Availability of an Implied Civil Cause of Action under Section 17(a) of the Securities Act of 1933

William E. Aiken Jr.
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by William E. Aiken, Jr.*

I. Introduction

A. Background

The Securities Act of 1933 was the initial federal legislation enacted in a program to protect securities investors from fraudulent transactions, or from transactions where lack of sufficient information would lead to uninformed decisions by prospective investors. Although the Act is principally a disclosure Act, requiring the disclosure of certain information in a registration statement and a prospectus before securities may lawfully be offered for sale, it also contains antifraud provisions. The primary antifraud provision is Section 17(a) of the Act.2

Because Section 17(a) does not expressly provide for a private right of action, if such a right is to exist it must arise by implication. In determining whether such an implied right exists, Section 17(a) must be read in pari materia with other pertinent provisions of the Act and with the applicable provisions of other federal securities laws. The Securities Act expressly provides for civil liability in Section 11,3 which calls for civil liability for faulty compliance with the registration requirements of the

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* B.S. 1954, University of Pennsylvania; J.D. 1962, Temple University.

Mr. Aiken is an adjunct professor of business law at Monroe Community College in Rochester, New York, where he is in private practice.


2 Section 17(a) reads as follows:

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 the 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.

Id. § 17(a), 15 U.S.C. § 77q(a) (1982).

Act, and Section 12(1), which provides for civil recovery for noncompliance with those requirements. In addition, Section 12(2) of the Act expressly provides for a civil cause of action based upon fraudulent activities in the general nature of those activities proscribed by Section 17(a). Section 13 of the Act is a statute of limitations applicable to actions brought pursuant to Sections 11 or 12. It provides that such an action must be brought within one year after the right thereto has been discovered, or with reasonable diligence would have been discovered, but in no event more than three years after the sale upon which such action is based.

The Securities Exchange Act of 1934 supplemented the Securities Act. Together, they provide the principal body of federal legislation governing securities transactions. In contrast to the Securities Act, which was designed to compel disclosure and thus protect investors with regard to the initial issuance of securities, the Exchange Act is primarily concerned with the protection of investors in the continuing trading of securities subsequent to their issuance. The Exchange Act has a number of antifraud provisions, the principal one being Section 10(b).

Unlike Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act does not specify in detail the nature of the proscribed conduct. Instead, it authorizes the Securities and Exchange Commission ("SEC") to promul-

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5 Section 12(2) provides as follows:
   Any person who —
   
   (2) Offers or sells a security (whether or not exempted by the provisions of Section 3 . . . ), by the use of any means or instrumentality of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission) and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission, shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

8 Section 10(b) provides as follows:
   It shall be unlawful for any person, directly or indirectly, by 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.

9 Id. § 10(b), 15 U.S.C. § 78j(b) (1982).
gate rules and regulations prohibiting manipulative and deceptive devices. Pursuant to such authority, the SEC promulgated Rule 10b-5.\(^9\)

The substantial similarity between Rule 10b-5 and Section 17(a) of the Securities Act suggests that the Rule was essentially derived from the antifraud provision of the earlier statute. The only significant difference between the two is that Section 17(a) applies to conduct "in connection with the purchase or sale of any security."\(^10\) Because the Securities Act is primarily concerned with the issuance of securities, it imposes controls only upon sellers. In contrast, the Exchange Act is broader in scope and is concerned with the conduct of both parties to a securities transaction. Like Section 17(a) of the Securities Act, neither Section 10(b) of the Exchange Act nor Rule 10b-5 contains express authorization for a civil action. It was decided early on, however, in *Kardon v. National Gypsum Co.*\(^11\) that the Exchange Act Provision and Rule gave rise to an implied private right of action. Since that time, numerous courts, including the United States Supreme Court, have reaffirmed that decision and there is no longer any question about the availability of a civil cause of action under Section 10(b) and Rule 10b-5.\(^12\) Given the similarity between Rule 10b-5 and Section 17(a) of the Securities Act, the question arises whether Section 17(a) also supports a civil action, or whether the availability of civil actions under the express provisions of Section 12(2) precludes such a conclusion. The picture with respect to Section 17(a) is not clear.

### B. Why the Availability of a Private Cause of Action under Section 17(a) is Important

One variance between Section 17(a) of the Securities Act and SEC Rule 10b-5, promulgated under the Exchange Act, is that the Rule prescribes manipulative or deceptive conduct with respect to the purchase or sale of securities, whereas Section 17(a) applies only with respect to the sale (or offer for sale) of securities. Therefore, if a private action exists under Section 17(a) it would appear to be narrower than one under Rule

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\(^9\) 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.


\(^12\) See Herman & MacLean v. Huddleston, 103 S. Ct. 683, 687 (1983) (existence of a private right of action under § 10(b) and Rule 10b-5 is "simply beyond peradventure").
Courts which have considered the question have generally held that if an action is available under Section 17(a), it is limited to purchasers of securities. Thus, if Section 17(a) gives rise to an implied private action, defrauded purchasers of securities would have a right of action under both Section 17(a) of the Securities Act and Section 10(b) and Rule 10b-5 of the Exchange Act. In contrast, even if a civil action was available under Section 17(a), defrauded sellers of securities would still be limited to an action under Section 10(b) of the Exchange Act and Rule 10b-5. Given this situation, the importance of whether a civil action is implied under Section 17(a) has been questioned.

In his oft-quoted concurring opinion in SEC v. Texas Gulf Sulphur Co., Judge Friendly doubted that a private remedy under Section 17(a) was ever intended, but said that there seemed to be little practical point in denying the existence of such an action once it was established that an aggrieved buyer had a private action under Section 10(b) of the Exchange Act. Civil actions often charge violations of both Section 17(a), and of Section 10(b) and Rule 10b-5. While assuming without deciding that an action is available under Section 17(a), courts have usually avoided ruling upon the validity of the Section 17(a) claims by deciding the actions under the Exchange Act claims.14

The conclusion that the question is academic, however, is based upon the presumption that the action available under Section 10(b) and Rule 10b-5 is in every respect as broad as any action which might be available under Section 17(a), so that an action could never be maintained under Section 17(a) which could not be maintained under Section 10(b) and the Rule. This, however, does not seem to be true. Consider first the conduct which is prohibited. Rule 10b-5 prohibits manipulative or deceptive conduct “in connection with the purchase or sale” of a security. Section 17(a) prohibits such conduct in “the offer or sale” of a security. Thus, a civil action under Rule 10b-5 may be maintained by either a buyer or seller of securities, while such an action, if it exists under Section 17(a), does not extend to a seller because that provision does not proscribe improper activities in the purchase of securities.15

Thus, in this regard, Section 10(b) and Rule 10b-5 offer a broader remedy than one which might be available under Section 17(a). Section

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14 See, e.g., Kramas v. Security Gas & Oil Co., 672 F.2d 766 (9th Cir. 1982), cert. denied, 103 S. Ct. 444 (1982); Johns Hopkins Univ. v. Hutton, 488 F.2d 912 (4th Cir. 1973); Katz v. Amos Treat & Co., 411 F.2d 1046 (2d Cir. 1969); Globus v. Law Research Serv., Inc., 287 F. Supp. 188 (S.D.N.Y. 1968). Perhaps the main reason for the somewhat awkward development of law under § 17(a) is the presence of Rule 10b-5. After the recognition of a private cause of action under the Rule, cases that might have been brought under § 17(a) were instead brought under the Rule. Even when cases were brought under § 17(a), courts often decided them under the Rule. See, e.g., Landry v. All American Assurance Co., 688 F.2d 381, 386 (5th Cir. 1982).
17(a), however, refers to an "offer or sale" of securities. The Exchange Act provisions make no mention of an offer, only of activities in connection with the purchase or sale of a security. Although "in connection with" could be interpreted to include preliminary negotiations, including an offer, the Supreme Court has ruled that only a purchaser or seller may maintain an action under Section 10(b) or Rule 10b-5.\(^{16}\) Thus, an action is not available to one who has been defrauded by someone who has made an offer where the offeree has not purchased or sold the security.\(^{17}\) But the language of Section 17(a) clearly encompasses, as a potential plaintiff, an offeree in an offer to sell a security. Where the question has been addressed, it has been recognized that if an implied right of action exists under Section 17(a), it extends to offerees.\(^{18}\) Those cases which have held that a Section 17(a) action is available only to purchasers generally have distinguished between purchasers and sellers\(^{19}\) and have not considered the availability of the action to offerees.

A more important distinction between an action under Section 10(b) and Rule 10b-5 and a potential action under Section 17(a) involves the issue of scienter. For years, a battle raged as to whether a showing of scienter was required in a civil action under Section 10(b) and Rule 10b-5.\(^{20}\) Although questions remain concerning what constitutes the requisite scienter, the Supreme Court laid the basic question to rest in *Ernst & Ernst v. Hochfelder.*\(^{21}\) In *Hochfelder*, the Court held that negligence was an insufficient ground for a civil action under Section 10(b) and Rule 10b-5. Allegations of the defendant's scienter are an essential element of such an action. The Court based its holding on the language of Section 10(b), not the language of the Rule, stating that the narrower language of the statutory section constrained the reach of the broader Rule 10b-5.\(^{22}\)

The law regarding the requirement of showing scienter in a Section 17(a) private action (presuming that one exists) is not so distinct. A number of courts have ruled on the question and, with some exceptions,\(^{23}\) most have held that some form of scienter is necessary to support


\(^{17}\) Id.


\(^{22}\) Id. at 212-14. See also *Landry v. All American Assurance Co.*, 688 F.2d 381 (5th Cir. 1982).

\(^{23}\) See, e.g., *SEC v. American Realty Trust*, 586 F.2d 1001 (4th Cir. 1978) (injunction may
an action based upon an alleged violation of Section 17(a). A showing of negligent conduct is said to be insufficient. For the most part, however, these decisions were handed down prior to the Supreme Court decision in Aaron v. SEC. Although not addressing the specific questions under discussion in this article, the Court in that case was faced with the question of whether the SEC was required to establish scienter as an element of a civil enforcement action to enjoin violations of Section 10(b) and Rule 10b-5 under the Exchange Act, and Section 17(a) under the Securities Act. While deciding that a showing of scienter was a necessary prerequisite under the Exchange Act, the position of the Court was split as to Section 17(a), depending upon which of the three paragraphs of that Section was considered. In the view of the Court:

The language of § 17(a) strongly suggests that Congress contemplated a scienter requirement under § 17(a)(1), but not under § 17(a)(2) or § 17(a)(3). The language of § 17(a)(1), which makes it unlawful "to employ any device, scheme, or artifice to defraud," plainly evinces an intent on the part of Congress to proscribe only knowing or intentional misconduct. Even if it be assumed that the term "defraud" is ambiguous, given its various meanings at law and in equity, the terms "device," "scheme," and "artifice" all connote knowing or intentional practices.

By contrast, the language of § 17(a)(2), which prohibits any person from obtaining money or property "by means of any untrue statement of a material fact or any omission to state a material fact," is devoid of any suggestion whatsoever of a scienter requirement.

Finally, the language of § 17(a)(3), under which it is unlawful for any person "to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit," (emphasis added) quite plainly focuses upon the effect of particular conduct on members of the investing public, rather than upon the culpability of the person responsible.

It is our view, in sum, that the language of § 17(a) requires scienter under § 17(a)(1), but not under § 17(a)(2) or § 17(a)(3).

Although the Supreme Court resolved the issue only with respect to SEC enforcement issues, it is doubtful that a different interpretation

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27 Id. at 695-97.
would be given if an implied private cause of action is found to exist.\textsuperscript{28} This conclusion is consistent with the Court's decision in \textit{Hochfelder} where it held that a showing of scienter is an essential element of an action under the Exchange Act Section 10(b) and Rule 10b-5. The Court, by basing its decision on the statutory provision rather than the Rule, and by expressly pointing out that the narrower language of the statute constrained the reach of the broader Rule 10b-5, strongly suggests that the Rule itself, without the constraint of the authorizing statute, would be sufficiently broad to support a civil action without a showing of scienter. In the case of the Securities Act, the statutory provision is substantially identical to the Exchange Act Rule and is not similar to Section 10(b) of the Exchange Act, therefore, an argument can be made that a showing of scienter would not be an essential element of a civil action under Section 17(a). Such a conclusion would not be inconsistent with \textit{Hochfelder}.

As to actions under Sections 17(a)(2) and 17(a)(3), it appears that a showing of scienter would not be necessary. In view of the existence of such a requirement under Section 10(b) and Rule 10b-5, Section 17(a) would be an attractive, viable alternative to some actions previously brought under the Rule, particularly as to actions based on negligence,\textsuperscript{29} provided that such an action exists.

Punitive damages may be another area in which 17(a) may offer an advantage over Section 10(b) and Rule 10b-5. It is well established that such damages are not available under Section 10(b).\textsuperscript{30} These decisions, however, are based on Section 28(a) of the Exchange Act\textsuperscript{31} which limits recovery under that Act to "actual damages." Courts have consistently held that such provision precludes the recovery of punitive damages.\textsuperscript{32} The Securities Act has no corresponding provision. Nevertheless, in those cases in which the question has been considered, courts usually have held that punitive damages are also unavailable under Section 17(a).\textsuperscript{33} Courts have stated that to permit punitive damages under Section 17(a) but not under Section 10(b) would create "an unreasoned split between buyers and sellers of securities subjected to fraud of an equally heinous nature."\textsuperscript{34} However, given the limited number of cases in relatively few circuits which have addressed the issue, it cannot be regarded as a closed question.

\textsuperscript{28} See Landry v. All American Assurance Co., 688 F.2d 381 (5th Cir. 1982).
\textsuperscript{29} Id.
\textsuperscript{30} See, e.g., Byrnes v. Faulkner, Dawkins, & Sullivan, 550 F.2d 1303 (2d Cir. 1977); De-Haas v. Empire Petroleum Co., 435 F.2d 1223 (10th Cir. 1970).
\textsuperscript{34} Globus, 418 F.2d at 1286.
In view of the probable difference in scienter requirements between Section 10(b) actions under the Exchange Act and Section 17(a) of the Securities Act, it appears that the existence or non-existence of a private right of action under Section 17(a) is a significant question.

II. Considerations

A. Generally

The Supreme Court has never ruled on whether Section 17(a) of the Securities Act gives rise to an implied right of action. On two occasions the Court has expressly declined to do so. Thus, in determining whether such a right exists, one must look to guidance from the Court in a general sense, derived from decisions bearing upon the right to a civil action under other federal statutes, and to lower court decisions.

The Supreme Court has demonstrated a decided trend away from recognizing an implied private cause of action based upon statutes which are silent on the question of civil remedies. The test currently applied, as established in *Cort v. Ash*, is said to be more restrictive than any of its predecessors. Prior to *Cort v. Ash*, the Court implied a private cause of action absent evidence of Congressional authorization or acquiescence, on the theory that such remedies were necessary to vindicate important federal interests. Such decisions appeared to rest on the presumption that a civil damage remedy ordinarily would be inferred from a blanket statutory prohibition, unless there was some persuasive indication that Congress intended existing remedies and procedures to be exclusive. In a substantial retreat from its previous liberal position, the Supreme Court in *Cort v. Ash* set forth four factors which must be considered in determining whether a private action may be implied from a federal statute. These factors are:

1. Is the plaintiff one of the class for whose especial benefit the statute was enacted; that is, does the statute create a federal right in favor of the plaintiff?

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35 See Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 733 n.6 (1975) ("We express no opinion, of course, on whether Section 17(a) in light of the express civil remedies of the 1933 Act gives rise to an implied cause of action"); Aaron v. SEC, 446 U.S. 680, 689 (1980).


(2) Is there any indication of the legislative intent, explicit or implicit, either to create such a remedy or deny one?
(3) Is it consistent with the underlying purposes of the legislative scheme to imply such a remedy for the plaintiff?
(4) Is the cause of action 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?\textsuperscript{41}

In \textit{Touche Ross & Co. v. Redington},\textsuperscript{42} the Court further explained that although all four factors were relevant, they were not necessarily entitled to equal weight. The central inquiry remains whether Congress intended to create, either expressly or by implication, a private cause of action.\textsuperscript{43} Because the Securities Act has provisions calling for express civil remedies, two further pronouncements of the Supreme Court are important to the present analysis. In \textit{Touche Ross & Co.}, the Court expressed reluctance to imply a cause of action "that is significantly broader than the remedy that Congress chose to provide,"\textsuperscript{44} and in \textit{Transamerica Mortgage Advisors, Inc. v. Lewis},\textsuperscript{45} the Court emphasized the "elemental canon of statutory construction that where a statute provides a particular remedy or remedies, a court must be wary of reading others into it."\textsuperscript{46}

Does Section 17(a) give rise to a civil cause of action under the \textit{Cort v. Ash} test? Because Section 17(a) was enacted to protect securities investors from fraud in the purchase and sale of securities, offerees and purchasers of securities are members of a class for whose benefit the section was created.\textsuperscript{47} Accordingly, the first element of the four pronged test established by the Supreme Court in \textit{Cort} is satisfied. That a statutory provision has been enacted to protect a particular class does not necessarily mean, however, that Congress intended that provision to be enforced through private litigation.\textsuperscript{48} There must be some objective indication of congressional intent to create a private action. If such an intent can be found, the right of action should be recognized because the fourth con-

\textsuperscript{41} \textit{Ash}, 422 U.S. at 79.
\textsuperscript{42} 442 U.S. 560 (1979).
\textsuperscript{43} Id. at 569.
\textsuperscript{44} Id. at 574.
\textsuperscript{45} 444 U.S. 11 (1979).
\textit{See generally} \textit{Note}, supra note 36.
\textsuperscript{48} \textit{See} \textit{Hill}, 521 F. Supp. at 1376-78.
consideration specified by the Supreme Court is met: securities regulation is
not an area of the law traditionally relegated to the states or one basically of concern to the states.

To determine the intent of Congress as expressed a half century ago,
one must look to the legislative history and the structure of the Securities
Act. Both of these are considered in the subdivisions immediately
following.

B. Arguments Against Implied Action

Of the meager legislative history available for consideration, most
supports the conclusion that no implied private action under Section
17(a) was intended by Congress. In Basile v. Merrill Lynch, Pierce, Fenner &
Smith, Inc., \textsuperscript{49} the court pointed out that, "in listing the sections of the
Securities Act that create and define civil liability the House Committee
Report noted only Sections 11 and 12."\textsuperscript{50} The report added that "[T]o
impose a greater responsibility . . . would unnecessarily restrain the con-
scientious administration of honest business with no compensating ad-
vantage to the public."\textsuperscript{51} Thus, the court concluded that the legislative
history reveals no congressional intent to create an implied right of ac-
tion.\textsuperscript{52} In agreement, the Fifth Circuit has stated: "The legislative
history of the 1933 Act makes no mention of civil liability under Section
17(a); congressional discussion of civil liability under the Act centers on
Sections 11 and 12."\textsuperscript{53} In 

Dyer v. Eastern Trust and Banking Co., \textsuperscript{54} the
court, without specifically identifying authority, states: "The argument,
based on legislative history and statutory construction, is persuasive that
Section 17(a) was intended only to afford a basis for injunctive relief and,
if willfulness is present, for criminal liability, and was not intended to
provide a civil remedy for damages supplementing that afforded by Sec-
tion 12(2)."\textsuperscript{55}

An additional means of obtaining insight on the congressional in-
tent is provided by Professor Loss in his treatise on Securities Law. Pro-
fessor Loss points out that in November 1933, Commissioner Landis of
the Federal Trade Commission, who is said to have played a prominent
part in the drafting of the Securities Act, stated in an address:

The suggestion has been made on occasion that civil liabilities arise from
a violation of Section 17, the first subsection of which makes unlawful
the circulation of falsehoods and untruths in connection with the sale of

\textsuperscript{49} 551 F. Supp. 580 (S.D. Ohio 1982).
\textsuperscript{50} Id. at 586. See H.R. REP. NO. 85, 73d Cong., 1st Sess. 9 (1933) (hereinafter cited as
HOUSE REPORT).
\textsuperscript{51} HOUSE REPORT, supra note 50, at 9-12.
\textsuperscript{52} Basile, 551 F. Supp. at 587.
\textsuperscript{53} Landry, 688 F.2d at 389 (citing HOUSE REPORT, supra note 50, at 9-10). See also Hill, 521
1980).
\textsuperscript{54} 336 F. Supp. 890 (D. Me. 1971).
\textsuperscript{55} Dyer, 336 F. Supp. at 904.
a security in interstate commerce or through the mails. But a reading of this section in the light of the entire Act leaves no doubt but that violations of its provisions give rise only to a liability to be restrained by injunctive action or, if wilfully done, to a liability to be punished criminally.56

The strongest argument against an implied private action under Section 17(a) stems from the construction of the Securities Act as a whole. The Act contains provisions expressly providing for civil actions under certain circumstances which fall within the purview of Section 17(a). The Act also places limitations and restrictions on the maintenance of such private actions. If a private action is implied under Section 17(a), it would appear to render Section 12(2) of the Securities Act largely unnecessary, and would permit the limitations and restrictions placed upon private actions under the express provisions to be avoided by the simple expedient of maintaining an action under the implied authority of Section 17 instead of the express authority of Section 12. It is unlikely that Congress would have intended by implication to emasculate the provisions it expressly set forth in the statute.

At a relatively early date, Professor Loss succinctly articulated this argument. After noting that it was established that Section 10(b) of the Exchange Act supports an implied private action, he posed the question whether there was similar justification for implying a private action under Section 17(a) of the Securities Act. His response was as follows:

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 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—for example, the fact that § 11 but not § 12 imposes liability on certain persons connected with the issuer without regard to their participation in the offering and the fact that § 12(2) does not go so far in relation to § 17(a) as § 12(1) goes in relation to § 5—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.57

57 3 L. Loss, supra note 56, at 1785 (2d ed. 1961). This evaluation by Professor Loss has frequently been cited by the courts in decisions denying a § 17(a) private right of action. See, e.g., Hill, 521 F. Supp at 1376-77; Ingram Indus., Inc. v. Nowicki, 502 F. Supp. 1060, 1069 (E.D.
Notwithstanding that a number of courts have held that Section 17(a) does support an implied private action, Professor Loss' analysis seems to have continued vitality.

C. Arguments for an Implied Action

The principal argument in favor of an implied action under Section 17(a) of the Securities Act is that the section is substantially identical to SEC Rule 10b-5, and it now is well established that the Rule, in conjunction with its underlying statutory provision, Section 10(b) of the Exchange Act, supports such an implied action. Therefore, it would be inconsistent to deny a private action under Section 17(a). This argument has been the basis of judicial decisions which have held that such an action does exist. The Seventh Circuit Court of Appeals has held that the language of Section 17(a) is broad enough to imply a private right of action, and is more specific than Section 10(b) of the Exchange Act, under which a private right of action has commonly been approved.\(^{58}\) Similarly, the Ninth Circuit Court of Appeals has said that in light of the minimal differences between Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act, arguments in favor of an implied action under Section 17(a) are persuasive.\(^{59}\)

Other arguments in favor of an implied action under Section 17(a) are rather passive. It has been said that such an action exists because Section 17(a) is broad enough to imply it,\(^{60}\) or that the action is to be implied because the section makes the prohibited conduct unlawful.\(^{61}\) In addition, there is the "why not" argument, set forth by Judge Friendly in his concurring opinion in *SEC v. Texas Gulf Sulphur Co.*,\(^{62}\) which states that since an implied action is recognized under Section 10(b) of the Exchange Act, there is little point in denying one under Section 17(a). As previously discussed, this argument presupposes that, assuming the existence of an action under Section 17(a), any action which could be brought thereunder also might be brought under Section 10(b). That supposition no longer appears valid in light of the developments concerning scienter requirements which have evolved since Judge Friendly made his comments.

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59 Stephenson v. Calpine Conifers II, Ltd., 652 F.2d 808, 815 (9th Cir. 1981). As discussed earlier, see supra notes 2-9 and accompanying text, § 17(a) of the 1933 Act is not closely similar to § 10(b) of the 1934 Act, but it is substantially identical to Rule 10b-5, which, as a regulation promulgated under § 10(b), might effectively be regarded as part of that section.

60 See Kirshner v. United States, 603 F.2d 234, 241 (2d Cir. 1978), cert. denied, 442 U.S. 909 (1979); Daniel, 561 F.2d at 1245.


Some have suggested that a limited private action should be available under Section 17(a) to the extent that it is not inconsistent with the private remedies expressly provided by the Act. Under the express recovery provisions of Section 12 of the Act, an action may be brought based upon conduct of the defendant which does not amount to fraud. Hence, it is argued, if a civil action under Section 17(a) requires proof of fraud, it does not duplicate the remedy offered by Section 12. Only Section 17(a)(1) and Section 17(a)(3) inherently require fraud for violations to be found; Section 17(a)(2), by its terms, does not. Section 17(a)(2) can be violated by the negligent use of misinformation. Thus, it has been concluded by a limited number of courts that Section 17(a) should be regarded as giving rise to an implied right of action under paragraphs (1) and (3) without such action being subject to the limitations which are applicable to private actions under Section 12 of the Act; but to the extent that a private right of action exists under paragraph (2), it would be subject to such limitations. Therefore, it is argued that an implied private action exists under Section 17(a)(1) and Section 17(1)(3), but not under Section 17(a)(2).

An additional argument in favor of implying a private action under Section 17(a) may be derived from the Supreme Court's opinion in Herman & MacLean v. Huddleston. In Huddleston, the Court considered the question whether purchasers of registered securities who allege that they were defrauded by misrepresentations in a registration statement may maintain an action under Section 10(b) of the Exchange Act notwithstanding the express remedy for misstatements and omissions in registration statements provided by Section 11 of the Securities Act. Distinguishing between the scopes of the two provisions and pointing out that scienter is a necessary element of a Section 10(b), but not of a Section 11 violation, the Court held that the action under Section 10(b) could be maintained. Conceding that the same conduct on the part of a defendant could sometimes give rise to rights of action under both statutory provisions, even though the burdens placed on the plaintiff would not be the same, the Court said that since Section 10(b) and Section 11 address different types of wrongdoing, it saw no reason to carve out an exception to Section 10(b) for fraud occurring in a registration statement just because the same conduct may be actionable under Section 11.

The decision of the Supreme Court in Huddleston may seem initially to be inconsistent with the previously discussed position that no implied

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63 Compare 1933 Act, supra note 1, §§ 17(a)(1), (3), 15 U.S.C. §§ 77g(a)(1), (3) with 1933 Act, supra note 1, § 17(a)(2), 15 U.S.C. § 77g(a)(2). This conclusion is entirely consistent with the Supreme Court's recent decision in Aaron v. SEC, 446 U.S. 680 (1980). The Court in Aaron held that scienter was an element of a cause of action under § 17(a)(1), but not under § 17(a)(2) or § 17(a)(3). See supra notes 26-29 and accompanying text.


66 Id. at 687-90.
action under Section 17(a) should be recognized because it would enable a plaintiff to bypass the provisions of the Securities Act which expressly establish civil actions. Further examination shows two essential differences, however, between the question being analyzed in this article and the question addressed by the Court in Huddleston. First, the Court in Huddleston was considering whether express remedies of one statute precluded the application of implied remedies from another statute. This should not be heavily emphasized, however, since the Court regarded the two Acts as constituting "interrelated components of the federal regulatory scheme governing transactions in securities." Nevertheless, it remains a legitimate consideration.

The second difference is of greater importance. The present analysis concerns whether a private right of action should be implied for Section 17(a). That basic question remains unresolved. In contrast, in Huddleston, the Court started with the unquestioned fact that Section 10(b) does give rise to such a right. The Court stated, "The existence of this implied remedy is simply beyond peradventure." The Court was determining only whether, recognizing the existence of such a right of action, that right should be permitted to be applied where an express remedy was also provided. In the words of the Court: "It would be anomalous indeed if the special protection afforded to purchasers in a registered offering by the 1933 Act were deemed to deprive such purchasers of the protection against manipulation and deception that Section 10(b) makes available to all persons who deal in securities." Thus, the Court seems to be saying that where two remedies generally are available to securities investors, an investor should not be deprived of one remedy which covers his situation, merely because the situation also is covered by another remedy. It is a logical argument for the situation which faced the Court in Huddleston, but it is not relevant to the instant question. Huddleston does not mandate, nor even suggest that a private action should be recognized under Section 17(a).

III. Judicial Decisions

A. Generally

The judicial decisions on the question addressed herein have not been uniform. The courts in the Second, Fourth, Seventh and Ninth Circuits have held that a private action does exist under Section 17(a) of the Securities Act, while those in the First, Fifth, Sixth, Eighth and Tenth Circuits have held that there is no such private right of action.

67 Id. at 686 (quoting Hochfelder, 425 U.S. at 206).
68 Huddleston, 103 S. Ct. at 687.
69 Id. at 688.
70 See id. at 686 & 686 n.9.
71 "Courts are split on whether Section 17(a) provides an implied private right of action for damages. Neither the Supreme Court nor the First Circuit [Court of Appeals] has addressed the issue." Kaufman v. Magid, 539 F. Supp. 1088, 1097 (D. Mass. 1982).
The courts of appeals have not ruled on the question in all circuits. The results have varied in the Third Circuit, with no ruling from the court of appeals, and no court in the Eleventh Circuit has yet considered the question.\(^72\)

The trend appears to be toward holding that there is no implied private action under Section 17(a). For some time the courts, to some extent relying upon Judge Friendly's dictum,\(^73\) held or assumed that such a right of action existed, largely because it did not seem to make much difference.\(^74\) In some jurisdictions the right is recognized without having been subjected to strict scrutiny.\(^75\) Other courts have held that the right exists on the grounds previously discussed, (i.e., Section 17(a) is substantially identical to SEC Rule 10b-5 under which an action does exist).\(^76\) Such holdings, however, almost invariably have been made pursuant to very limited consideration of the question.\(^77\)

The courts which have held that no private action may be implied under Section 17(a) have generally concluded that because the Securities Act contains express provisions calling for private actions, it would frustrate the congressional purpose in enacting the express provisions to superimpose an implied right.\(^78\) In this regard, the court in \textit{Landy v. All American Assurance Co.}\(^79\) commented as follows:

The Securities Act of 1933 contains two express civil liabilities [provisions] for the protection of purchasers. The first of these is § 11 which prohibits falsehoods and omissions in the registration statement. The second is § 12(2) which protects purchasers from misstatements or omissions in written or oral communications. Together these sections confer specific private rights upon purchasers. Before a purchaser may successfully bring suit under either of these two sections, however, strict procedural requirements must first be satisfied. Section 17(a)(2) prohibits the same type of conduct as §§ 11 and 12, but has none of the limitations imposed by Congress. The creation of an implied cause of action [under] § 17(a) under these circumstances would effectively frustrate the care-

\(^{72}\) See \textit{infra} notes 82-120 and accompanying text for an in-depth discussion of the positions taken by the courts of appeals and district courts.

\(^{73}\) See \textit{supra} note 13 and accompanying text.


\(^{76}\) See \textit{supra} note 59 and accompanying text. See, \textit{e.g.}, Stephenson v. Calpine Conifers II, Ltd., 652 F.2d 808 (9th Cir. 1981); Daniel v. Int'l Bhd. of Teamsters, 561 F.2d 1223 (7th Cir. 1977), rev'd on other grounds, 439 U.S. 551 (1979).

\(^{77}\) See Basile v. Merrill Lynch, Pierce, Fenner & Smith, 551 F. Supp. 580, 585 (S.D. Ohio, 1980): It is true that the Second, Fourth, Seventh and Ninth Circuits have held that section 17(a) provides a private right of action. They, however, did so with a minimum of discussion; the most marked characteristic of all these decisions is the total absence of the analysis mandated by the Supreme Court for any case raising the issue of whether Congress intended that a private cause of action be implied.

\(^{78}\) See \textit{infra} Landy, 688 F.2d at 384.


\(^{79}\) 688 F.2d 381 (5th Cir. 1982).
fully laid framework of the Act.\textsuperscript{80} In holding that no private action may be implied under Section 17(a), some courts also have looked to the trend in Supreme Court decisions regarding implied actions under federal statutes.\textsuperscript{81} In addition, there are decisions falling within the two extremes in which it effectively has been held that a private action exists under Sections 17(a)(1) and 17(a)(3), but not under Section 17(a)(2).

\textbf{B. Positions Taken by the Circuits}

The following is a brief summary of the position taken in the several circuits with respect to the question addressed herein. This discussion is not exhaustive as to authority in each circuit, but an attempt has been made to collect and analyze the recent decisions to reflect the current position taken by the courts.

\textit{FIRST CIRCUIT:}

The First Circuit Court of Appeals has not ruled on whether Section 17(a) gives rise to an implied right of action. The district courts in Maine,\textsuperscript{82} Massachusetts,\textsuperscript{83} and New Hampshire,\textsuperscript{84} however, have ruled in the negative. The initial district court decision in the circuit, \textit{Dyer v. Eastern Trust and Banking Co.},\textsuperscript{85} was based on the court's evaluation of congressional intent, as reflected in the structure of the Securities Act. The subsequent decisions were reached with minimal analysis, but are consistent with the \textit{Dyer} holding.

\textit{SECOND CIRCUIT:}

In \textit{Kirshner v. United States},\textsuperscript{86} the Second Circuit Court of Appeals held that the language of Section 17 of the Exchange Act is broad enough to imply a private right of action. Prior to the \textit{Kirshner} decision, there was a split of authority among the district courts in the circuit.\textsuperscript{87} None of the cases which have held that the action exists contain a significant analysis of the question.

\textit{THIRD CIRCUIT:}

There is no Third Circuit Court of Appeals ruling on whether an implied private right of action arises out of the proscriptions of Section

\textsuperscript{80} \textit{Id.} at 390 (footnotes omitted).
\textsuperscript{86} 603 F.2d 234 (2d Cir. 1978), \textit{cert. denied}, 442 U.S. 909 (1979).
17(a) of the Securities Act. The Third Circuit district courts do offer, however, two well reasoned opinions which present contrasting conclusions. In *Hill v. Der*, 88 the court traced the evolution of the Supreme Court decisions on the general question of implied actions arising from federal statutes and applied its conclusions to Section 17(a). In view of the civil remedies provided in the Act, the court concluded that none was intended under Section 17(a). In addition to looking to Sections 11 and 12, the court looked to Sections 20 and 24 of the Act to show that Congress had considered sanctions against violators from every angle. The court stated:

[U]nder § 24 of the Securities Act, 15 U.S.C. § 77x, willful violations of the Act are punishable by fine, imprisonment or both. Similarly, § 20, 15 U.S.C. § 77t, authorizes the SEC to bring civil actions in federal court to enjoin existing or imminent violations of the provisions of the Act, including § 17(a). These compliance measures when juxtaposed with the civil remedies contained in §§ 11 and 12 make it unlikely that Congress “absentmindedly” omitted an intended civil remedy under § 17(a).

The court in *Dorfman v. First Boston Corp.* 90 held that Section 17(a) does give rise to a civil action for fraud under paragraphs (1) and (3), independent of the restrictions and limitations applicable to Section 12. An action alleging violations of Section 17(a)(2), on the other hand, would be subject to such restrictions and applications. Subsequently, in *Wulc v. Gulf & Western Industries, Inc.* 91 the court cited and accepted the position taken in *Dorfman*.

In *B & B Investment Club v. Kleinert’s, Inc.*, 92 the dichotomy between Sections 17(a)(1) and 17(a)(3), and Section 17(a)(2) was again recognized, but with different consequences. In *B & B Investments*, the court held that a private right of action exists under Section 17(a), but added that while a valid claim may be stated under Section 17(a)(1) and Section 17(a)(3) without allegations of privity, a claim under Section 17(a)(2) is subject to the limitations of Section 12. 93 Finally, to round out the varying positions taken by the district courts in the Third Circuit, in *Cromwell v. Pittsburgh & Lake Erie Railroad Co.*, 94 the court merely stated, without extended discussion, that Section 17 does give rise to a private cause of action. It should be noted, however, that this decision preceded the *Wulc* decision in the same district.

**FOURTH CIRCUIT**:

89 Id. at 1377 (footnotes omitted).
93 Id. at 726.
94 373 F. Supp. 1303 (E.D. Pa. 1974). *But see* Kimmel v. Peterson, 565 F. Supp 476 (E.D. Pa. 1983), a recent decision where the court, after reviewing the authorities, held that no private action was available under § 17(a).
In *Newman v. Prior*\(^9^5\) the Fourth Circuit Court of Appeals stated that that circuit is committed to the rule that Section 17(a) of the Securities Act supports a private damages claim for the fraudulent sale of a security.\(^9^6\)

**FIFTH CIRCUIT:**

Although there was a split of opinion among the district courts, the majority of decisions have held that Section 17(a) of the Securities Act does not give rise to an implied right of action.\(^9^7\) Any question as to the law in the circuit on the question, however, was resolved by the court of appeals in *Landry v. All American Assurance Co.*\(^9^8\) In *Landry*, the court held that no such private action is available. The court looked to the Supreme Court’s general position on implied actions and the overall structure of the Act and concluded that:

[I]t would appear that the Cort test as applied to § 17(a) of the Securities Act of 1933 points away from the implication of a private cause of action. This, together with the Supreme Court’s conservative interpretation of the test in recent years, leads us to the conclusion that the district court correctly dismissed this theory of relief.\(^9^9\)

**SIXTH CIRCUIT:**

The Sixth Circuit Court of Appeals has not ruled on the availability of a private action under Section 17(a), and the status of the question is not completely clear from the district court decisions. The circuit can be considered, with reasonable confidence, however, to be in the camp of the jurisdictions which reject the proposition that such an action is available. The district courts handed down several decisions in which the question was addressed over the two year period from 1980 to 1982. In 1980, the District Court for the Eastern District of Kentucky noted that the question is basically one of statutory construction.\(^1^0^0\) The court said that Section 17(a) simply proscribes certain conduct. If Congress had wanted to create a civil remedy for damages within that section it could expressly have done so. The statutory language does not evidence any congressional intent to provide a private suit for damages, and Congress did not provide an alternative means of securing relief for its violations. Accordingly, the court held that Section 17(a) does not provide for an

\(^9^5\) 518 F.2d 97 (4th Cir. 1975).
\(^9^6\) Id. at 50. See also Reid v. Madison, 438 F. Supp. 332 (E.D. Va. 1977).
\(^9^8\) 688 F.2d 381 (5th Cir. 1982).
\(^9^9\) Id. at 391. The court referred to the test adopted by the Supreme Court in Cort v. Ash, 422 U.S. 66 (1975). See supra notes 37-48 and accompanying text.
\(^1^0^0\) See Ingram Indus., Inc. v. Nowicki, 502 F. Supp. 1060 (E.D. Ky. 1980).
implied private cause of action. In 1981, the court in *State of Ohio v. Crofters* rendered a half-hearted decision in favor of recognizing the action. The court said: "We are inclined at this point in the case to follow the majority of circuit courts in finding that an implied private cause of action exists under [Section 17(a)]." A year later, however, the same court analyzed the question and came to the opposite conclusion. In *Basile v. Merrill Lynch, Pierce, Fenner & Smith, Inc.* the court pointed out that the legislative history of the Securities Act did not support a finding of Congressional intent to create an implied action under Section 17(a), and that the structure of the Act was convincing evidence of the absence of such an intent. To imply a private cause of action under Section 17(a) would be to create judicially a broader remedy than that expressly provided by Congress in Sections 11 and 12 of the Act.

In holding that there is no such implied action, the court conceded that the courts of appeals in the Second, Fourth, Seventh, and Ninth Circuits had held that Section 17(a) does provide an implied private action, but commented that they did so with a minimum of discussion and without the analysis mandated by the Supreme Court for such holdings.

**SEVENTH CIRCUIT**:

The Seventh Circuit Court of Appeals, in holding that an implied right of action under Section 17(a) is available on the ground that the section is broad enough to support such an implication, implicitly overruled contrary prior district court decisions. The court did not consider the effect of the provisions of the Act expressly providing for civil remedies.

**EIGHTH CIRCUIT**:

In *Shull v. Dain, Kalman & Quail, Inc.* the Eighth Circuit Court of Appeals held without discussion that Section 17(a) gives no private cause of action.

**NINTH CIRCUIT**:

Early district court decisions in the Ninth Circuit generally held that no implied private action exists under Section 17(a), although in

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101 Id. at 1070.
103 Id. at 1140.
105 Id. at 587.
106 Id. at 585.
110 Id. at 159. See also Lingenfelter v. Title Ins. Co. of Minn., 442 F. Supp. 981 (D. Neb. 1977).
some instances the courts took qualified positions.\textsuperscript{112} Court of appeals decisions on the question recognize a private action, although the conclusion that such is the rule in the circuit may be subject to some question. In \textit{Stephenson v. Calpine Conifers II, Ltd.}\textsuperscript{113} the court held that the right of action exists on the basis of the minimal difference between Section 17(a) and Section 10(b) of the Exchange Act. In \textit{Kramas v. Security Gas \& Oil, Inc.},\textsuperscript{114} the court stated that it assumed such a private action to be available, but expressly declined to rule on the question, stating that it was not properly before the court. In a later district court decision, \textit{Zatkin v. Primuth},\textsuperscript{115} the court pointed out that the \textit{Kramas} decision may cast doubt on the earlier Ninth Circuit decision in \textit{Stephenson}. Hence, the existence of a private action under Section 17(a) in the Ninth Circuit may be in doubt, but the existing authority continues to support the position that the right of action does exist.

\textbf{TENTH CIRCUIT:}

The Court of Appeals in the Tenth Circuit has not ruled on the availability of an implied civil action under Section 17(a) of the Securities Act. Two district courts in that circuit have considered the question, however, and have concluded that the section will not support such an action. In \textit{Freeman v. McCormack},\textsuperscript{116} the court granted summary judgment declaring that no such action exists. The court noted that those activities which constitute both a violation of Section 17(a)(2) and Section 12(2) of the Act may be prosecuted by private civil action pursuant to the authority granted by Section 12 of the Act.\textsuperscript{117} It noted, however, that there are portions of Section 17(a) not encompassed by the scope of private civil actions under Section 12, which indicates that Congress did not intend to permit suits based on those activities. Accordingly, the court concluded that Section 17(a) does not imply any private right of action.\textsuperscript{118}

In \textit{Woods v. Home \& Structures, Inc.},\textsuperscript{119} the court observed what it regarded as fallacious reasoning of courts which had held that Section 17(a) gives rise to a private action. The court noted that, given the almost identical language of Rule 10b-5 and Section 17(a) and the broader scope of Rule 10b-5, some courts have seen no practical point in denying the existence of a private action under Section 17. The court stated, however, that the practical significance of denying a private right of ac-

\begin{itemize}
\item \textsuperscript{112} See \textit{In re Equity Funding Corp. of America Sec. Litig.}, 416 F. Supp. 161 (C.D. Cal. 1976)(Section 17(a) private action held unavailable, at least to the extent that it would duplicate the implied private right of action under § 10(b) of the 1934 Act); \textit{Demoe v. Dean Witter \& Co.}, 476 F. Supp. 275 (D. Alaska 1979)(Section 17(a) private action held available only under § 17(a)(3) and not under § 17(a)(1) or § 17(a)(2)).
\item \textsuperscript{113} 652 F.2d 808 (9th Cir. 1981).
\item \textsuperscript{114} 672 F.2d 766 (9th Cir.), \textit{cert. denied}, 103 S. Ct. 444 (1982).
\item \textsuperscript{115} 551 F. Supp. 39 (S.D. Cal. 1982).
\item \textsuperscript{116} 490 F. Supp. 767 (W.D. Okla. 1980).
\item \textsuperscript{117} \textit{Id.} at 768.
\item \textsuperscript{118} \textit{Id.}
\item \textsuperscript{119} 489 F. Supp. 1270 (D. Kan. 1980).
\end{itemize}
tion under Section 17 is that plaintiffs will be unable to circumvent the
express civil remedies of both the 1933 and 1934 Acts. Such a rationale
was sufficient to satisfy it that a private right of action should not be
allowed under Section 17(a).120

IV. CONCLUSIONS

In view of the foregoing, it is submitted that Section 17(a) of the
Securities Act was not intended and should not be construed to support a
general implied private right of action. It is not inconsistent with legisla-
tive intent, however, to imply such a right under Section 17(a)(1) based
on fraudulent activities which are violative of that subsection. That is
the most reasonable interpretation of the Act.

As previously discussed,121 a number of courts have held that a gen-
eral right of action may be implied under Section 17(a) because the pro-
vision is "broad enough" to support such an interpretation and because
it is essentially identical to SEC Rule 10b-5, which by the overwhelming
weight of authority supports such an action. The validity of this view,
however, depends upon viewing Section 17(a) in a vacuum — unaffected
and uninfluenced by the remainder of the Act. The standard rules of
statutory construction do not permit such isolated consideration of indi-
vidual provisions. They must be viewed in conjunction with the remain-
der of the Act. When the section is so viewed, it compels the conclusion
reached by those courts which have held that Section 17(a) does not im-
ply a general private action. The existence of other sections expressly
calling for civil remedies (particularly Section 12), with restrictions and
limitations placed on those express remedies, shows that to imply a gen-
eral private remedy under Section 17(a) would enable the statutory
scheme to be circumvented.

Although superficially attractive, the "similarity" argument (i.e., be-
tween Section 17(a) and Rule 10b-5) does not withstand close scrutiny.
That the two provisions are almost identical, and that Rule 10b-5 gives
rise to a private action, supports the proposition that each such provision,
in itself and standing alone, is broad enough to create an implied private
action. But the two statutes are otherwise different. The Securities Act
has relatively comprehensive express private action provisions; the Ex-
change Act does not. Thus, there are provisions which restrict the inter-
pretation of Section 17(a) which do not apply to Section 10(b) or Rule
10b-5. Accordingly, Section 10(b) and Rule 10b-5, without such restric-
tions, may be reasonably interpreted to support a general private right of
action, but Section 17(a) which is subject to such restrictions should not
be so interpreted.

120 Id. at 1287. In so holding, the court reversed the position it had taken one month earlier
in Seiffer v. Topsy's Int'l, Inc., 487 F. Supp. 653 (D. Kan. 1980), where it held that there was an
implied private action under § 17(a) because it is virtually identical to Rule 10b-5.
121 See supra notes 58-60 and accompanying text.
It is also not persuasive to argue that a private action under Section 17(a) should be recognized once a right of action is recognized under Section 10(b) and Rule 10b-5. The coverage of Section 10(b) and Rule 10b-5 does not extend to every act or activity encompassed by Section 17(a), so that independent utility for a private action under Section 17(a) may exist. Even absent such an interpretation of the provisions of the two statutes, however, such an argument is insufficient. As the court noted in Woods v. Homes & Structures, Inc., it is an adequate refutation of that argument that the practical significance of denying a private action under Section 17(a) is that plaintiffs will be unable to use such an action to circumvent the express civil remedy provisions of the federal securities laws.

Although a general implied private action should not be recognized under Section 17(a), a private suit limited to an action under Section 17(a)(1) based upon fraudulent activities should be recognized. Dorfman v. First Boston Corp. is persuasive on this point. In Dorfman, the court noted that civil actions under Section 12 of the Securities Act are not limited to actions in which redress for fraud is sought. It is only necessary that the plaintiff has been damaged by a misstatement attributable to the defendant; fraudulent intent is not required. The court concluded that where a showing of fraud is required for a violation of Section 17(a), an implied private action free from the limitations of Section 12 should be recognized because of the more difficult burden of proof associated with showing fraud. The court pointed out, however, that not all of the language of Section 17(a) refers to language amounting to fraud. The court took the position that Section 17(a)(1), which makes it unlawful to employ any device, scheme, or artifice to defraud, and Section 17(a)(3), which makes it unlawful to engage in any transaction, practice, or course of business which would operate as a fraud or deceit upon the purchaser, require fraud. Section 17(a)(2), on the other hand, makes it unlawful 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 the light of the circumstances under which they were made, not misleading. That subsection does not require fraud for a finding of a violation. Accordingly, the court concluded that while an implied action may be maintained under Section 17(a)(2), it would be subject to the limitations applicable to Section 12. Such a holding is tantamount to saying that a violation of Section 17(a)(2) is subject to civil redress in a civil action brought under Section 12.

The structure and wording of Section 17(a)(2) and Section 12 are very similar, but they differ substantially from Sections 17(a)(1) and


\[123\] Id. at 1287. See also supra note 120 and accompanying text.


\[125\] Id. at 1095. See also supra note 90 and accompanying text.
17(a)(3). This supports the argument that Section 12 effectively provides a civil action corresponding only to Section 17(a)(2), leaving Sections 17(a)(1) and 17(a)(3) without express civil actions. This buttresses the conclusion of the *Dorfman* court that these latter two subsections, but not Section 17(a)(2), should be considered to support an implied private action free from the limitations and restrictions which apply to Section 12. However, because this conclusion was based in major part upon the proposition that those parts of Section 17(a) which entail a showing of fraud should be treated differently from those which do not, it is necessary to examine Section 17(a)(3) a bit more closely.

As previously noted, the Supreme Court has determined that a violation of Section 17(a)(1) requires scienter, but that a violation of Sections 17(a)(2) and 17(a)(3) does not. As to Section 17(a)(3), the Court emphasized that the subsection made it unlawful to engage in a transaction or conduct which *would operate* as a fraud or deceit. The Court concluded from that language that Section 17(a)(3) focuses on the effect of particular conduct on investors rather than on the culpability of the person responsible and, therefore, that scienter is not an element of violation of that subsection. Since fraud necessarily entails scienter, one is constrained by the Supreme Court's decision to conclude that Section 17(a)(3) is not a fraud provision.

In suggesting that the most reasonable interpretation of the Securities Act is that Section 17(a)(1) should be regarded as giving rise to an implied private action based on fraudulent conduct, it is recognized that some actions which would thereby be possible, could also be brought under Section 12, since that section, while not requiring fraud for a violation, does encompass activities which do involve fraud. To that extent, there would be an overlap of remedies. Not all violations of Section 17(a)(1), however, would give rise to an action under Section 12, since Section 12 is limited to actions based on misstatements or omissions, whereas Section 17(a)(1), a much broader provision, relates generally to fraudulent activities.

The interpretation urged here also remains subject to the countering argument that Congress provided for private actions to the extent that it wanted them to exist. Therefore, no additional remedies were intended. Congress, however, has proscribed different kinds of activities: some necessarily involving fraud and others involving a lesser degree of culpability. Congress did not expressly address the question whether a plaintiff, in seeking redress for activities involving a lesser degree of culpability than fraud, should have a more difficult burden of showing his right to recovery than a plaintiff seeking redress for fraudulent conduct. It is suggested, however, that the limitations and restrictions imposed on

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126 *See supra* notes 26-29 and accompanying text.
127 *But see* *Aaron v. SEC*, 446 U.S. 680, 696-97 (1980); *Dorfman*, 336 F. Supp. at 1095 (§ 17(a)(3) held to be a fraud provision).
Section 12 actions are more severe than might be expected in actions based on fraud. Hence, it is reasonable and not necessarily inconsistent with the express or implied intent of Congress, to imply a civil cause of action for fraud under Section 17(a)(1), which would not be subject to the limitations applicable to an action involving a defendant who might be held liable even though he was not guilty of fraud.

The solution offered is consistent with the philosophy employed by the Supreme Court in *Herman & MacLean v. Huddleston*. In holding that an action could be maintained under Section 10(b) of the Exchange Act based upon misrepresentations in a registration statement, notwithstanding the availability of a private action for such misrepresentations under Section 11 of the Securities Act, the Court in *Huddleston* pointed out the difference in scope of coverage of the two sections and emphasized that scienter is required for a violation of Section 10(b). Therefore, it must be shown for recovery under that Section, but there is no corresponding requirement for a showing of scienter under Section 11.

The suggested solution to the problem addressed herein reflects to some extent a retreat to the early position expressed by some courts, that there would seem to be little practical effect of such a solution since, if we limit implied actions under Section 17(a)(1) to fraud actions, most of the actions which might be brought in this manner also would be cognizable under Section 10(b) and Rule 10b-5. The overlap, however, would not be complete, because a potential action under Section 17(a) would extend to an action by an offeree, who neither bought nor sold securities, while a Section 10(b) action is limited to purchasers or sellers.

In summary, the circuits are about equally divided on the question whether Section 17(a) will support an implied private action. The better reasoned decisions appear to be those which have concluded that no such action is available, and the trend seems to be in that direction. This article suggests that although a general private action should not be recognized, a limited exception should be made. A private action should be implied for fraudulent activities which violate Section 17(a)(1) of the Act.

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