# THE IMPORTANCE OF STATUTORY TEXT: From Scienter to Nonstatutory Defenses under Arizona Securities Law

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## INTRODUCTION

Although securities cases are statutory cases, attorneys commonly begin their securities research with a search for cases. We do not begin by reading the statutes. We turn first to Arizona case law, and if that is missing, we usually search for SEC rule 10b-5[1] cases that address the issue. Not often does anyone begin Arizona securities research with an analysis of the statutory text and the principles of interpretation that guide courts in construing statutes. This is a mistake.[2]

It is a mistake for at least two reasons. First, unlike actions under rule 10b-5, liability under Arizona's securities statutes is express liability.[3] The

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1. 17 C.F.R. § 240.10b-5 (2007).

2. It is a common mistake that extends beyond securities cases. Justice Scalia was asked in a 2008 interview, "Do you think law students would be better served if they focused more on statutory construction than the case method?" *A Voice for the Write: Tips on Making Your Case from a Supremely Reliable Source*, 94 A.B.A. J. 36, 38 (May 2008) (containing excerpts of a March 2008 interview by Richard Bust with U.S. Supreme Court Justice Antonin Scalia and author Bryan Garner). Justice Scalia agreed wholeheartedly, "Well, I have made that very point . . . what judges do nowadays is very little common law. But what they do almost all the time is that they interpret a [statutory or other] text. They almost always have a text in front of them." *Id.*; *see also* ANTONIN SCALIA & BRYAN A. GARNER, MAKING YOUR CASE: THE ART OF PERSUADING JUDGES xxii (2008) ("[U]nconstrained common-law decision-making is an increasing rarity. Courts are usually confronted with interpreting a governing text, whether a constitutional provision, a statute, an agency regulation, or a municipal ordinance.").

3. *See* ARIZ. REV. STAT. ANN. § 44-2001(A) (2008) (providing that a defrauded purchaser "may bring an action in a court of competent jurisdiction to recover the consideration paid for the securities, with interest, taxable court costs and reasonable attorney fees, less the amount of any income received by dividend or otherwise from ownership of the securities, on tender of the securities purchased or the contract made, or for damages if the purchaser no longer owns the securities."); *id.* § 44-2002(A) (2008) (providing that a defrauded seller "may bring an action in a court of competent jurisdiction to recover the amount of the seller's damages, with interest, taxable court costs and reasonable attorney fees"); *see also* Grand v. Nacchio, 147 P.3d 763,

rule 10b-5 action is an implied right of action. The federal courts have looked to the rules governing common-law fraud to define the 10b-5 action.[4] In contrast, the elements of liability under Arizona's express-liability provisions are defined by the statutes themselves.[5] It is a mistake therefore to use the common law to define what the legislature defined. Besides that, Arizona's securities laws were passed for public protection that the common law did not provide.[6] Using the common law to interpret the securities statutes risks undermining the expanded protection the legislature envisioned.

Second, statutory construction requires careful thought. American courts have no "generally accepted, and consistently applied theory of statutory interpretation."[7] This means we must make choices about what may be competing theories of statutory interpretation. Reasoned analysis will typically require consideration of a mix of interpretative approaches including analysis of the statute's words; legislative history, intent, and purpose; canons of construction; and precedent, both judicial and administrative.[8] Anyone who addresses a securities-law issue without

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772–73 (Ariz. Ct. App. 2006) (explaining the statutory remedies under Arizona Revised Statutes section 44-2001(A)).

4. *See* Dura Pharms., Inc. v. Broudo, 544 U.S. 336, 343 (2005) ("Judicially implied private securities-fraud actions resemble in many (but not all) respects common-law deceit and misrepresentation actions."); Basic Inc. v. Levinson, 485 U.S. 224, 231 (1988) (referring to "positive and common-law requirements for a violation of [section] 10(b) or of rule 10b-5"); 9 LOUIS LOSS & JOEL SELIGMAN, SECURITIES REGULATION 4379 (3d rev. ed. 2004) (stating as to rule 10b-5 that "if it is 'cricket' for the federal courts to invent new torts or tort-like actions, it seems fair enough for them to invent reasonable restrictions on the new actions as common law judges a long time ago invented doctrines like materiality, scienter, reliance, and causation in order to achieve a sense of balance").

5. Aaron v. Fromkin, 994 P.2d 1039, 1042 (Ariz. Ct. App. 2000) ("The elements of securities fraud are articulated within the statute itself.").

6. *See id.* ("The legislature made the task of proving securities fraud much simpler than proving common-law fraud."); *cf.* Herman & MacLean v. Huddleston, 459 U.S. 375, 389 (1983) ("[A]n important purpose of the federal securities statutes was to rectify perceived deficiencies in the available common law protections by establishing higher standards of conduct in the securities industry."); *see also* Bullard v. Garvin, 401 P.2d 417, 419 (Ariz. Ct. App. 1965) (interpreting the securities registration statutes and stating that, "[g]enerally, statutes of this nature providing a remedy for those who may have been taken advantage of have been liberally construed in favor of those persons whom they are designed to protect").

7. HENRY M. HART, JR. & ALBERT M. SACKS, THE LEGAL PROCESS: BASIC PROBLEMS IN THE MAKING AND APPLICATION OF LAW 1169 (William N. Eskridge, Jr. & Philip P. Frickey eds., 1994); *accord* ANTONIN SCALIA, A MATTER OF INTERPRETATION: FEDERAL COURTS AND THE LAW 14 (1997).

8. *See* WILLIAM N. ESKRIDGE, JR., PHILIP P. FRICKEY & ELIZABETH GARRET, LEGISLATION AND STATUTORY INTERPRETATION 9 (2000) (suggesting that practitioners should "craft their arguments as cumulative rhetoric, taking the most convincing pieces of whatever approaches best fit their side of the case"); SCALIA & GARNER, *supra* note 2, at 44–51

focusing on the legislative text and the approaches to statutory interpretation that courts use is not fully analyzing the issue.

The following discussion is divided into four parts. Through a discussion of scienter, Part I introduces the use of reasoned statutory interpretation as a framework within which to apply case law in resolving securities issues. It shows that administrative precedent and statements of legislative intent play an especially important role in interpreting Arizona's securities statutes. Part II expands upon the importance of administrative precedent, particularly decisions by the Arizona Corporation Commission, in interpreting the state's securities laws. Part III returns to the use of legislative statements and shows how Arizona's courts, since 2001, have used these legislative statements to explain and interpret the state's securities laws. With the aid of this background information, Part IV analyzes six securities issues on which Arizona case law is unsettled or could be clarified through statutory analysis: unauthorized trading, reliance, contributory fault by investors, participant liability, aiding and abetting, and nonstatutory defenses. In each instance statutory analysis is used to provide insights and answers that a purely case-driven approach would overlook. Through these examples the Article shows the importance of using statutory interpretation as the foundation for developing reasoned securities-law precedent.

## I. AN EXAMPLE: SCIENTER

In trial-court litigation, arguments are occasionally made that subsection (3) of Arizona Revised Statutes section 44-1991(A)[9] requires scienter, i.e.,

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(explaining the importance of collectively using textual analysis, canons of construction, and legislative history to make persuasive arguments).

9. Section 44-1991(A) (2008) provides:

> It is a fraudulent practice and unlawful for a person, in connection with a transaction or transactions within or from this state involving an offer to sell or buy securities, or a sale or purchase of securities, including securities exempted under [sections] 44-1843 or 44-1843.01 and including transactions exempted under [sections] 44-1844, 44-1845 or 44-1850, directly or indirectly to do any of the following:
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> 1. Employ any device, scheme or artifice to defraud.
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> 2. Make any untrue statement of material fact, or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.
>
> 3. Engage in any transaction, practice or course of business which operates or would operate as a fraud or deceit.

intent to defraud.[10] The argument is not surprising since all three subsections of rule 10b-5 require scienter.[11] No Arizona appellate case addresses scienter under section 44-1991(A)(3). But as a matter of statutory construction, a reasoned analysis might proceed as follows.

First, the language of subsection (3) does not by its words require intent to defraud. By its terms, subsection (3) makes it a fraudulent practice to "[e]ngage in any transaction, practice or course of business which operates or would operate as a fraud or deceit."[12] These words focus on the effect of the defendant's conduct, not the defendant's culpability. Under a plain reading of the statute's language, someone could engage in a course of business that operates as a fraud on investors without intending to deceive.

Second, the 1951 Arizona Securities Act was enacted with a statement of legislative intent that instructs courts to construe the securities statutes liberally, as remedial measures.[13] Reading subsection (3) to focus on the effect on investors, rather than the defendant's intent, furthers this legislative directive. Likewise, reading the statute to prohibit unintentional fraud enhances investor protection and is faithful to the liberal reading the legislature mandated.

Third, in 1996 a second statement of legislative intent was enacted. This legislative statement provides that, "[T]he courts may use as a guide the interpretations given by the securities and exchange commission and the federal or other courts in construing substantially similar provisions in the federal securities laws of the United States."[14] Through this statement, the legislature has expressed its intent to allow courts to find guidance in interpretations under "substantially similar" federal securities laws.

Substantially the same language found in section 44-1991(A) appears in section 17(a) of the 1933 Securities Act.[15] The 1996 statement of intent

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10. *See, e.g.*, Little v. First Cal. Co., [1977–78 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,226, at 92,561 (Oct. 17, 1977), *available at* 1977 WL 1055, at *8 (concluding without citation of authority that subsections (1) and (3) of the Arizona Revised Statutes section 44-1991 (now section 44-1991(A)) require scienter).

11. *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 212 (1976) (rejecting arguments that the language of subsections (b) and (c) of rule 10b-5 encompass negligent behavior).

12. ARIZ. REV. STAT. ANN § 44-1991(A)(3) (2008).

13. Securities Act of Arizona, ch. 18, § 20, 1951 Ariz. Sess. Laws 46, 75 (quoted *infra* text accompanying note 26).

14. Sales of Securities–Litigation–Fraud, Unlawful Activity, Etc., ch. 197, sec. 11(C), § 44-2126, 1996 Ariz. Legis. Serv. 1168, 1189 (West).

15. *Compare* 1933 Securities Act § 17(a), 15 U.S.C. § 77q(a) (2006), *with* ARIZ. REV. STAT. ANN § 44-1991(A) (quoted *supra* note 9). Section 17(a) reads:

> It shall be unlawful for any person in the offer or sale of any securities or any security-based swap agreement (as defined in section 206B of the Gramm-Leach-Bliley Act) by the use of any means or instruments of

therefore suggests that interpretations under section 17(a) may provide guidance on the meaning of section 44-1991(A). And even before 1996, the Arizona Supreme Court looked to the U.S. Supreme Court's interpretation of section 17(a) for guidance on scienter under section 44-1991. In *State v. Gunnison*, a 1980 decision, the Arizona Supreme Court adopted the reasoning of *Aaron v. SEC*, a U.S. Supreme Court decision, and its interpretation of section 17(a)(2) to decide whether scienter was required under subsection (2) of Arizona Revised Statutes section 44-1991 (now 44-1991(A)).[16] Section 17(a)(2) makes it unlawful to make "any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading."[17] *Aaron* found nothing in this language to require intent to deceive.[18] *Gunnison*, in turn,

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> transportation or communication in interstate commerce or by use of the mails, directly or indirectly–
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> (1) to employ any device, scheme, or artifice to defraud, or
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> (2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; or
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> (3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

15 U.S.C. § 77q(a). Nearly the same language appears in rule 10b-5. But as explained in *Ernst & Ernst v. Hochfelder*, rule 10b-5 is limited by section 10(b) of the 1934 Act. 425 U.S. at 212–13. Section 10(b) does not contain the language that appears in rule 10b-5. The operative language of section 10(b) makes it,

> unlawful for any person . . . [t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. § 78j(b) (2006). *Hochfelder* interpreted this language to require scienter and held that arguably broader language in subsections (b) and (c) of rule 10b-5 is limited by the statute. 425 U.S. at 214 ("[D]espite the broad view of the Rule [10b-5] advanced by the Commission in this case, its scope cannot exceed the power granted the Commission . under [§] 10(b)."). *Aaron v. SEC* reaffirmed *Hochfelder*, but reached a different conclusion as to subsections (2) and (3) of section 17(a) because those subsections, like subsections (2) and (3) of Arizona Revised Statutes section 44-1991(A), are part of the statute itself. 446 U.S. 680, 695–96 (1980) ("The language of § 17(a) strongly suggests that Congress contemplated a scienter requirement under § 17(a)(1) but not under § 17(a)(2) or § 17(a)(3).").

16. State v. Gunnison, 618 P.2d 604, 606–07 (Ariz. 1980); *see Aaron*, 446 U.S. at 680.

17. 15 U.S.C. § 77q(a)(2).

18. *Aaron*, 446 U.S. at 696 ("[T]he language of § 17(a)(2), which prohibits any person from obtaining money or property 'by means of any untrue statement of a material fact or any omission to state a material fact,' is devoid of any suggestion whatsoever of a scienter requirement.").

found this textual interpretation persuasive and concluded that scienter is not required for a violation of section 44-1991(2).[19]

*Gunnison* did not interpret subsection (3) of Arizona Revised Statutes section 44-1991, but because the language of subsection (3) is nearly identical under both sections 17(a) and 44-1991(A), it is reasonable, especially given the 1996 statement of intent, to look to *Aaron*'s interpretation of section 17(a)(3). Under subsection (3), *Aaron* holds that scienter is not required.[20] Subsection (3) looks to whether the investor would be misled. The defendant's intent is irrelevant. The Court explained:

> [T]he language of [section] 17(a)(3), under which it is unlawful for any person "to engage in any transaction, practice, or course of business which *operates* or *would operate* as a fraud or deceit," . . . quite plainly focuses upon the *effect* of particular conduct on members of the investing public, rather than upon the culpability of the person responsible.[21]

This is a logical way to read parallel language in section 44-1991(A)(3).[22]

Finally, securities law interpretations by the Arizona Corporation Commission ("ACC") are entitled to "great deference."[23] Decisions by the ACC hold that scienter is not required for violations of subsection (3).[24]

In sum, the language of section 44-1991(A)(3), legislative intent, analogous federal interpretation, and deference to administrative precedent support the conclusion that scienter is not required for a subsection (3) violation. This is a departure from federal law under rule 10b-5, which has required scienter since the 1976 *Hochfelder* decision.[25] But by analyzing section 44-1991(A)(3) through the lens of statutory interpretation, it can be seen that scienter is not an element of a subsection (3) claim.

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19. *Gunnison*, 618 P.2d at 607.

20. *Aaron*, 446 U.S. at 697.

21. *Id.* at 696–97 (emphasis in original).

22. *See* Orthologic Corp. v. Columbia/HCA Healthcare Corp., No. CIV 01-0006, 2002 WL 1331735, at *5 (D. Ariz. Jan. 7, 2002) ("Because the language of [section] 17(a) of the 1933 Act and [section] 1991 of the Arizona Securities Act are identical in all relevant respects and because the Arizona Supreme Court has acknowledged its concurrence with the United States Supreme Court's interpretation of section 17(a), this court finds that proof of scienter is required to succeed on a claim under [section] 1991(A)(1), but not under [section] 1991(A)(2) or [section] 1991(A)(3).").

23. Eastern Vanguard Forex, Ltd. v. Ariz. Corp. Comm'n, 79 P.3d 86, 97 (Ariz. Ct. App. 2003).

24. *See In re* Nutek Info. Sys., Inc., No. S-3046-I, 1996 WL 494745 (Ariz. Corp. Comm'n Aug. 22, 1996) ("Scienter is not an element of a violation of A.R.S. §§ 44-1991(2) or 44-1991(3)."). *In re* Lost Dutchman Invs., Inc., No. S-2299-I, 1993 WL 173726, at *13 (Ariz. Corp. Comm'n Apr. 8, 1993) (same).

25. *See* Ernst & Ernst v. Hochfelder, 425 U.S. 185, 191–94 (1976).

## II. STATEMENTS OF LEGISLATIVE INTENT

### *A. The 1951 Statement of Intent*

As mentioned, two statements of legislative intent have been enacted by the Arizona legislature. The first was enacted with the 1951 Securities Act. It directs the courts to avoid narrow interpretations in favor of liberal constructions that advance the Act's remedial goals:

> Sec. 20. INTENT AND CONSTRUCTION. The intent and purpose of this Act is for the protection of the public, the preservation of fair and equitable business practices, the suppression of fraudulent or deceptive practices in the sale or purchase of securities, and the prosecution of persons engaged in fraudulent or deceptive practices in the sale or purchase of securities. This Act shall not be given a narrow or restricted interpretation or construction, but shall be liberally construed as a remedial measure in order not to defeat the purpose thereof.[26]

Three points are made in this legislative statement:

- The securities laws are intended to deter fraud and protect the public.
- Narrow interpretations are to be avoided.
- The Act is to be liberally construed.

Each point is a useful guidepost in understanding how Arizona's securities laws should be interpreted.

The 1951 statement of intent has been quoted in three decisions by the Court of Appeals. In each decision, the Court of Appeals departed from federal law in favor of a broad reading that promoted public protection.[27] The initial decision was the 2001 decision in *Siporin v. Carrington*.[28] *Siporin* refused to follow federal precedent on the treatment of viatical

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26. Securities Act of Arizona, ch. 18, § 20, 1951 Ariz. Sess. Laws 46, 75.

27. The 1951 statement of intent has also been advanced by the ACC as a reason to explain why civil liability under Arizona's securities laws is broader than under federal securities law. *See, e.g.*, *In re* Woodington Group, Inc., No. S-2798-I, 1992 WL 409822, at *6 (Ariz. Corp. Comm'n Dec. 10, 1992) ("Because state securities laws should be more broadly construed than federal securities laws, and because of our legislative mandate, this Commission must broadly interpret the Act as a remedial measure to ensure the protection of Arizona investors.").

28. 23 P.3d 92 (Ariz. Ct. App. 2001).

settlements[29] as investment contracts under the statutory definition of securities.[30] At the time the major appellate decision on viatical settlements was one by the District of Columbia Circuit in *SEC v. Life Partners, Inc.*[31] *Life Partners* held that the viatical settlement agreements before it were not securities.[32] In *Siporin*, the defendants relied upon *Life Partners* to obtain summary judgment dismissing the plaintiff's securities law claims.[33] *Siporin* acknowledged that Arizona courts often look to federal decisions on the meaning of a security, but it declined to follow *Life Partners*.[34] It quoted the 1951 statement of intent and explained that it would "not defer to federal case law, when by doing so, we would be taking a position inconsistent with the policies embraced by our own legislature."[35] It reasoned that federal securities law should not be followed when it does not adequately protect the public: "We will depart from those federal decisions that do not advance the Arizona policy of protecting the public from unscrupulous investment promoters."[36]

The Court of Appeals found that *Life Partners* fell "squarely within this category" because it adopted a rigid definition of statutory investment contracts that contravened the Arizona legislature's directive to avoid narrow interpretations of our state's securities laws.[37]

The second decision was the 2003 decision in *Eastern Vanguard Forex, Ltd. v. Arizona Corp. Commission*.[38] *Eastern Vanguard* concerned controlling-person liability under Arizona Revised Statute section 44-

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29. By statute, "'viatical or life settlement contract' means an agreement for consideration for the purchase, assignment, transfer, sale, devise or bequest of any portion of the death benefit under or ownership of either an insurance policy or certificate of insurance." ARIZ. REV. STAT. ANN. § 44-1801(29) (2008). Multiple exceptions to the definition exist. *Id.* § 44-1801(29)(a)–(d).

30. Investment contracts are listed as securities under Arizona Revised Statutes section 44-1801(26). In addition to *Siporin*, leading Arizona cases on investment contracts include *Daggett v. Jackie Fine Arts, Inc.*, 733 P.2d 1142 (Ariz. Ct. App. 1986), *Nutek Info. System., Inc. v. Ariz. Corp. Comm'n*, 977 P.2d 826 (Ariz. Ct. App. 1998), and *Vairo v. Clayden*, 734 P.2d 110 (Ariz. Ct. App. 1987).

31. 87 F.3d 536 (D.C. Cir. 1996).

32. *Id.* at 547–48.

33. *Siporin*, 23 P.3d at 99 ¶ 37.

34. *Id.* at 98 ¶ 28.

35. *Id.*

36. *Id.*

37. *Id.* at ¶¶ 28–29. In 2000, the legislature amended Arizona Revised Statute section 44-1801(29) to include "viatical or life settlement investment contract[s]" as securities. *See* Trade and Commerce–Securities, ch. 108, § 2, 2000 Ariz. Sess. Laws 539 (codified at ARIZ. REV. STAT. ANN. § 44-1801(29) (2008)). The legislature also included a statutory definition of "viatical settlement investment contracts." *Id.*

38. 79 P.3d 86 (Ariz. Ct. App. 2003).

1999,[39] a statute modeled on section 15 of the Securities Act of 1933[40] and section 20(a) of the Securities Act of 1934.[41] Section 44-1999 imposes joint and several liability on actors who control persons who violate the securities laws.[42] The issue in *Eastern Vanguard* was whether control liability requires a showing that the control person participated in the controlled person's underlying securities violation. Some case law in the Ninth Circuit suggests this interpretation.[43] The alleged control persons in *Eastern Vanguard* relied upon this authority. In response, the ACC contended that an actual-participation test did not adequately protect the public.[44] The Court of Appeals agreed.[45] As an initial matter, it observed that actual participation is not required by the language of section 44-1999.[46] Second, it reasoned that requiring actual participation thwarts the purpose behind the creation of

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39. Section 44-1999 (2008) provides:

> A. Every person who, by or through stock ownership, agency or otherwise or who pursuant to or in connection with an agreement or understanding with one or more other persons by or through stock ownership, agency or otherwise controls any person liable under this article, other than section 44-1991 or 44-1992, is liable jointly and severally with and to the same extent as the controlled person to any person to whom the controlled person is liable, unless the controlling person had no knowledge of or reasonable grounds to believe in the existence of the facts by reason of which the liability of the controlled person is alleged to exist.
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> B. Every person who, directly or indirectly, controls any person liable for a violation of section 44-1991 or 44-1992 is liable jointly and severally with and to the same extent as the controlled person to any person to whom the controlled person is liable unless the controlling person acted in good faith and did not directly or indirectly induce the act underlying the action.

40. 15 U.S.C. § 77o (2006).

41. *Id.* § 78t(a).

42. For further discussion of Arizona Revised Statutes section 44-1999, see Richard G. Himelrick, *Arizona Securities Fraud Liability: Charting a Non-Federal Path*, 32 ARIZ. ST. L.J. 203, 226–28 (2000) and *infra* notes 155–62 and accompanying text.

43. *See Eastern Vanguard Forex*, 79 P.3d at 98 ¶ 40 (citing Paracor Fin., Inc. v. Gen. Elec. Capital Corp., 96 F.3d 1151, 1162 (9th Cir. 1996) (holding that CEO was not liable for alleged misrepresentations and omissions about company's sales because investors' evidence of CEO's involvement in misrepresentations was virtually nonexistent)); Burgess v. Premier Corp., 727 F.2d 826, 832 (9th Cir. 1984) (holding that director who was not involved in company's day-to-day operations and who had nothing to do with the preparation of the prospectuses at issue could not be liable as a controlling person). More recent Ninth Circuit cases hold that the plaintiff need not prove actual participation. *See, e.g.*, Howard v. Everex Sys., Inc., 228 F.3d 1057, 1065 (9th Cir. 2000) ("[I]n order to make out a prima facie case, it is not necessary to show actual participation or the exercise of actual power; however, a defendant is entitled to a good faith defense if he can show no scienter and an effective lack of participation.").

44. *East Vanguard Forex*, 79 P.2d at 98 ¶ 41.

45. *Id.*

46. *Id.* at 99 ¶ 41.

controlling-person liability.[47] That purpose was to hold accountable those actors with the authority to control securities violators but who could not be held legally responsible under existing law.[48] Third, it found interpretative guidance in the 1951 statement of intent.[49] It found an actual-participation requirement too restrictive to protect the public.[50] It reasoned that the remedial goal expressed in the statement of intent is best achieved by "imposing presumptive control liability on persons who have the *power* to directly or indirectly control the activities of those persons or entities liable as primary violators of sections 44-1991 and -1992."[51] It therefore declined to follow the Ninth Circuit's actual-participation cases.[52]

The third decision is the 2006 decision in *Grand v. Nacchio*.[53] *Grand* involved a variety of issues concerning statutory requirements for rescission, loss causation, and tender of the securities for which rescission is sought. Grand[54] sought statutory rescission under Arizona Revised Statutes section 44-2001(A), which requires that the plaintiff tender the securities to the defendant as a condition to rescission.[55] Grand had sold his stock and was therefore unable to tender it.[56] He argued that publicly traded stock is fungible and that he should be able to satisfy the tender requirement by tendering replacement shares.[57] The ability to tender the shares and obtain rescission (rather than damages) was important because loss causation is not required for rescission under subsections (1) and (3) of Arizona Revised Statutes section 44-1991(A).[58]

The Court of Appeals agreed with Grand's position on substitute tender and relied upon the 1951 statement of intent to support its decision.[59] It reasoned that a requirement of strict tender under which the identical shares

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47. *Id.*
48. *Id.*
49. *Id.* at 97 ¶ 36.
50. *Id.* at 98 ¶ 41.
51. *Id.* at 99 ¶ 42 (emphasis in the original).
52. *Id.* at 98 ¶¶ 40–41.
53. 147 P.3d 763 (Ariz. Ct. App. 2006).
54. The plaintiffs were Richard and Marcia Grand, trustees of the R.M. Grand Revocable Living Trust. *Id.* at 767 ¶ 1.
55. *See infra* note 98 (quoting ARIZ. REV. STAT. ANN. § 44-2001(A) (2008)).
56. *Grand*, 147 P.3d at 775 ¶ 37.
57. *Id.* at 775–76 ¶¶ 39–40.
58. *Id.* at 778–79 ¶¶ 49–51. "Loss causation is nothing more than proximate cause–'the allegedly unlawful conduct [that] caused the economic harm.'" *Id.* at 773 ¶ 30 (quoting AUSA Life Ins. Co. v. Ernst & Young, 206 F.3d 202, 209 (2d Cir. 2000)); *see also* Standard Chartered, PLC v. Price Waterhouse, 945 P.2d 317, 343–44 (Ariz. Ct. App. 1996) (explaining loss causation). Inability to prove loss causation is often fatal to the plaintiff's claim. In fact, Grand lost on this ground in the trial court. *See Grand*, 147 P.3d at 768 ¶¶ 8–9.
59. *Grand*, 147 P.3d at 777 ¶ 45.

must be tendered does not further public protection.[60] On the other hand, permitting tender of equivalent shares recognizes the economic realities of equity securities as fungible items and is true to the legislative directive mandating that the state's securities law be liberally interpreted.[61]

### *B. The 1996 Statement of Intent*

A second statement of legislative intent accompanied amendments in 1996 to the Arizona Securities Act. It provides: "[T]he courts may use as a guide the interpretations given by the securities and exchange commission and the federal or other courts in construing substantially similar provisions in the federal securities laws of the United States."[62] This provision was quoted in *Eastern Vanguard* for the proposition that "we may look to federal court decisions for interpretative guidance."[63]

*Eastern Vanguard*, *Siporin*, and *Grand*—each of which found federal law too restrictive to guard the public—show that Arizona's securities laws are broader than their federal counterparts. But rule 10b-5 cases continue to influence Arizona courts,[64] and the 1996 statement of intent shows that it is proper to look to these federal decisions (as well as SEC precedent) to interpret "substantially similar provisions in the federal securities laws."[65]

### *C. Proper use of Federal Precedent*

When read together, the 1951 and 1996 statements of intent clarify the proper use of federal precedent. They show that two conditions must exist for federal case law to have precedential value under Arizona's securities statutes. First, the federal precedent must interpret a federal statute with

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60. *Id.* at 778 ¶ 47.

61. *Id.* at 777–78 ¶ 46–47.

62. Sales of Securities–Litigation–Fraud, Unlawful Activity, Etc., ch. 197, sec. 11(C), § 44-2126, 1996 Ariz. Legis. Serv. 1168, 1189 (West).

63. Eastern Vanguard Forex, Ltd. v. Ariz. Corp. Comm'n, 79 P.3d 86, 97 ¶ 36 (Ariz. Ct. App. 2003).

64. *See, e.g.*, Nutek Info. Sys., Inc. v. Ariz. Corp. Comm'n, 977 P.2d 826, 830 ¶ 16 (Ariz. Ct. App. 1998) (finding that the statutory definition of security under Arizona law was substantially similar to the definition under federal law and stating that, "Arizona courts therefore look to federal courts for guidance in interpreting the statutes"); Vairo v. Clayden, 734 P.2d 110, 114 (Ariz. Ct. App. 1987) ("Arizona courts look to federal law for guidance in interpreting its securities law.").

65. The 1996 statement of intent refers to decisions by "federal or other courts." *See* Sales of Securities–Litigation–Fraud, Unlawful Activity, Etc., ch. 197, sec. 11(C), § 44-2126, 1996 Ariz. Legis. Serv. 1168, 1189 (West). The reference to "other courts" allows use of state court decisions interpreting the federal securities laws.

language substantially similar to the text of the Arizona statute.[66] Second, the federal interpretation must be one that advances the Arizona policy of public protection.[67] Unless both requirements of substantial similarity and public protection are met, reliance on federal precedent is misplaced.

## III. ADMINISTRATIVE PRECEDENT

Statutory interpretations by administrative agencies like the ACC are often afforded judicial deference.[68] If the statute is one the agency is entrusted to enforce, the agency's interpretation is commonly given considerable weight.[69]

Justice Jackson's opinion in *Skidmore v. Swift & Co.* is often quoted as the rationale for relying upon nonbinding-agency interpretations.[70] His opinion focused upon the experience and expertise of the agency responsible for administering the statute:

> We consider that the rulings, interpretations and opinions of the Administrator under this Act, while not controlling upon the courts by reason of their authority, do constitute a body of experience and informed judgment to which courts and litigants may properly resort for guidance. The weight of such a judgment in a particular case will depend upon the thoroughness evident in its

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66. *See id.* (quoting the 1996 statement of intent).

67. *See, e.g.*, Siporin v. Carrington, 23 P.3d 92, 98 ¶ 28 (Ariz. Ct. App. 2001) (using the 1951 statement to explain the court's refusal to follow federal decisions that would reduce public protection).

68. *See, e.g.*, Jenney v. Ariz. Express, Inc., 362 P.2d 664, 667 (Ariz. 1961) (deferring to the ACC's interpretation of a nonsecurities statute and stating that "although we are not bound by the administrative interpretation, where any serious doubt as to the proper interpretation exists we will not adopt one different from that adopted by the appropriate administrative body"); Donna M. Nagy, *Judicial Reliance on Regulatory Interpretations in SEC No-Action Letters: Current Problems and a Proposed Framework*, 83 CORNELL L. REV. 921, 928 (1998) (arguing "that while courts are never required to defer automatically to regulatory interpretations in no-action letters, courts should nonetheless treat no-action letters as informal and unofficial authority, and may rely on regulatory interpretations in the letters to the extent that they are persuasive").

69. *See, e.g.*, Eastern Vanguard Forex, Ltd. v. Ariz. Corp. Comm'n, 79 P.3d 86, 97 ¶ 35 (Ariz. Ct. App. 2003) (stating as to the ACC's interpretation of the securities laws that "even though we resolve questions of law involving statutory construction de novo, we give great deference to the agency's interpretation and application of the statute"); Walgreen Ariz. Drug Co. v. Ariz. Dept. of Revenue, 97 P.3d 896, 898 ¶ 12 (Ariz. Ct. App. 2004) ("We also recognize that an agency's interpretation of a statute that it implements is entitled to great weight.").

70. *See generally* Kristin E. Hickman & Matthew D. Krueger, *In Search of the Modern* Skidmore *Standard*, 107 COLUM. L. REV. 1235 (2007) (analyzing the *Skidmore* standard of judicial review under what the authors describe as the revitalized, modern standard that began in 2001).

> consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking power to control.[71]

Although *Skidmore* has not been explicitly followed in Arizona, *Skidmore*'s recognition of the experience and expertise of administrative agency is implicit in the deference Arizona courts give to administrative agencies.[72] A 2003 decision by the Court of Appeals acknowledged the importance of the ACC's administrative precedent.[73] The decision holds that the ACC's interpretation of the securities statutes is entitled to "great deference."[74] It said: "[E]ven though we resolve questions of law involving statutory construction de novo, we give great deference to the agency's interpretation and application of the statute."[75]

This deference is reasonable. The ACC's Securities Division has technical expertise in the financial issues common to securities litigation, as well as a history of applying the securities laws through which it has come to understand the practical implications of how these laws are best applied. There is also something to be said for promoting legal uniformity by harmonizing judicial interpretations with administrative interpretations. Under *Skidmore*'s power-to-persuade standard, these factors are appropriately taken into account by the courts when they consider the ACC's securities-law interpretations.[76]

## IV. RECURRING ISSUES

### *A. Unauthorized Trading*

Arizona and federal securities law differ on liability for unauthorized trading. A line of federal cases holds that unauthorized trading by itself is

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71. Skidmore v. Swift, 323 U.S. 134, 140 (1944).

72. *See, e.g.*, City of Phoenix v. Super. Ct., 514 P.2d 454, 457 (Ariz. 1973) (noting the importance of the agency staff's technical expertise). *See generally* Note, *The Two Faces of Chevron*, 120 HARV. L. REV. 1562, 1563 (2007) (arguing that the federal courts of appeals "have come to rely on agency expertise in more contexts, and more heavily, in deciding the degree of deference to provide to agency interpretations than the Supreme Court does").

73. *Eastern Vanguard Forex*, 79 P.3d at 97 ¶ 35.

74. *Id.*

75. *Id.*

76. *See* Hickman & Krueger, *supra* note 70, at 1258–59 (discussing the rationale used by courts in applying *Skidmore* deference and listing as factors (1) the thoroughness evident in the agency's interpretation, (2) the formality of the decision, (3) the validity of the reasoning, (4) its consistency with other interpretations by the agency, and (5) the agency's expertise).

not a rule 10b-5 violation.[77] These cases typically reason that unauthorized trading without misrepresentations or some other fraud does not involve the deception or scienter needed for a rule 10b-5 violation.[78] In Arizona, *Washington National Corp. v. Thomas*, a 1977 decision, suggests that unauthorized trading may violate Arizona Revised Statutes section 44-1991(A).[79] In that case the court awarded damages for the value of the stock plus capital gains taxes arising out of a broker's unauthorized stock sale.[80] Liability was based on section 44-1991.[81] But the basis for the statutory violation is unclear. In part the court relied upon the broker's violation of the customers' instructions not to sell the stock.[82] But the opinion also discusses misrepresentations concerning the manner in which the customers were induced to give up control of the stock by placing it in a discretionary trust.[83] A more reasoned analysis of unauthorized trading could have been based on statutory interpretation.

First, the language of section 44-1991(A), particularly subsection (3), is broad enough to cover unauthorized trading. Buying or selling securities without authority can reasonably be interpreted as a "transaction" or "practice" that operates as a fraud on the customer.

Second, the 1951 statement of intent instructs courts to avoid narrow interpretations in favor of liberal readings that foster public protection. Reading section 44-1991(A) to cover unauthorized trading fosters the legislature's goals and intent. Why would a reasonable legislator, acting

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77. *See, e.g.*, Brophy v. Redivo, 725 F.2d 1218, 1221 (9th Cir. 1984); Shamsi v. Dean Witter Reynolds, Inc., 743 F. Supp. 87 (D. Mass. 1989); Pross v. Baird, Patrick & Co., Inc., 585 F. Supp. 1456, 1460 (S.D.N.Y. 1984). The efficacy of these decisions was diminished by *SEC v. Zandford*, 535 U.S. 813 (2002). *Zandford* held that a broker's conduct in selling his customer's securities with the undisclosed intent of misappropriating the proceeds could constitute fraud under rule 10b-5. *Id.* at 825.

78. *See, e.g.*, *Brophy*, 725 F.2d at 1221 ("The mere fact that defendant Redivo must have acted intentionally—i.e., consciously—while making the unauthorized trades is not sufficient to show scienter."); *Pross*, 585 F. Supp. at 1460 (holding that the defendant's unauthorized trades did "not involve the element of deception necessary to be violative of Rule 10b-5").

79. 570 P.2d 1268, 1275 (Ariz. Ct. App. 1977).

80. *See id.* at 1275–76 (holding that the unauthorized sale was voidable under Arizona Revised Statutes section 44-2002 (now section 44-2002(A)) and that plaintiffs' damages included the loss of the stock and the taxes paid on capital gain).

81. *Id.* at 1274–76.

82. *See id.* at 1272–73 (describing the salesman's conduct in selling stock he had been instructed not to sell).

83. *See id.* at 1274–75.

with the intent described in the 1951 statement, want to exempt unauthorized trading from the general antifraud statute?[84]

Third, decisions by the ACC have consistently interpreted section 44-1991 to prohibit unauthorized trading. For example, *In the Matter of Merrill*, a 2003 ACC decision, held that a broker violated section 44-1991 by engaging in an unauthorized trade and by failing to disclose the unauthorized trade after it occurred.[85] As already explained, the Court of Appeals has held that agency interpretations like this are entitled to "great deference."[86]

Fourth, by administrative rule the ACC has defined unauthorized trading as a "dishonest and unethical practice."[87] In Arizona Revised Statutes sections 44-1991(B) and 44-2082(E), the legislature used the ACC's definition of "dishonest and unethical practices" to identify those types of securities violations for which loss causation is not required.[88] In short, dishonest and unethical practices, which include unauthorized trading, are among the acts that may violate section 44-1991(A). Thus, we again have an administrative interpretation—this time by agency rule—that treats unauthorized trading as a violation of section 44-1991(A).

In summary, interpretation based upon the statute's text, legislative intent, and administrative interpretations leads to a reasoned conclusion that unauthorized trading violates section 44-1991(A).

### *B. Reliance*

Reliance is a common-law concept that is a necessary element of an action for common-law fraud.[89] The federal courts have followed the

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84. *Cf.* STEPHEN BREYER, ACTIVE LIBERTY: INTERPRETING OUR DEMOCRATIC CONSTITUTION 88 (2005) (reasoning that statutes should be analyzed on the basis of what a reasonable legislator would have done if the legislator had thought about the problem).

85. No. S-03450A, 2003 WL 23156709, at *14 (Ariz. Corp. Comm'n Dec. 9, 2003); *see also In re* Brown, No. S-3036-I, 1995 WL 225211, at *3 (Ariz. Corp. Comm'n Apr. 5, 1995) (holding that broker violated section 44-1991 by engaging in unauthorized trading and also by failing to disclose that she intended to engage in unauthorized trading); *In re* Schneider Sec., Inc., No. S-3062-I, 1996 WL 776997, at *4 (Ariz. Corp. Comm'n Dec. 18, 1996) (finding that unauthorized trades violated section 44-1991 and citing the language of subsections (1) and (3) of the statute).

86. Eastern Vanguard Forex, Ltd. v. Ariz. Corp. Comm'n, 79 P.3d 86, 97 ¶ 35 (Ariz. Ct. App. 2003).

87. ARIZ. ADMIN. CODE § R14-4-130(A)(6) (2007).

88. Himelrick, *supra* note 42, at 215–16.

89. *See, e.g.*, Echols v. Beauty Built Homes, Inc., 647 P.2d 629, 631 (Ariz. 1982) (affirming summary judgment as to certain plaintiffs on fraud claims because no evidence of reliance existed); Wilson v. Byrd, 288 P.2d 1079, 1082 (Ariz. 1955) (holding that buyers could not recover for fraud because they had no right to rely upon the alleged misrepresentations).

common law and read a reliance requirement into rule 10b-5.[90] This can be a significant hurdle for plaintiffs who seek to sue fraud participants with whom the plaintiff had no contact. As the Enron litigation illustrates, law firms, accountants, and investment banks may be deeply entrenched in a securities fraud.[91] But if the plaintiff cannot show reliance on each fraud participant's conduct, claims against those actors with whom the plaintiff had no direct contact will often fail.[92]

Arizona's courts have held that reliance is not an element of the plaintiff's proof in actions under Arizona Revised Statutes section 44-1991(A). The clearest precedent is the 1986 Court of Appeals decision in *Rose v. Dobras*.[93] *Rose* held that reliance is not required under section 44-1991 and made the point that actions under Arizona's securities laws do not require all of the elements of a claim under rule 10b-5.[94] But *Rose* did not reach its conclusion on the basis of statutory interpretation. Instead, it supported its holding with citations to rule 10b-5 cases—a strange approach because reliance is required under rule 10b-5. A clear explanation of why reliance is not an element of an action under section 44-1991 could have been based on statutory language and legislative purpose.

As explained in *Aaron v. Fromkin*, "[t]he elements of securities fraud are articulated within the statute itself."[95] If we look to the statute's text, nothing in the language of section 44-1991(A) speaks of reliance.[96] Why, then, should the courts read a reliance requirement into the statute that the legislature did not include?[97]

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90. Louis Loss, *The Assault on Securities Act Section 12(2)*, 105 HARV. L. REV. 908, 910 (1992) ("In the common law tradition, the courts have read into rule 10b-5 not only scienter, but also the additional elements of justifiable reliance and causation.").

91. *See generally In re* Enron Corp. Sec., Derivative & ERISA Litig., 235 F. Supp. 2d 549 (S.D. Tex. 2002) (deciding issues arising out of securities-law claims against law firms, accounting firms, and investment banks).

92. *See, e.g.*, Stoneridge Inv. Partners v. Scientific-Atlanta, Inc., 128 S.Ct. 761, 774 (2008) (affirming dismissal of claims against customers and suppliers in alleged revenue scheme because investors did not rely upon any statements or representations by these defendants).

93. 624 P.2d 887, 892 (Ariz. Ct. App. 1981); *see also* Trimble v. Am. Sav. Life Ins. Co., 733 P.2d 1131, 1135–36 (Ariz. Ct. App. 1986) (holding reliance unnecessary in a public enforcement action under section 44-1991 (now section 44-1991(A))).

94. *Rose*, 624 P.2d at 892.

95. Aaron v. Fromkin, 994 P.2d 1039, 1042 ¶ 13 (Ariz. Ct. App. 2000).

96. *See supra* note 9 (quoting ARIZ. REV. STAT. ANN. § 44-1991(A) (2008)).

97 *See genearlly* John C.P. Goldberg, Anthony J. Sebok & Benjamin C. Zipursky, *The Place of Reliance in Fraud*, 48 ARIZ. L. REV. 1001 (2006) (arguing that reliance is a distinct and essential element of common-law fraud but noting that there may be reasons to relax reliance requirements in actions under consumer-fraud and securities statutes); *cf. Bridge v. Phoenix Bond & Indem. Co.*, 128 S.Ct. 2131, 2142–43 (2008) (describing reliance as "a specialized condition that happens to have grown up with common law fraud" and refusing to read reliance into statutory actions for RICO damages predicated on mail fraud (quoting Anza v. Ideal Steel

The legislature dispensed with a reliance requirement and created a rescissionary remedy for violations of section 44-1991(A). The remedy is provided in section 44-2001(A), which allows an investor who proves a violation of 44-1991(A) to recover the consideration paid, less income received, upon tendering the securities that were purchased.[98] To trigger this right to statutory rescission, the "[p]laintiffs' burden of proof requires only that they demonstrate that the [defendant's] statements were material and misleading."[99] Adding reliance to the plaintiff's burden of proof imposes a requirement that is unsupported by the language of either section 44-1991(A) or 44-2001(A).

The statutory argument against reliance becomes even more cogent when one considers the purpose of Arizona's securities laws. As expressed in the 1951 statement of intent, that purpose is to deter fraud and protect the public.[100] Eliminating a reliance requirement advances this purpose. It also respects the integrity of language the legislature used and ensures that the statutory right to rescind is not narrowed through a common-law reliance requirement.[101]

### *C. Contributory Fault by Investors*

Behavioral research has shown that the typical investor is not a careful investor.[102] Investors tend to overestimate their investment abilities and to

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Supply Corp., 547 U.S. 451, 477 (2006) (Thomas, J., concurring in part and dissenting in part) (internal quotation marks omitted)).

98. Section 44-2001(A) (2008) provides:

> A sale or contract for sale of any securities to any purchaser in violation of section 44-1841 or 44-1842 or article 13 of this chapter is voidable at the election of the purchaser, and the purchaser may bring an action in a court of competent jurisdiction to recover the consideration paid for the securities, with interest, taxable court costs and reasonable attorney fees, less the amount of any income received by dividend or otherwise from ownership of the securities, on tender of the securities purchased or the contract made, or for damages if the purchaser no longer owns the securities.

99. *Aaron*, 994 P.2d at 1042 ¶ 15.

100. *See supra* notes 27–60 and accompanying text.

101. *See* Rose v. Dobras, 624 P.2d 887, 892 (Ariz. Ct. App. 1981) (holding that unlike common-law fraud, reliance is not required for a violation of section 44-1991 (now section 44-1991(A)).

102. *See, e.g.*, Stephen J. Choi & A.C. Pritchard, *Behavioral Economics and the SEC*, 56 STAN. L. REV. 1, 2 (2003) ("Not all investors are rational. Quite apart from the obvious examples of credulity in the face of the latest Ponzi scheme, there is no shortage of evidence that many investors' decisions are influenced by systematic biases that impair their abilities to maximize their investment returns. These biases are not merely isolated quirks, rather, they are consistent, deep-rooted, and systematic behavioral patterns." (footnote omitted)).

minimize the risk associated with their investments.[103] They commonly fail to read offering materials and other disclosure documents.[104] They rely much more on verbal assurances.[105] It is no surprise then that investors, even those who can be described as sophisticated through traits like education, business background, and investment experience, are behaviorally vulnerable to fraud.[106]

The securities laws recognize this vulnerability. They were enacted to deter fraud and protect the public.[107] As explained by the Arizona Court of Appeals, "The securities laws are designed to protect less-than-prudent investors from giving their money to irresponsible or unscrupulous businessmen."[108] Nothing in the language of the securities statutes imposes a duty of care on the part of investors. Nor is there anything in the text of the statutes that allows a defendant to use the plaintiff's negligence as a defense. On the contrary, the securities laws impose an affirmative duty not

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103. *See* David A. Hoffman, *The "Duty" to Be a Rational Shareholder*, 90 MINN. L. REV. 537, 555–56 (2006) (discussing the overconfidence bias in investor behavior); Robert Prentice, *Whither Securities Regulation? Some Behavioral Observations Regarding Proposals For Its Future*, 51 DUKE L.J. 1397, 1457–61 (2002) (same).

104. Donald C. Langevoort, *Selling Hope, Selling Risk: Some Lessons for Law from Behavioral Economics About Stockbrokers and Sophisticated Customers*, 84 CAL. L. REV. 627, 681–85 (1996) (explaining that investment relationships are based upon trust that causes investors to forego reading prospectuses and other disclosure materials); *cf.* Robert Prentice, *Contract-Based Defenses in Securities Fraud Litigation: A Behavioral Analysis*, 2003 U. ILL. L. REV. 337, 361 (2003) ("Typically it is simply not worth the commitment of time and mental energy for an investor to master all the details of a complex contract, especially when the seller's agent likely does not know its provisions herself and has no authority to alter them anyway." (footnotes omitted)).

105. *See, e.g.*, Hoffman, *supra* note 103, at 558 (explaining that "individuals consistently overvalue the importance of oral information"); Langevoort, *supra* note 104, at 683–84 ("Reading a prospectus after accepting the recommendation of a broker whom the customer is inclined to trust, then, is inconsistent with several phenomena: (1) the time-saving and responsibility-shifting reasons for using that broker in the first place, (2) the cognitive commitment to the broker as a credible source of recommendations, and (3) the preference for making the investment.").

106. *See, e.g.*, Prentice, *supra* note 103, at 1460 ("Educated people and professionals are generally just as subject to phenomena such as overoptimism and overconfidence as are unsophisticated investors." (footnotes omitted)).

107. *See supra* notes 26–61 and accompanying text.

108. Nutek Info. Sys., Inc. v. Ariz. Corp. Comm'n, 977 P.2d 826, 833 ¶ 27 (Ariz. Ct. App. 1998).

to mislead,[109] which cannot be overcome by proving the plaintiff's contributory negligence.[110]

These principles remain unchanged under the provisions on proportionate liability that were added to Arizona Revised Statutes section 44-2003 in 1996. In that year, the Arizona legislature enacted a modified version of the proportionate liability provisions of the Private Securities Litigation Reform Act of 1995 ("PSLRA").[111] Under the proportionate liability regime, only those defendants who knowingly or recklessly violate section 44-1991(A) are jointly and severally liable.[112] For those defendants whose violations are neither knowing nor reckless (i.e., negligent or strict liability violations),[113] the defendant's liability is based upon a complicated

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109. State v. Super. Ct., 599 P.2d 777, 784 (Ariz. 1979), *overruled in part on other grounds by* State v. Gunnison, 618 P.2d 604, 607 (Ariz. 1980); Aaron v. Fromkin, 994 P.2d 1039, 1042 ¶ 15 (Ariz. Ct. App. 2000); Trimble v. Am. Sav. Life Ins. Co., 733 P.2d 1131, 1136 (Ariz. Ct. App. 1986).

110. *See* Wash. Nat'l Corp. v. Thomas, 570 P.2d 1268, 1275 (Ariz. Ct. App. 1977); *see also* A.G. Edwards & Sons, Inc. v. McCullough, 764 F. Supp. 1365, 1370 (D. Ariz. 1991) (interpreting Arizona Revised Statutes section 44-1991 and holding that "[i]t is clear to the Court that contributory negligence is no defense to defendants' state [securities] law claim"), *rev'd on other grounds*, 967 F.2d 1401 (9th Cir. 1992).

111. Pub. L. No. 104-67, 109 Stat. 737 (codified in scattered sections of 15 U.S.C. and 18 U.S.C. § 1964(c) (2006)). *See* Laperriere v. Vesta Ins. Group, Inc., 526 F.3d 715, 719–21 (11th Cir. 2008) (describing the legislative background and the requirements for proportionate liability under the PSLRA).

112. *See* ARIZ. REV. STAT. ANN. § 44-2003(B) (2008); *see also* Richard M. Weinroth et al., *Reformation of the Arizona Securities Act: A Brief Summary*, ARIZ. ATT'Y, Aug.–Sept. 1996, at 25–26 (discussing Arizona's version of the proportionate liability statutes). Joint and several liability for reckless conduct is a major departure from federal law. Under the PSLRA, only those defendants who act knowingly are jointly and severally liable. In passing the PSLRA, Congress made it a point to eliminate joint and several liability for reckless conduct. *See Laperriere*, 526 F.3d at 728–29 (explaining that the PSLRA allows joint and several liability for knowing but not reckless violations); Donald C. Langevoort, *The Reform of Joint and Several Liability Under the Private Securities Litigation Reform Act of 1995: Proportionate Liability, Contribution Rights and Settlement Effects*, 51 BUS. LAW. 1157, 1162–66 (1996) (discussing the federal standard for joint and several liability and explaining that Congress wished to ensure that liability for reckless behavior was proportionate only).

113. Subject to a reasonable-case defense under Arizona Revised Statutes sections 44-2001(B) and -2002(B) (2008), liability under subsection (2) of Arizona Revised Statutes section 44-1991(A) is strict liability. *See Aaron*, 994 P.2d at 1042 ¶ 15 ("Plaintiffs' burden of proof requires only that they demonstrate that the statements were material and misleading."). This also is true under subsection (3) of the statute. As explained in Part I, *supra*, subsection (3) focuses on the effect the defendant's conduct has on investors. Liability follows regardless of the defendant's intent if the conduct operates as a fraud on the plaintiff. For further discussion of the reasonable-care defense, see generally Mark B. Barnes & Matthew R. St. Louis, *The Unreasonable Burden of Proving the Reasonable Care Defense Under the Uniform Securities Act*, 63 BUS. LAW. 1223 (2008).

set of rules on fault apportionment.[114] These rules provide for fault apportionment among defendants and nonparties who (1) violate section 44-1991(A)[115] and (2) whose violation caused or contributed to the plaintiff's loss.[116] Both requirements–a securities violation and causation–must be shown before fault can be allocated.[117] No provision exists for reducing the defendant's liability on the basis of the plaintiff's fault[118]–a result that advances the Arizona policy of public protection and tracks prior law rejecting contributory negligence as a defense.[119]

### *D. Participant Liability*

As discussed earlier, securities fraud may involve many parties besides the seller who passes title.[120] The drafters of the Securities Act were aware of this. Through what is now section 44-2003(A), the drafters defined potentially liable parties to include any person who "made, participated in

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114. *See* ARIZ. REV. STAT. ANN. § 44-2003(C)–(E).

115. *See id.* § 44-2003(D)(1) (requiring findings on whether each person alleged to be at fault committed a securities violation).

116. *See id.* § 44-2003(E) (requiring the fact finder to consider whether the conduct of the person claimed to be at fault caused or contributed to the plaintiff's loss).

117. *See* statutes cited *supra* notes 115–116.

118. In isolation, language in Arizona Revised Statutes section 44-2003(D) that refers to the fault of "any other person" suggests that a plaintiff's fault could be considered. But when read in its entirety, subsection (D) requires that that the person whose fault is considered must both cause or contribute to the plaintiff's loss and commit a securities violation:

> D.The court in a private action shall instruct the jury to answer special interrogatories, or if there is no jury, make findings, for each covered person and *any other person the parties claim to have caused or contributed to the loss incurred by the plaintiff*, including any person who has entered into a settlement with the plaintiff or plaintiffs, concerning each of the following:
>
> 1. Whether the person *committed a violation of this chapter*.
>
> 2. The percentage of responsibility of the person, measured as a percentage of the total fault of all persons who caused or contributed to the loss incurred by the plaintiff.
>
> 3. Whether the person knowingly committed a violation of this chapter.

ARIZ. REV. STAT. ANN. § 44-2003(D) (emphasis added). The securities-violation requirement points to a comparison of fault by persons other than the plaintiff. *Cf.* John C. Coffee, Jr., *Developments Under the Private Securities Litigation Reform Act of 1995: The Impact After Two Years*, SC53 ALI-ABA 395, 421 (1997) (suggesting that the PSLRA statute on proportionate liability "contemplates allocation of the loss only among the tortfeasors because it expressly requires the factfinder to determine first 'whether such person violated the securities laws.' Although the plaintiff could well be contributorily negligent, his negligence cannot alone amount to a legal violation").

119. *See supra* note 107–110 and accompanying text.

120. *See supra* notes 42–45, 91 and accompanying text.

or induced" a sale or purchase that violates Arizona Revised Statutes section 44-1991(A).[121]

The range of potentially culpable participants is illustrated by the cases decided under section 44-2003(A). These have included claims against a bank,[122] incorporators,[123] an auditor,[124] state regulators,[125] a mutual fund company,[126] a guarantor,[127] and a business broker.[128] These cases provide some indication of the line between culpable and nonculpable participation. They show, for example, that more is required than providing ordinary business services that facilitate what turns out to be a fraudulent securities sale.[129] Thus, a bank that provides funds that are used in securities fraud is

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121. ARIZ. REV. STAT. ANN. § 44-2003(A).

122. Little v. First Cal. Co., [1977–1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,226, at 92,561–62 (Oct. 17, 1977), *available at* 1977 WL 1055, at *8–9 (analyzing bank's liability under Arizona Revised Statutes section 44-2003 (now section 44-2003(A)) and denying summary judgment because of disputed facts).

123. Trump v. Badet, 327 P.2d 1001, 1003–04 (Ariz. 1958) (upholding judgment against incorporators who used an attorney to find investors for their company).

124. Standard Chartered PLC v. Price Waterhouse, 945 P.2d 317, 333–34 (Ariz. Ct. App. 1996) (holding on the facts shown at trial that an accounting firm was a collateral actor too remote from the securities transaction to be liable as a statutory participant or inducer).

125. State v. Super. Ct., 599 P.2d 777, 783–84 (Ariz. 1979), *overruled in part on other grounds by* State v. Gunnison, 618 P.2d 604 (Ariz. 1980) (upholding trial court's refusal to dismiss claims under Arizona Revised Statutes sections 44-1991 and 44-2003 (now sections 44-1991(A) and 44-2003(A)) against the ACC and its commissioners).

126. Wash. Nat'l Corp. v. Thomas, 570 P.2d 1268, 1274 (Ariz. Ct. App. 1977) (holding that mutual fund company whose agent made misrepresentations and sold plaintiff's stock in unauthorized trades was liable as a participant).

127. Orthologic Corp. v. Columbia/HCA Healthcare Corp., No. CIV 01-0006, 2002 WL 1331735, at *4 (D. Ariz. Jan. 7, 2002) (finding that plaintiff's claim of inducement under section 44-2003(A) was not adequately pled and holding that on repleading the plaintiff "must specify how [the guarantor] adopted the alleged omissions or misrepresentation made in the Stock Purchase Agreement").

128. Strom v. Black, 523 P.2d 1339, 1340–41 (Ariz. Ct. App. 1974) (affirming judgment against business broker and salesman who were found to have participated in and induced securities violations).

129. *See* Little v. First Cal. Co., [1977–1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,226, at 92,561–62 (Oct. 17, 1977), *available at* 1977 WL 1055, at *8 ("Plaintiffs must show more than the undisputed financial transaction to establish participation."). In one of the few discussions of participant liability under state law, Professor Branson identified blind-eye practices and false-appearance cases as examples of culpable participation. Douglas M. Branson, *Collateral Participant Liability Under State Securities Laws*, 19 PEPP. L. REV. 1027, 1036–37, 1059–62 (1992). Blind-eye practices involve conduct in which a collateral participant like an attorney, accountant, or appraiser turns a blind eye to what he or she knows is a disclosure or registration violation. *Id.* at 1036–37. False-appearance cases are those in which the participant helps the primary securities violator create a false appearance for an investment. *Id.* at 1060–61; *see also* Matthew J. Morrison, *Participant Liability Under Blue Sky Rescission Statutes: The Diminishing Importance of the Definition of a Statutory Seller*, 33 No. 2 SEC. REG. L.J. 1 (2005) (discussing participant-liability developments under state law).

not by the loan itself a culpable participant.[130] Nor is an auditor whose report is used as part of a securities transaction automatically liable because the report contains a misstatement.[131]

On the other hand, where the actor takes part in the sale through a commission or receipt of part of the sale proceeds, statutory participation is almost certain to be found.[132] But the statute also contemplates liability when the defendant does not share in the sale proceeds.[133] For example, case law suggests that participant liability will be found when the defendant knowingly takes part in the seller's fraud.[134] But where precisely should the line between culpable and nonculpable participation in fraud be drawn? Careful statutory interpretation clarifies the issue.

In this regard, section 44-2003(A) should be interpreted against the backdrop of the statement of legislative intent that accompanied its passage.[135] It should be read broadly without narrow interpretations so that section 44-1991(A), the statute it implements, achieves its purpose of deterring fraud and protecting the public.[136] But in cases where the statutory purpose is not advanced, there is no reason to find liability.[137] The postman

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130. *See Little*, 1977 WL 1055, at *8.

131. *See* Standard Chartered PLC v. Price Waterhouse, 945 P.2d 317, 333–34 (Ariz. Ct. App. 1996) (finding that auditor's role was too remote to support liability for either participation or inducement).

132. *See id.* at 332–33 (implying that an auditor would have been liable if it had financially participated in the sale).

133. *See* Trump v. Badet, 327 P.2d 1001, 1004 (Ariz. 1958) (interpreting Arizona Revised Statutes section 44-2003 (now section 44-2003(A)) to allow rescission even when the defendant receives none of the consideration from the securities sale).

134. *See Little*, 1977 WL 1055, at *8 (concluding that scienter is required for participant liability under section 44-2003 (now section 44-2003(A)) and upholding for trial participant-liability claims against a bank); Orthologic Corp. v. Columbia/HCA Healthcare Corp., No. CIV 01-0006, 2002 WL 1331735, at *4 (D. Ariz. Jan. 7, 2002) (suggesting that a guarantor would be liable under 44-2003(A) if the guarantor adopted specific omissions or misrepresentations in the agreement it guaranteed); *see also* Branson, *supra* note 129, at 1036–37, 1060–62 (discussing non-Arizona cases imposing participant liability on the basis of blind-eye and false-appearance conduct).

135. *See supra* note 27 (quoting the statement of legislative intent).

136. *See supra* note 27 (quoting the statement of legislative intent); *see also* Grand v. Nacchio, 147 P.3d 763, 777 ¶ 45 (Ariz. Ct. App. 2006) (referencing the importance of public protection and adopting a broad view of tender to ensure defrauded shareholders are able to obtain statutory rescission for securities fraud). *But see Standard Chartered*, 945 P.2d at 332 (failing to consider the legislature's statement of intent and stating that, "[W]e believe it better fits Arizona Revised Statutes section 44-2003 to give 'induce' the narrower and more active construction suggested by its synonyms 'persuade' and 'prevail'").

137. *Cf. Standard Chartered*, 945 P.2d at 333 (construing section 44-2003 (now section 44-2003(A)) and stating, "[W]e conclude that the legislature did not mean, by use of the word 'induce,' to stretch civil liability under the Security Act to collateral actors . . . remote from the

who mails a fraudulent letter is surely not a culpable participant; nor is the retailer who sells the paper on which misleading documents are printed;[138] nor is a title company that innocently provides escrow services in what turns out to be a fraudulent syndication.[139] In none of the examples would it promote public protection to treat the actor as a culpable participant.

But when imposing participant liability will deter fraud, the likelihood that the legislature intended liability increases. Thus, the first step in identifying culpable participation is to ask whether imposing liability will further the legislative purpose. If the answer is yes, analysis should then turn to whether finding culpability is consistent with the statutory scheme of which section 44-2003(A) is a part.[140]

Four parts of the legislative scheme are especially relevant. One is section 44-1991(A), which is the statute for whose violations section 44-2003(A) creates participant liability.[141] The second is the comparative fault provisions of section 44-2003, which allocate damages among securities violators who were at fault in the securities violation.[142] The third is the control liability provisions under section 44-1999.[143] The fourth is the last sentence of section 44-2003(A), which qualifies the scope of participant liability by creating a safe harbor for professionals who act solely in the course of their professional capacity.[144] When these provisions are read collectively, the line between culpable and nonculpable participation begins to emerge.

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transaction, who neither financially participate, nor promote or solicit the transaction, but merely provide information that contributes to a buyer or seller's decision to close the deal").

138. Woodward v. Metro Bank of Dallas, 522 F.2d 84, 96 (5th Cir. 1975) (interpreting rule 10b-5 and stating that, "[t]he postman who mails a fraudulent letter is not covered by the Act, nor is the company that manufactured the paper on which the violating documents are printed").

139. *Cf.* Burkons v. Ticor Title Ins. Co. of Cal., 813 P.2d 710, 718 (Ariz. 1991) (holding in a nonsecurities case that escrow agent has no duty to search for fraud, but if the agent is aware of facts that a reasonable escrow agent would recognize as evidence of fraud, a duty to disclose exists).

140. *Cf., e.g.*, KZPZ Broad., Inc. v. Black Canyon City Concerned Citizens, 13 P.3d 772, 777 ¶ 19 (Ariz. Ct. App. 2000) ("[W]e must examine the statutory scheme as a whole, to give effect to all the statutes involved."); Ruth Fisher Elementary Sch. Dist. v. Buckeye Union High Sch. Dist., 41 P.3d 645, 648 ¶ 12 (Ariz. Ct. App. 2002) (explaining that statutes that relate to the same subject or have the same general purpose, should be construed as one system even when the statutes were enacted at different times and do not refer to one another).

141. *See* ARIZ. REV. STAT. ANN. § 44-1991(A) (2008).

142. *See id.* § 44-2003(B)–(E) (2008).

143. *See id.* § 44-1999 (2008).

144. *Id.* § 44-2003(A). The final sentence of section 44-2003(A) provides that "[n]o person shall be deemed to have participated in any sale or purchase solely by reason of having acted in the ordinary course of that person's professional capacity in connection with that sale or purchase." *Id.*

Consider section 44-1991(A) first. It is the statute for which section 44-2003 imposes participant liability. Section 44-1991(A) makes it unlawful for a person, directly or indirectly, to make misleading statements or engage in other deceptive acts in connection with the purchase or a sale of a security.[145] It therefore seems reasonable to treat any person who takes part in an act of fraud prohibited by section 44-1991(A) as potentially liable under section 44-2003(A). Even so, it is not enough that the actor merely participate in the transaction out of which the fraud arises. That is why the postman, the retailer, and the title company in the earlier examples are not culpable. But when the defendant participates in fraudulent activity and does so with a culpable state of mind, liability should follow.[146]

To take an example, an attorney who prepares loan documents that happen to be used in what turns out to be a securities swindle seems unlikely to be a culpable participant by that conduct alone. But if the loan documents contain misrepresentations, the possibility of culpable participation becomes more likely. And if the lawyer acted knowingly or recklessly in drafting the misrepresentations, liability should exist. This follows from a second part of the statutory scheme, i.e., Arizona Revised Statutes section 44-2003(B).

Section 44-2003(B) provides for joint and several liability if a person knowingly or recklessly commits a violation of section 44-1991(A).[147] If this provision is to have meaning,[148] those persons who knowingly or recklessly participate in a fraudulent act should be found culpable. A lender, for example, who knowingly or recklessly writes misrepresentations into loan documents used in a securities sale has not only participated in a fraudulent sale but has done so with a state of mind that the legislature has

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145. *See id.* § 44-1991(A).

146. *See* Little v. First Cal. Co., [1977–1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,226, at 92,561–62 (Oct. 17, 1977), *available at* 1977 WL 1055, at *8 (citing Barnes v. Vozack, 540 P.2d 161, 165 (Ariz. 1975) for the rule that plaintiff "must show direct or indirect participation in specific act of fraud" and concluding that scienter rather than mere negligent participation is required for liability).

147. Section 44-2003(B) provides that "[a]ny covered person against whom a final judgment is entered in a private action is jointly and severally liable for damages only if the trier of fact determines that the covered person recklessly or knowingly committed a violation of this chapter."

148. All statutes within a legislative enactment should be given meaning. *See* Tanque Verde Unified Sch. Dist. No. 13 v. Bernini, 76 P.3d 874, 884 ¶ 32 (Ariz. Ct. App. 2003) ("[W]e may not construe statutes in a way that renders any portion superfluous, void, or insignificant."); State v. Heinze, 993 P.2d 1090, 1096 ¶ 27 (Ariz. Ct. App. 1999) ("A fundamental principle of statutory construction is to give each section meaning so that no part is rendered void, superfluous, contradictory or insignificant.").

found culpable enough to justify joint and several liability.[149] The same can be said of an attorney who continues to provide legal services after the attorney knows investor funds are being misused,[150] or of a real-estate agent who proceeds with a sale knowing that the buyer is financially unable to perform.[151] In each example, the actor has a culpable state of mind (knowledge or recklessness) that the legislature has defined as sufficient for joint and several liability.

This is not to say that only those actors who act knowingly or recklessly can be found liable as statutory participants. We have already seen that financially participating in a sale by taking a commission or sharing in the sale proceeds may lead to liability.[152] This is consistent with the legislative scheme of proportionate liability for those actors who violate the securities laws without acting knowingly or recklessly.[153] Proportionate liability allows the fact finder, whether judge or jury, to assess a percentage of the plaintiff's damages against those defendants who commit negligent or strict liability securities violations.[154]

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149. *Cf.* Wells Fargo Bank v. Ariz. Laborers, Teamsters and Cement Masons Local No. 395 Pension Trust Fund, 38 P.3d 12, 23–28 ¶¶ 31–57 (Ariz. 2002) (finding, in a non-securities case, triable claims of aiding and abetting fraud by bank that allegedly helped its customer conceal his financial troubles).

150. *Cf.* Riley v. Brazeau, 612 F. Supp. 674, 680 (D. Or. 1985) (upholding state securities-law claims against attorney who "participated in the development and implementation of the Alpha plan even though he knew or recklessly disregarded that Alpha was not investing plaintiffs' funds properly"); Ainslie v. Spolyar, 926 P.2d 822, 828 (Or. Ct. App. 1996) (holding under Oregon's participant-liability statute that an attorney who was deeply involved in events that led to improper use of investor money materially aided the issuer's securities violations).

151. *Cf.* Lombardo v. Albu, 14 P.3d 288, 291 ¶¶ 12–13 (Ariz. 2000) (holding in a nonsecurities case that the inability of a "buyer to perform goes to the heart of the transaction" and must be disclosed by the buyer and the buyer's real estate agent).

152. *See supra* note 132 and accompanying test.

153. *See supra* note 112 and accompanying text (discussing proportionate liability). The proportionate-liability statutes evidence the legislature's intent to hold proportionately liable those actors who negligently, or in violation of strict-liability statutes like subsections (2) and (3) of Arizona Revised Statutes section 44-1991(A), participate in a purchase or sale. ARIZ. REV. STAT. ANN. § 44-2003(C)–(E) (2008). The possibility of proportionate liability for less culpable defendants is also suggested by section 44-2001(B), which gives defendants a defense to negligent and strict liability violations of section 44-1991(A). *Id.* § 44-2001(B) (2008). Under section 44-2001(B), a defendant who violates section 44-1991(A) is not liable if the defendant "sustains the burden of proof that the person did not know and in the exercise of reasonable care could not have known of the untrue statement or misleading omission." *Id.* This defense seems unnecessary if only those defendants who act knowingly or recklessly are potentially liable. By its terms, the defense implies liability for defendants who cannot prove reasonable care. *See* Barnes & St. Louis, *supra* note 113, at 1224–25 (discussing the reasonable-care defense under the Uniform Securities Act).

154. *See* ARIZ. REV. STAT. ANN § 44-2003(B)–(E) (providing for the judge or jury to make findings that show the percentage of damages caused by defendants or nonparties who did not

A third part of the legislative scheme—control liability under section 44-1999[155]—also sheds light on the difference between culpable and nonculpable participation. Like participant liability under section 44-2003(A), control liability under section 44-1999 extends liability beyond the seller or other primary violator.[156] Section 44-1999 does this through the concept of statutory control, while section 44-2003(A) extends liability through the concept of participation.[157] Control liability holds responsible those persons with the ability to control the primary securities violator.[158] Arizona has adopted an expansive interpretation of control. In *Eastern Vanguard*, a 2003 decision, the Court of Appeals rejected arguments that the control person must actually participate in the underlying securities violation. It reasoned that an actual-participation requirement is "'too restrictive to guard the public interest as directed by our state legislature.'"[159] Instead, the court held that subject to statutory defenses of

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knowingly commit the securities violation). On the strict liability aspects of violations of Arizona Revised Statutes section 44-1991(A), see Garvin v. Greenbank, 856 F.2d 1392, 1398 (9th Cir. 1988) (holding under section 44-1991 (now section 44-1991(A)) that "[a] seller of securities is strictly liable for the misrepresentations or omissions he makes"); Rosier v. First Fin. Capital Corp., 889 P.2d 11, 15 (Ariz. Ct. App. 1994) ("A misrepresentation in the sale of securities, even an innocent one, can be a violation of the securities statute . . . ."); *see also* Aaron v. Fromkin, 994 P.2d 1039, 1042 ¶ 15 (Ariz. Ct. App. 2000) ("Plaintiffs' burden of proof requires only that they demonstrate that the statements were material and misleading."). But as suggested earlier, a finding of culpable participation, even on a proportionate basis, seems unreasonable if the statutory goals of public protection and deterring fraud are not furthered. *See supra* notes 137–40 and accompanying text.

155. *See supra* note 39 (quoting ARIZ. REV. STAT. ANN. § 44-1999 (2008)).

156. *See* Eastern Vanguard Forex, Ltd. v. Ariz. Corp. Comm'n, 79 P.3d 86, 97–98 ¶ 38 (Ariz. Ct. App. 2003) (explaining that liability based upon control was legislatively enacted because of the difficulty of proving primary liability through participation under traditional legal principles).

157. *Cf.* Trump v. Badet, 327 P.2d 1001, 1004 (Ariz. 1958) (interpreting section 44-2003 (now section 44-2003(A)) and explaining that a person who induces a sale in violation of former section 44-2003 may be liable even though the person received none of the consideration and was not a party to the sale); *see also* Branson, *supra* note 129, at 1055–56 (explaining that participant-liability statutes like the Arizona statute eliminate the need for expanded-seller tests like those adopted in some jurisdictions).

158. Control may arise in many ways. Among the persons potentially liable as controlling persons are officers, directors, dominant shareholders, creditors, and attorneys. *See* Loftus C. Carson, II, *The Liability of Controlling Persons Under the Federal Securities Acts*, 72 NOTRE DAME L. REV. 263, 307–43 (1997) (discussing the potential liability of these and other actors); *see also* Laperriere v. Vesta Ins. Group, Inc., 526 F.3d 715, 721–22 (11th Cir. 2008) (discussing federal law and explaining that "[t]he legislative purpose in enacting a control person provision was to prevent people and entities from using straw parties, subsidiaries, or other agents acting on their behalf to accomplish ends that would be forbidden directly by the securities laws").

159. *Eastern Vanguard Forex*, 79 P.3d at 98 ¶ 41.

reasonable care and good faith,[160] "the evidence need only show that the person targeted as a controlling person had the legal power, either individually or as part of a control group, to control the activities of the primary violator."[161]

This interpretation of control liability suggests two things about culpable participation under section 44-2003(A). The first concerns the interpretative approach that should inform judicial interpretations of participant liability. Sections 44-1999 and 44-2003(A) are companion statutes that are intended to protect the public by extending liability to actors beyond the immediate securities violator.[162] The broad view of public protection adopted in *Eastern Vanguard* should guide interpretation of both statutes. No reason exists to believe the goal of public protection should lead to narrower interpretations under one statute than the other. Second, if actual participation is not required for control liability, then those actors who culpably participate in the primary violator's wrongdoing should be liable under the concept of participant liability created by section 44-2003(A).[163] In this way, the range of extended liability under sections 44-1999 and 44-2003(A) is harmonized so that the statutes supplement one another. Section 44-1999 will operate to hold responsible those actors with the power to control securities violators. And section 44-2003(A) will hold accountable those actors who, regardless of their ability to control the violator, culpably participate in the securities violation.[164]

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160. Under subsection (A) of Arizona Revised Statutes section 44-1999, the control person may assert as a defense that he "had no knowledge of or reasonable grounds to believe in the existence of the facts by reason of which the liability of the controlled person is alleged to exist." ARIZ. REV. STAT. ANN. § 44-1999(A). Under subsection (B) of the statute the control person may defend by showing that he "acted in good faith and did not directly or indirectly induce the act underlying the action." *Id.* § 44-1999(B)/=.

161. *Eastern Vanguard Forex*, 79 P.3d at 99 ¶ 42.

162. *Cf. Laperriere*, 526 F.3d at 725 (explaining that control liability under the Securities Exchange Act of 1934 "was intended to supplement, not to supplant the common law theory of *respondeat superior* as a basis for vicarious liability under the Act . . . ").

163. *See Eastern Vanguard Forex*, 79 P.3d at 96–97 ¶ 38 (explaining that control liability was legislatively enacted to supplement traditional legal principles imposing primary liability for direct participation). For examples of cases applying section 44-2003 (now section 44-2003(A)) to those who participate in fraudulent acts, see Little v. First Cal. Co., [1977–1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,226, at 92,561–62 (Oct. 17, 1977), *available at* 1977 WL 1055, at *8 (holding that direct or indirect participation by a bank in an act of fraud could create liability under section 44-2003 (now section 44-2003(A)); Strom v. Black, 523 P.2d 1339, 1341–42 (Ariz. Ct. App. 1974) (affirming judgment against business broker who prepared misleading advertising on the basis that the broker was a statutory participant and inducer under section 44-2003 (now section 44-2003(A)).

164. Section 44-1991(A) is in part a strict liability statute. *See* discussion *supra* note 113. It is therefore possible that unintentional, even non-negligent, participatory acts may lead to liability. For example, a defendant who receives a commission might justifiably be found liable

A fourth part of the statutory scheme is also relevant. In 1996, the legislature amended section 44-2003(A) to provide that, "No person shall be deemed to have participated in any sale or purchase solely by reason of having acted in the ordinary course of that person's professional capacity in connection with that sale or purchase."[165] This provision creates a safe haven for those persons who act solely within the ordinary course of their profession.[166] Like the postman, the retailer, and the title company who innocently provide services connected to a fraudulent transaction, professionals who do no more than provide ordinary professional services will incur no liability. On the other hand, those who depart from the ordinary course of their profession are likely to have engaged in culpable participation.[167]

Most professions have rules or standards that identify unprofessional conduct. For example, in the legal profession it is unprofessional conduct for a lawyer to engage in conduct involving dishonesty, fraud, deceit, or misrepresentation.[168] Arizona's State Board of Accountancy has a rule that prohibits certified public accountants from knowingly or recklessly making misrepresentations.[169] Similar rules exist for real estate agents[170] and

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under the rationale that holding non-negligent defendants who financially benefit from a securities violation proportionately liable is a reasonable means of protecting the public by encouraging heightened care. *Cf.* Baker v. Stewart Title & Trust of Phoenix, 5 P.3d 249, 259 ¶ 42 (Ariz. Ct. App. 2000) (explaining that strict liability through respondeat superior encourages employers to monitor their employees' activities to prevent harm).

165. ARIZ. REV. STAT. ANN. § 44-2003(A) (2008).

166. *See* Weinroth, *supra* note 112, at 27 (explaining that the statute is intended to protect professionals who "legitimately advise" their clients).

167. *Id.* (stating that "professionals who fail to fulfill their proper role and recklessly disregard securities violations by their clients" should be liable); *see also* Branson, *supra* note 129, at 1059–62 (reasoning that professionals who turn a blind eye to securities violations or who knowingly help create or maintain a false appearance for an investment are not performing routine professional services).

168. *See* MODEL RULES OF PROF'L CONDUCT R. 1.2(d) (2002) (providing that "[a] lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent . . . "); *id.* at R. 4.1(a) (providing that a lawyer "shall not knowingly make a statement of material fact or law to a third person"); *id.* at R. 4.1(b) (providing that a lawyer "shall not knowingly fail to disclose a material fact when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client, unless disclosure is prohibited by ethical rule 1.6"); *id.* at R. 8.49(c) (providing that it is professional misconduct to "engage in conduct involving dishonesty, fraud, deceit or misrepresentation").

169. ARIZ. ADMIN. CODE § R4-1-455(B) (2007) ("Certified public accountants, public accountants, or firms shall not knowingly or recklessly misrepresent facts when engaged in the practice of public accounting, including the rendering of tax and management advisory services.").

170. *See, e.g.*, *id.* § R28-1101 (2005) (requiring real estate agents to disclose any information that materially or adversely affects the consideration that is to be paid).

securities professionals.[171] Defendants who knowingly or recklessly violate the standards of their profession when advising their clients are not providing legitimate professional advice for which statutory protection should exist.[172]

To sum up, the statutory scheme leads to four conclusions regarding participant liability. First, culpable participation should be found when a defendant knowingly or recklessly takes part in a securities violation.[173] Second, when the defendant takes part in a securities violation with a less culpable state of mind–a negligent or a strict liability violation–the fact finder still retains discretion to impose proportionate liability for a percentage of the plaintiff's damage.[174] Third, when the defendant is a professional, misleading conduct that violates the rules or standards of the defendant's profession should be admitted as evidence on whether the defendant's conduct amounts to culpable participation for which proportionate or joint and several liability should be assessed.[175] Fourth, when an actor innocently participates in a securities transaction tainted by a statutory violation, liability should not be found unless it will further the legislative purpose–deterring fraud and protecting the public.[176]

### *E. Aiding and Abetting*

In 1979 the Arizona Supreme Court recognized aiding-and-abetting liability under Arizona Revised Statutes Section 44-1991 (now section 44-1991(A)).[177] Fifteen years later, in *Central Bank v. First Interstate Bank*, the U.S. Supreme Court eliminated aiding-and-abetting liability in rule 10b-5 actions.[178] But *Central Bank* does not bind Arizona's courts.[179] Two years

171. *See, e.g.*, NASD MANUAL (CCH), CONDUCT RULE 2120 (2006) ("No member shall effect any transaction in, or induce the purchase or sale of, any security by means of any manipulative, deceptive or other fraudulent device or contrivance.").

172. *Cf.* Lombardo v. Albu, 14 P.3d 288, 291 ¶ 15 (Ariz. 2000) (citing ARIZ. ADMIN. CODE § R4-28-1101(B)) (stating that "the rule provides minimum standards of care in the exercise of the [real estate] agent's duties"); Elliot v. Videan, 791 P.2d 639, 642 (Ariz. Ct. App. 1989) (holding that an attorney's violation of the rules of professional conduct is evidence of malpractice); 2 NORMAN S. POSER & JAMES A. FANTO, BROKER–DEALER LAW AND REGULATION § 16.06[B], 16-164 (4th ed. 2008) (explaining that the prevailing view is that self-regulatory rules promulgated by the securities industry are "'excellent tools' against which to assess the reasonableness of a broker's handling of a customer's account").

173. *See supra* notes 146–151 and accompanying text.

174. *See supra* notes 152–164 and accompanying text.

175. *See supra* notes 165–172 and accompanying text.

176. *See supra* notes 137–140 and accompanying text.

177. State v. Super. Ct., 599 P.2d 777, 784 (Ariz. 1979), *overruled in part on other grounds by* State v. Gunnison, 618 P.2d 604, 607 (1980).

178. 511 U.S. 164, 192 (1994).

after *Central Bank*, the Arizona legislature passed a statement of intent indicating that it was for Arizona's courts to decide whether to recognize aiding-and-abetting liability.[180] Since then, Arizona's courts have continued to recognize liability for aiding-and-abetting violations of section 44-1991(A).[181] This approach follows American law generally, which has experienced steady growth in aiding-and-abetting liability in tort and statutory law despite *Central Bank*.[182]

But a reasoned explanation of the basis for aiding-and-abetting liability under Arizona's statutes has not been made. Probably for this reason, trial-court motions are occasionally filed in which *Central Bank* is used to argue that aiding-and-abetting liability is no longer tenable under Arizona's Securities Act.[183] Rarely does anyone ask whether a statutory basis for aiding and abetting exists. This oversight occurs, as often happens, because cases are cited without attention to what the statutes say. A careful statutory reader would ask whether aiding and abetting is a form of participant liability under Arizona Revised Statutes section 44-2003(A).[184]

As discussed earlier in Part 4(D), section 44-2003(A) imposes joint-and-several liability on any person "who made, participated in or induced [an] unlawful [securities] sale or purchase."[185] In a 2002 nonsecurities case, the

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179. *See* Carrington v. Ariz. Corp. Comm'n, 18 P.3d 97, 99 ¶ 10 (Ariz. Ct. App. 2000) (holding that "when interpreting Arizona law, Arizona courts are not bound even by the United States Supreme Court's interpretation of federal securities laws").

180. During 1996, a senate bill was introduced to eliminate aiding-and-abetting liability. *See* RICHARD G. HIMELRICK & BRIAN J. SCHULMAN, ARIZONA SECURITIES FRAUD LIABILITY: STATUTORY AND COMMON-LAW REMEDIES § 5.1.3.2, at 90 (2d ed. 2006). As eventually enacted, the bill was amended to delete this language. *Id.* Contemporaneously, a statutory note was added to explain that "[n]othing in this act . . . determines whether or in what circumstances aiding and abetting liability exists . . . ." Private Securities Litigation, ch. 197, § 11(B), 1996 Ariz. Sess. Laws 1003, 1023.

181. *See* Wojtunik v. Kealy, 394 F. Supp. 2d 1149, 1170 (D. Ariz. 2005) ("[T]he Arizona Supreme Court's recognition in 1979 of a private right of action for aiding and abetting in the *State v. Super. Ct.* case stands as the law currently controlling" the issue of aiding-and-abetting violations under Arizona Revised Statute section 44-1991(A).).

182. *See* Richard C. Mason, *Civil Liability for Aiding and Abetting,* 61 BUS. LAW. 1135, 1136–37 (2006) (stating that since *Central Bank*, "claims of aiding and abetting, in areas such as breach of fiduciary duty, commercial fraud, and state law securities liability, steadily have increased"); *see also* Wells Fargo Bank v. Ariz. Laborers, Teamsters and Cement Masons Local No. 395 Pension Trust Fund, 38 P.3d 12, 26–28 (Ariz. 2002) (acknowledging *Central Bank* but using pre-*Central Bank* securities cases to define the elements of aiding and abetting common-law fraud).

183. *See Wojtunik*, 394 F. Supp. 2d at 1170 (rejecting argument that *Central Bank* eliminated aiding-and-abetting under Arizona's securities laws).

184. *See* Weinroth, *supra* note 112, at 26 (suggesting that "an overlap may exist between express 'participant' liability under section 44-2003 and implied aiding and abetting liability").

185. ARIZ. REV. STAT. ANN. § 44-2003(A) (2008).

Arizona Supreme Court defined aiding and abetting to include conduct in which a person knowingly provides substantial assistance to the primary tortfeasor.[186] As previously explained, the culpability needed for participant liability should be found when a defendant knowingly takes part in an act of fraud.[187] Aiding and abetting, when defined as knowingly providing substantial assistance to fraud, is reasonably viewed as one way to culpably participate in a securities sale.

It is reasonable because, as an initial matter, it advances the statutory goals of deterring fraud and protecting the public. It is difficult to imagine a reasonable legislator, acting with the intent described in the 1951 statement, who would want to exclude from liability those who knowingly assist securities fraud. Treating these actors as culpable participants ensures that those who knowingly contribute to fraudulent securities sales are held accountable.

The 1996 amendments regarding joint and several liability and proportionate fault also suggest the legislature's intent to impose liability on those who knowingly assist fraud. Under these provisions, defendants who act knowingly or recklessly are jointly and severally liable for securities violations,[188] while those who act with a state of mind less culpable than knowing or reckless conduct are liable only for their percentage of responsibility.[189] These rules reflect legislative judgments about the actors who should be liable for all or part of the damage caused by a securities violation.[190] And they tell us that those persons who knowingly commit securities fraud are jointly and severally liable. From this it follows logically that those persons who aid and abet by knowingly assisting fraudulent securities sales are culpable.

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186. *Wells Fargo Bank*, 38 P.3d at 23. The elements of aiding-and-abetting in a securities case were listed in *State v. Super. Ct.*, 599 P.2d 777, 784 (Ariz. 1979), *overruled in part on other grounds by* State v. Gunnison, 618 P.2d 604, 607 (1980) ("There are three prerequisites to a finding that one has aided and abetted a securities law violation: (1) a primary violation has occurred; (2) knowledge of or a duty of inquiry with regard to the primary violation by the person charged; and (3) a necessary contribution to the underlying scheme by the person charged.").

187. *See supra* notes 147–151.

188. Section 44-2003 provides: "Any covered person against whom a final judgment is entered in a private action is jointly and severally liable for damages only if the trier of fact determines that the covered person recklessly or knowingly committed a violation of this chapter." ARIZ. REV. STAT. ANN. § 44-2003 (2008).

189. *See* ARIZ. REV. STAT. ANN. § 44-2003(B)–(C). For further discussion, see *supra* notes 113–19 and accompanying text.

190. *Cf.* Jill E. Fisch, *The Scope of Private Securities Litigation: In Search of Liability Standards for Secondary Defendants*, 99 COLUM. L. REV. 1293, 1313 (1999) (reasoning as to rule 10b-5 that "[p]roportionate liability rules are of limited importance unless the general standard of liability holds collateral defendants responsible for securities fraud").

Finally, there is the 1996 decision in *Standard Chartered PLC v. Price Waterhouse*.[191] In that case, the Court of Appeals read an earlier Supreme Court case[192] as having held that participant liability exists where a defendant "actively promote[s] a fraudulent transaction."[193] The Court of Appeals then examined the meaning of participant liability in the context of an auditor's liability. It concluded that a defendant participates for purposes of section 44-2003 when the defendant "take[s] part in" a fraudulent securities transaction or shares in the proceeds of the transaction.[194] Although aiding and abetting was not an issue in *Standard Chartered*, knowingly assisting a person who makes a prohibited sale is one way to take part in the sale.[195] In short, the standard of knowingly providing substantial assistance that provides the common-law basis for aiding-and-abetting liability is also one way to incur participant liability under section 44-2003(A).

To recap, then, the following factors point to the conclusion that aiding and abetting is a form of participant liability. First, the legislature broadly worded section 44-2003(A) to impose securities liability not only on sellers, but on all persons who participate in a fraudulent sale. Second, the legislative goals of public protection and fraud deterrence, coupled with the legislative directive to construe the securities statutes broadly, suggests that participation should be read to embrace knowing assistance. Third, the 1996 amendments providing for joint and several liability among securities violators who act knowingly point to a legislative intent to hold accountable secondary actors who knowingly participate in fraud. Fourth, *Standard Chartered* defined participation broadly enough to include aiding and abetting. Thus, through statutory interpretation and case law we have a reasoned explanation for why Arizona's securities laws, unlike rule 10b-5, provide express support for aiding-and-abetting liability.

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191. 945 P.2d 317 (Ariz. Ct. App. 1996).

192. State v. Super. Ct., 599 P.2d 777, 784 (Ariz. 1979), *overruled in part on other grounds by* State v. Gunnison, 618 P.2d 604, 607 (Ariz. 1980).

193. *Standard Chartered*, 945 P.2d at 332.

194. *Id.*

195. *See, e.g.*, Little v. First Cal., Co., [1977–78 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,226, at 92,561 (Oct. 17, 1977), *available at* 1977 WL 1055, at *8 (reasoning that knowing participation in an act of fraud creates liability under section 44-2003 (now section 44-2003(A)); Strom v. Black, 523 P.2d 1339, 1340–41 (Ariz. Ct. App. 1974) (holding business broker who created misleading advertising liable as statutory participant under section 44-2003 (now section 44-2003(A)).

### F. Nonstatutory Defenses

Common-law defenses like waiver, ratification, estoppel, and failure to mitigate are routinely asserted in litigation under rule 10b-5.[196] The same defenses are often attempted in trial court litigation under Arizona's Securities Act.[197] Yet early blue-sky cases decided before the 1951 version of Arizona's Securities Act rejected equitable defenses to registration violations.[198] And courts in other states have held that nonstatutory, common-law defenses are not available in actions under their securities laws.[199] These decisions suggest caution in accepting rule 10b-5 defenses in cases under Arizona's securities statutes.

Use of waiver, ratification, and other common-law defenses is understandable in rule 10b-5 actions. Because the rule 10b-5 action arose as a judicially implied action, the rule does not contain legislatively enacted defenses. The federal courts were therefore compelled to create defenses just like they defined the elements of the 10b-5 action through judicially crafted doctrines like materiality, reliance, and scienter.[200] But as we have

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196. *See, e.g.*, Hecht v. Harris, Upham & Co., 430 F.2d 1202, 1207–08 (9th Cir. 1970) (upholding findings of estoppel, laches, and waiver in 10b-5 action); Royal Air Props., Inc. v. Smith, 312 F.2d 210, 213 (9th Cir. 1962) (holding that waiver and estoppel are defenses in a 10b-5 action); Van Syckle v. C.L. King & Assocs., Inc., 822 F. Supp. 98, 101–03 (N.D.N.Y. 1993) (recognizing the plaintiff's failure to mitigate as a defense to claims under rule 10b-5).

197. *See, e.g.*, Noonan v. Hackett Inv. Advisors Inc., No. CV 2005-010186, 2006 WL 3501241, at *3 (Ariz. Super. Ct. Nov. 20, 2006) (trial court order holding that ratification and failure to mitigate are not defenses to violations of Arizona Revised Statutes section 44-1991(A)).

198. *See* Reilly v. Clyne, 234 P. 35, 39–40 (Ariz. 1925) (rejecting ratification and in pari delicto defenses to registration violation); *see also* United Bank & Trust Co. v. Joyner, 11 P.2d 829, 832 (Ariz. 1932) (same). These cases reason that a stock subscription agreement that violates a statute is incapable of ratification. *See, e.g.*, *Reilly*, 234 P. at 39. They also make the point that the parties cannot be in pari delicto "where the law which makes the agreement unlawful was intended for the special protection of the one seeking relief . . . " *Id.* at 39–40.

199. *See, e.g.*, Gowdy v. Richter, 314 N.E.2d 549, 557–58 (Ill. App. Ct. 1974) (rejecting estoppel and in pari delicto defenses to registration violation because "[t]he law in Illinois is clear in allowing only statutory, not equitable, defenses to be raised by a defendant in a case involving a blue sky violation"); Duperier v. Tex. State Bank, 28 S.W.3d 740, 753 (Tex. Ct. App. 2000) (holding that common-law ratification is not a defense to statutory-securities fraud under Texas law); Riggs v. Riggs, 322 S.W.2d 571, 574 (Tex. Ct. App. 1959) (stating in dictum that laches was inapplicable to a statutory violation under the former version of the Texas blue-sky laws: "[Defendant] was seeking to enforce a statutory legal right. The defense of laches is not available to the defendant in such a suit"); Go2Net, Inc. v. FreeYellow.Com, Inc., 143 P.3d 590, 591 (Wash. 2006) (holding that the equitable defenses of waiver and estoppel are not available in an action for violations of the Washington Securities Act's antifraud statute).

200. *See Royal Air Props.*, 312 F.2d at 213 (reasoning that because liability under rule 10b-5 was judicially implied, it is appropriate to permit common-law defenses like waiver and estoppel); *cf.* Loss, *supra* note 90, at 910 (explaining that the rule 10b-5 elements of scienter,

seen, liability under Arizona's securities laws is express liability.[201] The statutes that define this liability identify the defenses that apply.[202] These include a two-year statute of limitations;[203] loss causation under sections 44-1991(B) and 44-2082(E);[204] proportionate fault if the defendant did not act knowingly or recklessly;[205] reasonable care as to violations of section 44-1991(A);[206] good faith, reasonable care and noninducement as to controlling-person claims;[207] and the duty to tender.[208] These express defenses show that the legislature listed the defenses that it intended to exist. Why then should the courts add defenses the legislature did not see fit to enact?[209]

The 1951 statement of intent also weighs against importing common-law defenses into the statutory scheme.[210] The statement of intent requires that Arizona's securities statutes be read broadly to deter fraud and protect the

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reliance, and causation were judicially created). In 1995, Congress added loss causation as a statutory requirement. *See* Dura Pharms., Inc. v. Broudo, 544 U.S. 336, 345–46 (2005).

201. *See supra* notes 3, 5 and accompanying text.

202. *Cf. Go2Net*, 143 P.3d at 593 ("[B]ecause the [Washington Securities] Act sets forth a limited number of defenses to claimed violations of the Act, the Act's silence with respect to the equitable defenses of waiver and estoppel suggests that the legislature intended to exclude them.").

203. *See* ARIZ. REV. STAT. ANN. § 44-2004(B) (2008).

204. *Id.* § 44-1991(B) (2008) (permitting the defendant to reduce a plaintiff's damages by negativing loss causation); *id.* § 44-2082(E) (2008) (providing that except as stated in section 44-1991(B), the plaintiff has the burden of proving loss causation).

205. The Securities Act has its own rules on proportionate fault. *Id.* § 44-2003(B)–(D) (2008). Under these rules defendants who act knowingly or recklessly are jointly and severally liable without reduction for comparative fault. *Id.* § 44-2003(B). On the other hand, those who act with a less culpable state of mind are liable only for their proportionate fault in causing the plaintiff's injury. *Id.* § 44-2003(C); *see supra* note 189 and accompanying text.

206. Section 44-2001(B) provides that a person sued under section 44-1991(A) is not liable "if the person sustains the burden of proof that the person did not know and in the exercise of reasonable care could not have known of the untrue statement or misleading omission." ARIZ. REV. STAT. ANN. § 44-2001(B) (2008); *see generally* Barnes & St. Louis, *supra* note 113 (discussing the reasonable care defense under the Uniform Securities Act).

207. *See* Himelrick, *supra* note 42, at 227–28.

208. ARIZ. REV. STAT. ANN. § 44-2001(A) (requiring tender when the plaintiff seeks a rescissionary recovery); *see* Grand v. Nacchio, 147 P.3d 763, 775–78 ¶¶ 37–48 (Ariz. Ct. App. 2006) (discussing the tender requirement and holding that a plaintiff who has sold the securities may still obtain rescission if the plaintiff purchases replacement securities and tenders them).

209. *See* State v. Fell, 52 P.3d. 218, 221 ¶ 11 (Ariz. Ct. App. 2002) (invoking the expressio unius canon (i.e., the expression of one thing suggests the exclusion of others) and refusing to read a necessity defense into the DUI statute); Massey v. Colaric, 725 P.2d 1099, 1100–01 (Ariz. 1986) (refusing to read assumption of risk into the dog-bite statute, which lists provocation as the only defense).

210. *See supra* note 27 and accompanying text.

public.[211] Diluting statutory remedies with common-law defenses undermines this legislative intent by creating barriers to statutory remedies designed to deter fraud and compensate defrauded investors.[212]

Moreover, the structure of the statutory scheme, particularly its remedial features, precludes some defenses. For example, proximate cause, and its securities-law counterpart, loss causation,[213] has been held inconsistent with statutory rescission under Arizona Revised Statutes section 44-2001(A).[214] Similarly, allowing a defendant to block statutory rescission because an investor failed to mitigate his or her damages seems contrary to the right to elect rescission.[215] This follows from *Grand v. Nacchio*, which held that causation is not required for rescission.[216] If causation is unnecessary, it cannot be proper to bar or reduce a plaintiff's recovery because the plaintiff's conduct contributed to the loss.[217] Thus, the common-law defense of failure to mitigate is inconsistent with the statutory scheme.[218]

A final example of the incompatibility of common-law defenses with the statutory scheme is provided by Arizona Revised Statutes section 44-2000, which prohibits contracts that bind a person to waive compliance with the Securities Act.[219] Under this statute, some forms of common-law waiver are

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211. *See supra* Part.II.A (discussing the broad, investor-protective interpretation taken by Arizona courts since 2001).

212. *Cf.* Go2Net, Inc. v. FreeYellow.Com, Inc., 143 P.3d 590, 593 ¶ 11 (Wash. 2006) ("[P]ermitting a seller to assert equitable defenses is contrary to the [Washington Securities] Act's primary purpose of protecting investors.").

213. *See Grand*, 147 P.3d at 773 ¶ 30 ("Loss causation is nothing more than proximate cause . . . .").

214. *See id.* at 778 ¶ 50 ("[U]nder Arizona law, a plaintiff who proves a violation of A.R.S. § 44-1991(A)(1) or (3) may rescind the sale, despite having suffered no loss.").

215. *See* Wash. Nat'l Corp. v. Thomas, 570 P.2d 1268, 1276 (Ariz. Ct. App. 1977) (awarding both statutory rescission and damages; rejecting claim that securities plaintiff's damages were "self-inflicted"; and stating that the defendants "cannot complain as to the course chosen by appellees in their reaction to the misleading statements"); *cf.* Odmark v. Westside Bancorporation, Inc., No. C85-1009R, 1988 WL 108288, at *2 (W.D. Wash. Mar. 9, 1988) (holding that mitigation is not a limitation on statutory rescission under Washington's Securities Act).

216. 147 P.3d at 778–79 ¶¶ 49–51.

217. *Cf. Odmark*, 1988 WL 108288, at *2 (holding that mitigation is not a limitation on statutory rescission under Washington's Securities Act).

218. *Cf. id.* Failure to mitigate is a form of contributory fault by the plaintiff. Recognizing this defense would also be inconsistent with the comparative fault statutes, which do not provide for an allocation of fault to plaintiffs. *See supra* note 218 and accompanying text. But a caveat exists. The statutory right to tender requires a timely tender. *See Grand*, 147 P.3d at 778 ¶ 48. If an investor deliberately delays tender so that the investor can speculate on which way the market moves, the tender may be untimely. *Id.* at 778 n.13.

219. Section 44-2000 (2008) reads: "Any condition, stipulation or provision binding any person acquiring any security to waive compliance with this chapter or chapter 13 of this title or of the rules of the commission is void."

prohibited.[220] This might occur, for instance, when a seller attempts to use a merger or no-reliance clause[221] to trump the duty not to mislead that exists under Arizona's securities laws.[222] Contractually reducing disclosure duties seems contrary to section 44-2000's antiwaiver policy as well as the legislative directive to broadly read the securities laws in favor of public protection. The purpose of the antiwaiver statute is to prevent securities sellers from using contractual waivers to narrow the protection from fraud at which the Securities Act is aimed.[223] Consequently, use of contractual provisions to create an argument that the plaintiff waived his or her right to prove fraud is inconsistent with section 44-2000.

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220. *Cf.* Go2Net, Inc. v. FreeYellow.Com, Inc., 143 P.3d 590, 593 ¶ 11 (Wash. 2006) (holding that allowing a waiver defense based on post-sale conduct would be contrary to the "strong antiwaiver provision" under Washington's Securities Act); Todaro v. E.F. Hutton & Co., 1982–1984 Blue Sky L. Rep. (CCH) 70,410 ¶ 71,957, 70,412–13 ¶ 71,957 (E.D. Va. 1982) (construing Virginia's antiwaiver statute and holding: "[T]he remedial purposes of the Virginia Securities Act require a broad construction of its protective provisions. To allow a waiver defense as proposed by defendants would greatly contract an investor's remedies") (citations omitted)).

221. For an example of a no-reliance clause, see *Rissman v. Rissman*, 213 F.3d 381 (7th Cir. 2000). The contract in that case provided: "[T]his Agreement is executed by [Arnold] freely and voluntarily, and without reliance upon any statement or representation by Purchaser, the Company, any of the Affiliates or O.R. Rissman or any of their attorneys or agents except as set for herein . . " *Id.* at 383. (second alteration in original). *Rissman* held that the no-reliance clause precluded fraud claims based on oral misrepresentations. *Id.* at 384 ("[A] written anti-reliance clause precludes any claim of deceit by prior representations."). *Rissman* is criticized in Prentice, *supra* note 104, at 349 ("[B]y simply adding a sentence of boilerplate in the form of a no-reliance clause ('plaintiff relies on no statements not contained herein') that seemingly adds nothing meaningful to a standard integration clause, defendants can prevent plaintiffs from even having the opportunity to prove they were defrauded, no matter how strong their evidence.").

222. *Cf.* Wash. Nat'l Corp. v. Thomas, 570 P.2d 1268, 1275 (Ariz. Ct. App. 1977) (rejecting arguments that the plaintiffs should not have relied upon defendant's misrepresentations because Arizona Revised Statutes section 44-1991 (now section 44-1991(A)) "imposes an affirmative duty not to mislead"); Prentice, *supra* note 104, at 350–58 (discussing differing interpretations of the antiwaiver statutes under the federal securities laws and arguing that no-reliance clauses violate these provisions); *see also* Formento v. Encanto Bus. Park, 744 P.2d 22, 26 (Ariz. Ct. App. 1987) ("[A] seller should not be allowed to hide behind an integration clause to avoid the consequences of a misrepresentation, whether fraudulent or negligent.").

223. *Cf.* AES Corp. v. Dow Chemical Co., 325 F.3d 174, 183 (3d Cir. 2003) (construing the antiwaiver provision under section 29(a) of the 1934 Exchange Act and explaining that "Section 29(a) is not intended to protect substantive rights created by contract. It is designed to protect rights created by the Exchange Act, and it expressly forecloses contracting parties from 'defin[ing] the boundaries of the[ir] transaction' in a way that relieves a party of the duties imposed by that Act") (alterations in the original); *In re* Nat'l Century Fin. Enters., Inc., Inv. Litig., 541 F. Supp. 2d 986, 1005 (S.D. Ohio 2007) ("[I]t would defeat the securities laws if parties could escape liability for their own deliberate misrepresentations by inserting boilerplate disclaimers into offering materials.").

## V. CONCLUSION

Securities cases are statutory cases. Appellate decisions interpreting Arizona's Securities Act are rare. In the more than seven years spanning 2000 through 2008, only six decisions provide meaningful discussion of an issue under the Act.[224] It is not surprising, therefore, that controlling Arizona precedent is frequently absent. Even so, the examples in this Article on scienter, unauthorized trading, reliance, contributory fault by investors, participant liability, aiding and abetting, and nonstatutory defenses show that thoughtful statutory construction will often supply answers and insights on which case law is silent.

Focusing on statutory interpretation is particularly useful in identifying those areas where Arizona securities law departs from common-law fraud and federal securities law. For example, through statutory interpretation we have seen that common-law reliance is not an element of statutory securities fraud.[225] Nor are common-law defenses properly applied to state securities claims.[226] Statutory analysis also identifies those instances in which Arizona law differs from federal law. We have seen examples of this in the discussion of unauthorized trading and aiding and abetting.[227] Differences like these are easily muddied in the nonstatutory, case-driven analysis used by most attorneys and many courts. Because Arizona securities law is statutory law, its analysis should be grounded in statutory interpretation. Proceeding on this basis significantly enhances the likelihood of developing well-reasoned state securities law.

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224. *See* Grand v. Nacchio, 147 P.3d 763, 778–80 ¶¶ 49–60 (Ariz. Ct. App. 2006) (deciding issues regarding loss causation and statutory rescission); Eastern Vanguard Forex, Ltd. v. Ariz. Corp. Comm'n, 79 P.3d 86, 97–102 ¶¶ 36-51 (Ariz. Ct. App. 2003) (interpreting section 44-1999 control liability provisions); Albers v. Edelson Tech. Partners L.P., 31 P.3d 821, 825–26 ¶¶ 14–16 (Ariz. Ct. App. 2001) (discussing pleading standards for securities fraud and holding that a promise made without intent to perform may be securities fraud); Siporin v. Carrington, 23 P.2d 92, 94–96 ¶¶ 3–17 (Ariz. Ct. App. 1991) (holding that viatical settlements are securities); Carrington v. Ariz. Corp. Comm'n, 18 P.3d 97, 99–100 ¶¶ 10–12 (Ariz. Ct. App. 2000) (deciding issues regarding the enforceability of ACC subpoenas and explaining that when interpreting Arizona law, Arizona courts are not bound by even the U.S. Supreme Court's decisions on federal securities law); Aaron v. Fromkin, 994 P.2d 1039, 1042–1044 ¶¶ 10–28 (Ariz. Ct. App. 2000) (discussing materiality, scienter, the elements of a prima facie case, and the statute of limitations).

225. *See supra* notes 89–101 and accompanying text.

226. *See supra* notes 197–233 and accompanying text.

227. *See supra* notes 77–87, 117–195 and accompanying text.

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