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 PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF

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Respondents' brief in opposition to the petition underscores the need for review by this Court. First, Respondents conveniently disregard that the Fifth, Seventh and District of Columbia Circuits have held and the Securities Exchange Commission ("SEC") has found that a fundamental split exists among the circuits in devising and applying the conduct test.

Second, contrary to Respondents' attempts to harmonize the Second Circuit's decision with other circuits, it is clear that Petitioners would have prevailed under the conduct test standards adopted by the Third, Fifth, Seventh, Eighth and Ninth Circuits.

Third, Respondents do not dispute that this Court has *never* addressed the conduct test. Their attempt to analogize this securities case to this Court's authority construing the extraterritorial applicability of the antitrust and patent laws is unavailing.

Fourth, Respondents evade the SEC's conclusion in its Second Circuit amicus brief that the court should exercise subject matter jurisdiction here because of the "material and substantial conduct in furtherance of" the securities fraud that occurred in the United States.[1] App. 49a-50a. In any event, *Petitioners respectfully request that this Court solicit the opinion of the SEC with respect to the issues raised in this petition.*

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1. Notwithstanding Respondents' attempt to soften the alleged allegations of fraud as nothing more than "mistakes" and "estimates", the SEC clearly found that the allegations of the Complaint alleged a legitimate, viable fraud. App. 75a-76a.

1. As their lead argument in opposition to the petition, Respondents posit that "[t]he decision of the court of appeals does not conflict with any decision of another court of appeals." Brief For Respondents In Opposition ("Resp.") 2. However, this argument ignores: (a) the explicit holdings of the Fifth, Seventh and District of Columbia Circuits and the opinion of the SEC that a serious conflict exists among the circuits in applying the conduct test; and (b) the Second Circuit's decision does, in fact, conflict with the holdings of other courts of appeals.

The courts of appeals have acknowledged the split among the circuits. In the words of the Fifth Circuit,, "*[t]he circuits are divided* as to precisely what sort of activities are needed to satisfy the conduct test . . . ." *Robinson v. TCI/US W. Commc'ns, Inc.*, 117 F.3d 900, 905 (5th Cir. 1997)(emphasis added).

Similarly, the Seventh Circuit has held that "the circuits that have confronted the [conduct test] have articulated a *number of methodologies.*" *Kauthar SDN BHD v. Sternberg*, 149 F.3d 659, 665-66 (7th Cir. 1998)(emphasis added) (analyzing spectrum of holdings, with the District of Columbia Circuit taking the most restrictive approach, the Third, Eighth and Ninth Circuits taking the most permissive approach, and the Second and Fifth Circuits setting a "course between the two *extremes*")(emphasis added).

Finally, Judge Bork in *Zoelsch v. Arthur Andersen & Co.*, 824 F.2d 27 (D.C. Cir. 1987), analyzed the split among the circuits and observed that "[t]he Second Circuit has set the most *restrictive* standard", *id.* at 303,

while "[t]he Third, Eighth and Ninth Circuits appear to have *relaxed* the Second Circuit's test." *Id.* at 304 (emphasis added).

Put most simply, how can there be "divisions" or "extremes" among the circuits without a clear conflict?

Similarly, the SEC, in its amicus brief submitted in this action at the request of the Second Circuit, also found that there is a significant split among the circuits. App. 55a-56a (citing *Kauthar* and analyzing the distinct and competing conduct test methodologies adopted, respectively, by: (a) the District of Columbia Circuit; (b) the Second, Fifth and Seventh Circuits; and (c) the Third, Eighth and Ninth Circuits).

Commentators also have observed this split. *See, e.g.*, Hannah L. Buxbaum, *Multinational Class Actions Under Federal Securities Laws: Managing Jurisdictional Conflict*, 46 Colum. J. Transnat'l L. 14, 17 (2007) (in discussing the effects and conduct tests, the author notes that the "lower federal courts apply in *inconsistent and therefore unpredictable ways* a pair of judicially created jurisdictional tests that are now almost 40 years old") (emphasis added).

This case would permit the Court to resolve the split among the circuits and create a uniform jurisdictional test to guide the lower courts on an issue whose importance grows more patent day by day, as the world economy crumbles and the number of transnational securities fraud claims grows.

2. The decision of the Second Circuit at issue here does conflict with the decisions of other circuits. As Respondents acknowledge, the Second Circuit essentially held that the locus of the alleged *misrepresentation* was critical and determined whether subject matter jurisdiction existed, rather than the locus of the *overall conduct* that comprised the fraud. Resp. 9-10; App. 19a.

This definition of the conduct test now puts the Second Circuit in the camp of Judge Bork's narrow explanation of the conduct test for the District of Columbia Circuit in *Zoelsch*, 824 F.2d at 31 (the domestic conduct at issue must itself constitute a securities violation).

Contrary to Respondents' analysis (Resp. 15-18), the holding of the Second Circuit that the locus of the misrepresentations controls for purposes of the conduct test directly contravenes the holdings reached by the Third, Fifth, Seventh, Eighth and Ninth Circuits. These latter circuits, if they focus on the locus of misrepresentations at all, view the misrepresentations as one factor in context of defendants' overall fraudulent conduct in the United States.

Put differently, the Fifth and Seventh Circuits have adopted a "proximate cause" or "directly caused" conduct test. *See Robinson*, 117 F.3d at 905 (Fifth Circuit adopted "[t]he more restrictive position that the domestic conduct must have been 'of material importance to' or have 'directly caused' the fraud complained of. . ."); *Kauthar*, 149 F.3d at 667 (Seventh Circuit holding that "[w]e believe, therefore, that federal

courts have jurisdiction over an alleged violation of the antifraud provisions of the securities laws when the conduct occurring in the United States directly causes the plaintiff's alleged loss. . .").[2]

The Third, Eighth and Ninth Circuits have adopted a looser "in furtherance of"/"but for" conduct test. Thus in *SEC v. Kasser*, 548 F.2d 109 (3d Cir.), *cert. denied*, 431 U.S. 938 (1977), the Third Circuit held that "[t]he federal securities laws, in our view, do grant jurisdiction in transnational securities cases where at least *some activity* designed to further a fraudulent scheme *occurs* within this country." *Id.* at 114. *See also Continental Grain (Austl.) Pty. Ltd. v. Pacific Oilseeds, Inc.*, 592 F.2d 409, 415 (8th Cir. 1979) (Eighth Circuit adopted identical standard); *Grunenthal GmbH v. Hotz*, 712 F.2d 421 (9th Cir. 1983) (Ninth Circuit adopted identical standard).

Here, the Florida-based individual defendants conceived the fraudulent scheme in Florida, perpetrated the fraud in Florida by manipulating the assumptions in HomeSide Lending's MSR valuation models, generated the fraudulent financials using those models

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2. Older Second Circuit decisions also applied this "directly caused" test. *See, e.g., SEC v. Berger*, 322 F.3d 187, 193 (2d Cir. 2003)(subject matter jurisdiction exists where "the activities or culpable failures to act within the United States 'directly caused' the claimed losses"); *Itoba Ltd. v. Lep Group PLC*, 54 F.3d 118, 122 (2d Cir. 1995)(same). However, this is irrelevant as there are still at least three competing conduct test rules: (1) the conduct itself must be a violation of the securities laws; (2) the conduct must "proximately cause" the violation; or (3) the conduct must be part of a "but for" chain causing the violation.

and then transmitted that fraudulent data to Australia knowing that it would be ministerially and automatically incorporated into its parent's financials. As the SEC concluded, "the domestic conduct was an integral link in the chain of events to the overseas investors' losses." App. 75a-76a.

Another case dealing with Australia highlights the problem. The Eighth Circuit in *Continental Grain (Austl.) Pty Ltd.* found subject matter jurisdiction under the conduct test because "[e]ven though the ultimate effect . . . was felt in Australia, *the fraudulent scheme of nondisclosure was devised and completed in the United States. Then it was 'exported' to Australia.*" 592 F.2d at 420 (emphasis added). These words describe the instant case exactly. If this Court's role is in no small part is to harmonize federal law so that a federal case in St. Louis with Australian parties is treated the same as a federal case in New York City with Australian parties, then the aforementioned split among the circuits leads to a conflict that warrants this Court's review.

Respondents, in a footnote, argue that alleged Ponzi schemes, such as those run by Madoff and Stanford, "fall well within the scope of the conduct test in any of the circuits". Resp. 17 n.8. However, this simply is not true. For example, assuming that: (a) Madoff, based in New York, used a publicly-traded entity based in Australia as a "feeder fund" that solicited investments for Madoff from Australians, and (b) Australians brought a lawsuit against the Australian entity in New York based on misrepresentations that entity made only in Australia, subject matter jurisdiction would not exist in the Second Circuit because the locus of the

misrepresentations occurred in Australia. The Second Circuit would ignore, as it did in the case below, the salient fact that the case "involved a fraudulent transnational investment scam controlled, masterminded and implemented from New York", Resp. 17 n.8, in the case of Madoff or from Florida in the case of HomeSide Lending. Indeed, *this* case would be even stronger given that the fraudulent conduct in Florida was coupled with the trading of National Australia Bank's American Depository Receipts ("ADRs") on the New York Stock Exchange.[3]

3. Respondents also argue that "[p]etitioners and their amicus make no suggestion that the decision below conflicts with any decision of this Court. . . ." Resp. 20-21. However, this argument misses the central point that *this Court has never addressed the conduct test.* As one commentator noted:

> Considering the stakes involved, one might expect the scope of subject-matter jurisdiction under the federal securities laws would by now be firmly established. Quite the opposite is true. Congress has enacted no legislation on the point, [and] *the Supreme Court has declined to address the question. . . .*

Hannah L. Buxbaum, *Multinational Class Actions Under Federal Securities Laws: Managing Jurisdictional Conflict*, 46 Colum. J. Transnat'l L. 14, 17 (2007) (emphasis added; footnote omitted).

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3. Respondents try to ignore the ADRs because there are no surviving plaintiffs who purchased ADRs whereas it remains an important jurisdictional issue to be weighed by the Court and shows the volitional conduct of NAB in the United States.

Respondents attempt to sidestep this crucial fact by citing to two non-securities cases: *F. Hoffman-La Roche, Ltd. v. Empagran S.A.*, 542 U.S. 155 (2004), an antitrust case, and *Microsoft Corp. v. AT&T Corp.*, 550 U.S. 437 (2007), a patent case. Neither decision applies to the issues raised in this petition.

Empagran S.A. was founded on the Court's perception that Congress, in enacting the Sherman Act, was primarily concerned with regulating the domestic economy, such that foreign anti-competitive injury wholly separate from any such domestic injury is not redressable under the Sherman Act. 542 U.S. at 165-66. However, the securities laws are concerned not only with cleansing domestic securities markets of fraud, but also, as Judge Friendly held years ago, preventing the exportation of fraud from the United States. *ITT v. Vencap, Ltd.*, 519 F.2d 1001, 1017 (2d Cir. 1975) ("We do not think Congress intended to allow the United States to be used as a base for manufacturing fraudulent security devices for export even when these are peddled only to foreigners"). Application of the Sherman Act to purely foreign economic injury threatens interference with other countries' internal economic policy arrangements that may diverge from American-style capitalism in a way that providing a fraud claim to foreign citizens injured by a fraud formulated and conducted in the United States does not.

In *Microsoft Corp.*, this Court expressed its particular reservations over the worldwide application of the United States patent regime, to the detriment of other countries' patent laws. 550 U.S. at 455. But again, that is a different matter from giving foreign citizens redress in United States courts for fraudulent conduct that occurred in the United States.

4. Respondents attempt to dismiss the SEC's analysis by arguing that the amicus brief was limited to "intra-circuit splits." Resp. 25. This argument ignores two salient facts. First, the SEC did opine on the split among the circuits. App. 55a-56a. Second, the SEC primarily focused on Second Circuit case law in obvious recognition that the Second Circuit "is bound by prior precedent . . . ." App. 55a n.2. For this reason alone, Petitioners respectfully request that the Court seek the views of the SEC on the issues raised by this petition.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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