

**MEMO# 15378**

November 21, 2002

## **U.S. DISTRICT COURT AFFIRMS THAT RESCISSION AND RESTITUTION ARE THE ONLY PRIVATE REMEDIES AVAILABLE UNDER THE ADVISERS ACT**

[15378] November 21, 2002 TO: COMPLIANCE ADVISORY COMMITTEE No. 103-02 INVESTMENT ADVISER ASSOCIATE MEMBERS No. 34-02 INVESTMENT ADVISER MEMBERS No. 51-02 RE: U.S. DISTRICT COURT AFFIRMS THAT RESCISSION AND RESTITUTION ARE THE ONLY PRIVATE REMEDIES AVAILABLE UNDER THE ADVISERS ACT The U.S. District Court for the District of Massachusetts in a case of first impression since the 1990 amendments to the Investment Advisers Act has held that “the only private remedies available under the [Investment Advisers Act] remain rescission of an investment advisers contract and restitution of fees paid thereunder under Section 215 [of the Act].”<sup>1</sup> This case was originally filed in state court in December 1998 and alleged that the defendants, as the plaintiffs’ investment advisers, breached their fiduciary duties, rendered negligent investment advice, and employed a scheme to defraud. The defendants removed the case to the U.S. District Court based upon the plaintiffs’ claims under Section 206 of the Advisers Act, for which the plaintiffs were demanding “damages plus interest and costs, and such other relief as [the] court deems appropriate.” In response, the defendants moved for summary judgment citing *Transamerica Mortgage Advisers, Inc. v. Lewis*, 444 U.S. 11 (1979) for the proposition that private remedies under the Advisers Act are limited to rescission of an adviser’s contract and restitution of fees paid thereunder. While the court acknowledged the Supreme Court’s holding in *Transamerica* that a limited private right of action for rescission and restitution was implied under Section 215 of the Advisers Act but not under Section 206, it noted that no courts had explored the scope of private rights of action for damages under the Advisers Act since the Advisers Act was amended in 1990 through the Securities Law Enforcement Remedies Act of 1990 (SERA).<sup>2</sup> The plaintiffs argued that amendments in SERA to Section 214 of the Advisers Act indicated “an intent to expand district court jurisdiction to encompass a private litigant’s action at law to 1 See *Filson v. Langman* (D. Mass 99-30021-FHF, November 13, 2002). A copy of the court’s opinion is available through the court’s website at: <http://pacer.mad.uscourts.gov/recentopinions.html> 2 As discussed in the court’s opinion, SERA amended Section 209 of the Advisers Act to grant the SEC additional remedies including the power: to assess civil monetary penalties in administrative proceedings, to order an accounting and disgorgement of profits, to issue cease and desist orders, and to seek monetary penalties in injunctive actions in district court for violation of the Advisers Act and of the SEC’s cease and desist orders. 2 enforce liabilities and duties created by the [Advisers Act].”<sup>3</sup> In addressing this argument, the court reviewed both the statutory amendments as well as their legislative history, from which it concluded that the

amendments to Section 214 were “nothing more than ‘a conforming amendment’” that were “necessitated by” the amendments to Section 209 that expanded the remedies available to the SEC in enforcement proceedings. In the court’s view, “[n]othing in SERA’s structure indicates a further intent to open the courthouse doors to private litigants seeking damages beyond restitution. . . . Implying a more expansive private right of action would upset the delicate balance that Congress intended.” As regards the plaintiffs’ entitlement to restitution, the court noted that the plaintiffs’ complaint asked only for “damages” under Section 206 and not for rescission and restitution under Section 215. While the plaintiffs conceded that they were not seeking rescission of the advisory contract,<sup>4</sup> they maintained that their demand for relief included restitutionary damages. The court, however, found that because the plaintiffs failed to advance a theory of relief pursuant to Section 215 of the Advisers Act, they had “waived their right to rescission and restitution.” The court found this waiver “fatal to [the plaintiffs’] only federal law claim.” On this basis, the court granted the defendants’ motion for summary judgment on the federal law claim and remanded the case back to state court to address the plaintiffs’ remaining state law claims. Tamara K. Salmon Senior Associate Counsel 3 The amendments to Section 214 expanded the district courts’ jurisdiction to include “actions at law brought to enforce any liability or duty created by [the Act] . . . .” 4 According to the court’s opinion, the defendants disputed the existence of an advisory contract. The court, however, analyzed the plaintiffs’ entitlement to damages by assuming, but not deciding, that such contract existed.