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Expanding Seller Liability under the Securities Act of Washington—Habermann v. WPPSS, 109 Wash. 2d 107, 744 P.2d 1032 (1987)

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EXPANDING SELLER LIABILITY UNDER THE SECURITIES ACT OF WASHINGTON—*Haberman v. WPPSS*, 109 Wash. 2d 107, 744 P.2d 1032 (1987).

The Washington Public Power Supply System's ("WPPSS") abandonment of two nuclear power projects led to the largest municipal bond default in American history.[1] This default generated an unprecedented volume of securities litigation.[2] Among the many court decisions handed down in the wake of the WPPSS fiasco was the Washington Supreme Court's decision in *Haberman v. WPPSS*.[3] The *Haberman* court significantly expanded the civil liability provisions of the Securities Act of Washington ("WSA").[4] In *Haberman*, the court expressly included as a "seller" the bond issuer and implicitly suggested that professional consultants who provide services in conjunction with a bond issuance may also be held liable as "sellers."

Seller liability was a significantly contested issue in *Haberman* because WSA's seller liability subsection[5] is its most attractive civil liability provision. The subsection sets a low culpability standard by requiring negligence rather than scienter.[6] It offers stern remedies in the form of rescission or damages plus interest, costs and attorneys' fees, and no relief is given to defendants who assert a good-faith or due diligence defense.[7]

Read literally, the statute requires strict privity between the buyer and another person in a securities transaction before that other person can be held liable as a seller.[8] However, the *Haberman* court seemed

1. Haberman v. WPPSS, 109 Wash. 2d 107, 117, 744 P.2d 1032, 1044 (1987); Nat'l L.J., Apr. 13, 1987, at 1, col. 3.

2. Nat'l L.J., *supra* note 1, at 33–34.

3. *Haberman*, 109 Wash. 2d 107, 744 P.2d 1032.

4. Securities Act of Washington, ch. 282, 1959 Wash. Laws 1311 (codified at WASH. REV. CODE ch. 21.20 (1987)).

5. WASH. REV. CODE § 21.20.430(1) (1987) provides:

Any person, who offers or *sells a security* in violation of any provisions of RCW 21.20.010 or 21.20.140 through 21.20.230, *is liable to the person buying the security from him or her*, who may sue either at law or in equity to recover the consideration paid for the security, together with interest at eight percent per annum from the date of payment, costs, and reasonable attorneys' fees, less the amount of any income received on the security, upon the tender of the security, or for damages if he or she no longer owns the security. Damages are the amount that would be recoverable upon a tender less (a) the value of the security when the buyer disposed of it and (b) interest at eight percent per annum from the date of disposition. (Emphasis added.)

6. *Cf. id.* § 21.20.430(7) (scienter required to hold certain persons liable who materially aid in offer or sale of government-issued securities).

7. *Cf. id.* § 21.20.430(3) (controlling persons allowed good-faith defense).

8. *Id.* § 21.20.430(1).

preoccupied with imposing liability on bond issuer WPPSS despite its lack of privity with bond buyers. Using nebulous language that does little to clarify who can or should be held liable as a seller, the court broadly interpreted "seller" to include anyone whose acts are a "substantial contributive factor" in the sales transaction.[9] The court, without examining the implications of its decision for the professional consultant defendants in *Haberman,* thereby adopted a liberal reading of the statute that suggests that anyone tangentially involved with a sales transaction might now be forced to defend against WSA seller liability claims.

This Note examines the WSA seller liability subsection, its language, legislative history and case law. The *Haberman* decision is reviewed in the context of the WPPSS default and other resulting litigation. The majority's rationale for redefining "seller" and the dissent's repudiation of that rationale is examined. The result apparently sought by the *Haberman* court is compared with the result actually achieved. Suggestions for defending against WSA seller liability claims are given. Finally, specific statutory amendments are recommended to clarify the scope of WSA seller liability.

I. SELLER LIABILITY UNDER THE SECURITIES ACT OF WASHINGTON

WSA[10] encompasses a number of provisions. The statute requires registration of most securities sold within the state.[11] It mandates registration and regulation of broker-dealers, securities salesmen and investment advisers.[12] The statute prohibits certain fraudulent and certain other practices[13] and establishes express civil, criminal and injunctive remedies for violation of its provisions.[14] In addition, subsection 21.20.430(1) of the Revised Code of Washington establishes a private right of action for persons who buy securities from offerors or sellers who use fraud or misstatements or who omit material facts.[15]

9. Haberman v. WPPSS, 109 Wash. 2d 107, 131, 744 P.2d 1032, 1052 (1987).

10. Securities Act of Washington, ch. 282, 1959 Wash. Laws 1311 (codified at WASH. REV. CODE ch. 21.20 (1987)).

11. WASH. REV. CODE § 21.20.140 (1987).

12. *Id.* § 21.20.040–.135.

13. *Id.* § 21.20.010–.030.

14. *Id.* § 21.20.390–.430.

15. WASH. REV. CODE § 21.20.430(1) (1987) also attaches liability for offering or selling unregistered securities. In addition to the seller liability subsection, civil liability attaches to certain nonsellers under section 21.20.430(2) (buyers who use fraud or misrepresentation) and section 21.20.430(3) (specific categories of persons who have certain relationships with sellers or

WSA was derived from the Uniform Securities Act, promulgated in 1956 by the Conference of Commissioners on Uniform State Laws and the American Bar Association.[16] Rather than imitate the federal statutory scheme, the drafters adopted some federal securities provisions,[17] discarded others,[18] and encouraged enacting states to treat some Uniform Securities Act sections as "options."[19] The Uniform Securities Act's seller liability subsection[20] was derived from section 12(2) of the federal Securities Act of 1933.[21] The Washington legislature, discarding the Uniform Securities Act and federal section 12(2) provisions for a good-faith defense, adopted the remainder of the Uniform Securities Act's seller liability subsection as subsection

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buyers, including controlling persons and employees). Subsection 21.20.430(3) alone permits a good-faith defense.

16. UNIFORM SECURITIES ACT historical note, 7B U.L.A. 510, 514 (1985). The original Uniform Securities Act text appears in L. LOSS, COMMENTARY ON THE UNIFORM SECURITIES ACT (1976) [hereinafter LOSS COMMENTARY].

17. *Compare* UNIFORM SECURITIES ACT § 101, 7B U.L.A. 510, 516 (1985) (the source of the general fraud provision in WASH. REV. CODE § 21.20.010 (1987)) *with* Rule 10b-5, 17 C.F.R. § 240.10b-5 (1987); *compare* UNIFORM SECURITIES ACT § 410(b), 7B U.L.A. at 516 (the source of the controlling person subsection of the civil liability provision in § 21.20.430(3)) *with* Securities Act of 1933, § 15, 15 U.S.C. § 77o (1982) *and* Securities Exchange Act of 1934, § 20, 15 U.S.C. § 78t (1982) (separate provisions for controlling person liability).

18. For example, the Uniform Securities Act contains no equivalent to Section 11 of the Securities Act of 1933, 15 U.S.C. § 77k (1982) (issuer and professional liability for false registration of securities).

19. LOSS COMMENTARY, *supra* note 16, at 168–76 (three appendices suggesting optional wordings); *see also* 7B U.L.A. 97–100 (Supp. 1987); 7B U.L.A. 510, 511–14 (1985) (noting that all thirty-six enacting states have modified the Uniform Securities Act, with nearly all making "numerous" changes); Rooks, *The Blue Sky of Washington: Registration of Securities of a New Venture*, 6 GONZ. L. REV. 187, 188 (1971).

20. UNIFORM SECURITIES ACT § 410(a)(2), 7B U.L.A. 643 (1985):

> Any person who . . . offers or sells a security by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading (the buyer not knowing of the untruth or omission), and who does not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the untruth or omission, is liable to the person buying the security from him . . . .

LOSS COMMENTARY, *supra* note 16, at 145.

21. 7B U.L.A. 644 (1985). Section 12(2):

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

15 U.S.C. § 77l (1982).

21.20.430(1) of the Revised Code of Washington.[22] Since enacting the seller liability statute, the legislature has amended it repeatedly, although without substantively significant change and at least partly to conform to nationwide trends.[23]

Who specifically might be deemed a "seller" under subsection 21.20.430(1), however, was not delineated by Washington courts before *Haberman.* The few WSA seller liability cases dealt with face-to-face selling conducted primarily by persons who actually held title to the securities sold.[24] The only notable exception was *McClellan v. Sundholm,* [25] where a silver bullion salesman was held liable as a seller even though, as an employee of the selling company, he did not personally pass title to the bullion.[26] The salesman had directly approached the buyer, described his employer's services and told the buyer face-to-face that bullion was a sound investment.[27] Although the trial court found the salesman liable as a "controlling person,"[28] the supreme court rejected that claim and concluded that the salesman, who did not "own" the bullion, "did in fact sell" it under subsection 21.20.430(1).[29] The *McClellan* court's only expansion of "seller"

22. Securities Act of Washington, ch. 282, 1959 Wash. Laws 1344 (codified at WASH. REV. CODE ch. 21.20 (1987)).

23. *See* Act of Apr. 11, 1979, ch. 68, 1979 Wash. Laws 1196, 1223 (changing references to male sellers to male or female sellers); Act of May 26, 1977, ch. 172, 1977 Wash. Laws 672, 678 (incorporating WASH. REV. CODE § 21.20.010 violations); Act of May 16, 1975, ch. 84, 1975 Wash. Laws 354, 370 (increasing recoverable interest to eight percent); Act of Feb. 6, 1974, ch. 77, 1974 Wash. Laws 156, 165 (incorporating new subsection prohibiting certain contract-based suits); Securities Act, ch. 199, 1967 Wash. Laws 999, 1003 (changing act to code references); *cf.* Haberman v. WPPSS, 109 Wash. 2d 107, 179, 744 P.2d 1032, 1076 (1987) (Pearson, C.J., dissenting) (although legislature has amended section 21.20.430(1), the original language requiring privity remains intact).

24. *See* Clausing v. DeHart, 83 Wash. 2d 70, 515 P.2d 982 (1973) (100% stockholders negotiated nursing home sale face-to-face); Kittilson v. Ford, 23 Wash. App. 402, 595 P.2d 944 (1979), *aff'd,* 93 Wash. 2d 223, 608 P.2d 264 (1980) (real estate contracts seller directly solicited investment); Garretson v. Red-Co, Inc., 9 Wash. App. 923, 516 P.2d 1039 (1973) (closely-held corporation solicited stock sale). The *Haberman* court, in its discussion of WSA seller liability, also cited Golberg v. Sanglier, 27 Wash. App. 179, 616 P.2d 1239 (1980), *rev'd,* 96 Wash. 2d 874, 639 P.2d 1347 (1982), a buyer liability case analogous to the seller cases because facts were misrepresented during a direct purchase. *Haberman,* 109 Wash. 2d at 126, 744 P.2d at 1049; *see also* Shermer v. Baker, 2 Wash. App. 845, 472 P.2d 589 (buyer who was managing officer and majority stockholder misrepresented value of stock purchased directly from minority stockholder), *review denied,* 78 Wash. 2d 994 (1970). Dicta in Kaas v. Privette, 12 Wash. App. 142, 149–51, 529 P.2d 23, 28–29 (1974) (participant liability claims in a common law fraud case) noted that WSA civil liability for fraud attaches only to "face to face" negotiations and "direct dealings."

25. 89 Wash. 2d 527, 574 P.2d 371 (1978).

26. *Id.*

27. *Id.* at 529, 574 P.2d at 372.

28. *Id.* at 533–34, 574 P.2d at 374.

29. *Id.* at 534, 574 P.2d at 374.

was to include persons who engage in direct selling practices regardless of whether they personally pass title to the securities.

While Washington state courts had little opportunity to fully construe the term "seller" prior to *Haberman,* federal courts in Washington, considering WSA seller liability claims in factual contexts resembling *Haberman,* added confusion rather than insight with their conflicting interpretations of state law. In two WPPSS-related opinions, Judge Browning[30] of the Western District of Washington said in dicta that a securities issuer, although not an actual seller, could be held liable as a seller under subsection 21.20.430(1).[31] Soon after Judge Browning's comments, Judge Rothstein of the same court noted that WSA liability for fraud could not attach to an issuer and its professional consultant because they were not "connected with the innumerable persons who *actually* sold" the securities.[32] Judge Rothstein said that WSA liability attaches only to "those who bear some actual 'connection' to an offer or transaction, either as an offeror or offeree, a seller or buyer, or someone involved indirectly as provided in RCW § 21.20.430(3)."[33] With Judge Rothstein's narrow interpretation simply counteracting Judge Browning's expansive reading, the meaning of the term "seller" under WSA remained unresolved, awaiting clarification by Washington state courts.

II. THE WPPSS BOND DEFAULT AND RESULTING LITIGATION

In the 1950's and 1960's, experts predicted that hydroelectric supplies would not meet the Pacific Northwest's power needs.[34] The Bonneville Power Administration, by 1972, succeeded in encouraging WPPSS[35] to plan the construction of three nuclear power projects.[36] In 1976, WPPSS obtained the necessary financial commitments for

30. United States District Court Judge Browning of Tucson, Arizona, was assigned in 1985 to hear the WPPSS cases in the Western District of Washington.

31. *In re* WPPSS, [1986–87 Transfer Binder] Blue Sky L. Rep. (CCH) ¶ 72,371, at 71,676 (W.D. Wash. Jan. 24, 1986) (subsection 21.20.430(1) claims not at issue); Mirotznick v. Ernst & Whinney, No. C85-1103, slip op. at 5 (W.D. Wash. Jan. 24, 1986) (accountants not held liable as subsection 21.20.430(1) sellers).

32. Naye v. Boyd, [1986–87 Transfer Binder] Blue Sky L. Rep. (CCH) ¶ 72,393, at 71,777 (W.D. Wash. Mar. 25, 1986) (emphasis added) (Seafirst Corporation, its directors, officers and independent auditor not held liable in stock transactions made while bank suffered huge financial losses).

33. *Id.* at 71,782.

34. Asson v. City of Burley, 105 Idaho 432, 670 P.2d 839, 841 (1983), *cert. denied,* 469 U.S. 870 (1984).

35. WPPSS was formed under state law in 1957 as a municipal corporation and joint operating agency to finance, construct, own and operate electrical generating facilities. Chemical

two additional plants, Projects 4 and 5, when 88 utilities and municipalities signed "Participant Agreements."[37] These "Participants" agreed to pay the " 'total annual cost of the Projects, including debt services on the Bonds . . . *whether or not the Projects are operable or operating.*' "[38] The next year, sales began in a $2.25 billion, fifteen-part bond offering to finance the new plants.[39] In 1982, after delays and cost overruns made completion of Projects 4 and 5 financially impossible,[40] WPPSS terminated the plants, announcing that no more bonds would be issued.[41]

To forestall the Participants' efforts at avoiding their bond payment obligations,[42] the WPPSS bond fund trustee, Chemical Bank, filed a state court declaratory action to require payment.[43] In *Chemical Bank I*[44] and *Chemical Bank II*,[45] the Washington Supreme Court held the agreements unenforceable because the Participant utilities and municipalities lacked express or implied statutory authority to enter into the Participant Agreements.[46] Unable to secure repayment under the agreements, bondholders filed suit in federal and state courts against any entity that might be held responsible for the WPPSS bond default.[47]

Bank v. WPPSS, 99 Wash. 2d 772, 776–77, 666 P.2d 329, 331 (1983), *reconsidered and aff'd*, 102 Wash. 2d 874, 691 P.2d 524 (1984), *cert. denied*, 471 U.S. 1065, 1075 (1985).

36. Bonds guaranteed by the Bonneville Power Administration financed WPPSS Projects 1, 2 and 3. *Id.* at 772, 779, 666 P.2d at 332–33.

37. *Asson*, 670 P.2d at 843; DeFazio v. WPPSS, 296 Or. 550, 679 P.2d 1316, 1319 (1984); . The eighty-eight Participants included nine Washington cities, seven Oregon cities, five Idaho cities, nineteen Washington public utility districts, four Oregon public utility districts, forty-three rural electric cooperatives and one Washington irrigation district. *Chemical Bank*, 102 Wash. 2d at 881 n.1, 691 P.2d at 529 n.1.

38. *DeFazio*, 679 P.2d at 1322 (quoting WPPSS Official Statement accompanying the bond issuance).

39. Haberman v. WPPSS, 109 Wash. 2d 107, 114, 117, 744 P.2d 1032, 1043, 1044 (1987).

40. Chemical Bank v. WPPSS, 99 Wash. 2d 772, 776, 666 P.2d 329, 331 (1983), *reconsidered and aff'd*, 102 Wash. 2d 874, 691 P.2d 524 (1984), *cert. denied*, 471 U.S. 1065, 1075 (1985).

41. *Haberman*, 109 Wash. 2d at 117, 744 P.2d at 1044. *See generally* D. CHASAN, THE FALL OF THE HOUSE OF WPPSS 49–55 (1985).

42. *See generally DeFazio*, 679 P.2d 1316 (the first WPPSS "ratepayers' revolt" case, filed in December 1981, in which Oregon ratepayers challenged the validity of the Participation Agreements); D. CHASAN, *supra* note 41, at 69–71.

43. *Chemical Bank*, 99 Wash. 2d at 776, 666 P.2d at 331.

44. Chemical Bank v. WPPSS, 99 Wash. 2d 772, 666 P.2d 329 (1983).

45. Chemical Bank v. WPPSS, 102 Wash. 2d 874, 691 P.2d 524 (1984), *cert. denied*, 471 U.S. 1065, 1075 (1985).

46. *Chemical Bank*, 99 Wash. 2d at 784–94, 666 P.2d at 335–40.

47. By late 1987, over 25,000 investors were involved in WPPSS lawsuits nationwide. Gleckman, *The Jury's Still Out on 'Whoops'— Way Out*, BUS. WK. Nov. 2, 1987, at 168. Some of the federal litigation was consolidated in the Western District of Washington, where it remains pending. *See In re* WPPSS, 568 F. Supp. 1250 (J.P.M.D.L. 1983) (consolidating 13 WPPSS-

III. THE *HABERMAN* DECISION

On May 7, 1984, *Haberman v. WPPSS* was filed in state court by a group of individual WPPSS bondholders[48] asserting violations of WSA, the federal securities laws, and the Washington Consumer Protection Act, along with common law allegations of negligence, misrepresentation and fraud.[49] Defendants were WPPSS, its twenty-three member utilities and municipalities, the eighty-eight Participants and professional consultants (attorneys, engineers, accountants and investment advisors). The professionals provided services in conjunction with the preparation of "Official Statements" released by WPPSS to underwriters,[50] who used the Official Statements in selling the bonds directly to investors.[51]

Judge Carroll of the King County Superior Court dismissed the suit for failure to state a claim upon which relief could be granted.[52] The Washington Supreme Court accepted direct review of the appeal and reinstated plaintiffs' WSA claims and claims based on common law theories of negligence, misrepresentation and fraud.[53] Claims under section 12(2) of the federal Securities Act of 1933 were dismissed, along with derivative claims of negligence and malpractice and claims under the Washington Consumer Protection Act.[54]

WSA claims reinstated by the court included claims under the seller liability and controlling person liability provisions.[55] The court, how-

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related actions in the Western District of Washington and the Southern District of New York for pretrial proceedings).

48. Haberman v. WPPSS, 109 Wash. 2d 107, 118, 744 P.2d 1032, 1045 (1987). Subsequently, two groups of institutional investors intervened as additional plaintiffs. *Id.* Intervenors included: One, five subsidiaries of American Express, holding $90 million in WPPSS bonds; and two, United States Trust Company, trustee of investment funds holding $270 million in WPPSS bonds. First Amended Complaint in Intervention of American Express Company Subsidiaries and Restated Demand for Jury Trial at 10–12, Haberman v. WPPSS (King County Super. Ct. Mar. 29, 1985) (No. 84-2-06452-8); First Amended Complaint in Intervention of United States Trust Company of New York, Trustee[,] and Restated Demand for Jury Trial at 4, Haberman v. WPPSS (King County Super. Ct. Mar. 29, 1985) (No. 84-2-06452-8).

49. *Haberman,* 109 Wash. 2d at 119, 744 P.2d at 1045–46.

50. *Id.* at 116, 118, 744 P.2d at 1044, 1045. The Official Statements were written by WPPSS and its investment advisors. They included legal opinions of bond counsel that Participants were obligated to pay the projects' costs regardless of plant completion or operation. Opinions of engineers and accountants regarding the structural and financial feasibility of the projects were also included in the statements. *Id.*

51. *Id.* at 117, 744 P.2d at 1044.

52. Haberman v. WPPSS, No. 84-2-06452-8 (King County Super. Ct. Oct. 7, 1985).

53. *Haberman,* 109 Wash. 2d at 119, 744 P.2d at 1046.

54. *Id.*

55. WASH. REV. CODE § 21.20.430(1), (3) (1987).

ever, declined to address claims under WSA's general fraud provision, despite the availability of cumulative remedies under WSA.[56]

A. New "Forces" Unleashed in the Field of Seller Liability

The most far-reaching ruling by the *Haberman* court was the decision on seller liability under WSA subsection 21.20.430(1). In allowing claims against issuer WPPSS and its professional consultants, Justice Brachtenbach wrote for the majority:

> [A] defendant is liable as a seller under RCW 21.20.430(1) if his acts were a *substantial contributive factor in the sales transaction.* Considerations important in determining whether a defendant's conduct is a substantial contributive factor in the sales transaction include: (1) the number of other factors which contribute to the sale and the extent of the effect which they have in producing it; (2) whether the defendant's conduct has created a force or series of forces which are in continuous and active operation up to the time of the sale, or has created a situation harmless unless acted upon by other forces for which the actor is not responsible; and (3) lapse of time. . . . Whether a defendant's conduct was a substantial contributive factor is necessarily a question of fact.[57]

The majority developed four rationales for adopting a substantial contributive factor test.[58] First, the express language of section 21.20.900 and prior case law required that any interpretation of WSA be in harmony with interpretations of analogous federal and state provisions.[59] Harmony, according to the majority, would be furthered by adopting a substantial contributive factor test for WSA seller liabil-

56. *Id.* § 21.20.010. The court also rejected an argument that WSA should not be applied to out-of-state defendants or transactions. *Haberman,* 109 Wash. 2d at 134, 744 P.2d at 1053. Further, the court rejected a challenge to the constitutionality of section 21.20.430(7), which lowers the standard of culpability for certain persons who materially aid in the offer or sale of certain government-issued securities. *Haberman,* 109 Wash. 2d at 136–47, 744 P.2d at 1054–60.

57. *Haberman,* 109 Wash. 2d at 131–32, 744 P.2d at 1052 (emphasis added).

58. The court refers to both a "substantial contributive factor" test and a "substantial factor-proximate cause" test. *Haberman,* 109 Wash. 2d at 128–33, 744 P.2d at 1050–52. Although the *Haberman* court uses the terms interchangeably, many courts have taken slightly varying approaches when applying the tests. For a comparison of cases emphasizing the participation element with cases stressing proximate cause and cases focusing on the "position" of the defendant, see O'Hara, *Erosion of the Privity Requirement in Section 12(2) of the Securities Act of 1933: the Expanded Meaning of Seller,* 31 UCLA L. REV. 921, 946–79 (1984); see also Comment, *Attorneys and Participant Liability Under § 12(2) of the Securities Act of 1933,* 1982 ARIZ. ST. L.J. 529, 532–50; Comment, *Seller Liability Under Section 12(2) of the Securities Act of 1933: A Proximate Cause-Substantial Factor Approach Limited by a Duty of Inquiry,* 36 VAND. L. REV. 361, 367–76 (1983).

59. *Haberman,* 109 Wash. 2d at 125, 744 P.2d at 1049.

ity.[60] Second, the Official Comments to revised Uniform Securities Act section 605(a) supported a substantial contributive factor test.[61] Third, the court's adoption of the test was "in harmony with similar developments in general tort law."[62] Finally, the majority, noting that WSA does not address issuer liability, explained that WSA's "clear purposes" required as a matter of policy the expansion of seller liability.[63]

The dissent,[64] favoring dismissal of WSA claims and certain negligent misrepresentation claims, emphasized that WSA's "clear language" requires privity between plaintiff and defendant.[65] The dissent argued that the majority's use of revised Uniform Securities Act comments was "without merit,"[66] and that the use of tort principles to construe statutory law was "inappropriate."[67] The majority's interpretation of WSA mirroring the interpretation of federal securities acts was "improper," according to the dissent, because of the acts' sharply differing purposes and statutory schemes.[68] The substantial participant test for seller liability used by other courts did not encompass persons who were "merely involved in preparing reports and offering circulars."[69] Other state courts, the dissent continued, have not interpreted state securities acts in an "inconclusive" manner, as

60. *Id.* at 126–29, 744 P.2d at 1049–51. The majority based this decision on its view that a majority of federal circuits interpreting seller liability under section 12(2) of the federal Securities Act of 1933 used a substantial factor test.

61. Acknowledging that the revised Uniform Securities Act had not been enacted by the Washington legislature, the majority stated nonetheless that "this approach best promotes the legislative purpose behind the [WSA]." *Id.* at 130, 744 P.2d at 1051.

62. *Id.* (citing Davis v. AVCO Fin. Services, Inc., 739 F.2d 1057, 1066 (6th Cir. 1984), *cert. denied,* 470 U.S. 1005, *cert. denied,* 472 U.S. 1012 (1985), a Sixth Circuit case that took language directly from RESTATEMENT (SECOND) OF TORTS §§ 432, 433 (1965) to formulate a substantial contributive factor test).

63. *Id.* at 132, 744 P.2d at 1052.

64. Chief Justice Pearson wrote the dissent and was joined by Justices Dolliver and Andersen. The majority comprised Justices Brachtenbach, Utter, Dore, Goodloe and Durham and Judge Wetherall of the King County Superior Court, who sat pro tempore. Justice Callow took no part in the opinion. *See id.* at 178, 190, 744 P.2d at 1076, 1082.

65. *Id.* at 179, 744 P.2d at 1076.

66. *Id.* at 180, 744 P.2d at 1077. "Our Legislature has not espoused that act and its comments in any part; indeed, only two states have adopted the act, and then with numerous variations. Whether other states will adopt the act is not only speculative but improbable, because both the American Bar Association and the North American Securities Administrators Association criticized and refused to endorse it." *Id.* at 180–81, 744 P.2d at 1077 (citations omitted).

67. *Id.* at 181, 744 P.2d at 1077 ("In fact, the securities laws were created specifically to regulate a unique aspect of commerce that no other area of law touches upon, including common law tort.").

68. *Id.* at 181, 182, 744 P.2d at 1077, 1078.

69. *Id.* at 183, 744 P.2d at 1078.

suggested by the majority, but rather "according to their plain language."[70] The dissent noted that federal courts not mirroring section 12(2) interpretations "generally employ a plain meaning interpretation" of state securities acts.[71]

B. The Result Sought by the Court vs. the Result Achieved

Although a lengthy portion of the *Haberman* opinion is devoted to the seller liability issue,[72] only a single paragraph discussed application of the court's new test to the *Haberman* defendants.[73] That brief discussion stated that issuers, such as WPPSS, should not escape liability by selling to "middlemen beyond their control" in a firm commitment underwriting.[74] Acknowledging the lack of separate issuer liability under WSA, the majority reinstated seller liability claims against issuer WPPSS.[75]

In extending seller liability to WPPSS, however, other liabilities not discussed in the opinion resulted. The majority opinion included a single, oblique reference to "others acting together with the issuer who were the actual beneficiaries of the sales proceeds."[76] Without explaining its reasoning or outlining the new scope of WSA seller liability, the majority then reinstated all WSA seller liability claims against all defendants. While an argument might be made that the WPPSS members and Participants were "actual beneficiaries of the sale proceeds," professional consultants, whose service fees were not contingent on the bond offering's success, were simply not beneficiaries. The court did not identify any specific actions by the professionals that might incur seller liability. Furthermore, the court did not expressly acknowledge that its expansive reading of the seller liability statute could potentially be used to attach liability not only to issuers

70. *Id.* at 184, 744 P.2d at 1078.

71. *Id.* at 186, 744 P.2d at 1079.

72. *Id.* at 124–33, 744 P.2d at 1048–52.

73. *Id.* at 132, 744 P.2d at 1052.

74. *Id.* "Firm commitment underwriting," the most common underwriting method in the United States, occurs when an issuer sells securities to underwriters (for example, investment bankers) who then resell to investors. *See generally* L. LOSS, FUNDAMENTALS OF SECURITIES REGULATION 83–90 (1983) [hereinafter LOSS FUNDAMENTALS]. Following industry practice, WPPSS sold the bonds to underwriters who sold them to the *Haberman* plaintiffs. *Haberman*, 109 Wash. 2d at 132, 744 P.2d at 1052.

75. *Haberman*, 109 Wash. 2d at 132–33, 744 P.2d at 1052.

76. *Id.* at 132, 744 P.2d at 1052 ("If we were to require strict privity for liability under RCW 21.20.430(1), only the underwriters would be potentially liable for prospectus fraud, cutting off all potential claims against the issuer of the bonds *and others acting together with the issuer who were the actual beneficiaries of the sale proceeds.*") (emphasis added).

but also to professionals who have little or no involvement in the selling process.

Because the *Haberman* decision was result-oriented, it seems fair to consider the final result if the case were litigated to its conclusion and all defendants found liable. Plaintiffs would then seek payment of the judgment award. WPPSS demonstrated its inability to pay bondholders before the lawsuit began, and the WPPSS members and Participants are small local utilities lacking surplus funds. As a result, the professionals, backed by insurance policies,[77] might be forced to pay the bulk of any judgment award. If the "deep pocket" among the *Haberman* defendants is worn, not by WPPSS, but by the outside professionals, a serious question is raised by the court's result-oriented decision: Was seller liability in Washington expanded not merely to allow claims against an issuer but to allow bond buyers the right to seek damages from anyone marginally involved in the transaction who might be financially capable of "substantially contributing" to the payment of judgment awards?

C. Increased Uncertainty in the Defense of Seller Liability Claims

Although future unhappy securities buyers were assisted by the *Haberman* court's expansion of seller liability, professional consultants were left uncertain about what specific actions might subject them to liability. The majority opinion creates new black-letter law in the area of seller liability without applying that law to the *Haberman* facts to indicate which of the defendants' actions were "substantial contributive factors" sufficient to invoke seller liability. Rather than giving a clear, practical definition of its new seller liability test, the court simply announced "considerations" that would be "important" in applying the test.[78]

These "considerations" were borrowed, almost verbatim, from common law tort principles on legal causation found in the *Restatement (Second) of Torts.*[79] The central "consideration" is whether the

77. For example, WPPSS bond counsel Houghton, Cluck, Coughlin & Riley (a *Haberman* defendant) reached a $7.25 million settlement with bondholders in federal litigation in the Western District of Washington. In reporting the settlement, the Seattle Times noted that the amount was believed to be the maximum limit available under the law firm's insurance policy. Seattle Times, Dec. 25, 1987, at C14, col. 1.

78. *Haberman,* 109 Wash. 2d at 131, 744 P.2d at 1052.

79. *Compare supra* text accompanying note 57 (text of *Haberman* court's substantial contributive factor test) *with* RESTATEMENT (SECOND) OF TORTS §§ 432, 433 (1965). *See also* Davis v. AVCO Fin. Services, Inc., 739 F.2d 1057, 1063–68 (6th Cir. 1984), *cert. denied,* 470 U.S. 1005, *cert. denied,* 472 U.S. 1012 (1985). *But see* Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299, 310 (1985) (questioning the pertinence of common law doctrines in applying

defendant's conduct creates a "force or series of forces" that are in "continuous and active operation" up to the time of the sale, or creates a "situation harmless" unless acted upon by other forces for which the actor is not responsible.[80] These quoted phrases lack obvious meanings in the context of Washington's securities laws.[81] Because the *Haberman* court offered no explanation, Washington courts will be required to further interpret the new test for seller liability.

IV. FACTORS THAT SUBSTANTIALLY CONTRIBUTED TO AN EXPANSION OF SELLER LIABILITY

The majority suggested that the primary reason for expanding seller liability was to reach a "result" whereby issuer WPPSS could be found liable.[82] In failing to consider fully the policy ramifications of its decision, the court effectively adopted a statutory scheme never considered by the Washington legislature.

The new test for seller liability expands the strict privity approach to include "those parties who have the attributes of a seller and thus *who policy dictates should be subject to liability* under RCW § 21.20.430(1)."[83] The majority does not specify what policy dictates this result except that the "clear purposes" of WSA[84] are "to protect investors."[85] The statute, presumably written to reflect those "clear purposes," expressly holds a seller liable only "to the person buying the security *from him or her.*"[86] Imposition of liability for setting in motion "forces which are in continuous and active operation"[87] until the moment a sale occurs was accomplished by the court, not by the statute.[88] If courts expand seller liability statutes merely because a plaintiff invokes the phrase "investors must be protected," the investment marketplace will be severely disrupted.[89] The market cannot

securities statutes); *Haberman,* 109 Wash. 2d at 181, 744 P.2d at 1077 (Pearson, C.J., dissenting) (majority's argument based on tort principles is misplaced because question is one of statutory construction).

80. *Haberman,* 109 Wash. 2d at 131, 744 P.2d at 1052.

81. "[I]n matters of literary style the sovereign virtue for the judge is *clearness.*" Cardozo, *Nourishing our Power of Clear Statement,* in THE GREAT POWER AT THE BAR AND BENCH 1142 (J. Rivera ed. 1972) (emphasis added).

82. *Haberman,* 109 Wash. 2d at 132, 744 P.2d at 1052.

83. *Id.* at 132, 744 P.2d at 1052 (emphasis added).

84. *Id.*

85. *Id.* at 125, 744 P.2d at 1049.

86. WASH. REV. CODE § 21.20.430(1) (1987) (emphasis added).

87. *Haberman,* 109 Wash. 2d at 131, 744 P.2d at 1052.

88. *Id.* at 132, 744 P.2d at 1052.

89. *In re* WPPSS, MDL No. 551 (W.D. Wash. Oct. 21, 1987), in which Judge Browning dismissed "with considerable personal reluctance" all claims against the Bonneville Power

offer money-back guarantees to investors who demand that all securities be risk-free.[90] Investors should be protected by the securities laws, but a policy of protection does not and should not afford to investors automatic legal immunity for their own bad investment decisions.[91]

A. Misunderstanding of Federal and State Securities Statutes

In *Haberman,* the majority contended that WSA section 21.20.900 requires "harmony" between WSA and federal and other states' seller liability laws.[92] By citing section 21.20.900 as requiring harmonization, the court effectively avoided an accurate or in-depth discussion of the federal statutes and case law.

The *Haberman* court, turning to section 12(2) of the federal Securities Act of 1933 for guidance, noted that the WSA seller liability subsection was "modeled after" the Uniform Securities Act, which was "modeled after" section 12(2). Subsection 21.20.430(1) is a direct descendant but not a clone of section 12(2).[93] Perhaps the biggest difference between the two statutes lies in the state subsection's lack of a good-faith defense as found in the federal section.[94] But in addition to this and other obvious wording differences,[95] the two statutes were

Administration ("BPA"). In realizing that the BPA was absolved of liability because it fell under the discretionary function exception to the Federal Tort Claims Act, 28 U.S.C. § 1346(b) (1982), Judge Browning did not attempt to reinterpret the statute just to hold the BPA liable. Instead, he wrote: "While this Court is powerless to address those concerns, the Congress is not. Fundamental fairness and elementary principles of accountability demand that Congress address these charges and, if substantiated, provide relief through private legislation or otherwise." *WPPSS,* at 18–19.

90. *See* H.R. REP. No. 85, 73d Cong., 1st Sess. 4 (1933); H. CHERRINGTON, THE INVESTOR AND THE SECURITIES ACT 246 (1973).

91. President Franklin D. Roosevelt, in his message to Congress recommending passage of the Securities Act of 1933, wrote, "The purpose of the legislation I suggest is to protect the public *with the least possible interference to honest business.*" H.R. REP. No. 85, 73d Cong., 1st Sess. 2 (1933) (emphasis added).

92. *Haberman,* 109 Wash. 2d at 125, 744 P.2d at 1049; *cf.* Kittilson v. Ford, 93 Wash. 2d 223, 227, 608 P.2d 264, 265 (1980) ("The coordination of the federal courts with federal regulations does not require imitation by this court in construing our act, only that our construction not interfere with the federal scheme."). Not all courts share the Washington Supreme Court's predilection for statutory uniformity. In Admiralty Fund v. Jones, 677 F.2d 1289 (9th Cir. 1982), the Ninth Circuit reviewed section 12(2) seller liability along with a seller liability claim under a California statute virtually identical to section 21.20.430(1) and held that liability was available under the federal, but not the state, statute. *Id.* at 1295, 1296.

93. *Haberman,* 109 Wash. 2d at 125, 744 P.2d at 1048; *see also* UNIFORM SECURITIES ACT § 410 comment, 7B U.L.A. 644 (1985).

94. *See supra* note 6 and accompanying text.

95. *Compare supra* note 5 (text of WASH. REV. CODE § 21.20.430(1) (1987)) *with supra* note 21 (text of federal section 12(2)).

enacted for different purposes[96] and fit into different statutory schemes.[97]

Section 12(2) was part of a federal act written with the philosophy that the best way to protect investors was to force disclosure of all financial information relevant to securities and securities transactions.[98] The theory was that, with the necessary information in hand, investors could make the best decisions regarding their own investments.[99] WSA section 21.20.430, however, was enacted as part of a state securities act intended not only to force disclosure but also to regulate the merit of securities being sold.[100]

Section 12(2) is part of a statutory scheme that takes an entirely different approach to who can be held liable for securities violations than does WSA. For example, section 3 of the Securities Act of 1933 expressly exempts municipal bonds from its coverage,[101] but WSA has no parallel provision.[102] Further, section 11 of the federal act provides express civil liability for issuers, professional consultants and underwriters involved in preparation of registration statements that misrepresent or omit material facts.[103] WSA contains no equivalent to section 11 but augments its seller liability section[104] with subsections allowing buyer liability[105] and providing liability for persons who control or who have specified relationships with the seller/buyer.[106] The

96. *Haberman*, 109 Wash. 2d at 181, 744 P.2d at 1077 (Pearson, C.J., dissenting).

97. *Id.* at 182, 744 P.2d at 1077 (Pearson, C.J., dissenting). *See generally* O'Hara, *supra* note 58, at 925 & n.13, 994–1001.

98. *See* Landreth Timber Co. v. Landreth, 471 U.S. 681, 687 (1985); Ernst & Ernst v. Hochfelder, 425 U.S. 185, 195 (1976); H.R. REP. NO. 85, 73d Cong., 1st Sess. 1 (1933).

99. *See* H. CHERRINGTON, *supra* note 90, at 238.

100. *See* Naye v. Boyd, [1986–87 Transfer Binder] Blue Sky L. Rep. (CCH) ¶ 72,393, at 77,781 (W.D. Wash. Mar. 25, 1986); Rooks, *supra* note 19, at 188; Comment, *Securities Fraud Under the Blue Sky of Washington,* 53 WASH. L. REV. 279, 282 n.10 (1978). *See generally* LOSS FUNDAMENTALS, *supra* note 74, at 29–38 (discussing the differences between and historical bases for merit and disclosure philosophies of securities regulation).

101. 15 U.S.C. § 77c (1982); *see also* Davidson v. Dean Witter Reynolds, Inc., 478 F. Supp. 494, 495 (D. Colo. 1979); Trussell v. United Underwriters, Ltd., 228 F. Supp. 757, 767 (D. Colo. 1964).

102. The *Haberman* court, noting that the WPPSS bonds "remain exempt from section 12(2) liability," affirmed dismissal of federal section 12(2) claims. Haberman v. WPPSS, 109 Wash. 2d 107, 124, 744 P.2d 1032, 1048 (1987).

103. 15 U.S.C. § 77k (1982).

104. WASH. REV. CODE § 21.20.430(1) (1987).

105. *Id.* § 21.20.430(2).

106. *Id.* § 21.20.430(3); *see also* Mirotznick v. Sensney, Davis & McCormick, [1986–87 Transfer Binder] Blue Sky L. Rep. (CCH) ¶ 72,480, at 72,781 (W.D. Wash. Aug 11, 1986) (dismissing WSA seller liability claims against local counsel in a WPPSS-related case who provided opinion letters to various Participants because WSA "limits those liable to certain categories of persons" specified in subsections 21.20.430(1) and 21.20.430(3)).

Securities Act of 1933 contains no statute identical to the WSA subsection, although it does provide for "controlling person" liability.[107]

Perhaps the *Haberman* court saw the state statutory scheme as lacking the sophisticated provisions found in the federal act, such as the section providing express issuer and professional liability. The majority may have felt compelled to stretch the seller liability subsection to overcome perceived deficiencies in WSA. Such an impulse, although possibly misplaced, would be understandable, but the opinion offered no such rationale. Instead, the court analogized subsection 21.20.430(1) to federal section 12(2) simply because both shared a common origin and contained some identical language. As the dissent noted, however, "[o]nly a strict privity approach ensures meaningful application of *all* portions of section .430."[108]

B. Misapplication of Federal Case Law

The *Haberman* court adopted its substantial contributive factor test from seller liability tests used by other jurisdictions without analyzing how other courts have actually applied their tests. The court, noting that only two federal circuits require privity between buyer and seller in federal section 12(2) cases, opted for the viewpoint of the majority of circuits, which requires "participation in the sale [that is] a substantial factor in causing the transaction to take place."[109] However, the court failed to recognize that the "split" in the federal circuits is more form than substance; the courts differ not in what they do, but merely in how they describe what they do.

Whether federal courts approach the matter as strict constructionists, as substantial participant or substantial contributive factor proponents, the results are the same. Seller liability is found almost exclusively where actual title passes from "seller" to buyer or where the "seller" plays an active, personal role in face-to-face negotiations or solicitations leading directly to a specific sales transaction.[110]

The Ninth Circuit first applied a "substantial factor" test for seller liability in *SEC v. Murphy.*[111] The *Murphy* court held a corporate officer of a cable TV financing venture liable under section 12 because his acts were "both necessary to and a substantial factor in the sales

107. 15 U.S.C. § 77o (1982).

108. Haberman v. WPPSS, 109 Wash. 2d 107, 180, 744 P.2d 1032, 1076 (1987) (emphasis added).

109. *Id.* at 126, 127, 130, 744 P.2d at 1049, 1051.

110. *Cf. id.* at 183, 744 P.2d at 1078 (Pearson, C.J., dissenting).

111. 626 F.2d 633, 652 (9th Cir. 1980).

transaction."[112] The officer had met personally with investors and their representatives.[113]

The Fifth Circuit took an early lead[114] in expanding section 12(2) liability but, like the Ninth Circuit, has consistently found liability only where defendants have direct involvement with buyers or own title to the security being sold.[115] The remaining circuits, whether

112. *Id.* at 650.

113. *Id.* at 652; *see also* Anderson v. Aurotek, 774 F.2d 927 (9th Cir. 1985) (*Murphy* test applicable to determine whether two stockholders were section 12(2) "sellers"); Admiralty Fund v. Jones, 677 F.2d 1289 (9th Cir. 1982) (*Murphy* test applicable to determine whether corporation's attorney, present at all meetings with the buyer, was a section 12(2) seller); McFarland v. Memorex Corp., 581 F. Supp. 878 (N.D. Cal. 1984) (substantial participant test applicable to determine section 12(2) liability of stock issuer and issuer's president).

For cases in which no liability was found under the substantial factor test, see, e.g., *In re* Victor Technologies Sec. Litig., [1986–87 Transfer Binder] Blue Sky L. Rep. ¶ 72,491 (N.D. Cal. Jan. 8, 1987) (defendant examined and prepared financial statements included in stock registration statement and prospectus); Fine v. Rubin, 623 F. Supp. 171 (N.D. Cal. 1985) (defendants drafted stock registration statement and prospectus, dealing only with underwriters); *In re* Activision Sec. Litig., 621 F. Supp. 415 (N.D. Cal. 1985) (issuer and its officers and directors set stock prices, negotiated underwriting agreement, helped in presentations to brokers and analysts, etc.); *In re* Fortune Sys. Sec. Litig., 604 F. Supp. 150, 162 (N.D. Cal. 1984) (issuer prepared registration statement but was not directly involved in the "*particular* sales transaction to the *particular* plaintiff") (emphasis in original); *In re* Diasonics Sec. Litig., 599 F. Supp. 447 (N.D. Cal. 1984) (issuer's officers and directors prepared stock registration statement and arranged financing but did not play substantial role in sales process); Hudson v. Capital Management Int'l, Inc., [1982–83 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 99,222 (N.D. Cal. Aug. 24, 1982) (attorneys and accountants prepared opinions in offering statements but did not participate in selling process). *But see In re* Wickes Companies, Inc. Sec. Litig., [1982–83 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 99,056 (S.D. Cal. Jan. 6, 1983) (section 12(2) participant liability claim could be stated against accountants who prepared financial statements used in offering materials).

114. As early as 1940, the First Circuit expanded section 12(2) liability to include not only sellers in privity with buyers but also stock brokers soliciting sales transactions on behalf of others. Cady v. Murphy, 113 F.2d 988 (1st Cir.), *cert. denied,* 311 U.S. 705 (1940). *See generally* O'Hara, *supra* note 58, at 933–46. No significantly broader expansion occurred until Lennerth v. Mendenhall, 234 F. Supp. 59 (N.D. Ohio 1964), in which a stock seller's agent, who met personally with buyers to solicit sales, was held liable as a seller for "proximately" causing the transactions. The Fifth Circuit subsequently adopted the *Lennerth* proximate-cause test in Hill York Corp. v. American Int'l Franchises, Inc., 448 F.2d 680 (5th Cir. 1971).

115. In an early case applying a substantial factor test, the Fifth Circuit expanded section 12(2) liability to include franchise promoters who had no direct involvement in actual sales transactions but who were "the motivating force" behind the sale. *Hill York,* 448 F.2d at 693. Subsequent Fifth Circuit cases, however, have been less expansive, with liability attaching only where defendants are directly involved in sales transactions. *See, e.g.,* Junker v. Crory, 650 F.2d 1349 (5th Cir. 1981) (attorney who actively negotiated merger transaction held liable as seller); Croy v. Campbell, 624 F.2d 709 (5th Cir. 1980) (attorney who gave negligent tax advice to investors not held liable as seller because advice was not a substantial factor in investment decision); Pharo v. Smith, 621 F.2d 656 (5th Cir. 1980) (major stockholder did not play substantial role in sales of stock to other investors prior to anticipated public offering). *See generally* O'Hara, *supra* note 58, at 961–74; Rapp, *Expanded Liability Under Section 12 of the Securities Act: When Is a Seller Not a Seller?,* 27 CASE W. RES. L. REV. 445 (1977).

adopting the rhetoric of substantial participation[116] or of traditional strict privity,[117] have similarly found liability only where the defendants were involved in a face-to-face selling process with buyers or where the defendants passed title.[118]

If the *Haberman* court had looked more closely at the facts in the federal cases, the court would have realized that WSA seller liability claims against WPPSS, its members, the Participants and the professional consultants should have been dismissed. Federal case law would mandate dismissal unless actual title passed from WPPSS or the other defendants or unless they played active, personal roles in face-to-face negotiations or solicitations leading directly to the specific sales transactions. In *Haberman,* only the underwriters passed title. No claims of personal, face-to-face involvement were asserted against any defendants.[119]

In addition to incorrectly interpreting federal case law, the Washington Supreme Court also acted prematurely. The *Haberman* court recognized that the United States Supreme Court has not addressed the "split" in the federal circuits on section 12(2) seller liability.[120]

116. *See, e.g.,* Foster v. Jesup & Lamont Sec. Co., 759 F.2d 838 (11th Cir. 1985) (underwriter who did not directly communicate with buyer and who made only one comment to buyer's accountant regarding parties to transaction not held liable as seller), *modified on other grounds,* 782 F.2d 901 (11th Cir. 1986); Davis v. Avco Fin. Services, Inc., 739 F.2d 1057 (6th Cir. 1984) (finance company manager who, in face-to-face transactions, loaned money to finance pyramid scheme investments held liable as seller), *cert. denied,* 470 U.S. 1005, *cert. denied,* 472 U.S. 1012 (1985); Stokes v. Lokken, 644 F.2d 779 (8th Cir. 1981) (attorney who rendered opinion to auditor whose audit report was included in materials advertising sale of precious metals not held liable as seller); Lawler v. Gilliam, 569 F.2d 1283 (4th Cir. 1978) (broker who actively solicited stock orders held liable as section 12(1) seller); Katz v. Amos Treat & Co., 411 F.2d 1046 (2d Cir. 1969) (brokerage firm and attorney could be held liable for actively soliciting stock sales); *In re* WICAT Sec. Litig., 600 F. Supp. 1236 (D. Utah 1984) (issuer in firm commitment underwriting not held liable as seller).

117. *See, e.g.,* Sanders v. John Nuveen & Co., 619 F.2d 1222 (7th Cir. 1980) (firm commitment underwriter that owned stock sold to plaintiff held liable as seller), *cert. denied,* 450 U.S. 1005 (1981); Collins v. Signetics Corp., 605 F.2d 110 (3d Cir. 1979) (issuer in firm commitment underwriting not held liable as seller); Beck v. Cantor, Fitzgerald & Co., 621 F. Supp. 1547 (N.D. Ill. 1985) (broker who sold common stock and accounting firm that audited issuer's financial statements not held liable as sellers because neither passed title).

118. "In each of the cases the parties have cited to this Court [in urging application of the substantial factor test], substantial participation has been found only where the defendant has engaged in [a] high degree of individual effort to sell the security and *usually has been in actual contact with the plaintiff.*" *In re* Fortune Sys. Sec. Litig., 604 F. Supp. 150, 161 (N.D. Cal. 1984) (emphasis added).

119. *See* First Amended Complaint in Intervention of American Express Company Subsidiaries and Restated Demand for Jury Trial, Haberman v. WPPSS (King County Super. Ct. Mar. 29, 1985) (No. 84-2-06452-8); First Amended Complaint in Intervention of United States Trust Company of New York, Trustee[,] and Restated Demand for Jury Trial, Haberman v. WPPSS (King County Super. Ct. Mar. 29, 1985) (No. 84-2-06452-8).

120. Haberman v. WPPSS, 109 Wash. 2d 107, 127, 744 P.2d 1032, 1050 (1987).

Yet the court ignored the fact that the federal substantial factor test is certain to obtain United States Supreme Court review shortly.[121] Given the Supreme Court's recent history of using a strict statutory construction approach to limit liability,[122] the Washington court may be forced to reconsider its views soon.

C. Inconclusiveness of Other States' Laws

Although the *Haberman* court used federal case law in its analysis, the court acknowledged the futility of drawing any parallels from other states' laws. Other states' decisions were "inconclusive," according to the court, and federal courts' interpretations of other states' statutes reflected a "federal analysis of section 12(2) as applied to the state law in question" rather than state court analysis.[123] Although the court emphasized earlier in the *Haberman* opinion the goal of uniformity with other states' laws, it recognized that the laws of other states displayed a remarkable lack of uniformity.[124]

The diverse interpretations of state seller liability laws exist not only because state courts have interpreted similar statutes differently,[125] but also because of significant variation in the express language and construction of state statutes.[126] Even in states adopting the Uniform Securities Act, state legislatures have freely modified the Uniform

121. Dahl v. Pinter, 787 F.2d 985, *reh'g denied,* 794 F.2d 1016 (5th Cir. 1986), *cert. granted,* 107 S. Ct. 1885 (1987). Although considering section 12(1) rather than section 12(2), the Fifth Circuit in *Dahl* appended a new requirement to its test for seller liability: Not only must the alleged seller have been a substantial factor in the sales transaction, but the seller must also have "received or hoped to receive some financial benefit from his efforts." *Id.* at 990. On April 20, 1987, the Supreme Court agreed to review *Dahl.* 107 S. Ct. 1885.

122. *See* Admiralty Fund v. Jones, 677 F.2d 1289, 1294 n.3 (9th Cir. 1982) ("the broad reading of 'seller' may be in some doubt in light of recent Supreme Court cases that prescribe a strict statutory construction approach to the securities acts and reject their expansion with tort and criminal theories"); *see also* Touche Ross & Co. v. Redington, 442 U.S. 560, 578 (1979); SEC v. Sloan, 436 U.S. 103, 116 (1978); O'Hara, *supra* note 58, at 924–25 & n.12, 986, 987–1001. *But see* Herman & MacLean v. Huddleston, 459 U.S. 375, 383, 386–87 (1983).

123. *Haberman,* 109 Wash. 2d at 129, 744 P.2d at 1050, 1051.

124. *Id.* at 129, 744 P.2d at 1050. The dissent argued that other courts' interpretations of state securities acts were not "inconclusive" but generally construed state statutes strictly in accordance with their plain language. *Id.* at 184, 744 P.2d at 1078 (Pearson, C.J., dissenting).

125. *Id.* at 129, 744 P.2d at 1050. As the *Haberman* court noted, the only two state courts construing statutes similar to WASH. REV. CODE § 21.20.430(1) (1987) have taken opposite approaches. *Haberman,* 109 Wash. 2d at 129, 744 P.2d at 1050. The Oklahoma Supreme Court refused to extend state seller liability to participants in Nikkel v. Stifel, Nicolaus & Co., 542 P.2d 1305 (Okla. 1975). The Minnesota Court of Appeals adopted the Eighth Circuit's substantial factor test for state seller liability in Anders v. Dakota Land & Dev. Co., 380 N.W.2d 862 (Minn. Ct. App. 1986).

126. " 'Language within a statute must be read in context with the entire statute and construed in a manner consistent with the general purposes of the statute.' " Chemical Bank v. WPPSS, 99 Wash. 2d 772, 782, 666 P.2d 329 (1983) (quoting Nationwide Papers, Inc. v.

Securities Act upon adoption and amended it later.[127] As a result, some state statutes provide express liability for underwriters who participate in sales transactions,[128] and some hold accountants, engineers and other professionals involved in sales transactions liable.[129] Others extend liability to participants or those who materially aid in a sale[130] and still others demand strict privity between buyer and seller.[131]

D. The Pretense of "Uniformity" Among Securities Laws

One rationale for the *Haberman* court's adoption of a substantial contributive factor test was the need for uniformity between Washington law and the laws of federal and other state jurisdictions.[132] While many state and federal securities laws assert that uniformity is needed,[133] Washington, like other states, has ignored this goal by repeatedly revising WSA.[134] Even minor changes in form moved the Washington statutes slightly further away from strict uniformity with the Uniform Securities Act. When the *Haberman* court used "uniformity" to support its argument that WSA seller liability should be interpreted similarly to other state courts' interpretations of other states' Uniform Securities Act-derived statutes, the court ignored the legislature's demonstrated rejection of absolute strict "uniformity."

Another flaw in the court's rationale for adopting a substantial contributive factor test is its use of the Official Comments to the 1985 revised Uniform Securities Act.[135] The Washington legislature adopted neither the Official Comments accompanying the original Uniform Securities Act[136] nor the revised Uniform Securities Act and

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Northwest Egg Sales, Inc., 69 Wash. 2d 72, 76, 416 P.2d 687, 689 (1966)), *reconsidered and aff'd,* 102 Wash. 2d 874, 691 P.2d 524 (1984), *cert. denied,* 471 U.S. 1065, 1075 (1985).

127. *See supra* note 19.

128. *See, e.g.,* Shofstall v. Allied Van Lines, Inc., 455 F. Supp. 351, 358 (N.D. Ill. 1978) (Illinois statute).

129. *See, e.g.,* Koehler v. Pulvers, 614 F. Supp. 829, 846 (S.D. Cal. 1985) (California statute).

130. *See, e.g.,* Xaphes v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 597 F. Supp. 213 (D. Me. 1984) (Maine statute); Crane v. Courtright, 2 Ohio App. 2d 125, 206 N.E.2d 913 (Ohio Ct. App. 1964) (Ohio statute); Fakhrdai v. Mason, 72 Or. App. 681, 696 P.2d 1164 (Or. Ct. App.), review denied, 299 Or. 314, 702 P.2d 1111 (1985) (Oregon statute).

131. *See, e.g., In re* North Am. Acceptance Corp. Sec. Cases, 513 F. Supp. 608 (N.D. Ga. 1981) (Georgia statute); Ging v. Parker-Hunter, Inc., 544 F. Supp. 49 (W.D. Pa. 1982) (Pennsylvania statute).

132. Haberman v. WPPSS, 109 Wash. 2d 107, 125, 744 P.2d 1032, 1048–49 (1987) (citing Wash. Rev. Code § 21.20.900 (1987)).

133. *See, e.g.,* WASH. REV. CODE § 21.20.900 (1987).

134. *See supra* note 23 and accompanying discussion.

135. 7B U.L.A. 30 (Supp. 1987).

136. Securities Act of Washington, ch. 282, 1959 Wash. Laws 1311 (codified at WASH. REV. CODE § 21.20 (1987)).

Official Comments as promulgated by the National Conference of Commissioners on Uniform State Laws.[137] Yet the *Haberman* court turned to official comments appended to the revised act for additional authority to support its adoption of a substantial contributive factor test. The official comment to section 605(a) of the revised Uniform Securities Act would extend seller liability to a person whose participation is a substantial contributive factor in violating the act's provisions.[138] Stating that "this approach best promotes the legislative purpose behind the [WSA],"[139] the court effectively usurped legislative authority by "adopting" part of a proposed statute not yet considered by the legislature itself.

V. PROPOSALS TO CLARIFY SELLER LIABILITY LAW IN WASHINGTON

The trial court in *Haberman* properly dismissed all WSA seller liability claims against all defendants. The supreme court, in reversing the lower court's decision,[140] incorrectly broadened WSA's scope to include parties, other than direct sellers, who are substantial contributive factors in sales transactions. Until the legislature corrects the *Haberman* mistake or the court modifies its position, other courts and litigants should dissect the *Haberman* opinion to understand that the opinion's thrust was toward holding a specific issuer, WPPSS, liable. Fairness to both investors and professional consultants requires that the substantial contributive factor test for seller liability be applied in the same manner that other courts have applied it. Only where privity between buyer and seller exists or where active, face-to-face "participation" in the selling process occurs should liability attach.

137. *See* Haberman v. WPPSS, 109 Wash. 2d 107, 180, 744 P.2d 1032, 1077 (1987) (Pearson, C.J., dissenting); 7B U.L.A. 30 (Supp. 1987).

138. 7B U.L.A. 81 (Supp. 1987).

139. *Haberman,* 109 Wash. 2d at 130, 744 P.2d at 1051.

140. If the intervenors' complaints had supported certain allegations in their briefs on the motion to dismiss, the Washington Supreme Court could have reinstated seller liability claims without broadening WSA's scope. Intervenors' briefs contended that WPPSS and the other defendants made direct sales presentations to some of the complaining parties during tours of WPPSS facilities in the Pacific Northwest and meetings in New York prior to issuance of the bonds. Brief of Appellants American Express Company Subsidiaries and United States Trust Company at 15–16, Haberman v. WPPSS, 109 Wash. 2d 107, 744 P.2d 1032 (1987) (No. 52559-5). No such claims, however, were made in the underlying complaints. *See* First Amended Complaint in Intervention of American Express Company Subsidiaries and Restated Demand for Jury Trial, Haberman v. WPPSS (King County Super. Ct. Mar. 29, 1985) (No. 84-2-06452-8); First Amended Complaint in Intervention of United States Trust Company of New York, Trustee[,] and Restated Demand for Jury Trial, Haberman v. WPPSS (King County Super. Ct. Mar. 29, 1985) (No. 84-2-06452-8).

A clearer definition of "substantial contributive factor" would enhance the predictability of judgments on the issue of WSA seller liability. Adoption by Washington courts of federal court language that a defendant is a substantial factor "if he or she 'actively solicits an order, participates in the negotiations, or arranges the sale' "[141] would clarify the scope of the *Haberman* substantial contributive factor test.

The Washington legislature needs to clarify subsection 21.20.430(1) by an amendment[142] as follows:

> Any person, who offers or sells a security in violation of any provisions of RCW 21.20.010 or 21.20.140 through 21.20.230, is liable to the person buying the security from him or her. *Liability attaches under this subsection only (a) to a seller who has passed actual title to the security to the buyer or (b) to any person who has played an active, personal role in face-to-face negotiations or solicitations leading directly to the specific sales transaction at issue.* The buyer under this subsection may sue . . . .

The proposed new second sentence in subsection 21.20.430(1) would align Washington with the actual holdings of courts interpreting similar statutes. By specifying that direct contact must occur, it would aid professionals and other potential defendants in assessing the likelihood that their acts might incur seller liability in Washington, and it would avoid unwitting and innocent exposure to such liability by professionals in the ordinary course of their business.[143]

The legislature could also adopt a new provision holding an issuer liable for misrepresentations or omissions of material fact contained in registration statements or offering materials prepared by the issuer. Such liability could extend to all issuers, including issuers, like WPPSS, who sell securities via firm-commitment underwritings.

Legislative action such as this would send a clear message to the courts that, where liability is not available under revised WSA sections regarding seller/offeror, buyer or issuer provisions, liability properly

141. *In re* Activision Sec. Litig., 621 F. Supp. 415, 421 (N.D. Cal. 1985) (quoting Lawler v. Gilliam, 569 F.2d 1283, 1288 (4th Cir. 1978)); *see also* Lennerth v. Mendenhall, 234 F. Supp. 59, 65 (N.D. Ohio 1964) ("liability must lie somewhere between the narrow view, which holds only the parties to the sale, and the too-liberal view which would hold all who remotely participated in the events leading up to the transaction").

142. In amending WSA, the legislature should not blindly mimic the federal securities statutes. Rather, it should heed its own words in WASH. REV. CODE § 21.20.900 (1987) and "coordinate" with the federal scheme, not duplicate it.

143. Attention should be paid to the official draftsmen's commentary to the Uniform Securities Act's seller liability subsection: "Civil liability is an essential adjunct to a blue sky law. But by the same token it should be sufficiently precise . . . so that honest people will not be given the difficult choice of staying out of a state or subjecting themselves to uncertain and possibly ruinous liabilities." LOSS COMMENTARY, *supra* note 16, at 146.

attaches only to the categories of persons specified under section 430(3).

VI. CONCLUSION

The Washington Supreme Court's decision in *Haberman v. WPPSS* left seller liability law under the Securities Act of Washington in a state of disarray. Clearly, the decision expands seller liability. Less clear is the scope of that expansion. In reaching a result-oriented decision aimed at holding a specific bond issuer, WPPSS, liable as a seller, the court borrowed from federal law a "substantial contributive factor" test for seller liability. However, the court ignored the fact that other courts applying a substantial contributive factor test impose liability almost exclusively where defendants are directly involved in the sales process or pass title to the securities sold. By using the test to reinstate seller claims against not only issuer WPPSS but also against professional consultants who neither owned the bonds nor were directly involved in the sales, the *Haberman* court stretched seller liability law into previously uncharted territory. Yet rather than indicating specifically which of the professional consultants' acts made them vulnerable to seller claims, the court propounded vague "considerations" for determining liability that will require additional interpretation by future courts to gain practical meaning.

Professional consultants, issuers, investors and all others involved either directly or indirectly in the sale of securities need a clearer explanation of when seller liability attaches than that provided by the *Haberman* court. The Washington legislature should clarify this area by amending the seller liability statute to limit liability to persons who are directly involved in sales or who pass title to securities. Enactment of a new statute expressly providing for issuer liability could also eliminate some of the confusion. Until these legislative corrections are made, courts and litigants should apply the new substantial contributive factor test for seller liability only to defendants who engage in direct, face-to-face selling or who pass title to the securities sold.

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