NOTE
PURCHASER'S DUTY TO DISCLOSE UNDER SECURITIES
AND EXCHANGE COMMISSION RULE X-10B-5

In recent years, there have been a number of cases involving non-disclosure of inside information by purchasers when buying corporate securities. The purpose of this Note is to delineate the nature and extent of the affirmative duty to disclose imposed on securities buyers under SEC Rule X-10B-5. No attempt is made to deal with the further problems of disclosure by sellers under the Rule.

Prior to 1933, the Federal Government had no power over corporate securities frauds, except by enforcement of the fraud section of the federal postal laws. The Securities Act of 1933 included § 17(a), which was designed to preclude fraud by any person selling securities. Section 10(b) of the Exchange Act of 1934 gave the SEC power to make rules protecting investors from manipulative or deceptive devices in security transactions. Pursuant to this authority the SEC announced Rule X-10B-5 forbidding fraudulent practices by any person in connection with the purchase or sale of any security. This rule was apparently designed to fill the gap between § 17(a) which concerns the use of fraud by any person in the sale of securities and § 15(c)(1) of the Exchange Act of 1934 which covers fraud by a broker-dealer in the sale or purchase of securities other than on a national security exchange. Although

1. 17 C. F. R. § 240.10b-5 (1949) “It shall be unlawful for any person to employ any device, scheme, or artifice to defraud. (a) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or (b) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.”
2. See Loss, Securities Regulation 806 (1951). For a brief historical background to the Securities Act of 1933 see McCormick, Understanding the Securities Act and the S.E.C. 3-17 (1948).
5. 48 Stat. 891 (1934), 15 U. S. C. § 78 j (b) (1952) “It shall be unlawful for any person to the use of any means or instrumentalities of interstate commerce or by the mails (b) To use in connection with the purchase or sale of any security registered on a national securities exchange or not so registered, any manipulative or deceptive device in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest.”
Rule X-10B-5 overlaps § 17(a) and § 15(c) (1) and rules thereunder, it alone covers fraud in purchases by persons other than broker-dealers.

While the Rule is concerned with "fraudulent practices," it is not limited to cases in which all the elements of common-law fraud are present. One of the most significant effects of the Rule has been its modification of common-law standards of fraud by making unlawful the non-disclosure of material facts by a buyer of corporate securities. Typically this problem arises where a buyer purchases securities without disclosing inside financial information not available to the seller which would indicate that the securities are worth more than the asking price.

DISCLOSURE AT COMMON LAW

Traditionally no action for misrepresentation would lie at common law for mere non-disclosure. Nevertheless, in order to mitigate the harshness of this rule, the courts have developed a number of exceptions. If a person makes any disclosure, he has a duty to say enough so that his words will not be misleading. Also, there is a duty to disclose if a fiduciary relationship can be found.

Although an officer or director occupies a fiduciary relation to the corporation and to the stockholders collectively, a majority of courts have traditionally held that a director owes no fiduciary duty to an individual stockholder. Therefore, failure to disclose to an individual stockholder inside information which has a bearing on the stock's value would not militate against the buyer so long as he did not actively mislead or misrepresent. However, a minority of jurisdictions, in order to implement disclosure, hold that a fiduciary relationship does exist between a director and individual stockholders and that the latter must accordingly be informed of all

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8. The Commission generally brings action against broker-dealers under § 15 (c) and § 10 (b). See e.g., R. D. Bayly & Co., 19 S. E. C. 773 (1945). Since § 15 (c) deals specifically with broker-dealers, their transactions are more profitably considered under that section and will not be covered by this Note.


11. Id. at 723.

12. Ibid.


relevant facts concerning the affairs of the corporation. The traditional view is slowly being broken down by an intermediate doctrine asserted by the United States Supreme Court in *Strong v. Rapide*. That case, which has been widely followed, ruled that even if the relationship between an officer or director and a stockholder is not of such a nature to require general disclosure, there are instances where, because of "special facts," a duty to disclose exists. This special facts doctrine has been broadened by some courts to such an extent that there is little distinction between it and the minority rule. In some other jurisdictions, however, the traditional view still has considerable influence on judicial thinking and X-10B-5 will then provide a more effective remedy.

**Persons Covered by the Rule**

Section 10(b) forbids deceptive practices by "any person" in the purchase of securities. Although "person" is broadly defined in § 3(a) (9) of the Exchange Act, it is doubtful whether the court would require all persons acquiring inside information to make full disclosure before purchasing. But certainly any director, officer, controlling stockholder, or the corporation itself would come within the statute's provision. There is, however, some question of the applicability of Rule X-10B-5 to persons not actually managing the corporation but who, nevertheless, have access to inside information.

Broker-dealers acting in collusion with an insider cannot purchase for themselves\(^2\) or for the insider\(^2\) without full disclosure, nor can a person who learns inside information while doing business with a corporation.\(^2\) It would also seem that employees who have confidential information,\(^2\) as well as persons exercising great influence over corporate policy even though not officers or directors,\(^2\) should, for disclosure purposes, be considered insiders. And since protection given to shareholders by X-10B-5 would be largely illusory if an officer or director could channel his information through a member of his immediate family,\(^2\) disclosure rules should extend at least this far. Moreover, since the duty of disclosure runs to the stockholder, the lack of a "fiduciary relationship" with the corporation should not allow a person who confederates with an officer or director to escape liability under X-10B-5.

**Purchases by a Corporation of Its Own Securities**

Rule X-10B-5 has been used by the SEC with particular effectiveness in forcing a corporation to disclose financial information when purchasing its own securities.\(^2\) One can readily see that there is as great an opportunity to defraud a seller by non-disclosure when corporations purchase as when insiders purchase. If a company, guilty of not disclosing pertinent financial information, buys back its common stock at an undervalued price,\(^2\) the remaining stockholders benefit as definitely by their increased equity in the corporation as if they had purchased themselves. Preferred shares on which dividends have not been paid and arrearages have accumulated, often sell at a fraction of their book value because the improved financial position of the company has not been disclosed.\(^2\)

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27. See Slavin v. Germantown Fire Ins. Co., 174 F. 2d 799 (3d Cir. 1949).\(^3\)
29. There is some common law authority that absent special circumstances no fiduciary relationship exists between a director purchasing for the corporation and an individual stockholder and therefore there is no duty to disclose. Gladstone v. Murray Co., 314 Mass. 584, 50 N. E. 2d 958 (1943). *Contra:* Northern Trust Co. v. Essaness Theatres Corp., 348 Ill. App. 134, 108 N. E. 2d 493 (1952) (When directors act for the corporation they occupy a position of trustee for each individual stockholder and must disclose all material facts).
If the corporation purchases without disclosing the information, the common stockholders are benefited because preferential claims are removed at an unusually low price. Similarly, if preferred shares are subject to call, but have conversion privileges, or debentures are selling at a large discount, disclosure should be required before the corporation purchases, lest the common stockholders be unduly benefited at the expense of the selling security holders.

By § 3(a)(13) of the Exchange Act the term “purchase” includes any contract to buy or otherwise acquire. The Commission has, therefore, brought injunction proceedings to prevent a corporation from benefiting from its improved financial condition by offering to exchange less valuable stock of another company for its own preferred shares. And where a corporation, pursuant to a merger, gave the stockholders an option to exchange common stock in the old company for either common or preferred stock in the new company, the SEC required the company to disclose disparity of value between the old common and the new preferred. Moreover, it would seem that under the terms of § 3(a)(13) of the Exchange Act, X-10B-5 would cover cases where insiders do not disclose material facts to shareholders before the latter vote to merge, consolidate, or reorganize and thereby exchange old securities of a high value for securities of a lesser value in the new company.

It has been argued that an officer might, under some circumstances, have a legitimate duty to better the financial structure of a corporation by purchasing for the corporation, without full disclosure, debt securities at as low a price as possible. However, any strengthening of the corporation is done for the benefit of the

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32. Ibid.
36. See note 67 infra and text thereto.
39. Originally the SEC, in relation to registration of securities issued during reorganization, ruled that any exchange of stock pursuant to a merger, reorganization, or consolidation was not a “sale” under § 5 of the Securities Act. Loss, op. cit. supra note 2, at 335. It might be argued that correspondingly, exchanges pursuant to mergers are not “sales” or “purchases” and thereby excluded from X-10B-5 regulation. However, the Commission has ruled that the “no sale” theory does not apply to the fraud provisions of the Exchange Act. Securities and Exchange Act Release No. 3420 (1951). The courts will probably agree.
stockholders at the expense of the seller. Thus a director's duty to the corporation should not outweigh a more important duty to refrain from taking unfair advantage of a selling security holder.  

**Use of Instrumentalities of Interstate Commerce**

In applying § 10 the courts have held it unnecessary for plaintiff to allege and prove that fraudulent representations or omissions were made by use of the mails or other instrumentalities of interstate commerce.  

Since § 10(b) requires use of interstate instrumentalities *in connection with* the purchase of securities, it is sufficient if the defendant has used the mails, telephone, or telegraph at some time during the transaction. Furthermore, a defendant cannot claim that since his business is entirely intrastate § 10(b) has no application. It has been held that there is nothing in the act which would limit its application to interstate commerce, so long as an instrument of interstate commerce is used.

**Securities Included**

Section 10 and Rule X-10B-5 cover all securities, whether or not registered on a national exchange. No securities are exempted from the provisions of § 10. Thus the fact that a security qualifies as an exempted security under the Securities Act of 1933 has no bearing on the applicability of X-10B-5. Furthermore, "security" is so inclusively defined in § 3(a)(10) of the Exchange Act that it would seem that Rule X-10B-5 covers all types of security transactions. Even so, some defendants have contended that X-10B-5 does not apply where the securities in question were neither registered on a securities exchange nor traded on an over-the-counter market. They base their argument on § 2, the preamble of the Exchange Act, which states that transactions in securities, as commonly conducted upon securities exchanges and over-the-counter markets, are affected with a national public interest and must be regulated. Therefore, defendants argue, securities which do not fall within the purview of the preamble are exempt. The courts have rejected this argument, holding that X-10B-5 includes all securities.

41. See Loss, *op. cit. supra* note 2 at 831.
42. *Fratt v. Robinson*, 203 F. 2d 627, 633 (9th Cir. 1953); *Northern Trust Co. v. Essaness Theatres Corp.*, 103 F. Supp. 954, 961 (N.D. Ill. 1952).
43. *Fratt v. Robinson*, *supra* note 42.
47. See *e.g.*, *Fratt v. Robinson*, 203 F. 2d 627, 628-629 (9th Cir. 1953).
The courts base their decision on grounds either that the term “over-the-counter” in the preamble is broad enough to embrace all securities not listed on a national exchange, or that, although “over-the-counter” means transactions concerning brokers and dealers, the language of § 10(b) and X-10B-5 is not ambiguous and no additional sections are needed to clarify them.

**Sale by an Injured Shareholder to Persons other than Defendant**

Does X-10B-5 apply to situations where defendant insider withholds material information in an offer to buy and plaintiff, on the basis of this under valued offer, sells to a third party? Since the language of § 10(b) and X-10B-5 makes deceptive practices in connection with the purchase of securities unlawful, the plaintiff would almost certainly have a good claim for relief if he acted in reliance on the offer price, and was one of the persons intended by the defendant to be defrauded. But if the plaintiff, in selling to a third party, relied only on the under-valued market price resulting from dealings between the non-disclosing defendant and other sellers, rather than relying on defendant’s asking price made directly to him, it is unlikely that X-10B-5 would apply. In an analogous case bearing on this problem, plaintiffs alleged that they bought securities on an exchange at a price inflated by false and misleading representations and non-disclosures of defendant-insider, and sold at a price deflated by discovery of these misrepresentations. Defendant previously sold at the overvalued price. The court denied relief under X-10B-5 since the plaintiff had not alleged reliance on the false representations, furthermore, according to the court, there was no semblance of privity. By this the court apparently meant that the plaintiff could not have bought the same stock sold by the defendant since thirteen days had elapsed between the last sale by the defendant and the first purchase by the plaintiff. However this was an action in the nature of fraud, which action has been held to

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52. Director of A Co. learns of uranium find made by the company. Without disclosing he offers to purchase at market price. Plaintiff B does not learn of director's offer but sells to a third party at current market price. B brings action against director for damages.
lie where the plaintiff was induced to deal with a third party by the false representations of the defendant.\textsuperscript{54} To require some type of contractual relation between the parties in X-10B-5 actions would defeat the words of the statute and unnecessarily limit the rule.

It has been contented that the court by finding no "semblance of privity" may have meant that this plaintiff was not one of the persons the defendant had intended to defraud.\textsuperscript{55} This interpretation of the court's decision introduces a common law limitation, corresponding to the doctrine of proximate cause, designed to prevent too great an extension of plaintiff's liability.

Thus it might be reasoned that a plaintiff will have to satisfy at least two requirements in order to recover under X-10B-5 when not having sold directly to the defendant. (1) He must have relied on the implications raised by the defendant's non-disclosure and (2) he must be a person intended by the defendant to be defrauded.\textsuperscript{56}

Quite probably a plaintiff selling to a third party, in a suit under X-10B-5, will have to show material reliance other than just reliance on a market price undervalued because of defendant's non-disclosure. However it is doubtful whether the strict interpretation of restrictions (2), above, will be read into the Rule. Already there is evidence that X-10B-5 will extend to persons other than those intended by the defendant to be defrauded.\textsuperscript{57} Moreover, even if the transaction is not of the type intended to be induced by the defendant, the courts might well grant relief if the plaintiff has relied and such reliance was reasonably to be anticipated.\textsuperscript{58} Since this latter restriction has to some extent, been liberalized at common law,\textsuperscript{59} it is to be expected that this liberalization will be reflected in the application of X-10B-5.

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WHAT MUST BE DISCLOSED
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Theoretical grounds for imposing an affirmative duty to dis-\textsuperscript{\ldots}

\begin{footnotesize}
\footnote{Prosser, \textit{op. cit. supra} note 10, at 705.}
\footnote{Joseph v. Farnsworth Radio & Television Corp., 198 F 2d 883, 884 (2d Cir. 1952) (dissenting opinion). See Comment, 4 Stan. L. Rev. 308 (1952).}
\footnote{See note 53 supra. These limitations were developed as common law restrictions as to the persons to whom a defendant guilty of false representation would be liable. 3 Restatement, Torts § 531 (1938) (as limited by §§ 532, 536).}
\footnote{In a case involving false representations and non-disclosure in a registration statement of preferred stock, the court allowed common stockholders, who bought common stock on the market relying on the false registration statement to bring action under X-10B-5. Fischman v. Raytheon Mfg. Co., 188 F 2d 783 (2d Cir. 1951).}
\footnote{Defendant-insider, without disclosing material facts, offers to purchase from A at a stated price. A, relying on the offer, sells to B, at this undervalued price. A sues defendant for damages.}
\footnote{Prosser, \textit{op. cit. supra} note 10, at 731-732.}
\end{footnotesize}
close can be found in all three subsections of the rule. Non-disclosure has been ruled an act or practice which operates as a fraud under subsection (3), an artifice to defraud under subsection (1), and an implied misrepresentation or misleading omission under subsection (2).

In practical application the Rule requires an insider to disclose facts obtained by means of his inside position which would materially affect the judgment of the seller. While this viewpoint in effect adopts the fiduciary rule, it is still necessary to decide whether a specific fact, if disclosed, would be "material" in influencing the seller's judgment. *Speed v. Transamerica Corp.* points up a potential conflict between the courts and the Commission as to what constitutes "materiality." In that case the majority stockholders offered to buy the plaintiff's stock at approximately 33 1/3% above the market value but "neglected" to disclose that the earnings of the company had greatly increased and the market value of its tobacco inventory had tripled in value. The company was subsequently liquidated, the majority stockholder making a substantial profit on the shares purchased. The plaintiffs brought action for damages under X-10B-5. The court found that before the offer was made the defendant had decided to liquidate. Thus, the failure to disclose this plan coupled with a failure to disclose the appreciated value of the inventory materially affected the seller's judgment. However, the court indicated that had there been no plan to liquidate at the time of the offer, full disclosure would have been unnecessary. The court felt that the stock's market price reflected the increased inventory value and besides, the defendant had offered substantially more than this market price. If the price offered is equal to or above the resultant market price had all the facts been known, disclosure would be immaterial. However, any doubts about materiality should be resolved against the non-disclosing purchaser.

62. *Ibid.* It has been reasoned that when an insider makes an offer he impliedly represents that the price is, in his judgment, fair. If because of failure to disclose, the price is undervalued there is an implied misrepresentation. See Loss, *op cit. supra* note 2, at 834.
65. See note 15 *supra* and text thereto.
67. See note 94 *infra* and text thereto.
Thus, had there been no plan to liquidate, the price offered by the
defendant would, according to the court, have been equivalent to or
greater than the market price would have been if all the facts had
been known. This position has dangers because a court must
hypothesize as to how the market would react to complete disclosure,
a risky guess at best.

The Commission, appearing as amicus curiae, argued on the
other hand that the increased inventory value would have been
material even in the absence of a plan to liquidate. Since the pur-
pose of X-10B-5 is to equalize the bargaining position of the parties
by encouraging the dissemination of information, the Commission's
view would seem to be the better one. Full disclosure means a price
set by informed bargaining rather than a unilateral determination
by an insider, even though the latter price might be higher than
market value.

Other civil actions by a defrauded seller under X-10B-5 have in-
volved either fraudulent representations or non-disclosure of
special facts which in most jurisdictions would presumably create
liability under the common-law doctrines. Thus courts have stated
that a purchaser must disclose secret negotiations for the acquis-
tion of a business or an agreement to sell the corporate assets at
an advantageous price.

Under the power to enjoin rule violations, the SEC, alleging
non-disclosure of material facts, has instituted a number of in-
junction proceedings against purchasers under X-10B-5. Most often
these cases concern small companies which are exempt from the
registration requirements of the Securities Act, and furthermore
are not compelled to disclose the financial data required by the
Exchange Act. In such instances, the Commission has required

69. Id. at 826 n. 9 (dictum).
70. E.g., Fratt v. Robinson, 203 F. 2d 627 (9th Cir. 1953); Robinson v.
Northern Trust Co. v. Essaness Theatres Corp., 103 F. Supp. 954, 956-957
(N.D. Ill. 1952) (dictum).
72. Northern Trust Co. v. Essaness Theatres Corp., supra note 71, at
956-957 (dictum).
75. For a discussion of the grounds most commonly used by small cor-
porations for exemption of securities from registration under the Securities
Act of 1933 see Lane, Securities and the Small Company, 2 Cleve-
76. Every issuer of a security registered on a national securities ex-
change must file financial reports with the exchange and the SEC pursuant
to § 13(a) of the Exchange Act. Also, companies not registered on an ex-
change but making securities issues of substantial size must file reports under
§ 15 (d). See Loss, op. cit. supra note 2, at 492-499.
an insider-purchaser to make full disclosure of the financial condition of the company before buying. The Commission considers as “material” such facts as sales volume,\(^7\) net earnings per share,\(^8\) book value,\(^9\) and net current assets per share;\(^10\) nor is it sufficient to state only the net sales of the previous year, if current sales are up.\(^11\) In three instances where assets were carried on the books at cost, the Commission indicated that a vast appreciation of the market value of the assets must be disclosed, even though the defendants followed normal accounting procedures.\(^12\)

In addition to requiring information concerning the financial welfare of the corporation, the SEC has compelled purchasers to disclose additional facts which might influence the seller’s judgment such as the market value when the security is traded only over-the-counter,\(^13\) and the extent and nature of the purchaser’s holdings in the company’s securities.\(^14\) Moreover the insider-purchaser cannot take advantage of his knowledge of such special circumstances as current negotiations to sell the stock at a higher price,\(^15\) or that the company will be profitably liquidated\(^16\) or re-organized.\(^17\) In most of the injunction proceedings initiated by the SEC a number of material facts have been undisclosed. This is not surprising since these factors tend to be inter-related, however, it seems that non-disclosure of any one of the material facts listed by the Commission as a basis for injunction would be sufficient for action if it points to an insider’s attempt to profit improperly at the seller’s expense.

A special problem which has caused some concern is whether a purchaser violates X-10B-5 by merely concealing his identity. Although there has been no case where non-disclosure of the purchaser’s identity has been the sole deciding factor, the Commission has ruled in a number of instances that the purchaser’s name is one of many material facts which must be disclosed. Therefore it would seem that in any fairly large offer to purchase, concealment of identity would be an invitation to SEC investigation of all aspects of the transaction. In view of the fact that sellers often base their judgments on what actions insiders take, the purchaser’s identity in nearly every case would be material and should therefore be disclosed.

A company cannot necessarily defend against charges of non-disclosure in purchases by showing that shareholders were furnished with as much information as is customarily furnished by other companies in the industry. If the welfare of the company demands that information be kept confidential, the officers and directors should be precluded from dealing in the company’s shares where disclosure is required. Further, delayed full disclosure should not be a good defense if, at the time of disclosure, the seller’s plans could not be changed or withdrawn.

It should be noted that “disclosure of material facts” does not mean disclosure of opinion or other similar reasons for buying. The SEC has attempted only to prevent the insider from cashing in on a sure thing. Just because an insider acts with superior foresight is no reason to rescind a transaction.

**Remedies**

The Commission, under § 21 of the Exchange Act, has power to investigate, when it deems necessary, suspected violations of the Act and is authorized to transmit evidence of such violations to the Attorney General for criminal proceedings. Likewise, under §

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89. This argument was made in SEC v. Standard Oil Co. of Kansas, S. D. Tex., Civil No. 2552, Feb. 26, 1947, Litigation Release 388.

90. See Slavin v. Germantown Fire Ins. Co., 174 F. 2d 799 (3d Cir. 1949). A mutual insurance company set up a plan to convert into a stock company. Its chief agent secured assignments of pre-emptive rights thereby defeating company’s plan for wide distribution of stock. The agent disclosed just before the plan was to go into effect. The majority held there was full disclosure but the dissent felt that the agent had violated X-10B-5 since the company could not, at the time of disclosure, have withdrawn the plan.


the SEC can enjoin violations of the Act or rules promulgated under it.

In *Kardon v. National Gypsum Co.*, a federal district court granted to a complainant a civil cause of action for violation of X-10B-5, even though § 10(b) had no express provision for civil liability. The court based its decision on the common law ground that the violation of a statute makes the actor liable for the invasion of another's interest if the injured party was one of a class intended to be protected by the statute and the harm suffered was one which the statute was designed to prevent. The Kardon doctrine has been widely followed; under it a plaintiff is entitled to damages or such equitable remedies as recission, accounting, or the prosecution of a derivative suit on the corporation's behalf. While one court has held that a private complainant has no right to an injunction for repeated violations of X-10B-5, another has indicated that a plaintiff can enjoin the violation of the Commission's proxy rules, and it would seem that once a plaintiff has established a right to redress, he should be allowed to enjoin violations of the Act where normal equitable grounds for an injunction exist.

**Time Within Which Suit Must Be Brought**

Section 10(b), which creates the right of action, contains no statute of limitations. There is, furthermore, no general federal statute of limitations applicable to a federally created cause of action. Under such circumstances the United States Supreme Court

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94. 69 F Supp. 512 (E.D. Pa. 1947)
95. The court also reasoned that § 29 (b) of the Exchange Act which provides that contracts in violation of the Act shall be void implies a civil remedy since § 29 "would be of little value unless a party to the contract could apply to the courts to relieve himself of obligations under it." *Id.* at 514.
96. *E.g.*, Fratt v. Robinson, 203 F 2d 627 (2d Cir. 1953)
97. *Kardon v. National Gypsum Co.*, 73 F Supp. 798, 802 (E.D. Pa. 1947) (dictum). In a recent case the SEC as amicus curiae argued that the inclusion of non-securities (land) as well as securities in an action which would otherwise come under X-10B-5 should not bar recission under the Rule. The Commission contended that to hold otherwise would create a simple way of frustrating the Rule. See Brief for the SEC as amicus curiae pp. 10-11, Cornell v. Errion, W. D. Wash., Civil No. 3556, Jan. 1954. The motion to dismiss was denied. See Loss, *Securities Regulations 1955 Supplement* 373 (1955)
102. See Loss, *op cit. supra* note 2, at 1006 (1951)
103. See Note, 53 Colum. L. Rev. 68 (1953)
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has held that where the action is legal or, though equitable, is concurrent with a legal remedy, the state statute of limitations must apply. But when a complainant is seeking only an equitable remedy under a federally created substantive right, the federal doctrine of laches applies. Since in most cases actions under X-10B-5 will be for money damages, a legal remedy, the courts will look to the state statutes of limitations. Presumably, however, a purely equitable action under the Rule would be governed by laches. Thus far the X-10B-5 cases holding on the question have applied the law of the state in which the court sits.

SUMMARY AND CONCLUSION

Rule X-10B-5 has tremendous potential as a remedy for sellers defrauded by non-disclosure. By imposing on buyers a duty to disclose all material facts, the Rule, at least in some jurisdictions, liberalizes the traditional common law doctrine of disclosure. And since X-10B-5 is drawn to include "any person," the scope of disclosure requirements may be extended to embrace persons other than those covered at common law. Probably the Rule has been most effectively used in preventing a corporation from purchasing its own securities without full disclosure. The SEC has required corporations to comply as strictly as individuals with rules of disclosure. Moreover, it is not necessary for a plaintiff to sell directly to the defendant in order to be protected by the Rule, so long as the sale was induced by him, although it is questionable whether mere reliance on an undervalued market price created by the defendant would be sufficient to hold him for non-disclosure.

The Rule's effectiveness is enhanced by the power of the SEC to investigate and enjoin potential rule violations. This has the advantage of being a strong deterrent, often preventing injury which would have otherwise occurred. Also the availability of civil

108. Fischman v. Raytheon Mfg. Co., 188 F. 2d 783 (2d Cir. 1951); Northern Trust Co. v. Essaness Theatres Corp., 103 F. Supp. 954 (N.D. Ill. 1952); Osborne v. Mallory, 86 F. Supp. 869 (S.D. N.Y. 1949). Even after deciding that a state statute of limitation will apply there is still the further question of whether related problems must be settled according to state law, e.g., when the limitation period commences. Compare the reasoning in Fratt v. Robinson, 203 F. 2d 627, 634-635 (9th Cir. 1953) (Circuit Court seemed to make its own determination of which of two state statutes of limitations to apply) with Northern Trust Co. v. Essaness Theatres Corp., 103 F. Supp. 954, 966-967 (N.D. Ill. 1952) (court looked to state law to determine which of two state statutes of limitations to apply). See Note, 53 Colum. L. Rev. 68, 71-72 (1953).
remedies to parties injured by the Rule's violation increases its value and gives plaintiffs the Rules liberal grounds for relief. Furthermore, the civil litigant gets the benefits of the venue, jurisdictional, and process serving advantages of § 27 of the Act. Suit may be brought in any district where the defendant is found, or is an inhabitant, or transacts business. Process can be served wherever the defendant is an inhabitant or is found and the federal courts have exclusive jurisdiction of violations under the Act.

To determine what must be disclosed the courts look to whether the fact would have materially influenced the seller's judgment. While it is difficult to decide which facts taken by themselves are material, it is clear that non-disclosure of any fact pointing to an insider's attempt to profit unfairly should be considered a violation of X-10B-5.