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SECURITIES LAW

A REMEDY WITHOUT A RIGHT: THE NINTH CIRCUIT DENIES A PRIVATE RIGHT OF ACTION UNDER SECTION 17(A) OF THE SECURITIES ACT OF 1933

I. INTRODUCTION

In *In Re Washington Public Power Supply System Securities Litigation*¹ the Ninth Circuit overruled² its previous plaintiff position³ by holding that a private plaintiff does not have an implied right of action under the broad antifraud provisions of section 17(a) of the Securities Act of 1933.⁴ With this

1. 823 F.2d 1349 (9th Cir. 1987)(en banc)(per Hall, J.; the other panel members were Anderson, J., Brunetti, J., Kennedy, J., Kozinski, J., Nelson, J., Norris, J., Thompson, J., Wiggins, J., and Tang, J., dissenting). A partial settlement was announced on September 10, 1987. *The Wall Street Journal*, September 11, 1987, at 3, col. 3. Under the terms of the settlement, which is still subject to court approval, four brokerage firms and other syndicates that underwrote Washington Public Power Supply System's \$2,250,000,000 bond offering agreed to pay bondholders \$92,000,000 to settle a class action lawsuit. *Id.* In reaching the settlement the defendants did not admit or concede fault or liability regarding allegations that the bonds were sold with official statements that were materially misleading. *Id.* Thus, the settlement does not affect the issues discussed in this note. *Id.* A jury trial involving all remaining defendants is scheduled to start in September 1988. *Id.*

2. *In re Washington Pub. Power Supply Sys. Sec. Litig.*, 823 F.2d at 1358 [hereinafter *WPPSS*].

3. *Stephenson v. Calpine Conifers II Ltd.*, 652 F.2d 808 (9th Cir. 1981). *See infra* note 20 and accompanying text.

4. 15 U.S.C. § 77q(a)(1982) provides:

It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails directly or indirectly -

(1) to employ any device, scheme or artifice to defraud, or
(2) to obtain money or property 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

holding, the Ninth Circuit has joined a growing trend among the circuits.⁵ The Supreme Court has not yet ruled on this question,⁶ but it has placed heavy restrictions on a private right of action under section 10(b) of the Securities Exchange Act of 1934⁷ which is very similar to section 17(a). The restrictive view toward a private right of action under section 17(a) adopted by the Ninth Circuit further circumscribes the opportunities for a private plaintiff to recover damages suffered in a fraudulent or misleading securities transaction.

II. FACTS

Plaintiffs purchased bonds issued by the Washington Public Power Supply System (WPPSS). The proceeds were used to finance the construction of two nuclear power plants, WPPSS 4 and WPPSS 5.⁸ WPPSS is a joint action agency consisting of 19 public utility districts and the cities of Ellensburg, Richland, Seattle and Tacoma, which are all located in the State of Washington.⁹ WPPSS issued a total of \$2.25 billion of debt between 1977 and 1981 and became the nation's largest issuer of tax-free mu-

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

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

5. See *infra* note 55 and accompanying text.

6. The Supreme Court has expressly reserved this question on five separate occasions. *Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 304 n.9 (1985); *Herman & MacLean v. Huddleston*, 459 U.S. 375, 378 n.2 (1983); *Aaron v. SEC*, 446 U.S. 680 (1979); *International Brotherhood of Teamsters v. Daniel*, 439 U.S. 551, 557 n.9 (1979); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 734 n.6 (1975).

7. 15 U.S.C. § 78j(b)(1982) provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange-

. . . .

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance 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.

8. WPPSS, 823 F.2d at 1350.

9. SHEARSON/AMERICAN EXPRESS, INC. *Washington Public Power Supply System Straight Answers To The 30 Most Asked Questions*. (1983).

municipal bonds.¹⁰ Plagued by huge construction cost overruns and uncertain demand for the power plants' output, all construction on plants 4 and 5 was suspended in January 1982¹¹ and eventually terminated.¹² In July 1983, WPPSS defaulted on the WPPSS 4 and WPPSS 5 bond obligations, creating the largest municipal bond default in United States history.¹³ Alleging that the bonds were sold in violation of both federal and state securities laws, plaintiffs filed a class action suit against WPPSS and nearly 200 other defendants on behalf of themselves and all others who purchased the bonds between February 23, 1977 and June 15, 1983.¹⁴

In the fall of 1983 defendants moved to dismiss plaintiffs' section 17(a) claims.¹⁵ Judge Browning vacated the substantive motions previously ruled upon by Judge Bilby¹⁶ and granted the defendants' motion to dismiss all of plaintiffs' section 17(a) claims on December 3, 1985.¹⁷ Recognizing that this decision conflicted with the then prevailing Ninth Circuit authority, Judge Browning certified his interlocutory order for immediate appeal pursuant to 28 U.S.C. section 1292(b).¹⁸ Plaintiffs then successfully petitioned the Ninth Circuit for permission to file an interlocutory appeal.¹⁹ Relying on *Stephenson v. Calpine Co-*

10. The Wall Street Journal, July 26, 1983, at 3, col. 1.

11. The Wall Street Journal, March 6, 1983, at 18, col. 1.

12. The Wall Street Journal, January 27, 1984, at 6, col. 1.

13. The Wall Street Journal, July 26, 1983, at 3, col. 1.

14. WPPSS, 823 F.2d at 1349.

15. In re Washington Pub. Power Supply Sys. Sec. Litig., 623 F. Supp. 1466 (W.D.Wash.1987). District Judge Richard Bilby denied the motion in December 1983. WPPSS, 823 F.2d at 1350. In January 1985, Judge Bilby learned that his father and stepmother owned \$100,000 in WPPSS bonds. *Wash. Pub. Power Supply Sys.*, 623 F. Supp. at 1470. Because of this possible conflict of interest, Judge Bilby recused himself and was replaced by District Judge William Browning. WPPSS, 823 F.2d at 1350.

16. WPPSS, 623 F. Supp. at 1470.

17. *Id.* at 1474.

18. 28 U.S.C. § 1292(b)(1984) provides:

When a district judge, in making in a civil action an order not otherwise appealable under this section, shall be of the opinion that such order involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation, he shall so state in writing in such order. The Court of Appeals may thereupon, in its discretion, permit an appeal to be taken from such order. . . .

19. WPPSS, 823 F.2d at 1350.

nifers II Ltd.,²⁰ the Ninth Circuit granted plaintiffs' motion for a summary reversal of District Judge Browning's dismissal of the section 17(a) claims.²¹ An en banc rehearing was then granted to reconsider the right of private plaintiffs to bring an action pursuant to section 17(a) under *Stephenson*.²²

III. BACKGROUND

The Ninth Circuit's decision in *WPPSS* denying a private right of action under section 17(a) of the Securities Act of 1933 continues a trend²³ away from an expansive approach to judicially implied private rights of action. A previous, liberal attitude is exemplified by the Supreme Court's 1964 ruling in *J.I. Case v. Borak*.²⁴ In *Borak*, the Supreme Court recognized an implied right of action in the proxy provisions of the 1934 Securities Exchange Act.²⁵ It held that such private remedies were necessary to ensure full disclosure in shareholder proxy statements.²⁶ Citing investor protection as the chief purpose of the 1934 Act,²⁷ the Court stated that individual lawsuits were

20. *Stephenson v. Calpine Conifers II Ltd.*, 652 F.2d 808 (9th Cir. 1981)(plaintiffs, investors in a failed limited partnership, brought an action under the Securities Act of 1933 and under certain California statutes). The *Stephenson* court held that a private cause of action exists under § 17(a) of the Securities Act of 1933, codified at 15 U.S.C. 77q(a)(1976).

21. *WPPSS*, 823 F.2d at 1350.

22. *Id.*

23. See *infra* note 55, and accompanying text.

24. 377 U.S. 426 (1964). *Borak* involved a civil action brought for alleged deprivation of preemptive rights by reason of a merger effected through use of a false and misleading proxy statement. *Id.* at 429. The Supreme Court held that private suits are permissible under § 27 of the Securities Exchange Act of 1934 for violations of § 14(a). The Court stated that the federal courts will provide the remedies required to carry out the congressional purpose. *Id.* at 430-31, 33-35.

25. *Id.* at 431-33. Section 14(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78n(a)(1982), 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 any national securities exchange or otherwise to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security (other than an exempted security) registered on any national securities exchange in contravention of such rules and regulations as the [Securities and Exchange] Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

26. *Borak*, 377 U.S. at 432.

27. *Id.* While the Court conceded that Congress did not explicitly declare that pri-

valuable enforcement mechanisms which aided the SEC as it sought to review thousands of proxy solicitations each year.²⁸ The Warren Court's pro-plaintiff stand on implied private rights of action is best expressed in *Borak* when it stated that it is the duty of the courts to provide remedies whenever necessary to effectuate Congress' purpose.²⁹

This expansive attitude was again exhibited in *Wyandotte Transportation Co. v. United States*.³⁰ Citing *Borak* as authority, the Court stated that civil actions were proper when plaintiffs fell within the class that the statute was designed to protect and when the harm that occurred was the type that the statute was intended to forestall.³¹

Private rights of action have ebbed considerably³² from the *Borak* holding since the Supreme Court decided *Cort v. Ash*³³ in 1975. In *Cort*, the Burger Court established a four-part test for a judicial finding for an implied private right.³⁴ The first part of the test requires the plaintiff to be "one of the class for whose especial benefit the statute was created."³⁵ The second factor is congressional intent. That is, is there any indication that Congress explicitly or implicitly intended either to create such a remedy or to deny one?³⁶ Third, the entire surrounding legislative scheme must be examined to see whether a finding of a private cause of action would disrupt Congress' statutory struc-

vate plaintiffs should have a private right of action under § 14(a), the congressional reference to "the protection of investors" was sufficient for the Court to imply the "availability of judicial relief where necessary to achieve that result." *Id.*

28. *Borak*, 377 U.S. at 432.

29. *Id.* at 433.

30. 389 U.S. 191 (1967). *Wyandotte* involved the assertion of in personam rights by the federal government against the owners of two vessels negligently sunken in navigable waterways. *Id.* at 193.

31. *Id.* at 202.

32. See *infra* notes 45-49 and accompanying text. See also Pillai, *Negative Implication: The Demise of Private Rights of Action in the Federal Courts*, 47 U. CIN. L. REV. 1 (1978); Note, *A New Direction for Implied Causes of Action*, 48 FORDHAM L. REV. 505 (1980); Note, *Implied Private Actions Under Federal Statutes - the Emergence of a Conservative Doctrine*, 18 WM. & MARY L. REV. 429 (1976).

33. 422 U.S. 66 (1975) (plaintiff stockholder brought action for damages and injunctive relief under the Federal Election Campaign Act Amendments of 1974, 18 U.S.C. § 610 (1982), which prohibit corporate contributions in specific federal elections).

34. *Cort*, 422 U.S. at 69.

35. *Id.* at 78, quoting *Texas & Pac. R. Co. v. Rigsby*, 241 U.S. 33, 39 (1916).

36. *Cort*, 422 U.S. at 78.

ture.³⁷ Lastly, a determination must be made whether the cause of action is one traditionally relegated to state law, in an area basically the concern of the states, so that it would be inappropriate to infer a cause of action based solely on federal law.³⁸

After *Cort*, the Supreme Court amplified and modified its restrictive stance regarding implied private rights of action in *Touche Ross & Co. v. Reddington*,³⁹ when it cautioned courts to be wary of broadening causes of action beyond those intended by Congress.⁴⁰ In *Reddington*, the Court decided that each part of the *Cort* test was not of equal weight.⁴¹ Instead, the central inquiry was whether Congress intended, either expressly or by implication, to create a private right of action.⁴² This narrow posture was reiterated in *Transamerica Mortgage Advisers, Inc. v. Lewis*,⁴³ where the Court stated that rules of construction re-

37. *Id.*

38. *Id.*

39. 442 U.S. 560 (1978). Plaintiff, trustee in the liquidation of a failed securities firm brought suit under § 17(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78q(a) (1970), which requires every member of a national securities exchange to keep such books and records as the Securities and Exchange Commission deems necessary for the protection of investors. *Id.* at 563. Defendant was the independent auditor of the securities firm. *Id.* Plaintiff alleged that the accountant's improper audit contributed to the losses suffered by customers of the securities firm. *Reddington*, 442 U.S. at 564-66. In holding that no private right of action existed under § 17(a) of the Securities Exchange Act, the Court declared that the statute's purpose was to provide the SEC with early warning of a securities firm's financial collapse and could not be construed to confer a private right of action. *Id.* at 568-71. The Court also found that the statute's legislative history was entirely silent on whether such a right existed and that other sections of the 1934 Act contained explicit private causes of action. *Id.* at 571. In particular, it noted that § 18(a) of the 1934 Act, 15 U.S.C. § 78r(a)(1976) provides the principal express civil remedy for misstatements in reports but limits it to purchasers and sellers of securities. *Id.* at 573-74.

40. *Reddington*, 442 U.S. at 574.

41. *Id.* at 575. *But see Id.* at 579-89 (Brennan, J., concurring); *Id.* at 580 (Marshall, J., dissenting).

42. *Id.* at 575-76. The Court noted that the first three factors of the *Cort* test were the traditional inquiries into legislative intent. *Id.* Moreover, this inquiry was determinative. *Id.* Once answered in the negative the entire discussion of a private right of action was at an end. *Id.*

43. 444 U.S. 11 (1979). Plaintiff, a shareholder in Mortgage Trust of America (Trust) brought a derivative action on behalf of Trust and a class action on behalf of Trust's shareholders against Trust and its investment adviser alleging fraud and breach of fiduciary duty. *Id.* at 13. The Supreme Court held that the Investment Adviser's Act of 1940, 15 U.S.C. § 80b-1-80b-21 (1982), did not confer an implied private right for damages. The Court stated that though the clients of investment advisers were the intended beneficiaries of the statute, enforcement through private actions for damages would unduly extend the remedies of rescission and restitution that Congress intended. *Lewis*, 444 U.S. at 16-17.

quired that where a statute expressly provides a particular remedy, a court must be careful of reading others into it.⁴⁴

Following the restrictive *Cort* standard, the Court has been very reluctant to find an implied private right of action in statutes where none was expressly provided. The *Cort* analysis as amplified and refined in *Reddington* and *Lewis* has had a broad effect, denying private rights of action under the Federal Water Pollution Control Act and the Marine Protection, Research, and Sanctuaries Act,⁴⁵ section 10 of the Rivers and Harbors Appropriations Act,⁴⁶ section 1 of the Davis-Bacon Act,⁴⁷ section 1302 of the Indian Civil Rights Act,⁴⁸ and section 14(e) of the 1934 Securities Exchange Act dealing with unsuccessful tender offers.⁴⁹ One of the few exceptions to this trend was *Cannon v.*

44. *Lewis*, 444 U.S. at 19. Supporting this proposition, the Court cited *Botany Mills v. United States*, 278 U.S. 282, 289 (1928): "When a statute limits a thing to be done in a particular mode, it includes the negative of any other mode."

45. *Middlesex County Sewerage Auth. v. National Sea Clammers Ass'n*, 453 U.S. 1 (1981). Plaintiffs, an organization of fishermen, brought suit against various governmental entities complaining of sewage being discharged into waterways. *Id.* at 4-5. The Court held that neither the Federal Water Pollution Control Act, 33 U.S.C. § 1251-1376 (1982), nor the Marine Protection Research and Sanctuaries Act of 1972, 33 U.S.C. § 1401-45 (1982), granted a private right of action. Both acts contained elaborate enforcement mechanisms, including express citizen-suit provisions, and thus it "cannot be assumed that Congress intended to authorize additional judicial remedies." *Middlesex County*, 453 U.S. at 13-14.

46. *California v. Sierra Club*, 451 U.S. 287 (1981). An environmental organization and two other private plaintiffs sought enforcement of § 10 of the Rivers and Harbors Act of 1899. *Id.* at 289. The Supreme Court ruled that the general prohibition of certain activities does not indicate any intent by Congress to provide a private right of action. *Id.* at 297-98.

47. *Universities Research Ass'n v. Coutu*, 450 U.S. 754 (1981). In *Coutu*, plaintiff brought suit against former employer alleging violation of the Davis-Bacon Act, 40 U.S.C. § 276a(a) (1982), which requires contractors on federal construction projects to pay laborers the prevailing local wage. *Coutu*, at 757. The Supreme Court held that it was not Congress' intent to grant an implied private right of action. *Id.* at 771-73.

48. *Santa Clara Pueblo v. Martinez*, 436 U.S. 49 (1978). In *Martinez*, a female member of an Indian tribe brought action seeking declaratory and injunctive relief against enforcement of a tribal ordinance denying membership in the tribe to children of female members who married outside the tribe, while extending membership to children of male members who married outside the tribe. *Id.* at 51. In holding that no private right of action exists under the Indian Civil Rights Act of 1968, 25 U.S.C. §§ 1301-03 (1982), the Court stated that such a right "would be at odds with the congressional intent of protecting tribal self-government." *Martinez*, 436 U.S. at 64.

49. *Piper v. Chris-Craft Indus.*, 430 U.S. 1 (1977). Chris-Craft Industries was the unsuccessful tender offeror for control of a corporation and brought suit for damages and injunctive relief alleging violations of § 14(e) of the 1934 Exchange Act. *Id.* at 4. The Supreme Court held that a private right of action was not necessary to effectuate Congress' intent under § 14(e). *Id.* at 37-41.

University of Chicago,⁵⁰ a Title IX action where a female plaintiff alleged that she was denied admission to the medical schools of two private universities on the basis of her sex.⁵¹ There the Court held that the plaintiff overcame each part of the *Cort* test quite easily because: (1) Title IX explicitly recognized the class of which plaintiff was a member as the group for whose benefit the measure was enacted; (2) the legislative history of Title IX clearly indicated Congress' intention that a private right of action should be recognized by the courts; (3) the recognition of a private right of action, far from disrupting the overall legislative scheme, would further its underlying purpose by providing individual citizens with effective protection against discriminatory practices and; (4) anti-discriminatory measures have been the province of the federal government since the enactment of the Civil War amendments.⁵²

The issue as to whether a private plaintiff should have standing to sue for being defrauded or misled in the offer or sale of securities under section 17(a) of the 1933 Securities Act remains an open one,⁵³ with many circuits and lower courts recognizing such an action,⁵⁴ but a trend to the contrary appears to be

50. 441 U.S. 677 (1979).

51. *Id.* at 680.

52. *Id.*

53. R. JENNINGS & H. MARSH, *SECURITIES REGULATION: CASES AND MATERIALS*, 63, (6th ed. 1987).

54. Many circuit and district courts have recognized an implied right of action under § 17(a) of the Securities Act of 1933. *See Stephenson, supra* note 20 at 815; *Kirshner v. United States*, 603 F.2d 234 (2nd Cir. 1978), *cert. denied*, 442 U.S. 909 (1979)(retired schoolteacher sought order compelling retirement board to exchange poorly-rated, low-yield Municipal Assistance Corporation bonds for higher yielding bonds issued by creditworthy corporations); *Daniel v. International Bhd. of Teamsters*, 561 F.2d 1223 (7th Cir. 1977), *reversed on other grounds*, 439 U.S. 551 (1979)(union member brought action against local union to recover for misrepresentations made concerning his rights in pension plan); *Newman v. Prior*, 518 F.2d 97 (4th Cir. 1975)(purchasers of oil and gas production interests brought action against seller alleging fraud in the sale of securities); *Lanza v. Drexel & Co.*, 479 F.2d 1277, 1280 n.2 (2nd Cir. 1973)(in action for compensatory and punitive damages against former officers and directors of failed construction firm with whom plaintiff merged, the court held that requirements for a private cause of action under § 17(a) were identical to those under Rule 10b-5); *Simmons v. Wolfson*, 428 F.2d 455 (6th Cir. 1970), *cert. denied*, 400 U.S. 999 (1971)(action by stockholders to recover value of stock for alleged conspiracy of corporate officers and directors to sell shares at a profit after manipulating market in violation of § 17(a), § 10(b) and Rule 10b-5); *Kellman v. ICS Inc.*, 447 F.2d 1305 (6th Cir. 1970)(purchaser of common stock brought suit for damages over refund offered by corporation claiming that refund did not adequately measure consideration originally paid for such shares as promised by the corporation); *Jacobs v. McCrory*, [1986 Transfer Binder] Fed. Sec. L. Rep.

growing.⁵⁵

(CCH) ¶ 92,893 (D. Md. 1986)(investors brought action against adviser alleging violations of § 17(a), § 10(b) and Rule 10b-5 for misrepresenting the nature and volume of their investments); *Ackerman, Jablonski, Porterfield & DeTure v. Alhadeff*, [1986 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 92,756 (W.D. Wash. 1986)(investors in an oil and gas limited partnership brought suit against its organizers and its auditors alleging the prospectus contained misrepresentations); *Levine v. Futransky*, 636 F. Supp. 899 (N.D. Ill. 1986)(beneficiaries/trustees of various trusts brought suit against investment adviser to recover losses arising from latter's unauthorized, risky trading strategy); *Onesti v. Thomson McKinnon Sec., Inc.*, 619 F. Supp. 1262 (N.D. Ill. 1985)(plaintiffs brought suit against securities firm for allegedly misrepresenting the riskiness of its investment recommendations and for charging excessive commission fees; in finding an implied right of action under § 17(a), the court cited the minimal differences between § 17(a) of the 1933 Act and § 10(b) of the 1934 Act); *Dannenberg v. Dorison*, 603 F. Supp. 1238 (S.D.N.Y. 1985). In *Dannenberg*, investors sued to recover damages sustained from investment in a fraudulent limited partnership tax shelter, alleging that the offering memorandum was false and misleading since the partnership never intended to engage in mining activities necessary for creation of tax benefits. The court declined to allow private actions based on negligence despite the Supreme Court's ruling in *SEC v. Aaron*, 446 U.S. 680 (1980), that in an SEC enforcement action negligence was a sufficient basis to state a claim under § 17(a)(2) and § 17(a)(3). See also *Nunes v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 609 F. Supp. 1055 (D. Md. 1985)(investor brought suit against securities firm under § 17(a), § 10(b), Rule 10b-5 and the Racketeer Influenced and Corrupt Practices Act, 18 U.S.C §§ 1961-68 (1982) for excessive and unauthorized transactions which resulted in more than \$50,000 in commission expenses); *Excalibur Oil, Inc. v. Sullivan*, 616 F. Supp. 458 (N.D. Ill. 1985)(investors in oil and gas leases brought suit against attorney alleging misrepresentation as leases were encumbered by numerous judgment and mechanics liens, mortgages and assignments when attorney claimed, with knowledge of their existence, that no such encumbrances existed); *First Interstate Bank of Nevada v. National Republic Bank of Chicago*, [1984-85 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 91,994 (N.D. Ill. 1985)(bondholders of defaulted issue claimed fraud and misrepresentation due to defendants' failure to disclose the financial interests of defendants in the properties to be developed with bond proceeds); *Hanratty v. Ostertag*, 470 F.2d 1096 (10th Cir. 1972)(plaintiff suffered financial loss by following defendant's advice in exchanging all of his shares in one firm for a larger number of shares in another).

55. Several circuit and district courts have refused to find an implied right of action under § 17(a) of the 1933 Securities Act. See *Barnes v. Resource Royalties, Inc.*, 795 F.2d 1359 (8th Cir. 1986)(investor claimed that he was fraudulently induced by defendant to purchase unregistered securities on the pretext that the corporations in which he was investing were developing and marketing new products); *Landry v. All Am. Assurance Co.*, 688 F.2d 381 (5th Cir. 1982)(purchasers of bank common stock brought suit against underwriters and bank executives alleging that financial statements of bank were misrepresented); *Shull v. Dain, Kalman & Quail, Inc.*, 561 F.2d 152 (8th Cir. 1977), *cert. denied*, 434 U.S. 1086 (1978)(customer sued brokerage firm and its branch manager to recover losses sustained in allegedly unauthorized stock speculation); *Greater Iowa Corp. v. McLendon*, 378 F.2d 783 (8th Cir. 1967)(plaintiff corporation alleged that dissident shareholders violated § 5 of the Securities Act of 1933 by not registering voting trust certificates with the Securities and Exchange Commission and § 17(a) by making allegedly fraudulent statements in solicitation material); *Citizens State Bank v. FDIC*, 639 F. Supp. 758 (W.D. Okla. 1986)(bank which bought loan participations brought securities fraud action against selling bank); *Mursau Corp. v. Florida Penn Oil & Gas, Inc.*, 638 F. Supp. 259 (W.D. Pa. 1986)(investor in oil and gas limited partnership sued promoter alleging nondisclosure of material facts); *David K. Lindemuth Co. v. Shannon Fin. Corp.*,

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A private right of action under section 17(a) hardly seemed to matter when section 10(b) of the 1934 Exchange Act was seen as embodying a readily available implied right. Frequently, section 17(a) was a mere "tag along" to a Rule 10b-5 claim.⁵⁶ Due to the high degree of similarity in the language employed by the two statutes, a private plaintiff, defrauded in the purchase or sale of a security, was readily able to state a cause of action under section 10(b) of the Exchange Act.⁵⁷ Section 17(a) actions brought by private plaintiffs were on occasion dismissed for being redundant when accompanied by a section 10(b) action.⁵⁸ In *Osborne v. Mallory*,⁵⁹ the first case to recognize a private right of

637 F. Supp. 991 (N.D. Cal. 1986)(purchasers of shares in pipe inspection equipment sued sellers alleging that inflated value of and market for such equipment constituted securities fraud); *Memphis Hous. Auth. v. Paine, Webber, Jackson & Curtis, Inc.*, 639 F. Supp. 108 (W.D. Tenn. 1986)(investor sued brokerage firm alleging failure to disclose risks and safeguard investor's interests, encouragement of excessive speculation and churning of account for commission income); *Schriner v. Bear, Stearns & Co.*, 635 F. Supp. 373 (N.D. Cal. 1986)(buyer of revenue bonds brought action against seller after issuer of bonds declared bankruptcy); *In re Storage Technology Corp. Sec. Litig.*, 630 F. Supp. 1072 (D. Colo. 1986)(plaintiffs alleged officers and directors of computer manufacturer concealed and misrepresented firm's financial condition and progress of new product development); *Akers v. Bonfasi*, 629 F. Supp. 1212 (M.D. Tenn. 1985)(franchisee brought action against franchisor of mobile telephone equipment alleging violations of securities laws, Racketeer Influenced and Corrupt Organizations Act, and state consumer protection laws); *Braun v. Stifel, Nicolaus & Co.*, 445 F. Supp. 141 (E.D. Mo. 1978), *aff'd*, 600 F.2d 139 (8th Cir. 1979)(customer sued brokerage firm alleging, *inter alia*, that defendant misrepresented the riskiness of plaintiff's investment portfolio). *See also*, Pillai, *Negative Implication: The Demise of Private Rights of Action in the Federal Courts*, 47 U. CIN. L. REV. 1 (1978).

56. *See Hazen, A Look Beyond the Pruning of Rule 10b-5: Implied Remedies and Section 17(a) of the Securities Act of 1933*, 64 VA. L. REV. 641, 648 (1978).

57. A private right of action under § 10(b) of the Exchange Act was first recognized in *Kardon v. National Gypsum Co.*, 69 F. Supp. 512 (E.D. Pa. 1946), and was sanctioned by the Supreme Court in *Herman & MacLean v. Huddleston*, 459 U.S. 375 (1983).

58. *See, e.g., Globus v. Law Research Servs., Inc.*, 418 F.2d 1276 (2d Cir. 1969). In *Globus*, shareholders charged the president of a corporation and an underwriter of a stock issue with federal securities law violations and common law fraud in connection with the offering circular accompanying the offer of the sale of stock. *Id.* at 1278-79. The court did not answer whether § 17(a) by itself would support a private right of action for compensatory damages since its affirmation of the lower court's ruling on this issue could stand under § 10(b). *Id.* at 1283; *See also Schaeffer v. First Nat'l Bank*, 509 F.2d 1287, 1293 (7th Cir. 1975), *cert. denied*, 425 U.S. 943 (1976). In *Schaeffer*, victims of a stock market manipulation brought an action against brokerage and stock exchange for fraud and misrepresentation in violation of federal securities laws. *Id.* at 1290. The court stated that where § 17(a) has been concurrently pleaded with a sufficient Rule 10b-5 claim, courts should refrain from ruling on the sufficiency of the § 17(a) claim. *Id.* at 1293. *See also Greater Iowa Corp. v. McLendon*, 378 F.2d 783 (8th Cir. 1967). *See also* H. BLOOMENTHAL, *SECURITIES LAW HANDBOOK*, (1985).

59. 86 F. Supp. 869 (S.D.N.Y. 1949). The purchasers of common stock brought action against sellers claiming fraud and misrepresentation in violation of federal securities

action under section 17(a), the Second Circuit's reasoning was little more than a recognition of this similarity.⁶⁰ In denying defendant's motion to dismiss, the court in *Osborne* merely determined that the reasons for implying liability under section 10(b) were equally applicable to section 17(a).⁶¹ So long as the section 10(b) remedy was readily available to defrauded investors and other participants in the securities markets, the existence of a similar private action under section 17(a) or lack thereof made little practical difference.⁶² This relationship eroded dramatically in the 1970s when the Supreme Court began limiting the section 10(b) private right of action by adding restrictions and qualifications.

In *Blue Chip Stamps v. Manor Drug Stores*,⁶³ the Supreme Court adopted a standing requirement first imposed by the Second Circuit in 1952 in *Birnbaum v. Newport Steel Corp.*⁶⁴ Plaintiffs claimed in *Birnbaum* that they would have purchased the securities in question were it not for defendants' misleading and pessimistic prospectus.⁶⁵ There, the Second Circuit held that a section 10(b) private plaintiff had to be either a purchaser or seller of the securities in question.⁶⁶ In doing so, the Second Circuit gave a strict interpretation to the "in connection with the purchase or sale of any security" language contained in the 1934 Act.⁶⁷

laws. *Id.* at 871. The court held that civil liability is implied under section 17(a) for fraudulent and deceptive practices in the sale of securities and a remedy is available despite the absence of specific language. *Id.* at 879.

60. *Osborne*, 86 F. Supp. at 879.

61. *Id.* Other cases adopting the analogy approach of *Osborne* are *Dack v. Shanman*, 227 F. Supp. 26 (S.D.N.Y. 1964), *Pfeffer v. Cressaty*, 223 F. Supp. 756 (S.D.N.Y. 1963), and *Thiele v. Shields*, 131 F. Supp. 416 (S.D.N.Y. 1955).

62. See Horton, *Section 17(a) of the 1933 Securities Act - The Wrong Place for a Private Right*, 68 Nw. U.L. Rev. 44 nn. 12-15 (1973).

63. 421 U.S. 723 (1975). In *Blue Chip Stamps*, defendant corporation issued a prospectus which, plaintiffs alleged, was misleading due to its unjustified pessimistic earnings forecast. *Id.* at 726. Shares of common stock were being offered through a prospectus to retailers at discounted prices pursuant to a settlement of a civil antitrust action brought by the United States. *Id.* at 726. Plaintiffs alleged that the gloomy prospectus was designed to discourage the retailers from purchasing the shares so that the shares could then be offered to the public at a higher price. *Id.* at 727.

64. 193 F.2d 461 (2nd Cir. 1951), *cert. denied*, 343 U.S. 956 (1952) (in action for fraud the court held that Rule 10b-5 provided a remedy only to actual purchasers and sellers of securities).

65. *Birnbaum*, 193 F.2d at 462-63.

66. *Id.* at 463.

67. 15 U.S.C. § 78j(b) (1982).

In *Blue Chip Stamps*, Justice Rehnquist, writing for a divided court focused on four factors.⁶⁸ First, the legislative history showed that Congress rejected attempts to include something less than a completed sale or purchase.⁶⁹ Second, allowing a broader basis for standing for implied rights of action under rule 10b-5 would be inconsistent with the remedies explicitly included in the Securities Act of 1933 and the Securities Exchange Act of 1934.⁷⁰ Third, a large body of case law supported the *Birnbaum* rule.⁷¹ Lastly, as a matter of public policy there was a strong need to avoid vexatious litigation that would result if mere offerees could bring suit.⁷²

Justice Powell's concurrence emphasized a literal interpretation of the statutory language.⁷³ He characterized the plaintiff's arguments as a plea for judicial reconstruction of section 10(b) to include offers along with purchases and sales⁷⁴ and stated that such an alteration could only be made with the unmistakable support in the legislation's history and structure.⁷⁵ Finding none⁷⁶ and concerned as well about the chilling effect of overturning *Birnbaum* on the capital markets,⁷⁷ Justice Powell

68. *Blue Chip Stamps*, 421 U.S. at 731-46.

69. *Id.* at 731-33.

70. *Id.* at 731-36. The Court noted that § 11(a) of the 1933 Act confines the express cause of action to persons "acquiring such security." *Id.* at 736. Section 12 of the 1933 Act provides a remedy limited to purchasers. *Id.* Section 9 of the 1934 Act, which prohibits a variety of fraudulent and manipulative devices, limits its express remedy to purchasers and sellers in transactions violating the provision. *Id.* Lastly, § 18 of the 1934 Act, prohibiting false and misleading statements in documents filed with the Securities and Exchange Commission, provides a remedy available only to purchasers and sellers. *Id.*

71. *Blue Chip Stamps*, 421 U.S. at 731-32.

72. *Id.* at 737-46. The Court allowed that actual damages as required by § 28(a) of the 1934 Act, 15 U.S.C. § 78bb(a)(1982), in all private actions may be difficult to prove. However, in the normal case involving actual purchasers and sellers, such damages usually have a tangible basis in the number of shares bought or sold. *Blue Chip Stamps*, 421 U.S. at 742. In contrast, the claim of the plaintiff in *Blue Chip Stamps*, whose claim was based on a non-contractual opportunity to buy or sell, suffered only an intangible economic injury and recovery would have involved a number of shares grounded only on plaintiff's uncorroborated oral evidence. *Id.* at 746. The Court stated that a more generous standing criterion would frustrate or delay normal business activity and would open the door to nuisance or strike suits, the resolution of which would be reduced to unverifiable oral recollections. *Id.* at 741-43.

73. *Blue Chip Stamps*, 421 U.S. 723, 755 (1975) (Powell, J., concurring).

74. *Id.* at 756.

75. *Id.*

76. *Id.*

77. *Id.* at 760.

rejected plaintiff's arguments by deferring any standing expansion to Congress.⁷⁸

Justice Blackmun in dissent characterized the *Birnbaum* standing restriction as a mechanical requirement quite out of keeping with the broad antifraud protection afforded by Congress when it drafted section 10(b).⁷⁹ He chided the majority's pursuit of expediency, convenience and ease⁸⁰ and offered, as a substitute for *Birnbaum*, a standing requirement satisfied by a showing of a "logical nexus between the alleged fraud and the sale or purchase of a security."⁸¹

The restriction imposed in *Blue Chip Stamps* has drawn both support⁸² and criticism⁸³ from commentators. The Supreme Court's ruling in *Blue Chip Stamps* seemed to put an end to the numerous exceptions to the *Birnbaum* rule created by the lower courts.⁸⁴ These exceptions had led commentators to predict the rule's demise.⁸⁵ However, there still remain some exceptions to the Court's restrictive standing criteria.⁸⁶

78. *Id.*

79. *Id.* at 765 (Blackmun, J., dissenting).

80. *Id.* at 770.

81. *Id.*

82. See Gallagher, *10b-5 After Blue Chip Stamps: How Stands the Judicial Oak?*, 80 DICK. L. REV. 1 (1975).

83. See Note, *Section 17(a) of the 1933 Securities Act: An Alternative to the Recently Restricted Rule 10b-5* 9 RUT.-CAM. L.J. 340 (1977). The author argues that the standing requirement adopted by the Court contradicts the broad remedial purposes of the 1933 Act and severely reduces the number and type of defrauded plaintiffs able to seek such relief under Rule 10b-5. *Id.* at 343. See also Hazen, *A Look Beyond the Pruning of Rule 10b-5: Implied Remedies and Section 17(a) of the Securities Act of 1933*, 64 VA. L. REV. 641 (1978). The author notes with irony that the fear of vexatious litigation was unfounded in *Blue Chip Stamps* since the terms of the underlying antitrust consent decree could have easily limited the class of plaintiffs. *Id.* at 661 n.102.

84. See, e.g., *James v. Gerber Prods. Co.*, 483 F.2d 944 (6th Cir. 1973) (beneficiaries of a trust from which securities were sold had standing to sue); *Crane Co. v. Westinghouse Air Brake Co.*, 419 F.2d 787 (2d Cir. 1969), *cert. denied*, 400 U.S. 822 (1970) (standing extended to tender offeror who suffered a defeat due to deception and manipulation of defendant); *Tully v. Mott Supermarkets, Inc.*, 337 F. Supp. 834 (D.N.J. 1972) (shareholders ousted from control of the corporation by means of an allegedly illegal conspiracy involving a sale of securities had standing to sue).

85. See e.g., Bradford, *Rule 10b-5: The Search for a Limiting Doctrine*, 19 BUFFALO L. REV. 268 (1968); Comment, *Another Demise of the Birnbaum Doctrine: "Tolls the Knell of Parting Day?"*, 25 U. MIAMI L. REV. 131 (1970).

86. W. CARY AND M. EISENBERG, *CASES AND MATERIALS ON CORPORATIONS*, 808 (1980). Among the exceptions retaining some vitality are those involving forced sellers, pledgors or pledgees, and the plaintiff seeking injunctive relief. *Id.*

The standing requirement imposed by *Blue Chip Stamps* was supplemented by a scienter criterion when the Supreme Court decided *Ernst and Ernst v. Hochfelder*⁸⁷ in 1976. In *Hochfelder*, the Supreme Court held that the independent auditors of a fraudulent securities firm were not subject to section 10(b) liability for simple negligence in conducting an audit.⁸⁸ A defrauded purchaser or seller of securities has to allege some higher standard of fault, either recklessness or intentional wrongdoing in order to state a cause of action.⁸⁹ The Court noted that section 10(b) prohibited the "use or employment of 'any manipulative or deceptive device or contrivance' in contravention of Commission rules."⁹⁰ It focused on the words "manipulative or deceptive" in holding that Congress intended only to proscribe conduct involving a higher state of culpability than mere negligence.⁹¹

Lastly, in 1977 the Supreme Court in *Santa Fe Industries v. Green*⁹² disallowed a section 10(b) action on the basis that the plaintiff failed to allege an act of "manipulation or deception."⁹³ According to the majority, a short-form merger carried out with full disclosure does not violate section 10(b) or Rule 10b-5 despite the lack of prior notice or any justifiable business pur-

87. 425 U.S. 185 (1976). The plaintiffs, customers of a fraudulent securities firm, brought a section 10(b) action against firm's accountants for negligent failure to uncover fraud. *Id.* at 189-90. The Supreme Court held that no private right of action exists under § 10(b) of the 1934 Act absent an allegation of scienter. *Id.* at 208-10.

88. *Id.* at 186.

89. *Id.* at 188. The Court defined scienter as an intent to defraud, deceive or manipulate. It expressly left open, however, whether reckless behavior constituted scienter. *Id.* at 193.

90. *Id.* at 197.

91. *Id.*

92. 430 U.S. 462 (1977). Minority investors in a corporation 95% owned by Santa Fe Industries (SFI) brought suit under § 10(b) and Rule 10b-5 claiming SFI's buyout offer of \$150 per share, although supported by an independent appraisal, was inadequate and represented an attempt to freeze-out the minority shareholders at an unfair price. *Id.* at 467. The Court held: (1) only conduct involving manipulation and deception is reached by § 10(b) or Rule 10b-5. *Id.* at 471-74; (2) the SFI offer fully complied with applicable state law and thus was not deceptive or manipulative. *Id.* at 474-77; and 3) to hold that plaintiffs' allegations constituted fraud would federalize corporate law, an area better left to the states. *Id.* at 477-80.

93. *Id.* at 473. The Court noted that "manipulation" when used in connection with the purchase or sale of securities, generally refers to "practices . . . that are intended to mislead investors by artificially affecting market activity." *Id.* No deception was found by the Court due to the lack of omissions or misstatements in the prospectus accompanying the notice of merger. *Id.*

pose.⁹⁴ The Court concluded that as a matter of statutory interpretation, no evidence existed showing Congress intended to prohibit corporate activities which lacked manipulative or deceptive conduct.⁹⁵ Justice White, writing for the majority, rejected the argument that “fraud” found in Rule 10b-5 but not section 10(b), brought breaches of fiduciary duty within the scope of federal securities laws.⁹⁶ The Court stated that the Securities and Exchange Commission, in promulgating rules under section 10(b), was limited by the language of that statute.⁹⁷ The Court ruled that state created causes of action for mismanagement and other breaches of fiduciary duty were not cognizable under section 10(b).⁹⁸

IV. THE COURT’S ANALYSIS

A. THE MAJORITY

With this as its background, the Ninth Circuit in *WPPSS*⁹⁹ concluded that its previous decision in *Stephenson v. Calpine Conifers II Ltd.*¹⁰⁰ was incorrect and was no longer controlling precedent in its circuit.¹⁰¹ In *Stephenson*, the Ninth Circuit had held that a private cause of action existed under section 17(a) and had relied on *Kirshner v. United States*,¹⁰² a Second Circuit opinion. The *Kirshner* court, in turn, had based its decision on *SEC v. Texas Gulf Sulphur Co.*¹⁰³ In *Texas Gulf Sulphur*, Judge Friendly stated in a concurring opinion that there was no real reason for denying the existence of an action under section

94. *Id.* at 468.

95. *Id.* at 473.

96. *Id.* at 472-73.

97. *Id.* at 472.

98. *Id.* at 477, 479-80.

99. *In re Washington Pub. Power Supply Sys. Sec. Litig.*, 823 F.2d 1349 (9th Cir. 1987).

100. 652 F.2d 808 (9th Cir. 1981). *See supra* note 20.

101. *WPPSS*, 823 F.2d 1349 at 1351.

102. 603 F.2d 234, 241 (2nd Cir. 1978), *cert. denied*, 442 U.S. 909 (1979). *See supra* note 54. The Second Circuit recognized a private cause of action under § 17(a) stating that the language of that statute was broad enough to imply such a right. *Id.*

103. *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 867 (2nd Cir. 1968) (Friendly, J., concurring), *cert. denied*, 394 U.S. 976 (1969). In *Texas Gulf Sulphur*, corporate insiders who purchased stock based on undisclosed material information were held liable for violations of § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b)(1982), under the “disclose or abstain” doctrine. *Id.* at 849.

17(a) once a plaintiff established a private action under section 10(b) of the Securities Exchange Act of 1934. The *Kirshner* court, and indirectly, the Ninth Circuit in *Stephenson*, relied on this portion of Judge Friendly's opinion. Omitted from the *Kirshner* opinion, however, was Judge Friendly's proviso that "fraud as, distinct from mere negligence, must be alleged."¹⁰⁴

The Ninth Circuit, in reversing *Stephenson*, found this omission particularly important in light of the elevated standards for a private cause of action under section 10(b) that the Supreme Court had imposed in *Blue Chip Stamps*, *Hochfelder*, and *Santa Fe Industries*.¹⁰⁵ The Ninth Circuit concluded that to permit section 17(a) actions to be governed by the lesser negligence action as it had when it relied on *Kirshner* would be to allow plaintiffs to circumvent the Supreme Court's higher standards for culpability under section 10(b).¹⁰⁶ Acknowledging the flawed reasoning underlying its previous position, along with the narrowed scope of implied private rights, the Ninth Circuit reversed *Stephenson*.¹⁰⁷

The Ninth Circuit continued its re-examination by declaring that it had erred in *Stephenson* by not following the criteria established by the Supreme Court in *Cort v. Ash*.¹⁰⁸ for determining whether a private right of action should be implied from a congressional statute that is silent on the matter.¹⁰⁹ In particular, the Ninth Circuit focused on the second and third prongs of *Cort*, citing these factors as the determinative elements according to *Reddington* and another recent Supreme Court affirmation of *Cort*.¹¹⁰ The Ninth Circuit did not decide whether plaintiffs in *WPPSS* satisfied the first prong of the *Cort* test because their failure to show congressional intent and harmony with the

104. *Kirshner*, 603 F.2d at 241.

105. *Ernst and Ernst v. Hochfelder*, 425 U.S. 185 (1976). *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975). *Santa Fe Industries v. Green*, 430 U.S. 462 (1977).

106. *WPPSS*, 823 F.2d at 1352.

107. *Id.* at 1358.

108. 422 U.S. 66 (1975). *See supra* note 33 and accompanying text.

109. *Id.* at 78. *See supra* notes 33-38 and accompanying text.

110. *Massachusetts Mut. Life Ins. Co. v. Russell*, 473 U.S. 134 (1985). In *Russell*, an employee of defendant insurance company sued under the Employee Retirement and Income Security Act (ERISA) and state law, alleging improper termination of disability benefits. *Id.* at 137. The Supreme Court held that no private right of action exists under ERISA due to strong evidence of legislative intent to the contrary. *Id.* at 148.

overall statutory program precluded, in the court's view, the recognition of a private cause of action under section 17(a).¹¹¹

The Ninth Circuit began its analysis of congressional intent, the second prong of the *Cort* test, by examining the "plain" language of section 17(a)¹¹² and determined that there simply was no indication, explicit or implicit, of legislative intent to create a private right of action under section 17(a).¹¹³ It read section 17(a) as representing merely a general censure of fraudulent practices.¹¹⁴ Moreover, the Ninth Circuit concluded that an examination of the statute's legislative history failed to support a private right of action.¹¹⁵ As pointed out in *Gunter v. Hutcheson*,¹¹⁶ when the House Committee Report listed the sections that created and defined the civil liabilities imposed by the 1933 Securities Act¹¹⁷ it referred only to sections 11 and 12.¹¹⁸ Congress felt that to impose a greater responsibility than that provided by these sections would unnecessarily hamper honest businessmen and provide no offsetting advantage to the public.¹¹⁹

In discussing legislative scheme, (the third prong to the *Cort* test), the majority cited the views of Professor Louis Loss. Professor Loss saw the 1933 Securities Exchange Act as a "neat

111. *WPPSS*, 823 F.2d at 1354.

112. *Id.*

113. *Id.* at 1355.

114. *Id.* at 1354. For authority, the court cited *Coutu*, 450 U.S. 754 (1981), wherein the Supreme Court held that a private right of action did not exist under the Davis-Bacon Act, 40 U.S.C. § 276a(a) (1982). In its discussion the Court in *Coutu* stated:

[T]he fact that an enactment is designed to benefit a particular class does not end the inquiry; instead it must also be asked whether the language of the statute indicates that Congress intended that it be enforced through private litigation . . . The Court has consistently found that Congress intended to create a cause of action 'where the language of the statute explicitly confers a right directly on a class of persons that includes the plaintiff in the case.'

Coutu, 450 U.S. at 771-72 (quoting *Cannon*, 441 U.S. 677 at 690 n.13 (1979), *supra* notes 50-52).

115. *WPPSS*, 823 F.2d at 1355.

116. 433 F. Supp. 42 (N.D. Ga. 1977). Action for fraud in the sale of stock in a bank. The district court, citing the restrictive *Cort* test and the requirements imposed in *Hochfelder*, *Blue Chip Stamps* and *Santa Fe Industries*, held that no private right of action should be implied under § 17(a) of the 1933 Act.

117. *Id.*

118. *Id.* at 44.

119. *Hutcheson*, 433 F. Supp. 42 (N.D. Ga. 1977) citing H.R. Rep. No. 85, 73d Cong., 1st Sess. 9-10 (1933).

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pattern" whose two substantive provisions, sections 5¹²⁰ and 17(a), had sections 11¹²¹ and 12(2)¹²² as their respective enforcement mechanisms.¹²³ According to Professor Loss, recognition of a private right of action under section 10(b) of the 1934 Act and Rule 10b-5 promulgated thereunder¹²⁴ makes sense, whereas a similar remedy under section 17(a) is impermissible because of the differing scope of the two acts.¹²⁵ While the 1933 Act deals

120. Section 5 of the 1933 Act, 15 U.S.C. § 77e (1982), makes it unlawful to sell any nonexempt security that is not registered with the Securities and Exchange Commission. *Id.*

121. Section 11 of the 1933 Act, 15 U.S.C. § 77k (1982), holds all participants in a registered offering under the Act potentially liable to purchasers of the securities for any material omissions or misstatements in the registration statement. *See Hazen, A Look Beyond the Pruning of Rule 10b-5: Implied Remedies and Section 17(a) of the Securities Act of 1933*, 64 VA. L. REV. 641, 644 n.14 (1978).

122. Section 12(2) of the 1933 Act, 15 U.S.C. § 77l(2) (1982), provides that a purchaser may sue a seller of securities for material misstatements or omissions made in the offer or sale of securities.

123. 3 L. LOSS, SECURITIES REGULATIONS 1785-86, (2d. ed. 1961).

124. Rule 10b-5 provides as follows:

It shall be unlawful for any person, directly or indirectly by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

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

17 C.F.R. § 240.10b-5 (1981).

125. Regarding the propriety of implying a private right of action under § 10(b) of the 1934 Act, and § 17(a) of the 1933 Act, Professor Loss explained the interrelationship of the statutory provisions as follows:

The question is simply whether there is the same justification for implying such liability under the 1933 Act as there is under the 1934 Act. It is one thing to imply a private right of action under § 10(b) or the other provisions of the 1934 Act, because the specific liabilities created by §§ 9(e), 16(b) and 18 do not cover all the variegated activities with which that Act is concerned. But it is quite another thing to add an implied remedy under § 17(a) of the 1933 Act to the detailed remedies specifically created by §§ 11 and 12. The 1933 Act is a much narrower statute. It deals only with disclosure and fraud *in the sale of securities*. It has but two important substantive provisions, §§ 5 and 17(a). Non-compliance with § 5 results in civil liability under § 12(1). Faulty compliance results in liability under § 11. And § 17(a) has its counterpart in § 12(2). It all

only with disclosure and fraud in the sale of securities, the 1934 Act is much broader and the specific liabilities expressly provided by Congress, sections 11 and 12(2), do not cover all the 1934 Act's substantive provisions.¹²⁶ To recognize a private right of action under section 17(a) would thus disrupt the balance of the 1933 Act by rendering section 11 entirely superfluous. Additionally, "the complex scheme which Congress wove in express civil liability sections would be totally undermined."¹²⁷

The last major portion of the majority opinion discussed the question of legislative re-enactment, a doctrine espoused in *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*.¹²⁸ This doctrine states "when Congress acts in a statutory context in which an implied remedy has already been recognized by the courts . . . the question is whether Congress intended to preserve the pre-existing remedy."¹²⁹ An implied remedy is seen as receiving tacit legislative support if it had been widely recognized by the

makes a rather neat pattern. Within the area of §§ 5 and 17(a), §§ 11 and 12 (unlike §§ 9(e), 16(b) and 18 of the 1934 Act) are all embracing. This is not to say that the remedies afforded by §§ 11 and 12 are complete. But the very restrictions contained in those sections and the differences between them . . . make it seem the less justifiable to permit plaintiffs to circumvent the limitations of § 12 by resort to § 17(a). Particularly is this so in view of the fact that § 11, together with the statute of limitations in § 13, was actually tightened in the 1934 amendments to the Securities Act. [Emphasis in original.]

3 L. LOSS, SECURITIES REGULATIONS 1785-86, (2d ed. 1961).

126. *Id.*

127. WPPSS, 823 F.2d 1349, 1355-56 quoting *Kimmel v. Peterson*, 565 F. Supp. 476, 487 (E.D. Pa. 1983). In *Kimmel*, the district court adopted the statutory construction and the reasoning of the courts who refused to imply a private right of action under § 17(a). *Id.* at 483. It applied its own *Cort* analysis and concluded that although § 17(a) met the first prong, namely, that purchasers of securities were among the class for whose especial benefit the statute was created, its failure to clear the second hurdle, legislative intent, proved fatal for the implied right. *Id.* at 487. The court in *Kimmel* also stated that the implication of a private right of action under § 17(a) would "undermine the complex and carefully crafted" legislative scheme found in the 1933 Act and would render §§ 11 and 12 superfluous. *Id.*

128. 456 U.S. 353 (1982). In *Curran*, a customer brought an action against a futures commissions merchant, alleging mismanagement, misrepresentations, and excessive "churning" in connection with the management of its account. *Id.* at 368. The Court focused on the state of the law when the statute was enacted and held that an implied private cause of action under the Commodity Exchange Act, 7 U.S.C. §§ 1-26 (1982) was a part of the contemporary legal context when Congress legislated in 1974. *Curran*, 456 U.S. at 392-95.

129. WPPSS, 823 F.2d at 1357.

courts at the time Congress re-enacted a substantive portion of the underlying statutes.¹³⁰ The majority in *WPPSS* distinguished *Curran* by stating that at the time Congress comprehensively revised the securities laws in 1975, the existence of a right of action for private plaintiffs under section 17(a) of the 1933 Securities Act was greatly disputed by the circuits.¹³¹ By contrast, in *Curran*, the Supreme Court held a private plaintiff's right to sue under the Commodity Exchange Act¹³² was part of the contemporary legal context in 1964 when Congress amended the Act at that time.¹³³

B. THE DISSENT

In his dissent,¹³⁴ Judge Tang conducted his own *Cort* analysis and concluded¹³⁵ that a private right of action is implied under section 17(a) of the Securities Act of 1933.¹³⁶ He began by stating that section 17(a) satisfies the first requirement of *Cort*, namely, that the plaintiff seeking the implied remedy be "one of the class for whose especial benefit the statute was enacted."¹³⁷ Judge Tang buttresses this conclusion by quoting language from the congressional debate over the 1933 Act to the effect that the legislation's main purpose is to protect the investing public by compelling disclosure of material facts and by preventing fraud and misrepresentation.¹³⁸

Judge Tang then proceeded to the second factor of the *Cort* test, legislative intent, and concluded that this too was satisfied

130. *Id.* at 1356.

131. *Id.*

132. 7 U.S.C. §§ 1-26 (1982).

133. *Curran*, 456 U.S. at 374-82. The Court also stated that the decision by Congress to leave intact the clauses under which courts had implied this private right of action implied a congressional intent to preserve the remedy. *Id.* at 384-87. The Court also found that the Act's legislative history supported this implication and clearly showed that purchasers and sellers of futures contracts were intended to have standing. *Id.* at 390. Due to these factors the Court held that a private plaintiff does have a right of action under the Commodity Exchange Act. *Id.* at 395.

134. *In re Washington Pub. Power Supply Sys. Sec. Litig.*, 823 F.2d 1349, 1358 (Tang, J., dissenting).

135. *Id.*

136. 15 U.S.C. § 77q(a) (1981).

137. *WPPSS*, 823 F.2d at 1358.

138. *Id.* at 1358 quoting 77 CONG. REC. 2923 (May 8, 1933) (remarks of Sen. Fletcher).

by section 17(a).¹³⁹ Though the statute's history offered little indication of Congress' intent,¹⁴⁰ Judge Tang found support for this conclusion by emphasizing the legislative re-enactment found in *Curran*.¹⁴¹ This doctrine is pertinent to the question of a private plaintiff's right of action under section 17(a) due to the comprehensive revision by Congress of the securities laws in 1975. At the time of this revision the Second, Third, Fourth, Fifth, Seventh, and Ninth Circuits accepted private plaintiffs' rights of action under section 17(a) either at the trial or appellate level.¹⁴² Had Congress intended to disavow any private right

139. *WPPSS*, 823 F.2d at 1358.

140. *Id.*

141. *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353 (1982). See *supra* note 128 and accompanying text.

142. *Dack v. Shanman*, 227 F. Supp. 26 (S.D.N.Y. 1964). *Shanman* involved an action for the return of the purchase price of securities. *Id.* at 28. Plaintiffs alleged violation of § 5(a) of the 1933 Act [interstate sale of securities prior to filing of a registration statement], violation of § 5(c) of the 1933 Securities Act [no registration statement] and violation of § 12 of the 1933 Act [untrue statements and material omissions in the prospectus] under § 17(a). *Id.* at 28-29. The district court held that a private right of action under § 17(a) is to be implied from the fact that the section makes it unlawful in the sale of securities to employ a scheme to defraud or to obtain money by means of untrue statements of material fact. *Id.* at 29. See also *Thiele v. Shields*, 131 F. Supp. 416 (S.D.N.Y. 1955). In *Thiele*, purchasers of municipal bonds brought an action for damages and rescission, alleging that the offering circular contained material misrepresentations concerning revenues to be generated by the project. *Id.* at 418. While noting that § 17(a) does not expressly provide for a private right of action, the district court held that such a right could be implied from prohibitions contained in this section. *Id.* at 419. The court also held that if a plaintiff could prove that defendant knowingly or intentionally misrepresented the bonds, a private plaintiff may maintain an action under Rule 10b-5 and § 17(a). *Id.* *Pfeffer v. Cressaty*, 223 F. Supp. 756 (S.D.N.Y. 1963). *Pfeffer* was a private action for damages incurred by purchasers of stock arising from defendant's false statements of material fact. *Id.* at 757. Citing *Osborne*, 86 F. Supp. 869 (S.D.N.Y. 1949) and *Thiele*, 131 F. Supp. 416 (S.D.N.Y. 1955), the court in *Pfeffer* held that a private right of action was no longer an open question in its district. *Pfeffer*, 223 F. Supp. at 757. *Wulc v. Gulf & Western Ind.*, 400 F. Supp. 99 (E.D. Pa. 1975). In *Wulc*, a corporate officer who held options to purchase stock in a corporation acquired by Gulf & Western brought action for violations of federal securities laws and common law fraud, alleging that Gulf & Western deceived him into supporting the merger by falsely assuring him of their willingness to assume liability for the stock options when they had no intention of doing so. *Id.* at 101-02. The district court, pointing to the "offer or sale" language of § 17(a) as the vital distinction between the antifraud provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934, granted standing to a private plaintiff under § 17(a). *Id.* at 103. See *Cromwell v. Pittsburgh and L. E. R. Co.*, 373 F. Supp. 1303 (E.D. Pa. 1972), in which minority shareholders brought suit against majority stockholder alleging violations of federal securities laws and state corporate law in the financing of railroad cars which were purchased from defendant by majority stockholder. *Id.* at 1305. After finding that conditional sales contracts constituted securities for purposes of the 1934 Act, the district court held that § 17(a) gives rise to a private right of action, stating that courts which have faced the issue squarely have come to this conclusion. *Id.*

of action under section 17(a) it surely would have done so expressly, particularly in light of the widespread recognition given to such claims in six of the federal circuits. Instead, Congress left section 17(a) unchanged.¹⁴³ It is unlikely that this was a mere oversight. Congress' silence on this issue, as stated by Judge Tang, "evidences an intent to preserve the remedy" already accepted by the courts.¹⁴⁴

The third part of the *Cort* test, consistency with the underlying purposes of the legislative scheme,¹⁴⁵ is also satisfied by a private right of action under section 17(a), according to Judge Tang.¹⁴⁶ Stating simply that the purpose of federal securities laws is the encouragement of private enforcement,¹⁴⁷ Judge Tang concluded that section 17(a) was consistent with the overall statutory scheme because private actions are effective enforcement mechanisms and necessary supplements to the actions of the Securities and Exchange Commission.¹⁴⁸ Moreover, the presence of explicit civil remedies in section 11¹⁴⁹ and section 12¹⁵⁰ of the 1933 Securities Act does not make a private right of action under section 17(a) redundant as contended by the majority.¹⁵¹

at 1310. *See also* Johns Hopkins Univ. v. Hutton, 488 F.2d 912 (4th Cir. 1973), *cert. denied*, 416 U.S. 916 (1974), in which a buyer sought rescission of the purchase of oil and gas production interests, alleging the seller had misrepresented and omitted material facts. *Larson v. Tony's Investments, Inc.*, [1967-69 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 92,324 (M.D. Ala. 1968). In *Larson*, class action plaintiffs sued for violations of federal securities laws claiming defendant sold unregistered securities in more than one state in violation of § 12(1) of the 1933 Act, and that the prospectus under which such securities were sold contained omissions of material facts, thus violating § 12(2) and § 17(a) of the 1933 Act. *Id.* at 97,530. The district court stated that the weight of authority supported a private right of action under § 17(a). *Id.* at 97,532. The court also noted that although plaintiffs' § 17(a)(2) theory was based on the same facts as their § 12(2) claim, the former was not duplicative since punitive damages are recoverable under § 17(a). *See* Hecht v. Harris, Upham & Co., 283 F. Supp. 417, 422 (N.D. Cal. 1968), *modified*, 430 F.2d 1202 (9th Cir. 1970) (action by customer against brokerage firm and its commodities manager for alleged violations of the Securities Act of 1933, the Securities Exchange Act of 1934, and the Commodity Exchange Act).

143. *WPPSS*, 823 F.2d at 1359 (Tang, J., dissenting).

144. *Id.*

145. *Cort*, 422 U.S. at 78.

146. *WPPSS*, 823 F.2d at 1359 (Tang, J., dissenting).

147. *Id.*

148. *Id.*, quoting *Bateman, Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 310 (1985).

149. *See supra* note 121.

150. *See supra* note 122.

151. *WPPSS*, 823 F.2d at 1359 (Tang, J., dissenting).

Judge Tang cited *Cannon v. University of Chicago*,¹⁵² for the proposition that the existence of explicit remedies in one or more sections of a complex statutory scheme should not preclude the implication of appropriate remedies under other sections.¹⁵³ Judge Tang concluded his independent analysis of a private right of action in section 17(a) under the *Cort* test by citing *Transamerica Mortgage Advisers v. Lewis*,¹⁵⁴ to support his conclusion that regulation of misconduct in the securities field is not a concern peculiar to the states.¹⁵⁵

The dissent ended by chiding the majority's technical and restrictive view of federal securities laws¹⁵⁶ and echoing Justice Blackmun's lament in *Blue Chip Stamps*,¹⁵⁷ that the "Court exhibits a preternatural solicitousness for corporate well-being and a seeming callousness toward the investing public quite out of keeping . . . with our own traditions and the intent of the securities laws."¹⁵⁸

V. CRITIQUE

The *Cort*¹⁵⁹ test for implication of a private cause of action was misapplied by the Ninth Circuit in *WPPSS*. Regarding the test's threshold requirement, namely, that the plaintiff be a member of the class for whose especial benefit the statute was enacted,¹⁶⁰ the court viewed section 17(a) as an undifferentiated whole and failed to look at each subsection separately.¹⁶¹ In *Cannon*¹⁶² the Supreme Court concluded that to satisfy the first prong of the *Cort* test a statute must explicitly confer a right on a class of persons that included the plaintiff.¹⁶³ The mere fact

152. 441 U.S. 677 (1979). *See supra* notes 50-52 and accompanying text.

153. *Id.* at 711.

154. 444 U.S. 11, 35 (1979). *See supra* notes 43-44 and accompanying text.

155. *WPPSS*, 823 F.2d at 1360 (Tang J., dissenting).

156. *Id.*

157. 441 U.S. 723 (1975). *See supra* notes 79-81 and accompanying text.

158. *WPPSS*, 823 F.2d at 1360-61 (Tang, J., dissenting) *quoting* *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 762 (1975) (Blackmun, J., dissenting).

159. *Cort v. Ash*, 421 U.S. 66 (1975).

160. *Id.* at 78.

161. *In re Washington Pub. Power Supply Sys. Sec. Litig.*, 823 F.2d 1349, 1359-60 (1987).

162. *Cannon v. University of Chicago*, 441 U.S. 677 (1979). *See supra* notes 50-52 and accompanying text.

163. *Id.* at 690 n.13.

that a class of persons benefit from the legislation is insufficient by itself to confer standing on private parties.¹⁶⁴ Instead, explicit congressional intent must be shown.¹⁶⁵ Subsection 17(a)(3), which prohibits fraud or deceit "upon the purchaser" specifically designates a particular group for protection while subsections 17(a)(1) and 17(a)(2) are general prohibitions with no particular beneficiary.¹⁶⁶ Those commentators that see section 17(a) fulfilling the first prong of the *Cort* test limit their affirmative finding to subsection 17(a)(3) and would grant standing to actual purchasers.¹⁶⁷ This result does not conflict with the standing rule adopted in *Blue Chip Stamps* and fulfills the requirement of sufficient specificity as set forth in *Cannon*.

The second part of the *Cort* test is an inquiry into congressional intent.¹⁶⁸ That is, does the legislation provide any indication, explicitly or implicitly, either to create such a remedy or to deny one.¹⁶⁹ An examination of section 17(a) reveals no intent to

164. *California v. Sierra Club*, 451 U.S. 287 (1981). See *supra* note 46 and accompanying text.

165. *Cannon*, 441 U.S. at 690 n.13.

166. 15 U.S.C. § 77q(a) (1982) provides:

It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails directly or indirectly -

(1) to employ any device, scheme or artifice to defraud, or

(2) to obtain money or property 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 light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Offerees are also protected by § 17(a), but the Supreme Court has denied standing to offerees in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975), *supra* note 63, and it is unlikely that the Court would deny standing to offerees under Rule 10b-5 only to allow it under § 17 (a). Although it is possible for the result in *Blue Chip Stamps* regarding offerees to be distinguished by the fact that Rule 10b-5 prohibits only fraudulent activity in connection with the purchase or sale of any security while § 17(a) explicitly covers offerees, the same concerns over vexatious litigation and problems of proof are present in both.

167. See Note, *Implied Private Rights of Action Under the Securities Act of 1933 Section 17(a)*, 14 J. OF L. REF. 563, 575 n.80 (1981); Note, *Section 17(a) of the Securities Act of 1933: Implication of a Private Right of Action*, 29 U.C.L.A. L. REV. 244, 258 n.92 (1981).

168. *Cort*, 422 U.S. at 78.

169. *Id.*

create a private cause of action and the statute's history lacks any such discussion.¹⁷⁰ When discussing civil liabilities under the Securities Act of 1933, Congress focused on sections 11 and 12.¹⁷¹ However, to imply that Congress intended to deny a private right of action would be to adopt the maxim of statutory construction, *expressio unius est exclusio alterius*, (the expression of one thing is the exclusion of others)¹⁷² which was rejected in *Cort*.¹⁷³

In favor of finding congressional intent to provide a right of action under section 17(a) is the fact that when Congress amended the federal securities laws in 1975 it left section 17(a) unchanged.¹⁷⁴ At that time, the majority of the circuits that had decided the issue were in favor of finding a private right of action under section 17(a).¹⁷⁵ Under the doctrine of statutory re-enactment as set forth by the Supreme Court in *Merrill Lynch, Pierce, Fenner and Smith v. Curran*,¹⁷⁶ these facts infer a congressional purpose to keep the private right of action under section 17(a) intact. At best, the legislative history of section 17(a), before and since its enactment, is inconclusive on the issue of congressional intent regarding a private right of action.¹⁷⁷ Without a more definitive showing that Congress intended to negate it, the second part of the *Cort* test will not prove fatal to a private right of action under section 17(a).¹⁷⁸

The third factor in the *Cort* test weighs the effect of an implied private right on the overall statutory scheme to insure that Congress' underlying purposes are preserved.¹⁷⁹ In later cases

170. H.R. REP. NO. 85, 73d Cong. 1st Sess. 9-10 (1933).

171. *Id.*

172. BLACK'S LAW DICTIONARY, 521 (5th ed. 1979).

173. *Cort*, 422 U.S. at 82 n.14.

174. *WPPSS*, 823 F.2d at 1359 (Tang, J., dissenting).

175. *See supra* note 142.

176. 456 U.S. 353 (1982). *See supra* note 128 and accompanying text.

177. *See Note, Section 17(a) of the Securities Act of 1933: Implication of a Private Right of Action*, 29 U.C.L.A. L. REV. 244, 259 n.106 (1981). The author considers the element of congressional intent a "neutral factor" in determining a private right of action under § 17(a) of the Securities Act of 1933. *Id.*

178. In *Cort*, 422 U.S. 65, the Supreme Court stated that in cases where the class of plaintiffs was clearly granted certain rights, legislative intent to create a private right of action need not be shown but an "explicit purpose to deny such cause of action would be controlling." *Id.* at 82.

179. *Id.* at 78.

the Court recast this inquiry in less demanding language, requiring only that the implication of a private remedy help accomplish the statutory purpose.¹⁸⁰ To the extent that a private right of action furthers the protection of investors without restricting the raising of capital or the conduct of honest business people, it aids the fulfillment of the statutory purpose. However, if a private right of action under section 17(a) conflicts with the statutory provisions where Congress explicitly granted a civil action to private plaintiffs, it would be inconsistent with the statutory scheme and fail to satisfy the third prong of *Cort*. Some commentators¹⁸¹ have objected to standing for private plaintiffs under section 17(a) on this basis. They argue that section 12(2)¹⁸² of the Securities Act of 1933 provides the remedy for a section 17(a) violation. To permit a separate action under section 17(a) would duplicate the remedy provided by section 12(2) but would lack its limitations.¹⁸³

The persuasiveness of this argument is undermined by the fact that the overlap between section 17(a) and section 12(2) is incomplete. Section 17(a) requires the plaintiff to sustain the burden of proof unlike section 12(2), which places the burden on the defendant. Section 17(a) also lacks the privity requirement found in section 12(2).¹⁸⁴ Lastly, section 12(2) is subject to the short one year statute of limitations found in section 13 while section 17(a) is not.¹⁸⁵

180. *Cannon v. University of Chicago*, 441 U.S. 677, 703 (1979).

181. 3 L. Loss, *SECURITIES REGULATION*, 1784-85 (2d ed. 1961).

182. *See supra* note 122.

183. Section 12(2) actions are subject to the one year statute of limitations found in § 13, 15 U.S.C. § 77m (1982), and are also subject to a privity requirement, 15 U.S.C. § 77l(2) (1982), i.e. purchasers can only sue their sellers.

184. Section 12(2) of the Securities Act of 1933, 15 U.S.C. § 77l(2) states in pertinent part:

Any person who-
 (2) offers or sells a security . . . in interstate commerce
 . . . by means of a prospectus . . . which includes an untrue
 statement of a material fact or omits to state a material fact
 necessary in order to make the statements . . . not misleading
 . . . and who shall not sustain the burden of proof that he did
 not know . . . of such untruth or omission, shall be liable to
 the person purchasing such security from him. . .

Id.

185. Section 13 of the Securities Act of 1933, 15 U.S.C. § 77m, states in pertinent part: "No action shall be maintained to enforce any liability created under section 11 or section 12(2) unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reason-

These differences indicate that a private right of action under section 17(a) would not supplant the remedy provided by section 12(2). For example, an investor, defrauded in the purchase of securities, suing his seller within one year after his cause of action arose would certainly opt for section 12(2) because the burden of proof is placed by that section on the defendant. Section 17(a) would only be chosen as the basis for a private action when it is necessary to avoid the one year statute of limitations or where the privity requirement could not be fulfilled. To do so, however, the plaintiff must be able to sustain the burden of proof. At least one commentator believes that Congress imposed the privity requirement and short statute of limitations on section 12(2) actions in exchange for the unusual burden of proof placed on the defendant.¹⁸⁶ Thus, since section 17(a) and section 12(2) address different factual circumstances the overlap between them is incomplete. As a result, a section 17(a) action does not displace section 12(2) and would not, therefore, be inconsistent with the overall statutory scheme.

The Securities Act of 1933 has two major goals: complete disclosure to investors of all material information regarding the public sale of new issues of securities, and the prohibition of fraud in connection with the sale of such securities.¹⁸⁷ The added enforcement mechanism provided by section 17(a) under the limited factual circumstances described above may provide an incremental inducement to an issuer to comply with this goal. With no additional costs associated with this inducement, any chilling effect on the raising of capital would likely be insignificant.

The last part of the *Cort* test simply asks whether the cause of action is in an area that is a traditional concern of the states

able diligence." *Id.* Obviously, since the right of action under § 17(a) is an implied one, the Act's statute of limitations contains no reference to § 17(a). However, one commentator feels that it would be preferable from a policy point of view to adopt the short statute of limitations of § 13 for private rights of action under § 17(a) as a trade-off against the more stringent requirements imposed on private actions brought under Rule 10b-5. Hazen, *A Look Beyond the Pruning of Rule 10b-5: Implied Remedies and Section 17(a) of the Securities Act of 1933*, 64 VA. L. REV. 641, 688 nn.243-45 (1978).

186. Note, *Section 17(a) of the Securities Act of 1933: Implication of a Private Right of Action*, 29 U.C.L.A. L. REV. 244, 262 (1981).

187. R. JENNINGS & H. MARSH, *SECURITIES REGULATION: CASES AND MATERIALS*, 63 (6th ed. 1987).

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and not the federal government.¹⁸⁸ Securities laws regulate activities that have been primarily a federal concern for more than fifty years. Indeed, a major thrust for the passage of the Securities Act was the states' inability to adequately cope with securities fraud.¹⁸⁹ A private right of action under section 17(a) would not invade a preserve of the individual states and, therefore, fulfills the final prong of the *Cort* test. Thus, a closer examination of the compatibility of section 17(a) with the Supreme Court's four part test argues in favor of a private right of action under section 17(a) and against the majority's position in *WPPSS*.

Over and above the majority's interpretation of and reliance upon the Supreme Court's rigid *Cort* test, the best argument in favor of finding a private right of action under section 17(a) lies in an open recognition of the true purposes of the Securities Act of 1933: prevention of fraud and protection for the investing public.¹⁹⁰ That these are important federal interests cannot be denied. The smooth functioning of the nation's capital markets is essential not only for the health and well being of the U.S. economy but that of the interdependent global economy as well. These goals cannot be achieved without preserving the highest level of investor confidence. Such confidence is diminished, if not lost altogether, if investors, wronged by perceived or actual fraud and misrepresentation lack a necessary and useful remedy. Thus, national and individual interests will often be intertwined and both will be served when mischief in the securities markets is uncovered and punished. This policy was reaffirmed by the Supreme Court in 1964 in *Borak*¹⁹¹ and more recently in *Bateman, Eichler, Hill Richards, Inc. v. Berner*,¹⁹² when the Court stated that "implied private actions provide a 'most effective weapon in the enforcement' of the securities law and are a necessary supplement to Commission action."¹⁹³

188. *Cort*, 422 U.S. at 78.

189. See Note, *Implied Private Rights of Action Under the Securities Act of 1933 Section 17(A)*, 14 J. OF L. REF. 563, 579-80 n.108 (1981); Note, *Section 17(a) of the Securities Act of 1933: Implication of a Private Right of Action*, 29 U.C.L.A. L. REV. 244, 263 n.92 (1981).

190. S. REP. NO. 47, 73d Cong., 1st Sess. 1 (1933), 77 Cong. Rec. 2983 (May 8, 1933)(remarks of Sen. Fletcher).

191. *Borak*, 377 U.S. 426.

192. 472 U.S. 299 (1985).

193. *Bateman*, 472 U.S. at 310 quoting *J.I. Case v. Borak*, 377 U.S. 426, 432 (1964).

The holding in *WPPSS*, coupled with the restrictions imposed on private plaintiffs by the Supreme Court in *Blue Chip Stamps*, *Hochfelder*, and *Santa Fe Industries*, runs counter to the underlying purposes of the federal securities laws. Legislative reform is necessary to undo these restrictions, protect the investing public and achieve the legislative purposes.

VI. CONCLUSION

The Ninth Circuit held that a private right of action does not exist under section 17(a) of the Securities Act of 1933.¹⁹⁴ With this decision the Ninth Circuit joined a growing trend within the circuits.¹⁹⁵ It also aligned itself with the Supreme Court's restrictive attitude in implication cases generally¹⁹⁶ and private rights of action in securities cases in particular.¹⁹⁷ However, the Supreme Court has avoided ruling on a private plaintiff's right of action under section 17(a).¹⁹⁸ Even under the Court's restrictive standard for implying private rights of action an implied right can be found in section 17(a). This interpretation is more consistent with the underlying purposes of the federal securities acts and is necessary to encourage compliance with the antifraud provisions and to assure investor confidence in the securities markets. These important goals are undermined by the Ninth Circuit's holding in *WPPSS* and private plaintiffs will find it increasingly difficult to gain standing under the protective provisions of the Securities Acts.

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194. *In re Washington Pub. Power Supply Sys. Sec. Litig.*, 823 F.2d 1349 (9th Cir. 1987).

195. *See supra* note 55 and accompanying text.

196. *See supra* notes 32-52 and accompanying text.

197. *See supra* notes 63-98 and accompanying text.

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

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