HARMONIZING CIVIL AND CRIMINAL ENFORCEMENT OF FEDERAL REGULATORY STATUTES: THE CASE OF THE SECURITIES EXCHANGE ACT OF 1934

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Many federal regulatory statutes (including those governing antitrust, securities, and the environment) are hybrid statutes: their prohibitions are enforceable in criminal actions as well as in private or governmental civil actions (or both). Courts have long divided over whether prohibitions in hybrid statutes can be construed differently in different enforcement contexts. Resolution of this uncertainty has become urgent now that criminal enforcement of federal regulatory statutes is relatively frequent.

In this article, Professor Sachs argues that prohibitions in hybrid statutes should be limited to a single interpretation. How to apply this principle (referred to in this article as "the core principle") is not self-evident, however, since the one interpretation that is chosen must be suitable for all enforcement contexts. Accordingly, Professor Sachs identifies rules that supplement the core principle. She extracts the core principle and rules from Supreme Court decisions that apply the core principle and rules but leave them unstated.

Professor Sachs then examines the core principle and rules in relation to the Securities Exchange Act of 1934 ("Exchange Act"). Before 1980, lower federal courts construing the Exchange Act expressed support for the core principle. In the 1980s and thereafter, however, some courts abandoned the core principle to accommodate changes that were taking place with respect to Exchange Act criminal actions, implied private actions, and actions involving international securities fraud. Professor Sachs shows that courts adhering to the

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core principle enhance their ability to promote the Exchange Act's policy of combating unscrupulousness in the securities markets.

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I. INTRODUCTION

Many federal regulatory statutes are hybrid statutes—their prohibitions[1] are enforceable in criminal actions as well as in private or govern-

1. For purposes of this article, the term "prohibition" refers to the part of the statute that identifies proscribed conduct. The plaintiff must prove that the defendant engaged in this conduct in order to establish a prima facie case.

mental civil actions (or both).[2] Leading examples include the Sherman Antitrust Act,[3] the Clean Water Act,[4] the Truth in Lending Act,[5] the False Claims Act,[6] the Racketeer Influenced Corrupt Organizations Act,[7] the Federal Food, Drug and Cosmetic Act,[8] and the Securities Exchange Act of 1934.[9] Hybrid statutes present an important question that has divided courts but received virtually no attention from legal scholars—can the same prohibition mean different things in different enforcement contexts?[10]

2. The term "hybrid statute" has begun to appear in law reviews. *E.g.*, Michael P. Kenny & Teresa D. Thebaut, *Misguided Statutory Construction to Cover the Corporate Universe: The Misappropriation Theory of Section 10(b)*, 59 ALB. L. REV. 139, 158 (1995) (referring to § 10(b) of the Securities Exchange Act of 1934 as a "hybrid statute"); Taurie M. Zeitzer, Note, *In* Central Bank's *Wake, RICO's Voice Resonates: Are Civil Aiding and Abetting Claims Still Tenable?*, 29 COLUM. J.L. & SOC. PROBS. 551, 551 (1996) (referring to the antitrust, racketeering, and securities statutes as "hybrid statutes"); *cf.* Epstein v. Epstein, 966 F. Supp. 260, 261 (S.D.N.Y. 1997) (describing the Racketeer Influenced Corrupt Organizations Act as a "hybrid civil/criminal statute").

3. Sherman Antitrust Act, 15 U.S.C. §§ 1–7 (1994).

4. Clean Water Act of 1977, Pub. L. No. 95-217, 91 Stat. 1566 (codified as amended in scattered sections of 33 U.S.C.).

5. Truth in Lending Act, Pub. L. No. 90-321, 104 Stat. 2721 (codified as amended in scattered sections of 15 U.S.C.).

6. False Claims Act, 31 U.S.C. §§ 3729–3733 (1994).

7. Racketeer Influenced Corrupt Organizations Act, 18 U.S.C. §§ 1961–1968 (1994).

8. Federal Food, Drug and Cosmetic Act, 21 U.S.C. §§ 301–395 (1994).

9. Securities Exchange Act of 1934, ch. 404, 48 Stat. 881 (codified as amended in scattered sections of 15 U.S.C.). For additional federal regulatory statutes that are hybrid statutes, see Sedima, S.P.R.L. v. Imrex Co., 741 F.2d 482, 505 (2d Cir. 1984) (Cardamone, J., dissenting), *rev'd*, 473 U.S. 479 (1985); United States v. Cappetto, 502 F.2d 1351, 1356–57 (7th Cir. 1974). There are also numerous state statutes that are hybrid statutes. *See generally* 3 NORMAN J. SINGER, SUTHERLAND STATUTORY CONSTRUCTION § 60.04 (5th ed. 1992). This article makes no attempt to treat such state statutes directly, although observations made herein may be relevant to them.

10. *Compare* United States v. Nippon Paper Indus. Co., 109 F.3d 1, 4 (1st Cir. 1997) (holding that § 1 of the Sherman Antitrust Act should be read the same way in a criminal action as in a civil action), *and* Drasner v. Thomson McKinnon Sec., Inc., 433 F. Supp. 485, 499 (S.D.N.Y. 1977) (holding that Regulation T of the Securities Exchange Act of 1934 should be read the same way in a criminal action as in a civil action), *with* United States v. Plaza Health Labs., Inc., 3 F.3d 643, 648–49 (2d Cir. 1993) (rejecting civil precedent on the meaning of the term "point source" under the Clean Water Act when the term arose in a criminal action), *and* United States v. Rudi, 927 F. Supp. 686, 688 (S.D.N.Y. 1996) (rejecting an interpretation of a Municipal Securities Regulation Board rule under the Securities Exchange Act of 1934 in the context of a criminal action but noting that the interpretation might be acceptable in a civil action), *and Nippon*, 109 F.3d at 10 (Lynch, J., concurring) (noting in connection with the Sherman Antitrust Act that "it is at least conceivable that different content could be ascribed to the same language depending on whether the context is civil or criminal").

The only extensive commentary appears in Bryan T. Camp, *Dual Construction of RICO: The Road Not Taken in* Reves, 51 WASH. & LEE L. REV. 61 (1994) (arguing that courts should construe prohibitions in the Racketeer Influenced Corrupt Organizations Act differently in different enforcement contexts). *See also* 2 PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW 29 (rev. ed. 1995) (maintaining that "courts should, and to some extent already do, define an antitrust violation somewhat differently according to the remedy sought and the public or private identity of the enforcer"); Matthew C. Blickensderfer, Note, *Unleashing RICO*, 17 HARV. J.L. & PUB. POL'Y 867, 878 n.66 (1994) (arguing that courts should construe prohibitions in the Racketeer Influenced Corrupt Organizations Act no differently in criminal actions than in civil actions); *cf.* Bruce A. Markell, *Bankruptcy, Lenity, and the Statutory Interpretation of Cognate Civil and Criminal Statutes*, 69 IND. L.J. 335 (1994) (addressing whether to apply different constructions to terminology shared by separate but related civil and criminal bankruptcy statutes).

The following example, drawn from the Securities Exchange Act of 1934 ("Exchange Act"), illustrates why some courts endorse multiple constructions.[11] George convinced his friend Mary that Sweets, Inc., was a highly profitable company. Mary entrusted money to George for the purchase of Sweets stock, but George misappropriated the money for his own use. Later, Mary discovered that there was no such company as Sweets. Section 10(b) of the Exchange Act and Rule 10b-5 prohibit fraud "in connection with the purchase or sale of any security"[12] but say nothing about whether transactions involving nonexistent securities are covered.[13] Section 10(b) and Rule 10b-5 are enforceable by the Justice Department in criminal actions, by the Securities & Exchange Commission ("Commission") in civil actions,[14] and by investors in implied private actions.[15] Should the type of action that is brought against George determine whether section 10(b) and Rule 10b-5 apply to his conduct?

11. For representative decisions endorsing multiple constructions, see *supra* note 10. *See infra* notes 119–22, 140–54, 167, 175 and accompanying text (describing further examples of multiple construction involving the Exchange Act).

12. Section 10(b) provides as follows:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—
>
> . . . .
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. § 78j(b) (1994) [hereinafter § 10(b)].

Rule 10b-5, promulgated by the Securities & Exchange Commission in 1942, provides as follows:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5 (2000) [hereinafter Rule 10b-5].

13. For the text of § 10(b) and Rule 10b-5, see *supra* note 12. The legislative history of § 10(b) and the administrative history of Rule 10b-5 likewise do not address coverage of nonexistent securities. *See generally* Margaret V. Sachs, *The Relevance of Tort Law Doctrines to Rule 10b-5: Should Careless Plaintiffs Be Denied Recovery?*, 71 CORNELL L. REV. 96, 117–21 (1985) (describing the legislative and administrative history). For decisions holding that § 10(b) and Rule 10b-5 encompass transactions involving nonexistent securities, see Local 875 I.B.T. Pension Fund v. Pollack, 992 F. Supp. 545, 564 (E.D.N.Y. 1998); SEC v. Bremont, 954 F. Supp. 726, 732 (S.D.N.Y. 1997). For a decision holding that § 10(b) and Rule 10b-5 do not encompass such transactions, see *United States v. Jones*, 648 F. Supp. 225, 232–34 (S.D.N.Y. 1986), *aff'd in part, rev'd in part on other grounds sub nom.* United States v. Blackmon, 839 F.2d 900 (2d Cir. 1988). *See also* Renner v. Chase Manhattan Bank, [1999 Transfer Binder] Federal Sec. L. Rep. (CCH) ¶ 90,438 at 91,993 (S.D.N.Y. Feb. 3, 1999) (leaving the question open).

14. The Commission can also enforce § 10(b) and Rule 10b-5 in administrative proceedings. *See* § 21C of the Exchange Act, 15 U.S.C. § 78u-3 (1994). Administrative proceedings are beyond the scope of this article. *See infra* note 23.

15. For background on the Exchange Act, see *infra* notes 100–09 and accompanying text.

Assume first that the action against George is criminal. The court may reason that given the absence of clarity in the law, George may have lacked fair warning that section 10(b) and Rule 10b-5 encompass transactions in nonexistent securities.[16] It may therefore employ strict construction and limit these prohibitions to fraud involving extant securities only.[17] This ruling may subsequently be ignored by courts adjudicating Commission and implied private actions because for those actions, fair warning concerns are of lesser significance.[18]

Assume next that Mary brings an implied private action against George. Such actions elicit considerable judicial antipathy because they are perceived as vexatious.[19] Thus, the court may deny Mary a federal forum for what is arguably merely a claim for conversion under state law.[20] This ruling may thereafter be ignored by courts adjudicating criminal and Commission actions on the ground that it was premised on antipathy towards implied private actions.[21]

Assume finally that the Commission brings an action against George. The court may reason that section 10(b) and Rule 10b-5 were adopted to combat securities fraud and that fraud involving nonexistent securities is simply securities fraud in an extreme form. It may therefore hold that the section and the Rule cover such fraud in order to promote the underlying statutory policy.[22] This ruling may later be ignored by courts adjudicating criminal actions because of the failure to take into account fair warning concerns. It may likewise be ignored by courts adjudicating implied private actions because of the failure to take into account the threat of vexatious private litigation.

This article argues that prohibitions in hybrid statutes should be limited to one interpretation apiece. This principle—which this article calls "the core principle"—is easier to state than to apply, because the

16. *See Jones*, 648 F. Supp. at 233–34. The purpose of the fair warning requirement is not only to alert potential wrongdoers to the conduct constituting crimes but also to "confine the discretion of prosecuting authorities." United States v. Standard Oil Co., 384 U.S. 224, 236 (1966) (Harlan, J., dissenting).

17. *See Jones*, 648 F. Supp. at 233–34; *see also* United States v. Naftalin, 441 U.S. 768, 778–79 (1979) (endorsing strict construction of ambiguities in the Securities Act of 1933 for the purpose of alleviating fair warning concerns).

18. *Cf.* Vill. of Hoffman Estates v. Flipside, Hoffman Estates, Inc., 455 U.S. 489, 498–99 (1982) (noting that "[t]he Court has . . . expressed greater tolerance of enactments with civil rather than criminal penalties because the consequences of imprecision are qualitatively less severe") (footnote omitted).

19. *E.g.*, Cent. Bank v. First Interstate Bank, 511 U.S. 164, 189 (1994); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 739–47 (1975).

20. *Cf.* Santa Fe Indus., Inc. v. Green, 430 U.S. 462, 478 (1977) (noting that a consideration in determining whether § 10(b) and Rule 10b-5 should cover particular circumstances is whether such coverage would duplicate a long-standing state law action).

21. *Cf.* United States v. O'Hagan, 521 U.S. 642, 664–65 (1997) (noting that the "dangers" presented by implied private actions under § 10(b) and Rule 10b-5 are irrelevant to criminal actions).

22. *Cf.* SEC v. Lauer, 52 F.3d 667, 670 (7th Cir. 1995) (holding a fraud prohibition in the Securities Act of 1933 to reach transactions involving nonexistent securities because "[i]t would be a considerable paradox if the worse the securities fraud, the less applicable the securities laws").

one interpretation that is chosen must be appropriate for all enforcement contexts. Accordingly, this article assists courts[23] with the core principle's implementation by identifying supplemental rules and giving each rule a name that is reflective of its distinctive function.[24]

Part II of this article extracts the core principle and the rules from a disparate array of Supreme Court decisions. These decisions do not make the core principle or the rules explicit, much less set forth their underlying rationales. Part II fills that void.

Parts III, IV, and V examine the core principle and the rules in relation to the Exchange Act. Part III shows that many courts disregard the core principle, and Part IV shows that many courts disregard the rules. Part V demonstrates that application of the core principle and the rules to the Exchange Act would significantly enhance the quality of the resulting interpretations.

II. HARMONIZING CIVIL AND CRIMINAL ENFORCEMENT OF HYBRID STATUTES

Buried in a handful of Supreme Court decisions issued over the past sixty years is an analytic framework for construing hybrid statutes.[25] These decisions do not make the framework explicit, let alone explain it.[26]

A. The Core Principle and Its Justifications

Hybrid statutes present the question whether the same statutory prohibition should be construed differently in different enforcement contexts. The Supreme Court has often insisted that the answer is no but has not said why. Consider as an illustration the Court's 1954 decision in

23. The focus in this article is on courts and not administrative agencies, despite the fact that some hybrid statutes give agencies authority to interpret prohibitions in administrative proceedings. *E.g.*, § 21C of the Exchange Act, 15 U.S.C. § 78u-3 (1994). One reason for excluding agencies is that they do not adjudicate criminal actions and are thereby not positioned to evaluate the policies underlying those actions as required by the supplemental rules proposed in this article. Another reason is that administrative statutory interpretations are necessarily subject to judicial review, even if granted deference. *See* Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842–45 (1984).

24. The rules are the all contexts rule, *see infra* notes 52–63 and accompanying text; the default fair warning rule, *see infra* notes 65–75 and accompanying text; the alternative fair warning rule, *see infra* notes 76–89 and accompanying text; and the differentiated intent rule, *see infra* notes 90–99 and accompanying text.

25. The Supreme Court upheld the constitutionality of hybrid statutes more than a century ago. *In re* Debs, 158 U.S. 564, 599 (1895). For a discussion of the *Debs* decision, see United States v. Cappetto, 502 F.2d 1351, 1356–57 (7th Cir. 1974).

26. *E.g.*, United States v. Thompson/Ctr. Arms Co., 504 U.S. 505, 517–18 & n.10 (1992) (National Firearms Act); Aaron v. SEC, 446 U.S. 680, 691 (1980) (Exchange Act); United States v. United States Gypsum Co., 438 U.S. 422, 438–43 (1978) (Sherman Antitrust Act); FCC v. ABC, 347 U.S. 284, 296 (1954) (Federal Communications Act); United States *ex rel.* Marcus v. Hess, 317 U.S. 537, 541–42 (1943) (False Claims Act); *see also* Nat'l Org. for Women, Inc. v. Scheidler, 510 U.S. 249, 262 (1994) (Racketeer Influenced Corrupt Organizations Act).

FCC v. ABC.[27] At issue in this case was whether a prohibition against radio broadcasts involving "any lottery, gift enterprise, or similar scheme"[28] encompassed broadcasts that awarded prizes to contestants for correct answers to questions.[29] The Federal Communications Commission (FCC) conceded that one element of a lottery, gift enterprise, or similar scheme was consideration,[30] but argued that this element was satisfied because the contestants heard the broadcasts.[31] In support of its broad interpretation, the FCC noted that "these are not criminal cases."[32] Rejecting this argument, the Court observed only that "[t]here cannot be one construction for the [FCC] and another for the Department of Justice."[33]

Decisions such as *ABC* have not convinced lower courts to limit prohibitions to a single construction.[34] The result might be otherwise if the Court had explained why multiple constructions are unacceptable.

There are in fact four powerful reasons that the Court could have cited. These reasons involve principles of statutory analysis that cut across subject matter boundaries. Thus, they apply to all hybrid statutes regardless of their substantive content.

The first reason focuses on Congress's decision to enact a hybrid statute rather than a statute with different prohibitions for different forms of enforcement. There is no basis for supposing—without more—that Congress expects courts to abrogate its choice of statutory form by means of construction. If Congress intends distinctions between different forms of enforcement under a hybrid statute, it can simply write them into the statutory text. For example, Congress has enacted pleading requirements for private actions under the Exchange Act that are irrelevant to government actions under the Act.[35] Moreover, Congress has au-

27. 347 U.S. 284 (1954).

28. 18 U.S.C. § 1304 (1994).

29. *See FCC*, 347 U.S. at 290.

30. *See id.*

31. *See id.*

32. *Id.* at 296.

33. *Id.*; *see also* United States v. Thompson/Ctr. Arms Co., 504 U.S. 505, 518–19 n.10 (1992) (noting that "[t]he rule of lenity . . . is a rule of statutory construction whose purpose is to help give authoritative meaning to statutory language . . . [and] is not a rule of administration calling for courts to refrain in criminal cases from applying statutory language that would have been held to apply if challenged in civil litigation"); United States *ex rel.* Marcus v. Hess, 317 U.S. 537, 542 (1943) (noting that "we cannot say that the same substantive language has one meaning if criminal prosecutions are brought by public officials and quite a different meaning where the same language is invoked by an informer"). *But cf.* FCC v. Pacifica Found., 438 U.S. 726, 739 n.13 (1978) (construing a prohibition in a civil action but noting that "we do not need to consider" whether the construction would apply in a criminal action because the structure of the Federal Communications Act as originally enacted separated civil and criminal enforcement and the subsequent legislative history confirmed their continuing "independence"); *but see* United States v. Naftalin, 441 U.S. 768, 779 (1979), discussed *infra* notes 119–22 and accompanying text.

34. For illustrative lower court decisions expressing support for multiple constructions, see *supra* note 10. *See also infra* notes 140–54, 167, 175 and accompanying text.

35. *See* § 21D(b)(2), 15 U.S.C. § 78u-4(b)(2) (requiring the plaintiff to plead "with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind") (1994

thorized government actions against those who aid and abet Exchange Act violations, whereas it has not authorized private actions for this purpose.[36] Finally, under the Exchange Act as well as a number of other hybrid statutes, Congress has enacted an intent requirement for criminal actions that does not apply to civil actions.[37]

The second reason derives from the fact that some hybrid statutes contain an intent requirement for criminal actions that does not apply to civil actions.[38] As hybrid statutes, however, these statutes make no other express distinction between the predicates for criminal actions and the predicates for civil actions.[39] This statutory pattern invites application of the maxim *expressio unius est exclusio alterius* (to include one thing is to exclude other things).[40] By singling out intent as the distinctive feature of criminal actions, Congress implies that the prohibitions are otherwise identical.

The third reason extrapolates from the well-established presumption that language appearing repeatedly in a statute has one meaning throughout.[41] According to a recent Supreme Court decision, this presumption is "virtually impossible" to rebut when the language is repeated within the space of a single sentence.[42] Because a prohibition in a hybrid statute is stated once and not repeated,[43] the presumption that it has but a single meaning should be completely impervious to rebuttal. Compelling support for this conclusion comes from the Supreme Court's 1994 decision in *Ratzlaf v. United States.*[44] At issue in *Ratzlaf* was whether the defendant could be convicted for "willfully" violating the antistructuring

& Supp. III 1997); SEC v. ICN Pharms., Inc., 84 F. Supp. 2d 1097, 1099 (C.D. Cal. 2000) (holding that the Commission need not comply with the Exchange Act's pleading requirements for private actions).

36. *See* Private Securities Litigation Reform Act of 1995 § 104, 15 U.S.C. § 78t(e) (1994 & Supp. III 1997) (expressly allowing the Commission to bring actions against "any person that knowingly provides substantial assistance to another person in violation of a provision [of the Exchange Act] or any rule or regulation"). Congress enacted § 104 because of its concern that the Commission's power to sue aiders and abettors might be foreclosed by the Supreme Court's decision in *Central Bank v. First Interstate Bank*, 511 U.S. 164 (1994). In *Central Bank*, the Court barred private actions for aiding and abetting under § 10(b) of the Exchange Act based on the absence of authority for such actions in the language of the § 10(b) prohibition. *See id*. at 177. Rather than using § 104 to overturn *Central Bank* with respect to both private actions and Commission actions, Congress acted with respect to Commission actions only. There was no need for Congress to act with respect to criminal actions, which can encompass aiding and abetting liability based on 18 U.S.C. § 2(a) (1994).

37. For discussion of this aspect of the Exchange Act, see *infra* notes 210–19 and accompanying text. For other examples of hybrid statutes of this type, see *infra* note 91.

38. *See supra* note 37 and accompanying text.

39. For the definition of the term "hybrid statute," see *supra* notes 1–2 and accompanying text.

40. *See generally* David L. Shapiro, *Continuity and Change in Statutory Interpretation*, 67 N.Y.U. L. REV. 921, 927–29 (1992) (discussing the *expressio unius* maxim); Cass R. Sunstein, *Interpreting Statutes in the Regulatory State*, 103 HARV. L. REV. 405, 455–56 (1989) (same).

41. *E.g.*, Cohen v. De La Cruz, 523 U.S. 213, 220 (1998); United States v. Thompson/Ctr. Arms Co., 504 U.S. 505, 512 n.5 (1992); Atlantic Cleaners & Dyers, Inc. v. United States, 286 U.S. 427, 433 (1932).

42. Brown v. Gardner, 513 U.S. 115, 118 (1994).

43. For the definition of the term "prohibition," see *supra* note 1. For the definition of the term "hybrid statute," see *supra* notes 1–2 and accompanying text.

44. 510 U.S. 135 (1994).

prohibition of the Currency and Foreign Transactions Reporting Act without proof that he knew his actions were illegal.[45] The willfulness requirement, set forth in one provision of the Act,[46] applied to prohibitions (including the antistructuring prohibition) located elsewhere in the Act.[47] In concluding that knowledge of illegality was a prerequisite to conviction, the Court found it significant that several circuits had read the willfulness requirement to require knowledge of illegality when a prohibition other than the antistructuring prohibition was at issue.[48] Referring to the presumption that language appearing repeatedly in a statute has one construction throughout,[49] the Court observed that there is an "even stronger cause to construe a *single* formulation . . . the same way each time it is called into play."[50]

The final reason is simply a prediction that multiple constructions of a single prohibition are likely to be unstable. Indeed, such constructions arise out of the identical statutory language and legislative history, and these shared origination points may propel the constructions towards convergence. Thus, preserving the distinctiveness of a prohibition's multiple constructions may prove more difficult than first appears.[51]

These four reasons give rise to a core principle: courts should limit prohibitions in hybrid statutes to a single interpretation. The rules described in the next section are designed to assist in the core principle's implementation.

B. Implementing the Core Principle: The Rules

To implement the core principle, courts should apply the following rules. This article shows that the Supreme Court has approved each of the rules but has left them unstated.

1. The All Contexts Rule

Because the core principle limits every prohibition to a single interpretation,[52] that interpretation must suit all enforcement actions. In deciding upon the single interpretation, therefore, courts should not focus solely on the immediate enforcement context. Rather, they should apply the all contexts rule, which requires them to consider every action to enforce the prohibition under the hybrid statute and the policies pertinent

45. *Id.* at 136–37.
46. 31 U.S.C. § 5322(a) (1994).
47. *Id.*; *see also Ratzlaf*, 510 U.S. at 141.
48. *See Ratzlaf*, 510 U.S. at 141–42.
49. *Id.* at 143; *see also* cases cited *supra* note 41.
50. *Ratzlaf*, 510 U.S. at 143 (emphasis added).
51. No data are yet available to support this prediction, since judicial willingness to countenance multiple constructions is quite new. *See* cases cited *supra* note 10 and *infra* notes 140–54, 167, 175.
52. *See supra* Part I.A.

to each. If the policies conflict, courts should seek the most appropriate compromise.

The Supreme Court ratified the all contexts rule in its 1943 decision in *United States ex rel. Marcus v. Hess.*[53] In *Hess*, the plaintiff brought a qui tam action—a civil action on the government's behalf[54]—to enforce a prohibition in the U.S. Criminal Code applicable to anyone "who . . . causes . . . to be presented for payment . . . any claim upon or against the Government of the United States . . . knowing such claim to be . . . fraudulent."[55] Construing the prohibition "'with utmost strictness'"[56] on the ground that qui tam actions "'have always been regarded with disfavor,'"[57] the Third Circuit concluded that the prohibition applied only to those in privity of contract with the United States.[58] So construed, the prohibition did not extend to the defendants, who had dealt with the United States through a middleman.[59] The Supreme Court reversed because the Third Circuit's construction "treat[ed] the language of [the prohibition] in such fashion that no criminal proceedings could be brought against the respondents, a result to which the policy on qui tam actions is immaterial even if it exists or could properly be applied."[60] Thus, the Court made clear that the Third Circuit had erred in focusing solely on the policies pertinent to qui tam actions; it should have interpreted the prohibition in a manner that was appropriate for criminal actions as well.[61]

The importance of the all contexts rule becomes apparent upon considering what would happen if courts rejected it while at the same time accepting the core principle. Under these circumstances, a prohibition's meaning would be determined by the nature of the lawsuit that ad-

53. 317 U.S. 537 (1943).

54. The dictionary definition of a qui tam action is as follows:

> It is an action brought by an informer, under a statute which establishes a penalty for the commission or omission of a certain act, and provides that the same shall be recoverable in a civil action, part of the penalty to go to any person who will bring such action and the remainder to the state or some other institution.

BLACK'S LAW DICTIONARY 1251 (6th ed. 1990). *See generally* J. Randy Beck, *The False Claims Act and the English Eradication of Qui Tam Legislation*, 78 N.C. L. REV. 539 (2000). The qui tam action in *Hess* was authorized by 31 U.S.C. § 232 (1940) (currently codified as 31 U.S.C. § 3730(b)(1) (1994)). *See* United States *ex rel.* Marcus v. Hess, 317 U.S. 537, 539 (1943).

55. *See* 18 U.S.C. § 80 (1940) (currently codified as 18 U.S.C. §§ 287, 1001 (1994)).

56. *Hess*, 317 U.S. at 540 (quoting United States *ex rel.* Marcus v. Hess, 127 F.2d 233, 235 (3d Cir. 1942)).

57. *Id.* at 541 (quoting United States *ex rel.* Marcus v. Hess, 127 F.2d 233, 235 (3d Cir. 1942)).

58. *See id.* (citing United States *ex rel.* Marcus v. Hess, 127 F.2d 233, 237 (3d Cir. 1942)).

59. *See id.* (citing United States *ex rel.* Marcus v. Hess, 127 F.2d 233, 237 (3d Cir. 1942)).

60. *Id.* at 542.

61. The Third Circuit seemed to think that its interpretation could be limited to qui tam actions only:

> We wish to make it quite plain that the decision herein has no bearing whatever on ultimate restitution. Insofar as the United States . . . [has] been defrauded, suit can be brought and the injured made completely whole. Furthermore, any defendants who are guilty can be punished by more than financial penalty—they can be sent to jail.

United States *ex rel.* Marcus v. Hess, 127 F.2d 233, 237 (3d Cir. 1942), *rev'd*, 317 U.S. 537 (1943).

dressed it first, thereby precipitating a race to the courthouse door.[62] Indeed, private attorneys might encourage marginal plaintiffs to bring weak cases to establish narrow interpretations that would thereafter frustrate the enforcement efforts of the government or of private parties. The government, on the other hand, would attempt to bring civil cases first to establish broad interpretations and then bring criminal cases that sweep up minor malefactors who would have had fair warning based on the civil precedent already on the books.[63]

2. The Fair Warning Rules

To provide fair warning of the conduct constituting crimes, courts should determine which of two fair warning rules is appropriate to the hybrid statute before them—the default fair warning rule or the alternative fair warning rule. Courts should make this determination not only when the action before them is criminal but also when it is civil because, as this article shows, the default fair warning rule applies to civil as well as to criminal actions.[64]

a. The Default Fair Warning Rule

The default fair warning rule builds upon the criminal law canon, sometimes known as the rule of lenity, that requires strict construction of statutory ambiguities in order to avoid subjecting criminal defendants to surprise.[65] The default fair warning rule expands the canon to civil actions in order to accommodate the core principle. The rule holds that a court must construe a prohibition strictly in a civil action if in a criminal action a court would be required to construe the statute strictly to pro-

62. The government's efforts in connection with insider trading are illustrative in this regard. The Commission established the application of § 10(b) and Rule 10b-5 to insider trading in *In re Cady, Roberts & Co.*, 40 S.E.C. 907 (1961), an enforcement action as to which the Commission had the benefit of being not only the complainant but also the judge. It then convinced the Second Circuit to hold Rule 10b-5 applicable to insider trading on the basis of the *Cady, Roberts* precedent in *SEC v. Tex. Gulf Sulphur Co.*, 401 F.2d 833, 848 (2d Cir. 1968). The Justice Department thereafter tried to rely on *Texas Gulf Sulphur* to obtain a conviction in *Chiarella v. United States*, 445 U.S. 219 (1980). *See* Brief for the Respondent United States at 9–10, Chiarella v. United States, 445 U.S. 219 (1980) (No. 78-1202). The Supreme Court did not, however, accept this argument. *See Chiarella*, 445 U.S. at 226–30.

63. *Cf.* United States v. Farris, 614 F.2d 634, 640–42 (9th Cir. 1980) (concluding on the basis of civil precedent that the criminal defendant had fair warning of the meaning of the term "security" in the Securities Act of 1933).

64. *See infra* note 66 and accompanying text.

65. *See generally* 1 WAYNE R. LAFAVE & AUSTIN W. SCOTT, JR., SUBSTANTIVE CRIMINAL LAW § 2.2(d) (1986) (strict construction of criminal statutes); Lawrence M. Solan, *Law, Language, and Lenity*, 40 WM. & MARY L. REV. 57 (1998) (tracing the evolution of the rule of lenity); *see also* United States v. Lanier, 520 U.S. 259, 266 (1997) (referring to "strict construction of criminal statutes" and "the rule of lenity" as different names for the same thing).

vide fair warning.[66] By mandating strict construction, the rule strips courts of the flexibility to interpret ambiguities in accordance with the policies that prompted the hybrid statute's enactment.[67]

The Supreme Court applied the default fair warning rule in its 1992 decision in *United States v. Thompson/Center Arms Co.*[68] In *Thompson/Center*, an arms manufacturer sought a refund of a tax that the National Firearms Act levies on those who "make" certain firearms.[69] The Act imposes criminal penalties on those who fail to pay the tax.[70] The issue in *Thompson/Center* was whether a manufacturer "makes" a firearm when it distributes a package of component parts that can be assembled into two different firearms, one of which would trigger the tax's application and the other of which would not.[71] The Court found the statute ambiguous on this point.[72] Reasoning that strict construction would be appropriate if the action were criminal,[73] it construed the ambiguity in the civil defendant's favor and concluded that a manufacturer does not "make" a firearm under the circumstances described.[74] Constrained by strict construction, it was unable to consider whether the policy underlying the National Firearms Act—regulation of dangerous armaments—would favor a different result.[75]

66. Application of this rule raises two questions that extend beyond hybrid statutes and beyond the scope of this article as well. The first question is how ambiguous statutory language must be in order to bring strict construction into play. *Compare* Muscarello v. United States, 524 U.S. 125, 135–39 (1998) (finding no ambiguity), *with id.* at 139–50 (Ginsburg, J., dissenting) (finding ambiguity); *compare* Thompson/Ctr. Arms Co., 504 U.S. at 513–17 (finding ambiguity), *and id.* at 519 (Scalia, J., concurring in the judgment) (finding a different ambiguity), *with id.* at 524 (White, J., dissenting) (finding no ambiguity). The second question is whether legislative history should play a role in determining whether an ambiguity exists. *Compare id*. at 518 n.8 (1992) (arguing that legislative history should be consulted), *with id.* at 521 (Scalia, J., concurring in the judgment) (arguing that legislative history should not be consulted).

67. For illustrations of this phenomenon, see *infra* notes 75 and 192 and accompanying text.

68. 504 U.S. 505 (1992).

69. *See* 26 U.S.C. § 5801 (1994).

70. *See id.* § 5871.

71. *Thompson/Ctr. Arms Co.*, 504 U.S. at 507.

72. *Id.* at 517.

73. *Id*. at 517–18 & n.10.

74. *Id*. at 518. *See* Nat'l Org. for Women, Inc. v. Scheidler, 510 U.S. 249, 262 (1994) (suggesting in a private action under the Racketeer Influenced Corrupt Organizations Act that the Court would have applied strict construction if the statutory language in question had been ambiguous); *see also* United States v. O'Hagan, 521 U.S. 642, 679 (1997) (Scalia, J., concurring in part and dissenting in part) (arguing that ambiguities in § 10(b) of the Exchange Act and Rule 10b-5 should be construed strictly because of their criminal applications); H.J., Inc. v. Northwestern Bell Tel. Co., 492 U.S. 229, 255 (1989) (Scalia, J., concurring in the judgment) (observing that the Racketeer Influenced Corrupt Organizations Act, "since it has criminal applications . . . must, even in its civil applications, possess the degree of certainty required for criminal laws") (citation omitted); *cf.* Crandon v. United States, 494 U.S. 152, 157–58 (1990) (applying strict construction to a federal criminal prohibition when it arose in a common-law civil action).

75. In a dissent in which no other justice joined, Justice Stevens argued that the statutory policy was worthy of attention. *See* United States v. Thompson/Ctr. Arms Co., 504 U.S. 505, 526 (1992) (Stevens, J., dissenting). To allow the policy to be considered, he argued that strict construction should not apply to civil actions. *See id.*

b. The Alternative Fair Warning Rule

The alternative fair warning rule is based on the criminal law canon that enforcement of an intent requirement can alleviate fair warning concerns. The Supreme Court rationalized the canon as follows in *American Communications Ass'n v. Douds*:[76]

> [S]ince the constitutional vice in a vague or indefinite statute is the injustice to the accused in placing him on trial for an offense, the nature of which he is given no fair warning, the fact that punishment is restricted to acts done with knowledge that they contravene the statute makes this objection untenable.[77]

The alternative fair warning rule applies to any hybrid statute with a criminal intent requirement[78] that calls for proof of either knowledge of illegality or knowledge of wrongfulness sufficient to make illegality likely.[79] The rule holds that enforcement of a criminal intent requirement defined in these terms alleviates fair warning problems.

The definitions of intent mandated by the alternative fair warning rule are more demanding than the ordinary common-law definition, which requires factual knowledge but not legal knowledge.[80] As distinguished legal scholars have noted, the common-law definition does not eliminate fair warning problems:

> [S]cienter—at least as it has been traditionally defined—cannot cure vagueness in a statute or regulation. One "knowingly" commits an offense when he knows that his acts will bring about certain results (those defined in the statute in question), and whether he knows that deliberately causing such results is proscribed by statute is immaterial. Because it is knowledge of the consequences of one's actions and not knowledge of the existence or meaning of the criminal law which is relevant, it seems clear that uncertain language in a statute is not clarified by the addition of a scienter element. . . . Or, to put it . . . another way, it is possible willfully to

76. 339 U.S. 382 (1950).

77. *Id.* at 413. *See* Vill. of Hoffman Estates v. Flipside, Hoffman Estates, Inc., 455 U.S. 489, 499 (1982) (noting that "a scienter requirement may mitigate . . . the adequacy of notice to the complainant that his conduct is proscribed") (footnote omitted); Screws v. United States, 325 U.S. 91, 102 (1945) (noting that "[t]he requirement that the act must be willful or purposeful . . . relieve[s] the statute of the objection that it punishes without warning an offense of which the accused was unaware"); United States v. Ragen, 314 U.S. 513, 524 (1942) (noting that "[a] mind intent upon willful evasion is inconsistent with surprised innocence").

78. There is a presumption in favor of a criminal intent requirement even where the statute in question does not explicitly so provide. *E.g.*, Posters 'N' Things, Ltd. v. United States, 511 U.S. 513, 522–23 (1994); United States v. Unites States Gypsum Co., 438 U.S. 422, 437 (1978).

79. These definitions of intent are adopted from Anthony G. Amsterdam, Note, *The Void-for-Vagueness Doctrine in the Supreme Court*, 109 U. PA. L. REV. 67, 87 n.98 (1960); *see also* 1 LAFAVE & SCOTT, *supra* note 65, § 2.3, at 130–31 (by implication). For why these definitions are necessary, see *infra* notes 80–81 and accompanying text.

80. *See* 1 LAFAVE & SCOTT, *supra* note 65, § 2.3 at 130; W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS 34 (5th ed. 1984).

bring about certain results and yet be without fair warning that such conduct is proscribed.[81]

The alternative fair warning rule liberates courts from the strict construction that the default fair warning rule would otherwise require.[82] The Supreme Court's 1978 decision in *United States v. United States Gypsum Co.*[83] provides an illustration. In *Gypsum*, the Court concluded that criminal liability under the Sherman Antitrust Act should call for proof of intent despite the absence of an intent requirement from the statutory text.[84] In support of this conclusion, the Court mentioned not only the "generally inhospitable attitude to non-*mens rea* offenses"[85] but also reasons that pertained to the Sherman Antitrust Act specifically.[86] These reasons included the fact that the Act contains broadly worded prohibitions that do not clearly identify the nature of the conduct that is criminalized.[87] To provide fair warning by construing the prohibitions strictly, however, would involve jettisoning a considerable body of caselaw in which the Act "has been construed to have a 'generality and adaptability comparable to that found to be desirable in constitutional provisions.'"[88] A criminal intent requirement, on the other hand, would render strict construction inapposite and thereby preserve the flexible judicial interpretation that the Court believed Congress wanted.[89]

3. The Differentiated Intent Rule

Because the core principle limits prohibitions to a single construction, courts cannot interpret them to require more egregious conduct for criminal liability than for civil liability. But if the same conduct triggers

81. 1 LAFAVE & SCOTT, *supra* note 65, § 2.3 at 130–31 (footnotes omitted); *see* Amsterdam, *supra* note 79, at 87 n.98.

The Supreme Court has adopted various formulations for the level of intent necessary to eliminate fair warning problems. *Compare* Am. Communications Ass'n v. Douds, 339 U.S. 382, 413 (1950) (requiring "acts done with knowledge that they contravene the statute"), *with* Boyce Motor Lines, Inc. v. United States, 342 U.S. 337, 342 (1952) (requiring acts done with knowledge of the facts but not necessarily knowledge of the law), *and United States Gypsum Co.*, 438 U.S. at 444 (requiring "action undertaken with knowledge of its probable consequences and having the requisite anticompetitive effects").

82. *Cf.* United States v. Thompson/Ctr. Arms Co., 504 U.S. 505, 517 (1992) (noting that the absence of a willfulness requirement for criminal actions under the National Firearms Act necessitates strict construction of the Act's prohibitions); United States v. Standard Oil Co., 384 U.S. 224, 236 (1966) (Harlan, J., dissenting) (noting that strict construction is "particularly important under a statute . . . which imposes criminal penalties with a minimal, if any, scienter requirement") (footnote omitted).

83. 438 U.S. 422 (1978).

84. *See id.* at 434–43.

85. *Id.* at 438.

86. *Id.* at 438–43.

87. *Id.* at 440–41 (observing that "the behavior proscribed by the Act is often difficult to distinguish from the gray zone of socially acceptable and economically justifiable business conduct").

88. *Id*. at 439 (quoting Appalachian Coals, Inc. v. United States, 288 U.S. 344, 359–60 (1933)).

89. Another reason given for upholding a criminal intent requirement under the Sherman Antitrust Act was that the requirement would establish a civil/criminal distinction. *See infra* notes 95–99 and accompanying text.

both civil and criminal liability, there is the risk that some marginal offenders will be prosecuted and convicted as the result of prosecutorial indiscretion.[90] To mitigate this risk, Congress sometimes establishes an intent requirement for criminal liability that does not apply to civil liability.[91]

The differentiated intent rule comes into play for hybrid statutes that have a criminal intent requirement and either a less stringent civil intent requirement or no civil intent requirement at all. Unlike the alternative fair warning rule,[92] the differentiated intent rule does not direct courts to enforce a specific definition of criminal intent. Rather, the differentiated intent rule directs them simply to treat the criminal intent requirement in a manner that maintains the civil/criminal distinction the requirement was designed to provide. Thus, they should not dismiss the requirement as boilerplate.[93] Nor should they allow the requirement to become indistinguishable from the less stringent intent requirement (if any) applicable to civil actions.[94]

The Supreme Court has acknowledged the role that an intent requirement can play under a hybrid statute in differentiating the civil and criminal liability requirements. Recall again the Court's decision in *United States v. United States Gypsum Co.*,[95] which upheld an intent requirement for criminal actions under the Sherman Antitrust Act.[96] The Court did not extend the requirement to civil actions, however.[97] In its view, Congress wanted to differentiate the requirements of civil liability from those of criminal liability. Evidence that Congress desired such a differentiation lay in the statutory sanctions, which consisted of "a range of nonpenal alternatives,"[98] on the one hand, coupled with criminal penalties that included imprisonment on the other hand.[99]

90. *Cf.* Henry M. Hart, Jr., *The Aims of the Criminal Law,* 23 LAW & CONTEMP. PROBS. 401, 424 (1958) (criticizing the idea that "prosecutors only pick out the really guilty ones for criminal prosecution").

91. Hybrid statutes with a criminal intent requirement that does not apply to civil liability include the Exchange Act, see *infra* notes 205–14, accompanying text, and the Clean Water Act, 33 U.S.C. § 1319(c)(2)(A) (1994). While the Sherman Antitrust Act does not fit this pattern as written, it has nonetheless been so construed. *See infra* notes 95–99 and accompanying text. A hybrid statute with no intent requirement for criminal actions is the National Firearms Act. *See* 26 U.S.C. § 5871 (1994). *See also* United States v. Thompson/Ctr. Arms Co., 504 U.S. 505, 517 (1992) (explicitly making this point about the National Firearms Act).

92. For discussion of the alternative fair warning rule, see *supra* notes 76–89 and accompanying text.

93. *Cf.* United States v. English, 92 F.3d 909, 915 (9th Cir. 1996) (refusing to reverse a conviction for fraud under the Securities Act of 1933 despite the failure to instruct the jury on the willfulness requirement on the ground that fraud is "inherently nefarious").

94. *Cf.* United States v. DeSantis, 134 F.3d 760, 764 (6th Cir. 1998) (equating the intent requirement relevant to criminal actions under the Exchange Act with the intent requirement relevant to civil actions under that Act).

95. 438 U.S. 422 (1978).

96. *See supra* notes 83–89 and accompanying text.

97. United States v. United States Gypsum Co., 438 U.S. 422, 436 n.13 (1978).

98. *Id*. at 442.

99. *Id.* at 442–43 & n.18.

In short, the Supreme Court has provided an analytic framework for the construction of hybrid statutes. It is against this framework that decisions construing individual hybrid statutes should be evaluated.

III. THE CORE PRINCIPLE AND THE EXCHANGE ACT

This Part examines whether courts follow the core principle when construing the Exchange Act. Some background about the Act is therefore in order.

A. Exchange Act Background

The Exchange Act authorizes criminal actions as well as two types of civil actions—those brought by the Commission and those brought by private plaintiffs.[100] The Commission is entitled to bring civil actions to enforce all prohibitions in the Act and its accompanying rules and regulations.[101] In contrast, private plaintiffs are entitled to enforce only those prohibitions as to which private actions have been created either expressly[102] or by judicial implication.[103] The volume and significance of private litigation has been considerable, however, largely because of judicial recognition of implied private actions under some of the Exchange Act's most important prohibitions—section 10(b) and Rule 10b-5, section 14(a)[104] and Rule 14a-9,[105] and section 14(e).[106]

Criminal actions under the Exchange Act are within the exclusive control of the Justice Department.[107] Convictions can rest on the violation of any prohibition in the Exchange Act and its accompanying rules

100. The Exchange Act also gives the Commission authority to bring administrative proceedings. *See* § 21C of the Exchange Act, 15 U.S.C. § 78u-3 (1994). Administrative proceedings are beyond the scope of this article. *See supra* note 23.

101. *See* § 21(d)(1) of the Exchange Act, 15 U.S.C. § 78u(d)(1) (1994) [hereinafter § 21(d)(1)]. Section 21(d)(1) authorizes the Commission to file an action in federal district court under the following circumstances:

> Whenever it shall appear . . . that any person is engaged or is about to engage in acts or practices constituting a violation of any provision of this chapter, the rules or regulations thereunder, the rules of a national securities exchange or registered securities association of which such person is a member or a person associated with a member, the rules of a registered clearing agency in which such person is a participant, or the rules of the Municipal Securities Rulemaking Board. . . .

Id. § 21(d)(1). Section 21(d)(3) authorizes the Commission to seek civil penalties. *See* 15 U.S.C. § 78u(d)(3) (1994).

102. The express private actions are set forth in the following sections of the Exchange Act: § 9(e), 15 U.S.C. § 78i(e) (1994) [hereinafter § 9(e)]; § 18(a), 15 U.S.C. § 78r(a) (1994); and § 16(b), 15 U.S.C. § 78p(b) (1994). For discussion of the express private actions, see 9 LOUIS LOSS & JOEL SELIGMAN, SECURITIES REGULATION 4278–4312 (3d ed. 1992 & Supp. 2000).

103. For the history of implied private actions under the Exchange Act, see 9 LOSS & SELIGMAN, *supra* note 102, at 4312–39.

104. Section 14(a) of the Exchange Act, 15 U.S.C. § 78n(a) (1994) [hereinafter § 14(a)].

105. Rule 14a-9, 17 C.F.R. § 240.14a-9 (2000) [hereinafter Rule 14a-9].

106. Section 14(e) of the Exchange Act, 15 U.S.C. § 78n(e) (1994) [hereinafter § 14(e)]. For discussion of the Exchange Act's implied private actions, see 9 LOSS & SELIGMAN, *supra* note 102, at 4339–4427.

107. *See* 17 C.F.R. § 202.5(f) (2000).

and regulations so long as there is proof that the defendant acted "willfully."[108] Authorized criminal penalties include imprisonment for up to ten years, a fine of up to $1 million, or both.[109]

B. The Core Principle in the Supreme Court

The Supreme Court has devoted little attention to the core principle in the context of the federal securities laws. There is one relevant decision involving the Exchange Act as well as two others involving the closely related Securities Act of 1933 ("Securities Act").[110]

Consider first the Court's 1943 decision in *SEC v. C.M. Joiner Leasing Corp.*[111] At issue in *Joiner* was whether oil lease assignments met the definition of a "security" under the Securities Act[112] by virtue of being either an "investment contract" or "any interest or instrument commonly known as a security."[113] Because criminal as well as civil actions under the Securities Act must involve a "security," the defendants argued that the definition of that term should be construed strictly.[114] The Court rejected this argument, holding that Congress intended the definition to embrace oil lease assignments regardless of whether enforcement was civil or criminal.[115] By giving the definition a unitary construction, the Court seemed to accord the core principle its imprimatur.[116]

But the *Joiner* Court's apparent acceptance of the core principle was not as instructive as might first appear. Indeed, the Court did not say whether it would have adhered to the core principle if it had found the definition ambiguous.[117] Under such circumstances, it might have concluded that strict construction was appropriate in a criminal action to alleviate fair warning concerns, but not in a civil action.[118]

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108. Section 32(a) of the Exchange Act, 15 U.S.C. § 78ff(a) (1994) [hereinafter § 32(a)]. Section 32(a) provides that criminal liability can be imposed on "[a]ny person who *willfully* violates any provision of this chapter . . . or any rule or regulation thereunder the violation of which is made unlawful or the observance of which is required under the terms of this chapter." 15 U.S.C. § 78ff(a) (1994) (emphasis added).

109. *Id.* A fine of up to $2.5 million is authorized when the defendant "is a person other than a natural person." *Id.*

110. Securities Act of 1933, 15 U.S.C. § 77(a)–(mm) (1994 & Supp. II 1996).

111. 320 U.S. 344 (1943).

112. Section 2(a)(1) of the Securities Act, 15 U.S.C. § 77b(a)(1) (Supp. II 1996).

113. That definition encompasses a laundry list of instruments, of which these are two. *Id.*

114. *Joiner*, 320 U.S. at 353. The Court acknowledged the significance of this argument by querying: "What . . . shall we say of the construction of a section like this which may be the basis of either civil proceedings of a preventive or remedial nature or of punitive proceedings, or perhaps both?" *Id.*

115. *Id.* at 355.

116. For illustrative decisions that cite *Joiner* for the proposition that Exchange Act prohibitions have only one construction, see *United States v. Charnay*, 537 F.2d 341, 348 (9th Cir. 1976); *United States v. Fields*, [1977–78 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,074 at 91,855 (S.D.N.Y. June 3, 1977), *aff'd in part, rev'd in part on other grounds*, 592 F.2d 638 (2d Cir. 1978).

117. *Cf.* SEC v. C.M. Joiner Leasing Corp., 320 U.S. 344, 355 (1943) (noting that "[i]n the present case we do nothing to the words of the Act; we merely accept them").

118. *Cf.* United States v. Naftalin, 441 U.S. 768, 778–79 (1979), discussed *infra* notes 119–22 and accompanying text.

The Court in fact adopted that position in dictum thirty-six years later in *United States v. Naftalin.*[119] After holding that section 17(a)(1) of the Securities Act[120] clearly prohibited fraud against brokers as well as fraud against investors,[121] the Court announced that it would have read the language in the criminal defendant's favor had it been ambiguous: "This is a *criminal* case, and we have long held that . . . a [criminal] defendant may not 'be subjected to a penalty unless the words of the statute plainly impose it.'"[122] By endorsing strict construction because the case was criminal, the Court implied that strict construction would have been inappropriate if the case had been civil.

One year later in *Aaron v. SEC*,[123] the Court endorsed the core principle in a case that did not involve ambiguous statutory language. At issue was whether the Commission had to prove scienter when enforcing section 10(b) of the Exchange Act and Rule 10b-5.[124] The Commission argued that the Court was not bound to follow its decision in *Ernst & Ernst v. Hochfelder*,[125] which had upheld a scienter requirement for implied private actions based on the language and history of section 10(b).[126] According to the Commission, *Hochfelder* was distinguishable because it had involved an implied private action rather than a Commission action.[127] The Court rejected the Commission's argument: "[T]he rationale of *Hochfelder* ineluctably leads to the conclusion that scienter is an element of a violation of section 10(b) and Rule 10b-5, regardless of the identity of the plaintiff or the nature of the relief sought."[128] Thus, the Court had no occasion to address whether it would have upheld a scienter requirement for Commission actions had section 10(b)'s language and history been unclear on the subject.

In short, the Court has accepted the core principle in two securities decisions and rejected it in dictum in another. Even its acceptances of the core principle are relatively limited, however, because both involved statutory language that the Court deemed unambiguous. The Court did not indicate whether it would have stood by the core principle if it had found the language ambiguous.[129]

119. 441 U.S. 768 (1979).
120. Section 17(a)(1) of the Securities Act, 15 U.S.C. § 77q(a)(1) (1994).
121. *Naftalin*, 441 U.S. at 777.
122. *Id.* at 778–79 (emphasis added) (quoting United States v. Campos-Serrano, 404 U.S. 293, 297 (1971), quoting Keppel v. Tiffin Sav. Bank, 197 U.S. 356, 362 (1905)).
123. 446 U.S. 680 (1980).
124. *Id.* at 682.
125. 425 U.S. 185 (1976).
126. *Id.* at 197–211; *see also* Aaron v. SEC, 446 U.S. 680, 689–91 (1980).
127. *See Aaron*, 446 U.S. at 691.
128. *Id.* at 691.
129. *See supra* notes 111–16 & 123–28 and accompanying text.

C. The Core Principle in the Lower Federal Courts

Before 1980, lower federal courts expressed support for the core principle when construing the Exchange Act. One court stated that aside from the burden of proof and the willfulness requirement, "criminal and civil liability under the securities laws are coextensive."[130] Another court observed that "there is no reasonable basis for holding that some different interpretation [of section 10(b) and Rule 10b-5] should apply to a criminal action [than to a civil action]."[131] Beginning in the 1980s, however, the tide turned. At least some lower federal courts abandoned the core principle to accommodate changes that were taking place with respect to criminal actions,[132] implied private actions,[133] and actions involving international securities fraud.[134]

1. Criminal Actions

Until the 1980s, criminal actions under the Exchange Act rarely posed legal questions of first impression. Instead, they tended to involve merely the application of principles previously established in civil actions.[135] Therefore, when defendants argued that they lacked fair warning of the conduct constituting crimes, lower federal courts could respond that the applicable principles were already on the books.[136]

The situation changed in the 1980s, when the Justice Department—its interest in securities regulation piqued by the insider trading scandals

130. United States v. Chiarella, 588 F.2d 1358, 1368 n.16 (2d Cir. 1978), *rev'd on other grounds*, 445 U.S. 222 (1980).

131. United States v. Clark, 359 F. Supp. 128, 130 (S.D.N.Y. 1973); *see also* United States v. Gleason, 616 F.2d 2, 28 (2d Cir. 1979) (noting that "[i]t is . . . settled that the same standards apply to civil and criminal liability under the securities law"); United States v. Charnay, 537 F.2d 341, 348 (9th Cir. 1976) (observing that "the primary difference between criminal and civil prosecutions under the securities laws is the burden of proof"); United States v. Fields, [1977–78 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,074 at 91,855 (S.D.N.Y. June 3, 1977) (observing that the meaning of § 14(a) is "the same" in a criminal action as in a civil action), *aff'd in part, rev'd in part*, 592 F.2d 638 (2d Cir. 1978); *see also* SEC v. Burns, 614 F. Supp. 1360, 1367 (S.D. Cal. 1985) (suggesting that a prohibition must be strictly construed in a civil action if it would have to be so construed in a criminal action), *aff'd on other grounds*, 816 F.2d 471 (9th Cir. 1987); Drasner v. Thomson McKinnon Sec., Inc., 433 F. Supp. 485, 498–99 (S.D.N.Y. 1977) (same). *But see* United States v. Chiarella, 588 F.2d 1358, 1377–78 (2d Cir. 1978) (Meskill, J., dissenting) (arguing that § 10(b) and Rule 10b-5 should be construed more restrictively in criminal actions than in civil actions), *rev'd*, 445 U.S. 222 (1980).

132. *See infra* notes 135–54 and accompanying text.

133. *See infra* notes 155–67 and accompanying text.

134. *See infra* notes 168–75 and accompanying text.

135. *E.g.*, United States v. Gleason, 616 F.2d 2, 28 (2d Cir. 1979) (applying civil precedent on the meaning of materiality); United States v. Cook, 573 F.2d 281, 283 (5th Cir. 1978) (applying civil precedent on extraterritoriality); United States v. Charnay, 537 F.2d 341, 348–49 (9th Cir. 1976) (applying civil precedent as to what constitutes manipulation); United States v. Koenig, 388 F. Supp. 670, 701, 715 (S.D.N.Y. 1974) (applying civil precedent on the meaning of materiality and Rule 10b-5's "in connection with" requirement).

136. *E.g.*, United States v. Farris, 614 F.2d 634, 642 (9th Cir. 1979) (relying on civil precedent for the definition of the term "security"); United States v. Persky, 520 F.2d 283, 288 (2d Cir. 1975) (relying on civil precedent for the meaning of Rule 10b-5's "in connection with" requirement).

besetting Wall Street[137]—stepped up its prosecution of cases with the capacity to break new legal ground.[138] The novelty of the government's arguments raises the question whether courts should apply strict construction in order to provide fair warning.[139] Some courts have given an affirmative answer, while at the same time maintaining that strict construction is probably inapplicable to civil actions.[140]

Consider *United States* v. *Rudi*, a 1996 decision of the Southern District of New York.[141] *Rudi* involved a criminal action under section 15B(c)(1) of the Exchange Act,[142] which prohibits brokers and dealers from violating rules of the Municipal Securities Rulemaking Board.[143] The rule at issue mandated accurate maintenance of "records relating to transactions in municipal securities."[144] The inaccurate records in question had come into existence only after the transaction had closed.[145] The Justice Department argued that the Rule was nonetheless applicable: "[T]ransactions like the one at issue here are routinely followed by post-closing balancing payments, adjustments of accounts and financial statements, whose accuracy is so germane to the transaction itself that if the records are false the whole transaction is tainted, the statute is invoked, and a crime committed."[146] Describing the Justice Department's argument as "plausible,"[147] the court nonetheless rejected it on the ground

137. *See* Harvey L. Pitt & Karen L. Shapiro, *Securities Regulation by Enforcement: A Look Ahead at the Next Decade*, 7 YALE J. REG. 149, 219–20 (1990).

138. *Id.* at 219–20, 292–93. For illustrative criminal cases of this type, see United States v. O'Hagan, 521 U.S. 642, 649–66 (1997) (analyzing argument made by the government in favor of the misappropriation theory of insider trading); United States v. Bingham, 992 F.2d 975, 976 (9th Cir. 1993) (analyzing the government's arguments in favor of two per se rules regarding materiality); United States v. Teicher, 987 F.2d 112, 120 (2d Cir. 1993) (analyzing the government's argument that a prima facie case of insider trading does not require proof that the defendant used the illegal tip in making his trade); United States v. Chestman, 947 F.2d 551, 569 (2d Cir. 1991) (analyzing the government's argument in favor of a liberal definition of relationships of trust for purposes of the misappropriation theory of insider trading); United States v. Mulheren, 938 F.2d 364, 368 (2d Cir. 1991) (analyzing the government's argument as to the meaning of manipulation under Rule 10b-5); United States v. Holtzclaw, 950 F. Supp. 1306, 1313–14 (S.D. W. Va. 1997) (analyzing the government's argument that horizontal commonality should not be a prerequisite to establishing an "investment contract" when the Fourth Circuit lacked precedent on point and the other circuits were divided), *aff'd in part, vacated in part on other grounds*, 131 F.3d 137 (4th Cir. 1997); United States v. Rudi, 927 F. Supp. 686, 688 (S.D.N.Y. 1996) (analyzing the government's argument involving the scope of rule regulating municipal securities transactions).

139. *Cf.* United States v. Lanier, 520 U.S. 259, 266 (1997) (noting that "due process bars courts from applying a novel construction of a criminal statute to conduct that neither the statute nor any prior judicial decision has fairly disclosed to be within its scope").

140. *E.g.*, *Chestman*, 947 F.2d at 567, 569–70, discussed *infra* notes 145–49 and accompanying text; *Rudi*, 927 F. Supp. at 688, discussed *infra* notes 141–49 and accompanying text; *see also* United States v. Jones, 648 F. Supp. 225, 232–34 (S.D.N.Y. 1986), *aff'd in part, rev'd in part on other grounds sub nom.* United States v. Blackmon, 839 F.2d 900 (2d Cir. 1988).

141. 927 F. Supp. 686 (S.D.N.Y. 1996).

142. Section 15B(c)(1) of the Exchange Act, 15 U.S.C. § 78o-4(c)(1) (1994).

143. *Id.*

144. Rule G-8(b), MSRB Manual (CCH) ¶ 3536 (1999).

145. *Rudi*, 927 F. Supp. at 687.

146. *Id*. at 688.

147. *Id*.

that the records were "too remote and peripheral" to the transaction to provide the predicate for a criminal conviction.[148] The court cautioned, however, that the result might be different in a civil case: "Although . . . [the government's] arguments may be given scope in civil proceedings under the securities laws, the proximity [between the records and the municipal securities transaction] must be more rigorously examined in criminal cases."[149]

Consider also the Second Circuit's 1991 decision in *United States v. Chestman*.[150] In *Chestman*, the defendant was convicted of insider trading in violation of section 10(b) and Rule 10b-5.[151] The conviction was based on the misappropriation theory, which requires (among other things) that the defendant know that the person who tipped him breached a relationship of trust by so doing.[152] The court disregarded the core principle by its very framing of the question at issue: "[W]hat constitutes a fiduciary or similar relationship of trust and confidence *in the context of Rule 10b-5 criminal liability*?"[153] Moreover, it rejected the government's "suitable occasion" test for such relations in a manner that suggested the test's possible application to civil actions:

> Useful as . . . an elastic and expedient definition of . . . relations of trust and confidence . . . may be in the civil context, it has no place in the criminal law. A "suitable occasion" test for determining the presence of criminal fraud would offend not only the rule of lenity but due process as well. More than a perfunctory nod at the rule of lenity . . . is required. We will not apply outer permutations of chancery relief in addressing what is frequently the core inquiry in a Rule 10b-5 criminal conviction—whether a fiduciary duty has been breached.[154]

Thus, the courts in *Rudi* and *Chestman* suggest that prohibitions should be construed strictly in criminal actions but not in civil actions. By sanctioning different interpretations for different enforcement contexts, these courts violated the core principle.

148. *Id.*

149. *Id*.

150. 947 F.2d 551 (2d Cir. 1991).

151. *Id.* at 554.

152. *Id.* at 570. *See generally* WILLIAM K.S. WANG & MARC I. STEINBERG, INSIDER TRADING § 5.4.2 (1996 & Supp. 1998).

153. *Chestman*, 947 F.2d at 567 (emphasis added).

154. *Id.* at 570 (citations omitted). In *United States v. O'Hagan*, 521 U.S. 642 (1997), Justice Scalia dissented because of the majority's failure to apply the rule of lenity in construing § 10(b) and Rule 10b-5 in the context of a criminal prosecution for insider trading. *See id.* at 679 (Scalia, J., dissenting); Richard W. Painter et al., *Don't Ask, Just Tell: Insider Trading After* United States v. O'Hagan, 84 VA. L. REV. 153, 199 (1998); *see also* United States v. Falcone, 97 F. Supp. 2d 297, 302–03 (E.D.N.Y. 2000) (criticizing courts for disregarding the rule of lenity in the context of insider trading prosecutions under § 10(b) and Rule 10b-5).

2. Implied Private Actions

The 1960s and early 1970s were the heyday for implied private actions under the Exchange Act.[155] During that time, the Supreme Court not only recognized implied private actions under Rule 10b-5[156] and Rule 14a-9[157] but also established presumptions of reliance on behalf of plaintiffs who brought those actions.[158]

The heyday came to a halt in the mid-1970s. In its 1975 decision in *Blue Chip Stamps v. Manor Drug Stores*,[159] the Supreme Court announced that implied private actions under Rule 10b-5 presented an especially grave threat of vexatiousness: "[T]he mere existence of an unresolved lawsuit has settlement value to the plaintiff not only because of the possibility that he may prevail on the merits . . . but because of the threat of extensive discovery and disruption of normal business activities which may accompany a lawsuit which is groundless . . . ."[160] Because of this concern, the Court limited standing to sue under the Rule to those who had purchased or sold the security at issue,[161] thereby excluding those who had, because of fraud, refrained from buying or selling.[162] In subsequent decisions, the Court shortened the limitations period applicable to implied private actions under Rule 10b-5[163] and restricted the presumption of reliance applicable to implied private actions under Rule 14a-9.[164]

In the 1980s, some lower federal courts expanded the war on implied private actions to the prohibitions themselves. Consider the language of section 10(b) and Rule 10b-5 that the fraud occur "in connection with the purchase or sale of a security."[165] This language gives rise to a requirement—known as the "in connection with" requirement—that calls for a linkage between the fraud and a securities trade.[166] Some lower federal courts now make it more difficult to establish this linkage in implied private actions than in other actions. As the Ninth Circuit

155. This time period was marked by judicial activism in the area of securities regulation generally. *See* Margaret V. Sachs, *Judge Friendly and the Law of Securities Regulation: The Creation of a Judicial Reputation*, 50 SMU L. REV. 777, 784–89 (1997).

156. *See* Superintendent of Ins. v. Bankers' Life & Cas. Co., 404 U.S. 6, 13 n.9 (1971).

157. *See* J.I. Case Co. v. Borak, 377 U.S. 426, 431–32 (1964).

158. *See* Affiliated Ute Citizens v. United States, 406 U.S. 128, 152–54 (1972) (presumption under Rule 10b-5); Mills v. Elec. Auto-Lite Co., 396 U.S. 375, 384–85 (1970) (presumption under Rule 14a-9).

159. 421 U.S. 723 (1975).

160. *Id.* at 742–43.

161. *Id*. at 747–49.

162. *Id.* at 743.

163. *See* Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson, 501 U.S. 350, 364 (1991).

164. *See* Va. Bankshares, Inc. v. Sandberg, 501 U.S. 1083, 1099–1108 (1991) (refusing minority shareholders suing under § 14(a) and Rule 14a-9 a presumption of reliance in situations where their votes were unnecessary to the approval of the transaction in question).

165. For the text of § 10(b) and Rule 10b-5, see *supra* note 12.

166. For discussion of the "in connection with" requirement, see 8 LOSS & SELIGMAN, *supra* note 102, at 3680–91.

conceded when discussing the "in connection with" requirement in the context of a Commission action: "We have read the 'in connection with' provision somewhat more narrowly in determining whether a private plaintiff may recover damages under Rule 10b-5."[167] In reading the "in connection with" requirement differently in implied private actions than in other actions, these courts violated the core principle.

3. Actions Involving International Securities Fraud

As the securities markets became increasingly internationalized in the early 1970s,[168] lower federal courts had to resolve a question about which the Exchange Act provided no direct guidance: whether and to what extent section 10(b) and Rule 10b-5 apply to fraud perpetrated on foreign nationals who trade securities outside the territory of the United States.[169] Judge Friendly of the Second Circuit, the author of the seminal opinions in this area,[170] maintained that "[w]e do not think Congress intended to allow the United States to be used as a base for manufacturing fraudulent security devices for export, even when these are peddled only to foreigners."[171] He accordingly held Rule 10b-5 applicable so long as

167. SEC v. Clark, 915 F.2d 439, 449 n.18 (9th Cir. 1990); *see also* SEC v. Rana Research, Inc., 8 F.3d 1358, 1362 (9th Cir. 1993) (noting that "[w]hile interpretations of 'in connection with' continue to change as applied to private plaintiffs, its meaning in [Commission] . . . actions remains as broad and flexible as is necessary to accomplish the statute's purpose of protecting investors") (footnote omitted); SEC v. Jakubowski, 912 F. Supp. 1073, 1085–86 (N.D. Ill. 1996) ("While the meaning of 'in connection with' has varied somewhat in actions brought by private plaintiffs, the meaning of the phrase in actions brought by the Commission 'remains as broad and flexible as is necessary to accomplish the statute's purpose of protecting investors.'") (citation omitted); Mark T. Story, Note, *The Pendulum Swings Farther: The "in Connection with" Requirement and Pretrial Dismissals of Rule 10b-5 Private Claims for Damages*, 56 TEX. L. REV. 62 (1977) (demonstrating the impact on the "in connection with" requirement of the Supreme Court's decisions restricting implied private actions). *But cf. In re* Ames Dep't Stores Stock Litig., 991 F.2d 953, 962 (2d Cir. 1993) (reading the "in connection with" requirement broadly in an implied private action involving fraud on the market). Courts appear to have aligned criminal actions with Commission actions so far as construction of the "in connection with" requirement is concerned. *Cf.* United States v. O'Hagan, 521 U.S. 642, 649–66 (1997) (construing the "in connection with" requirement broadly in a criminal action involving the misappropriation theory); United States v. Russo, 74 F.3d 1383, 1390 (2d Cir. 1996) (construing the "in connection with" requirement broadly in a criminal action involving a stock manipulation scheme).

168. For a history of the internationalization of the securities markets, see SEC, REPORT TO SENATE COMM. ON BANKING, HOUSING, AND URBAN AFFAIRS AND HOUSE COMM. ON ENERGY AND COMMERCE ON THE INTERNATIONALIZATION OF THE SECURITIES MARKETS ch. III, at 29–33 (1987).

169. *E.g.*, Bersch v. Drexel Firestone, Inc., 519 F.2d 974, 993 (2d Cir. 1975) (identifying the circumstances under which Rule 10b-5 applies to fraud perpetrated on foreign nationals trading outside the United States but "freely acknowledg[ing] that if we were asked to point to language in the statutes, or even in the legislative history, that compelled these conclusions, we would be unable to respond"). *But cf.* Margaret V. Sachs, *The International Reach of Rule 10b-5: The Myth of Congressional Silence*, 28 COLUM. J. TRANSNAT'L L. 677, 680–82 (1990) (arguing that the Congress that enacted the Exchange Act intended to extend the Act's benefits only to those investors whose trades occur within the United States).

170. *See* 10 LOSS & SELIGMAN, *supra* note 102, at 5100 & n.2 (collecting Judge Friendly's opinions on the international reach of the federal securities laws).

171. IIT v. Vencap, Ltd., 519 F.2d 1001, 1017 (2d Cir. 1975); *see* Bersch v. Drexel Firestone, Inc., 519 F.2d 974, 987 (2d Cir. 1975).

the preponderance of the fraudulent activity occurred in this country.[172] In Judge Friendly's view, the requisite amount of domestic activity did not vary with the form of enforcement: "If there would be subject matter jurisdiction over a suit by the SEC to prevent the concoction of securities frauds in the United States for export, there would also seem to be jurisdiction over a suit for damages or rescission by a defrauded foreign individual."[173]

By the late 1980s, some circuits held that Rule 10b-5 reached fraud perpetrated on foreign nationals trading outside the United States even where the amount of domestic activity was less than a preponderance.[174] Seeking to diminish the impact of these decisions, the District of Columbia Circuit argued that they should apply to Commission actions (and presumably to criminal actions) but not to actions brought by the defrauded foreign nationals themselves:

> The SEC, while an independent agency, is a responsible governmental agency and will surely take into account in framing its enforcement actions any foreign policy concerns communicated to it by the Department of State. A private individual need not and often will not. A court can feel more comfortable asserting jurisdiction if it knows that foreign policy concerns can be accommodated by the plaintiff and are not left entirely to the court's untutored evaluation.[175]

By suggesting that interpretation of Rule 10b-5 should turn on whether enforcement was private or public, the District of Columbia Circuit violated the core principle.

IV. THE RULES AND THE EXCHANGE ACT

This Part examines whether courts construing the Exchange Act follow the rules that implement the core principle. These rules are the all contexts rule,[176] the fair warning rules,[177] and the differentiated intent rule.[178]

172. *See IIT*, 519 F.2d at 1018; *Bersch*, 519 F.2d at 993.

173. *IIT*, 519 F.2d at 1017–18 (footnote omitted).

174. *See* SEC v. Kasser, 548 F.2d 109, 114 (3d Cir. 1977) (concluding that § 10(b) and Rule 10b-5 apply "where at least some activity designed to further a fraudulent scheme occurs within this country"); Cont'l Grain (Australia) Pty., Ltd. v. Pac. Oilseeds, Inc., 592 F.2d 409, 421 (8th Cir. 1979) (concluding that § 10(b) and Rule 10b-5 apply when the conduct in this country is "in furtherance of a fraudulent scheme and . . . significant with respect to its accomplishment"); Grunenthal GmbH v. Hotz, 712 F.2d 421, 423–25 (9th Cir. 1983) (adopting the approach of *Kasser*); *see also* Kauthar SDN BHD v. Sternberg, 149 F.3d 659, 666 (7th Cir. 1998) (noting that the Second Circuit "requires a higher quantum of domestic conduct than do the Third, Eighth, and Ninth Circuits"); Zoelsch v. Arthur Andersen & Co., 824 F.2d 27, 31 (D.C. Cir. 1987) (same).

175. *Zoelsch*, 824 F.2d at 33 n.3. The court added that "[w]hether or not that consideration should be sufficient to allow jurisdiction in an SEC action that would not lie in a private action we need not decide." *Id.*

176. *See supra* notes 52–63 and accompanying text.

177. *See supra* notes 64–89 and accompanying text.

178. *See supra* notes 90–99 and accompanying text.

A. The All Contexts Rule

The all contexts rule holds that when construing prohibitions in hybrid statutes, courts should not focus solely on the immediate enforcement context. Rather, they should take into account every action to enforce the prohibition under the hybrid statute and the policies pertinent to each. If the policies conflict, courts should seek the most appropriate compromise.[179]

Some recent decisions under the Exchange Act have ignored the all contexts rule. Consider the Supreme Court's 1991 decision in *Virginia Bankshares, Inc. v. Sandberg*.[180] There the plaintiffs brought an implied private action under section 14(a) and Rule 14a-9, which prohibit the misrepresentation or omission of a "material fact" in a proxy statement.[181] The issue was whether a "fact" qualifies as an opinion for these purposes.[182] The Court concluded that while an opinion constitutes a "fact,"[183] it is not actionable simply because it is material and "misstate[s] the speaker's reasons."[184] It must also be "false or misleading about its subject."[185] The Court's sole justification for imposing the latter requirement was that it would curb the threat of vexatious private litigation previously recognized in *Blue Chip Stamps v. Manor Drug Stores*:[186]

> [T]o recognize liability on mere disbelief or undisclosed motive without any demonstration that the proxy statement was false or misleading about its subject would authorize § 14(a) litigation confined solely to . . . the "impurities" of a director's "unclean heart." This, we think, would cross the line that *Blue Chip Stamps* sought to

179. *See supra* text accompanying note 52.

180. 501 U.S. 1083 (1991).

181. *Id.*; *see also* 15 U.S.C. § 78n(a) (1994); 17 C.F.R. § 240.14a-9 (2000). For discussion of implied private actions under § 14(a) and Rule 14a-9, see 9 LOSS & SELIGMAN, *supra* note 102, at 4339–75.

182. *Va. Bankshares*, 501 U.S. at 1090. The opinion at issue concerned the value of the company's shares. *Id.*

183. *Id.* at 1095. The Court reached this conclusion by drawing upon its previous decision in *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975). At issue in *Blue Chip Stamps* was whether plaintiffs bringing implied private damages actions under Rule 10b-5 had to be purchasers or sellers of the security in question. *Id.* at 725. The Court adopted a purchaser-seller requirement because of concern that a defendant ordinarily would have no way of ascertaining whether the plaintiff had failed to buy or sell. *Id.* at 746. Hence the absence of a purchaser-seller requirement would present "[t]he very real risk . . . that the door . . . [would] be open to recovery of substantial damages on the part of one who offers only his own testimony to prove that . . . [the defendant's] representations . . . damaged him." *Id.* (footnote omitted). In contrast, the evidence relevant to an opinion is "subject neither to a plaintiff's control nor ready manufacture." *Va. Bankshares*, 501 U.S. at 1094.

184. *Va. Bankshares*, 501 U.S. at 1095.

185. *Id.* at 1095–96. Writing separately, Justice Scalia explained the requirement that the opinion mislead concerning its subject:

> [T]he statement "In the opinion of the Directors, this is a high value for the shares" would produce liability if in fact it was not a high value and the directors knew that. It would not produce liability if in fact it was not a high value but the directors honestly believed otherwise.

Id. at 1108–09 (Scalia, J., concurring in part and dissenting in part).

186. 421 U.S. 723 (1975). For additional discussion of the *Blue Chip Stamps* decision, see *supra* notes 159–62 and accompanying text.

> draw. While it is true that the liability, if recognized, would rest on an actual, not hypothetical, psychological fact, the temptation to rest an otherwise non-existent § 14(a) action on psychological enquiry alone would threaten just the sort of strike suits and attrition by discovery that *Blue Chip Stamps* sought to discourage.[187]

The Court violated the all contexts rule by failing to consider whether the requirement it imposed would have an adverse impact on Commission and criminal actions.[188] If such an impact seemed probable, the Court should have balanced it against the desired curtailment of vexatious private litigation and arrived at the most appropriate compromise.[189]

B. The Fair Warning Rules

To provide fair warning of the conduct constituting crimes, courts should determine which of two rules is appropriate to the hybrid statute before them—the default fair warning rule or the alternative fair warning rule. Courts should make this determination not only when the action before them is criminal but also when it is civil because the default fair warning rule affects the construction of prohibitions in civil as well as criminal actions.[190]

1. The Default Fair Warning Rule

The default fair warning rule holds that a court must construe a prohibition strictly in a civil action if it would be required to do so in a criminal action to provide fair warning. By mandating strict construction, the rule strips courts of the flexibility to interpret ambiguities in ac-

187. *Va. Bankshares*, 501 U.S. at 1096 (citation omitted).

188. At least some private plaintiffs have found the requirement burdensome. *E.g.*, Mendell v. Greenberg, 938 F.2d 1528, 1529 (2d Cir. 1991) (damages action for failure to disclose founding family's motive in seeking cash-out merger; trial court instructed to require evidence of the inadequacy of the merger price "before . . . enter[ing] the morass of alleged motivation"); Zemel Family Trust v. Philips Int'l Realty Corp., [Current Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 91,271 at 95,496 (S.D.N.Y. Nov. 30, 2000) (motion to preliminarily enjoin a liquidation for failure to disclose the CEO's motive regarding the liquidation's terms; motion denied in part because of the absence of evidence that the terms will cause injury to the shareholders); *see also* Freedman v. Value Health, Inc., 958 F. Supp. 745, 753 (D. Conn. 1997) (noting that "plaintiffs do not state a cause of action with respect to an opinion statement unless they offer allegations that the statement was incorrect or misleading as to both its objective and subjective aspects").

189. By focusing only on the policies relevant to implied private actions, the Court invited the conclusion that the requirement it imposed applies to private actions only. The invitation appears to have been accepted, since *Virginia Bankshares* has yet to be cited in any reported securities decision involving an action brought by the Commission or the Justice Department. *Cf.* SEC v. Pros Int'l, Inc., 994 F.2d 767 (10th Cir. 1993) (fraudulent opinion at issue but no mention of *Va. Bankshares)*; SEC v. Deyon, 977 F. Supp. 510, 517–18 (D. Me. 1997) (same). *But cf.* United States v. Morris, 80 F.3d 1151, 1164–65 (7th Cir. 1996) (suggesting that *Va. Bankshares* applies to a criminal action involving mail and wire fraud).

190. *See supra* note 66 and accompanying text.

cordance with the policies that prompted the hybrid statute's enactment.[191]

Some lower federal courts have construed Exchange Act ambiguities strictly in criminal actions, thereby foregoing the opportunity to resolve them in a manner that promotes the underlying statutory policy of combating unscrupulousness in the securities markets.[192] These courts have suggested, however, that they would probably not apply strict construction in civil actions.[193]

These decisions are flawed in two respects. First, they do not extend strict construction to civil actions as the default fair warning rule requires.[194] Second, and more fundamentally, they fail to recognize that there is no need to engage in strict construction in order to provide fair warning of Exchange Act crimes. Indeed, as this article shows, all that is necessary in this regard is to enforce the Exchange Act's willfulness requirement in accordance with the alternative fair warning rule.[195]

2. The Alternative Fair Warning Rule

The alternative fair warning rule applies to any hybrid statute with a criminal intent requirement that calls for proof of either knowledge of illegality or knowledge of wrongfulness sufficient to make illegality likely. The rule holds that enforcement of a criminal intent requirement defined in these terms alleviates fair warning problems.[196]

a. Applicability to the Exchange Act

While section 32(a) of the Exchange Act conditions criminal liability on proof that the defendant acted "willfully,"[197] it precludes defining willfulness as knowledge of illegality—one of the two definitions that satisfies the alternative fair warning rule.[198] To understand why, consider

191. *See supra* note 67 and accompanying text.

192. *E.g.*, United States v. Chestman, 947 F.2d 551, 567–70 (2d Cir. 1991) (strictly construing the relationship of trust and confidence that is a prerequisite to liability for insider trading under § 10(b) and Rule 10b-5 based on the misappropriation theory); United States v. Rudi, 927 F. Supp. 686, 688 (S.D.N.Y. 1996) (strictly construing Municipal Securities Regulation Board rule); United States v. Jones, 648 F. Supp. 225, 233–34 (S.D.N.Y. 1986) (strictly construing § 10(b) and Rule 10b-5 with respect to their applicability to transactions involving nonexistent securities), *aff'd in part, rev'd in part on other grounds sub nom.* United States v. Blackmon, 839 F.2d 900 (2d Cir. 1988). *But see* United States v. Peltz, 433 F.2d 48, 53 (2d Cir. 1970) (rejecting strict construction of § 10(b) and Rule 10b-5 in part because of the "adverse effect on the public").

193. *E.g.*, *Chestman*, 947 F.2d at 567, 569–70; *Rudi*, 927 F. Supp. at 688; *Jones*, 648 F. Supp. at 232–34; *see also* United States v. Naftalin, 441 U.S. 768, 778–79 (1979) (endorsing strict construction of ambiguities in criminal actions under the Securities Act but suggesting that that approach would be inapplicable to civil actions).

194. *See supra* note 66 and accompanying text.

195. *See infra* notes 197–206 and accompanying text.

196. *See supra* notes 78–79 and accompanying text.

197. For the text of § 32(a), see *supra* note 108.

198. *See supra* note 79 and accompanying text.

section 32(a)'s final clause ("no knowledge" clause): "[N]o person shall be subject to imprisonment under this section for the violation of any rule or regulation if he proves that he had no knowledge of such rule or regulation."[199] The "no knowledge" clause contemplates that at least some defendants will be convicted and fined despite a lack of knowledge that their conduct was illegal.[200]

On the other hand, the "no knowledge" clause does not preclude defining willfulness as knowledge of wrongfulness sufficient to make illegality likely—the second of the two definitions that satisfies the alternative fair warning rule.[201] Nor is such a definition of willfulness countermanded by the legislative history[202] or by a general jurisprudence of willfulness that cuts across statutory boundaries.[203] Thus, the alternative fair warning rule applies to the Exchange Act provided courts define willfulness as knowledge of wrongfulness sufficient to make illegality likely.

199. Section 32(a) of the Exchange Act, 15 U.S.C. § 78ff(a) (1994).

200. *See* United States v. Peltz, 433 F.2d 48, 54–55 (2d Cir. 1970). The "no knowledge" clause comes into play when the prohibition at issue appears in a rule or regulation only and not in the Exchange Act itself. *See* United States v. Lilley, 291 F. Supp. 989, 992 (S.D. Tex. 1968) (noting that "[i]t would frustrate the intent of Congress to permit a person whose conduct is expressly prohibited by statute to attempt to prove no knowledge of a parallel rule provision").

201. *See supra* note 79 and accompanying text.

202. The legislative history of the Exchange Act is assembled in 4–11 LEGISLATIVE HISTORY OF THE SECURITIES ACT OF 1933 AND SECURITIES EXCHANGE ACT OF 1934 (J.S. Ellenberger & Ellen P. Mahar eds., 1973) [hereinafter LEGISLATIVE HISTORY]. During the House Hearings, drafter Thomas Corcoran confessed uncertainty about the meaning of "willfully." *See* Exchange Act House Hearings, *reprinted in* 8 LEGISLATIVE HISTORY, *supra*, item 23, at 113 (asserting that "willfully" means "knowingly" but acknowledging that "I may be wrong" and that the statute "needs redrafting" on the point). Moreover, comments made during the Senate hearings by committee counsel Pecora fail to give "willfully" any precise substantive content. *See* Exchange Act Senate Hearings, *reprinted in* 6 LEGISLATIVE HISTORY, *supra*, item 22, at 6967 (noting that a willful violation is "something far different from an unwitting or innocent violation"); *id.* at 6969 (explaining that criminal liability could not be premised on an "unwitting violation"); Exchange Act Senate Hearings, *reprinted in* 7 LEGISLATIVE HISTORY, *supra*, item 22, at 7465 (noting that "a mere slip would not be a willful violation"); *id*. (stating that "[t]here is a great difference between a willful violation of a penal statute and an innocent violation of it"). A commentator writing at the time of the Exchange Act's enactment argued that Congress had affirmatively equated willfulness with "a realization on the defendant's part that he was doing a wrongful act." William B. Herlands, *Criminal Aspects of the Securities Exchange Act of 1934*, 21 VA. L. REV. 139, 149 (1934). But this argument was not supported by specific references to the legislative history. *See id.*

203. Numerous federal statutes condition criminal liability on proof that the defendant acted "willfully." *See* Sharon L. Davies, *The Jurisprudence of Willfulness: An Evolving Theory of Excusable Ignorance*, 48 DUKE L.J. 341, 420–27 (1998) (listing such statutes). But no generally accepted definition of willfulness has emerged. *See* Bryan v. United States, 524 U.S. 184, 191 (1998) (characterizing "willfully" as "a word of many meanings," quoting Spies v. United States, 317 U.S. 492, 497 (1943)); Lydia Pallas Loren, *Digitization, Commodification, Criminalization: The Evolution of Criminal Copyright Infringement and the Importance of the Willfulness Requirement*, 77 WASH. UNIV. L.Q. 835, 873 (1999) (noting the uncertain meaning of "willfulness" in federal criminal legislation in general and in federal criminal copyright infringement in particular). *But cf.* Davies, *supra*, at 343 (noting the growing judicial inclination to equate willfulness with knowledge of illegality). The Model Penal Code equates "willfully" with "knowingly . . . unless a purpose to impose further requirements appears." MODEL PENAL CODE § 2.02(8) (1985).

The applicability of the alternative fair warning rule to the Exchange Act avoids a seemingly insoluble conflict. Indeed, if the rule did not apply, the default fair warning rule would come into play, with its directive to courts to construe ambiguities strictly in both civil and criminal actions.[204] Constrained by strict construction, courts would lose the flexibility to shape prohibitions in a manner best suited to combating unscrupulousness in the securities markets.[205] Congress commissioned such flexibility when it worded the Exchange Act's prohibitions broadly.[206] Thus, the applicability of the alternative fair warning rule to the Exchange Act moots the conflict that would otherwise arise between strict construction and Congress's mandate for judicial flexibility.

b. Judicial Disregard

Many lower federal courts define the willfulness requirement in a manner that disregards the alternative fair warning rule.[207] According to these courts, a defendant acts "willfully" when she recklessly engages in the prohibited conduct, regardless of whether she knows that the conduct is wrongful enough to make illegality likely.[208]

C. The Differentiated Intent Rule

The differentiated intent rule applies to hybrid statutes that have a criminal intent requirement and either a less stringent civil intent requirement or no civil intent requirement at all. The rule directs courts to treat the criminal intent requirement in a manner that maintains the civil/criminal distinction it was designed to provide. Thus, they should not dismiss the requirement as boilerplate. Nor should they allow the requirement to become indistinguishable from the less stringent intent requirement (if any) applicable to civil actions.[209]

204. *See supra* note 66 and accompanying text.

205. *See supra* note 192 and accompanying text.

206. *Cf.* Reves v. Ernst & Young, 494 U.S. 56, 63 n.2 (1990) (noting that "[o]ne could question whether, at the expense of the goal of clarity, Congress overvalued the goal of avoiding manipulation by the clever and dishonest" when it drafted the Exchange Act); SEC v. W.J. Howey Co., 328 U.S. 293, 299 (1946) (noting that the term "investment contract" in the Securities Act "embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits").

207. The Supreme Court has mentioned the willfulness requirement but has never defined it. *E.g.*, United States v. O'Hagan, 521 U.S. 642, 665 (1997).

208. *See* 10 LOSS & SELIGMAN, *supra* note 102, at 4760 (collecting cases). *But see* United States v. Dixon, 536 F.2d 1388, 1395 (2d Cir. 1976) (holding that willfulness requires "'a realization on the defendant's part that he was doing a wrongful act'" and "that the act be 'wrongful under the securities laws and that the knowingly wrongful act involve a significant risk of effecting the violation that has occurred,'" quoting United States v. Peltz, 433 F.2d 48, 55 (2d Cir. 1970)).

209. *See supra* notes 92–94 and accompanying text.

1. Applicability to the Exchange Act

While the Exchange Act contains a willfulness requirement for criminal actions,[210] it contains intent requirements for various civil actions as well. Indeed, the express private action in section 9(e) has an intent requirement on its face.[211] Moreover, Commission and implied private actions to enforce the prohibitions in section 10(b) and Rule 10b-5 and section 14(e) have intent requirements as the result of judicial interpretations of those prohibitions.[212] The differentiated intent rule applies only if Congress expected courts to define these civil intent requirements less stringently than the willfulness requirement for criminal actions.

That Congress had such an expectation emerges from the Supreme Court's 1933 decision in *United States v. Murdock*.[213] At issue in *Murdock* was the willfulness requirement for criminal actions under the federal tax laws.[214] That requirement—like the one for criminal actions under the Exchange Act[215]—is set forth in a section applicable to criminal actions only.[216] The defendant argued that to establish willfulness, the government had to show that he acted with an "evil motive."[217] The Court accepted this definition, but only for purposes of a willfulness requirement that was limited to criminal actions:

> The word ["willfulness"] often denotes an act which is intentional, or knowing, or voluntary, as distinguished from accidental. But when used in a criminal statute, it generally means an act done with a bad purpose. . . .
>
> . . . .
>
> Aid in arriving at the meaning of the word "willfully" may be afforded by the context in which it is used . . . .[218]

Acting only months after *Murdock*, the Congress enacting the Exchange Act would have expected courts to construe the willfulness requirement for criminal actions more stringently than the intent requirements for

210. *See supra* note 108 and accompanying text.

211. Section 9(e) provides as follows:

> Any person who *willfully* participates in any act or transaction in violation of subsection (a), (b), or (c) of this section, shall be liable to any person who shall purchase or sell any security at a price which was affected by such act or transaction, and the person so injured may sue in law or in equity in any court of competent jurisdiction to recover the damages sustained as a result of any such act or transaction.

15 U.S.C. § 78i(e) (1994) (emphasis added).

212. For discussion of the intent requirement of § 10(b) and Rule 10b-5, see 8 LOSS & SELIGMAN, *supra* note 102, at 3663–69. For discussion of the intent requirement of § 14(e), see 5 LOSS & SELIGMAN, *supra* note 102, at 2255–56.

213. 290 U.S. 389 (1933).

214. *See id.* at 394.

215. *See supra* note 108 and accompanying text.

216. *See* 26 U.S.C. § 7201 (1994).

217. United States v. Murdock, 290 U.S. 389, 396 (1933).

218. *Id.* at 394–95. *Cf.* 6 LOSS & SELIGMAN, *supra* note 102, at 3037 n.152 (noting that willfulness "may well mean something more in the criminal context" than in the civil context).

civil actions.[219] That expectation brings the differentiated intent rule into play.

2. *Judicial Disregard*

Many lower federal courts violate the differentiated intent rule by employing recklessness to define the willfulness requirement in criminal actions[220] as well as to define the intent requirements in civil actions.[221] In the words of the Third Circuit, "there is no reason to suppose that in enacting criminal statutes prohibiting . . . securities fraud the Congress intended that . . . the scienter . . . should be different than for civil liability for fraud."[222]

To satisfy the differentiated intent rule, courts must give the willfulness requirement for criminal actions a definition more stringent not only than recklessness but also than actual knowledge that the acts committed will cause the proscribed results—the state of mind that Congress requires for private fraud actions involving forward-looking statements.[223] A definition meeting these criteria would be knowledge of wrongfulness sufficient to make illegality likely—a definition that satisfies the alternative fair warning rule as well.[224]

In short, courts construing the Exchange Act frequently disregard the rules that implement the core principle. In so doing, these courts undermine the core principle itself.

V. HARMONIZING CIVIL AND CRIMINAL ENFORCEMENT UNDER THE EXCHANGE ACT

Courts should construe the Exchange Act in accordance with the framework applicable to all hybrid statutes that is described in Part II.

219. *Cf.* Johnson v. Home State Bank, 501 U.S. 78, 85–86 (1991) (making the assumption that Congress understands the contemporaneous legal context in which it acts).

220. *See supra* notes 208 and accompanying text.

221. Most courts define scienter under § 10(b) and Rule 10b-5 as recklessness. *See* 8 LOSS & SELIGMAN, *supra* note 102, at 3665 n.521. Most courts equate § 14(e)'s scienter requirement with that of § 10(b) and Rule 10b-5. *See* 5 LOSS & SELIGMAN, *supra* note 102, at 2256. Courts likewise appear to define the intent requirement in § 9(e) as they do the intent requirements in other civil actions under the Exchange Act. *See* Chemetron Corp. v. Bus. Funds, Inc., 682 F.2d 1149, 1164 & n.39 (5th Cir. 1982), *vacated on other grounds*, 460 U.S. 1007 (1983).

222. United States v. Boyer, 694 F.2d 58, 60 (3d Cir. 1982); *see also* 10 LOSS & SELIGMAN, *supra* note 102, at 4760 (noting without apparent criticism that courts equate the scienter requirement of § 10(b) and the willfulness requirement of § 32(a)). *But cf.* United States v. Chestman, 903 F.2d 75, 88 (2d Cir. 1990) (Carman, J., concurring in part and dissenting in part) (maintaining that criminal liability under § 14(e) and Rule 14e-3 requires proof of scienter as well as willfulness), *vacated*, 947 F.2d 551 (2d Cir. 1991).

223. *See* § 21E(c)(1)(B) of the Exchange Act, § 78u-5(c)(1)(b) (Supp. II 1996).

224. *See supra* text accompanying notes 201–03. The willfulness requirement should retain the same definition where civil enforcement of the prohibition in question does not involve a scienter requirement. *See* Ratzlaf v. United States, 510 U.S. 135, 143 (1994) (holding that the willfulness requirement of the Currency and Foreign Transactions Reporting Act must have the same construction for all prohibitions).

This Part briefly recapitulates the framework as it applies to the Exchange Act and then illustrates the framework's operation.

The framework is bottomed on the core principle of one interpretation per prohibition.[225] To arrive at that one interpretation, courts should consider all actions to enforce the prohibition under the hybrid statute and the policies pertinent to each. If the policies conflict, the most appropriate compromise should be sought.[226] Concerns about fair warning should be addressed through enforcement of the Exchange Act's willfulness requirement for criminal actions, with willfulness defined as knowledge of wrongfulness sufficient to make illegality likely.[227] Because defendants who act with such knowledge cannot claim surprise at being prosecuted, there is no need to construe ambiguous prohibitions strictly.[228]

Consider again the case of George, who convinced his friend Mary that Sweets, Inc., was a highly profitable company.[229] Mary entrusted money to George for the purchase of Sweets stock, but George appropriated the money for his own use. Later, Mary discovered that there was no such company as Sweets. Section 10(b) and Rule 10b-5 prohibit fraud "in connection with the purchase or sale of a security,"[230] but say nothing about whether transactions involving nonexistent securities are covered.[231] Do these prohibitions encompass George's transaction with Mary?

Liberated from the constraint of strict construction, the court hearing a criminal, Commission, or private action against George can focus on the statutory policy of "protect[ing] investors against false and deceptive practices."[232] As one district court recently observed, that policy would be undermined if section 10(b) and Rule 10b-5 were read to exclude transactions involving nonexistent securities:

> Making substantial misrepresentations as to the value of a worthless but technically extant security is a paradigmatic form of securities fraud. Extending the protection of the securities laws to the victims of schemes so fraudulent that the underlying paper does not exist logically follows, as fraudsters would have a perverse incentive to magnify their deceptive conduct.[233]

To be sure, a court hearing the action against George would also have to consider the policy of curbing vexatious private litigation under

225. *See supra* Part II.A.
226. *See supra* Part II.B.1.
227. *See supra* Part IV.B.2.a.
228. *See supra* note 82 and accompanying text.
229. The introduction to this article used this example to illustrate why some courts allow prohibitions to mean different things in different enforcement contexts. *See supra* text accompanying notes 11–15.
230. For the text of § 10(b) and Rule 10b-5, see *supra* note 12.
231. *See supra* note 14 and accompanying text.
232. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 198 (1976).
233. SEC v. Bremont, 954 F. Supp. 726, 732 (S.D.N.Y. 1997).

section 10(b) and Rule 10b-5.[234] But that policy does not seem to be relevant here. The threat of vexatious private litigation arises from "a plaintiff's capacity to manufacture claims of hypothetical action, unconstrained by independent evidence."[235] When Mary alleges that George sold her stock in a nonexistent company, she does not offer evidence that only she controls. If George wishes to assert the company's existence, he has equal access to the relevant evidence and is well positioned to respond.

An additional comment is appropriate concerning the willfulness requirement, which comes into play if George is a defendant in a criminal action.[236] That requirement calls for proof that George knew his conduct was wrongful enough to make illegality under the Exchange Act likely.[237] Because the scienter requirement for Rule 10b-5 civil actions is less demanding,[238] enforcement of the willfulness requirement increases the prospect that George will be convicted only if his offense is egregious.[239]

By applying the framework to the Exchange Act, then, courts can avoid strict construction, focus on policy considerations, and maintain a civil/criminal distinction. Because some courts construing the Exchange Act do none of these things,[240] their adoption of the framework would constitute a significant step forward.

VI. CONCLUSION

During the last hundred years, there has been a radical shift in the roles of courts and legislatures. As Dean (now Judge) Calabresi put it in his landmark book, *A Common Law for the Age of Statutes*,[241] "we have gone from a legal system dominated by the common law, divined by courts, to one in which statutes enacted by legislatures have become the

234. For a discussion of this policy, see *supra* notes 159–64 and accompanying text.

235. Va. Bankshares, Inc. v. Sandberg, 501 U.S. 1083, 1092 (1991). In *Virginia Bankshares*, the plaintiffs brought a Rule 14a-9 action to challenge the reasons given by directors for supporting a merger. The defendants argued that litigation of "reasons" presented the threat of vexatious private litigation. *Id.* at 1091. The Court rejected this argument on the ground that the evidence relevant to the litigation of reasons was "subject neither to a plaintiff's control nor ready manufacture." *Id.* at 1094.

236. The willfulness requirement is set forth in § 32(a) of the Exchange Act, the text of which appears *supra* note 108.

237. *See supra* notes 197–203 and accompanying text.

238. *See supra* note 221 and accompanying text.

239. *See supra* note 90 and accompanying text.

240. For decisions applying strict construction to the Exchange Act and thereby losing the opportunity to focus on policy considerations, see *supra* note 192 and accompanying text. For decisions equating the willfulness requirement for criminal actions with civil intent requirements and thereby preventing the establishment of a civil/criminal distinction, see *supra* notes 220–22 and accompanying text.

241. GUIDO CALABRESI, A COMMON LAW FOR THE AGE OF STATUTES (1982).

primary source of law."[242] Calabresi might have added that this is not only the age of statutes but also the age of hybrid statutes—statutes whose prohibitions are enforceable in criminal actions as well as in private or governmental civil actions.[243] Indeed, numerous federal regulatory statutes are of this type.[244]

While courts struggle with how to construe hybrid statutes, they have yet to recognize them as a jurisprudential problem cutting across subject matter lines. This article calls attention to the problem and provides a solution—an analytic framework for the construction of all hybrid statutes, irrespective of their substantive content.

242. *Id.* at 1 (footnote omitted). Calabresi explains this shift as follows: "[C]ourts are not capable of writing speedily enough most of the rules that a modern society apparently needs." *Id.* at 163.

243. *See supra* notes 1–2 and accompanying text.

244. *See supra* notes 3–9 and accompanying text.