



Summer 6-1-1978

Iv. Rule 10B-6

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Recommended Citation

Iv. Rule 10B-6, 35 Wash. & Lee L. Rev. 845 (1978).

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IV. RULE 10b-6

The Securities and Exchange Commission (SEC) has promulgated certain rules designed to check manipulative acts in the securities market.¹ The primary antimanipulative provision through which the SEC regulates the transactions of participants in a distribution of securities is Rule 10b-6.² This Rule generally prohibits certain persons,³ who participate in the distribution of securities,⁴ from directly or indirectly bidding for or purchasing, or inducing others to bid for or purchase, securities of the same class and series as those distributed until the distribution is completed.⁵ The Rule also enumerates eleven transactions that are excepted from its coverage.⁶

transactions. In one of the transactions, directors of the subsidiary had caused the corporation to make loans to its corporate parents. *Id.* at 662. The plaintiffs claimed that the loans were advanced in violation of a prospectus statement and that this fact and the fact that the loans were for far less than fair consideration were not disclosed. *Id.* at 664. The complaint did not allege that the terms of the loans had not been disclosed, but only that the terms were unfair and that the loans were inconsistent with company policy as stated in the prospectus. *Id.* at 664-65. The court held that since the shareholders were not misled as to the actual terms of the loan transactions, mere nondisclosure of "unfairness" did not rise to the level of deception contemplated in *Santa Fe*. *Id.* at 665. This holding recognized an appropriate limitation in the *Meridor* decision. The *Meridor* court noted that Rule 10b-5 does not require insiders to characterize conflict of interest transactions in pejorative terms. 567 F.2d at 218 n.8. To require disclosure that a transaction is "unfair" in addition to disclosure of the terms of that transaction would amount to requiring a pejorative characterization. Failure to make such "disclosure" is not a sufficient claim of deception after *Santa Fe*. 442 F.2d at 665.

¹ 17 C.F.R. § 240.10b-6, -7, -8, -13 (1977). Rule 10b-6 is the primary antimanipulative provision. See text accompanying notes 2-11 *infra*. Rules 10b-7 and 10b-8 govern the permissible scope of stabilizing transactions during securities offerings. 17 C.F.R. § 240.10b-7, -8 (1977). Rule 10b-13 prohibits manipulative or deceptive devices in connection with exchange or tender offers. 17 C.F.R. § 240.10b-13 (1977); see text accompanying notes 153-157 *infra*.

² 17 C.F.R. 240.10b-6 (1977). Rule 10b-6 was first proposed on May 18, 1954. SEC Securities Exchange Act Release No. 5040 (May 18, 1954) [1952-1956 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 76,294. After being revised in April, 1955, SEC Securities Exchange Act Release No. 5159 (April 19, 1955) [1952-1956 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 76,339, the Rule finally was adopted on August 15, 1955. SEC Securities Exchange Act Release No. 5194 (July 5, 1955) [1952-1956 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 76,350.

³ The classes of persons covered are underwriters and prospective underwriters, see text accompanying notes 39-47 *infra*, issuers or other persons on whose behalf the distribution is being made, see text accompanying notes 48-96 *infra*, and brokers and dealers, see text accompanying notes 96-114 *infra*.

⁴ Neither Rule 10b-6 nor the Securities Exchange Acts define the term "distribution." The SEC and the courts have thus undertaken this task. See, e.g., Collins Sec. Corp., SEC Exchange Act Release No. 11,766 (October 23, 1954) [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327; Bruns, Nordeman & Co., 40 S.E.C. 652 (1961); see text accompanying notes 19-37 *infra*.

⁵ Rule 10b-6 states that such activity shall constitute a "manipulative or deceptive device or contrivance. . . ." See text accompanying notes 7-18 *infra*.

⁶ 17 C.F.R. § 240.10b-6(a)(3)(i)-(xi) (1977). The Rule does not apply to eleven specified transactions because those transactions either do not involve manipulative purposes or are

Section 9(a)(2) of the Securities Exchange Act of 1934⁷ provides the general antimanipulative section upon which Rule 10b-6 is based.⁸ Of particular importance in understanding the thrust of Rule 10b-6 is the prohibition in section 9(a)(2) of transactions that create "actual or apparent active trading" in a distributed security.⁹ The two-fold purpose of this prohibition is to protect against the defrauding of unwary investors and to remove any impediments to a free and open market.¹⁰ Rule 10b-6 was designed to codify principles generally followed by the courts and the SEC in construing section 9 and to define further the phrase "actual and apparent trading activity."¹¹ The classic case of manipulation occurs when persons distributing stock drive up the selling price by making purchases in the market, thereby inducing others to buy at the artificially inflated price.¹²

necessary to allow the offering to proceed. For example, exception (iv), which permits odd-lot transactions by registered odd-lot dealers, and exception (vii), which allows the exercise of any right or conversion privilege to acquire securities, cannot involve manipulative purposes because the transactions are closely regulated and have fixed prices. *See also* exceptions (viii)-(x) (transactions governed by Rules 10b-7, 10b-8, and 10b-2 respectively). Exceptions (i) and (vi) permit underwriters to purchase from an issuer and to solicit purchasers for the distributed securities. No offering could ever proceed without these two essential steps.

Exception (iii) allows unsolicited, privately negotiated purchases of a substantial amount, effected neither on a security exchange nor from or through a broker. The purpose of this exception is to permit the issuer to acquire securities from a large stockholder to add to the distributed securities. *See* Wolfson, *Rule 10b-6: The Illusory Search for Certainty*, 25 STAN. L. REV. 809, 809-10 n.4 (1973) [hereinafter cited as Wolfson]; text accompanying notes 53-58 *infra*. Exception (v) permits brokerage transactions not involving solicitation of the customer's order. *See* PRACTICING LAW INSTITUTE, NINTH ANNUAL INSTITUTE ON SECURITIES REGULATION 216-28 (Mundheim, Fleisher & Vandegrift eds. 1977) [hereinafter cited as NINTH ANNUAL INSTITUTE].

⁷ 15 U.S.C. § 78i(a)(2) (1976). The pertinent part of § 9(a)(2) provides:

"(a) It shall be unlawful for any person, directly or indirectly, by use of the mails or any means . . . of interstate commerce, or of any facility of any national securities exchange, or for any member of a national securities exchange . . . (2) [t]o effect, alone or with one or more persons, a series of transactions in any security registered on a national securities exchange creating actual or apparent active trading in such security or raising or depressing the price of such security, for the purpose of inducing the purchase or sale of such security by others. . .

Section 10(b) of the '34 Act, another general antimanipulative section, prohibits manipulative devices whether in the over-the-counter market or on an exchange in contravention of the rules of the SEC. *Id.* at § 78j(b). Thus the scope of Rule 10b-6 extends to both exchange and over-the-counter markets.

⁸ Wolfson, *supra* note 6, at 809.

⁹ *See* note 7 *supra*.

¹⁰ Masland, Fernon & Anderson, 9 S.E.C. 338, 344 (1941); *see* 3 L. LOSS, SECURITIES REGULATION 1549-60 (2d ed. 1961) [hereinafter cited as L. LOSS]; REPORT OF THE SENATE COMM. ON BANKING AND CURRENCY, STOCK EXCHANGE PRACTICES, S. REP. NO. 1455, 73d Cong., 2d Sess. 54 (1934).

¹¹ SEC Securities Exchange Act Release No. 5194 (July 5, 1955) [1952-1956 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 76,350; Whitney, *Rule 10b-6: The Special Study's Rediscovered Rule*, 62 MICH. L. REV. 567, 568-72 (1964); *see* Foshay, *Market Activities of Participants in Securities Distributions*, 45 VA. L. REV. 907, 918-21, 926-37 (1959).

¹² *See, e.g.,* SEC v. Scott Taylor & Co., 183 F. Supp. 904, 907-09 (S.D.N.Y. 1959).

Section 9(a)(2) identifies the two elements of a prohibited manipulation as a series of transactions¹³ coupled with a purpose of inducing others to purchase or sell a security.¹⁴ Before the adoption of Rule 10b-6, the courts and the SEC had held that manipulative purposes existed where a motive to manipulate could be shown.¹⁵ Since intent is difficult to prove, the courts and the SEC usually relied on circumstantial evidence to establish the requisite state of mind in cases of manipulation.¹⁶ Under Rule 10b-6, however, purchasing or inducing purchases during a distribution is per se manipulative without regard to purpose.¹⁷ By defining certain behavior as per se manipulation, Rule 10b-6 obviates any need for a specific finding of intent.¹⁸

The attempt to curb manipulation by use of Rule 10b-6's per se approach has produced difficulties in the application of the Rule. Since the presence of a distribution makes all unexempted purchases or inducements to purchase a violation of the Rule, the scope of that term determines the applicability of the Rule. While neither the 1933¹⁹ or 1934 Acts defines distribution, the courts²⁰ and the SEC²¹ have struggled to interpret its meaning. Although at one time the SEC distinguished between registered and unregistered stock offerings,²² the generally accepted standard is the

¹³ The Commission has held that as few as three purchases constitute a "series." *Kidder Peabody & Co.*, 18 S.E.C. 559, 568 (1945). A single order might also result in a "series of transactions" if the alleged manipulator knew that the order could not be executed all at one time. *Charles C. Wright*, 3 S.E.C. 190, 206-09 (1938), *rev'd on other grounds Wright v. SEC* 112 F.2d 89 (2d Cir. 1940). Furthermore, the Commission has held that transactions are not limited to purchases and sales but also extend to bids. *Gob Shops of America, Inc.*, 39 S.E.C. 92, 101 (1959); *Halsey, Stuart & Co.*, 30 S.E.C. 106, 121, 125-26 (1949).

¹⁴ Securities Exchange Act of 1934, § 9(a)(2), 15 U.S.C. § 78j(b) (1976); L. Loss, *supra* note 10, at 1550.

¹⁵ See, e.g., *Halsey, Stuart & Co., Inc.*, 30 S.E.C. 106, 124 (1949); *The Federal Corp.*, 25 S.E.C. 227, 231 (1947); *Charles C. Wright*, 3 S.E.C. 190, 206 (1938).

¹⁶ An early SEC decision succinctly stated "Since it is impossible to probe into the depths of a man's mind, it is necessary . . . that the finding of manipulative purpose be based on inferences drawn from circumstantial evidence." *The Federal Corp.*, 25 S.E.C. 227, 230 (1947); see *SEC v. Torr*, 22 F. Supp. 602, 608 (S.D.N.Y. 1938); *Halsey, Stuart & Co., Inc.*, 30 S.E.C. 106, 124 (1949).

¹⁷ 17 C.F.R. 240.10b-6(a) (1977); *Wolfson*, *supra* note 6, at 810-12.

¹⁸ See *Jaffee & Co. v. SEC*, 446 F.2d 387, 391 (2d Cir. 1971). *But see* text accompanying notes 31-35 *infra*.

¹⁹ 15 U.S.C. §§ 77a-77bb (1976).

²⁰ See, e.g., *Byrnes v. Faulkner, Dawkins & Sullivan*, 413 F. Supp. 453 (S.D.N.Y. 1976), *aff'd* 550 F.2d 1303 (2d Cir. 1977); *SEC v. Georgia Pacific Corp.*, 272 F. Supp. 148 (S.D.N.Y. 1967).

²¹ See, e.g., *Collins Sec. Corp.*, SEC Exchange Act Release No. 11,766 [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 82,327; *Jaffee & Co.*, 44 S.E.C. 285 (1970); *aff'd in part, vacated in part Jaffee & Co. v. SEC*, 446 F.2d 387 (2d Cir. 1971); *Bruns, Nordeman & Co.*, 40 S.E.C. 652 (1961).

²² In *Jaffee & Co.*, 44 S.E.C. 285 (1970), the SEC had held that a distribution under the Securities Exchange Act of 1933, 15 U.S.C. §§ 77a-77bb (1976), was also a distribution for Rule 10b-6 purposes. 44 S.E.C. at 288. In *Jaffee*, a broker was appointed agent for thirty-four selling stockholders in an offering of about 28% of the outstanding stock of Solitron Corporation. The biggest block involved was registered on a shelf registration by one of the partners

facts and circumstances test originally formulated by the SEC in *Bruns, Nordeman & Company*.²³ The *Bruns, Nordeman* test is "to be interpreted in light of the Rule's purposes" and focuses upon the selling efforts utilized and the magnitude of the offering.²⁴ This necessarily requires a case by case determination. The relation of the amount of stock offered to the total amount outstanding,²⁵ the amount of "float,"²⁶ and the amount of normal trading volume for that particular security²⁷ are examined to determine whether the magnitude of the offering constitutes a distribution. Any extra sales commission paid to the broker,²⁸ the sales literature employed to recommend the stock,²⁹ and the number of investors to whom the securities are offered³⁰ are the factors used to evaluate the selling effort. Moreover,

in *Jaffee & Company*. Another broker made purchases on behalf of Jaffee from the appointed agent. Jaffee argued that a shelf registration, while a distribution under the '33 Act because the offering was syndicated and under a registration statement, was not a distribution for Rule 10b-6 purposes. *Id.* at 288. The SEC maintained, however, that such an offering was a distribution per se, *id.* at 288-89, stating only that an offering of stock pursuant to a registration statement is "by its very nature" a 10b-6 distribution. *Id.* at 288.

Commissioner Smith disagreed with this per se approach, stating that the purpose of the '33 Act registration was to provide adequate disclosure and not to prevent manipulation. *Id.* at 296-97. Forecasting the demise of this per se application of 10b-6 to all registered distributions, Commissioner Smith advocated the position ultimately taken by the SEC in *Collins Sec. Corp.* SEC Exchange Act Release No. 11,766 (Oct. 23, 1975) [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327; see text accompanying notes 21-35 *infra*.

²³ 40 S.E.C. 652 (1961). While the *Bruns, Nordeman* test was formulated in the context of an unregistered distribution, the SEC's decision in *Collins Sec. Corp.* made it applicable to registered distributions also. [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327 at 85,800.

²⁴ 40 S.E.C. at 660.

²⁵ See, e.g., *Collins Sec. Corp.*, SEC Exchange Act Release No. 11,766 (Oct. 23, 1975) [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327, at 85,800. In *Collins*, the fact that the offering amounted to 30% of the issuer's outstanding stock made the offering clearly a distribution. *Id.*

²⁶ NINTH ANNUAL INSTITUTE, *supra* note 6, at 203.

²⁷ See, e.g., *Collins Sec. Corp.*, SEC Exchange Act Release No. 11,766 (Oct. 25, 1975) [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327, at 85,795-96. The SEC emphasized that the market for the manipulated stock in *Collins Sec. Corp.* was stagnant and that only two brokers were entering quotations for the stock. *Id.* at 85,795. Thus, when the market for a stock is so inactive, even the trading of a small number of shares will increase the market price. *Id.* at 85,796. Trading in a stock that has previously been very inactive such as in *Collins Sec. Corp.* is very strong circumstantial evidence of manipulative purpose and therefore evidence of a distribution for 10b-6 purposes. *Id.* at 85,799; see text accompanying notes 21-24 *supra* and notes 31-35 *infra*.

²⁸ Extra sales commission paid to a broker indicates the increased interest of the issuer in distributing its stock and provides extra incentive for the broker to accomplish that goal. Both factors make it more likely that manipulation may occur to further those objectives. See NINTH ANNUAL INSTITUTE, *supra* note 6, at 202-03; Wolfson, *supra* note 6, at 820-21.

²⁹ See *Collins Sec. Corp.*, SEC Exchange Act Release No. 11,766 (Oct. 23, 1975) [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327, at 85,796-97 (letters advertising warrants sent with prospectus; second notice sent reminded shareholders of expiration date and urged immediate action; and telephone canvas made of warrant holders); F.S. Johns & Co., SEC Exchange Act Release No. 7972 (Oct. 10, 1966) [1966-1967 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 77,410; see NINTH ANNUAL INSTITUTE, *supra* note 6, at 202-03; Wolfson, *supra* note 6, at 820.

the presence of any one factor alone may identify a distribution because that factor so greatly differentiates the offering from a normal trading transaction.³¹

By focusing on these factors, the *Bruns, Nordeman* test attempts to find a distribution in situations where the application of Rule 10b-6 will serve the antimanipulative purposes for which it was drafted.³² Special selling efforts identify circumstances where both the temptation and opportunity to manipulate the market exist.³³ The use of such a pragmatic test, however, has led to the infusion of the element of purpose into the Rule and thus has sacrificed the advantages of a per se application of the Rule.³⁴ Nevertheless, the *Bruns, Nordeman* test has the advantages of precluding arbitrary stifling of bona fide market activity and of allowing the SEC and the courts to adapt the Rule to manipulative practices in novel situations.³⁵

The *Bruns, Nordeman* criteria make Rule 10b-6 distributions difficult to identify with any certainty because the key is not the existence of some concrete entity named a distribution but the existence of a substantial interest in manipulation coupled with trading activity.³⁶ One person's ordinary trading transaction may be another's distribution due to the presence of an interest to manipulate.³⁷ By identifying a distribution through factors that demonstrate a possible motive to manipulate the market, the test determines which parties are subject to the Rule. When a participant in an offering of stock acquires sufficient interest to manipulate the market, the *Bruns, Nordeman* test identifies a distribution and triggers the application of Rule 10b-6 to that participant.

The first group of persons identified in the Rule as participants in the distributive process are underwriters³⁸ and "prospective underwriters."³⁹ In

³¹ The nature of the selling effort appears to be more important than the magnitude of the offering. For example, the SEC found a distribution in an offering of less than 1% of the outstanding securities because of the selling effort. *SEC v. Electronics Sec. Corp.*, 217 F. Supp. 831 (D. Minn. 1963).

³² *Collins Sec. Corp.*, SEC Exchange Act Release No. 11,766 (Oct. 23, 1975) [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327, at 85,800; *Bruns, Nordeman & Co.*, 40 S.E.C. 652, 655 (1961).

³³ Special selling efforts differentiate the transaction from an ordinary one and indicate that the persons involved may have a motive to manipulate the market. This is essentially what the concept of distribution intends to define. See text accompanying notes 23-31 *supra*.

³⁴ *Wolfson*, *supra* note 6, at 812, 821.

³⁵ *Id.* at 812-14, 821.

³⁶ See *Wolfson*, *supra* note 6, at 821; text accompanying notes 23-31 *supra*.

³⁷ See *Collins Sec. Corp.*, SEC Exchange Act Release No. 11,766 (Oct. 23, 1975) [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327, at 85,800 (dealing in distributed security by market maker as part of normal activity not a distribution); *Scott & Stringfellow, Inc.*, (May 10, 1977) [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,232 (no action letter); text accompanying notes 102-105 *infra*.

³⁸ 17 C.F.R. 10b-6(c)(1) (1977). An underwriter is an investment company that specializes in the marketing of new issues of securities. The underwriter may act strictly as an agent of the seller (a "best efforts" underwriting), or may purchase the issue outright and then sell to the public. Usually a managing underwriter will form a syndicate of underwriters who each

the competitive bid situation,⁴⁰ an underwriter is subject to the Rule when he submits a bid to become an underwriter.⁴¹ In negotiated underwritings,⁴² an underwriter is subject to the Rule when he reaches an understanding with the issuer that he will underwrite that particular offering.⁴³ Under the specific language of the Rule, a prospective underwriter refers only to a person "who has reached an understanding *with the issuer*. . ." and therefore applies only to the managing underwriter.⁴⁴ Other underwriters may be subject to the Rule, however, soon after the registration statement is filed either on the theory that they are broker-dealers who have agreed to participate⁴⁵ or on the theory that the managing underwriter is their agent.⁴⁶ Once the other underwriters receive their invitations to participate and make the business judgment to accept, they should consider themselves subject to the Rule as a practical matter even though they have not formally accepted by notifying the managing underwriter.⁴⁷

take a portion of the issue. Underwriters receive commissions or a concession off the public offering price as their compensation. *See generally* 1 L. LOSS, *supra* note 6, at 159-72; PRACTICING LAW INSTITUTE, WHEN CORPORATIONS GO PUBLIC (C. Israel & G. Duff, Jr. eds. 1962).

³⁹ Rule 10b-6 defines a "prospective underwriter" as a "person (i) who has agreed to submit or has submitted a bid to become an underwriter of securities as to which the issuer, or other person on whose behalf the distribution is to be made, has issued a public invitation for bids, or (ii) who has reached an understanding, with the issuer or other person on whose behalf a distribution is to be made, that he will become an underwriter, whether or not the terms and conditions of the underwriting have been agreed upon."

17 C.F.R. § 240.10b-6(c)(2) (1977).

⁴⁰ A competitive bidding situation occurs when a group of underwriters form a syndicate in order to submit a bid to underwrite. The issuer then awards the issue to the lowest syndicate bid. 1 L. LOSS, *supra* note 6, at 159-72.

⁴¹ The members of the underwriting syndicate are subject to Rule 10b-6 when they submit their bid, and not when the syndicate is formed or when the bid price is agreed upon, because the Rule contemplates agreement with the issuer. 17 C.F.R. § 240.10b(c)(2)(ii) (1977); *see* NINTH ANNUAL INSTITUTE, *supra* note 6, at 212.

⁴² In the usual negotiated underwriting, the issuer meets with an underwriter, the underwriter makes a preliminary examination of the issuer, and then the underwriter decides whether to go ahead with the offering. The exact terms of price and other details are reached before the effective date of the registration statement. *See generally* JENNINGS & MARSH, SECURITIES REGULATION 23 (4th ed. 1977) [hereinafter cited as JENNINGS & MARSH].

⁴³ 17 C.F.R. § 240.10b-6(c)(1) (1977). Once the understanding with the issuer is reached, the underwriter has acquired a significant interest in the price of the issue although he is not legally committed. The underwriter's interest in the price stems from the fact that his commission is based upon it. In a firm commitment offering, he will be forced to retain any stock he cannot sell to the public. *See* Wolfson, *supra* note 6, at 824-25.

⁴⁴ 17 C.F.R. § 240.10b-6(c)(2)(ii) (1977) (emphasis added).

⁴⁵ Lum's, Inc., 43 S.E.C. 223, 236 (1966); *see* text accompanying notes 97-117 *infra*.

⁴⁶ *Id.*; *cf.* Hazel Bishop, Inc., 40 S.E.C. 718, 736 (1961) (broker who acted as selling shareholder's agent is subject to Rule 10b-6).

⁴⁷ An invited underwriter could technically argue that since it has no contractual agreement with the issuer until notification of acceptance, he has no agreement to participate. An express agreement has not been necessary, however, to find participation in some instances. *See, e.g.*, Lum's Inc., 43 S.E.C. 223, 236 (1966); Hazel Bishop Inc., 40 S.E.C. 718, 736 (1961). From a practical viewpoint, the decision to accept should trigger compliance because notification of acceptance is a mere formality. NINTH ANNUAL INSTITUTE, *supra* note 6, at 210-12.

Issuers or other persons on whose behalf a distribution is made are the second major group of persons subject to Rule 10b-6.⁴⁸ Selling shareholders are covered by the "other persons" language. Since an issuer is usually a corporation, the SEC staff holds officers, directors and anyone in a control relationship subject to the Rule although such persons are not specifically mentioned.⁴⁹ Further, if the decision to sell is made solely by shareholders who are officers, directors or control persons of an issuer, the issuer is nonetheless subject to the Rule on the basis that the control persons' close relationship with the issuer and the issuer's participation in the preparation, execution and filing of the registration statement constitutes participation in the distribution.⁵⁰

Nevertheless, exemptions are available which enable issuers to make purchases of their stock even when control persons propose to sell shares under a shelf registration.⁵¹ The SEC has developed standard guidelines that permit an issuer to trade so long as the issuer's purchase program and the control persons' sales are harmonized to avoid any distortion of the market.⁵² The staff explained the interplay of these conditions in a recent no-action letter.⁵³ The SEC stated in the letter that a control person of a company must notify the company one week before the person is to make any sales and the company must discontinue all purchases until the seller

⁴⁸ 17 C.F.R. § 240.10b-6(a)(2) (1977).

⁴⁹ In 1956, the SEC proposed to amend Rule 10b-6 to extend specifically to officers, directors and control persons of an issuer. SEC Exchange Act Release No. 5415 (Dec. 5, 1956) [1952-1956 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 76,417. The proposal was never adopted however. For the SEC position on such persons, see *Richland v. Cheatham*, 272 F. Supp. 148 (S.D.N.Y. 1966). See also *SEC v. Resch-Cassin*, 362 F. Supp. 964 (S.D.N.Y. 1973); *SEC v. Scott Taylor & Co.*, 183 F. Supp. 904 (S.D.N.Y. 1960) (Rule 10b-6 applied to all officers, directors and control persons of underwriter or other broker-dealer participants in distribution).

⁵⁰ The problem of issuer involvement in a distribution by its officers, directors or other control persons is another illustration of the issue of whether Rule 10b-6 should be applied automatically by its language or only to those situations where a manipulative purpose may be present. See text accompanying notes 19-37 *supra*. Since the Rule applies to an issuer "on whose behalf [the] distribution is being made" and to a person "who has agreed to participate," an automatic application of the Rule to the issuer could result whenever control persons sell a significant amount of stock. 17 C.F.R. § 240.10b-6(a)(2)(3) (1977). If the issuer's involvement or interest in the success of the control persons' offering is analyzed, however, the Rule could then be more appropriately applied in light of its purpose. See NINTH ANNUAL INSTITUTE, *supra* note 6, at 208-210.

A more difficult question is presented when strangers to the company are effecting sales under a registration statement prepared and filed by the issuer. See, e.g., *Cooper Laboratories, Inc.* [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,032 (no-action letter). However, a similar analysis focusing on the issuer's interest in the stockholder's sales would prove useful.

⁵¹ Exemptions are allowed if the SEC determines that the transaction does not constitute a manipulative device within the purpose of the Rule pursuant to 17 C.F.R. § 240.10b-6(f) (1977).

⁵² Appendices 1-B and B-6 are included in almost every no-action letter issued by the Commission. See 2 FED. SEC. L. REP. (CCH) ¶ 22,726.11.

⁵³ *Capital Cities Communications, Inc.* [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,854.

notifies the company that he will make no further purchases.⁵⁴ The thrust of this requirement is to prevent insiders of a company from selling company stock at a price which has been influenced by company purchases.⁵⁵ Direct purchases by the company of stock from selling insiders are not prohibited by the Rule, however, as long as such purchases are not solicited by the company and are not to the advantage of any insider.⁵⁶ Analogous to this situation is whether large block purchases by the company are also prohibited. The Commission staff maintains that there is no waiting period after the insiders' sales are completed⁵⁷ and that Rule 10b-6(a)(3)(iii) excepts "unsolicited privately negotiated purchases . . . (of) a substantial amount. . . ."⁵⁸

The Commission staff also has attempted to apply Rule 10b-6 only if necessary when confronted with the problem of issuer purchases. In another recent no action letter,⁵⁹ the SEC responded to an issuing company that wanted to purchase its common stock as a defensive maneuver against a tender offer the company considered to be against the best interests of its shareholders. The company feared the application of the Rule because officers and directors had simultaneously proposed to sell 25,000 shares under a registration statement.⁶⁰ While indicating that a secondary offering by the control persons might constitute a distribution for 10b-6 purposes,⁶¹ the small number of shares offered compared to the total outstanding,⁶² the fact that no special effort to sell was to be made,⁶³ and the fact that the qualified options currently exercisable covered only a small number of shares⁶⁴ combined to preclude the possibility that purchases by the company would be for manipulative purposes.⁶⁵

Issuer purchases of its own stock for employee stock benefit plans also may be subject to Rule 10b-6 due to the actions of control persons.⁶⁶ The

⁵⁴ *Id.* at 87, 258-59. See also 2 FED. SEC. L. REP. (CCH) ¶ 22,726.11.

⁵⁵ Capital Cities Communications, Inc., [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,854, at 87,259.

⁵⁶ *Id.*

⁵⁷ Appendix 1-B, 2 FED. SEC. L. REP. (CCH) ¶ 22,726.11.

⁵⁸ 17 C.F.R. § 240.10b-6(a)(3)(iii) (1977). The exception is not precluded by the Appendix. Capital Cities Communication, Inc. [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,854, at 87,259.

⁵⁹ Inexco Oil Co., [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,943.

⁶⁰ *Id.* at 87,486-87.

⁶¹ The Commission staff said the matter was "not free from doubt." *Id.*

⁶² The 25,000 shares offered by the control persons were insignificant when compared with the over 11 million shares of Inexco outstanding. *Id.*

⁶³ No underwriter was employed to sell the shares. *Id.*

⁶⁴ The options exercisable by the control persons covered only 45,000 shares. *Id.*

⁶⁵ *Id.* The analysis of factors by the staff in the *Inexco* letter closely resembles the *Bruns, Nordeman* test. See text accompanying notes 21-29 *supra*.

⁶⁶ Some employee stock plans are automatically excluded from Rule 10b-6 restrictions by paragraph (e). 17 C.F.R. § 240.10b-6(e) (1977). In order to qualify for the exclusion, the plan must either meet the requirements of §§ 422 and 423 or § 424(b) of the Internal Revenue Code of 1954 or be a plan providing for periodic payments for acquisitions by employees and periodic purchases by either the employees or the person acquiring the securities for the

greatest possibility for manipulation in this context arises when a company is contemplating an exchange or merger offer with another company. Because the exchange formula is a function of the price of the acquiring company's stock which may be driven up by company purchases of its own stock, the type of artificial market influence proscribed by Rule 10b-6 is clearly present. The market price of the stock would then reflect the inflated value caused by the acquiring company's purchases and not the true market value.⁶⁷

The crucial issue in the exchange offer context concerns the point at which the distribution commences so that the time when the acquiring company may not make any more purchases can be determined. In *Richland v. Cheatham*,⁶⁸ the district court confronted this issue only implicitly. The case is important, however, because the terms of that judgment have served as a model for subsequent staff restrictions. The SEC restrained Georgia Pacific, the acquiring company, from directly or indirectly bidding for or purchasing any Georgia Pacific stock after an agreement in principle had been reached for the acquisition of the target company. Purchases and bids for stock within ten days prior to the time the market price of Georgia Pacific stock was to be used to determine the exchange ratio were also prohibited.⁷⁰ Georgia Pacific also agreed to disclose the daily volume and prices of purchases made after the commencement of serious negotiations.⁷¹ Because the prohibition on purchases began when an agreement in principle had been reached, the court and the SEC implicitly recognized at least this point as the commencement of the distribution.

Subsequent to the *Richland* judgment, the SEC issued releases which further tightened the restrictions on purchases enunciated in *Richland*.⁷² The SEC indicated that the restrictions now commence when a "definite arrangement" to acquire has been made⁷³ and that the disclosure obligation now arises at "the very beginning of negotiations."⁷⁴ Nevertheless, these disclosure guidelines do not mark the commencement of the distribu-

employees. 17 C.F.R. § 240.10b-6(e) (1977); cf. Tandy Brands, Inc., [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,161 (trustees made purchases at sole discretion of company, plan held not exempt).

⁶⁷ See *Richland v. Cheatham*, 272 F. Supp. 148 (S.D.N.Y. 1966).

⁶⁸ *Id.*

⁶⁹ See, e.g., Lincoln Am. Corp., [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,040 (no action letter); MEI Corp., [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,855 (no action letter).

⁷⁰ 272 F. Supp. at 151.

⁷¹ *Id.*

⁷² Genesco, Inc., [1964-1966 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 77,354; Appendix B-6, 2 FED. SEC. L. REP. (CCH) ¶ 22,726.11.

⁷³ *Id.* A "definite arrangement" may be made earlier than the "agreement in principle" discussed in *Richland v. Cheatham*. See, e.g., *Fridrich v. Bradford*, [1974-1975 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,723 (M.D. Tenn. 1974), *rev'd on other grounds*, 542 F.2d 307 (6th Cir. 1976), *cert. denied*, 429 U.S. 1053 (1977).

⁷⁴ Appendix B-6, 2 FED. SEC. L. REP. (CCH) ¶ 26,726.11.

tion because the disclosure obligation illustrates that such purchases are permissible, which would not be true if the distribution had commenced.⁷⁵ Rather, the "definite arrangement" to acquire the target company marks the commencement of the distribution.⁷⁶

Because many employee stock purchase plans do not satisfy the stringent requirements of paragraph (e) of Rule 10b-6,⁷⁷ issuers must frequently ask the Commission staff for rulings on the application of the Rule to transactions pursuant to such plans. Many of the restrictions of the *Richland* judgment and the principles involved in Rule 10b-6 are well illustrated by some of the more recent no action letters. The most common situation in which a company has asked for an exemption has been when the employee stock plan fails in some minor way to meet the requirements of Rule 10b-6(e). For example, the plan may have non-qualified, non-restrictive options held by control persons,⁷⁸ or the purchases may be controlled by the company and therefore not be periodic.⁷⁹ In such situations, the SEC has granted exemptions because neither the amounts of stock involved nor the circumstances of the purchase show any manipulative purpose.⁸⁰

Nevertheless, company purchases of its own stock for employee plans often cause Rule 10b-6 problems in more irregular contexts that call for closer examination of the transactions. Recently, a corporation proposed to make a cash tender offer for approximately one-fifth of its outstanding stock.⁸¹ The company also had an employee stock plan that did not fit the paragraph (e) exemption because the company retained sole discretion over the terms and prices at which the stock would be purchased.⁸² The significant amount of shares involved in the tender offer and the com-

⁷⁵ PRACTICING LAW INSTITUTE, EIGHTH ANNUAL INSTITUTE ON SECURITIES REGULATION 235 (Mundheim, Fleisher, & Vandegrift, eds. 1976) [hereinafter cited as EIGHTH ANNUAL INSTITUTE].

⁷⁶ See *Fridrich v. Bradford* [1974-1975 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,723 (M.D. Tenn. 1974).

⁷⁷ See text accompanying note 66 *supra*.

⁷⁸ See, e.g., *McDonald's Corp.* [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,233 (no action letter) (unrestricted stock options); *Modern Merchandising, Inc.*, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,202 (no action letter) (warrants held by control persons).

⁷⁹ *Uniroyal, Inc.*, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,162 (no action letter) (company exercises control and influence over purchases); *Tandy Brands, Inc.*, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,161 (no action letter) (purchases made at sole discretion of company).

⁸⁰ No manipulative purpose is present because either the amount of shares distributed pursuant to the plan is small as compared to the company's total outstanding shares, see *McDonald's Corp.* [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,233 (no action letter), or the distribution to employees is the only one in which the company is engaged, see *Tandy Brands, Inc.*, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,161 (no action letter).

⁸¹ *Tandy Corp.* [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,284 (no action letter).

⁸² *Id.* at 88,347.

pany's unlimited power over employee stock purchases gave the company both the capability and the temptation to manipulate the market.⁸³ However, the staff granted a no action position to the company.⁸⁴ Following safe practice, the company had suspended all purchases at the time management determined to submit the tender offer proposal to the company's board of directors,⁸⁵ thereby eliminating any market impact on the shareholder's decision to tender. Other conditions were imposed to insure fairness to the tendering shareholders.⁸⁶

Employee plans of this sort often have appointed trustees to make the purchases of the company's stock for the plan.⁸⁷ When the trustee is independent of the company and the trustee and company do not have common control persons, Rule 10b-6 problems usually do not arise.⁸⁸ When the company has wholly owned subsidiary broker-dealers, however, any transactions of the subsidiaries in the parent company's stock with the trustee present 10b-6 issues. The Commission is concerned that a broker-dealer's professional expertise and proximity to the market for its own securities afford greater opportunity to affect the market price.⁸⁹ Therefore, the SEC's proposed Rule 13e-2 would prohibit an issuer who is also a broker-dealer from purchasing its own securities except through a totally independent agent.⁹⁰ In a recent no action letter, the Commission applied similar reasoning to prevent a wholly owned subsidiary broker-dealer from selling the issuer parent company's stock to an independent trustee of the company's employee stock purchase plan.⁹¹ The parent company claimed that the trustee and the subsidiary conducted arms-length deals, that each had

⁸³ See *id.*; text accompanying notes 21-29 *supra*.

⁸⁴ Tandy Corp., [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,284 (no action letter).

⁸⁵ *Id.* at 88,349.

⁸⁶ The conditions imposed by the SEC were: (1) appropriate notice to all holders of the company's common stock; (2) shares of common stock tendered could be withdrawn at any time until seven days after the offer was published or at any time within sixty days of the original offer; (3) any increased consideration paid for shares acquired after the offer must be paid to all who tendered. These conditions are fairly typical of limitations placed on tender offerors when Rule 10b-6 may be applicable. See, e.g., NICOR, Inc., [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,308 (no action letter); Ethyl Corp., [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,105 (no action letter).

⁸⁷ See 17 C.F.R. § 240.10b-6(e) (1977).

⁸⁸ See, e.g., The Mead Corp., [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,307 (no action letter). If the issuer has no control over the trustee's purchases, it has no capability to manipulate the market. Thus, application of Rule 10b-6 would not further the Rule's purposes.

⁸⁹ Inter-Regional Fin. Group, Inc. [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,042, at 87,757 (no action letter).

⁹⁰ See SEC Exchange Act Release No. 10539 (Dec. 6, 1973) [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 79,600. Proposed Rule 13e-2 would impose certain limitations on issuer purchases of their own securities. The proposal includes express provisions for employee stock plans that exempt such plans from Rule 10b-6. *Id.* at 83,574. See generally JENNINGS & MARSH, *supra* note 42, at 769-778.

⁹¹ Inter-Regional Fin. Group, Inc., [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,042 (no action letter).

separate fiduciary duties, that the broker-dealer subsidiary's customers would be disserved if they could not trade parent company stock, and that neither the trustee nor the parent company controlled the stock's prices.⁹² The Commission still denied the request, claiming that the purpose of the independent agent requirement of proposed Rule 13e-2 would be undermined if that agent could trade with subsidiaries of the parent company.⁹³ While the Commission may have been unduly cautious considering the many safeguards on the transaction and its valid business purpose,⁹⁴ the motive and capability to manipulate the market are present and Rule 10b-6 should apply.⁹⁵

The third category of persons explicitly covered by Rule 10b-6 are brokers and dealers.⁹⁶ Under the terms of the Rule, they are subject to its prohibitions when they have agreed to participate, or are participating, directly or indirectly, in the distribution.⁹⁷ Thus, a broker-dealer⁹⁸ is probably subject to the Rule when he solicits his customers and is clearly subject to the Rule when he accepts his allotment from the underwriter, even if this occurs prior to the effective date of the offering.⁹⁹ Acceptance of the allotment and solicitation of customers demonstrate that the broker-dealer has committed himself to participate in the distribution. Furthermore, no express agreement or contractual understanding is necessary to find that a dealer is a participant in the distribution, as any furthering or facilitating of the offering will suffice.¹⁰⁰ Similarly, a broker-dealer is subject to the Rule if others place bids for him,¹⁰¹ and the agent who places the bids is also subject to Rule 10b-6 if he should have known that the traded securities were being distributed.¹⁰²

⁹² *Id.* at 87,758-59.

⁹³ *Id.* at 87,757.

⁹⁴ Besides the arms-length nature of the transaction, the separate fiduciary duties of trustee and subsidiary, and the company's lack of control over the stock's prices, the company further demonstrated that the purchases would be made in compliance with certain New York Stock Exchange rules. *Id.* at 87,758.

⁹⁵ See SEC Exchange Act Release No. 10539 (Dec. 6, 1973), [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 79,600.

⁹⁶ 17 C.F.R. § 240.10b-6(a)(3) (1977).

⁹⁷ *Id.*

⁹⁸ There is no practical difference between a "broker" and a "dealer" in the securities industry. See REPORT OF SPECIAL STUDY OF SECURITIES MARKETS, H.R. DOC. NO. 95, 88th Cong., 1st Sess. [pt 1, pp. 17-19] (1963). The term broker-dealer is used in this article to embrace individual proprietorships, partnerships, and corporations that engage in the business of effecting securities transactions with or for the investing public, whether they act as agents for others or buy and sell for their own accounts, and whether they style themselves brokerage firms, investment bankers, or securities dealers.

⁹⁹ Wolfson, *supra* note 6, at 877.

¹⁰⁰ *Id.*; see, e.g., SEC v. Scott Taylor & Co., 183 F. Supp. 904, 908-09 (S.D.N.Y. 1959). In *Scott Taylor*, a broker was held to have violated Rule 10b-6 based upon the fact that he knew that the securities he supplied to Scott Taylor would be offered and distributed. The court held that the broker thereby facilitated and furthered the distribution. *Id.*

¹⁰¹ Causing others to place bids for the broker-dealer would be covered by the "indirectly bids for" language of Rule 10b-6. 17 C.F.R. § 240.10b-6(a)(3) (1977).

¹⁰² See *Dlugash v. SEC*, 373 F.2d 107 (2d Cir. 1967). In *Dlugash*, the agent, Douglas

Because market makers¹⁰³ buy and sell securities during a distribution to maintain a liquid market and facilitate the offering, they are subject to Rule 10b-6 if they are deemed to be participating in a distribution.¹⁰⁴ Under the SEC's prior view that any shelf registered offering was a distribution for 10b-6 purposes, any person who traded the securities covered by the registration statement was a participant and subject to the Rule.¹⁰⁵ As a result, sales to market makers were excluded as a means by which shelf registration securities might be offered.¹⁰⁶ The Commission's opinion in *Collins Securities Corp.*,¹⁰⁷ overruling the per se application of distribution to securities sold under a registration statement, however, gave helpful guidance to permissible market making activities. The *Collins* opinion, while not specifically discussing the scope of the term "participation", concluded that a market maker's normal trading activities in distributed stock are not prohibited by the Rule.¹⁰⁸ This conclusion implicitly recog-

Enterprises, was to place quotations for another broker-dealer, F.S. Johns & Company, at prices dictated by F.S. Johns. Douglas claimed it was unaware of any manipulative scheme, but the court noted that Douglas knew there was no demand for the stock and that rapidly rising prices in the absence of demand are well-known symptoms of unlawful market activity. Such facts put Douglas on notice that a distribution was in progress. *Id.* at 109-10.

¹⁰³ A market maker is a broker-dealer who quotes both a bid and asked price, and stands ready either to buy or sell as principal in reasonable quantities. The readiness of firms to make a continuous market is essential to the existence of a liquid stock market. Wolfson, *supra* note 6, at 815 n.34; see 17 C.F.R. § 240.17a-9(f)(1) (1977).

¹⁰⁴ Market makers, if deemed to be participating in the distribution by selling the offered securities, could not purchase those same securities. 17 C.F.R. § 240.10b-6 (1977); see Wolfson, *supra* note 6, at 817.

¹⁰⁵ *Jaffee & Co.*, 44 S.E.C. 285 (1970); *aff'd in part, rev'd in part*, *Jaffee & Co. v. SEC*, 446 F.2d 387 (2d Cir. 1971). In *Jaffee*, a market maker was held to have violated Rule 10b-6 by its purchase of 25,000 of the 107,700 shares offered from another broker-dealer who had been appointed exclusive agent for the selling shareholders. The market maker had not agreed to participate and claimed that its transactions were part of its normal trading activities. 44 S.E.C. at 288. The Commission, however, held that the market maker was aware of the distribution because it had received a prospectus from the appointed agent and thus violated Rule 10b-6 by its transactions. *Id.* at 290.

In dissent, Commissioner Smith correctly noted that to require any market maker who buys shares covered by a registration statement to withdraw from sales would unnecessarily disrupt the trading market. *Id.* at 298. If the Rule is applied in light of its purposes, see text accompanying notes 21-29 *supra*, there is no reason to prohibit normal trading transactions where no manipulative purposes exist. 44 S.E.C. at 298. Commissioner Smith's position was ultimately accepted in *Collins Sec. Corp.* [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327.

¹⁰⁶ NINTH ANNUAL INSTITUTE, *supra* note 6, at 213. In response to a request for a no action position, the Commission staff outlined four methods by which shelf registered securities might be sold: (1) directly by the broker-dealer to its customers; (2) through a syndication of underwriters; (3) by a placement of bid wanted solicitations in the pink sheets; (4) by sales under Rule 144 after the registration becomes stale. All these eliminate the purchase end of the broker-dealer's market making functions. See *Siliconix, Inc.*, [1974-1975 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327.

¹⁰⁷ SEC Exchange Act Release No. 11,766 (Oct. 23, 1975), [1975-1976 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 80,327.

¹⁰⁸ The Commission stated in *Collins* that it would unnecessarily disrupt the market and extend the restrictions of 10b-6 beyond their purpose to prohibit such activity. *Id.* at 85,800.

nized that a market maker does not participate in the stock's distribution. In a recent letter, the staff declined to give a no action position to a market maker because its sales might constitute a distribution, but did state that sales by a dealer which are part of his usual and customary market making activities are not generally viewed by the SEC as involvement in a distribution.¹⁰⁹

*Byrnes v. Faulkner, Dawkins & Sullivan*¹¹⁰ further illustrates the scope of the term "participation" in 10b-6 as it relates to market makers. The market maker in *Byrnes* attempted to rescind a sale when it found that the shares were covered by a registration statement.¹¹¹ The district court found that the market maker was not participating in the offering and thus did not fall within Rule 10b-6 prohibitions.¹¹² The court based this finding by focusing on the nature and extent of the particular market maker's role rather than the nature of the offering in general.¹¹³ While the court found that a distribution was in progress, it held that the market maker did not participate in that distribution because the number of shares involved were a very small percentage of the total registered shares, and the market maker's purchase was in the ordinary course of its business.¹¹⁴

The *Collins* and *Byrnes* opinions stand for the proposition that a market maker will not automatically be deemed a participant in a distribution solely because the shares are covered by a registration statement. This application of a facts and circumstances test to determine the scope of the individual's participation is consistent with the Rule's application in other situations.¹¹⁵

Rule 10b-6 can accomplish its antimanipulative objectives without inadvertently obstructing bona fide market activity if the Rule is applied when the facts and circumstances indicate that a transaction contains possible opportunities to manipulate the market. The recent letters and cases discussed illustrate that a flexible application of Rule 10b-6 achieves greater effectiveness and simultaneously does not unduly restrict legitimate business transactions in the securities market.

¹⁰⁹ Scott & Stringfellow, Inc. [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,232.

¹¹⁰ 413 F. Supp. 453 (S.D.N.Y. 1976), *aff'd*, 550 F.2d 1303 (2d Cir. 1977).

¹¹¹ 413 F. Supp. at 467. The market maker feared the impact of *Jaffe & Co.*, 44 S.E.C. 285 (1970). See note 106 *supra*.

¹¹² 413 F. Supp. at 472.

¹¹³ *Id.* at 471.

¹¹⁴ The *Byrnes* court, by focusing on the magnitude of the offering, applied the *Bruns, Nordeman* test to determine whether the market maker participated in the distribution. See text accompanying notes 23-37 *supra*. When the focus is on the individual's actions rather than on the offering in general, the *Bruns, Nordeman* test is helpful in distinguishing the transaction from an ordinary one and to determine whether Rule 10b-6 should apply. See 413 F. Supp. at 471; text accompanying notes 32-37 *supra*.

¹¹⁵ See text accompanying notes 50-95 *supra*.

Standing

While there has been comparatively little litigation concerning private rights of action under the antimanipulative provisions of Rule 10b-6, two recent district court decisions may foreshadow an increase in interest on the standing issue.

In *Halle & Stieglitz Filor, Bullard, Inc. v. Empress International, Ltd.*,¹¹⁶ the defendant counterclaimed for violations of Rules 10b-6 and 10b-7,¹¹⁷ but the district court applied a purchaser-seller requirement to private actions under Rule 10b-6 and found that the defendant did not meet that requirement.¹¹⁸ In *Warren v. Bokum Resources Corp.*,¹¹⁹ the district court implied a private right of action under Rule 10b-13¹²⁰ in favor of persons who had tendered their securities pursuant to a tender offer by Bokum.¹²¹ Examination of both these cases in light of the recent Supreme Court decision in *Piper v. Chris-Craft Industries, Inc.*¹²² demonstrates the major issues involved in determining whether and in whose favor standing exists under the antimanipulative rules.

In *Empress*, the plaintiffs publicly offered Empress stock as underwriters and then traded actively in the stock during the distribution.¹²³ The court never reached the issue of whether Halle & Stieglitz's actions violated Rule 10b-6, but summarily dismissed Empress' claim for lack of standing.¹²⁴ The court based this determination on its findings that Empress did not purchase or sell, but only held the stock. The *Empress* court applied the purchaser-seller requirement,¹²⁵ originally applied in Rule 10b-5 private actions,¹²⁶ as a prerequisite for maintenance of a 10b-6 private action.¹²⁷ The purchaser-seller limitation requires that the plaintiff allege

¹¹⁶ 442 F. Supp. 217 (D. Del. 1977); see text accompanying notes 123-36 *infra*.

¹¹⁷ 17 C.F.R. § 240.10b-7 (1977).

¹¹⁸ 442 F. Supp. at 226-27.

¹¹⁹ 433 F. Supp. 1360 (D.N.M. 1977); see text accompanying notes 174-207 *infra*.

¹²⁰ 17 C.F.R. § 240.10b-13 (1977); see text accompanying notes 167-70 *infra*.

¹²¹ 433 F. Supp. at 1367-68.

¹²² 430 U.S. 1 (1977).

¹²³ 442 F. Supp. at 226. Halle & Stieglitz commenced a public offering of Empress stock as underwriters on May 3, 1972. All of the stock was not ultimately distributed, however, and large amounts were returned to Halle & Stieglitz. From May 3 to May 9, 1972, Halle & Stieglitz engaged in stabilization transactions in Empress stock but failed to file the reports required by Rule 10b-7. Between May 9 and October, 1972, Halle & Stieglitz participated in the distribution of Empress stock and also purchased and sold the stock. *Id.* Empress alleged Rule 10b-6 and Rule 10b-7 violations. The court did not distinguish the Rules in its discussion of the standing issue because of its analysis of their common statutory origins. See text accompanying notes 134-36 *infra*.

¹²⁴ 442 F. Supp. at 226-27.

¹²⁵ The purchaser-seller requirement was first formulated by the Second Circuit in *Birnbaum v. Newport Steel Corp.*, 193 F.2d 461 (2d Cir.), *cert. denied*, 343 U.S. 956 (1952). In *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975), the Supreme Court firmly established the purchaser-seller requirement as a limitation on the class of plaintiffs entitled to sue under Rule 10b-5. See text accompanying notes 129-35 *infra*.

¹²⁶ 17 C.F.R. § 240.10b-5 (1977); see note 125 *supra*.

¹²⁷ 422 F. Supp. at 226-27.

that he suffered the claimed injury in connection with his purchase or sale of a security.¹²³

The *Empress* court relied on the Supreme Court's decision in *Blue Chip Stamps v. Manor Drug Stores*¹²⁹ to impose the purchaser-seller limitation on persons who can sue for Rule 10b-6 violations. In *Blue Chip*, the Supreme Court posed three principal justifications for the purchaser-seller requirement. The Court relied on the longstanding judicial acceptance of the requirement,¹³⁰ the fact that the requirement conforms to the statutory language and legislative history of section 10(b) of the Securities Exchange Act of 1934,¹³¹ and the danger of vexatious litigation should the requirement be removed.¹³² The *Empress* court justified the imposition of the purchaser-seller limitation to Rule 10b-6 actions principally because of the limitation's conformity with the language and legislative history of section 10(b).¹³³ Under section 10(b), no person may use, in connection with the purchase or sale of any security, any manipulative or deceptive device in contravention of rules promulgated by the SEC.¹³⁴ Congress' failure to amend the language "in connection with the purchase or sale" in section 10(b) persuaded the *Blue Chip* Court to affirm the applicability of the purchaser-seller requirement to actions under Rule 10b-5.¹³⁵

While recognizing that the purchaser-seller requirement derived from Rule 10b-5 cases and that the Supreme Court's affirmance of that requirement was also in the context of Rule 10b-5, the *Empress* court noted that the *Blue Chip* opinion indicated that the purchaser-seller requirement applies generally to section 10(b).¹³⁶ The *Empress* court held that the purchaser-seller requirement is applicable to Rule 10b-6 because that Rule also derives its statutory authority from section 10(b).¹³⁷ Since *Empress*

¹²³ *Birnbaum v. Newport Steel Corp.*, 193 F.2d 461, 464 (2d Cir. 1952).

¹²⁹ 421 U.S. 723 (1975).

¹³⁰ The Court noted that the purchaser-seller requirement had been upheld by virtually all of the reported cases considering the limitation. *Id.* at 731-33.

¹³¹ *Id.* at 733-36. The Court emphasized that several provisions of the Securities Acts provide express remedies for nonpurchasers/sellers. *Id.* at 733-34.

¹³² *Id.* at 737-49. The Supreme Court in *Blue Chip* offered the following policy justifications for retaining the purchaser-seller requirement: (1) the potential for vexatious "strike" suits arising out of the fact that a Rule 10b-5 action may have great settlement value to a plaintiff and may thus disrupt normal business activity absent limits that allow for dismissal; (2) the possibility for abuse of discovery rules in such suits; (3) the guidance that an objectively demonstrable fact of a sale transaction affords triers of fact in Rule 10b-5 cases beyond the plaintiff's testimony as to what he would have done in the absence of the alleged fraud. *Id.*

¹³³ 442 F. Supp. at 227.

¹³⁴ 15 U.S.C. § 78j (1976).

¹³⁵ 421 U.S. at 732-33.

¹³⁶ 442 F. Supp. at 227. The *Empress* court relied on the passage in *Blue Chip* that cites Congress' failure to amend § 10(b). See 421 U.S. at 732-33. The SEC had requested Congress to amend the language of § 10(b) to bar fraud in connection with "any attempt" to purchase or sell any security. However, Congress has not amended the section which only prohibits fraud in connection with an actual purchase or sale. 442 F. Supp. at 227, citing 421 U.S. at 732-33.

¹³⁷ 442 F. Supp. at 227.

International held but did not purchase or sell their shares, the court found that the company lacked standing to claim damages for Rule 10b-6 violations.¹³⁸

In *Piper v. Chris-Craft Industries, Inc.*,¹³⁹ the Supreme Court strongly suggested that a purchaser-seller limitation is applicable to potential plaintiffs under Rule 10b-6 private actions. Because of the posture of the case, the Supreme Court did not fully resolve the standing issue¹⁴⁰ and most of the analysis presented is either dicta or based on unchallenged SEC interpretations. However, the Court's discussion of Chris-Craft's standing to sue Bangor Punta Corp. for alleged violations of Rule 10b-6 is still instructive.

Both Bangor Punta and Chris-Craft sought control of Piper Aircraft Co. by use of competing tender offers. After Bangor Punta was victorious, Chris-Craft sued Bangor Punta for alleged violations of the securities laws.¹⁴¹ The Second Circuit held that Chris-Craft had standing to sue for damages resulting from Rule 10b-6 violations,¹⁴² but the Supreme Court reversed, holding instead that Chris-Craft's complaint was beyond the concerns of Rule 10b-6.¹⁴³

As one of its reasons for not fully resolving the Rule 10b-6 standing issue, the Court in *Piper* stated that the Court of Appeals below did not have the benefit of the *Blue Chip* decision when it decided the case.¹⁴⁴ This

¹³⁸ *Id.* The *Empress* court also cited *Weitzen v. Kearns*, 271 F. Supp. 616, 623 (S.D.N.Y. 1967), in which the district court held that Rule 10b-6 was designed to protect purchasers of securities. The court in *Weitzen* denied standing to stockholders of a corporation in a suit against the directors because the stockholders had not purchased the distributed securities. *Id.*

¹³⁹ 430 U.S. 1 (1977).

¹⁴⁰ *Id.* at 44-45.

¹⁴¹ For a complete history of the contest for corporate control and the eight years of protracted litigation in the *Piper* case, see *id.* at 4-21.

¹⁴² 480 F.2d 341 (2d Cir. 1973), *rev'd*, 430 U.S. 1 (1977). The Second Circuit held that Chris-Craft had standing to sue even though Chris-Craft had not purchased the manipulated stock of Bangor Punta Corp. 480 F.2d at 379. Chris-Craft did not complain that it was misled or defrauded by Bangor Punta's illegal purchases, but rather that these purchases misled Piper shareholders into accepting the Bangor Punta exchange offer and that Chris-Craft, as a rival for Piper stock, was thereby injured. *Id.* at 378. The Supreme Court held that such a complaint was outside the concern of Rule 10b-6 and thus denied Chris-Craft standing. 430 U.S. at 46; see text accompanying notes 150-52 *infra*.

The Second Circuit did not apply the purchaser-seller limitation to Rule 10b-6 because no "purchase or sale" language is found in Rule 10b-6. The Second Circuit reasoned that the requirement evolved from Rule 10b-5's reference to purchase or sale and thus was applicable only to Rule 10b-5 private actions. 480 F.2d at 378. The Second Circuit also took a broad view of the purpose of Rule 10b-6 to support its holding. Rather than limiting Rule 10b-6's purpose to protection of purchasers, the court found that the Rule is designed to promote fairness in contests for corporate control. *Id.* at 378. Chris-Craft was entitled to sue for violations of Rule 10b-6 that infringed its right to a fair contest. *Id.* at 378-79. The Supreme Court rejected this broad interpretation, holding instead that Rule 10b-6 protects only purchasers and sellers. 430 U.S. at 45-46; see text accompanying notes 149-51 *infra*.

¹⁴³ 430 U.S. at 45-46.

¹⁴⁴ *Id.* at 44.

reference to *Blue Chip* strongly suggests that the Supreme Court recognized the applicability of the purchaser-seller requirement to Rule 10b-6 private actions.¹⁴⁵ Such a position also can be inferred from the Court's discussion of the statutory origin of Rule 10b-6 in *Piper*. The Court noted the "close relationship" between section 9 of the '34 Act¹⁴⁶ and Rule 10b-6, and found that section 9 provided an express cause of action in favor of any person who purchases or sells any security at a price affected by unlawful market activity.¹⁴⁷ The language of section 9 focuses on the amount actually paid by an investor for stock affected by manipulation.¹⁴⁸ Because Chris-Craft complained of lost opportunity for control of Piper, and not that it paid an unfair price, Chris-Craft's complaint was "beyond the bounds of the specific concern of Rule 10b-6."¹⁴⁹ By denying standing to Chris-Craft on this basis,¹⁵⁰ the Court implicitly recognized that relief would be available to an investor who asserts that the price paid in his transaction was affected by Rule 10b-6 violations. Such emphasis on price necessarily requires that the plaintiff have purchased or sold the affected security and thus implies a purchaser-seller limitation on Rule 10b-6 plaintiffs.

Bangor Punta's purchases of Piper stock during the exchange offer were

¹⁴⁵ Since *Blue Chip* sustained the purchaser-seller requirement for private actions under Rule 10b-5, the *Piper* Court's reference to *Blue Chip* indicates that it viewed the reasoning in *Blue Chip* as applicable to Rule 10b-6.

¹⁴⁶ 15 U.S.C. § 78i (1976).

¹⁴⁷ 430 U.S. at 46.

¹⁴⁸ *Id.* The Court's reasoning that § 9 focuses on the price of the affected security suggests that damages allowed for Rule 10b-6 private actions may be limited to the pecuniary loss suffered as a result of the violations. The Court did not discuss the issue of what the proper measure of damages would be in a successful action under Rule 10b-6. The Court's emphasis on the price paid, however, would seem to favor recovery of the difference between the fair market value of the securities at the time of the violation and the actual consideration paid. This out-of-pocket theory is the most common measure of damages under Rule 10b-6. *Ross v. Licht*, 263 F. Supp. 395, 410 (S.D.N.Y. 1967). Another possible measure of damages is the difference between what the seller received and the fair value of what he would have received had there been no fraudulent or deceptive conduct. *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 155 (1972). See generally *Jacobs, The Measure of Damages Under Rule 10b-5*, 65 *Geo. L. Rev.* 1093 (1977).

¹⁴⁹ 430 U.S. at 45.

¹⁵⁰ By denying Chris-Craft standing to sue because its complaint was concerned with lost opportunity for control, the Supreme Court rejected the Second Circuit's position that Rule 10b-6's purpose includes assuring fairness in corporate control contests. The Second Circuit cited a SEC release as authority for its view of the purpose of Rule 10b-6 in a tender offer context. SEC Securities Exchange Act Release No. 8595 (May 5, 1969) [1969-70 Transfer Binder] *FED. SEC. L. REP. (CCH)* ¶ 77,706. The "fairness" referred to in that release probably meant fairness to the tendering shareholders, insuring that the offeror would not pay a different consideration to some tendering shareholders than others. See SEC Securities Exchange Act Release No. 8712 (Oct. 8, 1969) [1969-70 Transfer Binder] *FED. SEC. L. REP. (CCH)* ¶ 77,745; SEC Securities Exchange Act Release No. 9395 (Nov. 24, 1971) [1970-1971 Transfer Binder] *FED. SEC. L. REP. (CCH)* ¶ 78,417. Thus, the Supreme Court's narrower view of Rule 10b-6's purpose appears more sound than the Second Circuit's, especially since § 14(e) of the Williams Act was designed to regulate tender offers. 430 U.S. at 22-42; see 15 U.S.C. § 78(n)(e) (1970).

regulated by Rule 10b-6 when the alleged violations occurred. Besides prohibiting participants in a distribution from purchasing any distributed stock, Rule 10b-6 also prohibits the purchase of "rights to purchase" such stock.¹⁵¹ The position of the SEC is that the stock of the target company in an exchange offer constitutes rights to purchase the acquiring company's stock and thus purchases of target-stock outside the exchange offer are prohibited.¹⁵² Rule 10b-13¹⁵³ now expressly covers tender offers and exchange offers, and the SEC maintains that the Rule, as applied to exchange offers, is a codification of interpretations of Rule 10b-6 as it applied to exchange offers.¹⁵⁴ Thus, Rule 10b-13 prohibits any person who makes a tender offer or exchange offer from purchasing either securities of the target company or of the acquiring company.¹⁵⁵ The central purpose behind Rule 10b-13's codification of the SEC's interpretation of Rule 10b-6 appears to be to insure fair treatment of all stockholders of the target company.¹⁵⁶ Because of this close relationship between Rules 10b-6 and 10b-13, any analysis of standing under Rule 10b-13 is particularly relevant to Rule 10b-6 private actions.

The right of private parties to sue for violations of Rule 10b-13 was analyzed fully in *Warren v. Bokum Resources Corp.*¹⁵⁷ In *Warren*, Bokum Resources Corp. sent a tender offer and exchange offer to the plaintiffs. After the plaintiffs tendered their shares pursuant to the offers, they alleged violations of Rule 10b-13.¹⁵⁸ The defendants moved to dismiss the Rule 10b-13 claim on the ground that no private action may be implied under the Rule. The district court denied the motion, holding that a private remedy was proper¹⁵⁹ for reasons similar to those advanced by the Supreme Court in other private action cases.¹⁶⁰ The *Warren* decision also parallels the Supreme Court's approach to Rule 10b-6 standing issues in *Piper*.¹⁶¹

The court in *Warren* applied the *Cort v. Ash*¹⁶² test to determine

¹⁵¹ 17 C.F.R. § 240.10b-6(a)(2) (1977).

¹⁵² SEC Securities Exchange Act Release No. 8595 (May 5, 1969) [1969-70 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 77,706.

¹⁵³ 17 C.F.R. § 240.10b-13 (1977).

¹⁵⁴ SEC Securities Exchange Act Release No. 8595 (May 5, 1969) [1969-70 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 77,706. *But see* Lowenfels, *Rule 10b-13, Rule 10b-6 And Purchases of Target Company Securities During An Exchange Offer*, 69 COLUM. L. REV. 1392, (1969) [hereinafter cited as Lowenfels].

¹⁵⁵ 17 C.F.R. § 240.10b-13 (1977).

¹⁵⁶ Certain substantial holders of target stock are prevented from receiving greater consideration for their shares than lesser stockholders receive. Lowenfels, *supra* note 154, at 1395.

¹⁵⁷ 433 F. Supp. 1360 (D.N.M. 1977).

¹⁵⁸ *Id.* at 1363.

¹⁵⁹ *Id.* at 1366-67.

¹⁶⁰ *See, e.g., Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1 (1977); *National R.R. Passenger Corp. v. National Ass'n of R.R. Passengers*, 414 U.S. 453 (1974).

¹⁶¹ 430 U.S. at 42-46; *see* text accompanying notes 139-156 *supra*.

¹⁶² 422 U.S. 66 (1975). In *Cort v. Ash*, the plaintiffs alleged that the directors of Bethlehem Steel Corp. had violated a federal election campaign contribution law. The plaintiff-shareholders sought damages on behalf of the corporation, contending that a derivative cause of action for shareholders could be implied under the relevant statute. The Supreme Court

whether a private right of action could be implied from Rule 10b-13. In *Cort v. Ash*, the Supreme Court held that in order to determine if a federal statute implies a private cause of action, a court must decide whether the plaintiff is a member of the class for whose especial benefit the statute was enacted,¹⁶³ whether the statute indicates any explicit or implicit legislative intent either to deny or create a private action,¹⁶⁴ whether an implied cause of action would be consistent with the underlying purposes of the legislative scheme,¹⁶⁵ and whether the cause of action is one traditionally relegated to state law.¹⁶⁶

The origin and purpose of the statute must be examined to discover whether the plaintiff is a member of the class for whose especial benefit the statute was enacted.¹⁶⁷ Relying on an SEC release that accompanied the adoption of Rule 10b-13,¹⁶⁸ the *Warren* court found that the Rule was enacted expressly to protect investors and to safeguard the interests of persons who have tendered their securities in response to a tender or ex-

held that such a remedy would be improper because the statute showed no concern for individuals in the plaintiff's position, *id.* at 78-83, the legislative history suggested no congressional intent to vest in shareholders a federal right to damages, *id.* at 82-84, a private remedy would not further the purpose of the statute, *id.* at 84, and the cause of action was one traditionally relegated to state law. *Id.* at 84-85. Although *Cort v. Ash* concerned the implication of a private right from a criminal statute, the Supreme Court and lower federal courts have held that the analysis is applicable to civil statutes as well. See *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. at 37-42; *Lloyd v. Regional Transp. Auth.*, 548 F.2d 1277 (7th Cir. 1977); *Mason v. Belieu*, 543 F.2d 215, 221 (D.C. Cir. 1976); *Michigan Dist. Council No. 77 of AFSCME v. City of Detroit*, 436 F. Supp. 858, 861-63 (E.D. Mich. 1977); *Sullivan v. Chase Inv. Serv.*, 434 F. Supp. 171, 179-84 (N.D. Cal. 1977). See generally *McMahon & Rodos, Judicial Implication of Private Causes of Action: Reappraisal and Retrenchment*, 80 *DICK L. REV.* 167 (1976); *Mowe, Federal Statutes and Implied Private Actions*, 55 *ORE. L. REV.* 3 (1976); *Comment, Implying Private Causes of Action From Federal Statutes: Amtrak and Cort Apply the Brakes*, 17 *B.C. INDUS. & COM. L. REV.* 53 (1975) [hereinafter cited as *Implying Private Causes of Action*].

¹⁶³ 422 U.S. at 78.

¹⁶⁴ *Id.* The distinction between whether the plaintiff is a member of the class for whose especial benefit the statute was enacted and whether there is any legislative intent to create or deny a remedy is difficult to perceive. In fact, these two tests essentially may be alternative ways for the plaintiff to show that a private cause of action would be consistent with legislative intent. *Implying Private Causes of Action*, *supra* note 162, at 62-63; see text accompanying notes 176-79 *infra*.

¹⁶⁵ The reason usually advanced to support the third part of the *Cort v. Ash* test is that courts should pay deference to legislative intent and not engage in "judicial legislation." See *Chavez v. Freshpict Foods, Inc.*, 456 F.2d 890, 895 (10th Cir.), *cert. denied*, 409 U.S. 1042 (1972); Note, 77 *HARV. L. REV.* 285, 291 (1963). Further, if a statutory scheme of enforcement is ineffective to achieve the statute's purpose, implied private rights of action are desirable as a matter of policy. *J. I. Case Co. v. Borak*, 377 U.S. 426, 433 (1964); see Note, *The Implication of a Private Cause of Action Under Title III of the Consumer Credit Protection Act*, 47 *S. CAL. L. REV.* 383, 411 (1974).

¹⁶⁶ The fourth component of the *Cort v. Ash* test illustrates the Supreme Court's concern for the interests of federalism. 422 U.S. at 78.

¹⁶⁷ *Id.*

¹⁶⁸ SEC Securities Exchange Release No. 8712 (Oct. 8, 1969) [1969-70 Transfer Binder] *FED. SEC. L. REP.* (CCH) ¶ 77,745.

change offer.¹⁶⁹ The plaintiffs in *Warren* were investors who had so tendered their securities. Thus, the court concluded that they were clearly in the class for whose "especial benefit" Rule 10b-13 was adopted.¹⁷⁰

The second inquiry necessary under the *Cort v. Ash* test concerns whether any implicit or explicit legislative intent to create or deny a private remedy exists.¹⁷¹ The *Warren* court noted that while Rule 10b-13 does not explicitly create a private remedy, the SEC gave no indication that it did not intend to create such a right of recovery.¹⁷² The court then relied on language in *Cort v. Ash* stating that in situations where a statute clearly grants rights to a certain class of persons, a showing of express intent to create a private cause of action is unnecessary.¹⁷³ Such reasoning must assume that the creation of a class of rights for certain persons automatically implies the requisite intent.¹⁷⁴ Since Rule 10b-13 gives persons who tender their securities the right to be assured that the offeror will not purchase on different terms elsewhere, the *Warren* court concluded that a demonstration of intent to create a remedy was unnecessary.¹⁷⁵

This analysis by the district court merges the second inquiry of *Cort v. Ash* into the first inquiry when no legislative intent to create or deny a remedy can be demonstrated.¹⁷⁶ Determining whether the relevant statute has granted a class of persons certain rights necessitates essentially the same inquiry as determining whether the statute was enacted for the benefit of an "especial class."¹⁷⁷ The second inquiry would only become relevant if an "especial class" was found but the statute evidenced an intent to deny a private cause of action. Such a negative intent would control.¹⁷⁸ Unless an "especial class" and a "clear grant of certain rights" can be differentiated, the first and second tests are alternative ways for a plaintiff to show that the implication of a private right in his favor would be consistent with legislative intent.¹⁷⁹

The *Warren* court buttressed its finding that such a right would be consistent with the legislative intent by drawing a parallel between Rule 10b-13 and section 14(a) of the Securities Exchange Act of 1934.¹⁸⁰ Because section 14(a) has among its chief purposes the "protection of investors,"

¹⁶⁹ 433 F. Supp. at 1366.

¹⁷⁰ *Id.*, citing *Cort v. Ash*, 422 U.S. at 78.

¹⁷¹ 422 U.S. at 78.

¹⁷² 433 F. Supp. at 1366-67.

¹⁷³ *Id.* at 1367.

¹⁷⁴ The assumption that the creation of a class of rights for certain persons automatically implies a private right, however, would be defeated if an explicit intent to deny such a private right is shown. 422 U.S. at 82.

¹⁷⁵ 433 F. Supp. at 1367.

¹⁷⁶ See text accompanying notes 163-164 *infra*.

¹⁷⁷ *Implying Private Causes of Action*, *supra* note 162, at 62.

¹⁷⁸ 422 U.S. at 82. If the plaintiff is a member of the protected class and the statute already provides private remedies, the remedies created by the statute are exclusive. *National R.R. Passenger Corp. v. National Ass'n of R.R. Passengers*, 414 U.S. 453, 458 (1974).

¹⁷⁹ See *Implying Private Causes of Action*, *supra* note 162, at 62.

¹⁸⁰ 15 U.S.C. § 78n(e) (1976).

the Supreme Court implied a right to the availability of a private right of judicial relief.¹⁸¹ The *Warren* court concluded that since Rule 10b-13 was also enacted for the protection of investors, judicial relief was similarly appropriate.¹⁸²

The third relevant factor under the *Cort v. Ash* analysis is whether an implied remedy would be consistent with the underlying purposes of the statute.¹⁸³ Reasoning that the threat of damages against a tender offeror would provide additional protection for the investor, that any damages awarded would benefit those investors intended to be protected, and that the remedy would be available only to the protected class,¹⁸⁴ the *Warren* court concluded that allowing a private right would further the purpose of Rule 10b-13.¹⁸⁵ Such reasoning appears sound when compared to the Supreme Court's treatment of this third factor in *Piper*.¹⁸⁶

The final inquiry under the *Cort v. Ash* test is whether the cause of action is one "traditionally relegated to state law."¹⁸⁷ The *Warren* court concluded that resort to state law would not protect the interests Rule 10b-13 was intended to safeguard,¹⁸⁸ noting the comprehensive federal legislation in this area and the major role played the SEC in securities regulation.¹⁸⁹ Since no comparative state statutory or common law prohibits the purchase of target securities outside a tender or exchange offer, no state

¹⁸¹ *J. I. Case Co. v. Borak*, 377 U.S. 426, 432 (1964).

¹⁸² 433 F. Supp. at 1367. An analysis similar to that applied by the *Warren* court with respect to Rule 10b-13 would also be appropriate to determine whether a private right is implied in Rule 10b-6. The purpose of Rule 10b-6 is to eradicate manipulation that would create an unjustifiable impression of market activity and consequent higher prices. *SEC v. Scott Taylor & Co.*, 183 F. Supp. 904, 907 (S.D.N.Y. 1959). Thus, the Rule protects purchasers of distributed securities from buying at artificially high prices. *Weitzen v. Kearns*, 271 F. Supp. 616, 623 (S.D.N.Y. 1967); *Miller v. Steinbach*, 268 F. Supp. 255, 280 (S.D.N.Y. 1967). Rule 10b-6 can be viewed as protecting purchasers (the especial class) and assuring these purchasers that the price paid for a distributed security is not the product of prohibited market manipulations. See *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. at 45-46; *Weitzen v. Kearns*, 271 F. Supp. at 623; *Miller v. Steinbach*, 268 F. Supp. at 280.

¹⁸³ 422 U.S. at 78.

¹⁸⁴ The *Warren* court's enumeration of factors that demonstrate the consistency of an implied right of action with Rule 10b-13's purposes are relevant to a similar inquiry under Rule 10b-6. The threat that damages might be assessed against the participant in a distribution would provide additional protection for investors, a major purpose of the statute. See note 138 *supra*. If a purchaser-seller limitation is applied to Rule 10b-6 actions as suggested by *Empress* and *Piper*, see text accompanying notes 122-148 *supra*, then the remedy would be available only to the protected class and any damages awarded would benefit those intended to be protected. *Cf. Piper v. Chris-Craft Indus., Inc.*, 422 U.S. at 39 (remedy for defeated tender offeror inappropriate because damage award would not benefit protected class nor would remedy be available to persons within protected class).

¹⁸⁵ 433 F. Supp. at 1367.

¹⁸⁶ 422 U.S. at 39. The Supreme Court in *Piper* held that a private remedy for defeated tender offerors like *Chris-Craft* would not be consistent with the *Williams Act's* purpose of protecting target shareholders. *Id.*

¹⁸⁷ 422 U.S. at 78.

¹⁸⁸ 433 F. Supp. at 1367.

¹⁸⁹ *Id.*