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Foreign Time Deposits Become “Securities”: Wolf v. Banco Nacional de Mexico

In a case of first impression, a federal district court in California held that time deposits1 in a Mexican bank were “securities” under the federal securities statutes.2 The holding in Wolf v. Banco Nacional de Mexico3 enlarged the scope of the Securities Act of 1933,4 which requires detailed registration5 of securities offered or sold publicly6 in the United States. By bringing foreign time deposits within the Act’s definition of a security,7 the court imposed registration requirements on foreign banks and insured that the securities statutes8 will protect Americans who invest in foreign countries against fraud.

In Wolf, R.J. Wolf, an American citizen, deposited twenty thousand dollars in each of two ninety-day accounts and in one six-month account

1 A time deposit is a “[b]ank deposit which is to remain for [a] specified period of time, or on which notice must be given to [the] bank before withdrawal.” BLACK’S LAW DICTIONARY 396 (rev. 5th ed. 1979).

2 The non-security status of a time deposit in a domestic bank is well settled. See, e.g., Marine Bank v. Weaver, 455 U.S. 551 (1982); Burrus, Cootes & Burris v. McKethan, 537 F.2d 1262 (4th Cir. 1976), cert. denied, 434 U.S. 826 (1977); Bellah v. First Nat'l Bank of Hereford, 495 F.2d 1109 (5th Cir. 1974). For a discussion of Weaver, see notes 92-97 and accompanying text. For a statutory definition of “security,” see infra note 7.

3 549 F. Supp. 841 (N.D. Cal. 1982).


5 For insight into how expensive, time-consuming and complex registration can be, see generally Snowmass Small Business Securities Conference, 35 BUS. LAW. 1367, 1399-1401 (1980) (sponsored by ABA Section of Corporation, Banking and Business Law). See infra notes 49, 50, 53 and accompanying text.

6 See infra text accompanying note 49.

7 The following is the definition of a security in the 1933 Act:

When used in this subchapter, unless the context otherwise requires— (1) The term “security” means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas or other mineral rights, any put, call, straddle, option or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a “security”, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.


8 See supra note 4.
with Banco Nacional de Mexico (Banamex). In a promotional brochure mailed to Wolf, Banamex guaranteed interest rates on these accounts of 31.4 percent, 32.75 percent and 33.9 percent. Upon maturity, however, Wolf discovered that his impressive returns were more than offset by significant losses of principal, once Banamex reconverted the pesos into dollars.

Banamex’s brochure explained that “the Mexican peso . . . is a floating currency which means that the rate of exchange . . . could vary upwards or downwards between the time you purchase your Time Deposit and maturity.” Wolf claimed that despite this seemingly straightforward disclaimer, Banamex misled him into thinking that the Banco de Mexico (Banxico), Mexico’s Central Bank, would maintain a stable peso-dollar parity by intervening in the money market. Banxico, however, abruptly ceased its practice of intervention, whereupon the exchange rate of the peso fell dramatically. Consequently, Wolf’s original sixty thousand dollars was worth roughly thirty-five thousand dollars upon reconversion at maturity.

Wolf sued Banamex, alleging that Banamex was strictly liable for selling him unregistered securities and that Banamex was also liable for misleading him by omitting material information from the promotional brochure. The court did not reach the latter issue, as both parties found dispositive the issue of whether Wolf’s deposits were securities and moved for summary judgment. The court determined that the time deposits were, in fact, securities and found Banamex liable for Wolf’s losses. Judge Schwarzer, writing for the court, surveyed the various approaches used to define a security, and declared them inade-

9 549 F. Supp. at 842.
10 Id. In order to guarantee these high returns, Banamex required conversion of dollars into pesos and did not permit withdrawal of funds until maturity of these accounts. Banamex did make monthly interest payments, however.
11 Id. (Wolf’s $60,000 principal was worth only $35,500 at maturity).
12 Id.
13 The brochure, entitled “Mexico’s Other Great Climate . . . Investment,” stated that Banxico had intervened in the money market “since 1977.” Id. Such intervention likely entails the purchase of large amounts of pesos, for example, to reduce the supply and, thus, increase the demand (represented by the exchange rate for other currencies) for pesos.
14 Id.
15 Id. The sale of unregistered securities is a violation of § 12(1) of the 1933 Act, which governs the issuance of securities. 15 U.S.C. § 77b(1) (1982).
16 549 F. Supp. at 842-43. Here, Wolf sought antifraud protection under the 1934 Act, which governs the resale of securities. 15 U.S.C. §§ 77I(1), 77q(a), 78j(b) (1982).
17 549 F. Supp. at 843. Time deposits are not defined or mentioned in the Acts. The court admits that “if the deposits were not securities, then this court has no jurisdiction over any of plaintiff’s claims.” Yet, “[i]f the deposits were securities, then Banamex is strictly liable under the 1933 Act for failing to register them.” Id. Upon finding that the deposits were securities, the court dealt rather summarily with Banamex, establishing its liability in two short paragraphs. Id. at 853. See infra note 126.
18 Id. at 853. Liability under 15 U.S.C. § 77I(1) is absolute. Damages are available to purchasers who no longer own the unregistered securities.
19 Id. at 846-50.
quately. Instead, the court fashioned a new test which focuses on financial instruments that are not securities. Under the Wolf test, instruments or transactions that unquestionably exhibit the elements most commonly associated with securities are considered such unless they fall into certain well-defined categories of exclusions.

Both the Securities Act of 1933 and the Securities Exchange Act of 1934 omit any mention of time deposits; in fact, both Acts exclude instruments with a maturity of less than nine months. Eschewing a literal reading of the Acts, however, the court refused "to assign the peso accounts to a particular statutory pigeonhole," reasoning that "the emphasis should be on economic reality rather than on the form of the transaction and the letter of the statute." Further, a court should "construe the details of an act in conformity with its dominating general purpose . . . . so far as the meaning of the words fairly permits . . . . " Since both Acts preface the definition of a security with the words "unless the context otherwise requires," the definition is not all-inclusive. In fact, the statutes expressly invite an inquiry into 'context' which has largely superseded the language of the Acts.

Before fashioning its own test, the Wolf court methodically evaluated prior tests, finding that none comprehend a time deposit in a foreign bank as being a security. The court found that the traditional test, formulated in SEC v. W.J. Howey Co., did not apply to debt instruments since the holders of debt instruments invest with "a reasonable expectation of profits." The Howey court defined profits as "either capital appreciation resulting from the development of the initial investment . . . or a participation in earnings resulting from the use of investors' funds." Because time deposits yield a specific interest rate and nothing more, the Howey test did not apply in Wolf.

The court also found unhelpful the "commercial-investment" test,
despite its adoption by four other circuits. This test involves comparing the instrument in question with other instruments that are easily identified with either investment or commercial transactions. According to the court, the weakness of this test is its simplicity: it provides virtually no guidance to transacting parties and lower courts and requires case-by-case treatment.

Finally, the "risk capital" test, seen by the court as a "variation on Howey," fails in its attempt to classify debt instruments as either a "risky loan" or "risk capital." Under the test, a "risky loan," to which inheres the usual risk of lending money, does not rise to the level of "risk capital," which is dependent on the borrower's "enterprise efforts." The court questioned the analytical viability of the test, finding that its prescribed factors "lack definition and defy weighting."

Adopting what it considered "[t]he most direct and reliable approach," the Wolf court defined a security and enumerated various exclusions. According to the court:

[A] transaction in which one person ("the investor") provides funds to another with the expectation of a financial or economic benefit is a security unless: (a) the benefit derives largely from the managerial efforts of the investor; or (b) the investor received something of intrinsic value which he intends to use or consume; or (c) the provider of funds is in the business of lending funds in such transactions; or (d) the person to whom the investor provides funds is merely the investor's agent; or (e) the transaction is virtually risk-free to the investor by reason of governmental regulation.

Wolf's time deposits could fall only under exception (e), but the court was unwilling to classify the peso accounts as "virtually risk-free," because Wolf assumed not only the risk of Banamex's insolvency, but also the much more significant risk of currency devaluation.

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33 Id. at 847. For an application of "the 'commercial-investment' dichotomy of the Third, Fifth, Seventh and Tenth Circuits," see American Bank & Trust Co. v. Wallace, 702 F.2d 93, 96 (6th Cir. 1983) (citing United Am. Bank of Nashville v. Gunter, 620 F.2d 1108 (5th Cir. 1980)); National Bank of Commerce of Dallas v. All Am. Assurance Co., 583 F.2d 1295 (5th Cir. 1978); Woodward v. Metro Bank of Dallas, 522 F.2d 84 (5th Cir. 1975); McClure v. First Nat'l Bank of Lubbock, Texas, 497 F.2d 490 (5th Cir. 1974), cert. denied, 420 U.S. 930 (1975); Zabriskie v. Lewis, 507 F.2d 546 (10th Cir. 1974); Bellah v. First Nat'l Bank of Hereford, 495 F.2d 1109 (5th Cir. 1974); Lino v. City Investing Co., 487 F.2d 689 (3d Cir. 1973). See also C.N.S. Enterprises, Inc. v. G & G Enterprises, Inc., 506 F.2d 1354 (7th Cir. 1975).

34 549 F. Supp. at 847. Easily identifiable investment instruments include common stock, bonds and debentures. Well-recognized commercial instruments include consumer loans and short-term commercial paper. Id.

35 Id.

36 Id. at 847-48.

37 Id. at 848.

38 Id. at 849.

39 Id. at 850. See infra note 110.

40 Id. at 850.

41 Id. at 850-52 (citations omitted) (emphasis in original).

42 Id. at 852.

43 Banamex deposits were not insured. Id. at 845.

44 Id.
ception (e) did not apply. The rationale behind exception (e) is that the protection afforded by the Securities Acts is unnecessary because other governmental regulation largely eliminates risks that would otherwise be faced by the 'investor.' Acknowledging the thoroughness of Mexican banking regulation, the court nonetheless maintained that governmental regulation has no effect on the primary risk to which an investor in foreign time deposits is exposed — the risk of devaluation.

Understanding the *Wolf* decision requires familiarity with the 1933 and 1934 Acts and the Supreme Court decisions construing these Acts. In *United Housing Foundation, Inc. v. Forman*, the Supreme Court made it clear that:

> [T]he primary purpose of the Acts of 1933 and 1934 was to eliminate serious abuses in a largely unregulated securities market. The focus of the Acts is on the capital market of the enterprise system: the sale of securities to raise capital for profit-making purposes, the exchanges on which securities are traded, and the need for regulation to prevent fraud and to protect the interest of investors.

The Acts set forth strict requirements for the registration of, and public access to, detailed information concerning securities offered or sold in the United States. Failure to properly register such securities with the Securities and Exchange Commission (SEC) can result in significant civil liability. Therefore, whether or not a particular instrument is a security greatly affects the rights of both seller and purchaser.

The first Supreme Court case construing the definition of a security in the 1933 Act was *SEC v. C.M. Joiner Leasing Corp.*, in which the Court set out rules of statutory construction that courts still apply to both Acts. In *Joiner*, the respondents attempted to sell assignments of oil leases by mail to almost one thousand prospective buyers. Although the 1933 Act definition of a security lists particular documents, instruments and interests, it is not exhaustive. According to the *Joiner* Court:

> [T]he reach of the Act does not stop with the obvious and commonplace. Novel, uncommon, or irregular devices, whatever they appear to be, are also reached if it be proved as a matter of fact that they were widely offered or dealt in under terms or courses of dealing which established their character in commerce as "investment contracts," or as "any interest or instrument commonly known as a 'security.'"

45 Id. at 852.
46 Id. at 853.
48 Id. at 849.
50 Id. at § 77f(d).
51 Id. at § 77g.
52 Id. at § 77c.
53 Id. at § 77h.
54 Id. at § 77k.
55 320 U.S. 344 (1943).
56 Id. at 346.
57 Id. at 351.
The Court noted further that the general purpose of the 1933 and 1934 Acts was to prevent fraud and to protect investors. Therefore, in applying acts of this general purpose, the courts have not been guided by the nature of the assets back of a particular document or offering. The test rather is what character the instrument is given in commerce by the terms of the offer, the plan of distribution, and the economic inducements held out to the prospect. In the enforcement of an act such as this it is not inappropriate that promoters’ offerings be judged as being what they were represented to be.\textsuperscript{58}

Noting that the early state antifraud securities statutes were given “a liberal construction,”\textsuperscript{59} the \textit{Joiner} Court urged similar interpretation of the 1933 and 1934 Acts.\textsuperscript{60} Respondents sold leasehold rights, but the drilling agreements offered along with the leases gave the leases most of their value and all of their appeal as investment instruments. Thus, the \textit{Joiner} Court found the oil leases to be “investment contracts,”\textsuperscript{61} which are specifically included in the 1933 and 1934 definitions of a security.\textsuperscript{62}

Three years later, in \textit{SEC v. W.J. Howey Co.},\textsuperscript{63} the Supreme Court specifically defined “investment contract.” In \textit{Howey}, respondents sold interests in a citrus grove coupled with contracts for cultivating, marketing and remitting the net proceeds to the investors.\textsuperscript{64} Reasoning that the 1933 “Congress was using a term the meaning of which had been crystallized by . . . prior judicial interpretation,”\textsuperscript{65} the \textit{Howey} Court adopted the following definition:

\begin{quote}
[An investment contract for purposes of the Securities Act means a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party, it being immaterial whether the shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed in the enterprise.\textsuperscript{66}
\end{quote}

The \textit{Howey} Court interpreted the legislative intent behind the 1933 Act as embodying “a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised

\textsuperscript{58} \textit{Id.} at 352-53.
\textsuperscript{59} \textit{Id.} at 353. The Court noted that “[w]hile the [various state] laws are not uniform, they . . . all have the dominating purpose to prevent and punish fraudulent floating of securities.” \textit{Id.} (footnotes omitted).
\textsuperscript{60} \textit{Id.} at 353-55.
\textsuperscript{61} \textit{Id.} at 349. The Court noted that if the exploration for oil had not been “woven into these leaseholds, it would have been a quite different proposition.” \textit{Id.} at 348. The facts, however, showed that drilling the wells “was necessary not only to fulfill the hopes of purchasers but apparently even to avoid forfeiture of their leases.” \textit{Id.} at 349.
\textsuperscript{62} The definitions of a security, of both Acts, are expansive in order to insure “full and fair disclosure” in the issuance and resale of unusual instruments “that fall within the ordinary concept of a security.” \textit{SEC v. W.J. Howey}, 328 U.S. 293, 299 (1946) (citing \textit{Joiner}).
\textsuperscript{63} 328 U.S. 293 (1946).
\textsuperscript{64} \textit{Id.} at 295-96.
\textsuperscript{65} \textit{Id.} at 298.
\textsuperscript{66} \textit{Id.} at 298-99. The Court found it “reasonable to attach that meaning to the term as used by Congress, especially since such a definition is consistent with the statutory aims.” \textit{Id.} at 298. Further, the \textit{Howey} Court acknowledged that this definition had prevailed in \textit{Joiner}. \textit{Id.} at 299.
by those who seek the use of the money of others on the promise of profits.\textsuperscript{67} The fact that the interests in the citrus grove were without intrinsic value was immaterial,\textsuperscript{68} as was the speculative or non-speculative nature of the enterprise.\textsuperscript{69} The test was whether there was an investment in a common enterprise with profits arising solely from the efforts of others.\textsuperscript{70}

The Supreme Court first construed the definition of a security in the 1934 Act\textsuperscript{71} in \textit{Tcherepnin v. Knight}.\textsuperscript{72} In \textit{Tcherepnin}, the instruments in question were withdrawable capital shares in a state-chartered savings and loan association.\textsuperscript{73} Employing the \textit{Howey} test, along with language from both \textit{Howey} and \textit{Joiner}, the \textit{Tcherepnin} Court had little difficulty fitting the withdrawable capital shares held by the petitioners into the expansive concept of a security.\textsuperscript{74} \textit{Tcherepnin}'s most significant contribution to the development of securities law was its finding that the definitions of a security, in the 1933 and 1934 Acts, despite slight differences,\textsuperscript{75} were "intended to be 'substantially' the same."\textsuperscript{76}

The Court refined its concept of a security in \textit{United Housing Foundation, Inc. v. Forman}.\textsuperscript{77} In \textit{Forman}, shares of "stock" which entitled the respondents to acquire an apartment in a state subsidized and nonprofit housing cooperative were held not to fall within the definition of a security.\textsuperscript{78} The Court refused to adopt a literal reading of the 1933 Act,\textsuperscript{79} which explicitly defines stock as a security,\textsuperscript{80} choosing instead to examine

\textsuperscript{67} \textit{Id.}
\textsuperscript{68} \textit{Id. at 301.}
\textsuperscript{69} \textit{Id.}
\textsuperscript{70} \textit{Id.}
\textsuperscript{71} The following is the definition of a security in the 1934 Act:

\begin{quote}
When used in this chapter, unless the context otherwise requires . . . the term "security" means any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit, for a security, . . . or in general, any instrument commonly known as a "security"; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; but shall not include currency or any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited.
\end{quote}


\textsuperscript{72} 389 U.S. 332 (1967).
\textsuperscript{73} \textit{Id. at 333.}
\textsuperscript{74} \textit{Id. at 338.} Instruments which share in profits of an organization closely resemble stock, which is usually a security.

\textsuperscript{75} The definitions of a security differed slightly between the two Acts, compare \textit{supra} note 7 with \textit{supra} note 71; however, \textit{Tcherepnin} made clear that they are effectively one.

\textsuperscript{76} 389 U.S. at 342 (footnotes omitted). The Court cited specific legislative history to support this conclusion.

\textsuperscript{77} 421 U.S. 837 (1975).
\textsuperscript{78} \textit{Id. at 848.}
\textsuperscript{79} \textit{Id.} (quoting \textit{Tcherepnin}).
\textsuperscript{80} See \textit{supra} note 7.
the economic realities of the transaction. According to the Court, "Congress did not attempt to articulate the relevant economic criteria for distinguishing 'securities' from 'non-securities.'" The task of setting out such criteria, therefore, "has fallen to the ... SEC ... and ultimately to the federal courts."

The Forman Court borrowed from the Howey test. "The touchstone is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others." Because the investors in Forman were attracted solely by the prospect of acquiring a place to live, and not by financial returns on their investments, the necessary stock shares were not securities. Focusing on the buyer's motivation in purchasing the instrument, the Court was able to distinguish the shares of "stock" from securities.

In a recent case with facts similar to those in Wolf, the Court held that a certificate of deposit (CD) was not a security. In Marine Bank v. Weaver, the Weavers purchased a CD from Marine Bank which they pledged back to the bank as a guarantee for a loan to a third party. The Weavers made a separate business agreement with the third party. When the third party defaulted on the loan, the bank claimed the pledged CD. Respondents sued for protection under the 1934 Act, asserting that the bank had acted fraudulently by not disclosing to them the third party's weak financial condition. The Weaver Court distinguished the CD from the withdrawable capital shares of a savings and loan association which were held to be securities in Tcherepnin. Although admittedly a long-term debt instrument, a CD pays only a fixed rate of interest, not a share of profits. In addition, this CD was insured by the Federal Deposit Insurance Corporation (FDIC), and the holder was "virtually guaranteed payment in full." The ordinary long-term debt in-

81 421 U.S. at 848. As the shares could not be "transferred to a nontenant ... pledged or encumbered," id. at 842, the Court reasoned that these were not stock, as defined in the Acts.
82 Id. at 847.
83 Id. at 848.
84 Id. at 852.
85 Id. at 853.
86 Id. at 851.
87 Certificates of deposit are essentially time deposits, or "[d]ocument[s] evidencing [the] existence of a time deposit." BLACK'S LAW DICTIONARY 205 (rev. 5th ed. 1979).
88 455 U.S. 551 (1982).
89 Id. at 552-53.
90 Id. at 553-54.
91 Id. at 554. The bank was aware of the third party's prior obligations, but let the Weavers pledge their CD, without alerting them to the possible default. Id.
92 Id. at 553. The Weavers were unaware that the third party already had overdue obligations, which the loan paid off. The Weavers alleged that the agreement was that the loan would provide working capital to the third party.
93 Id. at 557.
94 Id. Compare supra note 87 with supra note 1.
95 455 U.S. at 558.
instrument holder, on the other hand, undertakes the risk of the borrower's potential insolvency.96 Accordingly, the Court reasoned, "It is unnecessary to subject issuers of bank [CDs] to liability under the antifraud provisions of the federal securities laws since the holders of bank [CDs] are abundantly protected under the federal banking laws."97 Weaver, therefore, stands for the proposition that securities regulation need not apply where other regulatory schemes provide antifraud protection.

The court in Wolf also denigrated any literal reading of the 1933 and 1934 Acts,98 arguing that the statutes expressly invite an inquiry into "context,"99 and that predictability, certainty and soundness of result remain the primary concerns of courts construing these Acts.100 The holding in Wolf, however, extended prior reasoning to encompass an entirely new area of law. While rejecting the Howey test as inapplicable to debt instruments,101 the court also characterized as dicta the Forman refinement of Howey,102 and attempted to set precedent by formulating what it called "[t]he most direct and reliable approach" to determining whether or not a particular instrument is a security.103

Despite its eloquence, the Wolf decision is unimpressive in its treatment of prior cases. In support of its novel analysis, the Wolf court listed numerous cases to support its reformulated test,104 carefully explaining each exclusion. Only exclusion (e)105 applied to Wolf's peso accounts, however, and exclusion (e) was supported only by the rationale expressed in Weaver and Forman,106 cases held in low regard by the Wolf court. The court had rejected outright the notion that Weaver was controlling;107

96 Id.
97 Id. at 559.
98 The court claimed that "[t]he avid literalism in which both parties engage has been repudiated by the courts, and it is unnecessary to assign the peso accounts to a particular statutory pigeonhole." 549 F. Supp. at 843.
99 Id. at 844. To support this claim, the court cited numerous cases which have "yielded results that squarely conflict with [the statutory] language." As an example, the court noted that the exemption for instruments of more than nine months maturity has "in effect been deleted from the statute by judicial interpretation." Id.
100 Id. at 850. Defending its new test, the court explained its motives: "[A] considerable degree of predictability can be derived by importing into the literalist approach the substance of the existing decisional law. While doing so will not enable parties or lower courts to predict with certainty the outcome of an appeal, it provides them with helpful guidelines." Id. at 850 n.11.
101 Id. at 847.
102 The Wolf court boldly stated that the "statement of the Supreme Court focusing on the requirement of an expectation of profit goes beyond what was necessary for the decision." Id. at 846. The inescapable implication is that Forman added very little precedential language to the Howey test, which Wolf rejected outright. In treating Forman instead as an example of an exclusion category in its new test, the Wolf court cleverly avoided contradicting a Supreme Court holding. Id. at 848-49 n.7.
103 Id. at 850.
104 Id. at 850-52.
105 Id. at 852. See supra text accompanying notes 40-45.
106 Id. at 852-53.
107 Id. at 845.
and had found that the *Forman* test posed "obvious difficulties" in its application. This inconsistent use of Supreme Court cases — on the one hand denying their applicability, and on the other hand citing to them as authority — adds more confusion than illumination. Further, the *Wolf* court repudiated a Ninth Circuit holding, *Great Western Bank & Trust v. Kotz*, which applied the "risk capital" test, because, of the six factors in the test, "three factors lead to one conclusion while an equal number leads to the opposite conclusion." Refusing to weigh the factors, and asserting that the Supreme Court had refused to endorse the test in *Forman*, the *Wolf* court discarded the "risk capital" test. Finally, in eschewing the commonly used "risk capital" and "commercial-investment" tests, the *Wolf* court complained that "the process of decision in those cases rests less on analysis than on synthesis."

Two paragraphs later, however, the court declared that in employing its new test,

> [this Court is of course bound by the law of the Ninth Circuit, and this decision is founded on that principle. But the Court views that law, in accordance with the common law tradition, as residing more in the results reached by the cases than in the articulation of particular reasons for those results.]

In sum, *Wolf* denounced a multi-factor analytical approach that seeks to identify securities, and proposed instead a multi-exclusion approach that seeks to identify non-securities.

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108 Id. at 848 n.7.
109 532 F.2d 1252 (9th Cir. 1976). See *also* AMFAC Mortgage Corp. v. Arizona Mall of Tempe, Inc., 583 F.2d 426 (9th Cir. 1978); United Cal. Bank v. Fin. Corp., 557 F.2d 1351 (9th Cir. 1977); El Khadem v. Equity Secur. Corp., 494 F.2d 1224 (9th Cir.), cert. denied, 419 U.S. 900 (1974).
110 The *Kotz* test includes six factors used to determine the presence of risk capital: (1) the length of time of the risk; (2) whether or not the funds are collateralized; (3) the number of investors; (4) the relationship of the sum involved to the size of the borrower's business, (5) whether the funds are used as capital or for operations; and (6) the form of the obligation. *Wolf*, 549 F. Supp. at 848 (citing *Kotz*).
111 Id. at 850. The court found that the short maturity periods, the vast underlying assets of Banamex, and the small size of the time deposits in relation to Banamex's total business (factors (1), (2), and (4) of the *Kotz* test) militate toward finding that the time deposits were not securities. On the other hand, the large number of time deposit investors, Banamex's use of the funds as capital, and the form of the transaction (factors (3), (5), and (6)) lead to the conclusion that the time deposits were securities. *Id.* at 849.
113 549 F. Supp. at 850.
114 Id. at 850 n.10.
115 Id. at 850.
116 Id.
Wolf left unanswered many questions, particularly with respect to future application of the Wolf test. To distinguish Weaver, the court framed the question "whether a [CD] whose purchaser is not completely insulated from risk is 'within the broad sweep of the [1933] Act.'"\textsuperscript{117} Perhaps the court meant to imply that all instruments uninsulated from risk are within the Act's scope. CDs, however, are risk instruments, in that inflation — like a currency exchange rate — may devalue the principal. In fact, the purchaser of any fixed maturity instrument takes the risk that interest rates will rise before maturity. The Wolf court noted that bonds may fall under the Securities Acts\textsuperscript{118} but failed to pursue the analogy. The court constructed an elaborate formula, yet it is unclear to what instruments, other than foreign CDs, it will apply. It remains unclear, as well, how a foreign citizen will fare upon purchase of a CD from a United States bank. The risk of insolvency is de minimis, but the risk of devaluation remains. Another question arises as to how courts will treat an American who purchases a CD at an American financial institution not insured by the FDIC. Despite the Wolf court's aim of providing predictability,\textsuperscript{119} difficult questions remain unanswered.\textsuperscript{120}

Further questions arise as to the analytical soundness of the Wolf decision. The court fails to acknowledge that Wolf, a wealthy investor who was sufficiently sophisticated and informed to know the attendant risks,\textsuperscript{121} knowingly undertook the risk of devaluation because of the "impressive yields" available. Perhaps an investor's assumption of the risk is an inapposite consideration in securities law analysis, especially where a statute imposes absolute liability. The Wolf court did argue that the "risk capital" test\textsuperscript{122} was unacceptable, as the Supreme Court had not endorsed it.\textsuperscript{123} Yet, the controlling issue in Wolf was "the essential risk to which an investor in foreign time deposits is exposed — the risk of

\textsuperscript{117} Id. at 845-46.
\textsuperscript{118} Id. at 848 n.7.
\textsuperscript{119} Id. at 850 n.9.
\textsuperscript{120} Commentators have complained that even Weaver failed to articulate reasons why the existence of federal banking law protection obviates the need for application of federal securities law protection. They also argue that Weaver failed to provide any "guidance on either the depth of analysis or the amount of fact finding that a court must conduct" before it finds that the existence of other federal legislation renders unnecessary the application of federal securities law. Also unanswered is "how much risk is necessary to require the protection of federal securities law." Note, The Definition of Security: Marine Bank v. Weaver, 24 B.C.L. REV. 1053, 1079 (1983). See also Ianni, "Security" Under the Glass-Steagall Act and the Federal Securities Acts of 1933 and 1934: The Direction of the Supreme Court's Analysis, 100 BANKING L.J. 100, 136 (1983). Wolf does little to provide certainty and predictability in these areas. See also Legal Times, Sept. 26, 1983, at 9, col. 3.
\textsuperscript{121} See United Cal. Bank v. THC Fin. Corp., 557 F.2d 1351 (9th Cir. 1977)(a commercial lending arrangement, between sophisticated parties with equal access to relevant information, was not a security). Wolf rejected this holding, as it employed the "risk capital" test. 549 F. Supp. at 848. But Wolf probably had equal access to Banxico's record of such information as these are probably commonplace and ordinary to both foreign banks and sophisticated investors.
\textsuperscript{122} See supra notes 36-37.
\textsuperscript{123} 549 F. Supp. at 847-48.
devaluation."\textsuperscript{124}

Questionable analysis notwithstanding, the \textit{Wolf} decision reflects a significant judicial concern about the danger to Americans of investing in foreign countries. Distinguishing \textit{Wolf}'s facts from those of prior cases achieved some important goals. First, the court did not feel bound by the case law precedent of either the Ninth Circuit or the Supreme Court, no matter how insightful the reasoning. No previous case had considered a foreign security, particularly a foreign debt instrument. Although the facts in \textit{Wolf} could have fit within the "risk capital" analysis, if the court had not given up on its six-factor test, the court attempted to set out novel securities law analysis. The result, under the "risk capital" test, may well have been the same, but the court used the unique facts of the instant case to avoid such an analysis, achieving a clever subterfuge. In departing from traditional analysis, the \textit{Wolf} court escaped the inevitable scrutiny and likely condemnation of banking regulation in Mexico. Thus, by emphasizing the uniqueness of a time deposit in a foreign bank, the \textit{Wolf} court watered down its evidently controlling sentiment that American investors should not suffer at the hands of poorly regulated foreign banks or enterprises.

A close reading of \textit{Wolf} reveals that the decision advanced the court's goals as to results and predictability. Although the claim that this new \textit{Wolf} test comprehends "almost all situations likely to arise\textsuperscript{125} may be too grand, the test clearly controls all foreign CDs and similar instruments. Thus, until the final disposition of \textit{Wolf},\textsuperscript{126} foreign banks and enterprises that fail to register CDs with the SEC may incur absolute liability. \textit{Weaver} may hold that the Federal Securities Acts do not provide remedies for all fraud,\textsuperscript{127} but \textit{Wolf} neatly limits the \textit{Weaver} holding, which is regarded with some disfavor,\textsuperscript{128} to deposit accounts within the United States.\textsuperscript{129} Given the general aim of the Acts—to protect investors

\textsuperscript{124}Id. at 853 (emphasis added).
\textsuperscript{125}Id. at 850.
\textsuperscript{126}See \textit{Wolf} v. Banco Nacional de Mexico [1983 Transfer Binder] \textit{Fed. Sec. L. Rep.} (CCH) ¶ 99,580. The Ninth Circuit found the \textit{Wolf} judgment unappealable as there was "no direction for entry of final judgment on the first claim." The court of appeals also declared that as the lower court's "judgment did not consider [the fraud] claims . . . they remain live claims for relief." In describing the judgment as a "curious document" and declining to review, the Ninth Circuit has side-stepped, for the moment, the merits of this case. Such treatment of \textit{Wolf} is unlikely to remove the case's deterrent effect on foreign banks and enterprises in issuing CDs.
\textsuperscript{127}See Odom v. Slavik, 703 F.2d 212, 215 (6th Cir. 1983); Am. Bank & Trust Co. v. Wallace, 702 F.2d 93, 97 (6th Cir. 1983).
\textsuperscript{128}"\textit{Weaver} will probably resolve the security issue as to [CDs], but it will be of little assistance otherwise because it relied so heavily on the existence of a protective bank regulatory system." \textit{Annual Review of Federal Securities Regulation}, 38 \textit{Bus. Law.} 1851, 1863 (1983). "[T]he \textit{Weaver} opinion bristles with analytical deficiencies, . . . [and] in its desire to narrow the scope of the federal securities laws, [the Court] resorted to inaccurate and hasty generalizations . . . [which] will undoubtedly precipitate much securities litigation." Bunch, \textit{Marine Bank v. Weaver: What is a Security?}, 94 \textit{Mercer L. Rev.} 1017, 1042-43 (1983). See also supra note 120.
\textsuperscript{129}The \textit{Wolf} court again avoids direct contradiction of a Supreme Court case, pointing to the \textit{Weaver} court's admission that it did not intend its holding to cover CDs under all circum-
and prevent fraud — the protection of Americans investing abroad may be warranted. By saying "Buy American" to United States investors, however, the court revealed its judgment that foreign regulation is untrustworthy.

Thus, "despite the formulas and rhetoric, the common thread which winds throughout the [fifty] years of experience with the definition [of a security] involves an analysis of risk in the light of economic reality." The holding in Wolf v. Banco Nacional de Mexico places one of the risks of today’s economic realities — currency devaluation — on foreign banks that fail to register United States offerings of deposit accounts. More broadly, Wolf portends that the risks of fraud and abuse in unregulated investment instruments will rest on foreign enterprises that seek out American investors.

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130 See supra text accompanying note 47.
131 The current unsettled relationship between the United States and Mexico, in particular, does make Mexico’s investment market appear uncertain. See generally Inman, U.S.-Mexican Trade: New Initiatives Are Needed Now, 7 N.C. J. INT’L L. & COM. REG. 355 (1982); see also Comment, The Regulation of Foreign Business in Mexico: Recent Legislation In Historical Perspective, 7 N.C. J. INT’L L. & COM. REG. 383, 383 (1982) ("Any foreigner who attempts to do business in Mexico will immediately encounter a legal system which treats the outsider as both a partner and an adversary.").