
**IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT**

SECURITIES AND EXCHANGE COMMISSION
Plaintiffs – Appellants

v.

DOUGLAS J. BARTEK AND NANCY A. RICHARDSON
Defendants - Appellees

***AMICUS CURIAE* BRIEF OF THE SECURITIES INDUSTRY
AND FINANCIAL MARKETS ASSOCIATION IN SUPPORT OF
APPELLEES**

On Appeal From The United States District Court
For The Northern District of Texas
(Dallas Division) In Case No. 3:08-CV-1105-B

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**CERTIFICATE OF INTERESTED PERSONS
UNDER FIFTH CIRCUIT RULE 28.2.1**

The Securities Industry and Financial Markets Association is an industry association that brings together the shared interests of hundreds of securities firms, banks, and asset managers with the goal of supporting a strong financial industry that promotes job creation and economic growth. Per Rule 28.2.1 of the Fifth Circuit Rules, undersigned counsel of record lists the following interested persons and is unaware of any additional parties, persons, or entities whose interests in these appeals must be disclosed:

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INTEREST OF THE SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION AS *AMICUS CURIAE*

As an association comprised of hundreds of member securities firms, banks and asset managers, the Securities Industry and Financial Markets Association (“SIFMA”)¹ has an interest in the strong, accurate, and timely enforcement of the federal securities laws. SIFMA also has an interest in repose – the principle that there comes a time after which even a party accused of violating the securities laws is free from the risk of stale claims. Those interests are served when the Securities and Exchange Commission (“SEC”) brings timely claims and when, if the parties are not able to resolve those claims, they can be adjudicated based on evidence that is fresh. They are also served by clear rules that tell corporations and other entities how long they must retain documents and information that may have evidentiary value and when they are entitled to repose for acts that were committed long in the past. Those interests are furthered by the plain language of Section 2462 of Title 28, which requires the government to bring penalty actions within five years of when the claim first accrued.

SIFMA regularly files *amicus curiae* briefs in cases that raise legal

¹ SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA’s mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

issues of particular importance to the participants in the securities industry.² The position of the SEC in this case – that a “discovery rule” applies to all claims sounding in fraud – is of particular importance. If adopted, it would undermine those principles that undergird the effective and efficient functioning of the securities markets: It would potentially permit the SEC to bring an ancient claim on the mere allegation that it could not have discovered the existence of the claim earlier and thus free the SEC from the main constraint that requires all litigants to bring timely claims. It would place market participants in perpetual peril of charges based on conduct that took place years (even decades) ago. Further, it would compromise the accurate and efficient adjudication of claims of federal securities law violations. The document retention regulations that govern all participants in the securities markets assume there comes a time when even records that might relate to a potential violation in the past need not be retained. Under the rule the SEC urges, it would potentially have the right to bring a claim long after those records are no longer in existence and despite the absence of any prior notice.

SIFMA takes no position on any of the factual allegations here or on whether, if timely, any violations have occurred or any penalty is appropriate. However, SIFMA does strongly believe that statutes of limitations are critical to

² SIFMA hereby certifies that no counsel for a party authored this brief in whole or in part; that no party or counsel for a party contributed money that was intended to fund preparation or submission of this brief; and that no person other than the *amicus curiae*, its members, and its counsel, contributed money that was intended to fund preparation or submission of this brief.

protect interests in repose and in freedom from defending against ancient claims and that the SEC's position here is inconsistent with those fundamental principles.³

PRELIMINARY STATEMENT

For the over 150 years that Section 2462 and its predecessors have been in existence, all federal agencies that seek to bring a penalty claim have been subject to a clear rule: unless the defendant has engaged in conduct to conceal his own wrongdoing and thus to frustrate the bringing of a timely claim, or unless Congress provides otherwise, the agency must bring a penalty claim within five years of when the violation occurred and the agency first had a legal right to sue.

The SEC's proposed rule would overturn that clear rule and the principles of repose that it furthers. Under that approach, even when a defendant has not engaged in concealing conduct and equitable tolling does not apply, the SEC would potentially be able to bring an ancient claim on the mere allegation that it did not discover and could not have discovered the violation earlier. That rule would eviscerate the statute of limitations at least as applied to claims sounding in fraud. If adopted, a federal agency could bring, and sustain, a penalty action for ancient, wholly unconcealed, conduct on the sole basis that it chose not to pursue an investigation earlier, unless the defendant makes the showing by a

³ Pursuant to Federal Rule of Appellate Procedure 29(a), all parties have consented to the filing of this amicus brief. The SEC has consented on the condition amicus consent that it be given thirty days to file its reply to Appellees' response briefs. SIFMA has no objection to the requested extension.

preponderance of the evidence that the agency knew or should have known of the violation earlier. Such a showing could not easily be made on the pleadings and would be virtually impossible to make in practice, even after the destruction of a defendant's reputation and the expenditure of substantial legal fees.

The SEC's proposed rule improperly seeks to import into a government enforcement setting a legislative rule designed for damages claims by tort victims. It is contradicted by the plain language of Section 2462 and its structure, is inconsistent with over a century of decisions interpreting Section 2462 and its predecessors, violates the vital purposes of statutes of limitations in penalty actions brought by the government, and would lead to pernicious results.

ARGUMENT

I. THE PLAIN LANGUAGE AND STRUCTURE OF SECTION 2462 REQUIRE PENALTY ACTIONS TO BE BROUGHT WITHIN FIVE YEARS OF WHEN THE CLAIM FIRST AROSE

SIFMA joins in and adopts Appellees' statutory interpretation. Section 2462 of Title 28 states in plain language that: "Except as otherwise provided by Act of Congress, an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued" 28 U.S.C. § 2462 (emphases added). The Supreme Court and other courts long have held that "[i]n common parlance a right accrues when it comes

into existence,” that is, when the plaintiff first has the legal right to bring suit. United States v. Lindsay, 346 U.S. 568, 569 (1954).⁴ No Act of Congress has “otherwise provided” or adopted a discovery rule for SEC enforcement actions. Accordingly, the SEC must bring a penalty claim within five years of when the violation “first” occurred. It is not up to the courts to provide a different rule.

When Congress has intended a discovery rule to apply, it has said so, including in the federal securities laws themselves.⁵ It could have added a

⁴ This settled definition accords with that of numerous current and nineteenth century dictionaries. See, e.g., BLACK’S LAW DICTIONARY 23 (9th ed. 2009) (defining accrue to mean “to come into existence as an enforceable claim or right; to arise”); THE AMERICAN HERITAGE DICTIONARY 12 (3d ed. 1994) (defining accrue as “[t]o come into existence as a claim that is legally enforceable”); Merriam-Webster.com, available at <http://www.merriam-webster.com> (Aug. 7, 2011) (defining accrue as “[t]o come into existence as a legally enforceable claim”); 1 BOUBIER’S LAW DICTIONARY 66 (1897) (defining accrue as “[t]o arise, to happen, to come to pass; as the statute of limitation does not commence running until the cause of action has accrued.”); 1 AMERICAN AND ENGLISH ENCYCLOPAEDIA OF LAW 142 (1886) (stating that a “[c]ause of Action shall accrue or shall have accrued. . . . whenever the defendant’s liability became perfect and complete.”). It also was well accepted by courts in the Nineteenth Century when the first predecessor statute to Section 2462 was enacted. See Meredith v. United States, 38 U.S. (13 Pet.) 486, 493-94 (1839) (duties accrue to government at time when goods arrive at their port of entry, not when government knows they are there); Bank of the U.S. v. Daniel, 37 U.S. (12 Pet.) 32, 56 (1838) (“cause of action to recover the money, (had it been well founded) accrued at the time the mistaken payment was made”); Evans v. Gee, 36 U.S. (11 Pet.) 80, 84 (1837) (“A refusal to accept [a good in exchange for payment] is, then, a breach of the contract, upon the happening of which, a right of action instantly accrues to the payee.”); Wilcox v. Plummer, 29 U.S. (4 Pet.) 172, 181 (1830) (holding that claim accrues at the moment a violation occurs).

⁵ See 15 U.S.C. § 78r(c); 15 U.S.C. § 77www; 28 U.S.C. § 1658(b); 15 U.S.C. § 77m; 15 U.S.C. § 78i(f). See also Federal Trade Commission Act, 15 U.S.C. § 1679i (action by the government “to enforce any liability under this subchapter may be brought before the later of . . . the end of the 5-year period beginning on the date of the occurrence of the violation involved; or . . . the end of the 5-year period beginning on the date of the discovery by the consumer of the misrepresentation.”); False Claims Act, 31 U.S.C. § 3731(b) (explaining that an FCA suit must be brought within six years of the date from which the fraudulent act occurred, or within three years of the date when the government official, responsible to act, knew or reasonably should

discovery rule to either Section 2462 or the underlying statute the SEC seeks to enforce, but did not. The courts thus are not free to do so by implication.⁶

II. THE SEC’S ARGUMENT IS INCONSISTENT WITH SECTION 2462’S HISTORY AND APPLICATION IN CASE LAW

The long line of cases, including from this Court, holding that the term “first accrued” in Section 2462 means the earliest date on which the plaintiff agency could sue, see Brief for Appellee Nancy A. Richardson at 29-33 (citing, e.g., United States v. Core Labs, Inc., 759 F.2d 480, 482 (5th Cir. 1985)),⁷ is further compelling evidence that Congress did not intend to import a discovery rule

have known the claim was false and that the suit must be within 10 years after the date of occurrence.). Indeed, when Congress included a discovery rule it was careful to emphasize the difference between “accrual” of the claim and “discovery” for purposes of a discovery rule. See, e.g., Federal Deposit Insurance Corporation Improvement Act of 1991, 12 U.S.C. § 1817(g); Federal Food, Drug and Cosmetic Act, 21 U.S.C. § 335b(b)(3).

⁶ See Cent. Bank v. First Interstate Bank, 511 U.S. 164 (1994).

⁷ See also 3M Co. v. Browner, 17 F.3d 1453, 1461-63 (D.C. Cir. 1994) (outlining history of cases interpreting “accrual” under Section 2462 and its predecessors and noting not a single case imported a discovery of violation rule); United States v. Athlone Indus., Inc., 746 F.2d 977, 982 n.1 (3d Cir. 1984); W. Pac. Fisheries, Inc. v. S.S. President Grant, 730 F.2d 1280, 1287 (9th Cir. 1984); United States v. Ancorp Nat’l Servs., Inc., 516 F.2d 198, 201 n.5 (2d Cir. 1975); United States v. Witherspoon, 211 F.2d 858, 861 (6th Cir. 1954); Smith v. United States, 143 F.2d 228, 229 (9th Cir. 1944) (construing predecessor statute), cert. denied, 323 U.S. 729 (1944); Lancashire Shipping Co. v. Durning, 98 F.2d 751 (2d Cir. 1938) (same), cert. denied, 305 U.S. 635 (1938); The Ng Ka Py Cases, 24 F.2d 772, 774 (9th Cir. 1928) (same); see also Fed. Election Comm’n v. Williams, 104 F.3d 237, 240 (9th Cir. 1996), cert. denied, 522 U.S. 1015 (1997); United States v. Maillard, 26 F. Cas. 1140, 1143 (S.D.N.Y. 1871) (construing predecessor statute and holding “[the claim] did so accrue, as against the defendants in this case, when the offenses alleged were committed [I]gnorance does not prevent the running of the statute or the accruing of the forfeiture.”).

into Section 2462.⁸

The SEC relies primarily on a single Supreme Court case to support its argument, but that case (Bailey v. Glover, 88 U.S. 342 (1874)) not only involves a different statute than Section 2462 but also a fundamentally different concept. In Bailey, the Supreme Court held that, where a defendant engages in deliberate concealment to prevent the discovery of a claim during the otherwise applicable statute of limitations, she is equitably estopped from invoking a statute of limitations defense:

[W]e hold that when there has been no negligence or laches on the part of a plaintiff in coming to the knowledge of the fraud which is the foundation of the suit, and when the fraud has been concealed, or is of such character as to conceal itself, the statute does not begin to run until the fraud is discovered by, or becomes known to, the party suing, or those in privity with him.

88 U.S. at 349-50 (emphasis added). The case thus stands for the familiar proposition, read into a number of different statutes, that a defendant who through her conduct intentionally frustrates the ability of the plaintiff to sue within the statute of limitations cannot then invoke the statute of limitations.⁹

⁸ See Herman & MacLean v. Huddleston, 459 U.S. 375, 385-56 (1983). SEC v. Gabelli, 653 F.3d 49 (2d Cir. 2011), is the first appellate case ever to unambiguously embrace the “discovery rule,” but the cases it relied on, as prior Second Circuit precedent explained, were equitable tolling cases, not discovery cases. See Cerbone v. Int’l Ladies’ Garment Workers’ Union, 768 F.2d 45, 48 (2d Cir. 1985) (interpreting Bailey v. Glover to explain that “[t]he doctrine of equitable tolling of a statute of limitations was developed in the context of actions based on fraud.”); Long v. Abbott Mortg. Corp., 459 F. Supp. 108, 113 (D. Conn. 1978) (same).

⁹ Id. at 349 (“To hold that by concealing a fraud, or by committing a fraud in a manner that it concealed itself until such time as the party committing the fraud could plead the statute of

The SEC's proposed rule, however, by definition, applies in those cases where the SEC is unable to prove equitable tolling, i.e., when the defendant through his own conduct has not frustrated the ability of the SEC to bring a timely suit. It would permit the SEC to bring an untimely claim not based on some inequitable conduct by the defendant but based on the SEC's own avowed failure or inability with reasonable diligence to discover the violation earlier. It thus involves a fundamentally different concept than equitable tolling and one singularly inappropriate to the government enforcement context. In latent tort and certain other civil cases where injuries are difficult to detect and damages or other remedial relief are an element of the claim, some courts and legislatures have suspended the accrual of a claim until the date harm has been felt on the theory "that plaintiffs cannot have a tenable claim for the recovery of damages unless and until they have been harmed." 3M Co. v. Browner, 17 F.3d 1463, 1460 (D.C. Cir. 1994) (emphasis added); see also William A. Graham Co. v. Haughey, No. 10-2762, 2011 WL 1833238, at *10 (3d Cir. May 16, 2011).

limitations to protect it, is to make the law which was designed to prevent fraud the means by which it is made successful and secure"). It is thus similar to other equitable doctrines the courts have adopted to preclude a party who has frustrated the operation of a statute from enjoying its benefit. See, e.g., Nen Di Wu v. Holder, 617 F.3d 97, 100 (2d Cir. 2010) (fugitive disentitlement doctrine); Pinter v. Dahl, 486 U.S. 622, 632 (1998) ("[t]he equitable defense of in pari delicto"); see also Precision Instrument Mfg. Co. v. Auto. Maint. Mach. Co., 324 U.S. 806, 814 (1945) (The unclean hands doctrine "closes the door of a court of equity to one tainted with inequity or bad faith relative to the matter in which he seeks relief, however improper may have been the behavior of the defendant.").

The discovery rule has “nothing whatever to do” with penalty claims where the government sues not as tort victim but as law enforcer. Injuries or damages resulting from a violation are not an element of an SEC enforcement action and the SEC need not wait until it has experienced harm (or anyone has experienced harm) before it brings suit. 3M, 17 F.3d at 1460 (“[I]njuries or damages resulting from the violation are not part of [a punitive] cause of action.”). There is thus no warrant to judicially import a discovery rule into Section 2462.

III. THE SEC’S PROPOSED RULE WOULD VIOLATE THE CORE OBJECTIVES OF STATUTES OF LIMITATIONS AND PERIODS OF REPOSE IN GOVERNMENT PENALTY ACTIONS

This Court has aptly held that there comes a time when “the right to be free of stale [government enforcement] claims, ... prevail[s] over the right to prosecute them.” Core Labs, Inc., 759 F.2d at 483; see also 3M, 17 F.3d at 1457. That notion is fundamental to a free society. As Chief Justice Marshall observed long ago, the concept that there would in effect be no limitations period for a penalty action “would be utterly repugnant to the genius of our laws ... where not even treason can be prosecuted after a lapse of three years.” Adams v. Woods, 6 U.S. (2 Cranch) 336, 342 (1805) (Marshall, C.J.); accord U.S. v. Mayo, 26 F. Cas. 1230, 1231 (C.C.D. Mass. 1813) (No. 15755) (Story J.) (“it would be utterly repugnant to the genius of our laws, to allow such prosecutions a perpetuity of existence”).

The SEC's position would, for the first time, reverse that ordinary presumption and undermine the core principles of statutes of limitations. It "would leave the statute open for that portion of eternity concurrent with the [defendant's] life, whether he lives three score and ten or as long as Methuselah." Core Labs, 759 F.2d at 483 n.2 (internal quotations and citation omitted). Statutes of limitations, including Section 2462, are designed to protect a defendant from having to defend against a claim after "evidence has been lost, memories have faded, and witnesses have disappeared." See Order of R.R. Telegraphers v. Ry. Express Agency, 321 U.S. 342, 349 (1944) (explaining that to defend a stale penalty claim is in conflict with core legal principles). This protection would disappear under the SEC's proposed rule where claims could theoretically be brought – and would need to be defended – regardless of how ancient the evidence so long as the government could show (at summary judgment or trial) that it did not know of the evidence earlier.

These principles are especially important in the enforcement context where the agency seeks not to recover damages for injuries it has suffered but to impose punishment for conduct it views as unlawful. "[S]ome of the policies promoted by statutes of limitation," such as assuring accurate decisions and providing repose, "loom even larger in the criminal context than they do in the civil context." Andrew J. Wistrich, Procrastination, Deadlines, and Statutes of

Limitation, 50 WM. & MARY L. REV. 607, 664 (2008); see also Yair Listokin, Efficient Time Bars: A New Rationale for the Existence of Statutes of Limitations in Criminal Law, 31 J. LEGAL STUD. 99, 99 (2002). This type of coercive power by the state (with limited exceptions for murder and other egregious offenses) has always been subject to statutes of limitations.¹⁰

A defendant who personally has concealed his wrongdoing to prevent a claim from being timely brought can hardly complain when – after her concealment has ceased to be effective – the claim is brought. She has effectively forfeited her right to rely on the statute of limitations and cannot justifiably complain that she is being subjected to stale claims: the delay is of her own manufacture. Here, however, the SEC does not claim that Appellees concealed their misconduct, but solely that it could not have discovered the violation earlier. The Appellees have not forfeited their right to invoke the statute. “An agency may experience problems in detecting statutory violations because its enforcement effort is not sufficiently funded; or because the agency has not devoted an adequate

¹⁰ See Wistrich, 50 WM. & MARY L. REV. at 610. Beyond the accepted principle of fairness animating repose, the government’s ability to generally and specifically deter wrongdoing dissipates as time passes and the risk of ineffective, or worse arbitrary or vindictive, exercise of governmental power increases. Tyler Ochoa & Andrew Wistrich, The Puzzling Purposes of Statutes of Limitation, 28 PAC. L.J. 453, 471-82 (1997) (Statutes of limitations help reduce litigation costs and assure accurate decisions by taking account of the deterioration of evidence over time.); see also Michael J. Kaufman & John M. Wunderlich, Toward a Just Measure of Repose: The Statute of Limitations for Securities Fraud, 52 WM. & MARY L. REV. 1547, 1609-10 (2011) (“A bright-line rule removes the uncertainty that plagues Merck’s ‘discovery’ standard. . . . In any event, if claims are filed that lie outside the statute of repose, they can be easily dispensed with by the judiciary at the preliminary stage, thus saving the courts and the parties costs of later litigation.”).

number of trained personnel to the task; or because the agency's enforcement program is ill-designed or inefficient; or because the nature of the statute makes it difficult to uncover violations; or because of some combination of these factors and others." 3M, 17 F.3d at 1461. But, the SEC's "failure to detect violations" is not Appellees' fault and "does not avoid the problems of faded memories, lost witnesses and discarded documents in penalty actions brought decades after alleged violations are finally discovered." 3M, 17 F.3d at 1461.¹¹ Nor does it offer solace to the defendant. It thus cannot delay the accrual or the running of the statute of limitations.

IV. THE SEC'S PROPOSED RULE WOULD LEAD TO UNREASONABLE AND UNFAIR RESULTS

The civil fraud provisions of the federal securities laws cover a broad swath of economic activity. To name a few: Section 10(b) of the Securities Exchange Act and Rule 10b-5 promulgated thereunder make it unlawful "for any person, directly or indirectly ... [t]o employ any device, scheme or artifice to defraud," "[t]o make any untrue statement of a material fact," or "[t]o engage in any act, practice or course of business which operates or would operate as a fraud

¹¹ See Kaufman & Wunderlich, 52 WM. & MARY L. REV. at 1551 ("[L]imitations are designed to mitigate the risk that evidence of meritorious claims will become stale and to relieve potential defendants from unending uncertainty about whether they will be brought into court."); see also Ochoa & Wistrich, 28 PAC. L.J. at 453 (examining purported justifications for statutes of limitations in civil cases including to promote repose, to minimize deterioration of evidence, to prompt enforcement of substantive law and to reduce the volume of litigation).

or deceit upon any person [] in connection with the purchase or sale of any security.” 17 C.F.R. § 240.10b-5 (emphasis added). They regulate the literally millions of securities trades that course through the U.S. public exchanges on any given day, as well as those effected off-exchange or over-the-counter. Section 17 of the Securities Act, in similar language, regulates “the offer or sale of any securities ... by the use of any means or instruments of transportation or communications in interstate commerce or by the use of the mails.” 15 U.S.C. §77q (emphasis added). Section 206 of the Investment Advisers Act, 15 U.S.C. § 80b-6(1) and (2), addresses all conduct by “any investment adviser” that “could operate” as a fraud or deceit including “all conflicts of interest which might incline an investment adviser – consciously or unconsciously – to render advice which was not disinterested” and imposes on advisers “an affirmative duty of utmost good faith, and full and fair disclosure of all material facts, as well as an affirmative obligation to employ reasonable care to avoid misleading his clients.” SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 191-92, 194 (1963) (internal quotation marks omitted) (explaining that the Investment Advisers Act does not require proof of the elements of common law fraud). The Supreme Court has directed that these laws are “to be construed ... not technically and restrictively, but flexibly to effectuate [their] remedial purposes.” Id. at 194-95.¹²

¹² See also SEC v. Zanford, 535 U.S. 813, 819 (2002) (Section 10(b) “should be construed not

Violation of these provisions is unlawful and can give rise to a penalty regardless whether it is concealed, and regardless whether a defendant has an intent to conceal it.

Congress has not by “Act” enacted a “discovery rule” with respect to any of these statutes, as it has in other statutes. The SEC’s proposed rule nonetheless would relieve the agency, as a categorical matter, from its obligation to bring a timely case for all these claims and any other claims brought pursuant to a statute that sounds in fraud, regardless whether the violation has been concealed or the defendant has concealed it, and place the burden on defendant to prove as a factual matter that the SEC should have discovered the violation earlier. In so doing, it would lead to extraordinarily pernicious results. With respect to discovery, by focusing the inquiry exclusively on the government’s knowledge and not on whether the defendant intentionally concealed his conduct, it would lead to one of two equally unpalatable and unfair results. On the one hand, all evidence bearing on the SEC’s knowledge of the alleged violation, even evidence the SEC has gathered in seemingly unrelated investigations, would potentially be relevant and discoverable. Evidence that the agency knew or should have known that a particular type of market conduct, as committed by regulated entity A, was abusive

technically and restrictively, but flexibly to effectuate its remedial purposes.”) (internal quotations omitted); Aaron v. SEC, 446 U. S. 680, 693-95 (1980) (discussing the broad remedial nature of securities laws in context of section 17(a) of the Securities Act).

clearly would be relevant to and would undermine a claim by the SEC that it could not have discovered that the same type of conduct, committed by regulated entity B, was also abusive.¹³ At the same time, corporate entities and individuals often cooperate with SEC investigations on the understanding and promise that, until charges are brought, such investigations are confidential.¹⁴ Cf. Molchatsky v. United States, No. 09 Civ. 8697 (LTS)(AJP), 2011 WL 1471798, at **11-12

¹³ From the record below it appears the SEC knew of options backdating practices years prior to investigating Appellees but decided these practices were abusive and in violation of the securities laws only after the Wall Street Journal ran an article in 2006 exposing such practices as harmful. See Charles Forelle & James Bandler, The Perfect Payday, WALL ST. J., March 18, 2006, at A1 (reporting on the widespread occurrence of stock option backdating and on the SEC's systematic review of these practices by a dozen entities). Similarly, in the mutual fund market timing context it was only after the New York Attorney General ("NYAG") investigated the negative effects of market timing that the SEC concluded market timing conduct known to it before the NYAG investigation was abusive. U.S. Securities and Exchange Commission, Staff Report, Exemptive Rule Amendments of 2004: The Independent Chair Condition at 31 (Apr. 2005), available at <http://www.sec.gov/news/studies/indchair.pdf>, (stating the SEC was prompted to investigate the practice of mutual fund market timing after the NYAG's identification of market timing as an abusive practice).

¹⁴ The SEC's common practice regarding the confidentiality of investigations is that:

investigations are conducted confidentially to protect evidence and reputations. Important documents could be destroyed if an investigation is publicly announced, so confidential treatment may help to preserve key evidence in a case. A confidential process also protects the reputations of companies and individuals where the SEC finds no wrongdoing by the firm or the individuals that were the subject of the investigation. As a result, the SEC generally will not confirm or deny the existence of an investigation unless and until it becomes a matter of public record. An investigation becomes public when the SEC files an action in court or through an administrative proceeding. The SEC website contains information about public enforcement actions.

U.S. Securities and Exchange Commission, Investigations by the Securities and Exchange Commission, available at <http://www.sec.gov/answers/investg.htm> (last visited May 11, 2005); see also Securities and Exchange Commission Division of Enforcement, Enforcement Manual at 3 (Aug. 2, 2011), available at <http://www.sec.gov/divisions/enforce/enforcementmanual.pdf> (informing the SEC staff of a number of ethical considerations, including "Confidentiality and the Protection of Nonpublic Information").

(S.D.N.Y. April 19, 2011) (dismissing case based on SEC's failure to bring claim). The preservation of that confidentiality is critical to the effective and efficient functioning of the markets and to effective SEC enforcement. The Court should not adopt a rule that would lead to one of these two possibilities: a hollow defense or diminished confidentiality and enforcement. And it need not in the absence of an "Act of Congress."

Rules have developed regarding the appropriate retention of documents and conduct of civil investigations. Broker-dealers must retain records for periods of up to six years. See Books and Records Requirements for Brokers and Dealers Under the Sec. Exch. Act of 1934, Release No. 33-44992, 2001 WL 1327088 (SEC Oct. 26, 2001) (books and records documents must be retained for periods of two, three, and six years). Auditors must keep records for seven years, two years beyond the "five years after the end of the fiscal period in which an accountant audits or reviews an issuer's financial statements." In re Retention of Records Relevant to Audits and Reviews, Release No. 33-8180, 2003 WL 164273, at *4 (SEC Jan. 4, 2003). As Congress specified, the intent of these rules was "to require the retention of [] materials, including material that casts doubt on the views expressed in the audit or review, for such a period as is reasonable and necessary for effective enforcement of the securities laws and the criminal laws, most of which have a five-year statute of limitations." Id. at *19 n.39 (quoting

statement of Senator Leahy on the Senate floor, 148 CONG. REC. S7419 (July 26, 2002)).¹⁵ The SEC’s proposed rule would turn those regulations and the careful cost-benefit balancing they reflect. See, e.g., SEC Release No. 34-44992 (discussing cost benefit analysis of broker dealer books and records requirements). Those periods are predicated on the understanding, supported by the plain meaning of Section 2462, that claims must be brought within five years of the violation. The SEC’s proposed rule, however, would turn those rules on their head. A business or entity wanting to make sure that it preserved evidence for so long as the SEC might be able to bring a claim would have to retain records not just five years, or seven years, but indefinitely – or at least until the indeterminate date upon which it could be said that the SEC “could or should” have discovered the violation.

The SEC rule would have still other perverse results. The record retention rules exist not just for firms to protect themselves, but to preserve evidence relevant to the question whether others have violated the law. Audit firms, for example, are required to retain their work papers for seven years, not just because those records are relevant to their conduct, but because they could establish alternatively the existence of a fraud by the auditor’s client or the reliance by that client in good faith on the auditor’s advice. See, e.g., SEC v. Caserta, 75 F.

¹⁵ See also Ochoa & Wistrich, 28 PAC. L.J. at 469-70 (“With a fixed and ascertainable limitation period, it is clear when records may safely be destroyed.”).

Supp. 2d 79, 94 (E.D.N.Y. 1999). It would be intolerable for the results to differ in two otherwise comparable cases depending only on whether the audit firm chose voluntarily to retain records beyond that required by rule.

The SEC Rule would lead to perverse enforcement incentives, permitting the SEC to devote all of its resources to whatever might be the flavor of the day, based on press reports, and to ignore violations of equally important laws, secure in the knowledge that its ignorance would come at low cost. It may argue that because it chose not to investigate, it could not have discovered, and because it could not have discovered, its claims will not be time-barred.

An ABA Task Force has concluded that “with no specific maximum cutoff” for timely suits, and under threat the SEC could at any time begin to investigate, “managements of publicly held companies, as well as their auditors and attorneys, are frequently unable to assess the impact of possible litigation,” which “deprives investors of information adequate for informed evaluation of [the] companies’ potential liabilities.” James W. Beasley, Jr., Report of the Task Force on Statute of Limitations for Implied Actions, 41 BUS. LAW. J. 645, 647 (1986). Companies would, indefinitely, be forced to go back and consider ancient conduct that might lead to fraud liability so that they could report such liability to their auditors and accurately record current liabilities in their financial statements.

Ultimately, “[p]articularly in the field of securities law . . . limitations

periods provide repose not only for the allegedly guilty parties but for potentially large numbers of innocent dependents who rely upon the continued financial health of a defendant.” Christopher A. Ford, Knowledge and Notice in Section 10(b) Limitations Law, 103 YALE L.J. 1939, 1951 (1993).¹⁶ Statutes of limitations not only protect individual defendants but also promote a functioning marketplace. This is one of the primary reasons securities laws have “limitations periods,” “to encourage business activity by limiting the disruptions that litigation can cause” and “promote[] stability in the ownership of assets and avoid[] chilling entrepreneurial activity with the threat of litigation many years after an alleged wrong.” Ford, 103 YALE L.J. at 1952. Certainty and repose are critical elements of a functioning marketplace and have long been recognized by our laws. See H.R. REP. NO. 101-734, at 27 (1990), reprinted in 1990 U.S.C.C.A.N. 6860, 6870 (stating that “settling the expectations of prospective parties is an essential purpose of statutes of limitation” for private securities actions).

¹⁶ See also Kaufman & Wunderlich, 52 WM. & MARY L. REV. at 1610 (“[W]ithout repose, securities fraud would affect settled economic expectations of nonculpable markets participants.”); Michael A. Perino, Enron’s Legislative Aftermath: Some Reflections on the Deterrence Aspects of the Sarbanes-Oxley Act of 2002, 76 ST. JOHN’S L. REV. 671, 692 (2002) (discussing the “significant costs on our capital markets” of extending statutes of repose that have the effect of “reduc[ing] deterrence and decreas[ing] social welfare”); Elizabeth Consenza, Dura-tion: A New Paradigm for Construing the Statute of Limitations in Securities Fraud Class Actions, 62 BAYLOR L. REV. 681, 687 (2010) (“Limiting potential defendants’ long-term exposure to suit promotes stability in business activity and avoids chilling entrepreneurial activity with the threat of extended exposure to litigation many years after an alleged violation. Time bars placed upon the availability of a cause of action thus speed the vindication of the public’s interest in securities law enforcement while minimizing the business costs of extended exposure to liability.”).

It is an acceptable compromise, and one the legislature has drafted, that the SEC may seek disgorgement from one who continues to hold ill-gotten gains after the five-year period has expired. The retrieval of those funds “is remedial rather than punitive,”¹⁷ addresses the continuing wrong of the holding, and can be defeated at any time by the simple return of the alleged funds. It would undermine not only the language of the statute and well-established principles of statutory interpretation, but also the entire function of a statute of limitations and the effective and efficient functioning of the securities markets for the courts to accomplish the same result for penalty claims by applying the SEC’s attempted importation of a discovery rule into Section 2462.

CONCLUSION

For the foregoing reasons, SIFMA opposes the SEC’s argument regarding the existence of an implied discovery rule under Section 2462 and believes the order of the district court should be affirmed.

¹⁷ SEC v. Grossman, No. 87 Civ. 1031 (SWK), 1997 WL 231167, at *9 (S.D.N.Y. May 6, 1997), aff’d in part, vacated in part on other grounds sub nom, SEC v. Hirshberg, 173 F.3d 846 (2d Cir. 1999).

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CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limitations of Fed. R. App. P. 29(d) because it contains 6,082 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

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