We Must Never Forget That it is an Inkblot We Are Expounding: Section 10(b) as Rorschach Test

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WE MUST NEVER FORGET THAT IT IS AN INKBLOT WE ARE EXPOUNDING: SECTION 10(b) AS RORSCHACH TEST

Joseph A. Grundfest*

I. INTRODUCTION

A Rorschach test is a series of inkblots. Inkblots have no intrinsic meaning. They are inkblots. The patient describes images evoked by the inkblots. The analyst interprets the patient's descriptions.

Ideally, there would be no connection between Rorschach tests and the challenges posed by statutory interpretation. Ideally, Congress would draft clear statutes that provide precise guidance to the courts and to society.

We do not live in an ideal world. Congress often legislates with great imprecision. Sometimes the imprecision is inadvertent. Sometimes it is calculated. But whether imprecision is the consequence of oversight or design, when Congress compels the judiciary to interpret exceedingly vague or incomplete statutory language, Congress places the judiciary in the injudicious position of having to interpret a "legislative inkblot"—that is, a statutory utterance that has no intrinsic meaning but which must be plumbed for deeper consequence.

* Professor of Law, Stanford Law School. Commissioner, Securities and Exchange Commission, 1985-1990. I would like to thank Mel Eisenberg, Si Lorne, and Therese Maynard for provoking me to write this Article. Needless to say, I absolve them of responsibility, express or implied, for the views expressed herein.

2. EXNER, supra note 1, at 27-28; HUTT, supra note 1, at 395.
3. HUTT, supra note 1, at 395.
4. Id.
5. See, e.g., 136 CONG. REC. S9694 (daily ed. July 13, 1990) (statement of Sen. Armstrong complaining that vagueness in the Americans with Disabilities Act would create a "legislative Rorschach test, an inkblot whose meaning and significance will be determined through years of costly litigation").
The demand for judicial interpretation of legislative inkblots has spawned a cottage industry that generates rules, standards, and principles for the interpretation of vague or incomplete legislative language. Much of this literature is imaginative, well-reasoned, and carefully considered. But no matter how cogent, this literature cannot paper over the fact that many principles of statutory construction are, at root, efforts to impose meaning where there is none.

When a poorly drafted statute compels the judiciary to employ these interpretive principles, some academics rise and assume the mantle of Rorschachian analyst. They criticize the judicial interpretation of the statutory inkblot as passive, aggressive, neurotic, obsessive, controlling, vindictive, or worse, because the court’s interpretation of the blot differs from the academic analyst’s.

I have little interest in that game. Inkblots are inkblots. They should be treated as inkblots. When a statute presents itself as an inkblot, it should be construed as narrowly as practicable lest it become a breeding ground for competing judicial imaginations. To one Justice the blot is a cow. To another it is Mount Rushmore. Justices can defend their own interpretations of the blot by picking a suitable interpretive principle from a long list of plastic standards. Who is to say that any Justice is wrong when they are, after all, interpreting a blot? The winner in this debate is the Justice who rises to proclaim, “Stop! We must never forget that it is an inkblot we are expounding!”

Granted, reasonable minds can and will differ as to whether a particular statute is simply a difficult piece of abstract legislative expressionism with a discernible but nonrepresentational message, or whether it is an inkblot. In recognition of this problem, this Article

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7. I recognize that this proposal is itself a rule of statutory construction. However, as explained in part V, infra, I believe this rule is the one most reasonably applied and easily defended in the context of § 10(b).


9. With apologies to McCulloch v. Maryland, 17 U.S. (4 Wheat.) 316, 407 (1819) (Marshall, C.J.) (“[W]e must never forget that it is a constitution we are expounding.”).
draws no conclusions regarding categorical principles of statutory construction as they might apply to the vast majority of statutes. Nor is this Article a defense of strict textualism as an appropriate mode of statutory construction for a broad class of statutes.  

This Article's goal is far more modest. Its goal is to persuade the reader that in the wild and sometimes wacky world of statutory construction, when a statute presents itself as an inkblot, it should be construed as narrowly as practicable. Few statutes better warrant a narrow interpretation because of their inkblot characteristics than section 10(b) of the Securities Exchange Act of 1934 and rule 10b-5 promulgated thereunder. This support for narrow construction is rooted in straightforward institutional and pragmatic considerations. If a statute presents itself as an inkblot, then any attempt to fashion a broader interpretation inevitably relies on the subjective and unguided preference of the judiciary rather than the articulated guidance of the elected legislature. Indeed the task of defining the narrowest practical interpretation of an inkblot is difficult enough, and any broader charge simply provides fuel for more dramatically subjective controversy and confusion.

Few cases better illustrate section 10(b)'s inkblot characteristics than the cause of this Symposium, the Supreme Court's decision in Central Bank v. First Interstate Bank. Central Bank held that there is no implied private right of action against those who aid or abet a violation of section 10(b). This holding was contrary to the ruling of every court of appeals that had previously addressed the issue. Central Bank spawned a bitter storm of protest from some segments of the securities bar. The Court's holding "shocked lawyers who represent investors." Those lawyers bemoaned the decision as a

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10. See Eisenberg, supra note 6.
13. While Professor Eisenberg's critique of strict textualism is an attack on the Supreme Court's stated rationale in Central Bank, I do not read it as necessarily rejecting a principle of narrow interpretation in the face of a cryptic legislative utterance. Indeed, Professor Eisenberg articulates a policy-based rationale for construing § 10(b) to preclude aiding-and-abetting liability, but he does not endorse it. Eisenberg, supra note 6, at 20-22.
15. Id. at 1455.
16. Id. at 1456 n.1 (Stevens, J., dissenting) (collecting cases).
"travesty" and a “tragic day for investors.” The Court’s logic was denigrated as the consequence of a judicial “rigidity and callousness that is disconcerting.” The decision was also reviled as a “judicial wolf in sheep’s clothing, an act of extreme judicial activism carried out while purporting to employ the strictest possible interpretive means.” Whew.

This Article suggests that the critics of Central Bank are wrong. They are wrong to predict that Central Bank will significantly weaken the federal securities laws. They are also wrong to so harshly criticize the motives or logic of the Supreme Court’s decision. The federal securities laws in general, and section 10(b) in particular, are hardly models of clarity. Reasonable minds can differ as to the import of the section 10(b) inkblot, and honorable Justices strongly opposed to fraud in the nation’s securities markets can legitimately oppose limitless extensions of section 10(b)’s cryptic language. The Supreme Court’s holding in Central Bank that the implied section 10(b) right does not extend to private suits against aiders and abettors is hardly beyond the pale, and certainly not a cause for invective.

The Court’s critics would do well to remember that when they criticize Central Bank they criticize an interpretation of a cause of action that neither Congress nor the Securities and Exchange Commission ever intended to create. Moreover, interpreting the intent of the section 10(b) implied private right is an inherently quixotic exercise because, as the Court explained almost twenty years ago, there is no original intent to divine. Intentionalists in search of original meaning thus run into the problem that “there is no there there,” and would do just as well to kvetch about the ending of

18. Id. at A1 (quoting Arthur Bryant, executive director of the Trial Lawyers for Public Justice).
19. Id. (quoting Joseph Cotchett, “an attorney for the 23,000 bond holders who sued the lawyers and accountants of convicted savings and loan executive Charles H. Keating, Jr. and won $275 million”).
22. Section 10(b) “does not by its terms create an express civil remedy for its violation, and there is no indication that Congress, or the Commission when adopting Rule 10b-5, contemplated such a remedy.” Ernst & Ernst v. Hochfelder, 425 U.S. 185, 196 (1976).
23. Id.
Franz Schubert’s *Unfinished Symphony* as to complain about the interpretation of the contours of a cause of action that Congress never contemplated. Thus, to borrow Professor Eisenberg’s cogent admonition that text is insufficient because interpretation must consider “text in context,” the problem with section 10(b)’s implied private right is that its context is as vaporous as its text.

This Article takes a decidedly different approach to the debate over *Central Bank*. This Article argues that the federal securities laws in general, and section 10(b) in particular, pose inherently difficult interpretive challenges for the Court because they contain provisions that are cryptic in the extreme. This Article is a plea for compassion for nine Justices forced to interpret statutory provisions that are so complex, vague, and controversial that there is often no possible construction free of serious critique. This Article is also an argument in favor of a narrow approach to the interpretation of section 10(b), much like the approach adopted in *Central Bank*.

The threshold challenge in supporting a narrow interpretation of a statute on the grounds that it reads like an inkblot is to first reach the conclusion that the statute is indeed an inkblot. Part II of this Article supports the thesis that the federal securities laws have strong inkblot characteristics by presenting a statistical analysis demonstrating that the Court has split 5-4 in cases interpreting the federal securities laws with an unusually great frequency. Part II further demonstrates that these splits involve unusual and unstable coalitions,

25. FRANZ SCHUBERT, SYMPHONY IN B MINOR (1822).
26. Some musicologists suggest that Schubert’s Symphony in B minor—the Unfinished Symphony—is in fact complete. 16 THE NEW GROVE DICTIONARY OF MUSIC AND MUSICIANS 761 (Stanley Sadie ed., 1980). This minority view would no doubt be latched upon by intentionalists as the foundation for an extensive critique of the work’s ending.
27. Eisenberg, supra note 6, at 35 (emphasis in original).
28. Professor Maynard offers the hypothesis that the unusually high incidence of 5-4 decisions in cases construing the federal securities laws is the result of a clash between an evolving hostility to implied private remedies and a commitment to *stare decisis* which compels respect for decisions crafted in an earlier era when implied rights were found more easily and construed more broadly. Maynard, supra note 6, at 4 n.19. This explanation is not at all inconsistent with the “inkblot” explanation of section 10(b) jurisprudence because, in order for Professor Maynard’s hypothesized conflict to arise, there must first exist a more fundamental dispute over the meaning of the statute. Thus, instead of contradicting the “inkblot” hypothesis, Professor Maynard’s hypothesis provides a potential explanation for a mechanism that determines the tipping point that defines how the Supreme Court decides 10b-5 cases: The line dividing majority from minority is the line defined by the path-dependent balancing between the urge to respect *stare decisis* with the desire to construe implied rights as narrowly as possible.
and that unanimous decisions interpreting the federal securities laws are also unusually rare. As explained in greater detail below, these findings are sufficient but unnecessary statistics in support of the inkblot hypothesis as applied to the federal securities laws. They are sufficient because if the statute had a clearly discernible meaning it would not generate 5-4 splits more frequently than other matters presented to the Court. These statistics are not, however, necessary for a finding that a statute is an "inkblot" because even the most incoherent statute could generate a series of 9-0 decisions if the Court unanimously agreed on the interpretive principles to be applied to that otherwise incomprehensible statute.

Part III focuses on problems unique to section 10(b) jurisprudence and identifies seven distinct factors that make section 10(b) particularly difficult to interpret. These factors reasonably lead the Court to treat section 10(b) as if it were an inkblot and explain the unusual incidence of 5-4 decisions in section 10(b) cases. Part IV suggests that Central Bank's critics who complain that the decision does material harm to the integrity of the nation's securities markets have greatly exaggerated any realistic cause for concern.

Part V concludes with the observation that, while the Supreme Court's confusion and uncertainty over the interpretation of the federal securities laws is understandable, it is not desirable. The root cause of this confusion is, however, a Congress that has legislated ambiguously and then proven itself unable to clarify the ambiguities it has spawned. The Court is thus the victim of Congress's inarticulate locution and not the cause of the confusion. Indeed, if the Court must continue interpreting the enigmatic section 10(b) implied private right, the Court can reasonably and prudently extend Central Bank's narrow, textualist reading of the statute. Such an approach is preferable to the inkblot game the Court is forced to play whenever it embarks on a search for meaning that is not there.

II. Divided Courts and Unstable Coalitions: Empirical Evidence That the Federal Securities Laws Are Construed as Though They Are Inkblots

Suppose we want to test the hypothesis that the federal securities laws in general, and section 10(b) in particular, are perceived by the Supreme Court as inkblots—statutory utterances with few clearly discernible meanings, subject to sharply differing interpretations, and lacking organizing principles in text or context that provide consistent or coherent rules of construction. What pattern of Supreme Court decision-making would we then expect to observe?

It should be sufficient to observe a higher than normal incidence of sharply split decisions involving the formation of unstable and unusual coalitions. In the absence of any clear statutory meaning or intent, the Justices should be expected to split almost randomly over the images they perceive in the statutory blots. The Justices should also be expected to form coalitions that do not correlate with coalitions formed in debates involving well-defined issues of principle. In addition, we should also observe an unusually low incidence of unanimous decisions as the Justices find uniform consensus relatively difficult to achieve.

A. The Evidence from 5-4 Split Decisions and Unanimous Decisions

The data are consistent with the inkblot hypothesis. Even on a Court known for the incidence of 5-4 split opinions, decisions interpreting the federal securities laws are stunning for the frequency with which they are decided by the narrowest of margins. Table 1 lists major Supreme Court decisions interpreting the federal securities laws from 1987 to date. It also reports the margins by which the cases were decided, and describes the composition of the majorities and minorities in each case. Of the twelve decisions catalogued in Table 1, seven (58.3%) were decided by a margin of 5-4. One (8.3%) resulted in an evenly split court. One (8.3%) was decided by a plurality. One (8.3%) was decided by a unanimous court. The sole

30. See supra note 28 and accompanying text.
31. Appendix A describes the construction of Table 1. Votes in several cases can be counted in a variety of ways but, as explained in notes 35-41, infra, the conclusions presented in the text are robust with regard to these alternative classifications.
TABLE 1
Margins and Voting Patterns in Major Supreme Court Decisions

<table>
<thead>
<tr>
<th>DECISION</th>
<th>YEAR</th>
<th>VOTE</th>
<th>JUSTICES IN MAJORITY*</th>
<th>JUSTICES IN MINORITY*</th>
<th>NOT VOTING</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gustafson v. Alloyd</td>
<td>1995</td>
<td>5-4</td>
<td>Kennedy, Rehnquist, Stevens, O'Connor, Souter</td>
<td>Thomas, Scalia, Ginsburg, Breyer</td>
<td></td>
</tr>
<tr>
<td>Central Bank</td>
<td>1994</td>
<td>5-4</td>
<td>Kennedy, Rehnquist, O'Connor, Scalia, Thomas</td>
<td>Stevens, [Blackmun], Souter, Ginsburg</td>
<td></td>
</tr>
<tr>
<td>Musick Peeler</td>
<td>1993</td>
<td>6-3</td>
<td>Kennedy, Rehnquist, [White], Stevens, Scalia, Souter</td>
<td>Thomas, [Blackmun], O'Connor</td>
<td></td>
</tr>
<tr>
<td>Lampf Pleva</td>
<td>1991</td>
<td>5-4</td>
<td>[Blackmun], Rehnquist, [White], [Marshall], Scalia</td>
<td>Stevens, Souter, O'Connor, Kennedy</td>
<td></td>
</tr>
<tr>
<td>Gollust v. Mendell</td>
<td>1991</td>
<td>9-0</td>
<td>Souter, Rehnquist, [White], O'Connor, Scalia</td>
<td>Kennedy, [Marshall], [Blackmun], Stevens</td>
<td></td>
</tr>
<tr>
<td>Virginia Bank-shares (Causation under § 14(a))</td>
<td>1990</td>
<td>5-4</td>
<td>Souter, Rehnquist, [White], O'Connor, Scalia</td>
<td>Kennedy, [Marshall], [Blackmun], Stevens</td>
<td></td>
</tr>
<tr>
<td>Reves v. Ernst &amp; Young (9 month provision)</td>
<td>1990</td>
<td>5-4</td>
<td>[Marshall], [Brennan], [Blackmun], Stevens, Kennedy</td>
<td>Rehnquist, White, O'Connor, Scalia</td>
<td></td>
</tr>
<tr>
<td>Pinter v. Dahl</td>
<td>1988</td>
<td>7-1</td>
<td>[Blackmun], Rehnquist, [Brennan], [White], [Marshall], O'Connor, Scalia</td>
<td>Stevens</td>
<td>Kennedy</td>
</tr>
<tr>
<td>Basic v. Levinson</td>
<td>1988</td>
<td>4-2</td>
<td>[Blackmun], [Brennan], [Marshall], Stevens</td>
<td>[White], O'Connor</td>
<td>Scalia, Rehnquist, Kennedy</td>
</tr>
<tr>
<td>Shearson v. McMahon</td>
<td>1987</td>
<td>5-4</td>
<td>O'Connor, Rehnquist, White, [Powell], Scalia</td>
<td>[Blackmun], [Brennan], [Marshall], Stevens</td>
<td></td>
</tr>
<tr>
<td>Carpenter (Securities law violation)</td>
<td>1987</td>
<td>4-4</td>
<td>Undisclosed</td>
<td>Undisclosed</td>
<td></td>
</tr>
</tbody>
</table>

* Justices no longer sitting on the Court are denoted in brackets.
unanimous decision, *Gollust v. Mendell*, involved the interpretation of section 16(b) of the Securities Exchange Act of 1934. In sharp contrast to the vague language of section 10(b), section 16(b) is quite detailed, and in interpreting section 16(b) the Court has been able to follow a "literal, 'mechanical' application of the statutory text in determining who may be subject to liability." No such literal or mechanical application is possible for section 10(b).

In the aggregate, nine of the twelve decisions (75.0%) were by the narrowest of possible margins or by plurality. Only three of twelve decisions (25.0%) were decided by majorities that could have lost even one vote and still prevailed as majorities.

These data are remarkable. During the period covered by Table 1—the 1986 through 1994 Terms—21.3% of the Court’s decisions were decided by margins of 5-4. In the recently completed 1994

<table>
<thead>
<tr>
<th>Term</th>
<th>All Cases</th>
<th>5-4 Cases</th>
<th>% 5-4</th>
</tr>
</thead>
<tbody>
<tr>
<td>1986*</td>
<td>152</td>
<td>47</td>
<td>30.9%</td>
</tr>
<tr>
<td>1987*</td>
<td>142</td>
<td>32</td>
<td>22.5%</td>
</tr>
<tr>
<td>1988*</td>
<td>143</td>
<td>34</td>
<td>23.8%</td>
</tr>
<tr>
<td>1989*</td>
<td>137</td>
<td>42</td>
<td>30.7%</td>
</tr>
<tr>
<td>1990*</td>
<td>121</td>
<td>23</td>
<td>19.2%</td>
</tr>
<tr>
<td>1991**</td>
<td>114</td>
<td>14</td>
<td>12.3%</td>
</tr>
<tr>
<td>1992**</td>
<td>114</td>
<td>18</td>
<td>15.8%</td>
</tr>
<tr>
<td>1993**</td>
<td>87</td>
<td>13</td>
<td>14.9%</td>
</tr>
<tr>
<td>1994***</td>
<td>82</td>
<td>18</td>
<td>22.0%</td>
</tr>
<tr>
<td>TOTAL</td>
<td>1,092</td>
<td>241</td>
<td>21.3%</td>
</tr>
</tbody>
</table>

* These data describe 5-4 decisions as a percentage of cases decided by full opinion and are as reported in Robert E. Riggs, *When Every Vote Counts: 5-4 Decisions in the United States Supreme Court*, 21 HOFSTRA L. REV. 667, 712 Table I (1993).

term, 22.0% of all cases were decided by a margin of 5-4. The peak frequency of 5-4 decisions was reached in 1986 when 30.9% of all cases decided by a full opinion were by votes of 5-4.

By this yardstick, 5-4 decisions in cases interpreting the federal securities laws since 1986 are almost twice as frequent as the peak incidence of 5-4 decisions in any single term in the history of the Supreme Court. They are almost three times more frequent than the incidence of 5-4 decisions in the Court's overall docket since 1986.

This pattern of closely split decision-making is highly significant in a statistical sense. The probability of drawing seven or more 5-4 decisions from a random sample of twelve Supreme Court opinions is less than four-tenths of one percent.36 If 4-4 and plurality decisions are counted as 5-4 decisions, then the probability of drawing nine or more such decisions from a random sample of twelve Supreme Court opinions is below four-tenths of one percent.36

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36. These probabilities are calculated on the assumption that 20% of Supreme Court decisions are not by 5-4 margins and that the binomial distribution applies to the suggested experiment—that is, that the probability of drawing at least seven 5-4 decisions from a random sample of Supreme Court decisions of which 20% are decided by 5-4 margins, is analogous to the probability of drawing from a sequence of binary random, independent, and identically distributed variables with a distribution identical to that observed in 5-4 Supreme Court decisions from the 1986 through 1994 terms. See generally, MICHAEL O. FINKELSTEIN & BRUCE LEVIN, STATISTICS FOR LAWYERS 111-15 (1990) (explaining the derivation and application of the binomial distribution).

The use of the 20%-assumption is to approximate the actually observed 21.3% probability and to conform with generally available statistical tables.

The cumulative probabilities associated with such decisions for a range of distributional parameters surrounding the observed data are as follows:

| Number of 5-4, 4-4, or Plurality Votes Drawn from a Sample of Twelve Decisions | Assumed Cumulative Probability |
|---|---|---|
|   | 15% | 20% | 25% |
| Nine | .0000 | .0001 | .0004 |
| Eight | .0001 | .0006 | .0028 |
| Seven | .0007 | .0039 | .0143 |
| Six | .0046 | .0194 | .0544 |
| Five | .0239 | .0726 | .1576 |

**Id. at 542-43 Table B.**
Court opinions is in the range of one-hundredth of one percent. If the cases are construed as generating only five 5-4 opinions out of twelve, then the probability of drawing five or more such decisions from a random sample of twelve Supreme Court decisions is approximately 7.26%. I present this range of statistical estimates because reasonable minds can differ as to the categorization of specific votes described in Table 1, and because I have no data describing the incidence of 4-4 and plurality decisions. The statistics suggest, however, that no matter how one slices the data, narrow margins are far more common in cases interpreting the federal securities laws than in the Court's docket as a whole, and that this difference is not the result of mere chance.

If the incidence of 5-4 splits is subdivided to distinguish between cases deciding constitutional issues and cases deciding questions of statutory construction or of common law, the tendency toward 5-4 splits in cases construing the federal securities laws is all the more remarkable. A study by Judge Easterbrook suggests that "[c]onstitutional cases produce significantly more disagreement than statutory cases." He explains this pattern, in part, by suggesting that "Justices have more discretion in constitutional than in statutory cases because of the age and vagueness of the [Constitutional] text." If the pattern found by Judge Easterbrook continues to hold true beyond his sample period, then the securities laws are all the more remarkable because they appear to have achieved a level of vagueness more comparable to questions of constitutional construction than to questions of statutory interpretation.

Moreover, if the inkblot hypothesis is correct as applied to the federal securities laws, then we should also observe a lower than normal incidence of unanimous decisions in cases interpreting the federal securities statutes. In the nine terms spanning 1986-1987 through 1994-1995, an average of approximately 37.1% of all decisions

37. Id. This estimate is not exact because it does not adjust sample statistics to account for the aggregate incidence of 4-4 and plurality decisions, but such decisions are relatively rare and are not likely to change the closest estimate of cumulative probability incidence from 20%. Even if the cumulative probability increased to 25%, the probability of drawing nine of twelve such cases would be only four-hundredths of one percent.

38. This count results if Virginia Bankshares, Inc. v. Sandberg, 501 U.S. 1083 (1991), and Reves v. Ernst & Young, 494 U.S. 56 (1990), are construed as not being 5-4 decisions.


40. Id. at 391.
were by a unanimous court, with or without separate concurrences.\textsuperscript{41} During the same period, only one of twelve—8.3%—of the decisions interpreting the federal securities statutes was unanimous. The probability of there being only one such decision of twelve in a population containing 35% unanimous decisions is less than one-half of one percent.\textsuperscript{42} The relatively rare incidence of unanimous decisions interpreting the federal securities laws provides further support for the inkblot hypothesis.

B. The Evidence from Unusual and Unstable Coalitional Patterns

As would be expected when voting on the meaning of inkblots, close decisions interpreting the federal securities laws are often the result of unusual and unstable coalitions. Consider, for example, the four Justices in the \textit{Gustafson v. Alloyd Co.} dissent.\textsuperscript{43} Justices Scalia and Thomas are most frequently viewed as the "right wing" of the Court.\textsuperscript{44} Justices Ginsburg and Breyer are often viewed as leaning toward the Court's "left wing."\textsuperscript{45} It is difficult to conceive of a general or coherent judicial or political philosophy that would draw these four Justices as natural adherents. Indeed, during the 1994 term, Justices Ginsburg and Breyer were least likely to agree with Justice Thomas, the author of the \textit{Gustafson} dissent in which they joined.\textsuperscript{46} No other decision in the 1994 term drew Justices Scalia, Thomas, Ginsburg, and Breyer as members of the minority.\textsuperscript{47} Such an unlikely coalition is most easily formed when there is no clear principle at stake. The lack of a clear principle at stake is a characteristic common to the interpretation of inkblots.\textsuperscript{48}

Longer-term voting patterns by Justices Kennedy, O'Connor, Souter, and Stevens reinforce the same point. Justice Kennedy authored the majority opinions in \textit{Musick, Peeler & Garrett v.}
Employers Ins. of Wassau, Central Bank, and Gustafson, the three most recent Supreme Court decisions interpreting the federal securities laws. Justice Kennedy's decisions in Gustafson and Central Bank limit the scope of plaintiffs' ability to prevail in securities fraud actions. Those decisions have been criticized as overly crabbed and narrow interpretations of the federal securities laws. Yet, in Lampf, Pleva, Lipkind, Prupis & Pettigrow v. Gilbertson and Virginia Bankshares, Inc. v. Sandberg, Justice Kennedy wrote for minorities supporting more expansive, pro-plaintiff interpretations of the federal securities laws. Justice Kennedy's critics would do well to remember that the Justice they criticize for limiting plaintiffs' rights in Gustafson and Central Bank is also the Justice they should applaud for trying to protect plaintiffs' rights in Lampf, Pleva and Virginia Bankshares.

Justices O'Connor, Stevens, and Souter also appear inconsistently among members of the majority and minority in recent securities law cases. As shown in Table 1, while Justice O'Connor was in the

49. 113 S. Ct. 2085 (1993).
50. See supra Table 1.
55. Lampf, Pleva, 501 U.S. at 374-78 (Kennedy, J., dissenting) (criticizing the majority's adoption of a limited three-year period of repose for SEC § 10(b) actions and stating that § 10(b) violations commonly go undiscovered for long periods of time); Virginia Bankshares, 501 U.S. at 1114-16 (Kennedy, J., dissenting) (criticizing the majority's standard of proof for nonvoting causation in § 14(a) actions as too limiting). Justice Kennedy's majority opinion in Musick, Peeler is more difficult to categorize. That opinion contains elements reinforcing the Court's earlier expansive approach to interpreting the securities laws, although plaintiffs might actually prefer a rule that prohibits contribution because such a rule could be used to increase settlement pressure on more solvent defendants. See Roberts, supra note 21, at 1262; see also Richard L. Jacobson, Shining a Lampf on Section 10(b) Limitations Periods, INSIGHTS, Mar. 1992, at 12 (asserting that Justice Kennedy criticized the standard for § 10(b) claims set forth in Lampf, Pleva because it was "unreasonably short" and made § 10(b) useless to injured investors); S. Scott Luton, The Ebb and Flow of Section 10(b) Jurisprudence: An Analysis of Central Bank, 17 U. ARK. LITTLE ROCK L.J. 45, 46 n.2 (1994) (stating that Justice Kennedy's approach in Central Bank was more restrictive than in Virginia Bankshares).
56. Carrying the analysis back farther in time with regard to coalition formation on the current Court becomes problematic because at least four of the then-sitting Justices from earlier cases no longer serve on the Court.
majority in *Gustafson, Central Bank, and Virginia Bankshares*, she was in the minority in *Reves v. Ernst & Young*, *Musick, Peeler, and Lampf, Pleva.* Justice Stevens was in the majority in *Gustafson, Musick, Peeler, and Reves*, but found himself in the *Central Bank, Lampf, Pleva, and Virginia Bankshares* minorities. Justice Souter was in the *Gustafson, Musick, Peeler, and Virginia Bankshares* majorities, but in the *Central Bank and Lampf, Pleva* minorities. The track records of Justices Thomas, Ginsburg, and Breyer appear too short to troll for patterns.

The only meaningful regularity appears to emanate from the Chief Justice and Justice Scalia. Chief Justice Rehnquist has been in the majority in every case in which he has participated except *Reves*. The Chief Justice's batting average in those cases, nine majorities out of ten, is a stunning 90.0%. Justice Scalia has also been a consistent member of Court majorities, missing out on only two of the ten cases in which his vote is reported—*Gustafson* and *Reves*. Justice Scalia's batting average in these cases is a healthy 80.0%. This high correlation between the Chief Justice and Justice Scalia is consistent with broader voting patterns.

What are we to make of these generally chaotic coalitional patterns? At one level, this sort of coalitional analysis is simply too reductionist to support an inference regarding the interpretive philosophy of any individual member of the Court, with the possible exception of the Chief Justice and Justice Scalia, who display a high regularity in voting patterns. Indeed, closer examination of individual Justice's rationales in deciding specific cases can discern logical patterns of statutory construction over time. From these

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58. See supra Table 1.
59. See supra Table 1.
60. See supra Table 1.
61. See supra Table 1.
62. See, e.g., Coyle, supra note 35, at C2 (noting that Chief Justice Rehnquist is most likely to agree with Justice Scalia in civil cases).
64. For example, Justice Kennedy's opinions in *Gustafson, Central Bank, Musick, Peeler, Lampf, Pleva, and Virginia Bankshares* generally display a two-step approach to the interpretation of the federal securities laws. First, Justice Kennedy considers evidence that the language or history of the statute supports a particular interpretation, or that such interpretation is necessary for the practical effectuation of the statute. If this analysis suggests that a right should be implied or that a particular interpretation should be
patterns it is possible to argue that the federal securities laws have a consistent but individualized meaning to many of the Justices. However, these individualized interpretations tend neither to cohere, nor to persuade, to the extent of forming stable blocks capable of drawing more than two Justices with any regularity.

Accordingly, individual Justices may well possess fully formed and internally consistent approaches to the interpretation of the federal securities laws, but these individual approaches are like private languages that are not broadly shared by other members of the Court. When the Court operates as a collective body forced to resolve questions of statutory interpretation involving the federal securities laws, the result is a curious and inconsistent series of coalitions that suggest no clear, collectively shared meaning in the statute at all. 14

III. THE PATH FROM STATUTE TO INKBLOT: REASONS WHY SECTION 10(b), IN PARTICULAR, IS INTERPRETED AS THOUGH IT IS A BLOT

The observation that Supreme Court voting patterns are consistent with the inkblot hypothesis is buttressed by historical analysis of the section 10(b) implied private right of action. The history of the Court’s interpretation of section 10(b) is replete with curiosities and contradictions, and there are at least seven distinct factors that contribute to legitimate confusion over the statute’s meaning. These factors provide good reason for the statute to be perceived as a blot.

First, when Congress enacted section 10(b), it did not anticipate that it was creating a private remedy. 15 The statutory language and adopted, then Justice Kennedy “triangulates” to find the statutory provision or principle clearly established in the law that most closely resembles the provision created. No doubt, other Justices following the same formula can—and do—reach different conclusions, but Justice Kennedy cannot fairly be accused of being intentionally inconsistent in his approach to the interpretation of federal securities laws.

65. This result is akin to a cyclic voting pattern in which each voter has a rational and consistent set of preferences which, when aggregated through a majority voting rule, gives rise to seemingly irrational or indecisive outcomes. For an example of such cycling in a legislative context, see Eskridge, supra note 8, at 34-38; see also Kenneth J. Arrow, Social Choice and Individual Values 2-3 (2d ed., Yale Univ. Press (1973) (1951)) (exploring whether it is possible to create a method for “passing from individual to collective tastes”).

66. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 196 (“Section 10(b) does not by its terms create an express civil remedy for its violation, and there is no indication that Congress, or the Commission when adopting Rule 10b-5, contemplated such a remedy.”)
legislative history are therefore totally silent as to the contours of the private right.\textsuperscript{67} Intentionalist analysis runs headlong into the problem that there is no intent to analyze when it comes to discerning the contours of the section 10(b) implied private right of action. This is not a small problem.

Second, section 10(b) is not self-executing.\textsuperscript{68} It is a delegation of authority to the SEC.\textsuperscript{69} Rule 10b-5 is an exercise of that delegated authority.\textsuperscript{70} At no time in the adoption of rule 10b-5 did the Commission consider the possibility that it was aiding and abetting the creation of a private right of action.\textsuperscript{71} The record is instead crystal clear that the Commission adopted rule 10b-5 for reasons wholly unrelated to any desire to create an implied private right of action.\textsuperscript{72} No doubt, the Commission has subsequently urged the broadest possible interpretation of the implied private right that it never intended to create in the first instance.\textsuperscript{73} Those efforts, however, have been uniformly rejected by the Supreme Court as \textit{ultra vires} interpretations of the delegated statutory authority.\textsuperscript{74} The Court's tendency to reject the Commission's expansionary interpretations of section 10(b) also predates by many years its perceived recent shift to post-\textit{Chevron}\textsuperscript{75} textualism.\textsuperscript{76} Intentionalists advocating a broad construction of the implied private right therefore cannot even find support in the original intent of the agency that adopted the regulation at issue. They must instead wrestle with a substantial body of precedent suggesting that the agency has a tendency to construe its authority under section 10(b) far too generously.

Third, while the Supreme Court states that the section 10(b) implied private right is "beyond peradventure,"\textsuperscript{77} the Court has

\footnotesize{(citations omitted).}

\textsuperscript{67} See S. Rep. No. 792, 73d Cong., 2d Sess. 5-6 (1934).
\textsuperscript{68} Ernst & Ernst, 425 U.S. at 213-14.
\textsuperscript{69} Id.
\textsuperscript{70} Id. at 195.
\textsuperscript{72} Ernst & Ernst, 425 U.S. at 196.
\textsuperscript{73} Id. at 198; see also Central Bank v. First Interstate Bank, 114 S. Ct. 1439, 1447 (1994).
\textsuperscript{74} Louis Loss & Joel Seligman, \textit{Securities Regulation} 4332-38 (3d ed. 1989).
\textsuperscript{76} See, e.g. Pierce supra note 63.
never explained why the right exists. Absent an articulated rationale for the existence of such an implied private right, it is trivially easy to argue about the ultimate reach of the unexplained cause of action.

Fourth, while the lower courts have articulated a variety of rationales in support of an implied private 10(b) right of action, the Court has explicitly rejected each of those rationales. Lower court decisions therefore provide no contemporaneously useful analytic guidance regarding the theoretical foundation for section 10(b)’s implied right. The implied section 10(b) private right of action seems to float without foundation in the intellectual air.

Fifth, in the almost fifty years since the implied section 10(b) private right was initially recognized, the doctrine governing the implication of private rights has been radically transformed. The emphasis now is on whether Congress intended to create an implied private right, and we already know that Congress never expressed such an intention. Therefore, if the question were to arise on a clean slate, it is improbable in the extreme that the Court today would imply the section 10(b) private right.

Sixth, Congress has remained silent as to the scope of the section 10(b) implied private right. Silence begets confusion. Those who support the implied section 10(b) private right interpret silence as acquiescence. Others draw no inference from the silence, recognizing that inaction can be a symptom of failure to agree on an alternative rather than a sign of support for the status quo. In any event, the debate over the implications of congressional inaction regarding section 10(b) underscores the difficulty in drawing any inference from congressional inaction regarding the interpretation of any statute.

Seventh, congressional intent is far from stable over time. The interpretation of section 10(b) that would be supported by today’s Republican-dominated Congress is likely quite different from the interpretation that would have been supported by last year’s or last

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78. See Grundfest, supra note 71, at 985-88.
79. Id. at 988-91.
81. See, e.g., Central Bank, 114 S. Ct. at 1457 (Stevens, J., dissenting) (“Our approach to implied causes of action, as to other matters of statutory construction, has changed markedly since the Exchange Act’s passage in 1934.”). See also supra note 28; Maynard, supra note 6, at 4 n.19.
82. See Grundfest, supra note 71, at 986-89.
83. Central Bank, 114 S. Ct. at 1442.
decade's Democrat-dominated Congress. Intentionalists thus confront the uncomfortable problem that, if they look to the intent of the Congress that in 1934 enacted section 10(b) they find no guidance, but if they look to the intent of subsequent Congresses they can infer sharply conflicting guidance depending on where their intentionalist time machines stop along the way.

In sum, the implied section 10(b) private right was never intended at inception by Congress or by the Commission, has never been explained by the Supreme Court, has no currently viable explanation in any Supreme Court or lower court opinion, would probably not exist if presented to the Court on a clean slate, has not been clarified by congressional action subsequent to 1934, and would likely be subject to differing interpretations by subsequent Congresses. The implied section 10(b) private right of action thus exists as an unexplained and inexplicable anachronism—a vestige of an earlier era in which private rights were more easily implied, but even then not so easily defined or explained.

All of these factors contribute to honest and legitimate confusion over the meaning of the statute and uncertainty over the outer limits of the implied private right's reach. All of these factors also make it reasonable for the Court to perceive section 10(b) as though it is an inkblot that lacks clear, inherent meaning. The high incidence of split decisions and of unstable coalitions exist for good reason and not out of lack of care, obstinacy, or contrariness on the part of the Court.

IV. CENTRAL BANK'S PRACTICAL SIGNIFICANCE IS OVERSTATED

The controversy engendered by Central Bank's narrow interpretation of the section 10(b) inkblot is all the more remarkable for the predictions of doom that followed in the opinion's wake.84 The suggestion that fraudsters would celebrate Central Bank as a license to pillage and plunder is exaggerated for several reasons.

First, as the Court itself explained:
The absence of § 10(b) aiding and abetting liability does not mean that secondary actors in the securities markets are always free from liability under the securities Acts. Any person . . . may be liable as a primary violator under 10b-5, assuming all of the requirements for primary liability under

84. See supra text accompanying notes 17-21.
Rule 10b-5 are met. In any complex securities fraud, moreover, there are likely to be multiple violators.\textsuperscript{85} Courts historically have paid scant attention to the distinction between primary and secondary liability under section 10(b) because little hinged on that categorization.\textsuperscript{86} Now, however, that the distinction is critical, the courts are finding that much conduct that had traditionally been denominated as aiding and abetting can also be prosecuted as a primary violation.\textsuperscript{87} Real “bad guys” therefore find no comfort in \textit{Central Bank} because they are now successfully prosecuted as primary violators. The only defendants who may now find that they are immune from section 10(b) liability—but not necessarily from liability under state law—are the remote, fringe participants in, or bystanders to, a securities fraud. Eliminating those defendants from the process is unlikely to threaten the core values of the federal securities laws.

Second, even if \textit{Central Bank}'s holding is extended to preclude aiding and abetting prosecutions by the SEC,\textsuperscript{88} the Commission has available to it a rich arsenal of alternative enforcement tools that it can use to reach wrongdoers who are not primary violators of section 10(b).\textsuperscript{89} The Commission has said as much,\textsuperscript{90} and \textit{Central Bank} will

\begin{itemize}
\item \textsuperscript{85} \textit{Central Bank}, 114 S. Ct. at 1455 (citations omitted).
\item \textsuperscript{86} Edward Brodsky, \textit{Aiding and Abetting Claims Under Rule 10b-5}, N.Y. L.J., June 14, 1995, at 3.
\item \textsuperscript{87} Id.
\item \textsuperscript{88} For an excellent description of the debate over whether \textit{Central Bank} can, should, or already has been extended to preclude Commission enforcement actions alleging aiding and abetting, see Edward C. Brewer, III & John L. Latham, \textit{SEC v. Central Bank: A Draft Opinion for the Court's Conference}, 50 Bus. Law 19 (1994) (responding to Lorne, infra, and describing an argument that the Supreme Court could rely upon to extend its \textit{Central Bank} holding to preclude Commission enforcement proceedings under § 10(b)); Simon M. Lorne, \textit{Central Bank of Denver v. SEC}, 49 Bus. Law. 1467 (1994) (describing an alternative argument that the Supreme Court could rely upon to limit its \textit{Central Bank} holding to private implied rights). A recent decision held that \textit{Central Bank} does, in fact, preclude SEC enforcement proceedings alleging aiding and abetting violations of § 10(b). SEC v. United States Envtl., Inc., No. 94 Civ. 6608, (S.D.N.Y. filed Sept. 13, 1994). The same question is currently pending before the Ninth Circuit in SEC v. Fehn, No. 94-16136 (9th Cir. filed May 6, 1994).
\item \textsuperscript{89} See, e.g., Bettina M. Lawton & Catherine Botticelli, \textit{New Weapon in the SEC's Arsenal}, Bus. L. TODAY, July-Aug. 1995, at 34, 35-36 (discussing § 21C of the Securities Exchange Act of 1934, which allows the SEC to “obtain a cease-and-desist order against . . . any . . . person that is, was, or would be a cause of [a] violation, due to an act or omission the person knew or should have known would contribute to”’ a breach of rule 10b-5) (quoting 15 U.S.C. § 78u-3(a) (1994)).
\item \textsuperscript{90} \textit{Abandonment of the Private Right of Action for Aiding and Abetting Securities Fraud: Staff Report on Private Securities Litigation}, 103d Cong., 2d Sess. 13-14 (1994)
\end{itemize}
therefore steal little thunder from the Commission's ongoing campaign to stamp out fraud in the securities markets.

V. CONCLUSION

We are thus left with much wailing and wearing of sackcloth over a Supreme Court opinion whose holding will have little material effect on the future course of securities law enforcement. The theories of some prosecutions may change, but the practical outcome of many cases will likely not be affected.

So what's the big deal? The big deal is that in Central Bank a majority of the Supreme Court adopted a strict-textualist approach to section 10(b). To supporters of a broad, expansionary interpretation of the implied section 10(b) private right of action, this mode of analysis sounds a death knell for anything but the narrowest statutory interpretations that can be directly supported by the statutory language. To these observers, the real danger in Central Bank is not the holding in that case, but the holding that might result from the next decision rendered pursuant to Central Bank's logic.

But what are the alternatives? Should the Court set out to speculate over an intention that we knew was never even contemplated by Congress? If so, from where should the Court obtain its guidance? Or, should the Court simply conclude that section 10(b)'s reach is unconstrained and thus expand the statute as far as possible on the theory that no fraud is a good fraud? Such an expansion of liability would, however, run roughshod over the explicit statutory provisions contained in the Securities Act and the Securities Exchange Act that establish a host of due diligence and other defenses to liability under the federal securities laws.

Indeed, Professor Eisenberg's preferred policy-based rationale for deciding Central Bank stands as a valuable illustration of the intractable problems that arise once a court abandons a narrow interpretation of section 10(b), whether that interpretation is rooted in strict textualism or in some other interpretative doctrine.91 Under Professor Eisenberg's proposed decision rule, the Court would consider empirical data describing the various costs and benefits generated by a rule that imposes aiding-and-abetting liability under

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91. Eisenberg, supra note 6, at 20-22.
The result of this policy-based analysis would be historically contingent and subject to vehement debate. In particular, the answer to the question, "is there aiding-and-abetting liability for violations of section 10(b)?" would depend on the data available at the time the question is asked, the Court's subjective evaluation of those data, and the Court's subjective balancing of the costs and benefits suggested by those data. All of this overt legislating from the bench would, moreover, be justified in the name of potentially expanding a cause of action that neither Congress nor the Commission contemplated creating in the first instance.

No doubt, strict textualism suffers from a host of serious flaws, but so does every rule for interpreting a statute that presents itself as an inkblot. In order to avoid these intractable interpretive difficulties, the best the Court can do is adopt an avowedly narrow interpretive approach which gives section 10(b) the minimally necessary scope required for its practical existence as an implied private right of action. This result can be achieved through a wide variety of analytic techniques, of which strict textualism is but one.

My argument for narrow construction of section 10(b) is thus pragmatic at heart. Once the Court abandons a narrow construction of the statute, it is without any objective guidance as to how far it should stretch in defining the scope of the implied section 10(b) private remedy. Moreover, by reading section 10(b) narrowly, the Court will be doing its best to satisfy its obligation to act as a faithful servant of a Congress that never even created the cause of action that the Court is forced to interpret.

Clearly, a better answer is to obtain from Congress a precise and well-crafted articulation of the contours of the section 10(b) private right of action. Absent such legislative guidance, however, a strict-textualist approach may present the best, although imperfect, hope for consistency and predictability in Supreme Court securities law jurisprudence. Courts do not belong in the inkblot business. A strict-textualist approach may, for all its flaws, be the best available organizing principle for a rule of narrow construction that can end the string of sharply divided securities law decisions recently emanating from the Supreme Court.

92. Id.
APPENDIX A

Margins And Voting Patterns in Major Supreme Court Decisions

Table 1 excludes from consideration cases relating to, but not interpreting, the federal securities laws. For example, Mastrobuono v. Shearson Lehman Hutton, Inc.94 deals with a securities arbitration matter but turns on questions relating to choice of law issues and to the interpretation of the Federal Arbitration Act.95 Likewise, Plaut v. Spendthrift Farm, Inc.96 deals with the constitutionality of section 27A(b) of the Securities Exchange Act of 1934 (1934 Act),97 but turns on the application of separation of powers principles.98 Such cases are properly excluded from an analysis of Supreme Court decisions construing the federal securities laws.

In Gustafson v. Allied Co.,99 the Court ruled 5-4 that a buyer's right of rescission under section 12(2) of the 1933 Securities Act (1933 Act) does not extend to private agreements for the sale of securities.100 The section 12(2) cause of action gives buyers the right of rescission against securities sellers who make material misstatements or omissions via a "prospectus."101 Justice Kennedy's majority opinion, joined by Chief Justice Rehnquist and Justices Stevens, O'Connor, and Souter, found that the overall structure of the 1933 Act and its legislative history showed that Congress intended the term "prospectus" to refer only to the offering of securities by an issuer or controlling shareholder to the general public.102 The majority concluded that the section 12(2) cause of action did not reach private agreements for the sale of securities.103 Justice Thomas, in a dissent joined by Justices Scalia, Ginsburg, and Breyer, argued that the 1933 Act used two distinct definitions of the term "prospectus,"104 the

† Prepared by Hugh Miller, student at Stanford Law School.
95. Id. at 1213-14.
97. Id. at 1449.
98. Id.
100. Id. at 1073-74.
102. Id. at 1069-70.
103. Id. at 1073-74.
104. Id. at 1076 (Thomas, J., dissenting).
broadest definition supporting a section 12(2) cause of action involving private securities transactions. In a separate dissent, Justice Ginsburg, joined by Justice Breyer, adduced further textual and historical support for Justice Thomas's interpretation and approvingly reviewed scholarly and lower court authority for the proposition that section 12(2) applies to private sales of securities.

In *Central Bank v. First Interstate Bank* the Court ruled 5-4 that there is no implied private right of action for aiding and abetting a violation of section 10(b) of the 1934 Act. Justice Kennedy's majority opinion stated that the text of the 1934 Act did not reach aiding-and-abetting liability for section 10(b) violations. Moreover, Congress chose not to impose such liability for any of the expressly created private causes of action in the Act. The majority thus inferred that Congress did not intend to attach liability to aiding and abetting since it did not explicitly provide for a private section 10(b) cause of action and therefore declined to extend such liability to the implied private cause of action created by lower courts. Justice Stevens's dissent, joined by Justices Blackmun, Souter, and Ginsburg, argued that the Court should follow administrative and lower court precedent implying a private section 10(b) cause of action for aiding and abetting because this would be consistent with the broad remedial purposes of the 1934 Act. The dissent also suggested that Congress's failure to amend section 10(b) in light of this precedent implies legislative assent to the existence of a private cause of action for aiding and abetting.

In *Musick, Peeler & Garrett v. Employers Ins. of Wassau* the Court held 6-3 that defendants have an implied right to seek contribution from joint tortfeasors in a cause of action governed by section 10(b) of the 1934 Act and SEC rule 10b-5 promulgated thereunder. Justice Kennedy's majority opinion observed that

105. *Id.* at 1074 (Thomas, J., dissenting).
106. *Id.* at 1081-83 (Ginsburg, J., dissenting).
108. *Id.* at 1455.
109. *Id.* at 1448.
110. *Id.* at 1449.
111. *Id.* at 1448.
112. *Id.*
113. *Id.* at 1456 (Stevens, J., dissenting).
114. *Id.* at 1458 (Stevens, J., dissenting).
116. *Id.* at 2092.
Congress declared rights of contribution in two sections of the 1934 Act—sections 9 and 18—that expressly define private causes of action. Since these two sections are similar both in structure and purpose to section 10(b), the majority concluded that consistency and coherence with the overall structure and purpose of the 1934 Act imply a right to contribution attaching to the private cause of action established by the judiciary under section 10(b) and rule 10b-5. In a dissent joined by Justices Blackmun and O'Connor, Justice Thomas argued against a right to contribution on the ground that Congress could have expressly provided for such a right, either in the original 1934 Act or in a subsequent amendment, but has chosen not to do so. Absent a clear declaration of legislative intent, Thomas opined that the Court should decline to extend protection to joint tortfeasors under section 10(b) and rule 10b-5 because such tortfeasors are not the intended beneficiaries of the 1934 Act.

In Lampf, Pleva, Lipkind, Prupis & Pettigrow v. Gilbertson, the Court ruled 5-4 that the statute of limitations for section 10(b) violations under the 1934 Act bars any claim not filed within one year after a violation’s discovery and within three years of the violation’s occurrence. Justice Blackmun’s majority opinion noted that Congress created a one-year discovery period and three-year period of repose for the express causes of action defined under sections 9(e) and 18(c), and a one-year discovery period coupled with a two-year period of repose for actions defined under section 16(b). Furthermore, the majority found that the special focus of section 16(b) contrasted with the broad remedial purposes shared by sections 9(e), 10(b), and 18(c) of the 1934 Act. It thus concluded that the implied cause of action under section 10(b) should have the same one-and three-year time limitations that Congress established for the express causes of action defined under sections 9(e) and 18(c). Justice Scalia concurred, suggesting that absent a congressionally

117. Id. at 2090-91.
118. Id. at 2090.
119. Id. at 2091.
120. Id. at 2095 (Thomas, J., dissenting).
121. Id. at 2094-95 (Thomas, J., dissenting).
123. Id. at 364.
124. Id. at 360 nn.5-6.
125. Id. at 360 n.5.
126. Id. at 360-61.
127. Id. at 361.
legislated time limit, state statutes of limitation should control unless they conflict with the purpose of the federal statute, in which case no time limit will exist. Since the Court took the regrettable step of creating a private section 10(b) cause of action by judicial fiat, Scalia reasoned that the most responsible way to manage the consequences was to use the time limitation of an analogous cause of action.

Justice Stevens, in a dissent joined by Justice Souter, advocated the Court's endorsement of existing precedents which borrowed state statutes of limitations for private section 10(b) actions. Justice O'Connor also filed a dissent joined by Justice Kennedy arguing that, given lower court precedent and retroactivity considerations, fairness mandated the use of state statutes of limitation for all section 10(b) causes of action initiated prior to the ruling in the case. Justice Kennedy's dissent, joined by Justice O'Connor, accepted the one-year discovery period but rejected a three-year period of repose as contrary to the remedial purposes of the 1934 Act.

In *Gollust v. Mendell*, its sole unanimous securities decision, the Court held that securities holders have standing under section 16(b) of the 1934 Act as long as they held those securities at the time their suit was instituted. The plaintiff owned shares of Viacom International, Inc. (Viacom) and, in 1987, brought a derivative action under section 16(b) of the 1934 Act. That section imposes strict liability on owners of more than ten percent of a corporation's listed stock for "short swing" trading. Arsenal Acquiring Corporation subsequently acquired Viacom, and the holders of Viacom's stock received shares in the acquiring company. After this transaction, the plaintiff no longer held shares in Viacom.

The issue presented was whether standing existed under section 16(b). The Court first stated that because section 16(b) "imposes liability without fault within its narrowly drawn limits," [the Court has] been reluctant to exceed a literal, 'mechanical' application of the

128. *Id.* at 364 (Scalia, J., concurring).
129. *Id.* at 365-66 (Scalia, J., concurring).
130. *Id.* at 368 (Stevens, J., dissenting).
131. *Id.* at 373-74 (O'Connor, J., dissenting).
132. *Id.* at 374 (Kennedy, J., dissenting).
134. *Id.* at 118.
135. *Id.*
136. *Id.* at 121.
137. *Id.*
statutory text."\textsuperscript{138} The Court, however, had "no difficulty concluding that, in the enactment of § 16(b), Congress understood and intended that, throughout the period of his participation, a plaintiff authorized to sue insiders on behalf of an issuer would have some continuing financial interest in the outcome of the litigation."\textsuperscript{139} The Court, however, found that this financial stake is "maintained when the plaintiff's interest in the issuer has been replaced by one in the issuer's new parent."\textsuperscript{140} The Court therefore held that the plaintiff had "satisfied the statute's requirements [since] [h]e owned a 'security' of the 'issuer' at the time he 'instituted' [the] § 16(b) action."\textsuperscript{141}

In \textit{Virginia Bankshares, Inc. v. Sandberg},\textsuperscript{142} the Court ruled 8-1 that knowingly false statements of opinion or beliefs made by corporate directors for the purpose of soliciting proxies, even though conclusory in form, may be actionable as misstatements of material facts under section 14(a) of the 1934 Act and SEC rule 14a-9.\textsuperscript{143} The Court further held by a 5-4 vote that minority shareholders who collectively lack the votes necessary to defeat a planned corporate merger advocated by majority shareholders cannot prove the required element of causation under an alleged section 14(a) violation.\textsuperscript{144} On the latter issue Justice Souter, writing for the majority, argued that congressional silence concerning the proper scope of the judicially implied right of private action under section 14(b) posed a serious obstacle to expanding its protection to include claims where minority shareholders lack votes necessary to defeat a majority-endorsed plan promoted via a misleading proxy statement.\textsuperscript{145}

In a dissent joined by Justice Marshall, Justice Stevens argued that materially false statements in proxy materials are actionable under section 14(a) and that no additional element of causation should be imposed.\textsuperscript{146} In a separate dissent joined by Justices Marshall, Blackmun, and Stevens, Justice Kennedy advocated relaxation of the majority's standard of proof for causation to permit

\begin{itemize}
\item \textsuperscript{138} \textit{Id.} at 122.
\item \textsuperscript{139} \textit{Id.} at 126.
\item \textsuperscript{140} \textit{Id.} at 126-27.
\item \textsuperscript{141} \textit{Id.} at 127.
\item \textsuperscript{142} 501 U.S. 1083 (1991).
\item \textsuperscript{143} \textit{Id.} at 1087.
\item \textsuperscript{144} \textit{Id.} at 1106-08.
\item \textsuperscript{145} \textit{Id.} at 1104.
\item \textsuperscript{146} \textit{Id.} at 1112 (Stevens, J., dissenting).
\end{itemize}
recovery in cases where, but for misleading proxy statements, majority shareholders might have voted with the interests of a dissenting but powerless minority, or where the board of directors or majority shareholder has breached a fiduciary duty to the minority shareholders.\footnote{147}

In \textit{Reves v. Ernst & Young}\footnote{148} the Court ruled 5-4 that demand notes offered by a business organization to finance its general operations are “securities” within the meaning of section 3(a)(10) of the 1934 Act.\footnote{149} Justice Marshall’s majority opinion adopted the Second Circuit’s four-point “family resemblance” test to rebut a presumption that any note with a term of more than nine months is a “security” for purposes of the 1934 Act, placing the note within a list of judicially created exemptions.\footnote{150} The majority further declared that notes payable on demand have a maturity exceeding the 1934 Act’s statutory exemption for notes with terms not longer than nine months.\footnote{151}

In a separate concurrence, Justice Stevens agreed with the dissenters that demand notes have a maturity of less than nine months but argued that legislative history indicates that the 1934 Act’s statutory exemption applies only to “commercial paper,” and not to notes drafted as financial investments.\footnote{152} Chief Justice Rehnquist, joined by Justices White, O’Connor, and Scalia, filed a separate opinion concurring with the use of the “family resemblance” test\footnote{153} but dissenting on the ground that demand notes have immediate maturity and should fall within the 1934 Act’s statutory exemption.\footnote{154}

In \textit{Rodriguez v. Shearson/American Express Inc.}\footnote{155} the Court, by a 5-4 vote, held that predispute agreements to arbitrate claims under the Securities Act of 1933 are enforceable and resolution of claims in a judicial forum is not required.\footnote{156} Justice Kennedy’s majority opinion overruled the Court’s prior holding in \textit{Wilko v.}
Swan that arbitration agreements violated the 1933 Act's section 14 prohibition on "waiving compliance with any provision" of the Act. The majority premised its decision on the Court's prior finding in Shearson/American Express v. McMahon that claims under section 10(b) of the 1934 Act could be arbitrated under predispute arbitration agreements. Following the McMahon pattern of reasoning, the majority distinguished the substantive non-waivable rights conferred by the 1934 Act from procedural rights not subject to the 1933 Act's section 14 prohibition against waiver. The majority found that the right to select the judicial forum and the wider choice of courts are not essential procedural protections of the 1933 Act and may be waived under a predispute arbitration agreement. A dissenting Justice Stevens, joined by Justices Brennan, Marshall, and Blackmun, observed that Congress has declined to amend the 1933 Act in light of the Wilko precedent and argued that stare decisis considerations should have precluded its renunciation.

In Pinter v. Dahl the Court ruled by 7-1 vote that a common-law in pari delicto defense is available for defendants in a private section 12(2) cause of action under the Securities Act of 1933. The Court further held that a person who gratuitously promotes unregistered securities does not incur "seller" liability under section 12(1) of the Securities Act. Justice Blackmun's majority opinion declared that the in pari delicto defense, previously established for section 10(b) violations of the 1934 Act in Bateman Eichler, Hill, Richards, Inc. v. Berner, applies to any private cause of action under the federal securities laws. The majority also held that the term "seller" under section 12(1) of the 1933 Act did not apply to a nonowner party who substantially causes a sales transaction, but who gratuitously solicits the purchase without any desire to serve his or her own financial interests or the interests of the securities owner.

158. Rodriguez, 490 U.S. at 482-86.
160. Rodriguez, 490 U.S. at 481-82.
161. Id. at 481.
162. Id.
163. Id. at 487 (Stevens, J., dissenting).
165. Id. at 632-41.
167. Pinter, 486 U.S. at 635.
168. Id. at 648.
Justice Stevens's dissenting opinion accepted the majority's ruling on the availability of the *in pari delicto* defense but disputed its application to the facts of the instant case. Stevens also objected to the majority's discussion of "seller" in a contribution suit context as both misleading and merely advisory, the legal issue concerned not contribution among joint tortfeasors, but assignment of seller's liability to an investor facilitating transactions between a securities owner and third party purchasers. Justice Kennedy took no part in this case.

In *Basic, Inc. v. Levinson* the Court ruled 6-0 that the standard for materially false or misleading statements in a section 10(b) action under the 1934 Act depends upon "the significance the reasonable investor would place on the withheld or misrepresented information." The Court also held by a 4-2 margin that the dissemination of materially false or misleading company information to the marketplace creates a rebuttable presumption of reliance on the part of stockholders.

Justice Blackmun, writing for the majority, declared that the appropriate measure of materiality for actions involving section 10(b) of the 1934 Act is the "reasonable investor" standard established in *TSC Industries, Inc. v. Northway, Inc.* for section 14(a) of the same Act. The majority further stated that requiring each member of a plaintiff class to prove individual reliance upon misinformation would place an impracticable and unfair burden upon a section 10(b) action. Disseminating misinformation to the marketplace creates a rebuttable presumption of investor reliance for purposes of section 10(b). This presumption coheres with the legislative history and purpose of the 1934 Act. Justice White, joined by Justice O'Connor, filed a separate opinion concurring with the materiality standard while criticizing the holding that injection of material misinformation into the marketplace creates a presumption of investor reliance.
reliance. Justice White argued that the legislative history of the 1934 Act weighed against the majority's "fraud-on-the-market" theory of investor reliance because Congress rejected a similar proposal. He argued further that the "fraud-on-the-market" theory conflicted with the 1934 Act's goal of promoting disclosure by rewarding investors who refuse to read or rely on such disclosures. Chief Justice Rehnquist and Justices Scalia and Kennedy took no part in this case.

In *Shearson/American Express Inc. v. McMahon* the Court, by a 5-4 vote, ruled that claims under section 10(b) of the 1934 Act were arbitrable under predispute arbitration agreements. The Court unanimously held that a claim under the Racketeer Influenced and Corrupt Organizations Act must be arbitrated in accordance with the terms of a predispute agreement. Justice O'Connor, writing for the majority, stated that congressional intent to mandate a judicial forum for the resolution of section 10(b) claims cannot be inferred from section 29(a) of the 1934 Act prohibiting waiver of "compliance with any provision" of the Act. Justice O'Connor reasoned that section 29(a) merely barred waiver of the "substantive" duties secured by the Act. As such, section 29(a) does not preclude waiver of the section 27 provision conferring exclusive federal jurisdiction for claims brought under section 10(b) because section 27 does not impose any duty with which securities traders must "comply."

Justice O'Connor distinguished the Court's prior decision in *Wilko v. Swan*, holding that claims arising under the Securities Act of 1933 with similar antiwaiver and jurisdictional provisions were not subject to arbitration agreements, on the ground that *Wilko* must be read as barring waiver only when arbitration inadequately safeguards substantive duties conferred by the Act. Justice O'Connor also concluded that subsequent legislative history does not

179. *Id.* at 250 (White, J., dissenting).
180. *Id.* at 257 (White, J., dissenting).
181. *Id.* at 258-59 (White, J., dissenting).
182. *Id.* at 225.
184. *Id.* at 232.
185. *Id.* at 242.
186. *Id.* at 227-28.
187. *Id.* at 228.
188. *Id.* at 227-28.
190. *Shearson*, 482 U.S. at 228.
reflect congressional intent to bar enforcement of all predispute arbitration agreements under section 29(a). Justice Blackmun, joined by Justices Brennan and Marshall, dissented from the majority's holding on these issues. According to Justice Blackmun, the majority's statutory interpretation of "compliance" implies the surprising result that the "literal language of § 29(a) does not apply to an investor's waiver of his own action." Justice Blackmun felt that the Court's earlier holding in Wilko that "the express language, legislative history, and purposes of the Securities Act [of 1933] all made predispute agreements to arbitrate section 12(2) claims unenforceable" exceptions to the Arbitration Act of 1925. Justice Blackmun asserted that the majority's holding effectively overruled Wilko but found that the legislative history cited by Justice O'Connor supported the conclusion that Congress acquiesced in the Wilko perspective. In a separate opinion, Justice Stevens also dissented on this issue. Justice Stevens cited circuit court precedents extending the Wilko holding to claims brought under the Securities Exchange Act and appealed to stare decisis considerations.

In Carpenter v. United States an evenly divided Court left standing a lower court conviction under section 10(b) of the 1934 Act by a vote of 4-4 and unanimously upheld mail and wire fraud convictions arising from the same conduct. Justice White delivered the opinion of the Court, reciting the lower court's reasoning on the section 10(b) violation: Petitioners were involved in a scheme to make advance use of proprietary information, slated for publication in a Wall Street Journal investment column, to buy and sell securities at a profit. This advance use of proprietary information was a deliberate breach of a confidentiality duty owed by one scheme member who was employed by the Journal. The other scheme

191. Id. at 238.
192. Id. at 242.
193. Id. at 253 n.9 (Blackmun, J., dissenting).
194. Id. at 221.
195. Id. at 254 (Blackmun, J., dissenting).
196. Id. at 247 (Blackmun, J., dissenting).
197. Id. at 268-69 (Stevens, J., dissenting).
199. Id. at 24.
200. Id. at 28.
201. Id. at 23.
202. Id. at 23-24.
members used this information to make profitable trades in light of
the expected impact that dissemination of the information would have
on the marketplace after publication and split the proceeds with the
Journal employee. The lower court held with respect to the
section 10(b) charges that the breach of confidentiality was a fraud
and deception on the Journal. The victim of the fraud was not
involved in the securities traded as a result of the breach of confiden-
tiality. But the lower court found that the fraud was “in connec-
tion with” the purchase and sale of securities within the meaning of
section 10(b). The record does not show whether Justice White
voted to uphold the section 10(b) conviction, nor does it identify
which Justices would have upheld the Carpenter decision.

203. Id. at 23.
204. Id. at 24.
205. Id.
206. Id.