ("[T]he Tiebout model depends on a number of assumptions, including the absence of externalities . . . .").

249. Indeed, even in the domestic context, "[a] number of economists have also advocated general legal restrictions on private agreements to deal with undesirable externalities." Richard R.W. Brooks, *Credit Past Due*, 106 COLUM. L. REV. 994, 1017 (2006) (collecting sources).

250. For instance, certain federal regulatory statutes, including the Securities Act of 1933, expressly prohibit parties from avoiding liability through direct contractual waiver. *See, e.g.*, Securities Act of 1933, 15 U.S.C. § 77n (2012) ("Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this [subchapter] or of the rules and regulations of the Commission shall be void.").

251. Trachtman, *supra* note 22, at 17. Mandatory structural rules imposed by the state may also be designed to solve coordination problems endemic to certain business transactions. *See, e.g.*, Alan Schwartz, *A Contract Theory Approach to Business Bankruptcy*, 107 YALE L.J. 1807, 1808 (1998) ("That bankruptcy systems solve a coordination problem rather than regulate the substance of transactions accounts for some of the distinctions between bankruptcy and commercial law generally . . . . Structural rules of the game must be mandatory or the game cannot be played at all.").

252. Trachtman, *supra* note 22, at 6. To be sure, one's view on how "mandatory" a set of rules ought to be is undoubtedly influenced by his or her view on whether and to what extent domestic laws are infected by the rent-seeking behavior of various interest groups. This is the influential public-choice theory that in part motivates the private-choice-driven approach to regulatory law. *See, e.g.*, DANIEL A. FARBER & PHILIP P. FRICKEY, LAW AND PUBLIC CHOICE: A CRITICAL INTRODUCTION 1 (1991):

> [W]e cannot simply take for granted that the legislature represents the public interest. Realistically, we must also consider the possibility that a statute represents private rather than public interests, because of the undue influence of special interest groups. Alternatively, a statute may fail to represent any identifiable "public" interest because the public itself is too fragmented to generate any coherent public policy.

For important work applying the public-choice theory to regulatory law governing private transactions, see O'HARA & RIBSTEIN, *supra* note 238; Larry E. Ribstein, *Choosing Law by Contract*, 18 J. CORP. L. 245 (1993); and Larry E. Ribstein & Bruce H. Kobayashi, *State Regulation of Electronic Commerce*, 51 EMORY L.J. 1 (2002). While there are surely domestic laws that reflect this premise, that generalization does not stand up to serious scrutiny as a universal theory. It

Professor Robert Wai reminds us, "[T]he policy goals of private law include social regulation: to provide public goods, to correct for market failure, and to contribute to social deterrence."[253]

Efficiency is wonderful, but not at the cost of accepting a watered-down conception of the law. Bankruptcy law, for instance, may be conceptualized as a set of rules governing the relationship between the creditor and the debtor.[254] But it could also be understood as laws designed to effectuate certain policy goals that take into account other stakeholders affected by corporate bankruptcies.[255] Securities regulation may be purely examined as the law governing the relationship between investors and issuers.[256] But it may also be understood as law designed to deter fraud and assortments of market failures that have resulted in mass externalities borne by the general public.[257] The list can go on and on.[258]

The private choice rationale espoused by efficiency-oriented scholars is particularly hard to justify when legislatures—as in the case of statutes like civil RICO—include treble damages provisions for successful private litigants.[259] The overcompensation of the plaintiff is perhaps the clearest indication of the legislature relying on "private attorneys general" to complement the efforts of public enforcement

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seems at least equally plausible that "legislation incorporates the public interest as well as possible given institutional constraints." Trachtman, *supra* note 22, at 16.

253. Robert Wai, *Transnational Private Law and Private Ordering in a Contested Global Society*, 46 HARV. INT'L L.J. 471, 474 (2005).

254. In a seminal piece, Professors Douglas Baird and Thomas Jackson famously articulated the goal of bankruptcy law as enhancing the collection efforts of "those . . . who, outside of bankruptcy, have property rights in the assets of the firm." Douglas G. Baird & Thomas H. Jackson, *Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy*, 51 U. CHI. L. REV. 97, 103 (1984).

255. *See e.g.*, Elizabeth Warren, *Bankruptcy Policymaking in an Imperfect World*, 92 MICH. L. REV. 336, 343 (1993) (arguing that bankruptcy law constitutes "a collection system that determines the value of a failing business, how to distribute that value among parties whom the failure affects, and the extent to which affected parties can externalize the costs of failure to others who did not deal with the debtor").

256. Mandatory rules imposed by a domestic legal regime, under this view, may be overly restrictive on welfare-enhancing private transactions. *See* O'HARA & RIBSTEIN, *supra* note 238, at 1–10.

257. As Professor Merrit Fox observes, "[A]bsent regulation, firms can be expected to disclose less than is socially optimal." Merritt B. Fox, *Securities Disclosure in a Globalizing Market: Who Should Regulate Whom*, 95 MICH. L. REV. 2498, 2551 (1997).

258. *Cf.* David Singh Grewal, *The Laws of Capitalism*, 128 HARV. L. REV. 626, 659 (2014) (reviewing THOMAS PIKETTY, CAPITAL IN THE TWENTY-FIRST CENTURY (2014)) ("[L]aw structures not just the particular bargains in capitalism . . . but also the broader social and political setting of the market.").

259. 18 U.S.C. § 1964(c) (2012) (providing that a successful plaintiff under civil RICO "shall recover threefold the damages he sustains and the cost of the suit").

agencies to effectuate particular legislative aims.[260] The United States famously relies on a diffused system of enforcement mechanisms, relying on both public regulatory agencies and private litigants to effectuate legislative aims. This system is in part necessitated by endemic resource constraints facing agencies like the SEC. Reliance on public enforcement alone, under this structural design, is unlikely to detect enough violations of any given statute.[261] This is because private litigants, "through pursuit of their own interests . . . serve larger social purposes of regulation."[262] This point is critical to understanding the underappreciated role of private litigants in detecting violations of public regulatory law. While private litigants often do rely on the investigative efforts of public agencies like the Securities and Exchange Commission or the Department of Justice to bring private claims, the reverse is also true: public regulators, in some cases, decide to bring enforcement actions following the initiation of private litigation.[263] This should be unsurprising, given that private litigants, in certain situations, are at an institutional advantage by virtue of possessing "[t]he best sources of information about private wrongs."[264]

The presence of negative externalities associated with certain private misconduct gives little reason to make regulatory statutes amenable to private choice,[265] under the pretense of being governed by

260. The term "private attorneys general" was coined by Judge Jerome Frank. *See* Associated Indus. of New York State, Inc. v. Ickes, 134 F.2d 694, 704 (2d Cir. 1943), *vacated as moot*, 320 U.S. 707 (1943) ("[T]here is nothing constitutionally prohibiting Congress from empowering any person, official or not, to institute a proceeding involving such a controversy, even if the sole purpose is to vindicate the public interest. Such persons, so authorized, are, so to speak, private Attorney Generals."); *see also* Jill E. Fisch, *Federal Securities Fraud Litigation as a Lawmaking Partnership*, 93 WASH. U. L. REV. 453, 462 (2015) ("In legislating private securities fraud, Congress reaffirmed the critical policy considerations that had previously been identified by the Court. Congress explicitly recognized the importance of private litigation as a supplement to public enforcement efforts.").

261. J. Maria Glover, *The Structural Role of Private Enforcement Mechanisms in Public Law*, 53 WM. & MARY L. REV. 1137, 1178 (2012); *see also* Matthew C. Stephenson, *Public Regulation of Private Enforcement: The Case for Expanding the Role of Administrative Agencies*, 91 VA. L. REV. 93, 95–96 (2005) (arguing that private litigants in the United States play an important role in "deterring, detecting, and correcting socially harmful violations of the law"). It is for this reason that the relatively broad "extraterritorial" regulatory authority enjoyed by public enforcement agencies in the financial regulation context, *see* Griffith, *supra* note 20, at 1329–30, in my view is insufficient to fully safeguard U.S. interests.

262. Wai, *supra* note 253, at 474.

263. John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter is not Working*, 42 MD. L. REV. 215, 223, 231 n.18 (1983).

264. *See* Glover, *supra* note 261, at 1154.

265. To be clear, there are good reasons to leave certain areas of the laws—including corporate law—largely amenable to private choice. These areas tend to be predominantly default laws in domestic contexts, where the sovereign supplies templates of laws that private entities can opt in and out of as they see fit. EASTERBROOK & FISCHEL, *supra* note 213, at 2 ("The corporate code in

foreign law.[266] In particular, a race to the bottom may be enabled by the phenomenon of "legislative capture,"[267] whereby private entities can opt into a desirable bundle of rules by literally writing the laws of foreign jurisdiction.[268] Perhaps the most salient example is the case of the Cook Islands in the South Pacific Ocean, a jurisdiction that pioneered laws in the late 1980s "devised to protect foreigners' assets from legal claims in their home countries."[269] The Cook Islands trusts law was written by Colorado-based lawyer Barry Engel "with Americans in mind."[270] Cook Islands law, unsurprisingly, offers strict bank secrecy rules and refuses to recognize or enforce foreign judgments.[271] The Cook Islands government generates revenues in the form of "registration fees, taxes on trust companies and their employees, and various support services."[272]

Legislative capture is a phenomenon especially vulnerable to the governments of small offshore jurisdictions looking to convert their lawmaking authority into staple revenue streams. It is no secret that interested private parties work intimately with local legislatures in offshore financial havens. One "offshore magic circle" law firm, for instance, even advertises "its close working relations with tax haven

almost every state is an 'enabling' statute. An enabling statute allows managers and investors to write their own tickets, to establish systems of governance without substantive scrutiny from a regulator."). Regulatory statutes, on the other hand, tend to be precisely the kinds of laws that are designed to force private actors to internalize costs that are not being fully internalized by private transactions.

266. As Professor Steven Ratner observes, "[T]he desire of many less developed states to welcome foreign investment means that some governments have neither the interest nor the resources to monitor corporate behavior, either with respect to the [multinational corporation's] employees or with respect to the broader community." Steven R. Ratner, *Corporations and Human Rights: A Theory of Legal Responsibility*, 111 YALE L.J. 443, 462 (2001).

267. James Kwak, *Incentives and Ideology*, 127 HARV. L. REV. FORUM 253, 256 (2014) (describing legislative capture as "the ability of industry to use its financial clout to influence Congress and, indirectly, agencies that are overseen by Congress").

268. The related phenomenon of "regulatory capture" is a concept well developed in the economic policy literature. Regulatory capture is broadly understood as the "process through which special interests affect state intervention in any of its forms, which can include areas as diverse as the setting of taxes, the choice of foreign or monetary policy, or the legislation affecting R&D." *See* Ernesto Dal Bó, *Regulatory Capture: A Review*, 22 OXFORD REV. ECON. POL'Y 203, 203 (2006).

269. Leslie Wayne, *Cook Islands, a Paradise of Untouchable Assets*, N.Y. TIMES (Dec. 14, 2013), http://www.nytimes.com/2013/12/15/business/international/paradise-of-untouchable-assets.html [https://perma.cc/M5N6-2UD5].

270. *Id.* ("A Cook official, seeking revenue for the islands, read in The Economist about Mr. Engel's firm, which was pioneering the concept of asset protection trusts, and hired Mr. Engel to help write the 1989 law.").

271. *See* Reuben W. Tylor, *Effective Firewall Legislation—Cook Islands*, 14 TRUSTS & TRUSTEES 685 (2008) (emphasizing the effectiveness of Cook Islands' firewall legislation).

272. Wayne, *supra* note 269.

governments."[273] Other law firm partners have been members of the local legislatures of notorious tax havens.[274] The transnational public-private collaboration that could have catastrophic consequences is not a mere theoretical inquiry. In a recent case before the Fifth Circuit, victims of a Ponzi scheme brought an action against the island nation of Antigua for playing a role in facilitating a $7 billion Ponzi scheme involving financier Allen Stanford.[275] While the suit was thrown out for lack of subject matter jurisdiction under the Foreign Sovereign Immunities Act, defrauded investors pleaded (with substantial evidence) that "Antigua accepted numerous loans and other financial contributions from Stanford and in return provided him with a significant amount of influence over Antigua generally, and especially over its financial regulatory sector."[276] While good arguments can be made about legislative capture lowering the transactional costs for producing desirable templates of *default* rules governing private relations,[277] leaving regulatory laws to the hands of captured lawmakers makes little sense both from a democratic legitimacy standpoint and from an efficiency standpoint.

D. Advice to Congress and Courts: Toward Sensible Extraterritoriality

The unterritorial aspects of modern financial transactions challenge territorially configured domestic laws at their core.[278] This Article has argued that a restrictive approach to construing the

273. John Christensen, *Do They Do Evil? The Moral Economy of Tax Professionals*, *in* NEOLIBERALISM AND THE MORAL ECONOMY OF FRAUD 72, 79 (David Whyte & Jörg Wiegratz eds., 2016).

274. *See id.*

275. Frank v. Antigua & Barbuda, 842 F.3d 362, 365–67 (5th Cir. 2016).

276. Frank v. Antigua & Barbuda, No. 3:09-CV-2165-N, 2015 WL 13173102, at *1 (N.D. Tex. June 26, 2015), *rev'd*, 842 F.3d 362 (5th Cir. 2016).

277. U.S. corporate law, dominated by Delaware notwithstanding its small size, would be a paradigmatic example. *See, e.g.*, LEWIS S. BLACK, JR., WHY CORPORATIONS CHOOSE DELAWARE 4 (2007) (describing the "unwritten compact between [Delaware lawyers] and the state lawmakers" where the Delaware lawmakers regularly "call upon the expertise of the Corporation Law Section of the Delaware Bar Association to recommend, review, and draft almost all amendments to the statute").

278. This problem is not unique to modern finance. For instance, unterritorial aspects of data challenge territorially defined Fourth Amendment jurisprudence. *See* Jennifer Daskal, *The Un-Territoriality of Data*, 125 YALE L.J. 326, 326 (2015):

> Fourth Amendment rights turn on whether the search or seizure takes place territorially or extraterritorially . . . . The ease and speed with which data travels across borders, the seemingly arbitrary paths it takes, and the physical disconnect between where data is stored and where it is accessed critically test these foundational premises.

geographic scope of federal statutes has created loopholes for commercial entities to evade important federal regulatory laws. Correcting this problem necessarily requires a structural reexamination of our extraterritoriality jurisprudence. This Section outlines lessons to draw on from the foregoing discussion.

First, determining the scope of federal statutes in the modern era requires us to refine territorially tethered conceptions of the law that were developed largely presupposing the link between territorial contact and a jurisdiction's lawmaking authority.[279] Today, territorial contact with a particular jurisdiction, even if factually ascertainable, could misleadingly or arbitrarily track whether that jurisdiction has an interest in applying its law to a dispute related to that contact. Forming a feeder fund in the Cayman Islands, for instance, typically entails maintaining a physical mailbox in the Cayman Islands and hiring a "dummy director" residing in the Cayman Islands.[280] As discussed above, however, this form of "territorial" contact with the Cayman Islands does not necessarily trigger the sovereign interest of the Cayman Islands to regulate conduct involving the feeder fund.

Territorially tethering the scope of domestic statutes is a particularly undesirable method for regulating modern financial transactions. Given unprecedented capital mobility and the ubiquity of online transactions,[281] private actors can easily shift the locus of their transactions outside of the territory of any given jurisdiction.[282] When a transaction takes place either in multiple places or electronically, fixating on the location of that transaction is bound to result in arbitrary and inconsistent decisions. At worst, it creates loopholes for private actors to opt out of mandatory laws of the United States that are in part designed to safeguard the general public's interest at large.[283] While territorial contact continues to retain important

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279. *See supra* Section III.A.1.

280. *Establishing Investment Funds in the Cayman Islands: Key Considerations*, DELOITTE 5 (Nov. 2015), https://www2.deloitte.com/content/dam/Deloitte/bm/Documents/financial-services/cayman-islands/establishing-investment-funds-in-the-cayman-islands.pdf [https://perma.cc/VMY5-EFEX]. Directors typically do not exist in domestic hedge funds. As John Morley explains, these "dummy directors" exist in offshore jurisdictions like the Cayman Islands only "because quirks of law in offshore jurisdictions require it." Morley, *Investment Fund*, *supra* note 70, at 1253.

281. Moon, *Tax Havens*, *supra* note 58, at 1089.

282. Brummer, *supra* note 36, at 515.

283. *See* Trachtman, *supra* note 22, at 5–6. Indeed, the existence of negative externalities in the financial contracting context is relatively well known. *See, e.g.*, Kevin E. Davis, *Contracts as Technology*, 88 N.Y.U. L. REV. 83, 97 (2013) ("Contractual innovations can also generate negative externalities. The classic example is that of financial contracts which magnify contracting parties' risk of insolvency and thereby jeopardize their creditors' solvency. In extreme cases, these kinds of innovations can throw entire economies into turmoil.").

probative value in many interjurisdictional cases, it should not categorically dictate how we allocate interjurisdictional lawmaking authority.

Second, we should resist the temptation to isolate policy goals underlying statutes to determine whether a dispute at hand is sufficiently "domestic" to warrant the application of federal statutes.[284] This is the central methodological defect encouraged by the *Morrison* Court's "focus" test, which instructs courts to search for the "objects of the statute's solicitude."[285] For one, instructing courts to decipher the policy behind a statute is often unhelpful because it is almost never clear whether a particular statute's concern "refer[s] to domestic conduct, domestic effect, or any discernable domestic connection."[286] Statutes, often written in majestically general terms,[287] are also difficult, if not impossible, to discern because many are laden with multiple (and some conflicting) goals.[288] The text of the statute typically does little to alleviate this problem. As Professor Lea Brilmayer reminds us, "[I]n the vast majority of cases, legislatures have no actual intent on territorial reach."[289]

To that end, Congress should enact an omnibus statute expressly overruling *Morrison*'s interpretive methodology.[290] As readily acknowledged by the *Morrison* Court, the presumption against extraterritoriality is a canon of statutory interpretation, and not a

284. Decades of domestic choice of law jurisprudence teaches us that it is unproductive to force judges to isolate policy goals to determine the reach of statutes that are textually silent in scope. *See, e.g.*, BRILMAYER, *supra* note 225 , at 43–107; Lea Brilmayer, *Governmental Interest Analysis: A House Without Foundations*, 46 OHIO ST. L.J. 459, 459–61 (1985).

285. Morrison v. Nat'l Austl. Bank Ltd., 561 U.S. 247, 267 (2010).

286. Zachary D. Clopton, *Replacing the Presumption Against Extraterritoriality*, 94 B.U. L. REV. 1, 15 (2014).

287. ROOSEVELT, *supra* note 182, at 46.

288. Robert A. Katzmann, *Statutes*, 87 N.Y.U. L. REV. 637, 680 (2012) ("It is unreasonable to expect Congress to anticipate all interpretive questions [about a statute] that may present themselves in the future."); *see also* ROOSEVELT, *supra* note 182, at 57 ("It is hard to be confident about exactly what the legislature aimed to achieve, and in fact legislatures probably often have multiple and perhaps conflicting goals.").

289. Brilmayer, *Legislative Intent*, *supra* note 210, at 393 (emphasis omitted); *see also* Symeon C. Symeonides, *The Choice-of-Law Revolution Fifty Years After Currie: An End and a Beginning*, 2015 U. ILL. L. REV. 1847, 1857 ("[S]tatutes that expressly declare their intended territorial reach are the exception rather than the rule.").

290. Examples of omnibus statutes overriding statutory interpretation decisions of federal courts include "reconciliation statutes, statutory reform efforts, and recodifications." William N. Eskridge, Jr., *Overriding Supreme Court Statutory Interpretation Decisions*, 101 YALE L.J. 331, 338 (1991).

constraint on congressional power.[291] Thus, Congress could override *Morrison*'s interpretive methodology through legislation.[292]

In lieu of *Morrison*'s extraterritoriality test, Congress should institute a more flexible test requiring courts to determine the scope of federal statutes by contextually and collectively weighing all connecting factors of each case.[293] Under this test, courts can weigh the relevant connecting factors (e.g., the place of injury, the place of conduct, the location of the decisionmakers) collectively to determine whether the United States has a sufficiently significant interest in applying its laws to a particular dispute at hand.[294] This form of "aggregate contacts" test allows courts to progressively develop case law that adapts to new forms of cross-border commercial transactions that will continue to challenge territorially defined laws. While there will inevitably be difficult cases that require courts to weigh international comity concerns, this type of test allows courts to at least smoke out "easy cases"—that is, those where no foreign jurisdiction actually has a sufficient factual nexus with a particular case to warrant the nonapplication of federal statutes. As applied to the offshore finance context, for instance, it would allow courts to avoid the absurd result of a case with overwhelming factual connections to the United States (and no risk of conflict with foreign law) being dismissed as an "extraterritorial" transaction.[295]

To the extent that *Morrison*'s interpretive methodology remains good law, it is important to bear in mind that not all hope is lost under

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291. Morrison v. Nat'l Austl. Bank Ltd., 561 U.S. 247, 255 (2010) (describing the presumption against extraterritoriality as a "canon of construction . . . rather than a limit upon Congress's power to legislate").

292. *See* Matthew R. Christiansen & William N. Eskridge, Jr., *Congressional Overrides of Supreme Court Statutory Interpretation Decisions, 1967-2011*, 92 TEX. L. REV. 1317, 1317 (2014) (observing that Congress "could alter a judicial construction with a statutory amendment").

293. One method of doing so would be to instruct courts to apply federal law when the United States has "the most significant relationship" to a dispute laden with both domestic and foreign factual elements. This method, of course, is not entirely new. It adopts a version of state law "extraterritoriality" jurisprudence advocated by prominent scholars in the domestic choice of law context. *See* Lea Brilmayer, *Hard Cases, Single Factor Theories, and a Second Look at the Restatement 2D of Conflicts*, 2015 U. ILL. L. REV. 1969, 1977 (2015); Brilmayer, *supra* note 210, at 145.

294. This method of determining the scope of law draws on modern conflict of laws theory that recommend state courts apply the law of a jurisdiction with the "most significant relationship" to the case. *See, e.g.*, RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 145, 188 (AM. LAW INST. 1971).

295. Abandoning the *Morrison* test, for instance, would allow courts to apply U.S. securities law in cases where significant conduct and harm occurred in the United States. In many ways, the conduct and effects tests employed by the Second Circuit in securities cases prior to *Morrison* reflect one version of what an aggregate contact test might look like. *See, e.g.*, Itoba Ltd. v. Lep Group PLC, 54 F.3d 118, 122 (2d Cir. 1995) (allowing application of the Exchange Act where an admixture or combination of conduct and effects suggest "sufficient United States involvement to justify the exercise of jurisdiction by an American court").

the Supreme Court's new extraterritoriality test. As others have observed, the "focus" test is a notoriously "standardless concept."[296] The test, which has also been described as "entirely circular,"[297] is summed up by a federal judge in Pennsylvania adjudicating a civil RICO claim after *Morrison*: "Reflexive reference to the term 'focus' is unhelpful, as a statute could be described as concentrated on the activities it criminalizes . . . or on the entity or person it seeks to protect, or on a blend of both, and all three options may be accurate depending on context."[298]

A standardless concept, on the flip side, provides opportunities. In particular, federal statutes devoid of direct Supreme Court precedent on their extraterritorial scope leave the door open for lower court judges to broadly construe the "focus" of statutory concerns, thereby enabling them to more holistically examine the connecting factors of a case. Consider the *Madoff* case presided by Judge Rakoff discussed earlier.[299] In that case, Judge Rakoff concluded that the "focus" of the U.S. Bankruptcy Code's fraudulent transfer laws was on the " 'property transferred' and the fact of its transfer, not the debtor."[300] But the "focus" of fraudulent transfer laws could be more broadly understood to concern the improper depletion of a domestic bankruptcy estate's assets.[301] Indeed, this is what Judge Burton Lifland concluded in a related case.[302] This type of broad construction of a statute's solicitude, which doctrinally comports with *Morrison*'s generic guidance to search for the "objects of the statute's solicitude,"[303] may help lower courts avoid reaching results that facilitate the private evasion of important regulatory statutes. Without congressional override, however, there is

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296. Brilmayer, *New Extraterritoriality*, *supra* note 108, at 660 (describing the "focus" test as "a standardless concept").

297. Franklin A. Gevurtz, *Determining Extraterritoriality*, 56 WM. & MARY L. REV. 341, 345–46 (2014):

> [T]he test [is] entirely circular because the purpose of asking whether the claim involves extraterritoriality is to decide whether to invoke the presumption as a means to determine Congress's intent. The circularity of the statutory focus test renders the presumption against extraterritoriality useless except in easy cases in which none of the challenged conduct or its effect occurs in the United States.

298. *In re* Le-Nature's, Inc., No. 9-1445, 2011 WL 2112533, at *2 n.3 (W.D. Pa. May 26, 2011).

299. *See supra* Section II.B.1.

300. Sec. Inv'r Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC, 513 B.R. 222, 227 (Bankr. S.D.N.Y. 2014) (quoting 11 U.S.C. § 550(a) (2012)).

301. *See* Morrison, *Extraterritorial Avoidance*, *supra* note 134, at 169.

302. *See* Sec. Inv'r Prot. SIPA Liquidation Corp. v. Bernard L. Madoff Inv. Sec. LLC, 480 B.R. 501, 524 (Bankr. S.D.N.Y. 2012) ("As demonstrated by the text and structure of the avoidance and recovery sections of the Code, their focus is on the improper depletion of the bankruptcy estate's assets.").

303. Morrison v. Nat'l Austl. Bank Ltd., 561 U.S. 247, 267 (2010).

only so much that judges can do to come up with sensible "extraterritoriality" solutions.

CONCLUSION

Capital mobility enabled by technological advancements enhances the ability of private actors to shift the locus of financial transactions outside of any particular jurisdiction. Indeed, it is this mobility that enabled states to compete for corporate charters in the domestic corporate law context.[304] But any claim suggesting that offshore finance is beyond the regulatory reach of the United States is exaggerated at best, given that shifting property and human capital entirely offshore is a significant enterprise. At least in the near future, nation states "still wield total formal authority over resources and capabilities in their territories."[305]

A cramped vision of domestic interest embraced by recent U.S. Supreme Court opinions on the spatial reach of federal statutes seems to romanticize old-fashioned territorialism that received the scholarly burial it deserved in the mid-twentieth century. But this line of jurisprudence should be more alarming than ever before. In today's world, territorially tethered laws promise not only to produce arbitrary results but also risk breeding a cottage industry of private regulatory evasion.[306] The emergence of the offshore world, in many cases, has less to do with respecting the interests of foreign sovereigns than with private entities bootstrapping foreign sovereign interests in the name of building and expanding the ever-more unregulated juridical spaces to conduct modern financial transactions.

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304. Tung, *supra* note 28, at 45–46 ("Legislatures could not afford to . . . driv[e] business out of state to the detriment of local interests.").

305. Brummer, *supra* note 36, at 524.

306. *See, e.g.*, Avi-Yonah, *supra* note 79, at 1575 (attributing international tax competition to the mobility of capital, which resulted from "technological advances as the electronic transfer of funds and the relaxation of exchange controls").