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The Federal Securities Laws, the First Amendment, and Commercial Speech: A Call for Consistency

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NOTES

THE FEDERAL SECURITIES LAWS, THE FIRST AMENDMENT, AND COMMERCIAL SPEECH: A CALL FOR CONSISTENCY

In light of the Supreme Court's increasingly expansive interpretation of the first amendment,[1] particularly in the area of commercial speech,[2] the issue has arisen whether the federal securities laws can withstand current first amendment scrutiny.[3] Indeed, one

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[1] U.S. CONST. amend. I. The first amendment provides in pertinent part: "Congress shall make no law . . . abridging the freedom of speech, or of the press . . . ." *Id.* The Supreme Court had not addressed first amendment issues until the Court developed the "clear and present danger" doctrine in cases arising during World War I. J. NOWAK, R. ROTUNDA & J. YOUNG, CONSTITUTIONAL LAW 874-75 & n.12 (2d ed. 1983); *see* Abrams v. United States, 250 U.S. 616, 618-19 (1919) (sustaining conviction for resisting war effort); Debs v. United States, 249 U.S. 211, 216 (1919) (sustaining conviction for obstruction of military recruitment services); Schenck v. United States, 249 U.S. 47, 52 (1919) (sustaining conviction under Espionage Act of 1917 for distributing leaflets critical of draft). Subsequently, however, the guarantee of free speech developed into this nation's most zealously protected constitutional right. *See, e.g.*, Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations, 413 U.S. 376, 381-82 (1973); Murdock v. Pennsylvania, 319 U.S. 105, 115 (1943); Stonecipher, *Safeguarding Speech and Press Guarantees: Preferred Position Postulate Reexamined*, in THE FIRST AMENDMENT RECONSIDERED 89, 94-96 (1982). Justice Cardozo recognized the preferred status of the first amendment as early as 1937 when he remarked that freedom of speech and thought "is the matrix, the indispensable condition, of nearly every other form of freedom." Palko v. Connecticut, 302 U.S. 319, 326-27 (1937). The words "preferred position" have been avoided by the Court during the past 35 years; however, the vagueness and overbreadth doctrines, the rule against prior restraints, and requirements of a "clear and present danger" or "actual malice" before speech may be punished exemplify other "judicial tools" that the Court has developed to sustain the preferred status of freedom of speech. *See generally* J. NOWAK, R. ROTUNDA & J. YOUNG, *supra*, at 864-65; Stonecipher, *supra*, at 98-107.

[2] *See infra* notes 25-48 and accompanying text.

[3] *See, e.g.*, SEC v. Suter, 732 F.2d 1294, 1299-1300 (7th Cir. 1984) (first amendment raised as defense in SEC action for injunction under Investment Advisers Act of 1940); SEC v. Lowe, 725 F.2d 892, 898-902 (2d Cir. 1984) (first amendment raised as defense in SEC action for injunction under the Investment Advisers Act of 1940), *cert. granted*, 105 S. Ct. 81 (1984) (No. 83-1911); SEC v. Wall St. Publishing Inst., Inc., 591 F. Supp. 1070, 1080-81 (D.D.C. 1984) (discussing first amendment issues involved in regulation of investment advice magazine), *motion for stay pending appeal granted*, [Current] FED. SEC. L. REP. (CCH) ¶ 91,635, at 99,219-20 (D.C. Cir. Aug. 10, 1984); *In re* W.T. Grant Co., [1980 Transfer

first amendment authority has suggested that the enormous power granted to the Securities and Exchange Commission (SEC or Commission) by the federal securities laws presents the most serious statutory regulation of speech.[4] For example, requirements that issuers, brokers, and dealers be registered with the Commission before they lawfully may engage in specified types of communication regarding securities[5] resemble licensing schemes that in other contexts have been struck down by the Supreme Court as prior restraints.[6] Statutory provisions that grant the Commission power to review documents before they become "effective," or public,[7] strengthened by the availability of criminal sanctions and SEC injunctions, essentially authorize the SEC to exercise the functions of a censor,[8] and thus present serious issues of prior restraint and

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Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,636, at 98,407-08 (Bankr. S.D.N.Y. Sept. 16, 1980) (first amendment discussed in private action to enjoin the communication of a proxy solicitation letter); Goodale, *The First Amendment and Securities Act: A Collision Course?*, N.Y.L.J., April 8, 1983, at 1, col. 1 (analyzing district court opinion in *Lowe* and arguing that the securities laws authorize unconstitutional prior restraints); Karmel, *First Amendment Questions Challenge the SEC*, N.Y.L.J., Oct. 18, 1984, at 1, col. 1 (arguing that the SEC often unconstitutionally restricts and chills free speech); *see also* Lewin, *Business and the Law: Commercial Free Speech*, N.Y. Times, Feb. 7, 1984, at D2, col. 1 (discussion with first amendment experts about ramifications of *Lowe*); Noble, *Business and the Law: The Licensing of Newsletters*, N.Y. Times, Aug. 21, 1984, at D2, col. 1 (analysis of *Wall St. Publishing* and *Lowe* cases); *cf.* Schoeman, *Subscription Advisers, Blue Sky Registration and the First Amendment*, 33 BUS. LAW. 249, 249-56 (1977) (first amendment violated by state blue sky regulation laws). One commentator has noted the "fundamental clash" between the securities laws and the first amendment, *see* Stephan, *Highlights of the Montgomery Ward Proxy Contest From a Lawyer's Viewpoint*, BUS. LAW., Nov. 1955, at 86, 93-95, and another the "inherent tension" between the two, *see* Fried, *Convicted Analyst Gets Right to Publish Advice*, N.Y. Times, Feb. 2, 1983, at D1, col. 1, D19, col. 3 (quoting former SEC commissioner Richard Smith).

[4] Goodale, *supra* note 3, at 1, col. 1. Floyd Abrams, a prominent first amendment practitioner, remarked that "the SEC went too far" when it totally banned the publication of investment newsletters in SEC v. Lowe, 725 F.2d 892, 902 (2d Cir. 1984), *cert. granted*, 105 S. Ct. 81 (1984) (No. 83-1911). *See* Lewin, *supra* note 3, at D2, col. 2. Similarly, James Clayton, co-director of the Reporters Committee for Freedom of the Press, accused the Commission of "expand[ing] its jurisdiction beyond that intended by Congress and beyond that authorized by the First Amendment." Noble, *supra* note 3, at D2, col. 2.

[5] For a discussion of first amendment issues raised by the registration provisions, see *infra* notes 49-56 & 118-123 and accompanying text.

[6] *See infra* note 14. In Jones v. SEC, 298 U.S. 1 (1936), the Supreme Court recognized that registration is "in effect an *ex parte* application for a license." *Id.* at 22.

[7] The word "effective" has been defined by the Supreme Court as connoting "completeness of operative force and freedom to act." Jones v. SEC, 298 U.S. 1, 18 (1936). For a discussion of SEC functions that entail reviewing documents, see *infra* notes 124-35 and accompanying text.

[8] *See infra* note 15.

"chilling."[9]

Although the Burger Court has been criticized for being too restrictive in its interpretation of the first amendment,[10] freedom of speech and press remains as expansive as ever.[11] As currently construed, the first amendment protects virtually all types of speech.[12] Even unprotected classes of speech continue to benefit from the Court's intolerance of prior restraints,[13] particularly when

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[9] *See* Karmel, *supra* note 3, at 2, col. 5. "Chilling" is a form of self-censorship that results when the legality of a contemplated speech or publication cannot readily be determined beforehand, causing the speaker to be deterred from communicating the message, or to make only those statements that clearly will not be punishable. *See* New York Times Co. v. Sullivan, 376 U.S. 254, 278-79 (1964); Smith v. California, 361 U.S. 147, 153-54 (1959). For a discussion of SEC "chilling," see *infra* note 129.

[10] *See, e.g.*, Abrams, *The Burger Court and the First Amendment: Putting a Decade into Perspective—II. An Analysis*, in THE FIRST AMENDMENT RECONSIDERED 138-43 (1982); Emerson, *First Amendment Doctrine and the Burger Court*, 68 CALIF. L. REV. 422, 440-58 (1980); Meiklejohn, *Commercial Speech and the First Amendment*, 13 CAL. W.L. REV. 430, 431 (1977).

[11] *See* Abrams, *supra* note 10, at 143; Emerson, *supra* note 10, at 422.

[12] *See, e.g.*, Erznoznik v. City of Jacksonville, 422 U.S. 205, 209-10 (1975) (ordinance cannot forbid drive-in theatres from showing offensive films even where visible from public street or public place); Papish v. Board of Curators, 410 U.S. 667, 670 (1973) (political cartoon depicting a policeman raping the Statue of Liberty and the Goddess of Justice, and an article entitled "M____f____ Acquitted"); Cohen v. California, 403 U.S. 15, 25 (1971) (granting full protection to wearing in public a jacket that displayed the words "F____ the Draft").

Notwithstanding the broad scope of the first amendment, some classes of speech have been denied first amendment protection. *See, e.g*, Herbert v. Lando, 441 U.S. 153, 158-60 (1979) (defamatory speech); Miller v. California, 413 U.S. 15, 23-24 (1973) (obscene speech); Chaplinsky v. New Hampshire, 315 U.S. 568, 571-72 (1942) ("fighting words").

[13] *See, e.g.*, Nebraska Press Ass'n v. Stuart, 427 U.S. 539, 570 (1976) (invalidating criminal trial judge's order prohibiting news media from reporting anything "strongly implicative" of defendant, despite judge's belief that order was necessary to ensure a fair trial); New York Times Co. v. United States, 403 U.S. 713, 714 (1971) (per curiam) (refusing to enjoin publication of Pentagon Papers despite assertion by government that publication would endanger national security); Organization for a Better Austin v. Keefe, 402 U.S. 415, 419-20 (1971) (reversing injunction that had prevented distribution of leaflets critical of real estate broker's business practices); Bantam Books, Inc. v. Sullivan, 372 U.S. 58, 70-71 (1963) (holding unconstitutional practices of local committee that functioned to suppress sale and circulation of objectionable literature); Near v. Minnesota, 283 U.S. 697, 713-19 (1931) (invalidating statutory "gag order" permitting injunctions against publication of malicious, scandalous, and defamatory periodicals). The rule against prior restraints dates back at least to Sir William Blackstone's criticism of the English censorship laws. *See* 4 W. BLACKSTONE, COMMENTARIES 152; *see also* T. EMERSON, THE SYSTEM OF FREEDOM OF EXPRESSION 504 (1970). Indeed, it has been argued that the sole purpose of the first amendment was to prevent prior restraint. *See* T. EMERSON, *supra*, at 504.

The Supreme Court has declared that "prior restraints on speech and publication are the most serious and the least tolerable infringement on First Amendment rights." Nebraska Press Ass'n v. Stuart, 427 U.S. 539, 559 (1976). Thus, the Court has observed that while subsequent punishment might "chill" speech, "prior restraint 'freezes' it at least for

achieved through licensing[14] and censorship.[15] Moreover, the Burger Court has parted with precedent by enlarging the scope of first

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the time." *Id.* (footnote omitted). The Court has warned repeatedly that prior restraints on speech come to the Court with a "heavy presumption against" their constitutional validity. *E.g.*, New York Times Co. v. United States, 403 U.S. 713, 714 (1971) (per curiam) (quoting Bantam Books, Inc. v. Sullivan, 372 U.S. 58, 70 (1963)).

[14] *See* W. HACHTEN, THE SUPREME COURT ON FREEDOM OF THE PRESS 72 (1968). Licensing is the least tolerated form of speech restriction. *Id.* Indeed, the rule against prior restraints grew directly from governmental attempts to license the press. Emerson, *The Doctrine of Prior Restraint*, 20 LAW & CONTEMP. PROBS. 648, 662 (1955). In the leading case of Lovell v. City of Griffin, 303 U.S. 444 (1938), the Court held facially invalid an ordinance that prohibited the distribution of circulars, handbooks, advertisements, or other literature without first obtaining a permit from the city manager. *See id.* at 451. Such an ordinance, the Court admonished, "strikes at the very foundation of the freedom of the press by subjecting it to license and censorship. The struggle for the freedom of the press was primarily directed against the power of the licensor." *Id.* The Court has noted that the defect in such a licensing scheme "is not merely the sporadic abuse of power by the censor but the pervasive threat inherent in its very existence," and, thus, one need not prove abuse to challenge the scheme. Thornhill v. Alabama, 310 U.S. 88, 97 (1940). In Schneider v. State, 308 U.S. 147 (1939), decided the year after *Lovell*, the Court held invalid as a prior restraint an ordinance that required a permit for canvassing, and that allowed the Chief of Police to refuse a permit where the applicant was "not of good character or [was] canvassing for a project not free from fraud." *Id.* at 158, 165. The *Schneider* Court implied that any requirement of advance permission would be viewed as an unconstitutional prior restraint. *See id.* at 160-65; Emerson, *supra*, at 663. For a more recent illustration of judicial intolerance of licensing, see Shuttlesworth v. City of Birmingham, 394 U.S. 147, 149-51 (1969).

[15] *See* W. HACHTEN, *supra* note 14, at 59 (censorship and prior restraint are "repugnant" under the Constitution, and the Supreme Court has made it increasingly difficult for the official censor to do his job). In Near v. Minnesota, 283 U.S. 697 (1931), the Supreme Court struck down a statute that permitted the prior restraint of malicious, scandalous, and defamatory newspapers and periodicals. *See id.* at 701-02, 722-23. Chief Justice Hughes, writing for the majority, noted that "liberty of the press, historically considered and taken up by the Federal Constitution, has meant, principally although not exclusively, immunity from previous restraints or censorship." *Id.* at 716. Justice Black also has labelled censorship "the deadly enemy of freedom and progress. The plain language of the Constitution forbids it." Smith v. California, 361 U.S. 147, 160 (1959) (Black, J., concurring). Justice Douglas, dissenting in Times Film Corp. v. City of Chicago, 365 U.S. 43 (1961), decried censorship because:

> The regime of the censor is deadening. One who writes cannot afford entanglements with the man whose pencil can keep his production from the market. The result is a pattern of conformity. . . .
>
> Another evil of censorship is the ease with which the censor can erode liberty of expression. One stroke of the pen is all that is needed. Under a censor's regime the weights are cast against freedom. . . . [T]he censor . . . is given a presumption of being correct. That advantage disappears when the government must wait until a publication is made and then prove its case . . . in a public trial. . . .
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> . . . .
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> No more potent force . . . could be designed than censorship. It is a weapon that no minority or majority group, acting through government, should be allowed to wield over any of us.

Id. at 82-84 (Douglas, J., dissenting) (footnotes omitted).

amendment protection to include commercial speech.[16] The Court, however, has not extended full first amendment protection to commercial speech,[17] and has left open the question of whether the strict rule against prior restraint will apply to regulation of commercial speech.[18]

It is suggested that the enormous authority granted to the SEC under the securities laws is inconsistent with the Supreme Court's current interpretation of the first amendment. It is suggested further that no court has provided an adequate reconciliation of the interests represented in this conflict.[19] Accordingly, this Note will analyze the federal securities laws under current first amendment law. After an initial examination of the Supreme Court cases that have developed the law of commercial speech,[20] the Note will discuss and critique several recent cases in which federal courts have considered, but rejected, first amendment defenses against SEC enforcement of the Investment Advisers Act of 1940.[21] The Note then will consider freedom of speech issues presented by provisions in the Securities Act of 1933[22] and the Se-

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[16] *See infra* notes 32-47 and accompanying text. Even those who have criticized the present Court for interpreting the first amendment too narrowly have recognized the liberal approach taken in commercial speech cases. *See, e.g.*, Meiklejohn, *supra* note 10, at 431.

[17] *See, e.g.*, Bolger v. Youngs Drug Prods. Corp., 103 S. Ct. 2875, 2879 (1983) (citing Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n, 447 U.S. 557, 562-63 (1980) and Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc., 425 U.S. 748, 771-72 n.24 (1976)). *But see* J. NOWAK, R. ROTUNDA & J. YOUNG, *supra* note 1, at 923 (commercial speech now seems to receive full protection).

[18] Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n, 447 U.S. 557, 571 n.13 (1980) (citing Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc., 425 U.S. 748, 771-72 n.24 (1976)).

[19] In the few securities cases in which the first amendment has been raised, the courts generally have not given much consideration to the issue. *See, e.g.*, Underhill Assocs., Inc. v. Bradshaw, 674 F.2d 293, 296 (4th Cir. 1982) (one paragraph in opinion devoted to dismissal of first amendment challenge to state registration statute); SEC v. Wall St. Transcript Corp., 422 F.2d 1371, 1378-80 (2d Cir.) (rejecting first amendment challenge against Investment Advisers Act of 1940), *cert. denied*, 398 U.S. 958 (1970); Halsted v. SEC, 182 F.2d 660, 668-69 (D.C. Cir. 1950) (rejecting first amendment challenge against Public Utility Holding Company Act of 1935).

[20] *See infra* notes 25-48 and accompanying text.

[21] SEC v. Suter, 732 F.2d 1294, 1299-1300 (7th Cir. 1984); SEC v. Lowe, 725 F.2d 892, 902 (2d Cir.1984), *cert. granted*, 105 S. Ct. 81 (1984) (No. 83-1911); SEC v. Wall St. Publishing Inst. Inc., 591 F. Supp. 1070 (1984), *motion for stay pending appeal granted*, [Current] FED. SEC. L. REP. (CCH) ¶ 91,635, at 99,219-20 (D.C. Cir. Aug. 10, 1984); *see infra* notes 49-93 and accompanying text. For a discussion of the Investment Advisers Act of 1940, 15 U.S.C. §§ 80b-1 to 80b-21 (1982), see *infra* notes 49-55 and accompanying text.

[22] 15 U.S.C. §§ 77a-77aa (1982); *see infra* notes 120-22 & 125-30 and accompanying text.

curities Exchange Act of 1934,[23] and will conclude with the suggestion that SEC prior restraint cannot be justified under present constitutional standards.[24]

COMMERCIAL FREE SPEECH

Until recently, the Supreme Court recognized no protection for purely commercial speech. In *Valentine v. Chrestensen*,[25] the Court sustained the constitutionality of a New York City ordinance that completely prohibited the distribution of commercial advertisement handbills, cards, and circulars in the streets.[26] Justice Roberts, writing for a unanimous Court, stated unequivocally that regulation of commercial advertising was a matter solely of legislative judgment, subject to no first amendment restraint.[27] Apparently, the rationale behind the Court's holding was that commercial advertising is motivated purely by economic self-interest, and thus is more "durable" and less likely to be "chilled" than other classes of speech.[28] As a result of *Valentine*, legislatures were free to regulate business advertising as they would other types of business activity.[29]

Valentine subsequently was distinguished in cases involving noncommercial advertising,[30] but denial of first amendment pro-

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[23] 15 U.S.C. §§ 78a-78kk (1982 & Supp. 1983); *see infra* notes 123 & 131-35 and accompanying text.

[24] *See infra* notes 142-54 and accompanying text.

[25] 316 U.S. 52 (1942).

[26] *Id.* at 55. The defendant in *Valentine* prepared and printed a handbill advertising a United States Navy submarine he exhibited for profit. *See id.* at 52-53. The Court rejected the defendant's argument that because the reverse side of his handbill contained a message of protest against a city agency, the communication should be protected. *Id.* at 55.

[27] *Id.* at 54.

[28] *See id.* at 55; *see also* Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc., 425 U.S. 748, 771-72 n.24 (1976). In footnote 24 of the *Virginia Board* opinion, the Court noted the "commonsense differences" between commercial speech and other speech, reasoning that since the communicator of the former necessarily has extensive knowledge of his product, and is motivated by a desire for profit, a lesser degree of protection is necessary. 425 U.S. at 771-72 n.24; *see also* Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n, 447 U.S. 557, 564 n.6 (1980) (noting factors that render commercial speech "a hardy breed of expression").

[29] *See, e.g.*, Breard v. Alexandria, 341 U.S. 622, 631-33, 641-45 (1951) (upholding as valid exercise of police power an ordinance forbidding door-to-door solicitations of magazines and periodicals).

[30] In the landmark defamation case of New York Times Co. v. Sullivan, 376 U.S. 254 (1964), the Court accorded protection to a paid advertisement because it communicated information, opinion, and grievances "of the highest public interest and concern." *Id.* at 266. In Bigelow v. Virginia, 421 U.S. 809 (1975), the Court likewise distinguished the purely com-

tection for purely commercial advertising remained the law for over three decades.[31] In 1976, however, the Supreme Court overruled this "highly paternalistic approach" in *Virginia State Board of Pharmacy v. Virginia Citizens Consumer Council, Inc.*[32] In invalidating a Virginia statute that prohibited pharmacists from advertising the prices of prescription drugs, the Court held that, as long as it is truthful and concerns lawful activity, speech is not wholly outside first amendment protection even if it does "no more than propose a commercial transaction."[33] Purely economic motive, the Court reasoned, should not of itself disqualify the speaker from protection.[34] In a free market economy, it was observed, "the free flow of commercial information is indispensable."[35] Therefore, particular consumers, and society as a whole, enjoy first amendment rights to receive the information contained in commercial advertisements.[36]

Although the *Virginia Board* holding has not escaped criticism,[37] the Court has reaffirmed and expanded protection of com-

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mercial advertisement in *Valentine* from protected public interest advertisement. *See id.* at 819-22. The abortion advertisement in *Bigelow*, the Court reasoned, contained sufficient factual information of general interest to deserve first amendment protection. *Id.* at 822.

[31] *See, e.g.*, Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations, 413 U.S. 376, 384-85, 388-91 (1973) (rejecting first amendment challenge to ordinance forbidding newspapers to carry gender-designated employment advertisements); Breard v. Alexandria, 341 U.S. 622, 641-45 (1951) (upholding ordinance forbidding door-to-door business solicitations).

[32] 425 U.S. 748, 770 (1976).

[33] *Id.* at 762, 773 (quoting Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations, 413 U.S. 376, 385 (1973)).

[34] 425 U.S. at 762; *cf.* New York Times Co. v. Sullivan, 376 U.S. 254, 266 (1964) (that the publisher is paid for printing an advertisement does not, of itself, render the advertisement commercial). Justice Stevens has observed that "even Shakespeare may have been motivated by the prospect of pecuniary reward." Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n, 447 U.S. 557, 580 (1980) (Stevens, J., concurring in judgment).

[35] *Virginia Board*, 425 U.S. at 765.

[36] *Id.* at 756-57, 763-65. The *Virginia Board* Court found that "[a]s to the particular consumer's interest in the free flow of commercial information, that interest may be as keen, if not keener by far, than his interest in the day's most urgent political debate." *Id.* at 763. One commentator, in an influential article written before commercial speech was afforded any protection, argued that commercial speech is often as valuable as, and even more valuable than, political speech, and consequently should be given comparable protection. *See* Redish, *The First Amendment in the Marketplace: Commercial Speech and the Values of Free Expression*, 39 GEO. WASH. L. REV. 429, 432-34, 443-48 (1971).

[37] *See, e.g.*, Baker, *Commercial Speech: A Problem in the Theory of Freedom*, 62 IOWA L. REV. 1, 2-3, 44-49, 53-54 (1976); Baldasty & Simpson, *The Deceptive "Right to Know": How Pessimism Rewrote the First Amendment*, 56 WASH. L. REV. 365, 391-92 (1981). Justice Rehnquist, who has dissented from nearly all of the cases affording protection to commercial speech, *see* Riggs, *The Burger Court and Individual Rights: Commercial Speech as*

mercial speech in the decade following that decision.[38] The first amendment has been applied to strike down government restrictions placed on contraceptive advertisements,[39] attorney advertisements,[40] public utility messages,[41] and the use of "for sale" signs in

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a Case Study, 21 SANTA CLARA L. REV. 957, 986 (1981) (table), has been perhaps the strongest critic of the Court's holding in *Virginia Board*. Insisting that the first amendment was intended primarily to protect speech about "political, social, and other public issues," Justice Rehnquist's dissent in *Virginia Board* objected to the majority's inclusion of speech concerning "the decision of a particular individual as to whether to purchase one or another kind of shampoo." *Virginia Board*, 425 U.S. at 787 (Rehnquist, J., dissenting). Justice Rehnquist has demonstrated a reluctance "to take even one step down the 'slippery slope' away from" the rule set out in *Valentine*. *See* Bates v. State Bar of Arizona, 433 U.S. 350, 405 (1977) (Rehnquist, J., dissenting). More recently, Justice Rehnquist warned that the present four-part test for commercial speech restrictions, *see infra* note 47 and accompanying text, has "devitalized" the first amendment by raising commercial speech to a level of protection "virtually indistinguishable from that of noncommercial speech." Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n, 447 U.S. 557, 591 (1980) (Rehnquist, J., dissenting).

[38] *See infra* notes 39-44 and accompanying text. *But see* G. GUNTHER, CASES AND MATERIALS ON CONSTITUTIONAL LAW 1381-82 (10th ed. 1980) (Court recently has become skeptical about its protection of commercial speech).

[39] *See, e.g.*, Bolger v. Youngs Drug Prods. Corp., 103 S. Ct. 2875, 2885 (1983); Carey v. Population Servs. Int'l, 431 U.S. 678, 700 (1977). In *Carey*, a New York statute prohibited all "advertisement or display" of contraceptives. 431 U.S. at 681 & n.1. The Court held that the asserted state interests—to shield the public from offensive and embarrassing material and to avoid legitimizing sexual promiscuity among young people—were not sufficient to justify suppression of commercial speech. *Id.* at 701.

The statute in *Bolger* was a federal law that prohibited the mailing of unsolicited contraceptive advertisements. 103 S. Ct. at 2877. The Court again dismissed the contention that the government could suppress material because of its offensive character, *id.* at 2883, and opined that the statute only marginally advanced the second asserted governmental interest of aiding parents in educating their children about birth control, *id.* at 2883-84. The government may allow addressees to give affirmative notice to the mailer that they wish no further offensive mailings, but the government may not completely exclude from the mails all material that it decides might potentially offend the public. *Id.* at 2883.

[40] *See, e.g.*, Bates v. State Bar of Arizona, 433 U.S. 350, 384 (1977). Less than 2 years after the *Virginia Board* Court left the question open, *see* 425 U.S. at 773 n.25, attorney advertising was given first amendment protection for the first time in *Bates*, *see* 433 U.S. at 384. As in *Virginia Board*, the Court in *Bates* stressed the "indispensable role" performed by commercial speech: informing the public to facilitate the allocation of resources in a free market economy. *Id.* at 364. At issue in *Bates* was a bar association disciplinary rule forbidding attorney advertisement by any means of commercial publicity. *See id.* at 355. The appellants placed an advertisement in a daily newspaper and were suspended from the practice of law. *Id.* at 354, 356. Concluding that *Virginia Board* was controlling, the Court held the disciplinary rule unconstitutional because it "serve[d] to inhibit the free flow of commercial information and to keep the public in ignorance." *Id.* at 365.

Within the year following *Bates*, the Court decided two more attorney advertisement cases on the same day, invalidating a disciplinary sanction in one, while upholding a sanction in the other. In *In re* Primus, 436 U.S. 412 (1978), an attorney associated with the American Civil Liberties Union (ACLU) was reprimanded for sending a letter to a woman advising her that free legal assistance was available from the ACLU, *see id.* at 416-19, 416 n.6. The other case decided that day, Ohralik v. Ohio State Bar Ass'n, 436 U.S. 447 (1978),

the sale of private homes.[42] With few exceptions,[43] the Court has evinced a consistent intolerance of state action that, even when serving a substantial governmental interest, unnecessarily interferes with one's right to communicate freely with potential customers.[44]

The current status of commercial speech law was solidified in *Central Hudson Gas & Electric Corp. v. Public Service Commis-*

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involved the disciplinary sanctioning of an attorney who had personally solicited a hospitalized automobile accident victim, *id.* at 449-54. The disciplinary sanction in *Ohralik* was upheld, *id.* at 468, while the sanction in *Primus* was reversed, 436 U.S. at 439. In distinguishing the two cases, the Court determined that the letter of advice at issue in *Primus* was significantly less likely to provide opportunity for overreaching or coercion than the in-person solicitation in *Ohralik*. *See Primus*, 436 U.S. at 435-36. The Court also distinguished the motive of advancing beliefs and ideas in *Primus* from the motive of pecuniary gain in *Ohralik*. *Id.* at 422.

The Court's most recent decision on attorney advertising is *In re* R.M.J., 455 U.S. 191 (1982). In *R.M.J.*, the attorney advertisement, placed in newspapers and a local telephone directory, violated a state rule prohibiting the use of specified words and phrases in attempting to solicit clients. *See id.* at 196-98, 197 n.8. Invalidating the restrictive rule, the Court summarized the law of commercial speech concerning attorney advertising:

> Truthful advertising related to lawful activities is entitled to the protections of the First Amendment. But when the particular content or method of the advertising suggests that it is inherently misleading or when experience has proved that in fact such advertising is subject to abuse, the States may impose appropriate restrictions. . . . [However,] restrictions upon such advertising may be no broader than reasonably necessary to prevent the deception.

Id. at 203. For a discussion of the implications of *R.M.J.*, and of the current status of attorney advertising, see Whitman & Stoltenberg, *The Present Constitutional Status of Lawyer Advertising—Theoretical and Practical Implications of* In re R.M.J., 57 ST. JOHN'S L. REV. 445, 474-82 (1983).

[41] *See, e.g.*, Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n, 447 U.S. 557, 571-72 (1980); Consolidated Edison Co. of New York, Inc. v. Public Serv. Comm'n, 447 U.S. 530, 544 (1980). In *Consolidated Edison*, a public utility included in its bills inserts discussing issues of public policy, *see* 447 U.S. at 532, and thus the commercial speech doctrine was not controlling, *see id.* at 533. *Central Hudson*, on the other hand, has become the most crucial case in the law of commercial speech. *See infra* notes 45-48 and accompanying text.

[42] *See, e.g.*, Linmark Assocs., Inc. v. Township of Willingboro, 431 U.S. 85, 98 (1977). Conceding that the town asserted a "vital" interest in maintaining a stable, racially integrated community, *id.* at 94, the Court nevertheless invalidated an ordinance restricting the use of "for sale" signs because it did not directly advance that interest and it restricted the right of the community to receive a free flow of housing information, *id.* at 95-96. The majority reasoned that, to protect the community from the evils of "panic selling," the remedy should be "more speech, not enforced silence." *Id.* at 97 (quoting Whitney v. California, 274 U.S. 357, 377 (1927) (Brandeis, J., concurring)).

[43] *See, e.g.*, Friedman v. Rogers, 440 U.S. 1, 12-13 (1979) (statute prohibiting practice of optometry under a trade name upheld because trade names may easily be used to deceive and mislead); Ohralik v. Ohio State Bar Ass'n, 436 U.S. 447, 464-65 (1978) (disciplinary sanction imposed against attorney for "ambulance chasing" upheld because such in-person solicitation creates substantial risk of overreaching).

[44] *See supra* notes 39-42 and accompanying text.

sion.[45] In *Central Hudson*, the Court invalidated a regulation that prohibited an electric utility from advertising to promote the consumption of electricity.[46] A four-part analysis was developed to determine the constitutionality of commercial speech restrictions:

> For commercial speech to come within [first amendment protection], it at least must concern lawful activity and not be misleading. Next, we ask whether the asserted governmental interest is substantial. If both inquiries yield positive answers, we must determine whether the regulation directly advances the governmental interest asserted, and whether it is not more extensive than is necessary to serve that interest.[47]

Thus, if speech regulated by the SEC is within the class of commercial speech, the *Central Hudson* test will determine the constitutional validity of the regulatory scheme.[48] However, as will be suggested in the following analysis of cases arising under the Investment Advisers Act of 1940, courts should be cautious not to conclude prematurely that all publications about securities are necessarily commercial speech.

FIRST AMENDMENT CHALLENGES TO THE INVESTMENT ADVISERS ACT

Designed to prevent deception, manipulation, and other potential misconduct by those who furnish paid advice about securities investments,[49] the Investment Advisers Act of 1940 (Invest-

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[45] 447 U.S. 557 (1980).

[46] *See id.* at 558, 571-72. The regulation in *Central Hudson* originally was passed in 1973 as a response to the fuel shortage, but was continued after the shortage to help promote the national policy of conserving energy. *See id.* at 559. "Informational" advertising—that which merely encouraged ratepayers to shift their consumption to off-peak hours—was permitted by the regulation. *See id.* at 560.

[47] *Id.* at 566. Applying the four-part test, the *Central Hudson* Court found both of the asserted state interests—conservation of energy and maintenance of fair and efficient rates—to be "substantial." *Id.* at 568-69. The Court further found that the regulation directly advanced the state interest in conservation. *Id.* at 569. However, the ban on promotional advertising failed to meet the fourth requirement of the test: it was not proven to be the least restrictive means by which the interest could have been achieved. *See id.* at 569-71. Thus, it was more extensive than necessary, and consequently was held invalid. *See id.* at 571-72.

[48] *See infra* notes 142-54 and accompanying text.

[49] *See* S. REP. No. 1775, 76th Cong., 3d Sess. 21 (1940); H.R. REP. No. 2639, 76th Cong., 3d Sess. 28 (1940). *See generally* SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186-92 (1963) (Investment Advisers Act designed to eliminate certain abuses in the securities industry); Abrahamson v. Fleschner, 568 F.2d 862, 870-73 (2d Cir. 1977) (Act illustrates that the problems and abuses of investment advisory services must be controlled through federal legislation), *cert. denied*, 436 U.S. 905 (1978).

ment Advisers Act or Act)[50] prohibits an investment adviser from using the mails or interstate commerce before registering with the SEC.[51] The term "investment adviser" includes anyone who, for compensation, either advises others about buying and selling securities, or as part of a regular business analyzes or reports about securities.[52] The statute excludes from its coverage, however, "the publisher of any bona fide newspaper, news magazine or business or financial publication of general and regular circulation."[53] The SEC may enforce the Act by, *inter alia*, denying or revoking an adviser's registration,[54] and obtaining injunctive relief against the publication of advice by unregistered advisers.[55] Recently, litigation has arisen in which defendants have argued unsuccessfully that to allow the SEC to enjoin the publication of impersonal investment periodicals would constitute prior restraint in violation of the first amendment.[56]

SEC v. Lowe

In *SEC v. Lowe*,[57] the defendant Lowe published subscription newsletters containing general observations and comments about the securities and bullion markets, and impersonal advice about the buying and selling of specific stocks and bullion.[58] After Lowe was convicted of criminal misconduct as an investment adviser, the

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[50] Ch. 686, tit. 2, 54 Stat. 847 (1940) (codified as amended at 15 U.S.C. §§ 80b-1 to 80b-21 (1982)).

[51] 15 U.S.C. § 80b-3(a) (1982).

[52] *Id.* § 80b-2(a)(11).

[53] *Id.*

[54] *Id.* § 80b-3(e).

[55] *Id.* § 80b-9(e).

[56] *See* SEC v. Suter, 732 F.2d 1294, 1299-1300 (7th Cir. 1984); SEC v. Lowe, 725 F.2d 892, 901-02 (2d Cir.), *cert. granted*, 105 S. Ct. 81 (1984) (No. 83-1911); SEC v. Wall St. Publishing Institute, Inc., 591 F. Supp. 1070, 1080-81 (D.D.C. 1984), *motion for stay pending appeal granted*, [Current] FED. SEC. L. REP. (CCH) ¶ 91,635, at 99,219-20 (D.C. Cir. Aug. 10, 1984). In the past 3 years, the SEC has commenced seven civil cases, twelve administrative proceedings, and five investigations against publishers of investment newsletters. Ingersoll, *Regulating Advice: Financial Newsletters Face Growing Pressure to Register with SEC*, Wall St. J., Nov. 15, 1984, at 1, col. 6, 20, col.1.

[57] 725 F.2d 892 (2d Cir.), *cert. granted*, 105 S. Ct. 81 (1984) (No. 83-1911).

[58] *See* SEC v. Lowe, 556 F. Supp. 1359, 1361 (E.D.N.Y. 1983), *rev'd*, 725 F.2d 892 (2d Cir.), *cert. granted*, 105 S. Ct. 81 (1984) (No. 83-1911). Lowe published three services: the *Lowe Investment Letter*, the *Lowe Stock Advisory*, and the *Lowe Stock Chart Service*. *Id.* The former two were published only at irregular intervals, and the third had not yet been published. *Id.* Lowe also offered a telephone hotline with the most current information. *Id.* Both the district court and the Second Circuit held this hotline unprotected by the first amendment. *See* 556 F. Supp. at 1371; 725 F.2d at 902.

SEC, pursuant to the Investment Advisers Act, revoked his registration.[59] Lowe nevertheless continued to publish his newsletters, and the Commission brought an action in federal district court to enjoin further publication.[60] In one of the first decisions in which a court has applied the first amendment to restrict the SEC's ability to enforce the securities regulations, Chief Judge Weinstein of the Eastern District of New York denied the injunctive relief.[61] Chief Judge Weinstein observed that "the combination of fact, economic and political analyses, conjecture, and recommendation" that is characteristic of newsletters published by "detached observer[s]" such as Lowe probably renders such communication outside the category of commercial speech.[62] The case was decided, however, under the more lenient scrutiny of a commercial speech analysis.[63] Chief Judge Weinstein held that an impermissible prior restraint would result if the Investment Advisers Act authorized the SEC to deny, by means of a license revocation based on past misconduct, Lowe's right to publish impersonal investment advice.[64] Instead of declaring the Act unconstitutional, however, Chief Judge Weinstein narrowly construed the Act to avoid its constitutional infirmity.[65] The opinion distinguished between personal and impersonal advice, holding that only the former may constitutionally be

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[59] *In re* Lowe Management Corp., [1981 Transfer Binder] FED SEC. L. REP. (CCH) ¶ 82,873, at 84,324 (May 11, 1981). Lowe's criminal misconduct included misappropriation of client funds, failure to register under New York law, grand larceny, and tampering with evidence. *See id.*

[60] *Lowe*, 556 F. Supp. at 1362.

[61] *Id.* at 1371. Experts believe the decision of the district court was the first to accept the argument that SEC injunctions may violate the free speech guarantee. *See, e.g.*, Fried, *supra* note 3, at D19, col. 3 (quoting former SEC commissioner Richard Smith); Goodale, *supra* note 3, at 4, col. 1. *But see* SEC v. Wall St. Transcript Corp., 294 F. Supp. 298, 304, 307 (S.D.N.Y. 1968) (denying enforcement of SEC subpoena against weekly securities tabloid), *rev'd*, 422 F.2d 1371 (2d Cir.), *cert. denied*, 398 U.S. 958 (1970).

[62] *Lowe*, 556 F. Supp. at 1366-67. Observing that economic discussion is often intermingled with political discussion, and even more important to the public, *id.* at 1367, Chief Judge Weinstein determined that the Lowe newsletters more closely resembled public issue speech than product advertising, *id.* at 1366-67.

[63] *See id.* at 1365-66. Chief Judge Weinstein applied the four-part test of Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n, 447 U.S. 557, 566 (1980); *see supra* notes 45-47 and accompanying text, and determined that the Investment Advisers Act failed to meet the fourth requirement of the test; namely, it was more extensive than necessary to achieve what was conceded to be a substantial governmental interest, *Lowe*, 556 F. Supp. at 1366. The court found that less restrictive alternative means were available, such as requiring disclosure about Lowe's past convictions. *Id.*

[64] *Lowe*, 556 F. Supp. at 1361, 1371.

[65] *Id.* at 1368-69.

subjected to the prior restraint of the Investment Advisers Act.[66]

The district court decision was reversed by a divided Second Circuit.[67] The circuit court, rejecting the view that commercial speech includes only advertising, had little difficulty dismissing the contention that investment newsletters are entitled to full first amendment protection.[68] The majority relied upon pre-*Virginia Board* precedent to sustain the facial validity of the Investment Advisers Act,[69] and drew an analogy between SEC registration and the licensing of professionals to dismiss the argument that revocation of registration on the basis of past misconduct is impermissible.[70] Such revocation, reasoned the court, is a legitimate regula-

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[66] *Id.* at 1369, 1371. The distinction between personal and impersonal advice presumably rests upon the assumption that the latter is inherently more susceptible to abuse. *Cf.* Ohralik v. Ohio State Bar Ass'n, 436 U.S. 447, 455, 457 (1978) (distinguishing in-person solicitation from public advertisement by attorney). Chief Judge Weinstein also held that Lowe was not required under current securities laws or regulations to disclose to his subscribers any information concerning his past misconduct or his registration revocation. 556 F. Supp. at 1370.

[67] SEC v. Lowe, 725 F.2d. 892, 902 (2d Cir. 1984), *cert. granted*, 105 S. Ct. 81 (1984) (No. 83-1911). Judge Oakes wrote the opinion of the court in which Judge Van Graafeiland concurred in a separate opinion. District Judge Brieant, sitting by designation, dissented.

[68] *See id.* at 900-01. The Second Circuit suggested that free speech was not an issue at all; the case involved merely "the permissible regulation of economic *activity*." *Id.* at 901 (emphasis added).

[69] *See id.* at 898-900. The precedent cited as controlling was SEC v. Wall St. Transcript Corp., 422 F.2d 1371 (2d Cir.), *cert. denied*, 398 U.S. 958 (1970), wherein the Second Circuit held that enforcement of a subpoena that required the production of materials by a weekly securities information tabloid did not offend the first amendment, *see* 422 F.2d at 1381. In *Wall St. Transcript*, the court held that the Investment Advisers Act need not exclude "all publications which could conceivably be brought within the term 'typical newspaper,'" *id.* at 1378, and that it "does not on its face abridge freedom of the press simply because it may be applied to publications which are classified formally as part of the 'press,'" *id.* at 1379. In *Lowe*, the Second Circuit was well aware that *Wall St. Transcript* was decided before commercial speech was given any first amendment protection, but nonetheless determined that it "still states good law." 725 F.2d at 899. This determination, it is submitted, was erroneous; the holding in *Wall St. Transcript* was premised on case law emphasizing that commercial speech is wholly unprotected by the first amendment, *see Wall St. Transcript*, 422 F.2d at 1379. *See Lowe*, 725 F.2d at 904 (Brieant, J., dissenting) (*Wall St. Transcript* is now "as dead as Marley").

[70] *Lowe*, 725 F.2d at 901. "Saying that appellees may not sell their views as to the purchase, sale, or holding of certain securities is no different from saying that a disbarred lawyer may not sell legal advice." *Id.* at 902. This analogy, it is submitted, is inapposite. The more appropriate analogy is whether a bar association may prohibit a disbarred attorney from publishing impersonal newsletters about citizens' legal rights, including opinions about the value of legal services performed by specific law firms and practitioners, or whether non-attorneys may be prohibited from publishing law-related articles. *Cf. id.* at 903 (Brieant, J., dissenting) (distinguishing health care periodical and book advising how to avoid probate from the practices of medicine and law).

tion of business activity, and is not rendered any less legitimate merely because the activity involves speech.[71]

In dissent, Judge Brieant agreed with Chief Judge Weinstein that the newsletters were outside the rubric of commercial speech and, therefore, entitled to full first amendment protection against prior restraint.[72] Judge Brieant reasoned that the sale of Lowe's "editorial expression of . . . facts and opinions" was no more commercial speech than the sale of "our most respected daily newspaper."[73] Consequently, the dissent maintained, the case should have been treated as a pure first amendment speech case, with the traditional heavy burden against the constitutional validity of any prior restraint.[74] Judge Brieant viewed the statute as both overinclusive and underinclusive in its coverage,[75] and objected to the injunction sought because it was " 'more extreme than necessary' " and would be illusory and impractical to enforce.[76]

Subsequent Developments: SEC v. Suter *and* SEC v. Wall Street Publishing Institute, Inc.

Four months after the Second Circuit decided the *Lowe* case, the Seventh Circuit reached a similar result in *SEC v. Suter.*[77] In *Suter*, the district court granted the SEC injunctive relief against the publication of false and misleading promotional advertisements of an investment adviser's newsletter.[78] The injunction pre-

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[71] *Id.* at 899, 901. To rely only on subsequent punishment, according to the majority, would be inadequate for the protection of the public. *Id.* at 901-02.

[72] *Id.* at 904 (Brieant, J., dissenting). Judge Brieant was convinced "that the concept of commercial speech [is] now . . . confined to naked advertising and closely related methods of commercial solicitation." *Id.* (Brieant, J. dissenting). The dissent argued that investment opinion should be protected from prior restraint just in the same manner as "political opinion, philosophy or gibberish." *Id.* at 907 (Brieant, J., dissenting).

[73] *Id.* at 904 (Brieant, J., dissenting).

[74] *Id.* at 907 (Brieant, J., dissenting) (citing Bantam Books, Inc. v. Sullivan, 372 U.S. 58, 70 (1963)); *see supra* note 13.

[75] 725 F.2d at 908 (Brieant, J., dissenting). According to Judge Brieant, the majority's construction of the statute was overinclusive in that it permitted the licensing of newsletters that should be given the protection of bona fide newspapers, and underinclusive because Lowe would have been fully protected if he had published the same information in someone else's bona fide newspaper. *Id.* (Brieant, J., dissenting).

[76] *Id.* at 910 & n.4 (Brieant, J., dissenting) (quoting SEC v. Lowe, 556 F. Supp. at 1366).

[77] 732 F.2d 1294 (7th Cir. 1984).

[78] *Id.* at 1298. The advertisements at issue contained misrepresentations about what purportedly "satisfied" subscribers had said about Suter, exaggerated Suter's market experience, and falsified Suter's educational qualifications. *Id.* at 1297.

vented not only the publication of the advertisements, but also the publication of any investment advice, unless defendant Suter allowed the Commission to inspect his records and provided the Commission with copies of all future publications.[79] Rejecting a first amendment argument by Suter, the Court of Appeals for the Seventh Circuit upheld the injunction.[80] The court based its decision solely on commercial speech law and did not even address the possibility that the case involved pure first amendment speech.[81] Applying the test set forth in *Central Hudson*,[82] the *Suter* court held that Suter's speech was unprotected because it was misleading.[83] The court further indicated that the injunction was no broader than necessary to prevent Suter's deception.[84] Thus, without fully considering the implications of enjoining Suter's newsletters along with his advertisements, the Seventh Circuit found no unlawful prior restraint in the SEC injunction.[85]

Most recently, in *SEC v. Wall Street Publishing Institute, Inc.*,[86] the Commission obtained an injunction against the publisher of *Stock Market Magazine*, a monthly magazine devoted to helping investors "make intelligent investment decisions."[87] The Commission alleged that the publisher was operating as an unregistered investment adviser and was involved in various fraudulent and misleading practices,[88] including the publication of ostensibly objective articles that were, in fact, written by press agents of the subject companies.[89] Although the district court did not directly

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[79] *Id.* at 1298. In addition to restrictions placed upon Suter's future publication, the injunction prohibited Suter from employing fraud or deceit in his business, and from offering for sale or selling unregistered securities. *Id.* The injunction also mandated that Suter provide the SEC with a detailed accounting of all funds received by him or his business in connection with securities trading. *Id.*

[80] *Id.* at 1299-1300, 1302.

[81] *See id.* at 1299.

[82] *Central Hudson*, 447 U.S. at 566; *see supra* notes 45-47 and accompanying text.

[83] *Suter*, 732 F.2d at 1299. The court determined that Suter's advertisements "blatantly lie[d] about his experience, education and qualification," and "unashamedly carr[ied] a worthless money-back guarantee." *Id.*

[84] *Id.* at 1299-1300.

[85] *Id.* at 1300, 1302.

[86] 591 F. Supp. 1070 (D.D.C. 1984), *motion for stay pending appeal granted*, [Current] FED. SEC. L. REP. (CCH) ¶ 91,635, at 99,219-20 (D.C. Cir. Aug. 10, 1984).

[87] 591 F. Supp. at 1076.

[88] *Id.* at 1074.

[89] *Id.* at 1076. It was admitted by the defendant publisher that in exchange for printing articles written by and favorable to subject companies, the companies, as a *quid pro quo*, would purchase advertising space in the magazine. *See id.*

address a first amendment challenge, the opinion cited the *Lowe* decision for the broad proposition that the Investment Advisers Act has survived constitutional scrutiny.[90] Thus, the court focused its attention on whether the defendant was entitled to the statutory exemption available to "the publisher of any bona fide newspaper, news magazine or financial publication of general and regular circulation."[91] Holding that the publisher of *Stock Market Magazine* was not entitled to the exemption, and side-stepping the first amendment issue, the court enjoined future publication of the magazine until the publisher registered with the SEC and abided by the Commission's rules for investment advisers.[92] However, the Court of Appeals for the District of Columbia Circuit, citing "the magnitude of the First Amendment interests at stake," has suspended the injunction pending appeal.[93]

Determining the Proper Level of Protection for Investment Advice

It is submitted that the courts in *Lowe*, *Suter*, and *Wall Street Publishing* have underestimated the expansiveness of the Supreme Court's current interpretation of the first amendment. In denying full first amendment protection to impersonal investment advice, the courts have expanded the scope of the commercial speech class to include a medium of communication far removed from any other that the Supreme Court has thus far included.[94] Concededly, the Supreme Court has not yet had an occasion to set forth an authoritative definition of the term "commercial speech."[95] To date, however, all the commercial speech cases de-

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[90] *See id.* at 1080.

[91] Investment Advisers Act of 1940 § 202(a)(11)(D), 15 U.S.C. § 80b-2(a)(11) (1982); *see Wall St. Publishing*, [Current] FED. SEC. L. REP. (CCH) ¶ 91,575, at 98,934-36.

[92] *Wall St. Publishing*, 591 F. Supp. at 1079-81.

[93] [Current] FED. SEC. L. REP. (CCH) ¶ 91,635, at 99,219-20.

[94] Thus far, the Supreme Court has afforded less than full protection only to commercial speech that "has been inextricably intertwined with advertising." *Lowe*, 725 F.2d at 905 (Brieant, J., dissenting); *see supra* notes 32-47 and accompanying text; *infra* notes 97-99 and accompanying text.

[95] *See* Alderman, *Commercial Entities' Noncommercial Speech: A Contradiction in Terms*, 1982 UTAH L. REV. 731, 741. The Court has characterized commercial speech as that which does "no more than propose a commercial transaction," Bolger v. Youngs Drug Prods. Corp., 463 U.S. 60, ____, 103 S. Ct. 2875, 2880 (1983) (quoting Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations, 413 U.S. 376, 385 (1973)), and as "expression related solely to the economic interests of the speaker and its audience," *Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n*, 447 U.S. 557, 561 (1980).

cided by the Supreme Court have involved pure commercial advertising.[96]

At least three Justices presently on the Supreme Court have expressed a reluctance to expand the category of commercial speech beyond advertising.[97] This view has been adopted by at least two federal courts, which have inferred that the Supreme Court intended to limit the class of commercial speech exclusively to advertisements.[98] Several commentators likewise have discussed the commercial speech cases under the assumption that commercial speech is coterminous with advertising.[99] Other commentators, however, advocate a much broader scope for the concept of commercial speech.[100] One suggested interpretation would include "*any* speech by a commercial entity,"[101] a definition that has been re-

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[96] *See, e.g.*, Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations, 413 U.S. 376, 385 (1973). The *Pittsburgh Press* Court characterized the advertisements at issue in that case as "classic examples of commercial speech." *Id.*

[97] *See Central Hudson*, 447 U.S. at 573 (Blackmun, J., concurring); *id.* at 579-80 (Stevens, J., concurring). Justice Brennan joined in both of these concurring opinions. Justice Stevens warned that "[b]ecause 'commercial speech' is afforded less constitutional protection . . . , it is important that the commercial speech concept not be defined too broadly lest speech deserving of greater constitutional protection be inadvertently suppressed." *Id.* at 579 (Stevens, J., concurring). In addition to Justices Stevens, Blackmun, and Brennan, Justice Rehnquist has made clear his disapproval of the entire idea of protection for commercial speech. *See supra* note 37 and accompanying text.

[98] *See* Ad World, Inc. v. Township of Doylestown, 672 F.2d 1136, 1140 (3d Cir.) (community newspaper devoted almost exclusively to advertising given full first amendment protection), *cert. denied*, 456 U.S. 975 (1982); SEC v. Lowe, 556 F. Supp. 1359, 1366-67 (E.D.N.Y. 1983) (investment newsletter is probably outside the rubric of commercial speech, and therefore deserving of full first amendment protection), *rev'd*, 725 F.2d 892 (2d Cir.), *cert. granted*, 105 S. Ct. 81 (No. 83-1911) (1984); *see also Lowe*, 725 F.2d at 904 (Brieant, J., dissenting) (commercial speech limited to "naked advertising" and solicitation).

[99] *See, e.g.*, J. NOWAK, R. ROTUNDA & J. YOUNG, *supra* note 1, at 923 (describing commercial speech as "speech of any form that advertises a product or service for profit or for business purposes"); Barrett, *"The Unchartered Area"—Commercial Speech and the First Amendment*, 13 U.C.D. L. REV. 175, 205 (1980) (line distinguishing pure speech from commercial speech should be between general public interest advertising and advertisement for particular goods); Farber, *Commercial Speech and First Amendment Theory*, 74 NW. U.L. REV. 372, 381, 386 (1979) (subject matter of commercial speech is product or service, and speaker is the seller).

[100] *See, e.g.*, Alderman, *supra* note 95, at 731, 744 (all speech by commercial entity should be classified as commercial speech); Comment, *First Amendment Protection for Commercial Advertising: The New Constitutional Doctrine*, 44 U. CHI. L. REV. 205, 234 (1976) (favoring an overinclusive definition of commercial speech).

[101] Alderman, *supra* note 95, at 744. Alderman suggests that a "broad, inclusive definition" of commercial speech would "simplify the process." *Id.* Thus, "any and all speech of a commercial entity" should be the definition, *id.* at 732, with "commercial entity" likewise broadly defined to include any business whose existence is based on profit, *see id.* at 744 & n.51.

jected by the Supreme Court.[102] Before commercial speech received even limited protection, Justice Douglas referred to the unprotected class as "speech directed at private economic decisionmaking,"[103] which clearly includes more than advertisement. In *Lowe*, the Second Circuit expressed a view consistent with that of Justice Douglas when it rejected the proposition that commercial speech is limited to advertising.[104]

It is suggested that commercial speech should not include third-party commentary by people who, though selling their advice, have no economic interest in the outcome of the particular transactions about which they report. Although the Supreme Court may have intended to include within the class of commercial speech more than pure commercial advertising, it is suggested that the Court did not intend to include all speech by commercial entities, or all speech concerning private economic decisionmaking. The underlying rationale of limited protection for commercial speech suggests that the concept was intended to be narrower.[105] The investment adviser's desire for profit cannot be controlling, for profit is also the primary motive of many book authors, newspaper publishers, and even political pamphleteers.[106] Similarly, speech is not deemed "commercial" merely because the speaker is a commercial entity,[107] or because the speech relates to commercial matters.[108] At the very least, it is suggested, "commercial speech"

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[102] *See* First Nat'l Bank of Boston v. Bellotti, 435 U.S. 765, 784 (1978). *Bellotti* involved a challenge to a Massachusetts statute that prohibited specific business corporations from making expenditures or contributions to influence popular voting unless the subject matter of the vote materially affected the corporation. *Id.* at 767-70. The appellant corporations wished to spend money to influence voting on a referendum issue that did not materially affect them. *See id.* at 769. The speech proffered by the corporation, the Court held, was "at the heart of the First Amendment's protection." *Id.* at 776. The Court continued: "The inherent worth of the speech in terms of its capacity for informing the public does not depend upon the identity of its source, whether corporation, association, union, or individual." *Id.* at 777.

[103] Dun & Bradstreet, Inc. v. Grove, 404 U.S. 898, 905 (1971) (Douglas, J., dissenting).

[104] *See Lowe*, 725 F.2d at 900-01 (holding that investment advice newsletters are within the scope of commercial speech).

[105] *See* Ad World, Inc. v. Township of Doylestown, 672 F.2d 1136, 1140 (3d Cir.), *cert. denied*, 456 U.S. 975 (1982); SEC v. Lowe, 556 F. Supp. 1359, 1366-67 (E.D.N.Y. 1983), *rev'd*, 725 F.2d 892 (2d Cir. 1984), *cert. granted*, 105 S. Ct. 81 (1984) (No. 83-1911).

[106] *See supra* note 34 and accompanying text.

[107] *See supra* note 102 and accompanying text.

[108] *See* Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc., 425 U.S. at 748, 761 (1976). If speech were deemed commercial merely because it concerned commercial matters, publications like *Forbes* and *The Wall St. Journal* would be given less than full first amendment protection. Such a result, it is submitted, would make a mockery

should not include opinions about transactions to which the speaker is not a potential party. Thus, it is submitted, since commercial speech is given less protection because of the speaker's extensive knowledge and economic self-interest,[109] a useful definition would include all speech that proposes a commercial transaction and is made by a potential party to that particular transaction.[110] Such a definition would permit regulation of speech that goes beyond pure advertisement, but would protect third-party commentators who lack economic self-interest in consummating particular transactions.[111]

If subscription newsletters and investment advice periodicals are to be accorded full first amendment protection, it is suggested that the Investment Advisers Act is facially invalid. Courts have shown less tolerance of licensing schemes similar to SEC registration requirements than of any other method of speech restriction.[112] The Supreme Court has admonished that it "strikes at the very heart" of the first amendment to require a license from the government as a condition of exercising freedom of speech or press,[113] particularly when, as with the SEC, the discretion of the

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of freedom of speech.

[109] *Central Hudson*, 447 U.S. at 564 n.6; *see also Virginia Board*, 425 U.S. at 771-72 n.24 (commercial speech is verifiable by the disseminator).

[110] *See* Baker, *supra* note 37, at 35. Although Baker argues that commercial speech deserves no protection, *see id.* at 3, he nevertheless limits the category of commercial speech to that which "is directed towards influencing private commercial transactions *and is made by a potential party to such transactions*," *id.* at 35 (emphasis added). Another commentator has intimated that if the author of a communication is not the seller of the product or service involved, the communication should be eligible for full first amendment protection. *See* Rotunda, *The Commercial Speech Doctrine in the Supreme Court*, 1976 U. ILL. L.F. 1080, 1090; *see also* Farber, *supra* note 99, at 386 (one difference between commercial speech and pure speech is that the former is spoken by the seller).

[111] *See Central Hudson*, 447 U.S. at 564 n.6; *Virginia Board*, 425 U.S. at 771-72 n.24. Of course, if a third-party commentator has an economic interest in the transactions about which he reports, any false or misleading statements or omissions, for example "scalping, would be actionable under § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j (1982), and rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5 (1984). *See, e.g.*, Zweig v. Hearst Corp., 594 F.2d 1261, 1266 (9th Cir. 1979).

[112] *See supra* note 14. Soon after the securities acts were passed, the Supreme Court acknowledged that the SEC is a licensing authority: "[T]he filing of the registration statement is in effect an *ex parte* application for a license to use the mails and the facilities of interstate commerce for the purposes recognized by the act." Jones v. SEC, 298 U.S. 1, 22 (1936).

[113] Schneider v. State, 308 U.S. 147, 164 (1939); *see supra* note 14. In *Schneider*, the Court invalidated a licensing scheme because it rendered "liberty to communicate . . . depend[ent] upon the exercise of the officer's discretion." 308 U.S. at 164. The Court continued:

licensing agency in determining who is fit to publish is limited only by a vague "in the public interest" standard.[114] Moreover, courts rarely accept the prevention of anticipated wrongdoing as a justification for enjoining speech,[115] especially when the prediction is based upon speculative assessments of the speaker's past misconduct.[116] The SEC unquestionably has a compelling interest in

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> To require a censorship through license which makes impossible the free and unhampered distribution of pamphlets strikes at the very heart of the constitutional guarantees.
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> *Conceding that fraudulent appeals may be made . . .*, we hold a municipality cannot, for this reason, require all who wish to disseminate ideas to present them first to police authorities for their consideration and approval, with a discretion in the police to say some ideas may, while others may not, be carried to the homes of citizens; some persons may, while others may not, disseminate information from house to house. Frauds may be denounced as offenses and punished by law. . . . If it is said that these means are less efficient and convenient . . . , the answer is that considerations of this sort do not empower a municipality to abridge freedom of speech and press.

Id. (emphasis added). Thus, freedom of speech cannot be conditioned upon obtaining a license, even if the government asserts the interest of preventing fraud. *See id.* Even assuming impersonal investment newsletters are pure commercial speech—no different from advertisement—the Supreme Court has upheld bans on such speech only when they are inherently misleading or susceptible to fraud and overreaching. *See* Friedman v. Rogers, 440 U.S. 1, 12-13 (1979) (use of trade names in the practice of optometry); Ohralik v. Ohio State Bar Ass'n, 436 U.S. 447, 464-65 (1978) ("ambulance chasing" by attorney); *see also In re* R.M.J., 455 U.S. 191, 203 (1982) (misleading professional advertising may be regulated).

[114] *See* 15 U.S.C. § 80b-3(e), (f), (h) (1982). "In the public interest" provisions are found in subsections 203(e), (f) and (h) of the Investment Advisers Act. *See id.* Such a standard, it is submitted, is not sufficiently narrow to withstand first amendment scrutiny. *Cf.* Shuttlesworth v. City of Birmingham, 394 U.S. 147, 149-51 (1969) (city commission guided by statutory standard of "the public welfare, peace, safety, health, decency, good order, morals or convenience"); Staub v. Baxley, 355 U.S. 313, 322 (1958) (in decisions on permits, mayor and city council shall consider "effects upon the general welfare of citizens"). As the *Shuttlesworth* Court held, such a standard falls "squarely within the ambit of the many decisions of this Court . . . holding that a law subjecting the exercise of First Amendment freedoms to the prior restraint of a license, without narrow, objective, and definite standards to guide the licensing authority, is unconstitutional." 394 U.S. at 150-51.

[115] *See* Consolidated Edison Co. v. Public Serv. Comm'n, 447 U.S. 530, 543 (1980) (invalidating commission order prohibiting inclusion of public issue inserts in monthly utility bills).

[116] *See, e.g.*, Vance v. Universal Amusement Co., 445 U.S. 308, 315-16 (1980) (per curiam) (extremely heavy burden on prior restraint of obscenity when it is based upon past communication); Near v. Minnesota, 283 U.S. 697, 711 (1931) (all nine prior editions of newspaper contained malicious, scandalous, and defamatory material in violation of statute); Entertainment Concepts, Inc. v. Maciejewski, 631 F.2d 497, 506 (7th Cir. 1980) (use of prior restraint based upon past conduct is precisely what was condemned in *Near*), *cert. denied*, 450 U.S. 919 (1981). As stated succinctly by Judge Goettel of the Southern District of New York:

> A regulatory scheme under which a license necessary to the exercise of First Amendment rights may be denied or revoked because of a past conviction . . .

preventing fraud in the securities markets; however, similar compelling interests in other contexts have not justified the use of prior restraint.[117] It is therefore suggested that, if it is to be interpreted consistently, the first amendment should limit the Commission, as it does other agencies, to subsequent punishment of unlawful speech.

FIRST AMENDMENT ISSUES RAISED BY THE 1933 AND 1934 ACTS

Background Issues

The issues presented in *Lowe*, *Suter*, and *Wall Street Publishing* invite inquiry into the possibility of first amendment problems with SEC regulation of public offerings under the Securities Act of 1933 (1933 Act)[118] and of securities trading under the Securities Exchange Act of 1934 (1934 Act).[119]

Section 5 of the 1933 Act prohibits the use of the mails or interstate commerce for the purpose of selling or offering to sell securities unless the issuer is registered with the SEC.[120] As does

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> constitutes a system of prior restraint. [It is] impermissible to deny a person the right to exercise a fundamental freedom (by denying a license . . .) solely upon the ground that that person has suffered a prior criminal conviction . . .
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> . . . .
>
> The City may not . . . utilize its licensing power to deprive a party of the right to exercise a constitutionally protected right solely because of past misconduct.

Natco Theatres, Inc. v. Ratner, 463 F. Supp. 1124, 1129-30 (S.D.N.Y. 1979). In *Natco*, the statute allowed revocation or denial of a license only for crimes directly related to the license sought. *Id.* at 1130-31. By contrast, the Investment Advisers Act sweeps much more broadly, allowing prior restraint based upon past misconduct outside one's business as an investment adviser, and even outside one's activity in any securities-related endeavor. *See* 15 U.S.C. § 80b-3(e)(2) (1982).

[117] *See, e.g.*, Nebraska Press Ass'n v. Stuart, 427 U.S. 539, 562-63 (1976) (compelling interest in ensuring a fair trial for criminal defendant); New York Times Co. v. United States, 403 U.S. 713, 714 (1971) (per curiam) (compelling interest in national security); *see infra* note 154 and accompanying text.

[118] 15 U.S.C. §§ 77a-77aa (1982).

[119] *Id.* §§ 78a-78kk.

[120] *Id.* § 77e. Section 5(c) of the 1933 Act provides:

> It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order . . . .

Id. § 77e(c). The concept of "offer to sell" is defined broadly to include, with exceptions, "every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security." *Id.* § 77b(3). This definition "goes well beyond the common law concept of an offer." 1 L. LOSS, SECURITIES REGULATION 181 (2d ed. 1961) (citing Carl M. Loeb, Rhoades &

the Investment Advisers Act, the 1933 Act provides for injunctive relief and criminal sanctions to assist the Commission in preventing unregistered public offers, sales, or advertisements of securities.[121] Thus, under the 1933 Act, an issuer's right to promote a public offering of securities is conditioned upon the issuer's success in obtaining an "effective" license from the Commission.[122] The 1934 Act contains similar registration requirements for transactions involving the trading of securities.[123]

Unlike the Investment Advisers Act, the 1933 and 1934 Acts authorize the Commission not only to deny and revoke registrations, but also to censor documents before they are made public.[124] The 1933 Act, for example, requires as part of the registration process the filing with the Commission of a copy of the issuer's prospectus, the primary means by which the issuer solicits public purchases of his securities.[125] The Commission may prevent a registration from becoming effective until the Commission is satisfied with the content of the prospectus.[126] Through the use of

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Co., Securities Exchange Act Release No. 5870, at 8 (1959)). *See generally* Publication of Information Prior to or After the Effective Date of a Registration Statement, Securities Act Release No. 3844 (Oct. 8, 1957) (outlining a number of examples to illustrate the Commission's view that the statute includes any publicity pertaining to the sale of a security that "may in fact contribute to conditioning the public mind or arousing public interest in the issuer"). The word "prospectus" similarly has a very broad definition. *See infra* note 125. Thus, the Commission has statutory authority to license the dissemination of an extraordinarily broad range of communications.

[121] *See* 15 U.S.C. § 77t(b) (1982).

[122] *See id.* §§ 77g-77h. Sections 7 and 8 of the 1933 Act provide methods by which the Commission may give notification that an issuer's registration statement is deficient, and deny effectiveness of the statement until the deficiencies are cured. *See id.* The Supreme Court has acknowledged that the registration process is a licensing scheme. *See* Jones v. SEC, 298 U.S. 1, 22 (1936).

[123] *See, e.g.*, 15 U.S.C. §§ 78*l*, 78o (1982). Under the 1934 Act, a registration may be suspended, revoked, or denied by the Commission, *see id.* § 78l(j), and violators of the 1934 Act are subject to injunction and criminal sanction, *see id.* §§ 78u(d), 78ff.

[124] *See infra* notes 125-35 and accompanying text.

[125] D. RATNER, SECURITIES REGULATION 37 (1980); *see* 15 U.S.C. § 77b(10) (1982). Section 2 of the 1933 Act defines "prospectus" broadly as "any prospectus, notice, circular, advertisement, letter, or communication, written or by radio or television, which offers any security for sale or confirms the sale of any security." 15 U.S.C. § 77b(10) (1982). It "is no more than an advertisement for the sale of securities." Goodale, *supra* note 3, at 4, col. 1. As such, it is substantially similar to the commercial speech involved in cases considered by the Supreme Court. *See supra* notes 32-47 and accompanying text.

[126] *See, e.g.*, Goodale, *supra* note 3, at 1, col. 1; Schneider & Manko, *Going Public—Practice, Procedure and Consequences*, 15 VILL. L. REV. 283, 293-94 (1970) (Commission gets the "last word").

"stop orders,"[127] "deficiency letters,"[128] and other means of inducement and chilling,[129] the SEC is able to ensure that all documents concerning public offers conform to the content standards of the Commission.[130] Section 14 of the 1934 Act,[131] and the SEC rules

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[127] *See* 15 U.S.C. § 77h(d) (1982). Section 8(d) of the 1933 Act provides, in pertinent part:

> If it appears to the Commission at any time that the registration statement includes any untrue statement of a material fact or omits to state any material fact required to be stated therein or necessary to make the statements therein not misleading, the Commission may . . . issue a stop order suspending the effectiveness of the registration statement. When such statement has been amended in accordance with such stop order, the Commission shall so declare and thereupon the stop order shall cease to be effective.

Id. See generally Oklahoma-Texas Trust v. SEC, 100 F.2d 888, 891-93, 896 (10th Cir. 1939) (affirming SEC use of stop order against materially deficient registration statement of mineral leasing trust). Similarly, section 8(b) of the 1933 Act provides, in pertinent part:

> If it appears to the Commission that a registration statement is on its face incomplete or inaccurate in any material respect, the Commission may . . . issue an order prior to the effective date of registration refusing to permit such statement to become effective until it has been amended in accordance with such order.

15 U.S.C. § 77h(b) (1982). Commission procedure, moreover, places the burden of proof on the registrant to show cause why a stop order should not be issued. *See* Jones v. SEC, 298 U.S. 1, 18 (1936). The registrant acts "at his peril" until he has sustained this burden. *Id.*

[128] *See* Schneider & Manko, *supra* note 126, at 293-94 (SEC nearly always finds deficiencies, and usually gets the last word).

[129] *See* Karmel, *supra* note 3, at 2, col. 5. One obvious chilling effect is the time factor; if an issuer wishes to avoid all delay in the offering of securities, presumably including the desire to have his registration effectiveness "accelerated" pursuant to section 8(a) of the 1933 Act, 15 U.S.C. § 77h(a) (1982), the issuer will choose to stay clear of any possible deficiencies, in effect self-censoring its documents. *See* Schneider & Manko, *supra* note 126, at 293. Two commentators on the process note that the fear of civil liability in itself can cause self-censorship:

> With the view toward protection against liability, there is a tendency to resolve all doubts against the company and to make things look as bleak as possible. . . . [E]xperienced counsel, guided at least in part by their knowledge of the SEC staff attitudes, traditionally lean to a very conservative presentation. They avoid glowing adjectives, subjective evaluations and predictions about the future. The prospectus is limited to provable statements of historic fact. The layman frequently complains that all the glamor and romance has been lost.

Id. The threat of criminal sanction is a further element of chilling, particularly because SEC procedure can, in effect, shift the burden of proof against the issuer. *See supra* note 127. The issuer's fear of adverse publicity has also been cited as an effective Commission weapon. *See, e.g.*, Freedman, *A Civil Libertarian Looks at Securities Regulation*, 35 OHIO ST. L.J. 280, 284 (1974); Gellhorn, *Adverse Publicity by Administrative Agencies*, 86 HARV. L. REV. 1380, 1406 n.107 (1973); Lacy, *Adverse Publicity and SEC Enforcement Procedure*, 46 FORDHAM L. REV. 435, 449-51 (1977). Lastly, it has been argued that companies do not assert first amendment rights because they wish to avoid getting "on the wrong side" of the SEC. *See* Lewin, *supra* note 3, at D2, col. 3 (quoting Floyd Abrams).

[130] Joseph H. Sharlitt, attorney for the Wall St. Publishing Institute, Inc., referring to the Investment Advisers Act as a "classic case of prior restraint," protested that "[y]ou can't publish until you are not only registered but comply with their rules." Noble, *supra* note 3,

promulgated thereunder,[132] provide another salient illustration of the censorial function of the Commission. Under section 14, materials relating to proxy solicitations and tender offers must be filed with the SEC before they are made public.[133] These materials are subject to detailed content regulation,[134] and the Commission is empowered to ensure strict adherence to the regulations.[135]

The significant constitutional distinction between the Investment Advisers Act and the 1933 and 1934 Acts, however, is that the latter two do not regulate anything that is arguably pure first amendment speech. Communications subject to SEC licensing and censorship under the 1933 and 1934 Acts may properly be classified as commercial speech.[136] Although distinguishable from the

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at D2, col. 1.

[131] 15 U.S.C. § 78n (1982).

[132] 17 C.F.R. §§ 240.14a-1 to 240.14f-1 (1984).

[133] 15 U.S.C. § 78n (1982). Section 14(a) of the 1934 Act, which regulates the solicitation of proxies, provides:

> It shall be unlawful for any person, by the use of the mails or by any means or instrumentality of interstate commerce or of any facility of a national securities exchange or otherwise, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors, to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any [registered] security . . . .

Id. § 78n(a). Section 14(d), added in 1968 by the Williams Act, Pub. L. No. 90-439, § 3, 82 Stat. 454, 456 (1968), makes it unlawful to use the mails, interstate commerce, or a national securities exchange "to make a tender offer for, or a request or invitation for tenders of, any class of any [registered] equity security," if upon consummation of the deal the offeror would be the beneficial owner of more than 5% of that class, unless the offeror has filed with the Commission a copy of the offer or request or invitation. 15 U.S.C. § 78n(d)(1) (1982).

> All requests or invitations for tenders or advertisements making a tender offer or requesting or inviting tenders of such a security shall be filed . . . and shall contain such . . . information . . . as the Commission may by rules and regulations prescribe.

Id. Section 14(e) gives the Commission broad authority to prevent the making of any false or misleading statements or omissions in any of the documents filed under § 14. *See id.* § 78n(e).

[134] *See, e.g.*, 17 C.F.R. §§ 240.14a-3, 240.14a-101, 240.14a-102 (1984) (content requirements for proxy materials); *id.* § 240.14d-6 (content requirements for tender offer materials). Rule 14a-9, which regulates proxy solicitations, sets forth illustrations of what "may be misleading," including predictions about future market values, defamatory opinions, and predictions about the results of the solicitation. *Id.* § 240.14a-9.

[135] The Commission may obtain injunctions and writs of mandamus from federal district courts, and may threaten potential violators with criminal sanctions. *See* 15 U.S.C. § 78u(d), (e) (1982).

[136] *See, e.g., In re* W.T. Grant Co., [1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,636, at 98,407-08 (Bankr. S.D.N.Y. Sept. 16, 1980) (proxy solicitation letter is commercial speech); Goodale, *supra* note 3, at 4, col. 1 (prospectus is nothing more than an

"classic examples" of commercial speech—product and service advertisements[137]—promotional information about securities fits within the parameters of the commercial speech concept.[138] Prospectuses, proxy solicitations, and communications about tender offers are all propositions of commercial transactions, and all relate to the economic interests of both the speaker and the audience.[139] More significantly, they are communicated by potential parties to the proposed transaction—that is, by persons who possess the "extensive knowledge" and "economic self-interest" that renders commercial speech "more durable" and less likely to be chilled than other forms of speech.[140] Under current first amendment law, therefore, these forms of communication deserve only the limited protection of a commercial speech analysis.[141]

Application of the Central Hudson *Test*

Since the 1933 and 1934 Acts regulate only commercial speech, the proper test for their constitutional validity is the four-part analysis set forth in *Central Hudson Gas & Electric Corp. v. Public Service Commission.*[142] As it is lawful to effectuate transactions in securities, and, because advertisements and solicitations to buy and sell securities are neither generally nor inherently misleading,[143] the first prong of the *Central Hudson* test is satisfied. The

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advertisement).

[137] *See* Pittsburgh Press Co. v. Pittsburgh Comm'n on Human Relations, 413 U.S. 376, 385 (1973).

[138] *See supra* notes 94-111 and accompanying text.

[139] *See* Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n, 447 U.S. 557, 561-62 (1980); *In re* W.T. Grant Co., [1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,636, at 98,407-08 (Bankr. S.D.N.Y. Sept. 16, 1980).

[140] *See Central Hudson*, 447 U.S. at 564 n.6; Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc., 425 U.S. 748, 771-72 n.24 (1976).

[141] *See infra* notes 142-54 and accompanying text.

[142] 447 U.S. 557, 566 (1980); *see supra* notes 45-47 and accompanying text.

[143] There is some difficulty satisfying the "not misleading" requirement of the *Central Hudson* test, since the Commission surely would assert that it prohibits only false, misleading, and fraudulent speech. However, the Commission licenses and censors *all* speech about securities, scrutinizing the true and accurate along with the false and misleading. *See supra* notes 118-35 and accompanying text. Unless it is assumed that speech about securities is inherently misleading, *cf.* Friedman v. Rogers, 440 U.S. 1, 12-13 (1979) (use of trade name in practice of optometry is inherently deceptive); Ohralik v. Ohio State Bar Ass'n, 436 U.S. 447, 464-65 (1978) ("ambulance chasing" by an attorney is inherently susceptible to overreaching), it is submitted that the SEC clearly regulates speech that is not misleading. *Cf.* Smith v. California, 361 U.S. 147, 153-54 (1959) (fear of subsequent liability for obscenity leads to prior restraint in the form of self-censorship by all publishers). *But see In re* W.T. Grant Co., [1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,636, at 98,407 (Bankr.

Commission undoubtedly fulfills the second requirement of the test by asserting the substantial governmental interest in preventing fraud and other abuses in the securities markets.[144] When the Commission encroaches upon first amendment rights, however, any interference with free speech must directly advance the asserted governmental interest and be no more restrictive than necessary.[145] Thus, the third and fourth parts of the *Central Hudson* analysis present the most serious challenges to the constitutionality of SEC licensing and censorship under the 1933 and 1934 Acts.

Although the registration and disclosure requirements of the securities laws originally were enacted to advance the governmental interest in preventing securities fraud and promoting full and fair disclosure,[146] recent commentary and research have challenged the continuing validity of these bases for SEC oversight.[147] Thus,

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S.D.N.Y. Sept. 16, 1980) (granting injunction of proxy solicitation letter).

[144] *See, e.g.*, SEC v. Capital Gains Research Bureau, 375 U.S. 180, 186 (1963). The very purposes of the 1933 and 1934 Acts, as stated by their respective preambles, are to "provide full and fair disclosure," "to prevent frauds," 48 Stat. 74, 74 (1933), and "to prevent inequitable and unfair practices," 48 Stat. 881, 881 (1934).

[145] *Cf. Central Hudson*, 447 U.S. at 569-72 (invalidating ban on promotional advertising by electric utility as more restrictive than necessary).

[146] *See supra* note 144.

[147] *See, e.g.*, G. STIGLER, THE CITIZEN AND THE STATE: ESSAYS ON REGULATION 28-29, 78-99 (1975); Benston, *An Appraisal of the Costs and Benefits of Government-Required Disclosure: SEC and FTC Requirements*, 41 L. & CONTEMP. PROBS., Summer 1977, at 30, 42-54; Kripke, *The Myth of the Informed Layman*, 28 BUS. LAW. 631, 631-34 (1973). It has been argued that the disclosure laws have assured no more information for purchasers than would an unregulated market. *See, e.g.*, H. KRIPKE, THE SEC AND CORPORATE DISCLOSURE: REGULATION IN SEARCH OF A PURPOSE 117-33 (1979); Benston, *supra*, at 51-53; Lothian, *The Role of Government in the Securities Market*, 33 U. MIAMI L. REV. 1587, 1591-95 (1979). Indeed, unlike the era during which the securities laws were enacted, the modern market is dominated by sophisticated individual and institutional investors. *See* Wolfson, *A Critique of the Securities and Exchange Commission*, 30 EMORY L.J. 119, 134-37 (1981). Those individuals who buy and sell securities, it has been argued, are at least as sophisticated in the securities markets as are consumers in the markets of other industries subject to much less regulation. *See* Lothian, *supra*, at 1594; Stephan, *supra* note 3, at 94-95. For example, it has been argued that SEC regulation of proxy contests has underestimated the intelligence of shareholders:

> A proxy contest is much like a political contest. There are exaggerated denunciations of the opposition, lofty exaltation of oneself and the always present tendency to state issues in terms of black and white when many of us know they are often a murky gray. But the American people are used to this type of bombast in electioneering and they are not easily taken in by it. . . . [T]he American public [should not] be bored to death by speeches and statements by contestants written by their lawyers, and reading like a marine insurance policy.

Stephan, *supra* note 3, at 94-95.

It has been argued further that expansion of SEC regulation has rendered the market so inefficient that long run costs have been inflated and opportunities for corporate mischief

the Commission may fail to satisfy even the third requirement of the *Central Hudson* test, which requires that commercial speech regulation directly advance the governmental interest involved.[148]

Assuming the third part of the analysis is satisfied, however, SEC regulation must clear the fourth hurdle of *Central Hudson*: It must be no more extensive than necessary to achieve the governmental interest alleged.[149] This fourth prong of *Central Hudson* adopts a test that is, it is submitted, indistinguishable from the least-restrictive-alternative test used in analyzing encroachments on pure first amendment speech.[150] Thus, it is suggested that the constitutional validity of SEC prior restraint is highly questionable, since the Court's injection of a form of the least-restrictive-alternative test into the commercial speech arena would be inconsistent with anything but the traditional "heavy presumption against" prior restraint.[151]

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and incompetency have been opened. *See* Wolfson, *supra*, at 134, 157; *see also* H. KRIPKE, *supra*, at 106-14 (examining the costs of excessive SEC regulation); Lothian, *supra*, at 1588, 1590, 1594, 1595 (noting costliness of conforming to Commission rules and regulations). Thus, regulation of communication about securities may be unnecessary, and perhaps contrary to the public interest. *See* Lothian, *supra*, at 1588, 1595; Wolfson, *supra*, at 157. For a recent exposition of the argument that mandatory disclosure has been unhelpful and inefficient, see Easterbrook & Fischel, *Mandatory Disclosure and the Protection of Investors*, 70 VA. L. REV. 669, 692-96, 707-14 (1984).

[148] *Central Hudson*, 447 U.S. at 566.

[149] *Id.*

[150] *See* Barrett, *supra* note 99, at 199 (suggesting, even before *Central Hudson* was decided, that adoption of the least-restrictive-alternative test may be "constitutionally compelled"); *see also Central Hudson*, 447 U.S. at 591 (Rehnquist, J., dissenting) (protection of commercial speech is now "virtually indistinguishable from that of noncommercial speech); J. NOWAK, R. ROTUNDA & J. YOUNG, *supra* note 1, at 923 (commercial speech now seems to receive full first amendment protection). The least-restrictive-alternative test requires that, where government regulation impedes freedom of speech, the regulation must be no more restrictive of speech than necessary. *See, e.g.*, Martin v. City of Struthers, 319 U.S. 141, 148-49 (1943) (striking down ordinance that prohibited knocking on doors and ringing doorbells to deliver handbills because there were less restrictive alternatives available); Lovell v. City of Griffin, 303 U.S. 444, 451 (1938) (license requirement for distribution of leaflets was too restrictive in that it reached all kinds of literature); *cf.* United States v. Robel, 389 U.S. 258, 267-68 (1967) (statute that interferes with first amendment freedom of association must be the least drastic alternative); Jacob Siegel Co. v. FTC, 327 U.S. 608, 612 (1946) (use of trade name is a valuable business asset which, even if deceptive, should not be destroyed if there exists a less restrictive alternative of requiring qualifying language to clarify the deception).

[151] *See* New York Times Co. v. United States, 403 U.S. 713, 714 (1971) (per curiam) (quoting Bantam Books, Inc. v. Sullivan, 372 U.S. 58, 70 (1963)); *supra* note 13.

Some of the Court's commercial speech opinions have suggested that the rule against prior restraint might not apply to regulation of commercial speech. *See, e.g., Central Hudson*, 447 U.S. at 571 n.13 (quoting *Virginia Board*, 425 U.S. at 771-72 n.24). This aspect of the lower level of protection afforded commercial speech seems at the very least to be

The ultimate question, it is suggested, is whether SEC regulation of speech is to be scrutinized under the standards applicable to other regulation of speech, or whether the Commission is to receive preferential treatment. In other contexts, prior restraints in the forms of licensing and censorship have failed to satisfy the least-restrictive-alternative test,[152] a test that now appears to apply not only to restrictions on pure speech, but also to those on commercial speech. Courts consistently have stated that the proper method of monitoring speech—even speech wholly outside first amendment protection—is not prior restraint, but subsequent punishment.[153] Of course, damages suffered by those misled by communications about securities should not be trivialized. It is submitted, however, that unless courts are inclined to give greater priority to the prevention of such financial injury than to the prevention of the types of injury inflicted by other forms of destructive speech,[154] the SEC should not be given preferential treatment;

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greatly undermined by the *Central Hudson* requirement that restrictions on commercial speech be no more extensive than necessary. 447 U.S. at 566. Thus, it is submitted that by incorporating into its commercial speech analysis the least-restrictive-alternative test, the Court has negated its suggestions that the rule against prior restraints might not apply to commercial speech regulation.

[152] *See, e.g.*, Shuttlesworth v. City of Birmingham, 394 U.S. 147, 150-56 (1969) (although time, place, and manner regulation on the use of public streets is permissible, it may not be done in a way that unnecessarily interferes with first amendment rights); Smith v. California, 361 U.S. 147, 153-55 (1959) (imposition of absolute criminal liability for mere possession, without scienter, of obscene material interferes too much with freedom of speech); Schneider v. State, 308 U.S. 147, 160-65 (1939) (licensing scheme is too restrictive of first amendment rights); *see also supra* notes 13-15 and accompanying text (discussing judicial distaste for licensing, censorship, and other prior restraints).

[153] *See, e.g.*, Bantam Books, Inc. v. Sullivan, 372 U.S. 58, 69-70 (1963) (obscenity); Near v. Minnesota, 283 U.S. 697, 713-17 (1931) (defamation).

[154] Our judicial system, wisely or unwisely, has adopted an extraordinarily expansive construction of a preferred first amendment. *See supra* notes 1 & 13-15 and accompanying text. As a result, our system tolerates the publication of various forms of offensive speech.

For example, courts refuse to enjoin the publication of defamatory speech despite the destructive effects the publication might have on the lifestyle of the victim. *See, e.g.*, Near v. Minnesota, 283 U.S. 697, 713-17 (1931). Similarly, courts refuse to enjoin racist group defamation, despite its perpetuation of a legacy of prejudice, discrimination, and hostility against its targets. *See, e.g.*, Sambo's Restaurants, Inc. v. City of Ann Arbor, 663 F.2d 686, 694-95 (6th Cir. 1981) (conceding that the use by a restaurant of the name "Sambo's" is a "pernicious racial stereotype of blacks as inferior," but holding that the right to use the name is protected commercial speech and could not be waived by contract with city); Collin v. Smith, 578 F.2d 1197, 1202-06 (7th Cir.) (conceding that proposed Nazi demonstration would "seriously disturb" the residents of predominantly Jewish village in which it was scheduled, but holding that ordinances prohibiting demonstration were unconstitutional), *cert. denied*, 439 U.S. 916 (1978). Persuasive arguments have been made that the suppression of such speech is warranted, or at least permissible. *See* State Div. of Human Rights v.

the Commission should be limited to punishment of speech that is proved false or misleading after publication.

CONCLUSION

The purpose of this Note has been to analyze the system of securities regulation under the first amendment as it is currently interpreted by the Supreme Court. The *Lowe*, *Suter*, and *Wall Street Publishing* cases have helped bring to the forefront the fundamental conflict between an expansive construction of the free speech clause and the extraordinary regulatory power exercised by the SEC. This Note has suggested that, although first amendment issues in securities law have been litigated only recently, SEC restriction of speech is pervasive, and no longer can be ignored. In one of the first decisions to limit SEC authority, the Supreme Court cautioned against permitting such administrative agencies "gradually to extend their powers by encroachments—even petty encroachments—upon the fundamental rights."[155] It would behoove courts to heed that warning today when evaluating the constitutionality of SEC prior restraint.

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McHarris Gift Center, 52 N.Y.2d 813, 814-16, 418 N.E.2d 393, 393-94, 436 N.Y.S.2d 878, 878-79 (1980) (Cooke, C.J., dissenting); *id.* at 816-17, 418 N.E. 2d at 394-95, 436 N.Y.S.2d at 879-80 (Jasen, J., dissenting). *See generally* O'Neil, *Second Thoughts on the First Amendment*, 13 N.M.L. REV. 577 (1983).

Courts are also exceedingly reluctant to permit prior restraint of obscene and pornographic material, despite the generally accepted view that such speech is devoid of all social value and harmful to the moral fabric of society. *See, e.g.*, Vance v. Universal Amusement Co., 445 U.S. 308, 315-17 (1980) (per curiam); Freedman v. Maryland, 380 U.S. 51, 58-60 (1965); Marcus v. Search Warrant of Property, 367 U.S. 717, 729-33 (1961). "Surely reporters and investment advisers are entitled to as much protection under the First Amendment as pornographers." Karmel, *supra* note 3, at 2, col. 5.

Indeed, the Supreme Court has intimated that only speech that would seriously and immediately endanger national security may be enjoined, Near v. Minnesota, 283 U.S. 697, 716 (1931) (dictum) (government may prevent the publication of information concerning the movement of troops or supplies during wartime); *see* Brown v. Glines, 444 U.S. 348, 353-58 (1980) (upholding military regulation requiring advance approval from commander before circulation of any petitions on Air Force bases), and yet in practice the Court has been hesitant even in this type of case, *see* New York Times Co. v. United States, 403 U.S. 713, 714 (1971) (per curiam) (refusing to enjoin publication of Pentagon Papers).

[155] Jones v. SEC, 298 U.S. 1, 24 (1936).