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Financial Reporters, the Securities Laws and the First Amendment: Where to Draw the Line

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INTRODUCTION

Congress included various antifraud provisions in the securities laws¹ to protect the investing public by ensuring the disclosure of material in-

1. The Securities Act of 1933, ch. 38, 48 Stat. 74 (1933) (codified as amended at 15 U.S.C. §§ 77a to 77aa (1982)) contains several antifraud provisions: §§ 17(a), 11 and 12. Section 17(a) makes it unlawful to sell securities by misrepresenting or omitting material facts or by engaging in fraudulent practices. See 15 U.S.C. § 77q(a) (1982). Section 11 permits a purchaser to sue specified defendants if the registration statement contains "an untrue statement of a material fact or [omission of] . . . a material fact . . . necessary to make the statements therein not misleading." 15 U.S.C. § 77k (1982); see 5 A. Jacobs, The Impact of Rule 10b-5, § 3.01[a], at 1-26; L. Loss, Fundamentals of Securities Regulations 96 (1983) [hereinafter cited as Loss I]. Section 12(1) imposes civil liability on any person who "offers or sells a security" in violation of the prospectus requirements of section 5, see 15 U.S.C. § 77l (1), and section 12(2) provides that any person who offers or sells a security by means of a prospectus or verbal communication that includes a misrepresentation or omission of a material fact shall be liable for rescission or damages, see 15 U.S.C. 77l (2); Loss I, supra, at 96.


Section 10(b) states:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange . . .

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Id. § 78j(b).

Rule 10b-5 was promulgated under section 10(b) in 1942 by the Securities and Exchange Commission (SEC) and states:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.


Section 10(b) has been held to provide an implied private right of action. See, e.g., Superintendent of Ins. v. Bankers Life & Cas. Co., 404 U.S. 6, 13 n.9 (1971); Fischman v. Raytheon Mfg. Co., 188 F.2d 783, 787 (2d Cir. 1951); Kardon v. National Gypsum Co., 69 F. Supp. 512, 513-14 (E.D. Pa. 1946). The section and rule permit only defrauded purchasers and sellers of securities to sue. See Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 730-31 (1975); Seigal v. Merrick, 422 F. Supp. 1213, 1217 (S.D.N.Y. 1976);
formation. One such provision, section 10(b) of the Securities Exchange Act of 1934, seeks to stop the use of manipulative devices and to guarantee that no single group of traders enjoys unfair informational advantages over the rest of the market. Recent Supreme Court decisions have nar-

5 A. Jacobs, supra, § 3.01[d], at 1-46; see also Dasho v. Susquehanna Corp., 461 F.2d 11, 24 (7th Cir.) (rule protects purchasers and sellers), cert. denied, 408 U.S. 925 (1972).


4. See, e.g., SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 848 (2d Cir. 1968) (en banc) (rule based on policy "that all investors trading on impersonal exchanges have relatively equal access to material information"), cert. denied, 394 U.S. 976 (1969); O'Brien v. Continental Ill. Nat'l Bank & Trust Co., 431 F. Supp. 292, 296 (N.D. Ill.) ("purpose of rule . . . [is] to insure that all persons making investment decisions have full and accurate information"), appeal dismissed, 566 F.2d 1175 (7th Cir. 1977); Jackson v. Oppenheim, 411 F. Supp. 659, 665 (S.D.N.Y. 1974) ("intent of Congress in passing . . . [antifraud provisions] was to provide equal access to material information"), aff'd in part, rev'd in part on other grounds, 533 F.2d 826 (2d Cir. 1976); In re Penn Cent. Sec. Litig., 357 F. Supp. 869, 876 (E.D. Pa. 1973) (section designed to protect the "purity" of the buying and selling process and to ensure full disclosure to investors), aff'd, 494 F.2d 528 (3d Cir. 1974); S. Goldberg, SEC Trading Restrictions and Reporting Requirements for Insiders 6 (1973) (purpose is to provide "informational equality"); 5 A. Jacobs, supra note 1, § 6.05, at 1-137 to 40 (purpose of rule is to encourage disclosure of information). Courts have inferred various other purposes behind the section and the rule. See, e.g., Rochelle v. Marine Midland Grace Trust Co., 535 F.2d 523, 532 (9th Cir. 1976) (purpose of section is "to protect the purity of the securities market"); Tomera v. Galt, 511 F.2d 504, 510 (7th Cir. 1975) (to achieve a "high standard of business ethics"); Sargent v. Genesco, Inc., 492 F.2d 750, 760 (5th Cir. 1974) ("to protect investors and instill confidence in the securities markets by penalizing unfair dealings"). One reason for this multiplicity of views is that there is very little legislative history discussing section 10(b). See 1 A. Bromberg & L. Lowenfels, Securities Fraud & Commodities Fraud § 2.2, at ¶ 331 (1984); 5 A. Jacobs, supra note 1, § 5, at 1-121. According to Thomas G. Corcoran, a witness at hearings held by the House Interstate and Foreign Commerce Committee, section 10(b) (or section 9(c), as it was then called, see Loss I, supra note 1, at 821) is a "catch-all clause to prevent manipulative devices." Stock Exchange Regulation: Hearing on H.R. 7852 and H.R. 8720 Before the House Comm. on Interstate and Foreign Commerce, 73d Cong., 2d Sess. 115 (1934) [hereinafter cited as Stock Exchange Hearing], reprinted in 8 J. Ellenberger & E. Mahar, Legislative History of Securities Act of 1933 and Securities Exchange Act of 1934, at 115 (1973); accord Ernst & Ernst v. Hochfelder, 425 U.S. 185, 203 (1976). Other witnesses, however, were unclear on the exact scope of the section and were troubled by its vagueness. See Stock Exchange Hearing, supra, at 305 (Frank R. Hope, Pres. of the Ass'n of Stock Exch. Firms, New York, N.Y., stating that the section "might be construed to mean almost anything"), reprinted in 8 J. Ellenberger & E. Mahar, supra, at 305; id. at 258 (statement of Eugene E. Thompson, Pres., Associated Stock Exchs., Washington, D.C., noting that "[t]his subsection is so vague and inadequate for the purpose it evidently is intended to accomplish that it should be stricken out in its entirety"); reprinted in 8 J. Ellenberger & E. Mahar, supra, at 258.
rowed the reach of section 10(b) by predicking liability on the existence of a fiduciary duty running from the defendant to a purchaser or seller. The Securities and Exchange Commission (SEC) and at least one court, however, have attempted to expand section 10(b)'s scope by extending liability to financial reporters who engage in manipulative practices such as "scalping"—using advance knowledge of the timing of their newspaper articles to trade in securities or to enable others to do so. To justify this result, a general duty to readership has been proposed. Because this


6. The pending case of United States v. Winans, No. 84-CR-605 (S.D.N.Y.) is an example of the SEC's views on financial reporters. R. Foster Winans, formerly a reporter for the Wall Street Journal's "Heard on the Street" column, allegedly told friends, in exchange for money, that favorable comments about various securities would be appearing in the paper. The SEC's original civil action was based in part on a theory that Winans owed a duty to his readers to disclose his intent to profit from publication of the article. See N.Y. Times, May 19, 1984, at 31, cols. 4-5; Wall St. J., May 18, 1984, at 2, col. 2. Although this theory was dropped from the criminal case, see Wall St. J., Oct. 11, 1984, at 2, col. 3, it remains a part of the SEC's civil suit against Winans. See N.Y. Times, Oct. 23, 1984, at D31, col. 3. The duty to readership theory represents the SEC's current thinking, and the agency has publicly announced its intention to continue to subject journalists to liability under this theory. See Mathews & Levine, First Amendment Problems Complicate SEC Enforcement, N.Y.L.J., Dec. 10, 1984, at 44, col. 5; N.Y. Times, Oct. 23, 1984, at D31, col. 3. The SEC has approved this theory under other circumstances, see, e.g., Letter from SEC to J.T. Rybolz (May 6, 1982) (available on LEXIS, Fedsec library, Noact file), and brought a prior case against a journalist engaged in such practices, see SEC v. Campbell, [1972-1973 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,580, at 92,703 (C.D. Cal. July 24, 1972).

7. See Zweig v. Hearst Corp., 594 F.2d 1261, 1268-69 (9th Cir. 1979).

8. Scalping involves the "purchase of securities by a person in a position to influence others by his recommendation or favorable commentary on that security, the recommendation of that security to investors, and the sale of that security after capital appreciation." Peskind, Regulation of the Financial Press: A New Dimension to Section 10(b) and Rule 10b-5, 14 St. Louis U.L.J. 80, 81 (1969). It is normally an activity associated with investment advisors. See, e.g., SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 181 (1963) (scalping is the practice whereby an investment advisor purchases securities for own account, recommends securities to clients and then sells following the recommendation); Mathews & Levine, supra note 6, at 44, col. 3 (scalping is a violation of investment advisors' duties to advisory clients). The term has also been applied to activities by journalists. See Zweig v. Hearst Corp., 594 F.2d 1261, 1265 (9th Cir. 1979) (plaintiffs defined scalping as buying stock shortly before columns about companies were published and then selling "after the columns caused a jump in the market price"); Kotler, Reporter Charged with Insider Trading, 5 Cal. Law., Feb. 1985, at 44, 46 (SEC spokesman says scalping is taking a position in a particular stock and then disseminating information that supports the position).

9. In Winans, the government is not accusing the defendant of taking positions in securities and then selling after the appearance of the article. Rather, he is accused of profiting from revealing in advance the timing and subject matter of his column. See Kotler, supra note 8, at 46-47; N.Y. Times, May 19, 1984, at 37, col. 4; Wall St. J., May 18, 1984, at 20, col. 1.

novel concept of duty was unknown at common law,\textsuperscript{11} such attempts to fit journalists within the Court’s fiduciary framework are inappropriate. Congress, however, through the recently enacted Insider Trading Sanctions Act of 1984,\textsuperscript{12} has indicated its intent to stop such manipulative practices by financial reporters.\textsuperscript{13}

Part I of this Note argues that journalists cannot be held liable under current interpretations of section 10(b). Part II, after examining the intent behind the Insider Trading Sanctions Act of 1984, concludes that Congress’ purpose would best be effectuated by subjecting journalists to liability under section 10(b). Part III explores the SEC’s suggested disclosure remedy and the first amendment problems it raises, and then suggests a solution that will reconcile these two important interests.

I. CURRENT THEORIES OF LIABILITY UNDER SECTION 10(b) AND THEIR INAPPLICABILITY TO JOURNALISTS

A. The Fiduciary Duty and Misappropriation Theories

Section 10(b) prohibits the use of any “manipulative or deceptive device” in connection with the purchase or sale of a security.\textsuperscript{14} Rule 10b-5 promulgated thereunder creates liability for an omission of a material fact if the omission makes a statement misleading.\textsuperscript{15} Traditionally, an affirmative duty to disclose was imposed only on the corporate insider—an officer, director or controlling shareholder with access to corporate information not available to ordinary shareholders.\textsuperscript{16} Later cases sometimes took a different approach, imposing a broad duty to disclose on all participants in a market transaction.\textsuperscript{17} Recent decisions have nar-

\textsuperscript{11} See infra notes 48-66 and accompanying text.
\textsuperscript{13} See infra notes 80-95 and accompanying text.
\textsuperscript{16} It is well established that directors, officers and controlling or major shareholders are corporate insiders for the purposes of § 10(b) and rule 10b-5. See, e.g., Moss v. Morgan Stanley, Inc., 719 F.2d 5, 10 & n.8 (2d Cir. 1983), cert. denied, 104 S. Ct. 1280 (1984); Reed v. Riddle Airlines, 266 F.2d 314, 315 (5th Cir. 1959); Chelsea Assocs. v. Rapanos, 376 F. Supp. 929, 932, 939 (E.D. Mich. 1974), aff'd, 527 F.2d 1266 (6th Cir. 1975); Tully v. Mott Supermarkets, Inc., 337 F. Supp. 834, 850 (D.N.J. 1972); Kuehnert v. Texstar Corp., 286 F. Supp. 340, 344 (S.D. Tex. 1968), aff'd, 412 F.2d 700 (5th Cir. 1969).
\textsuperscript{18} See United States v. Chiarella, 588 F.2d 1358, 1365 (2d Cir. 1978) (anyone regularly receiving material nonpublic information has affirmative duty to disclose), rev'd, 445 U.S. 222 (1980); SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 848 (2d Cir. 1968) (en
rowed the scope of liability by requiring that the duty to disclose be predicated on the existence of a fiduciary relationship. This fiduciary analysis is not required in cases involving traditional corporate insiders because their status as fiduciaries has long been established. It is only in cases involving so-called "outsiders" that such reasoning is necessary.

For example, the Supreme Court, in Chiarella v. United States, employed the fiduciary duty analysis. In Chiarella, the defendant, an employee of a financial printer, was responsible for printing notices of takeover bids. The names of the target companies had been left blank, but the defendant deduced them and purchased stock in the companies immediately before the takeovers were announced publicly. In holding that Chiarella had not violated section 10(b), the Court rejected the argument that a broad duty existed among all market participants, holding

This broad concept of duty appears to stem from the seminal case of In re Cady, Roberts & Co., 40 S.E.C. 907 (1961). In Cady, Roberts, a director of a corporation who was also a registered representative of a brokerage firm received information that the corporation's dividend would be reduced. Before the public was informed, the director disclosed the information to one of his partners, a broker who sold large amounts of corporate stock held by his and the director's clients. The Commission held that the broker had violated §10(b). The opinion contains a fairly broad two-part test to determine liability under section 10(b):

Analytically, the obligation rests on two principal elements; first, the existence of a relationship giving access, directly or indirectly, to information intended to be available only for a corporate purpose and not for the personal benefit of anyone, and second, the inherent unfairness involved where a party takes advantage of such information knowing it is unavailable to those with whom he is dealing.

Id. (footnote omitted). The flexible language of the test led the courts to interpret it expansively. See SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 848 (2d Cir. 1968) (en banc), cert. denied, 394 U.S. 976 (1969); Outsider Trading, supra, at 600.
that a duty to disclose arises only when a corporate insider breaches a duty to security holders\textsuperscript{27} or when a relationship of trust and confidence exists between parties to a transaction.\textsuperscript{28} In a later case, the Court clarified \textit{Chiarella} by holding that a duty does not stem from mere possession of nonpublic market information, but from the "existence of a fiduciary relationship."\textsuperscript{29}

To conform to the framework developed in \textit{Chiarella},\textsuperscript{30} some courts have endorsed an alternative fiduciary theory, known as misappropriation.\textsuperscript{31} This theory has been applied to facts similar to those of \textit{Chiarella}.\textsuperscript{32} In the typical case, an employee of an investment banking

\begin{itemize}
\item \textsuperscript{27} See \textit{id. at} 230.
\item \textsuperscript{28} See \textit{id.}
\item \textsuperscript{29} \textit{Dirks v. SEC}, 103 S. Ct. 3255, 3261 (1983). Raymond Dirks, an officer of a broker-dealer firm, had received information from a former officer of Equity Funding that the assets of Equity Funding were vastly overstated. \textit{Id.} at 3258. After an investigation, Dirks discussed his findings with clients and members of the press. \textit{Id.} In holding that Dirks had not violated § 10(b), the Court relied on \textit{Chiarella} and again rejected an equal-access to information theory. \textit{See id.} at 3262-63. In addition, the Court created a "temporary insider" rule for those hired by a corporation to work on tender offers, acquisitions or mergers:
\begin{quote}
Under certain circumstances, such as where corporate information is revealed legitimately to an underwriter, accountant, lawyer, or consultant working for the corporation, these outsiders may become fiduciaries of the shareholders. The basis for recognizing this fiduciary duty is not simply that such persons acquired nonpublic corporate information, but rather that they have entered into a special confidential relationship in the conduct of the business of the enterprise and are given access to information solely for corporate purposes.
\end{quote}
\textit{Id.} at 3261 n.14

This special rule might have been used to reconcile misappropriation, see \textit{infra} notes 30-44 and accompanying text, with \textit{Chiarella}'s fiduciary principles. \textit{See Outsider Trading, supra} note 18, at 627-28. The SEC, however, has not relied heavily on the "temporary" or "constructive" insider analysis and has chosen to achieve its aims through the misappropriation theory. \textit{See infra} notes 30-45 and accompanying text.

\item \textsuperscript{30} It has been suggested that the misappropriation theory appears to be a rather contorted legal concept. \textit{See Glaberson, Insider Trading; A Widening Net Catches the Small Fry}, Bus. Wk., Feb. 11, 1985, at 61, col. 1; \textit{Outsider Trading, supra} note 18, at 627. The theory makes sense only by recognizing its relationship to the fiduciary principles embodied in \textit{Chiarella}. Without such recognition, the use of misappropriation becomes a way to punish those who trade on the basis of information not available to others, a proposition rejected in \textit{Chiarella}, 445 U.S. at 233, 235. \textit{See} \textit{Langevoort, Insider Trading and the Fiduciary Principle: A Post-Chiarella Restatement}, 70 Calif. L. Rev. 1, 52 (1982) ("This [view of misappropriation] would bring the law back close to the fairness-based theories that began the federal law of insider trading.").
\item \textsuperscript{32} In United States v. Newman, 664 F.2d 12 (2d Cir. 1981), cert. denied, 104 S. Ct. 193 (1983), for example, employees of an investment banking firm that had been retained by corporations interested in mergers and takeovers acquired confidential information about the mergers and takeovers. \textit{See id.} at 15. They then passed on this information to confederates who purchased and sold securities using the misappropriated data. \textit{Id.; see also SEC v. Materia, 745 F.2d 197, 199 (2d Cir. 1984), cert. denied, 53 U.S.L.W. 3757 (U.S. Apr. 23, 1985)} (employee of financial printer divined names of tender offer targets
firm or financial printer misappropriates confidential information entrusted to the firm by corporate clients or their fiduciaries, such as law firms. The employee uses this information to purchase securities of merger or takeover targets. Although the misappropriation theory was first considered in *Chiarella* itself, the Court declined to pass on its validity. The theory is understood best by viewing it as a means of transferring to the noninsider defendant the corporation's fiduciary duty to its security holders. By stealing information that belongs to the corporate client, the employee has violated his fiduciary duty to the em-

... and used information as basis for purchasing securities in those companies); SEC v. Musella, 578 F. Supp. 425, 431-32, 438-41 (S.D.N.Y. 1984) (manager of office services at law firm misappropriated information about acquisitions, takeovers and reorganizations entrusted to firm by corporate clients and passed stolen information to friends, who used it to purchase securities).

United States v. Reed, 601 F. Supp. 685 (S.D.N.Y. 1985), is the only misappropriation case with a slightly different fact pattern. In *Reed*, the son of a director of Amax, Inc. allegedly received from his father information in confidence about the proposed merger of Amax into Standard Oil Company of California. See id. at 689-90. He then purchased Amax stock call options on the basis of the confidential information. *Id.* at 690-91. In denying a motion to dismiss, the court held that whether there was a relationship of trust and confidence between the son and father sufficient to satisfy the misappropriation theory was a question of fact. See *id.* at 717-18. Although this fact pattern is different, it fits into the misappropriation analysis that is developed later in this Note. See *infra* text accompanying notes 33-45.

33. See *supra* note 32 and accompanying text.


35. *Id.* at 236. Several different views of the misappropriation theory were set out in *Chiarella*. The majority, in its limited discussion, correctly discerned that the theory rests on an ultimate duty to "the acquiring corporation" owed by a printer employed "by the corporation." *Id.* at 235. See *infra* text accompanying notes 36-45. In a brief concurrence, Justice Stevens took a similar stance, suggesting that there is a "duty of silence . . . owed to [an] employer and to [the] employer's customers." *Id.* at 238 (Stevens, J., concurring). He also noted that although a breach of that duty might constitute fraud on the acquiring corporation, liability under § 10(b) would not inevitably result, because the acquiring corporation was neither a purchaser nor seller of the securities of the target company. See *id.* (Stevens, J., concurring). Chief Justice Burger, in his dissent, set forth a much more expansive concept, one requiring no breach of any fiduciary duty: "I would read § 10(b) and Rule 10b-5 to encompass and build on this principle: to mean that a person who has misappropriated nonpublic information has an absolute duty to disclose that information or to refrain from trading." *Id.* at 240 (Burger, C.J., dissenting). For discussions of Burger's theory, see Langevoort, *supra* note 30, at 15-16; *Outsider Trading*, *supra* note 18, at 605-06.

36. Lower courts' analyses of the misappropriation theory have been inconsistent. In United States v. Newman, 664 F.2d 12 (2d Cir. 1981), *cert. denied*, 104 S. Ct. 193 (1983), the court adopted a two-step duty consistent with the *Chiarella* majority. See *supra* note 35 and accompanying text. The *Newman* court stated:

By sullying the reputations of . . . employers as safe repositories of client confidences, [defendant] and his cohorts defrauded those employers as surely as if they took their money. . . .

[Defendant] and his cohorts also wronged [the employers'] clients, whose takeover plans were keyed to target company stock prices fixed by market forces, not artificially inflated through purchases by purloiners of confidential information.

*Id.* at 17. The *Newman* court noted the two-step nature of the misappropriation theory, recognizing that the ultimate effect of misappropriation was to drive up the price of the
ployer and has caused the employer to violate its duty to the corporate target company's shares, thus damaging the offering corporation's tender offer plans. See id. at 17-18.

Subsequent cases, however, either did not follow the Newman reasoning or simply misinterpreted it. In United States v. Materia, 745 F.2d 197 (2d Cir. 1984), cert. denied, 53 U.S.L.W. 3757 (U.S. Apr. 23, 1985), for example, the court relied on Chief Justice Burger's dissent in Chiarella, see supra note 35, stating that Materia "misappropriated—stole to put it bluntly—valuable nonpublic information entrusted to him in the utmost confidence." Id. at 201 (quoting Chiarella v. United States, 445 U.S. 222, 245 (1980) (Burger, C.J., dissenting)). The Materia court however, employed a variation of the Stevens view in its holding: "[O]ne who misappropriates nonpublic information in breach of a fiduciary duty and trades on that information to his own advantage violates Section 10(b) and Rule 10b-5." Id. at 203. See supra note 35.

In SEC v. Musella, 578 F. Supp. 425 (S.D.N.Y. 1984), the court floundered among several theories. The court first rejected the notion that the defendant could be held liable as a "temporary insider," see supra note 29, reasoning that even if defendant owed a fiduciary duty to shareholders of the offering company, the stock purchased was that of the target corporation, and no duty was owed to shareholders of that corporation. See id. at 436-37. After alluding to Justice Stevens' concurrence, see id. at 437 n.11, the Chiarella majority's view of misappropriation, see id. at 437, and the Newman binary analysis, see id. at 437-38, the court concluded with a paragraph that seemingly constituted a ringing endorsement of both Chief Justice Burger's dissent and the broad duty to disclose theory:

From Newman . . . and Materia, the general principle emerges that Rule 10b-5 liability may be imposed on those who trade on the basis of material nonpublic information tainted by the breach of an insider's fiduciary duty, regardless of whether that duty runs to the sellers of the securities involved. By endorsing . . . [the] "misappropriation" [theory] . . . the Second Circuit gave legal effect to the commonsensical view that trading on the basis of improperly obtained information is fundamentally unfair . . . .

Id. at 438. At the end of the opinion the court returned to the "temporary insider" concept and, in seeming contradiction to its earlier pronouncements, noted that the defendant had become a temporary insider for the purposes of misappropriation. See id. at 439. Although the court made no attempt to reconcile the opinion's internal inconsistencies, its conclusion might be interpreted as meaning that no duty need flow to the actual defrauded purchasers or sellers for liability to attach under misappropriation; rather, under the court's view, use of the misappropriation theory confers on a defendant a general duty to the market.

In United States v. Reed, 601 F. Supp. 685 (S.D.N.Y. 1985), the court endorsed the notion that only a single fiduciary duty is required under the misappropriation theory: [O]utsider trading liability is premised on the common law principle that when a fiduciary profits from confidential information that he had received because of his fiduciary status, he breaches a legal duty to the person or entity that entrusted him with the information. The misappropriation of secret information for personal aggrandizement in breach of such a relationship constitutes fraud.

Id. at 700.

The confusion within the Second Circuit stems from a basic misunderstanding of the misappropriation theory. See supra notes 31-35, infra notes 37-45 and accompanying text. Although the Materia, Musella and Reed courts all misunderstood the misappropriation theory, they apparently reached correct results. In each case, a defendant violated a fiduciary duty or duty of trust and confidence owed to an employer or, in the case of Reed, to a corporate insider. In turn, the defendant's violation caused the employer or insider to violate a duty to a corporation. The defendants thus took on the fiduciary duty owed by the corporation to its shareholders. There was therefore no need to resort to inconsistent and contorted reasoning. Only the financial reporter should escape liability. See infra notes 67-70 and accompanying text.

37. See infra notes 67-69 and accompanying text.
Fiduciary duty is traced from employee to employer to corporation, and the employee becomes a substitute for the corporation, taking on its fiduciary responsibility to security holders. Thus, the existence of the second duty—the employer's duty to its client—is crucial in imposing liability.

Several courts have mistakenly expanded the misappropriation theory by asserting that it applies to all breaches of fiduciary duty occurring in the context of securities transactions. For example, assume that a law clerk to a Supreme Court Justice, aware that a decision favorable to X Corporation will be handed down within the week, buys securities of X Corporation. The clerk—an employee—has breached a fiduciary duty to the Justice—the employer. Courts with a mistaken view of misappropriation would find that the breach of this duty is sufficient to warrant liability under section 10(b). It is clear from the principles enunciated in Chiarella, however, that such an interpretation is incorrect. The Justice does not have a fiduciary or similar duty to X Corporation. Unless a duty is traced back to the corporation, the employee cannot assume the corporation's fiduciary duty to its security holders.

B. Journalists and Section 10(b) Theories of Liability

The Chiarella Court recognized two relationships that mandate a duty to disclose: the corporate insider's duty to security holders, or some

38. The employer's duty to a corporate client is that of agent to principal. See infra notes 67-69 and accompanying text.

39. As previously discussed, see supra note 36 and accompanying text, after Chiarella, only the Newman case correctly interpreted the misappropriation theory. See United States v. Newman, 664 F.2d 12, 15-16 (2d Cir. 1981) (defendants “breached the trust and confidence placed in them and their employers by the employers’ corporate clients and the clients’ shareholders”) (emphasis added), cert. denied, 104 S. Ct. 193 (1983); see also SEC v. Musella, 578 F. Supp. 425, 438 (S.D.N.Y. 1984) (“liability may be imposed on those who trade on the basis of material nonpublic information tainted by the breach of an insider’s fiduciary duty”) (emphasis added).

40. See supra note 36 and accompanying text. The SEC has endorsed the mistaken view of misappropriation. See Wall St. J., May 18, 1984, at 20, col. 6 (“[A]lthough one can be very sympathetic to the SEC’s desire to extend the law, the misappropriation theory has to date been applied only where the employer from whom the information was misappropriated was in a fiduciary relationship with an issuer or with a company making a tender offer.”) (quoting lawyer retained by the Wall Street Journal in connection with the Winans case). Mere breach of the employer/employee relationship should not give rise to liability under rule 10b-5. See Outsider Trading, supra note 18, at 629 n.199.

41. A similar hypothetical was suggested in Loss I, supra note 1, at 851. Professor Loss expressed no opinion on whether the situation in the hypothetical constitutes a violation of the securities laws.

42. See infra notes 67-69 and accompanying text.


46. See id. at 230.
other relationship of trust and confidence existing between parties to a market transaction.\textsuperscript{47} A journalist is not a corporate insider because the journalist is not an officer, director or controlling shareholder.\textsuperscript{48} Any duty to disclose must therefore be based on a relationship of trust and confidence among the parties.\textsuperscript{49} Because the journalist and the purchasers and sellers of securities are essentially strangers,\textsuperscript{50} the requisite relationship could be found only if a "duty to readership" were imposed on the journalist.\textsuperscript{51} Although this theory has been endorsed by the Ninth Circuit,\textsuperscript{52} it is contrary to existing common law fiduciary concepts.\textsuperscript{53}

A fiduciary,\textsuperscript{54} such as a trustee\textsuperscript{55} or partner,\textsuperscript{56} is typically one who acts for the benefit of another.\textsuperscript{57} Because of this special relationship, often contractual\textsuperscript{58} and almost always consensual,\textsuperscript{59} the fiduciary owes a duty

\textsuperscript{47} See id.
\textsuperscript{48} See supra note 16. It is possible that a journalist could be an officer, director or controlling shareholder of a corporation. This Note does not address those situations.
\textsuperscript{50} The assumption is that the journalist is not personally acquainted with the sellers or purchasers.
\textsuperscript{51} See infra notes 63-66 and accompanying text.
\textsuperscript{52} See Zweig v. Hearst Corp., 594 F.2d 1261, 1268 (9th Cir. 1979).
\textsuperscript{53} See infra notes 54-62 and accompanying text.
\textsuperscript{54} There is no absolute definition of fiduciary or fiduciary relationship. See Koehler v. Haller, 62 Ind. App. 8, 12, 112 N.E. 527, 528 (1916); Patton v. Shelton, 328 Mo. 631, 645, 40 S.W.2d 706, 712 (1931); Roecher v. Story, 91 Mont. 28, 45, 5 P.2d 205, 210 (1931); Van Sickle v. Keck, 42 N.M. 450, 464-65, 81 P.2d 707, 717 (1938) (Hudspeth, C.J., dissenting); 36A C.J.S. \textit{Fiduciary} 381 (1961). A dictionary definition states that a fiduciary is "[a] person having a duty, created by his undertaking, to act primarily for another's benefit in matters connected with such undertaking." Black's Law Dictionary 563 (5th ed. 1979). A fiduciary can be judicially appointed, such as a guardian or executor, see G. Bogert, The Law of Trusts and Trustees § 13, at 147-48, 152 (rev. 2 ed. 1984), or the relationship may be imposed by statute, see Alessi v. Raybestos-Manhattan, Inc., 451 U.S. 504, 510 n.5 (1981) (ERISA establishes fiduciary standards for plan managers); Vincent v. International Bhd. of Elec. Workers, 622 F.2d 140, 141 (§ 511 of Labor-Management Reporting and Disclosure Act imposes a fiduciary duty on officers and representatives of labor organizations). However, there are certain elements common to all fiduciaries. See infra notes 55-62 and accompanying text.
of good faith and loyalty. The fiduciary must refrain from taking profits that belong to the person to whom the duty is owed. In the corporate context, officers and directors owe the shareholders, as owners of the corporation, the duty to manage it for their benefit.

Although readers may rely on reporters and newspapers to tell the truth, this reliance does not rise to the level of a fiduciary relationship. The reporter is not obliged to refrain from taking advantage of benefits not enjoyed by readers. There is no special relationship, and no duty to act on another’s behalf or account for profits. In addition, the reporter


59. See Valley View Cattle Co. v. Iowa Beef Processors, Inc., 548 F.2d 1219, 1221 (5th Cir.), cert. denied, 434 U.S. 855 (1977); Grace Line v. Todd Shipyards Corp., 500 F.2d 361, 373 (9th Cir. 1974); Courtney v. Remler, 566 F. Supp. 1225, 1230 (D.S.C. 1983), aff’d, 745 F.2d 50 (4th Cir. 1984); Haluka v. Baker, 66 Ohio App. 308, 312-13, 34 N.E.2d 68, 70 (1941); see also Restatement (Second) of Agency §1(1), at 7 (1958) (agency is a consensual relationship); I A. Scott, supra note 55, § 2.8, at 44 (settlor manifests intent to create relationship and trustee assumes duties).


63. See Peskind, supra note 8, at 85 (no statutory or judicial authority stating that member of financial press has fiduciary relationship with readers); Henry, Impropriety or Criminality?, Time, Sept. 10, 1984, at 45 (notion of an implied contract with readers is both sweeping and vague); N.Y. Times, Aug. 29, 1984, at D4, col. 4 (reporter’s ties to readers too “attenuated” to make him legally obligated to them); N.Y. Times, May 19, 1984, at 37, col. 5 (James Goodale, lawyer with Debevoise & Plimpton, stating that reporters have no duty to disclose to readers).

64. Cf. CBS v. Democratic Nat’l Comm., 412 U.S. 94, 117-18 (1973) (broadcast licensees serve as public trustee; newspapers have no such obligations); Curtis, Responsibility for Raising Standards, in The Responsibility of the Press 94 (G. Gross ed. 1966) (although newspapers should have high ethical standards, such standards cannot be imposed by law); Steirman, The Publisher’s Responsibility: A Matter of Public Trust or Private Conscience?, in The Responsibility of the Press 253 (G. Gross ed. 1966) (publisher’s responsibility is strictly a moral one). But see Peskind, supra note 8, at 88-89 (newspaper reporters might be liable on the theory that they breach an “implied warranty of disinterestedness”).

65. A survey of case law indicates that no case has stated that reporters owe a fiduciary duty to readers. Even Zweig v. Hearst Corp, 594 F.2d 1261 (9th Cir. 1979), does not posit a fiduciary duty. Rather, the court indicated that although the reporter does not owe a fiduciary duty under common law, somehow the reporter owes a duty to readers. See id. at 1269; see also Peskind, supra note 8, at 85 (no statutory or judicial authority
has not consented to any fiduciary relationship. Thus, because the reporter is not an insider and has no fiduciary duty to readers, no section 10(b) liability can be found under the rationale of Chiarella.

Similarly, no liability should be found under the misappropriation theory. The relationship between the reporter and the newspaper involves only one fiduciary duty. Just as in other employer/employee relationships, the financial journalist owes the newspaper the duty of loyalty, the duty not to compete, and the duty not to use confidential information for private purposes. The better view of misappropriation, however, requires a second fiduciary duty: one between the employer and its corporate client. Because the newspaper normally owes no fiduciary duty to corporations about which it reports, this essential element is missing and precludes application of the theory. Without the linking of the duties, misappropriation breaks down and becomes, in essence, a way to circumvent Chiarella's rigid fiduciary requirements.

II. THE INSIDER TRADING SANCTIONS ACT OF 1984

Existing theories of liability under section 10(b) do not cover the jour-
nalist engaged in scalping or similar practices. Nevertheless, the harms to investors caused by such practices are exactly of the type Congress intended to prevent when it enacted the original securities laws. The Insider Trading Sanctions Act of 1984 (Act) affirmed Congress' desire to punish persons, such as financial reporters, who, although not classic insiders, trade on the basis of information not publicly available. An examination of the Act's language and legislative history supports this conclusion.

A. Language

The Act is very brief and consists of modifications to the existing securities laws. One of its provisions allows the SEC to seek treble damages against those who trade "while in possession of material nonpublic information." The Act thus bases liability on mere possession of information, a much broader concept than Chiarella's fiduciary duty requirement. This emphasis on possession rather than fiduciary duty does not appear in the text of the original securities laws and indicates an intent to expand section 10(b)'s coverage beyond the narrow confines of Chiarella.

71. See supra notes 47-70 and accompanying text.
72. In the Senate Report accompanying the Securities Exchange Act of 1934, mention was made of various manipulative practices, including some by dishonest reporters:

In one instance a financial writer on a great New York newspaper was discovered to have been a regular participant in the profits of a free-lance trader, without obligation except to publicize the stocks of the trader. Another witness admitted that his business was "financial publicity," and that his articles were published for the purpose of interesting the public in the stock in which he and those who employed him were interested, thereby causing the market value of the stock to increase; and for this work he was paid by calls and options. Still other cases were observed where persons were employed to broadcast over the radio, ostensibly as economists tendering gratuitous advice, but in reality as publicity agents of stock-exchange firms.

74. See infra notes 78-95 and accompanying text.
75. The Act authorizes the SEC to seek treble damages for violations of provisions of the Securities Exchange Act of 1934 and provides that an action to seek these damages may not be brought more than five years after the date of the purchase or sale that constitutes the alleged violation. See Pub. L. No. 98-376, 53 U.S.L.W. 21 (Jan. 22, 1985) (to be codified at 15 U.S.C. § 78u(d)). It increases the maximum criminal fine for violations of the Securities Exchange Act, from $10,000 to $100,000. See id. (to be codified at 15 U.S.C. 78ff(a)). In addition, it authorizes the SEC to bring administrative proceedings against persons failing or causing a failure to comply with the proxy and tender offer reporting provisions. See id. (to be codified at 15 U.S.C. 78o(c)(4)).
76. Id. (to be codified at 15 U.S.C. § 78u).
B. Legislative History and Policy

This reading of the Act is supported by its legislative history. Statements by the SEC and members of Congress indicate that financial reporters engaged in scalping or similar activities should be subject to liability. For example, a sponsor of the Act listed manipulative practices by a Wall Street Journal reporter as a prime example of insider trading. In addition, the SEC noted with approval that “newspaper columnists” had been the targets of insider trading actions.

In an attempt to expand liability to those normally considered to be outsiders, such as financial reporters, Congress did not endorse Chiarella’s fiduciary relationship concepts. Instead, Congress sought to broaden the traditional insider category, normally consisting of officers, directors and controlling shareholders. Congress refused to define “insider.” It explained that a definition would be too inflexible to encompass unusual situations and would thus tend to limit prosecutions. Instead, Congress stressed that recent judicial developments, including the misappropriation theory, had permitted the expansion of the insider concept to encompass those normally termed outsiders, such as underwriters, investment analysts and others who often learn of market infor-

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78. In his remarks to the House, Representative John Dingell, Chairman of the House Committee on Energy and Commerce and one of the sponsors of the bill, see Insider Trading Hearing, supra note 77, at 4, stated:

Insider trading is becoming commonplace in our markets and threatens to undermine investor confidence and the integrity of our securities markets.

In May the SEC filed a complaint against a former Wall Street Journal reporter in connection with a scheme to profit by trading in stocks on the basis of advance knowledge of market-sensitive articles in the Journal’s “Heard on the Street” column.


81. See id. at 13-14, reprinted in 1984 U.S. Code Cong. & Ad. News at 2286-87. Several private parties who appeared before the committee urged such a refusal. See Insider Trading Hearing, supra note 77, at 197 (remarks of Arnold S. Jacobs, Acting Chairman of the Association of the Bar of the City of New York); id. at 234-35 (statement of A.A. Sommer, Jr., partner at Morgan, Lewis & Bockius); id. at 242-43 (statement of Ted J. Fiflis, Chairman of the Research Task Force of the American Law Institute’s Proposed Federal Securities Code). But see id. at 106-07 (statement of Dennis J. Block, member of Weil, Gotshal and Manges, asserting that insider trading should be defined).

mation and use it as the basis for trading. "Insider trading by such persons undermines confidence in the markets in the same manner as trading by corporate insiders." By endorsing this flexible, shifting concept of an insider, Congress indicated that sanctions against insiders should be applied against those traditionally considered outsiders, if they engage in unfair trading practices.

Congress expanded several concepts in order to turn outsiders into insiders. It redefined insider trading as "the term used to refer to trading in the securities markets while in possession of 'material' information . . . that is not available to the general public." This broad concept is significantly different from the prevailing view of insider trading as the misuse of confidential information by corporate fiduciaries. Congress focused on possession itself as a means of bringing a person into the insider category. Market information is no different from inside corporate information, and those who use it unlawfully become insiders.

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86. See SEC v. Monarch Fund, 608 F.2d 938, 941 (2d Cir. 1979); Insider Trading Hearing, supra note 77, at 263 (statement of Ted J. Fiflis, Chairman of the Research Task Force of the American Law Institute's Proposed Federal Securities Code, noting that the classic form of insider trading is one in which "a corporate executive or other insider buys or sells securities while in possession of material nonpublic information obtained from a corporate source"); id. at 149 (statement of David M. Brodsky, member of Schulte, Roth & Zabel, noting that the classic example of insider trading is president of company trading on unannounced information learned at board meeting); id. at 165 (statement of Milton Freeman, partner at Arnold & Porter, stating that "true" insider trading occurs when the officer of a corporation buys shares from its shareholders).
87. The House Report implied that once information is received and used as the basis for trading, the information becomes inside information. Possession and use are the crucibles for changing market information into inside information. "Thus, if a purchaser of a target company's securities in a tender offer has information received from the investment banker . . . this 'market' information may be considered inside information . . . [T]hose who unlawfully possess or use material nonpublic information . . . can earn substantial profits . . . " H.R. Rep. No. 355, 98th Cong., 1st Sess. 4, reprinted in 1984 U.S. Code Cong. & Ad. News 2274, 2277.
88. Id., reprinted in 1984 U.S. Code Cong. & Ad. News at 2277. A distinction has often been drawn between market information and corporate information. Market information is "information about events or circumstances which affect the market for a company's securities but which do not affect the company's assets or earning power." Fleischer, Mundheim & Murphy, An Initial Inquiry into the Responsibility to Disclose Market Information, 121 U. Pa. L. Rev. 798, 799 (1973); see Oppenheimer & Co., Sec. Exch. Release No. 12319 (Apr. 2, 1976), in [1975-1976 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 80,551, at 86,415 & n.2; Note, An Outsider Looks at Insider Trading: Chiarella, Dirks and the Duty to Disclose Material Nonpublic Information, 12 Fordham Urb. L.J. 777, 782 (1984) [hereinafter referred to as Duty to Disclose]. Corporate information is "information which comes from within the corporation or affects the price of corporate stock because of its reflection of a corporation's expected earnings or assets." Brudney, supra note 2, at 329; see SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 848-49, 852 (2d Cir. 1968) (en banc), cert. denied, 394 U.S. 976 (1969); Duty to Disclose, supra, at 781. As one commentator has noted, however, the distinction is often made to criticize the distinction. See Langevoort, supra note 30, at 42 n.168. Chief Justice Burger has stated that for the purposes of the securities laws there is no difference between these two
Additionally, by endorsing the misappropriation theory, Congress has attempted to expand the potential range of defendants.

A broad view of insider trading is also supported by Congress' policy statements. In enacting the Act, Congress exhibited its concern with the increase in insider trading and the resulting enforcement problems. Congress sought to increase sanctions and to stop abuses to ensure fairness in the markets: "The abuse of informational advantages that other investors cannot hope to overcome through their own efforts is unfair and inconsistent with the investing public's legitimate expectation of honest and fair securities markets where all participants play by the same rules." Thus, the Act provides a clear signal of congressional desire to stop insider trading, in all its guises, without being constricted by unnecessary notions of fiduciary duty. Although Congress did not overrule Chiarella or announce that liability should be premised on a broad duty to disclose imputed to all market participants, it probably did not see a need to do so. By relying on the SEC's analysis of case law, Congress assumed that almost all situations, including that of the "scalping" financial reporter, would be covered either by the misappropriation theory or by treating the outsider as an insider. Given the previous analysis of misappropriation, it is clear that it does not cover the journalist. Nonetheless, to effectuate congressional policy, courts should broaden their definition of insider to encompass all who trade on the basis of material nonpublic information. In other words, in cases in which the misappropriation theory of information. See Chiarella v. United States, 445 U.S. 222, 240 n.1 (1980) (Burger, C.J., dissenting).


90. Statements by members of the House and Senate indicate Congress' concern with the need to increase sanctions for insider trading. "The need for increased sanctions to deter insider trading is well documented on the front pages of our newspapers." 129 Cong. Rec. H7012 (daily ed. Sept. 19, 1983) (remarks of Rep. Wirth). "The [SEC] has in recent years stepped up its efforts to combat this threat. . . . Prior to 1978, the Commission initiated about forty cases . . . . Since then, the Commission has brought over fifty insider trading cases." H.R. Rep. No. 355, 98th Cong., 1st Sess. 21, reprinted in 1984 U.S. Code Cong. & Ad. News 2274, 2294. "Insider trading has become a more widespread problem in recent years, with the increase in mergers and tender offers . . . and with the growth of the options market . . . ." Id. at 5, reprinted in 1984 U.S. Code Cong. & Ad. News at 2278.


94. See supra notes 30-45 and accompanying text.

95. See supra notes 67-70 and accompanying text.
puration theory simply will not work, a broad duty to disclose should be imposed on all participants in market transactions.

III. Remedies

A. The SEC's Approach and the First Amendment

The SEC has announced that it plans to impose section 10(b) liability on financial columnists who engage in scalping. Although such liability is unsupportable under Chiarella and the better view of misappropriation, the Act indicates that Congress has given its imprimatur to such SEC actions. Given a broad duty to disclose, the SEC would naturally endorse the traditional requirement of "disclose or abstain." Indeed, even under its own view of journalistic liability, the SEC would like the reporter either to abstain from the transaction or to disclose the security holdings in question in the article itself. This suggested remedy, however, has raised the ire of first amendment lawyers.

The choice between disclosure and abstention is consistent with the purposes of the securities laws. Congress' regulatory scheme places great weight on a well-informed investing public. As applied to a newspaper, however, a disclosure requirement could force the paper to publish

96. See supra note 6.
97. See supra notes 30-45.
98. In cases in which a duty to disclose has been found, the SEC and the courts have consistently found that the person owing the duty has the option of disclosing the material information or abstaining from the transaction. "Thus, anyone in possession of material inside information must either disclose it to the investing public, or, if he is disabled from disclosing it in order to protect a corporate confidence, or he chooses not to do so, must abstain from trading in or recommending the securities concerned while such inside information remains undisclosed." SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 848 (2d Cir. 1968) (en banc), cert. denied, 394 U.S. 976 (1969); see Affiliated Ute Citizens v. United States, 406 U.S. 128, 153 (1972); Jackson v. Oppenheim, 411 F. Supp. 659, 665 (S.D.N.Y. 1974), aff'd in part, rev'd in part on other grounds, 533 F.2d 826 (2d Cir. 1976); In re Cady, Roberts & Co., 40 S.E.C. 907, 911 (1961).
99. See supra notes 46-70 and accompanying text.
100. See N.Y. Times, Oct. 23, 1984, at D31, col. 4 (John Fedders, ex-head of SEC's enforcement division said that Winans was "required to inform his readers that he had taken positions in the securities about which he was writing and intended to realize profits promptly.").
102. Disclosure of information is one of the principles underlying the securities laws. See SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186 (1963); Anderson, The Disclosure Process in Federal Securities Regulation: A Brief Review, 25 Hastings L.J. 311, 316-20 (1974); Brudney, supra note 2, at 324-25; Sommer, Therapeutic Disclosure, 4 Sec. Reg. L.J. 263, 263-64 (1976). As Professor Anderson has observed, disclosure was consonant with the needs and philosophy of the Roosevelt administration, see Anderson, supra, at 319, and was intended to protect investors by deterring fraud and unethical behavior, see id. at 320. The antifraud provisions "command disclosure of their own force." Brudney, supra note 2, at 325. Thus, the disclose or abstain requirement is consistent with congressional purposes.
material it has no desire to include in the story and thus could constitute an impermissible interference with the editorial process.\textsuperscript{103}

An examination of first amendment doctrine demonstrates that the SEC's proposed remedy cannot survive constitutional scrutiny. In \textit{Miami Herald Publishing Co. v. Tornillo},\textsuperscript{104} the Supreme Court declared unconstitutional a state right-of-reply statute.\textsuperscript{105} The statute mandated that political candidates who were the subject of newspaper editorials be given space to reply.\textsuperscript{106} The Court held that such compelled publication constituted a penalty for the exercise of the constitutional right of freedom of the press.\textsuperscript{107} The statute violated that right because it forced the newspaper to give up space that could have been devoted to other material, and it thus represented an intrusion into the editorial function.\textsuperscript{108}

The choice of material to go into a newspaper, and the decisions made as to limitations on the size and content of the paper . . . constitute the exercise of editorial control and judgment. It has yet to be demonstrated how governmental regulation of this crucial process can be exercised consistent with First Amendment guarantees of a free press . . . .\textsuperscript{109}

Under the scenario proposed by the SEC, the reporter could either disclose or abstain from trading.\textsuperscript{110} If disclosure were chosen, the newspaper would be forced to print the financial holdings of the reporter\textsuperscript{111}

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103. See \textit{infra} notes 104-19 and accompanying text.
105. See \textit{id.} at 258.
106. \textit{Id.} at 244. The Court has consistently distinguished between the press and the broadcast industry and has invariably given more protection to the press. For example, in \textit{Red Lion Broadcasting Co. v. FCC}, 395 U.S. 367 (1969), the FCC developed rules requiring broadcasters to give fair coverage to all sides of an issue. \textit{See id.} at 373-75. Although these rules were analogous to the Florida right of reply statute struck down in \textit{Miami Herald}, the Court upheld them because of the unique character of the electronic broadcast media and the limited availability of broadcast frequencies. \textit{See id.} at 386-89, 400-01; \textit{see also FCC v. Pacifica Found.}, 438 U.S. 726, 748 (1978) (first amendment protects newspaper publishers from being required to print replies of those they criticize, but does not afford such protection to broadcasters).
108. \textit{See id.} at 256-58.
109. \textit{Id.} at 258. Although the Supreme Court has often used a balancing test in first amendment cases, see \textit{infra} notes 121-25, the Court did not do so in \textit{Miami Herald}. Emerson, \textit{First Amendment Doctrine and the Burger Court}, 68 Calif. L. Rev. 422, 449 (1980). Rather, the Court merely examined the impact of the regulation on the newspaper and determined that it imposed a substantial burden. \textit{Id.} Professor Tribe interprets Supreme Court cases as suggesting that compelled publication is the flip side of prior restraint: Telling the newspaper what to print is not dissimilar to telling the newspaper that it cannot print, and thus this type of regulation must be forbidden. \textit{See L. Tribe, American Constitutional Law § 12-22, at 697 (1978).}
110. \textit{See Kotler, supra} note 8, at 46 (SEC's intent is to broadcast the message: "Publish a disclosure statement or be punished.").
111. \textit{See Mathews & Levine, supra} note 6, at 44, col. 5 (SEC says that news reporters have an obligation under the law to publish information about their financial dealings); \textit{N.Y. Times}, Oct. 23, 1984, at D31, col. 4 (reporters must inform readers that they have taken positions in securities about which they are writing); \textit{Wall St. J.}, May 18, 1984, at
and possibly of relatives and friends of the reporter.\textsuperscript{112} Such a requirement, although perhaps not as intrusive as a right-of-reply statute, would nevertheless constitute interference in the editorial processes of the paper.\textsuperscript{113} The newspaper would be left with several unpalatable choices: print the required information, find another reporter to write the story, or refuse to publish. Any of these options might have a chilling effect, leading to the suppression of true news stories. If the newspaper decided to print the article, it nevertheless might determine that publication of such articles in the future is simply not worth the trouble, especially given the possibility of an adverse public reaction.\textsuperscript{114} If the newspaper decided to select another reporter, the story might be out of date by the time a second journalist of equal competence was found. A refusal to publish because of the governmentally imposed conditions could lead to the complete suppression of certain articles, thus limiting public debate and knowledge.\textsuperscript{115}

\textsuperscript{2, col. 2} (SEC theory could impose duty on journalists to disclose in their stories any financial interest they have in the securities about which they write).

\textsuperscript{112} See N.Y. Times, May 19, 1984, at 37, col. 6 (expressing concern that this type of requirement might lead to disclosure of the interests of the reporter's spouse or child).

\textsuperscript{113} See supra notes 104-12, infra notes 114-19 and accompanying text. Interference with the press has been an anathema to the Supreme Court. As Justice Stewart noted in considering the possibility that newspapers might be subject to government regulations:

Perhaps [the Court of Appeals'] "balancing" of First Amendment "values" would require no more than that newspapers be compelled to give "limited" access to dissident voices, and then only if those voices were "responsible." And perhaps it would require that such access be compelled only when there was a single newspaper in a particular community. But it would be a close question for me which of these various alternative results would be more grossly violative of the First Amendment's guarantee of a free press. For that guarantee gives every newspaper the liberty to print what it chooses and reject what it chooses, free from the intrusive editorial thumb of Government.


\textsuperscript{115} At the heart of the first amendment is the notion that truth and democracy flourish through public knowledge and debate.

[When men have realized that time has upset many fighting faiths, they may come to believe even more than they believe the very foundations of their own conduct that the ultimate good desired is better reached by free trade in ideas— that the best test of truth is the power of the thought to get itself accepted in the competition of the market, and that truth is the only ground upon which their wishes safely can be carried out.


This "marketplace of ideas" theory is often coupled with a discussion whether a regulation will have a "chilling effect" on a first amendment right. In the case of disclosure of holdings by the financial reporter, media attorneys are concerned that forced disclosure...
Even if the newspaper did not have strong objections to the printing of the few words or sentences, the paper would be forced to serve as a policeman. Editors would be consulted on whether SEC rules required disclosure of a particular transaction, such as a purchase by a reporter's mother-in-law. In addition, this sort of compelled publication may lead to further limitations on freedom of the press. If the SEC can force newspapers to print material, other governmental agencies with legitimate purposes might demand the same privileges. Thus, the SEC's suggested remedy is constitutionally defective because it would compel publication in violation of the first amendment. In addition, the remedy has disturbing ramifications. There is, however, a solution that safeguards the interests of both the government and the newspapers, while punishing the true culprit—the reporter.

B. Disclosure to the SEC

Although compelling a newspaper to publish the reporter's holdings would infringe the first amendment right to freedom of the press, this constitutional issue can be avoided by requiring disclosure, not in the pages of the newspaper, but to the SEC. The reporter would still be forced to disclose or abstain, as required by the securities laws, but the paper would be left out of the entire process, as required by the first amendment. If the reporter failed to comply with the disclosure requirement, a section 10(b) action could be initiated.
It can be argued that this solution raises a constitutional problem because disclosure to the SEC limits the reporter's expression. While it is true that the article cannot be published lawfully unless the reporter discloses securities holdings to the SEC, any restriction on speech is incidental. It is the wrongful conduct—the attempted scalping—that is the subject of the regulation. The Supreme Court has developed a three-part test to scrutinize statutes that regulate conduct that is tangentially related to speech: A government regulation is sufficiently justi-
fied if it furthers an important and substantial government interest, if the
government interest is unrelated to the suppression of free expression,
and if the incidental restriction on alleged first amendment freedoms is
no greater than is essential to further that interest.125

In the case of disclosure to the SEC, the government has a substantial
interest in regulating the securities markets,126 an interest unrelated to
the suppression of speech. The government is not concerned with the

v. Douds, 339 U.S. 382, 385-86, 399 (1950) (labor union officials required to sign loyalty
oath); Cox v. New Hampshire, 312 U.S. 569, 577-78 (1941) (upholding parade permit
requirement); see also Brennan, The Supreme Court and the Meiklejohn Interpretation of
the First Amendment, 79 Harv. L. Rev. 1, 11 (1965) (discussing application of balancing
test to regulations that incidentally limit speech). For general discussions of the O'Brien
test, see Ely, Flag Desecration: A Case Study in the Roles of Categorization and Balancing
in First Amendment Analysis, 88 Harv. L. Rev. 1482, 1483-84 (1975); Emerson, supra
note 109, at 450-51.

has also used other tests in first amendment cases. In Buckley v. Valeo, 424 U.S. 1 (1976)
(per curiam), a case involving campaign contribution ceilings and disclosure regulations,
the Court noted that the limitation on contributions restricted freedom of political associ-
ation, which is closely allied to freedom of speech. See id. at 24-25. In holding these
limitations constitutional, the Court invoked a standard of the "closest scrutiny" and
applied a two-part test: The government must demonstrate a sufficiently important inter-
est and must employ narrowly drawn means to avoid unnecessary abridgement of associ-
atonal freedoms. Id. at 25; see Members of the City Council v. Taxpayers for Vincent,
104 S. Ct. 2118, 2135-36 (1984); Emerson, supra note 109, at 449-51; cf. First Nat'l Bank
v. Bellotti, 435 U.S. 765, 786 n.23 (1978) (regulation was aimed at speech, but Court
noted approvingly the existence of the O'Brien test).

In addition, the Valeo Court upheld a system of disclosure whereby political commit-
tees or candidates are required to register with the Federal Election Commission, see 424
U.S. at 63, 66-68, keep records of many contributors, see id. at 63, and file quarterly
reports containing detailed financial information about all persons contributing over a
certain amount of money. See id. This type of compelled disclosure must survive "exact-
ing scrutiny," id. at 64, and the Court used a somewhat simpler test: The government
interest and the information to be disclosed must be substantially related. Id.; see also
1459, 1468-71 (1985) (spending limitations on independent expenditures by political ac-
tion committees struck down under the Valeo test of a narrowly tailored regulation cou-
ped with a sufficiently strong government interest).

The disclosure rule proposed in this Note meets all possible tests. See supra notes 121-
24, infra notes 126-28 and accompanying text.

126. The securities laws were enacted to provide for governmental regulation of an
important part of the economy—the markets.

It is my belief that exchanges for dealing in securities and commodities are
necessary and of definite value to our commercial and agricultural life. Never-
theless, it should be our national policy to restrict, as far as possible, the use of
these exchanges for purely speculative operations.

I therefore recommend to the Congress the enactment of legislation providing
for the regulation by the Federal Government of the operations of ex-
changes dealing in securities and commodities for the protection of investors,
for the safeguarding of values, and so far as it may be possible, for the elimina-
tion of unnecessary, unwise, and destructive speculation.

S. Rep. No. 792, 73d Cong., 2d Sess. 2 (1934) (letter from President Roosevelt to Con-
gress); see id. at 4 (it is "essential" that the government enact measures that will enable it
to stop massive speculation); see Silver v. New York Stock Exch., 373 U.S. 341, 366
(1963) ("It requires but little appreciation . . . of what happened in this country during
content of an article. Its interest is in preventing fraud in the securities markets. Moreover, any incidental restriction on first amendment rights is no greater than is necessary. Disclosure in the paper itself would be too broad and would infringe the paper's constitutional rights. A narrowly drawn rule requiring disclosure to the SEC, however, would not violate the Constitution.

1. A Bright Line Rule

The SEC, under its rulemaking powers, should promulgate a rule that would mandate such disclosure. The rule would require disclosure whenever a reporter, knowing that an article about a specific security will be published, purchases or sells securities mentioned in the article. No disclosure should be required, however, if the reporter can prove that the securities transaction did not occur in anticipation of the story's publication. The rule might read as follows:

When a reporter, writing for a newspaper, magazine or other publication, purchases or sells, receives consideration for the purchase or sale, or controls the purchase or sale, of a security, such reporter

the 1920's and 1930's to realize how essential it is that the highest ethical standards prevail . . . .


128. See supra notes 104-17 and accompanying text.

129. Section 10(b) authorizes the SEC to promulgate rules that it determines are "necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. § 78j(b) (1982); see Loss I, supra note 1, at 821-22 (discussion of the creation of rule 10b-5).

130. The rule must cover both purchases and sales. Although most trading would involve purchases, it is possible that a reporter would engage in "short sales" knowing that an unfavorable article would appear. Short selling is the practice of selling securities, sometimes not yet owned, in anticipation of a price decline. The securities are subsequently purchased at the lower price, enabling the speculator to make delivery of the stock sold. See Edwards & Hanly v. Wells Fargo Sec. Clearance Corp., 602 F.2d 478, 481 (2d Cir. 1979), cert. denied, 444 U.S. 1045 (1980); Fryling v. Merrill Lynch Pierce, Fenner & Smith, Inc., 593 F.2d 736, 740 n.2 (6th Cir. 1979); Loss I, supra note 1, at 711-17.

131. The addition of the word "controls" would make the rule applicable to situations in which the reporter neither trades nor receives obvious consideration. For example, a transaction by a spouse, a child or a roommate might fall within the control category. The concept of control is not new to the securities laws, as the 1934 Act imposes liability on "[e]very person who, directly or indirectly, controls any person liable under any provision of this chapter." 15 U.S.C. § 78t(a) (1982); see Strong v. France, 474 F.2d 747, 752 (9th Cir. 1973); see also 15 U.S.C. § 77o (1982) (1933 Act imposing liability on control persons). To determine whether control exists in the case of the reporter, certain concepts that have developed under the "controlling persons" section of the 1934 Act, such as bad faith, might be utilized. See Hecht v. Harris, Upham & Co., 430 F.2d 1202, 1210 (9th Cir. 1970).
shall disclose the purchase or sale, receipt of consideration, or control to the SEC:

(1) if the reporter writes or has written an article dealing with the security in question within three months\(^\text{132}\) of the purchase or sale or has advance knowledge of the publication of an article within such time; and

(2) if the reporter has purchased or sold or controlled the purchase or sale of the security in question intending to profit from the advance knowledge of the publication of the article, or has received consideration for communicating such advance knowledge to another.

The rule might also contain language limiting such disclosure to purchases or sales involving more than an insubstantial amount of money or number of securities.\(^\text{133}\) By specifying threshold limits, the SEC could incorporate the concept of materiality into the rule.\(^\text{134}\) In addition, the rule should clearly state that disclosure is not required if the securities have been held for a period longer than three months.\(^\text{135}\) There must be

\(^{132}\) Such a requirement is consistent with other provisions of the securities laws. For example, § 16(b) of the Securities Exchange Act of 1934 provides that in most cases all profits from any sale and purchase or purchase and sale of equity securities by officers or directors of the issuer or holders of more than 10% of the issuer’s equity securities shall inure to the corporation if the transaction occurs within six months. See 15 U.S.C. 78p(b) (1982). Although courts have recognized that six months is an arbitrary time limit, see Kern County Land Co. v. Occidental Petroleum Corp, 411 U.S. 582, 593 n.23 (1973); Adler v. Klawans, 267 F.2d 840, 845 (2d Cir. 1959), it has been noted that Congress was doing its best to “minimize misuse of confidential information, without unduly discouraging bona fide long-term investment.” Blau v. Max Factor & Co., 342 F.2d 304, 308 (9th Cir.), cert. denied, 382 U.S. 892 (1965); see Loss I, supra note 1, at 611 n.23.

\(^{133}\) Threshold limits are not a new concept. Section 16(a) of the 1934 Act requires a beneficial owner of a more than 10% equity security interest to register with the SEC. See 15 U.S.C. § 78p(a). Threshold limits are also found in other areas of the law. In Buckley v. Valeo, 424 U.S. 1 (1976) (per curiam), the Court upheld a recordkeeping threshold of $10 per contributor and a disclosure requirement for those with contributions aggregating more than $100. See id. at 82-84. Although cognizant that the limits were low, the Court stated that it was a “judgmental decision, best left . . . to congressional discretion.” Id. at 83.

\(^{134}\) In a rule 10b-5 action, the omission or misstatement must be “material.” 17 C.F.R. § 240.10b-5(b) (1984); see Greenfield v. Heublein, Inc., 575 F. Supp. 1325, 1336 (E.D. Pa. 1983), aff’d, 742 F.2d 751 (3d Cir. 1984), cert. denied, 105 S. Ct. 1189 (1985); 5 A. Jacobs, supra note 1, § 61.02[a] at 3-75. There are several tests for materiality. Many involve some variation of the question: “What would the reasonable investor want to know?” Id. § 61.02[b][ii], at 3-92. One often-used test is if “there is a substantial likelihood that a reasonable shareholder would consider it important in deciding whether or not to sell his stock.” Greenfield v. Heublein, Inc., 575 F. Supp. 1325, 1336 (E.D. Pa. 1983), aff’d, 742 F.2d 751 (3d Cir. 1984), cert. denied, 105 S. Ct. 1189 (1985); accord Sundstrand Corp. v. Sun Chem. Corp., 553 F.2d 1033, 1040 (7th Cir.), cert. denied, 434 U.S. 875 (1977); Lucas v. Florida Power & Light Co., 575 F. Supp. 552, 569 (S.D. Fla. 1983); cf. TSC Indus. v. Northway, Inc., 426 U.S. 438, 449 (1976) (applied in the context of Rule 14a-9). See generally 5 A. Jacobs, supra note 1, §§ 61.02[a], [b], [c] (discussion of the various concepts of materiality). The SEC, in the rule, could indicate that trading in insignificant amounts would not be material.

\(^{135}\) Reporters are concerned that the mere holding of securities might trigger the disclosure requirements. See N.Y. Times, Jan. 23, 1985, at D2, col. 4 (editor decided that it was not a violation of the Wall Street Journal guidelines to keep silent about his wife’s
a purchase or sale within the three month period. Finally, a provision permitting public access to these records would be essential.\textsuperscript{136}

2. The Effect of the Rule

Although the proposed rule may not prevent trading at the outset, it would serve as a deterrent. If the reporter disclosed information about purchases or sales, the SEC could not prosecute.\textsuperscript{137} By allowing the employer/newspaper to monitor the list of financial holdings, however, the SEC could ensure the reporter's punishment.\textsuperscript{138} Because such trading would constitute a violation of internal employee guidelines,\textsuperscript{139} most newspapers would discharge the reporter. In addition, there is even the

\textsuperscript{136} In Buckley v. Valeo, 424 U.S. 1 (1976) (per curiam), lists of campaign contributors, including detailed financial and personal information, were "made available by the Commission for public inspection and copying," \textit{id.} at 63 (quoting 2 U.S.C. § 438(a)(4) (1976)), and the Court upheld these requirements, \textit{see id.} at 72. In the case of the proposed rule, public access would serve important functions. \textit{See infra} note 143 and accompanying text.

\textsuperscript{137} In line with the policy behind the securities laws, see \textit{supra} notes 1-4 and accompanying text, the SEC does not normally bring actions as long as the requested information is disclosed. Content is theoretically not relevant. \textit{See Anderson, supra} note 102, at 322 (Commission has no authority to pass on quality of registered security); Douglas & Bates, \textit{The Federal Securities Act of 1933}, 43 Yale L.J. 171, 172 (1933) (government should not pronounce investments sound or unsound); Heller, \textit{Disclosure Requirements Under Federal Securities Regulation}, 16 Bus. Law. 300, 301 (1961) (filing of registration statement does not constitute SEC approval of security).

\textsuperscript{138} Almost all newspapers and magazines have a code of ethics or conflict of interest policy. \textit{See infra} note 139. These publications may fire a reporter trading in securities in advance of publication. \textit{See Adler, Trouble on the Street}, Newsweek, Feb. 4, 1985, at 59 & n.*; \textit{Greenwald, The Talk of the Money World}, Time, Apr. 16, 1984, at 44; \textit{Henry, supra} note 63, at 45.

\textsuperscript{139} Various media organizations have strict disclosure and conflict of interest policies. Newsweek forbids editorial employees to own stock in a company they report on or to invest on the basis of advance information gathered by the magazine. \textit{Adler, supra} note 138, at 59 & n.*. At the Washington Post, business writers are required to file an annual report listing personal investments. \textit{Id.} Institutional Investor magazine forbids staffers to trade in the securities of companies that will be mentioned in future articles. \textit{Id.} Both Time Magazine and the Wall Street Journal have strict policies on conflicts of interest. \textit{Greenwald, supra} note 138, at 44 & n.*. The Journal's policy requires that if an employee or a member of his family should buy a security and then learn of a proposed article about the security, a supervisor must be notified. \textit{See N.Y. Times, Jan. 23, 1985, at D2, col. 4. Dow Jones & Company, Inc., the parent company of the Wall Street Journal, has an extremely detailed and comprehensive conflict of interest policy. The company prohibits employees with "knowledge of a forthcoming article, item or advertisement concerning a company or industry" from investing in the company prior to publication. \textit{See Memorandum, Dow Jones & Company, Inc., Conflicts of Interest Policy}, at 4 (available in files of \textit{Fordham Law Review}). Any employee with prior knowledge of an article should delay trading in the securities of the companies involved "until the general public has an opportunity to read and digest the information." \textit{Id.} In addition, the company prohibits an employee from selling short. \textit{See id. See supra} note 130 and accompanying text.
If a reporter did not disclose the requested information, the SEC could institute a section 10(b) action. Although the proposed rule would require the SEC to police the markets to ensure compliance, such policing is already one of its functions. The adoption of a rule and the bringing of test cases would allow the SEC to punish this type of conduct, when discovered. As well as providing the employer/newspaper and the SEC with possible causes of action, disclosure to the SEC would enable the public to monitor the list of financial holdings to determine if any reporter is engaged in manipulative activity. Investors or their advisors could then make an informed choice on whether to follow that reporter's future recommendations.

140. At the Winans trial, a Wall Street Journal assistant editor pointed out that the newspaper's reputation had been damaged by Winans' actions. See N.Y. Times, Jan. 23, 1985, at D2, cols. 3-4; see also N.Y. Times, Jan. 24, 1985, at D9, cols. 3-4 (Wall Street Journal editor stating that Winans case had hurt the newspaper with readers and sources, with the way we do business internally, and with at least one institution we deal with on a continuing basis: the American Stock Exchange). It is possible that a newspaper could bring an action for damages on this basis, by proving a loss in circulation. See Zoecno Indus. v. American Stockman Tag Co., 713 F.2d 1174, 1180 (5th Cir. 1983) (plaintiff corporation awarded damages due to misappropriation of trade secrets by former employees); Duane Jones Co. v. Burke, 306 N.Y. 172, 195-96, 117 N.E.2d 237, 249-50 (1954) (advertising company sued disloyal executives for damages); see also Tlapely v. Chevron Oil Co., 407 F.2d 1129, 1133-34 (8th Cir. 1969) (court affirmed constructive trust recovery by defrauded employer). In addition, the employee might be subject to criminal liability under the mail or wire fraud statutes. The mail fraud statute provides that anyone "having devised or intending to devise any scheme or artifice to defraud...[who] places in any post office... any matter or thing whatever" can be fined or imprisoned. 18 U.S.C. § 1341 (1982). The wire fraud statute is similarly broad, stating that the same conduct can be punished if carried out "by means of wire, radio, or television communication." Id. § 1343. These statutes have been used to punish breaches of the employer/employee relationship. See, e.g., United States v. Von Barta, 635 F.2d 999, 1006-07 (2d Cir. 1980), cert. denied, 450 U.S. 998 (1981); United States v. Brown, 540 F.2d 364, 374-75 (8th Cir. 1976); United States v. Bush, 522 F.2d 641, 646-47 (7th Cir. 1975), cert. denied, 424 U.S. 977 (1976). Another possibility is an action by the employer or the government under the Racketeering Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961-1968 (1982). See United States v. Weiss, 579 F. Supp. 1224, 1229-30 & n.9 (S.D.N.Y. 1983) (government sued employee for stock fraud); Beth Israel Medical Center v. Smith, 576 F. Supp. 1061, 1063-64 (S.D.N.Y. 1983) (nonprofit organizations sued chief legal officer for selling confidential information).


143. One of the major purposes behind the securities laws was to allow investors to make informed investment decisions. See supra notes 1-4 and accompanying text. The proposed rule would provide additional guidance for the investor, in the same manner as any other publicly available material, such as a 10-k report, see 15 U.S.C. § 78m(a)(2) (1982); 17 C.F.R. § 240.13a-1 (1984).
The argument may be made that the proposed rule does not sufficiently protect investors because at the time of publication the article contains a material omission of which the public is not aware. This argument fails to recognize that the public interest in enforcing the securities laws must be balanced against the newspaper's first amendment rights. Although the rule may lack the immediacy of disclosure in the newspaper, it would deter manipulative practices by journalists while protecting freedom of the press.

**CONCLUSION**

Scalping and other manipulative practices by journalists writing on financial issues are serious problems. Although *Chiarella* and the better view of misappropriation do not mandate actions against such journalists under section 10(b) and Rule 10b-5, Congress, through the Insider Trading Sanctions Act of 1984, has expressed its desire to punish reporters engaging in this type of behavior. Because of first amendment concerns, the usual methods of disclosure under the securities laws cannot be utilized. The SEC, however, should promulgate a rule that establishes a procedure requiring journalists to disclose to the SEC transactions involving securities about which the reporter will be writing. Such a rule would serve the policies of the securities laws by helping the investing public to make informed choices and by deterring future fraudulent conduct.

*Tira Harpaz*

[As this issue was going to press, Judge Stewart handed down his opinion in *United States v. Winans.* As anticipated by the author, the opinion endorsed a view of misappropriation requiring only one fiduciary duty—that between employer and employee—and specifically rejected the idea that the ultimate duty must flow to a corporate client. In the opinion of the author, Judge Stewart has misinterpreted the misappropriation

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144. Although disclosure at the time of the transaction would be optimal, the securities laws do not always provide for this. For example, the Securities Act of 1933 requires that a prospectus be delivered with confirmation of the purchase, but not necessarily before the formation of the contract. See 15 U.S.C. § 77e (1982) (security must be "accompanied or preceded by a prospectus"); Mundheim, *Selected Trends in Disclosure Requirements for Public Corporations*, 3 Sec. Reg. L.J. 3, 8 (1975) (1933 Act requires only that prospectus be delivered with confirmation of sale). Professor Homer Kripke has pointed out certain problems with the prospectus in general. He noted that there is a myth that the layman to whom the prospectus is addressed actually uses it. See Kripke, *The Myth of the Informed Layman*, 28 Bus. Law. 631, 633 (1973). He submits that in practice, only sophisticated investors and professionals are capable of understanding today's technical prospectuses. See id.; Vrignon, *Scylla and Charybdis: A Consideration of Certain Inconsistencies in Federal Securities Regulation*, 5 Sec. Reg. L.J. 25, 34-36 (1977).

145. See *supra* notes 104-28 and accompanying text.

* No. 84-CR-605 (S.D.N.Y. June 24, 1985).

** See *id.* at 23-27.
theory. The analysis found on pages 1041-43 of this article points out the flaws in his argument.