Chiarella v. United States: A Study in Legal Style

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I.

When the law is against you, lawyers learn, you argue the facts; when the facts are against you, you argue the law. When each party has an arguable case, in other words, what the facts are and what the law is are interdependent questions.

Linking the facts presented to the court to past resolutions of similar disputes, a successful judicial opinion constructs a rationale that differentiates the particular exercise of judicial authority from different results reached in arguably similar cases and from the arbitrary application of superior power. Legal distinctions attempted in the opinion in order to differentiate its holding from cases relied on in the losing argument are often denominated, by the losing party, distinctions of style rather than substance. This characterization is not surprising, since distinctions of style are differences produced by subtle variations in the construction of essentially similar objects—variations that define the work of particular masters of a given craft. The use of the word style by the losing party as an antonym for substance, however, represents a charge that the words used by the court do not adequately distinguish either the facts or the law relied upon by that party. Such a charge can be demonstrated conclusively, in the sense that lawyers as well as litigants must accept it as valid, only when distinctions used in the opinion involve the court in logical inconsistencies. So long as the court's reasoning is consistent, in other words, the relevant question can be only whether the particular proposition on which the judge relies to justify the distinction is, in the circumstances, a persuasive one.

A wholly disinterested judge could reproduce, for his opinion, the arguments made by each side. This would eliminate the possibility that the judge's personal style dictated the substantive result. What it would

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Another article by Professor Deutsch, which also in part concerned *Chiarella v. United States*, appeared last year in these pages. That article was written after the Supreme Court granted certiorari in *Chiarella*, but before it handed down its decision. *See* Deutsch, *The New Deal and the Burger Court: The Significance of* United States v. Chiarella, 57 TEXAS L. REV. 965 (1979).

fail to do is to indicate the judge's rationale for deciding which argument to accept—a decision that requires justification if it is to be treated as legitimate. Legitimacy in this sense is determined by whether the justifying opinion continues to be cited as a precedent. Insofar as it is, the opinion's holding is necessarily being treated as a legitimate application of judicial authority, and the meaning of that holding is determined by the propositions for which it is cited.

The precedent contained in any given opinion thus encompasses both the propositions for which that opinion will be cited in future cases and the propositions imposed by it on the earlier holdings that defined the context in which it was written. To understand the concept of precedent, this article attempts to show, is to grasp the meaning of law, not only for the lawyer and the litigant, but also for the judge writing the opinion.

II.

Justice Powell begins by defining the question presented:[1] Is section 10(b) of the Securities Exchange Act[2] violated by a printer who has traded in the securities of a corporation but failed to disclose that he learned about a takeover attempt involving that corporation[3] by successfully deducing its identity from documents being printed by the firm in which he is employed.[4] The opinion notes that Chiarella (the printer) was indicted, under a statute imposing criminal penalties for willful violations of the Securities Exchange Act, seven months after he had been discharged by his employer,[5] and that he had entered into a consent decree with the Securities and Exchange Commission providing for return of his profits to the sellers of the shares.[6] It is then announced that Chiarella's conviction by a jury on all seventeen counts, affirmed by the Court of Appeals for the Second Circuit,[7] is being re-

1. Chiarella v. United States, 445 U.S. 222, 224 (1980).

2. 15 U.S.C. § 78j(b) (1976). This section prohibits the use "in connection with the purchase or sale of any security . . . [of] any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe." Pursuant to this section, the Securities and Exchange Commission has adopted Rule 10b-5, 17 C.F.R. § 240.10b-5 (1979), which formed the basis of Chiarella's indictment.

3. After learning of the takeover plans from the announcements he was printing, Chiarella purchased stock in the target companies and sold the shares immediately after the takeover bids were made public. 445 U.S. at 224.

4. In the documents delivered to the printer the identities of the acquiring and target companies were concealed by blank spaces or false names. Chiarella, however, was able to deduce the identities from other information contained in the documents. *Id.*

5. *See id.* at 225. The statute is § 32(a) of the Securities Exchange Act, 15 U.S.C. § 78ff(a) (1976 & Supp. II 1978).

6. 445 U.S. at 224.

7. United States v. Chiarella, 588 F.2d 1358 (2d Cir. 1978), *rev'd*, 445 U.S. 222 (1980).

versed.[8]

Thereafter, the language of the statutory provision Chiarella is claimed to have violated (barring the use of manipulative or deceptive devices in connection with the purchase or sale of any security) is analyzed,[9] and a survey is undertaken of the decision by the Securities and Exchange Commission in *Cady, Roberts & Co.*,[10] such circuit court decisions as *SEC v. Texas Gulf Sulphur Co.*,[11] and the Supreme Court's opinion in *Affiliated Ute Citizens v. United States*,[12] all of which expanded the scope of section 10(b) liability. Based on his examination of these authorities, Justice Powell concludes:

> We cannot affirm petitioner's conviction without recognizing a general duty between all participants in market transactions to forgo actions based on material, nonpublic information. Formulation of such a broad duty, which departs radically from the established doctrine that duty arises from a specific relationship between two parties, . . . should not be undertaken absent some explicit evidence of congressional intent.
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> . . . Section 10(b) is aptly described as a catch-all provision, but what it catches must be fraud. When an allegation of fraud is based upon nondisclosure, there can be no fraud absent a duty to speak. We hold that a duty to disclose under § 10(b) does not arise from the mere possession of nonpublic market information.[13]

The style of this *rationale*, a narrow construction of judicial and administrative attempts to deal with a given problem and an unwillingness to use judicial authority to fill gaps in statutory language, is that of the Burger Court. It contrasts sharply with the many Warren Court opinions in which the search for a remedy to the dispute being litigated, the need to reach the result perceived as correct, turns aside concern about exceeding the bounds of judicial authority.

In strict terms, a court itself only rarely can be said to have a style. When the Justices decide to draw attention to the fact that they are acting as an institution, they speak per curiam. In all other instances the rationale in the opinion, the choice of words, is identified with an individual Justice. For that Justice to enunciate a precedent, however, his opinion must be joined by other members of the Court, and that

8. 445 U.S. at 225.
9. *Id.*
10. 40 S.E.C. 907 (1961).
11. 401 F.2d 833 (2d Cir. 1968), *cert. denied*, 404 U.S. 1005 (1971), *discussed at* 445 U.S. 229.
12. 406 U.S. 128 (1972).
13. 445 U.S. at 233-35.

requirement imposes significant limits on the exent to which style—the way in which a given controversy is viewed—can remain an individual matter.[14]

One often can determine what a particular holding means by examining the style of the opinion in which it is enunciated. As a guide to substantive meaning, however, analysis of style reveals only the lowest common denominator of what the Justices joining that opinion believe the law to be. As a result, concurrences are as useful as dissents in determining the precise meaning of a decision. Other Justices may well join an opinion whose style differs drastically from their own, as long as they agree with the substance of the *rationale* it contains. Unless they regard the result as more significant than the opinion's precedential effect in all arguably similar cases, however, they cannot concur in a style perceived by them as significantly distorting the law.

In *Chiarella*, for example, Justice Brennan concurs only in the judgment.[15] He agrees that " 'a duty to disclose under § 10(b) does not arise from the mere possession of nonpublic market information,' "[16] but holds that "THE CHIEF JUSTICE's dissent . . . correctly states the applicable substantive law—a person violates § 10(b) whenever he *improperly obtains or converts* to his own benefit nonpublic information which he *then* uses in connection with the purchase or sale of securities."[17] He cannot join that dissent, however, because the instructions to Chiarella's jury failed to incorporate that law: "the instructions in effect permitted the jurors to return a verdict of guilty merely upon a finding of failure to disclose material nonpublic information in connection with the purchase of stock."[18]

III.

The Powell opinion does not examine the impact of the jury instructions in arriving at its decision. Its reasoning is that "[w]e need not decide whether [a] theory has merit [since] it was not submitted to the jury."[19] The theory referred to is "that petitioner breached a duty to the acquiring corporation when he acted upon information that he obtained by virtue of his position as an employee of a printer employed

14. *See* Deutsch, *Harvard's View of the Supreme Court: A Response*, 57 TEXAS L. REV. 1445 (1979).
15. 445 U.S. at 238.
16. *Id.* (quoting 445 U.S. at 235).
17. *Id.* at 239. (emphasis added).
18. *Id.*
19. *Id.* at 236.

by the corporation."[20] Thus phrased, the theory differs from that contained in the Chief Justice's dissent, in that it specifies that the printer owed a duty, not to his employer, but to the corporation whose documents he was printing. The theory contained in the Chief Justice's dissent—"that a person who has misappropriated nonpublic information has an absolute duty to disclose that information or to refrain from trading"[21]—leaves unclear the identity of the person to whom the duty of disclosure is owed. The words of section 10(b) identify the acquiring corporation—a purchaser of securities—as such a person. The analysis adopted by the court of appeals (and presumably accepted by the Chief Justice) focuses on the fact that financial printers have "regular access to market information" and "occupy . . . strategic places in the market mechanism."[22] The legal issue raised by this analysis is whether such persons—known as "market insiders"—are liable to the duties imposed by the language of section 10(b).

The holding in the Powell opinion that a decision on this issue would be premature presumably was necessary to obtain the concurring vote of Justice Stevens, a vote required if Justice Powell was to speak for a majority of the Court. In his concurrence Justice Stevens states that he "agree[s] with the Court's determination that petitioner owed no duty of disclosure to the sellers"[23] and that "[t]he Court correctly does not address the . . . question . . . whether the petitioner's breach of his duty of silence—a duty he unquestionably owed to his employer and to his employer's customers—could give rise to criminal liability under Rule 10b-5."[24] As a footnote to his opinion indicates,[25] however, one theory of criminal liability that Justice Stevens thinks relevant would require limiting the holding in *Blue Chip Stamps v. Manor Drug Stores*.[26] In that case, the Burger Court attempted to call a halt to the expansion of section 10(b) liability by holding that the Second Circuit had "rightly decided," in *Birnbaum v. Newport Steel Corp.*,[27] to limit "the plaintiff class for purposes of private damage action under

20. *Id.* at 235.
21. *Id.* at 240.
22. 588 F.2d at 1365.
23. 445 U.S. at 237.
24. *Id.* at 238. Again, the Court did not address that question because it concluded that it was not one presented to the jury. *See* notes 19-20 *supra* & accompanying text.
25. 445 U.S. at 238 n.*.
26. 421 U.S. 723 (1975). The theory referred to is the same one the Court refused to consider on the ground that it was not presented to the jury. *See* notes 19-20 *supra* & accompanying text. Justice Stevens does not completely foreclose that theory, for he notes that "the limitation on the right to recover pecuniary damages in a private action identified in *Blue Chip* is not necessarily coextensive with the limits of [Rule 10b-5] itself." 445 U.S. at 238 n.*.
27. 193 F.2d 461 (2d Cir.), *cert. denied*, 343 U.S. 956 (1952).

§ 10(b) and Rule 10b-5 . . . to actual purchasers and sellers of securities."[28]

The response by Chief Justice Burger to the majority's holding that a ruling on his theory would be premature rests on the doctrine of harmless error. The Chief Justice quotes statements made by Chiarella at trial admitting that the information he obtained was confidential and not to be used for personal gain. He concludes that "[i]n light of this testimony, it is simply inconceivable to me that any shortcoming in the instructions could have 'possibly influenced the jury adversely to [the defendant].' "[29] In terms of the law, moreover, the Chief Justice argues that "[the] interpretation of § 10(b) and Rule 10b-5 [to mean that a person who has misappropriated nonpublic information has an absolute duty to disclose that information or to refrain from trading] is in no sense novel. It follows naturally from legal principles enunciated by the Securities and Exchange Commission in its seminal *Cady, Roberts* decision."[30]

The majority agrees that "[t]he SEC took an important step in the development of § 10(b) when it held that a broker-dealer and his firm violated that section by selling securities on the basis of undisclosed information obtained from a director of the issuer corporation who was also a registered representative of the brokerage firm."[31] As the majority reads *Cady, Roberts*, however, that decision based liability on abuse of "a relationship of trust and confidence between the shareholders of a corporation and those insiders who have obtained confidential information by reason of their position with that corporation."[32] While this reading is wholly plausible as long as one focuses on the fact that *Cady, Roberts* involved a corporate director, that same person was the registered representative of a brokerage firm and, as such, can be said to "occupy [a] strategic place[] in the market mechanism."[33] The question, in other words, is whether the law embodied in *Cady, Roberts* compels Chiarella's conviction, or whether the Chief Justice's reading of that decision does constitute a novel interpretation of section 10(b).

Another way of making this inquiry is to ask whether the Chief Justice's reading of *Cady, Roberts* is a neutral one. Herbert Wechsler characterized the segregation decisions made by the Warren Court as

28. 421 U.S. at 730 (paraphrasing *Birnbaum*).
29. 445 U.S. at 244 (quoting Chapman v. California, 386 U.S. 18, 23 (1967)).
30. *Id.* at 241.
31. *Id.* at 226.
32. *Id.* at 228.
33. The quoted language is from the Second Circuit's opinion in *Chiarella*, 588 F.2d at 1365, rejected by the Supreme Court.

"[having] the best chance of making an enduring contribution to the quality of our society of any that I know in recent years."[34] He nevertheless disapproved of the opinions in those cases because they were not based on neutral principles of law, but could be read as rationalizations of a desirable result.[35] The argument Wechsler made was that, because judicial decisions can legitimately supplant those arrived at by the legislature only in a limited number of cases, desirable results must await legislative action in many spheres of social activity. Given this limitation on judicial power, the area in which a court can act legitimately is determined by the extent to which judges can arrive at their decisions on the basis of principles that are neutral, that transcend the interests of the contending parties. The "novelty" of the Chief Justice's reading of *Cady, Roberts* thus would reside in the fact that it compels a result the majority regards as unwarranted in the absence of more definitive indications of legislative approval.

IV.

The more evenly balanced the contending arguments, the more likely it is that the court will resort to a formality in resolving the substantive dispute described in its opinon. Similarly, the demand for substantive judicial neutrality can become a requirement that formal judicial proprieties be observed rigorously, a sentiment reflected in the last sentence of the Brennan opinion: "The simple fact is that to affirm the conviction without an adequate instruction would be tantamount to directing a verdict of guilty, and that we plainly may not do."[36]

Justice Blackmun, whose dissent was joined by Justice Marshall, avoids the difficulty presented by the arguably inadequate jury instruction. He accepts the court of appeals' analysis of federal securities laws as having "created a system providing equal access to the information necessary for reasoned and intelligent investment decisions."[37] Given this postulate, it follows that "petitioner's conduct [would be] fraudulent within the meaning of § 10(b) . . . even if he had obtained the blessing of his employer's principals before embarking on his profiteering scheme."[38] The validity of the postulate is established, says Justice Blackmun, in "my opinion . . . for the Court" in *Affiliated Ute Citizens*

34. H. WECHSLER, *Toward Neutral Principles of Constitutional Law*, in PRINCIPLES, POLITICS, AND FUNDAMENTAL LAW 3, 37 (1961).
35. *Id.* at 45-46.
36. 445 U.S. at 239 (Brennan, J., concurring in the judgment).
37. 588 F.2d at 1362.
38. 445 U.S. at 246 (Blackmun, J., dissenting).

v. United States,[39] which "held that bank agents dealing in the stock of a Ute Indian development corporation had a duty to reveal to mixed-blood Indian customers that their shares could bring a higher price on a non-Indian market of which the sellers were unaware," and which therefore "lends strong support to the principle that a structural disparity in access to material information is a critical factor under Rule 10b-5 in establishing a duty either to disclose the information or to abstain from trading."[40]

Justice Blackmun fails to note that the corporation in question was created by the federal government to hold Indian assets as part of a program aimed at ending the system of reservations by acquainting Indians with a market economy. Given that context, it may well have been inappropriate to assume that mixed-blood Indians would know that the bank agents purchased their shares only on the assumption that buyers willing to pay higher prices could be found for the stock. In the absence of such a context, however, a market in which no structural disparities exist represents, not an existing institution, but simply an analytic construct.[41] For a market to function, individuals must agree to transactions each party regards as profitable. At the moment they agree to enter such transactions, however, not only do the parties by definition possess "inside" information, but, except in rare cases, profit will elude at least one of them. As a result, the market will continue to function only as long as participants believe that they possess information or occupy positions better, at the margin, than those available to other participants.

What has been described is the mechanism of a market, and it is this mechanism that the federal securities laws attempt to regulate. In connection with the distribution of securities, for example, the Securities Act of 1933[42] provides a highly detailed body of rules applied to underwriters and traders who are "making" markets, and the precision of the Securities Act is replicated in the description of persons and situations covered by section 16(b) of the Securities Exchange Act of 1934,[43] which bans profits derived from "inside" information. Section 10(b), on the other hand, was specifically drafted in sufficiently open-ended terms to be applicable to situations whose novelty would permit undesirable conduct to elude more precisely drafted regulations. Stat-

39. 406 U.S. 128 (1972).
40. 445 U.S. at 250-51 (Blackmun, J., dissenting).
41. *See* Deutsch, *The New Deal and the Burger Court: The Significance of* United States v. Chiarella, 57 TEXAS L. REV. 965, 969-70 (1979).
42. 15 U.S.C. §§ 77a-77aa (1976).
43. 15 U.S.C. § 78p(b) (1976).

utes such as section 10(b), because their terms are open-ended, permit litigants to use the judicial process in an attempt to achieve results contrary to the intent of Congress. In the case of section 10(b), the judicial response to such attempts took the form of reading into the statute limitations based on common law fraud such as reliance, scienter, and materiality.

The technical nature of the issues by which the boundaries of section 10(b) were judicially delineated served to shield lower court opinions from Supreme Court review, and since litigation concerning securities law was centered in the Southern District of New York, the Second Circuit functioned as the de facto Supreme Court on the interpretation of section 10(b). *SEC v. Texas Gulf Sulphur Co.*[44] was the en banc decision perceived by the bar as the Second Circuit's definitive exposition of the law of section 10(b). In that case, the court held that "insider trading activity . . . constitutes . . . the only truly objective evidence of the materiality" of the inside information there at issue.[45] The court reversed a District Court's finding of lack of materiality (based on the uncontradicted testimony of expert witnesses), on the ground that "Rule [10b-5] is based in policy on the justifiable expectation of the securities marketplace that all investors trading on impersonal exchanges have relatively equal access to material information."[46]

Chiarella does not help in determining whether *Blue Chip* in fact overruled such developments as *Texas Gulf Sulphur*'s de facto elimination of materiality as an element of a section 10(b) action against corporate insiders. Even the meaning of the *Chiarella* holding itself remains unclear. As the Chief Justice notes:

> There is some language in the Court's opinion to suggest that only "a relationship between petitioner and the sellers . . . could give rise to a duty [to disclose]." . . . The Court's holding, however, is much more limited, namely that mere possession of material nonpublic information is insufficient to create a duty to disclose or to refrain from trading . . . . Accordingly, it is my understanding that the Court has not rejected [my] view . . . that an absolute duty to disclose or refrain arises from the very act of misappropriating nonpublic information.[47]

44. 401 F.2d 833 (2d Cir. 1968), *cert. denied*, 404 U.S. 1005 (1971).
45. *Id.* at 851.
46. *Id.* at 848.
47. 445 U.S. at 243 n.4 (Burger, C.J., dissenting) (quoting 445 U.S. at 232).

V.

Since Justice Powell's opinion leaves open the validity of the misappropriation theory advanced by the Chief Justice, whether that theory is eventually adopted will clarify the meaning of the majority's holding that a consideration of the jury instructions would have been premature. What the *Chiarella* opinion stresses is that

> [t]he dissent of THE CHIEF JUSTICE rely[d] upon a single phrase from the jury instructions, which states that the petitioner held a "confidential position" at Pandick Press, to argue that the jury was properly instructed on the theory "that a person who has misappropriated material nonpublic information has an absolute duty to disclose that information or refrain from trading."[48]

The question presented is whether a few words contained in the instructions of a trial judge can legitimate a conviction in the circumstances presented in *Chiarella*. The majority held to the contrary:

> The conviction would have to be reversed even if the jury had been instructed that it could convict the petitioner either (1) because of his failure to disclose material, nonpublic information to sellers or (2) because of a breach of a duty to the acquiring corporation. We may not uphold a criminal conviction if it is impossible to ascertain whether the defendant has been punished for noncriminal conduct.[49]

In the very Holmes lecture that criticized the Warren Court for unwarrantedly sweeping readings of constitutional guarantees, on the other hand, Herbert Wechsler based the legitimacy of judicial review on the existence of a few words in the constitutional text.[50]

A willingness to regard the exercise of power as legitimate so long as authorizing words can be found ultimately rests on the view that the function of legal words is to draw lines "[whose] meaning . . . is that you intentionally may go as close to it as you can if you do not pass it."[51] This phrase was written by Justice Holmes and quoted by the New York Court of Appeals in dismissing a shareholder action against directors who controlled two corporations, one of which was a public utility. The directors had authorized large intercorporate loans to that utility at favorable rates for periods of less than one year, but invariably extended the terms of such loans despite a law providing that all indebtedness "payable at periods of more than twelve months" re-

48. *Id.* at 237 n.21 (quoting 445 U.S. at 240 (Burger, C.J., dissenting)).
49. *Id.*
50. H. WECHSLER, *supra* note 34, at 5-7.
51. Superior Oil Co. v. Mississippi, 280 U.S. 390, 395-96 (1930).

quired the approval of the Public Service Commission.[52]

Holmes himself dealt with the duties of corporate insiders in *Bates v. Dresser*,[53] which concerned "a bill in equity, brought by the receiver of a national bank, to charge its former president and directors with the loss of a great part of its assets through the thefts of an employee of the bank while they were in power."[54] Although the particular fraud at issue "was a novelty in the way of swindling a bank, so far as the knowledge of any experience had reached [the town in which the bank was located],"[55] Holmes held Dresser, the president, liable because "[the losses] that happened were chargeable to his fault, after he had warnings that should have led to steps that would have made fraud impossible."[56]

In an analogous case, *Barnes v. Andrews*,[57] involving a bill of equity attempting to hold a director liable on a theory of "general inattention to his duties as a director,"[58] Judge Learned Hand, while concluding that "I cannot acquit [the director] of misprision in his office,"[59] declined to hold him liable because "I pressed [counsel] to show me a case in which the courts have held that a director could be charged generally with the collapse of a business in respect of which he had been inattentive, and I am not aware that he has found one."[60]

The insistence upon precedent as the justification for imposing liability—because it requires that defendant's behavior be judged in terms of standards applicable at the time he acted—prevented Hand from establishing standards that could legitimately be applied to future behavior. In *Dresser* Holmes acknowledged his responsibility not to "magnif[y] unduly" the "hints and warnings"[61] on the basis of which he found liability, but characterized the situation facing him as involving "[Dresser's] invincible repose upon the status quo."[62]

Holmes relies on the following evidence:

> [O]ne Fillmore learned that a package containing $150 left with the bank for safekeeping was not to be found, told Dresser of the loss, wrote to him that he could but conclude that the package

52. Everett v. Phillips, 288 N.Y. 227, 235, 43 N.E.2d 18, 21 (1942).
53. 251 U.S. 524 (1920).
54. *Id.* at 526.
55. *Id.* at 529.
56. *Id.* at 531.
57. 298 F. 614 (S.D.N.Y. 1924).
58. *Id.* at 615.
59. *Id.* at 616.
60. *Id.* Hand believed that the plaintiff also had to prove "that the performance of the defendant's duties would have avoided loss, and what loss it would have avoided." *Id.*
61. 251 U.S. at 530.
62. *Id.*

> had been destroyed or removed by someone connected with the bank, and in later conversation said that it was evident that there was a thief in the bank. He added that he would advise the president to look after [the suspected employee], that he believed he was living at a pretty fast pace, and that he had pretty good authority for thinking that he was supporting a woman. In the same year, or the year before, [the employee], whose pay was never more than $12 a week, set up an automobile, as was known to Dresser and commented on unfavorably to him. There was also some evidence of notice to Dresser that [the employee] was dealing in copper stocks.[63]

The evidence, though arguably insufficient, is, in the context of the opinion, persuasive. As is most clearly demonstrated in his well-known first amendment analysis based on the false cry of "Fire!" in a theater,[64] it was Holmes' style to persuade, not by detailing the facts or law of the case before him, but by sketching the striking vignette. It was a style that worked as all good stories work, not by retailing the murky and confusing truth of how things are, but by confirming our felt certainties about how we know they should be.

The contrast of Holmes' style with Hand's is underlined in the area of first amendment law in the *Dennis* case,[65] in which Hand defends his formulation of a test holding that "the gravity of the 'evil,' discounted by its improbability, justifies such invasion of free speech as is necessary to avoid the danger."[66] The justification is that

> [w]e can never forecast with certainty; all prophecy is a guess, but the reliability of a guess decreases with the length of the future which it seeks to penetrate. In application of such a standard courts may strike a wrong balance; they may tolerate "incitements" which they should forbid; they may repress utterances they should allow; but that is a responsibility that they cannot avoid. Abdication is as much a failure of duty, as indifference is a failure to protect primal rights.[67]

It is unclear how these words improve on the phrase "clear and present danger," although the formulaic phrasing gives the impression of a greater degree of clarity and precision.

It is crucially important to the decision of the *Chiarella* majority that *Cady, Roberts* be read as emphasizing violation of a fiduciary relationship rather than occupation of a strategic position in the market mechanism. In Powell's opinion, that reading is justified:

63. *Id.* at 530-31.
64. Schenck v. United States, 249 U.S. 47, 52 (1919).
65. United States v. Dennis, 183 F.2d 201 (2d Cir. 1950), *aff'd*, 341 U.S. 494 (1951).
66. *Id.* at 212.
67. *Id.*

> The [Securities and Exchange] Commission embraced the reasoning of Judge Learned Hand that "the director or officer assumed a fiduciary relation to the buyer by the very sale; for it would be a sorry distinction to allow him to use the advantage of his position to induce the buyer into the position of a beneficiary although he was forbidden to do so once the buyer had become one."[68]

The quoted language, because it encompasses both a relationship and a position, leaves unclear whether the majority's or dissent's view about the applicability of section 10(b) to "market insiders" will in the future constitute the meaning of the *Chiarella* precedent.

Similarly ambivalent was Hand's participation in judging the events at issue in *Birnbaum v. Newport Steel Corp.*[69] The corporation had complied with government requests not to raise steel prices despite the existence of a market shortage produced by the outbreak of the Korean War. After negotiations concerning a stock-for-stock merger had been broken off, however, the controlling shareholder sold his shares at a premium well above the market price to a corporation whose stockholders were users of steel. A panel including Learned Hand dismissed an attack on the transaction based on section 10(b) in *Birnbaum*. Thereafter suit was brought in *Perlman v. Feldmann*,[70] alleging that, under the circumstances presented, part of the premium received for control of the corporation constituted a violation of the controlling shareholder's common law fiduciary duties.[71]

Selected as a member of the panel designated to hear the case in the Court of Appeals, Hand, on October 12, 1954, circulated a memorandum in which he indicated the basis on which he would reverse the trial judge, who had rendered judgment for the defendants:

> Hincks, J., seemed to question whether, since the transaction was "unethical," the court would hold its nose and compel Feldmann to disgorge. I suppose he was thinking of the bill for an accounting by one highwayman against another that Popham, J., entertained; but on this occasion it was the other shareholders that Feldman deprived of a benefit, and they were not personally implicated. Besides, the fault, if it was one, was not of a kind that stank so much in the nose of the court that the fiduciary could keep his swag.[72]

68. 445 U.S. at 227 n.8 (quoting Gratz v. Claughton, 187 F.2d 46, 49 (2d Cir.), *cert. denied*, 349 U.S. 952 (1955)).

69. 193 F.2d 461 (2d Cir.), *cert. denied*, 343 U.S. 956 (1952).

70. 219 F.2d 173 (2d Cir.), *cert. denied*, 349 U.S. 952 (1955).

71. For further discussion of *Perlman*, see Deutsch, *Politics, Economics, and Corporate Power: The Challenge of Bureaucracy*, 58 TEXAS L. REV. 777 (1980).

72. Papers of Charles E. Clark, collected at the Yale Law School Library.

On December 27, 1954, counsel were informed that Judge Hand "had determined that he should hold himself disqualified."[73] Although his son-in-law was a member of a law firm representing the defendants, it is difficult to believe that Hand had delayed consideration of the implications of that fact for almost three months after argument in the case. It is more likely, therefore, that he was dissatisfied with his position. Successfully distinguishing the precedents relied on by one's opponents does not, of course, establish the validity of one's own arguments, and *Barnes*[74] is testimony to the importance Hand attached to firm precedential support for judicial action. It should be remembered, in this connection, that Wechsler, when he rooted the power of judicial review in the constitutional text, was in part replying to Learned Hand, who, in an earlier Holmes lecture,[75] had confessed himself totally unable to legitimate judicial acts overriding decisions of institutions that derived their powers directly from the electorate.

VI.

Even if it be granted that the vignettes employed by Holmes in arriving at a decision tell less of the truth about the matter being adjudicated than Hand's detailed analyses, that concession is an insufficient basis on which to assess Hand as more successful than Holmes in filling the judicial role. Readers of literature, especially if they think a work worthy of repeated readings, will at some point find the story contrived, but that fact does not lessen the meaning of what they read, as long as the words reveal something to the reader that was not previously apparent.

Insofar as the writer's individual perception of the truth differs from that of the reader, the story will not succeed, and it was the risk of that failure which Hand's insistence on precedential support sought to avoid. As Holmes' tenure on the Supreme Court demonstrates, however, it is precisely this risk that is always involved in the creation of a significant precedent, in the making of law.

73. *Id.*
74. *See* text accompanying notes 57-60 *supra*.
75. L. HAND, THE BILL OF RIGHTS 1-30 (1958).