

11-5227-cv

IN THE
United States Court of Appeals
FOR THE SECOND CIRCUIT

UNITED STATES SECURITIES AND EXCHANGE COMMISSION,
Plaintiff-Appellant-Cross-Appellee,
—against—

CITIGROUP GLOBAL MARKETS INC.,
Defendant-Appellee-Cross-Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

**BRIEF OF AMICUS CURIAE SECURITIES INDUSTRY
AND FINANCIAL MARKETS ASSOCIATION
IN SUPPORT OF APPELLANTS AND
IN SUPPORT OF REVERSAL**

Ira D. Hammerman
Kevin M. Carroll
SECURITIES INDUSTRY AND
FINANCIAL MARKETS
ASSOCIATION
1101 New York Avenue, NW
Washington, D.C. 20005

Annette L. Nazareth
Edmund Polubinski III
Gina Caruso
DAVIS POLK & WARDWELL LLP
450 Lexington Avenue
New York, New York 10017
(212) 450-4000

Attorneys for Amicus Curiae

CORPORATE DISCLOSURE STATEMENT

The Securities Industry and Financial Markets Association has no parent company, nor has it issued any stock.

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INTEREST OF AMICUS CURIAE

The Securities Industry and Financial Markets Association (“SIFMA”) is a securities industry trade association representing the interests of hundreds of securities firms, banks, and asset managers.¹ SIFMA’s mission is to support a strong financial industry while promoting investor opportunity, capital formation, job creation, economic growth, and trust and confidence in the financial markets. SIFMA has offices in New York and Washington, D.C. and is the United States regional member of the Global Financial Markets Association. SIFMA regularly files amicus curiae briefs in cases that raise matters of vital concern to participants in the securities industry.

SIFMA and its members have a strong interest in the issues presented by the appeal of the district court’s November 28, 2011 order (the “District Court’s Order,” SPA-1)² refusing to approve the proposed final judgment and consent between the United States Securities and Exchange Commission (the “SEC”) and Citigroup Global Markets Inc. (“Citigroup”). This appeal raises important questions about the circumstances in which a financial institution and its primary regulator may, in their discretion, enter into a consent settlement to resolve an enforcement action. This issue has far-reaching

¹ Pursuant to Federal Rule of Appellate Procedure 29(c)(5), SIFMA states that no one besides SIFMA, its members, or its counsel authored this brief in whole or in part or contributed money that was intended to fund preparing or submitting this brief.

² Citations in the form of “JA-__” refer to pages in the Joint Appendix. Citations in the form of “SPA-__” refer to pages in the Special Appendix.

significance, not only for SIFMA's members, but also for the securities industry as a whole and all its participants.

INTRODUCTION

The District Court's Order, if permitted to stand, would have a profoundly negative impact on the effective enforcement of the securities laws. In particular, the limitations the district court's approach would impose on negotiated consent settlements of SEC enforcement actions would harm SIFMA's members, their shareholders and clients, and the investing public more broadly.

As this Court observed, a central feature of the District Court's Order was its strong disapproval of the SEC's longstanding practice of entering into settlements in which defendants neither admit nor deny the underlying allegations. *SEC v. Citigroup Global Mkts. Inc.*, 673 F.3d 158, 161-62 (2d Cir. 2012) (per curiam) (the "*Citigroup Per Curiam Opinion*"), JA 302–05. In rejecting the settlement in this case, the District Court's Order focused on the absence of admissions by the settling defendant, both because the court indicated that the lack of admitted or proven facts prevented it from appropriately evaluating the settlement, and because private plaintiffs "cannot derive any collateral estoppel assistance from Citigroup's non-admission/non-denial of the S.E.C.'s allegations." *Id.* (quoting *SEC v. Citigroup Global Mkts. Inc.*, No. 11-cv-7387, 2011 U.S. Dist. LEXIS 135914, at *16 (S.D.N.Y. Nov. 28, 2011), SPA-12).

Requiring admissions as a condition of settlement would, however, sharply reduce the number of settled enforcement actions, particularly in cases involving financial institutions. As this Court explained, this approach to judicial approval of negotiated consent settlements "would in most cases undermine any chance

for compromise.” *Citigroup Per Curiam Opinion* at 165, JA-310.

Limiting the availability of SEC consent settlements would have substantial adverse consequences that would be particularly acute in cases involving SIFMA’s members. Because such cases often involve complex facts, transactions, and regulations, they are precisely the types of matters that the SEC should have the discretion to settle where appropriate. Curtailing the ability of the SEC and defendants to resolve these disputes through consent settlements would needlessly impose costs on shareholders and would deplete limited resources that the SEC could deploy more effectively elsewhere.

Moreover, the SEC’s well-established approach to consent settlements benefits the securities industry in other ways by encouraging self-reporting and cooperation by regulated entities, by compensating injured parties, and by conserving judicial resources. For all these reasons, upholding the longstanding practice of judicial approval of negotiated consent settlements of SEC enforcement actions would benefit the securities industry as a whole.

BACKGROUND

The SEC has historically resolved the vast majority of its enforcement actions through negotiated settlements. *See, e.g., SEC v. Clifton*, 700 F.2d 744, 748 (D.C. Cir. 1983) (“Because of its limited resources, the SEC has traditionally entered into consent decrees to settle most of its injunctive actions.”). In fiscal year 2011, for example, the SEC settled 92% of the enforcement actions it brought. *See SEC, FY 2011 Performance and Accountability Report 2* (2011) (noting that the SEC brought 735 enforcement actions in 2011); Max Gulker et al., NERA Economic Consulting, *SEC Settlement Trends*:

2H11 Update 1 (2012) (“NERA Report”) (stating that 682 enforcement actions settled in FY 2011).

In 1972, the SEC, by an amendment to its Rules of Practice, began requiring settling defendants to state that they did not deny the allegations against them. *See* Consent Decrees in Judicial or Administrative Proceedings, Securities Act Release No. 33-5337 (Nov. 28, 1972) (codified at 17 C.F.R. § 202.5(e)). Consistent with its prior practice, however, the SEC also did not require defendants to admit the allegations against them. *See id.* Notwithstanding the district court’s decision in this case, district courts around the country consistently and routinely approve such settlements. *See Citigroup Per Curiam Opinion* at 166, JA-312 (“It is commonplace for settlements to include no binding admission of liability.”).³

Numerous other federal agencies follow similar settlement practices. The Department of Justice, for instance, often obtains consent decrees in civil enforcement actions in which a defendant expressly *denies* liability. *See United States v. BAC Home Loans Servicing, LP*, No. 11-cv-04534 (doc. no. 3) at 3 (C.D. Cal. May 31, 2011) (approving consent order in which defendant “denies any wrongdoing as alleged by the

³ On January 7, 2012, the SEC announced that companies that admit to or are convicted of criminal conduct in parallel cases brought by the Department of Justice will no longer be permitted to simultaneously settle SEC charges without admitting or denying allegations. *See* Statement of Robert Khuzami (Jan. 7, 2012), *available at* <http://www.sec.gov/news/speech/2012/spch010712rsk.htm>. This policy does not affect the vast majority of SEC actions—including this one—where there is no related criminal action. *See id.*

United States or otherwise”); *United States v. New Puck, LP*, No. 04-cv-05449 (doc. no. 2) at 2 (S.D.N.Y. July 14, 2004) (approving consent decree providing that “the defendant denies liability”). Federal district courts routinely approve consent decrees without defendant admissions involving the Equal Employment Opportunity Commission, Federal Trade Commission, Commodity Futures Trading Commission, Environmental Protection Agency, Department of Agriculture, Department of Labor, and the Food and Drug Administration, among others. (See Brief of Def.-Appellee-Cross-Appellant Citigroup at 24-25 (listing agencies that settle suits without admissions and citing authorities); Brief of Appellant/Pet’r SEC at 34-40 (same).) Other federal agencies, like the SEC, have codified their neither-admit-nor-deny settlement practices. See 17 C.F.R. § 10 app. A (CFTC); 40 C.F.R. § 22.18 (EPA); 7 C.F.R. § 110.8 (Dep’t of Ag.); 45 C.F.R. § 672.11 (Nat. Sci. Found.).

ARGUMENT

- I. The District Court’s Order, If Upheld, Would Have a Direct Harmful Impact on All Participants in the Securities Industry**
 - A. The District Court’s Approach Would Dramatically Reduce the Number of Settled Actions, Particularly in Cases Involving Financial Institutions.**

Requiring admissions in SEC consent settlements would dramatically reduce the number of settled enforcement actions involving financial institutions both (1) because the complicated and disputed facts typically at issue are often not susceptible to admissions, and (2) because of the severe collateral consequences associated with any admission.

1. In Cases Involving Complex Facts and Regulations, Admissions May Not Be Accurate or Possible

Given the complex and ambiguous subject matter of many cases involving financial institutions, a judicially imposed requirement that a settling defendant admit SEC allegations would preclude many settlements. Enforcement actions against SIFMA members routinely involve complicated facts and transactions and their intersection with laws and regulations that are themselves open to multiple interpretations. Compounding these complexities are statutes and regulations that turn on the intent of one or more individuals, which may or may not be imputed to an institution. In such cases, the SEC and a defendant very often will have strong good-faith disagreements about both ultimate liability and the relevant underlying facts. These disagreements and the defendant's accompanying good-faith understanding of the facts would often preclude a defendant from admitting the SEC's allegations in the way the District Court's Order would require.

A prime example of this complexity is § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5, as promulgated thereunder. To prevail in a case under Rule 10b-5(b), the SEC must prove that a defendant (i) in connection with the purchase or sale of a security (ii) acting with scienter (iii) made a material misrepresentation (or a material omission if the defendant had a duty to speak). *VanCook v. SEC*, 653 F.3d 130, 138 (2d Cir. 2011), *cert. denied*, 132 S. Ct. 1582 (2012). Particularly in a case relating to a complex financial transaction—in which sophisticated parties often receive detailed disclosures, negotiate transaction documents, and conduct their own legal and financial due diligence—many key facts and elements

may be the subject of an intense, but good-faith, dispute between the SEC and a defendant.

For instance, to prove the materiality of information that was not disclosed by a defendant, the SEC must show “a substantial likelihood that the disclosure of [an] omitted fact would have been viewed by the reasonable investor as having significantly altered the ‘total mix’ of information made available.” *Matrixx Initiatives, Inc. v. Siracusano*, 131 S. Ct. 1309, 1318 (2011) (quoting *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988)). Even in less complex cases, materiality is a notoriously fact-intensive question on which reasonable minds may differ. See generally Dale A. Oesterle, *The Overused and Underdefined Notion of “Material” in Securities Law*, 14 U. Pa. J. Bus. L. 167, 167 (2011) (“A study of close to 800 cases in which a federal court applies the term to specific facts finds that the case-law is quixotic at best, and fickle at worst.”); Richard C. Sauer, *The Erosion of the Materiality Standard in the Enforcement of the Federal Securities Laws*, 62 Bus. Law. 317, 321 (2007) (“[T]he . . . standard is general and abstract, establishing a framework for analysis rather than a formula for deciding specific cases.”).⁴ The determination of materiality is only more

⁴ Other subsections of Rule 10b-5 are far less precise and therefore even more problematic from the perspective of an admission. Rule 10b-5(a), for example, makes it unlawful, “directly or indirectly . . . to employ any device, scheme, or artifice to defraud, . . . in connection with the purchase or sale of any security.” 17 C.F.R. § 240.10b-5(a). Given how little guidance the rule provides on what the SEC may deem to be a “device, scheme, or artifice to defraud”—especially in the context of a complex financial transaction—a good-faith admission by a defendant will often be similarly problematic.

difficult—and subject to good faith disagreement—in the context of a complicated financial transaction between sophisticated, counseled parties.

Likewise, in many cases where a settlement may otherwise be an appropriate resolution of a disputed SEC enforcement action, a defendant will strongly disagree that any relevant individual acted with the required state of mind in connection with a transaction. These are not simple assault cases, in which an individual either threw a punch or did not. Rather, many cases the SEC pursues to settlement involve good-faith disagreements over complicated core facts, as well as liability.

The facts of this case provide another illustration. The SEC has alleged that Citigroup negligently failed to make certain disclosures about its own role in the structuring and marketing of a synthetic collateralized debt obligation (“CDO”)—a debt security backed by credit default swaps that reference the performance of still another set of specific assets. (Complaint, JA-14 ¶¶ 1-6, 9.) The lengthy offering documents contained specific disclosures regarding Citigroup’s role in this complex security. (*Id.* ¶ 43.) And the ultimate purchasers of the security—the alleged victims—were sophisticated commercial participants in the financial markets with extensive investing experience and, in many cases, specific experience managing CDO transactions. (*See id.* ¶¶ 47-49.) The SEC’s allegations raise complex, fact-intensive questions about whether Citigroup’s disclosures were materially accurate and complete. Given the express disclosures in the offering materials and the level of knowledge and sophistication of the purchasers, any admission of liability—or indeed of any shortcomings in the offering disclosures—could very well conflict directly with Citigroup’s good-faith beliefs about the completeness of its disclosures. As this Court noted, the district court appears to have discounted the possibility

that, notwithstanding its decision to settle, “Citigroup perhaps did not mislead investors.” *Citigroup Per Curiam Opinion* at 163, JA-307.

In short, requiring admissions to obtain approval of settlements in complex SEC enforcement actions would in many instances unfairly force SIFMA members to choose between continuing to litigate matters with their primary regulator that they for any number of good reasons would prefer to resolve consensually, and conceding the truth of that which they strongly believe not to be true. Settlements in which defendants do not admit or deny the allegations against them offer a way to resolve good-faith disagreements—as to ambiguous facts or unclear law—between the SEC and a defendant, even in situations where a defendant believes, in good faith, that its interpretation is correct and its conduct blameless.

2. The Collateral Consequences of Admissions Would Impose Massive Costs on Settling Defendants and Their Shareholders

Even where good-faith admissions are possible, the substantial collateral consequences associated with any admission would sharply reduce the number of settled SEC enforcement actions under the approach taken by the district court.

These consequences would be most severe in the defense of the private civil litigation that inevitably accompanies any SEC enforcement action. Plaintiffs in these actions would seek to admit a settlement into evidence as a party admission under Federal Rule of Evidence 801(d)(2) or even seek to use it as the basis for collateral estoppel. In fact, the District Court’s Order specifically notes the *lack* of collateral estoppel effect of the current settlement in related private civil litigation as

a perceived shortcoming of the current settlement. *Citigroup*, 2011 U.S. Dist. LEXIS 135914, at *13-16, SPA-10-12. But the consequences of an admission of liability—or of admissions of key facts or elements of a violation—could be financially devastating for a defendant.

In modern private securities fraud class actions, the size of potential damages is astronomical because of the “fraud on the market” doctrine, which enables plaintiffs to seek damages on behalf of vast classes of allegedly injured shareholders. *See generally* William W. Bratton & Michael L. Wachter, *The Political Economy of Fraud on the Market*, 160 U. Pa. L. Rev. 69 (2011). As much as a third of the recoveries in such cases may go to lawyers, rather than investors, Denise N. Martin et al., *Recent Trends IV: What Explains Filings and Settlements in Shareholder Class Actions*, 5 Stan. J.L. Bus. & Fin. 121, 141 (1999)), and class members have “virtually no say in the conduct of the lawsuit or the terms of any settlement,” Patrick M. Garry et al., *The Irrationality of Shareholder Class Action Lawsuits: A Proposal for Reform*, 49 S.D. L. Rev. 275, 277 (2004).

Those financial consequences are borne directly by the defendant corporation’s shareholders. “[B]ecause the costs of securities class actions—both the settlement payments and the litigation expenses of both sides—fall largely on the defendant corporation, its shareholders ultimately bear these costs indirectly and often inequitably.” John C. Coffee, Jr., *Litigation Reform Since the PSLRA: A Ten-Year Retrospective*, 106 Colum. L. Rev. 1534, 1536 (2006); *see also* Garry, *supra*, at 278 (“Since any settlement basically comes out of the shareholders’ own assets, accompanied by an extremely high transaction price in the form of lawyers’ fees, the lawsuit can actually yield a net negative return to the class members.”).

Indeed, even where liability is not admitted, admissions of even discrete underlying facts in an SEC consent order can have negative consequences in private litigation. For example, statements made by another financial institution in a recent SEC consent settlement—noted in the District Court’s Order, *see Citigroup*, 2011 U.S. Dist. LEXIS 135914, at *17 n.7, SPA-13—as a condition of settling have featured prominently in a number of private civil complaints, as well as in at least one court’s decision denying the defendant’s motion to dismiss. *ACA Fin. Guar. Corp. v. Goldman Sachs & Co.*, No. 6500027/11, 2012 N.Y. Misc. LEXIS 1940, at *15, 22-23, 32 (N.Y. Sup. Ct. Apr. 23, 2012).

The negative impact of consent orders in subsequent private litigation would only be magnified were admissions required. Under those circumstances, defendants would rarely be willing to settle, leading to significant expense litigating complex financial cases, a cost that would be borne primarily by shareholders and investors, *see Coffee, supra*, at 1536—precisely the constituency the SEC is charged with protecting.

In addition, admissions would pose severe reputational consequences. Clients of SIFMA members, and investors more generally, are appropriately sensitive to violations of the securities laws committed by their service providers. The inability or disinclination of prospective clients—including municipal and foreign governmental entities—to award opportunities to financial institutions that have admitted allegations in an SEC enforcement action could disadvantage those institutions by limiting available investment alternatives. For example, many institutional investors require that a request for proposal questionnaire be completed prior to awarding business to an investment firm. An admission could disqualify or severely prejudice

a firm from being awarded future business. An admission of liability would also trigger a range of potential disqualifications that would directly threaten the ability of broker-dealers and investment advisers to do their work.⁵ Here too, the collateral consequences would directly impact the institution's shareholders.

Collectively, these various collateral consequences would in many cases foreclose the possibility of settlement altogether. See *Examining the Settlement Practices of U.S. Financial Regulators: Hearing Before the H. Comm. on Fin. Servs.*, 112th Cong. 40-42 (May 17, 2012) (Testimony of Robert Khuzami, Director, Division of Enforcement, SEC; Scott Alvarez, General Counsel, Board of Governors, Federal Reserve; Richard Osterman, Jr., Deputy General Counsel, Litigation and Resolutions Branch, FDIC) (uniformly testifying that mandating that settlements include admissions of wrongdoing would significantly decrease the number of settlements agencies could obtain, resulting in harm to investors and the

⁵ Absent a multitude of necessary waivers, an admission of liability can trigger a broad spectrum of disqualifications, including under: (i) the Securities Exchange Act of 1934, 15 U.S.C. § 78C(a)(39)(F); (ii) FINRA membership requirements, FINRA Bylaws art. III, § 3; (iii) NASDAQ's listing requirements, NASDAQ Market Rule 1002(b); (iv) the Uniform Securities Act, Unif. Sec. Act § 204(a) (Nat'l Conference on Unif. State Laws 2002); (v) the Investment Advisers Act of 1940, 15 U.S.C. § 80b-3(e)(4)-(5); (vi) the Commodity Exchange Act, 7 U.S.C. §§ 12a(2)(C), 12a(2)(E); (vii) the membership requirements of the National Futures Association, Nat'l Futures Ass'n Bylaws § 301; and (viii) the Investment Company Act of 1940, 15 U.S.C. § 80a-9(a)(2).

financial system); *Harvey Goldschmid: Securities and Exchange Commission*, Compliance Rep., Aug. 10, 2003 (“If we tried to force admissions . . . the settlement process would grind to a halt. We can’t afford that in terms of national policy in terms of the deterrence and accountability we need.”); *Clifton*, 700 F.2d at 748 (identifying the avoidance of harsh collateral consequences as one of the major reasons for settlement in SEC cases); *cf. Citigroup Per Curiam Opinion* at 163, JA-307 (“Citigroup might well not consent to settle on a basis that requires it to admit liability . . .”).

B. Reducing the SEC’s Discretionary Ability to Enter into Consent Settlements with Financial Institutions Would Harm All Participants in the Securities Industry.

The entire securities industry would suffer if the SEC’s discretion to settle cases were curtailed substantially. The staggering costs of complex litigation and the stock price decline caused by the uncertainty of protracted actions are ultimately borne by a defendant’s shareholders. Similarly, all investors would suffer if the SEC were limited in its ability to collect sanctions and achieve reforms in settled cases.

Litigation is extremely expensive for all parties, particularly in complex cases involving ambiguous facts and law. *See* Lawyers for Civil Justice et al., *Litigation Cost Survey of Major Companies 2* (2010) (finding average litigation costs, exclusive of judgments and settlements, of \$115 million per year for Fortune 200 companies responding to survey). Full-blown litigation with a primary regulator in particular poses a host of unique risks beyond those associated with ordinary civil litigation. Litigation is also an inefficient use of company resources that could be spent on revenue-generating

activities for the benefit of shareholders, SEC resources that could be used to pursue other enforcement actions, and finite judicial resources. *See SEC v. Everest Mgmt. Corp.*, 475 F.2d 1236, 1240 (2d Cir. 1972) (“The SEC can bring the large number of enforcement actions it does only because in all but a few cases consent decrees are entered.”); *Clifton*, 700 F.2d at 748 (noting that consent judgments allow the SEC to “conserve its own and judicial resources”). A rule that limited parties’ ability to enter into non-admission-based settlements would result in more contested proceedings and considerably greater litigation costs.

Moreover, the capital markets respond negatively to regulatory overhang and punish companies and their shareholders for the uncertainty associated with contested regulatory proceedings. For example, Goldman Sachs & Co.’s share price dropped in the wake of the SEC’s filing of its action on April 16, 2010 against Goldman relating to a single CDO transaction, and that action no doubt created investor concerns until it was resolved. As illustrated by this example, SIFMA members (as well as their shareholders and investors) can be expected to suffer as much from the uncertainty surrounding litigation with the SEC as they would from actual adverse resolutions. *See Kevin C. Brown et al., Risk Aversion, Uncertain Information, and Market Efficiency*, 22 J. Fin. Econ. 355, 356 (1988) (finding that uncertainty surrounding unfavorable news “causes a market comprising risk-averse investors to set stock prices significantly below their conditional expected values”).

A sophisticated private party’s decision to minimize and mitigate such costs and risks by entering into a negotiated consent settlement should not be subject to judicial second-guessing. In this way, the district court’s asserted concerns for Citigroup’s interests were

misplaced. As this Court has already recognized, it is doubtful that “it is a proper part of [a] court’s legitimate concern to protect a private, sophisticated, counseled litigant from a settlement to which it freely consents.” *Citigroup Per Curiam Opinion* at 165, JA-310. Financial institutions regulated by the SEC routinely make pragmatic determinations regarding settlement in cases involving the prospect of expensive and distracting litigation over uncertain law and facts; courts are poorly situated to second guess such analysis, let alone to rewrite the terms of the parties’ agreements. *See United States v. Akzo Coatings of Am. Inc.*, 949 F.2d 1409, 1436 (6th Cir. 1991) (in evaluating a consent decree “it is not our function to determine whether [it] is the best possible settlement that could have been obtained”); *United States v. Cannons Eng’g Corp.*, 899 F.2d 79, 84 (1st Cir. 1990) (“[T]he relevant standard, after all, is not whether the settlement is one which the court itself might have fashioned, or considers as ideal . . .”).

Similarly, in deciding whether, and on what terms, to settle, the SEC must gauge the strength of its own case, its policy priorities, and the most efficient use of its limited resources. “[T]he agency must not only assess whether a violation has occurred, but whether agency resources are best spent on this violation or another, whether the agency is likely to succeed if it acts, whether the particular enforcement action requested best fits the agency’s overall policies, and, indeed, whether the agency has enough resources to undertake the action at all.” *Heckler v. Chaney*, 470 U.S. 821, 831-32 (1985). As this Court has recognized, these are “legitimate policy choices” that are vested by the Constitution in the Executive Branch and the responsibilities for assessing their wisdom and “resolving the struggle between competing views of the public interest are not judicial ones.” *Citigroup Per Curiam Opinion* at 163-64, JA-308 (citing *Chevron*,

U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 866 (1984)).

All participants in the financial industry, including investors, would be negatively impacted by a regime that limited the SEC's ability to enter into settlements that do not include admissions. Such settlements afford the SEC flexibility to enter into settlements that apply consistent policy determinations, that are informed by the agency's knowledge of industry practice, and that maximize its investigatory and enforcement resources. *See SEC v. Randolph*, 736 F.2d 525, 530 (9th Cir. 1984) (noting that the initial determination of whether a consent decree is in the public interest "is best left to the SEC and its decision deserves our deference"); *Clifton*, 700 F.2d at 748 ("We are reluctant to upset this balance of advantages and disadvantages . . .").

Moreover, it is safe to assume that—in a world where admissions were a settlement prerequisite—the SEC would be unable to pursue as many cases because it would need to devote more of its limited budget to litigating actions to judgment. In this way, the SEC would be forced to expend resources unnecessarily by litigating to uncertain result many cases where injunctive and other substantial relief could have been achieved through settlement. And even if the SEC were to prevail in each of the cases it did litigate, it would still entirely forego the monetary damages and remedial measures that it could have recovered through settlement in cases that it simply would not have time and resources to litigate to judgment.⁶

⁶ The ability of the SEC to proceed administratively does not obviate the problems caused by the district court's approach to settlement. A defendant cannot select the forum in which the SEC chooses to bring an

II. The Current Approach to Settlement Benefits the Securities Industry, the SEC, and Investors

A. The Current Approach to Settlement Promotes Self-Reporting, Cooperation, and Effective Remedial Measures.

As it has made clear in many contexts, the SEC gives credit in the settlement process to entities that cooperate with its investigations and that self-report.⁷ The prospect of settlement without admissions and the attendant collateral consequences thus promotes an early and open exchange of information with the SEC. The resulting culture of cooperation benefits all participants in the securities industry by permitting the SEC to operate more efficiently and by encouraging disclosure of actual or potential wrongdoing at the time it is first discovered. *See* SEC Enforcement Manual, *supra*, § 6.1.1 (“Cooperation by individuals and entities in the Commission’s investigations and related enforcement actions can contribute significantly to the success of the agency’s mission.”) (quoting 17 C.F.R. § 202.12).

In addition, settlements under the current regime—particularly with SIFMA’s members, who are regulated entities and have an ongoing relationship with the SEC—

enforcement action. In cases where the SEC chooses to litigate in federal court, the District Court’s Order effectively eliminates the possibility of a settlement because few defendants would willingly expose themselves to the catastrophic collateral consequences associated with admissions.

⁷ For example, the SEC’s Enforcement Manual contains guidelines for crediting cooperation by individuals and companies. *See* Enforcement Manual, SEC Div. of Enforcement §§ 6.1.1, 6.1.2 (Mar. 9, 2012).

often include substantial agreed-upon remedial measures and other changes designed to enhance future compliance. These measures benefit SIFMA members, their clients, and the investing public. In this case, for example, Citigroup agreed to enhancements in its review of offering documents and marketing materials prepared in connection with residential mortgage-related securities, as well as other measures, including expanded legal and compliance review, scrutiny by outside counsel, periodic audits, and certification requirements. (Citigroup Consent, JA-46–47) A system that discouraged settlements would forego opportunities for such agreed-upon remedial measures.

B. The Current Approach to Settlement Leads to Substantial Penalties and Deters Future Violations.

SEC settlements—notwithstanding the absence of admissions—have significant deterrent effects. In addition to substantial monetary penalties, considerable deterrence flows from negative publicity. *See, e.g., Clifton*, 700 F.2d at 748 (noting that consent judgments help the SEC to “protect the public by informing potential investors that a certain person has violated SEC rules in the past and by reminding defendants that they must obey the law in the future”). That publicity is particularly potent in light of the requirement that defendants not deny the alleged conduct.

In fact, the initiation of an SEC investigation alone has significant negative consequences for SIFMA’s members. One academic study found “measurable and significant *indirect* penalties on underwriters and their clients” following the announcement of an SEC investigation.⁸

⁸ The indirect penalties identified by the study included (1) the average share of the IPO market held by

Randolph P. Beatty et al., *The indirect economic penalties in SEC investigations of underwriters*, 50 J. Fin. Econ. 151, 177 (1998) (emphasis in original); *see also* Mahmoud M. Nourayi, *Stock Price Responses to the SEC's Enforcement Actions*, 13 J. Acct. & Pub. Pol'y 333 (1994) (measuring the negative impact of the announcement of an SEC enforcement action on stock prices). The prospect of settlement by no means eliminates this harm (which is concededly more modest and proportionate than the punitive stock price reaction to the filing of an SEC complaint after initiation of an investigation against a financial institution, *see* p. 14, *supra*), and its deterrent impact is entirely independent of the settlement process.

SEC settlements typically enjoin defendants from future violations of the securities laws, which also serves a significant deterrent function.

Once [a] Court has enjoined a defendant from future violations of the securities laws, the S.E.C., if it has evidence of a subsequent violation, can move summarily to have the Court

the targeted underwriter declined by at least 50% in the year immediately after the SEC investigation was made public; (2) the number of trading days between registration and offer dates of IPOs on which a targeted underwriter was the lead underwriter increased because of increased regulatory scrutiny; (3) the client's daily stock returns were substantially more volatile; (4) the stock prices of rival underwriters declined (because the SEC's investigation signaled less than favorable industry-wide profits); and (5) the equity value of the underwriter's past and current clients decreased (because of an association between the reputation of an underwriter and its clients). Beatty, *supra*, at 152-53.

hold the defendant in contempt, following an expedited hearing, rather than having to go through the laborious process of filing a civil complaint, undergoing full discovery and motion practice, and trying the case to a jury.

Randolph, 736 F.2d at 528 (internal quotation omitted); *accord Universal City Studios, Inc. v. N.Y. Broadway Int'l Corp.*, 705 F.2d 94, 96 (2d Cir. 1983).

The SEC, as the primary regulator of financial institutions, is in a position to enforce injunctions against them. Beyond serving as a basis for contempt sanctions, those injunctions impact future regulatory determinations and enforcement actions. (*See, e.g.*, SEC Mem. in Response to Questions Posed by Ct., JA-99) (explaining that the existence of prior enforcement actions is a factor in determining an appropriate monetary penalty) (citing *Statement of the Securities and Exchange Commission Concerning Financial Penalties*, SEC Release No. 2006-4 (Jan. 4, 2006)).) Neither admit nor deny settlements also have collateral estoppel effect in future SEC proceedings. *See In re Marshall E. Melton*, Investment Advisers Act Release No. 2151, Securities Exchange Act Release No. 48228, 56 S.E.C. 695, 711-12 (July 25, 2003).

C. The Current Approach to Settlement Effectively Compensates Injured Investors.

SEC Fair Funds provide substantial recovery for investors (and generally do so far more quickly than private litigation). Moreover, unlike private class actions, no portion is used to compensate lawyers. *See Verity Winship, Fair Funds and the SEC's Compensation of Injured Investors*, 60 Fla. L. Rev. 1103, 1132 (2008) ("One rationale for the Fair Fund provision was that it avoided attorney's fees."). Monetary recovery in SEC settlements is significant, approaching the limits of what

could be obtained in any successful litigation.⁹ In this case, for example, \$285 million would be returned to investors. *See* Press Release, SEC, *SEC Enforcement Director's Statement on Citigroup Case* (Dec. 15, 2011), <http://www.sec.gov/news/press/2011/2011-265.htm> (“The \$285 million obtained from Citigroup under the proposed settlement, while less than investor losses, represents most of the total monetary recovery that the SEC itself could have sought at trial.”). Moreover—as is always the case—the “SEC settlement does not limit the ability of injured investors to pursue claims for additional relief.” *Id.* To the contrary, SEC settlements often greatly strengthen the bargaining position of private plaintiffs in related cases. *See* Ellen M. Ryan & Laura E. Simmons, *Securities Class Action Settlements: 2011 Review and Analysis* 14 (2012) (noting that “[c]ases that involve SEC actions are associated with significantly higher settlements” in private litigation, even when controlling for other variables).

D. The Current Approach to Settlement Allows the SEC to Deploy its Limited Resources Efficiently and to Provide Certainty in a Wide Array of Cases.

The availability of consent judgments allows the SEC to efficiently deploy its limited resources. *See generally Everest Mgmt. Corp.*, 475 F.2d at 1240; *Randolph*, 736 F.2d at 529-30; *Clifton*, 700 F.2d at 748. Settlements also

⁹ In 2011, the division filed 735 enforcement actions, producing \$2.8 billion in penalties and money returned to investors. Liz Skinner, *Juggling budget constraints, more-aggressive enforcement*; Robert S. Khuzami, Investment News, Dec. 19, 2011, at 18. Since 2002, there have been ten settlements in excess of \$300 million. NERA Report at 4.

allow the SEC to implement consistent policies across multiple jurisdictions and with respect to different entities. All participants in the securities industry benefit from this consistency.¹⁰

Agreed-upon settlements have the benefit of providing clarity about the SEC's position on important and evolving issues sooner than contested proceedings, which may extend for years. *See Hearing Before the H. Comm. on Fin. Servs., supra*, at 19 (Testimony of Robert Khuzami, Director, Division of Enforcement, SEC) (estimating that the average time between the initiation of an SEC investigation and a consent settlement is between one and three years, whereas litigated cases typically take an additional two to four years from filing through trial). SIFMA members, who interface with the SEC on a daily basis across a range of complex areas, benefit from the resulting knowledge of the SEC's views and priorities. The SEC, in turn, benefits from more informed regulated entities, as does the investing public generally.

¹⁰ The undertakings in the proposed consent judgment against Citigroup mirror closely undertakings in the consent decrees entered in *SEC v. Goldman Sachs & Co.*, No. 10-cv-3229 (S.D.N.Y. July 20, 2010), and in *SEC v. J.P. Morgan Sec., LLC*, No. 11-cv-4206 (S.D.N.Y. June 29, 2011).

CONCLUSION

For the foregoing reasons, the District Court's Order refusing to approve the proposed final judgment and consent between the SEC and Citigroup should be reversed.

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Respectfully Submitted,

/s/ Edmund Polubinski III
Annette L. Nazareth
Edmund Polubinski III
Gina Caruso
DAVIS POLK & WARDWELL LLP
450 Lexington Avenue
New York, New York 10017
(212) 450-4000
*Counsel for Amicus Curiae
Securities Industry and Financial
Markets Association*

Of Counsel:

Ira D. Hammerman
Kevin M. Carroll
SECURITIES INDUSTRY AND
FINANCIAL MARKETS
ASSOCIATION
1101 New York Avenue, NW
Washington, D.C. 20005

CERTIFICATE OF COMPLIANCE

Pursuant to Rule 32(a)(7)(C) of the Federal Rules of Appellate Procedure, the undersigned counsel for amicus curiae SIFMA hereby certifies that this brief complies with the type-volume limitations of Rule 32(a)(7)(B). As measured by the word-processing system used to prepare this brief, there are 5,913 words in the brief.

By: /s/ Edmund Polubinski III
Edmund Polubinski III