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27 *Rutgers L. J.* 627**LENGTH:** 3900 words**SYMPOSIUM:** PERSPECTIVES ON JUSTICE JOHN PAUL STEVENS: DESPERATELY SEEKING A STEVENS
[WHO CARES ABOUT THE FEDERAL SECURITIES LAWS]**NAME:** Karl Shumpei Okamoto ***BIO:**

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SUMMARY:

... We concluded that recent decisions evidence a priority in the Court's analysis for certain meta issues unrelated to the sound development of the regulatory scheme under the federal securities laws. ... Because of this, we approached the project of reviewing Justice Stevens' opinions in the federal securities law area as something of a search for our hero on the Supreme Court. ... And generally, I question whether implied private rights of action are a regulatory burden that impose costs that are justified by the benefits they produce. ... So when each of us pursued Justice Stevens' opinions looking for our common hero in terms of the rejection of the literalist approach in favor of a purposive approach, we each did so with our own substantive agenda in the back of our minds. ... He points out that in 1974, before the Cort decision, it was reasonable for Congress to assume that under the current judicial view of the matter, a private right of action would be implied from any regulatory statute that Congress would adopt of the kind in question in the case. ... Is it enough that both of us applaud his negative position on a literalist approach while differing on his positive approach to a substantive outcome? ...

TEXT:

[*627]

A few years ago Professor Branson and I co-authored an article entitled "The Supreme Court's Literalism and the Definition of 'Security' in the State Courts." n1 The subject of that article was the Supreme Court's recent approach to interpreting the definition of the term "security" in the federal securities statutes. The content of that definition is central to the interpretation of the federal securities laws because the term defines the jurisdictional ambit for the federal regulation. If a transaction involves a "security," the federal securities statutes apply. If it does not, the statutes are not relevant, and the parties must resort to common law or some other statutory basis to pursue any claim of fraud or misrepresentation.

In the article, Professor Branson and I critiqued what we saw as an increasingly literalist or formalistic approach by the United States Supreme Court to crafting the definition of "security." n2 We saw this as an abandonment of the historical, purposive approach in which the Court would evaluate the application of the statute to the facts at hand based on the purpose and policies underlying the law. We concluded that recent decisions evidence a priority in the Court's analysis for certain meta issues unrelated to the sound development of the regulatory scheme under the federal securities laws. These meta issues include concerns for federalism, concerns for the separation of powers, and an increasingly literalist approach to statutory interpretation as a response to these institutional issues. n3 In our discussion we bemoaned this development as an abandonment of the substantive development of such an important area of law as securities regulation.

Our critique of the literalist tendency of the Supreme Court focused on the decision in *Landreth Timber Co. v. Landreth*. n4 Much like the infamous rose, the Supreme Court decided that stock is stock is stock. n5 And because stock is a term that is literally included within the definition of "security," [*628] stock is therefore a security. n6 This

conclusion led the Court to decide that in every transaction, except the most unusual, involving an instrument labeled "stock," the federal securities laws apply. n7 This decision was reached in what must be the worst factual context as a matter of policy for the application of the federal securities law. Namely, the court was extending the federal antifraud remedy to a privately negotiated sale of a company, which if effected through an asset sale rather than a stock sale, would not have benefited from a private right of action under the federal anti-fraud rule. By virtue of this decision, the disappointed purchaser in a stock deal would have a federal claim despite being sophisticated and having knowingly negotiated limitations on a right to sue.

Justice Stevens, in his dissent, made very clear that this was illogical as a matter of policy. n8 He argued that the Court, in attempting to adopt presumptive or formalistic approaches to the interpretation of the statute, had abandoned its historical role of evaluating the policy implications of its interpretation of the statute. n9 He concluded very simply that it was, as a matter of policy, illogical to apply the federal anti-fraud rule to a transaction structured as a stock sale and not to a transaction structured as an asset sale when there was no rational basis for discriminating between the two types of structures. n10

In an evaluation of the new "literalism" in the Court's decisions, Professor Schauer suggested that a plain meaning approach, although unsound as an interpretive tool, nevertheless might serve as "a second-best coordinating device for multiple decision makers attempting to reach some methodological consensus in the face of substantive disagreements among them." n11 Schauer further notes that the majority tends to adopt a plain meaning approach where it appears to find the substance of the case both complex and uninteresting. n12 Now, the idea that the Justices would be uninterested in federal securities regulation is a notion that is, of course, especially galling to two legal professionals—Professor Branson and myself—who spend their professional lives on the subject. [*629]

Professor Branson and I were therefore eager to see in Justice Stevens' dissent an example of the kind of methodology we prefer to the new literalism evidenced in the recent Supreme Court decisions. Because of this, we approached the project of reviewing Justice Stevens' opinions in the federal securities law area as something of a search for our hero on the Supreme Court. Our hero being the Justice who, rather than pursuing interpretation of the federal securities laws with an agenda focused on these meta, institutional issues, would rather approach the federal securities laws with an agenda based on developing sound comprehensive regulatory policy in this very important area of regulation critically affecting the nation's economy. n13 And perhaps more importantly, a Justice who found the securities law interesting. Disappointingly, however, my conclusion is that Justice Stevens is not the hero we were looking for—at least not in the sense that he would be the champion in the federal judiciary of sound policy development with regard to the federal securities laws. Rather, we discover, as was concluded in an earlier article in the Duke Law Journal, n14 that Justice Stevens is simply a Justice with a very traditional, I would say "old style," view of the judicial function.

I reach this conclusion by confessing that while Professor Branson and I share a common critical position vis a vis the Supreme Court's recent approaches to the federal securities statutes, namely a criticism of their literalist, non-policy based approach to interpretation, we diverge when it comes to a substantive critical position. Generally speaking, I am predisposed to favor free market solutions and a lessening of the regulatory burden under the federal securities statutes. I am especially predisposed towards excluding federal regulation from privately negotiated transactions. And generally, I question whether implied private rights of action are a regulatory burden that impose costs that are justified by the benefits they produce. Generally speaking, Professor Branson, on the other hand, focuses on the plight of small, unsophisticated investors who are still, even in a highly efficient market, often the victims of con men, greedy Wall Streeters, and unprincipled penny stock pushers. My view is, generally, that while these are victims who deserve some form of attention, a regulatory system which focuses on them as the principle subject matter for protection, is missing the forest for the trees. So when each of us pursued Justice Stevens' opinions looking for our common hero in terms of the rejection of the [*630] literalist approach in favor of a purposive approach, we each did so with our own substantive agenda in the back of our minds.

So, for example, when we looked at the Landreth case and Justice Stevens' dissent, I was unequivocally enthusiastic. I agreed with Justice Stevens' rejection of the literalist approach to the definition of stock as a "security." I also agreed with the substantive outcome of his dissent, namely, the exclusion of the federal securities laws from the privately negotiated stock sale. Professor Branson, on the other hand, agreed only so far as the decision rejected the literalist approach. He was, however, less enthusiastic about the conclusion that that approach should prevent the federal securities laws from providing a remedy even in the privately negotiated context, although perhaps not under the particular facts of Landreth. He is concerned that this slippery slope of dividing private and public will leave widows and retirees unprotected from

exactly the kind of door-to-door sales techniques that he is concerned about in preserving for them a private right of action under the federal securities laws. Thus, for Professor Branson, Stevens' Landreth decision is less of an unequivocal plus than for me.

If, however, we look at an earlier decision—the last majority opinion written by Justice Stevens in the securities area—his opinion in *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*,ⁿ¹⁵ our positions shift. That case immediately precedes Landreth in the line of securities cases in which Stevens writes an opinion. In a 5–4 decision, writing for the last time for the majority in a case interpreting the federal securities statutes, Stevens decides that under the Commodities Exchange Act there is an implied private right of action for disappointed investors to obtain damages.ⁿ¹⁶ Focusing on provisions which are analogous to Rule 10b–5 and similar anti-fraud provisions in the Securities Act of 1933 and Securities Exchange Act of 1934, Justice Stevens concludes that the Commodities Exchange Act similarly provides a private right of action for fraud.ⁿ¹⁷ This decision comes after the famous decisions in *Cannon v. University of Chicago*ⁿ¹⁸ and *Cort v. Ash*,ⁿ¹⁹ in which the Supreme Court unequivocally shifted its position away from readily implying private causes of action for beneficiaries of federal regulatory statutes in favor of an increasingly restrictive view absent express authorization by Congress for such a remedy. Justice Stevens argues for what is now a waning majority that, as Branson notes, the "congressional [*631] reenactment doctrine" basically saves the implication of a private right of action under the Commodities Exchange Act from this new analysis.ⁿ²⁰ He points out that in 1974, before the Cort decision, it was reasonable for Congress to assume that under the current judicial view of the matter, a private right of action would be implied from any regulatory statute that Congress would adopt of the kind in question in the case.ⁿ²¹ Just as the Court had done for Section 10(b) and Rule 10b–5, Congress could have assumed that the Court would imply a similar cause of action for the similar provision in the Commodities Exchange Act.ⁿ²² Stevens therefore argued that it would be anachronistic to assume, that when adopted both in the 1930s and then amended in subsequent years up to 1974, these provisions were adopted by Congress with a view and expectation that the Courts would interpret them differently.ⁿ²³

Again, Branson and I agree that the current Court's approach to the implied causes of action under federal securities laws is a result of a larger meta policy regarding the Court's relationship to the other branches of government. We believe that their increasingly restrictive approach to the implied causes of action are not the result of sound policy development under the federal securities laws, but rather the result of fundamentally political conclusions regarding their role in the tripartite federal government. We again bemoan that kind of decision making process, namely, the decision of substantive issues related to specific subject matter of federal securities regulation by reference to meta agendas regarding the role of the federal judiciary. Whether or not an implied private right of action under Rule 10b–5 or under the Commodities Exchange Act is a wise policy matter is of course open to some discussion, and I think Professor Branson and I differ on the conclusion. What we agree on, however, is that that decision should not be based solely upon a view of the proper role of the federal judiciary. Therefore, we are pleased with Justice Stevens' methodology in rejecting the sudden shift in judicial policy regarding implied rights of action in the *Curran*ⁿ²⁴ case. We differ, however, about the substantive outcome and its wisdom.

So what has come of our search for a hero? In looking at both *Curran* and *Landreth*, we have found both common ground and differences of opinion. We share our enthusiasm for Stevens' rejection of the literalist, [*632] formalist approach. We differ, however, in the substantive outcomes and their wisdom. I feel less enthusiastic about *Curran* because of my view of the wisdom of implied rights of action. Professor Branson feels less enthusiastic about *Landreth* because of his views on the need to extend federal securities regulation to both public and private transactions. Is it enough that both of us applaud his negative position on a literalist approach while differing on his positive approach to a substantive outcome?

In the end, I do not think so. I conclude that neither of us has found our hero. Rather what we have found is a traditional judge who pursues his own meta-agenda of a very anti-activist approach to interpreting the federal securities statutes. We found a conservative in the old sense of the word. His subsequent opinions, written since his last utterance as the majority opinion writer in *Curran*, exemplify his approach.

For example, consider his dissents in two cases in which the Supreme Court overrules its long standing precedent holding that both the Securities Act of 1933 and the Securities Exchange Act of 1934 prohibit the enforcement of predispute arbitration agreements with respect to alleged violations of the federal securities laws. In the first case, *Shearson/American Express, Inc. v. McMahon*,ⁿ²⁵ the Court held that its prior opinion in *Wilko v. Swan*,ⁿ²⁶ which held that such agreements were not enforceable with respect to claims under the Securities Act, would not apply to claims

arising under the Securities Exchange Act. Therefore, the Court decided to enforce predispute agreements to arbitrate claims under the Securities Exchange Act. In his dissent, Stevens writes:

During the 32 years immediately following this Court's decision in *Wilko*, each of the eight Circuits that addressed the issue concluded that the holding of *Wilko* was fully applicable to claims arising under the Securities Exchange Act of 1934. This long standing interpretation creates a strong presumption, in my view, that any mistake that the courts may have made in interpreting the statute is best remedied by the Legislative, not the Judicial, Branch. n27

Stevens voiced an even stronger objection in the subsequent case, *Rodriguez de Quijas v. Shearson/American Express, Inc.* n28 In that case the [*633] Court expressly overruled its prior decision in *Wilko*, extending its earlier holding in *Shearson/American Express* to Securities Act claims. Stevens' dissent in that case stated:

The Court of Appeals refused to follow *Wilko*, a controlling precedent of this Court. As the majority correctly acknowledges, the Court of Appeals therefore engaged in an indefensible brand of judicial activism. We, of course, are not subject to the same restraint when asked to upset one of our own precedents. But when our earlier opinion gives a statutory provision concrete meaning, which Congress elects not to amend during the ensuing 3 1/2 decades, our duty to respect Congress' work product is strikingly similar to the duty of other federal courts to respect our work product.

In the final analysis, a Justice's vote in a case like this depends more on his or her views about the respective lawmaking responsibilities of Congress and this Court than on conflicting policy interests. Judges who have confidence in their own ability to fashion public policy are less hesitant to change the law than those of us who are inclined to give a wide latitude to the views of the voters' representatives on non-constitutional matters. n29

In this last statement Stevens makes clear his "meta issue" point of view in deciding this case. Rather than pursuing the substantive policy concerns of the federal securities laws, which I think both Professor Branson and I would agree would favor enforcing predispute arbitration agreements, Stevens decides this case by arguing against overruling a long-standing Court interpretation which has, through Congressional inaction, taken on the status of a legislative utterance.

Similarly in the more recent case of *Reves v. Ernst & Young*, n30 in which the Supreme Court again approached the definition of "security" but this time in the case of notes, Stevens was quick to point out in rejecting a literalist approach to the interpretation of the definition that "in his view such a settled construction of an important federal statute should not be disturbed unless and until Congress so decides." n31

This kind of judicial conservatism should be distinguished from that which we associate with Justice Scalia and Justice Rehnquist's more dogmatic conservatism. Take for example the recent case *Lampf, Pleva, [*634] Lipkind, Prupis & Petigrow v. Gilbertson*, n32 in which the Court determined what the statute of limitations ought to be for the private cause of action under Rule 10b-5. In that case, the Court decided to reject the traditional approach of borrowing the state statute of limitations in comparable causes of action in favor of a uniform federal statute of limitations borrowed from analogous provisions of the federal statute. n33 Stevens argued for the "traditional" rule. n34 He argued that the implied cause of action seen under Section 10(b) was recognized at a time when it was common to read statutes to imply private causes of action and also was the practice to adopt the analogous state statutes of limitation. n35 In his view, only Congress is equipped to engage in the policy analysis needed for the dramatic changes advocated by the majority. n36 He states "when the Court ventures into this lawmaking arena, however, it inevitably raises questions concerning the retroactivity of its new rule that are difficult and arguably inconsistent with the neutral, nonpolicymaking role of the judge." n37

The same reasoning is found in the more recent *Central Bank of Denver N.A. v. First Interstate Bank of Denver N.A.* case. n38 In that decision the 5-4 majority concludes that Section 10(b) and Rule 10(b)(5) of the 1934 Act do not support a cause of action for aiding and abetting against secondary parties in a transaction affected by securities fraud. Justice Stevens writes a dissent in which he maintains that the Court made two mistakes. n39 The first mistake was that

"instead of simply addressing the questions presented by the parties, on which the law really was unsettled, the Court sua sponte directed the parties to address a question on which even the petitioner justifiably thought the law was settled, and reaches out to overturn a most considerable body of precedent." n40 Justice Stevens concludes that "there is a risk of anachronistic error in applying our current approach to imply the causes of action to a statute enacted when courts commonly read statutes of this kind broadly to accord with their remedial purposes and regularly approved rights to sue despite statutory silence." n41 Again, Stevens is reiterating themes we have seen since his decision in *Curran*. [*635]

He makes clear the rationale for this traditionalist view of how to approach the case in the following statement:

A policy of respect for consistent judicial and administrative interpretations leaves it to elected representatives to assess settled law and to evaluate the merits and demerits of changing it. n42

I think it is that view of judging, that it is neutral and non-policymaking, which is ultimately Stevens' credo. That is why Professor Branson and I really do not find in him what we are looking for.

Rather, I think one final quote from Stevens dissent in the *Central Bank of Denver* case might capture most clearly Stevens' role in the past two decades in the Courts' attempts to interpret the federal securities laws:

While we are now properly reluctant to recognize private rights of action without an instruction from Congress, we should also be reluctant to lop off rights of action that had been recognized for decades, even if the judicial methodology that gave them birth is now out of favor. n43

In that statement we see a conservative of two kinds—a judicial conservative as to the substance of the Court's powers to make policy through broad interpretation of a statute evidenced by his term "properly reluctant to recognize private rights of action," and a judicial conservative who feels bound by precedent and tradition evidenced by his hesitancy to "lop off rights of action that have been recognized for decades." To put it simply, I think Justice Stevens is not the person to seek out as a champion for intelligent development of the securities laws. Rather, he is the fulcrum around which the Court's more activist—both liberal and conservative—tendencies have swung in the past twenty years.

Legal Topics:

For related research and practice materials, see the following legal topics:
 Governments
 Legislation
 Statutes of Limitations
 Time Limitations
 Civil Procedure
 Alternative Dispute Resolution
 Judicial Review
 Securities Law
 Liability
 Statutory Application & Interpretation

FOOTNOTES:

n1 Douglas M. Branson & Karl Shumpei Okamoto, *The Supreme Court's Literalism and the Definition of "Security" in the State Courts*, 50 *Wash. & Lee L. Rev.* 1043 (1993).

n2 *Id.* at 1051-55.

n3 *Id.* at 1068-73.

n4 471 *U.S.* 681 (1985).

n5 *Id.* at 686.

n6 *Id.*

n7 *Id.*

n8 *Id.* at 697-700 (Stevens, J., dissenting).

n9 *Id.* at 700 n.2.

n10 *Id.* at 699-700.

n11 Frederick Schauer, *Statutory Construction and the Coordinating Function of Plain Meaning*, 1990 *Sup. Ct. Rev.* 231, 232.

n12 *Id. at 247-49.*

n13 Much like the "hero" Professor Klevorick has found in Justice Stevens and his antitrust jurisprudence. See

n14 William D. Popkin, A Common Law Lawyer on the Supreme Court: The Opinions of Justice Stevens, *1989 Duke L.J. 1087* (1989)(reviewing his jurisprudence generally).

n15 *456 U.S. 353* (1982).

n16 *Id. at 381-82.*

n17 *Id. at 390-91.*

n18 *441 U.S. 677* (1979).

n19 *422 U.S. 66* (1975).

n20 *Curran, 456 U.S. at 381-82.*

n21 *Id. & n.66.*

n22 *Id. at 389 & n.88.*

n23 *Id. at 391 n.92.*

n24 *456 U.S. 353* (1982).

n25 *482 U.S. 220* (1987).

n26 *346 U.S. 427* (1953), overruled by *Rodriquez Qujas v. Shearson/American Express, 490 U.S. 477* (1989).

n27 *McMahon, 482 U.S. at 268-69* (Stevens, J., dissenting) (citations omitted).

n28 *490 U.S. 477* (1989).

n29 *Id. at 486-87* (Stevens, J., dissenting) (citations omitted).

n30 *494 U.S. 56* (1990).

n31 *Id. at 74* (Stevens, J., dissenting).

n32 *501 U.S. 350* (1991).

n33 *Id. at 354-55.*

n34 *Id. at 368* (Stevens, J., dissenting).

n35 *Id. at 366-67* (Stevens, J., dissenting).

n36 *Id. at 367.*

n37 *Id. at 367-68* (Stevens, J., dissenting)(citations omitted).

n38 *114 S. Ct. 1439* (1994).

n39 *Id. at 1455-1460* (Stevens, J., dissenting).

n40 *Id. at 1457.*

n41 *Id. at 1458.*

n42 *Id. at 1457* (citations omitted).

n43 *Id. at 1460.*