

The Burger Court Opinion Writing Database

Ernst & Ernst v. Hochfelder

425 U.S. 185 (1976)

Paul J. Wahlbeck, George Washington University
James F. Spriggs, II, Washington University in St. Louis
Forrest Maltzman, George Washington University



✓
Supreme Court of the United States
Washington, D. C. 20543

CHAMBERS OF
THE CHIEF JUSTICE

March 26, 1976

Re: 74-1042 - Ernst & Ernst v. Hochfelder

Dear Lewis:

Please join me in your circulation of March 11.

✓ Regards,

W. J. Powell

Mr. Justice Powell

Copies to the Conference

Supreme Court of the United States
Washington, D. C. 20543

CHAMBERS OF
JUSTICE WM. J. BRENNAN, JR.

March 9, 1976

WJ
RE: No. 74-1042 Ernst & Ernst v. Hochfelder, et al.

Dear Harry:

You and I were the only dissenters in this one. Are you still disposed to affirm after reading Lewis' circulation, and, if so, would you care to take on the dissent?

Sincerely,

Blackmun

Mr. Justice Blackmun

March 18, 1976

RE: NO. 74-1042 Ernst & Ernst v. Hochfelder

Dear Harry:

I have absolutely no doubt that this is right. I'm happy to join it. Lewis' fine job for his side still doesn't answer you.

Sincerely,

WJB

Mr. Justice Blackmun

Supreme Court of the United States
Washington, D. C. 20543

CHAMBERS OF
JUSTICE WM. J. BRENNAN, JR.

March 25, 1976

RE: No. 74-1042 Ernst & Ernst v. Hochfelder, et al.

Dear Harry:

Please join me in your dissenting opinion in the
above.

Sincerely,



Mr. Justice Blackmun

cc: The Conference

✓ Supreme Court of the United States
✓ Washington, D. C. 20543

CHAMBERS OF
JUSTICE POTTER STEWART

March 10, 1976

No. 74-1042 - Ernst & Ernst

Dear Lewis,

I am glad to join your opinion
for the Court in this case.

Sincerely yours,

P.S.
✓

Mr. Justice Powell

Copies to the Conference

Supreme Court of the United States
Washington, D. C. 20543

CHAMBERS OF
JUSTICE BYRON R. WHITE

March 15, 1976

Re: No. 74-1042 - Ernst & Ernst v. Hochfelder

Dear Lewis:

Please join me in your very good opinion
in this case.

Sincerely,

Byron

Mr. Justice Powell

Copies to Conference

To: The Chief Justice
 Mr. Justice Brennan
 Mr. Justice Stewart
 Mr. Justice White
 Mr. Justice Marshall
 Mr. Justice Powell
 Mr. Justice Rehnquist
 Mr. Justice Stevens

From: Mr. Justice Blackmun

Circulated: 3/24/76

Recirculated: _____

1st DRAFT

SUPREME COURT OF THE UNITED STATES

No. 74-1042

Ernst & Ernst, Petitioner, | On Writ of Certiorari to the
 v. | United States Court of Ap-
 Olga Hochfelder et al. | peals for the Seventh Cir-
 circuit.

[March —, 1976]

MR. JUSTICE BLACKMUN, dissenting.

Once again—see *Blue Chip Stamps v. Manor Drug Stores*, 421 U. S. 723, 730 (1975)—the Court interprets § 10 (b) of the Securities Exchange Act of 1934, 15 U. S. C. § 78j (b), and the Securities and Exchange Commission's Rule 10b-5, 17 CFR § 240.10b-5 (1975), restrictively and narrowly and thereby stultifies recovery for the victim. This time the Court does so by confining the statute and the Rule to situations where the defendant has "scienter," that is, the "intent to deceive, manipulate, or defraud." Sheer negligence, the Court says, is not within the reach of the statute and the Rule, and was not contemplated when the great reforms of 1933, 1934, and 1942 were effectuated by Congress and the Commission.

Perhaps the Court is right, but I doubt it. The Government and the Commission doubt it too, as is evidenced by the thrust of the brief filed by the Solicitor General on behalf of the Commission, as *amicus curiae*. The Court's opinion, *ante*, to be sure, has a certain technical consistency about it. It seems to me, however, that an investor can be victimized just as much by negligent conduct as by positive deception, and that it is not logical to drive a wedge between the two, saying that Congress clearly intended the one but certainly not the other.

To: The Chief Justice
Mr. Justice Brennan
Mr. Justice Stewart
Mr. Justice White
- Mr. Justice Marshall
Mr. Justice Blackmun
Mr. Justice Rehnquist
Mr. Justice Stevens

From: Mr. Justice Powell

Circulated: MAR 9 1976

Recirculated: _____

1st DRAFT

SUPREME COURT OF THE UNITED STATES

No. 74-1042

Ernst & Ernst, Petitioner, } On Writ of Certiorari to the
v. } United States Court of Ap-
Olga Hochfelder et al. } peals for the Seventh Cir-
cuit.

[March —, 1976]

MR. JUSTICE POWELL delivered the opinion of the Court.

The issue in this case is whether an action for civil damages may lie under § 10 (b) of the Securities Exchange Act of 1934 (1934 Act), 48 Stat. 891, 15 U. S. C. § 78j (b), and Securities and Exchange Commission Rule 10b-5, 17 CFR § 240.10b-5, in the absence of an allegation of intent to deceive, manipulate, or defraud on the part of the defendant.

I

Petitioner, Ernst & Ernst, is an accounting firm. From 1946 through 1967 it was retained by First Securities Company of Chicago (First Securities), a small brokerage firm and member of the Midwest Stock Exchange and of the National Association of Securities Dealers, to perform periodic audits of the firm's books and records. In connection with these audits Ernst & Ernst prepared for filing with the Securities and Exchange Commission (the Commission) the annual reports required of First Securities under § 17 (a) of the 1934 Act, 15 U. S. C. § 78q (a).¹ It also prepared for First Securities responses

¹ Section 17 (a) requires that securities brokers or dealers "make . . . and preserve . . . such accounts . . . books, and other

p. 7

To: The Chief Justice
 Mr. Justice Brennan
 Mr. Justice Stewart
 Mr. Justice White
 Mr. Justice Marshall
 Mr. Justice Flanagan
 Mr. Justice Rehnquist
 Mr. Justice Stevens

From: Mr. Justice Powell

Circulated: _____

Recirculated: MAR 11 1975

2nd DRAFT

SUPREME COURT OF THE UNITED STATES

No. 74-1042

Ernst & Ernst, Petitioner, } On Writ of Certiorari to the
 v. } United States Court of Ap-
 Olga Hochfelder et al. } peals for the Seventh Cir-
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[March —, 1976]

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¹ Section 17 (a) requires that securities brokers or dealers "make . . . and preserve . . . such accounts . . . books, and other

April 6, 1976

Cases Held for No. 74-1042 ERNST & ERNST v. HOCHFELDER

MEMORANDUM TO THE CONFERENCE:

There are three cases being held for ERNST & ERNST, two of which are related and will be discussed together:

No. 74-1366, Schaefer v. First National Bank of Lincolnwood, and No. 74-1407 Rodman & Renshaw v. Schaefer.

The petitions in these cases arise from a complex stock fraud. A number of persons, including an employee of the petitioner brokerage firm in No. 74-1407 [hereinafter Rodman & Renshaw] conspired to drive up the price of the stock of a certain corporation in order to facilitate a merger. Petitioners in No. 74-1366 [hereinafter Schaefer] were purchasers of the shares during the period in which their market price was artificially inflated. They brought this civil action under § 1 of the Sherman Act and various sections of the Securities Act of 1933 and the Securities Exchange Act of 1934.

CA 7 held that Schaefer had a cause of action under § 10(b) and Rule 10b-5 despite the express remedy for price manipulation in § 9 of the 1934 Act and that the applicable state statute of limitations for civil actions under § 10(b) was equitably tolled because Rodman & Renshaw had facilitated the fraud of their employee through negligence. The court further held that Schaefer's Sherman Act claim was incompatible with the damage remedies under the Securities Acts.

No. 75-1065 John Nuveen & Co., Inc. v. Sanders

This case concerns the application of § 10(b) and Rule 10b-5 to dealers in commercial paper. CA 7 held that commercial paper with a maturity of 90 days constituted "securities" within the meaning of the Securities Exchange Act of 1934, despite the definition of "security" in § 3(a)(10) of that Act which expressly states that the term "shall not include . . . any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months" The court further held that the petitioner, a dealer in commercial paper, was liable for civil damages under § 10(b) and Rule 10b-5 to purchasers of such paper for failure to make an adequate investigation of the financial strength of the issuer corporation. Although CA 7 purported not to rely on a "mere negligence" standard, it is evident from the opinion that petitioner was held liable without any proof of "scienter", as that term is used in Ernst & Ernst. Petitioner's liability was premised on the fact that it had failed to make a "reasonable investigation" of the issuer, CA 7 noting that petitioner had "acted in the mistaken, but honest belief that financial statements prepared by certified public accountants correctly represented the condition of the issuer" Pet. App. 1.

Petitioner challenges each of these holdings. Although the issue of the scope of the term "security" under the 1934 Act is important, in view of the liability standard under § 10(b) and Rule 10b-5 adopted by CA 7, I will vote to grant, vacate, and remand in light of Ernst & Ernst.

L.F.P., Jr.

LFP/gg

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Supreme Court of the United States
✓
Washington, D. C. 20543

CHAMBERS OF
JUSTICE WILLIAM H. REHNQUIST

March 11, 1976

Re: No. 74-1042 - Ernst & Ernst v. Hochfelder

Dear Lewis:

Please join me.

Sincerely,

W. H. R.

Mr. Justice Powell

Copies to the Conference