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in the Federal Securities Laws

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JUSTICE LEWIS F. POWELL, JR.
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This project would not have been possible without the assistance of John Jacob, archivist of the Powell Archives at the Washington & Lee Law Library. John went above and beyond the call of duty in providing me with access and insights to the collection. He is a credit to his profession and I am grateful for his assistance. Unpublished sources are from the Powell Archives unless otherwise noted, and copies are on file with the author.

Dan Spies and the libraries of the University of Michigan Law School and the Georgetown University Law Center provided helpful research assistance. Numerous individuals also provided background on Powell’s corporate law practice and former Powell clerks offered insights into his work on the Supreme Court; their very helpful contributions are acknowledged in footnotes at appropriate places in the text. Steve Bainbridge, Evan Caminker, Steve Choi, Rich Friedman, John Jeffries, Jill Fisch, Mitu Gulati, Don Langevoort, Joan Larsen, Ronald Mann, Richard Painter, Hillary Sale, Mike Seidman, Joel Seligman, Randall Thomas, Bob Thompson, Mark West and Chris Whitman provided useful comments on earlier drafts of this article. Any remaining errors of fact or interpretation are my own. The Cook Fund of the University of Michigan Law School provided generous financial support for this research.
Justice Lewis F. Powell, Jr. and the Counter-Revolution in the Federal Securities Laws

The confirmation of Lewis F. Powell, Jr. to the Supreme Court led to a dramatic shift in the Court’s approach to securities law. This article relies on Powell’s internal Court files to document Powell’s influence in changing the Court’s direction in securities law. Powell’s influence was the product of his extensive experience with the securities laws as a corporate lawyer, which gave him much greater familiarity with that body of law than his fellow justices had. That experience also made him skeptical of civil liability, particularly class and derivative actions. Powell’s skepticism led him to interpret the securities law in a consistently narrow fashion to reduce liability exposure and increase predictability. Powell also rebuffed the SEC’s efforts to expand its reach, particularly in insider trading and takeover regulation. Powell’s experience and interest produced a counter-revolution in the federal securities law.

The 1960s witnessed a rapid expansion of the federal securities laws, primarily through broad interpretations of Rule 10b-5\(^1\) by the courts and the Securities and Exchange Commission. Rule 10b-5—ostensibly a simple anti-fraud provision—threatened to become an overarching “federal corporation law.”\(^2\) In 1961, the SEC pioneered prohibitions against insider trading in its Cady, Roberts decision.\(^3\) In 1964, the Supreme Court recognized the existence of a private cause of action for proxy violations in J.J. Case v. Borak.\(^4\) That recognition tacitly validated private suits under Rule 10b-5 as well, setting loose a plethora of decisions in which lower federal courts imposed a variety of duties on corporate officers and directors. In 1969, Louis Loss observed that “the great Rule 10b-5 seems . . . to be taking over the universe gradually.”\(^5\) The lower courts could feel confident that their expansive interpretations would be upheld, given the Supreme

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\(^1\) 17 C.F.R. §240.10b-5.


\(^4\) 377 U.S. 426 (1964).

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Court’s consistently broad reading of those laws from the time of their enactment.\(^6\) This trend reached its “apogee” during the Court’s October ‘71 term, with two of the most expansive decisions.\(^7\) The federal securities laws seemed poised to take over the law governing corporations entirely.

This trend dominated corporate and securities law when Lewis F. Powell, Jr. was sworn in as an associate justice of the Supreme Court on January 7, 1972. Powell’s swearing in coincided with an immediate sea-change in the path of the federal securities laws.\(^8\) While the Burger Court has been described as “the counter-revolution that wasn’t” in constitutional law, that description does not fit the field of securities law.\(^9\)

By the time Powell retired from the Court on June 26, 1987, federal securities law had been

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\(^6\) Alfred Conard, Securities Regulation in the Burger Court, 56 U. Colo. L. Rev. 193, 195 (1985) (showing that in nineteen securities law cases that the Supreme Court decided between 1933 and 1971 which required a choice in the breadth of coverage of the securities laws, the court opted for the broader approach in sixteen).

\(^7\) Charles M. Elson & Robert B. Thompson, Van Gorkom’s Legacy: The Limits of Judicially Enforced Constraints and the Promise of Proprietary Incentives, 96 Nw. L. Rev. 579, 579 (2002). The two cases are Affiliated Ute Citizens v. United States et al., 406 U.S. 128 (decided April 24, 1972) (recognizing a presumption of reliance for fraudulent omissions); Superintendent of Insurance v. Bankers Life and Casualty Company et al., 404 U.S. 6 (decided Nov. 8, 1971) (expanding the “in connection” requirement under Section 10(b)). Neither Powell nor Justice Rehnquist participated in these two cases. Bankers Life was Justice Douglas’s last securities law opinion for the Court and Affiliated Ute was Justice Blackmun’s first. Bankers Life was unanimous and Affiliated Ute was unanimous except for a partial dissent by Justice Douglas; he would have held the United States liable for the fraud as well. Affiliated Ute, 406 U.S. at 157. Blackmun characterized his opinion in Affiliated Ute as taking “a very liberal approach to Rule 10b-5. This may represent a step beyond any point the Court has heretofore reached.” Memorandum to the Conference from Harry A. Blackmun, No. 70-78, Affiliated Ute Citizens v. United States (April 10, 1972).

\(^8\) Lewis D. Lowenfels, Recent Supreme Court Decisions under the Federal Securities Laws: The Pendulum Swings, 65 Geo. L. J. 891, 891-892 (1977) (“Before recent Supreme Court decisions, plaintiffs’ lawyers and the Securities and Exchange Commission had been relatively free to devise original and imaginative causes of action based upon the federal securities laws. Following these decisions, however, the entire momentum has shifted. In these recent holdings, the Supreme Court has consistently decided in favor of the defendants and has enunciated principles that may circumscribe the rights of plaintiffs under the federal securities laws for many years to come.”)

The threat has recently resurfaced in the recently-enacted Sarbanes-Oxley Act, which intrudes upon state corporate law in a variety of ways. Corporate Auditing Accountability, Responsibility and Transparency Act of 2002, Pub. L. No. 107-204 (July 30, 2002).

It would be an exaggeration to give Justice Powell sole credit for this retrenchment – other justices wrote important opinions curtailing the growth of liability under the federal securities law. Moreover, the election of Ronald Reagan augured a renewed commitment to the governing role of the states. Nonetheless, it would be difficult to identify anyone who did more to limit the reach of the federal securities law than Powell.

This article chronicles Justice Powell’s influence on federal securities law. Powell participated in 41 decisions involving the federal securities laws, writing eleven opinions for the Court. Powell wrote some of the foundational opinions in securities law, found in every securities casebook: Chiarella and Dirks in insider trading, Ernst & Ernst on scienter, Forman and Landreth Timber on the definition of a security. Even in those cases in which Powell did not write, he played an important role in their selection and resolution.

The article makes two principal contributions to the literature. First, it fills a major gap in the understanding of Justice Powell’s work on the Supreme Court. John Jeffries’ otherwise excellent biography of Powell discusses Powell’s practice as a

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CORPORATE LAWYER, BUT IT DOES NOT DISCUSS Powell’s work in securities cases.\textsuperscript{13} Securities law, however, was of singular importance to Powell. His background as a corporate lawyer gave him a level of experience and familiarity with the securities laws unmatched by his colleagues. Consequently, Powell felt a special responsibility to guide his colleagues when they faced securities law questions. Of equal importance, Powell’s experience as a corporate lawyer had left him with definite views on the direction that the securities laws should take. In contrast to his reputation in constitutional law as a swing vote, Powell had profoundly conservative views on the proper scope of the federal securities laws and he pushed the Court toward holdings consistent with those views.

The article’s second contribution is to show how Powell, more than any other justice, helped cabin the federal securities law. In contrast to most studies of the Supreme Court’s work, which rely exclusively on published opinions, I draw heavily from Powell’s private Court papers, including drafts of opinions and correspondence among the justices, to explore how the Court’s opinions came to their final, published form.\textsuperscript{14} Most of the case files contain memoranda dictated by Powell, either to memorialize his


\textsuperscript{14}The papers are well-organized and comprehensive. Powell took care to ensure that they would be of use to historians. Memo to Sally [Smith] and Linda [Blandford] from LFP, Re: Legibility of Carbon Copies (2/28/79). Many of the papers relied upon were dictated by Powell and unedited, as they were for his internal use. Consequently, there are some typographical errors in selections that I quote. I have quoted these materials as they appear in the original documents. The errors should not be construed as carelessness on Powell’s part, but rather an effort to economize on secretarial time. Powell was meticulous in editing work that was to be published; indeed, he was sufficiently compulsive in this regard that he frequently corrected typographical and grammatical errors in certiorari pool memos.
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VIEW OF A CASE DURING THE SUMMER RECESS OR TO GUIDE THE CLERK WORKING ON THE CASE.\(^{15}\)

Powell frequently outlined the points that he intended to make at conference (particularly in complicated cases). The papers also include Powell’s tally of votes on certiorari as well as notes on oral argument and discussion at the justices’ subsequent conference.\(^{16}\) These materials taken as a whole give a fuller account than is available from reading only published opinions, providing a window into judicial behavior and how the Supreme Court makes law. They also show the influence that a single justice can have on his colleagues and how clerks and justices work together to draft opinions.

The materials also demonstrate a fact that might be obscured by looking simply at published opinions: in interpreting the securities laws, text and statutory structure mattered to Powell and the other members of the Court, but policy mattered at least as much. Powell’s policy views, grounded in his experience as a corporate lawyer, generally favored the narrower reading of the federal securities laws. Powell favored predictability in application of the securities laws and he was suspicious of the efforts of private plaintiffs and the SEC to bring the federal securities law into areas traditionally governed by state law and private agreement. Powell led the Court to narrower interpretations of the securities law, reversing its direction from the path it had taken in the 1960s. The cases decided during Powell’s tenure helped confine the

\(^{15}\)In addition, these papers include certiorari memoranda as well as bench memoranda. Powell wrote extensive comments in the margins on the merits and the relative importance of issues presented. Powell had the helpful habit (for a researcher) of indicating his agreement with a point by writing “Yes” in the margin of documents that he reviewed.

\(^{16}\)These notes must be read with some caution, as they reflect Powell’s view of the discussion at conference and his choices on what to record. His attitudes on the underlying issues no doubt affected the record that he made.
FEDERAL SECURITIES LAWS, SLOWING THE GROWTH OF LIABILITY AND REVERSING THE TAKEOVER OF
STATE CORPORATE LAW. POWELL’S EMERGENCE AS THE COURT’S SECURITIES LAW LEADER PRODUCED
A COUNTER-REVOLUTION IN THE FEDERAL SECURITIES LAWS.

THIS ARTICLE PROCEEDS IN SEVEN PARTS. PART ONE PROVIDES BACKGROUND ON POWELL’S
career before his nomination to the Supreme Court. PART TWO DEMONSTRATES THE
LEADERSHIP ROLE THAT POWELL PLAYED ON THE SUPREME COURT IN THE FIELD OF SECURITIES LAW.
THE REMAINDER OF THE ARTICLE IS ORGANIZED BY GENERAL THEMES IN POWELL’S WORK IN SECURITIES
CASES. PART THREE DESCRIBES POWELL’S EFFORTS TO MINIMIZE LIABILITY EXPOSURE UNDER THE
SECURITIES LAW. IT FOCUSES ON CASES DEFINING “SALE,” AS WELL AS THE ELEMENTS OF RULE 10b-5,
REPRESENTATIVE ACTIONS, AND THE IMPLICATION OF PRIVATE RIGHTS OF ACTION. PART FOUR
EXAMINES POWELL’S PREFERENCE FOR PREDICTABILITY IN THE SECURITIES LAWS ALLOWING LAWYERS
TO ADVISE THEIR CLIENTS OF THEIR DUTIES UNDER THOSE LAWS. THE TENSION BETWEEN
PREDICTABILITY AND THE DESIRE TO LIMIT LIABILITY IS DISCUSSED IN THE CONTEXT OF CASES DEFINING
“SECURITIES.” PART FIVE EXAMINES POWELL’S PROTECTION OF LOCAL BUSINESS FROM THE THREAT OF
HOSTILE TAKEOVER. PART SIX Focuses ON POWELL’S SKEPTICISM TOWARD THE SECURITIES AND
EXCHANGE COMMISSION’S EFFORTS TO EXPAND ITS AUTHORITY, FOCUSING IN PARTICULAR ON HIS
INSIDER TRADING OPINIONS. PART SEVEN CONCLUDES.

PART ONE: EXPERIENCE AND OUTLOOK

APART FROM WILLIAM O. DOUGLAS, WHO SERVED AS CHAIRMAN OF THE SEC BEFORE HIS
Nomination to the Supreme Court, LEWIS POWELL IS THE ONLY SECURITIES LAWYER TO SERVE ON
THE COURT SINCE THE FEDERAL SECURITIES LAWS WERE PASSED IN 1933 AND 1934. WHILE OTHER
JUSTICES HAD PRIVATE PRACTICE EXPERIENCE, NONE HAD THE LEVEL OF HANDS-ON EXPERIENCE WITH THE FEDERAL SECURITIES LAWS THAT POWELL DID. POWELL’S EXPERIENCE AS A CORPORATE LAWYER HAD AN ENORMOUS IMPACT ON HIS WORK AS A JUSTICE IN SECURITIES LAW. THIS PART GIVES A FLAVOR OF THAT PRACTICE. I ALSO DISCUSS HOW POWELL’S YEARS IN PRACTICE Affected HIS VIEWS ON REGULATION AND MOTIVATED HIS INVOLVEMENT IN POLITICS. THOSE YEARS IN PRACTICE WOULD PROFOUNDLY SHAPE POWELL’S WORK IN SECURITIES LAW DURING HIS TIME ON THE COURT.

A. PRACTICE

LEWIS POWELL WAS BORN AND RAISED IN RICHMOND, VIRGINIA. WHEN HE COMPLETED HIS LEGAL EDUCATION IN 1932, POWELL TURNED DOWN AN OFFER OF $150 A MONTH TO JOIN THE DAVIS, POLK FIRM IN NEW YORK, INSTEAD GOING TO CHRISTIAN, BARTON AND PARKER IN RICHMOND FOR A MONTHLY SALARY OF $50. NO OTHER FIRM IN TOWN WOULD OFFER HIM EVEN AN OFFICE IN THE LEAN YEARS OF THE DEPRESSION. HE LEFT TWO YEARS LATER TO JOIN HUNTON & WILLIAMS, WHERE HE PRACTICED (INTERRUPTED ONLY BY MILITARY SERVICE) UNTIL HIS NOMINATION TO THE SUPREME COURT IN 1971. HUNTON & WILLIAMS WAS RICHMOND’S LEADING FIRM AND POWELL, A CONSUMMATE RAINMAKER, BECAME ITS DOMINANT PARTNER.

POWELL BEGAN HIS CAREER AS A LITIGATOR. IN HIS FIRST MAJOR CASE, A FIDUCIARY CLAIM,

17Powell took his law degree at Washington & Lee before getting an LLM from Harvard. Jeffries, supra note, at 36-42.
18Memorandum from Lewis F. Powell, Jr. to Joe Carter, Hunton & Williams History, at 3 (August 1977).
19Telephone Interview with Larry Blanchard (March 22, 2002) (describing Powell as a “master at making connections”).
20Jeffries, supra note, at 187. Powell’s abilities evidently were apparent from the beginning. When Powell was just beginning as a lawyer, his first boss, Andrew Christian, told Morton G. Thalhimer (a department store owner who would later become a client of Powell’s): “Mark my words. Our mutual friend, Lewis Powell, is going to go the very top of the legal profession. He is one of the most brilliant men I have ever had the privilege of meeting and one of the nicest.” Letter from Morton G. Thalhimer to Lewis F. Powell, Jr. (March 17, 1976).
HE REPRESENTED THE RECEIVER OF A FAILED BANK AGAINST ITS FORMER DIRECTORS.\textsuperscript{21} HIS CASES WERE A TYPICAL MIX, INCLUDING NEGLIGENCE CASES AGAINST THE SOUTHERN RAILWAY,\textsuperscript{22} A TAX CASE FOR A REAL ESTATE DEVELOPER, \textsuperscript{23} A PATENT INFRINGEMENT CASE FOR GENERAL MOTORS,\textsuperscript{24} RAILROAD REORGANIZATIONS,\textsuperscript{25} AND LITIGATION OVER A STOCK SUBSCRIPTION AGREEMENT.\textsuperscript{26} POWELL LOST HIS ONE CASE IN THE SUPREME COURT, A CONSTITUTIONAL CHALLENGE TO AN “ENTRANCE FEE” THAT VIRGINIA IMPOSED ON FOREIGN CORPORATIONS WISHING TO DO BUSINESS IN THE STATE.\textsuperscript{27} POWELL CONTINUED TO LITIGATE CASES THROUGHOUT HIS CAREER, WINNING HIS LAST ONE, AN ANTITRUST CHALLENGE BY THE JUSTICE DEPARTMENT TO UNITED VIRGINIA BANK’S ACQUISITION OF A LOCAL BANK; THE TRIAL CONCLUDED JUST A FEW DAYS BEFORE POWELL’S NOMINATION TO THE COURT.\textsuperscript{28}

GRADUALLY, HOWEVER, POWELL MOVED TOWARD A “GENERAL BUSINESS PRACTICE”\textsuperscript{29} WITH CLIENTS RANGING FROM ESKIMO PIE TO PHILIP MORRIS.\textsuperscript{30} THIS PRACTICE WAS BUILT ON A FOUNDATION

\textsuperscript{21}Memo from L.F.P., Jr. to Jody, Penny, Molly and Lewis III, Unrecorded Biographical Facts About Your Father, at 5 (December 15, 1981).

\textsuperscript{22}Southern Railway Co. Barker, 173 Va. 313, 4 SE2d 395 (Va. 1939).

\textsuperscript{23}Camp v. Murray, 226 F.2d 931 (4th Cir. 1955).


\textsuperscript{25}Old Colony Bondholders v. New York, N.H. & H.R. Co., 161 F.2d 413 (2nd Cir. 1947).

\textsuperscript{26}Marcuse v. Broad-Grace Arcade Corporation, 164 Va. 553, 180 S.E. 327 (Va. 1935).

\textsuperscript{27}Atlantic Refining Co. v. Virginia, 302 U.S. 22 (1937). Although he lost the case, Powell did win the admiration of opposing counsel in getting the Court to hear it at all. Letter from W.W. Martin to Lewis F. Powell, Jr., (May 20, 1936) (congratulating Powell on the grant of certiorari and “the most creditable manner by which you won this opportunity”).

\textsuperscript{28}Letter from Lewis F. Powell, Jr. to Robert P. Buford, May 24, 1973; Memorandum from Lewis F. Powell, Jr. to Joe Carter, Hunton & Williams History, at 19 (August 1977).

\textsuperscript{29}Letter from Lewis F. Powell, Jr. to Robert P. Buford, May 8, 1981.

\textsuperscript{30}Memorandum from Lewis F. Powell, Jr. to Joe Carter, Hunton & Williams History, at 21, 23 (August 1977). Powell never lost interest in the companies that he represented, continuing to read their annual reports during his time on the Court. Letter from Lewis F. Powell, Jr. to Paul H. Riley (January 5, 1976) (requesting the annual report of Commonwealth Natural
of securities work. According to Powell, “I file[d] two of the earliest registration statements filed from the Richmond area under the Act of ‘33. This qualified me as an ‘expert,’ with the result that I was retained to do a good deal of securities work.”

In a field that values precision, Powell developed a reputation for “meticulous” work. Powell’s work on registered offerings for Scott & Stringfellow (a local investment bank) led to other corporate work. Powell advised clients on the private offering exemption from registration under the Securities Act and corporate governance issues, drafted charter amendments for preferred stock issues, helped them wage proxy fights.

Gas Corporation). He also maintained his interest in investing, continuing to consult Harvie Wilkinson on stock recommendations. Letter from Lewis F. Powell, Jr. to J. Harvie Wilkinson, Jr. (March 25, 1982). Powell sold his stocks in companies subject to federal regulation upon joining the Court to limit the need for recusals. Letter from Lewis F. Powell, Jr. to John W. Riely (October 1, 1980). While he held a significant portfolio, Powell was not an active trader. He became quite defensive on the subject after newspaper accounts suggested that he was an active trader and that his stock ownership was causing a substantial number of recusals. Letter from Lewis F. Powell, Jr. to Steve Wermiel (June 15, 1981). Powell’s letter had a salutary effect, as the Journal wrote an article that Powell considered more balanced. Letter from Lewis F. Powell, Jr. to Stephen Wermiel (August 25, 1981) (thanking Wermiel for his “constructive” article).


32Telephone Interview with Larry Blanchard (March 22, 2002) (“The most meticulous securities lawyer I ever knew.”).

33Memorandum from Lewis F. Powell, Jr. to Joe Carter, Hunton & Williams History, at 10, 11, 13, 14 (August 1977).

34Memorandum to Messrs. James J. Ward and James E. Galleher from Lewis F. Powell, Jr. (10/5/40) (advising that “an offering to ten or fifteen institutions would clearly seem to be private, other things being consistent, whereas, an offering from twenty to twenty-five institutions may not be such a clear case.”).

35Letter from Lewis F. Powell, Jr. to Edwin B. Horner (March 22, 1957).

36Letter from Lewis F. Powell, Jr. to Martin Victor (November 15, 1946).
Battles, and set up life insurance companies and public utilities. In sum, Powell faced the broad range of issues handled by the typical corporate lawyer. Powell also did deals. Powell represented Miller & Rhoads (a local retailer) when it merged with Garfinckel, serving on the board of the merged company and acting as its general counsel. More prominently, Powell represented Albemarle (a small Virginia paper company) in its 1962 acquisition of Ethyl, a joint venture of General Motors and Standard Oil. Albemarle was Powell’s first major corporate client. Powell met its president, Floyd Gottwald, in the late 1940’s, when Powell represented an investment bank that was arranging a loan to Albemarle. Powell became Albemarle’s counsel shortly thereafter, joining its board in 1953. Gottwald had a flair for the audacious. At the time, the Ethyl transaction was

37 Letter from Lewis F. Powell, Jr. to Edwin Hyde (June 1, 1956).
38 Letter from Edwin B. Horner to Lewis F. Powell, Jr., (November 8, 1971) (“I remember vividly in your office the day you said, ‘You cannot start a life insurance company. You have done enough funny things.’ But at your desk First Colony was created.”).
39 Letter from Lewis F. Powell, Jr. to John W. Riely (October 1, 1980) (discussing the formation of Commonwealth Natural Resource).
40 He also found time to lecture to the Corporations class at the University of Richmond Law School “on the legal problems involved in the obtaining of public capital by corporations. This will include the registration of securities with the SEC, and also ‘intrastate within Virginia’ and ‘private placements.’” Letter from Lewis F. Powell, Jr. to William T. Muse (April 1, 1955). Powell also was a lecturer at the graduate business school at the University of Virginia. Letter from Francis L. Berkeley to Lewis F. Powell, Jr. (10 December 1954).
42 Jeffries’ account of this transaction can be found at Jeffries, supra note at 189-192.
43 Letter from Lewis F. Powell, Jr. to Mrs. F.D. Gottwald (August 16, 1982).
44 Letter from Lewis F. Powell, Jr. to F.D. Gottwald (January 5, 1954) (“Just about the nicest thing that happened to me during 1953 was being invited to join your board.”).
CALLED “Jonah swallowing the whale”; today, we would call it a leveraged buyout. Albemarle, with a net worth of $25 million and no background in the chemical industry, needed to borrow $200 million to acquire the much larger Ethyl, which would leave it with “an almost unheard of 85 to 90 per cent debt ratio.” Ethyl was closely held by General Motors and Standard Oil, but the holding made little strategic sense for those firms. Despite Albemarle’s small size, they were willing to give Gottwald a chance to get the deal done, apparently impressed by his vision and energy. Arranging the financing for this transaction was an enormous effort, involving a series of delicate negotiations and a fair amount of creativity. The acquisition was financed through four levels of financing: insurance companies lent the first $114 million; $16 million came from Chase Manhattan; General Motors and Standard Oil took back $20 million of the purchase price as debt; and $50 million in “Junior-Junior Notes”—subordinated debt accompanied by warrants—was sold to institutional investors. The transaction was complicated by the fact that Standard Oil insisted that its part in the negotiations be done in Nova Scotia so that its gain from the sale would constitute foreign income. Powell drafted the proxy statement for the Albemarle shareholders himself, “walking an extremely tight rope between disclosing enough but not too much.” “Too much” in this context


46Id. at 7, 18.

47Id. at 15.

48Id. at 5.

49Id. at 17.
Presumably meant unduly emphasizing the risks of this high stakes gamble by Albemarle. The deal’s success “astounded Wall Street” and cemented Hunton, Williams’ reputation as a corporate firm.\footnote{50}

Another milestone transaction was the aggregation of a number of regional banks to create United Virginia Bank (“UVB,” now part of SunTrust).\footnote{51} Lewis Powell’s best friend was Harvie Wilkinson, president of the State Planters Bank, headquartered in Richmond and Virginia’s largest bank.\footnote{52} Wilkinson arranged for Powell to serve as general counsel of the bank and Powell became a director in 1959.\footnote{53} Powell served as much as a business advisor as a lawyer; Wilkinson observed that Powell had more business sense than most businessmen that Wilkinson knew.\footnote{54}

Virginia had difficulty competing with other states to attract business because its fragmented banking structure did not allow for the large aggregation of capital necessary to finance business development.\footnote{55} Wilkinson wanted to create a larger bank, but that goal raised important strategic questions. Businesses and bankers in smaller communities such as Lynchburg and Danville were wary of the larger Richmond banks.

\footnote{50}{Lewis F. Powell, Jr., The Albemarle/Ethyl Deal in 1962: Addendum to Larry Blanchard’s Memorandum of August 1974 (July 3, 1975).}
\footnote{51}{Jeffries discusses this transaction at Jeffries, supra note 5, at 188.}
\footnote{52}{Wilkinson and Powell attended McGuire’s University School together and became reacquainted when both returned to Richmond after completing their education. William K. Klingaman, J. Harvie Wilkinson, Jr.: Virginian, Banker, Visionary 8, 73 (1994).}
\footnote{53}{Letter from J. Harvie Wilkinson, Jr. to Lewis F. Powell, Jr. (October 8, 1959).}
\footnote{54}{Telephone Interview with J. Harvie Wilkinson III, March 18, 2002.}
\footnote{55}{Klingaman, supra note at 89-95.}
RATHER THAN MERGING THE DISPARATE BANKS INTO ONE COMPANY, WILKINSON AND POWELL SETTLED ON A HOLDING COMPANY STRUCTURE. THIS STRUCTURE NOT ONLY ALLOWED FOR THE BANKS TO RETAIN THEIR LOCAL IDENTITIES, BUT ALSO ALLOWED MANAGEMENT OF THE ACQUIRED BANKS TO RETAIN THEIR POSITIONS, THUS NEATLY SIDESTEPPING A POTENTIAL OBSTACLE TO THE PLAN. \(^56\)

TO ACHIEVE THE GOAL OF A STATE-WIDE BANK, HOWEVER, REQUIRED A CHANGE IN VIRGINIA LAW. \(^57\) FORTUNATELY, POWELL MOVED EASILY AMONG VIRGINIA’S POLITICAL, LEGAL AND BUSINESS CIRCLES. HE NOT ONLY DRAFTED THE NECESSARY LEGISLATION, HE LOBBIED THE VIRGINIA GENERAL ASSEMBLY ON ITS BEHALF, TESTIFYING AT COMMITTEE HEARINGS. \(^58\) HE ALSO PARTICIPATED IN THE NEGOTIATIONS WITH THE BANKS TO BE JOINED UNDER THE HOLDING COMPANY’S UMBRELLA. \(^59\) POWELL, AS HE DID FOR MANY CLIENTS, \(^60\) SERVED ON THE BOARD OF UVB, RESIGNING ONLY AFTER HIS NOMINATION TO THE COURT. \(^61\)

POWELL’S POLITICAL TIES BENEFITED NOT ONLY UVB, BUT ALSO HIS OTHER CLIENTS, AND HE CAREFULLY MAINTAINED THOSE TIES. EXPLAINING TO WILKINSON’S SON WHY HE COULDN’T SUPPORT HIS CANDIDACY FOR CONGRESS, POWELL WROTE:

**I FEEL MORALLY OBLIGATED TO SUPPORT DAVE SATTERFIELD. HE HAS BEEN EXTREMELY**

\(^56\)Klingaman, supra note at 94-98.

\(^57\)Memorandum from Lewis F. Powell, Jr. to Joe Carter, *Hunton & Williams History*, at 17 (August 1977).

\(^58\)Id. at 18.

\(^59\)Telephone Interview with J. Harvie Wilkinson III, March 18, 2002.

\(^60\)Memorandum from Lewis F. Powell, Jr. to Joe Carter, *Hunton & Williams History*, at 30 (August 1977)(“I served on the boards of directors of a high percentage of my corporate clients. Where the client is a Virginia corporation, the lawyer responsible for its general legal work often can be most useful if he serves on the board. Moreover, many clients find that lawyers make constructive directors. . . . perhaps the single best way to retain client loyalty, as well as serve the client, was to be an active member of its board.”).

\(^61\)Klingaman, supra note at 101.
HELPFUL TO IMPORTANT CLIENTS OF HUNTON, WILLIAMS FOR WHOM I AM RESPONSIBLE. HE HAS GONE FAR BEYOND THE ORDINARY “CALL OF DUTY” OF A CONGRESSMAN TO SUPPORT CONSTITUENTS. THE HOUSE IS NOW CONSIDERING LEGISLATION WHICH – QUITE LITERALLY – IS A MATTER OF LIFE AND DEATH TO A SIGNIFICANT PART OF ETHYL CORPORATION’S BUSINESS. MY TEAM HERE – INCLUDING MYSELF PERSONALLY – HAS BEEN WORKING INTIMATELY WITH DAVE (ALMOST DAILY) TO AMEND THE MOST OBJECTIONABLE FEATURES OF THE PROPOSED LAW. HE IS A MEMBER, WITH SOME SENIORITY NOW, OF THE IMPORTANT COMMITTEE ON INTERSTATE COMMERCE – A COMMITTEE WHICH DEALS WITH A NUMBER OF MATTERS OF VITAL INTEREST TO OUR MAJOR CLIENTS.  

BEING THE LEADING LAWYER IN RICHMOND REQUIRED A TOTAL COMMITMENT. 

POWELL BOLSTERED HIS POLITICAL CONNECTIONS THROUGH HEAVY INVOLVEMENT IN CIVIC AFFAIRS. IN ADDITION TO HIS INVOLVEMENT WITH THE AMERICAN BAR ASSOCIATION (OF WHICH HE EVENTUALLY BECAME THE PRESIDENT), POWELL ALSO PLAYED A NUMBER OF ROLES WITH THE LOCAL CHAMBER OF COMMERCE, BECOMING ITS VICE-PRESIDENT IN 1948 AND ITS PRESIDENT FOUR YEARS LATER. POWELL’S CONNECTIONS WOULD PROVE INVALUABLE IN HIS EFFORTS TO REFORM RICHMOND’S PUBLIC SCHOOLS AND KEEP THEIR DOORS OPEN IN THE FACE OF DESEGREGATION. POWELL’S WIDE INVOLVEMENT IN CIVIC AFFAIRS PRODUCED THE “POSITIVE BY-PRODUCT” OF ESTABLISHING HIS NAME AMONG PROSPECTIVE CLIENTS AS WELL.  

POWELL’S WORK WITH BUSINESSMEN IN COMMUNITY AFFAIRS MADE HIM A STRONG DEFENDER  

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62 Letter from Lewis F. Powell, Jr. to J. Harvie Wilkinson, III (April 28, 1970). Wilkinson III bounced back from his electoral defeat to later clerk for Powell on the Supreme Court and now serves as the Chief Judge of the Fourth Circuit.  

63 Memorandum from Lewis F. Powell, Jr. to Joe Carter, Hunton & Williams History, at 28 (August 1977).  

64 Letter from Morton Thalhimer to Lewis F. Powell, Jr. (Feb. 16, 1948).  

65 Jeffries, supra note , at 124.  

66 Jeffries, supra note , at 131-180.  

67 Memorandum from Lewis F. Powell, Jr. to Joe Carter, Hunton & Williams History, at 8 (August 1977).

W R ITING ABOUT HIS FRIEND HARVIE WILKINSON, POWELL REFLECTED: “IT IS FASHIONABLE TO CRITICIZE BUSINESSMEN AS BEING INTERESTED ONLY IN MAKING MONEY FOR STOCKHOLDERS. I HAVE NEVER THOUGHT THIS WAS A FAIR OR EVEN HONEST GENERALIZATION. THE LEADING BUSINESSMEN IN MOST COMMUNITIES ALSO ARE AMONG THE LEADERS IN CIVIC, EDUCATIONAL, CHARITABLE AND CULTURAL AFFAIRS.” SOME MIGHT THINK THAT DESCRIBING A BUSINESSMAN “AS BEING INTERESTED ONLY IN MAKING MONEY FOR STOCKHOLDERS” WAS MEANT AS PRAISE. POWELL, HOWEVER, SAW THE ROLE OF BUSINESS THROUGH THE LENS OF HIS CIVIC INVOLVEMENT:

THE FREE ENTERPRISE SYSTEM IS NOW UNDER WIDE-RANGING ATTACK FROM MANY IN THE MEDIA, IN POLITICS, AND ON THE CAMPUS. YOUNG PEOPLE ARE NO LONGER TAUGHT IN SCHOOLS AND COLLEGES THAT THIS SYSTEM - AND ONLY THIS SYSTEM - ENABLED AMERICA TO ACHIEVE ITS GREATNESS. THERE ARE MANY WHO WOULD SUBSTITUTE A STULTIFYING SOCIALISM, LEADING US DOWN THE ROAD WHICH ENGLAND IS FOLLOWING SO DISASTROUSLY. IN A SOCIALISTIC SYSTEM, THERE WOULD BE NO ROOM FOR MEN LIKE HARVIE WILKINSON. THE GREAT THINGS THAT HE HAD DONE TO IMPROVE THE WELL BEING OF HIS FELLOW MAN WOULD BE RELEGATED TO FACELESS BUREAUCRATS.

POWELL WAS A FIERCE OPPONENT OF SOCIALISM THROUGHOUT HIS CAREER, PARTICULARLY OBJECTING

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68Letter from Lewis F. Powell, Jr. to Morton G. Thalhimer (November 27, 1951). Prior to that time, there had been lapses, which had played a role in the rise of the regulatory state, Powell thought:

[T]he comparative lack of morals in business during the latter part of the Nineteenth Century [which] caused a great deal of public and private criticism of business, and resulted in the era of governmental regulation of business. This same situation developed again following the boom of the Twenties and the collapse of the early Thirties.

Id.

69Letter from Lewis F. Powell, Jr. to Virginius Dabney (June 3, 1975).

70Id.
Justice Powell and the Counter-Revolution

TO THE USE OF THE COURTS TO REDISTRIBUT WEALTH.\textsuperscript{71}

\textbf{Powell’s hostility to socialism (along with his hawkish views on national defense) appears to have driven his involvement in national politics. While he was a “Virginia Democrat” in local elections,\textsuperscript{72} he campaigned for Republican presidential candidates.\textsuperscript{73} Powell feared Roosevelt’s vendetta against the capitalist system: “I really cannot tell you how strongly I feel that the welfare of this country requires the defeat of Mr. Roosevelt[...], and the election of a man who is sympathetic (rather than antagonistic) to the system of private profit which has enabled this country to attain its present greatness.”\textsuperscript{74} Powell also lobbied against Roosevelt’s “Court packing” plan.\textsuperscript{75} Powell similarly feared Harry Truman and Adlai Stevenson’s “left-wing socialism.”\textsuperscript{76} Powell campaigned for Eisenhower, helping to organize the Virginia Democrats for Eisenhower.\textsuperscript{77}

\textsuperscript{71}Memorandum from Lewis F. Powell, Jr. to Joe Carter, \textit{Hunton & Williams History}, at 31 (August 1977) (“Unfortunately, government grows ever larger and more intrusive; the legislative branch enacts laws at every session that both require and stimulate litigation; and, increasingly, the judicial system is exploited for the redistribution of wealth – despite the inherent inequity in such a process.”).

\textsuperscript{72}Powell’s work on behalf of local Democrats was limited to financial support and some speeches on behalf of politicians who were friends. Letter from Lewis F. Powell, Jr. to Colgate W. Darden, Jr. (March 15, 1976).

\textsuperscript{73}Memo from L.F.P., Jr. to Jody, Penny, Molly and Lewis III, Unrecorded Biographical Facts About Your Father, at 9 (December 15, 1981).

\textsuperscript{74}Letter to Henry C. Riely (10/5/40).

\textsuperscript{75}Letter from Lewis F. Powell, Jr. to Senator Burton K. Wheeler (March 25, 1937) (noting that “I am doing what I can in a quiet way to stimulate activity against this attack on the Supreme Court.”).

\textsuperscript{76}Letter from Lewis F. Powell, Jr. to Senator Harry F. Byrd (October 15, 1952) (“Stevenson will be more successful than Truman in obtaining the passage of pet left-wing legislation such as the FEPC, socialized medicine, continued deficit spending, higher taxes and the like. In short, the trend toward socialism will inevitably be accelerated if Stevenson is elected.”).

\textsuperscript{77}Letter from Lewis F. Powell, Jr. to Webster S. Rhoads (October 13, 1952) (“I am now in this campaign up to my neck. With the indulgence of my partners and my clients, I am averaging only three or four per day practicing law. The remainder of my time, usually until about midnight, is devoted to the campaign.”). Powell also campaigned for Eisenhower in 1956. Letter from Lewis F. Powell, Jr. to Senator Harry F. Byrd (October 10, 1956) (“if Stevenson should
AND ALSO SUPPORTED Richard Nixon, who appointed him to the Supreme Court.\textsuperscript{78}

\textbf{C. SUMMARY}

Powell’s career as a practicing lawyer laid the groundwork for the influence he would later have on the Court in securities cases. Powell was an experienced corporate lawyer, who also had an extensive litigation practice on behalf of corporate clients. Those experiences would be an important influence on Powell (and by the extension, the Supreme Court as a whole). Powell’s political activities were generally pragmatic, premised on serving the needs of his clients, but his involvement in national politics was ideologically motivated. Powell’s close interaction with businessmen led him to trust their character. That trust, in turn, made him generally hostile to “excessive” regulation,

\textsuperscript{78}Letter from Lewis F. Powell, Jr. to Winthrop Rockefeller (September 19, 1968); Letter from Lewis F. Powell, Jr. to Pvt. James Harvie Wilkinson, III (October 20, 1968) (“I am afraid Virginia is going for Humphrey . . . The idiot vote – and lots of otherwise sensible votes – will go to Wallace; the Negro bloc and the straight-ticket Democrats will, of course, go for Humphrey.”); Letter from Lewis F. Powell, Jr. to Richard M. Nixon (October 27, 1960) (“I appreciate very much your letter concerning my support in the campaign. I want you to know that I think, regardless of the outcome, that you are making a magnificent effort against the most formidable odds. I have also been proud of the way in which you have stood by your principles, and not endeavored to ‘out promise’ your opponent.”).

Powell’s appointment to the Court put an end to active involvement in politics, but not his interest. Letter from Lewis F. Powell, Jr. to J. Harvie Wilkinson, Jr. (November 4, 1980) (“I write this on election day, with ‘butterflies’ very much in my tummy.”). Powell’s abstention from politics extended to not voting. Letter from Lewis F. Powell, Jr. to Harry F. Byrd, Jr. (December 27, 1980). He did, however, continue to advise Senator Byrd on political issues. Id. (advising that Byrd join the Republican Party); Letter from Harry F. Byrd, Jr. to Lewis F. Powell, Jr. (November 21, 1980) (letter soliciting Powell’s views on points to be made to President-elect Reagan; Powell notes that “Harry came to my chambers and we had an interesting, off-the-record discussion.”). He was pleased by Nixon’s victory over McGovern. Letter from Lewis F. Powell, Jr. to Edwin Hyde (November 8, 1972). He strongly favored Ronald Reagan over Jimmy Carter. Letter from Lewis F. Powell, Jr. to Virginius Dabney, George Gibson and J. Harvie Wilkinson, Jr. (November 18, 1980) (“[M]y relief that the country will not be in such inept hands for the next four years is tempered by the fear that our economic problems are too intractable to be resolved in the short term by any government. . . . I do think that the federal judiciary will benefit substantially from the change in administration.”). He worried, however, about the boldness of some of Reagan’s policies. Letter from Lewis F. Powell, Jr. to J. Harvie Wilkinson, Jr. (April 8, 1982) (“Granted that the President has inherited much of his economic problems from the excesses of a welfare state from Roosevelt through Carter, and from a world-wide recession, it does seem to me that Reagan’s simplistic notions have been carried to a dangerous extreme.”).

17
WHICH HE SAW AS AN INFRINGEMENT ON FREE ENTERPRISE AND THE FIRST STEP DOWN THE PATH TOWARD SOCIALISM.

**PART TWO:  POWELL’S INFLUENCE**

**Powell**’s experience as a corporate lawyer lent him credibility with his colleagues in securities law cases, and Powell worked diligently to maximize that influence. Powell came well prepared to conferences in securities cases, with the often-complicated facts mastered and a carefully thought-out analysis reduced to writing. 79 Powell believed in hard work and organization, and his thorough preparation may have given him an advantage in the Court’s deliberations. In a frequently-technical area where most of the justices were unlikely to have strongly-held views, Powell’s superior knowledge and preparation were a powerful force. And Powell was not afraid to use that influence from his earliest time on the Court. Unlike many areas of the Court’s docket that Powell was confronting for the first time, he knew securities law and was confident of his views. 80 Those views remained very much informed by his experience as corporate counsel. 81

Consider the first securities case in which Powell participated, *Kern County Land*...
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CO. v. OCCIDENTAL PETROLEUM. 82  The Court split 4-4 at conference, with Justice White passing. 83  After sending White a memo on the merits, Powell – not content to wait on White’s response – sent a memo to his law clerk the next day, instructing him to begin working on an opinion. 84  Powell explained that “As I led the discussion at the Conference, I would think the chances are good that the opinion would be assigned to me if we have a majority. If I am in the minority, I will wish to dissent.” As a strategic matter, Powell noted that “[T]here is obvious advantage in our circulating a draft at a fairly early date.” 85  Being first to write his chances of getting the crucial fifth vote. This memo from Powell’s first securities case strikes a note that would become familiar in subsequent cases – Powell leading the discussion and expecting to write the opinion in his area of expertise. 86

Within a few years, Powell was also confident in his role as the Court’s securities


83Conf. Notes, 71-1059 Kern Cty. v. Occidental, Conf. 12/8/72. Powell’s note indicate that Justice Blackmun tentatively voted to reverse, but subsequently switched his vote.

84Memorandum from Lewis F. Powell, Jr. to Mr. William C. Kelly, Jr., No. 71-1059 Kern County Land Co. v. Occidental, (December 10, 1972).

85Id. at 1.

86Powell did not hesitate to remind his colleagues of his superior experience. Objecting to passage in an opinion by Burger characterizing bank as lending money to “obtain” the pledge of securities, Powell invoked his work as counsel to State Planters and United Virginia Bank.

Any bank officer who makes a loan for the purpose of obtaining an inchoate interest in collateral should be fired. Collateral may be indispensable to the extension of credit, but lending officers of the bank I represented were instructed never to make a loan on the assumption that it probably could be repaid only by liquidating the borrower’s collateral.

Consider the following passage from a memo in *Piper v. Chris-Craft Industries*:

**If I should vote with the majority, there is a fair possibility — I would guess — that the opinion would be assigned to me in view of my having written several SEC cases. In view of the relevance of *Ernst and Ernst* to a central issue in this case, the Conference will expect me to take the lead in advising the Conference whether the standard of liability imposed by CA2 (see Judge Timber’s opinion) is compatible with the standard we adopted in *Ernst and Ernst*.**

After only four years on the Court, Powell had established the securities laws as his domain. As it happened, however, Powell’s expectation that the case would be assigned to him proved wrong, as the Chief Justice kept it for himself.

More often, Powell’s hard work in preparation for conference was rewarded with the opinion assignment. Not only did Powell write some of the most important cases during his tenure, he dominated in sheer numbers, writing 25% (11/41) of the majority opinions in securities cases in which he participated which is more than any other Justice during that period. As the chart below demonstrates, Powell rarely found himself in the minority. Of the 41 securities cases in which Powell participated on the merits, he dissented only once.

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88 The Court sidestepped the scienter issue, instead holding that the Williams Act did not provide a cause of action for damages to a defeated bidder in a takeover contest. See text at infra notes.


Burger has the same percentage of votes in the majority as Powell over this period, but his percentage is inflated by his not infrequent practice of reserving his vote until a majority emerged so he could assign the opinion.
**Supreme Court Federal Securities Law Decisions During Lewis F. Powell, Jr.’s Tenure**

<table>
<thead>
<tr>
<th>Justice</th>
<th>Case S</th>
<th>For Cert.</th>
<th>Majority</th>
<th>Majority Opinions</th>
<th>Disse nt</th>
<th>Majority %</th>
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<tbody>
<tr>
<td>Lewis F. Powell, Jr.</td>
<td>41</td>
<td>40</td>
<td>40</td>
<td>11</td>
<td>1</td>
<td>98%</td>
</tr>
<tr>
<td>Antonin Scalia</td>
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<td>2</td>
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<tr>
<td>Sandra Day</td>
<td>11</td>
<td>6</td>
<td>11</td>
<td>2</td>
<td>0</td>
<td>100%</td>
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<td>O’Connor</td>
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<tr>
<td>John Paul Stevens</td>
<td>32</td>
<td>16</td>
<td>25</td>
<td>3</td>
<td>7</td>
<td>78%</td>
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<tr>
<td>William H. Rehnquist</td>
<td>44</td>
<td>29</td>
<td>42</td>
<td>4</td>
<td>2</td>
<td>95%</td>
</tr>
<tr>
<td>Harry A. Blackmun</td>
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<td>38</td>
<td>4</td>
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<tr>
<td>Warren E. Burger</td>
<td>43</td>
<td>26</td>
<td>42</td>
<td>8</td>
<td>1</td>
<td>98%</td>
</tr>
<tr>
<td>Thurgood Marshall</td>
<td>45</td>
<td>19</td>
<td>32</td>
<td>4</td>
<td>13</td>
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<tr>
<td>Byron R. White</td>
<td>46</td>
<td>35</td>
<td>39</td>
<td>3</td>
<td>7</td>
<td>85%</td>
</tr>
<tr>
<td>Potter Stewart</td>
<td>32</td>
<td>23</td>
<td>30</td>
<td>4</td>
<td>2</td>
<td>94%</td>
</tr>
<tr>
<td>William J. Brennan, Jr.</td>
<td>46</td>
<td>24</td>
<td>27</td>
<td>3</td>
<td>19</td>
<td>59%</td>
</tr>
<tr>
<td>William O. Douglas</td>
<td>11</td>
<td>5</td>
<td>2</td>
<td>0</td>
<td>9</td>
<td>18%</td>
</tr>
</tbody>
</table>

This record of success is more remarkable when one considers that Powell consistently took the most conservative position of any justice in securities cases. In Powell’s more-widely noticed constitutional law opinions, he often found the middle ground in some multi-factor balancing test that may have had stronger roots in political expediency than in constitutional principle. Not surprisingly, this gave Powell a reputation among Court followers as a “swing vote.” That description does not fit Powell’s work in the

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90 Jeffries, supra note at 560-561.
FIELD OF SECURITIES LAW; HE WAS A FIXTURE IN THE MAJORITY, BUT IT WAS A CONSISTENTLY
CONSERVATIVE MAJORITY.

POWELL WAS PROUD OF THE WORK THAT HE WAS DOING TO CURB THE SEC AND THE
PLAINTIFFS’ BAR AND PLEASED BY THE RECEPTION THAT HIS WORK RECEIVED AMONG HIS FRIENDS IN THE
CORPORATE BAR. WRITING TO HIS FORMER LAW CLERK, POWELL NOTED THAT:

[T]HE HARVARD LAW REVIEW . . . DID A REAL HATCHET JOB ON ERNST & ERNST. THAT
PART OF THE SUPREME COURT REVIEW MUST HAVE BEEN WRITTEN BY A SUMMER
INTERN AT THE SEC. THE EXPERIENCED CORPORATE BAR (MANY OF WHOM SPOKE TO
ME AT THE ABA MEETING IN ATLANTA AND ALSO AT THE VIRGINIA BAR MEETING)
VIEW ERNST & ERNST AS A LANDMARK DECISION, THE RESULT BEING COMPELLED BY THE
LANGUAGE, LEGISLATIVE HISTORY AND STRUCTURE OF THE ACT. I REMAIN MORE THAN
CONTENT WITH THE OPINION.\textsuperscript{91}

POWELL’S AUDIENCE FOR HIS WORK WAS PRACTICING LAWYERS, NOT LAW STUDENTS.\textsuperscript{92}

Perhaps Powell’s success in bringing the Court to narrow the scope of the securities
laws stemmed from the fact that there was no one on the other side to pose a
counterweight to Powell’s views. Of the 41 cases in which Powell participated, only four
involved five-four votes. Douglas had been chairman of the SEC, but he was a marginal
figure by the time Powell joined the Court, and he retired early in Powell’s tenure.
Brennan served during Powell’s entire tenure and opposed Powell in securities cases more
that any other justice, but Brennan did not have Powell’s interest or experience in the
securities laws. Brennan’s undisputed intellect and coalition-building skills were saved

\textsuperscript{91} Letter to Gregory K. Palm from Lewis F. Powell, Jr. (January 1, 1977). The “hatchet job” is Narrowing Liability under
the 1934 Act, 90 Harv. L. Rev. 255 (1976).

\textsuperscript{92} Judges apparently were also part of that audience. Powell sent a copy of Ernst & Ernst to Henry Friendly, telling
Friendly that his “opinions and writing contributed significantly to our resolution of . . . [the] case[].” Letter from Lewis
F. Powell, Jr. to Henry J. Friendly (April 6, 1976). Friendly responded that he “was delighted both at the result and at your
for more politically-charged cases, leaving the securities law as Powell’s domain. This may have been a shrewd strategic choice on Brennan’s part; by letting Powell have his way in the cases that he cared about, Brennan may have built a reservoir of good will that he could tap in the cases that he cared most about.

Powell’s influence was felt not only through his opinions and affect on outcomes, but also in the Court’s agenda. The chart also demonstrates that Powell, more than any other justice, was responsible for the substantial number of securities law cases the Court heard during his tenure. From 1933 to 1971, the Court decided thirty securities cases, an average of less than one per term.\(^\text{93}\) The Court averaged three securities cases per term for the fifteen full terms that Powell sat on the Court. Powell voted to grant certiorari in 40 of the 46 securities cases granted during his time on the Court (and three cases heard the term following his retirement). In the fifteen terms since Powell’s retirement, the Court has heard only seventeen securities cases, an average of slightly more than one per term.\(^\text{94}\) While the smaller docket since Powell’s retirement accounts for some of this decline, the Court’s diminished interest in the securities law persists even after the numbers are adjusted to reflect the smaller overall docket. During Powell’s

\(^{93}\)H.W. Perry quotes an anonymous justice on this point: “there was a time when four members simply weren’t interest in hearing Securities and Exchange Commission cases . . . Now I believe the Court is more disposed to hearing those cases.” Perry, supra note at 261. Perry also quotes an anonymous justice for the proposition that “Justice [unnamed] is intensely interested in the securities area.” Id. at 262. Although this is speculation, the unnamed justice is almost certainly Powell.

\(^{94}\)If OT ‘87 is excluded, during which three cases in which Powell voted to grant certiorari were heard, the average drops below one per term. From 1934 to 1971, the Court averaged less than one securities case per term.
TENURE, SECURITIES CASES WERE 2% OF THE COURT’S DOCKET; SINCE HIS RETIREMENT, SECURITIES CASES HAVE MADE UP ONLY 1%. 95

POWELL ENHANCED HIS INFLUENCE OVER THE COURT’S DOCKET WITH HIS WILLINGNESS TO WRITE DISSENTS FROM THE DENIAL OF CERTIORARI IN SECURITIES CASES. 96 POWELL WROTE FIVE SUCH DISSENTS DURING HIS TIME ON THE COURT, PERSUADING THE COURT TO GRANT CERTIORARI FOUR TIMES. 97 OTHER JUSTICES WROTE ONLY FOUR DISSENTS FROM DENIAL IN SECURITIES CASES DURING POWELL’S TENURE, AND NONE OF THOSE RESULTED IN A GRANT OF CERTIORARI. 98 SINCE POWELL’S

95 Totals are taken from the Harvard Law Review’s annual Supreme Court volume.

96 It was also not unusual for Powell to note on certiorari memoranda that he would “write if not granted.” See, e.g., Preliminary Memo, International Brotherhood of Teamsters v. Daniel, Nos. 77-753 and 77-754 (February 1, 1978 Conference) (Powell’s marginal notes); Preliminary Memorandum, No. 82-276, Dirks v. SEC (November 12, 1982 Conference) (Powell’s marginal notes) (same) Preliminary Memorandum, Shearson/American Express, Inc. v. McMahon, No. 86-44-CFX, (September 29, 1986 Conference) (Powell notes: “If denied, I may write.”).

97 2nd Draft, United Housing Foundation, Inc. v. Forman, Nos. 74-157 and 74-647, at 1 (Powell, J., dissenting) (Jan. 16, 1974); 1st Draft, Transamerica Mortgage Advisors, Inc. v. Lewis, Nos. 77-1645 and 77-1717 (Powell, J., dissenting from the denial of certiorari) (12 October 1978); John Nuveen & Co., Inc. v. Sanders, 450 U.S. 1005 (1981) (Powell, J., joined by Rehnquist, dissenting from the denial of certiorari); Draft, Carpenter et al. v. United States, No. 86-422, at 1 (Powell, J., dissenting from the denial of certiorari) (December 10, 1986); First Draft, Pinter v. Dahl, No. 86-805 (Powell, J., dissenting from denial of certiorari). Powell’s failure to persuade his colleagues to grant certiorari in Nuveen may be explained by the fact that Justice Stevens had written the relevant lower court decision while a judge on the Seventh Circuit. 554 F.2d 790 (7th Cir. 1977).

It is apparently not unusual for dissents from denials to result in a grant of certiorari. H.W. Perry, Jr., Deciding to Decide: Agenda Setting in the United States Supreme Court 170 (1991) (quoting an anonymous justice: “Many times a dissent from denial will pick up a fourth vote.”). Perry got estimates that ten to thirty dissents from denial per term picked up additional votes. Id. at 173. Powell does not appear to have carried over this willingness to write at the certiorari stage to other areas; he was less likely to write dissents from denial than most of his colleagues. Id. at 186-187 (reporting number of dissents from denial for period 1976-1980: Brennan, White, Marshall, Blackmun and Rehnquist all wrote more dissents than Powell).

98 The one that stands out is Mordaunt v. Incomco, 469 U.S. 1115 (1985) (White, J., joined by Burger and Brennan, dissenting from the denial of certiorari), which raised the issue of whether horizontal commonality was required for an investment contract. Powell was absent from the Court at the time due to complications from surgery. It is inconceivable that he would have voted against hearing the case, given the clear conflict and the importance of the issue. It remains unresolved. The other three are: Dupuy v. Dupuy, 434 U.S. 911 (1977) (White, J., dissenting) (standard of care required of plaintiffs in Rule 10b-5 actions); Sennott v. Rodman & Renshaw, 414 U.S. 926 (1973) (Douglas, J., joined by Blackmun, dissenting from the denial of certiorari) (standard for control person liability under Section 20(a) of the Exchange Act); Yeomans v. Kentucky, 423 U.S. 983 (1975) (Brennan, J., dissenting from the denial of certiorari); (sovereign immunity in a securities case).
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RETIREMENT, ONLY ONE SECURITIES CASE HAS RESULTED IN A PUBLISHED DISSENT FROM THE DENIAL OF CERTIORARI.99

POWELL’S INFLUENCE OVER THE COURT’S DOCKET PERSISTED TO THE END OF HIS CAREER AND EVEN WHEN HIS ARGUMENTS WERE WEAK. POWELL’S LAST SECURITIES LAW OPINION DURING HIS COURT TENURE WAS A DISSENT FROM DENIAL THAT PERSUADED HIS COLLEAGUES TO GRANT REVIEW (HIS SECOND OF THE TERM).100 PINTER V. DAHL RAISED THE ISSUE OF THE APPLICATION OF THE IN PARI DELICTO DEFENSE.101 DAHL PURCHASED INTERESTS IN AN OIL AND GAS VENTURE FROM PINTER AND ENCOURAGED FRIENDS, RELATIVES AND BUSINESS ASSOCIATES TO INVEST AS WELL.102 WHEN THE INVESTMENTS SOURED, DAHL SUED PINTER FOR FAILING TO REGISTER THE SECURITIES. PINTER RAISED THE IN PARI DELICTO DEFENSE, BASED ON DAHL’S SOLICITATION OF THE OTHER INVESTORS, BUT THE FIFTH CIRCUIT REJECTED THE DEFENSE. POWELL DISAGREED WITH THIS RESULT:

SOPHISTICATED INVESTORS WHO PURCHASE UNREGISTERED SECURITIES PLACE THEMSELVES IN A NO-LOSE SITUATION. IF THE INVESTMENT PROVES PROFITABLE, THE BUYER COMES OUT AHEAD. IF THE VENTURE IS UNPROFITABLE, THE BUYER CAN SUE TO RECOVER HIS INVESTMENT, WITH INTEREST, IN A § 12(1) ACTION. . . [DAHL] FACES NO SANCTIONS OF ANY KIND FOR HIS PARTICIPATION IN THE ILLEGAL TRANSACTIONS. MOREOVER, § 12(1) IMPOSES LIABILITY WITHOUT REGARD TO WHETHER THE SELLER INTENDED TO DEFRAUD THE BUYER. ABSENT AN IN PARI DELICTO DEFENSE, BUYERS WILL INDEED OBTAIN AN “ENFORCEABLE WARRANTY” THAT THEIR INVESTMENT WILL BE PROFITABLE.103


100The other was Carpenter. See text at supra notes .

101Pinter v. Dahl, 486 U.S. 622 (1988). The case also raised the definition of “seller” under Section 12(1) of the Securities Act. This issue appears to have been of less concern to Powell, although it is an important holding of the Court.

102Pinter, 486 U.S. at 626.

POWELL’S COMPLAINT HERE SEEMS TO CONCERN SECTION 12(1)’S LIABILITY WITHOUT FAULT FOR THE SALE OF UNREGISTERED SECURITIES104 AS MUCH AS THE FIFTH CIRCUIT’S APPLICATION OF THE IN PARI DELICTO DEFENSE. THE “ENFORCEABLE WARRANTY” HE INVOKES EXISTS WHETHER OR NOT THERE IS AN IN PARI DELICTO DEFENSE. AND UNDER THE INTERPRETATION OF “SELLER” THAT POWELL APPEARED TO FAVOR, THE DISAPPOINTED BUYERS MIGHT WELL SEEK RELIEF FROM DAHL AS WELL AS PINTER, SO THERE WOULD BE SOME SORT OF SANCTION.

NOTWITHSTANDING THE WEAKNESS IN POWELL’S POSITION, HE NONETHELESS CONTINUED TO WIELD SUFFICIENT INFLUENCE IN THIS AREA THAT HE WAS ABLE TO ATTRACT TWO MORE VOTES SO THE CASE COULD BE HEARD.105 BY THE TIME THE CASE WAS ARGUED, POWELL HAD RETIRED. ALTHOUGH POWELL’S ARGUMENT FOR THE IN PARI DELICTO DEFENSE WAS REJECTED IN A FOOTNOTE,106 THE COURT DID RECOGNIZE A FORM OF THE DEFENSE.107

IN SUM, POWELL WAS THE COURT’S LEADER IN SECURITIES LAW.108 THAT LEADERSHIP IS REFLECTED NOT ONLY IN THE MANY MAJORITY OPINIONS THAT POWELL WROTE IN THE AREA, BUT ALSO BY HIS EXTRAORDINARY WINNING PERCENTAGE AND INFLUENCE OVER THE COURT’S DOCKET. POWELL’S EXTENSIVE EXPERIENCE IN THE AREA, BOLSTERED BY HIS WILLINGNESS TO WRITE AT THE CERTIORARI STAGE WHEN OTHER JUSTICES DID NOT RECOGNIZE THE IMPORTANCE OF A SECURITIES ISSUE, MADE HIM

105 At the initial conference, only Powell and Rehnquist favored a grant, with even Rehnquist’s support a tepid “Join 3.” Conference Notes, April 3, 1987. White and O’Connor switched their votes. Conference Notes, April 17, 1987.
106 Pinter, 486 U.S. 622, 637 n. 13.
107 Id. at 639.
a force to be reckoned with. These advantages were magnified by Powell’s hard work and thorough preparation. No other justice could (or perhaps, would) match his mastery of the facts of the cases and the law in this area.

PART THREE: CURTAILING LAWSUITS

The proliferation of securities class actions was still a nascent trend in the 1960s. Having received a green light from the Supreme Court in *J.I. Case v. Borak*, the lower courts, particularly the Second Circuit, had been expanding steadily the litigation exposure that corporations faced under the securities laws. Powell played a key role in stemming that tide in a series of cases involving the requirements for a cause of action under Rule 10b-5, the definition of “sale,” procedures applicable to representative actions, and judicial implications of private rights of action. Congress would not step in to curb securities class actions until 1995 when it adopted the Private Securities Litigation Reform Act; Powell and the Supreme Court began the process of limiting securities class actions in the mid-1970s.

Powell’s distrust of litigation reflected his experience as a corporate lawyer. Powell made the following “somewhat personal” observations in a memo to his law clerk

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110 See, e.g., SEC v. Texas Gulf Sulfur, 401 F.2d 833 (2nd Cir. 1968) (holding that a corporation need not have engaged in a securities transaction to be sued under Rule 10b-5).
IN A CASE\textsuperscript{111} RAISING THE QUESTION OF THE STANDARD OF PROOF IN PRIVATE CAUSES OF ACTION UNDER RULE 10b-5:

IN BALANCING THE “EQUITIES” OR POLICY CONSIDERATIONS RELEVANT TO THE STANDARD OF PROOF, I . . . KNOW FROM MY CORPORATE EXPERIENCE IN THE LATTER YEARS OF MY PRACTICE THAT THE INCREASE IN DAMAGE SUITS HAS CERTAIN NEGATIVE EFFECTS. . .

THE TYPICAL PRIVATE DAMAGES ACTION UNDER THE SECURITIES ACTS TAKES PLACE SEVERAL YEARS AFTER THE ALLEGED FRAUD. THERE ARE BANKRUPT COMPANIES TODAY THAT, ONLY A YEAR OR TWO AGO, WERE WIDELY VIEWED AS FINE INVESTMENTS. JURORS—AND INDEED JUDGES—TEND TO BE INFLUENCED BY THE PRESENT RATHER THAN CONDITIONS EXISTING AT THE TIME OF THE ALLEGED FRAUD. INFORMATION THAT MAY NOT HAVE SEEMED IMPORTANT THEN CAN LOOM QUITE LARGE YEARS LATER. THE NUMBER OF SUITS HAVE MULTIPLIED, AND SOMETIMES DAMAGES HAVE BEEN LARGE AND—AS YOUR MEMORANDUM NOTED—REPUTATIONS DESTROYED.

ONE CONSEQUENCE OF ALL OF THIS IS THAT MANY OF THE ABLEST PEOPLE IN OUR COUNTRY NO LONGER SERVE ON BOARDS OF DIRECTORS. I KNOW THIS FROM PERSONAL EXPERIENCE. EVEN INSURANCE COVERING DIRECTORS IS USUALLY LIMITED TO NEGLIGENCE AND NOT FRAUD. PREMIUMS ARE HIGH, AN EXPENSE CONSUMERS ULTIMATELY PAY. OUR BASIC ECONOMIC SYSTEM—THE FREE ENTERPRISE SYSTEM—IS A “RISK” SYSTEM AND INVESTORS SHOULD NOT EXPECT GUARANTEED EQUITY INVESTMENTS IN PARTICULAR.

AGAINST THIS BACKGROUND, IF THE FOLLOWING INFORMATION IS READILY OBTAINABLE ON LEXIS IT MIGHT BE INTERESTING, AND POSSIBLY RELEVANT TO THE STANDARD OF PROOF: HOW MANY 10b CASES HAVE THERE BEEN SINCE FLESCHMAN WAS DECIDED IN 1951? HAS THE NUMBER ACCELERATED IN RECENT YEARS? WILL LEXIS IDENTIFY SUITS FILED AGAINST VARIOUS CATEGORIES OF DEFENDANTS: PERSONS WHO SIGN REGISTRATION STATEMENTS, OFFICERS AND DIRECTORS, UNDERWRITERS, EXPERTS—PARTICULARLY ACCOUNTING FIRMS. MY IMPRESSION IS THAT A GOOD MANY SMALL ACCOUNTING FIRMS NO LONGER WILL WORK ON REGISTRATION STATEMENTS.

IN THE LITERATURE IN THIS AREA, IS THERE ANY DISCUSSION . . . AS TO THE PUBLIC INTEREST THAT MAY BE ADVERSELY AFFECTED BY OPENING THE FIELD WIDE TO DAMAGE SUITS THAT HAVE NEVER BEEN EXPRESSLY AUTHORIZED BY CONGRESS.\textsuperscript{112}

THIS PASSAGE CAPTURES SEVERAL THEMES THAT DROVE POWELL’S EFFORTS TO REIN IN SECURITIES FRAUD CLASS ACTIONS. FIRST, POWELL CONSIDERED THE JUDGE-MADE REMEDY UNDER RULE 10b-5 TO

\textsuperscript{111}Herman & MacLean v. Huddleston, 459 U.S. 375 (1983).

\textsuperscript{112}Memorandum to Jim Browning from Lewis F. Powell, Jr., 81-680 Herman & MacLean v. Huddleston, at 1.
BE A SPECIES OF FEDERAL COMMON LAW, AND THUS APPROPRIATE FOR JUDGES TO CONSIDER POLICY IN DEFINING ITS LIMITS.\textsuperscript{113} SECOND, POWELL UNDERSTOOD, BASED ON EXPERIENCE COUNSELING CORPORATE CLIENTS, THE CONSEQUENCES THAT THE PHENOMENON OF CLASS ACTION LAWSUITS HAD FOR CORPORATIONS AND THEIR OFFICERS AND DIRECTORS.\textsuperscript{114} FINALLY, POWELL WAS PROFONDLY SUSPICIOUS OF JUDICIALLY CREATED PRIVATE CAUSES OF ACTION NOT SPECIFICALLY AUTHORIZED BY CONGRESS. FROM POWELL’S PERSPECTIVE, THE EXPANSION OF SECURITIES FRAUD LAWSUITS BASED ON IMPLIED RIGHTS OF ACTION WAS CREATING A LITIGATION CRISIS. THAT PERCEPTION OF CRISIS WOULD INFLUENCE THE OUTCOME IN A NUMBER OF CASES THAT CAME TO THE SUPREME COURT.

THIS PART PROCEEDS IN FOUR SECTIONS. THE FIRST DISCUSS CASES LIMITING THE REACH OF RULE 10B-5. THE SECOND DEALS WITH REPRESENTATIVE ACTIONS, INCLUDING BOTH CLASS ACTIONS AND DERIVATIVE SUITS. THE LAST TWO SECTIONS DEAL WITH THRESHOLD ISSUES: THE DEFINITION OF SALE AND THE JUDICIAL IMPLICATION OF PRIVATE CAUSES OF ACTION FROM REGULATORY STATUTES. THE CONSISTENT THEME OF POWELL’S WORK ACROSS THESE SUBJECT AREAS IS THE NEED TO REIN IN LAWSUITS.

A. \textit{The Construction of Rule 10B-5}

\textsuperscript{113}Powell’s clerk failed to turn up any useful empirical work on the topic. Memorandum to Mr. Justice Powell from Jim [Browning], RE: \textit{Herman & MacLean v. Huddleston}, No. 81-680.

\textsuperscript{114}The SEC and the Solicitor General were arguing for a preponderance of the evidence standard. Bench Memorandum to Mr. Justice Powell from Jim [Browning], \textit{Herman & MacLean v. Huddleston}, at 17 (Powell’s marginal notes). Powell agreed with his law clerk that “the SG undervalues a professional’s reputation” and the harm to that reputation from a jury finding that the defendant (in this case an accounting firm) acted with deceptive intent. Id. (Powell’s marginal notes). Powell instead favored the common law “clear and convincing” evidence standard. Memorandum to Jim Browning from Lewis F. Powell, Jr., \textit{81-680 Herman & MacLean v. Huddleston}, at 1 (Sept. 13, 1982). Powell’s influence was not felt in this particular case. After writing this memo, Powell recused himself when he learned that his son-in-law’s investment banking firm was a defendant in a similar suit. Letter from Lewis F. Powell, Jr. to the Chief Justice, \textit{81-680 Herman & MacLean v. Huddleston} (November 11, 1982). With no one to advocate for the higher standard of proof at the Conference, the Court unanimously upheld the preponderance standard advocated by the SEC. Herman & MacLean v. Huddleston, 459 U.S. 375 (1983). Deference to agency expertise still had bite when there was not an expert Justice taking the contrary position.
A TRILOGY OF RULE 10B-5 CASES FROM THE MID-70S – BLUE CHIP STAMPS, ERNST & ERNST, and SANTA FE – established the Supreme Court’s intention to reverse the expansion of RULE 10B-5. These cases are the cornerstone of the counter-revolution the in the federal securities law, not only in substance, but perhaps more importantly, in style.

BLUE CHIP STAMPS is the rhetorical high point of the Supreme Court’s counterrevolution in the federal securities laws. REHNQUIST’s opinion for the Court holds that a private plaintiff must be a purchaser or seller of securities to state a claim under RULE 10B-5, which had been established in the Second Circuit for more than twenty years. The Court was wary of the SEC’s efforts (as amicus) to change the rule through the courts rather than Congress. REHNQUIST’s opinion is notable, however, for its skepticism regarding securities fraud class actions. REHNQUIST warned that “litigation under RULE 10B-5 presents a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general” and the risk that the threat of enormous discovery costs could produce “IN TERRORREM” settlements. REHNQUIST’s opinion has been

115421 U.S. 723 (1975).
118421 U.S. 723 (1975).
120Powell noted at argument that “Brennan asked if SEC had ever asked Congress to change Rule – it has been with us for 20 yrs. Answer was ‘No.’” Argument Notes, No. 74-124, Blue Chips Stamps v. Manor Drug Stores (undated ; case argued March 24, 1975). Despite his skeptical question, Brennan voted against the rule.
1211st Draft, Blue Chip Stamps v. Manor Drug Stores, No. 74-124 (Rehnquist, J.) at 10, 16 (5/9/75).
A common citation in subsequent Supreme Court and lower court opinions reinining in class actions.

Powell was not happy with the opinion, which “reaches correct result – but meanders and wobbles about in an unlawyerlike manner!”\(^{122}\) Powell was concerned that the opinion apologized excessively for its holding and that it paid insufficient attention to the statute’s “language” and “legislative history.”\(^{123}\) In light of his “special interest in this subject” Powell wrote a concurrence emphasizing the statutory language.\(^{124}\) Powell thought the rule was compelled by text, legislative intent, long history, and “policy considerations . . . extending standing (who may) to sue” which were particularly relevant in “a private cause of action . . . wholly of judicial creation.”\(^{125}\) Those policy concerns grew out of his own experience.

Powell expressed surprise at the SEC’s departure from its longstanding practices:

Absolute factual accuracy with respect to a corporate enterprise is impossible, except with respect to certain hard facts (e.g., some balance sheet items). The outcome of pending litigation, the effect of relatively new legislation, the possible enactment of adverse legislation, the expenditures needed to meet escalating environmental regulations, the likelihood and effect of new competition or of new technology and many similar matters of potential relevancy, must be addressed in registration statements and prospectuses. In administering the 1933 Act, the SEC traditionally and consistently has encouraged and often required offerors to take conservative postures in prospectuses, especially with respect to judgmental and unfavorable matters. If a different philosophy now were to be read

\(^{122}\)Id. at 1 (Powell’s handwritten comments).

\(^{123}\)Id.


\(^{125}\)Notes for Conference, Blue Chip (74-124) (undated ).
into the 1934 Act, inviting litigation for arguably misleading understatement as well as for overstatement of the issuer’s prospects, the hazard of “going to market” — already not inconsequential — would be immeasurably increased.\textsuperscript{126}

Despite Powell’s warning, the SEC has adopted this “different philosophy,” sanctioning companies for understatement as well as overstatement. Powell’s understated concurrence has not received the same attention as Rehnquist’s shrill dicta on the dangers of vexatious class action litigation; perhaps this reflects changes in attitudes toward class action litigation since \textit{Blue Chip} was decided.

Powell wrote the second case in this trilogy, \textit{Ernst & Ernst v. Hochfelder},\textsuperscript{127} the Court’s seminal opinion on the state of mind required for liability under Section 10(b) of the \textit{Exchange Act}.\textsuperscript{128} While Powell’s opinion discouraged securities fraud class actions alleging “fraud by hindsight,” the question he left unanswered continues to be the central dispute in securities class actions today.

\textit{Ernst & Ernst} arose from a claim against an accounting firm for failing to uncover the long-running fraudulent scheme of a brokerage house’s principal.\textsuperscript{129} The plaintiffs alleged that \textit{Ernst & Ernst} had aided and abetted the fraud by its negligence.\textsuperscript{130} The case came to the \textit{Supreme Court} on the question whether negligence would suffice to

\textsuperscript{126}Chambers Draft, Blue Chip Stamps v. Manor Drug Stores, (Powell, J., concurring), at 5 n.4 (May --, 1975).

\textsuperscript{127}425 U.S. 185, 189 (1976).

\textsuperscript{128}15 U.S.C. §78.

\textsuperscript{129}425 U.S. 185, 189 (1976).

\textsuperscript{130}Id. at 190.
STATE A CLAIM UNDER SECTION 10(B), OR WHETHER A HIGHER STATE OF MIND WAS REQUIRED TO
ESTABLISH LIABILITY.\footnote{131}{Id. at 193.}

POWELL’S VIEW OF THE CASE WAS COLORED BY HIS CONCERN ABOUT A RELATED ISSUE: THE LIABILITY OF THIRD PARTIES FOR MISSTATEMENTS. POWELL OBSERVED IN HIS “SUMMER MEMO,” WRITTEN AFTER READING THE BRIEFS DURING THE COURT’S SUMMER BREAK:

\textit{As we had occasion recently to note in Blue Chip Stamps v. Manor Drug Stores, private causes of action for damages under Section 10(b) and Rule 10b-5 have evolved expansively by judicial interpretation. The decision of CA7, if affirmed by us, would advance this process to new frontiers. Damage liability could be imposed for negligence not only upon the contracting party (the brokerage firm in this case), but also upon a “third party” accounting firm.}\footnote{132}{Memorandum, No. 74-1042, Ernst & Ernst v. Hochfelder, et al, at 5 (August 21, 1975).}

POWELL RETURNED TO HIS CONCERN WITH EXTENDING THIRD PARTY LIABILITY LATER IN THE MEMO:

\textit{[A] NEGLIGENCE STANDARD APPLICABLE TO AUDITORS WOULD INVITE LITIGATION BASED ON A SIMPLE AVERMENT OF ABSENCE OF DUE CARE, NOT MERELY IN THE RECORDING OF THE FACTS AS REFLECTED BY THE COMPANY’S BOOKS BUT IN FAILING PROPERLY TO DISCOVER MISMANAGEMENT OR FRAUD. THIRD PARTY SUITS OF THIS KIND BROUGHT YEARS AFTER THE OCCURRENCE OF THE ALLEGED NEGLIGENCE AND VIEW WITH “HIND-SIGHT” VISION, WOULD IMPOSE A HIGH RISK OF LIABILITY ON ACCOUNTANTS.}\footnote{133}{Id. at 8.}

POWELL WAS AT LEAST AS CONCERNED WITH THE IDENTITY OF THE DEFENDANT AS HE WAS WITH THE STANDARD OF LIABILITY. POWELL DISTRusted LAWSUITS THAT EXTENDED LIABILITY “TOO FAR.”\footnote{134}{This concern also provoked Powell to write his dissent from the denial of certiorari in John Nuveen & Co. v. Sanders, 450 U.S. 1005 (1981) (Powell, J., dissenting from the denial of certiorari). Powell strenuously objected to the Seventh Circuit’s holding in that case that reasonable care for an underwriter under §12(2) required “independent investigation such as examination of the accountant’s work papers underlying the certified financial statements.” Memorandum to Mr. Justice Powell from Paul Cane, No. 80-299, John Nuveen & Co. v. Sanders (February 6, 1981) (Powell’s marginal notes: “No!”).}
POWELL WAS ASSIGNED THE OPINION, AND IN A MEMO TO HIS LAW CLERK REVIEWING A DRAFT, HE NOTED THAT “[W]E DO NOT DISCUSS THE ABSENCE OF ‘PRIVACY’ IN THE COMMON LAW SENSE BETWEEN ERNST & ERNST AND RESPONDENTS. I VIEW THIS AS AN IMPORTANT FACT, AND INDEED ONE THAT COULD BE CONTROLLING WITH ME.”

POWELL RECOGNIZED, HOWEVER, THAT THE COURT HAD NOT GRANTED CERTIORARI ON THIS QUESTION AND HE DID NOT THINK A MAJORITY COULD BE ASSEMBLED TO DISMISS ON ABSENCE OF PRIVACY. SUCH A HOLDING WOULD HAVE HAD PROFOUND CONSEQUENCES FOR THE LAW OF SECURITIES FRAUD; IT SUGGESTS THAT POWELL WOULD HAVE HAD LITTLE TROUBLE VOTING FOR THE SUPREME COURT’S CONTROVERSIAL DECISION IN CENTRAL BANK, WRITTEN BY HIS SUCCESSOR, ANTHONY KENNEDY, WHICH FORECLOSED LIABILITY FOR AIDERS AND ABETTORS.

GIVEN THE CASE’S POSTURE, POWELL SATISFIED HIMSELF BY DRAFTING A FOOTNOTE HIGHLIGHTING HIS “POLICY CONCERNS.”

ON THE QUESTION OF THE REQUIRED STATE OF MIND, POWELL, IN A SOMEWHAT IMPATIENT TONE (FOR HIM) objected to his clerk’s distinction between “‘KNOWING OR INTENTIONAL MISCONDUCT’, ON THE ONE HAND, AND NEGLIGENCE OR ‘NEGLIGENT MISFEASANCE’, ON THE OTHER.” POWELL PREFERRED THE MIDDLE GROUND ESTABLISHED BY JUDGE ARLIN ADAMS IN A CONCURRENCE TO A THIRD CIRCUIT OPINION:

135 Memorandum from Lewis F. Powell, Jr. To Greg Palm, No 74-1042 Ernst & Ernst, at 3 (February 4, 1976).

136 Id.


138 425 U.S. 185, 214 n.33 (1976); Lewis F. Powell, Jr., Possible Footnote (Ernst & Ernst) (2/20/76).

139 Telephone Interview with Christine Whitman, April 17, 2002.

140 Memorandum from Lewis F. Powell, Jr. To Greg Palm, No 74-1042 Ernst & Ernst. (February 4, 1976), at 2.
Judge Adams in Korn (at p. 287) used language that I like:
“AN INTENT TO DECEIVE, MANIPULATE OR DEFRAUD.”
Adams, p. 285, also referred to Judge Friendly’s formulation as including “recklessness” that amounts to fraud. What would you think of our using the term “scienter” and defining it early in the opinion, using the Adams/Friendly terminology?141

This discussion suggests that Powell thought that recklessness would satisfy the scienter requirement. The first part of this suggestion was adopted, with the eventual opinion defining scienter as “a mental state embracing intent to deceive, manipulate or defraud.”142 The final opinion, however, did not incorporate recklessness, specifically reserving the question.143

Why not resolve this critical issue? The answer is fairly mundane. Powell, despite his desire to offer guidance to the bar, had a general preference for not addressing questions unnecessary to the decision. Accordingly, resolution of this issue was left to a subsequent case.144 This preference to leave questions to another day sits in considerable tension with Powell’s preference for predictability. Resolution of this critical question would have made the securities laws much easier to apply.

Powell could have settled the law in Ernst & Ernst, but held back. The Supreme Court has avoided the question of whether recklessness satisfies Section 10(b) for another twenty-five years. Powell can be forgiven for failing to anticipate that the

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141Id. (citing Kohn v. American Metal Climax, Inc., 458 F.2d 255, 270 (3rd Cir. 1972) (Adams, J., concurring in part and dissenting part). Judge Friendly’s formulation is “the kind of recklessness that is equivalent to willful fraud.” SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 868 (2nd Cir. 1968) (Friendly, J., concurring).


143Id.

144Telephone Interview with Greg Palm (June 6, 2002).
Justice Powell and the Counter-Revolution


The final case in the trilogy, Santa Fe Industries v. Green, is the Court’s most sweeping defense of state corporate law. The Second Circuit held that a short-form merger authorized by Delaware law, which “froze out” the company’s minority shareholders, violated Rule 10b-5. That court held that “no allegation or proof of misrepresentation or nondisclosure is necessary” to state a violation of Rule 10b-5; a

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Breach of fiduciary duty was sufficient. Moreover, that breach of fiduciary duty arose out of federal, rather than state, common law. The decision was startling enough to Powell that he wrote nine page memorandum summarizing it; he spent little time, however, criticizing the decision because it seemed so obviously wrong:

As the title of § 10b indicates, it is concerned with “manipulative and deceptive devices.” I would not have thought, until CA 2’s opinion, that anyone would have deemed a merger to be such a device solely because the price offered dissenters was “grossly” below fair market value so long as there was no misrepresentation or omission of a material fact. The purpose of § 10b and Rule 10b(5) is to substitute full disclosure for the doctrine of Caveat Emptor.

Nor would I have thought that § 10b was intended to create a federal common law [sic] of corporations contrary to valid state statutes.

Notwithstanding the intuitive appeal of the point that fraud requires a misrepresentation, four justices voted for some variant of the Second Circuit’s rule: Brennan and Marshall voted to affirm because appraisal was not an adequate remedy, while Stevens and Blackmun voted to reverse only because they thought that the plaintiffs had not demonstrated inadequacy. The lure of a federal common law of corporations had a base of support on the Court, but not a majority.

148533 F.2d 1283, (197 ).
149Memorandum to File from Lewis F. Powell, Jr., No. 75-1753 Santa Fe Industries, Inc., et al. v. S. William Green, et al., at 9 (December 27, 1976).
White’s straightforward holding for the Court is that fraud requires a misrepresentation or nondisclosure, but he goes out of his way to defend the role of state corporate law:

The reasoning behind a holding that the complaint in this case alleged fraud under Rule 10b-5 could not be easily contained. The result would be to bring within the rule a wide variety of corporate conduct traditionally left to state regulation. In addition to posing a danger of vexatious litigation which could result from a widely expanded class of plaintiffs under Rule 10b-5, this extension of the federal securities laws would overlap and quite possibly interfere with state corporate law. Federal courts applying a ‘federal fiduciary principle’ under Rule 10b-5 could be expected to depart from state fiduciary standards at least to the extent necessary to ensure uniformity within the federal system. Absent a clear indication of congressional intent, we are reluctant to federalize the substantial portion of the law of corporations that deals with transactions in securities, particularly where established policies of corporate regulation would be overridden.

The Supreme Court was drawing a line in the sand to preserve state corporate law from the development of ‘federal corporate law’ by the lower courts.

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151 Santa Fe Industries, Inc. v. Green, 430 U.S. 462, 478 (1977). The Court dealt with a similar issue under Section 14(e) in another case, Schreiber v. Burlington Northern, Inc. 472 U.S. 1 (1985) (holding that § 14(e) requires misrepresentation or nondisclosure), but Powell was recovering from complications from surgery and did not participate in the decision. His notes on the preliminary memorandum indicate his agreement with the lower court, which was affirmed. Preliminary Memorandum, No. 83-2129, Schreiber v. Burlington Northern, Inc., (Sept. 24, 1984 Conference).

152 Santa Fe, 430 U.S. at 478-479 (citations and footnotes omitted).

153 Santa Fe’s lesson on the need to preserve state corporate law was reaffirmed in the context of investment companies. Burks v. Lasker raised the question of whether the independent directors of an investment company had the authority to dismiss a derivative claim. Investment companies are incorporated under state authority, but their governance is subject to substantial federal regulation under the Investment Company Act. This unique balance creates the potential for numerous conflicts between state and federal law. The Second Circuit held that the directors did not have the authority to dismiss the suit, invoking a federal common law rule based on the policies of the Investment Company Act, which was silent on the issue. 562 F.2d 1208 (1978). The SEC argued that a federal rule should apply, but that rule would not bar the independent directors from dismissing the claim. Brief of the Securities and Exchange Commission as Amicus Curiae, Burks v. Lasker, No. 77-1724. The Supreme Court held that state law controlled. 441 U.S. 471 (1979). The only controversy raised by the case was how emphatic the endorsement of state law would be. The opinion was assigned to Brennan, but Powell and Stewart were “not happy with his grudging approach to authority of the disinterested Board members.” 1st Draft, Burks v. Lasker, No. 77-1724 (Brennan, J.) (18 April 1979) (Powell’s handwritten notes). Stewart wrote a concurrence suggesting blanket deference to state law was appropriate, which Powell joined. 2nd Draft, Burks
B. **Representative Actions**

Powell appears to have been unnerved by the spread of securities class actions, and he wrote two opinions for the Court slowing the trend. His work in this area is largely defensive, however, and class actions continue to be a threat to corporations despite Powell’s efforts.

Powell wrote the Court’s seminal opinion on class action procedure: *Eisen v. Carlisle & Jacquelin*. The case contains both securities and antitrust allegations, but its implications extend well beyond those core areas of business law. Powell described it as “the major test case involving the contours of a proper class action case under Rule 23 [of the Federal Rules of Civil Procedure], as well as the notice requirements in class action compelled by Due Process.”

The claim was based on price fixing by New York Stock Exchange member firms in the commissions charged for trading in “odd lots” (trades of less than 100 shares). The district court held that class members need not be given individual notice because their claims were so small that they would be unlikely to opt out. Powell, however, did not want Rule 23’s interpretation to be determined by the facts of a particular case: “we must decide case on principle of general application – not on a guess as to what members of class will do.” Moreover, the district court had imposed the costs of notice on the

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v. Lasker, No. 77-1724 (Stewart, J., concurring) (30 April 1979).


DEFENDANTS BASED ON ITS “PRELIMINARY” ASSESSMENT THAT THE DEFENDANTS WERE LIKELY TO BE FOUND LIABLE. Powell distrusted this procedural innovation: this “requirement that a party pay his adversary’s costs is unique in the law.” 157 This case stands out from many of the cases studied here, however, in that the Second Circuit had also balked at the district court’s innovation, reversing both the ruling on notice and the imposition of costs on the defendants. The Second Circuit had reversed on another ground as well, holding that the class was unmanageable because there was no practical means by which any recovery could be paid to the actual class members.

This final holding raised complications. Appellate jurisdiction over the first two issues was clear under the Cohen doctrine as an appealable final order. 158 The manageability question was appealable only under the “death knell” doctrine, under which a case could be appealed if the denial of class certification would mean that the case would be abandoned as uneconomical. A majority (Burger, Douglas, Brennan, White, Marshall and Blackmun) thought there was jurisdiction over the manageability issue, but Rehnquist and Stewart strongly disagreed. 159

The opinion was assigned to Powell. With a clear majority on the notice and costs issues (only Douglas disagreed and his views were tentative), 160 Powell determined to

157Id.


159Conference Notes, No. 73-203, Eisen v. Carlisle & Jacquelin (Conf. 2/27/74).

160Id.
STEER CLEAR OF THE DIFFICULT JURISDICTIONAL ISSUEPOSED BY THE MANAGEABILITY QUESTION.  

NONETHELESS, POWELL CLEARLY WORRIED ABOUT THE ABILITY OF COURTS TO MANAGE CLASS ACTIONS OF THE SIZE AND COMPLEXITY SEEN IN EISEN. HE WROTE (IN A FOOTNOTE THAT DID NOT MAKE ITS WAY INTO THE OPINION):

THIS CASE’S HISTORY WELL ILLUSTRATES THE ARRAY OF INTRACTABLE PROBLEMS LATENT IN THIS TYPE OF CLASS ACTION. WITH COMPETENT COUNSEL AND IN A DISTRICT AND CIRCUIT UNIQUELY EXPERIENCED IN COMPLEX CIVIL LITIGATION, THIS SUIT, — IN WHICH APPEALING POLICY AND LEGAL CONSIDERATIONS ARE IMPLICATED ON BOTH SIDES — HAS DEFIED RATIONAL RESOLUTION. IT SUGGESTS THE NEED FOR THOUGHTFUL REEXAMINATION OF SOME OF THE ASSUMPTIONS THAT UNDERLIE THE CLASS ACTION RULES, WITH DUE RECOGNITION OF THE NEED FOR SOME FORM OF CLASS ACTION RELIEF, AND ALSO RULES WHICH IN FACT CAN BE ADMINISTERED WITHIN THE FRAMEWORK OF THE ADVERSARY SYSTEM WITH REASONABLE EXPEDITION AND FAIRNESS TO ALL CONCERNED.  

POWELL WAS NOT THE SORT TO USE JUDICIAL OPINIONS TO ADVOCATE REFORM, BUT EVEN THIS GUARDED FOOTNOTE SHOWS HIS CONCERN, WHICH OTHER MEMBERS OF THE COURT SHARED. BURGER WROTE (IN A PRIVATE NOTE TO POWELL): “I HOPE THIS WILL ‘CONTAIN’ THE DRIFT FOR GOVERNMENT-BY-CLASS-ACTION. WHAT WE NEED IS VIGOROUS ACTION BY APPROPRIATE REGULATORY AGENCIES

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161There was a conflict among the circuits, as Winokur v. Bell Fed. S& L Ass’n, in which the Seventh Circuit had rejected the “death knell” doctrine, was being held for the decision in Eisen. Despite the conflict, Powell recommended that certiorari be denied in Winokur. Memorandum to the Conference from L.F.P., Jr., Holds of No. 73-203 Eisen v. Carlisle & Jacqueline (May 29, 1974). This deferral led to a different outcome, as the Court rejected the doctrine four years later. Coopers & Lybrand v. Livesay, 437 U.S. 463 (1978). Given the majority in favor of the “death knell” doctrine in Eisen, this is a surprising result, but Powell’s conference notes reflect an 8-1 vote against the doctrine in Coopers & Lybrand, with only Brennan disagreeing, and even Brennan ended up joining Stevens’ opinion for the Court. Conference Notes, No. 76-1836, Coopers & Lybrand v. Livesay (Conf. 3/24/78). This decision’s effect has been ameliorated somewhat by the adoption of Fed. R. Civ. P. 23(f), which allows courts of appeals discretion to entertain class action certification questions. See generally, Wright, Miller & Cooper, 15 Federal Procedure § 3912.

WHEN THESE BROKERS GET OUT OF LINE.”¹⁶³  POWELL’S OPINION WAS A STEP TOWARD “CONTAINING” CLASS ACTIONS,¹⁶⁴ BUT CLASS ACTIONS CONTINUE AS A THREAT TO THE SECURITIES INDUSTRY.¹⁶⁵

POWELL STRUCK ANOTHER BLOW AGAINST REPRESENTATIVE ACTIONS THE SAME TERM, ALTHOUGH THE FACTS OF THE CASE WERE SUFFICIENTLY UNUSUAL THAT THE EFFECT OF THE HOLDING WAS LIMITED.  POWELL SUMMARIZED THE CONTROLLING ISSUE IN BANGOR PUNTA THIS WAY:

(CAI SEEMS TO BE THROWING THE LAW BOOKS AWAY!) CAI, OVER-RULING DC, HELD THAT A 99% STOCKHOLDER OF CORP MAY BRING A DERIVATIVE STOCKHOLDERS’ SUIT IN NAME OF CORP VS. THE FORMER OWNER CONTROLLING STOCK IN THE CORP. FOR MISMGRT.  CAI ALLOWED SUIT ON THEORY THAT ALTHOUGH THE RESP. (PRESENT 99% OWNER) ALLEGED NO INJURY OR DAMAGE TO ITSELF (+ NO FRAUD AT TIME IT ACQUIRED THE 99% INTEREST), RESP. WAS ENTITLED TO SUE FOR GENERAL BENEFIT OF PUBLIC’S INTEREST IN RAILROADS.  IN SHORT, RESP. WAS SELF APPOINTED ATTY-GEN.”¹⁶⁶


POWELL LOOKED TO PRINCIPLES OF EQUITY TO RESOLVE THE CASE.  A MAJORITY AGREED WITH POWELL THAT THE FIRST CIRCUIT SHOULD BE REVERSED, ALTHOUGH NO CLEAR CONSENSUS EMERGED


¹⁶⁴Not surprisingly, Powell’s opinion was met with hostility by class action advocates.  Powell clipped the article with their reactions, but made no notation of his own.  Linda Charlton, Impact of Ruling by Court Studied: Lawyers See Strong Effect on Class-Action Suits by Consumer Groups, New York Times (no page number or date on clipping).

¹⁶⁵That industry has secured greater protection from class actions through an industry-wide practice of arbitration.  The Court decided three cases implicating arbitration in the field of securities law during Powell’s tenure.  Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Ware, 414 U.S. 117 (1973); Scherk v. Alberto-Culver Co., 417 U.S. 506 (1974); Shearson/American Express, Inc. McMahon, 482 U.S. 220 (1987).  Powell, while generally favoring arbitration, does not appear to have had a significant influence on the Court in this area.

AT THE CONFERENCE AS TO THE BASIS FOR REVERSAL.\textsuperscript{167} Powell’s opinion is carefully grounded in “the settled principle of equity that a shareholder may not complain of acts of corporate mismanagement if he acquired his shares from those who participated or acquiesced in the allegedly wrongful transactions.”\textsuperscript{168}

Powell expressed skepticism at the “private attorney general” concept (striking the same note that Burger had shared in his Eisen letter): “Quite apart from purely equitable considerations, there is sound reason to leave the safeguarding of the public interest in the soundness of railroads and the quality of their service to the regulatory authorities rather than to encourage some concept of ‘private attorney general’ litigation.”\textsuperscript{169}

Marshall’s invocation of the concept provoked Powell’s (private) disdain. Powell recorded Marshall’s view at conference as “party who stole money should give it up.”\textsuperscript{170} Powell’s reaction: “Wow! This sounds like Robin Hood.”\textsuperscript{171} Marshall’s dissent, with its “typical juvenile style” provoked even more scorn.\textsuperscript{172} According to Powell (an avid hunter), Marshall “fired, at random, a load of birdshot - some remotely relevant but

\textsuperscript{167}Conference Notes, No. 73-718, Bangor Punta v. Bangor & Aroostook RR (Conf. 4/17/74).

\textsuperscript{168}Bangor Punta Operations, Inc. v. Bangor & Aroostook RR Co., 471 U.S. 703, 710 (1974). One complication was the fact that the claim was not, in fact, a derivative claim, but instead had been brought directly by the affected corporation, which caused Powell and his clerk some difficulty in drafting the opinion. Telephone Interview with John Buckley (June 5, 2002). In the end, they simply relied on the principle that a court of equity should not confer windfall gains on parties who have not suffered damages.

\textsuperscript{169}Memorandum to Mr. John Buckley from Lewis F. Powell, Jr., Bangor Punta (May 20, 1974).

\textsuperscript{170}Conference Notes, No. 73-718, Bangor Punta v. Bangor & Aroostook RR (Conf. 4/17/74).

\textsuperscript{171}Id.

\textsuperscript{172}No. 73-718, Bangor Punta Operations, Inc., et al. v. Bangor & Aroostook Railroad Co. et al. (Marshall, J., dissenting), at 4 (June 13, 1974) (Powell’s comment in margin). Powell instructed his clerk to “answer summarily some of the more absurd points.” Id. at 1.
MOST OF THEM IRRELEVANT. HE SEEMS TO OVERLOOK THE FACT ENTIRELY THAT THE PARTIES FOR WHOM HE SHED TEARS (THE MINORITY STOCKHOLDERS AND CREDITORS) MAY BRING SUIT ON THEIR OWN BEHALF; NOTHING PRECLUDES THEM, AND THEY HAVE ASSERTED NO INJURY.”

Powell’s uncharacteristically exasperated tone may have reflected just end-of-the-term tension (the published responses are more measured), but it also seems plausible that he viewed regulation by class or representative action as an abuse of the litigation process. The final case affecting procedures in securities fraud class actions decided by the Court during Powell’s tenure is Parklane Hosiery Co. v. Shore. Parklane Hosiery raised the question whether issues resolved against a defendant in an SEC enforcement action were entitled to collateral estoppel effect in a subsequent private action. The case is significant, not only for the procedural advantage it affords class action plaintiffs, but more importantly for the coercive threat it affords the SEC. Defendants in SEC enforcement actions are loath to contest the agency’s charges in court, given the ruinous liability exposure an adverse decision would create for them in a follow-on class action. As a result, the overwhelming majority of SEC enforcement actions are resolved through consent decrees, with defendants agreeing to pay fines and/or have injunctions entered against them, but without any admission of wrongdoing.

173 Memorandum to Mr. John Buckley from Lewis F. Powell, Jr., No. 73-718 Bangor Punta (June 14, 1974).

174 Powell might vent his frustration with his colleagues in the privacy of his chambers, but he took care to not allow that frustration into his opinions. Powell “preferred understatement in responding to dissents.” Telephone Interview with John Buckley (June 5, 2002). This restraint no doubt enhanced his influence with his colleagues.

Given Powell’s suspicion of the SEC, it is a little surprising that he would acquiesce in a decision that affords the agency such leverage.\textsuperscript{176} Moreover, Powell’s law clerk pointed out (and Powell agreed) that allowing “class action plaintiffs . . . to gain a ‘free ride’ following a successful government enforcement suit” was inconsistent with the concept of class action plaintiffs serving as “‘private attorneys general.’”\textsuperscript{177} Powell nonetheless joined Stewart’s majority opinion upholding the use of collateral estoppel.

Rehnquist, in his dissent, worried that the Court’s:

\textit{decision will have the result of coercing defendants to agree to consent orders or settlements in agency enforcement actions in order to preserve their right to jury trial in the private actions. In that event, the Court, for no compelling reason, will have simply added a powerful club to the administrative agencies’ arsenals that even Congress was unwilling to provide them.}\textsuperscript{178}

Powell conceded Rehnquist had written a “good dissent – but I still agree with Stewart’s opinion.”\textsuperscript{179}

\textbf{C. \textit{Definition of Sale}}

\textit{International Brotherhood of Teamsters v. Daniel} was a sympathetic case. John Daniel had worked for over twenty years under a collective bargaining agreement between Teamsters Local 705 and a variety of employers. That agreement included a pension fund arrangement under which employees qualified for a pension if employed “for

\textsuperscript{176}The issue was highlighted in an \textit{amicus} brief filed by the Washington Legal Foundation. Bobtail Bench Memorandum to Justice Powell from D[avid] W[estin], Parklane Hosiery Company, Inc., et al. v. Shore, at 5 (10/27/78).

\textsuperscript{177}Id. at 14.


\textsuperscript{179}1\textsuperscript{st} Draft, Parklane Hosiery Company, Inc. v. Shore, No. 77-1305 (Rehnquist, J., dissenting) (Dec. 22, 1978).
AT LEAST 20 CONSECUTIVE, CONTINUOUS AND UNINTERRUPTED YEARS IMMEDIATELY PRECEDING RETIREMENT.”

Daniel could not meet the “continuous” service requirement because he had been laid off for a three-month period at one point during his employment. Daniel claimed that he had been deceived about the continuity requirements for vesting of the pension. More creatively, he asserted that his participation in the pension plan was the sale of a security and therefore subject to the federal securities laws. The district court and Seventh Circuit agreed.

Powell found the lower courts’ holding “close to being absurd” with “far reaching . . . results.” Daniel faced four obstacles to his claim: (1) contributions to the pension plan were made by his employers, not him; (2) he was required to participate in the plan; (3) the scheme at issue was a “defined benefit” plan, under which the benefits did not vary with the fund’s performance; and (4) application of the federal securities laws to pension plans threatened to interfere with the separate federal regulatory scheme for pensions. Daniel needed to show both that his interest in the pension plan was a “security” and that there had been a “sale” of that interest to him. The court of appeals found a “security” because the pension fund was similar to a mutual fund or variable annuity, and a “sale”

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181 Id. at 8.

182 Id.

183 410 F. Supp. 541, 561 F.2d 1223.

BECAUSE DANIEL HAD MADE AN INVESTMENT DECISION TO PARTICIPATE IN THE PENSION PLAN BY
FOREGOING ALTERNATIVE EMPLOYMENT OPPORTUNITIES.185 THE LOWER COURTS DISTINGUISHED
CONGRESS’S REGULATION OF PENSION PLANS AS “CONCERNING THE ADMINISTRATION OF SUCH FUNDS
. . . RATHER THAN REGULATION OF CIRCUMSTANCES OF ENTRY INTO THE PLAN.”186

POWELL WORRIED THAT THE LOWER COURTS’ DECISION COULD DRAMATICALLY EXPAND THE
SCOPE OF THE SECURITIES LAWS: “ANY OFFER + ACCEPTANCE OF EMPLOYMENT MIGHT VIEWS AS AN
INVESTMENT [CONTRACT]” AND, THEREFORE, THE SALE OF A SECURITY.187 HE ALSO THOUGHT THAT IT
COULD NOT BE SQUARED WITH THE COURT’S FOCUS UPON ECONOMIC REALITIES IN THE DEFINITION OF
A “SECURITY.”188 POWELL’S COLLEAGUES AGREED; THE CONFERENCE VOTE WAS 8-0 TO REVERSE, WITH
POWELL STUNNED TO FIND EVEN BLACKMUN IN ACCORD.189

BURGER’S ASSIGNMENT OF THE OPINION TO POWELL MADE A NARROW REVERSAL UNLIKELY.
POWELL SAW SECURITIES LAW OPINIONS AS AN OPPORTUNITY TO SHAPE THE LAW, NOT JUST RESOLVE
CONFLICTS AMONG THE LOWER COURTS. POWELL ADDED TO THE DRAFT THAT “[T]HE SEC’S PRESENT
POSITION WITH RESPECT TO THE TERM “SALE” IS QUITE UNSUPPORTABLE.”190 SPECIFICALLY, POWELL
QUESTIONED THE SEC’S POSITION THAT “IT IS POSSIBLE TO REGARD A PARTICULAR FINANCIAL

18561 F.2d at 1237, 1243.

186410 F. Supp. at 549.

187Bench Memorandum from Paul [B. Stephan] to Mr. Justice Powell, International Brotherhood of Teamsters v. Daniel,
No. 77-753 (August 21, 1978) (Powell’s marginal notes).

188Copy of J. Mark Fisher, Note, The Application of the Antifraud Provisions of the Securities Laws to Compulsory,
(1978) (Powell’s marginal notes).

189Conference Notes, No. 77-753 Inter. Brotherhood v. Daniel, (11/3/78) (Powell’s notation next to Blackmun’s vote to
reverse punctuated with two exclamation points).

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TRANSACTION AS CONSTITUTING A SALE UNDER CERTAIN PROVISIONS OF THE SEcurities Act BUT NOT UNDER OTHERS. 191 THE IMPlicit CONCERN HERE WAS THAT THE SEC was trying to EXTEND its REACH BY APPLYING THE ANTI-FRAUD RULES, WITHOUT RISKING A BACKLASH FROM CONGRESS IF IT APPLIED ITS BURDENSOME REGISTRATION REQUIREMENTS TO THE SAME TRANSACTIONS. 192 A “SALE” is a “SALE,” POWELL THOUGHT. FACED WITH OBJECTIONS FROM WHITE AND BURGER, HOWEVER, POWELL ELIMINATED THIS LANGUAGE AND RESERVED THE QUESTION. 193 THE COURT’S HOLDING IS LIMITED TO THE CONCLUSION THAT THE PENSION PLAN IN QUESTION WAS NOT AN INVESTMENT CONTRACT, AND THEREFORE, NOT A SECURITY. 194

THE DEFINITION OF “SALE” SOON RETURNED TO THE COURT. BANKERS TRUST CO. v. MALLIS RAISED THE ISSUE OF WHETHER THE PLEDGE OF STOCK TO SECURE A LOAN WAS A “SALE” OF THAT SECURITY FOR PURPOSES OF RULE 10B-5. 195 FOR POWELL, THE ANSWER WAS NO:

A PLEDGE IS NOT A TRANSFER OF TITLE. IT INVOLVES NEITHER A PURCHASE NOR A SALE, AND MY RECOLLECTION . . . IS THAT NOTHING WHATEVER IN [THE ACTS OF ’33 AND ’34] SUGGESTS OR IMPLIES THAT EITHER THE PLEDGE OF THE RELEASE OF SECURITIES

191 id.

192 Bench Memorandum from Paul [B. Stephan] to Mr. Justice Powell, International Brotherhood of Teamsters v. Daniel, No. 77-753 (August 21, 1978), at 18 (“[T]he SEC has taken the position that almost every form of injustice that results from a failure to disclose information violates § 10(b) of the Securities Exchange Act. That agency has been free to do this in part because it has not enforced a concomitant registration requirement, a burden that would both swamp the agency and engender substantial political pressure to amend the securities laws. A determination that a sale means the same thing for both registration and fraud may enable the SEC to take a more responsible position in these cases and to husband its resources for those situations where the securities laws were meant to apply.”).


FROM A PLEDGE CONSTITUTES A PURCHASE OR SALE WITHIN THE MEANING OF THE SECURITIES ACTS.\textsuperscript{196}

THE SECOND CIRCUIT’S CONTRARY CONCLUSION PROVOKED POWELL’S USUAL REACTION: “THE CASE APPEARS TO REPRESENT AN ATTEMPT TO EXTEND SIGNIFICANTLY THE REACH OF § 10 (B) FAR BEYOND THE ORIGINAL INTENT OF THE SECURITIES ACTS.”\textsuperscript{197} POWELL APPEARS FRUSTRATED BY THE SECOND CIRCUIT’S INDIFFERENCE TO THE COURT’S PRIOR REBUKES OF THAT COURT’S EXPANSION OF THE SECURITIES LAWS: “OUR CASES REFUTE VIEW THAT 10(b)5 [sic] IS A LICENSE TO FEDERALIZE CORP. LAW GENERALLY. SANTA FE, BLUE CHIP, FOREMAN [sic] (ACT OF ’33). I THINK CA2 IS DEAD WRONG!”\textsuperscript{198} POWELL CHARACTERIZED THE SOLICITOR GENERAL’S ARGUMENT SUPPORTING THAT COURT’S POSITION AS “ABSURD IN CONTEXT OF NORMAL COMMERCIAL TRANSACTIONS.”\textsuperscript{199}

THE VAGARIES OF LITIGATION, HOWEVER, COMPLICATED THE CASE. THE PLAINTIFFS CHANGED THEIR THEORY AT ORAL ARGUMENT, DECLINING TO DEFEND THE SECOND CIRCUIT DECISION. WORSE YET, IT TURNED UP THAT THERE WAS NO DOCUMENT RECORDING THE JUDGMENT OF THE DISTRICT COURT, SUGGESTING THAT THE SECOND CIRCUIT MAY HAVE LACKED JURISDICTION.\textsuperscript{200} THE COURT SPLIT 4-4 AT CONFERENCE. POWELL JOINED WITH BURGER, STEWART, AND REHNQUIST TO REVERSE, WHILE

\textsuperscript{196}Memo to Nancy Bregstein from LFP, Jr., No. 76-1359 Bankers Trust Co. v. Mallis and Kupferman, at 2 (October 25, 1977).

\textsuperscript{197}Id. at 3.

\textsuperscript{198}Bench Memo from Bob Comfort to Mr. Justice Powell, No. 76-1359 Bankers Trust Co. v. Mallis, (Nov. 18, 1977) (Powell’s marginal notes).

\textsuperscript{199}Bench Memo – Supplemental from Bob Comfort to Mr. Justice Powell, Bankers Trust Co. v. Mallis, No. 76-1359, at 1 (Nov. 28, 1977) (Powell’s marginal notes).

\textsuperscript{200}Bob Comfort, Memorandum for Mr. Justice Powell, Bankers Trust Co. v. Mallis, No. 76-1359 (Nov. 30, 1977).
BRENNAN, WHITE, MARSHALL AND STEVENS VOTED TO AFFIRM. BLACKMUN WAS ABSENT FROM THE
CONFERENCE. 201

LOOKING FOR A WAY OUT OF THE DEADLOCK, BRENNAN (IN THE ABSENCE OF THE CHIEF JUSTICE)
ASSIGNED REHNQUIST THE TASK OF SORTING OUT THE JUDGMENT ISSUE. REHNQUIST CONCLUDED THAT
THE REQUIREMENT OF A SEPARATED DOCUMENT MEMORIALIZING THE JUDGMENT COULD BE WAIVED AND,
THEREFORE, THAT THE SECOND CIRCUIT HAD JURISDICTION. 202 REHNQUIST HAD A MAJORITY FOR THIS
POSITION, THUS FORCING THE COURT TO ADDRESS THE MERITS. BUT THE COURT WAS DIVIDED EQUALLY
ON THE MERITS AND REHNQUIST FEARED AN AFFIRMANCE BY AN EQUALLY DIVIDED COURT. REHNQUIST
WORRIED THAT “[W]ITH HARRY’S VOTING RECORDS IN 10(b)(5) [sic] CASES, I THINK AFFIRMANCE
SHOWING HIM OUT WOULD BE TANTAMOUNT TO RATIFYING THE CA2 OPINION EVEN THOUGH WE WROTE
NOTHING.” 203 REHNQUIST THEREFORE PROPOSED A STRATEGIC RETREAT, DISMISSING THE PETITION FOR
CERTIORARI AS IMPROVIDENTLY GRANTED (A “DIG”). 204 AS TWO OF THE VOTES FOR AFFIRMANCE WERE
WILLING TO ACQUIESCE IN A DISMISSAL (WHITE AND STEVENS), REHNQUIST GOT A MAJORITY FOR THIS
COURSE AND THE PETITION WAS DISMISSED. 205

THIS MEANT THAT WHETHER A PLEDGE WAS A SALE REMAINED AN OPEN QUESTION TWO YEARS
LATER WHEN RUBIN V. UNITED STATES MADE ITS WAY TO THE COURT. 206 RUBIN DIFFERED, HOWEVER,

201Conference Notes, No. 76-1359 Bankers v. Mallis (12/2/77).


203Note from [J]ustice Rehnquist to Lewis (2/28/78).

204Id.

205Bankers Trust Co. v. Mallis, 435 U.S. 381, 388 (1978); Conference Notes, 76-1359 Bankers Trust (Special Conference
March 6, 1978).

IN THAT IT RAISED THE ISSUE UNDER SECTION 17(A) OF THE ‘33 ACT, RATHER THAN THE ‘34 ACT.\textsuperscript{207} 

While Section 3(a)(14) of the 1934 Act defines a sale as “any contract of sale or otherwise dispose of” a security, Section 2(3) of the 1933 Act defines “sale” as “every contract of sale or disposition of a security or interest in a security for value.”\textsuperscript{208} Congress’ inclusion of “every” and “interest” pushed toward a broad definition. Powell was unmoved by this textual distinction – the policy reasons for excluding this transaction from the scope of the securities law were the same. He agreed with his law clerk that “applying §17(a) to commercial loans seems to extend the scope of the 1933 Act beyond its purposes. Second, there seems to be no practical need for the extension.”\textsuperscript{209} Powell’s concerns were mitigated, however, by the fact that §17(a) did not give rise to a private cause of action and any interpretation by the Court would not control a 10b-5 case.\textsuperscript{210} In any event, Powell’s support in Bankers Trust evaporated in Rubin; Burger, Stewart and Rehnquist all switched sides. Powell bowed to reality and voted to uphold the broad interpretation.\textsuperscript{211}

\textsuperscript{207}15 U.S.C. §77r.

\textsuperscript{208}15 U.S.C. 77b(3).

\textsuperscript{209}Bench Memorandum to Mr. Justice Powell from Peter Byrne, No. 79-1013 Rubin v. United States, at 13 (September 16, 1980) (Powell noting agreement).

\textsuperscript{210}Id. at 16.

\textsuperscript{211}Conference Notes, No. 79-1013 Rubin v. U.S. (Conf. 11/14/80).
POWELL’S ACQUIESCENCE LEFT HIM IN THE POSITION OF DAMAGE CONTROL. POWELL WAS DISAPPOINTED BY BURGER’S “SIMPLISTIC” OPINION,\textsuperscript{212} BUT HE OFFERED TO JOIN IT IF BURGER WOULD REFRAIN FROM CITING:

THE 1963 CASE OF \textsc{Sec v. Capital Gains Research Bureau}, quoting language to the effect that federal security laws must be construed “not technically and restrictively but flexibly to effectuate [their] remedial purposes.”

A NUMBER OF MORE RECENT DECISIONS, FOR EXAMPLE, \textsc{Hochfelder} relied on by your opinion, have looked primarily to the plain language of the securities acts. These are highly technical and well drawn statutes, and as you make clear by the remainder of your opinion this case falls within the explicit language of §§2(3) and 17(a). Thus, the quote from \textsc{Capital Gains Research Bureau} is unnecessary and perhaps could be viewed as undercutting to some extent your reliance on the statutory language itself.\textsuperscript{213}

THE QUOTED LANGUAGE WAS A STAPLE OF THE SEC’S BRIEFS, REFLECTING THE INTERPRETIVE STYLE THAT POWELL WAS ANXIOUS TO EXPUNGE FROM THE SECURITIES LAWS.\textsuperscript{214} POWELL ALSO WANTED A FOOTNOTE RESERVING THE STATUS OF PLEDGES UNDER THE ’34 ACT.\textsuperscript{215} BURGER DROPPED THE OFFENSIVE LANGUAGE FROM \textsc{Capital Gains}, but he declined to include the footnote explicitly reserving the question under the 1934 Act.\textsuperscript{216} PREDICTABLY, THE LOWER COURTS HAVE INTERPRETED THE ’34


\textsuperscript{214} Id. at 1-2.

\textsuperscript{215} Id. at 2.

\textsuperscript{216} Letter from the Chief Justice to Lewis F. Powell, Jr., No. 79-1013 Rubin v. United States (January 8, 1981).
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Act definition of “sale” to include pledges of securities.\textsuperscript{217} Perhaps Powell should have challenged Burger on this issue, rather than the inclusion of the cite to \textit{Capital Gains}.\textsuperscript{218}

D. Private rights of action

The implication of private rights of action under federal statutes was of paramount importance to Powell. Powell worried that novel causes of action for securities law violations could impose crippling liability. Accordingly, his work in this area is characterized by a consistent effort to curtail causes of action not authorized by statutory text. The Court’s decision in \textit{J.I. Case v. Borak}\textsuperscript{219} in 1964 reflected a liberal attitude toward implying private rights of action. Proponents of implied private rights relied on broad readings of congressional purpose.\textsuperscript{220} Powell, by contrast, emphasized the possible interference with regulatory schemes that could result from the judicial creation of private rights of action. In addition, Powell worried about the separation of powers issues raised by the judiciary expanding its own jurisdiction through the creation of private rights of action.

\textsuperscript{217}See, e.g., Chemical Bank v. Arthur Andersen & Co., 726 F.2d 930 (2\textsuperscript{nd} Cir.), cert. denied, 469 U.S. 884 (1984).

\textsuperscript{218}Powell’s efforts to root out the \textit{Capital Gains} decision were for naught, as the Court’s most recent opinion in this area (expanding the reach of the securities laws) invokes the case. SEC v. Zandford, 122 S.Ct. 1899 (2002).

The Court decided one other case during Powell’s tenure that touches upon the “offer or sale” language, United States v. Naftalin, 441 U.S. 768 (1979), but Powell was absent from argument due to complications from surgery and therefore did not participate in the decision. 1\textsuperscript{st} Draft, United States v. Naftalin, No. 78-561 (8 May 1979).

\textsuperscript{219}377 U.S. 426 (1964).

\textsuperscript{220}See, e.g., Fleischer, supra note at 1174-1175.
THE FIRST SECURITIES CASE DURING POWELL’S TENURE TO GENERATE CONTROVERSY OVER IMPLIED PRIVATE CAUSES OF ACTION WAS PIPER V. CHRIS-CRAFT INDUSTRIES.\(^{221}\) THE FACTS OF THE CASE WERE CONVOLUTED, WITH TWO BIDDERS, CHRIS-CRAFT AND BANGOR PUNTA, VYING TO TAKE OVER THE PIPER AIRCRAFT CORPORATION (CONTROLLED BY THE PIPER FAMILY). AFTER MANY TWISTS, BANGOR PUNTA ULTIMATELY PREVAILED AND CHRIS-CRAFT SOUGHT DAMAGES UNDER §14(e) AND RULE 10b-6 OF THE EXCHANGE ACT,\(^{222}\) ALLEGING THAT BANGOR PUNTA, THE PIPER FAMILY, AND FIRST BOSTON (BANGOR PUNTA’S UNDERWRITER) HAD VIOLATED THE SECURITIES LAWS IN GAINING CONTROL OF PIPER.\(^{223}\)

POWELL VIEWED THE QUESTION OF SCIENTER AS CENTRAL TO THE CASE:

THE LANGUAGE OF SECTION 10(b) AND OF SECTION 14(e) IS SUFFICIENTLY SIMILAR TO JUSTIFY THE CONCLUSION THAT THE ERNST AND ERNST HOLDING WITH RESPECT TO § 10(b) WILL GOVERN § 14(e). MY PRELIMINARY IMPRESSION IS THAT CA2 (JUDGE TIMBERS) ENUNCIATED AND APPLIED A STANDARD OF LIABILITY CONSIDERABLY LESS SEVERE THAN THE SCIENTER STANDARD WE ADOPTED IN ERNST AND ERNST.\(^{224}\)

IN ADDITION TO THE TEXTUAL SIMILARITIES BETWEEN § 10(b) AND § 14(e), POWELL ALSO IDENTIFIED “IDENTICAL POLICY REASONS” TO THOSE THAT HAD DRIVEN THE DECISION IN ERNST & ERNST: “WHEN A COURT IMPLIES A CAUSE OF ACTION FOR DAMAGES, IT SHOULD HESITATE – EVEN IF THE FIRST HURDLE

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\(^{221}\) 430 U.S. 1 (1977). An earlier case raising the question of the implication of a private right of action from a regulatory scheme, Securities Investor Protection Corporation v. Barbour, 421 U.S. 412 (1975), had generated no controversy. The Securities Investor Protection Act (“SIPA”) gave the Securities Investor Protection Corporation (“SIPC”) the power, in its discretion, to apply for a decree invoking the protections of the SIPA. 15 U.S.C. § 78ggg(b). That power was subject to oversight by the SEC, which was authorized, again in its discretion, to apply to the relevant district court for an order requiring the SIPC to cover a particular situation. Id. Notwithstanding this regulatory scheme, the Sixth Circuit had held that investors had a private cause of action to enforce the SIPC, despite the absence of any mention of such a cause of action in the statute. 496 F.2d 145 (6th Cir. 1977). The Court unanimously voted to reverse. Conference Notes, 73-2055 Securities Investor v. Barbour (Conf. 3/19/75).


\(^{223}\) Piper, 430 U.S. at 4-5.

IS CLEARED (II IS WITHIN SPECIALLY PROTECTED CLASS) – TO IMPOSE A LOW STANDARD (THRESHOLD) OF LIABILITY. 225 ON THE QUESTION OF WHETHER A CAUSE OF ACTION SHOULD BE IMPLIED AT ALL FOR DEFEATED TENDER OFFERORS, POWELL DOUBTED THAT THEY WARRANTED PROTECTION: “OFFERORS CAN TAKE CARE OF THEMSELVES. (ALWAYS CORPS. OF SOME SIZE).” 226 POWELL WAS ALSO TROUBLED BY THE DAMAGES AWARD, WHICH HAD LITTLE RELATION TO ANY ECONOMIC HARM: “THE $35 MIL. JUDGMENT EXCEEDS ENTIRE NET WORTH (NET EQUITY) OF PIPER.” 227

THE COURT SIDESTEPPED THE SCIENTER ISSUE, INSTEAD HOLDING THAT THE WILLIAMS ACT DID NOT PROVIDE A CAUSE OF ACTION FOR DAMAGES TO A DEFEATED BIDDER IN A TAKEOVER CONTEST. THE COURT APPLIED THE FOUR-FACTOR TEST PREVIOUSLY ANNOUNCED IN CORT V. ASH: (1) WHETHER THE PLAINTIFF IS A MEMBER OF THE “CLASS FOR WHOSE ESPECIAL BENEFIT THE STATUTE WAS ENACTED”; (2) WHETHER THERE IS ANY EXPRESSION OF LEGISLATIVE INTENT TO CREATE OR DENY A PRIVATE CAUSE OF ACTION; (3) WHETHER A PRIVATE REMEDY WOULD BE CONSISTENT WITH THE PURPOSES OF THE LEGISLATIVE SCHEME, AND (4) WHETHER THE CAUSE OF ACTION IS ONE “TRADITIONALLY RELEGATED TO STATE LAW.” 228 THE CRITICAL FACTOR HERE WAS THAT TARGET SHAREHOLDERS, NOT RIVAL BIDDERS, WERE THE CLASS THAT CONGRESS INTENDED TO PROTECT BY ENACTING THE WILLIAMS ACT. 229 POWELL

225 Notes, Chris-Craft (10/4/76).

226 Id.

227 Notes for Conference, 75-353 Bangor Punta (10/5/76). Powell had previously noted that First Boston faced “the imposition on it of three times the amount of damages that would be imposed under Section 11 of the 1933 Act.” Memo to file from LFP; No. 75-353, -354, and -355 Piper, et al. v. Chris Craft Industries, Inc., at 3 (8/26/76).

228 Piper, 430 U.S. at 37-41 (citing Cort v. Ash, 422 U.S. 66 (1975)).

229 430 U.S. at 26-36.
HAD NO QUARREL WITH THIS REASONING, ALTHOUGH HE WORRIED THAT "THERE IS SOME INCONGRUITY IN DISTINGUISHING, FOR STANDING PURPOSES, BETWEEN INJUNCTIVE AND DAMAGE RELIEF."230

**Health problems forced Powell to miss the Court’s next foray into implied rights of action in securities law.**231 Powell also missed the argument in *Transamerica Mortgage Advisors*, but the Court split 4-4,232 so it was set for reargument the next term. In his draft dissent from the initial denial of certiorari (the Court subsequently voted to grant), Powell proposed a high threshold for implying a private right of action: "Recent decisions of this Court have reaffirmed that private causes of action will be inferred from securities statutes only if such an inference is consistent with the language and history of the statute and is necessary to avoid subversion of Congress’ purpose in passing the statute."233 Rare will be the case where the implication of a private right of action is "necessary to avoid subversion of Congress’ purpose"—if it were "necessary," presumably Congress would have provided for it. Never a proponent of implied rights, Powell was now actively hostile:

*I have come to think that the Court has gone much too far in inferring federal private causes of action where Congress has chosen to remain silent. Principles of federalism where state courts traditionally have*

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230Letter to the Chief Justice from Lewis F. Powell, Jr., Nos. 75-353, 75-354, and 75-355 (The Bangor Punta Cases) (December 30, 1976).

231Touche Ross v. Redington, 442 U.S. 560 (1979) (finding no private cause of action under § 17(a) of the Exchange Act, which requires broker-dealers to keep books and records as required by the SEC). Powell appears to have agreed with the result: "§17(a) is not an anti-fraud statute. It proscribes nothing. It merely requires reports. §18a provides remedies." Preliminary Memorandum, No. 78-309, Touche Ross & Co. v. Redington (November 22, 1978 Conference).

232Argument Notes, 77-1645 *TransAmerica v. Lewis* (Argued 10/2/79) ("Last Spring Aff.: WJB, BRW, TM, JPS. Rev.: WHR, HAB, PS, Cl.").

2331st Draft, Transamerica Mortgage Advisors, Inc. v. Lewis, Nos. 77-1645 and 77-1717, at 3 (12 October 1978).
EXERCISED JURISDICTION OVER A PARTICULAR TYPE CLAIM, SHOULD REQUIRE THAT CONGRESS CONFRONT OPENLY THE QUESTION WHETHER THERE ARE SOUND REASONS FOR ALSO AUTHORIZING FEDERAL COURT SUITS. ONE EVEN CAN SUSPECT THAT THE DRAFTSMEN AND SPONSORS OF LEGISLATION, TAKING NOTE OF WHAT CAN BE DESCRIBED AS THE EAGERNESS OF FEDERAL COURTS TO ENHANCE THEIR OWN JURISDICTION, DELIBERATELY AVOID LEGISLATIVE HEARINGS AND CONTROVERSY SIMPLY BY DRAFTING STATUTES IN WHAT [DEPUTY SOLICITOR GENERAL FRANK] EASTERBROOK CALLS A “NEUTRAL” FASHION.\(^{234}\)

POWELL WAS READY TO RETHINK IMPLIED PRIVATE RIGHTS OF ACTION.

POWELL FIRED THE FIRST VOLLEY IN THIS DEBATE BEFORE *TransAmerica* COULD BE REARGUED. *Cannon v. University of Chicago* INVOLVED THE QUESTION OF THE IMPLICATION OF A PRIVATE RIGHT OF ACTION UNDER *Title IX*, WHICH PROHIBITS SEX DISCRIMINATION BY UNIVERSITIES RECEIVING FEDERAL AID.\(^{235}\) POWELL DISSenting, ARGUING THAT “[W]HEN CONGRESS CHOOSES NOT TO PROVIDE A PRIVATE CIVIL REMEDY, FEDERAL COURTS SHOULD NOT ASSUME THE LEGISLATIVE ROLE OF CREATING SUCH A REMEDY AND THEREBY ENLARGE THEIR JURISDICTION.”\(^{236}\) *J.I. Case v. Borak*\(^{237}\) WAS SINGLEd OUT FOR SPECIAL SCORN, AS A:

DECISION BOTH UNPRECEDENTED AND INCOMPREHENSIBLE AS A MATTER OF PUBLIC POLICY. THE DECISION’S RATIONALE, WHICH LIES ULTIMATELY IN THE JUDGMENT THAT “[P]RIVATE ENFORCEMENT OF THE PROXY RULES PROVIDES A NECESSARY SUPPLEMENT TO COMMISSION ACTION,” IGNORES THE FACT THAT CONGRESS, IN DETERMINING THE DEGREE OF REGULATION TO BE IMPOSED ON COMPANIES COVERED BY THE SECURITIES EXCHANGE ACT, ALREADY HAD DECIDED THAT PRIVATE ENFORCEMENT WAS UNNECESSARY. MORE SIGNIFICANT FOR PRESENT PURPOSES, HOWEVER, IS THE FACT THAT *Borak*, RATHER THAN SIGNALING THE START OF A TREND IN THIS COURT, CONSTITUTES A SINGULAR AND, I BELIEVE, ABERRANT INTERPRETATION OF A FEDERAL REGULATORY STATUTE. . . ALTHOUGH I DO NOT SUGGEST THAT WE SHOULD CONSIDER

\(^{234}\) Memorandum to Clerk from Lewis F. Powell, Jr., No. 77-1645 TransAmerica Mortgage [sic] v. Lewis, at 6-7 (Feb. 20, 1979).

\(^{235}\) 441 U.S. 677 (1979).

\(^{236}\) 441 U.S. at 730-731.

\(^{237}\) 377 U.S. 426 (1964).
OVERRULING \textit{Borak} at this late date, the lack of precedential support for this decision militates strongly against its extension beyond the facts of the case.\textsuperscript{238}

The expansion of private rights of action during the 1960s had fueled the expansion of the securities laws and Powell was now ready to tackle head-on the source of the problem.

When TransAmerica was finally reargued, Powell worried that the damages remedy that the plaintiffs were seeking “would allow circumvention of Ernst + Ernst and Blue Stamps [sic], etc.”\textsuperscript{239} Whether this result was appropriate was a question for Congress; the issue for the Court was what Congress intended.\textsuperscript{240} Powell found Congress’s intention clear from the text of the statute: the Investment Advisors Act conferred jurisdiction over suits in equity, but unlike the Securities Act and Exchange Act, omitted jurisdiction over suits at law.\textsuperscript{241} For Powell, anxious to narrow the reach of the federal securities law, this textual difference was decisive.

The split in the Court that had required putting the case over for reargument reemerged. This time, however, Powell joined Stewart, Blackmun and Rehnquist in voting against the recognition of the private right of action; Burger, who had agreed with the latter three after the first argument, was now “reserving judgment.”\textsuperscript{242} Stewart now said he agreed with Powell’s intervening dissent in \textit{Cannon}, but he had voted with the

\textsuperscript{238}\textit{Cannon}, 441 U.S. at 735-736 (citations omitted).

\textsuperscript{239}Argument Notes, 77-1645 \textit{TransAmerica v. Lewis} (Argued 10/2/79).

\textsuperscript{240}Id.

\textsuperscript{241}Notes for Conference, 77-1645, TAMA (10/4/79).

\textsuperscript{242}Conference Notes, 77-1645 TransAmerica v. Lewis, (Conf. 10/5/79).
MAJORITY ONLY “BECAUSE OF VOTE IN BAKKE” WHICH POWELL NOTES WAS ALSO TRUE OF RENQUIST. 243 THE RANDOM INTERVENTION OF BAKKE HAD PRESERVED THE PRIVATE RIGHT IN CANNON, BUT THE CONSENSUS SUPPORTING PRIVATE RIGHTS OF ACTION WAS ERODING.

WITH BURGER ON THE FENCE, HOWEVER, TRANSAMERICA WAS NOT THE CASE FOR RETHINKING THE COURT’S PRIVATE RIGHT OF ACTION DOCTRINE. STEWART, WHO UNDERTOOK THE OPINION IN AN EFFORT TO GET A MAJORITY, DID NOT REPUDIATE THE FOUR-FACTOR TEST OF CORT V. ASH, BUT HE TOOK A STEP TOWARD POWELL’S POSITION IN EMPHASIZING THAT THE “DISPOSITIVE QUESTION REMAINS WHETHER CONGRESS INTEND TO CREATE ANY SUCH REMEDY.”244 POWELL WAS WILLING TO GO ALONG WITH THIS APPROACH, ALTHOUGH HE FILED A BRIEF CONCURRENCE NOTING THAT HE SAW STEWART’S OPINION AS “COMPATIBLE WITH MY DISSENT IN CANNON.”245

HE ALSO LOBBIED STEWART (IN A PRIVATE LETTER) TO DEFINE NARROWLY THE EQUITABLE ACTION FOR RESCISSION THAT THE COURT WAS RECOGNIZING.246 AT POWELL’S URGING, STEWART ADDED A FOOTNOTE LIMITING THE RESTITUTION AVAILABLE UNDER THE ACT.247 POWELL ALSO ARGUED (TO NO AVAIL) AGAINST CITING “BORAK AT ALL. AN ANOMALY WHEN DECIDED, AND IN LIGHT OF MORE

243Id. Stewart and Rehnquist had avoided the constitutional issue in Bakke by agreeing with Stevens that the affirmative action plan challenged there was prohibited by Title VI of the Education Amendments, which forbid discrimination on the basis of race. That necessarily supposed that Bakke had a private right of action to assert his claim. The two felt obliged to uphold the private right of action in Cannon, thus creating a five-vote majority in that case. Conference Notes, 77-926 Cannon v. University of Chicago (1/12/79) (Under Stewart, “Reverse (unhappily) . . . In view of vote last term in Bakke, ‘I’m stuck.’” Under Rehnquist, “Reverse reluctantly. Bakke should won on 14th Amend., + WHR is uncomfortable with his vote on VI. But can’t think of principled way to reverse his vote in Bakke.”). Brennan noted at the time of Bakke that there was probably a majority that would have voted against a private right of action under Title VI, but he did not include Stewart in that majority. Lee Epstein & Jack Knight, Piercing the Veil: William J. Brennan’s Account of Regents of the University of California v. Bakke, 19 Yale L. & Pol. Rev. 341, 358 (2001).


245444 U.S. at 25 (Powell, J., concurring).

246Letter from Lewis F. Powell, Jr. to Mr. Justice Stewart, No. 77-1645 TAMA v. Lewis (October 30, 1979).

247444 U.S. at 24 n.14.
RECENT CASES (Especially TOUCHE, ROSS, and your opinion in this case), I VIEW BORAK AS A
‘DEAD COCK IN THE PIT.’” Powell wanted to eradicate all vestiges of the interpretive
attitude that had fueled the expansion of the federal securities laws in the 1960s. In this
quest he appears ultimately to have prevailed – the Court now requires that Congress
speak in “clear and unambiguous terms” when it creating a private right of action.249

TWO TERMS LATER IN HERMAN & MACLEAN V. HUDDLESTON, THE COURT SQUARELY FACED THE
MECHANISM RESPONSIBLE FOR THAT EXPANSION: THE IMPLIED PRIVATE RIGHT OF ACTION UNDER RULE
10B-5.250 THE QUESTION UNDERLAY THE QUESTION OF WHETHER SECTION 10(b) AFFORDED A PRIVATE
CAUSE OF ACTION FOR CONDUCT THAT WOULD BE ACTIONABLE UNDER THE EXPLICIT PRIVATE CAUSE OF
ACTION PROVIDED BY SECTION 11 OF THE SECURITIES ACT. WHILE POWELL WAS “TEMPTED” TO VOTE
THAT THERE WAS NO PRIVATE CAUSE OF ACTION UNDER SECTION 10(b), HE PULLED BACK FROM
REPUDIATING A CAUSE OF ACTION THAT WENT BACK MORE THAN THIRTY YEARS.251 HAVING CONCEDED
THE EXISTENCE OF THE PRIVATE RIGHT OF ACTION UNDER SECTION 10(b), POWELL SAW NO DEFENSIBLE
BASIS FOR CARVING OUT EXCEPTIONS WHEN THE SECURITIES LAWS EXPRESSLY PROVIDED CAUSES OF
ACTION.252

248 Letter from Lewis F. Powell, Jr. to Mr. Justice Stewart, No. 77-1645 TAMA v. Lewis (October 30, 1979); 444 U.S. at 15 (citing Borak).
251 Bench Memorandum to Mr. Justice Powell from Jim [Browning], Herman & MacLean v. Huddleston, et. al., No. 81–680, at 20 (09/09/82).
252 Id. at 1, 11. The Court addressed one additional case raising the question of an implied right of action under the securities laws, but the conclusion that there was no private right was uncontroversial. Daily Income Fund v. Fox, 464 U.S. 523 (1984) (holding shareholders asserting a claim under Investment Company Act need not satisfy the demand requirement of Fed. R. Civ. P. 23.1 because investment company had no implied right of action under the Act).
PART FOUR: PREDICTABILITY

Determinable legal rules allow lawyers to counsel corporate clients who are trying to stay within the law; they may, however, also provide a roadmap for those seeking to evade the policies behind those laws. The latter possibility does not appear to have concerned Powell unduly. Like most corporate lawyers, Powell favored predictability.

In a 1967 speech to a conference of financial executives, Powell canvassed the state of antitrust law, fretting that “the trend of merger decisions seems steadily into the smog of uncertainty – rather than toward higher visibility and predictability.”

Powell was open to amendment of the antitrust laws to clarify their application. A revised antitrust code would allow “economic realism, rather than nebulous and varying legal concepts, [to guide] corporate expansion.”

Although the speech was on antitrust, the sentiment carried over to the interpretation of the securities laws. Powell’s preference for predictability was generally, but not always, consistent with his desire to limit liability. For example, Powell argued in Gordon v. NYSE that: “It would be grossly inequitable to impose liability of this magnitude [a claimed $1.5 billion in damages, plus attorneys fees] upon private parties who have, for nearly 40 years, followed a practice to the knowledge of

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254Id. at 17.

255Gordon v. NYSE, Inc., 422 U.S. 659 (1975) (holding that NYSE was immune from antitrust liability for fixing commission rates among its members because of SEC oversight); see also United States v. NASD, 422 U.S. 694 (1975) (holding that certain sales practices of investment companies are immune from antitrust liability because of SEC oversight).
THE GOVERNMENT AND WITH FULL APPROVAL OF THE AGENCY ESTABLISHED BY THE CONGRESS TO REGULATE THIS BUSINESS."

Powell could not countenance springing liability on firms for well-settled business practices with the imprimatur of regulatory approval. Powell’s aversion to unanticipated liability exposures would be a recurring theme.

A. Short Swing Profits Under Section 16(b)

Kern County Land Co. v. Occidental Petroleum,257 involved the recovery of short swing profits under Section 16(b) of the Exchange Act.258 The facts were somewhat convoluted, but the basic question was a recurring one: when a bidder for a company loses out to a competing bidder, what is the status under Section 16(b) of profits derived from the losing bidder’s “toehold” acquisition? Occidental Petroleum acquired a twenty percent stake in Kern through a tender offer, thereby making it a statutory insider within the meaning of Section 16.259 Kern then arranged a defensive transaction, in the form of a sale of assets, with Tenneco at a substantial premium above Occidental’s offer.

This put Occidental in a difficult position. If Kern sold its assets and the Tenneco stock was distributed to Kern’s shareholders within six months of the purchase making Occidental a 10% holder, Occidental’s profits on the exchange could be subject to disgorgement under Section 16(b). Critically, Occidental could not control the timing of


25815 U.S.C. §78p(b). Section 16(b) provides for the disgorgement of trading profits by insiders (defined to include holders of more than ten percent of a company’s equity) resulting from purchases and sales, or sales and purchases, within six months of each other.

The exchange. Tenneco did not want a large block of its stock in potentially hostile hands, so it entered into an option agreement with Occidental whereby Tenneco could repurchase the Tenneco shares that Occidental would receive after the Kern asset sale. The option could not be exercised, however, until six months and one day after the closing of Occidental’s tender offer, thereby putting that part of the transaction outside Section 16(b)’s window. Tenneco exercised the option, but nonetheless caused its acquisition subsidiary, New Kern, to file suit against Occidental for recovery of its profits under Section 16(b).260

The conference split 4-4, with Justice White passing.261 With the outcome in doubt, Powell wrote a memo to White. There was general agreement that the option agreement was not a sale, but the exchange of shares pursuant to the asset sale posed a closer question. Powell argued that the statutory language itself compelled the conclusion that the exchange of shares was not a sale: “The concept of a purchase or sale necessarily connotes volition, i.e., a willing or conscious act on the part of the 10% owner. There is no such act in this case, and the absence of it seems to me to be dispositive.”262 The sale of assets required only a majority vote of Kern’s shareholders and California law did not provide for appraisal. Accordingly, Occidental had no

260 The Exchange Act’s anti-waiver provision precluded Tenneco from contractually waiving its rights under Section 16(b).

261 Conf. Notes, 71-1059 Kern Cty. v. Occidental, Conf. 12/8/72. Powell’s note indicate that Justice Blackmun tentatively voted to reverse, but subsequently switched his vote.

262 Memorandum from Lewis F. Powell, Jr. to Mr. Justice White, No. 71-1059 Kern County v. Occidental, (December 9, 1972).
ALTERNATIVE TO THE EXCHANGE: “there may have been a ‘shotgun wedding’ but there certainly was no sale.”

White joined Powell’s side to form a majority. The Chief Justice assigned the opinion to White, perhaps to keep a wavering member of the majority on board. While Powell agreed with White’s general approach, Powell felt that the opinion did not emphasize sufficiently that the exchange of shares was involuntary. Powell wrote that he would consider a concurrence because “Bar needs an answer to this question. This opinion is fact oriented [and] gives little guidance.” Powell thought White’s unduly emphasized “whether Occidental could have had insider information, an “immaterial” concern, because Occidental could not [and] did not arrange the merger.” Powell also disliked White’s reference to the fact that appraisal was not available, which Powell considered “not a dispositive fact,” and the statement that “We do not suggest that an exchange of stock pursuant to a merger may never result in § 16 (b) liability.” Powell favored a more sweeping holding offering clearer guidance. He feared that courts and lawyers would struggle to apply White’s flexible standard, a concern that has proved to be justified.

261Id. at pp. 2-3.


263Id. at 14-16 (Powell’s marginal notes).

264Id. at 18 (Powell’s marginal notes).

265See James D. Cox et al., Securities Regulation: Cases and Materials 1001 (3rd ed. 2001) (“Ever since the Supreme Court announced its Kern County pragmatic approach, the lower courts have had trouble applying it.”).
POWELL JOINED WHITE’S OPINION, BUT DRAFTED A CONCURRENCE, NOTING THAT “THE COURTS AND COUNSEL HAVE BEEN PERPLEXED AS TO THE APPLICABILITY OF §16 (B) TO A WIDE VARIETY OF ‘UNORTHODOX’ TRANSACTIONS. COUNSEL CALLED UPON TO ADVISE CLIENTS WITH RESPECT TO SUCH TRANSACTIONS HAVE LACKED DEFINITIVE GUIDANCE.”

A “FACTUALLY ORIENTED ‘PRAGMATIC’ APPROACH” MIGHT BE NECESSARY IN SOME CASES, EVEN THOUGH IT RISKED BEING “INEXACT” AND “EVEN SUBJECTIVE.”

BUT “THE COURT NEED NOT HAVE REACHED IN THIS MERGER CASE THE INQUIRY WHICH IS THE FOCUS OF ATTENTION UNDER THE ‘POSSIBILITY OF ABUSE’ TEST, WITH ITS FOCUS ON THE DEFENDANT’S ACCESS TO INSIDE INFORMATION.” THAT INQUIRY WAS “IMATERIAL” BECAUSE OCCIDENTAL “COULD NEITHER HAVE BLOCKED THE MERGER NOR ASSURED ITS CONSUMMATION. . . . THERE WAS SIMPLY NO ACT OF VOLITION – INDEED NO RELEVANT ACT AT ALL – ON THE PART OF RESPONDENT WITH RESPECT TO THE ACCOMPLISHMENT OF THE MERGER.”

POWELL’S “VOLITIONAL” APPROACH WOULD HAVE PROVIDED A MORE DETERMINATE TEST THAN WHITE’S POSSIBILITY OF ABUSE STANDARD. POWELL WAS QUITE TOLERANT OF PRIVATE PLANNING TO AVOID THE COVERAGE OF SECTION 16(B), EVIDENTLY THINKING THAT THE ABUSES CONGRESS SOUGHT TO CURB THROUGH THE STATUTE WERE REMOTE. POWELL NOTES IN HIS MEMO TO HIS CLERK ASKING

In truth, as you know from our discussions, even one who enjoys the status of a 10% stockholder is not entitled by virtue of that status to any inside information. To be sure, if such a stockholder is able to place a representative on the board, the stockholder may end up obtaining the information. This would certainly be true if an individual owned 10% and also served as an officer or director. But absent a presence on the board there would be a clear violation of 10b-5 for a corporation (or its

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HIM TO REVIEW THE CONCURRENCE THAT “I KNOW FROM PROFESSIONAL EXPERIENCE THAT THIS IS AN AREA WHICH CREATES CONSIDERABLE DOUBT AND CONFUSION. MY CONCURRENCE WILL NOT HELP MUCH, BUT IT MAY PUT THE QUESTION WHICH LAWYERS USUALLY ARE CALLED UPON TO ANSWER IN A LITTLE SHARPER FOCUS.”

Powell’s file does not reveal why he decided against publishing the concurrence, to which White had “no objection whatsoever.” Perhaps White’s reminder that Occidental was already a 10% shareholder when it extended its tender offer caused Powell to rethink the wisdom of his concurrence; getting into this question might require the Court to resolve the issue of “whether these shares obtained by the tender offer should be treated as having been obtained all at one time or at separate times.”

The majority was fragile enough without taking on this question.

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275Id.

The question of whether the purchase that makes an individual a ten percent holder is subject to Section 16(b) was presented in Foremost-McKesson v. Provident Securities Co. 423 U.S. 232 (1976). Provident had sold its assets to Foremost-McKesson in exchange for convertible debentures and cash. If converted, the debentures would have made Provident a ten percent holder of Foremost’s equity. Provident did not convert, but instead promptly sold the debentures to an investment bank pursuant to an underwriting arrangement. Foremost-McKesson then filed suit under 16(b) to recover Provident’s profits.

In his notes for use at the Court’s conference, Powell argued that under the plain language of the proviso, “Provident was not a 10% holder at time of purchase. At that time it was zero holder.” Notes for Conference, No. 74-742 Foremost v. Provident, at p.1 (10/10/75). Moreover, the purpose of the statute – to prevent the unfair use of information – would not be served by liability in this case because “[u]ntil one becomes 10% holder, Congress has concluded there is little likelihood of obtaining information to use unfairly. 16(b) is directed vs. insiders. One is not an insider under statute until he owns 10%. What information can he acquire “simultaneously” with purchasing 10%?" Id. at 2. Powell also argued that a statute requiring “liability w/o fault” such as Section 16(b) should be “construed strictly – not expansively.” The equities, “altho[ugh] irrelevant” did not favor Foremost-McKesson, which sold the debentures to Provident “with full knowledge . . . that they would be sold.” Id. at 3. Powell’s observation that this was “[n]ot a pretty
B. Materiality

Materiality arises in virtually every securities lawsuit, whether brought by a private litigant, the SEC, or the Justice Department. The higher the standard for materiality, the lower the risk that corporations will run afoul of the securities laws. The Court addressed this universal issue in only one case during Powell’s tenure, TSC v. Northway.277 The Seventh Circuit had held that certain omissions from a proxy statement were material as a matter of law because they “might have been considered important by a reasonable shareholder.”278

Powell saw this formulation as an “unrealistic standard,”279 a view perhaps colored by his perception of the case as a “strike suit.”280 Powell instead argued at conference for his reading of the Second Circuit’s standard: a “significant likelihood that a reasonable investor would consider information important in arriving at his choice of action.”281 Powell characterized this standard as “middle-of-road” and argued that “courts should avoid extreme standards either of laxity or liability” when dealing with a “judicially created remedy.” Powell’s characterization seems a bit stained here.

posture for a litigant who is relying on a statute designed to prevent unfairness!” may have resonated with some of his colleagues. Id. Powell’s final argument was grounded in experience: “Proviso distinguishes between officers + directors – and 10% owners. There is a reason: Vast difference between managerial insiders and stockholders.” Id. Having served on numerous corporate boards, Powell was well placed to assess the access to information enjoyed by blockholders.


278Preliminary Memo, No. 74-1471, TSC Indus., Inc. v. Northway, Inc., at 2 (Summer List 1).

279Id. at 1 (Powell’s marginal notes).


281Id.
Although the private right of action under Rule 10b-5 is judicially created, the materiality language is drawn from the statute and applies to both private and SEC actions.

After articulating the standard, Powell then went through a careful explication of the facts in arguing that the Seventh Circuit had erred in holding that the omissions were material as a matter of law, rather than leaving them for the jury. Powell’s thorough preparation paid off, as the Chief Justice, Stewart, Marshall and Rehnquist agreed with him across the board.

Powell liked Marshall’s draft opinion, with two small exceptions. Marshall wrote that “[o]ur cases have not considered, and we have no occasion in this case to consider, what showing of culpability, if any, is required to establish the liability under § 14(a).” The “if any” drew Powell’s ire – even the suggestion of strict liability was anathema – and Marshall withdrew the offensive language. Powell also objected to a footnote reserving judgment “as to how the standard of materiality and its application might be altered in a case involving a contested election.” Powell the corporate lawyer could not have been comfortable with the notion that the supposedly-objective standard for materiality might vary with the context in which it was applied. Even Blackmun, no

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282 Id. at 3-5.


284 Typescript Draft, No. 74-1471, TSC Industries, Inc. v. Northway, Inc. at FN-4, n. 7 (emphasis supplied). Focused as they were on the summary judgment awarded to plaintiffs in this case, none of the justices appears to have given any thought to the implications that precluding pre-trial materiality determinations might have on defendants who were seeking dismissal.
FRIEND OF DEFENDANTS IN SECURITIES CASES, SHARED THIS CONCERN.285 THE OFFENDING FOOTNOTE WAS REMOVED. THE STANDARD ADOPTED IN TSC EVENTUALLY BECAME THE GENERAL STANDARD OF MATERIALITY UNDER THE SECURITIES LAWS.286

C. DEFINITION OF SECURITY

THE DEFINITION OF A SECURITY IS A THRESHOLD ISSUE IN SECURITIES LAW.287 UNLESS A TRANSACTION INVOLVES A SECURITY, THE FEDERAL SECURITIES LAWS DO NOT APPLY. PRIOR TO POWELL’S APPOINTMENT, THE SUPREME COURT HELD EVERY INSTRUMENT IT REVIEWED TO BE A SECURITY.288 DURING POWELL’S TENURE, THE COURT DECIDED FIVE CASES RAISING THIS QUESTION, REJECTING THE SECURITY LABEL IN THREE. POWELL WROTE FOUR OF THE FIVE OPINIONS ON THE DEFINITION OF “SECURITY.” HIS SUSTAINED EFFORT IN THIS AREA CONFINED THE SECURITIES LAW TO INSTRUMENTS THAT COMMONLY WOULD BE UNDERSTOOD AS INVESTMENTS.

POWELL’S EVOLUTION IN THIS AREA IS STRIKING. POWELL FOCUSED ON “ECONOMIC REALITY” TO REIN IN THE DEFINITION OF “SECURITY” IN UNITED HOUSING FOUNDATION V. FORMAN.289 THAT EMPHASIS CONFLICTED WITH POWELL’S GOAL OF PREDICTABILITY; LOOKING AT ECONOMIC REALITY SUGGESTED A CASE-BY-CASE ANALYSIS OF FINANCIAL INSTRUMENTS TO DETERMINE WHETHER THEY


286 Powell voted to grant certiorari in the Court’s case establishing the standard for materiality under Rule 10b-5. Docket Sheet, Basic Inc. v. Levinson, No. 86-279 (February 20, 1987). Somewhat surprisingly, the second issue in that case, the “fraud-on-the-market” presumption of reliance, went unremarked on by Powell. Reliance does not appear to have been an important issue for Powell. See Docket Sheet, John Nuveen & Co. v. Sanders, No. 80-299 (October 31, 1980) (noting that Powell would not grant certiorari on question “whether person who never saw prospectus could sue” under Section 12(2) because “Market may be affected.”).

287 Securities Act §2(a)(3); Exchange Act §3(a)(14).


WERE A SECURITY, A LESS THAN COMFORTING PROSPECT FOR CORPORATE LAWYERS ADVISING CLIENTS.

WHEN THAT UNPREDICTABILITY BECAME UNMANAGEABLE IN Landreth Timber and Gould, Powell pulled back from the full implications of “ECONOMIC REALITY.”

As Powell saw it, the transaction at issue in Forman had nothing to do with investment. The plaintiffs had purchased “stock” in a non-profit housing cooperative subsidized by the State of New York which allowed them to rent apartments in the cooperative.290 One senses in this passage Powell’s exasperation with the Second Circuit’s ongoing efforts to expand the securities laws:

In this case members of Co-op City have not bought stock or real estate for investment purposes but rather have purchased living quarters generously subsidized by the State of New York. Certainly there was no profit motive, as no rational person would purchase an apartment in this nonprofit housing co-op as an investment for profit. . . Nor can it even be suggested that the promoters of the cooperative, including the State of New York, sold shares in Co-op City as a means of raising venture capital for a profitmaking operation. Indeed, the promoter is a non-profit corporation. Nothing in the instant transaction partakes of the kind of investment traditionally found to be within the scope and purpose of the securities laws.291

The Second Circuit’s “novel” conclusion that this transaction involved a security ignored economic reality. “Novel” was not a favorable term when Powell was describing legal decisions.

The SEC predictably came in on the side of the plaintiffs, arguing for the broadest possible interpretation. This time, the agency was aided by literalism: “[T]he shares issued

2902nd Draft, United Housing Foundation, Inc. v. Forman, Nos. 74-157 and 74-647, at 1 (Powell, J., dissenting from the denial of certiorari) (Jan. 16, 1974).

291Id. at 4.
BY RIVERBAY CORPORATION ARE SECURITIES BECAUSE THEY ARE STOCK” AND “STOCK” IS SPECIFICALLY ENUMERATED IN THE EXCHANGE ACT’S DEFINITION OF SECURITY.²⁹² POWELL, HOWEVER, WAS NOT PERSUADED BY THIS STRAIGHTFORWARD TEXTUALIST ARGUMENT AND HE SELDOM WAS INCLINED TO DEFER TO THE SEC’S AGENCY EXPERTISE. THAT INCLINATION WAS BOLSTERED BY THE FACT THAT THE SEC HAD REVERSED ITS PRIOR POSITION.²⁹³ IN HIS VIEW, THE LABEL “STOCK” WAS MISAPPLIED TO THIS INSTRUMENT.

LOOKING THROUGH FORM TO SUBSTANCE BECAME THE CENTRAL THEME OF POWELL’S EVENTUAL OPINION FOR THE COURT. “BECAUSE SECURITIES TRANSACTIONS ARE ECONOMIC IN CHARACTER CONGRESS INTENDED THE APPLICATION OF THESE STATUTES TO TURN ON THE ECONOMIC REALITIES UNDERLYING A TRANSACTION, AND NOT ON THE NAME APPENDED THERETO.”²⁹⁴ THE ECONOMIC REALITIES REFLECTED EXPENDITURES ON HOUSING, NOT INVESTMENTS, AND LABELING THE PURCHASE “STOCK” COULD NOT CHANGE THAT FACT.

IT DOES NOT APPEAR THAT POWELL EVER CONSIDERED THE POSSIBILITY THAT THE LABEL “STOCK” COULD BE DISPOSITIVE. WHILE IT MIGHT HAVE BEEN THE WRONG RESULT IN THE CASE BEFORE THE COURT, A HOLDING THAT THE INSTRUMENT IN FORMAN WAS A SECURITY WOULD HAVE BEEN READILY AVOIDED IN THE FUTURE BY SIMPLY CHOOSING ANOTHER LABEL (SAY “HOUSING UNITS”). MORE IMPORTANTLY, IT WOULD HAVE MADE THE DEFINITION OF SECURITY CONSIDERABLY MORE PREDICTABLE. FOR POWELL, PERHAPS THE MESSAGE WAS AS IMPORTANT AS THE HOLDING. AS POWELL SAW IT,


Justice Powell and the Counter-Revolution

PRIVATE PLAINTIFFS AND THE SEC WERE ATTEMPTING TO PUSH THE SECURITIES LAWS INTO AREAS THAT CONGRESS HAD NEVER INTENDED THAT THEY REACH. HIS INSTINCT FOR PREDICTABILITY COULD NOT OVERCOME THAT VISCERAL REACTION.²⁹⁵

POWELL RETURNED THE DEFINITION OF SECURITY TO THE PATH OF PREDICTABILITY IN HIS LAST TWO OPINIONS IN THIS AREA, ALTHOUGH IT REQUIRED GOING AGAINST HIS STRONGEST INSTINCT.

²⁹⁵The Court decided one case on the definition of a security in which Powell did not write the opinion. Marine Bank v. Weaver, 455 U.S. 551 (1982), involved two instruments that potentially could be a security: (1) a certificate of deposit issued by a bank; and (2) a unique contract negotiated between two parties for an investment in a business. The second question particularly worried Powell: “If the agreement here – unique on its facts – is a ‘security,’ a vast number of business [contracts] will come under Act. (Sad case!)” Notes, 80-1562, Marine Bank v. Weaver, (1/8/82). Both instruments ultimately were held not to be securities, but the Chief Justice’s opinion for the Court further muddied the water on the definition of a security.

On the question of whether a CD is a security, Burger sensibly enough said no. Certificates of deposit are not among the enumerated categories in the definition of security. More importantly, the risk of holding the instrument is virtually eliminated by federal banking regulation and deposit insurance. Burger confused the matter, however, in responding to a concern raised by Stevens. Stevens urged that the Court’s holding not preclude later holdings that a CD is a security under the Investment Company Act (despite identical language in the definition) or that a CD might somehow become a security in secondary market trading, even though it was not one at the time of issue. Letter from John Paul Stevens to the Chief Justice, No. 80-1562 Marine Bank v. Weaver, (March 4, 1982). Despite the implausibility of these concerns (and not needing Stevens for a majority), Burger obliged: “It does not follow that a certificate of deposit or business arrangement between transacting parties invariably falls outside the definition of a security as defined by statute. Each transaction must be analyzed and evaluated on the basis of the content of the instrument in question, the purposes intended to be served and the factual setting as a whole.” Marine Bank v. Weaver, 455 U.S. 551, 560 n. 11 (1982). This caveat rendered the Court’s holding good for only one case—a CD could reemerge as a security in the next case, making it very difficult for lawyers to advise their clients on the status of the instrument.

Burger got further off track in addressing whether the privately negotiated investment was a security. He notes that the owners of business “distributed no prospectus to the [plaintiffs] or to other potential investors, and the unique agreement they negotiated was not designed to be traded publicly.” First Draft, Marine Bank v. Weaver, No. 80-1562, at 8 (March 1, 1982). Powell objected that these facts were “immaterial,” but he did not share his concerns with Burger. Id. at 1, 8. Powell presumably would have written a much cleaner opinion, focusing on the fact that the unique contract, tailored through the negotiations of the parties, was not within the realm that Congress had sought to regulate. Alternatively, the case might have been resolved on a lack of “horizontal commonality,” i.e., no “common enterprise” among investors. The Court did not take this tack, leaving the issue whether horizontal commonality is required to satisfy the “common enterprise” test unresolved. Instead, Burger’s loose approach raised the possibility that a variety of private placements of instruments commonly thought to be securities (e.g., preferred stock) might be outside the reach of the securities laws. See Marc I. Steinberg & William E. Kaulbach The Supreme Court And The Definition of Security: The ‘Context’ Clause, ‘Investment Contract’ Analysis, And Their Ramifications, 40 Vand. L. Rev. 489, 490 (1987) (“the Court’s analysis in Weaver has resulted in a great deal of uncertainty about the circumstances under which instruments clearly fitting within the statutory definition should be denied coverage and when other, more unusual, transactions similarly ought to be excluded.”). Unless, of course, the Court decided that they were securities based on the flabby caveat that Burger had included at Stevens’ urging.
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*Landreth Timber Co.* v. *Landreth*[^296] and its companion case, *Gould v. Ruefenacht*,[^297] involved the “sale of business” doctrine. Under that doctrine, the sale of an entire business, if achieved by the sale of 100% of a company’s stock (or perhaps just a majority), was outside the securities laws. The doctrine was at least questionable given the specific enumeration of stock in the definition of “security.” The lower courts, however, had held that common stock was not a security unless it also met the test for an “investment contract.”[^298] That test, set forth by the Supreme Court in *Sec v. W.J. Howe Co.*, required an expectation of profits from the efforts of others.[^299] A purchaser of 100% of a company’s stock typically could not satisfy this requirement because of the control conferred by majority ownership. The notion that the *Howey* test applied generally got support from Powell’s opinion in *Forman*, with its focus on “economic realities” and its observation that the *Howey* test “embodies the essential attributes that run through all of the Court’s decisions defining a security.”[^300]

Although this dicta hardly compelled the lower courts’ decisions, Powell’s instinct again was to cabin the federal securities laws (and their liability exposures) narrowly. The sale of an entire company, even if done through the sale of stock, typically

[^297]: The case was consolidated with, 471 U.S. 701 (1985), which raised the applicability of the sale of business doctrine to 50% of a company’s stock.
[^299]: 328 U.S. 293 (1946).
[^300]: 421 U.S. at 852-853.

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would be negotiated face-to-face. The potential buyer could demand those disclosures relevant to him and would be protected by state common law fraud. Powell had endorsed the “sale of business” doctrine a decade earlier in a draft concurrence in Scherk v. Alberto-Culver:

It is unnecessary to say that no acquisition of an entire business, where the method employed is transfer of stock, is ever converted [sic] by 10(b) of the Act. There may be situations where the substance or essence of the transaction is in fact the purchase and sale of securities. But certainly in a case where one large business interest is seeking to acquire the entire business of another large interest for the purpose of operating it, if [sic] blinks reality to say that a security’s [sic] transaction occurs within the language and intent of § 10(b). In this case Alberto-Culver’s purpose was to acquire these business entities - their assets and going concern value - Western Europe. Alberto-Culver desired to operate these businesses itself, and was free from the time of acquisition to convert them into such business forms as best suited its tax and business purposes. It is plain that Alberto-Culver had no interest in merely becoming a shareholder in Scherk’s enterprises. In short, the purchase here was not in any realistic sense a security’s [sic] transaction. It was the 100% acquisition of businesses by a strong, sophisticated purchaser fully capable of making all necessary investigations, and which indeed did make such investigations through American and European and [sic] accountants.

There is nothing in the history or language structures of the Securities Acts of 1933 and 1934 which remotely suggests an intent or purpose to apply to transactions such as this or to afford protection to parties such as Alberto-Culver.

Powell objected to bringing the federal securities laws into negotiations between sophisticated commercial parties. The “sale of business” doctrine provided the hook by which Powell could limit the reach of the securities laws. Powell chose not to publish his Alberto-Culver concurrence, however, apparently satisfied by Stewart’s specific

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RESERVATION OF THE QUESTION IN THE MAJORITY OPINION. So Powell was free to consider the question de novo.

At the certiorari stage in Landreth and Gould, Powell favored the “sale of business” doctrine, a view that he still held the next spring when he reviewed the case prior to argument:

As I had some familiarity with both of these statutes, I confess to a rather strong bias in favor of CA9’s position that one must look to the substance of the transaction, rather than rely solely to the term “stock”, to conclude that the anti-fraud provisions of these Acts apply. Although the SG struggles to distinguish my decision in United Housing Foundation v. Forman, I am not yet persuaded.

To all intense [sic] purposes, both of these transactions involved - in effect - the transfer of assets rather than securities in the normal sense of the term. This is more obvious where 100% of the business was bought than in the case where an individual purchased only 50% of the stock. But both cases involve types of transactions that I doubt anyone, at the times these statutes were enacted, would have believed were covered by any provisions of these two federal laws.

Powell nonetheless conceded that the Solicitor General made “strong arguments.”

Powell also wondered whether the doctrine should be applied to the sale of a smaller percentage of stock.

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303 Suggested note to be added to the opinion of the Court. No. 73-781 Scherk v. Alberto-Culver (Ifp) (6/6/74); 4th Draft, No. 73-781 Scherk v. Alberto-Culver Co., (Stewart, J.) (June 7, 1974) (Powell notes: “My suggested note 8 is included.”).

304 Powell wrote on the cert pool memo that he was “inclined to agree” with the Ninth Circuit’s application of the doctrine. Preliminary Memorandum, No. 83-1961, Landreth Timber Co. v. Landreth (September 24, 1984 Conference).


306 Id. at 3.

307 Id. at 4.
WRESTLING WITH THIS LAST QUESTION EVIDENTLY CHANGED POWELL’S MIND, WITH A PUSH FROM HIS LAW CLERK. POWELL’S CLERK, LYnda SIMPSON, NOTED IN HER BENCH MEMORANDUM TO POWELL THAT “THE DETERMINATION OF WHETHER STOCK IS A ‘SECURITY’ IN THESE CASES WILL DEPEND ON EXTENSIVE FACT-FINDING AS TO WHETHER CONTROL HAS PASSED AND HOW ACTIVE IN MANAGEMENT THE PURCHASER BECOMES, INQUIRIES THAT MAKE THE ‘SALE OF BUSINESS’ DOCTRINE MORE THAN A LITTLE ELUSIVE TO APPLY.”

Moreover, she noted in a supplemental memorandum, “IT DOESN’T MAKE MUCH SENSE TO ME THAT THE SAME STOCK IS OR IS NOT A ‘SECURITY’ DEPENDING ON HOW MUCH OF IT WAS SOLD OR WHO BOUGHT IT.” SIMPSON’S INVOCATION OF PREDICTABILITY RESONATED WITH POWELL’S PREFERENCE FOR CLEAR RULES: POWELL NOTED “LINDA [sic] MAY BE RIGHT.”

He wrote in his notes prepared before argument that he saw this lack of predictability as a “SERIOUS WEAKNESS” IN THE “SALE OF BUSINESS” DOCTRINE. By the time of conference, Powell voted with his colleagues in rejecting the doctrine, after first “EXPRESSING MY DOUBTS AT LENGTH.”

POWELL WAS ASSIGNED THE OPINIONS FOR A UNANIMOUS COURT. IN THE LANDRETH OPINION, HE LIMITED FORMAN’S “ECONOMIC REALITY” TEST TO THE DEFINITION OF “INVESTMENT CONTRACT.”

THE “INVESTMENT CONTRACT” TEST WOULD NOT BE ALLOWED TO SWALLOW SPECIFICALLY
Forced to choose between predictability of application and his aversion to expanding the scope of the securities laws, Powell opted for predictability: “Uncertainties attending the applicability of the Acts would hardly be in the best interests of either party to a transaction.” It helped that the expanded reach of the securities laws easily could be avoided — by structuring a transaction as an asset sale, a corporate lawyer could sidestep the securities laws. There is no evidence that grappling with the sale of business doctrine caused Powell to reconsider Forman’s focus on economic realities and the uncertainty that it had engendered.

Powell was afforded one final opportunity to contribute to the interpretation of “security.” After retiring from the Supreme Court, Powell sat by designation for a number of years on the Fourth Circuit. His opinion in Rivanna Trawlers v. Thompson Trawlers holds that a general partnership interest is not an “investment contract.” Powell was wary of turning partnership disputes into a federal case via the securities laws. The decision is notable for Powell’s rejection of the notion that “courts must examine [the] business acumen” of an investor found to be a general partner when deciding whether the partnership interest qualifies as an “investment contract.” Powell thought that “[u]nless a person is incompetent I have thought that a general partner is bound by the

315 Id. at 696.
318 Memo to Bob [Werner], No. 87-2516 Rivanna Trawlers v. Thompson Trawlers, et al., at 3 (1/18/88).
TERMS AND CONDITIONS OF THE PARTNERSHIP AGREEMENT. OTHERWISE, IT SEEMS TO ME THE LAW WOULD BE CHAOTIC.319 HERE, POWELL’S PENCHANT FOR PREDICTABILITY ALIGNED WITH HIS GOAL OF LIMITING THE SECURITIES LAWS.

PART FIVE: THE TAKEOVER WARS

POWELL’S EFFORTS TO CURTAIL THE EXPANSION OF THE FEDERAL SECURITIES LAW ARE SEEN MOST CLEARLY IN THE INTERSECTION WITH STATE CORPORATE LAW. THE SUPREMACY CLAUSE REQUIRES THAT STATE LAW MUST GIVE WAY WHEN FEDERAL AND STATE LAW CONFLICT, BUT JUDGES NONETHELESS HAVE SUBSTANTIAL LATITUDE IN INTERPRETING THE SCOPE OF FEDERAL LAW AND IDENTIFYING CONFLICTS. THE LONGSTANDING CLASH BETWEEN STATE CORPORATE LAW AND FEDERAL SECURITIES LAW WAS EXACERBATED DURING POWELL’S LAST YEARS ON THE COURT AS A WAVE OF HOSTILE TAKEOVERS REACHED ITS ZENITH. THE STATES WERE TAKING THE LEAD IN DISCOURAGING TAKEOVERS. THE SEC WAS IN THE OPPOSING CORNER, ATTEMPTING TO USE FEDERAL LAW TO HEAD OFF STATE EFFORTS TO RESTRICT THE MARKET FOR CORPORATE CONTROL.320 IN THIS DISPUTE, THE QUESTION WAS NOT WHETHER ONE WAS “FOR” OR “AGAINST” BUSINESS; HERE ONE WAS FORCED TO TAKE SIDES FOR OR AGAINST MANAGEMENT. POWELL WAS FIRMLY IN THE PRO-MANAGEMENT CAMP.

CONSIDER THE FOLLOWING PASSAGE FROM HIS CONCURRENCE IN EDGAR V. MITE:

THE CORPORATE HEADQUARTERS OF THE GREAT NATIONAL AND MULTI-NATIONAL CORPORATIONS TEND TO BE LOCATED IN THE LARGE CITIES OF A FEW STATES. WHEN CORPORATE HEADQUARTERS ARE TRANSFERRED OUT OF A CITY AND STATE INTO ONE OF THESE METROPOLITAN CENTERS, THE STATE AND LOCALITY FROM WHICH THE TRANSFER IS MADE INEVITABLY SUFFER SIGNIFICANTLY. MANAGEMENT PERSONNEL –

319 Id.

320 Telephone interview with Steve Lamb (May 30, 2002).
MANY OF WHOM HAVE PROVIDED COMMUNITY LEADERSHIP – MAY MOVE TO THE NEW CORPORATE HEADQUARTERS. CONTRIBUTIONS TO CULTURAL, CHARITABLE, AND EDUCATIONAL LIFE – BOTH IN TERMS OF LEADERSHIP AND FINANCIAL SUPPORT – ALSO TEND TO DIMINISH WHEN THERE IS A MOVE OF CORPORATE HEADQUARTERS.\footnote{Edgar v. Mite, 457 U.S. 624, 646 (1982) (Powell, J., concurring).}

**THIS DISCUSSION SMACKS OF SMALL-TOWN PROTECTIONISM, I.E., PRESERVING THE ABILITY OF STATES TO EXTRACT RENTS FROM CORPORATIONS IN EXCHANGE FOR THE PROTECTION OF INCUMBENT MANAGEMENT.**

**POWELL WOULD NOT HAVE LABELED HIMSELF A PROTECTIONIST, BUT SIMPLY A CONSERVATIVE ANXIOUS TO PRESERVE THE SORT OF BUSINESS COMMUNITY THAT HE HAD KNOWN. IN POWELL’S BUSINESS WORLD, BUSINESSMEN LIKE HARVIE WILKINSON (AND FOR THAT MATTER, POWELL HIMSELF) WERE ENGAGED IN BUILDING COMMUNITIES AS WELL AS BUSINESSES. THE CORPORATE BOTTOM LINE WAS RELEVANT, BUT IT WAS NOT THE ONLY GOAL. POWELL, HAVING SPENT SO MANY YEARS IN CORPORATE BOARDROOMS, PAID SCANT ATTENTION TO THE INTERESTS OF SHAREHOLDERS, NOTICEABLY ABSENT FROM HIS DISCUSSION HERE. ALSO ABSENT IS ANY ATTEMPT TO DEAL WITH THE CONSEQUENCES THAT THIS VIEW WOULD HAVE FOR THE GOAL OF PRESERVING A COMMON MARKET AMONG THE STATES, IF STATES ARE TO BE ALLOWED TO PROTECT THEIR LOCAL FAVORITES FROM TAKEOVER BY BIG CITY FIRMS. POWELL’S “CHAMBER OF COMMERCE” PERSPECTIVE ULTIMATELY PREVAILED IN THE SUPREME COURT.**

**A. VIRGINIA’S ANTI-TAKEOVER STATUTE**

**POWELL HAD A PERSONAL INTEREST IN STATE ANTI-TAKEOVER LAWS – HE HAD LOBBIED TO ENACT THE FIRST ONE. VIRGINIA WAS THE FIRST STATE (PREDATING EVEN THE FEDERAL WILLIAMS ACT) TO ADOPT AN ANTI-TAKEOVER STATUTE IN RESPONSE TO THE TENDER OFFER WAVE OF THE LATE**
1960s.\(^{322}\) Powell worried as that wave emerged that the existing regulatory void meant that a tender “offer may be sprung upon unwary management almost overnight.”\(^{323}\) Powell’s worries became more acute when one of the great conglomerates of the 1960s, Tenneco, targeted Newport News Shipbuilding for a takeover. Although Newport News was not a regular client, the company came to Powell when it needed legislation to ward off Tenneco.

Powell’s connections helped: he was a longtime supporter of Edward Lane, who sponsored the legislation.\(^{324}\) Lane introduced a bill that would apply to offers for more than 10% of a company’s shares for companies that were both incorporated and doing business in Virginia. Based on a mark-up of a predecessor bill of the Williams Act,\(^{325}\) the bill’s provisions track the federal law.\(^{326}\) Powell lobbied for the bill on behalf of Newport News, meeting with Virginia’s Attorney General (whom Powell had supported

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\(^{324}\)Letter from Lewis F. Powell, Jr. to Edward E. Lane (July 28, 1953) (congratulating Lane on his election); Letter from Lewis F. Powell, Jr. to Edward E. Lane (May 13, 1957) (pledging support “in the coming election, as I always have in the past”); Letter from Lewis F. Powell, Jr. to F. Carlyle Tiller (June 21, 1957) (forwarding “checks for Ed Lane” from Powell and two of his partners); Letter from Lewis F. Powell, Jr. to Edward E. Lane (November 10, 1965) (congratulating Lane on his reelection).


\(^{326}\)The Virginia statute includes a specified period for the offering, a requirement that offerors take up shares from over-subscribed offers pro rata, a series of disclosure requirements, an anti-fraud provision, and both criminal and civil liability provisions (including a private right of action). The act was later amended in 1980 to reach so-called “creeping tender offers,” i.e., large-scale open-market purchases. The Fourth Circuit struck down the amendment as imposing an undue burden on interstate commerce. Telvest, Inc. v. Bradshaw, 697 F.2d 576 (1983). A successor statute was upheld by the Fourth Circuit on the basis of Powell’s opinion in CTS. WLR Foods, Inc. v. Tyson Foods, Inc., 65 F.3d 1172 (4th Cir. 1995).
IN HIS ELECTION CAMPAIGN)³²⁷ AND APPEARING BEFORE BOTH HOUSE AND SENATE COMMITTEES OF THE GENERAL ASSEMBLY.³²⁸ A MEMBER OF POWELL’S “TEAM,” JOE CARTER, WAS SENT TO “POUND[] THE HALLS OF THE GENERAL ASSEMBLY WITH COOTIE HOLT [NEWPORT’S GENERAL COUNSEL] BEGGING OUR FRIENDS TO SAVE NEWPORT NEWS SHIP FROM BEING TAKEN OVER.”³²⁹


B. THE WILLIAMS ACT


³²⁸Billing Records, 1/22/68 to 2/29/68.

³²⁹Letter from Joseph C. Carter to Lewis F. Powell, Jr. (April 22, 1981); Telephone Interview with Joe Carter (May 21, 2002).

³³⁰Note to Joe Carter from Lewis F. Powell, Jr. (April 18, 1981) (“As I recall, you and I drafted the Virginia statute for Newport News Shipbuilding Company, and then the company backed down on using it against Tenneco. We “lobbied” it through the legislature, and persuaded Mills Godwin to sign it.”); Letter from Lewis Powell, Jr. to Hon. Mills E Godwin (November 10, 1965) (congratulating Godwin on his election).

³³¹Letter from Lewis F. Powell, Jr. to Hon. Edward E. Lane (March 9, 1968). See also Letter from Lewis F. Powell, Jr. to Mills E. Godwin, Jr. (March 9, 1968) (thanking Godwin for his “full support” of the legislation).


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The federal Williams Act, adopted shortly after the Virginia statute in 1968,\textsuperscript{334} first made its way to the Supreme Court in 1975.\textsuperscript{335} Rondeau v. Mosinee Paper Company raised the question of remedies under the Act. Rondeau acquired more than 5% of Mosinee Paper’s shares, but unwittingly failed to file the notices required by the “early warning” provision of the Act.\textsuperscript{336} Although Rondeau subsequently filed the required notices, the company filed suit and Seventh Circuit barred Rondeau for five years from voting the shares he acquired after the filing date.\textsuperscript{337}

Powell thought the injunction was “an absurd penalty, where there was no showing of prejudice or injury to [Mosinee].”\textsuperscript{338} Powell knew the potential mischief that could result from putting a weapon of this sort into the hands of management: “Suits by Mgt. (like this) are a standard tactic to frustrate tender offers.”\textsuperscript{339} Despite Powell’s uneasiness with tender offers, he was not prepared to discard the equitable rule requiring a showing of irreparable harm for an injunction.\textsuperscript{340} At conference, only Brennan disagreed, and he offered no justification for his position. The Court voted to reverse seven to one (Douglas was absent).\textsuperscript{341}


\textsuperscript{335}Rondeau v. Mosinee Paper Corp., 422 U.S. 49 (1975).

\textsuperscript{336}Id. at 51-53.

\textsuperscript{337}500 F.2d 1011, 1017.

\textsuperscript{338}Preliminary Memorandum, No. 74-415, Rondeau v. Mosinee Paper Co. (December 6, 1974 Conference).

\textsuperscript{339}Argument Notes, 74-415 Rondeau v. Mosinee Paper Corp., (Aruged [sic] 4/15/75).

\textsuperscript{340}Conference Notes, 74-415 Rondeau v. Mosinee (Conf. 4/18/75).

\textsuperscript{341}Id. Marshall later switched his vote, dissenting without opinion. 422 U.S. at 65.
BURGER’S OPINION FOR THE COURT IS A STRAIGHTFORWARD APPLICATION OF WELL-SETTLED PRINCIPLES OF EQUITY, NOTABLE ONLY FOR ITS READING OF THE LEGISLATIVE HISTORY OF THE WILLIAMS ACT, WHICH:

EXPRESSLY DISCLAIMED AN INTENTION TO PROVIDE A WEAPON FOR MANAGEMENT TO DISCOURAGE TAKEOVERS BIDS OR PREVENT LARGE ACCUMULATIONS OF STOCK WHICH WOULD CREATE THE POTENTIAL FOR SUCH ATTEMPTS. INDEED, THE ACT’S DRAFTSMEN COMMENTED UPON THE ‘EXTREME CARE’ WHICH WAS TAKEN ‘TO AVOID TIPPING THE BALANCE OF REGULATION EITHER IN FAVOR OF MANAGEMENT OR IN FAVOR OF THE PERSON MAKING THE TAKEOVER BID.‘

THIS PASSAGE DID TWO SIGNIFICANT THINGS: (1) IT TRANSFORMED RATHER TRANSPARENT DENIALS BY CONGRESS OF ITS INTENT TO DISCOURAGE HOSTILE TAKEOVERS INTO THE GOVERNING RATIONALE OF THE WILLIAMS ACT; AND (2) IT LAID THE GROUNDWORK FOR THE PREEMPTION ARGUMENTS THAT THE COURT WOULD LATER ADDRESS AND FINALLY REJECT IN CTS. NONE OF THE JUSTICES – INCLUDING POWELL, WHO WAS WELL-AWARE OF THE ANTI-TAKEOVER PURPOSE OF LEGISLATION OF THIS SORT – COMMENTED UPON THE PASSAGE AT THE TIME.

THE COURT INTERPRETED THE WILLIAMS ACT NARROWLY AGAIN IN PIPER v. CHRIS-CRAFT INDUSTRIES, HOLDING THAT THE ACT DID NOT PROVIDE A CAUSE OF ACTION FOR DAMAGES TO A DEFEATED BIDDER IN A TAKEOVER. POWELL URGED BURGER TO “IMPly NO VIEW AS TO LIABILITY” IN HIS OPINION FOR THE COURT BECAUSE IF IT:

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343 See text at infra notes .
344 Powell’s only suggestion was that the question of whether equitable relief would be available in the face of an ongoing violation should be reserved, Letter from Lewis F. Powell, Jr. to the Chief Justice, No. 74-415 Rondeau v. Mosinee Paper Corp. (June 5, 1975), which was adopted. Memorandum to the Conference from the Chief Justice, Re: 74-415 - Rondeau v. Mosinee Paper Corp (June 5, 1975).
345 30 U.S. 1 (1977). Piper is discussed in the section on private rights of action. See text at supra notes .
C. Preemption

Rondeau and Piper set the stage for a trilogy of cases addressing whether the Williams Act preempted state take anti-takeover laws and the constitutionality of those state laws under the Dormant Commerce Clause. In the first, Leroy v. Great Western United Corporation, Great Western had made an unsolicited tender offer to the shareholders of Sunshine Mining Company, a Washington corporation with its principal mining operations in Idaho. The Fifth Circuit had upheld an injunction by a Texas district court barring the director of Idaho’s Department of Finance from

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346 Letter to the Chief Justice from Lewis F. Powell, Jr., Nos. 75-353, 75-354, and 75-355 (The Bangor Punta Cases) (December 30, 1976).

347 Id.


349 Preliminary Memorandum, No. 78-759, Kidwell v. Great Western United Corp, at 1-3 (12/18/78).
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Enforcing Idaho’s antitakeover statute against Great Western. The Idaho statute added further delay and disclosure requirements beyond those imposed by the Williams Act. In addition, it required the approval of tender offers by state regulators.\(^350\) The Fifth Circuit concluded that the Idaho statute placed an undue burden on interstate commerce, thus violating the Dormant Commerce Clause, and in addition frustrated the purposes of the Williams Act, and therefore was preempted.\(^351\)

Powell conceded that “the potential availability of tender offers is valuable to shareholders in almost all corporations as an incentive to efficient management,” but he worried that “the Williams Act is a weak statute that does not adequately protect shareholders of target co.”\(^352\) Despite his sympathies for the purposes of Idaho’s law, Powell thought that it “may have gone too far, especially by not limiting its Act to Idaho corps and in requiring approval by Idaho Commission.”\(^353\)

If the Court were to get to the merits, at least eight justices thought the Idaho statute should be struck down, although they disagreed on the rationale. A majority, however, believed that the Texas district court lacked jurisdiction.\(^354\) Stevens was


\(^351\)577 F.2d 1256 (1978).


\(^353\)Id. at 1 (Powell’s marginal notes).

\(^354\)White, along with Brennan and Marshall, wanted to affirm the Fifth Circuit’s decision. The Chief Justice, along with Rehnquist, agreed that the statute ran afoot of the Dormant Commerce Clause as well as the Williams Act. Stewart favored only preemption and Blackmun thought it only unconstitutional. None of these four, however, thought that the Texas district court had jurisdiction over the Idaho securities regulator, either under the Texas long arm statute or the jurisdictional provision of the Exchange Act. Powell thought that the Texas long-arm statute, but not the Exchange Act, conferred jurisdiction. The assertion of jurisdiction on these facts, however, would violate the Due Process Clause. He did not offer a view on the merits. Finally, Stevens was uncertain on jurisdiction, but felt that the case could be reversed.
ASSIGNED THE OPINION, WHICH HE WROTE REVERSING THE FIFTH CIRCUIT’S RULING THAT VENUE WAS PROPER IN THE TEXAS DISTRICT COURT. DESPITE STEVENS’ FREELANCING, HE GOT A MAJORITY, PERHAPS BECAUSE NONE OF THE OTHER JUSTICES WANTED TO TACKLE THE THORNY JURISDICTIONAL ISSUES.\textsuperscript{355} WHITE, JOINED BY BRENNAN AND MARSHALL, DISSENTED, BUT HE DID NOT ADDRESS THE MERITS OF GREAT WESTERN’S CLAIM.\textsuperscript{356} THE CONSTITUTIONAL STATUS OF STATE ANTI-TAKEOVER PROVISIONS REMAINED AT SEA.

The opportunity for clarification arose soon enough, but once again the justices were badly splintered. \textit{EDGAR v. MITE}\textsuperscript{357} presented a constitutional challenge to ILLINOIS’ ANTI-TAKEOVER STATUTE, which like the IDAHO STATUTE, applied to corporations that operated in ILLINOIS, whether or not they were incorporated under ILLINOIS LAW. An additional similarity to the IDAHO STATUTE was found in the ILLINOIS PROVISION’S REQUIREMENT THAT A STATE REGULATOR APPROVE TENDER OFFERS. The other similarity to GREAT WESTERN was a procedural complication – the potential acquiror had dropped its offer by the time the case reached the Court. At first glance, the case looked moot. Moreover, the SEC recently had adopted rules which would preempt statutes of this sort.\textsuperscript{358}


\textsuperscript{356}443 U.S. at 187.

\textsuperscript{357}457 U.S. 624 (1982).

\textsuperscript{358}Preliminary Memorandum, No. 80-1188, Edgar v. MITE Corp., at 6-7 (May 1, 1981 Conference).

The SEC’s rule that preempted the first generation of state antitakeover laws with its Rule 14d-2(b), which had the effect of preempting the first generation of state antitakeover laws. This rule was referred to at the SEC as the “kneecap” rule because Chairman Harold Williams had instructed John Huber to cut the state statutes off at the kneecap. Telephone Interview with Steve Lamb, May 30, 2002. \textit{MITE} provided substantial authority for upholding the rule. National City Lines, Inc. v. LLC Corp., 687 F.2d 1122 (8th Cir. 1982).
JUSTICES NONETHELESS DECIDED TO NOTE PROBABLE JURISDICTION. HAVING NOTED JURISDICTION, HOWEVER, A MAJORITY VOTED FOR MOOTNESS, AND MARSHALL WAS ASSIGNED TO WRITE THE OPINION. POWELL WENT ALONG WITH THE MAJORITY ALTHOUGH HE EXPRESSED THE OPINION THAT HE THOUGHT – “[I]F WE REACH MERITS” – THE STATUTE WAS PREEMPTED.\(^{359}\)

O\(N\)LY AFTER MARSHALL CIRCULATED HIS DRAFT DID THINGS BEGIN TO GO OFF TRACK.\(^{360}\) A SERIES OF SHIFTS AMONG THE JUSTICES RESULTED IN A MAJORITY FAVORING MOOTNESS BECOMING A MAJORITY STRIKING DOWN THE ILLINOIS LAW UNDER THE DORMANT COMMERCE CLAUSE.\(^{361}\) WHITE MUSTERED ONLY A PLURALITY OF THREE, HOWEVER, FOR HIS OPINION THAT THE LAW WAS ALSO PREEMPTED BY THE WILLIAMS ACT. THREE JUSTICES WHO HAD THOUGHT THAT THE IDAHO STATUTE WAS PREEMPTED IN G\(R\)\(E\)\(A\)\(T\) W\(E\)\(S\)T\(E\)N\(D\) (BRENNAN, MARSHALL AND REHNQUIST) DID NOT REGISTER THEIR VOTES ON THE MERITS IN MITE (THEIR VIEWS APPEAR TO HAVE BEEN THE SAME) BECAUSE THEY VIEWED THE CASE AS MOOT.\(^{362}\) FOCUSED ON THE PROCEDURAL ISSUE, THEY APPEAR TO HAVE IGNORED THE CASE’S IMPLICATIONS FOR SUBSTANTIVE REGULATION.

\(^{359}\)Conference Notes, No. 80-1188, Edgar v. Mite Corp. (Conf. 12/2/81).


\(^{361}\)At the end of it all, Marshall circulated the following summary of the maneuvering:


Memorandum to the Conference from Thurgood Marshall, No. 80-1188, Edgar v. Mite (June 18, 1982).

\(^{362}\)Conference Notes of William J. Brennan, Jr., No. 80-1188, Edgar v. MITE Corp.
Powell also believed that the case was moot and had endorsed preemption at conference. Despite his belief that the case was moot, he had intended to join White’s opinion when it was first circulated. He switched course, however, and provided the fifth vote striking down the law under the Dormant Commerce Clause. The result was to preserve more room for state anti-takeover legislation. Powell noted with interest that the “Virginia Act (that I helped write and lobbied through Va Legislature) has been followed – in substance – in 36 states.” Powell’s efforts preserved that legacy. Powell declined to join White’s holdings that the statute was preempted by the Williams Act and unconstitutional under the Dormant Commerce Clause because it directly regulated interstate commerce occurring wholly outside Illinois in the shares of public companies. Powell joined only White’s more limited holding that the Illinois statute imposed an undue burden on interstate commerce relative to the state interests. Powell joined this reasoning because it:

363 Conference Notes of Lewis F. Powell, Jr., No. 80-1188, Edgar v. MITE Corp. (12/2/81); 1st Draft, No. 80-1188, Edgar v. Mite Corporation (White, J.) (28 May 1982) (“Though I am not persuaded on “mootness” issue, if BRW gets a court I’ll join it.”). Powell switched in spite of the recommendation of his law clerk, John Wiley, who argued that the preemption analysis was the narrowest basis on which to decide the case because it “applies only tender offer laws, and could have no possible application to state blue sky statutes. In addition, I agree with the numerous commentators on this point that Congress sought to preserve a neutrality with which state takeover laws -- although completely well intentioned and perhaps of superior wisdom -- do undoubtedly interfere. This interference is plain from the frequency with which target companies resort to state statute protection.” Memorandum to Justice Powell, Re: Edgar v. Mite, at 2 (06/16/82). Wiley declined to discuss the case with me. My speculation, to some extent confirmed by Powell’s concurrence and subsequent opinion in CTS, is that Powell preferred the Commerce Clause basis because he was more concerned with preserving some room for state antitakeover laws than he was with blue sky law. In any event, state blue sky laws have now been largely preempted by Congress, while state antitakeover provisions have been left untouched.

364 1st Draft, NO. 80-1188, Edgar v. MITE Corp., at 1 (28 May 1982). Powell had considered at the certiorari stage whether his role in drafting the Virginia statute required recusal and had concluded that it did not. Preliminary Memorandum, Edgar v. MITE Corp., May 1, 1981 Conference (“I wrote Va Act - I think it was the first state law - but I’ll not disqualify.”).

LEAVES SOME ROOM FOR STATE REGULATION OF TENDER OFFERS. IN A PERIOD IN OUR HISTORY MARKED BY CONGLOMERATE CORPORATE FORMATIONS ESSENTIALLY UNRESTRICTED BY THE ANTITRUST LAWS, IT IS FAR FROM CLEAR TO ME THAT THE WILLIAMS ACT’S POLICY OF “NEUTRALITY” OPERATES FAIRLY OR IN THE PUBLIC INTEREST. OFTEN THE OFFEROR POSSESSES RESOURCES, IN TERMS OF PROFESSIONAL PERSONNEL EXPERIENCE IN TAKEOVERS AS WELL AS OF CAPITAL, THAT VASTLY EXCEED THOSE OF THE TAKEOVER TARGET. THIS DISPARITY IN RESOURCES MAY SERIOUSLY DISADVANTAGE A RELATIVELY SMALL OR REGIONAL TARGET CORPORATION. THE WILLIAMS ACT PROVISIONS SEEM TO ASSUME CORPORATE ENTITIES OF SUBSTANTIAL EQUAL RESOURCES. MOREOVER, IN TERMS OF GENERAL PUBLIC INTEREST, WHEN CORPORATE HEADQUARTERS ARE MOVED AWAY FROM A CITY AND STATE INEVITABLY THERE ARE CERTAIN ADVERSE CONSEQUENCES. I THEREFORE AGREE WITH JUSTICE STEVENS THAT THE WILLIAMS ACT SHOULD NOT NECESSARILY BE READ AS PROHIBITING STATE LEGISLATION DESIGNED TO ASSURE — AT LEAST IN SOME CIRCUMSTANCES — GREATER PROTECTION TO INTERESTS THAT INCLUDE BUT OFTEN ARE BROADER THAN THOSE OF INCUMBENT MANAGEMENT.366

THE CRITICISM OF THE WILLIAMS ACT DID NOT MAKE IT INTO PRINT, BUT NOT BECAUSE POWELL HAD DOUBTS ABOUT THE SUBSTANCE. HE NOTED IN A SUBSEQUENT CASE THAT, “I THINK THE WILLIAMS ACT HAS BEEN A DISASTER AS IT ENCOURAGES GIANT CORPS. TO ‘TAKE OVER’ SMALLER CORPS.”367 POWELL HERE EQUATES CONGRESS’S GRUDGING TOLERANCE OF TENDER OFFERS IN THE WILLIAMS ACT WITH ENCOURAGEMENT, A READING DIFFICULT TO SQUARE WITH THE LEGISLATIVE HISTORY.368 PERHAPS THIS


Justice Stevens objection to White’s preemption argument was more substantial:

I agree with you that when Congress enacted the Williams Act, it took extreme care to avoid tipping the scales of either in favor or management or in favor of possible takeovers. However, it seems to me that there is a significant difference between adopting such a policy of neutrality with respect to federal legislation that Congress was enacting, and requiring states to follow the same policy. As of now, I am not persuaded that Congress intended to prevent the states from loading the scales one way or the other. You are, of course, dead right in your analysis of the Illinois statute as being loaded in favor of management.

Letter from John Paul Stevens to Justice White, 80-1188 - Edgar v. Mite Corporation (June 1, 1982). O’Connor thought that the “Williams Act did not preempt the state law because Congress had not expressed such an intent.” Letter from
was a plausible reading in a context in which the SEC was relying on the Williams Act to preserve the market for corporate control (or at least a market controlled by the SEC, not the states).

Powell got his chance to preserve some space for state protection of local corporations five years later. States had gone back to the drawing board after the twin setbacks in MITE and the SEC’s adoption of its preemptive rules. Indiana’s effort was typical of the second generation of antitakeover statutes. It required a potential acquirer (defined as anyone acquiring certain threshold percentages of the company’s shares), to obtain the approval of a company’s “disinterested” shares (defined as shares not owned by the acquirer or management) before it would be allowed vote its own shares.369 Thus, a hostile tender offeror would be precluded from using its voting power to remove incumbent management without the approval of the company’s independent shareholders. The Indiana statute was more narrowly cast than the Illinois statute struck down in MITE. The Illinois statute applied to corporations with their principal executive offices and requisite number of shareholders in Illinois.370 The Indiana statute was limited to corporations organized under the law of Indiana, with their principal place of business in Indiana, and a substantial shareholder presence in Indiana.371 It also

Sandra Day O’Connor to Justice White, 80-1188 Edgar v. Mite Corporation (April 23, 1982).


371 CTS, 481 U.S. at 73.
LACKED THE REQUIREMENT THAT THE OFFER BE APPROVED BY A STATE REGULATOR, WHICH HAD PROVED PROBLEMATIC IN MITE AND HAD BEEN PREEMPTED BY THE SEC.\footnote{MITE, 457 U.S. at 639-640.}

THE SEVENTH CIRCUIT RELIED ON MITE TO INVALIDATE THE INDIANA STATUTE ON BOTH COMMERCE CLAUSE AND PREEMPTION GROUNDS.\footnote{794 F.2d 250 (1986).} NEEDLESS TO SAY, POWELL STRONGLY DISAGREED WITH SEVENTH CIRCUIT JUDGE RICHARD POSNER’S ENTHUSIASM FOR THE ECONOMIC BENEFITS OF TENDER OFFERS.\footnote{Bench Memorandum from Ronald [Mann] to Justice Powell, Nos. 86-71, CTS v. Dynamics Corp.; -97, Indiana v. Dynamics Corp., at 5 (February 11, 1987) (Powell responding to citation to Posner’s view that “tender offers are uniformly good for the economy” with a resounding “NO!”).} POWELL SAW THE CASE AS AN OPPORTUNITY TO CUT BACK ON MITE’S PREEMPTIVE REACH, BUT HE WAS PESSIMISTIC ABOUT HIS CHANCES OF SUCCESS. HE WAS PLEASANTLY SURPRISED WHEN THE VOTES WERE THERE TO NOTE PROBABLE JURISDICTION RATHER THAN AFFIRM,\footnote{Preliminary Memorandum, No. 86-79, Indiana v. Dynamics Corp. of America, (September 29, 1986 Conference) (Powell’s marginal notes) (“If other Justices show any interest I could Note this case, but I expect this will be affirmed.”).} BUT HE STILL DOUBTED THAT HE COULD SWING A MAJORITY ON THE MERITS. POWELL REMAINED ANXIOUS TO CURB THE TAKEOVER WAVE THAT SEEMED TO BE SWEEPING THE NATION: “I STILL ADHERE TO MY VIEW THAT THE WILLIAMS ACT HAS BECOME AN ECONOMIC DISASTER — A VIEW THAT INCREASINGLY IS BEING HELD BY RESPONSIBLE ECONOMISTS. INDEED HEARINGS ARE NOW PENDING IN THE CONGRESS TO CONSIDER APPROPRIATE MEANS OF CURBING TAKEOVER BIDS, AND THE BYPASSING IN EFFECT OF ANTITRUST LAWS.”\footnote{Memo To File, 86-71 CTS v. Dynamics Corp.; 86-97 Indiana v. Dynamics Corporation (CA7), at 1 (February 6, 1987).} JUSTICE WHITE’S OPINION IN MITE, HOWEVER, LOOMED AS A SUBSTANTIAL OBSTACLE TO PERMITTING A MORE MERCANTILIST ECONOMIC VIEW:

\footnote{MITE, 457 U.S. at 639-640.}

\footnote{794 F.2d 250 (1986).}

\footnote{Bench Memorandum from Ronald [Mann] to Justice Powell, Nos. 86-71, CTS v. Dynamics Corp.; -97, Indiana v. Dynamics Corp., at 5 (February 11, 1987) (Powell responding to citation to Posner’s view that “tender offers are uniformly good for the economy” with a resounding “NO!”).}

\footnote{Preliminary Memorandum, No. 86-79, Indiana v. Dynamics Corp. of America, (September 29, 1986 Conference) (Powell’s marginal notes) (“If other Justices show any interest I could Note this case, but I expect this will be affirmed.”).}

\footnote{Memo To File, 86-71 CTS v. Dynamics Corp.; 86-97 Indiana v. Dynamics Corporation (CA7), at 1 (February 6, 1987).}
Justice Powell and the Counter-Revolution

My brief concurring opinion in *MITE* summarizes my basic objections to the *Williams Act* and particularly the way it has been applied so expansively. But *MITE* is “the law”, and I would find it difficult to sustain the complex *Indiana Statute* in light of the reasoning of the Court’s opinion in *MITE*. If my law clerk has any ideas in this respect, they would be more than a little welcomed!377

Powell now regretted his vote to give White a majority in *MITE*, but he nonetheless considered it controlling.378 Powell needed a way around *MITE* to save the “beneficial” *Indiana Statute*.379

Powell’s clerk found a path out in the internal affairs doctrine. The Court had traditionally deferred to state regulation of corporations established under their laws. Should this deference extend to interstate transactions in shares created under that authority? Powell’s clerk identified the “internal affairs” doctrine as the critical issue:

If you think state corporate governance should be limited strictly to laws that affect the attributes of shares and transactions by the corporation itself, you will find that *Indiana* has overstepped its bounds. On the other hand, if you think states legitimately can act to protect shareholders from being coerced in ways that affect major corporate changes, you will find the law satisfactory.380

The internal affairs doctrine would allow Powell to protect management from the threat of takeover.

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379Notes 2/15, 86-71 *CTS v. Dynamics Corp.*; 86-97 *Ind. v. Dynamics Corp.*.

POWELL FOUND HIMSELF WITH SOME UNEXPECTED ALLIES AT CONFERENCE — BRENNAN, MARSHALL AND REHNQUIST, WHO HAD THOUGHT THE IDAHO AND ILLINOIS STATUTES WERE PREEMPTED BY THE WILLIAMS ACT, SAW NO CONFLICT BETWEEN THE INDIANA STATUTES AND THAT LAW. NOR DID THEY SEE A PROBLEM UNDER THE DORMANT COMMERCE CLAUSE. MOREOVER, SCALIA WHO HAD TAKEN BURGER’S SEAT,381 SAW NO PREEMPTION ISSUE AND TOOK A MUCH NARROWER VIEW OF THE REACH OF THE DORMANT COMMERCE CLAUSE. O’CONNOR SHARED POWELL’S FEDERALIST STREAK.382 THE RESULT WAS A 6-3 MAJORITY TO UPHOLD THE INDIANA STATUTE, WITH REHNQUIST GIVING POWELL THE ASSIGNMENT.

POWELL SAW THE BALANCING OF STATE INTERESTS AGAINST THE BURDEN ON INTERSTATE COMMERCE AS RELATIVELY STRAIGHTFORWARD. IN HIS VIEW, THE INDIANA “REGULATIONS . . . WILL BE RELATIVELY EASE [SIC] FOR TENDER OFFERING CORPORATIONS TO COMPLY WITH IF THEIR OFFERS ARE AGRAUABLY [SIC] BENEFICIAL TO THE INDIANA CORPORATION AND ITS SHAREHOLDERS. IT IS NOT EASY TO SEE ANY “BURDEN” OTHER THAN POSSIBLE DELAY IN BRINGING A TENDER OFFER TO FRUITION – HARDLY A SIGNIFICANT BURDEN ON A REASONABLE AND BENEFICIAL TENDER PROPOSAL.”383 POWELL IGNORES HERE THE SIGNIFICANT COSTS THAT DELAY CAN IMPOSE ON AN OFFEROR, BOTH IN TERMS OF FINANCING AND TIME FOR TARGET MANAGEMENT TO OBSTRUCT BIDS OR SEEK OUT A “WHITE KNIGHT.”384

381 More precisely, Rehnquist succeeded Burger and Scalia was confirmed as Rehnquist’s replacement.


384 Powell, of course, was aware of the strategic advantages afforded management by delay. In MITE, his law clerk had written that “forcing delay is a known weapon in tender offer battles.” Bench Memorandum from John Wiley to Mr. Justice Powell, No. 80-1188: Edgar v. Mite Corp. et al., at 9 (November 25, 1981). Powell’s response? “Of course – but ‘tender offers’ are not inevitably good.” Id.
These risks increase substantially if a tender offer must be held open for fifty days, rather than the twenty required by the Williams Act. The draft opinion asserted that:

If a majority of the target company’s shareholders think the offer is attractive, it is likely that a majority will tender their shares on the twentieth business day, and that a majority of the target company’s shareholders will vote to accord voting rights to the offeror so that the transaction can be consummated. Once the shares are tendered, the opportunities for incumbent management to defeat the tender offer by lobbying its own shareholders are greatly reduced.385

At best this is speculation, at worst it is implausible. Why would a shareholder tender at the earliest point, rather than waiting to see if a better offer emerged while the vote was pending? An offeror would certainly take into account the risk of losing its target in determining whether to launch a bid at all. Powell’s corporate law experience, grounded in the more leisurely dealmaking pace of the 1950s and 1960s (the Ethyl deal, managed under stringent deadlines, nonetheless took nearly three months to close),386 was badly out of date in the junk-bond fueled 1980s. This passage was cut before circulation to the other justices.

Another discarded passage provides further evidence of the dated nature of Powell’s understanding of the takeover market:

It may well be that a successful tender offer will result in more effective management or may have such other benefits as providing needed diversification. Yet, we know of no convincing evidence that the type of conglomerates that may result from repetitive take over offers are in fact

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385 No. 86-71, CTS Corporation v. Dynamics Corporation, at 28 n.7 (March 19, 1987 draft).

MORE EFFICIENT OR THAT THE OWNERS OF SHARES IN THE RESULTING CONGLOMERATE ARE BENEFITED [SIC].

POWELL IS RESPONDING TO THE 1960S TAKEOVERS WAVE, IN WHICH UNRELATED BUSINESSES WERE COMBINED INTO DIVERSIFIED CONGLOMERATES. HE WAS RIGHTLY SKEPTICAL THAT SHAREHOLDERS WOULD BENEFIT FROM THESE TRANSACTIONS. THE TAKEOVERS OF THE 1980S, HOWEVER, WERE DRIVEN BY EFFICIENCY GAINS FROM BREAKING UP THESE CONGLOMERATES, AND THE EVIDENCE THAT SHAREHOLDERS BENEFITTED FROM THIS PROCESS IS SIMPLY OVERWHELMING. THE NOTE WAS TONED DOWN IN THE FINAL OPINION.

POWELL WAS ON STRONGER GROUND IN EMPHASIZING THE ANALOGY BETWEEN INDIANA’S VOTING PROCEDURE FOR TENDER OFFERS AND SHAREHOLDERS VOTES REQUIRED BY STATE CORPORATE LAW FOR Mergers OR ASSET SALES. VOTING REQUIREMENTS ARE A TRADITIONAL MEANS TO PROTECT SHAREHOLDERS FROM EXPROPRIATION. TO BE SURE, THE CONTEXTS IN WHICH SHAREHOLDER VOTES ARE REQUIRED HAVE THE RISK OF UNFAIR VALUATION BECAUSE THEY GENERALLY LACK THE MARKET TEST BY WHICH TENDER OFFERS ARE JUDGED, BUT THE ANALOGY IS AT LEAST PLAUSIBLE. EXPROPRIATION IS A RISK ONLY WITH “TWO-TIER” TENDER OFFERS, IN WHICH A LOWER BACK END PRICE MAY INDUCE SHAREHOLDERS TO TENDER AT THE FRONT END EVEN IF THEY DEEM THE OFFERED CONSIDERATION INADEQUATE. POWELL RECOGNIZED “THAT THE PERCENTAGE THAT REALLY ARE COERCIVE IS RELATIVELY SMALL.” THE OPINION CLOAKS THE WEAKNESS OF THIS POINT IN DEFERENCE

387 Rider A, p. 43 (CTS Corp.), at 2 n.* (3/20/87).
388 Rider A, p. 21 (CTS Corp.) (03/27/86).
389 Memorandum from Lewis F. Powell, Jr. to Ronald [Mann], 86-71 CTS v. Dynamics Corp.; 86-97 Indiana v. Dynamics Corp., at 4 (March 18, 1987) (pointing out that “Virginia required, as did many other states, a two-thirds vote on a merger. In addition, the state prescribes the requisite vote on a sale of corporate assets and a liquidation.”).
390 Memorandum from Lewis F. Powell, Jr. to Ronald [Mann], 86-71 CTS Corp. v. Dynamics, at 2 (March 20, 1987).
TO THE “EMPIRICAL JUDGMENTS OF LAWMAKERS.” Nonetheless, distinguishing permissible uses of shareholder voting from impermissible uses would have been difficult. Moreover, state authority over voting rights was supported by tradition: “No principle of corporation law and practice is more firmly established than a State’s authority to regulate domestic corps, including the voting rights of shareholders.” By implication, the SEC’s authority in this area was questionable absent explicit legislative authorization.

CTS proved to be the death knell of the free market for corporate control. Marty Lipton’s invention of the “poison pill” proved to be a much more potent defense than any state legislation and CTS made it essentially invulnerable to legal attack. When combined with a staggered board, the poison pill becomes unassailable, a result foreshadowed by Powell in CTS. An important tool in harnessing managers to serve the interests of shareholders has been undercut substantially as a result. Whether Powell would have favored this result is impossible to say.

391 CTS, 481 U.S. at 92.

392 Draft Rider A page 39, 86-71 CTS Corporation v. Dynamics Corporation (March 20, 1987) (“The beneficial free market system depends at its core upon the fact that a corporation – except in the rarest situations – is organized under, governed by, the laws of the state of its incorporation. These laws govern the voting rights of shareholders that directly apply to a variety of corporate transactions including takeover bids.”).

393 No. 86-71, CTS Corporation v. Dynamics Corporation, at 37 (March 19, 1987 draft).


395 CTS, 481 U.S. at 85-86 (discussing potential delay in effecting takeovers resulting from classified boards).
PART SIX:  THE SEC


AS A CORPORATE LAWYER, POWELL’S RELATIONSHIP WITH THE SEC HAD NOT ALWAYS BEEN SMOOTH. LIKE MOST SECURITIES LAWYERS, POWELL FOUND THE AGENCY TO BE UNREASONABLE AT

396See Conard, supra note at 196.

397See text at infra notes .

398Stephen Wermiel and Stan Crock, High Court Rulings Are Putting SEC On Shorter Leash, Wall St. J. (October 2, 1980) (“Since 1975, the SEC has made its views known to the Supreme Court in 18 cases. The Justices have ruled against the SEC in 12 of them. The contrast couldn’t be sharper with the period from 1934, when the commission was established, to 1974. In 60 appearances, as a party or friend of the court, the SEC won 48 Supreme Court cases.”).

399Telephone Interview with Jon Sallet, (May 21, 2002); Letter from Stephen Wermiel to Mr. Justice Powell (July 17, 1980) (“I had a pleasurable chat with John Sallet and wanted to express my thanks to you for your kind assistance.”). When the story did not immediately appear, Powell wrote to Wermiel to inquire. Letter from Lewis F. Powell, Jr. to Stephen Wermiel (August 8, 1980).

Other coverage was less favorable. The New York Times quoted Arthur Miller: “This is a pro-business Court,” and Powell in particular “has a Virginia plantation mentality. I have a hunch that possibly he thinks the Civil War went the wrong way.” Louis Kohlmeier, Justice Powell: For Business, a Friend in Court, New York Times (March 14, 1976).
TIMES. TAKING A BREAK FROM THE INVASION OF NORTH AFRICA TO COMPLAIN TO A COLLEAGUE ABOUT A CLIENT’S LOSS BEFORE THE AGENCY, POWELL WROTE:

I HAD HOPE THE WAR . . . WOULD TEMPER THE CRUSADING ORDER OF THE SEC, AND THAT [THE CLIENT] WOULD RECEIVE MODERATE AND FAIR TREATMENT. IT IS EXTREMELY DISAPPOINTING TO FIND THAT AGENCIES OF THE GOVERNMENT ARE STILL FIGHTING AN INTERNAL WAR AGAINST CAPITALISM WHEN THE UNIFIED ENERGIES OF ALL SHOULD BE CONCENTRATED ON FIGHTING THE VERY URGENT AND REAL WAR FOR PHYSICAL SURVIVAL. ALSO ONE OF THE THINGS I HOPE WE ARE FIGHTING FOR IS A JUST AND FAIRLY REGULATED CAPITALISM (I.E. - THE RIGHT TO PRIVATE PROPERTY AND MODERATE PROFIT) IS AN ESSENTIAL COMPONENT OF DEMOCRACY.\textsuperscript{400}

WHILE POWELL WAS FAR FROM BEING AN ADVOCATE OF \textit{LAISSEZ FAIRE} (“FAIRLY REGULATED CAPITALISM,” “MODERATE PROFIT”), HE OBJECTED TO THE SEC’S PERCEIVED HEAVY-HANDEDNESS.

POWELL WAS AFFORDED A CHANCE TO REIN IN THE SEC, BUT HE DECLINED. HIS ACCOUNT:

WALTER S. ROBERTSON, A PARTNER IN SCOTT & STRINGFELLOW, AND A PERSONAL CLIENT OF MINE, BECAME ASSISTANT SECRETARY OF STATE FOR THE FAR EAST IN THE EISENHOWER ADMINISTRATION. HE CALLED ME FROM THE WHITE HOUSE EARLY IN 1953 AND SAID THAT THE PRESIDENT WOULD APPOINT ME CHAIRMAN OF THE SECURITIES & EXCHANGE COMMISSION IF I WOULD ACCEPT THE POSITION. AGAIN, I CONFERRER WITH CLIENTS, SENIOR PARTNERS AT HUNTON & WILLIAMS AND – OF COURSE – WITH JO. ALTHOUGH I HAD DONE A GOOD DEAL OF SEC WORK, AND THE CHAIRMANSHIP OF THE SEC WOULD ASSURE A SUBSTANTIAL LAW PRACTICE THEREAFTER, MY PARTNERS WANTED ME TO STAY IN RICHMOND. I HAD COMMENCED TO DEVELOP MAJOR CLIENTS OF MY OWN . . . AND ALSO — HAVING BEEN AWAY NEARLY FOUR YEARS DURING THE WAR – I PREFERRED TO REMAIN IN MY NATIVE CITY AND STATE AND CONCENTRATE ON BEING A LAWYER.\textsuperscript{401}

\textsuperscript{400}Letter from Lewis F. Powell, Jr. to George Gibson (Nov. 25, 1942).

\textsuperscript{401}Memo from L.F.P., Jr. to Jody, Penny, Molly and Lewis III, Unrecorded Biographical Facts About Your Father, at 10-11 (December 15, 1981). See also Letter from Lewis F. Powell, Jr. to Walter S. Robertson (February 26, 1953); Letter from Walter S. Robertson to Lewis F. Powell, Jr. (March 2, 1953). Shortly after the offer of the SEC chairmanship, Ralph Demmler, appointed chairman after Powell declined, asked Powell if he would be interested in being a commissioner; Powell again declined (without telling Demmler of the earlier offer). Letter from Lewis F. Powell, Jr. to Ralph H. Demmler (April 23, 1953); Letter from Ralph H. Demmler to Lewis F. Powell, Jr. (April 27, 1953).
POWELL LIKED BEING A CORPORATE LAWYER, SPURNING MANY ATTRACTIVE OFFERS THAT WOULD TAKEN HIM AWAY FROM HIS PRACTICE.\textsuperscript{402} AS IT TURNED OUT, POWELL ENDED UP WIELDING FAR GREATER INFLUENCE OVER THE SECURITIES LAWS AS A JUSTICE THAN HE WOULD HAVE EXERCISED AS A CHAIRMAN OF THE SEC.

POWELL OBJECTED MOST TO THE SEC’S EFFORTS TO EXPAND ITS JURISDICTION. IN A MEMO TO A CLERK, HE WROTE:

MY FIRST EXPERIENCE IN CORPORATE AS DISTINGUISHED FROM TRIAL PRACTICE WAS IN THE REPRESENTATION OF VIRGINIA INVESTMENT BANKING FIRMS. I THEREFORE HAVE SOME FAMILIARITY WITH THE SECURITIES ACTS, AND ALSO WITH THE WAY IN WHICH THEY HAVE BEEN ADMINISTERED. GENERALLY, I THINK THESE ACTS HAVE BEEN AMONG THE BEST OF THE REGULATORY STATUTES. BUT THE SEC HAS ALWAYS SOUGHT TO EXPAND ITS REACH. THE HISTORY OF 10B-5 IS AN EXAMPLE.\textsuperscript{403}


\textsuperscript{402}Powell also declined a position teaching law at the University of Virginia. Letter from Lewis F. Powell, Jr. to Dean F.D.G. Ribble (May 10, 1958). Powell also declined the considerably greater prestige of the presidency of the University, as well as the presidency of his alma mater, Washington & Lee, not to mention seats on the Fourth Circuit and the Virginia Supreme Court. Memo from L.F.P., Jr. to Jody, Penny, Molly and Lewis III, Unrecorded Biographical Facts About Your Father, at 11-13 (December 15, 1981).

\textsuperscript{403}Memorandum to Jim Browning from Lewis F. Powell, Jr., 81-680 Herman & MacLean v. Huddleston, at 1.

\textsuperscript{404}Bench Memorandum to Mr. Justice Powell from Jim [Browning], Herman & MacLean v. Huddleston, at 17 (Powell’s marginal notes).
It was the SEC’s effort to expand its authority—not its existence—that troubled Powell.

This Part first addresses a number of cases in which the SEC was rebuked by the Supreme Court for attempts to expand its reach. It then turns to insider trading, the area in which Powell dealt the agency its most stinging losses.

A. The SEC in the Supreme Court

The most extreme example of the SEC’s aggressive litigation strategy appears to have been *International Brotherhood of Teamsters v. Daniel.* The SEC apparently was playing fast and loose regarding its change in position. As recently as 1971, the SEC had taken the position that involuntary pension plans did not involve the sale of security;

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405 Letter from Lewis F. Powell, Jr. to Michael P. Dooley (October 25, 1980).

406 The Court did give the SEC one victory based on deference to agency expertise. *E.I. du Pont de Nemours and Co. v. Collins,* 432 U.S. 46 (1977), involved the unwinding of a holding company structure that the DuPont family had created for their holdings in the DuPont company. Preliminary Memo, No. 75-1870 E. I. Du Pont de Nemours and Co. v. Collins (Summer List 11, Sheet 3). The holding company, Christiana, was to be merged into DuPont, with the Christiana shareholders to receive DuPont shares in the merger. Christiana fell within the definition of an investment company, thus requiring SEC approval of the merger. The SEC approved the merger as “fair” because the merger ratio reflected the net asset value of Christiana (its assets were primarily DuPont stock) and the transaction did not dilute the interests of the DuPont shareholders. The Eighth Circuit reversed, 532 F.2d 584 (1977), holding that the SEC applied the wrong legal standard to the transaction, which the court held to be fair market value of the Christiana stock. The Christiana stock traded at a substantial discount to net asset value, largely due to tax disadvantages of the holding company structure and embedded capital gains in the DuPont stockholdings. The Eighth Circuit believed that in an arms’ length transaction the tax benefits of the transaction would have been shared with the DuPont shareholders.

The Supreme Court reversed, with only Brennan dissenting, based on deference to agency discretion. The discussion at conference, however, went to the substance of “fairness” in the context of a merger. No member of the Court expressed the view that “fairness” requires sharing of benefits or the duplication of the result of an arms’ length transaction, standards favored by some state courts in evaluating mergers. E.g., Rosenblatt v. Getty Oil Co., 493 A.2d 929 (Del. 1985). Instead, the justices viewed the tax benefits to the Christiana shareholders as irrelevant. Conference Notes, No. 75-1870, DuPont v. Collins (Conf. 3/4/77). As Powell put it: “What consideration of fairness would entitle DuPont to claim a share in tax benefits derived by C[hristiana]’s shareholders?” Notes for Conference (undated, from DuPont file). Powell appears to have been swayed by the fact that “SEC consistently has used net asset value.” Id. Powell’s refusal to defer to the SEC in so many cases was based in large part on the SEC’s shifts in position.

407 See text at supra notes.
NOW IT WAS TAKING THE OPPOSITE POSITION. 408 Judge Tone, concurring in the Court of Appeals decision, noted that:


Powell observed that the SEC’s lack of candor about its switch was “not unusual.” 410 The SEC’s brief in the Supreme Court further undermined its credibility. Powell’s clerk advised him that: “THE SEC HAS MADE REPRESENTATIONS TO THIS COURT IN ITS BRIEF [REGARDING ITS CHANGE IN POSITION], WHICH, PUT IN THE MOST CHARITABLE LIGHT, ARE LESS THAN CANDID.” 411

The SEC’s failure to hold to a consistent position was undermining its hopes for deference by the Supreme Court. 412

Powell was frustrated with the SEC, but his own norms of professionalism prevented public criticism. His clerk drafted a sharp rebuke of the SEC, 413 but whatever

408 561 F.2d at 1251.

409 Preliminary Memo, International Brotherhood of Teamsters v. Daniel, Nos. 77-753 and 77-754, at 9 (February 1, 1978 Conference) (Powell’s marginal notes) (emphasis Powell’s).

410 Id. (Powell’s marginal notes).


412 The Solicitor General also rejected the SEC’s newfound position, siding with the Department of Labor in favoring reversal. Motion of the United States for Leave To File Brief Amicus Curiae and Brief for the United States as Amicus Curiae, Nos. 77-753 and 77-754, International Brotherhood of Teamsters v. Daniel, October Term, 1978.

413 The initial draft explained the Court’s refusal to defer to the SEC this way: [W]hen it becomes apparent that an agency has shaped its interpretation of a statute solely to determine the outcome of a particular case, without regard to the ongoing problems of policy and purpose that underlie that agency’s regulatory function, this deference is forfeited. Ad hoc, unprincipled decisionmaking does not draw on developed expertise and constitutes an abuse of
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The Court’s actual practice, Powell was not prepared to announce a position of no deference to the agency. The final opinion contains much milder language. Powell would not indulge the SEC’s enthusiasm for expanding the federal securities laws, which he saw as a profound shift for an agency that historically held a modest view of its power, but he would not characterize the SEC as a rogue agency.

Problems with the SEC were not limited to recent switches in position. Some of the agency’s abuses were longstanding practices. SEC v. Sloan involved the agency’s authority under Section 12(k) of the Exchange Act to “summarily . . . suspend trading in any security . . . for a period not exceeding ten days” if “in its opinion the public interest and the protection of investors so require.” In Sloan, the SEC had relied on this authority to issue a series of orders summarily suspending trading in the common stock of Canadian Javelin.

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On a number of occasions in recent years this Court has found it necessary to reject the SEC’s interpretation of various positions of the Securities Acts. In those cases the SEC either had shifted its position, had not previously developed a position, or had developed its position without consideration of the statutory authorization under which it acts. This case falls into the same category. Our review of the SEC’s past actions convinces us that until the instant litigation arose that agency never had consider the Securities Acts applicable to non-contributory, involuntary pension plans and that its argument to the contrary here demonstrates an alarming and disheartening lack of candor.


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Justice Powell and the Counter-Revolution

The SEC had been issuing successive orders under this authority since 1944.\(^{418}\) Its interpretation, however, was difficult to square with the statutory scheme. Section 12(j) of the Exchange Act authorizes the SEC to suspend securities from registration (which would have the effect of suspending trading) for up to 12 months, but only after giving the affected company notice and a hearing.\(^{419}\) By using its summary power, the SEC could avoid the notice and hearing requirements (which would afford the opportunity for judicial review). Powell found it “[d]ifficult to believe Congress intended to allow the notice + hearing requirements of 12(j) to be by-passed by repetitive resort to 12(k).”\(^{420}\) The situation was exacerbated by the SEC’s attempts to evade review by lifting the orders after Sloan sued (only to renew them subsequently). This was an easy application of the exception to mootness for cases “capable of repetition yet evading review.”\(^{421}\) The brazenness of the SEC did not sit well with the justices; even Brennan, usually a dependable ally for the SEC, thought that an “[a]dmin. agency that acts as SEC did is not entitled to usual deference.”\(^{422}\)

The SEC’s tendency to overreach hurt its position when the Court was called upon to address procedures applicable to the agency’s enforcement actions. The SEC had supported the plaintiff in *Ernst & Ernst* seeking a negligence standard under Section 10(b).

\(^{418}\)Id.


\(^{420}\)Argument Notes, 76-1607 SEC v. Sloan (Argued 3/27/78).

\(^{421}\)Southern Pacific Terminal Co. v. ICC, 219 U.S. 498, 514-515 (1911).

\(^{422}\)Conference Notes, 76-1607 SEC v. Sloan (Conf. 3/29/78).
THE SEC’S ONLY CONSOLATION IN ERNST & ERNST WAS THAT POWELL WAS FORCED, IN ORDER TO HOLD HIS MAJORITY, TO RESERVE THE QUESTION OF WHETHER THE SCIENTER STANDARD WOULD APPLY TO AN ACTION FOR INJUNCTIVE RELIEF BROUGHT BY THE SEC. 423 AARON V. SEC SQUARELY RAISED THAT QUESTION. 424 POWELL’S CONFERENCE NOTES FROM ERNST & ERNST RECORD STEWART’S VIEW THAT AN INJUNCTIVE SUIT BY THE SEC MIGHT PRESENT A DIFFERENT CASE, 425 BUT POWELL’S HEAVY RELIANCE ON THE LANGUAGE OF SECTION 10(B) IN ERNST & ERNST GREATLY WEAKENED THAT POSITION. SECTION 10(B) MAKES NO DISTINCTION BETWEEN GOVERNMENT AND PRIVATE LITIGANTS, HARDLY A SURPRISE GIVEN THAT PRIVATE LITIGATION UNDER SECTION 10(B) WAS NOT ANTICIPATED BY CONGRESS WHEN IT ADOPTED THE EXCHANGE ACT IN 1934. NONETHELESS, “POLICY CONCERNS” RAISED BY PRIVATE LITIGATION PLAYED AN IMPORTANT ROLE IN ERNST & ERNST. IN AARON, THE SECOND CIRCUIT (IN AN OPINION WRITTEN BY JUDGE TIMBERS, FORMER GENERAL COUNSEL OF THE SEC) HAD HELD THAT THE SEC ONLY NEEDED TO SHOW NEGLIGENCE WHEN SEEKING AN INJUNCTION. 426


423 Telephone Interview with Greg Palm, June 6, 2002; 425 U.S. at 193 n. 12.


425 Conference Notes, No. 74-1402, Ernst & Ernst v. Hochfelder, (12/5/75).


427 Bench Memorandum, No. 79-66, Aaron v. SEC, at 1 (Feb. 15, 1980).
AS A MONETARY SANCTION.\textsuperscript{428} THE SEC COULD OVERREACH AND THE SCIENTER STANDARD PROTECTED
DEFENDANTS AGAINST UNWARRANTED DAMAGE TO THEIR STANDING IN THE BUSINESS COMMUNITY.\textsuperscript{429}

Aaron, however, raised another issue that was not present in Ernst & Ernst: the
state of mind required for liability under Section 17(a) of the Securities Act, which
prohibited “any transaction, practice, or course of business which operates or would
operate as a fraud or deceit upon the purchaser.”\textsuperscript{430} The Court previously had found that
similar language in the Investment Advisers Act did not require the SEC to establish an
intent to deceive.\textsuperscript{431} Powell agreed with his clerk that a looser interpretation of Section
17 would lead “the SEC [to] pitch much of its enforcement effort toward that statute,
but the provision is limited to those selling securities . . . as a result, a certain asymmetry
of enforcement policy would develop, where negligent fraud by sellers of securities would
be punishable while negligent fraud by buyers would not.”\textsuperscript{432}

\textsuperscript{428}Id. at 3 (“Injunctions are punitive”).

\textsuperscript{429}Another example of Powell’s efforts to guard against expansions of the SEC’s authority is Bateman Eichler, Hill
Richards, Inc. v. Berner. 472 U.S. 299, 301 (1985). Bateman Eichler raised the issue of whether the in pari delicto
defense could be raised by corporate insiders and brokers-dealers who induce an investor to trade by falsely
representing that they are conveying inside information. The Bateman Eichler opinion, written by Brennan, is
unexceptional, emphasizing that the in pari delicto defense can only be invoked when the fault of the parties is
substantially equal and recognition of the defense would not “significantly interfere with the effective enforcement of
the securities laws.” Bateman Eichler, 472 U.S. at 310-311. Powell’s only notable contribution was to persuade Brennan
to delete a footnote discussing the SEC’s “shingle theory.” See Charles Hughes & Co. v. SEC, 139 F.2d 434 (2nd Cir.
1943), cert. denied, 321 U.S. 786 (1944) (holding that broker-dealers make an implied representation of fair dealing by the
act of putting out their “shingle” as broker-dealers). Powell feared “the SEC might view [the note] as at least an implicit
approval of its theory.” Letter from Lewis F. Powell, Jr. to William J. Brennan, Jr., No. 84-679, Bateman Eichler v. Berner
(May 24, 1985).

\textsuperscript{430}17 U.S.C. § 77q(a)(3).

\textsuperscript{431}SEC v. Capital Gains Research Bureau, 375 U.S. 180 (1963) (construing § 206 of the Investment Advisers Act, which
makes it illegal for any investment adviser “(1) to employ any device, scheme, or artifice to defraud any client or
prospective client;(2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit
upon any client or prospective client”).

\textsuperscript{432}Bench Memorandum, No. 79-66, Aaron v. SEC, at 6 (Feb. 15, 1980).
POWELL UNCHARACTERISTICALLY HAD LITTLE TO SAY AT THE CONFERENCE IN AARON. HE DISCUSSED THE CASE WITH STEWART BEFORE THE CONFERENCE AND THEY AGREED UPON A RESOLUTION. HIS DISCUSSION WITH STEWART WAS NOT UNUSUAL; STEWART WAS “BY A LONG REACH HIS CLOSEST COLLEAGUE ON THE COURT” AND POWELL REGULARLY SPOKE TO HIM ABOUT PENDING CASES, WHICH WAS NOT POWELL’S PRACTICE WITH HIS OTHER COLLEAGUES. \(^{433}\) POWELL APPARENTLY CAME ROUND TO STEWART’S VIEW THAT SECTION 17(a) COULD NOT BE INTERPRETED IN THE SAME FASHION AS SECTION 10(b). \(^{434}\) THIS TIME, TEXT PREVAILED OVER POLICY.

AT THE CONFERENCE, THE CHIEF JUSTICE LED OFF BY VOTING TO AFFIRM THE SECOND CIRCUIT. \(^{435}\) STEWART CAME NEXT; HE MADE IT EASIER FOR POWELL TO AGREE WHEN HE ARGUED THAT “INJUNCTIONS ARE FATAL” AND PROPOSED THAT THE OPINION SAY THAT THE “SEC SHOULD BE CAUTIOUS ABOUT ISSUING AN INJUNCTION.” \(^{436}\) DESPITE THE CONSEQUENCES FOR THE DEFENDANT SUBJECT TO AN INJUNCTION, HOWEVER, STEWART FOUND THE LANGUAGE OF SECTION 17(a) COULD NOT BE READ TO REQUIRE A FINDING OF SCIENTER, ALTHOUGH SECTION 10(b) REQUIRED A “KNOWING” VIOLATION. \(^{437}\) WHITE AGREED THAT 10(b) REQUIRED A “KNOWING” VIOLATION, BUT SECTION 17(a) DID NOT. POWELL AND REHNQUIST SIMPLY EXPRESSED THEIR AGREEMENT WITH STEWART AND WHITE, WHILE BRENNAN, MARSHALL AND BLACKMUN MADE NO EFFORT TO PERSUADE THEIR COLLEAGUES,

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\(^{433}\) Telephone Interview with David Stewart, April 17, 2002.


\(^{435}\) Id.

\(^{436}\) Id.

\(^{437}\) Id.
Simply voting to affirm.\textsuperscript{438} Finally, Stevens gave Stewart and Powell a court, stating that he “would not have joined Hochfelder, but will accept it.”\textsuperscript{439} With a majority for vacatur, the Chief Justice switched to the majority\textsuperscript{440} and assigned the opinion to Stewart.

Stewart wrote the opinion, leaning “heavily + properly on Ernst & Ernst.”\textsuperscript{441} Stewart again reserved the question of the definition of scienter.\textsuperscript{442} For the SEC, Aaron has to be considered a victory, despite the Court’s rejection of its argument for a negligence standard under Section 10(b). Statutory language and precedent preserved the enforcement tool of Section 17(a), despite the misgivings of at least Powell and Stewart about the SEC’s use of injunctions. The threat perceived by Powell was confined; Stewart took care to note that the Court did not address whether a private cause of action exists under § 17(a).\textsuperscript{443}

The combination of a negligence standard for § 17(a), which has subsequently been read not to give rise to a private cause of action,\textsuperscript{444} and a scienter standard for § 10(b) strikes a workable balance. The SEC’s burden of proof is not excessive in the case that is the principal concern of the securities law – selling securities through misstatements

\textsuperscript{438}Id.

\textsuperscript{439}Id.

\textsuperscript{440}Id. Burger eventually ended up concurring. Aaron, 446 U.S. at 702.

\textsuperscript{441}1\textsuperscript{st} Draft, Aaron v. SEC, Nol 79-66 (16 Apr. 1980).

\textsuperscript{442}446 U.S. at 686 n. 5.

\textsuperscript{443}446 U.S. at 689.

\textsuperscript{444}See Maldonado v. Dominguez, 137 F.3d 1 (1\textsuperscript{st} Cir. 1998).
— While private litigants are not free to impose enormous damages on defendants in open-market fraud cases without a showing that the defendants intended to distort securities prices. The Court got to this result primarily as a matter of precedent and statutory language, but it can be defended on policy grounds as well.

Powell’s suspicion of the SEC carried over to Steadman v. SEC, a remarkable case for one reason: it is the only securities case in which Powell dissented. The question raised was the standard of proof to be applied by the SEC in administrative proceedings to bar an investment adviser. The SEC had applied a preponderance standard. Powell worried that: “To bar a middle aged professional investment adviser from pursuing his vocation for life, and at the same time stigmatize him with a judgment of fraud, is more serious than most criminal penalties.” For this reason, Powell favored the “clear and convincing” evidence standard for common law fraud. Despite his dissent, Powell conceded at conference that his vote to reverse was “very tentative.” Without a more vigorous stand from Powell, his colleagues were not inclined to agree with his view on the relative severity of criminal and SEC sanctions. Consequently, the Court adopted the

445 50 U.S. 91, 104 (Powell, J., dissenting).

446 Letter to Mr. Justice Stewart from LFP, 79-1266 Steadman v. SEC (February 12, 1981).

447 Steadman, 450 U.S. at 105.

MORE TYPICAL PREPONDERANCE OF THE EVIDENCE STANDARD.\textsuperscript{449} \emph{Steadman} was Powell’s only dissent in 41 securities law cases over a fifteen year period.\textsuperscript{450}

\textbf{B. Insider Trading}

Powell wrote two foundational opinions on insider trading: \textit{Chiarella v. United States}\textsuperscript{451} and \textit{SEC v. Dirks}.\textsuperscript{452} These opinions reflect Powell’s unease with the SEC’s efforts to expand Rule 10b-5 through aggressive interpretation. Powell thought “that the SEC should have gone to Congress long ago. Rather, it has elected to write expansive Rules (e.g., Rule 10b-5, drafted by Louis Loss one morning), and then undertake to extend the vague language of the Rule to the edge of rationality.”\textsuperscript{453} Powell saw Rule 10b-5’s jurisprudence as a species of “federal common law.” The courts needed to develop workable rules.\textsuperscript{454} This common-law perspective gave wide latitude for policy concerns. Powell worried that prohibitions against insider trading could chill incentives for

\textsuperscript{449}Id. at 101.

\textsuperscript{450}One final case implicated the SEC’s authority. In \textit{SEC v. O’Brien} the Ninth Circuit required the SEC to provide notice to the targets of its non-public investigations that it was serving subpoenas on third parties. 704 F.2d 1065 (1983). The decision lacked any constitutional or statutory basis, and the Solicitor General argued persuasively that the Ninth Circuit’s holding threatened to undermine investigations relating to over 100 programs that used subpoenas of the type issued by the SEC. Preliminary Memorandum, No. 83-751, SEC v. O’Brien (January 6, 1984 Conference). While Powell worried about conferring too much discretion on the SEC in its enforcement efforts, he did not want to see the agency hobbled. The Court voted unanimously to reverse; Powell’s notes suggest that there was virtually no discussion. Conference Notes, No. 83-751, SEC v. O’Brien (Conf. 4/20/84).

\textsuperscript{451}445 U.S. 222 (1980).

\textsuperscript{452}463 U.S. 646 (1983).


ANALYSTS AND OTHER MARKET PROFESSIONALS TO UNCOVER INFORMATION ABOUT PUBLICLY-TRADED COMPANIES.

CHIARELLA WAS AN UNLIKELY BENEFICIARY OF THESE CONCERNS. HE WAS A “MARKUP MAN” AT PANDICK PRINTERS, A PRINTER OF FINANCIAL DOCUMENTS, GIVING HIM ACCESS TO DOCUMENTS RELATING TO CONFIDENTIAL TAKEOVER PLANS. HE DEDUCED THE IDENTITY OF TAKEOVER TARGETS, DESPITE THE BEST EFFORTS OF PANDICK’S CLIENTS (THE POTENTIAL TENDER OFFERORS) TO CONCEAL THEM, FROM THE PRICE HISTORIES, PAR VALUES AND THE NUMBER OF LETTER IN THE FAKE NAMES IN THOSE DOCUMENTS. CHIARELLA CONCEDED AT TRIAL THAT HE KNEW HE WAS GOING “AGAINST THE SEC.” POWELL AGREED THAT CHIARELLA’S CONDUCT WAS “EGREGIOUSLY DISHONEST,” BUT WARNED THAT “WE SHOULD RESIST TEMPTATION TO MAKE BAD LAW.” HE WAS MORE CONCERNED BY THE SECOND CIRCUIT’S “MAJOR EXTENSION OF 10B” TO FIND SILENCE TO BE FRAUD EVEN WITH “NO FIDUCIARY DUTY.”

POWELL ALSO WORRIED THAT REGULATION COULD IMPAIR MARKET EFFICIENCY. HE SAW THE SEC’S EFFORTS TO IMPOSE A “PARITY OF INFORMATION” RULE AS UNDERMINING “INCENTIVES TO PERFORM MARKET RESEARCH IN ORDER TO DISCOVER UNDervalued STOCKS AND THEREBY BRING ABOUT A MORE EFFICIENT ALLOCATION OF RESOURCES.” POWELL AGREED WITH A STUDENT AUTHOR

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455 Memo from Ellen [Richey] to Mr. Justice Powell, Chiarella v. United States, No. 78-1202, at 17 (September 28, 1979).

456 Id. at 27 (Powell’s marginal notes).

457 Preliminary Memorandum, No. 78-1202, Chiarella v. United States (April 13, 1979 Conference). (Powell’s marginal notes.)

458 Memo from Ellen [Richey] to Mr. Justice Powell, Chiarella v. United States, No. 78-1202, at 7 (September 28, 1979) (Powell’s handwritten notes agreeing with this statement by his law clerk).
IN THE HARVARD LAW REVIEW: “[T]he courts must also recognize . . . the importance of preserving incentives for legitimate economic effort, such as gathering new information or perceptively analyzing generally available facts.”

Powell’s understanding of the market mechanisms was an informed one, distinguishing demand theories of price change in the securities markets from informational ones. In response to the government’s claim that Chiarella’s trading could have harmed the offerors that hired Pandick by driving up the target’s stock price, Powell noted that this was unlikely given the small number of shares that Chiarella had purchased.

Powell agreed, however, with the proposition that Chiarella’s unusual trading patterns might have been decoded by other market participants given that he was “a single investor known to his broker to work in a printing firm [who] shows a pattern of predicting tender offers.” Powell’s concern with market efficiency would play a larger role in Dirks, but he clearly had it in his mind in Chiarella.

The Court found itself divided, with five votes to reverse the conviction and three to affirm. The majority was tenuous, however, with Stevens advancing a different rationale. While Stewart, White and Rehnquist agreed with Powell that Chiarella’s conduct did not violate Section 10(b) under any theory, Stevens thought there was a violation, but the government had “tried case on basis of fraud to wrong party.”

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461 Richey Memorandum at 12, supra note.

462 Id.

463 Justice Marshall missed the conference, but later communicated his vote to affirm.

THIS THEORY – THE “MISAPPROPRIATION” THEORY – CHIARELLA HAD DEFRAUDED PANDICK’S CLIENTS, THOUGHT STEVENS, NOT THE INVESTORS FROM WHOM HE PURCHASED.


THE JURY WAS INSTEAD INSTRUCTED THAT IT COULD FIND DECEIT IF CHIARELLA HAD FAILED TO DISCLOSE MATERIAL INFORMATION TO THE SELLERS.

ACCORDINGLY, POWELL (AFTER CONSULTING WITH STEVENS) WROTE TO STEWART, WHITE AND REHNQUIST PROPOSING AN OPINION REVERSING THE SECOND CIRCUIT ON THE GROUND THAT CHIARELLA OWED NO DUTY TO THE SELLERS OF THE SECURITIES. POWELL PROPOSED THAT THEY LEAVE FOR ANOTHER DAY THE QUESTION OF WHETHER CHIARELLA’S BREACH OF DUTY TO PANDICK’S CLIENTS VIOLATED SECTION 10(b).

THE PUBLISHED OPINION REFLECTS STEVENS’ POSITION. POWELL REJECTS A DUTY TO THE SELLERS:

NO DUTY COULD ARISE FROM [CHIARELLA]’S RELATIONSHIP WITH THE SELLERS OF THE TARGET COMPANY’S SECURITIES, FOR PETITIONER HAD NO PRIOR DEALINGS WITH THEM. HE WAS NOT THEIR AGENT, HE WAS NOT A FIDUCIARY, HE WAS NOT A PERSON IN WHOM THE SELLERS HAD PLACED THEIR TRUST AND CONFIDENCE. HE WAS, IN FACT, A

465 Memorandum from Jon Sallet to Mr. Justice Powell, No. 78-1202 United States v. Chiarella, at 1 11/25/79.

466 Id. at 3.

467 Letter from Lewis F. Powell, Jr. to Mr. Justice Stevens, 78-1202 Chiarella, (November 28, 1979).

468 Letter from LFP, Jr. to Potter, Byron and Bill, No. 78-1202 Chiarella, November 29, 1979.
The common law of fraud required a duty to the person on the other side of the transaction. Powell used the common law as a guide to congressional intent. He was creating a federal fiduciary principle, not incorporating state common law doctrines into the federal law of fraud, despite White’s rejection of a federal fiduciary standard in Santa Fe. The SEC and the Justice Department were attempting to extend Section 10(b) beyond Powell’s understanding of Congress’s intention in 1934, and the Second Circuit was acquiescing in those efforts. As Powell saw it, courts had a responsibility to check such overreaching by the executive branch. Chiarella was a conscious attempt to bring precision and rigor to an area of the law in which the lower courts had strayed from Congress’s purposes. Hence Powell’s reminder that “Section 10(b) is aptly described as a catchall provision, but what it catches must be fraud.”

While the opinion attempts to ground Rule 10b-5 in the common law of fraud, it does not reject the broader “misappropriation” theory.

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470 Id. at 228.
471 Telephone Interview with Jonathan Sallet (May 21, 2002).
472 See text at supra note. On the tension between Santa Fe and Chiarella, see Stephen M. Bainbridge, Insider Trading Regulation: The Path Dependent Choice Between Property Rights and Securities Fraud, 52 SMU L. Rev. 1589 (2000).
473 Telephone Interview with Jonathan Sallet (May 21, 2002).
474 Id.
475 Chiarella, 445 U.S. at 234-235.
476 Chiarella, 445 U.S. at 236.
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Majority, but left the misappropriation theory alive. To make matters worse, Stevens highlighted the theory’s potential in his concurrence.477 Powell responded that he would prefer:

Not emphasizing that the result may have been different if liability had been premised on a duty to the acquiring company, as I am by no means sure that 10(b) should be extended this far beyond its clear purposes at the time of its enactment in 1934. As we are talking about criminal liability, I am inclined to think we should leave it to Congress to draft a more refined and specific criminal statute. To be sure, you leave the question for another day. But with a five to four vote by the Court, I would prefer—I think—not to invite a judicial rather than a legislative consideration of the question.478

This was about as strong an objection as Powell could muster, but Stevens nonetheless published the concurrence. In Powell’s estimation, Congress was better placed to specify the conduct to be prohibited. As he wrote to Chief Justice Burger,

If I were in Congress, I would probably support a carefully drawn criminal statute that would make it a crime for one to do what Chiarella did. But it is clear (at least to me) that Congress never had the slightest intention—back in 1933 and 1934—to extend the Securities Acts to this type of situation. . . . Before criminal liability is imposed by the courts, I think the Congress should face up to this question, and draft a proper criminal statute that puts people on notice.

I add that I do not admire Mr. Chiarella any more than you do.479

Powell’s preference for congressional action went unheeded, as Congress was unable to agree on a definition of insider trading.480 Powell’s successors filled the gap by interpreting Section 10(b) flexibly to facilitate the SEC’s efforts to crack down on insider

477Id. at 237.

478Letter from Lewis F. Powell, Jr. to Mr. Justice Stevens, No. 78-1202 Chiarella v. United States, February 4, 1980.


trading. That interpretive flexibility carries with it a breadth of application that would have astounded the 1934 Congress that drafted Section 10(b).

Powell’s opinion in SEC v. Dirks addresses more squarely the relation between restrictions on the use of inside information and market efficiency. The SEC censured Dirks, a securities analyst, for passing to his customers information about a massive fraud at Equity Funding that he had learned from current and former Equity Funding employees. Dirks’ customers relied on that information to sell large quantities of Equity Funding shares before the company’s collapse.

On petition for certiorari, the Solicitor General authorized the SEC to file an opposition to certiorari, but refused to join the SEC’s position. The Solicitor General took the position that information obtained by Dirks could not be considered confidential, highlighting the enormous obstacle that Dirks’ role in uncovering the Equity Funding fraud posed for the SEC’s argument. The SEC was therefore left to its own devices to defend its censure of Dirks. The agency got no help from the DC Circuit, which affirmed

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482 On Congress’s intent in 1934, see generally Steve Thel, The Original Conception of Section 10(b), 42 Stan. L. Rev. 385 (1990).


485 Preliminary Memorandum, No. 82-276, Dirks v. SEC, at 8, November 12, 1982 Conference.

486 Powell noted this point made by the United States in its brief on the merits: “The Commission’s erroneous imposition of liability in this case has serious consequences for federal law enforcement, which frequently depends upon private initiative to uncover criminal conduct . . . Petitioner accomplished what regulatory authorities were unable to do.” Brief for the United States, quoted in Powell’s memo to file, 82-276 Dirks v. SEC, 03/21/83.
the censure on the ground that Dirks “breached his duty to the Commission and to the public not to misuse insider information.”

This “absurd” holding squarely conflicted with Powell’s reasoning in Chiarella. Although the lower court issued a more limited opinion on petition for rehearing, the SEC faced an uphill battle to defend the judgment.

The case was of obvious importance to the securities industry: Powell’s law clerk, Jim Browning recalls that there was “a blanket of blue and gray suits in the courtroom” with SEC staff and the local corporate bar taking up all the places in the audience for the argument.

Powell had no doubt that the DC Circuit’s judgment should be reversed, but he wanted to do so in way that would uphold a ban on insider trading and tippee liability. He charged Browning with developing a theory that would achieve this result.

Browning was in some ways an odd choice for this task because he had “considerable doubts that federal securities law should ban any insider trading.”

Moreover, he felt either the SEC’s position prohibiting any use of inside information in trading, or the free market position permitting unconstrained insider trading, were more

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487 Bobtail Bench Memorandum, No. 82-276, Dirks v. SEC, from James Browning, at 3 (March 21, 1983).

488 Id. (Powell’s marginal notes.)

489 681 F.2d 824 (1982).

490 Courts addressing the issue of tippee liability had taken a narrower approach. See Donald C. Langevoort, Insider Trading and the Fiduciary Principle: A Post-Chiarella Restatement, 70 Cal. L. Rev. 1, 29-32 (discussing cases).

491 Telephone interview with James Browning, April 3, 2002.

492 Memorandum to Mr. Justice Powell from Jim, Dirks v. SEC, No. 82-276, at1, 3/22/83.
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INTELLECTUALLY DEFENSIBLE THAN THE MIDDLE GROUND SOUGHT BY POWELL.493 BUT POWELL SAW
THE SEC’S APPROACH AS UNPREDICTABLE AND UNFAIR; MOREOVER, HE THOUGHT THAT ANALYSTS
WERE IMPORTANT TO THE OPERATION OF THE SECURITIES MARKETS. THE SEC’S PROSECUTION OF DIRKS
WAS AN ASSAULT ON THE ANALYST INDUSTRY.494 ON THE OTHER HAND, POWELL’S SENSE OF PROPERITY
ABHORRED THE ABUSE OF TRUST THAT INSIDER TRADING REPRESENTED.495 A PROHIBITION WAS
APPROPRIATE, IF THAT PROHIBITION COULD BE APPLIED FAIRLY AND PREDICTABLY.496

DESPITE HIS SKEPTICISM, BROWNING SUCCEEDED IN THE TASK SET FOR HIM BY HIS BOSS. HE
FOUND THE MIDDLE GROUND IN A COMMENTARY ON THE CASE IN A LEGAL NEWSPAPER.497 ALTHOUGH
POWELL APPEARS TO HAVE BEEN UNINTERESTED IN BROWNING’S EXTENDED ANALYSIS OF THE WELFARE

493 Telephone Interview with James Browning, April 3, 2002.

494 Id.

495 A later case confirms that Powell’s position on insider trading was based on ethics, not finance theory. Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299 (1985), raised the issue of whether corporate insiders and brokers-dealers who induce an investor to trade by falsely representing that they are conveying inside information could raise an in pari delicto defense. The plaintiffs made the somewhat unusual admission that they had purchased stock on the basis of what they believed was nonpublic information. The information proved to be false, however, and the plaintiffs lost money. They sought to recover their losses from the broker-dealer who had communicated the false inside information, as well as an officer of the issuer that was the subject of the rumor, who had tacitly confirmed the information. Id. at 301-302.

Powell summarized his view of the case in his notes for the post-argument conference:

I conclude Tippees did know that [the corporate officer] had breached his duty by confirming
that info. was not public + that broker was trustworthy. Thus tippees were culpable.

But tippees conduct was not as culpable as tippers. Duty of tippers was clear.

Disallowing defense of in pari delicto furthers policy of Securities Acts. Persons who
becomes tippers present basic problem of insiders giving out tips. They should not go free because

Notes for Conference, Bateman Eichler, etc. v. Berner, No. 84-679, at p.1 (4/4/85). This excerpt confirms that Powell viewed the principal problem with insider trading as the abuse of trust by the corporate insider. The harm to the securities markets stemming from information asymmetry was, at most, a secondary concern. Powell’s greater concern with insider trading law was the risk posed by over-aggressive enforcement of the prohibition by the SEC.

496 Telephone Interview with James Browning, April 3, 2002.

497 Chazen, “Dirks” Presents Unique Corporate, Social Issues, Legal Times 14 (March 14, 1983). The author would not receive attribution in the opinion, however, because of Powell’s unease with citing a piece that was not in “a scholarly journal.” Second Draft, Dirks v. SEC, No. 82-276, at 24, 5/10/83.
EFFECTS OF INSIDER TRADING PROHIBITIONS, BROWNING HIT THE MARK WITH HIS LEGAL ANALYSIS.

BROWNING ARGUED THAT:

THERE WAS NO “EXPLOITATION” BY THE INSIDERS. DIRKS’ INFORMANTS RECEIVED NO MONETARY BENEFIT FOR REVEALING EQUITY FUNDING’S SECRETS, NOR DID THEY HAVE ANY APPARENT DESIRE TO MAKE A GIFT OF VALUABLE INFORMATION TO DIRKS. THE INFORMANTS MAY HAVE HAD A DUTY NOT TO TRADE ON INSIDE INFORMATION WITHOUT DISCLOSURE, BUT THEY DID NOT. THEREFORE, EVEN IF DIRKS’ INFORMANTS DID VIOLATE A DUTY TO THE COMPANY BY DISCLOSING, THEIR CONDUCT DID NOT HAVE ONE OF THE ESSENTIAL ELEMENTS OF BREACH OF THE AGENCY RELATIONSHIP: THE EXPLOITATION OF CORPORATE INFORMATION BY AN INSIDER.

WE BOTH KNOW DIRKS IS A FREAK CASE. THE SITUATIONS WE ARE CONCERNED WITH ARE WHERE SECURITIES ANALYSTS INTERVIEW EMPLOYEES SEEKING INFORMATION: IS THERE LIABILITY? IF THE BREACH OF AN EMPLOYEE’S DUTY ALONE IS ENOUGH TO ESTABLISH TIPPIE LIABILITY, SECURITIES ANALYST [sic] WILL BE CHILLED FROM USING ANY OF THE INFORMATION HE GETS. IF, ON THE OTHER HAND, EXPLOITATION OF CONFIDENTIAL INFORMATION BY INSIDERS IS A PREREQUISITE TO TIPPIE LIABILITY, SECURITIES ANALYSTS WILL BE ENCOURAGED TO SEEK INFORMATION FROM CORPORATE EMPLOYEES. I WILL NOT EMPHASIZE THE OBVIOUS BENEFITS OF PROTECTING THE INFORMATION-GATHERING DUTIES OF A SECURITIES ANALYST.498

POWELL AGREED THAT “DIRKS IS EASY, BUT IS THERE A GENERAL PRINCIPLE?”499

POWELL FOUND HIS GENERAL PRINCIPLE IN BROWNING’S “EXPLOITATION” FORMULATION, ALTHOUGH HE RECAST IT. POWELL, IN AN UNUSUAL STEP, PREPARED A MEMO FOR THE CONFERENCE AT WHICH THE JUSTICES WOULD DECIDE THE CASE,500 PERHAPS AS A BID FOR THE OPINION ASSIGNMENT.501

POWELL WROTE:

WE MADE AN IMPORTANT POINT IN CHIARELLA. IT DID NOT INVOLVE A TIPPIE, BUT IT DID ESTABLISH THAT LIABILITY CANNOT BE IMPOSED IN THE ABSENCE OF A

498 Memorandum to Mr. Justice Powell from Jim, Dirks v. SEC, No. 82-276, at 1, 3/22/83.

499 Id.

500 Memo for Conference, 82-276 Dirks v. SEC, at 1, 3/23/83.

501 Telephone Interview with James Browning, April 3, 2002.
fiduciary duty to disclose before trading. The only reference in Chiarella to tippees is in fn. 12. The critical sentence in this note says:

“The tippee’s obligation has been viewed as arising from his role as a participant after the fact in the insider’s breach of a fiduciary duty.”

Thus, where the tippee becomes a “participant after the fact”, he shares whatever duty the insider breached by conveying the information. This analysis makes Dirks’ case easy to decide. His liability depends on a finding that the former Equity Funding employees – of which Secrist [Dirks’ principal source] was only one – who disclosed the fraud, breached their fiduciary duty to Equity Funding.

But even the SEC concedes there was no such breach of duty. None of these employees profited by disclosing fraud they acted strictly in the public interest. Therefore, Dirks was not a participant after the fact in anyone’s breach of duty.502

In sum, Chiarella required a breach of duty and Dirks’ sources had violated no duty.

Dirks therefore could not be liable for violating Rule 10b-5. Powell was not satisfied, however, with merely reversing the judgment of the DC Circuit. He continued:

Deciding this case without identifying a general principle would accomplish very little.

Let me make clear the type of situation to which the principle would be applied. This case does not involve a Texas Gulf Sulfur situation where an officer or director of a corporation himself trades on inside information for personal gain. No do we have an insider – who to benefit a friend – discloses inside information on which the friend profits. The law is fairly well settled with respect to these straightforward cases.

The much broader, underlying problem in this case concerns the necessity of information being made available for the health of the securities markets. In this case, the SEC’s opinion stated:

In the course of their work, analysts actively seek out bits and pieces of corporate information not generally known to the market for the express purpose of analyzing that information and informing their clients who, in turn, can be expected trade on the basis of the information. The value to the entire market of these efforts cannot be gainsaid: market

502Memo for Conference, 82-276 Dirks v. SEC, at 1, 3/23/83.
EFFICIENCY IN PRACTICE IS SIGNIFICANTLY ENHANCED BY SUCH INITIATIVE TO FERRET OUT AN[ ]D ANALYZE INFORMATION, AND THE ANALYSTS’ WORKS REDOWNS [SIC] TO THE BENEFIT OF THE INVESTORS.”

IF WE SUSTAIN ITS OPINION IN THIS CASE SECURITIES ANALYSTS WILL BE FAR LESS LIABLE TO “FERRET OUT” INFORMATION. THEY WILL BE CONCERNED CONSTANTLY WITH THE UNCERTAINTY OF LAWSUITS, WITH JURIES DETERMINING WHETHER THE INFORMATION CIRCULATED WAS CONFIDENTIAL AND SHOULD NOT HAVE BEEN DISCLOSED. 503


(i) THE RELATIONSHIP BETWEEN THE INSIDER AND THE RECIPIENT (E.G., THE ANALYST); WHAT WERE THEIR RESPECTIVE PURPOSES? PARTICULARLY, DID THE INSIDER EXPECT TO PROFIT HIMSELF OR TO BENEFIT A FRIEND RATHER THAN TO INFORM THE MARKET GENERALLY?

(ii) WHO INITIATED THE DISCLOSURE? TYPICALLY, THE ANALYST SEeks OUT THE CORPORATE EXECUTIVE – THIS IS COMMONPLACE. Equally, commonplace, executives brief large meeting of analysts. THE CIRCUMSTANCES OF DISCLOSURE ARE RELEVANT – AS IN THIS CASE. 505

THIS FACT-INTENSIVE INQUIRY WENT AGAINST POWELL’S USUAL PREFERENCE FOR PREDICTABILITY AND FAIRNESS, WHICH HAD PREVAILED IN CHIARELLA. BUT THE ALTERNATIVES – THE SEC’S BLANKET BAN ON THE USE OF INSIDE INFORMATION, ON THE ONE HAND, AND TURNING A BLIND EYE TO ABUSES OF OFFICE BY CORPORATE INSIDERS, ON THE OTHER – WERE WORSE.

503Id. at 2-3.
504Id. at 4.
505Id.
Powell’s diligent preparation was rewarded by the opinion assignment. Holding a court, however, would not be simple. The outrageousness of the SEC’s sanctioning Dirks made it easy to find a majority for reversal, but no consensus emerged from the conference on the rationale. White’s vote, for example, was “tentative,” and seemed to be based on the fact that Dirks “didn’t unload.” Although White thought that “[h]is tippees may be guilty of violating rules,” Stevens, by contrast, thought that “Dirks breached no duty. Even if he had owned stock + sold it, but he had no duty. A person who is an outsider has no duty.” O’Connor thought that “the ultimate solution is to require fraud to be disclosed first to SEC - + would like to say this.” There was a real possibility that the Dirks majority would fragment.

Powell and Browning struggled through seven drafts of the opinion before it was ready to circulate. After reviewing Browning’s first draft, Powell again emphasized the importance of protecting the role of market analysts:

As you know, it is customary for management of listed companies to convey supplemental information (some people call in [sic] “chumming” the market) to analysts. This is done in primarily in two ways: talks to, and questions and answer sessions with, large groups of analysts – in effect, open meetings. Similarly, information not available through required filings with the SEC often is given at stockholders meetings where most of the stock is represented by proxies, and news coverage may be scant and uninforming. The more difficult type of information gathering – difficult in terms of line drawing for our purposes – is where the analysts will visit


507 Conference Notes of LFP, No. 82-276. Dirks v. SEC.

508 Id.

509 Id.
CORPORATE HEADQUARTERS AND CONFERENCE WITH SENIOR OFFICERS. THE ANALYST IS LIKELY TO BE A SPECIALIST IN THE PARTICULAR BUSINESS. WHEN HE RETURNS TO HIS FIRM, OFTEN HE WILL CIRCULATE “BUY” OR “SELL” RECOMMENDATIONS TO CLIENTS AND PERSON WHO THE FIRM WOULD LIKE TO HAVE AS CLIENTS. THESE RECOMMENDATIONS ARE BACKED UP BY A REPORT ON THE INTERVIEW. THE LINE DRAWING PROBLEM IS ONE THAT IMPACTS DIRECTLY ON BOTH THE CORPORATE OFFICERS AND THE ANALYSTS. NEITHER CAN BE QUITE SURE WHEN THE “LINE” IS CROSSED.  

POWELL’S YEARS IN CORPORATE BOARDROOMS GAVE HIM A CLEAR UNDERSTANDING OF HOW CORPORATE DISCLOSURE WORKED ON THE GROUND.

THE EMPHASIS ON “PURPOSE” IN DETERMINING WHETHER THERE WAS A FIDUCIARY BREACH PROVED TO BE A STUMBLING BLOCK IN GAINING A MAJORITY. POWELL QUICKLY GOT THREE VOTES FOR HIS INITIAL CIRCULATION (WHITE, RENQUIST AND STEVENS), BUT O’CONNOR HAD RESERVATIONS. THE FIRST WAS RATHER IDIOSYNCRATIC; SHE WANTED TO RESERVE THE QUESTION OF WHETHER INFORMATION ABOUT CRIMINAL CONDUCT COULD BE CONSIDERED MATERIAL INFORMATION.  

While the answer to this question would almost certainly be “YES,” deferring the answer cost Powell nothing.

O’CONNOR’S SECOND CONCERN WAS MORE SUBSTANTIAL. SHE WORRIED THAT FOCUSING ON THE INSIDER’S PURPOSE IN DISCLOSING THE INFORMATION WOULD REQUIRE “THE FACT-FINDER ... TO DETERMINE THE SUBJECTIVE STATE OF MIND OF THE INSIDER” “AN INHERENTLY DIFFICULT

510 Memorandum to Jim from Lewis F. Powell, Jr., 82-276 Dirks v. SEC, (May 2, 1983).

511 Powell previously appears to have taken a narrower view of the legality of selective disclosure. In a memo to his law clerk in a Section 16(b) case, Powell wrote: “absent a presence on the board there would be a clear violation of 10b-5 for a corporation (or its officers or directors) to disclose to any stockholder information not available to all holders.” Memorandum from Lewis F. Powell, Jr. to Carl Schenker, No. 74-742 Foremost-McKesson v. Provident Securities, at pp. 4-5 (November 19, 1975). Powell’s apparently believed that Rule 10b-5 would cover any selective disclosure to stockholders that led to trading. Powell’s considerably narrower position in Dirks now has been overturned by the SEC through its Regulation FD. Securities Act Rel. No. 33-7881 (August 15, 2000).

512 Letter from Sandra Day O’Connor to Lewis F. Powell, Jr., No. 82-276 Dirks v. SEC, June 7, 1983.
Justice Powell and the Counter-Revolution

Determination.\textsuperscript{513} She suggested omitting the purpose discussion, a change that Powell was not willing to make.\textsuperscript{514} More promising was her proposed alternative, which looked to:

\begin{quote}
Whether the insider derives a direct or indirect benefit from his disclosure, and that benefit is primarily of a pecuniary nature. An emphasis on benefit differs from your approach only insofar as it establishes a more objective indicia of liability. If, as a factual matter, the insider did not benefit from his disclosure, then I am not inclined to be concerned with a further inquiry into his motivation. I am not sure about what will be gained from an inquiry into intent, but from my past experience on the bench, I know that a great deal of time will be lost!\textsuperscript{515}
\end{quote}

O’Connor shrewdly couched her suggested change as “more objective” and based on her “past experience on the bench.” These factors were well calculated to persuade Powell, who favored predictability and respected the practical wisdom of experience. The opinion accordingly was revised to reflect O’Connor’s “quite constructive” suggestions.\textsuperscript{516} These

\begin{itemize}
\item \textsuperscript{513}Id.
\item \textsuperscript{514}Id.
\item \textsuperscript{515}Id.
\item \textsuperscript{516}Letter from Lewis F. Powell, Jr. to Sandra Day O’Connor, 82-276 Dirks v. SEC, June 9, 1983. The changes:
\end{itemize}

\begin{itemize}
\item \textbf{Before:} both the insider and the analyst will act in good faith
\item \textbf{After:} the insider will act consistently with his fiduciary duty
\item \textbf{Before:} Whether disclosure is a breach of duty therefore depends in large part on the purpose or good faith of the insider who made the disclosure.
\item \textbf{After:} Whether disclosure is a breach of duty therefore depends in large part on the purpose of the disclosure, \textit{i.e.}, whether the insider personally expects to benefit, directly or indirectly, from his disclosure.
\item \textbf{Added:} The SEC argues that, if inside-trading liability does not exist when the information is transmitted for a proper purpose but is used for trading, it would be a rare situation when the parties could not fabricate some ostensibly legitimate business justification for transmitting the information. We think the SEC is unduly concerned. In determining whether the insider’s purpose in making a particular disclosure is fraudulent, the SEC and the courts are not required to read the parties minds. Scienter may be relevant in some case in determining whether the tipper has violated his \textit{Cady, Roberts} duty, but to determine whether the disclosure itself “deceive[s], manipulate[s], or defraud[s]” shareholders,
Changes narrowed the scope of improper purposes that the SEC could argue constituted breaches of fiduciary duty under Rule 10b-5. Garden variety breaches of the duty of care were clearly out; tipping required a breach of the duty of loyalty. As a result, the federal common law of insider trading was brought into line with the traditional distinction in state corporate law between breaches of care and loyalty. Powell achieved his goal of protecting the analyst community from being swamped by the prohibition against insider trading; O’Connor helped him achieve this goal within a predictable framework.

Powell wrote a third insider trading opinion, but it never made it to the United States Reports. Carpenter v. United States came to the Court during Powell’s last term on certiorari. The case raised the issue that Chiarella had left unresolved: Was a breach of duty to the owner of inside information, rather than the counterparty to the trade, sufficient for Rule 10b-5 liability? Powell saw the Second Circuit’s affirmative

\*Aaron v. SEC, 446 U.S. 680 (1980), courts should focus on whether the insider expects to receive a direct or indirect personal benefit from the disclosure, such as – for example – a pecuniary gain or a reputational benefit that may translate into future earnings.

Before: Determining the purpose of any one disclosure, a question of fact, will not always be easy for the courts.

After: Determining whether an insider personally benefits from a particular disclosure, a question of fact, will not always be easy for courts.


RESPONSE TO THIS QUESTION AS A DIRECT CHALLENGE TO THE DOCTRINE THAT HE HAD DEVELOPED IN

_Chiarella_ and_ Dirks_.

_Carpenter_ involved unusual facts. Defendant R. Foster Winans was a reporter for the _Wall Street Journal_ and one of the writers of the “Heard on the Street” column; defendant David Carpenter was a news clerk at the _Journal_. 519 Defendant Kenneth Felis was a stockbroker. 520 Winans would pass securities-related information scheduled to appear in the next day’s column through Carpenter to Felis, who would then, depending upon the tenor of the article, buy or sell the subject securities. 521 _Wall Street Journal_ policy deemed all news information to be company property and required nonpublic information to be treated as confidential. 522 Ignoring this policy, the conspirators netted nearly $690,000 from the scheme. 523 The stress of an SEC inquiry caused the conspirators to turn on each other, 524 and an indictment followed. The Second Circuit affirmed the conspirators’ convictions for mail, wire, and securities fraud. 525 With respect to the


520 Id.

521 Id.

522 Id.

523 Id. at 1027.

524 Id.

525 Id. at 1036.
SECURITIES FRAUD COUNTS, THE SECOND CIRCUIT UPHOLD THE CONVICTIONS UNDER THE MISAPPROPRIATION THEORY BASED ON ITS EARLIER CASES.526

THE CONSPIRATORS PETITIONED FOR CERTIORARI, WHICH THE COURT INITIALLY VOTED TO DENY. POWELL HAD PLANNED TO WRITE IN THE EVENT OF A DENIAL,527 AND HIS DRAFT DISSENT MADE IT CLEAR THAT HE WOULD HAVE REJECTED THE MISAPPROPRIATION THEORY ALTOGETHER.528 HE ARGUED THAT "THE SECOND CIRCUIT HAS RESOLVED AN IMPORTANT QUESTION OF SECURITIES LAW IN A WAY THAT APPEARS TO CONFLICT WITH RECENT OPINIONS OF THIS COURT."529 THE FIRST OF THESE OPINIONS WAS CHIARELLA, WHICH BEGAN WITH THE PREMISE THAT:

[PARTIES TO A BUSINESS TRANSACTION GENERALLY DO NOT HAVE AN AFFIRMATIVE DUTY TO DISCLOSE INFORMATION ABOUT THE TRANSACTION. THE COURT NOTED, HOWEVER, THAT A FAILURE TO DISCLOSE MATERIAL INFORMATION COULD BE FRAUDULENT IN CERTAIN CIRCUMSTANCES. "BUT SUCH LIABILITY IS PREMISED UPON A DUTY TO DISCLOSE ARISING FROM A RELATIONSHIP OF TRUST AND CONFIDENCE BETWEEN PARTIES TO A TRANSACTION."530

POWELL'S TIED HIS READING OF CHIARELLA CLOSELY TO THE COMMON LAW OF DECEIT, WHICH REQUIRES THAT "[O]NE PARTY TO A BUSINESS TRANSACTION IS UNDER A DUTY TO EXERCISE REASONABLE CARE TO DISCLOSE TO THE OTHER BEFORE THE TRANSACTION IS CONSUMMATED . . . MATTERS KNOWN TO HIM THAT THE OTHER IS ENTITLED TO KNOW BECAUSE OF A FIDUCIARY OR OTHER SIMILAR RELATION OF

526Id. at 1034-1035. The Second Circuit also rejected the argument that the misappropriation theory did not apply because the victim of the misappropriation was the Wall Street Journal and not the companies whose shares were traded. Id. at 1032-1034.

527Preliminary Memorandum, Carpenter v. United States, No. 86-422, December 5, 1986 conference. (Powell’s marginal notes.)

528Draft dissent from denial of certiorari, Carpenter et al. v. United States, No. 86-422, at 1 (December 10, 1986).

529Id.

530Id. at 3 (citation omitted).
TRUST AND CONFIDENCE BETWEEN THEM. 531 Thus, deceit requires that one party to a transaction owe a duty of disclosure to the other. Powell argued that Chiarella had incorporated this common law requirement into § 10(b), 532 notwithstanding the concessions he had made to Justice Stevens in that case to secure a majority.

Powell then turned to Dirks, which "established that when outsiders have a fiduciary duty to the shareholders, they cannot purchase securities from those shareholders without first informing them of material information that might influence the decision to purchase or sell the securities." 533 Again, the relevant disclosure duty was between the parties to the securities transaction. By contrast, in Carpenter there was no fiduciary relationship between the defendants and those who had sold them securities. 534 The only fiduciary relationship at issue was Winans' duty to the Journal. 535 Powell noted, however, that previous cases did not support the proposition that the fiduciary duty an individual owes to his employee was sufficient to support an action under Rule 10b-5. 536 Rather, the inquiry under Rule 10b-5 "must focus on the petitioner's relationship with the sellers of . . . securities." 537 Because there was no such relationship, Powell concluded that the petitioners' conduct did not violate Rule 10b-5.

531Restatement (Second) of Torts § 551(2) (1977).
532Draft dissent, at 4.
533Id.
534See id.
535See id. at 4-5.
536See id. at 6.
537Id. (internal quotation marks and citations omitted).
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Powell's draft dissent was joined by O'Connor and Rehnquist, both of whom had initially voted to grant certiorari. The dissent was never published, however, because Brennan and Scalia changed their votes to grant certiorari. Before Carpenter was argued, Powell retired. His successor, Anthony Kennedy, was not confirmed until after the argument. The Court split 4-4 on the misappropriation theory and consequently upheld the conviction without opinion. Given Powell's rejection of the misappropriation theory in his draft dissent, it is reasonable to conclude that if Powell had not retired when he did, the Supreme Court would have rejected the misappropriation theory in 1987. As it turned out, the Court did not decide the issue for another decade, upholding the theory by a 6-3 vote in United States v. O'Hagan. In this case Powell's influence did not survive his retirement, with even O'Connor voting to uphold the theory.

Part Seven: Conclusion

538See Letter from Chief Justice Rehnquist to Justice Powell, (Dec. 11, 1986); Letter from Justice O'Connor to Justice Powell, (Dec. 11, 1986).


541Stuart Taylor, Jr., Kennedy Sworn In as 104th Justice on High Court, N.Y. Times, Feb. 19, 1988, at A10 (Kennedy sworn in on February 18, 1988).

542Carpenter, 484 U.S. at 24.

POWELL WORRIED THAT HIS EXPERIENCE AS A CORPORATE LAWYER WOULD GENERATE
CONTROVERSY WHEN HE WAS NOMINATED TO THE SUPREME COURT. POWELL WROTE TO ATTORNEY
GENERAL JOHN MITCHELL IN 1969, WHEN HIS NAME WAS FIRST MENTIONED AS A POSSIBLE NOMINEE:

MY OWN PRACTICE, BOTH IN LITIGATION AND OFFICE WORK OVER THE YEARS, HAS BEEN
LARGELY FOR CORPORATE AND BUSINESS CLIENTS. I ALSO SERVE ON THE BOARDS OF
DIRECTORS OF SEVERAL CORPORATIONS OF FAIRLY SUBSTANTIAL SIZE. IN VIEW OF THE
OPPOSITION OF ORGANIZED LABOR TO JUDGE [CLEMENT] HAYNSWORTH BECAUSE OF HIS
ALLEGED “ANTILABOR BIAS”, IT MUST BE ASSUMED THAT THERE WOULD BE SIMILAR
OPPOSITION TO ANY LAWYER WHOSE PROFESSIONAL CAREER HAS BEEN DEVOTED
PRIMARILY TO BUSINESS REPRESENTATIONS. 544

AS IT HAPPENED, POWELL FACED NO SIGNIFICANT OPPOSITION FROM LABOR GROUPS545 AND HIS VIEWS
ON BUSINESS RECEIVED LITTLE ATTENTION DURING HIS CONFIRMATION HEARINGS. 546 ONLY AFTER
POWELL’S CONFIRMATION DID HIS SOMEWHAT STRIDENT VIEWS ON DEFENDING FREE ENTERPRISE COME
UNDER MEDIA SCRUTINY, BUT BY THEN IT WAS TOO LATE.547

POWELL’S JUDICIAL CAREER SHOWS THE IMPORTANT ROLE THOSE VIEWS PLAYED IN THE
DEVELOPMENT OF THE SECURITIES LAW. MOST OF THE ISSUES PRESENTED TO THE COURT IN THE CASES
DISCUSSED IN THIS ARTICLE WERE NOMINALLY QUESTIONS OF STATUTORY INTERPRETATION. THE
COURT’S OPINIONS EMPHASIZE STATUTORY LANGUAGE, WITH POWELL’S OPINIONS IN PARTICULAR

544Letter from Lewis F. Powell, Jr. to John N. Mitchell (December 12, 1969).

545Powell may have benefitted from having his nomination coupled with Rehnquist’s. Jeffries, supra note at 10 (“Labor,
liberals, and civil rights leaders who tried to defeat Rehnquist were willing to accept Powell, if only to emphasize the
contrast between the two.”).
Powell did have an “antilabor bias” as conventionally understood, having lobbied to strengthen Virginia’s
“Right to Work” law. Letter from Lewis F. Powell, Jr. to Edward Emerson Lane (March 4, 1954). He also favored
extending the antitrust laws to unions. Lewis F. Powell, Jr., Trends in Antitrust, at 13 (delivered to the Conference of
Financial Executives, Williamsburg, VA, June 17, 1967) (“When the antitrust laws were enacted there was perhaps good
reason for exclusion of fledgling unions from their anti-monopoly provisions. Today, under vastly different social,
经济 and political conditions, the great monopolists in this country are the major unions.”).


GROUNDING IN CAREFUL STATUTORY READINGS. Nonetheless, Powell’s reading of those texts and their legislative purposes was colored by his experience in corporate boardrooms, consistently leading him favor to narrower readings.

Powell’s conservative stance in securities cases was not the product of grand theory. He did not subscribe to the normative libertarianism or economic analysis that enchants some corporate and securities law academics. Rather, Powell’s nearly forty years of experience in corporate boardrooms led Powell to trust the character of the average American businessman. That trust was reinforced by working alongside those clients in civic affairs. In Powell’s world, free enterprise and the businessmen who made it work were the foundation of strong communities. Free enterprise was a resource to be preserved, not a menace to be tamed. Character, not lawsuits, was the safeguard of the integrity of American capitalism. That trust in American business led Powell to read the securities laws— in all good faith—as setting down predictable rules that would allow business to proceed without undue interference or liability risk. These narrow readings reversed the trend in the Second Circuit and other lower courts to expand the securities laws. The securities laws experienced a counter-revolution, not as the result of a coup, but because of the commitments and intuitions derived from one person’s experience before becoming a justice.

Powell’s experience as a corporate lawyer gave him credibility when he called upon his colleagues to disagree with the position taken by the SEC, as he so often did. Having worked with the SEC from its earliest days, Powell recognized the departure that the agency’s aggressively expansionist tack represented. Agency expertise carried no weight
When the SEC came into court with newly-developed positions that conflicted with Powell’s understanding of well-established practice. The deference that the SEC had enjoyed in the Supreme Court before Powell’s confirmation evaporated. If there was any deference on the Court in securities cases, it was to Powell and his experience, not the SEC and its efforts to reshape the securities markets. As a result, the SEC’s winning percentage plummeted, particularly in the highest profile cases.

Powell’s experience did not always push him to oppose regulation. Powell was not naïve; he recognized that there were abuses in American business. His distaste for the abuse of trust that insider trading represented led him to read the common law of fraud broadly in Chiarella to make room for a prohibition under §10(b). The SEC’s “parity of information” position would have cracked down on this abuse more completely, but it went “too far” beyond any possible intention of Congress. While regulation of insider trading was warranted, it could not come at the expense of the law’s predictability.

A more significant departure from free market dogma was Powell’s profound suspicion of takeovers. Federal preemption, pushed by the SEC, was the most promising avenue for preserving a free market in corporate control. Powell’s distrust of that market led him to tolerate state regulation of takeovers, which invariably protected management. Here, too, his instincts were grounded in experience. Powell wanted to preserve space for local businesses and businessmen to contribute to the community in the way that he and his clients, people like Harvie Wilkinson, had done. Powell’s support for state efforts to discourage takeovers was consistent with his Federalist principles,
Making Powell’s position that much easier to defend. Powell shut the door to a free market in corporate control in CTS and corporate managers sleep better as a result.

Was Lewis Powell’s influence on securities law a good thing? One can disagree with the normative perspective that Powell brought to the interpretation of the federal securities law. Powell’s experience gave him expertise, but that expertise was infused with attitudes gained through nearly forty years of practice as a corporate lawyer. It seems unlikely that many justices consider the corporate bar the relevant audience for his or her work, as Powell did. The close connection between Powell’s attitudes and his readings of statutory text will trouble those who subscribe to formalist theories of statutory interpretation which require judges to be neutral readers. Realism seems to capture better the interpretive practice of the Supreme Court in the field of securities law. Perhaps another justice with a firmer belief in formalism would have greater success in separating his own views from his statutory readings. Powell’s emphasis on statutory text and structure in his opinions may have been a strategic device, intended to cabin the interpretive latitude of the lower courts rather than the Supreme Court.

The deference that Powell got from his colleagues due to his experience (and perhaps, their lack of interest) will trouble those who are sanguine about the role that private litigation may play in protecting investors and who are relatively unconcerned by the risk of SEC overreaching. Perhaps he trusted the character of the American businessman too much and the staff of the SEC too little. As Powell recognized, the

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548 The SEC was also apparently part of the relevant audience. See Memo to Paul Cane from L.F.P., Jr. (March 17, 1981) (“The SEC’s staff - and perhaps members of the Commission - will be interested in our opinion [in Naveen].”).
REPUTATION OF BUSINESS AND BUSINESSMEN HAS WAXED AND WANED THROUGHOUT AMERICAN HISTORY. THE PUBLIC’S REGARD FOR THE BUSINESS COMMUNITY IS AT A LOW EB今天的DUE TO EVENTS THAT WOULD HAVE APPALLED POWELL. ENRON AND THE ACCOUNTING SCANDALS THAT HAVE FOLLOWED IT MIGHT WELL HAVE SHAKEN HIS CONFIDENCE IN THE CHARACTER OF AMERICAN BUSINESSMEN, A CENTRAL PREMISE UNDERLYING HIS EFFORTS TO CABIN THE SECURITIES LAW.

POWELL’S SECURITIES LAW LEGACY, HOWEVER, DOES NOT REST SOLELY ON THE ATTITUDES THAT HE BROUGHT TO THAT WORK. POWELL’S PRESENCE ENSURED THAT THE COURT WOULD AVOID THE TEMPTATION TO NEGLECT THE HIGHLY TECHNICAL FIELD OF SECURITIES LAW, AS IT HAS DONE SINCE HIS RETIREMENT. MORE IMPORTANTLY, HIS INFLUENCE ENSURED THAT THE COURT’S WORK IN THE AREA WOULD AT LEAST BE SENSIBLE, IF NOT INVULNERABLE TO CRITICISM. SINCE POWELL’S RETIREMENT, THE COURT’S FORAYS INTO THIS AREA HAVE BEEN OCCASIONALLY IMPENETRABLE AND SOMETIMES BIZARRE. ON OTHER OCCASIONS THE COURT SIMPLY REGURGITATES THE PARTY LINE OFFERED BY THE SEC. OVERALL, “SCHOLARS AND LEARNED PRACTITIONERS ARE GIVING THE COURT’S SECURITIES LAW OPINIONS LOW GRADES FOR LOGIC, CLARITY, AND USEFULNESS IN FUTURE CASES.”

CRITICISMS OF THIS SORT CANNOT BE LEVELED AT POWELL’S WORK IN THE FIELD OF SECURITIES LAW. WHILE PRACTITIONERS AND SCHOLARS CAN QUARREL WITH PARTICULAR OUTCOMES, THE CASES DECIDED UNDER POWELL’S GUIDANCE CANNOT BE DESCRIBED AS INCOMPATIBLE WITH THE BASIC

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STRUCTURE OF THE SECURITIES LAWS AND CORPORATE PRACTICE. Powell ensured that the revolution in the securities laws that the Second Circuit had launched in the 1960s (with the Supreme Court’s encouragement) would not stifle the free enterprise in which Powell so fervently believed. Powell would take pride in his success as a counter-revolutionary.
APPENDIX
SUPREME COURT FEDERAL SECURITIES LAW DECISIONS AND CERTIORARI GRANTS
JANUARY 7, 1972 – JUNE 26, 1987

AMK = ANTHONY M. KENNEDY
AS = ANTONIN SCALIA
SOC = SANDRA DAY O’CONNOR
JPS = JOHN PAUL STEVENS
WHR = WILLIAM H. REHNQUIST
LFP = LEWIS F. POWELL, JR.
HAB = HARRY A. BLACKMUN
WEB = WARREN E. BURGER
TM = THURGOOD MARSHALL
BRW = BYRON R. WHITE
PS = POTTER STEWART
WJB = WILLIAM J. BRENNAN, JR.
WOD = WILLIAM O. DOUGLAS

JUSTICES WRITING OPINIONS ARE DESIGNATED BY BOLD AND CONCURRENCES ARE DESIGNATED BY ITALICS. JUSTICES VOTING TO “JOIN 3” FOR CERTIORARI ARE ALSO DESIGNATED BY ITALICS.

CERTIORARI: WJB, PS, BRW, HAB, LFP, JPS. MAJORITY: WEB, PS, BRW, LFP, WHR, JPS. DISSenting: WJB, TM, HAB.

CERTIORARI: WHR, LFP, HAB, BRW, WEB. MAJORITY: WHR, LFP, HAB, PS, WEB. DISSenting: WOD, WJB, BRW, TM.

BANKERS TRUST CO. v. MALLIS, 435 U.S. 381, No. 76-1359.
CERTIORARI: WHR, LFP, PS, WEB. MAJORITY: JPS, WHR (PER CURIAM), LFP, TM, BRW, PS, WJB, WEB. NOT PARTICIPATING: HAB.

BASIC, INC. v. LEVINSON, 485 U.S. 224, No. 86-279.
CERTIORARI: WJB, BRW, TM, HAB, LFP, JPS, SOC, AS. MAJORITY: WJB, TM, HAB, JPS. DISSenting (IN PART): BRW, SOC. NOT PARTICIPATING: WHR, AS, AMK.

BATEMAN EICHLER, HILL RICHARDS, INC. v. BERNER, 472 U.S. 299, No. 84-679.
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Certiorari: WEB, WJB, BRW, TM, HAB, LFP, WHR, JPS. Majority: WEB, WJB, BRW, HAB, LFP, WHR, JPS, SOC. Not participating: TM.


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CERTIORARI: WEB, WJB, HAB, LFP, WHR. MAJORITY: WEB, BRW, HAB, LFP, JPS, SOC.
Dissenting: WJB, TM, WHR.

E.I. duPont de Nemours and Co. v. Collins, No. 75-1870, 75-1872
Certiorari: WHR, LFP, HAB, PS, WEB. MAJORITY: JPS, LFP, HAB, TM, BRW, PS, WEB.
Dissenting: WJB. Not participating: WHR.

Eisen v. Carlisle & Jacquelin, U.S., No. 73-203
Certiorari: TM, PS, WJB, WOD. MAJORITY: LFP, WEB, PS, BRW, HAB, WHR. Dissenting: WJB, TM, WOD.

Ernst & Ernst v. Hochfelder, 425 U.S. 185, No. 74-1042.
Certiorari: WEB, PS, BRW, LFP, WHR. MAJORITY: WEB, PS, BRW, TM, LFP, WHR. Dissenting:
HAB, WJB. Not participating: JPS.

Certiorari: LFP, TM, BRW, WJB. MAJORITY: WHR, LFP, HAB, TM, BRW (except as to Part IV-C), PS, WJB, WEB. Not participating: JPS.

Gordon v. NYSE, 422 U.S. 659, No. 74-304.
Certiorari: TM, BRW, WJB, WOD. MAJORITY: WHR, LFP, BRW, HAB, TM, WOD, WEB, PS, WJB.

Gould v. Ruefenacht, 471 U.S. 701, No. 84-165
Certiorari: WJB, BRW, TM, HAB, LFP. MAJORITY: WEB, WJB, BRW, TM, HAB, LFP, WHR, SOC.
Dissenting: JPS.

Herman & MacLean v. Huddleston, 459 U.S. 375, Nos. 81-680, 81-1076.
Certiorari: WEB, WJB, BRW, LFP, WHR, SOC. MAJORITY: WEB, WJB, BRW, TM, HAB, WHR,
JPS, SOC. Not participating: LFP.

Certiorari: WEB, WJB, PS, BRW, TM, LFP, WHR. MAJORITY: WEB, WJB, PS, BRW, TM, HAB,
LFP, WHR, JPS.


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CERTIORARI: BRW, PS, WJB, WOD, WEB. MAJORITY: WHR, LFP, HAB, TM, BRW, WEB.
Dissenting: WOD, WJB, PS.

CERTIORARI: WEB, WJB, BRW, TM, HAB, LFP, JPS, SOC. MAJORITY: WEB, WJB, BRW, TM, HAB, LFP, WHR, SOC. Dissenting: JPS.

LEROY v. GREAT WESTERN UNITED CORPORATION, 443 U.S. 173, NO. 78-759.
CERTIORARI: PS, BRW, TM, LFP, WHR, JPS. MAJORITY: WEB, PS, HAB, LFP, WHR, JPS.
Dissenting: WJB, BRW, TM.

CERTIORARI: WJB, LFP, WHR, SOC. MAJORITY: WEB, WJB, BRW, TM, HAB, WHR, JPS, SOC. Not participating: LFP.

MARINE BANK v. WEAVER, 455 U.S. 551, NO. 80-1562.
CERTIORARI: PS, BRW, LFP, WHR, JPS. MAJORITY: WEB, PS, BRW, WJB, TM, HAB, LFP, WHR, JPS.

MERRILL LYNCH, PIERCE, FENNER & SMITH, INC. v. WARE, 414 U.S. 117, NO. 72-312.
CERTIORARI: LFP, TM, BRW, WJB, WEB. MAJORITY: WHR, LFP, HAB, TM, BRW, WJB, WOD, WEB. Not participating: PS.

PARKLANE HOSIERY CO. v. SHORE, 439 U.S. 322, NO. 77-1305.
CERTIORARI: WEB, PS, BRW, HAB, LFP, WHR, JPS. MAJORITY: WEB, WJB, PS, BRW, TM, HAB, LFP, JPS. Dissenting: WHR.

PINTER v. DAHL, 486 U.S. 622, NO. 86-805.
CERTIORARI: WHR, BRW, LFP, SOC. MAJORITY: HAB, WHR, WJB, BRW, TM, SOC, AS.
Dissenting: JPS. Not participating: AMK.

PIPER v. CHRIS-CRAFT INDUS., INC. 430 U.S. 1, NOS. 75-353, 75-354 AND 75-355.
CERTIORARI: JPS, WHR, LFP, BRW. MAJORITY: WHR, LFP, HAB, TM, BRW, PS, WEB. Dissenting: JPS, WJB.
RADZANOWER v. TOUCHE ROSS & CO., 426 U.S. 148, No. 75-268.
CERTIORARI: WHR, HAB, BRW, PS, WEB. MAJORITY: WHR, LFP, HAB, TM, BRW, PS, WJB. DISSenting: JPS.

CERTIORARI: WJB, BRW, TM, HAB, LFP, SOC. MAJORITY: WEB, BRW, TM, HAB, LFP, WHR, JPS, SOC. DISSenting: WJB.

RONDEAU v. MOSINEE PAPER CO., 422 U.S. 49, No. 74-415.
CERTIORARI: LFP, HAB, BRW, PS. MAJORITY: WHR, LFP, HAB, BRW, PS, WEB. DISSenting: WOD, WJB, TM.

RUBIN v. UNITED STATES, 449 U.S. 424, No. 79-1013.
CERTIORARI: WEB, PS, BRW, TM, LFP, WHR, JPS. MAJORITY: WEB, WJB, PS, BRW, TM, HAB, LFP, WHR, JPS.

SANTA FE INDUS., INC. v. GREEN, 430 U.S. 462, No. 75-1753.
CERTIORARI: JPS, WHR, LFP, HAB, TM, BRW, PS, WJB, WEB. MAJORITY: JPS, WHR, LFP, HAB, TM, BRW, PS, WEB. DISSenting: WJB.

SCHERK v. ALBERTO-CULVER CO., 417 U.S. 506, No. 73-781.
CERTIORARI: WHR, LFP, HAB, PS. MAJORITY: WHR, LFP, HAB, PS, WEB. DISSenting: TM, BRW, WJB, WOD.

SCHREIBER v. BURLINGTON NORTHERN, INC., 472 U.S. 1, No. 83-2129.
ARGUED JAN. 9, 1985. DECIDED JUNE 4, 1985
CERTIORARI: WJB, BRW, TM, HAB. MAJORITY: WEB, WJB, BRW, TM, HAB, WHR, JPS. NOT PARTICIPATING: LFP, SOC.

SECURITIES INVESTOR PROTECTION CORP. v. BARBOUR, 421 U.S. 412, No. 73-2055.
ARGUED MARCH 17, 18, 1975. DECIDED MAY 19, 1975.
CERTIORARI: WHR, LFP, BRW, PS, WEB. MAJORITY: WHR, LFP, HAB, TM, BRW, PS, WJB, WEB. DISSenting: WOD.

Justice Powell and the Counter-Revolution

Certiorari: WEB, BRW, TM, HAB, LFP, WHR, JPS, SOC. Majority: WEB, WJB, BRW, TM, HAB, LFP, WHR, JPS, SOC.

Certiorari: WEB, WJB, BRW, HAB, LFP. Majority: WEB, WJB, PS, BRW, TM, HAB, LFP, WHR, JPS.

Shearson/American Express, Inc. McMahon, 482 U.S. 220, No. 86-44.
Certiorari: WHR, WJB, BRW, TM, HAB, LFP, JPS, SOC. Majority: SOC, WHR, BRW, LFP, AS. Dissenting (in part): WJB, TM, HAB, JPS.

Steadman v. SEC, 450 U.S. 91, No. 79-1266
Certiorari: WJB, PS, BRW, TM, HAB, LFP, JPS. Majority: WEB, WJB, BRW, TM, HAB, WHR, JPS. Dissenting: LFP, PS.

Certiorari: WEB, BRW, HAB, LFP, WHR. Majority: JPS, WHR, HAB, BRW, WJB, PS, WEB. Dissenting: TM. Not participating: LFP.

Transamerica Mortgage Advisors, Inc. v. Lewis, 444 U.S. 11, No. 77-1645.
Certiorari: WEB, PS, HAB, LFP. Majority: WEB, PS, HAB, LFP, WHR. Dissenting: WJB, BRW, TM, JPS.

Certiorari: WHR, LFP, HAB, BRW, PS, WEB. Majority: WHR, LFP, HAB, TM, BRW, PS, WJB, WEB. Not participating: JPS.

Certiorari: WHR, LFP, HAB, BRW, PS, WEB Majority: WHR, LFP, HAB, TM, PS, WEB. Dissenting: WJB, WOD, BRW.

United States v. NASD, 422 U.S. 694, No. 73-1071.
Certiorari: WHR, LFP, HAB, TM, BRW, PS, WJB, WOD, WEB. Majority: WHR, LFP, HAB, PS, WEB. Dissenting: TM, BRW, WJB, WOD.
UNITED STATES, v. NAFTALIN, 441 U.S. 768, No. 78-561.
CERTIORARI: WEB, WJB, HAB, LFP, JPS. MAJORITY: WEB, WJB, PS, BRW, TM, HAB, WHR, JPS.
NOT PARTICIPATING: LFP.