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## Central Bank v. First Interstate Bank: Not Just the End of Aiding and Abetting Under Section 10(b)

Carrie E. Goodwin

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# *Central Bank v. First Interstate Bank:* Not Just the End of Aiding and Abetting Under Section 10(b)

Carrie E. Goodwin\*

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### I. Introduction

In *Central Bank v. First Interstate Bank*,<sup>1</sup> the Supreme Court shocked the securities industry.<sup>2</sup> On its own motion, the Court questioned and then abolished the aiding and abetting cause of action for securities fraud under the Securities Exchange Act of 1934 (1934 Act).<sup>3</sup> The Court's holding overruled thirty years of lower court precedent.

Congress enacted the 1934 Act and the Securities Act of 1933 (1933 Act)<sup>4</sup> after the stock market crash of 1929. The 1933 Act is narrower in coverage than the 1934 Act, which reflected Congress's effort to regulate all aspects of securities trading.<sup>5</sup> Section 10(b) of the 1934 Act is a general antifraud provision that imposes civil liability on those who commit manipulative or deceptive acts in connection with the purchase or sale of securities.<sup>6</sup> For over thirty years, lower federal courts routinely allowed

1. 114 S. Ct. 1439 (1994).

2. See David S. Ruder, *The Future of Aiding and Abetting and Rule 10b-5 After Central Bank of Denver*, 49 BUS. LAW. 1479, 1479 (1994) (stating that Supreme Court's decision in *Central Bank* marked dramatic event in history of interpretation of Rule 10b-5); Joel Seligman, *The Implications of Central Bank*, 49 BUS. LAW. 1429, 1430 (1994) (touting *Central Bank* decision as most important federal securities decision in years). See generally *Chairman of SEC Vows to Protect Investors*, ST. LOUIS POST DISPATCH, July 23, 1994, at A7 (discussing testimony by SEC Chairmen in response to *Central Bank* decision); Sharon Walsh, *Congress, SEC Ponder Shareholder Lawsuits*, WASH. POST, May 11, 1994, at D1 (describing reaction by defendants' and plaintiffs' lawyers to *Central Bank* decision); Thom Weidlich, *Professionals Still at Risk: Plaintiffs' Bar Shifts Gears to Revise Claims in Central Bank's Wake*, NAT'L L.J., July 18, 1994, at A4 (discussing plaintiffs' bar's response to *Central Bank*).

3. Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78ll (1988 & Supp. V 1993).

4. Securities Act of 1933, 15 U.S.C. §§ 77a-77bbbb (1988 & Supp. V 1993).

5. See THOMAS L. HAZEN, *THE LAW OF SECURITIES REGULATION* § 1.2, at 7-8 (2d ed. 1990) (noting that 1933 Act covers only distributions of securities and that investor protection extends only to purchasers of securities, while 1934 Act regulates all aspects of public trading of securities).

6. See *infra* note 14 (providing text of Securities Exchange Act of 1934 § 10(b), 15

victims of manipulative or deceptive acts to recover not only against those who themselves violated Section 10(b), but also against those who aided and abetted the Section 10(b) violation.<sup>7</sup> Despite the history of the aiding and abetting cause of action, the Supreme Court in *Central Bank* concluded that aiding and abetting fell outside the text of Section 10(b). After *Central Bank*, therefore, courts can no longer allow Section 10(b) recovery for aiding and abetting a Section 10(b) violation.

*Central Bank* sends a clear message: While courts may sometimes imply a private cause of action to penalize conduct that Congress has *expressly proscribed*, courts may not imply a cause of action creating liability for conduct that Congress *has not expressly proscribed*. Thus, *Central Bank* not only abolished the private cause of action for aiding and abetting under Section 10(b); *Central Bank* also instituted a new methodology for evaluating all implied causes of action. For example, lower federal courts have routinely recognized claims of conspiracy<sup>8</sup> and vicarious liability<sup>9</sup> under Section 10(b) as well as aiding and abetting under the Racketeer Influenced and Corrupt Organizations Act (RICO).<sup>10</sup> Each cause of action creates liability for conduct that Congress has not expressly proscribed. Thus, *Central Bank* raises serious questions about the continued vitality of these implied causes of action.

*Central Bank* also affects the interaction among various participants in the American system of government. The Supreme Court, in effect, insists that Congress directly decide and expressly state where and when it wishes to penalize aiding and abetting conduct. Moreover, those with strong opinions about the appropriateness of aiding and abetting claims may no longer speak as litigants and amicus curiae; they now must shift their debate to Congress. Finally, civil plaintiffs must refocus their legal claim and present different facts in order to sustain a claim under Section 10(b).

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U.S.C. § 78j (1988)); see also ROBERT C. CLARK, CORPORATE LAW § 8.9, at 309 (1986) (stating that Congress designed § 10(b) as catchall provision and characterizing § 10(b) as most open-ended and important provision in 1934 Act); HAZEN, *supra* note 5, § 1.2, at 8 (stating that § 10(b) is general provision that bars fraud and material misstatements or omissions of material facts in connection with any purchase or sale of securities).

7. See *infra* note 29 (citing cases involving aiding and abetting liability); see also *infra* notes 21-25 and accompanying text (describing differences between primary and secondary liability).

8. See *infra* notes 129-35 (discussing conspiracy claims under § 10(b)).

9. See *infra* notes 157-70 (discussing vicarious liability under § 10(b)).

10. See *infra* notes 198-203 (discussing implication of aiding and abetting under RICO).

Part II of this Note reviews the background of aiding and abetting under Section 10(b) and discusses the *Central Bank* decision.<sup>11</sup> Part III examines *Central Bank's* effects on other implied causes of action.<sup>12</sup> Part IV describes the impact *Central Bank* has had and will continue to have on congressional debates and securities litigants and proposes a tactic that Congress should follow if it chooses to override *Central Bank*.<sup>13</sup> Finally, Part V suggests that, while certain aspects of the *Central Bank* decision deserve criticism, events since *Central Bank* demonstrate that with this particular securities issue, Congress, not the Court, is the better branch to resolve the dispute.

## II. The Central Bank Decision

### A. The Implied Cause of Action Under Section 10(b)

The aiding and abetting cause of action under Section 10(b) makes sense only against the background of Section 10(b)'s text and its interpretations by federal courts. The text of Section 10(b) does not expressly create a private cause of action.<sup>14</sup> However, federal courts traditionally have filled the inter-

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11. See *infra* notes 14-124 and accompanying text (discussing aiding and abetting under § 10(b) and *Central Bank* decision).

12. See *infra* notes 125-217 and accompanying text (examining effects that *Central Bank* will have on other implied causes of action).

13. See *infra* notes 218-58 and accompanying text (describing current congressional debate over *Central Bank* and suggesting strategy for Congress).

14. See the Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j (1988), which provides in part:

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

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

Section 10(b) does not, by itself, seem to proscribe anything; it simply makes it unlawful to violate Securities and Exchange Commission (SEC) rules. See CLARK, *supra* note 6, § 8.9, at 309 (noting that § 10(b) does not prohibit anything unless there is SEC rule implementing it); Steve Thel, *The Original Conception of Section 10(b) of the Securities Exchange Act*, 42 STAN. L. REV. 385, 387 n.10 (1990) (commenting that § 10(b) is not self-executing). Consequently, SEC Rule 10b-5 is relevant. See Employment of Manipulative and Deceptive Devices, 17 C.F.R. § 240.10b-5 (1994), which 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

stances of federal statutes in the name of effectuating congressional intent.<sup>15</sup> Accordingly, in 1946, the United States District Court for the Eastern District of Pennsylvania held that Section 10(b) contained an implied private cause of action that allowed private citizens to bring civil suits against violators of Section 10(b).<sup>16</sup> Twenty-five years later, the Supreme Court confirmed the existence of an implied private cause of action under Section 10(b) in *Superintendent of Insurance v Bankers Life & Casualty Co*.<sup>17</sup> The Supreme Court concluded that injured private individuals could rightfully sue violators of Section 10(b) even though Congress did not expressly provide for 10(b) civil liability.<sup>18</sup>

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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

This Note will refer only to § 10(b); this reference implies the inclusion of Rule 10b-5.

15. See *Cannon v University of Chicago*, 441 U.S. 677, 689-94 (1979) (implying private cause of action under Title IX of Education Amendments of 1972, 20 U.S.C. § 1681(a) (1988), and commenting that doing so effectuated Congress's intent to create broad remedial scheme); *J.I. Case Co. v Borak*, 377 U.S. 426, 432-33 (1964) (implying private cause of action under Securities Exchange Act of 1934 § 14(a), 15 U.S.C. § 78n(a) (1988), and commenting that Court had duty to imply remedy to preserve Congress's chief purpose of protecting investors); see also ERWIN CHEMERINSKY, *FEDERAL JURISDICTION* § 6.3, at 353, 358 (2d ed. 1994) (describing Court's willingness to imply private cause of action or create federal law to further congressional intent).

16. See *Kardon v National Gypsum Co.*, 69 F Supp. 512, 513 (E.D. Pa. 1946) (applying common-law tort principles and concluding that when person disregards commands of statute that person commits wrongful act and tort). In *Kardon*, the district court considered whether a private individual had a cause of action pursuant to § 10(b) to enforce its text. *Id.* at 513. The plaintiffs alleged that the defendants participated in certain fraudulent misrepresentations and suppressions of truth which induced plaintiffs to sell their stock to defendants for less than the stock's true value. *Id.* The district court noted that without question the complaint set forth sufficient facts to show a violation of § 10(b). *Id.* The court acknowledged that § 10(b) did not expressly allow a civil suit by persons injured as a result of § 10(b) violations. *Id.* The district court, however, considered the whole statute and its broad remedial purpose and concluded that it could imply a private cause of action under § 10(b). *Id.* at 514.

17. 404 U.S. 6 (1971).

18. *Superintendent of Ins. v Bankers Life & Casualty Co.*, 404 U.S. 6, 13 n.9 (1971) (confirming implied private cause of action under § 10(b) with virtually no discussion). In *Superintendent*, the Court addressed whether § 10(b) protected a seller of bonds from fraud

Originally, courts advanced two separate grounds to justify the implied cause of action for damages under Section 10(b). First, courts stated that the implied cause of action would effectuate congressional intent.<sup>19</sup> Second, courts invoked the common-law tort principle that, "where a right exists, a remedy exists."<sup>20</sup> In effect, the courts concluded that actors who engage in the central acts proscribed by Section 10(b) are primarily liable for that violation.<sup>21</sup>

Additionally, courts extended liability for conduct not expressly prohibited by Section 10(b) by adhering to the common-law theory of secondary liability.<sup>22</sup> Secondary liability differs from primary liability in one significant respect: Primary liability involves a violation of the text of the statute;

and deceit. *Id.* at 7. The complaint alleged that Bankers Life & Casualty Co., among others, deceived Manhattan, the seller of Treasury bonds, into authorizing the sale by misrepresenting that the sale proceeds would be of equal value with a certificate of deposit that Bankers Life and others gave to Manhattan in exchange for the bonds. *Id.* at 7-8 & n.1. The Court concluded that § 10(b)'s text protected Manhattan from any manipulative or deceptive devices. *Id.* at 9. The Court recognized that implication of a private right of action under § 10(b) was appropriate. *Id.* at 13 n.9. The Court remanded the case for trial providing no opinion on the merits but held that § 10(b) provided Manhattan with a cause of action. *Id.* at 13-14.

19. See *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 730 (1975) (noting that implication of private cause of action under § 10(b) was consistent with general recognition that private enforcement supplements SEC action in terms of protecting investors); *Kardon*, 69 F. Supp. at 514 (noting that 1934 Act has broad purpose of regulating securities transactions; therefore, mere omission of express provision for civil liability was not sufficient to negate what general law implies).

20. See *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 196-97 (1976) (noting that although there was no indication that Congress contemplated private remedy under § 10(b), § 10(b) created right and courts had firmly established private cause of action to enforce that right); *Kardon*, 69 F. Supp. at 513 (citing ancient maxim which means "where a right exists, a remedy exists"); see also *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 163 (1803) (noting that essence of civil liberty consists in right of every injured individual to claim protection of laws and stating that it is duty of government to afford that protection); Daniel R. Fischel, *Secondary Liability Under Section 10(b) of the Securities Act of 1934*, 69 CAL. L. REV. 80, 80 (1981) (describing origins of implied right of action under § 10(b)).

21. See William H. Kuehnle, *Secondary Liability Under the Federal Securities Laws — Aiding and Abetting, Conspiracy, Controlling Person, and Agency: Common-Law Principles and the Statutory Scheme*, 14 J. CORP. L. 313, 318 (1988) (noting that courts classify those who engage in central act proscribed by statute as primary violators).

22. See Fischel, *supra* note 20, at 80 (noting that lower federal courts relied on criminal and tort common-law doctrines when imposing secondary liability); Kuehnle, *supra* note 21, at 315 (acknowledging that Congress did not expressly provide for secondary liability in securities laws, except for "controlling person" provisions, although courts rarely question secondary liability's basis).

secondary liability does not.<sup>23</sup> Thus, a defendant can be secondarily liable for a violation of Section 10(b) by having a close relationship with the primary violator,<sup>24</sup> even though the defendant did not engage in conduct proscribed by Section 10(b).<sup>25</sup>

### B. Aiding and Abetting

The United States District Court for the Northern District of Indiana, in *Brennan v. Midwestern Life Insurance*,<sup>26</sup> was the first court to find a defendant who did not engage in conduct prohibited by the text of Section 10(b) secondarily liable because of the defendant's close relationship to the primary violator.<sup>27</sup> The *Brennan* court created 10(b) liability based on the

23. See Fischel, *supra* note 20, at 80 (drawing distinction between primary and secondary liability and noting that defendant may be secondarily liable for actions of primary violator if defendant had close enough relationship to primary violator). See generally Ralph C. Ferrara & Diane Sanger, *Derivative Liability in Securities Law: Controlling Person Liability, Respondeat Superior, and Aiding and Abetting*, 40 WASH. & LEE L. REV. 1007 (1983) (providing overview of manner in which judicial and administrative decisions have balanced congressional intent with common law in areas of controlling person liability, respondeat superior, and aiding and abetting liability); J. Michael Gottesman, *Brokers' Derivative Liability: Does Supervision Make a Difference?*, 41 BROOK. L. REV. 181 (1974) (examining relationship between statutory and common-law basis for liability under securities laws); Kuehnle, *supra* note 21 (discussing secondary liability based on aiding and abetting, conspiracy, and respondeat superior under securities laws); David S. Ruder, *Multiple Defendants in Securities Law Fraud Cases: Aiding and Abetting, Conspiracy, In Pari Delicto, Indemnification, and Contribution*, 120 U. PA. L. REV. 597 (1972) (describing common-law elements underlying courts' decisions concerning secondary liability under securities laws).

24. See *infra* notes 31-32 and accompanying text (describing nature of "close relationship" that creates secondary liability in defendant).

25. See Kuehnle, *supra* note 21, at 318 (stating that secondary violator does not engage in central act proscribed by statute but assists or supports primary violator's act and therefore is liable because of relationship with primary violator).

26. 259 F. Supp. 673 (N.D. Ind. 1966).

27. See *Brennan v. Midwestern Life Ins.*, 259 F. Supp. 673, 681 (N.D. Ind. 1966) (allowing plaintiff to assert cause of action against defendant based on theory of secondary liability), *aff'd*, 417 F.2d 147 (7th Cir. 1969), *cert. denied*, 397 U.S. 989 (1970). The *Brennan* court addressed the issue of whether a plaintiff had an implied cause of action for aiding and abetting under § 10(b). *Id.* at 675-76. Plaintiff alleged that Dobich Securities Corp. was a principal violator of § 10(b). *Id.* at 675. Dobich, while in bankruptcy, allegedly used stock purchase money as working capital for speculation and other improper purposes and then fraudulently misrepresented to plaintiffs the reasons for the delays in the delivery of the purchased shares of stock. *Id.* Plaintiffs alleged that defendants knew of Dobich's activities and failed to report Dobich's activities to the proper authorities. *Id.*



common-law tort theory that a defendant who aided and abetted a primary violator was secondarily liable even though the defendant's conduct did not violate the text of Section 10(b).<sup>28</sup> After the *Brennan* decision, all twelve circuits acknowledged the existence of a cause of action for aiding and abetting under Section 10(b).<sup>29</sup> The Supreme Court did not refute or reinforce the lower federal courts' assumption that a valid claim existed for aiding and abetting under Section 10(b); instead, prior to *Central Bank*, the Court specifically reserved judgment on the question.<sup>30</sup>

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Further, plaintiffs contended that defendants knowingly and purposely encouraged an artificial build-up in the market of its stock. *Id.* As a result, plaintiffs asserted that defendants were in a more favorable position and that defendants' officers and directors realized substantial personal profit from the sale of the stock. *Id.* In *Brennan*, the district court referred to other § 10(b) cases in which the SEC asserted claims based on aiding and abetting. *Id.* at 677. The district court considered the legislative history of § 10(b), but noted that it shed little light on the congressional understanding of the applicability of § 10(b) to aiders and abettors. *Id.* The court referred to the *Restatement of Torts* and concluded that tort principles best fulfilled the purposes of the 1934 Act. *Id.* at 680. Consequently, the district court recognized an aiding and abetting cause of action under § 10(b) based on the premise that it should read the 1934 Act flexibly in order to implement the 1934 Act's policies and purposes. *Id.* at 681.

28. See *id.* at 681 (recognizing implied cause of action for aiding and abetting).

29. See, e.g., *Farlow v. Peat, Marwick, Mitchell & Co.*, 956 F.2d 982, 986 (10th Cir. 1992) (outlining elements that plaintiff must allege to establish secondary liability in defendant as aider and abettor under § 10(b)); *K & S Partnership v. Continental Bank*, 952 F.2d 971, 977 (8th Cir. 1991) (same), *cert. denied*, 112 S. Ct. 2993 (1992); *Levine v. Diamanthuset, Inc.*, 950 F.2d 1478, 1483 (9th Cir. 1991) (same); *Schatz v. Rosenberg*, 943 F.2d 485, 495 (4th Cir. 1991) (same), *cert. denied*, 112 S. Ct. 1475 (1992); *Fine v. American Solar King Corp.*, 919 F.2d 290, 300 (5th Cir. 1990) (same), *cert. dismissed sub nom. Hurdman v. Fine*, 502 U.S. 976 (1991); *Schlifke v. Seafirst Corp.*, 866 F.2d 935, 947 (7th Cir. 1989) (same); *Schneberger v. Wheeler*, 859 F.2d 1477, 1480 (11th Cir. 1988) (same), *cert. denied*, 490 U.S. 1091 (1989); *Zoelsch v. Arthur Anderson & Co.*, 824 F.2d 27, 35-36 (D.C. Cir. 1987) (suggesting that aiding and abetting claim exists under § 10(b)); *Moore v. Fenex, Inc.*, 809 F.2d 297, 303 (6th Cir.) (outlining elements that plaintiff must allege to establish secondary liability in defendant as aider and abettor under § 10(b)), *cert. denied*, 483 U.S. 1006 (1987); *Cleary v. Perfectune, Inc.*, 700 F.2d 774, 777 (1st Cir. 1983) (same); *International Inv. Trust v. Cornfeld*, 619 F.2d 909, 922 (2d Cir. 1980) (same); *Monsen v. Consolidated Dressed Beef Co.*, 579 F.2d 793, 799 (3d Cir.) (same), *cert. denied*, 439 U.S. 930 (1978).

30. See *Herman & MacLean v. Huddleston*, 459 U.S. 375, 379 n.5 (1983) (reserving question of whether courts could imply cause of action for aiding and abetting under § 10(b)). In *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976), the Supreme Court held that a plaintiff could not sustain a § 10(b) claim by alleging only that the defendant was negligent in his or her participation in the deceit, manipulation, or fraud. *Id.* at 193. The *Hochfelder* Court concluded that the plaintiff had not proven the required level of intent. *Id.* at 214-15. The Court, therefore, noted that it was unnecessary to consider whether civil liability for aiding and abetting existed under § 10(b). *Id.* at 191 n.7

Common-law tort principles guided lower federal courts in fixing the parameters of aiding and abetting actions.<sup>31</sup> Thus, courts extended secondary liability to all defendants if plaintiffs showed that (1) someone other than the accused aider-abettor violated the text of Section 10(b), (2) the accused aider-abettor had general awareness of the impropriety of his conduct, and (3) the accused aider-abettor substantially assisted the primary wrongdoer.<sup>32</sup> Consequently, lower federal courts transformed common-law elements for aiding and abetting into a cause of action that extended 10(b) liability to those other than the primary violators.<sup>33</sup>

While twelve circuits recognized a private aiding and abetting cause of action and generally applied a similar test, some differences remained.<sup>34</sup> For

31. See Ruder, *supra* note 23, at 620 (noting that tort theory is fertile source of doctrine under § 10(b)). Professor Ruder specifically referred to § 876 of the *Restatement of Torts*. *Id.* Section 876 provided courts with a source of liability for secondary defendants and outlined three elements that plaintiffs had to satisfy before courts would impose liability. *Id.* The elements outlined in § 876 served as the basis for the three-part test that courts used when confronted with a claim that the defendant was secondarily liable. Section 876 stated that a person is liable if he:

- (a) orders or induces such conduct, knowing of the conditions under which the act is done or intending the consequences which ensue, or
- (b) knows that the other's conduct constitutes a breach of duty and gives substantial assistance or encouragement to the other so to conduct himself, or
- (c) gives substantial assistance to the other in accomplishing a tortious result and his own conduct, separately considered, constitutes a breach of duty to the third person.

RESTATEMENT OF TORTS § 876 (1939).

32. See, e.g., *Farlow v. Peat, Marwick, Mitchell & Co.*, 956 F.2d 982, 986 (10th Cir. 1992) (applying tort common-law elements of aiding and abetting); *K & S Partnership v. Continental Bank*, 952 F.2d 971, 977 (8th Cir. 1991) (same), *cert. denied*, 112 S. Ct. 2993 (1992); *Levine v. Diamantheset, Inc.*, 950 F.2d 1478, 1483 (9th Cir. 1991) (same); *Schatz v. Rosenberg*, 943 F.2d 485, 495 (4th Cir. 1991) (same), *cert. denied*, 503 U.S. 936 (1992); *Fine v. American Solar King Corp.*, 919 F.2d 290, 300 (5th Cir. 1990) (same), *cert. dismissed sub nom. Hurdman v. Fine*, 502 U.S. 976 (1991); *Schlifke v. Seafirst Corp.*, 866 F.2d 935, 947 (7th Cir. 1989) (same); *Schneberger v. Wheeler*, 859 F.2d 1477, 1480 (11th Cir. 1988) (same), *cert. denied*, 490 U.S. 1091 (1989); *Moore v. Fenex, Inc.*, 809 F.2d 297, 303 (6th Cir.) (same), *cert. denied*, 483 U.S. 1006 (1987); *Cleary v. Perfectune, Inc.*, 700 F.2d 774, 777 (1st Cir. 1983) (same); *International Inv. Trust v. Cornfeld*, 619 F.2d 909, 922 (2d Cir. 1980) (same); *Monsen v. Consolidated Dressed Beef Co.*, 579 F.2d 793, 799 (3d Cir.) (same), *cert. denied*, 439 U.S. 930 (1978).

33. Compare *supra* note 31 (outlining common-law test courts used when confronted with claim that defendant was secondarily liable) with *supra* note 32 and accompanying text (describing elements that courts used when deciding whether defendant aided and abetted primary violator).

34. *Hearing on Abandonment of the Private Right of Action and for Aiding and Abetting*

example, every circuit considered "substantial assistance" an element of Section 10(b) aiding and abetting liability.<sup>35</sup> Different courts, however, characterized "substantial assistance" in slightly different ways.<sup>36</sup> These

*Securities Fraud/Staff Report on Private Securities Litigation Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing, and Urban Affairs*, 103d Cong., 2d Sess. 77-78 (1994) [hereinafter *Senate Hearing*] (prepared statement of David S. Ruder, Professor of Law, Northwestern University, Former Chairman of the SEC 1987-1989) (noting that while courts had generally imposed aiding and abetting liability in consistent manner prior to *Central Bank*, some areas of doubt existed).

35. See, e.g., *Farlow v. Peat, Marwick, Mitchell & Co.*, 956 F.2d 982, 986 (10th Cir. 1992) (requiring plaintiff to show that defendant substantially assisted primary wrongdoer before extending 10(b) liability based on claim of aiding and abetting); *K & S Partnership v. Continental Bank*, 952 F.2d 971, 977 (8th Cir. 1991) (same), *cert. denied*, 112 S. Ct. 2993 (1993); *Levine v. Diamantheset, Inc.*, 950 F.2d 1478, 1483 (9th Cir. 1991) (same); *Schatz v. Rosenberg*, 943 F.2d 485, 495 (4th Cir. 1991) (same), *cert. denied*, 503 U.S. 936 (1992); *Fine v. American Solar King Corp.*, 919 F.2d 290, 300 (5th Cir. 1990) (same), *cert. dismissed sub nom. Hurdman v. Fine*, 502 U.S. 976 (1991); *Schlifke v. Seafirst Corp.*, 866 F.2d 935, 947 (7th Cir. 1989) (same); *Schneberger v. Wheeler*, 859 F.2d 1477, 1480 (11th Cir. 1988) (same), *cert. denied*, 490 U.S. 1091 (1989); *Moore v. Fenex, Inc.*, 809 F.2d 297, 303 (6th Cir.) (same), *cert. denied*, 483 U.S. 1006 (1987); *Cleary v. Perfectune, Inc.*, 700 F.2d 774, 777 (1st Cir. 1983) (same); *International Inv. Trust v. Cornfeld*, 619 F.2d 909, 922 (2d Cir. 1980) (same); *Monsen v. Consolidated Dressed Beef Co.*, 579 F.2d 793, 799 (3d Cir.) (same), *cert. denied*, 439 U.S. 930 (1978).

36. See, e.g., *Camp v. Dema*, 948 F.2d 455, 460 (8th Cir. 1991) (noting that substantial causal connection must exist between culpable conduct of alleged aider and abettor and harm to plaintiff); *Schatz v. Rosenberg*, 943 F.2d 485, 497 (4th Cir. 1991) (requiring plaintiff to prove that defendant rendered "substantial assistance" to primary securities law violation, not merely to person committing violation), *cert. denied*, 503 U.S. 936 (1992); *Moore v. Fenex, Inc.*, 809 F.2d 297, 303-04 (6th Cir.) (distinguishing cases involving nondisclosure and requiring plaintiff to show that aider and abettor consciously intended to provide aid by proving either culpable state of mind or conduct from which court or jury could infer culpable state of mind), *cert. denied*, 483 U.S. 1006 (1987); *Woods v. Barnett Bank*, 765 F.2d 1004, 1009-10 (11th Cir. 1985) (determining whether substantial assistance existed based upon all circumstances surrounding transaction in question); *International Inv. Trust v. Cornfeld*, 619 F.2d 909, 922, 925-27 (2d Cir. 1980) (noting that courts were still delineating exact content of phrase "substantial assistance," but that there may exist nexus between degree of scienter and requirement that alleged aider and abettor rendered "substantial assistance"); *Monsen v. Consolidated Dressed Beef Co.*, 579 F.2d 793, 800 (3d Cir.) (inaction may constitute substantial assistance when plaintiff demonstrates that aider and abettor consciously intended to assist in perpetration of wrongful act), *cert. denied*, 439 U.S. 930 (1978); *Woodward v. Metro Bank*, 522 F.2d 84, 97 (5th Cir. 1975) (commenting that "substantiality" of assistance is function of all circumstances). The United States Court of Appeals for the Seventh Circuit also required the plaintiff to prove that the defendant substantially assisted the primary offender. This requirement, however, was not as important in the Seventh Circuit as in other circuits because the Seventh Circuit imposed aider and abettor liability only when the plaintiff showed that the aider and abettor's conduct met all the elements for primary liability except

variations occurred because Section 10(b) does not prohibit "substantial assistance" of a primary violation.<sup>37</sup> Courts, therefore, lacked textual guidance as to precisely what conduct amounted to "substantial assistance."<sup>38</sup> Courts tended to focus on different factors, so predicting what would constitute substantial assistance in any one case became difficult. For example, some courts focused on whether a causal connection existed between the defendant's action or inaction and the plaintiff's harm.<sup>39</sup> Others focused on whether the defendant had a duty to disclose the primary violator's activities to the plaintiff.<sup>40</sup> Additionally, courts struggled to isolate the precise state of mind required in order to sustain a claim of aiding and abetting against the defendant. Although most lower courts adjusted the required intent according to whether the accused aider and abettor had a fiduciary duty to

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that the aider and abettor had not actually sold the securities. *See Barker v Henderson, Franklin, Starnes & Holt*, 797 F.2d 490, 495-96 (7th Cir. 1986) (stating that plaintiff must show that each alleged aider and abettor committed "manipulative or deceptive" acts or otherwise met standards of direct liability, except plaintiff does not have to show that defendant offered or sold securities).

37. Compare note 14 (providing text of § 10(b), which makes no mention of prohibited conduct encompassing "substantial assistance") with notes 35-40 and accompanying text (including "substantial assistance" as element of aiding and abetting cause of action under § 10(b)).

38. *See* Brief for Petitioner at 17, *Central Bank v First Interstate Bank*, 114 S. Ct. 1439 (1994) (No. 92-854) (noting that while each court of appeals addressed "substantial assistance" issue, there was little uniformity in courts' application of "substantial assistance" standard).

39. *See Camp v. Dema*, 948 F.2d 455, 462 (8th Cir. 1991) (noting that affirmative acts will only constitute substantial assistance if there is substantial causal connection between these acts and harm suffered by plaintiff); *Moore v Fenex, Inc.*, 809 F.2d 297, 303-04 (6th Cir.) (noting that in cases involving nondisclosure, plaintiffs must show that defendant consciously intended for silence to aid securities law violation), *cert. denied*, 483 U.S. 1006 (1987); *Woods v Barnett Bank*, 765 F.2d 1004, 1012-13 (11th Cir. 1985) (concluding that alleged aider and abettor's atypical business action was causal factor in perpetration of fraud and therefore finding substantial assistance); *Woodward v Metro Bank*, 522 F.2d 84, 97 (5th Cir. 1975) (noting that if evidence shows no more than transaction constituting routine activities, court would not find § 10(b) liability without clear proof of intent to violate securities laws); *Landy v FDIC*, 486 F.2d 139, 163 (3d Cir. 1973) (referring to *Restatement of Torts* and explaining that "substantial assistance" may occur if encouragement or assistance is substantial factor in causing resulting tort), *cert. denied*, 416 U.S. 960 (1974).

40. *See Schatz v Rosenberg*, 943 F.2d 455, 496-97 (4th Cir. 1991) (stating that in absence of duty to disclose primary violator's action, defendant's inaction cannot constitute substantial assistance), *cert. denied*, 503 U.S. 936 (1992); *International Inv Trust v Cornfeld*, 619 F.2d 909, 927 (2d Cir. 1980) (noting that generally inaction can create aiding and abetting liability only when there is conscious or reckless violation of independent duty to act).

disclose or act,<sup>41</sup> a minority of courts discarded this inquiry and asked simply whether defendants took affirmative action in their roles as aiders and abettors.<sup>42</sup>

### C. Central Bank

#### 1. The Facts

In *Central Bank*, the plaintiffs did not allege that the court should find Central Bank primarily liable for violating the text of Section 10(b).<sup>43</sup> Instead, the plaintiffs sought to make Central Bank secondarily liable based on a claim that Central Bank aided and abetted the Section 10(b) violation.<sup>44</sup> The plaintiff argued that three main actors participated in the transactions that led to the suit in *Central Bank*: the Colorado Springs-Stetson Hills Public Building Authority (Authority), the developer of Stetson Hills (Developer), and the Central Bank of Denver (Central Bank).

The Authority wanted to make public improvements in a planned residential and commercial development in Colorado Springs, Colorado.<sup>45</sup> The

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41. See, e.g., *Camp v Dema*, 948 F.2d 455, 463 (8th Cir. 1991) (holding that because defendant owed no duty of disclosure to plaintiff, showing of recklessness did not satisfy knowledge requirement); *Schatz*, 943 F.2d at 496 (noting that degree of knowledge required for aiding and abetting liability turns on whether defendant owed duty to plaintiff); *Woods v Barnett Bank*, 765 F.2d 1004, 1010 (11th Cir. 1985) (requiring plaintiff to prove defendant's conscious intent to provide assistance to violation when defendant owed no duty to disclose); *Cleary v Perfectune, Inc.*, 700 F.2d 774, 777 (1st Cir. 1983) (same); *Armstrong v McAlpin*, 699 F.2d 79, 91 (2d Cir. 1983) (noting that if alleged aider and abettor owes fiduciary duty to plaintiff, recklessness is enough; otherwise, assistance rendered must be knowing and substantial); *Walck v American Stock Exch.*, 687 F.2d 778, 791 (3d Cir. 1982) (requiring plaintiff to show that defendant had actual knowledge of § 10(b) violation when defendant lacked fiduciary duty to plaintiff), *cert. denied*, 461 U.S. 942 (1983); see also Joel S. Feldman, *The Breakdown of Securities Fraud Aiding and Abetting Liability: Can a Uniform Standard Be Resurrected?*, 19 SEC. REG. L.J. 45, 53-57 (1991) (describing scienter requirement employed by majority of circuits).

42. See *First Interstate Bank v Pring*, 969 F.2d 891, 899 (10th Cir. 1992) (rejecting notion that absent duty to disclose, silence or inaction cannot be basis for aiding and abetting liability), *rev'd sub nom.* *Central Bank v First Interstate*, 114 S. Ct. 1439 (1994). In *Pring*, the court of appeals placed emphasis on whether the alleged aider and abettor would benefit from silence instead of categorically stating that silence or inaction can never be a basis for aiding and abetting liability. *Id.*, see also *Levine v Diamanthuset, Inc.*, 950 F.2d 1478, 1484 (9th Cir. 1991) (inferring substantial assistance from defendant's actions, not because defendant's assistance aided in retention of investors, but because prospective investors relied on defendant's confirmations).

43. *Central Bank v First Interstate Bank*, 114 S. Ct. 1439, 1443 (1994).

44. *Id.*

45. *Id.*

Authority had to raise capital to reimburse the Developer for the cost of the public improvements.<sup>46</sup> By issuing bonds in 1986 and 1988, the Authority raised a total of \$26 million.<sup>47</sup>

In an effort to increase the attractiveness of the bonds to investors, the Authority offered a bond indenture<sup>48</sup> that included several provisions designed to protect investors. First, landowner assessment liens on the Colorado Springs property secured the bonds.<sup>49</sup> Second, the bond indenture required that the value of the land subject to the liens equal at least 160% of the bonds' outstanding principal and interest (160% test).<sup>50</sup> Third, the bond indenture named Central Bank as the indenture trustee for the bond issues.<sup>51</sup> Finally, the bond indenture required the Developer to provide Central Bank with an annual appraisal verifying that the land subject to the liens met the 160% test.<sup>52</sup>

In 1986, the land subject to the liens met the 160% test. In January 1988, while proposing to secure the 1988 bonds, the Developer provided Central Bank with an appraisal of the same land that secured the 1986 bonds.<sup>53</sup> According to the Developer's 1988 appraisal, the land values remained virtually unchanged from the 1986 appraisal and thus the property appeared to meet the 160% test.<sup>54</sup> Shortly after receiving the Developer's 1988 appraisal, however, Central Bank became concerned about the appraisal's accuracy. Central Bank's concern stemmed from comments made

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46. *Pring*, 969 F.2d at 893.

47. *Id.*

48. *Black's Law Dictionary* defines "bond indenture" as a contract between the issuer of the bonds and the bondholders. BLACK'S LAW DICTIONARY 181 (6th ed. 1991).

49. *Black's Law Dictionary* defines "assessment" as a determination as to the value of property and "lien" as a charge against the property that secures performance of an obligation. *Id.* at 116, 922 (defining assessment and lien respectively). Therefore, with the bonds at issue in *Central Bank*, the bondholders' security was dependent on the value of the property.

50. *Central Bank*, 114 S. Ct. at 1443.

51. *Black's Law Dictionary* defines "indenture trustee" as a person or entity charged with carrying out the terms of the bond indenture. BLACK'S LAW DICTIONARY 770 (6th ed. 1991). The theory behind the appointment of an indenture trustee is that the trustee will be an impartial party who can mediate and resolve conflicts between the issuer of the bonds and the bondholders who may at times have adverse interests. See HARRY G. HENN & JOHN R. ALEXANDER, LAWS OF CORPORATIONS § 300, at 837-38 (3d ed. 1983) (discussing requirement that bond indenture name trustee as protector of investors).

52. *Central Bank*, 114 S. Ct. at 1443.

53. *Id.*

54. *Id.*

by the senior underwriter for the 1986 bonds.<sup>55</sup> The senior underwriter informed Central Bank that property values in Colorado Springs had decreased. More significantly, the senior underwriter stated that the Developer's appraisal was sixteen months old and that therefore the senior underwriter doubted that the appraisal accurately reflected the property's value.<sup>56</sup>

Because the bond indenture named Central Bank as indenture trustee, Central Bank expressed concern that the Developer had violated the 160% test. Central Bank first consulted with an in-house appraiser about the Developer's 1988 appraisal.<sup>57</sup> The in-house appraiser agreed with the senior underwriter that the appraisal appeared optimistic and suggested that Central Bank retain an outside appraiser to conduct an independent review.<sup>58</sup> In light of the apparent inaccuracy of the Developer's appraisal, Central Bank, as indenture trustee, required that an independent appraiser review the Developer's 1988 appraisal.<sup>59</sup>

Before the independent appraiser conducted the review, Central Bank met with representatives of the Developer and the Authority to determine why the Developer's appraisal did not show a decline in land values from the 1986 appraisal.<sup>60</sup> The Developer responded that the real estate values reflected \$10 million worth of improvements to the property that offset any decline in real estate value.<sup>61</sup> The bond indenture gave Central Bank, as indenture trustee, the discretionary power to demand an independent review of the Developer's appraisal.<sup>62</sup> After hearing the Developer's explanation, however, Central Bank agreed to delay the independent review until the end of 1988, approximately six months after the closing on the 1988 bond issue.<sup>63</sup> The Authority defaulted on the 1988 bonds before the independent review took place.<sup>64</sup>

After the Authority's default, First Interstate Bank of Denver (First Interstate) and two 1988 bondholders sued the Developer and Central Bank, among others, alleging that the sale of bonds violated Section 10(b) of the

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55. *Id.*

56. *Id.*

57. *Id.*

58. *Id.*

59. *First Interstate Bank v. Pring*, 969 F.2d 891, 894 (1992), *rev'd sub nom. Central Bank v. First Interstate Bank*, 114 S. Ct. 1439 (1994).

60. *Id.*

61. *Id.* at 894 n.6.

62. *Id.* at 894.

63. *Id.* at 895.

64. *Central Bank*, 114 S. Ct. at 1443.

1934 Act.<sup>65</sup> First Interstate did not allege that Central Bank was the primary violator of Section 10(b).<sup>66</sup> Instead, First Interstate alleged that the Developer was a primary violator of Section 10(b) because the Developer fraudulently inflated the value of the Colorado real estate that the Authority used to secure the municipal bonds.<sup>67</sup> First Interstate alleged that Central Bank was secondarily liable because Central Bank knowingly or recklessly aided and abetted the Section 10(b) violation by deciding to postpone the independent review of the appraisal until after the Authority issued the 1988 bonds.<sup>68</sup>

## 2. The Supreme Court Decision

While lower federal courts were developing a federal common law aiding and abetting liability under Section 10(b), the Supreme Court was developing its own method of statutory interpretation of securities statutes.<sup>69</sup> The Court diminished the emphasis on common-law principles<sup>70</sup> and the

65. See *supra* note 14 (providing text of § 10(b)).

66. See *Warren v Reserve Fund, Inc.*, 728 F.2d 741, 744 (5th Cir. 1984) (outlining elements of primary liability under § 10(b)). *Warren* provides an example of the elements that a plaintiff must establish before courts will impose primary liability under § 10(b). The plaintiff must establish: (1) a misrepresentation, omission, or other fraudulent device, (2) a purchase or sale of securities in connection with the fraudulent device, (3) scienter by defendant in making the misrepresentation or omission, (4) materiality of the misrepresentation or omission, (5) justifiable reliance on the fraudulent device by plaintiff; and (6) damages resulting from the fraudulent device. *Id.*

67. *Central Bank*, 114 S. Ct. at 1443.

68. See Petitioner's Brief at 8, *Central Bank*, (No. 92-854); see also *supra* notes 22-33 and accompanying text (discussing distinction between secondary and primary liability and aiding and abetting claim).

69. See generally H. Miles Foy, III, *Some Reflections on Legislation, Adjudication, and Implied Private Actions in the State and Federal Courts*, 71 CORNELL L. REV. 501 (1986) (discussing Court's movement from presumption in favor of implying remedies to approach focusing more strictly on congressional intent); Thomas L. Hazen, *Implied Private Remedies Under Federal Statutes: Neither a Death Knell Nor a Moratorium — Civil Rights, Securities Regulation, and Beyond*, 33 VAND. L. REV. 1333 (1980) (discussing Supreme Court's criteria development and clarification when faced with question of whether implied right exists under statute); H. Peter Haveles, Jr., Note, *An Analytical Framework for Implied Causes of Action: Section 17 of the Securities Exchange Act and Redington v Touche Ross & Co.*, 59 B.U. L. REV. 157 (1979) (discussing Supreme Court's use of clarified and refined criteria when determining whether to imply private cause of action).

70. In *Herman & MacLean v Huddleston*, 459 U.S. 375 (1983), the Supreme Court addressed whether persons seeking recovery under § 10(b) must prove their cause of action by clear and convincing evidence rather than by a preponderance of the evidence. *Id.* at 377. In making the decision, the Court noted that "[r]eference to common-law practices can be misleading." *Id.* at 388. In *Blue Chips Stamps v Manor Drug Stores*, 421 U.S. 723 (1975),



effectuation of Congress's broad remedial purposes; instead, the Court focused on the statute's text.<sup>71</sup> Two decisions exemplify this interpretive shift: *J.I. Case Co. v Borak*<sup>72</sup> and *Touche Ross & Co. v Redington*.<sup>73</sup> Both cases involved the 1934 Act, and in both cases the plaintiffs argued that the statute implied a private cause of action.

In *Borak*,<sup>74</sup> the Court addressed the issue of whether a violation of Section 14(a) of the 1934 Act entitled a shareholder to a private cause of action for damages.<sup>75</sup> Essentially, Section 14(a) states that an individual violates the law when he solicits proxies in violation of the rules the Securities and Exchange Commission (SEC) prescribes.<sup>76</sup> The *Borak* Court conceded that Section 14(a)'s text made no specific reference to a private cause of action.<sup>77</sup> The Court stated, however, that because Congress adopted Section 14(a) primarily to protect investors, the Court had a duty to provide remedies necessary to effectuate that congressional purpose.<sup>78</sup>

the Court noted that the typical fact situation in which the classic tort of misrepresentation and deceit evolved was extremely different from the world of commercial transactions to which Rule 10b-5 is applicable. *Id.* at 744-45.

71. See *infra* notes 101-05 and accompanying text (describing Supreme Court's emphasis on statute's language when deciding whether to imply private cause of action).

72. 377 U.S. 426 (1964).

73. 442 U.S. 560 (1979).

74. *J.I. Case Co. v Borak*, 377 U.S. 426 (1964). In *Borak*, the Supreme Court considered whether it was appropriate to imply a private cause of action under § 14(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78n(a) (1988). *Id.* at 427. A stockholder of *J.I. Case Co.* (Case) brought the civil suit. *Id.* The stockholder objected to a merger between Case and another company. *Id.* The stockholder alleged that those proposing the merger circulated a false and misleading proxy statement in violation of § 14(a). *Id.* at 428. The Court noted that § 14(a) did not specifically grant the private stockholder the right to enforce § 14(a) by bringing a civil suit. *Id.* 432. The *Borak* Court, however, relied on the overall purpose of the 1934 Act and concluded that it should imply a private cause of action when the remedies would further the congressional purpose. *Id.* at 432-33.

75. See the Securities Exchange Act of 1934 § 14(a), 15 U.S.C. § 78n(a) (1988), which states:

It shall be unlawful for any person, by the use of the mails or by any means or instrumentality of interstate commerce or of any facility of any national securities exchange or otherwise, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors, to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security (other than an exempted security) registered pursuant to Section 78l of this title.

76. See *supra* note 75 (providing text of § 14(a)).

77. *Borak*, 377 U.S. at 432.

78. *Id.* at 432-33; see CHEMERINSKY, *supra* note 15, § 6.3, at 359 (discussing *Borak*

Fifteen years later in *Redington*,<sup>79</sup> the Supreme Court considered whether Section 17(a) of the 1934 Act implied a private cause of action for damages.<sup>80</sup> Section 17(a) established record-keeping requirements for exchanges, brokers, and dealers.<sup>81</sup> Like Section 14(a), Section 17(a)'s text did not expressly provide for a private cause of action.<sup>82</sup> Instead of emphasizing the 1934 Act's broad purpose to protect investors, however, the *Redington*

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decision and noting that *Borak* approach allows federal courts to create private cause of action if damage suits would help accomplish legislative purpose of statute).

79. *Touche Ross & Co. v. Redington*, 442 U.S. 560 (1979). The *Redington* Court determined whether it could imply a private cause of action under § 17(a) of the 1934 Act so that private customers could bring a civil suit for damages against those who violated the requirements of § 17(a). *Id.* at 562. Section 17(a) established record-keeping requirements for exchanges, brokers, and dealers. *See infra* note 80 (providing text of § 17(a)). Weis Securities, Inc. (Weis), a securities brokerage firm, retained Touche Ross & Co. (Touche Ross) to serve as Weis's independent certified public accountant. *Redington*, 442 U.S. at 563. The case arose out of Weis's insolvency and liquidation. *Id.* at 564. The Securities Investor Protection Corporation (SIPC) and the appointed trustee in the liquidation of the Weis business filed an action for damages against Touche Ross for conducting an improper audit and certification of Weis's financial statements. *Id.* at 565-66. Along with other claims, SIPC and the trustee alleged that Touche Ross violated § 17(a). *Id.* at 566. The *Redington* Court noted that SIPC's argument in favor of implying a private cause of action based on tort principles was not persuasive. *Id.* at 586. The Court analyzed § 17(a) and concluded that Congress did not intend to create a private cause of action. *Id.* at 568-78. Consequently, the Court concluded it would not create an implied cause of action. *Id.* at 579.

80. At the time relevant to the *Redington* decision, Securities Exchange Act § 17(a), 15 U.S.C. § 78q(a) (1970), read as follows:

Every national securities exchange, every member thereof, every broker or dealer who transacts a business in securities through the medium of any such member, every registered securities association, and every broker or dealer registered pursuant to section 78o of this title, shall make, keep, and preserve for such periods, such accounts, correspondence, memoranda, papers, books, and other records, and make such reports, as the Commission by its rules and regulations may prescribe as necessary or appropriate in the public interest or for the protection of investors. Such accounts, correspondence, memoranda, papers, books, and other records shall be subject at any time or from time to time to such reasonable periodic, special, or other examinations by examiners or other representatives of the Commission as the Commission may deem necessary or appropriate in the public interest or for the protection of investors.

Congress amended § 17 of the 1934 Act after the *Redington* decision. Compare 15 U.S.C. § 78q(a) (1970) with 15 U.S.C. § 78q(a)(1) (1988).

81. 15 U.S.C. § 78q(a) (1970).

82. *Redington*, 442 U.S. at 562. Compare *supra* note 75 (providing text of § 14(a)) with *supra* note 80 (providing text of § 17(a)).

Court looked closely at Section 17(a)'s text and at what the statutory scheme should reasonably permit.<sup>83</sup>

This different approach led the *Redington* Court to conclude that if Congress did not provide investors with a private damages remedy, then the Court would not imply one.<sup>84</sup> In response to the plaintiff's contention that such a conclusion served an injustice, the *Redington* Court noted that even if that were the case, the Supreme Court was the wrong forum in which to make the injustice argument.<sup>85</sup> According to the Court, plaintiffs should make the injustice argument before Congress — the branch at liberty to legislate.<sup>86</sup>

Like *Borak* and *Redington*, *Central Bank* involved the 1934 Act. In *Central Bank*, however, the Court faced a different issue. In *Borak* and *Redington*, the Court decided whether an implied civil remedy existed for private plaintiffs when defendants violated the text of Sections 14(a) and 17(a), respectively.<sup>87</sup> *Central Bank* did not involve a similar inquiry because the Supreme Court had already determined that a plaintiff could bring a private civil suit against defendants who violate the text of Section 10(b).<sup>88</sup>

Perhaps because of the Supreme Court's altered disposition toward implied causes of action under the 1934 Act,<sup>89</sup> the Court on its own motion

83. See *Redington*, 442 U.S. at 578 (noting that generalized references to remedial purposes of 1934 Act do not justify reading provision more broadly than its language and statutory scheme reasonably permit).

84. *Id.* at 578-79; see CHEMERINSKY, *supra* note 15, § 6.3, at 358 (noting that Court's basic inquiry when determining whether to imply cause of action is always whether Congress intended, explicitly or implicitly, to create private cause of action, but stating that what constitutes sufficient evidence of intent and Court's restrictive or liberal approach to construing that evidence have changed over time).

85. *Redington*, 442 U.S. at 579.

86. *Id.*

87. See *supra* note 21 and accompanying text (noting that when defendant violates expressed language of statute, courts characterize defendant as primary violator).

88. See *Superintendent of Ins. v. Bankers Life & Casualty Co.*, 404 U.S. 6, 13 n.9 (1971) (recognizing implied cause of action under § 10(b)); see also *Herman & MacLean v. Huddleston*, 459 U.S. 375, 380 (1983) (noting that existence of implied remedy under § 10(b) was "simply beyond peradventure"); *Ernst & Ernst v. Hochfelder*, 452 U.S. 185, 196, 212-14 (1976) (accepting existence of private cause of action under § 10(b) and concluding that plaintiff could not sustain § 10(b) action without allegation of scienter); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 733 (1975) (noting that private enforcement of § 10(b) furthered congressional intent).

89. See *supra* notes 69-86 and accompanying text (discussing Supreme Court's increasing unwillingness to imply private causes of action under 1934 Act).

ordered counsel to brief the issue of whether a plaintiff could create secondary liability under Section 10(b) based on a claim of aiding and abetting.<sup>90</sup> The Court noted that it had confronted two main issues surrounding Section 10(b):<sup>91</sup> the scope of the conduct prohibited by Section 10(b)<sup>92</sup> and the requirements that a plaintiff must meet to create primary liability under Section 10(b).<sup>93</sup> The Court classified the *Central Bank* issue as one that concerned only the scope of 10(b) liability.<sup>94</sup>

First Interstate and the SEC, as amicus curiae,<sup>95</sup> advanced four arguments in support of an implied private cause of action for aiding and abetting under Section 10(b). First, they argued that the phrase "directly or indirectly" in Section 10(b) covered aiding and abetting.<sup>96</sup> Second, First Interstate and the SEC asserted that when Congress enacted the 1934 Act,

90. See Respondent's Brief at 10, *Central Bank* (No. 92-854) (noting that vitality of aiding and abetting cause of action under § 10(b) was not challenged by *Central Bank* or by Tenth Circuit). Because lower courts had implied the cause of action for aiding and abetting for 30 years, *Central Bank* did not challenge the existence of aiding and abetting liability on appeal. *Central Bank*, 114 S. Ct. at 1457 (Stevens, J., dissenting). Instead, *Central Bank* appealed the Tenth Circuit's conclusion that a showing of recklessness satisfied the scienter requirement for aiding and abetting. *Id.*, see also *supra* note 29 (listing lower court cases in which courts allowed plaintiff to bring cause of action for aiding and abetting § 10(b) violation).

91. *Central Bank*, 114 S. Ct. at 1445.

92. See *id.* (citing as examples *Dirks v. SEC*, 463 U.S. 646, 653-54 (1983) (establishing that violation of § 10(b) by corporate insiders requires showing of relationship which affords access to inside information and taking advantage of information by trading without disclosure); *Chiarella v. United States*, 445 U.S. 222, 230 (1980) (noting that silence in connection with purchase or sale of securities may operate as actionable fraud under § 10(b) despite absence of statutory language or legislative history specifically addressing legality of nondisclosure); *Santa Fe Indus. Inc. v. Green*, 430 U.S. 462, 477-80 (1977) (refusing to extend § 10(b) to breaches of fiduciary duty of majority against minority shareholders without charge of misrepresentation or lack of disclosure and reasoning that to do so would bring within Rule 10b-5 wide variety of corporate conduct traditionally left to state regulation); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 201 (1976) (refusing to impose § 10(b) liability for negligent conduct alone)).

93. See *id.* at 1445-46 (citing as examples *Musick, Peeler & Garrett v. Employers Ins.*, 113 S. Ct. 2085, 2091 (1993) (holding that defendants in actions under § 10(b) had right to seek contribution); *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*, 501 U.S. 350, 357 (1991) (noting absence of statute of limitations in § 10(b) and adopting uniform federal statute of limitations); *Basic Inc. v. Levinson*, 485 U.S. 224, 243 (1988) (requiring plaintiff in § 10(b) action to prove reliance on defendant's misrepresentation before court will award damages); *Aaron v. SEC*, 446 U.S. 680 (1980) (requiring SEC to establish scienter as element of civil enforcement action to enjoin violations of § 10(b)).

94. *Id.* at 1446.

95. See *infra* notes 237-39 and accompanying text (discussing role of amicus curiae in courts and their present role in congressional debate).

96. *Central Bank*, 114 S. Ct. at 1447; see *supra* note 14 (providing text of § 10(b)).

Congress legislated with a general understanding of tort law.<sup>97</sup> They asserted that Congress, therefore, intended to include aiding and abetting liability under Section 10(b), even though the 1934 Act had not expressly defined aiding and abetting.<sup>98</sup> Third, First Interstate and the SEC argued that Congress had silently acquiesced in the judicial interpretation of Section 10(b) by amending the securities laws on various occasions after lower courts recognized the aiding and abetting cause of action without overruling this line of cases.<sup>99</sup> Finally, the SEC asserted that the aiding and abetting cause of action deterred secondary actors from contributing to fraudulent activities and ensured that defrauded plaintiffs received compensation.<sup>100</sup>

Justice Kennedy, writing for the Court, stated that Section 10(b)'s text defined the scope of prohibited conduct.<sup>101</sup> The Court construed the text strictly and rejected First Interstate's and the SEC's argument that Section 10(b)'s phrase — "directly or indirectly" — encompassed aiding and abetting conduct.<sup>102</sup> The Court concluded that this interpretation of Section 10(b) would extend liability to persons who did not engage in the activities expressly proscribed by Congress.<sup>103</sup> For example, the Court noted that if the Court allowed recovery for aiding and abetting under Section 10(b), a plaintiff could create 10(b) liability without proving reliance — a critical element for recovery under Section 10(b).<sup>104</sup> The Court reasoned that had

97. *Central Bank*, 114 S. Ct. at 1450; see *supra* notes 28-33 and accompanying text (discussing common-law cause of action for aiding and abetting).

98. *Central Bank*, 114 S. Ct. at 1450.

99. *Id.* at 1452.

100. *Id.* at 1453; see *infra* notes 236-38 and accompanying text (discussing fact that those parties who wanted to affect definition of prohibited conduct under § 10(b) had to resort to filing amicus curiae briefs).

101. See *Central Bank*, 114 S. Ct. at 1446 (commenting that Court would not permit challenges to conduct not prohibited by text of statute); see also Felix Frankfurter, *Some Reflections on the Reading of Statutes*, 47 COLUM. L. REV. 527, 535 (1947) (commenting that while inquiry may not end with text of statute, that is appropriate place to look initially).

102. *Central Bank*, 114 S. Ct. at 1447-48. In *Central Bank*, the Court concluded that § 10(b)'s "directly or indirectly" phrase had a variety of meanings so that First Interstate and the SEC failed to support the suggestion that § 10(b)'s text *itself* prohibited aiding and abetting. *Id.* at 1448. The Court stated that aiding and abetting liability extended to persons who did not indirectly engage in the prohibited activity, but who merely gave a degree of aid to those who did. *Id.* at 1447.

103. *Id.* at 1447-50.

104. *Id.* at 1449 (citing *Basic Inc. v. Levinson*, 485 U.S. 224, 243 (1988)); see *infra* notes 255-57 and accompanying text (describing elements that plaintiff must prove to impose primary liability on defendant under § 10(b)).

Congress desired to make aiding and abetting a Section 10(b) violation, Congress would have used the words "aid" and "abet" in the text.<sup>105</sup>

Even though the Court analyzed and based the decision on the text of Section 10(b), the Court examined and rejected the other arguments. In response to First Interstate's and the SEC's assertion that the 1934 Congress legislated with a general understanding of the common law of torts, the Court noted that such a general assertion could not support the theory that Congress specifically intended to impose aiding and abetting liability under Section 10(b).<sup>106</sup> The Court concluded that Congress decided instead when to impose aiding and abetting and other forms of secondary liability on a statute-by-statute basis.<sup>107</sup> The Court concluded, therefore, that Congress deliberately had chosen to create secondary liability in some contexts and not in others.<sup>108</sup> The Court stated that the judiciary should not interfere with this congressional choice.<sup>109</sup>

The Court summarily dismissed First Interstate's and the SEC's argument that Congress silently acquiesced in the lower courts' implication of aiding and abetting liability under Section 10(b). The Court stated that congressional inaction could not expand the scope of a duly enacted statute.<sup>110</sup>

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105. *Central Bank*, 114 S. Ct. at 1448. Unlike the lower federal courts that implied an aiding and abetting cause of action despite the absence of the exact words, the Supreme Court concluded that the absence of the words "aid" and "abet" resolved the case. *Id.* Additionally, the Court noted that had the text of § 10(b) not resolved the issue, the Court would have attempted to infer how the 1934 Congress would have addressed the issue. *Id.* The Court stated that it would have looked to the other expressed causes of action in the 1934 Act as a model for the § 10(b) action. *Id.* In *Central Bank*, the Court concluded that because Congress did not attach private aiding and abetting liability to any other express provision, Congress similarly would not have attached aiding and abetting liability to § 10(b). *Id.* at 1448.

106. *See id.* at 1450 (surveying common-law basis of aiding and abetting and concluding that existence and application of aiding and abetting was uncertain).

107. *Id.* at 1450-52. The *Central Bank* Court noted that while Congress had enacted a general aiding and abetting statute applicable to all federal criminal offenses, Congress had not enacted a civil counterpart. *Id.* at 1450. The Court specifically considered § 20(a) of the 1934 Act, which imposes liability on controlling persons who control any person liable under other provisions of the 1934 Act. *Id.* at 1451-52; *see infra* notes 163-70 and accompanying text (providing text and discussion of § 20(a)). The Court concluded that the fact that Congress chose to impose some forms of secondary liability, while not imposing others, indicated a deliberate congressional choice with which the Court should not interfere. *Central Bank*, 114 S. Ct. at 1452.

108. *Central Bank*, 114 S. Ct. at 1451-52.

109. *Id.* at 1452; *see supra* note 107 (describing Court's comparison of § 10(b) with other statutes).

110. *Central Bank*, 114 S. Ct. at 1453 (referring to U.S. Const. art. I, § 7, cl. 2 for proposition that there is only one proper way in which Congress may enact statute); *see*

Finally, the Court addressed the SEC's contention that aiding and abetting liability deterred secondary actors from contributing to fraudulent activities and ensured that participants in the Section 10(b) violation make the defrauded party whole.<sup>111</sup> While conceding that aiding and abetting liability expanded the civil remedy, the Court concluded that the uncertainties surrounding the rules of aiding and abetting had rippling effects.<sup>112</sup> For example, the Court suggested that entities exposed to secondary liability as aiders and abettors might abandon substantial defenses and pay settlements rather than face the risks of a trial.<sup>113</sup> The Court theorized that such costs might create difficulties for smaller companies in obtaining advice from professionals who have been traditional targets of aiding and abetting claims.<sup>114</sup>

While the Supreme Court's view of the other arguments offered by First Interstate and the SEC may provide insight into the resolution of future cases, the significance of the decision lies in the majority's heavy emphasis on the actual text of and statutory structure surrounding Section 10(b). Although the Court made reference to the intentions of the 1934 Congress,<sup>115</sup> the Court determined the scope of Section 10(b) by adhering primarily to a "plain statement" policy. That is, by refusing to extend Section 10(b) liability to aiders and abettors and by emphasizing the absence of the words "aid" and "abet" in the text, the Court sent an unambiguous message to Congress: "If you intend to make this conduct actionable you must say so plainly."<sup>116</sup>

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William D. Popkin, *Law-Making Responsibility and Statutory Interpretation*, 68 IND. L.J. 865, 885-86 (1993) (asserting that courts should not infer congressional intent to ratify statute's judicial interpretation from re-enactment or inaction because legislature is often unaware of judicial interpretation and because there are too many possible reasons for legislative inaction).

111. *Central Bank*, 114 S. Ct. at 1453-54.

112. *Id.* at 1454; see Tamar Frankel, *Implied Rights of Action*, 67 VA. L. REV. 553, 570-84 (1981) (critiquing policy reasons for restricting implied causes of action for securities violations); cf. *supra* notes 34-42 and accompanying text (discussing confusion among circuits as to aiding and abetting claim).

113. *Central Bank*, 114 S. Ct. at 1454. Defendants' tendency to settle when faced with a claim of aiding and abetting was significant because secondary defendants were jointly and severally liable with primary violators for any judgment rendered. See *Hearing on Securities Litigation Reform Before the Subcomm. on Telecommunications & Finance of the House Comm. on Energy & Commerce*, 103d Cong., 2d Sess. 124 (1994) [hereinafter *House Hearing*] (prepared statement of Donald C. Langevoort, Lee S. and Charles A. Speir Professor of Law, Vanderbilt University) (stating that presence of joint and several liability creates unique risks in securities litigation environment).

114. *Central Bank*, 114 S. Ct. at 1454.

115. *Id.* at 1448-50.

116. See HENRY M. HART, JR. & ALBERT M. SACKS, *THE LEGAL PROCESS: BASIC*

Justice Kennedy and four other justices emphasized the text of Section 10(b) and gave virtually no merit to the long history surrounding aiding and abetting in the lower federal courts.<sup>117</sup> For this reason, four Justices dissented.<sup>118</sup> Justice Stevens, writing for the dissent, did not contend that the phrase "directly or indirectly" in Section 10(b) created aiding and abetting liability.<sup>119</sup> Instead, he asserted that the Supreme Court had changed its approach to implied causes of action since Congress enacted the 1934 Act.<sup>120</sup> Justice Stevens argued that Congress passed the 1934 Act against a backdrop of liberal construction of remedial statutes.<sup>121</sup> Additionally, Justice Stevens

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PROBLEMS IN THE MAKING AND APPLICATION OF LAW 1209 (William N. Eskridge, Jr. & Philip P. Frickey eds., 1994) (stating that judicial opinions on interpretation of statutes are full of references and presumptions). Judicial opinions that reference presumptions, or suggest the existence of presumptions, amount to policies of clear statement. *Id.* In effect, these presumptions all say to the legislature, "[I]f you mean *this*, you must say so plainly." *Id.*, see also *infra* notes 223-31 and accompanying text (discussing message to Congress about future statutes); cf. *New York State Dep't of Social Servs. v. Dublino*, 413 U.S. 405, 431 (1973) (Marshall, J., dissenting). In *Dublino*, Justice Marshall stated that the policy of clear statement serves a useful purpose: It informs legislators that if they wish to alter the accommodations, they must clearly indicate that wish. *Id.* Justice Marshall reasoned that lawmakers will only clearly indicate their intent if the Court regularly adheres to the clear statement policy. *Id.* See generally William V. Luneberg, *Justice Rehnquist, Statutory Interpretation, the Policies of Clear Statement, and Federal Jurisdiction*, 58 IND. L.J. 211 (1982) (discussing clear statement requirement and its role in statutory interpretation).

117. *Central Bank*, 114 S. Ct. at 1442. Chief Justice Rehnquist and Justices O'Connor, Scalia, and Thomas joined Justice Kennedy's opinion.

118. *Id.* Justices Blackmun, Souter, and Ginsberg joined Justice Stevens's dissent.

119. See *id.* at 114 S. Ct. at 1455-60 (Stevens, J., dissenting) (making no assertion that § 10(b)'s phrase "directly or indirectly" encompasses aiding and abetting behavior).

120. *Id.* at 1457 (Stevens, J., dissenting). Justice Stevens noted that at the time Congress passed the 1934 Act, courts had adopted common-law presumptions that a statute enacted for the benefit of a particular class conferred on members of that class the right to sue violators of that statute. *Id.* Justice Stevens cited *Piedmont & Northern Co. v. ICC*, 286 U.S. 299, 311 (1932), for the proposition that just before Congress passed the 1934 Act, the Supreme Court had stated that remedial legislation should receive a broader and more liberal interpretation than the mere dictionary definitions of the words employed by Congress. *Central Bank*, 114 S. Ct. at 1457.

121. *Central Bank*, 114 S. Ct. at 1457. Justice Stevens implied that the Supreme Court's statutory interpretation of remedial statutes during the period in which Congress passed the 1934 Act formed part of the legal framework under which Congress operated when it wrote the statute. *Id.*, see Luneberg, *supra* note 116, at 253-54 (noting that Court should consider legal context that existed when Congress enacted statute when Court is trying to determine statute's meaning); see also REED DICKERSON, *THE INTERPRETATION AND APPLICATION OF STATUTES* (1975). When discussing the general concept of meaning, Dickerson posed the insightful question of whether the interpreter should determine meaning by looking from the point of view of the lawmakers or from a member of the audience to whom the lawmakers



pointed to the broad and long-standing acceptance of the aiding and abetting claim in the lower federal courts and concluded that courts and individuals had solidified the private cause of action against aiders and abettors within the statutory scheme.<sup>122</sup> As a result, Justice Stevens took an opposite approach from the majority's position. The majority maintained that Congress had to state specifically its intent if it wanted to permit plaintiffs to bring a claim for aiding and abetting under Section 10(b).<sup>123</sup> Justice Stevens argued that courts should continue to imply a cause of action for aiding and abetting unless Congress specifically stated otherwise.<sup>124</sup>

### III. The Central Bank Effect

In the immediate aftermath of *Central Bank*, a large number of lower courts have dismissed aiding and abetting claims.<sup>125</sup> The Supreme Court's

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addressed the statute. *Id.* at 36. Dickerson noted that the reader should consider the intentions of the author (lawmakers) because otherwise the process of communication makes no sense. *Id.*, see also RONALD DWORKIN, *LAW'S EMPIRE* 338 (1986) (suggesting that courts should not try to reach what courts believe is best substantive result, but rather that courts should construct story of democratically elected legislature enacting text in particular circumstances and that account should justify whole story, not just its ending). These comments lend support to Justice Stevens's assertion that the Court should have considered the legal context surrounding the passage of the 1934 Act.

122. *Central Bank*, 114 S. Ct. at 1458; see William N. Eskridge, Jr., *Overriding Supreme Court Statutory Interpretation Decisions*, 101 YALE L.J. 331, 400 (1991) (noting that Court invokes legislative inaction doctrines mainly when Court finds some indication that there is insufficient support in Congress for overriding contested interpretation); Donna L. Goldstein, Note, *Implied Private Rights of Action Under Federal Statutes: Congressional Intent, Judicial Deference, or Mutual Abdication?*, 50 FORDHAM L. REV. 611, 643 (1982) (asserting that Supreme Court should treat uniform judicial recognition of implied right under statute prior to its amendment as weighing in favor of implication because this encourages courts to adhere to judicial precedent and thus promotes consistency in law).

123. *Central Bank*, 114 S. Ct. at 1448; see *supra* notes 101-05 and accompanying text (discussing Supreme Court's position on what Congress had to do to establish aiding and abetting cause of action under § 10(b)).

124. *Central Bank*, 114 S. Ct. at 1458-59 (Stevens, J., dissenting) (arguing that Congress and not Supreme Court should alter established law surrounding private claim against aiders and abettors under § 10(b)).

125. See, e.g., *Broadview Fin., Inc. v Entech Management Servs. Corp.*, 859 F. Supp. 444, 453 (D. Colo. 1994) (dismissing private cause of action for aiding and abetting based on *Central Bank* holding); *In re Checkers Sec. Litig.*, 858 F. Supp. 1168, 1179 (M.D. Fla. 1994) (same); *Schultz v Rhode Island Hosp. Trust Nat'l Bank*, No. CIV.A.88-2870-JLT, 1994 WL 326376, at \*3 (D. Mass. May 24, 1994) (same); *Greenfield v Shuck*, 856 F. Supp. 705, 711 (D. Mass. 1994) (same). The Supreme Court did not explicitly foreclose the aiding and abetting claim to the SEC; nevertheless, the SEC and lower federal courts have interpreted *Central Bank* as precluding the SEC from pursuing such claims. See *Senate Hearing*,

analysis, however, not only abolishes aiding and abetting under Section 10(b) but also forces lower courts to question seriously whether other forms of secondary liability currently recognized under Section 10(b), such as conspiracy<sup>126</sup> and vicarious liability<sup>127</sup> can survive after *Central Bank*. Additionally, *Central Bank* has seriously undermined lower federal courts' justifications for implying an aiding and abetting cause of action under RICO.<sup>128</sup>

### A. Section 10(b)

#### 1. Conspiracy

##### a. History of Conspiracy in the Lower Federal Courts

In addition to recognizing secondary liability under Section 10(b) based on a claim of aiding and abetting, lower courts have permitted plaintiffs to assert conspiracy claims under Section 10(b).<sup>129</sup> Like the aiding and abetting cause of action, conspiracy has borrowed common-law tort principles.<sup>130</sup> Conspiracy seeks to extend secondary liability to those who have formed an agreement with another and then merely plan, assist, or encourage the active wrongdoer.<sup>131</sup> Conspiracy, as implied under Section 10(b), is a form of

*supra* note 34, at 46 (statement of Arthur Levitt, Chairman, SEC). Chairman Levitt stated that because other enforcement options are available, the SEC would not devote substantial resources to litigate the question of whether *Central Bank* applies to the SEC's enforcement actions. *Id.* Chairman Levitt noted that the SEC would generally refrain from asserting aiding and abetting theories of liability where the statute does not expressly provide for such claims. *Id.*, see SEC v Bilzerian, 29 F.3d 689, 694 n.10 (D.C. Cir. 1994) (questioning whether SEC can pursue aiding and abetting claim in light of *Central Bank*); SEC v Patel, No. 93 CIV 4603, 1994 WL 364089, at \*5 n.1 (S.D.N.Y. July 13, 1994) (dismissing SEC's § 10(b) aiding and abetting claim).

126. See *infra* notes 136-56 and accompanying text (examining *Central Bank*'s impact on conspiracy claims under § 10(b)).

127. See *infra* notes 171-97 and accompanying text (applying *Central Bank* decision to claims based on vicarious liability under § 10(b)).

128. See *infra* notes 204-17 and accompanying text (applying *Central Bank* decision to aiding and abetting cause of action as currently implied under RICO).

129. See, e.g., Dasho v Susquehanna Corp., 380 F.2d 262, 265 (7th Cir.) (alleging defendant joined conspiracy and took steps to assure its success), *cert. denied*, 289 U.S. 977 (1967); Texas Continental Life Ins. Co. v Dunne, 307 F.2d 242, 246 (6th Cir. 1962) (alleging defendants conspired to violate § 10(b)); Eastwood v National Bank of Commerce, 673 F. Supp. 1068, 1079 (W.D. Okla. 1987) (claiming aiding and abetting or conspiracy).

130. See 4 ALAN R. BROMBERG & LEWIS D. LOWENFELS, SECURITIES FRAUD & COMMODITIES FRAUD § 8.5(540) (1970) (noting that conspiracy has tort pedigree that is similar to aiding and abetting).

131. See W PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 46, at 324 (5th ed. 1984) (describing common-law doctrine of conspiracy).

secondary liability because proof of conspiracy imposes liability on a defendant for the agreement made with and assistance given to the primary violator, even if the defendant did not violate the text of Section 10(b).<sup>132</sup>

Because of the elements' similarity, courts have rarely drawn a distinction between conspiracy and aiding and abetting.<sup>133</sup> Courts generally impose 10(b) liability based on a claim of conspiracy if the plaintiff shows that (1) someone other than the alleged conspirator violated the text of Section 10(b), (2) an *agreement* existed between the alleged conspirator and the primary violator to violate Section 10(b), and (3) the alleged conspirator provided the primary violator with substantial assistance in furtherance of the Section 10(b) violation.<sup>134</sup> Because the claim of conspiracy closely resembles that of aiding and abetting, plaintiffs may simply alter their complaints and make claims of conspiracy to compensate for *Central Bank* and the loss of their aiding and abetting claims.<sup>135</sup> The *Central Bank* decision, however, should result in the dismissal not only of aiding and abetting claims but also of conspiracy claims.

132. See *id.* (noting that conspiracy is form of secondary liability because mere agreement to do wrong act is not enough alone to amount to tort; one of the parties in agreement must commit tortious act).

133. See 9 LOUIS LOSS & JOEL SELIGMAN, SECURITIES REGULATION 4489-90 (3d ed. 1992) (noting that recent court decisions have characterized conspiracy and aiding and abetting as requiring same scienter); Kuehnle, *supra* note 21, at 321 (commenting that in civil tort law, general concept of joint tortfeasor liability encompasses both aiding and abetting and conspiracy); Ruder, *supra* note 23, at 639 (explaining that securities cases have not clearly distinguished between charges that secondary defendant aided and abetted another person in achieving an unlawful result and charges that secondary defendant conspired to help another accomplish that unlawful result). In fact, the first case that established the implied cause of action for aiding and abetting also used conspiracy language to sustain the complaint against the company with which the defendants had negotiated a sale of assets. See *Kardon v National Gypsum Co.*, 69 F Supp. 512, 514 (E.D. Pa. 1946) (using conspiracy and aiding and abetting language when creating secondary liability in defendant).

134. See *Bresson v Thomson McKinnon Sec. Inc.*, 641 F Supp. 338, 348 (S.D.N.Y. 1986) (outlining elements of conspiracy claim); *Kronfeld v First Jersey Nat'l Bank*, 638 F Supp. 1454, 1468-70 (D.N.J. 1986) (same); *Hill v Equitable Bank*, 599 F Supp. 1062, 1083 (D. Del. 1984) (same).

135. Compare *supra* note 134 and accompanying text (outlining elements of conspiracy under § 10(b)) with *supra* notes 31-32 and accompanying text (outlining elements of aiding and abetting under § 10(b)); see also *Halberstam v Welch*, 705 F.2d 472, 477 (D.C. Cir. 1983) (distinguishing conspiracy from aiding and abetting); *Decker v Massey-Ferguson, Ltd.*, 681 F.2d 111, 119 (2d Cir. 1982) (noting that outside director may be liable as aider and abettor or conspirator), *cert. denied*, 459 U.S. 1178 (1983); *Eastwood v National Bank of Commerce*, 673 F Supp. 1068, 1079 (W.D. Okla. 1987) (treating aider and abettor and conspirator liability as essentially the same).

*b. Applying Central Bank to Conspiracy Claims*

Past Supreme Court decisions suggest that the Court sanctions conspiracy claims.<sup>136</sup> The Supreme Court's makeup, however, changed markedly between the last approving reference to secondary liability in *Herman & MacLean v Huddleston*<sup>137</sup> and *Central Bank*.<sup>138</sup> As *Central Bank* makes

136. See *Herman & MacLean v Huddleston*, 459 U.S. 375, 379 n.5 (1983) (using language that suggests Court's approval of conspiracy claim under § 10(b)); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v Curran*, 456 U.S. 353, 394 (1982) (noting that it necessarily follows that those who participate in conspiracy to manipulate market are also subject to suit in addition to primary violators); see also *Kuehnle*, *supra* note 21, at 317 (noting that Supreme Court has made references that suggest that participants in conspiracy may be subject to suit under securities laws).

137 459 U.S. 375 (1983).

138. See *Herman & MacLean v Huddleston*, 459 U.S. 375, 379 n.5 (1983) (reserving question of whether cause of action for aiding and abetting existed under § 10(b), but citing *Curran* in way that one could plausibly infer that such cause existed under § 10(b)). The *Huddleston* Court addressed two unrelated questions concerning § 10(b). *Id.* at 377 First, the Court considered whether purchasers of registered securities who allege that defendants defrauded them through misrepresentations in a registration statement may maintain an action under § 10(b) even though § 11, 15 U.S.C. § 77k (1988), of the 1933 Act provides an expressed remedy for that action. *Huddleston*, 459 U.S. at 377 Second, the Court addressed whether persons seeking recovery under § 10(b) had to prove their cause of action by clear and convincing evidence rather than by a preponderance of the evidence. *Id.* In 1969, Texas International Speedway, Inc. (TIS) filed a registration statement and prospectus with the SEC offering \$4,398,900 in securities to the public. *Id.* TIS planned to use the proceeds to finance the construction of a speedway. *Id.* TIS was not successful and filed a petition for bankruptcy in 1970. *Id.* Purchasers of the securities instituted a class action suit. *Id.* at 378. Plaintiffs sued the accounting firm, Herman and MacLean, among others and alleged that defendants violated § 10(b) when defendants engaged in a fraudulent scheme to misrepresent or conceal material facts regarding the financial conditions of TIS. *Id.* at 378. The Court analyzed the purposes of the provisions under the 1933 Act and the 1934 Act and concluded that § 11 of the 1933 Act and § 10(b) of the 1934 Act address different types of wrongdoing. *Id.* at 380-82. The Court, therefore, stated that it saw no reason to carve out an exception to § 10(b) for fraud occurring in a registration statement just because the same conduct is also actionable under § 11 of the 1933 Act. *Id.* at 382-83. Next, the Court noted that in typical suits for money damages plaintiffs must prove their case by a preponderance of the evidence. *Id.* at 387 The Court acknowledged that because courts had implied the cause of action under § 10(b), Congress had obviously not prescribed the appropriate standard of proof. *Id.* at 389. The Court noted that in the absence of a prescribed standard of proof, the Court must provide one. *Id.* The Court noted that a preponderance-of-the-evidence standard allowed both parties to share the risk of error in roughly equal fashion. *Id.* at 390. The Court weighed the interests of both defendants and plaintiffs in a securities case and concluded that because defrauded investors were among the individuals Congress sought to protect, investors who could prove it was more likely than not that defendants violated § 10(b) could recover money damages. *Id.*

When the Court decided *Merrill Lynch, Pierce, Fenner & Smith, Inc. v Curran*, 456

clear, the Court's current members appear more concerned with the text of the securities laws and less concerned with the broad policy reasons underlying the passage of those statutes.<sup>139</sup> In *Central Bank*, the Court first analyzed the text of Section 10(b).<sup>140</sup> The Court stated that the problem with aiding and abetting under Section 10(b) was the plaintiff's ability to make the defendant liable for a Section 10(b) violation even though the defendant did not engage in activities that Section 10(b)'s text proscribes.<sup>141</sup> The Court presumed that if Congress intended to create aiding and abetting liability, Congress would have used the words "aid" and "abet" in the statutory text.<sup>142</sup>

This logic applies with equal force to a claim of conspiracy. Like an aider and abettor, courts find a conspirator liable for a Section 10(b) violation even if she did not violate the text of the statute.<sup>143</sup> Consequently, courts that imply a cause of action for conspiracy allow plaintiffs to create 10(b) liability for conduct not proscribed by Congress. Using the rationale

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U.S. 353 (1981), Justice Stevens wrote the Court's opinion in which Justices Brennan, White, Marshall, and Blackmun joined. *Id.* at 354. In *Curran*, Justice Powell wrote a dissenting opinion in which Justices Burger, Rehnquist, and O'Connor joined. *Id.* at 395. In the interim between *Curran* and *Central Bank*, Justices Brennan, White, Marshall, Burger, and Powell retired from the bench, while Justices Scalia, Kennedy, Thomas, Souter, and Ginsberg joined. Justice Stevens, who wrote the majority opinion in *Curran* and the dissent in *Central Bank*, and Justice Blackmun, who joined the *Central Bank* dissent, were the only two justices remaining out of the five that made up the *Curran* majority. While Justice Stevens, in *Curran*, interpreted congressional inaction in the face of judicial opinions recognizing an implied right as evidence of congressional feeling on the issue, the dissenters placed more emphasis on determining the intent of Congress when it enacted the Commodity Exchange Act (CEA), 7 U.S.C. §§ 1-26 (1988 & Supp. V 1993). *Curran*, 456 U.S. at 381-82, 394-95, 395-409; see Luneberg, *supra* note 116, at 260-61 (discussing dissenters' position in *Curran*). The *Central Bank* majority's method of statutory interpretation appears more closely aligned with the *Curran* dissent rather than the *Curran* majority. Compare the method of statutory interpretation in *Central Bank*, 114 S. Ct. at 1445-53, with the dissent in *Curran*, 456 U.S. at 395-404 (Powell, J., dissenting).

139. See *supra* notes 101-05 and accompanying text (describing Court's use of clear statement approach in *Central Bank*).

140. See *Central Bank*, 114 S. Ct. at 1447 (commenting that statutory text of § 10(b) controls definition of conduct prohibited by § 10(b)); see also Frankfurter, *supra* note 101, at 535 (commenting that when interpreting statute, judges should initially look to words of that statute).

141. See *Central Bank*, 114 S. Ct. at 1447-48 (rejecting notion that word "indirectly" in § 10(b) reached persons who aid and abet because by definition one could aid and abet without violating expressed provisions).

142. *Id.* at 1448.

143. See *supra* note 134 and accompanying text (describing elements of conspiracy).

of *Central Bank*, if Congress wanted to extend Section 10(b) to include secondary liability based on a theory of conspiracy, Congress would have used the word "conspiracy" in Section 10(b)'s text.<sup>144</sup>

While the Court noted that Section 10(b)'s text resolved the question of whether the Court could imply a cause of action for aiding and abetting,<sup>145</sup> the majority supported the *Central Bank* decision on other fronts. The Court pointed out that Congress had taken a statute-by-statute approach when imposing secondary liability for aiding and abetting.<sup>146</sup> For example, Congress enacted a general aiding and abetting statute applicable to all federal criminal offenses,<sup>147</sup> yet no corollary general civil aiding and abetting statute exists.<sup>148</sup> Consequently, the Court interpreted Congress's actions as a deliberate choice to exclude civil aiding and abetting liability.<sup>149</sup> The Court stated that the judicial branch should respect this congressional choice.<sup>150</sup> Similarly, Congress enacted a general conspiracy statute applicable to all federal criminal offenses,<sup>151</sup> but like the criminal aiding and abetting statute,

144. Cf. *Central Bank*, 114 S. Ct. at 1448 (noting that if Congress wanted to create secondary liability based on aiding and abetting under § 10(b), Congress could have used words "aid" and "abet" in statute).

145. *Id.* at 1448.

146. *Id.* at 1451.

147. See 18 U.S.C. § 2 (1988), which provides:

(a) whoever commits an offense against the United States or aids, abets, counsels, commands, induces or procures its commission, is punishable as a principal.

(b) whoever willfully causes an act to be done which if directly performed by him or another would be an offense against the United States, is punishable as a principal.

148. *Central Bank*, 114 S. Ct. at 1450. The *Central Bank* Court also referred to § 20(a) of the 1934 Act, which imposes controlling person liability, a form of secondary liability, on defendants. *Id.* at 1451-52; see *infra* notes 163-67 and accompanying text (describing § 20(a)). The Court applied the interpretational principle that the expression of one thing implies the exclusion of another and concluded that when Congress wished to create secondary liability, it knew how to and did so. *Id.* at 1452 (citing *Pinter v. Dahl*, 486 U.S. 622, 650 (1988)); see also Goldstein, *supra* note 122, at 648-50 (discussing interpretative principle — congressional expression of one thing means congressional exclusion of another — and congressional silence).

149. *Central Bank*, 114 S. Ct. at 1452.

150. *Id.*, see Note, *Intent, Clear Statements, and the Common Law: Statutory Interpretation in the Supreme Court*, 95 HARV. L. REV. 892, 895-96 (1982) (noting that Court has extended maxim's exclusion-by-implication logic to resolve complex statutory issues and to find that express provision of remedy in one statute signifies congressional intent to exclude that remedy from other statute lacking similar express provision).

151. See 18 U.S.C. § 371 (1988 & Supp. V 1993), which states,

If two or more persons conspire either to commit any offense against the United

it also lacks a civil counterpart. If Congress's choice about aiding and abetting deserves the Court's respect, that same respect should preclude further implication of conspiracy under Section 10(b).

Finally, the *Central Bank* majority opinion noted that litigation in the securities area demands a degree of certainty and predictability.<sup>152</sup> The Court reasoned that expansive undefined liability under Section 10(b) caused secondary actors to incur substantial expenses for pretrial defense and settlements.<sup>153</sup> The Court suggested that professionals would in turn pass these expenses to the company's investors and thereby harm the intended beneficiaries of the statute.<sup>154</sup> The uncertainty surrounding conspiracy appears even greater than the uncertainty surrounding aiding and abetting because an alleged conspirator may be liable for actions that occurred before or after the alleged conspirator joined the conspiracy.<sup>155</sup> Accordingly, each justification given by the Supreme Court in support of the *Central Bank*

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States, or to defraud the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined under this title or imprisoned not more than five years, or both

152. *Central Bank*, 114 S. Ct. at 1454.

153. *Id.*

154. *Id.* at 1454, *see also* Frankel, *supra* note 112, at 570 (suggesting that private compensatory action under securities statutes may actually hamper central purposes of those statutes). Professor Frankel commented that the costs of private enforcement under § 10(b) fell not only on defendants, but also on investors, consumers, and society at large. *Id.* at 577. Frankel reasoned that when a corporation pays a judgment or settlement, the value of the corporation's stock may fall and cost of capital rise. *Id.* Thus, Frankel argued that not only do shareholders lose but the firm's productivity may decline at some cost to society. *Id.* at 577-78. Furthermore, Professor Frankel suggested that the broad scope of liability may deter the issuance of public securities and hinder investment. *Id.* at 578.

155. *See* United States v. Read, 658 F.2d 1225, 1230 (7th Cir. 1981) (noting that even if defendants did not participate in later events of conspiracy, they are still responsible for its actions in furtherance of initial goal); *Herpich v. Wilder*, 430 F.2d 818, 819 (5th Cir. 1970) (holding defendant, who had committed overt acts in furtherance of conspiracy between himself and third parties to violate securities laws, responsible for acts of co-conspirators in furtherance of scheme, although defendant had to some extent departed scene), *cert. denied*, 401 U.S. 947 (1971); *Texas Continental Life Ins. Co. v. Dunne*, 307 F.2d 242, 249 (6th Cir. 1962) (stating that conspiracy did not terminate when bonds were sold but instead stating that fraud permeated and affected entire issue of bonds even though there was no privity between plaintiff and defendants); Frankel, *supra* note 112, at 575 (noting that uncertainty as to existence and magnitude of liability creates powerful incentive for defendant in private securities action to settle claims against him without trial on merits); *cf.* Kuehnle, *supra* note 21, at 344 n.167 (remarking that conspiracy has certain advantages with regard to damages and procedure because under conspiracy rule courts can hold co-conspirator liable for action taken before he joined conspiracy).

decision applies with equal force to conspiracy. Conspiracy claims under Section 10(b), therefore, should fall with their aiding and abetting counterparts.<sup>156</sup>

## 2. Vicarious Liability

### a. History of Vicarious Liability in the Lower Federal Courts

Much like the common-law principles that support the Section 10(b) cause of action for aiding and abetting, common-law tort and agency principles provide the basis for another form of secondary liability — *respondeat superior*, which is a form of vicarious liability.<sup>157</sup> The common law defines vicarious liability as a tort doctrine that allocates loss based on policy considerations.<sup>158</sup> Because an employer derives a benefit from employees, the doctrine of *respondeat superior* maintains that the law should hold the employer liable for the tortious actions of the employees, even if the employer acts without fault.<sup>159</sup> The common-law principles of agency,

156. Some district courts have already taken the lead and dismissed conspiracy claims because of *Central Bank*. See *In re Medimmune, Inc. Sec. Litig.*, 873 F. Supp. 953, 964 (D. Md. 1995); *In re Rasterops Corp. Sec. Litig.*, No. C-93-20349, 1994 WL 618970, at \*4 (N.D. Cal. Oct. 31, 1994).

157. See 2 BROMBERG & LOWENFELS, *supra* note 130, § 5.10(100) (1983) (stating that *respondeat superior* is common-law concept that means that master is liable in certain cases for wrongful acts of servant, and that principal is liable for those of agent); see also Fischel, *supra* note 20, at 86-87 (noting that plaintiffs use common-law theory of *respondeat superior* to create broader liability than that provided by 1934 Act). See generally Jennifer H. Arlen & William J. Carney, *Vicarious Liability For Fraud on Securities Markets: Theory and Evidence*, 1992 U. ILL. L. REV. 691 (1992) (making policy arguments for why *respondeat superior* should not exist); William J. Fitzpatrick & Ronald T. Carman, *Respondeat Superior and the Federal Securities Laws: A Round Peg in a Square Hole*, 12 HOFSTRA L. REV. 1 (1983) (discussing interaction between common-law principles of *respondeat superior* and liability under securities acts); Kuehnle, *supra* note 21, at 348-76 (encouraging courts' use of common-law principles to extend liability to secondary participants in securities violations).

158. See KEETON ET AL., *supra* note 131, § 69, at 500 (discussing policy justifications underlying vicarious liability); Ferrara & Sanger, *supra* note 23, at 1017 (noting that *respondeat superior* represents policy determination to allocate risk of loss to employer, rather than to innocent victim of employee's misconduct, because employer can absorb monetary loss as cost of doing business).

159. See KEETON ET AL., *supra* note 131, § 69, at 499-500. Keeton cited several policy reasons for enforcing the doctrine of vicarious liability. *Id.* at 500. The employer has engaged in a business which will at some time harm others through the torts of her employees. *Id.* The theory is that the employer, rather than the innocent injured plaintiff, should bear the costs of the injury caused by the employee. *Id.* On a more cynical note, Keeton noted that the reason for the employers' liability is so that the plaintiff may recover damages from a deep pocket. (citation omitted) *Id.*, see also Ferrara & Sanger, *supra* note 23, at 1016-17



however, qualify the *respondeat superior* doctrine. The law imposes liability on employers for the employee's tortious act only if the act occurred within the scope of the employee's employment<sup>160</sup> and the employee acted with apparent authority.<sup>161</sup>

Just as the 1934 Act does not expressly create a private cause of action for aiding and abetting, the 1934 Act does not expressly create this common-law form of vicarious liability.<sup>162</sup> Section 20(a) of the 1934 Act, however, does create "controlling person liability," which is itself a form of secondary or vicarious liability.<sup>163</sup> Section 20(a) makes controlling parties jointly and severally liable for the controlled person's violations of the 1934 Act, including violations of Section 10(b).<sup>164</sup> While Section 20(a) creates a form of secondary liability, one important distinction exists between the liability created by Section 20(a) and that created by the common-law

(noting that principal justification underlying *respondeat superior* is that employer hires and controls employee and expects to profit from employee, so employer should bear burden of employee's wrongful conduct); Fitzpatrick & Carman, *supra* note 157, at 27 (reciting various rationales for vicarious liability doctrine including: (1) principal's ability to bear economic loss involved, (2) principal's act of placing agent in position to commit tortious act, and (3) principal's ability to control person or entity that committed tortious act).

160. See RESTATEMENT (SECOND) OF AGENCY § 219 (1958) (stating that master is subject to liability for torts of servant committed while acting in scope of servant's employment).

161. See *id.* § 265 (stating that master or other principal is subject to liability for torts that result from reliance upon, or belief in, statements or other conduct within agent's apparent authority).

162. See generally Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78ll (1988 & Supp. V 1993) (including no provision that creates aiding and abetting or strict vicarious liability).

163. See the Securities Exchange Act of 1934 § 20(a), 15 U.S.C. § 78t(a) (1988), which provides:

Every person who, directly or indirectly, controls any person liable under any provision of this chapter or of any rule or regulation thereunder 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 acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or cause of action.

See also 2 BROMBERG & LOWENFELS, *supra* note 130, § 5.10(100) (stating that two legal theories exist under which courts may hold employers vicariously or secondarily liable for legal violations of their employees under federal securities law: *respondeat superior* and controlling person); Fischel, *supra* note 20, at 86 (noting that § 20(a) imposes liability on controlling persons who control *primary* wrongdoer).

164. See Ferrara & Sanger, *supra* note 23, at 1007-08 n.4 (noting that § 20(a) includes secondary liability for violations of broad antifraud provision of § 10(b)); see also *supra* note 14 (providing text of § 10(b)).

doctrine of *respondeat superior*<sup>165</sup> Section 20(a) expressly provides relief from liability when the controlling person shows he acted in good faith.<sup>166</sup> In contrast, common-law agency principles do not relieve the principal from liability even when the principal acted in good faith.<sup>167</sup>

Although Section 20(a) provides a good-faith safe harbor for controlling persons who would otherwise be vicariously liable for the controlled person's violations of the 1934 Act, eight circuits have concluded that Section 20(a) does not preclude courts from recognizing liability based on the common-law doctrine of *respondeat superior*<sup>168</sup> Another circuit has

165. See Kuehnle, *supra* note 21, at 349 (recognizing similarity between coverage of agent-principal relationship and controlling person provision, but noting that controlling person provision provides for expressed relief from liability in situations where liability based on agent-principal relationship does not).

166. See *supra* note 163 (providing relevant text of § 20(a)); see also Ferrara & Sanger, *supra* note 23, at 1012 (commenting that defendant can avoid liability under § 20(a) if defendant shows that she acted in good faith and did not directly or indirectly engage in acts constituting violations); Fischel, *supra* note 20, at 86 (commenting that § 20(a)'s good-faith defense shields person from liability if that person exercised reasonable internal supervision against securities violation).

167. See *Jackson v Bache & Co.*, 381 F. Supp. 71, 94 (N.D. Cal. 1974) (noting that agency principles of *respondeat superior* differ significantly from § 20(a) liability because once plaintiff establishes appropriate agency relationship, liability on part of principal is absolute — no good-faith defense is available); Fitzpatrick & Carman, *supra* note 157, at 11 (noting that § 20(a)'s good-faith defense becomes irrelevant when courts apply common-law theory of *respondeat superior* because employer incurs liability for actions of employee if action occurred within scope of employee's employment); Gottesman, *supra* note 23, at 185-86 (noting that agency law imposes personal liability on innocent principal because *respondeat superior* theory distributes loss based on commercial and social policy justifications). Compare *supra* note 163 (providing text of § 20(a)) with *supra* notes 160-61 (reciting agency principles).

168. See *Hollinger v Titan Capital Corp.*, 914 F.2d 1564, 1577-78 (9th Cir. 1990) (affirming applicability of common-law vicarious liability for suits under Securities Acts), *cert. denied*, 499 U.S. 976 (1991); *In re Atlantic Fin. Management, Inc.*, 784 F.2d 29, 32-34 (1st Cir. 1986) (providing reasons for concluding that § 20(a) does not preclude imposition of common-law vicarious liability), *cert. denied*, 481 U.S. 1072 (1987); *Commerford v Olson*, 794 F.2d 1319, 1323 (8th Cir. 1986) (concluding that Congress did not mean § 20(a) to narrow defenses to cases otherwise governed by traditional agency principles); *Henrickson v. Henrickson*, 640 F.2d 880, 887 (7th Cir.) (noting that doctrine of *respondeat superior* was independent of and potentially broader than § 20(a) liability), *cert. denied*, 454 U.S. 1097 (1981); *Paul F. Newton & Co. v. Texas Commerce Bank*, 630 F.2d 1111, 1119 (5th Cir. 1980) (concluding that *respondeat superior* remains viable in actions brought under 1934 Act and provides means of imposing secondary liability for violations of 1934 Act independent of § 20(a)); *Marbury Management, Inc. v. Kohn*, 629 F.2d 705, 716 (2d Cir.) (noting that when *respondeat superior* principles apply, special good-faith defense afforded by last clause of § 20(a) is unavailable), *cert. denied*, 449 U.S. 1011 (1980); *Holloway v. Howerdd*, 536

applied the more encompassing common-law theory of *respondeat superior* but has failed to address its relationship to Section 20(a).<sup>169</sup> Only two circuits question the availability of the common-law theory of *respondeat superior* because of Section 20(a)'s good-faith defense.<sup>170</sup>

### *b Applying Central Bank to Vicarious Liability*

When the Court decided that an implied cause of action for aiding and abetting did not exist under Section 10(b), the Court focused solely on Section 10(b)'s text.<sup>171</sup> Because aiding and abetting was outside the con-

F.2d 690, 695 (6th Cir. 1976) (contending that Congress did not intend Securities Acts to preempt doctrine of *respondeat superior* in cases involving unlawful activities by brokerage firm's employees).

Congress carved the Eleventh Circuit out of the Fifth Circuit on October 1, 1981. Fifth Circuit Court of Appeals Reorganization Act of 1980, Pub. L. No. 96-452, 94 Stat. 1994. In *Bonner v. City of Prichard*, 661 F.2d 1206 (11th Cir. 1981), the Eleventh Circuit held that decisions of the Fifth Circuit decided before October 1, 1981 are binding precedent. *Id.* at 1207. Therefore, while the Eleventh Circuit has not had an opportunity to address this issue, according to *Bonner*, the Fifth Circuit's decision in *Paul F. Newton & Co.* is binding.

169. See *Kerbs v. Fall River Indus.*, 502 F.2d 731, 740-41 (10th Cir. 1974) (extending liability to Fall River Industries for actions of company president because president was acting within scope of his apparent authority when he violated § 10(b)).

170. See *Rochez Bros. v. Rhoades*, 527 F.2d 880, 884-85 (3d Cir. 1975) (stating that legislative history of § 20(a) and § 20(a)'s good-faith defense illustrate that Congress intended defendant's liability to derive from something besides control, like culpable participation), *cert. denied*, 425 U.S. 993 (1976). The Third Circuit applies the general rule that § 20(a) limits employer liability, but has been willing to make exceptions. See *Sharp v. Coopers & Lybrand*, 649 F.2d 175, 181 (3d Cir. 1981) (permitting exceptions to general prohibition against vicarious liability for accounting firms that render investment oriented opinion letters), *cert. denied*, 455 U.S. 938 (1982).

Two lines of authority exist in the Fourth Circuit. See 2 BROMBERG & LOWENFELS, *supra* note 130, § 5.10(230)(3) (commenting that there are two lines of authority in Fourth Circuit). In one case, the Fourth Circuit concluded that the 1934 Congress intended to impose liability only on those who fall within § 20(a)'s definition of control and not on those defendants whom plaintiffs could reach only with a claim based on common-law vicarious liability. *Carpenter v. Harris, Upham & Co.*, 594 F.2d 388, 394 (4th Cir.) (concluding that § 20(a)'s history demonstrated that Congress had rejected insurer's liability standard for controlling persons), *cert. denied*, 444 U.S. 868 (1979). The Fourth Circuit made this decision, however, without overruling two earlier Fourth Circuit cases that recognized common-law vicarious liability. See *Carras v. Burns*, 516 F.2d 251, 260-61 (4th Cir. 1975) (noting that well-settled principles of agency supported claim of vicarious liability); *Johns Hopkins Univ. v. Hutton*, 422 F.2d 1124, 1130 (4th Cir. 1970) (stating that Congress did not intend § 15 of 1933 Act (which is analogous to § 20 of 1934 Act) to insulate employers from tort and agency principles of liability for misdeeds of employees), *cert. denied*, 416 U.S. 916 (1974).

171. See *Central Bank*, 114 S. Ct. at 1446 (beginning analysis with text of statute); see

duct expressly proscribed by the text of Section 10(b), the Court refused to imply a cause of action for that conduct.<sup>172</sup> Nothing in the *Central Bank* decision suggests that the Court intended to limit this strict textual approach to the aiding and abetting claim. Consequently, the decision may force lower courts to apply the same strict analysis to all implied causes of action that extend liability to conduct beyond that proscribed by the text of the statute.

Lower courts must confront the question of whether *Central Bank* limits plaintiffs to the confines of Section 20(a) or whether, instead, plaintiffs may still reach secondary defendants with the implied common-law doctrine of *respondeat superior*.<sup>173</sup> The common-law doctrine of *respondeat superior* potentially imposes liability on a defendant for a broader range of conduct than Section 20(a) because defendants in a common-law action cannot rely on Section 20(a)'s good-faith defense.<sup>174</sup> For example, a majority of circuits allow a plaintiff to pursue the common-law claim of vicarious liability and hold a controlling person vicariously liable for the controlled person's violation of Section 10(b).<sup>175</sup> This is so even if the controlling person had a good-

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also Frankfurter, *supra* note 101, at 535 (noting that statutory interpretation should begin with analysis of text).

172. See *Central Bank*, 114 S. Ct. at 1447-48 (commenting that § 10(b)'s phrase "directly or indirectly" does not encompass aiding and abetting conduct).

173. See *supra* notes 163-67 and accompanying text (discussing text of and liability under § 20(a)).

174. See Fischel, *supra* note 20, at 86 (recommending that to preclude employers from relying on § 20(a)'s good-faith defense, plaintiffs sue defendants under § 10(b) using theory of *respondeat superior*); Fitzpatrick & Carman, *supra* note 157, at 2 (noting that when firm faces § 10(b) fraud claim and demonstrates good-faith defense in accordance with § 20(a), imposing liability under *respondeat superior* effectively nullifies exculpatory provisions of § 20(a)).

175. See, e.g., *Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1577-78 (9th Cir. 1990) (affirming applicability of vicarious liability for suits under Securities Acts), *cert. denied*, 499 U.S. 976 (1991); *Commerford v. Olson*, 794 F.2d 1319, 1323 (8th Cir. 1986) (agreeing with other circuits that Congress did not intend § 20(a) to narrow defenses to cases otherwise governed by traditional agency principles); *In re Atlantic Fin. Management, Inc.*, 784 F.2d 29, 32-34 (1st Cir. 1986) (concluding that § 20(a) does not preclude imposition of common-law vicarious liability), *cert. denied*, 481 U.S. 1072 (1987); *Henrickson v. Henrickson*, 640 F.2d 880, 887 (7th Cir.) (noting that doctrine of *respondeat superior* was independent of and potentially broader than § 20(a) liability), *cert. denied*, 454 U.S. 1097 (1981); *Paul F. Newton & Co. v. Texas Commerce Bank*, 630 F.2d 1111, 1119 (5th Cir. 1980) (concluding that *respondeat superior* remains viable in actions brought under 1934 Act and provides means of imposing secondary liability for violations of Act independent of § 20(a)); *Marbury Management, Inc., v. Kohn*, 629 F.2d 705, 716 (2d Cir.) (noting that when *respondeat superior* principles apply, special good-faith defense afforded by last clause of § 20(a) is

faith defense and hence Section 20(a)'s good-faith provision would seem to provide immunity.<sup>176</sup> Thus, an implied cause of action under the common-law doctrine of *respondeat superior* allows a plaintiff to hold a defendant liable even though neither Section 10(b) nor Section 20(a) encompasses the defendant's conduct. A textual analysis similar to that performed by the Court in *Central Bank* strongly suggests that courts should no longer impose vicarious liability when the defendant presents a good-faith defense.<sup>177</sup> Otherwise, defendants would face liability for conduct not expressly proscribed by Congress — exactly the result *Central Bank* rejected.<sup>178</sup>

Although the Court in *Central Bank* based its decision on the statutory text, the Court noted that had the text not resolved the issue, the Court would have attempted to determine how the 1934 Congress would have addressed the issue.<sup>179</sup> Examining the legislative history and comparing the provision in question with other provisions passed at the time presents one way to determine the intent of the enacting Congress.<sup>180</sup> Section 20(a) is closely linked to another controlling person provision — Section 15 of the 1933 Act.<sup>181</sup> When Congress enacted Section 15 in 1933, that section

unavailable), *cert. denied*, 449 U.S. 1011 (1980).

176. See Gottesman, *supra* note 23, at 187 (noting that if courts import *respondeat superior* doctrine to determine liability under securities laws, courts impose liability for employees' securities law violations without regard to good-faith defenses).

177. See *Central Bank*, 114 S. Ct. at 1446-48 (analyzing text of § 10(b) and determining that Congress did not intend to include aiding and abetting liability under that text).

178. See *id.* at 1448 (rejecting aiding and abetting claim because it encompassed conduct broader than text of § 10(b)). But see *American Tel. & Tel. Co. v. Winback & Conserve Program, Inc.*, 42 F.3d 1421, 1430-31 (3d Cir. 1994) (suggesting that basing liability on agency theories is not expanding category of affirmative conduct proscribed by relevant statute, instead it is deciding on whose shoulders to place responsibility for conduct indisputably proscribed by relevant statute), *cert. denied*, 115 S. Ct. 1838 (1995); Patrick J. McNulty, *Central Bank of Denver v. First Interstate Bank of Denver: The End of Aiding and Abetting Liability Under Section 10(b)*, 29 TORT & INS. L.J. 847, 858 (1994) (noting that *respondeat superior* is legal maxim for imposing liability on one based on one's legal relationship to another who has committed violation of certain rule and therefore *respondeat superior* does not involve determination of breadth of prohibited conduct).

179. *Central Bank*, 114 S. Ct. at 1448; see *supra* note 105 (describing additional rationale provided by Court in support of its decision in *Central Bank*).

180. See *Central Bank*, 114 S. Ct. at 1448-50 (analyzing other provisions in 1934 Act in effort to support Court's position that 1934 Congress did not intend for § 10(b) to include aiding and abetting liability); Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson, 501 U.S. 350, 359 (1991) (noting that Court can receive clear indication of how Congress would handle policy considerations by looking at same Congress's actions in similar and related provisions).

181. Securities Act of 1933 § 15, 15 U.S.C. § 77o (1988); see Ferrara & Sanger, *supra*

contained no defense to liability and therefore resembled the common-law theory of strict vicarious liability.<sup>182</sup> In 1934, Congress amended Section 15 to include a good-faith defense.<sup>183</sup> Congress simultaneously adopted Section 20(a), which also contained a good-faith defense.<sup>184</sup>

In rejecting the notion that secondary liability existed under the theory of aiding and abetting, the Supreme Court referred to Section 20(a) of the 1934 Act.<sup>185</sup> The Court noted that the imposition of liability on controlling persons was a form of secondary liability.<sup>186</sup> Thus, the Court concluded that the 1934 Congress had the skill and experience to create secondary liability at will.<sup>187</sup> When discussing Congress's intent with regard to the *respondeat superior* doctrine, one could draw a similar analogy between Section 15, as originally enacted,<sup>188</sup> and the amended Section 15<sup>189</sup> and Section 20(a).<sup>190</sup> That is, Congress had the skill and experience to impose strict vicarious liability, but chose in the alternative to alter this liability by adding the good-faith defense.<sup>191</sup> Thus, as the Court stated in *Central*

note 23, at 1009 (noting that Congress modeled § 20(a) on § 15 and that courts tend to interpret these sections analogously); Fischel, *supra* note 20, at 86 (stating that § 15 of 1933 Act and § 20(a) of 1934 Act each impose liability on persons who control primary wrongdoer); Fitzpatrick & Carman, *supra* note 157, at 23 (noting that congressional intent underlying § 15 of 1933 Act was equally relevant in interpreting legislative intent underlying § 20(a) of 1934 Act).

182. See Securities Act of 1933, Pub. L. No. 22, § 15, 48 Stat. 74, 84 (1934) (including no defense to controlling person liability); Fitzpatrick & Carmen, *supra* note 157, at 23 (noting that Congress originally enacted § 15 without "good-faith defense" clause).

183. Securities Act of 1933, Pub. L. No. 22, § 15, 48 Stat. 74, 84 (1933), as amended by Securities Exchange Act of 1934, Pub. L. No. 291, § 208, 48 Stat. 881, 908 (1934) (codified as amended at 15 U.S.C. § 77o (1988)).

184. See *supra* note 163 (providing text of § 20(a)); see also S. REP. NO. 792, 73d Cong., 2d Sess. 22 (1934) (including good-faith defense in § 20(a)); H.R. REP. NO. 1838, 73d Cong., 2d Sess. 42 (1934) (same).

185. *Central Bank*, 114 S. Ct. at 1451-52.

186. *Id.*

187. *Id.* at 1452 (citing *Touche Ross & Co. v. Redington*, 442 U.S. 560, 572 (1979)).

188. Securities Act of 1933, Pub. L. No. 22, § 15, 48 Stat. 74, 84.

189. Securities Act of 1933, Pub. L. No. 22, § 15, 48 Stat. 74, 84, as amended by Securities Exchange Act of 1934, Pub. L. No. 291, § 208, 48 Stat. 881, 908 (codified as amended at 15 U.S.C. § 77o (1988)).

190. See *supra* note 163 (providing text of § 20(a)).

191. See 2 BROMBERG & LOWENFELS, *supra* note 130, § 5.10(220) (stating that courts have interpreted legislative history and text of §§ 15 and 20(a) in different ways in course of dealing with coexistence or preemption in context of common-law secondary or vicarious liability under federal securities laws). Compare Fischel, *supra* note 20, at 86-87 (noting that courts that impose strict vicarious liability under *respondeat superior* theory effectively elim-

*Bank*, this deliberate congressional choice deserves the respect of the judiciary<sup>192</sup>

Some commentators disagree with this interpretation of the legislative history underlying Sections 15 and 20(a).<sup>193</sup> The general argument against the conclusion that Sections 15 and 20(a) preempt common-law vicarious liability is that from a policy standpoint, the 1934 Congress could not have intended to create liability that was narrower than that which existed at common law.<sup>194</sup> This policy argument is persuasive but becomes irrelevant when the Court adheres to a strict textual analysis like that employed in

imate good-faith defense provided by statute) and Fitzpatrick & Carman, *supra* note 157, at 22-23 (acknowledging that legislative history of controlling person provisions does not directly provide insight into whether Congress intended *respondeat superior* to be supplement to controlling provisions of federal securities laws, but placing emphasis on fact that Congress originally enacted § 15 without good-faith defense and then added good-faith defense to §§ 15 and 20 and thus asserting that Congress intended to restrict scope of liability, not expand it) with Ferrara & Sanger, *supra* note 23, at 1015 (commenting that Congress enacted §§ 15 and 20(a) against background of existing common law and asserting that Congress therefore did not intend federal securities laws to replace existing law) and Gottesman, *supra* note 23, at 202 (stating that § 20(a) assumed degree of fault on part of controlling person and simply provided defense to shield controlling person from liability when he was without fault, but suggesting that that did not compel conclusion that Congress designed control provisions to preempt all other theories for imputation of common-law liability) and Kuehnle, *supra* note 21, at 351-54 (asserting that legislative history of controlling person provisions does not support reading of restrictions on agency liability).

192. See *Central Bank*, 114 S. Ct. at 1451-52 (pointing to § 20(a) and noting fact that Congress chose to impose forms of secondary liability in some contexts and not in others, which indicates deliberate congressional choice with which courts should not interfere).

193. See *infra* note 194 (summarizing commentators' arguments in opposition to conclusion that controlling person provisions preempt common-law liability).

194. See 9 LOSS & SELIGMAN, *supra* note 133, at 4477 (interpreting §§ 15 and 20(a) and concluding that Congress intended for these provisions to extend liability beyond that recognized at common law); Gottesman, *supra* note 23, at 202 (asserting that interpretation of §§ 15 and 20(a) as preempting common-law liability would run counter to principle that Congress designed securities laws to complement common-law liability); Kuehnle, *supra* note 21, at 353 (asserting that because nothing in language of controlling person provisions excludes agency liability or applies affirmative defense to agency liability, proponents of exclusion have burden of showing congressional intent not expressed in plain language). Kuehnle's analysis, however, is counter to that asserted by the Court in *Central Bank*. Kuehnle infers that because Congress did not explicitly limit common-law liability, Congress did not intend to restrict the common-law remedies available. *Id.* at 253-54. The *Central Bank* Court, on the other hand, focused not on congressional silence with regard to aiding and abetting under § 10(b) but instead focused on the fact that Congress, when it enacted § 10(b), did not explicitly create aiding and abetting liability. *Central Bank*, 114 S. Ct. at 1448 (emphasis added).

*Central Bank*,<sup>195</sup> indeed, the *Central Bank* Court acknowledged that imposing civil liability for aiding and abetting might be good policy.<sup>196</sup> But the issue was not whether implying a cause of action constituted a good or bad policy; the issue was whether the text of Section 10(b) explicitly created liability for aiding and abetting.<sup>197</sup> Consequently, despite the policy arguments that may exist to the contrary, the Court's method of statutory interpretation suggests that actions based on common-law vicarious liability should no longer exist when the defendant is able to comply with Section 20(a)'s good-faith defense.

## *B. Aiding and Abetting Under RICO*

### *1. RICO and the Lower Federal Courts*

In 1970, Congress enacted RICO<sup>198</sup> to curb the infiltration of organized crime into legitimate businesses.<sup>199</sup> RICO is relevant to securities law because plaintiffs frequently add a civil RICO claim to their complaints when filing federal and state securities fraud suits.<sup>200</sup> Like Section 10(b), Section

195. See *supra* notes 101-05 and accompanying text (discussing Supreme Court's strict adherence to § 10(b)'s text in determining whether Congress intended to encompass aiding and abetting liability under § 10(b)).

196. *Central Bank*, 114 S. Ct. at 1448.

197. *Id.* Additionally, in *Central Bank*, the SEC, as amicus curiae, contended that numerous policy arguments existed in favor of implying an aiding and abetting cause of action under § 10(b). *Id.* at 1453. Notably, the SEC urged that the 1934 Act needed such a cause of action to ensure that the Act made the defrauded plaintiffs whole. *Id.* The Court dismissed the SEC's policy arguments and noted contrary policy arguments of its own. *Id.* at 1453-54. The Court reasoned that because far-reaching liability increases costs, implying secondary liability may actually perform a disservice to the goals of fair dealing and efficiency in the securities markets. *Id.* at 1454; see Frankel, *supra* note 112, at 578 (commenting that broad scope of liability may deter issuance of public securities and hinder investment). Vicarious liability also rests on the policy that courts should make injured persons whole. See KEETON ET AL., *supra* note 131, § 69, at 500 (noting that vicarious liability rests on presumption that innocent employer should bear costs as opposed to innocent injured plaintiff); Gottesman, *supra* note 23, at 186 (commenting that courts allocate liability under *respondeat superior* because distribution of loss is commercially and socially reasonable). Consequently, *Central Bank*'s rejection of the SEC's policy argument strikes at the foundation supporting strict common-law vicarious liability.

198. 18 U.S.C. §§ 1961-1968 (1988) (enacted as Title IX of the Organized Crime Control Act of 1970, Pub. L. No. 91-452, 84 Stat. 922, 941-48).

199. See generally Statement of Findings and Purpose of the Organized Crime Control Act of 1970, Pub. L. No. 91-452, 84 Stat. 922, 922-23 (stating that among other effects, organized crime had infiltrated and corrupted legitimate businesses).

200. See, e.g., *Reves v. Ernst & Young*, 113 S. Ct. 1163, 1168 (1993) (asserting both



1962 of RICO uses the words "directly and indirectly" to describe the scope of prohibited conduct.<sup>201</sup> Just as lower federal courts used criminal and tort common-law principles to increase the liability under Section 10(b), courts have used these same principles to increase significantly the number of persons subject to civil RICO liability.<sup>202</sup> The Court's method of statutory

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securities law violations and claims based on civil RICO); *Craighead v. E.F. Hutton & Co.*, 899 F.2d 485, 493-94 (6th Cir. 1990) (same); *Moss v. Morgan Stanley Inc.*, 719 F.2d 5, 18 n.13 (2d Cir. 1983) (noting that plaintiffs may bring garden-variety securities fraud claims under civil RICO), *cert. denied*, 465 U.S. 1025 (1984); *Knight v. E.F. Hutton & Co.*, 750 F. Supp. 1109, 1111 (M.D. Fla. 1990) (asserting both securities law violations and claims based on civil RICO); *Pincetich v. Jeanfreau*, 699 F. Supp. 1469, 1472 (D. Or. 1988) (same); *Hybert v. Shearson Lehman/Am. Express Inc.*, 688 F. Supp. 320, 323 (N.D. Ill. 1988) (same); *see also* Arthur F. Mathews, *Shifting the Burden of Losses in the Securities Markets: The Role of Civil RICO in Securities Litigation*, 65 NOTRE DAME L. REV. 896, 897-98 (1990) (commenting that RICO is becoming alternative statute of choice to federal securities statutes as plaintiffs search for "deep pockets"); Mark S. Poker, *Reaching a Deep Pocket Under the Racketeer Influenced and Corrupt Organizations Act*, 72 MARQ. L. REV. 511, 512 (1989) (noting that major source of RICO claims originate from common business and financial relationships); Diane L. Virzera, *Redirecting the Debate on "Garden Variety" Abuses of Civil RICO: Suitability Rule Violations and the Case for Treble Damages*, 26 COLUM. J.L. & SOC. PROBS. 341, 341-43 (1993) (describing rise of RICO claims in securities suits).

201. See § 1962 of RICO which states:

(a) It shall be unlawful for any person who has received any income derived, *directly or indirectly*, from a pattern of racketeering activity or through collection of an unlawful debt in which such person has participated as a principal within the meaning of section 2, title 18, United States Code, to use or invest, directly or indirectly, any part of such income, or the proceeds of such income, in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce

(b) It shall be unlawful for any person through a pattern of racketeering activity or through collection of an unlawful debt to acquire or maintain, *directly or indirectly*, any interest in or control of any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce.

(c) It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, *directly or indirectly*, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

(d) It shall be unlawful for any person to conspire to violate any of the provisions of subsection (a), (b) or (c) of this section.

18 U.S.C. § 1962 (1988) (emphasis added).

202. *See, e.g.*, *Cox v. Administrator U.S. Steel & Carnegie*, 17 F.3d 1386, 1410 (11th Cir. 1994) (recognizing civil RICO liability for aiding and abetting and using same common-law tort elements as used by courts involved in securities cases), *modified*, 30 F.3d 1347, *cert. denied*, 115 S. Ct. 900 (1995); *Petro-Tech, Inc. v. Western Co. of N. Am.*, 824 F.2d

interpretation in *Central Bank* should govern claims of civil aiding and abetting under RICO in order to prevent plaintiffs from simply switching their claims from Section 10(b) to Section 1962 of RICO. Plaintiffs should not be able to bring a charge of racketeering more easily than a charge of securities fraud.<sup>203</sup>

## 2. Applying Central Bank to RICO

*Central Bank* instructs that the starting point for determining the scope of prohibited conduct under a statute begins with the text of the statute itself.<sup>204</sup> Because Section 10(b) does not include the words "aid" and "abet," the Court concluded that aiding and abetting conduct could not create 10(b) liability.<sup>205</sup> Similarly, the words "aid" and "abet" do not appear in RICO Section 1962.<sup>206</sup> Section 1962(a), however, does make reference to the criminal aiding and abetting statute.<sup>207</sup> Therefore, although Congress did not actually use the words "aid" and "abet," Congress's reference to the criminal aiding and abetting statute may constitute sufficient evidence of Congress's intent to create liability for aiding and abetting under Section 1962(a).<sup>208</sup>

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1349, 1361 (3d Cir. 1987) (inferring civil aiding and abetting under § 1962(a), but not under § 1962(c)); *Armco Indus. Credit Corp. v. SLT Warehouse Co.*, 782 F.2d 475, 485-87 (5th Cir. 1986) (using criminal standard articulated in 18 U.S.C. § 2 for civil aiding and abetting action); *Rodriguez v. Banco Cent.*, 727 F. Supp. 759, 773 (D.P.R. 1989) (recognizing civil aiding and abetting theory under RICO); *San Jacinto Sav. Ass'n v. TDC Corp.*, 707 F. Supp. 1579, 1582 (M.D. Fla. 1989) (same); *WAIT Radio v. Price Waterhouse*, 691 F. Supp. 102, 108 (N.D. Ill. 1988) (commenting that common-law doctrine of aiding and abetting, like vicarious liability, can apply to RICO if other RICO criteria are met); see also DOUGLAS E. ABRAMS, *THE LAW OF CIVIL RICO* § 4.9.2, at 256-58 (1991) (describing aiding and abetting under RICO).

203. See *Bowdoin Constr. Corp. v. Rhode Island Hosp. Trust Nat'l Bank*, 869 F. Supp. 1004, 1009 (D. Mass. 1994) (noting that it should not be easier to bring racketeering claim than securities fraud claim) (citing *New Eng. Data Servs. v. Becher*, 829 F.2d 286, 291 (1st Cir. 1987)).

204. See *Central Bank*, 114 S. Ct. at 1447 (using text of § 10(b) to define scope of liability); *Reves v. Ernst & Young*, 113 S. Ct. 1163, 1169 (1993) (looking first to statute's text in civil RICO suit); see also Frankfurter, *supra* note 101, at 535 (suggesting statutory interpretation must begin with statute's text).

205. *Central Bank*, 114 S. Ct. at 1448.

206. See *supra* note 201 (providing text of § 1962).

207. See *supra* note 201 (providing text of § 1962(a)).

208. See Judith L. Rosenthal, Comment, *Aiding and Abetting Liability for Civil Violations of RICO*, 61 TEMP. L.Q. 1481, 1505 (1988) (noting that only subsection (a) of § 1962 references criminal aiding and abetting statute).

Courts, however, should not draw a similar inference with respect to the other subsections included under Section 1962.<sup>209</sup> Instead, lower courts should employ the same interpretive principle used by the Court in *Central Bank*. The Court reasoned that the inclusion of secondary liability in one provision indicated the conscious intent to exclude secondary liability from others.<sup>210</sup> Section 1962(a)'s unique reference to the criminal aiding and abetting statute indicates that courts should confine aiding and abetting to that subsection.<sup>211</sup> Moreover, Section 1962(d) creates secondary liability based on conspiracy.<sup>212</sup> In *Central Bank*, the Court referenced Section 20(a) of the 1934 Act, which creates a form of secondary liability, and concluded that congressional inclusion of one form of secondary liability suggested that when Congress wished to create secondary liability, Congress did so.<sup>213</sup> Thus, the *Central Bank* rationale suggests that one draw the same conclusion between Section 1962(d) and the other subsections: Congress knew how to and chose to extend liability based on conspiracy, but not on other forms of secondary liability, such as aiding and abetting.

Finally, at least one lower court justified its recognition of aiding and abetting liability based on Section 1962(c)'s imposition of liability for "indirect" conduct.<sup>214</sup> In *Central Bank*, the Court expressly rejected this

209 See *supra* note 201 (providing text of § 1962(b)-(c)).

210. See *supra* note 107 and accompanying text (explaining that *Central Bank* Court interpreted Congress's inclusion of form of secondary liability in § 20(a) as indication that Congress did not intend there to be other forms of secondary liability in other provisions). Examples exist of decisions in which lower courts did not draw a distinction between § 1962(a) and § 1962(b)-(d). See *Armco Indus. Credit Corp. v. SLT Warehouse Co.*, 782 F.2d 475, 485-86 (5th Cir. 1986) (making no distinction among subsections of § 1962 when discussing aider and abettor liability); *United States v. Local 560, Int'l Bhd. of Teamsters*, 780 F.2d 267, 270 (3d Cir. 1985) (linking aiding and abetting to violations of § 1962(b) and (d) even though neither contains reference to aiding and abetting statute), *cert. denied*, 476 U.S. 1140 (1986); *Rodriguez v. Banco Cent.*, 727 F. Supp. 759, 773 (D.P.R. 1989) (making no distinction among subsections of § 1962 when discussing aider and abettor liability); *San Jacinto Sav. Ass'n v. TDC Corp.*, 707 F. Supp. 1579, 1582 (M.D. Fla. 1989) (same); *WAIT Radio v. Price Waterhouse*, 691 F. Supp. 102, 108 (N.D. Ill. 1988) (same); *GLM Corp. v. Klein*, 684 F. Supp. 1242, 1246-47 (S.D.N.Y. 1988) (same).

211. See Rosenthal, *supra* note 208, at 1505 (noting that courts considering aiding and abetting under civil RICO have not made distinction that reference to criminal aiding and abetting only occurs in subsection (a)).

212. See *supra* note 201 (providing text of § 1962(d)).

213. See *Central Bank*, 114 S. Ct. at 1451-52 (drawing conclusion that Congress's explicit inclusion of secondary liability in another provision of 1934 Act indicated congressional choice to exclude secondary liability under § 10(b)).

214. See *Rodriguez v. Banco Cent.*, 727 F. Supp. 759, 773-74 (D.P.R. 1989) (noting that § 1962(c) contemplates civil RICO liability for "indirect" participation and therefore

argument.<sup>215</sup> The Court stated that Section 10(b)'s phrase "directly or indirectly" does not extend liability to those who aid and abet the primary violator.<sup>216</sup> Consequently, the *Central Bank* decision not only affects and limits the actionable conduct under Section 10(b) of the 1934 Act, but its logic, when applied to civil RICO claims, also seriously undermines the claim of aiding and abetting under Section 1962.<sup>217</sup>

#### IV Central Bank: *Shaping Communication Between the Judicial and Legislative Branches*

Not only does the Court's method of statutory interpretation undermine other long-standing causes of action such as conspiracy and vicarious liability,<sup>218</sup> *Central Bank* has a profound effect on the communication among various participants in the American system of government.<sup>219</sup> *Central Bank* provides judges with a methodology to use when deciding whether to imply a cause of action, but the Court's method of analysis also imposes upon

holding that person may be liable under § 1962(c) by means of aiding and abetting pattern of predicate acts).

215. *Central Bank*, 114 S. Ct. at 1447-48.

216. *Id.* at 1447; see *supra* notes 102-05 and accompanying text (discussing Supreme Court's rejection of First Interstate's and SEC's argument that phrase "directly or indirectly" in § 10(b) extended liability to aiding and abetting conduct).

217. See *supra* notes 207-08 and accompanying text (acknowledging that cause of action for aiding and abetting under § 1962(a) may survive *Central Bank* attack).

218. See *supra* notes 136-56, 171-97 and accompanying text (applying *Central Bank* analysis to conspiracy and vicarious liability under § 10(b) and concluding that *Central Bank* places these claims in jeopardy).

219. There exists broad debate over the constitutionality of the Supreme Court's decision to deny a cause of action when Congress has not specifically provided for one in the statutory text. See generally George D. Brown, *Of Activism and Erie — The Implication Doctrine's Implications for the Nature and Role of the Federal Courts*, 69 IOWA L. REV. 617 (1984) (discussing Justice Powell's and Chief Justice Rehnquist's emphasis on law of separation of powers in their reluctance to imply causes of action); Foy, *supra* note 69 (reviewing Court's movement away from implying causes of action based on separation of powers concerns, but noting that traditional purpose of courts was to give remedies for wrongs defined by legislation); Linda S. Green, *Judicial Implication of Remedies for Federal Statutory Violations: The Separation of Powers Concerns*, 53 TEMP. L.Q. 469 (1980) (contending that judicial fashioning of remedies is inherently "judicial" and therefore is not violation of separation of powers); Thomas W. Merrill, *The Common Law Powers of Federal Courts*, 52 U. CHI. L. REV. 1 (1985) (discussing separation of powers limitation on Supreme Court's ability to imply causes of action); Martin H. Redish, *Federal Common Law, Political Legitimacy, and the Interpretive Process: An "Institutionalist" Perspective*, 83 NW U. L. REV. 761 (1989) (contending that Congress and not Supreme Court should make alterations in preexisting legislation to remedy contemporary social problems).

Congress a framework for communicating congressional intent if it decides to override *Central Bank*.<sup>220</sup> The Court has also shifted an intense debate from federal courtrooms to Congress. Interested parties, who once argued or filed amicus curiae briefs in federal courts, now debate with each other and with lawmakers in the hearing rooms of Congress.<sup>221</sup> Finally, *Central Bank* alters the interaction between private litigants and federal judges because private plaintiffs must now allege different facts, and judges must articulate to plaintiffs and to defendants what conduct remains actionable under Section 10(b).<sup>222</sup>

#### A. Central Bank and Future Statutes

If Congress decides to override *Central Bank*, Congress must do so on the Supreme Court's terms.<sup>223</sup> The Supreme Court focused almost exclusively on the text of Section 10(b); thus, by merely adding the words "aid" and "abet" to the text of Section 10(b), Congress can override *Central Bank* and reinstate a private cause of action for aiding and abetting.<sup>224</sup> Yet if Congress merely includes the words "aid" and "abet" in the text of Section 10(b), Congress will forego an opportunity to incorporate the ideas generated by congressional debate into a statute.<sup>225</sup> Even when all the circuits agreed that a cause of action for aiding and abetting existed under

220. See *infra* notes 230-31 and accompanying text (suggesting provisions that Congress should include in statute if Congress chooses to override *Central Bank*).

221. See *infra* notes 232-47 and accompanying text (discussing debate in Congress).

222. See *infra* notes 248-58 and accompanying text (discussing fact that judges must draw distinction between primary and secondary liability under § 10(b)).

223. Cf. Foy, *supra* note 69, at 570 (praising certainty and encouraging Court to make decisions that tell members of Congress that if they want to create or deny private cause of action, members must clearly say so to achieve that objective); Frankfurter, *supra* note 101, at 545 (commenting that what courts do with legislation in turn affects what Congress will do in future). Frankfurter noted that loose judicial reading makes for loose legislative writing. *Id.*, see also Cass R. Sunstein, *Interpreting Statutes in the Regulatory State*, 103 HARV L. REV 407, 457 (1989) (noting that function of interpretative principles is to promote better lawmaking). Sunstein stated that courts adhere to the "plain meaning" principle in statutory interpretation probably in hopes that Congress will express itself more clearly in the future. *Id.* Implicitly then, the literal textual reading in *Central Bank* should make lawmakers write more crisply and with greater specificity.

224. In the Senate on July 21, 1994, Senator Metzenbaum introduced Senate Bill No. 2306 that would override *Central Bank*, but only by adding the words "aid" and "abet" to the text of § 10(b). See 140 CONG. REC. S9446 (daily ed. July 21, 1994).

225. See *infra* notes 239-45 (discussing congressional debate over appropriateness and parameters of aiding and abetting liability under § 10(b)).

Section 10(b), differences remained as to the parameters of that claim.<sup>226</sup> Returning the aiding and abetting issue to the judiciary without further clarification would once again require courts to trudge through the various arguments; and again, courts would only resolve the debate incrementally.<sup>227</sup> For example, courts would again face the debate over what kind of behavior constitutes substantial assistance<sup>228</sup> and what mental state in a defendant creates aiding and abetting liability.<sup>229</sup>

Thus, mere insertion of the words "aid" and "abet" into the text of Section 10(b) would clearly articulate Congress's intent to create liability for this conduct; this action, however, would neither incorporate the ideas generated by congressional debate nor answer the questions that surrounded aiding and abetting prior to *Central Bank*.<sup>230</sup> Consequently, if Congress reinstates liability for aiding and abetting conduct under Section 10(b), Congress should provide the following provisions: (1) a specific determination on whether the plaintiff can create liability by showing that the defendant acted recklessly or whether the plaintiff must show that the defendant knew that she was aiding the primary violator, (2) a description about what may and may not constitute "substantial assistance," and (3) a decision about whether courts should hold aiders and abettors jointly and severally liable to plaintiffs for damages caused by the Section 10(b) violation or whether aiders and abettors should only be proportionally liable for the plaintiff's damage along with the primary violator.

Additionally, the *Central Bank* Court's method of statutory analysis seriously undermines other common-law forms of secondary liability such as conspiracy and vicarious liability.<sup>231</sup> Consequently, *Central Bank* not only

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226. See *supra* notes 34-42 and accompanying text (discussing differences among circuits in their treatment of aiding and abetting cause of action under § 10(b)).

227. See *supra* notes 34-42 and accompanying text (discussing differences among lower federal courts as to what conduct aiding and abetting ought to include); see also *infra* notes 239-45 and accompanying text (discussing disagreements among commentators as to parameters of aiding and abetting liability under § 10(b)).

228. See *supra* notes 35-40 and accompanying text (describing differences among circuits about what factors courts emphasized when determining whether defendant substantially assisted primary violator of § 10(b) so that defendant was liable as aider and abettor).

229. See *supra* notes 41-42 and accompanying text (describing differences among circuits about what mental state plaintiff had to prove to impose § 10(b) liability on defendant for aiding and abetting).

230. See *supra* notes 34-42 and accompanying text (describing disagreements among circuits about parameters of aiding and abetting cause of action under § 10(b)).

231. See *supra* notes 136-56, 171-97, 204-17 and accompanying text (discussing *Central Bank* ramifications on other implied causes of action).

forces Congress to address the narrow issue of aiding and abetting under Section 10(b), but the decision also requires that Congress make clear its intent to include or exclude these other forms of secondary liability. Otherwise, because of the Court's textual emphasis, these claims may disappear even if Congress enacts a statute expressly extending 10(b) liability to aiding and abetting.

### B. Central Bank: *Molding the Debate in Congress*

Many commentators and lawmakers have vehemently criticized the Court's rejection of the implied aiding and abetting action under Section 10(b).<sup>232</sup> Yet no one — not even Justice Stevens, who wrote the *Central Bank* dissent — contends that Section 10(b)'s text encompasses aiding and abetting conduct.<sup>233</sup> Blanket criticism of the *Central Bank* decision thus fails to acknowledge an important distinction: While it may be appropriate, and in fact desirable, for the judiciary to imply a private cause of action to redress conduct *expressly proscribed* by Congress, it does not follow that the judiciary should, in the absence of conduct proscribed by Congress, imply and define a separate cause of action.<sup>234</sup>

With the *Central Bank* decision, the Court has invited Congress to either respond with a statute that describes prohibited conduct or to remain satisfied with the current state of Section 10(b) without aiding and abetting liability and arguably without other forms of secondary liability.<sup>235</sup> This

232. See *House Hearing*, *supra* note 113, at 235 (prepared statement of Mark J. Griffin, Securities Division, Utah Department of Commerce) (suggesting that investors are considerably worse off after *Central Bank*); *id.* at 235 (statement of Donald C. Langevoort, Lee S. and Charles A. Speir Professor of Law, Vanderbilt University) (finding Court's reasoning in *Central Bank* unpersuasive, especially in its treatment of judicial precedent in lower courts); *Senate Hearing*, *supra* note 34, at 1 (statement of Sen. Christopher J. Dodd) (noting common-law foundation of aiding and abetting and stating that before Supreme Court changed landscape, aiding and abetting was important tool in ensuring honesty and high professional standards); 140 CONG. REC. S9460 (daily ed. July 21, 1994) (statement of Sen. Howard M. Metzenbaum) (characterizing *Central Bank* as result of bizarre legal reasoning).

233. See *supra* notes 118-24 and accompanying text (discussing Justice Stevens's dissent in *Central Bank*).

234. Cf. Michael P. Dooley, *The Effects of Civil Liability on Investment Banking and the New Issues Market*, 58 VA. L. REV. 776, 801 (1972) (suggesting that predictability is most important factor in assessing risks of legal liability and that parties assign high costs to those perceived risks that are not only substantial but also indeterminate).

235. See *supra* notes 101-05 and accompanying text (describing *Central Bank* decision and statutory analysis employed by Supreme Court). But cf. James J. Brudney, *Congressional Commentary on Judicial Interpretations of Statutes: Idle Chatter or Telling Response?*, 93 MICH. L. REV. 1, 17 (1994) (arguing that Court's theory that Congress can simply "do it

invitation has led interested parties from the courtrooms to the congressional hearing rooms — some in support of the *Central Bank* decision and some seeking legislation to override the decision.<sup>236</sup> But unlike a judicial setting, where the nature of our adversarial system limits nonparties to amicus briefs on narrow issues,<sup>237</sup> congressional subcommittees have permitted nonparties to present a wide array of information and opinions about aiding and abetting under Section 10(b) as well as other issues affecting securities regulation.<sup>238</sup>

Those testifying before Congress have debated some of the same issues that parties litigated piecemeal in the judiciary. Just as the SEC, as amicus curiae, differed from the majority in *Central Bank*, those who testified before Congress have similarly disagreed about whether imposing broad liability in the securities industry has a positive or negative impact upon investors and those involved in capital formation.<sup>239</sup> Most witnesses have

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better next time" discounts how resource intensive "next time" is likely to be). Professor Brudney asserts that congressional time constraints are such that it is naive for the Court to refuse to interpret legislative history and to demand that congressional intent be fully encompassed within the text of the statute. *Id.* at 22; *see also* Note, *supra* note 150, at 905 (arguing that realities of legislative power constrain Congress from constant re-examination of all its statutes and thus that clear-statement policy foists upon Congress responsibility that it cannot meet).

236. *See House Hearing, supra* note 113 (providing various commentators and interested parties with chance to give their opinion on how Congress should proceed in wake of *Central Bank*); *Senate Hearing, supra* note 34 (same); *see also* Hardon F. Stone, *The Common Law in the United States*, 50 HARV. L. REV. 4, 25 (1936) (using phrase "sober second thought" when referencing congressional response to Supreme Court decisions).

237. *See supra* note 95-100 and accompanying text (noting that SEC had to submit amicus brief in *Central Bank* case when SEC wanted to influence definition of aiding and abetting liability).

238. *See, e.g., House Hearing, supra* note 113, at 265-66 (prepared statement of Leonard B. Simon, on behalf of National Association of Securities and Commercial Law Attorneys) (providing statistics that undermine Supreme Court's assumption that securities litigation results in harm to securities formation); *id.* at 235, 245-46 (prepared statement of Mark J. Griffin, Securities Division, Utah Department of Commerce) (suggesting that Congress may want to investigate procedures currently provided to judiciary to deal with frivolous claims and advocating that Congress overrule *Central Bank* decision with legislation); *Senate Hearing, supra* note 34, at 64 (prepared statement of Stuart J. Kaswell, senior vice president and general counsel, Securities Industry Association) (praising *Central Bank* decision and encouraging Congress to avoid "quick fix" on secondary liability and instead emphasizing importance of continued comprehensive review of securities litigation system); *id.* at 28 (statement of Eugene L. Goldman, partner, McDermott, Will & Emory) (asserting that *Central Bank* decision provides Congress with opportunity to examine whole issue of varying levels of liability for defendants in securities law suits).

239. *See Central Bank*, 114 S. Ct. at 1453-54 (rejecting SEC's policy arguments that secondary liability is necessary to deter secondary actors from contributing to fraud and nec-



contended that Congress should create aiding and abetting liability under Section 10(b), but have disagreed among themselves over the parameters of that liability

Moreover, like those appearing before lower federal courts, those testifying before Congress disagreed over the types of evidence that plaintiffs must assert to sustain a cause of action for aiding and abetting.<sup>240</sup> Some urged Congress to adopt a liberal definition of aiding and abetting under Section 10(b) by, for example, encouraging Congress to explicitly sanction a plaintiff's reliance on a showing of recklessness to create liability in the defendant.<sup>241</sup> Others countered by encouraging Congress to create a stricter

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essary to ensure that courts make defrauded parties whole). The *Central Bank* Court struck down the argument that broad-based civil liability under federal securities laws would better serve the objectives of the statute. *Id.* at 1454. The Court, instead, noted that securities litigation was an area that demanded a degree of certainty and predictability. *Id.* The Court reasoned that the uncertainty surrounding the governing rules of aiding and abetting caused defendants to abandon substantial defenses and incur large settlement expenses. *Id.* The Court concluded that instead of helping the intended beneficiaries of the securities laws, having uncertain causes of action actually hurt investors because professionals passed the increased costs along to investors. *Id.*

A representative of the Securities Industry Association made an analogous argument before a Senate subcommittee following the *Central Bank* decision. *See Senate Hearing, supra* note 34 (prepared statement of Stuart J. Kaswell, senior vice president and general counsel, Securities Industry Association). Kaswell argued that secondary liability had an especially deleterious effect on capital formations because its contours were vague and elastic. *Id.* at 66. Kaswell contended that professionals like accountants and attorneys inevitably charged higher fees because of the possibility that a plaintiff would make a claim that they were secondarily liable. *Id.* Kaswell reasoned that this in turn made it more difficult for new or innovative businesses to raise capital. *Id.*

Others, however, presented evidence that undermined the assertion that the imposition of secondary liability has harmed capital formation. *See House Hearing, supra* note 113, at 238-39 (prepared statement of Mark J. Griffin, Securities Division, Utah Department of Commerce) (presenting evidence that securities industry has incurred no harm in terms of capital formation). Griffin noted that over the last 20 years, stock offerings and stock trading have increased dramatically. *Id.* at 238.

240. *See supra* notes 34-42 and accompanying text (describing differences among circuits in terms of evidence required by plaintiffs to sustain a cause of action for aiding and abetting under § 10(b)).

241. *See House Hearing, supra* note 113, at 291 (prepared statement of Leonard B. Simon, on behalf of National Association of Securities and Commercial Law Attorneys) (asserting that exemption for reckless conduct was manifestly unfair to fraud victims). Simon argued that if an accountant, lawyer, or some other professional acted recklessly and thus furthered a fraud, he or she ought to be liable to defrauded victims. *Id.*, *see also Senate Hearing, supra* note 34, at 72 (prepared statement of Harvey J. Goldschmid, Dwight Professor of Law, Columbia University) (encouraging Congress to consider showing of recklessness as sufficient to satisfy scienter requirement under § 10(b)).

form of aiding and abetting liability by aligning the required elements more closely with those necessary to establish a primary violation. For example, some disfavored a plaintiff's showing of recklessness and argued that courts should only impose aiding and abetting liability if the plaintiff shows that the defendant rendered knowing assistance or deliberately disregarded the truth.<sup>242</sup> Another suggestion that would create a stricter form of aiding and abetting liability was that aiding and abetting liability should attach only when the plaintiff is able to show that he relied on the defendant's conduct.<sup>243</sup> Finally, some testified that secondary defendants should remain jointly and severally liable to plaintiffs along with the primary violator,<sup>244</sup> while others maintained that a secondary defendant's liability should be proportional to that of the primary violator.<sup>245</sup>

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242. See *House Hearing*, *supra* note 113, at 126 (prepared statement of Donald C. Langevoort, Lee S. and Charles A. Speir Professor of Law, Vanderbilt University) (favoring restoration of private aiding and abetting liability under § 10(b) but urging creation of liability for ancillary participation only when participant rendered knowing assistance or deliberately disregarded truth); *Senate Hearing*, *supra* note 34, at 74 (prepared statement of Eugene L. Goldman, partner, McDermott, Will & Emory) (worrying that courts align "recklessness" standard too closely with concepts of negligence and therefore jeopardize participation in routine business transactions).

243. See *Senate Hearing*, *supra* note 34, at 74 (prepared statement of Eugene L. Goldman, partner, McDermott, Will & Emory) (stating that specific standard for imposing aiding and abetting liability should include reliance requirement). The inclusion of a reliance requirement as an element of aiding and abetting would essentially eliminate aiding and abetting liability as it existed in lower courts prior to *Central Bank* and would force plaintiffs to prove a primary violation. See also *Central Bank*, 114 S. Ct. at 1449 (noting that SEC's and First Interstate's argument would impose § 10(b) aiding and abetting liability on defendant without proof of reliance). Compare *supra* notes 26-33 and accompanying text (providing discussion of aiding and abetting liability prior to *Central Bank*) with *infra* notes 254-57 and accompanying text (describing elements of primary violation under § 10(b)).

244. See *House Hearing*, *supra* note 113, at 242-43 (prepared statement of Mark J. Griffin, Securities Division, Utah Department of Commerce) (arguing that critics of joint and several liability were forgetting that purpose of securities system is to protect rights of defrauded investors). Griffin argued that when forced to choose between innocent investors and professionals who knowingly or recklessly assisted the fraud, those professionals — not innocent investors — should bear the risk of financial loss. *Id.*, see also *id.* at 156 (statement of Arthur R. Miller, Bruce Bromley Professor of Law, Harvard University) (noting that elimination of joint and several liability would weaken the compensatory purpose and effectiveness of private securities actions).

245. See *id.* at 126 (prepared statement of Donald C. Langevoort, Lee S. and Charles A. Speir Professor of Law, Vanderbilt University) (noting that restoration of § 10(b) aiding and abetting should only create proportionate liability for aider and abettor instead of joint and several liability); *id.* at 90 (prepared statement of Joel Seligman, Professor of Law, University of Michigan) (advocating restoration of aiding and abetting liability under § 10(b),

When critiquing the Court's method of statutory interpretation, one must consider the extensive debate and diversity of opinions that have surfaced in congressional hearings since *Central Bank*. Although persuasive arguments exist against the Court's use of strict textualism in statutory analysis,<sup>246</sup> with regard to securities regulation and to the creation of secondary liability specifically, the Court's use of this method in the securities context may not be all bad. The extensive debate and diversity of opinions suggest that Congress, not the Court, remains the better forum in which to sort through the policy arguments to decide whether Section 10(b) should include a cause of action for aiding and abetting and to define the parameters of any claim.<sup>247</sup> Thus, the Court has given Congress — the branch with the procedures to hear and respond to this broad debate — the opportunity to enact a comprehensive statute instead of relying on the judiciary for such work.

### C. *A Difficult Line to Draw*

While *Central Bank* leaves Congress with the task of determining whether to create secondary liability under Section 10(b), *Central Bank* creates a much different situation among lower courts. For the first time in thirty years, lower courts must draw a clear distinction between primary and secondary liability under Section 10(b). In *Central Bank*, the Court stated that any person or entity, even those who have traditionally faced claims based on secondary liability, could be liable as a *primary violator* of Section 10(b) if a plaintiff meets *all* the requirements to create primary liability.<sup>248</sup> The Court, however, noted that those who only aid and abet cannot be subject to 10(b) liability because, by definition, aiders and abettors do not

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but asserting that Congress should limit aiders and abettors to proportionate liability except in circumstances of insolvent primary violator whose damages are not adequately insured).

246. See Brudney, *supra* note 235, at 57 (suggesting that requiring Congress to expand its text would probably not result in better job of statutory drafting, but instead, in effort to add details and illustrations, text would likely become more precise but less coherent); Luneburg, *supra* note 116, at 217 (noting that clear-statement techniques of statutory interpretation function in part to free court from its duty to abide by results of its investigation into meaning of statute); Sunstein, *supra* note 223, at 416 (stating that textualist approach in its purest form is inadequate because meaning of words, whether plain or not, depends on both *culture* and *context*).

247. See Luneburg, *supra* note 116, at 220 (noting that Court's adherence to clear statement method of statutory interpretation tends to force Congress to directly and expressly address issue in way that focuses its public responsibility for action).

248. *Central Bank*, 114 S. Ct. at 1455.

engage in any of the activities proscribed by Section 10(b).<sup>249</sup> One commentator has noted that *Central Bank* may create a litigation morass because the Court created the need to draw this distinction, but failed to provide lower courts with a guide as to where the line between a primary and secondary violation exists.<sup>250</sup> During the thirty years that the cause of action for aiding and abetting existed, courts gave little attention to the distinction between primary and secondary liability because both classes of actors were jointly and severally liable for the Section 10(b) violation.<sup>251</sup>

In an effort to avoid the confusion, judges should adhere strictly to Federal Rule of Civil Procedure 9(b) (Rule 9(b))<sup>252</sup> and communicate to plaintiffs that courts will dismiss claims that they would have once sustained under Section 10(b) unless the plaintiff can demonstrate with particularity that the defendant's conduct constitutes a primary violation. Strict use of Rule 9(b) will highlight the marked differences between the general elements necessary to allege secondary participation and the elements required to allege a primary violation because Rule 9(b) forces the plaintiff to clearly distinguish and communicate these differences.<sup>253</sup> In the past, plaintiffs asserting a claim of aiding and abetting had to plead with particularity, but only as to (1) whether there was a primary violation, (2) whether the accused aider-abettor had general awareness that his conduct was improper, and

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249. *Id.* at 1447

250. *Senate Hearing*, *supra* note 34, at 72 (statement of Harvey J. Goldschmid, Dwight Professor of Law, Columbia University); *see supra* note 14 (providing text of § 10(b)).

251. *See Senate Hearing*, *supra* note 34, at 52-53 (prepared statement of Donald C. Langevoort, Lee S. and Charles A. Speir Professor of Law, Vanderbilt University) (noting that courts hold both primary and secondary defendants jointly and severally liable for § 10(b) violation).

252. See FED. R. CIV. P. 9(b), which provides: "In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other condition of mind of a person may be averred generally."

253. *See supra* note 252 (providing text of Rule 9(b)); *see also House Hearing*, *supra* note 113, at 79 (prepared statement of Joel Seligman, Professor of Law, University of Michigan) (arguing that courts have been effective in their use of Rule 9(b) to weed out nonmeritorious lawsuits); *cf. id.* at 123 (prepared statement of Donald C. Langevoort, Lee S. and Charles A. Speir Professor of Law, Vanderbilt University) (proposing that Congress empower courts to conduct evidentiary hearing at outset of case in which plaintiffs have to show significant likelihood of success on merits). Professor Langevoort proposed the creation of an evidentiary hearing in securities cases. *Id.* Courts would not require plaintiffs to show that success is more likely than not, but plaintiffs would have to show that the case is more than speculative. *Id.* Langevoort asserted that unlike the current 9(b) motion, the hearing should be evidentiary so that courts do not have to accept the plaintiffs' allegations at face value. *Id.*

(3) whether the accused aider-abettor substantially assisted the primary wrongdoer.<sup>254</sup> By contrast, plaintiffs who now attempt to create primary liability face a higher threshold because the elements for a primary violation are significantly more stringent. To avoid a motion to dismiss, a plaintiff must set forth particular facts establishing that (1) the defendant misrepresented or omitted material facts or engaged in some other fraudulent device, (2) the defendant purchased or sold securities in connection with the fraudulent device, (3) the defendant acted with the required mental state when making the misrepresentation or omission,<sup>255</sup> (4) the plaintiff justifiably relied on the misstatement or omission,<sup>256</sup> and (5) damages resulted from the

254. See, e.g., *Farlow v Peat, Marwick, Mitchell & Co.*, 956 F.2d 982, 986 (10th Cir. 1992) (applying common-law tort elements of aiding and abetting); *Levine v Diamantheset, Inc.*, 950 F.2d 1478, 1483 (9th Cir. 1991) (same); *Schatz v Rosenberg*, 943 F.2d 485, 495 (4th Cir. 1991) (same), *cert. denied*, 503 U.S. 936 (1992); *Fine v American Solar King Corp.*, 919 F.2d 290, 300 (5th Cir. 1990) (same), *cert. dismissed sub nom. Hurdman v Fine*, 502 U.S. 976 (1991); *Schliife v Seafirst Corp.*, 866 F.2d 935, 947 (7th Cir. 1989) (same); *Schneberger v Wheeler*, 859 F.2d 1477, 1480 (11th Cir. 1988) (same), *cert. denied*, 490 U.S. 1091 (1989); *Moore v Fenex, Inc.*, 809 F.2d 297, 303 (6th Cir.) (same), *cert. denied*, 483 U.S. 1006 (1987); *Clery v Perfecune, Inc.*, 700 F.2d 774, 777 (1st Cir. 1983) (same); *International Inv Trust v Cornfeld*, 619 F.2d 909, 922 (2d Cir. 1980) (same); *Monsen v Consolidated Dressed Beef Co.*, 579 F.2d 793, 799 (3d Cir.) (same), *cert. denied*, 439 U.S. 930 (1978); see also *Ruder, supra* note 23, at 620 (describing common-law elements of aiding and abetting).

255. See *Ernst & Ernst v Hochfelder*, 425 U.S. 185, 193 (1976) (concluding that courts should not sustain private cause of action for damages under § 10(b) in absence of allegation of "scienter"). In *Hochfelder*, the Court considered whether scienter was a necessary element in an action under § 10(b). *Id.* at 193. The Court concluded that scienter was a necessary element, but left open the issue of whether recklessness could satisfy this element. *Id.* at 193 n.12. Since *Hochfelder*, most circuits have held that recklessness is sufficient to satisfy the scienter requirement. See, e.g., *McLean v Alexander*, 599 F.2d 1190, 1197-98 (3d Cir. 1979) (accepting showing of recklessness to satisfy scienter requirement in § 10(b) action); *Hoffman v Estabrook & Co.*, 587 F.2d 509, 516-17 (1st Cir.) (accepting plaintiff's showing of recklessness, but defining recklessness conservatively), *cert. denied*, 439 U.S. 970 (1978); *First Va. Bankshares v Benson*, 559 F.2d 1307, 1312 (5th Cir. 1977) (including "reckless" within definition of what behavior is necessary to maintain § 10(b) action), *cert. denied*, 435 U.S. 952 (1978); *Sundstrand Corp. v Sun Chem. Corp.*, 553 F.2d 1033, 1044 (7th Cir.) (same), *cert. denied*, 434 U.S. 875 (1977); see also CLARK, *supra* note 6, § 8.10.3, at 266 (noting that Supreme Court's decision in *Hochfelder* requiring allegation of scienter to support cause of action for damages under § 10(b) removed large class of threats to professional firms like accountants and lawyers).

256. See *Central Bank*, 114 S. Ct. at 1449 (emphasizing § 10(b)'s reliance element) (citing *Basic Inc. v Levinson*, 485 U.S. 224, 243 (1988)). The *Central Bank* Court commented that the fact that an action for aiding and abetting would impose 10(b) liability even when the plaintiff failed to establish reliance confirmed the Court's reasoning not to extend § 10(b) to include conduct for aiding and abetting. *Id.*, see also CLARK, *supra* note 6, § 8.10.5, at 329

defendant's misstatement, omission, or fraudulent device.<sup>257</sup>

Because of the high cost of litigation,<sup>258</sup> judges should require plaintiffs to communicate clearly that defendants' conduct is still actionable, even after *Central Bank*. Mere dismissal of the aiding and abetting count after trial, or even after discovery, without a careful preliminary inquiry at the pleading stage into whether the plaintiff can sustain a claim under Section 10(b) will not alleviate the costs defendants currently face. If courts allow plaintiffs simply to manipulate the complaint without substantially changing the facts alleged, defendants will suffer unjustly because they will incur litigation expense and settlement pressures for conduct the Supreme Court has said Congress does not proscribe.

### V Conclusion

The Supreme Court's emphasis on the text of Section 10(b) in *Central Bank* has both negative and positive ramifications. The Supreme Court's analysis abolishes thirty years of judicial precedent and calls into question other established claims, such as conspiracy and vicarious liability under Section 10(b) and aiding and abetting under RICO. Thus, the Court has undermined concepts of judicial precedent and stability

Prior to *Central Bank*, however, the parameters of liability under Section 10(b) were unclear. Lower courts had developed an extensive body of law surrounding aiding and abetting liability, but Congress had taken no part in that development. Consequently, courts were exhausting judicial resources and defendants were incurring costs for suits involving conduct not

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(noting that proof of reliance forms part of causal chain from violation to injury); LOUIS LOSS & JOEL SELIGMAN, *FUNDAMENTALS OF SECURITIES REGULATION* 1051 (3d ed. 1995) (same). See generally Note, *The Reliance Requirement in Private Actions Under SEC Rule 10b-5*, 88 HARV L. REV 584 (1975) (discussing § 10(b)'s reliance requirement).

257 See *Warren v Reserve Fund, Inc.*, 728 F.2d 741, 744 (5th Cir. 1984) (applying element requirement to determine whether primary liability exists); *Schlick v Penn-Dixie Cement Corp.*, 507 F.2d 374, 378-81 (2d Cir. 1974) (discussing elements of §10(b) claim and whether plaintiff alleged sufficient facts to support that claim), *cert. denied*, 421 U.S. 976 (1975); *Weitzman v Stein*, 436 F Supp. 895, 902-04 (S.D.N.Y. 1977) (same); see also Mary Siegel, *The Interplay Between the Implied Remedy Under Section 10(b) and the Express Causes of Action of the Federal Securities Laws*, 62 B.U. L. REV 385, 393-94 (1982) (describing substantive requirements for § 10(b) actions).

258. See 138 CONG. REC. S12605 (daily ed. Aug. 12, 1992) (statement of Sen. Sanford). Senator Sanford asserted that litigation under § 10(b) requires secondary actors to expend large sums. *Id.* The Senator noted that in 83% of the § 10(b) cases, major accounting firms, who are often the target of secondary claims, paid eight dollars in legal fees for every dollar paid in claims. *Id.*

proscribed by Congress. Therefore, although a strict textualist approach to statutory interpretation warrants criticism in some circumstances, the Court's use of this approach in *Central Bank* should not receive blanket criticism. The approach has threatened judicial precedent and stability to a certain extent, but at the same time, the decision has triggered broad debate in Congress. Consequently, even those who strongly oppose the decision may present their positions to Congress where the procedures are such that Congress can respond comprehensively to the arguments made. If those interested can convince a majority of the members of Congress to override *Central Bank*, the Supreme Court's textually oriented approach dictates that those members respond comprehensively by defining the parameters of aiding and abetting and by making clear their intent with regard to other forms of secondary liability, such as conspiracy and vicarious liability.

If a majority does not develop in support of overriding *Central Bank*, the decision will indeed strike a severe blow to those who believe that secondary liability is an essential component of securities regulation. Yet, for others who believe that courts should not expend judicial resources and that defendants should not have to defend actions for conduct not proscribed by Congress, *Central Bank* will prove to be a welcome decision.