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Securities Acts - Antifraud Provisions - Pension Plans - Sale of Security

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SECURITIES ACTS—ANTIFRAUD PROVISIONS—PENSION PLANS—SALE OF SECURITY—The United States District Court for the Northern District of Illinois has held that an employee's acquisition of an interest in a union's collectively bargained, defined-benefit pension plan, which was both involuntary and noncontributory, involved the sale of a security subject to the antifraud provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934.

Daniel v. International Brotherhood of Teamsters, 410 F. Supp. 541 (N.D. Ill. 1976).

Before plaintiff, John Daniel, was hired, the defendant union had established and collectively bargained for employer contributions to the union's involuntary, noncontributory, defined-benefit pension plan.[1] Daniel became a participant in the plan in 1950.[2] In 1955, the union adopted a rule, ratified by its members, requiring twenty years of uninterrupted employment with employer sponsors in order to receive any pension benefits. This eligibility requirement was communicated to Daniel in the same year.[3] Daniel worked for plan sponsors for twenty-two and one-half years with the exception of his being laid off for several months in 1960. In 1973, he retired and applied for a pension benefit. The plan's trustees rejected his application; his 1960 lay-off prevented him from accruing twenty years of uninterrupted employment.

The plaintiff filed a class action against the union and the trus-

1. The plan in which Daniel later acquired an interest was maintained by several employers pursuant to a collective bargaining agreement with the union. A union member's employment with any of the several employers contributing to the union's plan would make the employee a participant in the plan. Daniel v. International Bhd. of Teamsters, 410 F. Supp. 541, 543 (N.D. Ill. 1976).

2. The plan was funded solely by the employers' contributions. Members of the local union came under the plan automatically by reason of their union membership and employment with a contributing employer. The plan provided a fixed benefit to retiring employees. *Id.* at 551-52.

3. In 1958 and later in 1969, relevant information about the plan was compiled in booklet form and sent to all plan participants. The plaintiff allegedly received these booklets. From 1959, a copy of the trust agreement was available for inspection in the local union office, and, upon request, would be sent to a participant. In 1971, letters were allegedly sent to all participants, including the plaintiff, outlining the eligibility requirements. *Id.* at 544. In the court's view, a factual issue existed as to whether, in light of the plaintiff's eighth grade education and claimed difficulty in understanding the intricacies of the plan, the defendants' disclosures of the break-in-service rules which were couched in technical language adequately informed the plaintiff of all material facts. *Id.* at 545.

tees seeking relief under the Securities Act of 1933[4] and the Securities Exchange Act of 1934[5] (Securities Acts) based on the Acts' antifraud provisions.[6] He alleged that his participation in the pension plan created an interest involving the sale of a security within the meaning of the Securities Acts.[7] Daniel claimed damages resulting from the defendants' misleading statements and omissions of material facts regarding the length and continuity-of-service requirements.[8] The defendants moved to dismiss the complaint on alternative grounds. They argued that pension plans were controlled by other federal legislation,[9] and that this particular plan involved neither a security nor a sale—the Securities Acts' nexus requirements.[10] The court denied the defendants' motions to dismiss, and held that the complaint did allege a violation of the antifraud provisions of the Securities Acts in connection with the acquisition of the pension plan interest.[11]

4. 15 U.S.C. §§ 77a-77aa (1970) [hereinafter referred to as Securities Act of 1933].

5. 15 U.S.C. §§ 78a-78jj (1970) [hereinafter referred to as Securities Exchange Act of 1934].

6. The Securities Acts make it unlawful for any person, in the offer or sale of any securities by the use of interstate commerce or the mails, to employ any scheme to defraud, to obtain money by misrepresenting a material fact or failing to disclose a material fact, or to engage in any transaction which would operate to defraud or deceive a purchaser. *See* 15 U.S.C. § 77q(a) (1970); *id.* § 78j(b) (1970). *See also* rule 10b-5, 17 C.F.R. § 240.10B-5 (1976).

7. The plaintiff also alleged that the continuous service rules under the plan were not for the sole and exclusive benefit of employees and therefore violated § 302(c)(5) of the Labor Management Relations Act, 29 U.S.C. § 186(c)(5) (1970). 410 F. Supp. at 554-55.

8. *Id.* at 545-46.

9. The defendants claimed that the comprehensive regulatory scheme and legislative history of the Employee Retirement Income Security Act of 1974, 29 U.S.C. §§ 1001-1381 (Supp. 1974), and the Welfare and Pension Plans Disclosure Act, Pub. L. No. 85-836, §§ 2-12, 72 Stat. 997 (1958) (repealed in 1975), preempted the Securities Acts to the extent they regulated such pension plans. 410 F. Supp. at 546-49. *See* notes 15-17 and 34-40 and accompanying text *infra.*

10. *See* note 6 *supra.*

11. In order to uphold the plaintiff's claim, the court had to conclude that a private cause of action existed under § 17(a) of the Securities Act of 1933, 15 U.S.C. § 77q(a) (1970). 410 F. Supp. at 546-47. The Supreme Court has specifically declined to rule on this question. *See* Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 734 n.6 (1975). Other lower courts do not agree with the *Daniel* court that such a private right of action exists under § 17(a). *See, e.g.*, Reid v. Mann, 381 F. Supp. 525 (N.D. Ill. 1974); Welch Foods Inc. v. Goldman, Sachs & Co., 398 F. Supp. 1393, 1399-1401 (S.D.N.Y. 1974) (§ 17(a) implies no private cause of action). *But cf.* Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976). The Supreme Court acknowledged the existence of a private cause of action under § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78(b) (1970), which is by rule similar to § 17(a) of the Securities Act of 1933.

The first issue the court addresed was whether the Securities Acts by their own terms are applicable to employee pension plans. Judge Kirkland relied heavily on the Securities and Exchange Commission's (SEC) interpretation of Congress' rejection in 1934 of proposed amendments to the Securities Act of 1933,[12] amendments which would have exempted from registration certain securities sold in connection with employee plans. He agreed with the SEC that the rejection was indicative of Congress' intent that the Securities Acts be applied to such plans.[13] Furthermore, Congress had specifically recognized pension funds as securities when it exempted interests in certain types of pension funds from the registration requirements of the Securities Acts.[14] The court was also convinced that specialized pension legislation, the Welfare and Pension Plans Disclosure Act of 1958 (WPPDA)[15] and the Employee Retirement Income Security Act of 1974 (ERISA),[16] did not preempt the pension field. ERISA and WPPDA were enacted to regulate the ongoing administration of pension plans rather than the entry into such pension plans; the latter activity was covered by the Securities Acts. In the court's view, the specialized pension legislation complemented the securities laws and both could be given effect.[17]

Turning to the issue of whether a sale of a security had occurred,[18]

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12. *See* note 30 *infra*.

13. 410 F. Supp. at 547.

14. Section 3(a)(2) of the Securities Act of 1933 requires no registration for the sale of certain exempted securites defined in part as:

> [A]ny interest or participation in a single or collective trust fund maintained by a bank or . . . insurance company . . . issued in connection with . . . [a qualified] . . . pension, or profit-sharing plan . . . other than any plan . . . under which an amount in excess of the employer's contribution is allocated to the purchase of securities (other than interests or paticipations in the trust or separate account itself) issued by the employer . . . .

15 U.S.C. § 77c(2) (1970). Section 3(a)(12) of the Securities Exchange Act of 1934, 15 U.S.C. § 78(c)(12) (1970), contains a similar provision.

15. Pub. L. No. 85-836, §§ 2-12, 72 Stat. 997 (1958) (repealed in 1975).

16. 29 U.S.C. §§ 1001-1381 (Supp. 1974).

17. 410 F. Supp. at 548. The court determined that, in view of the savings clauses contained in WPPDA and the Securities Acts, which preserve remedies under other laws, the antifruad provisions would apply to pension plans regardless of whether pension legislation precluded the Securities Acts' procedural regulation of pension plans. *Id.* at 549.

18. Section 2(3) of the Securities Act of 1933 defines "sale" as follows:

> The term "sale" or "sell" shall include every contract of sale or disposition of a security or interest in a security, for value. The term "offer to sell", "offer for sale", or "offer" shall include every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value.

Judge Kirkland noted that the statutory definition of a security included investment contracts.[19] Relying on the Supreme Court's decision in *SEC v. W.J. Howey Co.*,[20] he determined that an interest in a pension plan such as the one involved in *Daniel* falls within the definition of an investment contract. To satisfy the *Howey* test, a pension plan interest would have to involve a scheme whereby a person invests his money in a common enterprise and expects profits solely from the efforts of the plan sponsor or a third party.[21] The plan satisfied the *Howey* criteria since pension plan contributions are the employee's investment,[22] the pension fund is the common enterprise in which the trustees have sole power of control over the investments, and profits are expected in the form of retirement benefits.[23]

"Sale" as statutorily defined in the Securities Acts requires the disposition of a security for value.[24] Whether value was given for the plaintiff's interest in the plan was the only statutory question in *Daniel* as far as the sale issue was concerned. The court ruled that the value element was satified either by the employee providing

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15 U.S.C. § 77b(3) (1970). Sale is similarly defined in § 3(a)(14) of the Securities Exchange Act of 1934, 15 U.S.C. § 78c(a)(14) (1970).

Section 2(1) of the Securities Act of 1933 defines "security" as follows:

> The term "security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security . . . or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in . . . any of the foregoing.

15 U.S.C. § 77b(1) (1970). Security is similarly defined in § 3(a)(10) of the Securities Exchange Act of 1934, 15 U.S.C. § 78c(10) (1970).

19. *See* § 2(1) of the Securities Act of 1933, 15 U.S.C. § 77b(1) (1970).

20. 328 U.S. 293 (1946). In *Howey*, the Supreme Court held that the offering for sale of units of a citrus grove development, coupled with a contract for developing property and remitting profits, constituted the offer for sale of a security in the nature of an investment contract requiring registration under the Securities Acts. *Id.* at 299.

21. *Id.* at 301.

22. The court prefaced its analysis of the sale issue by emphasizing that the Securities Acts were remedial legislation and traditionally such legislation was broadly construed in the interest of protecting investors through full disclosures. 410 F. Supp. at 550. The conclusion that plan contributions are the employee's investment is based on the theory that pension plan benefits were uniformly recognized as part of an employee's wage package. *See* S. Rep. No. 1440, 85th Cong., 2d Sess. 4 (1958). *See also* Inland Steel Co. v. NLRB, 170 F.2d 247 (7th Cir. 1948), *cert. denied*, 336 U.S. 960 (1949) (pension benefits are a proper subject of collective bargaining for purposes of the National Labor Relations Act).

23. 410 F. Supp. at 551.

24. For the language used to define sale see note 18 *supra*.

services or contributing a portion of his wages.[25] The plaintiff had given value, and his eligibility to ratify the wage package evidenced an investment decision; thus, in the court's view, its holding was not inconsistent with the SEC's policy[26] of refusing to find a sale in a pension plan situation unless both value and an investment decision were present.[27]

Daniel marks the first successful attempt to implement the Securities Acts' antifraud provisions to remedy pension plan abuses where a sale of stock was not involved.[28] The court's determination that the Securities Acts are at least facially applicable to pension plans not involving a sale of stock[29] is supported by a number of factors: the Acts' legislative history,[30] the statutory language itself,

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25 410 F. Supp. at 552, 553.

26. *See* notes 47 & 48 and accompanying text *supra* for a fuller discussion of this policy of the SEC.

27. 410 F. Supp. at 553.

28. Prior to *Daniel,* several cases involving employee benefit plans had arisen under the antifraud provisions, but they had generally involved plans under which stock was purchased or sold. *See, e.g.*, Richland v. Cheatham, 272 F. Supp. 148 (S.D.N.Y. 1967) (10(b) action involving a stock bonus trust fund). The only case discovered in which an antifraud liability action was brought with respect to a plan not involving stock transactions was Kaminsky v. Abrams, 281 F. Supp. 501 (S.D.N.Y. 1968). The case was dismissed on other grounds and the issue of whether an interest in such a plan involved the sale of a security subject to the antifraud provisions was not developed. For commentary concerning the applicability of the Securities Acts to employee benefit plans see 1 L. Loss, SECURITIES REGULATION 506-11 (2d ed. 1961, Supp. 1969) [hereinafter cited as Loss]; Hipple & Harkelroad, *Anomalies of SEC Enforcement: Two Areas of Concern*, 24 EMORY L.J. 697 (1975); Mundheim & Henderson, *Applicability of the Federal Securities Laws to Pension and Profit-Sharing Plans*, 29 LAW & CONTEMP. PROB. 795 (1964); Comment, *Securities Aspects of Pension, Profit-Sharing, and Stock Bonus Plans*, 17 S.W.L.J. 444 (1963); Note, *Pension Plans as Securities*, 96 U. PA. L. REV. 549 (1948); 1 CCH PENS. PLAN GUIDE ¶ 1100-1218 (1977).

29. *See* text accompanying notes 15-17 *supra*.

30. The legislative history of the Securities Acts demonstrates a gradual congressional acknowledgment of the security-like nature of an interest in a pension plan. A review of the committee reports and records of hearings preceding enactment of the Securities Act of 1933 discloses no mention of pension plans. *See* S. REP. No. 47, 73d Cong., 1st Sess. (1933); H.R. REP. No. 152, 73d Cong., 1st Sess. (1933). *See also Hearings on H.R. 5832 Before the House Comm. on Interstate and Foreign Commerce*, 77th Cong., 1st Sess. 877-78, 895 (1941) [hereinafter referred to as *1941 Hearings*]. The drafters of the Securities Act of 1933 claimed it was not Congress' intent to include pension plans within the purview of the Act. *Id.*

In 1934, the Senate proposed amendments to the 1933 Act which would have exempted from registration certain offerings made solely to employees of an issuer in connection with a bona fide plan for the payment of extra compensation or stock-investment plan for the exclusive benefit of such employees. The amendments were rejected in conference for the reason that participants in stock-investment plans may need protection as much as other members of the public. *See* H.R. REP. No. 1838, 73d Cong., 2d Sess. 41 (1934); *1941 Hearings*, and the Acts' registration requirements. In the Securities Acts' exempted securities provisions, the specific references to "securities (other than interests or participations in the trust or separate account itself) issued by the employer"[31] suggests that not only stock sold in connection with a plan, but also the interest in a pension "trust" conforms to the definition of a security. Furthermore, the SEC has applied the Securities Acts' registration requirements which, like the antifraud provisions, are applicable where the sale of a security is involved, to securities sold in connection with employee benefit plans.[32] The SEC's requirement for registration of both stock sold in connection with, and interests in, certain employee benefit plans implies not only that the Securities Acts may be applied to pension plans, but also that the acquisition of an interest in such a plan comprises the sale of a security for purposes of the Acts.[33]

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supra at 895. During the 1941 hearings, SEC Commissioner Purcell stated that the rejection of the 1934 Senate-proposed amendment to the Securities Act of 1933 was interpreted as applying the Act to employee plans involving the sale of a security. Any pension plan under which employees were given the oportunity to place part of their earnings in a fund to be invested for their benefit and returned to them at a later date involved the offering of an investment contract. He noted that employee plans were comparable to investment companies, which offer securities to the public at large. *Id.* at 895-96, 905. Significantly, the fact that Congress did exempt certain pension plans from the definition of a securities company under the Investment Company Act of 1940, 15 U.S.C. §§ 80a-1 to 80a-52 (1970), suggests that without the exemption, the definition of a security would include pension plans. *See 1941 Hearings, supra* at 895.

In 1941, the SEC invited suggestions to relieve plans from undue registration burdens while retaining the Securities Acts' safeguards in situations where employees might need protection. *See* SEC SECURITIES ACT RELEASE No. 2485 (Feb. 27, 1941). These efforts culminated in the SEC proposals to amend the Securities Acts by exempting from registration requirements certain interests in plans meeting certain standards, and authorizing the SEC to exempt other plans by promulgating rules. *See 1941 Hearings, supra* at 887-1021. Another bill, H.R. 6437, 77th Cong., 2d Sess. (1942), proposed to exclude interests in all kinds of employee benefit plans from the definition of security. No action was taken on either proposal.

Whatever the reasons for Congress' refusal to exempt pension plans from registration or other provisions of the Securities Acts, it is apparent that Congress was cognizant of the security-like nature of interests in pension plans and the SEC's intention to treat them as such. Finally, in 1970, Congress did specifically recognize pension plans by exempting certain plan interests from the Securities Acts' registration requirements. For the language of the exempted securities provision see note 14 *supra*. The logical inference is that Congress recognized that interests in certain pension plans did involve the sale of securities and would have to be registered unless exempted from registration.

31. For the appropriate language defining exempted securities in § 3(a)(2) of the Securities Act of 1933, 15 U.S.C. § 77c(2) (1970), see note 14 *supra*.

32. *See* authorities cited at note 33 *infra*.

33. Under certain stock purchase plans involving the sale of employer stock, both the

The *Daniel* court's reasoning that subsequent pension legislation did not preclude the Securities Acts' applicability to pension plans is persuasive. The defendants maintained that the exemption provisions of the securities legislation regarding pension plans,[34] viewed in light of WPPDA and ERISA, indicated Congress' desire to have the Securities Acts not apply to pension plans. The exemptions were designed, however, only to reduce the registration burden on small plans, and the antifraud provisions of the Securities Acts should still apply to pension plans involving the sale of a security.[35] In addition, a comparison of the reporting and disclosure provisions of WPPDA and ERISA with those of the Securities Acts supports a conclusion that the laws serve different functions, undermining the defendants' argument that the pension legislation's more demanding requirements suggest preemption.[36] ERISA, the more comprehensive pension law, does not require disclosure of break-in-service rules and other material facts to employee-participants until ninety days after the employee becomes a participant in the plan.[37] In contrast, the Securities Acts' antifraud provisions require disclosure of material facts on or before entry into the plan—at the point of sale.[38] In practical effect, then, the laws are complementary; ERISA requires post-participation disclosure and the Securities Acts man-

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securities and the interests in the plan may be securities requiring registration. Additionally, in certain employee savings plans where no employer stock is sold, the interests in the plan may be securities requiring registration. *See* 1 CCH PENS. PLAN GUIDE ¶ 1100-1218 (1977). *See generally* Givner, *ESOPs and the Federal Securities Laws*, 31 BUS. LAW. 1889 (1976); Overman, *Registration and Exemption from Registration of Employee Compensation Plans Under the Federal Securities Laws*, 28 VAND. L. REV. 455 (1975).

34. Section 3(b)(11) of the Investment Company Act of 1940, 15 U.S.C. § 80a-3(c)(11) (1970), specifically excluded certain employee pension trusts from the definition of an investment company. The 1970 amendments to the Securities Acts specifically exempted from registration requirements interests issued in connection with certain pension plans. *See* note 30 *supra*.

35. *See* S. REP. NO. 184, 91st Cong., 2d Sess., U.S. CODE CONG. & AD. NEWS 4897, 4907 (1970).

36. A review of the pension laws' legislative history provides no answer to the preemption issue. *See* SUBCOMM. ON LABOR OF THE SENATE COMM. ON LABOR AND PUBLIC WELFARE, INTERIM REPORT OF ACTIVITIES OF THE PRIVATE WELFARE AND PENSION PLAN STUDY, S. REP. NO. 634, 92d Cong., 2d Sess. (1972). *See also* SUBCOMM. ON LABOR OF THE SENATE COMM. ON LABOR AND PUBLIC WELFARE, 94TH CONG., 2D SESS., LEGISLATIVE HISTORY OF THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974, vol. I (Comm. Print 1976).

37. *See* 29 U.S.C. §§ 1021-1031 (Supp. 1974).

38. *See* note 6 *supra* for a summary of the antifraud provisions of the Securities Acts which require disclosure of material facts during a sale.

date pre-participation disclosure.[39]

If the pension legislation was intended to be all-encompassing, such legislation should render inapplicable other provisions of the Securities Acts which relate to pension plans. Yet the SEC continues to exercise jurisdiction over certain pension plans where registration is concerned, further suggesting that preemption was not intended.[40] Congress' failure to expressly confer in ERISA or WPPDA exclusive regulatory control over all pension matters by specifically preserving other federal laws governing pension plans[41] also implies that the Securities Acts' antifraud provisions apply to pension plans involving the sale of a security.[42]

The *Daniel* court's finding that a security was involved is tenable. In a pension plan context, a security can be treated as either an investment contract or a profit-sharing agreement;[43] the former approach was adopted in *Daniel.* The basic definition of an investment contract set forth in *Howey* has been recently reaffirmed by the Supreme Court, with minor modification, in *United Housing Foundation, Inc. v. Forman.*[44] Under the *Howey* test, the major area of dispute concerned the profit criterion of the sale; the investment must be made with the expectation that it will generate a profit. *Forman* requires, in addition to the *Howey* criteria, that the *primary*

39. The basic presumption against the implied repeal or displacement of prior laws supports the conclusion that ERISA and the Securities Acts are complementary. Where different legislative acts concern a similar subject, and a repealing intent is not clearly disclosed, the laws will stand together and be given consonant operation where such a construction is reasonably possible. *See* 1A STATUTES AND STATUTORY CONSTRUCTION § 23.10 (C. Sands 45th ed. 1972).

40. *See* notes 32 & 33 and accompanying text *supra.*

41. *See* 29 U.S.C. § 1144 (Supp. 1974). The *Daniel* court also cited the savings clauses of WPPDA and the Securities Acts as evidence of congressional intent not to preempt the Securities Acts. 410 F. Supp. at 549. *See* note 17 *supra.*

42. The jurisdictional boundaries of ERISA (and WPPDA) and the Securities Acts are notably confused, attributable in part to the SEC's failure to provide significant comment to Congress during the drafting of ERISA. *See* BNA PENS. REP. No. 78, at A-10 (1976) (noting the SEC's lack of such input). Absent congressional clarification of when a plan involves a sale of a security, actions under the Securities Acts' antifraud provisions may be expected to recur leaving to the courts the task of determining when the Securities Acts are applicable.

43. *See* Loss, *supra* note 28, at 506-11.

44. 421 U.S. 837 (1975). *Forman* expressly reaffirmed the *Howey* test as the touchstone for defining investment contracts, and held that shares of stock purchased from a housing cooperative did not constitute investment contracts within the purview of the Securities Acts. Its refusal to find an investment contract was based upon the belief that the spirit of the Securities Acts militated against protecting persons purchasing commodities for personal consumption. *Id.* at 848, 858.

purpose of the investment be to obtain the profits.[45] The *Daniel* defendants argued that no profits could be expected from a pension plan that provided a definite benefit rather than a benefit dependent upon the earnings of the plan trust fund. Yet benefits under the plan are reasonably expected to exceed contributions due to the fund's earning capacity; under that analysis, the profit element is arguably satisfied.[46] Assuming arguendo that the plaintiff actually made an investment, the primary purpose of the investment would be to realize profits, whether they be the growth of the fund or the total retirement benefit. The *Forman* test is satisfied and a security in the nature of an investment contract is present.

Perhaps the most significant aspect of the *Daniel* case is that its disposition of the sale issue effectively repudiates the SEC's no-sale rule[47] regarding pension plans as an unrealistic approach to resolving the sale issue in the context of the antifraud provisions. Under its no-sale rule, the SEC will not find a sale where a plan is either noncontributory or involuntary despite the fact the statutory definition of sale is ostensibly satisfied. The rule stipulates that both value and an investment decision must be found in a pension plan context before a sale has occurred and the antifraud provisions are applied. The SEC's reasoning is that when a plan is noncontributory, the employee has received a gift and has not given value which is a statutory requirement of a sale; when a plan is involun-

45. Under *Forman*, where there is an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others, an investment contract will be found. The primary purpose of the investment, under *Forman*, must be to obtain the profit; the investment must be economically induced. *Id.* at 852.

46. Generally, a defined-benefit pension plan is a retirement plan whereby a plan sponsor makes contributions which are actuarially determined to provide a fixed or defined retirement benefit. The actuarial determination assumes a certain rate of earnings for the funds contributed and usually the contribution will grow, through fund earnings, to provide benefits substantially exceeding contributions. Profit is, therefore, a very realistic element of a defined-benefit plan from a contributor's view. *See generally* S. GOLDBERG, PENSION PLANS AND EXECUTIVE COMPENSATION 1-24 (1974); CCH PENS. PLAN GUIDE (1977); P-H PENS. & PROFIT-SHARING FORMS (1977).

47. The SEC no-sale theory is basically an administrative policy designed to alleviate the burdens of registration under the Securities Acts by finding no sale of a security. *See* Letter from Assistant General Counsel of Securities and Exchange Commission to Commerce Clearing House, Inc., May 12, 1953, in 1 CCH FED. SEC. L. REP. ¶ 2105.50 (1977); CCH DEC. ¶ 75,195 (1941-44); Letter from Chief Counsel, Division of Corporation Finance of the Securities and Exchange Commission to Commerce Clearing House, Inc., August 1, 1962, in 1 CCH FED. SEC. L. REP. ¶ 2105.52 (1977).

tary, the employee has made no investment decision or choice and would not logically need the protection of the Securities Acts.[48]

Because the plan in *Daniel* was both involuntary and noncontributory, the defendants claimed that the plaintiff either had not given value for his interest or had made no investment decision. The court's finding of value in the contribution of a portion of the plaintiff's wages[49] or services[50] is, however, well-supported. It was argued in *Daniel* that there is no choice of whether or not to participate (invest) in a pension plan when it is negotiated on an industry-wide basis because the plaintiff's ratification vote may provide an individual no effective control if other union members oppose him. If a court were to examine the reasoning applied in analogous corporate merger cases, where collective ratification also takes place by way of voting, that argument is attenuated. It has consistently been held that Securities Acts' antifraud liability may obtain where shareholders vote to approve mergers based on misleading facts.[51] This protection is available to shareholders regardless of the way they voted.[52] A union member voting to ratify an amendment to a pension plan has the same degree of choice as a shareholder voting in a merger situation and should be similarly protected.

The *Daniel* determination that a sale of a security occurred for antifraud purposes appears to be consistent with public policy considerations. The need to protect investors was recognized by the Supreme Court in both *Howey*[53] and *Forman*[54] as an underlying factor compelling a broad definition of security. Since ERISA does not require pre-participation disclosures,[55] nor apply retroactively,[56]

48. There is some doubt whether the no-sale rule is applicable in the antifraud liability area since the rule specifically addresses the sale issue in the context of registration. *See* authorities cited at note 47 *supra.* If the rule did not apply in situations where fraud has been alleged, the finding of a sale would be much easier.

49. *See* note 22 *supra.*

50. There is authority for the proposition that the value element for purposes of finding a sale is satisfied by the performance of services. *See, e.g.*, Collins v. Rukin, 342 F. Supp. 1282 (D. Mass. 1972).

51. *See* Simon v. New Haven Bd. & Carton Co., 250 F. Supp. 297 (D. Conn. 1966). *See also* Richland v. Crandall, 259 F. Supp. 274 (S.D.N.Y. 1966) (where approval of sale of corporate assets was fraudulently obtained, stockholders permitted to bring action under the Securities Exchange Act of 1934).

52. *See* cases cited at note 51 *supra.*

53. *See* SEC v. W.J. Howey Co., 328 U.S. 293, 298, 301 (1946).

54. *See* United Housing Foundation, Inc. v. Forman, 421 U.S 837, 849 (1975).

55. Pre-participation, material omissions regarding pension plans would not be actionable under ERISA because civil actions for material omissions are generally conditioned upon

a failure to disclose a material fact affecting an employee's rights in a pension plan which occurred prior to an employee's participation in a plan or prior to enactment of ERISA would be insulated from an effective statutory remedy if *Daniel* were decided differently. Furthermore, the Supreme Court's recent decision in *Ernst & Ernst v. Hochfelder*[57] restricts antifraud liability to cases involving intentional as opposed to negligent material omissions. Employees intentionally deceived by plan sponsors would certainly be in need of the Securities Acts' protection.

If *Daniel* is upheld on appeal, it will establish a remedial precedent in an expanding pension field. It is important to keep in mind, however, that because the Securities Acts might apply to pension plans does not mean that all plans will be subject to the Acts' antifraud provisions. Only those pension plans involving the sale of a security will be subject to antifraud liability and an investment decision will still be required to establish a sale. The mere fact that a plan is involuntary or noncontributory, however, will not foreclose suit. Unless Congress acts to clarify the scope of the Securities Acts' applicability to pension plans, the sale-of-a-security determination will have to be made on a case by case basis. If *Daniel* is reversed based on a finding that either no security or no sale was involved, other plaintiffs might conceivably obtain relief under the antifraud provisions where a sale of a security is established. Thus, other types of employee benefit plans could be implicated.

The consequences of applying the Securities Acts' antifraud provisions to pension plans and the court's rejection of the SEC no-sale theory are difficult to predict.[58] The ultimate impact of *Daniel* may

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disclosures required under ERISA. *See* 29 U.S.C. § 1132 (Supp. 1974). ERISA does not require pre-participation disclosures. *See* note 37 and accompanying text *supra*.

56. *See* 29 U.S.C. § 1144 (Supp. 1974).

57. 425 U.S. 185 (1976). In *Ernst & Ernst*, the Supreme Court held that an action for civil damages could not be maintained under § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (1970), absent an allegation of scienter or some intent to deceive, manipulate, or defraud. 425 U.S. at 214.

58. Several potential ramifications relevant to the *Daniel* decision are beyond the scope of this note. The court's rationale may be extended to non-collective bargaining situations in which an individual negotiates wage and pension benefits with a prospective employer. If so, every pension plan in existence may be affected. A union may be able to avoid providing a union member with an investment decision by simply removing the ratification procedure. This may be disruptive to the collective bargaining process. The rejection of the SEC no-sale rule may also be extended into the registration area, causing plan interests to be registered. This could be an expensive, time-consuming, and, in view of ERISA, a duplicative disclosure

be to discourage employers who fear antifraud liability or high costs regarding disclosures from adopting new plans. The decision may cause other employers to terminate existing plans. This would militate against an express governmental policy of encouraging the implementation of private pension plans.[59] *Daniel's* effect on the interests of plan sponsors was not fully explored by the court. A more thorough analysis of the competing interests at stake, including a balancing of the collective interests of plan sponsors against the interests of plan participants, should be undertaken. With this accommodation in mind, prompt congressional action to define when a plan interest involves the sale of a security, and to clarify the jurisdictional boundaries of the Securities Acts and ERISA, would obviate potential confusion and a drawn out process of judicial rulemaking.[60]

Donald J. Harrell

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process. The most desirable approach may be to amend ERISA to require more immediate disclosure in order to satisfy the Securities Acts' disclosure requirements and avoid duplicative reporting. Finally, *Daniel* provides no effective guideline for determining when a pension plan interest becomes a security. Legislative action to avoid disclosure duplications or to clarify the jurisdictional boundaries of the Securities Acts and ERISA would obviate a proliferation of litigation on both antifraud and registration issues and restore some degree of certainty in these areas of the law.

59. *See* 29 U.S.C. § 1001 (Supp. 1974).

60. As evidence of the confusion in this area, the United States District Court for the Central District of California has recently held, in sustaining a motion to dismiss, that an interest in an employee benefit plan trust is not a security, that the acquisition of the interest is not a sale under the Securities Acts, and that the exclusive remedy for disputes over pension benefits is provided by ERISA. Hurn v. Retirement Fund Trust of the Plumbing Heating & Piping Indus., 424 F. Supp. 80 (C.D. Cal. 1976).

The SEC has filed an amicus curiae brief in *Daniel* contending that the antifraud provisions of the Securities Acts do protect Mr. Daniel and that ERISA was not meant to compromise such protection. Brief of the SEC as Amicus Curiae, Daniel v. International Bhd. of Teamsters, 410 F. Supp. 541 (N.D. Ill. 1976). The *Daniel* decision has been appealed and is now pending before the Seventh Circuit Court of Appeals.