NOS. 11-55859 & 11-55958

United States Court of Appeals for the Ninth Circuit

HOLLY HANSON, *et al.*,

Plaintiffs-Appellants in No. 11-55859,

– v. –

MORGAN STANLEY SMITH BARNEY LLC,

Defendant-Appellee.

MARCIA BLOEMENDAAL, *et al.*,

Plaintiffs-Appellants in No. 11-55958,

– v. –

MORGAN STANLEY SMITH BARNEY LLC,

Defendant-Appellee.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA
CASE NO. 5:10-CV-01455 DSF (PLAx)
DALE S. FISCHER, UNITED STATES DISTRICT JUDGE

BRIEF FOR SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION AS *AMICUS CURIAE* IN SUPPORT OF APPELLEE

IRA D. HAMMERMAN
KEVIN M. CARROLL
SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION
1101 New York Avenue, NW
Washington, DC 20005
(202) 962-7300

ALLAN DINKOFF
WEIL, GOTSHAL & MANGES LLP
767 Fifth Avenue
New York, New York 10153
(212) 310-8000

Attorneys for Amicus Curiae Securities Industry and Financial Markets Association

CORPORATE DISCLOSURE STATEMENT

The Securities Industry and Financial Markets Association is not a publicly traded corporation. It has no parent corporations and no publicly traded corporation owns more than 10% of its stock.

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page

CASES

STATUTES, RULES & REGULATIONS

TABLE OF AUTHORITIES
(continued)

Page

OTHER AUTHORITIES

INTEREST OF AMICUS CURIAE

The Securities Industry and Financial Markets Association ("SIFMA") brings together the shared interests of more than 600 securities firms, banks and asset managers globally. Many of SIFMA's members, like defendants in these consolidated appeals, are subject to requirements imposed by Congress, the Securities and Exchange Commission ("SEC"), and self-regulatory organizations ("SROs") to adopt polices and procedures to supervise the trading activities of their employees in order to effectively deter and prevent insider trading and other consumer and market abuses perpetrated by their employees. Also, like the defendants in these appeals, many of SIFMA's members have long determined that, subject to limited exceptions, requiring their employees to maintain personal self-directed trading accounts within the firm is the most effective way to monitor their employees' trading activities. SIFMA's members thus have a strong interest in this appeal because California Labor Code § 450, if applied as plaintiffs suggest, would prevent firms from utilizing the most common and effective practice in the industry for supervising the trading activities of their employees.

All parties have consented to SIFMA appearing as amicus curiae and filing this brief.[1]

[1] This brief is submitted pursuant to Fed. R. App. P. 29(a). No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund preparation or submission of this brief.

SUMMARY OF ARGUMENT

Congress, the SEC, and SROs like the New York Stock Exchange ("NYSE") and the Financial Industry Regulatory Authority ("FINRA") require brokerage firms to adopt *effective* compliance systems designed to protect the integrity of the public securities markets. The federal regulatory scheme does not contemplate brokerage firms adopting ineffective, but theoretically *possible* mechanisms dictated by plaintiffs' lawyers. Nor does the federal regulatory scheme envision granting every employee at every brokerage firm the *right* to have trading accounts away from their firm, regardless of the nature of the firm's business, and regardless of the employee's access to inside information, the employee's compliance history, and the employee's trading patterns. Instead, the federal regulatory scheme requires firms to take all of these and other factors into account when deciding whether to grant the employee permission to maintain an account at another firm. At bottom, plaintiffs seek to turn the federal regulatory scheme on its head – transforming a world of compliance systems tailored to a firm's business model and discretionary decisions grounded in an employee's unique circumstances into a world where one size fits all and employees no longer seek permission to maintain brokerage accounts at another firm, but have an absolute right to do so.

Discharging their responsibilities under the securities laws and exercising the flexibility granted to them by Congress and the regulators, many firms, but by no means all, have determined that they can best prevent insider trading and other market abuses perpetrated by their employees if they generally require employees to maintain their self-directed trading accounts at their own firm. These firms have concluded that while it may be *possible* to monitor employee trading activity by receiving information from other firms where employees maintain accounts, it is not the most *effective* way to supervise their employees' trading. Among other benefits, requiring employees to utilize in-house trading accounts permits firms to employ real-time electronic monitoring, use proprietary data to analyze an employee's trading patterns and activity, and move quickly to reverse suspicious trades so as to mitigate any damage. But brokerage firms also recognize that any monitoring policy must be flexible, and so firms routinely make exceptions to these general policies when an employee's individual circumstances warrant.

Applying Section 450 as plaintiffs urge would eliminate the flexibility mandated by federal securities laws. If plaintiffs prevail, every broker-dealer would likely be required to permit *all* of its employees in California to maintain *all* of their brokerage accounts outside the firm, including employees with highly sensitive positions or even employees suspected of insider trading, such as David Notrica, one of the plaintiffs in *Bloemendaal*.

ARGUMENT

I. Most Large Brokerage Firms Limit Employees' Access to External Trading Accounts to Prevent Insider Trading and Market Abuses

As outlined in detail at Point II below, Congress, the SEC, and SROs have concluded that brokerage firms need flexibility when designing effective mechanisms for supervising their employees. This discretion is an integral part of the regulatory scheme, since what is effective in one circumstance is not necessarily effective in another. For example, a small broker-dealer engaged principally in market-making activities may permit its employees to have personal self-directed trading accounts outside the firm because the firm's operations are small enough, and sufficiently limited in scope, that the firm can effectively supervise its employees through other procedures. As the SEC has observed, smaller firms can effectively monitor their employees by requiring "pre-clearance of all employee trades, either by the compliance department or the individual supervisor." SEC Division of Market Regulation, Broker-Dealer Policies and Procedures Designed to Segment the Flow and Prevent the Misuse of Material Non-Public Information, [1989-1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 84,520, at 80,621 (Mar. 1, 1990).

In contrast, large complex firms like the defendants here are required to adopt effective compliance systems to monitor the trading of employees around the globe who are engaged in an incredibly wide range of activities and who have the ability to misuse their position at the firm for personal gain. A few examples illustrate the point: (1) Investment bankers who advise companies about potential acquisitions, divestitures, and stock and bond offerings have the ability to trade on this information in advance of it being made public. The same is true for the people supporting these investment bankers – compliance personnel, lawyers, secretaries, document production personnel, and individuals in other areas of the firm who facilitate the client's transactions, such as individuals on sales and trading desks around the world who will assist in the sale of stock or bond offerings to the general public after the deal is publicly announced. (2) Individuals involved in designing customized complex derivative transactions to assist clients in hedging their business risks have access to client information that is not publicly available and thus can trade on that information to their personal advantage. (3) Sales and trading personnel who facilitate customer trades in the market have the ability to trade ahead of their client's orders, which allows them to profit at their client's expense. These activities take place globally, twenty-four hours a day, seven days a week.

Firms of the size and complexity of the defendants here have concluded that they can prevent the abuses illustrated above more effectively if they require employees to maintain their self-directed trading accounts at the firm. While it may be possible to monitor employee trading activity by receiving information from other firms where employees maintain accounts, it is not the most *effective* way for many firms to do so. In-house monitoring of employee trading accounts has many advantages, including the ability to implement real-time electronic monitoring, rather than having to rely on trade confirmations and statements sent by other firms. Although many firms now transmit this information to others electronically, many do not, and instead provide confirmations and statements only in hard copy, and only after a significant delay. This prevents firms from uncovering, reporting, and remedying potential regulatory violations expeditiously (as required by the securities laws), reduces the accuracy of firms' detection efforts, and adds to the firms' burden in monitoring employee accounts by reducing the automation of the supervisory process. *See generally* ER 67-68.[2]

Even where firms receive external trading information electronically, the ability to monitor in-house trading activity in real time carries significant advantages. For one thing, firms can implement before-the-fact trading restrictions when the accounts are maintained in-house. For example, if an employee or group of employees has access to sensitive, inside information about a particular company or issuer, the firm can prevent those employees from trading in that issuer's securities. Such before-the-fact intervention is not possible with externally held accounts.

[2] Unless otherwise specified, citations to the Excerpts of Record ("ER") refer to the Excerpts of Record filed in No. 11-55958.

Firms also do not receive as much information about accounts held externally as they do about the accounts held at the firm. Consequently, firms can far more effectively employ their internal filters and algorithms to analyze employees' historical trading patterns when their employees' accounts are held in-house. *See* ER 68. As compared to an external firm, an employee's firm has far more comprehensive information about the employee's historical trading activity, including information about the employee's trades on behalf of the firm's clients in addition to information about trades in the employee's personal account. Thus not only can a firm use its proprietary systems to analyze an employee's trading activity to determine whether particular trades are unusual in light of historical patterns in the employee's portfolio (or even as compared to other individuals holding similar portfolios), but the firm also can analyze the employee's personal trading side-by-side with his trading on account of clients. Such an analysis might reveal that an employee is engaging in the illegal practice of "front running," whereby he executes trades in a particular security on his own account with advance knowledge of pending orders in the same security on behalf of clients that may affect the security's price. *See id.* Simply put, when firms have in-house access to trading information by their employees, they are more likely to be able to detect and prevent certain illegal trading behaviors that might go undetected if the account were held externally.

Moreover, when trading accounts are kept in-house, firms can more quickly react to potential violations by, for example, correcting and reversing suspect trades. *See id.* For obvious reasons, a firm cannot easily reverse trades that have occurred at another firm. The ability to act quickly in the face of a potential violation of the securities laws is vital not only in identifying the perpetrators of the violation, but in minimizing the economic and reputational damages that stem from such improper activity.

In addition, if insider trading or other market abuses are suspected, it is far easier for a firm to investigate the matter when the account is held in-house and potential witnesses and other information relating to the trade are readily available. *See id.* For instance, if an employee's trading pattern appears abnormal, the firm can interview the employee's financial advisor to determine the circumstances surrounding the trade when the account is held in-house; obtaining access to such an individual is far more complicated when the account is held externally.[3]

Nearly all firms, however, recognize that a one-size-fits-all approach does not work for every employee's situation, and so they grant exceptions from the general prohibition against external brokerage accounts where insider trading and other market abuses are not likely to occur. For example, firms often allow

---

[3] The named plaintiffs in these consolidated cases are financial advisors, but the rules at issue here are equally applicable to other employees, such as investment bankers and traders.

employees to maintain external accounts that hold certain types of securities and instruments, such as mutual funds in some circumstances. *See* ER 65. In addition, firms also typically exempt certain types of accounts—including 401(k) accounts and other retirement and college savings accounts—from requirements that employees keep these accounts in-house. *See* ER 235-36.

II. Securities Firms Must Employ Effective Measures to Monitor the Trading Activities of their Employees or Else Face Regulatory Sanctions and Reputational Harm

"The general responsibility of broker-dealers and investment advisers [sic] to supervise their employees is well established under the securities laws." H.R. Rep. No. 100-910, at 20 (1988), *reprinted in* 1988 U.S.C.C.A.N. 6043, 6057.[4] This supervision obligation dates back at least as far as 1960, when the SEC held in *In re Reynolds & Co.*, Exchange Act Release No. 6273, 1960 WL 56264 (May 25, 1960), that where the failure of a brokerage firm and its responsible personnel to maintain and enforce adequate supervisory procedures resulted in the perpetration of fraud upon customers, or in other misconduct, then the failure to supervise constituted "participation in" the misconduct of the employees.[5]

---

[4] *See generally Hollinger v. Titan Capital Corp.*, 914 F.2d 1564, 1574 (9th Cir. 1990) ("[T]he broker-dealer is required by statute to establish and enforce a reasonable system of supervision to control its representatives' activities.").

[5] *See also In re Reynolds & Co.*, 1960 WL 56264, at *10 ("We have repeatedly held that brokers and dealers are under a duty to supervise the actions of employees and that in large organizations it is especially imperative that the system of internal control be adequate and effective and that those in authority exercise the

The Securities Exchange Act of 1934 was amended in 1964 to provide the SEC with express statutory authority to sanction both the firm and the firm's supervisory personnel for failure to supervise. Specifically, the SEC can sanction a broker-dealer, or anyone at the firm with supervisory responsibility, if the SEC finds that the firm or such person has failed reasonably to supervise, with a view toward preventing violations of the securities laws, another person who commits such a violation. To satisfy this duty to supervise, firms must establish and follow policies and procedures that reasonably can detect or prevent employee misconduct that violates the federal securities laws. *See* 15 U.S.C. § 78o(b)(4)(E).[6]

SROs, like the NYSE and FINRA, have also promulgated rules that are integral to enforcing "[t]he obligation of broker-dealers to supervise their

---

utmost vigilance whenever even a remote indication by irregularity reaches their attention.").

[6] Specifically, 15 U.S.C. § 78o(b)(4)(E) provides that a securities firm can be subject to regulatory sanctions, including the suspension or revocation of the firms' registration, for failing reasonably to supervise, "with a view to preventing violations of [the securities laws], another person who commits such a violation, if such other person is subject to his supervision." But,

> no person shall be deemed to have failed reasonably to supervise any other person, if—
>
> (i) there have been established procedures, and a system for applying such procedures, which would reasonably be expected to prevent and detect, insofar as practicable, any such violation by such other person, and
>
> (ii) such person has reasonably discharged the duties and obligations incumbent upon him by reason of such procedures and system without reasonable cause to believe that such procedures and system were not being complied with.

Id.

employees." H.R. Rep. No. 100-910, at 20, 1988 U.S.C.C.A.N. at 6057.[7] For example, NASD Rule 3010 provides that "[e]ach member [firm] shall establish and maintain a system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations."[8] *See also* NYSE Rule 342.21. To ensure compliance with these supervisory obligations, SROs require securities firms to certify that the firm "has in place processes to establish, maintain, review, test and modify written compliance policies and written supervisory procedures reasonably designed to achieve compliance with . . . federal securities laws and regulations." FINRA Rule 3130; *see also* NYSE Rule 351. As the SRO rules make clear, "[f]inal responsibility for proper supervision shall rest with the member" firm. NASD Rule 3010(a).

Insider trading is a particularly pernicious form of market abuse, which employees at brokerage firms can engage in by reason of their access to confidential information necessary to perform their job. Congress thus recognized

---

[7] All SRO rules are subject to SEC approval. 15 U.S.C. § 78s(b)(1); *see also Credit Suisse First Boston Corp. v. Grunwald*, 400 F.3d 1119, 1128 (9th Cir. 2005) ("The Securities Exchange Act of 1934 created a system of supervised self-regulation in the securities industry whereby organizations such as the NASD or the NYSE could promulgate their own governing rules and regulations, subject to oversight by the Securities and Exchange Commission.").

[8] *Accord Coleman & Co. Sec., Inc. v. Giaquinto Family Trust*, 236 F. Supp. 2d 288, 302-03 (S.D.N.Y. 2002) ("NASD Conduct Rule 3010(a) imposes the same duty [as the securities laws] on member firms").

that "[w]ith respect to insider trading in particular, the necessity for appropriate supervision to prevent violations is evident in view of the special opportunities for abuse in this area." H.R. Rep. No. 100-910, at 17, 1988 U.S.C.C.A.N. at 6054. To prevent insider trading by brokerage firm employees, Congress enacted the Insider Trading and Securities Fraud Enforcement Act of 1988 ("ITSFEA"), which expressly requires brokerage firms to

> establish, maintain, and enforce written policies and procedures *reasonably designed, taking into consideration the nature of such broker's or dealer's business,* to prevent the misuse in violation of this chapter . . . of material, nonpublic information by such broker or dealer or any person associated with such broker or dealer.

15 U.S.C. § 78o(g) (emphasis added).

This statutory obligation is reinforced by NYSE Rule 342.21(a), which requires firms to "subject trades in NYSE listed securities and in related financial instruments which are effected . . . for the accounts of members or employees of the member or member organization and their family members . . . to review procedures that the member or member organization [i.e., securities firm] determines to be reasonably designed to identify trades that may violate" the securities laws.

Securities firms face significant regulatory sanctions if they fail to take adequate steps to prevent insider trading and other market abuses perpetrated by their employees. The SEC has not been shy in imposing sanctions on firms and supervisors who have not reasonably supervised their employees. For example, the SEC recently sanctioned a firm for failure to reasonably supervise its employees where it "too frequent[ly]" granted employees "permission to keep accounts away from the firm." *See In re Janney Montgomery Scott LLC*, Exchange Act Release No. 64,855, 2011 WL 2680704, at *5 (July 11, 2011). In addition, A.G. Edwards & Sons was required to pay disgorgement and civil penalties totaling nearly $4 million in connection with the failure to supervise its employees who were engaging in illegal market timing activities. *See In re A.G. Edwards & Sons, Inc.*, Exchange Act Release No. 55692, 2007 WL 1285761 (May 2, 2007); *see also In re SG Americas Sec. LLC*, Exchange Act Release No. 59401, 2009 WL 367024, at *9 (Feb. 13, 2009) (imposing sanctions for failure "reasonably to supervise [an employee] with a view to preventing and detecting [the employee's] violations of the federal securities laws by failing to respond to various 'red flags' relating to [the employee's] trading activity," including, *inter alia*, insider trading).

In addition to regulatory sanctions, firms face significant reputational risks if one of their employees engages in insider trading or other market or customer abuses. Insider trading scandals involving brokerage firm employees are often front-page news and can be damaging not only for the individuals involved, but also for the firms that employ them. For example, well-publicized accounts of insider trading cases include a scheme coordinated by employees of Merrill Lynch and Goldman Sachs, who traded on inside information about deals in which the firms were engaged. *See Two Arrested On Charges of Insider Trading*, N.Y. Times, Apr. 11, 2006, *available at* http://www.nytimes.com/2006/04/11/business/worldbusiness/11iht-inside.html. Companies rely on brokerage firms to maintain the confidentiality of their non-public information, and illegal activities by firm employees threaten to undermine a firm's credibility with its clients.

III. Congress and Regulators Have Recognized that Brokerage Firms Must Have Flexibility to Adopt the Policies They Believe are Most Effective at Detecting and Preventing Securities Law Violations, Including Restrictions on their Employees' Access to External Trading Accounts

Congress and regulators have long endorsed requiring employees to maintain directed trading accounts at their firm as an effective means of detecting and preventing insider trading and other market and consumer abuses. In enacting the ITSFEA, Congress "expect[ed] that a firm's supervisory system would include, at a minimum, employment policies ***such as those requiring personnel to conduct their securities trading through in-house*** accounts ***or*** requiring that any trading in outside accounts be reported expeditiously to the employing firm." H.R. Rep. No. 100-910, at 22, 1988 U.S.C.C.A.N. at 6059. (emphasis added). Similarly, the SEC found that "[a]ll firms attempt to reinforce their policies concerning employee misuse of confidential information by placing restrictions on employee trading activity. For example, almost all firms require employees to maintain accounts with the firm." SEC Division of Market Regulation, Broker-Dealer Policies and

Procedures Deigned to Segment the Flow and Prevent Misuse of Material Non-Public Information, [1989-1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 80, 621. *See also* Order Approving Proposed Rule Change Relating to Written Notification of Employer Members and Executing Members by Associated Person Regarding Relations with Each Member, 56 Fed. Reg. 10,931-02 (Mar. 14, 1991) ("The NASD acknowledges the fact that there *may be circumstances* which dictate that an associated person hold an account with someone other than their employer member." (Emphasis added)).

Congress also recognized that firms need to maintain the flexibility to adopt alternative mechanisms for monitoring employee behavior. The ITSFEA dictates that firms tailor their compliance procedures to the firm's individual circumstances. *See* 15 U.S.C. § 78o(g) (requiring firms to establish and maintain policies and practices "reasonably designed, *taking into consideration the nature of such broker's or dealer's business*, to prevent" violations of the securities laws) (emphasis added).

The legislative history is equally clear that brokerage firms must have the flexibility to design programs that meet each firm's circumstances and the varied circumstances of the firm's employees. Congress expressly noted that the securities laws do not "set forth specific policies and procedures that are required of every broker-dealer or investment adviser. Rather, [the ITSFEA] recognizes that the question of what policies and procedures are reasonable for a particular firm may involve consideration of the differing business operations, organizational structure, scope and nature of a firm's business." H.R. Rep. No. 100-910, at 21-22, 1988 U.S.C.C.A.N. at 6058-59. Congress' position followed the SEC's views that brokerage firms must have flexibility in designing their systems for monitoring employee trading activity if those programs were going to be effective. *Id.* at 22, 1988 U.S.C.C.A.N. at 6059 (noting that the SEC "has indicated the importance of providing flexibility to an institution to tailor its policies and procedures to fit its own situation").

The SROs have taken a similar approach. NYSE Rule 407(b) grants securities firms discretion to determine if and when an employee may be permitted to open a brokerage account at another securities firm. That rule provides:

> No member . . . or employee associated with a member or member organization shall establish or maintain any securities or commodities account or enter into any securities transaction with respect to which such person has any financial interest or the power, directly or indirectly, to make investment decisions, at another member or member organization, or a domestic or foreign non-member broker-dealer, investment advisor, bank, other financial institution, or otherwise *without the prior written consent* of another person designated by the member or member organization under Rule 342(b)(1) to sign such consents and review such accounts.

(Emphasis added.)

IV. Section 450 Would Prevent Firms from Implementing the Most Effective Practices to Deter Market Abuses by their Employees and Expose Firms to a Patchwork of Regulation

Federal policy – embodied in acts of Congress, legislative history, SEC regulations, and SRO rules – has both charged firms with the responsibility to supervise their employees' trading to prevent market abuses, and granted firms the flexibility to implement the polices and procedures the firms believe will be most effective in preventing violations of the securities laws by the firms' employees. If plaintiffs prevail in this lawsuit, however, financial services firms will lose this flexibility. They will be precluded from implementing in California the procedures that federal regulators have long endorsed as an acceptable, if not the preferred, method for large firms like defendants here to ensure that their employees comply with the federal securities laws. In place of the flexibility that Congress and the regulators have given to brokerage firms, Section 450, if applied here as plaintiffs insist, would mandate that brokerage firms allow *every* employee in California to maintain self-directed trading accounts outside the firm.

Plaintiffs' reading of Section 450 creates real risks to the investing public. Under plaintiffs' interpretation, Section 450 could *require* brokerage firms to allow *every* employee to maintain an external trading account, even when there are sound reasons to suspect that the employee may well be engaging in insider trading or other potential market and consumer abuses. Plaintiffs suggest that restricting employees' access to external trading accounts, while generally coercive, would "probably not" amount to "compulsion" or "coercion" in circumstances where an employee "had displayed a pattern of abusing outside accounts or was suspected of insider trading." Appellants' Br. in No. 11-55859 ("Pl. Br."), at 20. But plaintiffs make no effort to square this proposition with the plain language of Section 450 or their claims here. Indeed, plaintiffs practically concede this point—they argue that under Section 450, requiring "an employee who had displayed a pattern of abusing outside accounts or was suspected of insider trading" to maintain their accounts at the firm "would *probably* not be considered compulsion or coercion." Pl. Br. 20 (emphasis added). Even here, plaintiffs are unwilling to say definitively that firms could require employees to keep trading accounts in-house under Section 450. This illustrates quite starkly why registered broker-dealers such as the defendants here cannot comply with both Section 450 and their obligations under the federal securities laws to adopt effective mechanisms for supervising their employees.

Accordingly, *Williamson v. Mazda Motor of Am., Inc.*, 131 S. Ct. 1131 (2011), a recent Supreme Court decision on which plaintiffs heavily rely, confirms that Section 450 is preempted here, because it would restrict securities firms from exercising the flexibility that Congress, the SEC, and SROs determined was essential if firms were to develop truly effective compliance systems for monitoring employee trading activity.

The case at bar is virtually identical in many respects to *Geier v. Am. Honda Motor Co.*, 529 U.S. 861 (2000), which *Williamson* distinguished. In *Geier*, the court held that a state tort law suit was preempted by federal regulations that gave manufacturers a choice among several different types of passive restraint systems. As *Williamson* explained, the regulatory scheme at issue in *Geier* was "intended to assure manufacturers that they would retain a choice of installing any of several different passive restraint devices." 131 S. Ct. at 1134. The regulators "deliberately provided the manufacturer with a range of choices," 529 U.S. at 875, because they had made the "policy judgment that safety would best be promoted if manufacturers installed *alternative* protection systems in their fleets rather than one particular system in every car." 131 S. Ct. at 1137.

This is exactly the situation here. Congress, the SEC, and SROs have all determined that granting firms discretion to adopt monitoring polices tailored to their individual circumstances is critical to the effective detection and deterrence of insider trading and other market abuses. *See, e.g.*, H.R. Rep. No. 100-910, at 22, 1988 U.S.C.C.A.N. at 6059 ("The [SEC] has indicated the importance of providing flexibility to an institution to tailor its policies and procedures to fit its own situation."). This stands in sharp contrast to *Williamson*, where there was no compelling reason why car manufacturers were given the option to install different types of seat belts for rear inner seats. State tort law was not preempted in

Williamson, because unlike the situation here and in *Geier*, there was no evidence that providing manufacturers a choice in deciding what type of seat belt to install was a "significant objective of the federal regulation." 131 S. Ct. at 1134.

Section 450 also exposes financial services firms to a patchwork of divergent state laws. The federal securities laws and SRO rules are designed to create a uniform, nationwide regulatory framework. Applying Section 450 to employees in California (and to employees in other states with potentially similar statutes) would create substantial logistical problems as firms struggle to comply with a patchwork of different state regulations while attempting to fulfill their federal regulatory obligations.

The residents of California would also be injured if firms can no longer require their employees to maintain directed trading accounts at the firm. As discussed above, many firms have concluded that requiring employees to maintain directed trading accounts at the firm is the most effective way to prevent violations of the federal securities laws. This approach has been endorsed by Congress and the regulators. But, if plaintiffs prevail, California residents will be forced to live with less effective controls over employee misconduct in the state. Their broker dealers will also be faced with higher costs of ensuring compliance, which may be passed onto California consumers.

V. Offering Brokerage Services for Free Is Not a Viable Alternative

Securities firms have enacted policies requiring employees to maintain self-directed accounts at the firm in order to comply with their obligations under federal law, not to capture additional revenue. And, many firms offer their employees deep discounts on self-directed trading accounts relative to market prices. But applying section 450 to require firms to offer free self-directed trading accounts would not only impinge on a firm's discretion under federal law, but could well create a host of additional problems. Most notably, free trading accounts would encourage employees to engage in excessive trading, detracting from customer service and increasing the risk of market abuses.

In addition, requiring securities firms to offer free trading accounts would impose costs on firms that Congress and the regulators never intended. Firm employees like investment bankers and research analysts would be entitled to open accounts that are typically handled by financial advisors, who generally are paid based on the revenue the accounts generate. Mandating that firms offer these accounts for free would require either the financial advisers to work on these accounts without compensation or, more likely, would require the firms to find some way to compensate the advisors, increasing the firms' cost of compliance with the federal securities laws. This is in addition to the general costs firms incur for customer accounts, such as processing and clearing costs. Congress and the

SROs gave firms discretion in deciding how best to fulfill their responsibility to prevent insider trading and other market abuses. This federal scheme does not permit states to impose what is in effect a penalty on firms that do so by adopting practices the industry and regulators have viewed as the most effective for firms such as the defendants here.

Finally, in weighing any relative equities, it should be kept in mind that if plaintiffs prevail in these cases, brokerage firms could lawfully decide to meet their regulatory obligation by prohibiting employees from opening any self-directed trading accounts at all. This is the safest course for firms, but imposes the greatest burden on employees. Section 450 could not have been intended to create such a result, and Congress clearly sought to permit such accounts while giving firms the flexibility to design the most effective compliance system for detecting market abuses consistent with each firm's circumstances, as well as the unique circumstance of each employee.

CONCLUSION

The Court should protect the regulatory scheme adopted by Congress and the regulators, and affirm the decisions below.

Dated: January 26, 2012

Respectfully submitted,

/s/ Allan Dinkoff

Allan Dinkoff
WEIL, GOTSHAL & MANGES LLP
767 Fifth Avenue
New York, NY 10153-0119
Telephone: (212) 310-8000

Attorneys for Amicus Curiae Securities Industry and Financial Markets Association

Ira D. Hammerman
Kevin M. Carroll
SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION
1101 New York Avenue, NW
Washington, DC 20005
Tel.: (202) 962-7382

CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitations of Fed. R. App. P. 32(a)(7)(B) because this brief contains 5,252 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because it has been prepared in a proportionally spaced typeface using Microsoft Word 2002 in Times New Roman font size 14.

/s/ Allan Dinkoff
Allan Dinkoff

STATE OF NEW YORK)
) ss.: **AFFIDAVIT OF**
COUNTY OF NEW YORK) **CM/ECF SERVICE**

I, Natasha S. Johnson, being duly sworn, depose and say that deponent is not a party to the action, is over 18 years of age.

On January 26, 2012

deponent served the within: **Brief for Securities Industry and Financial Markets Association as Amicus Curiae in Support of Appellee**

upon:

SEE ATTACHED LIST

via the CM/ECF Case Filing System. All counsel of record in this case are registered CM/ECF users. Filing and service were performed by direction of counsel.

Sworn to before me on January 26, 2012

s/Maria Maisonet
MARIA MAISONET
Notary Public State of New York
No. 01MA6204360
Qualified in Bronx County
Commission Expires Apr. 20, 2013

s/Natasha S. Johnson

Job # 239902

Service List:

Lynne C. Hermle
Kenneth P. Herzinger
Trish M. Higgins
Robert M. Yablon
ORRICK, HERRINGTON & SUTCLIFFE LLP
1000 Marsh Road
Menlo Park, CA 94025-1015
(650) 614-7400

E. Joshua Rosenkranz
ORRICK, HERRINGTON & SUTCLIFFE LLP
51 West 52nd Street
New York, NY 10019-6142
(212) 506-5000
Counsel for Defendant-Appellee

Maxwell M. Blecher
Alyson C. Decker
BLECHER & COLLINS, PC
515 South Figueroa Street, Suite 1750
Los Angeles, CA 90071
Tel: 213-622-4222

James Robert Noblin
GREENWELLING, PC
4500 East Pacific Coast Hwy, 4th Fl.
Long Beach, CA 90804
Tel: 562-391-2487

Robert D. Blasier
ROBERT J. BLASIER JR. LAW OFFICES
3600 Peidra Montana Rd.
El Dorado Hills, CA 95762
Tel: 916-933-7289

Robert S. Green
Nicole D. Reynolds
GREENWELLING, PC
595 Market Street, Suite 2750
San Francisco, CA 94105
Tel: 415-477-6700
Counsel for Plaintiffs-Appellants in Hanson

Louis M. Benowitz
LAW OFFICES OF LOUIS BENOWITZ
9454 Wilshire Blvd. PH
Beverly Hills, CA 90212
Tel: 310-888-7771

Chaim Shaun Setareh
Hayley DeAnn Schwartzkopf
LAW OFFICE OF SHAUN SETAREH, APC
9454 Wilshire Blvd., PH Suite #3
Beverly Hills, CA 90212
Tel: 310-888-7771

David G. Spivak, Attorney
THE SPIVAK LAW FIRM
9454 Wilshire Blvd., Suite 303
Beverly Hills, CA 90212
Tel: 310-499-4730

Mark R. Thierman
Jason Kuller
THIERMAN LAW FIRM
7287 Lakeside Drive
Reno, NV 89511
Tel: 775-284-1500
Counsel for Plaintiffs-Appellants in Bloemendaal