

Securities and Exchange Commission Historical Society
Oral History Project
Interview with Richard Posner
Conducted on January 25, 2011, by Kenneth Durr

KD: Interview with Judge Richard Posner, January 25th, 2011, in Chicago, Illinois, by Kenneth Durr. Let's go back to the early years a bit. I want to talk about the state of corporate law when you were at Harvard. Did you think that you would go into areas of corporate law, antitrust, when you were at Harvard?

RP: No. I took corporation law, of course. It was from Derek Bok, who later became dean of the law school and president of Harvard. It was a good course; he's a good teacher. I don't remember anything about the course. I took Louie Loss's securities regulation course, which I also don't remember.

KD: He later became legendary in the field of securities laws, writing the book on it.

RP: I think he was already; this would've been about 1960. I think he'd written his treatise. I took an antitrust course from Philip Areeda. I didn't particularly like it at that time. Obviously, I later became interested in antitrust; but, no, I wouldn't say the corporate area particularly excited me in law school.

KD: What did excite you in law school?

RP: I actually liked the common law courses, the first-year courses in law school, best.

KD: How did you land the job clerking for Justice Brennan?

RP: He had delegated the appointment of his law clerk to Professor Paul Freund. So Freund appointed me and another fellow. That was it.

KD: Was this something that you get to register an interest in doing?

RP: No.

KD: Or do you just hear that you're it?

RP: No, I never applied for anything. He just picked. That was a very common way of appointing law clerks in those days.

KD: Tell me a little bit about working for Justice Brennan; what kind of a guy was he?

RP: He was a very nice person, a very good boss. He wasn't very interested in the details of legal analysis, so we law clerks wrote the opinions and he would go over them. I don't recall substantial editing. I was told that in later years, if he was dissatisfied with a law clerk's draft, he would write it himself. He had been a state Supreme Court justice before he came to the Supreme Court, so he knew how to write opinions. But if he liked the law

clerks, he left it pretty much to them.

KD: Who were your colleagues, clerking for Brennan?

RP: My fellow law clerk was a fellow named Bob O'Neill, who later became president of Wisconsin University and Virginia University, and now has a position in the law school in Virginia. There was just two clerks.

KD: That was a pretty pivotal time, mid-sixties; the Warren Court was in full flower.

RP: No, this was the 1962 term. It was really the beginning of the full flowering of the Warren Court, because it was the year in which Goldberg replaced Frankfurter. It was a decisive shift.

KD: Why?

RP: Well, now there was a very solid majority for typical Warren Court liberal decisions: Warren, Black, Douglas, Goldberg, and Brennan. So they had five right there. The others were Harlan, Stewart and Clark, they were more conservative. The ninth—I know White came along pretty quickly—but I've forgotten, might have been Reed. But when Goldberg replaced Frankfurter, the Court had a solid five liberals.

KD: What were some notable cases that you were able to assist on in that period?

RP: Well, one of them was *Fay v. Noia*, which was a big habeas corpus case, later overruled. There was *Sanders v. United States*, which was a case under § 2255, the habeas corpus substitute for federal prisoners. That was an important case in its time.

There was another important habeas corpus case that I wrote, *Townsend v. Sain*, which I think came out as a per curiam. Warren had assigned it to himself, but he asked Brennan to help him and Brennan asked me.

There was another important case, *NAACP v. Button*, about the use of litigation as a form of first amendment expression. That was one I did for Brennan. But the one that was most significant for my career was *United States v. Philadelphia National Bank*. That was a big antitrust case. That quickened my interest in antitrust. I don't remember the other cases I worked on.

KD: That was about the time the *Silver* case went through, having to do with the New York Stock Exchange. That was also antitrust.

RP: I don't remember that.

KD: You talked about *U.S. v. Philadelphia National Bank* quickening your interest. What made that different from some of the other antitrust cases?

RP: Well, there weren't a lot of antitrust cases then. The previous year, the Supreme Court had decided an antitrust case, *Brown Shoe*. These were both cases under Section 7 of the Clayton Act. Section 7 had been amended in 1952 to strengthen its application to mergers. The *Brown Shoe* opinion had been very murky and meandering. The law clerk who worked on it for Warren, I don't think he had any clue about antitrust.

Philadelphia Bank was another Section 7 case. But in law school, as a junior editor on the *Harvard Law Review*, I had been assigned to do a cite check a portion of a very good article by Derek Bok called "Section 7 and the Merging of Law and Economics," in which he had argued for a simplified approach to Section 7 cases. I remembered that when I started working on *Philadelphia Bank*.

So I incorporated the idea of a simple prima facie case. I got that from Bok's article. Just working on it, I thought this was interesting. I hadn't liked Phil Areeda's course on antitrust. I think it may have been the first time Areeda taught it. He later became a very, very successful teacher, but his antitrust course was not, but working on the bank case, as I say, quickened my interest in antitrust.

KD: And it sounds like you were starting to see some of the emerging concerns that came out of law and economics as you developed it.

RP: Well, clearly there were economic issues. Yes, I could see that although I didn't know any economics.

KD: The other thing about your early experience that stands out is your time in the solicitor general's office.

RP: Yes, although I spent two years in the Federal Trade Commission in between the Supreme Court and the SG's office, and that was when I really got interested in antitrust, because that was a big part of the FTC's jurisdiction.

KD: Did you argue any cases in that capacity?

RP: In the FTC?

KD: No, going into the solicitor general's.

RP: Yes, I argued two major antitrust cases. One was *Von's Grocery*, which was a merger case. And the other was the *Schwinn* case, which dealt with restricted distribution.

KD: What was it like working for Thurgood Marshall?

RP: We liked it. The people in the office liked it, because he just backed the staff, it didn't matter what. Because he was a national figure, the attorney general was hesitant to cross him. So we liked that. But he had no interest in the job. He was just marking time. It was just one of the jobs he had to do to become appointed to the Supreme Court, but he

had no interest in it.

So the office was run by three senior lawyers who would now be called deputy solicitors general. They were then called the first, second, and third assistant to the solicitor general. The rest of us were just plain assistants to the solicitor general. The three were very good, and they ran the office, so everything was fine.

KD: Did any securities cases come through during your period with the solicitor general?

RP: Probably, but I don't remember.

KD: Now, after your time there, you were tasked with, I think it was general counsel for a study on the FTC.

RP: It was a task force on telecommunications policy.

KD: You didn't look specifically at the FTC?

RP: No, the FTC had nothing to do with telecommunications.

KD: There was a certain antitrust component looking at AT&T, right?

RP: Yes, there was concern about the AT&T monopoly and its refusal to connect to potential

competitors. AT&T refused to allow attaching any equipment to the telephone network that hadn't been produced by Western Electric. So we were dealing with problems of monopoly and competition, but not with antitrust law as such.

KD: You'd gotten a close look at the independent agency and administrative law with the FTC?

RP: Yes.

KD: What was your take on it, what was your opinion? Was it working at that point? I'm interested in the analog to the Securities and Exchange Commission in the same period.

RP: Well, the FTC was a backwater. It had been intended to be an important component of the progressive movement; the Federal Trade Commission Act was passed at the same time as the Clayton Act. But over the years the FTC had dwindled and became a real backwater. But the commissioner I worked for, Philip Elman, who had been in the solicitor general's office and clerked for Frankfurter, was a very smart lawyer. He was terrific and shook up the Commission a lot.

I was the major author of the Federal Trade Commission's report on cigarette advertising and labeling, in which the Commission adopted a rule requiring disclosure of the hazards of smoking in advertising and labeling. The rule was quickly preempted by Congress, which confined the disclosure requirements to labels. That was a big thing for the

Federal Trade Commission to do in 1964. It was the major consumer protection achievement of the two years I was there. I also wrote antitrust opinions for Elman. He was very different from Brennan. He did a lot of rewriting. He was very engaged in the production of the opinions. He was very smart.

KD: One of the questions here, and you might be in a position to talk about it, is how the judicial system, especially the Supreme Court, deals with administrative law. You're looking at the FTC and the case law that would be shaped by that. Can you talk a little bit about what the general approach was during the 1960s and going into the seventies as far as the Supreme Court and administrative law cases, generally?

RP: No, I don't really remember that. I imagine the Supreme Court was pretty tolerant of administrative action. I don't recall big fights. Of course, there was the famous opinion, *Vermont Yankee*, where the Supreme Court slapped down the D.C. Circuit for imposing restrictions on administrative procedure that went beyond the Administrative Procedure Act. The administrative agencies had, up until the deregulation movement in the late seventies, a lot of prestige from the Progressive Era and the New Deal. I think they were treated well by the courts.

KD: The Chicago School, in general, had a lot to do with that deregulation that you talk about. At the same time after this period, you're becoming involved with the shaping of the law and economics movement. Now, it's pretty clear that antitrust is something that's pretty central to that. Is corporate and securities law central, as well?

RP: Well, it wasn't a focus of mine. There were significant questions about the need for and efficacy of the 1933 Act. George Stigler, a famous economist in Chicago, wrote a very critical empirical paper about the effect of the 1933 Act on new issues, trying to compare price movements of new issues after '33 and before. It was a controversial article. It was a strong attack on the SEC.

Bill Baxter, a lawyer at Stanford who was very knowledgeable about economics, wrote a very critical article about the stock brokers' cartel. So as part of the deregulation movement, there was indeed criticism of the SEC. But I don't recall that there was antitrust litigation, or that the courts were important in the change in the policies in the SEC.

KD: This is the idea that the SEC was somehow a captive agency?

RP: Of the brokers, yes. Then you also get in the late sixties-seventies, the rise of modern finance theory and the notion that the securities markets are efficient markets and don't require much regulation, and that conventional views about stock picking and timing market turns were erroneous. So that was an attack on conventional, not just regulation, but conventional conceptions of the securities markets.

KD: Is this Henry Manne?

RP: Manne's was a specific challenge to prohibiting insider trading. That challenge never went anywhere, but was typical of hostility to regulation, which is a big factor, obviously, in deregulation.

KD: Why don't you think it ever went anywhere?

RP: I don't think it ever made much sense. Obviously people don't like to trade against insiders, right? They're at a terrible disadvantage. I don't know why he pushed so hard on it. I don't think it convinced many people.

KD: I want to talk a little bit about some of the topics, starting with insider trading, some of the key issues in securities law as you experienced them on the Seventh Circuit. And one of the ones where you can see a lot of changes in insider trading from 1980 with *Chiarella* and moving through the nineties. The SEC's position and the way the courts are coming down, it seems to me, are changing fundamentally.

RP: Really? What is the fundamental change?

KD: Well, you're looking at different rationales, certainly, from the SEC's point of view, and the development of you're going from what had been dominant in the 1960s with *Texas Gulf Sulphur*, and moving to *O'Hagan* where a misappropriation becomes dominant. Do you see any fundamental changes in the way insider trading law was interpreted by judges or argued by the SEC?

RP: I probably don't know enough about it to answer your question.

KD: Certainly you must have been involved in some insider trading cases on the Seventh Circuit.

RP: I can't remember any. What's the change?

KD: I think it's interesting that the SEC was making different arguments at different times, looking for ways to justify prosecuting insider trading.

RP: Why? I don't understand. The objection to insider trading is that insiders have an advantage against the rest of the world that makes other people leery about investing in the stock market, for, if they do, they're competing against people who have that advantage. There's also the concern that insider trading allows losers to make a lot of money; they can trade as their stock is declining or they can sell their own stock. Is there anything else to the objections to insider trading?

KD: I'm not the expert. You've been an appellate judge and I would assume that that one would have come across the bench.

RP: No, I can't remember having an insider trading case.

KD: How about corporate takeover statutes? In the 1980s, that was a pretty big deal.

RP: The poison pills and so on, yes.

KD: And the *Mite* case, it was *Edgar v. Mite*, I think, in the Supreme Court. Were you involved with that one?

RP: No. That did come out of this circuit, but no. I had a case that was reversed by the Supreme Court. Actually, I don't know if they reversed my case or another case, but it was the sale of business doctrine. The notion was that if you sell an entire business, you don't have to make the ordinary disclosure. Anyway, I was on one side of that, Supreme Court took the other side. That's back in the eighties, so it's fuzzy in my mind. I think we had some poison pill cases, but the main ones were in Delaware and so I don't know a lot about them.

KD: It was CTS, does that ring a bell?

RP: Vaguely.

KD: I think that was the Seventh Circuit as well. During your time in the Seventh Circuit, are there any securities cases that stand out as being significant or important to you?

RP: I have written a number of opinions in securities cases, and the other judge who had

many is Judge Easterbrook. You really ought to talk to him. That's one of his academic fields, securities law. I wrote a case called *Bastian*, which was about separating out accidental consequences of investing at one time rather than another from the consequences that are due to the actual misrepresentation. Loss causation versus transaction causation. That was one. I wrote an opinion, called "Scattered," about whether you can sell short more stock than the company owns. We said yes. That was fun.

KD: Why did you say yes?

RP: There was nothing to prohibit it. It's just a form of speculation. Recently, I wrote the opinion on remand of the *Tellabs* case. That had come from the Circuit. I wasn't on the original panel, but when it came back from the Supreme Court, I was on the (new) panel and I wrote an opinion trying to make sense of the Supreme Court's new standard. I've written other securities law opinions, but I don't have a clear recollection.

KD: What was the issue at hand in the *Tellabs* case?

RP: Let me see if I can reconstruct that. It's vague in my mind. It had to do with how much the senior officers had to know in order for the complaint to survive dismissal. We said there was enough and that was, I think, the end of the case. I don't remember the details at all, although it's not that long ago.

KD: Did this have to do with secondary participants and the ability to aiders and abettors, that kind of thing?

RP: No. I think the aiders and abettors had been eliminated. You could look up on Westlaw my opinion on securities using the word “securities.”

KD: Is it your experience that judges pay particularly close attention to what the Supreme Court’s attitude might be toward their decisions when they’re making them?

RP: Some do. I don’t. Some of the court of appeals judges follow the Supreme Court closely, read all decisions and try to figure out what’s next on their agenda. Most judges don’t bother with that. They just take what the Supreme Court has said without worrying about how the Court might change. Obviously, this Supreme Court is very pro-business, but it hasn’t done a lot yet. I wrote a dissent in a case the Supreme Court took and reversed, *Jones v. Harris*, involving mutual fund fees. That’s within the SEC’s domain.

KD: Well, the law and economics movement, one of the fundamentals, at least as I understand it, is to look at outcomes. Is that a correct statement?

RP: Yes.

KD: To evaluate outcomes? In the case of securities law, what would those outcomes be and how does one evaluate them?

RP: Well, you want to create a competitive market in securities. As in any other competitive market, you want to minimize transaction costs and you want to prevent fraud. Ideally, you'd like people to make the choice between buying equities and bonds or other forms of security, just on the basis of risk and expected return and transaction costs. You want a system of regulation or nonregulation that minimizes transaction costs and promotes information and so on.

KD: Are there examples of cases where you have taken such considerations into account?

RP: I'm sure that's a concern whenever I have a securities case, but I can't recite chapter and verse.

KD: In your experience—and you started earlier in your career, you were involved with an administrative agency and you've had a chance to think about such things—is the administrative agency still viable? Is something like the SEC still a viable, efficient way to administer markets?

RP: Well, I don't know much about the SEC. Of course, it took a terrific hit in the 2000s with the Madoff business and the incompetent management of the agency by Christopher Cox, which contributed to the economic crisis. Now it has a much better chairman and it's got more funding, so I'm sure it's rebuilding and improving. I don't know whether it'll be successful. It wants to regulate hedge funds; it's not clear that that's worth doing.

The greatest failure of the SEC in this past decade was its total oblivion to the transformation of the banking industry whereby the big broker dealers had really become banks. All the SEC was worrying about was consumer protection, doing it ineptly. It had no sense of the macroeconomic significance of companies like Goldman and Morgan and Lehman Brothers.

You still have this very divided regulation. Even though Goldman Sachs and Morgan Stanley are now bank holding companies, and Merrill Lynch is owned by a bank and so on, nevertheless, the non-banking activities, which include a great deal of banking by another name, of these companies are still regulated by the SEC. The SEC has had to create a new division to try to be a real banking regulatory agency. I don't know what success they've had.

The SEC has always had a good reputation, partly because, unlike the FTC, it offered a good career path for lawyers. They could work for the SEC for a few years and then go into practice. Whereas for the FTC lawyers, practice opportunities weren't very good. I think the SEC has always been a pretty high class agency in terms of personnel, although obviously it fell down very badly with Madoff. I'd say, you know, good agency.

KD: How important has the difference between state regulation and federal regulation been?

RP: I don't know anything about state regulation. Like blue sky laws?

KD: Yes, every state has its own. That's not something that courts would end up—

RP: Not the federal courts, no.

KD: Anything else in your career that might be relevant to the development of securities law that we should talk about?

RP: Well, I do think there are a lot of abuses. In *Jones v. Harris*, the different fees charged by the investment advisor for captive mutual funds and independent mutual funds did seem pretty abusive. I don't know whether the SEC is actively dealing with that. I know there are complaints that compliance with SEC regulations is very cumbersome, but I haven't studied that. Do the prospectuses for new issues have any real function, or are they just boilerplate? Does anybody pay any attention to them?

One thing that's happened is that the efficient markets theory has taken a hit in this economic crisis. There have been two big stock bubbles and a housing bubble in recent years. So clearly a lot of trading is not based on estimates of corporate earnings. They're based on what people think other people think. I don't know whether the SEC can deal with bubbles, but their existence underscores the need for regulation, since the bubble phenomenon is apparently not self-correcting. The market doesn't prevent bubbles, so maybe that calls for government regulation.

KD: All right, if there's nothing else then thank you very much for your time.

[End of Interview]