

TRANSCRIPT OF PROCEEDINGS

IN THE UNITED STATES SUPREME COURT

DAVID CARPENTER, KENNETH P. FELIS)
AND P. FOSTER WINANS,)

Petitioners,)

v.)

UNITED STATES.)

No. 86-422 .

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SUPREME COURT, U.S.
WASHINGTON, D.C. 20543

Pages: 1 through 43

Place: Washington, D.C.

Date: October 7, 1987

Heritage Reporting Corporation

Official Reporters
1220 L Street, N.W.
Washington, D.C. 20005
(202) 628-4888

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4 AND P. FOSTER WINANS, :

5 Petitioners, :

6 v. : No. 86-422

7 UNITED STATES :

8 -----x

9 Washington, D.C.

10 October 7, 1987

11 The above-entitled matter came on for oral argument
12 before the Supreme Court of the United States at 11:00 a.m.

13 APPEARANCES:

14 DON D. BUCHWALD, ESQ., New York, New York, on behalf of the
15 Petitioners.

16 CHARLES FRIED, ESQ., Solicitor General, Department of Justice,
17 Washington, D.C., on behalf of the Respondent.

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1 adversely affect the newspaper's reputation. This kind of
2 wrong, we submit, however one may view it, is simply not what
3 was intended to be covered by the securities laws, even if the
4 wrong is cast in terms of the misappropriation of information.

5 The securities laws were designed to protect market
6 participants from fraud, and not employers from potential
7 damage to their reputations. Just as the mail and wire fraud
8 statutes protect persons from fraud in their capacities as
9 property holders, the laws proscribing securities fraud protect
10 persons from fraud in their capacity as investors or
11 participants in market transactions.

12 QUESTION: Mr. Buchwald, can I ask you a question
13 right there? Supposing -- I know the theory of the case as-
14 tried was a little different. But supposing, on precisely the
15 same facts, there had been an allegation in the indictment or
16 the complaint, or whatever it was, that said, "as a by-product
17 of this scheme, investors were injured, those who sold or
18 purchased from, Winans?" They just threw that in and then they
19 proved it. Would that amount to a -- would there have been a
20 violation then?

21 MR. BUCHWALD: There would not, Your Honor.

22 QUESTION: In that you could reasonably conclude that
23 there was some injury to market participants as a result of
24 this?

25 MR. BUCHWALD: We would submit that that would not

1 suffice, that there must be fraud upon the market participants.

2 Here, Justice Stevens, what we have as Foster Winans'
3 trading on what he perceives will likely be the market impact
4 of the accurate articles that he is writing and that, we
5 submit, is no different than a situation where Salomon Bros.
6 may trade knowing that their very well-known economist partner,
7 Murray Kaufman is going to be making a speech in the afternoon,
8 in which he gives his opinion that interest rates are going
9 down, and Salomon Bros., in anticipation of the market impact
10 of that speech, buys into sensitive stocks in the morning.

11 QUESTION: But in the short answer, you are saying
12 that, taking these facts, even if they had alleged and proved
13 adverse market impact as a result of the fraud, that would
14 still not be a violation because -- because what?

15 MR. BUCHWALD: Because a market participant must be
16 defrauded in that capacity as a market participant, and that
17 that is the reach of the securities laws. It is not sufficient
18 that there simply be a fraud, assuming that Winans' conduct
19 here vis-a-vis the Wall Street Journal is a fraud, which is a
20 premise we dispute. It is not sufficient that there be a fraud
21 upon a third party, which who himself, has no interest in the
22 purchase, sale or value of securities and is not participating
23 in a securities transaction; and then that fraud somehow
24 relates or impacts upon --

25 QUESTION: But why is this any less of a fraud on the

1 market participants than if the information that gave him an
2 advantage in trading was corporate information instead of
3 information about the timing of his columns?

4 MR. BUCKWALD: It would still not be a fraud on the
5 market participants unless there was a pre-existing
6 relationship between Mr. Winans in this case and the people
7 selling him the stock that he buys in advance of the column,
8 which gave rise to a duty to disclose that information.

9 QUESTION: But you never have that on a trade on the
10 open market.

11 MR. BUCHWALD: Well, in the cosmic sense, that I
12 think that the securities laws presume in the discloser's
13 staying -- obligation exists even when you have open market
14 transactions. And the existence of that relationship occurs
15 where you have a pre-existing relationship to the corporation
16 whose securities are being traded; there, as in essence, say a
17 fiduciary or trustee of the corporation's information, the
18 securities laws presume that you are a trustee or fiduciary of
19 the information of all of the shareholders.

20 QUESTION: What if the insider uses inside
21 information that pertains not to his own corporation but to
22 another corporation that this corporation somehow, somehow
23 happens to have acquired? And he uses that to purchase shares
24 of that other corporation -- you would say that that would not
25 be within the securities laws either?

1 MR. BUCHWALD: That that would not be in the
2 securities laws because there is no -- that is really the
3 situation of Tiorello, where you have information that emanates
4 from the acquiring company side, and you then use that
5 information in the -- to buy stock of the company to be
6 purchased -- the target company.

7 And while that Tiorello kind of situation is now
8 covered by Rule 14e-3, the 10b analysis, it would not apply
9 because there is no pre-existing relationship that gives rise
10 to the duty to disclose.

11 QUESTION: Counsel, do you concede there was
12 impropriety here, however?

13 MR. BUCHWALD: I think that there clearly was an
14 ethical breach by Mr. Winans --

15 QUESTION: Is there any remedy for this kind of
16 thing?

17 MR. BUCHWALD: Yes. There is the remedy that the
18 Wall Street Journal took. They fired him. They wrote about
19 him on the front page of their newspaper; went into every
20 aspect of his personal life, both that relevant to the ethical
21 breach and that not relevant to it, and effectively have
22 drummed him out of the profession.

23 QUESTION: But there is no judicial remedy of any
24 kind?

25 MR. BUCHWALD: There is no judicial remedy, Your

1 Honor because there is no fraud that he has committed within
2 the meaning of any state law, or within the meaning of any
3 federal securities law.

4 There are potential civil remedies, if the Wall
5 Street Journal can establish some kind of --

6 QUESTION: But why is there no fraud sufficient for a
7 mail fraud or wire fraud, purposes?

8 MR. BUCHWALD: Justice O'Connor, there are I guess
9 three main reasons that we have on the mail and wire fraud
10 side. Number one, that the simple -- that the breach of a
11 private policy: of the undisclosed breach, of a private
12 policy, is not a criminal fraud.

13 Now number two, that here the only --

14 QUESTION: But the cases have been pretty generous in
15 looking at different schemes or artifices, as sufficing for
16 purposes of a fraud.

17 MR. BUCHWALD: I think that they have -- that there
18 has been, certainly pre-McNally, Your Honor, a tendency to be
19 very expansive in the view of what is fraud, and that many
20 cases in the Circuits have suggested that whenever one violates
21 a rule of one's employer, there is potential mail or wire fraud
22 exposure.

23 QUESTION: But you said there were three reasons.
24 You think there is no fraud? We might disagree on that.

25 Now, what is the next reason?

1 MR. BUCHWALD: Our position is that, the kind of
2 injury which is asserted here, namely a putative reputational
3 injury, is not the kind of injury that is cognizable under the
4 mail or wire fraud statutes.

5 QUESTION: Well, it is more than that. It is
6 "reputation" with an economic effect. I do not think any of
7 our cases have dealt with it in such a way such as to indicate
8 that could not be enough.

9 MR. BUCHWALD: But the suggestion, the process -- the
10 district court held not that there was, in fact, reputational
11 harm here; not that Winans intended reputational harm, but that
12 because he could contemplate that, if his unethical conduct was
13 discovered and became public, though that was not his aim,
14 obviously; that that could cause diminished reputation of the
15 employer and that, in turn, could have economic impact on the
16 Wall Street Journal.

17 QUESTION: Do you not think that the employer, that
18 the Wall Street Journal had maybe a property right in its
19 publication schedule? Is that not a sort of a business secret?

20 MR. BUCHWALD: Well, the short answer, Justice White,
21 is I think that there can be a property interest in the
22 publication schedule, but the question is, in what way are they
23 deprived of that property interest by Foster Winans' conduct?

24 They -- when I use --

25 QUESTION: Well, it was certainly no longer a secret

1 that they, if they --

2 MR. BUCHWALD: But, if Foster Winans, for example --

3 QUESTION: -- have not been deprived, if they were
4 trying to keep that secret and it is suddenly given out to a
5 limited number of people, it is no longer a secret.

6 MR. BUCHWALD: But the fact of secrecy has no
7 independent value, we submit, except vis-a-vis, competitors.
8 If Foster Winans were to have told his mother about the
9 interesting article that he had written that was going to
10 appear on Monday's newspaper, thought that would be a violation
11 of the Wall Street Journal policy, it does not hurt. There is
12 no economic impact.

13 QUESTION: Whatever property interest the paper has
14 is suddenly gone. So you are really saying there are really no
15 property interest that needs to be considered?

16 MR. BUCHWALD: What we are saying is, the only way
17 that a property interest can be said to exist is in the
18 exclusive use of the knowledge, and that that is a meaningful
19 interest only vis-a-vis competitors.

20 QUESTION: Mr. Buchwald, why is that so? I assume
21 that, I assume that one reason the Wall Street Journal is
22 purchased by a lot of people is that they read articles such as
23 this one about a company that may contain public information,
24 but it brings it all together and I say, "gee, if I read that
25 article and purchase that stock right away, I will get a rise

1 of 30 points," let us say.

2 [Mirth.]

3 To the extent that Mr. Winans, or anybody else, leaks
4 in advance the fact that this article is coming out, or using
5 his, the knowledge that the article is coming out, to make a
6 profit, the rise will not be 30 points; it will be 29 1/2
7 points. I mean, he milked some of that rise. Now, why is that
8 not something of value to the Wall Street Journal?

9 Indeed, why would not the Wall Street Journal itself
10 trade on the knowledge that it is coming out with an article?
11 The only explanation I have is that it knows that, if it traded
12 on that, the jump would not be as much and its articles would
13 not be as -- have as much of an impression. And therefore they
14 would not sell as many newspapers. Now why is that not
15 something of value that he has taken away? The half-point
16 spread?

17 MR. BUCHWALD: The Journal itself, and very
18 specifically, and at trial, through its testimony, disclaimed
19 any intention of giving market advice to its readers, or to
20 recommending or suggesting they buy or sell stocks.

21 QUESTION: People just read it from general interest?

22 [Mirth.]

23 MR. BUCHWALD: It does not seem to me that the
24 Journal could claim to be defrauded with respect to a function
25 which it specifically denies that it has. And a purpose that

1 it specifically disclaims with respect to the column.

2 QUESTION: Estoppel? Is it estoppel you are arguing
3 here? Estoppel? Is that why this theory cannot be used?

4 MR. BUCHWALD: This theory could not be used because
5 it is not charged at all. They were -- the first time there is
6 even mention of a potential value of the column as an
7 investment advice vehicle to investors, which the Journal
8 itself, therefore, has a property interest in, is in the
9 supplemental post-McNally brief. That argument was never made
10 below.

11 Your Honors, if I might return to the -- well, let me
12 follow up the argument about reputation while we are here. It
13 seems to me, if you can follow a process of "my ethical breach,
14 which is not itself illegal conduct, but my ethical breach, if
15 it is discovered, can cause reputational damage to my employer
16 -- that might have economic fallout; therefore I am guilty of a
17 federal mail and wire fraud, assuming the requisite mailings
18 and wires."

19 What you have done, essentially, is elevated every
20 employee ethical breach into a federal crime. You have given
21 federal prosecutors a vehicle, even though you start with
22 conduct that is not illegal, for establishing a process, if it
23 is discovered -- though that is not intended, if the public
24 therefore thinks less of your employer, though there is no
25 finding that that occurred here, and indeed, every indication

1 is that it did not occur here -- and if that reputational
2 damage can translate somehow into economic harm.

3 So all ethical breaches by employees are elevated to
4 the status of federal crimes, and we submit that quite aside
5 from trivializing the criminal law as that would do, and quite
6 aside from federalizing the rules pertaining to employee
7 ethical breaches, and quite aside from the enormous discretion
8 that this places in the hands of prosecutors, that there are
9 three additional reasons on the facts of this case why that
10 putative reputational damage cannot translate into the kind of
11 economic injury which McNally requires the schemers aim for.

12 Number one is, that on the facts of this case, and
13 the testimony is undisputed, the Wall Street Journal had never
14 made known its policy to the readers or to the public prior to
15 the events of this case. That it never appeared in the
16 newspaper, and never appeared in any public filing of the Wall
17 Street Journal's -- and therefore reliance by members of the
18 public on the existence of the policy or on adherence to the
19 policy, had never been invited.

20 The second reason is that the Court -- this Court has
21 held in construing the term, "property," within Paul v. Davis,
22 in the context of state deprivation of property without due
23 process of law, that property does not include reputation. And
24 with respect to interpreting the 1868 civil rights amendment,
25 the 14th Amendment, 'it seems to me that the relatively

1 contemporaneous mail and wire fraud statute, we should not
2 assume that Congress --

3 QUESTION: Well, I think that in Paul v. Davis, the
4 Court really just said that reputation alone, apart from some
5 more tangible interest, such as employment, or so forth, would
6 not. So I think you are reading a lot more into that case than
7 is warranted.

8 MR. BUCHWALD: Justice O'Connor, the think about
9 reputation, and the facts there, it were the case that, because
10 the plaintiff there had been defamed and called a "pickpocket,"
11 and therefore it was less likely that he would be employed by
12 the bank as a teller, or less likely that he would get any one
13 of a number of employment opportunities, the damage to
14 reputation could only, as a theoretical level, as a putative
15 injury concept, be stretched out to mean "potential economic
16 harm."

17 So it seems to us that, while I think Your Honor is
18 quite correct, that Paul v. Davis simply went off on a
19 "reputation" concept, reputation, the value of my name, the
20 value of reputation, is the way it translates economically.

21 QUESTION: Congress could, in the mail fraud statute,
22 define "property" more broadly than we said it was defined by
23 the Constitution in Paul v. Davis, could it not?

24 MR. BUCHWALD: I think that is clearly the case. We
25 do not mean to suggest that, because of the interpretation in

1 one, but the relatively contemporaneous nature of the statute

2 --

3 QUESTION: But you say it has not done so yet?

4 MR. BUCHWALD: That is correct, Your Honor. And we
5 believe that it would be unwise to do so for the very reason
6 that we have here, that you elevate an ethical breach into a
7 federal crime if the ethical breach, if discovered, could cause
8 reputational injury.

9 QUESTION: But your argument is only partly that it
10 would be "unwise," I take it. Your argument is basically
11 against constructive crimes.

12 MR. BUCHWALD: That is correct, Your Honor. That is
13 correct, Your Honor. At -- here, as I go through the litany of
14 things that we believe are wrong with using reputational damage
15 as the fulcrum for mail and wire fraud injury, the third reason
16 that we would give here, is that there is simply no intent by
17 these Petitioners to deprive the Wall Street Journal of its
18 reputation. And we think that McNally has set forth a
19 requirement in defining what is the "scheme" that there be an
20 intent to deprive the victim of money or property.

21 Here the pre-McNally concurrent findings of fact
22 below, were that, was that there was no intent and that,
23 indeed, it was the aim of the -- of Mr. Winans' and the co-
24 Petitioners, to maintain the reputation and the journalistic
25 integrity of the articles, because, in the words of the courts

1 below, "only if that reputation were maintained," could their
2 hopes, or their perception that the articles would have impact,
3 and therefore that their trades would be profitable, only if it
4 were maintained, could that arrangement succeed.

5 Turning, if I might, back to the mail and wire fraud
6 -- well, let me just address one other point with respect to
7 the mail and wire fraud statute, and then turn to the
8 securities law: we have also argued as a third grounds for
9 reversal of the mail and wire fraud convictions, that the
10 mailings and wirings here, what is alleged is that the printing
11 of the Wall Street Journal articles, and that the mailings of
12 the Wall Street Journal to subscribers the following day were
13 "wires and mails" caused for the purpose for this scheme to
14 deprive the Wall Street Journal of property.

15 And if one focuses on the publication schedule, or
16 the exclusive use of the publication schedule is that which is
17 deprived, even in this context of it not going to a competitor,
18 of it not going to the New York Times, as the property that is
19 deprived, on the facts here, that all occurs on the day
20 preceding publication of the article, when there is a leak in
21 the information, when the initial purchase of stock in
22 anticipation of the article, occurs.

23 So if that is a cognizable property deprivation, it
24 is something which has fully occurred before the wires, before
25 the mailings, of the Wall Street Journal, and in no sense can

1 those wires or mailings be said to be caused for the purpose of
2 executing the scheme to defraud.

3 There is no fraud alleged here nor, in fact, was
4 there a fraud upon the readers of the Journal or on the
5 investors. And so even though that subsequent publication may
6 enable, may cause to exist, that process by which Winans
7 believes he is going to be successful in the stock market, that
8 is not the cognizable fraud that is alleged on the Wall Street
9 Journal in the mail and wire fraud counts. And therefore,
10 these mailings and wires, if that language, "cause for the
11 purpose of executing," has any meaning, are not sufficient
12 here.

13 With respect, if I might return to the securities law
14 point: we believe that the requirement of fraud that the
15 participants in market transactions, how investors be
16 defrauded, follows from the language of the statute, for which
17 the misappropriation theory is not a substitute. One must, in
18 each case where the government alleges that misappropriation
19 has occurred, look to the particular conduct which the
20 government asserts constitutes that misappropriation, and then
21 determine if that conduct constitutes "a manipulative or
22 deceptive device or contrivance employed in connection with the
23 purchase or sale of securities," as Section 10b requires, and
24 is it a fraud, as Rule 10b-5 requires?

25 And those terms in turn, have come to have recognized

1 meaning. A "manipulative or deceptive device or contrivance"
2 prescribes conduct directed at investors. The hoodwinking of
3 investors, either indirectly through manipulations, watched
4 sales, matched orders, things aimed at the market as a whole,
5 but designed to affect individual investor conduct, or the
6 "hoodwinking of investors directly through deceptions,
7 falsehoods, half-truths, or silence, where there is a duty to
8 speak."

9 And that fraud under Rule 10b-5 encompasses
10 "deceptions or manipulations designed to affect an investment
11 decision to the economic detriment of a market participant, or
12 to deprive a person of investment value."

13 Virtually by definition, a private wrong endangering
14 an employer's reputation is not what the securities laws are
15 about. There are, when you have an alleged misappropriation,
16 there are two directions that you look instead of the
17 traditional one direction. You look to see if the conduct
18 defrauds the seller of the stock that you are buying, and you
19 can look to see if the conduct defrauds the person or entity
20 from whom this information is allegedly misappropriated. And
21 you ask yourself in each instance, "is that a securities
22 fraud?"

23 With respect to that first view, is the seller
24 defrauded? That is not something that is alleged here because
25 it could not be alleged under the Court's holding in Chiarella

1 that there is a "requirement of disclosure with respect to
2 informational advantages only where there is a pre-existing
3 relationship which gives rise to the duty to disclose."

4 And with respect to the second view here, is there a
5 securities fraud upon the entity from whom the information has
6 been misappropriated -- has the printer, Chiarella, defrauded
7 the acquiring company in that case by virtue of the
8 misappropriation, has Winans here committed a securities fraud
9 upon the Wall Street Journal by virtue of misappropriation?

10 If the answer to that question is "yes," in
11 Chiarella, it is because the acquiring companies are defrauded
12 in their capacity as investors and in their capacity as market
13 participants. And we submit that certainly is not the case
14 with respect to the Wall Street Journal.

15 Your Honors, the whole notion that a private employer
16 can make a special securities law for his employees simply does
17 not make sense. Here we had a Wall Street Journal rule
18 presented to its employees as intended to go beyond the
19 requirements of the law, and suddenly it has the force of the
20 law.

21 Let us suppose that that rule said explicitly what we
22 believe it means implicitly, namely that, "here at the Wall
23 Street Journal, we want to follow the highest ethical
24 requirements, while we recognize that the equal access to
25 information rule was not accepted by the Supreme Court majority

1 in the Chiarella decision, we nonetheless believe that it
2 represents a higher standard of ethics, which we want Wall
3 Street Journal employees to follow, so that we may have the
4 highest reputation.

5 If you do not follow the equal access to information
6 rule, your employment here will be terminated."

7 That, in essence, is what happened here. That, as a
8 matter of internal policy, policy which the Wall Street Journal
9 made up on pain of firing those who do not follow the policy,
10 that by adopting that rule, the government claims that
11 therefore the securities laws are changed with respect to the
12 employees of the Wall Street Journal.

13 Your Honors, we submit that, if Congress wants to
14 pass a statute which says that, "utilization in the stock
15 market of an informational advantage in violation of a private
16 contract with anyone is a new species of crime," that is fine.
17 Because then we will all know what the rules are.

18 But to try to stuff that result, in effect, into
19 existing securities fraud legislation, is simply to rewrite the
20 law to give it a new ex post facto interpretation, and we
21 submit, is contrary to the very integrity of the law.

22 Mr. Chief Justice, if I might reserve the balance of
23 my time?

24 CHIEF JUSTICE RHENQUIST: Thank you, Mr. Buchwald.

25 We will hear now from General Fried.

1 ORAL ARGUMENT BY CHARLES FRIED

2 ON BEHALF OF THE RESPONDENT

3 MR. FRIED: Thank you, Mr. Chief Justice, and may it
4 please the Court.

5 Just a few preliminary things to clear up. It should
6 be quite clear that, in our view, the property which was
7 misappropriated here was not reputation. It was confidential
8 information. That was the property. And as to that, there
9 was, of course, a very clear intent to deprive. A very clear
10 intent to misappropriate the confidential information.

11 QUESTION: You are speaking now to the mail fraud
12 count or to the securities count?

13 MR. FRIED: In fact, in that respect, I speak to both
14 counts, but certainly to the mail fraud count. The harm comes
15 about via the reputation which was put at-risk. The fact that
16 they did not intend to get caught, I think, is not a
17 particularly compelling -- answer to that point.

18 Now, there is another issue that has been raised
19 which, I feel, must be answered at the outset.

20 QUESTION: Excuse me, this would have been an offense
21 even if there had never been any publication of the fact that
22 this is what Winans did, putting the reputation at-risk
23 constitutes damage?

24 MR. FRIED: Oh, it certainly does. I think Judge
25 Stewart, in his findings, and we set out this point in our, in

1 a footnote in our Supplemental Brief, made the point very well.
2 THE information was the property of the Wall Street Journal.
3 If somebody takes my car, Justice Scalia, and returns it with a
4 full tank of gas and no dents, it is not okay for them to say,
5 "oh, nothing happened." They have deprived me of my car.
6 True, they did not intend to get caught, and they did not get
7 caught until they brought the car back. But nevertheless they
8 deprived me of my property and they put it at-risk in ways
9 which I am entitled to prevent being put at-risk. I am lucky
10 there were no dents, but there might have been. And I am
11 entitled to control that property to prevent that happening.

12 That, I think is just what Judge Stewart meant in his
13 findings.

14 QUESTION: Does not fraud ordinarily require that the
15 same respect in which you are damaged I am benefitted? For
16 example, if someone pays me money to trick you into burning
17 your house down, it does not seem to me I could be prosecuted
18 for defrauding you of your house? It would be a very strange
19 use of the word, "defraud."

20 I somehow have to get the benefit from what you are
21 deprived of, and that is what I do not see here. There may
22 have been either an actual harm to the reputation, or a threat
23 to the reputation, but it is not that same harm to the Wall
24 Street Journal which constitutes the benefit to the person who
25 allegedly did the defrauding.

1 MR. FRIED: In fact, I would differ there. I think
2 there is considerable symmetry between the mechanism of
3 benefit, I would say, Justice Scalia, on one hand, and the
4 mechanism of the potential harm on the other: the mechanism of
5 benefit to Winans and his confederates is that people believe
6 in this column and do not imagine that, in fact, all this stuff
7 has been traded upon and it is just to be discounted.

8 If it were not for that conviction -- your questions
9 to Mr. Buchwald earlier pointed that out -- if it were not for
10 that conviction on the part of the readers, the fraud would not
11 have its effect. So the reputation is there on both sides. It
12 is the very thing that the Wall Street Journal is selling its
13 newspapers on, on one hand.

14 Now, that is not very much money on any particular
15 day, but over the years it mounts up. That is the very thing
16 the Journal is selling its newspapers on on the one hand, and
17 it is the very thing which Winans and his confederates are
18 profiting from on the other. So I think that there is quite
19 considerable --

20 QUESTION: But not what they sought to deprive the
21 Journal of, as was pointed out by your opponent. To the
22 contrary, they did absolutely not want to deprive the Wall
23 Street Journal of its reputation. The continuation of its
24 reputation was essential to their scheme. They were not
25 depriving it of its reputation.

1 MR. FRIED: No, they were depriving it of the
2 information. The information was valuable to the Wall Street
3 Journal and its confidentiality was valuable to the Wall Street
4 Journal. The fact that nobody outside knew what the column
5 would be and what day it would run was valuable to the Journal
6 and it was very valuable to Winans and his confederates. And
7 that is what they took.

8 Now, the point has been urged by Petitioners --

9 QUESTION: "That" is what they took? What precisely
10 is "that?"

11 MR. FRIED: The confidential information regarding
12 the timing and the contents of the column. That a column about
13 -- that a column saying that "Digital Switch is going to have
14 some good luck, we think," and the fact that that column was
15 going to appear on Wednesday, "that fact" is what they
16 misappropriated. That fact was entrusted to them.

17 QUESTION: So now you can misappropriate a fact?

18 MR. FRIED: The information. What is being
19 misappropriated is the information as to the timing and content
20 of the column. And you certainly can --

21 QUESTION: And it was a confidential information
22 which was then used by them in their scheme?

23 MR. FRIED: Precisely. This Court, every Member of
24 this Court recognized the nature of confidential information in
25 an employment relation in the Snep case, where the Court said

1 that, "even in the absence of a written contract, an employee
2 has the fiduciary obligation to protect confidential
3 information obtained during the course of his employment."
4 That is the duty which he breached. That precisely is the --

5 QUESTION: Now, does McNally bear on this problem?

6 MR. FRIED: I think McNally is wholly irrelevant to
7 this case. Because McNally addressed a concern that the
8 government was federalizing breaches which deprived --
9 employers of the faithful service of their employees, and even
10 more troublesome, breaches which somehow deprived state and
11 local governments of good government and the faithful service
12 of public service. That is not the issue in this case. In
13 this case, the breach of loyalty, the same breach that the
14 Court noticed in the Snep case, is the instrument, not the end,
15 of the crime.

16 And the breach of loyalty is a constant feature of
17 many garden variety frauds practiced upon employers --

18 QUESTION: Snep was not a criminal case.

19 MR. FRIED: Snep was not a criminal case, but Snep
20 recognized that there is this duty of confidentiality. And
21 that duty of confidentiality is the very duty which Winans
22 breached in this case.

23 QUESTION: Yes, but if Congress wanted to say in so
24 many words, "no person shall breach a duty of confidentiality
25 to their employer" in these circumstances, the case would give

1 one little trouble. But Congress has spoken in very general
2 terms and it seems to me you are kind of putting layers on the
3 thing.

4 MR. FRIED: I hope not, because in speaking of fraud,
5 Congress necessarily assumed the ordinary common law meaning of
6 fraud. Fraud can only take place, as is true of many property
7 crimes, on the shoulders, as it were, of pre-existing relations
8 within the civil law. And the criminal cannot reach down and
9 define all of those pre-existing relations before the crime can
10 be said to have been "properly defined."

11 So in the usual case, where there is a fraud, what
12 you have? A fraud through nondisclosure, what you have is a
13 relationship of trust. That relationship is not itself defined
14 anywhere in the criminal --

15 QUESTION: Well, more than that, you have property,
16 and that is what is hard to take here. You are -- I think what
17 you have said is true; it builds on existing common law
18 concepts, but one of those concepts is property. And the
19 property you are asserting that has been taken here is --

20 MR. FRIED: Confidential information.

21 QUESTION: -- is the fact of later publication and
22 the date of the publication.

23 MR. FRIED: The confid -- the property clearly is
24 confidential information. And we have to stand on that; we are
25 quite comfortable standing on that. It is quite a traditional,

1 though intangible, form of property right. This Court in
2 Ruckleshouse v. Monsanto recognized trade secrets as property
3 which would raise 5th Amendment concerns, so I see no
4 difficulty in treating confidential information as a species of
5 property.

6 Under the securities law, of course, one need not
7 even find property with that degree of focus and specificity.
8 That is a requirement only under the mail fraud. So in either
9 event, I think we are not doing anything so far-out as
10 petitioners suggest.

11 QUESTION: What is the closest criminal fraud case
12 that you would have to this species of property? What case of
13 ours comes the closest? A trade secret case, where a trade
14 secret was purloined?

15 MR. FRIED: Well, there are McNally cases where trade
16 secrets -- where I believe confidential information, and
17 Indeed, privacy rights were obtained, where somebody obtained
18 access. I am thinking of the Louderman case where there was
19 access to private information, and that access was thought to
20 be a kind-of interest that was protected by the mail and wire
21 fraud statutes. But here, in speaking of confidential
22 information as property, I think we really are not even as far
23 afield as that particular case would have got. It is not --

24 QUESTION: Is that a decision of this Court?

25 MR. FRIED: It is not in this Court. It is a Court

1 of Appeals case.

2 QUESTION: General Fried, I am a little troubled
3 because, are you claiming that the obtaining of this property,
4 namely the information, was done by fraud?

5 MR. FRIED: The fraud, the information was
6 misappropriated at the time either that Winans himself traded
7 on it, as he did I think on at least one occasion, or when he
8 communicated it to his confederates for the purpose of trading
9 on it.

10 QUESTION: No, it was misused, as you say, but the
11 acquisition of the information was not obtained by fraud?

12 MR. FRIED: No. If you want a common law equivalent,
13 we would say, "this property indeed was stolen, but the form of
14 theft was embezzlement rather than larceny by trick or false
15 pretenses."

16 QUESTION: I am not contending the information was,
17 there was nothing dishonest about his finding out when the
18 column was going to be published, was there?

19 MR. FRIED: No. The initial acquisition of the
20 information, at least at the outset of the scheme, he may have
21 been entirely honest; it is the subsequent use of the
22 information which had been entrusted to him, just like any
23 other servant who is entrusted with property and who, perhaps,
24 receives that property in quite good faith, but subsequently
25 misappropriates it, is guilty of embezzlement.

1 QUESTION: I do not know how he is guilty of mail
2 fraud?

3 MR. FRIED: Well, as this Court said in Grin v.
4 Shine, "embezzlement is fraud."

5 QUESTION: Yes, but you are saying that, to complete
6 your elements of the crime, you have got to have the harm, and
7 you say the harm is the injury to the reputation?

8 MR. FRIED: That is correct.

9 QUESTION: But yet you are saying it is different
10 from the intangible right to honest and good government
11 somehow, the intangible right to honest and good reporting, is
12 different in intent. I am worried about the McNally
13 implications when you focus on this intangible interest in good
14 reputation.

15 MR. FRIED: Well, I see this as very different from
16 those concerns in McNally because what was the object of the
17 fraud here was the confidential information, which does seem to
18 be a familiar, though intangible, form of property.

19 QUESTION: But it is also an element to deprive the
20 Wall Street Journal of its good reputation and so-forth.

21 MR. FRIED: The harm of its -- the reputation is the
22 harm. It is not the property. The reputation is the harm
23 which the Wall Street Journal suffers, or which is at least put
24 at-risk. There is no need to show that it suffered harm.

25 QUESTION: But you do agree that some kind of harm of

1 that nature beyond the acquisition of the property is an
2 essential ingredient of the offense?

3 MR. FRIED: Well, I think of Mr. Buchwald's example
4 of Foster Winans telling his mother about this information just
5 because he is a gossip. I think that is quite different.

6 QUESTION: Yes, it is an essential element of the
7 defense.

8 MR. FRIED: There has to be some kind of harm which
9 is contemplated or risked. I do not think that it has to
10 actually eventuate.

11 QUESTION: If that is true, why is this "harm," which
12 I would call some sort of an intangible harm, why is that
13 different than the "harm" in McNally?

14 MR. FRIED: Because in McNally, what was lacking,
15 what was utterly lacking, was the depriving of anything like
16 the property which in this case we have I would say we have in
17 sufficient degree. So we have the taking of the property and
18 the only question is, "how does depriving the Wall Street
19 journal of this property harm it?"

20 If somebody takes your car, Justice Stevens, and it
21 is up in the country, and you do not know about it, they have
22 taken your property and then there is a further question, "what
23 harm has it done you?" Those are two separate questions.

24 QUESTION: I understand that, but I suppose in a
25 sense, one could say in McNally there was a property interest

1 in controlling the placement of insurance and they acquired
2 that without violating any laws by exercising their authority.

3 MR. FRIED: One might have said that, indeed. I
4 think we urged that on the Court -- unsuccessfully.

5 [Mirth.]

6 But I think that we had, and we did not prevail, in
7 part because the interest in being able to direct where
8 insurance commissions will go is a rather unfamiliar species of
9 property, while confidential information is an entirely
10 familiar species of information.

11 QUESTION: I must say that the concept of putting
12 something at-risk as harm sufficient to support a criminal
13 charge is, it seems to me, rather strange. It is not even harm
14 sufficient to support a tort action, or we would have a lot of
15 tort suits for near misses in traffic accidents --

16 [Mirth.]

17 -- instead of even fender-benders.

18 MR. FRIED: With respect, Justice Scalia, in every
19 trespass action, the harm is presumed in just the way it is
20 presumed here. Even though the person who trespasses upon your
21 land and walks across to the other side without bending a twig,
22 has done you no monetary harm. So I think that there is
23 nothing --

24 QUESTION: Is that the theory of it? That he could
25 have done you harm? I never heard that theory espoused. I

1 thought that the theory is, he should not be on your land? The
2 harm is, he is on your land. You have a right to have him off
3 your land.

4 MR. FRIED: And the harm here is he should not be
5 trafficking in your confidential information even though as
6 things may turn out through your own diligence, you can put a
7 stop to the reputational loss which might otherwise come about.

8 QUESTION: Well, you just said that, but I do not
9 know why that is self-evident, and I never heard it before?

10 QUESTION: I do not know why you think you even have
11 to get to reputational harm. They have appropriated the
12 property and you say you presume that there is harm: your
13 property is appropriated.

14 MR. FRIED: Well, Judge Stuart in the district court
15 so-said --

16 QUESTION: I know that.

17 MR. FRIED: -- and I think it is a very strong
18 argument. I am making a further argument if that should not be
19 satisfactory to some members of the Court.

20 QUESTION: Now, a while ago you thought there had to
21 be something beyond the appropriation of the property?

22 MR. FRIED: Oh, I think the harm is presumed, Justice
23 White. If I thought there had to be something other than --

24 QUESTION: Well, it is like your car example, you --
25 he took my car.

1 MR. FRIED: He took my car, returned it, full tank of
2 gas and no dents. Exactly. That is quite sufficient.

3 QUESTION: Turn back the odometer.

4 MR. FRIED: Turn back the odometer?

5 [Mirth.]

6 QUESTION: Yes, but I thought really, and there is a
7 misunderstanding on my -- I thought you were saying, as a
8 matter of law, even though there is no physical or pecuniary
9 injury, there is a legal harm by his having taken something he
10 was not entitled to?

11 MR. FRIED: Yes, oh, yes. We certainly hold that,
12 but we say there is the further harm which is the reputational
13 harm. And both harms were found by the district court, so we
14 stand on both of them.

15 Now, a great deal has been made of the point that we
16 are seeking here to criminalize work rules of an employer. And
17 with respect, I think that is a "red herring." The work rule
18 is neither a necessary nor a sufficient condition of the kind
19 of fraud which we say took place here. The heart of the fraud
20 here is that there is a relationship of trust and that somebody
21 who is in that relationship of trust misappropriates what has
22 been entrusted to him to the detriment of the one who trusts
23 him.

24 Now, the work rule may simply set the context. The
25 contours, if you like, of what relationship of trust is. So,

1 for instance, if I may use a humble example, but one which I
2 suppose happens every day: one employer may say to his
3 employees, "When you are travelling, we consider it a proper
4 travel expense for reimbursement to charge laundry, telephone
5 calls home, pay-television in your hotel room," and another
6 employer might say, "We have a work rule that no only-business
7 expenses and all of those are private expenses." I take it
8 that the employee who submits a hotel bill, including those
9 items, to the second employer, and does it by mail and receives
10 a check back by mail, has defrauded his employer because he is
11 in a relationship of trust to him; the employer trusts him and
12 the statement there is an implicit statement that he is playing
13 by those rules, and he has broken the trust.

14 So the work rule is really just a part of the context
15 of trust.

16 QUESTION: Well, General, do you think that this
17 argument carries the day in the securities side of this case?

18 MR. FRIED: Oh, I think so. I think very much so. I
19 think as to the securities --

20 QUESTION: You mean just the fact that he has
21 defrauded his employer sustains the securities?

22 MR. FRIED: I am glad you brought me back to the
23 securities fraud issue, because the concern which Petitioners
24 raise is that we are criminalizing ordinary frauds, and I think
25 there was a fraud here; there was a breach of trust here via

1 the securities law in an open-ended way. I do not think that
2 is so because the way in which the securities law makes sure
3 that the fraud is securities-related, securities-focused, if
4 you wish, is by the provision that the fraud which the rule
5 says can be committed on any person -- not a market participant
6 -- by any person, must be in connection with the purchase and
7 sale of securities.

8 Now, we maintain that, obviously, this fraud, and a
9 palpable fraud it was, was a fraud that was committed in
10 connection with the purchase and sale of securities. How could
11 it have been more closely connected? Were it not for the
12 purchase and sale of securities, there would have been no
13 point. The whole point and purpose was that: were it not for
14 the purchase and sale of securities, the rule which he broke
15 would have no point. Were it not for the purchase and sale and
16 securities, the reputational harm which was suffered would not
17 be present.

18 So the connection was intimate.

19 QUESTION: General Fried, can I -- will you tell me
20 why this hypothetical is not covered by the mail fraud statute,
21 or perhaps it is? I am employer of the Fred M. Smith Company,
22 and Mr. Smith tells -- one of his employees asks him, you know,
23 "What does 'M' stand for?" And Smith says, "Well, I will tell
24 you this just in confidence." He is a trusted employee; "It is
25 Marmaduke. I am really very ashamed of it."

1 The employee writes to a newspaper and says, "You
2 know, Fred M. Smith's middle name is 'Marmaduke.'" And he gets
3 some -- he gets five bucks from the newspaper for that. Is
4 that mail fraud?

5 MR. FRIED: No, it is not.

6 QUESTION: Why not?

7 MR. FRIED: Well, I am confident in saying it is not.
8 And now let us try and figure out why not?

9 QUESTION: Right.

10 [Mirth.]

11 I believe you so far.

12 MR. FRIED: I would say that it is not because there
13 is no harm. There is no breach of trust, and I say that --

14 QUESTION: The mere taking of the confidential
15 information is the harm is what you said before. And the mere
16 using of it for your own advantage -- it does not matter if the
17 car is harmed or not. The mere taking of it was enough.

18 MR. FRIED: Because, because -- the notion of
19 "confidential information," the notion of "confidential
20 information" and of "trust" --

21 QUESTION: Doesn't involve "Marmaduke?" Right?

22 MR. FRIED: -- are both concepts which are intended
23 to have enough weight and seriousness not to cover every
24 trivial peccadillo. This was not a trivial peccadillo. It
25 netted the defendants almost \$700,000.

1 QUESTION: Well, you might draw the line there;
2 others might draw the line between a genuine trade secret of
3 the sort that is used in manufacturing processes or something
4 like that, and the mere fact that an article is going to appear
5 in the Wall Street Journal several months from now. You have
6 to draw the line somewhere, right?

7 MR. FRIED: In that respect, I would draw it where
8 the Court drew it in the Snep case. It seems to me that is
9 quite sufficient. Now --

10 QUESTION: General Fried, what if there had been no
11 Wall Street Journal work rule? Would either the mail fraud
12 count or the securities count be good? Could it be good
13 without that rule?

14 MR. FRIED: In the absence of such a work rule, for
15 instance, if Winans had worked for the Daily Scalper instead of
16 the Wall Street Journal, I would suppose that they would not
17 have been given the context of the relationship that there
18 existed, there would have been no understanding, no mutual
19 understanding, that this kind of action is a breach of trust.
20 The work rule does not have to be spelled out in order to make
21 it plain that a particular course of conduct is an act of
22 disloyalty or is not an act of disloyalty.

23 But the work rule here made it clear beyond
24 peradventure that there was disloyalty. I do not know if the
25 financial writers for the New York Times have been made aware

1 of a similar work rule, but if there is an understanding that
2 that is the nature of the relation, that is quite sufficient.

3 Now, I would like to address briefly the question
4 about what the securities laws are directed against, because
5 Petitioners say they are "directed against protection from
6 fraud of those persons who are trading in this particular
7 case."

8 What the statute says is that, "in general, the
9 securities laws are directed at procuring or assuring honest
10 securities markets." And in specific, they say via 10b-5,
11 "fraud against any person in connection."

12 Now, in this case, it seems to me that what has been
13 done is not at all a parody of information theory, not at all.
14 Because, what we are saying is that, "when you trade you should
15 be on the lookout for trading against people who are smarter
16 than you are, luckier than you are: better informed than you
17 are -- but not against people who have stolen the information
18 which they are trading on." Because that kind of vigilance
19 encourages what I would call a "cascading deterioration" of the
20 honesty of the securities markets of the sort which the charge,
21 at least in Chiarella, did not.

22 Where you think that somebody may have learned
23 something, perhaps as an eavesdropper --- well, perhaps by
24 accident, through greatest diligence -- well that is just the
25 kind of incentive you want to put out. But I do not think you

1 want to put out an incentive to go out and steal information
2 yourself, so that you can make good on the stock market.

3 QUESTION: So it is a federal securities crime for
4 any embezzler of money to buy securities?

5 MR. FRIED: Decidedly not. Because the embezzler
6 does not commit his fraud in connection with --

7 QUESTION: The only reason he embezzled was to buy.
8 Just like this fellow. The only reason he stole this
9 information was to buy stock.

10 MR. FRIED: He -- Justice White --

11 QUESTION: You said the connection was "palpable."

12 MR. FRIED: He had the money, the embezzler did, and
13 he could have committed it to the parimutuel, or to the numbers
14 racket, or to a poker game; he chose to commit it to the stock
15 market.

16 QUESTION: Yes, but on the facts of the case, the
17 reason he embezzled it was to buy securities.

18 MR. FRIED: Yes, but he might have changed --

19 QUESTION: Well, but he did not.

20 MR. FRIED: -- his mind and the harm would have been
21 there --

22 QUESTION: But he did not.

23 MR. FRIED: -- and the money in his pocket.

24 QUESTION: But he did not. He just went to buy
25 securities. He got the money and went right across the street.

1 MR. FRIED: The crime is completed and fully
2 identified at the moment he has the money in his pocket. What
3 he does with it next --

4 QUESTION: Why can you not say that in this case?

5 MR. FRIED: No, because the crime is not completed in
6 this case until Winans either trades on the information himself
7 --

8 QUESTION: Oh, I do not know. He gave it to his co-
9 conspirators.

10 MR. FRIED: -- for the purpose of trading.

11 QUESTION: Well --

12 MR. FRIED: If he just told it to his mother to
13 satisfy gossip interests, there would have been no effects.
14 But he communicated for the purpose of trading.

15 If there are no further question, I thank the Court.

16 CHIEF JUSTICE RHENQUIST: Thank you General Fried.

17 Mr. Buchwald, you have two minutes remaining.

18 MR. BUCHWALD: Thank you, Your Honor.

19 ORAL ARGUMENT OF DON B. BUCHWALD

20 ON BEHALF OF THE PETITIONER -- REBUTTAL

21 Very briefly, on the mail and wire fraud analysis in
22 the deprivation of information point: "We believe that all
23 roads lead to a putative reputational damage," is what the
24 government is talking about. Here you have lawfully acquired
25 information. When you use information, unlike a car, you are

1 not depriving the other person of that information either
2 permanently, temporarily, or partially.

3 And the cutoff point, it seems to us, as to where
4 information takes on some kind of property value in anything
5 even remotely resembling a McNally sense, is either when you
6 use the information in competition with your employer, or where
7 you are giving the information to a competitor to use in
8 competition; in essence in a "trade secret" sense.

9 With respect to General Fried's suggestion that, the
10 "in connection with" requirement is satisfied if the scheme is
11 for the purpose of buying or selling stocks, in addition to the
12 example which Justice White gave, the example of obtaining
13 information from a prominent investment advisor, if I join the
14 Joe Granville hotline with a bounced check and no intention
15 actually of paying Mr. Granville for his advice and I then get
16 a telegram in return for my \$1000 bounced check, saying that he
17 recommends XYZ company and then I now go out and buy the stock
18 in XYZ, under the government's theory, that would be a
19 securities fraud, because it is for the purpose of trading in
20 securities.

21 And essentially, because the government wishes to
22 move away from these examples of the embezzlement, and the use
23 of information fraudulently obtained from an investment
24 advisor, they place a limiting principle of fairness on the
25 market, which we believe cannot be found on the market, which

1 we believe is not and cannot be found, in the language of --

2 CHIEF JUSTICE RHENQUIST: Your time has expired, Mr.
3 Buchwald. The case is submitted.

4 [Whereupon, at 12:00 noon, the case in the above-
5 entitled matter was submitted.]

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3 REPORTER'S CERTIFICATE

4 DOCKET NUMBER: 86-422

5 CASE TITLE: David Carpenter, Kenneth P. Felis and P. Foster
6 Winans v. United States

7 HEARING DATE: October 7, 1987

8 LOCATION: Washington, D.C.

9 I hereby certify that the proceedings and evidence
10 are contained fully and accurately on the tapes and notes
11 reported by me at the hearing in the above case before the
12 United States Supreme Court.

13 Date: 10/8/87

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