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WHAT'S IN YOUR PORTFOLIO?
U.S. INVESTORS ARE UNKNOWINGLY FINANCING STATE SPONSORS OF TERRORISM

Amy Deen Westbrook*

INTRODUCTION

A. The Conflict

In 2004, a television newscaster asked, "Did it ever occur to you that when President Bush [said], 'Money is the lifeblood of terrorist operations,' he [was] talking about your money—and every other American's money?" With over 78 million Americans holding an increasingly global array of securities though pension plans and mutual funds, the chances are good that you have money invested in companies that are doing business in nations that support terrorism. Further...

* Associate Professor and Co-Director, Business and Transactional Law Center, Washburn University School of Law. I would like to thank Marc Miller, Phil Halpern, and Cheryl Nichols for their encouragement and input; Brad Borden for his helpful advice; and Sheila Reynolds for the opportunity to complete the database. I am also grateful to Sarah Brancatella and Carl Petterson for their research help. Finally, I would like to thank my husband, David A. Westbrook, for his patience and insight. Any mistakes in the Article are my responsibility.


3. As one expert expresses it, "[T]he principal source of financial and economic support for Iran and certain other countries of concern are [publicly traded companies]. Most Americans hold at least some of these companies in their retirement accounts and other investment portfolios." Foreign Policy Implications of U.S. Efforts to Address the International Financial Crisis: TARP, TALF and the G-20 Plan: Hearing Before the Subcomm. on Terrorism, Nonproliferation and Trade of the H. Comm. on Foreign Affairs, 111th Cong. 55 (2009) [hereinafter Foreign Policy Hearing] (statement of Roger Robinson, Jr., President and CEO, Conflict Securities Advisory Group). The U.S. Department of State uses the following definition of terrorism: "[T]he term 'terrorism' means premeditated, politically motivated violence perpetrated against noncombatant targets by subnational groups or clandestine agents," usually intended to influence an audience. 22 U.S.C. § 2656f(d)(2) (2006).
thermore, because of the way U.S. securities regulation currently operates, you may not be able to find out if you do.

This Article explores why, in an ostensibly public securities market, investors cannot find out whether their own money goes to countries that have been designated by the U.S. Department of State as State Sponsors of Terrorism (SSTs). It also examines the way in which imposition of U.S. economic sanctions on SSTs should influence the mandatory disclosure regime for securities that are offered to the public in the United States.

This issue is timely. In the wake of the financial crisis, the United States is attempting to reform its financial regulatory system. At the same time, in the post-September 11th world, with ongoing wars in Iraq and Afghanistan, and renewed concerns about nuclear proliferation in Iran and elsewhere, the United States is reexamining the ways in which it responds to security threats. This Article will show that financial and foreign policy must be coordinated in order to create a sensible and safe regime to govern both securities and security.

The very existence of this issue may be somewhat surprising. One might assume that if the United States has designated a country as an

4. "Countries determined by the Secretary of State to have repeatedly provided support for acts of international terrorism are designated pursuant to three laws: section 6(j) of the Export Administration Act of 1979, section 40 of the Arms Export Control Act, and section 620A of the Foreign Assistance Act." U.S. Dep't of State, State Sponsors of Terrorism, http://www.state.gov/s/ct/c14151.htm (last visited Jan. 15, 2010). Such countries are then subject to restrictions on, for example, "U.S. foreign assistance including Export-Import Bank credits and guarantees (under the Foreign Assistance Act of 1961)." GARY CLYDE HUFBAUER, JEFFREY J. SCHOTT & BARBARA OEGG, POLICY BRIEF 01-11: USING SANCTIONS TO FIGHT TERRORISM (Nov. 2001), http://www.iie.com/publications/pb/pb.cfm?ResearchID=79 (last visited Feb. 10, 2010). Currently the Department of State has designated Cuba, Iran, Sudan, and Syria as state sponsors of terrorism (SSTs). See U.S. Dep't of State, State Sponsors of Terrorism, supra. North Korea was removed from the list in the fall of 2008, although it remains subject to a number of other U.S. sanctions. See Gary G. Yerkey, North Korea's Removal from Terrorism List Seen Having Only Marginal Impact on Exports, 25 Int'l Trade Rep. (BNA) 1517 (Oct. 23, 2008).

5. For example, the Troubled Asset Relief Program (TARP) and the Term Asset Backed Securities Law Facility (TALF) involved enormous outlays of tax dollars with little vetting of recipients regarding their business activities overseas. See Foreign Policy Hearing, supra note 3, at 53 (statement of Roger Robinson, Jr., President and CEO, Conflict Securities Advisory Group).

SST and has imposed sanctions, then it has isolated that country because U.S. companies may not conduct business in the embargoed nation, and U.S. investors may not invest in companies that conduct business there.

The legal situation is more complex. U.S. sanctions may not apply to non-U.S. companies that sell securities in the United States or to non-U.S. subsidiaries of U.S. companies. Although U.S. companies cannot do business in most countries subject to U.S. sanctions, if a foreign country opts not to impose sanctions, then its companies may lawfully conduct business there. This creates an opportunity for regulatory arbitrage. For example, a U.S. company may raise money in the U.S. capital markets and incorporate a subsidiary in a country that does not impose any sanctions that prohibit doing business in an SST. Or, a foreign company may do business in an SST and at the same time raise capital in the United States. As a result, the objectives of the U.S. sanctions regime—to isolate the SST—are somewhat frustrated.

The core mechanism of the federal securities laws—namely, disclosure—can be used to address this tension between national security policy and global business that is conducted in multiple jurisdictions. While the United States may not be able to prevent a foreign entity from doing business in an SST, it can require that entity to disclose such business if it seeks to raise capital in the U.S. public markets.

The general legal issue, then, is whether issuers with operations in or with SSTs must disclose those operations in the filings that they are required to make available to the U.S. investing public. Unsurprisingly, such issuers have resisted disclosing their business activities in SSTs unless the issuers are obviously required to do so because those activities are financially very significant.

As discussed in detail below, under U.S. securities laws, whether business activities must be disclosed generally depends on whether the information is "material." The materiality of information is analyzed by asking whether there is a substantial likelihood that a reasonable investor would find the information significant. This Article argues that business in or with an SST is material and must therefore be disclosed.

As an empirical matter, disclosure of operations in or with SSTs is inadequate. This Article analyzes the publicly available disclosure of over a hundred companies reported to be doing business in the three

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7. See TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438 (1976); see also infra Part III.C (analyzing materiality).
SSTs that are subject to the most comprehensive U.S. economic sanctions: Cuba, Iran, and Sudan (the "Sanctioned Countries"). Less than half of these companies make any disclosure of their activities in or with the Sanctioned Countries in the periodic reports they file with the U.S. Securities and Exchange Commission (SEC). Even in cases in which companies disclose the existence of operations in or with the Sanctioned Countries, information about the nature or extent of such business is often withheld. Moreover, investors looking for information about companies' activities in the Sanctioned Countries often cannot find that information, even if it is nominally disclosed. In short, disclosure of business in or with the Sanctioned Countries is ineffective.

The lack of disclosure and the difficulty of finding the information that is disclosed mean that U.S. investors may unwittingly be supporting activities contrary to the security policy of the United States, activities that would be illegal for a U.S. person to undertake. To the extent that disclosure is inadequate, the conduct of such companies is not disciplined by public scrutiny. Fortunately, this problem may be easily addressed. This Article demonstrates the need for, and then concludes with suggestions for, a stronger approach to making information about capital flows to SSTs more available, thereby fostering more sound investments and perhaps more responsible business.

8. Cuba was listed as an SST in 1982, "primarily because of its support for the M-19 guerrilla organization in Colombia." Hufbauer et al., supra note 4, at 5. Cuba remains on the list "because it continues to provide [a] safe haven to individual terrorists and maintains ties to Latin American insurgents." Id.

9. The State Department listed Iran as an SST in 1984 "in response to [its] alleged . . . involvement in the bombing of the U.S. marine base in Lebanon." Id. at 3.

10. Sudan was listed as an SST in 1993 for harboring terrorists and for its unwillingness to cooperate with international counterterrorism efforts. See id. at 4.

11. In order to study the problem of securities being sold to U.S. investors without disclosing the issuer's operations in countries designated as SSTs and sanctioned by the United States, this Article will focus on the three SSTs subject to the most stringent U.S. sanctions and in which foreign investment is likely: Iran, Sudan, and Cuba. This Article will not include a discussion of Syria, which has not historically offered significant business opportunities to outside companies. But see Jay Solomon, Syria Cracks Open Its Frail Economy, Wall St. J., Sept. 1, 2009, at A1; Jay Solomon, Syria to Open Its Economy to Foreign Investors, Wall St. J., May 14, 2009, at A11.

12. See infra Part V (discussing those findings, which were collected using the SEC's Electronic Data Gathering Analysis and Retrieval system (EDGAR)).

13. The current limitations of the SEC's web-based search engine, EDGAR, make finding companies' disclosure of such activities difficult. For example, full text searches of a company's disclosure are only available for documents that are less than four years old. For a more detailed discussion of the limitations of EDGAR for these purposes, see infra Part V.A.2.b.
B. The Halliburton Story

The story of Halliburton Company provides an introduction to the confusion between existing securities law and the stated objectives of U.S. security policy. Founded in 1919, Halliburton is one of the world’s largest providers of products and services to the energy industry. Halliburton derives over half of its revenue from operations outside the United States, and it owns or controls a large number of U.S. and non-U.S. subsidiaries.

In 2002 and 2003, one of Halliburton’s non-U.S. subsidiaries, Halliburton Products and Services, Ltd. (HPSL), earned all of its approximately $30 million to $40 million in annual revenues from oilfield service work in Iran. At that time, Iran was already the subject of comprehensive U.S. sanctions. Consequently, U.S.-incorporated companies could not—and in fact, still cannot—do business in Iran. Nevertheless, by using HPSL, Halliburton was able to do indirectly what it could not do directly because HPSL is incorporated in the Cayman Islands and headquartered in Dubai, United Arab Emirates (neither of which imposes sanctions on Iran). Halliburton’s Iranian activities may have worked against the intent of the U.S. sanctions,
but they were not necessarily illegal because the U.S. measures apply to U.S. companies but not their non-U.S. subsidiaries.\textsuperscript{20}

Moreover, because HPSL’s revenues represented only about 0.5% of Halliburton’s revenue,\textsuperscript{21} Halliburton took the position that the Iran business was not material and did not need to be disclosed to investors. Halliburton’s disclosure documents filed with the SEC for 2002 provided no information about HPSL’s activities in Iran and no discussion of any risk that those activities might pose to Halliburton’s share value or reputation other than a brief reference to potential “restrictions on our ability to provide products and services to Iran, Iraq and Libya, all of which are significant producers of oil and gas.”\textsuperscript{22} Halliburton’s disclosure for 2003 discussed HPSL and activities in Iran only in the context of informing investors that Halliburton had received a letter from the Department of the Treasury’s Office of Foreign Assets Control (OFAC) requesting information about the company’s compliance with U.S. sanctions on Iran.\textsuperscript{23}

Regardless of whether Halliburton’s business in Iran was in compliance with U.S. sanctions on Iran, some of Halliburton’s investors would have considered the company’s business activities in Iran as important to their investment decision. On November 12, 2002, William Thompson, Comptroller of the City of New York and investment adviser and trustee of the New York City Police and Fire Department Pension Funds (the “NYC Funds”), which together held nearly 318,000 shares of Halliburton, began to pressure Halliburton to disclose details about its Iranian business by submitting a shareholder proposal to have the company establish a committee of its Board of Directors to review the risks of its operations in Iran.\textsuperscript{24} Halliburton

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\textsuperscript{20} But see infra Part II.B.1 (discussing facilitation and approval).

\textsuperscript{21} Press Release, Halliburton Co., supra note 18.

\textsuperscript{22} Halliburton Co., Annual Report (Form 10-K), at 43 (Mar. 28, 2003), http://www.sec.gov/Archives/edgar/data/45012/000004501203000018/ed10k_2002.txt (last visited Feb. 10, 2010). The reference was found in a “Legal” subsection of the “Forward Looking Information” section as an example of a type of risk and uncertainty that might cause actual results to differ from Halliburton’s forward-looking statements and potentially adversely affect its financial condition and results of operations. See id.

\textsuperscript{23} See Halliburton Co., Annual Report (Form 10-K), at 54 (Mar. 8, 2004), http://www.sec.gov/Archives/edgar/data/45012/000004501204000086/ed10k2003.txt (last visited Feb. 10, 2010). In connection with that disclosure, the 2003 Form 10-K also mentioned that Halliburton had received a similar inquiry in mid-2001 and that the company had responded that it believed it was in full compliance with U.S. sanctions regulations. See id.

\textsuperscript{24} See Letter from William C. Thompson, Jr., Comptroller, Office of the Comptroller of the City of N.Y., to Ms. Susan Steward Keith, Vice President & Sec’y, Halliburton Co. (Nov. 12, 2002), in Halliburton Co., SEC No-Action Letter, 2003 WL 1561298, at *4 (Mar. 14, 2003) [hereinafter SEC No-Action Letter]. Halliburton resisted the NYC Funds’ request. Halliburton wrote to the SEC to request permission to omit the proposal from the proxy materials. See
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eventually released a brief report summarizing its activities in Iran.\textsuperscript{25} Partially fueled by then-Vice President Dick Cheney's connection with the company, several negative articles and news programs about Halliburton's Iranian activities added to the pressure.\textsuperscript{26}

In 2005, in the face of investor pressure, negative publicity, and government inquiries into Halliburton's compliance with U.S. sanctions programs,\textsuperscript{27} Halliburton announced that HPSL would wrap up its existing business in Iran and launch no new business there. Nevertheless, Halliburton firmly maintained that, given the small percentage of Halliburton revenue represented by the Iranian activities and its decision not to accept any new contracts,

\begin{quote}
[w]e do not believe our remaining contracts with Iran constitute a material investment risk for our shareholders. We are not aware that any person or entity has made the decision to invest or not to invest in Halliburton based on activity in Iran, nor do we think it likely that they would do so.\textsuperscript{28}
\end{quote}
In March 2007, Halliburton opened a second corporate headquarters in Dubai, United Arab Emirates, and it moved its CEO to that office. In April 2007, Halliburton announced that all of its contractual commitments in Iran had been completed, and that it no longer was doing business there. Again, Halliburton maintained that its Iranian activities had not been in violation of U.S. laws and regulations.

Despite shareholder objections and negative publicity about HPDL’s Iranian activities, Halliburton’s quarterly disclosure (Form 10-Q) and annual disclosure (Form 10-K) never included more potentially negative information about Iran than a brief mention of the OFAC inquiry and the inclusion of Iran in a long list of countries in which Halliburton operates and in which significant amounts of political risk exist. In fact, some of the disclosure about the OFAC inquiry included information about a study that Halliburton undertook in 2002 and 2003, which had found that Halliburton’s Iranian activities complied with all U.S. laws.

The Halliburton story is unusual because it was known to the public and resulted in Halliburton’s eventual decision to discontinue operations in the Sanctioned Country. Review of company disclosure patterns demonstrates that many companies conclude, like Halliburton did, that their lawful activities in SSTs that are subject to U.S. sanctions are not material under U.S. securities regulations and therefore do not need to be disclosed to U.S. investors.

This Article looks first at how the United States sanctions SSTs and then at the disclosures that the United States requires of public com-

May 15, 2006 letter from Cecilia D. Blye, Chief, Office of Global Sec. Risk, SEC, to David J. Lesar, President and CEO, Halliburton Co., that inquired about Halliburton and HPDL operations in Iran.


31. See id. (“Separate from the OFAC inquiry, we completed a study in 2003 of our activities in Iran during 2002 and 2003 and concluded that these activities were in compliance with applicable sanction regulations.”).
panies that do business in the sanctioned SSTs. Part II walks through the extensive measures that the United States has put in place in order to isolate and restrict capital flows to the Sanctioned Countries. Part III looks at U.S. securities regulation and the standards—particularly materiality—that govern disclosure of operations in or with the Sanctioned Countries. Part IV reviews efforts by investors, non-governmental organizations (NGOs), the SEC, and private data services to promote disclosure about companies’ activities in or with the Sanctioned Countries, and it then explores the objections that have been raised to proposed disclosure requirements. Part IV concludes that the attention of issuers and others demonstrates that operations in or with the Sanctioned Countries are material within the meaning of the securities laws. Part V presents the empirical results of a study that reviewed companies’ disclosure of activities in or with the Sanctioned Countries and demonstrates that disclosure is inadequate. Part VI draws conclusions from the disclosure patterns and makes some recommendations for change.

II. U.S. Sanctions Programs

A. Background, Uses, and Authority

Economic sanctions are “the deliberate, government-inspired withdrawal, or threat of withdrawal, of customary trade or financial relations.” Sanctions are an old weapon, historically connected with warfare, that are designed to isolate another country. In 1919, President Woodrow Wilson famously stated,

A nation that is boycotted is a nation that is in sight of surrender. Apply this economic, peaceful, silent, deadly remedy and there will be no need for force. It is a terrible remedy. It does not cost a life

32. See infra notes 37–178 and accompanying text.
33. See infra notes 179–249 and accompanying text.
34. See infra notes 250–332 and accompanying text.
35. See infra notes 333–380 and accompanying text.
36. See infra notes 381–389 and accompanying text.
38. Their first recorded use was in 432 BCE, when Pericles adopted the Megarian Decree. See id. at 9–10; Thucydides, History of the Peloponnesian War 139–40 (Rex Warner trans., Penguin Books 1954) (mentioning the Megarian Decree as a trigger of the first part of the Peloponnesian War); see also Aristophanes, Acharnians 520–43 (Jeffrey Henderson ed. & trans., Harvard Univ. Press 1998) (assigning the Megarian Decree more direct responsibility for starting the war).
39. Most well known in U.S. history, perhaps, was the North’s blockade of the Confederate States during the Civil War, as the result of which the South lost crucial access to foreign imports. See Hufbauer et al., supra note 37, at 40.
outside the nation boycotted but it brings pressure upon the nation which, in my judgment, no modern nation could resist.\textsuperscript{40}

Since World War I, countries have imposed economic sanctions more than 187 times to achieve their goals.\textsuperscript{41} By imposing economic sanctions, instead of or in addition to military force, a country is trying to change the behavior of another country's government.\textsuperscript{42} Sanctions are an instrument of foreign policy,\textsuperscript{43} "part and parcel of international diplomacy."\textsuperscript{44}

Sanctions remain controversial. While sanctions may avoid bloodshed for the sanctioning country, sanctions impact the target country like a siege: the greatest suffering is inflicted on society's weakest elements.\textsuperscript{45} Business interests tend to oppose sanctions, citing their adverse impact on competitiveness.\textsuperscript{46} In addition, sanctions may fail.\textsuperscript{47} Many policymakers doubt their effectiveness,\textsuperscript{48} and since the onset of the financial crisis, some analysts have argued that sanctions stand in...

\textsuperscript{40} Id. at 1 n.1 (citing \textsc{Wilson's Ideals} 108 (Saul K. Padover ed., 1942)). The increase in the use of economic sanctions was also connected to the establishment of the League of Nations.

\textsuperscript{41} For a list, see id. at 20–38 (presenting Table IA-1 for the period 1914–2000 and Table IA-2 for the period 2000–2006).

\textsuperscript{42} See Raj Bhala, \textit{MRS. WATU and International Trade Sanctions}, 33 \textsc{Int'l Law}. 1, 2 (1999).

\textsuperscript{43} See id. at 1.

\textsuperscript{44} \textsc{Hufbauer et al.}, supra note 37, at 5.

\textsuperscript{45} For a demonstration of this effect, see Richard Garfield, Morbidity and Mortality Among Iraqi Children from 1990 Through 1998: Assessing the Impact of the Gulf War and Economic Sanctions (Mar. 1999) (unpublished manuscript), available at https://www.ciaonet.org/wps/garo/index.html (showing that mortality among children under five doubled during the 1990s, accounting for "a minimum of 100,000 and a more likely estimate of 227,000 excess deaths among young children from August 1991 through March 1998," most of which were associated with sanctions (emphasis added)). See also \textsc{Geoff Simons}, \textit{Imposing Economic Sanctions: Legal Remedy or Genocidal Tool?} 124–40 (1999) (detailing the U.S. imposition of sanctions on Cuba and categorizing them as "genocide").

\textsuperscript{46} See, e.g., USA Engage, Background and History, http://www.usaengage.org (last visited Feb. 10, 2010).

\textsuperscript{47} See \textsc{Hufbauer et al.}, supra note 37, at 7–9.

\textsuperscript{48} See, e.g., Posting of Simon Cox, Economics Correspondent, \textit{The Economist}, to Council on Foreign Relations, Online Debate, Are Economic Sanctions Good Foreign Policy? (July 27, 2007), http://www.cfr.org/publication//13853/are_economic_sanctions_good_foreign_policy.html (last visited Feb. 10, 2010) (noting that "by the time sanctions are imposed, they have probably already failed"). For a more positive explanation, see R. Richard Newcomb, Former Dir. of the Office of Foreign Assets Control, Canada and U.S. Approaches to Trade Sanctions—U.S. Speaker, Address at the Proceedings of the Canada-United States Law Institute Conference on Understanding Each Other Across the Largest Undefended Border in History (Apr. 15, 2005), in 31 \textsc{Can.-U.S. L.J.} 43, 44 (2005) ("I certainly hope it safely can be said that we demonstrated that sanctions can be an effective tool of U.S. foreign policy and national security."). Mr. Newcomb served as the director of the Office of Foreign Assets Control (OFAC) from January 1987 until October 2004.
the way of restoring U.S. economic prosperity. After all, Halliburton moved its CEO and half of its headquarters to Dubai.

U.S. economic sanctions are often particularly controversial for several reasons. First, the United States sanctions frequently. It has been estimated that approximately two-thirds of the world's population has been subject to U.S. economic sanctions at some point. Second, U.S. sanctions often affect third parties that are neither in the United States nor the target country. Applied extraterritorially, U.S. sanctions regimes may conflict with international legal principles regarding a nation's authority to legislate, and they have triggered negative responses by other countries. For example, U.S. trading

49. See, e.g., Bryan Early, Op-Ed, To Lift the US Economy, Lift Sanctions on America's Foes, CHRISTIAN SCI. MONITOR, Mar. 25, 2009, at 9 ("American sanctions cost American jobs. With a new administration and a major economic crisis before us, there is a unique opportunity for policymakers to overcome the entrenched interests that support the sanctions against countries such as Iran and Cuba and do something positive for the American economy.").


51. For a conflicting view, see Jesse Helms, What Sanctions Epidemic? U.S. Business' Curious Crusade, FOREIGN AFF., Jan.-Feb. 1999, at 2, 4 ("The allegation of a sanctions epidemic is demonstrably false—a myth spread with the intention of misleading Congress, the American Public, and the American business community.").

52. See Bhala, supra note 42, at 4. Sanctions have been popular with both Republican and Democratic administrations and are one of the principal tools of U.S. foreign policy. See Newcomb, supra note 48, at 45.

53. The U.S. trend toward increased extraterritorial use of sanctions can be discerned in many developments. For example, the Cuban Democracy Act, enacted in 1992, included a provision that prohibited U.S.-owned or -controlled firms in foreign countries from engaging in certain types of transactions in Cuba. See 22 U.S.C. § 6005(a) (2006). For a more general discussion of this and similar provisions of the Cuban Democracy Act, see Comm. on Inter-Am. Affairs, The Legality of the Extra-Territorial Reach of the Cuban Democracy Act of 1992, 51 REC. Ass'N B. CTTY N.Y. 322, 327 (1996).

54. This is not only true in the context of economic sanctions. Consider, for example, Judge Learned Hand's famous ALCOA decision in 1945 regarding the use of the Sherman Act to bring charges against foreign aluminum traders who affected the price of aluminum in the United States. See United States v. Aluminum Co. of Am., 148 F.2d 416 (2d Cir. 1945).

55. Generally, a state's legislation with regard to conduct satisfies these criteria only (1) if the conduct takes place "wholly or in substantial part . . . within its territory," (2) if the conduct is intended to have substantial effect within its territory, or (3) if the conduct is directed against the security of the state or a limited class of other states interests. RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 402(1)(a); see also id. §§ 401(1)(c), 403(3). Even when one of the bases for legislative jurisdiction is present, international law would not permit a state to legislate "with respect to a person or activity having connections with another state [if] the exercise of such [legislative] jurisdiction [would be] unreasonable." Id. § 403(1). When it would not be unreasonable for each of two states to legislate with respect to a particular matter and the legislation of the two states conflicts, a state should, under international law, defer to the other state if the interest of the other state is clearly greater. See id. § 403(3).

56. Negative responses have not been limited to other countries. A variety of U.S. and international private sector groups have sharply criticized U.S. imposition of extraterritorial sanctions. See, e.g., Gary G. Yerkey, Advisory Panel Set to Urge State Department to Oppose Extraterritorial Sanctions by U.S., 25 Int'l Trade Rep. (BNA) 830 (June 5, 2008); see also HARRY
partners have objected in multilateral venues and enacted "blocking statutes" that prohibit their companies from complying with U.S. sanctions. The U.S. sanctions programs against Iran, Sudan, and Cuba analyzed in this Article all have significant impacts on non-U.S. entities. Third, U.S. sanctions are often imposed unilaterally. That is, the United States may impose measures limiting the activities of U.S. companies in SSTs. Other states, however, may choose not to impose such restrictions on companies that are incorporated under their law. The resulting gap created the space for the Halliburton conflict, and this gap is getting bigger.

The United States' frequent, extraterritorial, and unilateral use of sanctions means that companies with activities in multiple jurisdictions may be subject to different and conflicting regulations. These conflicts create not only difficulties for those companies but also opportunities to capitalize on the gaps, a form of regulatory arbitrage. Companies that have operations in terrorism-sponsoring countries that are subject to U.S. sanctions, and that also offer securities in the United States without even disclosing those operations, capitalize on the differences among regulatory regimes.


57. For example, the European Union took the United States to the World Trade Organization (WTO) Dispute Settlement Body over the extraterritorial measures put into place by the United States in 1996. See infra note 171 and accompanying text.

58. For a full survey and analysis of such measures, see CLARK & WANG, supra note 56, at 8–12.

59. The United States also has such a "blocking" statute: the anti-boycott law that grew out of U.S. opposition to the Arab League's boycott of Israel. The U.S. law was part of the 1977 Amendments to the Export Administration Act. See 15 C.F.R. § 760.2 (2009).


62. For example, approximately 50 German firms have branch offices in Iran, and nearly 12,000 German companies do business there. Mehr News Agency, 12,000 German Companies Doing Business in Iran, PAYVAND IRAN NEWS, May 5, 2009, http://www.payvand.com/news/09/may/1055.html (last visited Feb. 10, 2010).
Most U.S. sanctions are imposed through executive action by OFAC, a part of the Department of the Treasury. In some cases, Congress, states, and even local municipalities impose measures as well. Currently, OFAC imposes restrictions with respect to thirteen

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63. This Article focuses on formal U.S. sanctions programs, but it is important to bear in mind that much of U.S. action is more informal. For example, in the mid- and late 2000s, U.S. Treasury officials met with dozens of banks worldwide to discuss the financial and reputational risk of doing business with Iran. See Isolating Proliferators and Sponsors of Terror: The Use of Sanctions and the International Financial System to Change Regime Behavior: J. Hearing Before the Subcomm. on Terrorism, Nonproliferation & Trade of the H. Comm. on Foreign Affairs and the Subcomm. on Domestic and International Monetary Policy, Trade & Technology of the H. Comm. on Financial Servs., 110th Cong. 29–30 (2007) (joint statement of Daniel Glaser, Deputy Assistant Sec'y for Terrorist Fin. & Fin. Crimes, and Adam J. Szubin, Dir. of OFAC). Deputy Assistant Secretary Glaser and OFAC Director Szubin referred to the voluntary implementation of U.S. sanctions by non-U.S. international financial institutions as a decisive “force multiplier.” Id. at 28. Economic sanctions are also occasionally imposed by the United Nations. U.S. imposition of sanctions in such a multilateral context, however, does not create the “gap” or the disclosure problem that is the focus of this Article.


65. Typically, the President will issue an executive order declaring an international emergency and directing the Department of the Treasury to promulgate appropriate regulations. Sanctions put into place before 1977 were based on the Trading with the Enemy Act (TWEA). See 50 U.S.C. § 5(b)(1)(B) (2006) (authorizing the President of the United States “during the time of war” to prevent or prohibit transactions in any property in which a foreign country or national has any interest by any person subject to the jurisdiction of the United States). The embargo against Cuba is based on TWEA. For more recent sanctions programs, the International Emergency Economic Powers Act (IEEPA) provides the statutory authority. 50 U.S.C. §§ 1701-07 (2006). The sanctions against Iran and the Sudan are primarily based on IEEPA, which was amended in 2007 by the International Emergency Economic Powers Enhancement Act to increase the civil penalties for violations of orders or regulations issued pursuant to IEEPA. Pub. L. No. 110-96, 121 Stat. 1011 (amending IEEPA § 206, 50 U.S.C. § 1705 (2006)).

66. State and local measures were used most famously against South Africa in the 1980s and early 1990s. However, some state measures have been successfully challenged. See, e.g., Crosby v. Nat'l Foreign Trade Council, 530 U.S. 363 (2000) (overturning Massachusetts's Burma law); Nat'l Foreign Trade Council v. Giannoulas, 523 F. Supp. 2d 731 (N.D. Ill. 2007) (striking down Illinois's Sudan law).

67. Technically, they are licensing systems with detailed rules about which activities require a license. See Lillian V. Blageff, Overview of U.S. Sanctions and Embargoes Programs, Including 2006 Update, 16 IN'TL HUM. RTS. J. 3 (2007). Thus, some transactions may qualify for a so-called general license, which means that they may be undertaken without prior OFAC approval. All others must receive a license from OFAC on a case-by-case (that is, “specific”) basis. In the more extensive sanctions programs, such as the ones for Cuba, Iran, and Sudan, a license may be required for virtually all activity and be nearly impossible to obtain. See generally Tracy J. Chin, An Unfree Trade in Ideas: How OFAC's Regulations Restrict First Amendment Rights, 83 N.Y.U. L. REV. 1883 (2008) (discussing the denial of a license to Iranian author and Nobel Peace Prize winner, Shirin Ebadi).
countries including Cuba, Iran, and Sudan, which are also among the countries designated as SSTs.

B. U.S. Sanctions on Iran

1. OFAC Measures

The United States has imposed some kind of economic sanction on Iran since the Islamic revolution in 1979. The current Iranian Transactions Regulations were put into place pursuant to President Ronald Reagan’s 1987 Executive Order 12,613, which imposed an import embargo on Iranian-origin goods and services in response to Iran’s support for international terrorism and its aggressive actions against


69. SSTs are countries designated by the Department of State under § 6(j) of the Export Administration Act of 1979. Such countries are then subject to restrictions on, for example, U.S. foreign assistance, including Export-Import Bank credits and guarantees under the Foreign Assistance Act of 1961. Historically, the U.S. State Department’s list of “State Sponsors of Terrorism” could be different from the list of countries designated by the Department of the Treasury, through OFAC, in the “Terrorism List Governments Sanctions Regulations,” which was based on the countries designated as of the effective date of those regulations. In May 2009, however, OFAC revised the regulations to reconcile the two lists, with the result that Iraq, Libya, and North Korea were removed from the OFAC list. See 31 C.F.R. § 596.201 (2009).

70. For a full discussion of the chronology and impact of various U.S. sanctions against Iran, which is beyond the scope of this Article, see Hufbauer et al., supra note 37, at 144-46.


nonbelligerent shipping in the Persian Gulf.\(^{73}\) Between 1995 and 1997, President William J. Clinton issued Executive Orders 12,957,\(^{74}\) 12,959,\(^{75}\) and 13,059,\(^{76}\) which initially prohibited U.S. involvement with petroleum development in Iran, and later prohibited virtually all trade and investment activities with Iran.\(^{77}\)

The Iranian Transaction Regulations prohibit the importation of Iranian goods or services into the United States,\(^{78}\) as well as the exportation of almost all U.S. goods, technology, or services to Iran.\(^{79}\) With the exception of contracts entered into before May 7, 1995, no investment in Iran is permitted.\(^{80}\) The regulations also prohibit financing, trading, or performing services related to Iranian oil or petroleum products that are refined in Iran.\(^{81}\) All transactions with the broadly defined "Government of Iran" are also prohibited.\(^{82}\)

Thus, the regulations amount to a ban on virtually all U.S. trade and investment activities with Iran, and they apply to all "U.S. Persons," defined as "any United States citizen, permanent resident alien, entity organized under the laws of the United States (including foreign branches), or any person in the United States."\(^{83}\) The OFAC Iranian


\(^{76}\) See Exec. Order No. 13,059, 3 C.F.R. 217 (1997) (clarifying Executive Orders 12,957 and 12,959, and confirming that virtually all trade and investment activities with Iran by U.S. persons are prohibited).

\(^{77}\) Two subsequent changes were made to the regulations. In 2000, the sanctions were eased by the Trade Sanctions Reform and Export Enhancement Act (TSREEA) in order to allow U.S. persons to purchase and import carpets and certain food products. See Pub. L. No. 106-387, 114 Stat. 1549A-67 (codified as amended at 22 U.S.C. §§ 7201-11 (2006)). In 2008, sanctions were tightened when authorization for so-called U-turn transactions that involve Iran was revoked. See 73 Fed. Reg. 66,541, 66,541-42 (Nov. 10, 2008) (amending 31 C.F.R. §§ 560.405, 560.516).

\(^{78}\) See 31 C.F.R. § 560.201 (2009).

\(^{79}\) There is an exception for U.S. agricultural exports. In fact, in the summer of 2008, Iran bought more than one million tons of hard red winter wheat directly from the United States—its first purchase of U.S. wheat since the 1981-1982 marketing year. Tom Polansek & Louise Radnofsky, Iran Buys Wheat from U.S. for First Time in 27 Years, WALL ST. J., Aug. 21, 2008, at A3; see 31 C.F.R. § 560.204.

\(^{80}\) See id. § 560.207.

\(^{81}\) See id. § 560.209.

\(^{82}\) See id. pt. 560. "Government of Iran" is defined in 31 C.F.R. § 560.304 to include any entity owned or controlled by the Government of Iran, which is in turn defined in § 560.313. In December 2008, OFAC further expanded the scope of that definition to include various nonfinancial as well as financial institutions determined to be owned or controlled by the Government of Iran. See id. pt. 560 app. A (2009).

\(^{83}\) Id. § 560.314.
regulations do not directly apply to the foreign subsidiaries of U.S. companies, but they do prohibit any U.S. person from approving, financing, facilitating, or guaranteeing a transaction between Iran and a foreign person (such as a foreign subsidiary of a U.S. company) if the U.S. person is precluded from performing the transaction directly. The scope of the Iranian regulations’ application to non-U.S. subsidiaries of U.S. companies has been controversial. The activities conducted in Iran by HPSL, discussed above in Part I.B, may be an example of the uncertain scope of the “approval and facilitation” language.

2. Congressional Action

a. The Iran Sanctions Act

Many other countries chose not to join the United States in enacting trade sanctions against Iran in 1995 and 1996. In fact, in late 1995, foreign companies began to increase their investment in Iran’s energy sector, and those investments produced profits that the unilateral U.S. sanctions denied to U.S. companies. In 1996, the U.S. Congress passed and President Clinton signed what is now known as the Iran Sanctions Act (ISA).

The ISA prohibits any person from making an investment of over $20 million per year that directly and significantly contributes to the enhancement of Iran’s ability to explore for, extract, refine, or trans-

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84. See id. § 560.208 ("[N]o United States person, wherever located, may approve, finance, facilitate, or guarantee any transaction by a foreign person where the transaction by that foreign person would be prohibited by this part if performed by a United States person or within the United States.").


87. See id. at 1–2.

88. The Iran Sanctions Act (ISA) was originally known as the Iran and Libya Sanctions Act of 1996. See Pub. L. No. 104-172, 110 Stat. 1541. However, on April 23, 2004, President George W. Bush certified that Libya had fulfilled the requirements of all UN resolutions relating to the downing of Pan Am Flight 103, and the Act was terminated with respect to Libya. See Katzman, supra note 86, at 3. The ISA was renewed in 2001 and again in 2006, and it is currently scheduled to expire on December 31, 2011.

89. The definition of “investment” in the ISA includes entry into a contract [on or after August 5, 1996] that includes responsibility for the development of petroleum resources located in Iran or . . . provides for the general supervision and guarantee of another person’s performance of such a contract. . . . or provides for the participation in royalties, earnings, or profits [from such] development
port by pipeline its petroleum and natural gas reserves. The ISA instructs the President to impose at least two sanctions from a menu of seven possible sanctions on any person that the President determines has made such an investment. The sanctions choices include measures such as denying the U.S. Export-Import Bank’s assistance for the export of any goods or services to the sanctioned person, and prohibiting any U.S. financial institution’s extension of more than $10 million in credit during a twelve-month period to any sanctioned person.90

U.S. companies were already prohibited from investing in Iran when the ISA was passed. Its primary targets were non-U.S. companies profiting from the exploitation of the significant oil and natural gas resources in Iran. Such investment is often not prohibited under the law of those companies’ home countries.

However, the ISA has not been enforced by the United States. The President may waive application of sanctions if he certifies that doing so is important to the U.S. national interest.91 One such waiver was granted by President Clinton for the 1997 investment in the South Pars gas field by French company Total S.A., along with Russia’s Gazprom and Malaysia’s Petronas.92

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90. The sanctions include (1) denial of Export-Import Bank loans, credits, or credit guarantees for U.S. exports to the sanctioned person; (2) denial of licenses for the U.S. export of military or militarily useful technology; (3) denial of U.S. bank loans exceeding $10 million in one year; (4) if the sanctioned person is a financial institution, a prohibition on its service as a primary dealer in U.S. government bonds; (5) if the sanctioned person is a financial institution, a prohibition against serving as a repository for U.S. government funds; (6) prohibition on U.S. government procurement from the sanctioned person; and (7) restrictions on imports from the sanctioned person, in accordance with the International Emergency Economic Powers Act. See Pub. L. No. 104-172, § 14(9), 110 Stat. 1549–50 (current version at 50 U.S.C. § 1701 note (2006)). It also includes additions to existing investment. See ILSA Extension Act of 2001, Pub. L. No. 107-24, § 5, 115 Stat. 199, 200 (current version at 50 U.S.C. § 1701 note (2006)). Expressly excluded from the definition of “investment” are the “entry into, performance, [and] financing of contract[s] to sell or purchase goods, services, or technology.” See Pub. L. No. 104-172, § 14(9), 110 Stat. 1550 (current version at 50 U.S.C. § 1701 note (2006)).

91. See Pub. L. No. 104-172, § 9(c), 110 Stat. 1547 (current version at 50 U.S.C. § 1701 note) (providing a presidential waiver in the “national interest”). There are also several “exceptions” that grant the President discretion not to impose sanctions, such as when sanctions would negatively affect the procurement of goods or services that are essential to national security. See id.

92. The waiver was part of the settlement of the European Union’s WTO complaint about the United States’ extraterritorial application of both the ISA and the Helms-Burton Act. See KATZMAN, supra note 86, at 3; infra notes 156–173 and accompanying text. Total S.A. recently announced that it is seeking to continue its investment in Iran in partnership with the China National Petroleum Corporation (CNPC). See Simon Hall & Jason Dean, Total Aims for Deeper Ties to Chinese Firm, WALL ST. J., Dec. 22, 2009, at B3.
b. Additional Congressional Measures Against Iran

In the United States, there has been some frustration with the weakness of the ISA\(^93\) and the unwillingness of successive administrations to enforce it. U.S. companies are strongly prohibited from doing business in Iran, but many of their foreign competitors and even affiliates conduct business in Iran. Companies that have operations in Iran may not make the operations widely known, and yet they are able to access the U.S. capital markets freely. In the final years of the Bush Administration, Congress considered several different pieces of legislation that would have produced better information or restricted access to U.S. capital markets by companies doing business in Iran.\(^94\) None, however, were enacted.

President Barack Obama initiated a new approach of outreach to U.S. adversaries.\(^95\) The Obama Administration adopted a "two-track" policy of engagement with Iran, which was backed by the prospect of new sanctions. The United States made several overtures to the Iranian regime, and it attempted to broker a deal to ship more than half of Iran's low-enriched uranium abroad.\(^96\) However, the contested June 2009 election, harsh treatment of democratic protests, and the discovery of an undisclosed uranium facility in Qom further strained U.S.-Iranian relations.\(^97\)

Congress has continued to work to stiffen sanctions on Iran. In October 2009, the House overwhelmingly approved the Iran Sanctions Enabling Act,\(^98\) which authorizes a state or local government to adopt

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and enforce measures to prohibit the investment of its assets in Iran's 
energy sector, and to divest its assets from or prohibit the investment 
of assets it controls in, persons who have investments of more than 
$20 million in Iran's energy sector. In December 2009, the House 
passed the Iran Refined Petroleum Sanctions Act, which aims to 
restrict gasoline supplies to Iran and strengthen the ISA. On January 
28, 2010, the Senate passed the Comprehensive Iran Sanctions, Ac- 
countability and Divestment Act of 2009, which seeks to expand the 
ISA, impose new sanctions on entities that are involved in exporting 
refined petroleum products to Iran or building Iran's domestic re- 
fining capacity, impose a broad ban on most imports from and exports to 
Iran, freeze the assets of Iranians active in weapons proliferation or 
terrorism, and enable Americans to divest their assets from energy 
firms doing business with the Iranian regime.

3. State Measures

In addition, approximately a dozen states—including Arizona, Cali- 
ifornia, Florida, Georgia, Illinois, Indiana, Louisiana, Michigan, 
Minnesota, Missouri, and New Jersey—re-
quire their state investment boards, pension funds, or both to divest their assets from companies that do business in Iran. Many other states have more limited measures in place or under review.\textsuperscript{114} The adoption of these Iranian divestment measures indicates that information about companies’ business in and with Iran is material; these large, influential institutional investors cannot make an informed investment decision without such information. Furthermore, restrictions on and risks associated with investment in Iran may increase due to Iran’s continued refusal to abandon its plans to acquire nuclear weapons. Investors’ need to know about business in Iran is likely to increase.

\section*{C. U.S. Sanctions on Sudan}

\subsection*{1. OFAC Measures}

The United States has maintained sanctions against Sudan for over a decade.\textsuperscript{115} Citing the Government of Sudan’s (the “GOS”) continued support for international terrorism, its efforts to destabilize neighboring governments, and its widespread human rights violations, President Clinton issued Executive Order 13,067 in 1997.\textsuperscript{116} The Order resulted in OFAC’s promulgation of the Sudanese Sanctions Regulations (the “SSRs”) on July 1, 1998. The SSRs prohibit U.S. companies without a license from engaging in commercial transactions with the GOS.\textsuperscript{117} In addition, the SSRs block any property or interests in property of the GOS that are in the United States or within the possession or control of U.S. companies.\textsuperscript{118} The SSRs were expanded by President Bush in 2006,\textsuperscript{119} and they now block all property of persons determined to be contributing to the conflict in Darfur.\textsuperscript{120}


\textsuperscript{117} See OFAC, supra note 115, at 11.

\textsuperscript{118} See 31 C.F.R. § 538.201 (2009); OFAC, supra note 115, at 4.


\textsuperscript{120} These provisions implement the Darfur Peace and Accountability Act of 2006, which calls for support of the Government of Southern Sudan and assistance with the peace efforts in...
impose a broad trade embargo on Sudan. In addition, the 2006 changes excluded the regional Government of Southern Sudan (the "GOSS") and several other areas of Sudan (the "Specified Areas") from the definition of the GOS, thereby removing them from the scope of the blocking authority under the U.S. regulations.\textsuperscript{121} The regulations also now prohibit all U.S. companies from engaging in transactions "relating to petroleum or petro-chemical industries in Sudan, including but not limited to oil, oilfield services, and oil or gas pipelines."\textsuperscript{122}

The SSRs, like the Iranian regulations, largely do not apply to non-U.S. subsidiaries of U.S. companies, although they do have some "anti-facilitation" language. The SSRs apply to "U.S. Persons," again defined as "any United States citizen, permanent resident alien, entity organized under the laws of the United States or any jurisdiction within the United States (including foreign branches), or any person in the United States."\textsuperscript{123} The SSRs "prohibit the facilitation by a U.S. person of the direct or indirect exportation or reexportation of goods, technology or services to or from non-Specified Areas of Sudan."\textsuperscript{124} The SSRs do not prohibit facilitation of a trade or financial transaction that the U.S. person could engage in directly.\textsuperscript{125} Further, the SSRs allow U.S. persons to perform "services of a purely clerical . . . nature, such as reporting on the results of a subsidiary's trade, that [do] not further trade or financial transactions with Sudan or the [GOS]."\textsuperscript{126}

In May 2009, in furtherance of the purposes of the executive orders issued by President George W. Bush in 2006 and as a complement to the SSRs, OFAC promulgated a separate set of Darfur Sanctions Reg-
The DSRs are targeted sanctions that are directed at certain actors in connection with the conflict in Darfur.

2. Congressional Action

Congress has acted numerous times in response to the conflict in Sudan. In 2002, Congress passed the Sudan Peace Act, which directed the President to work toward a solution in Sudan. In 2004, Congress passed the Comprehensive Peace in Sudan Act, which strengthened the Sudan Peace Act in response to events in Darfur. In 2006, Congress passed the Darfur Peace and Accountability Act, which imposed sanctions against individuals who were responsible for the genocide in Darfur, and included other measures that were designed to support the protection of civilians, humanitarian operations, and peace efforts in Darfur.

Congress acted directly again with the Sudan Accountability and Divestment Act of 2007 (SADA). SADA authorizes state and local governments to divest public assets from companies that are involved in certain business sectors in Sudan. It also provides a safe harbor for mutual funds and pension plans choosing to divest their assets from such companies. Finally, it prohibits the U.S. federal government from entering into new contracts with these offending companies.

In April 2008, the SEC implemented regulations governing disclosure of divestment by registered investment companies in accordance with SADA. These regulations require investment funds that seek the protection of the safe harbor to disclose their divestment from securities and issuers that the investment funds determine either do direct business in Sudan or have investments in companies that do business in Sudan. Thus, the SEC enables investment funds to divest from

128. This is in addition to the changes that resulted from the TSREEA, Pub. L. No. 106-387, 114 Stat. 1549A-67.
130. See id. §§ 2(16)(A), 6(b)(2).
companies that are doing business in an SST, but it still does not advance a mechanism that enables these funds to discover such business to begin with.

3. State Measures Relating to Sudan

Some of the most well-publicized information about companies' activities in or with Sudan has come out because a number of states have revised guidelines for their pension funds, procurement agencies, and treasuries in order to prohibit investment in companies that do business in or with Sudan. The Illinois Act to End Atrocities and Terrorism in the Sudan (the "Illinois Sudan Act") prohibited the Illinois Treasury from depositing state funds into any financial institution that had not certified that it had implemented policies to ensure that loan applicants do not directly or indirectly do business in Sudan, and it restricted the investment of public pension funds in Sudan-connected entities. In February 2007, the U.S. District Court for the Northern District of Illinois struck down the Illinois Sudan Act, stating that it interfered with the federal government's authority over foreign affairs. To some extent, SADA was passed in response to this ruling. Nevertheless, a number of states and institutional investors maintain terror-free or Sudan-free investment disclosure or prohibition provisions.

D. U.S. Sanctions on Cuba

1. OFAC Measures

The third Sanctioned Country considered in this Article is Cuba. U.S. sanctions against Cuba are some of the oldest and most restrictive of existing U.S. sanctions regimes. The Cuban Assets Control

136. See 15 ILL. COMP. STAT. 520/22.5–22.6 (2009); id. 5/1-110.5.
137. See 15 ILL. COMP. STAT. 520/22.6(b)(1)–(5).
140. This was much like the situation when U.S. sanctions against Burma (Myanmar) were meaningfully strengthened after the Supreme Court struck down the Massachusetts law that restricted investment in Burma. See Crosby v. Nat'l Foreign Trade Council, 530 U.S. 363 (2000).
141. For example, the California Public Employees' Retirement Systems (CalPERS) is required to submit to the California legislature a report on investment holdings in companies with business operations in Sudan. See CAL. GOV'T CODE § 7513.6 (West 2008). Another example is the state of Louisiana. See LA. REV. STAT. ANN. § 11:313 (2009).
142. Only the measures in place against North Korea are older. Although North Korea was recently removed from the SST list, the majority of measures remain in place against it. See Yerkey, supra note 5, at 1517. This of course draws into question the efficacy and economic impact of such long-running sanctions. See U.S. INT'L TRADE COMM'N, THE ECONOMIC IMPACT
Regulations (the "CACRs") were issued in 1963, and they prohibit virtually all trade and transactions with Cuban nationals or the Cuban government without an OFAC license. The goal of the sanctions is "to isolate the Cuban government economically and deprive it of U.S. dollars."144

In addition, the CACRs impose a total freeze on Cuban assets in the United States, both government and private; all property of Cuba and Cuban nationals that is within the possession or control of persons subject to the regulations is blocked.145 The CACRs differ from the sanctions against Iran and Sudan because they clearly apply to non-U.S. subsidiaries of U.S. issuers; the CACRs apply to "person[s] subject to the jurisdiction of the United States,"146 which includes all U.S. citizens and permanent residents wherever they are located, all people and organizations physically in the United States, and all branches and subsidiaries of U.S. organizations throughout the world.147 The application of the CACRs to non-U.S. companies owned or controlled by U.S. individuals or companies (that is, foreign subsidiaries) means that U.S. companies cannot conduct operations in or with Cuba indirectly that they cannot conduct directly.

The CACRs have been revised numerous times.148 During President Obama's Administration, for example, the regulations have been eased with respect to restrictions on trade and travel,149 and on the provision of telecommunications services in Cuba.150 Nevertheless,
the United States' long-term policy of isolating Cuba may be noteworthy to investors.

2. Congressional Action

a. The Cuban Democracy Act

Congress has also implemented a number of measures directly. In 1992, partially in response to Cuba’s post-Soviet efforts to attract income through foreign tourism, the Cuban Democracy Act (CDA) was passed. The CDA denounced human rights abuses in Cuba, tightened U.S. restrictions on trade with Cuba, and increased pressure on other countries that provided assistance to Cuba. The most controversial provision of the CDA was the seemingly extraterritorial prohibition on U.S.-owned or U.S.-controlled foreign firms’ engagement in certain types of transactions with Cuba.

b. The Cuban Liberty and Democratic Solidarity (Libertad) Act (Helms-Burton Act)

The subsequent limited market reforms implemented by the Castro regime led to an increase in foreign investment, though due to the OFAC embargo and the CDA, no U.S. or U.S.-controlled companies can make such investments. A turning point came in 1996—just as the Clinton Administration was considering relaxing the U.S. embargo—when the government of Cuba shot down two U.S.-based civilian air-

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153. See id. § 6005. The CDA also prohibited vessels that had entered a Cuban port from loading or unloading in the United States for at least 180 days. See id. § 6005(b).
154. See 22 U.S.C. § 6003. The CDA states,
   The President may apply the following sanctions on any country that provides assistance to Cuba:
   (A) The government of such country shall not be eligible for assistance under the Foreign Assistance Act of 1961 or assistance or sales under the Arms Export Control Act . . . .
   (B) Such country shall not be eligible, under any program, for forgiveness or reduction of debt owed to the United States Government.
   Id. § 6003(b)(1) (citation omitted).
155. See 22 U.S.C. § 6005(a). This section effectively prohibited trade between Cuba and foreign corporations that are owned by U.S. persons. For a good discussion of the extraterritorial reach of the CDA, see Comm. on Inter-Am. Affairs, supra note 53, at 327. Of course, the OFAC regulations had a similar reach, but the direct imposition by Congress of such a measure attracted attention.
craft. Soon afterward,156 Congress passed and President Clinton reluctantly157 signed the Cuban Liberty and Democratic Solidarity (Libertad) Act, which is popularly known as the Helms-Burton Act.158

Like the Cuban Democracy Act, the Helms-Burton Act was primarily targeted at non-U.S. companies doing business in Cuba.159 Under Title III of the Helms-Burton Act,160 any person, including any U.S. or foreign person or entity, that traffics161 in property that was confiscated162 by the Cuban government on or after January 1, 1959 can be liable in U.S. courts to any U.S. national who owns the claim to such property.163 No claims have been filed under Title III, however, because its application has been suspended164 since it went into force.165

Title IV of the Helms-Burton Act requires the U.S. Secretary of State to deny a visa to any alien determined to be a person who con-

158. The legislation was sponsored in the Senate by Jesse Helms (R-NC) and in the House by Dan Burton (R-IN).
159. U.S. companies were already prohibited from that business by the Cuban Assets Control Regulations.
161. Under Title III, a person or entity “traffics” in property if, at any time three months or more after the effective date of Title III, such person knowingly and intentionally:
   (i) sells, transfers, distributes, dispenses, brokers, manages or otherwise disposes of confiscated property, or purchases, leases, receives, possesses, obtains control of, merges, uses or otherwise acquires or holds an interest in confiscated property,
   (ii) engages in commercial activity using or otherwise benefiting from confiscated property, or
   (iii) causes, directs, participates in, or profits from, trafficking . . . by another person . . . without the authorization of any United States national who holds a claim to the property.
162. For these purposes, confiscated property is generally defined as property nationalized, expropriated, or otherwise seized by the Cuban government on or after January 1, 1959, for which adequate compensation has not been paid, with the exception (for Title III purposes) of certain residential property. See id. § 6023(4)(A).
163. The amount of liability to which a trafficker may be subject is unconnected to the benefits derived from the trafficking activity; instead, it is based on the value of the claim to the property. See id. § 6082(a)(1).
164. The Helms-Burton Act provides that the President may suspend the right to bring Title III actions upon a determination that suspension is necessary to the national interests of the United States and will expedite a transition to democracy in Cuba. See id. § 6085(b).
165. The President may suspend Title III for periods of up to six months. See id. Suspensions have been made every six months (in January and July) by Presidents Clinton, Bush, and Obama. For the most recent suspension, see Letter from President Barack Obama to Sen. Daniel K. Inouye, Chairman, Senate Comm. on Appropriations et al. (July 14, 2009), available at http://www.gpoaccess.gov/presdocs/2009/DCPD-200900567.pdf (last visited Feb. 10, 2010).
fiscates property, or who traffics\textsuperscript{166} in confiscated property,\textsuperscript{167} a claim to which is owned by a U.S. national.\textsuperscript{168} Likewise, Title IV requires the Attorney General to exclude these aliens from the United States. Title IV cannot be waived by the President, but it requires action by the U.S. government (normally the Secretary of State) and has been little enforced.\textsuperscript{169}

One of the reasons for the consistent suspension of Title III and the lack of enforcement of Title IV of the Helms-Burton Act has been the negative reactions of U.S. trade partners to its extraterritorial effect.\textsuperscript{170} Since no U.S. persons or entities could trade with Cuba under the existing OFAC embargo, the Helms-Burton Act targeted non-U.S. persons, and it triggered strong objections from other countries. The European Union, Mexico, and Canada, none of which prohibit companies from doing business in Cuba, initiated a World Trade Organization (WTO) claim, and they enacted or revised existing “blocking

\textsuperscript{166} Under Title IV, trafficking is defined slightly differently than under Title III. It occurs when a person knowingly and intentionally:

(i) transfers, distributes, dispenses, brokers or otherwise disposes of confiscated property,

(ii) purchases, receives, or obtains control of, or otherwise acquires confiscated property, or

(iii) improves . . . , invests in . . . , or begins after [the date of enactment of the Helms-Burton Act] to manage, lease, possess, use or hold an interest in confiscated property,

(iv) enters into a commercial arrangement using or otherwise benefiting from confiscated property, or

(v) causes, directs, participates in, or profits from, trafficking . . . by another person . . . without the authorization of any United States national who owns a claim to the property.


\textsuperscript{167} For purposes of Title IV, confiscated property is defined slightly more broadly than for Title III, as any property nationalized, expropriated, or seized by the Cuban government without compensation, whether before or after January 1, 1959. See id. § 6091(b)(1).

\textsuperscript{168} The same sanctions will apply to any alien who is a “corporate officer, principal, or shareholder with a controlling interest [in] an entity which has been involved in [such] trafficking,” as well as such person’s agent, spouse and minor children. Id. § 6091(a)(3)-(4).

\textsuperscript{169} The only notable exclusions have been of principals of “Sherritt International, a Canadian mining company, Grupo Domos, a Mexican telecommunications firm, and Grupo B.M., an Israeli citrus company.” CLARK \& WANG, supra note 56, at 16. Several other companies were reportedly sent “warning” letters to cease trafficking. See, e.g., Paolo Spadoni, The Impact of the Helms-Burton Legislation on Foreign Investment in Cuba, 11 CUBA TRANSITION 18, 28–29 (2001), available at http://lanic.utexas.edu/project/asce/pdfs/volume11/spadoni.pdf (last visited Feb. 10, 2010) (reporting that the U.S. had excluded the executives of three companies and maintained pressure on others by sending warning letters); Firms Told of Visa Denial Under U.S.-Cuba Law, CUBANET.ORG, July 10, 1996, http://www.cubanet.org/CNews/96/jul96/11e2.html (quoting White House spokesperson Nicholas Burns’ statement that letters had been sent to a “handful” of firms).

\textsuperscript{170} For a good introduction to international reactions to the Helms-Burton Act, see ROY, supra note 157.
statutes” that prevent their companies from complying with the Helms-Burton Act. The United States eventually reached a compromise with its trading partners: they withdrew their objections and the U.S. President pledged to suspend the application of the private right of action provision (Title III) and not to enforce the exclusion provision (Title IV) against companies incorporated in those countries.

c. The Trade Sanctions Reform and Export Enhancement Act

In 2000, Congress relaxed trade sanctions on agricultural and medical exports with the passage of the Trade Sanctions Reform and Export Enhancement Act of 2000 (TSREAA). Some of the restrictions relating to sale of agricultural products to Cuba were tightened again in 2004 as a result of a Treasury Department interpretation of “payment of cash in advance.” That interpretation was in turn reversed in 2009, a change expected to increase U.S. agricultural exports to Cuba.

3. State Measures

Some measures have been enacted at the state level to restrict commerce with Cuba. For example, in an effort to discourage travel to Cuba, the Florida Legislature approved the Sellers of Travel Act in 2008, which would have imposed “new fees and performance bond requirements on travel agencies that sell trips to Cuba” and other countries listed by the State Department as SSTs. The Sellers of

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171. The blocking statutes also prevent compliance with the ISA.
173. There has been meager enforcement of Title IV with only a handful of companies—STET, Grupo Domos, BM Group—receiving letters. The Helms-Burton Act also codified the existing economic embargo of Cuba in § 102(h), which had previously been implemented by OFAC, so that the President cannot lift it without making a determination according to § 205 that a transition government in Cuba is in power and consulting with Congress in accordance with § 102(h). Some discretion to modify the embargo was left with the Executive Branch, and OFAC has continued to issue licenses and implement changes as needed.
Travel Act was characterized as a consumer protection initiative and a homeland security measure, but it never took effect. All three of the Sanctioned Countries—Iran, Sudan, and Cuba—are subject to extensive U.S. sanctions. U.S. companies may not do business in any of the Sanctioned Countries. Iran and Sudan are U.S. foreign policy priorities. Cuba, although not as newsworthy in terms of terrorism, is the subject of longstanding U.S. sanctions that frequently conflict with other countries’ tolerance, if not encouragement, of business there. But what about foreign companies that are permitted by their home country law to do business in or with the Sanctioned Countries? Do foreign companies have to disclose those operations in order to operate in the United States or to access the U.S. capital markets?

III. The Demand for Information and Securities Laws: Who Does Business Where?

A. The Demand for Information

The scope of the U.S. sanctions regimes and the pressure on institutional investors to divest from companies doing business in the Sanctioned Countries has increased the demand for information about the activities of foreign companies and foreign affiliates of U.S. companies. Both large institutional investors (for example, CalPERS) and individuals want to know where the companies they invest in are doing business.

For their part, large multinational companies with activities and shareholders in multiple jurisdictions may resist providing different

177. Representative David Rivera proposed the measure as a homeland security initiative because it targets Florida-based agencies that sold trips to the countries on the State Department’s list, stating that “[n]ow more than ever Florida must protect our consumers.” Laura Figueroa, Federal Ruling Offers New Hope for Cuba-Trip Travel Agents, MIAMI HERALD, Mar. 22, 2009, at B3.


179. As Richard Newcomb, Director of OFAC from 1987–2004, expresses it, “Shareholders, regulators, corporate officers, directors, pension fund managers, politicians, and the public at large are becoming sensitized and aware more and more of how corporate decisions about who, where, and how they do business may affect their lives and the lives of others.” Newcomb, supra note 48, at 52.
types and amounts of information to an international alphabet soup of
regulators. Given the unilateral nature of many U.S. sanctions pro-
grams, some non-U.S. companies may lawfully do business in and with
the Sanctioned Countries while U.S. companies may not. What hap-
pens when the non-U.S. company sells stock in the United States?
Must it disclose any activity in or with a Sanctioned Country?

As discussed below, if the business activities in the Sanctioned
Country are financially substantial in comparison to the size of the
company, then disclosure of operations in the Sanctioned Country is
clearly required. The more difficult question arises when the opera-
tions in the Sanctioned Countries are economically slight in compari-
son with the size of the company. Does the fact that such business
could be prohibited if the company were organized under U.S. law
mean that it must be disclosed? Does an extensive U.S. sanctions re-
gime have a policy implication that makes the information about oper-
ations in or with a Sanctioned Country something that investors
necessarily need or want? To think about that question, it is first
necessary to think about the purpose of U.S. securities laws and the
disclosure that they require.

B. The U.S. System of Securities Regulation Is Based on Disclosure

The U.S. system of securities regulation is based on the assumption
that information is the key to preventing fraud and ensuring sound
investment decisions. The Securities Act of 1933 and the Securities
Exchange Act of 1934 were both passed in the wake of the 1929
stock market crash, which was attributed in part to the large number
of fraudulently floated securities that were sold to the public by un-
scrupulous promoters. The Securities Act of 1933, in fact, became
known as the Truth in Securities Act.

The emphasis on the disclosure of information in the securities laws
is often traced to the well-known words of Louis Brandeis: “Sunlight
is said to be the best of disinfectants; electric light the most efficient
policeman.” Brandeis' words had a strong influence on Felix

180. See infra Part III.B (discussing Regulation S-K requirements).
181. If so, is it because of the U.S. sanctions, or is it because of the underlying risky situation
that gave rise to the U.S. sanctions? Is there a difference?
183. Id. §§ 78a–78nn.
(1966).
186. LOUIS D. BRANDEIS, OTHER PEOPLE'S MONEY AND HOW THE BANKERS USE IT 92
(1914).
Frankfurter who wrote, as he was working to get the laws passed, \textsuperscript{187} “The Securities Act is strong insofar as publicity is potent; it is weak insofar as publicity is not enough.” \textsuperscript{188} In general, the purpose of disclosure is to provide investors with all of the information they need in order to make informed investment decisions. \textsuperscript{189} 

The U.S. system of federal securities regulation requires that adequate information be provided to investors, but it does not regulate the particular type or soundness of the investments themselves. \textsuperscript{190} Federal securities regulation is disclosure-based, not “merit-based,” \textsuperscript{191} like some regulations imposed by state “blue sky” \textsuperscript{192} securities laws. \textsuperscript{193} 

Over the years, the federal disclosure regime has been strengthened. \textsuperscript{194} In particular, after the Enron and WorldCom scandals, Con-
gess passed the Sarbanes-Oxley Act, which dramatically heightened federal disclosure and compliance requirements for public companies.

Companies that sell securities to the public are required to provide substantial amounts of information about their operations and prospects. The companies subject to these disclosure requirements (so-called reporting companies or public companies) include companies that have listed securities on a U.S. exchange, companies involved in interstate commerce that have at least 500 shareholders and $10 million in assets, and companies that have engaged in a registered public offering in the United States. The regulations require disclosure of specified information about the companies in the registration statement upon the initial issuance of securities, periodically thereafter, and whenever there is an extraordinary corporate event.


196. See HAZEN, supra note 184, § 1.2(3)(D)(3).
198. For purposes of this Article, a company that sells securities to the public is the same as a reporting company. This category also includes a number of non-U.S. companies that sell securities in the United States and that the SEC classifies as "foreign private issuers."
200. See id. § 78l(g)(1).
201. See id. § 78o(d).
202. See 15 U.S.C. §§ 77e–77g, 77j, 77aa (2006). The registration process for issuing securities to the public includes the production of a prospectus and a registration statement using, for example, Form S-1 or Form S-3 or, in the case of non-U.S. issuers, Form F-1 or Form F-3 in order to provide investors with the information they need in order to make an informed decision about purchasing the securities.
203. See 15 U.S.C. §§ 78l(b)(1), 78l(g)(1), 78m, 78o(d). This includes filing annual (for example, Form 10-K, or in the case of non-U.S. issuers, Form 20-F) and quarterly (Form 10-Q) reports.
204. See 15 U.S.C. § 78n(a), (d), (f) (2006). This includes filing Form 8-K reports (or in the case of a non-U.S. issuer, Form 6-K). The list of events that will trigger such a "current report" filing was extended substantially by the Sarbanes-Oxley Act of 2002. Disclosure is also required
WHAT'S IN YOUR PORTFOLIO?

The specific information that must be included in the filings has been defined by the SEC over time. The SEC has made a number of ex ante decisions about what information is important to investors, and it promulgated Regulation S-K\textsuperscript{205} to provide instructions to reporting companies.\textsuperscript{206} Part of the integrated disclosure system,\textsuperscript{207} Regulation S-K removes much of the issuer’s (and its counsel’s) discretion about what to include in filings.\textsuperscript{208}

Regulation S-K specifies a number of categories of information that must be disclosed: information about the company’s business,\textsuperscript{209} the company’s securities,\textsuperscript{210} the company’s financial data,\textsuperscript{211} the company’s management and certain security holders,\textsuperscript{212} and other information from the registration statement and prospectus.\textsuperscript{213} Importantly, for the purposes of this Article, companies must disclose the items listed in Regulation S-K whether or not the information is believed to be important to investors in any particular instance. The SEC has determined that investors will find the required information relevant most of the time, and the consistent disclosure obligations make it possible to compare firms.\textsuperscript{214}

In light of the foregoing, why is there any uncertainty about whether a public company must disclose its activities in or with the Sanctioned Countries? As currently drafted, the U.S. federal securities laws and regulations, including Regulation S-K, do not impose a specific disclosure requirement that addresses business in or with a country against which the United States has imposed sanctions, even if the sanctions have been imposed because the country has been identified as an SST. Certain general instructions in Regulation S-K suggest, however, that such information must be disclosed.

\textsuperscript{206} The SEC also promulgated Regulation S-X in order to provide instructions about quantitative disclosures. See 17 C.F.R. pt. 210 (2009).
\textsuperscript{208} See Stephen J. Choi & A.C. Pritchard, Securities Regulation: Cases and Analysis 45 (2d ed. 2008).
\textsuperscript{209} See 17 C.F.R. §§ 229.101–229.103.
\textsuperscript{210} See id. §§ 229.201–229.202.
\textsuperscript{211} See id. §§ 229.301–229.308T.
\textsuperscript{212} See id. §§ 229.401–229.407.
\textsuperscript{213} See id. §§ 229.501–229.512.
\textsuperscript{214} Choi & Pritchard, supra note 208, at 45.
Specifically, Item 101 (Description of Business) requires a general description of the business of the company,\(^{215}\) including, "[t]o the extent material to an understanding of the registrant's business taken as a whole,"\(^{216}\) information about where a company does business, the principal markets for the company's products,\(^{217}\) and the sources of the raw materials used by the company.\(^{218}\) Item 101 also instructs companies to describe "any risks attendant to [their] foreign operations."\(^{219}\)

Item 103 of Regulation S-K (Legal Proceedings) requires disclosure of "any material pending legal proceedings... to which the registrant or any of its subsidiaries is a party," including any such proceeding "known to be contemplated by governmental authorities" and not routine or incidental to the company's business.\(^{220}\)

Item 303 (Management's Discussion and Analysis of Financial Condition and Results of Operations) requires a broader discussion of the company's operations from the management's perspective. Item 303(a) thus requires the company to disclose "currently known trends, events, and uncertainties that are reasonably expected to have material effects" on results of the company's operations or to cause a material increase or decrease in the company's liquidity or capital resources.\(^{221}\) For example, if substantial numbers of investors ceased purchasing or divested themselves of the securities of a company because of its operations in or with a Sanctioned Country, the investors' actions could have a "foreseeable material impact on the company's ability to raise cash through the sale of its securities," and the company would be required to disclose those material effects.\(^{222}\) The instructions to Item 303(a) further clarify that "[f]oreign private registrants also shall disclose briefly any governmental economic, fiscal, monetary, or political policies or factors that have materially af-

\(^{215}\) See 17 C.F.R. § 229.101(c).

\(^{216}\) Id. § 229.101(c)(1).

\(^{217}\) See id. § 229.101(c)(1)(i).

\(^{218}\) See id. § 229.101(c)(1)(iii).

\(^{219}\) Id. § 229.101(d)(3).

\(^{220}\) Id. § 229.103.

\(^{221}\) Concept Release on Management's Discussion and Analysis of Financial Condition and Operations, Exchange Act Release No. 33-6711, 52 Fed. Reg. 13,715, 13,717 (Apr. 24, 1987). Regulation S-K, Item 303(a)(1), for example, instructs companies to "[i]dentify any known trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way." 17 C.F.R. § 229.303(a)(1) (2009).

\(^{222}\) Memorandum from David B.H. Martin, Dir., Div. of Corp. Fin., SEC, to Laura Unger, Acting Chair, SEC, 1278 PLI/Corp 1125, at *1127 (May 8, 2001) [hereinafter Martin Memorandum]; see also infra Part IV.B (discussing Director Martin's analysis in more detail).
fected or could materially affect, directly or indirectly, their operations or investments by United States nationals."\(^{223}\)

Finally, a company selling securities to the public in the United States is required by Item 503(c) to disclose risk factors that may affect the issuer of the securities being offered. Certainly the political instability in the Sanctioned Countries and the imposition of U.S. sanctions could be significant enough to require disclosure.\(^{224}\) In fact, the term “global security risk” has been coined to describe the risk to companies from their operations in SSTs.\(^{225}\)

Even if information about business in or with a Sanctioned Country is not required to be disclosed under Regulation S-K, Exchange Act Rule 12b-20 functions as a catch-all rule, providing that “[i]n addition to the information expressly required to be included in a statement or report, there shall be added such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made not misleading.”\(^{226}\)

The inclusive anti-fraud provision of the Exchange Act, Rule 10b-5 (Employment of Manipulative and Deceptive Practices), also regulates the information that a company must disclose about its activities in the Sanctioned Countries because it creates liability not only for making “any untrue statement of material fact” but also for omitting “a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading” in connection with the purchase or sale of a security.\(^{227}\)

C. Materiality

The key to these disclosure obligations is whether the information is “material.”\(^{228}\) Unless the information is expressly required without qualification in Regulation S-K (for example, the year the company

\(^{223}\) 17 C.F.R. § 229.303(a) (Instruction 11).


\(^{225}\) See Foreign Policy Hearing, supra note 3, at 53–54 (statement of Roger Robinson, Jr., President and Chief Executive Officer, Conflict Securities Advisory Group).

\(^{226}\) 17 C.F.R. § 12b-20 (2009). Rule 408 of the Securities Act has virtually identical wording except that it applies to registration statements instead of statements and reports.

\(^{227}\) Id. § 240.10b-5(b).

\(^{228}\) Jeffrey A. Smith, Disclosure of Climate Change Risks and Opportunities, 41 REV. SEC. & COMMODITIES REG., Jan. 2, 2008, at 1, 4. It is important to remember, however, that although materiality is a key concept with respect to securities law disclosure, not all material information has to be disclosed. Similarly, with respect to liability, nondisclosure of material information “will not give rise to liability under Rule 10b-5 unless the defendant had an affirmative duty to disclose that information.” Oran v. Stafford, 226 F.3d 275, 285 (3d Cir. 2000).
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was organized\textsuperscript{229} or the existence of transactions worth more than $120,000 between the company and family members of the directors\textsuperscript{230}, the information must only be disclosed if it is material. As a practical matter, whether and exactly what a company discloses usually depends on the company's and its attorneys' materiality determination.

The Supreme Court provided the definitive definition of materiality in 1976 in \textit{TSC Industries, Inc. v. Northway, Inc.}\textsuperscript{231} When analyzing a proxy statement issued in National Industries' proposed acquisition of TSC Industries, the Court found that information is material if there is a "substantial likelihood that the disclosure . . . would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."\textsuperscript{232} Over a decade later, in \textit{Basic, Inc. v. Levinson}, the \textit{TSC Industries} standard was expressly adopted in the antifraud context. The \textit{Basic} Court considered the defendant's public statements denying merger negotiations that were, in fact, ongoing.\textsuperscript{233} The Court held that the materiality of information about future events may be determined by balancing the probability that the event will occur with the expected magnitude of the event.\textsuperscript{234}

Since the announcement of the materiality test by the Court, there has been pressure on the SEC to eliminate the uncertainty inherent in the test and to develop a more objective, bright line rule.\textsuperscript{235} In 1999, the SEC provided some clarification of the concept in SEC Staff Accounting Bulletin No. 99 (the "1999 SAB"), which explained, "A matter is 'material' if there is a substantial likelihood that a reasonable person would consider it important."\textsuperscript{236} The 1999 SAB explicitly confronting the issue of whether an objective test for materiality, in the form of a numerical threshold, was desirable, and it found that such a test was useful as a preliminary step but not dispositive: "quantifying,

\begin{itemize}
  \item \textsuperscript{229} See 17 C.F.R. § 229.101(a)(1) (2009).
  \item \textsuperscript{230} See id. § 229.404(a).
  \item \textsuperscript{231} TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438 (1976).
  \item \textsuperscript{232} Id. at 449.
  \item \textsuperscript{233} Basic, Inc. v. Levinson, 485 U.S. 224 (1988) (concerning a Rule 10b-5 claim).
  \item \textsuperscript{234} See id. at 249–50.
  \item \textsuperscript{235} The \textit{Basic v. Levinson} Court specifically considered a Third Circuit test that offered a bright line rule but rejected it: "[E]ase of application alone is not an excuse for ignoring the purposes of the Securities Acts and Congress's policy decisions." \textit{Id.} at 236.
  \item \textsuperscript{236} SEC Staff Accounting Bulletin No. 99, 64 Fed. Reg. 45,150, 45,151–52 (Aug. 19, 1999) ("Qualitative factors may cause misstatements of quantitatively small amounts to be material."). Although Staff Accounting Bulletin No. 99 did not carry the force of law, courts have relied on it as constituting "a body of experience and informed judgment" and "persuasive guidance." \textit{Ganino v. Citizens Utils. Co.}, 228 F.3d 154, 163 (2d Cir. 2000) (quoting \textit{Skidmore v. Swift & Co.}, 323 U.S. 134 (1944), and explicitly rejecting the use of numerical benchmarks for assessing materiality).\end{itemize}
in percentage terms, the magnitude of a misstatement is only the beginning of an analysis of materiality; it cannot appropriately be used as a substitute for a full analysis of all relevant considerations."\textsuperscript{237} The instructions to Item 101 of Regulation S-K also specify that in determining materiality for purposes of the description of a business, a company should take both quantitative and qualitative factors into account: "Situations may arise when information should be disclosed about a segment, although the information in quantitative terms may not appear significant to the registrant's business taken as a whole."\textsuperscript{238}

Obviously, a reasonable investor would want to know about a company's principal lines of business and the prospects and risks associated with such business. In arguing that their operations or investments in the Sanctioned Countries are not material, and therefore need not be disclosed, companies have often urged that their business in the Sanctioned Countries is a miniscule part of their global operations. For example, in correspondence with the SEC, General Electric compared the sales made to customers in Iran with its total consolidated revenues in 2003, 2004, and 2005, and it found that the Iranian sales represented only 0.33\%, 0.19\%, and 0.15\% of its total revenues during each of those respective years.\textsuperscript{239} BASF argued that less than 0.2\% of its total sales in 2004 were to customers in Iran,\textsuperscript{240} and that sales of dual-use products to Iran represented less than 0.01\% of BASF's worldwide consolidated sales in 2004.\textsuperscript{241}

There are obvious concerns with such claims. How credible is the corporate accounting for business that is not disclosed? How is long-term damage to a firm's reputation, especially in the case of war or a terrorist attack, monetized? Why, if the activity is so marginally rewarding as to be of no importance to the firm's putative business own-

\textsuperscript{237} SEC Staff Accounting Bulletin No. 99, 64 Fed. Reg. at 45,151.

\textsuperscript{238} 17 C.F.R. § 229.102 (2009) (Instruction 1 to Item 101).


\textsuperscript{241} BASF Corp., Registration Statement (Form 20-F), at 12 (Mar. 14, 2007), http://www.sec.gov/Archives/edgar/data/1024148/00010465907018854/a07-6595_120f.htm (last visited Feb. 10, 2010). This disclosure was made after several rounds of correspondence with the Office of Global Security Risk (OGSR). Six months later, on September 6, 2007, BASF delisted.
ers, does the firm's management persist in that line of business? Bracketing such questions, the narrow securities law question is whether some information that is neither expressly required by Regulation S-K or otherwise nor directly significant to the firm's bottom line is nonetheless sufficiently material to require disclosure.242

D. Materiality Per Se, Evolving Standards, and the Debate about Social Disclosure

Some kinds of information about a company must be disclosed regardless of the percentage of overall company revenue that the activity represents. Some kinds of information will always be material to investors. As discussed above, much of that information is specified in Regulation S-K.

But the materiality standard is also adaptable.243 As global markets and investor priorities evolve over time, the materiality standard ensures that information important to investors continues to be disclosed. If combating terrorism is a priority for the United States, then it may be material to potential U.S. investors that the money they pay for shares in a company may be used to fund operations in a country that sponsors terrorism. Investors may need information about those operations in order to make an informed investment decision.

The adaptability of the materiality standard not only applies to the information being disclosed but also, some argue, to the reason for the disclosure. As Louis Loss explained in 1969, given the fact that "appropriate publicity tends to deter questionable practices and to elevate standards of business conduct,"244 Congress or the SEC may expand the disclosure mechanism beyond the principal purpose of informing investor trading in order to address business ethics and corporate responsibilities. In fact, this expanded use of securities regulation has already been achieved in some contexts. The securities laws have incorporated requirements for disclosure of, for example, climate change risks and opportunities.245

242. If institutional investors represent a significant percentage of investors and many of them are prohibited from investing in SSTs, then the SST operations are material operations and should be disclosed to enable those investors to make informed investment decisions.

243. One investor's flexibility is another's uncertainty, though, and there is often a need for a clearer standard.


The materiality standard could in theory be read to require broad disclosure requirements, including disclosures that serve public interest purposes. Such so-called social disclosure was analyzed by Cynthia Williams in her 1999 *Harvard Law Review* article entitled *The Securities and Exchange Commission and Corporate Social Transparency.*

Williams defined “social disclosure” to include information about the countries in which a company does business and argued that, in the context of proxy solicitations, the SEC has the power to compel expanded social disclosure in the public interest. Professor Williams analyzed the materiality standard and the situations in which a social issue that is not financially material might be important to investors who would invest or divest on that basis, creating a financially material impact on the company. According to Professor Williams, “[T]oday’s social issue is tomorrow’s financial issue.”

IV. THE SEC, TERROR, AND SHIFTING STANDARDS OF MATERIALITY

A. The PetroChina Offering

A widely reported example of the conflict between the disclosure required by the U.S. securities laws and a company’s business operations in a Sanctioned Country was the PetroChina Company Limited offering. PetroChina was a wholly-owned subsidiary of the China National Petroleum Company (CNPC), and it was created for the purpose of attracting foreign capital through an initial public offering (IPO) in the U.S. markets.


246. Williams, supra note 187.

247. Id. at 1201 n.5.

248. See id. at 1204.

249. Id. at 1284. The academic conversation about using disclosure for policy or public interest purposes continued a few years later when the *Harvard Law Review* published a note that argued for a “mandate bounded by considerations of investor welfare and underpinned by the same economic logic that supports mandatory financial disclosure.” Note, *Should the SEC Expand Nonfinancial Disclosure Requirements?*, 115 HARV. L. REV. 1433, 1435 (2002).


There was considerable controversy surrounding the PetroChina offering because CNPC held a minority joint venture position in Sudan's Greater Nile Oil Project, which was accused of human rights abuses. Various anti-slavery, religious, and conservative national security groups, as well as the AFL-CIO and several members of Congress, therefore objected to the PetroChina offering.

The question was whether the proceeds from PetroChina's U.S. offering would be used by the parent company (CNPC) to fund operations in Sudan. CNPC promised to segregate the PetroChina offering funds and to create separate accounts for the IPO proceeds so that they would not be used for the Sudanese joint venture. Critics considered this a restructuring scheme that was designed to avoid U.S. sanctions on Sudan, and they charged that CNPC created PetroChina to access the U.S. capital markets while protecting itself from negative public reaction to its operations in Sudan.

There was no legal prohibition, however, on offering the PetroChina shares to U.S. investors. OFAC issued an opinion that the shares could be purchased without violating the U.S. sanctions in place against Sudan, as long as "there was no 'clear statement' that CNPC would use the proceeds to retire Sudan-related debt." Groups objecting to the offering had to content themselves with the fact that CNPC's involvement in Sudan was disclosed at all.

The IPO went forward in April 2000 with minimal disclosure of any connection between PetroChina and CNPC's Sudan activities and

252. Republican Spencer Bachus, Democrat Dennis Kucinich, and Socialist Bernard Sanders sent a letter to President Clinton that expressed concerns about the use of proceeds from the offering. See Letter from Congressman Spencer Bachus et al., to President William Jefferson Clinton (Mar. 31, 2000) (on file with the author).

253. A number of members of Congress expressed their concerns in a letter to President Clinton that, inter alia, PetroChina would use the IPO proceeds to support the CNPC joint venture in the Sudan. See id.

254. See Diamond, supra note 250, at 67.


258. In the “Industry Overview” section of the prospectus, PetroChina described the 1999 “restructuring” whereby CNPC incorporated PetroChina and transferred substantially all of its assets, liabilities, and interests in a number of businesses and operations in China. See PetroChina Co., Final Prospectus 74 (Mar. 27, 2000) (on file with the author). PetroChina specifically noted that CNPC retained the assets, liabilities, and interests relating to business in Sudan. See id. at 75.
the inclusion of a special "Use of Proceeds Verification" subsection in the "Business" section. The "Use of Proceeds Verification" subsection merely disclosed that PetroChina shares were listed in countries that may impose sanctions on certain other countries, including Sudan, where CNPC owned equity interests. The subsection then described the segregated accounts into which PetroChina and CNPC would deposit their proceeds from the offering, and the way in which funds would be disbursed from the accounts. The PetroChina U.S. IPO was somewhat disappointing, raising considerably less capital than CNPC had originally planned.

The PetroChina offering illustrates the problems with U.S. securities regulations then and now: the securities laws allowed an offering that arguably worked against stated U.S. foreign policy goals, and the offering went forward with inadequate disclosure of the controversial operations of PetroChina's controlling parent.

259. See id. at 119.

260. See id. The Form 20-Fs filed by PetroChina for fiscal years 2001, 2002, and 2003 made no mention of Sudan. When the company restructured in 2005, Sudan was mentioned because it and several other countries were "carved out" of the agreement in order to "give comfort to investors that their investments would not violate U.S. economic sanctions regulations." Letter from Li Huaqi, Sec'y to the Bd. of Dirs., PetroChina Co., to Cecilia D. Blye, Chief, Office of Global Sec. Risk, SEC 2 (June 19, 2007) (describing PetroChina's intent regarding its activities in Sudan and Iran). http://www.sec.gov/Archives/edgar/data/1108329/000114554907001074/filename1.txt; see PetroChina Co., Annual Report (Form 20-F) exhibit 4.3 (2005), http://www.sec.gov/Archives/edgar/data/1108329/000114554905001175/u99842exv4w3.txt (last visited Feb. 10, 2010). For a good discussion of PetroChina's understanding of what is significant to its investors and investors' perception of the Sudan activities of PetroChina's parent company (CNPC), see Letter from Li Huaqi, Sec'y to the Bd. of Dirs., PetroChina Co., to Cecilia D. Blye, Chief, Office of Global Sec. Risk, SEC 3 (Feb. 15, 2007), http://www.sec.gov/Archives/edgar/data/1108329/000114554907000265/filename1.txt (last visited Feb. 10, 2010) ("[I]nvestors understand that [the company] has no control over how dividends that it pays to its shareholders are ultimately used and will therefore not consider CNPC's activities in Sudan and other countries to have an impact on PetroChina's business reputation or share value.").


262. See Diamond, supra note 250, at 70 (stating that the offering was scaled back "from an initial goal of raising $10 billion to the final figure of $2.9 billion"). It is unclear whether the Use of Proceeds Verification mechanism was sufficient to enable investment by U.S. institutional investors with prohibitions on investment in Sudan. Uncertainty about that issue was probably not helpful to the offering. PetroChina issued additional shares as an IPO on the Shanghai Stock Exchange on November 5, 2007, and raised an additional US$8.9 billion. See Elaine Kurtenbach, After Surge, PetroChina Stumbles in New York, USA TODAY, Nov. 5, 2007, http://www.usatoday.com/money/economy/2007-11-04-1494307240_x.htm (last visited Feb. 10, 2010).

263. Arguably, investors did not have the information they needed in order to make informed investment decisions. In its first annual report in 2000, the U.S. Commission on International
B. The Unger Letter

On April 2, 2001, Congressman Frank Wolf wrote to Laura S. Unger, Acting Chairman of the SEC, expressing his concerns about the PetroChina offering and making ten recommendations for enhanced disclosure by foreign firms seeking access to the U.S. markets. Chairman Unger’s May 2001 response (the “Unger Letter”) outlined the SEC’s efforts with respect to Sudan and attached a detailed memorandum about the disclosure standards prepared by David Martin, Director of the SEC’s Division of Corporation Finance (the “Martin Memo”). The Unger Letter stated that the SEC staff “will attempt to review all registration statements filed by foreign companies which reflect material business dealings with governments of countries subject to U.S. economic sanctions administered by OFAC, or with persons or entities in those countries.”

Most strikingly, the Unger Letter proposed enhanced disclosure for foreign registrants doing business in sanctioned countries. Chairman Unger pointed out that foreign companies may do business in Sudan or other countries that are subject to OFAC sanctions, yet still list on U.S. securities exchanges and offer stock to investors on U.S. markets. She stated that the SEC does not have the statutory authority to deny such companies access to the U.S. markets on the basis of their involvement with a particular foreign country, such as Sudan. However, she pointed out that the SEC does have the “statutory au-
authority to require that U.S. investors receive adequate disclosure about where the proceeds of their securities investments are going and how they are being used.”

In the letter, Chairman Unger used language that closely tracked the definition of materiality that was articulated in *TSC Industries Inc. v. Northway, Inc.* and in the 1999 SAB stating that “the fact that a foreign company is doing material business with a country, government or entity on OFAC’s sanctions list is, in the SEC staff’s view, substantially likely to be significant to a reasonable investor’s decision about whether to invest in that company.” The implication was that such business is material per se and it must therefore be disclosed. The Martin Memo expanded on that position and reviewed the existing disclosure requirements (for example, of business operations, material risks, and pending litigation).

The Martin Memo concluded that “existing SEC disclosure requirements might very well warrant disclosure of a foreign company’s operations in, or business relationships with companies from, countries on . . . the U.S. State Department’s lists of sponsors of terrorism.” Director Martin reiterated that if there is no specific disclosure requirement relating to a company’s operations in, or its business relationships with companies from, the countries on the State Department’s lists, then “the question of whether disclosure [of operations in SSTs] is required will depend on the materiality of the financial impact of those operations and business relationships on the company’s conduct of its business.”

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270. *Id.* Chairman Unger reiterated that the federal securities laws are about disclosure and making sure that investors have “access to material information about the companies and securities in which they are considering investing.” *Id.*


274. *See supra* Part III.C, D (regarding the standard of materiality). Chairman Unger’s exact meaning was debated because she used the word “material” several times in her letter but did not explicitly write that such information is material per se.

275. *See supra* note 222.


277. *Id.* at 1128 (discussing Recommendation No. 1). Director Martin went on to write, In assessing materiality, the SEC staff takes the view that the reasonable investor generally focuses on matters that have affected, or will affect, a company’s profitability or financial outlook. Because securities are financial investment vehicles, the materiality of a foreign company’s operations in a particular country and its business relationships with companies from that country will generally depend on whether these operations or relationships have had, or are likely to have, a financial impact on the company. *Id.* at 1128–29.
The Martin Memo cited the materiality standard from *TSC Industries, Inc. v. Northway, Inc.* and stated, "We agree that a reasonable investor would likely consider it significant that a foreign company raising capital in the U.S. markets has business relationships with countries, governments or entities with which any U.S. company would be prohibited from dealing because of U.S. economic sanctions."279

Response to the Unger Letter was strong,280 most notably from industry groups such as the National Foreign Trade Council (NFTC), and the position did not survive the term of the next SEC Chairman, Harvey L. Pitt. In late September 2001, the NFTC President announced that he had been assured by Chairman Pitt that the SEC had no plans to require foreign companies with securities listed on U.S. stock exchanges to make additional disclosures about their business dealings in countries that were subject to U.S. sanctions.281

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278. See id. at 1128 (discussing Recommendation No. 1).
279. Id. at 1129. Martin continued,

The staff will, therefore, seek information from foreign registrants about their material business in countries on the OFAC’s sanctions list and their business relationships with countries, governments, or entities on those lists. This type of disclosure would make available to investors additional information about situations in which the proceeds of an offering could however indirectly benefit countries, governments, or entities that, as a matter of U.S. foreign policy, are off-limits to U.S. companies.

*Id.* Director Martin responded to Congressman Wolf’s recommendation that foreign companies disclose steps taken to identify and assess risk from doing business in or with SSTs. He pointed out that “[w]hen a foreign company initially registers its securities with the SEC, and thereafter in its annual disclosure on Form 20-F, [it] is required to prominently disclose risk factors that [might] make an investment in [its securities] speculative or high risk.” *Id.* at 1130; see SEC Form 20-F, Item 3.D. Such risk factors may include factors that relate to countries subject to OFAC sanctions where the company has material operations. *See Martin Memorandum, supra* note 222, at 1130 (discussing Recommendation No. 2). Director Martin explained,

If it is reasonably likely that U.S. governmental sanctions will be imposed on the company as a result of its operations in a particular country, this risk would need to be disclosed if the sanctions were likely to have a material impact on the company. Likewise, if it is reasonably likely that public opposition to the company would have a materially adverse effect on the operations of the company, this risk would also need to be disclosed.

*Id.* (introducing the concept of probability versus magnitude, which was also part of the materiality test articulated by Basic, Inc. v. Levinson, 485 U.S. 224 (1988)).


C. The SEC Office of Global Security Risk

Thinking about the relationships between financial markets and securities issues shifted in the wake of September 11th and the accounting scandals that led not only to the passage of the Sarbanes-Oxley Act but also to the ouster of Chairman Pitt from the SEC. In 2004, Congress directed the SEC to establish the Office of Global Security Risk (OGSR). Part of the Division of Corporation Finance, the OGSR’s role is to increase “the investing public’s access to the information it needs about any public company to make an informed investment decision, including material information about global security risk.”

At the time it was established, the mandate of the OGSR was to “ensure that companies listed on U.S. exchanges disclose whether they are doing business in states designated by the State Department as sponsoring terrorism.” The OGSR was tasked with establishing a process by which the SEC can identify all companies traded on U.S. exchanges that are operating in states designated as State Sponsors of Terrorism [and] ensuring that all companies traded on U.S. exchanges that are operating in states designated as State Sponsors of Terrorism are disclosing those activities to investors.


[T]o identify companies whose activities raise concern about global security risks that are material to investors; to obtain appropriate disclosure where merited; and to share information as necessary and appropriate with other key government agencies responsible for tracking terrorist financing.


The Office of Global Security Risk will focus on asymmetric risk by assisting review staff in giving consideration to whether U.S. or foreign companies that are registered with the SEC have operations or other exposure with or in areas of the world that may subject it and its investors to material risks, trends or uncertainties. This consideration would include whether a company has operations in a country or area of activity where political, economic or other risks exist that are material, or whether a company faces public or government opposition, boycotts, litigation, or similar circumstances that are
The House Committee Report that instructed the SEC to establish the OGSR noted its concern that “American investors may be unwittingly investing in companies with ties to countries that sponsor terrorism and countries linked to human rights violations.” The Committee went on to say, “[A] company’s association with sponsors of terrorism and human rights abuses, no matter how large or small, can have a material adverse effect on a public company’s operations, financial condition, earnings, and stock prices, all of which can negatively affect the value of an investment.”

D. The Pension Fund Letters

In June 2005, representatives of fifty public employee retirement systems, under strong pressure to divest from companies doing business in Sudan, wrote to the SEC and the Departments of State, Treasury, and Commerce and asked for “assistance in identifying any publicly traded companies that are of concern to the United States government for doing business with, or having business ties to, entities that support terrorism or threaten U.S. humanitarian goals” (the “June 3 Letter”). Investors objected to pension fund investments in companies doing business in countries that were subject to U.S. sanctions for a variety of interconnected reasons: moral outrage, low tolerance for the risk to the company's share value from business in such countries, concern about bad publicity, and the impact on the company's reputation. Some states had required divestment, and the pen-

reasonably likely to have a material adverse impact on a company's financial condition or results of operations.

Id.

285. H.R. REP. NO. 108-221, at 151 (2003). The House Report specified, The duties of this office shall include, but not be limited to: (1) establishing a process by which the SEC identifies all companies on U.S. exchanges operating in State Department designated terrorist-sponsoring states; (2) ensuring that all companies sold on U.S. exchanges operating in State Department-designated terrorist-sponsoring states are disclosing such activities to investors; (3) implementing enhanced disclosure requirements based on the asymmetric nature of the risk to corporate share value and reputation stemming from business interests in these higher risk countries; (4) coordinating with other government agencies to ensure the sharing of relevant information across the Federal government; and (5) initiating a global dialogue to ensure that foreign corporations whose shares are traded in the United States are properly disclosing their activities in State Department-designated terrorist-sponsoring states to American investors.

Id.

286. Id.

sion funds could not determine from available disclosure which companies conducted the problematic activities.

In the June 3 Letter, the pension funds stated that they needed information about these entities to "ensure that [they were] not inadvertently acting in conflict with the foreign policy and humanitarian goals of the United States, thereby subjecting [their] members to excessive investment risk." The pension funds pointed out that "existing laws require your agencies to identify, monitor and sanction companies with business or financial ties to terrorist sponsoring countries," and they specifically referred to the SEC's mandate from Congress to establish a process to identify such companies and to ensure that their activities are disclosed to investors. The pension funds complained, "At this time, no comprehensive list or report of such companies has been created."

Three days later, officials from national organizations representing state auditors, state retirement administrators, public employee retirement systems, state legislatures, and teacher retirement funds wrote to the same four agencies (the "June 6 Letter"), both to express support for the public pension fund position in the June 3 Letter and to press for public disclosure by the four agencies of the "identity of companies that, by virtue of their business or business ties in terrorist sponsoring countries, are acting contrary to U.S. foreign policy and humanitarian interests." The June 6 Letter described a meeting that the organizations and the OGSR had held earlier in the year, and the OGSR's decision, at that time, not to disclose its correspondence or its findings to the public. The June 6 Letter urged the SEC and the other agencies to "[m]andate readily accessible disclosures" and to "[p]rovide a searchable, publicly available database . . . of publicly held companies with material business or operations in nations classified as supporting terrorism or subject to sanctions."

In short, by 2005, many U.S. institutional investors were concerned about inadvertently investing in companies doing business in sanc-
tioned countries, and by extension, they were concerned about the adequacy of U.S. securities disclosure requirements.

E. Getting Disclosure and Making it Available

1. A Slow Start for the OGSR

Between 2005 and 2007, the OGSR sent numerous letters to reporting companies asking whether they were doing business in or with SSTs. Nevertheless, the OGSR was perceived as having gotten off to a slow start. In a 2007 letter to SEC Chairman Christopher Cox, Senator Chris Dodd, who was then the Senate Banking Committee Chairman, wrote,

I understand that the SEC’s efforts have long been underway to outfit the Office of Global Security Risk fully with adequate staff and resources. But I remain concerned about the pace at which such efforts have been pursued. It is critically important that the intent of Congress be fully followed as soon as possible, particularly given the importance of this office’s missions to promoting human rights, U.S. security interests, and investor knowledge.294

Senator Dodd also noted the national security implications of “American investors unknowingly promoting terrorist states through certain key investments,” and he stated, “I remain particularly concerned about the ability of shareholders to access reliable information regarding publicly traded companies’ business transactions involving Iran and Sudan.”295

In response to “the urging of certain members of Congress to expand the role of the OGSR and certain officials and investors to make existing disclosure of business in or with State Sponsors of Terrorism easier to find,”296 SEC Chairman Christopher Cox agreed,

No investor should ever have to wonder whether his or her investments or retirement savings are indirectly subsidizing a terrorist haven or genocidal state. The law already requires companies to report on any material activities in a country the Secretary of State

294. Letter from Sen. Chris Dodd, Chairman, Senate Comm. on Banking, Hous. & Urban Dev., to Christopher Cox, Chairman, SEC (May 31, 2007), http://dodd.senate.gov/?q=node/3923 (last visited Feb. 10, 2010); see Dodd Urges SEC to Ensure Disclosure About Firms in States Sponsoring Terrorism, 39 Sec. Reg. & L. Rep. (BNA) 874, 875 (June. 4, 2007) (quoting Senator Dodd as “concerned about the pace at which such efforts [to get the OGSR equipped with staff and resources] have been pursued”).


296. SULLIVAN & CROMWELL LLP, supra note 284, at 3.
has formally designated a State Sponsor of Terrorism. Our role is to make that information readily accessible to the investing public.\textsuperscript{297}

2. The Web Tool

On June 25, 2007, the SEC introduced a web tool, called Software Tool for Investors Seeking Information on Companies’ Activities in Countries Known to Sponsor Terrorism (the “Web Tool”), that facilitated investors’ ability\textsuperscript{298} to search documents that are filed by issuers for references to activity in sanctioned countries.\textsuperscript{299} All of the information was already available using the SEC’s Electronic Data Gathering Analysis and Retrieval system (EDGAR), but the Web Tool made it easier to find information that companies had disclosed about activities in, for example, the Sanctioned Countries. The database was organized by country (SST) and provided direct links to specific companies’ EDGAR disclosures.\textsuperscript{300} The Web Tool did not change the definition of what had to be disclosed. The Web Tool merely made any information disclosed by the issuer more accessible to investors.

As soon as it was online, the Web Tool was inundated by hits. Chairman Christopher Cox reported that “[b]etween June 25, when the web tool was unveiled, through July 16, visitors have ‘hit’ material posted on the site well over 150,000 times. Iran was the country most frequently clicked on, followed by Cuba, Sudan, North Korea, and Syria.”\textsuperscript{301} The Web Tool was widely criticized by public companies, securities industry professionals, some members of Congress,\textsuperscript{302} and even one of the SEC Commissioners.\textsuperscript{303} Many reporting companies

\textsuperscript{298} The web tool was located in the, “Investor Information” section of the SEC website. See id.
\textsuperscript{299} See id.
\textsuperscript{302} Congressman Barney Frank, Chairman of the House Financial Services Committee, wrote to Chairman Christopher Cox of the SEC on July 12, 2007: “I hope you will give serious consideration to deeming either a more rigorous, materiality-based methodology for developing the list you are presenting to investors or else eliminating the webpage entirely.” Press Release, House Comm. on Fin. Servs., Frank Letter to Cox Regarding SEC List of Terrorist-Financing States (July 13, 2007), http://www.house.gov/apps/list/press/financialsvcs_dem/press071307.shtml (last visited Feb. 10, 2010).
opposed the database as a "blacklist" because simply being listed in a part of the SEC website identified with SSTs was prejudicial to them. In almost all cases, the activity described was lawful under applicable usually non-U.S. law. In some cases (for example, Western Union) the activity was explicitly licensed by OFAC. The Web Tool was criticized as over-inclusive because "it captured (and potentially stigmatized) any issuer that disclosed even benign activities in [an SST]," and as under-inclusive because it only included issuers' 2006 annual reports (Form 10-K or Form 20-F) and not disclosure made after those reports.\textsuperscript{304}

3. The Concept Release

The SEC suspended the Web Tool on July 25, 2007.\textsuperscript{305} On November 16, 2007, the SEC solicited comments on the Web Tool and the disclosure of business in SSTs in the Concept Release on Mechanisms to Access Disclosures Relating to Business Activities in or with Countries Designated as State Sponsors of Terrorism (the "Concept Release").\textsuperscript{306} The Concept Release articulated the SEC's understanding of the disclosure requirements with respect to business activities in or with SSTs:

The federal securities laws do not impose a specific disclosure requirement that addresses business activities in or with a country based upon its designation as a State Sponsor of Terrorism. However, the federal securities laws do require disclosure of business activities in or with a State Sponsor of Terrorism if this constitutes material information that is necessary to make a company's statements, in the light of the circumstances under which they are made, not misleading.\textsuperscript{307}

In addition, the Concept Release briefly summarized what the SEC understands as the general definition of materiality: "[T]he Supreme Court has determined information to be material if there is a substantial likelihood that a reasonable investor would consider the information important in making an investment decision or if the information would significantly alter the total mix of available information."\textsuperscript{308}

\begin{itemize}
\item \textsuperscript{304} Sullivan & Cromwell LLP, supra note 284, at 3.
\item \textsuperscript{305} See Press Release, supra note 301.
\item \textsuperscript{306} Concept Release on Mechanisms to Access Disclosures Relating to Business Activities in or with Countries Designated as State Sponsors of Terrorism, SEC Release Nos. 33-8860, 34-56803 (Nov. 16, 2007), 72 Fed. Reg. 65,862 (Nov. 23, 2007) [hereinafter Concept Release].
\item \textsuperscript{307} Id. at 65,863 (citing Rule 408 and Rule 12b-20).
\item \textsuperscript{308} Id. at 65,863 (citing Basic, Inc. v. Levinson, 485 U.S. 224 (1988); TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976)).
\end{itemize}
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With respect to the possibility that a different standard might be applicable to activities in the SSTs, the SEC clarified,

The materiality standard applicable to a company's activities in or with State Sponsors of Terrorism is the same materiality standard applicable to all other corporate activities. Any such material information not covered by a specific rule or regulation must be disclosed if necessary to make the required statements, in the light of the circumstances under which they are made, not misleading. The materiality standard's extensive regulatory and judicial history helps companies and their counsel to interpret and apply it consistently, and we remain committed to employing this standard to company disclosure regarding business activities in or with State Sponsors of Terrorism.309

Moreover, the Concept Release asked whether the SEC should continue to interpret materiality in the context of SSTs in the same way it does when reviewing disclosure related to other corporate activities that are not covered by a specific rule or regulation.310

The SEC received comment letters ranging from twenty-page memoranda from international financial institutions to handwritten notes from individuals. Many comments were about how the Web Tool worked. Of the twenty-eight comment letters received, just over half were critical of the Web Tool.311 In response to the question about whether the SEC had properly described materiality, about a third of the letters312 either assumed that materiality in the context of SSTs was the same as in other contexts313 or explicitly supported making no

309. Id.
310. See id. The SEC also asked whether information about companies' activities in or with SSTs was important to investors in making investment decisions. See id.
311. There is always, of course, considerable self-selection in submitting SEC concept release comment letters.
313. Several letters took the existing standard for granted. See Letter from Sepideh Behram, Senior Compliance Counsel, Ctr. for Regulatory Compliance, Am. Bankers Ass'n, to Nancy M. Morris, Sec'y, SEC 2 (Jan. 22, 2008) (on file with author); Christopher L. White, Executive Vice President, Gen. Counsel & Assistant Sec'y, AdvaMed, to Nancy M. Morris, Sec'y, SEC 3 (Jan. 18, 2008) (on file with author); Letter from Dr. Werner Schnappauf, Dir. & Gen. Member of the Presidential Bd., Bundesverband der Deutschen Industrie e.V., to Nancy M. Morris, Sec'y, SEC 2 (Jan. 21, 2008) (on file with author).
changes to the standard. Another, smaller, group of the comment letters advocated a broader or specialized standard for disclosure of activities in or with SSTs. As of this writing, over two years later, the SEC has not responded to the comments. The Web Tool remains suspended.

In the absence of the Web Tool, investors seeking disclosed information about a company’s activities in the Sanctioned Countries use the more cumbersome “full text” search engine on the SEC webpage to search for, for example, references to “Cuba” on a company-by-company basis. A couple of the comment letters submitted in response to the Concept Release praised the existing EDGAR search as adequate for investors seeking information about business operations in or with SSTs. The Organization for International Investment argued that by using the advanced full text search function, investors can “quickly and efficiently” find disclosures made by a company about its activities in any particular country. This, of course, assumes that such disclosures have been made. Part V below describes empirical research demonstrating that such disclosure is often unavailable.

F. Has the OGSR Made a Difference?

Since its establishment in 2004, the OGSR’s activities have included sending numerous inquiry letters to reporting companies asking about their operations in the Sanctioned Countries. In his May 2007 Senate testimony, SEC Chairman Christopher Cox stated that in the prior year, the OGSR had issued comments to approximately 212 companies. Some but not nearly all of the OGSR comment letters and the companies’ responses are available (some in redacted form and some


315. I spent hundreds of hours looking for disclosures about companies with business in SSTs, and I found the EDGAR system to be difficult to use.


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in full) on EDGAR.\(^{319}\) During the four-year period between January 1, 2006 and January 1, 2010, OGSR uploaded onto EDGAR 420 letters that were addressed to over 200 companies.\(^{320}\) The research presented in the next Section will discuss some of the OGSR's correspondence with public companies about their reported (either in disclosure, on their website, or in the media) activities in or with the Sanctioned Countries.

The OGSR is not, however, attempting to change the standard for whether disclosure is required. In requesting additional information, the OGSR is working within the parameters of the existing "materiality" definition: "The Commission's disclosure-based regulatory approach has served the investing public and this agency well over the years, and the standard for disclosure—that of materiality—has long been the foundation of the Commission's work. We are committed to maintaining the materiality standard as the basis for our disclosure-based approach."\(^{321}\) The OGSR sees itself as tasked with enforcing the existing materiality standard, not changing it.\(^{322}\)

G. Private Sector Databases

In the absence of an adequate official source of information about U.S. exchange-listed companies with operations in countries that are subject to U.S. economic sanctions for their sponsorship of terrorism, a private industry has developed. At the institutional investor level, for example, World-Check provides a database of known heightened risk to individuals and businesses.\(^{323}\) World-Check claims that its subscribing customers include more than 3,000 institutions, including over 90% of the world's largest banks and "200 enforcement and regulatory agencies."\(^{324}\)

Individual and institutional investors, as well as asset managers and mutual fund providers, can also purchase private global security risk assessment services from entities such as RiskMetrics or Conflict Se-


320. A list of companies to which the OGSR wrote letters that are available on EDGAR is on file with the author.


322. The materiality standard is flexible. It is possible that by making more companies disclose, the OGSR may make operations in Sanctioned Countries more prominent in investors' minds, and that prominence may make such activities material to more investors.


324. Id.
Securities Advisory Group (CSAG).\textsuperscript{325} Founded in the weeks after the September 11th attacks, CSAG is an independent research provider that specializes in identifying and assessing publicly traded companies that have business activities in or with countries on the U.S. State Department's list of SSTs.\textsuperscript{326} CSAG has also partnered with FTSE Group to provide a “Terror-Free” index,\textsuperscript{327} and CSAG identifies mutual funds that offer “Terror-Free products.”

The development of the private services adds another wrinkle to the question of whether companies should disclose activities in the Sanctioned Countries on the basis that the activities are material. Some investors argue that disclosure standards should not be strengthened because, thanks to the market, the current materiality standard results in sufficient disclosure for most investors, and private services are available for investors that want additional, specific types of information. A number of the comment letters submitted in response to the Concept Release praised the private services, calling them “thoughtful, well-researched, and competitively priced.”\textsuperscript{328}

Others objected to this “outsourcing” and questioned whether it is appropriate for the private sector to provide this information. In the June 3 Letter, the pension funds discussed the possibility of using private entities to perform a screening function, but insisted that “the U.S. government is the only credible and centralized authority to identify, monitor, and report domestic and international companies that are operating in such countries and thereby may be acting contrary to U.S. foreign policy and humanitarian objectives.”\textsuperscript{329} The June 6 Letter also urged that “the federal government is the only credible centralized authority having the power to identify publicly held companies with material business or operations in nations classified as supporting terrorism or subject to sanctions, and to bring this type of


\textsuperscript{326} See id.


\textsuperscript{328} Letter from Paul D. Glenn, Counsel, Inv. Adviser Ass'n, to Nancy M. Morris, Sec'y, SEC 2 (Jan. 22, 2008) (on file with the author); see Letter from Michael J. Ryan, Jr., Senior Vice President & Executive Dir., U.S. Chamber Ctr. for Capital Mkts. Competitiveness, to Nancy M. Morris, Sec'y, SEC 2 (Feb. 4, 2008) (on file with the author); Letter from Todd D. Malan, President & CEO, Org. for Int'l Inv., to Nancy M. Morris, Sec'y, SEC 3–4 (Jan. 15, 2008) (on file with the author) (advocating the use of private and not-for-profit sources of information).

\textsuperscript{329} Letter from Gail Stone, supra note 287, at 2.
information to light in the investment marketplace." The organizations rejected the use of private services, arguing that fee-based lists provided by private organizations can have a high degree of subjectivity and may not include credible or authoritative information sanctioned by the federal government. They are also not without significant transaction costs and investment implications. Possible risks to corporate share value and reputation stemming from business interests in higher-risk countries cannot be properly assessed unless the information is credible, transparent and readily available.

Nevertheless, in the absence of an accessible, publicly available database, investors, including public employee retirement funds, are using the private services.

H. Business Dealings in SSTs Are Material

This brief history of the disclosure issues presented by companies doing business in or with the Sanctioned Countries demonstrates a proposition that should have been obvious all along: information about a company's business dealings in or with an SST is material information, something that reasonable investors want to know. Companies doing business in SSTs often argue that such activity does not need to be disclosed if it is not a substantial part of their global operations. However, these arguments are belied by the attention given to offerings like PetroChina, the explicit interest of institutional investors, the establishment of a new office within the SEC, the SEC's crea-

330. Letter from Cornelia Chebinou, supra note 292, at 1. The Concept Release comment letter submitted by the national auditors, legislatures, and retirement organizations also discussed the availability and adequacy of private services to provide information about activities in or with SSTs. See Letter from Robert "Kinney" Poynter, Executive Dir., Nat'l Ass'n of State Auditors, Controllers & State Treasurers, to Nancy M. Morris, Sec'y, SEC, supra note 314. The organizations argued that identifying companies that operate in states that sponsor terrorism involves judgments that should not be delegated to non-governmental organizations or vendors that may be motivated more by profit than U.S. foreign policy. Id. at 3.


332. On September 7, 2005, New York City Comptroller William C. Thompson, Jr., as the custodian and investment advisor to the New York City pension funds, and the same comptroller who exchanged correspondence with PetroChina in 2000, announced that he had sent letters to twenty-four companies requesting that each company review its business ties to Sudan, examine any potential financial and reputational risks, and report its findings to shareholders. The companies that received letters had been identified by a private service as having business ties to Iran, Syria, Libya, Sudan, Iraq, and North Korea. Comptroller Thompson's press release identified the companies by name and disclosed the funds' holdings in each. See New York City Comptroller Thompson Announces List of Companies Urged to Review Business Ties to Sudan Due to Human Rights, Terrorism Concerns, U.S. STATE NEWS, Sept. 7, 2005, available at 2005 WLNR 15344922.
tion of the Web Tool for investor use, the issuance of the Concept Release, the development of a private market in the non-disclosed information, the sustained attention of NGOs, and the extensive efforts of firms to resist legal requirements that their activities be disclosed. Clearly, the fact that a company is doing business in or with an SST is material to many reasonable investors and should be disclosed.

The technical debates over the Web Tool and the use of private services, and the broader discussions of materiality should not, however, be allowed to obscure more fundamental questions about the scope of U.S sanctions and how the securities laws should handle information in the post-September 11th world. Is the disclosure system, and in particular the concept of materiality, functioning to give investors the information that they need about companies doing business in or with the Sanctioned Countries? Five years after being established, what has the OGSR accomplished? What kinds of information are companies disclosing? As the next part demonstrates, at the present time, the securities laws are not achieving much meaningful disclosure.

V. The Database and Analysis

A. Methodology

1. Establishing a List of Companies Doing Business in or with Iran, Sudan, or Cuba

The first step in evaluating existing disclosure was to create a list of companies doing business in the Sanctioned Countries (the "Preliminary List"). Unfortunately no comprehensive list is publicly available. This Article's research, therefore, proceeded on a new database that was constructed for the purpose.\textsuperscript{333}

a. Sources

The sources of the data were diverse. Mainstream and business media reports (for example, the \textit{Wall Street Journal}, the \textit{New York Times}, and \textit{Business Week}) contained variable amounts and types of information about companies' activities in or with the Sanctioned Countries. Most of this information was hard to locate in a methodical way. For example, newswires were full of information about the Sanctioned Countries, but typing general search terms like "doing business in" and "Iran" into a Google search yielded 3,560,000 results. There were a handful of U.S. newspaper articles and television shows that focused

\textsuperscript{333} Ideally, the database could be expanded and kept up to date through the collaboration of others.
on U.S. companies doing business in SSTs, but a company's investment in a Sanctioned Country was often only newsworthy if investment was large enough to be financially significant to the company's overall operations. Also, many reports that mentioned companies' operations in the Sanctioned Countries only mentioned them in passing and in the context of a report on another topic.

Of course, once a violation of U.S. sanctions laws was alleged, there was often a media report and, at some later point, a government press release or statement. Moreover, in the case of a violation of U.S. sanctions laws, the business activities leading to the violation had to be disclosed not because of general notions of materiality, but because of the specific requirements of Regulation S-K. The goal here, however, was to find companies that were operating lawfully (at least vis-a-vis the sanctions regime) in the Sanctioned Countries and to analyze their disclosure.

NGOs turned out to be the most fruitful source of public information. In response to public concern over companies' activities in the Sanctioned Countries, several organizations that focus on particular countries have compiled lists of companies doing business there. Two of the most useful were United Against Nuclear Iran and the Sudan


336. The point of the Article might be, instead, the health of Fidel Castro in Cuba or post-election violence in Iran.


339. Of course, much of the information that such organizations used to create their lists also came from press reports, but the NGOs also often review companies' websites.

Divestment Task Force. United Against Nuclear Iran publishes a publicly available registry of companies doing business in Iran. Through the first quarter of 2009, the Sudan Divestment Task Force, a project of the Genocide Intervention Network, published a free list of companies doing business in or with Sudan. In June 2009, however, the Sudan Divestment Task Force was replaced by the Conflict Risk Network, which describes itself as "a network of high-net individual and institutional investors whose combined efforts to mitigate conflict risk and increase responsible foreign investment will result in the protection of civilians and improvement of investment returns." The Conflict Risk Network requires a paid subscription for access to information about companies doing business in Sudan.

Thus, all of the information used to create the Preliminary List of companies doing business in the Sanctioned Countries was publicly available. The list does not rely on any information only available on subscription services (such as Westlaw and LexisNexis). It also does not draw from any of the private security risk services (such as Worldcheck, CSAG, and Riskmetrics).

b. Qualitative Assessment of the Data

Information about companies doing business in the Sanctioned Countries gathered from different media and NGO sources varied in depth and quality. In some cases, sources discussed investments in detail, but most sources made only a passing reference to a company doing business in a Sanctioned Country.

In addition, the accuracy of the information gathered through media reports was difficult to assess. Certainly some sources were more credible than others; data gathered from The Economist was more

344. Id. The Sudan Divestment Task Force was also an initiative of the Genocide Intervention Network. Information used to create the Preliminary List of companies for this Article was limited to the last free Sudan Company Report (First Quarter 2009).
345. Of course, some of the information that is publicly available does reflect private services' research. For example, a CalPERS letter that listed companies in which it would not invest cited information that was purchased from Riskmetrics. See Memorandum from Anne Stausboll, Interim Chief Investment Officer, CalPERS, to Members of the Investment Committee 2-3 (Aug. 18, 2008) (on file with the author).
likely to be true than information found on BobHatesCuba.com. However, verification of any of the media reports was difficult. While frustrating for scholarly purposes, the difficulties in data collection and assessment demonstrate an important policy point: Even with determined effort, investors have a hard time getting information about a company's activities in the Sanctioned Countries. Little information is available. The available information is different for each company, so comparing companies is difficult. Even if the information can be found, there is no sure way to know how accurate it is.

2. Cross Referencing with SEC Disclosure

The Preliminary List included 208 large multinational companies that were credibly reported as having operations in or with the Sanctioned Countries. The next step was to identify which of the companies on the Preliminary List filed searchable disclosures with the SEC.

a. Which Companies File Documents with the SEC?

Most companies that file documents with the SEC are public companies. Public companies include companies with securities listed on a national securities exchange, companies traded on the over-the-counter market if they have at least 500 shareholders and $10 million in assets, and companies that have filed Securities Act registration statements (that is, companies that made IPOs in the United States). These companies are required to file reports periodically with the SEC. Most reporting companies are U.S. companies, but some are organized under the laws of another country and access the

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346. There is no website called BobHatesCuba.com. It was invented to avoid singling out any particular site.
347. One of the benefits of SEC-required disclosure is the credibility of the information provided. Companies will make a greater effort to provide accurate, truthful information in order to avoid penalties connected with filing a false report with the SEC.
348. Research conducted by the Conflict Securities Advisory Group estimates that there are over 350 publicly traded companies worldwide with active, nonhumanitarian business ties to Iran, and over 200 with such ties to Sudan. See Foreign Policy Hearing, supra note 3, at 3 (statement of Roger Robinson, Jr., President and CEO, Conflict Securities Advisory Group).
349. Although sometimes a company that issues American Depositary Receipts (ADRS) will file some limited information.
351. See id. § 78l(g).
352. See id. § 78o. Most IPOs will trigger Exchange Act Section 12(g) and, if on an exchange, Exchange Act Section 12(a). Exchange Act Section 15(d) will catch companies that sell debt to the public but keep their equity closely held.
353. For example, Form 10-K, Form 20-F, and Form 40-F reports are filed annually; Form 10-Q reports are filed quarterly, and Form 8-K and Form 6-K reports are filed occasionally.
U.S. capital markets by selling securities in the United States. Non-U.S. companies may sell securities directly or through an American Depositary Receipt (ADR) program. In December 2008, there were 1,024 foreign companies registered and reporting with the SEC.

Foreign companies made up the bulk of the Preliminary List because U.S.-incorporated companies can only do business in Iran and Sudan through certain non-U.S. subsidiaries or affiliates, and they cannot do business in Cuba at all (not even indirectly). The narrowing of the Preliminary List of companies to reporting companies yielded a smaller list of 142 companies (the “Pool”) that issue securities to the public in the United States, and that have operations in or with the Sanctioned Countries. Of the 142 companies in the Pool, 33 are U.S. companies, 61 are organized in European Union countries, and 18 are Japanese.

354. Many of these are foreign private issuers. A “foreign private issuer” is defined in Exchange Act Rule 3b-4(c) to include any corporation or other organization incorporated or organized under the laws of any foreign country, unless

more than 50 percent of [its] outstanding voting securities are directly or indirectly held of record by residents of the United States; and [either] [t]he majority of the executive officers or directors are United States citizens or residents; [m]ore than 50 percent of the assets of the issuer are located in the United States; or [t]he business of the issuer is administered principally in the United States.

17 C.F.R. § 240.3b-4(c) (2009).

355. ADRs are U.S. securities that represent a specified number of a foreign company’s shares. See SEC, International Investing, http://www.sec.gov/investor/pubs/ininvest.htm (last visited Feb. 10, 2010). J.P. Morgan, which created the first depositary receipt program in 1927, estimates that more than 2000 issuers from more than 80 markets have established depositary receipt programs, and that depositary receipts account for more than 15% of the U.S. equity market. J.P. Morgan, About DRs, http://www.adr.com/Reference/Reference.aspx?Ll=AboutDRs&L2=DRsIntro (last visited Feb. 10, 2010). Foreign companies with ADR programs file Form F-6 with the SEC, and more limited disclosure is made on EDGAR.


357. See supra Part II.D.1.


359. A summary of this database is on file with the author.

360. This includes sixteen from the United Kingdom, twelve from France, and ten from Germany.
b. "Searchability"

The Pool was also limited by the dates of the reports that were filed with the SEC: the company had to have filed documents within the last four years—between January 1, 2006 and January 1, 2010. This limitation was imposed by the capabilities of the SEC website. Using EDGAR, only disclosure filed in the last four years can be searched in "full text."

In other words, if an investor is concerned that a particular company is doing business in Cuba, then, by using the Advanced Search tool, she can enter the name of the company and the term "Cuba," and any documents filed by that company with the SEC in the last four years that contain the word "Cuba" will appear on a list. Maybe. Sometimes the search will report that, for example, 15 documents were found, but only 11 will be listed. Sometimes the same search will yield different results on different days.

To see what the company actually disclosed and what kind of activities are concerned, the investor then has to open every document produced by the search and use the "find" (control-F) function to look for the word "Cuba." The paucity of disclosure is thus aggravated by the cumbersome method of gathering the information that is disclosed.

Although the SEC is in the process of adopting a more advanced data submission and retrieval system called Interactive Data Electronic Applications (IDEA), there is some controversy about when and how that system will be implemented. In addition, as discussed below, the benefits to investors from an ability to search for information in companies' filed disclosures are limited by the quality of that disclosure.

3. Limitations and Successes of the Database

The Pool was, of course, incomplete and inconclusive. The media information it relied on varied in depth and was often impossible to verify. The SEC disclosure it relied on was difficult to access and

361. Older disclosures can be searched, but every single document has to be opened and searched separately. For many of these companies, that would be hundreds if not thousands of documents. One could, of course, limit searches to annual (Form 10-K or Form 20-F) reports, but data from the past four years showed that the annual reports provide less than half of the disclosures about business in SSTs that are filed with the SEC.

362. The SEC has been putting into place the "Next Generation EDGAR." See SEC, Search the Next-Generation EDGAR System, http://www.sec.gov/edgar/searchedgar/webusers.htm (last visited Feb. 10, 2010). For example, beginning on August 19, 2009, all EDGAR results pages displayed direct links to an interactive data viewer for company financials and provided links to insider transactions reports. This change, however, had no effect on the data or data retrieval methods used in creating the database for this Article.
probably incomplete. The Pool was not a list of all the companies in the world that had business operations in or with the Sanctioned Countries. It was not even a list of all of the companies filing reports with the SEC that had operations in or with the Sanctioned Countries. It was a broad sample of such companies that was put together to see whether the existing regulatory framework elicits the information investors need and whether it does so in a way they can access. For this limited purpose, the Pool was successful. The Pool included enough companies to provide a look at patterns of company behavior and disclosure.

A review of the disclosure produced by the companies in the Pool showed a low rate and quality of disclosure. Moreover, insofar as the policy question is whether investors can assess where their money is spent, the under-inclusiveness of the database, despite hundreds of hours of work and study, supports the proposition that important information about companies’ business in and with SSTs is simply unavailable.

B. Analysis of Correspondence with the SEC

1. What Is in the Correspondence?

In some cases, the SEC, usually through the OGSR, sent inquiries to companies because those companies referred to a Sanctioned Country in their periodic disclosure. In other cases, the SEC wrote because of the lack of such a reference or disclosure in the face of media reports or a company web page that indicated activity in a Sanctioned Country.

The SEC/OGSR inquiry letter was often formulaic. It identified the periodic disclosure in question, it asked a substantive question, and it asked the company to evaluate the materiality of its operations in or with a Sanctioned Country. Many of the letters cited specific state laws, pension fund guidelines, and university policies against investing in companies with operations in the Sanctioned Country, and asked the company to respond.

Company responses varied, but they generally offered a serious response to the SEC questions. They set forth the details of the oper-
Both quantitative and qualitative materiality were often discussed, but in nearly all cases, the financial impact of the activities in the country in question was estimated to be less than 1% of the company's total revenues or assets, which the company then concluded was not material. The qualitative analysis that followed usually discussed reputation and share value, but was often influenced by the asserted small financial impact as well.

A number of responding companies also cited a lack of interest in the issue on the part of investors. For example, Benetton Group S.p.A. wrote, "The Company is not aware that any investor in the securities of Benetton has ever made any inquiry regarding activities carried on in Cuba, Syria, or Iran." CNOOC Ltd. went even further and argued,

"[T]he Company has not received any significant inquiries from its shareholders or the general public about its affiliates' contacts with Iran. In fact, we have seen no indication that either the United States holders of CNOOC Limited's shares (who constitute a very small percentage of our total shareholders, as discussed below) or..."
our shareholders outside the United States are concerned about this issue.\textsuperscript{366}

Other companies stated that they were aware of no investor selling its shares because of the operations in question, which functioned as further evidence that the operations were not material. Halliburton argued in a May 2006 letter, "We are not aware that any person or entity has made the decision to invest or not to invest in Halliburton based on activity in Iran, nor do we think it likely that one would do so."\textsuperscript{367}

Several companies also discussed whether divestiture by the pension funds or educational institutions mentioned by the SEC would have an impact, and they concluded that such a divesture would not be material: "Assuming that all such institutions were to divest all of their Alcatel stockholdings, we do not believe that such divesture would have a material impact on the market value of our securities."\textsuperscript{368}

The majority of firms responded that their activities in SSTs were not financially significant (whatever that "significant" number may be), were not material, and did not have to be disclosed. As Cummins argued, "We are not aware of any precedent or guidance that requires disclosure of this business [in sanctioned countries] when the amount of sales is de minimis. We do not believe that a reasonable investor would find such information to be material."\textsuperscript{369}

Even companies that disclosed activities in or with a Sanctioned Country after receiving an SEC inquiry often do so while insisting that disclosure is not actually required. In a September 2006 letter to the SEC, Mitsubishi UFJ Financial Group argued against materiality and then conceded, "[Mitsubishi] does not believe that its past and current operations with entities in Iran should be considered a material invest-


\textsuperscript{367} Letter from Margaret Carriere, Senior Vice President & Corporate Sec'y, Halliburton Co., to Cecilia D. Blye, Chief, Office of Global Sec. Risk, SEC (May 26, 2006), http://www.sec.gov/Archives/edgar/data/45012/000004501206000242/filenamel.htm (last visited Apr. 13, 2010). This appears to disregard the stated intention of the NYS pension funds. For a similar argument, see Letter from Jean-Jacques Gathier, Executive Vice President & CFO, Lafarge S.A., to John Hartz, Senior Assistant Chief Accountant, Division of Corp. Fin., SEC 1 (Jan. 31, 2007), http://www.sec.gov/Archives/edgar/data/913785/000119312507017179/filenamel.htm (last visited Apr. 13, 2010).

\textsuperscript{368} Letter from Jean-Pascal Beaufret, CFO, Alcatel-Lucent, to Cecilia D. Blye, Chief, Office of Global Sec. Risk, SEC 2 (Mar. 6, 2006) (on file with the author).

ment risk for investors. Nevertheless, to enhance its ongoing disclosure of potential risks [Mitsubishi] proposes to include additional risk factor disclosure in its [next] annual report.”

2. **What is the Effect of Correspondence?**

The impact of such inquiries seems mixed. Of the 142 companies in the Pool, 75 (53%) were engaged in correspondence with the SEC about their operations in the Sanctioned Countries.\(^{371}\) From these 75 companies, the following data were collected: in 47 cases, an inquiry by the SEC had no marked impact\(^{372}\) on the disclosure made by the company;\(^{373}\) in 21 cases, the company provided better disclosure after exchanging correspondence with the SEC about their activities in or with SSTs;\(^{374}\) and in 7 cases, companies provided less disclosure after an inquiry from the SEC.\(^{375}\)

3. **Is Correspondence Disclosure?**

When the OGSR first began sending inquiry letters to companies, they were not made public. Following strong objections from investors and Congress, the SEC uploaded a large cache of letters, and it began posting the inquiries and requiring companies to respond via EDGAR. Currently, much of the correspondence between the SEC and companies with operations in the Sanctioned Countries is publicly available.

Nevertheless, correspondence between the SEC and reporting companies does not really constitute disclosure. Letters from the SEC are not issued to all companies doing business in the Sanctioned Countries. Companies’ responses range from reasoned analysis prepared by Wall Street law firms to brief one-page answers. There is no stan-

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371. Of the remaining 67 companies, some may have received letters from and responded to the OGSR before January 1, 2006, and some may not have received inquiries from the OGSR at all.

372. Quality of disclosure and impact were judged broadly. Each company’s disclosure was rated “no,” “low,” “good,” or “very good” based on the level of specificity and whether issues such as U.S. sanctions, materiality, or investor sentiment were mentioned. A category change, as opposed to a small tweak in the language, was recorded as an impact.

373. Three of those companies subsequently delisted, 5 discontinued their operations in the country in question, and 4 cases involved a sanctions violation.

374. Two of those companies subsequently delisted, 1 discontinued its activities in the country in question, and 6 were reported to have committed a sanctions violation.

375. In almost half of those cases, however, the company either delisted or discontinued operations in the country in question.
Standard format or guidance for answering an SEC inquiry. These are not documents written for investors. They are not easy to compare. Some are highly redacted. They sometimes disclose information, but they are not disclosure for these purposes.

D. Analysis of the Disclosure

1. Quantitative Summary

The following data reflect the disclosures—available on EDGAR—made by the 142 companies in the Pool in the past four years: 18 (13%) of the companies only mentioned the Sanctioned Countries in their periodic disclosure; 52 (37%) of the companies mentioned the Sanctioned Countries in both disclosure and correspondence with the SEC; 23 (16%) of the companies only discussed the Sanctioned Countries in correspondence initiated by the SEC; and 49 (35%) of the companies made no reference to any of the Sanctioned Countries in any documents filed with the SEC, whether disclosure or correspondence.\(^3\)\(^7\)\(^6\) This means that, at best, 70 (49%)\(^3\)\(^7\)\(^7\) of the companies in the Pool included some mention of the Sanctioned Countries, if only by using the word “Iran,” “Sudan,” or “Cuba,”\(^3\)\(^7\)\(^8\) in their disclosure that was filed with the SEC.

2. Qualitative Summary

Of course, getting companies to provide some disclosure of their operations in or with the Sanctioned Countries is only a beginning. It is also important to review the quality of information that is then disclosed. A review of the actual disclosure revealed that counting 70 companies as “disclosing” likely overestimates the amount of information available to investors. Of the 70 companies that provided any disclosure mentioning the Sanctioned Countries, 19 provided only meaningless disclosure (for example, listing a subsidiary with the word

\(^3\)\(^7\)\(^6\) Of these, 35 were ADR facilities without significant periodic disclosure by the non-U.S. company.

\(^3\)\(^7\)\(^7\) This figure represents the 18 companies that only disclosed, plus the 52 companies that both disclosed and engaged in correspondence with the SEC.

\(^3\)\(^7\)\(^8\) In what may be a simple way to avoid having the name of a Sanctioned Country in its searchable disclosure, Sinopec referred to its purchase of oil from Iran and Sudan by referring to oil sourced from suppliers in “countries or regions that are on the sanction list published and administered by the Office of Foreign Assets Control of the U.S. Department of the Treasury.” China Petroleum & Chem. Corp., Annual Report (Form 20-F), at 3 (May 20, 2009), http://www.sec.gov/Archives/edgar/data/1123658/000134104090001031/china_20f.htm (last visited Feb. 10, 2010).
“Iran” in its name). Only 51 of the companies actually provided disclosure with information about activities in or with a Sanctioned Country that might be useful to an investor. Even the meaningful disclosure varied widely: 18 companies explicitly stated that the company’s activities in the Sanctioned Country were not material; 40 companies made a reference to U.S. sanctions; 21 companies noted a risk from divestment or reputational harm; and 7 companies conceded that the imposition of sanctions could have a material adverse effect on the company.

Even overlooking the quality variations in disclosure, however, the results are striking. Of the Pool of 142 companies with business activities in or with the Sanctioned Countries, only 51 (36%) meaningfully disclosed those activities.

VI. RECOMMENDATIONS AND CONCLUSIONS

In this “post-September 11th”/“War in Iraq”/“War in Afghanistan”/“Genocide in Sudan”/“Iran with Nuclear Ambitions” world, the United States uses economic sanctions to counter global threats and to try to increase global security. As discussed in Part II, sanctions are a cornerstone of U.S. foreign policy. Sanctions are not without problems. In particular, political and legal limitations on the ability of the United States to impose its laws extraterritorially provide an opportunity for regulatory arbitrage: multinational businesses will conduct operations under the varying laws of different jurisdictions. As a practical matter, the foreign subsidiaries of U.S. corporations and foreign corporations doing business in the United States may conduct operations in SSTs or otherwise do business in contravention of U.S. foreign policy and even security interests.

Securities law, through its central mechanism of disclosure, can be used to address this problem. As discussed in Part III, shareholders expect to know what their companies do, and investors generally expect to know how their capital is being used. In particular, as discussed in Part IV, U.S. investors expect to know whether a company

379. It is not clear what to do with the meaningless disclosure cases, and whether they should be considered disclosure at all. However, because the companies did use the word “Iran,” “Sudan,” or “Cuba” in their disclosure documents, thereby making them retrievable through an EDGAR search, those disclosures were counted.

380. Some companies avoided the term “material” and noted instead the potential for “adverse effects” from investor reticence or the imposition of sanctions. See Total S.A., Annual Report (Form 20-F), at 6–7 (Apr. 3, 2009). Others stated that they could not say that the imposition of sanctions would not have a material adverse effect. See Sasol Ltd., Annual Report (Form 20-F), at 26–28 (Oct. 7, 2008), http://www.sec.gov/Archives/edgar/data/314590/000104746908010739/a2187995z20-f.htm (last visited Feb. 10, 2010).
in which they are investing—a company to which they are providing money in return for a share of the profits—is conducting operations in opposition to their nation's foreign policy. Of course, due to the possibilities of regulatory arbitrage in a globalized world, in some cases an investor may decide to invest in a company doing business in an SST anyway. But to keep the investor ignorant of her complicity, albeit indirect, with the regimes of countries such as Iran, Sudan, and Cuba, runs counter to the spirit of the U.S. securities laws.

Precisely because interest in such operations is widespread and intense (and resistance to disclosure is high), information about these operations is "material" in the traditional securities law sense, as laid out by the Supreme Court in *TSC Industries* and *Basic*. For example, institutional investors, NGOs, and much of the international community have expressed concern about Iran's nuclear ambitions, and horror at the violent treatment of protesters in the wake of the June 2009 elections. More generally, as demonstrated by the history of the issue discussed in Part IV, there is a "substantial likelihood" that a "reasonable person" would consider information about operations in or with countries sanctioned by the United States as SSTs "important."381

If information about a company's operations in or with the Sanctioned Countries is important to investors, then the U.S. federal securities laws should be enforced by requiring companies to disclose it.382 Yet the research described in Part V shows that the majority of companies are not providing any disclosure. Although the SEC, using the OGSR, seems to be attempting to elicit disclosure, such efforts have not been effective. Information about activities in and with the Sanctioned Countries is being disclosed at a low rate. To add insult to injury, five years after the establishment of the OGSR and two years since the Web Tool, it is still nearly impossible for investors to find the information they need from publicly available sources, including the SEC. In short, very little information is effectively disclosed.

In the absence of clear guidance from the SEC, it appears that the materiality standard is not taken seriously by ostensibly "reporting" companies and their counsel.383 Specifically, a putatively small finan-

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381. See supra Part III.C.
382. Bear in mind, as mentioned above, that not all material information must be disclosed under the securities laws.
383. This is especially troubling given the recent discovery of Bernard Madoff's fraudulent investment scheme, the recent collapse of stock prices, and the financial crisis.
cial impact of many of the operations in question is treated as simply dispositive. 384

As a matter of accounting, after Enron and the accounting scandals, and after AIG and the financial crisis, claims that a line of business is unimportant and need not be disclosed, at least not in any detail, ought to serve as a warning flag. A line of business that is indeed de minimis might need to be discontinued, not operated in hiding. As a matter of securities law, neither Congress nor the Supreme Court nor the SEC has ever defined materiality in terms of some financial threshold or said that matters of lesser monetary consequence need not be disclosed. The standard has always been what a reasonable investor would likely want to know.

Some issues are accepted by the SEC and investors to be material regardless of their monetary amount. For example, if a company hires a CEO who was convicted of a small amount of embezzlement, the law requires the company to disclose that. As demonstrated in Part IV, interest in business in SSTs is high. The general economic reasons for such interest are obvious. Operations in countries sanctioned as SSTs confront more risks by definition. 385 Activities in the Sanctioned Countries may have a significant financial impact on a company once such activities are made public because of the general repugnance for many of the regimes in question. In fact, a negative public reaction is no doubt a large part of why companies are so hesitant to disclose and why they expend real money fighting the Web Tool, resisting OGSR suggestions about disclosure, commenting on the Concept Release, and so forth. Company reputation and share value are at risk because investors find this issue significant. The potential quantitative impact of divestment, boycotts, and public shaming may be high.

It should also be remembered, however, that more than money is at issue here. It is likely that a U.S. investor would want to know if the company in which his retirement savings are invested is helping Iran’s nuclear program or electoral repression, or buying transportation for Janjaweed raids in Sudan, or facilitating attacks on U.S. troops in Af-

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384. This is in spite of the SEC’s clear statement in the 1999 SAB that a quantitative analysis cannot be used as a substitute for a full analysis of all relevant considerations. See SEC Staff Accounting Bulletin No. 99, 64 Fed. Reg. 45,150, 45,151 (Aug. 19, 1999).

385. A number of state investment retirement boards continue to take the position that companies with business operations in SSTs are exposed to a special risk category. See, e.g., Protecting Georgia’s Investments Act, 2008 Ga. Laws 1022 (codified at GA. CODE ANN. § 47-20-83.1) (requiring public defined benefit retirement plans in Georgia to determine if they have in their portfolios any securities of companies doing significant business with the petroleum industry of Iran).
ghanistan. U.S. investors are also often taxpayers and citizens who have profound interests in not supporting threats to U.S. security.

So what is to be done? Simply enough, the SEC could make clear what Chairman Unger strongly implied years ago: information about business activities in and with SSTs—enemies of the United States—is something that reasonable U.S. investors want to know. This has been empirically demonstrated in this Article. Such activities are therefore material under traditional legal standards. No new law or regulation is necessary. All that is required is for the SEC to enforce a reasonable, indeed traditional, understanding of “materiality.”

Alternatively, reporting companies could be required to disclose whether they, or any of their affiliates, conduct operations in or with SSTs through stricter application of Regulation S-K. The materiality standard is not at issue. Regulation S-K Item 101(d)(3) requires disclosure of risks attendant to foreign operations. In addition, Regulation S-K requires foreign private issuers to disclose whether investors may bring actions against it under civil liberty provisions. Any of those sections would be a reasonable place to require companies to disclose the existence of any direct or indirect operations in or with countries that are subject to U.S. sanctions as SSTs.

Finally, Regulation S-K could simply be amended to include an explicit requirement that business in or with SSTs by a company or its affiliates be disclosed as a matter of course. This would not be an onerous requirement—there are simply not that many countries that the United States designates as SSTs.

As the United States increases the complexity of its sanction regimes, and as companies consolidate and sell securities across borders, issues like this are bound to arise. While some bankers and politicians have objected to the use of the capital markets as a tool for foreign policy, in a globalized world, financial policy simply cannot be isolated from foreign policy concerns, including security concerns.

386. Regulation S-K Item 101 already requires a company to provide a description of its business, its principal products, availability of raw materials, seasonality, and backlog orders. See, e.g., 17 C.F.R. § 229.101(c)(1)(i)-(viii) (2009). Note, however, that this information is required to be disclosed “[t]o the extent material to an understanding of the registrant’s business taken as a whole.” Id. § 229.101(c)(1).

387. See id. § 229.101(d)(3).

388. As of January 1, 2010, the United States has designated four countries as SSTs: Cuba, Iran, Sudan, and Syria.

and foreign policies have always been intertwined. From the negotiations to fund the U.S. War of Independence, to the Marshall Plan, to contemporary worries about U.S.-China debt relations, financial policy is responsive to foreign policy, and vice versa.

It is time for securities lawyers on both sides of this issue to acknowledge that the emperor has no clothes. Companies object to disclosing information about their operations in or with SSTs because they fear that disclosure would alarm investors who do not want to invest in a company that does business in such a country. And that is precisely why, as a matter of securities law, plain and simple, such disclosure must be made.

that market-oriented reforms requiring more disclosure of operations in SSTs and global security risk could be “the most potent non-military means available to the U.S. to curtail terrorism sponsorship and WMD development and proliferation.” See Foreign Policy Hearing, supra note 3, at 6 (statement of Roger Robinson, Jr., President and Chief Executive Officer, Conflict Securities Advisory Group). Robinson goes on to argue,

The U.S. financial system remains a dominant force on the global landscape that few responsible foreign financial institutions and companies can live without. Regrettably, requiring these hard choices on the part of primarily foreign companies and banks is now a necessity. Postponing this day of final reckoning will make more likely a nuclear Iran and more capable and dangerous U.S. adversaries worldwide.

Id.