

1. HISTORICAL DEVELOPMENT

(Blue Sky Laws) *Blue Sky Cases (1917)* 14 Amend (LL8)
 'so many feet of 'blue sky' *Hall v Geiger-Jones Co (1917)*

- 1. Background 1929 UK Prospectuses Merit & Disclosure Theory & EMT
- 2. Dual State and Federal (and Tax) Regulation State Reservation Clause s18(c)SA
- 3. Statutory Basis (1) Securities Act 1933 Primary Offerings

- 'integrated disclosure system' Reg SK SX (2) Securities and Exchange 1934 Exchanges and Broker Dealers
- TEFRA (registered bonds) (3) Trust Indenture Act 1939 Bond Issues registered under SA
- (7) Public Utility Holding Co 35 (4) Investment Company Act 1940 CIS 'investment company' inc SPVs
- (8) Sec Investor Protection 70 (5) Investment Advisers Act 1940 Advice not 'incident' to brokerage
- (6) Sarbanes Oxley Act 2002 Registered security filings/governance

<http://www.sec.gov/about/whatwedo.shtml#laws>

2. PUBLIC ISSUES AND THE SECURITIES ACT 1933 Govern offer and sale of securities

- 1. Establish SEC (five Commissioners five-year terms) [Fin Industry Reg Auth (FINRA) (NASD)]
- 2. Registration or Exemption of publicly offered 'securities' reg state 5 SA/ 10 SA prospectus

- Strict Under* (1) Unlawful sell sec transportation or communication interstate commerce or mails
- Firm Commitnt* (2) Registration Statement (s5(1) and Prosp (s10) subject Exempt *Sec (s3) *Trans (s4)
- Best Efforts* (3) Dist (a) Before Filing RS (b) Waiting Period (oral offers) (c) After Effective Date RS
- Shelf Regtn* (4) Liability ss5, 11 (miss RS), 12 (Pros), 17 (antifraud), 23 (misrepresent), 24 (violation)
- (5) Financial Statements prepared under US GAAP or IFRS with SA 202 and liability

- 3. Exemptions (1) **Section 4(a)(2) ('transactions not involving a public offering') & Reg D

- (vi) Poss comply wh Form D Reg D (i) No general 'solicitation or advertising' 'private placement'
- (vii) 'Investment letter' signature (ii) 'Accredited investors' or 35 other 'experienced' persons
- (viii) Poss aggregation other issues (iii) Information furnishing to non-AIs (but generally only AIs)
- (ix) Registered under TEFRA (iv) Not apply 'underwriters' (generally used agency basis)
- (x) Blue Sky Laws compliance (v) Form D filing within 15 days of first sale

- (2) **Rule 144A Resales to institutional investors (QIBs 100m) Resales

- (vi) Gen registered TEFRA (i) 'Eligible securities' (not listed exchange or quoted NASDAQ)
- (vii) Blue Sky Laws compliance (ii) 'QIB' (discretionary investors over \$100 million and BDs)
- (viii) Due Diligence with 'cover' audit (iii) Information provision to investors & prospective purchasers
- Rule 10b-5 letter lawyers (iv) Notice of reliance
- (v) No 'general solicitation or advertising' in the US

- (3) **Regulation S ('Safe Harbour') for non-US purchasers (unless used for

purposes of avoidance Regulation S Preliminary Note 2) Offshore

(i) 'Offshore Transaction' Cat 1,2,3 (a) Offshore transactions

(ii) No 'directed selling efforts' US (b) Directed selling effort

- (4) Section 4(1-1/2) (resales of privately privately placed securities)

Non-affiliates 6 months or 1 year (5) Rule 144 SA (public resales of privately privately placed securities)

- (6) Commercial paper 'prime quality' 3(a)(3) (c) Offering & transaction

(not purchased general public, 9 months, for current transactions)

- 4. TEFRA (prevent tax evasion with registered form requirement) (principal and interest),

TEFRA NA - (unless natural person, not offer general public, over 1 year and non-US or 'foreign targeting')

(i) Registered ('arrangements reasonably designed' no sale to US person, no interest paid US, use legend)

(ii) Less 1 year (TEFRA C Rules issued outside US and no 'interstate commerce') (TEFRA D Rules 40 day

(iii) Secondary 'lock-up' to confirm non-US beneficial ownership before definitive notes issue / interest paid).

transactions (D 'safe harbour') (D more restrictive Reg S no certification and wider definition 'US person')

- 5. Liability

- (1) TEFFA Issuer (excise tax 1% principal times maturity and loss interest deduction) with Holder (loss deduction and tax schemes as ordinary & not capital gain income)

- (2) Eurobond sales restrictions (invitation telex, offer circular, subscription agree, note)

<http://www.sec.gov/about/whatwedo.shtml#VLFNks4pUuU> <http://www.sec.gov/images/secorg.pdf>

3. SECONDARY TRADING & SECURITIES AND EXCHANGE ACT 1944 Extends SA continuous disclosure

EDGAR 1. US Securities Exchanges and Broker Dealers (reporting, liability and proxies/tender offers)

- 2. SEC (s4(a)) and reg exchanges and OTC markets, anti-fraud and securities credit control Fed

- 3. (**Secs traded NSE registered under s12 SEA)

s13 co *reporting obligations & s16 *direct, officers and 10% stockholders ('s 16 insiders')

- 4. Extensive SEC rulemaking power and doubled 1975 esp National Market System (NMS) clear

- 5. Gen based SROs (Nat Sec Exchs, NASD, regtd clear ags, Municipal Sec Rulemaking Board 75)

- 6. Reg NMS (Order Protection Rule (OPR), Access Rule, Sub-Penny Rule & Market data Rule)

NSEs <http://www.sec.gov/rules/sro.shtml>

4. BROKER DEALER REGULATION *s15 <http://www.sec.gov/divisions/marketreg/bdguide.htm>

- SIPC 1. Register with SEC (Form BD) and join SRO (s15b) (bank brokerage ss 3(a)(4)(B) and 3(a)(5)(C))

<http://www.sec.gov/answers/regis33.htm>

- 2. Broker (business effecting transactions in sec for the account off others s3(a)(4)(A))

- 3. Dealer (business buying & selling sec own account through broker or otherwise s 3(a)(5)(A))

US Securities Laws

4. **Sec futures regulated SEC and CFTC**
5. **Antifraud Provisions (ss 9(a) (man price), 10(b) (MDDs) and 15(c)(1) and (2) (govt sec BDs)**

5. **USE MANIPULATIVE AND DECEPTIVE DEVICES** s 10b and Rule 10b-5 (17 CFR) 240 10b-5) (SEC lawyers Boston Regional Office 1942 president issue negative statements & purchase stock ss10(b),17))

1. **Liability** (1) *s11 SA Misstatements and omissions registration file SEC
***Implied private right action (2) *s12(c)(2) SA Material untrue statement prospectus or oral
RICO Statute 1974 (3) s17 SA SEC (fraudulent interstate transactions)
(pattern of violations (4) s20 SEA 'Controlling persons' (office, director, sig shareholder)
triple damages) (5) Blue Sky Laws Common law fraud and negligent misrepresentation
2. **Conditions** 'any untrue statement of a material fact' or omission
Limitation 1 yr discovery and max 3 years (a) To employ 'any device, scheme or artifice to defraud'
(c) To make any untrue statement of material facts or material omission
(c) To engage in any act, practice course of business which operates as fraud or deceit
- Not underprice* (1) Manipulation or deception No qu fairness *Santa Fe Industries v Green* (1977)
(2) Materiality Nec each disclosure or non-disclosure material
(3) Connection Nec relate 'purchase or sale'
(4) Knowledge or 'Scienter' Intention or knowledge
'intent to deceive, manipulate or defraud' *Ernst & Ernst v Hochfelder* [1976] and Recklessness
Possibly 'Fraud on Market' with reliance market price & multiple suits *Basic Inc v Levinson* (1988)
- Private Party (5) Standing Necessary purchasers or sellers *Blue Chip Stamps v Manor Drugs* (1975)
Basic v Levinson (6) Reliance (or omission) Fraud on Market Theory of Reliance. Due diligence
Levinson 1988 (7) Loss and Causation Nec plead 'fraud with particularity' FRCP Rule 9b
(8) Damages (defences in pari delicto, laches and waiver) *Limitation 1 year loss*
3. Insider trading unclear with SEC 'Equal Access Theory' but strict theory rejected by Supreme Court *Chiarella v US* (1980) (no duty to disclose information if no fiduciary duty) but support 'Misappropriation theory' in *US v OHagan* (1997) (duty to disclose or abstain if misappropriate confidential information). SEC allow 'information barriers' or Chinese walls (refer training, trading restrictions, physical barriers, isolation depts and limits prop trading).
- [GF] 4. Euro 'Due diligence defence' & letter ss 11/12(a)(2) (request Issuers and Managers lawyer)
(1) s 11SA (after reasonable investigation reasonable ground no misstatement omission) *Sanders v John Nuveen* (1980); *Quincy Coop Bank v AG Edwards* (1986); *Elfenbein v American Financial Corp* (1980); *University Hill Foundation v Goldman Sachs* (1976)
(2) s 12(a)(2) SA (not know and could not have known after exercise reasonable care) *In re Software Toolworks Inc Securities Litigation* (1994); *In re International Rectifier Securities Litigation* (1987); *Phillips v Kidder Peabody* (1996); *In re WorldCom* (2004)
5. **Alternative Remedies and Secondary Liability**

6. **US INSIDER TRADING**

<http://www.sec.gov/answers/insider.htm>

1. s15 SA (fraud) and s16b SEA (short swing profits >10% co stock) and s 10b (fraud trading)
2. SED Reg FD (Fair Disclosure simultaneous disclosure by co of material non-public infomatn)
- 15-20% 3. Williams Act 1968 amdts SEA (disclose info on cash tender offers replace proxy campaigns)
- x3 prof 4. Insider Trading Sanctions Act 1984 and In Tr and Securities Fraud Enforcement Act 1988
- or loss 5. Sig contribution SC *SEC v. Texas Gulf Sulphur Co* (1966) (disclose or refrain trading); *Strong v. Repide* (1909) (director not use info acquire shares; *Dirks v. SEC* (1984) (tippee liable if tipper breach fid duty, *SEC v Materia* (1984) (proofreader liable IT under misappropriation theory); *US v Carpenter* (1986) (info supplied by journalist R Foster Winans WSJ); *US v O'Hagan* (1997) (lawyer for Grand Metropolitan buy shares Pillsbury \$4.3m as no fid duty under misappropriation confidential info theory)

Control' 1965

7. **CORPORATE CONTROL & RESTRUCTURING**

HG Manne, 'Mergers and the Market for Corporate

1. No poss restructuring practices and strategies with no responses defences
- s13e-3 2. Going Private ss10b and 13e-3 (fraud) and 4 <http://www.sec.gov/answers/gopriv.htm>
- s14b 3. Proxy Contests <http://www.wlrk.com/webdocs/wlrknew/AttorneyPubs/WLRK.22925.13.pdf>
- s13d 4. Hostile Tender Offer s13d(1) (if acquire >5% disclose info 10 days under Sch 13D)
5. Hart Scott Rodino Antitrust Improvements Act 1976 (pre-acquisition disclosure) 99 SEC amdts

8. **SEC ENFORCEMENT AND EXTRATERRITORIALITY**

<http://www.sec.gov/litigation.shtml>

1. Sig powers but 90% SEC actions settle under 'Consent Negotiation Process' (Issues subpoena, parallel proceedings, penalties (CDOs, MPs, RSOs), injunctions, limitations)
2. Division of Corporation Finance poss issue No-Action, Interpretive and Exemptive Letters <http://www.sec.gov/divisions/corpfin/cf-noaction.shtml>
3. US securities laws applies extraterritoriality to offers or sales to US persons outside the US where a 'jurisdictional means' is established such as use of US mail or telephone systems *Morrison v Nat Austraila Bank* [2008] *Sec Cir dismiss lack subject matter jurisdiction Apply narrow 'transactional' test rather than earlier 'conduct and effects' test 10(b)*

PROF G A WALKER