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TechnoLiability: Corporate Websites, Hyperlinks, and Rule 10(b)-5

Mason Miller

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* J.D. Candidate, Washington and Lee University, 2001; B.S., Communication Studies, Northwestern University, 1998. The author wishes to thank Professor Lyman Johnson and everyone else who contributed to the development of this Note.

Ever think the day would come when the Internet and your phone worked as one to expand communications beyond all boundaries?[1]

I. Introduction – The Rise of the Internet Empire

In the new economy information age, the ability to capture and utilize the means of communication as a capital resource could mean the difference between a profitable and a bankrupt business enterprise.[2] More than any other commercial activity, securities trading has recognized the potential opportunities this information revolution creates.[3] This revolution has had two effects: the growth of corporate websites for the dissemination of information to the public,[4] and the increased reliance by the public on the Internet as a means of information gathering and financial research.[5] Concurrent with this growth has emerged the need to develop a regulatory structure adapted to the intricacies of the Internet as it relates to securities laws.[6] This Note addresses the

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1. INC. THE MAGAZINE FOR GROWING COMPANIES, Feb. 2000, at 34 (quoting advertisement for Vstream.com).

2. *See* Brett Duval Fromson, *Where the Next Fortunes Will Be Made; The Secret Is Spotting a Major Trend and Then Climbing Aboard at Just the Right Moment*, FORTUNE, Dec. 5, 1988, at 185 (discussing value of information communication to emerging companies).

3. *See* Robert A. Prentice, *The Future of Corporate Disclosure: The Internet, Securities Fraud, and Rule 10b-5*, 47 EMORY L.J. 1, 2 (1998) (discussing growth of Internet as medium of communication for financial information). *See generally* Robert A. Robertson, *Personal Investing in Cyberspace and the Federal Securities Laws*, 23 SEC. REG. L.J. 347 (1996) (outlining effect of Internet on personal investment decisions and Securities and Exchange Commission's (SEC) reaction to such changes); Lourdes Gonzalez & Diane Mage Roberts, *Internet-Based and Other Online Trading Systems*, INSIGHTS, July 1997, at 8 (discussing development of Internet capable trading systems and needed protections for such transactional systems); John C. Wilcox, *Electronic Communication and Proxy Voting: The Governance Implications of Shareholders in Cyberspace*, INSIGHTS, Mar. 1997, at 8 (noting SEC aggressiveness in promoting use of Internet as tool for financial markets).

4. *See infra* notes 15-21 and accompanying text (discussing growth of websites run by publicly traded corporations).

5. *See infra* notes 22-29 and accompanying text (noting development of Internet as research medium for public).

6. *See generally* David M. Cielusniak, Note, *You Cannot Fight What You Cannot See: Securities Regulation on the Internet*, 22 FORDHAM INT'L L.J. 612, 613-14 (1998) (discussing possibility of securities fraud on Internet and regulatory challenges posed by such fraud); Karen Donovan, *The Web: A Valid Proxy for Proxy-Fight Notices?*, NAT'L L.J., Jan. 29, 1996, at B1 (discussing SEC regulation of proxy contests on Internet in context of RJR Nabisco case); Andrew Kandel, *Securities Fraud and the Internet: How New York Regulators Are Keeping Up*, WALLSTREETLAWYER.COM, Jan. 1998, at 8 (explaining how Internet presents unique risk of fraudulent securities marketing). *But see* Joseph F. Cella III & John Reed Stark, *SEC Enforcement and the Internet: Meeting the Challenge of the Next Millennium – A Program for the Eagle and the Internet*, 52 BUS. LAW. 815, 835 (1997) (arguing that current SEC regulations

potential liability under Rule 10b-5[7] facing companies that operate webpages with hyperlinks[8] to analyst reports that contain inaccurate or misleading information.[9]

Part I of this Note discusses the growth of the Internet as a tool of financial information delivery by companies and the increasing reliance by the public on the Internet as a means of gathering such information.[10] Part II of this Note provides a background to Rule 10b-5 and analyzes its potential application to a corporate website with a hyperlink to an analyst report containing misleading information.[11] Part III then gives policy arguments in support of extending 10b-5 liability to the aforementioned situation.[12] Part IV of this Note outlines potential strategies through which a company may avoid such liability yet maintain hyperlinks to analyst reports through the use of disclaimers and staleness provisions.[13] Finally, Part V of this Note concludes that successful regulation must balance the interests of both investors and corporations.[14]

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can be adapted to Internet without development of new regulatory structure). However, even Cella and Stark recognized the need for the SEC to address seriously the changes the Internet poses to securities regulation, writing:

> The synergy created by the joining of the Internet with global capital markets creates an ever-changing and developing investment emporium which has not only changed the way the players think but also the way the scofflaws think. Above all, the [SEC] must position itself to respond quickly to the concerns of the investing public while also considering the mores of the Internet community.

Id. at 847.

7. *See infra* notes 66-75 and accompanying text (analyzing Rule 10b-5 and its potential application to corporate websites).

8. *See* JOHN R. HEWITT & JAMES B. CARLSON, SECURITIES PRACTICE AND ELECTRONIC TECHNOLOGY § 4.03[2][c] (1998) (explaining use of hyperlink as device through which one website can be connected to another). A hyperlink allows a user to navigate easily between different websites without initiating a new search and beginning at a fresh page. *Id.*

9. *See infra* notes 42-47 and discussion (describing meaning of misleading information in context of Rule 10b-5).

10. *See infra* notes 16-29 and accompanying text (discussing growth of Internet and use as financial tool).

11. *See infra* notes 30-75 and accompanying text (analyzing application of Rule 10b-5 to hyperlink from corporate website to analyst report).

12. *See infra* notes 76-104 and accompanying text (outlining policy arguments in favor of application of Rule 10b-5 to corporate hyperlink to analyst report).

13. *See infra* notes 105-185 and accompanying text (providing potential strategies to avoid liability for hyperlinks from company website to analyst report).

14. *See infra* notes 186-201 and accompanying text (discussing proper regulatory balance for corporate websites).

A. *The Growth of the Corporate Website*

Corporations are rapidly expanding the use of the Internet as a means to fulfill SEC disclosure requirements and otherwise to disseminate financial information to the public.[15] The use of a company webpage as a means of communication to the public arguably creates enormous savings in contrast to paper-based mailings and distribution.[16] In June 1993 the entire world wide web consisted of only 130 websites.[17] Three years later, the total number of webpages had grown to over 650,000, and this number continues to rise exponentially.[18]

A large proportion of the Internet now is dominated by corporate home pages.[19] Today, according to the National Investor Relations Institute, approximately ninety percent of all publicly traded companies in the United States have launched their own corporate websites.[20] Practitioners have published manuals instructing attorneys on how to create a home page for their corporate clients.[21] How many of these corporate websites are being accessed by the public for the purposes of gathering financial information concerning potential investment decisions remains a question.

B. *The Internet and the Public*

Even more striking than the increasing use of the Internet by corporations is the growing reliance on the Internet as a means of financial research by the public.[22] Moreover, recent research indicates that by 2001 there will be

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15. *See* Prentice, *supra* note 3, at 2-3 (discussing growth of corporate website usage); Gloria Santona, *More Corporations Using 'Net to Reach Investors*, NAT'L L.J., July 14, 1997, at B16 (detailing use of Internet by corporations as tool of communication to reach potential investors).

16. *See* Santona, *supra* note 15, at B16 (noting that several companies already have distributed their annual reports electronically and others have used Internet as means of distributing proxy materials).

17. Clifford Lynch, *Searching the Internet*, SCI. AM., Mar. 1997, at 52, 53.

18. *Id.* at 53.

19. *See* Simon Petravick & John Gillett, *Financial Reporting on the World Wide Web*, MGMT. ACCT., July 1996, at 26 (noting that by May 1996, 69% of Fortune 150 companies had websites).

20. *See Proactive Corporate Practices Recommended by ABA Panelists*, Sec. Reg. & L. Rep. (BNA), 1113-14 (Aug. 20, 1999) (noting increase in number of corporate websites and arguing that corporate counsel should carefully scrutinize information on corporate homepages). *See generally* Paul Davies, *Huge Growth in Net Forecast; Business Leaders Expect High Cost to Fall, Survey Says*, ARIZ. REPUBLIC, Apr. 12, 1997, at E9 (projecting rapid growth in use of Internet by corporations).

21. *See* HEWITT & CARLSON, *supra* note 8, § 4 (providing instruction on construction and maintenance of simple web page).

22. *See* Alexander C. Gavis, *The Offering and Distribution of Securities in Cyberspace:*

approximately 9.3 million investment accounts handled directly over the Internet.[23] In pursuit of these members of the online investing public, over 150 brokerages are now available on the Internet.[24]

The public attraction to online investing is enormous. Internet investors have the opportunity to receive access to free and inexpensive investment information.[25] Moreover, investing on the Internet provides the public lower transaction costs than traditional brokers,[26] twenty-four hour access to account information,[27] and portfolio tracking services.[28] Given these two trends, the growth of the number of Internet users combined with the expanding number of corporate home pages, it is clear that the regulation of corporate disclosure policies over the Internet will become increasingly important.[29]

II. The Traditional Duty to Correct Misleading Statements

A. Background to Rule 10b-5 and SEC Anti-Fraud Regulation

The primary mechanism used by the SEC to regulate fraud with respect to informal (or "soft") communications between a company and the public is Rule 10b-5.[30] Promulgated in 1942, Rule 10b-5 mirrors Section 17(a) of the

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A Review of Regulatory and Industry Initiatives, 52 BUS. LAW. 317, 319-20 (1996) (describing growing number of personal computer (PC) owners and Internet users worldwide). *But see* CLIFFORD STOLL, SILICON SNAKE OIL 16-17 (1995) (arguing that total number of Internet users in United States is exaggerated).

23. *See* Christina K. McGlosson, Comment, *Who Needs Wall Street? The Dilemma of Regulating Securities Trading in Cyberspace*, 5 COMMLAW CONSPECTUS 305, 312 (1997) (quoting Forrester Research estimates concerning number of online investment accounts in 2001); *see also* Cielusniak, *supra* note 6, at 617 (estimating total number of online investment accounts in 2001 to be twenty million).

24. Ahmad Diba, *They Want You Wired*, FORTUNE, Dec. 20, 1999, at 113 (discussing pursuit of online investors by numerous online Internet brokers).

25. *See* Leah Nathans Spiro & Linda Himelstein, *With the World Wide Web, Who Needs Wall Street?*, BUS. WEEK, Apr. 29, 1996, at 120 (discussing various benefits of online account maintenance); *The Web's Plethora of Information and Services Means Financial Planning in No Longer a Spectator Sport*, FORTUNE, Dec. 1, 1999, at 236 (noting that Yahoo.com and Excite.com provide free links to over 1,400 subcategories of financial information and reports).

26. *See* Spiro & Himelstein, *supra* note 25, at 120 (discussing value of lower commission costs to active traders and total savings affecting portfolios).

27. *See id.*; Daniel Spulber, *Clock Wise: Customer Convenience is the Key to Ecommerce*, BUSINESS 2.0, Mar. 2000, at 214 ("Ameritrade and E*Trade connect investors to markets for financial assets. . . . By adding convenience, companies engaged in electronic commerce stand to earn returns from speeding up transactions.").

28. *Id.*

29. *See supra* note 6 (discussing problems with securities regulation in Internet environment).

30. Employment of Manipulative and Deceptive Devices, 17 C.F.R. § 240.10b-5 (1999). Rule 10b-5 states:

1933 Act[31] except that Rule 10b-5 extends to misstatements occurring in connection with either "a purchase or sale of any security," while Section 17(a) of the 1933 Act focuses only on fraudulent sales or offers to sell.[32] The SEC has utilized the broad language contained in Rule 10b-5 in a variety of antifraud contexts.[33] Moreover, the Supreme Court has recognized a private right of action implied within Rule 10b-5.[34] Although limited in scope in recent years, the Rule 10b-5 implied remedy remains a powerful tool for class-action suits against public corporations.[35]

To sustain a viable 10b-5 claim, a plaintiff must show fraud or deceit, which requires proving that the defendant acted with scienter[36] in connection

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> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
> (a) to employ any device, scheme, or artifice to defraud,
> (b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
> (c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
> in connection with the purchase or sale of any security.

Id.

31. Securities Act of 1933 § 17(a), 15 U.S.C. § 77k (1994).

32. *See id.* (stating that "any person acquiring such security" has cause of action for untrue statements of material fact contained in registration statement).

33. *See generally* Primary Care Investors, Seven v. PHP Healthcare Corp., 986 F.2d 1208 (8th Cir. 1993) (finding 10b-5 violation could be based on nondisclosure of planned public offering but holding no violation occurred in case due to plaintiff's inability to show right to convert company interests into common stock upon offering); Elkind v. Liggett & Myers, Inc., 635 F.2d 156 (2d Cir. 1980) (applying Rule 10b-5 to allegations of insider trading); Drachman v. Harvey, 453 F.2d 722 (2d Cir. 1971) (utilizing 10b-5 as basis for liability in corporate mismanagement context where fraud is also found in underlying securities transaction).

34. *See* Superintendent of Ins. v. Bankers Life & Cas. Co., 404 U.S. 6, 10 (1971) (concluding that 10b-5 offers protection for petitioner corporation, when corporation was defrauded by illegal sale of securities owned by corporation).

35. *See generally* Santa Fe Indus., Inc. v. Green, 430 U.S. 462 (1977) (requiring in class action that alleged conduct be deceptive); Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976) (concluding in class action that more than mere negligence is required to sustain 10b-5 claim); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975) (stating that class action plaintiffs bringing 10b-5 claim must be either purchasers or sellers of securities in question).

36. *See Hochfelder*, 425 U.S. at 201 (concluding 10b-5 addresses practices "that involve some element of scienter"); *see also In re* Wells Fargo Sec. Litig., 12 F.3d 922, 931 (9th Cir. 1993) (finding plaintiffs must show that defendant "knew or recklessly ignored that its challenged statements were misleading"); Breard v. Sachnoff & Weaver, Ltd., 941 F.2d 142, 144 (2d Cir. 1991) (finding plaintiffs may include allegations of recklessness to support 10b-5 scienter requirement); Backman v. Polaroid Corp., Nos. 89-1171, 89-1172, 1990 WL 3832, at *11-12 (1st Cir. Jan 23, 1990) (concluding recklessness sufficient basis for 10b-5 liability).

with the purchase or sale of any security.[37] Moreover, because Rule 10b-5 requires the establishment of a fraud claim, the plaintiff must prove the elements of common law fraud – reliance,[38] materiality,[39] causation,[40] and damages.[41] The Supreme Court has provided some guidance in their application of these common law requirements to securities litigation.[42] To determine whether a misstatement is material, the courts will examine the types of information that a reasonable investor would deem important in making investment decisions.[43] This inquiry into the materiality of a particular statement is highly dependent upon the specific circumstances of the case and the totality of the information available to the investor in the marketplace.[44] Likewise, courts are reluctant to make any determinations with respect to reliance without careful consideration of the specific facts at hand.[45] However, the Su-

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37. *See Blue Chip Stamps*, 421 U.S. at 730-49 (discussing requirement that plaintiff be purchaser or seller of security in question). The courts have relaxed the strict seller/purchaser requirement to allow individual shareholders in a shareholder derivative suit brought on behalf of a corporation defrauded in connection with its purchase or sale of securities to acquire standing. *See* Frankel v. Slotkin, 984 F.2d 1328, 1332-33 (2d Cir. 1993) (allowing shareholder to maintain derivative action on allegations that corporation fraudulently was induced to sell its equity holdings).

38. *See* List v. Fashion Park, Inc., 340 F.2d 457, 462 (2d Cir. 1965) (noting that "[t]hus, to the requirement that the *individual plaintiff* must have acted upon the fact misrepresented, is added the parallel requirement that a *reasonable man* would also have acted upon the fact misrepresented").

39. *See* Basic Inc. v. Levinson, 485 U.S. 224, 231 (1987) (recognizing incorporation of common law materiality requirement into Rule 10b-5).

40. *See* Wilson v. Ruffa & Hanover, P.C., 844 F.2d 81, 85-6 (2d Cir. 1988) (discussing theory of transaction causation in securities litigation) *vacated sub nom.* Wilson v. Santine Exploration & Drilling Corp, 872 F.2d 1124 (2d Cir. 1989); *In re* Fortune Sys. Sec. Litig., 680 F. Supp. 1360, 1365 (N.D. Cal. 1987) (stating loss causation requires plaintiff to show his damage "is a result of defendant's wrongdoing").

41. *See* Wool v. Tandem Computers Inc., 818 F.2d 1433, 1437 (9th Cir. 1987) (using "out of pocket" rule to measure damages when plaintiff was injured by fraudulent market transactions); Harris v. Union Elec. Co., 787 F.2d 355, 367 (8th Cir. 1986) (determining that measure of damages in securities fraud claim is equivalent to actual damages of plaintiff).

42. Of the traditional common law requirements, only reliance and materiality are relevant to the purpose of this Note. Although the Court has imposed significant limitations upon the elements of causation and damages in the securities context, such developments are outside the scope of the present discussion.

43. *See Basic Inc.*, 485 U.S. at 231-32 (discussing development of Court's materiality jurisprudence). The Court in *Basic Inc.* used the opportunity to apply the materiality test adopted for proxy disclosure in *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438 (1976), to the 10b-5 context. *See supra* note 38 and accompanying text (discussing importance of reliance in 10b-5 claim).

44. *See* Basic Inc. v. Levinson, 485 U.S. 224, 232-41 (1988) (analyzing proper amount of information necessary to maximize investor knowledge and adopting fact specific standard).

45. *See generally* Longden v. Sunderman, 737 F. Supp. 968 (N.D. Tex. 1990) (denying

preme Court has recognized the "fraud on the market" presumption of reliance through which a plaintiff may prove reliance by showing that a misstatement adversely affected the market price of the security involved.[46] If a potential plaintiff is able to meet these basic requirements, a viable 10b-5 claim may be sustained in cases in which a corporation has made or adopted misleading statements.[47]

B. The Duty to Correct Third Party Statements

Although the general rule is that a company is not required to correct misleading third party statements,[48] this duty may exist when the company implicitly adopts the statements of the third party.[49] This duty has arisen most often in relation to analyst reports.[50] When an analyst and his report serve as intermediaries between a company and the public, this implicit adoption may occur in three potential ways.

First, a company may have a duty to correct a misleading report under Rule 10b-5 when the company has distributed the analyst's report with other company materials to the public.[51] In *In re RasterOps Corp. Securities Litigation*,[52] the *RasterOps* court rejected the assertion that the company was merely a distribution medium for the analyst's report. Instead the court concluded that, "RasterOps' attempt to relegate itself to the status of a mailcarrier or glorified delivery boy is unconvincing. By passing out the favorable analyst report,

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summary judgment of 10b-5 claim thus indicating questions of reliance are highly factual); Becher v. Farkas, 717 F. Supp. 1327 (N.D. Ill. 1989) (denying summary judgment on 10b-5 claim for similar reasons).

46. *Basic Inc.*, 485 U.S. at 241-47 (recognizing fraud on market theory as adequate means for plaintiff to prove reliance in 10b-5 action thus satisfying common law requirements for fraud claim).

47. *See* Bentley v. Legent Corp., 849 F. Supp. 429, 431-32 (E.D. Va. 1994) (noting that once projection or prediction is disclosed it must satisfy materiality test if inaccurate).

48. *See* State Teachers Ret. Bd. v. Fluor Corp., 654 F.2d 843, 850 (2d Cir. 1981) (concluding that "[a] company has no duty to correct or verify rumors in the marketplace unless those rumors can be attributed to the company"). The court went on to conclude that a company has no duty to correct rumors once discovered unless failure to so could be considered reckless. *Id.* at 851.

49. *See infra* notes 50-65 and accompanying text (discussing theories upon which adoption of third party statements may be based).

50. *See infra* note 56 and accompanying text (providing detailed discussion of *In re Presstek, Inc.*, Exchange Act Release No. 34-39472, 66 S.E.C. Docket 328, 1997 WL 784548 (S.E.C. Dec. 22, 1997)).

51. *See infra* notes 52-54 and discussion (detailing manner through which distribution can create implied adoption of analyst report by company).

52. [1994-1995 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,467 at 91,193 (N.D. Cal. Oct. 31, 1994).

RasterOps clearly was implying that the company agreed with the forecasts contained in the reports."[53] Other courts have reached similar findings of liability when a company has distributed misleading analyst reports.[54]

Second, courts will find implicit adoption of an analyst report when a company provides information to the analyst or participates in the preparation of the production of the report.[55] The most explicit statement of this "preparation" based liability is found in *In re Presstek, Inc.*,[56] a case in which the chairman of the company reviewed an analyst's report prior to distribution and corrected some of the financial information.[57] However, the chairman left intact and unaltered an overly optimistic projection of per share earnings for 1997.[58] The Commission concluded that the chairman "impliedly repre-

53. *In re* RasterOps Corp. Sec. Litig., [1994-1995 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,467 at 91,195 (N.D. Cal. Oct. 31, 1994). In *RasterOps*, the court considered a 10b-5 claim against the company alleging that officers of the corporation supplied false information to analysts in order to generate reports and then distributed those reports to potential investors. *Id.* The officers had contacted analysts at Donaldson, Lufkin, and Jenrette and told those analysts that the business was strong and the company would reach earnings estimates for fiscal year 1992. *Id.* The officers then obtained draft copies of the analysts' reports and circulated them among potential investors. *Id.* The court found that "[t]he act of circulating the reports amounts to an implied representation that the information in the reports is accurate or reflects the company's views." *Id.* Moreover, the court determined that explicit ratification was not necessary for a finding of liability under Rule 10b-5. *Id.* Thus, the court refused to dismiss RasterOps's motion to dismiss the allegations for failure to state a claim. *Id.*

54. *See, e.g.*, Stack v. Lobo, 903 F. Supp. 1361, 1371 (N.D. Cal. 1995) (discussing requirement of implicit adoption of report as basis for liability); Strassman v. Fresh Choice, Inc., No. C-95-20017 RPA, 1995 WL 743728 at *12 (N.D. Cal. Dec. 7, 1995) (dismissing complaint alleging post-publication ratification of analyst reports when plaintiff failed to show defendant circulated reports); *see also In re* Cypress Semiconductor Sec. Litig., 891 F. Supp. 1369, 1377 (N.D. Cal. 1995) (noting that "[d]istributing analysts' reports to potential investors may, depending on the circumstances, amount to an implied representation that the reports are accurate").

55. *See infra* notes 56-60 and accompanying text (describing preparation of report as basis for implicit adoption of analyst report by company).

56. *See In re* Presstek, Inc., Exchange Act Release No. 34-39472, 66 S.E.C. Docket 328, 1997 WL 784548, at *10 (S.E.C. Dec. 22, 1997) (determining that preparation and editing of analyst reports by company constitutes pre-publication implicit adoption of information in report). In *Presstek*, the Commission considered a 10b-5 claim against the company for the distribution and publication of false and misleading information. *Id.* at *1. Senior management officers at the company reviewed, edited, and distributed an analyst's report that overstated earnings estimates for fiscal year 1997; the Chairman had revised the sales projection for one of Presstek's products but failed to correct sales figures for another product that he knew were incorrect. *Id.* at *2. The Commission concluded that by "providing forecasts that were incorporated into the initial draft PMG report [and] editing the report prior to publication . . . Presstek is liable for the report's material misrepresentations under . . . the entanglement . . . theor[y] . . . and, accordingly, had a duty to correct its material misrepresentations." *Id.* at *10.

57. *Id.* at *7.

58. *Id.*

sented . . . that those he did not revise were accurate"[59] by altering the earnings projections for 1996 but leaving in place the 1997 figures. Despite this potential exposure to liability under Rule 10b-5, vast numbers of companies continue to review and revise analyst reports.[60]

Finally, a court may impose liability when a company is aware of an analyst's report and makes statements indicating a level of comfort with the conclusions of the report.[61] Such liability arises most often when a company expresses the belief that analyst projections are attainable by the company. For example, in *In re Adobe Systems Inc. Securities Litigation*,[62] the chief financial officer answered questions concerning analyst projections of the company's earnings estimates in which he expressed the view that he supported a "consensus estimate of $2.10."[63] The court concluded that such public comments constituted adoption of the analyst's projections and thus could serve as the basis for a private 10b-5 claim.[64]

The aforementioned cases suggest that companies should take special caution when dealing with analyst's reports, especially when communicating such information to the general public. Courts are likely to attribute statements in such reports to the companies themselves, and consequently, the companies will find themselves subject to a duty to correct any misleading information in the reports.[65] This risk of entanglement will become more important as nonverbal acts, such as the act of establishing a link to an analyst's report from a company's website, begin to serve as the basis for implicit adoption.

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59. *Id.* at *10.

60. *See Put Away the Red Pencil*, CFO MAGAZINE, March 1998, at 24 (reporting that "78% of companies review analyst reports for factual accuracy").

61. *See infra* note 62-65 and accompanying text (discussing use of comfortability as basis for implicit adoption of third party statement in analyst report context).

62. 767 F. Supp. 1023 (N.D. Cal. 1991).

63. *See In re* Adobe Sys., Inc. Sec. Litig., 767 F. Supp. 1023, 1027 (N.D. Cal. 1991) (finding that statements indicating comfort with analyst projections constitute implicit adoption of such projections). In *Adobe Systems*, the court considered whether a company, in reaction to a recent stock price decline, could be liable for statements made by a company officer indicating that a lower consensus estimate was supported by the corporation. *Id.* at 1025-26. The court found that the statements, even if cautionary in nature, could still be overly optimistic and misleading. *Id.* at 1028. In doing so, the court rejected the defendant's argument that an overly broad definition of actionable projection statements would chill corporate communication with the general public. *Id.* Thus, the court refused to dismiss the defendant's motion to dismiss the allegation for failure to state a viable 10b-5 claim. *Id.*

64. *Id.*

65. *See generally supra* notes 42-44 (discussing duty to correct misleading statements under Rule 10b-5).

C. Application of Duty to Correct to a Company's Website

When a company links its website to an analyst's report containing misleading information, a court may consider the link itself to be an implicit adoption of the report.[66] The act of creating the connection between the company and the report may serve as a means of distribution of the report, similar to including the report in a mailing of other company materials.[67] Moreover, the link arguably reflects a level of comfort by the company with the information contained in the report.[68] Although litigation concerning this issue has yet to be considered, the SEC has indicated that it views links between different websites as creating a single electronic document.[69] In doing so, the SEC has indicated that Rule 10b-5 is applicable to both traditional, paper-based communication and electronically delivered information.[70]

This duty to correct misleading information may extend to errors not present at the time the company established the link.[71] For example, if a company creates a link to an analyst's site and the analyst subsequently revises his report without informing the company, then the presence of the link itself still may serve as the basis for implied adoption of the statements.[72]

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66. For a general discussion of the concept of implicit adoption of third party statements and a subsequent duty to correct such statements, see J. ROBERT BROWN, JR., THE REGULATION OF CORPORATE DISCLOSURE § 3.04[5] (1999) (discussing duty to update or correct third party statements in context of paper based communications).

67. *See generally* Prentice, *supra* note 3 (drawing comparisons between paper-based and electronic-based communications for purposes of securities regulation); Gavis, *supra* note 22 (discussing corporate distribution of regulated materials through Internet).

68. *See supra* note 61-65 and accompanying text (analyzing comfortability as mechanism of implicit adoption of third party statement).

69. *See* Use of Electronic Media for Delivery Purposes, Exchange Act Release No. 33-7233, 60 S.E.C. Docket 1091, 1995 WL 588462, at *9 (S.E.C. Oct. 6, 1995) (determining, in context of prospectus located on company's website, that "[t]he hyperlink function enables the final prospectus to be viewed directly as if it were packaged in the same envelope as the sales literature"); *see also* Kathleen M. Gibson, *In a Dearth of Disclosure Lies Exposure*, NAT'L L.J., June 24, 1996, at B12 (arguing that technological advances make it more complicated to avoid selective disclosure of corporate information).

70. *See* Exchange Act Release No. 33-7233, at *3 n.11 (determining that "the liability provisions of the federal securities laws apply equally to electronic and paper-based media").

71. *See infra* notes 120-28 and accompanying discussion (analyzing concept of "alive" statements in context of reliance and 10b-5 claims).

72. The meaning of communications within the context of securities regulation extends to more than direct oral or printed materials; it can also include non-verbal conduct and other forms of expression. *See generally* Safe Harbor Rule for Projections, Securities Act Release 6084, 1979 SEC LEXIS 1254, at *21-22 (June 25, 1979) (noting that "the Commission reminded issuers of their responsibility to make full and prompt disclosure. . . where management knows or has reason to know that its earlier statements no longer have a reasonable basis"); BROWN, *supra* note 66, at § 3.03[3] (discussing varied forms of communication regulated in

Each day the link is present constitutes a reaffirmation by the company that the information to which the site is connected is reliable.[73] At least one court has supported a similar finding of a duty to correct with respect to paper-based communications when a company became aware of misleading information subsequent to the adoption of the report.[74]

However, the traditional duty to correct implicitly adopted statements of a third party has been limited to an unchanging paper-based report or presentation.[75] To require a similar duty of companies with respect to an analyst's website would necessitate the introduction of an elevated and continual duty to review the information on the analyst's site to monitor for any changes or new errors. This elevated duty of correction has yet to be addressed by either the SEC or the courts; although the Securities Acts of 1933 and 1934 originally were designed as vehicles for consumer protection, it is unclear how much protection the courts will provide to the public.

III. Justification for a Higher Duty to Correct

A. The Problem of Information Overload

As stated above, the duty to correct implicitly adopted statements of a third party has, so far, been limited to an unchanging paper-based report or presentation. To elevate this duty based solely upon the fact that a particular communication was made through electronic media rather than through more traditional forms would seem to create an unfair disparity in regulation. However, given the unique capabilities of the Internet to provide enormous amounts of information quickly, the courts should adopt this duty in order to promote informed decisionmaking by the public concerning investment decisions.[76]

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securities context). The SEC believes there is a duty to correct, noting:

> [I]f the statements either have become inaccurate by virtue of subsequent events, or are later discovered to have been false and misleading from the outset, and the issuer knows or should know that persons are continuing to rely on all or any material portion of the statements.

Id. at *22.

73. This re-affirmation of the credibility of a particular source of communication may derive support from the "comfortability" theory of implicit adoption. *See supra* notes 62-65 and accompanying text (discussing comfortability in context of implicit adoption).

74. *See* Backman v. Polaroid Corp., Nos. 89-1171, 89-1172, 1990 WL 3832, at *9 (1st Cir. 1990) (concluding that when subsequent events make previous statement or communication misleading company has duty to correct information (citing Greenfield v. Heublin, Inc., 742 F.2d 751, 758 (3d Cir. 1984))).

75. *See generally* Cella & Stark, *supra* note 6 (discussing application of traditional SEC regulation to emerging forms of communication).

76. *See generally* Donald C. Langevoort, *Information Technology and the Structure of Securities Regulation*, 98 HARV. L. REV. 747 (1985) (analyzing changing role of SEC in modern

The federal securities laws concerning disclosure of corporate information initially were designed in order to combat the problem of limited information;[77] investors typically were defrauded or misled because access to information concerning a potential investment was limited.[78] In the aftermath of the stock market crash of 1929 and the Great Depression, congressional concerns with the myriad of problems emanating from insiders taking advantage of non-public information led to the passage of the Securities Act of 1934 and the adoption of its open disclosure philosophy.[79]

The Internet poses the opposite problem in that the speed and information to which an individual has access is enormous. This may result in more impulse decisionmaking as investors have the ability to review a company, to read analyst reports, and to purchase stock in a company all within one quick

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information-based economy); Robertson, *supra* note 3 (discussing effect of technology on personal investment decisions and SEC reaction); Christopher Sharples, *Policing Cyber-Fraud on the World Wide Web*, DAILY TELEGRAPH, Mar. 24, 1997, at 25 (discussing Internet and effect on securities regulation); Spulber, *supra* note 27, at 214 (arguing that "[w]hether at work, at home, or on the road, electronic communications promise substantial time savings").

77. *See* Gavis, *supra* note 22, at 323 (discussing development of SEC regulations and Congressional modification of regulations).

78. *See generally* LOUIS D. BRANDEIS, OTHER PEOPLE'S MONEY AND HOW THE BANKERS USE IT 92 (1914) (discussing role of disclosure as means to combat insider trading); *see also* Ted Smith, *Congress Must First Learn to Surf the Internet, If It Ever Hopes to Catch the Next Wave of Securities Fraud*, 17 J. MARSHALL J. COMPUTER & INFO. L. 589, 590-91 (1999). Smith argued that the impact of fraudulent information threatens market stability, noting that:

> One risk that an investor faces when deciding to allocate funds to a particular investment is the integrity of the opportunity. If integrity is lacking in the investment and it turns out to be a sham, the investor may lose his entire investment. Securities fraud is an issue that has plagued the SEC since its inception. Securities fraud not only causes financial hardships on those caught up in the fraud, but it also jeopardizes the integrity of the entire securities market. History has proven that incidents of securities fraud are more prevalent when there is an increase in the popularity of securities trading. . . . [T]he Internet makes the opportunities to perpetuate securities fraud more complex and tougher to police than ever before.

Id.

79. *See* H.R. REP. NO. 73-1383, at 11 (1934) (discussing value of information to public investors). The Report noted that:

> No investor, no speculator, can safely buy and sell securities . . . without having an intelligent basis for forming his judgment as to the value of the securities he buys and sells. The idea of a free and open public market is built upon the theory that competing judgments of buyers and sellers as to the fair price of the security brings about a situation where the market price reflects as nearly as possible a just price. Just as artificial manipulation tends to upset the true function of an open market, so the hiding and secreting of important information obstructs the operations of the markets as indices of real value. There cannot be honest markets without honest publicity.

Id.

session on the Internet.[80] Courts often have interpreted the disclosure philosophy of the 1934 Act as a remedy to this problem.[81] In *TSC Industries, Inc. v. Northway, Inc.*,[82] the Supreme Court, in addressing the correct standard for materiality in an action under §14-a-9, expressed concern for the problem of information overload.[83] Specifically, the Court noted that "[s]ome information is of such dubious significance that insistence on its disclosure may accomplish more harm than good . . . . [M]anagement's fear of exposing itself to substantial liability may cause it simply to bury the shareholders in an avalanche of trivial information – a result that is hardly conducive to informed decisionmaking."[84] To reduce the potential of this occurring, which results from the Internet's capability to deliver high-speed research materials, courts

80. *See The Web's Plethora of Information*, *supra* note 25, at 236 ("[T]he Internet has rapidly become capitalism's great equalizer . . . . Of course, speed and access to reams of information can't make up for bad judgment."); Robert Reid, *The Impulse Economy*, BUSINESS 2.0, Mar. 2000, at 284 (arguing that "[t]he tight link between the call to action and the response within the Impulse Economy, coupled with the Web's unique auditability, gives marketers more powerful insight into the efficacy of their campaigns than they ever dreamed possible"). *See generally* Gina Imperato, *Report from the Future: The Money Value of Time*, FAST COMPANY, Jan./Feb. 2000, at 40 (arguing that Internet provides new premium for value of time). Imperato argued that:

> We all understand, instinctively, the timeless logic behind the "time value of money" – that a dollar received today is worth more than a dollar received a year from now. But the new world of business requires an instinctive appreciation of a different logic as well. Think of it as the "money value of time." Cutting-edge people and companies rethinking the nature of their relationship with time. To them, time is every bit as tangible, every bit as measurable, and every bit as valuable as money.

Id.

81. *See generally* BROWN, *supra* note 66 (analyzing disclosure requirements under federal securities laws and courts interpretations of such regulations).

82. 426 U.S. 438 (1976).

83. TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 448-49 (1976). In *TSC Industries*, the Court considered a 14a-9 claim alleging that a proxy statement submitted to shareholders concerning a proposed merger was incomplete and materially misleading. *Id.* at 441. The complaint alleged, among other claims, that TSC had failed to disclose that the purchaser of the company, National Industries, Inc., was the "parent" company of TSC and that members of TSC's board of directors were also officers of National Industries, Inc. *Id.* at 451. The Court concluded that such omissions were not misleading because the additional facts were not necessary to determine that National Industries was intertwined with TSC prior to the merger. *Id.* at 452-53. However, in doing so, the Court provided the modern test for what will be deemed material by stating that "[a]n omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote." *Id.* at 449. The Court constructed this test with recognition of the fact that a lower standard of materiality might encourage companies to disclose too much information to investors, thus leading to the problem of information overload. *Id.* at 448-49.

84. *Id.*

should encourage companies to review information more carefully. Although the public may still find themselves making impulse stock purchases based on overwhelming amounts of materials, requiring that companies review this information on a continuous basis for errors or misstatements may reduce the pitfalls of impulsive stock purchasing.

B. Deterrence of Link-Shopping

Often, the number of links and visitors to the site determines the credibility or "value" of a website.[85] For example, many sites utilize "counter" software to reflect the total number of "hits" (visits) received; companies that market such software have seen demand for their products explode with the growth of the Internet.[86] Websites featuring analyst's reports are not immune from this method of valuation; many of the on-line brokerage companies, such as E-Trade and Ameritrade, attempt to differentiate themselves based upon the depth and scope of their research and analyst materials.[87] Because of the close relationship between analysts and company officers, analysts have an economic incentive to report positively on a company's outlook in order to encourage that company to link to their site.[88] As a result, the total amount of traffic to the site increases.[89] However, this incentive may have the effect of distorting the validity of the information contained in such reports; a process of "link-shopping" may overcome an analyst's neutrality in his or her assessment of a company's prospects for future growth.[90] In order to deter link-

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85. *See* Cella & Stark, *supra* note 6, at 822 (discussing use of hyperlinks as mechanism for improving perceived validity of fraudulent website). By the term "link-shopping," this Note refers to the process of improving a site's value and credibility by increasing the total number of visits; this can be accomplished by establishing as many access points to the site as possible. If each hyperlink constitutes a different access point, sites have an incentive to increase the total number available and thus will cater to those who can provide such hyperlinks.

86. *See* Smith, *supra* note 78, at 609-10 (explaining that "[h]yperlinks are the essence of the Internet system and the validity of a website is often determined by the extent to which it is hyperlinked").

87. *See* Diba, *supra* note 24, at 113 (discussing access to institutional research as differentiating factor among competing online brokers).

88. *See* Roger J. Dennis, *Materiality and the Efficient Capital Market Model: A Recipe for the Total Mix*, 25 WM. & MARY L. REV. 373, 414 (1984) (arguing that relationship between management and analysts necessarily is close and should be encouraged by regulatory structure).

89. *See* Langevoort, *supra* note 76, at 779 (discussing interaction between analysts and corporate officers and incentive of analysts to maintain cordial relationships with such officers).

90. *See* Wielgos v. Commonwealth Edison Co., 892 F.2d 509, 518 (7th Cir. 1989) (concluding that "[i]ssuers and underwriters must decide what information will be useful without burying investors under a blizzard of paper . . . . No investor absorbs sheafs of dense type. . . . They require absorption by professional traders and investors"). The role of analyst reports in transforming the volume of corporate information into digestible materials in the securities markets cannot be understated.

shopping by analysts, courts should require companies to review the contents of analyst reports. Such action would eliminate the incentive of analysts to inflate their projections in order to garner more links to their site.

C. The Products Liability Rationale

The Internet has provided a quick, efficient, and economical way for companies to distribute information to the public, much like mass production reduced the cost of business for manufacturers.[91] In the modern information age, knowledge and data are often the most valuable commodities to a company, regardless of its size.[92] Products liability law has evolved to place the burden and risk of error on the manufacturer because the manufacturer gains the most from the use of the supply chain.[93] Likewise, courts should impose a similar risk and burden on companies that choose to distribute information through the Internet "supply" chain.[94]

The seminal case that expounded the policy rationale for strict liability in tort is *Escola v. Coca Cola Bottling Co.*[95] In that case, a waitress was injured when a Coca Cola bottle broke in her hand.[96] In a concurring opinion,

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91. *See* John C. Coffee, Jr., *Brave New World?: The Impact(s) of the Internet on Modern Securities Regulation*, 52 BUS. LAW. 1195, 1195 (1997) (noting that increase in total Internet users has reached between thirty and sixty million worldwide and likely will continue to grow). Coffee argued that concurrent with the growth of the number of Internet users is a reduction in the number of filtration channels, writing:

> Earlier technological innovations (such as the telephone) seem to have assisted the issuer more than the investor, allowing the former to target the latter. In contrast, while the Internet may assist the prospective issuer to access the market, it does even more to enable the investor to obtain significantly more information without filtration by brokers or other securities professionals who may have a self-interest in promoting transactions.... [Investors] can also engage in new non-linear browsing strategies through hyperlink features that connect related materials.

Id. at 1197.

92. *See* Fromson, *supra* note 2, at 185 (recognizing that industries in which knowledge represents largest input to production, rather than labor, dominate economy).

93. *See infra* notes 95-98 and accompanying text (discussing evolution of strict liability in tort).

94. *See* Gavis, *supra* note 22, at 321 (noting that "[c]oncurrent with corporate America's realization that the Internet provides a new distribution channel for communicating with the public, financial service industries . . . have all begun to incorporate the Internet into their strategic plans.... [T]he Internet presents an entirely new mechanism for the interaction of these entities with the public"). The value of the Internet to small companies for the distribution of information cannot be understated.

95. 150 P.2d 436 (Cal. 1944).

96. *See* Escola v. Coca Cola Bottling Co., 150 P.2d 436, 437 (Cal. 1944). In *Escola*, a waitress brought suit against the bottling company of a beverage which had exploded in her hand. *Id.* at 437. A majority of the court provided recovery for the plaintiff based on the theory of res ispa loquitor. *Id.* at 440. Justice Traynor, writing separately, would have allowed the

Justice Traynor concluded that manufacturers should be strictly liable for injuries resulting from products they had placed into the stream of commerce.[97] The comments to the *Restatement (Second) of Torts* Section 402A echo a similar policy rationale, explaining that "the justification for the strict liability has been said to be that . . . public policy demands that the burden of accidental injuries caused by products intended for consumption be placed upon those who market them, and be treated as a cost of production."[98]

The Internet serves as a similar stream of commerce for companies wishing to market information. By placing a hyperlink on one site to another, a company directs public consumption towards the information contained on the second site. In other securities contexts the SEC has recognized that a corporation implicitly can represent an analyst's report as reliable.[99] The use of a link to a report serves as tangible evidence of this representation. Borrowing from products liability jurisprudence, courts may find that this link, insofar as it provides economic benefits to the company, also should serve as a source of liability to be treated as a cost of production.

D. *The Decline of Intermediary Information Filters*

Traditionally, the public could evaluate information based upon the ease of access to it.[100] For example, the public would likely consider information in the *New York Times* more reliable than contradictory information published in more politically radical journals simply because the *New York Times* reached a larger audience. However, the Internet has radically destabilized this "hegemonic" domination of information providers.[101] To the average investor, the majority of websites are similar.[102] There is no intermediary to adequately

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plaintiff to recover by holding the defendant strictly liable in tort, based upon the inherent dangers to consumers and the benefits provided to manufacturers by automation. *Id.* at 443 (Traynor, J., concurring).

97. *Id.* (Traynor, J., concurring).

98. RESTATEMENT (SECOND) OF TORTS § 402A cmt. c (1987).

99. *See supra* notes 51-54 and accompanying text (discussing implicit adoption of analyst reports by distribution).

100. *See* Dennis, *supra* note 88, at 414 (discussing effect analysts, especially prominent ones, can have on price of security in secondary market).

101. *See* Cielusniak, *supra* note 6, at 626-27 (discussing concept of anonymity on Internet as means by which fraudulent traders may manipulate public access to information).

102. *Id.* at 628. Cielusniak contended that because investors cannot adequately distinguish between professional and amateur websites, combined with the speed of information delivery, there exists a high potential for Internet-based fraud, arguing that the Internet is "the modernized version of the boiler room." *Id.* Cielusniak argued that:

> Although investors can use the Internet as a place for obtaining information, advice, and opportunities, it has also become a new medium for fraud. By some estimates, Internet investors are defrauded of over U.S. $100 million per year. For a variety

evaluate the information on an analyst's webpage; one website may seem just as credible as another, especially when the topic is complex economic evaluations of a company.

Although the analyst's employer often serves as a gauge of the report's credibility, this gauge has less value to the average investor.[103] The majority of the public pauses only briefly to see who wrote a report, and instead hurries to the conclusion page to discover the analyst's recommendation.[104] Thus, because the potential for fraudulent information conveyance is great, courts should protect the public from the lack of a hegemonic information filter by creating incentives for companies to evaluate data on sites to which they link.

IV. Avoiding HyperLiability: Strategies for Corporate Counsel

Given the possibility that courts may find a company liable for fraud under Rule 10b-5 when its website contains a link to a misleading or incorrect analyst report, one obvious solution to liability would be to avoid establishing the hyperlink altogether. However, such a blanket prohibition may hinder the development of the Internet as a tool for companies to disseminate information to the public. By hyperlinking an analyst's report, a company may gain numerous advantages. First, hyperlinking offers small companies the opportunity to attract potential investors at a low cost of information delivery by supplanting the need for costly paper-based mailings.[105] Second, it provides a mechanism for companies to capitalize on the quick decisionmaking process of investors by encouraging them to read the analyst reports and then immediately purchase shares of the company.[106] Finally, it provides corporations a streamlined

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> of reasons, the Internet provides an ideal setting for fraud. The cost of setting up an Internet webpage is decreasing, as is the cost for an investor to access the Internet. Both of these aspects, together, lower the barriers to entry, and the Internet becomes a much less expensive way for scam artists to find victims than by using traditional techniques such as mass mailing and cold-calling.

Id. at 627-28.

103. *See* Kevin Mason, Comment, *Securities Fraud on the Internet: The Flies in the Ointment and a Hope of Fly Paper*, 30 CASE W. RES. J. INT'L L. 489, 498 (1998) (discussing value of anonymity on Internet and investment calculus of public when evaluating data posted in newsgroups). *But see* Gregory C. Yadley, *The Challenges of Technology: The Regulators' Response to Securities Offerings on the Internet*, SB69 A.L.I.-A.B.A. 189, 197 (1997) (quoting SEC Commissioner M.H. Wallman's assertion that investment decisions by public do not influence discussions on chat-boards and other Internet rumors).

104. *See* Cielusniak, *supra* note 6, at 612 (arguing that speed and volume of Internet information delivery can overwhelm average member of public seeking reliable investment advice and strategies).

105. *See id.* at 618-19 (discussing value of Internet to corporations).

106. *See supra* notes 100-04 and accompanying text (discussing effect of Internet on reflective process of investors).

communication method to reach investors – they can deliver both required disclosure materials and optional soft communications (such as analyst reports) to investors without the associated cost of maintaining two information delivery infrastructures.[107] Thus, a more flexible solution than eliminating links – one that would shield the corporate client from liability while maintaining the viability of links to analyst reports – would be optimal.[108] The mechanisms discussed below may be combined in different fashions in order to tailor the solution to the particular client's needs and desires.

A. The Utility of Staleness Provisions

Because the information contained on a website constantly is reaffirmed as valid each day that a link to a site exists,[109] companies may choose to make clear to visitors that the data on linked sites is only valid for a certain period of time, after which it can be deemed to be stale.[110] This staleness provision

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107. *See supra* notes 100-04 and accompanying text (discussing communication of information to investors by corporations through Internet).

108. *See* Mark A. Metz, *Don't Get Too Comfy With That Home Page*, BUS. L. TODAY, July/Aug. 1998, at 61-62 (arguing that companies should never link to analyst reports from corporate home page). Metz's advice is from the perspective of an attorney seeking to minimize the potential liability of clients; it fails to take into account the business needs of publicly traded companies and the competitive advantage that hyperlinked analyst reports may provide. *Id.* at 61-63. Metz provided a comprehensive checklist concerning advice with respect to a client's corporate homepage, which includes the following:

1. Designate a member of the upper management to review the information posted on the home page on a periodic basis and after any significant development at the company. Correct any errors and delete all noncurrent information.
2. State the date of the most recent update of the information in the home page and include a disclaimer of responsibility for inaccuracies and omissions as a result of events occurring after that date.
3. Minimize the amount of forward-looking and other information requiring frequent updating.
4. Avoid including analysts' reports and hyperlinks to third-party materials.
5. Avoid including material information about the company that has not been publicly disseminated by means of a press release or SEC reports.
6. Avoid including a chat room in the home page. If one is included, strongly discourage employees from participating in it.
7. Avoid statements that could be considered a general solicitation of investors.
8. Review the home page prior to commencing any public or private securities offering.

Id. at 62.

109. *See supra* notes 66-75 and accompanying text (discussing role of hyperlinks as mechanism through which courts may find implied adoption).

110. *See* Mason, *supra* note 103, at 494 (analyzing use of password and gateway system as mechanism for reduced liability). The staleness provision (or disclaimer, as later discussed) could be communicated to the visitor by a "pop-up" window when the hyperlink is accessed.

may reduce the risk that a court will find a continuous duty to correct information.[111] Absent such a staleness provision, information that remains easily accessible and unchanged may be subject to valid reliance by investors, and a document may remain "alive" long after it otherwise would have.[112]

The requirement that a statement be "alive" in order to provide the basis for a valid 10b-5 claim finds its guiding principles in *Ross v. A.H. Robins Co., Inc.*[113] In *Ross*, the district court considered a shareholders' 10b-5 claim against a pharmaceutical company. The case concerned statements, made in the company's 1970 Annual Report, that indicated a product, the Dalkon Shield, was a safe and effective birth control device.[114] The shareholders, who had purchased stock in the company in 1973, argued that they had done so in reliance upon the 1970 statements.[115] The Shield did not perform as expected, but the company failed to correct the previous statements concerning the efficacy of the device until 1974.[116]

The court needed to distinguish between the statements that triggered a continuing duty to correct and those statements that did not; for example, a press release issued years ago at some point ceases to be accurate and thus is invalid as a basis for reliance.[117] A failure to make this distinction would be

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Id. Before the link is completed, the investor could be required to acknowledge that he or she is a sophisticated investor who understands that the information contained on the linked website may be either incorrect or outdated. IPONet utilized a similar approach to place public offerings of securities over the Internet. *Id.* at 494. Such a "gateway" likely would deter courts from finding reasonable reliance on the part of an investor who had agreed to such a statement before viewing linked analyst reports.

111. *See* BROWN, *supra* note 66, § 4.04 n.49 (discussing use of staleness rule as means to limit corporate liability with respect to electronic media).

112. *See infra* notes 120-28 and accompanying text (describing and analyzing doctrine of "alive" statements as component of reliance in 10b-5 actions). By the use of the term "alive," this Note refers to the measure of time upon which an investor can reasonably rely on a statement.

113. 465 F. Supp. 904 (S.D.N.Y. 1979), *rev'd on other grounds*, 607 F.2d 545 (2d Cir. 1979).

114. Ross v. A.H. Robins Co., Inc., 465 F. Supp. 904, 906 (S.D.N.Y. 1979), *rev'd on other grounds*, 607 F.2d 545 (2d Cir. 1979). In *Ross*, the court considered whether statements made in a 1970 annual report could be the basis for reliance by an investor who decided to purchase stock in 1973. *Id.* at 908. The specific statements indicated that the product, the Dalkon Shield, was developing "significant market appeal and arguably projected a favorable future for the Shield." *Id.* The court concluded that the passage of time alone was not sufficient to render a statement invalid as a basis for reliance. *Id.* In reaching this conclusion, the *Ross* court restricted the duty to correct misleading statements to only those that remained "alive." *Id.*

115. *Id.* at 906-07.

116. *Id.*

117. *Id.* at 907.

unreasonably burdensome and would overwhelm investors with enormous amounts of relatively useless information, risking the "overload" concerns of the *TSC Industries* Court.[118] Thus, the court added the requirement that the statement be "alive" in order to maintain a 10b-5 motion.[119]

Therefore, a statement remains "alive" so long as it continues to engender reliance.[120] Determining when reliance has ended is not always easy.[121] In some instances, reliance ceases to be reasonable once the purpose of disclosure has ended.[122] For example, a proxy statement will be considered to be no longer alive after its mailing unless evidence can be presented to show that the company was aware of the misleading statements at the time the proxy statement was presented.[123] Informal communications, on the other hand, create determinations that are more difficult.[124] Although "soft" communications may cease to be "alive" after the passage of time,[125] courts have yet to devise

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118. *See supra* notes 76-84 and accompanying text (discussing concept of "information overload" as addressed by *TSC Industries* Court).

119. *Ross*, 465 F. Supp. at 908.

120. *See* Mitchell v. Tex. Gulf Sulphur Co., 446 F.2d 90, 103 (10th Cir. 1971) (discussing concept of reliance in discussion of length of time statement reasonably could be relied upon).

121. *See* Ross v. A.H. Robins Co., Inc., 465 F. Supp. 904, 908 (S.D.N.Y. 1979) (discussing period upon which reliance may be reasonable). The *Ross* court noted that:

> [L]ogic compels the conclusion that time may render statements immaterial and end any duty to correct or revise them. In measuring the effect of time in a particular instance, the type of later information and the importance of earlier information contained in a prior statement must be considered. Thus, general financial information in a two-year old annual report may be stale and immaterial. . . . However, no general rule of time can be applied to all circumstances.

Id.

122. *See* Series Feldman & David Priebe, *Securities Litigation and Recent Developments – Federal Securities Law and the Internet*, MONDAQ BUS. BRIEFING, July 3, 1998, at 4 (contending that duty to update should apply to statements on webpage).

123. *See* Kennedy v. Chomerics, Inc., 669 F. Supp. 1157, 1161 (D. Mass. 1987) (determining that reliance on proxy statement, however misleading, was invalid as not "alive" given that company's Board of Directors was not aware of misleading statements at time they distributed proxy statement).

124. *Compare* Banc One Capital Partners Corp. v. Kneipper, 67 F.3d. 1187, 1193 (5th Cir. 1995) (holding that seller in "all or none" offering does have continuing duty to inform investors of facts after initial commitment to invest) *with* Hillson Partners Ltd. P'ship v. Adage, Inc., Civ. No. S 93-2315, 1994 WL 724924, at *6 (D. Md. Jan. 5, 1994) (finding company did not have duty to update error with respect to immaterial information).

125. *See* Warner Communications, Inc. v. Murdoch, 581 F. Supp. 1482, 1489-90 n.13 (D. Del. 1984) (discussing reasonable length of time upon which investor may rely on statement). The *Warner* court reasoned in a footnote that:

> In the absence of a limit on the continuing materiality of public statements by corporations or management, any misrepresentations in a statement could potentially result in liability to all investors who, at anytime thereafter, engage in transac-

a bright line test for the resolution of this issue.[126] Instead, courts tend to analyze the facts and circumstances of each particular case to determine whether a statement should be considered "alive."[127] In doing so, two factors become important in determining whether reliance is reasonable, especially in the context of a hyperlink to an analyst's report: the type of information disclosed and the circumstances of the disclosure.[128]

With respect to the type of information disclosed, courts generally have required that companies correct forward-looking statements, such as projections or analyst reports, once they are no longer accurate;[129] such statements tend to have a "life-span" much longer than other types of information.[130] For example, in *In re Time Warner Inc. Securities Litigation*,[131] the Court of Appeals for the Second Circuit concluded that "a duty to update opinions and projections may arise if the original opinions or projections have become misleading as the result of intervening events."[132] The court distinguished be-

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> tions in the company's stock. At some point, such a result would not only be harsh, but simply absurd.

Id.

126. *See id.* (noting unwillingness to commit to any specific time period as determinative of expiration of reliance period).

127. *See* Ross v. A.H. Robins Co., Inc., 465 F. Supp. 904, 908 (S.D.N.Y. 1979) (noting that in measuring time that statement remains "alive," court should consider type and context of information disclosed).

128. *See infra* notes 129-52 and accompanying text (discussing different types of information and circumstances of disclosure).

129. *See In re* Home Health Corp. Sec. Litig., No. 98-834, 1999 U.S. Dist. LEXIS 1230 (E.D. Pa. Jan. 29, 1999) (concluding Section 10(b) imposes duty to correct both historical and forward looking earnings projections (citing *In re* Burlington Coat Factory Sec. Litig., 114 F.3d 1410, 1433-34 (3d Cir. 1997))). *But see Hillson*, 1997 WL 724924, at *6 (arguing duty to correct projections would discourage disclosure that securities laws seek to encourage).

130. *See* Rubinstein v. Collins, 20 F.3d 160, 170 n.41 (5th Cir. 1994) (noting that in context of projections "it appears that defendants have a duty under Rule 10b-5 to correct statements if those statements have become materially misleading in light of subsequent events"); *In re* Kulicke & Soffa Indus., Inc. Sec. Litig., 697 F. Supp. 183, 185 (E.D. Pa. 1988) (recognizing duty to correct projections that subsequently become misleading); *see also In re* Nations-Mart Corp. Sec. Litig., 130 F.3d 309, 321 (8th. Cir. 1997) (noting that some courts have found duty to correct or update statements once incorrect). *But see In re* Gen. Instrument Corp. Sec. Litig., No. 96-C-1129, 1997 U.S. Dist. LEXIS 14855, at *26 (N.D. Ill. Sept. 23, 1997) (recognizing no duty exists in Seventh Circuit to correct projections that are incorrect due to unexpected reasons); Wallace v. Sys. & Computer Tech. Corp., No. 95-CV-6303, 1997 U.S. Dist. LEXIS 14677, at *73 n.43 (E.D. Pa. Sept. 23, 1997) (determining that there is no duty to update "run-of-the-mill earnings projections").

131. 9 F.3d 259 (2d Cir. 1993).

132. *In re* Time Warner Inc. Sec. Litig., 9 F.3d. 259, 267 (2d Cir. 1993). In *Time Warner*, the Second Circuit considered statements made by company officials indicating that talks with potential merger candidates were likely to be successful. *Id.* at 262. After such talks failed to

tween definite statements that may engender reliance, such as earnings forecasts, and more ambiguous statements of company policy.[133] With respect to definitive statements of company projections, such as those contained in analyst reports, the court was willing to consider the time such statements were to be "alive" as much longer than other types of statements.[134] Similarly, in the context of a hyperlink to an analyst's report, courts are likely to consider the material to be "alive" for a longer period.[135] As a result, courts are likely to find that less obvious actions by a company ratifying this information serve as a reasonable basis for reliance.[136] In *Time Warner*, the court's decision could lead future courts to conclude that the seemingly innocuous presence of a hyperlink may be interpreted as sufficient to establish to potential investors that the report is valid every day that the hyperlink continues to exist.[137]

Courts also will analyze the circumstances of disclosure to determine whether a particular statement is still "alive."[138] When a company discloses information in such a way that it is virtually guaranteed to reach a significant audience, courts are more likely to impose a duty to correct subsequent errors than if the statements were thinly distributed.[139] For example, in *In re Meridian Securities Litigation*,[140] the court reached a similar conclusion.[141] In that

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materialize in a profitable merger, the plaintiff sought to bring a 10b-5 claim for failure to correct the previous statements concerning the status of the merger discussions. *Id.* at 261. The court drew a distinction between statements that made definitive positive projections, such as earnings forecasts or analyst reports, and more ambiguous statements concerning company prospects, such as the statements at issue, concluding that the latter failed to provide enough factual basis to support a finding of reasonable reliance. *Id.* at 267. Thus, the court dismissed the plaintiff's claim with respect to the failure to correct the statements concerning merger talks that had yet even to commence. *Id.*

133. *Id.*

134. *Id.*

135. *See* Feldman & Priebe, *supra* note 122, at 4 (arguing that information on web page engenders investor reliance for longer period of time).

136. *See supra* notes 66-75 and accompanying text (discussing hyperlink as non-verbal form of communication that may give rise to implied adoption of third party statement).

137. *See supra* notes 66-75 and accompanying text (discussing hyperlink and possibility of finding of implied adoption).

138. *See In re* Gulf Oil/Cities Serv. Tender Offer Litig., 725 F. Supp. 712, 748-49 (S.D.N.Y. 1989) (stating that in context of previously disclosed merger agreement, subsequent change of heart triggered duty to correct information).

139. *See generally* Capri Optics Profit Sharing v. Digital Equip. Corp. 950 F.2d 5 (1st Cir. 1991) (finding disclosure of future profit projections to investors as potentially misleading from investors' standpoint, although court did not find violation in this case due to circumstances of disclosure).

140. 772 F. Supp. 223 (E.D. Pa. 1991).

141. *See In re* Meridian Sec. Litig., 772 F. Supp. 223, 227 (E.D. Pa. 1991) (discussing lack of disclosure and duty to correct misleading statements). In *Meridian*, the court considered

case, public statements made by the officers and the directors of the corporation concerning the company's potential earnings were at issue.[142] Finding that senior management made the statements to the entirety of the public, the court was willing to discount the fact that the information disclosed was "soft" rather than definitive statements of financial conditions.[143] Thus, the court imposed a duty to correct on the corporation based solely upon the circumstances of disclosure.[144] Had the company provided the "soft" information in a limited press conference by a lower-level employee, the court likely would have been more hesitant to impose such a duty.[145] In the context of a company's website, a court is likely to view the medium of communication as a wide-ranging distribution, similar to the full public disclosure made by Meridian officers.[146] Thus, even if information to which a company's website is linked can be argued to be "soft," the circumstances of disclosure may still trigger a duty to correct – the statements will be considered to be alive for as long as the hyperlink exists.[147]

A problem arises when a company wishes to sever itself from a statement that might engender reliance. Two potential solutions may allow a company to maintain the hyperlink yet avoid the problem of "extended life" conferred to the information by the hyperlink.[148] First, a clear statement on the analyst's page should indicate that the information should only be considered current as of the publication date and that subsequent events may have intervened to make the report inaccurate.[149] This disclaimer would prevent investors from

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public statements made by directors of the corporation concerning earnings forecasts as they related to investments in Meridian Bancorp, Inc. *Id.* at 225. The shareholders' suit claimed that the directors were under a duty to correct statements made after it was learned that Meridian Bancorp's title insurance companies were troubled financially. *Id.* The defendant directors contended that they were under no duty to correct the statements because silence, absence a duty to disclose, was not misleading. *Id.* at 227. The court determined that the nature of the original statements, being made by high ranking directors to the entirety of the general public, provided enough of a basis to create reasonable reliance even though such information was "soft" rather than firm projections. *Id.* at 226.

142. *Id.* at 225.

143. *Id.* at 226-27.

144. *Id.* at 227.

145. *Id.*

146. *See* Metz, *supra* note 108, at 63 (arguing that hyperlink presence means information is disseminated each time user accesses link).

147. *See id.* (contending use of hyperlink to another website triggers continual duty to correct linked information).

148. *See infra* notes 149-52 and accompanying text (discussing possible limits to reliance on website information).

149. *See* BROWN, *supra* note 66, § 9.03[2] (discussing dating of disclaimer as potential strategy to avoid liability).

claiming that the report engendered reasonable reliance.[150] Second, companies should insist that any analyst's website to which they provide a hyperlink undergo periodic archiving, that is, the removal of older information to a clearly marked "archive" file.[151] Such a policy would sever the capability of the hyperlink to grant an "extended life" to information that otherwise would be deemed to have become "dead" with the passage of time.[152] By incorporating these solutions into their website management practices, companies may begin to eliminate the extended life generated by Internet distribution of analyst materials.

B. Disclaimers – The HyperLiability "Exit Strategy"

The second potential solution that would allow companies to maintain a hyperlink as a mechanism of information communication but still avoid the possibility of liability through entanglement is to use a general disclaimer.[153] Such a disclaimer would indicate that the company provides links to the analyst reports only as an information service, but does not endorse their accuracy and, accordingly, visitors should view such information and act upon it at their own risk.[154] Generally, courts have been unwilling to recognize such disclaimers as effective within the scope of securities law.[155] However, three different lines of cases support an interpretation that would give legal effect to a hyperlink disclaimer on a website.[156]

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150. *Id.*

151. *Id.*

152. *Id.*

153. *See generally* Prentice, *supra* note 3, at 62-4 (discussing role of disclaimers as related to website liability for companies with home pages). Prentice suggested a disclaimer should conform to the following model:

> XYZ provides links to the analyst reports listed below as a service to those interested in this information. XYZ does not endorse these reports and can make no guarantee as to their accuracy or completeness. Users visit the analysts' Web sites at their own risk. Those interested in investing in XYZ are directed to the materials filed with the SEC by XYZ.

Id. at 62.

154. *See* Lawrence Hertz, *Top Ten Cyber-Commandments for Website Legal Pages*, CYBERSPACE LAW., Apr. 1997, at 5 (supporting use of similar disclaimer for any material posted at linked site). Hertz acknowledged that the legal effectiveness of such disclaimers is uncertain. *Id.*

155. *See* Prentice, *supra* note 3, at 63 (arguing that policies underlying Rule 10b-5 are inconsistent with recognition of disclaimers as effective waivers of liability).

156. *See infra* notes 157-78 and accompanying text (discussing secondary liability, disclaimers of fraud, and merger doctrine as possible support for use of disclaimers to avoid hyperlink liability); *see also* Robert A. Prentice, *Locating That "Indistinct" and "Virtually Non-*

1. A Consideration of Secondary Liability

Some courts have indicated a willingness to absolve a person of liability when the only cause of action is aiding another person's communication for the commission of fraud;[157] aiding another person does not provide the basis for an actionable claim based upon secondary liability.[158] In *Central Bank of Denver v. First Interstate Bank of Denver*,[159] the Supreme Court determined that the language in Rule 10b-5 imposing liability for "directly or indirectly" violating the statute did not include liability for aiding and abetting.[160] In that case, the Supreme Court considered the general question of whether liability should attach to a person who had endorsed the communication of another who intentionally had misrepresented the value of a security but who had made such an endorsement without knowledge of the misrepresentation.[161] After discussing how to construct properly the "directly or indirectly" language in Rule 10b-5, the Court determined that:

Existent" Line Between Primary and Secondary Liability Under Section 10(b), 75 N.C. L. REV. 691, 776 (1997) (criticizing distinction between primary and secondary liability). Prentice argued that Rule 10b-5 liability should be imposed on the following persons:

> [T]hose who (a) make false representations or omissions themselves; (b) by their visible and substantial participation in another's communications impliedly vouch for the accuracy of those statements; (c) participate substantially in another's false statements (or omissions) knowing that they are false and will be shown to investors who will rely on them; and (d) fail, in very limited circumstances, to blow the whistle on fraud when they have a duty to do so....

Id. at 776.

157. *See, e.g.*, Anixter v. Home-Stake Prod. Co., 77 F.3d 1215, 1224 (10th Cir. 1996) (imposing no liability for aiding and abetting actions under Rule 10b-5 (citing Cent. Bank of Denver v. First Interstate Bank of Denver, 114 S.Ct. 1439, 1455 (1994))); Lycan v. Walters, 904 F. Supp. 884, 901 n.12 (S.D. Ind. 1995) (same).

158. *See* Prentice, supra note 156, at 63-64 (providing general discussion of secondary versus primary liability strand of cases).

159. 511 U.S. 164 (1994).

160. Cent. Bank of Denver v. First Interstate Bank of Denver, 511 U.S. 164, 176-77 (1994). In *Central Bank*, the Court considered a claim by the respondents that Central Bank had violated Rule 10b-5 by delaying a review of an appraisal of bonds issued by a client to whom Central Bank served as indenture trustee for the issue. *Id.* at 167-68. Although it was clear that Central Bank's client had violated the Rule by intentionally misrepresenting the value of the bonds in light of the declining prices in the local real estate market, it was unclear whether Central Bank should be held secondarily liable for delaying an appraisal of the bonds' value where the Bank was unaware of the intentional misrepresentation of their value. *Id.* The Court resolved the issue by examining the "directly or indirectly" language used in the Rule and concluded that because Congress knew how to explicitly include liability for aiding and abetting actions, the lack of such an explicit inclusion in this case meant they did not intend to do so. *Id.* at 176-77.

161. *Id.* at 167-68.

> Extending the 10b-5 cause of action to aiders and abettors no doubt makes the civil remedy far more reaching, but it does not follow that the objectives of the statute are better served. Secondary liability for aiders and abettors exacts costs that may disserve the goals of fair dealing and efficiency in the securities markets.[162]

The language of *Central Bank* suggests that a disclaimer embodies the same lack of scienter that was present in the aforementioned case, such that a disclaimer serves to insulate a company from liability for misrepresentations of which they know nothing and to which their only contact is the presence of a hyperlink. Of course, such a disclaimer would only be viable when the company had not given any information to or reviewed any findings of the analyst.[163] In such cases there would be more substantial evidence of knowledge of the misleading information.[164] Thus, secondary liability would not be the basis of a 10b-5 claim.[165] However, when the misstatements occur as a result of changes on an analyst's page of which the company is unaware, a disclaimer may be a powerful tool to avoid liability.

2. *Professional Disclaimers of Fraud*

The second line of cases that may insulate a company from liability through the use of a disclaimer concerns other professional occupations' use of disclaimers of fraud.[166] For example, courts have upheld disclaimers as effective when included as part of attorney statements and when such disclaimers reflected the fact that the attorney's communications were merely restatements of information provided by a client.[167] In such cases, courts have refused to impose liability when disclaimers were present on the grounds that

162. *Id.* at 188.

163. *See supra* notes 48-65 and accompanying text (discussing entanglement as basis for implied adoption). Once entanglement exists, the court presumes the company to have made the statements itself, even if the communication is originally the product of a third party. *Id.*

164. *Id.*

165. *Id.* In cases in which entanglement allegedly is basis of the company's adoption of a communication, the 10b-5 claim would contend that the statements were made directly by the company.

166. *See* Prentice, *supra* note 3, at 64-66 (discussing professional disclaimers of fraud).

167. *See* Fortson v. Winstead, McGuire, Sechrest & Minick, 961 F.2d 469, 475 (4th Cir. 1992) (determining that imposing duty of responsibility on attorneys for client statements would artificially inflate costs of legal counsel involved in commercial transactions); Moorhead v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 949 F.2d 243, 245-46 (8th Cir. 1991) (giving effect to cautionary statements in defendant's feasibility study). *But see* Turkish v. Kasenetz, 27 F.3d 23, 27-28 (2d Cir. 1994) (determining that disclaimers are ineffective insofar as they shield defendant from his own fraudulent conduct); Kline v. First W. Gov't Sec., Inc., 24 F.3d 480, 488 (3d Cir. 1994) (refusing to give effect to disclaimer due to reasonableness of plaintiff's reliance on attorney's opinion).

failure to do so would alter the role of the disclaiming party from conveyor of information to watchdog for information seeking parties.[168] Moreover, a failure to give effect to an attorney's disclaimer would make "a party . . . liable for unlimited information even though it would be well beyond the matter for which it was retained."[169]

A disclaimer on a company website arguably serves a similar function as the attorney fraud disclaimers in the aforementioned cases. Especially in cases in which the company is unaware of the errors in the analyst report, courts likely will give the disclaimer great prophylactic effect;[170] for courts to do otherwise would convert the role of the public company to the that of the SEC – monitoring disclosure of information by securities traders.[171] Even when a company is aware of errors in the report, a disclaimer may still shield the company from liability for such errors just as it does for attorneys.[172] Even when a company knows of the mistakes, the disclaimer, if properly drafted and clearly displayed, would indicate that the report is the sole product of the analyst and its conclusions and information are not the responsibility or product of any actions taken by the company.[173] An appropriate disclaimer should serve to eliminate the possibility of reasonable reliance by the investor, a claim that cannot be saved by merely pointing to a hyperlink and citing entanglement jurisprudence.

3. *The Use of the Merger Doctrine*

Finally, the merger doctrine may provide justification for the enforcement of disclaimers on a website. The merger doctrine, as applied by most courts, insulates a company from fraudulent and intentional acts of its employees when a company incorporates a disclaimer into all contracts and transactions with the plaintiff.[174] One commentator has described the doctrine as merely an

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168. *See Fortson*, 961 F.2d at 475 (concluding that "[t]he end result would have attorneys stand as the guarantors of integrity in all commercial transactions . . . [l]awyers, in short, would function in the business world as designated watchdogs").

169. *Id.* at 475 (quoting Roberts v. Peat, Marwick, Mitchell & Co., 857 F.2d. 646, 654 (9th Cir. 1988)).

170. *See* Kennedy v. Josephthal & Co., Inc., 814 F.2d 798, 803-05 (1st Cir. 1987) (finding plaintiff barred from reliance on oral statements at odds with written offering memorandum).

171. *See Fortson*, 961 F.2d at 475 (expressing concern over shifting monitoring duties to those outside regulatory capacities).

172. *See* Prentice, *supra* note 3, at 66 (concluding that courts likely will reach similar conclusion based on analogy to attorney disclaimers of fraud).

173. *See* Metz, *supra* note 108, at 64 (advocating use of carefully drafted disclaimer on corporate websites).

174. *See* Harsco Corp. v. Segui, 91 F.3d 337, 345 (2d Cir. 1996) (concluding that plaintiff may not recover based on misrepresentations by employees when contract explicitly excluded

application of the parol evidence rule to the securities context: Written disclaimers shall be given precedence over oral statements of fraud concerning the sale of securities.[175] For example, if an investor purchases securities from a broker relying on statements made in a discussion with that broker, but existing in the purchase agreement is a clause indicating that the investor made the purchase without relying on any information provided by the broker, courts will use the merger doctrine to insulate the broker from 10b-5 claims.[176]

A company's disclaimer on a website concerning a hyperlink to an analyst's report could function in a similar manner. A company could construct the disclaimer in such a way that every time the link is "clicked" the disclaimer would appear and require the viewer to acknowledge it before the analyst's page would appear. If constructed in such a fashion, the disclaimer arguably would function as a written agreement similar to the one outlined in the above hypothetical situation. In such a case, the merger doctrine would function to give precedence to the implied adoption by the hyperlink of the validity of the analyst report; the reasonability of the reliance of the investor would be eliminated by an express agreement to the contrary.[177] Given the relative ease with which courts uphold disclaimers based on all three theories,[178] corporate counsel would be well-advised to incorporate easily seen and carefully worded disclaimers with every hyperlink installed.

C. Docking in a Safe Harbor: The 1995 PSLRA

In December 1995 Congress passed the Private Securities Litigation Reform Act (PSLRA).[179] The PSLRA contained important provisions con-

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such claims); Brown v. E.F. Hutton Group, Inc., 991 F.2d. 1020, 1033 (2d Cir. 1993) (deciding that cautionary statements included in prospectus insulated defendant from 10b-5 claim); Davidson v. Wilson, 973 F.2d. 1391, 1401 (8th Cir. 1992) (concluding investors may not reasonably rely on oral misrepresentations where contradictory written disclaimers are present). *But see* Margaret V. Sachs, *Freedom to Contract: The Trojan Horse of Rule 10b-5*, 51 WASH. & LEE L. REV. 879, 911-14 (1994) (arguing that merger doctrine defense is inconsistent with policy of Section 29(a) of 1934 Securities Act). Sachs also contended that the reasonableness of reliance is understated by the merger doctrine given that investors are more likely to give credence to oral statements made by employees of a brokerage house rather than by volumes of written materials that they are handed. *Id.* at 911.

175. *See* Prentice, *supra* note 3, at 67 (framing merger doctrine as an application of parol evidence rule).

176. *See id.* at 66 (outlining hypothetical situation).

177. *See* Kennedy v. Josephthal & Co., Inc., 814 F.2d 798, 803-05 (1st Cir. 1987) (giving priority to written disclaimer in offering memorandum over oral misrepresentations).

178. *See supra* notes 153-76 (discussing potential doctrines by which courts give effect to disclaimers of liability in context of both securities and other professions).

179. Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67 (Dec. 22, 1995). For a discussion of the legislative history surrounding the passage of the Act, see generally John

cerning a safe harbor for projections and forward-looking statements.[180] The safe harbor extends to any forward-looking statement identified as such and "accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement. . . ."[181] Although the Act itself does not define "meaningful cautionary statements," if companies accompany hyperlinks with such a cautionary statement, they can shield themselves from liability for misstatements in any analyst reports.[182] The question then arises as to what a company must provide with a hyperlink in order to constitute a "meaningful cautionary statement."

The legislative history behind the Act indicates that the statement must contain specific information that would provide investors and others with an understanding of identifiable factors that could render the forward looking statement or projections inaccurate.[183] It may be more difficult for a company to fashion a cautionary statement that would suffice in cases in which the error in the analyst's report is unknown to the company; a court may not consider a boilerplate provision indicating that analyst reports may change and contain misinformation specific enough.[184] However, at least one court has found relatively vague disclosure is sufficient to meet the cautionary statement requirement.[185] If other courts follow suit, the potential for avoiding hyperlink liabil-

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W. Avery, *Securities Litigation Reform: The Long and Winding Road to the Private Securities Litigation Reform Act of 1995*, 51 BUS. LAW. 335 (1996) (discussing both original and modified forms of Act and debate surrounding each before passage).

180. Private Securities Litigation Reform Act of 1995 §27A. For a judicial interpretation of the meaning of forward-looking statement under application of the Act, see Harris v. Ivax Corp., 998 F. Supp. 1449, 1453 (S.D. Fla. 1998) (finding that statements indicative of future rather than present condition constitute forward-leaning statements under Act).

181. Private Securities Litigation Reform Act of 1995 § 27A(c)(1)(A), Pub. L. No. 104-67 (Dec. 22, 1995).

182. *See* Prentice, *supra* note 3, at 41-44 (discussing safe harbor provision of PSLRA in context of electronic communications).

183. *See* Securities Litigation Reform Act, *Conference Report*, H.R. REP. NO. 104-369, at 43 (1995) (noting that "[t]he cautionary statements must convey substantive information about factors that realistically could cause results to differ materially from those projected in the forward-looking statement, such as, for example, information about an issuer's business"); *see also id.* at 43-44 (arguing that "'[i]mportant' factors means the stated factors identified in the cautionary statement must be relevant to the projection and must be of a nature that the factor or factors could actually affect whether the forward-looking statement is realized").

184. *See* Metz, *supra* note 108, at 62 (discounting value of boilerplate provisions as capable of eliminating finding of reliance by courts).

185. *See* Rasheedi v. Cree Research, Inc., No. 1:96CV00890, 1997 U.S. Dist. LEXIS 16968, at *4-8 (M.D.N.C. Oct. 17, 1997) (validating press release containing cautionary statements that "actual results may differ" and listing "important factors" that may cause projections to be inaccurate).

ity by companies may become as simple as the inclusion of a standardized boilerplate statement accompanying every hyperlink.

V. Conclusion – A Brave New World?

Faced with the growing importance of the Internet to the securities trading community, the SEC must now realize the significance of adapting its regulations to the new communication sphere.[186] As companies begin to make the majority of their required disclosures and soft information available to the public through primarily electronic means,[187] the need for this adaptation will grow. Given the incentives for companies to provide links from their website to detailed financial information for potential investors,[188] the SEC should determine how Rule 10b-5 will apply in the context of these hyperlinks. Initially, the SEC must determine whether the hyperlink itself is to be seen as a form of nonverbal communication, and if so, how such a communication interacts with the doctrine of implied adoption.[189]

This Note has argued that such an adoption of analyst statements should be inferred from the presence of a "naked" hyperlink[190] to analyst reports from a corporation's home page.[191] Moreover, this Note has argued that although this theory would result in an elevated and continual duty to correct and update information on the linked site, this duty is justified by the benefits the Internet provides to the corporate world.[192] However, to place the entire burden (and associated liability) on corporations would be exceedingly unfair; some responsibility must lie with the investor making the actual investment decision.[193]

186. *See supra* notes 11-14 and accompanying text (discussing need for SEC adaptation of securities regulation to Internet).

187. *See supra* notes 15-21 and accompanying text (describing shift to Internet as primary means of information delivery by corporate America).

188. *See supra* notes 105-07 (analyzing potential benefits to corporations by providing direct hyperlinks to analyst reports). *See generally* Stan Davis & Christopher Meyer, *Risky Business*, BUSINESS 2.0, March, 2000, at 308 (arguing that corporate CEOs spend majority of their time attempting to manage risks and balance costs against benefits).

189. *See supra* notes 66-75 and accompanying text (analyzing hyperlink to analyst reports as mechanism through which courts may find implicit adoption of analyst statements).

190. By the term "naked" hyperlink, this Note refers to a hyperlink that is not accompanied by the presence of a disclaimer, staleness provision, or other prophylactic device.

191. *See supra* notes 66-75 (arguing that hyperlink serves as nonverbal communication indicating adoption of linked materials).

192. *See supra* notes 76-104 and accompanying text (providing multiple policy justifications for implied adoption of third party statements by presence of hyperlink).

193. *See supra* notes 91-99 (discussing analogy between elevated duty to correct and strict liability in tort).

This Note has argued that the best mechanism to place this burden on the investor is the enforcement of the requirement of reasonable reliance in 10b-5 actions.[194] If corporations are use disclaimers, staleness provisions, and specific cautionary statements, courts are likely to view such measures as prophylactic devices limiting an investors claim to reasonable reliance.[195] In this manner, companies can dilute the risks associated with the rapid pace of the information age,[196] while at the same time embracing the Internet and the potential it offers to streamline information delivery into an efficient communicative system.

Critics may contend that the ever-changing Internet requires a new set of regulations and guidelines apart from the Securities Acts of 1933 and 1934.[197] However, the SEC already has established the basic infrastructure to make the metamorphosis from a paper-based to an Internet-based regulatory system.[198] As indicated earlier, the SEC is willing to view electronically delivered documents in the same light as traditionally delivered disclosure materials.[199] The only task thus remaining is to adapt the specific disclosure rules to this view of document delivery.[200] Intrinsic to this process will be the need to reassess the burdens the various rules place on particular parties.[201] A successful balance of these burdens between investors and corporations assures the continued viability of the application of Rule 10b-5 as it faces the rapidly changing world of the Internet.

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194. *See supra* notes 35-47 and accompanying text (discussing requirement of reliance in context of 10b-5 claims by plaintiffs).

195. *See supra* notes 109-85 (analyzing judicial treatment of various devices intended to shield corporations from liability for hyperlinks to inaccurate analyst reports).

196. *See supra* notes 76-84 and accompanying text (arguing that rapid access to information through Internet poses unique problem of information overload to investors).

197. *See* Cielusniak, *supra* note 6, at 613-14 (arguing that current regulatory structure is inapplicable to Internet securities trading); Smith, *supra* note 78, at 611 (contending new regulatory structure for securities fraud is needed). *But see* Cella & Stark, *supra* note 6, at 835 (advocating use of current regulatory schemes for SEC prosecution of securities fraud over Internet).

198. *See* Prentice, *supra* note 3, at 10-12 (discussing enforcement initiatives of SEC through use of Internet).

199. *See supra* note 69 and accompanying text (describing SEC view of hyperlink as creating single electronic document).

200. *See* Cella & Stark, *supra* note 6, at 835-36 (advocating use of expanded surveillance as tool to discourage and monitor securities fraud over Internet).

201. *See supra* notes 71-75 and accompanying text (discussing elevated duties arising from view of hyperlinks as mechanism of single document creation when companies constantly altered webpages).

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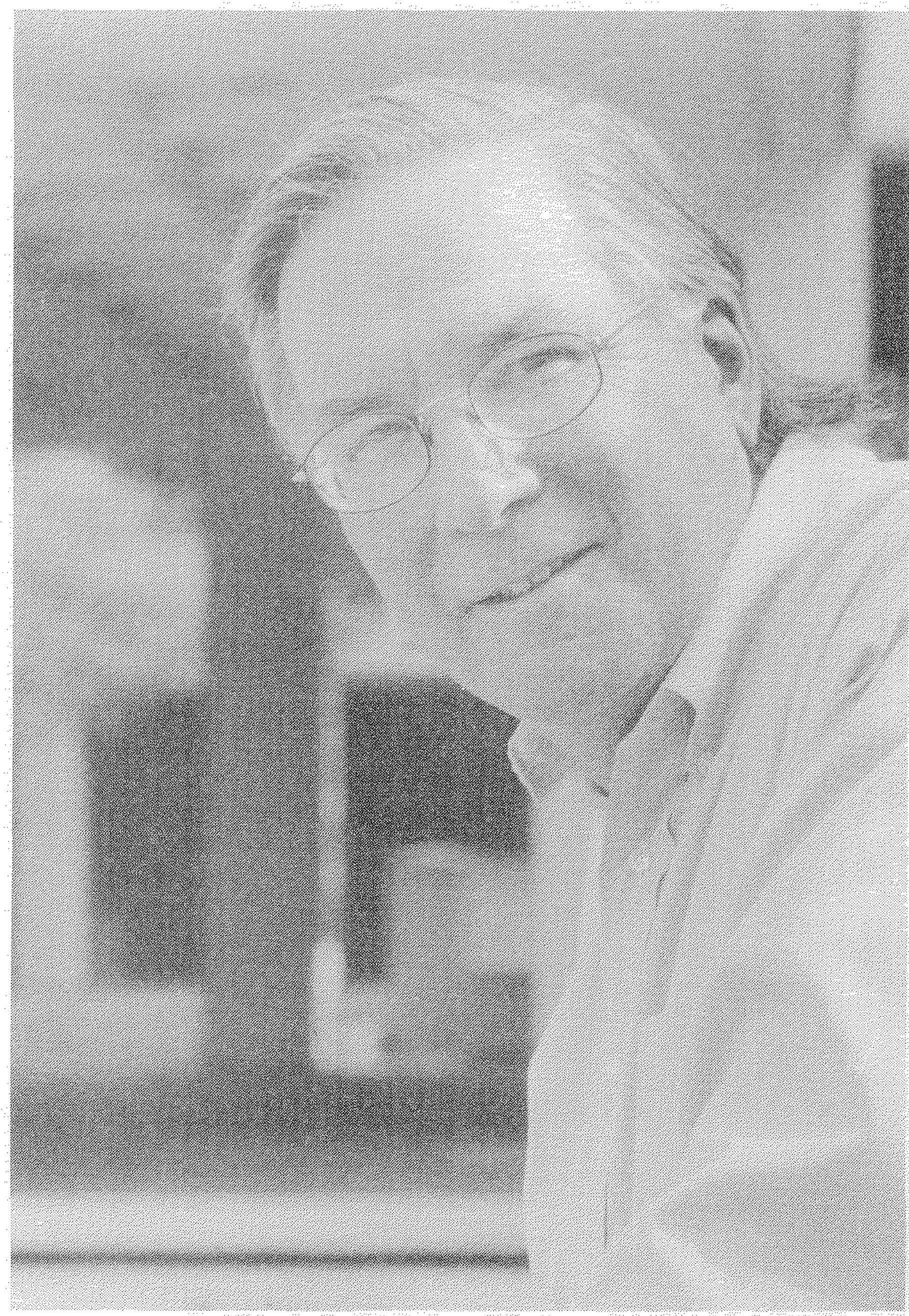
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William S. Geimer