

328 U.S. 293, *; 66 S. Ct. 1100, **;

90 L. Ed. 1244, ***; 1946 U.S. LEXIS 3159

SECURITIES & EXCHANGE COMMISSION v. W. J. HOWEY CO. ET AL.

No. 843 SUPREME COURT OF THE UNITED STATES

328 U.S. 293; 66 S. Ct. 1100; 90 L. Ed. 1244; 1946 U.S. LEXIS 3159; 163 A.L.R. 1043

May 2, 1946, Argued

May 27, 1946, Decided

Case write up #1

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Facts:

Respondents are W. J. Howey Company and Howey-in-the-Hills Service, Inc., both Florida corporations under common management. W. J. Howey Company owns a large area of citrus lands in Lake County, Florida where they've been planting 500 acres of citrus trees every year in recent years. Half of the land is owned by the company while half is sold to the public offering benefit opportunities from more harvest. Land is usually sold in narrow strips and each acre consists of 48 trees. From 02/1941 to 05/1943 31 out of 42 customers bought land less than 5 acres each and the average of their land purchase was 1.33 acres. To indicate, the price of land depends on the quantity of years the land has been planted with citrus trees. 85% of 3-year land sales ended on May 31, 1943, were accompanied by service contracts. Harvesting and marketing services are offered by Howey-in-the-Hills Service, Inc.

While the purchaser is free to choose other service companies, the superiority of Howey-in-the-Hills Service Inc service's company's superiority is stressed. Its service contract is made for 10 years giving full ownership and discretion to the company. Out of 51 purchasers 42 entered a service contract. Company maintains skilled personnel and equipment - 75 tractors, sprayer wagons, fertilizer trucks and etc.

Profits in 1943-1944 amounted to 20%, 10% return was to be expected in the 10-year period. The buyers are generally not Florida residents and have no interest in managing the crop, and many are patrons of the resort owned by the Howey Company. After full payment, the land is transferred to the buyer under a warranty deed. The purchased plots are not separated by fences, and information about the property can only be found in a plat book record.

It's been revealed that the mails and instrumentalities of interstate commerce were used in the offer and sale of land and service contracts which violates 5(a) of the Securities Act of 1933 (then "Act"). But both District and Circuit court denied the injunction.

Section 2 (1) of the Act defines a security to be documents traded for investments or speculation whereas investment contract is defined as a contract or scheme for "the placing of capital or laying out of money in a way intended to secure income or profit from its employment." State v. Gopher Tire & Rubber Co., 146 Minn. 52, 56, 177 N. W. 937, 938.

Procedural posture:

The District Court denied the injunction to restrain the respondents from using the mails and instrumentalities of interstate commerce in the offer and sale of unregistered and non-exempt securities in violation of § 5 (a) of the Act and the Fifth Circuit Court of Appeals upheld this decision. Lower courts

bring up the argument that the existence of an "investment contract" had to be made independently by the District Court and it found against its existence. 60 F.Supp. 440. The Circuit Court of Appeals for the Fifth Circuit confirmed that finding.

The case is brought up to Supreme Court with petitioners who argued that the given action is considered an investment contract and respondents should be restrained from using the mails and instrumentalities of interstate commerce in the offer and sale of unregistered and non-exempt securities in violation of § 5 (a) of the Act.

Issue:

The legal question to be decided by the Supreme court is whether a land sales contract, warranty deed and a service contract by W. J. Howey Company and Howey-in-the-Hills Service, Inc. are investment contract within the meaning of Section 2 (1) and if it violates 5 (a) of the Act which restrains the sale of unregistered and non-exempt securities unless the security is granted an exemption under 3 (b).

Holding:

Yes. The Court decided indeed the land purchase and sale contract, the warranty deed and the service contract together constitute an "investment contract" within the meaning of 2 (1). It requires compliance with the registration requirements of 5(a) unless the security is exempt under 3(b).

Reasoning:

Most of the facts are stipulated. The Court determined that the investment contracts in this case take the form of land sales contracts, warranty deeds and service contracts. I agree with Court's decision. First, the fact that purchasers had a choice not to make a service contract is weak to disprove the presence of an investment contract. Most purchases, 85% were covered by service contracts. Conditions under the service contract are quite strict. It gives full ownership and discretion to Howey over the cultivation, harvesting and marketing of the crops. Purchasers are people who don't get involved in the management of land or harvest but share the profit and benefit from the efforts of the promoter or Howey. These circumstances indicate that the components of a profit-oriented business venture existed, with the promoters (Howey) overseeing, directing, and running the enterprise. Land sales contracts and warranty deeds are a convenient method to determine the purchasers'/investor's respective shares of the profits. Sales and service contracts under these circumstances meet the definition of securities set by Securities Act: investment contract is a contract, transaction, or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party. Thus, sale of unregistered and non-exempt securities violates 5 (a) of the Act. It requires compliance with the registration requirements of 5(a) unless the security qualifies for an exemption under 3(b).

Dissent:

A dissenting argument is that the conception of an "investment contract" is broadly defined by SEC in 2 (1) of the Securities Act. He states that it was upon the District Court to independently decide whether the existence of an "investment contract" and it found against its existence. He argues that both the District Court and the Fifth Circuit Court of Appeals found that the contracts in question did not constitute an investment contract and he call to respect these findings. Furthermore, he describes the transparency of the purchase and sale process and recalls that customers were not necessitated to make service contracts. The dissenting viewpoint is that the

existence of similar arrangements that are used to circumvent the Securities Act does not necessarily imply that the current contracts were evasive too.

Critique:

I don't agree with the decision of the Supreme court. Even if the arrangements made by Howey and their customers resemble the definition of an investment contract, I think there is more and deeper to study from other perspectives. First, it offers freedom of choice to a purchaser whether to sign a service contract or not. This means if the purchaser doesn't want to sign a service contract, then the purchaser becomes a landowner and has freedom of how to exploit her or his own land. I think Howey's company should not be subject to scrupulous securities regulation and incur expenses because of it.

It was a win-win contract between Howey and its customers who didn't want to get involved in cultivating land and harvesting but it was easy for them to trust their land to a well-established company and share the benefits.