FEDERAL APPELLATE PROCEDURE—STATUTORY AUTHORIZATION FOR AWARDING OF ATTORNEYS' FEES APPLIED RETROACTIVELY TO SERVICES RENDERED PRIOR TO ITS ENACTMENT, DESPITE AN ABSENCE OF LANGUAGE OR LEGISLATIVE HISTORY INDICATING IT WAS TO BE APPLIED TO PENDING CASES.—*Bradley v. School Board* (U.S. Sup. Ct. 1974).

Plaintiff-petitioners were parties to a class action suit brought under the Civil Rights Act of 1971[1] to desegregate the Richmond, Virginia, public schools. In the course of litigation, the district court awarded petitioners expenses and attorneys' fees for services rendered during a specified ten month period.[2] The court's allowance of fees and expenses was made without reliance on any explicit statutory authorization for the making of such an award, but rather was based on grounds rooted in its general equity power. The court of appeals reversed the award,[3] despite the enactment prior to the rendering of its decision of the Emergency School Aid Act, which grants authority to a federal court to award a reasonable attorneys' fee when appropriate in school desegregation cases.[4] On appeal to the United States Supreme Court, *held*, reversed, all justices who participated concurring, the district court may in its discretion allow petitioners a reasonable attorneys' fee, as the provision authorizing such an award applies retroactively to fees and expenses incurred prior to the date that provision came into effect. *Bradley v. School Board*, 416 U.S. 696 (1974).

Though frequently stated since its original enunciation nearly one-hundred seventy-five years ago in the case of *United States v. Schooner Peggy*,[5] the principle that a reviewing court is to apply the law in effect at the time it renders its decision has not always met with consistent application in the course of its development. Aware of this, the Supreme Court in *Bradley v. School Board*[6] devoted its time to a review of the legal precedents leading to its decision to retroactively apply section 718 of the Emergency School Aid Act, as well as to an enumeration of those general factors to be considered by courts in their future applications of changes in law to cases then pending before them on direct appeal.[7]

As already noted, the origin of the rule that a court is to apply the law in

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1. 42 U.S.C. § 1983 (1970).
2. Bradley v. School Bd., 53 F.R.D. 28, 43-44 (E.D. Va. 1971).
3. Bradley v. School Bd., 472 F.2d 318 (4th Cir. 1972).
4. 20 U.S.C. § 1617 (Supp. II, 1972):
   Upon the entry of a final order by a court of the United States against a local educational agency, a State (or any agency thereof), or the United States (or any agency thereof), for failure to comply with any provision of this chapter or for discrimination on the basis of race, color, or national origin in violation of title VI of the Civil Rights Act of 1964, or the fourteenth amendment of the Constitution of the United States as they pertain to elementary and secondary education, the court, in its discretion, upon a finding that the proceedings were necessary to bring about compliance, may allow the prevailing party, other than the United States, a reasonable attorney's fee as part of the costs.
5. 5 U.S. (1 Cranch) 103 (1801).
6. 416 U.S. 696 (1974).
7. The effect of a subsequent ruling of invalidity on a prior final judgment under collateral attack was not discussed by the Court in *Bradley v. School Board*, and is beyond the scope of this casenote. *But see* Linkletter v. Walker, 381 U.S. 618 (1965).

effect at the time it renders its decision is found in *United States v. Schooner Peggy*,[8] a case involving condemnation proceedings brought against the French vessel, Peggy, which was seized pursuant to an act of Congress.[9] The trial court found against the United States and held the Peggy not to be a lawful prize. The circuit court reversed the trial court's findings and imposed the sentence and condemnation decree. Subsequent to this, while the case was pending appeal to the Supreme Court, a convention was signed in Paris between the United States and French plenipotentiaries providing in part that "[p]roperty captured, and not yet definitively condemned. . . shall be mutually restored . . . ."[10] In reversing the circuit court's decision, the Supreme Court applied the terms of the convention and established the foundation for the change of law doctrine by stating:

> It is in the general true that the province of an appellate court is only to inquire whether a judgment when rendered was erroneous or not. But if, subsequent to the judgment, and before the decision of the appellate court, a law intervenes and positively changes the rule which governs, the law must be obeyed, or its obligation denied. If the law be constitutional . . . I know of no court which can contest its obligation. It is true that in mere private cases between individuals, a court will and ought to struggle hard against a construction which will, by retrospective operation, affect the rights of parties, but in great national concerns . . . the court must decide according to existing laws, and if necessary to set aside a judgment, rightful when rendered, but which cannot be affirmed but in violation of law, the judgment must be set aside.[11]

While seemingly a definitive statement, this language has left open to discussion at least three areas of uncertainty: (1) what constitutes the "intervening law" to be given cognizance by a federal reviewing court, (2) when is the application of this "intervening law" called for, and conversely (3) when is the application of this "intervening law" to be specifically avoided? The development of each of these areas will be discussed in turn.

Though the Court in *Schooner Peggy* stated that "if . . . a law intervenes and positively changes the rule which governs, the law must be obeyed . . . ,"[12] the Court failed to delineate what it meant by "intervening law." However, when considered both theoretically and historically, the term has admitted of many applications, including treaty,[13] constitutional amendment,[14] a change in

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8. 5 U.S. (1 Cranch) 103 (1801).
9. Act of July 9, 1798, ch. 68, § 1, 1 Stat. 578.
10. Treaty with France on Peace, Commerce, and Navigation, Sept. 30, 1800, art. IV, para. 1, 8 Stat. 178.
11. United States v. Schooner Peggy, 5 U.S. (1 Cranch) 103, 109 (1801).
12. *Id.*
13. *E.g.*, United States v. Schooner Peggy, 5 U.S. (1 Cranch) 103 (1801) (convention between the United States and France applied to set aside a condemnation decree entered prior to the signing of the bilateral agreement).
14. *E.g.*, United States v. Chambers, 291 U.S. 217 (1934) (ratification of the twenty-first amendment to the Constitution applied so as to discontinue pending prosecutions under the National Prohibition Act, the act having been rendered inoperative by the amendment).

federal statutory law,[15] a ruling by an administrative agency,[16] and a change in state law brought about by statutory revision[17] or state court decision.[18] Yet it is uniquely the province of only those cases falling within the last category—that is, cases affected by changes in law brought about by state court decision—to have caused courts any major problems simply by virtue of their nature.

The problems arose due to the construction given the words "the laws of the several states"[19] by the Supreme Court ruling in *Swift v. Tyson*,[20] whereby federal courts were not bound in all instances to state court determinations of state law. As applied to the change in law doctrine, this meant that a federal appellate court need not reverse a federal trial court decision so as to conform to a subsequent pronouncement of state law.[21] As a result, the change in law doctrine as it related to the application of a change in state law brought about by state court decision underwent a period of great complexity and confusion. Some reviewing courts bound themselves strictly to the *Schooner Peggy* principle, applying the law in effect at the time of review. Other courts, however, envisioned their task to be only the correction of reversible error made at the time of trial, and declined to apply the changed law.[22]

This inconsistent state of the law continued without hope of resolution until the Supreme Court rendered its historic decision in the case of *Erie Railroad Co. v. Tompkins*,[23] binding federal courts to the adjudications of state courts in all matters of general jurisprudence in cases in which their jurisdiction is based solely on diversity of citizenship. While it was not reached in *Erie* as to what point in the cause the state law would be finally determined, the stage was set for the Court's later decision on this issue in *Vandenbark v. Owens-Illinois Glass Co.*[24] In *Vandenbark*, plaintiff brought an action against the defendant in the federal district court of Ohio under its diversity jurisdiction, alleging negligence that resulted in her contraction of various occupational diseases,

15. *E.g.*, United States v. Alabama, 362 U.S. 602 (1960) (amendment to Civil Rights Act of 1957); Ziffrin, Inc. v. United States, 318 U.S. 73 (1943) (amendment to Interstate Commerce Act); Carpenter v. Wabash Ry., 309 U.S. 23 (1940) (amendment to Bankruptcy Act).

16. *E.g.*, Thorpe v. Housing Authority, 393 U.S. 268 (1969) (Department of Housing and Urban Development circular prescribing new eviction procedures for federally assisted projects applied to reverse a pending state court eviction order rendered prior to the issuance of those procedures).

17. *E.g.*, Diffenderfer v. Central Baptist Church, Inc., 404 U.S. 412 (1972) (change in state law pertaining to tax-exempt status of church property renders relief sought inappropriate); Hall v. Beals, 396 U.S. 45 (1969) (change in state's voter residency law moots proceedings).

18. *E.g.*, Vandenbark v. Owens-Illinois Glass Co., 311 U.S. 538 (1941) (Ohio supreme court decision authorizing previously unrecognized cause of action applied to reverse prior dismissal of plaintiff's complaint).

19. Federal Judiciary Act of Sept. 24, 1789, ch. 20, § 34, 1 Stat. 92.

20. 41 U.S. (16 Pet.) 1 (1842).

21. *E.g.*, Concordia Ins. Co. v. School Dist., 282 U.S. 545 (1931); Burgess v. Seligman, 107 U.S. 20 (1882); Pease v. Peck, 59 U.S. (18 How.) 595 (1856).

22. *Compare* Annot., 97 A.L.R. 515 (1935), *with* Annot., 101 A.L.R. 776 (1936), *and* Annot., 111 A.L.R. 1317 (1937).

23. 304 U.S. 64 (1938).

24. 311 U.S. 538 (1941).

including silicosis. At the time of trial, however, neither Ohio statutory law nor common law recognized an action stemming from the contraction of that disease, and the action was dismissed. Subsequent to the dismissal and while the case was pending on appeal, the Supreme Court of Ohio expressly overruled its prior holdings and opened the door to recovery for such an injury. The court of appeals nonetheless affirmed the district court's dismissal,[25] holding that the law declared applicable at the time the trial court's judgment was rendered was controlling. In reversing the lower courts, the Supreme Court held that the application of *Erie Railroad Co. v. Tompkins*[26] to the principle first enunciated in *United States v. Schooner Peggy*[27] bound the appellate court to apply the law of Ohio as declared by its highest court at the time it rendered its decision.[28]

Subsequent cases only served to reassert and strengthen the *Vandenbark* position,[29] so that at present this onetime problem area stands as a firmly entrenched development in the area of federal appellate procedure. As one commentator concludes:

> Unlike the situation under Swift v. Tyson, where the federal court was free to disregard even state court decisions construing state statutes if the decisions came down after a lower federal court had decided the case, under the Erie rule it is never too late to change in conformity to some new pronouncement of state law, and a court of appeals must rely on the latest state decisions even though they come after the federal court decision that the appellate court is reviewing.[30]

The second question implicitly raised, yet left unresolved by *United States v. Schooner Peggy*,[31] was whether a change in law should affect a case pending on appeal only where the changed law expressly provides for its application to then pending cases,[32] or whether the changed law is automatically to be given effect unless there is clear indication that it is not to apply.[33] Stated another way, what of the situation where the change in law makes no express provision for—and, if statutory, its legislative history is inconclusive as to—application to then pending appeals? The Supreme Court was forced to admit that its

25. Vandenbark v. Owens-Illinois Glass Co., 110 F.2d 310 (6th Cir. 1940).
26. 304 U.S. 64 (1938).
27. 5 U.S. (1 Cranch) 103 (1801).
28. Vandenbark v. Owens-Illinois Glass Co., 311 U.S. 538, 540-41 (1941).
29. *E.g.*, Nolan v. Transocean Air Lines, 365 U.S. 293 (1961); Huddleston v. Dwyer, 322 U.S. 232 (1944).
30. C. WRIGHT, HANDBOOK OF THE LAW OF FEDERAL COURTS 238 (2d ed. 1970). *See also* Annot., 151 A.L.R. 987 (1944).
31. 5 U.S. (1 Cranch) 103 (1801).
32. *E.g.*, Carpenter v. Wabash Ry., 309 U.S. 23 (1940) (amendment to the Bankruptcy Act applied retroactively where amendment expressly provided it was to apply to "any claims now or hereafter pending in any court of the United States. . . ." Subsection (n) of § 77 of the Bankruptcy Act as amended by Act of Congress of Aug. 11, 1939, 53 Stat. 1406).
33. *E.g.*, Ziffrin, Inc. v. United States, 318 U.S. 73 (1943) (amendment to the Interstate Commerce Act held applicable despite an absence of any express provision that it was to apply to pending cases, the Court stating that "[a] change in law between a nisi prius and an appellate court decision requires the appellate court to apply the changed law." *Id.* at 78).

decisions "did little to clarify this issue"[34] until the more recent case of *Thorpe v. Housing Authority*.[35]

In *Thorpe*, petitioner refused to vacate her premises after respondent housing authority gave notice that her lease was being cancelled at the end of the month. After the Supreme Court of North Carolina affirmed a lower state court's eviction order,[36] the United States Supreme Court granted certiorari to consider petitioner's allegations that she had been denied due process by the summary eviction.[37] While the case was pending before the Supreme Court, the Department of Housing and Urban Development (HUD) issued a circular prescribing new eviction procedures for federally assisted projects.[38] The Supreme Court remanded the case to the state court for disposition in light of the new directive,[39] but again granted certiorari[40] when the state supreme court adhered to its former decision.[41] Respondent housing authority argued that since the HUD circular made no mention of its applicability to then pending cases, its sanctions could not apply to eviction proceedings commenced prior to the date the circular was issued. The Court unanimously rejected this argument, and in reliance upon the language used in *United States v. Schooner Peggy*[42] and subsequent cases, reiterated the principle that the law to be applied is that law prevailing at the time of disposition of the case on appeal. The *Thorpe* Court went on to state that such principle must apply "with equal force where the change is made by an administrative agency acting pursuant to legislative authorization."[43]

Since the HUD circular made no mention of its applicability to then pending cases, the *Thorpe* decision has been construed as standing for the proposition that "even where the intervening law does not explicitly recite that it is to be applied to pending cases, it is to be given recognition and effect."[44]

In *Bradley v. School Board*[45] the Supreme Court again stated that the law prevailing at the time of disposition on appeal is the law to be applied. In so holding the Court rejected the argument that since section 718 of the Emergency School Aid Act allowing for attorneys' fees did not by its terms or by its legislative history[46] clearly indicate that it was to be applied to then pend-

34. Bradley v. School Bd., 416 U.S. 696, 713 (1974).
35. 393 U.S. 268 (1969).
36. Housing Authority v. Thorpe, 267 N.C. 431, 148 S.E.2d 290 (1966).
37. Thorpe v. Housing Authority, 385 U.S. 967 (1966).
38. The circular provided in substance that a tenant be notified of the reasons for his or her eviction and be afforded an opportunity to contest the charges. *See* Thorpe v. Housing Authority, 393 U.S. 268, 272 & n.8 (1969).
39. Thorpe v. Housing Authority, 386 U.S. 670 (1967).
40. Thorpe v. Housing Authority, 390 U.S. 942 (1968).
41. Housing Authority v. Thorpe, 271 N.C. 468, 157 S.E.2d 147 (1967).
42. 5 U.S. (1 Cranch) 103 (1801).
43. Thorpe v. Housing Authority, 393 U.S. 268, 282 (1969).
44. Bradley v. School Bd., 416 U.S. 696, 715 (1974).
45. 416 U.S. 696 (1974).
46. Two circuits in three separate cases before *Bradley* had already passed on the applicability of section 718 to services rendered prior to its enactment, and in all three cases had declined to apply it. Henry v. Clarksdale Municipal Separate School Dist., 480 F.2d 583 (5th Cir. 1973); Thompson v. School Bd., 472 F.2d 177 (4th Cir. 1972); Johnson v.

ing cases, the section was not to be applied retroactively.[47] Rather, the Court stated that, in the absence of any legislative direction to the contrary, there exists "at least implicit support for the application of the statute to pending cases,"[48] so far as such application does not result in "manifest injustice."[49]

This statement by the Court in *Bradley*—that a court is to apply the law in effect at the time it renders its decision, unless doing so would result in manifest injustice, or unless there is statutory direction or legislative history to the contrary—both clarifies yet confuses the answer to the third question implicitly raised though left unanswered by the decision in *United States v. Schooner Peggy*.[50] When is the application of this "intervening law" to be specifically avoided? The statement in *Bradley* clarifies, of course, in that it concisely reduces to a two-point determination the retroactive application of a change in law[51] to pending cases: the law is to be given recognition and effect in the absence of a showing of (1) contrary legislative direction, or (2) manifest injustice. Yet it confuses in so far that, if by this language the Court intends to raise a "presumption" in favor of retrospective application as a general rule, it does so counter to an ancient bias to the contrary.[52] The traditional jurisprudential concept is that "the essence of a law [is] that it be a rule for the future."[53] It would appear that, in considering whether such a scope is intended by the *Bradley* decision, what the Court means by "manifest injustice" assumes special significance, being the one of the two criteria which is, by its terms, open to the more extensive interpretation. It is left to be concluded, then, whether the phrase "manifest injustice" is given some new or otherwise expansive meaning by the Court.

The *Schooner Peggy* decision states that "in mere private cases between individuals, a court will and ought to struggle hard against a construction which

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Combs, 471 F.2d 84 (5th Cir. 1972). In *Thompson v. School Board, supra*, the court held that "legislation is not to be given retrospective effect to prior events unless Congress has clearly indicated an intent to have the statute applied in that manner," and found the legislative history insufficient to suggest such an intent. 472 F.2d at 178. The court in *Johnson v. Combs, supra*, also found the legislative history "inconclusive." 471 F.2d at 87. *See also* Bradley v. School Bd., 416 U.S. 696, 716 n.23 (1974).

47. "[W]e must reject the contention that a change in the law is to be given effect in a pending case only where that is the clear and stated intention of the legislature." Bradley v. School Bd., 416 U.S. 696, 715 (1974).

48. Bradley v. School Bd., 416 U.S. 696, 716 (1974).

49. *Id.* at 711.

50. 5 U.S. (1 Cranch) 103 (1801).

51. It must be assumed that the Court is not referring to a change in law of a judicial nature; that is, to a change in law brought about by a subsequent state court decision, as discussed above. Arguably this is so on the theory that, since *Vandenbark v. Owens-Illinois Glass Co.*, 311 U.S. 538 (1941), the question of such application no longer falls precisely within that obligation of the federal reviewing court to apply subsequent state law pursuant to the change in law doctrine, but rather more simply falls within its broader obligations regarding the ascertaining of state law generally. *See, e.g.*, Universal Underwriters Ins. Co. v. Wagner, 367 F.2d 866 (8th Cir. 1966).

52. Smead, *The Rule Against Retroactive Legislation: A Basic Principle of Jurisprudence*, 20 MINN. L. REV. 775 (1936).

53. *Id.* at 780. *See also* Union Pac. Ry. v. Laramie Stock Yards Co., 231 U.S. 190, 199 (1913). "[T]he first rule of construction is that legislation must be considered as addressed to the future, not to the past." *Id.*

will, by a retrospective operation, affect the rights of parties, but in great national concerns, . . . the court must decide according to existing laws . . . ."[54] The traditional considerations in passing on retroactive application evolving from this are: (1) whether the concerns of the case are "national" or "private" in nature, and (2) whether the rights in question are of a "vested" nature.[55] As mentioned, however, the *Bradley* decision states that, in the absence of contrary legislative direction, a court is to apply the change in law "unless doing so would result in manifest injustice."[56] The answer as to when a court is to specifically decline to retroactively apply a change in law properly turns, then, on whether the *Bradley* enunciation is intended to stand as anything more than a modern restatement of the more traditional considerations. It would appear that such is not the case, and that the phrase "manifest injustice" is not to be given a totally new or otherwise expansive meaning.

The Court in *Bradley v. School Board*[57] sets out three factors a reviewing court should consider in determining whether a "manifest injustice" would issue from the retroactive application of a change in law. These include (1) the nature and identity of the parties, (2) the nature of the rights of those parties, and (3) the nature of the impact of the change in law upon those rights.[58]

With respect to the first criterion—the nature and identity of the parties—the Court places heavy emphasis not only on the relative abilities of the parties to adequately present and protect their interests, but also on the very interest advocated. It notes the fact that the school board is a publicly funded government entity with access to disproportionately greater financial and human resources than are the parent-guardian petitioners. It also recognizes the fact that, by its very nature, school desegregation litigation "is of a kind different from 'mere private cases between individuals,' "[59] the parties bringing the action—as verbalized by the Court's decision in *Newman v. Piggie Park Enterprises, Inc.*[60]—doing so "as a 'private attorney general,' vindicating a policy

54. United States v. Schooner Peggy, 5 U.S. (1 Cranch) 103, 109 (1801).

55. "There is no fixed formula which measures the content of all the circumstances whereby a party is said to possess a 'vested right'; it is a term, rather, which sums up a judicial determination that the facts of the case render it inequitable that the State impede the individual from taking certain action." Lefrak Forest Hills Corp. v. Galvin, 40 App. Div. 2d 211, 225, 338 N.Y.S.2d 932, 939 (1972). Generally, however, the concept of a "vested right" is that of a present fixed interest which in reason and natural justice should be protected against arbitrary state action. Troy Hills Village, Inc. v. Fischler, 122 N.J. Super. 572, 580, 301 A.2d 177, 181 (1971). The United States Supreme Court has long held that where an enacted law acts to divest rights—particularly those which have been vested anterior to the enactment of the law—such law would be invalid unless such is "the unequivocal and inflexible import of the terms, and the manifest intention of the legislature." United States v. Heth, 7 U.S. (3 Cranch) 399, 413 (1806). *See also* Smead, *supra* note 52, at 797. "[A]ny law which divests property rights is retroactive and, unless justified by the court as being reasonable, is invalid." *Id.*

56. Bradley v. School Bd., 416 U.S. 696, 711 (1974).

57. 416 U.S. 696 (1974).

58. *Id.* at 717.

59. *Id.* at 718.

60. 390 U.S. 400 (1968).

that Congress considered of the highest priority."[61] The touchstone the Court relies upon seems clearly one of a "national concern" versus "private concern" type of determination which, as mentioned, has roots dating back to *Schooner Peggy*.

With respect to the second criterion—the nature of the rights involved—the Court in *Bradley* examined briefly to see whether or not an application of section 718 would infringe upon any "matured" or "unconditional" right,[62] and finding it would not, held there was no injustice worked.[63] This it distinguished from its decisions in *Greene v. United States*[64] and *Union Pacific Railway Co. v. Laramie Stock Yards Co.*[65] —both cases involving rights of a private, vested, and proprietary nature. Again, it would seem that this new focal point of determination serves as a modern repository for prior traditional considerations—for what were traditionally deemed questions involving antecedent rights.

Finally, as regards the nature and impact of the change in law upon existing rights, the Court voiced concern over the potential denial of due process—that "new and unanticipated obligations may be imposed upon a party without notice or an opportunity to be heard."[66] However, it found that there was no imposition of an increased burden on the school board, since section 718 did not alter "the Board's constitutional responsibility for providing pupils with a nondiscriminatory education."[67] As with the former two criteria, such consideration is not new in the determinations regarding retroactive application of legislation.[68]

It remains to be seen to what extent the Court's decision in *Bradley v. School Board*[69] will be applied in future decisions, and any real conclusion as to *Bradley's* significance must abide the outcome of these cases. It can here be noted only that, while the Court was hestitant to break away from traditional considerations in making its determination of "manifest injustice," it nonetheless displayed a decisive eagerness not to be bound by a prospective application of legislation which is inconclusive or silent as to possible retroactive effect; an eagerness drafters of legislation may be well-advised to consider. It may be, of course, that *Bradley* will be given only a limited future application, intended

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61. *Id.* at 402.
62. Bradley v. School Bd., 416 U.S. 696, 720 (1974).
63. *Id.*
64. 376 U.S. 149 (1964) (claimant's prior adjudicated right to recover lost earnings held to have vested prior to effective date of Defense Department regulation altering the conditions entitling him to restitution, so that retrospective application of the new regulation was refused).
65. 231 U.S. 190 (1913) (act subjecting original grant of right of way to railroad to possible forfeiture denied retrospective effect).
66. Bradley v. School Bd., 416 U.S. 696, 720 (1974).
67. *Id.* at 721.
68. *E.g.*, Ochoa v. Hernandez y Morales, 230 U.S. 139 (1913) (order by military governor of Puerto Rico reducing time period during which possession must continue in order to convert an entry of possession into a record of ownership held to violate due process when applied retroactively, as it enabled one with claim by possession only to take title immediately without notice to the owners).
69. 416 U.S. 696 (1974).

as but an extension in this instance of the federal trial court's already broad powers to effect equitable remedies in school desegregation cases.[70] However, should the Court seek instead to enforce a broad compliance with the *Schooner Peggy* principle, it has, by *Bradley*, laid for itself a strong foundation for such action.

RAYMOND A. NOWAK

70. *E.g.*, Bradley v. School Bd., 53 F.R.D. 28, 34-40 (E.D. Va. 1971) and cases cited.

SECURITIES REGULATION—NONDISCLOSURE OF MATERIAL INSIDE INFORMATION IS SUFFICIENT TO IMPOSE LIABILITY UPON NON-TRADING "TIPPERS" AND TRADING "TIPPEES" TRANSACTING ON AN ANONYMOUS SECURITIES EXCHANGE TO ALL PERSONS WHO PURCHASED THE STOCK DURING THE PERIOD OF NONDISCLOSURE WITHOUT KNOWLEDGE OF THE INFORMATION.—*Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc.* (2d Cir. 1974).

Due to its status as the prospective managing underwriter of a large issue of Douglas Aircraft Corporation debentures,[1] defendant Merrill Lynch, Pierce, Fenner & Smith, Inc. (Merrill Lynch) and some of its officers, directors and employees (the individual defendants) were informed by Douglas of data contained in a forthcoming revised earnings report. This accounting was subsequently released to the public on June 24th, and indicated a radical change from the published report of June 7th; the projected 85 cents per share earnings was reduced to only 49 cents per share for the first half of fiscal year 1966, the company expected no profit for that fiscal year and the earnings for 1967 would be half of those predicted in the earlier report.[2] Prior to the report's public dissemination, between June 20 and June 24th, defendant Merrill Lynch and the individual defendants disclosed its contents to certain customers (the selling defendants), most of whom were institutional investors. Armed with this non-public data, the selling defendants sold from their existing positions or sold short[3] more than 165,000 shares of Douglas common stock, approximately half of all the Douglas shares sold on the New York Stock Exchange from June 20 to June 23.[4] Commencing June 22-23, the market price suddenly plummetted from a high of $90.50 per share and this trend continued until the price reached a low of $30 per share in October, 1966.[5] Plaintiffs had purchased their shares before the public availability of the revised report, and the resulting plunge in the stock's market price caused them to suffer substantial losses. Four years after this series of events and sub-

1. The debentures offering was for $75,000,000; the registration statement naming Merrill Lynch as managing underwriter became effective on July 12, 1966. Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 495 F.2d 228, 231 (2d Cir. 1974).

2. *Id.* at 231-32; *In re* Investors Management Co., [1970-1971 TRANSFER BINDER] CCH FED. SEC. L. REP. ¶ 78,163, at 80,515-16 (SEC 1971).

3. 17 C.F.R. § 240.3b-3 (1974). This section defines a "short sale" as "any sale of a security which the seller does not own or any sale which is consummated by the delivery of a security borrowed by or for the account of the seller." Two additional provisions relating to "short sales" were established by the SEC to prevent a repeat of disastrous effects of short selling felt in the plunging market of 1937. 2 L. LOSS, SECURITIES REGULATION 1229-30 (2d ed. 1961) [hereinafter cited as Loss]; *see* 17 C.F.R. § 240.10a-1 and -2 (1974).

4. Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 495 F.2d 228, 232 (2d Cir. 1974). In another proceeding, the Securities and Exchange Commission noted that the aggregate price of these shares totaled more than $13,300,000. *In re* Investors Management Co., [1970-1971 TRANSFER BINDER] CCH FED. SEC. L. REP. ¶ 78,163, at 80,516 (SEC 1971).

5. Shapiro v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 495 F.2d 228, 233 & n.8 (2d Cir. 1974); *In re* Investors Management Co., [1970-1971 TRANSFER BINDER] CCH FED. SEC. L. REP. ¶ 78,163, at 80,516 (SEC 1971).