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PROSPECTUS LIABILITY FOR FAILURE TO DISCLOSE
POST-EFFECTIVE DEVELOPMENTS: A NEW DUTY AND
ITS IMPLICATIONS

The prospectus has always been a significant instrument in the securities field. Its use furthers the basic purpose of the Securities Act of 1933 to secure "full disclosure of every essentially important element attending the issue of a new security. . . ." and to impose "high standards of trusteeship" upon all persons "who sponsor the investment of other people's money." In pursuit of this purpose the Securities and Exchange Commission (SEC) has continuously reviewed and revised prospectus requirements. Through this process and through court decisions, liability for breach of the duty of disclosure has been continuously expanded.

The recent case of SEC v. Manor Nursing Centers, Inc. exemplifies this trend. In Manor, an issuer initiated an effort to sell 450,000 shares of stock. In the prospectus the issuer said that the offering would be on an "all or nothing basis," that the proceeds would be placed in an escrow account "unavailable for other uses," and that the shares would be sold for cash only. The prospectus did not provide for any special types of compensation to be given to certain purchasers or brokerage firms. From the beginning the underwriter experienced difficulty selling the stock. To assist in developing sales, an extensive solicitation of brokerage firms, corporations, and individuals was made. During this solicitation, several parties were able to secure favors and special compensation from the issuer for their participation in the offering. Also, when it ap-

5. 458 F.2d 1082 (2d Cir. 1972).
6. Id. at 1090.
7. Id. at 1089-90. All shares offered on an "all or nothing" basis must be sold within a specified period. Otherwise the offering terminates and all funds are returned to the subscribers. Id. at 1089-90.
8. 458 F.2d at 1090.
9. Id.
peared that all of the shares would not be sold by the closing date specified on the prospectus, a number of "bootstrapping" sales were made which required drawing checks on sales proceeds which had never been placed in the escrow account. As a result, many of the terms of the prospectus and those of a subsequent amendment were violated. In an action brought by the SEC, the district court found that the stock issue violated the anti-fraud and prospectus delivery requirements of the securities acts and issued an order for injunctive relief. On appeal, the Second Circuit affirmed on both counts. Not surprisingly, as to the first charge, the appellate court held that

the effect of the antifraud provisions of the Securities Act (§ 17(a)) and of the Exchange Act (§ 10(b) and Rule 10b-5) is to require the prospectus to reflect any post-effective changes necessary to keep the prospectus from being misleading in any material respect.

However, the court went further and held that, pursuant to the prospectus delivery requirements of the 1933 Act,

10. Id. at 1091. Checks were drawn on sales proceeds which had never been placed in the escrow account and were made payable to a corporation which was controlled by a member of the Manor selling group. These funds were used to purchase additional Manor shares. Id.
12. 458 F.2d at 1096.
Section 17(a) of the 1933 Act provides that
It shall be unlawful for any person in the offer or sale of any securities . . .
(1) to employ any device, scheme or artifice to defraud, or
(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or
(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Section 10(b) of the Securities Exchange Act of 1934 provides that
It shall be unlawful for any person, . . . [to] use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the [SEC] may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Rule 10b-5 provides that
It shall be unlawful for any person . . .
(a) to employ any device, scheme, or artifice to defraud,
(b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
(c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

the appellants were under a duty to amend or supplement the Manor prospectus to reflect post-effective developments; that their failure to do so stripped the Manor prospectus of compliance with § 10(a); and that appellants therefore violated § 5(b)(2).\(^\text{18}\)

This note explores the duty to reflect post-effective developments in the prospectus under both approaches and also discusses a new SEC stop order policy which may lie behind the decision in Manor.

**Duty Under Anti-Fraud Rules**

The SEC, commentators, and courts have recognized that the anti-fraud provisions of the securities acts require that post-effective developments which materially alter the picture expressed in the registration statement must be communicated to the offerees.\(^\text{14}\) Authorities also recognize the prospectus as a vehicle for satisfying this duty.\(^\text{15}\) Consistent with this background, the Manor court used the anti-fraud provisions of § 17(a) of the 1933 Act, § 10(b) of the 1934 Act, and rule 10b-5 to support its first theory of liability. Quoting from SEC v. Bangor Punta Corp.,\(^\text{16}\) the Manor court said:

"[t]he effect of the anti-fraud provisions . . . is to require the prospectus to reflect any post-effective changes necessary to keep the prospectus from being misleading in any material respect. . . ."\(^\text{17}\)


Section 5(b)(2) of the 1933 Act provides that it shall be unlawful for any person . . . to carry . . . in interstate commerce any . . . security for the purpose of sale or delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of [Section 10(a)].


16. 331 F. Supp. 1154 (S.D.N.Y. 1971) (defendant required to offer rescission to its shareholders because of its failure to accurately disclose the value of one of its major assets).

17. 458 F.2d at 1096. The court also relied on Danser v. United States, 281 F.2d 492 (1st Cir. 1960). 458 F.2d at 1096. In Danser the First Circuit concluded that a failure to disclose post-effective developments would result in § 17(a) liability. Danser v. United States, supra at 496-97.
There are two ways in which information reflecting post-effective changes can be communicated to purchasers. First, the prospectus (and registration statement) can be amended; this requires review and declaration of effectiveness by the SEC. Second, the prospectus can be supplemented by means of a sticker or similar attachment. A supplemented prospectus is not processed as such by the SEC. The rules only require that 25 copies be filed with the Commission before it is used.

An accepted rule of thumb for determining which of the two methods to use is that addition of information indicates supplementing, while substitution of information suggests amending.

In most cases, which involve failure to disclose post-effective changes, the issuer has made no attempt whatsoever to communicate the information. Thus the courts have not been forced to decide when amendment rather than mere supplementation is necessary to avoid liability. Manor typifies such cases by its simple conclusion that disclosure must be made, without indicating what form that disclosure must take.

**Duty Under §§ 10(a) and 5(b)(2) of the 1933 Act**

In addition to finding that the issuer in Manor violated the anti-
fraud rules, the court held that appellants were under a duty to amend or supplement the Manor prospectus to reflect post-effective developments; that their failure to do so stripped the Manor prospectus of compliance with § 10(a); and that appellants therefore violated § 5(b)(2). 24

The language of § 10(a) does not include a general duty to update prospectuses. Section 10(a)(3) requires supplementation when the prospectus is used nine months after the effective date and the information contained in it is 16 months old. 25 Other than this provision, the only substantive requirement on prospectus content is § 10(a)(1), which states that the prospectus "shall contain the information contained in the registration statement." 26

As the Manor court recognized, a line of authority holds that there is no duty to update the registration statement to reflect post-effective developments. 27 In Charles A. Howard, 28 the leading authority for this position, the SEC said that the truth of the information in the registration statement is only tested as of the time it becomes effective. If the registration statement is true at the effective date, there is no duty to update it even though it subsequently becomes false and misleading. 29 The SEC has adopted this position because of its interpretation of § 8(d) of the 1933 Act which provides that a stop order may be issued if it appears to the Commission at any time that the registration statement includes any untrue statement of a material fact or omits to state any material fact required to be stated therein or necessary to make the statements therein not misleading. . . . 30

In Howard, the SEC said that [Section 8(d)] does not . . . permit the Commission to issue

24. Id. at 1100.
26. Id. § 77j(a)(1).
28. 1 S.E.C. 6 (1934).
29. Id. at 10. See Sowards, supra note 14. It is interesting to note that one of the cases cited by the Manor court as supporting the duty to reflect post-effective developments under the fraud theory also clearly recognizes that the registration statement speaks as of the effective date. SEC v. Bangor Punta Corp., 331 F. Supp. 1154, 1160 (S.D.N.Y. 1971).
a stop order if it finds that a statement which reflected the truth as of the time the registration statement became effective no longer reflects the truth.\textsuperscript{31}

The SEC thus interpreted "at any time" to mean that it may issue a stop order \textit{at any time it discovers} that a statement did "not reflect the truth as of the time that the registration statement became effective. . . ." but the SEC may not issue a stop order for a statement true at the effective date which becomes \textit{untrue at any time} after the effective date.\textsuperscript{32}

This interpretation has found some support in the case law.\textsuperscript{33} It would seem, therefore, that a prospectus required only to "contain the information contained in the registration statement," would need no updating to satisfy the statute.

\textit{Manor} found this line of argument unpersuasive.\textsuperscript{34} The court held that implicit in § 10(a)’s requirement that the prospectus contain certain information, was the additional requirement that such information be true and correct.\textsuperscript{35} Reasoning from this holding, the court further held that since the information supplied in the prospectus was not "true and correct" at the delivery date, the prospectus did not comply with § 10(a), and therefore violated § 5(b)(2). Neither the exact source of the implication underlying the court’s first holding nor the reasoning involved in drawing such an implication were explained by the court or supported by the authority cited.\textsuperscript{36} Moreover, the court gave no authority

\begin{itemize}
  \item \textsuperscript{31} 1 S.E.C. at 10.
  \item \textsuperscript{32} \textit{Id.} Although some commentators have disagreed with the SEC’s interpretation of § 8(d), they have generally concluded that a registration statement need not be amended after its effective date to reflect post-effective developments. \textit{Loss, supra} note 14, at 290; \textit{Shulman, Civil Liability and the Securities Act, 43 Yale L.J. 227, 243 (1933).}
  \item \textsuperscript{33} Section 11 also supports the proposition that there is no duty to update the registration statement. Liability under § 11 does not attach if the inaccuracy of the registration statement is the result of post-effective date changes. 15 U.S.C. § 77(k) (1970).
  \item \textsuperscript{34} SEC v. Bangor Punta Corp., 331 F. Supp. 1154 (S.D.N.Y. 1971).
  \item \textsuperscript{35} Although conceding that \textit{Howard} found no duty to update the registration statement, the \textit{Manor} court cited \textit{Howard} as recognizing a duty to recognize a duty to update the prospectus. 458 F.2d at 1099. \textit{Manor} thus implied that §§ 5(b) or 10(a) created the duty. While \textit{Howard} does recognize a duty to reflect post-effective developments in the prospectus it did not base its conclusion on §§ 5(b) and 10(a). Rather, its conclusion was based on an interpretation of the anti-fraud provisions of §§ 12 and 17(a).
  \item \textsuperscript{36} To support its holding that information required by § 10(a) must be true and correct, \textit{Manor} cited SEC v. North American Fin., Co., 214 F. Supp. 197 (D. Ariz. 1959), and Eugene M. Rosenson, 40 S.E.C. 948 (1961). These two cases arose out of the same factual occurrence. In \textit{Rosenson} the information in the prospectus and registration statement as well as subsequent amendments was found to be false concerning the “independent” certification of financial statements by the accountant and it was further found that this information was untrue and misleading \textit{when filed}. Eugene M. Rosenson, \textit{supra} at 952. The Commission also found that these false statements were willfully made. \textit{Id.} at 951. The SEC held that it was "implicit from . . . Sections 7
or rationale for its additional assertion that the prospectus must change to reflect developments occurring after the effective date.

Addressing the long assumed absence of a duty to update the registration statement, the Manor court considered the existence of this duty an open question, but found resolution unnecessary for decision of the case. Therefore, whether or not the registration statement has to be amended, the prospectus must be changed to reflect post-effective developments. As mentioned above, Manor also left open the question whether amendment or mere supplementation of the prospectus is required to satisfy the § 10(a) duty. If supplementation is acceptable, then it may indeed be possible for the new prospectus duty to coexist with the absence of a corresponding duty to update the registration statement.

Significance of Manor

Liability under § 5(b) for failure to update prospectuses is clearly a novel creation in Manor. Its creation was apparently also unnecessary because the defendant had already been found in violation of the anti-fraud rules. Yet both the SEC in its brief and the court in its decision went to great lengths to establish this new principle. Since the reason for this effort is not clear from the Manor opinion and facts, some speculation is required to determine the significance of the decision. Manor’s impact can best be judged by examining its effect on the three major means of enforcing securities laws: injunctions by the SEC, private actions by investors, and stop orders.

Injunctions

Section 20(b) of the 1933 Act grants the SEC authority to sue in federal courts for injunctions whenever it appears that

any person is engaged or about to engage in any acts or practices
which constitute or will constitute a violation of the provisions

and 10 that a registration statement and prospectus contain certain information, and that certain information be true and correct.” Id. at 952. The Commission said that its conclusion was “confirmed by Section 24 of the Securities Act, which provides criminal penalties for any untrue or misleading statement of a material fact in any registration statement filed under that Act.” Id. (emphasis added). Since the statements were untrue when made, a stop order would have been available as well as prosecution under the fraud provisions. Therefore, these cases do nothing to support the position of the Manor court as to creation of a duty under §§ 5(b) and 10(a) to update the prospectus for developments which occur after the effective date of the registration statement. The only clear meaning of Rosenson and North American is that the prospectus and registration statement must be true and correct when filed.

37. 458 F.2d at 1099 n.24.
38. Id. at 1099 n.23.
The impact of the new § 5 liability on § 20(b) injunctions can best be measured by determining whether such liability will be more expansive than that now imposed by the anti-fraud provisions of § 17. Section 5 on its face requires no element of scienter. The Manor court undertook an examination of the good faith of the defendants in connection with the anti-fraud rules and found it lacking. However, no separate examination or mention of the element was made in the portion of the opinion dealing with §§ 10(a) and 5(b). Thus, strict liability for misstatements remains a possibility under § 5(b). This result contrasts with the current case law on § 17 injunctions which at least requires proof of negligence. No cases have granted § 17 injunctions under a strict liability standard, and defendants have been allowed to defeat such injunctions by showing due diligence. Section 17(a)(2) also requires proof of misstatements of material facts. A large body of case law has developed defining "materiality" as it relates to the various anti-fraud rules.

42. Section 5 merely speaks of sales activities without a registration statement, without a prospectus satisfying § 10, or while a § 8 stop order is in effect. 15 U.S.C. § 77e (1970). Nothing in § 5 conditions liability on the existence of any particular state of mind.
43. 458 F.2d at 1096-97.
44. See United States v. Sussman, 37 F. Supp. 294, 296 (E.D. Pa. 1941) (criminal case holding that defendant's knowledge of the security's sale in violation of the law was not an element of § 5(a) violation).
46. SEC v. Frank, 388 F.2d 486, 489 (2d Cir. 1968); Walker v. SEC, 383 F.2d 344, 345 (2d Cir. 1967).
48. In an action by the SEC for injunctive relief, a material fact is considered that which would cause a reasonable investor to rely thereon and in reliance cause him to buy or sell a corporation's securities. SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 849 (2d Cir. 1968) cert. denied 394 U.S. 976 (1969); SEC v. R. A. Holman & Co., 366 F.2d 455, 459 (2d Cir. 1966); Cady, Roberts & Co., 40 S.E.C. 907, 915 (1961). At one time it was thought that only facts involved in "extraordinary" situations which would substantially affect the market price were material facts. Fleischer, Securities Trading and Corporate Information Practices: The Implications of the Texas Gulf Sulphur Proceeding, 51 Va. L. Rev. 1271, 1289 (1965). Later decisions have not required "extraordinary" facts such as information related to dividend distributions or earnings. "Material facts" now extends to those facts which would affect the "desire of the investor to buy, sell, or hold." Bromberg, Corporate Information: Texas Gulf Sulphur and Its Implications, 22 Sw. L.J. 731, 741 (1968).
the types of changes which § 10(a) requires to be communicated. It is possible, therefore, that the familiar tests developed in the context of the anti-fraud rules will be carried over to § 5(b) prospectus liabilities, and materiality will need to be proved under both theories to secure an injunction.

**Purchasers Actions**

Section 12(1) of the 1933 Act gives the purchaser a cause of action for damages against "any person who offers or sells a security in violation of section 5 . . . ." Thus, violations of §§ 5(b) and 10(a) as found in Manor give purchasers the right, under § 12, "to recover the consideration paid for such security with interest thereon, [less income received], . . . or for damages if he no longer owns the security."

The relative importance of Manor to purchasers' remedies is dependent upon whether § 12(1) liability will now be more expansive than that already imposed by the anti-fraud provisions. Prior cases under § 12(1) have dealt almost exclusively with sale of securities without registration. Since the existence of the registration statement was the primary issue in these cases, a finding against the seller on this point was virtually determinative of liability. Because of these early cases, and the wording of the statutes, the issues of reliance, scienter, good faith,

49. 458 F.2d at 1098-99.
51. Id.
53. Lynn v. Caraway, 252 F. Supp. 858, 863 (note 6) (W.D. La. 1966), aff'd 379 F.2d 943 (5th Cir. 1967), cert. denied, 393 U.S. 951 (dictum); Loss, supra note 14, at 1693. To establish a prima facie case for unregistered sale under § 12(1), the plaintiff need only prove five elements. First, the plaintiff must establish that the defendant was an offeror or seller or a person in control of an offeror or seller. Securities Act of 1933, § 5(b), 15 U.S.C. § 77e(b) (1970); id. § 15, 15 U.S.C. § 77o (1970). Accord, Loss, supra note 14, at 1719; Sowards, supra note 14, at § 9.03[1]. Second, he must prove that the mails or an instrumentality of interstate commerce was used in the offer or sale. Securities Act of 1933 § 5, 15 U.S.C. § 77e (1970); Loss, supra note 14, at 1693. Third, he must show that the transmittal of a prospectus has taken place. Sowards, supra note 14, at § 9.03. Fourth, he must show that the defendant failed to comply with the prospectus requirements of § 10. Securities Act of 1933, § 5, 15 U.S.C. § 77e (1970); id. § 10, 15 U.S.C. § 77j (1970). Accord, Loss, supra note 14, at 1693; Sowards, supra note 14, at § 9.03. Finally, the plaintiff must prove that a registration statement has not been filed. Securities Act of 1933, § 5, 15 U.S.C. § 77e (1970); Sowards, supra note 14, at § 9.03. Once a prima facie case has been established, the only meaningful defense is that of exemption under §§ 3 or 4. 15 U.S.C. § 77c (1970) (exempted securities); id. § 77d (exempted transactions). See Winter v. D. J. & M. Inv. & Constr. Corp., 185 F. Supp. 943, 946 (S.D. Cal. 1960); Sowards, supra note 14, at § 9.03. Under certain circumstances the defendant may also assert waiver or estoppel defenses to § 12 liability. Straley v. Universal Uranium & Milling Corp., 289 F.2d 370, 373-74 (9th Cir. 1961); Dale v. Rosenfeld, 229 F.2d 855, 859 (2d Cir. 1956).
knowledge of the alleged violation, and causation have been completely irrelevant in § 12(1) cases prior to Manor.

Not so for liability under the anti-fraud provisions. There, the purchaser must show a connection between his detriment and the seller’s misstatements or omissions of “material facts.” To determine whether the particular plaintiff was so influenced, courts must consider the related issues of material fact, reliance, and causation. At common law the plaintiff had to prove reliance and a causal connection between defendant’s conduct and his own. Congress, through enactment of the securities law, has lifted the burden of proving “active” reliance as a condition of recovery. The test of reliance for cases of material omissions has been held to be “whether the plaintiff would have been influenced to act differently... if the defendant had disclosed to him the undisclosed fact.” However, a recent decision has apparently returned to a more active standard by holding that the plaintiff must prove that the defendant’s misstatements or omissions played a substantial part in bringing about the plaintiff’s injury and, further, that the injury was a direct result of the defendant’s action. In any event, the requirements of causation, reliance, and material fact are probably necessary to put some limit on liability, and to that extent are generally desirable.

54. While an action under §§ 12(1), 12(2), 11, and 17(a) of the 1933 Act can only be brought by purchasers, an action under § 10(b) of the 1934 Act and Rule 10b-5 may be brought by sellers as well as purchasers. Simmons v. Wolfson, 428 F.2d 455, 456 (6th Cir. 1970); Birnbaum v. Newport Steel Corp., 193 F.2d 461, 463 (2d Cir. 1952), cert. denied, 343 U.S. 956.
56. List v. Fashion Park, Inc., 340 F.2d 457, 463 (2d Cir.), cert. denied, 382 U.S. 811 (1965). While courts use a reasonable investor standard to decide what are “material facts” in injunctive proceedings brought by the SEC, in private actions for damages, the question is whether the particular plaintiff would be influenced. Id.
Also, in contrast to the early § 12(1) cases the anti-fraud provisions, such as § 12(2), require a showing of negligence. Accordingly, § 12(2) provides a due diligence defense. Thus a defendant is not liable if he sustain[s] the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission. . . .

In sum, it seems unlikely that the courts, with their general disfavor of strict liability, will consider § 12(1) precedent persuasive in personal damage actions based on §§ 5(b) and 10(a) as expanded in Manor. As indicated above, the courts have tried in some instances to put limits on the liability created by the anti-fraud rules by using such doctrines as reliance and due diligence. Furthermore, the Manor court included "materiality" as a prerequisite to its expanded § 5 liability. Assuming that materiality will remain a requirement for § 5(b) and § 10(a) liability, many of the other elements required for liability under the anti-fraud provisions will likely follow.

Stop Orders

The Manor decision does not overturn the longstanding SEC rule that § 8(d) stop orders cannot be issued against a registered offering for failure to reflect post-effective developments. The court assumes this rule's validity before proceeding to explain the § 10(a) duty to update prospectuses. However, the case is significant to stop orders in two ways. First, the court indicated that the issue of whether or not a registration statement speaks only as of its effective date is an open ques-

62. Some cases have held that mere negligence was sufficient in private actions for damages. Stevens v. Vowell, 343 F.2d 374, 379 (10th Cir. 1965); Ellis v. Carter, 291 F.2d 270, 274 (9th Cir. 1962); Royal Air Properties, Inc. v. Smith, 312 F.2d 210, 212 (9th Cir. 1962). Though the mere negligence standard is still the subject of much debate, see Globus v. Law Research Service, Inc., 418 F.2d 1276, 1290-91 (2d Cir. 1969) and Ellis v. Carter, supra at 272-74, recent decisions indicate that mere negligence is not enough to support an action for damages under § 17(a) or Rule 10b-5. Shemtob v. Shearson, Hammill & Co., 448 F.2d 442, 445 (2d Cir. 1971); Globus v. Law Research Service, Inc., supra at 1290-91.


64. 458 F.2d at 1098.

65. For example, the material fact standard requires a misstatement or omission of information that a reasonable investor would rely on to make an investment decision. An issuer, at least, would be considered negligent, since through due diligence he should be able to discover any change in a truly material fact. If the material fact standard is carried over to § 5 violations, then the elements of reliance, negligence and due diligence will also likely be required for liability.

66. See text accompanying notes 27-32 supra.

67. 458 F.2d at 1099.
This posture gives room for examination and change by other courts. Second, and more importantly, the SEC itself requested the court to characterize the rule in a way which would remove statutory barriers to the rule's modification.69 The fact that this characterization is supported by the SEC makes change likely as well as possible.

As mentioned above, the SEC previously felt that it was without power to stop order a registration statement if post-effective developments made the statement untrue.70 The SEC's brief in Manor reveals that it has changed this position. The brief characterizes the Charles A. Howard71 line of cases as not based on statutory interpretation of § 8(d), as was stated in the Howard case, but rather as based on a series of discretionary refusals to exert statutory power for reasons of policy and convenience.72 In support of its newly claimed authority, the SEC quotes the House Report of the 1933 Act as indicating that Congress intended the Commission to have and use stop order power when a registration statement became misleading.73 The same House Report had been put forth by commentators as inconsistent with the Howard rule,74 and it does indeed support the new interpretation.75

The SEC's brief indicates that the factors which determine when § 5(b) has been violated by delivery of an out-of-date prospectus are the same factors which go into the stop order decision.76 The SEC's argu-

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68. Id. at 1099 n.24.
69. SEC Brief, supra note 39, at 44-49.
70. See text accompanying notes 28-32 supra.
71. 1 S.E.C. 6 (1933). See text accompanying notes 28-32 supra.
72. The basis for the adoption of this position in those cases was the Commission's belief that, if the truth or falsity of a registration statement were to be determined after its effective date, an issuer, in order to avoid the risk of a stop order, would have to halt its offering repeatedly each time a material post-effective event occurred until an amendment to the registration statement should be filed and declared effective. Such a result, of course, would impose an unnecessary burden upon honest issuers involved in legitimate public offerings, since compliance by the issuer with other provisions of the statute normally would assure full disclosure to investors of developments occurring during the selling period.

SEC Brief, supra note 39, at 47-48.
73. In determining whether a stop order should issue, the Commission will naturally have regard to the facts as they then exist and will stop order the further sale of securities even though the registration statement was true when made, [and] it has become untrue or misleading by reason of subsequent developments.

74. See, e.g., Loss, supra note 14, at 290.
75. Language in the House Report clearly flies in the face of the Howard rule. For the specific language, see notes 73 supra & 76 infra.
76. After [the registration statement becomes effective] . . . securities may be sold . . . only if the buyer is given a substantial replica of the information included in the "registration statement"; and if sales are made without giving
ment in Manor may well indicate the criteria which it will use when and if it exerts its stop order authority. An excerpt from the brief demonstrates the Commission’s perspective on post-effective developments. After noting policy considerations applied in the Howard line of cases, the brief continues:

But the Commission has never applied this policy where, as here, the post-effective developments involved a major and substantial change in the basic nature and terms of the public offering which was deliberately, willfully and voluntarily effected by the issuer and selling shareholders. Under such circumstances it is clear that no unnecessary burden is imposed in requiring an amendment of the registration statement and prospectus since those kinds of changes are of such magnitude and purport that the misleading impression conveyed to investors in the prospectus could not be cured simply by stickering or otherwise supplementing the prospectus.

The test suggested above will probably not remain in such a restricted form. The context of an appellate brief and the need to distinguish the Howard line of cases exerted pressure on the Commission to state the narrowest and most persuasively clear basis for SEC action. In practice, such restraints would not be present, and the real policies underlying regulation of distributions would lead to development of new criteria. The factor of deliberateness is not relevant in any stop order proceeding and almost certainly will be dropped. The other criterion, that the change involve the nature and terms of the offering, is substantive and may, with more definition and explanation, prove to be a meaningful distinction.

Where the condition of the issuer or his assets substantially change, and therefore the original prospectus would mislead a reasonable investor, such changes should be disclosed. Supplementation of the prospectus should satisfy this duty. But where there is a “major and substantial” change in the “nature and terms” of the offer itself, the registration statement no longer fully covers the actual distribution. Thus, amendment of the registration and prospectus should be required. Should the issuer

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77. See note 72 supra & text accompanying.
78. SEC Brief, supra note 39, at 48.
79. Loss, supra note 14, at 304.
not file an amendment, the SEC should have the right to stop order the registration.

CONCLUSION

Manor clearly holds that there is a duty to update the prospectus under both the anti-fraud rules and the prospectus delivery requirements of §§ 5(b)(2) and 10(a). This latter liability is a novel creation and has implications on three major methods of enforcing the 1933 Act—injunctions, purchasers' actions, and stop orders. With regard to this last method, the new stop order policy suggested by the SEC in its brief may ultimately give Manor its greatest significance.

Jon S. Readnour