No. 11-1274

IN THE

Supreme Court of the United States

MARC J. GABELLI AND BRUCE ALPERT,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

ON WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

BRIEF FOR NATIONAL ASSOCIATION OF CRIMINAL DEFENSE LAWYERS AS AMICUS CURIAE IN SUPPORT OF PETITIONERS

JOSHUA L. DRATEL
CO-CHAIR, AMICUS COMMITTEE
NATIONAL ASSOCIATION OF CRIMINAL DEFENSE LAWYERS
2 Wall St., Third Floor
New York, NY 10005
(212) 732-0707

PAUL R.Q. WOLFSON
Counsel of Record
SHIRLEY CASSIN WOODWARD
JOSHUA M. SALZMAN
WILMER CUTLER PICKERING HALE AND DORR LLP
1875 Pennsylvania Ave., NW
Washington, DC 20006
(202) 663-6000
paul.wolfson@wilmerhale.com

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INTEREST OF AMICUS CURIAE

Amicus curiae National Association of Criminal Defense Lawyers (NACDL) is a nonprofit, professional bar association representing public defenders and private criminal defense lawyers across the nation.[1] Founded in 1958, NACDL has a direct national membership of more than 10,000 attorneys and more than 28,000 affiliate members from all fifty states. NACDL's mission is to ensure justice and due process for the accused; to foster the integrity, independence, and expertise of the criminal defense profession; and to promote the proper and fair administration of criminal justice and the defense of individual liberties. NACDL frequently files amicus curiae briefs in this Court in matters pertinent to its mission. As relevant here, NACDL has a strong interest in ensuring that statutes of limitations are properly applied in a manner that will not prevent those accused of misconduct from mounting an effective defense to the charges against them.

SUMMARY OF ARGUMENT

Nowhere are meaningful and definite statutes of limitations more important than in cases where the government acts to punish wrongdoers, including penalty actions governed by 28 U.S.C. § 2462. This Court has long recognized the special importance of repose in criminal cases, and penalty actions similarly seek to punish the defendant rather than remedy a past harm.

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[1] Both parties have given written consent to the filing of all amicus briefs. No counsel for a party authored this brief in whole or in part, and no person other than amicus, its members, or their counsel made a monetary contribution to the preparation or submission of this brief.

In penalty actions, a defendant's reputation and livelihood are at stake. Yet by effectively expanding the limitations period for fraud actions and thus allowing the government to proceed in cases where vital exculpatory evidence may have disappeared, the decision below substantially increases the possibility that defendants will be unfairly subjected to these sanctions. This risk is particularly unacceptable because in penalty actions there is no countervailing equitable interest in keeping claims alive so as to give an injured party a fair opportunity to obtain compensation, and because the government has the resources and tools necessary to prosecute claims in a timely manner.

Practical business considerations also weigh against construing Section 2462 as incorporating a discovery rule for actions that sound in fraud. The decision of the court of appeals exposes corporations to potentially open-ended liability for past wrongdoing. This, in turn, will inevitably create greater uncertainty that will hamper business transactions, as executives, investors, and professional service providers alike will be unable to reliably ascertain the extent of a company's potential exposure. The absence of repose thus will chill economically beneficial transactions. And the uncertainty engendered will also lead companies to take costly document preservation and other measures in an effort to mitigate the risks created by the Second Circuit's rule, which in turn will consume resources that could be more productively deployed.

Finally, the decision below defangs an important check against prosecutorial abuses. It will empower regulators to pressure defendants into unjust settlements. And it will substantially increase the likelihood that the laws will be applied arbitrarily based on shift-ing political whims, and discriminatorily against politically disfavored industries, companies, and individuals.

ARGUMENT

I. THE STATUTE OF LIMITATIONS IN GOVERNMENT PENALTY ACTIONS IS NOT EXTENDED BY A DISCOVERY RULE

A. Repose Is Particularly Important In The Context Of Penalty Actions

This Court has long recognized that "[s]tatutes of limitation are vital to the welfare of society and are favored in the law." *Wood* v. *Carpenter*, 101 U.S. 135, 139 (1879). While the social policy favoring repose after passage of time applies to some degree in all kinds of cases, its importance is particularly salient in penalty actions such as those governed by 28 U.S.C. § 2462, where the government acts not to redress a private harm but to identify and punish alleged wrongdoers. In such cases, the importance to the defendant of avoiding stale claims is particularly great, whereas the government's interest in bringing an action long after the occurrence of the underlying facts is considerably diminished.

1. There is a particularly compelling need for repose in actions where the government seeks to impose punishment

This Court has repeatedly recognized the important function that statutes of limitations play in "minimiz[ing] the danger of official punishment because of acts in the far-distant past." *Toussie* v. *United States*, 397 U.S. 112, 115 (1970), *superseded by statute on other grounds*, Act of Sept. 28, 1971, Pub. L. No. 92-129, § 101(a)(31), 85 Stat. 348, 352-353. As early as

Chief Justice Marshall's opinion in *Adams* v. *Woods*, 6 U.S. (2 Cranch) 336 (1805), this Court remarked that "[i]n a country where not even treason can be prosecuted after a lapse of three years, it could scarcely be supposed that an individual would remain forever liable to a pecuniary forfeiture." *Id.* at 339. This point was echoed by Justice Story, who reiterated that "it would be utterly repugnant to the genius of our laws[] to allow such prosecutions a perpetuity of existence." *United States* v. *Mayo*, 26 F. Cas. 1230, 1231 (C.C.D. Mass. 1813) (No. 15,755). Consistent with these holdings, this Court has repeatedly indicated that criminal statutes of limitation are to be "liberally interpreted in favor of repose." *Toussie*, 397 U.S. at 115; *see United States* v. *Habig*, 390 U.S. 222, 227 (1968); *United States* v. *Scharton*, 285 U.S. 518, 522 (1932).

Congress, accordingly, has strictly defined statutes of limitations for many criminal offenses—even those that might be particularly difficult for the government to discover. For example, the statute of limitations for criminal prosecution for a "securities fraud offense" expires "6 years after the *commission of the offense*." 18 U.S.C. § 3301 (emphasis added). The exceptions to these federal criminal statutes of limitations are quite limited and narrow, reflecting Congress's recognition that individuals in our society have a strong interest in being free from the frightening prospect of criminal prosecution after the passage of time. *See id.* § 3292 (suspension of limitations to permit United States to obtain foreign evidence); *id.* § 3290 (statute of limitations does not apply to fugitives from justice). Federal criminal statutes of limitations have not, to amicus's knowledge, been subject to extension under a "discovery rule" on the ground that the government could not have discovered the violation more quickly; rather, Congress has determined that even criminal prosecutions, which serve a critical public interest, should be pursued in an expeditious manner.

The wise social policy that prevents the government from threatening individuals with "official punishment" for acts in the "far distant past" applies equally to penalty actions governed by Section 2462. Penalty actions share several important and relevant features with criminal prosecutions. First, "a 'penalty,' as the term is used in Section 2462, is a form of punishment imposed by the government for unlawful or proscribed conduct, which goes beyond remedying the damage caused to the harmed parties by the defendant's action." *Johnson* v. *SEC*, 87 F.3d 484, 488 (D.C. Cir. 1996) (emphasis added); *see Meeker* v. *Lehigh Valley R.R. Co.*, 236 U.S. 412, 423 (1915) (describing "penalty," as used in prior codification of Section 2462, as "something imposed in a punitive way for an infraction of a public law," as opposed to "a liability imposed solely for the purpose of redressing a private injury"). In other words, a government-brought penalty action, like a criminal prosecution but unlike a lawsuit for damages, is intended to identify a person as an offender against society and to punish that person for his wrongdoing, rather than to compensate another individual who has been harmed.

Second, a defendant to a government penalty action faces not just the prospect of a monetary loss but also the public opprobrium of being branded a wrongdoer. Individuals and corporations may find their reputations seriously harmed after they are publicly identified as defendants to such actions. If their defense is unsuccessful, they may also incur collateral consequences that effectively deprive them of their livelihood. Individuals and companies found to have committed violations of law may, for reasons both practical and legal, be unable to continue to work in their chosen line of business. Even for those exonerated in an enforcement action, the reputational costs can be significant and can make it difficult if not impossible for them to continue to work in their field.

For these reasons, penalty actions are sufficiently analogous to criminal proceedings that Section 2462—like criminal statutes of limitations—should be construed in favor of repose.[2] At the very least, there is no valid basis to *extend* the limitations period—by judicial gloss—beyond that specified by the plain language of the statute.

2. Allowing adjudication of stale claims substantially compromises factfinders' ability to distinguish between wrongdoers and the wrongly accused

This Court has repeatedly recognized that statutes of limitations not only protect the special interest in repose but also serve to avoid the potential prejudice and unfairness to defendants posed by stale evidence. In particular, the critical truth-finding function of the courts is significantly compromised in cases where the evidence has become stale. Statutes of limitations "rest[], in large part, upon evidentiary concerns—for example, concern that the passage of time has eroded

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[2] Several courts have recognized that penalty actions have at least some of the characteristics of criminal proceedings. *See, e.g.*, *SEC* v. *Kramer*, 778 F. Supp. 2d 1320, 1323 n.3 (M.D. Fla. 2011) ("[T]he Commission's request for a civil penalty undoubtedly lends criminal character to the proceeding."); *SEC* v. *Snyder*, CIV. H-03-04658, 2006 WL 6508273, at *1 (S.D. Tex. Aug. 22, 2006) (recognizing "the quasi-criminal nature of [an SEC penalty action], as well as the gravity of what is at stake for Defendant").

memories or made witnesses or other evidence unavailable." *Stogner* v. *California*, 539 U.S. 607, 615-616 (2003); *see also United States* v. *Kubrick*, 444 U.S. 111, 117 (1979) (noting statutes of limitations "protect defendants and the courts from having to deal with cases in which the search for truth may be seriously impaired by the loss of evidence, whether by death or disappearance of witnesses, fading memories, disappearance of documents, or otherwise"); *Wilson* v. *Garcia*, 471 U.S. 261, 271 (1985) ("Just determinations of fact cannot be made when, because of the passage of time, the memories of witnesses have faded or evidence is lost."), *superseded by statute on other grounds as recognized in Jones* v. *R.R. Donnelley & Sons Co.*, 541 U.S. 369, 377-378 (2004). In other words, statutes of limitations "specify[] a limit beyond which there is an irrebuttable presumption that a defendant's right to a fair trial would be prejudiced." *United States* v. *Marion*, 404 U.S. 307, 322 (1971); *see Wood*, 101 U.S. at 139 ("While time is constantly destroying the evidence of rights, [statutes of limitations] supply its place by a presumption which renders proof unnecessary.").

The dangers of stale evidence are particularly acute in penalty actions. The stakes are far higher than in private civil lawsuits; an erroneous adverse judgment is especially damaging to a defendant when, as a result, he is not only forced to pay a substantial monetary penalty but also wrongly stigmatized with the label of a fraudster.[3] An individual merely accused of

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[3] One particularly perverse consequence of the decision below is that it gives prosecutors a strong incentive to characterize and charge a wider array of conduct as "fraud," which would be subject to a discovery rule, even if virtually identical conduct would be subject to a strict statute of limitations if charged under a different

fraud in an SEC penalty action will suffer significant if not livelihood-destroying reputational harm, and even individuals who are ultimately exonerated may find their careers ended. By contrast, defendants who are found liable for damages in private securities actions, or who settle such claims, are not subject to the same level of opprobrium and do not suffer the same reputational harms.

Moreover, stale evidence is particularly likely to cause unfair prejudice to innocent defendants in penalty cases. Although penalty actions seek to impose punishment, they are adjudicated under a preponderance-of-the-evidence standard rather than the more defendant-protective standards used in criminal cases.[4] Because of this lower burden of proof, defendants in penalty actions—unlike criminal defendants—often must, as a practical matter, introduce affirmative evidence to

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label (which might more accurately reflect the government's longstanding enforcement policies). As a consequence, not only will more defendants be subject to charges, but more will be labeled as fraudsters even when the substance of the charge is really regulatory in nature. For example, the government may be more apt to charge a failure to file an accurate Form 10-K with the SEC as fraud rather than as a potentially less-stigmatizing offense. This increased incentive to charge offenses as frauds may also exacerbate the coercion on defendants to settle charges, given the disastrous consequences of losing a fraud charge at trial.

[4] That defendants in penalty actions lack the safeguards given to criminal defendants weighs in favor of treating defendants in penalty actions no worse than criminal defendants for purposes of statutes of limitations. *Cf. Pendergast* v. *United States*, 317 U.S. 412, 418 (1943) (noting, in the course of discussing applicable statute of limitations for criminal contempt, that "[t]here is no reason why this lesser crime, punishable without some of the protective features of criminal trials, should receive" a more lenient limitations period).

establish that their actions complied with the law. In cases alleging violations of complex regulatory regimes, such as the securities laws, where there may be genuine uncertainty whether certain conduct is within the law, such affirmative evidence may often implicate issues of intent and the defendant's contemporaneous understanding of the facts and law. Yet the passage of time can severely undermine the defendant's ability to marshal such evidence, as memories fade, witnesses are no longer available, and documents or other evidence that could establish the defendant's contemporaneous understanding of the facts and the law and thus demonstrate good-faith compliance with the law might no longer be available.

A lengthy statute of limitations places defendants at a significant disadvantage in other ways as well. The SEC and other government agencies have the ability to investigate the facts, including by using compulsory process such as subpoenas, even before suit is filed. *See infra* pp. 14-15; *see also* Pet. Br. 40-41. Defendants, by contrast, do not have compulsory process before litigation commences and may not even know that the government is preparing a case against them until the action is instituted. The government can investigate for years, taking testimony and collecting documents, while the defendant cannot begin to build a defense until the action is in court, at which time critical exculpatory witnesses and evidence might no longer be available. As a consequence the evidence that is likely to be preserved in a long-delayed suit is evidence favorable to the government, not the defense.

3. The justifications proffered for a discovery rule in private lawsuits are much less forceful in penalty actions

Statutes of limitations are not without costs. The price of repose is that otherwise meritorious claims might be barred. In the private damages context, it might be inequitable to apply statutes of limitation inflexibly where doing so could prevent an injured plaintiff from securing compensation for her injuries. But in the context of government penalty actions, where the object is to punish the defendant rather than to redress a plaintiff's injury, this cost of repose to the private plaintiff is not present, whereas the danger of unfairness to the defendant is far greater. In the case of government penalty actions, therefore, equitable considerations do not undercut the strong justifications for strict application of the limitations period.

One rationale offered for the discovery rule in private damages actions is that a plaintiff injured by fraud should have a fair opportunity to seek compensation for that injury. Yet that plaintiff might not be immediately aware of the injury (which is usually an indispensable element of a private right of action) or any basis to connect the injury to a particular defendant. A discovery rule in those circumstances promotes fairness "where a plaintiff has been injured by fraud and remains in ignorance of it without any fault or want of diligence or care on his part." Br. in Opp. 9 (quoting *Holmberg* v. *Armbrecht*, 327 U.S. 392, 397 (1946) (internal quotation marks and citation omitted)).

In government penalty actions, by contrast, there is no injured party at risk of losing the opportunity to be made whole. And for most statutory violations, damage is not an element of the offense, so the government can proceed immediately after the commission of the violation without needing to establish the scope (or even the existence) of harm resulting from the defendant's conduct. Moreover, the government has significant investigative resources at its disposal, and it can deploy those resources to ferret out wrongdoers whenever it suspects that a violation of law may have occurred. In many circumstances the government does not even need an articulable suspicion to commence an investigation. The government also has significant discretion in deciding how to allocate those resources; indeed it can effectively control when it "discovers" a potential violation by deciding when to pursue an investigation and how urgently to do so. *See* Pet. Br. 39 (noting that the government's discovery of a potential violation is a function of when the government begins to investigate). As a result, in government penalty actions there is no countervailing equitable interest analogous to a tort victim's interest in being able to discover her injury and to be made whole through an award of damages, and certainly nothing comparable to the practical and legal difficulties that confront private individuals who may not even be aware that they may have a basis to seek redress for an injury.

Another reason why public policy strongly favors repose in penalty actions is that the deterrence interests in government enforcement actions diminish over time. *See Johnson*, 87 F.3d at 492 ("In addition, the SEC argues that enforcing § 2462 would hobble efforts to prevent future harm to the public. It is equally likely, however, that once the SEC has delayed more than five years in proceeding against a broker it considers a grave threat to the public, the bulk of the harm has already been done." (internal citation and quotation marks omitted)); *see also Marion*, 404 U.S. at 322-323 (recognizing "the salutary effect of encouraging law enforcement officials promptly to investigate suspected criminal activity"). The SEC itself recognizes timeliness in investigation and enforcement as a high institutional priority. In 2009 testimony before Congress, the Director of the Enforcement Division listed it among four guiding principles for the Division:

> [W]e have to be as swift as possible. A sense of urgency is critical. If cases are unreasonably delayed, if there is a wide gap between conduct and atonement, then the message—to the investing public that the SEC is vigilant and effective, as well as the message to those who might themselves be considering a step outside the law—is diluted. Timeliness is critical. Corporate institutions are dynamic and ever-changing. People come and go. When a case is brought years after the conduct, the fines and the penalties still hurt, but the opportunity to achieve a permanent change in behavior and culture is greatly reduced.

Strengthening the SEC's Vital Enforcement Responsibilities: Hearing Before the Subcomm. on Securities, Insurance, and Investment of the S. Comm. on Banking, Housing, and Urban Affairs, 111th Cong. 46 (2009) (statement of Robert Khuzami, Dir., Div. of Enforcement, SEC).[5] The SEC's enforcement manual, recog-

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[5] The SEC is in good company on this point; legal philosophers have long expressed the view that punishment is most effective when imposed swiftly. *See, e.g.*, Cesare Beccaria, *On Crimes and Punishments* § xix (1764); *see also* Note, *The Statute of Limitations in Criminal Law: A Penetrable Barrier to Prosecution*, 102 U. Pa. L. Rev. 630, 634 (1954) ("The pursuit of only more recent criminals is consistent with that aim of criminal law which

nizing that "[s]wift investigations generally are most effective and enhance the public interest," similarly instructs that SEC "[s]taff should take care not to delay or slow the pace of an investigation based on the potential availability or existence of a tolling agreement." SEC, Div. of Enforcement, *Enforcement Manual* § 3.1.2, at 41 (2012), *available at* http://www.sec.gov/divisions/enforce/enforcementmanual.pdf.

Congress, too, has recognized the value of timely investigation and enforcement. The recent Dodd-Frank Act imposed new 180-day deadlines, subject to certain exceptions, for the SEC to file (or determine not to file) any enforcement action after the issuance of a Wells notice and to provide notice of the results of a compliance examination or inspection. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 929U, 124 Stat. 1376, 1867-1868 (2010).

In short, requiring the government to bring penalty actions within five years of the alleged violation protects fairness through repose, does not leave injured parties without a claim to compensation, and promotes effective deterrence.

B. Government Regulators Have The Tools And Resources Necessary To Fulfill Their Functions Without A Discovery Rule

Requiring government enforcement agencies like the SEC to adhere to a five-year statute of limitations in penalty actions will not undermine the ability of those agencies to fulfill their functions. Those agencies

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seeks to rehabilitate wrongdoers and serves to free the citizen from vexatious fear of prosecution for old crimes.").

have the resources and tools necessary to enforce the laws without the need for a discovery rule.

Enforcement agencies have extensive resources at their disposal. The SEC's Division of Enforcement, for example, has a staff of nearly 1250 full-time-equivalent employees and a budget of $467 million. *See* SEC, *In Brief: FY 2013 Congressional Justification* 51 (Feb. 2012), *available at* http://www.sec.gov/about/secfy13congbudgjust.pdf. While those resources must be allocated across a wide array of enforcement objectives, they can be brought to bear on whatever investigations and according to whatever priorities the agency determines serves the public interest.

Second, enforcement agencies like the SEC are specially empowered by law to investigate violations *before* the filing of any action. The Commission or members of its staff may subpoena testimony and documents in the course of an investigation,[6] and its subpoenas now have nationwide reach. *See* Dodd-Frank Act, § 929E, 124 Stat. at 1853. Unlike private litigants, therefore, regulators can fully investigate a matter *before* having to meet the fraud pleading standard of Federal Rule of Civil Procedure 9(b), or even the more lenient standards of Rule 8 and Rule 11. Even when it is never exercised, the mere threat of the SEC's muscular subpoena power can effectively force investigated parties to disclose information voluntarily. *See, e.g.*, Robert Khuzami, Dir., Div. of Enforcement, SEC, *Re-*

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[6] This authority is established by Section 19(c) of the Securities Act, 15 U.S.C. § 77s(c); Section 21(b) of the Securities Exchange Act, *id.* § 78u(b); Section 209(b) of the Investment Advisers Act, *id.* § 80b-9(b); and Section 42(b) of the Investment Company Act, *id.* § 80a-41(b).

marks Before the New York City Bar: My First 100 Days as Director of Enforcement (Aug. 5, 2009), *available at* http://www.sec.gov/news/speech/2009/spch080509rk.htm ("[I]f defense counsel resist the voluntary production of documents or witnesses, or fail to be complete and timely in responses or engage in dilatory tactics, there will very likely [] be a subpoena on your desk the next morning."). Other enforcement agencies, such as the IRS and FTC, have similarly broad investigative powers. *See* 26 U.S.C. §§ 7602, 7604 (IRS summons power); 15 U.S.C. § 49 (FTC subpoena power); *see also United States* v. *Powell*, 379 U.S. 48, 57 (1964).

Third, when despite their significant investigative resources regulators are still unable to meet the five-year statute of limitations, they can enter into agreements with investigated parties to toll the statute of limitations. *See, e.g.*, *SEC Enforcement Manual* § 3.1.2, at 39-40. Investigated parties have a strong practical incentive to enter into tolling agreements with federal agencies who are conducting an investigation in order to avoid facing the burden of an immediate penalty action; indeed, the two defendants in this very case agreed to toll the limitation period. The ability of a regulator to negotiate extensions of the limitations period as needed in specific cases obviates any need for a blanket discovery rule. Defendants are also better served by tolling agreements than a discovery rule, because in order to seek such an agreement, the government must give the defendant notice of the investigation, which provides the defendant the opportunity to take steps to preserve evidence that might otherwise have been lost or destroyed.

Finally, even if a regulator is unable to act within the limitations period for bringing a penalty action, the regulator can still safeguard the public interest through other mechanisms. The district court in this case, for example, held that while the SEC's claims for monetary penalties were time-barred, Section 2462 would not bar the SEC from seeking injunctive relief or disgorgement. Pet. App. 35a. Indeed, the SEC instructs members of its enforcement staff to "[k]eep in mind that certain claims are not subject to the five-year statute of limitations under Section 2462, including claims for injunctive relief and disgorgement." *SEC Enforcement Manual* § 3.1.2, at 41; *see also SEC* v. *Wencke*, 622 F.2d 1363, 1369 (9th Cir. 1980) (Kennedy, J.) (noting that "[t]he federal courts have inherent equitable authority to issue a variety of 'ancillary relief' measures in actions brought by the SEC to enforce the federal securities laws").[7] The application of the five-year statute of limitations for monetary penalties therefore will not impede the efforts of regulators like the SEC to protect the public.

[7] Notably, a typical injunction or disgorgement action presents different issues of staleness than a penalty action. Injunctions—such as orders requiring the defendant to comply with securities laws—are forward-looking remedies that are focused not on past misconduct but rather on the extent to which the defendant represents a threat to the public in the future. A defendant can therefore rebut the government's arguments for an injunction with present evidence that he poses no such threat. And while disgorgement is to some degree backward-looking, it does nothing more than strip the defendant of his ill-gotten gains and thus return him to the position he would have occupied but for his misconduct. Because disgorgement is remedial rather than punitive, a defendant can rebut the government's arguments for disgorgement by presenting current evidence that he has returned any wrongfully obtained funds or is otherwise in the same position as he would have been absent a violation. By contrast, penalty actions focus on evidence of past violations; in most cases a defendant cannot as a practical matter avoid liability without access to contemporaneous evidence that may have disappeared or grown stale.

II. THE SECOND CIRCUIT'S RULE WILL HAMPER THE ABILITY OF INDIVIDUALS AND CORPORATIONS TO ARRANGE THEIR AFFAIRS

The Second Circuit's ruling, if adopted, will have adverse practical consequences not only for particular defendants facing penalty actions but also for the public more generally. The court of appeals' discovery rule would create significant uncertainty and risk for corporations, which could never be truly certain whether they were free of the prospect of enforcement actions, as well as for non-culpable market participants. *See generally* Mark T. Roberts et al., *Will the SEC Have Forever to Pursue Securities Violations?* SEC v. Gabelli, BNA Sec. Reg. & L. Rep. (July 23, 2012), *available at* 2012 WL 2949120. This increase in risk and uncertainty—with no countervailing equitable or policy gains—is likely to have adverse effects on the economy.

The Second Circuit's rule will hinder the ability of both corporations and individuals to order their affairs in an efficient and predictable manner. The elimination of repose will make it difficult for defendants to account fully for their potential liabilities in the ordinary course of operations and will accordingly create uncertainty and risk aversion that is harmful to the defendant's business as well as to the market as a whole. *Cf.* Suzette M. Malveaux, *Statutes of Limitations: A Policy Analysis in the Context of Reparations Litigation*, 74 Geo. Wash. L. Rev. 68, 76 (2005) ("With a limitations system intact, institutions can engage in commercial transactions unencumbered by the risk of litigation and able to structure and plan their affairs.").

The manifestations of this problem are numerous. For example, the prospect of perpetual penalty actions will make it difficult for auditors and accountants to identify and evaluate future potential liabilities. According to standards promulgated by the American Institute of Certified Public Accountants, auditors must account for liabilities arising from "actual or potential litigation" and must inquire into even "unasserted claims" that present "at least a reasonable possibility of an unfavorable outcome," as long as "management considers [the claims] to be probable of assertion" and has sought "legal counsel." Am. Inst. of CPAs, *Audit & Attest Standards, AU-C* §§ 501.17, .22(c), *available at* http://www.aicpa.org/Research/Standards/AuditAttest/DownloadableDocuments/AU-C-00501.pdf. The task of attempting to account for claims that could be brought years if not decades after the conduct in question is particularly challenging in complex regulatory contexts like the securities industry, where individuals and corporations may frequently confront uncertainty as to whether certain conduct is within the law. *See* Stuart R. Cohn, 1 *Sec. Counseling for Small & Emerging Companies* § 19:14 (2012) ("[P]ending SEC actions could cause havoc with company balance sheets that must reflect contingent liabilities."). More generally, the perpetual threat of government penalty actions for distant conduct will make it extremely difficult if not impossible for businesses to reliably identify, evaluate, plan for, dedicate resources to, and potentially disclose the possible threat of future enforcement actions. *See* James W. Beasley, Jr., *Report of the Task Force on Statute of Limitations for Implied Actions by the Committee on Federal Regulation of Securities*, 41 Bus. Lawyer 645, 647 (1986) (recognizing that when statutes of limitations are unclear, "managements of publicly held companies, as well as their auditors and attorneys, are frequently unable to assess the impact of possible litigation").

Another adverse consequence of the Second Circuit's rule is that potential defendants will perceive a need to preserve documents indefinitely. Since corporations and individuals may never know which documents might prove to be important evidence in a future investigation, without a clearly defined limitations period they will likely err on the side of caution by preserving everything. This step is not a minor inconvenience. As the Sedona Conference Working Group on Electronic Document Retention & Production has explained, the obligation to preserve documents in anticipation of litigation can "cripple" day-to-day operations unless it is reasonably cabined in scope. *The Sedona Principles: Best Practices Recommendations & Principles for Addressing Electronic Document Production* cmt. 5.a, at 28 (2d ed. 2007); *see, e.g.*, *Best Buy Stores, L.P.* v. *Developers Diversified Realty Corp.*, 247 F.R.D. 567, 570 (D. Minn. 2007) (cost of storing information from database would be $27,823 per month). An obligation to preserve documents for decades, in case the SEC or another regulator might someday decide to bring a penalty action, is expensive and inefficient and does not bring any countervailing enforcement or public policy benefits. *See supra* Part I.B (explaining lack of enforcement need for a discovery rule).

Third, open-ended exposure to the potential for government penalty actions will vastly complicate corporate due diligence. "Every day, companies that are bought and sold also happen to be parties to litigation and the due diligence required for these corporate transactions inevitably requires examination of the relevant lawsuits." Jonathan T. Molot, *A Market in Litigation Risk*, 76 U. Chi. L. Rev. 367, 391 (2009). But due diligence cannot accurately account for potential future liabilities that may be based on decades-old conduct.

The increased uncertainty created by the court of appeals' rule is likely to chill corporate merger, acquisition, and investment activity—and harm the economy as a whole. *See id.* at 374-375 ("[T]he uncertainty surrounding a significant potential liability may increase a company's cost of capital by depressing its stock price or increasing the interest rate it must pay on its debt."); Beasley, 41 Bus. Lawyer at 647 (explaining that a lack of clarity as to the statute of limitation for securities actions "deprives investors of information adequate for informed evaluation of … companies' potential liabilities"); Jacob A. Kling, Comment, *Tax Cases Make Bad Work Product Law*, 119 Yale L.J. 1715, 1722 (2010) ("Without the assurances that a litigation risk analysis can provide to potential outside investors, they may be unwilling to purchase the company's securities or enter into a business combination with the company or, if they do so, they may value the company on a 'worst case' basis.").

III. Repose For Penalty Actions Supplies An Important Check Against Abuses Of Enforcement Power

A. The Second Circuit's Rule Will Make It Easier For Regulators To Coerce Defendants Into Settling Non-Meritorious Claims

Statutes of limitations play an important role in preventing the government from forcing targets into unjust settlements of non-meritorious claims. In their absence (or in their near-perpetual extension through a discovery rule), the government can aggregate penalties for violations going back years if not decades, which can make it impossible for many defendants to run the risk of going to trial. This danger is exacerbated by the government's ability—and willingness—to "stack" alleged violations, resulting in potential penalties so massive that defendants have no realistic choice but to settle. In addition, without statutes of limitations, the government may likewise be able to obtain settlements of non-meritorious present claims by threatening to pursue charges based on conduct from the distant past. The threat of investigation into past conduct may also lead a defendant to forgo a viable defense to present charges.

Many federal statutes, including the securities laws, authorize regulators to seek civil monetary penalties for multiple acts or transactions within an overall course of conduct. For example, under the Securities Act, the Securities Exchange Act, the Investment Advisers Act, and the Investment Company Act, the SEC can seek significant monetary penalties for each "violation" of the statute. But the statutes fail to define a "violation." *See* Marc I. Steinberg & Ralph C. Ferrara, 25 *Securities Prac. Fed. & State Enforcement* § 6:9 (Westlaw through 2012) ("The Remedies Act [which created the penalty provisions]…does not define the term 'violation,' and the legislative history does not discuss whether a course of conduct prohibited by the securities statutes will constitute a single violation or whether each illegal act or transaction will constitute a separate violation."). The SEC therefore can "dramatically increase the maximum penalties that can be imposed" by "characterizing a course of conduct as multiple violations of multiple provisions." *Id.*; *see* Richard A. Spehr & Michelle J. Annunziata, *The Remedies Act Turns Fifteen: What Is Its Relevance Today?*, 1 N.Y.U. J. L. & Bus. 587, 593 n.15 (2005); Matthew Scott Morris, Comment, *The Securities Enforcement Remedies and Penny Stock Reform Act of 1990*, 7 Admin. L.J. Am. U. 151, 183 n.163 (1993). Whereas previously, the SEC was at least limited to aggregating "violations" over a five-year period, the decision below effectively gives the SEC license to "stack" such charges over a much longer period of time.[8]

The penalties in question are not small change. For individuals, the penalties for violations subsequent to March 3, 2009, range from $7,500 for a "first-tier" violation to $75,000 for a "second-tier" or $150,000 for a "third-tier" violation, where graduation from the first tier to the second requires "fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement," and graduation from the second to the third requires that the "violation directly or indirectly [have] resulted in substantial losses or created a significant risk of substantial losses to other persons." 15 U.S.C. § 77t(d)(2) (Securities Act); *see id.* §§ 78u(d)(3)(B), 80a-41(e)(2), 80b-9(e)(3) (similar provisions under the other Acts); 17 C.F.R. § 201.1004 and pt. 201, subpt. E, tbl. IV (indexing the penalty amounts for inflation). For corporations, the amounts are substantially higher. *Id.* When multiplied by any number of individual acts or transactions, these penalties add up quickly.

The SEC has in fact sought to "stack" penalties in this fashion. In one enforcement action, the agency requested a monetary penalty of $3,000,000, reaching that

[8] "Stackable" penalties are not limited to the securities laws. The EPA, for example, can seek a penalty of $37,500 *per day* for certain violations of environmental statutes, including the Clean Air Act, 42 U.S.C. § 7413(b), the Clean Water Act, 33 U.S.C. § 1319(d), and the Resource Conservation and Recovery Act, 42 U.S.C. § 6928(g). *See* 40 C.F.R. § 19.4 (indexing statutory penalties for inflation).

figure by multiplying the third-tier penalty of $100,000 by the number of statutes that the defendant allegedly violated and the number of time periods in which he did so. *See* Securities and Exchange Commission's Memorandum in Support of its Request for Remedies at 28, *SEC* v. *Koenig*, 532 F. Supp. 2d 987 (N.D. Ill. 2007) (No. 02 C 2180), 2006 WL 3608027 (explaining that Koenig was liable for five penalties because he violated Section 13(a) of the Exchange Act by filing "false corporate reports" for "each year from 1992 through 1996"); *see also id.* at 26 ("The Commission seeks penalties under a *per violation* approach."). In another enforcement action, the SEC went even further, arguing that the statute permitted penalties of $6.03 and 1.206 *billion* (for the corporate and individual defendants respectively), reaching those figures by multiplying the third-tier penalty amounts by the "10,052 illegal late trades" at issue. Plaintiff Securities and Exchange Commission's Post-Trial Memorandum of Law Regarding Imposition of Penalties in the Final Judgment at 8, *SEC* v. *Pentagon Capital Mgmt. PLC*, No. 08 Civ. 3324, 2012 WL 1615496 (S.D.N.Y. Mar. 20, 2012). And courts have acceded to such requests. *See, e.g.*, *Pentagon Capital Mgmt.*, No. 08 Civ. 3324, 2012 WL 1036087, at *3 (S.D.N.Y. Mar. 28, 2012) (agreeing with the SEC's interpretation of the potential penalty, though declining to impose it); *SEC* v. *AmeriFirst Funding, Inc.*, No. 07-CV-1188, 2008 WL 1959843, at *9 (N.D. Tex. May 5, 2008) (imposing a $1.178 million penalty, calculated by multiplying $2,000 by the number of fraudulently obtained investments); *SEC* v. *Kenton Capital, Ltd.*, 69 F. Supp. 2d 1, 17 & n.15 (D.D.C. 1998) (imposing a $1.2 million penalty, calculated by multiplying the third-tier penalty amount by the number of fraudulently obtained investments).

What makes this sort of "stacking" so troubling, and what should caution against expanding the time horizon over which the government can further aggregate charges, is that it allows the government to threaten to seek penalties so massive as to make it practically impossible for a defendant to risk trial. In a complex regulatory regime, even informed individuals and corporations can find themselves, despite their good faith, in non-compliance with the law. Yet the defendant in such a circumstance might have no choice but to settle, given that the potential penalties could destroy her business. Indeed, even a clearly non-meritorious claim might be too risky to challenge. The decision below, which significantly multiplies the government's power to stack alleged violations, creates an unacceptable danger of such coercive actions.

In addition, defendants who are otherwise inclined to contest allegations may find themselves pressured by regulators with threats of additional charges based on conduct from their pasts. A defendant may be led to understand that if he does not accede to the present charges, the government will dig back as far as necessary to discover alternative or additional grounds for a penalty action. When confronted with the prospect of having a motivated prosecutor review his entire career in search of a past infraction, many defendants will doubtless choose to settle even non-meritorious claims. This kind of coercive pressure to settle questionable charges undermines the fairness and integrity of our legal system.

B. The Second Circuit's Approach Gives The Government A New Power That Is Highly Susceptible To Being Used In Arbitrary And Discriminatory Ways

The court of appeals' rule also increases the risk that the government's enforcement power will be deployed in arbitrary and discriminatory ways. The government's enforcement priorities always reflect policy judgments, and those policies and priorities often change over time, as mores and political values change. A particular danger arises when the government is empowered to bring enforcement actions for long-past conduct. Under the Second Circuit's rule, conduct that no one (including the government) might have perceived as illegal at the time, or might have thought sufficiently problematic to be worth pursuing, "may later become the focus of enforcement and prosecutions as policies and media focus shift." Roberts et al., *Will the SEC Have Forever to Pursue Securities Violations?*, at 7.

Even though it is clearly desirable for the government to have flexibility to adjust its enforcement priorities, this flexibility always carries the potential for overreaching and abuse. In our system, that possibility is usually cabined by the reality that agencies will choose *not* to pursue conduct that does not warrant the expenditure of enforcement resources. The court of appeals' decision significantly loosens this important constraint. In particular, the possibility that the government might decide—perhaps motivated by political considerations that make a particular class of defendants momentarily unpopular—to turn its attention suddenly to incidents that took place years before should be deeply worrisome.

This Court has recognized that "[a]n agency generally cannot act against each technical violation of the statute it is charged with enforcing" and that every agency therefore 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, [and] whether the particular enforcement action requested best fits the agency's overall policies." *Heckler* v. *Chaney*, 470 U.S. 821, 831 (1985); *see also Morrison* v. *Olson*, 487 U.S. 654, 727-728 (1988) (Scalia, J., dissenting) (quoting then-Attorney General Robert Jackson's statement that "[i]f the Department of Justice were to make even a pretense of reaching every probable violation of federal law, ten times its present staff will be inadequate," and that "[w]hat every prosecutor is practically required to do is to select the cases for prosecution and to select those in which the offense is the most flagrant, the public harm the greatest, and the proof the most certain"). The Second Circuit's ruling vitiates the need to carefully weigh the relative merits of enforcement and the need to limit enforcement actions only to those most "flagrant" violations. Instead, the government will be free to seek punishment, many years later, for conduct that was not thought to be worthy of pursuit at the time it occurred.

The dangers of such "rediscovered" need for enforcement, long after an alleged violation occurred, are similar to those that the Ex Post Facto Clause was designed to prevent. A discovery rule allows the government to pursue and punish conduct that was previously tolerated. As a result, there is a real danger of arbitrary and discriminatory application of the law, as conduct is judged not by norms contemporaneous to the conduct but by current (and often changed) political and popular values. The Second Circuit's rule exacerbates the danger (which is always present to some degree) that the government's enforcement power will be used to punish "being unpopular with the predominant or governing group, being attached to the wrong political views, or being personally obnoxious to or in the way of the prosecutor himself." *Morrison*, 487 U.S. at 728 (Scalia, J., dissenting) (again quoting then-Attorney General Jackson). This can happen even in a system with meaningful statutes of limitations:

> With the law books filled with a great assortment of crimes, a prosecutor stands a fair chance of finding at least a technical violation of some act on the part of almost anyone. In such a case, it is not a question of discovering the commission of a crime and then looking for the man who has committed it, it is a question of picking the man and then searching the law books, or putting investigators to work, to pin some offense on him.

Id. But the possibility that an agency might attempt to unearth a past violation committed by a selected target improves dramatically if the agency can draw on its target's entire career rather than merely the past five years.

Even if line attorneys in federal regulatory agencies will be generally unlikely to pursue politically motivated investigations of their own volition, their agencies are subject to substantial political pressure from Congress and other political actors. The head of an agency who has failed to bring a case—any case—against an individual, corporation, or industry that is being publicly vilified at a given point in time may find herself subject to considerable pressure to bring suit so that political actors can claim that the government is taking vigorous action against the alleged wrongdoers. *See, e.g.*, *FDIC* v. *Maxxam, Inc.*, 523 F.3d 566, 571-573 (5th Cir. 2008) (recounting political pressure on FDIC to sue director of failed bank).

This Court has recognized in other contexts that statutes raise due process concerns when they "authorize and even encourage arbitrary and discriminatory enforcement." *City of Chicago* v. *Morales*, 527 U.S. 41, 56 (1999); *see Kolender* v. *Lawson*, 461 U.S. 352, 360 (1983) (striking down law that "furnishes a convenient tool for harsh and discriminatory enforcement by local prosecuting officials, against particular groups deemed to merit their displeasure" (internal quotation marks omitted)). The court of appeals' decision, regrettably, creates and exacerbates many of the same risks. Government agencies should not be able to comb the distant past to unearth potential violations that could result in massive monetary liability and social opprobrium. Section 2462 can and should be read to avoid such a troubling result.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

PAUL R.Q. WOLFSON
Counsel of Record
SHIRLEY CASSIN WOODWARD
JOSHUA M. SALZMAN
WILMER CUTLER PICKERING
HALE AND DORR LLP
1875 Pennsylvania Ave., NW
Washington, DC 20006
(202) 663-6000
paul.wolfson@wilmerhale.com

JOSHUA L. DRATEL
CO-CHAIR, AMICUS COMMITTEE
NATIONAL ASSOCIATION OF CRIMINAL DEFENSE LAWYERS
2 Wall St., Third Floor
New York, NY 10005
(212) 732-0707

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