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Robinson v. Dean Witter Reynolds, Inc.: Searching for the Basis of an Implied Cause of Action Under SEC Rule 10B-16

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Margin trading is a method of stock acquisition that allows investors to buy securities by paying a portion of the purchase price, and obtaining a loan for the remaining amount. Brokers extending credit in margin transactions are required to disclose the terms of the credit agreement under Securities and Exchange Commission (SEC) Rule 10b-16. The SEC promulgated Rule 10b-16 in response to a congressional enactment that exempted securities margin transactions from the disclosure requirements of the

1 See L. Engel & B. Boyd, How to Buy Stocks 174-81 (7th ed. 1982); B. Stark, Special Situation Investing: Hedging, Arbitration and Liquidation 36-39 (1983). The term margin refers to the portion of the price that an investor contributes toward the purchase of a security. B. Stark, supra, at 36. The remaining amount is typically advanced to the investor by his broker or extended by a financial institution. See L. Engel & B. Boyd, supra, at 175-76. Interest is charged on the credit extended. B. Stark, supra, at 36-37. To secure its loan, the broker retains the securities in the street name of the brokerage firm as collateral. Id. at 37. If the value of the securities subsequently declines, thereby devaluing the broker's collateral, the broker may request additional margin (margin call). Id.; L. Engel & B. Boyd, supra, at 177. If a margin call is not met within a specified period, the broker may cancel the loan and sell the securities to affect repayment. Id. B. Stark, supra, at 37. This Comment will consider only margin transactions in a long account. See generally R. Auster, Option Writing and Hedging Strategies 7-15 (1975) (differentiating use of margin in long and short positions).

2 17 C.F.R. § 240.10b-16 (1985). The rule provides in pertinent part:

(a) It shall be unlawful for any broker or dealer to extend credit, directly or indirectly, to any customer in connection with any securities transaction unless such broker or dealer has established procedures to assure that each customer:

(i) is given or sent at the time of opening the account, a written statement or statements disclosing (i) the conditions under which an interest charge will be imposed; (ii) the annual rate or rates of interest that can be imposed; (iii) the method of computing interest; (iv) if rates of interest are subject to change without prior notice, the specific conditions under which they can be changed; (v) the method of determining the debit balance or balances on which interest is to be charged and whether credit is to be given for credit balances in cash accounts; (vi) what other charges resulting from the extension of credit, if any, will be made and under what conditions; and (vii) the nature of any interest or lien retained by the broker or dealer in the security or other property held as collateral and the conditions under which additional collateral can be required.

Id. (emphasis added).
Truth In Lending Act (TILA). While a private right of action is explicitly granted for violations of the TILA provisions, Rule 10b-16 does not expressly provide such a remedy. Federal courts, adjudicating margin investors' actions against brokers who have violated the disclosure requirements of Rule 10b-16, have produced inconsistent holdings. Recently, in *Robertson v. Dean Witter*...
Reynolds, Inc., \(^7\) the Court of Appeals for the Ninth Circuit recognized an implied private cause of action for violations of Rule 10b-16 and required proof of scienter as a prerequisite to recovery of damages.\(^8\)

In Robertson, the plaintiff-investor (Robertson) purchased treasury bonds on margin \(^9\) through his broker Dean Witter Reynolds, Inc. (Dean Witter). \(^10\) As interest rates rose, the value of the bonds, which represented the collateral for Dean Witter’s loan, fell.\(^11\) To secure its loan, Dean Witter made several requests for additional collateral over a period of seven months.\(^12\) When Robertson failed to meet these margin calls, Dean Witter sold the bonds to satisfy its outstanding loan, and Robertson suffered a substantial loss.\(^13\) Claiming that his loss was caused by Dean Witter’s failure to disclose the conditions on which credit was extended to him,\(^14\) Robertson brought suit alleging violations of sec-

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\(^8\) Id. at 534, 539-41.

\(^9\) Id. at 533; see supra note 1.

\(^10\) Robertson, 749 F.2d at 532-33. In Robertson, the plaintiff (Robertson) opened a brokerage account on Aug. 15, 1980. Id. On Jan. 22, 1981, Robertson purchased margin treasury bonds with a face value of $500,000 for $367,138 by paying $36,714 down. Id. at 533. The treasury bonds in question were substantially discounted from their face value because interest rates had risen since their issuance. Id.

\(^11\) Id. at 533; see supra note 1.

\(^12\) Robertson, 749 F.2d at 533; see supra note 1.

\(^13\) Robertson, 749 F.2d at 533. Robertson incurred a loss exceeding $149,000, including his $36,714 down payment, $76,753 paid in interest charges to Dean Witter, and $36,000 paid to reduce the principal of his debt. Id.

\(^14\) Id. at 533. The Robertson court tacitly accepted the allegation that the failure of Dean Witter to disclose credit information caused the loss of Robertson’s investment in the bonds. See id. at 533-41. In securities cases where the defendant has an obligation to disclose information but fails to do so, the causal connection between nondisclosure and the injury can be established by showing that the information withheld was material. See Affiliated Ute Citizens v. United States, 406 U.S. 128, 153-54 (1972). A fact is material when a reasonable investor would have considered it important in deciding whether to invest. See TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 446-49 (1976). By violating the specific disclosure requirements of Rule 10b-16, Dean Witter withheld information that Congress and the SEC determined investors needed to know to intelligently select a broker for a credit transaction. See SEC Release No. 34-8773 (December 16, 1969), 34 Fed. Reg. 19,717,
tion 10(b) of the Securities Exchange Act of 1934 (Exchange Act)\(^5\) and SEC Rule 10b-16.\(^6\) The district court dismissed the suit for failure to state a claim upon which relief could be granted.\(^7\) On appeal, the Ninth Circuit reversed.\(^8\)

Writing for a unanimous court, Judge Nelson employed a two-step analysis\(^9\) determining first that the SEC was congressionally authorized to establish rules implying a private cause of action under section 10(b) of the Exchange Act,\(^10\) and that Rule 10b-16 was drafted such that the private right of action in section 10(b) could legitimately be implied into the Rule.\(^11\) The Court of Appeals for the Ninth Circuit rejected Robertson’s argument that the necessary congressional intent for an implied right of action is in the TILA, and held that the proper source of statutory authority is section 10(b) of the Exchange Act.\(^12\) The court declared that the existence of an implied cause of action under section 10(b) is “well-established”\(^13\) and that Congress gave the SEC broad authority to promulgate rules pursuant to section 10(b).\(^14\) The court reasoned


\(^{16}\) 17 C.F.R. § 240.10b-16 (1986); Robertson, 749 F.2d at 533.

\(^{17}\) Robertson, 749 F.2d at 532. “A complaint may be dismissed as a matter of law for two reasons: [1] lack of a cognizable legal theory, or [2] insufficient facts under a cognizable legal claim.” 2A J. Moore, Moore’s FEDERAL PRACTICE ¶ 12.08 at 2271 (2d ed. 1982). Robertson exposed himself to dismissal on both grounds by asserting that Rule 10b-16 provides an implied cause of action, and by failing to plead facts alleging scienter. See Robertson, 749 F.2d at 534. The district court did not indicate whether the dismissal was based on lack of a private cause of action or the failure to plead scienter; to prevent an immediate successive appeal by either party, therefore, the Ninth Circuit addressed both issues. Id.

\(^{18}\) See Robertson, 749 F.2d at 534.

\(^{19}\) Id. at 534; see infra notes 43-46 and accompanying text.

\(^{20}\) See Robertson, 749 F.2d at 534-36.

\(^{21}\) See id. at 536-39.

\(^{22}\) See id. at 534-35.


\(^{24}\) 749 F.2d at 536. Section 10(b) proscribes the “contravention of such rules and regulations as the [SEC] may prescribe as necessary or appropriate in the public interest or for the protection of investors.” 15 U.S.C. § 78j(b) (1982); see infra note 47 (§ 10(b) set forth). Section 23(a) grants the SEC “power to make such rules and regulations as may be necessary or appropriate to implement the provisions of this chapter . . . or for the execution of the functions vested in [the SEC] by this chapter . . . .” Securities Exchange Act of 1934, §
that although a private remedy under section 10(b) is implied on the basis of judicial construction rather than congressional intent, such remedy should be implied into rule 10b-16 because the rule is reasonably related to the anti-fraud goals of section 10(b). 26

The Robertson court held that the pleadings of a plaintiff could not be complete without an allegation of scienter. 27 Judge Nelson declared that the rationale of Ernst & Ernst v. Hochfelder, 28 in which the Supreme Court held that plaintiffs who brought private actions under section 10(b) and Rule 10b-5 must allege scienter, 29 "requires us to hold that pleading scienter is requisite to maintaining an action brought pursuant to Rule 10b-16." 30 While the court recognized that requiring scienter in actions based on the disclosure standards of Rule 10b-16 might undercut the effectiveness of the margin disclosure regulation, 31 it nonetheless maintained that the resolution of such inequalities was beyond judicial power. 32

Although the Ninth Circuit determined that an implied cause of action is available to margin investors suffering losses as a result

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23a, 15 U.S.C. § 78w(a)(1) (1982). The authority of the SEC to adopt rules and regulations necessary for the execution of its functions has been interpreted as “broad.” See Commercial Capital Corp. v. SEC, 360 F.2d 856, 857 (7th Cir. 1966); see also Hooper v. Mountain States Sec. Corp., 282 F.2d 195, 202 (5th Cir. 1960) (suggestion that SEC has broad authority to regulate under section 10(b)), cert. denied, 365 U.S. 814 (1961).


28 See Robertson, 749 F.2d at 541.


30 Id. at 194-214. See generally Note, Scienter’s Scope and Application in Rule 10b-5 Actions: An Analysis in Light of Hochfelder, 52 NOTRE DAME LAW. 925 (1977) (examining import and suggesting appropriate treatment of scienter standard enunciated by Hochfelder on private suits seeking damages or SEC injunctions).

31 Robertson, 749 F.2d at 540.

of inadequate disclosure of credit terms, the court’s conclusion that section 10(b) of the Exchange Act provides the basis for an implied remedy unduly limits the availability of such relief for injured investors. It is asserted that an analysis originating from section 10(b) of the Exchange Act mistakenly permits courts to infuse that section’s judicially created scienter requirement into an implied 10b-16 nondisclosure action. Such an infusion frustrates the congressional mandate to ensure disclosure in securities margin transactions. This Comment will suggest that the TILA, not section 10(b) of the Exchange Act, provides the congressional intent supporting a private remedy under Rule 10b-16, and therefore the plaintiff should not be required to alleged scienter.

Appropriateness of Section 10(b) as the Basis for Securities Margin Non-Disclosure Actions

The judicial standard for finding an implied cause of action within a federal statute was enunciated by a unanimous Supreme Court in Cort v. Ash. Restraining a previously expansive trend, the Court articulated four factors relevant to determining whether an implicit cause of action should exist. The Supreme Court has

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33 See Cannon v. University of Chicago, 441 U.S. 677, 730 n.1 (1979) (Powell, J., dissenting). A private cause of action has been defined as "the right of a private party to seek judicial relief from injuries caused by another's violation of a legal requirement. Id. In the context of legislation enacted by Congress, the legal requirement involved is a statutory duty." Id.


36 See Cort, 422 U.S. at 78. The four factors are:

First, 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? Second, is there any indication of legislative intent, explicit or implicit, either to create such a remedy or to deny one? Third, is it consistent with the underlying
purposes of the legislative scheme to imply such a remedy for the plaintiff? And finally, is the cause of action 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?

Id. (citations omitted).

Although it is not necessary to satisfy all four Cort factors, see Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran, 456 U.S. 353, 388 (1982), it is submitted that the four factors are met when Rule 10b-16 is violated. First, Rule 10b-16 was clearly created for the "special benefit" of persons, such as Robertson, who purchased securities on margin from federally registered brokers. See SEC Release, supra note 14, at 19,717. Second, while explicit indicators of legislative intent do not negate an implied right of action, see H.R. Rep., supra note 3; S. Rep., supra note 3, implicit indicators strongly suggest a congressional intent to create a private remedy. See Haynes v. Anderson & Strudwick, Inc., 508 F. Supp. 1303, 1320-21 (E.D. Va. 1981); infra notes 68-69 and accompanying text. Third, implication of a private right of action is consistent with the legislative scheme of the TILA. See 15 U.S.C. §§ 1635, 1640 (1982); cf. Haynes, 508 F. Supp. at 1319 ("the [TILA] and the Rule should be read in harmony, if at all possible"). It is also consistent with the legislative scheme of the federal securities acts to imply a private right of action. See, e.g., Herman & MacLean v. Huddleston, 459 U.S. 375, 380 (1983) ("[I]n addition to the private actions created explicitly by the 1933 and 1934 Acts, federal courts have implied private remedies under other provisions of the two laws."); J.I. Case Co. v. Borak, 377 U.S. 426, 431-35 (1964) (private cause of action implied under § 14(a) of the 1934 Act); Dan River, Inc. v. Unitex, Ltd., 624 F.2d 1216, 1222-24 (4th Cir. 1980) (private cause of action implied under section 13(d) of the 1934 Act), cert. denied, 449 U.S. 1101 (1981). Fourth, the TILA and the federal securities acts were created by Congress to fill specific needs previously unmet by state regulation, one of which was the disclosure of credit terms in connection with federal securities transactions. See S. Rep. supra note 3, at 1-3; H.R. Rep. supra note 3, at 8-9, 13; Ernst & Ernst v. Hochfelder, 425 U.S. 185, 194-95 (1976).


38 Cf. California v. Sierra Club, 451 U.S. 287, 302 (1980) (Rehnquist, J., concurring). Four justices have agreed that "the so-called Cort factors are merely guides in the central task of ascertaining legislative intent." Id.


40 Robertson, 749 F.2d at 594. Because the rule was not enacted directly by Congress,
cuit in *Jablon v. Dean Witter & Co.*, the bifurcated test requires a court to determine "(1) whether Congress intended to delegate authority to establish rules implying a private right of action; [and] (2) whether the . . . rules were drafted such that a private action may legitimately be implied."

It is submitted that the components of the *Jablon* test were misstated and misapplied by the *Robertson* court, thus rendering its reasoning and result erroneous.

The *Robertson* court did not correctly state the first prong of the *Jablon* test as "whether Congress intended to delegate authority to establish [a rule] implying a private right of action," but rather misstated the test as "whether Congress delegated authority to establish [a rule] implying a private right of action."

Premising the inquiry in this manner, the *Robertson* court confused the fundamental question of congressional intent to permit a private action for violations of margin disclosure rules with the SEC’s authority to issue Rule 10b-16. Unquestionably, Congress intended that the SEC promulgate rules to supplement section 10(b) of the Exchange Act, but congressional intent to provide disclosure of

but by the SEC acting on authority delegated by Congress, the *Robertson* court used the *Jablon* consideration. *See infra* notes 41-42 and accompanying text. The existence of a cause of action derived from a federal statute is a question of statutory construction. *See* Touche Ross v. Redington, 442 U.S. 560, 568 (1979); Cannon v. University of Chicago, 441 U.S. 677, 688 (1979). Since Rule 10b-16 is not a statute but a rule promulgated pursuant to a statute, a two-step analysis was necessary. *See Robertson*, 749 F.2d at 536.


* 42 *Jablon*, 614 F.2d at 679.

* 43 *Id.* (emphasis added).

* 44 *Robertson*, 749 F.2d at 534 (emphasis added).

* 45 *See supra* note 42 and accompanying text.

* 46 *See Robertson*, 749 F.2d at 535.

* 47 *See* 15 U.S.C. § 78j(b) (1982). Section 10(b) states:

> 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 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 securities national 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.

*Id.* (emphasis added).
securities margin credit terms is not found within section 10(b). Congress intended that a securities margin disclosure rule analogous to the TILA regulations be enacted, but allowed the SEC discretion to choose an appropriate power base. After Congress exempted securities margin disclosures from TILA, the SEC chose section 10(b) and the general regulatory power under section 23(a) of the Exchange Act as the authority under which to issue Rule 10b-16.

Allowing congressional intent for an implied cause of action to be derived from a power base selected by the SEC would permit the intent of Congress to vacillate according to the choice made by the SEC. Therefore, it is submitted that the Ninth Circuit improperly concluded that the congressional intent necessary to imply a private cause of action is found in section 10(b) of the Exchange Act.

The Robertson court next considered the second prong of the Jablon test, determining whether Rule 10b-16 "was drafted such that [a] private action may legitimately be implied." Accepting

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44 See S. REP. supra note 3, at 9; SEC Release supra note 14, at 19,717; Margin Credit, supra note 33, at 391 n.71; Comment, supra note 31, at 1059-60; see also Haynes v. Anderson & Strudwick, Inc., 508 F. Supp. 1303, 1320 (E.D. Va. 1981) (since Rule 10b-16 was promulgated as the analogue of TILA, court should be guided by whether Congress created a private right of action under TILA in determining whether a private right of action should be implied under Rule 10b-16). But see Furer v. Paine, Webber, Jackson & Curtis, Inc., [1982 Transfer Binder] FED. SEC. L. REP. CCH 98,701 at 93, 495 (C.D. Cal. 1982); Abeles v. Oppenheimer & Co., 597 F. Supp. 532, 536 (N.D. Ill. 1983). The Senate Report stated: "In recommending an exemption for stockbroker margin loans in the [TILA], the Committee intends for the SEC to require substantially similar disclosure by regulation as soon as it is possible to issue such regulation." S. REP. supra note 3, at 9 (emphasis added).

45 See S. REP. supra note 3, at 9. The Senate Report stated that "[t]he committee has been informed by the Securities and Exchange Commission that the Commission has adequate regulatory authority under the Securities Exchange Act of 1934 to require adequate disclosure of the costs of such credit." Id. The Senate Report also stated that the "SEC already has the power to require margin disclosure under the 1933 Securities Act." Id. at 22. Additionally, the House Report indicated that the SEC's authority to issue a margin disclosure regulation was embodied in the 1933 Act, not section 10(b) of the 1934 Act. See H.R. REP. supra note 3, at 28 ("the SEC is authorized to require disclosure as to [margin] transactions under the Securities Act of 1933").


55 See Jablon v. Dean Witter & Co., 614 F.2d 677, 679 (9th Cir. 1980); supra notes 41-43 and accompanying text.

58 Robertson, 749 F.2d at 534.
arguendo the court's determination that section 10(b) is the proper source of the congressional intent for securities margin disclosure rules with an implied private remedy, it is submitted that Rule 10b-16 was not drafted so that a cause of action under section 10(b) may legitimately be implied into it. Section 10(b) is a "catch-all" anti-fraud statute designed to prohibit knowing and intentional misconduct. Rule 10b-16, however, is a mechanical disclosure provision designed to protect and inform investors. The Robertson court affixed an anti-fraud statute cause of action to a disclosure rule because it determined that fraud prevention and disclosure were reasonably related goals. Admittedly, the promotion of disclosure helps prevent fraud, but it is suggested that the Robertson court's action was illegitimate in a section 10(b) context. The language used by Congress in section 10(b) necessitates a re-

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56 Id. at 535.
The Rule requires an initial disclosure and periodic disclosures. The initial disclosure is designed to insure that the investor, before his account is opened, understands the terms and conditions under which credit charges will be made. This will enable him to compare the various credit terms available to him and to understand the methods used in computing the actual credit charges. The periodic statement will inform the investor of the actual cost of credit and, with the aid of the initial disclosure, enable him to accurately assess that cost.
SEC Release, supra note 14, at 19,717.
59 Robertson, 749 F.2d at 539. Having found § 10(b) to be the proper basis for implication of a private right of action, id. at 535, the Robertson court reasoned that it need only review Rule 10b-16 to determine whether it was reasonably related to the purposes of its enabling statute, also section 10(b). See id. at 537; see Mourning v. Family Pub. Serv. Inc., 411 U.S. 356, 359 (1973); American Hosp. Management Corp. v. Harris, 638 F.2d 1205, 1212 (9th Cir. 1981).
60 See Affiliated Ute Citizens v. United States, 406 U.S. 128, 151 (1972); O'Brien v. Continental Ill. Nat'l Bank & Trust Co., 593 F.2d 54, 60 (7th Cir. 1979); Arber v. Essex Wire Corp., 490 F.2d 414, 418 (6th Cir. 1974); Dooley, Enforcement of Insider Trading Restriction, 66 Va. L. Rs. 1, 62-63 (1980); Comment, supra note 57, at 949-68.
61 15 U.S.C. § 78j(b) (1982). Section 10(b) states in pertinent part that: "It shall be unlawful . . . to use or employ . . . any manipulative or deceptive device or contrivance"; see also supra note 47 (§10(b) in greater detail).
requirement of scienter for an implied section 10(b) action. However, this strong anti-fraud language is manifestly absent from Rule 10b-16, suggesting that Rule 10b-16 was not narrowly designed to thwart only manipulative and fraudulent conduct, but was broad in scope so as to encompass conduct that unintentionally causes harm. Allowing an antifraud provision to act as the touchstone for a nondisclosure action illogically encumbers the remedy with a scienter burden, thereby frustrating the congressional purpose behind the margin disclosure provision.

THE TILA AS THE PROPER SOURCE OF CONGRESSIONAL INTENT

The TILA gives consumers an express right of action for nondisclosure of credit terms. Since Congress intended the securities margin disclosure rules to be “substantially similar” to the TILA disclosure provisions, it is suggested that the congressional intent behind the TILA should be utilized to imply a private cause of action for violations of Rule 10b-16. This would demonstrate that Congress intended to delegate authority to the SEC to establish a securities margin disclosure rule implying a private right of action, and that a disclosure rule like Rule 10b-16 could be drafted such that a private cause of action could legitimately be implied from the TILA.

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62 Ern`st & Ernst v. Hochfelder, 425 U.S. 185, 197-99 (1976). The Court stated: “The words ‘manipulative or deceptive’ used in conjunction with ‘device or contrivance’ strongly suggest that § 10(b) was intended to proscribe knowing or intentional misconduct.” Id. at 197.

63 See 17 C.F.R. § 240.10b-16 (1985); supra note 2 (Rule 10b-16 set forth in pertinent part).


65 See Margin Credit, supra note 31, at 376, 387, 390 n.66; Comment, supra note 31 at 1079.

66 See supra note 4 and accompanying text.

67 See S. Rep., supra note 3, at 9; supra note 48 and accompanying text.


69 See supra notes 47-52 and accompanying text.

70 See supra notes 66-68 and accompanying text.
THE SCIENTER REQUIREMENT

Relying on the Exchange Act and the Hochfelder decision, the Robertson court erroneously required scienter as a necessary element of an implied cause of action under Rule 10b-16.71 While Rule 10b-5 shares the anti-fraud language and legislative history of section 10(b), and thus warrants a scienter requirement, Rule 10b-16 shares neither the language nor the legislative history of section 10(b).72 Moreover, the concerns that prompted the Hochfelder

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71 See Robertson, 749 F.2d at 539-41. Drawing from Hochfelder, the Robertson court based its Rule 10b-16 scienter requirement on the structure of the Securities Act of 1933 and the Exchange Act of 1934, noting that in each instance in which Congress had expressly created a civil remedy, it also specified the standard of liability. Id. at 540. See Hochfelder, 425 U.S. at 208-10. Therefore, the Robertson court reasoned, applying section 10(b) to merely negligent conduct ignores the fact that “when Congress intended to accomplish that result, it did so expressly, and subjected these actions to procedural restrictions not found under section 10(b).” See Robertson, 749 F.2d at 540; Hochfelder, 425 U.S. at 206-11. However, when Congress intended a scienter standard under the securities laws, it also specifically provided for such. See Hochfelder, 425 U.S. at 207-08. Therefore, this specificity-of-standards argument becomes a two-edged sword that can be used to preclude a scienter standard, as well as a negligence standard, for an implied cause of action under section 10(b). See Bucklo, The Supreme Court Attempts to Define Scienter Under Rule 10b-5: Ernst & Ernst v. Hochfelder, 29 STAN. L. REV. 213, 225 (1977). Because Congress did not provide an express remedy in section 10(b), the procedural context of the remedies it did expressly consider gives little insight into the extent of the section 10(b) duty. See Comment, Securities Law—Private Cause of Action for Damages Under Rule 10b-5 Requires Scienter—Ernst & Ernst v. Hochfelder, 25 EMORY L.J. 465, 467-68 (1976).


Employment of manipulative and deceptive devices.

It shall be unlawful . . .

(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 (1985) (emphasis added). See supra note 47 (section 10(b) set forth in pertinent part). While there is a “dearth of evidence” in legislative history concerning the congressional intent behind section 10(b), see 1 A. Bromberg, Securities Law: Fraud—Sec Rule 10b-5, § 2.2 (331) at 22.2 (1975), the pertinent legislative history that exists demonstrates a commonality between section 10(b) and Rule 10b-5. See Hochfelder, 425 U.S. at 201-06; S. REP. No. 792, 73d Cong., 2d Sess. 7-9 (1934); H.R. REP. No. 1383, 73d Cong., 2d Sess. 10-11, 20-21 (1934); H.R. CONF. REP. No. 1388, 73d Cong., 2d Sess. 32-33 (1934); Hearings on H.R. 7852 and H.R. 8720 Before the House Comm. on Interstate and Foreign Commerce, 73d Cong., 2d Sess. 115 (1934); see also SEC Exchange Act Release No. 3230 (May 21, 1942) (Rule 10b-5 expanded to include all individuals and companies within anti-fraud rules that theretofore applied only to brokers and dealers). See generally Berner & Franklin, Scienter and Securities and Exchange Commission Rule 10b-5 Injunctive Actions: A
court to impose a scienter requirement under section 10(b) and Rule 10b-5—that unless the scope of section 10(b) was limited to knowing or intentional misconduct, actions for negligence could be brought under section 10(b) rather than under the more limited express remedy provisions of the securities acts, undermining the overall effectiveness of the securities laws—are not present in a Rule 10b-16 situation. Because Rule 10b-16 is purely a "mechanical rule" that "sets forth objectives and specific disclosure requirements for credit terms in margin transactions," it is submitted that no interference with the comprehensive enforcement scheme of the securities acts will arise if scienter is not imposed under Rule 10b-16. Finally, when Rule 10b-16 was promulgated, there was no scienter requirement in actions brought under section 10(b). Therefore, it cannot be argued that Congress or the SEC intended to make scienter a requirement in actions under Rule 10b-16.

CONCLUSION

The availability of an implied cause of action for a violation of Rule 10b-16 insures complete disclosure in margin securities transactions and fosters informed investment. While the essential question is whether Congress intended that the courts create a private remedy, the Robertson court mistakenly found the requisite congressional intent in section 10(b) of the Exchange Act. However, by deriving the intent of Congress from the TILA, as this Comment has suggested, the obtrusive requirement of scienter would be eliminated and the underlying purpose of Rule 10b-16 would be more effectively promoted.

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