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 Petition for A Writ of Certiorari to the United States Court of Appeals for the Second Circuit

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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PETITIONERS' REPLY BRIEF

The Government's opposition hinges on two assertions that have been undermined by a decision the Fifth Circuit issued after the Government filed its brief: that there is no circuit split and that the distinction between discovery accrual and equitable tolling is always "unimportant." The holding below creates a circuit split on an important and recurring federal question: whether a claim accrues under Section 2462 when it arises or when the Government discovers, or should have discovered, it. Under the Second Circuit's holding, a defendant whom the Government can allege violated an antifraud statute will forever be at peril of a governmental penalty, so long as the Government claims it discovered the claim recently and did not know of it earlier. In the history of the statute, no appellate court has ever previously read such a discovery rule into Section 2462.

1. The Government argues that there is no circuit split because the four appellate courts that have held that Section 2462 did not incorporate discovery did not do so in the context of an antifraud statute and the fifth appellate court that held that the statute for a fraud penalty claim begins to run when the violation takes place did not explicitly consider discovery. Opp. 18-20. In its recent decision, *SEC v. Bartek*, No. 11-10594, slip op. at 2 (5th Cir. Aug. 7, 2012), however, the Fifth Circuit explicitly rejected those distinctions. It held

that Section 2462's "first accrued" language refers to the date of violation and that the discovery rule did not apply even when the Government alleged the defendant violated an antifraud statute. *Bartek*, slip op. at 5-7; *see also id.* at 10 n.7 ("[W]e have rejected an automatic application of a fraud discovery rule into a federal statute when the statute is 'explicit in commanding' at what moment a suit must be brought.") (citation omitted). In so doing, it relied on *Trawinski v. United Techs.*, 313 F.3d 1295, 1298 (11th Cir. 2002); *FEC v. Williams*, 104 F.3d 237, 240 (9th Cir. 1996); *3M Co. v. Browner*, 17 F.3d 1453, 1460 (D.C. Cir. 1994); and *United States v. Core Labs., Inc.*, 759 F.2d 480, 483 (5th Cir. 1985), each of which it concluded had "similarly held that § 2462 does not incorporate a discovery rule." *Bartek*, slip op. at 6. Moreover, although the Fifth Circuit did not rely on it, *United States v. Witherspoon*, 211 F.2d 858, 861 (6th Cir. 1954), is also inconsistent with the decision below: that case *held* the statute of limitations for a fraud penalty claim applied when "the last alleged act of fraud" was committed and did not look to the date of discovery. The only other appellate decision to state that the discovery rule might apply is *SEC v. Koenig*, 557 F.3d 736, 739 (7th Cir. 2009), but in that case the evidence also supported equitable tolling and thus whether the doctrine was called discovery or tolling was, according to that court, "unimportant in practice." *Id.* at 739-40.[1]

[1] The Government also relies on *SEC v. Tambone*, 550 F.3d 106, 148-49 (1st Cir. 2008), but that case involved equitable tolling. *Id.* at 148 n.50.

2. The Government also asserts that the distinctions between discovery and equitable tolling are “unimportant.” Opp. 8-12. But, as this case and *Bartek* both establish, that claim is untrue. The federal securities laws regulate a broad range of economic activity. *See* Pet. 28. Both here and in *Bartek*, the district courts held that the SEC made no allegations of concealing conduct or a self-concealing fraud. The district court here held that Plaintiff did not allege with particularity under Rule 9(b) that Defendants took affirmative acts to conceal their wrongdoing or that the conduct at issue was self-concealing. Pet. App. 39a. The SEC did not appeal those holdings in either case. *Compare* Brief of SEC at 35, *SEC v. Gabelli*, No. 10-3581 (2d Cir. Oct. 29, 2010) (“[W]e note that the Commission does not appeal from the district court’s ruling rejecting the Commission’s alternative argument that the statute of limitations was tolled by the ‘fraudulent concealment’ doctrine.”), *with* Brief of SEC at 28, *SEC v. Bartek*, No. 11-10594 (5th Cir. Sept. 21, 2011) (using identical language); *see also Bartek*, slip op. at 5.[2] The SEC argued and the Sec-

[2] *See also* Tr. of Oral Argument at 27, *SEC v. Gabelli*, No. 10-3581 (2d Cir. June 2, 2011) (“We don’t invoke the fraudulent concealment doctrine. We don’t invoke tolling. What we invoke is the discovery rule.”); Reply Brief of SEC at 36, *SEC v. Gabelli*, No. 10-3581 (2d Cir. Mar. 15, 2011) (“The discovery rule is an accrual doctrine which determines when a limitations period begins to run, whereas the other doctrines toll the statute of limitations after it has already begun to run, or estop the defendant from asserting the statute’s bar based on his inequitable conduct.”).

ond Circuit held here that regardless whether Petitioners concealed their alleged misconduct or engaged in self-concealing conduct, they must defend against an ancient claim because "fraud claims by their very nature involve self-concealing conduct" and "since the Advisers Act claim is made under the antifraud provisions of that Act and alleges that the defendants aided and abetted [a] fraudulent scheme, . . . the discovery rule defines when the claim accrues." Pet. App. 18a-19a. The *Bartek* court held to the contrary. *See Bartek*, slip op. at 10.[3]

3. This case also presents an important federal question that warrants this Court's review. *See* Pet. 19-27. Many federal statutes that permit the Government to seek penalties could be characterized as "anti-fraud," as the Court characterized Section 206 here. *See* Pet. 28, 35 n.15; *e.g.*, 15 U.S.C. § 78j(b); 17 C.F.R. § 240.10b-5; 15 U.S.C. § 77q; 15 U.S.C. § 78n. Under the ruling below, the Government need not plead that the defendant engaged in a self-concealing fraud or concealed a fraud to seek a penalty for violations of those statutes based on ancient conduct. It need allege only "that the SEC first discovered the facts of [an alleged] fraudulent scheme" within five years of fil-

[3] *Bartek* purported to distinguish *Gabelli* claiming it "involved an inherently self-concealing fraudulent scheme." *Bartek*, slip op. at 9-10 & n.7. But the SEC correctly disavowed any reliance on the nature of the fraud or the conduct of the defendants here in precisely the same language it used in *Bartek*.

ing and did not know the claim earlier. *See* Pet. App. 21a. But the Government's detection of violations does not rest on the nature of the claim or difficulty of detection alone. It rests on the monies Congress appropriates for detection and the investigative priorities set and choices made in allocating resources, subjects "more appropriate for a congressional oversight hearing." *3M*, 17 F.3d at 1461.[4] The Government's failure to know of a fraud for reasons unrelated to the defendant's conduct does not "avoid the problems [for the defendant] of faded memories, lost witnesses and discarded documents." *Id.* It aggravates them. Moreover, equitable tolling applies in most cases where "the statute of limitations has run before the plaintiff obtained information essential to deciding whether he had a claim" and then only gives the plaintiff the time that is necessary. *Cada v. Baxter Healthcare Corp.*, 920 F.2d 446, 452-53 (7th Cir. 1990).[5] The Second Circuit's discovery rule would, for entire categories of claims, "leave the statute open for . . . eternity." Pet. 16.

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[4] The SEC has stipulated that "[b]eginning in the mid 1990s, the SEC knew about the practice of market timing in mutual funds, and the decision was to let the marketplace regulate itself." *See* Mark T. Roche, Sean C. Adams, & Scott H. Frewing, *Will the SEC Have Forever to Pursue Securities Violations?* SEC v. Gabelli, BNA Securities Regulation & Law Report, July 23, 2012, at n.3 and accompanying text, *available at* 2012 WL 2949120.

[5] Here, the SEC knew all of the facts it bases its claim on well before the statute expired—it even asked for tolling agreements. It just chose to sit on the case after the tolling agreements expired.

Additionally, under the discovery rule, all evidence bearing on the Government's knowledge of the alleged violation, including evidence gathered in separate investigations, would be relevant and potentially discoverable, in derogation of the understanding that such investigations are confidential. Open-ended liability would also frustrate Congress' intent to "require the retention of . . . material[s] . . . 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." *In re Retention of Records Relevant to Audits and Reviews*, Release No. 33-8180, 2003 WL 164273, at *19 n.39 (SEC Jan. 24, 2003) (quoting 148 Cong. Rec. S7419 (July 26, 2002) (statement of Sen. Leahy)).

4. The decision below is also inconsistent with this Court's decisions. The discovery rule delays the accrual of a *tort victim's* claim where he does not know (and could not have known) he was victimized or defrauded "to the date when he discovers he has been injured." *Cada*, 920 F.2d at 450. By its terms, it does not apply to Section 2462 where the Government is not a victim. Moreover, assuming discovery could ever be implied where a statute is silent, this Court has held that when a statute makes explicit exceptions to a statute of limitations, "additional exceptions are not to be implied." *TRW Inc. v. Andrews*, 534 U.S. 19, 28 (2001) (quotation marks and citation omitted). In Section 2462, "Congress explicitly enumerate[d] certain exceptions to [the] general prohibition," *id.*, that a claim

for penalties may not be brought more than five years after the violation, providing an exception where "the offender or the property is [not] found within the United States in order that proper service may be made thereon." 28 U.S.C. § 2462. Section 2462 also provides that the accrual-on-violation rule applies "[e]xcept as otherwise provided by Act of Congress"—thereby precluding the courts from implying their own court-made rules. *Id.* Finally, "Congress implicitly excluded a general discovery rule [for Investment Advisers Act claims] by explicitly including a more limited one," *TRW*, 534 U.S. at 28-29, providing that claims would accrue on discovery only when brought by a private plaintiff claiming damages. *See* 28 U.S.C. § 1658(b). There is no evidence that Congress intended to write an open-ended discovery rule into the Advisers Act for penalty claims when it did not allow injured private party—without the Government's powers of discovery—more than three years to bring a damages claim. *Accord Bartek*, slip op. at 6.

5. The Government wrongly argues the holding below is supported by "a background principle that presumptively governs the application of federal limitations statutes unless Congress specifies otherwise." Opp. 12. At the time Congress adopted the precursor to Section 2462 in 1839 (Act of Feb. 28, 1839, ch. 36, § 4, 5 Stat. 322), *Bailey* had not even been decided. *See TRW*, 534 U.S. at 37 (Scalia, J., concurring in the judgment) (discovery of "recent vintage"). Indeed, the "contemporary legal context" in which Section 2462 must be read, *Cottage Sav.*

Ass'n v. Comm'r of Internal Revenue, 499 U.S. 554, 562 (1991) (citation omitted), was expressed in *United States v. Maillard*, 26 F. Cas. 1140, 1143 (S.D.N.Y. 1871): a "court has no right or power to make [an exception to the statute of limitations], either directly, or by the indirect method of saying that the cause of action does not accrue, in case of a fraudulent concealment, until the discovery of the fraud." The background principle here is not the discovery rule, but that actions for "penalties . . . brought at any distance of time . . . would be utterly repugnant to the genius of our laws." *Adams v. Woods*, 6 U.S. (2 Cranch) 336, 342 (1805) (Marshall, C.J.). Pet. 29. The Government's failure to address this Court's long-standing hostility to untimely actions for penalties speaks volumes.

6. The Government argues, citing *Exploration Co. v. United States*, 247 U.S. 435, 435 (1918), that it does not "matter . . . that the Commission is the plaintiff [and] is seeking civil penalties." Opp 14. But *Exploration Co.* involved a claim by the Government, as defrauded landowner, to cancel (and require the defendants to disgorge) land patents that had been obtained from it as a result of fraud; the defendants did not just commit a fraud but also "for the period named in the statute . . . conceal[ed] their fraudulent action from the knowledge of the agents of the government." *Id.* at 449. It did not involve penalties or the discovery rule. The Court stated the rule thusly: "It is not our belief that Congress intended that the government should be deprived of title to public lands by those

who *add* to the fraud by which they were obtained *artifices which enable them to conceal the fraudulent manner in which they were secured until the action was supposed to be barred by the lapse of six years*." *Id.* at 449-50 (emphasis added).[6] *Exploration Co.* provides no support for the Government's contention that it can seek a penalty, rather than the return of a defendant's ill-gotten gains, for violation of an antifraud statute outside the five-year period on the mere allegations that it has stated a claim and could not have discovered that claim earlier.

7. Further, although the Government quotes *Bailey v. Glover*, 88 U.S. 342, 349-50 (1874) (Opp. 16), for the proposition that "the bar of the statute does not begin to run until the fraud is discovered, though there be no special circumstances or efforts on the part of the party committing the fraud to conceal it from the knowledge of the other party," the Court merely stated this was the view of other courts. 88 U.S. at 348. There, "the bill contain[ed] a distinct allegation that the defendants kept secret and concealed from the parties interested the fraud which [was] sought to be redressed"—fraudulent concealment. *Id.* at 348-49; *accord Bartek*, slip op. at 8 & n.4. As the Government has elsewhere acknowledged, *Bailey* thus rests on the familiar "equitable tolling" principle—not applicable here—that a defendant who frustrates the

[6] *Exploration Co.* thus contained precisely the allegations that the district court concluded—and the Government did not dispute—were missing here. *Compare* Pet. App. 39a.

plaintiff's ability to bring a timely claim may not complain when the claim is brought outside the limitations period. Brief for the SEC as Amicus Curiae at 29 n.44, *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*, 501 U.S. 350 (1991) (No. 90-333).[7]

8. Finally, the Government argues that "to bring an enforcement action like this one," the SEC must satisfy "the pleading standards for fraud," and that a court can "consider the passage of time" in setting a civil penalty. Opp. 17. But the Govern-

[7] The cases upon which the Government relies involve the doctrine of equitable tolling which the Government expressly disavowed here, which the district court held in an unappealed ruling did not apply, and which requires the plaintiff to plead and prove not just the elements of fraud but also that the defendant concealed a fraud or committed it in a self-concealing manner. *See Holland v. Florida*, 130 S. Ct. 2549, 2554 (2010) ("equitable tolling."); *John R. Sand & Gravel Co. v. United States*, 552 U.S. 130, 134-39 (2008) ("tolling"); *Irwin v. Department of Veterans Affairs*, 498 U.S. 89, 96 & n.4 (1990) (tolling; construing *Glus* and *Holmberg* as cases "where the complainant has been induced or tricked by his adversary's misconduct into allowing the filing deadline to pass"); *Glus v. Brooklyn E. Dist. Terminal*, 359 U.S. 232, 232-33 (1959) (equitable estoppel); *Holmberg v. Armbrecht*, 327 U.S. 392, 393 (1946) (defendant "concealed his ownership of one hundred shares of the Bank stock under [another name]"); *Sherwood v. Sutton*, 21 F. Cas. 1303, 1305, 1307 (C.C.N.H. 1828) (noting "the concealment of the fraud avoids the bar of the statute of limitations" and "[i]t is material to state, that the point is not, whether mere ignorance of the fact on the part of the plaintiff ought to remove the bar; but whether this ignorance, resulting from the fraudulent concealment of the fact by the defendant, ought to have that effect").

ment did not appeal the district court's ruling that the Complaint did not allege concealed or self-concealing conduct with particularity under Rule 9(b), Pet. App. 39a, and the rule it successfully urged the court to adopt does not require the Government to make such allegations—under that rule, any alleged fraud is, by definition, self-concealing. Pet. App. 21a.[8] The Government also does not get any benefit from the language of the applicable penalty provisions because those provisions increase a defendant's punishment, and do not decrease it, when the claim is for fraud. 15 U.S.C. §§ 78u-2(b), 80b-9(e)(2)(A).[9]

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[8] Regardless, the Government has taken the position that Rule 9(b) "does not apply to the SEC's claim under Rule 206(2), which is not scienter based and can be based on a showing of negligence." Brief of SEC at 6, *SEC v. Gruss*, No. 11 Civ. 2420 (RWS) (S.D.N.Y. Aug. 16, 2011).

[9] To the extent the Court believes the doctrinal differences are unimportant, we request it modify the question presented to whether penalty claims must be brought within five years of violation unless Congress expressly provides otherwise.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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