Factoring the Ambiguity: A Futile Attempt to Understand the Ambiguous Nature of the Integration Doctrine's Five Factor Test

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I. Introduction

In 1961, the Securities and Exchange Commission (SEC) introduced five factors, launching more than forty years of ambiguity, confusion, and contradiction. The SEC developed the integration doctrine's five factor test to assist issuers and judges determine whether supposedly separate offers are really part of the same integrated transaction.[1] However, the SEC failed to provide any meaningful guidance to aid in the interpretation or application of these factors. As a result, courts have reached a wide-range of contradictory opinions, and issuers have little solid guidance to predict whether the five factor test will integrate offers.[2]

The integration doctrine combines all offers that are part of the same transaction unless the offers qualify for an exemption from integration.[3] The doctrine developed shortly after Congress passed the Securities Act of 1933 (Securities Act) and the Securities Exchange Act of 1934 (Exchange Act) in the wake of the Great Depression.[4] The SEC designed the doctrine to

expose issuers attempting to take advantage of the registration exemptions by trying to perfect multiple exemptions for the same transaction.[5] This is important because the availability of an exemption depends on the entire transaction.[6] If a transaction does not qualify for an exemption, then the issuer must register the offering.[7] If an issuer offers securities and subsequently is unable to perfect an exemption, then the issuer will be liable for a Section 5 violation, which can carry harsh consequences. The greatest risk for the issuer comes from Section 12(a)(1) of the Securities Act, which gives purchasers of securities sold in violation of Section 5 an automatic right to rescission.[8] This means that the purchaser is entitled to have the entire dollar amount of his or her purchase refunded with prejudgment interest if the purchaser still owns the securities. If the purchaser has sold the securities, then the purchaser is entitled to damages, which is the difference between the price the purchaser bought the securities and the price the purchaser sold the securities.[9]

The integration doctrine applies to several areas of securities law including § 4(2) of the Securities Act, § 3(a)(10) of the Securities Act, and § 3(c)(1) of the Investment Company Act of 1940 (ICA). [10] An issuer generally wants to avoid application of the integration doctrine in all areas where the doctrine applies.[11] An issuer can avoid the doctrine by engaging

in excluded transactions such as Regulation S foreign offers.[12] Alternatively, an issuer can seek the shelter of a regulatory safe harbor such as the ones offered by Rule 155 and Rule 502.[13] If an issuer does not qualify for a safe harbor, then the issuer may still avoid the doctrine by applying the five factor test to weigh the facts and circumstances surrounding purportedly separate offers to decide whether the offers are part of the same offering.[14]

However, application of the five factor test is especially onerous because the five factor test is highly ambiguous. Even though the five factor test has been in existence for more than forty years, the SEC has never satisfactorily clarified the meaning of the factors. Furthermore, courts have never reached a consensus on the meaning of any of the five factors. The ambiguous nature of the factors is so extreme that courts cannot even agree on how many factors are necessary to integrate offerings.

This article will examine each of the five factors in turn in an effort to identify common interpretative patterns applied in court proceedings and SEC no-action letters. This article will then try to identify how the factors interrelate to shape the outcome of an integration analysis. Finally, this article will develop suggestions on ways that the SEC could mitigate the ambiguous nature of the factors.

II. Alternatives to the Factors

As a preliminary note to a full examination of the five factors, it is useful to consider the alternatives to the factors that the SEC has provided issuers. Perfecting a safe harbor exemption is the primary vehicle for an issuer to avoid the factors. Safe harbors automatically treat as distinct certain offers that the integration doctrine might otherwise combine into a single offer. The main safe harbors include Rule 147, Rule 155, Rule 251, Rule 502, and Rule 701. It is instructive to briefly examine each of these rules and consider the SEC justification for these safe harbors in light of the goal of promoting investor protection.[15]

A. Rule 155

The SEC adopted the Rule 155 safe harbor in 2001 following three years of proposed rule-making and consideration.[16] The Commission did not intend for the safe harbor to change the integration doctrine but meant for the safe harbor to provide additional clarity and certainty for an issuer.[17] Rule 155 provides a safe harbor when an issuer abandons a private offering and then makes a public registered offering or when an issuer abandons a public registered offering and then makes a private offering.[18] Essentially,

the safe harbor allows an issuer to change an offering if the issuer waits thirty days and discloses the change to new investors.[19] The SEC justifies the Rule 155 safe harbor by asserting that the rule facilitates capital fund-raising while not compromising investor protection since it does not modify the factors underlying the integration doctrine.[20] Therefore, Rule 155 implies that a waiting period of thirty days under the right circumstances is a sufficient temporal separation between offers to justify non-integration.

B. Rule 502

Rule 502 provides a safe harbor for Regulation D offers made more than six months apart with no offers of the same or similar securities made in between.[21] Under Rule 502(a), Regulation D may integrate all offers unless the issuer separates the offers by six months or meets some other exception or exemption.[22] Therefore, Rule 502 implies that a waiting period of six months, regardless of the circumstances of the issuer, is a sufficient temporal separation between offers to justify non-integration. Furthermore, Rule 502 implies that an offer made pursuant to a proper employee benefit is a sufficiently distinct purpose to justify non-integration with other offers made by the issuer.

C. Rule 147

Rule 147 provides a safe harbor for issuers who make offers that are exempt from registration because they are entirely intrastate.[23] Like Rule 502, Rule 147 exempts from integration intrastate offers made with six months separation so long as there are no offers of the same or similar securities made in between.[24] Therefore, Rule 147 also implies that a waiting period of six months, regardless of the circumstances of the issuer, is a sufficient temporal separation between offers to justify non-integration.

D. Rule 251

Rule 251 provides a safe harbor for offers that are exempt from registration under Regulation A.[25] Rule 251 follows the same pattern as Rules 502 and 147 by exempting from integration offers made with at least six months separation and offers made pursuant to a proper employee benefit plan.[26] Therefore, Rule 251 also implies that a six month waiting period is a sufficient temporal separation and an offer made pursuant to a proper employee benefit plan is a sufficiently distinct purpose to justify non-integration with other offers.

E. Rule 701

Rule 701 provides a safe harbor from integration for offers made pursuant to a proper employee compensation plan.[27] In adopting Rule 701, the SEC pointed out that many commentators were concerned that Rule 701 would create integration problems for an issuer.[28] Accordingly, the SEC crafted the Rule 701 integration safe harbor under the assumption that an offer made pursuant to Rule 701 constitutes a sufficiently distinct purpose to justify non-integration because such an offer would naturally constitute "a single, discrete offering".[29]

This brief summary of the main safe harbors reveals a pattern of excluding offers from the integration doctrine based on certain objective time or purpose distinctions. The safe harbors establish irrebuttable presumptions that offers made for certain purposes, such as employee compensation, or made with certain temporal separations, such as six months, are sufficiently distinct from other offers that the offers need not be integrated.[30] Therefore, the primary logical string running through all of the SEC's safe harbors is the establishment of objective facts and circumstances under which offers are obviously distinct. The desirability of these objective facts and circumstances becomes evident when an issuer or lawyer considers

the five factor test that applies when offers do not qualify for an exception or safe harbor.

III. The Birth of the Factors

The SEC débuted the five factor test in 1961 in a release aimed at clarifying the Section 3(a)(11) exemption for local offerings.[31] However, the five factors were not the main subject of the 1961 release. Instead, the five factors received one sentence in the context of determining what constitutes an issue under federal law for purposes of the Section 3(a)(11) exemption. The single sentence that gave birth to the five factor test merely listed the five factors with a brief mention that any one or more of the factors may be determinative of the question of integration.[32] In fact, the SEC introduced the five factors with only sixteen words of interpretive guidance.[33]

In 1962, the SEC promulgated the five factors again in a release on the Section 4(2) non-public offering exemption.[34] The often cited 1962 release provided even less guidance than the 1961 release.[35] Like the 1961 release, the 1962 release only dedicated one sentence to the five factors.[36] The 1962 release gave a whole ten words of interpretative guidance: "The following factors are relevant to such question of integration: [list of factors]."[37] Thus, the 1962 release does not provide even as much guidance

as the 1961 release, which at least noted that one or more factors may be determinative.[38]

Despite the extraordinarily pithy introduction of the five factor test, the factors contained in the 1961 and 1962 releases have become the standard for determining whether purportedly separate offers are part of the same integrated transaction.[39] Unfortunately, the factors have never escaped the ambiguity they inherited from birth. Instead, the factors remain vague and indeterminate.[40]

Furthermore, there is relatively little case law dealing with the factors. The case law that is available frequently reaches contradictory applications of the factors.[41] Adding to the confusion, the SEC refused to answer questions about these factors in no-action letters from 1979 to 1985.[42] Therefore, an issuer should examine each of the factors in turn in an effort to identify the facts and circumstances that are relevant to determining whether offers are integrated.

IV. The Five Factors

When offers do not qualify for one of the automatic exclusions or safe harbors, an issuer may still avoid integration by proving that a subsequent offer is distinct from earlier offers.[43] An issuer does this by examining the

facts and circumstances surrounding the offers.[44] The SEC promulgated the five factors to guide issuers, judges, and SEC staff members in examining the facts and circumstances. The five factors are:

1. the different offerings are part of a single plan of financing;
2. the offerings involve issuance of the same class of security;
3. the offerings are made at or about the same time;
4. the same type of consideration is to be received;
5. the offerings are made for the same general purpose.[45]

A. Single Plan of Financing

The first factor relevant to the facts and circumstances inquiry under the integration doctrine is whether the purportedly separate offers are part of a single plan of financing (the "single plan of financing" factor).[46] This factor weighs in favor of integration if it appears from the facts and circumstances that the offers are part of a single plan of financing.[47] As with all of the factors, the SEC and the courts have offered very little concrete guidance to help an issuer determine what types of facts and circumstances are relevant to determining that a series of offers are part of a single plan of financing. Furthermore, the interpretation of this factor is often

indistinguishable from the general purpose factor, which adds to the ambiguity.[48]

1. Contemplating Subsequent Offers

Some of the facts that courts focus on in interpreting this factor are not as ambiguous as others. Whether the issuer contemplated subsequent offers during the first set of offers is one of the less ambiguous facts that courts may find relevant to determining whether purportedly separate offers constitute a single plan of financing.[49] For instance, in *Walker v. Montclaire Housing Partners*, the defendants organized a limited partnership to invest in four different partnerships, each of which owned and operated government-assisted apartment complexes. Without any offering documents, Montclaire sold a limited partnership interest to John Hill as a tax-shelter. While making the offer to Mr. Hill, Montclaire prepared a private placement memorandum (PPM) that showcased Mr. Hill's investment to elicit other limited partners for the venture. After Mr. Hill died, his estate sued for rescission under the North Carolina securities laws. Under North Carolina law, the outcome of the case turned on whether the offer to Mr. Hill constituted a separate offer from the subsequent offers made with the PPM.[50]

Hearing the case under diversity jurisdiction, the federal district court applied federal precedents to determine whether the offers constituted an integrated offering. The court found that the single plan of financing factor weighed in favor of integration because the issuer contemplated the subsequent offers at the same time the issuer made the offer to Mr. Hill.[51] The court contrasted this with an earlier case where a court found that there was no single plan of financing when the issuer planned no subsequent offers during the first offer and an SEC no-action letter that found a single plan of financing when the issuer anticipated the need for capital from both offers to go forward with operations.[52]

The SEC no-action letter in Independent News, Inc. also supports the court's view in *Walker*. In Independent News, Inc., the issuer started a debenture offering without any plans to make subsequent offers.[53] Unfortunately, the company failed to meet its projected net income goals and proposed a second set of offers to cover the short-fall. Independent News, Inc. argued that these facts proved that the offers did not involve a single plan of financing. The SEC staff agreed with the company that the offers were separate. The staff reiterated the company's argument on the single plan of financing factor and cited it as one of the reasons that helped the staff reach its conclusion.[54] Therefore, Independent News, Inc. supports

the conclusion made by the court in *Walker* that the outcome of the single plan of financing factor may depend on whether the issuer contemplated subsequent offers at the time of the first offers.[55]

2. Using Different Techniques

Another somewhat straightforward fact looked to is whether different techniques are used to carryout the offers.[56] The use of different offering techniques indicates that offers do not constitute a single plan of financing.[57] Different techniques may include making offers in different markets or using different methods for the offers.[58]

For instance, the SEC issued a no-action letter agreeing not to recommend integration of First & Merchants Corporation's (F&M) plan to make simultaneous offers of commercial paper and notes aimed at different markets. F&M sold the commercial paper primarily to regional market institutional investors through established commercial paper dealers. F&M proposed to sell the notes primarily to national market institutional investors, though F&M conceded that there would probably be some overlap in purchasers. Nevertheless, the staff issued the no-action letter on the basis that the offers did not constitute a single plan of financing. Among other

factors, the staff recited the fact that F&M aimed the offers at different markets.[59]

The SEC also issued a no-action letter agreeing not to recommend integration of Pittsburgh National Corporation's (PNC) plan to make simultaneous offers of commercial paper and notes using different methods. PNC sold the commercial paper primarily in direct sales to institutional investors. PNC proposed to sell the notes through a private placement orchestrated by a broker-dealer. PNC noted that it might occasionally sell commercial paper through a broker-dealer but promised to use a different dealer if it did so. In its response, the staff quoted PNC's statement that "the methods of offering the two types of securities are sufficiently different to constitute separate plans of financing" and the staff agreed not to recommend integration of the offers.[60]

3. Pursuing the Same Business Venture

While the interpretation of some facts may be reasonably straightforward, other facts are much more ambiguous. A particularly ambiguous fact that courts sometimes focus on is whether purportedly separate offers pursued, or attempted to engage in, the same business venture.[61] The ambiguity of this fact is two-fold. First, an issuer may be

legitimately confused as to what constitutes pursuit of the same business venture. Second, an issuer may have difficulty distinguishing the relationship of this fact between the single plan of financing factor and the general purpose factor.

The case of *Johnston v. Bumba* helps to illustrate the ambiguity. In *Johnston*, the plaintiffs organized a limited partnership called Aqua-Solar to purchase and lease solar water heating systems to homeowners in Florida. The business plan called for Aqua-Solar to contract with Nationwide-Florida, which the plaintiffs largely controlled, to obtain the leases and provide all services related to the installation and maintenance of the water systems. The plaintiffs also organized three other limited partnerships with an identical business plan.[62]

Lincoln Bumba purchased a partnership interest in Aqua-Solar and executed a promissory note in partial payment for the interest. Mr. Bumba refused to pay the promissory note, and the plaintiffs sued to enforce the note. Mr. Bumba successfully defended on the grounds that the partnership interest violated the securities laws if all of the partnerships were part of an integrated transaction, so the plaintiffs could not enforce collection of the consideration. In applying the factors of the integration doctrine, the court found that the only material question was whether the four partnerships were

part of the same plan of financing.[63] The plaintiffs contended that the partnerships did not constitute a single plan of financing since each partnership purchased its own water heating units with no cross-collateralization or sharing of funds between the partnerships. However, the court found that the partnerships constituted the same business venture even though they purchased distinct lots of heating units.[64]

Unfortunately, the court in *Johnston* did not elaborate on what the plaintiffs could have done to prove that the partnerships did not share a single plan of financing. Evidently, the court found that all of the partnerships operated in nearly an identical fashion meaning that the partnerships constituted a single plan of financing. This raises a key question; namely, from which perspective should the analysis of the single plan of financing factor take place? In other words, is the single plan of financing factor judged from the perspective of the issuer meaning that the issuer had a single plan of financing carried out through multiple identical partnerships (even if each partnership carried out different tasks) or is the factor determined from the perspective of the partnership meaning that each individual partnership had the same plan to finance its operations? If the former view is correct, then would not the issuer almost always form partnerships with the single plan to finance the issuer (i.e., a plan to form

multiple identical partnerships to carryout the issuer's objectives), which would mean that this factor would always weigh in favor of integration? If the later view is correct as the court in *Johnston* implies, must an issuer always change the business plan of new partnerships to avoid integration under this factor?[65]

The case of *SEC v. Cavanagh* stands for the proposition that courts should judge the single plan of financing factor from the perspective of the issuer. In *Cavanagh*, the issuers made multiple offers in a highly complex scheme designed to allow the issuers to take over a company for a small amount of capital and then sell shares at a highly inflated price.[66] To carryout their objectives, the issuers merged two companies, Curbstone and WTS, and offered shares to a group of Spanish investors (the Spanish Shares). In analyzing the single plan of financing factor, the court concluded that the merger and the sale of the Spanish Shares constituted a single plan of financing, which was to provide the issuers with their desired return.[67] Thus, the court in *Cavanagh* judged this factor from the perspective of the issuer.

The case of *Donohoe v. Consolidated Operating & Production Corp.* stands for the proposition that courts should judge the single plan of financing factor from the perspective of the partnership, which means that

the partnerships can have the same business plan without necessarily having a single plan of financing. In *Donohoe*, the Seventh Circuit upheld the district court's finding that multiple partnerships formed to drill oil near Corsicana, Texas did not involve a single plan of financing.[68]

In *Donohoe*, the defendants established four limited partnerships to drill oil near Corsicana.[69] The business plan for all four partnerships called for each to contract with Ona Drilling Corp. to carry-out the actual drilling operations for a set fee. The plaintiffs alleged that the four partnerships constituted the same offer, which would result in a Section 5 violation and a rescission right.[70] Despite the fact that the partnerships each had the same business plan, the court found that the partnerships involved separate financing plans since each partnership was designed to stand or fall on its own merits and any benefit that Ona Drilling Corp. received from the combined effect of the four contracts did not affect the price that each partnership paid for Ona's services.[71]

Despite the strong similarity between *Johnston* and *Donohoe*, where both involved multiple limited partnerships serviced by a single operating entity, the courts reached opposite conclusions. While both courts applied the factor from the perspective of the partnership, the courts took opposite views of how the factor relates to the facts. The court in *Donohoe* found that

the partnerships could involve a different plan of financing despite having the same operational business plan, while *Johnston* found the opposite. As a result, the starkly opposite opinions of *Johnston* and *Donohoe* create significant ambiguity for an issuer trying to understand the single plan of financing factor. The presence of *Cavanagh*, which approaches this from an entirely different perspective, deepens the ambiguity. Furthermore, an issuer may wonder how this fact is any different from the general purpose factor. After all, would not all businesses operating with nearly identical business plans (i.e., using identical suppliers and operating in identical geographic locations) accomplish nearly identical purposes?[72]

The authorities interpreting the single plan of financing factor leave an issuer with significant uncertainty as to which facts and circumstances are particularly relevant to deciding whether purportedly separate offers constitute a single plan of financing. While some relevant facts appear to be whether subsequent offers were contemplated during the first set of offers, whether the offers involved the same type of business venture or plan, whether each offering stood or fell on its own merits, and whether the offers relied on different offering techniques such as varying the market where the offerings were made or using different methods to sell the offers; the

fundamental question of how to interpret these facts and distinguish them from the general purpose factor remains.

B. Same Class of Securities

The second factor relevant to the facts and circumstances inquiry under the integration doctrine is whether the purportedly different offers involve the same class of securities (the "class of securities" factor).[73] A review of the authorities sheds some insight into the facts and circumstances relevant to determining whether purportedly separate offers involve the same class of securities. However, the exact interpretation of the facts remains ambiguous. In particular, there is a great deal of ambiguity as to how and where courts should look for relevant variations.

The authorities interpreting the same class of securities factor do not agree how variations are relevant. In other words, the authorities do not agree as to how or where an issuer can vary the securities offered to avoid integration under this factor. For instance, variations may be located at the "type" level meaning the securities vary by type (e.g., debt securities and equity securities are different types of securities), at the "category" level meaning the securities vary by category (e.g., LLC memberships and limited partnership interests are different categories of equity type securities), or at

the "subcategory" level meaning the securities have sub-categorical variations (e.g., limited partnerships with different distribution rights are different subcategories of securities).[74]

1. Type Variations

Authorities almost always consider variations at the type level relevant.[75] In *Kevin D. Kunz* II, the Commission agreed that the fact the offers were different types of securities is relevant to the analysis of this factor.[76] Indeed, the Commission in *Kevin D. Kunz* II essentially concluded that different types of securities are not the same class of securities.[77] However, authorities may consider an offer of different types of securities as an offer of the same class if the offers are convertible into the same type of security.[78] For instance, if an issuer offers equity in Offer A and debt convertible to equity in Offer B, then these offers are actually offers of the same type of security since the securities offered in Offer B are convertible to the same type of securities offered in Offer A.[79]

2. Category Variations

While variations at the type level are almost always relevant, variations at the category level may not be.[80] For instances, in *Kevin D.*

Kunz II the defendant offered MLP Interests (equity), Accrual Notes (debt), and Monthly Notes (debt).[81] The Commission agreed that the MLP Interests were not in the same class as the other offers since they were a different type of security. However, the Commission was not as convinced that the Accrual Notes and the Monthly Notes were in a different class even though they were a different category of debt securities.[82] The Commission accepted the defendant's argument *arguendo* without expressing an opinion as to the actual validity of the argument. Instead, the Commission concluded that the weight of the remaining factors was so heavy that the outcome of this factor was irrelevant.[83]

However, an issuer could read the Commission's decision as questioning whether there was sufficient variation between the Accrual Notes and Monthly Notes categories to justify a finding that the notes really belonged in different categories of debt instruments rather than questioning whether different categories of securities can belong in different classes. Nevertheless, the real battleground for this argument appears to be whether differences at the subcategory level are relevant.

3. The *Walker* View on Subcategory Variations

The *Walker* decision stands for the proposition that variations found at the subcategory level are irrelevant. The court in *Walker* held that all securities in the same category are the same class of securities regardless of any subcategory variations that may exist.[84] In *Walker*, the fact that the securities belonged to the limited partnership interest category was sufficient to satisfy the class of securities factor. The court refused to give any weight to the argument that the limited partnership interests were different classes because the interests apportioned profits and losses differently.[85] For authority, the *Walker* court cited *SEC v. Murphy* and *Currie v. Cayman Resources Corp.*[86]

However, the *Murphy* court did not address the issue of whether courts can consider securities of the same type and category a different class of securities if the securities provide different rights at the sub-categorical level.[87] The defendant in *Murphy* sold limited partnership interests in cable companies to investors. In applying the second factor to the interests, the court held that "[t]o the extent that we can define classes of securities that are not stocks or bonds, the securities at issue here all limited partnership interests are of the same class [sic]."[88] However, the recitation of the facts in *Murphy* gave no indication that the limited partnership interests offered had

sub-categorical variations in terms of the rights that the interests conveyed to the investors.[89] Unlike *Walker*, the *Murphy* court did not apparently face a situation where the issuer offered securities of the same type and category but with different sub-categorical rights. Therefore, the *Walker* court might have inappropriately extended *Murphy* for the proposition that securities of the same type and category are always the same class.

Similarly, the *Currie* court did not address the issue of whether securities of the same type and category are always the same class. In *Currie*, the defendants operated REB Petroleum Company (REB), which was a small oil company that financed its operations by selling limited partnership interests in multiple limited partnerships with REB as the general partner.[90] While applying the integration factors, the court concluded that the limited partnership interests constituted the same class of securities.[91] However, the record did not contain any indication that the limited partnership interests had sub-categorical variations between limited partnerships.[92] Therefore, a judicial body should not hold that *Currie* is proper authority for the proposition that all limited partnership interests (i.e., securities of the same type and category) are in the same class regardless of any substantive sub-categorical variations that may exist among the interests.

4. The Fifth Circuit View on Subcategory Variations

At least in the Fifth Circuit, subcategory variations are relevant to distinguish whether securities in the same category belong to different classes. In *Doran v. Petroleum Management Corp.*, the defendants offered multiple limited partnership interests in a partnership organized to drill and operate wells in Wyoming.[93] The defendants offered two types of limited partnership interests. The defendants called the first set of limited partnership interests "participants", and the partnership used their contributions first to pay all intangible expenses. The defendants called the second set of limited partnership interests "special participants", and the partnership used their contributions first to pay tangible drilling expenses. The partnership could charge either set of interests with an expense if one set of interests was inadequate to pay the expenses allocated to it. As a result, the only real difference between the two sets of interests was that "participants" received a greater portion of the tax deductions.[94]

William Doran, one of the "special participants" sued for rescission for a Section 5 violation.[95] The defendants claimed a Section 4(2) exemption from registration. In contemplating whether the defendants qualified for the Section 4(2) exemption, the court applied the five factor test to determine whether to integrate the two types of limited partnership

interests.[96] The court focused on the class of securities factor as the only possible distinction between the two offers.[97] Unlike *Walker*, the *Doran* court was willing to consider whether the limited partnership interests may still constitute a different class of securities based on sub-categorical differences between the securities.[98] However, the *Doran* court did not find the limited partnership interests in question sufficiently distinct to qualify as a different class of securities.[99]

The importance of *Doran* is the court's implication that offers of securities of the same type and category may still be offers of distinct classes of securities. The fact that the court did not find the limited partnership interests in *Doran* sufficiently distinct implies that the interests could have been distinct classes if there had been more subcategory distinctions.[100] Therefore, *Doran* indicates that the issuer may insert relevant variations at the type, category, and subcategory levels.

5. The SEC Staff View on Subcategory Variations

The SEC staff also considers type, category, and subcategory variations relevant to determining whether offers involve the same class of securities. For instance, the SEC staff issued a no-action letter determining that integration was not necessary when an issuer offered multiple sets of

similar debt securities with materially different cash flows.[101] The Resolution Trust Corporation no-action letter involved a question of whether the ICA would integrate two issuers selling collateralized bond obligations.[102] Here, the staff concluded that integration was inappropriate especially in light of the fact that the issuers allocated materially different cash flows to the securities issued in prior collateralized bond obligation transactions.[103] Therefore, even though the securities at issue were the same type (debt) and the same category (collateralized bond obligations), the staff implied that the sub-categorical cash flow distinction was a sufficient basis to classify the securities in different classes.[104]

Based on the authorities interpreting the second factor of the integration analysis, an issuer can conclude that this factor is as ambiguous as the first factor. Not only have the courts and the SEC done a poor job of illustrating what sorts of variations are relevant to this analysis, the authorities cannot even agree how or where to begin looking for variations. Aside from offering different types of securities, an issuer has no certainty that this factor will not weigh in favor of integration regardless of how many categorical or sub-categorical variations may exist.[105]

C. At or About the Same Time

The third factor relevant to the facts and circumstances inquiry under the integration doctrine is whether the purportedly different offers occurred at or about the same time (the "time" factor).[106] The SEC rules state that a separation of at least six months generally is sufficient to avoid integration.[107] Therefore, offers separated by at least six months do not occur at or about the same time. However, the integration factors do not provide a definite time-line for evaluating how the time-interval between offers made zero to six months apart weighs in favor of integration.

If the offers occur at the same time, then this factor typically weighs in favor of integration. In fact, some issuers concede this factor and focus on the weight of the other factors to show non-integration.[108] For instance, Blue Cross and Blue Shield of Virginia (Blue Cross) planned to offer Class C Common Stock and an Initial Public Offering simultaneously.[109] In presenting its case to the SEC staff for non-integration, Blue Cross stated that the offers would occur at the same time but then argued that all of the remaining factors weighed against integration.[110] Similarly, F&M admitted that the offers in question did occur at the same time but argued that the other factors outweighed this one.[111] In both cases, the SEC staff concurred

with the issuers and decided not to recommend integration of the offers despite the fact that the timing weighed in favor of integration.

1. The All-or-Nothing Approach

In many cases applying the integration factors, courts merely noted that the timing weighed in favor of integration and moved on to other factors.[112] However, other courts have adopted the viewpoint that this factor weighs in favor of integration anytime offers occur less than six months apart. These cases are an example of the "all-or-nothing" approach to the time factor. The all-or-nothing approach posits that "the factor might be established by a discrete line (six months, for example) and all sales within that six month period would be considered 'at or about the same time' and would count the same toward integration, whether such sales are one day apart or five months and twenty-nine days apart."[113]

For instance, in *Johnston*, the plaintiffs established a limited partnership and began selling interests in March 1982 and ended the offering in late December 1982.[114] The plaintiffs organized three more partnerships and began selling interests in early 1983 with the offering ending in December 1983.[115] Since the court did not find a six month interval between the end of the 1982 offers and the start of the 1983 offers, the court found

that this factor weighed in favor of integration.[116] Similarly, the court in *Melchior* found that this factor weighed in favor of integration because the offers began in September 1983 and ended in December 1984 with no six-month interval between offers.[117]

2. The Varying Weight Approach

While the courts in both *Johnston* and *Melchior* implicitly adopted the all-or-nothing approach, other cases indicate that a time lag of less than six months between offers can at least neutralize this factor.[118] These cases illustrate a "varying weight" approach to the time factor. Under a varying weight approach, the weight of the time factor varies depending on the temporal separation between the offers.[119]

For instance, in *Donohoe*, the court found this factor was "fairly neutral" when there were four limited partnership offerings that all occurred within twelve months of each other without a six month interval between offers.[120] In *Donohoe*, the defendants offered the first limited partnership in April 1983. The defendants followed this almost six months later with the second offering in October 1983. The third offering occurred in November 1983, and the fourth offering occurred approximately four months later in March 1984.[121] Unfortunately, the court did not opine on how this timing

sequence made the weight of this factor "fairly neutral". Certainly, the timing between the October and November offerings weighed in favor of integration.[122] Therefore, the court presumably made its determination on the nearly six month gap between the first and second offers and the four month gap between the third and fourth offers.[123]

From looking at the available authority, an issuer can clearly conclude that the timing factor weighs in favor of integration when the offers occur simultaneously, and, conversely, that offers occurring more than six months apart are not integrated.[124] Unfortunately, the time between zero and six months is a legal gray area shrouded in ambiguity with no clear timing delineation. However, as shown by *Donohoe*, the weight of this factor in favor of integration may diminish the further apart the offers occur, though the case law is widely split on the issue.[125]

D. Type of Consideration

The fourth factor relevant to the facts and circumstances inquiry under the integration doctrine is whether the purportedly separate offers received the same type of consideration (the "consideration" factor).[126] This factor weighs in favor of integration if the supposedly separate offers received the same type of consideration.[127] Of all five factors, this one is the most

straightforward and enjoys the most consistent interpretation by regulatory and judicial bodies.

Indeed, like the timing factor, this is a factor that issuers may concede. For instance, PNC told the SEC in its letter requesting a no-action letter, "It is recognized that both types of offerings involve . . . the same form of consideration...."[128] Similarly, F&M stated, "It is recognized that both types of offerings will be made at or about the same time, and the same form of consideration will be received therefor."[129]

1. The Insurance Letters

However, other issuers emphasize the difference in consideration as a key reason for non-integration. For instance, Metropolitan Life Insurance Company (MetLife) argued that the difference in consideration was a key reason not to integrate its offers. MetLife proposed a reorganization whereby MetLife would become a stock life insurance company controlled by a holding company. To carryout the reorganization, the holding company proposed to make two offers: 1) an Initial Public Offering for cash compensation and 2) an offer of stock in the holding company for existing policyholder membership interests.[130] John Hancock Financial Services,

Inc., the Standard Insurance Company, and The Canada Life Assurance Company made a nearly identical argument.[131]

In all of these nearly identical SEC no-action requests, the SEC staff agreed that integration was not necessary. However, the SEC staff responded to each with essentially the same statement, "While disagreeing with your analysis, the Division concurs in your view that the issuance of Holding Company common stock in the demutualization need not be integrated with the proposed offerings."[132] Unfortunately, the SEC staff did not elaborate on why the staff disagreed with the analysis or what aspects of the companies' arguments persuaded the staff that integration was unnecessary. However, this pattern of insurance letters shows that issuers rely on varying the form of consideration between offers by having one offer for cash and another for equity or debt as a major method of shifting the weight of this factor against integration.

2. Varying the Form of Consideration

Other SEC no-action letters have received more responsive answers from the staff with regards to its view of whether varying the form of consideration is a sufficient method to shift the weight of this factor against integration. In particular, all of the insurance letters listed above relied on

the Guarantee Mutual Life Company no-action letter, which proposed a similar type of transaction.[133] In Guarantee Mutual Life Company, the staff noted that the difference in consideration (i.e., cash for one offer and equity for another) was one of the two primary reasons for agreeing that integration was inappropriate.[134] In another example, the promoters of North American Leisure Group, Inc. proposed to receive cash from a Rule 504 offering and common stock from an offer made in conjunction with the incorporation of the company.[135] The staff agreed not to integrate the proposed offers and stated that it particularly noted in reaching its conclusion that the proposed offerings would involve different consideration.[136] Thus, the staff seems to support a view that varying the form of consideration is a sufficient method to shift the weight of this factor against integration.

Some of the case law has also addressed the question of whether varying the form of consideration is a sufficient method to satisfy this factor. For instance, in the case of *Goodwin Properties, LLC v. Acadia Group, Inc.*, the court found against integration because the form of consideration was different in the two offers.[137] In the first offer, the consideration was stock and corporate assets. In the second offer, the consideration was cash and loan forgiveness. The court in *Goodwin Properties* found these differences in consideration a sufficient basis to keep the offers separate.[138] Thus, the

law appears to be relatively clear that the consideration factor does not weigh in favor of integration when offers receive completely different forms of consideration.

3. Mixing the Form of Consideration

However, the law is not as clear when an issuer tries to mix the forms so that the offers receive some of the same form of consideration. Some of the authorities indicate that this factor does not weigh in favor of integration just because offers receive overlapping forms of mixed consideration. For instance, Farm Family Mutual Insurance Company (Farm Family) proposed to engage in two sets of offers. The first set of offers was a demutualization transaction that would primarily involve equity but would also involve cash.[139] The second set of offers was a Subscription Offering and a Public Offering designed to raise cash.[140] Despite the fact that cash was a component of the consideration in both sets of transactions, the staff agreed with Farm Family that integration was unnecessary and stated that the staff particularly noted that the offers would involve different forms of consideration.[141] However, this factor typically weighs in favor of integration when all transactions can involve cash.[142] The key distinction in Farm Family, therefore, may be that Farm Family aimed the first set of

offers primarily at receiving equity and received cash only on a limited basis.

Whatever the distinction in Farm Family may be, the authorities are clear that the form of consideration is the key to determining whether offers receive the same type of consideration. From examining the applicable authorities, an issuer can conclude that utilizing different forms of consideration may help shift the weight of this factor against integration. Conversely, use of the same form of consideration typically means that this factor will weigh in favor of integration.[143]

E. Same General Purpose

The fifth factor relevant to the facts and circumstances inquiry under the integration doctrine is whether the purportedly separate offers are for the same general purpose (the "general purpose" factor).[144] This factor weighs in favor of integration if the issuer makes the supposedly separate offers for the same general purpose. Unfortunately, the integration factors do not contain an explanation of what constitutes the same general purpose.[145] Indeed, the available authorities provide an issuer with little more than an opaque picture of what constitutes having the same general purpose. The most transparent fact that arises from a review of the authorities is that this

factor is often indistinguishable in application from the single plan of financing factor.

1. Relationship of the Purposes

The safe harbors have identified certain types of offers as automatically having a distinct general purpose. For instance, Rule 155 and Rule 251 provide that a proper employee benefit plan is a sufficiently distinct purpose to justify non-integration with other offers.[146] Similarly, Rule 701 provides that offers made as part of a proper employee compensation package are sufficiently distinct from other offers so that integration is unnecessary.[147] However, neither the safe harbors nor the SEC releases have adequately addressed how closely related the purposes of offers may be and still be considered offers for different general purposes.

The courts have addressed this issue in an effort to determine how closely related the purposes of offers must be in order to be considered having the same general purpose. For example, the *Walker* court addressed the defendants' argument that the purposes of their offers were different because the issuers used one offer as seed money for the partnership while they used the other offer for general operating expenses.[148] The court responded by saying, "Such a distinction between whether the proceeds of

an offering act as 'seed' money or working capital is insufficient to avoid integration."[149] Instead, the court found that the general purpose of both offers was to produce "'the total capitalization of the partnership'" for the purpose of investing in limited partnerships that owned and operated low income housing units.[150] Similarly, the court in *Melchior* found that a series of oil drilling partnerships were "engaged in the same purpose, oil exploration, in the same market, San Antonio."[151]

However, the courts are far from being in total agreement on this issue. The Seventh Circuit in *Donohoe* essentially adopted the district court's finding that "[t]o credit plaintiffs' theory [that the series of limited partnerships were engaged in the same general purpose, which was drilling for oil near Corsicana, Texas] would make it inordinately complex and expensive for anyone to fund, by way of limited partnerships, separate drilling programs in the same area--because by definition all such programs would have the same general purpose: to drill for oil."[152] The contrast between *Melchior* and *Donohoe* is stark and raises a great deal of ambiguity. In both cases, an issuer sold limited partnerships to fund separate drilling operations in the same general geographic area. However, the *Melchior* court found that the partnerships served the same general purpose while the *Donohoe* court reached the exact opposite conclusion. Unfortunately, the

Melchior court did not make any attempts to reconcile its conclusion with the one reached a year earlier in *Donohoe*.[153] However, it probably would not have made any difference because the two cases are patently irreconcilable.[154]

The SEC staff has provided a little more guidance than the courts to help issuers determine how distinct the purposes of offers must be to avoid having the general purpose factor weigh in favor of integration. The SEC staff seems to indorse the viewpoint that offers do not have the same general purpose just because the offers are integral to the existence of a business venture. For instance, Farm Family made an offer to demutualize its operations into a stock corporation, and Farm Family made an offer to raise operating capital for the resulting stock corporation.[155] The SEC staff decided that these offers were separate and cited the different purposes of the offers as a primary reason for its conclusion.[156] Similarly, the SEC staff did not find integration necessary when Guarantee Mutual Life Company made one offer to effect a demutualization and another offer to raise operating capital for the resulting stock corporation.[157]

From these two letters, an issuer can deduce that the SEC staff does not consider two offers that are both critical to the business venture as automatically having the same general purpose.[158] What appears to be

relevant is the relationship of the offers to the total business venture. However, the general purpose factor does not weigh in favor of integration just because the offers are critical to the total success of the business venture.[159] Unfortunately, though, the case law is unclear how closely related the critical tasks can be. *Walker* stands for the proposition that distinctions based on the difference between seed capital and operating capital are insufficient to avoid integration. Conversely, North American Leisure and Guarantee Mutual Life Company stand for the proposition that incorporation and operating capital are sufficiently distinct purposes. However, *Melchior* and *Donohoe* stand for diametrically opposed propositions that multiple limited partnerships engaged in the same business venture are offers made for the same general purpose.

2. Confusion with the Single Plan of Financing Factor

The general purpose factor entails more ambiguity than simply deciphering what the factor means. Namely, the analysis of the factor is difficult to separate from the single plan of financing factor. As mentioned during the discussion of single plan of financing factor in Section IV(A), *supra*, the analysis of this factor is confusingly similar to the single plan of financing factor.[160] For instance, the key to the single plan of financing

factor in *Johnston* was the fact that the limited partnership interests at issue were part of a "common business venture" while the key to the general purpose factor was the fact that the interests were "engaged in the same business in the same market."[161] Unfortunately, the court made no effort to elaborate on the difference between being in a common business venture and being engaged in the same business in the same market. Perhaps the court neglected to make such a distinction because no distinction really exists.

The *Murphy* decision is even better for highlighting the ambiguous differences between the single plan of financing and general purpose factors. In *Murphy*, the court listed all five factors and stated that only one, the time factor, did not weigh in favor of integration.[162] The court then gave a one sentence explanation of how the other factors weighed in favor of integration. However, the court combined its explanation of the single plan of financing and general purpose factors into one sentence that read, "Clearly, the offerings were all made for the same general purpose: they were part of one financing plan which Murphy aptly described, 'to give dollars to the cable operating company that could be used at a cost they could live with.'"[163] With this sentence, the *Murphy* court mashed together the two factors into one confused amalgamation that compressed the general purpose factor into the single plan of financing factor. Instead of

establishing separate facts to support its analysis of each factor, the court allowed the general purpose factor to weigh in favor of integration because the single plan of financing factor weighed in favor of integration.

However, *Murphy*'s amalgamation of these two factors is not unique. In *Donohoe* I, the court addressed the single plan of financing and general purpose factors by stating, "[T]hey were *not* part of a single plan of financing for the same general purpose."[164] In applying the facts to this statement, the court did not make any efforts to separate the single plan of financing factor from the general purpose factor. Instead, the court blended the facts into one collective argument.[165] Thus, the *Donohoe* I decision provides another example of how the general purpose factor is confused with the single plan of financing factor.

In all aspects, the general purpose factor is confusing and ambiguous. Judicial bodies confuse this factor with the single plan of financing factor making it difficult for issuers to understand. Furthermore, the authorities are very unclear on how to interpret the factor even when the authorities manage to separate this factor from the single plan of financing factor. While this factor typically analyzes the business relationship between the offers with an emphasis on the interdependence of the offers, the authorities are deeply split over how close the business relationship can be without tilting this

factor towards integration. The net result is to obscure this factor in a haze of ambiguity.[166]

F. Weighing the Factors

After examining some of the facts that are particularly relevant to each of the factors, the next question is how to apportion weight to the factors.[167] Unfortunately, though, divining how to apportion the weight is no less ambitious than interpreting what the factors mean. As pointed out by the court in *Cavanagh*, "[n]either [sic] the Commission nor the courts have provided express guidance on how to weigh these factors when analyzing an integration problem."[168] For instance, an issuer may wonder whether all of the factors are supposed to receive the same weight.[169] An issuer may also wonder whether courts can base a decision to integrate or not integrate on the weight of only one factor. In a related question, an issuer or lawyer may ask whether a proponent of integration must offer evidence on all five factors.[170]

1. How Many Factors Does Integration Require?

The law is relatively clear that proof of all five factors is not necessary to integrate offers. As the court in *Cavanagh* said, "Not all of these factors

need be established to justify a finding that transactions claimed to be separate were in fact one integrated transaction."[171] Furthermore, in the 1961 release, the SEC stated that any one or more of the factors may establish a case for integration.[172] The case law and administrative law have also generally held that all five factors are not necessary. For example, the court in *Murphy* concluded that the timing factor did not weigh in favor of integration but found that the other factors were sufficient to integrate the offers.[173] In *Kevin D. Kunz* I, the National Adjudicatory Council of the National Association of Securities Dealers, Inc. (the "council") stated that "the presence or absence of, or the weight given to, any one of the five factors listed above is not determinative."[174]

However, the case law is not in total agreement with this position. In *Goodwin Properties*, the plaintiffs sought to prove that the offer they purchased under should lose its registration exemption because the offer was part of a larger integrated offering that would not qualify for an exemption.[175] The court rejected the plaintiffs' argument because the plaintiffs failed to present evidence that the offers received the same type of consideration even though the plaintiffs presented evidence supporting integration on the remaining four factors. The court held that the integration factors constituted elements all of which the plaintiff had to present evidence

of to maintain a case for integration.[176] In reaching its conclusion, the court relied on *Johnston* for authority to require evidence of all five elements.[177]

In *Johnston*, the court found that the last four factors clearly weighed in favor of integration.[178] The issue, therefore, focused on whether the offerings were part of a single plan of financing. The plaintiffs, who were trying to avoid integration, argued that the defendant failed to satisfy the single plan of financing criteria. From the evidence presented, the court concluded that the offers involved a single plan of financing.[179] Therefore, the *Johnston* court ultimately concluded that all five factors favored integration. However, the court never held that evidence of all five factors was required for integration.[180] Therefore, the *Goodwin Properties* decision was probably an erroneous decision, at least with regards to its conclusion that the plaintiffs had to offer evidence of all five factors for the court to integrate the offers.[181]

If proof of all five factors is unnecessary, then an issuer might ask whether a court may base integration on only one factor. An issuer could conclude that one factor is a sufficient basis to support integration based on the 1961 Securities Act Release listing the five factors.[182] However, proof of more than one factor is probably necessary in practice.[183] For instance, in *Kevin D. Kunz* I, the council concluded that the class of securities factor

weighed in favor of integration but stated that such a determination did not end the inquiry.[184] The council stated, "[W]e cannot say that the 'class of security' factor, standing alone, militates for or against integration."[185] Instead, the council held that it must base a decision to integrate on "the totality of the circumstances."[186] Issuers seem to have enough confidence in this proposition that some are willing to concede one or more of the factors and still hope to maintain a successful argument for non-integration on the balance of the remaining factors.[187] If courts routinely based integration on only one factor, then issuers probably would be very reluctant to make any concessions.[188]

2. How Much Weight Does Each Factor Deserve?

The available authorities indicate that the factors do not necessarily deserve the same weight. According to the court in *Cavanagh*, "A review of the cases and no-action letters strongly suggests that the 'single plan of financing' and 'same general purpose' factors normally are given greater weight than the other factors."[189] The council in *Kevin D. Kunz* I also stated that it placed greater weight on these two factors and cited *Cavanagh* as support for doing so.[190]

Indeed, many court decisions support the viewpoint of *Cavanagh* and *Kevin D. Kunz* I. In many cases, courts based the decision to integrate or not integrate on one of these two factors. As anecdotal evidence, this author reviewed several cases that analyzed the five factors. Unfortunately, most of the cases do not specifically state which factors the court found most persuasive. However, *Goodwin Properties* was the only one of the cases examined that reached a conclusion entirely on the basis of a factor other than the single plan of financing or general purpose factor.[191] Of the other cases, three primarily placed the emphasis on the single plan of financing and general purpose factors.[192] Three other cases relied on both the single plan of financing and general purpose factors among other factors.[193] Three other cases relied on the general purpose factor, among others.[194] This anecdotal analysis lends at least some support for the proposition that the single plan of financing and general purpose factors are the most important.[195]

The SEC staff has been more direct than the courts in adopting the position that the single plan of financing and general purpose factors are the most important factors. For instance, in Sonnenblick, Parker, & Selvers, the SEC staff decided in favor of integration and noted that it considered these two factors "to be most important to a determination whether to integrate the

offerings."[196] There is also sufficient anecdotal evidence among the no-action letters to support this proposition. This author reviewed several no-action letters where the SEC staff's response to the question of integration included a clear reference to the factors the staff relied on in reaching its conclusion.[197] Of the letters: a) one letter primarily relied on all five factors,[198] b) four letters primarily relied on the single plan of financing and general purpose factors,[199] c) four letters primarily relied on the consideration and general purpose factors,[200] and d) one letter primarily relied on the class of securities factor.[201] Therefore, out of the no-action letters surveyed, only one of the letters did not rely on the general purpose factor.[202] This anecdotal analysis supports the findings in the case analysis, especially for the general purpose factor.

This anecdotal review of the case law and SEC no-action letters reveals a pattern of greater reliance on the single plan of financing and general purpose factors. The general purpose factor appears to be especially important to the analysis as evidenced by the fact all but two of the cases and no-action letters relied on the general purpose factor. Even though the single plan of financing factor was not quite as prevalent, an issuer should remember that the single plan of financing and general purpose factors are

often confused and combined so the single plan of financing factor may be more relevant than this relatively succinct review reveals.

Thus, an issuer or lawyer may reach several reasonably transparent conclusions about how courts and the SEC staff weigh the integration factors. First, all five factors are at least somewhat important to the analysis.[203] Second, the single plan of financing and general purpose factors are especially important.[204] Third, all of the factors do not have to be present.[205] Fourth, no one factor is always dispositive.[206] However, the clarity ends abruptly when an issuer tries to delve deeper into any of these conclusions. While all five factors are somewhat important, some factors seem to be far more important than others but none of the authorities provide any guidance for an issuer trying to determine how to apportion weight to the factors. Furthermore, even though all of the factors do not have to be present, there is no guidance to say how many factors have to be present. Cases like *Goodwin Properties* make the analysis even more ambiguous by contradicting, or at least clouding, these fairly well-established conclusions.

V. Addressing the Ambiguity

Many scholars have offered a wide-spectrum of suggestions to resolve the ambiguity.[207] These suggestions include shortening the temporal safe

harbors to three months, reducing the number of factors by eliminating the consideration and general purpose factors, creating a safe harbor for offers that involve different forms of consideration, and providing a "rational business reason" exception to integration.[208] Another suggestion has been the complete elimination of the integration doctrine and the five factors.[209]

Many of these suggestions have a great deal of merit and deserve serious consideration by the SEC. However, some of the measures proposed may be extreme and would take considerable political will to implement. While it is possible that some of the more radical proposals may be the best solution to the problem, this author would like to suggest, at the risk of sounding cliché, that the SEC should not sacrifice the good in a pursuit of the best. In other words, radical solutions typically take considerable time and political effort, which could lead to the abandonment of any reform efforts. Therefore, it would be better for the SEC to pursue a conservative, manageable strategy to reduce the ambiguity. The SEC can accomplish this by issuing a new release clarifying the facts and circumstances most relevant to each factor as established by existing precedent. Considering it has been more than forty years since the SEC created the five factors, a release designed merely to clarify and standardize the five factors is long overdue.

The SEC should begin by identifying the three main sources of ambiguity currently surrounding the factors. Some of the ambiguity comes from the vagueness as to which facts are relevant to each factor. Another source of ambiguity is the confusion of the single plan of financing and general purpose factors, which is due to the lack of clearly delineated facts relevant to each factor. The final major source of ambiguity is the uncertainty of how to weigh the factors. The SEC release should make an effort to reduce the ambiguity caused by each of these sources.

1. Clearly Establish the Relevant Facts

The first major source of ambiguity is the uncertainty as to which facts are relevant for each factor. To reduce this ambiguity, the SEC release should specifically identify facts that are relevant to each factor and provide interpretive guidance for analyzing the facts under each factor. Precedent should guide the release so that the results do not unduly affect issuers relying on the existing authorities. Furthermore, careful drafting of the explanation of each factor could also eliminate the ambiguity between the single plan of financing and general purpose factors.

For the single plan of financing factor, the most important facts currently relied on are whether subsequent offers are contemplated during

the first set of offers, whether the offers involve the same type of business venture or plan, whether each offering can stand or fall on its own merits, and whether the offers rely on different offering techniques such as varying the market where the offerings are made or using different methods to sell the offers. Facts such as whether the offers involve the same type of business venture or plan and whether each offering can stand or fall on its own merits are more readily confused with the general purpose factor than others.[210] To reduce confusion, the release should explicitly shift those facts to the general purpose factor.[211] The release should focus the attention of this factor on whether the issuer contemplates subsequent offers during the first set of offers and whether the offers rely on different offering techniques such as varying the market where the issuer makes the offerings or using different methods to sell the offers.

The SEC release should consider making the following statements to clarify this factor:

> The single plan of financing factor is used to weigh the similarity between offers by gauging differences in the mechanics of how and why the offers are made. The more similar the mechanics of how and why the offers are made, the more likely the offers are integrated. A relevant fact is whether the issuer contemplates

subsequent offers during the first set of offers. *See Walker*, 736 F. Supp. at 1365. If an issuer contemplates the need to make additional offers at the time of the first offers, then this indicates that all of the offers are part of a single plan of financing. *See* Independent News, Inc., SEC No-Action Letter, 1977 WL 10972 (Aug. 22, 1977). Another relevant fact is whether the issuer relies on different offering techniques such as varying the market or geographical location where the issuer makes the offers or using different methods to sell the offers. *See* Citicorp, SEC No-Action Letter, 1976 WL 12639 (Sep. 20, 1976) *and* Pittsburg National Corp., SEC No-Action Letter, 1977 WL 10903 (August 15, 1977) *and* First & Merchants Corp., SEC No-Action Letter, 1978 WL 13000 (July 27, 1978). Greater similarities between the offering techniques indicate the offers should be integrated.

For the class of securities factor, the most important facts currently relied on are whether the offers belong to the same type, category, or subcategory of securities. The main problem is that the courts do not agree on whether categorical or sub-categorical variations are relevant.[212] The release should resolve this split by unequivocally stating that all variations are relevant regardless of whether the variations are at the type, category, or

subcategory levels.[213] The release should not try to restrain the types of variations that issuers may present to distinguish offers except to the extent that precedential authority has singled out certain variations as having special significance or non-significance as the case may be.[214]

Therefore, the SEC release should consider making the following types of statements:

> The same class of securities factor is used to weigh the similarity between offers by determining whether the offers provide essentially the same class of securities. The greater the similarities between the class of securities, the more likely the offers are integrated. This factor should be weighed by examining all of the variations that may exist between the securities regardless of whether those variations exist in the type, category, or subcategory of securities offered. *Accord Doran,* 545 F.2d at 901 n.9. However, variations based solely on the tax treatment of the securities are irrelevant. *See id. and Walker*, 736 F. Supp. at 1365 *and Melchior*, 1993 WL 89141, at *10. Furthermore, variations in the type of securities should shift the weight of this factor against integration provided that the securities are not convertible into the same type of securities. *See Kunz D. Kunz*, Exchange Act Release 2002 WL

54819, at *7 *and* Black Box, Inc., SEC No-Action Letter, 1992 WL 55818 (Feb. 28, 1992).

For the time factor, the most relevant fact is how far apart in time the offers occurred. Of course, the safe harbors automatically exempt from integration offers separated by at least six months with no intervening offers.[215] However, the courts are currently split as to whether this factor automatically weighs in favor of integration if the offers occur within six months or whether the weight of this factor varies on the temporal proximity of the offers.[216] The release should clearly state that the weight of this factor varies on the temporal separation of the offers since the "all-or-nothing" approach makes this factor completely meaningless. Otherwise, this factor would weigh in favor of integration in every case since any offers separated by at least six months would qualify for a safe harbor and skip the five factor analysis altogether. Furthermore, the SEC should provide a time-line to guide issuers and courts in determining how specific temporal separations will affect the weight of this factor.

For instance, the SEC release should state something similar to the following:

> The time factor is used to weigh the similarity between offers by determining whether the offers are separated by a sufficient

temporal period to distinguish the offers. The weight of this factor shifts more towards integration the closer in time the offers occur, and the weight shifts against integration as the time between the offers increases. Courts should apportion the weight of this factor based on the following time-line: 0-1 Months Separation (Completely in Favor of Integration); 1-2 Months Separation (Somewhat in Favor of Integration); 2-4 Months Separation (Neutral); 4-5 Months Separation (Somewhat in Favor of Non-Integration); 5-6 Months Separation (Completely in Favor of Non-Integration). *See generally Donohoe*, 982 F.2d at 1140.

For the consideration factor, the most relevant fact is whether the issuer offered the securities for the same form of consideration. Most authorities agree that this factor weighs in favor of non-integration if the offers receive different forms of consideration.[217] The main question is whether this factor weighs in favor of integration if the offers receive a mixed form of consideration that includes some overlap in the form of consideration received. The release should resolve this question by stating that this factor does not weigh in favor of integration when the offers receive a different form of consideration, even if there is some overlap in the form as a result of mixed consideration.

For example, the SEC release should state something similar to the following:

> The consideration factor is used to weigh the similarity between offers by determining whether the offers receive the same form of consideration. If offers receive the same form of consideration, then this factor should weigh in favor of integration. Conversely, this factor should weigh against integration if the offers involve a different form of consideration. *See* Guarantee Mutual Life Company, SEC No-Action Letter, 1995 WL 256250 (Apr. 13, 1995) *and Goodwin Properties*, 2001 WL 800064, at *9. The fact that some overlap in the form of consideration exists should have no material impact on the weight of this factor in offers that receive a mixed form of consideration. *See* Farm Family Mutual Ins. Co., SEC No-Action Letter, 1996 WL 157393 (Apr. 2, 1996).

For the general purpose factor, the most relevant fact is the closeness of the relationship between the purposes of the offers. This should be determined by considering whether the offers involve the same type of business venture or plan and whether each offering can stand or fall on its own merits.[218] The release needs to clarify that the general purpose of the offers can be critical to the overall success of a business venture without

automatically shifting the weight of this factor towards integration.[219] The release also needs to clarify that the business ventures can be very similar so long as the success of each business depends on its own merits.[220] Also, the release should state that this factor does not weigh in favor of integration when the issuer uses the proceeds of offers with otherwise identical business purposes in clearly different geographical regions.[221] Furthermore, the release should unambiguously state that this factor considers different facts than the single plan of financing factor and, therefore, judges should not confuse the two factors.[222]

The SEC release should state something similar to the following:

> The same general purpose factor is designed to weigh the similarity between offers by determining whether the offers are designed to fulfill the same general purpose. This factor weighs in favor of integration if the offers fulfill the same general purpose. Courts should not confuse this factor with the single plan of financing factor despite any past confusion that might have existed. Questions relevant to this analysis are whether the offers involve the same type of business venture or plan and whether each offering can stand or fall on its own merits. Courts should analyze these questions from the perspective of each offer rather than from the perspective of the

issuer. Simply because the offers are critical to the success of an overall business venture does not mean that this factor weighs in favor of integration. *See* Farm Family Mutual Ins. Co., SEC No-Action Letter, 1996 WL 157393 (Apr. 2, 1996) *and* Guarantee Mutual Life Company, SEC No-Action Letter, 1995 WL 256250 (Apr. 13, 1995). This factor does not weigh in favor of integration if the offers create separate, even if very similar, business ventures that can succeed or fail on their own merits. *See Donohoe*, 982 F.2d at 1140. Furthermore, this factor should not weigh in favor of integration if the issuer uses the proceeds of the offers in distinct geographic regions separated by at least 350 miles. *See* Tele-Tower, Inc., SEC No-Action Letter, 1978 WL 13141 (Feb. 27, 1978) *and* Daseke & Company, Inc. Floyd R. Hardesty Syndications, SEC No-Action Letter, 1975 WL 11315 (May 2, 1975).

2. Clearly Establish How to Weigh the Factors

Another major source of ambiguity is the confusion surrounding how to weigh the factors.[223] The release needs to clear up two major points on this topic to reduce the ambiguity. First, the release needs to identify how

many factors must weigh in favor of integration to justify a finding. Second, the release needs to clarify how much weight to apportion each factor.

For the first point, the release should reject the *Goodwin Properties* decision and adopt the generally accepted approach that all five factors do not have to weigh in favor of integration to support such a finding and, consequently, the party challenging the exemption does not have to present evidence on all five factors.[224] The release should also reject the 1961 Release and require proof of more than one factor to justify integration. Issuers do not have sufficient certainty if courts can base integration on only one factor. If courts can base integration on only one factor, then courts can integrate otherwise completely distinct offers just because the offers occur simultaneously, receive the same consideration, or happen to overlap in some other regard. This ridiculous result ignores the point of having five factors to judge an offering.[225]

For the second point, the release should provide clear guidance on how to weigh the factors. The single plan of financing and general purpose factors traditionally weigh more than the other three factors.[226] Indeed, the authorities almost always cite the general purpose factor as a reason to support a finding for or against integration.[227] While authorities cite the single plan of financing factor frequently, authorities rely on this factor less

often than the general purpose factor. Furthermore, it is possible that the confusion with the general purpose factor accounts for the somewhat greater reliance on the single plan of financing factor over the other factors. Therefore, the single plan of financing factor should probably receive less weight than the general purpose factor, though it might be entitled to more weight than the other factors.

After the single purpose factor, the class of securities factor seems the most useful for determining whether to integrate offers since there is relatively well established precedent that sufficient variation in the class of securities is a strong basis for non-integration.[228] Therefore, the class of securities factor should receive more weight than the time or consideration factors. The time factor should receive more weight than the consideration factor since offers separated by at least six months with no intervening offers automatically qualify for a safe harbor.[229] It is therefore reasonable to conclude that offers occurring nearly six months apart are more likely to be distinct since six months automatically means the offers are distinct. In other words, the fact that five months and twenty-nine days separate offers is more relevant than the type of consideration received. Therefore, the release should rank the weight of the factors in descending order from the general

purpose to the single plan of financing to the class of securities to the time to the consideration.

Also, the release could give issuers a little more certainty by assigning a numeric value to these weights. For instance, the release could assign each factor a maximum number of points with judicial discretion to determine how many possible points the facts support for each factor. For example:

> General Purpose (15 points possible), Single Plan of Financing (10 points possible), Class of Securities (7 points possible), Time (5 points possible), Consideration (3 points possible)—the total number of points must exceed twenty-five (25) to support a finding of integration.

Alternatively, the SEC release could assign weighted percentages to each factor. For example:

> General Purpose (40%), Single Plan of Financing (25%), Class of Securities (20%), Time (10%), and Consideration (5%).

Even without the adoption of a numeric scale, the SEC release should at least state something similar to the following:

> The five factors represent a balancing test and are not elements that must all be proven by an issuer or plaintiff to support integration or non-integration. *Cf. Goodwin Properties*, 2001 WL 800064, at *9

(requiring the plaintiffs to present proof of all five factors) and *Cavanagh*, 1 F. Supp.2d at 364 (finding that proof of all five factors is not necessary to justify integration). Therefore, proof of all five factors is not necessary to integrate offers. However, courts should not base integration on only one factor. In analyzing the factors, courts should afford the most weight to the general purpose factor. *See Cavanagh*, 1 F. Supp.2d at 364. After the general purpose factor, courts should afford the most weight to the single plan of financing factor. After the single plan of financing factor, courts should afford the most weight to the time factor. Courts should afford the least weight to the consideration factor.

By issuing a new release on the five factors, the SEC could eliminate much of the ambiguity surrounding the factors. A release does not need to create new law but merely should collect existing precedent into one cohesive and comprehensible format. A release would promote uniform adjudication in the courts and provide issuers with a greater degree of certainty than they currently have. Furthermore, issuing a release that merely clarifies and standardizes the existing precedent would not compromise the investor protection motivations behind the integration doctrine.

VI. Conclusion

The five factor test is the method an issuer uses to prove that the facts and circumstances surrounding purportedly separate offers do not call for integration.[230] However, the five factors are inherently ambiguous. Neither the SEC nor the courts have made the meaning of these factors sufficiently clear since the début of the factors in 1961. Therefore, an issuer may wonder what facts and circumstances are relevant to the analysis and how the factors weigh together.[231]

An analysis of the applicable authority reveals that certain facts are particularly relevant for each of the factors, though the authorities are often contradictory and usually provide only a vague sense of what is important to consider. For the single plan of financing factor, particularly relevant facts appear to be whether subsequent offers are contemplated during the first set of offers, whether the offers involve the same type of business venture or plan, whether each offer has economic substance, and whether the offers rely on different offering techniques such as varying the market where the offerings are made or using different methods to sell the offers.[232] However, some of these facts are easily confused with the general purpose factor. Furthermore, the exact meaning of these facts is uncertain.

For the class of securities factor, particularly relevant facts appear to be whether the securities fit in the same type, category, and subcategory.[233] However, the authorities are not in uniform agreement on the relevancy of these facts. Furthermore, the authorities do not agree on what facts are relevant to establishing type, category, or subcategory distinctions. The confusion is so great that some courts will not even consider sub-categorical variations.

For the time factor, some authorities hold that the weight of this factor varies depending on the temporal separation.[234] However, other authorities say that any time-frame less than six months weighs in favor of integration.[235] As a result, there is widespread ambiguity as to how to consider the time factor.

For the consideration factor, particularly relevant facts appear to be that the offers receive a different form of consideration or at least a different mix of consideration.[236] Even though this is the most transparent factor, even with this factor, the law is not completely clear, particularly with regards to whether offers with overlapping forms of consideration weigh in favor of integration.[237]

For the general purpose factor, a particularly relevant fact appears to be whether the offers essentially fulfill an identical task; however, the law is

unclear how closely related the critical tasks can be.[238] Unfortunately, judges have made the fifth factor more ambiguous by confusing this factor with the single plan of financing factor and blending the two factors into one convoluted factor.[239]

The authority is also unclear on the subject of weighing the factors. What is clear is that all five factors are at least somewhat important to the analysis.[240] What is unclear is whether evidence on all five factors has to be present to support a finding of integration.[241] However, the authorities are a little clearer that no one factor is all important.[242] Nevertheless, the law indicates that the single plan of financing and general purpose factors are especially important.[243] Unfortunately, though, there is simply no clear guidance on how to weigh the factors.

Thus, the SEC needs to produce a new release to clarify nearly every aspect of the five factor test. The release needs to explain the facts that are relevant to each factor. The release also needs to clearly delineate the difference between the single plan of financing and general purpose factors. In addition, the release needs to detail how courts should analyze and weigh the factors.

Ambiguity will continue to reign over the five factors until the SEC issues a sufficiently clear release. No one gains from the current ambiguity;

it does not benefit the SEC, the courts, or issuers. There is no reason to continue the ambiguity created by the 1961 and 1962 releases. With a new release based on existing precedent, the SEC could squelch much of the ambiguity that currently leads to contradictory and confused interpretations of the factors.

However, until the SEC issues a new release to clarify the integration factors, issuers must review the existing authority to search for clues as to the relevant facts. By reviewing the authority interpreting the integration doctrine, an issuer can take the first steps towards deciphering the integration factors into a comprehensible analytical framework. Through identifying and exploring the facts and circumstances that seem to have relevance in the analysis, an issuer can better understand how to structure transactions to avoid integration or to determine whether purportedly separate offers are actually part of the same transaction. Nevertheless, achieving a complete understanding of the factors is a task made futile by ambiguity. No matter how Herculean the effort, an issuer is incapable of clearing away the decades of ambiguous interpretations surrounding the factors. At this time, only the SEC has the wherewithal to do that.

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[1] The Five Factors are:

1. whether the offerings are part of a single plan of financing;

2. whether the offerings involve issuance of the same class of security;

3. whether the offerings are made at or about the same time;

4. whether the same type of consideration is to be received;

5. whether the offerings are made for the same general purpose.

See Section 3(a)(11) Exemption for Local Offerings, Securities Act Release 1961 WL 61651 (Dec. 6, 1961).

[2] The Securities Act applies to both sales of securities and offers to sell securities. For simplicity, the term "offer" is used to include both offers and sales unless otherwise noted.

[3] *See* Integration of Abandoned Offerings, Securities Act Release 74 S.E.C. Docket 571 (Jan. 26, 2001).

[4] *See* C. Steven Bradford, *Transaction Exemptions in the Securities Act of 1933: An Economic Analysis*, 45 EMORY L.J. 591, 650 (1996). Congress believed that the key to investor protection lay in requiring issuers of securities to provide investors with accurate and comprehensive financial information relating to an investment. To accomplish this goal, the Securities Act requires issuers to disclose that information through the process of registering the securities. *See generally* Alan R. Bromberg, *Texas Business Organization and Commercial Law—Two Centuries of Development*, 55 SMU L. REV. 83, 108 (2002).

[5] Since the process of registering securities is usually very onerous and expensive, especially for small issuers or issuers wishing to offer only a small number of securities, Congress provided exemptions from registration to allow small or private offerings to have easier access to the capital markets under circumstances in which investors are still likely to have adequate protection. *See* LOLA MIRANDA HALE, REGULATION A: SMALL BUSINESS FINANCING EXEMPTION § 5.1 (1997) *and* Stephen Knute Gregg, *Regulation A Initial Public Offerings on the Internet: A New Opportunity for Small Business?*, 1 J. SMALL & EMERGING BUS. L. 417, 425 (1997) *and* C. Steven Bradford, *The SEC's New Regulation CE Exemption: Federal-State Coordination Run Rampant*, 52 U. MIAMI L. REV. 429, 430 (1998) *and* David T. Mittelman, *Testing-the-Waters: How Warm is Regulation A's Model for Soliciting Investor Interest?*, 32 SUFFOLK U.

L. REV. 233, 264 (1998) *and* Securities Act of 1933 §§ 3(b) *and* 4(2), 15 U.S.C.A. §§ 77c(b) *and* 77d(2) (West 2003).

[6] *See* C. Steven Bradford, *Regulation A and the Integration Doctrine: The New Safe Harbor*, 55 OHIO ST. L.J. 255, 258 (1994). *See also* MARC I. STEINBERG, UNDERSTANDING SECURITIES LAW 34-35, 62-63 (2001) *and* Daniel J. Morrissey, *Integration of Securities Offerings: The ABA's "Indiscreet" Proposal*, 26 ARIZ. L. REV. 41, 48-49 (1984).

[7] *See SEC v. Melchior*, 1993 WL 89141, at *8-*9 (D. Utah Jan. 14, 1993).

[8] *See* Securities Act of 1933 § 12(a)(1), 15 U.S.C.A. § 77l(a)(1) (West 2003). *See also Donohoe v. Consolidated Operating & Production Corp.,* 982 F.2d 1130, 1140 (7th Cir. 1992).

[9] A Section 5 violation carries strict liability, which means that "[t]he exercise of reasonable care or bona fide but unsuccessful efforts to perfect an exemption from registration are irrelevant." STEINBERG, *supra* note 6, at 174. Additionally, the issuer may face a SEC enforcement action for violating Section 5. While the defendant's degree of scienter is a factor in granting an SEC injunction brought for violation of Section 5, the SEC could, at least in theory, still enjoin an issuer who attempted to comply with the securities laws with the utmost good faith but nonetheless committed a Section 5 violation. *See Melchior*, 1993 WL 89141, at *17. Furthermore, the issuer could be subject to SEC money penalties even for a technical violation. *See* STEINBERG, *supra* note 6, at 368.

Both the SEC and the courts interpret and apply the integration doctrine and the five factor test. For simplicity, this article will sometimes refer to the SEC or the courts meaning both the courts and the SEC.

[10] *See* Regulation D Revisions; Exemption for Certain Employee Benefit Plans, Securities Act Release 37 S.E.C. Docket 588 (January 16, 1987). *See, e.g.,* 17 C.F.R. § 230.502 (2003) *and* Standard Ins. Co., SEC No-Action Letter, 1999 WL 46696 (Jan. 26, 1999) *and* Equitable Capital Management Corp., SEC No-Action Letter, 1992 WL 18810 (Jan. 6, 1992).

[11] *See, e.g.,* 17 C.F.R. § 230.502 *and* Standard Ins. Co., SEC No-Action Letter, 1999 WL 46696 (Jan. 26, 1999) *and* Equitable Capital Management Corp., SEC No-Action Letter, 1992 WL 18810 (Jan. 6, 1992).

[12] *See* The Canada Life Assurance Co., SEC No-Action Letter, 1999 WL 812254 (Oct. 12, 1999).

[13] *See* 17 C.F.R. §§ 230.155 *and* 230.502 (2003).

[14] *See Donohoe,* 982 F.2d at 1140. *See also* Bradford, *supra* note 4, at 651.

[15] Another way to avoid the five factors is to sell securities overseas in a Regulation S offering. Regulation S allows an issuer to conduct an offering outside the United States without being concerned that a court will integrate the transaction with offers made in the United States even if the issuer makes the offers contemporaneously. *See* 17 C.F.R. § 230.502. Regulation S states that offers made outside the United States are not subject to Section 5 of the Securities Act. *See* Offshore Offers and Sales, Securities Act, Exchange Act, and Investment Company Act Release 46 S.E.C. Docket 52 (Apr. 24, 1990). Section 5 of the Securities Act prohibits the offer of unregistered securities without an exemption. *See Melchior*, 1993 WL 89141, at *8-*9. Therefore, an issuer does not have to register securities offered outside the United States. *See* Offshore Offers and Sales, Securities Act, Exchange Act, and Investment Company Act Release 46 S.E.C. Docket 52 (Apr. 24, 1990). Since offshore offers are not subject to Section 5, the SEC reasoned that it should not integrate such offers with domestic offers. *See id. See also* Bradford, *supra* note 6, 268.

However, the SEC stated that an issuer may not use Regulation S as a vehicle to evade registration requirements. *See* Offshore Offers and Sales, Securities Act, Exchange Act, and Investment Company Act Release 46 S.E.C. Docket 52 (Apr. 24, 1990). In cases where the issuer's intent is to avoid registration, Regulation S is unavailable even if the issuer meets the technical requirements of the regulation. *See id. See, e.g., Dietrich v. Baur*, 126 F. Supp.2d 759, 761 (S.D.N.Y. 2001) (involving a suit based on allegations of a scheme to sell unregistered securities in the United States through a fraudulent use of Regulation S). Furthermore, the antifraud provisions of the securities laws still apply. *See* Offshore Offers and Sales, Securities Act, Exchange Act, and Investment Company Act Release 46 S.E.C. Docket 52 (Apr. 24, 1990).

Regulation S provides an issuer safe harbor to assist issuers who want to be certain they do not violate Section 5. *See Robert G. Weeks,* 2002 WL 169185, at *11 (SEC Feb. 4, 2002). In crafting Regulation S and the issuer safe harbor, the SEC wanted to be sure that it did not endanger U.S. investors. The SEC was particularly concerned with the risk of securities flowing back to the U.S. market "where there is little (if any) information available to the marketplace about the issuer and its securities." Offshore Offers and Sales, Securities Act, Exchange Act, and Investment Company Act Release 46 S.E.C. Docket 52 (Apr. 24, 1990). The SEC, therefore, divided the safe harbor provisions into different categories

depending on the type of securities offered based on the theory that certain securities, such as debt instruments, are less likely to flowback into the U.S. market. *See id.* The SEC also tailored the safe harbor to treat registered-issuers different from unregistered-issuers based on the theory that a flowback of a registered-issuer's securities would cause less harm because of the information available to the public. *See id.* Essentially, the SEC designed the safe harbor to allow unregistered offshore offers so long as there is a reasonable likelihood the securities will not return to the United States before the offering comes to rest.

The SEC justified Regulation S by arguing that Section 5 only applies to the territorial limits of the United States since the goal of registration is "to protect the U.S. capital markets and investors purchasing in the U.S. market, whether U.S. or foreign nationals." *Id.* The SEC argued that offshore governments were responsible for providing their own investor protections, even if the issuer was from the United States. *See id.* The SEC's rationale, therefore, is that foreign governments will provide the necessary protection to investors in foreign nations, though the U.S. antifraud provisions may still apply. *See id.* Americans, on the other hand, are adequately protected because an issuer faces a possible Section 5 violation if the securities flow back to the United States unless the issuer can prove compliance with a safe harbor. *See Robert G. Weeks,* 2002 WL 169185, at *11. Since the SEC designed the safe harbor to prevent flowback, the SEC allows an issuer to conduct offshore offers without having those offers affect domestic offers. Hence, the integration doctrine does not act to add Regulation S offers to other offers. *See* The Canada Life Assurance Co., SEC No-Action Letter, 1999 WL 812254 (Oct. 12, 1999).

[16] *See* Integration of Abandoned Offerings, Securities Act Release 74 S.E.C. Docket 571 (Jan. 26, 2001).

[17] *See id.* The SEC designed Rule 155 largely to clarify some of the ambiguity associated with Rule 152, which is another safe harbor that provides protections similar to those afforded in Rule 155. However, Rule 152 has been notoriously difficult to understand; so, the SEC adopted Rule 155 to ameliorate some of the problems associated with Rule 152. *See id*. *Accord* The Regulation of Securities Offerings, Securities Act Release, Exchange Act Release, Investment Company Act Release 1998 WL 792508 (Nov. 17, 1998).

[18] *See* Integration of Abandoned Offerings, Securities Act Release 74 S.E.C. Docket 571 (Jan. 26, 2001).

[19] *See* 17 C.F.R. § 230.502.

[20] *See* Integration of Abandoned Offerings, Securities Act Release 74 S.E.C. Docket 571 (Jan. 26, 2001).

[21] *See* 17 C.F.R. § 230.502. *See also* Revision of Certain Exemptions from Registration for Transactions Involving Limited Offers and Sales, Securities Act Release 1982 WL 125672 (March 16, 1982). There is a limited exception to allow offers of the same or similar securities through an employee benefit plan without affecting the six-month waiting period. *See* 17 C.F.R. §§ 230.502 *and* 230.405 (2003).

[22] *See* 17 C.F.R. § 230.502.

[23] *See* 17 C.F.R. § 230.147 (2003).

[24] *See id.*

[25] *See* 17 C.F.R. § 230.251 (2003).

[26] *See id.*

[27] *See* 17 C.F.R. § 230.701 (2003). *See also* THOMAS LEE HAZEN, LAW OF SECURITIES REGULATION § 4.17[5] (2003 update).

[28] *See* Compensatory Benefit Plans and Contracts, Securities Act Release 1988 WL 263350 (Apr. 20, 1988).

[29] *Id.*

[30] Assuming the offer was not part of a plan or scheme to evade the registration requirements of the Act. *See, e.g., id. and* 17 C.F.R. §§ 230.155, 230.501, *and* 230.701 (Preliminary Notes) (2003).

[31] *See* Bradford, *supra* note 4, at 650-51.

[32] *See* Section 3(a)(11) Exemption for Local Offerings, Securities Act Release 1961 WL 61651 (Dec. 6, 1961).

[33] The entire paragraph containing the five factors is reprinted here to illustrate the extreme brevity with which the SEC introduced the five factors:

> The determination of what constitutes an 'issue' is not governed by state law. Shaw v. U.S., 131 F. 2d 476,480 (C.A. 9, 1942). Any one or more of the following factors may be determinative of the question of integration: (1) are the offerings part of a single plan of financing; (2) do the offerings involve issuance of the same class of security; (3) are the offerings made at or about the same time; (4) is the same type of consideration to be received, and (5) are the offerings made for the same general purpose.

Id.

[34] The release referred to what is now known as Section 4(2) as "the second clause of Section 4(1)." Non-Public Offering Exemption, Securities Act Release 1962 WL 69540 (Nov. 6, 1962).

[35] Courts often cite the 1962 release as the basis for applying the five factors as the integration test when the issuer cannot perfect a safe harbor. *See, e.g., Donohoe*, 982 F.2d at 1140 *and SEC v. Murphy*, 626 F.2d 633, 645 (9th 1980) *and SEC v. Cavanagh,* 1 F. Supp.2d 337, 364 (S.D.N.Y. 1998), *aff'd SEC v. Cavanagh,* 155 F.3d 129 (2d 1998) *and Steed Finance LDC v. Nomura Securities Intern., Inc.*, 2001 WL 1111508, at *6 (S.D.N.Y. Sept. 20, 2001) (citing *Cavanagh* and *Murphy*).

[36] The entire paragraph containing the five factors is reprinted here to illustrate the even greater brevity with which the SEC reissued the five factors in the 1962 release:

> A determination whether an offering is public or private would also include a consideration of the question whether it should be regarded as a part of a larger offering made or to be made. The following factors are relevant to such question of integration: whether (1) the different offerings are part of a single plan of financing, (2) the offerings involve issuance of the same class of security, (3) the offerings are made at or about the same time, (4) the same type of consideration is to be received, (5) the offerings are made for the same general purpose.

Non-Public Offering Exemption, Securities Act Release 1962 WL 69540 (Nov. 6, 1962).

[37] *Id.*

[38] The omission of the "one or more" language in the 1962 release could lead a judge to conclude that the SEC changed its approach to the five factors. From the omission, a judge might draw the conclusion that more than one factor is necessary or, perhaps, that all five factors are necessary. Though the courts are split as to how many factors are necessary (see Section IV(F)(1), *infra*), this author is unaware of any authority that traces the root of the split back to the change in language from the 1961 release to the 1962 release.

[39] *Accord* Bradford, *supra* note 4, at 651. Of note, some commentators argue that the five factors are really a "subterfuge" to allow courts to base integration on other considerations. Bradford, *supra* note 6, at 266.

[40] *Accord* Bradford, *supra* note 4, at 651 (stating, "The exact meaning of each of these factors has never been totally clear. The two SEC releases that established the five factor test made no attempt to explain it, and subsequent SEC interpretations have been confusing."). The factors are so vague that an SEC

commissioner commented in a recent speech that reliance on the five factors "creates significant uncertainty" for an issuer. Commissioner Roel C. Campos, Remarks at the Twenty-First Annual Government-Business Forum on Small Business Capital Formation (Sept. 26, 2002) (transcript available at 2002 WL 31484905). *See also* C. Steven Bradford, *Expanding the Non-Transactional Revolution: A New Approach to Securities Registration Exemptions*, 49 EMORY L.J. 437, 439 (2000).

[41] *Compare Melchior,* 1993 WL 89141, at *9 *with Donohoe*, 982 F.2d at 1140 (reaching different results in the application of the fifth factor on substantially similar facts).

[42] *See* Rutheford B. Campbell, *The Overwhelming Case for Elimination of the Integration Doctrine Under the Securities Act of 1933*, 89 KY. L.J. 289, 289 (2001). *See, e.g.,* BancOhio Financial Corporation, SEC No-Action Letter, 1979 WL 11320 (May 10, 1979) (stating in response to a question about integration that "[b]ecause of the possibility that staff positions on the integration concept may be misconstrued and misapplied in other situations, we will no longer be issuing interpretations in this area. Rather, it is our position that counsel, with the guidance of Release No. 33-4552, should make a determination as to whether or not particular offerings should be integrated.") *and* Associates Corp. of N. Am., SEC No-Action Letter, 1979 WL 13715 (May 10, 1979) (stating in response to a question about integration that "[b]ecause of the complexity of the proposed arrangements and the possibility that staff positions on the integration concept may be misconstrued and misapplied in other situations, we will not be issuing interpretations in this area any longer. Rather, it is our position that counsel, with the guidance of Release No. 33-4552, should make a determination as to whether or not particular offerings should be integrated.") *and* Crosswinds Enterprises, SEC No-Action Letter, 1979 WL 14049 (July 9, 1979 (stating in response to a question about integration that "Because of the complexity of the proposed arrangements and the possibility that staff positions on the integration concept may be misconstrued and misapplied in other situations, we will not be issuing interpretations in this area any longer. Rather, it is our position that counsel, with the guidance of Release No. 33-4434, should make a determination as to whether or not particular offerings should be integrated.").

[43] *See* 17 C.F.R. § 230.251. *See also* Bradford, *supra* note 4, at 651. The SEC or the private party challenging the validity of an exemption has the initial burden of presenting facts that the issuer violated the registration process. *See Murphy*, 626 F.2d at 641. If the validity of an exemption turns on whether

offers are integrated, then the challenging party must introduce evidence supporting a finding of integration under the five factor test. *See Goodwin Properties, LLC v. Acadia Group, Inc*., 2001 WL 800064, at *13 (D. Me. July 17, 2001). The burden of proof shifts to the issuer to prove that the exemption is valid once the challenging party has introduced evidence against the validity of the exemption. *See SEC v. Ralston Purina Co.*, 346 U.S. 119, 126 (1953) *and Doran v. Petroleum Management Corp.,* 545 F.2d 893, 899 (5th 1977) *and Murphy*, 626 F.2d at 641. *See also Johnston v. Bumba*, 764 F. Supp. 1263, 1273-74 (N.D. Ill. 1991). In the integration context, this means that the issuer must present or rebut facts analyzed by the five factors to prove that a court should not integrate the offers. *See Goodwin Properties*, 2001 WL 800064, at *13.

[44] *See* 17 C.F.R. § 230.251. *See also* Bradford, *supra* note 4, at 651.

[45] Non-Public Offering Exemption, Securities Act Release 1962 WL 69540 (Nov. 6, 1962).

[46] *See id*. *Accord Steed Finance LDC*, 2001 WL 1111508, at *6.

[47] *See* Non-Public Offering Exemption, Securities Act Release 1962 WL 69540 (Nov. 6, 1962).

[48] *See* Campbell, *supra* note 42, at 307. For a complete discussion of the same general purpose factor, see Section IV(E), *infra*.

[49] *See Walker v. Montclaire Housing Partnership*, 736 F. Supp. 1358, 1365 (M.D.N.C. 1990).

[50] *See id.* at 1363-64.

[51] *See id.* at 1364-65. The court concluded that the PPM's highlighting Mr. Hill's involvement evidenced the fact that the issuers contemplated the subsequent offers at the same time the issuers made the offer to Mr. Hill. *See id.*

[52] *See id.* at 1365 (citing *Livens v. William D. Witter, Inc.,* 374 F. Supp. 1104, 1107 (D. Mass. 1974) *and* Sonnenblick, Parker & Selvers, SEC No-Action Letter, 1986 WL 66490 (Jan. 1, 1986)).

[53] *See* Independent News, Inc., SEC No-Action Letter, 1977 WL 10972 (Aug. 22, 1977).

[54] *See id.*

[55] *Accord* Morrissey, *supra* note 6, at 62 (discussing a case where a court did not find a single plan of financing when the only intent of the issuer was to issue securities when an attractive opportunity presented itself). *See also* Bradford, *supra* note 4, at 652.

[56] *See* Pittsburg National Corp., SEC No-Action Letter, 1977 WL 10903 (August 15, 1977) *and* First & Merchants Corp., SEC No-Action Letter, 1978 WL 13000 (July 27, 1978).

[57] *See, e.g.,* Pittsburg National Corp., SEC No-Action Letter, 1977 WL 10903 (August 15, 1977) *and* First & Merchants Corp., SEC No-Action Letter, 1978 WL 13000 (July 27, 1978).

[58] *See* Pittsburg National Corp., SEC No-Action Letter, 1977 WL 10903 (August 15, 1977) *and* First & Merchants Corp., SEC No-Action Letter, 1978 WL 13000 (July 27, 1978).

[59] *See* First & Merchants Corp., SEC No-Action Letter, 1978 WL 13000 (July 27, 1978).

[60] Pittsburg National Corp., SEC No-Action Letter, 1977 WL 10903 (August 15, 1977).

[61] *See, e.g., Johnston,* 764 F. Supp. at 1272.

[62] *See id.* at 1268-69. The facts of *Johnston* are also discussed in Section IV(C)(1) in reference to the timing of the offers.

[63] *See id*. at 1272.

[64] *See id. Accord Kevin D. Kunz*, Exchange Act Release 2002 WL 54819, at *7 (N.A.S.D. Administrative Proceeding Jan. 16, 2002) [hereinafter *Kunz* II] (finding a single plan of financing where the purpose of all PPMs was to finance the issuer's mortgage lending and trust deed business).

[65] Of course, these same questions could apply to other types of business ventures such as LLCs.

[66] *See Cavanagh*, 1 F. Supp.2d at 344.

[67] *See id.* at 365.

[68] *See Donohoe*, 982 F.2d at 1140. The facts of *Donohoe* are also discussed in Section IV(C)(2) in reference to the timing of the offers.

[69] *See id.* at 1133-34.

[70] *See id.* at 1140.

[71] *See id.*

[72] For a complete discussion on the general purpose factor and the ambiguity between the two factors, see Section IV(E)(2), *infra.*

[73] *See* Non-Public Offering Exemption, Securities Act Release 1962 WL 69540 (Nov. 6, 1962). *Accord Steed Finance LDC*, 2001 WL 1111508, at *6.

[74] *See generally* Campbell, *supra* note 42, at 308.

[75] *See generally Kunz* II, *supra* note 64, at *8.

[76] *See id.*

[77] *See id*. For more on the facts of *Kunz* II, see Section IV(B)(2), *infra*.

[78] *See* Black Box, Inc., SEC No-Action Letter, 1992 WL 55818 (Feb. 28, 1992).

[79] *See, e.g., id.*

[80] *See generally Kunz* II, *supra* note 64, at *7. *See also Walker*, 736 F. Supp. at 1365 (asserting that securities of the same category, such as limited partnerships, are always the same class while implying the possibility that a categorical variation [e.g., a limited partnership interest versus an LLC membership interest] could be relevant). For more on *Walker*'s view of variations, see Section IV(B)(3), *infra*.

[81] *See Kunz* II, *supra* note 64, at *8.

[82] *See id.*

[83] The Commission added a footnote criticizing the defendant's argument for ignoring the fact that the notes had exactly the same maturity period, a fact that indicated the securities were in the same class despite any categorical differences. *See id.* at *8 n.45.

[84] *See Walker*, 736 F. Supp. at 1365. For more on the facts of *Walker*, see Section IV(A)(1), *supra*.

[85] *See id.*

[86] *See id.* (citing *Murphy*, 626 F.2d 633 and *Currie v. Cayman Resources Corp.*, 595 F. Supp. 1364 (D.C. Ga. 1984)).

[87] *See Murphy*, 626 F.2d at 646.

[88] *Id.*

[89] *Accord id.* at 637-39.

[90] *See Currie*, 595 F. Supp. at 1369-70.

[91] *See id.* at 1377.

[92] *See id.* at 1369-70.

[93] *See Doran,* 545 F.2d at 897.

[94] *See id.*

[95] *See id.* at 898.

[96] *See id.* at 901 n.9.

[97] *See id.*

[98] *See id.*

[99] *See id.*

[100] Of note, *Doran* seems to have established a precedent that a distinction based solely on tax advantages is an insufficient basis to show that securities are in a different class. *See Walker*, 736 F. Supp. at 1365 *and Melchior*, 1993 WL 89141, at *10.

[101] *See* Resolution Trust Corp., SEC No-Action Letter, 1991 WL 176870 (July 18, 1991).

[102] Even though this question arose under the ICA, the staff applies the same facts and circumstances integration analysis to this type of question as it does to integration questions under Section 4(2) of the Securities Act. Therefore, the staff's interpretation of this question should be relevant to other integration questions. *See* Joseph H. Moss, SEC No-Action Letter, 1984 WL 45009 (Feb. 27, 1984).

[103] *See* Resolution Trust Corp., SEC No-Action Letter, 1991 WL 176870 (July 18, 1991).

[104] *Accord id.* In another no-action letter, the staff concluded that integration was unnecessary when the issuer argued that the securities in question had different interest rates. *See* First & Merchants Corp., SEC No-Action Letter, 1978 WL 13000 (July 27, 1978).

[105] Of note, if the issuer offers different classes of securities, then the courts and the SEC often will not integrate. *See, e.g.,* Resolution Trust Corp., SEC No-Action Letter, 1991 WL 176870 (July 18, 1991) (finding non-integration and noting that the staff's opinion was especially influenced by the difference in the class of securities offered) *and* Citicorp, SEC No-Action Letter, 1976 WL 12639 (Sep. 20, 1976) (finding non-integration and noting "[t]he Notes and the commercial paper are not a single or similar class of security.") *and* Agri-Quip, SEC No-Action Letter, 1974 WL 9638 (Sep. 20, 1974) (finding non-integration and noting "the offering involves entirely different classes of securities, one equity and one debt."). *See also* Bradford, *supra* note 4, at 652 (stating, "When different classes of securities are offered, the courts and the SEC generally will not integrate, even if the differences between the two classes are small.") *and* Cheryl L. Wade, *The Integration of Securities Offerings: A Proposed Formula That Fosters the Policies of Securities Regulation*, 25 LOY. U. CHI. L.J. 199, 217 (1994) (stating, "Generally, the courts and SEC staff have found offerings non- integrable where the types of securities offered are clearly different, such as an offering of common stock and an offering of preferred stock.").

[106] *See* Non-Public Offering Exemption, Securities Act Release 1962 WL 69540 (Nov. 6, 1962). *Accord Steed Finance LDC*, 2001 WL 1111508, at *6.

[107] *See* 17 C.F.R. §§ 230.147, 230.251, *and* 230.502. Of course, an issuer cannot use the safe harbor if the issuer's intent was to evade the securities laws. *See, e.g.,* 17 C.F.R. § 20.502 (Preliminary Note 6) (stating "In view of the objectives of these rules and the policies underlying the Act, Regulation D is not available to any issuer for any transaction or chain of transactions that, although in technical compliance with these rules, is part of a plan or scheme to evade the registration provisions of the Act. In such cases, registration under the Act is required.").

[108] *See* Judith D. Fryer, *Integration Issues in Real Estate Securities Offerings*, 9 No. 5 Insights 13, at *16 (1995).

[109] *See* Blue Cross & Blue Shield of Va., SEC No-Action Letter, 1996 WL 330514 (June 14, 1996).

[110] *See id.*

[111] *See* First & Merchants Corp., SEC No-Action Letter, 1978 WL 13000 (July 27, 1978). For more on the facts of F&M, see Section IV(A)(2), *supra*.

[112] *See, e.g., Doran*, 545 F.2d at 901 n.9.

[113] Campbell, *supra* note 42, at 308.

[114] *See Johnston,* 764 F. Supp. at 1268-69. For more on the facts of *Johnston*, see Section IV(A)(3), *supra*.

[115] *See id*. at 1269.

[116] *See id*. at 1272.

[117] *See Melchior*, 1993 WL 89141, at *10. The court cited offers made September 1983-December 1983, April 1984-August 1984, and September-December 1984. Thus, the longest gap between offers appears to be four months, though the court did not make it completely clear in the record that no offers took place between December 1983 and April 1984. *See id.* at *2-3.

[118] *See id.* at *10 *and Johnston,* 764 F. Supp. at 1272.

[119] *See* Campbell, *supra* note 42, at 308-09.

[120] *Donohoe*, 982 F.2d at 1140. For more on the facts of *Donohoe*, see Section IV(A)(3), *supra*.

[121] *See id.* at 1134.

[122] *Accord Walker*, 736 F. Supp. at 1365 (finding that the timing factor weighed in favor of integration when the first set of offers ended on November 1, 1985 and the second set of offers commenced a little more than one month later on December 15, 1985).

[123] The court in *Murphy* added to this ambiguity with its analysis of the integration factors. In *Murphy*, the court found that all of the factors weighed in favor of integration except the timing factor. Unfortunately, the court did not provide a detailed time-line of the four hundred limited partnership interests that the defendants sold from 1971-1974. *See Murphy*, 626 F.2d at 646.

[124] *See, e.g.,* 17 C.F.R. § 230.502.

[125] In the Independent News, Inc. no-action letter, the SEC staff raised an interesting possibility concerning this factor. The issuer in Independent News, Inc. proposed a second set of offers at the same time that another set of offers was still in effect. However, the issuer argued that it really did not make the offers at the same time because the first set of offers was still in effect only because the issuer had not yet sold the total principal amount of the first offers. The SEC staff reiterated this argument as one of the reasons supporting its conclusion not to integrate the offers. *See* Independent News, Inc., SEC No-Action Letter, 1977 WL 10972 (Aug. 22, 1977). This no-action letter seems to imply that the time factor should not weigh in favor of integration if the overlap in time was merely coincidental or unintended.

The Independent News no action letter presents several interesting interpretations of the factors. Even though Independent News is more than twenty-five years old, neither the SEC nor the courts have overturned or explicitly modified the letter.

[126] *See* Non-Public Offering Exemption, Securities Act Release 1962 WL 69540 (Nov. 6, 1962). *Accord Steed Finance LDC*, 2001 WL 1111508, at *6.

[127] *See generally* HAZEN, *supra* note 27, § 4.36[4][A] (noting that issuing securities for different types of consideration can militate against integration).

[128] Pittsburg National Corp., SEC No-Action Letter, 1977 WL 10903 (August 15, 1977).

[129] First & Merchants Corp., SEC No-Action Letter, 1978 WL 13000 (July 27, 1978).

[130] *See* Metropolitan Life Ins. Co., SEC No-Action Letter, 1999 WL 1063264 (Nov. 23, 1999).

[131] *See* John Hancock Financial Services, Inc., SEC No-Action Letter, 1999 WL 101812 (Nov. 8, 1999) (stating, “The Holding Company will receive cash consideration in the IPO. By contrast, the

extinguishment of Membership Interests in the Company is the consideration that is ultimately received by the Holding Company in consideration for issuing Holding Company Stock to Eligible Policyholders in the Demutualization.") *and* Standard Ins. Co., SEC No-Action Letter, 1999 WL 46696 (Jan. 26, 1999) (stating, "The Holding Company will receive cash consideration in the Initial Public Offering which differs from the consideration, the extinguishment of members' Membership Interests, received by Standard and the Holding Company in consideration for issuing Holding Company Stock to Eligible Members in the demutualization.") *and* The Canada Life Assurance Co., SEC No-Action Letter, 1999 WL 812254 (Oct. 12, 1999) (stating, "The Holding Company will receive cash consideration for the issuance of primary shares in the Offerings, which differs from the consideration to be received in the demutualization transaction, consisting of the extinguishment of the Ownership Interests of Eligible Policyholders.").

[132] The Canada Life Assurance Co., SEC No-Action Letter, 1999 WL 812254 (Oct. 12, 1999).

[133] *See id. and* Metropolitan Life Ins. Co., SEC No-Action Letter, 1999 WL 1063264 (Nov. 23, 1999) *and* John Hancock Financial Services, Inc., SEC No-Action Letter, 1999 WL 101812 (Nov. 8, 1999) *and* Standard Ins. Co., SEC No-Action Letter, 1999 WL 46696 (Jan. 26, 1999).

[134] *See* Guarantee Mutual Life Company, SEC No-Action Letter, 1995 WL 256250 (Apr. 13, 1995) (citing the different purposes of the offer as the second reason for non-integration).

[135] *See* N. Am. Leisure Group, Inc., SEC No-Action Letter, 1988 WL 235271 (Dec. 15, 1988).

[136] *See id.*

[137] *See Goodwin Properties*, 2001 WL 800064, at *9. *Goodwin Properties* was decided by a magistrate judge pursuant to 28 U.S.C.A. § 636 (West 2003). Therefore, the decision was technically only a recommendation. However, the district court did not reject the magistrate's recommendation.

[138] *See id.*

[139] *See* Farm Family Mutual Ins. Co., SEC No-Action Letter, 1996 WL 157393 (Apr. 2, 1996).

[140] *See id.*

[141] *See id.*

[142] *See, e.g., Donohoe,* 982 F.2d at 1140 *and Murphy*, 626 F.2d at 646 *and Walker*, 736 F. Supp. at 1365 *and Melchior,* 1993 WL 89141, at *10.

[143] The SEC staff also raised an interesting possibility concerning this factor in the Independent News, Inc. no-action letter. The issuer in Independent News, Inc. proposed two offers that would both receive cash consideration. The first offers were debentures and the second offers were limited partnership interests. The issuer argued that the cash received in the debenture offers was "more in the nature of debt," while the cash received in the limited partnership offers was "more in the nature of capital." Independent News, Inc., SEC No-Action Letter, 1977 WL 10972 (Aug. 22, 1977). The SEC staff reiterated this argument as one of the reasons supporting its conclusion not to integrate the offers. *See id.* This no-action letter seems to imply that the consideration factor should not weigh in favor of integration even if all offers receive cash consideration so long as the "nature" of the cash is different. Unfortunately, the staff did not elaborate on what this truly means. However, the argument seems to be that the purpose or form of the cash receipts can dictate whether offers received the same consideration.

[144] *See* Non-Public Offering Exemption, Securities Act Release 1962 WL 69540 (Nov. 6, 1962). *Accord Steed Finance LDC*, 2001 WL 1111508, at *6.

[145] Furthermore, courts often confuse this factor with the "single plan of financing" factor and, in practice, the factors often involve consideration of the same facts. *See* Campbell, *supra* note 42, at 307.

[146] *See* 17 C.F.R. §§ 230.155 *and* 230.251. For more on this topic, see Section II, *supra*.

[147] *See* 17 C.F.R. § 230.701. For more on this topic, see Section II, *supra*.

[148] *See Walker*, 736 F. Supp. at 1365. For more on the facts of *Walker*, see Section IV(A)(1), *supra*.

[149] *Id.*

[150] *Id.*

[151] *Melchior,* 1993 WL 89141, at *10.

[152] *Donohoe*, 982 F.2d at 1140.

[153] In fact, *Melchior* did not even cite *Donohoe*.

[154] The most viable distinction between the cases is the fact that there was a great deal of fraud and misconduct on the part of the defendants in the *Melchior* case, which might have influenced the court's perception of the situation. *See generally Melchior*, 1993 WL 89141, at *18 (discussing the fact that numerous documents were backdated and falsified). When the law is so ambiguous that judges can reasonably reach multiple outcomes (as is the case with the five factor test), there may be a tendency on the

part of a judge to favor the interpretation that punishes a party who engaged in clearly fraudulent activity. *See generally* Steven M. Bainbridge and G. Mitu Gulati, *How Do Judges Maximize? (The Same Way Everybody Else Does—Boundedly): Rules of Thumb in Securities Fraud Opinions*, 51 EMORY L.J. 83, 90, 108 (2002). Nevertheless, the *Melchior* and *Donohoe* decisions applied the general purpose factor in completely opposite manners, which is bad for an issuer trying to determine whether a judge will integrate offers.

[155] *See* Farm Family Mutual Ins. Co., SEC No-Action Letter, 1996 WL 157393 (Apr. 2, 1996). For more on the facts in Farm Family, see Section IV(D)(2), *supra*.

[156] *See id.*

[157] *See* Guarantee Mutual Life Company, SEC No-Action Letter, 1995 WL 256250 (Apr. 13, 1995).

[158] *Accord* N. Am. Leisure Group, Inc., SEC No-Action Letter, 1988 WL 235271 (Dec. 15, 1988) (deciding against integration when the first offer was for the purpose of incorporation and the second offer was to raise capital).

[159] *See* Guarantee Mutual Life Company, SEC No-Action Letter, 1995 WL 256250 (Apr. 13, 1995) *and* N. Am. Leisure Group, Inc., SEC No-Action Letter, 1988 WL 235271 (Dec. 15, 1988).

[160] *See* Wade, *supra* note 105, 213-14.

[161] *Johnston*, 764 F. Supp. at 1272. For more on the facts in *Johnston*, see Section IV(A)(3) and Section IV(C)(1), *supra*.

[162] *See Murphy*, 626 F.2d at 646. For more on the facts in *Murphy*, see Section IV(B)(3), *supra*.

[163] *Id.*

[164] *Donohoe v. Consolidated Operating & Production Corp.* I, 736 F. Supp. 845, 877 (N.D. Ill. 1990), *vacated in part and aff'd in part,* 982 F.2d 1130 (7th Cir. 1992) (affirming the portion of the district court's decision relevant to the analysis of the integration factors) (italics in original).

[165] *Id.*

[166] *Accord* Wade, *supra* note 105, at 214-16.

[167] *See* Bradford, *supra* note 40, at 462.

[168] *Cavanagh,* 1 F. Supp.2d at 364.

[169] *See, e.g.,* N. Am. Leisure Group, Inc., SEC No-Action Letter, 1988 WL 235271 (Dec. 15, 1988) (stating in the request for non-integration, "The SEC has consistently applied the criteria stated above [the five factors] on integration issues, but it is unclear how much weight is to be given to each criterion.").

[170] *See, e.g., Goodwin Properties,* 2001 WL 800064, at *9 (requiring proof of all five factors to integrate the offers at issue).

[171] *Cavanagh*, 1 F. Supp.2d at 364. For more on the facts in *Cavanagh*, see Section IV(A)(3), *supra.*

[172] *See* Section 3(a)(11) Exemption for Local Offerings, Securities Act Release 1961 WL 61651 (Dec. 6, 1961). For more on the wording of the 1961 release, see Section III, *supra.*

[173] *See Murphy*, 626 F.2d at 646.

[174] *Kevin D. Kunz,* 1999 WL 1022141, at *16 (National Adjudicatory Council/NASD July 7, 1999) [hereinafter *Kunz* I].

[175] *See Goodwin Properties,* 2001 WL 800064, at *9.

[176] *See id.* The plaintiff must present evidence to challenge the validity of a claimed registration exemption before the burden of proving the exemption shifts to the defendant. The court in *Goodwin Properties* required the plaintiffs to offer evidence of all five factors before shifting the burden to the defendant. However, based on other authorities, this is the wrong result because a court can integrate offers on less than all five factors. *See, e.g., Murphy*, 626 F.2d at 646 *and Cavanagh*, 1 F. Supp.2d at 364 *and Kunz* I*, supra* note 174, at *16. Therefore, the court should not have required the plaintiffs to present evidence of all five factors to shift the burden of proof. *Accord* J. WILLIAMS HICKS, CIVIL LIABILITIES: ENFORCEMENT AND LITIGATION UNDER THE 1933 ACT § 6:18 n. 24 (2001). For more on the burden of proof, see Section IV, n. 43, *supra.*

Of note, the *Goodwin Properties* decision has been criticized on other points as well. For instance, one scholar asserted that the court in *Goodwin Properties* misinterpreted the First Circuit's *Maldonado v. Dominguez,* 137 F.3d 1 (1st Cir. 1998) decision, which dealt with Section 12(a)(2) of the Securities Act, and misused the *Maldonado* decision as authority to dismiss a Section 12(a)(1) claim. *See* HICKS, *supra* note 176, § 5:18 n. 14.

[177] *See Goodwin Properties,* 2001 WL 800064, at *9.

[178] *See Johnston,* 764 F. Supp. at 1272. For more on the facts in *Johnston*, see Section IV(A)(3) and Section IV(C)(1), *supra.*

[179] *See id.* The court stated that its conclusion would be the same even if the plaintiffs' version of the facts was true; so, the court did not reach a conclusion as to which version of the facts was true.

[180] *See generally id.*

[181] *Accord Cavanagh,* 1 F. Supp.2d at 364 (stating, "Not all of these factors need be established to justify a finding that transactions claimed to be separate were in fact one integrated transaction.").

[182] *See* Section 3(a)(11) Exemption for Local Offerings, Securities Act Release 1961 WL 61651 (Dec. 6, 1961). *See also* Section III, n.38, *supra*.

[183] Of course, the safe harbors provide for non-integration on the basis of only one fact. In other words, certain facts (such as a six month temporal separation) are so indicative of non-integration that the SEC has built safe harbors around those facts. So, while the safe harbors operate around only one fact, they do so merely because the SEC has singled out those facts as especially influential. *See, e.g.,* 17 C.F.R. § 230.502. Therefore, just because the safe harbors turn on the presence or absence of one fact does not mean that the factor analysis should operate the same way.

[184] *See Kunz* I, *supra* note 174, at *16.

[185] *Id.*

[186] *Id.*

[187] *See* Fryer, *supra* note 108, at *16. *See, e.g.,* Blue Cross & Blue Shield of Va., SEC No-Action Letter, 1996 WL 330514 (June 14, 1996) (conceding the time factor) *and* Pittsburg National Corp., SEC No-Action Letter, 1977 WL 10903 (August 15, 1977) (conceding the consideration factor) *and* First & Merchants Corp., SEC No-Action Letter, 1978 WL 13000 (July 27, 1978) (conceding the time factor and the consideration factor).

[188] *But cf. Goodwin Properties,* 2001 WL 800064, at *9.

[189] *Cavanagh,* 1 F. Supp.2d at 364. *See also* Bradford*, supra* note 4, at 651 (noting that these factors tend to overlap).

[190] *See Kunz* I, *supra* note 174, at *17.

[191] *See Goodwin Properties*, 2001 WL 800064, at *9 (finding non-integration on the basis that the plaintiffs failed to provide evidence of the consideration factor).

[192] *See Donohoe*, 982 F.2d at 1140 (finding non-integration based primarily on the single plan of financing and general purpose factors) *and Cavanagh*, 1 F. Supp.2d at 365 (finding integration based primarily on the single plan of financing and general purpose factors) *and Walker*, 736 F. Supp. at 1364-65 (finding integration on all five factors but placing particular emphasis on the single plan of financing and general purpose factors).

[193] *See Doran*, 545 F.2d at 901 n.9 (finding integration based primarily on the single plan of financing, time, consideration, and general purpose factors) *and Kunz* II, *supra* note 64, at *7-8 (finding integration based primarily on the single plan of financing, time, consideration, and general purpose factors) *and Murphy*, 626 F.2d at 646 (finding integration based primarily on the single plan of financing, class of securities, consideration, and general purpose factors).

[194] *See Currie*, 595 F. Supp. at 1377 (finding integration based primarily on the class of securities, consideration, and general purpose factors) *and Johnston*, 764 F. Supp. at 1272 (finding integration based primarily on the class of securities, time, consideration, and general purpose factors) *and Melchior*, 1993 WL 89141, at *10 (finding integration based primarily on the time, class of securities, consideration, and general purpose factors).

[195] In other words, 90% of the cases relied on the general purpose factor, 70% on the consideration factor, 60% on the single plan of financing factor, 40% on the time factor, and 40% on the class of securities factor.

[196] Sonnenblick, Parker & Selvers, SEC No-Action Letter, 1986 WL 66490 (Jan. 1, 1986).

[197] Unfortunately, many of the staff responses simply stated that the staff did not consider integration necessary based on the facts presented in the request for no-action without being more specific as to which factors were most persuasive. *See, e.g.*, Standard Ins. Co., SEC No-Action Letter, 1999 WL 46696 (Jan. 26, 1999) *and* Metropolitan Life Ins. Co., SEC No-Action Letter, 1999 WL 1063264 (Nov. 23, 1999) *and* Anthem Insurance Companies, Inc., SEC No-Action Letter, 2001 WL 1314739 (Oct. 25, 2001).

[198] *See* Independent News, Inc., SEC No-Action Letter, 1977 WL 10972 (Aug. 22, 1977) (finding non-integration based primarily on the single plan of financing, class of securities, time, consideration, and general purpose factors).

[199] *See* Pittsburg National Corp., SEC No-Action Letter, 1977 WL 10903 (August 15, 1977) (finding non-integration based primarily on the single plan of financing and general purpose factors) *and* Charles E. Watters, SEC No-Action Letter, 1978 WL 13303 (May 24, 1978) (finding integration based primarily on the single plan of financing and general purpose factors) *and* Pacific Physician Services, Inc., SEC No-Action Letter, 1985 WL 55629 (Aug. 20, 1985) (finding non-integration based primarily on the single plan of financing and general purpose factors) *and* Sonnenblick, Parker & Selvers, SEC No-Action Letter, 1986 WL 66490 (Jan. 1, 1986) (finding non-integration based primarily on the single plan of financing and general purpose factors).

[200] *See* N. Am. Leisure Group, Inc., SEC No-Action Letter, 1988 WL 235271 (Dec. 15, 1988) (finding non-integration based primarily on the consideration and general purpose factors) *and* Guarantee Mutual Life Company, SEC No-Action Letter, 1995 WL 256250 (Apr. 13, 1995) (finding non-integration based primarily on the consideration and general purpose factors) *and* Farm Family Mutual Ins. Co., SEC No-Action Letter, 1996 WL 157393 (Apr. 2, 1996) (finding non-integration based primarily on the consideration and general purpose factors) *and* Blue Cross & Blue Shield of Va., SEC No-Action Letter, 1996 WL 330514 (June 14, 1996) (finding non-integration based primarily on the consideration and general purpose factors).

[201] *See* Resolution Trust Corp., SEC No-Action Letter, 1991 WL 176870 (July 18, 1991) (finding non-integration based primarily on the class of securities factor).

[202] In other words, 90% of the letters relied on the general purpose factor, 50% on the consideration factor, 50% on the single plan of financing factor, 10% on the time factor, and 20% on the class of securities factor.

[203] *See* Section 3(a)(11) Exemption for Local Offerings, Securities Act Release 1961 WL 61651 (Dec. 6, 1961).

[204] *See Cavanagh,* 1 F. Supp.2d at 364.

[205] *See Murphy*, 626 F.2d at 646.

[206] *Kunz* I, *supra* note 174, at *16.

[207] *See* Bradford, *supra* note 40, at 471.

[208] *See id.* at 471 n.214.

[209] *See* Campbell, *supra* note 42, *passim*.

[210] For more on this topic, see Section IV(E)(2), *supra*.

[211] Shifting consideration of the business plan entirely to the general purpose factor should also shift the current case law split on whether this fact should be judged from the perspective of the issuer or the offer. *See Cavanagh*, 1 F. Supp.2d at 364-65 (standing for the proposition that the single plan of financing factor should be judged from the perspective of the issuer) *and Donohoe*, 982 F.2d at 1140 (standing for the proposition that the single plan of financing factor should be judged from the perspective of each offer). The SEC release should address this issue and clearly state that courts should judge the business plan from the perspective of each offer because the alternative produces a ridiculous result. If judged from the issuer's perspective, nearly every offer will have the same business plan since the issuer almost always plans to make money. Judging the business plan from the perspective of each offer makes true differences between business plans more apparent.

[212] *See, e.g., Kunz* II, *supra* note 64, at *8 (questioning whether securities ostensibly belonging to different categories were distinct enough to belong to different classes) *and Walker*, 736 F. Supp. at 1365 (rejecting sub-categorical variations as a basis for finding that offers belong to different classes).

[213] *Accord Doran,* 545 F.2d at 901 n.9. As a public policy matter, courts should consider all relevant facts to determine whether offers are really integrated. It is unfair to an issuer to ignore legitimate variations that may distinguish offers just because the variations are categorical or sub-categorical.

[214] Specifically, several courts have concluded that variations in tax benefits are an insufficient basis to support non-integration. *See id. and Walker*, 736 F. Supp. at 1365 *and Melchior*, 1993 WL 89141, at *10. Precedent also supports the notion that *bona fide* type variations automatically shift the weight of this factor against integration. *See Kunz* II, *supra* note 64, at *7. However, a type variation is not *bona fide* if the offers are convertible into the same type of security. *See* Black Box, Inc., SEC No-Action Letter, 1992 WL 55818 (Feb. 28, 1992).

[215] *See generally* 17 C.F.R. § 230.502.

[216] *Cf. Johnston*, 764 F. Supp. at 1272 (finding that this factor weighs in favor of integration if the offers occur less than six months apart) *and Donohoe*, 982 F.2d at 1140 (finding that the weight of this factor varies on the temporal separation of the offers).

[217] *See, e.g.,* Guarantee Mutual Life Company, SEC No-Action Letter, 1995 WL 256250 (Apr. 13, 1995) *and Goodwin Properties*, 2001 WL 800064, at *9.

[218] *See* Section V(1)*, supra*.

[219] *See* Farm Family Mutual Ins. Co., SEC No-Action Letter, 1996 WL 157393 (Apr. 2, 1996) *and* Guarantee Mutual Life Company, SEC No-Action Letter, 1995 WL 256250 (Apr. 13, 1995).

[220] *Cf. Melchior,* 1993 WL 89141, at *10 (holding that the same general purpose factor weighed in favor of integration because the purpose of multiple oil drilling limited partnerships was to search for oil even though all of the partnerships functioned independently from each other) *and Donohoe*, 982 F.2d at 1140 (holding that the same general purpose factor weighed in favor of non-integration even though all of the oil drilling limited partnerships were searching for oil since each partnership functioned independently from the others).

[221] *See* Tele-Tower, Inc., SEC No-Action Letter, 1978 WL 13141 (Feb. 27, 1978) (finding non-integration when the issuer proposed to use the proceeds of offers in different shopping malls across the country) *and* Daseke & Company, Inc. Floyd R. Hardesty Syndications, SEC No-Action Letter, 1975 WL 11315 (May 2, 1975) (finding non-integration when the issuer proposed to use the proceeds of offers in six geographically distinct construction projects located in three different states). The SEC should establish a bright-line to determine whether the issuer will use the proceeds in distinct geographical areas. A good bright-line would be to require a geographical separation of at least 350 miles between cities where the issuer uses the proceeds of the offers.

[222] The SEC could reduce much of the confusion between the two factors by narrowing the scope of facts relevant to the single plan of financing factor.

[223] *See, e.g., Cavanagh,* 1 F. Supp.2d at 364 (stating, "[n]either [sic] the Commission nor the courts have provided express guidance on how to weigh these factors when analyzing an integration problem.").

[224] *Cf. Goodwin Properties,* 2001 WL 800064, at *9 (requiring proof of all five factors to justify integration) *and Cavanagh*, 1 F. Supp.2d at 364 (finding that proof of all five factors is not necessary to

justify integration) *and Murphy*, 626 F.2d at 646 (finding that proof of all five factors is not necessary to justify integration) *and Kunz* I, *supra* note 174, at *16 (finding that proof of all five factors is not necessary to justify integration).

[225] *See generally Kunz* I, *supra* note 174, at *16 (requiring proof of more than one factor).

[226] *See Cavanagh,* 1 F. Supp.2d at 364 *and Kunz* I, *supra* note 173, at *17. *See also* Bradford*, supra* note 4, at 651.

[227] *See, e.g., Donohoe*, 982 F.2d at 1140 (finding non-integration based primarily on the single plan of financing and general purpose factors) *and Cavanagh*, 1 F. Supp.2d at 365 (finding integration based primarily on the single plan of financing and general purpose factors) *and Walker*, 736 F. Supp. at 1364-65 (finding integration on all five factors but placing particular emphasis on the single plan of financing and general purpose factors) *and Currie,* 595 F. Supp. at 1377 (finding integration based primarily on the class of securities, consideration, and general purpose factors) *and Johnston*, 764 F. Supp. at 1272 (finding integration based primarily on the class of securities, time, consideration, and general purpose factors) *and Melchior*, 1993 WL 89141, at *10 (finding integration based primarily on the time, class of securities, consideration, and general purpose factors) *and* Guarantee Mutual Life Company, SEC No-Action Letter, 1995 WL 256250 (Apr. 13, 1995) (finding non-integration based primarily on the consideration and general purpose factors) *and* Farm Family Mutual Ins. Co., SEC No-Action Letter, 1996 WL 157393 (Apr. 2, 1996) (finding non-integration based primarily on the consideration and general purpose factors) *and* Blue Cross & Blue Shield of Va., SEC No-Action Letter, 1996 WL 330514 (June 14, 1996) (finding non-integration based primarily on the consideration and general purpose factors).

[228] *See* Bradford, *supra* note 4, at 652 (noting, "When different classes of securities are offered, the courts and the SEC generally will not integrate, even if the differences between the two classes are small.").

[229] *See, e.g.,* 17 C.F.R. § 230.502.

[230]*See* Section 3(a)(11) Exemption for Local Offerings, Securities Act Release 1961 WL 61651 (Dec. 6, 1961).

[231] *See, e.g.,* N. Am. Leisure Group, Inc., SEC No-Action Letter, 1988 WL 235271 (Dec. 15, 1988) (stating in the request for non-integration, "The SEC has consistently applied the criteria stated above [the five factors] on integration issues, but it is unclear how much weight is to be given to each criterion.").

[232] *See generally Johnston,* 764 F. Supp. at 1272 *and* Pittsburg National Corp., SEC No-Action Letter, 1977 WL 10903 (August 15, 1977) *and Donohoe,* 982 F.2d at 1140 *and* First & Merchants Corp., SEC No-Action Letter, 1978 WL 13000 (July 27, 1978).

[233] *See generally* Resolution Trust Corp., SEC No-Action Letter, 1991 WL 176870 (July 18, 1991).

[234] *See generally Donohoe*, 982 F.2d at 1134-40.

[235] *See Johnston*, 764 F. Supp. at 1272.

[236] *See generally* Farm Family Mutual Ins. Co., SEC No-Action Letter, 1996 WL 157393 (Apr. 2, 1996).

[237] *See id.*

[238] *See generally Melchior,* 1993 WL 89141, at *10 *and Donohoe*, 982 F.2d at 1140.

[239] *See, e.g., Donohoe* I, 736 F. Supp. at 877.

[240] *See* Section 3(a)(11) Exemption for Local Offerings, Securities Act Release 1961 WL 61651 (Dec. 6, 1961).

[241] *Cf. Murphy*, 626 F.2d at 646 *and Goodwin Properties,* 2001 WL 800064, at *9.

[242] *See Kunz* I, *supra* note 174, at *16 *and* Section 3(a)(11) Exemption for Local Offerings, Securities Act Release 1961 WL 61651 (Dec. 6, 1961).

[243] *See Cavanagh,* 1 F. Supp.2d at 364. Ironically, these two factors are the most factually related and difficult to distinguish. *See* Campbell, *supra* note 42, at 307.