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## Administrative Law - Powers of Agencies - Right of Registrant to Withdraw Registration Statement Filed with the Securities and Exchange Commission

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ADMINISTRATIVE LAW—POWERS OF AGENCIES—RIGHT OF REGISTRANT TO WITHDRAW REGISTRATION STATEMENT FILED WITH THE SECURITIES AND EXCHANGE COMMISSION—Petitioner filed a registration statement with the Securities and Exchange Commission for an issue of corporate stock. Shares of the same class as those being registered were widely held by members of the public. Petitioner repeatedly amended the statement,<sup>1</sup> so that it had not yet become effective nearly three months after the initial filing. At this time, petitioner sought to withdraw its registration statement. The commission denied the application for withdrawal, and after a hearing, issued a stop order, preventing the statement from becoming effective and indicating its unreliability.<sup>2</sup> On petition for review

<sup>1</sup> 17 C.F.R. §230.473 (1949; Supp. 1959).

<sup>2</sup> 48 Stat. 79 (1933), 15 U.S.C. (1958) §77h (d). Both a stop order and withdrawal prior to the effective date prevent the registration statement from becoming effective and make further sales and distribution activities through the instruments of interstate commerce or the mails unlawful. 48 Stat. 77 (1933), 15 U.S.C. (1958) §77e. However, there are significant differences between the effects of a stop order and a withdrawal. See note 5 *infra*.

of the order, *held*, affirmed. Where members of the public hold shares of the same class of security covered by a registration statement filed with the SEC, the commission may deny permission to withdraw the statement before the effective date and issue a stop order prohibiting further sales activities by use of the mails or in interstate commerce. *Columbia General Investment Corporation v. Securities and Exchange Commission*, (5th Cir. 1959) 265 F. (2d) 559.

In 1936, the United States Supreme Court, in *Jones v. Securities and Exchange Commission*,<sup>3</sup> held that a registrant had an absolute right, unfettered by administrative discretion, to retract a registration statement prior to its effective date, at least where no securities of the class seeking to be registered were publicly outstanding.<sup>4</sup> This decision gave the registrant an absolute right to terminate the commission's jurisdiction to investigate in order to determine whether the registrant willfully had filed a false or incomplete statement, making him amenable to prosecution.<sup>5</sup> The lower federal courts early limited *Jones* to cases where withdrawal was sought prior to the effective date.<sup>6</sup> The court in the principal case distinguished *Jones* on the ground that in that case shares of the same class as those being registered were not publicly outstanding at the time the registration statement was filed.<sup>7</sup> Although the *Jones* case may have been properly distinguished to avoid the application of its rule, in the light of congressional action subsequent to that decision the general soundness of the distinction, and thus, the continued vitality of *Jones*, must be questioned. The Securities Act of 1933 originally prohibited the offering for sale of securities filed for registration until the statement's effective date.<sup>8</sup> In 1954, Congress amended the act so as to permit registrants to make offers for sale and to solicit offers to buy<sup>9</sup> during the period after filing

<sup>3</sup> 298 U.S. 1 (1936).

<sup>4</sup> Prior to the *Jones* decision, the commission had discretion, under rule 960, now 17 C.F.R. §230.477 (1949; Supp. 1959), to refuse withdrawal of a registration statement, either before or after its effective date, in any case where it had reason to suspect that the filed statement included a material misstatement or omission. Under such rule there must be a finding by the commission that the withdrawal is "consistent with the public interest and the protection of investors."

<sup>5</sup> See *Jones v. SEC*, 298 U.S. 1 at 23 (1936). Although withdrawal terminates the commission's jurisdiction to investigate further concerning the registration statement, issuance of a stop order would have no such effect. In addition, under rule 252(c) of the S.E.C.'s Regulation A, 17 C.F.R. §230.252(c) (1949; Supp. 1959), adopted subsequent to *Jones*, the issuance of a stop order bars the registrant's use of the \$300,000 general exemption from registration requirements for five years. A registrant armed with an absolute right of withdrawal, however, obviously could avoid the impact of this rule.

<sup>6</sup> *Oklahoma-Texas Trust v. SEC*, (10th Cir. 1939) 100 F. (2d) 888; *Resources Corporation International v. SEC*, (D.C. Cir. 1939) 103 F. (2d) 929; *SEC v. Hoover*, (N.D. Ill. 1938) 25 F. Supp. 484. See, generally, Loss, *SECURITIES REGULATION* 202 (1951). See also 84 *UNIV. PA. L. REV.* 1019 (1936).

<sup>7</sup> Principal case at 562.

<sup>8</sup> 48 Stat. 77 (1933).

<sup>9</sup> In practice, the general sales promotion, just short of actual sales, may be extensive. See, generally, CHOKA, *AN INTRODUCTION TO SECURITIES REGULATION* 17 (1958).

but before the registration becomes effective.<sup>10</sup> Thus, the 1954 amendments in conjunction with an absolute right of withdrawal would allow a registrant a minimum of nineteen days (allowing one day for withdrawal) to capitalize upon the phantasm of legality afforded him by filing the registration statement. Delaying amendments, by which he may postpone the statement's effective date, license additional time for exploitation. Under these circumstances, it seems clear that, regardless of whether or not shares of the same class are held by members of the public at the time of filing, the possible mischief resulting from an absolute right of withdrawal is equally violative of the purpose of the Securities Act of 1933.<sup>11</sup> In the former case, a profiteering registrant might buy some of the outstanding shares, file a statement and distribute a fraudulently favorable prospectus, and then sell his shares at a price reflecting investor optimism generated by the false representations. To avoid an investigation which might uncover his fraud, the registrant need only withdraw his statement. Similarly, even if there were no shares outstanding, a registrant might excite potential investor interest by a fraudulently optimistic prospectus, then withdraw and consummate the sales without utilization of interstate commerce or the mails, thus avoiding the reach of the federal act. Hence, the distinction made in the principal case to avoid application of the *Jones* rule, although proper for that purpose, appears to be generally unsound. In either case, an unscrupulous registrant might file and capitalize upon a false or incomplete prospectus with apparent immunity from prosecution, where an absolute right of withdrawal exists. In a recent case,<sup>12</sup> the Securities and Exchange Commission has faced the problem directly, rather than searching for questionable distinctions,<sup>13</sup> and found the effects of the 1954 amendments<sup>14</sup> sufficient to prevent absolute withdrawal on facts substantially the same as *Jones*. The position taken by the commission is certainly worthy of support in the courts.

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<sup>10</sup> 68 Stat. 684 (1954), 15 U.S.C. (1958) §77e (a), (c).

<sup>11</sup> The design of the act and of the provision requiring registration is to protect the investing public against imposition and fraud in the sale of securities by requiring the full and fair disclosure of information concerning the character of the security before its sale in interstate commerce or through the mails. See *Creswell-Keith, Inc. v. Willingham*, (D.C. Ark. 1958) 160 F. Supp. 735; *Wilko v. Swan*, 346 U.S. 427 (1953); *SEC v. Ralston Purina Co.*, 346 U.S. 119 (1953).

<sup>12</sup> In the Matter of *Comico Corp.*, Securities Act (1933) Release No. 4050 (1959), decided just three weeks after the principal case.

<sup>13</sup> Although the existence of an option to purchase some of registrant's shares might have raised the question of whether a public interest was involved, the commission determined the issue of absolute right of withdrawal without regard to the option.

<sup>14</sup> In regard to the 1954 amendments, the commission stated: ". . . we think the change in the effect of the filing of a registration statement which was made by the 1954 amendment to Section 5 of the Act creates a public interest upon filing which precludes an absolute right of withdrawal. . . ." See note, 45 VA. L. REV. 1061 (1959).