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Casenotes: Federal Securities Law — Definition of a Security — the Sale of Business Doctrine Rejected — Federal Jurisdiction under Rule 10b-5 When Fraud Occurs in Connection with the Sale of a Business Structured as a Sale of the Corporate Stocks. *Golden v. Garafalo*, 678 F.2d 1139 (2d Cir. 1982)

Donna Bianco Imhoff
University of Baltimore School of Law

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FEDERAL SECURITIES LAW — DEFINITION OF A SECURITY
— THE SALE OF BUSINESS DOCTRINE REJECTED — FEDERAL
JURISDICTION UNDER RULE 10b-5 WHEN FRAUD OCCURS IN CONNECTION WITH THE SALE OF A BUSINESS
STRUCTURED AS A SALE OF THE CORPORATE STOCKS.
Golden v. Garafalo, 678 F.2d 1139 (2d Cir. 1982).

The *Golden v. Garafalo*¹ case involved the sale of a ticket brokerage firm by defendant Garafalo to the Goldenes. The attorneys for the parties structured the transaction as a sale of stock in order to circumvent a nonassignment clause in the defendant's lease.² The contract provided that the plaintiffs pay an amount equal to the assets of the business plus one hundred and eight thousand dollars.³ Several months after assuming control of the business, the plaintiffs filed suit in federal district court alleging that the defendant had made material misstatements in both the negotiations and in the contract of sale. They based their federal claim solely on rule 10b-5.⁴ The district court granted defendant's motion to dismiss for lack of subject matter jurisdiction.⁵ Relying upon the sale of business doctrine, the court found that the protective purposes of the federal securities laws were not implicated because the economic reality of the transaction was the sale of an entire business. Furthermore, the court held that since the transaction did not involve a security, there was no cause of action under rule 10b-5 and therefore no basis for federal jurisdiction. On appeal, the United States Court of Appeals for the Second Circuit explicitly rejected the sale of business doctrine and reversed the decision of the district court.⁶ The appellate court held that when there is a sale of an instrument with the characteristics of stock, there is no need to examine the economic reality of the transaction because the instrument is a security within the purview of the federal securities laws.

1. 678 F.2d 1139 (2d Cir. 1982).

2. *Golden v. Garafalo*, 521 F. Supp. 350, 351 (S.D.N.Y. 1981), *rev'd*, 678 F.2d 1139 (2d Cir. 1982). Ultimately the *Golden* court determined that the reason for structuring the transaction as a sale of stock was irrelevant.

3. 521 F. Supp. at 351.

4. *Id.* at 352. Rule 10b-5 states:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national security exchange,

(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.

17 C.F.R. § 240.10b-5 (1982). Under the federal claim, the plaintiffs sought rescission of the contract. They also sought compensatory and punitive damages and equitable relief pursuant to four pendent state law claims.

5. *Golden*, 678 F.2d at 1140.

6. *Id.* at 1144.

Prior to the United States Supreme Court's 1975 decision in *United Housing Foundation, Inc. v. Forman*,⁷ the term "stock," as stated in the definition of a security,⁸ was considered to be reasonably precise and did not result in any significant confusion.⁹ Thus, courts consistently held the sale of a business represented by a sale of its stock to be a securities transaction, and readily granted federal jurisdiction under the securities laws.¹⁰ The most recent of those cases, *Occidental Life Insurance Co. v. Pat Ryan & Associates, Inc.*,¹¹ held that as a matter of law, the sale of stock representing the sale of a business warranted the protection of the federal securities acts.¹² The *Occidental Life* court further stated that every instrument used in a sales transaction need not meet the definition of a security established by the Supreme Court in *SEC v. W.J. Howey Co.*¹³ In *Howey*, the Court determined that an investment contract was a security when it involved an investment in a common enterprise with profits derived solely from the efforts of others.¹⁴ The court in *Occidental Life* found that when the sale of a corporation is structured as a sale of stock "rather than a simple trans-

7. 421 U.S. 837 (1975).

8. The definitional section of the Securities Exchange Act of 1934 provides: "When used in this chapter, unless the context otherwise requires: The term 'security' means any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement . . . investment contract . . . or, in general, any instrument commonly known as a 'security' . . ." 15 U.S.C. § 78c(10) (1976). Since Congress did not articulate the relevant economic criteria for practical application of the definitional section, that task has fallen to the Securities and Exchange Commission and the federal courts. See Seldin, *When Stock Is Not A Security: The "Sale of Business Doctrine" Under The Federal Securities Laws*, 37 BUS. LAW. 637, 666 (1982).

9. Hannan & Thomas, *The Importance of Economic Reality and Risk in Defining Federal Securities*, 25 HASTINGS L.J. 219, 222 (1974).

10. See *Occidental Life Ins. Co. v. Pat Ryan & Assocs., Inc.*, 496 F.2d 1255 (4th Cir.), cert. denied, 419 U.S. 1023 (1974); *Matheson v. Armbrust*, 284 F.2d 670 (9th Cir. 1960), cert. denied, 365 U.S. 870 (1961); *Bailey v. Meister Brau, Inc.*, 320 F. Supp. 539 (N.D. Ill. 1970); *Dauphin Corp. v. Davis*, 201 F. Supp. 470 (D. Del. 1962). Permitting federal jurisdiction in sale of business cases was apparently the general rule in the pre-*Forman* era and, although objections were raised, there was no judicial articulation of the sale of business doctrine as a means to avoid jurisdiction. Indeed, prior to *Forman*, noted authorities warned practitioners that a sale of a corporate business should be structured as a sale of assets in order to avoid 10b-5 liability and subsequent litigation in federal court. 4 A. BROMBERG & L. LOWENFELS, *SECURITIES FRAUD & COMMODITIES FRAUD* § 12.10(1) (1967 & Supp. 1974).

11. 496 F.2d 1255 (4th Cir.), cert. denied, 419 U.S. 1023 (1974).

12. 496 F.2d at 1261 (quoting *SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344, 351 (1943)). *Occidental Life* involved the sale by Occidental of its wholly-owned subsidiary, an insurance company. The transaction was structured as a sale of all the outstanding stock of the company. Prior to the sale, the capital of the company was found to be substantially impaired. In addition the seller entered into agreements with two states which required future purchasers of the business to requalify. The buyer purchased without knowledge of the seller's mishandling of the company. *Id.* at 1259.

13. 328 U.S. 293 (1946).

14. *Id.* at 301.

fer of assets . . . th[e] case . . . literally fits the definition of a security."¹⁵

The sale of business doctrine had its origins in *United Housing Foundation, Inc. v. Forman*,¹⁶ in which the Supreme Court considered the status of an instrument called "stock." The *Forman* Court determined that shares of stock entitling a purchaser to lease an apartment in a housing cooperative were not securities within the purview of the federal securities laws.¹⁷ The Court applied a two-step analysis and determined that, first, the instruments had none of the characteristics of ordinary stock.¹⁸ Second, the Court found that they were not securities in light of the *Howey* decision.¹⁹ Courts that apply the sale of business doctrine rely upon this second step of the *Forman* analysis to determine whether an instrument described as "stock" is actually a security.²⁰ In so doing, they interpret *Forman* as a renunciation of the literal approach to defining securities as exemplified in *Occidental Life*.²¹ These courts hold, in effect, that an instrument possessing all the common characteristics of stock is not a security, and will not be protected by

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15. 496 F.2d at 1263. The *Occidental* court also stated: "Section 10(b) must be read flexibly, not technically and restrictively. *Since there was a "sale" of a security and since fraud was used "in connection with" it, there is redress under § 10(b), whatever might be available as a remedy under state law.*" *Id.* at 1262 (emphasis in original) (quoting Superintendent of Ins. of N.Y. v. Bankers Life & Cas. Co., 404 U.S. 6, 10-12 (1971)). The court in *Occidental Life* reasoned that application of section 10(b) cannot depend on whether the purchaser buys a small interest, a controlling interest, or all of the stock of a corporation. 496 F.2d at 1263.
 16. 421 U.S. 837 (1975).
 17. *Id.* at 848-51. When an instrument possesses none of the significant characteristics typically associated with a security, the name of the instrument is not dispositive in determining whether it is a security.
 18. Those characteristics are: (1) negotiability; (2) ability to be pledged or hypothecated; (3) voting rights in proportion to the number of shares owned; (4) ability to appreciate in value; and (5) right of the holder to receive dividends contingent upon apportionment of profits. *Id.* at 851.
 19. *Id.* at 851-58. The instrument failed to meet the *Howey* definition of a security because there was no expectation of profits and the purchase involved a commodity for personal consumption. *See supra* note 14 and accompanying text for the *Howey* definition.
 20. *See, e.g.,* Anchor-Darling Indus., Inc. v. Suozzo, 510 F. Supp. 659 (E.D. Pa. 1981); Barsy v. Verin, 508 F. Supp. 952 (N.D. Ill. 1981). It is notable that several commentators have criticized the *Howey* formula because of its lack of precision. Coffey, *The Economic Realities of "Security": Is There a More Meaningful Formula?*, 18 WESTERN RESERVE L. REV. 367 (1967) (ambiguous); Hannan & Thomas, *The Importance of Economic Reality and Risk in Defining Federal Securities*, 25 HASTINGS L.J. 219 (1974) (applied restrictively without recognizing that it is merely a statement of a result based on the facts of a particular case); Long, *An Attempt To Return "Investment Contracts" to the Mainstream of Securities Regulation*, 24 OKLA. L. REV. 135 (1975) (misleading).
 21. *See Frederiksen v. Poloway*, 637 F.2d 1147, 1150-51 (7th Cir.), cert. denied, 451 U.S. 1017 (1981), which is the seminal case on the doctrine. *See generally* Thompson, *The Shrinking Definition of a Security: Why Purchasing All of a Company's Stock Is Not a Federal Security Transaction*, 57 N.Y.U. L. REV. 225 (1982).

the securities laws unless all the requirements of the *Howey* test are satisfied.

Typical of decisions relying on the sale of business doctrine, the district court in *Golden* found that the stock purchased was not a security because the purchaser gained personal control of the business.²² When one acquires one hundred percent or a controlling percentage of the stock of a business, which he then manages, there is no reliance upon the efforts of others so as to satisfy that element of the *Howey* test.²³

In addition to relying upon an interpretation of the *Forman/Howey* cases, courts which apply the sale of business doctrine find support for their position in the commercial-investment dichotomy.²⁴ The dichotomy presumes a distinction between transactions of a primarily commercial character and those of a primarily investment character. When a transaction involves a transfer of control it is characterized as a commercial, rather than an investment, transaction which does not merit the shelter of the federal securities laws. Thus, the sale of business doctrine has been applied to deny federal jurisdiction when the plaintiff was the buyer or seller of as little as fifty percent of the stock of a corporation.²⁵ Such an individual is deemed an entrepreneur engaged in a commercial transaction, rather than a passive investor, and therefore not eligible to claim protection under rule 10b-5.²⁶ However, the commercial-investment dichotomy causes problems in transactions that involve less than one hundred percent of the stock of a business, because an ad hoc decision is required to determine whether a transfer of control has occurred.²⁷

Critics of the sale of business doctrine, including the Securities and Exchange Commission,²⁸ contend that the *Forman* case is not dispo-

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22. *Golden*, 521 F. Supp. 350 (S.D.N.Y. 1981), *rev'd*, 678 F.2d 1139 (2d Cir. 1982).
23. 521 F. Supp. at 354-55; *see also* Frederiksen v. Poloway, 637 F.2d 1147 (7th Cir.), *cert. denied*, 451 U.S. 1017 (1981).
24. *See generally* Thompson, *The Shrinking Definition of a Security: Why Purchasing All of a Company's Stock Is Not a Federal Security Transaction*, 57 N.Y.U. L. REV. 225 (1982). The author submits that purchasers in sale of business cases are buying for their own "consumption." *Id.* at 243.
25. *Oakhill Cemetery of Hammond, Inc. v. Tri-State Bank*, 513 F. Supp. 885 (N.D. Ill. 1981) (purchaser of 50% of the company's stock was merely resuming control of the business); *Barsy v. Verin*, 508 F. Supp. 952 (N.D. Ill. 1981) (plaintiff was the seller of 50% of the stock of a printing company). In both cases the courts found an intent to engage in a commercial enterprise rather than an intent to make an investment.
26. *Sutter v. Groen*, 687 F.2d 197, 203 (7th Cir. 1982).
27. *Golden*, 678 F.2d at 1146. In order to avoid this ad hoc decision-making, the Seventh Circuit in *Sutter v. Groen*, 687 F.2d 197 (7th Cir. 1982), established a rebuttable presumption that one who has or who acquires more than 50% of the common stock of a corporation is an entrepreneur rather than an investor. *Id.* at 203.
28. While the federal courts are split on the issue, it is the position of the Securities and Exchange Commission that when a sale of a business is represented by a sale of the stock of the business, a security is involved. *See* Amicus Curiae Brief of the

tive of transactions involving ordinary stock. They challenge *Forman* as the basis of the doctrine because it concerned an instrument which, although called stock, possessed none of the characteristics of ordinary stock. The SEC and courts which refuse to apply the doctrine maintain that since the federal securities laws define stock as a security, those laws are applicable to any instrument that possesses the characteristics of ordinary stock.²⁹

In *Golden v. Garafalo*,³⁰ the Second Circuit examined previous Supreme Court decisions³¹ and found that the determination of whether an instrument was a security centered on the instrument itself, without regard to the relative holdings of the parties or their intentions.³² In contrast, the sale of business doctrine treats a particular instrument as a security for some purposes but not for others.³³ The *Golden* court noted that *Forman* and *Howey*, which form the basis of the doctrine, both involved "unique or idiosyncratic instruments."³⁴ Hence, any language purporting to apply the economic reality test to traditional securities is mere dictum.³⁵ Furthermore, the court criticized proponents of the doctrine for overlooking the first step of the *Forman* analysis which focuses upon whether the instrument in question could be classified as ordinary stock and therefore a security. The Second Circuit asserted that if economic reality were the universal jurisdictional test, the *Forman* court would not have first examined whether the shares in question were stock according to conventional criteria. Therefore, the court concluded that *Forman* requires application of the *Howey* test if, and only if, an instrument purporting to be stock possesses none of the characteristics of stock.³⁶

In addition, the *Golden* court found the application of the commercial-investment dichotomy to be especially strained within the con-

Securities and Exchange Commission, *Daily v. Morgan*, 701 F.2d 496 (5th Cir. 1983). In *Daily*, plaintiffs purchased 100% of the stock of defendant's corporation and later learned that the financial information provided to them in connection with the sale was incomplete and misleading. Defendants failed to disclose the company's high debt-equity ratio or that the business, a franchise truck dealership, was in violation of the franchisor's capital requirements.

29. *E.g.*, *Golden*, 678 F.2d 1139 (2d Cir. 1982); *Mifflin Energy Sources, Inc. v. Brooks*, 501 F. Supp. 334 (W.D. Pa. 1980); *Titsch Printing, Inc. v. Hastings*, 456 F. Supp. 445 (D. Colo. 1978). See *supra* note 18 for the characteristics of ordinary stock.

30. 678 F.2d 1139 (2d Cir. 1982).

31. *Marine Bank v. Weaver*, 455 U.S. 551 (1982); *United Housing Found., Inc. v. Forman*, 421 U.S. 837 (1975); *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946).

32. *Golden*, 678 F.2d at 1143-44.

33. For example, according to the doctrine, when a new manager purchases 100% of the shares of a business from a number of stockholders, the federal securities laws would protect the passive investors but not the new manager. *Id.* at 1142.

34. *Id.* at 1144.

35. *Id.*

36. *Id.* at 1145. *Howey* is of little help in determining the meaning of "specific words which refer to instruments with commonly agreed upon characteristics, such as 'stock.'" *Id.*

text of corporate transfers. The court determined that purchasers of the stocks of a business are investors if they intend to profit by reselling their shares at a future date.³⁷ Therefore, when a transfer of corporate control is motivated by a hope for future capital gains, it is artificial to classify such transactions as exclusively commercial.³⁸ Finally, the *Golden* court noted that the securities acts have always been understood to apply to transactions in shares of closely as well as publicly held corporations, and to negotiated as well as market sales and purchases of stock. Hence, the court found no basis for denying federal jurisdiction in a case involving a negotiated sale of the stock of a closely held corporation.³⁹

Several basic flaws undermine the sale of business doctrine. First, the validity of the doctrine hinges upon the Supreme Court's opinion in *United Housing Foundation, Inc. v. Forman*,⁴⁰ which is not dispositive of the characterization of ordinary stock under the federal securities laws.⁴¹ Second, proponents of the doctrine have failed to define a compelling reason for ignoring Congress' express intent to include ordinary stock as a security by specifically enumerating stock in the definitional sections of the securities acts. Third, application of the doctrine results in an inconsistency because it bars the federal claims of the entrepreneurs engaged in a transaction, but not those of parties to the same transaction who are deemed passive investors. Finally, as a matter of policy, parties who benefit by structuring a business sale as a securities transaction should not be permitted to use the doctrine as a shield against liability under federal law.

There was no question prior to *Forman* that an ordinary stock is a security under the federal securities laws.⁴² Since the *Forman* Court initially determined that the instrument in question was not on its face a stock, the Court's analysis is clearly inapplicable to ordinary stock.

37. *Id.* at 1146. In *Golden*, the court suggested that the sale of business doctrine is of limited value insofar as it concludes that an intent to manage is determinative in finding that a stock transfer is a sale of a business to an entrepreneur rather than a sale of a security to an investor. *Id.* at 1145. The court also pointed out that mixed questions of law and fact, which exceed the scope of the doctrine, would arise when shareholders are part-time managers, intervene sporadically in management, or when new investors, who intend initially to remain passive, are forced into management roles. *Id.*

38. *Id.* at 1146.

39. *Id.* at 1146-47.

40. 421 U.S. 837 (1975).

41. *Coffin v. Polishing Mach., Inc.*, 596 F.2d 1202, 1204 (4th Cir.) (*Forman* requires application of *Howey* only when stock lacks "significant characteristics typically associated with the named instrument"), *cert. denied*, 444 U.S. 868 (1979); *Miffin Energy Sources, Inc. v. Brooks*, 501 F. Supp. 334, 335-36 (W.D. Pa. 1980) (*Forman* does not require application of the economic reality test to shares which possess the common features of stock); *Titsch Printing, Inc. v. Hastings*, 456 F. Supp. 445, 449 (D. Colo. 1978) (*Forman* does not require application of the *Howey* test to stock).

42. *See supra* notes 7-15 and accompanying text.

Therefore, the *Golden* court correctly characterized as dictum the language in *Forman* which appears to support the sale of business doctrine.⁴³ *Forman* simply created a two-step test to determine whether an instrument purporting to be stock is, in fact, a security. The first step is to determine whether the instrument in question bears the characteristics of ordinary stock. If it does, the instrument is a security and further inquiry is unnecessary. If it does not, an examination of the context of the transaction is required. Thus, *Forman* is not authority for the premise of the sale of business doctrine that all instruments must be analyzed in terms of the *Howey* test for investment contracts.

Under the sale of business doctrine courts impose the *Howey* test upon ordinary stock because they hold that whenever a business sale involves a transfer of control, an examination of the context of the transaction is required to determine whether the stock is, in fact, a security. Courts rely upon the words in the prefatory clause of the definitional section of the Securities Exchange Act as statutory authority for a presumption that ordinary stock is not a security unless it satisfies the *Howey* test.⁴⁴ Those words, "unless the context otherwise requires," are critical to the doctrine. Yet *Forman* ignored the phrase and therefore does not support the use of the prefatory clause to examine the context of a sale of stock. While the legislative history of the federal securities laws is virtually silent with regard to the definition of a security, there is no apparent congressional intent to base the definition on the context of the transaction rather than the instrument itself. In fact, the prefatory phrase found in the original draft of the Securities Act of 1933 states, "unless the *text* otherwise indicates."⁴⁵ This suggests that the clause excepts from the definition only those instruments which the

43. See *Golden*, 678 F.2d at 1144.

44. See *Frederiksen v. Poloway*, 637 F.2d 1147, 1150 (7th Cir.) (the prefatory phrase demands a narrow reading of the statute and prevents a literal interpretation of the definitional section), *cert. denied*, 451 U.S. 1017 (1981); see also *Golden*, 678 F.2d at 1141 (under the sale of business doctrine, these words limit the inclusion of instruments to those in which the "context" directly involves the protective purposes of the Securities Acts). See *supra* note 8 for the applicable portion of the act.

45. When the original bill for the Securities Act of 1933 was introduced in the House of Representatives on March 29, 1933, the prefatory clause of the definitional section stated: "That when used in this Act the following terms shall, unless the *text* otherwise indicates, have the following respective meanings" 3 J. ELLENBERGER & E. MAHAR, LEGISLATIVE HISTORY OF THE SECURITIES ACT OF 1933 AND THE SECURITIES EXCHANGE ACT OF 1934 Item 22 (1973) (emphasis added).

While the sale of business doctrine deals with the definitional section of the Securities Exchange Act of 1934, the legislative history of the 1933 Act is significant since it served as a model for the 1934 Act. Hannan & Thomas, *The Importance of Economic Reality and Risk In Defining Federal Securities*, 25 HASTINGS L.J. 219, 220 n.6 (1974). Furthermore, the prefatory clauses are identical in the two acts. Compare 15 U.S.C. § 78c(a) (1976) with 15 U.S.C. § 77b (1976).

text of the act explicitly excludes.⁴⁶ Therefore, since the text of the act expressly includes ordinary stock, there is no basis for the presumption that when a sale of a business occurs the context of the transaction removes ordinary stock from its protection.

While the act limits the definition of a security through exemptions for the purposes of reporting and registration, section 10(b) provides protection against fraud in the purchase and sale of any security, regardless of whether registration is required.⁴⁷ The sale of business doctrine is an attempt to circumvent the plain and unambiguous language of the statute for the purposes of rule 10b-5. Hence, the rejection of the doctrine is not an attempt to expand the coverage of the federal securities laws, but merely to maintain the protection that has traditionally been granted against fraud in connection with the purchase and sale of ordinary stock.

Application of the sale of business doctrine to bar federal jurisdiction results in inconsistent treatment of different parties involved in a single transaction because it denies federal protection to entrepreneurs but not to passive investors.⁴⁸ One who buys or sells a controlling block of the stock of a corporation is considered an entrepreneur. Thus the element of control distinguishes entrepreneurs from investors. However, the need to define control on a case-by-case basis cannot be alleviated by the doctrine's presumption that a transaction involving fifty percent or more of the stock of a corporation effects a transfer of control. The sale of business doctrine neglects to consider any factors used to define control.⁴⁹ Rather, it considers only the percentage of stock involved in the transaction, thus rendering the distinction between entrepreneurs and investors superficial at best.

Finally, equitable considerations mandate that liability under rule 10b-5 exist when fraud occurs in connection with a sale of stock, de-

46. *Frederiksen* and its progeny assert that the prefatory phrase requires an examination of the context of the transaction. One authority submits that courts which take this approach are practicing sophistry. LONG, CASES AND MATERIALS ON STATE SECURITIES (BLUE SKY) REGULATION 11-12 (4th ed. 1981). Professor Long contends that the introductory clause means that under certain conditions a word used in the statute itself may be given a different meaning, depending upon the context in which the word is used. *Id.*

47. The definition is interpreted more broadly for the purposes of antifraud than for registration. 1 A. BROMBERG & L. LOWENFELS, SECURITIES FRAUD & COMMODITIES FRAUD § 4.6 (1967 & Supp. 1974); see also Dillport, *Restoring Balance to the Definition of a Security*, 10 SEC. REG. L.J. 99, 122-23 (1982).

48. See *supra* notes 24-27 and accompanying text.

49. The difficulty of defining control has become apparent in cases dealing with the issue of whether general partnerships or joint ventures are securities. See, e.g., *Pawgan v. Silverstein*, 265 F. Supp. 898 (S.D.N.Y. 1967); *Williamson v. Tucker*, 632 F.2d 579 (5th Cir. 1980). Factors which are important in determining whether control exists are: distribution of power among the parties over the interest involved; experience, knowledge, and ability to make intelligent decisions; and dependence upon some unique ability of another. *Williamson v. Tucker*, 632 F.2d 579, 599 (5th Cir. 1980).

spite the fact that a sale of a business has been effected. The sale of business doctrine permits parties to enjoy the benefit of choosing the structure of the transaction without accepting the concomitant liability under federal law.⁵⁰ Individuals victimized by fraud in connection with the sale of a security have a bona fide federal claim to assert. Thus, they are necessarily entitled to federal jurisdiction.⁵¹

Currently, there is a lack of uniformity in federal judicial administration due to the conflict which exists over the sale of business doctrine.⁵² Unless Congress acts to change the federal statutory definition of a security, or the Supreme Court agrees to decide the issue,⁵³ the conflict will continue to foster uncertainty as to whether the sale of all

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50. A transfer of a business may take place by a sale of stock, a sale of assets or by merger. J. MCGAFFEY, *BUYING, SELLING AND MERGING BUSINESSES* 1 (1979). Among the reasons for structuring the sale as a securities transaction is the avoidance of real estate taxes when real estate of substantial value is involved. *Id.* at 25. Additionally, a stock transaction dispenses with the necessity of compliance with the bulk sales statute, reduces the number of closing papers and eliminates third party consents to the transfer. 1 *BUSINESS ACQUISITIONS* § 5.201b (J. Hertz & C. Baller, eds. 2d ed. 1981). The SEC analogizes the sale of business doctrine to an argument for denying the protections of the bulk sales provisions of Article 6 of the Uniform Commercial Code where a business sale is structured as a sale of assets simply because it could have been structured as a sale of securities. Amicus Curiae Brief of the Securities and Exchange Commission, *Daily v. Morgan*, 701 F.2d 496 (5th Cir. 1983).
 51. Federal courts have exclusive jurisdiction over claims arising under rule 10b-5. 4 A. BROMBERG & L. LOWENFELS, *SECURITIES FRAUD & COMMODITIES FRAUD* § 11.1 (1967 & Supp. 1974).
 52. The sale of business doctrine has been adopted in the Seventh, Tenth, and Eleventh Circuits. *See King v. Winkler*, 673 F.2d 342 (11th Cir. 1982); *Canfield v. Rapp & Son, Inc.*, 654 F.2d 459 (7th Cir. 1981); *Frederiksen v. Poloway*, 637 F.2d 1147 (7th Cir.), *cert. denied*, 451 U.S. 1017 (1981); *Chandler v. Kew, Inc.* [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,965 at 96,053 (D. Colo. Dec. 4, 1975), *aff'd*, [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,966 at 96,053 (10th Cir. Apr. 19, 1977). To date, the Second, Third, Fourth, and Fifth Circuits have granted federal jurisdiction under rule 10b-5 when the sale of a business is structured as a sale of stock. *See Daily v. Morgan*, 701 F.2d 496 (5th Cir. 1983); *Golden v. Garafalo*, 678 F.2d 1139 (2d Cir. 1982); *Glick v. Campagna*, 613 F.2d 31 (3d Cir. 1979); *Coffin v. Polishing Mach., Inc.*, 596 F.2d 1202 (4th Cir.), *cert. denied*, 444 U.S. 868 (1979). Lower federal courts that have refused to apply the doctrine and grant federal jurisdiction are: *Mifflin Energy Sources, Inc. v. Brooks*, 501 F. Supp. 334 (W.D. Pa. 1980); *Titsch Printing, Inc. v. Hastings*, 456 F. Supp. 445 (D. Colo. 1978); *Bronstein v. Bronstein*, 407 F. Supp. 925 (E.D. Pa. 1976). Those which have denied federal jurisdiction under the doctrine are: *Reposystem, B.V. v. SCM Corp.*, 522 F. Supp. 1257 (S.D.N.Y. 1981); *Oakhill Cemetery of Hammond, Inc. v. Tri-State Bank*, 513 F. Supp. 885 (N.D. Ill. 1981); *Anchor-Darling Indus., Inc. v. Suozzo*, 510 F. Supp. 659 (E.D. Pa. 1981); *Barsy v. Verin*, 508 F. Supp. 952 (N.D. Ill. 1981); *Zilker v. Klien* [1981 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,992, at 91,096 (N.D. Ill. 1981); *Dueker v. Turner* [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,386, at 97,535 (N.D. Ga. 1979); *Bula v. Mansfield* [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,964, at 96,051 (D. Colo. 1977).
 53. The Supreme Court denied certiorari in the *Frederiksen*, *Coffin*, and *Occidental Life* cases. All three cases concerned the question of whether federal jurisdiction exists under the federal securities laws in the sale of business cases.

the stock of a business, or even a controlling share, constitutes a security. Ultimately, the statutory maxim that courts give effect to the plain and unambiguous language of a statute⁵⁴ must outweigh the competing policy that lurks behind the sale of business doctrine — that of clearing the federal dockets.

Donna B. Imhoff

54. 2 A. SUTHERLAND, STATUTORY CONSTRUCTION § 46.01 (1973 & Supp. 1982).