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THE ASSIGNMENT OF PRIVATE CAUSES OF ACTION UNDER THE FEDERAL SECURITIES LAWS: EXPRESS VERSUS AUTOMATIC ASSIGNMENT

In the years after the stock market crash of 1929, Congress enacted statutes regulating the issuance and sale of securities, the Securities Act of 1933 (1933 Act) and the Securities Exchange Act of 1934 (1934 Act).¹ Congress directed the two statutes at the unfair and dishonest conduct of securities underwriters and securities dealers that had contributed to the stock market crash of 1929.² Section 10(b) of the 1934 Act (section 10(b))

1. Securities Act of 1933, 15 U.S.C. §§ 77a-77aa (1982); Securities Exchange Act of 1934, 15 U.S.C. § 78 (1982). Prior to the enactment of the Securities Act of 1933 (1933 Act) and the Securities Exchange Act of 1934 (1934 Act), 47 of the 48 states had passed "blue sky laws" discouraging corporations from engaging in speculative issuances of securities. L. Loss, *SECURITIES REGULATION* 18-19 (1951). State blue sky laws, however, did not sufficiently protect investors in securities from the questionable practices of issuers of securities because the state laws did not affect interstate business transactions, states often lacked sufficient budgets or personnel to enforce their blue sky laws, and some of the state blue sky laws contained so many exemptions that the laws were ineffective. *See id.* at 43, 56-58 (analyzing shortcomings of state blue sky laws).

In addition to the ineffectiveness of state legislation in addressing the issues of fraud and deception in securities transactions, both a failed campaign for federal incorporation and licensing legislation and government concern over fraudulent bond trading during World War I contributed to a demand for federal legislation regulating securities. *See id.* at 58-66 (discussing factors before stock market crash of 1929 that pressured Congress to consider legislation regulating securities). In 1929 the stock market crash prompted the Senate Banking and Currency Committee to begin investigating securities trading and commercial and investment banking. *Id.* at 75-76. President Franklin D. Roosevelt wrote a letter to Congress requesting legislation governing the issuance of securities and stressing the importance of requiring full disclosure to the buying public of all important information regarding securities issuances. H.R. REP. NO. 85, 73d Cong., 1st Sess. 1-2 (1933). Congress responded to demands for legislation, first, by enacting the Securities Act of 1933, which addresses new offerings of securities. *See id.* at 5 (scope of 1933 bill extends only to new offerings of securities, not ordinary redistribution of securities). Second, Congress enacted the Securities Exchange Act of 1934, which concerns the post-issuance trading of securities and authorizes the Securities Exchange Commission (SEC) to make and enforce rules governing fraud and manipulation in the securities markets. L. Loss, *supra*, at 84-85.

2. H.R. REP. NO. 85, 73d Cong., 1st Sess. 2-3 (1933). The abandonment by underwriters and dealers in securities of standards of fair, honest and prudent dealing made possible the postwar flotation of fraudulent securities. *Id.*; *see* S. REP. NO. 792, 73d Cong., 2d Sess. 3 (1934) (acknowledging that uncontrolled speculation by dealers in securities helped cause stock market crash of 1929 and calling for regulation to protect public). In Congress' report on the need for legislation regulating the sale of securities, Congress reported that, in the decade after World War I, \$25,000,000 worth of worthless securities entered the market. H.R. REP. NO. 85, 73d Cong., 1st Sess. 2 (1933). Congress accused underwriters and dealers in securities of promising investors "easy wealth" without assisting investors in estimating the value of securities. *Id.* Because of the resulting high demand for securities, investment bankers and underwriters forced corporations unnecessarily to issue securities to meet the demand. *Id.* Congress concluded that these unfair and dishonest actions led to the inaccurate valuation of corporate properties and the flotation of essentially worthless securities. *Id.*

forbids the use of "any manipulative or deceptive device or contrivance" that violates the rules and regulations of the Securities and Exchange Commission (SEC).³ Rule 10b-5 of the SEC Rules (rule 10b-5), enacted several years after the stock market crash, prohibits the use of fraudulent devices or untrue statements of material facts by any person "in connection with the purchase or sale of any security."⁴ Although rule 10b-5 does not expressly provide a remedy for violations of the rule's provisions,⁵ in 1971 the United States Supreme Court held that the rule itself implies a private right of action for alleged violations of the rule's provisions.⁶ Subsequently,

3. Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j (1982). Section 10(b) of the 1934 Act provides that no person lawfully may employ, in connection with the purchase or sale of any security, a manipulative or deceptive device that would violate any rules or regulations that the SEC might prescribe. *Id.* One of the six primary purposes of Congress in enacting the Securities Exchange Act of 1934 was the control of manipulative corporate practices. H.R. REP. No. 1383, 73d Cong., 2d Sess. 7 (1934). By enacting provisions like section 10(b), Congress intended to promote securities pricing based on the balance of investment demand with investment supply. *Id.* at 10. Furthermore, Congress hoped to discourage misleading statements on the value of securities and the purposeful marking up or down of prices. *Id.*

4. Securities and Exchange Commission Rules, 17 C.F.R. § 240.10b-5 (1980). Rule 10b-5 provides that, in purchasing or selling securities, no person shall employ any "device, scheme, or artifice" to defraud, make an untrue statement of a material fact, or omit a material fact that is necessary to prevent the statements from being misleading. *Id.* Furthermore, rule 10b-5 prohibits all persons from engaging in any fraudulent or deceitful act, practice, or course of business in connection with the purchase or sale of any security. *Id.*

5. *See id.* (describing activities that shall be unlawful if conducted in connection with purchase or sale of any security); H. BLOOMENTHAL, SECURITIES LAW HANDBOOK § 12.01 (1987) (general fraud provision of rule 10b-5 does not provide express remedy for fraud).

6. Superintendent of Ins. v. Bankers Life & Casualty Co., 404 U.S. 6, 12 (1971). In *Bankers Life* the United States Supreme Court considered for the first time whether a private corporation could base a claim against issuers of securities on violations of section 10(b) of the 1934 Act and rule 10b-5 of the SEC Rules. *Id.* at 6. In *Bankers Life* the defendant, Bankers Life & Casualty Company (Bankers Life), sold all of Manhattan Casualty Company's (Manhattan) stock to Begole, a shareholder and director of Manhattan. *Id.* at 8. Begole fraudulently paid for the Manhattan stock with Manhattan's assets. *Id.* To accomplish the fraud on Manhattan, Begole procured a check from Irving Trust Company for the purchase price of the Manhattan stock, although Begole had no funds on deposit with Irving Trust. *Id.* On the same day that Begole purchased all of the Manhattan stock, Begole and several other Manhattan directors installed a new president of Manhattan. *Id.* Under its new President, Manhattan immediately sold United States Treasury bonds and deposited the proceeds from the bonds sale and some cash in Manhattan's Irving Trust account. *Id.* Irving Trust then charged Begole's original check for the purchase of the Manhattan stock against the new deposit of proceeds from the sale of the United States savings bonds. *Id.* Despite this depletion of Manhattan's assets, the Manhattan books did not show Begole's use of the Manhattan assets to finance Begole's purchase of Manhattan securities. *Id.* at 8-9. The plaintiff, Manhattan's liquidator, sued Bankers Life under section 10(b) of the 1934 Act, alleging that Bankers Life defrauded Manhattan by selling the Manhattan securities to Begole. *Id.* at 7. The United States District Court for the Southern District of New York dismissed Manhattan's complaint, basing its decision on section 10(b) and rule 10b-5, and the United States Court of Appeals for the Second Circuit affirmed. *See id.* at 7 (discussing lower courts' disposition of *Bankers Life*). Manhattan appealed the Second Circuit's decision

in resolving a number of issues associated with rule 10b-5, the Supreme Court held that only actual purchasers and sellers of securities may bring damages actions under rule 10b-5.⁷ The Supreme Court has not determined, however, whether a purchaser or seller of a security who possesses a rule 10b-5 right of action or another right of action under the 1933 or 1934 Acts either expressly or automatically assigns the right of action to a subsequent purchaser of the security. Although the Supreme Court has not decided the assignment issue, several lower federal courts have recognized the issue.⁸ A majority of the federal courts addressing the issue

to the United States Supreme Court and the Supreme Court granted Manhattan's writ of certiorari. *Id.* at 9. The Supreme Court determined that section 10(b) of the 1934 Act, under which employing any manipulative or deceptive device in connection with the purchase or sale of securities is unlawful, protected Manhattan as a seller of Treasury bonds. *Id.* The Supreme Court found that the defendant injured Manhattan by fraudulently leading Manhattan into believing that Manhattan would receive the proceeds from the sales of the bonds. *Id.* at 9-10. The Supreme Court reasoned that, because Bankers Life acted fraudulently in connection with the sale of a security, section 10(b) provided a remedy for Manhattan. *Id.* at 12. Accordingly, the Supreme Court reversed the Second Circuit's dismissal of *Bankers Life* and remanded the case for trial. *Id.* at 13; *see also* *J. I. Case Co. v. Borak*, 377 U.S. 426, 432 (1964) (recognizing that private enforcement of SEC rules might become necessary in addition to SEC action to enforce rules); *Kardon v. National Gypsum Co.*, 69 F. Supp. 512, 513 (E.D. Pa. 1946) (concluding that plaintiff was intended beneficiary of statute and therefore could maintain private action under rule 10b-5).

7. *See* *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 730-31 (only actual purchasers and sellers of securities may assert claims in private damages action under section 10(b) and rule 10b-5), *rehearing denied*, 423 U.S. 884 (1975); *infra* notes 115-21 and accompanying text (discussing facts and Supreme Court's reasoning in *Blue Chip*); *see also* *Birnbaum v. Newport Steel Corp.*, 193 F.2d 461, 463 (2d Cir.) (only actual purchasers and sellers of securities may maintain private damages actions under section 10(b) and rule 10b-5), *cert. denied*, 343 U.S. 956 (1952).

8. *See, e.g., In re Nucorp Energy Sec. Litig.*, 772 F.2d 1486, 1490 (9th Cir. 1985) (federal cause of action that arises from original security holder's reliance on misrepresentation does not follow security to remote purchaser who did not rely on misrepresentation); *Lowry v. Baltimore & O. R.R.*, 707 F.2d 1207, 1209 (3d Cir.) (per curiam) (rule 10b-5 actions are assignable if owner expressly assigns rule 10b-5 action to subsequent purchaser of owner's security), *modification denied*, 711 F.2d 1207 (3d Cir.), *cert. denied*, 464 U.S. 893 (1983); *Soderberg v. Gens*, 652 F. Supp. 560, 563-64 (N.D. Ill. 1987) (federal cause of action does not attach automatically to security and pass to subsequent purchaser); *Ciarlante v. CSX Corp.*, 629 F. Supp. 534, 537 (W.D. Pa. 1986) (federal law does not provide for automatic assignment of federal securities laws claims); *In re Saxon Sec. Litig.*, 644 F. Supp. 465, 471 (S.D.N.Y. 1985) (assignment of rule 10b-5 right of action to subsequent purchaser does not occur automatically); *Rose v. Arkansas Valley Envtl. & Util. Auth.*, 562 F. Supp. 1180, 1188 (W.D. Mo. 1983) (because only defrauded purchasers and sellers may bring actions under rule 10b-5, purchaser of security who does not allege fraud does not acquire rule 10b-5 right of action by automatic assignment); *Independent Investor Protective League v. Saunders*, 64 F.R.D. 564, 572 (E.D. Pa. 1974) (right of action belonging to defrauded security holder does not travel automatically to subsequent purchaser of security, even if subsequent purchaser was victim of fraud); *International Ladies' Garment Workers' Union v. Shields & Co.*, 209 F. Supp. 145, 149 (S.D.N.Y. 1962) (rule 10b-5 actions for remedial damages are assignable); *Mills v. Sarjem Corp.*, 133 F. Supp. 753, 761-62 (D.N.J. 1955) (because at common law nonpersonal and nonpenal damages actions were assignable, rule 10b-5 remedial damages actions survive security holder's death and are assignable).

of assignment of securities law causes of action has decided that, although an action under the securities statutes does not travel automatically with a security to a subsequent purchaser, an owner of a security expressly may assign the owner's securities law claim to a subsequent purchaser.⁹

Addressing the issue of the assignment of a rule 10b-5 cause of action in *Lowry v. Baltimore & Ohio Railroad Co.*,¹⁰ the United States Court of Appeals for the Third Circuit considered whether purchasers of convertible debentures of the Baltimore and Ohio Railroad Company (B & O) could assert the section 10(b) and rule 10b-5 claims of previous owners of the debentures.¹¹ In *Lowry* the plaintiffs, who had purchased debentures from previous debentureholders, claimed that the previous debentureholders automatically had assigned their section 10(b) and rule 10b-5 claims to the plaintiff purchasers of the debentures.¹² In considering the plaintiffs' claim of automatic assignment, the *Lowry* court first examined the facts upon which the previous owners had based their section 10(b) and rule 10b-5 causes of action.¹³ The court in *Lowry* noted that the previous debentureholders had purchased their debentures from B & O at a time when B & O owned rail and nonrail assets.¹⁴ The debentures thus were convertible into common stock representing both the rail and nonrail assets of B & O.¹⁵ After the previous debentureholders purchased their debentures, B & O transferred all of its nonrail assets to Mid-Allegheny, a subsidiary corporation of B & O.¹⁶ On December 13, 1977, B & O declared a stock

9. See, e.g., *In re Saxon Sec. Litig.*, 644 F. Supp. 465, 471 (S.D.N.Y. 1985) (under limited circumstances, owner of securities expressly may assign rule 10b-5 cause of action to subsequent purchaser, but assignment of rule 10b-5 cause of action does not occur automatically); *Rose v. Arkansas Valley Envtl. & Util. Auth.*, 562 F. Supp. 1180, 1189 (W.D. Mo. 1983) (some act by seller of security in addition to sale of security must occur for seller effectively to assign rule 10b-5 cause of action to subsequent purchaser); *Independent Investor Protective League v. Saunders*, 64 F.R.D. 564, 572 (E.D. Pa. 1974) (recognizing support for express assignability of rule 10b-5 causes of actions, but finding no support for automatic assignment of rule 10b-5 causes of action).

10. 707 F.2d 721 (2d Cir.), *modification denied*, 711 F.2d 1207 (3d Cir.), *cert. denied*, 464 U.S. 893 (1983).

11. *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 722 (3d Cir. 1983).

12. *Id.*

13. See *id.* (discussing action against B & O by original debentureholders that preceded plaintiffs' action in *Lowry*); see also *Pittsburgh Terminal Corp. v. Baltimore & O. R.R.*, 680 F.2d 933 (3d Cir.) (action by original convertible debentureholders against B & O, alleging violation of rule 10b-5), *cert. denied*, 103 S. Ct. 476 (1982).

14. See *Lowry*, 707 F.2d at 722 (noting that, while owning rail and nonrail assets, B & O issued both common stock and convertible debentures); see also *Pittsburgh Terminal Corp. v. Baltimore & O. R.R. Co.*, 680 F.2d 933, 936 (3d Cir.) (same), *cert. denied*, 103 S.Ct. 476 (1982).

15. See *Lowry*, 707 F.2d at 722 (before creation of subsidiary corporation, Mid-Allegheny, B & O debentureholders could convert debentures into common stock that represented both B & O's rail and nonrail assets).

16. *Id.*; see also *Pittsburgh Terminal Corp. v. Baltimore & O. R.R. Co.*, 680 F.2d 933, 936 (3d Cir. 1982) (discussing B & O's transfer of B & O nonrail assets to Mid-Allegheny Corporation). Because B & O owned rail assets, the Interstate Commerce Com-

dividend, distributing all of the Mid-Allegheny stock to B & O common stockholders.¹⁷ In distributing the Mid-Allegheny stock, B & O failed to give notice of the distribution to B & O convertible debentureholders.¹⁸ Because B & O failed to give notice of the stock dividend to the debentureholders, the convertible debentureholders were unable to convert their debentures to common stock before B & O distributed the Mid-Allegheny stock dividend.¹⁹ Thus, although at the time the previous holders had purchased their debentures, the debentures were convertible into common stock representing B & O's rail and nonrail assets, after December 13 the debentures were convertible into common stock representing only B & O's rail assets.²⁰ Accordingly, prior to the *Lowry* action, the previous debentureholders brought an action under section 10(b) of the 1934 Act against B & O in the United States District Court for the Western District of Pennsylvania.²¹ In their action against B & O, the previous debentureholders alleged that B & O's distribution of Mid-Allegheny common stock to B & O common stockholders constituted a fraud on the previous debentureholders because B & O had failed to notify the debentureholders of the distribution to common stockholders.²² On appeal, the Third Circuit Court of Appeals determined that the previous debentureholders had a private right of action against B & O under section 10(b) and rule 10b-

mission regulated all of B & O's assets. *Pittsburgh Terminal*, 680 F.2d at 936. Therefore, to avoid Interstate Commerce Commission regulations that prohibited a railroad corporation from pursuing nonrail ventures, B & O had created a wholly owned subsidiary, Mid-Allegheny Corporation. *Id.* By transferring B & O's nonrail assets to Mid-Allegheny, B & O could allow Mid-Allegheny, a nonrail corporation, to develop B & O's nonrail assets without having to comply with ICC regulations. *Id.*

17. *Lowry*, 707 F.2d at 722. By distributing the Mid-Allegheny stock as a dividend to B & O's common stockholders, B & O avoided registering Mid-Allegheny's stock dividend with the SEC. See *Pittsburgh Terminal Corp. v. Baltimore & O.R.R.*, 680 F.2d 933, 936 (3d Cir. 1982) (discussing B & O's reluctance to register Mid-Allegheny stock with SEC).

18. *Lowry*, 707 F.2d at 722. The Restructuring Committee for B & O determined that, to avoid registering Mid-Allegheny Corporation with the SEC, B & O would not give notice to B & O convertible debentureholders of the Mid-Allegheny stock distribution. See *Pittsburgh Terminal Corp. v. Baltimore & O. R.R.*, 680 F.2d 933, 936 (3d Cir. 1982) (discussing B & O's reluctance to register Mid-Allegheny with SEC). The Restructuring Committee reasoned that, if convertible debentureholders knew of the impending stock dividend to B & O common stockholders, the convertible debentureholders would exercise their right to convert to common stock. *Id.* If the number of B & O common stockholders rose sharply just prior to the Mid-Allegheny distribution, the Committee concluded, the SEC would require that B & O register Mid-Allegheny's securities. *Id.*

19. *Lowry*, 707 F.2d at 722.

20. *Id.*

21. See *id.* (discussing action of original debentureholders against B & O for violations of section 10(b) and rule 10b-5); see also *Pittsburgh Terminal Corp. v. Baltimore & O. R.R.*, 680 F.2d 933, 935 (3d Cir. 1982) (discussing plaintiffs' allegation that B & O's stock dividend without notice to convertible debentureholders violated federal securities laws).

22. See *Lowry*, 707 F.2d at 722 (discussing plaintiffs' claims in *Pittsburgh Terminal*); see also *Pittsburgh Terminal Corp. v. Baltimore & O.R.R.*, 680 F.2d 933, 939 (3d Cir.) (discussing original B & O convertible debentureholders' action against B & O), *cert. denied*, 103 S. Ct. 476 (1982).

5.²³ The plaintiff class in *Lowry* consisted of debentureholders who after

23. See *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 722 (3d Cir. 1983) (discussing holding in *Pittsburgh Terminal*); see also *Pittsburgh Terminal Corp. v. Baltimore & O. R.R.*, 680 F.2d 933, 943 (3d Cir.) (by failing to give notice of impending stock dividend, B & O defrauded convertible debentureholders), *cert. denied*, 103 S. Ct. 476 (1982).

In *Pittsburgh Terminal* the plaintiffs, Pittsburgh Terminal Corporation and Monroe Guttman, held B & O debentures, which were convertible at any time before maturity into ten shares of B & O common stock for each \$1000 of face value of the debentures. *Pittsburgh Terminal*, 680 F.2d at 935. In the indenture applying to the plaintiffs' debentures, B & O agreed not to declare or pay any stock dividend on B & O common stock without giving general notice of the record date of the distribution. *Id.* at 936-37. Additionally, B & O's listing agreement with the New York Stock Exchange (NYSE) stipulated that B & O promptly would publish to the holders of B & O securities any dividend action that B & O might take, allowing security holders a "proper period" in which to exercise their rights in the securities. *Id.* at 937. Last, the Rules of the NYSE also governed the activities of B & O. *Id.* The Rules provide that corporations listed with the NYSE must release to the public any information that reasonably might affect materially the market for the corporation's securities. *Id.* In *Pittsburgh Terminal* the plaintiff, Monroe Guttman, a B & O convertible debentureholder, requested that B & O promptly notify convertible debentureholders of a dividend declaration so that the convertible debentureholders would have sufficient time to exercise their conversion option and receive the stock dividend as common stockholders. *Id.* In November 1977, B & O replied to Guttman that B & O promptly would disseminate to the general public any information concerning dividend action on B & O stock. *Id.*

B & O declared a dividend, payable in stock of B & O's subsidiary, Mid-Allegheny Corporation, to B & O common stockholders on December 13, 1977. *Id.* at 938; see also *supra* notes 15-17 and accompanying text (discussing B & O's transfer of nonrail assets and subsequent stock dividend declaration). B & O, however, failed to notify the convertible debentureholders that B & O was declaring a dividend. *Pittsburgh Terminal*, 680 F.2d at 938. The plaintiffs maintained an action against B & O in the United States District Court for the Western District of Pennsylvania, alleging that B & O's stock dividend of December 13, 1977, violated section 10(b) of the 1934 Act and rule 10b-5 by depriving debentureholders of the opportunity to convert their debentures into shares of common stock before the record date and to participate in the stock dividend of December 13. *Id.* at 935. The district court recognized that the plaintiffs had standing to sue B & O but rejected each of the plaintiffs' claims, reasoning that B & O had a legitimate business purpose in declaring the stock dividend without giving notice to convertible debentureholders. *Id.* at 942.

On appeal, the Third Circuit first determined that B & O had a duty to notify B & O convertible debentureholders of the impending stock dividend to B & O common shareholders. *Id.* at 940-42. In finding that B & O had a duty to notify, the *Pittsburgh Terminal* court first reasoned that the NYSE listing agreement affirmatively required B & O to give B & O security holders an opportunity to exercise their rights in their securities if B & O declared and paid a dividend. *Id.* at 941. Second, the *Pittsburgh Terminal* court found that B & O had a similar affirmative duty under SEC Rule 10b-17, which states that failure to give notice of a dividend or other distribution in cash or in kind shall constitute a "manipulative or deceptive device." *Id.*

After finding that B & O had a duty to notify the plaintiffs of the stock dividend of December 13, the *Pittsburgh Terminal* court determined that B & O knowingly and intentionally timed the distribution of Mid-Allegheny shares to avoid giving notice to the convertible debentureholders. *Id.* at 942. Therefore, the Third Circuit concluded that the plaintiffs satisfied the scienter requirement of section 10(b) and rule 10b-5. *Id.* Accordingly, the Third Circuit reversed the decision of the district court in *Pittsburgh Terminal*, holding that by failing to notify the plaintiffs of the stock dividend of December 13, B & O violated section 10(b) and rule 10b-5. *Id.* at 943.

December 13 had purchased convertible debentures from the previous debentureholders.²⁴ The plaintiff class in *Lowry* claimed that the previous debentureholders automatically had assigned their section 10(b) and rule 10b-5 causes of action to the subsequent purchasers of the debentures.²⁵ Thus, the plaintiff class in *Lowry* asserted against B & O the rule 10b-5 claims of the original B & O debentureholders.²⁶

Six of the eight judges sitting en banc in *Lowry* agreed with the plaintiff class that a security holder who possessed a rule 10b-5 cause of action could assign the cause of action to a subsequent purchaser of the security.²⁷ The six judges, however, disagreed over whether the possessor of a rule 10b-5 cause of action automatically assigns his cause of action to a subsequent purchaser of the security or whether the possessor expressly must assign the cause of action to a subsequent holder of the security.²⁸ Two judges in a concurring opinion determined that courts should permit only security holders that have suffered fraud themselves or that are express assignees of defrauded holders to maintain rule 10b-5 actions.²⁹ The concurring judges noted that the securities laws have a remedial purpose and that, by enacting the securities laws, Congress intended to provide a remedy to individuals injured by fraud.³⁰ Thus, the concurring judges reasoned that a rule permitting only defrauded security holders and

24. *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 722 (3d Cir. 1983).

25. *Id.*

26. *Id.*

27. *Id.* at 729-32, 734-47.

28. *Id.* Five of the eight judges who participated in the *Lowry* decision joined the decision to dismiss the plaintiff class' federal causes of action against B & O. *Id.* at 723. Three of the five judges in favor of the dismissal, however, acknowledged that if the December 13 debentureholders expressly had assigned their rule 10b-5 causes of action to the subsequent purchasers of the debentures who constituted the plaintiff class, the plaintiff class in *Lowry* would have had a valid claim against B & O under section 10(b) and rule 10b-5. *See id.* at 729 (Garth, J., concurring) (absent express assignment of federal securities law causes of action to subsequent purchasers, subsequent purchasers may not assert federal claims of previous owners of securities); *infra* notes 29-35 and accompanying text (discussing reasoning behind determination of concurring judges that security holders expressly may assign rule 10b-5 causes of action to subsequent purchasers). The remaining three judges who participated in the *Lowry* decision dissented from the Third Circuit's dismissal of the plaintiffs' federal claims, determining that rule 10b-5 causes of action travel automatically to subsequent purchasers of securities. *See Lowry*, 707 F.2d at 739 (Gibbons, J., dissenting) (decisions of federal courts holding that section 10(b) and rule 10b-5 claims freely are assignable are well supported by federal case law); *infra* notes 36-49 and accompanying text (discussing reasoning behind determination of dissenting judges in *Lowry* that rule 10b-5 causes of action travel automatically to subsequent purchasers of securities).

29. *Lowry*, 707 F.2d at 729 (Garth, J., concurring). In *Lowry*, Judge Sloviter joined Judge Garth's concurring opinion. *Id.* at 723.

30. *See id.* (Garth, J., concurring) (remedial purposes of securities laws demand that compensation for securities fraud must inure to individuals injured by fraud, not to corporate bounty hunters); *see also* S. REP. NO. 792, 73d Cong., 2d Sess. 3 (1934) (purpose of 1934 Act was to provide remedy for investors that suffered injury from unfair methods of speculation in securities transactions prior to and during stock market crash).

their express assignees to bring a rule 10b-5 action supports the congressional purpose behind rule 10b-5 more effectively than a rule permitting automatic assignment.³¹ Accordingly, the concurring judges examined whether B & O's stock distribution actually injured the plaintiff class in *Lowry*.³² The concurrence noted that the price which the plaintiffs in *Lowry* paid for the debentures reflected the decrease in the debentures' value that resulted from B & O's transfer of nonrail assets to Mid-Allegheny.³³ The concurring judges reasoned that, because the plaintiff class had knowledge of the Mid-Allegheny stock distribution and because the price of the debentures reflected the decrease in the value of the debentures, the class suffered no loss or injury as a result of purchasing the B & O debentures.³⁴ The concurrence concluded that, to allow subsequent purchasers that suffered no loss from B & O's fraudulent conduct to recover under rule 10b-5 in the absence of an expression of the seller's intent to assign his cause of action to the purchasers would defeat the remedial purpose underlying the securities laws.³⁵

Although the concurring judges in *Lowry* were in favor of recognizing only express assignments of rule 10b-5 causes of action, three judges dissenting from the majority opinion in *Lowry* asserted that owners of securities automatically assign their section 10(b) actions to subsequent purchasers of the securities.³⁶ The dissent determined that rule 10b-5 claims

31. *Lowry*, 707 F.2d at 729.

32. *See id.* (whether plaintiff class in *Lowry* suffered injury depends upon whether price that plaintiff class paid for B & O convertible debentures reflected fraud on previous debentureholders).

33. *See id.* (recognizing that post-December 13 prices reflected dilution in value of B & O convertible debentures that B & O's corporate restructure caused). According to the concurrence in *Lowry*, after B & O declared the distribution of Mid-Allegheny stock to B & O common stockholders on December 13, the convertible debentures, once convertible into common stock representing both rail and nonrail assets of B & O, were convertible into stock representing only rail assets of B & O. *Id.* Because the B & O convertible debentures represented an option to acquire less valuable common stock after December 13, B & O's transfer of its nonrail assets to Mid-Allegheny diluted the value of the B & O convertible debentures. *Id.* In addition, the concurrence noted that, because the subsequent purchasers of the debentures knew of the stock dividend and transfer of nonrail assets, they must have paid a lower price than the original debentureholders paid for the debentures. *Id.*

34. *Id.*

35. *Id.* One of the three concurring judges in *Lowry* agreed with the concurring opinion of the other two judges and, in a separate concurrence, also asserted that federal law does not allow the automatic assignment of federal securities law causes of action. *Id.* at 732 (Adams, J., concurring).

36. *See id.* at 734-48 (Gibbons, J., and Seitz, J., dissenting) (determining that federal securities law claims automatically are assigned to subsequent purchasers of securities). In *Lowry* Chief Judge Seitz wrote a concurring and dissenting opinion, which Judge Becker joined. *Id.* at 748. The dissenting judges in *Lowry* first determined that previous federal cases had established that actions for damages under federal securities laws are freely assignable. *See id.* at 739 (Gibbons, J., dissenting) (decisions establishing that federal securities law claims are assignable achieve purpose behind federal securities laws by

must be freely transferable to achieve the rule's underlying policy of protecting security holders from manipulative or deceptive acts or practices of sellers of securities.³⁷ The dissent reasoned that because not all security holders can afford the expense and delay of a rule 10b-5 action, security holders should be able to sell their securities and their causes of action in the market.³⁸ Furthermore, the dissenting judges suggested that, assuming that federal common law determines whether an assignment has occurred,³⁹ the federal common law of assignability of securities fraud claims must

protecting investors from manipulative or deceptive practices); *see also* *Western Auto Supply Co. v. Gamble-Skogmo, Inc.*, 348 F.2d 736, 739-41 (8th Cir. 1965) (surviving corporation after merger assigned right of action under § 16 of 1934 Act to purchaser corporation), *cert. denied*, 382 U.S. 987 (1966); *International Ladies Garment Workers Union v. Shields & Co.*, 209 F. Supp. 145, 149-50 (S.D.N.Y. 1962) (remedial damages actions under § 10(b) of 1934 Act survive holder's death and are assignable); *Mills v. Sarjem Corp.*, 133 F. Supp. 753, 761 (D.N.J. 1955) (because common law tests of assignability and survivability are same, remedial damages actions that survive death are assignable).

37. *Lowry*, 707 F.2d at 739 (Gibbons, J., dissenting).

38. *Id.* at 739-40 (Gibbons, J., dissenting).

39. *Id.* at 740 (Gibbons, J., dissenting). In determining which law governs the assignment of federal securities law causes of action, the dissenting judges in *Lowry* queried, first, whether state or federal law governs the assignment of federal securities law causes of action. *Id.* Although the dissent cited ample support for the applicability of state law to questions concerning the transferability of property, the dissent assumed for the sake of argument that federal common law decides the issue of assignment of federal securities law claims. *Id.* Second, the dissenting judges explored whether the federal common law provides a uniform rule of assignment of federal securities law claims or whether courts should determine the federal common law according to the law of the state in which the sale of the securities occurred. *Id.* at 740-42. The dissent determined that applying the law of the state to the issue of assignment does not frustrate the federal government's objective of protecting the securities market from manipulative and deceitful practices. *Id.* The dissent explained that, because state law will determine only the assignment issue, the victim of fraud or his assignee still will be able to obtain a federal remedy for the fraud. *Id.* at 741. Additionally, the dissent reasoned that a federal rule on assignment of federal securities law claims would disrupt commercial relationships founded in state law because many states have adopted the Uniform Commercial Code (UCC), which provides for the automatic transfer from seller to buyer of all rights that the seller possesses. *Id.* at 741-42; *see also* N.Y. [GENERAL OBLIGATIONS] LAW § 13-107 (McKinney 1978) (transfer of bond vests in transferee all claims or demands of transferor for damages or rescission); N.Y. [UNIFORM COMMERCIAL CODE] LAW § 8-301 (McKinney 1964) (upon delivery of security, purchaser acquires all rights in security that transferor had or had authority to convey); *but see* *Licht v. Donaldson, Lufkin & Jenrette Sec. Corp.*, No. 24560/82, slip op. (N.Y. Sup. Ct. Sept. 1983) (holding that seller of security does not automatically transfer his state law claims when he sells a security). Finally, assuming arguendo the need for a uniform federal rule, the dissenting judges questioned whether state law, nevertheless, should define the national consensus on the issue of assignment of federal securities law claims. *Lowry*, 707 F.2d at 742-43. Because adopting the rule of the UCC would provide uniformity, the dissent concluded that the New York and UCC rules sufficiently represent the consensus of the commercial world on the assignment issue. *Id.* By this process of reasoning, the dissent concluded that state law should govern the assignment of federal securities law claims, but that, even if the federal common law governs the assignment issue, state law should define the content of the federal common law. *Id.*

reflect the law of the state in which the buyer purchased the security.⁴⁰ Because the convertible debenture sale in *Lowry* occurred in New York, the dissent determined that a New York state law that provides for the automatic assignment of accrued causes of action to subsequent purchasers in bond and debenture transactions governed the debenture sale in *Lowry*.⁴¹ The dissent noted, therefore, that the original holders of the B & O debentures automatically assigned their rule 10b-5 rights to the subsequent purchasers of the debentures.⁴² The dissenting judges in *Lowry* concluded that the Third Circuit should remand the case to the lower court for further proceedings consistent with New York law.⁴³

In addition to asserting that the Third Circuit should recognize a rule of automatic assignment, two of the three dissenting judges recognized that security holders often will sell their securities before investors discover fraud and the ground for a rule 10b-5 action.⁴⁴ Thus, the two judges determined that, by recognizing a rule of automatic assignment of securities fraud claims, courts will give fraud claims to the subsequent holders of the securities, who are the parties most likely to discover the fraud claims.⁴⁵ The two dissenting judges reasoned that in giving the claim to the investor who discovers the fraud, courts most effectively will realize the goal behind section 10(b) and rule 10b-5, the deterrence of manipulative and deceptive practices in the exchange of securities.⁴⁶ Additionally, the two dissenting judges recognized that most securities transactions occur in a market in which buyers and sellers never meet.⁴⁷ The two dissenting judges noted that, in a market in which buyers and sellers of securities never meet, the parties never have the opportunity to negotiate an express assignment.⁴⁸ Therefore, according to the two dissenting judges, a rule requiring the seller of a security expressly to assign his rule 10b-5 claims seriously would curtail the effectiveness of rule 10b-5 claims and fail to achieve the maximum fraud deterrence that Congress intended section 10(b) and rule 10b-5 to have.⁴⁹

40. *Lowry*, 707 F.2d at 742-43; see *supra* note 39 and accompanying text (describing reasoning behind *Lowry* dissent's assertion that state law should define federal common law on issue of assignability of federal securities law claims).

41. *Lowry*, 707 F.2d at 742-43 (Gibbons, J., dissenting); see *supra* note 39 and accompanying text (discussing reasoning behind dissent's conclusion in *Lowry* that state law governed assignment of 10b-5 action); see also N.Y. [GENERAL OBLIGATIONS] LAW § 13-107 (McKinney 1978) (transfer of bond vests in transferee all claims or demands of transferor for damages or rescission).

42. *Lowry*, 707 F.2d at 742 (Gibbons, J., dissenting).

43. *Id.* at 743-44.

44. *Id.* at 746 (Seitz, J., concurring and dissenting). In *Lowry* Judge Becker joined Chief Judge Seitz's opinion. *Id.*

45. *Id.*

46. *Id.*

47. *Id.*

48. *Id.*

49. *Id.*

Other courts addressing the issue of the assignability of federal securities law causes of action have been less divided than the *Lowry* court on the questions of express and automatic assignment.⁵⁰ For example, in *In re Nucorp Energy Securities Litigation*⁵¹ the United States Court of Appeals for the Ninth Circuit considered whether Nucorp debentureholders automatically assigned their actions for breach of trust under the Trust Indenture Act (TIA) to the plaintiffs, who were subsequent purchasers of Nucorp debentures.⁵² In *Nucorp Continental Illinois Bank and Trust Company of Chicago (Continental)* acted as indenture trustee for holders of convertible debentures of Nucorp Energy, Inc. (Nucorp), who purchased debentures on and after October 1, 1981.⁵³ On January 20, 1982, Nucorp publicly announced that Nucorp was experiencing financial difficulties.⁵⁴ In an action that preceded *Nucorp*, Nucorp debentureholders who held the debentures between October 1, 1981, and January 20, 1982, charged Continental with breach of trust in violation of the TIA for knowing or having reason to know that Nucorp's disclosure documents supporting Nucorp's January 20 announcement were materially misleading.⁵⁵ The plaintiffs in *Nucorp* were Nucorp debentureholders who after January 20 had purchased Nucorp debentures from the October-January debenture-

50. See *infra* notes 51-84 and accompanying text (discussing courts' similar reasoning in *In re Nucorp Securities Litigation* and *Soderberg v. Gens*); see also *In re Nucorp Sec. Litig.*, 772 F.2d 1486, 1493 (9th Cir. 1985) (claim under federal Trust Indenture Act did not travel automatically with security); *Soderberg v. Gens*, 652 F. Supp. 560, 566 (N.D. Ill. 1987) (owner of security did not automatically assign cause of action under § 10(b) of 1934 Act to subsequent purchaser of security).

51. 772 F.2d 1486 (9th Cir. 1985).

52. *In re Nucorp Energy Sec. Litig.*, 772 F.2d 1486, 1488 (9th Cir. 1985). The Trust Indenture Act of 1939 (TIA) is a companion statute to the Securities Act of 1933. Trust Indenture Act of 1939, 15 U.S.C. §§ 77aaa-77bbb (1982); see L. Loss, *supra* note 1, at 94 (TIA operates in conjunction with registration requirements of Securities Act of 1933). The TIA requires that companies issuing debt securities such as bonds or debentures prepare and file with the SEC a document known as an "indenture," defining the rights of the holders of the debt securities that the company issues. Trust Indenture Act of 1939, 15 U.S.C. §§ 302, 304(a)(9), 305(a). The TIA also requires trustees under indentures to protect and enforce the rights of the debt security holders. *Id.* § 315; see L. Loss, *supra* note 1, at 94 (purpose of TIA is to provide for trustees who will protect holders of bonds and debentures that corporation issues under TIA). Under the TIA, holders of bonds and debentures may maintain actions against indenture trustees for breach of trust. Trust Indenture Act of 1939, 15 U.S.C. § 77ooo(d) (1982); see *Caplin v. Marine Midland Grace Trust Co.*, 406 U.S. 416, 434 (1971) (trustee under Chapter X of Bankruptcy Act may not assert debentureholder's claim under TIA for breach of trust); *Aladdin Hotel Co. v. Bloom*, 200 F.2d 627, 633 (8th Cir. 1953) (terms of indenture will determine rights of bondholders); *Ray v. Marine Midland Grace Trust Co.*, 35 N.Y.2d 147, 156, 359 N.Y.S.2d 28, 33, 316 N.E.2d 320, 323 (1974) (holding that class action on behalf of debentureholders claiming breach of trust under TIA was proper).

53. *Nucorp*, 772 F.2d at 1488.

54. *Id.*

55. See *id.* at 1488 (discussing action by original debentureholders against Continental that preceded *Nucorp*).

holders.⁵⁶ The *Nucorp* plaintiffs brought a separate class action for breach of trust against Continental, claiming that the October-January debentureholders automatically assigned their TIA causes of action to the *Nucorp* plaintiffs when the *Nucorp* plaintiffs purchased the *Nucorp* debentures.⁵⁷ The United States District Court for the Southern District of California dismissed the plaintiffs' federal claims for failure to state a claim for which a court could grant relief.⁵⁸ The plaintiffs appealed the district court's decision to the United States Court of Appeals for the Ninth Circuit.⁵⁹

In determining that the October-January debentureholders had not automatically assigned their TIA claims to the plaintiffs in *Nucorp*, the Ninth Circuit noted that federal law governs issues arising under the TIA, which is a federal statute.⁶⁰ The *Nucorp* court recognized that purchasers of indentured securities have a cause of action under the TIA only if the purchasers relied on the misleading statements and omissions of the issuers of the indentured securities and suffered actual damages.⁶¹ Therefore, the *Nucorp* court reasoned that a cause of action under the TIA is personal to injured purchasers of securities and does not automatically travel with the securities to a subsequent purchaser who did not rely on the misrepresentations of the issuers.⁶² The *Nucorp* court noted that to recognize the

56. *Id.* at 1488.

57. *Id.* In *In Re Nucorp Securities Litigation* the plaintiff, the Phelps Committee, represented convertible debentureholders who bought *Nucorp* debentures from security holders who had held the debentures before January 20, 1982. *Id.* The security holders from whom the *Nucorp* plaintiffs bought their debentures, therefore, had been members of the plaintiff class in the original action against Continental for breach of the TIA. *Id.*

58. *Id.* In dismissing the plaintiffs' federal claims on the merits, the district court in *Nucorp* agreed with the defendant, Continental, that because the plaintiffs had not demonstrated that Continental had violated the TIA and because the plaintiffs had suffered no injury from the materially misleading indenture documents, the plaintiffs had no cause of action against Continental for breach of the trust agreement. *Id.* The district court in *Nucorp* also dismissed the plaintiffs' state claims, concluding that the plaintiffs had failed to show that Continental had violated any state laws. *Id.*

59. *Id.*

60. *Id.* at 1489; see Trust Indenture Act of 1939, 15 U.S.C. §§ 77aaa-77bbb (1982); *supra* note 52 and accompanying text (discussing TIA). In determining that federal law governed the plaintiffs' claims in *Nucorp*, the Ninth Circuit noted that the TIA is part of the Securities Act of 1933. *In re Nucorp Sec. Litig.*, 772 F.2d, 1486, 1489 (9th Cir. 1985). The *Nucorp* court reasoned that, as a securities statute, the TIA shares the policy behind the Securities Act of 1933 of protecting investors. *Id.* Because the TIA is a federal statute and invokes considerations of federal policy and because other federal courts have relied on federal law when determining whether federal securities law claims are assignable, the Ninth Circuit concluded that federal law governed the issue of the assignability of a cause of action under the TIA. *Id.*

61. *In re Nucorp Sec. Litig.*, 772 F.2d, 1486, 1489-90 (9th Cir. 1985).

62. *Id.* at 1490; see also *Independent Investor Protective League v. Saunders*, 64 F.R.D. 564, 572 (E.D. Pa. 1974) (rights of individuals that have suffered injury do not attach forever to security). Unlike the Third Circuit in *Lowry*, the *Nucorp* court did not distinguish between express and automatic assignment of rights of action. *Nucorp*, 772 F.2d

plaintiffs' cause of action would take the action from the defrauded parties and "gratuitously" transfer the cause of action to parties who were not victims of the issuer's fraud.⁶³ Therefore, the Ninth Circuit affirmed the decision of the district court and held that sellers of indentured securities do not automatically assign their causes of action to subsequent purchasers.⁶⁴

In a recent case, the United States District Court for the Northern District of Illinois followed the reasoning of the Ninth Circuit in *Nucorp*.⁶⁵ In *Soderberg v. Gens*⁶⁶ the United States District Court for the Northern District of Illinois considered whether the right to sue under section 10(b) of the 1934 Act and rule 10b-5 of the SEC Rules for rescission of a security transaction is automatically assignable to a subsequent holder of a security.⁶⁷ In *Soderberg* the plaintiff was the widow of John Soderberg, who had been the controlling shareholder of Copco Corporation (Copco), which owned all the stock of the Constitutional Casualty Company (Constitutional).⁶⁸ Upon John Soderberg's death, his shares in Copco passed to a trust, of which Soderberg's widow, the plaintiff in *Soderberg*, and his daughters were beneficiaries and cotrustees.⁶⁹ After Soderberg's death, Constitutional encountered financial difficulties and hired the defendant,

at 1490; see *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 729 (3d Cir. 1983) (Garth, J., concurring) (recognizing express assignment rule). *But see Lowry*, 707 F.2d at 739 (Gibbons, J., dissenting) (acknowledging rule of automatic assignment of section 10(b) causes of action).

63. *Nucorp*, 772 F.2d at 1490.

64. *Id.* In addition to considering the plaintiffs' federal cause of action, the United States Court of Appeals for the Ninth Circuit in *In re Nucorp Securities Litigation* considered whether the October-January debentureholders' state law claims against Continental for breach of fiduciary duty, willful misconduct, fraud and deceit, and negligence automatically transferred to the plaintiffs when the plaintiffs purchased the Nucorp debentures. *Id.* at 1492-93. The Ninth Circuit in *Nucorp* concluded that New York courts have determined that state law claims do not travel automatically with securities when an individual purchases a security. *Id.* at 1493. *But see* N.Y. [GENERAL OBLIGATIONS] LAW § 13-107 (McKinney 1978) (transfer of bond vests in transferee all claims or demands of transferor for damages or rescission); N.Y. [UNIFORM COMMERCIAL CODE] LAW § 8-301 (McKinney 1964) (with respect to investment securities generally, upon delivery of security, purchaser acquires all rights in security that transferor had or had authority to convey). Therefore, the Ninth Circuit held that, under New York law, sellers of securities do not automatically assign their federal causes of action to subsequent purchasers of the securities. *Nucorp*, 772 F.2d at 1493.

65. *Soderberg v. Gens*, 652 F. Supp. 560 (N.D. Ill. 1987); see *infra* notes 79-84 and accompanying text (discussing reasoning and holding of court in *Soderberg*); see also *Nucorp*, 772 F.2d at 1493 (under New York law, sellers of securities do not automatically assign federal causes of action to purchasers of their securities); *supra* notes 61-65 and accompanying text (discussing reasoning and holding of court in *Nucorp*).

66. 652 F. Supp. 560 (N.D. Ill. 1987).

67. *Soderberg v. Gens*, 652 F. Supp. 560, 563 (N.D. Ill. 1987).

68. *Id.* at 561-62.

69. *Id.*

Gens, as a management consultant.⁷⁰ Gens' investment advice to Constitutional consisted of a complex scheme for acquiring six new assets, including the stock of two shell companies that Constitutional set up.⁷¹ Although the Illinois Department of Insurance declared that Constitutional's stock purchases were inadmissible and ordered Constitutional to raise additional capital to cover the investment that Gens had suggested, Constitutional continued to receive cash dividend checks from the two shell companies.⁷² Later, when the Soderbergs sold Copco and Constitutional, the purchaser requested that the Soderbergs and the minority Copco shareholders buy back the six assets from Copco.⁷³ The purchaser requested that the shareholders buy back the assets because the purchaser did not want to purchase the six new assets.⁷⁴ At the same time that Constitutional repurchased the six assets, Constitutional assigned all claims, causes of action, and rights arising out of the purchase, acquisition, or retention of the six assets, including the stock in the shell companies, to the plaintiff, the former controlling shareholder in Constitutional.⁷⁵ Pursuant to this assignment, the plaintiff received dividend payments from the two shell companies for three or four months after the sale of Copco and Constitutional.⁷⁶ Then, on September 26, 1984, the plaintiff announced that she was rescinding the "purchase" of the two shell companies and refused to accept any further dividend payments.⁷⁷ Alleging fraud in the sale of the shell company stock under section 10(b) of the 1934 Act, the plaintiff in *Soderberg* filed an action against Gens to rescind Constitutional's purchase of stock from the shell companies.⁷⁸

In determining that Constitutional had not assigned to the plaintiff the right to rescind the purchase of the stock of the shell companies, the *Soderberg* court first recognized that a federal cause of action does not attach automatically to a security and pass to a subsequent purchaser of

70. *Id.* at 562. In *Soderberg* a budding romantic involvement between the Soderbergs' daughter, Janet, executive vice president of both Copco and Constitutional, and Timothy Gens was instrumental in Constitutional's hiring of Gens as a management consultant. *Id.*

71. *Id.* In *Soderberg v. Gens* Constitutional ceased showing a profit in early 1983. *Id.* The defendant, Gens, advised Constitutional to acquire six new assets. *Id.* Gens' plan included the purchase of the stock of Constitutional shell corporations, Acquitech Corporation and Madison Professional Group. *Id.*

72. *Id.*

73. *Id.* In *Soderberg* Constitutional received all proceeds from the sale of Copco, including the plaintiff's share of the proceeds, so that Constitutional could repurchase the six Constitutional assets that the purchaser of Copco and Constitutional did not want. *Id.*

74. *Id.*

75. *Id.*

76. *Id.*

77. *Id.*

78. *Id.* In *Soderberg*, in addition to filing suit against Gens, the plaintiff also filed suit against Acquitech and Madison, the shell companies that, under Gens' direction, had sold their stock to Constitutional. *Id.* In addition to alleging fraud under the 1934 Act, the plaintiff claimed a right of rescission under section 12(2) of the 1933 Act, section 206 of the Investment Advisers Act of 1940, two Illinois statutes, and common law fraud. *Id.*

the security.⁷⁹ Next the *Soderberg* court acknowledged that the plaintiff might have had a cause of action if Constitutional expressly had assigned its right of rescission to the plaintiff, but rejected the plaintiff's argument that Constitutional had done so.⁸⁰ In rejecting the plaintiff's argument, the *Soderberg* court noted that although some courts have recognized that claims for damages are expressly assignable, according to the common law of assignment, claims for rescission usually are not assignable.⁸¹ Furthermore, the court noted that, even if the court recognized a rule of express assignment, Constitutional's attempt to assign the right to rescind was ineffective because Constitutional had relinquished its right to rescind.⁸² The *Soderberg* court explained that, by receiving and cashing dividends that the shell companies had distributed, Continental had behaved in a manner that was inconsistent with an intention to retain the right to rescind.⁸³ Accordingly, in addition to holding that an owner of a security does not automatically assign his cause of action to a subsequent purchaser, the court concluded that Constitutional's attempt expressly to assign the right to rescind to the plaintiff was ineffective.⁸⁴

Consistently with the *Nucorp* and *Soderberg* courts, the majority of courts in recent years has recognized that security holders do not automatically assign their federal securities law causes of action to subsequent purchasers of their securities.⁸⁵ Although early opinions indicated that federal securities fraud claims might be automatically assignable,⁸⁶ recent federal court decisions suggest a trend toward recognizing a theory of express assignment and rejecting the concept of automatic assignment.⁸⁷

79. *Id.* at 563-64.

80. *Id.* at 564.

81. *Id.* at 565.

82. *Id.*

83. *Id.* at 566.

84. *Id.* The *Soderberg* court noted that the court's decision not to recognize automatic assignability was limited to actions for rescission. *Id.* Therefore, the *Soderberg* court acknowledged that the court did not decide whether all securities fraud actions are assignable. *Id.*

85. *See, e.g.,* Ciarlante v. CSX Corp., 629 F. Supp. 534, 537 (W.D. Pa. 1986) (federal law does not provide for automatic assignment of federal securities laws claims); *In re Saxon Sec. Litig.*, 644 F. Supp. 465, 471 (S.D.N.Y. 1985) (assignment of rule 10b-5 right of action to subsequent purchaser does not occur automatically); *Rose v. Arkansas Valley Envtl. & Util. Auth.*, 562 F. Supp. 1180, 1188 (W.D. Mo. 1983) (because only defrauded purchasers and sellers may bring actions under rule 10b-5, purchaser of security who does not allege fraud does not acquire rule 10b-5 right of action by automatic assignment); *Independent Investor Protective League v. Saunders*, 64 F.R.D. 564, 572 (E.D. Pa. 1974) (right of action that belongs to victim of fraud does not attach automatically to security).

86. *See, e.g.,* *International Ladies' Garment Workers' Union v. Shields & Co.*, 209 F. Supp. 145, 149 (S.D.N.Y. 1962) (rule 10b-5 actions for remedial damages are assignable); *Mills v. Sarjem Corp.*, 133 F. Supp. 753, 761-62 (D.N.J. 1955) (because remedial damages actions survive death of holder, rule 10b-5 remedial damages action is assignable); *infra* notes 100-05 and accompanying text (discussing reasoning and holding of *Mills v. Sarjem Corp.* court).

87. *See, e.g.,* *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 729 (3d Cir.) (Garth, J.,

A few courts, however, have not joined the recent trend of the federal courts, but instead have recognized a theory that a seller automatically assigns his securities fraud action to a subsequent buyer.⁸⁸ The decisions of courts that recognize a theory of automatic assignment, however, are distinguishable in several respects from the majority position rejecting the theory of automatic assignment.⁸⁹ For example, in *Phelan v. Middle States Oil Corp.*⁹⁰ the United States Court of Appeals for the Second Circuit considered whether executors of a deceased bondholder's estate could assert the cause of action of the original bondholder.⁹¹ The original bondholder, who sold the bonds to the decedent, had a cause of action against the receiver of a bankrupt issuing company for the receiver's fraudulent actions.⁹² The *Phelan* court concluded that a cause of action against a receiver that arises from fraud automatically travels with a bond from the seller to the purchaser of the bond.⁹³ Although the *Phelan* court recognized a theory of automatic assignment of fraud claims, the *Phelan*

concurring) (owners of securities expressly may assign rule 10b-5 causes of action), *modification denied*, 711 F.2d 1207 (3d Cir.), *cert. denied*, 464 U.S. 893 (1983); *In re Saxon Sec. Litig.*, 644 F. Supp. 465, 471 (S.D.N.Y. 1985) (noting in dictum that although rule 10b-5 claims are not automatically assignable, rule 10b-5 claims may be expressly assignable in limited circumstances); *Rose v. Arkansas Valley Envtl. & Util. Auth.*, 562 F. Supp. 1180, 1188 (W.D. Mo. 1983) (security owner must do something in addition to selling security to assign rule 10b-5 cause of action to purchaser of security); *cf. Independent Investor Protective League v. Saunders*, 64 F.R.D. 564, 572 (E.D. Pa. 1974) (seller expressly may transfer chose in action to buyer).

88. See *Phelan v. Middle States Oil Corp.*, 154 F.2d 978, 1001 (2d Cir. 1946) (executrix of estate could maintain decedent's securities law cause of action); *International Ladies' Garment Workers' Union v. Shields & Co.*, 209 F. Supp. 145, 149 (S.D.N.Y. 1962) (original owners of bonds automatically assigned to plaintiffs original owners' right of action against defendant for fraudulent misrepresentation); *Mills v. Sarjem Corp.*, 133 F. Supp. 753, 762 (D.N.J. 1955) (executors of decedent's estate could maintain decedent's securities law cause of action).

89. See *infra* notes 90-104 and accompanying text (discussing courts' reasoning and holdings in *Phelan* and *Mills*).

90. 154 F.2d 978 (2d Cir. 1946).

91. *Phelan v. Middle States Oil Corp.*, 154 F.2d 978, 988 (2d Cir. 1946).

92. See *id.* (executors of bondholder's estate in receivership proceedings against defendant corporation charged receivers of corporation with fraud). In *Phelan* the plaintiff's husband before his death purchased the bonds of United, a subsidiary of a bankrupt corporation. *Id.* at 988. When the plaintiff's husband presented the United bonds for payment under the parent company's bankruptcy reorganization plan, the plaintiff's husband received a liquidating distribution. *Id.* The plaintiff, as executrix of her husband's estate, made a motion in the receivership proceedings against the defendant corporation for a compulsory accounting by the receivers. *Id.* The plaintiff claimed that the receiver of the bankrupt corporation fraudulently reported the assets and liabilities of the corporation and that the liquidating distribution price of the United bonds was fraudulently low. *Id.* In determining whether the receivers of Middle States Oil Corporation had acted fraudulently, the Second Circuit considered whether the original bondholder's cause of action passed automatically to the decedent bondholder upon the decedent's purchase of the bonds. *Id.* at 999.

93. *Id.* at 1000-02.

decision is distinguishable from the decisions that have not recognized automatic assignment.⁹⁴ First, *Phelan* was a bankruptcy case involving a fraud claim under tort law, not federal securities law.⁹⁵ Second, the Second Circuit in *Phelan* emphasized the fiduciary nature of a federal receiver's position.⁹⁶ The *Phelan* court noted that a receiver, as an "arm of the court," is under the highest kind of fiduciary duty to act fairly and openly.⁹⁷ The court concluded, therefore, that a rule of express assignment would limit the ability of the federal courts to hold federal receivers to their strict duty of accountability.⁹⁸ In promoting a policy of strict accountability of federal receivers, the Second Circuit in *Phelan*, in determining that fraud claims are automatically assignable, considered a policy that is not relevant to actions under the securities statutes.⁹⁹

A second decision that authorities cite for the rule of automatic assignability of securities law claims, although not concerning the accountability of federal receivers, is also distinguishable from the decisions that have not recognized automatic assignment.¹⁰⁰ In *Mills v. Sarjem Corp.*¹⁰¹ the plaintiffs, executors of the decedent plaintiff's estate, alleged that the defendant corporation, of which the decedent plaintiff had been a stockholder, conspired to purchase the stock of another company in violation of the 1934 Act and rule 10b-5.¹⁰² The plaintiffs in *Mills*, seeking damages under rule 10b-5, moved to substitute themselves in the decedent's action.¹⁰³ In *Mills* the United States District Court for the District of New Jersey granted the plaintiffs' motion to substitute the executors of the plaintiff's estate for the deceased plaintiff.¹⁰⁴ Without distinguishing between express and automatic assignment, the District Court in *Mills* noted that remedial damages actions under rule 10b-5 are neither personal nor penal in nature and, therefore, that rule 10b-5 remedial damages actions survive the security holder's death and are assignable.¹⁰⁵ The decision in *Mills*, like

94. See *infra* notes 95-99 and accompanying text (discussing factors that distinguish *Phelan v. Middle States Oil Corp.* from decisions not recognizing automatic assignment).

95. See *Phelan*, 154 F.2d at 988 (plaintiffs moved for compulsory accounting in receivership proceeding, alleging fraud and irregularities in connection with receivership).

96. See *id.* at 1000-02 (rejecting state rule of express assignment of fraud claims because of special nature of receiver's fiduciary duty).

97. *Id.* at 991.

98. See *id.* at 1000-01 (state rules of express assignment should not hamper federal courts in holding receivers, as officers of court, to high standard of accountability).

99. *Id.* at 1000-01. In *Phelan v. Middle States Oil Corp.* the United States Court of Appeals for the Second Circuit stressed the importance of strict accountability for federal receivers of bankrupt estates. *Id.* at 1001. Because of a strong federal policy protecting victims of the fraudulent activity of federal receivers, the *Phelan* court allowed the plaintiff to recover against the receiver corporation. *Id.*

100. See *infra* notes 101-05 and accompanying text (discussing decision in *Mills v. Sarjem Corp.*):

101. 133 F. Supp. 753 (D.N.J. 1955).

102. *Mills v. Sarjem Corp.*, 133 F. Supp. 753, 762 (D.N.J. 1955).

103. *Id.*

104. *Id.*

105. *Id.* at 761.

the decision in *Phelan*, is distinguishable from the decisions that do not recognize automatic assignment of securities fraud actions.¹⁰⁶ First, the district court decided *Mills* before the United States Supreme Court in *Blue Chip Stamps v. Manor Drug Stores* determined that only defrauded purchasers or sellers of securities may maintain rule 10b-5 actions.¹⁰⁷ Because the Supreme Court's decision in *Blue Chip* effectively overruled *Mills*,¹⁰⁸ the *Mills* court's reasoning that the executors of the plaintiff's estate could maintain the plaintiff's remedial damages action does not support a rule permitting the automatic assignment of securities fraud claims.¹⁰⁹ Second, the *Mills* court's reasoning does not support the automatic assignability of securities fraud claims because, by providing an action to individuals uninjured by fraud, the *Mills* court defeated the policy underlying section 10(b) and rule 10b-5, of protecting victims of fraud from deceptive and manipulative practices.¹¹⁰ Finally, the plaintiffs in *Mills* were not subsequent purchasers of securities who deliberately may have purchased the securities to benefit from the previous owners' fraud claims.¹¹¹ Rather, the plaintiffs in *Mills* and *Phelan* wished to substitute themselves as executors of a decedent's estate in the decedent's action against the defendant.¹¹² Many authorities assert, as an exception to the

106. See *infra* notes 107-13 and accompanying text (discussing facts that distinguish *Mills v. Sarjem Corp.* from decisions that have not recognized automatic assignment).

107. *Mills v. Sarjem Corp.*, 133 F. Supp. 753 (D.N.J. 1955); see also *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 754 (only actual purchasers and sellers of securities may maintain actions under § 10(b) and rule 10b-5); *infra* notes 116-22 and accompanying text (discussing *Blue Chip Stamps v. Manor Drug Stores*).

108. See *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 754 (only actual purchasers and sellers of securities may maintain actions under section 10(b) and rule 10b-5); see also *infra* notes 116-22 and accompanying text (discussing facts and United States Supreme Court's holding in *Blue Chip Stamps v. Manor Drug Stores*).

109. Compare *Mills*, 133 F. Supp. at 761 (because actions for remedial damages at common law survive death of holder, original security holder assigned rule 10b-5 action to executors of original security holder's estate) with *Blue Chip*, 421 U.S. at 733-37 (in enacting securities statutes, Congress ensured that only purchasers and sellers of securities would be able to maintain securities law claims).

110. See *Mills*, 133 F. Supp. at 761 (because actions for remedial damages at common law survive death of holder, original security holder assigned rule 10b-5 action to executors of original security holder's estate); see also S. REP. NO. 792, 73d Cong., 2d Sess. 3 (1934) (purpose of 1934 Act was to provide remedy for investors that suffered injury from unfair methods of speculation in securities transactions prior to and during stock market crash).

111. See *Mills*, 133 F. Supp. at 761 (plaintiffs were executors of decedent stockholder's estate).

112. See *id.* (executors of estate moved to be substituted as plaintiffs in decedent's securities fraud action against corporation); see also *Phelan v. Middle States Oil Corp.*, 154 F.2d 978, 990 (2d Cir. 1946) (plaintiff, widow of original bondholder, requested that court substitute plaintiff, as executrix of decedent bondholder's estate, in decedent bondholder's rule 10b-5 action).

In addition to the decisions in *Mills* and *Phelan*, the decision in *International Ladies' Garment Workers' Union v. Shields & Co.* to recognize the automatic assignability of federal securities fraud claims also is distinguishable from decisions rejecting the automatic assign-

express assignment rule, that a rule 10b-5 cause of action does not abate upon a security holder's death, but instead, passes to the executor of the security holder's estate.¹¹³

In addition to the distinctions between the decisions supporting an automatic assignment rule and the decisions recognizing only a rule of express assignment, several policy considerations, as well as the common law of assignment, further support rejecting a rule of automatic assignment.¹¹⁴ In recent years, the federal courts carefully have defined the policy and purpose behind the securities regulations laws.¹¹⁵ For example, in *Blue Chip Stamps v. Manor Drug Stores*¹¹⁶ the United States Supreme Court established that only actual purchasers and sellers of securities may bring private damages actions under section 10(b) and rule 10b-5.¹¹⁷ In deter-

ment rule. *International Ladies' Garment Workers' Union v. Shields & Co.*, 209 F. Supp. 145 (S.D.N.Y. 1962). In *Shields* the United States District Court for the Southern District of New York considered whether subsequent purchasers of bonds could assert the previous bondholders' claim of reliance on the allegedly false representations of the defendants. *Id.* at 149. In determining whether the previous bondholders had assigned their rights of action to the plaintiffs, the *Shields* court relied upon the district court's reasoning in *Mills*. *Id.* at 149-50. The *Shields* court noted that the plaintiffs in *Shields* requested remedial relief. *Id.* In accordance with the decision in *Mills*, the *Shields* court reasoned that, because other courts have ruled that actions for remedial damages are assignable, the original owners of the bonds automatically had assigned to the plaintiffs the original owners' rights of action against the defendant for fraudulent misrepresentation. *Id.*; see *Mills*, 133 F. Supp. at 762 (because actions for remedial damages at common law survive death of holder, original security holder assigned rule 10b-5 action to executors of original security holder's estate). Like the court in *Mills*, the *Shields* court decided *Shields* before the United States Supreme Court enunciated the policy behind rule 10b-5 of protecting defrauded investors from manipulative and deceptive practices. *International Ladies' Garment Workers' Union v. Shields & Co.*, 209 F. Supp. 145 (S.D.N.Y. 1962); *Mills*, 133 F. Supp. at 762; see *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 728-29 (Congress enacted securities statutes to protect investors from fraudulent practices of speculators); *supra* notes 1-2 and accompanying text (by enacting securities statutes in 1930s, Congress was reacting to abuse of securities markets by dealers and underwriters that resulted in injury to investors). Accordingly, the *Shields* court's reliance on the *Mills* decision in recognizing a rule of automatic assignment does not support a rule permitting the automatic assignment of federal securities law claims. *Shields*, 209 F. Supp. at 149-50. Additionally, in *Shields* the plaintiffs' predecessors in title to the bonds "duly assigned" to the plaintiffs all of the predecessors' rights, titles, and interests in the bonds. *Shields*, 209 F. Supp. at 149. Although the *Shields* court did not elaborate on the predecessors' apparently express assignment to the plaintiffs, the decision of the *Shields* court may represent approval only of an express assignment rule and give no support to an automatic assignment rule. *Id.*

113. See *In re Saxon Sec. Litig.*, 644 F. Supp. 465, 471 n.12 (S.D.N.Y. 1985) (cases in which decedent's estate claimed right to maintain decedent's action do not support general proposition that securities law claims are automatically assignable).

114. See *infra* notes 115-24 and accompanying text (discussing policy considerations behind federal securities law and common law of assignment).

115. See *infra* notes 116-24 and accompanying text (discussing cases defining policy behind securities laws).

116. 421 U.S. 723 (1975).

117. *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 730-31 (1975). In *Blue Chip Stamps v. Manor Drug Stores* the United States Supreme Court considered whether

mining that only actual purchasers or sellers may bring rule 10b-5 actions, the Supreme Court relied upon Congress' intent in enacting the Securities Act of 1933 and the Securities Exchange Act of 1934.¹¹⁸ The Supreme Court in *Blue Chip* noted that the congressional intent to permit only defrauded purchasers or sellers of securities to recover damages for securities fraud is evident in the phrasing of section 10(b).¹¹⁹ Comparing the phrasing of section 10(b) to the phrasing of other provisions of the 1933 Act and the 1934 Act, the Supreme Court noted that the 1933 Act, in sections other than section 10(b), provides remedies for parties other than the actual purchasers or sellers of securities.¹²⁰ The Supreme Court ex-

offerees of a stock offering, who neither purchased nor sold the offered shares, could maintain a private cause of action based on the offeror's alleged violation of rule 10b-5. *Id.* at 725. In *Blue Chip* the United States, under an antitrust reorganization plan, required New Blue Chip, a company that sold trading stamps to retailers, to offer shares of Blue Chip common stock to retailers who were not shareholders of Blue Chip prior to the antitrust action. *Id.* at 725-26. New Blue Chip registered the offering and distributed a prospectus to the offerees in accordance with the Securities Act of 1933. *Id.* at 726. Manor Drug Stores, representing a class of plaintiff-offerees, filed a complaint alleging that New Blue Chip phrased its prospectus in an intentionally negative manner to discourage the offerees from accepting the offer of common stock, in violation of section 10(b) and rule 10b-5. *Id.* at 726-27. Manor Drug Stores' complaint alleged further that, by discouraging the offerees from accepting the offer, New Blue Chip could reserve the shares for a subsequent public offering at a higher price. *Id.* at 727. The United States District Court for the Central District of California dismissed the complaint for failure to state a claim upon which a court could grant relief. *See id.* (discussing district court's disposition of *Blue Chip*). The United States Court of Appeals for the Ninth Circuit reversed the holding of the district court, finding that Manor Drug Stores, although neither a purchaser nor a seller of securities, could maintain a cause of action under rule 10b-5. *See id.* at 727 (discussing appellate disposition of *Blue Chip*). The defendants appealed the decision of the Court of Appeals for the Ninth Circuit to the Supreme Court of the United States. *Id.* The Supreme Court granted Blue Chip Stamps' petition for writ of certiorari. *Id.* at 723. The Supreme Court in *Blue Chip* determined that the purchaser-seller requirement for actions under section 10(b) and rule 10b-5 is a sound, well-supported requirement. *Id.* at 737-49. Accordingly, the Supreme Court reversed the judgment of the Ninth Circuit in *Blue Chip*. *Id.*; *see infra* notes 119-22 and accompanying text (discussing Supreme Court's reasoning in *Blue Chip*); *see also* *Birnbaum v. Newport Steel Corp.*, 193 F.2d 461, 463 (2d Cir.) (only actual purchasers and sellers of securities may maintain private actions under § 10(b) and rule 10b-5), *cert. denied*, 343 U.S. 956 (1952).

118. *See Blue Chip*, 421 U.S. at 727-29 (reviewing congressional intent in enacting securities laws).

119. *Id.* In its decision in *Blue Chip*, the United States Supreme Court reasoned that the wording of rule 10b-5 prohibiting fraud "in connection with the purchase or sale" of securities, and the lack of evidence of a congressional intent to provide a remedy under section 10(b) to parties other than defrauded purchasers or sellers of securities supported limiting recovery under rule 10b-5 to actual purchasers and sellers. *Id.*; *see supra* notes 1-2 and accompanying text (discussing legislative history of section 10(b)).

120. *See Blue Chip*, 421 U.S. at 733-37 (when Congress intended to provide remedy to individuals other than purchasers and sellers of securities, Congress expressly provided remedy); *see also* Trust Indenture Act, 15 U.S.C. § 77q (1982), *as amended by* Act of Aug. 10, 1954, 68 Stat. 686 (providing that any person who in offer or sale of securities acts fraudulently shall act unlawfully); Trust Indenture Act, 15 U.S.C. § 77bb(a) (1982) (limiting recovery in any private damages action under Securities Exchange Act of 1934 to persons who have suffered actual damages).

plained that if Congress had intended to provide the remedies in section 10(b) to parties that were neither injured purchasers nor injured sellers of securities, Congress expressly would have provided the remedies in the phrasing of section 10(b).¹²¹ In interpreting section 10(b) and rule 10b-5, the Supreme Court concluded, therefore, that Congress intended to provide a remedy only for defrauded purchasers and sellers of securities.¹²² Courts that have addressed the issue of assignment of rule 10b-5 actions since the Supreme Court's decision establishing the purchaser-seller requirement have recognized that a rule of automatic assignment of securities fraud actions under rule 10b-5 would be inconsistent with the congressional policy underlying section 10(b).¹²³ These courts have rejected the rule of automatic assignment in securities fraud cases because the rule would reward parties who have not suffered fraud but, on the contrary, may have planned their investments carefully to take advantage of a defrauded party's legal claim.¹²⁴

In addition to the policy that underlies the securities fraud action, the common law of assignment supports the rejection of the rule of automatic assignment of securities fraud claims and the acceptance of the rule of

121. See *Blue Chip*, 421 U.S. at 733-34 (comparing phrasing of § 10(b) to wording of both antifraud provision of 1933 Act and § 28(a) of 1934 Act, and concluding that Congress intended to limit right to recover rule 10b-5 damages to actual purchasers and sellers of securities).

122. See *id.* at 733-37 (holding that only purchasers and sellers may maintain claims under securities acts); *Rose v. Arkansas Valley Envtl. & Util. Auth.*, 562 F. Supp. 1180, 1188-89 (W.D. Mo. 1983) (recognizing in United States Supreme Court's decision in *Blue Chip* underlying premise that Congress intended that only defrauded purchasers and sellers may bring actions under rule 10b-5).

123. See *In re Nucorp Energy Sec. Litig.*, 772 F.2d 1486, 1490 (9th Cir. 1985) (rule of automatic assignment fails to provide remedy to individual for whom securities acts provide remedy); *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 729 (3d Cir.) (Garth, J., concurring) (automatic assignment rule contravenes congressional intent underlying securities laws by unjustly depriving injured security holders of right to recover and granting right to recover instead to subsequent purchasers who sustained no injury), *modification denied*, 711 F.2d 1207 (3d Cir.) *cert. denied*, 464 U.S. 893 (1983); *Independent Investor Protective League v. Saunders*, 64 F.R.D. 564, 572 (E.D. Pa. 1974) (automatic assignment rule contravenes congressional policy underlying securities acts that only injured party may recover under securities acts).

124. See *Blue Chip*, 421 U.S. at 733 (recognizing that wording of § 10(b) provides remedy for investors that have suffered injury in connection with purchase or sale of securities); *In re Nucorp Energy Sec. Litig.*, 772 F.2d 1486, 1490 (9th Cir. 1985) (rule of automatic assignment fails to provide remedy to individual for whom securities acts provide remedy); *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 729 (3d Cir.) (Garth, J., concurring) (automatic assignment rule contravenes congressional intent underlying securities laws by unjustly depriving injured security holders of right to recover and granting right to recover instead to subsequent purchasers who sustained no injury), *modification denied*, 711 F.2d 1207 (3d Cir.) *cert. denied*, 464 U.S. 893 (1983); *Independent Investor Protective League v. Saunders*, 64 F.R.D. 564, 572 (E.D. Pa. 1974) (automatic assignment rule would contravene congressional policy underlying securities acts that only injured party may recover under securities acts).

express assignment.¹²⁵ At common law, choses in action, which are legal rights that are enforceable in a suit at law, are assignable if the chose is neither personal nor penal in nature.¹²⁶ Because a rule 10b-5 action is neither personal nor penal in nature, early decisions relying on the assignability of choses in action held that remedial damages actions under rule 10b-5 were assignable.¹²⁷ The traditional common law rule of assignment, however, required that, to assign his rights effectively, a party clearly must evidence his intent to assign his rights to a second party.¹²⁸ The common law practice of determining assignment from the intent of the parties, therefore, suggests that if rule 10b-5 actions are assignable, a security holder expressly must assign his cause of action to a subsequent holder for the assignment to be effective.¹²⁹

Along with policy and common law support for a rule of express assignment, other considerations support the rejection of the automatic assignment rule and acceptance of the express assignment rule.¹³⁰ Proponents of the automatic assignment rule contend that the automatic assignment of rule 10b-5 claims adequately serves the policy behind section 10(b) of protecting security holders from manipulative or deceptive practices in securities transactions.¹³¹ The proponents reason that because automatic assignment ensures that either a defrauded party or his successor may bring a rule 10b-5 claim to court, the rule of automatic assignment advances the policy behind section 10(b) of protecting security holders.¹³²

125. See *infra* notes 126-28 and accompanying text (discussing common law of assignment).

126. See 6 AM. JUR. 2D *Assignments* §§ 27-29 (1963) (only choses in action that are not assignable are torts for personal injuries and for wrongs to person, reputation, or feelings).

127. See *International Ladies' Garment Workers' Union v. Shields & Co.*, 209 F. Supp. 145, 149 (S.D.N.Y. 1962) (because remedial actions are assignable at common law, remedial action under § 10(b) and rule 10b-5 is assignable); *Mills v. Sarjem Corp.*, 133 F. Supp. 753, 761 (D.N.J. 1955) (same); *supra* notes 101-05 and accompanying text (discussing *Mills*).

128. See 6 AM. JUR. 2D *Assignments* § 1 (1963) (evidence of intent to assign defines legal assignment); see *Russell v. Texas Consolidated Oils*, 120 F. Supp. 508, 512-13 (D.C.N.M. 1954) (without evidence of intent to bind by assignment, court cannot recognize attempted assignment).

129. See Note, *Express Versus Automatic Assignment of Section 10(b) Causes of Action*, 1985 DUKE L.J. 813, 823 (1985) (rule of express assignment of § 10(b) causes of action is consistent with common law practice of examining parties' intent to determine whether assignment has occurred).

130. See *infra* notes 131-50 and accompanying text (discussing further support for rule of express assignment).

131. See *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 740-41 (3d Cir. 1983) (Gibbons, J., dissenting) (because automatic assignment rule ensures, through free transfer of claims, that one security holder will maintain cause of action, automatic assignment rule achieves Congress' policy of protecting security holders from manipulative or deceptive acts of securities sellers).

132. See *id.* (Gibbons, J., dissenting) (if victims of securities fraud freely may sell securities and causes of action on market, subsequent purchaser will maintain action and accomplish goal of securities law of combating manipulative and deceptive practices in securities transactions).

This argument, however, assumes that the victim of fraud wishes to assign his rule 10b-5 cause of action to a subsequent purchaser.¹³³ Of course, a victim that does not wish to assign his right of action to a purchaser expressly could provide that the right of action does not pass with the sale of the security.¹³⁴ In the absence of an express reservation of rights, however, assuming that the cause of action arose prior to the sale, a court which determined that a cause of action automatically traveled with the sale of a security would confer the cause of action upon a second party that has suffered no injury.¹³⁵ In contrast, a rule allowing the express assignment of rule 10b-5 causes of action would respect the intentions of a selling party who expressly transferred his cause of action to a subsequent purchaser.¹³⁶

In addition to arguing that an automatic assignment rule respects the congressional intent behind the securities statutes, proponents of the au-

133. See *id.* (Gibbons, J., dissenting) (under automatic assignment rule, securities law causes of action automatically travel with securities to subsequent purchasers of securities, regardless of original owners' wishes).

134. See 6 AM. JUR. 2D *Assignments* § 1 (1963) (evidence of intent to assign defines legal assignment).

135. See *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 729 (3d Cir. 1983) (Garth, J., concurring) (automatic assignment rule tends to reward uninjured security holders by gratuitously transferring causes of action to them); *In re Nucorp Energy Sec. Litig.*, 772 F.2d 1486, 1490 (9th Cir. 1985) (rule of automatic assignment gratuitously transfers cause of action to person who has not suffered fraud); *Independent Investor Protective League v. Saunders*, 64 F.R.D. 564, 572 (E.D. Pa. 1974) (automatic assignment rule deprives injured person of cause of action and gives cause of action to person that is simply shrewd or lucky).

136. See Note, *supra* note 129, at 831 (in faceless market, only requirement that security holder express his intent to assign his cause of action to subsequent purchaser will support security holder's intent). Proponents of the automatic assignment rule fail to respect a security holder's intent when transferring his security. *Id.* Accordingly, in assuming that the seller transfers both his property and the rights incident to the property, proponents of the automatic assignment rule fail to consider the common law distinction between the transfer of property and the transfer of rights arising from property ownership. See *id.* at 828 (dissent in *Lowry* overlooked distinction between transfer of property and transfer of property rights); see also *Lowry*, 707 F.2d at 741 (Gibbons, J., dissenting) (holding that seller of security automatically assigns seller's cause of action to subsequent purchasers of security, without mentioning seller's intent). An express assignment rule would enable the assignment of securities law claims to transpire in the same way that the assignment of rights of action for breach of warranty transpires. Note, *supra* note 129, at 828. A seller of property does not automatically assign his right of action for breach of warranty, because the sale of the property does not necessarily indicate that the seller intended to relinquish his cause of action for breach of warranty. *Id.* In the breach of warranty situation, in accordance with the common law of assignment, the law recognizes that a seller's intent determines whether or not he assigned his right of action in his property to a subsequent purchaser. *Id.* A court determining whether a seller of a security automatically assigned his cause of action to a subsequent purchaser of the security has no more reason than a court reviewing the assignment of a right of action for breach of warranty to assume that the seller intended to assign his cause of action. *Id.* Thus, because an express assignment rule respects the intent of the seller of a security, an express assignment rule most effectively accords with the common law of assignment. *Id.*

automatic assignment rule claim that, in the anonymous securities market in which parties conduct most transfers without ever meeting, a rule requiring transferors expressly to assign their rule 10b-5 rights to transferees is impractical.¹³⁷ The proponents, however, fail to recognize that although the securities market is usually anonymous, buyers and sellers operate through intermediary securities brokers.¹³⁸ Because these brokers arrange all other terms of purchase agreements, they also may arrange for an express provision that the seller's 10b-5 right of action will pass with the security that he is selling to other investors.¹³⁹

Proponents of a rule of automatic assignment also contend that a rule of automatic assignment allows the party that is most likely to discover the fraud to pursue a fraud claim.¹⁴⁰ The proponents reason that, because security holders often sell their securities before discovering that they have a rule 10b-5 claim, a rule of automatic assignment permits the adjudication of claims that a holder could not maintain under a rule of express assignment if the seller sold his securities prior to discovering his rule 10b-5 cause of action.¹⁴¹ The rule's supporters conclude that, by recognizing a rule of automatic assignment, courts more effectively will deter manipulative and deceptive practices in securities transactions.¹⁴²

The arguments of the proponents of a rule of automatic assignment are convincing in the context of only one particular scenario.¹⁴³ In most instances, when an investor sells his security before discovering that he has a rule 10b-5 claim, the express assignment rule still will accomplish the policy goals behind the securities laws.¹⁴⁴ Under an express assignment rule, when the original security holder discovers that he had a rule 10b-5 claim, if he neither expressly nor automatically assigned his cause of action to the purchaser of his security, the original holder still may be able to maintain an action based on his previous ownership of the security.¹⁴⁵ If

137. See *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 746 (3d Cir. 1983) (Seitz, J., dissenting) (in faceless securities market, express assignment rule is impractical); see *supra* notes 36-49 and accompanying text (discussing dissenters' opinions in *Lowry*).

138. See Note, *supra* note 129, at 824 (buyers and sellers routinely agree on details of securities transactions through intermediary brokers).

139. See *id.* (whether seller of security assigns seller's cause of action to buyer of security is contractual term, upon which buyer and seller can agree through broker).

140. *Lowry v. Baltimore & O. R.R.*, 707 F.2d 721, 746 (3d Cir. 1983) (Seitz, J., dissenting); see *supra* notes 36-49 and accompanying text (discussing dissenters' opinion in *Lowry* that because securities law claims do not always arise quickly, purchaser of security is more likely than original holder to discover original holder's claim).

141. See *Lowry*, 707 F.2d at 746 (Seitz, J., dissenting) (automatic assignment rule advances remedial purpose of securities laws by placing securities law claim with person most likely to learn of existence of claim).

142. See *id.* (courts will deter manipulative practices in securities trading by placing securities law claim with person most likely to discover claim).

143. See *infra* notes 144-47 and accompanying text (discussing reasons for failure of arguments of proponents of automatic assignment rule).

144. See Note, *supra* note 129, at 827 (express assignment rule accomplishes purposes of § 10(b) at least as well as automatic assignment rule).

145. *Id.*

the original holder expressly does assign his rights to a subsequent purchaser of the security, the subsequent purchaser can maintain an action.¹⁴⁶ However, assuming an efficient capital market, if the subsequent purchaser of the security is injured by the fraud when the price of his stock goes down in reaction to the news of the fraud, then he probably has no right of action against the issuer of the security.¹⁴⁷ Thus, an express assignment rule only advances the policy and purpose underlying the securities laws if the cause of action against the issuer of the security has become public knowledge.¹⁴⁸ As a result, a rule of automatic assignment seems preferable in those instances in which the subsequent purchaser of a security suffers injury from the fraudulent acts of the issuer against the previous owner of the security.¹⁴⁹

The majority of courts that have addressed the issue of the assignability of section 10(b) and rule 10b-5 causes of action in recent years has rejected the concept of automatic assignment in favor of a rule that allows only the express assignment of section 10(b) and rule 10b-5 causes of action.¹⁵⁰ These courts have founded their decisions on the traditions of the common law of assignment and the United States Supreme Court's recent interpretations of the policy underlying federal securities law.¹⁵¹ Furthermore, these courts have determined that a rule of express assignment most effectively advances the policy behind the federal securities laws of protecting investors from deceptive and manipulative practices by preventing uninjured investors from maintaining claims to which they are not entitled.¹⁵² Only a few courts have recognized a rule of automatic assignment and these decisions either differ factually from the decisions rejecting the automatic assignment rule or precede the United States Supreme Court's decision in *Blue Chip Stamps v. Manor Drug Stores*.¹⁵³ Although the

146. *Id.*

147. *See id.*, n.91 (in *Lowry* cause of action against B & O for fraud had become public knowledge and plaintiff knew of cause of action, in which case express assignment rule is most appropriate).

148. *Id.*

149. *Id.*

150. *See supra* notes 9, 52-84, 87 and accompanying text (discussing reasoning and holdings of courts announcing express assignment rule in federal securities law cases).

151. *See Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 731 (1975) (lack of evidence of congressional intent to provide remedy under section 10(b) to parties other than defrauded purchasers or sellers of securities supports limiting recovery under rule 10b-5 to actual purchasers and sellers); *supra* notes 9, 52-84, 87 and accompanying text (discussing reasoning and holdings of courts announcing express assignment rule in federal securities law cases); *supra* notes 125-29 and accompanying text (discussing common law of assignment); *supra* notes 117-22 and accompanying text (discussing *Blue Chip* Court's analysis of congressional intent underlying securities laws).

152. *See supra* notes 9, 52-84, 87 and accompanying text (discussing reasoning and holdings of courts announcing that express assignment rule in federal securities law promotes policy underlying federal securities laws); *supra* notes 114-24 and accompanying text (discussing policy underlying securities laws).

153. *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 731 (1975); *see supra*

federal courts of appeals have failed to enunciate a clear rule on the assignment of federal securities law causes of action,¹⁵⁴ the noticeable trend toward rejecting the concept of automatic assignment of federal securities fraud claims is well supported and, except in the case of the injured subsequent purchaser, in the future, should provide a clear precedential rule for securities investors.¹⁵⁵

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notes 89-113 and accompanying text (discussing distinguishing factors of cases in which courts have recognized rule of express assignment); *supra* notes 117-22 and accompanying text (discussing reasoning of Supreme Court in *Blue Chip*).

154. *See supra* notes 8-9 and accompanying text (discussing conflicting opinions among federal courts regarding question of assignment of securities claims).

155. *See supra* notes 85-149 and accompanying text (discussing arguments in support of express assignment rule).