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Group Formation under Section 13(d) of the Securities Exchange Act of 1934

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Notes

GROUP FORMATION UNDER SECTION 13(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Section 13(d) of the Securities Exchange Act of 1934 requires financial disclosure by any person acquiring beneficial ownership of more than five percent of the registered securities of a corporation. Section 13(d)(3) includes within the definition of "person" a "group" formed to acquire, hold, or dispose of securities. This Note examines the dynamics behind section 13(d)(3) group formation. Following a discussion of the elements necessary to establish that a section 13(d)(3) group has been formed, the Note concludes that courts should expressly adopt the use of a rebuttable presumption of an agreement to act as a group to demonstrate section 13(d)(3) activity.

INTRODUCTION

THE GENERAL increase in corporate takeover activity during the 1960's led to passage of the Williams Act[1] in 1968, which added section 13(d) to the Securities Exchange Act of 1934.[2] That section now[3] requires disclosure of certain information by persons acquiring more than a five percent equity interest in a corporation. Several questions of statutory construction have arisen under the Williams Act. As two commentators have observed,

> [t]he most difficult question of statutory construction . . . under the Williams Act derives from the interrelationship of Section 13(d)(3), defining a "group" as a "person," and Section 13(d)(1) and rule 13d-1 thereunder, which require a Schedule 13D statement to be filed by any "person" acquiring more than 5 percent of a class of certain specific equity securities . . . .[4]

This Note examines this interrelationship in an attempt to provide a comprehensive yet functional definition of the term "group." The scope of the Williams Act, the reasons for its enactment, and the difficulty of defining a statutory group using the

1. Pub. L. No. 90-439, 82 Stat. 454 (1968), *codified at* 15 U.S.C. § 78m(d)-(e), n(d)-(f) (1976 and Supp. IV 1980).

2. 15 U.S.C. § 78m(d) (1976 & Supp. IV 1980).

3. *See infra* note 17.

4. E. ARANOW & H. EINHORN, TENDER OFFERS FOR CORPORATE CONTROL 83 (1973).

language of the Act alone will be discussed first.[5] An examination of the legislative history of section 13(d) and relevant federal case law, to determine what activities constitute group formation, will follow.[6] The Note then analyzes federal court decisions and recommends, consistent with their methods of inferring the requisite agreement to act as a group, that a presumption for the existence of that agreement be raised when the plaintiff shows (1) communication among the defendants, (2) a common objective, and (3) acts in furtherance of that objective.[7] Defendants may rebut the presumption by showing that any one of the elements is lacking.[8]

The Note also explores the collateral issue of whether, in light of its investor protection policy, the Williams Act should apply to management groups, urging that such groups should be subject to the filing requirements of the Act.[9] The Note concludes that the judicial adoption of a rebuttable presumption, allowing for the inference of an agreement to act as a group, would further the Act's investor protection goal and place potential defendants on notice that certain actions will constitute "group" activity.[10]

I. THE PERSONA OF GROUPS—SUBSECTION 13(d)(3)

The "go-go years"[11] brought with them new perils for the investing public which necessitated greater regulation of the methods of corporate acquisition.[12] Congress responded by passing the Williams Act to require disclosure of information from persons who "purchase by direct acquisition or by tender offers . . . sub-

5. *See infra* notes 11–24 and accompanying text.

6. *See infra* notes 27–92 and accompanying text.

7. *See infra* notes 59–83 and accompanying text.

8. *See infra* notes 84–92 and accompanying text.

9. *See infra* notes 121–23 and accompanying text.

10. *See infra* notes 115–20 and accompanying text.

11. "The 1960's on Wall Street may best be remembered for the pyrotechnics of corporate takeovers and the phenomenon of conglomeration." GAF Corp. v. Milstein, 453 F.2d 709, 717 (2d Cir. 1971), *cert. denied*, 406 U.S. 910 (1972). *See generally* P. STEINER, MERGERS 1–29, *passim* (1975).

12. H.R. REP. NO. 1711, 90th Cong., 2d Sess. 1, 2-3, *reprinted in* 1968 U.S. CODE CONG. & AD. NEWS 2811, 2811–12. The report indicates that

> S. 510 amends the Securities Exchange Act of 1934 by requiring the disclosure of pertinent information and would afford other protections to stock holders . . . .
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> . . . .
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> The competence and integrity of a company's management, and of the persons who seek management positions, are of vital importance to stockholders. Secrecy in this area is inconsistent with the expectations of the people who invest in the securities of publicly held corporations.

Id.

stantial blocks of the securities of publicly held companies."[13] In so doing, Congress sought to facilitate informed investment decisions by shareholders and other investors where corporate control is at issue.[14]

Section 13(d) of the Securities Exchange Act of 1934[15] requires any person acquiring a beneficial interest[16] in more than five percent[17] of a corporation's registered stock to file a Schedule 13D within ten days after that acquisition.[18] Such disclosure concerns "the acquirer, the acquisition transaction, and the acquirer's future plans [and] is valuable in calculating the possibility of, and the effect of, an exercise of control."[19] Since Congress intended to make public *every* stock acquisition which could affect the control of a corporation[20] (every acquisition in excess of five percent of qualifying securities), it enacted subsection (3) to prevent individuals who pool their securities "from evading the provisions of the statute because no one individual owns more than 10 [now 5] percent of the securities."[21] Subsection (3) accomplishes this goal by

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13. 113 CONG. REC. 24,664 (1967).

14. H.R. REP. NO. 1711, *supra* note 12, at 2.

15. 15 U.S.C. § 78m(d) (1976 & Supp. IV 1980). Section 13(d) provides in pertinent part as follows:

> (1) Any person who, after acquiring directly or indirectly the beneficial ownership of any equity security of a class which is registered pursuant to [the Act], . . . is directly or indirectly the beneficial owner of more than 5 per centum of such class shall, within ten days after such acquisition, send to the issuer of the security . . . to each exchange where the security is traded, and [to] . . . the Commission, a [Schedule 13D statement according to the requirements of this subsection and Rule 13d-1].

Id.

16. For a definition of "beneficial ownership" as that term is used in § 13(d), see Rule 13d-3, 17 C.F.R. § 240.13d-3 (1982).

17. As originally enacted, section 13(d) had a filing threshold of ten percent. Williams Act, Pub. L. No. 90-439, 82 Stat. 454 (1968). Congress reduced this threshold to five percent in 1970 because of the significant impact a purchase of even a five percent equity interest in a company could have at the public market and firm management levels. Act of December 22, 1970, Pub. L. No. 91-567, § 1, 84 Stat. 1497 (1970); *see* H.R. REP. NO. 1655, 91st Cong., 2d Sess., *reprinted in* 1970 U.S. CODE CONG. & AD. NEWS 5025, 5027–28.

18. Securities Exchange Act of 1934, § 13(d)(1), 15 U.S.C. § 78m(d)(1) (1976 & Supp. IV 1980).

19. Comment, *Section 13(d) and Disclosure of Corporate Equity Ownership*, 119 U. PA. L. REV. 853, 863 (1971); *see also Hearings on S. 510 Before the Subcomm. on Securities of the Senate Comm. on Banking & Currency*, 90th Cong., 1st Sess. 123 (1967).

20. *Securities Exchange Commission Report on Tender Offer Laws to the Senate Comm. on Banking, Housing and Urban Affairs*, 96th Cong., 2d Sess. 48 (1980).

21. H.R. REP. NO. 1711, *supra* note 12, at 9, *reprinted in* 1968 U.S. CODE CONG. & AD. NEWS at 2818. As one commentator notes,

> [i]n terms of protection for investors . . . the method of aggregation is not vital, but rather the existence of a new aggregation itself . . . . [T]here is little distinction between a market purchase of six percent and the grouping together of three

considering the group itself as the beneficial owner of the aggregate number of its members' securities:[22]

> When two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities of an issuer, such syndicate or group shall be deemed a "person" for the purposes of this subsection.[23]

Determining when a group has been formed is critical, since section 13(d) requires the filing of a Schedule 13D statement within ten days after the requisite acquisition of securities.[24] The statute, however, fails to provide adequate guidelines for making this determination. Although subsection (3) clearly states that to be deemed a "person," a group must have the purpose of "acquiring,[25] holding, or disposing of[26] securities," it fails to specify which activities constitute group formation.

II. ESTABLISHING THE EXISTENCE OF A STATUTORY "GROUP"

A section 13(d)(3) "group" contains two basic elements: an agreement, and a purpose to acquire, hold, or dispose of securities. This Note confines its discussion to the first element, the agreement, for two reasons. First, it is the more difficult element to prove,[27] and second, once proven, the requisite purpose becomes essentially self-evident.[28] A section 13(d) plaintiff has the burden

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previously independent shareholders each owning two percent. In each instance a new block of securities exceeding the critical size has become subject to a common control and direction.

Comment, *supra* note 19, at 866; *see supra* note 17.

22. H.R. REP. No. 1711, *supra* note 12, at 6–7, *reprinted in* 1968 U.S. CODE CONG. & AD. NEWS at 2818. The report also indicates that § 13(d)(3)

> would prevent a group of persons who seek to pool their voting or other interests in the securities of an issuer from evading the provisions of the statute because no one individual owns more than [5] percent of the securities. The group would be deemed to have become the beneficial owner . . . at the time they agreed to act in concert.

Id. One cannot be a member of a § 13(d)(3) group, moreover, without being a beneficial owner of some shares of the subject company. Transcon Lines v. A.G. Becker, Inc., 470 F. Supp. 356, 373 (S.D.N.Y. 1979).

23. Securities Exchange Act of 1934, § 13(d)(3), 15 U.S.C. § 78m(d)(3) (1976).

24. *See supra* note 18.

25. *See* Mid-Continent Bancshares, Inc. v. O'Brien, [Current Binder] FED. SEC. L. REP. (CCH) ¶ 98,734 (E.D. Mo. 1981) (individuals who agreed to buy stock in a target company through a common representative constituted a "group" under section 13(d)(3)).

26. *See* Wellman v. Dickinson, [Current Binder] FED. SEC. L. REP. (CCH) ¶ 98,731 (2d Cir. 1982) (five shareholders who agreed to dispose of their stock so as to aid a third party in gaining corporate control were a "group" under section 13(d)(3)).

27. *See infra* notes 35–72 and accompanying text.

28. The court in SEC v. Savoy Indus., 587 F.2d 1149 (D.C. Cir. 1978) described its

of proof to a preponderance that a group was formed. Since direct proof is almost always lacking, circumstantial evidence is used to infer an agreement. The case law interpreting section 13(d) suggests the use of a rebuttable presumption to establish the existence of an agreement. Such a presumption is raised when three factors are present: (1) communication among defendants, (2) a common objective, and (3) acts in furtherance of that objective. The absence of any one of these factors precludes the establishment of the presumption.

A. *The Elements of Group Formation*

The sine qua non of section 13(d)(3) is the *agreement* of two or more persons to act as a group.[29] While the statute does not expressly require it, "the fact that the [legislative history] speaks of those 'who seek to pool . . . their interests,' and of those who 'agree[d] to act in concert,' strongly implies that some type of combination toward concerted action is necessary."[30] The courts of appeals have held uniformly that absent an agreement between the defendants, a group does not exist.[31]

Additionally, the group must have a *purpose* to acquire, hold, or dispose of securities.[32] While this language seems unambiguous, early decisions gave conflicting interpretations of the "purpose" requirement.[33] In *Bath Industries v. Blot*,[34] for example, the Seventh Circuit Court of Appeals interpreted section 13(d)(3) to require that the agreement to act in concert be for the purpose of

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task of searching for the purpose to be "to sift through the record to determine whether there is sufficient direct or circumstantial evidence to support the inference of a formal or informal agreement or understanding." *Id.* at 1163.

29. *See* SEC v. Savoy Indus., 587 F.2d 1149, 1162–63 (D.C. Cir. 1978), *cert. denied*, 440 U.S. 913 (1979); Corenco Corp. v. Schiavone & Sons, Inc., 488 F.2d 207, 217 (2d Cir. 1973); GAF Corp. v. Milstein, 453 F.2d 709, 718 (2d Cir. 1971), *cert. denied*, 406 U.S. 910 (1972); Texasgulf, Inc. v. Canada Dev. Corp., 366 F. Supp. 374, 403 (S.D. Tex. 1973).

30. SEC v. Savoy Indus., 587 F.2d 1149, 1163 (D.C. Cir. 1978) (citing H.R. REP. NO. 1711, *supra* note 12, at 8–9, *reprinted in* 1968 U.S. CODE CONG. & AD. NEWS at 2818).

31. SEC v. Savoy Indus., 587 F.2d 1149, 1162–63 (D.C. Cir. 1978); General Aircraft Corp. v. Lampert, 556 F.2d 90, 95 (1st Cir. 1977); Corenco Corp. v. Schiavone & Sons, Inc., 488 F.2d 207, 217 (2d Cir. 1973); GAF Corp. v. Milstein, 453 F.2d 709, 718 (2d Cir. 1971); Bath Indus. v. Blot, 427 F.2d 97, 109 (7th Cir. 1970).

32. *See supra* note 23 and accompanying text.

33. One commentator explained the confusion as resulting from "the normal evidentiary problems associated with the search for a 'purpose' . . . compounded by the difficulty involved in reading this definition into section 13(d)(1) . . . ." Comment, *supra* note 19, at 857.

34. 427 F.2d 97 (7th Cir. 1970).

acquiring *additional* shares of stock.[35] Shortly thereafter, however, in *GAF Corp. v. Milstein*,[36] the Second Circuit Court of Appeals held that individuals agreeing to acquire control over a corporation who collectively possess the threshold level of securities need not acquire additional shares to be subject to the section 13(d) disclosure requirements.[37] The Second Circuit's position is consistent with the legislative history[38] and has since been incorporated into the rules accompanying section 13(d).[39]

B. *Evidentiary Characteristics*

The courts have uniformly held that the party claiming that a section 13(d) group was formed has the burden of proving it.[40] This burden is met when a fair preponderance of the evidence establishes that the alleged members of the group agreed to act in concert with respect to the shares held or acquired by them.[41] No affirmative action in furtherance of the agreement need be shown.[42]

Although existence of an agreement may be established by direct evidence, such proof is not usually available. As the court in *Bath Industries v. Blot* stated, "[a]part from the unlikely execution of a formal agreement by a group . . . proof of . . . an agreement would be difficult for anyone not privy to the group's plan."[43] Therefore, the courts have allowed the existence of a group to be

35. *Id.* at 109.

36. 453 F.2d 709 (2d Cir. 1971), *cert. denied*, 406 U.S. 910 (1972).

37. *Id.* at 716.

38. "[T]he group would be required to file . . . within 10 days after they agree to act together, whether or not any member of the group had acquired any securities at that time . . . ." H.R. REP. No. 1711, *supra* note 12, at 9, *reprinted in* 1968 U.S. CODE CONG. & AD. NEWS at 2818.

39. SEC Rule 13d-5(b)(1), for instance, states in part that "[w]hen two or more persons agree to act together for the purpose of acquiring, holding, voting or disposing of equity securities . . . the group formed thereby shall be deemed to have acquired beneficial ownership . . . *as of the date of such agreement*, of all equity securities . . . owned by any such persons." 17 C.F.R. § 240.13d-5(b)(1) (1982) (emphasis added).

40. *See, e.g.*, GAF Corp. v. Milstein, 453 F.2d 709, 718 (2d Cir. 1971), *cert. denied*, 406 U.S. 910 (1972); Financial Gen. Bankshares, Inc. v. Lance, [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,403, at 93,425 (D.D.C.); Jewelcor Inc. v. Pearlman, 397 F. Supp. 221, 250 (S.D.N.Y. 1975). As one commentator emphasizes, "[t]he practical difficulty of determining when a group was formed [has been eased] by treating the issue as a problem of proof for the plaintiff, and not to be disposed of on preliminary motions." Stanton, *Acquisition By a Group*, 5 REV. SEC. REG. 985, 986 (1972).

41. *See* GAF Corp. v. Milstein, 453 F.2d 709, 718 (2d Cir. 1971), *cert. denied*, 406 U.S. 910 (1972); Jewelcor Inc. v. Pearlman, 397 F. Supp. 221, 250 (S.D.N.Y. 1975).

42. Jewelcor Inc. v. Pearlman, 397 F. Supp. 221, 250 (S.D.N.Y. 1975).

43. 427 F.2d 97, 110 (7th Cir. 1970).

demonstrated by circumstantial evidence of an agreement.[44]

The courts have struggled to determine what circumstantial evidence effectively demonstrates the existence of an agreement, since the concept resists precise definition. This Note will examine those cases which have attempted to interpret the agreement requirement of section 13(d)(3) in an attempt to extract a functional definition of that requirement.[45]

The legislative history indicates that a group may be formed by "any contract, understanding, relationship, agreement or other arrangement."[46] This all-embracing language indicates that the concerted action need not be formalized or express.[47] As one court noted, the statute "was intended to extend beyond agreements and contracts in the classical 'offer' and 'acceptance' sense."[48]

Thus, while the existence of an agreement must unquestionably be established, the expansive interpretation of the form that an agreement may take prevents the exaltation of form over substance, thereby promoting the investor protection purpose of the statute.[49]

C. *Inferring an Agreement from Circumstantial Evidence*

Group formation is best conceived of as a linear continuum, with point zero denoting the precise moment that the "agreement" comes into existence. The negative side of zero represents activities which alone do not give rise to an agreement, while the positive side represents activities in furtherance of the agreement. The courts have treated the actual moment of entering into an agreement as an abstraction that serves only as a point of reference as to the start of the statutory ten day period.[50] Because the instant

44. *See, e.g.*, SEC v. Savoy Indus., 587 F.2d 1149, 1162 (D.C. Cir. 1978).

45. *See infra* notes 52–70 and accompanying text.

46. H.R. REP. No. 1711, *supra* note 12, at 9, *reprinted in* 1968 U.S. CODE CONG. & AD. NEWS at 2818.

47. "A written agreement, of course, is not necessary to the formation of the group. Such a requirement could render nugatory the purpose of the statute . . . ." Water & Wall Assoc., Inc. v. American Consumer Indus., [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 93,943, at 93,756 (D.N.J.); *see also* Twin Fair, Inc. v. Reger, 394 F. Supp. 156, 160 (W.D.N.Y. 1975) (defendant and corporations under his control held to constitute a group upon defendant's instructions that the corporations purchase stock).

48. SEC v. Savoy Indus., 587 F.2d 1149, 1163 (D.C. Cir. 1978).

49. *Id.*

50. In response to the district judge's statement that "[t]he inherent difficulty of ascertaining when a group was formed is akin to an attempt to grasp quicksilver," GAF Corp. v. Milstein, 324 F. Supp. 1062, 1068 (S.D.N.Y. 1971), the Court of Appeals for the Second

of agreement is practically incapable of precise resolution, the critical inquiry is on which side of the zero point the defendants'[51] activities fall.

1. *Preliminary Activities*

While recognizing that section 13(d)'s investor protection purpose supports its liberal construction,[52] the courts have permitted individuals to engage in certain associational activity without triggering group formation. In discussing the range of permissible activity, the court in *Lane Bryant, Inc. v. Hatleigh Corp.*[53] stated:

> Section 13(d) seems carefully drawn to permit parties seeking to acquire large amounts of shares in a public company to obtain information with relative freedom, to discuss preliminarily the possibility of entering into agreements and to operate with relative freedom *until they get to the point where they do in fact decide to make arrangements* which they must record under the securities laws. By requiring the existence of a "group", the law is designed to avoid discouraging and making risky that kind of preliminary activity.[54]

Consequently, such activities as a mere relationship among persons or entities;[55] meetings, conferences, and telephone calls;[56] and securities transactions[57] do not, of themselves, constitute an agreement. These "preliminary" activities, however, may support the inference of an agreement when found in conjunction with other probative evidence.[58]

Circuit responded that "any difficulty in pinpointing the precise date, as distinguished from an approximate time, when the conspiracy was formed and the group became subject to section 13(d) can be one of the elements considered by the district judge in fashioning appropriate equitable relief." GAF Corp. v. Milstein, 453 F.2d 709, 718–19 (2d Cir. 1971), *rev'g* 324 F. Supp. 1062 (S.D.N.Y.), *cert. denied,* 406 U.S. 901 (1972).

51. The term "defendant" is used in this Note to indicate any alleged group members. While such individuals are not always the defendants in section 13(d)(3) litigation, the consistent use of one term promotes clarity.

52. *See, e.g.*, Financial Gen. Bankshares, Inc. v. Lance, [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,403, at 93,424 (D.D.C.).

53. [1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,529 (S.D.N.Y.).

54. *Id.* at 97,766 (emphasis added).

55. *See, e.g.*, Texasgulf, Inc. v. Canada Dev. Corp., 366 F. Supp. 374, 403 (S.D. Tex. 1973).

56. *See, e.g.*, Scott v. Multi-Amp Corp., 386 F. Supp. 44, 72 (D.N.J. 1974).

57. *See, e.g.*, Sisak v. Wings and Wheels Express, Inc., [1970–1971 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 92,991, at 90,670 (S.D.N.Y. 1970). The court further noted that "the notion of a group does not comfortably embrace both buyer and seller . . . at least where the sole aspect of the transaction is to sell all of the securities of one party to another . . . ." *Id.*

58. *See infra* notes 61–83 and accompanying text.

2. *Raising the Presumption*

While allowing the existence of an agreement to be proven circumstantially eases the plaintiff's burden, other problems are created. The court's task becomes more difficult because circumstantial evidence introduces an element of uncertainty into the determination of whether an agreement has been reached that would not be present using only direct evidence. Decisions based on circumstantial evidence also provide a confusing and complex standard against which persons whose activities approach group formation must measure their behavior. Thus, even persons who might ultimately be considered to be engaging in "preliminary activities" are faced with the dilemma of filing a possibly unnecessary Schedule 13D statement or risking potential liability for noncompliance. This result is clearly contrary to the expressed legislative intent to favor neither management nor the persons making takeover bids, since a premature filing due to uncertainty would provide management with information that Congress has deemed it does not yet deserve.[59] Thus, whereas restricting plaintiffs to the presentation of direct evidence would too easily allow persons to avoid the filing requirements of section 13(d), the greater uncertainty associated with circumstantial evidence gives the statute a broader impact than was originally intended.[60]

The adoption of a clearly defined rebuttable presumption, the establishment of which would raise the inference of an agreement, would ameliorate this situation. Such a presumption not only would foster more uniform judicial decisions by providing a functional definition of the term "agreement," but also would promote

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59. *See infra* text accompanying notes 114–16. In Financial Gen. Bankshares, Inc. v. Lance, [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,403 (D.D.C.), the district court noted:

> [Section 13(d)] should be construed liberally to ensure that its investor protection purpose is given full effect. *The Court must take care, however, to see that Section 13(d) is not transformed into a "weapon for management to discourage takeover bids or prevent large accumulations of stock which would create the potential for such attempts."*

Id. at 93,424–25 (emphasis added) (quoting Rondeau v. Mosinee Paper Corp., 422 U.S. 49, 58 (1975)). This interest in preventing premature disclosure of information was also discussed in Lane Bryant, Inc. v. Hatleigh Corp., [1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,529 (S.D.N.Y.), where the court observed that "the decisions indicate [that] substantial interests exist . . . in not requiring—indeed, to an extent even frowning upon—disclosure of non-concretized plans." *Id.* at 97,768.

Section 13(d)(1) requires that a Schedule 13D statement be sent to "the issuer of the security at its principal executive office . . . ." 15 U.S.C. § 78m(d)(1) (1976 & Supp. IV 1980).

60. *See supra* notes 43–49, 52–58 and accompanying text.

greater statutory compliance by enabling potential defendants to determine when they have triggered the section 13(d) filing requirements. The Seventh Circuit enunciated such a presumption in *Bath Industries v. Blot*,[61] stating that a rebuttable presumption that alleged group members have acted pursuant to an agreement is raised once it is demonstrated that they had communicated a common objective and that their subsequent activities had furthered that objective.[62] Although no subsequent case has applied the *Bath* test as an express presumption, the decisions reveal that the existence of an agreement is established once the plaintiff proves the following elements: (1) communication, (2) a common objective that the aggregation of securities would facilitate, and (3) acts in furtherance of the objective. Thus, while the *Bath* holding has been disputed in part,[63] the presumption it formulated remains generally applicable. The confusion presently associated with group formation could be effectively eliminated by expressly adopting the presumption which the courts already (but not explicitly) have been applying.

The presumption itself is a logical one. While proof of all three elements provides a sufficient factual basis for implying an agreement, proof of each element is necessary. Communication among the alleged group members is the presumption's most basic element. Such communication is required in the circumstantial proof of a section 13(d)(3) agreement because inherent within the concept of any agreement is that the parties to it collectively express an intent to act in concert. That the defendants communicated with each other establishes their opportunity to have entered into an agreement.

The essential element of the presumption is that the defendants share an objective that the aggregation of securities would facilitate. A desire to affect corporate control is the objective from which an agreement is most frequently inferred,[64] since the primary value of combining securities ownership is the accumulation

61. 427 F.2d 97 (7th Cir. 1970).

62. *Id.* at 110.

63. *See supra* notes 33-39 and accompanying text.

64. *See, e.g.*, Wellman v. Dickinson, [Current Binder] FED. SEC. L. REP. (CCH) ¶ 98,731 (2d Cir. 1982); General Aircraft Corp. v. Lampert, 556 F.2d 90 (1st Cir. 1977); GAF Corp. v. Milstein, 453 F.2d 709 (2d Cir. 1971); Bath Indus. v. Blot, 427 F.2d 97 (7th Cir. 1970); Financial Gen. Bankshares, Inc. v. Lance, [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,403 (D.D.C.). *But see* Nicholson File Co. v. H.K. Porter Co., 341 F. Supp. 508 (D.R.I. 1972) (holding that group formation for a common purpose, not intent to acquire control, invokes § 13(d)).

of voting power.[65] When considered in light of such an objective, the defendants' otherwise random activities are transformed into an orderly progression of agreement-related behavior. While proving the elements of communication and common objective establishes the opportunity and rationale for an alleged agreement, demonstrating that the defendants furthered their common objective establishes that they have acted as if they had in fact entered into an agreement.[66] The presumption thus shifts the burden of proof to the defendants, while promoting the policy of allowing pre-agreement discussions[67] without unfairly favoring management.[68]

The following two cases illustrate the operation of the presumption. In *General Aircraft Corp. v. Lampert*,[69] the issue was whether the three individual defendants constituted a "group" when they first acquired stock in the plaintiff-corporation.[70] Although the shares were acquired simultaneously in almost identical transactions,[71] and two of the defendants held their shares in one name,[72] these facts, considered alone, probably would not have manifested a section 13(d)(3) agreement. The defendants,

65. As one court observed, "where the principal concern is focused on the battle for corporate control, 'voting control of stock is the only relevant element of beneficial ownership.'" GAF Corp. v. Milstein, 453 F.2d 709, 716 (quoting Bath Indus. v. Blot, 427 F.2d 97, 112 (7th Cir. 1970)).

66. Curiously, the plaintiff, in sustaining its burden of proving a group formation, need not show that the defendants took any affirmative steps in furtherance of their agreement. *See supra* notes 40–42 and accompanying text. The plaintiff must, however, show that the defendants acted in furtherance of their agreement as part of sustaining the presumption which infers its existence. The agreement, together with the purpose to acquire, hold, or dispose of securities, constitutes the "group" defined in section 13(d)(3). *See supra* notes 27–39 and accompanying text. This apparent contradiction is resolved by observing that the burden of proof defines the elements that a particular party must show to establish liability against a defendant. The agreement itself invokes section 13(d). The presumption, by comparison, is simply a judicially created method to assemble circumstantial evidence in a probative fashion where, as here, direct evidence is usually lacking. As a practical necessity, acts in furtherance of a common objective are used to relate back to the creation of an agreement at an earlier time, which, but for the later acts, would not be evidenced by sufficient facts to sustain the burden of proof. The distinction is clearest in a case involving only direct evidence of an agreement. The burden of proof would be sustained by showing a formal, contractual agreement. Moreover, since the evidence of the agreement would be sufficiently manifest from the written document, it would be unnecessary to show acts pursuant to that agreement to create a presumption of its existence.

67. *See supra* notes 53–54 and accompanying text.

68. *See supra* note 59 and accompanying text.

69. 556 F.2d 90 (1st Cir. 1977).

70. The stock acquisitions constituted more than 12% of the plaintiff's outstanding common shares. *Id.* at 92.

71. *Id.* at 95.

72. *Id.* at 92.

however, made additional stock acquisitions and sometime thereafter (approximately three months after the initial acquisitions) filed a Schedule 13D on behalf of all three defendants. While the schedule stated that the transactions were solely for investment purposes, the defendants' subsequent actions revealed an additional objective: for the next year and a half the defendants clashed with the corporation's management,[73] using threats to solicit proxies as leverage to obtain board positions.[74] Furthermore, copies of correspondence between the corporation and any one defendant were sent to the other two.[75] The identical nature of the transactions and the jointly-held stock by two defendants implied that the defendants had discussed these matters before the acquisitions. Moreover, the defendants' repeated proxy threats revealed a common objective to gain corporate control, and the defendants' subsequent actions could reasonably be interpreted as furthering that objective. Thus, the necessary elements of the presumption were established. Accordingly, the First Circuit held that the defendants had acted as a "group" at the time of their first stock acquisition.[76]

In another case, *SEC v. Savoy Industries*,[77] the District of Columbia Circuit Court of Appeals examined whether the individual defendant was part of a section 13(d)(3) group although not mentioned in its Schedule 13D statement. As a shareholder in a life insurance corporation, the defendant hoped to benefit from the purchase of such corporation by Savoy (the issuing corporation)[78] and met with the members of the group to discuss the purchase of Savoy stock.[79] The group members later individually purchased Savoy stock and filed a Schedule 13D statement indicating the group's intention to direct Savoy toward the life insurance busi-

73. *Id.*

74. *Id.* at 92–93.

75. *Id.* at 95.

76. *Id.* Recall the concept of the continuum for group formation described at *supra* notes 50–51 and accompanying text. This case illustrates the conceptual difficulty of trying to determine when in the past an agreement was made and the method by which the courts use circumstantial evidence to relate back to that prior event. Point zero, as the court held in this case, was the date of the first stock purchase; yet, the facts known at that time were insufficient to raise an inference of an agreement. It was only possible to pinpoint the agreement date by reference to the later acts of the defendants, or, in other words, to the positive side of zero.

77. 587 F.2d 1149 (D.C. Cir. 1978), *cert. denied*, 440 U.S. 913 (1979).

78. SEC v. Zimmerman, 407 F. Supp. 623, 627 (D.D.C. 1976), *aff'd in part and vacated in part on other grounds sub nom.* SEC v. Savoy Indus., 587 F.2d 1149 (D.C. Cir. 1978), *cert. denied*, 440 U.S. 913 (1979).

79. *Id.*

ness.[80] Although the defendant did not purchase securities at this time, he did participate in discussions which led to a complete overhaul of Savoy's leadership.[81] In fact, he knew the new president and all the new directors.[82] Thus, the defendant was found to have shared the group's objective to affect control of Savoy and direct the corporation toward the life insurance business. Also, the defendant's participation in meetings with group members before and after their stock purchases acted to further the common objective. The court held that the evidence supported the inference of an agreement and that the defendant should have been included in the Schedule 13D statement.[83]

3. *Rebutting the Presumption*

The presumption which raised the inference of an agreement in the preceding cases will fail unless all three of its elements are established.[84] In *National Home Products, Inc. v. Gray*,[85] a group was formed to seek control of the issuing corporation. The defendant had expressed dissatisfaction with her investment in the corporation to a member of the group.[86] She also received advice from a second member of the group and transferred 10,000 shares to a third.[87] By these acts, the defendant certainly communicated with the group members and may have facilitated their objective by transferring the shares. The presumption's key element was lacking, however, since the evidence failed to indicate that the defendant shared the group's common objective. The court held that the defendant's activities were insufficient to make her a "group" member.[88]

Additionally, the presumption may be rebutted by an affirmative demonstration that the defendants acted inharmoniously. In *Cook United, Inc. v. "Stockholders Protective Committee of Cook United, Inc.*,"[89] several shareholders held a meeting to discuss conducting a proxy contest for control of the issuing corporation.

80. 587 F.2d at 1164.

81. *Id.*

82. SEC v. Zimmerman, 407 F. Supp. at 628.

83. 587 F.2d at 1165.

84. *See infra* notes 85-92 and accompanying text.

85. 416 F. Supp. 1293 (D. Del. 1976).

86. *Id.* at 1323.

87. *Id.*

88. *Id. See also* Camelot Indus. Corp. v. Vista Resources, Inc. [Current Binder] FED. SEC. L. REP. (CCH) ¶ 98,611, at 93,005 (S.D.N.Y. 1982) (holding that lack of common purpose precluded the finding of a § 13(d)(3) group).

89. [1979 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,875 (S.D.N.Y.).

Although most expressed an interest in waging such a contest, the court held that a "group" was not formed at this meeting because some shareholders were indecisive about participating, and some never joined the effort.[90] In *Lane Bryant, Inc. v. Hatleigh Corp.*,[91] the court similarly held that an agreement was not formed. Although the defendants had discussed combining forces for the purpose of gaining corporate control, one faction expressed that it did not want to make a deal, preferring to proceed on its own.[92]

III. MANAGEMENT GROUPS

A collateral issue to that of "group" formation is whether Section 13(d)(3) applies to groups composed of members of a firm's management personnel.[93] Early cases answered this question in the negative.[94] More recent cases, however, have limited the early decisions to their particular facts and have held, with some exceptions, that the term "group" does encompass members of a firm's management.[95]

The two groundbreaking section 13(d) decisions—*Bath Industries v. Blot*[96] and *GAF Corp. v. Milstein*[97]—both mentioned the issue of management groups in dicta. In *Bath*, the Seventh Circuit stated that in enacting section 13(d) Congress was seeking to protect individual investors "when substantial shareholders *or management* undertake to acquire shares in a corporation for the purpose of solidifying their own position . . . ."[98] In *GAF*, the Second Circuit noted that while it would be unusual for management to form groups for the purpose of acquiring, holding, or disposing of their own securities, if such a group were formed the filing requirements of section 13(d) would apply.[99]

Approximately two years after deciding *GAF*, the Second Circuit faced the same issue in *Corenco Corp. v. Schiavone & Sons,*

90. *Id.* at 95,578.

91. [1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,529 (S.D.N.Y.).

92. *Id.* at 97,766.

93. *See generally* E. ARANOW, H. EINHORN & G. BERLSTEIN, DEVELOPMENTS IN TENDER OFFERS FOR CORPORATE CONTROL 42–48 (1977) [hereinafter cited as E. ARANOW]; Block & Schwarzfeld, *Management Groups Under the Williams Act*, 5 SEC. REG. L.J. 69 (1977).

94. *See infra* notes 98–104 and accompanying text.

95. *See infra* notes 105–11 and accompanying text.

96. 427 F.2d 97 (7th Cir. 1970).

97. 453 F.2d 709 (2d Cir. 1971), *cert. denied*, 406 U.S. 910 (1972).

98. 427 F.2d at 109 (emphasis added).

99. 453 F.2d at 719.

Inc.,[100] where the management of Corenco attempted to defeat a tender offer. The court held that the members of management were not required to file a Schedule 13D statement for agreeing to pool their interests to fight the threatened take over. It further noted that:

> [s]ection 14(d)(4) of the Exchange Act specifically requires the disclosure of certain information when the management of a company advises its shareholders to reject a tender offer . . . . Since the Exchange Act contains a specific provision governing the disclosures required of a target company's management, it would be pointless to superimpose requirements found in another section, which does not deal specifically with management disclosures.[101]

The next case to address the issue was *Scott v. Multi-Amp Corp.*[102] The plaintiff in *Scott* alleged that management attempted to obtain shareholder approval to sell the corporation's assets and liquidate the company.[103] Consistent with *Corenco*, the court concluded that section 13(d) did not apply to management groups.[104]

The trend against the application of section 13(d) to management groups was slowed in *Jewelcor Inc. v. Pearlman*,[105] which involved a group comprising both management and nonmanagement persons. The court first distinguished *Corenco* and *Scott*, since those cases involved groups consisting entirely of management personnel.[106] The court further distinguished *Corenco* by noting that a tender offer had been involved in that case and held that "where there has been no tender offer . . . § 13(d) should apply to management groups, especially management groups including nonmanagement members."[107] In support of its decision, the court cited *Tony Lama Co.*[108] an SEC staff opinion indicating that section 13(d) applied to management groups and "[was] not satisfied by disclosure made apart from the required filing, and [might] not be waived."[109] In dicta, the *Jewelcor* court further stated that "even if the alleged . . . directors' group were to con-

100. 488 F.2d 207 (2d Cir. 1973).
101. *Id.*
102. 386 F. Supp. 44 (D.N.J. 1974).
103. *Id.* at 52.
104. *Id.* at 62.
105. 397 F. Supp. 221 (S.D.N.Y. 1975).
106. *Id.* at 243.
107. *Id.* at 244.
108. [1974–1975 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 79,901 (1974).
109. *Id.* at 84,311.

sist only of management personnel, that group still would have been required to file a Schedule 13D."[110]

The most recent case to decide the issue, *Podesta v. Calumet Industries, Inc.*,[111] is also the most adamant about the application of section 13(d) to management groups. Unlike *Jewelcor*, *Podesta* involved a group composed entirely of management personnel. The evidence demonstrated that members of management had "agreed to acquire shares as part of their desperate efforts to retain control."[112] Citing *Bath* and *Tony Lama*, the court held that "at least in a case such as this, where no outside tender offer is involved, management groups are subject to the requirements of Section 13(d)."[113]

The application of section 13(d) to management groups is further supported by the legislative history of the Williams Act. It was stated that "extreme care [was taken] to avoid tipping the scales either in favor of management or in favor of the person making takeover bids"[114] and that *any* person or group that acquires "substantial blocks of the securities of publicly held companies"[115] is subject to the disclosure requirements. Moreover, the language of section 13(d)(3) makes no distinction between management and nonmanagement groups, and there would appear to be no valid reason to make such a distinction since members of management must individually comply with section 13(d).[116]

IV. CONCLUSION

Except for the rare case in which direct evidence is available, the party alleging that a "group" violated section 13(d) of the Securities Exchange Act of 1934 by failing to meet its filing requirements must prove, by circumstantial evidence, that the alleged group members agreed to act in concert.[117] Although the courts have failed to articulate a precise definition of "agreement," close analysis of the cases reveals an underlying presumption, the ele-

110. 397 F. Supp. at 244.

111. [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,433 (N.D. Ill.); *see* Bayly Corp. v. Marantette, [1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,834 at 94,292 (alternative holding without discussion, citing *Podesta*).

112. *Id.* at 93,559.

113. *Id.* at 93,560.

114. 113 CONG. REC. 24,664 (1967).

115. *Id.*

116. *See* E. ARANOW, *supra* note 93, at 46–47.

117. *See supra* notes 40–45 and accompanying text.

ments of which provide a functional definition of the term.[118] For purposes of section 13(d)(3), persons who (1) communicate with one another, (2) demonstrate a common objective respecting securities, and (3) act in a manner consistent with the furtherance of that objective will be deemed to have "agreed to act in concert" and thereby constitute a "group."[119] The usefulness of this presumption, both to foster more uniform judicial opinions and to promote greater statutory compliance by placing potential defendants on notice that their activities might constitute "group" behavior, depends upon its express adoption by courts. Though all the existing section 13(d)(3) cases are arguably reconcilable with the presumption,[120] most[121] courts have failed to explicitly recognize its existence.[122]

Finally, recent decisions indicate that groups consisting of management personnel are covered by the scope of section 13(d)(3) and, therefore, are responsible for meeting its filing requirements.[123] Support for these decisions is found in the legislative intent of the Williams Act to favor neither management nor those making takeover bids[124] and in the fact that the language of section 13(d)(3) makes no distinction between management and nonmanagement groups. The exemption of management groups in situations involving tender offers that remains from the early cases should, therefore, be eliminated.[125]

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118. *See supra* notes 59–83 and accompanying text.

119. *See supra* notes 61–65 and accompanying text.

120. *See supra* notes 59–63 and accompanying text.

121. Bath Indus. v. Blot, 497 F.2d 97, 110 (7th Cir. 1970) is the exception. *See supra* text accompanying notes 61–63.

122. *See supra* notes 59–63 and accompanying text.

123. *See supra* notes 105-13 and accompanying text.

124. *See supra* notes 114-16 and accompanying text.

125. *See supra* notes 93-113 and accompanying text.