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Enforcement of Securities Law in the Global Marketplace: Cross-Border Cooperation in the Prosecution of Transnational Hedge Fund Fraud

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ENFORCEMENT OF SECURITIES LAW IN THE GLOBAL MARKETPLACE: CROSS-BORDER COOPERATION IN THE PROSECUTION OF TRANSNATIONAL HEDGE FUND FRAUD

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INTRODUCTION: THE GROWTH OF HEDGE FUND FRAUD

Over the last few decades, the global hedge fund industry has grown at a surprising rate.[1] In 2007, more than 10,000 hedge funds ran their business in the global marketplaces, and they collectively managed US$2.150 trillion.[2] Although the hedge fund industry declined in 2008 due to the financial crisis, its recovery is well in progress now.[3] Indeed, the number of hedge funds in operation in 2010 reached 9500, and their total assets under management were US$1.920 trillion.[4]

As the hedge fund industry has expanded, securities law violations by hedge fund managers have also increased.[5] Such se-

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1. George Sami, Comment, *A Comparative Analysis of Hedge Fund Regulation in the United States and Europe*, 29 NW. J. INT'L L. & BUS. 275, 275 (2009).

2. MARKO MASLAKOVIC, THECITYUK, HEDGE FUNDS 2 (2011), *available at* http://www.thecityuk.com/assets/Uploads/Hedge-funds-2011.pdf.

3. *See id.* at 1.

4. *Id.* at 1–2.

5. Linda Chatman Thomsen et al., *Hedge Funds: An Enforcement Perspective*, 39 RUTGERS L.J. 541, 555–56 (2008); *see also* Paul M. Jonna, Comment, *In Search of Market Discipline: The Case for Indirect Hedge Fund Reg-*

curities law violations can significantly impair the integrity of the market and threaten the confidence of investors. In recent years, the U.S. Securities and Exchange Commission ("U.S. SEC" or "SEC") has filed a number of enforcement actions against hedge funds and their managers.[6] For example, in 2009 the SEC and the U.S. Department of Justice ("U.S. DOJ" or "DOJ") initiated their enforcement proceedings against Raj Rajaratnam, a hedge fund manager, for insider trading.[7] As one of the biggest insider trading rings on record,[8] his fraud produced millions of dollars in illegal benefits.[9] Moreover, Rajaratnam's scheme affected securities from various major companies, including Google, Hilton, and Intel to name a few.[10] In light of these negative effects, securities regulators have called for strict enforcement for hedge fund fraud.[11]

Despite the need for strict enforcement, securities regulators often face difficulties in combating hedge fund fraud. Hedge funds can make fraudulent schemes more difficult to detect due

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ulation, 45 SAN DIEGO L. REV. 989, 1008 (2008); *see also* SEC, IMPLICATIONS OF THE GROWTH OF HEDGE FUNDS 72–75 (2003), *available at* http://www.sec.gov/news/studies/hedgefunds0903.pdf [hereinafter 2003 SEC STAFF REPORT].

6. Thomsen et al., *supra* note 5, at 555–56.

7. *See* Complaint at 1, SEC v. Galleon Mgmt. LP, 274 F.R.D. 120 (S.D.N.Y. 2011) (No. 09 Civ. 8811) (JSR) (Oct. 16, 2009), *available at* http://www.sec.gov/litigation/complaints/2009/comp21255.pdf; *see also* Complaint at 1, United States v. Rajaratnam, No. 09 MAG 2306 (S.D.N.Y. Oct. 15, 2009), *available at* http://www.justice.gov/usao/nys/hedgefund/rajaratnamrajetalcomplaint.pdf.

8. Azam Ahmed & Guibert Gates, *The Galleon Network*, N.Y. TIMES (May 11, 2011), http://www.nytimes.com/interactive/2011/03/08/business/galleon-graphic.html; Press Release, U.S. Attorney's Office S.D.N.Y., Hedge Fund Billionaire Raj Rajaratnam Found Guilty in Manhattan Federal Court of Insider Trading Charges 1 (May 11, 2011), *available at* http://www.justice.gov/usao/nys/pressreleases/May11/rajaratnamrajverdictpr.pdf; SEC v. Rajaratnam, 822 F. Supp. 2d 432, 434 (S.D.N.Y. 2011); United States v. Rajaratnam, 802 F. Supp. 2d 491 (S.D.N.Y. 2011).

9. Press Release, SEC, SEC Obtains Record $92.8 Million Penalty Against Raj Rajaratnam (Nov. 8, 2011), http://www.sec.gov/news/press/2011/2011-233.htm.

10. Litigation Release No. 21284, SEC, SEC Charges 13 Additional Individuals and Entities in Galleon Insider Trading Case (Nov. 5, 2009), *available at* http://www.sec.gov/litigation/litreleases/2009/lr21284.htm.

11. *See* 2003 SEC STAFF REPORT, *supra* note 5, at 72–75; *see also* Thomsen et al., *supra* note 5, at 555.

to the complexity of the fund structures and operations.[12] Indeed, as the hedge fund industry has expanded beyond borders, securities fraud involving hedge funds has also become transnational.[13] For instance, even if hedge fund managers are working in the United States or United Kingdom ("U.K."), the hedge funds themselves are often located in tax havens of less-regulated countries.[14] Furthermore, certain managers operate both domestic and offshore funds at the same time.[15]

In order to respond to the global expansion of securities fraud, including hedge fund fraud, domestic securities regulators must act transnationally.[16] With no single regulatory scheme to govern all global markets, each country has sought to apply its domestic laws extraterritorially to combat transnational securities fraud;[17] however, in order to enforce domestic securities laws that reach extraterritorially, regulators need to secure assistance from foreign authorities.[18] Because enforcement of law is limited within a territory, domestic regulators cannot generally use their enforcement power within the terri-

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12. *See* Thomas C. Pearson, *When Hedge Funds Betray a Creditor Committee's Fiduciary Role: New Twist on Insider Trading in the International Financial Markets*, 28 REV. BANKING & FIN. L. 165, 175–76 (2008).

13. *See Hedge Funds in the Crosshairs: The Year in Review*, 41 SEC. REG. & L. REP. (BNA) No. 519 (Mar. 23, 2009), *available at* http://www.gibsondunn.com/publications/Documents/Goldsmith-Ahn-Boone-HedgeFundsInTheCrosshairs.pdf [hereinafter *Hedge Funds in the Crosshairs*].

14. *See* Thomas C. Pearson & Julia Lin Pearson, *Protecting Global Financial Market Stability and Integrity: Strengthening SEC Regulation of Hedge Funds*, 33 N.C. J. INT'L L. & COM. REG. 1, 26–27 & n.145 (2007) (quoting FIN. SERVS. AUTH., HEDGE FUNDS AND THE FSA: FEEDBACK STATEMENT ON DP16, 6 (2003), *available at* http://www.fsa.gov.uk/pubs/discussion/fs16.pdf); *see also* 2003 SEC STAFF REPORT, *supra* note 5, at 10; *see also* FRANÇOIS-SERGE LHABITANT, HANDBOOK OF HEDGE FUNDS 87–88 (2006).

15. *See* LHABITANT, *supra* note 14, at 108–11 (explaining mirror structures and master-feeder structures).

16. *See* Kun Young Chang, *Multinational Enforcement of U.S. Securities Laws: The Need for the Clear and Restrained Scope of Extraterritorial Subject-Matter Jurisdiction*, 9 FORDHAM J. CORP. & FIN. L. 89, 90 (2003).

17. *See id.* at 90–91.

18. J. WILLIAM HICKS, INTERNATIONAL DIMENSIONS OF U.S. SECURITIES LAW § 11:53 (2012); *see also* Sec. & Futures Comm'n, 58 ENFORCEMENT REP. 6, 7 (2008), *available at* http://www.sfc.hk/sfc/doc/EN/speeches/public/enforcement/08/may_08.pdf.

tory of other countries.[19] The regulators, therefore, have to obtain cooperation from other countries, particularly when they enforce their own laws against fraud involving cross-border transactions.[20]

Recognizing the territorial limits on enforcement power, many jurisdictions provide a legislative framework for authorizing domestic securities regulators to assist foreign authorities.[21] Based on these pieces of legislation, securities regulators entered into international networks to execute cross-border assistance.[22] Popular networks for international securities enforcement include Memoranda of Understanding ("MOUs") and Mutual Legal Assistance Treaties ("MLATs").[23] Since 1982, the SEC has signed a number of bilateral MOUs with different foreign authorities.[24] Since 2002, the International Organization of Securities Commissions ("IOSCO") also has promoted a multilateral MOU ("IOSCO MMOU" or "MMOU"),[25] listing ninety-seven authorities as full signatories.[26] In addition to the MOUs, the United States currently has a number of MLATs with vari-

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19. INT'L BAR ASS'N, REPORT OF THE TASK FORCE ON EXTRATERRITORIAL JURISDICTION 9–10 (2009), *available at* http://www.ibanet.org/Document/Default.aspx?DocumentUid=ECF39839-A217-4B3D-8106-DAB716B34F1E.

20. HICKS, *supra* note 18, § 11:53; *see also* Sec. & Futures Comm'n, *supra* note 18, at 7.

21. Felice B. Friedman et al., *Taking Stock of Information Sharing in Securities Enforcement Matters*, 10 J. FIN. CRIME 37, 40–41 (2002); *see also* HICKS, *supra* note 18, § 11:54.

22. Friedman et al., *supra* note 21, at 41.

23. *See* OFFICE OF INT'L AFFAIRS, SEC, INTERNATIONAL COOPERATION IN SECURITIES LAW ENFORCEMENT 3–4 (2004), *available at* http://www.sec.gov/about/offices/oia/oia_enforce/intercoop.pdf (last visited Mar. 19, 2012).

24. *Cooperative Arrangements with Foreign Regulators*, SEC, http://www.sec.gov/about/offices/oia/oia_cooparrangements.shtml (last visited Feb. 28, 2012).

25. *International Enforcement Assistance*, SEC OFFICE OF INT'L AFFAIRS, http://www.sec.gov/about/offices/oia/oia_crossborder.shtml (last visited Sept. 10, 2011) [hereinafter *SEC International Enforcement Assistance*].

26. *IOSCO MMOU: Current Signatories - 97*, IOSCO, http://www.iosco.org/library/index.cfm?section=mou_siglist (last visited Nov. 12, 2013) [hereinafter *Current Signatories*]. Currently, twenty-three authorities "have committed to seeking the legal authority necessary to enable them to become full signatories to the IOSCO MMOU." *Id*.

ous foreign countries.[27] Despite these efforts, current network mechanisms promoting cooperation have not been effective in combatting multinational hedge fund fraud. In particular, although many securities regulators across the world have sought to cooperate through international networks, defects in the network mechanisms themselves and a lack of domestic legal authority impede effective cooperation among regulators.

In seeking how to overcome these obstacles, this article will explore ways that promote international cooperation in detecting, investigating, and prosecuting cross-border hedge fund fraud. In particular, it will describe the trends toward globalization of hedge fund fraud. Next, it will discuss how to enforce national securities laws cooperatively by using international network mechanisms. Finally, this study will provide recommendations for reforming the international securities enforcement system, thereby achieving more effective cooperation in combatting hedge fund fraud.

I. AN ANALYSIS OF RECENT ENFORCEMENT ACTIONS REGARDING HEDGE FUNDS AND THEIR MANAGERS

A. Overview

Securities fraud schemes employed by hedge fund managers are not unique to the hedge fund context.[28] Most commonly, securities violations committed by hedge fund professionals fall into traditional fraud categories; however,[29] hedge fund managers are more easily enticed to employ fraudulent schemes

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27. DIV. OF ENFORCEMENT, SEC, ENFORCEMENT MANUAL § 3.3.6.3 (2011), *available at* http://www.sec.gov/divisions/enforce/enforcementmanual.pdf; *see also* Treaty on Mutual Assistance in Criminal Matters, U.S.-Switz., May 25, 1973, 27 U.S.T. 2019 (entered into force on Jan. 23, 1977) [hereinafter U.S.-Switz. MLAT]; *see also* Treaty on Mutual Legal Assistance in Criminal Matters, U.S.-Can., Mar. 18, 1985, S. TREATY DOC. NO. 100-14 [hereinafter U.S.-Can. MLAT]; *see also* Treaty on Mutual Legal Assistance in Criminal Matters, U.S.-U.K., Jan. 6, 1994, 1994 U.S.T. 205 (1995) (entered into force on Dec. 2, 1996) [hereinafter U.S.-U.K. MLAT]; *see also* Agreement on Mutual Legal Assistance in Criminal Matters, U.S.-H.K., Apr. 15, 1997, 1997 U.S.T. 115 (1997) (entered into force on Jan. 21, 2000) [hereinafter U.S.-H.K. MLAT]; *see also* Treaty on Mutual Legal Assistance in Criminal Matters, U.S.-S. Korea, Nov. 23, 1993, 1993 U.S.T. 135 (1995) (entered into force on May 23, 1997) [hereinafter U.S.-S. Korea MLAT].

28. 2003 SEC STAFF REPORT, *supra* note 5, at 73.

29. *See id*. at 73–74; Thomsen et al., *supra* note 5, at 555.

because they have the motive and ability to do so.[30] For example, they routinely handle a large amount of money,[31] employ high risk investment strategies,[32] are compensated based on their performance,[33] operate funds largely at their discretion,[34] have close connections with other financial entities,[35] and have a favorable environment to engage in misrepresentation.[36] Possible violations may include misappropriation of funds, insider trading, and market manipulation.[37]

Hedge funds tend to make fraudulent schemes more difficult to detect due to the complexity of the fund structures and operations.[38] Most importantly, as the hedge fund industry has expanded beyond national borders, securities fraud involving hedge funds has also become transnational.[39] For example, although many hedge fund managers work in the United States or U.K., the hedge funds themselves are often located outside these countries in order to maximize the tax benefits and lower regulatory compliance costs.[40] Furthermore, certain managers operate both domestic and offshore funds at the same time.[41] Such multinational hedge funds are generally set up as a mirror structure or a master-feeder structure.[42] In the course of the operation, the multinational fund managers conduct for-

30. *See* Richard Strohmenger, Note, *Insider Trading and Hedge Funds: A Dangerous Pair*, 15 FORDHAM J. CORP. & FIN. L. 523, 532–34 (2010).

31. *See* 2003 SEC STAFF REPORT, *supra* note 5, at 73.

32. Strohmenger, *supra* note 30, at 533.

33. Thomsen et al., *supra* note 5, at 558; *see also* WULF ALEXANDER KAAL, HEDGE FUND REGULATION BY BANKING SUPERVISION – A COMPARATIVE INSTITUTIONAL ANALYSIS 24 (2006).

34. *See* 2003 SEC STAFF REPORT, *supra* note 5, at 73; *see also* Thomsen et al., *supra* note 5, at 557, 567; DOUGLAS L. HAMMER ET AL., U.S. REGULATION OF HEDGE FUNDS 273 (2005).

35. Pearson, *supra* note 12, at 175.

36. *See* Thomsen et al., *supra* note 5, at 558–59.

37. *See id*. at 542.

38. *See* Pearson, *supra* note 12, at 175–76.

39. *See Hedge Funds in the Crosshairs*, *supra* note 13.

40. *See* Pearson & Pearson, *supra* note 14, at 26–27 & n.145 (quoting FIN. SERVS. AUTH., *supra* note 14, at 6); *see also* 2003 SEC STAFF REPORT, *supra* note 5, at 10; *see also* FIN. SERVS. AUTH., *supra* note 14, at 6; *see also* LHABITANT, *supra* note 14, at 87–88.

41. LHABITANT, *supra* note14, at 108–11 (explaining mirror structures and master-feeder structures).

42. *See id*.

eign or cross-border transactions.[43] Furthermore, hedge fund managers often use Internet communication and networking to expand their businesses worldwide.[44]

Given the circumstances, securities fraud committed by hedge fund managers has become largely transnational.[45] The trend toward the internationalization of hedge fund frauds has become particularly evident in enforcement actions targeting misappropriation, insider trading, and market manipulation.

B. Misappropriation and Hedge Funds

Misappropriation of funds entails "the application of another's property or money dishonestly to one's own use."[46] Motives to misappropriate hedge funds may vary among managers. Some may manage the funds in a legitimate manner at the beginning of their operation, deciding later to employ a fraudulent scheme when encountering financial difficulty.[47] Others, however, may create a hedge fund entity solely for the purpose of misusing investors' money for their own sake.

If so inclined, hedge fund managers are able to commit misappropriation because they operate with a large amount of money in day-to-day investment.[48] Furthermore, managers can avoid investors' surveillance simply by misrepresenting the profitability of the funds.[49] Investors may not suspect misappropriation if the fund looks profitable on paper.[50] For this reason, when managers misappropriate hedge fund assets, they

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43. *See id.* at 109–10 (explaining the transfer of funds).

44. *See, e.g.*, Complaint at 4–5, 8, 45–51, SEC v. Ficeto, CV–11–1637 GHK (RZx) (C.D. Cal. Feb. 24, 2011), *available at* http://www.sec.gov/litigation/complaints/2011/comp21865.pdf [hereinafter Ficeto Complaint] (addressing the Internet communication between Colin Heatherington, a Canadian resident, and Tony Ahn, an American resident).

45. *See Hedge Funds in the Crosshairs*, *supra* note 13.

46. BLACK'S LAW DICTIONARY 1088 (9th ed. 2009).

47. *See* Press Release, U.S. Attorney's Office S.D.N.Y., Chief Executive Officer of Bayou Funds Sentenced to 20 Years in Federal Prison for Massive Investor Fraud (Apr.14, 2008), *available at* http://www.justice.gov/usao/nys/pressreleases/April08/israelsamuelsentencepr.pdf; *see also* Nick S. Dhesi, Note, *The Conman and the Sheriff: SEC Jurisdiction and the Role of Offshore Financial Centers in Modern Securities Fraud*, 88 TEX. L. REV. 1345, 1360 (2010).

48. *See* 2003 SEC STAFF REPORT, *supra* note 5, at 73.

49. *See* Thomsen et al., *supra* note 5, at 558–59; *see also* 2003 SEC STAFF REPORT, *supra* note 5, at 74.

50. *See* Thomsen et al., *supra* note 5, at 559.

usually then misrepresent fund operations to conceal the evidence.[51] To that end, the managers may fabricate the fund's appearance by using false documentation.[52] The misrepresentation enables the managers to disguise their violations and to deceive investors into remaining in the fund.[53]

A typical misappropriation involving hedge funds may become more complicated with hedge funds that are globally organized and thereby involve foreign or cross-border transactions.[54] For example, in a master-feeder structure, investors put their money into a domestic or offshore feeder fund, and the feeder funds then reinvest the money in a master fund.[55] Conversely, in redemption of shares, a master fund pays a domestic or offshore feeder fund for shares, and the feeder funds then repay individual investors.[56]

Regardless of whether hedge funds are globally organized, their managers may transfer money to foreign bank accounts after misappropriation.[57] This transaction can be designed to facilitate other fraudulent schemes, including money laundering.[58] In particular, the money laundering scheme enables the managers to conceal the source of the money and use it for their own purpose, avoiding regulatory nets.[59]

C. Insider Trading and Hedge Funds

Unlawful insider trading involves "buying or selling a security, in breach of a fiduciary duty or other relationship of trust and confidence, while in possession of material, nonpublic information about the security."[60] In recent years, many insider

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51. 2003 SEC STAFF REPORT, *supra* note 5, at 74; *see also* Thomsen et al., *supra* note 5, at 560, 567.

52. 2003 SEC STAFF REPORT, *supra* note 5, at 74; *see also* Thomsen et al., *supra* note 5, at 560, 567.

53. *See* Thomsen et al., *supra* note 5, at 559.

54. *See* LHABITANT, *supra* note 14, at 109–10.

55. *Id*. at 109.

56. *Id*. at 109–10.

57. *See, e.g.*, Information at 12–15, United States v. Madoff, 09 CRIM 213 (Mar. 10, 2009), *available at* http://www.justice.gov/usao/nys/madoff/20090310criminalinfo.pdf.

58. *See, e.g.*, *id*.

59. *See, e.g.*, *id*. at 13–15.

60. *Insider Trading*, SEC, http://www.sec.gov/answers/insider.htm (last visited Mar. 7, 2011).

trading cases have involved hedge funds and their managers.[61] The SEC also has considered "hedge fund insider trading as a top priority"[62] for its enforcement program.[63] This results from concerns that high-risk investment strategies and performance-based compensation of hedge funds may entice managers to devise insider trading schemes.[64] Also, in day-to-day operations, hedge funds develop close relationships with corporate clients and investment bankers who possess material nonpublic information.[65] This operational environment enables hedge fund managers to obtain inside information.[66]

One major concern involves the investment strategies employed by hedge fund managers.[67] These strategies usually contain various high-risk techniques.[68] In order to reduce the investment risks, hedge fund managers may seek to obtain information regarding financial events. In some instances, the managers may trade on material information that is available to them, but not yet disclosed to the public.[69] For example, a hedge fund manager employing an event-driven strategy might make transactions based on nonpublic information regarding

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61. *See* DONNA M. NAGY ET AL., SECURITIES LITIGATION AND ENFORCEMENT: CASE AND MATERIALS 467 (3rd ed. 2012); *see, e.g.*, Press Release, SEC, SEC Charges 14 in Wall Street Insider Trading Ring (Mar. 1, 2007), http://www.sec.gov/news/press/2007/2007-28.htm; Press Release, SEC, SEC Charges Billionaire Hedge Fund Manager Raj Rajaratnam with Insider Trading (Oct. 16, 2009), http://www.sec.gov/news/press/2009/2009-221.htm; Press Release, SEC, SEC Charges Hedge Fund Managers and Traders in $30 Million Expert Network Insider Trading Scheme (Feb. 8, 2011), http://www.sec.gov/news/press/2011/2011-40.htm.

62. Press Release, SEC, SEC Charges 14 in Wall Street Insider Trading Ring, *supra* note 61.

63. *Id.*; *see also* Thomsen et al., *supra* note 5, at 577 (citing *Examining Enforcement of Criminal Insider Trading and Hedge Fund Activity: Hearing Before the S. Comm. on the Judiciary*, 109th Congr. (2006) (testimony of Linda Chatman Thomsen, Dir., Div. of Enforcement, SEC), *available at* http://www.sec.gov/news/testimony/2006/ts120506lct.pdf).

64. Strohmenger, *supra* note 30, at 533.

65. *See* NAGY ET AL., *supra* note 61, at 467; Thomsen et al., *supra* note 5, at 578–81; Pearson, *supra* note 12, at 175.

66. Pearson, *supra* note 12, at 173–77.

67. Strohmenger, *supra* note 30, at 533.

68. *Id.*; Pearson & Pearson, *supra* note 14, at 19–20.

69. *See* Strohmenger, *supra* note 30, at 533.

corporate "bankruptcies, reorganizations, and mergers."[70] Indeed, hedge funds that function as lenders or substantial investors in a corporation may receive information in their capacity that has not been shared with the general public.[71]

Another concern is that performance-based compensation of hedge funds can also induce managers to commit illegal insider trading.[72] Because performance is closely related to compensation in hedge funds, managers might trade on inside information in order to increase their personal income.[73] In addition, high water marks and hurdle rates designed to limit performance fees might pressure managers enough to consider insider trading.[74] Under the provision of high water marks, each term fund managers have to achieve a better profit than the previous one in order to receive a performance fee.[75] Under the provision of hurdle rates, they must make more profits than the "minimum investment performance."[76] In these circumstances, managers are pressured to perform, which could lead them to commit insider trading.[77]

A final concern is that the operational environments of hedge funds enable the managers to obtain confidential information from investors or brokerage firms.[78] Hedge fund investors not only have the ability to commit insider trading, but also the motivation.[79] Some investors work as officials in other corporations, frequently dealing with corporate inside information.[80] Such investors might deliver corporate information to their fund managers,[81] aiming to benefit the funds that they invest

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70. PRESIDENT'S WORKING GROUP ON FIN. MKTS., HEDGE FUNDS, LEVERAGE, AND THE LESSONS OF LONG-TERM CAPITAL MANAGEMENT 3 (Apr. 1999); Thomsen et al., *supra* note 5, at 578.

71. Thomsen et al., *supra* note 5, at 578–79; *see also* Strohmenger, *supra* note 30, at 533.

72. Strohmenger, *supra* note 30, at 533.

73. *See id.*

74. *See* 2003 SEC STAFF REPORT, *supra* note 5, at 62–63.

75. *Id.* at 62.

76. *Id.* at 63.

77. *See* Strohmenger, *supra* note 30, at 533.

78. *See* NAGY ET AL., *supra* note 61, at 467; Thomsen et al., *supra* note 5, at 578–81; Pearson, *supra* note 12, at 175.

79. *See* Thomsen et al., *supra* note 5, at 578–79.

80. *See id.* at 578.

81. *Id.*

in. In light of their access and motives, hedge fund investors as corporate officials have great potential for insider trading.[82]

Outside entities assisting hedge funds also have the capacity and motive to be involved in insider trading.[83] In particular, a number of investment banks provide prime brokerage services to hedge funds.[84] While working with "public companies, mutual funds, and other hedge funds,"[85] investment banks usually handle nonpublic information.[86] Furthermore, many seek to maintain hedge fund clients because hedge funds trade regularly and frequently, which enables the banks to collect large amounts of service fees.[87] Thus, in order to maintain good relationships with hedge fund clients, investment bankers might transfer nonpublic information to those clients.[88]

In light of such risks, it is not surprising that the SEC has recently initiated a number of enforcement proceedings against hedge fund managers for insider trading.[89] Regulators, however, may face difficulties when investigating insider trading during the enforcement process. These complications typically arise because of the international aspects of hedge fund operations. For example, a hedge fund manager can globally organize hedge fund entities,[90] employ overseas transactions,[91] transfer money across borders,[92] invest in foreign securities,[93] and work with foreign persons or entities.[94]

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82. *See id.*

83. *See* NAGY ET AL., *supra* note 61, at 467; *see also* Thomsen et al., *supra* note 5, at 580.

84. Thomsen et al., *supra* note 5, at 580.

85. *Id.*

86. *Id.*

87. *Id.*

88. *Id.*; *see also* Strohmenger, *supra* note 30, at 534.

89. Thomsen et al., *supra* note 5, at 555.

90. Pearson, *supra* note 12, at 175–76; *see, e.g.*, Complaint at 5–6, SEC v. Lyon, 605 F.Supp.2d 531 (S.D.N.Y. 2009), *available at* http://www.sec.gov/litigation/complaints/2006/comp19942.pdf [hereinafter Lyon Complaint].

91. *See* LHABITANT, *supra* note 14, at 109–10.

92. Complaint at 40, SEC v. Galleon Mgmt. LP, 683 F.Supp.2d 316 (S.D.N.Y. 2010) (No. 09 Civ. 8811), *available at* http://www.sec.gov/litigation/complaints/2010/comp21397.pdf.

93. *See. e.g.*, *id.* at 11, 40 (describing the investment in a Canadian company's stock).

94. *See. e.g.*, *id.* at 39; Lyon Complaint, *supra* note 90, at 10.

D. Market Manipulation and Hedge Funds

Market manipulation refers to "intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities."[95] Typical manipulative conduct might involve circulating false information and using deceptive trading practices.[96] Such manipulative schemes are often attractive to hedge fund managers because they can falsify their performance by maneuvering markets in their favor.[97] Because performance is directly related to compensation, managers are enticed to trade manipulatively in order to increase their income.[98]

In addition, hedge fund managers have the ability to manipulate markets due to their strategic trading activities,[99] as well as due to the large amount of fund money at their discretionary use.[100] This operational environment enables managers to exploit fund investment for their manipulative trading.[101] For example, a hedge fund manager may invest the fund in stock, using various trading techniques in order to maneuver the price of the stock.[102] Then, he directs the fund to buy the stock at the raised price.[103] Finally, the manager can fabricate his performance based on the manipulative transactions.[104]

Similar to the situations in misappropriation and insider trading, a typical manipulation case may become more complicated with hedge funds that are globally managed.[105] Many hedge fund managers in the course of day-to-day business invest funds in foreign markets and, in doing so, frequently

95. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 199 (1976); *see also* NAGY ET AL., *supra* note 61, at 615.

96. *See Manipulation*, SEC, http://www.sec.gov/answers/tmanipul.htm (last visited Nov. 7, 2013); *see also* NAGY ET AL., *supra* note 61, at 615–16.

97. Thomsen et al., *supra* note 5, at 617.

98. *See id.*

99. *See* Pearson, *supra* note 12, at 174, 176.

100. *See* 2003 SEC STAFF REPORT, *supra* note 5, at 73; *see also* HAMMER ET AL., *supra* note 34, 273.

101. *See, e.g.*, Press Release, SEC, SEC Charges Securities Professionals and Traders in International Hedge Fund Portfolio Pumping Scheme (Feb. 24, 2011), http://www.sec.gov/news/press/2011/2011-51.htm.

102. *See, e.g.*, *id.*

103. *See, e.g.*, Ficeto Complaint, *supra* note 44, at 4.

104. *See, e.g.*, *id.*

105. *See* Pearson, *supra* note 12, at 175–76 (discussing difficulties in enforcing insider trading regulation).

communicate with overseas professionals,[106] making their activities difficult to detect and prosecute. A more serious concern is that some managers violating securities laws may intentionally make their schemes transnational in order to avoid regulatory detection.

II. INTERNATIONAL COOPERATION IN INVESTIGATING AND PROSECUTING SECURITIES FRAUD

A. Domestic Legislation Enabling Enforcement Cooperation

In order to respond to the global expansion of securities fraud, including hedge fund fraud, domestic securities regulators must act transnationally.[107] With no single regulation to govern all global markets, each country has sought to apply its domestic laws extraterritorially to combat transnational securities fraud.[108] In the United States, the SEC and the DOJ can currently apply the antifraud provisions of U.S. securities laws to certain overseas transactions.[109] The U.S. Supreme Court discarded the effects and conduct tests in *Morrison*,[110] yet Congress, immediately after this decision, enacted a provision in the Dodd-Frank Act re-authorizing the SEC and the DOJ to use these two tests.[111] Although national securities laws extend extraterritorially, the ability to gather facts and evidence of a violation, and the ability to prosecute that violation, is not guaranteed.[112] Because enforcement of law is limited within a territory, domestic regulators generally cannot use their en-

106. *See, e.g.*, Ficeto Complaint, *supra* note 44, at 4–5, 8, 45–51 (addressing the Internet communication between a trader in Canada and a trader in the United States).

107. *See* Chang, *supra* note 16, at 90.

108. *See id*. at 90–91.

109. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 929P(b), 124 Stat. 1376, 1864–65 (2010) [hereinafter Dodd-Frank Act].

110. Morrison v. Nat'l Austl. Bank Ltd., 130 S.Ct. 2869, 2879–88 (2010); *see also* Letter from Hannah L. Buxbaum, Ind. Univ., Maurer Sch. of Law, Comments on Study on Extraterritorial Private Rights of Action Release No. 34-63174, File No. 4-617, 1 (Feb. 18, 2011), *available at* http://www.sec.gov/comments/4-617/4617-14.pdf.

111. *See* Dodd-Frank Act § 929P(b); *see also* HICKS, *supra* note 18, § 11:50.

112. *See* INT'L BAR ASS'N, *supra* note 19, at 9–10; *see also* Sec. & Futures Comm'n, *supra* note 18, at 6, 7.

forcement power within the territory of other countries.[113] Thus, securities regulators should cooperate with each other to successfully enforce national securities laws.[114]

For this reason, many countries have established provisions authorizing their securities regulators to provide cross-border assistance. For example, the United States has Section 21(a)(2) of the Securities Exchange Act ("Exchange Act");[115] Switzerland has Article 38 of the Federal Act on Stock Exchange and Securities Trading ("Stock Exchange Act")[116] and Article 42 of the Federal Act on the Financial Market Supervision Act ("Financial Market Supervision Act");[117] Canada has Sections 11(1)(b), 126, 143.10(1), and 153 of the Ontario Securities Act;[118] the U.K. has Sections 169 and 354 of the Financial Services and Markets Act of 2000;[119] Hong Kong has Section 186 of the Securities and Futures Ordinance;[120] and South Korea has Article 437 of the Financial Investment Services and Capital Markets Act ("Financial Investment Act").[121] These provisions enable domestic securities regulators to obtain evidence located abroad, thereby overcoming the obstacles to enforcing laws

113. INT'L BAR ASS'N, *supra* note 19, at 9–10.

114. *See* HICKS, *supra* note 18, §11:53; *see also* Sec. & Futures Comm'n, *supra* note 18, at 7.

115. 15 U.S.C. § 78u(a)(2) (2006).

116. Federal Act on Stock Exchange and Securities Trading (Stock Exchange Act, SESTA) of March 24, 1995, art. 38 (Jan. 1, 2009) (Switz.), *available at* http://www.six-exchange-regulation.com/download/admission/regulation/federal_acts/sesta_en.pdf (unofficial translation).

117. Federal Act on the Financial Market Supervisory Authority (Financial Market Supervision Act, FINMASA) of 22 June 2007 (2009), art. 42 (July 1, 2013) (Switz.), *available at* http://www.admin.ch/ch/e/rs/9/956.1.en.pdf.

118. Securities Act, R.S.O. 2011, c. S.5, §§ 11(1)(b), 126(1)(b), 143.10(1), 153 (Can.), *available at* http://www.e-laws.gov.on.ca/html/statutes/english/elaws_statutes_90s05_e.htm.

119. Financial Services and Markets Act, 2000, c. 8, §§ 169, 354 (U.K.), *available at* http://www.legislation.gov.uk/ukpga/2000/8/pdfs/ukpga_20000008_en.pdf.

120. Securities and Futures Ordinance, (2003) Cap. 571, § 186 (H.K.), *available at* http://www.legislation.gov.hk/blis_pdf.nsf/6799165D2FEE3FA94825755E0033E532/5167961DDC96C3B7482575EF001C7C2D/$FILE/CAP_571_e_b5.pdf.

121. FINANCIAL INVESTMENT SERVICES AND CAPITAL MARKETS ACT art. 437 (S. Kor.), *available at* http://www.fsc.go.kr/eng/lr/list03.jsp?menu=0203&bbsid=BBS0087 (last visited Oct. 17, 2013).

against transnational securities fraud.[122] With no single regulator to govern the global financial market,[123] securities regulators can most effectively combat globalized securities fraud by cooperating with one another.[124]

B. International Networks for Enforcement Cooperation

The aforementioned legislation enables securities regulators to assist foreign counterparts in enforcing domestic laws.[125] The execution of this assistance allows for certain arrangements among nations.[126] Although ad hoc arrangements can be used by regulators in a particular case, prearranged international networks are more common.[127] Popular networks for international securities enforcement include MOUs, particularly those that are bilateral and multilateral, and MLATs.[128] MOUs are nonbinding arrangements allowing regulators to share information and to provide assistance to their foreign counterparts.[129] Because of their flexibility, MOUs are increasingly considered key tools for transnational cooperation among securities regulators.[130] By contrast, MLATs are less flexible because establishing MLATs involves complicated procedures, such as diplomatic negotiation and legislative ratification.[131] As treaties, MLATs are legally binding agreements and typically

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122. *See* Friedman et al., *supra* note 21, at 41.

123. *See* Chang, *supra* note 16, at 90.

124. *See SEC International Enforcement Assistance*, *supra* note 25.

125. *See* Friedman et al., *supra* note 21, at 40 (stating that the legislation enables securities regulators to share information freely with their foreign counterparts).

126. *See id.*

127. *See SEC International Enforcement Assistance*, *supra* note 25.

128. *See* OFFICE OF INT'L AFFAIRS, *supra* note 23, at 3–4.

129. Elliott M. Beard, *A Critical Analysis of the Effects Of* Colello v. SEC *on International Securities Law Enforcement Agreements*, 7 DUKE J. COMP. & INT'L L. 271, 274 (1996).

130. *See* Roberta S. Karmel & Claire R. Kelly, *The Hardening of Soft Law in Securities Regulation*, 34 BROOK. J. INT'L L. 883, 885, 894 (2009); *see also* Dinah Shelton, *Soft Law*, *in* ROUTLEDGE HANDBOOK OF INTERNATIONAL LAW 68, 75 (David Armstrong ed., 2009) (describing the increasing importance of "soft law," which includes "any written international instrument, other than a treaty, containing principles, norms, standards, or other statements of expected behavior").

131. *See* Caroline A.A. Greene, *International Securities Law Enforcement: Recent Advances in Assistance and Cooperation*, 27 VAND. J. TRANSNAT'L L. 635, 649 (1994).

require regulators to provide assistance to each other in criminal matters.[132] In recent years, countries have relied largely on such international networks to promote cooperation in securities enforcement.[133]

1. Memoranda of Understanding (MOUs)

a. Bilateral MOUs

i. Overview

MOUs refer to "regulator-to-regulator arrangements regarding information sharing and cooperation in securities matters."[134] These arrangements are memorialized in nonbinding agreements.[135] Since 1982, the SEC has signed bilateral MOUs on enforcement cooperation with a number of authorities from different jurisdictions, including Argentina, Australia, Brazil, Canada, Chile, France, Germany, Hong Kong, Israel, Italy, Japan, Jersey, Mexico, the Netherlands, Norway, Portugal, Singapore, Spain, Switzerland, and the U.K.[136] The United States concluded MOUs with Switzerland in 1982[137] and 1987,[138] Canada in 1988,[139] the U.K. in 1991,[140] and Hong Kong in 1995.[141]

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132. *Id.* at 640; *see also* Charles R. Mills et al., *International Enforcement: Enforcement Actions in the Global Market*, *in* THE SECURITIES ENFORCEMENT MANUAL: TACTICS AND STRATEGIES 489, 498–99 (Richard M. Phillips ed., 1997).

133. Although countries can use the Hague Convention on the Taking of Evidence Abroad in Civil or Commercial Matters (Hague Convention or Convention), this mechanism suffers a number of problems all its own. Greene, *supra* note 131, at 639–40 (listing the limitations of using the Hague Convention); Beard, *supra* note 129, at 272.

134. DIV. OF ENFORCEMENT, SEC, *supra* note 27, § 3.3.6.3.

135. Beard, *supra* note 129, at 274.

136. *SEC International Enforcement Assistance*, *supra* note 25; SEC, *Cooperative Arrangements with Foreign Regulators*, *supra* note 24.

137. Memorandum of Understanding, U.S.-Switz., Aug. 31, 1982, *available at* http://www.sec.gov/about/offices/oia/oia_bilateral/switzerland.pdf [hereinafter 1982 U.S.-Switz. MOU] (Memorandum of Understanding between the United States Securities and Exchange Commission and the Government of Switzerland). As the first MOU for global enforcement cooperation, the 1982 MOU signed by the United States with Switzerland is historically important. Each part of this MOU demonstrates how difficult enforcement cooperation was in the early stage. The United States has modeled other MOUs on this first MOU with some revision. MARVIN G. PICKHOLZ, SECURITIES CRIME § 4:45 (11th ed. 2012). Given these circumstances, analyzing the 1982 MOU be-

tween the United States and Switzerland can be useful to understanding other MOUs' contents and to finding ways of overcoming their problems. This chapter, therefore, includes analysis of the 1982 MOU, even though "[t]his MOU has now been replaced by [the 1987 MOU]." David Chaikin, *The Impact of Swiss Principles of Mutual Assistance on Financial and Fiscal Crimes*, 16 REVENUE L.J. 192, 196 n.13 (2006), *available at* http://epublications.bond.edu.au/cgi/viewcontent.cgi?article=1173&context=rlj&sei-
re-
dir=1#search=%221982%20MEMORANDUM%20UNDERSTANDING%20GOVERNMENT%20SWITZERLAND%22.

138. Memorandum of Understanding on Mutual Assistance in Criminal Matters and Ancillary Administrative Proceedings, U.S.-Switz., Nov. 10, 1987, 27 I.L.M. 480 (1988), *available at* http://www.jstor.org/stable/pdfplus/20693205.pdf?acceptTC=true (Memorandum of Understanding between the Government of the United States of America and the Government of Switzerland). In addition to the 1982 and 1987 MOUs, on November 3, 1993, the United States exchanged diplomatic notes with Switzerland. Letter from Warren Christopher, Sec'y of State, U.S., to Carlo Jagmetti, Ambassador of Switz., at 1 (Nov. 3, 1993), *available at* http://www.cftc.gov/ucm/groups/public/@internationalaffairs/documents/file/ssc93.pdf [hereinafter 1993 U.S.-Switz. Notes]. This has expanded the range of assistance that the SEC could obtain under the 1987 MOU; in particular, the SEC has been able to "use information obtained in Switzerland as evidence in civil and administrative proceedings involving a wide array of securities-related offenses." *Exchange of Diplomatic Notes Between the United States and Switzerland*, SEC NEWS DIGEST 1, 2 (Nov. 3, 1993), *available at* http://www.sec.gov/news/digest/1993/dig110393.pdf [hereinafter SEC NEWS DIGEST]; *see also* 1993 U.S.-Switz. Notes, *supra*, at 1–2 (Letter from Warren Christopher, Sec'y of State, U.S., to Carlo Jagmetti, Ambassador of Switzerland).

139. Memorandum of Understanding on Administration and Enforcement of Securities Laws, U.S.-Can., Jan. 7, 1988, 27 I.L.M. 412, *available at* http://sec.gov/about/offices/oia/oia_bilateral/canada.pdf [hereinafter U.S.-Can. MOU] (Memorandum of Understanding between the United States Securities and Exchange Commission and the Ontario Securities Commission, the Commission des Valeurs Mobilieres du Quebec, and the British Columbia Securities Commission).

140. Memorandum of Understanding on Mutual Assistance and the Exchange of Information, U.S.-U.K., Sept. 25, 1991, International Series Release No. 323, 1991 SEC LEXIS 1997, *available at* http://sec.gov/about/offices/oia/oia_bilateral/ukingdom_enfcoop.pdf [hereinafter U.S.-U.K. MOU] (Memorandum of Understanding between the United States Securities and Exchange Commission and Commodity Futures Trading Commission and the United Kingdom Department of Trade and Industry and Securities and Investments Board). As the second MOU between the United States and the U.K., this agreement has replaced the previous 1986 MOU. Memorandum of Understanding on Exchange of Information, U.S.-

ii. Scope of Assistance

Whether a domestic regulator can successfully prosecute an international fraud case depends largely on the assistance that can be obtained from foreign authorities.[142] If foreign authorities can provide assistance by leveraging their own domestic power, a domestic regulator can prosecute international fraud as effectively as a local case.[143] On the other hand, if foreign authorities so requested are restricted from using their power fully, a domestic regulator may be unable to obtain crucial pieces of evidence.[144]

Given the crucial importance of substantial transnational assistance, most MOUs, including those signed by the United States with Switzerland, Canada, the U.K., and Hong Kong, define the scope of assistance.[145] Under the 1982 MOU between

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U.K., Sept. 23, 1986, International Series Release No. 4, 1986 SEC LEXIS 2308, *available at* http://sec.gov/about/offices/oia/oia_bilateral/ukingdom_enfcoop.pdf (Memorandum of Understanding between the United States Securities and Exchange Commission and the Department of Trade and Industry of the United Kingdom); *see also* MARC I. STEINBERG, INTERNATIONAL SECURITIES LAW: A CONTEMPORARY AND COMPARATIVE ANALYSIS 221 (1999).

141. Memorandum of Understanding Concerning Consultation and Cooperation and Enforcement of Securities Law and Declaration on Cooperation and Supervision of Cross-Border Investment Management Act, U.S.-H.K., Oct. 5, 1995, 1995 SEC LEXIS 2810, *available at* http://sec.gov/about/offices/oia/oia_bilateral/hongkong.pdf [hereinafter U.S.-H.K. MOU] (Memorandum of Understanding between the United States Securities and Exchange Commission and the Hong Kong Securities and Futures Commission).

142. ANA CARVAJAL & JENNIFER ELLIOTT, INT'L MONETARY FUND, THE CHALLENGE OF ENFORCEMENT IN SECURITIES MARKETS: MISSION IMPOSSIBLE? 22 (2009), *available at* http://www.imf.org/external/pubs/ft/wp/2009/wp09168.pdf; *see also SEC International Enforcement Assistance*, *supra* note 25.

143. *See* Technical Comm., Int'l Org. of Sec. Comm'ns, Principles for Memoranda of Understanding § 7 (1991), http://www.iosco.org/library/pubdocs/pdf/IOSCOPD17.pdf.

144. *See id.*; *see also* Sec. & Futures Comm'n, *supra* note 18, at 7.

145. *See* 1982 U.S.-Switz. MOU, *supra* note 137, pt. III, para. 1; Agreement XVI of the Swiss Bankers' Association with Regard to the Handling of Requests for Information from the SEC on the Subject of Misuse of Insider Information, arts. 4, 9, Aug. 31, 1982, 22 I.L.M. 7 (1983) [hereinafter Agreement XVI of the Swiss Bankers' Association]; U.S.-Can. MOU, *supra* note 139, art. 2; U.S.-U.K. MOU, *supra* note 140, pt. II, para. 6; U.S.-H.K. MOU, *supra* note 141, para. 3.1.

the United States and Switzerland, the Swiss Bankers' Association was able to provide information to the SEC, bypassing Swiss bank secrecy laws.[146] If certain conditions were met, asset freezing assistance was also available under this MOU.[147] This assistance was limited to insider trading investigations; thus it was not available for most securities law violations.[148] Nevertheless, since the exchange of diplomatic notes between the United States and Switzerland in 1993, this narrow scope of assistance has been expanded to include various securities law violations.[149]

The MOUs signed by the United States with Canada, the U.K., and Hong Kong recognize a broad range of assistance in gathering evidence.[150] In particular, these agreements call for "the fullest mutual assistance,"[151] requiring that authorities assist each other in (1) "providing . . . information in the files of the requested [a]uthority,"[152] (2) "taking the evidence of persons,"[153] and (3) "obtaining documents from persons."[154] Such assistance is governed by "the laws of the jurisdiction of the requested [a]uthority."[155] The scope of assistance agreed upon by these three countries is reflected in the IOSCO MMOU.[156]

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146. 1982 U.S.–Switz. MOU, *supra* note 137, pt. III, para. 1; Agreement XVI of the Swiss Bankers' Association, *supra* note 145, art. 4.

147. Agreement XVI of the Swiss Bankers' Association, *supra* note 145, art. 9, para. 1.

148. 1982 U.S.–Switz. MOU, *supra* note 137, pt. I, para. 1, pt. III, para. 2.

149. SEC NEWS DIGEST, *supra* note 138, at 2; 1993 U.S.-Switz. Notes, *supra* note 138, at 1 (Letter from Warren Christopher, Sec'y of State, to Carlo Jagmetti, Ambassador of Switzerland).

150. *See* U.S.-Can. MOU, *supra* note 139, art. 2; U.S.-U.K. MOU, *supra* note 140, pt. II, para. 6; U.S.-H.K. MOU, *supra* note 141, para. 3.1.

151. U.S.-Can. MOU, *supra* note 139, art. 2, para. 1; U.S.-H.K. MOU, *supra* note 141, para. 3.1.1. The MOU between the U.S. and the U.K. also has a similar provision. *See* U.S.-U.K. MOU, *supra* note 140, pt. II, para. 6.

152. U.S.-Can. MOU, *supra* note 139, art. 2, para. 2(a).

153. *Id.* art. 2, para. 2(b).

154. *Id.* art. 2, para. 2(c). MOUs signed by the U.S. with the U.K. and Hong Kong also have similar provisions. *See* U.S.-U.K. MOU, *supra* note 140, pt. II, para. 6; U.S.-H.K. MOU, *supra* note 141, para. 3.1.2.

155. U.S.-U.K. MOU, *supra* note 140, pt. IV, para. 13(a). MOUs signed by the U.S. with Canada and Hong Kong also have similar provisions. *See* U.S.-Can. MOU, *supra* note 139, art. 5, para. 3; U.S.-H.K. MOU, *supra* note 141, para. 3.4.3.

156. Int'l Org. of Sec. Comm'ns, Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information art. 7(b), May 2002, *available at*

Such a broad range of assistance in information sharing is necessary, but not sufficient, to establish an effective international enforcement mechanism.[157] In particular, assistance in freezing assets is also indispensable to combatting international securities fraud, for if wrongdoers can enjoy the proceeds of their fraudulent activities even after they are detected, the deterrent function of securities laws is decreased.[158] In light of the importance of freezing assets, it is problematic that the MOUs signed by the United States with Canada, the U.K., and Hong Kong do not explicitly provide for assistance in this regard.[159]

b. International Organization of Securities Commissions Multilateral MOU (IOSCO MMOU)

i. Overview

IOSCO was established in 1983 to promote regulatory cooperation in global securities markets.[160] It started with only eleven members—all of them North and South American securities regulators.[161] Later, from 1984 onward, non-American regulators also began to enter IOSCO.[162] Accordingly, with the constant expansion of its membership, it has admitted securities regulators from more than one hundred countries, involving over 95% of global securities markets.[163] IOSCO now functions as a primary governmental cluster to promote interna-

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http://www.iosco.org/library/pubdocs/pdf/IOSCOPD386.pdf [hereinafter IOSCO MMOU] (rev. May 2012).

157. *See* Michael D. Mann et al., *The Establishment of International Mechanisms for Enforcing Provisional Orders and Final Judgments Arising from Securities Law Violations*, 55 L. & CONTEMP. PROBS. 303, 304 (1992), *available at* http://www.jstor.org/stable/pdfplus/1192113.pdf?acceptTC=true ("Effective enforcement of securities laws requires that regulators be able to thwart the dissipation or secreting of the fruits of international securities fraud, and to facilitate the return of the illicit profits to injured investors.").

158. *Id.*; David Chaikin, *The Freezing of Criminal Assets*, 8 COMMW. L. BULL. 1197, 1198 (1982) (discussing the illegal gains of general crimes).

159. *See generally* U.S.-U.K. MOU, *supra* note 140; U.S.-Can. MOU, *supra* note 139; U.S.-H.K. MOU, *supra* note 141.

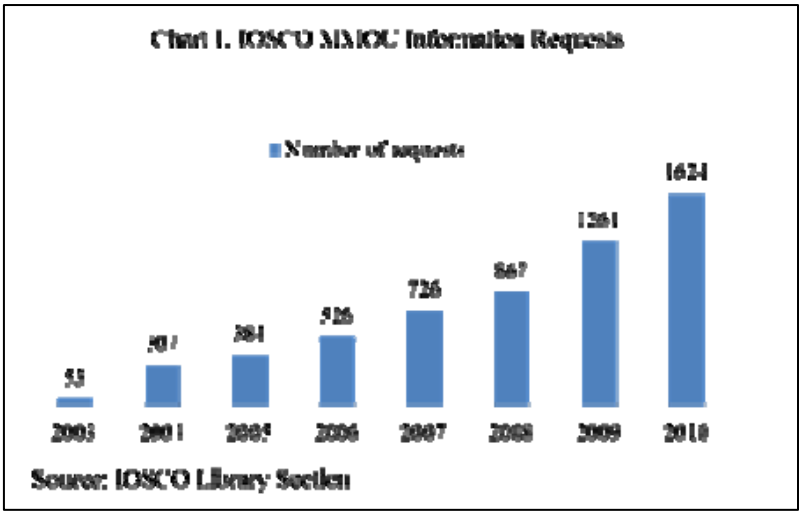
160. *About IOSCO: IOSCO Historical Background*, IOSCO, http://www.iosco.org/about/index.cfm?section=background (last visited Sept. 14, 2011) [hereinafter *IOSCO Historical Background*].

161. *Id.*

162. *See id.*; *see also* Chris Brummer, *Post-American Securities Regulation*, 98 CAL. L. REV. 327, 338 (2010).

163. *IOSCO Historical Background*, *supra* note 160.

tional cooperation in the context of securities regulation.[164] In particular, IOSCO has promoted a Multilateral Memorandum of Understanding since 2002.[165] The purpose of this MMOU is to "facilitate cross-border enforcement and exchange of information among international securities regulators."[166] In recent years, a significant number of regulators have signed the IOSCO MMOU,[167] and they have frequently employed the MMOU mechanisms for their enforcement cooperation.[168]



164. *See id.*; *see also* Brummer, *supra* note 162, at 338.

165. *IOSCO Historical Background*, *supra* note 160.

166. *Id.*

167. Currently, ninety-seven authorities are listed as signatories in Appendix A of the MMOU. *Current Signatories*, *supra* note 26.

168. In 2003, fifty-six requests were filed under the MMOU; in 2004, 307 requests; in 2005, 384 requests; in 2006, 526 requests; in 2007, 726 requests; in 2008, 867 requests; in 2009, 1261 requests; and in 2010, 1624 requests were filed. *IOSCO Library Section: Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information (MMoU)*, IOSCO, http://www.iosco.org/library/index.cfm?section=mou_main (last visited Nov. 9, 2013).

ii. Scope of Assistance

Article 7 of the IOSCO MMOU provides signatories with the ability to use its complete domestic power.[169] A requested signatory can thus choose from among three types of assistance to execute, depending on the request.[170] First of all, if a requesting authority is seeking information in the possession of a requested authority, the latter can comply under the MMOU by simply sending the information to the former.[171] On the other hand, if a requesting authority is seeking information that a requested authority does not have, the latter can use its investigative power to obtain the documents and then send them to the former.[172] Furthermore, in some instances, a requested authority can compel a particular person to make statements or give testimony.[173]

The MMOU also specifies types of information that can be shared.[174] The ability to obtain key information is crucial to succeeding in securities investigations.[175] Indeed, many authorities investigating securities fraud seek a broad range of information regarding investments, brokerage, transactions, and management.[176] Plenty of information can be obtained from entities regulated by a requested authority,[177] but certain information is accessible only through unregulated entities.[178] For example, an authority investigating market manipulation or insider trading usually requests bank records in order to track money involved in fraud.[179] Thus, in order to successfully combat market manipulation and insider trading, a requested authority must secure the ability to demand from unregulated

169. IOSCO MMOU, *supra* note 156, art. 7(a).
170. *See id.* arts. 7(b), 9.
171. *Id.* arts. 7(b)(i), 9(a).
172. *Id.* arts. 7(b)(ii), 9(b).
173. *Id.* arts. 7(b)(iii), 9(c).
174. *See id.* art. 7(b)(ii).
175. *See* CARVAJAL & ELLIOTT, *supra* note 142, at 15.
176. *Id.*
177. *Id.* at 15.
178. *Id.* at 16.
179. *Id.*

entities information that it can then deliver to a requesting authority.[180]

For this reason, the MMOU provides that an authority can share not only information obtained from a regulated entity, but also records received from an unregulated one, namely, a bank.[181] Article 7 stipulates that signatory authorities can perform a mutual exchange of (1) "contemporaneous records sufficient to reconstruct all securities and derivatives transactions, including records of all funds and assets transferred into and out of bank and brokerage accounts relating to these transactions";[182] (2) "records that identify: the beneficial owner and controller, and for each transaction, the account holder; the amount purchased or sold; the time of the transaction; the price of the transaction; and the individual and the bank or broker and brokerage house that handled the transaction";[183] and (3) "information identifying persons who beneficially own or control non-natural [p]ersons organized in the jurisdiction of the [r]equested [a]uthority."[184]

Despite these provisions, authorities have in recent years sought a range of information broader than what the MMOU requires they share while investigating insider trading and market manipulation.[185] In particular, authorities often find crucial evidence of insider trading from telephone conversations and Internet service history,[186] which are not made available under any explicit provision of the IOSCO MMOU.[187]

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180. *Id.*

181. *See* IOSCO MMOU, *supra* note 156, arts. 7(b)(ii), 9(b).

182. *Id.* art. 7(b)(ii).

183. *Id.*

184. *Id.*

185. *See* CARVAJAL & ELLIOTT, *supra* note 142, at 16; *see, e.g.*, United States v. Rajaratnam, 802 F. Supp. 2d 491, 499–500, 502, 507–12, 514–16 (S.D.N.Y. 2011) (showing that telephone conversations, instant messages, and emails exchanged between defendants revealed that the defendants committed insider trading).

186. *See* CARVAJAL & ELLIOTT, *supra* note 142, at 16; *see, e.g.*, *Rajaratnam*, 802 F. Supp. 2d at 499–500, 502, 507–12, 514–16.

187. *See generally* IOSCO MMOU, *supra* note 156, art. 7(b)(ii).

2. Mutual Legal Assistance Treaties (MLATs)

a. Overview

Besides MOUs, two countries often enter into treaties regarding mutual legal assistance in criminal proceedings.[188] Such an agreement is called an MLAT.[189] Though this treaty applies only in criminal cases, the SEC can nonetheless use it to "obtain assistance in any investigation that relates to any securities violation that might be punishable by criminal sanctions."[190] Thus, an MLAT can be a powerful tool for securities authorities to conduct international enforcement.[191] This is primarily because an MLAT contains its own binding power[192] and allows various types of assistance.[193] In the United States, this treaty is usually maintained by the DOJ.[194] As of 2011, the DOJ maintains MLATs with a number of foreign countries,[195] including Switzerland in 1973, Canada in 1985, the U.K. in

188. Lynda M. Ruiz, Note, *European Community Directive on Insider Dealing: A Model for Effective Enforcement of Prohibitions on Insider Trading in International Securities Markets*, 33 COLUM. J. TRANSNAT'L L. 217, 231 (1995); *see also* U.S. DEP'T OF STATE, A LIST OF TREATIES AND OTHER INTERNATIONAL AGREEMENTS OF THE UNITED STATES IN FORCE ON JANUARY 1, 2011, at 43, 55, 161, 265, 294 (2011) [hereinafter TREATIES IN FORCE], *available at* http://www.state.gov/documents/organization/169274.pdf.

189. Ruiz, *supra* note 188, at 231.

190. Mills et al., *supra* note 132, at 499; *see also* DIV. OF ENFORCEMENT, SEC, *supra* note 27, § 3.3.6.3.

191. *See* Friedman et al., *supra* note 21, at 42.

192. *See* Paul Coggins & William A. Roberts, *Extraterritorial Jurisdiction: An Untamed Adolescent*, 17 COMMW. L. BULL. 1391, 1402 (1991) (addressing the fact that MLATs legally oblige countries to provide assistance to each other); *see also* DIV. OF ENFORCEMENT, SEC, *supra* note 27, § 3.3.6.3 ("MLATs may be an effective mechanism to obtain assistance when an MOU with a particular country either does not exist or does not permit the type of information sought from a witness residing overseas.").

193. *See* John E. Harris, *International Cooperation in Fighting Transnational Organized Crime: Special Emphasis on Mutual Legal Assistance and Extradition*, *in* United Nations Asia & Far E. Inst. for the Prevention of Crime and Treatment of Offenders (UNAFEI), *Annual Report for 1999 and Resource Material Series No. 57*, at 133, 139 (Sept. 2001), *available at* http://www.unafei.or.jp/english/pdf/PDF_rms/no57/57-11.pdf (listing the types of assistance that can be provided under MLATs).

194. DIV. OF ENFORCEMENT, SEC, *supra* note 27, § 3.3.6.3.

195. *Id.*; *see, e.g.*, TREATIES IN FORCE, *supra* note 188, at 43, 55, 161, 265, 294.

1994, Hong Kong in 1997, and South Korea in 1993.[196] Thus, in order to obtain assistance from these countries under their MLATs, the SEC must ask the DOJ to assume the requesting process on its behalf.[197] This MLAT process proves useful in cases where MOUs are not available.[198]

b. Making Requests

Most MLATs specify how to make a request for assistance.[199] MLATs do not usually allow securities authorities to make a request directly to their counterparts.[200] Instead, they require authorities to communicate with each other through an official channel for administrating MLAT procedures, namely, a "Central Authority."[201] Given this requirement, all requests and responses to requests must be made through each country's respective Central Authority on behalf of other regulatory authorities in the country.[202]

Indeed, MLATs signed by the United States with Switzerland, Canada, the U.K., Hong Kong, and South Korea all have provisions to appoint Central Authorities for each party.[203] Under these MLATs, in the United States, the Central Authority

196. U.S.-Switz. MLAT, *supra* note 27; U.S.-Can. MLAT, *supra* note 27; U.S.-U.K. MLAT, *supra* note 27; U.S.-H.K. MLAT, *supra* note 27; U.S.-S. Korea MLAT, *supra* note 27.

197. *See, e.g.*, U.S.-Switz. MLAT, *supra* note 27, ch. VII, art. 28; U.S.-Can. MLAT, *supra* note 27, arts. I, VI, para. 1; U.S.-U.K. MLAT, *supra* note 27, art. 2; U.S-H.K. MLAT, *supra* note 27, art. 2; U.S.-S. Korea MLAT, *supra* note 27, art. 2.

198. DIV. OF ENFORCEMENT, SEC, *supra* note 27, § 3.3.6.3.

199. *See* U.S.-Switz. MLAT, *supra* note 27, ch. VII, art. 28; U.S.-Can. MLAT, *supra* note 27, art. VI; U.S.-U.K. MLAT, *supra* note 27, art. 2; U.S.-H.K. MLAT, *supra* note 27, art. 2; U.S.-S. Korea MLAT, *supra* note 27, art. 2.

200. Beard, *supra* note 129, at 274.

201. Harris, *supra* note 193, at 140; *see also* U.S.-Switz. MLAT, *supra* note 27, ch. VII, art. 28; U.S.-Can. MLAT, *supra* note 27, art. VI, para. 1; U.S.-U.K. MLAT, *supra* note 27, art. 2, paras. 3–4; U.S.-H.K. MLAT, *supra* note 27, art. 2, para. 3; U.S.-S. Korea MLAT, *supra* note 27, art. 2, paras. 1, 3.

202. Beard, *supra* note 129, at 274; *see also* U.S.-Switz. MLAT, *supra* note 27, ch. VII, art. 28, paras. 1–2; U.S.-Can. MLAT, *supra* note 27, art. VI, para. 1; U.S.-U.K. MLAT, *supra* note 27, art. 2, para. 3; U.S.-H.K. MLAT, *supra* note 27, art. 2, para. 3; U.S.-S. Korea MLAT, *supra* note 27, art. 2, para. 1.

203. U.S.-Switz. MLAT, *supra* note 27, ch. VII, art. 28, para. 1; U.S.-Can. MLAT, *supra* note 27, art. I; U.S.-U.K. MLAT, *supra* note 27, art. 2, paras. 1–2; U.S.-H.K. MLAT, *supra* note 27, art. 2, paras. 1–2; U.S.-S. Korea MLAT, *supra* note 27, art. 2, paras. 1–2.

is the Attorney General or his designee;[204] in Switzerland, the Division of Police of the Federal Department of Justice and Police in Bern;[205] in Canada, the Minister of Justice or his designee;[206] in the U.K., the Secretary of State for the Home Department or his designee;[207] in Hong Kong, the Attorney General of Hong Kong or his designee;[208] and in Korea, the Minister of Justice or his designee.[209]

c. The Demands of Dual Criminality

MLATs often require that a request demonstrate dual criminality.[210] Under this requirement, a case specified in a request must constitute a crime in not only the requesting but also the requested jurisdiction.[211] For example, the MLAT between the United States and Switzerland stipulates that each party can use its compulsory power for the purpose of assistance when "an offense . . . would be punishable under the law in the requested [s]tate if committed within its jurisdiction and [it] is listed in the [s]chedule [of the treaty]."[212] The MLATs signed by the United States with Hong Kong and South Korea also require that the request show dual criminality.[213] Under each of these three MLATs, however, dual criminality is not demanded

204. U.S.-Switz. MLAT, *supra* note 27, ch. VII, art. 28, para. 1; U.S.-Can. MLAT, *supra* note 27, art. I; U.S.-U.K. MLAT, *supra* note 27, art. 2, para. 2; U.S.-H.K. MLAT, *supra* note 27, art. 2, para. 2; U.S.-S. Korea MLAT, *supra* note 27, art. 2, para. 2.

205. U.S.-Switz. MLAT, *supra* note 27, ch. VII, art. 28, para. 1.

206. U.S.-Can. MLAT, *supra* note 27, art. I.

207. U.S.-U.K. MLAT, *supra* note 27, art. 2, para. 2.

208. U.S.-H.K. MLAT, *supra* note 27, art. 2, para. 2.

209. U.S.-S. Korea MLAT, *supra* note 27, art. 2, para. 2.

210. *See* U.S.-Switz. MLAT, *supra* note 27, ch. I, art. 4, para. 2; U.S.-H.K. MLAT, *supra* note 27, art. 3, para. 1(d); U.S.-S. Korea MLAT, *supra* note 27, art. 3, para. 1(d).

211. Harris, *supra* note 193, at 140.

212. U.S.-Switz. MLAT, *supra* note 27, ch. I, art. 4, para. 2. Under this MLAT, however, dual criminality is not demanded in cases where requests involve "offenses against the laws relating to bookmaking, lotteries and gambling when conducted as a business." *Id.* app. at 49.

213. U.S.-H.K. MLAT, *supra* note 27, art. 3, para. 1(d); U.S.-S. Korea MLAT, *supra* note 27, art. 3, para. 1(d).

in cases where requests involve certain crimes listed in its Annex.[214]

Arguably, discarding the dual criminality requirement would, in fact, promote better cooperation.[215] Because each country defines securities law violations in different ways, a requirement of this sort can actually impede international cooperation.[216] Indeed, the MLATs signed by the United States with Canada and the U.K. have no provision of dual criminality.[217] Thus, assistance is available under these MLATs as long as a requested case is criminally liable in a requesting country.[218]

III. REFORMING MEMORANDA OF UNDERSTANDING TOWARD GREATER ENFORCEMENT COOPERATION

A. Enhancing Mechanisms for Cooperation in Asset Freezing

1. Ineffectiveness of Current Methods

Assistance in freezing assets is indispensable to combatting international securities fraud because if violators cannot enjoy the proceeds of the frauds, the deterrent function of securities laws will increase.[219] Securities regulators, therefore, often seek to freeze assets abroad through cooperative mechanisms.[220] Unfortunately, examining the methods that are available reveals that they are too lengthy and unstable for se-

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214. U.S.-Switz. MLAT, *supra* note 27, ch. I, art. 4, para. 2(b); U.S.-H.K. MLAT, *supra* note 27, art. 3, annex; U.S.-S. Korea MLAT, *supra* note 27, art. 3, annex.

215. *See* Beard, *supra* note 129, at 274 (explaining the MLAT between the U.S. and Switzerland).

216. *See id.*; PICKHOLZ, *supra* note 137, §§ 4:42, 4:45.

217. U.S.-Can. MLAT, *supra* note 27, art. II, para. 3; Warren Christopher, Letter of Submittal to Treaty on Mutual Legal Assistance in Criminal Matters, U.S.-U.K., Jan. 6, 1994, S. TREATY DOC. NO. 104-2, 1994 U.S.T. LEXIS 205, at *4 (1995) [hereinafter Letter of Submittal].

218. *See* U.S.-Can. MLAT, *supra* note 27, art. II, para. 3; Letter of Submittal, *supra* note 217, at *4.

219. *See* Chaikin, *supra* note 158, at 1198 (discussing the illegal gains of general crimes); *see also* Mann et al., *supra* note 157, at 304; *see also* Ethiopas Tafara, Dir., Office of Int'l Affairs, SEC, IOSCO Annual Conference: Pub. Discussion Panel on Combating Fin. Crime Globally (Oct. 17, 2003), http://www.sec.gov/news/speech/spch101703iosco.htm [hereinafter IOSCO Annual Conference].

220. *See* OFFICE OF INT'L AFFAIRS, *supra* note 23, at 5.

curities enforcement and thus are not as effective as they should be.[221]

For example, MLATs can be used to freeze assets abroad if a treaty has been arranged beforehand.[222] This method, however, is not effective for securities enforcement because MLATs are designed for criminal prosecution and often require a request to demonstrate dual criminality.[223] Furthermore, MLATs are generally administered by criminal authorities, such as the DOJ, and not by securities regulators.[224] Indeed, most MLATs require that a request be processed through a Central Authority, which is designated in each MLAT.[225] Generally, each country designates the Ministry of Justice or the Attorney General to carry out this position.[226] For instance, in all MLATs to which the United States is a signatory, either the Attorney General, who serves as head of the DOJ,[227] or his designee serves as the Central Authority;[228] but using the Central Authority is not an effective process in international securities enforcement because securities regulators cannot directly make a request to foreign counterparts.[229] Such bureaucracy in the requesting process can also delay the execution of assistance. Indeed, in order to use MLATs to obtain information from a foreign securities agency, the SEC must ask the DOJ to make a request so that the DOJ may then forward the request to the designated

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221. *See* IOSCO Annual Conference, *supra* note 219.

222. OFFICE OF INT'L AFFAIRS, *supra* note 23, at 5; *see also* Mann et al., *supra* note 157, at 323–24.

223. *See, e.g.*, U.S.-Switz. MLAT, *supra* note 27, ch. I, art. 4, para. 2; U.S.-H.K. MLAT, *supra* note 27, art. 3, para. 1(d); U.S.-S. Korea MLAT, *supra* note 27, art. 3, para. 1(d); *see* Beard, *supra* note 129, at 273–74.

224. *See* Beard, *supra* note 129, at 273 & n.14, 274.

225. *See, e.g.*, U.S.-Switz. MLAT, *supra* note 27; U.S.-Can. MLAT, *supra* note 27, arts. I, VI, para. 1; U.S.-U.K. MLAT, *supra* note 27, art. 2; U.S.-H.K. MLAT, *supra* note 27, art. 2; U.S.-S. Korea MLAT, *supra* note 27, art. 2.

226. Harris, *supra* note 193, at 140.

227. 28 U.S.C. § 503 (2006).

228. *See, e.g.*, U.S.-Switz. MLAT, *supra* note 27, ch. VII, art. 28, para. 1; U.S.-Can. MLAT, *supra* note 27, art. I; U.S.-U.K. MLAT, *supra* note 27, art. 2, para. 2; U.S.-H.K. MLAT, *supra* note 27, art. 2, para. 2; U.S.-S. Korea MLAT, *supra* note 27, art. 2, para. 2; *see also* U.S. DEP'T. OF JUSTICE, Title 9 Criminal Resource Manual 276: Treaty Requests, UNITED STATES ATTORNEYS' MANUAL, http://www.justice.gov/usao/eousa/foia_reading_room/usam/title9/crm00276.htm.

229. Beard, *supra* note 129, at 274.

Central Authority of a foreign country rather than to the agency with the relevant expertise and knowledge.[230] In recent years, as securities law enforcement has increasingly required prompt action,[231] this process has become particularly problematic.

Securities regulators have another option besides using MLATs: namely, to bring a civil action in a foreign court and thereby seek to freeze illegal proceeds.[232] This method suffers from its own difficulties. If the SEC opts to use this method, it may be exposed to risks of litigation, in addition to facing difficult situations wherein a foreign court may require the SEC to pay financial undertakings for the filing of injunctions.[233] Indeed, in *SEC v. Lydia Capital*,[234] the SEC was faced with legal challenges that compelled it to pay financial undertakings.[235]

2. Need for the MOU Approach

To overcome the deficiencies in using the two methods mentioned above, securities regulators should enter into MOUs that require them to take all necessary steps to assist their foreign counterparts in obtaining asset freezes where the assets are located.[236] If securities regulators use MOUs instead of MLATs or civil actions, enforcement cooperation can be more effective, because securities regulators can directly communicate with one another to freeze assets abroad.[237] Indeed, when entering into these types of MOUs, authorities specializing in

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230. *See* U.S.-Switz. MLAT, *supra* note 27, ch. VII, art. 28; U.S.-Can. MLAT, *supra* note 27, art. VI, para. 1; U.S.-U.K. MLAT, *supra* note 27, art. 2; U.S.-H.K. MLAT, *supra* note 27, art. 2; U.S.-S. Korea MLAT, *supra* note 27, art. 2.

231. *See* Friedman et al., *supra* note 21, at 48.

232. IOSCO Annual Conference, *supra* note 219.

233. *Id.*

234. SEC v. Lydia Capital, No. 07-10712-RGS, 2008 WL 509136 (D. Mass. Feb. 21, 2008).

235. *SEC Obtains Asset Freeze in the United Kingdom Against Hedge Fund Principal*, GIBSON DUNN (June 25, 2008), *available at* http://www.gibsondunn.com/publications/Pages/SECAssetFreezeInUKAgainstHedgeFundPrincipal.aspx.

236. *See* Mann et al., *supra* note 157, at 326 (arguing that the MOU would be a useful tool for "enforcing provisional orders and final judgments"); *see also* Friedman et al., *supra* note 21, at 50 (calling for international assistance in freezing assets).

237. *See* IOSCO Annual Conference, *supra* note 219 (illustrating Canadian experience in cross-border asset-freezing assistance).

securities laws can directly negotiate and administer agreements so as to close the differences in securities enforcement regimes.[238] In addition, by directly communicating under MOUs, securities regulators can more quickly help freeze assets than they can under MLATs, which require an indirect and bureaucratic process.[239] Even so, MOUs signed by the United States with Canada, the U.K., and Hong Kong do not currently have explicit provisions to assist in freezing assets abroad.[240] The IOSCO MMOU, likewise, does not require asset freezing assistance.[241] Considering the benefits of direct cooperation, however, MOUs, including the IOSCO MMOU, should incorporate asset freezing assistance in some way.[242]

3. Need for the Enhanced Domestic Authority of the U.S. SEC

The scope of "asset freezing assistance" can be broad, from non-substantive assistance—for example, merely explaining the asset-freezing process[243]—to substantive assistance—such as obtaining asset freezes on behalf of a foreign authority.[244] Complicating matters, many securities regulators cannot currently provide substantive assistance to their foreign counterparts.[245] Indeed, most securities regulators may only be able to provide information about the domestic legal framework—as was the case when the U.K. Financial Services Authority ("U.K. FSA" or "FSA") provided it to the SEC in *Lydia Capi-*

238. *See* Mann et al., *supra* note 157, at 327.

239. *See* IOSCO Annual Conference, *supra* note 219 (addressing efficiency in asset-freezing assistance provided by Canadian regulators); *see also* Mann et al., *supra* note 157, at 326–27.

240. *See generally* U.S.-U.K. MOU, *supra* note 140; U.S.-Can. MOU, *supra* note 139; U.S.-H.K. MOU, *supra* note 141.

241. *See generally* IOSCO MMOU, *supra* note 156.

242. *See* Mann et al., *supra* note 157, at 327–28 (discussing that a possible MOU without asset-freezing assistance thwarts prosecution efforts to seize profits retained outside the United States, and describing how a potential MOU requiring asset-freezing assistance could operate).

243. *See, e.g.*, GIBSON DUNN, *supra* note 235 (describing how the U.K.'s FSA assisted the SEC in freezing assets in *Lydia Capital*).

244. *See, e.g.*, IOSCO Annual Conference, *supra* note 219.

245. *See* INT'L ORG. OF SEC. COMM'N'S PRESIDENTS COMM., RESOLUTION ON CROSS-BORDER COOPERATION TO FREEZE ASSETS DERIVED FROM SECURITIES AND DERIVATIVES VIOLATIONS 1 (June 7, 2006), http://www.iosco.org/library/resolutions/pdf/IOSCORES25.pdf [hereinafter IOSCO PRESIDENTS COMM.]; *see also* IOSCO Annual Conference, *supra* note 219.

tal[246]—or, at most, to provide information about other channels such as criminal authorities or private law firms. Thus, even if securities regulators change their MOUs to include asset freezing assistance, the difficulties in freezing assets abroad will not necessarily be eliminated.[247] This is primarily because most securities regulators, including the SEC, "still lack sufficient powers to freeze ill-gotten assets on behalf of a foreign regulator."[248] Because of this, the foreign regulator must work through criminal channels or private law firms to accomplish any asset freezing in the United States; however, these channels are either ineffective or risky, as discussed above.[249]

For this reason, the U.S. Congress should consider authorizing the SEC to go to court in the name of foreign authorities to obtain asset freezes.[250] Along with this authority of representation, the SEC can provide substantive assistance under MOUs, enhancing international cooperation accordingly.[251]

Indeed, securities regulators have recognized the importance of the authority to seek asset freezes on behalf of foreign regu-

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246. In this case, the SEC requested the FSA to provide legal advice. GIBSON DUNN, *supra* note 235. This advice aided the SEC in understanding the English legal system. *See id.* The SEC then directly brought a civil action in the U.K. High Court, arguing that the assets should remain frozen. SEC Obtains Asset Freeze in the United Kingdom Against Hedge Fund Manager, SEC Litigation Release No. 20585 (May 19, 2008), *available at* http://www.sec.gov/litigation/litreleases/2008/lr20585.htm; Aaron Helm, *U.S. SEC v. Manterfield: How Her Majesty's Courts Assisted the SEC in the Fight Against Global Financial Fraud*, 18 TUL. J. INT'L & COMP. L. 523, 524 (2010) (citing U.S. SEC v. Manterfield, [2008] EWHC (QB) 1349, Lloyd's Rep. F.C. 477 (Eng.)).

247. *See* IOSCO PRESIDENTS COMM., *supra* note 245, at 1; *see also* IOSCO Annual Conference, *supra* note 219.

248. *See* IOSCO PRESIDENTS COMM., *supra* note 245, at 1; IOSCO Annual Conference, *supra* note 219.

249. *See* Beard, *supra* note 129, at 273–74 (discussing the ineffectiveness of MLATs); *see also* IOSCO Annual Conference, *supra* note 219 (discussing problems in filing civil proceedings in a foreign country). For the details of this discussion, see *supra* Part III.A.1.

250. *See, e.g.*, Securities Act, R.S.O. 2011, c. S.5, § 126(1)(b) (Can.) (granting the Ontario Securities Commission the legal authority to temporarily freeze assets in Canada on behalf of foreign authorities).

251. *See* IOSCO Annual Conference, *supra* note 219 (calling for "increasing the abilities of securities regulators to freeze and repatriate assets on behalf of foreign counterparts").

lators.[252] In 1992, Michael D. Mann, who was the Director of the SEC Office of International Affairs, argued in an article that cooperation in enforcing provisional orders would benefit from MOU approaches,[253] and that "the foreign authority, pursuant to both the MOU and domestic law, would petition its courts or proper authorities for relief on behalf of the SEC."[254] In 2003, Ethiopis Tafara, the current Director of the SEC Office of International Affairs, also contended that "the next bold step for securities regulators in their fight against cross-border financial crime . . . is increasing the ability of securities regulators to freeze and repatriate assets on behalf of foreign counterparts."[255]

As did the domestic regulators, IOSCO recognized in 2006 that substantive assistance in freezing assets was crucial for effective cooperation in securities enforcement,[256] and reported that "many jurisdictions still lack sufficient powers to freeze illgotten assets on behalf of a foreign regulator."[257] IOSCO, therefore, encouraged "[a]ll member regulators . . . to examine the legal framework under which they operate and strive to develop, through law reform or otherwise, mechanisms by which they or another authority within their jurisdiction could, on behalf of foreign regulator, freeze assets derived from suspected and established cross-border securities and derivatives violations."[258]

Furthermore, in 2008 the SEC entered into an enhanced enforcement MOU with the Australian Securities and Investment Commission ("ASIC"),[259] which addressed the matters of freezing assets abroad and restraining the distribution of illegal profits. [260] Specifically, this MOU provided that "[e]ach

252. *See generally* Mann et al., *supra* note 157; IOSCO Annual Conference, *supra* note 219.

253. Mann et al., *supra* note 157, at 326.

254. *Id.* at 328.

255. IOSCO Annual Conference, *supra* note 219.

256. IOSCO PRESIDENTS COMM., *supra* note 245, at 1.

257. *Id.*

258. *Id.* at 2; *see also* TECHNICAL COMM., INT'L ORG. OF SEC. COMM'N, AN OVERVIEW OF THE WORK OF THE IOSCO TECHNICAL COMMITTEE 12 (Mar. 2007), http://www.iosco.org/library/pubdocs/pdf/IOSCOPD239.pdf.

259. PICKHOLZ, *supra* note 137, § 4:7.50.

260. Memorandum of Understanding Concerning Consultation, Cooperation and the Exchange of Information Related to the Enforcement of Securities Laws, U.S.-Austl., art. 3, Aug. 25, 2008, *available at*

[a]uthority . . . [confirm] its commitment to seek the legal authority to assist the other [a]uthority in freezing assets in its jurisdiction that constitute proceeds of a possible violation of [l]aws and/or [r]egulations, and [to] facilitate restitution to investors."[261] Christopher Cox, who was Chairman of the SEC at that time, explained that under this enhanced enforcement MOU "the SEC and ASIC are . . . committed to seeking asset freezes on each other's behalf, and to assisting with the restitution of funds to injured investors."[262]

Despite a series of efforts, however, the SEC still lacks the legal authority to obtain asset freezes on behalf of foreign authorities.[263] Indeed, the SEC cannot provide any substantive assistance in freezing assets even if MOUs are arranged.[264] This is primarily because the Exchange Act has no explicit provision authorizing the SEC to seek asset freezes on behalf of foreign regulators. In the context of information sharing, the SEC has the firm legal authority to obtain information on behalf of foreign authorities, thus allowing it to substantively cooperate with its foreign counterparts under MOUs.[265] Until 1988, however, the SEC had not been able to use its investigative power to assist foreign authorities[266] because "§ 21(a) of the Exchange Act, in its original version, limited the SEC's ability

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http://www.sec.gov/about/offices/oia/oia_mututal_recognition/australia/enhanced_enforcement_mou.pdf [hereinafter U.S.-Austl. MOU].

261. *Id.*

262. Christopher Cox, Chairman, SEC, Speech at the International Enforcement Institute: The Importance of International Enforcement Cooperation in Today's Markets (Nov. 7, 2008), http://www.sec.gov/news/speech/2008/spch110708cc.htm.

263. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO/GGD-92-110, SECURITIES AND FUTURES MARKETS: CROSS-BORDER INFORMATION SHARING IS IMPROVING, BUT OBSTACLES REMAIN 48 (1992), *available at* http://www.gao.gov/assets/160/152094.pdf [hereinafter GAO REPORT]. Many securities regulators lack this power. IOSCO Annual Conference, *supra* note 219.

264. *See* GAO REPORT, *supra* note 263, at 48; *see also* IOSCO Annual Conference, *supra* note 219.

265. Mann et al., *supra* note 157, at 319–20; *see also* Securities and Exchange Commission Historical Society Interview with Ethiopis Tafara Conducted on April 19, 2006 by Wayne Carroll, at 2, *available at* http://c0403731.cdn.cloudfiles.rackspacecloud.com/collection/oral-histories/tafara041906Transcript.pdf.

266. Mann et al., *supra* note 157, at 318–19.

to investigate violations of 'this Title.'"[267] In order to solve this problem, Congress added Section 21(a)(2) to the Exchange Act, thereby authorizing the SEC to conduct investigations for the purpose of gathering evidence and information for foreign securities regulators.[268] In the context of asset freezing assistance, however, the Exchange Act does not yet provide the SEC with explicit legal authority to act on behalf of foreign authorities.[269] The ability to obtain a court order to freeze assets on behalf of foreign regulators will enable the SEC to provide substantive assistance in freezing assets, thereby enhancing international cooperation.[270]

For example, the Ontario Securities Act of Canada grants the Ontario Securities Commission ("OSC") the legal authority to temporarily freeze assets in Canada on behalf of foreign authorities.[271] Foreign securities regulators can thus take advantage of this representing authority in Canada by requesting the OSC to exercise its power to freeze assets on a temporary basis.[272] Therefore, cross-border securities enforcement will be far more effective if all other securities regulators also obtain the power to obtain asset freezes on behalf of their foreign counterparts.[273]

The U.S. Congress, therefore, ought to consider passing legislation that gives the SEC power to seek asset freezes in a U.S. court in the name of foreign regulators.[274] These regulators can then take advantage of this authority by requesting the SEC to exercise it.[275] Furthermore, such legislation can encourage other countries to adopt similar provisions.[276] If the SEC and foreign securities regulators have the legal authority to obtain as-

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267. *Id.* at 319 n.68; *see also* Securities Exchange Act of 1934 § 21(a), 48 Stat. 899.

268. *See* 15 U.S.C. § 78u(a)(2) (2006); *see also* Friedman et al., *supra* note 21, at 40; Mann et al., *supra* note 157, at 319.

269. *See* GAO REPORT, *supra* note 263, at 48; *see also* IOSCO Annual Conference, *supra* note 219.

270. *See* IOSCO PRESIDENTS COMM., *supra* note 245, at 1; *see also* IOSCO Annual Conference, *supra* note 219.

271. Securities Act, R.S.O. 2011, c. S.5, § 126(1)(b) (Can.).

272. OFFICE OF INT'L AFFAIRS, *supra* note 23, at 5.

273. *See* IOSCO Annual Conference, *supra* note 219; *see also* IOSCO PRESIDENTS COMM., *supra* note 245, at 1.

274. *See, e.g.*, Securities Act, R.S.O. 2011, c. S.5, § 126(1)(b) (Can.).

275. *See* OFFICE OF INT'L AFFAIRS, *supra* note 23, at 5.

276. Mann et al., *supra* note 157, at 329.

set freezes on each other's behalf, they can then maximize the benefits of MOUs providing for asset freezing assistance.[277]

B. Requiring Exchange of a Broader Range of Information

To ensure more effective cooperation, the IOSCO MMOU needs to explicitly require signatories to obtain telephone or Internet records necessary for foreign counterparts' investigations.[278] The ability to obtain such information is crucial in successfully combatting international insider trading, for telephone records and Internet service histories often provide authorities with crucial evidence of insider trading.[279] Specifically, in *United States v. Rajaratnam*, telephone conversations, instant messages, and emails exchanged between Raj Rajaratnam and other defendants showed that he obtained inside information from various sources, and either disclosed that information as a tip, or traded stock based on it.[280] Thus, many authorities have recently sought a range of information broader than what the MMOU allows, particularly when these authorities are investigating insider trading.[281]

Despite the need for a broader range of information, there is no explicit provision of the MMOU that allows securities regulators to seek telephone and Internet records from foreign authorities.[282] This limitation of the MMOU may impede effective enforcement cooperation among signatories, inasmuch as they would have to seek the same information through other mech-

277. *See id*.

278. *See* CARVAJAL & ELLIOTT, *supra* note 142, at 16 (stating that telephone and Internet records can be crucial evidence in insider trading cases).

279. *Id*.

280. *See* United States v. Rajaratnam, 802 F. Supp. 2d 491, 499–500, 502, 507–12, 514–16 (S.D.N.Y. 2011); *see also* Tzyh Ng, *The Voice of the Galleon Trial*, N.Y. TIMES (May 11, 2011), http://dealbook.nytimes.com/2011/05/11/the-voices-of-the-galleon-trial/ (indicating links to the telephone recordings regarding insider trading); *see also* Douglas N. Greenburg et al., *Prosecutors Without Borders: Emerging Trends in Extraterritorial Enforcement*, PRACTICING LAW INSTITUTE CORPORATE LAW AND PRACTICE COURSE HANDBOOK SERIES, 1882 PLI/CORP 149, 167–68 (2011), *available at* http://www.lw.com/upload/pubContent/_pdf/pub4122_1.pdf.

281. *See* CARVAJAL & ELLIOTT, *supra* note 142, at 17 (describing a case where telephone records served as an important source of evidence). *See generally* IOSCO MMOU, *supra* note 156, art. 7(b)(ii) (specifying the types of information that should be obtained under the IOSCO MMOU).

282. *See generally* IOSCO MMOU, *supra* note 156, art. 7(b)(ii).

anisms. One such option for obtaining telephone and Internet records is to use a bilateral MOU that has been arranged between regulators.[283] The bilateral MOUs, however, cannot cover a broad range of jurisdictions.[284] A second path to acquiring telephone and Internet information might be to use MLAT procedures,[285] though these are limited to criminal cases.[286] The last option for obtaining that information involves using informal channels;[287] however, with respect to these informal methods, reliability and cooperativeness are often uncertain, making it difficult to anticipate whether the information is obtainable. For this reason, the IOSCO MMOU should contain an explicit provision requiring signatories to obtain telephone or Internet records for assistance.

CONCLUSION

This article has discussed international cooperation in securities enforcement, with particular emphasis placed on detecting, investigating, and prosecuting hedge fund fraud and market manipulation. It has revealed several concerns about current international enforcement systems for cross-border hedge fund fraud. A major concern is that the current MOUs have not been effective in combatting multinational hedge fund fraud.[288] Thus, this article calls for revisions of the MOUs. Specifically, bilateral MOUs and the IOSCO MMOU should explicitly pro-

283. Except for an MOU signed between the SEC and an Australian regulator, bilateral MOUs do not usually contain an explicit provision requiring exchange of telephone or Internet records. *See* U.S.-Austl. MOU, *supra* note 260, at 9; *see also* U.S.-U.K. MOU, *supra* note 140; U.S.-Can. MOU, *supra* note 139; U.S.-H.K. MOU, *supra* note 141; *see also SEC International Enforcement Assistance*, *supra* note 25.

284. The SEC entered into MOUs with only twenty different countries' authorities before IOSCO created the MMOU. *SEC International Enforcement Assistance*, *supra* note 25. Indeed, the SEC has no bilateral MOU with any Korean securities regulator. *See* SEC, *Cooperative Arrangements with Foreign Regulators*, *supra* note 24. By contrast, the number of full signatories of the IOSCO MMOU currently stands at ninety-seven. *Current Signatories*, *supra* note 26.

285. *See* Friedman et al., *supra* note 21, at 42.

286. *See* Greene, *supra* note 131, at 640 (stating that MLATs can be employed only for criminal cases).

287. *See* OFFICE OF INT'L AFFAIRS, *supra* note 23, at 4; *see also SEC International Enforcement Assistance*, *supra* note 25.

288. *See supra* Part III.

vide assistance in freezing assets.[289] The IOSCO MMOU should also be reformed by requiring that telephone records and Internet service history be shared.[290] These recommendations would provide guidance for international enforcement systems in order to promote a more cooperative environment.

289. *See supra* Part III.A.
290. *See supra* Part III.B.