Supreme Court of the United States
Washington, D.C.

CHAMBERS OF
JUSTICE FELIX FRANKFURTER

January 29, 1943

Re: No. 254 – the Chenery case

Dear Stanley:

Were I still at Cambridge I would be saddened to note that you underwrote an opinion like Black's dissent in the Chenery case. I don't think I should be less saddened because I am your colleague. I hate to see you "bogged down in the quagmire" of Populist rhetoric unrelated to fact. And so I should like to have you ask yourself a few questions.

Of course a fiduciary must not profit because of his position. That is an incontestable proposition. But that is the beginning and not the end of the inquiry in this case. Where is there any finding by the Commission of any profit because these respondents took advantage of their position? The Commission's findings are precisely the opposite – there was no dishonesty, there was no lack of full disclosure, there was no purchase at a unfair price. To be sure, a technical trustee is not allowed to deal with the trust property even though there is no finding of over-reaching or purchase at an unfair price. But that is so – that is a rule of law – because a trustee has no interest, no property interest, in the res. His complete interest in the res is to take care of it for another. And therefore the law summarizing human experience says in effect that we can't look into every situation to find out whether the trustee as a purchaser charged himself a fair price, and so we shall forbid self-purchase altogether. But stockholders who are also directors do have a pecuniary interest in their holdings and the right, as part of such pecuniary interest, to protect their holdings. The problem of the law therefore is a wholly different one from that pertaining to a conventional trustee – the problem is, in what manner and to what extent can a

stockholder-officer protect his interest. He cannot act on inside information he cannot act coercively by virtue of his position, etc., etc.

Now to be sure the Securities and Exchange Commission can, on the basis of its experience, establish a new rule of conduct. It can say "This business of ascertaining whether officers have acted on inside knowledge is subtle business, as a matter of evidence, and too many wrongs would slip through the net if we had to establish it in every case. And so we make a general rule that reorganization managers cannot change their holdings or extend their holdings while the reorganization is in process." I could understand such a general rule and I certainly would think the Commission is entitled to promulgate. It was in this connection that I referred to Judge Learned Hand's admirable opinion in the Morgan, Stanley & Co. case, 126 F 2d, 325, 332. But the decisive point is that the Commission made no such rule.

It made no such general rule and applied it to this case. It made the purest kind of an ad hoc decision without any reason whatever for its conclusion except that the respondents were reorganization managers. But that brings us back to the question: and so what? – considering the fact that the Commission not only finds no misuse of their position through use of inside information or any other form of unfairness but finds the opposite.

If someone were to say "Frankfurter is a bad judge", it would be merely an expression of judgment even though a very weighty judgment if uttered, say, by someone who presumably knows about such matters, like Chief Justice Hughes. But if such a judgment has to be reviewed by a superior authority, there would be no basis for reviewing the finding that "Frankfurter is a bad judge" if no reason whatever were given why he is a bad judge. To be sure, if it were said "Experience shows that a man who has been a professor for twenty-five years acquires a doctrinaire attitude toward law, whereas adjudication is the exercise of a creative art, based

partly on learning but perhaps even more on the wise use to which learning is put, and therefore we find that Frankfurter is a bad judge", you would have the ultimate finding of "badness" supported as an application of a general rule of experience to a particular case.

The trouble is the Commission did not enunciate a general rule of conduct which takes care of this particular case nor did it support this particular case on any set of circumstances which show that this particular case is to be condemned. It is pure fiat in there is such a thing as fiat, amounting to no more than to say that these respondents were "fiduciaries" – therefore what they did is wrong, although "fiduciary" is not a defined, distinctive status but a term equally applicable to a variety of relationships to the conduct of enterprise, with the greatest diversity of duties, responsibilities, and opportunities. To say "These officers are fiduciaries, therefore what they did is wrong, although there is neither a rule of conduct generally laid down by the Commission nor a reflection by the Commission of rules of conduct heretofore established by any other organ of the law, authorized to establish rules of conduct", affords no possible basis for a reviewing court to say that that which the Commission did was right. And so the case must be remanded to the Commission unless court review simply means rubber stamping what the Commission does.

Burke somewhere said, in effect, "I cannot think of English law without reason opinions setting forth the reasons for the law that is pronounced". Administrative agencies have two major functions. They exercise delegated legislation through their rule-making power, that is, they formulate general standards of conduct based on their experience and their expertness. The broadest leeway should be given to them in the exercise of this legislative function. Secondly, they exercise an adjudicatory function in disposing of specific controversies that come before them, much as courts would do if the jurisdictions in these matters were given to them. The

Chenery case is such an exercise of the administrative adjudicatory process. And it is subject, therefore, to the requirement that the reviewing courts be enabled to know the basis of the determination of the administrative in order to discharge the court's function of review. I have spent most of my professional life in trying to get recognition for the indispensability of the administrative process. I do not want slipshodness and, still worse, lust for power lead to curtailment of these administrative powers by determinations without reason or by appeals to rules of law for which there is no warrant.

In this case, if what these managers did transgresses any standard of ethical behavior, let the Commission so find. It has found the contrary. If the Commission thinks that a general rule is called for which may outlaw even innocent conduct in a particular case, let the Commission make such a rule on its good conscience that experience calls for such a rule. But let it not make a determination in a particular case disapproving of an action which no court of equity would strike down and for which it gives no other reason than a misconception of what a court of equity would do in the circumstances.

Ever yours,

F.F.

Mr. Justice Reed