SUPREME COURT OF THE UNITED STATES

No. 78–1202

Vincent F. Chiarella, Petitioner, v. United States. | On Writ of Certiorari to the United States Court of Appeals for the Second Circuit.

[March 18, 1980]

MR. JUSTICE BRENNAN, concurring in the judgment.

The Court holds, correctly in my view, that "a duty to disclose under § 10 (b) does not arise from the mere possession of nonpublic market information." *Ante,* at 12. Prior to so holding, however, it suggests that no violation of § 10 (b) could be made out absent a breach of some duty arising out of a fiduciary relationship between buyer and seller. I cannot subscribe to that suggestion. On the contrary, it seems to me that Part I of THE CHIEF JUSTICE's dissent, *post,* at 1–4, correctly states the applicable substantive law—a person violates § 10 (b) whenever he improperly obtains or converts to his own benefit nonpublic information which he then uses in connection with the purchase or sale of securities.

While I agree with Part I of THE CHIEF JUSTICE's dissent, I am unable to agree with Part II. Rather, I concur in the judgment of the majority because I think it clear that the legal theory sketched by THE CHIEF JUSTICE is not the one presented to the jury. As I read them, the instructions in effect permitted the jurors to return a verdict of guilty merely upon a finding of failure to disclose material nonpublic information in connection with the purchase of stock. I can find no instruction suggesting that one element of the offense was the improper conversion or misappropriation of that nonpublic information. Ambiguous suggestions in the indictment and the prosecutor's opening and closing remarks are no substitute for the proper instructions. And neither reference

to the harmless error doctrine nor some *post hoc* theory of constructive stipulation can cure the defect. The simple fact is that to affirm the conviction without an adequate instruction would be tantamount to directing a verdict of guilty, and that we plainly may not do.

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MR. CHIEF JUSTICE BURGER, dissenting.

I believe that the jury instructions in this case properly charged a violation of § 10b and Rule 10b–5, and I would affirm the conviction.

I

As a general rule, neither party to an arm's length business transaction has an obligation to disclose information to the other unless the parties stand in some confidential or fiduciary relation. See Prosser, The Law of Torts § 106. This rule permits a businessman to capitalize on his experience and skill in securing and evaluating relevant information; it provides incentive for hard work, careful analysis, and astute forecasting. But the policies that underlie the rule also should limit its scope. In particular, the rule should give way when an informational advantage is obtained, not by superior experience, foresight, or industry, but by some unlawful means. One commentator has written:

> "[T]he way in which the buyer acquires the information which he conceals from the vendor should be a material circumstance. The information might have been acquired as the result of his bringing to bear a superior knowledge, intelligence, skill or technical judgment; it might have been acquired by chance; or it might be acquired by means of some tortious action on his part. . . . *Any time information is acquired by an illegal act it would*

seem that there should be a duty to disclose that information." Keeton, Fraud—Concealment and Non-Disclosure, 15 Tex. L. Rev. 1, 25–26 (1936) (emphasis added).

I would read § 10b and Rule 10b–5 to encompass and build on this principle: to mean that a person who has misappropriated nonpublic information has an absolute duty to disclose that information or to refrain from trading.

The language of § 10b and of Rule 10b–5 plainly support such a reading. By their terms, these provisions reach *any* person engaged in *any* fraudulent scheme. This broad language negates the suggestion that congressional concern was limited to trading by "corporate insiders" or to deceptive practices related to "corporate information." [1] Just as surely Congress cannot have intended one standard of fair dealing for "white collar" insiders and another for the "blue collar" level. The very language of § 10b and Rule 10b–5 "by repeated use of the word 'any' [was] obviously meant to be inclusive." *Affiliated Ute Citizens* v. *United States*, 406 U. S. 128, 151 (1972).

The history of the statute and of the rule also support this reading. The antifraud provisions were designed in large measure "to assure that dealing in securities is fair and without undue preferences or advantages among investors." H. R. Conf. Rep. No. 94–229, 94th Cong., 1st Sess., 91–92 (1975). These provisions prohibit "those manipulative and deceptive practices which have been demonstrated to fulfill no useful

[1] Academic writing in recent years has distinguished between "corporate information"—information which comes from within the corporation and reflects on expected earnings or assets—and "market information." See, *e. g.*, Fleischer, Mundheim, & Murphy, An Initial Inquiry into the Responsibility to Disclose Market Information, 121 U. Pa. L. Rev. 798, 799 (1973). It is clear that the § 10b and Rule 10b–5 by their terms and by their history make no such distinction. See Brudney, Insiders, Outsiders, and Informational Advantages Under the Federal Securities Laws, 93 Harv. L. Rev. 322, 329–333 (1979).

function." S. Rep. No. 792, 73d Cong., 2d Sess., 6 (1934). An investor who purchases securities on the basis of misappropriated nonpublic information possesses just such an "undue" trading advantage; his conduct quite clearly serves no useful function except his own enrichment at the expense of others.

This interpretation of § 10b and Rule 10b–5 is in no sense novel. It follows naturally from legal principles enunciated by the Securities and Exchange Commission in its seminal *Cady, Roberts* decision. 40 S. E. C. 907 (1961). There, the Commission relied upon two factors to impose a duty to disclose on corporate insiders: (1) " . . . access to information . . . intended to be available only for a corporate purpose *and not for the personal benefit of anyone*" (emphasis added); and (2) the unfairness inherent in trading on such information when it is inaccessible to those with whom one is dealing. Both of these factors are present whenever a party gains an informational advantage by unlawful means.[2] Indeed, in *In re Blyth & Co.*, 43 S. E. C. 1037 (1969), the Commission applied its *Cady, Roberts* decision in just such a context. In that case a broker dealer had traded in Government securities on the basis of confidential Treasury Department information which it received from a Federal Reserve Bank employee. The Commission ruled that the trading was "improper use of inside information" violative of § 10b and Rule 10b–5. *Id.*, at 1040. It did not hesitate to extend *Cady, Roberts* to reach a "tippee" of a Government insider.[3]

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[2] See Financial Analysts Rec., Oct. 7, 1968, at 3, 5 (interview with SEC Commissioner Philip A. Loomis, Jr.) (the essential characteristic of insider information is that it is "received in confidence for a purpose other than to use it for the person's own advantage and to the disadvantage of the investing public in the market"). See also Note, The Government Insider and Rule 10b–5, 47 S. Cal. L. Rev. 1491, 1498–1502 (1974).

[3] This interpretation of the antifraud provisions also finds support in the recently proposed Federal Securities Code prepared by the American Law Institute under the direction of Professor Louis Loss. The ALI

Finally, it bears emphasis that this reading of § 10b and Rule 10b–5 would not threaten legitimate business practices. So read, the antifraud provisions would not impose a duty on a tender offeror to disclose its acquisition plans during the period in which it "tests the water" prior to purchasing a full 5% of the target company's stock. Nor would it proscribe "warehousing." See generally 4 SEC, Institutional Investor Study Report, H. R. Doc. 92–64, 92d Cong., 1st Sess., 2273 (1971). Likewise, market specialists would not be subject to a disclose-or-refrain requirement in the performance of their everyday market functions. In each of these instances, trading is accomplished on the basis of material nonpublic information, but the information has not been unlawfully converted for personal gain.

II

The Court's opinion, as I read it, leaves open the question whether § 10b and Rule 10b–5 prohibit trading on misappropriated nonpublic information.[4] Instead, the Court apparently concludes that this theory of the case was not submitted to the jury. In the Court's view, the instructions given the jury were premised on the erroneous notion that the mere

code would construe the antifraud provisions to cover a class of "quasi-insiders," including a judge's law clerk who trades on information in an unpublished opinion or a Government employee who trades on a secret report. See ALI Federal Securities Code § 1603, comment 3 (d), at 538–539. These quasi-insiders share the characteristic that their informational advantage is obtained by conversion and not by legitimate economic activity that society seeks to encourage.

[4] There is some language in the Court's opinion to suggest that only "a relationship between petitioner and the sellers . . . could give rise to a duty [to disclose]." *Ante*, at 9. The Court's holding, however, is much more limited, namely that mere possession of material nonpublic information is insufficient to create a duty to disclose or to refrain from trading. *Ante*, at 12. Accordingly, it is my understanding that the Court has not rejected the view, advanced above, that an absolute duty to disclose or refrain arises from the very act of misappropriating nonpublic information.

failure to disclose nonpublic information, however acquired, is a deceptive practice. And because of this premise, the jury was not instructed that the means by which Chiarella acquired his informational advantage—by violating a duty owed to the acquiring companies—was an element of the offense. See *ante*, at 13.

The Court's reading of the District Court's charge is unduly restrictive. Fairly read as a whole and in the context of the trial, the instructions required the jury to find that Chiarella obtained his trading advantage by misappropriating the property of his employer's customers. The jury was charged that "[i]n simple terms, the charge is that Chiarella wrongfully took advantage of information he acquired *in the course of his confidential position at Pandick Press* and secretly used that information when he knew other people trading in the securities market did not have access to the same information that he had at a time when he knew that information was material to the value of the stock." Record, at 677 (emphasis added). The language parallels that in the indictment, and the jury had that indictment during its deliberations; it charged that Chiarella had traded "without disclosing material nonpublic information he had obtained in connection with his employment." It is underscored by the clarity which the prosecutor exhibited in his opening statement to the jury. No juror could possibly have failed to understand what the case was about after the prosecutor said: "In sum what the indictment charges is that Chiarella misused material non-public information for personal gain and that he took advantage of his position of trust with full knowledge that it was wrong. That is what the case is about. It is that simple." R. 46. (Emphasis added.) Moreover, experienced defense counsel took no exception and uttered no complaint that the instructions were inadequate in this regard.

In any event, even assuming the instructions were deficient in not charging misappropriation with sufficient precision, on this

record that error was harmless beyond a reasonable doubt. Here, Chiarella, himself, testified that he obtained his informational advantage by decoding confidential material entrusted to his employer by its customers. R. 474. He admitted that the information he traded on was "confidential," not "to be use[d] for personal gain." R. 496. In light of this testimony, it is simply inconceivable to me that any shortcoming in the instructions could have "possibly influenced the jury adversely to [the defendant]." *Chapman* v. *California*, 386 U. S. 18, 23 (1967). See also *United States* v. *Park*, 421 U. S. 658, 673–676. Even more telling perhaps is Chiarella's counsel's statement in closing argument:

> "Let me say right up front, too, Mr. Chiarella got on the stand and he conceded, he said candidly, 'I used clues I got while I was at work. I looked at these various documents and I deciphered them and I decoded them and I used that information as a basis for purchasing stock.' There is no question about that. We don't have to go through a hullabaloo about that. It is something he concedes. There is no mystery about that." R. 711.

In this Court, counsel similarly conceded that "[w]e do not dispute the proposition that Chiarella *violated his duty as an agent of the offeror corporations not to use their confidential information for personal profit.*" Reply Brief at 4 (emphasis added). See Restatement (Second) of Agency § 395 (1958). These statements are tantamount to a formal stipulation that Chiarella's informational advantage was unlawfully obtained. And it is established law that a stipulation related to an essential element of a crime must be regarded by the jury as a fact conclusively proved. See, 8 J. Wigmore, Evidence § 2590 (McNaughton rev. 1961); *United States* v. *Houston*, 547 F. 2d 104 (CA9 1976).

In sum, the evidence shows beyond all doubt that Chiarella, working literally in the shadows of the warning signs in the print shop, misappropriated—stole to put it bluntly—valuable

nonpublic information entrusted in him in the utmost confidence. He then exploited his ill-gotten informational advantage by purchasing securities in the market. In my view, such conduct plainly violates § 10b and Rule 10b–5. Accordingly, I would affirm the judgment of the Court of Appeals.