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THE REINCARNATION OF RULE 152: FALSE HOPE ON THE INTEGRATION FRONT

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In a series of recent no-action letters,¹ the staff of the Securities and Exchange Commission (SEC) has breathed life into rule 152,² an obscure, near-dormant regulation enacted in the mid-1930s.³ The SEC has used the procession of rule 152 no-action requests as an opportune occasion for partially revisiting a concept that long has plagued securities professionals—the doctrine of integration. Essentially, the SEC now interprets rule 152 as precluding integration of a section 4(2) private placement of securities with a subsequent registered public offering of additional securities even if the issuer contemplated the public offering at the time the private placement commenced and undertook the public offering shortly after completing the private placement.⁴ Naturally, because this position appears to bring a measure of certainty to at least one part of the integration conundrum, issuers and their legal counsel will greet the development with great enthusiasm.

This article, after first describing the irksome manner in which the integration doctrine constrains capital financing decisions, examines rule 152 in depth and concludes that the SEC has chosen the wrong vehicle for seeking to settle a portion of the integration controversy. Historically, the

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1. See Country First Bank, SEC No-Action Letter (Mar. 31, 1989) (LEXIS, Fedsec library, Noact file) (stating that, under rule 152, public offering following offering otherwise exempt under rule 506 of regulation D does not vitiate rule 506 exemption); Vintage Group, Inc., SEC No-Action Letter, [1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,700, at 77,978 (Apr. 11, 1988) (stating that rule 152 precludes integration of exempt private offering with registered public offering as long as public offering follows private offering); The Immune Response Corp., SEC No-Action Letter (Nov. 2, 1987) (LEXIS, Fedsec library, Noact file) (relying on rule 152 to preclude integration of exempt private offering and registered public offering that followed private offering); Vulture Petroleum Corp., SEC No-Action Letter, [1987 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,407, at 77,319 (Dec. 31, 1986) (same); BBI Assocs., SEC No-Action Letter (Dec. 29, 1986) (LEXIS, Fedsec library, Noact file) (stating that filing of registration statement subsequent to offering otherwise exempt from registration under § 4(2) does not vitiate exemption provided by § 4(2)); Verticom, Inc., SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file) (same); *infra* notes 61-90 and accompanying text (discussing SEC's current interpretation of rule 152).

2. 17 C.F.R. 230.152 (1985).

3. See Securities Act Release No. 33-305 (Mar. 2, 1935) (available from SEC; reprinted in Appendix) (adopting rule 152).

4. See *infra* notes 61-90 and accompanying text (discussing SEC's current interpretation of rule 152).

SEC designed rule 152 for a very limited purpose—to enable a failed private offering to be salvaged by a registered public re-offering of the unsold securities—a purpose well-suited for the financial stagnation of the mid-1930s, but one that is unrelated to the modern phenomenon of successful multi-round private financings culminating in a registered public offering of still more securities. Therefore, while in fact the rule is linguistically amenable to the SEC's recent reading, a point that commentators heretofore have not recognized, the rule is made so only by distorting its intended purpose and committing historical error. Consequently, the article concludes that the securities bar should not be overly comforted by, and indeed should proceed cautiously with respect to, the SEC's new interpretive tack, particularly in light of continuing liability to disgruntled investors. Moreover, however laudable and meritorious SEC efforts on the nagging integration front might be, rule 152 is not a suitable instrument, and the no-action letter is not the proper format, for a dramatic shift in policy. Thus, we further conclude that the SEC should approach the whole notion of integration in a more forthright and punctilious fashion. Throughout this article we hope to make clear that the entire integration controversy ultimately implicates the larger question of the policies and purposes of registration and of exemptions therefrom, and that the SEC in its regulatory efforts on the integration front must be ever mindful of that relationship.

I. INTRODUCTION TO THE PROBLEM: THE REALITY OF MULTI-ROUND FINANCING AND THE DOCTRINE OF INTEGRATION.

Lacking adequate cash flow from operations, many start-up and emerging businesses turn to the financial markets for capital. Because the amount and timing of capital needs are difficult to predict, and because investors are reluctant to "overfund" unproven ventures, young companies often will return to the capital markets again and again for periodic infusions of cash. The result is that many companies engage in multiple "rounds" of financing before generating sufficient internal cash to slake their thirst for outside capital.

The process of capital formation does not occur in a regulatory vacuum. Both federal and state laws regulate the issuance of securities for value. Section 5⁵ of the Securities Act of 1933⁶ (the Securities Act) prohibits the public offering of securities until the issuer files a registration statement with the SEC and prohibits the sale of securities until the registration statement becomes effective.⁷ Although the registration process affords the

5. 15 U.S.C. § 77e (1982).

6. Securities Act of 1933, 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a-77aa (1982 & Supp. IV 1986)).

7. 15 U.S.C. § 77e (1982). Congress based the Securities Act on the premise that Congress can best protect investors that are unable to fend for themselves by requiring full and fair disclosure. See Preamble to the Act, 48 Stat. 74 (1933) (stating purposes of Securities Act). Those investors then can make intelligent investment decisions. *Id.* To achieve full and fair disclosure, § 5 of the Securities Act requires that issuers must register all nonexempt offerings of securities. See 15 U.S.C. § 77e (1982).

SEC an opportunity to review and comment on the registration statement to determine whether an issuer has made various required disclosures to the public about the issuer, the issuer's business, and the securities themselves, the registration process is costly and time-consuming and, from the issuer's standpoint, is to be avoided if at all possible.

In spite of its broad reach, the coverage of the Securities Act, unlike that of its counterpart the Securities Exchange Act of 1934⁸ (the Exchange Act), is episodic. An issuer triggers the intricate regimen of the Securities Act only when it "offers" or "sells" a "security."⁹ Even then, an issuer can avoid the requirements and proscriptions of section 5 of the Securities Act—and the resulting liability for certain Securities Act miscues¹⁰—if the security to be issued or the financing transaction to be engaged in can be brought within one of several exemptions from registration.¹¹

Importantly, an exemption from registration applies only to offers and sales associated with a particular transaction, not to capital-raising transactions that precede or follow the exempt transaction. For a company that seeks capital on more than one occasion in a relatively short period of time, the question arises as to whether each episode is part of one or more "transactions" that have preceded or followed the episode, or whether the episode truly stands alone as a discrete capital-raising incident. Because the Securities Act contains several transactional exemptions—each with distinct conditions, policy underpinnings, and rubric, and all of which the SEC and courts will strictly construe against the issuer¹²—two or more seemingly

8. Securities Exchange Act of 1934, 48 Stat. 881 (codified as amended at 15 U.S.C. §§ 78a-78kk (1982 & Supp. IV 1986)).

9. See 15 U.S.C. § 77e (1982) (requiring issuer to register securities that issuer offers or sells unless securities are otherwise exempt). While defined in sections 2(3) and 2(1) of the Securities Act, respectively, the terms "sell" and "offer" and the term "security" have, over the years, been interpreted broadly. See R. JENNINGS & H. MARSH, JR., *SECURITIES REGULATION* 69-109, 220-93 (6th ed. 1987) (discussing courts' interpretations of terms "sell," "offer," and "security").

10. See 15 U.S.C. §§ 77k, 77l (1982) (defining liability for certain violations of Securities Act). Section 11 of the Securities Act applies only to securities transactions for which a registration statement has become effective. See 15 U.S.C. § 77k (1982). However, the liability provisions of § 17 and, except for government securities, that of § 12(2) of the Securities Act, apply as well to exempted securities and transactions. See 15 U.S.C. §§ 77l, 77q (1982).

11. See R. JENNINGS & H. MARSH, JR., *supra* note 9, at 298-452 (discussing exemptions of Securities Act). The Securities Act contains many exemptions from the Act's registration requirements. See *id.* Those exemptions grounded in §§ 3(a)(11), 3(b), and 4(2) have been of especial importance. See *id.* at 298-395 (discussing §§ 3(a)(11), 3(b), and 4(2)).

12. See, e.g., *SEC v. Ralston Purina Co.*, 346 U.S. 119, 126 (1953) (holding that issuer relying on exemption has burden of proving exemption's availability); *SEC v. Culpepper*, 270 F.2d 241, 246 (2d Cir. 1959) (stating that issuer relying on exemption has burden of proving exemption's availability); *Gilligan, Will & Co. v. SEC*, 267 F.2d 461, 466 (2d Cir. 1959) (same); *SEC v. Sunbeam Gold Mining Co.*, 95 F.2d 699, 701 (9th Cir. 1938) (stating that terms of exemption must be strictly construed against one seeking to rely on exemption); Securities Act Release No. 33-4552, 1 Fed. Sec. L. Rep. (CCH) ¶ 2783, at 2922 (Nov. 6, 1962) (stating that terms of exemption are to be strictly construed against claimant who also has burden of proving exemption's availability).

separate exempt transactions that in fact are parts of a single large financing effort may not, when so viewed, meet the exacting requirements of the hoped-for exemptions. As a result, none of the transactions may qualify for the putative exemption, and all may violate section 5 of the Securities Act, thereby exposing the issuer, and conceivably others, to liability under section 12(1).¹³ In short, earlier (or later) approaches to the capital markets might jeopardize the legal status of later (or earlier) approaches.

To regard an apparently discrete capital financing transaction as, in fact, a part of another transaction is, in a word, to "integrate" the two transactions. Although not expressly a part of federal securities statutes, and even though securities lawyers view the concept as an unsettling nuisance, the doctrine of integration has played a vital role in the framework of federal regulation of securities almost since the Securities Act's inception.¹⁴ Without the doctrine, opportunistic issuers could split an undeniably nonexempt transaction, *i.e.*, a public offering, into two or more components and seek to qualify each of the components under one or more exemptions. The effect would be to subvert the Securities Act by avoiding the very predicate of registration—the existence of a "public offering." Thus, while today the concept of integration is much maligned and remains a continuing source of frustration because of its admittedly crude and hazy configuration, the notion of integration is a doctrinal construct born of regulatory necessity. This remains true even as heightened attention has been given in recent years to yet another policy objective of the Securities Act—fostering capital formation.¹⁵ In this altered regulatory environment the doctrine of integra-

13. See 15 U.S.C. § 77l(1) (1982) (holding liable any person who offers or sells securities in violation of § 77e of Securities Act). Clearly, the issuer faces liability as a "seller" under § 12 of the Securities Act. See *Pinter v. Dahl*, 108 S. Ct. 2063, 2075-83 (1988) (considering whether court may hold defendant liable under § 12(1) as statutory seller). In *Pinter* the United States Supreme Court articulated guidelines for determining who else may face liability under § 12(1). *Id.* at 2076-77. Courts have applied, and undoubtedly will continue to apply, the *Pinter* guidelines in § 12(2) cases. See, *e.g.*, *Abell v. Potomac Ins. Co.*, 858 F.2d 1104, 1113-15 (5th Cir. 1988) (applying *Pinter* guidelines).

14. See *In re Unity Gold Corp.*, 3 S.E.C. 618, 623-26 (1938) (analyzing whether offerings constituted separate "issues"); *cf.* Securities Act Release No. 33-97, 1 Fed. Sec. L. Rep. (CCH) ¶ 1027, at 2056 (Dec. 28, 1933) (stating that intrastate offering exemption is available only if entire issue is sold to residents within single state).

15. Congress is quite solicitous of the capital raising needs of small business. For example, pursuant to the Small Business Investment Incentive Act, Pub. L. No. 96-477, 94 Stat. 2275 (1980), Congress in 1980 increased the § 3(b) ceiling from \$2,000,000 to the section's current level of \$5,000,000. Congress also adopted § 4(6), which exempts "transactions involving offers or sales by an issuer solely to one or more accredited investors," provided that the following requirements are met: (1) the aggregate offering price does not exceed \$5,000,000, (2) the issuer files a notice with the SEC in prescribed form, and (3) "there is no advertising or public solicitation in connection with the transaction by the issuer or anyone acting on the issuer's behalf." 15 U.S.C. §§ 77c, 77d(6). The same year Congress passed the Omnibus Small Business Capital Formation Act, Pub. L. No. 96-477, 94 Stat. 2291 (codified as amended at 15 U.S.C. §§ 80c-80c-3 (1980)), which required the SEC to "use its best efforts to identify and reduce the costs of raising capital in connection with the issuance of securities by firms whose

tion still is needed, but the doctrine is subjected to an additional strain because it must continue to serve the original goal of investor protection while not unduly stifling capital formation, particularly for smaller businesses. Whether traditional formulations of the integration concept are (or can be) sufficiently certain and "bright-line" so as not to dissuade legitimate capital formation efforts, on the one hand, while remaining sufficiently fluid to capture those efforts that should be subjected to registration on investor protection grounds, on the other hand, is the root issue today.

Remaining mindful of the all-important but possibly evolving policy underpinnings of the integration doctrine, from the standpoint of both an issuer's lawyer and a policymaker the initial question of whether a specific financing transaction is exempt from the registration requirements of the Securities Act turns on the meaning of certain key words used in the exemption provisions, words that the Securities Act itself does not define. For example, section 3(a)(11) exempts from section 5 of the Securities Act any security that is "part of an issue" offered and sold only to persons residing within a single state.¹⁶ The traditional policy rationale for this exemption is that states can provide the regulatory oversight needed to protect their residents from capital raising activities occurring wholly within their borders. So far as integration of two or more capital-seeking overtures is concerned, the usual question that has arisen under section 3(a)(11) is phrased as a definitional one, whether the SEC or a court might consider an earlier or later overture to be "part of an issue"¹⁷ and, if so, whether the earlier or later financing as combined with the other transaction still complies with the stringent requirements of section 3(a)(11).¹⁸ In actuality, of course, that ostensibly definitional question traditionally has been an-

aggregate outstanding securities and other indebtedness have a market value of \$25,000,000 or less" and to report annually on the SEC's efforts in this regard, *Id.* at § 506, 15 U.S.C. § 80c-3 (1980). The goal of fostering capital formation must be accommodated to the goal of investor protection in the SEC's regulatory initiatives. *See, e.g.*, Securities Act Release No. 33-6389 [1981-82 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,106, at 84,907 (stating that regulation D was promulgated to facilitate capital formation consistent with protection of investors).

16. 15 U.S.C. § 77c(a)(11) (1982).

17. *See* Unity Gold Corp., 3 S.E.C. 618, 625 (1938) (stating that whether offering is "part of an issue" depends upon whether offerings are related part of plan or programs); Peoples Sec. Co., Securities Exchange Act Release No. 34-6176 (Feb. 10, 1960) (same); Securities Act Release No. 33-4434, 1 Fed. Sec. L. Rep. (CCH) ¶¶ 2271-72 (Dec. 6, 1961) (discussing determination of whether offering is "part of an issue"); L. LOSS, FUNDAMENTALS OF SECURITIES REGULATION 297-98 & n.d (2d ed. 1988) (discussing consequences of issuer offering or selling any part of § 3(a)(11) issue to nonresident). The same interpretive problem arises under § 3(a)(9), under § 3(b), and under rule 147, which was promulgated pursuant to § 3(a)(11).

18. *See* Opinion of the General Counsel, Securities Act Release No. 33-1459, 1 Fed. Sec. L. Rep. (CCH) ¶¶ 2260-62, at 2605-07 (May 29, 1937) (discussing § 3(a)(11) requirements); SEC v. Hillsborough Inv. Corp., 173 F. Supp. 86, 87-88 (D.N.H. 1958), *permanent injunction*, 176 F. Supp. 789, 790 (D.N.H. 1959), *aff'd on other grounds sub nom.*, Hillsborough Inv. Corp. v. SEC, 276 F.2d 665, 668 (1st Cir. 1960) (stating that any sale to nonresidents would destroy § 3(a)(11) exemption as to all securities that are part of that issue).

swered in a way that reflects a singular, unyielding policy objective of investor protection as achieved by registration, an objective partially at odds with the goal of facilitating capital formation.

The same integration question from a related policy standpoint arises under a somewhat different linguistic formulation with respect to the section 4(2) exemption. Section 4(2) exempts transactions by an issuer "not involving any public offering."¹⁹ To this day the precise rationale(s) of this important exemption remain murky, but many contend that certain kinds of persons simply do not need the protections that registration affords.²⁰ While the contour of section 4(2) needs a thorough revisiting in light of the Securities Act's twin goals of investor protection and capital formation, the seemingly narrower interpretive question is whether the integration doctrine will serve to join two seemingly separate financings so that, taken together, the two financings do indeed "involve" a "public offering" in that the combined offerings no longer fall within the blurry but strict requirements of the section 4(2) exemption. In fact, a proper resolution of this apparently narrow integration question requires appreciation of the interrelationship of the integration doctrine and the larger purposes of the Securities Act.

If the most basic objective of the Act is assumed to be registration itself—rather than registration as one (possibly preferred) means for achieving more basic goals such as investor protection through the dissemination of information and encouraging capital formation—in asking whether two financings are "part of an issue" the inquiry is not really directed toward determining whether the more basic goals themselves are being disserved by failing to integrate. Instead, registration alone is the norm against which issuer conduct is evaluated. With respect to section 4(2), even more so than with section 3(a)(11), however, the underlying purposes for the exemption should be relevant to the question of whether two financings will be integrated so as to lose the exemption. In that way exempted capital formation activity is not viewed simply as a deviation from the norm of registration, but as activity to be affirmatively valued and as achieving the explicit policy objectives of the Securities Act. Doing so in the integration context requires forthright consideration of what exactly investors would have gained by the registration that should have occurred if two financings are integrated—more and better information or "just" SEC review²¹—and

19. 15 U.S.C. § 77d(2) (1982).

20. See *Section 4(2) and Statutory Law—A Position Paper of the Federal Regulation of Securities Committee*, 31 BUS. LAW. 485, 489-95 (1975) (discussing conditions of § 4(2) exemption); Fletcher, *Sophisticated Investors Under the Federal Securities Laws*, 1988 DUKE L.J. 1081, 1120-24 (1988) (discussing § 4(2) cases in which courts emphasize that sophisticated offerees do not need protection that registration provides).

21. The question of what investors would have gained by a registration of securities that should have occurred if two financings are integrated is an even more basic question than whether and how "sophistication" ought to matter for § 4(2) and other provisions of the federal securities laws, a subject recently dealt with by Professor Fletcher. See Fletcher, *supra* note 20, at 1120-24 (discussing importance of offerees' sophistication). As far as exemption

what the investors lost in the exempted transactions. While courts may not be well equipped to formulate the integration doctrine so as to affirmatively value capital formation activity, the SEC certainly is.

The same problem exists with respect to transactions grounded in section 3(b) as provided for in rules 504 and 505 of regulation D and those "safe harbor" section 4(2) transactions provided for in rule 506 of regulation D. Section 3(b) states that no "issue" of securities sold under that subsection may exceed \$5,000,000,²² while rule 502(a) of regulation D states that all sales that are "part of the same regulation D offering must meet all of the terms and conditions of regulation D."²³ Thus, if a round of financing under regulation D is integrated with an apparently separate round of financing and so viewed as one financing, the separate rounds must, taken together, meet the requirements of a particular rule under regulation D or, unless the separate rounds happen to comply with the terms and conditions of yet another exemption, the offering will violate section 5 of the Securities Act.

Again, if registration as an end in itself is the benchmark against which all capital formation activity is to be assessed, perhaps it is appropriate that the slightest aberration should expose issuers to liability. But that is to put little, indeed no, weight on the other side of the balance—the good to be realized by prudent but energetic capital formation, especially by smaller businesses, and the way in which material information can be disseminated successfully to investors in exempt transactions. Essentially, one can engage in a quest for capital, but entirely at one's own risk, and with little sympathy for error. Error is error, however minor, even if the larger purpose of the law is fulfilled; close counts only in horseshoes.

While placing the burden of nonregistration on issuers may be entirely appropriate, it would be immensely beneficial for both the doctrine of integration and the doctrine that has grown up around exempt transactions to clarify precisely what are the advantages of registration. By rule 502(b) under regulation D, and in accordance with sound practice under other

from registration is concerned, financial sophistication is an important, but not sufficient, condition, particularly if access to material information is lacking. Yet, *if* access to material information is provided, why does investor sophistication matter for an exemption from registration if sophistication is not a qualification for purchasing in a *registered* offering? Rather than continuing to accept the distinction between "sophisticated" and "unsophisticated" investors as relevant for § 4(2) exemption purposes, but not for registration, the SEC might usefully focus on the kind and quality of information provided as the chief basis for an exemption. So far, the SEC has not done that and, therefore, the significance of registration is not what most commentators in the post-*Ralston Purina* era believe it is—*i.e.*, access to registration information—since near-equivalent information is provided (and can be so mandated) in many exempted transactions, but rather is the interjection of SEC review and comment. This is odd given that, in recent years, few repeat registrants have had their registration statements reviewed by the SEC with any thoroughness. Loss, *supra* note 17, at 124.

22. 15 U.S.C. § 77c (1982).

23. 17 C.F.R. § 230.502(a) (1985).

exemptions, prospective investors in these transactions receive registration statement-like information. Investors also receive the constraints on issuer behavior as are imposed by the application of significant liability provisions.²⁴ What investors in exempt transactions do not receive is SEC review. While not insignificant, the value of that oversight should be weighed against, first, the benefits of exempted capital activity and the mandated disclosure of information and fraud safeguards that continue to accompany that activity and, second, the awesome liability exposure flowing from the later integration of two or more financings and the potential chilling effect of that risk on capital formation. Such an appraisal should expressly inform the shape of the exemption and integration doctrines and the possibly toned-down consequences for running afoul of those doctrines.

Putting the problem of integration to the side for a moment, the quest with respect to all of the transactional exemptions historically has been to draw on experience to decipher the authoritative hallmarks of an "issue" or an "offering"—a kind of exercise in legal taxonomy in which one concludes that the presence of certain "markers" evidences the existence of some more elemental legal condition just as the presence of tusks, a trunk, and certain physical dimensions evidence the existence of an elephant. Not knowing an "issue" or "offering" by sight, those lawyers working in the securities area carefully review the list of supposedly objective features commonly or invariably associated with an exemption's existence. Thus, under section 3(a)(11) much attention is given to notions of "residency" and "doing business." Additionally, under section 4(2) the financial sophistication of offerees and the manner of offering have come to be important to complying with the exemption. Various SEC rules have sought to lend a measure of certainty to this task by creating certain "safe harbors."

Proceeding by inference is difficult enough when the question is simply whether a *single* financing transaction qualifies for a particular exemption, if only because the problem of assigning relative weights to the various markers raises the usual array of classification questions. Is a putative section 4(2) transaction really a private placement if the placement lacks a particular characteristic? Is a beast without two tusks an elephant? Returning to the problem of integration, the complexity quickly compounds when the question is not simply whether a single financing passes muster under a particular exemption, but also whether the financing is "part of" or "involves" yet another financing. Here, too, the inclination has been to concoct a supposedly definitive (and necessarily vague so as to cover all cases) list of attributes that indicates whether or not one capital transaction is "part of" or "involves" another capital transaction. Thus, at least since the early 1960s, when the SEC promulgated its famous five-factor formula for integration, much has been heard about whether two capital market overtures are "part of a single plan of financing;" "involve issuance of the

24. See 15 U.S.C. §§ 77k, 77l (1982); *supra* note 10 and accompanying text (discussing liability sections of Securities Act).

same class of securities;" involve sales "made at or about the same time;" require the "same type of consideration;" or are made for the "same general purpose."²⁵ Once two capital transactions are integrated pursuant to this vague prescription, one then resorts to the first set of markers to determine whether the larger transaction itself possesses the requisite number of qualifying features of an exemption. If not, then it matters not at all that investors received all material information and have the protection of the liability provisions of the Securities Act and the Exchange Act. The absence of registration—thus the absence of SEC review—is fatal.

What may be lost in this talismanic approach is an appreciation of the inescapable manner in which focusing on seemingly objective, definitional, and linguistic matters is an attempt to identify properties that are believed to *correspond to*, but are *not the same as*, the terms being defined. The wooden reliance on traits always poses the risk of under- or over-inclusiveness. Furthermore, the properties themselves—*e.g.*, a "single plan of financing"—require the very defining they were meant to supply for the more elemental terms "issue" and "offering." Thus, several terms must be defined or construed instead of one. Most important, however, a mechanical and cataloging approach to this matter diverts attention from the fact that the whole descriptive enterprise is policy driven. Furthermore, the enterprise is driven erratically when the policies themselves—*i.e.*, the baseline policies to be achieved by registration and exemptions and, hence, integration—are, as at present, somewhat uncertain or in a state of flux.²⁶

25. In 1961, the SEC addressed the integration issue in connection with § 3(a)(11) by stating the following:

Any one or more of the following factors may be determinative of the question of integration: (1) are the offerings part of a single plan of financing; (2) do the offerings involve issuance of the same class of security; (3) are the offerings made at or about the same time; (4) is the same type of consideration to be received, and (5) are the offerings made for the same general purpose.

Securities Act Release No. 33-4434, 1 Fed. Sec. L. Rep. (CCH) ¶ 2272, at 2608 (Dec. 6, 1961). According to the preface, the presence of a single factor may lead to integration under § 3(a)(11) and, because the same formulation is used in rule 147, under that rule as well.

In 1962 the SEC addressed the integration issue in connection with § 4(2). See Securities Act Release No. 33-4552, 1 Fed. Sec. L. Rep. (CCH) ¶¶ 2770-83, 2918-22 (Nov. 6, 1962). The SEC again recited the five factors enumerated in 1961, but stated that the factors are merely "relevant to [a] question of integration." *Id.* at ¶ 2781. As noted by Jennings and Marsh, the SEC said nothing as to what weight should be given to the various factors, whether a single factor might be determinative, or why the formulation differs from the formulation under § 3(a)(11) and rule 147. JENNINGS & MARSH, *supra* note 9, at 441.

26. The American Bar Association's Committee on Federal Regulation of Securities stated that, originally, the goal of the Task Force on Integration was "to formulate an analytical matrix, based upon objective criteria, for resolving all integration problems." American Bar Association, Committee on Federal Regulation of Securities, *Integration of Securities Offerings: Report of the Task Force on Integration*, 41 BUS. LAW. 595, 597 (1986) [hereinafter *ABA Task Force Report on Integration*]. That effort was abandoned in favor of devising a number of additional safe harbors because "the wide variety of offerings, securities offered, exemptions relied upon, and other relevant factors make such a comprehensive, analytical matrix virtually impossible to formulate." *Id.* at 624. We suspect a better reason

For an issuer of securities that seeks funding in the capital markets only once, or after relatively long intervals, the metaphysical mysteries of integration and its relationship to larger policies of the Securities Act are of no concern. Instead, these issuers are more interested in knowing with some certainty that their singular offerings will meet the fairly strict conditions of the transactional exemptions. Recent SEC adoption of new rule 508 may improve the chances that these issuers will succeed in that quest.²⁷ However, for the many issuers who seek capital with some regularity, integration may serve, with the clarity that only twenty/twenty hindsight accords, to unravel a carefully planned series of capital market overtures. The consequences can be dramatic, especially as one seemingly minor miscue can undermine an issuer's contention that the offerings are distinct and that the offerings' separate identities should remain intact.²⁸ Such issuer faces SEC enforcement action, as well as the prospect of investor claims for rescission, a course of action that could be financially devastating. In the interim, the issuer that becomes aware of the likely prospect of integration faces the decision of whether and how to reveal the contingent liability on the issuer's financial statements,²⁹ financial statements that may be reviewed by lenders, current shareholders, or even future investors and regulatory authorities in a later public offering. As with other mischief, the consequences of the legal mischief created by the concept of integration quickly can be magnified. Because of this issuers and their legal counsel long have sought relief from the hazards associated with the integration doctrine. As we will see, through its recent rule 152 responses the SEC has provided a partial antidote, but the SEC fails to see that convincing resolution of the integration puzzle depends, above all, on coming to a clearer understanding of the place of (and requirements of) exemptions from registration in the overall securities law regime.

for not tackling the whole of the integration issue is that until certain bedrock policy issues concerning the purpose of registration and exemptions therefrom are rethought in light of modern conditions, such an effort is inappropriate and futile.

27. See Securities Act Release No. 33-6825, 54 Fed. Reg. 11,369, 11,374 (1989) (to be codified at 17 C.F.R. § 230.508) (adopting new rule 508 as amendment to regulation D). New rule 508 essentially provides a defense against civil liability for selling securities without registration of the securities in reliance on substantial compliance with regulation D. See *id.* (describing application of new rule 508). For a thorough treatment of new rule 508 and other proposed changes to regulation D, see Schneider, *A Substantial Compliance ("I&I") Defense and Other Changes Are Added to SEC Regulation D*, _____ BUS. LAW. _____ (forthcoming 1989). To qualify for the defense, the failure to comply with the regulation D requirements must be insignificant and the party relying on the exemption must have acted in good faith and with a reasonable attempt to comply. Securities Act Release No. 33-6825, 54 Fed. Reg. 11,369, 11,374 (1989) (to be codified at 17 C.F.R. § 230.508).

28. The SEC believes that a single offer or sale to an unqualified offeree destroys the exemption for the entire issue. Loss, *supra* note 17, at 297 n.d.

29. Professor Loss believes that the SEC would require the registration statement to disclose a contingent liability under § 12(1) for selling in violation of § 5. *Id.* See *In re Hayes Mfg. Corp.*, 23 S.E.C. 574, 581-87 (1946) (discussing deficiencies in original registration statements).

II. THE PROBLEM: INTERPRETING RULE 152.

Rule 152 in its present form reads as follows:

DEFINITION OF "TRANSACTIONS BY AN ISSUER NOT INVOLVING ANY PUBLIC OFFERING" IN SECTION 4(2) FOR CERTAIN TRANSACTIONS.

The phrase "transaction by an issuer not involving any public offering" in Section 4(2) shall be deemed to apply to transactions not involving any public offering at the time of said transaction although subsequently thereto the issuer decides to make a public offering and/or files a registration statement.³⁰

The SEC adopted rule 152 in 1935, just two years after Congress enacted the Securities Act.³¹ Having been adopted so soon after passage of the Securities Act, the SEC must have regarded the rule as important for carrying out the purposes of that momentous legislation. Yet, the available administrative history of rule 152 does not fully explain the situation(s) to which the SEC originally intended the rule to apply.³² The Securities Act release announcing the SEC's adoption of rule 152 is the only official statement of rule 152's purpose, and the release is distressingly brief.³³ Furthermore, the SEC apparently did not apply the rule to any specific situation until 1986, when it issued a no-action letter expressing its surprising interpretation of the rule.³⁴

In addition to the sparse history concerning the purposes and scope of rule 152, an inherent problem with the rule is its linguistic ambiguity, particularly the problem of identifying the exact referent of the issuer's post-section 4(2) offering behavior.³⁵ In other words, the interpretive problem is to determine precisely what action an issuer may take "subsequently thereto" without vitiating the private placement exemption. The difficulty occurs primarily because of the SEC's unsound use of conjunctive/disjunctive language in drafting the rule.³⁶ That confusing drafting convention

30. 17 C.F.R. § 230.152 (1985).

31. See Securities Act Release No. 33-305 (Mar. 2, 1935) (available from SEC; reprinted in Appendix) (adopting rule 152).

32. See *infra* notes 33-34 and accompanying text (discussing sparsity of material concerning rule 152's purpose).

33. See Securities Act Release No. 33-305 (Mar. 2, 1935) (available from SEC; reprinted in Appendix) (adopting rule 152).

34. See Verticom, Inc., SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file) (interpreting rule 152 to preclude integration of successfully completed private placement and subsequent registered public offering); *infra* notes 61-69 and accompanying text (discussing Verticom no-action letter, which was SEC's first application of rule 152).

35. See 17 C.F.R. § 230.152 (1985) (containing rule 152); *supra* note 30 and accompanying text (reprinting rule 152); *infra* notes 36-37 and accompanying text (discussing ambiguity of rule 152).

36. See *supra* note 30 and accompanying text (reprinting rule 152); *infra* notes 37-38 and accompanying text (discussing ambiguity that rule 152's conjunctive/disjunctive language creates).

makes unclear whether the *subjective* decision to make a public offering or only the *objective* filing of a registration statement must be made subsequent to the section 4(2) placement to come within the rule. Thus, a close reading of the rule reveals that the wording is ambiguous and that the rule can be read in at least three very different ways.³⁷ The following subparts seek to sort through the ambiguities and explain in detail the rule's possible interpretations.³⁸ Later, we describe the interpretation adopted by the SEC and offer an extended critique of its choice.

A. Interpretation One.

In interpreting rule 152 the SEC could read the rule to say:

The phrase "transaction by an issuer not involving any public offering" in Section 4(2) shall be deemed to apply to transactions not involving any public offering at the time of said transaction although subsequently thereto the issuer *decides to make a public offering* [and/or files a registration statement].³⁹

Under this interpretation rule 152 would preclude integration of a private placement of securities followed closely by a public offering of yet additional securities *only* if the issuer decided to make the public offering after the issuer undertook, and presumably completed successfully, the private place-

37. See *infra* notes 39-60 and accompanying text (discussing three interpretations of rule 152).

38. See *infra* notes 39-60 and accompanying text (discussing ambiguity of rule 152's language). Some of rule 152's ambiguity stems from reliance on a widely-used and beguiling technique of drafting—the use of "and/or"—to describe coverage. See 17 C.F.R. § 230.152 (1985) (containing rule 152); *supra* note 30 and accompanying text (reproducing rule 152); *supra* notes 35-38 and accompanying text (discussing ambiguity that rule 152's conjunctive/disjunctive language creates). One commentator concisely has described the unexpected legal trouble that the hybrid conjunction and disjunctive has caused in other settings. See B. CHILD, DRAFTING LEGAL DOCUMENTS 55-56 (1988) (discussing problems that lawyers' use of "and/or" has caused). As Child notes, knowledgeable drafters uniformly have rallied against the hybrid conjunction and disjunctive, and judges have construed the hybrid conjunction and disjunctive against lawyers who have used it. See McCarty, *That Hybrid "and/or"*, MICH. ST. B.J., May 1960, at 9 (discussing cases in which judges have construed "and/or" against lawyers who use that phrase); see B. CHILD, DRAFTING LEGAL DOCUMENTS 55 (1988) (discussing fact that judges have construed "and/or" against lawyers who use it). Yet another instructor of legal drafting explains how use of the phrase "and/or" sometimes results in redundancy and other times in outright contradiction. See D. MELLINKOFF, LEGAL WRITING: SENSE AND NONSENSE 55-56 (1982) (discussing problems that "and/or" creates). In explaining how that drafting convention creates contradiction or redundancy, Mellinkoff notes that lawyers who use "and/or" are lawyers in a hurry and who are content to let others solve the problems that the lawyers create by imprecise writing. *Id.* The commentator explains that lawyers can remove the ambiguity that "and/or" creates simply by replacing "and/or" with "A or B or both" when such specification is necessary. *Id.* at 56. The unfortunate ambiguity of rule 152 illustrates the inappropriateness of the use of "and/or." See *infra* notes 39-60 and accompanying text (discussing ambiguity that language of rule 152 creates).

39. See 17 C.F.R. § 230.152 (1985) (containing rule 152) (emphasis added); *supra* note 30 and accompanying text (reprinting rule 152).

ment.⁴⁰ Under Interpretation One, assuming the unavailability of another “safe harbor” precluding integration, the SEC could draw on its five-factor formula to integrate any other public offering closely following a private placement. Interpretation One focuses on the issuer’s subjective intent and thus requires an almost impossible fathoming of what combination of subjective intent and objective manifestation of that intent constitutes “deciding.”⁴¹ As such, the rule affords virtually no reliable protection for an issuer required to demonstrate the time at which the issuer’s financing decisions were made. Another problem with Interpretation One is that it apparently, although maybe inadvertently, rewards an issuer who successfully completes a private offering but only then discovers either that the issuer has not received adequate capital to finance the project for which the issuer undertook the private offering or that the issuer now needs funds for a different project.⁴² On the other hand, the issuer who plans to complete a private placement before launching a public offering may not rely on the rule to preclude integration of the two financings because the issuer’s “decision” to make the public offering was made *prior to* the private placement. Finally, whether the term “public offering” includes exempt “public offerings”—such as widely-offered intrastate or rule 504 transactions—or only registered public offerings is not clear. While the use of both the term “public offering” and the term “registration statement” in the text of the rule supports inclusion of nonregistered public offerings within the scope of the rule, the use of the conjunctive “and” indicates that the public offering must also be registered. That, however, then raises the larger question of what purpose the word “or” serves. “Or” seems to import a more objective alternative—*filing* a registration statement, as opposed to subjectively *deciding* to make a public offering, may also bring an issuer within the rule. As such, the disjunctive language reveals the inherent weakness of Interpretation One.⁴³

To illustrate the application of Interpretation One, suppose that Issuer A wishes to obtain \$1,000,000 through a section 4(2) private offering. Having successfully completed the private offering, Issuer A discovers that \$1,000,000 will not fully cover the costs of the project. Issuer A then follows the private offering with a registered public offering of an additional \$1,000,000 worth of securities. Under Interpretation One, rule 152 appar-

40. See *infra* note 44 (discussing commentators who interpret rule 152 to preclude integration of exempt private offering with subsequent public offering if issuer decided to make public offering after issuer made private offering).

41. See *supra* note 39 and accompanying text (emphasizing in Interpretation One issuer’s decision to make public offering after issuer makes private offering).

42. See *infra* notes 44-45 and accompanying text (explaining that Interpretation One bestows bonanza on good faith issuer who underestimates capital that issuer wants from private offering); *infra* note 44 (discussing commentators’ interpretations of rule 152 that rule apparently allows issuer who underestimates capital that issuer needs from private offering to complete private offering by undertaking public offering).

43. See *supra* notes 34-38 and accompanying text (discussing ambiguity that “and/or” creates).

ently precludes integration of the two offerings, even though in retrospect both offerings are for the same purpose.⁴⁴ However, the interpretation provides no protection from integration for the issuer who, prior to commencing one or more private offerings, decides that the private placement(s) will be followed by a registered public offering of additional securities—the so-called “multi-round financing.” Moreover, this is so whether the purpose of the subsequent public offering is to raise additional funding for the project originally to have been financed wholly privately—a likely candidate for integration—or is to raise capital for a wholly separate undertaking—an unlikely candidate for integration. Thus, Interpretation One not only bestows a bonanza on shortsighted issuers who miscalculate their capital needs for a specific project, but the interpretation also does not offer reliable protection against integration for farsighted issuers seeking to fund one project via private financing and another project via public financing. The latter issuers, equally deserving of certainty in planning their capital financing activities, must seek uncertain solace in the traditional five-factor test.⁴⁵ In short, Interpretation One leads to anomalous outcomes, uncertainty of application, and little practical benefit.

B. Interpretation Two.

Alternatively, the SEC could read rule 152 to say:

The phrase “transaction by an issuer not involving any public offering” in Section 4(2) shall be deemed to apply to transactions not involving any public offering at the time of said transaction

44. See *supra* note 39 and accompanying text (containing text of Interpretation One of rule 152). Some commentators assert that rule 152 applies anytime an issuer makes a private offering of securities and subsequently decides to make a public offering of securities. See 3 H. BLOOMENTHAL, *SECURITIES AND FEDERAL CORPORATE LAW* § 4.14[5][a], at 4-214—4-215 (1988) (stating that rule 152 is applicable only if issuer subsequently decides to make public offering); Stevenson, *Integration and Private Placements*, 19 REV. OF SEC. & COMMODITIES REG. 49, 55 (1986) (stating, without recitation of authority, that SEC interprets rule 152 to apply only where decision to undertake public offering is made subsequent to private placement). No evidence exists, however, to show convincingly that the SEC adopted rule 152 to assist issuers who make a good faith mistake about the amount of money needed for a particular corporate project, or who fortuitously made their public offering decision subsequent to their private placement. See *supra* notes 32-34 and accompanying text (discussing sparse history of rule 152's purpose); *infra* note 45 and accompanying text (discussing inconsistency of Interpretation One with doctrine of integration). No language is present in the SEC release adopting rule 152 to support the idea that a shortsighted issuer of securities through a private offering can escape integration if the issuer follows the private offering with a public offering. See Securities Act Release No. 33-305 (Mar. 2, 1935) (available from SEC; reprinted in Appendix) (adopting rule 152 and briefly stating purpose of rule). From the standpoint of investor protection, no reason exists for the SEC to treat a shortsighted issuer who either miscalculates the amount of capital that the issuer needs from a private offering or otherwise “subsequently” decides to make a public offering differently from other issuers who may try to circumvent the registration requirements.

45. See *supra* note 25 and accompanying text (discussing five-factor test that SEC uses to determine whether SEC should integrate separate offerings of securities).

although subsequently thereto the issuer [decides to make a public offering and/or] *files a registration statement*.⁴⁶

This interpretation of rule 152 would allow an issuer's private offering and subsequent registered public offering of additional securities to escape integration in any case where an issuer *files* a registration statement after having made a private placement of securities.⁴⁷ Interpretation Two is a broader interpretation of rule 152 than Interpretation One because under Interpretation Two the SEC would focus on an issuer's objective act of *filing* a registration statement.⁴⁸ In contrast, under Interpretation One the focus is on the subjective intent ("decides") of an issuer during a particular period.⁴⁹ If rule 152 allows an issuer's private offering and subsequent public offering to escape integration when the issuer subsequently registers securities for a public offering, as Interpretation Two suggests, the rule would allow the issuer to plan both a private offering of securities and a subsequent public offering of additional securities before undertaking the initial private offering.⁵⁰ Additionally, Interpretation Two allows this sort of planning whether the subsequent public offering is for a distinct purpose or for exactly the same purpose as the private placement.

The following example illustrates the applicability of Interpretation Two. Suppose Issuer B wishes to obtain \$2,000,000. Issuer B plans to obtain \$1,000,000 through a section 4(2) private offering and \$1,000,000 through a public offering that would immediately follow completion of the private

46. See 17 C.F.R. § 230.152 (containing rule 152) (emphasis added); *supra* note 30 and accompanying text (reprinting rule 152).

47. See *infra* notes 61-90 and accompanying text (discussing no-action letters in which SEC interprets rule 152 to preclude integration of exempt private offering and subsequent public offering if issuer registers public offering after having made private offering).

48. See *supra* notes 39-45 and accompanying text (discussing Interpretation One of rule 152, which precludes integration of private offering with subsequent public offering if issuer decides to make public offering after undertaking private offering). If the SEC originally intended rule 152 to preclude integration merely upon an issuer's filing of a registration statement, no materials exist to clarify why the SEC included the phrase "decides to make a public offering" in the rule. See *supra* notes 31-34 and accompanying text (discussing sparse history of rule 152). Logic requires that an issuer who subsequently files a registration statement covering a public offering already has decided to make a public offering. See Securities Act of 1933 § 5, 15 U.S.C. § 77e (1982) (requiring registration of public offerings). Thus, rule 152 might serve the rule's purpose if the rule stated:

The phrase "transaction by an issuer not involving any public offering" in Section 4(2) shall be deemed to apply to transactions not involving any public offering at the time of said transaction although subsequently thereto the issuer files a registration statement.

See 17 C.F.R. § 230.152 (1985) (containing rule 152); *supra* note 30 and accompanying text (reprinting rule 152).

49. See *supra* notes 39-45 and accompanying text (discussing Interpretation One of rule 152, which precludes integration of private offering with subsequent public offering if issuer decides to make public offering after issuer undertakes private offering).

50. See *infra* notes 70-82 and accompanying text (discussing SEC no-action letters in which SEC apparently allows issuer to plan to make both private offering and subsequent public offering before issuer undertakes private offering).

offering. Interpretation Two would allow Issuer B to plan this sort of staged financing arrangement and escape integration of the two offerings simply by registering the subsequent public offering even if the two offerings were part of a "single plan of financing" or were conducted for the identical purpose and thus, absent the rule, might be integrated under the traditional five-factor test.⁵¹ In effect, under Interpretation Two integration is never an issue if a particular kind of exempt transaction—a section 4(2) private placement—is in fact followed by, however quickly,⁵² a particular kind of financing—a registered public offering.⁵³ Consequently, Interpretation Two precludes integration of conventional two-round financings—although apparently not two or more section 4(2) placements followed by a registered public offering because the private placements themselves might be integrated with one another even if the private placements (or at least the last of them) would not be integrated with the subsequent public offering. Interpretation Two also apparently sanctions, and possibly invites, precisely what the SEC long ago developed the doctrine of integration to prevent—the practice of dividing what otherwise unquestionably would be one public offering into first an exempt and then a registered component. Although sound policy reasons may exist for reading the rule so broadly, the point for now is simply that the SEC should be alert to the possibly unexpected breadth of such an interpretation. In fact, recent no-action letters indicate that the SEC now construes rule 152 to allow this sort of two-stage financing to occur, but has done so without acknowledging the potential reach of its interpretation and without clearly articulating either the rationale for that interpretation or the interpretation's applicability or limitation in other contexts. In short, Interpretation Two provides partial, if unexplained, relief from the trap of integration.⁵⁴

C. Interpretation Three.

Lastly, the SEC could read rule 152 to state:

The phrase "transactions by an issuer not involving any public offering" as used in Section 4(2) shall be deemed to apply to transactions not involving any public offering at the time of said

51. See *supra* notes 46-50 and accompanying text (discussing Interpretation Two of rule 152); *supra* note 25 and accompanying text (discussing five-factor test that SEC uses to resolve integration questions).

52. Although under Interpretation Two integration is apparently never an issue if a registered public offering follows a § 4(2) placement, whether the SEC, in light of the word "subsequently," also could read rule 152 to allow an issuer to undertake a private placement and a registered public offering *simultaneously* is not clear. See *supra* notes 46-51 and accompanying text (discussing Interpretation Two of rule 152). The question then becomes how broadly the SEC is willing to interpret rule 152.

53. See *supra* notes 46-51 and accompanying text (discussing Interpretation Two of rule 152).

54. See *infra* notes 70-82 and accompanying text (discussing no-action letters in which SEC allowed issuer to plan private offering and subsequent public offering).

transactions although subsequently thereto the issuer *decides to make a public offering and/or file[s] a registration statement* [(with respect to the securities as were offered but not sold in the Section 4(2) placement)].⁵⁵

Interpretation Three does not require choosing between an emphasis on the subjective intent of the issuer—as in Interpretation One—or the objective act of the issuer—as in Interpretation Two. Instead of implicitly referring to a decision to make, or the filing of a registration statement pertaining to, a separate subsequent public offering of *additional* securities, however, Interpretation Three's language is much narrower and refers only to a public offering of, and a registration statement covering, the securities offered but not sold in the original private offering. Under this interpretation, and unlike Interpretation Two, rule 152 alone would not preclude integration of a separate registered public offering of *additional* securities with an initial private placement.⁵⁶ Indeed, rule 152 would not apply at all to a situation where an issuer undertakes a private offering, successfully completes the private offering, and then follows the private offering with a registered public offering.⁵⁷ Rather, the rule addresses only the situation where a registered public offering follows a *failed* private offering, and the public offering is simply an alternative outlet for the disposition of the *unsold* securities, not additional securities.⁵⁸

Illustrative of the application of Interpretation Three is this example. Suppose Issuer C wishes to obtain \$1,000,000 through a private placement. Because Issuer C finds that it is able to sell only \$250,000 worth of securities through the private offering, Issuer C wants to sell the remaining \$750,000 worth of securities through a registered public offering. Interpretation Three of rule 152 would allow Issuer C to offer the unsold securities of the private offering in a subsequent public offering without facing the risk that, with hindsight, the earlier private placement will be deemed to “involve” the public offering avenue chosen to dispose of the unsold securities, a risk that might be substantial given that the offeror seeks to fulfill a single capital-raising venture through alternative means. Without the rule in this instance, the act of registering the unsold securities itself would be the event creating what might be regarded as the second “offering” that then might be “integrated” with the first “offering.” Absent the registration of the

55. See 17 C.F.R. § 230.152 (1985) (containing rule 152) (emphasis added); *supra* note 30 and accompanying text (reprinting rule 152).

56. See *infra* notes 59-60 and accompanying text (discussing applicability of rule 152 to situation where issuer makes private offering but private offering fails, forcing issuer to complete private offering by converting private offering to public offering).

57. See *infra* notes 59-60 and accompanying text (discussing applicability of rule 152 to situation where issuer makes private offering but private offering fails, forcing issuer to complete private offering by converting private offering to public offering).

58. See *infra* notes 59-60 and accompanying text (discussing applicability of rule 152 to situation where issuer makes private offering but private offering fails, forcing issuer to complete private offering by converting private offering to public offering).

unsold securities, no "integration" risk exists because no later overture to the capital markets occurs, only the failed private placement. Unfortunately, Issuer C lacks the desired funds. Without the rule, an issuer who goes forward with registration jeopardizes the exempt status of the earlier attempt to sell the securities. Such an issuer is in a real bind and faces a Hobson's choice: register and by that very act violate the Securities Act or halt the funding effort and face financial failure. To regard the act of registering securities as itself an event that vitiates an exemption for an earlier offering of those securities seems anomalous. Therefore, Interpretation Three of the rule solves Issuer C's dilemma and does so in a sensible manner. But under this interpretation, that is all rule 152 does. Interpretation Three does not address the question of whether the earlier private placement is deficient on some other grounds. It does not address the question of whether the private placement creates a "gun jumping" problem for the later registration.⁵⁹ Nor, importantly, does this interpretation do anything for issuers seeking relief from integration in conventional multiround financing situations. For that, issuers must continue to chart their course through the shoals of the five-factor formula.⁶⁰ We believe Interpretation Three is correct.

III. THE REINCARNATION OF RULE 152.

The SEC appears not to have addressed the function or scope of rule 152 during the first fifty years of the rule's existence.⁶¹ Furthermore, only one court has mentioned the rule, and then only briefly and without shedding any light on the rule's proper construction.⁶² Only in 1986 did the SEC begin using rule 152 to preclude integration in multiround financing situations when, beginning with *Verticom, Inc.*,⁶³ the SEC issued the first of several no-action letters construing the rule.⁶⁴ In *Verticom* the issuer had successfully completed a section 4(2) private placement of convertible debt and was considering a public offering of common stock the registration statement for which would be filed as early as three or four months after the completion date of the private placement.⁶⁵ The SEC essentially took

59. See *infra* notes 186-88 and accompanying text (discussing "gun-jumping" problem).

60. See *supra* note 25 and accompanying text (discussing SEC's use of five-factor formula to determine whether separate offerings should be integrated).

61. See *infra* notes 63-69 and accompanying text (discussing SEC's first interpretation of rule 152 in no-action letter).

62. See *Neuwirth Inv. Fund, Ltd. v. Swanton*, 422 F. Supp. 1187, 1196 (S.D.N.Y. 1975) (noting that rule 152 provides that later registration or registered public offering does not affect the nonpublic nature of original sale).

63. *Verticom, Inc.*, SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file).

64. See *infra* notes 65-90 and accompanying text (discussing no-action letters in which SEC addressed rule 152).

65. *Verticom, Inc.*, SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file). *Verticom* was organized in March 1983 and had raised approximately \$5 million in a series of separate and discrete financing transactions. *Id.* Each of the separate transactions

the position that rule 152 precluded integration of the successfully completed private placement and the registered initial public offering.⁶⁶ In arriving at its conclusion, the SEC explained that, by virtue of rule 152, the act of filing a registration statement following a placement otherwise exempt under section 4(2) does not vitiate the exemption.⁶⁷ In grounding its conclusion on an unprecedented reading of rule 152, the SEC found it unnecessary to address the relevance of the traditional five-factor formula for determining integration.⁶⁸ Thus, in allowing an issuer to escape integration of a private placement with a subsequent public offering of additional securities for which a registration statement would be filed, the SEC adopted the broadest possible interpretation of rule 152—Interpretation Two.⁶⁹

qualified for an exemption from registration pursuant to § 4(2) of the Securities Act. *Id.* Verticom was a high technology start-up company and had received the majority of its funding from professional investors. *Id.* Verticom scheduled the private placement at issue in *Verticom* as the last installment in obtaining venture capital. *Id.* The private placement provided Verticom with the capital that would enable Verticom to finance its operations until it turned the corner in terms of profitability and cash flow. *Id.* Counsel for Verticom characterized Verticom's financing process as contemplating two distinct financing plans. *Id.* The first financing plan was the venture financing phase, in which Verticom expected venture capitalists to provide funds for product development and the initial generation of revenues. *Id.* The second financing plan of Verticom's capitalization process was the public financing phase. *Id.* For purposes of the SEC's analysis of Verticom's situation, the SEC assumed that Verticom would undertake the initial public offering within three to four months of the private placement of securities. *Id.* In making a no-action request, Verticom advanced three arguments as to why the SEC should not integrate the private offering with the subsequent public offering. *Id.* First, Verticom argued that under the traditional five-factor formula, the offerings were independent because the offerings (1) were not part of a single plan of financing and (2) the offerings were not made for the same general purpose. *Id.*; see *supra* note 25 and accompanying text (discussing five-factor formula SEC uses to determine whether integration of securities should result). Verticom conceded that an analysis of the remaining three factors did not yield a result favorable to the Company's position. *Verticom, supra*; see *supra* note 25 and accompanying text (discussing five-factor formula SEC uses to determine whether SEC should integrate securities). Second, Verticom argued that rule 152 suggests that the filing of a registration statement covering a public offering should not vitiate the § 4(2) exemption for an otherwise qualifying private placement concluded prior to such filing. *Verticom, supra*. Finally, Verticom advanced a policy argument. *Id.* Specifically, Verticom argued that no compelling reason existed for integrating the two offerings. *Id.* Verticom stated that the two offerings simply did not represent an attempt to circumvent the registration requirements of the Securities Act through the misuse of the § 4(2) exemption. *Id.*; see *supra* note 7 and accompanying text (discussing reasons for registration requirement of Securities Act).

66. *Verticom, Inc.*, SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file).

67. *Id.*

68. *Id.*; see *supra* note 25 and accompanying text (discussing SEC's use of five-factor formula to determine whether SEC should integrate separate offerings of securities and, thus, require registration of all involved offerings).

69. See *supra* notes 63-68 and accompanying text (discussing SEC's analysis of integration in *Verticom*); *supra* notes 46-54 and accompanying text (discussing Interpretation Two of rule 152, which would preclude integration of private offering and subsequent public offering if issuer files registration statement for public offering after issuer undertakes private offering). The SEC applied essentially the same interpretation of rule 152 in *The Immune Response*

The SEC again interpreted rule 152 in *Vulture Petroleum Corp.*⁷⁰ In its no-action request, Vulture Petroleum Corporation sought the views of the SEC concerning the possible integration of a future registered public offering of common stock with a currently contemplated sale of common stock pursuant to rule 506 of regulation D.⁷¹ The issuer cited the *Verticom* letter in support of its request and argued that, because rule 506 is grounded in section 4(2) of the Securities Act, rule 152 ought to apply to prevent integration.⁷² The SEC agreed with the request, taking the position that rule 152 precluded integration of the proposed placement of securities under rule 506 with the later registered public offering.⁷³ Although the SEC did not state specifically the reason for interpreting rule 152 as it did, apparently the SEC construed the rule to categorically preclude integration of a section 4(2) private offering and a subsequent public offering of additional securities for which an issuer files a registration statement.⁷⁴ In short, once again the SEC adopted Interpretation Two of the rule.⁷⁵

The facts in *Vulture Petroleum* appear to differ from the facts in *Verticom* in one important respect. *Vulture Petroleum* involved an issuer's contemplation of both a private offering and a subsequent public offering

Corp. as the SEC had applied in *Verticom*. See *The Immune Response Corp.*, SEC No-Action Letter (Nov. 2, 1987) (LEXIS, Fedsec library, Noact file) (interpreting rule 152 to preclude integration of private placement and subsequent proposed registered public offering). In *Immune Response* The Immune Response Corporation requested that the SEC take a no-action position with respect to the integration of the company's completed private placement of securities and a proposed initial public offering to take place within six months of the private placement. *Id.* Immune Response argued that, as in *Verticom*, rule 152 should be available to prevent the company's subsequent filing of a registration statement relating to the company's proposed public offering from vitiating the company's exemption for the private placement. *Id.*; see *supra* notes 63-68 and accompanying text (discussing SEC's interpretation of rule 152 in *Verticom*). In taking a no-action position and reiterating the SEC's prior statements regarding the rule, the SEC relied on rule 152 and stated that the SEC should not integrate the private placement with the proposed registered public offering. *Immune Response, supra*.

70. *Vulture Petroleum Corp.*, SEC No-Action Letter, [1987 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,407, at 77,319 (Dec. 31, 1986).

71. *Id.* *Vulture Petroleum* was wholly-owned by three individuals. *Id.* *Vulture Petroleum* planned to offer common stock solely to certain *Vulture Petroleum* directors and less than 35 other persons in a limited offering that would qualify under rule 506 of regulation D of the Securities Act. *Id.* In its letter of inquiry *Vulture Petroleum* explained that it might undertake a registered initial public offering within six months of the private offering. *Id.* *Vulture Petroleum* argued that, under rule 152, the filing of a registration statement following an offering otherwise exempt under § 4(2) should not vitiate the exemption under § 4(2). *Id.* at 77,320.

72. *Id.* at 77,320.

73. *Id.*

74. See *supra* notes 63-69 and accompanying text (discussing SEC's interpretation of rule 152 in *Verticom* to preclude integration of private offering and subsequent public offering if issuer registers public offering after issuer completes private offering).

75. See *supra* notes 46-54 and accompanying text (discussing Interpretation Two of rule 152, which precludes integration of private offering of securities and subsequent registered public offering of additional securities upon issuer's filing of registration statement).

before *either* offering had taken place.⁷⁶ In *Verticom* the issuer already had completed a private offering before requesting that the SEC take a no-action position with respect to a subsequent public offering.⁷⁷ Arguably, in *Verticom* because the decision to go forward with the public offering was still somewhat uncertain at the time of the no-action request—although the public financing phase had been considered prior thereto—the issuer had *decided* to make a public offering, if at all, only *subsequently* to completion of the private offering. Therefore, *Verticom* might be viewed as reflecting the more cautious, uncertain, and less useful Interpretation One.⁷⁸ In *Vulture Petroleum*, however, any doubts concerning the irrelevance of an issuer's subjective intent were dispelled.⁷⁹ In fact, the position in *Vulture Petroleum* was extended somewhat in *The Immune Response Corp.*⁸⁰ In *Immune Response*, even though the issuer initially relied on rule 505 for the issuer's private placement preceding a public offering, where rule 506 was also available the SEC used rule 152 to preclude integration.⁸¹ Thus, in allowing an issuer to plan both a private placement and a public offering of additional securities to immediately follow the private placement with no danger of the SEC integrating the two transactions, the SEC has extended its position taken in *Verticom* and *Vulture Petroleum* and again embraced the broadest possible construction of the rule—Interpretation Two.⁸²

76. *Vulture Petroleum Corp.*, SEC No-Action Letter [1987 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,407, at 77,319 (Dec. 31, 1986); *supra* notes 70-75 and accompanying text (discussing facts in *Vulture Petroleum*); *cf.* *Verticom, Inc.*, SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file) (issuer requested views of SEC regarding integration of completed private offering with possible future public offering that issuer would undertake within three to four months of private offering); *supra* notes 63-69 and accompanying text (discussing *Verticom* no-action letter).

77. *Verticom, Inc.*, SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file); *see supra* notes 65-69 and accompanying text (discussing facts in *Verticom*).

78. *See supra* note 39-45 and accompanying text (discussing Interpretation One of rule 152, which precludes integration of private offering of securities and subsequent registered public offering of additional securities if issuer decides to undertake public offering after undertaking private offering); *supra* notes 63-69 and accompanying text (discussing SEC's analysis in *Verticom*).

79. *See supra* notes 70-75 and accompanying text (discussing SEC's views in *Vulture Petroleum*).

80. *See The Immune Response Corp.*, SEC No-Action Letter (Nov. 2, 1987) (LEXIS, Fedsec library, Noact file) (interpreting rule 152 to preclude integration of private offering and subsequent proposed registered public offering); *supra* note 69 (discussing SEC's analysis in *Immune Response*).

81. *See The Immune Response Corp.*, SEC No-Action Letter (Nov. 2, 1987) (LEXIS, Fedsec library, Noact file) (allowing rule 152 to preclude integration where issuer initially relied on rule 505 but rule 506 also was available).

82. *See supra* notes 70-80 and accompanying text (discussing SEC's interpretation of rule 152 in *Vulture Petroleum*); *supra* notes 46-54 and accompanying text (discussing Interpretation Two of rule 152, which precludes integration of private offering and subsequent registered public offering of additional securities upon issuer's filing of registration statement covering public offering). In a no-action letter that the SEC issued before *Vulture Petroleum*, the SEC had allowed essentially the same result that the SEC allowed in *Vulture Petroleum*. *See BBI*

A more recent no-action letter concerning rule 152 is *Vintage Group, Inc.*⁸³ In *Vintage Group*, Vintage Group, Inc. requested the views of the SEC regarding integration if, immediately upon termination of a rule 506 offering that the corporation currently was conducting, the corporation commenced a public offering under regulation E.⁸⁴ The SEC took a no-action position with respect to the request.⁸⁵ In doing so, the SEC summarily concluded that, under rule 152, a public offering that follows an offering

Assoc., SEC No-Action Letter (Dec. 29, 1986) (LEXIS, Fedsec library, Noact file) (interpreting rule 152 to preclude integration of proposed sale of assets and certain liquidation transactions with subsequent registered public offering). In *BBI Associates* the SEC considered the possible integration of a proposed sale of assets and certain liquidation transactions with a later registered public offering. *Id.* In *BBI Associates* the SEC determined that rule 152 precludes integration when an issuer files a registration statement following a private offering. *Id.* In reaching its conclusion the SEC relied on its position that, under rule 152, the filing of a registration statement subsequent to an offering otherwise exempt from registration under § 4(2) does not vitiate the exemption provided by § 4(2). *Id.* The SEC's position in *BBI Associates* assumed that the proposed transactions would be exempt from registration under § 4(2) of the Act. *Id.* As in *Verticom*, the SEC did not address BBI Associates' arguments concerning the traditional five-factor formula for determining integration in light of the SEC's conclusions concerning rule 152. *See id.* (stating that SEC found discussing traditional five-factor formula unnecessary in light of SEC's findings based on rule 152); *supra* note 68 and accompanying text (considering SEC's failure to discuss traditional five-factor formula in determining whether SEC should integrate separate offerings in *Verticom*). The SEC in *BBI Associates*, broadening the SEC's view in *Verticom*, interpreted rule 152 to allow an issuer to contemplate both a prospective private offering and a subsequent public offering without requiring integration of the two issues. *See supra* notes 63-69 and accompanying text (discussing SEC's analysis in *Verticom* no-action letter).

83. *Vintage Group, Inc.*, SEC No-Action Letter, [1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,700, at 77,978 (Apr. 11, 1988).

84. *Id.* In *Vintage Group*, Vintage Group, Inc. was a Colorado corporation that became a public company in 1983 and elected in June 1986 to have the SEC treat Vintage Group as a business development company pursuant to the Investment Company Act of 1940. *Id.* At the time of Vintage Group's inquiry, Vintage Group was engaged in an offering of its securities under rule 506 of regulation D. *Id.* In reliance on *Verticom* and *Vulture Petroleum*, Vintage Group argued that rule 152 should preclude integration of Vintage Group's regulation D offering and its subsequent regulation E offering. *Id.*; *see supra* notes 63-69 and accompanying text (discussing SEC's treatment of rule 152 in *Verticom*) and notes 70-82 and accompanying text (discussing SEC's treatment of rule 152 in *Vulture Petroleum*). In explaining that offerings made pursuant to regulation E are public offerings and, therefore, subject to exclusion from integration under rule 152, Vintage Group noted that the SEC promulgated regulation E in 1958 under § 3(c) of the Securities Act and amended regulation E in 1984 to include business development companies within the group of companies that may rely on the exemption. *Vintage Group, Inc.*, SEC No-Action Letter, [1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,700, at 77,978 (Apr. 11, 1988); *see* Investment Company Act Release No. 13,903, [1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 83,609, at 86,745 (Apr. 25, 1984) (proposing amendment to regulation E to include business development companies within group of companies that may rely on regulation E exemption); Amendments to the Offering Exemption Under Regulation E, Securities Act Release No. 33-6546, 31 SEC Docket 292. (Aug. 30, 1984) (adopting amendment to regulation E to include business development companies within group of companies that may rely on regulation E exemption).

85. *Vintage Group, Inc.*, SEC No-Action Letter, [1988 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,700, at 77,978 (Apr. 11, 1988).

exempt under rule 506 need not be integrated with the rule 506 transaction and, accordingly, would not vitiate the exemption under rule 506.⁸⁶ As in *Vulture Petroleum*, in *Vintage Group* the SEC allowed a public offering to follow a private offering without integration of the two offerings even though the issuer did not decide to make the public offering subsequent to completion of the private offering but made that decision prior to completion of the private offering.⁸⁷ Again, Interpretation Two was embraced.⁸⁸

Taken together, these path-breaking no-action letters make clear that the SEC's current interpretation of rule 152 allows an issuer to plan in advance a public offering of securities to follow soon after a private placement without fear that the SEC will integrate the two offerings.⁸⁹ Moreover, in this setting the SEC simply has discarded the five-factor formula. Through these no-action letters the SEC appears to have partially addressed the longstanding concerns associated with multiround financings, providing assurance that, at least in those capital transactions structured as section 4(2) exemptions followed by registered public offerings, the concept of integration will not be employed to upset the issuer's capital financing plans.⁹⁰ Welcome though this long-awaited development might be for those facing the nagging practical difficulties created by the doctrine of integration, the question remains whether the SEC is correct in its interpretation of rule 152.

IV. IS THE SEC'S CURRENT INTERPRETATION OF RULE 152 CORRECT?

From a linguistic viewpoint, the SEC's reading of rule 152 may be correct, a fact that largely has escaped commentators and securities profes-

86. *Id.*

87. *Id.*; see *supra* notes 70-82 and accompanying text (discussing SEC's treatment of rule 152 in *Vulture Petroleum*).

88. See *supra* notes 46-54 and accompanying text (discussing Interpretation Two of rule 152, which would allow issuer to plan to make both private offering and subsequent public offering before issuer undertakes private offering). In the SEC's most recent no-action letter concerning rule 152, the SEC re-affirmed its view that rule 152 precludes integration when a public offering follows a private offering. See *Country First Bank*, SEC No-Action Letter (Mar. 31, 1989) (LEXIS, Fedsec library, Noact file) (stating that, under rule 152, public offering following offering otherwise exempt under rule 506 of regulation D does not vitiate rule 506 exemption).

89. See *supra* notes 61-88 and accompanying text (discussing SEC's current interpretation of rule 152). In the third edition of Louis Loss' monumental treatise on securities regulation, L. LOSS & J. SELIGMAN, *SECURITIES REGULATION* (3d ed. 1989), Professors Loss and Seligman state, in discussing rule 152, that "the Commission staff has insisted that the subsequent public offering not be planned before or simultaneously with the earlier private placement." *Id.* at 1225. They also state that the staff "has permitted a subsequent public offering to be 'contemplated' as long as it is not 'planned' in a more formal sense." *Id.* at 1225 n.27. We do not think the staff is making that distinction, either expressly or in the broad reading given rule 152 in its cryptic no-action responses. Moreover, that distinction is too subtle to be made with any certainty. Either the SEC makes the distinction, with the result that issuers will shy away from reliance on the rule, or the SEC ignores the distinction, with the result that it lacks meaning and ought to be discarded.

90. See *supra* notes 61-88 and accompanying text (discussing SEC's current interpretation of rule 152).

sionals. After all, Interpretation Two is a perfectly accurate rendition to one who examines only the literal text of the rule.⁹¹ Still, at a time when the integration doctrine has come under renewed attack, this fortuitous "discovery" that rule 152 really does handily settle a portion of the integration enigma should be received critically, and for several reasons.

A. First, although a portion of the rule's language does accommodate the SEC's interpretation, the SEC is ignoring other language of the rule that might be read to require an analysis of whether an issuer who decides to make a public offering has done so before or after the issuer has made a private placement.⁹² As Interpretation One illustrates, and as most pre-*Verticom* commentators seem to think, rule 152 could be read to preclude integration of a private offering and a subsequent public offering only if an issuer makes a private offering and then *subsequently decides* to make a public offering.⁹³ This interpretation obviously does not address at all the multiround financing dilemma and is subject to other problems as well. Moreover, in our view this interpretation, although apparently the dominant pre-*Verticom* interpretation of rule 152, which is precisely the reason the rule has rested in obscurity all these decades, is also wrong. Nonetheless, here the point is simply that, while portions of the rule's language support the SEC's current interpretation, the rule can be, and long has been, read in quite another way.⁹⁴

B. Second, a further argument that the SEC currently may be misinterpreting, or at least is dramatically reinterpreting, rule 152 is the fact that in certain instances the SEC could have applied the rule but failed to do

91. See *supra* notes 46-54 and accompanying text (discussing Interpretation Two of rule 152, which would allow issuer to plan to make both private offering and subsequent public offering before issuer undertakes private offering); *supra* note 30 and accompanying text (reprinting rule 152).

92. See *supra* note 30 and accompanying text (reprinting rule 152); *supra* notes 39-45 and accompanying text (discussing Interpretation One of rule 152, which would preclude integration of private offering and subsequent public offering if issuer decides to make public offering after issuer already has made private offering).

93. See *supra* notes 39-45 and accompanying text (discussing Interpretation One of rule 152, which would preclude integration of private offering and subsequent public offering if issuer decides to make public offering after issuer already has made private offering).

Many commentators believe that the rule precludes integration only when an issuer makes a private offering and subsequently decides to make a public offering. See *supra* note 44 (noting commentators who interpret rule 152 to preclude integration if issuer decides to make public offering after completing private offering). Commentators also recognize the ambiguity that the rule creates. See H. BLOOMENTHAL, *supra* note 44, at 4-215 (discussing questions that rule 152 raises); Shapiro & Sachs, *Integration Under the Securities Act: Once an Exemption, Not Always. . .*, 31 MD. L. REV. 3, 17 (1971) (noting ambiguity of rule 152's language); Deaktor, *Integration of Securities Offerings*, 31 U. FLA. L. REV. 465, 497 n.206 (1979) (explaining different interpretations of rule 152). Many commentators focus only on the words of rule 152 rather than on what purpose in 1935 the SEC originally intended the rule to serve. Thus, the questions that many commentators have asked concerning rule 152—questions that grow out of Interpretation One—are the wrong questions.

94. See *supra* notes 92-93 and accompanying text (discussing inconsistency of SEC's current interpretation of rule 152 with full text of rule's language).

so.⁹⁵ One such recent opportunity where the SEC could have applied rule 152 but did not do so arose in *LaserFax, Inc.*⁹⁶ In *LaserFax* the issuer proposed to make a placement of subordinated convertible debentures pursuant to rules 505 and 506 within six months of the consummation of a private placement of common stock made in reliance on an unspecified rule under regulation D of the Securities Act.⁹⁷ *LaserFax* further proposed to make a registered public offering of common stock within six months of the proposed debenture offering.⁹⁸ *LaserFax* requested a no-action letter from the SEC as to whether the SEC would integrate the placement of debentures with either the earlier private placement or the later public offering or both.⁹⁹ The SEC declined to take a no-action position with respect to the integration of the debenture placement with either the earlier private placement or the proposed subsequent public offering.¹⁰⁰ The SEC, however, did not even consider the application of rule 152.¹⁰¹ Rather, the SEC applied the traditional five-factor formula used to resolve integration questions.¹⁰² Certainly, rule 152 had no bearing on whether the SEC would integrate the earlier regulation D common stock placement with the debenture offering.¹⁰³ The rule addresses only the situation of a section 4(2) offering followed by a registered *public* offering.¹⁰⁴ The debenture offering was not a public offering. Moreover, *LaserFax* did not state clearly that the earlier private placement of common stock was a rule 506 placement grounded in section 4(2) rather than a rule 504 or rule 505 placement grounded in section 3(b).¹⁰⁵ Consequently, the SEC had no alternative under existing law but to apply the vague five-factor test.

Although the SEC could not apply rule 152 to preclude integration of the offering of debentures with the earlier private placement, the SEC possibly could have relied on rule 152 to prevent integration of the debenture placement with the subsequent public offering of common stock. It is not completely clear why the SEC did not apply rule 152, especially in light of *Verticom*, which was issued just a year after *LaserFax*. One possible reason

95. See *infra* notes 96-129 and accompanying text (discussing situations in which SEC and courts could have applied rule 152 but failed to do so).

96. *LaserFax, Inc.*, SEC No-Action Letter, [1985-1986 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,136, at 76,614 (Aug. 15, 1985).

97. *Id.*

98. *Id.*

99. *Id.* at 76,615.

100. *Id.*

101. See *id.* (failing to consider rule 152).

102. *Id.*; see *supra* note 25 and accompanying text (discussing five-factor formula that SEC uses to resolve integration issues).

103. See 17 C.F.R. § 230.152 (1982); *supra* note 30 and accompanying text (reprinting rule 152). By its terms, rule 152 applies at most only to situations involving § 4(2) offerings and public offerings). See *id.*

104. See *supra* note 103 and accompanying text (discussing application of rule 152).

105. See *LaserFax, Inc.*, SEC No-Action Letter, [1985-86 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 78,136, at 76,615 (Aug. 15, 1985) (failing to state whether earlier private placement was rule 506 placement rather than rule 504 or 505 placement).

is that the issuer did not state clearly whether the issuer would make the debenture placement exclusively in reliance on rule 506 rather than rule 505 as well.¹⁰⁶ Because rule 506 is grounded in section 4(2) but rule 505 is grounded in section 3(b), failure to clarify that point would warrant SEC refusal to conclude that rule 152 applied. That appears clearly to be the case in one letter, issued shortly after *LaserFax*, in which the SEC did not concur that private placements need not be integrated with subsequent public offerings.¹⁰⁷ Another possible reason might be that the issuer's counsel did not base the no-action request on rule 152, and the SEC was not going to make the case for the issuer. Finally, it may not yet have dawned on the SEC to give rule 152 the reading given shortly thereafter in *Verticom*. Whatever might have been the reason or reasons for not applying rule 152 to the situation in *LaserFax*,¹⁰⁸ while later applying rule 152 to somewhat similar situations, the SEC, at least in retrospect, may have acted inconsistently with respect to the rule.¹⁰⁹

An earlier instance in which the SEC could have applied its recent reading of rule 152 but failed to do so arose in *Cameron Industries, Inc.*¹¹⁰ *Cameron* involved a proceeding to determine whether the SEC should issue a stop order suspending the effectiveness of a registration statement that the issuer had filed with respect to a proposed public offering of common stock.¹¹¹ Within the six-month period immediately prior to the month in

106. See *id.* (failing to state whether *LaserFax* was to make debenture placement exclusively in reliance on rule 506 rather than rule 505 as well).

107. See Financial Independence Inv. Corp., SEC No-Action Letter (LEXIS, Fedsec library, Noact file) (Oct. 30, 1985) (failing to clarify whether placement was made in reliance on rule 506 rather than rule 504 or rule 505 as well).

108. One commentator asserts that the SEC used *LaserFax* to confirm the SEC's position that rule 152 applies only where the decision to undertake a public offering is made subsequent to the private placement. See Stevenson, *supra* note 44, at 55. After *Verticom*, however, it is clear that the SEC does not hold—if it ever did—that position.

109. See *supra* notes 95-108 and accompanying text (discussing inconsistency of SEC's application of rule 152). Although the SEC may have acted inconsistently with respect to rule 152, Mary E.T. Beach, Associate Director of the Division of SEC's Division of Corporation Finance, has defended the position taken by the SEC in *LaserFax*. See *Real Estate Syndicators Ask Staff To Consider Reg D Changes*, [Jan.-June] 18 Sec. Reg. & L. Rep. (BNA), No. 17, at 590-91 (April 25, 1986) (discussing SEC's rationale in *LaserFax*). In defending the SEC's position in *LaserFax*, Beach explained that the staff always has focused on the purpose and the type of securities to be issued in multiple offerings to reach a conclusion on whether the SEC should integrate the offerings. *Id.* at 591. Beach further explained that in the *LaserFax* no-action request *LaserFax* did not identify the portion of regulation D on which the issuer proposed to rely in making the private offering. *Id.* In distinguishing the no-action position that the SEC took in *Verticom* from the position that the SEC took in *LaserFax*, Beach stated that the issuer in *Verticom* specified which part of regulation D it proposed to rely upon in making the private offering. *Id.* In addition, Beach explained that, in contrast to the requestor in *LaserFax*, counsel for *Verticom* argued that rule 152 should apply to the proposed offerings. *Id.* In response to *Verticom*'s request in *Verticom*, the SEC stated that the SEC would not focus on the "subsequently thereto" language in rule 152 to determine the issuer's state of mind at the time the issuer made the private offering. *Id.*

110. 39 S.E.C. 540 (1959).

111. *Cameron Indus., Inc.*, 39 S.E.C. 540, 540-41 (1959).

which the issuer filed the registration statement, the issuer had sold 291,500 shares of common stock.¹¹² Of the 291,500 shares, the issuer sold 23,500 shares directly to three persons for approximately \$10,000.¹¹³ The issuer distributed the remaining 268,000 shares to various persons through the efforts of a promoter.¹¹⁴ In the issuer's public offering prospectus the issuer stated that the prior sales of the 291,500 shares of common stock had been exempt from registration under what is now section 4(2) as a private placement of securities.¹¹⁵

In a proceeding before the full Commission the Division of Corporate Finance (the Division) argued that all of the sales of common stock pursuant to the alleged private placements were in fact a part of the issue of common stock that the issuer publicly offered pursuant to the issuer's registration statement.¹¹⁶ Thus, the Division argued that the SEC should integrate the prior private offerings and the subsequent public offering.¹¹⁷ In contrast, the issuer argued that the sales of the 23,500 shares constituted an exempt pre-underwriting offering created to raise funds to pay general corporate expenses, including the costs incurred in connection with the contemplated public offering.¹¹⁸ The issuer further argued that the sale of the remaining 268,000 shares was also a separate financing transaction exempt under current section 4(2).¹¹⁹ In spite of the issuer's arguments, the SEC held that the issuer sold the 23,500 shares in connection with and as part of a plan for the public distribution of the issuer's securities.¹²⁰ With respect to the remaining 268,000 shares, the SEC further found the issuance and distribution of the 268,000 shares to be an "integral part of the public offering of registrant's shares proposed pursuant to the registration statement filed shortly thereafter."¹²¹ As a result of these findings, the SEC integrated the two prior private placements into the subsequent public offering and held that the exemption claimed in the issuer's prospectus for the prior transactions was not available.¹²² The SEC held, therefore, that the prior sales violated the registration provisions of the Securities Act.¹²³ Accordingly, the SEC found the issuer's registration statement to be materially misleading because the statement falsely represented that the sales of the 291,500 shares of the issuer's stock were exempt from registration and failed to disclose the issuer's contingent liabilities resulting therefrom.¹²⁴

112. *Id.* at 545-46.

113. *Id.* at 546.

114. *Id.*

115. *Id.* at 545-46.

116. *Id.* at 546.

117. *Id.*

118. *Id.*

119. *Id.* at 545-46.

120. *Id.* at 546.

121. *Id.*

122. *Id.*

123. *Id.*

124. *Id.*

Thus, in *Cameron* the full Securities and Exchange Commission integrated an issuer's private placements of securities with a subsequent registered public offering of additional securities without regard to, or even mentioning, the effect of rule 152 on the situation.¹²⁵ The SEC staff, however, now has matter-of-factly applied rule 152 to preclude integration of a private offering and a subsequent public offering on the rationale that the plain language of the rule prevents integration of the transactions where a registration statement for the public offering has been filed.¹²⁶ Applying the staff's reasoning that rule 152 bars integration under those circumstances to the facts of *Cameron*, one is hard pressed to reconcile the two outcomes.¹²⁷ Perhaps, as with *LaserFax*, the rule was not presented in defense and was otherwise unknown to the SEC, or was thought not to apply to such a situation.¹²⁸ While traditional integration factors, though not necessarily sound policy, indicate that the SEC correctly integrated the financing transactions in *Cameron*, the SEC staff must reconcile its current interpretation of rule 152 with the SEC's holding in *Cameron*.¹²⁹ One of the two is wrong.

125. See *id.* at 545-46 (failing to discuss rule 152); *supra* notes 110-124 and accompanying text (discussing SEC's holding in *Cameron*).

126. See *supra* notes 61-90 and accompanying text (discussing no-action letters in which SEC took position that rule 152 precludes integration of private offering and subsequent public offering if issuer files registration statement for public offering after having made private offering).

127. See *supra* notes 110-124 and accompanying text (discussing facts in *Cameron*); *supra* notes 61-90 and accompanying text (discussing SEC staff's position in no-action letters that rule 152 precludes integration of private offering and subsequent public offering when issuer files registration statement for subsequent public offering).

128. See *supra* notes 95-109 and accompanying text (discussing SEC's failure to apply rule 152 in *LaserFax*).

129. See *supra* note 25 and accompanying text (discussing traditional five-factor test that SEC uses to determine whether SEC should integrate separate offerings of securities); *supra* notes 61-90 and accompanying text (discussing SEC staff's position that rule 152 precludes integration of private offering and subsequent public offering when issuer files registration statement for subsequent public offering). *But see* Shapiro & Sachs, *supra* note 93, at 17 (arguing that *Cameron*'s factual scenario falls outside protection that rule 152 affords). Shapiro & Sachs assert that *Cameron* falls outside the scope of rule 152's protection. See *id.* at 17 (arguing that rule 152 does not apply to facts of *Cameron*). These commentators note that the issuer in *Cameron* reached a decision with an underwriter relative to the exact terms of the proposed public offering prior to the time that the illegal sales were made. *Id.* The commentators, writing in 1971, wrongly assume that the SEC only allows rule 152 to preclude integration of a private offering and a subsequent public offering if the issuer decides to make the public offering after the issuer already has made the private offering of securities--*i.e.*, that Interpretation One is correct. Cf. *supra* notes 39-45 and accompanying text (discussing Interpretation One of rule 152, which would preclude integration of private offering and subsequent public offering if issuer decides to make public offering after issuer already has undertaken private offering). The SEC, however, has stated that rule 152 precludes integration of a private offering and a subsequent public offering merely when an issuer files the registration statement for the subsequent public offering. See *supra* notes 61-90 and accompanying text (discussing no-action letters in which SEC staff took position that rule 152 precludes integration of private offering and subsequent public offering when issuer files registration statement for

The *LaserFax* and *Cameron* situations emphasize the point that either the SEC has recently “rediscovered” rule 152 or that the SEC is using the rule for the wrong situation by deploying the rule in the multiround financing context.¹³⁰ The SEC, however, is not completely to blame for the present confusion surrounding the proper interpretation of rule 152.¹³¹ Understandable pressures from the securities bar for a wholesale revisiting of the nettlesome way in which the integration doctrine complicates capital formation, pressures that securities regulators have largely not heeded, aid in explaining the rule’s sudden arrival in the multiround financing setting.¹³² For some time members of the securities bar have been especially hopeful that the SEC will refrain from integrating private offerings made in anticipation of initial public offerings, largely on policy grounds.¹³³ Lacking any relief from the regulatory authorities, securities lawyers sought refuge from continuing uncertainty in an existing rule, albeit an obscure rule, that the lawyers could use to buttress their policy-based arguments.¹³⁴ A closer review of the *Verticom* letter bears out the creative and novel way in which rule 152 was interpreted to serve that end.¹³⁵

Verticom was apparently the first instance in which an issuer’s lawyer cited rule 152 to persuade the SEC staff to take a no-action position with regard to whether a private placement and a subsequent public offering should be integrated.¹³⁶ To convince the SEC to apply rule 152, counsel for *Verticom* explained that “one apparent effect” of the rule is to allow an issuer who had begun to undertake a private offering of securities to register the securities of the private offering for a public offering without incurring liability because the issuer first began to undertake the offering privately.¹³⁷

subsequent public offering). Because we believe both Shapiro and Sachs’ Interpretation One and the SEC’s Interpretation Two are wrong, we believe that Shapiro and Sachs are right about *Cameron* falling outside of rule 152, but that they are right for the wrong reason.

130. See *supra* notes 96-109 and accompanying text (discussing SEC staff’s analysis in *LaserFax*); *supra* notes 110-129 and accompanying text (discussing SEC’s analysis in *Cameron*).

131. See *supra* notes 31-60 and accompanying text (discussing reasons for confusion surrounding rule 152’s application).

132. See *infra* notes 133-141 and accompanying text (discussing pressures from securities bar that help explain SEC’s current interpretation of rule 152).

133. See Stevenson, *supra* note 44, at 55.

134. See *infra* notes 136-141 and accompanying text (discussing lawyers’ use of rule 152 to persuade SEC that SEC should not integrate private offering that issuer makes to raise seed capital with later initial public offering).

135. See *infra* notes 136-141 and accompanying text (discussing means by which counsel in *Verticom* persuaded SEC staff to take no-action position).

136. See *Verticom, Inc.*, SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file) (using rule 152 to support argument that SEC staff should take no-action position); *supra* notes 63-69 and accompanying text (discussing *Verticom* no-action letter).

137. *Verticom, Inc.*, SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file). We think there is little doubt the “one apparent effect” of rule 152 that counsel for *Verticom* in *Verticom* mentions is the only effect of the rule. Essentially, this interpretation of rule 152 would allow an issuer who makes a failed private offering of securities to complete the private offering by registering the unsold securities for a public offering and incur no liability for first having undertaken the offering privately. See *supra* notes 55-60 and accompanying text (discussing Interpretation Three).

In other words, Verticom's counsel seemed to acknowledge Interpretation Three of rule 152 as one "apparent effect," but did not concede that such an interpretation was, as we believe clearly is the case, the sum and substance of the rule.¹³⁸ Instead, counsel for Verticom went on to argue that "a reasonable construction of the rule" suggests that the filing of a registration statement covering a public offering should not vitiate the section 4(2) exemption for an otherwise qualifying private placement that the issuer concluded prior to such filing.¹³⁹ In spite of wholly misinterpreting rule 152 to cover something the rule was not designed to address—the mezzanine financing situation in *Verticom*—counsel for Verticom succeeded in persuading the SEC to apply the rule.¹⁴⁰ Moreover, since *Verticom* the SEC has continued to apply rule 152 to multiround financing situations and shows no signs of reversing that trend.¹⁴¹ By thus rising to the issuer's tantalizing bait, the SEC has done what it may have wanted to do for some time but lacked the ingenuity to accomplish—to address, at least in part, the abiding integration concerns of the practicing securities bar. The SEC now has done so, but only by abruptly reversing the direction of *LaserFax* and *Cameron* and, more important, by distorting the original purpose of rule 152.

C. In addition to challenging the linguistic and precedential underpinnings of the SEC's new interpretation of rule 152, a third argument that the SEC misunderstands the intended scope of the rule comes from the language of the release adopting the rule.¹⁴² The release takes care to explain that the rule is intended to clarify that, if an issuer makes a section 4(2) placement "prior to the filing of the registration statement. . . under circumstances which did not necessitate registration or contemplate registration. . . ," such initial private offerings do not by the "fact of registration become the type of offerings which are prohibited by the Securities Act."¹⁴³ Furthermore, the release states that the rule allows issuers "who have

138. See *supra* notes 55-60 and accompanying text (discussing Interpretation Three of rule 152).

139. Verticom, Inc., SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file). The rule 152 argument that counsel for Verticom pressed in *Verticom* is understandable in light of the nonexistent history of the rule's application. See *supra* notes 32-34 and accompanying text (discussing sparse history of rule 152). This lack of history regarding the rule, however, also indicates that the multiround financing situation, such as arose in *Verticom*, is the incorrect situation for application of the rule. Had the SEC originally intended rule 152 to apply to the multiround financing situation, no doubt the SEC would have made this clear during the first fifty years of the rule's existence.

140. Verticom, Inc., SEC No-Action Letter (Feb. 12, 1986) (LEXIS, Fedsec library, Noact file); see *supra* notes 63-69 and accompanying text (discussing SEC's interpretation of rule 152 in *Verticom*).

141. See *supra* notes 61-90 and accompanying text (discussing no-action letters in which SEC has interpreted rule 152 to preclude integration of private offering and subsequent public offering when issuer files registration statement for subsequent public offering).

142. See Securities Act Release No. 33-305 (Mar. 2, 1935) (available from SEC; reprinted in Appendix) (adopting rule 152 to Securities Act).

143. *Id.*

contemplated or begun to undertake a private offering to register *the* securities without incurring any risk of liability as a consequence of having first contemplated or begun to undertake a private offering.”¹⁴⁴ This language pretty clearly indicates that the rule refers to a registration of *the* securities that an issuer first offers privately instead of a registration covering *other* securities in a separate public offering.¹⁴⁵ Moreover, the release adopting rule 152 initially explains that the rule’s purpose is to define “transactions not involving any public offering” made prior to an issuer’s filing of a registration statement.¹⁴⁶ Consequently, the release does not directly address the issue of integrating separate financings so much as state that the character of a private placement as “private” is not altered by a later registered public re-offering of that portion of the securities offered, but not sold, privately.¹⁴⁷ In other words, under this interpretation of rule 152, the SEC will not recharacterize a private offering under section 4(2) as “involving” a public offering if an issuer subsequently files a registration statement covering the securities of the private offering in a subsequent public offering in order, essentially, to salvage a single financing transaction that began as a failed private placement.¹⁴⁸ Thus, the original release addresses what in the financial doldrums of 1935 might have been viewed as a pressing need—the dilemma of the issuer with a “sticky” private placement. So read, the release supports a more modest interpretation of rule 152—Interpretation Three—rather than the SEC’s newly found, broader interpretation.¹⁴⁹

144. *Id.* (emphasis added).

145. *See id.* (discussing purposes of rule 152); *supra* notes 55-60 and accompanying text (discussing Interpretation Three of rule 152, which allows issuer of private offering of securities to file registration statement covering private offering securities for public offering without affecting original exemption under § 4(2)).

146. Securities Act Release No. 33-305 (Mar. 2, 1935) (available from SEC; reprinted in Appendix).

147. *See id.* (stating purposes of rule 152).

148. *See supra* notes 142-147 and accompanying text (discussing language of release adopting rule 152). One commentator also indicates that the SEC originally intended rule 152 to apply to an issuer who makes a private offering of securities and then wishes to transform the private offering into a public offering. *See* L. LOSS, 1 SECURITIES REGULATION 688-89 (2d ed. 1961) (discussing applicability of rule 152 to issuer who makes private offering and subsequently decides to transform private offering into public offering). Loss states that rule 152 is a special rule that “affords a *locus poenitentiae* to an issuer which *starts* with a private offering and *subsequently* decides to make a public offering or file a registration statement.” *Id.* at 689 (first and third emphases in original; second emphasis added). Although not entirely clear—especially in light of the more ambiguous discussion of the function of rule 152 found in the third edition of the treatise, *see* L. LOSS & J. SELIGMAN, *supra* note 89, at 1225-26—Loss’ interpretation of rule 152 appears to comport with our Interpretation Three and, therefore, suggests that the rule should preclude integration for an issuer who makes a private offering and who subsequently decides to turn the “private” offering into a public offering and thus subsequently files a registration statement to finish the private offering. The subsequent decision to register the securities not sold in the private placement must be distinguished from a subsequent decision to make a public offering of additional securities after a successful § 4(2) placement. The latter reading is Interpretation One, which we believe is wrong.

149. *See* Securities Act Release No. 33-305 (Mar. 2, 1935) (available from SEC; reprinted

D. Support for a more restrictive reading of rule 152 is also found in a review of the SEC's thinking on the nascent integration issue at the time the rule was promulgated. The origins of the integration concept often are traced to an early Federal Trade Commission letter in which an issuer sought the views of the FTC.¹⁵⁰ Pending the effectiveness of a registration statement an issuer proposed to sell securities to residents of the state in which the issuer was incorporated and was doing business in reliance on what is now section 3(a)(11).¹⁵¹ The issuer contemplated that, after the registration statement became effective, it would sell to nonresidents in a public offering.¹⁵² The FTC stated that section 3(a)(11) required an issuer to sell the "entire issue" to residents of a single state and that the post-effective sales to nonresidents in the public offering would violate that condition.¹⁵³

In one sense it might be said that the FTC "integrated" two separate offerings. Yet, beyond the fact that the FTC did not use that word, the FTC did not so much combine two functionally separate entrees into the capital markets as rule that one entree may not be conducted along separate legal paths, one an exemption and the other a registration. Likewise, a given offering may not be grounded in part on one exemption and in part on others; in all respects an offering must meet the requirements of one or more exemptions. Without wishing to place too fine a point on the matter, unless, as appears not to be the case, the requesting issuer wished to view the in-state and out-of-state sales as more than different channels for funding a single plan of financing, little is gained by introducing the concept of integration to establish the noncontroversial principle that a concededly singular financing transaction may not be partially grounded on one exemption and partially grounded on another exemption (or on registration).¹⁵⁴ Clearly, that conclusion required the FTC to assume that the public offering was "part of" the same issue as the intrastate transaction, but that assumption is perfectly sensible on the facts and appears to have been conceded in the issuer's letter of inquiry.

Only in 1938 did the SEC squarely face the issue of what today we would call offering integration. On March 19, 1937, Unity Gold Corporation

in Appendix) (explaining purpose of rule 152); *supra* notes 142-148 and accompanying text (discussing release's support of Interpretation Three); *supra* notes 55-60 and accompanying text (discussing Interpretation Three of rule 152).

150. See Securities Act Release No. 33-97, 1 Fed. Sec. L. Rep. (CCH) ¶ 1027, at 2056 (Dec. 28, 1933).

151. *Id.*

152. *Id.*

153. *Id.*

154. See *id.*; *In re Brooklyn Manhattan Transit Corp.*, 1 S.E.C. 147, 161 (1935) (stating that to allow issuer to escape registration when issuer relies on § 3(a)(11) exemption in issuing securities to person in one state followed by interstate distribution by that person would nullify express purpose of Congress); *Texas Glass Mfg. Corp.*, 38 S.E.C. 630, 634 (1958) (stating that § 3(a)(11) exemption is unavailable to issuer who is unsuccessful in selling entire issue to residents of single state and who offers rest of issue, even after registration, to residents of other states).

entered into two contracts for the disposition of 600,000 shares of common stock.¹⁵⁵ One contract with a private investor provided, among other things, that the investor purchase 75,000 shares of common stock for approximately \$47,000 cash.¹⁵⁶ The statutory basis for this supposedly exempt transaction was section 3(b) of the Securities Act, which exempts from registration those classes of securities that the SEC exempts by rule.¹⁵⁷ Section 3(b) then also provided that “no issue of securities shall be exempted under this subsection where the aggregate amount at which such issue is offered to the public exceeds \$100,000.”¹⁵⁸ On May 25, 1937, Unity Gold filed a registration statement for 619,333 shares of common stock.¹⁵⁹ In a stop-order proceeding, the SEC held the sale to the private investor to be part of the same “issue” as the shares covered by the registration statement subsequently filed and, therefore, to exceed the \$100,000 ceiling of section 3(b) and violate the registration requirements of the Securities Act.¹⁶⁰

In rejecting the issuer’s contention that the two transactions were separate, the SEC stated that

The proviso [of section 3(b)] cannot be construed to permit the exemption of small portions of large financing operations. This would defeat its very purpose. Thus, securities of the same class, offered on the same general terms to the public in an uninterrupted program of distribution, cannot be segregated into separate “issues” merely by claiming an exemption for a limited portion of such shares under Rule 202, or under any other rules of the Commission adopted in accordance with Section 3(b) of the Act, and registering the remainder.¹⁶¹

The SEC then went on to articulate six factors that would guide the determination of whether seemingly discrete capital financing transactions were, in fact, one “issue.”¹⁶² Those factors guided SEC thinking on the integration question for more than two decades¹⁶³ when they were somewhat reformulated in Release Nos. 33-4434 and 33-4552, adopted in 1961 and 1962, respectively.¹⁶⁴

Given the SEC’s obvious concern over the integration issue in 1938, a concern rather pointedly directed at what might be called Unity Gold’s

155. Unity Gold Corp., 3 S.E.C. 618, 624 (1938).

156. *Id.* at 624.

157. *Id.* at 623.

158. *Id.*

159. *Id.* at 620.

160. *Id.* at 625-26.

161. *Id.* at 625.

162. *Id.*

163. *See, e.g.*, Opinion of the Counsel, Securities Act Release No. 33-2029, 1 Fed. Sec. L. Rep. (CCH) ¶ 2141, at 2584 (Aug. 8, 1939) (noting *Unity Gold*’s treatment of whether seemingly separate transactions are one “issue”).

164. *See, e.g.*, Herbert R. May and Russell H. Phinney, 27 S.E.C. 814, 818-20 (1948) (applying *Unity Gold* factors to determine whether separate transactions were one “issue”).

conventional "staged financing," a serious doubt exists as to whether it is proper to interpret a 1935 SEC rule—rule 152—as authorizing, in the context of a section 4(2) private placement followed by a public offering, precisely what in *Unity Gold* the SEC said could not be done in the context of a section 3(b) offering followed by a public offering. The *Unity Gold* language quoted above evinces a rather broad policy concern about issuers dividing financings into smaller constituent parts to subvert the policy of investor protection as achieved by registration, a concern that did not, in the eyes of the SEC as borne out in 1958 in the *Cameron* matter,¹⁶⁵ disappear when a public offering is preceded by a section 4(2) rather than, as in *Unity Gold*, a section 3(b) transaction.¹⁶⁶

Thus, at the time the SEC adopted rule 152 the SEC did not intend to address in any definitive way the integration issue that was still crystallizing in the collective experiences of the securities bar and the regulatory officials under a piece of monumental legislation that was only two years old. Indeed, as with the oft- and mis-cited 1933 FTC letter,¹⁶⁷ rule 152 is not even directed at the subject of integration as that term is generally used.¹⁶⁸ Rule 152 is much more modest in its aim. Properly understood, rule 152 deals only with the position of the issuer who admittedly is seeking to fund *one* business transaction via *two* distinct legal avenues, first a private offering and then, solely because of the issuer's inability to sell all of the offered securities, a registered public offering of the unsold securities.¹⁶⁹ The rule, at bottom a definitional rule, merely provides that the earlier private transaction does not "involve" a public offering simply because the latter is subsequently deployed to sell securities that could not be sold privately.¹⁷⁰ In other words, the character of the initial attempt to dispose of securities is not transformed by later registration. The policy rationale is obvious and sensible—without the rule, issuers could not go forward and register unsold securities, but would be left with the consequences of having failed to sell in the fashion first chosen. In 1935 that would have created a tremendous disincentive for using section 4(2). Unless an issuer was confident of putting away the whole offering, the issuer would either not seek capital at all via

165. See *supra* notes 110-129 and accompanying text (discussing SEC's analysis in *Cameron*).

166. See *Unity Gold Corp.*, 3 S.E.C. 618, 625-26 (1938) (disallowing § 3(b) exemption); *Cameron Indus., Inc.*, 39 S.E.C. 540, 546 (1958) (disallowing § 4(2) exemption); *supra* notes 155-164 and accompanying text (discussing SEC's analysis in *Unity Gold*); *supra* notes 110-129 and accompanying text (discussing SEC's analysis in *Cameron*); see also *Crowell-Collier Publishing Co.*, Securities Act Release No. 33-3825 (Aug. 12, 1957) (SEC stated that issuer may not establish that particular part of issue is private transaction if whole issue involves public offering of securities; and SEC did not recognize rule 152's existence).

167. See *supra* notes 150-154 and accompanying text (discussing FTC's analysis in 1933 FTC letter).

168. See *supra* notes 5-29 and accompanying text (discussing doctrine of integration).

169. See *supra* notes 55-60 and accompanying text (discussing Interpretation Three of rule 152).

170. See *supra* note 30 and accompanying text (reprinting rule 152).

the private placement or the issuer would go ahead and register the securities at the outset. Rule 152 created a viable middle ground—try a private placement and then, if not completely successful, finish off with a registered public offering.

Perhaps the relationship of rule 152 to the larger integration doctrine can be made clearer by another illustration. Suppose an issuer needs \$10,000,000. Obviously, in order to avoid registration, the issuer might seek to divide the funding effort into two or more parts, each of which would be made to appear freestanding and distinct from the other and so ostensibly be exempt. The danger of doing so, however, is that the doctrine of integration will “look through” these efforts and join the two or more components in a way that does not meet the requirements of any one exemption. Therefore, suppose that the issuer, believing the risk of integration in this case to be high, sets off to raise the \$10,000,000 in a section 3(a)(11) intrastate offering. While able to raise a large portion of the funds—say \$7,000,000—the issuer becomes aware that it cannot sell the remaining \$3,000,000 worth of securities within the single state. Suppose further that the issuer then learns of a prospective purchaser who lives in another state and that the prospective purchaser, who is accredited and sophisticated, might be interested in purchasing the remaining \$3,000,000 worth of securities. The problem for the issuer is that it cannot sell to the out-of-state sophisticated investor in an intrastate offering, and the presence of unsophisticated in-state investors might preclude reliance on any other exemptions. Having elected to proceed as the issuer did, however, the issuer’s later problem is the longstanding problem of not being able to split exemptions to support a singular placement of securities. The issuer cannot rely on the intrastate exemption for all purchasers except the out-of-state investor and then rely on, for example, section 4(2) for the remaining purchaser.

What does such an issuer do? Can the issuer now turn to rule 152 and seek to sell the remaining \$3,000,000 worth of securities in a registered public offering? Obviously, because rule 152 specifically refers only to section 4(2) private placements, not to section 3(a)(11) offerings, this situation is not covered by the rule.¹⁷¹ We may not be particularly interested in affording the issuer relief from this dilemma in light of the fact that the issuer initially chose not to register all \$10,000,000 worth of securities. Again, however, we speak too loosely if we characterize this as a matter of choosing whether or not to integrate an intrastate transaction and a public offering. Rather, it involves the narrower question of whether the rationale of rule 152 should be applied more broadly than to section 4(2) transactions—here, to a section 3(a)(11) transaction. Granted, the fear of integration may have motivated the issuer to be overly ambitious in seeking \$10,000,000 from the investors of a single state rather than dividing the funding effort into smaller parts that the SEC might legally recombine, but that excess of ambition does not directly present the same “integration”

171. See *supra* note 30 and accompanying text (reprinting rule 152).

issue if the issuer fails. Likewise, current rule 152 does not address in a wholesale fashion all facets of the integration problem as may arise whenever a section 4(2) placement precedes a registered offering so much as address the problem of an unsuccessful "sticky" offering where, apparently, the SEC is fairly sympathetic—for reasons not stated but readily understood—to an issuer's desire to extricate itself and salvage the transaction by a subsequent registered offering.¹⁷²

Of course, this policy of relief from failure to complete a deal privately might be extended to include other failed exempt transactions followed by registration of the unsold securities, and without necessarily implicating the larger doctrine of integration. For example, the failed intrastate offering under section 3(a)(11) described above or a failed section 3(b) transaction each might be salvaged by a subsequent public offering. Linguistically, however, this policy objective is harder to achieve. Unlike the verb "involve" in section 4(2), the key term in both section 3(b) and section 3(a)(11) is "issue," and no part of an "issue" may fail to comply with the stringent requirements of those sections.¹⁷³ Moreover, and much more significantly, the current policy underpinnings of the section 4(2) exemption differ from those of sections 3(b), 3(a)(11), and other exemptions. For example, section 4(2) is premised on the belief that certain "financially sophisticated" investors do not need the benefit of SEC pre-offering review provided by

172. If we are correct that rule 152 originally was intended to address only the situation of a failed private placement, not the conventional staged financing situation and the integration problem that grows out of that, could an imaginative issuer still utilize the rule to its advantage? Suppose an issuer needing \$10,000,000 originally planned to raise \$2,000,000 in a § 4(2) private placement and the remainder in a registered public offering shortly thereafter. If we are correct and the SEC is wrong, rule 152 offers no comfort to this issuer, and the issuer must satisfy the traditional vague five-factor formula to avoid integration. Suppose further, however, that to avoid that outcome, and believing our interpretation of rule 152 is correct, the issuer set out to raise all \$10,000,000 in the private placement and then when, as is likely and as the issuer may full expect, failed to do so, proceeded to register the remaining unsold securities, citing rule 152 as we have interpreted it in support of the proposition that "failed" private placements are the *raison d'être* of rule 152. Here, language in the adopting release seems to require that the issuer not "contemplate registration" at the time of the private placement. See *supra* note 143 and accompanying text and note 148 (pointing out that decision to register securities not sold in private offering must be "subsequent" to that offering). Thus, it is doubtful whether a cunning issuer could use our narrower interpretation of rule 152 to, nonetheless, obtain relief from the continuing spectre of integration and its haunting impact on conventional multiround financing.

173. See *supra* notes 16-18 and accompanying text (discussing that § 3(a)(11) exempts from § 5 of Securities Act any security that is "part of an issue" offered and sold only to persons residing within single state); *supra* note 22 and accompanying text (discussing that § 3(b) states that no "issue" of securities sold under § 3(b) may exceed \$5,000,000). In 1959 the then Director of the then Division of Trading and Exchanges stated that "if an issuer starts an intrastate offering and finds that the entire issue cannot be sold in the state, it cannot file a registration statement or comply with regulation A in order to sell the balance of the offering interstate since in such event the *entire issue* would not be limited to the state and the exemption would be lost as to the initial offering." Loomis, *Enforcement Problems Under the Federal Securities Laws*, 14 BUS. LAW. 665, 670-71 (1959) (emphasis added).

registration as long as they receive registration statement-like disclosure.¹⁷⁴ Section 3(a)(11) is premised on the ability of states to regulate wholly in-state capital formation.¹⁷⁵ SEC rules adopted pursuant to section 3(b) have varied policy rationales. Rule 504 offerings are sufficiently small not to warrant intrusive federal regulation, and certain of them will receive scrutiny by state regulatory officials; rule 505 requires a private placement memorandum providing registration statement-like disclosure—but not pre-offering SEC review—for nonaccredited investors; regulation A provides investors with an offering circular, the disclosures in which are modeled after but less demanding than those in a registration statement. Consequently, to extend the original policy of rule 152 to other failed exempt offerings might best be done by more formal rulemaking procedures in light of the linguistic obstacles and in light of the fact that the different policy bases of the various exemptions might conflict with the policy of salvaging “sticky” placements and therefore dictate not providing relief from failed offerings for those issuers who rely on exemptions other than section 4(2). On the other hand, the policy rationales of other exemptions—particularly the contemporary significance of the section 3(b) exemptions on capital formation by small businesses—might make certain of them more likely candidates for regulatory relief here as elsewhere. So viewed, the way in which both the narrow concern of rule 152 and the broader issue of integration itself are inextricably connected to the ever evolving policies of registration and exemptions becomes plainly visible.¹⁷⁶ The more immediate point, however, is simply that neither with respect to the subject matter of existing rule 152—failed section 4(2) private placements—nor with respect to an extension of the limited policy rationale of rule 152 to other failed exempt transactions is offering integration, as that term is commonly understood in the multiround financing context, really the subject.

V. THE CONSEQUENCES OF MISINTERPRETING RULE 152.

Integration is widely regarded as a necessary but troublesome concept. Integration is necessary because it prevents subversion of the registration requirements of the Securities Act.¹⁷⁷ Integration is troublesome because the concept has not been firmly linked to a modern conception of the purposes and policies of registration and exemptions therefrom. The prevailing five-factor formula is fuzzy, subjective, and imprecise as to how many and

174. See H.R. Rep. No. 85, 73d Cong., 1st Sess. 7 (1933) (discussing rationale for § 4(2)); *supra* notes 19-21 and accompanying text (discussing § 4(2) premise that certain “financially sophisticated” investors do not need SEC pre-offering review that registration provides).

175. See S. Rep. No. 47, 73d Cong., 1st Sess. 4 (1933) (discussing rationale for § 3(a)(11)); H.R. Rep. No. 85, 73d Cong., 1st Sess. 5 (1933) (same).

176. See *supra* note 29 and accompanying text (discussing relation of rule 152 and integration doctrine to policies of registration and exemptions).

177. See *ABA Task Force Report on Integration*, *supra* note 26, at 595 (discussing purposes of integration concept); *supra* notes 5-29 and accompanying text (discussing doctrine of integration).

which of the five criteria the issuer must satisfy to attain the desired status of nonintegration. The result is a doctrine well-suited in its fluidity to the remedial task of revisiting and upsetting capital-raising transactions that, in retrospect, were unsatisfactory to investors and, fortuitously, also should have been registered. Consequently, the concept affords a potent remedy for "bad" deals, even if unblemished by fraud, and the concept perhaps is to be valued for that alone.¹⁷⁸

Whether the concept in its current state has other benefits as well—encouraging registration instead of either foregoing a financing transaction or risking later application of the doctrine—that, on balance, outweigh the alleged "costs" of deterring desired capital formation is difficult to answer. What is not difficult to see, however, is that, whether a virtue or a vice, issuers and their legal counsel operate in a world of uncertainty and doubt because of the current formulation of the doctrine. Over the years, the SEC's actions on the integration front seem to reflect a curious ambivalence toward the notion. The SEC has supplied specific safe harbors from the doctrine's application—thereby affording a measure of certainty for issuers and thus advancing the goal of capital formation—while at the same time retaining the concept in all its useful vagueness in all other settings—thereby preserving the concept's vitality for both goading registration and remedying unsatisfactory investments. The SEC's action on rule 152 represents yet another step in the direction of the certainty and capital formation pole. Those in sympathy with that policy objective are, therefore, pleased with the recent initiatives. Yet, we suggest that, whatever one's position on the larger policy issues, the SEC has not offered genuine certainty in even the relatively narrow context in which it mistakenly believes rule 152 applies. Moreover, the SEC's manner of proceeding on this matter has in fact detracted from a surer resolution of the larger issues raised by integration. We believe this for several reasons.

First, as a historical matter, the SEC is misreading rule 152. No doubt, literally the words of the text do "contain" the reading given by the SEC. But those who interpret administrative rules—or statutes or constitutions—must seek the intentions of the writer. In doing so—that is, in being a "legal intentionalist"¹⁷⁹—of course one looks at the words themselves, but attention also must be paid to the background of and perceived problem addressed by the rule¹⁸⁰ and to the larger milieu, regulatory and otherwise,

178. See J. SELIGMAN, *THE SEC AND THE FUTURE OF FINANCE* 246-48 (1985) (arguing that SEC should regularly analyze likely extent to which mandatory disclosure law change will increase or decrease securities fraud or unfairness and increase or decrease incidence of fraud).

179. See R. POSNER, *LAW AND LITERATURE* 218 (1988) (discussing "legal intentionalist"). Judge Posner states that a legal intentionalist in reading a statute or the Constitution tries to "figure out from the words, the structure, the background, and any other available information how the legislators whose votes were necessary for enactment would probably have answered" a question of statutory interpretation if the question had occurred to them. *Id.*

180. See generally LaRue, *Statutory Interpretation: Lord Coke Revisited*, 48 U. PITT. L. REV. 733 (1987) (discussing need to read statutes in relation to problem legislators sought to address).

in which the rule was promulgated. Clearly, opening the interpretative task to include contextual factors potentially empowers the interpreter to depart from the writer's intended meaning and to supply his own. But, in construing legal texts, the check on such interpretative license is the continual seeking of the *writer's* intention, not, as when examining literary texts, responding to the private aesthetic tastes of the *reader*. Seeking the writer's intention preserves the integrity of the rule- or statute-making body from improper encroachment by the interpreting body, often a judge or administrative agency, while freeing that body to seek guidance from sources outside the text itself.

Applying this exegetical principle to the narrow problem of rule 152, for the reasons indicated we have little doubt that the writers of the rule did not intend it to be applied in the way the SEC has done in *Verticom* and subsequent no-action requests. One cannot so cavalierly depart from the intended meaning of a rule in formulating "desirable" legal policy without, in effect, simply substituting the will of the reader (here, the staff of the SEC) for the idea of the rule of law.

Second, because we believe that the SEC reading of rule 152 is erroneous, it is useful to recall that a court is not bound by SEC no-action letters. After all, a no-action letter is just that—a statement that the staff would recommend that the SEC take "no action" if the deeds in question transpired.¹⁸¹ The SEC itself has emphasized that no-action and interpretive responses by the staff are subject to reconsideration and should not be regarded as precedents binding on the full Commission.¹⁸² Additionally, the SEC has reminded issuers that "persons receiving advice from the staff of the Commission that no action will be recommended if they proceed without registration. . . should do so only with full realization that the test so applied may not be proof against claims by purchasers of the security that registration should have been effected."¹⁸³ Thus, while a no-action response can be of considerable comfort to an issuer, inasmuch as neither the full Commission nor a court is bound by the staff's interpretation of rule 152 the securities bar may be lulled into relying too heavily on that interpretation. Nothing prevents an aggrieved purchaser in a section 4(2) private placement from bringing an action against a corporation and arguing that the placement should be integrated with a subsequent registered public offering. In such a case, although the issuer will argue that a court should find the SEC's interpretation of rule 152 to be controlling, the court is free to find that

181. See Lowenfels, *SEC "No-Action" Letters: Some Problems and Suggested Approaches*, 71 COLUM. L. REV. 1256, 1256-57 (1971) (discussing definition and function of "no-action letter").

182. See Securities Act Release No. 33-5073 (July 14, 1970) (stating that no-action and interpretative responses by SEC staff are not binding precedents on SEC); *ABA Task Force Report on Integration*, *supra* note 26, at 613 n.75 (noting that no-action letters do not bind SEC).

183. Securities Act Release No. 33-4552, 1 Fed. Sec. L. Rep. (CCH) ¶ 2783, at 2922 (Nov. 6, 1962).

the private placement and subsequent public offering should be combined, or, at least, that rule 152 is no bar to integration. Therefore, the SEC's reading of rule 152 does not save issuers from claims by those with the greatest incentive to make an integration argument—the investment community.

Third, as a kind of corollary to the above, even if the full Commission rather than the staff was departing from the intended purpose of rule 152 in "interpreting" the rule, the agency action would be improper. As a matter of administrative law it is improper for an agency to use a rule designed for one specific purpose to accomplish an altogether different objective. Courts have long held that agencies can use adjudications to interpret rules, but not to amend or revoke those rules.¹⁸⁴ In not allowing agencies to adjudicatively amend or alter regulations in the name of interpreting them, courts state that agencies are bound by their regulations, and the courts conclude that to depart from a regulation is reversible error.¹⁸⁵ Through its apparently radical interpretation of rule 152, the SEC is departing from the rule's intended purpose. Thus, a court, if given a chance by an aggrieved purchaser, might find that the staff of the SEC has abused its discretion. Moreover, in essence the SEC has used the no-action format to enact its own "pet theory" about one facet of the integration problem.¹⁸⁶ As a matter of proper administrative procedure, not only should an existing rule not be distorted, but the no-action machinery should not be used to effect a dramatic shift in policy. Rather, a more formal rule promulgation, with the attendant safeguards of notice, comment, and careful deliberation, is the preferred avenue of action.

Fourth, the SEC's approach to rule 152 is indicative of its piecemeal approach to the integration problem, an approach that avoids genuinely revisiting the doctrine in a satisfactorily thorough manner. This observation

184. See, e.g., *Montgomery Ward & Co. v. FTC*, 691 F.2d 1322, 1328-29, 1331-32 (9th Cir. 1982) (holding that agency acted improperly in attempting to amend informal rule adjudicatively); *Bahat v. Sureck*, 637 F.2d 1315, 1318 (9th Cir. 1981) (stating that situations exist where agency reliance on adjudication to announce and apply new standard of conduct would be abuse of discretion); *United States v. Frontier Airlines, Inc.*, 563 F.2d 1008, 1011-13 (10th Cir. 1977) (concluding that agency could not adjudicatively undertake action that was inconsistent with agency's informal rule). One problem in analyzing agency behavior in the adjudicatory context is that no clear conception exists between what constitutes an "interpretation" and what constitutes an "amendment." Agencies can keep interpretation within defined parameters. See Weaver, *Judicial Interpretation of Administrative Regulations: An Overview*, 53 U. CIN. L. REV. 681, 721-28 (1984) (discussing approaches to interpretation of statutory language).

185. See *American Fed'n of Gov't Employees, Local 3090 v. NLRB*, 777 F.2d 751, 759 (D.C. Cir. 1985) (stating that agency is bound by rule or regulation until agency amends or repeals rule or regulation by legislative means); *Teleprompter Cable Communication Corp. v. FCC*, 565 F.2d 736, 742 (D.C. Cir. 1977) (stating that FCC's notion of public interest cannot justify FCC's failure to act in manner consistent with FCC precedents).

186. See Lowenfels, *supra* note 181 at 1266-69 (discussing problem that various SEC staff members use "no-action" machinery to enact into "law" their own personal interpretations of securities rules).

has two dimensions. First, the SEC still has not addressed numerous problems and uncertainties in and related to the integration penumbra surrounding staged financing. For example, while rule 152 as the SEC currently interprets it will not result in a public offering being brought “backwards” into a section 4(2) placement, can such a private placement be brought “forward” into a public offering and thereby constitute “gun jumping” of the public offering? Under section 5(c) of the Securities Act the act of offering to sell a security is illegal unless the issuer has filed a registration statement.¹⁸⁷ Because the term “offer” is given a very broad reading, the issuer and others must be careful during the pre-filing period that the issuer’s behavior not be construed as “designed to awaken an interest that later would be focused on [a] specific financing” and that would constitute “the first step in a sales campaign” and so be viewed as an “offer.”¹⁸⁸ An issuer, feeling relieved as to the risk of integration, which relief heightens the attractiveness of the private placement, may engage in selling efforts that link the placement to a soon-to-follow public offering. In doing so the issuer may “in fact contribute to conditioning the public mind or arousing public interest in the issuer or in the securities of an issuer”¹⁸⁹ in a way that raises the prospect that its private financing activities, unless carefully monitored, constitute gun-jumping. Rule 152 simply does not address that separate issue.

Nor does the SEC’s new interpretation of rule 152 have a great deal of practical value. Rule 152 does not preclude the integration of one exempt offering with another exempt offering. Thus, while a single section 4(2) private placement and subsequent registered public offering might not be integrated, true multiround financing is not made significantly easier in view of the fact that a non-section 4(2) exempt transaction (or possibly another section 4(2) transaction) might be integrated with the section 4(2) private placement without preclusion by rule 152. Furthermore, nothing in the rule prevents the integration of a registered public offering with exempt capital formation activity premised on sections other than section 4(2). Thus, rule 152 does not cover integration of transactions grounded on section 3(a)(11) or section 3(b)—which, together, form the legal basis for a great deal of private capital formation—and subsequent registered public offerings. If the SEC wishes to allow an issuer to plan a subsequent public offering before undertaking a private placement pursuant to section 4(2) or rule 506, the SEC should state why an issuer should not also be allowed to plan a public offering to follow a rule 147, rule 504, or rule 505 transaction. While the statutory underpinnings of those rules are not section 4(2), at the time the SEC adopted rule 152—in 1935—there was little flesh to the section 3(b)

187. 15 U.S.C. § 77e (1982).

188. See Securities Act Release No. 33-3844, 1 Fed. Sec. L. Rep. (CCH) ¶ 3256, at 3150 (Oct. 8, 1957) (using examples to illustrate specific pre-filing behavior that would violate § 5 of Securities Act).

189. *Id.* ¶ 3254, at 3149.

exemption. Currently, however, the SEC has issued rules 504 and 505 under section 3(b) and each of the rules represents the striking of a modern regulatory balance between the objectives of investor protection and small issuer capital formation. The logic of the SEC's interpretation of rule 152 should be forthrightly extended to, or forthrightly rejected with respect to, those rules.¹⁹⁰

This last point raises the other dimension of a problem with the SEC's specific action under rule 152—and general inaction on the broader integration front. The SEC has failed to provide a reasoned statement as to *why*, as a policy matter, section 4(2) private placements followed by registered public offerings should not be integrated. Why not also, to choose one small example, refrain from integrating section 4(2) placements followed by rule 504 offerings? What is lacking is a convincing expression of why certain exempted activity preceding *registration* is different. If the later event of registration itself is the key, then why is registration not sufficient to absolve non-section 4(2) exempt activity of the integration taint? If the key is the *nature of the investor* in a section 4(2) placement, then, apart from the aggregation problem, why not free an issuer from the risk of integration created by a subsequent rule 504 offering? And, further, similarly free the issuer from the risk of integration with respect to the rule 504 transaction? And so on.

Fundamentally then, what the SEC has not directly grappled with in the integration area is the same issue that lurks ever near the question of whether the several requirements of a particular exemption have been fulfilled—what today is the purpose of registration? If the purpose is to provide prospective investors with certain mandated information, then, so long as that is done, why have other conditions and proscriptions such as, in the section 4(2) and regulation D area, prohibitions on general solicitation and advertising?¹⁹¹ Why not, for example, have an exemption conditioned

190. See Frome, *Multiround Financings: A New Development on Integration Issue*, N.Y.L.J., Apr. 3, 1986, at 1, col. 1 (arguing that SEC should extend rule 152 to cover rules 504 and 505 of regulation D). Mr. Frome suggests that the SEC should interpret rule 152 more broadly and apply the rule to any regulation D offering rather than merely applying the rule to rule 506 offerings. See *id.* Frome argues that no distinction exists between the regulation exemptions provided under § 4(2) and regulation D. *Id.* Frome argues further that the SEC is acting inconsistently by treating integration questions under the two registration exemptions differently. Frome states that, because the statutory origins of regulation D are found in § 4(2), it follows that, if rule 152 permits a public offering subsequent to a § 4(2) offering, a similar reasoning should prevail to permit a public offering subsequent to any regulation D offering. Frome's argument is flawed, however, in that the statutory origins of regulation D are found in both § 4(2) and § 3(b). Regulation D consists, *inter alia*, of rules 504, 505, and 506. The statutory source of the exemptions that rules 504 and 505 provide is § 3(b) of the Securities Act. See *ABA Task Force Report on Integration*, *supra* note 26, at 604 (noting statutory source of rules 504 and 505). The statutory source of the rule 506 exemption is § 4(2). See *id.* (noting statutory source of rule 506). Rule 152 says nothing about allowing a public offering subsequent to a § 3(b) offering, thus precluding application of that rule to the question of whether a public offering should be integrated with a § 3(b) offering.

191. See generally Daugherty, *Rethinking the Ban on General Solicitation*, 38 EMORY L.J.

solely on the dissemination of substantially the same information as would be received in a registration statement since, if an offering were registered, such information is all that the investor—whether sophisticated or unsophisticated—would receive. The difference, of course, is SEC pre-sale review.

Thus, the real issue is how significant to the modern objectives of regulated capital markets that review remains. We are not here suggesting the wholesale abandonment of SEC review in favor of a self-governing regime essentially administered by the private securities bar, somewhat akin to current practice under regulation D. We contend only that the regulatory issues raised by the new fascination with the specific goal of capital formation and the larger goal of deregulation, be they manifested in calls for relaxing regulation D,¹⁹² rethinking the policy premises and parameters of section 4(2), or clarifying the contours of the integration doctrine, all bottom on more fundamental matters. The SEC, somehow, ought to face those matters squarely, not leave the matters buried in an uncoordinated jumble of regulatory complexity where the sheer mass of rules often makes rethinking of core premises so difficult, but therefore so necessary. However much we would like to provoke express rethinking of the first order questions on which all else in capital market regulation depends, we believe a very modest proposal on a fairly obscure rule can start moving securities professionals and regulators in that direction. We suggest that the SEC either modify its position to conform to the true purpose of rule 152 or change rule 152 to conform to the SEC's interpretation of the rule. And, most important, the SEC should state why it has so acted, and why those actions are both desirable and sufficient.

67 (1989) (advocating that prohibition on general solicitation and advertising be eliminated as condition to § 4(2) exemption).

192. See Securities Act Release No. 33-6825, 54 Fed. Reg. 11,369, 11,374 (1989) (to be codified at 17 C.F.R. § 230.508) (adopting new rule 508 as amendment to regulation D).

APPENDIX

For IMMEDIATE Release Saturday, March 2, 1935.

SECURITIES AND EXCHANGE COMMISSION
Washington

SECURITIES ACT OF 1933
Release No. 305

The Securities and Exchange Commission today announced the adoption of the following rule defining transactions not involving any public offering made prior to the filing of a registration statement. The rule makes clear that offerings made prior to the filing of the registration statement and made under circumstances which did not necessitate registration or contemplate registration, do not by the fact of registration become the type of offerings which are prohibited by the Securities Act. The rule allows those who have contemplated or begun to undertake a private offering to register the securities without incurring any risk of liability as a consequence of having first contemplated or begun to undertake a private offering. The rule is as follows:

Regulation defining transactions not involving any public offering made prior to filing of registration statement. The phrase "transactions by an issuer not involving any public offering" as used in Section 4(1) of the Securities Act of 1933 shall be deemed to apply to transactions not involving any public offering at the time of said transactions although subsequently thereto the issuer decides to make a public offering and/or files a registration statement.