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Statutory Interpretation in Securities Jurisprudence: A Failure of Textualism

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Ediberto Román*

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I. INTRODUCTION

Theory in statutory interpretation has engendered considerable scholarly debate in recent years.\(^1\) Much of this debate has centered on the renewed allure of a textualist theory in statutory interpretation.\(^2\) Textualist construction, also referred to recently as the new textualism,\(^3\) demands that, when interpreting a statute, a judge is to limit her inquiry to the text of the statute.\(^4\) Thus, the judge is forbidden

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3. Eskridge, Textualism, supra note 1, at 621.

4. Zeppos, supra note 2, at 1299; Plass, supra note 2, at 94-95; Eskridge, Textualism, supra note 1, at 652.
from using the legislative history as a statutory interpretation tool. To the textualist, the legislature demonstrates its intent through the text of the statute. Accordingly, a judge's role is to "interpret laws," and not to "reconstruct the legislators' intentions." Justice Scalia, one of textualism's most outspoken advocates, argues that a text-based theory reduces the potential for arbitrariness and abuse that may arise by having a judge substitute her values for that of the legislature.

In theory, the textualist's argument for judicial restraint is compelling. However, in practice, like other theories of statutory interpretation, textualism is also a malleable theory which can be manipulated to alter the legislature's intent. Yet, this theory in application can disguise its usurpation of the legislative function. Indeed, a judge applying textualism can actually alter the meaning of a statute, but still claim that her holding was merely what was called for by the plain meaning of the statutory text.

Federal securities jurisprudence provides a vivid example of the ease with which a court can usurp the legislative function. The Supreme Court's recent decision concerning the enforcement provisions of the federal securities laws provides an example of this sort of usurpation. In *Central Bank of Denver v. First Interstate Bank of Denver*, the Court refused to recognize aider and abettor claims under the Securities Exchange Act of 1934's ("Exchange Act") enforcement provision, section 10(b), by announcing that in interpreting

9. *But see* Public Citizen v. United States Dept. of Justice, 491 U.S. 440, 470 (1989)(Kennedy, J. concurring) ("Where the language of a statute is clear in its application, the normal rule is that we are bound by it. There is, of course, a legitimate exception to this rule... [w]here the plain language of the statute would lead to patently absurd consequences... "); Immigration and Naturalization Serv. v. Cardoza-Fonseca, 480 U.S. 421, 452 (1987)(Scalia, J., concurring) ("If the language of a statute is clear, that language must be given effect—at least in the absence of a patent absurdity.").

   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
This Article critiques the development of a textualist theory in securities jurisprudence and analyzes the *Central Bank* decision, an example of the defects inherent in the application of a textualist approach. In addition, this Article demonstrates how the development of textualist securities jurisprudence stemmed from decisions that casually rejected precedent and mischaracterized existing law, thereby resulting in a distortion of the legislature's intent. An analysis of the Exchange Act demonstrates how the *Central Bank* Court's myopic approach towards statutory interpretation led to its failure to analyze other relevant Exchange Act provisions, including the most relevant provision—section 20(a).


15. Section 20(a) is the 73d Congress’ secondary liability provision. Section 20(a) of the Exchange Act, 15 U.S.C. § 78t(a) (1988), provides:
In particular, the first section of this Article, after briefly summarizing the Central Bank decision, provides a framework for a statutory critique by reviewing the popular theories of statutory interpretation. The second section addresses the forms of secondary liability available under the Exchange Act, all of which were affected by Central Bank. This section illustrates how the post-Central Bank cases confirmed the dissent's and the commentateurs' concerns over the viability of secondary liability under section 10(b). The third section questions the Central Bank Court's adoption of textualist theory in light of its prior holdings concerning section 10(b)'s implied right of action, which followed a purposivist philosophy. The fourth section, in addition to addressing the decision's internal inconsistency, reviews its sweeping application in order to demonstrate its failure to adequately analyze the intended role of secondary liability under the Exchange Act. The fifth and final section addresses the decision's impact and calls for the revival of section 20(a) in order to follow the 73rd Congress' intent in allowing secondary liability claims. Additionally,
this section critiques the Private Securities Litigation Reform Act of 1995, which similarly distorted the 73rd Congress' intent.

THE CENTRAL BANK DECISION AND THE THEORIES OF STATUTORY INTERPRETATION APPLIED TO THE FEDERAL SECURITIES STATUTES

A. The Central Bank Decision

Central Bank of Denver, N.A., ("Central Bank") served as the indenture trustee on two bond issues brought to market in 1986 and 1988 on behalf of the Colorado Springs-Stetson Hills Public Building Authority ("Authority") to fund improvements of a residential and commercial development area in Colorado Springs. The bonds were secured by landowner assessment liens, and the covenants in the indenture required that the real estate subject to the liens have a market value of at least 160 percent of the bonds' outstanding principal and interest.

Prior to the issuance of the 1988 bond, Central Bank became aware that property values were declining in Colorado Springs and that the 160 percent requirement was probably not being met. After some negotiation with the developer, Central Bank agreed to delay an independent review of the appraisal until six months after the closing of the 1988 bond issue. However, before the independent review was undertaken, the Authority defaulted on the 1988 bond.

First Interstate Bank of Denver, the lead plaintiff, commenced a section 10(b) securities fraud action against Central Bank and others. The complaint alleged that Central Bank was "secondarily liable under [section] 10(b) for its conduct in aiding and abetting the fraud." After the district court granted Central Bank summary judgment, the Tenth Circuit Court of Appeals reversed, concluding, among other things, that the facts established a genuine issue concerning the recklessness element of aiding and abetting.

23. Id.
24. A Central Bank appraiser, who reviewed the 1988 appraisal, concluded that it appeared optimistic. Id.
25. Id.
26. Id.
27. Id.
28. Id.
29. Id.
30. Id. at 1444. The Tenth Circuit in Central Bank concluded that (1) Central Bank was aware of the concerns about the 1988 appraisal, (2) Central Bank knew that the sale of the 1988 bonds were imminent and that purchasers were using the
Central Bank petitioned for a writ of certiorari, which was subsequently granted, on the issue of whether recklessness satisfied the requirement for aiding and abetting liability when there was no breach of duty to disclose or to act. Upon granting certiorari, the Supreme Court sua sponte directed the parties to address "whether there [was] an implied private right of action for aiding and abetting violations of section 10(b)," an issue the parties had not questioned and the Court had refused to resolve decades earlier.

Writing for the Court, Justice Kennedy concluded that the text of section 10(b) controls the scope of conduct it prohibits. The Court, reaching what it described as "an uncontroversial conclusion," held that because section 10(b) does not refer to aiding and abetting, those who aid and abet cannot be held liable. Nevertheless, the Court still decided to address the 73rd Congress' likely intent, concluding

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1988 appraisal to evaluate the collateral for the bonds, and (3) a reasonable trier of fact could conclude that Central Bank rendered substantial assistance to the primary fraudfeasor.

32. Id.
33. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 191-92 n.7 (1976)("In view of our holding that an intent to deceive, manipulate or defraud is required for civil liability under section 10(b) and rule 10b-5, we need not consider whether civil liability for aiding and abetting is appropriate under the section and the Rule, nor the elements necessary to establish such cause of action."); Herman & MacLean v. Huddleston, 459 U.S. 375, 379 n.5 (1983)(explaining that the issue was reserved in Hochfelder).
35. Id. at 177. The Court's conclusion that its holding was "uncontroversial" is the thrust of this Article and will be addressed and questioned in detail.
36. Id.
37. The Court rejected the textual argument that the phrase "directly or indirectly" in section 10(b) includes aiding and abetting. The Court's problem with this argument was that aiding and abetting liability extends beyond persons who "indirectly" engage in manipulative or deceptive conduct, and aiding and abetting liability reaches persons who do not engage in the proscribed activities at all. Id. at 176. The Court had a further problem with the "indirectly" argument, namely, that there are "numerous provisions of the 1934 Act that use the term in a way that does not impose aiding and abetting liability." Id. The Court also considered the argument that Congress intended to make aiding and abetting liability part of the Act because the doctrine was well established at the time. Id. at 177. After questioning whether in fact the doctrine was well established, the Court rejected the view that Congress' silence on a potential remedy created such a remedy. Id.
38. Perhaps to avoid appearing to have departed too drastically from its previous decisions, the Court gave lip service to legislative intent despite its holding that required it not to do so. Id. at 175. However, the Court limited its review to express causes of action in the Exchange Act and noted that none imposed aiding and abetting liability. Id. at 178. Justice Kennedy also surprisingly opined that
that it probably would not have included aider and abettor liability\textsuperscript{39} in a private right of action under section 10(b).\textsuperscript{40}

In a harshly worded dissent, Justice Stevens, joined by Justices Blackmun, Souter, and Ginsburg, argued, among other things,\textsuperscript{41} that the majority gave short shift to the long history of aider and abettor liability under section 10(b) and imperiled other well-established forms of secondary liability.\textsuperscript{42} The dissent noted, among other things,\textsuperscript{43} that in hundreds of cases in every circuit the Securities Exchange Commission ("SEC") had concluded that aiders and abettors were subject to section 10(b) liability.\textsuperscript{44}

Finally, the dissent criticized the majority's insistence on addressing an issue not raised by the parties and for writing an opinion that swept far beyond the issues the majority intended to address.\textsuperscript{45} The dissent predicted that:

\begin{quote}
the majority's approach to aiding and abetting at the very least casts serious doubt, both for private and SEC actions, on other forms of secondary liability that, like the aiding and abetting theory, have long been recognized by the
\end{quote}

Congress knew how to impose liability on those who aid and abet the proscribed conduct, but "chose" not to with section 10(b). \textit{Id.}

Justice Kennedy's conclusion concerning Congress' "choosing" suggests that Congress expressed its view concerning the scope of liability under section 10(b). But, as Kennedy admitted, "Congress did not create a private § 10(b) cause of action." \textit{Id.} at 173. Congress thus did not "choose" to provide aider and abetter private rights of action because it did not "choose" to provide for any private right of action under section 10(b). It is, therefore, illogical to suggest that Congress intended section 10(b) to not cover certain rights of action when Congress never suggested that the provision covered any rights of action. \textit{Id.} at 177.

\textsuperscript{39} \textit{Id.} at 179.

\textsuperscript{40} The argument concerning what Congress probably would have done is also misleading. Congress did not expressly include any liability under section 10(b); therefore, unlike what the opinion suggests, Congress gave no expression regarding the scope of liability under section 10(b).

\textsuperscript{41} The dissent also criticized the majority for its judicial activism in the face of congressional acceptance of settled law and questioned whether the majority could show that aider and abettor liability in any way detracted from the legislative intent of the Act. \textit{Id.} at 198. In addition, the dissent focused on the legislative purpose of the section and noted that it was passed for remedial purposes and the Court had previously recognized that it should be read broadly. \textit{Id.} at 195.

\textsuperscript{42} \textit{Id.} at 200.

\textsuperscript{43} The dissent also argued that the aiding and abetting doctrine furthered the Exchange Act's remedial purpose of creating a "securities market that is free from fraudulent practices." \textit{Id.} at 193.

\textsuperscript{44} \textit{Id.} at 192. \textit{See}, e.g., Roberts v. Peat, Marwick, Mitchell & Co., 857 F.2d 646, 652 (9th Cir. 1988)("Aiding and abetting is itself a violation of Section 10(b)"); cert. denied, 493 U.S. 1002 (1989); \textit{In re Atlantic Fin. Management, Inc.}, 784 F.2d 29, 34-35 (1st Cir. 1986), cert. denied, 481 U.S. 1072 (1987); Congregation of the Passion v. Kidder Peabody & Co., 800 F.2d 177, 183 (7th Cir. 1986).

SEC and the courts but are not expressly spelled out in the securities statutes.\textsuperscript{46}

B. The Theories of Statutory Interpretation Applied to the Federal Securities Statutes

When faced with the common task of determining what a legislature intended by a particular statutory term, a court engages in statutory interpretation. In other words, statutory interpretation is a court's quest to ascertain the intended meaning the legislature sought to give a statutory provision.\textsuperscript{47} In this endeavor, a court's goal is to determine, according to the prescriptions set forth by the legislature, the appropriate meaning that ought to be attributed to a statutory provision.\textsuperscript{48} A court interpreting a statutory provision seeks to determine the legislature's intent or purpose behind the provision being reviewed.\textsuperscript{49} The following is a brief review of the statutory interpretation theories that have been applied in federal securities cases.

1. Textualism

As previously mentioned, textualism\textsuperscript{50} emphasizes the commands of a statute's text\textsuperscript{51} and demands that judges refrain from inquiring...

\textsuperscript{46} Id. at 200 n.12 (Stevens, J., dissenting)(emphasis added). Thus, the majority undertook a virtually exclusive focus on the language of the statute with misleading references to what it believed would have been the '73rd Congress' view. The dissent, on the other hand, focused on the universal, longstanding, judicially and administratively accepted position that aider and abettor claims could arise under section 10(b). Furthermore, the dissent noted the inconsistency between the majority's holding and the remedial purpose of the statute. While this Article does not endorse either opinion, it will demonstrate how a more rational opinion could have been reached by following the 73rd Congress' intent of addressing secondary liability under section 20(a) of the Exchange Act. See infra notes 58-83.


\textsuperscript{50} There are substantial works on statutory interpretation that exhaustively review the theories of statutory interpretation, including hybrids of textualism, for example, four-corners textualism versus textual-intentionalism. See, e.g., González, \textit{supra} note 1, at 597-605. This Article focuses on the form of four-corners textualism or new textualism that has been advocated by Justice Scalia and others and has caused significant debate over the last decade. See \textit{supra} notes 1-2.

into a statute's legislative history. In fact, textualism mandates that judges, in interpreting a statute, adhere to the statutory text unless the text is unclear or such a reading would result in an absurdity. While rarely addressed by proponents of textualism, a determination that a provision is unclear or that a literal reading would create an absurdity is necessarily subjective. Nevertheless, the normative goal of textualism is to eliminate a judge's injection of her values into the interpretation of a statute.

Essentially, textualism is based on two interrelated premises. The first premise is that the only legitimate source for statutory interpretation is the text of the statute. The second premise is that legislative history, which often comes from hearings or committee reports and not the Congress as a whole, is not a legitimate source for interpreting statutes. To the textualist, the "legislative purpose is expressed by the ordinary meaning of the words used," and it is only the words used in the statute that is law. Consequently, judges are never to legislate but is to merely ascertain the plain meaning of the statutory provision at issue.

Textualists base their disdain for legislative history on constitutional theory. The argument is as follows: since Article I of the Constitution prescribes the means by which law is to be made and since Article I grants Congress and the President with the lawmaking powers, legislative history, which does not represent the view of the entire Congress or of the President, should not be raised to the status of law. To Justice Scalia, elevating a phrase from the legislative his-

52. See Plass, supra note 2, at 94-95; Zeppos, supra note 2, at 1297.
55. Zeppos, supra note 2, at 1311.
56. Id. at 1299.
57. Id.
58. Id. at 1298. See also Begier v. IRS, 496 U.S. 53, 68 (1990)(Scalia, J., concurring) ("I think it is both demeaning and unproductive for us to ponder whether to adopt literal or not-so-literal readings of Committee Reports, as though they were controlling statutory text."); Taylor v. United States, 495 U.S. 575, 601 (1990)(Scalia, J., concurring in part and concurring in the judgment)(joining in opinion except for that part that examines the statute's legislative history because "the examination does not uncover anything useful (i.e., anything that tempts us to alter the meaning we deduce from the text anyway), but that is the usual consequence of these inquiries (and a good thing, too")).
60. West Virginia Univ. Hosp. v. Casey, 499 U.S. 83, 98 (1991)("The best evidence of that purpose is the statutory text adopted by both Houses of Congress and submitted to the President.").
61. Eskridge, Textualism, supra note 1, at 652.
tory to the level of statutory text is "about as helpful to the conduct of [the Court's] affairs as [the talismanic phrase] 'life is a fountain.'"63 While textualists, such as Justices Scalia and Kennedy,64 reject the use of legislative history, they, in theory, accept confirming their interpretation by reviewing: (1) the structure of the statute, (2) the interpretations given similar provisions, and (3) the canons of statutory construction.65

However, textualism does have many critics.66 While they are numerous,67 one of the more interesting critiques is that the criticisms the textualists level against the use of legislative history may also be equally applicable to textualist theory.68 Specifically, critics note that while textualists attack other theories of statutory interpretation for allowing the judge to substitute her intent for that of the legislature's, textualists fail to acknowledge that textualism is a "malleable theory" that also provides the judge with discretion to apply the theory with "as much or as little consistency as a particular judge chooses."69

While as a method of statutory interpretation textualism need not preordain either a restrictive or an expansionist result, the fact that it can be employed differently in different contexts raises concerns that unspoken policy rationales are driving the interpretive process.70 In fact, by focusing on the text, the textualist accepts and indeed anticipates arriving at results that may be inconsistent with any notion of what the legislature actually intended.71 This method of judicial

64. See supra note 9 and infra note 68.
65. United Sav. Ass'n v. Timbers of Inwood Forest Assocs., 484 U.S. 365, 371 (1988)(Scalia, J., concurring)("A provision that may seem ambiguous in isolation is often clarified by the remainder of the statutory scheme."). See also Eskridge, supra note 1, at 623-24.
66. See, e.g., Daniel A. Farber & Philip P. Frickey, supra note 1, at 423; Plass, supra note 2, at 97; Stephen F. Ross, Reagans Realism Comes to Detroit, 1989 U. Ill. L. Rev. 399; Muriel M. Spence, The Sleeping Giant: Textualism as Power Struggle, 67 S. Cal. L. Rev. 585 (1994); Zeppos, supra note 2, at 1309.
67. Other criticisms of textualism include that it leads to result-oriented judging, Zeppos, supra note 2, at 1322, and that it shifts power to the executive and judicial branches. Arthur Stock, Note, Justice Scalia's Use of Sources in Statutory and Constitutional Interpretation: How Congress Always Loses, 1990 Duke L.J. 160.
68. See Zeppos, supra note 2, at 1311; Plass supra note 2, at 101.
69. See, e.g., Plass, supra note 2, at 101; Zeppos, supra note 2, at 1311.
71. See Zeppos, supra note 2, at 1314 (Textualism accepts and, indeed, mandates such an approach.); Aleinikoff, supra note 5, at 23 (Textualism is willing to accept plain meaning as a reasonable approximation of the legislative intent even if the plain meaning does not identify the legislature's actual meaning.).
supremacy\textsuperscript{72} is particularly troubling when a court is addressing remedial legislation.\textsuperscript{73}

Another noteworthy critique of textualism relates to a court's inherent difficulty in identifying the relevant canonical text.\textsuperscript{74} The question is whether a court should only analyze the provision at issue, the entire statute, any related or unrelated statutes adopted by the enacting legislature, or all of the law at the time of the provision's enactment.\textsuperscript{75} The \textit{Central Bank} decision demonstrates the difficulty of this endeavor and typifies an inherent flaw with textualism, which is the inclination to find that a provision is "clear," thereby allowing a court to end its inquiry.\textsuperscript{76}

2. \textit{Intentionalism}

Unlike textualism, intentionalism emphasizes the actual or presumed intent of the legislature enacting the statute. It provides that judges should use interpretative tools to ascertain the enacting legislature's intent regarding a provision's meaning.\textsuperscript{77} Intentionalism advocates a contextual analysis since a word's meaning is affected by its context and usage.\textsuperscript{78} An intentionalist analysis can be either archeological or purely hypothetical.\textsuperscript{79}

When following archeological intentionalism, a judge searches for clues in the statute's text and its legislative history that might signal a legislative intent regarding the disputed statutory issue.\textsuperscript{80} Thus, intentionalism would support an examination of the events preceding enactment, such as legislative history, because they may provide insight into how the legislature would have wanted a particular question resolved.\textsuperscript{81} However, with hypothetical intentionalism,\textsuperscript{82} a judge

\textsuperscript{72} See Spence, supra note 66, at 587; Farber & Frickey, supra note 1, at 423.
\textsuperscript{73} When Congress decides to create law to remedy past wrongs, such as to provide economic stability in the capital market through the federal securities statutes or to address this country's history of racism through the federal civil rights statutes, a court, which is largely insulated and removed from this discourse, should respect the doctrine of separation of powers and should refrain from usurping Congress' role of legislating.
\textsuperscript{74} Eisenberg, supra note 53, at 22.
\textsuperscript{75} Id. at 22-23.
\textsuperscript{76} The \textit{Central Bank} decision's narrow inquiry that focused on the provision at issue distorted the legislature's intent by failing to address other relevant law, such as relevant statutory provisions.
\textsuperscript{78} Aleinikoff, supra note 5, at 23.
\textsuperscript{80} Id. at 813.
\textsuperscript{81} Id.
\textsuperscript{82} Advocated by Judge Posner, this form of intentionalism questions the use of evidentiary tools, such as committee reports, and argues for a court to engage in
does not ask what the legislature's stated position was, but rather what it would have been had the legislature considered the problem before the court. Accordingly, under this theory, where no clear legislative intent can be discerned, a judge is to take on the role of the legislature and determine what it would have done had it faced the issue.

3. Purposivism

The theory of purposivism focuses on the purpose or objective of the statute. Specifically, purposivism provides that "judges should give weight to the congressional purpose or policy behind the statute's enactment.” Instead of attempting to reconstruct how the legislature would have likely addressed a particular issue, purposivism calls on judges to identify the statute's purpose and to resolve the dispute at issue in light of that purpose. Under this theory, a judge should not ask "how did the enacting legislature intend to resolve the dilemma or how would the enacting legislature have resolved it had it been considered," but a judge should "discern the purpose of the statute by examining the 'mischief' the statute is designed to remedy." A judge is to read the text of the statute carefully, then infer plausible purposes of the language, which are to be rational since the judge has to assume that the legislature consisted of "reasonable persons pursuing reasonable purposes reasonably." Purposivism has been criticized for allowing judges too much discretion, which, according to its critics, may lead judges to substitute their values for that of the legislature.

While intentionalism and purposivism are similar, there is one significant difference between them. Intentionalism asks how the enact-
ing legislature would have decided the interpretive question facing the court. To the contrary, purposivism does not seek to determine the legislature's precise intent. Instead, it assumes a reasonable purpose behind the statute, thereby allowing for more judicial discretion than intentionalism. Nevertheless, both theories promote a judge's review beyond the statutory text into the legislative history to discern the legislature's intent.

The earliest Supreme Court decisions to interpret section 10(b) addressed whether the 73rd Congress intended the section to provide a private right of action. These decisions could be characterized as following the statutory interpretation theory of purposivism, as they focused on the "mischief" the Exchange Act intended to remedy. Indeed, these decisions held that section 10(b) should not be construed technically or restrictively, but flexibly to effectuate the statute's remedial purpose. However, with the retirement of a key member of the Court, Justice Douglas, the Supreme Court's philosophy towards statutory interpretation took a dramatic change of course. The Court went from broadly reading the Exchange Act to following a textualist theory of statutory interpretation. The Court's adoption of textualism in interpreting Section 10(b) has consequently provided

92. Redish & Chung, supra note 79, at 813.
93. Id. at 817.
95. There is a fourth fairly popular school of statutory interpretation, dynamic theory, which essentially analyzes the legislative process by utilizing economics. See Meetre, supra note 49, at 61. Because of a general disbelief with Congress' ability to enact laws that truly serve the public, dynamic theorists argue that judges should, in an effort to reach the best result, engage in active policy making, taking into account current policies and societal values. See Meetre, supra note 49, at 61. See also Eskridge, supra note 47, at 1483 (discussing the dynamic theory of statutory interpretation).
97. Rule 10b-5 was promulgated by the SEC in order to effectuate section 10(b)'s prescriptions. In order to simplify the foregoing discussion hereinafter, rule 10b-5 and section 10(b) will be referred to collectively as section 10(b).
98. Meetre, supra note 49, at 60 (Purposivism provides that judges should look to the purpose or objective of the statute.).
99. Gonzalez, supra note 1, at 611.
102. See Transamerica Mortgage Advisors, Inc. v. Lewis, 444 U.S. 11, 23 (1979)(essential determination to be made is whether Congress expressly intended to create a private remedy); Touche Ross & Co. v. Bedington, 442 U.S. 560, 568 (1979)(appropriate inquiry into the existence of a cause of action is one of express statutory
the Court with a vehicle to restrict the scope of the private civil remedies under the statute. After a brief review of the *Central Bank* decision’s impact on the enforcement provisions of the Exchange Act, the following sections in this Article will critique the development of the Court’s shift in statutory interpretation.

### III. FORMS OF SECONDARY LIABILITY AFFECTED BY *CENTRAL BANK*

Prior to *Central Bank*, private causes of actions under section 10(b) were based upon either primary liability or secondary liability. Generally, primary liability is placed on those who have been participants in the primary wrongdoing or have violated an independent duty. Secondary liability refers to the civil liability that is imposed on those who either assist a primary wrongdoer, as in the case of aiding and abetting, or are in some relationship with the primary wrongdoer, as in the case of respondeat superior.

Approximately ten years after the Exchange Act was passed, a federal court in *Kardon v. National Gypsum Company* recognized an implied private right of action for damages under section 10(b). Interestingly, that case was based upon a secondary liability claim. The court’s creation of a section 10(b) private right of action was based upon the tort law maxim, *ubi jus ibi remedium*, which means that where there is a right, there is a remedy. Subsequently, federal courts, including the Supreme Court itself, upheld section 10(b) claims relying upon secondary liability. Such claims were based on...
a variety of theories, including aiding and abetting, conspiracy, and respondeat superior.\textsuperscript{111}

\section{A. Conspiracy Liability}

Conspiracy, a doctrine originally derived from criminal and tort law,\textsuperscript{112} provides for civil liability against those who enter into an agreement to engage in both a proscribed act and at least one overt act in furtherance of the agreement.\textsuperscript{113} The first federal case that recognized a section 10(b) claim was based on a conspiracy theory.\textsuperscript{114} In \textit{Kardon v. National Gypsum Company},\textsuperscript{115} the plaintiffs accused the defendants of a conspiracy to induce the plaintiffs to sell their stock in two corporations for less than its true value.\textsuperscript{116} The court, following a purposivist theory, concluded that in view of the Exchange Act's general purpose to regulate securities transactions, "the mere omission of an express provision for civil liability is not sufficient to negate what the general law implies."\textsuperscript{117}

Similarly, the first Supreme Court decision addressing section 10(b) upheld a conspiracy-based claim.\textsuperscript{118} In \textit{Superintendent of Insurance of New York v. Bankers Life & Casualty Company},\textsuperscript{119} the plaintiff, a defunct insurance company, alleged that it was defrauded by one of its officers and others in a scheme that caused it to sell its securities in exchange for assets the company already owned.\textsuperscript{120} The \textit{Bankers Life} Court considered the claim to be based on conspiracy\textsuperscript{121} and had little difficulty in finding a cause of action under section 10(b).\textsuperscript{122}

\begin{thebibliography}{99}
\bibitem{111} See \textit{supra} note 110.
\bibitem{112} See Fischel, \textit{supra} note 105, at 80.
\bibitem{113} Lutton, \textit{supra} note 13, at 73.
\bibitem{115} Id.
\bibitem{116} Id. at 513.
\bibitem{117} Id. at 514. The \textit{Kardon} Court based its holding on: (1) section 20(b) of the Restatement (First) of Torts, which provided that the violation of a legislative enactment by engaging in a prohibited act gives rise to liability, and (2) the Supreme Court decision of Texas & Pacific R. Co. v. Rigby, 241 U.S. 33, 39 (1916), which held that a disregard of a command of a statute is a wrongful act and a tort. \textit{Id.}
\bibitem{119} Id.
\bibitem{120} Id. at 7.
\bibitem{121} Id.
\bibitem{122} Id. at 10.
\end{thebibliography}
B. Aider and Abettor Liability

Under the federal securities laws, aiding and abetting liability arises when there is "(1) a securities law violation by a primary party, (2) scienter on the part of the aider and abetter, and (3) 'substantial assistance' by the aider and abettor in the achievement of the primary violation." The seminal case establishing aider and abettor liability under section 10(b) is *Brennan v. Midwestern United Life Insurance Company*, where a plaintiff argued that a corporation was liable as an aider and abettor for the acts of its broker. Mirroring the Supreme Court's analysis in *Central Bank*, the defendant corporation argued that section 10(b) was devoid of any indication that Congress intended to impose aider and abettor liability. The Court, again following purposivism, held that "[i]n the absence of a clear legislative expression to the contrary," section 10(b) should be applied "so as to implement its policies and purposes." The *Brennan* Court also based its decision on section 876 of the Restatement of Torts, which provides for liability for those acting in concert.

C. Respondeat Superior Liability

The doctrine of respondeat superior holds a principal liable for the acts of an agent if those acts were done within the scope of the agent's authority. Thus, the principal may be liable irrespective of her culpable conduct. The only relevant inquiry under the doctrine is whether an individual's fraudulent act was committed within an unauthorized agency relationship. Typically, those who have written

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123. National Union Fire Ins. Co. v. Turtur, 892 F.2d 199, 206-07 (2d Cir. 1989)(In order to establish an aiding and abetting claim, the three elements must be met.). See also Rolf v. Blyth, Eastman Dillon & Co., 570 F.2d 38, 47-48 (2d Cir. 1978) (explaining in detail the three requirements to establish an aiding and abetting violation); Brennan v. Midwestern United Life Ins. Co., 417 F.2d 147, 154 (7th Cir. 1969)(The events that occurred were enough to establish an aiding and abetting violation.).


125. Id.

126. Id. at 676.

127. Id. at 680-81. As will be discussed further below, a review of the 73rd Congress' intent will demonstrate that Congress intended that secondary forms of liability be addressed by the "controlling person" provisions of section 15 of the Securities Act and section 20(a) of the Exchange Act.

128. Id. at 681.

129. Id. at 680 (citing Restatement of Torts § 876 (1939)).


about the applicability of respondeat superior to the law of securities
have also analyzed the control person provisions of both the Securities
Act of 1933 ("Securities Act") and the Exchange Act (collectively the
"Acts").

Section 15 of the Securities Act\textsuperscript{134} and Section 20(a) of the Ex-
change Act\textsuperscript{135} each impose liability on controlling persons. The "con-
trol person" language of these sections has been treated by courts as
the federal securities laws' modified codification of respondeat supe-
rior theories.\textsuperscript{136} There are, however, significant differences between
the Acts' control person liability provisions and the common law's re-
spendeat superior liability doctrine. Unlike the doctrine of respondeat
superior, sections 15 and 20(a) provide "good faith defenses" to control
person liability.\textsuperscript{137} Thus, under respondeat superior, a court will only
look to whether the employee's act was committed within the scope of
the employee's employment;\textsuperscript{138} whereas, under the Acts' control per-
son provisions, an individual who controls a primary wrongdoer is lia-
ble unless the control person acted in good faith and did not directly or
indirectly cause the violation.\textsuperscript{139}

\begin{itemize}
\item Section 15 of the Securities Act, 15 U.S.C. § 77 (1996), provides:
\begin{quote}
Every person who, by or through stock ownership, agency, or other-
wise, or who, pursuant to or in connection with an agreement or under-
standing with one or more persons by or through stock ownership,
agency, or otherwise, controls any person liable under sections [11 or 12]
... shall also be liable jointly and severally with and to the same extent
as such controlled person to any person to whom such controlled person
is liable, unless the controlling person had no knowledge of or reasonable
ground to believe in the existence of facts by reason of which the liability
of the controlled person is alleged to exist.
\end{quote}

\item The defense provision of section 15 absolves controlling persons from liability
when they "had no knowledge of or reasonable ground to believe in the existence of the facts by reason of which the liability of the controlled person is alleged to exist." 15 U.S.C. § 77(1994).

\item The defense provision of section 15 absolves controlling persons from liability
when they "had no knowledge of or reasonable ground to believe in the existence of the facts by reason of which the liability of the controlled person is alleged to exist." 15 U.S.C. § 77(1994).

\item The defense provision of section 20(a) makes controlling persons liable unless
they "acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action." 15 U.S.C. § 78(a)(1994).

\item See 15 U.S.C. § 78(a)(1994); Ruder, supra note 16, at 601-02; Fitzpatrick & Car-
men, supra note 132, at 11.
\end{itemize}
In an effort to prevent defendants from raising the good faith defenses available to them under sections 15 and 20(a), plaintiffs chose to sue under section 10(b) by using the theory of respondeat superior.\textsuperscript{140} By using this tactic, plaintiffs' lawyers effectively circumvent section 15's and section 20(a)'s good faith defenses.\textsuperscript{141}

D. Post-Central Bank: The Death of Common Law Secondary Liability Under Section 10(b)

As the Central Bank dissent feared, most of the post-Central Bank opinions addressing section 10(b) claims based on secondary liability, including aider and abettor, conspiracy, and respondeat superior liability, have rejected such claims.\textsuperscript{142} In fact, to the probable dismay of the dissent, at least one court in a post-Central Bank decision has cited Justice Steven's language as a basis for its decision.\textsuperscript{143}

The post-Central Bank decisions applied the new law to aider and abettor claims and eventually expanded Central Bank to other forms of secondary liability. For instance, in In re College Bound Consolidated Litigation,\textsuperscript{144} one of the first post-Central Bank decisions, the plaintiffs claimed that the defendant was part of "a full-blown conspiracy."\textsuperscript{145} The court treated the claim as an aiding and abetting claim\textsuperscript{146} and reasoned that, in light of Central Bank, in order to state

\textsuperscript{140} Fischel, \textit{supra} note 105, at 86 ("To preclude employers from relying upon this good faith defense, plaintiffs have sued these defendants under section 10(b) using respondeat superior."); Ruder, \textit{supra} note 16, at 602 ("The use of section 15 and 20 has been limited, however, because of the special defenses contained in the sections."); Gordon v. Burr, 366 F. Supp. 156, 167 (S.D.N.Y. 1973) (The principal virtue of using respondeat superior, for a plaintiff, is that section 20(a)'s good faith defenses are unavailable to a defendant.).

\textsuperscript{141} The tactic by plaintiffs' lawyers of avoiding section 20(a) appears to be no longer available in light of Central Bank. Now plaintiffs' lawyers have to contend with the good faith defenses of section 20(a)—the section which all along should have exclusively covered secondary liability claims.

\textsuperscript{142} See, e.g., Securities Investor Protection Corp. v. Holmes, [1995-1996 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 99,038 at 94,165 (9th Cir. Jan. 23, 1996) (securities claims raised were similar to conspiracy or aiding and abetting and, therefore, under Central Bank were unavailable).

\textsuperscript{143} See, e.g., S.E.C. v. United States Envtl., Inc., 897 F. Supp. 117, 119 (S.D.N.Y. 1995) ("However, as the Central Bank dissent pointed out, the Court's reasoning was more expansive, supporting an extension of the holding to actions brought by the Commission, as well as private parties, . . . and to other forms of secondary liability, such as civil conspiracy as well as aiding and abetting.").


\textsuperscript{145} \textit{Id.} at 90,134.

\textsuperscript{146} Although the College Bound decision refers to the complaint, which purportedly refers to the defendants' acts as a conspiracy, the court treated the claims as if they were aider and abettor claims. \textit{Id.}
a claim a plaintiff has to allege that the defendant violated section 10(b) as a primary violator.\textsuperscript{147}

With but two exceptions,\textsuperscript{148} subsequent cases expanded Central Bank's mandate, dismissing conspiracy claims.\textsuperscript{149} Indeed, these courts held that Central Bank's rationale applied to aider and abettor claims as well as claims sounding in conspiracy.\textsuperscript{150} In addition, at least one decision has applied Central Bank to dismiss a claim based on respondeat superior.\textsuperscript{151} Thus, courts have concluded that control person liability under section 20(a) is the only form of secondary liability that remains available under the Exchange Act.\textsuperscript{152}

While some decisions have avoided expanding Central Bank's holding,\textsuperscript{153} one post-Central Bank decision refused to dismiss a section

\textsuperscript{147} Id.


\textsuperscript{150} In these decisions, the courts dismissed the aiding and abetting claims but did not dismiss other secondary liability claims. How long these lower courts will be able to avoid addressing the issue of expanding Central Bank to other forms of
10(b) secondary liability claim. In *Pollack v. Laidlaw Holdings*,154 the plaintiffs asserted section 10(b) claims against the defendants based on apparent authority.155 After noting that *Central Bank* "called into question all common law claims that are adjunct to a direct securities claim," the court distinguished claims based upon apparent authority156 from aiding and abetting and respondeat superior claims.157 Secondary liability is subject to question. The *Medeva* and *Omnitrition* opinions did not address the *Central Bank* decision in their analysis of the conspiracy claims, but it is unclear whether defendants raised the *Central Bank* argument. *In re Medeva Sec. Litg.,* [1994-1995 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,325 at 90, 238 (C.D. Cal. June 8, 1994)(holding that the plaintiffs had adequately stated a claim for secondary liability under control person liability and conspiracy under section 10(b)); *In re Omnitrition Intl., Inc., Sec. Litig.,* [1994-1995 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,425 at 90,923(N.D. Cal. July 26, 1994)(plaintiffs did not have enough evidence to state their conspiracy claims). In another post-*Central Bank* decision, the court refused to dismiss the conspiracy claims, finding that defendants were charged with primary liability. *Adam v. Silicon Valley Bancshares,* 884 F. Supp. 1398, 1402 (N.D. Cal. 1995)(explaining that the *Central Bank* decision limited its holding to the issue of whether a private cause of action existed for aiding and abetting).

The *Pollack* decision is flawed. While it refers to *Central Bank*, it does not follow its language. The *Pollack* decision did not recognize that section 10(b) made no reference to vicarious liability or apparent authority. *Id.* Accordingly, under *Central Bank*, the claims in *Pollack* should have been dismissed. The *Pollack* court upheld the apparent authority claim because such claims were widely recognized by federal courts and by pointing out that under the apparent authority theory it is not necessary that the agent act with the intent to benefit the principal. *Id.* at 92,510. The court distinguished respondeat superior liability by noting that it is based solely on the position of the employee, whereas under apparent authority, it requires some preexisting relation between the principal and the customer. *Id.* at 92,510 n.20.

The *Pollack* decision, however, is flawed. While it refers to *Central Bank*, it does not follow its language. The *Pollack* decision did not recognize that section 10(b) made no reference to vicarious liability or apparent authority. *Id.* Accordingly, under *Central Bank*, the claims in *Pollack* should have been dismissed. The *Pollack* court upheld the apparent authority claim because such claims were widely recognized by federal courts. This same argument was made in *Central Bank* in an effort to uphold aider and abettor liability under section 10(b) but was specifically rejected by the Court. *Central Bank of Denver v. First Interstate Bank of Denver,* 511 U.S. 164, 178 (1994). The *Pollack* court should have addressed the issue more directly by using the line of cases prior to *Central Bank*, where the Supreme Court endorsed liability under section 10(b) and other statutory claims based on agency and other secondary liability principles. In particular, the *Pollack* court could have rested its decision on the *Affiliated Ute* decision, where the Supreme Court upheld section 10(b) liability based on respondeat superior and stated that "the liability of [a] bank, of course, is coextensive with that of [its officers]." *Affiliated Ute Citizens of Utah v. United States,* 406 U.S. 128, 154 (1992). See also supra note 109.
In short, most lower courts have expanded Central Bank's holding. However, a few have either avoided the issue or refused to apply Central Bank's analysis to other forms of secondary liability. The following section demonstrates how the inconsistent treatment of the Central Bank decision by lower courts is a result of the Central Bank Court's failure to reconcile inconsistent precedent and to fully address the role of secondary liability under the Exchange Act.

IV. THE GENESIS AND EVOLUTION OF THE SUPREME COURT'S THEORY OF STATUTORY INTERPRETATION WITH RESPECT TO SECTION 10(b)'S PRIVATE RIGHT OF ACTION

Shortly after the Stock Market Crash of 1929, the 73rd Congress enacted the first two components of the federal securities statutory scheme. The Securities Act and the Exchange Act sought to protect investors and promote market stability by instituting a philosophy of full disclosure concerning the companies traded in the securities market. In order to ensure that their purposes would be achieved, Congress provided that violators of the Acts would be subject to criminal sanctions and express civil private rights of action. In addition, federal courts, acknowledging the remedial purpose of the legislation, implied private rights of action under other provisions of the Acts.


160. See also Superintendent of Ins. v. Bankers Life & Cas. Co., 404 U.S. 6, 12 (1971); J. I. Case Co. v. Borak, 377 U.S. 426, 432 (1964)(holding that among the chief purposes of the Exchange Act is the protection of investors); Radzanower v. Touche Ross & Co., 426 U.S. 148, 155 (1976)(the primary purpose of the Exchange Act was "to provide a fair and honest mechanism for the pricing of securities.").
One such implied private right of action became the key enforcement tool of the Exchange Act, deriving from section 10(b) and its administrative counterpart, rule 10b-5.

Essentially, a section 10(b) action is a claim based on fraud. Despite the onerous pleading requirements for drafting a claim based on fraud, the right of action under section 10(b) and its administrative counterpart, rule 10b-5, became the primary enforcement tool for private litigants. In fact, section 10(b) has been considered the “catch-all antifraud provision” and the “all-encompassing” antifraud

of a private cause of action for violations of section 10(b) and Rule 10b-5; J.I. Case Co. v. Borak, 377 U.S. 426, 432 (1964) (Even though there is no specific reference to a private cause of action, one of the chief purposes is to protect investors.); Kardon v. National Gypsum Co., 69 F. Supp. 512, 514 (E.D. Pa. 1946)(holding that civil liability for violation of a statute accrues to a member of a class, which in this case is any type of investor in the securities market); Brennan v. Midwestern United Life Ins. Co., 259 F. Supp. 673, 680 (N.D. Ind. 1966)(civil liability was rested on the tort principles of “maxim, ubi jus, ibi remedium” - where there is a right, there is a remedy, by the courts in general); See also L. Loss & J. Seligman, Securities Regulation, 4312-39 (1992)(collecting cases).

162. Joseph A. Grundfest, Disimplying Private Rights of Action Under the Federal Securities Laws: The Commission's Authority, 107 Harv. L. Rev. 961, 965 (1994)(section 10(b) and rule 10b-5 have become civil plaintiffs' primary weapon in their battle against securities fraud). See also Sager, supra note 103, at 822 n.5 (roughly one-third of all securities law cases are brought under section 10(b) and rule 10b-5; by 1965 Rule 10b-5 was generating almost as much litigation as all the other general antifraud provisions combined); Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299, 310 (1985)(implied private rights of action provide a most effective weapon in the enforcement of the securities laws).

163. Section 10(b)'s administrative counterpart, rule 10b-5, promulgated by the SEC, 17 C.F.R. § 240.10b-5 (1994), provides:

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.


165. Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299, 310 (1985) ("Implied private rights of action provide a most effective weapon in the enforcement of the securities laws."). See also Grundfest, supra note 162, at 963 (the private right of action implied under rule 10b-5 has become civil plaintiffs' primary weapon in their battle against securities fraud); Daniel J. Bacastow, Due Process and Criminal Penalties Under Rule 10b-5: The Unconstitutionality and Inefficiency of Criminal Prosecutions for Insider Trading, 73 J. Crim. & Criminology L. 96 (1982)(Rule 10b-5 has for many years served as a foundation for an aggressive enforcement program under the federal securities laws.).
enforcement tool of the securities laws. Therefore, private litigants frequently used section 10(b) to bring both primary and secondary liability claims.

A. The Early Cases

In the Supreme Court's earliest decision interpreting section 10(b), it, following the theory of purposivism, focused on the "mischief" the statute was designed to remedy and emphasized the remedial purpose behind the Exchange Act. Specifically, in the first instance where the Court addressed section 10(b), the Court led by Justice Douglas, the leading securities scholar on the Court, held that the Acts should be read liberally. In Superintendent of Insurance of New York v. Bankers Life & Casualty Co., the plaintiff, a liquidator of an insurance company, alleged that the company was wrongfully induced to sell securities owned by it. Justice Douglas, writing for a unanimous Court, upheld the corporation's right of action to redress section 10(b) violations. He concluded that "section 10(b) must be read flexibly, not technically and restrictively." In addressing the conspiracy claim, Justice Douglas noted that the fact that the fraud was perpetrated by an officer of [the corporation] and his outside collaborators is irrelevant to our problem. . . . Since there was a sale of a security and since fraud was used in connection with it, there is redress under section 10(b), whatever might be available as a remedy under state law.

A year later, in 1972, the Court decided Affiliated Ute Citizens of Utah v. United States. Justice Douglas, writing for the Court again, referred back to his language in Bankers Life and focused on

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167. See Fischel, supra note 105, at 20-83; Ruder, supra note 16, at 600; Sager, supra note 103, at 821.
168. Gonzalez, supra note 1, at 610.
172. Id. at 7-8.
173. Id. at 12.
174. Id. at 10, 12.
the legislation's purpose. The Court held that the Exchange Act was to be construed "not technically and restrictively, but flexibly to effectuate its remedial purposes."  

B. The Cort v. Ash Test for Implying Private Rights of Action

Shortly after the Court's first proclamations concerning section 10(b), the Court resolved the issue of when a court could imply a right of action under a statute. To resolve this issue, the Court endorsed its previous focus on the legislature's purpose. In a unanimous decision, the Court in Cort v. Ash appeared to follow a purposivist-intentionalist combination and established four factors to determine whether there is a private remedy implicit in a statute. The factors established by Cort did not focus on the language of the statute, but on its purpose. These factors were: (1) whether the plaintiff was a part of the intended class targeted by the statute; (2) whether there was any indication of legislative intent, explicit or implicit, either to create such a remedy or to deny one; (3) whether it is consistent with the underlying purposes of the legislative scheme to imply such a remedy; and (4) whether the cause of action is one traditionally delegated to state law. Even Justice Rehnquist, a follower of textualism, accepted the fact that three out of the four Cort factors focused on legislative intent.

176. Interestingly, the first two Supreme Court decisions to recognize an implied cause of action under section 10(b), Banker's Life and Affiliated Ute, were based on secondary liability claims, conspiracy and respondeat superior, respectively. Although conspicuously not addressed by the majority in Central Bank, the Affiliated Ute decision is at odds with Central Bank not only because of its broad reading of the statute, but also because it specifically recognized an implied right of action based upon secondary liability. The Affiliated Ute Court, relying on agency principles, found a bank liable as a result of the actions of its employees. Resting its decision on respondeat superior or other agency-like principles, the Court concluded, without discussion or analysis, that "the liability of the bank, of course, is coextensive with that of [its officers]."  

177. Id. at 151.


179. It should be noted that the Cort v. Ash test is not confined to implying rights under the securities laws. Id. at 66.

180. Id. at 78.

181. Id.

182. Id.

183. Id.


185. Touche Ross & Co. v. Redington, 442 U.S. 560, 575-76 (1979)("Indeed, the first three factors discussed in Cort—the language and focus of the statute, its legislative history and its purpose . . . are ones traditionally relied upon in determining legislative intent.").
C. The Move Towards Textualism

With the retirement of Justice Douglas, the Court, which was for the most part comprised of the same justices, rejected its previous unanimous decisions without expressly analyzing them and initiated its move towards a textualist interpretation of the securities laws. The clearest example of the Court’s shift comes from the *Touche Ross & Co. v. Redington* decision. The *Touche Ross* Court held that the appropriate inquiry into the existence of a statutory cause of action is one of express statutory intent, and summarily concluded that determinations of implied causes of action based on tort principles were misplaced. The *Touche Ross* Court, focusing on the language of section 17(a) of the Exchange Act, concluded that it did not provide a private right of action because there was no express congressional intent to create such a remedy. The *Touche Ross* Court gave lip service to the *Cort* decision by allegedly focusing on Congress’ intent, but also noted that the central inquiry was whether Congress gave express indications in the statute that it intended to create a cause of action.

The Court’s analysis in *Touche Ross* was a drastic departure from the Court’s earlier proclamations concerning statutory interpretation in the securities field. Indeed, the decision represented a rejection of the Court’s previous philosophy, pronounced in *Cort*, concerning implied rights of action. In support of its new textualist approach, the *Touche Ross* Court quoted from its decision in *Cannon v. University of Chicago*, which noted that “the fact that a federal statute has been violated and some person harmed does not automatically give rise to a private cause of action in favor of that person.” Thus, the *Touche Ross* Court used the *Cannon* quote to suggest that the Court had previously moved closer to adopting a textualist philosophy.

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187. Id. at 568.
188. Id.
189. Id. at 575-76.
194. Id. at 688.
195. Interestingly, the *Cannon* Court never distinguished its decision in *Texas Pacific R. Co. v. Rigsby*, 241 U.S. 33, 39 (1916), which specifically held that a violation of a statute is tantamount to a tort.
While the 

Touche Ross

Court cited to Cannon in order to support its new approach to statutory interpretation, the decision mischaracterized Cannon. Despite the quote in Cannon, the Cannon Court did not use a textualist approach, but instead relied on the Cort decision's four factors. In fact, using an analysis that was completely at odds with Touche Ross' textual approach, the Cannon Court held that "the threshold question under Cort is whether the statute was enacted for the benefit of a special class of which the plaintiff is a member." In the same year that the Court decided Touche Ross, the Court decided Transamerica Mortgage Advisors, Inc. v. Lewis, where it rejected an implied claim under section 206 of the Investment Advisors Act of 1940. Once again, the Court mischaracterized the Cannon decision and implicitly rejected the Cort factors. The Transamerica Court held that the essential determination to be made is whether Congress expressly stated its intent in the statute to create the private remedy asserted.

Prior to its decision in Touche Ross, the Court, in the context of section 10(b) jurisprudence, gave indications of its intent to change its approach with regards to statutory interpretation. The earliest example was Blue Chip Stamps v. Manor Drug Stores, where the Court focused on section 10(b)'s language and made a fairly unremarkable conclusion of limiting recovery for manipulative or deceptive acts to section 10(b)'s "in connection with the purchase or sale of (or any attempt to sell) a security" language. A year later, after Justice Douglas had resigned, the Court in Ernst & Ernst v. Hochfelder began its attack on its previous holdings concerning statutory interpretation. The issue before the Hochfelder Court was whether section 10(b) proscribed negligent conduct. The Court, relying heavily on the language of the section, held that because section 10(b) "clearly connotes intentional misconduct," negligent conduct does not give rise to liability under the section. The Hochfelder Court pronounced, for the first time in the securities area, that the statute's language was the focus and starting point of the Court's analysis. Shortly after Hochfelder, commentators predicted that the decision repre-

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197. Id. at 689.
199. Id. at 15-16.
200. Id.
202. Id. at 732.
204. Id. at 187-88.
205. Id. at 201.
206. Id. at 197.
sent the Court's shift towards textualism and its new effort to limit the scope of the coverage and protections the Acts offered to the investing public.\textsuperscript{207}

Interestingly, the cases that the \textit{Ernst} Court cited do not support its textualist twist. For instance, \textit{Ernst} cited to Justice Powell's concurring opinion in \textit{Blue Chip Stamps v. Manor Drug Stores},\textsuperscript{208} where he noted that when interpreting a statute a court should begin with the language of the statute. However, Justice Powell's opinion also acknowledged the usefulness of looking at the statute's legislative history.\textsuperscript{209} Additionally, the \textit{Ernst} Court cited to \textit{FTC v. Bunte Bros, Inc.},\textsuperscript{210} where the Court specifically held that when interpreting a statute a court should not interpret the statute by exclusively looking at its text.\textsuperscript{211}

A year after its decision in \textit{Ernst}, the Court in \textit{Santa Fe Industries, Inc. v. Green},\textsuperscript{212} predictably by then,\textsuperscript{213} rejected the fraud claims of the minority shareholders against the parent company's merger efforts because "[t]he language of section 10(b) gives no indication that Congress meant to prohibit any conduct not involving manipulation or deception."\textsuperscript{214} Subsequent decisions similarly followed a textualist approach.\textsuperscript{215}

In short, soon after the Court held that section 10(b) should be read broadly and established the \textit{Cort v. Ash} test to determine when a cause of action may be implied under a statute, the Court began to demonstrate its fondness for the textualist approach, thereby "effectively overruling" established law such as \textit{Cort} and \textit{Banker's Life}, without specifically analyzing or overturning it.\textsuperscript{216} The Court charted


\textsuperscript{208} Ernst & Ernst v. Hochfelder, 425 U.S. 185, 179 (1975).


\textsuperscript{210} Ernst & Ernst v. Hochfelder, 425 U.S. 185, 179 (1975).

\textsuperscript{211} Federal Trade Comm'n v. Bunte Bros, 312 U.S. 349, 351 (1941).

\textsuperscript{212} 430 U.S. 462 (1977).

\textsuperscript{213} Finding that Congress did not intend "to bring within the scope of section 10(b) instances of corporate mismanagement," the Court noted that private rights of action "should not be implied where it is 'unnecessary to ensure the fulfillment of Congress' purposes' in adopting that Act." \textit{Id.} at 477.

\textsuperscript{214} \textit{Id.} at 473 (emphasis added).


\textsuperscript{216} Thompson v. Thompson, 484 U.S. 174, 189 (1988)(O'Connor, J., concurring)("We effectively overruled the \textit{Cort v. Ash} analysis in \textit{Touche Ross & Co. v. Redington} and \textit{Transamerica Mortgage Advisors, Inc. v. Lewis}, converting one of [Cort's] four factors (congressional intent) into the determinative factor, with the other three merely indicative of its presence or absence.") (emphasis added).
a new course—sometimes through the use of misquotations and misplaced reasoning such as in *Touche Ross*\(^{217}\)—that resulted in a narrower, inflexible approach to statutory interpretation.\(^{218}\) Eventually, this new approach, which called for a threshold and primary analysis of the language of the statute itself,\(^{219}\) led to an exclusive inquiry into only the text of the statute as evidenced in *Central Bank*.

The trend in Supreme Court securities caselaw of overturning law by implication in the name of textualism is troubling and should not be condoned because it rejects the foundation of jurisprudence—the value of precedent. As evidenced in its development in the securities field, textualism, notwithstanding its proclamations to the contrary, actually facilitates a judge’s manipulation of the provision at issue, along with prior precedent, in order to find a “plain meaning.”\(^{220}\) Such an approach can easily lead to perceptions that the decision was based on unspoken policy motivations.\(^{221}\) While textualism may lead to conclusions that are ultimately correct, particularly when the legislative history is consistent with a plain meaning analysis, the following sections illustrate how the textualist approach may distort the legislature’s intent and may leave more issues unresolved than a decision settles.

**D. How *Central Bank* Illustrates an Inherent Flaw in the Textualist Approach**

Not only is the Court’s textualist approach in *Central Bank* of troubling precedential underpinnings, but the *Central Bank* decision also typifies a fundamental flaw in textualist theory. By undertaking a virtually exclusive focus on the text of the provision at issue, the textualist approach effectively facilitates rewriting the statute at issue.

One of the many criticisms of the textualist approach is the difficulty in identifying the relevant canonical text.\(^{222}\) One writer asks, “Is the relevant text then only the statutory provision or the entire statute? . . . Going one step further, it would be equally foolish to treat as irrelevant the text of any statute adopted by the legislature that adopted the provision at issue.”\(^{223}\) While textualism in theory supports a review of the entire statute at issue, in practice, a judge apply-

\(^{217}\) See supra notes 185–95 and accompanying text.

\(^{218}\) See also Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975)(focusing on the language of section 10(b) and prohibiting plaintiffs who were neither purchasers nor sellers of securities).


\(^{220}\) Zeppos, supra note 2, at 1322. See also Plass, supra note 2, at 110-21.

\(^{221}\) Ross, supra note 66 (arguing that textualism can lead to a partisan application of the law).

\(^{222}\) See Eisenberg, supra note 53, at 22-26; Plass, supra note 2, at 107-08.

\(^{223}\) Eisenberg, supra note 53, at 22-23.
ing textualism can easily conclude that the text of a provision at issue is clear, thereby limiting her inquiry to the text of that provision.\textsuperscript{224} Such an approach allows the judge to usurp the legislative function and to deviate from the legislature's intent.\textsuperscript{225} Unfortunately, in many respects, this is exactly what occurred in \textit{Central Bank}.

The \textit{Central Bank} Court stated that even if the text of section 10(b) did not resolve the issue, it would nevertheless have reached the same conclusion as a result of looking at the express rights of action under the Securities Act and the Exchange Act.\textsuperscript{226} The Court, however, proceeded to analyze the issue narrowly by only looking at the provisions where aider and abettor liability arose under the Acts.\textsuperscript{227} Using this myopic approach to resolve an issue of secondary liability gave the Court ample opportunity to avoid other relevant text in the Exchange Act. Although the decision failed to address it,\textsuperscript{228} the truly relevant issue the Court was analyzing was the role of secondary liability under the Exchange Act. However, by narrowly focusing its analysis on aider and abettor liability under section 10(b), the Court was able to limit its inquiry to aider and abettor liability under the Acts and to section 10(b) precedent.\textsuperscript{229} The Court utterly failed to address the provision in the Exchange Act that was most relevant—section 20(a)—where Congress expressly addressed secondary liability.\textsuperscript{230}

Although the decision only dealt specifically with aiding and abetting, as addressed previously, it has been interpreted to be much broader in scope.\textsuperscript{231} Several writers, including Justice Stevens, have noted that as a result of the decision, private litigants will have to resort to theories of liability based on primary violations.\textsuperscript{232} To most observers, the \textit{Central Bank} Court effectively pruned the judicial oak\textsuperscript{233} by removing a massive bough with leaves that constituted all the traditional forms of secondary liability.\textsuperscript{234} While section 20(a)’s

\textsuperscript{224} \textit{See}, e.g., Plass, \textit{supra} note 2, at 106.

\textsuperscript{225} Eisenberg, \textit{supra} note 53, at 23-24. \textit{See also} Plass, \textit{supra} note 2, at 106. As mentioned above, a basic goal of textualism is to avoid judges replacing the legislature's values with their own. \textit{See supra} note 56 and accompanying text.


\textsuperscript{227} \textit{Id.} at 180-81.

\textsuperscript{228} \textit{Id.} at 185.

\textsuperscript{229} \textit{Id.} at 178-88.


\textsuperscript{231} Steinberg, \textit{supra} note 14, at 500. \textit{See also} \textit{supra} notes 143-51.


\textsuperscript{233} \textit{Blue Chip Stamps v. Manor Drug Stores}, 421 U.S. 723, 737 (1975).

control person liability is still available as a basis for secondary liability, as a result of the decision's failure to fully address the role of secondary liability under the Exchange Act and the deemphasizing of section 20(a) by the plaintiffs' bar, many observers, including a minority of justices on the Court, call into question the role of secondary liability under the Exchange Act.235 Therefore, as a result of the flawed use of the textualist approach, the 73rd Congress' intended vehicle for addressing secondary liability—section 20(a)—currently remains misunderstood and underutilized.237

V. THE ISSUES LEFT UNRESOLVED BY AND THE IMPACT OF THE CENTRAL BANK DECISION

The Central Bank decision has been described as a bombshell that has ushered in a new era of reform,238 but the decision is not even internally consistent. Using a textualist approach, the Court refused to recognize under section 10(b) a common form of secondary liability, aider and abettor liability, because the "text" of the statute did not explicitly provide for such a claim. Under this approach, however, there should be no rights of action under section 10(b) because the text of the section contains no explicit rights of action. Nonetheless, the Central Bank Court—in the same breath that it rejected aider and abettor liability—specifically recognized an implied section 10(b) right of action against primary violators.239

Since Congress did not create a section 10(b) private cause of action, the Court was thus left with the task of determining the parameters of a cause of action that under its own approach would not be


236. Because of the unique nature of section 10(b), that is, having no legislative history relating to a private remedy, it is unclear whether the Court will use its strict constructionist approach with other provisions of the securities laws. Notwithstanding the new greater acceptance of the strict textualism approach, it is imprudent for the Court to disregard legislative history when it addresses the language of a statute. It is hoped that the current Court will limit the use of its pure textualist approach to only addressing other attempts to imply a right of action.

237. See infra notes 283-323 and accompanying text. See also Baum, supra note 14, at 1839-41.


recognized.\textsuperscript{240} The Court was unwilling to strike down section 10(b)'s implied private right of action because in previous decisions it had acquiesced to lower court recognition of the right of action.\textsuperscript{241} But, as the dissent pointed out, aider and abettor liability under section 10(b) was also equally accepted by all courts addressing the issue.\textsuperscript{242} Even more troubling is the fact that the Court had specifically and previously recognized other forms of secondary liability under section 10(b).\textsuperscript{243} The Court also had little difficulty in speculating on Congress' intent,\textsuperscript{244} despite earlier Court decisions warning that "[t]he Court should] by no means be understood as suggesting that we are able to divine from the language of section 10(b) the express 'intent of Congress' as to the contours of a private cause of action under rule 10(b)."\textsuperscript{245}

Instead of addressing the questions presented by the certiorari petition,\textsuperscript{246} the Central Bank Court directed the parties to address an issue that even the defendants' lawyers believed was settled—whether aiding and abetting could be the basis for a section 10(b) claim.\textsuperscript{247} In fact, the Court sought to resolve an issue it specifically reserved in two previous decisions.\textsuperscript{248} Thus, a conservative court that purportedly prides itself on judicial restraint engaged in selective activism. Unfortunately, in doing so, the Court rendered a sweeping de-

\textsuperscript{244} See supra note 39.
\textsuperscript{245} Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 737 (1975).
\textsuperscript{246} While it may have been more prudent for Congress, either when the provision was enacted or subsequently to specifically recognize a private right of action under section 10(b), this Article does not support a dismantling of the implied right of action under section 10(b) against primary violators. As the Court and commentators have previously recognized, private enforcement of the securities laws, especially through section 10(b), has played an essential role in effectuating Congress' purpose for enacting the federal securities laws. Hassett, supra note 240, at 152.
cision with broad implications that left at least as many unresolved issues as were present before the decision was rendered. After Central Bank, aiding and abetting claims under section 10(b) are not viable, but questions remain concerning the status of conspiracy claims.249 For instance, how is an attorney or a court to resolve the conflict between Central Bank250 and Bankers Life, which upheld an implied cause of action under section 10(b) against conspirators?251 If the law is as most subsequent lower courts have resolved it, would it not have been more prudent for the Supreme Court to resolve any potential confusion?252

Likewise, it appears that under Central Bank's analysis, respondeat superior claims under section 10(b) may no longer be viable.253 If that is the case, how does a federal court reconcile Central Bank254 and Affiliated Ute, which upheld a section 10(b) claim based upon agency principles?255 While it may be that the Central Bank Court rejected Affiliated Ute and Bankers Life sub silentio because the decision only addressed aiding and abetting,256 is there a reason for an exception?257 Should the Court continue to follow Central Bank's approach of rejecting prior decisions, such as Affiliated Ute and Bankers Life, by implication? Is it not more appropriate for the Court to address related issues when addressing a consequential statutory issue? Is it better for the Court to leave these questions to be resolved by lower courts? Was the Court furthering its new approach to statutory

249. See supra notes 147 and 150 and accompanying text.
255. Id. at 200-01 n.12 (Stevens, J., dissenting)(following the majority's rationale, respondeat superior "appear[s] unlikely to survive"). See also Steinberg, supra note 14, at 501 ("In view of the Supreme Court's Central Bank decision, the continued vitality of respondeat superior is open to debate.").
257. While the Court in Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976), and Herman & MacLean v. Huddleston, 459 U.S. 375 (1983) had previously refused to address whether section 10(b) provided for aider and abettor claims, these decisions do not reject Affiliated Ute Citizens of Utah v. United States, 406 U.S. 128 (1972) and Superintendent of Insurance of New York v. Bankers Life & Casualty Co., 404 U.S. 6 (1971).
interpretation regardless of the decision's repercussions? In what could be perceived as a pro-deep-pocket defendant decision, did the Court further the purposes of the securities laws, for example, to protect investors and to provide efficient markets through full and fair disclosure to investors? There is little guidance given to the judiciary and the bar if the Court, in an effort to become more proactive to resolve an unsettled question, created more questions than it settled.

VI. AN ALTERNATIVE APPROACH—A SYSTEMATIC ARCHEOLOGICAL INTENTIONALIST APPROACH

After reviewing the Central Bank decision, commentators have questioned whether the Supreme Court will now address the litany of unresolved secondary liability issues left by its decision. As mentioned previously, textualism in theory allows a court to examine the structure of a statute in order to confirm its interpretation; but the form of new textualism applied in Central Bank failed to look beyond the provision at issue. Because the Central Bank Court was analyzing the role of secondary liability in the Exchange Act, it should have addressed the Act's secondary liability provision. Apparently, the Court did away with common law secondary liability claims under Section 10(b) of the Exchange Act. The only available alternative for plaintiffs to bring such claims is based upon section 20(a)'s control person liability. However, lower courts have long been in conflict over the appropriate role and scope of section 20(a).

This Article does not call for the Court to merely engage in dictum. The Central Bank Court sought to resolve an important issue involving the statutory framework of the securities laws, despite the fact that the parties themselves had not raised the issue, but rendered a sweeping decision whose impact went far beyond the Court's limited analysis. Since the Court was analyzing one component of secondary liability under the Exchange Act, yet rendered a decision that has affected all forms of secondary liability under the Exchange Act, the Court should have addressed those other forms of secondary liability, along with the secondary liability provision of the Exchange Act—sec-

258. J.I. Case Co. v. Borak, 377 U.S. 426 (1964)(unanimous court noting that among the chief purposes of the securities laws is the protection of investors).
259. See, e.g., Matthews & Callcott, supra note 20 ("The Central Bank decision will render more significant the explicit sources of secondary liability in the federal securities law: § 15 of the 1933 Act and § 20(a) of the 1934 act. . . . Perhaps now the Court will see fit to review the crazy quilt that lower courts have made of § . . . 29(a).”).
260. See supra notes 50-65 and accompanying text.
Accordingly, by engaging in this more prudent course, the Court not only could have addressed the unresolved issues relating to section 10(b) raised by its decision, but also could have resolved the litany of unresolved issues pertaining to secondary liability under section 20(a).264

VII. PRE- & POST-CENTRAL BANK CONFLICT OVER SECTION 20(a)

The federal circuits have been in considerable conflict over which provisions of the Exchange Act addressed secondary liability. Plaintiffs' lawyers have effectively circumvented section 20(a)'s statutory good faith defenses by bringing agency and other forms of secondary liability under section 10(b).265 Over time, this resulted in relegating section 20(a) to a minor component of the enforcement provisions of the securities laws.

Had the Central Bank Court more exhaustively addressed the issues it was opining upon, it would have resolved the question concerning the appropriate vehicle for bringing secondary liability claims under the Exchange Act. Even under a traditional textualist analysis, an inquiry into the legislative history of an ambiguous statutory provision is appropriate to buttress a court's conclusion.266 Had the Central Bank court undertaken such an approach to ascertain the 73rd Congress' meaning of the ambiguous term "control person,"267 the Court should have concluded that section 20(a) is the only provision in the Exchange Act where such claims could be brought. Nevertheless, it appears to be settled that, as a result of Central Bank, section 20(a), which remains subject to various interpretations, is the exclusive means under the Exchange Act by which a plaintiff can bring a secondary liability claim.268

263. While section 20(a) refers to "control person," federal courts have not limited this provision to individuals. See, e.g., Vucinich v. Paine, Webber, Jackson & Curtis, Inc., 803 F.2d 454, 461 (9th Cir. 1986); DelPorte v. Shearson, Hammill & Co., 548 F.2d 1149, 1153-54 (5th Cir. 1977); SEC v. First Sec. Co., 463 F.2d 981, 986-87 (7th Cir. 1972); see also Burns, supra note 133, at 1187 ("Courts have expanded the [control person] provisions to include claims against firms and corporations.").


265. See Fischel, supra note 105, at 86 ("[T]o preclude employers from relying upon this good faith defense, plaintiffs have sued defendants under section 10(b) using the theories of respondeat superior."). In addition, prior to Central Bank, it was fairly common in securities litigation for plaintiffs' lawyers merely to add a control person cause of action that mirrored the section 10(b) secondary liability claim.

266. See supra note 54 and accompanying text.

267. Eisenberg, supra note 53, at 29-36; Plass, supra note 2, at 107-08.

Interestingly, an ill-reasoned Supreme Court decision now focuses the debate on the conflict concerning the role of section 20(a), the section that the enacting Congress intended secondary claims to be brought under in the first place. But that ill-reasoned decision, instead of merely alluding to the issue, could have resolved the conflicts concerning section 20(a). A review of the legislative history of the Exchange Act demonstrates that the 73rd Congress intended that section 20(a) be both broad in scope and the exclusive means of addressing secondary liability under the Exchange Act. The conflict concerning the intended role of section 20(a) and the weakness of the pre-Central Bank majority view will be brought to light by analyzing Congress' intent with regard to secondary liability.

VIII. THE EXCLUSIVITY OF SECTION 20(a)

The pre-Central Bank majority view on the exclusivity of section 20(a) held "that section 20(a) was intended to supplement, and not supplant," the common law theory of respondeat superior as a basis for secondary liability in securities cases. Essentially, the majority view supported relegating the importance of section 20(a) claims to virtually an afterthought of section 10(b) secondary liability claims. As a result of Central Bank, that majority view fails; and section 20(a)
remains the exclusive means for addressing secondary liability under the Exchange Act. Nevertheless, a review of the legislative and judicial authority concerning the role of section 20(a) demonstrates that the Central Bank Court, while not fully resolving the issue of secondary liability, was correct in rejecting secondary liability claims under section 10(b) because Congress did not intend for the Exchange Act's key secondary liability provision, section 20(a), to be supplemented by common law claims under section 10(b).

The leading pre-Central Bank majority view decisions, coming from the Second and Fifth Circuits, held that the legislative history of section 20(a) does not reflect any congressional intent to restrict secondary liability for violations of the Act's control person provision. The Fifth Circuit stated in Paul F. Newton & Co. v. Texas Commerce Bank that "limiting secondary liability under the [Exchange Act] to that liability provided by section 20(a) would contradict the pervasive application of agency principles in nearly all other areas of the law." Courts and scholars supporting this view have also cited to the Exchange Act, section 28, which provides that "[t]he rights and remedies provided by this title shall be in addition to any and all other rights and remedies that may exist at law or in equity." For example, Professors Loss and Seligman argue that section 28's savings clause is eloquent testimony to the absence of any intent to preempt common law secondary liability.

A single circuit court, which is now in the majority as a result of Central Bank, held that section 20(a) is the exclusive means for estab-

276. See, e.g., Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1577 (9th Cir. 1990); Marbury Management, Inc. v. Kohn, 629 F.2d 705, 712 (2d Cir. 1980); Paul F. Newtown & Co. v. Texas Commerce Bank, 630 F.2d 1111, 1118 (5th Cir. 1980); S.E.C. v. Management Dynamics, Inc., 515 F.2d 801, 812 (2d Cir. 1975).
277. Paul F. Newton & Co. v. Texas Commerce Bank, 630 F.2d 1111, 1118 (5th Cir. 1980).
278. L. Loss & J. Seligman, supra note 261, at 4477. See also Marbury Management, Inc. v. Kohn, 629 F.2d 705, 716 (2d Cir. 1980); Paul F. Newton & Co. v. Texas Commerce Bank, 630 F.2d 1111, 1118 (5th Cir. 1980).
279. 15 U.S.C. § 78bb (1994), provides in pertinent part:
   The rights and remedies provided by this title shall be in addition to any and all other rights and remedies that may exist at law or in equity; but no person permitted to maintain a suit for damages under the provisions of this chapter shall recover, through satisfaction of judgement in one or more actions, a total amount in excess of his actual damages on account of the act complained of.
280. L. Loss & J. Seligman, supra note 261, at 4477-78.
lishing secondary liability.282 In Rochez Bros. v. Rhoades,283 the Third Circuit held that in determining the scope of the applicability of agency principles under the Exchange Act it is helpful to evaluate the legislative history of the Act itself and, specifically, section 20(a). 284 The Rochez court noted that the legislative history of section 20(a) indicated that “Congress intended liability to be based on something besides control. That something is culpable participation.”285 The court noted that the use of agency doctrines, such as respondeat superior, would not advance that legislative purpose and would undermine congressional intent by emasculating section 20(a).286 Furthermore, the court stated that the use of respondeat superior would, in essence, impose a duty on a corporation to supervise its employees or to face primary liability, a standard that the court believed Congress did not intend to impose on corporations.287

Irrespective of Central Bank, the reasoning of the decisions supporting the non-exclusivity of section 20(a) have failed to recognize the intended purpose and importance of that provision. They have generally reasoned that Congress intended to expand the common law, and this could only occur if respondeat superior and section 20(a) were available in a complementary statutory scheme.288 However, these arguments are misplaced.289

The pre-Central Bank majority view was based on the premise that the 73rd Congress intended that common law secondary liability claims could be brought under the Exchange Act, but a section other than 20(a). But the problem is there was no such suitable provision under the Exchange Act and Congress did not intend for there to be one.290 An analysis of section 20(a) is unlike addressing implied

282. Id. at 884-86. Some writers argue that the Third Circuit's view now resembles the majority view in light of Sharp v. Cooper's & Lyband, 649 F.2d 175 (3d Cir. 1982). See J. Christopher York, Vicarious Liability of Controlling Persons: Respondeat Superior and the Securities Acts, 42 Emory L.J. 313, 318 (1993). Nevertheless, the Rochez decision was one of the last supporters of the exclusivity argument.

283. 527 F.2d 880 (3d Cir. 1975).

284. Id. at 884. In addressing the viability of agency-based secondary liability claims under section 10(b), the Rochez court, unlike the Central Bank Court, recognized the need to analyze section 20(a).

285. Id. at 884-85.


288. See, e.g., Hollinger v. Titan Capital Corp., 914 F.2d 1564, 1577 (9th Cir. 1990); Marbury Management, Inc. v. Kohn, 629 F.2d 705, 716 (2d Cir. 1980).


290. When the Exchange Act was first introduced, there were only four provisions that even addressed civil liability: (1) section 9(e), then section 8, provides civil liability for those who “willfully participate” in price manipulation of securities; (2)
rights of action under section 10(b), where Congress had not provided guidance for how to treat wrongdoers. The 73rd Congress expressed its intent on how to treat secondary liability when it enacted section 20(a).\(^{291}\) In fact, section 20(a) is the only provision in the Exchange Act as originally introduced and enacted that even addressed secondary liability.\(^{292}\)

What the majority of courts and commentators essentially argued was that Congress intended section 20(a)'s control person liability to supplement secondary liability claims available under section 10(b).\(^ {293}\) Congress, however, did not provide for any civil liability under section 10(b); such a cause of action was judicially created. Thus, there was never a need to imply a secondary liability cause of action under section 10(b) when Congress had expressed its intent through section 20(a).

In addition, the pre-Central Bank majority is incorrect in holding that the legislative history of sections 15 and 20(a) "do not reflect any congressional intent to restrict secondary liability for violations of the [A]cts to the controlled persons formula...."\(^ {294}\) As originally enacted, the Securities Act, section 15, did not have a good faith defense.\(^ {295}\) When section 15 was amended a year later to include the good faith defense, Senator Fletcher, a drafter of the Acts, explained:

> The purpose of this amendment is to restrict the scope of the section so as more accurately to carry out its real purpose. The mere existence of control is not made a basis for liability unless that control is effectively exercised to bring about the action upon which liability is based.\(^ {296}\)

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\(^{291}\) See Sager, supra note 103, at 822; Nancy C. Staudt, Controlling Securities Fraud: Proposed Liability Standards for Controlling Persons Under the 1933 and 1934 Securities Acts, 72 MINN. L. REV. 930 (1988)(In addition to establishing primary liability, Congress established secondary liability through section 15 and section 20(a)).

\(^{292}\) See supra note 289.

\(^{293}\) See supra note 277.

\(^{294}\) Paul F. Newton & Co. v. Texas Commerce Bank, 630 F.2d 1111, 1118 (5th Cir. 1980).


\(^{296}\) 78 CONG. REC. 8185 (1934); 78 CONG. REC. 10,265 (1934).
Since section 20(a) was based upon section 15, Congress concluded that liability was not to be based merely on the relationship of the defendants, as it is with respondeat superior, but on culpability.

The argument that section 28 negates any theory of exclusivity under section 20(a) is equally misplaced. The legislative history of section 28 does not support the majority view that a plaintiff can substitute section 20(a)'s prescriptions with more favorable common law secondary liability principles. Congressional committees reviewing the proposed statute explained that section 28 (then section 27) "reserves the rights and remedies existing outside of those provided in the act. . . ."

Early committee statements demonstrate that Congress, by enacting section 28, recognized that the Exchange Act was not preempting then existing state or common law remedies. The statements by members of Congress and the questions raised by various interested parties concerning section 28 do not suggest that an injured party could replace remedies under the Exchange Act with remedies available under common law, for example, using a respondeat superior claim under section 10(b) instead of section 20(a). The concerns relating to section 28 addressed during the congressional hearings do not support using common law remedies as the Act's remedies, but merely relate to whether the statute would preempt state laws or the self-regulatory authority of the stock exchanges.

297. Paul F. Newton & Co. v. Texas Commerce Bank, 630 F.2d 1111, 1115-16 (5th Cir. 1980)(citing hearings on S. Res. 84 (72d Cong.) and S. Res 56 and 97 (73d Cong.) before the Senate Comm. on Banking and Currency, 73d Cong., 1st Sess. pt. 15, at 6571 (1934)).

298. H.R. Rep. No. 1838 73d Cong., 2nd Sess. 42 (1934)("The mere existence of control is made a basis for liability if it is shown that the controlling person had no knowledge of or reasonable ground to believe in the existence of the facts upon which the liability of the controlled person is alleged to be based.") See also Marbury Management Inc., v. Kohn, 629 F.2d 705, 715-16 (2d Cir. 1980)(a plaintiff must show the controlling person was "in some meaningful sense [a] culpable participant [ ] in the fraud perpetrated by [the] controlled person[ ]").

299. An eloquent argument supporting this point is addressed in Fitzpatrick and Carmen's article on section 20(a). See generally Fitzpatrick & Carmen, supra note 132.

300. 78 CONG. REC. 7709 (1934)(emphasis added).

301. 78 CONG. REC. 2270 (1934); 78 CONG. REC. 7709 (1934).

302. See also Fitzpatrick & Carmen, supra note 132, at 24.

303. One commentator expressed the concern: "it appears that the authority of the respective states to regulate brokers engaged in business therein would be practically emasculated." Hearing before the Committee on Interstate and Foreign Commerce House of Representatives, 73d Cong., 2d Sess. 22 on H.R. 7852 (March 8, 1934 Hearings of House Committee on Interstate and Foreign Commerce)(statements by Adolph Johnson, chief counsel to the Public Service Commissioner of Wisconsin). Other commentators during the hearing process also expressed a belief that section 28(a) was meant to supersede state law. Id. (March 6, 1934 Hearings of House Committee on Interstate And Foreign Com-
IX. SECTION 20(a)'s INTENDED COVERAGE

While the majority of authority analyzing section 20(a) limits the provision's control person language to a form of agency-based liability, section 20(a) is broad enough and was likely intended to address a broader range of activity that comes within the traditional rubric of secondary liability. When Senator Fletcher first introduced a bill entitled "The National Securities Exchange Act of 1934," the bill contained a control person section that was broad enough to cover liability based upon respondeat superior, conspiracy, and aiding and abetting principles. Specifically, section 20(a), then numbered section 19, provided liability for "every person who... [controls any person] pursuant to or in connection with any agreement or understanding with one or more other persons by or through stock ownership, agency or otherwise. ..." 

The congressional debate during the relevant period demonstrates that section 20(a) was to be broadly construed, covering culpable persons who were not active wrongdoers but because of their "behind the scenes" participation were liable under principles of secondary liability. Section 20(a)'s legislative history indicates that Congress purposefully refused to define a "control person":

304. See, e.g., Burns, supra note 133, at 1185 ("The conflict between agency principles and the controlling person provisions arises from subtle differences in their method of application."); Staudt, supra note 291, at 934 ("Section 15 of the 1933 Act and section 20(a) of the 1934 Act establish liability similar in nature to the common law doctrine of respondeat superior."). See also Fey v. Walston & Co., Inc., 493 F.2d 1036, 1051 (7th Cir. 1974) (in view of the extension of the general respondeat superior doctrine by section 20(a), courts have tended to emphasize the control aspects of vicarious liabilities in the securities context.).

305. Ruder, supra note 16, at 602 ("The broad approach taken toward the definition of the term control person might suggest that the number of persons falling into the "control" category would be rather large.").

306. 78 CONG. REC. 2264-72 (1934).

307. Id. at 2269 (emphasis added).

308. Section 19's purpose was to prevent evasion of the provisions of that section by organizing dummies who will undertake the actual things forbidden by the section. Stock Exchange Practices: Hearings on S. Res. 84 (72d Cong.) and S. Res. 96 and S. Res. 97 (73d Cong.) Before the Senate Committee on Banking and Currency, 73d Cong., 1st Sess. 6571 (1934) (statement of Thomas Gardiner Corcoran, Office of Counsel for Reconstruction Finance Corp.). See also 78 CONG. REC. 8094-95 (1934).

309. 78 CONG. REC. 8094-95 (1934).
When reference is made to "control," the term is intended to include actual control as well as what has been called legally enforceable control. [citations omitted]. It was thought undesirable to attempt to define the term. It would be difficult if not impossible to enumerate or to anticipate the many ways in which actual control may be exerted. A few examples of the methods used are stock ownership, lease, contract, and agency.310

Notwithstanding recent decisions limiting Section 20(a) liability to respondent superior type claims, the enacting Congress expressly rejected limiting section 20(a) liability to agency-based liability. On May 4, 1934, Representative Hollister, in an attempt to do away with the ambiguous "control person" language, introduced an amendment to strike section 20(a), then section 19. While other commentators have made reference to the Hollister-Lea debate,311 a review of this significant discourse in greater depth is necessary in order to appreciate Congress' intended scope for section 20(a):

Mr. Hollister:

If there is any Member of this House who would like to stand up and define to me what a controlling person is, I should like to know... what an agent is; we know that if you perform something through an agent you perform it yourself. The term "agent" has a reasonable and well known legal meaning, but I should like to have someone tell me in what law, in what decisions, or in what textbooks I can be told what a controlling person is. I say that such a provision in no sense belongs in this law.

... Let me repeat that my amendment is merely an attempt to protect against the strike suit and takes out of the bill nothing which in any way is involved in the so-called "teeth" of the bill. It is a protection for the average man who should be able to be assured that he will not have to defend himself from suit when, as a matter of fact, he is not culpable....

Mr. Lea:

The object of this provision is to catch the man who stands behind the scenes and controls the man who is in a nominal position of authority. The man in control is just as well known as a dummy on a directorate....

Mr. Hollister:

Would not an ordinary agency provision cover that? A man is either an agent or he is not an agent.

Mr. Lea:

There would be no contractual relation, necessarily. It is just the same position as in the control of a dummy on a directorate. The man who stands behind the scenes and dominates the dummy ought to be responsible because he is the real party in interest.

Mr. Hollister:

The gentleman means that no matter how honest the man nominating the director may have been in making the nomination, if the director does something unlawful and unknown to the man nominating him, the latter should be held responsible?

311. Burns, supra note 133, at 1204-05. See also Staudt, supra note 291, at 933.
Mr. Lea:
The man charged with control is only responsible to the extent he did control the action complained of, and his actual control must be established.

Mr. Hollister:
What would constitute such control? Can the gentleman define to me any legal way a man can decide whether he has such control? . . .

Mr. Lea:
It is a question of fact to be determined by the issues presented in the case. . . .

Mr. Hollister:
I know there is the test of agency, and I know of no other test which would make a person responsible criminally. . . .

Mr. Lea:
It is simply a question of putting the responsibility on the man who is really responsible. . . .

It is a question of proving the case in court on the basis of the facts to show that one man did control the other in doing a wrongful thing, and until you have done that there is no punishment or penalty.

Mr. Hollister:
Here you are creating a new kind of unlawful act which is contrary to all accepted principles of jurisprudence.

Mr. Lea:
I think the gentleman is mistaken in stating it is a new kind of responsibility.

If he will refer to the definitions of the word "control," as established by the courts as set forth in Words and Phrases,312 he will find the term is well known and its meaning has been long established.313

Representative Hollister's amendment to strike out section 20(a) was rejected by a vote of 56 to 30,314 which illustrates that the 73rd Congress intended Section 20(a) to be based upon culpable participation and did not intend section 20(a) to merely address agency forms of liability.315

Likewise, the various versions of Section 20(a) support an expansive reading of the section. When the Exchange Act was proposed, section 20(a) provided for liability for "every person who, by or through stock ownership, agency, or otherwise, or who pursuant to or in connection with any agreement or understanding with one or more other persons by or through stock ownership, agency, or otherwise, controls any

313. 78 Cong. Rec. 8094-95 (1934).
314. 78 Cong. Rec. 8095 (1934).
315. While the Hollister-Lea debate and the Senate's ensuing vote provides significant insight into the 73d Congress' understanding of section 20(a)'s control person language, the form of new textualism advocated by those such as Justices Scalia and Kennedy, in all probability, would not seek guidance from this valuable legislative evidence. This is a reason in and of itself to reject textualism.
person liable under any provision of this Act."316 This language was initially adopted by both the House of Representative's and the Senate's versions of the bill.317 Eventually, the "through stock ownership" language of the provision was replaced with anyone who "directly or indirectly" controls a violator.318 A House of Representatives Committee explained that the Senate amendment did not contain the language "alone or pursuant to or in connection with any agreement or understanding" because it was considered mere "surplusage."319

Additionally, federal courts have construed the term "control" broadly, "imposing few limitations" on the categories of persons who may meet the standard.320 In general, the courts have only required that the controlling person possess some indirect means of discipline or have influence over the controlled person.321 Since Congress construed section 20(a) broadly, enabling it to address not only agency-based liability but other forms of secondary liability against those who acted "behind the scenes,"322 defendants who enter into a conspiracy or aid and abet a violation should be liable under section 20(a), provided that they possessed some means of discipline or influence over the controlled person. Several federal decisions support this broad reading of section 20(a).323 These decisions recognized section 20(a)

317. H.R. 7852 as introduced by Congressman Rayburn and referred to the House Interstate and Foreign Commerce Committee, February 10, 1934, S. 2693 as introduced by Senator Fletcher and referred to the Senate Banking and Currency Committee, February 9, 1934. 78 CONG. REC. 2378 (1934)(House version); 78 CONG. REC. 2204-70 (1934)(Senate version).
319. 78 CONG. REC. 10263 (1934).
322. The legislative history also evinces that "control persons" act not only in complicity with an active wrongdoer, but are the persons who directed the scheme to defraud, which demonstrates that Congress intended secondary liability based upon culpability. 78 CONG. REC. 8095 (1934).
323. Richardson v. MacAurthur, 451 F.2d 35, 41-42 (10th Cir. 1971)(section 20(a) not restricted by principles of agency or conspiracy). See also First Interstate Bank of Denver v. Pring, 969 F.2d 891, 896 (10th Cir. 1992)(section 20(a) is to be construed liberally); In re Clearly Canadian Sec. Litig., 875 F. Supp. 1410, 1420 (N.D. Cal. 1995)(complaint contained sufficient allegations of a conspiracy to support section 20(a) claim); Hershack v. Fiasck, [1992-1993 Transfer Binder] Fed.
claims based upon aider and abettor liability as well as liability based upon conspiracy.324 Specifically, the decisions noted that section 20(a) was not to be restricted by principles of agency.325 Thus, both the legislative history of section 20(a) and section 28, along with several federal decisions on point, support the view that section 20(a) was not only the exclusive means for addressing secondary liability under the Exchange Act, but was also intended to address a variety of forms of secondary liability. Accordingly, there was no reason for courts to use section 10(b) to address secondary liability claims, other than to support plaintiffs' lawyers' savvy avoidance of section 20(a)'s good faith defenses.326

X. OTHER IMPLICATIONS OF THE DECISION: EQUALLY TROUBLING STATUTORY REFORM

The Private Securities Litigation Reform Act of 1995 ("Reform Act") was enacted on December 22, 1995, when the Senate overrode President Clinton's veto of the bill. The intent of the Reform Act was to combat perceived abuses in the securities litigation process.327 The Reform Act, among other things, establishes presumptions and procedures for determining plaintiffs' counsel and class representatives in class action securities suits, provides more stringent pleading requirements for fraud, supports sanctions if claims are unsupported, and generally limits liability proportionate to responsibility.328 In response to the Central Bank decision, the Reform Act expressly grants to the Securities Exchange Commission ("SEC") the right to seek injunctions or sue for money damages against persons who aid


326. See Fischel, supra note 105, at 86-87.

327. See House Conference Report, H. Rep. No. 369, 104th Cong., 1st Sess. 31-32, reprinted in 1995 U.S. CODE CONG. & ADMN. NEWS at 730 ("The private securities litigation system is too important to the integrity of American capital markets to allow this system to be undermined by those who seek to line their pockets by bringing abusive and meritless suits.").

328. Congress overrides President's Veto of Securities Reform Measure, Fed. Sec. L. Rep. (CCH) No. 1694, at 1-3 (Dec. 27, 1995); Fallone, supra note 70.
and abet primary violations of the securities laws.329 The Reform Act, however, does not overrule that portion of the Central Bank decision concerning implied civil rights of action for aiding and abetting under section 10(b).330 A Senate Committee Report noted that overruling Central Bank's holding with respect to private litigants would be contrary to the Reform Act's goal of reducing meritless securities litigation.331 With this summary statement, the current Congress appears to adopt the view that secondary liability facilitates meritless litigation.

Interestingly, the Reform Act provides the SEC the right to sue aiders and abetters by amending section 20 of the Exchange Act.332 Congress thus followed the Central Bank Court's approach of limiting the issue to aider and abettor liability under section 10(b). While Congress amended section 20 and, therefore, overruled Central Bank in part, Congress, by refusing to look at the 73rd Congress' intent in passing section 20(a), utterly failed to recognize that private litigants and the SEC, even after Central Bank, should have had the right to redress against aiders and abetters under the Exchange Act's secondary liability section—section 20(a). By amending section 20 to empower the SEC to bring aider and abetter claims, Congress suggests that aider and abettor liability claims were not available under the Exchange Act as a result of Central Bank. If the SEC previously had such a right under section 20(a),333 section 20 did not have to be amended. As demonstrated in the previous section, Congress' amendment of section 20 is inconsistent with the 73rd Congress' intended scope of coverage of section 20(a) and judicial application of that section.

XI. BENEFITS OF RECOGNIZING THE APPROPRIATE ROLE OF SECTION 20(a)

There are several reasons for supporting the revival of section 20(a)'s control person liability, all of which essentially relate to following the 73rd Congress' intent. In general, this approach diminishes the impact of the current Court's inclination to substitute Congress' intent through the use of textualism. Specifically, the recognition of section 20(a)'s role will avoid the thorny issues a court is faced with.

330. Id.
when addressing implied rights of action, for example, Affiliated Ute\textsuperscript{334} versus Central Bank.\textsuperscript{335} In addition, when Congress legislates and explicitly expresses its intent, courts should take heed and follow Congress' view. This is especially so in the case of secondary liability where Congress had expressed through section 20(a) how secondary liability should be addressed under the Exchange Act. Courts should not be swayed by efforts that circumvent defenses provided by a statute, for example, the use of section 10(b) to avoid section 20(a)'s good faith defenses.

Further, when Congress enacted the Exchange Act, culpability was an essential prerequisite for liability.\textsuperscript{336} Section 20(a)'s language recognizes this and avoids the troubling effect caused when agency-based liability arises under section 10(b).\textsuperscript{337} Securities cases often involve the wrongdoing of only a small number of an issuer's officers, employees, or both. The fraud committed by these wrongdoers usually is committed for their own personal benefit and not for the benefit of the issuer. While the issuer may receive some incidental benefit, such as an increase in the price of its stock, if the wrongdoing was not a part of the corporate culture or was accomplished as a result of the influence exerted by the issuer, then innocent shareholders eventually compensate other innocent shareholders and their lawyers for the wrongs of those who should be accountable but often are not because they are judgment-proof.

Indeed, Judge Friendly, in SEC v. Texas Gulf Sulfur Co.,\textsuperscript{338} expressed this concern, noting that unduly expansive imposition of civil liability "will lead to large judgments, payable in the last analysis by innocent investors, for the benefit of speculators and their lawyers. . . ."\textsuperscript{339} Another scholar has noted one source of perplexity as to the appropriate bounds of the civil remedy for misleading filings is that any remedy imposed against the issuer itself is indirectly im-

\textsuperscript{336.} See 78 Cong. Rec. 8094-95 (1934). In addition, the majority of federal courts addressing the requisite intent for liability under section 20(a) have held that a control person must have some level of culpability. See, e.g., Hunt v. Miller, 908 F.2d 1210, 1215 (4th Cir. 1990); Orloff v. Allman, 819 F.2d 904, 907 (9th Cir. 1987); Durham v. Kelly, 810 F.2d 1500, 1504 (9th Cir. 1987); Buhler v. Audio Leasing Corp., 807 F.2d 833, 835-36 (9th Cir. 1987); Kersh v. General Council of Assemblies of God, 804 F.2d 546, 549 (9th Cir. 1986); Rochez Bros., Inc. v. Rhoades, 527 F.2d 880, 885, 888-89 (3d Cir. 1975); Lanza v. Drexel & Co., 479 F.2d 1277, 1299 (2d Cir. 1973); Kamen & Co. v. Paul H. Aschkar & Co., 382 F.2d 689, 697 (9th Cir. 1967).
\textsuperscript{337.} Rochez Bros., Inc. v. Rhoades, 527 F.2d 880, 884 (3d Cir. 1975).
\textsuperscript{338.} 401 F.2d 833 (2d Cir. 1968), cert. denied sub nom., Coates v. SEC, 394 U.S. 976 (1967).
\textsuperscript{339.} Id. at 867 (Friendly, J. concurring). See also Michael M. Boone & Patrick F. McGowan, Standing to Sue Under SEC Rule 10b-5, 49 Tex. L. Rev. 617 (1971).
posed on all holders of the common stock, which is usually the most important segment of the total category of investors intended to be protected.340 While the use of respondeat superior imposes liability on the issuer irrespective of culpability, section 20(a), on the other hand, follows Congress' intent that liability be based on culpability341 and allows the issuer to raise good faith defenses, which could lead to more equitable results.

XII. CONCLUSION

The Supreme Court's adoption of a textualist theory of statutory interpretation in the securities field evolved from a questionable application of precedent and the rejection of the stated legislative purpose of the securities laws. As evidenced by the Central Bank decision, the Court's application of textualism has resulted in a violation of the very tenets of textualism—replacing the legislature's values with those of the judiciary. As such, the decision illustrates the ease with which textualism can allow an exceedingly narrow approach to interpreting a statute and textualism's failure to acknowledge the role of interpretative tools, such as other statutory provisions or legislative history. The decision thus represents the Court's latest effort at usurping and distorting the 73rd Congress' intent concerning the civil remedies available under the Exchange Act. With the Central Bank decision, the Supreme Court not only legislated but also created an opinion that will necessitate several more decisions to clarify its holding. Had the Court respected, instead of rejected, legislative history, the Court would have resolved the conflict concerning the appropriate role of secondary liability under the securities laws. The Court, however, failed to follow the enacting Congress' intent and failed to recognize the importance of the Exchange Act's section 20(a), the provision whereby the Court should have begun its analysis.