ARTICLES

Private international law and finance: nothing special?

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Abstract

Financial firms, such as banks or investment funds, often claim that their activities are special and therefore cannot be subject to the ordinary rules of conflict of laws. Is this argument merely self-serving, or are there indeed peculiarities that justify special conflicts rules? This is the question that this article seeks to answer. Its focus is on the private international law rules that determine the law which is applicable to obligations, both contractual and non-contractual. In order to broaden the basis of investigation and to avoid a narrow EU perspective, it will also look at US law.

1. Introduction

Financial law is an extraordinarily complex subject. Private internationalists will however be sceptical as to the need for special treatment. They would rather break down the area into its different components: contract law, tort law, property law, insolvency law, and public law insofar as regulation and supervision are concerned. For them, it is simply a matter of characterizing the issue to be decided and applying the appropriate jurisdiction and conflict-of-laws rule to identify the forum and the governing law.

The question this article seeks to answer is if there are nevertheless some particularities of financial law that merit special treatment in a conflict-of-laws setting and therefore require particular attention by conflicts lawyers. This question will be analysed against the backdrop of the United States, where such a special rule exists (section 2). The article then proceeds to European conflicts rules on obligations in general (section 3), and more particularly in the area of contracts (section 4) and torts (section 5).

2. The US experience: conflict of laws as an annex to regulation

The US is well known for its bewildering variety of different conflict of laws approaches that are the result of the absence of federal rules on the subject.[1] Yet much of financial law, better known

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1 See S.C. Symeonides, 'The American Choice-of-Law Revolution in the Courts: Today and Tomorrow', *Collected Courses of the Hague Academy of International Law*, vol. 298, Leiden: Martinus Nijhoff Publishers 2002; S. Symeonides, *The American Choice-of-Law Revolution: Past, Present and Future*, Leiden: Martinus Nijhoff Publishers 2006. See also the annual survey by the same author, lastly S.C. Symeonides, 'Choice of Law in the American Courts in 2016: Thirtieth Annual Survey', *American Journal of Comparative Law* (65) 2017, p. 1.

as 'securities law' in American parlance, is implemented at the federal level. A principle that has a bearing on the determination of the applicable law has indeed been developed.

2.1 The Morrison *case*

This principle has been expounded in the landmark judgment *Morrison* v. *National Australia Bank*.[2] In this case, Justice Scalia brought to prominence the 'presumption against extraterritoriality', according to which 'legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States'.[3] Since it is restricted to US law, this principle is not a multilateral conflict-of-laws rule. It is not even a unilateral conflicts rule given that it is a mere presumption that can be overridden legislatively. Rather, it is a hermeneutic maxim – or in the words of the Supreme Court: 'a canon of construction' – for the application of federal statutes.[4]

The presumption has overwhelming importance in the financial area because most financial disputes stem from federal legislative and regulatory rules. To illustrate this, the Securities Act and the Securities Exchange Act provide a private cause of action that allows individual plaintiffs to recover damages from violators of rules of financial regulation.[5] The underlying principle is 'regulation through litigation'.[6] This has important advantages: the need for administrative personnel is reduced and enforcement is much more stringent by giving individual claimants the right to pursue private remedies. The private individual who sues an issuer or financial intermediary not only serve its own personal interests, but also the public interest of safeguarding the honesty, transparency and reliability of financial markets, which is why such a litigant is sometimes likened to a 'private attorney general'.[7]

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2 *Morrison et al.* v. *National Australia Bank Ltd et al.* 561 US 247, 130 S.Ct. 2869 (2010).

3 Ibid., p. 255; citing *EEOC* v. *Arabian American Oil Co* 499 US 244, 248 (1991). The latter case already called the presumption 'a long-standing principle of Americal law'. However, it did not have nearly the same influence before the *Morrison* judgment.

4 For criticism of the rationale of the *Morrison* judgment, see the concurring opinion by Justice Stevens, 130 S.Ct. 2888-2892 (2010) as well as L. Brilmayer, 'The New Extraterritoriality: *Morrison v. National Australia Bank*, Legislative Supremacy, and the Presumption Against Extraterritorial Application of American Law', *Southwestern Law Review* 2010, p. 655 at pp. 663-670; R.W. Kirby, 'Access to the United States Courts by Purchasers of Foreign Listed Securities in the Aftermath of *Morrison v. National Australia Bank Ltd.*', *Hastings Business Law Journal* 2011, p. 233 at pp. 233-251; A.L. Parish, 'Evading Legislative Jurisdiction', *Notre Dame Law Review* (87) 2013, p. 1673 at pp. 1699-1700.

5 The most important among those rules is Rule 10b-5, promulgated by the Securities and Exchange Commission (SEC) under Sect. 10(b) of the Securities Exchange Act 1934. Other private causes of action can be found, for instance, in Sects. 11 and 12 of the Securities Act 1933 regarding false registration statements and liability in connection with prospectuses and communications and in Sect. 20A of the Securities Exchange Act 1934 for insider trading.

6 See W. Kip Viscusi, *Regulation through Litigation*, Washington: Brookings Institution Press and AEI 2004.

7 See W.B. Rubenstein, 'On What a Private Attorney General Is – And Why It Matters', *Vanderbilt Law Review* (57) 2004, p. 2129; B.G. Garth, I.H. Nagel and S. Plager, 'The Institution of the Private Attorney General: Perspectives from an Empirical Study of Class Action Litigation', *Southern California Law Review* (61) 1988, p. 353.

Because of the regulatory background underlying securities claims, American courts identify the geographical reach of any private cause of action with that of the legislative regulatory act in which it is contained. In this way, the scope of public and private law coincide. The determination of the law governing cross-border financial disputes thus becomes an annex to regulation. This is not to deny the continuing importance of conflict-of-laws rules in areas such as ordinary contract or tort law. But the rules hardly play any role for statutory causes of action, such as Section 10(b) Securities Exchange Act and Rule 10b-5 promulgated thereunder. The latter define their scope of international application without being subject to a prior determination of the applicable law. From a doctrinal viewpoint of private international law purism, one could say that these causes of action are accompanied by an implied unilateral conflicts rule making the applicable law coincide with the provision's territorial scope of application. But American courts do not venture into such theoretical questions. Instead, they simply determine whether the statutory cause of action is applicable or not.

2.2 Connecting factors

When interpreting the Securities Exchange Act, Justice Scalia identified two points of contact with the US that allowed the application of the Act. The dispute must concern either (1) the purchase and sales of securities in the US, or (2) securities listed on US national exchanges.[8] These factors need to be adapted to other acts on financial regulation that concern persons and not securities, such as the Investment Adviser Act.[9] Importantly, the investor's domicile is not among the criteria that require the application of American law according to Justice Scalia's opinion. A US investor buying a foreign issuer's securities that are exclusively listed on a foreign exchange would therefore not be able to invoke the protection of US securities laws.[10] This aligns with the SEC mantra that 'As investors choose their markets, they choose the laws and regulations applicable in such markets'.[11] Instead of using conflict-of-law rules, US law achieves the protection of US investors through specific regulatory registration requirements that apply to all foreign firms offering securities to US investors.[12]

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8 *Morrison et al.* v. *National Australia Bank Ltd. et al.*, p. 2886 (*supra* n. 2): 'whether the purchase or sale is made in the United States, or involves a security listed on a domestic exchange'. The question where a purchase or sale is made is one of the trickiest issues that the judgment has created. For an attempt at clarification, see *Absolute Activist Value Master Fund Ltd.* v. *Ficeto*, 677 F.3d 60, 67-68 (2d Cir. 2012) (ruling that a transaction takes place in the US when either (1) a party incurs irrevocable liability within the United States to purchase or deliver a security or (2) title to a security is transferred within the United States). On this problem, see also C. Calfee, 'Can't See the Forest for the Trees: Where Does a Purchase or Sale of Securities Occur', *American University Business Law Review* (2) 2012, p. 153 at p. 178.

9 A. Laby, 'Regulation of Global Financial Firms After Morrison v. National Australia Bank', *St. John's Law Review* (87) 2014, p. 561 at pp. 571 et seq.

10 See A. Reed, 'But I'm an American – A Text-Based Rationale for Dismissing F-Squared Securities Fraud Claims after Morrison v. National Australia Bank', *University of Pennsylvania Journal of Business Law* (14) 2011, p. 515 at pp. 532 et seq., 535 et seq.

11 SEC, Securities Act Release No. 33-6383 (1990).

12 See e.g. Regulation S adopted by the SEC, 17 CFR 230.901-905. This Regulation requires issuers with a certain number of US investors or that deploy direct marketing activities to the US to register with the SEC.

The presumption against extraterritoriality is designed exclusively for statutory liability. For contractual liability, any law may govern a contract under the principle of party autonomy. It is true that the Restatement (Second) on Conflict of Laws is reluctant in accepting a choice of law that has no substantial connection with the parties or the transaction.[13] Yet state law supersedes this limitation if certain thresholds are exceeded, which often occurs in financial disputes.[14] Notwithstanding the paramount role for free choice of law, the primary conflicts approach from a US perspective remains the *Morrison* rule. This is because the primary remedy in securities cases is statutory, not contractual.

2.3 Practical effects

The presumption against extraterritoriality ended decades of applying American law to disputes having little connection to the US.[15] Litigants from Europe and the rest of the world were attracted to the American courts as litigation hubs. They could seek to redress wrongs suffered abroad when their home jurisdictions either did not provide adequate remedies or litigation opportunities. After *Morrison*, the application of US law to primarily foreign parties and transactions will only become possible where Congress has explicitly authorized its extraterritorial application.

From a European perspective, the result is that US courts are no longer a viable venue to obtain damages for wrongs suffered elsewhere. Increasingly, US courts dismiss claims filed by foreign plaintiffs and suits between American investors and foreign issuers on the ground that US law is not applicable to the dispute according to the presumption against extraterritoriality.[16] Although Justice Scalia in *Morrison* insisted on the need to differentiate between

13 See Restatement (Second), 1971, § 187(2)(a).

14 See e.g. New York General Obligations Law, § 5-1401 (allowing the choice of a non-related law for contracts with obligations of a value of more than US$250,000).

15 On the old law, see S. Choi and A. Guzman, 'The Dangerous Extraterritoriality of American Securities Law', *Northwestern Journal of International Law & Business* 1996, p. 207. It has to be noted that the influence of the *Morrison* decision extends far beyond the area of finance and also affects such areas as private remedies for human rights violations and corrupt practices, see *Kiobel* v. *Royal Dutch Petroleum*, 133 S.Ct. 1659 (2013); *RJR Nabisco, Inc.* v. *European Community*, 136 S.Ct. 2090, 2101 (2016).

16 See *In Re Royal Bank of Scotland Group PLC Securities Litigation*, 765 F. Supp. 2d 327, 336-38 (S.D.N.Y. 2011), aff. 2d Cir. 2013 (holding that plaintiffs' residence and their US-based decisions to invest in foreign shares was insufficient to justify the application of US law); *Elliott Associates et al.* v. *Porsche Automobil Holding SE et al.*, 759 F. Supp. 2d 469, 473-76 (S.D.N.Y. 2010), aff. 2d Cir. 2014 (ruling that swaps tied to the price of foreign securities were 'transactions conducted upon foreign exchanges and markets' and thus not domestic); *Loginovskaya* v. *Batratchenko*, 936 F. Supp. 2d 357, 367-75 (S.D.N.Y. 2013) (ruling that the Commodity Exchange Act's antifraud provision did not apply extraterritorially to the Russian plaintiff's asserted private right of action since the contracts had been negotiated and signed in Russia); *Parkcentral Global Hub Ltd.* v. *Porsche Auto. Holdings SE*, 763 F.3d 198, 214-18 (2d Cir. 2014) (holding that plaintiff investors' allegations failed to invoke § 10(b) Securities Exchange Act and SEC Rule 10b-5 in a manner which was consistent with the presumption against extraterritoriality since the swaps at issue were entered into on a foreign exchange); *Phelps* v. *Stomber*, 883 F. Supp. 2d 188, 206-10 (D.D.C. 2012) (holding that securities claims did not fall within the regulatory scope of § 10(b) Securities Exchange Act since the Class B shares were purchased on Euronext Amsterdam); *Cornwell* v. *Credit Suisse Grp.*, 729 F. Supp. 2d 620, 623-27 (S.D.N.Y.

jurisdiction and applicable law,[17] the non-applicability of US law will regularly result in the dismissal of the claim. Indeed, it did so in *Morrison*, where the Supreme Court did not even consider the application of Australian law, although the latter patently had the most significant connection to the dispute. The reason behind this seemingly contradictory practice is the 'public law taboo', a principle developed in the case law according to which American courts cannot apply or enforce the public law provisions of a foreign sovereign.[18] Although this principle has been criticized, it is still a firm part of US jurisprudence. As a result, federal courts will not apply the securities law of another nation because it is imbued with public law.

This puts pressure on the EU: If it wants its securities law to be applied in transnational disputes, this must be done in the courts of the Member States. Yet national procedural laws in Europe still lag behind in effectiveness compared to the more plaintiff-friendly US law. There are, for instance, not enough adequate mechanisms for class actions, no possibilities for pre-trial discovery, and many Member States still prohibit or restrict contingency fee arrangements. These instruments are indispensable if small and unprofessional investors are to have a fair chance in court against financial behemoths. The EU needs to remedy those shortcomings urgently in order to fill the void that *Morrison* has left. It must recognize the weakness of its current private enforcement mechanism and provide its own remedies for securities cases, for instance through the introduction of efficient collective action mechanisms.

3. The EU system: the primacy of private international law over financial law

3.1 Applicability of the Rome I and II Regulations to financial obligations

The situation in Europe is very different from the US. In the EU, choice-of-law issues are determined primarily by general conflicts rules that apply to all categories of disputes, whether they are contractual or non-contractual. Indeed, European private international law (PIL) does not have a specific category of qualification for financial law. As the main sources, the Rome I and II Regulations apply to all types of obligations, including those based on statutory causes of action. This system could therefore be characterised as being 'PIL-driven', in contrast to the 'regulation-driven' approach in the US.

That does not mean that EU PIL necessarily applies in all financial disputes without any exception. Article 1(2)(d) Rome I[19] and Article 1(2)(c) Rome II[20] exclude 'obligations arising

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2010) (holding that *Morrison* foreclosed the application of § 10(b) Securities Exchange Act to any claims related to foreign securities trades executed on foreign exchanges – the Swiss Exchange in this case); *In re Alstrom*, 741 F. Supp. 2d 469, 472 (S.D.N.Y. 2010) (rejecting class action claims because the securities were purchased on a French exchange).

17 See *Morrison et al.* v. *National Australia Bank Ltd. et al.*, p. 2877 (*supra* n. 2).

18 *The Antelope*, 23 US (1 Wheat.) 66, 123 (1825) ('The Courts of no country execute the penal laws of another […]'); *Moore* v. *Mitchell*, 30 F.2d 600, 603-604 (2d Cir. 1929); *British Columbia* v. *Gilbertson*, 597 F.2d 1161, 1165 (9th Cir. 1979).

19 Regulation (EC) 593/2008 of 17 June 2008 on the law applicable to contractual obligations [2008] *OJ* L 177/6 (Rome I).

20 Regulation (EC) No. 864/2007 of the European Parliament and of the Council of 11 July 2007 on the law applicable to non-contractual obligations [2007] OJ L 199/40 (Rome II).

under bills of exchange, cheques and promissory notes and *other negotiable instruments*' from the Rome Regulations' scope. The latter term includes, *inter alia*, financial instruments such as shares or bonds. Yet this exclusion applies only 'to the extent that the obligations under such other negotiable instruments arise out of their negotiable character'. This proviso covers the liability of the underwriter or third parties that have signed the instrument in relation to the instrument's holder.[21] The law which is applicable to these issues is determined by internationally harmonized conflicts rules that the EU legislator wanted to preserve.[22] But the typical financial dispute has no connection with the negotiable character of the financial instruments at hand. It arises out of special statutory rules that create contractual or non-contractual obligations, for instance the rules on the marketing and distribution of financial instruments or the liability of the issuer for false or incomplete information in a prospectus. Thus it falls squarely within the scope of the Rome Regulations.

3.2 Special conflicts rules outside of Rome I and II

Despite the general primacy of EU PIL over regulation, the legislator has autonomy to depart from the general rules. Article 23 Rome I and Article 27 Rome II expressly authorize the application of special provisions in other parts of EU law that impose conflict-of-laws rules for particular matters. Yet the EU legislator generally shuns the enactment of new conflicts rules for (contractual and non-contractual) obligations outside of Rome I and II, perhaps out of a fear of destroying the uniform PIL edifice.[23] Therefore, in regulating financial law, the EU does not attempt to escape from the rules of PIL, but instead submits to them. There is no special conflicts law or similar rule like in the US that falls outside the general conflicts paradigm.

4. The law applicable to financial contracts

4.1 The general rules

From the outset, it is necessary to clarify the ambiguity of the expression 'the law applicable to financial contracts'. Most financial contracts have a double nature: since they are concluded by an agreement between the parties, they are a *negotium*, but when they are traded, i.e. transferred to other parties, they become also an *instrumentum*, i.e. a financial instrument, which is the subject of proprietary rights.[24] This double nature leads to a dichotomy on the conflicts level.

21 For a concise overview of the obligations under negotiable instruments, see M. Lehmann, 'Bill of Exchange', 'Cheques' and 'Financial Instruments', in: J. Basedow, G. Rühl, F. Ferrari and P.A. Miguel Asensio (eds.), *Encyclopedia of Private international Law*, Chelthenham: Edward Elgar Publishing 2017.

22 See Report on the Convention on the Law Applicable to Contractual Obligations by Mario Giuliano and Paul Lagarde [1980] *OJ* C 282/1, p. 11, see also M. Lehmann, 'Cheques', in Basedow et al. 2017 (*supra* n. 21).

23 Some special acts have been adopted in the area of settlement finality and financial collateral, but they are mainly concerned with *proprietary* questions and do not interfere with the general rules on *obligations* in the Rome I and II Regulation, see below n. 27. See also Recital 31 Rome I Regulation.

24 For the distinction between *negotium* and *instrumentum*, see H. Causse, *Les titres négociables*, Paris: Litec 1993, p. 5; M. Lehmann, *Finanzinstrumente*, Tübingen: Mohr Siebeck 2010, p. 290.

One must distinguish between (1) the law applicable to the *content* of the instrument, i.e. the rights and obligations arising under it and (2) the law applicable to *proprietary* issues, e.g. the question of who is the owner of the instrument.[25] The Rome I Regulation addresses only the first but not the second issue. The latter is covered by texts such as the Hague Convention on Intermediated Securities,[26] by the Finality and Financial Collateral Directive[27] and by national law.[28] The following only concerns questions relating to the *negotium*, i.e. the content of the instrument, given that only it can create contractual obligations.

The contracting parties, in accordance with Article 3 Rome I Regulation, can freely select the law which is applicable to the content of the financial contract. For many cross-border financial contracts such as loans and derivatives, English and New York law are the most frequent choices.[29] In retail relationships, the special rules for consumer protection (Article 6 Rome I Regulation) must be observed. Overriding mandatory rules (Article 9 Rome I Regulation) are of special importance to financial law.

The double nature of financial instruments as contracts and objects of trade requires that they be *fungible*, meaning that they are interchangeable. In a large and anonymous marketplace, trading would cease and transaction costs would spike if the basic characteristics such as maturity, currency or the governing law of the products traded under the same name were not identical. Fungibility therefore requires that the law which is applicable to the content of the instruments of one issue is the same. To secure fungibility, the issuer will insert an identical choice-of-law clause into all instruments of the same issue. For bonds, the law chosen is often that of the place where they are first admitted to trading. However, this custom is not a binding principle; one can also imagine a bond governed by another law than that of the exchange, e.g. a sovereign bond that is governed by the law of the issuing country.

The law that is applicable to the rights and obligations arising from shares is not determined by the Rome I Regulation since it is part of the internal organization of the company, see Article 1(2)(f) Rome I. Under national conflicts principles, the law of the issuing company (*lex societatis*) applies.[30] This law is determined differently in the EU, with most Member States choosing

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25 The difference between these two laws is nicely encapsulated by the German dichotomy '*Wertpapierrechtsstatut*' and '*Wertpapiersachstatut*', see e.g. C. Wendehorst, in: *Münchener Kommentar zum BGB*, 7th edn., Munich: CH Beck 2018, Art. 43 EGBGB, margin no. 194. While the first designates the law applicable to the rights flowing *from* the instrument ('*Recht aus dem Papier*'), the latter concerns the right *to* the instrument ('*Recht am Papier*').

26 Hague Convention of 5 July 2006 on the law applicable to certain rights in respect of securities held with an intermediary, 46 *ILM* 649.

27 Art. 9(2) Settlement Finality Directive (Directive 1998/26/EC of 19 May 1998 on settlement finality in payment and securities settlement systems [1998] *OJ* L 166/45); Art. 9 Financial Collateral Directive (Directive 2002/47/EC of 6 June 2002 on financial collateral arrangements [2002] *OJ* L 168/43).

28 See for instance in Germany Art. 43 of the Introductory Law to the Civil Code (EGBGB) as well as Sect. 17a of the Act on intermediated securities (*Depotgesetz*).

29 See e.g. the two dominant models for cross-border financial contracts, the ISDA Master Agreement, Sect. 13a; and the Loan Markets Association Agreement, Sect. 33.1, which limit the choice to English and New York law.

30 See C. Gerner-Beuerle, F. Mucciarelli, E. Schuster and M. Siems, *Study on the Law Applicable to Companies*, Luxembourg: Publications Office of the European Union 2016, p. 143 (stating that it can be expected that

either the real seat or the place of incorporation as the connecting factor.[31] A European conflicts rule to determine this law is lacking, but the law of incorporation is clearly advantageous in terms of corporate mobility.[32]

4.2 Particularities resulting from the need for uniformity

4.2.1 A single law governing contracts entered into on trading venues

Many financial instruments are traded on stock exchanges or electronic trading platforms (such as multi-lateral trading facilities (MTF)). The contracts concluded on these venues have to be distinguished from their object – the financial instrument that is traded. They are intended for the purchase and sale of such instruments. Efficient trading requires that all of these contracts entered into on the same exchange or platform are governed by a single law. Most trading venues secure this uniformity by prescribing in their rules that one law applies to all contracts being entered into on the exchange or platform.[33] For the rare cases in which such a clause has not been inserted, the Rome I Regulation provides a fall-back rule in Article 4(1)(h) Rome I. The provision imposes a single law for all contracts entered into on an exchange. In order to define the term 'multilateral system', it refers to the Markets in Financial Instruments Directive (MiFID I).[34] A 'multilateral system' is meant to encompass all exchanges and electronic trading venues.[35] It does not matter whether the trading occurs within or outside the EU.[36] Thus the

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the *lex societatis* comprises 'at least […] internal management matters, especially the relationship between the shareholders, management, and the company').

31 Gerner-Beuerle et al. 2016, pp. 134-138 (*supra* n. 30) (highlighting also some exceptions).

32 Gerner-Beuerle et al. 2016, pp. 294-295 (*supra* n. 30) (recommending the application of the *lex incorporationis*). See also the proposal for codification by the Groupe européen de droit international privé (GEDIP), 'Regulation x on the Law Applicable to Companies and Other Bodies', 3rd draft 2015, available at www.gedip-egpil.eu/reunionstravail/gedip-reunions-25.htm#1, as well as the proposal by the German Council for Private International Law, published in H.-J. Sonnenberger, *Vorschläge und Berichte zur Reform des europäischen und deutschen internationalen Gesellschaftsrechts*, Tübingen: Mohr Siebeck 2007.

33 See e.g. no. 1.7, rule 1701 of the Euronext Rule Book I, available at www.euronext.com (last accessed 31 October 2017); § 33(1) of the General Terms and Conditions for the Regulated Market of the Frankfurt Stock Exchange (*Allgemeine Geschäftsbedingungen der Deutsche Börse AG für den Freiverkehr*), 1 March 2017, available at www.xetra.com (last accessed 28 October 2017).

34 Directive 2004/39/EC [2004] *OJ* L 145/1. This directive has been replaced by MiFID II (Directive 2014/65/EU [2014] *OJ* L 173/349).

35 The latest regulatory developments have already overtaken Art. 4(1)(h) Rome I: MiFID I has been replaced by MiFID II. This new version not only covers classic exchanges and MTFs, but also OTFs (organised trading facilities). For an extension of Art. 4(1)(h) Rome I to OTFs C. Kumpan, 'Börsen und außerbörsliche Handelssysteme – Die kollisionsrechtliche Behandlung von grenzüberschreitenden Wertpapierdienstleistungen', in: A. Zetzsche and M. Lehmann, *Grenzüberschreitende Finanzdienstleistungen*, Tübingen: Mohr Siebeck 2018, p. 281 at pp. 298-299, margin no. 39.

36 F. Garcimartín Alférez, 'The Rome I Regulation: Exceptions to the Rule on Consumer Contracts and Financial Instruments', *Journal of Private International Law* (5) 2009, p. 85 at p. 155; F. Garcimartín Alférez, 'New Issues in the Rome I Regulation: The Special Provisions on Financial Market Contracts', *Yearbook of Private International Law* (10) 2008, p. 244 at p. 249.

term is meant here in a general and not in a EU-specific manner, in line with the principle of universality under Article 2 Rome I.

The law that Article 4(1)(h) Rome I refers to as uniformly applying to all contracts entered into on the exchange is the law that governs the exchange. This must be understood as a reference to the law that governs the supervision and regulation of the exchange.[37] Article 4(1)(h) Rome I synchronizes public law and private law, and in this way may be superficially compared to the *Morrison* rule. Yet it must be remembered that the provision is merely a default rule. Given that most exchanges prescribe the choice of the same law in their contract models, the default rule has little practical application.[38]

Most contracts entered into on exchanges today are not concluded directly between exchange participants, but rather with a central counterparty (CCP) that acts as a co-contractor to every purchase and sale on the exchange. In order to ensure that its obligations under these transactions are uniform, the CCP inserts an identical choice-of-law clause in all of its contracts. What if such a clause has been forgotten? It appears that Article 4(1)(h) Rome I does not directly cover this situation, but the contract certainly presents the most significant relation to the law governing the CCP in the sense of Article 4(3) and (4) Rome I.

Guaranteeing the uniform application of the law of the trading venue is also the goal of Article 6(4)(e) Rome I. The provision contains a carve out from the mandatory application of the consumer rules.[39] This was necessary because the preference for the consumer's domicile in Article 6(1) and (2) Rome I would have led to a fragmentation of the law governing contracts entered into on exchanges and other trading venues. Buyers or sellers of securities would first have to determine where their counterparty is domiciled, which would have been nearly impossible given the anonymous conditions of trading on the exchange. Instead, Article 6(4)(e) Rome I allows the general rules to determine the law that is generally applicable to the instrument.

Although Article 6(4)(e) Rome I has a more important function than the mere default rule of Article 4(1)(h) Rome I in that it allows for a deviation from the otherwise mandatory consumer conflicts rules, it has limited practical value.[40] Currently, most consumers do not buy financial instruments directly on a stock exchange or dark pool, but instead through an intermediary, such as an investment firm, which will execute the transaction itself or through a contracted partner for the account of the consumer. Financial stability could also be negatively affected if swathes of retail customers were trading directly on exchanges. Article 6(4)(e) Rome I will become useful only if and when this situation changes.

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37 Cf. Garcimartín Alférez 2009, p. 156 (*supra* n. 36) (referring to Art. 36(1) MiFID I).

38 M. Lehmann, 'Financial Instruments', in: F. Ferrari and S. Leible, *The Law Applicable to Contractual Obligations in Europe*, Munich: Sellier 2009, pp. 89-90.

39 Garcimartín Alférez 2009, p. 142 (*supra* n. 36); Garcimartín Alférez 2008, p. 250 (*supra* n. 36).

40 Garcimartín Alférez 2009, p. 157 (*supra* n. 36) ('In most jurisdictions, the safeguard foreseen in Article 6[4][e] is superfluous'); Lehmann 2009, pp. 97-98 (*supra* n. 38); G.P. Callies, in: G.P. Callies (ed.), *Rome Regulations*, 2nd edn., Alpen aan den Rijn: Wolters Kluwer 2015, Art. 6, margin no. 66 ('the necessity and practical relevance of the norm seem to be questionable […]').

4.2.2 A single law governing the content and offering of financial contracts and products

Another carve out from the consumer protection rules is provided by Article 6(4)(d) Rome I. Although it bears some resemblance to Article 6(4)(e) Rome I, its scope and goal are different. The first part of the the provision ('rights and obligations which constitute a financial instrument and rights') concerns the content of financial instruments themselves. It secures their *fungibility* by discarding the consumer conflicts rules which would have led to different governing laws depending on the habitual residence of the investor.[41] The second part of the provision ('obligations constituting the terms and conditions governing the issuance or offer to the public and public take-over bids of transferable securities') applies to transactions that are not financial instruments at all, in particular public offerings and bids for securities. Here the provision aims more generally at securing *uniformity* in the terms and conditions of an issuance or offer of financial contracts and instruments because they cannot differ depending on the habitual residence of the offeree.[42] The goal therefore is to ensure that a single law applies to all relevant contractual aspects that bind the issuer or an offeror.[43] A similar goal also underpins the third part ('subscription and redemption of units in collective investment undertakings'), which concerns the acquisition and divestment of shares in investment funds. Uniformity corresponds to the collective nature of this form of investment, and it is achieved by excluding the application of the consumer conflicts provisions. The governing law is instead determined in accordance with Articles 3 and 4 Rome I, thus securing the parties' ability to choose the applicable law. Issuers and offerors will normally include a choice-of-law clause in their instrument or offering, thus making use of Article 3 Rome I. Where they fail to do so, the law of the place of their central administration or that of the transacting branch will apply in accordance with Article 4 Rome I.[44]

The end of Article 6(4)(d) Rome I contains an important exception for activities that 'constitute provision of a financial service'.[45] The caveat preserves the application of mandatory consumer law to the individual relationship between the investor and the distributor selling the instrument, which must be distinguished from the collective relationship between the investor and the issuer.[46] The exception mainly covers the relation between the investor and his intermediary, such as an investment firm (i.e. a bank or a broker).[47] It also applies if the issuer distributes its products itself.[48] The provision's operation can be illustrated by the following practical example: Intermediary B sells units of investment fund A to customer C. The law of the habitual residence of C will have no bearing on the organisation or structure of A, which is

41 See Recital 28 phrase 1 Rome I.

42 See Recital 28 phrase 2 Rome I.

43 See Recital 29 Rome I at the end.

44 Art. 4(1)(a), (b) in conjunction with Art. 19(1) subpara. 2, (2) Rome I.

45 The notion 'financial services' is further elaborated in Recital 26 of the Rome I Regulation in conjunction with Annex I Section A and B MiFID I.

46 See A. Zetzsche, 'Das grenzüberschreitende Investmentdreieck – das IPR und IZPR der Investmentfonds', in: A. Zetzsche and M. Lehmann, *Grenzüberschreitende Finanzdienstleistungen*, Tübingen: Mohr Siebeck 2018, p. 199 at pp. 218, margin no. 47.

47 Garcimartín Alférez 2009, p. 152 (*supra* n. 36); Lehmann 2009, p. 97 (*supra* n. 38).

48 See Zetzsche 2018, pp. 218-219, margin nos. 47-48 (*supra* n. 46).

exempted from the mandatory consumer conflicts rules by the first part of Article 6(4)(e) Rome I. The law of C's habitual residence will however set a mandatory minimum standard for the contract between B and C, which is merely a bilateral service relationship, such as a commission or brokerage contract.[49]

4.3 Particularities resulting from the different boundaries of consumer and investor protection

While financial services contracts are not excluded from the scope of Article 6 Rome I, its application requires that the investor qualifies as a consumer. In conformity with the functional definition of a 'consumer' in Article 6(1) Rome I, an investor is a consumer if he acts outside his trade or profession. The consumer conflicts rule thus covers any investment for private purposes. The sum at stake is irrelevant: A German court has ruled that even an investment of EUR 50 mio. can qualify as a consumer transaction.[50] It has also been held that Article 6 Rome I applies where an entrepreneur illegally entrusts proceeds of his company in his own name and for his own individual benefit to a foreign wealth manager.[51]

There is, however, a crucial disconnection between the definition of the consumer in PIL and in financial regulation. MiFID II, the current version of the Markets in Financial Instruments Directive, does not treat all those who act outside their trade or profession indistinctively, but draws different and somewhat finer categories than Rome I.[52] In particular, MiFID II allows natural persons acting for their private benefit to waive the protections afforded to them and become a 'professional investor' based on their past experience in financial matters, their occupation and the size of their investment portfolio (so-called 'opt-up').[53] At the same time, they remain consumers for the purposes of Article 6 Rome I. Investor protection and consumer protection are therefore different in scope.[54] Technically, this poses no difficulties, as the functions of PIL and financial regulation vary. It is nevertheless a remarkable divergence between the two fields that a private investor can waive protections under regulatory law by becoming a professional investor, but not waive the mandatory rules of his domicile through a choice of law.

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49 Cf. Lehmann 2009, p. 97 (*supra* n. 38).

50 Higher Regional Court (*Oberlandesgericht*) Stuttgart, judgment of 24 April 2015, 5 U 120/14, ECLI:DE:OLGSTUT:2015:0427.5U120.14.0A.

51 German Federal Court (*Bundesgerichtshof*), judgment of 9 February 2017, IX ZR 67/17, ECLI:DE:BGH:2017:090217UIXZR67.16.0, para. 17.

52 See Recital 86 MiFID II (Directive 2014/65/EU): 'One of the objectives of this Directive is to protect investors. Measures to protect investors should be adapted to the particularities of each category of investors (retail, professional and counterparties).'

53 See MiFID II, Annex II, sub II 1.

54 This does not exclude that the two interact. For instance, Dutch courts increasingly use the classifications of investors under the regulatory rules of the MiFID to define the scope of the duty of care that investment firms must honour *vis-à-vis* their clients. See, e.g., Hof Den Haag, 14 February 2017, ECLI:NL:GHDHA:2017:255.

4.4 Particularities resulting from the influence of regulation

4.4.1 Regulation as public policy rules

Financial markets today are subject to a plethora of regulatory rules that serve important public interests, such as preventing risks for the stability of the financial system. Insofar as these rules directly impact contractual relationships, they may qualify as public policy rules or 'overriding mandatory provisions' in the sense of Article 9 Rome I Regulation and supersede the law which otherwise governs the contract.

Usually, the characterization of a legal rule as an 'overriding mandatory provision' is done by the judiciary.[55] A more recent phenomenon is that the legislator constructs this qualification itself. A salient example can be found in Article 68(6) of the Bank Recovery and Restructuring Directive (BRRD):

> 'The provisions contained in this Article shall be considered to be overriding mandatory provisions within the meaning of Article 9 of Regulation (EC) No 593/2008 of the European Parliament and of the Council […]'.[56]

The Article containing the provision, Article 68 BRRD, suspends contractual arrangements like netting clauses in the event of a bank recovery and resolution measure ordered by a public authority, such as a bail-in of bank creditors or the transfer of bank assets to a bridge institution. These measures are likely to conflict with the law applicable to contractual claims and obligations under general private international law.[57] Article 68(6) BRRD seeks to ensure that the regulatory rules will prevail. Its formulation is only partially correct since the overriding mandatory provisions are not those of the Directive, but those of the transposing Member State law. Also, Article 9 Rome I secures the effectiveness of overriding mandatory 'provisions' but not that of administrative orders such as those adopted by resolution authorities. At any rate, the automatic overriding effect of Article 68(6) BRRD is only secured if the case ends up before a Member State court, while outside the Union it depends on the willingness of third States' tribunals to recognize the EU measure.[58]

Article 68(6) BRRD is a rare case in which the legislator expressly characterizes a rule as falling under Article 9 Rome I. Other rules without such an explicit characterization may also have an overriding mandatory nature. The relevant identification criteria are laid out in Article

55 See e.g. ECJ, Case C-184/12, *Unamar* v. *NMB*, ECLI:EU:C:2013:663, *NIPR* 2013, No. 349, para. 50 (holding that it is for the national court to assess whether a rule of law is mandatory in nature and whether the legislature adopted it in order to protect an interest judged to be essential by the Member State concerned).

56 Art. 68(6) BRRD (Directive 2014/59/EU of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms [2014] *OJ* L 173/190).

57 On this conflict, see M. Lehmann, 'Bail-in and Private International Law: How to Make Bank Resolution Measures Effective Across Borders', *International & Comparative Law Quarterly* (66) 2017, p. 107 at pp. 110 et seq.

58 Ibid., pp. 135 et seq.

9(1) Rome I. Examples of overriding mandatory provisions in the area of finance are rules prohibiting money laundering, terrorism financing or tax evasion.

4.4.2 Regulation as consumer protection

Not all regulatory rules fall within the category of overriding mandatory rules. For instance, one may doubt this nature for the information and exploration duties in relation to investment services under MiFID II.[59] They aim to protect the investor and cannot be deviated from by an agreement, but to say that they are 'regarded as crucial by a country for safeguarding its public interests, such as its political, social or economic organisation' in the sense of Article 9(1) Rome I could be considered an overstatement. If they are characterized as purely domestic mandatory norms, they would be subject to the normal choice-of-law process in a cross-border context. Nevertheless, they can become mandatorily applicable through Article 6(1) and (2) Rome I for contracts concluded with consumers.

Some Member States, however, see the last point differently. German courts, for instance, draw a sharp distinction between private law and public law. They think that the distribution rules of MiFID I constitute purely public law and therefore cannot influence contractual relationships.[60] This view will be hard to maintain after MiFID II, however, which expressly requires that Member States adopt mechanisms to ensure that compensation is paid and other remedial actions are taken for any violation of the Directive and its sister text, the MiFIR.[61] The new rule makes clear that the violation of the regulatory rules has to have at least some effect on the level of private law.

One may still entertain doubts as to whether private causes of action created by the transposition of MiFID II fall within the purview of Rome I. In this respect, it might be argued that because the remedies are statutory in nature and independent of the agreement between the parties, they would have to be characterized as non-contractual obligations covered by Rome II. However, the remedies under national legislation implementing MiFID II exist but for the contract between the investor and the intermediary. Moreover, these remedies sanction the violation of information duties and thereby determine the way in which the contract is to be performed. Therefore, they are so closely connected to a voluntary obligation by the intermediary that considering them to be part of the law of the contract is justified. Arguably, it is also possible to characterize these duties as pre-contractual. If violated, any subsequent liability would then be determined in accordance with Article 12(1) Rome II. This provision however refers back to the rules of the Rome I Regulation so that the result is the same.

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59 See Arts. 24 et seq. MiFID II.

60 See the German Federal Court (*Bundesgerichtshof*), judgment of 27 September 2011, XI ZR 182/10, BGHZ (official collection of the decisions of the German Federal Court) 191, 119, para. 47 (arguing that a violation of the German rules transposing Art. 19 MiFID I (=predecessor of Art. 24 MiFID II) could be sanctioned only by the supervisor and would not have any effect on the relation between private parties).

61 See Art. 69(2) subpara. 3 MiFID II 'Member States shall ensure that mechanisms are in place to ensure that compensation may be paid or other remedial action be taken in accordance with national law for any financial loss or damage suffered as a result of an infringement of this Directive or of Regulation (EU) No. 600/2014 [=MiFIR]'.

In sum, the national provisions sanctioning a violation of the duties in Articles 24 et seq. MiFID II fall under Article 6 Rome I. The scope of this conflicts rule extends beyond pure 'consumer' legislation and covers any mandatory rule that protects the non-professional counterparty.[62] As a result, a mere choice of a law cannot deprive the investor of the protections afforded by the mandatory provisions of the state of her habitual residence.

Still, the situational conditions of Article 6(1)(a) and (b) Rome I must be fulfilled for the provision to apply, i.e. the business must either pursue a professional or commercial activity in the state of the consumer's habitual residence, or it must direct its activities to this state. The latter will be the case where an investment firm targets the customer's market, for instance by advertisements on the internet, irrespective of how the contract is concluded.[63] The consumer's law will however not apply where she takes the initiative to contact the foreign firm herself without the latter deploying any business activity in or targeting activity towards the investor's home state.

5. The law applicable to financial torts

5.1 The general rules

The Rome II Regulation contains specific rules for economic torts in a number of areas – *inter alia* product liability, competition law, intellectual property law – but no such rules for financial law. During the Regulation's drafting, it was debated whether to introduce a special rule for financial torts or to exclude them from the Regulation's scope altogether.[64] Both proposals were rejected, and as a result, the general rules of the Regulation apply to financial torts. Therefore, the *lex lata* in the EU clearly differs from that in the US, where redress for securities fraud and similar claims is governed by a specific market-oriented rule.[65]

5.1.1 Loss localization under Article 4(1) Rome II

The application of Article 4 Rome II to financial torts raises challenging questions. Finding the country 'in which the damage occurs' in the sense of Article 4(1) Rome II proves to be an arduous task where economic – i.e. incorporeal – loss is involved.[66] The ECJ held in *Kolassa* that the damage occurs at the investor's domicile provided that she has suffered a loss in a

62 G.P. Callies, in: Callies 2015, Art. 6, margin no. 75 (*supra* n. 40) ('Protection is afforded to a consumer by any mandatory norm of the law of the consumer-country which is applicable in the individual case, irrespective of the question if such norm is limited in scope to consumers or if it would apply as well in a general context').

63 See ECJ, Case C-190/11, *Mühlleitner*, ECLI:EU:C:2012:542, *NIPR* 2012, No. 467; Case C-218/12, *Emrek*, ECLI:EU:C:2013:666, *NIPR* 2013, No. 367.

64 See A. Dickinson, *The Rome II Regulation: The Law Applicable to Non-Contractual Obligations*, Oxford: Oxford University Press 2008, p. 211, margin no. 3.171 and 3.172.

65 See above section 2.

66 See generally L. van Bochove, 'Purely economic loss in conflict of laws: the case of tortious interference with contract', *NIPR* 2016, p. 456; Dickinson 2008, pp. 313-314, margin nos. 4.36-4.37 (*supra* n. 64); M. Lehmann, 'Where Does Economic Loss Occur?', *Journal of Private International Law* (7) 2011, p. 527.

bank account located there.[67] The judgment concerned the determination of the competent court under the Brussels I Regulation,[68] but must be applied, *mutatis mutandis*, to the Rome II Regulation under the synergy paradigm.[69] Unfortunately, the ECJ ruling leaves many questions unanswered. To start with, it does not determine where the damage occurs if the investor's bank account is not located at the place of domicile. There is also disagreement about the meaning of 'bank account': While some authors have interpreted this to designate the securities account,[70] others read it as a reference to the cash account from which the securities have been paid.[71] Finally, the significance of *Kolassa* has been limited by the subsequent decision in *Universal Music*, which included the following passage:

> 'However, as the Advocate General stated in essence in points 44 and 45 of his Opinion in the present case, that finding [of the Kolassa judgment] is made within the specific context of the case which gave rise to that judgment.'[72]

In point 45 of his opinion, the Advocate General highlights as circumstances specific to *Kolassa* that the prospectus concerning the financial instruments in question was distributed in the investor's state, where the instruments were also sold.[73] The ECJ's reference to this part of the Advocate General's opinion in *Universal Music* indicates that the location of the investor's bank account alone shall not be dispositive and that one should also take into account the location where instruments are offered and where prospectuses are distributed.[74] Whatever one may think about the methodology of reinterpreting a past decision in a subsequent case, it is clear that the ECJ considers *Kolassa* to be an outlier. As indicated in *Universal Music*, the fact that purely financial loss occurs in the victim's bank account does not in and of itself justify the conclusion that the damage occurred there; only if this place is supplemented by *other*

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67 ECJ, Case C-375/13, *Kolassa*, ECLI:EU:C:2015:37, *NIPR* 2015, No. 50, para. 55.

68 Council Regulation (EC) No. 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters [2001] OJ L 12/1 (Brussels I).

69 See Recital 7 Rome II and E. Lein, 'The New Rome I/Rome II/Brussels I Synergy', *Yearbook of Private International Law* (10) 2008, p. 177.

70 T. Arons, 'On Financial Losses, Prospectuses, Liability, Jurisdiction (Clauses) and Applicable Law', *NIPR* 2015, p. 377 at p. 379; M. Haentjens and D.J. Verheij, 'Finding Nemo: Locating Financial Losses after Kolassa/Barclays Bank and Profit', *Journal of International Banking Law and Regulation* (*JIBLR*) 2016, p. 346 at p. 352.

71 L. d'Avout, 'Commercialisation de Titres Financiers et Compétence Internationale de Proximité', *Recueil Dalloz* 2015, p. 770; R. Freitag, 'Internationale Prospekthaftung Revisited – Zur Auslegung des europäischen Kollisionsrechts vor dem Hintergrund der "Kolassa"-Entscheidung des EuGH', *Wertpapier-Mitteilungen* (*WM*) (69) 2015, p. 1165 at p. 1168; J. von Hein, 'Anmerkung zu EuGH, Kolassa', *JuristenZeitung* 2015, p. 946 at pp. 948-949; M. Lehmann, 'Prospectus Liability and Private International Law – Assessing the Landscape after the CJEU's Kolassa Ruling (Case C-375/13)', *Journal of Private International Law* (12) 2016, p. 318 at p. 330.

72 ECJ, Case C-12/2015, *Universal Music*, ECLI:EU:C:2016:449, *NIPR* 2016, No. 298, para. 37.

73 Advocate General Szpunar, opinion in Case C-12/2015, *Universal Music*, para. 45.

74 This would also explain a mysterious reference to the distribution of the prospectus in the *Kolassa* judgment that otherwise could not be accounted for, see ECJ, *Kolassa* (*supra* n. 67); on the confusion created by this reference, see Lehmann 2016, p. 334 (*supra* n. 71).

circumstances specific to the case can the place of the bank account be considered as the place of damage.[75] The ECJ seems to favour the localization of loss by a combined multi-factor test with variable criteria. While this approach allows for flexibility, it does not yield any legal certainty.

Even more worrying are the consequences of fragmenting the applicable law by Article 4(1) Rome II. The ECJ determines the location of the loss suffered by each investor individually.[76] Consequently, the same tort, such as market manipulation or the failure to disclose inside information, may be governed by a number of different laws. Given that investors may be based around the world, any national law could apply. This diversity makes potential liability completely unforeseeable – and therefore also uninsurable – from the tortfeasor's perspective. The judicial enforcement of such claims becomes fraught with difficulties and attempts at collective action are rendered almost hopeless.[77] The last point is especially unsettling given that class actions are often the only effective remedy to discipline powerful issuers and financial intermediaries.

5.1.2 Investor equality and Article 4(2) Rome II

Article 4(2) Rome II causes another issue. Serious distortions are created when the common domicile rule is applied to financial claims. Take, for instance, an investor residing in state X who has bought stock of a company that is headquartered also in X, but listed on an exchange in state Y. If a prospectus liability claim arises, this investor will be allowed to sue the company under the law of the country of the issuer's central administration on the basis of Articles 4(2), 23(1)(1) Rome II, whereas the claims of all other investors are subject to a different law identified under Article 4(1) Rome II. Assuming the law of X provides a particularly stringent type of prospectus liability, the investor would benefit merely because he happens to be domiciled in the same country as the issuer. This seems like a windfall profit and discrimination against other purchasers of the same securities who receive less of the company's wealth solely because they reside in a different state.[78]

More generally, the principle of equal investor treatment, which is of paramount importance, is difficult to reconcile with the common domicile exception provided for in Article 4(2) Rome II.[79] Remarkably, the US Supreme Court in *Morrison* made no mention of the common domicile exception, despite its long-standing history in US conflicts law.[80] The US approach avoids giving domestic investors an unjust privilege when they choose to transact in a foreign market.

75 *Universal Music*, paras. 38-39 (*supra* n. 72).

76 See *Kolassa*, para. 54 (*supra* n. 67).

77 Cf. S. Corneloup, 'Roma II y el derecho de los mercados financieros: el ejemplo de los daños causados por la violación de las obligaciones de información', *Anuario español de derecho internacional privado* 2011, p. 63 at p. 75.

78 Lehmann 2016, pp. 337-338 (*supra* n. 71).

79 Corneloup 2011, p. 76 (*supra* n. 77).

80 See *Babcock* v. *Jackson*, 12 N.Y.2d 473, 483 (1963).

5.2 *Escape devices*

5.2.1 Public policy rules under Article 16 Rome II

An instinctive reaction to bypass the Article 4 conundrum could be to qualify all legislative rules concerning financial torts as 'overriding mandatory provisions' in the sense of Article 16 Rome II. It could be argued that provisions such as those regarding liability for insider trading or for market manipulation and even prospectus liability are crucial for safeguarding the EU's public interest, specifically for its economic organisation.

On the other hand, the text of Article 16 Rome II only addresses the application of overriding mandatory provisions of the forum and is silent as to the application of foreign public policy rules. Whether it is permissible to follow those at all is a hotly debated issue.[81] Even if they could be applied, uncertainty would still exist as to 'when' and 'under what conditions'. As a consequence, courts might determine the applicable rules differently. Regarding the law of the forum, courts are even required to reach different results if one understands Article 16 Rome II as an admonishment to actively discriminate between their own rules and foreign rules.

In sum, qualifying financial torts as public policy provisions does not guarantee more certainty or uniformity than following the general rules under Article 4 Rome II. On the contrary, it would even increase the cacophony of possibly applicable national laws. The same is true if one follows the local data theory and treats foreign mandatory rules as a matter of fact.[82] This was recently ruled by the ECJ as being compatible with Article 9 Rome I.[83] As a result, courts in the Member States can take foreign public policy rules into account if this possibility is offered by the governing national substantive law, for instance by a provision that outlaws contracts that are 'illegal' or 'contrary to good morals'. However, given that substantive laws offer very different conditions for considering foreign law, this theory would hardly result in a more uniform application of foreign financial law. Moreover, it seems to be incompatible with Article 17 Rome II, which limits the taking into account to the law in force at a certain place.

5.2.2 The conduct and safety rules and Article 17 Rome II

Many concerns over the Rome II Regulation's application to financial disputes are assuaged by Article 17. The provision requires the court to take into account 'as a matter of fact and in so

81 Pro application: J. von Hein, in: Callies 2015, Art. 16, margin no. 20 (*supra* n. 40); contra: Dickinson 2008, pp. 637-638, margin nos. 15.24-15.25 (*supra* n. 64); A. Fuchs, in P. Huber (ed.), *Rome II Regulation*, Munich: Sellier 2011, Art. 16, margin nos. 29-30; for a detailed analysis see L. Günther, *Die Anwendbarkeit ausländischer Eingriffsnormen im Lichte der Rom I- und Rom II-Verordnungen*, Saarbrücken: Alma Mater 2011, pp. 192-208.

82 See A. Ehrenzweig, 'Local and Moral Data in the Conflict of Laws: Terra Incognita', *Buff. Law Review* (16) 1966, p. 55. On the influence of this theory in Europe, see T. Pfeiffer, 'Datumtheorie und "local data" in der Rom II-VO – am Beispiel von Straßenverkehrsunfällen', in: *Liber Amicorum Schurig*, Munich: Sellier 2012, p. 229; T.W. Dornis, 'Die Theorie der local data: dogmatische Bruchstelle im klassischen IPR', *SZIER/RSDIE* (25) 2015, p. 183.

83 ECJ, Case C-135/15, *Republik Griechenland v Grigorios Nikiforidis*, ECLI:EU:C:2016:774, *NIPR* 2016, No. 405, paras. 51-53.

far as is appropriate' the rules of safety and conduct in force at the time and place of the event giving rise to liability. Recital 34 explains that this formulation refers to the country in which the harmful act was committed. The Rome II Regulation thereby introduces the distinction between 'conduct regulating' and 'loss allocating' rules that is known from US law.[84] While conduct is regulated by the law of the country of tortious action under Article 17 Rome II, loss allocation will be determined by the law of the place of damage in conformity with Article 4(1) Rome II.

Submitting conduct regulation to the law of the place where the conduct occurs has critical advantages. It allows the tortfeasor to discover the legal requirements he must comply with at relatively low costs. It also avoids the imposition of contradictory duties following from the applicability of different laws. By obeying the conduct rules of the place where one acts, any person can and should be able to avoid liability.

However, in the financial context, submitting conduct mechanically to the place of action has significant disadvantages. To illustrate this, imagine a corporate insider who discloses non-public information about a French company while on a business trip in Kiev. It would hardly make sense to assess the legality of his conduct under Ukrainian law. Discarding this law on the ground that it would not be 'appropriate' in the sense of Article 17 Rome II does not solve the problem of determining which law should govern his conduct instead. If it were the law designated by Article 4(1) Rome II, this would potentially lead to conflicting duties where numerous victims are affected by the tort.

In the area of closely integrated financial markets with virtual trading and incorporeal products, the location of one's action is mostly irrelevant. What matters is the market where the effect of the action occurs. While Article 17 Rome II is a useful starting point for the identification of a single law, it is inept to satisfy the specific needs of financial law.

5.3 Attempts at a special treatment for financial disputes

The shortcomings of the Rome II rules concerning financial disputes have not escaped doctrinal scrutiny. Different avenues have been developed to avoid the atomization of the applicable law and the uncertainty created by Article 4(1) as well as the inconsistencies of Article 4(2) Rome II.

5.3.1 Looking for a specific conflicts rule in financial markets regulation

One approach has been to submit financial disputes to special conflicts rules located in the regulatory rules on the basis of Article 27 Rome II.[85] Methodologically, this idea is similar to the one used by the US Supreme Court in *Morrison*. However, the problem of this approach

84 See *Babcock* v. *Jackson*, 12 N.Y.2d 473, 483 (1963); *Schultz* v. *Boy Scouts of America, Inc.*, 65 N.Y.2d 189, 201 (1985); P. Hay, P.J. Borchers and S.C. Symeonides, *Conflicts of Law*, 5th edn., St. Paul, MN: West Academic Publishing 2010, pp. 874-877; S.C. Symeonides, *Choice of Law*, New York, NY: Oxford University Press 2016, p. 249.

85 See e.g. M. Audit, 'Aspects internationaux de la responsabilité des agences de notation', *Revue critique de droit international privé* 2011, p. 581 at p. 590 (for the Rating Agency Regulation); P. Tschäpe, R. Kramer and O. Glück, 'Die ROM (sic!) II-Verordnung – Endlich ein einheitliches Kollisionsrecht für die gesetzli-

is that EU financial law mainly contains regulatory and supervisory standards. It rarely treats issues of private law, such as liability for loss, and it is even less likely to address conflicts rules for such issues. Even where special causes of action for the violation of regulatory rules exist, they do not deviate from the general rules of PIL, but rather refer to them, such as in the case of rating agency liability.[86]

The void of conflict-of-laws rules in EU financial law could perhaps be filled by using the rules on the distribution of supervisory competences in special regulations and directives and extending them to private disputes. Thus, some have suggested employing the country-of-origin principle underlying the Prospectus Directive[87] as a model for solving conflict-of-law issues regarding prospectus liability claims.[88] The advantage of this proposal is that it would synchronize the application of public and private law. However, serious differences exist between both areas that necessitate different treatment. For example, under the Prospectus Directive, the competent authority of the home Member State may transfer its authority to grant the approval of a prospectus to the competent authority of another Member State, subject to the latter's agreement.[89] This transfer is not conditioned on the transferee having a more significant connection with the case, but may be motivated by purely administrative convenience, for instance by the desire to distribute the workload between the authorities more evenly. It would be bizarre if such a transfer would have an influence on the standard of liability for mistakes or omissions in the prospectus. Furthermore, the intent of the legislator of the Prospectus Directive was not to create special conflicts rules for private law obligations, but rather to determine the competent supervisory authority. Finally, most EU regulatory provisions are focused on relations between Member States and leave cases involving third states to national law. In contrast, European PIL does not distinguish between intra- and extra-EU cases since it is applied universally.[90] The EU legislator wanted to create uniform conflicts rules that are not restricted to the EU. Establishing special intra-EU conflicts rules would thwart this goal.

Consequently, one may not escape the conundrum posed by Article 4(1) and (2) Rome I through the application of special conflicts rules under Article 27 Rome II. A European *Morrison* approach is not a promising avenue to follow.

che Prospekthaftung?', *Recht der Internationalen Wirtschaft* 2008, p. 657 at pp. 664-666 (for the Prospectus Directive).

86 See Art. 35a Regulation (EC) No. 1060/2009 on credit rating agencies [2009] *OJ* L 302/1, as amended by Regulation (EU) No. 462/2013 of the European Parliament and of the Council of 21 May 2013 [2013] *OJ* L 146/1. Para. 1 of this provision introduces a statutory liability for rating agencies in case of inaccurate ratings. The interpretation and application of key terms is subject to the applicable national law, which is expressly to be determined 'by the relevant rules of private international law'. This provision must be understood as a reference to the Rome II Regulation, which also determines the applicability of Art. 35a Regulation (EC) No. 1060/2009 itself. On this point, see M. Lehmann, 'Civil Liability of Rating Agencies: An Insipid Sprout from Brussels', *Capital Markets Law Journal* (11) 2016, p. 60 at p. 79.

87 Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC [2001] *OJ* L 345/64.

88 See Tschäpe, Kramer and Glück 2008, pp. 664-666 (*supra* n. 85).

89 Art. 13(5) Prospectus Directive.

90 See Art. 3 Rome II.

5.3.2 Identifying the place of loss with the market

Another suggested approach has been to identify the place of the damage under Article 4(1) Rome II not individually, but based on the market as a whole.[91] Proponents of this view stress that financial torts cause damage to a multitude of participants. Such damage would occur at the location of the market on which false information has been disseminated or correct information has been omitted.

The market-oriented interpretation of 'damage' has some attractiveness because it concentrates the applicable law in one place, thus ensuring that the same law applies to all investor claims. However, this approach has been clearly eschewed by the ECJ in *Kolassa*, where the court ruled in favour of an individual determination of the place of loss by saying that

> '[…] the loss occurred in the place where the investor suffered it.'[92]

This seemingly tautological statement dismisses any effort to abstract from the individual investor and look at the market that was damaged. It thereby prohibits the market localization of loss. The decision concerned jurisdiction, but it also has an indirect effect on the conflict of laws under the paradigm of parallel interpretation.[93] Although the parallel between the Rome I and the Brussels I Regulation need not be complete, it would be quite surprising should the ECJ construct the notion of 'damage', which is fundamental to private law, in a completely different way in each text.

5.3.3 Analogy to Article 6 Rome II

Other writers have proposed using the conflicts rules on competition, which provide two clear instances of market localization in Article 6(1) and (3) Rome II. It is suggested that these rules could be applied by analogy to financial disputes.[94] This theory is buttressed by a reference to Recital 21, according to which Article 6 is not an exception but rather a 'clarification' of Article 4 Rome II.

However, the fact that the EU legislator calls Article 6 Rome II a 'clarification' does not mean that courts would be allowed to clarify the law in the same way as the legislator by creating entirely new conflict-of-laws rules. It follows from the system of the Rome II Regulation that the torts or delicts not covered by a special rule have to be generally dealt with under Article 4. Applying a special conflicts rule by analogy is only allowed where the area concerned is sufficiently close or similar to the one that is regulated in the special rule. That is not the case

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91 P. Mankowski, 'Finanzmarktverträge', in: C. Reithmann and D. Martiny, *Internationales Vertragsrecht*, 7th edn., Cologne: Otto Schmidt, margin no. 2530; N. Nisi, 'La giurisdizione in materia di responsabilità delle agenzie di *rating* alla luce del regolamento Bruxelles I', *Rivista di diritto internazionale privato e processuale* 2013, p. 385 at p. 413; for the same result, but based on an individual loss localization, see S. Sánchez Fernández, *Ley aplicable a la responsabilidad derivada del folleto*, doctoral thesis Madrid 2014.

92 *Kolassa*, para. 54 (*supra* n. 67).

93 See above footnote 69.

94 D. Einsele, 'Internationales Prospekthaftungsrecht – Kollisionsrechtlicher Anlegerschutz nach der Rom II-Verordnung', *Zeitschrift für Europäisches Privatrecht* 2012, p. 23 at pp. 38-40.

for competition and financial law, which are entirely distinct. The rules of Article 6 Rome II do not fit the special context of financial law without some fundamental modifications, which is difficult to achieve in a legally certain manner through an analogy.

5.3.4 Applying the exception clause in Article 4(3) Rome II

An additional recommendation to avoid the unfortunate consequences of Article 4(1) and (2) Rome II in the financial context is to apply the 'exception clause' in Article 4(3) of the same Regulation.[95] Advocates of this approach contend that financial torts would have a manifestly closer connection to the law of the issuer's state of domicile or the state where the market on which the financial instruments in question are offered or traded than to the law identified by Article 4(1) and (2) Rome I. The law of this state would therefore govern liability for financial torts such as market manipulation or insider trading or the wrongful publication of a prospectus. This interpretation promises great benefits by applying the same law to all torts committed by the same issuer or on the same market. As it is easy to determine the place of the issuer or the place on which securities are traded or offered, this method would also save litigation costs. In case of multiple places of trading, the manifestly closer connection would be with the place where the instrument in question has been acquired.

However, doubts remain as to whether Article 4(3) Rome II is the proper device for achieving these goals. In its proposal for the Regulation, the Commission has stressed that the application of the exception clause must remain exceptional.[96] Using Article 4(3) Rome II to deviate from the otherwise applicable rules under the Regulation for an entire category of torts – financial torts – would be contrary to this intention. It would turn the clause into a device for the creation of new jurisprudential conflicts rules. This does not exclude that the ECJ will use Article 4(3) Rome II in future cases involving financial markets in order to avoid the calamitous consequences of its *Kolassa* ruling in the area of conflict of laws. Nevertheless, such an approach would create a misguided judicial precedent to employ the exception clause not as an exception, but as a general rule for the area of finance. It would also create new uncertainty, as the details of the new rule and its application to particular circumstances would have to be determined on a case-by-case basis.

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95 For prospectus liability cases: W.-G. Ringe and A. Hellgardt, 'The International Dimension of Issuer Liability – Liability and Choice of Law From a Transatlantic Perspective', *Oxford Journal of Legal Studies* (31) 2011, p. 23 at p. 32; J. von Hein, 'Die Internationale Prospekthaftung Im Lichte Der Rom II-Verordnung', in: H. Baum, A.M. Fleckner, A. Hellgardt and M. Roth (eds.), *Perspektiven des Wirtschaftsrechts*, Berlin: De Gruyter 2008, pp. 391-394; C. Weber, 'Internationale Prospekthaftung Nach Der Rom II-Verordnung', *Wertpapier-Mitteilungen* (*WM*) 2008, p. 1581 at pp. 1586-1587; for rating agency liability: U.G. Schroeter, 'Grenzüberschreitende Verhaltenspflichten und Haftung von Rating-Agenturen', in: A. Zetzsche and M. Lehmann, *Grenzüberschreitende Finanzdienstleistungen*, Tübingen: Mohr Siebeck 2018, p. 357 at pp. 387-388, margin nos. 82-84.

96 Commission, Proposal for a Regulation of the European Parliament and the Council on the law applicable to non-contractual obligations ('Rome II'), COM(2003) 427 final, p. 12.

5.4 The need for law reform

It has become clear that the Rome II Regulation in its current form is inept at providing a satisfactory solution to the determination of the applicable law in financial disputes. The clearest and most effective way to overcome this conundrum would be to introduce a new conflicts rule for financial torts.[97] Such special rules are not unusual, as evidenced by the *Morrison* judgment.

Inspiration can be taken from the laws of Switzerland and Liechtenstein, which both contain a special rule for the determination of the law governing prospectus liability claims.[98] They each give the victim a choice between the law of the issuer and the law of the market where the securities have been offered. While it is certain that the latter must have a bearing on liability, the role of the former is debatable. It has been argued that the application of the law of the issuer's state of incorporation would enable the application of a consistent and comprehensive corporate governance regime, which would in turn enhance the foreseeability of the applicable law in liability situations.[99] Yet this argument is specious given the very different purposes of corporate and securities law. Even in the US, where securities law and corporate law are closely intertwined, different connecting factors are used for both areas on the level of conflict of laws. While corporate issues are governed by the law of incorporation, the Supreme Court has opted in *Morrison* in favour of submitting securities liability to the law of the state in which a transaction is entered into or in which securities are listed. This is consistent with the general function of securities law in policing securities markets. It would seriously limit the regulatory power of the state if a law different from its own would determine the liability for wrongs committed on its financial markets. A state must guarantee the integrity of its own markets, including the offerings made by foreign issuers. Its rules should therefore apply independently of the place of the issuer's incorporation.

For these reasons, only the law of the state of the market on which securities are traded or offered should govern financial torts.[100] Using the market as the connecting factor not only would bring EU law into line with US law, it would also correspond to the essence of the approach underlying Article 6(1) and (3) Rome II. The German Council on Private International Law, a group of experts advising the German Ministry of Justice in the area of conflict of laws and jurisdictions, has formulated a proposal to introduce a new 'Article 6bis' for torts in financial matters that suggests the affected market as the connecting factor.[101] The proposal also contains

97 In this sense, see already T.M.C. Arons, '"All roads lead to Rome!": Beware of the consequences! The law applicable to prospectus liability claims under the Rome II Regulation', *NIPR* 2008, p. 481 at p. 486.

98 See Art. 156 Swiss Act on Private International Law, Art. 237d Liechtenstein Persons and Companies Act (*Liechtensteinisches Personen- und Gesellschaftsrecht*).

99 Ringe and Hellgardt 2011, p. 28 (*supra* n. 95).

100 In the same vein: Arons 2008, p. 485-486 (*supra* n. 97); Corneloup 2011, p. 79-81 (*supra* n. 77); F. Garcimartín Alférez, 'The Law Applicable to Prospectus Liability in the European Union', *Law and Financial Markets Review* (5) 2011, p. 449 at p. 455.

101 The English and a German version have been published in *IPRax* 2012, 470, a French version in *Revue critique de droit international privé* 2012, p. 679, see for comment M. Lehmann, 'Vorschlag für eine Reform der Rom II-Verordnung im Bereich der Finanzmarktdelikte', *IPRax* 2012, p. 399; M. Lehmann, 'Proposition d'une règle spéciale dans le Règlement Rome II pour les délits financiers', *Revue critique de droit international privé* 2012, p. 485.

a rule for multiple listings, an exception clause as well as a clause modelled on Article 6(3)(b) Rome II. Furthermore, an amendment of Recital 34 Rome II is proposed to allow for more flexibility with regard to the determination of the state of the relevant conduct.

The proposal results in the application of a single law to financial torts that is both foreseeable and in line with the particularities of highly regulated markets. Without these amendments, it will be practically impossible to achieve sensible results under Rome II in financial disputes. A comprehensive and certain solution is needed quickly. Therefore, the European lawmaker should not postpone reform by leaving the issue to the ECJ.

6. Summary and outlook

Finance is not unique in the sense that it would form a separate, self-standing area of private international law. Rather, financial relationships must be classified into the traditional categories of PIL, such as contractual and non-contractual obligations, before identifying the applicable law.

Yet finance is special in that it sometimes necessitates a deviation from the normal conflicts rules. This applies first to financial contracts: The trading of financial instruments requires the application of a single law to all transactions entered into on an exchange or electronic trading venue. Moreover, the fungibility of financial instruments as a necessary condition for trading and the principle of investor equality require that the same law determines the content of the financial instrument as well as the conditions of its public offering. These specificities exclude the application of the consumer protection provisions that would result in the application of different laws depending on the investor's habitual residence.

The second particularity of financial law is the paramount influence of financial regulation. The legislator often uses statutory private causes of action based on financial regulation as a means to discipline the market. This public interest is best served by tying private liability to the market affected. The current framework of the Rome II Regulation is incompatible with such a solution. It favours the application of the law of the place of the damage and of the common domicile of the tortfeasor and victim. These connecting factors are inapposite in the securities context. The Rome II Regulation should be quickly reformed so as to add a special conflicts rule for financial torts.