petition system, the most widely used means,[53] establishes a standard of public support to be shown as a prerequisite to ballot placement rather than a pecuniary standard. Such a standard is more directly related to restricting the ballot to serious candidates and is more equally applicable to all citizens whatever their status. Requiring a showing of support will restrict the ballot and insure seriousness both on the part of the candidate and on the part of the voters who give such support.

Applying the principle that a state's interest in employing a particular means of achieving valid state interests will not be necessary or compelling if there is available a viable alternative to achieve substantially the same result and place a lesser burden upon fundamental rights,[54] it is clear that a fee system must yield to alternative means of access. This approach to the reconciliation of filing fees and fundamental rights is practical, logical and consistent with current case development. It should provide adequate guidelines for further development in the area.[55]

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[53] *See* note 40 *supra.*

[54] *See* Boddie v. Connecticut, 401 U.S. 371, 381-82 (1971); Wormuth & Mirkin, *The Doctrine of the Reasonable Alternative,* 9 UTAH L. REV. 254 (1964); *Developments in the Law—Equal Protection,* 82 HARV. L. REV. 1065, 1102 & n. 154 (1969); Note, *Discriminations Against the Poor and the Fourteenth Amendment,* 81 HARV. L. REV. 435, 442 (1967).

[55] For an application of *Carter* principles see Jenness v. Miller, 346 F. Supp. 1060 (S.D. Fla. 1972).

SECURITIES—AN ACQUIRING CORPORATION'S LIABILITY FOR MISLEADING STATEMENTS CONTAINED IN THE ACQUIRED CORPORATION'S PROXY STATEMENT: WILL S.E.C. RULE 145 ABANDON THE "CONTROL" TEST OF BEATTY V. BRIGHT?—*Beatty v. Bright* (S.D. Iowa 1972).

An acquiring corporation has hitherto not been liable for misleading statements contained in the acquired corporation's proxy statement in a stock-for-assets reorganization under most circumstances.[1] However, with the adoption of SEC Rule 145,[2] an acquiring corporation will be liable for such misstatements even though it has no effective control over the acquired corporation.

In consummating a merger of Gains Guaranty Corporation (hereinafter Gains) and Life Investors, Inc. (hereinafter Life), the management of Gains sent proxy solicitation materials to its shareholders to secure approval of the transfer of Gains' assets to Life in return for stock in Life. While these and other instruments were being prepared, there were two shareholders' derivative suits pending against Gains' officers and directors. In a series of letters between officers, accountants, and attorneys for both corporations, Gains informed Life of the details of the pending litigation. At all times Life was kept informed as to the development of the proxy materials. The reorganization agreement, in essence, provided that Gains warranted that the consummation of the transfer would not violate any law, that the agreement would be validly authorized by Gains' corporate action, and that the instruments furnished by Gains would not contain any material misstatements or omissions. The obligations of Life were conditioned upon the truthfulness of Gains' representations. In addition, the merger agreement and other instruments were subject to the approval of Life's counsel "as to legal form, content, and sufficiency." The proxy statements sent to the Gains shareholders, however, failed to disclose the nature and extent of the two pending derivative suits. Plaintiffs contended that, as a matter of law, the approval control held by Life was sufficient to render it liable for the misleading proxy statement prepared and sent by Gains. In denying plaintiffs' motion for summary judgment against Life, the United States District Court, Southern District of Iowa, *held, inter alia,* that the contract provision and Life's activities under it did not establish such control over the Gains' proxy statement as to render Life liable for misleading statements contained therein. *Beatty v. Bright,* 345 F. Supp. 1188 (S.D. Iowa 1972).

In *Beatty*, the degree of control of the acquiring corporation over the acquired corporation was a significant factor in determining the liabilities for misstatements or omissions in proxy statements prepared by the acquired corporation.[3] However, in light of recent developments in the area of securities

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1 Beatty v. Bright, 345 F. Supp. 1188 (S.D. Iowa 1972).
2 SEC Securities Act Release No. 5316 (October 6, 1972).
3 345 F. Supp. 1188, 1192 (S.D. Iowa 1972).

regulation, "control" will not be relevant in determining such liabilities. It is likely that the acquiring corporation will, in the future, be held liable for the defective proxy statements in transactions similar to the one in *Beatty*.

The issuance of securities of one corporation in consideration of the transfer of assets of the acquired corporation is one of a number of rather common merger techniques.[4] Section 5 of the Securities Act of 1933[5] (hereinafter the Act), requires the registration of securities sold or offered for sale through the use of the instruments of interstate commerce or the mails. It also requires the accompanying prospectus to conform to the strict requirements of section 10[6] for disclosure purposes. However, by employing the stock-for-assets merger technique it has been possible for an enterprising, acquisition-bent enterprise to issue securities in significant volume (possibly creating a public market therefor) without registering the issued securities with the United States Securities and Exchange Commission (hereinafter the Commission).[7] This situation was made possible under SEC Rule 133[8] which formerly provided that, solely for the purpose of section 5, there is no "sale," "offer to sell," or "offer for sale" in an issuance of securities of one corporation to another in consideration of the transfer of assets of the acquired corporation. Absent such "sale," there was no violation of section 5 of the Act even though the acquiring corporation's securities thus came into the hands of a bevy of public investors new to the acquiring corporation.[9]

The rationale behind Rule 133 was that the decision to take the shares of the acquiring corporation as a substitute for the asset values of the acquired corporation constituted corporate action of the acquired corporation rather than actions by individual shareholders of the acquired corporation.[10] It was felt that under such circumstances there was no mutual assent between the acquiring corporation and the individual shareholder of the acquired corporation. Were there a bargain between the acquiring corporation and the individual

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4 *See, e.g.*, PRACTISING LAW INSTITUTE, WHEN CORPORATIONS GO PUBLIC 27 (C. Israels & G. Duff, Jr. ed. 1962).

5 15 U.S.C. § 77e (1970). The Securities Act of 1933 itself is set forth in 15 U.S.C. §§ 77a-77aa (1970).

6 15 U.S.C. § 77j (1970).

7 *See* 1 L. LOSS, SECURITIES REGULATION 522 (2d ed. 1961) [hereinafter cited as Loss].

8 17 C.F.R. § 230.133 (1972), which in pertinent part reads:

> (a) For purposes only of section 5 of the Act, no "sale," "offer to sell," or "offer for sale" shall be deemed to be involved so far as the stockholders of a corporation are concerned where . . . there is submitted to the vote of such stockholders a plan or agreement for a statutory merger or consolidation or reclassification of securities, or a proposal for the transfer of assets of such corporation to another person in consideration of the issuance of securities of such other person . . . .

9 Sargent, *A Review of the "No-Sale" Theory of Rule 133*, 13 BUS. LAW. 78 (1957) [hereinafter cited as Sargent].

10 *See generally* Loss, *supra* note 7, at 521; Orrick, *Registration Problems Under the Federal Securities Act—Resales Following Rule 133 and Exchange Transactions*, 10 HASTINGS L.J. 1, 10-11 (1958) [hereinafter cited as Orrick, *Registration Problems*]; Purcell, *A Consideration of the No-Sale Theory Under the Securities Act of 1933*, 24 BROOKLYN L. REV. 254, 256 (1958) [hereinafter cited as Purcell].

shareholders of the acquired corporation, a contractual agreement necessary for a "sale" might be indicated.[11] This rationale has been attacked on the ground that the consent of individual shareholders is the basis of corporate action and without such consent the corporation cannot act. Although it is, in a sense, a "class" action, each individual shareholder has a voice in that action.[12]

In a stock-for-assets transaction there is a disposition of the acquiring corporation's securities to the acquired corporation. A distribution of the acquiring corporation's securities to the shareholders of the acquired corporation usually follows. Undoubtedly such assets represent value to the acquiring corporation. Therefore, the rule seemed to conflict with the definitions of "sale" and "offers to sell" in section 2(3)[13] which include dispositions or offers to dispose of securities for value.

In addition, Rule 133 seemed to conflict with the very section to which it applied. The purpose of section 5 is to protect public investors by requiring registration and disclosure of pertinent information concerning the parties involved in the transaction.[14] By allowing transactions to go unregistered, "[t]he 'no-sale' theory as a practical matter, vitiates this very purpose and the means provided by Congress to accomplish its objectives because it calls for nondisclosure."[15]

The shortcomings of Rule 133 did not go unnoticed.[16] The Commission proposed its recision in 1956,[17] but in the face of stiff opposition,[18] it deferred any further action on the proposal.[19] After several court decisions determined that the resale of securities acquired in a "no-sale" transaction, previously unregistered because of Rule 133, nevertheless required registration upon resale under certain circumstances,[20] the Commission announced an

[11] Orrick, *Registration Problems, supra* note 10, at 11; Orrick, *Some Interpretative Problems Respecting Registration Requirements Under the Securities Act,* 13 Bus. Law. 369, 376-77 (1958) [hereinafter cited as Orrick, *Some Interpretative Problems*]; Comment, *Recent Developments in the No-Sale Theory Under the Securities Act of 1933: Proposed Revision of Rule 133,* 47 Calif. L. Rev. 112, 113 (1959) [hereinafter cited as *Recent Developments*].

[12] *See* Sargent, *supra* note 9, at 88; *Recent Developments, supra* note 11, at 113-15.

[13] 15 U.S.C. § 77b(3) (1970). *See* Sargent, *supra* note 9, at 83; Comment, *Rule 133 and the No-Sale Theory: Interpretation or Legislation?,* 13 J. Pub. L. 520, 528 (1964) [hereinafter cited as *Rule 133 and the No-Sale Theory*].

[14] S.E.C. v. North Am. Research & Dev. Corp., 280 F. Supp. 106, 121 (S.D.N.Y. 1968), *aff'd in part, vacated in part on other grounds,* 424 F.2d 63 (2d Cir. 1970).

[15] Sargent, *supra* note 9, at 84.

[16] *See, e.g.,* Demmler, *Developments in the Federal Regulation of Securities,* 12 Bus. Law. 470, 474-76 (1957) [hereinafter cited as Demmler]; Orrick, *Some Observations on the Administration of the Securities Laws,* 42 Minn. L. Rev. 25, 26-30 (1957); Purcell, *supra* note 10, at 278-90; Sargent, *supra* note 9, at 82-89.

[17] SEC Securities Act Release No. 3698 (Oct. 2, 1956).

[18] *See, e.g.,* Demmler, *supra* note 16; Orrick, *Some Interpretative Problems, supra* note 11, at 377-78; Throop, *In Defense of Rule 133—A Case for Administrative Self-Restraint,* 13 Bus. Law. 389 (1958).

[19] SEC Securities Act Release No. 3761 (March 15, 1957).

[20] Great Sweet Grass Oils, Ltd., 37 S.E.C. 683 (1957), *aff'd per curiam sub nom.* Great Sweet Grass Oils, Ltd. v. S.E.C., 256 F.2d 893 (D.C. Cir. 1958); Kroy Oils, Ltd.,

amendment to that effect.[21] However, serious problems relating to the operation and effects of Rule 133 remained.[22]

In 1967 a group was created by the Commission to study the disclosure provisions of the 1933 and 1934 Acts.[23] Included in this study, later known as "The Wheat Report," was a review of Rule 133,[24] which contained several recommendations to the effect that it be retained with modifications[25] or replaced entirely.[26] As a result of this and further considerations on the subject, the commission proposed the recision of Rule 133.[27] On October 6, 1972, the Commission announced the recision of Rule 133 and the adoption of Rule 145, effective January 1, 1973.[28]

Henceforth, under Rule 145, an "offer," "offer to sell," "offer for sale" or "sale" will be deemed to be involved in an issuance of securities of one corporation to another corporation in consideration of the transfer of assets of the acquired corporation.[29] Since there is deemed to be a sale or offer to sell

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37 S.E.C. 683 (1957); S.E.C. v. Micro-Moisture Controls, Inc., 148 F. Supp. 558 (S.D.N.Y. 1957) (preliminary injunction), 167 F. Supp. 716 (S.D.N.Y. 1958) (final injunction), *aff'd sub nom.* S.E.C. v. Culpepper, 270 F.2d 241 (2d Cir. 1959). *See generally* Disclosure To Investors—A Reappraisal of Federal Administrative Policies Under the '33 and '34 Acts 262-63 (1969) [hereinafter cited as Wheat Report].

21 SEC Securities Act Release No. 4115 (July 16, 1959). *See generally Recent Developments, supra* note 11, at 122-24.

22 *See generally* Wheat Report, *supra* note 20, at 259-69; PRACTISING LAW INSTITUTE, SEC CONSEQUENCES OF CORPORATE ACQUISITIONS 17-41 (C. Schneider ed. 1971) [hereinafter cited as SEC CONSEQUENCES]; Schneider, *Acqquisitions Under the Federal Securities Acts—A Program for Reform*, 116 U. PA. L. REV. 1323 (1968); *Rule 133 and the No-Sale Theory, supra* note 13, at 533-34.

23 SEC Securities Act Release No. 4885 (Nov. 29, 1967). *See* Wheat Report, *supra* note 20, at 3.

24 Wheat Report, *supra* note 20, at 251.

25 *Id.* at 273-77.

26 *Id.* at 277-78.

27 SEC Securities Act Release No. 5246 (May 2, 1972).

28 SEC Securities Act Release No. 5316 (Oct. 6, 1972). *See* CCH FED. SEC. L. REP. ¶ 3011A at 3053-3, 4 (1972) setting forth the text of Rule 145, which in part reads:

> (a) *Transactions Within the Rule.* An "offer," "offer to sell," "offer for sale" or "sale" shall be deemed to be involved, within the meaning of Section 2(3) of the Act, so far as the security holders of a corporation or other person are concerned where, pursuant to statutory provisions of the jurisdiction under which such corporation or other person is organized, or pursuant to provisions contained in its certificate of incorporation or similar controlling instruments, or otherwise, there is submitted for the vote or consent of such security holders a plan or agreement for—
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> (1) *Reclassification* . . . .
>
> (2) *Merger or Consolidations* . . . .
>
> (3) *Transfers of Assets.* A transfer of assets of such corporation or other person, to another person in consideration of the issuance of securities of such other person or any of its affiliates, if:
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> (A) such plan or agreement provides for dissolution of the corporation or other person whose security holders are voting or consenting; or
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> (B) such plan or agreement provides for a pro rata or similar distribution of such securities to the security holders voting or consenting; or
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> (C) the board of directors or similar representatives of such corporation or other person, adopts resolutions relative to (A) or (B) above within one year after the taking of such vote or consent; or
>
> (D) the transfer of assets is a part of a pre-existing plan for distribution of such securities, notwithstanding (A), (B), or (C), above . . . .

29 Rule 133, however, remains available for those transactions which had been submitted to security holders for consent or to the appropriate governmental agency for

securities in such transactions, the acquiring corporation is an issuer and will be required to register the securities proposed to be issued in the transaction in order to comply with section 5. In registering these securities, the issuer will be responsible for disclosing the necessary information in the registration statement[30] and the prospectus[31] to be received by offerees, who in these transactions are the shareholders of the acquired corporation.

Because "material" facts[32] relating to the condition of the acquired corporation will undoubtedly have a bearing on the value of the issuer's securities, they must be included in the issuer's (acquiring corporation's) prospectus[33] just as they must be included in the acquired corporation's proxy statement. If such information is misstated or omitted, the issuer is subject to potential civil liabilities under section 11(a) of the Act.[34] Even though the necessary information is furnished by the acquired corporation, the issuer could be liable for such deficiencies as undervaluations,[35] failure to discuss future plans[36] or, as in the *Beatty* case,[37] the failure to disclose a contingent asset. This, of course, places the issuer in a very uncomfortable position. On the one hand, it must, of necessity, rely on the information supplied by the acquired corporation, thereby exposing itself to potential section 11 liabilities. On the other hand, as an issuer it is not given the benefit of the due diligence defenses[38] afforded other defendants in sections 11(b)[39] and 15.[40] Thus, it appears that the acquiring corporation in transactions similar to that in *Beatty* will be liable for misstatements or omissions even though they lack sufficient control over the acquired corporation to obtain accurate information with which to prepare its prospectus.

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approval prior to January 1, 1973. In addition, Rule 145 does not affect transactions that are exempt from registration pursuant to other provisions of the Act. *See* CCH FED. SEC. L. REP. ¶ 3011A, at 3053-3 (1972).

30 15 U.S.C. § 77g (1970).

31 *Id.* § 77j.

32 17 C.F.R. § 230.405 (1972) defines "material" as that information about "which an average prudent investor ought reasonably to be informed before purchasing the security registered." In discussing the duty of insiders to disclose material facts, the court, in *Kohler v. Kohler Co.*, 319 F.2d 634, 642 (7th Cir. 1963), stated that those facts "which in reasonable and objective contemplation might affect the value of the corporation's stock or securities . . ." must be disclosed. *See* S.E.C. v. Texas Gulf Sulphur, 401 F.2d 833, 849 (2d Cir. 1968), *cert. denied sub nom.*, Coates v. S.E.C., 394 U.S. 976 (1969); List v. Fashion Park, 340 F.2d 457, 462 (2d Cir. 1965), *cert. denied sub nom.*, List v. Lerner, 382 U.S. 811 (1965); Chasins v. Smith, Barney & Co., 438 F.2d 1167, 1171 (2d Cir. 1971); Feit v. Leasco Data Processing Equip. Corp., 332 F. Supp. 544, 569 (E.D.N.Y. 1971).

33 Feit v. Leasco Data Processing Equip. Corp., 332 F. Supp. 544, 569 (E.D.N.Y. 1971). *See SEC Consequences, supra* note 22, at 72-73.

34 15 U.S.C. § 77k(a) (1970).

35 *See, e.g., Speed v. Transam. Corp.*, 235 F.2d 369, 372 (3d Cir. 1956), in which the acquired corporation's inventory was undervalued and *Gerstle v. Gamble-Skogmo, Inc.*, 298 F. Supp. 66, 92 (E.D.N.Y 1969), in which the fixed assets of the acquired corporation were undervalued

36 *See, e.g.*, Gerstle v. Gamble-Skogmo, Inc., 298 F. Supp. 66, 94 (E.D.N.Y. 1969).

37 345 F. Supp. 1188 (S.D. Iowa 1972).

38 *See* Schneider & Manko, *Rule 145*, 5 REV. OF SEC REG. 811, 824 (1972) [hereinafter cited as Schneider & Manko].

39 15 U.S.C. § 77k(b) (1970).

40 *Id.* § 77o.

It has been suggested that the acquiring corporation should insert a disclaimer in the prospectus[41] and negotiate for indemnification and contribution provisions in the acquisition agreement[42] in an effort to relieve itself of section 11 liabilities for materials supplied to it by the acquired corporation. The effectiveness of such provisions are, as yet, unknown. However, such provisions may provide a margin of relief for the issuer and, in light of potentially harsh results of Rule 145, should be included.[43]

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41 *See* Schneider & Manko, *supra* note 38, at 825.

42 *See generally* Ruder, *Multiple Defendants in Securities Law Fraud Cases: Aiding and Abetting Conspiracies, In Pari Delicti, Indemnification and Contribution*, 120 U. PA. L. REV. 597, 647-59 (1972) [hereinafter cited as Ruder]; Schneider & Manko, *supra* note 38, at 826.

43 *See* Ruder, *supra* note 42; Schneider & Manko, *supra* note 38, at 825-26.

WORKMEN'S COMPENSATION—AN INMATE WORKING IN PRISON INDUSTRIES IS NOT AN EMPLOYEE FOR PURPOSES OF THE WORKMEN'S COMPENSATION ACT.—*Frederick v. Men's Reformatory* (Iowa 1973).

Theodore Frederick was an inmate at the Men's Reformatory at Anamosa. On May 20, 1969, while Frederick was operating a punch press in the license plate factory at the prison, four of his fingers were crushed and later amputated. Without disputing the facts, the State denied the inmate's claim for workmen's compensation on the basis that he was not an employee of the State at the time of the injury.[1] He applied for arbitration[2] and the deputy industrial commissioner found that he was an employee and awarded benefits.[3] The State then applied for a review decision[4] and the industrial commissioner affirmed the award.[5] Upon appeal to the district court,[6] however, the court held that the commissioner had exceeded his powers and reversed his decision.[7] The Supreme Court of Iowa *held*, affirmed, an inmate working in prison industries is not an employee for purposes of the Workmen's Compensation Act. *Frederick v. Men's Reformatory*, 203 N.W.2d 797 (Iowa 1973).

The sole issue presented to the court was whether a prisoner could qualify as an employee of the State to recover workmen's compensation benefits. The issue is one of first impression in Iowa. The general rule regarding inmates injured while engaged in prison industries is to deny compensation, even when some type of monetary reward is paid for their services.[8] The reason most often given is that a prisoner cannot and does not make a contract of hire for his services and thus cannot be employed.[9] Most of the states which have dealt with this issue have used a similar rationale.[10] Other states deny-

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1 After an injury has occurred, the employee serves notice of his intent to claim compensation on his employer. IOWA CODE §§ 85.24-.25 (1971).

2 If the parties fail to reach an agreement as to compensation, either party may file a petition for arbitration with the industrial commissioner. IOWA CODE § 86.14 (1971).

3 Frederick v. Men's Reformatory, Arb. Dec. (1971) (Ferris, Arbitrator).

4 If either party is aggrieved by the decision of the deputy commissioner at the arbitration hearing, it may file a petition for review with the commissioner and at the review hearing, the commissioner hears all the evidence taken before the arbitration hearing and any additional evidence that is presented. IOWA CODE § 86.24 (1971).

5 Frederick v. Men's Reformatory, Rev. Dec. (1971) (Landess, Comm'r).

6 A party may appeal from the review decision to the district court of the county in which the injury occurred. IOWA CODE § 86.26 (1971).

7 Frederick v. Men's Reformatory, No. 16999 (D. Iowa, Oct. 29, 1971).

8 *See* 1A A. LARSON, THE LAW OF WORKMEN'S COMPENSATION § 47.31, at 759 (1st ed. 1967) [hereinafter cited as LARSON]; E. BLAIR, REFERENCE GUIDE TO WORKMEN'S COMPENSATION LAW 4-25 (1972).

9 *See* 1A LARSON, *supra* note 8, § 47.31, at 761.

10 *See, e.g.*, Watson v. Industrial Comm'n, 100 Ariz. 327, 414 P.2d 144 (1966) (no voluntary agreement or intent to contract); Schraner v. State, 189 N.E.2d 119 (Ind. 1963) (contract for hire must be voluntary; prison labor is involuntary); Jones v. Houston Fire & Cas. Ins. Co., 134 So. 2d 377 (La. 1961) (no capacity to contract for hire); Green's Case, 28 Mass. 506, 182 N.E. 857 (1932) (not an employee under a contract of hire); Scott v.