OFFICIAL TRANSCRIPT
PROCEEDINGS BEFORE

THE SUPREME COURT OF THE UNITED STATES

DKT/CASE NO. 84-165

TITLE W. GEORGE GOULD, Petitioner V. MAX A. RUEFENACHT, ET AL.

PLACE Washington, D. C.

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IN THE SUPREME COURT OF THE UNITED STATES

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W. GEORGE GOULD, :

Petitioner, :

V. : No. 84-165

MAX A. RUEFENACHT, :

ET AL. :

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Tuesday, March 26, 1985

Washington, D.C.

The above-entitled matter came on for oral argument before the Supreme Court of the United States at 1:00 o'clock p.m.

APPEARANCES:

ROBERT C. EPSTEIN, ESQ., Roseland, New Jersey; on behalf of the petitioner.

PETER STEVEN PEARLMAN, ESQ., Saddle Brook, New Jersey; on behalf of the respondents.

DANIEL L. GOELZER, ESQ., General Counsel, Securities and Exchange Commission, Washington, D.C.; on behalf of the SEC as amicus curiae in support of respondents.

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C O N T E N T S

P R O C E E D I N G S

CHIEF JUSTICE BURGER: We will hear arguments next in Gould against Ruefenacht.

Mr. Epstein, you may proceed whenever you are ready.

ORAL ARGUMENT OF ROBERT C. EPSTEIN, ESQ.,

ON BEHALF OF THE PETITIONER

MR. EPSTEIN: Thank you, Mr. Chief Justice, and may it please the Court, it is our contention that Mr. Ruefenacht's right to veto every major company decision is joint management of the Continental business in which he repeatedly referred to himself as a partner and the fact that this was an entirely private transaction unique between two individuals which in no sense involved a public capital market, that these collective factors require the conclusion that in substance this was the purchase of a one-half interest in a business, and that the transfer of stock was merely incidental to the transaction.

We submit that the federal securities laws were never meant to cover this kind of a transaction, and that Mr. Ruefenacht's claims of fraud belong in state court. As authority for our position, Your Honors, we rely fundamentally upon the legislative history of the federal securities laws.

Now, it is true, as was pointed out this morning, that the legislative history does not specifically address the sale of business situation, and indeed both factions in the current judicial debate acknowledge that Congress never specifically considered the sale of business question.

However, the legislative history is replete with an unmistakeable Congressional emphasis upon the goals that the securities laws do seek to achieve. Those goals, reaffirmed in the legislative history as recently as 1982, and as expressed by this Court in Forman fundamentally were to protect the integrity of public capital markets and to protect investors dealing in those markets.

Now, the legislative history also indicates that these goals emerged from a Congressional recognition that the dispersion of corporate ownership had led to abuses in the capital markets where people who ran corporations were taking advantage of people who owned corporations.

Most importantly, Your Honors, it was recognized by Congress that the effects of such abuses transcend the individual's loss, but rather chill investment and capital formation generally.

It was also recognized by Congress that such

abuses could be perpetrated because the owners of corporations did not have managerial control over the operations of those corporations. The owners held the symbols of ownership but had no ability effectively to influence the destiny of their investment or to influence the operations or the profitability of the corporation.

There is nothing, not one word in the legislative history about protecting someone like Mr. Max Ruefenacht, who engaged in a purely private transaction, unique, as I said, between two individuals which indeed involved stock which could not have been publicly traded because it did not have a common or equivalent value to most people.

QUESTION: Well, this argument would lead to just saying that there isn't any private sale of stock that was reached by the securities law.

MR. EPSTEIN: No, Your Honor, that is not our position.

QUESTION: Well, it sounds like it so far.

MR. EPSTEIN: Well, it is not our position --

QUESTION: A purely private transaction?

MR. EPSTEIN: We are a purely private transaction.

QUESTION: Well, so are thousands of others

that are covered, I suppose.

MR. EPSTEIN: Well, that may be so, Your Honor. May I point out that where the context is a public context involving either an organized exchange or a public solicitation, such as was involved in Howey and other cases, in our view, that goes so much to the heart of what Congress was talking about when it passed the securities laws that there ought to be coverage.

Where you are dealing, however, in an entirely private context, the inquiry has to be a little deeper. That is not to say that private transactions will necessarily not be covered, but the inquiry is into the economic realities of those transactions.

And if I may at this point, in further answer to your question, Your Honor --

QUESTION: Well, if I just buy some shares of General Motors from some other person and he misresents, is that exempt from the securities laws?

MR. EPSTEIN: I don't believe so, Your Honor, because --

QUESTION: I can't imagine anything more private.

MR. EPSTEIN: Well, except for the fact, Your Honor, that there is an important public element there, and that public element is --

QUESTION: Well, what if the stock isn't registered? It is just a small corporation. I just buy some shares of a private company from another person, no public -- is that a public matter?

MR. EPSTEIN: No, Your Honor. The way you have framed that hypothetical, no, that seems to be an entirely private and unique transaction.

QUESTION: Would that be covered by the securities laws under your view?

MR. EPSTEIN: Under my view, Your Honor, an entirely private transaction like the one you just -- I would have to ask Your Honor some more questions about the facts.

QUESTION: You may.

(General laughter.)

MR. EPSTEIN: The first question I would ask would be whether Your Honor as the purchaser of that stock in a privately held corporation --

QUESTION: I would have to report it at a certain way.

MR. EPSTEIN: I understand that, Justice. Whether Your Honor participated in some fundamental sense in the activities of that corporation.

QUESTION: I just bought the stock for investment, and that is all I wanted to do.

MR. EPSTEIN: Assuming that to be true, Your Honor, I would also ask whether this stock that Your Honor bought was a smaller unit of a larger offering or whether it was --

QUESTION: No, it was just -- the stock has been in these same hands for a long time. The fellow was just tired of owning it, so he sold it to me.

MR. EPSTEIN: Not covered, Your Honor.

QUESTION: Not covered.

MR. EPSTEIN: Not covered.

QUESTION: Is that the established rule or --

MR. EPSTEIN: Well, Your Honor, there is no established rule. That is, I believe, one of the reasons that we are here today, because there is confusion, but on this point of public versus private, I would like to raise and bring to the Court's attention the Superintendent of Insurance case, which has been cited by my opponents all throughout this litigation as standing for the proposition that private transactions are covered by the securities laws.

It is true, as Justice Douglas pointed out there, that that was a private transaction. However, there was an important public element to that transaction, which was that the securities that were sold in that case were Treasury bonds.

These were securities that were, if not being publicly traded at that time, were certainly of a common or equivalent value to most people, and therefore could have been publicly traded, and therein, I submit to the Court, lies an important public interest in that private transaction.

Now, we submit, Your Honor, that there is nothing in the legislative history indicating a desire to protect someone like Mr. Ruefenacht, who, as I said, engaged in a purely private transaction, idiosyncratic, as between two individuals, which involves no public captail market.

There is nothing in the legislative history indicating a desire to protect Mr. Ruefenacht, who jointly managed this company, and who was no more dependent upon others in this business than one partner is dependent upon another partner to use his or her best efforts and inimmitable talents to make a business a success.

Indeed, may I point out to the Court that there was no one in this business who had more control over profitability than Mr. Ruefenacht, and I specifically point to Magistrate Peretti's findings on the fact that Mr. Ruefenacht's veto powers extended not just to questions of capital structure of this company,

such as the issuance or transfer of shares, but also to operational decisions going right to the heart of what this company's business was, namely, questions of borrowing money and of the taking on of new product lines.

We submit that this Court in evaluating this transaction under the securities laws cannot ignore Congress's goals simply because there was stock involved in the transaction, but in effect that is just what the Third Circuit did by looking only to the characteristics of the stock and ignoring all of the findings found by the magistrate.

We don't believe that the literal or mechanical approach taken by the Third Circuit was ever intended by Congress in the application of the federal securities laws. The legislative history urges flexibility in application of the securities laws, but does not say that the Court shall be flexible only where the result will be to extend coverage.

Also, the context clauses, whether they be viewed as relating to the economic context ofthe transaction, as we believe this Court clearly held in the Weaver case, or as relating to the linguistic context of the statute, as the Third Circuit said, in either of them, I submit to the Court that the context

clauses amount to Congressional caveats against literalism and amount to a sufficient basis for the District Court looking into the economic realities of this transaction.

Finally, as we read this Court's decisions from Joiner through Weaver, the Court has never taken a literal or mechanical approach to the securities laws, but rather has repeatedly cautioned against just such an approach.

Now, I submit, Your Honors, that the flaws in the Third Circuit's approach to the securities laws are perhaps put best in focus when one considers application of the securities laws to transactions in notes.

Under a literal approach, all note transactions would be covered including mortgage notes executed in connection with the purchase of a single family residence, and also including notes executed in connection with consumer financing transactions.

But both sides of the current judicial debate, including such eloquent proponents of the literal approach as Judge Friendly and Judge Gibbons below, both sides acknowledge that Congress just could not have meant to cover those kinds of transactions, and as a result both sides, with some variations, employ a case by case analysis in the note context to determine which

note transactions implicate federal securities laws concerns.

I submit to the Court that the very same type of case by case analysis is just as essential in the stock area for the very same reasons, namely, to avoid sweeping within the coverage of the federal securities laws a multitude of cases which involve no significant federal concern but which happen to involve stock.

One of the concerns which led the Third Circuit to rule as it did was what can be called the line drawing concern, a concern by Judge Gibbons about distinguishing covered transactions from non-covered transactions.

I submit to the Court that that concern can be greatly ameliorated by the decision in this case. A narrow holding here that Mr. Ruefenacht's absolute veto powers, joint management, and the fact that this was a unique transaction, that those factors require a conclusion that this was not a federal securities transaction --

QUESTION: What is your -- I know you say we ought to look at the economic realities and all that. I am not sure I know even what you mean. Is it your view that you should look to see if the purchase is for investment or for management or for what?

MR. EPSTEIN: The objective of the transaction, Your Honor, is one of the economic realities. That is precisely correct. And here the --

QUESTION: Well, which is it? Which is covered and which isn't?

MR. EPSTEIN: There are gradations of cases, Your Honor, and it is difficult for me to answer that entirely in the abstract. I can say to Your Honor --

QUESTION: Well, if you can't, I don't know what kind of a bright line you are drawing.

MR. EPSTEIN: Your Honor, the line we are drawing is between the kinds of transactions Congress intended to cover and did not intend to cover. Let me see if I can --

QUESTION: That is fine. Now tell me what it is.

MR. EPSTEIN: Okay. When we are dealing with "public transactions," and I put that term in quotes, Your Honor, transactions which involve the public capital markets, whether organized or not, I submit that we are involved with a situation going so fundamentally to the concerns of Congress that the federal securities laws ought to apply as a general proposition.

Where we are dealing in private transactions, Your Honor, the inquiry has to be into whether the

purchaser in this case was dependent upon the efforts of others or not dependent upon the efforts of others. That inquiry involves two components as I see it.

QUESTION: In general you are talking about whether he is making an investment or whether he is buying it to make money by himself.

MR. EPSTEIN: That is exactly correct, Your Honor. In a general sense, that is true.

QUESTION: Well, refine it if that is too general.

MR. EPSTEIN: Well, there are two components to that inquiry. Component Number One, as we see it, is the control analysis that was performed by the magistrate and by the District Court below, where someone obtains the kind of control that Mr. Ruefenacht obtained over a company.

He is not the kind of investor that Congress was seeking to protect. He is not in that peculiarly vulnerable position which generates a need for the special protections of the federal securities laws.

QUESTION: He didn't have an affirmative control, did he?

MR. EPSTEIN: He could not impose his will on the ccrporation, Mr. Chief Justice, that is correct, but what he could do --

QUESTION: He could veto.

MR. EPSTEIN: That is exactly right, Your Honor, and not only that, through his joint management of the company as a result of his efforts in obtaining sales and operations and so on and so forth, he had, as the magistrate found, a fundamental influence over whether this corporation did well or did not do well. So he was anything but a passive investor in that sense.

QUESTION: You speak to the veto power. The veto cuts both ways, doesn't it?

MR. EPSTEIN: Yes, Your Honor, in the sense that Mr. Ruefenacht could not do anything without his partner going along.

QUESTION: Exactly.

MR. EPSTEIN: That is exactly right, Your Honor. There was here a deadlock situation, but we submit that Mr. Ruefenacht's veto powers amount to fundamental control going right to the heart of --

QUESTION: But it is also a good way to protect his invetment, isn't it?

MR. EPSTEIN: In a generic sense of the term "investment," Your Honor, that is true. In a generic sense, Your Honor, almost anything that you buy can be considered an investment to the extent that you expect

to earn a living perhaps from it or to have that asset that you purchased --

QUESTION: Yes, but a veto power doesn't always have the characteristics of control. It has just got -- it is a limited partner. You may not want to control the business at all except to protect your investment.

MR. EPSTEIN: That is true. I suppose in the Weaver case, Your Honor, the Weavers were in a sense seeking only to protect their investment, but nevertheless the Court found that their measure of control simply over the borrowing of money was uncharacteristic of the security.

If I may, I would like to turn to some of the concerns that --

QUESTION: May I ask a question?

MR. EPSTEIN: Yes, Your Honor.

QUESTION: We are all trying to grasp exactly where the dividing line is. You don't take the position then, I gather, that every sale of control is exempt from the Securities Act?

MR. EPSTEIN: No.

QUESTION: It is only if there is a sale of control and the purchaser thereafter relies on the management efforts of other to produce --

MR. EPSTEIN: Yes, Your Honor, and in a private setting that would be especially true.

QUESTION: So every sale of a business to, say, a bank or a trustee which would then be -- you would have to get some outsider to manage for them, those would all be covered, 12 percent sale of the business in the other case or your business here.

MR. EPSTEIN: Again, if we are talking --

QUESTION: To a bank or a university who is going to hire some management expert to run the business for them. Covered or not covered?

MR. EPSTEIN: If we are dealing in a totally private setting, not a publicly traded security in any sense --

QUESTION: Not a publicly traded security.

MR. EPSTEIN: Then it would not be covered, and the fact that management was delegated to somebody else makes no difference.

QUESTION: So is every sale of control of an unlisted security exempt under your view?

MR. EPSTEIN: No, Your Honor. I am not making a distinction between whether a security is listed on an organized exchange. There may be closely, and I am sure there are, closely held corporations which go into the "public capital markets" to obtain funds and

as a result of going into those markets they implicate a federal securiies interest, in my view.

If there is some wide dispersion of ownership, even though the security is not listed on any exchange, the transfer of 100 percent of that security may very well still be covered because you are dealing in a marketplace.

QUESTION: Well, let me go back. Every sale by a 100 percent owner to a 100 percent purchaser of an unlisted security, always exempt?

MR. EPSTEIN: Yes, Your Honor, I believe so. I can't see a situation where it would not be.

QUESTION: All right, then the next question is, all sales of control of an unlisted security by control block, 52 percent 30, or whatever it takes to constitute realistic control of an unlisted security, always exempt?

MR. EPSTEIN: Yes, if -- yes, if that security was not of a nature which could be publicly marketable. If you are dealing --

QUESTION: Well, I mean, if it is a big company, you are always going to be publicly marketed.

MR. EPSTEIN: Well, if we are talking about a security, Your Honor, which has roughly equivalent value to most people, and I take that language from the Weaver

case, if we are dealing in that kind of security, in my view, you start to implicate the kinds of Congressional concerns that I have been trying to address.

So, I can't give you a categorical answer on that point, Your Honor. Your Honor is giving me a quizzical look, and I am trying to give you the best answer that I can, but I have to qualify it because there can be no categorical rule, I don't believe, in these kinds of situations.

As the Weaver court stated, it is important to look to the entire factual matrix. One element of that factual matrix, I submit, is the nature of the instrument, whether it was idiosyncratic to that --

QUESTION: I am assuming, you know, ordinary common stock, you know. I am not talking about idiosyncratic instruments. We have just ordinary stock. That part is easy. But I still -- I just really don't understand your distinction.

MR. EPSTEIN: Your Honor, when I talk about idiosyncratic instruments, I am talking about the kind of stock that was involved in this case, which had value only as between Mr. Ruefenacht and Mr. Burkle, and had no widespread value to anyone else, had no equivalent value, as I said before, to other people.

QUESTION: Why didn't it have value to

somebcdy else? You say they resold 10 percent to each of ten people. Why wouldn't that have value?

MR. EPSTEIN: It would have value in that sense, but it did not have the kind of value that existed between these two people. For example, one of the facts that the magistrate found was that the purchase price of the stock was in part related to Mr. Ruefenacht rendering his services to the corporation.

That is an element of the uniqueness of this transaction between these two individuals which is different from a transaction we hypothesize where the stock would be sold to somebody else.

QUESTION: But you would come out differently if it were a publicly traded security?

MR. EPSTEIN: Yes, Your Honor --

QUESTION: You would agree, sale of control of a publicly traded security with management prerogatives and all this is covered by the Act?

MR. EPSTEIN: Yes, Your Honor. Frankly, I can't distinguish that conceptually from a tender offer situation, because when you are dealing in public markets, you get so much to the heart of what Congress was talking about in the securities laws that I think the securities laws do apply in Your Honor's hypothetical.

Now, to address some of the concerns of the Court below, one concern was that application of the so-called sale of business doctrine would lead to anomalous results. But may I point out to the Court that the Third Circuit did not find that it would be anomalous in this case or inconsistent with the legislative goals in this case to disqualify the transaction from coverage.

Admittedly, there have been raised in the briefs and in the academic commentary a great number of very perplexing factual issues, and we don't purport to address all hypothetical cases today.

What we do ask the Court for is a ruling on this case, which we believe will set forth clearly the applicable principles, and the so-called anomalous cases we believe will in large measure take care of themselves.

Also, the Court below was concerned about devoting federal judicial resources to the economic substance inquiry. Now, it is true that in this case we have a two-day non-jury hearing before the magistrate devoted to the issue of control, but the projected trial time that was saved by that inquiry was far greater than two days.

Now, I cannot prove this, Your Honors, but I

submit to you that the vast majority of questions of coverage under the securities laws will be clear.

Securities involved in organized exchanges, public capital markets, widespread solicitations or offerings or purchases, those cases, in my view, are clearly covered.

Where there is a legitimate issue concerning federal securities laws coverage, which I submit will occur most frequently in the private sphere, I submit that the resources devoted to that inquiry are well worth the savings in federal trial time otherwise devoted to questions or matters which involve no significant federal concern, but which happen to involve stock.

Finally, as I started to say earlier, the Third Circuit was mightily concerned about where to draw the line. Justice Stevens' hypotheticals put that concern greatly in issue. That is a concern which, as I said, I hope this case will help to ameliorate, but I don't believe that simply by adopting a mechanical test which makes line drawing very easy is the answer to that problem.

In conclusion, Your Honors, we ask this Court to decide this case based upon the facts of this case, as the District Court did, and not based upon

hypothesized concernn in other cases which in a fundamental sense led the Third Circuit to rule as it did.

QUESTION: But I suppose you must hope that we decide the immediate preceding case in a particular way.

MR. EPSTEIN: That's right, Your Honor. That is right. I agree that the Landreth case should be decided in the same way that this case should be decided.

QUESTION: Either way. No.

(General laughter.)

QUESTION: You don't mean either way.

MR. EPSTEIN: Your Honor leads me to an interesting point, and that is the point of common venture which was raised earlier in the colloquy, and I would like to tackle that one head-on. It is a difficult point.

As we pointed out, the federal courts seem to be very confused about what is a common venture. I submit to you that there was no common venture in this case, and as authority for that position I rely upon Howey and I rely upon Weaver.

I point out to you that in the Howey case where the common venture requirement was framed, the

matter involved 42 purchasers out of a solicitation of several hundred.

I point out to you that in the Weaver case, in Chief Justice Burger's opinion, there was great emphasis at the end of the opinion on the fact that there was a privately negotiated, face-to-face transaction unique as between two individuals.

I suggest to you that juxtaposing those two cases leads to the conclusion that where you have, as in this case, a completely unique transaction between two privately contracting parties, that that is not the kind of common venture that this Court has been addressing over the last 40 years, and we therefore ask the Court based upon the facts of this case and not upon hypothesized concern or the single fact relied upon by the Third Circuit, which essentially was that there was stock involved in this transaction, we ask the Court to reverse the Court below.

Thank you.

QUESTION: Very well.

Mr. Pearlman.

ORAL ARGUMENT OF PETER STEVEN PEARLMAN, ESQ.,

ON BEHALF OF THE REPONDENTS

MR. PEARLMAN: Mr. Chief Justice, and may it please the Court, on behalf of Max Ruefenacht, the

purchaser of one-half of the shares of traditional common stock of Continental Import and Export, Inc., I submit that to accept the sale of business doctrine will require this Court to disregard accepted principles of statutory construction by ignoring the specific and unambiguous language of the securities statutes, abandon its own prior precedent and policy, and to adopt a policy which is ambiguous, unworkable, not readily definable, and which creates results which are arbitrary and unfair in the extreme.

For 50 years, and through numerous securities cases, the question of whether the federal securities laws apply to traditional common stock has not troubled this Court, nor should it now. Nonetheless, Mr. Ruefenacht has devoted the last four years of his life to litigating just that issue.

The legislation which is in issue here is the definitional section of both the Securities Act of 1933 and the Securities Exchange Act of 1934. In both circumstances, the legislation says clearly that a security is defined as a list of items including specifically "stock."

This Court does not sit as a superlegislature. It is not up to this Court or any court to determine whether Congress was wise in enacting such a

definition. The term "stock" in the statute is clear and unambiguous. It is to be given its ordinary clear meaning.

Under those prescriptions, the shares which Mr. Ruefenacht purchased, albeit a private, non-publicly traded corporation, were shares of stock, and he is entitled to remedies under the federal securities laws.

Petitioner submits that we must depart from the letter of the statute, that we must ignore its plain meaning, and that we must examine the legislative history.

The perceived intent of Congress, and when I say perceived, I mean petitioner's perceived intent of Congress, to determine what they really meant when they gave a very clear and unambiguous definition in the statute.

The simple introductory answer to that is that it is not up to a Court to examine legislative history when the statute on its face is clear, but even an examination of the legslative history does not avail petitioner in the way in which he wishes.

The legislative history itself does not evince any intent to exclude transactions such as that to which Mr. Ruefenacht and Mr. Burkle entered. Quite the opposite. This Court in its prior precedent has

uniformly stated that instruments which answer to the name of stock, which are stock, which bear the traditional attributes of stock, are securities.

This Court has said it in Joiner. This Court has said it in Tcherepnin, in Forman, and most recently in Weaver, where this Court stated that the statutory definition of a security excludes only currency and notes with a maturity of less than nine months. It includes ordinary stocks and bonds. Nothing could be more ordinary than the stock and the bonds which Mr. Ruefenacht acquired.

Petitioner submits that the respondent is attempting to engraft into the statute something which is not there. Just the opposite is true. We are dealing here today with a situation where the statute says plainly any stock. Mr. Ruefenacht acquired stock.

In fact, the attempt to toss out all other portions of the definition other than that of investment contract not only violates almost every relevant concept of legislative interpretation, but makes no sense from a general common sense standpoint.

When this Supreme Court enunciated its opinion in Howey, it specifically dealt with the case involving an investment contract, and it said that the definition of an investment contract is investment of money in a

common enterprise, expectation of profits to come from the efforts of others.

Since then, this Court has used that definition on many occasions. And on every single such occasion it has been used to define an investment contract, to see whether a particular transaction qualified as an investment contract. This Court has never applied that standard to determine whether traditional common stock was a security, nor should it.

QUESTION: What did we use in the notes case?

MR. PEARLMAN: I don't believe that this Court has made a determination on --

QUESTION: On notes?

MR. PEARLMAN: -- a specific notes case. I don't believe that this Court has spoken on that, and I recognize that there is a split in the circuits on --

QUESTION: On that? On that?

MR. PEARLMAN: -- on that issue as well. That is not before the Court today, but perhaps at some future time it will be.

QUESTION: Maybe you will be here on that.

MR. PEARLMAN: It would be my great pleasure, Justice White. It would be my great pleasure and my

great honor.

QUESTION: Well, that really is the most difficult part of your argument, isn't it? Isn't it pretty well conceded that some differentiations have to be made as to notes, and so why shouldn't differentiations be permitted as to shares of stock?

MR. PEARLMAN: Justice Rehnquist, I don't believe that it is necessary to make these differentiations with respect to notes. I do not believe that we should sit down and try and determine what "notes" should be included within the statutory definition.

I believe that the statutory definition specifically excludes certain types of notes, notes with a maturity of less than nine months, but I do not believe that the statutory definition of notes permits an examination into the underlying transaction.

I would suggest, however, that to the extent that there is some confusion with respect to notes, it may be that notes are a less commonly defined term than stock. "Investment contract" is a vague term. It is a term to which this Court has applied a certain definition.

Stock is something which is, I think Professor Lewis has said, so quintessentially a security as to

foreclose further analysis.

It may be that notes fall somewhere in between, and it may be, although I disagree, and of course, as I said, the case is not here today, but it may be that with respect to notes, it is somewhat less specific than stock.

It is perhaps somewhat vaguer and more akin to an investment contract, although not necessarily with the same standard to be applied, and it may be that some definition is necessary with respect to note, just what a note is, what type of note we are talking about.

But there is no definition which is necessary with respect to traditional stock. Stock has been defined. At least what this Court means by stock was defined. It was defined in Tcherepnin. It was defined further in Forman.

So I do not believe that whatever problems may have arisen in the circuit with respect to notes need cause a problem with respect to whether or not this Court should adopt or reject the sale of business doctrine.

Until I came here or until I read the briefs, I should say, in connection with this appeal and then was reinforced a little bit this morning and then this afternoon by Mr. Epstein, I really thought I understood

what the sale of business doctrine was. I thought the sale of business doctrine was that you looked to the economic realities of the transaction and apply the Howey test to see whether you fall into that category.

I always felt it was impossible to really come to any sort of a meaningful conclusion by use of the Howey test because it necessarily excluded certain things which no one had ever questioned were security, such as Williams Act cases, such as many publicly traded transactions, because obviously frequently when a tender offer is made, there is the intent to control. That is one of the major purposes for the tender offer.

I now find out this morning that the Howey test is not the sale of business doctrine, or vice versa, because apparently under the version of the sale of business doctrine which I heard today, you applied the Howey test sometimes, but sometimes you don't apply the Howey test. Certainly you don't apply it when you are dealing with publicly traded corporations, I guess. At least in a tender offer with publicly traded corporations.

I am not sure where the line is drawn. There you have to look to some other sort of legislative philosophy. I am not sure what that philosophy is or is supposed to be. But what you do is, you sit down and

you look at the Congressional intent, I guess, every time a securities case comes to court.

And having done that, you decide whether it is publicly traded or privately traded, and then you have to form your own concept of whether or not it is a security. The test is completely unworkable. Clearly the Howey test cannot apply to transactions involving mergers, Williams Act cases.

When the Williams Act was passed, incidentally, it was used -- it used exactly the same definitional section. If Congress had intended to make control an issue, or if Congress had thought there was a problem with control in the current definition, they could have modified that definition.

They could have given some specific statement of intention with respect to tender offer cases, the acquisition of control. They didn't, because stock is stock. So we are here today being urged to accept a doctrine which really has not been defined.

QUESTION: Well, you say that any sale of any kind of stock that any fool would recognize as stock is reached by the securities laws?

MR. PEARLMAN: I don't know if any stock that any fool would recognize as stock is reached by the securities laws. Certainly something which Your Honors

would recognize as stock would be reached by the securities laws. Perhaps something which I would recognize --

QUESTION: Well, a fortiori if a fool would even recognize it.

(General laughter.)

MR. PEARLMAN: I am sure that was intended to reflect my recognition.

QUESTION: Anyway, you think that stock is stock, any sales stock is covered.

MR. PEARLMAN: Any sale of what is really stock is covered. I recognize the problem that arose in Forman, and without necessarily agreeing or disagreeing with whether or not that was traditional stock and whether it should have been considered stock, I recognize that there are circumstances when having called something stock doesn't mean that it really is stock. You can suggest that the world is flat. That doesn't mean that it is.

There are a number of policy considerations which favor the rejection of the so-called sale of business doctrine. The primary, and the one that first comes to mind, is the fact that the Securities Acts are to be construed liberally to enhance their remedial intent.

Certainly attempting to strike from the definition something which is clearly there, something which is unambiguously there does much damage to and doesn't benefit in any way the remedial intent of the securities laws.

The problem with control is something which I have already discussed, and that is not only does any test which is premised on control exclude transactions which I don't think anyone would ever intend be excluded, but it is very difficult to define control, as to when the control was to be exercised, what is control under any given circumstance, and the Ruefenacht case illustrates that, I think, rather well.

There has been some suggestion that when a person acquires control they don't really need the protection of the federal securities laws, because they have the ability to control the destiny of the business.

I suppose the simple answer to that is that the federal securities laws apply to fraud which took place before you assumed your control, and about the best you can do once you have assumed this control, whatever it is, is to be in a good position to grab the bucket and start bailing. It hardly is a good justification, however, for adopting the control

standard.

I suggest therefore that this Court reject the sale of business doctrine as it is carved out of whole cloth, having taken -- having made an attempt to add to the statute something which was never there in the first place by arguments which have no basis in logic and no basis in law, and affirm what I think my counsel that took the same position as I take today in Landreth this morning described as the scholarly opinion of Judge Gibbons of the Third Circuit.

I consider it well reasoned, and I wholeheartedly hope and expect that this Court will agree. I have nothing further to say affirmatively. I would be honored to answer any questions this Court may have of me.

CHIEF JUSTICE BURGER: None, apparently.

MR. PEARLMAN: Thank you.

CHIEF JUSTICE BURGER: Mr. Goelzer.

ORAL ARGUMENT OF DANIEL L. GOELZER, ESQ.,
ON BEHALF OF THE SEC AS AMICUS CURIAE
IN SUPPORT OF RESPONDENTS

MR. GOELZER: Thank you.

Mr. Chief Justice, and may it please the Court, in defining what is a security, Congress used the plain term "stock," and the stock in this case is the

garden variety of that type of instrument. Nowhere in the Securities Act or in the Securities Exchange Act did Congress suggest that sales of this sort of ordinary stock were ever to be excluded from the securities laws.

The petitioners' case rests in part on the notion that only passive public investors were intended to enjoy the protection of the securities laws, that those who engaged in private negotiated transactions where they have some ability presumably to extract information for themselves are not within the protection of the securities laws.

But Congress, I think, considered that issue and reached a different conclusion. Section 4 of the Securities Act of 1933 contains exemptions from the registration provisions of the Act. Almost 30 years ago, in SEC versus Ralston Purina, this Court construed the private placement exemption as excluding from registration and its disclosure obligations transactions where the purchaser can fend for himself or have obtained his own access to the sort of information that registration would supply.

Congress made clear in the introductory phrase to Section 4 that transactions excluded from registration were included in antifraud protection. I

think the arguments that petitioner makes here in this regard were simply considered by Congress, and the place it drew the line was between registration and antifraud protection, not by excluding these private transactions from the scope of the securities laws.

Petitioner argues that ordinary common stock is not stock at all when it changes hands in a transaction where the buyer acquires some measure of control over the issuing company, but if this Court were to adopt that theory, it would multiply the complexity and expense of both SEC and private securities litigation.

I would like to consider Commission litigation first. Under the test the petitioner advocates, Commission enforcement actions would necessarily become more complex for reasons having little or nothing to do with Congress's objectives in enacting the laws.

Petitioner argues in essence that every time a judge is confronted with a securities transaction, he needs to make his or her own decision concerning whether Congress intended federal protection to apply to that transaction.

Thus even if the Commission were to prove that a violation had occurred under the ordinary meaning of the laws, would still be open to the defendant trying to

convince the Court that there was something in Congress's spirit or intent not manifested in the words which provided a defense.

QUESTION: Mr. Goelzer, if your view is adopted by this Court, what is it likely to do to the numbers of cases dealt with by the Commission? Will it increase the numbers, do you think?

MR. GOELZER: If my view is adopted, I think it won't have any effect on the number of cases that the Commission deals with, since it has always been the Commission's assumption since 1933 and 1934 that any transaction in ordinary stock is within the scope of the securities laws.

The Commission would not typically bring an enforcement action in a case involving a transaction between two private parties simply because it wouldn't be a good use of our resources, although --

QUESTION: Is it likely to increase the numbers of cases filed in federal courts, do you think, to any significant degree?

MR. GOELZER: I think not, Your Honor. It certainly wouldn't increase them beyond what they were before 1980 or 1981, since no Court had suggested that this sale of business doctrine existed at all before that time. I think if the doctrine is adopted, if the

petitioner's position is adopted, we will have at least the same number of cases, but they will all include a long threshold consideration of whether control, a very subjective and amorphous concept, existed in the case or not.

QUESTION: What is the Commission's position concerning notes, and what type of meaning should be adopted for that word in the statute?

MR. GOELZER: Well, as was pointed out earlier, this Court, of course, has not considered the meaning of the term "note" in the --

QUESTION: No, I asked what the Commission's position is.

MR. GOELZER: Well, as I would with stock, I would begin with the literal term of the statute, and start with a presumption that any note is included within the scope of the Act. The lower courts have held, and the Commission doesn't disagree with it, that there are certain families, certain categories of notes that were not within Congress's intent that would relate primarily to notes issued in commercial transactions, mercantile transactions to finance inventory, for example, or for consumer purposes.

Other than those rather specialized exemptions or exceptions, I would say that a note is within the

scope of the definition. I think it is not -- the definition of security contains many terms. Stock is one. Note is one. Investment contract is another.

I think it is not surprising that each term has its own specialized meaning and its own body of case law interpreting it, but as I said earlier, in this case there is no question, no one has suggested that it is not conventional stock that is involved.

I think that a second way in which Commission enforcement actions would be significantly burdened if the petitioner's position were adopted is that inherent in that position is that each security transaction must show that it meets the definition of investment contract, yet the Commission often brings actions that involve instruments that don't promise a share of profits. Rather, they promise a fixed return to the invesntor.

The lower courts have disagreed concerning whether a fixed return meets the profit element of the Howey test, yet if it doesn't, such ordinary things as long-term corporate bonds issued by blue chip companies would be excluded along with irregular and unusual instruments issued by individual promoters.

At best, the Commission would be forced to relitigate all of this ground, presumably already

covered during the past 50 years under the doctrine.

I think it is also worth pointing out that the position the petitioner urges would result in arbitrary and illogical distinctions in private litigation. For example, in this case, if Mr. Ruefenacht had purchased his 50 percent interest in Continental in a series of five transactions of 10 percent each, presumably the first four would form a basis for federal litigation, the last would not, or if in the same transaction in which Mr. Ruefenacht purchased, his brother had purchased 5 percent of the stock based on the same representations that were made to Mr. Ruefenacht, the brother would apparently have a cause of action, Mr. Ruefenacht would not.

And if Mr. Ruefenacht had purchased his controlling interest from ten shareholders, each with 5 percent, apparently he would not have a cause of action against them. Would they have a cause of action against him?

They would seem to be the sort of people that Congress intended to protect, even under the petitioner's theory: passive, non-controling investors. Yet the petitioner says there was no securities transaction involved.

One circuit, the Seventh Circuit, has

suggested that there is a securities transaction for the sellers but not for the buyers. I think that leads to a good result, and I would support it, but I think the logic of the same transaction being or not being a securities transaction depending upon whether you are plaintiff or defendant, is illusive, and the issue would undoubtedly be litigated in the lower courts and perhaps ultimately brought back to this Court.

Finally, I would point out that adoption of the sale of business doctrine will inject great uncertainty into business transactions. Any time that a significant amount of stock is purchased, the parties will have no definite way of knowing whether they have possible liabilities and possible rights under the federal securities laws.

All that, no matter how sophisticated the advice they might get from counsel, all that will have to await litigation in the federal courts over this illusive and difficult issue of control.

Absent some clear directive from Congress that the securities laws were intended to create this sort of uncertainty, or that it is a necessary consequence of them, I think this Court should be reluctant to create it.

For nearly 50 years, the business community,

the Courts, and the Commission have taken Congress at its word and assumed that any purchase or sale of ordinary corporate securities, whether -- corporate stock, whether between sophisticated or unsophisticated parties, was within the antifraud protections of the securities laws.

If petitioners or others believe now that that determination should be changed, they should address their arguments to the Congress, not the Courts.

Thank you.

CHIEF JUSTICE BURGER: Do you have anything further, Mr. Epstein?

ORAL ARGUMENT OF ROBERT C. EPSTEIN, ESQ.,

ON BEHALF OF THE PETITIONER

MR. EPSTEIN: Yes, briefly, Your Honor. My remaining --

CHIEF JUSTICE BURGER: You have four minutes remaining.

MR. EPSTEIN: Thank you, Mr. Chief Justice.

I first would like to address Justice O'Connor's question about what will the result in this case do to the workload of the federal courts. This is, of course, theoretical, but I submit to the Court that especially with the increased awareness among practitioners of this issue, that if the sale of

business concept is rejected, tha plaintiff's lawyers will be constrained to bring all cases that in any tangential way involve stock and an allegation of fraud in federal court.

Plaintiff's lawyers, I submit, would be remiss if not negligent in failing to bring those cases in federal court so as to take full advantage of the easier burden of proof under the federal securities laws and of the broader privity requirements.

Secondly, a great deal has been made about the so-called structure of the securities laws and how that supposedly indicates a Congressional intent on the sale of business question. I submit that is an incorrect argument for the simple reason that both sides of the current debate recognize that Congress never considered this question, and if Congress never considered this question, I think that the better place to look for the Congressional intent is not to the structure of the Acts but to the legislative history of the Acts.

Finally, the point has been made that control or the passing of control should have no relevance because fraud very often takes place before control passes. Well, there are several answers to that.

Answer Number One is that as Congress saw it, the dependence of the investor defines whether he was

the kind of person that should receive protection of the securities laws, and the passage of control defines whether the individual was dependent.

Secondly, in the investment contract context, in the Howey case context, I think all sides recognize that the control analysis is very important to the third prong of the Howey test, and it is important because it gives courts a pathway to the legislative intent and a means to evaluate whether the investor involved in a particular case is in that peculiarly vulnerable positicn which Congress sought to address.

Thank you, Your Honors.

CHIEF JUSTICE BURGER: Thank you, gentlemen. The case is submitted.

(Whereupon, at 1:53 o'clock p.m., the case in the above-entitled matter was submitted.)

CERTIFICATION

Alderson Reporting Company, Inc., hereby certifies that the attached pages represents an accurate transcription of electronic sound recording of the oral argument before the Supreme Court of The United States in the Matter of:

#84-165 - W. GEORGE GOULD, Petitioner V. MAX A. RUEFENACHT, ET AL.

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BY Paul A. Richardson

(REPORTER)