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MUDDY WATERS, BLUE SKIES: CIVIL LIABILITY UNDER THE MISSISSIPPI SECURITIES ACT

Keith A. Rowley*

[I]nadequate budgets and uneven enforcement of the blue sky laws make civil liability the only effective sanction in many states—perhaps most states. Outside of California and a handful of other states, criminal prosecutions are undertaken sporadically and only with extreme reluctance. By the same token most administrators shy away generally from formal disciplinary proceedings But the threat of rescission or damages is always present.¹

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¹ IX LOUIS LOSS & JOEL SELIGMAN, *SECURITIES REGULATION* 4131-33 (3d ed. 1992); see also E. Clifton Hodge, Jr., *Civil Liability Under the Mississippi Securities Act*, 43 MISS. L.J. 597, 597-98 (1972) (“[I]n a state such as Mississippi where funds available for the administrative regulation of securities are definitely limited, civil liability may be the only effective means of enforcement.”).

That said, there is a relative dearth of reported Mississippi case law discussing civil securities liability—a problem that has been noted before. See Hodge, *supra* at 598 (noting “there is very little authority” to draw upon for purposes of exploring civil liability under Mississippi Securities Act); L. Keith Parsons, *A Review of Interpretive Opinions and Enforcement Proceedings Under the Mississippi Securities Act*, 12 MISS. C. L. REV. 179, 179 (1991) (“Judicial interpretation of the [Mississippi Securities] Act . . . is almost nonexistent.”); Bryn Vaaler, *Financing a Small Business in Mississippi: A Practitioner’s Guide to Federal and States Securities Exemptions—Part II*, 63 MISS. L.J. 267, 325 (1994) (“Judicial interpretation of the Mississippi Securities Act and the Mississippi Blue Sky Rules has been extremely sparse.”); Richard Baxter Wilson, Jr., Comment, *Selling the Blue Sky in Mississippi—A Comparison of the Mississippi Securities Act with the Uniform Securities Act*, 35 MISS. L.J. 421, 421 (1964) (“[N]o case has yet reached the Mississippi Supreme Court”). Fortunately, the Mississippi Secretary of State’s Business Services (né Securities) Division has issued a number of private interpretive opinions—similar to “no-action” letters issued by

I. INTRODUCTION

The decade of the 1990s produced a series of actions by the United States Supreme Court and by Congress that, collectively, reduced the number of avenues by which plaintiffs relying on federal law may pursue alleged wrongdoers for securities fraud; imposed significant additional requirements on plaintiffs suing under federal securities law; preempted state registration requirements for several classes of securities; and curbed the availability of state courts as an alternative forum in which plaintiffs may pursue securities fraud claims.² And yet, in spite of these changes, "Congress, the courts, and the SEC have

the U.S. Securities Exchange Commission—and Cease and Desist Orders that provide additional guidance on the scope and contours of the Mississippi Securities Act. Several hundred of these are available on line through LEXIS's Mississippi Secretary of State, Securities Division database (STATES; MSSEC) and are cited throughout this article, most often during the discussion of registration issues. *See infra* notes 14, 19, 23-31, 35-43, 46, 49, 52, 54-55, 58-63, 65-72, 78-79, 83-89, 92-94, 113-14, and 129-35. For a thorough review of interpretive opinions and enforcement orders issued from 1985 through 1991, see Parsons, *supra*.

² Namely, the Supreme Court's decisions in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 176-78 (1994) (eliminating implied private cause of action for aiding and abetting securities fraud), and *Gustafson v. Alloyd Co.*, 513 U.S. 561, 576-77 (1995) (holding section 12(a)(2) of 1933 Securities Act applies only to public offerings), Congress's passage of the Private Securities Litigation Reform Act (PSLRA), Pub. L. No. 104-67, 109 Stat. 737 (1995) (reforming number of relevant substantive and procedural provisions of both 1933 Securities Act and 1934 Securities Exchange Act), the National Securities Market Improvement Act (NSMIA), Pub. L. No. 104-290, 110 Stat. 3416 (1996), *codified at* 15 U.S.C. § 77r (Supp. V 1999) (amending 1933 Securities Act to eliminate its provision allowing concurrent state regulation of several categories of securities offerings), and the Securities Litigation Uniform Standards Act (SLUSA), Pub. L. No. 105-353, 112 Stat. 3227 (1998), *codified at* 15 U.S.C. § 77p & § 78bb(f) (preempting most state court securities class actions and empowering defendants to remove to federal court securities class actions filed in state court).

For discussions of the foregoing cases and legislation and their impact on state securities law, see Keith A. Rowley, *The Sky is Still Blue in Texas: State Law Alternatives to Federal Securities Remedies*, 50 BAYLOR L. REV. 99, 103-06 (1998) [hereinafter Rowley, *The Sky is Still Blue*], and the sources cited therein; Keith A. Rowley, *They Toil Not, Neither Do They Spin: Civil Liability Under the Oregon Securities Law*, 37 WILLAMETTE L. REV. 335, 337-41 (2001) [hereinafter Rowley, *They Toil Not*].

made explicit that federal regulation was not designed to displace state blue sky laws."³

As a general rule, Mississippi law holds those who sell securities in violation of statutory registration requirements,⁴ or by means of some misrepresentation or omission of material fact,⁵ liable to anyone who buys securities from or through them. Likewise, those who buy securities by means of some misrepresentation or omission of material fact may be liable to anyone who sells securities to or through them.⁶ In addition to, or in lieu of,⁷ those who committed the material misrepresentation or omission, liability for the consequences of a misrepresentation or omission may extend vicariously to others who are closely related to the primary wrongdoer or were involved in the transaction at issue.⁸

To the extent not foreclosed by recent changes in federal law,⁹ many acts and omissions that will give rise to liability under Mississippi law will also give rise to liability under federal securities law.¹⁰ Some federal securities claims may be

³ A.S. Goldmen & Co. v. N.J. Bureau of Sec., 163 F.3d 780, 781 (3d Cir.), cert. denied, 528 U.S. 868 (1999).

⁴ See MISS. CODE ANN. §§ 75-71-401, -717(a)(1) (2000); *infra* Part II.B.

⁵ See MISS. CODE ANN. § 75-71-717(a)(2); see also Seaboard Planning Corp. v. Powell, 364 So. 2d 1091, 1093-94 (Miss. 1978) (holding seller of securities liable for violating anti-fraud provisions of precursor to current Mississippi Securities Act); First Mobile Home Corp. v. Little, 298 So. 2d 676, 679 (Miss. 1974) (holding seller of securities liable for common law fraud). See *infra* Part II.C for a discussion of primary liability for statutory securities fraud.

⁶ The general anti-fraud provision of the Mississippi Securities Act (MSA) prohibits fraud in both the sale and purchase of securities. See MISS. CODE ANN. § 75-71-501. However, Mississippi courts refuse to recognize an implied cause of action under section 501. See Allyn v. Wortman, 725 So. 2d 94, 102 (Miss. 1998). The primary civil remedial provision holds liable only those who offer to sell or do sell securities in contravention of the MSA, not those who offer to buy or do buy. See MISS. CODE ANN. § 75-71-717(a)(2). Fortunately for aggrieved sellers, the lack of sellers' remedies in the MSA does not preempt them from bringing common law claims. See, e.g., Gray v. Baker, 485 So. 2d 306, 308 (Miss. 1986) (permitting seller to rescind contract with buyer based on buyer's fraud).

⁷ See *infra* note 167 and accompanying text.

⁸ See MISS. CODE ANN. § 75-71-719; *infra* Part II.D.

⁹ See *supra* note 2 and accompanying text.

¹⁰ Federal securities law imposes liability for failing to comply with applicable registration requirements. See 15 U.S.C. § 77l(a)(1) (Supp. V 1999). Federal securities law also contains three primary civil anti-fraud provisions: section 11 of the

brought in Mississippi state court,¹¹ while others may not.¹² In any event, while this Article focuses on Mississippi law, readers who have not already done so should familiarize themselves with the relevant federal statutory provisions and precedent—both because federal and state liability overlap to a significant degree,¹³ and because numerous provisions of Mississippi securities law are derived from or closely resemble federal law, leading Mississippi courts frequently to resort to cases construing analogous federal provisions in order to construe and apply Mississippi law.¹⁴

1933 Securities Act, *id.* § 77k (1994); section 12(a)(2) of the 1933 Securities Act, 15 U.S.C. § 77l(a)(2) (Supp. V 1999); and section 10(b) of the 1934 Securities Exchange Act, 15 U.S.C. § 78j(b) (1994). Section 11 addresses misrepresentations and omissions in registration statements filed with the Securities Exchange Commission. Section 12(a)(2) addresses misrepresentations and omissions “in connection with” a public offering of securities. Section 10(b), actionable through Rule 10b-5, 17 C.F.R. § 240.10b-5 (2000), is the general anti-fraud provision. For an excellent introduction to federal securities law, see LARRY D. SODERQUIST, UNDERSTANDING THE SECURITIES LAWS (3d ed. 1997 & Supp. 2000). For the definitive treatment, see LOSS & SELIGMAN, *supra* note 1.

¹¹ Claims under section 11 or 12 may be brought in either federal or state court, and cannot be removed other than for diversity of citizenship. *See* 15 U.S.C. § 77v(a) (Supp. V 1999); *Wilko v. Swan*, 346 U.S. 427, 430 (1953), *overruled on other grounds by* *Rodriguez de Quijas v. Shearson/Am. Express, Inc.*, 490 U.S. 477, 484 (1989); *Luce v. Edelstein*, 1985 WL 2257, at *2 (S.D.N.Y. Aug. 8, 1985); *Moran v. Paine, Webber, Jackson & Curtis*, 279 F. Supp. 573, 577 (W.D. Pa. 1966), *aff'd*, 389 F.2d 242 (3d Cir. 1968).

¹² Claims under section 10(b)/Rule 10b-5 must be brought in federal court. *See* 15 U.S.C. § 78aa (1994); *Lang v. French*, 154 F.3d 217, 221 (5th Cir. 1998). The exclusive jurisdiction of the federal courts over section 10(b)/Rule 10b-5 claims is subject to knowing waiver in favor of arbitration, *see Shearson/Am. Express, Inc. v. McMahon*, 482 U.S. 220, 227-28 (1987), but not in favor of state court.

¹³ *See, e.g., Johnson v. Yerger*, 612 F.2d 953, 955 (5th Cir. 1980) (plaintiffs brought claims under 1933 Securities Act, 1934 Securities Exchange Act, Rule 10b-5 and MSA, all arising from single transaction); *Shivangi v. Dean Witter Reynolds, Inc.*, 107 F.R.D. 313, 315 (S.D. Miss. 1985) (plaintiffs claimed under Rule 10b-5, section 501 of MSA and Mississippi common law).

¹⁴ *See, e.g., Allyn v. Wortman*, 725 So. 2d 94, 102 (Miss. 1998) (basing its refusal to recognize implied private cause of action under section 501 of MSA, MISS. CODE ANN. § 75-71-501, on fact that there is no implied private cause of action under section 17(a) of 1933 Securities Act, 15 U.S.C. § 77q(a), with which section 501 is “virtually identical”); *In re Stewart*, No. 97-05-59, 1998 Miss. Sec. LEXIS 3, at *5 (Aug. 27, 1998) (adopting test set out in *Reves v. Ernst & Young*, 494 U.S. 56, 64-65 (1990), for whether promissory notes are securities); *see also, e.g., Tatum v. Smith*, 887 F. Supp. 918, 924 n.6 (N.D. Miss. 1995) (summarily dismissing plaintiffs’ “control person” claims under MSA because MSA’s control

II. STATUTORY LIABILITY UNDER THE MISSISSIPPI SECURITIES ACT¹⁵

The Mississippi Securities Act (MSA) imposes liability on any person¹⁶ who sells or offers to sell a security in violation of the MSA's registration requirements.¹⁷ Irrespective of whether the security at issue was required to be and was properly registered, the MSA also imposes liability on any person who sells or offers to sell a security by means of an untrue statement of material fact or an omission of material fact necessary to make those statements that were made true.¹⁸

A. Key Concepts

The registration and antifraud provisions of the MSA apply only to devices or transactions the MSA deems to be "securities," and are triggered by their unauthorized or unlawful offer or sale.

1. The Meaning of "Security"

The MSA defines "security" to mean

any note; stock; treasury stock; bond; debenture; evidence of indebtedness; certificate of interest or participation in any profit-sharing agreement; collateral-trust certificate; preorganization certificate or subscription; transferable share; invest-

person liability provision "mirrors" that of 1933 Securities Act, claims which court had already disposed of); *Fortenberry v. Foxworth Corp.*, 825 F. Supp. 1265, 1279 (S.D. Miss. 1993) ("The nearly identical language of § 501 and Rule 10b-5 leads this court to the inexorable conclusion that they have nearly identical purposes.").

¹⁵ The discussion here and elsewhere in this article focuses solely on civil liability for violations of the applicable provisions of the MSA. However, an unregistered person selling securities not otherwise exempt under the MSA, as well as any person selling unregistered securities not otherwise exempt under the MSA, may also face criminal liability. See MISS. CODE ANN. § 75-71-735; *Campbell v. State*, 743 So. 2d 1050, 1053-54 (Miss. Ct. App. 1999).

¹⁶ For purposes of the MSA, "person" includes corporations, partnerships, joint stock companies, associations, syndicates and other business entities. See MISS. CODE ANN. § 75-71-105(k).

¹⁷ See *supra* note 4 and accompanying text.

¹⁸ See *supra* note 5 and accompanying text.

ment contract; voting-trust certificate; certificate of deposit for a security; certificate of interest or participation in an oil, gas or mining title or lease or in payments out of production under such a title or lease; interest in a limited partnership; viatical settlement investment contract or a fractionalized or pooled interest therein; or, in general, any interest or instrument commonly known as a "security," or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing, excluding] any insurance or endowment policy or annuity contract under which an insurance company promises to pay a fixed or variable sum of money, or both, either in a lump sum or periodically for life or some other specified period.¹⁹

¹⁹ MISS. CODE ANN. § 75-71-105(n); *see, e.g., In re Millennicom, Inc.*, No. 00-041, 2000 Miss. Sec. LEXIS 4, at *4 (Oct. 18, 2000) (promissory notes); *In re S. States Meat Goat Coop.*, No. 98-013, 1998 Miss. Sec. LEXIS 31, at *1 (Jan. 22, 1998) (preferred and common stock); *In re Brantley Capital Corp.*, No. 97-06-15, 1997 Miss. Sec. LEXIS 15, at *1 (Sep. 16, 1997) (investment company shares); *In re Money Makers Int'l*, No. 93-10-22, 1994 Miss. Sec. LEXIS 7, at *1 (Jan. 12, 1994) (common stock); *In re Interlochen Group, Inc.*, No. 93-09-01, 1993 Miss. Sec. LEXIS 16, at *1 (Nov. 9, 1993) (stock); *In re Gen. Research Indus. Inc.*, No. CD-90-1-3, 1990 Miss. Sec. LEXIS 2, at *1 (Jan. 24, 1990) (common stock); *In re Bond Servs. Int'l Corp.*, No. 89-08-11, 1989 Miss. Sec. LEXIS 1, at *2 (Oct. 18, 1989) (bonds); *In re Hi-Tech Plastic Mfg. Co.*, No. CD-90-1-2, 1990 Miss. Sec. LEXIS 3, at *1 (Jan. 18, 1990) (stock); *In re First Enterprizes, Inc.*, No. 88-1-08, 1988 Miss. Sec. LEXIS 3, at *1-3 (May 19, 1988) (oil, gas or mining title, lease, or payments participation).

By comparison, section 2 of the 1933 Securities Act defines "security" to mean

any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a "security," or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

15 U.S.C. § 77b(a)(1) (Supp. V 1999).

The definition of "security" in section 3 of the 1934 Securities Exchange Act is largely the same as that contained in section 2 of the 1933 Securities Act, al-

a. Investment Contract

By rule, the Secretary of State has defined “investment contract” to mean “any interest or participation in a contract, transaction, scheme, common enterprise, or profit-seeking venture whereby a person invests therein and looks primarily to the promoter or a third party for the financial success of such venture.”²⁰ This is consistent with the “modified *Howey* test”²¹ employed by federal courts and most other states.²²

though section 3 excludes “evidence of indebtedness” and “guarantees of” the various devices specified in the definition, describes oil, gas and mineral interests somewhat differently and explicitly excludes “currency or any note, draft, bill of exchange, or banker’s acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited.” *Id.* § 78c(a)(10). Despite these differences, courts generally treat the definitions of “security” in the two acts as functionally interchangeable. *See, e.g.*, *Landreth Timber Co. v. Landreth*, 471 U.S. 681, 686 n.1 (1985); *Great Rivers Coop. v. Farmland Indus., Inc.*, 198 F.3d 685, 698 (8th Cir. 1999).

For an enlightening examination of the evolving statutory definition and judicial application of the term “security,” see Theresa A. Gabaldon, *A Sense of Security: An Empirical Study*, 25 J. CORP. L. 307, 312-47 (2000). For a somewhat dated discussion of the same issues under state law, see Douglas M. Branson & Karl Shumpei Okamoto, *The Supreme Court’s Literalism and the Definition of “Security” in the State Courts*, 50 WASH. & LEE L. REV. 1043, 1060-68 (1993). *See generally* II LOSS & SELIGMAN, *supra* note 1, at 923-1138.19; Gary S. Rosin, *Historical Perspectives on the Definition of a Security*, 28 S. TEX. L. REV. 575, 597-610 (1987).

²⁰ Rule 103(H), Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,403, at 29,402.

²¹ *Policy Statement on Viatical Settlements*, Feb. 25, 2000, reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,627, at 29,553.

The Secretary of State considers the United States Supreme Court’s analysis in *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946) to be persuasive in defining the term “investment contract”. The *Howey* test holds that an investment contract has four principal elements or criteria: (i) the investment of money; (ii) in a common enterprise; (iii) with an expectation of profits; (iv) to be earned through the efforts of others. The fourth prong of the *Howey* test was clarified in *SEC v. Glenn W. Turner Enterprises*, which held that the “efforts” referred to “are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise.” *SEC v. Glenn W. Turner Enterprises*, 474 F.2d 476, 482 (9th Cir.) *cert. denied*, 414 U.S. 821 (1973). The Secretary concurs in this reasoning.

Id.

²² *See, e.g.*, *United Hous. Found., Inc. v. Forman*, 421 U.S. 837, 852 (1975);

In enforcement proceedings, the Business Services Division

SEC v. Banner Fund Int'l, 211 F.3d 602, 614 (D.C. Cir. 2000); Great Rivers Co-op. v. Farmland Indus., 198 F.3d 685, 700 (8th Cir. 1999); SEC v. Unique Fin. Concepts, 196 F.3d 1195, 1199 (11th Cir. 1999); Matassarini v. Lynch, 174 F.3d 549, 560 (5th Cir. 1999), *cert. denied*, 528 U.S. 1116 (2000); Allen v. Lloyd's of London, 94 F.3d 923, 930 (4th Cir. 1996); Revak v. SEC Realty Corp., 18 F.3d 81, 87 (2d Cir. 1994); SEC v. Eurobond Exch., Ltd., 13 F.3d 1334, 1338 (9th Cir. 1994); Stone v. Kirk, 8 F.3d 1079, 1085 (6th Cir. 1993); RTC v. Stone, 998 F.2d 1534, 1540 (10th Cir. 1993); Rodriguez v. Banco Cent. Corp., 990 F.2d 7, 10 (1st Cir. 1993); Schlifke v. Seafirst Corp., 866 F.2d 935, 941 (7th Cir. 1989); Hamblett v. Bd. of Sav. & Loan Assocs., 472 F. Supp. 158, 165 (N.D. Miss. 1979); Nutek Info. Sys., Inc. v. Arizona Corp. Comm'n, 977 P.2d 826, 830 (Ariz. Ct. App. 1998), *cert. denied*, 528 U.S. 932 (1999); SEC v. Infinity Group Co., 212 F.3d 180, 187 (3d Cir. 2000), *cert. denied*, 121 S. Ct. 1228 (2001); Feigin v. Digital Interactive Assocs., 987 P.2d 876, 881 (Colo. Ct. App. 1999); Brown v. Rairigh, 363 So. 2d 590, 592-93 (Fla. Dist. Ct. App. 1978); Huggins v. Chapin, 489 S.E.2d 109, 111 (Ga. Ct. App. 1997); State v. Res. Serv. Co., 950 P.2d 249, 253-54 (Idaho 1997); Ronnett v. Am. Breeding Herds, Inc., 464 N.E.2d 1201, 1203 (Ill. App. Ct. 1984); State v. Kraklio, 560 N.W.2d 16, 18 (Iowa 1997); State *ex rel.* Owens v. Colby, 646 P.2d 1071, 1077 (Kan. 1982); Dep't of Commerce v. DeBeers Diamond Inv., Ltd., 280 N.W.2d 547, 550 (Mich. Ct. App. 1979); State v. Kramer, 804 S.W.2d 845, 849 (Mo. Ct. App. 1991); State v. Jones, 453 N.W.2d 447, 451 (Neb. 1990); State v. Danek, 878 P.2d 326, 328-29 (N.M. 1994); People v. First Meridian Planning Corp., 614 N.Y.S.2d 811, 816-17 (N.Y. App. Div. 1994), *aff'd*, 658 N.E.2d 1017 (N.Y. 1995); Tschetter v. Berven, 621 N.W.2d 372, 376 (S.D. 2001); Busse v. Pac. Cattle Feeding Fund No. 1, Ltd., 896 S.W.2d 807, 814 (Tex. App. 1995); Sauve v. K.C., Inc., 591 P.2d 1207, 1209 (Wash. 1979).

A handful of states have recognized an alternative to the modified *Howey* test: the "risk capital" test, under which an instrument or transaction is an "investment contract" if the buyer provides a substantial portion of the initial capital a seller uses to initiate its operations—and, hence, is at the greatest risk of being lost because the venture turns out not to be viable—without the right to actively participate in the management of the venture. *See, e.g.*, Smith v. State, 587 S.W.2d 50, 52 (Ark. Ct. App. 1979); Silver Hills Country Club v. Sobieski, 361 P.2d 906, 908 (Cal. 1961); State v. Haw. Mkt. Ctr., Inc., 485 P.2d 105, 109 (Haw. 1971); State v. George, 362 N.E.2d 1223, 1227 (Ohio Ct. App. 1975); State *ex rel.* Healy v. Consumer Bus. Sys., Inc., 482 P.2d 549, 554-55 (Or. Ct. App. 1971); State v. Brewer, 932 S.W.2d 1, 13-14 (Tenn. Ct. Crim. App. 1996); *see also, e.g.*, Artistic Door Corp. v. Rheney, 384 So. 2d 179, 181-82 (Fla. Dist. Ct. App.) (finding transaction at issue to be "security" under both modified *Howey* test and "risk capital" test). The "risk capital" test

requires a consideration of the following factors: (1) whether funds are being raised for a business venture or enterprise; (2) whether the transaction is offered indiscriminately to the public at large; (3) whether the investors are substantially powerless to effect the success of the enterprise; and (4) whether the investors' money is substantially at risk because it is inadequately secured.

Moreland v. Dep't of Corps., 239 Cal. Rptr. 558, 566 (Cal. Dist. Ct. App. 1987).

has found a variety of transactions or devices to be investment contracts, including, e.g., purchases of emus with the option of having the seller care for and market the emus on behalf of the purchaser;²³ passive investments in an offshore "trust fund," the proceeds of which were to be used for international currency arbitrage by a third party;²⁴ offers of interest-free loans with an option to allow the offeror to invest and manage the loan proceeds on behalf of the offerees;²⁵ and passive investments in (non-existent) thoroughbred racing horses.²⁶

The Business Services Division has found memberships in a "venture capital trust" organized for the purpose of soliciting applications (and, more importantly, application fees) for funds from the trust,²⁷ investments in a mail-order and advertising business from which the passive investors expected to receive "tax-free" cash payments based on the amount invested,²⁸ membership, joint venture, or partnership interests through which individuals invest funds to be pooled with those of other investors for the purpose of developing and expanding a wireless cable television system,²⁹ and investments to be pooled with those of other investors to be used to seek a license from the Federal Communication Commission to operate an Interactive Television System to be "investment contracts and/or

²³ *In re S & W Emu Ranch*, No. 94-10-05, 1994 Miss. Sec. LEXIS 13, at *1 (Nov. 30, 1994).

²⁴ *In re Swiss Trade & Commerce Trust*, No. 94-04-09, 1994 Miss. Sec. LEXIS 12, at *1 (July 8, 1994); *In re Prof'l Mktg. Servs.*, No. 94-04-10, 1994 Miss. Sec. LEXIS 11, at *1 (June 3, 1994).

²⁵ *In re Dooley Billiu*, No. 89-10-07, 1989 Miss. Sec. LEXIS 2, at *1-2 (Nov. 27, 1989).

²⁶ *In re BMT Racing Stables*, No. CD 86-8-1, 1986 Miss. Sec. LEXIS 1, at *1-2 (Sep. 10, 1986).

²⁷ *In re Apex Co.*, No. 96-12-001, 1996 Miss. Sec. LEXIS 21, at *1-2 (Dec. 31, 1996).

²⁸ *In re G.C.M.C.*, No. 96-08-046, 1996 Miss. Sec. LEXIS 20, at *1-2 (Nov. 4, 1996).

²⁹ *In re Diversified Wireless Holdings*, No. 95-01-02, 1995 Miss. Sec. LEXIS 17, at *1 (Mar. 23, 1995); *In re Golden Triangle Wireless Television P'ship*, No. 95-03-02, 1995 Miss. Sec. LEXIS 20, at *1-2 (Mar. 22, 1995); *In re National Wireless Group*, No. 95-03-04, 1995 Miss. Sec. LEXIS 22, at *1-2 (Mar. 22, 1995); *In re Cont'l Wireless Cable Television, Inc.*, No. 95-01-01, 1995 Miss. Sec. LEXIS 21, at *1-2 (Jan. 2, 1995).

participations in a profit-sharing agreement.”³⁰

The Business Services Division has also encountered several transactions or devices that it has determined to be an investment contract and/or “certificate of interest or participation in an oil, gas or mining title or lease or in payments out of production under such a title or lease.”³¹

b. Notes

As do the comparable provisions of both the 1933 Securities Act and the 1934 Securities Exchange Act,³² the MSA explicitly includes “notes” in its definition of “security.”³³ As did the United States Supreme Court in *Reves v. Ernst & Young*,³⁴ the Business Services Division has concluded that “[e]ven though the plain language of the statute provides that any note is a security, that is not the end of the inquiry.”³⁵ Again following the lead of the *Reves* Court, the Division has adopted a four-part test to determine whether a particular note is a “security” for purposes of the MSA:

The Court in *Reves* adopted a four-part test for determining when a note so closely resembles an instrument in the above list of categories that it is not a security. The elements

³⁰ *In re* Pathway Planning, Inc., No. 93-11-14, 1993 Miss. Sec. LEXIS 18, at *2 (Nov. 17, 1993).

The Division allowed that this particular interest might also qualify as an “interest in a limited partnership.” *See id.* The MSA, unlike parallel federal law, specifically includes limited partnership interests in its statutory definition of “security.” *See supra* note 19 and accompanying text.

³¹ *See, e.g., In re* Myers & Assocs., No. 94-04-08, 1994 Miss. Sec. LEXIS 14, at *1-2 (Apr. 28, 1994); *In re* Basa Res., Inc., No. 91-07-21, 1991 Miss. Sec. LEXIS 15, at *1-3 (July 25, 1991); *In re* Rich-Ken, Inc., No. CD-90-1-1, 1990 Miss. Sec. LEXIS 1, at *1-3 (Apr. 2, 1990).

Neither the 1933 Securities Act nor the 1934 Securities Exchange Act explicitly include oil, gas or mineral title, lease or payment participations in their definitions of “security.” *See supra* note 19.

³² *See supra* note 19.

³³ MISS. CODE ANN. § 75-71-105(n) (2000).

³⁴ 494 U.S. 56 (1990).

³⁵ *In re* Stewart, No. 97-05-59, 1998 Miss. Sec. LEXIS 3, at *5 (Aug. 27, 1998); *cf. Reves*, 494 U.S. at 62-63 (advising “the phrase ‘any note,’ in section 3(a)(10) of the Exchange Act, “should not be interpreted to mean literally ‘any note,’ but must be understood against the backdrop of what Congress was attempting to accomplish in enacting the Securities Acts”).

to be considered in the four-part test are:

(1) The motivations that would prompt a reasonable seller and buyer to enter into it. If the seller's purpose is to raise money for the general use of a business enterprise or to finance substantial investments and the buyer is interested primarily in the profit the note is expected to generate, the interest is likely to be a "security;"

(2) The "plan of distribution" of the instrument to determine whether it is an instrument in which there is "common trading for speculation or investment" (citation omitted);

(3) The reasonable expectations of the investing public; [and]

(4) Whether some factor such as the existence of another regulatory scheme significantly reduces the risk of the instrument, thereby rendering application of the Securities Acts unnecessary.³⁶

Applying the *Reves* test to the promissory notes at issue, the Division found they were "securities" where: (1) "the buyers . . . purchased the notes to earn a profit in the form of interest and the sellers sold the notes to raise capital for the[ir] business;"³⁷ (2) the notes "were distributed to the general public through a network of at least fifteen agents" resulting in the purchase of "over \$2 million . . . worth of these promissory notes [by] at least 31 investors" in Mississippi,³⁸ (3) "[t]he disclosure document used to place the . . . notes refer[red] to them as 'prime investment grade commercial notes'" and "highlight[ed] the investment quality of the instruments;"³⁹ and (4) notwithstanding the disclosure document's representations to the contrary,⁴⁰

³⁶ *Stewart*, 1998 Miss. Sec. LEXIS 3, at *6-7 (citations and parentheticals omitted) (quoting *Reves*, 494 U.S. at 66).

³⁷ *Id.* at *10.

³⁸ *Id.* at *10-11.

³⁹ *Id.* at *11.

⁴⁰ *See id.* at *11-12 ("The . . . disclosure document states that 'the Notes will be partially secured on a revolving basis by U.S. Government Securities and other investments of comparable safety, cash reserves, and a perfected security interest in the Company's loan portfolio.' However, Respondents offered no proof that such risk reducing factors actually were in place." (record citation omitted)).

were it not for the applicability of the securities laws, these notes would not be subject to any substantial regulatory scheme. They were not insured by the Federal Deposit Insurance Corporation, and nothing in the record suggests that they were subject to regulation under the Employee Retirement Income Security Act of 1974 or any other substantial regulatory scheme. Therefore, it is impossible to find that these notes bear a significant resemblance to any of the consumer or commercial notes making up the list of non-security notes in *Reves*.⁴¹

c. Other Types of "Securities"

The MSA and the Mississippi Blue Sky Rules offer no further guidance, and there are no reported decisions of the Mississippi Supreme Court or the Mississippi Court of Appeals addressing whether a particular transaction or device constitutes a security for purposes of section 105 or any of its predecessors.

Enforcement proceedings brought by the Secretary of State necessarily consider whether the transaction or device at issue is a security⁴²—although the discussion in the published order is typically brief and often conclusory. Likewise, the Business Services Division occasionally addresses in an interpretive ruling the issue of whether a transaction or device is a security⁴³—although, again, the discussion is typically brief. To the extent that a question arises that is not clearly resolved by resort to the language of section 105, or Rule 103(H), or by re-

⁴¹ *Id.* at *12-13 (record citation omitted).

⁴² *See, e.g., In re J. F. (Jim) Straw*, No. 92-04-08, 1992 Miss. Sec. LEXIS 17, at *2 (Apr. 17, 1992) (finding agreement or contract under which person agrees to periodically pay small amounts of money in order to receive larger, interest-free loan at some future date to be determined by promoter was note and/or evidence of indebtedness and/or investment contract); *see also supra* notes 23-31 and accompanying text.

⁴³ *See, e.g., Vistana Fountains Condominiums*, 1990 Miss. Sec. LEXIS 38, at *1 (Jan. 18, 1990) (opining "unit weeks" in condominium time share arrangement were not securities); *Hardware Wholesalers, Inc.*, 1985 Miss. Sec. LEXIS 1, at *1 (Apr. 9, 1985) (opining, without explaining, that certain common stock was not "security" under MSA). *See generally* *Parsons*, *supra* note 1, at 182-83.

view of what guidance is available from the Business Services Division, Mississippi courts will have to look to cases construing analogous provisions in the federal securities acts⁴⁴ and to the securities acts of sister states.⁴⁵

2. "Sale" of or "Offer to Sell" Securities

Subject to certain exceptions,⁴⁶ the MSA defines "sale" and "offer to sell" to include: (1) every contract of sale of, contract to sell, or disposition of, a security or interest in a security for value; (2) every attempt to dispose of, or solicitation of an offer to buy, a security or interest in a security for value; (3) any gift or delivery of securities with, or as a bonus on account of, a purchase of securities; (4) any gift of assessable

⁴⁴ See *supra* note 14 and accompanying text.

⁴⁵ See generally 12 JOSEPH C. LONG, BLUE SKY LAW ch. 2 (2000), and cases cited therein.

⁴⁶ The MSA explicitly excludes the following from its definition of "sale":

(A) any bona fide pledge or loan; (B) any stock dividend, whether the corporation distributing the dividend is the issuer of the stock or not, if nothing of value is given by stockholders for the dividend other than the surrender of a right to a cash or property dividend when each stockholder may elect to take the dividend in cash or property or in stock; (C) any act incident to a class vote by stockholders, pursuant to the certificate of incorporation or the applicable corporation statute, on a merger, consolidation, reclassification of securities, or sale of corporate assets in consideration of the issuance of securities of another corporation; or (D) any act incident to a judicially approved reorganization in which a security is issued in exchange for one or more outstanding securities, claims or property interests, or partly in such exchange and partly for cash.

MISS. CODE ANN. § 75-71-105(l)(6) (2000).

These exceptions appear to prompt the most inquiries for interpretive guidance from the Business Services Division. Keith Parsons reported a decade ago that, "[f]rom 1985 through 1991 there were over 50 interpretations of this section of the Act." See Parsons, *supra* note 1, at 183 n.30. From 1992 through December 31, 2000, there appear to have been at least another thirty-one inquiries answered. Interestingly, all thirty-one related to section 105(j)(6)(C)—the exclusion relating to mergers, consolidations and sales of corporate assets. See, e.g., Affiliated Research Ctrs., Inc., 1996 Miss. Sec. LEXIS 13, at *1-3 (Sept. 16, 1996); Liberte Investors, 1996 Miss. Sec. LEXIS 15, at *1 (June 28, 1996); Mentor Capital Growth Portfolio (Exchange Offer), 1995 Miss. Sec. LEXIS 11, at *1 (June 14, 1995); State Mut. Life Assurance Co., 1995 Miss. Sec. LEXIS 8, at *1 (Mar. 7, 1995); Midland Mut. Life Ins. Co., 1994 Miss. Sec. LEXIS 4, at *1 (May 12, 1994); SAFECO Growth Fund, Inc., 1993 Miss. Sec. LEXIS 14, at *1 (July 23, 1993).

stock by or for any issuer or promoter; and (5) any sale or offer of an option, warrant, or other right to purchase or subscribe to a security.⁴⁷

3. "In Mississippi"

A person who sells or offers to sell securities will only be liable under the MSA if an offer to sell is made in Mississippi, or an offer to buy is made and accepted in Mississippi.⁴⁸ An offer to sell is "made in" Mississippi, whether or not either party to the transaction is then present in Mississippi, when the offer: (1) "originates from" Mississippi or (2) is "directed by the offeror to" and received in Mississippi.⁴⁹ An offer to buy is "accepted in" Mississippi when the buyer, not having previously accepted the offer elsewhere, directs his acceptance to the offeror in Mississippi "reasonably believing the offeror to be in [Mississippi], and it is received at the place to which it is directed."⁵⁰

B. Registration Liability Under the MSA

Section 401 makes it unlawful to sell or offer to sell an unregistered security in the state of Mississippi unless (1) the security is exempt under section 201; (2) the security is a "federal covered security;" (3) the transaction is exempt under section 203; or (4) the security or transaction has been exempted by rule or order of the Secretary of State in accordance with section 109(a).⁵¹

⁴⁷ MISS. CODE ANN. § 75-71-105(l)(1)-(5).

⁴⁸ *Id.* § 75-71-119(a).

⁴⁹ *See id.* § 75-71-119(c); *In re Stewart*, No. 97-05-59, 1998 Miss. Sec. LEXIS 3, at *2, 13 (Aug. 27, 1998) (Florida-based issuer sold notes to thirty-one residents of Mississippi); *In re Myers & Assocs., Inc.*, No. 94-04-08, 1994 Miss. Sec. LEXIS 14, at *4 (Apr. 28, 1994) (offers originated from respondent's Gulfport, Mississippi offices); *In re Basa Resources, Inc.*, No. 91-07-21, 1991 Miss. Sec. LEXIS 15, at *1 (July 25, 1991) (offers were mailed to Mississippi investors from Dallas, Texas).

⁵⁰ MISS. CODE ANN. § 75-71-119(d).

⁵¹ *See id.* § 75-71-401.

Securities may be registered, for purposes of section 401, either under the auspices of the MSA, *see id.* §§ 75-71-403, -405, or -408, or the Mississippi Affordable College Savings Plan, *see id.* § 37-15-515.

1. Exemptions from Registration

The MSA exempts offers and sales of securities from the reach of section 401 based on the nature of the securities themselves, the nature of the transaction in which the securities are offered or sold, or both; the seller or offeror claiming an exemption bears the burden of pleading and proving the exemption's applicability.⁵²

a. Exempt Securities

Section 201 exempts certain securities from registration, notwithstanding whether the transaction involved is otherwise exempt.⁵³ Section 201 exempts most securities issued or guaranteed by: (1) the federal government, including any agency or instrumentality of the federal government;⁵⁴ (2) a state, a po-

A "federal covered security" is "a covered security under section 18(b) of the Securities Act of 1933 or rules or regulations promulgated thereunder." *Id.* § 75-71-105(d).

In addition to requiring registration of securities sold or offered for sale in the state of Mississippi, the MSA also requires, subject to certain exemptions, the registration of all broker-dealers and agents who transact or offer to transact securities business in the state of Mississippi. *See id.* § 75-71-301; *id.* § 75-71-105(a) (defining "agent"); *id.* § 75-71-105(b) (defining "broker-dealer"); *id.* § 75-71-105(g) (defining "investment adviser"); *id.* § 75-71-105(h) (defining "investment adviser representative"). The regulation of broker-dealers, agents, investment advisers and investment adviser representatives, except in their capacities as buyers and sellers of securities and as culpable collateral participants in the purchase or sale of securities, is beyond the scope of this article.

⁵² *See id.* § 75-71-207; *Blinder, Robinson & Co.*, 1990 Miss. Sec. LEXIS 14, at *1 (Jan. 17, 1990); *Staple Cotton Disc. Corp.*, 1987 Miss. Sec. LEXIS 41, at *1 (Nov. 9, 1987).

⁵³ MISS. CODE ANN. § 75-71-201. The section 201 exemptions generally track those contained in section 402(a) of the 1956 Uniform Securities Act, 7C U.L.A. 218-19 (2000), after which the current version of the MSA is modeled. *See Vaaler, supra* note 1, at 323. Section 201 contains two categories of exemptions not included in the Uniform Act: section 201(12), exempting securities of Mississippi cooperatives, and section 201(13), exempting certain oil and gas securities. *See id.* at 324; *infra* notes 68 and 72 and accompanying text. The section 201 exemptions are also similar to those granted by section 3(a) of the 1933 Securities Act. 15 U.S.C. § 77c(a) (1994 & Supp. V 1999).

⁵⁴ MISS. CODE ANN. § 75-71-201(1); *see, e.g.*, *Pac. Crest Inv. & Loan*, 1996 Miss. Sec. LEXIS 1, at *1 (Dec. 17, 1996) (FDIC-insured deposits); *Foothill Thrift Loan*, 1989 Miss. Sec. LEXIS 13, at *1 (May 3, 1989) (same); *Gulf Oil Corp.*

litical subdivision of a state, or an agency or instrumentality of a state;⁵⁵ (3) a foreign government with which the United States currently maintains diplomatic relations;⁵⁶ (4) a federal credit union or a credit union, industrial loan association, or similar association organized under the laws of Mississippi;⁵⁷ or (5) a railroad, other common carrier, public utility, or public utility holding company.⁵⁸

Section 201 also exempts most securities issued by:⁵⁹ (6) a national bank⁶⁰ or federal savings and loan association,⁶¹ (7) a state bank,⁶² savings institution,⁶³ or trust company⁶⁴

Savs.—Stock Bonus Plan, 1985 Miss. Sec. LEXIS 2, at *1 (Feb. 19, 1985) (U.S. savings bonds). *See generally* Parsons, *supra* note 1, at 188.

⁵⁵ MISS. CODE ANN. § 75-71-201(1); *see, e.g.*, Va. Higher Educ. Tuition Trust Fund, 1996 Miss. Sec. LEXIS 3, at *1 (Sept. 5, 1996); Certificates of Participation, 1993 Miss. Sec. LEXIS 2, at *1 (Aug. 4, 1993); Stonegate Village Metro. Dist., 1992 Miss. Sec. LEXIS 3, at *1 (Apr. 16, 1992); S. Cal. Pub. Power Auth. Transmission Project Revenue Bonds, 1991 Miss. Sec. LEXIS 6, at *1 (Apr. 16, 1991); Salt Lake City, Utah Flexible Rate Revenue Bonds, Series 1990, 1990 Miss. Sec. LEXIS 12, at *1 (Jan. 8, 1990); Pa. Higher Educ. Assistance Agency, 1989 Miss. Sec. LEXIS 27, at *1 (Sept. 7, 1989); Mich. Educ. Trust, 1989 Miss. Sec. LEXIS 10, at *16 (Feb. 1, 1989). *See generally* Parsons, *supra* note 1, at 188.

⁵⁶ MISS. CODE ANN. § 75-71-201(2).

⁵⁷ *See id.* § 75-71-201(6).

⁵⁸ *Id.* § 75-71-201(7); *see, e.g.*, Duquesne Light Co., 1987 Miss. Sec. LEXIS 42, at *1 (Nov. 9, 1987); Ohio Edison Co. Collateralized Lease Bonds, 1987 Miss. Sec. LEXIS 25, at *1 (May 18, 1987); Niagara Mohawk Power Corp. Secured Facility Bonds, 1987 Miss. Sec. LEXIS 16, at *1 (Apr. 1, 1987). *See generally* Parsons, *supra* note 1, at 191.

⁵⁹ Notice the distinction here: sections 201(1), (2), (6), and (7) exempt securities “issued or guaranteed by” a listed entity; whereas, sections 201(3), (4), (5), and (9) exempt only securities “issued by” a listed entity and section 201(12) exempts only securities “of” a listed entity. *See* MISS. CODE ANN. § 75-71-201. The difference is more than semantic. *See, e.g.*, City of Redding Certificates of Participation, 1986 Miss. Sec. LEXIS 12, at *1 (Feb. 28, 1986) (refusing to recognize section 201(5) exemption for certificates guaranteed by Financial Guaranty Insurance Company (“FGIC”) because “FGIC is not the issuer”).

⁶⁰ *See* MISS. CODE ANN. § 75-71-201(3); *see also* Tender Options on State & Local Gov’t Bonds, 1990 Miss. Sec. LEXIS 13, at *1 (Jan. 9, 1990); Wells Fargo Inv. Trust, 1987 Miss. Sec. LEXIS 26, at *1 (May 18, 1987); Offer and Sale of Short Term Promissory Notes, 1986 Miss. Sec. LEXIS 5, at *1 (Jan. 31, 1986). *See generally* Parsons, *supra* note 1, at 188.

⁶¹ MISS. CODE ANN. § 75-71-201(4); *see, e.g.*, First Fed. Savs. & Loan Assoc., 1988 Miss. Sec. LEXIS 17, at *1-3 (May 3, 1988); Home Fed. Savs. & Loan Assoc., 1987 Miss. Sec. LEXIS 52, at *1-3 (Dec. 15, 1987); First Fed. Savs. & Loan Assoc., 1987 Miss. Sec. LEXIS 11, at *1-3 (Feb. 19, 1987). *See generally* Parsons, *supra* note 1, at 189.

⁶² MISS. CODE ANN. § 75-71-201(3); *see, e.g.*, Bank of Commerce, 1985 Miss.

organized and supervised under the law of any state; (8) a savings and loan, building and loan, or similar association organized and supervised under the law of any state and authorized to do business in Mississippi;⁶⁵ (9) an insurance company authorized to do business in Mississippi;⁶⁶ (10) a non-profit, religious, charitable, or benevolent corporation;⁶⁷ or (11) a cooper-

Sec. LEXIS 21, at *1-5 (Dec. 4, 1985). *See generally* Parsons, *supra* note 1, at 188.

⁶³ MISS. CODE ANN. § 75-71-201(3); *see, e.g.*, Imperial Thrift & Loan Assoc., 1996 Miss. Sec. LEXIS 4, at *1 (Oct. 22, 1996). *See generally* Parsons, *supra* note 1, at 188.

"The term 'savings institution' refers to a type of financial institution prevalent in the Northeast and not to savings and loan associations in general." *In re Sav. Inst. Sec. Exemption*, 1986 Miss. Sec. LEXIS 8, at *1-2 (Feb. 4, 1986). *See generally* Parsons, *supra* note 1, at 189.

⁶⁴ MISS. CODE ANN. § 75-71-201(3). *See generally* Parsons, *supra* note 1, at 188.

⁶⁵ MISS. CODE ANN. § 75-71-201(4). *See generally* Parsons, *supra* note 1, at 189.

The Mississippi Business Services Division has previously indicated its willingness to extend the section 201(4) exemption to, *inter alia*, notes issued by an agricultural cooperative marketing association and agricultural credit corporation, organized and authorized to do business in Mississippi, on the theory that it was "similar" to a savings and loan association. *See Staple Cotton Disc. Corp.*, 1987 Miss. Sec. LEXIS 41, at *1-5 (Nov. 9, 1987). *See generally* Parsons, *supra* note 1, at 189. However, the Division has indicated its unwillingness to extend the section 201(4) exemption to savings and loans not authorized to do business in Mississippi. *See, e.g.*, *Sav. Inst. Sec. Exemption*, 1986 Miss. Sec. LEXIS 8, at *1 (Feb. 4, 1986) ("The exemption relevant to your situation is found in section 75-71-201(4) and would require domestication by your company in this State in order to take advantage of the exemption."); *Offering of Subordinated Capital Notes*, 1985 Miss. Sec. LEXIS 17, at *1 (Aug. 23, 1985) ("Savings and loan associations such as Commonwealth must be authorized to do business in Mississippi before its securities are entitled to an exemption.").

⁶⁶ *See* MISS. CODE ANN. § 75-71-201(5); *see, e.g.*, P-I-E Mut. Ins. Co., 1992 Miss. Sec. LEXIS 5, at *1 (Dec. 10, 1992); VHA Ins. Co., 1987 Miss. Sec. LEXIS 20, at *1-2 (May 7, 1987); *see also supra* note 59 and accompanying text. *See generally* Parsons, *supra* note 1, at 192.

⁶⁷ MISS. CODE ANN. § 75-71-201(9); *see, e.g.*, Health Choice of Miss., Inc., 1995 Miss. Sec. LEXIS 1, at *1 (June 12, 1995); The Gen. Council of the Assemblies of God, 1993 Miss. Sec. LEXIS 1, at *1 (Oct. 8, 1993); Pooled Income Fund, 1989 Miss. Sec. LEXIS 29, at *1 (Sept. 19, 1989).

In addition to more traditional non-profit, charitable and religious issuers, the Business Services Division has determined that section 201(9) extends to non-profit corporate trade organizations. *See Collision Auto. Repair Servs., Inc.*, 1992 Miss. Sec. LEXIS 14, at *1-2 (Sept. 29, 1992).

ative organized under the laws of Mississippi, owned solely by residents of Mississippi, and operating wholly within the state.⁶⁸ Other exempt securities include: (12) any security listed or approved for listing on the American, Boston, Chicago, Cincinnati, Midwest, New York, Pacific, or Philadelphia Stock Exchange, or the Chicago Board Options Exchange;⁶⁹ (13) short-term promissory notes issued by commercial entities;⁷⁰ (14) investment contracts issued in connection with an

⁶⁸ MISS. CODE ANN. § 75-71-201(12); *see, e.g.*, Timber Producers Corp., 1988 Miss. Sec. LEXIS 24, at *1-3 (July 6, 1988).

⁶⁹ MISS. CODE ANN. § 75-71-201(8); Rule 707, Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,531, at 29,426; *see, e.g.*, Cent. Vt. Pub. Serv. Corp., 1992 Miss. Sec. LEXIS 2, at *1 (Nov. 10, 1992); AIG Liquidity Corp., 1992 Miss. Sec. LEXIS 1, at *1 (July 9, 1992); Niagara Mohawk Power Corp., 1987 Miss. Sec. LEXIS 16, at *1 (April 1, 1987); Clabir Corp., 1986 Miss. Sec. LEXIS 35, at *1-4 (Dec. 30, 1986); Sunshine Mining Co., 1986 Miss. Sec. LEXIS 28, at *1-4 (Oct. 1, 1986); Eastman Kodak Co., 1986 Miss. Sec. LEXIS 4, at *1 (Jan. 27, 1986); *see also infra* note 94 and accompanying text. *See generally* Securities, Broker-Dealer Registration, and Trade Exemptions, 1994 Miss. Sec. LEXIS 5, at *1-2 (Sept. 7, 1994) (noting section 75-71-201(8) exempts securities under certain stock exchanges and listed under Rule 707).

⁷⁰ MISS. CODE ANN. § 75-71-201(10); *see, e.g.*, *In re Stewart*, No. 97-05-59, 1998 Miss. Sec. LEXIS 3, at *14 (Aug. 27, 1998); *see also, e.g.*, *State v. Russell*, 358 So. 2d 409, 411-12 (Miss. 1978) (applying parallel exemption in former Mississippi Securities Law, MISS. CODE ANN. § 75-71-51(8) (1972), *repealed by* 1981 Miss. Laws, ch. 521, § 418).

This exemption “applies only to prime quality negotiable commercial paper of a type not ordinarily purchased by the general public, that is, paper issued to facilitate well recognized types of current operational business requirements,” and is only available to an offeror or seller who can establish that the instrument (1) is negotiable, (2) is of prime quality, (3) is not ordinarily purchased by the general public, (4) is used to facilitate current transactions, and (5) matures in nine months or less and does not automatically roll-over. *Stewart*, 1998 Miss. Sec. LEXIS 3, at *15-17. In *Stewart*, the Business Services Division concluded the promissory notes at issue were not entitled to the commercial paper exemption because they were not of “prime quality.” *Id.* at *17. It stated:

The issuer of the notes in this case, FLIC, was certainly not a seasoned or secure corporation . . . It was incorporated in Florida in April of 1995 and began issuing these promissory notes as early as eleven months thereafter. Within three years of its inception, FLIC was in bankruptcy. So, FLIC was not only unseasoned, but on the brink of bankruptcy during the period it issued the promissory notes. Clearly, under these circumstances, any promissory note it issued would not garner the title “prime quality” for the purposes of the commercial paper exemption.

Evidently, FLIC itself was not convinced of the quality of the notes, because there is no indication that it sought a rating from one of the

employee stock purchase, savings, pension, profit-sharing, or similar plan;⁷¹ and (15) oil, gas, and mineral leases, working interests, mineral or royalty interests or estates or an oil payment or net profit interest, provided the working interest is not less than 1/200th of the whole working interest, and any mineral lease or royalty sales are granted in exchange for labor, materials, or machinery used in drilling an oil or gas well.⁷²

Section 401 was amended in 1997 to also exempt from MSA registration "federal covered securities"⁷³ not otherwise exempt under section 201 or 203.⁷⁴ The MSA authorizes the Secretary of State to require the filing of certain documents and the payment of certain fees relating to federally covered securities.⁷⁵ However, the section 401 exemption is not premised on compliance with section 408. Therefore, no civil registration liability should attach to the offer or sale of federal covered securities even if the issuer, offeror or seller violates section 408.

established institutions which rate commercial paper such as Standard & Poor's, Dunn & Bradstreet or Moody's. Even if it had sought such a rating, nothing in the record indicates that any of these companies actually rated the FLIC promissory note offering.

Hence, FLIC's lack of an established history of operations and its financial insecurity during the offering period, prevents any finding other than that these notes are not prime quality. Thus, they are not commercial paper, and are, therefore, not exempt from the registration requirements of the Act.

Id. at *19-21.

⁷¹ MISS. CODE ANN. § 75-71-201(11); *see, e.g.*, Nissan Motor Corp. Employee Savs. Plan, 1993 Miss. Sec. LEXIS 3, at *1 (Nov. 29, 1993); Regan Holding Corp., 1991 Miss. Sec. LEXIS 9, at *1 (Dec. 16, 1991); Int'l Family Entm't, Inc., 1990 Miss. Sec. LEXIS 19, at *1 (Mar. 26, 1990); The Loewen Group, Inc., 1990 Miss. Sec. LEXIS 18, at *1 (Feb. 13, 1990); PCL Indus. Ltd., 1989 Miss. Sec. LEXIS 25, at *1-2 (Aug. 5, 1989); MCI Communications Corp., 1988 Miss. Sec. LEXIS 21, at *1-3 (June 10, 1988); Gulf Oil Corp. Savs., 1985 Miss. Sec. LEXIS 2, at *1 (Feb. 19, 1985). *See generally* Parsons, *supra* note 1, at 189; Vaaler, *supra* note 1, at 349-51 (discussing exemption of employer securities offered or sold pursuant to employee plans).

⁷² MISS. CODE ANN. § 75-71-201(13); *see, e.g.*, Physicians Drilling Group, 1988 Miss. Sec. LEXIS 33, at *1-2 (Sept. 28, 1988).

⁷³ *See supra* note 51 and accompanying text (discussing securities exempt from registration).

⁷⁴ MISS. CODE ANN. § 75-71-401.

⁷⁵ *See id.* § 75-71-408.

b. Exempt Transactions

Section 203 of the MSA identifies certain sales, offerings for sale, solicitations, subscriptions, dealings in, and deliveries of securities that—due to the nature of the transaction, the nature of the parties, or both—are exempt from the MSA's registration requirements;⁷⁶ and, therefore, will not give rise to registration liability.⁷⁷ Section 203 exempts from registration most: (1) isolated nonissuer transactions;⁷⁸ (2) nonissuer distributions of outstanding securities of issuers for which certain information is contained in a recognized securities manual;⁷⁹ (3) nonissuer distributions of outstanding securities with

⁷⁶ *Id.* § 75-71-203. The section 203 exemptions generally track those contained in section 402(b) of the 1956 Uniform Securities Act, 7C U.L.A. 219, 219-21 (2000). Mississippi's preorganization certificate or subscription exemption is noticeably more generous than the Uniform Act's, allowing up to thirty-five subscribers, as opposed to ten. Compare MISS. CODE ANN. § 75-71-203(10) (allowing up to thirty-five subscribers) with Uniform Securities Act § 402(b)(10), 7C U.L.A. at 220 (allowing only ten subscribers). The section 203 exemptions are also similar to those granted by section 4 of the 1933 Securities Act, 15 U.S.C. § 77d (1994), although both the MSA and the Uniform Act provide a number of transactional exemptions not provided by section 4.

⁷⁷ MISS. CODE ANN. § 75-71-401, -717(a)(1). Neither the transactional exemptions in section 203 nor securities exemptions in section 201 affect the liability of anyone who offers to sell or sells securities in violations of the MSA's anti-fraud provisions. See *infra* note 109 and accompanying text.

⁷⁸ MISS. CODE ANN. § 75-71-203(1). See generally *In re Securities, Broker-Dealer Registration, and Trade Exemptions*, 1994 Miss. Sec. LEXIS 5 (Sep. 7, 1994).

⁷⁹ MISS. CODE ANN. § 75-71-203(2)(A); see Rule 709, Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34, 352, at 29,426 (identifying eight "recognized securities manuals"); Mergent's Manuals Rule Change, 2001 Miss. Sec. LEXIS 7, *1 (Apr. 17, 2001) (recognizing the sufficiency, for purposes of Rule 709, of "information . . . published in Mergent's Manuals or CD-ROMs, or disseminated by Mergent's FIS, Inc. electronically over the Internet"); see, e.g., *Shivangi v. Dean Witter Reynolds, Inc.*, 107 F.R.D. 313, 322 (S.D. Miss. 1985); *AM Swiss Pharm., Inc.*, 1989 Miss. Sec. LEXIS 8 (Jan. 11, 1989); *Leeds Capital Corp.*, 1988 Miss. Sec. LEXIS 15 (Feb. 22, 1988); *FONAR Corp.*, 1987 Miss. Sec. LEXIS 17 (Apr. 21, 1987); *Elders IXL Ltd.*, 1987 Miss. Sec. LEXIS 23 (May 13, 1987).

In *Redland Preferred Stock PLC*, 1989 Miss. Sec. LEXIS 35 (Nov. 20, 1989), the Business Services Division found that section 203(2)(A) did not exempt from registration shares of an issuer for whom the required fiscal year financial information was lacking, despite the fact that a recognized securities manual included all other required information about the issuer and all required information about the issuer's parent.

a fixed maturity or fixed interest or dividend;⁸⁰ (4) unsolicited nonissuer orders or offers to buy executed by or through registered broker-dealers;⁸¹ (5) transactions between issuers and underwriters or among underwriters;⁸² (6) transactions in bonds or other evidences of indebtedness secured by a mortgage or deed of trust on real or chattel property;⁸³ (7) transactions by executors, administrators, receivers, trustees in bankruptcy, guardians, or conservators;⁸⁴ (8) transactions executed by a bona fide pledgee;⁸⁵ (9) offers or sales to a bank, savings institution, trust company, pension fund, profit-sharing trust, other financial institution, insurance company, investment company, broker-dealer, or institutional buyer;⁸⁶ (10) sales made by an issuer, without public solicitation or advertisement, for no commission, which sold its securities during the preceding twelve months to not more than ten persons who bought for their own account;⁸⁷ (11) transactions involving preorganization certifi-

⁸⁰ MISS. CODE ANN. § 75-71-203(2)(B).

⁸¹ *Id.* § 75-71-203(3).

⁸² *Id.* § 75-71-203(4).

⁸³ *Id.* § 75-71-203(5); *see, e.g.*, 1987 Miss. Sec. LEXIS 12 (Feb. 19, 1987).

⁸⁴ MISS. CODE ANN. § 75-71-203(6); *see, e.g.*, Paradyne Corp., 1987 Miss. Sec. LEXIS 22 (May 13, 1987).

⁸⁵ MISS. CODE ANN. § 75-71-203(7); *see, e.g.*, OmniBank of Mantee, 1990 Miss. Sec. LEXIS 10 (Sept. 26, 1990).

⁸⁶ MISS. CODE ANN. § 75-71-203(8); *see, e.g.*, Prudential Sec. Inc., 1995 Miss. Sec. LEXIS 3 (Oct. 12, 1995); Corporate Network Brokerage Servs., Inc., 1994 Miss. Sec. LEXIS 2 (May 13, 1994); *see also* Rule 103(G), Miss. Blue Sky Regs., *reprinted in* 2A BLUE SKY L. REP. (CCH) ¶ 34,403, at 29,401 (2001) (defining, *inter alia*, "Institutional Buyer"). *See generally* Vaaler, *supra* note 1, at 327-32.

⁸⁷ MISS. CODE ANN. § 75-71-203(9); *see, e.g.*, Gulfport Out-Patient Surgical Ctr., Ltd., 1992 Miss. Sec. LEXIS 6 (June 8, 1992); Union Compress Warehouse Co., L.P., 1988 Miss. Sec. LEXIS 28 (Sep. 7, 1988). *See generally* Parsons, *supra* note 1, at 189-90; Vaaler, *supra* note 1, at 332-37.

The ten person limit in section 203(9) "applies to the whole transaction, not just ten persons in the State of Mississippi." Concord Growth Corp., 1988 Miss. Sec. LEXIS 4, at *1 (Jan. 11, 1988). A husband and wife who purchase a security jointly are a single purchaser for purposes of section 203(9). *See* 1988 Miss. Sec. LEXIS 37, at *1 (Oct. 12, 1988). This exemption is self-effecting. *See* Rule 701, Miss. Blue Sky Regs., *reprinted in* 2A BLUE SKY L. REP. (CCH) ¶ 34,521, at 29,424 (2001).

The Business Services Division has the power, under both section 203(9) and section 203(13), to waive strict compliance with section 203(9). *See* MISS. CODE ANN. § 75-71-203(9), (13); *infra* text accompanying note 91. It has, at various times, chosen to exercise that power and to refrain from doing so. *Compare, e.g.*,

cates or subscriptions;⁸⁸ (12) transactions pursuant to a no-

Centech Labs., Inc., 1996 Miss. Sec. LEXIS 5 (July 1, 1996) (waiving ten-person limit), Gentry Gowns, Inc., 1991 Miss. Sec. LEXIS 12 (July 12, 1991) (waiving no-commission requirement), and Sabre Indus., Inc., 1991 Miss. Sec. LEXIS 11 (Jan. 16, 1991) (same), *with, e.g.*, Concord Growth Corp., 1989 Miss. Sec. LEXIS 11 (Feb. 24, 1989) (declining to waive either the ten-person limit or no-commission requirement).

⁸⁸ MISS. CODE ANN. § 75-71-203(10). *See generally* Vaaler, *supra* note 1, at 337-38. This exemption appears not to extend to offers pursuant to a merger or other corporate reorganization. First State Bank, 1985 Miss. Sec. LEXIS 3 (Feb. 21, 1985). Those transactions, however, are effectively exempted by section 105(1)(6)(C), which treats them as outside of the definition of "sale" or "offer to sell." *See* MISS. CODE ANN. § 75-71-105(1)(6)(C); *supra* note 46.

In *Russell v. Southern National Foods, Inc.*, 754 So. 2d 1246 (Miss. 2000), the Mississippi Supreme Court held that the MSA does not require registration of preorganization subscriptions, at least so long as the subscribers can be characterized as "insiders":

The appellants assert that the trial court erred in its application of the law when it relied on *Guynn v. Shulters*, 223 Miss. 232, 78 So. 2d 114 (1955). *Guynn* held that preincorporation stock certificates did not have to be registered if they were sold to the incorporators of a "to be formed" corporation. . . .

The appellants proceed on the theory that *Guynn* predates the current Blue Sky statutes, and thus the case has no application. Appellants' main contention is that the Mississippi Code of 1942 has been repealed or superceded by the Mississippi Securities Act of 1981, and thus *Guynn* contradicts the current securities regulations. . . .

. . . . In *Ayers v. Wolfenbarger*, 491 F.2d 8 (5th Cir. 1974), the court stated the acquisition of the original issue of stock was nothing more than organizational stock. The sale of stock to the promoters was a private offering and, therefore, exempt from the registration requirements of the Federal Securities Act.

In *SEC v. Ralston Purina Co.*, 346 U.S. 119, 125 (1953), the Court held the applicability of the registration requirement in the federal Securities Act should turn on whether the particular class of persons affected need the protection of the Act. As this Court held in *Guynn* and the chancellor also ruled here, the appellants did not need the protection of the Mississippi Securities Act nor was it the statute's intent to afford this group protection.

In summary, considering the clear purpose of the Act is to protect the general public, the trial court found the appellants were "insiders." Appellants were appraised of all material data, and they had access to information. There was a limited number of subscribers, having a privileged relationship with the corporation. Their present knowledge, involvement in forming the corporation, and ability to acquire information would not afford them protection under the Act. *Guynn* is not overruled.

Id. at 1249-52 (citations omitted).

commission offer to existing securities holders of the issuer who also hold convertible securities, nontransferable warrants, or short-term transferable warrants;⁸⁹ and (13) non-sale offers of securities registered under both the MSA and the 1933 Securities Act for which no stop order or refusal order is in effect and no public proceeding for such order is underway.⁹⁰

Section 203 also empowers the Secretary of State to exempt from registration otherwise non-exempt securities if the Secretary finds that "(A) such registration is neither necessary in the public interest nor for the protection of investors; or (B) such exemption shall further the objectives of compatibility with federal exemptions and uniformity among the states."⁹¹ Pursuant to that authority, the Secretary of State has (1) adopted the Uniform Limited Offering Exemption;⁹² (2) exempted domestic issuer private placements to not more than thirty-five (35) persons within a twelve (12) month period;⁹³ (3) in essence, extended the section 201(8) exchange-listed securities exemption to NASDAQ National Market System securities;⁹⁴ (4) adopted an Internet solicitation exemption;⁹⁵ (5) expanded the exemption already afforded by section 201(12)

⁸⁹ MISS. CODE ANN. § 75-71-203(11); *see, e.g.*, Affiliated Research Ctrs., Inc., 1996 Miss. Sec. LEXIS 13 (Sept. 16, 1996); Eastco Indus. Safety Corp., 1996 Miss. Sec. LEXIS 6 (Aug. 23, 1996); Commercial Nat'l Fin. Corp., 1989 Miss. Sec. LEXIS 34 (Nov. 10, 1989); Tex. Am. Group, Inc., 1989 Miss. Sec. LEXIS 28 (Sept. 13, 1989); Sun Equities Corp., 1988 Miss. Sec. LEXIS 34 (Oct. 5, 1988); Bucyrus-Erie Co., 1988 Miss. Sec. LEXIS 29 (Sept. 14, 1988); VMS Strategic Land Fund II, 1988 Miss. Sec. LEXIS 26 (Aug. 29, 1988). *See generally* Parsons, *supra* note 1, at 190-91; Vaaler, *supra* note 1, at 347-49.

⁹⁰ MISS. CODE ANN. § 75-71-203(12).

⁹¹ *Id.* § 75-71-203(13).

⁹² Rule 703, Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,522, at 29,424 (2001); *see, e.g.*, ROMAXSCO Exploration Co., 1987 Miss. Sec. LEXIS 36 (Sept. 14, 1987). *See generally* Vaaler, *supra* note 1, at 338-44.

⁹³ Rule 705, Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,523, at 29,426; *cf.* Physicians Drilling Group, 1988 Miss. Sec. LEXIS 33 (Sept. 28, 1988) (discussing Rule 705, but advising that it is only available to domestic issuers). *See generally* Vaaler, *supra* note 1, at 344-47.

⁹⁴ Rule 711, Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,534, at 29,428 (2001). *See generally* Securities, Broker-Dealer Registration, and Trade Exemptions, 1994 Miss. Sec. LEXIS 5, at *1-2 (Sept. 7, 1994).

⁹⁵ Rule 713, Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,536, at 29,428 (2001).

to cooperative securities;⁹⁶ and (6) exempted from registration the offer for sale and sale of certain viatical settlement investment contracts.⁹⁷

2. *Primary Liability for Selling Unregistered Securities*

Section 717(a)(1) entitles a buyer to sue “any person who offers or sells a security in violation of Section . . . 75-71-401.”⁹⁸ Section 717(a)(1), like its federal counterpart, section 12(a)(1) of the 1933 Securities Act,⁹⁹ is essentially a “strict liability” statute.¹⁰⁰ As long as the plaintiff can establish that the security was unregistered at the time of the sale, the defendant will be liable, unless the defendant can establish that the security or the transaction itself was exempt from registration.¹⁰¹

3. *Defenses to Registration Liability*

a. *Standing*

Section 717(a)(1)'s protection extends only to buyers.¹⁰² A

⁹⁶ Rule 715, Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,538, at 29,429 (2001).

⁹⁷ Rule 902, Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,572, at 29,432 (2001).

⁹⁸ MISS. CODE ANN. § 75-71-717(a)(1) (2000).

⁹⁹ 15 U.S.C. § 77l(a)(1) (Supp. V 1999); see *supra* note 10.

¹⁰⁰ See, e.g., *Hill York Corp. v. Am. Int'l Franchises, Inc.*, 448 F.2d 680, 686 (5th Cir. 1971) (holding that plaintiff may recover under what is now section 12(a)(1) “regardless of whether he can show any degree of fault, negligent or intentional, on the seller’s part”); accord *Swenson v. Engelstad*, 626 F.2d 421, 444-45 (5th Cir. 1980).

¹⁰¹ MISS. CODE ANN. § 75-71-207; see *Blinder, Robinson & Co.*, 1990 Miss. Sec. LEXIS 14, at *1 (Jan. 17, 1990); *Staple Cotton Disc. Corp.*, 1987 Miss. Sec. LEXIS 41, at *1 (Nov. 9, 1987).

¹⁰² MISS. CODE ANN. § 75-71-717(a)(1) (“Any person who offers or sells a security in violation of section . . . 75-71-401 . . . is liable to the person buying the security from him”); see, e.g., *Fortenberry v. Foxworth Corp.*, 825 F. Supp. 1265, 1279 (S.D. Miss. 1993) (“[O]nly purchasers of securities can bring an action under § 717.”).

What, exactly, makes one a “buyer” is less than clear. The term is undefined in the MSA and has not been the subject of any reported Mississippi case. Construing an analogous provision of the 1933 Securities Act, a federal district court held that a plaintiff did not have to be an owner to be considered the purchaser, but had to have “sufficient indicia of ownership to effectuate a tender of the secu-

person who did not purchase a security lacks standing to sue the person who sold it for failing to register properly the security.

b. Limitations

A purchaser must bring any claim for a violation of the MSA's registration provisions within two years of the date of sale.¹⁰³ This limitations period is unaffected by the plaintiff's failure to discover the violation or by any form of equitable tolling.¹⁰⁴

c. Waiver

The MSA prohibits any attempt by the parties to a transaction subject to the MSA to waive the MSA's requirements.¹⁰⁵

rities." *Monetary Mgmt. Group, Inc. v. Kidder, Peabody & Co.*, 604 F. Supp. 764, 768 (E.D. Mo. 1985) (holding that person must be "purchaser" within meaning of securities statutes to be real party in interest). The plaintiff in *Monetary Management Group* purchased the bonds in question for a customer, and the court found this sufficient to establish the plaintiff as the purchaser and as the proper party to bring an action for rescission. *Id.* at 767. A Texas Court of Appeals, construing the analogous provision of the Texas Securities Act, TEX. REV. CIV. STAT. ANN. art. 581-33A(1) (West Supp. 2000), found "sufficient indicia of ownership" where the plaintiff "negotiated with the control persons for the purchase of [the] stock and was the record holder of the stock," despite uncertainty as to the source of the funds to make the purchase. *Summers v. WellTech, Inc.*, 935 S.W.2d 228, 233 (Tex. App. 1996).

¹⁰³ See MISS. CODE ANN. § 75-71-725. By comparison, claims for violations of section 12(a)(1) of the 1933 Securities Act must be brought within one year of their occurrence, but in any event within three years of the first bona fide offer of the security to the investing public. See 15 U.S.C. § 77m. Thus, the MSA generally affords Mississippi plaintiffs a more generous period of time within which to bring suit over the sale of unregistered and non-exempt securities than they are afforded by section 12(a)(1).

¹⁰⁴ Likewise, equitable tolling may not extend limitations for a section 12(a)(1). See *Gardner v. Investors Diversified Capital, Inc.*, 805 F. Supp. 874, 878 (D. Colo. 1992) (finding that plaintiffs had failed to file complaint within one year statute of limitations).

¹⁰⁵ MISS. CODE ANN. § 75-71-729 (invalidating any "condition, stipulation or provision binding any person acquiring any security to waive compliance with any provision of [the MSA] or any rule or order hereunder"). The MSA's anti-waiver provision is essentially the same as the comparable federal provision. See 15 U.S.C. § 77n (1994) ("Any condition, stipulation, or provision binding any person

d. Other Defenses (or Lack Thereof)

In contrast to the MSA's antifraud provisions,¹⁰⁶ neither the buyer's knowledge of the offense nor the seller's lack of knowledge is a defense to liability under section 717. Likewise, equitable defenses such as estoppel, laches, waiver, *in pari delicto*, ratification, and unclean hands, which may apply to common law or statutory claims arising out of a defendant's material misrepresentations or omissions regarding a securities transaction,¹⁰⁷ do not apply to claims arising out of a defendant's violation of the registration provisions of the MSA.¹⁰⁸ Therefore, in the absence of a standing or limitations defense, a primary violator will be strictly liable.

C. Statutory Liability for Material Misrepresentations or Omissions in an Offer or Sale of Securities

Irrespective of any exemption from registration,¹⁰⁹ the MSA imposes liability on those who offer to sell or sell securities by means of any written or oral communication:

- (1) containing an untrue statement of material fact, or
- (2) omitting a material fact necessary to make those statements that were made, in light of the circumstances in which they were made, not misleading, *unless*:
- (3) the seller can prove:

acquiring any security to waive compliance with any provision of this subchapter or of the rules and regulations of the Commission shall be void.”).

Section 729 does not apply to, and therefore should not diminish the effectiveness of, a bona fide release or settlement of an existing claim, whether or not a suit has been filed. *See* Murtagh v. Univ. Computing Co., 490 F.2d 810, 816 (5th Cir.) (construing parallel provision in 1933 Securities Act).

¹⁰⁶ *See infra* Part II.C.6.c.i-ii.

¹⁰⁷ *See infra* note 148.

¹⁰⁸ *See generally* Hall v. Johnston, 758 F.2d 421, 423 (9th Cir. 1985) (applying analogous provision of Oregon Securities Law, OR. REV. STAT. § 59.115(1)(a) (1999)).

¹⁰⁹ Compare MISS. CODE ANN. § 75-71-717(a)(2) (“Any person who . . . offers or sells a security . . .”) with *id.* § 75-71-717(a)(1) (“Any person who offers or sells a security in violation of section 75-71-117(a), 75-71-301, or 75-71-401 . . .”). The only requirement for section 717(a)(2) to apply is that the device or transaction be a “security” for purposes of section 105(n). *See supra* Part II.A.1.

(a) that she did not know, nor could she have known in the exercise of reasonable care, of the untruth or omission, or

(b) that the buyer actually knew of the untruth or omission before purchasing the securities.¹¹⁰

¹¹⁰ MISS. CODE ANN. § 75-71-717(a)(2). Section 717(a)(2) parallels section 12(a)(2) of the 1933 Securities Act, which makes liable any person who

offers or sells a security . . . by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission.

15 U.S.C. § 77l(a)(2) (Supp. V 1999). Section 717(a)(2) is broader than section 12(a)(2) in two important ways. First, section 717(a)(2) does not limit its reach to only those securities sold "by the use of any means or instruments of transportation or communication in interstate commerce or of the mails." Second, section 717(a)(2) does not limit its reach to only those securities sold "by means of a prospectus or oral communication."

The MSA contains another anti-fraud provision prohibiting material misrepresentations or omissions in the offer or sale (as well as the purchase) of securities. Section 501 declares it

unlawful for any person, in connection with the offer, sale or purchase of any security, directly or indirectly,

- (1) To employ any device, scheme or artifice to defraud;
- (2) 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 are made, not misleading; or
- (3) To engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person.

MISS. CODE ANN. § 75-71-501; *see, e.g.*, *Felts v. Nat'l Account Sys. Ass'n*, 469 F. Supp. 54, 65-66 (N.D. Miss. 1978) (applying precursor to section 501, section 43 of former Mississippi Securities Law, MISS. CODE ANN. § 75-71-43 (1972), *repealed* by 1981 Miss. Laws, ch. 521, § 418, and finding that issuer "engaged in acts, practices and a course of business which operated as a fraud and a deceit and employed deceptive devices, artifices and schemes to defraud the plaintiffs in violation of," *inter alia*, former section 43(b)).

Section 501 is similar to Rule 10b-5(b), promulgated under section 10(b) of the 1934 Securities Exchange Act, 15 U.S.C. § 78j(b) (1994), and declaring it unlawful for any person . . .

- (a) To employ any device, scheme, or artifice to defraud,
- (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the

The buyer bears the burden of proving either a material misrepresentation or omission.¹¹¹ The seller bears the burden of proving either her own diligent lack of knowledge or the plaintiff's actual knowledge.¹¹²

1. Form of Misrepresentation

Silence can be a form of misrepresentation for purposes of section 717(a)(2),¹¹³ as can an incomplete statement, where what remains unsaid is material.¹¹⁴ An opinion may be actionable under section 717(a)(2) if the speaker did not actually hold the opinion at the time she expressed it or if she expressed it knowing that it was misleadingly incomplete.¹¹⁵

light of the circumstances under which they were made, not misleading,
or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5(b) (2000). While an integral part of criminal and administrative enforcement of the MSA, section 501 is of no particular relevance to our discussion because the Mississippi Supreme Court has held that it gives rise to no private cause of action. *See Allyn v. Wortman*, 725 So. 2d 94, 102 (Miss. 1998) (holding that no private cause of action is implied from section 17(a) of Securities Act of 1933, and therefore none exists for nearly identical state statute).

¹¹¹ *See, e.g., Russell v. S. Nat'l Foods, Inc.*, 754 So. 2d 1246, 1254 (Miss. 2000) (finding summary judgment proper when party fails to establish facts supporting claim of misrepresentation).

¹¹² *See infra* Parts II.C.6.c.ii & II.C.6.c.i, respectively.

¹¹³ MISS. CODE ANN. § 75-71-717(a)(2) (2000) (establishing liability for, *inter alia*, offering to sell or selling securities by use of written or oral communication which "om[its] 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"); *see, e.g., In re J. F. (Jim) Straw d/b/a Am. Bus. Club*, No. 92-04-08, 1992 Miss. Sec. LEXIS 17, at *4 (Apr. 17, 1992) (finding a material omission where offering materials "[f]ailed to state that the average period of time which an investor must wait to receive [the promised benefit] is two years").

¹¹⁴ *See, e.g., In re BMT Racing Stables*, No. CD 86-8-1, 1986 Miss. Sec. LEXIS 1, at *2 (Sep. 10, 1986) (finding that offerors made material misrepresentation when their materials offering for purchase interests in thoroughbred race horses included photo of horse in which offerors had no interest to sell).

¹¹⁵ *See Va. Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 1094-95 (1991) (finding opinion actionable under parallel federal law).

By comparison, it appears that Mississippi courts will not entertain a claim for common law fraud or negligent misrepresentation in the context of a securities transaction based on an opinion—whether truly held by the party expressing it or

Likewise, a promise may be actionable under section 717(a)(2) if the promisor made the promise for the purpose of inducing the promisee to purchase securities.¹¹⁶

A misrepresentation need not be made directly to the plaintiff to give rise to liability under section 717(a)(2).¹¹⁷

not. See *Guynn v. Shulters*, 78 So. 2d 114, 122 (Miss. 1955) (holding that, in order to rescind stock purchase based on fraudulent inducement, buyer must show, *inter alia*, "that the statement was not uttered as an opinion, but as an ascertained and existing fact").

¹¹⁶ See, e.g., *First Mobile Home Corp. v. Little*, 298 So. 2d 676, 681 (Miss. 1974) (explicitly distinguishing actionability under MSA of promises made to induce purchase of securities from actionability of promises in general under Mississippi common law).

As a rule, Mississippi courts will not entertain common law fraud or negligent misrepresentation claims based on promises of future action—regardless of whether the promisor intended to keep his promise when he made it. See, e.g., *Spragins v. Sunburst Bank*, 605 So. 2d 777, 780 (Miss. 1992) (holding that fraudulent misrepresentations must be related to past or present existing facts); *accord R.C. Constr. Co. v. Nat'l Office Sys., Inc.*, 622 So. 2d 1253, 1256 (Miss. 1993) (concurring in ruling that misrepresentations cannot contain promise of future conduct).

¹¹⁷ In this vein, the Mississippi Supreme Court has adopted the "fraud-on-the-market" theory, which dispenses with any requirement that the material misrepresentation or omission giving rise to the plaintiff's claim have been directed at the plaintiff.

The fraud-on-the-market theory . . . protects the integrity of the market as a whole by ensuring that the market receives timely and accurate information. Since the goal of the fraud-on-the-market doctrine is to ensure a level playing field for all potential investors, a plaintiff need not show that he heard or relied on the misrepresentations. He need only show that the defendant's misrepresentation distorted the securities market price and that the plaintiff was relying on the integrity of the market to establish the genuine value of the securities by reflecting all material information available.

Allyn v. Wortman, 725 So. 2d 94, 101 (Miss. 1998) (citations omitted). Justice McRae excoriated the majority for adopting this theory in a case in which the majority admitted it did not apply on the facts. See *id.* at 104 (McRae, J., dissenting). No subsequent opinion of the Mississippi Supreme Court has gainsaid the *Allyn* majority's adoption of the theory.

A plaintiff suing for common law fraud would have to prove, *inter alia*, that the defendant intended for the plaintiff to act in reliance upon the misrepresentation or omission. See *infra* note 138. The defendant must have directed the misrepresentation or omission to the plaintiff, intending the plaintiff to act thereon; otherwise, the plaintiff's common law fraud claim will fail. See, e.g., *Levens v. Campbell*, 733 So. 2d 753, 762 (Miss. 1999) (rejecting claim of fraud against person with whom plaintiff had never spoken); *Boling v. A-1 Detective & Patrol Serv., Inc.*, 659

2. Materiality

For purposes of the MSA, an omission or misrepresentation is actionable only if it is material.¹¹⁸ An omission or misrepresentation is material if it “would enable a prudent individual to make an informed investment decision.”¹¹⁹

So. 2d 586, 590 (Miss. 1995) (stating fraud can never be presumed, but must be proven by clear and convincing evidence); *Cook v. Children's Med. Group, P.A.*, 756 So. 2d 734, 744 (Miss. 1999) (Smith, J., concurring, joined by Cobb, J.) (refusing to adopt doctrine of imputed reliance). A plaintiff suing for common law negligent misrepresentation must show that, *inter alia*, the negligent misrepresentation was made to her. *See, e.g., Arnona v. Smith*, 749 So. 2d 63, 67 (Miss. 1999).

The *Allyn* court was considering the doctrine in the context of a common law fraud claim—hence, the “reliance” language. *See infra* note 138 and accompanying text. It seems unfathomable that the court would recognize the theory in the context of a common law claim but not in the context of a section 717(a)(2) claim.

¹¹⁸ *See* MISS. CODE ANN. § 75-71-717(a)(2). Materiality is also a requisite of liability under section 12(a)(2) of the 1933 Securities Act, *see supra* note 110, and section 10(b) of the 1934 Securities Exchange Act and Rule 10b-5 promulgated thereunder, *see id.*, as well as an element of both common law fraud, *see infra* note 138, and negligent misrepresentation, *see infra* note 139.

For purposes of section 12(a)(2) and section 10(b)/Rule 10b-5, information is material if there is a substantial likelihood that a reasonable investor would consider it important in deciding whether to buy or sell or how to vote the securities at issue. *See, e.g., TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976); *Grossman v. Novell, Inc.*, 120 F.3d 1112, 1119 (10th Cir. 1997) (all holding that fact may be considered material if there is “substantial likelihood that a reasonable person would consider it important in deciding whether to buy or sell shares”); *Azzielli v. Cohen Law Offices*, 21 F.3d 512, 518 (2d Cir. 1994). The materiality standard for common law fraud and negligent misrepresentation appears to be more strict. While the cases requiring materiality for a claim of either fraud or negligent misrepresentation, or both, are legion, few if any bother to hint at the meaning of “materiality.” From a review of the cases, it appears that the basic test of materiality for both common law fraud and negligent misrepresentation is whether the plaintiff would not have agreed to the transaction as structured “but for” the defendant’s material misrepresentation or omission. *See, e.g., Holland v. Mayfield*, No. 96-CA-01169-SCT, 1999 WL 353023, at *10 (Miss. June 3, 1999) (holding that defendant’s misrepresentations were material for purposes of plaintiffs’ common law fraud claims because “[a]lthough a couple of Investors testified that they were not sure if they would have invested . . . if they had known of the front-end payments, most testified that they definitely would not have invested if they had known.”).

¹¹⁹ Rule 103(I), Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,403, at 29,402. One might wonder if the “prudent individual” standard of materiality imposed by Rule 103(I) might be more difficult to establish than the “reasonable investor” standard under comparable federal law. Prudence might

In *Seaboard Planning Corp. v. Powell*,¹²⁰ decided under the precursor to section 717(a)(2),¹²¹ Yates, a registered agent of defendant Seaboard, sold \$20,000 worth of units in a real estate limited partnership to Powell. Powell was a 77-year-old farmer who “had never owned corporate stock,” “did not know

suggest more care than mere reasonableness. However, there is no indication in Mississippi case law—within or without the sphere of securities law—that prudent and reasonable are not synonymous.

In *New Amsterdam Casualty Co. v. Wood*, 57 So. 2d 141 (Miss. 1952), decided under the 1942 version of the MSA, MISS. CODE ANN. § 5360 (Supp. 1971), codified as amended at MISS. CODE ANN. § 75-71-1 (1972), repealed by 1981 Miss. Laws, ch. 521, § 418, the president of National Acceptance Corporation (NAC), Paul Schumpert, sold shares in NAC “by representations that payments for the stock sold would go into the capital structure of the corporation.” *Wood*, 57 So. 2d at 142. In fact, Schumpert was selling his own shares and pocketing the proceeds. *See id.* at 142-43. He also purchased stock from other existing shareholders and resold it at a substantial profit—again representing to the buyers that the shares were being issued by NAC. *See id.* at 143. While the court was not asked to decide specifically whether Schumpert’s representations were material, it did affirm the judgment against the surety (New Amsterdam), which was premised on Schumpert’s violation of the precursor to section 717(a)(2). *See id.* at 144. In any event, it seems obvious that the fact that he was selling his own shares rather than the corporation’s shares—suggesting that he might not have concerns about the future of the corporation—and the fact that the proceeds were going into his pocket rather than into the corporation—possibly affecting the corporation’s ability to meet current obligations or to expand—are both facts that “would enable a prudent individual to make an informed decision” whether to buy the shares. As Chief Judge Clark wrote in another case where the source of the shares was misrepresented:

By misrepresenting to Johnson that the stock was owned by an estate, and thus was available for sale due to the fortuity of a death, these defendants concealed that the chief executive officer of Mississippi Candies, although outwardly seeking financial capital for the financially plagued company, in fact, had chosen to divest himself of a portion of his investment in the corporation. In this context, the misstatement of the ownership of the securities offered for sale was a misrepresentation of material fact because there is a substantial likelihood that a reasonable investor would have considered the true ownership important in deciding on his course of action with respect to the transaction.

Johnson v. Yerger, 612 F.2d 953, 957 (5th Cir. 1980) (citations omitted).

¹²⁰ 364 So. 2d 1091 (Miss. 1978).

¹²¹ Former section 75-71-25 entitled “[a]ny person or persons who shall be induced to purchase any stocks, bonds or other securities . . . by reason of any misrepresentation of any material facts concerning such stocks, bonds or other securities” to bring suit over such misrepresentation. MISS. CODE ANN. § 75-71-25 (1972) (repealed by Laws, 1981, ch. 521, § 418, as of July 1, 1981).

what a prospectus . . . was,” and “had only a sixth grade education, and was totally unfamiliar with real estate . . . limited partnerships.”¹²² Powell initially asked Yates about buying bonds, but Yates discouraged Powell from buying bonds and recommended, on the advice of Seaboard *and without having read the prospectus himself*, the limited partnership interest.¹²³

The limited partnership interests that Yates sold to Powell were designed for

persons in higher federal income tax brackets, [who] by taking advantage of the depreciation provisions of the [IRS code] and regulations, produce considerable tax savings. . . . Persons in low income tax brackets generally do not profit from this type of partnership.¹²⁴

Despite Powell’s modest means,¹²⁵ Yates recommended the limited partnerships units because of their liquidity.¹²⁶

After Powell received the first two quarterly dividend checks as promised, the third check was for half the amount promised, and was the last one forthcoming. Powell sought to cash out his investment, but found that “the securities had no established market and no cash-in value.”¹²⁷ Powell and his wife sued Yates and Seaboard, and were awarded his \$20,000 at trial. The Mississippi Supreme Court affirmed, finding ample evidence in the record to support a judgment based on Yates’s material misrepresentations.¹²⁸

In one of a number of related enforcement orders,¹²⁹ the

¹²² *Seaboard Planning*, 364 So. 2d at 1093-94.

¹²³ *See id.* at 1093-94.

¹²⁴ *Id.*

¹²⁵ *See id.* (“Yates knew that the year of the sale was the only year that Mr. Powell had anything to sell to create any substantial tax liability, and that in the next year Mr. Powell, in all likelihood, was going to be back in a low income tax bracket, but did not explain this to them.”).

¹²⁶ *See id.* (“Yates told the Powells that he recommended this investment, and that this was a correct vehicle if Mr. Powell needed his money immediately.”).

¹²⁷ *Id.* at 1094.

¹²⁸ *See id.* (“Yates never read the prospectus in full and failed to tell Powell that the investment involved a high degree of risk; [and] Powell . . . testified that Yates promised him a guaranteed return of eight percent per annum, and that the investment could be cashed in at any time with a small discount.”).

¹²⁹ *See, e.g., In re Stewart*, No. 97-05-59, 1998 Miss. Sec. LEXIS 3 (Aug. 27,

Business Services Division found that Boston Acceptance Corporation d/b/a First Lenders Indemnity Company (FLIC) and its principals, Boston and Cunningham, made a number of material misrepresentations and omissions in connection with their efforts to solicit Mississippi investors to purchase promissory notes, including, but not limited to: (1) failing to disclose that Boston had been previously convicted of bank fraud; (2) failing to disclose that FLIC was subject to a cease and desist order issued by the state of Missouri for selling the same notes FLIC was selling in Mississippi; (3) failing to disclose that the SEC had secured a permanent injunction against FLIC, Boston, and Cunningham, who also agreed to pay \$85,000 in civil penalties for violations of federal securities law; (4) failing to disclose that any sale of the promissory notes would violate the aforementioned injunction; and (5) misrepresenting that the promissory notes were exempt from registration under both Mississippi and federal law.¹³⁰

In *In re J. F. (Jim) Straw d/b/a American Business Club*,¹³¹ the Securities Division found that the offerors made several material misrepresentations in connection with their offer of securities in the form of agreement or contract under which the offeree agreed to pay periodically small amounts of money in order to receive a larger, interest-free loan at some future date to be determined by the offeror, which the offeree was obligated to repay. Specifically, the offerors misrepresented

1998); *In re Crites*, No. 97-05-50, 1998 Miss. Sec. LEXIS 2 (June 18, 1998); *In re Dennis*, No. 97-05-58, 1998 Miss. Sec. LEXIS 45 (June 18, 1998); *In re Minga*, No. 97-05-49, 1998 Miss. Sec. LEXIS 1 (June 18, 1998).

These and other actions were brought against individual agents for, *inter alia*, selling unregistered securities in Mississippi. None of the enforcement orders against the individual agents finds that any of them made material misrepresentations or omissions.

¹³⁰ *In re Boston Acceptance Corp.*, No. 97-05-45, 1997 Miss. Sec. LEXIS 7, at *3-4 (Aug. 15, 1997). In addition to these material misrepresentations and omissions, which the Division found to be violations of section 501 of the MSA, MISS. CODE ANN. § 75-71-501 (2000); see *Boston Acceptance*, 1997 Miss. Sec. LEXIS 7, at *8. The Division also found that FLIC, Boston and Cunningham violated section 115 of the MSA, MISS. CODE ANN. § 75-71-115, by filing documents with the Secretary of State's office that contained "misleading statements and material falsehoods," *Boston Acceptance*, 1997 Miss. Sec. LEXIS 7, at *4.

¹³¹ No. 92-04-08, 1992 Miss. Sec. LEXIS 17 (Apr. 17, 1992).

that: (1) the funds from which the offerees' future payments would come were "guaranteed," (2) the interest-free loan was a "grant," (3) the interest-free loan was a "cash giveaway," (4) any payments made by the offerees to the offerors were "100% Deductible" for tax purposes, (5) an offeree could decrease her waiting time before receiving her interest-free loan by increasing her periodic payments to the offerors, and (6) the offerees were at no risk of losing the funds they invested with the offerors.¹³²

In *In re BMT Racing Stables*,¹³³ respondents were soliciting investments in thoroughbred race horses. The Securities Division found that the respondents (BMT) had materially misrepresented their ownership of horses stabled at a Lexington, Kentucky training center (BMT, in fact, did not own any horses stabled there) and their ability to provide videotapes of horses owned by BMT (there were no such tapes).¹³⁴ The Securities Division also found that including in the offering materials a photograph of a horse named "Oreo Jack" was misleading because it gave the false impression that "Oreo Jack" was one of the horses in which an investor could purchase an interest when, in fact, BMT was not offering any interests in "Oreo Jack."¹³⁵

The Mississippi Supreme Court has adopted the federal "bespeaks caution" doctrine to hold otherwise material misrepresentations immaterial as a matter of law if they are accompanied by sufficient "cautionary language."¹³⁶

The "Bespeaks Caution" doctrine applies when "optimistic projections are coupled with cautionary language—in particular, relevant specific facts or assumptions—affecting the reasonableness of the reliance on and the materiality of those projections." This means that offered documents must be read as a whole, and their statements must be read in context.¹³⁷

¹³² See *id.* at *3-4.

¹³³ No. CD-86-8-1, 1986 Miss. Sec. LEXIS 1 (Sep. 10, 1986).

¹³⁴ *BMT Racing Stables*, 1986 Miss. Sec. LEXIS, at *2.

¹³⁵ See *id.*

¹³⁶ See *Allyn v. Wortman*, 725 So. 2d 94, 103 (Miss. 1998) (citing *Moorhead v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 949 F.2d 243, 245-46 (8th Cir. 1991)).

¹³⁷ *Allyn*, 725 So. 2d at 103 (quoting *Rubinstein v. Collins*, 20 F.3d 160, 167

3. No Reliance Required

Unlike common law fraud,¹³⁸ negligent misrepresentation,¹³⁹ and Rule 10b-5,¹⁴⁰ section 717(a)(2) does not require

(5th Cir. 1994) (citation omitted)). In *Allyn*, the plaintiffs complained that the defendants misrepresented material facts in soliciting the plaintiffs' investments in a casino project. *Id.* at 97. The court found that the "bespeaks caution" doctrine insulated the defendants from liability:

[T]he PPM is replete with warnings and cautionary language regarding the casino venture. Furthermore, the PPM was targeted to a specific group of investors. The Investors were not targeted by the Defendants, did not buy the Preferred Stock through the issuance discussed in the PPM, and did not even purchase the same class of stock as described in the PPM. When considering the PPM, as a whole, it is clear that the warnings are sufficient as a matter of law.

Id. at 103. *But see id.* at 105 (McRae, J., dissenting) (arguing that whether "bespeaks caution" doctrine insulates defendant from liability must be determined on case-by-case basis by trier of fact, rather than as matter of law by court).

¹³⁸ To recover on a claim of common law fraud, a Mississippi plaintiff must plead and prove:

(1) a representation; (2) its falsity; (3) its materiality; (4) the speaker's knowledge of its falsity or ignorance of its truth; (5) the speaker's intent that the representation should be acted upon by the hearer and in the manner reasonably contemplated; (6) the hearer's ignorance of its falsity; (7) the hearer's reliance on the representation's truth; (8) the hearer's right to rely thereon; and (9) the hearer's consequent and proximate injury.

Levens v. Campbell, 733 So. 2d 753, 761-62 (Miss. 1999); *see Allen v. Mac Tools, Inc.*, 671 So. 2d 636, 642 (Miss. 1996); *Franklin v. Lovitt Equip. Co.*, 420 So. 2d 1370, 1373 (Miss. 1982).

Absent justifiable reliance, a plaintiff's fraud claim will fail. *See, e.g., Franklin*, 420 So. 2d at 1373. That said, reliance does not require that the material misrepresentation or omission "be the predominating inducement to act. If the statement was false, was a material factor inducing a third person to act in reliance to his detriment, and if reliance by the third person was reasonably foreseeable to the speaker or author of the statement, then the speaker or author is liable for damage proximately caused thereby." *Felts v. Nat'l. Account Sys. Ass'n*, 469 F. Supp. 54, 67 (N.D. Miss. 1978) (citing *H. D. Sojourner & Co. v. Joseph*, 191 So. 418, 421-22 (Miss. 1939)).

In *Geisenberger v. John Hancock Distributors, Inc.*, 774 F. Supp. 1045 (S.D. Miss. 1991), the court found that the plaintiff justifiably relied on the defendants' representations, notwithstanding contrary information in the prospectus, "because of the difficulty that a relatively unsophisticated investor would have in comprehending the nature of an investment about which even [the defendant] stockbroker is confused." *Geisenberger*, 774 F. Supp. at 1052.

¹³⁹ To recover on a claim of negligent misrepresentation, a Mississippi plaintiff

that the buyer prove reliance on the seller's misrepresentation or omission.¹⁴¹ That is to say, section 717(a)(2) does not re-

must plead and prove:

- (1) a misrepresentation or omission of a fact; (2) that the representation [or omission] is material or significant; (3) failure to exercise reasonable care on the part of the defendant; (4) reasonable reliance on the misrepresentation or omission; and (5) damages as a direct result of such reasonable reliance.

Levens, 733 So. 2d at 762. Absent justifiable reliance, a plaintiff's negligent misrepresentation claim will fail. *See, e.g., Arnona v. Smith*, 749 So. 2d 63, 67 (Miss. 1999).

¹⁴⁰ The elements of a cause of action under section 10(b) of the 1934 Act and Rule 10b-5 are: (1) a misrepresentation or omission (2) of a material fact, (3) made knowingly or without knowledge of the truth thereof (4) by a person who owes the plaintiff a duty to disclose, (5) on which the plaintiff relied, (6) resulting in damage to the plaintiff. *See TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449-50 (1976); *Paracor Fin., Inc. v. Gen. Elec. Capital Corp.*, 96 F.3d 1151, 1157 (9th Cir. 1996). However, where a plaintiff alleges a fraudulent omission, "positive proof of reliance is not a prerequisite to recovery." *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 153-54 (1972); *accord Burke v. Jacoby*, 981 F.2d 1372, 1379 (2d Cir. 1992). "All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision." *Affiliated Ute Citizens*, 406 U.S. at 153-54.

For a detailed discussion of the elements of and principal defenses to liability under section 10(b) of the 1934 Securities Exchange Act and Rule 10b-5 promulgated thereunder, which is the principal avenue available to private litigants under federal securities law, see Keith A. Rowley, *Cause of Action for Securities Fraud Under Section 10(b) of the 1934 Securities Exchange Act and/or Rule 10b-5*, in 9 CAUSES OF ACTION 2D 271 (1997).

¹⁴¹ *See MISS. CODE ANN. § 75-71-717(a)(2)* (2000); *supra* text accompanying note 110. *But see Geisenberger*, 774 F. Supp. at 1051 (finding that section 717(a)(2) "contain[s] an implicit requirement of reasonable reliance consistent with federal Rule 10b-5"), *declined to follow on other grounds by Allyn*, 725 So. 2d at 94. While *Allyn* only specifically disagreed with *Geisenberger's* conclusion that section 501 of the MSA gives rise to an implied private right of action, compare *Geisenberger*, 774 F. Supp. at 1049 with *Allyn*, 725 So. 2d at 102. *Geisenberger* appears to make a number of errors in its assessment of the MSA, owing to the district judge's dogged attempt to analogize section 717(a)(2) to Rule 10b-5, rather than to section 12(a)(2), with which section 717(a)(2) has much more in common. *See supra* note 110. Consequently, the *Geisenberger* court erroneously imported the Rule 10b-5 "loss causation" element into his section 717(a)(2) analysis. *See Geisenberger*, 774 F. Supp. at 1051. Fortunately, while Judge Barbour appears to have been doctrinally wrong in implying reliance and loss causation elements into a section 717(a)(2) claim, he found sufficient facts in the case at bar to satisfy both putative elements. *See id.* As a net result, his holding was the same as it should have been absent the two misplaced elements.

A plaintiff suing under section 12(a)(2) of the 1933 Act need not prove reli-

quire that the plaintiff show that she would not have purchased the stock if she had known of the alleged adverse material facts.

4. *No Scierter Required*

Nor does the section 717(a)(2) require the buyer to prove that the seller knew the representation was false or made it without regard to its truth or falsity with the intent that the buyer rely upon it¹⁴²—as is required to show common law

ance. A section 12(a)(2) plaintiff is only required to prove (1) an offer or sale of a security, (2) by the use of any means of interstate commerce, (3) through a prospectus or oral communication (4) which includes an untrue statement of material fact or omits to state a material fact, (5) that plaintiff did not know to be false. See 15 U.S.C. § 77l(a)(2) (Supp. V 1999); *Cook v. Avien, Inc.*, 573 F.2d 685, 693 (1st Cir. 1978); *Gridley v. Sayre & Fisher Co.*, 409 F. Supp. 1266, 1272-73 (D.S.D. 1976); *Thiele v. Shields*, 131 F. Supp. 416, 419 (S.D.N.Y. 1955). Reliance is not an element of a section 12(a)(2) claim. See *Metromedia Co. v. Fugazy*, 983 F.2d 350, 361 (2d Cir. 1992); *Sanders v. John Nuveen & Co.*, 619 F.2d 1222, 1225 (7th Cir. 1980). Indeed, some courts have gone so far as to hold that a section 12(a)(2) plaintiff need not have *read* the allegedly misleading prospectus prior to purchasing the securities in question. See *Caviness v. DeRand Res. Corp.*, 983 F.2d 1295, 1305 (4th Cir. 1993). Indeed, some courts have held that a section 12(a)(2) plaintiff need not have *received* the prospectus prior to purchase. See *In re TCW/DW N. Am. Gov't Income Trust Sec. Litig.*, 941 F. Supp. 326, 337 (S.D.N.Y. 1996); *Klein v. Computer Devices, Inc.*, 591 F. Supp. 270, 277 (S.D.N.Y. 1984).

For a detailed discussion of the elements of and principal defenses to liability under section 12(a)(2), see Keith A. Rowley, *Cause of Action for Securities Fraud Under Section 12(2) of the 1933 Securities Act*, in 11 CAUSES OF ACTION 2D 1 (1998).

¹⁴² See *supra* note 110; see e.g., *Fortenberry v. Foxworth Corp.*, 825 F. Supp. 1265, 1279 (S.D. Miss. 1993).

fraud¹⁴³ or a Rule 10b-5 violation.¹⁴⁴ Rather, as is the case with section 12(a)(2),¹⁴⁵ the seller's lack of scienter is an affirmative defense to a section 717(a)(2) claim.¹⁴⁶

5. No "Duty" Required

Furthermore, section 717(a)(2) does not require that the seller owe the purchaser any duty to disclose in order for an omission of material fact to be actionable, but rather implies such a duty in every securities offering or sale.¹⁴⁷

¹⁴³ See *supra* note 138; see, e.g., *Russell v. S. Nat'l Foods, Inc.*, 754 So. 2d 1246, 1256 (Miss. 2000) (requiring "an affirmative intent to deceive").

In order to establish the requisite intent to deceive, a plaintiff must establish that the defendant made a statement (1) with actual knowledge of its falsity; (2) recklessly without knowledge or disregard of either truth or falsity; or (3) under circumstances which indicate that the speaker should have known it was false, irrespective of whether or not he actually knew it was false. *Felts v. Nat'l Account Sys. Ass'n*, 469 F. Supp. 54, 67 (N.D. Miss. 1978) (citing *H. D. Sojourner & Co. v. Joseph*, 191 So. 418, 421 (Miss. 1939)).

Common law negligent misrepresentation does not require proof of scienter because, if scienter were present, the defendant's actions would be fraudulent, not negligent.

¹⁴⁴ See *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976); *supra* note 140.

¹⁴⁵ See *supra* note 141.

¹⁴⁶ See *infra* Part II.C.6.c.ii.

¹⁴⁷ By contrast,

Rule 10b-5 is violated by nondisclosure only when there is a duty to disclose. The parties to an impersonal market transaction owe no duty of disclosure to one another absent a fiduciary or agency relationship, prior dealings, or circumstances such that one party has placed trust and confidence in the other. A number of factors are used to determine whether a party has a duty to disclose: (1) the relationship of the parties, (2) their relative access to information, (3) the benefit that the defendant derives from the relationship, (4) the defendant's awareness that the plaintiff was relying upon the relationship in making his investment decision, and (5) the defendant's activity in initiating the transaction.

Paracor Fin., Inc. v. Gen. Elec. Capital Corp., 96 F.3d 1151, 1157 (9th Cir. 1996) (quotations and citations omitted).

6. Defenses to Primary Securities Fraud Liability¹⁴⁸

a. Standing

Section 717(a)(2)'s protection, like that of section 717(a)(1)¹⁴⁹ and section 12(a)(2),¹⁵⁰ extends only to buyers. Persons who did not buy the security thus lack standing to sue the person who sold it.¹⁵¹

b. Limitations

A plaintiff must bring a section 717(a)(2) claim within two years of the date on which the plaintiff knew, or should have known through the exercise of reasonable diligence, of the existence of her claim.¹⁵² The question of when a plaintiff dis-

¹⁴⁸ In addition to the statutory defenses discussed here, one or more common law affirmative defenses might be available to a section 717(a)(2) defendant. See generally Charles G. Stinner, Note, *Estoppel and In Pari Delicto Defenses to Civil Blue Sky Law Actions*, 73 CORNELL L. REV. 448 (1988) (discussing viability of estoppel and *in pari delicto* defenses under state blue sky laws).

¹⁴⁹ See *supra* Part II.B.4.a.

¹⁵⁰ See, e.g., *Ratner v. Sioux Natural Gas Corp.*, 770 F.2d 512, 517 (5th Cir. 1985) (holding that non-purchasers lack standing to sue under section 12(a)(2)).

¹⁵¹ See *supra* note 102.

By contrast, sellers can sue both under section 10(b) and/or Rule 10b-5, see, e.g., *Fortenberry v. Foxworth Corp.*, 825 F. Supp. 1265, 1279 (S.D. Miss. 1993); see also, e.g., *Am. Gen. Ins. Co. v. Equitable Gen. Corp.*, 493 F. Supp. 721, 744-47 (E.D. Va. 1980); *Rude v. Cambell Square, Inc.*, 411 F. Supp. 1040, 1049-50 (D.S.D. 1976), and at common law, see, e.g., *Fortenberry*, 825 F. Supp. at 1279.

¹⁵² MISS. CODE ANN. §§ 75-71-725 (2000); see, e.g., *Holland v. Mayfield*, No. 96-CA-01169-SCT, 1999 WL 353023, at *9 (Miss. June 3, 1999).

By comparison, claims under section 12(a)(2) of the 1933 Securities Act, section 10(b) of the 1934 Securities Exchange Act, or Rule 10b-5 must be brought no more than three years after the cause of action accrued, but in any case within one year of the date on which plaintiff discovered, or in the exercise of reasonable diligence should have discovered, the existence of her claim. See 15 U.S.C. § 77m (Supp. V 1999) (limitations for section 12(a)(2) claim); *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*, 501 U.S. 350, 364 (1991) (limitations for section 10(b) or Rule 10b-5 claim).

The statute of limitations for common law fraud claims runs for three years from the date the plaintiff's cause of action accrued. See MISS. CODE ANN. § 15-1-49(1) (1995 & Supp. 2000); see, e.g., *Holland*, 1999 WL 35023, at *8. Claims of negligent misrepresentation are also subject to a three-year limitations period. See MISS. CODE ANN. § 15-1-49(1); see, e.g., *Air Comfort Sys., Inc. v. Honeywell, Inc.*, 760 So. 2d 43, 47 (Miss. Ct. App. 2000). Limitations for fraud and negligent mis-

covered or, through reasonably diligent inquiry should have discovered, facts sufficient to trigger the two-year limitations period is generally a question of fact.¹⁵³

representation, unlike limitations under section 725, do not appear to be tolled until the plaintiff discovers, or through the exercise of reasonable diligence should have discovered, her injury. See MISS. CODE ANN. § 15-1-49(2) (tolling limitations until discovery only in cases involving latent injury and disease). However,

[i]f a person liable [for fraud or negligent misrepresentation] shall fraudulently conceal the cause of action from the knowledge of the person entitled thereto, the cause of action shall be deemed to have first accrued at, and not before, the time at which such fraud shall be, or with reasonable diligence might have been, first known or discovered [by the plaintiff].

Id. § 15-1-67; see, e.g., *Smith v. Franklin Custodian Funds, Inc.*, 726 So. 2d 144, 147 (Miss. 1998). Fraudulent concealment will toll limitations against a defendant as long as the fraud was committed by the defendant or someone in privity with the defendant. See *Smith*, 726 So. 2d at 147.

¹⁵³ See, e.g., *Stewart v. Germany*, 631 F. Supp. 236, 247-48 (S.D. Miss. 1986) (applying section 725).

In *Holland*, the Mississippi Supreme Court found that the plaintiffs timely filed their complaint on April 10, 1993, despite the defendant's argument that one or more plaintiff(s) knew or should have known of the alleged fraud more than two years before filing suit. *Holland*, 1999 WL 35023, at *8.

Holland contends that the Investors are barred because one of the Investors, Ward, testified that he had suspicions that there had been front-end profits paid as early as February of 1990 when he went to Houston to try and audit the books of BT. At that time, he discovered that a check for \$32,000 had been written to a Laurel law firm. Holland also points to the testimony of another Investor, Ferguson, who testified that he may have known about Holland getting a front-end profit in 1990.

The record in this case contradicts Holland's assertions as to when the Investors discovered that Holland had received a front-end profit on the Chandeleur Prospect. First, in his testimony concerning the \$32,000 check, Ward did not state that he knew that the check was paid on behalf of Holland. Ward went on to testify that he asked Holland the day of the discovery of the check if Holland knew of any reason that that check would have been paid to a Laurel law firm, and Holland responded that he did not.

Further, a reading of Ferguson's testimony shows that he was unsure of when or from whom he received the information that Holland had received a front-end commission. It was only when he was pressed by Holland's attorney to give a specific year, that Ferguson reluctantly said, "1990." He then qualified his statement by testifying that, "a lot of things escape me now, and please understand that this is true. I just can't remember a lot of things after my open heart surgery."

The other Investors testified that they first discovered that front-end commissions had been paid to Holland, the Evanses, and Gaskin, from a

In *Seaboard Planning Corp. v. Powell*,¹⁵⁴ decided under the precursor to section 725,¹⁵⁵ the defendants argued that limitations began to run when the plaintiffs (the Powells) received the prospectus, a careful reading of which might have disclosed the misrepresentations made previously by defendant Yates.¹⁵⁶ The Powells argued that limitations did not begin to run until ten months later, when they did not receive the dividend check they had been promised.¹⁵⁷ The trial court and the Mississippi Supreme Court agreed with the Powells:

To start the running of [limitations], there must be not only fraud but some event to put the Powells on notice. Here the Powells' lack of education was a factor in the success of the fraud. At the time the fraud was perpetrated upon the uneducated Powells, it cannot logically be held that they as reasonable persons should have known of the fraud from the very instant they fell for Yates' misrepresentations. The first indication that things were not as Yates had made them out to be was the receipt in October of \$200 for the third quarter of 1974, which would place the filing of suit well within the statute. We think the evidence establishes that Yates knew or should have known that even if the Powells undertook to peruse the prospectus they would not be able to comprehend its contents. The very nature of fraud is such that it cannot be discovered until sometime after the fraudulent act is committed. Here, the Powells had no reason to suspect Yates or distrust his representations until such time as they were put on notice by the smaller payments or the absence of payments. On these facts, we hold that the statute did not begin to run until the Powells received the check for the third quar-

deposition taken from one of the BT principals in the Texas case on January 2, 1992. The Investors' Complaint was filed on April 10, 1993, well within the statute of limitation.

Id.

¹⁵⁴ 364 So. 2d 1091 (Miss. 1978).

¹⁵⁵ Former section 75-71-31 of the Mississippi Code afforded a plaintiff two years within which to sue after she, "by the exercise of ordinary care, should have discovered that such sale was made . . . upon misrepresentation." MISS. CODE ANN. § 75-71-31 (1972), *repealed by* 1981 Miss. Laws, ch. 521, § 418.

¹⁵⁶ *See Powell*, 364 So. 2d at 1094.

¹⁵⁷ *See id.*

ter of 1974. Accordingly, the suit, filed less than two years afterward, was not barred by the statute.¹⁵⁸

c. Other Statutory Defenses

Unlike a section 717(a)(1) defendant, whose only statutory defenses are standing¹⁵⁹ and limitations,¹⁶⁰ section 717(a)(2) defendants have two additional statutory defenses.

i. Plaintiffs Actual Knowledge

First, a defendant is not liable under section 717(a)(2) if he can prove that the plaintiff actually knew of the untruth or omission.¹⁶¹ The burden is on the defendant to prove the

¹⁵⁸ *Id.* at 1094-95.

¹⁵⁹ *See supra* Part II.B.3.a.

¹⁶⁰ *See supra* Part II.B.3.b.

¹⁶¹ *See* MISS. CODE ANN. § 75-71-717(a)(2) (2000) (“Any person who . . . offers or sells a security by the use of . . . any untrue statement of a material fact or any omission to state a material fact . . . (the buyer not knowing of the untruth or omission) . . . is liable to the person buying the security from him . . .”).

A section 12(a)(2) plaintiff who actually knows of the defendant’s alleged fraud may be precluded from recovering damages allegedly caused by that fraud. *See* 15 U.S.C. § 77l(a)(2) (Supp. V 1999); *Haralson v. E.F. Hutton Group, Inc.*, 919 F.2d 1014, 1032 (5th Cir. 1990); *Mayer v. Oil Field Sys. Corp.*, 803 F.2d 749, 755 (2d Cir. 1986); *accord* *Wright v. Nat’l Warranty Co.*, 953 F.2d 256, 262 (6th Cir. 1992); *In re TCW/DW N. Am. Gov’t Income Trust Sec. Litig.*, 941 F. Supp. 326, 337 (S.D.N.Y. 1996). The burden of pleading and proving her lack of actual knowledge rests on the section 12(a)(2) plaintiff. *See, e.g.*, *Junker v. Crory*, 650 F.2d 1349, 1359 (5th Cir. 1981); *Gilbert v. Nixon*, 429 F.2d 348, 356 (10th Cir. 1970); *In re Gap Stores Sec. Litig.*, 79 F.R.D. 283, 306 (N.D. Cal. 1978). It is less clear whether the plaintiff’s actual knowledge of the defendant’s fraud precludes her from recovering under section 10(b) and Rule 10b-5. *Compare, e.g.*, *Ray v. Karris*, 780 F.2d 636, 643 (7th Cir. 1985) (holding that plaintiffs were unable to maintain derivative action under Rule 10b-5 where they knew “at least the essential facts” of defendants’ fraudulent scheme before scheme was consummated), *Cent. Microfilm Serv. Corp. v. Basic/Four Corp.*, 688 F.2d 1206, 1219 (8th Cir. 1982) (arguing simple logic dictates that actual knowledge of fact allegedly omitted defeats fraud claim based upon that omission, *and* *Horowitz v. Pownall*, 105 F.R.D. 615, 621 (D. Md. 1985) (quoting *Central Microfilm* with approval), *affd sub nom.* *Zimmerman v. Bell*, 800 F.2d 386 (4th Cir. 1986), *with*, *Travis v. Anthes Imperial Ltd.*, 473 F.2d 515, 521-23 (8th Cir. 1973) (finding that fact that sale of securities took place when plaintiffs were aware of all facts, including defendants’ misrepresentations, was not fatal to plaintiffs’ section 10(b) claim where defendants’ misrepresentations allegedly induced plaintiffs to retain their stock

plaintiff's actual knowledge, rather than on the plaintiff to prove his lack of knowledge or his diligence in seeking to determine the truthfulness of the defendant's misrepresentation or omission. The MSA imposes no duty of inquiry on the plaintiff.¹⁶²

ii. Defendant's Lack of Knowledge

Second, section 717(a)(2) excuses a defendant from liability for a material misrepresentation or omission if the defendant

until, by reason of de facto merger, defendants controlled relevant market and could dictate price of their stock); *Kohn v. Am. Metal Climax, Inc.*, 458 F.2d 255, 269 (3d Cir. 1972) ("[I]t is [not] a defense to a finding of material violations of 10b-5 to say that some stockholders 'discovered' the misrepresentations . . . and thus were not misled . . ."); *Stewart v. Bennett*, 359 F. Supp. 878, 881 n.9 (D. Mass. 1973) (stating that section 10(b) affords no defense on ground of either plaintiffs' knowledge), *supplemented on other grounds*, 362 F. Supp. 605 (D. Mass. 1973).

The plaintiff's ignorance of the falsity of the defendant's misrepresentation is an element of common law fraud. *See supra* note 138. Because it is an element of the claim, the plaintiff bears the burden of pleading and proving her lack of knowledge.

¹⁶² Similarly, section 12(a)(2) imposes no duty of inquiry on the plaintiff. *See Wright*, 953 F.2d at 262.

Indeed, a purchaser who is actually ignorant that a seller's representation is inaccurate or incomplete may recover even though the full truth is apparent from materials in her possession. The concept of a plaintiff's constructive knowledge has no place in section 12(2) actions.

Haralson, 919 F.2d at 1032 n.10 (citation omitted).

Authorities are split on the availability of a due diligence defense to liability under section 10(b) and Rule 10b-5. *Compare, e.g., Warren v. Reserve Fund, Inc.*, 728 F.2d 741, 747 (5th Cir. 1984); *Edwards & Hanly v. Wells Fargo Sec. Clearance Corp.*, 602 F.2d 478, 485-86 (2d Cir. 1979), *Straub v. Vaisman & Co.*, 540 F.2d 591, 597-98 (3d Cir. 1976), *Weir v. Merrill Lynch Pierce Fenner & Smith, Inc.*, 586 F. Supp. 63, 65 (S.D. Fla. 1984) (all recognizing some form of "due diligence" defense), *with, Sundstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1048 (7th Cir. 1977); *Holdsworth v. Strong*, 545 F.2d 687, 694 (10th Cir. 1976) (both holding that plaintiff's diligence is irrelevant and/or that there is no "due diligence" defense). Once the defendant raises the plaintiff's diligence as a defense to section 10(b)/Rule 10b-5 liability, the plaintiff bears the burden of negating her own recklessness. *See, e.g., Royal Am. Managers, Inc. v. IRC Holding Corp.*, 885 F.2d 1011, 1015-16 (2d Cir. 1989). Mere negligence on the plaintiff's part will not defeat the defendant's liability. *See Citizens & S. Sec. Corp. v. Braden*, 733 F. Supp. 655, 666 (S.D.N.Y. 1990). In order to defeat a due diligence defense, the plaintiff need only prove that she acted "reasonably" in the underlying transaction. *See Straub*, 540 F.2d at 598.

can show that he did not, and could not by the exercise of reasonable care, know of the untruth or omission.¹⁶³ The burden is on the defendant to prove his own reasonable diligence and lack of actual knowledge, rather than on the plaintiff to prove the defendant's actual knowledge or lack of diligence.

D. Statutory Secondary Liability

The MSA's reach is not limited to only those persons who actually sold unregistered securities or who offered or sold securities by means of a material misrepresentation or omission. Section 719 holds certain indirect sellers jointly and severally liable for a direct seller's violation of section 717.¹⁶⁴

¹⁶³ See MISS. CODE ANN. § 75-71-717(a)(2) ("Any person who . . . offers or sells a security by the use of . . . any untrue statement of a material fact or any omission to state a material fact . . . , and who does not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the untruth or omission, is liable to the person buying the security from him").

Section 12(a)(2) excuses from liability any defendant who "sustain[s] the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission." 15 U.S.C. § 77l(a)(2); see, e.g., *Ambrosino v. Rodman & Renshaw, Inc.*, 972 F.2d 776, 787-88 (7th Cir. 1992); *Alton Box Bd. Co. v. Goldman, Sachs & Co.*, 560 F.2d 916, 918 (8th Cir. 1977). A section 10(b)/Rule 10b-5 defendant can avoid liability by proving, by a preponderance of the evidence, that any misrepresentation or omission he made was not made knowingly, intentionally, with the intent to defraud or with reckless disregard for its truth or falsity. See, e.g., *In re Worlds of Wonder Sec. Litig.*, 814 F. Supp. 850, 870 (N.D. Cal. 1993), *aff'd in part, rev'd in part on other grounds*, 35 F.3d 1407 (9th Cir. 1994); *Koehler v. Pulvers*, 614 F. Supp. 829, 848 (S.D. Cal. 1985); *Pachter v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 444 F. Supp. 417, 422 (E.D.N.Y.), *aff'd*, 594 F.2d 852 (2d Cir. 1978).

¹⁶⁴ MISS. CODE ANN. § 75-71-719.

Every person who directly or indirectly controls a seller liable under section 75-71-717, every partner, officer or director of such a seller, every person occupying a similar status or performing similar functions, every employee of such a seller who materially aids in the sale, and every broker-dealer who materially aids in the sale [is] also liable jointly and severally with and to the same extent as the seller

Id. For purposes of the MSA, "officer" means

a president, vice president, secretary, treasurer or principal financial officer, comptroller or principal accounting officer, and any other persons performing similar functions with respect to any organization whether incorporated or unincorporated. A person shall not be deemed an officer merely because he is titled as such if he does not perform the legal func-

A purchaser seeking to establish secondary liability for a registration violation under section 719 need not prove that the indirect seller knew that the law required the security to be registered. The indirect seller's lack of knowledge is an affirmative defense that she must plead and prove.¹⁶⁵ A person who sells securities in concert with another person may be liable both as a primary violator and as a collateral participant.¹⁶⁶

As a general rule, a plaintiff may sue a jointly and severally liable collateral participant without also suing the jointly and severally liable primary violator.¹⁶⁷

1. Liability for "Controlling" a Primary Violator

Section 719 holds "[e]very person who directly or indirectly controls a seller liable under [s]ection 75-71-717, every partner, officer or director of such a seller, [and] every person occupying a similar status or performing similar functions . . . jointly and

tion of an officer.

Rule 103(L), Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,403, at 29,402-03 (1998).

¹⁶⁵ See *supra* Part II.R.3.d.

¹⁶⁶ See, e.g., *First Mobile Home Corp. v. Little*, 298 So. 2d 676, 681 (Miss. 1974).

¹⁶⁷ See generally *Hall v. Hilbun*, 466 So. 2d 856, 879 (Miss. 1985) ("[J]oint tortfeasors are jointly and severally liable to the plaintiff who, at his election, may sue fewer than all and recover full damages from those sued."). The same is true under analogous federal law. See, e.g., *SEC v. Savoy Indus., Inc.*, 587 F.2d 1149, 1170 n.47 (D.C. Cir. 1978) (reciting that, in action against control person, "the plaintiff need not proceed against the principal perpetrator, nor need the principal perpetrator be identified in the complaint"); *Kemmerer v. Weaver*, 445 F.2d 76, 78-79 (7th Cir. 1971) (holding that action against controlling persons may continue despite dismissal of suit against primary violator); *Keys v. Wolfe*, 540 F. Supp. 1054, 1062 (N.D. Tex. 1982) ("Nothing in the language of section 20(a) compels the presence of the controlled person whose misdeeds are sought to be attributed to the defendants charged to be controlling persons, and nothing in familiar and conceptually related attribution principles such as conspiracy membership, agency, or aider and abettor, demands a visiting of actual liability upon an active wrongdoer as a condition to an attribution of that liability."), *rev'd on other grounds*, 709 F.2d 413 (5th Cir. 1983); see also Ernest L. Folk, III, *Civil Liabilities Under the Federal Securities Acts: The BarChris Case (Part II)*, 55 VA. L. REV. 199, 217-18 (1969) (analogizing control person liability under 1933 Act to common law of master and servant and pointing out that, at common law, "[a] master answers vicariously for a servant's wrong, not for his adjudicated liability").

severally [liable] with and to the same extent as the seller."¹⁶⁸ "Control," in turn, means "the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise."¹⁶⁹ The power to control, whether or not the power is exercised, is the key.

The MSA's control person liability provisions parallel both section 15 of the 1933 Securities Act¹⁷⁰ and section 20(a) of the 1934 Securities Exchange Act,¹⁷¹ and may be interpreted

¹⁶⁸ MISS. CODE ANN. § 75-71-719; *see, e.g.*, *Felts v. Nat'l Account Sys. Ass'n*, 469 F. Supp. 54, 67-68 (N.D. Miss. 1978) (applying former Mississippi Securities Law, MISS. CODE ANN. § 75-71-1 *et seq.* (1972), *repealed by* 1981 Miss. Laws, ch. 521, § 418, to hold issuing corporation's past and current presidents, its vice-president and its treasurer liable as control person).

¹⁶⁹ Rule 103(F), Miss. Blue Sky Regs., reprinted in 2A BLUE SKY L. REP. (CCH) ¶ 34,403, at 29,401 (1998).

Rule 103(F) is an almost verbatim copy of SEC Rule 405(f). *See* 17 C.F.R. § 230.405 (2000) (defining "control" for purposes of federal securities law). For an excellent discussion of control person liability under federal securities law, discussing, *inter alia*, the likely outcome of a control-person analysis under a number of sample fact patterns, see Loftus C. Carson, II, *The Liability of Controlling Persons Under the Federal Securities Acts*, 72 NOTRE DAME L. REV. 263 (1997).

¹⁷⁰ Section 15 provides:

Every person who, by or through stock ownership, agency, or otherwise, . . . controls any person liable under section . . . 77l of this title, shall also be liable jointly and severally with and to the same extent as such controlled person is liable, unless the controlling person had no knowledge of or reasonable ground to believe in the existence of the facts by reason of which the liability of the controlled person is alleged to exist.

15 U.S.C. § 77o (1994).

¹⁷¹ Section 20(a) provides:

Every person who, directly or indirectly, controls any person liable under any provision of this chapter or any rule or regulation thereunder shall also be liable jointly and severally with and to the same extent as such controlled person to any person to whom such controlled person is liable, unless the controlling person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.

Id. § 78t(a). Section 15 of the 1933 Act and section 20(a) of the 1934 Act, despite somewhat different wording, are analogous provisions that should be interpreted similarly. *See, e.g.*, *Pharo v. Smith*, 621 F.2d 656, 673-74 (5th Cir.), *modified on other grounds*, 625 F.2d 1226 (5th Cir. 1980); *Felts*, 469 F. Supp. at 66.

In the wake of the Private Securities Litigation Reform Act, *see supra* note 2, joint and several liability for control persons under federal law may now be avail-

and applied accordingly.

The plaintiff bears the burden of establishing control. As a general rule, a plaintiff should plead and prove that the defendant (1) exercised active control over the day-to-day affairs of the controlled person or entity and (2) had the power to control and influence the particular transactions that gave rise to the underlying securities violations.¹⁷²

The MSA does not require the plaintiff to prove that the control person acted with knowledge of the underlying violation or with reckless disregard for the truthfulness of the primary violator's acts or omissions;¹⁷³ rather, the control person's lack of scienter is an affirmative defense to a section 719 claim.¹⁷⁴ If the plaintiff can prove that the controlled person violated section 717 and that the defendant was a "control person" under the statute, then judgment against the control person will be proper in the absence of a viable affirmative defense.¹⁷⁵

able only if the control person "knowingly committed a violation of the securities laws." Compare 15 U.S.C. § 78u-4(f)(2)(A) (Supp. V 1999), *with id.* §§ 77o, 78t(a). In the absence of a knowing violation, federal law may afford a plaintiff only proportionate liability against a control person. See Marc I. Steinberg & Christopher D. Olive, *Contribution and Proportionate Liability Under the Federal Securities Laws in Multidefendant Securities Litigation After the Private Securities Litigation Reform Act of 1995*, 50 SMU L. REV. 337, 349-50 (1996); Glen Shu, Comment, *Take a Second Look: Central Bank After the Private Securities Litigation Reform Act of 1995*, 33 HOUS. L. REV. 539, 569 (1996). If this proves to be the case, the MSA could now afford a Mississippi plaintiff greater relief than its federal progenitors.

¹⁷² See, e.g., *Abbott v. Equity Group, Inc.*, 2 F.3d 613, 620 (5th Cir. 1993); *Metge v. Baehler*, 762 F.2d 621, 631 (8th Cir. 1985). Thus, for example, in *G.A. Thompson & Co. v. Partridge*, 636 F.2d 945 (5th Cir. 1981), the Fifth Circuit found that a twenty-four percent (24%) shareholder, who was also an officer and director, and was involved in the day-to-day supervision of the types of activities that gave rise to the plaintiff's claims, was a "control person" under section 20 of the 1934 Act, 15 U.S.C. § 78t(a). See *G.A. Thompson & Co.*, 636 F.2d at 958. However, the court went on to note that "effective day-to-day control" may not be required. See *id.* at 958 n.24.

¹⁷³ See MISS. CODE ANN. § 75-71-719.

¹⁷⁴ See *infra* Part II.D.3.c.

¹⁷⁵ Under the prior Mississippi Securities Act, MISS. CODE ANN. § 75-71-1 *et seq.* (1972), *repealed by* 1981 Miss. Laws ch. 521, § 418, officers and directors were liable only if they participated in or induced the sale of an unregistered security or if they participated in the material misrepresentation or omission that induced the plaintiff to purchase the security. See, e.g., *First Mobile Home Corp. v. Little*, 298 So. 2d 676, 680 (Miss. 1974). See generally *Hodge, supra* note 1, at

2. Liability for "Materially Aiding" a Primary Violator

Section 719 also provides that every employee of a seller liable under section 75-71-717 of the Mississippi Code, as well as every broker-dealer or agent, who "materially aid[ed] in the sale" giving rise to the seller's liability, is "liable jointly and severally with and to the same extent as the seller."¹⁷⁶ A party materially aids a primary violator by, for example, preparing a document containing a material misrepresentation or omission.¹⁷⁷

The plaintiffs in *Felts v. National Account Systems Ass'n*¹⁷⁸ sued, *inter alia*, Peters, who was the attorney for the issuer (NASA), arguing that he was liable, in addition to those defendants who more directly dealt with the plaintiffs, due to his role in facilitating NASA's violations of state and federal securities law. The court held that

Peters owed a special duty of diligent investigation and disclosure. Not only was he the lawyer responsible for the issuer's compliance with applicable laws, he also permitted his name (and his office) to be exploited as "president" of NASA when he clearly knew the daily operation of NASA would be controlled by Steen. He permitted NASA to utilize his signature stamp and made no effort to determine how his signature was being used.

Peters and Steen jointly decided not to file a registration statement when a reasonable inquiry by Peters clearly would have revealed that no exemption was available for the sale of

622. As such, the prior law made no effective distinction between "control persons" and "material aiders" as does the current version of the MSA.

¹⁷⁶ MISS. CODE ANN. § 75-71-719 (2000); *see, e.g.*, *Felts v. Nat'l Account Sys. Ass'n*, 469 F. Supp. 54, 67 (N.D. Miss. 1978) (holding several secondary violators liable as "participants, aiders and abettors and co-conspirators").

¹⁷⁷ *See, e.g.*, *Felts*, 469 F. Supp. at 68. That said, merely "[t]yping, reproducing, [or] delivering sales documents," while those acts "may all be essential to a sale," should not give rise to liability for materially aiding a securities violation, because such acts "could be performed by anyone." *Prince v. Brydon*, 764 P.2d 1370, 1371 (Or. 1988) (construing similar provision of Oregon Securities Law, OR. REV. STAT. § 59.115(3) (1999)). "[I]t is a drafter's knowledge, judgment, and assertions reflected in the contents of the documents that are 'material' to the sale." *Id.*

¹⁷⁸ 469 F. Supp. 54 (N.D. Miss. 1978).

these securities. Peters failed to even attempt to determine the registration requirements of Mississippi law and, as a result, NASA initiated the sale of these securities in violation of law.

Peters, as lawyer for the issuer, secured an exemption based on promotional material furnished to him by Steen. He did not make a reasonable inquiry to ascertain the truth or falsity of the representations when these statements could have been readily verified by a lawyer. He secured the certificate of exemption without which these securities would not have been offered or sold when he knew or should have known that NASA was in violation of law, had issued no stock and had no paid-in capital. During the term of the offering, when Peters had ample opportunity to detect the misrepresentations, he failed to report violations to NASA, to the Secretary of State or to the Securities & Exchange Commission.

. . . [W]ithout the active, affirmative assistance of Peters as lawyer for the issuer, including the use and exploitation of his name, the sale would not have been accomplished. Therefore, under applicable law, Peters . . . is jointly liable with the issuer for all damages.¹⁷⁹

Neither the 1933 Act nor the 1934 Act contains a similar provision. As a consequence, the U.S. Supreme Court has held that no private cause of action exists for aiding and abetting a violation of section 10(b) and Rule 10b-5.¹⁸⁰ The Fifth Circuit

¹⁷⁹ *Id.* at 68.

¹⁸⁰ See *Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 191 (1994). See generally Steven A. Meetre, *Textualist Statutory Interpretation Kills Section 10(b) "Aiding and Abetting" Liability*, 63 DEF. COUNS. J. 58 (1996); Marc I. Steinberg, *The Ramifications of Recent U.S. Supreme Court Decisions on Federal and State Securities Regulation*, 70 NOTRE DAME L. REV. 489, 491-501 (1995) (chronicling Supreme Court's adherence to "strict statutory construction" in section 10(b) and Rule 10b-5 cases beginning, prominently, with *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976), and culminating in *Central Bank of Denver*).

For many years prior to *Central Bank of Denver*, "suits against aiders and abettors of violations under the federal securities laws had been the most widely used theory to hold nonprivity parties responsible for such violations." Lewis D. Lowenfels & Alan R. Bromberg, *A New Standard for Aiders and Abettors Under the Private Securities Litigation Reform Act of 1995*, 52 BUS. LAW. 1, 1 (1996). Indeed, "all 11 federal courts of appeals that had considered the question had

has followed suit.¹⁸¹ While it is true that Mississippi courts look to federal decisions for guidance on securities matters,¹⁸² because the *Central Bank of Denver* Court specifically found that no private aiding and abetting cause of action existed because the 1934 Act contained no language providing one,¹⁸³ and because the MSA does contain such language, a Mississippi court is not bound by *Central Bank*.

3. *Defenses to Statutory Secondary Liability*

Collateral participants have the same basic array of statutory defenses at their disposal as do primary violators, although the exact contours of the defenses may not be the same.

a. *Standing*

Only buyers can sue indirect sellers under section 719.¹⁸⁴

b. *Limitations*

As a general rule, claims against collateral participants in a section 717(a)(2) violation must be brought within two years of the date on which the plaintiff knew, or should have known through the exercise of reasonable diligence, of the existence of her claim.¹⁸⁵

c. *Defendant's Lack of Knowledge*

Section 719 provides a statutory defense for a secondary violator who pleads and proves that she did not know, and in the exercise of reasonable care could not have known, of the

already determined that aiders and abettors could be liable under section 10(b).” Bettina M. Lawton & Catherine Botticelli, *New Weapon in the SEC's Arsenal: Secondary Liability After Central Bank*, BUS. LAW TODAY, July/Aug. 1995, at 34; see also Steinberg, *supra*, at 489 (observing that *Central Bank of Denver* decision “swept away decades of lower court precedent that nearly universally recognized the propriety of” aiding and abetting liability under both section 10(b) and Rule 10b-5).

¹⁸¹ See, e.g., *Melder v. Morris*, 27 F.3d 1097, 1104 n.9 (5th Cir. 1994).

¹⁸² See *supra* note 2 and accompanying text.

¹⁸³ See *Central Bank*, 511 U.S. at 191.

¹⁸⁴ See *supra* note 102.

¹⁸⁵ MISS. CODE ANN. § 75-71-725 (2000).

facts on which her liability is based.¹⁸⁶ The burden is on the defendant to prove her own reasonable diligence and lack of actual knowledge. It is neither necessary nor sufficient for the secondary violator to prove that she did not know that the sale or purchase was illegal; the key is whether she knew or should have known the *facts* that made the sale or purchase illegal.

In addition, while not truly a defense, an indirect seller found liable under section 719 has the right to contribution from anyone else who is jointly and severally liable with the indirect seller.¹⁸⁷

d. Plaintiff's Actual Knowledge

Presumably, the defense afforded a primary violator by section 717(a)(2) who can prove that the plaintiff knew of the untruth or omission¹⁸⁸ is also available to a person being sued as secondarily liable for a primary violation of one of those provisions. However, section 719 does not explicitly mention the plaintiff's knowledge or lack thereof, and there are no published opinions on point.

Federal law, to which Mississippi courts look for guidance in interpreting and applying the MSA,¹⁸⁹ permits a control person—one class of persons covered by section 719—to avoid liability by proving that she “acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.”¹⁹⁰

¹⁸⁶ MISS. CODE ANN. § 75-71-719. Federal law similarly excuses a control person who proves that she “had no knowledge of or reasonable ground to believe in the existence of the facts by reason of which [her] liability . . . is alleged to exist.” 15 U.S.C. § 77o (1994); *see supra* note 164.

¹⁸⁷ MISS. CODE ANN. § 75-71-719.

¹⁸⁸ *See supra* Part II.C.6.c.i.

¹⁸⁹ *See supra* note 14 and accompanying text.

¹⁹⁰ 15 U.S.C. § 78t(a). Exactly what constitutes “good faith” under federal law has been the subject of much debate, and considerable disagreement among (and even within) the circuits. *See Rowley, The Sky is Still Blue, supra* note 2, at 178-79 n.343. For an excellent discussion of scienter under federal securities law, see William H. Kuehnle, Commentary, *On Scienter, Knowledge, and Recklessness Under the Federal Securities Laws*, 34 HOUS. L. REV. 121 (1997).

There is no comparable federal defense to liability for materially aiding a primary violation of federal securities law because federal securities law no longer

E. Purchaser's Remedies

Whether she has succeeded in establishing a violation of the MSA's registration requirements, a fraudulent sale of securities, or both, section 717 affords a purchaser the following remedies in addition to those available at common law or in equity.¹⁹¹ Because secondary liability under section 719 presumes a primary violation of section 717, a successful plaintiff should be entitled to the same remedies against a secondary violator as the plaintiff would recover if the defendant were a primary violator.

1. Rescission

A purchaser who still owns the securities is entitled to have the transaction rescinded and, upon making a tender of the securities, to recover from the seller the consideration she paid for the securities, plus interest from the date of payment, less "any income received on the security."¹⁹² Tender is a nec-

recognizes aiding and abetting liability. *See* Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A., 511 U.S. 164, 191 (1994); *supra* notes 180-81 and accompanying text.

¹⁹¹ The rights and remedies provided by the MSA are in addition to any other statutory or common-law rights and remedies available to the purchaser. *See* MISS. CODE ANN. § 75-71-731. As the Mississippi Supreme Court eloquently explained in *Sanders v. Neely*, 19 So. 2d 424 (Miss. 1944):

To the extent that statutes, by their terms and necessary implications, and the common law are not repugnant, they co-exist and will be given effect. The presumption is that the Legislature does not intend to make alterations in the law beyond what it explicitly declares, either by express terms or by necessary implication, and does not intend to overthrow fundamental principles or to infringe existing rights, without expressing or clearly implying such intention Statutes are not to be understood as affecting any change in the common law beyond that which is clearly indicated, either by express terms or by necessary implication from the language used This principle is so established by both reason and authority that we deem a citation of the numerous cases so holding in this and other jurisdictions to be unnecessary.

Id. at 426-27 (quotation and citation omitted). Nonetheless, while a purchaser may elect to sue, e.g., under both the MSA and common law, she is entitled to only one recovery for her same loss.

¹⁹² MISS. CODE ANN. § 75-71-717(a); *see, e.g.*, *Johnson v. Yerger*, 612 F.2d 953, 958 (5th Cir. 1980) (applying precursor to section 717(a)(1), MISS. CODE ANN.

essary precondition to recovering consideration paid, and may be made at any time before entry of judgment.¹⁹³

2. Statutory Damages

A purchaser who no longer owns the securities is entitled to recover: (1) “damages in the amount that would be recoverable upon a tender”—that is, the consideration paid for the security, plus interest thereon from the date of payment, less any amount the purchaser received on the security—(2) less the value of the security when the purchaser disposed of it and interest on that amount from the date the purchaser disposed of the security.¹⁹⁴

§ 75-71-31 (1972), *repealed by* Act of Apr. 23, 1981, ch. 521, § 418, 1981 Miss. Laws 1521, 1552). Interest is at the rate of eight percent (8%) per annum. MISS. CODE ANN. § 75-71-717(a) (2000).

A plaintiff suing for common law fraud, *see, e.g.*, *Ezell v. Robbins*, 533 So. 2d 457, 461 (Miss. 1988); *Turner v. Wakefield*, 481 So. 2d 846, 848-49 (Miss. 1985); or negligent misrepresentation, *see, e.g.*, *Turner v. Terry*, Nos. 1999-CA-00753-SCT, 1999-CA-01395-SCT, 2001 WL 171318, at *9 (Miss. Feb. 22, 2001), may seek rescission in appropriate cases. However, a common law plaintiff seeking rescission must do so promptly or she may lose the right to rescind:

[T]he Gardners waived their option to rescind the contract [by which they purchased the stock of a corporation from the Littles] by managing and operating the corporation after discovery of the Littles' alleged fraud. “[S]tated in general terms, . . . assuming the fact of fraud, a contract obligation obtained by fraudulent representation is not void, but voidable. Upon discovery thereof, the one defrauded must act promptly and finally to repudiate the agreement; however, a continuance to ratify the contract terms constitutes a waiver.” As with any contract, both parties have a responsibility to ensure that their interests are protected. In the instant case, the Gardners failed to do that. If the Gardners felt that the Littles misrepresented the corporation's net worth or acted in bad faith, then they were required to either promptly rescind the contract or affirm the contract and maintain an action in damages.

Gardner v. Little, 755 So. 2d 1273, 1276 (Miss. Ct. App. 2000) (quoting *Turner*, 481 So. 2d at 848-49 (citations omitted)).

¹⁹³ MISS. CODE ANN. § 75-71-721; *see, e.g.*, *Johnson*, 612 F.2d at 958 (finding that plaintiffs made “legally sufficient tender” in their complaint filed in district court).

¹⁹⁴ MISS. CODE ANN. § 75-71-717(a). Interest, again, is at the rate of eight percent (8%) per annum. *See supra* note 192.

Prior to 1981, the MSA did not afford plaintiffs who had already sold their securities the opportunity of suing for damages arising from their purchase of unregistered securities. *See* MISS. CODE ANN. § 75-71-31 (1972), *repealed by* 1981

3. Prejudgment Interest

Section 717(a) explicitly includes prejudgment interest as part of the recovery due a plaintiff who still owns the security at the time she brings suit.¹⁹⁵ Prejudgment interest is implicit

Miss. Laws, ch. 521, § 418; *see, e.g.*, *Shivangi v. Dean Witter Reynolds, Inc.*, 107 F.R.D. 313, 323 (S.D. Miss. 1985) (applying section 75-71-31 and holding that, because plaintiffs "did not retender their stock, but instead sold it on the open market, they no longer have a remedy under the Mississippi Blue Sky Laws").

The statutory damages recoverable under section 717(a) are somewhat different from those available to those section 12(a)(2) plaintiffs who no longer own the securities that are the subject of their claim and to all claimants under section 10(b). Whereas the MSA's statutory damage remedy is based on disgorgement by the seller of the consideration it received from the purchaser, damages under section 12(a)(2) and section 10(b) are based on the difference between the value the purchaser paid for the security and the value of the security the purchaser received. *See, e.g.*, *Randall v. Loftsgarden*, 478 U.S. 647, 661-62 (1986); *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 155 (1972).

In addition to a cash price paid for a security, "consideration paid" for purposes of section 12(a)(2) may include, *inter alia*, the value of (1) shares of some other tangible or intangible property given in exchange for shares of the security at issue, *see, e.g.*, *Weft, Inc. v. G.C. Inv. Assocs.*, 630 F. Supp. 1138, 1144 (E.D.N.C. 1986), *aff'd*, 822 F.2d 56 (4th Cir. 1987); (2) capital advanced to the issuer of the security in consideration for stock or stock options, *see, e.g.*, *Mecca v. Gibraltar Corp. of Am.*, 746 F. Supp. 338, 348-49 (S.D.N.Y. 1990); (3) a controlling interest in a going concern ceded in exchange for securities, *see, e.g.*, *Wigand v. Flo-Tek, Inc.*, 609 F.2d 1028 (2d Cir. 1980); or (4) a legal claim foresworn in exchange for securities, *see, e.g.*, *Foster v. Fin. Tech., Inc.*, 517 F.2d 1068, 1071 (9th Cir. 1975).

The measure of damages for common law fraud is the so-called "benefit of the bargain" rule, whereby the plaintiff may recover "the difference between the real and the represented value of the property." *Hunt v. Sherrill*, 15 So. 2d 426, 429 (Miss. 1943); *accord* *Lloyd Ford Co. v. Sharp*, 192 So. 2d 398, 400 (Miss. 1966). In the absence of other proof, the price paid by the plaintiff will establish the plaintiff's compensatory damages. *See Hunt*, 15 So. 2d at 429; *accord* *Davidson v. Rogers*, 431 So. 2d 483, 485 (Miss. 1983).

¹⁹⁵ MISS. CODE ANN. § 75-71-717(a) (2000); *see supra* note 192; *see, e.g.*, *Johnson v. Yerger*, 612 F.2d 953, 959 (5th Cir. 1980) (applying precursor to section 717(a)(1), MISS. CODE ANN. § 75-71-31 (1972), *repealed by* 1981 Miss. Laws, ch. 521, § 418).

Prejudgment interest is available to successful plaintiffs under section 12(a)(2). *See, e.g.*, *Kaufman & Enzer Joint Venture v. Dedman*, 680 F. Supp. 805, 813-14 (W.D. La. 1987); *Monetary Mgmt. Group v. Kidder, Peabody & Co.*, 615 F. Supp. 1217, 1223 (E.D. Mo. 1985). Unlike section 59.115(2), which mandates prejudgment interest, the amount of prejudgment interest awarded to a successful section 12(2) plaintiff is a matter of judicial discretion. *See, e.g.*, *Commercial Union Assurance Co. v. Milken*, 17 F.3d 608, 615 (2d Cir. 1994); *Sharp v. Coopers &*

for a plaintiff who no longer owns the security, because she is entitled to recover "damages in the amount that would be recoverable upon a tender."¹⁹⁶

4. Attorneys' Fees and Costs

A successful section 717 plaintiff is also entitled to recover costs and reasonable attorneys' fees.¹⁹⁷

Lybrand, 649 F.2d 175, 193 (3d Cir. 1981). In exercising that discretion, a court may consider a number of factors, including: (1) the need to fully compensate the wronged party for actual damages suffered, *see, e.g.*, *Osterneck v. Ernst & Whinney*, 489 U.S. 169, 176 (1989); (2) the degree of personal wrongdoing on the part of the defendant, *see, e.g., id.*; (3) whether the defendant has been unjustly enriched, *see, e.g.*, *Ballay v. Legg Mason Wood Walker, Inc.* No. 88-6867, 1990 WL 48195, at *1 (E.D. Pa. 1990); (4) whether the plaintiff delayed unduly in bringing or prosecuting the action, *see, e.g., Osterneck*, 489 U.S. at 176; (5) the availability of alternative investment opportunities to the plaintiff, *see, e.g., id.*; (6) the remedial purpose of the statute involved, *see, e.g., Commercial Union*, 17 F.3d at 615; (7) considerations of fairness and the relative equities of the award, *see, e.g., Osterneck*, 489 U.S. at 176; and (8) such other general principles as are deemed relevant by the court, *see, e.g., Commercial Union*, 17 F.3d at 615.

¹⁹⁶ MISS. CODE ANN. § 75-71-717(a) (2000). In other words, the purchaser is entitled to recover the damages she would have recovered if she still owned the security. *See supra* note 194.

¹⁹⁷ MISS. CODE ANN. § 75-71-717(a); *see, e.g.*, *Seaboard Planning Corp. v. Powell*, 364 So. 2d 1091, 1096 (Miss. 1978) (applying precursor to current Mississippi Securities Act and finding that chancellor acted within his discretion in awarding attorneys' fees to defrauded purchasers); *see also, e.g.*, *Felts v. Nat'l Account Sys. Ass'n*, 469 F. Supp. 54, 65-66 (N.D. Miss. 1978) (applying section 25 of former Mississippi Securities Law, MISS. CODE ANN. § 75-71-25 (1972), *repealed* by 1981 Miss. Laws, ch. 521, § 418).

Section 11(e) of the 1933 Act, 15 U.S.C. § 77k(e) (1994), appears to authorize a successful section 12(a)(2) plaintiff to recover attorneys' fees at the trial court's discretion. *See, e.g.*, *Guthrie v. Downs*, Nos. 88-CV-75066-DT, 89-CV-71525-DT, 1991 WL 354939, at *6 (E.D. Mich. Aug. 7, 1991) ("Plaintiffs are, however, entitled under section 12(2) . . . to recover their costs of bringing these actions and reasonable attorney fees."), *aff'd*, 972 F.2d 350 (6th Cir. 1992). *But see, e.g.*, *Junker v. Crory*, 650 F.2d 1349, 1364 (5th Cir. 1981) ("Section 11(e) of the 1933 Act provides for a discretionary award of attorney's fees to the prevailing plaintiff in any suit brought under the Act, if the court determines that the defense advanced is frivolous, without merit, or brought in bad faith. *Absent such a finding, attorneys fees may not be awarded under section 11(e).*" (emphasis added)). Authorities are split over whether attorneys' fees are available to a successful section 10(b)/Rule 10b-5 plaintiff. *Compare, e.g.*, *Cotton v. Slone*, 4 F.2d 176, 181 (2d Cir. 1993) ("[A]ttorney's fees are not permitted in actions brought solely under section 10(b) of the Securities and Exchange Act. . . .") and *Abell v. Potomac Ins. Co.*, 858 F.2d 1104, 1142 (5th Cir. 1988) ("[A]ttorney's fees are not available as a

5. Punitive Damages

The MSA does not provide for punitive damages.¹⁹⁸

matter of course under rule 10b-5"), *vacated on other grounds*, 492 U.S. 914 (1989), *with* SEC v. Capital Counsellors, Inc., 378 F. Supp. 224, 226 (S.D.N.Y. 1974) (holding that parties bearing costs of prosecuting or defending action in order to protect public investor are entitled to be reimbursed for such costs), *aff'd*, 512 F.2d 654 (2d Cir. 1975) *and* Chris-Craft Indus., Inc. v. Indep. Stockholders Comm., 354 F. Supp. 895, 903 (D. Del. 1973) ("[I]n some instances attorneys' fees [are] an appropriate remedy for private litigants who establish violations of the [1934 Securities Exchange] Act." (citing *Mills v. Elec. Auto-Lite Co.*, 396 U.S. 375 (1970))).

Attorneys' fees are, likewise, generally unavailable to a prevailing plaintiff on a common law fraud or negligent misrepresentation claim, unless she can establish that she is entitled to punitive damages. *See, e.g.*, *Holland v. Mayfield*, No. 96-CA-01169-SCT, 1999 WL 353023, at *12 (Miss. June 3, 1999).

¹⁹⁸ Punitive damages are, likewise, unavailable to plaintiffs who successfully prosecute a claim under section 12(a)(2) of the 1933 Securities Act, 15 U.S.C. § 77l(a)(2) (Supp. V 1999), *see* *Hill York Corp. v. Am. Int'l Franchises, Inc.*, 448 F.2d 680, 697 (5th Cir. 1971); *see also* *Hunt v. Miller*, 908 F.2d 1210, 1216 n.13 (4th Cir. 1990), or under section 10(b) of the 1934 Securities Exchange Act, 15 U.S.C. § 78j(b) (1994), or Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5 (2000), *see* 15 U.S.C. § 78bb(a) (Supp. V 1999); *Hunt*, 908 F.2d at 1216 n.13; *Green v. Wolf Corp.*, 406 F.2d 291, 302-03 (2d Cir. 1968). However, section 78bb(a) does not prevent a plaintiff from recovering punitive damages on a pendent state law claim. *See Hunt*, 908 F.2d at 1216 n.13; *Young v. Taylor*, 466 F.2d 1329, 1337-38 (10th Cir. 1972).

Punitive damages are available at common law to a plaintiff who establishes by clear and convincing evidence that he was actually defrauded. *See* MISS. CODE ANN. § 11-1-65(1)(a) (2000); *see, e.g.*, *Holland*, 1999 WL 353023 at *11-12.

The rule is firmly established in Mississippi, that punitive damages are recoverable not only for willful and intentional wrong, but for such gross and reckless (conduct) as is, in the eyes of the law, the equivalent of willful wrong. The award of punitive damages, and the amount thereof, if any, rests in the discretion of the trier of the facts.

Felts, 469 F. Supp. at 69 (quotation and citations omitted).

In all cases involving an award of punitive damages, the fact finder, in determining the amount of punitive damages, shall consider, to the extent relevant, the following: the defendant's financial condition and net worth; the nature and reprehensibility of the defendant's wrongdoing, for example, the impact of the defendant's conduct on the plaintiff, or the relationship of the defendant to the plaintiff; the defendant's awareness of the amount of harm being caused and the defendant's motivation in causing such harm; the duration of the defendant's misconduct and whether the defendant attempted to conceal such misconduct; and any other circumstances shown by the evidence that bear on determining a proper amount of punitive damages

6. Injunctive Relief

The MSA empowers the Secretary of State to seek an injunction to enforce the provisions of the MSA.¹⁹⁹ No such right is given to any private party.

F. Pre-Suit Rescission Offers

The MSA does not require a plaintiff seeking to sue for damages or rescission to afford the defendant the opportunity to make good on the plaintiff's economic damages or rescind the subject transaction before the plaintiff files suit. However, if an MSA defendant makes a qualifying rescission offer under section 717(b), the plaintiff may not sue for the violation that is the subject of the rescission offer.²⁰⁰

The formal requisites of a rescission offer to a buyer are set forth in detail in section 717(b). There is, to date, no published decision of any Mississippi court, nor any rule or interpretive ruling from the Secretary of State, which specifically

MISS. CODE ANN. § 11-1-65(1)(e). "Punitive damages do not follow as the day the night every finding that a defendant has been guilty of fraud . . . Punitive damages are assessed 'only in extreme cases.'" *Gardner v. Jones*, 464 So. 2d 1144, 1148 (Miss. 1985). Misrepresentations made negligently, rather than fraudulently, will not support punitive damages, *see, e.g., Finkelberg v. Lockett*, 608 So. 2d 1214, 1220 (Miss. 1992), unless they rise to the level of gross negligence, *see, e.g., Jenkins v. CST Timber Co.*, 761 So. 2d 177, 180 (Miss. 2000).

¹⁹⁹ MISS. CODE ANN. § 75-71-715(3). In some cases, injunctive relief may be available to a section 12(a)(2) plaintiff, *see, e.g., Deckert v. Independence Shares Corp.*, 311 U.S. 282, 287-90 (1940); *Hoxworth v. Blinder, Robinson & Co.*, 903 F.2d 186, 194-97 (3d Cir. 1990), or a section 10(b)/Rule 10b-5 plaintiff, *see, e.g., Chris-Craft Indus., Inc. v. Indep. Stockholders Comm.*, 354 F. Supp. 895, 903 (D. Del. 1973). As a general rule, a party requesting a preliminary injunction must show either: "(1) a likelihood of success on the merits and the possibility of irreparable injury, or (2) the existence of serious questions going to the merits and the balance of hardships tipping [sharply] in [its] favor." *MAI Sys. Corp. v. Peak Computer, Inc.*, 991 F.2d 511, 516 (9th Cir. 1993) (quotation omitted). The first showing represents a continuum in which "the required degree of irreparable harm increases as the probability of success decreases." *MAI Systems*, 911 F.2d at 516; *accord Am. W. Airlines, Inc. v. Nat'l Mediation Bd.*, 119 F.3d 772, 777 (9th Cir. 1997), *cert. denied*, 523 U.S. 1021 (1998). Injunctive relief may also be available to a plaintiff alleging common law fraud. *See, e.g., Guastella v. Wardell*, 198 So. 2d 227 (Miss. 1967).

²⁰⁰ MISS. CODE ANN. § 75-71-717(b).

addresses either the validity of a rescission offer made pursuant to section 717(b) or the consequences of a defendant's failure to make a rescission offer or a plaintiff's failure to accept one.²⁰¹

III. CONCLUSION

The relevant provisions of the Mississippi Securities Act provide Mississippi plaintiffs with additional protections beyond those afforded by Mississippi common law or federal statutory law, and, generally speaking, they do so on what are more generous terms.

As an initial matter, a plaintiff suing under section 717(a)(2) of the MSA may do so at any time within two years after she actually or constructively discovered the existence of her claim²⁰²—regardless of how much time has elapsed since she purchased the securities in question or since her cause of action actually accrued.²⁰³ Limitations periods for common law fraud and negligent misrepresentation claims run three years from the date the plaintiff's cause of action accrued,²⁰⁴ regardless of when or whether the plaintiff discovered the existence of her claim,²⁰⁵ subject to equitable tolling due to the defendant's fraudulent concealment of the facts necessary for the plaintiff to discover the existence of her claim.²⁰⁶ A plaintiff suing under federal securities law must do so within three years after her cause of action accrued, but in any case within one year after she actually or constructively discovered the basis for her claim—even if the one-year discovery period expires before the three-year default limitations period.²⁰⁷ Thus, unless a plaintiff discovered the existence of her claim less

²⁰¹ See generally Michelle Rowe, *Rescission Offers Under Federal and State Securities Law*, 12 J. CORP. L. 383 (1987); Stephen G. Christianson, Annotation, *What Gives Rise to a Right of Rescission Under State Blue Sky Laws*, 52 A.L.R. 5th 491 (1997).

²⁰² See *supra* notes 152-53 and accompanying text.

²⁰³ See *supra* notes 152-58 and accompanying text.

²⁰⁴ See *supra* note 152.

²⁰⁵ *Id.*

²⁰⁶ *Id.*

²⁰⁷ *Id.*

than one year after it accrued, she would be afforded more time to seek redress under the MSA than under either Mississippi common law or federal securities law.

Plaintiffs suing under the MSA need not prove that they relied on the defendant's misrepresentation or omission in order to have their purchase rescinded or to recover damages,²⁰⁸ whereas plaintiffs suing for fraud or negligent misrepresentation must do so,²⁰⁹ as must plaintiffs suing under Rule 10b-5.²¹⁰ Likewise, plaintiffs suing under the MSA,²¹¹ like those suing for negligent misrepresentation,²¹² need not prove the defendant's state of mind at the time of the transaction, whereas a plaintiff suing for common law fraud²¹³ or under Rule 10b-5²¹⁴ must prove that the defendant acted with requisite scienter. Neither reliance nor scienter are elements of a section 12(a)(2) claim.²¹⁵ Thus, a plaintiff suing under the MSA has an easier principal case to make than one suing under Mississippi common law or under Rule 10b-5, and no harder a case to make than a plaintiff suing under section 12(a)(2).

Plaintiffs alleging common law fraud may recover punitive damages unavailable to plaintiffs suing under the MSA, the Mississippi common law of negligent misrepresentation, or federal securities law.²¹⁶ Plaintiffs suing under the MSA may recover reasonable attorneys' fees,²¹⁷ as may plaintiffs suing under the comparable provisions of federal securities law.²¹⁸ Plaintiffs suing for fraud or negligent misrepresentation, by comparison, are generally not entitled to recover attorneys' fees,²¹⁹ although an award of punitive damages to a successful fraud plaintiff may entitle her also to recover attorneys' fees.

²⁰⁸ See *supra* note 141 and accompanying text.

²⁰⁹ See *supra* notes 138-39 and accompanying text.

²¹⁰ See *supra* note 140.

²¹¹ See *supra* note 142 and accompanying text.

²¹² See *supra* note 143.

²¹³ See *supra* note 143 and accompanying text.

²¹⁴ See *supra* note 144 and accompanying text.

²¹⁵ See *supra* note 141.

²¹⁶ See *supra* note 198 and accompanying text.

²¹⁷ See *supra* note 197 and accompanying text.

²¹⁸ See *supra* note 197.

²¹⁹ *Id.*

Control person liability under the MSA is—or, at least, should be—coterminous with control person liability under federal securities law,²²⁰ although some have suggested reading the applicable federal statutes to permit imposing only proportionate liability on a control person who did not knowingly violate federal securities law,²²¹ whereas the MSA imposes joint and several liability without regard to the control person's knowledge or state of mind.²²² The MSA's other theory of "secondary" liability—namely, liability for materially aiding an MSA violation—has no federal counterpart.²²³ Anyone is potentially subject to liability for materially aiding an MSA violation, regardless of their job title or status, whereas control person liability is, by its nature, limited to particular classes of persons or entities, based on their relation to the "primary" violator or to the "primary" violation. As a consequence, a plaintiff suing under the MSA may be able to hold persons accountable who are now beyond the reach of federal law.

Finally, and not to be overlooked, the MSA also creates liability for those who offer or sell unregistered securities that are not exempt from the MSA's registration provisions.²²⁴ In so doing, the MSA provides Mississippi plaintiffs who did not purchase their unregistered securities from or in response to an offer made by "any means or instruments of transportation or communication in interstate commerce or of the mails"²²⁵—and, therefore, cannot sue under section 12(a)(1) of the 1933 Securities Act²²⁶—an opportunity for relief that is not available under federal law or Mississippi common law.

²²⁰ See *supra* notes 168-72 and accompanying text.

²²¹ See *supra* note 171.

²²² See *supra* notes 165 and 173 and accompanying text.

²²³ See *supra* note 180 and accompanying text.

²²⁴ See *supra* Part II.B.

²²⁵ 15 U.S.C. § 77l(a)(1) (Supp. V 1999).

²²⁶ Cf. *Ayers v. Wolfenbarger*, 491 F.2d 8, 16 (5th Cir. 1974) (holding that sales of stock in Alabama financial corporation to Alabama residents did not require registration under section 5 of 1933 Act, 15 U.S.C. § 77e (1994), and therefore could not give rise to liability under what is now section 12(a)(1), *id.* § 77l(a)(1), where no means or instruments of transportation or communication in interstate commerce or of mails were used to sell stock).