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No. 08-1191

IN THE
Supreme Court of the United States

ROBERT MORRISON, individually and on behalf of all others similarly situated, RUSSELL LESLIE OWEN, BRIAN SILVERLOCK and GERALDINE SILVERLOCK,
Petitioners,

v.

NATIONAL AUSTRALIA BANK LTD., HOMESIDE LENDING INC., FRANK CICUTTO, HUGH HARRIS, KEVIN RACE and W. BLAKE WILSON,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF OF *AMICI CURIAE*, PROFESSORS AND STUDENTS OF THE YALE LAW SCHOOL CAPITAL MARKETS AND FINANCIAL INSTRUMENTS CLINIC, IN SUPPORT OF RESPONDENTS

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BRIEF OF PROFESSORS AND STUDENTS OF THE YALE LAW SCHOOL CAPITAL MARKETS AND FINANCIAL INSTRUMENTS CLINIC AS *AMICI CURIAE* IN SUPPORT OF RESPONDENTS

Professors and Students of the Yale Law School Capital Markets and Financial Instruments Clinic respectfully submit this brief as *Amici Curiae* in support of Respondent.[1]

INTEREST OF *AMICI CURIAE*

Amici are professors and students at Yale Law School who are members of the Capital Markets and Financial Instruments Clinic. The Clinic is a collaborative effort of students and faculty to generate comment letters regarding proposed financial regulations and *Amicus* briefs in pending cases involving corporate governance and capital markets.

Amici have no financial interest in Respondents or direct personal interest in the case. They file this brief because the Second Circuit's decision and parties' briefs fail to address important concerns

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[1] Pursuant to Rule 37.6, no counsel for a party authored this brief in whole or in part, and no such counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than the *Amici Curiae*, or its counsel, made a monetary contribution to its preparation or submission. Letters from the parties consenting to the filing of all *Amici* briefs have been filed with the Clerk of the Court.

related to the extraterritorial application of the fraud-on-the-market doctrine at issue. Failure to address these concerns could result in Supreme Court precedent with detrimental effects on global capital markets and the U.S. federal court system.

SUMMARY OF ARGUMENT

This case presents the Supreme Court with a question of first impression, namely, whether to extend the fraud-on-the-market doctrine to class actions in which plaintiffs purchased securities on overseas exchanges. The fraud-on-the-market doctrine allows plaintiffs in class action suits under 17 C.F.R. § 240.10b-5 ("Rule 10b-5") to proceed without ever proving that they directly relied on the defendant's misrepresentation or omission when purchasing securities. Importantly, most countries have not adopted the doctrine, and it only applies to securities transactions on efficient markets supported by robust regulatory regimes.

Petitioners, Respondents, and the Second Circuit's decision all overlook the critical importance of this doctrine to the case at bar. Although the Plaintiff-Petitioners' complaint rests on the fraud-on-the-market doctrine, Petitioners' brief at this stage of litigation omits mention of the doctrine entirely. Respondents, meanwhile, mention the fraud-on-the-market dimension of this case only in passing. And although the Second Circuit sided with Respondents, its refusal to articulate any "bright-line" rules regarding extraterritorial application of Rule 10b-5 left open the possibility that future plaintiffs would be able to assert fraud-on-the-

market claims arising out of foreign securities transactions.

Amici believe that, in the interest of international comity, the Court cannot ignore the fraud-on-the-market dimension of the instant case. We urge the Court to adopt a bright-line rule that the fraud-on-the-market doctrine does not extend to securities transactions on foreign exchanges. This holding would be consistent with four decades of Rule 10b-5 jurisprudence in the circuit courts up until the Second Circuit's *Morrison* decision.

On the one hand, we are mindful of Judge Friendly's concern that too narrow a construction of the Securities Exchange Act's geographic scope would allow the U.S. to become a base for transnational fraudulent activity. On the other hand, any extraterritorial application of the fraud-on-the-market doctrine sets U.S. courts on a collision course with the substantive laws of other sovereign states. Worse yet, it would force U.S. courts to serve as "schoolmasters" for global capital markets—giving pass-or-fail grades to the regulatory regimes of other countries. A bright-line rule restricting the fraud-on-the-market doctrine to domestic exchanges would address these comity concerns without generating any risk that the U.S. would become a safe haven for securities scammers.

Since the fraud-on-the-market doctrine is a necessary component of Petitioners' claim for relief, their claim can only succeed if the doctrine applies to securities transactions on foreign exchanges. The doctrine does not apply. As a result, Respondents

properly moved to dismiss this suit for failure to state a claim, and the District Court's dismissal of the suit should be affirmed.

ARGUMENT

I. Petitioners' Claim For Relief Requires The Supreme Court to Extend Fraud-on-The-Market Doctrine To Securities Transactions On Foreign Exchanges

In a private cause of action under Rule 10b-5, "[r]eliance by the plaintiff upon the defendant's deceptive acts is an essential element" of a plaintiff's claim for relief. *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta, Inc.*, 552 U.S. 148, 159 (2008). "Reliance provides the requisite causal connection between a defendant's misrepresentation and a plaintiff's injury." *Basic, Inc. v. Levinson*, 485 U.S. 224, 243 (1988).

The "fraud-on-the-market" doctrine provides that on efficient stock exchanges, "[a]n investor who buys or sells stock at the price set by the market does so in reliance on the integrity of that price. Because most publicly available information is reflected in the market price, an investor's reliance on any public material misrepresentations . . . may be presumed for purposes of a Rule 10b-5 action." *Id.* at 247. Unlike the United States, most jurisdictions have not adopted the fraud-on-the-market doctrine.[2]

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[2] *See, e.g.*, *Carom v. Bre-X Minerals Ltd.*, 41 O.R. 3d 780, 793 (Ont. Ct. Gen. Div. 1998) ("there is no support in the common law for the plaintiffs' assertion that a presumption of reliance

In their claim for relief under Rule 10b-5, Plaintiff-Petitioners allege that they "have suffered substantial damages in that, in reliance on the integrity of the market, they paid artificially inflated prices for N[ational] A[ustralia] B[ank] securities . . . ." Pls.' Br. 47. But this harm occurred on an *Australian* rather than an American stock exchange. Thus, unless the Supreme Court extends the fraud-on-the-market doctrine to other jurisdictions' exchanges, Petitioners have failed to meet the reliance requirement of a private cause of action under Rule 10b-5 and therefore failed to state a claim for which relief can be granted.[3]

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may arise as a matter of law"); Eilís Ferran, *Are US-style Investor Suits Coming to the UK?*, 9 J. Corp. L. Stud. 315, 327 (2009) (noting that "[t]he classic 'fraud on the market' theory developed in US securities law . . . has not been adopted" in the UK); *Id.* at 336 (noting that "fraud on the market doctrine has not been adopted in Australia"); Hans Tjio, *Enforcing Corporate Disclosure*, 2009 Sing. J. Legal Stud. 332, 349 (2009) (noting that Singapore has not adopted fraud-on-the-market theory); Theodor Baums & Kenneth E. Scott, *Taking Shareholder Protection Seriously? Corporate Governance in the United States and Germany*, 53 Am. J. Comp. L. 31, 71 n.89 (2005) (contrasting the German requirement of actual reliance with the U.S. fraud-on-the-market doctrine); Hubert De Vauplane & Odile Simart, *The Concept Of Securities Manipulation And Its Foundations in France and the USA*, 23 Brook. J. Int'l L. 203 (1997) (noting that the fraud-on-the-market doctrine has not been adopted in France).

[3] At the district court level, Defendant-Respondents moved to dismiss the complaint of the Plaintiff-Petitioners for lack of subject matter jurisdiction under Fed. R. Civ. P. 12(b)(1) and for failure to state a claim under Fed. R. Civ. P. 12(b)(6). *In re Nat'l Austl. Bank Sec. Litig.*, 2006 U.S. Dist. LEXIS 94162, at *3 (S.D.N.Y. Oct. 25, 2006). Regardless of whether the claim survives on 12(b)(1) grounds, it fails on

II. A Bright Line Rule Limiting The Fraud-On-The-Market Doctrine To Domestic Exchanges Would Be Consistent With Four Decades of Circuit Court Jurisprudence

A. The circuit courts' standards for the geographic scope of Rule 10b-5 were not developed with fraud-on-the-market in mind

The extraterritorial application of Rule 10b-5 grew out of a set of Second Circuit decisions written by Judge Friendly that did not involve the fraud-on-the-market doctrine. Indeed, they came years before the Supreme Court first allowed fraud-on-the-market claims in *Basic, Inc.* *See Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974 (2d Cir. 1975) (Friendly, C.J.); *Leasco Data Processing Equip. Corp. v. Maxwell*, 468 F.2d 1326 (2d Cir. 1972) (Friendly, C.J.). *See also Schoenbaum v. Firstbrook*, 405 F.2d 200 (2d Cir. 1968).

Other circuits' decisions extending the extraterritorial reach of 10b-5 also did not involve the fraud-on-the-market doctrine. Most came down before *Basic, Inc.* *See Zoelsch v. Arthur Andersen & Co.*, 824 F.2d 27 (D.C. Cir. 1987); *Tamari v. Bache & Co. (Lebanon) S.A.L.*, 730 F.2d 1103 (7th Cir. 1984); *Grunenthal GmbH v. Hotz*, 712 F.2d 421 (9th Cir. 1983); *Cont'l Grain (Austl.) Pty. Ltd. v. Pac. Oilseeds, Inc.*, 592 F.2d 409 (8th Cir. 1979); *SEC v. Kasser*, 548 F.2d 109 (3d Cir. 1977). While the Fifth

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12(b)(6) grounds if the fraud-on-the-market doctrine is not extended to foreign exchanges.

Circuit adopted its standard for the extraterritorial application of Rule 10b-5 after *Basic, Inc.*, it also did so outside the fraud-on-the-market context. *See Robinson v. TCI/US W. Commc'ns*, 117 F.3d 900, 903 (5th Cir. 1997) (in which the England-based plaintiff-appellant alleged that U.S. defendants deliberately defrauded him of a $9 million interest in a settlement agreement).

B. The concerns that led circuit courts to extend the reach of Rule 10b-5 do not apply to the fraud-on-the-market doctrine

Although "[t]he circuits are divided as to precisely what sort of activities" abroad might give rise to Rule 10b-5 claims, "all agree that . . . Congress did not want 'the United States to be used as a base for manufacturing fraudulent security devices for export, even when they are peddled only to foreigners.'" *Robinson*, 117 F.3d at 905 (citing *IIT v. Vencap, Ltd.*, 519 F.2d 1001, 1017 (2d Cir. 1975) (Friendly, C.J.)). *See also Cont'l Grain*, 592 F.2d at 420 (quoting Friendly and acknowledging "that the finding . . . in the present case is largely a policy decision"); *Kasser*, 548 F.2d at 114 (holding Friendly's rationale "sets forth a sound proposition . . . which we now adopt"). In *Morrison*, the Second Circuit explained the reasoning behind Friendly's concern: if the United States "decline[s] jurisdiction over all 'foreign-cubed' securities fraud actions," it will "be seen as a safe haven for securities cheaters." *Morrison v. Nat'l Austl. Bank, Ltd.*, 547 F.3d 167, 175 (2d Cir. 2009).

However, this concern does not apply in the

fraud-on-the-market context because almost all other jurisdictions *reject* that doctrine. *See supra* note 2. Countries will not look askance at the U.S. for declining to apply a doctrine that they themselves reject. Under the rule suggested by the *Amici*, foreign plaintiffs would still be able to seek relief in U.S. courts if they have fallen victim to "fraudulent security devices" exported from our shores. All that *Amici* ask is for plaintiffs who present 10b-5 claims arising out of foreign securities transactions to actually allege that they were deceived by these devices. Plaintiff-Petitioners' pleadings in the instant case do not meet this minimal standard.

Petitioners and the *Morrison* panel also overlook Judge Friendly's *own* repeated recommendations that courts apply a different, more stringent standard for the geographic scope of 10b-5 in non-traditional securities class actions. In *Vencap*, Judge Friendly ruled that a U.S. district court could assert jurisdiction over claims brought by Luxembourg-based plaintiffs who alleged that a U.S.-citizen defendant had sought to "spirit[] away" $3 million of plaintiffs' assets. 519 F.2d at 1019. But Judge Friendly cautioned that "[c]lass actions may stand differently" because of "the likelihood that a very small tail" of plaintiffs who prefer to adjudicate the dispute in U.S. courts "may be wagging an elephant" of foreign victims who would prefer to pursue their claims in their home jurisdiction. *Id.* at 1018 n.31. Similarly, in *Bersch,* Judge Friendly warned that "[t]he management of a class action with many thousands of class members imposes tremendous burdens on overtaxed district courts," especially

"when the class members . . . are abroad." 519 F.2d at 996. Fraud-on-the-market class actions—which encompass *all* purchasers of a particular security regardless of whether they actually relied on a defendant's misrepresentation—raise exactly these concerns about "wagging an elephant" and "overtax[ing] district courts." *See infra* note 8.

III. A Bright-Line Rule Limiting Fraud-On-The-Market Doctrine To Domestic Exchanges Would Avoid Clashes Between U.S. And Foreign Law

A. Applying fraud-on-the-market doctrine to foreign exchanges would interfere with the substantive laws of other nations

When "applicable foreign and domestic law provide different substantive rules of decision to govern the parties' dispute," U.S. courts should "refrain from exercising that jurisdiction with respect to a person or activity having connections with another state." *Hartford Fire Ins. Co. v. California*, 509 U.S. 764, 818-821 (Scalia, J., dissenting). Other jurisdictions' decisions not to adopt the fraud-on-the-market doctrine constitute such a difference in substantive law. These jurisdictions did not merely decline to adopt fraud-on-the-market. They deliberately rejected it after careful consideration and reflection.

For instance, New Zealand's Judge Blanchard, in rejecting the fraud-on-the-market doctrine, stated that "the purpose of the [New Zealand Securities Act 1978] is to ensure information is available to

investors, so that they can make their *own* assessment of the prospects of the issuer . . . ." *Boyd Knight v. Purdue*, 1999 NZLR LEXIS 406, at *42 (C.A. Wellington) (emphasis added). Judge Blanchard did *not* want to encourage investors to make financial decisions "without troubling to look at the accounts." *Id.* He found "no attraction in the doctrine of reliance on the integrity of the market which has been developed in some jurisdictions in the United States." *Id.* at *43. Justice La Forest of the Supreme Court of Canada, in explaining his country's decision to reject fraud-on-the-market doctrine, expressed concern that if the theory were incorporated into Canadian case law, the legal costs associated with preparing financial statements "would inevitably swell." *Hercules Mgmt. Ltd. v. Ernst & Young* [1997] 2 S.C.R. 165, 196 (Can.). *See also Carom*, 41 O.R. 3d at 782 (the "doctrine of American law known as fraud on the market theory . . . invokes a presumption unknown up to the present in Canadian law").[4]

It may be true, as the Second Circuit argues, that "governments and other regulators are generally in agreement that fraud should be discouraged. . . . [I]f

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[4] Similarly, "[t]here is no statutory presumption of reliance in relation to actions by shareholders for compensation in Australia." *See* Michael Duffy, *'Fraud on the Market': Judicial Approaches to Causation and Loss From Securities Nondisclosure in the United States, Canada, and Australia*, 29 Melbourne L. Rev. 621, 655 (2005). Although Professor Duffy considers the possibility that Australian courts may allow fraud-on-the-market claims in the future, *see id.* at 664, this is no reason for U.S. courts to preempt a sovereign state's development of its own case law.

our anti-fraud laws are stricter than a foreign state's, that country will surely not be offended by their application." *Morrison*, 547 F.3d at 175 (citing *IIT, Int'l Inv. Trust v. Cornfeld*, 619 F.2d 909, 921 (2d Cir. 1980) (Friendly, C.J.)). But it does not follow that *any* difference in anti-fraud regimes between countries simply reflects "stricter" enforcement in one. In the case of the fraud-on-the-market doctrine, differences between countries explicitly reflect different substantive legal regimes.[5] To impose the American regime on other countries would violate principles of international comity.

B. Applying the fraud-on-the-market doctrine to foreign exchanges would require U.S. courts to pass judgment on other countries' regulatory regimes

Plaintiffs may only rely on the fraud-on-the-market doctrine where they "allege and prove . . . that the shares were traded on an efficient market

[5] The geographic scope of fraud-on-the-market doctrine need not be coextensive with the geographic scope of other Rule 10b-5 claims. "[In cases of] 'core' securities fraud—that is, intentionally deceptive misrepresentation designed to line the pockets of the issuer or some broker or investment adviser—there is little problem in the conclusion that multiple countries could seek to exercise both subject matter and personal jurisdiction. Core fraud is considered to be an evil in all civilized countries . . . ." Donald C. Langevoort, Schoenbaum *Revisited: Limiting the Scope of Antifraud Protection in an Internationalized Securities Marketplace*, 55 Law & Contemp. Probs. 241, 245 (1992). The extraterritorial extension of fraud-on-the-market doctrine is particularly problematic because the doctrine is distinctly American and is *not* adopted by "all civilized countries."

. . . ." *Basic, Inc.*, 485 U.S. at 248 n.27. In an efficient market, "unexpected corporate events or financial releases" generate "an immediate response in the stock price." *Binder v. Gillespie*, 184 F.3d 1059, 1065 (9th Cir. 1999) (citing *Cammer v. Bloom*, 711 F. Supp. 1264, 1287 (D.N.J. 1989)). "This, after all, is the essence of an efficient market and the foundation for the fraud on the market theory." *Cammer,* 711 F. Supp. at 1287.[6]

This criterion can only be satisfied when a security trades on a market governed by an effective regulatory regime. If, for example, a jurisdiction fails to enforce anti-insider-trading laws, prices may not react to the announcement of corporate events or financial releases because corporate insiders who heavily trade their own firm's securities anticipated the announcement or release in advance. *See*, *e.g.*, Arturo Bris, *Do Insider Trading Laws Work?*, 11 Eur. Fin. Mgmt. 267 (2005). Moreover, "in countries that provide poorer protection for public investors," traders may not trust the credibility of corporate disclosures, and this will "impede the capitalization of firm-specific information into stock prices." Randall Morck et al., *The Information Content of Stock Markets: Why Do Emerging Markets Have Synchronous Stock Price Movements?*, 58 J. Fin. Econ. 215, 216-217 (2000) (noting that stock prices in

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[6] This inquiry requires courts not only to look at the characteristics of the "whole market," but also to the "characteristics of the individual stock itself." *Cammer*, 711 F. Supp. at 1281. In applying fraud-on-the-market abroad, then, U.S. courts would have to assess the efficiency of particular foreign exchanges with respect to particular foreign securities.

emerging markets do *not* appear to integrate firm-specific information efficiently).

Thus, the extraterritorial application of the fraud-on-the-market doctrine would require U.S. courts to deem at least some foreign regulatory regimes deficient. Such a statement from a U.S. court surely would offend other countries. *Cf. Nanus Asia Co. Inc. & Anor v. Standard Charter Bank*, [1988] 1 H.K.C. 377 (H.C.) (in which a Hong Kong court took offense at a U.S. district judge's suggestion that Hong Kong's securities regulatory regime was lax).

U.S. courts should not be in the business of deciding whose securities regulations pass muster and whose fall short. They should presume that Congress did not intend U.S. judges to act as schoolmasters for global securities markets — giving high grades to some and failing marks to others. "[P]rescriptive comity . . . is exercised by legislatures when they enact laws, and courts assume it has been exercised when they come to interpreting the scope of laws their legislatures have enacted." *Hartford Fire Ins.*, 509 U.S. at 817 (Scalia, J., dissenting). U.S. courts are instructed to interpret a statute's geographic scope narrowly when "the extra-territorial operation of the statute would impugn foreign law." *Air Line Stewards & Stewardesses Ass'n v. Trans World Airlines, Inc.*, 173 F. Supp. 369, 377 (S.D.N.Y. 1959).[7]

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[7] Petitioners suggest that "[c]oncerns relating to comity can . . . be addressed by application of the *forum non conveniens* doctrine." Pet'rs' Br. 41. *Cf. Warlop v. Lernout*, 473 F. Supp. 2d

Beyond concerns of comity, country-by-country and exchange-by-exchange determinations of market efficiency would severely strain the resources of U.S. federal courts. Proof of a particular market's efficiency would require "[e]xpensive experts with complex equations and long computer printouts." *See* Geoffrey Christopher Rapp, *Proving Markets Inefficient: The Variability of Federal Court Decisions on Market Efficiency in* Cammer v. Bloom *and Its Progeny*, 10 U. Miami Bus. L. Rev. 303, 319-320 (2002). These efficiency tests will be especially challenging to conduct when courts are unfamiliar with the markets at issue.[8] It not only

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260, 263 (D. Mass. 2007) (dismissing foreign plaintiffs' fraud-on-the-market claims against Belgium-based defendants under the doctrine of *forum non conveniens*). However, since Congress never intended the fraud-on-the-market doctrine to apply to foreign securities exchanges, Petitioners' claims do not survive Respondents' motion to dismiss under Fed. R. Civ. P. 12(b)(6) whether the forum is "convenient" or not. Moreover, if fraud-on-the-market suits based on foreign securities transactions necessarily raise comity concerns, as *Amici* argue, then it would be a waste of litigants' and judges' time to delay dismissal at this stage when the suit will be transferred to a foreign court regardless. *Cf. Bowen v. Massachusetts*, 487 U.S. 879, 930 (1988) (Scalia, J., dissenting) ("Nothing is more wasteful than litigation about where to litigate . . . .").

[8] For instance, courts assessing the efficiency of the market for a domestically-traded security generally look to whether a stock has "numerous market makers." *See Cammer*, 711 F. Supp at 1286. But "a trading system based on market makers is the exception rather than the rule outside North America." Hee-Joon Ahn & Yan-Leung Cheung, *The Intraday Patterns of the Spread and Depth in a Market Without Market Makers: The Stock Exchange of Hong Kong*, 7 Pacific-Basic Fin. J. 539, 540 (1999). A U.S. court considering the efficiency of a foreign market would find itself on *terra incognita*, and the guidelines

would be *impolitic* to extend fraud-on-the-market extraterritorially. It would be *impractical* as well.

IV. The Fraud-On-The-Market Doctrine Does Not Apply To ADR Transactions Because The ADR Market Is Not Efficient

At the circuit court level, Plaintiff-Appellants (now Petitioners) cited the fact that National Australia Bank's securities trade as American Depository Receipts (ADRs)[9] on the New York Stock Exchange as a "tipping factor[]" supporting subject matter jurisdiction. Pl-Appellants' Br. 45. *See also* Pet'rs' Br. 5 n.2. Some commentators have suggested that foreign plaintiffs should be able to ride the jurisdictional coattails of domestic ADR purchasers in fraud-on-the-market claims. *See, e.g.,* Hannah L. Buxbaum *Transnational Regulatory Litigation*, 46 Va. J. Int'l L. 251, 282 (2006); Brian P. Murray & Maurice Pesso, *The Accident of Efficiency: Foreign Exchanges, American Depository Receipts, and Space Arbitrage*, 51 Buff. L. Rev. 383 (2003). Petitioners' *Amici* similarly argue that the sale of ADRs based on National Australia Bank's stock should allow a U.S. district court to hear foreign investors' fraud-on-the-market claims. MN Br. 4.

This argument is only tenable if (1) the ADR market operates efficiently and (2) price movements

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that courts use to evaluate efficiency in the domestic context would not necessarily apply.

[9] "ADRs are issued by U.S. depository banks and represent one or more shares of foreign stock or a fraction of a share. If you own an ADR, you have the right to obtain the foreign stock it represents." *Morrison*, 547 F.3d at 168 n.1.

pass seamlessly to and from the ADR and overseas markets. Neither assumption holds true.

First, "[t]he 'fraud on the market' theory rests on the assumption that there is a nearly perfect market in information . . . ." *Peil v. Speiser*, 806 F.2d 1154, 1161 n.10 (3d Cir. 1986). But "because the ADR market is less liquid and tends to have more information asymmetries . . . investors will . . . be less willing to fully react to public announcements." Georgina Benou, *Market Underreaction to Large Stock Price Declines: The Case of ADRs*, 4 J. Behav. Fin. 21, 22 (2003). Moreover, if "[i]nvestors . . . hold ADR stocks for different reasons than the other stocks in their portfolios"—i.e. to diversify risk rather than beat the market rate of return—they may "be hesitant to react once negative news is out." *Id. See also* Diane Deqing Li & Kenneth Yung, *Institutional Herding in the ADR Market*, 23 Rev. Quantitative Fin. & Acct. 5, 16 (2004) (observing that in the ADR market, "past winners continue to be winners, and past losers continue to be losers"—which is inconsistent with market efficiency).

Second, "if the markets are fully efficient and the prices of underlying shares truly affect the prices of ADRs, a shock from the underlying share price should be reflected in the prices of ADRs by the same calendar day." Minho Kim, *et al.*, *Price Transmission Dynamics Between ADRs and Their Underlying Securities*, 24 J. Bank. & Fin. 1359, 1362 (2000). However, ADR prices do not fully integrate shocks to the prices of foreign underlying shares in the first twenty-four hours. *Id.* at 1373. This time lag persists particularly long for ADRs based on Australian

shares. *Id.*

Moreover, it appears that "U.S. investors initially attempt to price the ADRs partly with reference to their own [i.e. U.S.] market, rather than to the foreign market in which the underlying shares trade." *Id.* at 1378. This finding "is inconsistent with . . . market efficiency." Robert B. Durand & Douglas Scott, *iShares Australia: A Clinical Study in International Behavioral Finance*, 12 Int'l Rev. Fin. Analysis 223, 237 (2003) (noting that ADRs of Australian securities track U.S. macro-market movements more than underlying shares). *See also* Junming Hsu & Li-Hwei Tsai, *An Investigation of Information Transmission Between Stocks of Far Eastern Countries and Their American Depository Receipts*, 44 Emerging Markets Fin. & Trade 40, 56 (2008) (finding that price transmission between Asian stock exchanges and the ADR market is "not fully efficient" and that "returns between domestic stocks and their ADRs . . . differ substantially in the short run").

Since (1) ADRs based on a company's overseas stock underreact to available information regarding the company and its business and (2) mechanisms of price transmission to and from overseas and ADR markets operate imperfectly, ADR transactions on U.S. exchanges should not enable foreign or domestic plaintiffs to rely on the fraud-on-the-market doctrine in class-action suits.

In sum, ADR transactions alone cannot support the application of fraud-on-the-market doctrine in the instant case. Thus unless fraud-on-the-market

doctrine applies to foreign securities exchanges, Petitioners have failed to state a claim for which relief can be granted. This Court—in the interest of comity—should rule that the fraud-on-the-market doctrine does not apply to foreign exchanges as a matter of law. Thus Petitioners' claim likewise fails as a matter of law. Since Respondents' motion to dismiss for lack of subject matter jurisdiction was accompanied by a motion to dismiss for failure to state a claim, Respondents should prevail at this stage of the litigation even if the Court accepts all the arguments regarding subject matter jurisdiction asserted in Petitioners' brief.

CONCLUSION

For the foregoing reasons, the lower courts' decisions dismissing Petitioners' claims should be affirmed—albeit on grounds different from those asserted in the Second Circuit's opinion.

Respectfully submitted.

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