UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF FLORIDA

Case No. 0:11-Civ-62644-RNS

CARLOS ZELAYA, individually, and GEORGE GLANTZ, individually and as trustee of the GEORGE GLANTZ REVOCABLE TRUST, for themselves and on behalf of all those persons similarly situated,

Plaintiffs,

v.

UNITED STATES OF AMERICA,

Defendant.

/

PLAINTIFFS' OPPOSITION TO THE UNITED STATES OF AMERICA'S MOTION TO DISMISS THE COMPLAINT

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Dated: April 6, 2012

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INTRODUCTION

Plaintiffs hereby oppose the United States of America's Motion to Dismiss the Complaint (the "Motion"). This Court has subject matter jurisdiction over this action because the government fails to demonstrate that the discretionary function exception shields from liability the Securities and Exchange Commission's ("SEC") negligent failure to follow statutorily prescribed courses of action in the wake of its discovery of Robert Allen Stanford's Ponzi scheme.

The government's strategy on this Motion is to paint with a very broad brush. Thus, the government argues that "the manner in which the SEC chooses to regulate the securities industry" is discretionary conduct protected by the discretionary function exception in the Federal Tort Claims Act ("FTCA"), 28 U.S.C. § 2680(a). Generalized this way, the government's argument obviously cannot be contested. But framing the issue this way only creates a paper tiger. The conduct challenged in this case is not the SEC's regulation of the industry writ large, but rather its failure to comply with two specific, non-discretionary mandates. The government's over-generalization of the issue is an effort to move the battle to safer ground. This misdirection does not survive scrutiny.

Moreover, such a macro approach to the discretionary function exception results in the reverse of what Congress intended, which was to construe the remedial provisions of the FTCA liberally and the exceptions narrowly. If every claim against the SEC were to be construed as an attack on "the manner in which the SEC chooses to regulate the securities industry," then this narrow exception would swallow the general waiver and afford the SEC virtual immunity, contrary to Congress' intent. Indeed, as the government itself points out, Congress considered exempting the SEC from the FTCA entirely, but ultimately, did not do so.

Thus, the crucial first step in determining whether the exception applies is to isolate the specific conduct actually being challenged. Here, the Complaint does not make a broad attack on the manner in which the SEC regulates the securities industry, but rather, challenges two specific instances of SEC inaction: (1) a failure to notify the Securities Investor Protection Corporation ("SIPC") that U.S. registered broker-dealer Stanford Group Company "SGC") was in financial difficulty, after concluding that it was; and (2) a failure to deny continued registration to SGC as an investment advisor in light of the SEC's determination that SGC failed to satisfy registration requirements. Complaint, ¶¶ 4, 43, 60-61. These negligent omissions violated statutorily mandated duties to take prescribed courses of action and thus, were not and could not have been permissible policy choices. As the Supreme Court has explained and courts have consistently held, where there exists a mandatory responsibility, there is no room for a policy choice. Moreover, even if the government could show that the SEC's negligent omissions involved the exercise of judgment, the government also fails to demonstrate, as it must, that such judgment was grounded in considerations of public policy.

Instead of addressing the specific conduct at issue, the government falls back on generalities, arguing that the discretionary function exception should nevertheless apply here because "the manner in which the SEC chooses to regulate the securities industry" is "always susceptible to policy analysis"—although none is claimed to have been undertaken in this case. However, courts have consistently refused to rubber stamp the government's claim that all regulatory conduct falls within the discretionary function exception. Instead, courts look to the nature of the specific conduct actually being challenged and consider whether it: (1) involves an exercise of judgment and, if so; (2) whether it is additionally grounded in considerations of economic, social or political policy. To prevail on this Motion, the government must prove that the conduct being challenged by plaintiffs meets both of these criteria. Here, it fails to prove that it meets either of them.

The issues raised by this Motion are ones of first impression, despite the government's attempt to lump this case together with those that directly challenged when and how the SEC chose to investigate and prosecute wrongdoing.[1] No court has determined whether the SEC may be held liable for violating statutory directives to notify SIPC that SGC was in financial difficulty and to deny SGC amended registration as an investment advisor. Isolating exactly what conduct is at issue here, which is "the crucial first step" in deciding whether the complained of conduct was grounded in judgment or choice, *Rosebush v. United States*, 119 F3d 438, 441 (6th Cir. 1997), makes clear that the SEC negligently failed to follow prescribed courses of action in the wake of its discovery of Stanford's Ponzi scheme. These negligent omissions in no way challenge, or even implicate, the agency's discretionary authority over whether, when and how to investigate and prosecute Stanford, and are therefore cognizable under the FTCA. The government's Motion should be denied.

STANDARD OF REVIEW

On a motion to dismiss for lack of subject matter jurisdiction under Rule 12(b)(1), the Court must view the complaint in the light most favorable to the plaintiff, accept all factual allegations as true, and limit its consideration to the pleadings and any exhibits attached thereto. *See, e.g.*, *Jackson v. Okaloosa Cnty., Fla.*, 21 F.3d 1531, 1534 (11th Cir. 1991); *see also*, *Glover v. Liggett Group, Inc.*, 459 F.3d 1304, 1308 (11th Cir. 2006).

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[1] *See, e.g., Robert Juan Dartez, LLC v. United States*, No. 3:11-cv-0602N, ___ F. Supp.2d ___, 2011 WL 5529841, at *4 (N.D. Tex. Nov. 14, 2011) (claim that SEC failed to investigate Stanford entities at time and in manner that plaintiffs would have preferred directly implicated SEC's discretionary authority and was barred by discretionary function exception); *Molchatsky v. United States*, 778 F. Supp. 2d 421, 434 (S.D.N.Y. 2011) (SEC has broad discretion to decide how to conduct its investigations); *Dichter-Mad Family Partners LLP v. United States*, 707 F. Supp. 2d 1016, 1036 (C.D. Cal. 2011) (same).

To survive, a plaintiff need only "plead enough facts to state a claim to relief that is plausible on its face." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007); *James River Ins. Co. v. Ground Down Eng'g, Inc.*, 540 F.3d 1270, 1274 (11th Cir. 2008). A facially plausible claim is one where "the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1949 (2009). This plausibility standard "is not akin to a 'probability requirement,' but it asks for more than a sheer possibility that a defendant has acted unlawfully." *Id.* Facial plausibility exists "when the pleaded factual content allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Id*. The record must be reviewed "in the light of the principle that all doubts on jurisdictional points must be resolved in favor of plenary trial rather than dismissal at the pretrial stage." *Miller v. Central Chinchilla Group, Inc.*, 494 F.2d 414, 417 (8th Cir. 1974)).

Further, on a motion to dismiss for lack of subject matter jurisdiction on the ground that the government's conduct is shielded from liability by the discretionary function exception to the Federal Tort Claims Act, 28 U.S.C. § 2680(a), the government bears the burden of establishing that the discretionary function exception bars the plaintiff's claims. *See, e.g.*, *Sexton v. United States*, 132 F. Supp. 2d 967, 971-972 (M.D. Fla. 2000) (citing *National Union Fire Ins. v. United States*, 115 F.3d 1415 (9th Cir. 1997); *Autery v. United States*, 992 F.2d 1523 (11th Cir. 1993); *Carlyle v. United States*, 674 F.2d 554, 556 (6th Cir. 1982).

STATEMENT OF FACTS

Robert Allen Stanford created one of the largest Ponzi schemes in history through his Antiguan-based offshore bank, Stanford International Bank, Ltd. ("SIB") and registered broker-dealer, Stanford Group Company ("SGC"). Stanford created SGC in 1995, and registered the company with the SEC as a broker-dealer and investment adviser that same year. SGC amended its registration annually, going through virtually the identical process as for initial registration. Complaint, ¶¶ 27, 54.

After receiving several reports that SIB and SGC were part of an ongoing fraud, the SEC conducted multiple investigations of Stanford between 1997 and 2004, concluding after each investigation that he was operating a Ponzi scheme. The SEC took no action in response to that discovery until 2009, when it finally brought an enforcement action against him. Complaint, ¶¶ 28, 41.

A Ponzi scheme is, by its nature and as a matter of law, insolvent from inception to end.[2] Thus, the SEC knew after its investigation of Stanford that registered broker-dealer SGC was necessarily in or approaching financial difficulty, thereby triggering a mandatory statutory duty to notify SIPC of this fact. Complaint, ¶¶ 47-49. Further, all registered broker-dealers are required by the SEC to submit annual updating amendments to their registration. The SEC is mandated by statute to review those amendments and determine on an annual basis whether the requirements for registration—set forth in 15 U.S.C. § 80b-3—continue to be satisfied. When the requirements are not satisfied, the SEC is required to deny amended registration. Even though the SEC concluded, following its 2002 and 2004 investigations, that SGC was in violation of federal securities laws[3] and therefore had failed to satisfy the requirements for

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[2] *See, e.g.*, *Warfield v. Byron*, 436 F.3d 551, 558 (5th Cir. 2006) ("[A] Ponzi scheme ... is, as a matter of law, insolvent from its inception."); *In re Financial Fed. Title & Trust, Inc.*, 309 F.3d 1325, 1332 (11th Cir. 2002) (noting that by definition, a Ponzi scheme is driven further into insolvency with each transaction); *In re ATM Financial Services, Inc.*, Bankruptcy No. 6:08-bk-969-KSJ, 2011 Bankr. LEXIS 2394, 2011 WL 2580763, *6 (M.D. Fla. June 24, 2011) ("[T]here is little debate that a company run as a Ponzi scheme is insolvent as a matter of law").

[3] Specifically, the SEC concluded, after its 2002 investigation, that SGC was violating the anti-fraud provision of the Investment Advisors Act (15 U.S.C. § 80b-6) by failing to conduct any due diligence related to the SIBL CDs it was promoting to clients. Complaint, ¶ 55. After its 2004 investigation, the SEC concluded that SGC was willfully violating federal securities laws, including Rule 10b-5 and 10b-10 of the Securities Exchange Act of 1934 and Section 5 of the Securities Act of 1933. *Id.*, ¶ 56.

registration, the SEC failed to discharge its mandatory duty to deny SGC's amended registration as an investment advisor. Complaint, ¶¶ 43, 55-56.

ARGUMENT

I. THE GOVERNMENT FAILS TO MEET ITS BURDEN OF SHOWING EITHER THAT THE RELEVANT STATUTORY PROVISIONS CONFER DISCRETION ON THE SEC OR THAT ITS ACTIONS WERE OF THE KIND THAT ARE SUSCEPTIBLE TO POLICY ANALYSIS.

On a motion to dismiss for lack of subject matter jurisdiction based on the discretionary function exception, the government bears the burden of proving that the discretionary function exception applies to each of the negligent omissions being challenged by plaintiffs. *See, e.g.*, *GATX/Airlog Co. v. United States*, 286 F.3d 1168, 1173 (9th Cir. 2002), citing *Prescott v. United States*, 973 F.2d 696, 702 (9th Cir. 1992). "[W]hen determining whether the discretionary function exception is applicable, 'the proper question to ask is not whether the Government as a whole had discretion at any point, but whether its allegedly negligent agents did in each instance.'" *Id*. at 1174, citing *In re Glacier Bay*, 71 F.3d 1447, 1451 (9th Cir. 1995). The central question is whether, "at this stage of the case"—and under the standard of proof applicable at this stage—"the government has [or has] not established that choices exercised by government officials involved policy judgments." *Prescott*, 973 F.2d at 703.

The government does not and cannot meet its burden of showing that 15 U.S.C. § 78eee(a)(1) and § 80b-3(c) confer discretion on the SEC. Those provisions impose non-discretionary duties to act when specified circumstances exist, as they did here. *See* 15 U.S.C. § 78eee(a)(1) ("If the Commission … is aware … that any broker or dealer subject to its regulation is in or is approaching financial difficulty, it ***shall*** immediately notify SIPC[.]"); 15 U.S.C. § 80b-3(c) ("The Commission ***shall*** deny such registration if it does not make [find that the requirements of this section are satisfied] or if it finds that if the applicant were so registered, its registration would be subject to suspension or revocation under subsection (e) of this section.") (emphasis added).

The government also fails to meet its burden of showing that any policy analysis played a role in the SEC's decision to disregard those statutory mandates. In fact, the government does not offer a single policy consideration that did influence, or even could have influenced, the SEC's failure to notify SIPC that SGC was in financial difficulty and its failure to deny SGC's amended registration. This is fatal to the government's Motion. *See Lashley v. United States*, No. C 05-03288 (WHA), 2006 U.S. Dist. LEXIS 73667, *14 (N.D. Cal. Sept. 26, 2006) (rejecting discretionary function exception where "there was no evidence, nor any suggestion, that the governmental decisions were the products of policy considerations.").

II. THE GOVERNMENT FAILS TO SHOW THAT THE SEC'S NEGLIGENT OMISSIONS SATISFY THE TWO-PRONG TEST TO DETERMINE WHETHER GOVERNMENT CONDUCT FALLS WITHIN THE DISCRETIONARY FUNCTION EXCEPTION.

The Supreme Court has instructed that the waiver of sovereign immunity in the FTCA should be construed liberally, and further, that any exceptions to that waiver, including the discretionary function exception, should be construed narrowly. *See Dolan v. United States Postal Serv.*, 546 U.S. 481, 491 (2006); *O'Toole v. United States*, 295 F.3d 1029, 1037 (9th Cir. 2002) (holding that "in order to effectuate Congress's intent to compensate individuals harmed by government negligence, the FTCA, as a remedial statute, should be construed liberally, and its exceptions should be read narrowly").

With those principles in mind, the Supreme Court has established a two-part test to determine whether a government employee's action or omission falls within the discretionary function exception. Both prongs are subject to the narrowest construction in applying the facts of this case. First, the conduct at issue must "involve[ ] an element of judgment or choice."

Berkovitz v. United States, 486 U.S. 531, 536 (1988). If "a federal statute, regulation, or policy specifically prescribes a course of action for the employee to follow," then the employee can be held liable for failing to follow the prescribed directive. *U.S. v. Gaubert*, 499 U.S. 315, 322 (1991). Second, if the conduct at issue involves the exercise of judgment, the Court must then determine whether that judgment is grounded in considerations of public policy. Only if both parts of the test are satisfied does the discretionary function exception apply. *Id*. at 322-23.

With respect to the first part of the test, a federal statute, regulation or policy may still impose a mandatory directive even where it requires an element of judgment or choice about how to comply with that directive. The inquiry focuses on whether the controlling statute or regulation prescribes a course of action embodying a "fixed or readily ascertainable standard." *Autery v. United States*, 992 F.2d 1523, 1529 (11th Cir. 1993). "If the standard, however, is clear, the government official may maintain discretion over how to meet that standard, without retaining discretion over whether or not to do so." *Downs v. United States*, 2009 U.S. App. LEXIS 11166, *5 (11th Cir. May 27, 2009). *See also Aslakson v. United States*, 790 F.2d 688, 693 (8th Cir. 1986) (policy requiring Western Area Power Administration to elevate its power lines if they constituted a safety hazard imposed a mandatory directive even though the question of what constituted a safety hazard involved the exercise of judgment).

With respect to the second part of the test, the challenged act must be objectively one that would be expected to be grounded in considerations of policy. *See Autery*, 992 F.2d at 1530-31. Thus, "when properly construed, the exception 'protects only governmental actions and decisions based on considerations of public policy.'" *Gaubert*, 499 U.S. at 323, quoting *Berkovitz*, 486 U.S. at 537. Finally, as noted above, the exception must be construed narrowly. *See Dolan*, 546 U.S. at 491; *O'Toole*, 295 F.3d at 1037 ("in order to effectuate Congress's intent to compensate individuals harmed by government negligence, the FTCA, as a remedial statute, should be construed liberally, and its exceptions should be read narrowly").

The SEC violated controlling statutory directives by failing to notify SIPC that SGC was in financial difficulty and by failing to deny SGC continued annual registration as an investment advisor. These negligent failures to follow prescribed courses of action involved no element of judgment or choice. Even if there had been some judgment or choice involved, it was not one based on considerations of public policy. Thus, the discretionary function exception does not bar plaintiffs' claims and the government's motion to dismiss should be denied.

A. The SEC Had A Mandatory Statutory Duty To Notify SIPC That SGC Was In Financial Difficulty And Its Decision Not To Do So Is Not Susceptible To Policy Analysis.

1. Determining that SGC was in financial difficulty was not discretionary.

The SEC, after conducting several investigations of Stanford, concluded that Stanford was operating a Ponzi scheme and that the funds invested in the scheme were used, in part, to operate SGC. Because Ponzi schemes are, by definition and as a matter of law, insolvent operations, the SEC knew and believed that SGH was in or approaching financial difficulty. Complaint, ¶¶ 46-48. That knowledge of Stanford's scheme triggered a mandatory duty under 15 U.S.C. § 78eee(a)(1) to notify SIPC that SGH was in financial difficulty. Section 78eee(a)(1) provides, in pertinent part, as follows:

> If the Commission … is aware of facts which lead it to believe that any broker or dealer subject to its regulation is in or is approaching financial difficulty, it shall immediately notify SIPC ….

The SEC failed to notify SIPC of this fact and that failure proximately caused plaintiffs' losses. Complaint, ¶ 61-62, 64.

The government appears to concede that Section 78eee(a)(1) is a mandatory directive, but argues that the discretionary function exception should still apply because whether a broker or dealer is in or is approaching financial difficulty is "an inherently subjective determination" that involves an element of judgment, and hence, discretion. Motion at 10. Here, the government attempts (and fails) to unleash its paper tiger, focusing on a point in the regulatory process—the investigation, process, and thinking that led up to the SEC's conclusion that SGC was in financial difficulty—that is irrelevant because the claim here focuses only on what failed to happen <u>after</u> that point. *See, e.g.*, *GATX/Airlog Co. v. United States*, 286 F.3d 1168, 1173 (9th Cir. 2002), citing *Prescott v. United States*, 973 F.2d 696, 702 (9th Cir. 1992). "[W]hen determining whether the discretionary function exception is applicable, 'the proper question to ask is not whether the Government as a whole had discretion at any point, but whether its allegedly negligent agents did in each instance.'" *Id*. at 1174, citing *In re Glacier Bay*, 71 F.3d 1447, 1451 (9th Cir. 1995). In each instance complained of here, SEC agents negligently failed to discharge mandatory duties that arose <u>after</u> the SEC concluded that SGC was in financial difficulty. Having concluded Stanford was operating a Ponzi scheme, subjectivity evaporated, and the SEC's obligation to notify SIPC became fixed and clear.

In any event, even as to its own misguided inquiry, the government's argument fails. Determining "financial difficulty" requires no judgment, subjective or otherwise. It is an accounting formula. The government counters, without support, that determining "financial difficulty" is a discretionary function because "financial difficulty" is nowhere defined, and, thus, there is no fixed or readily ascertainable standard. This implausible position should be rejected.

The SEC has itself provided a readily ascertainable standard for "financial difficulty" and established a formula that it has applied in making that determination in other contexts. Specifically, in 1975, the SEC promulgated a net capital rule (SEC Rule 15c3-1) to establish uniform net capital standards for brokers and dealers registered with the SEC. Almost all broker-dealers must comply with this liquidity standard, which requires broker-dealers to perform two computations: one to determine net or liquid capital, and one to determine minimum net capital or base capital requirements. In addition to this liquidity standard, the SEC has also established "early warning levels of capital" to "alert SEC … to the fact that a broker-dealer is experiencing financial difficulty (i.e., the broker-dealer's net capital is dropping toward its minimum requirement…." *See* SEC Rule 15c3-1 (SEC Net Capital Rule) and Key SEC Financial Responsibility Rules at Appendix 11, pp. 135-36. These rules provide one readily ascertainable standard for determining "financial difficulty."

Moreover, a fixed or readily ascertainable standard needs no definitions or formulas. It need only, as the words suggest, provide a standard by which the government's conduct can be measured. *See Miller v. United States*, 710 F.2d 656, 663 (10th Cir. 1983), citing *Barton v. United States*, 609 F.2d 977, 979 (10th Cir. 1979). Thus, examples of fixed or readily ascertainable standards without definitions or formulas include: (1) a National Park Service requirement that park roads "conform to the original grades and alignments" and that graded roads be "Firm [and] uniform cross section" (*ARA Leisure Services v. United States*, 831 F.2d 193, 195 (9th Cir. 1987)); (2) an Everglades National Park policy requiring employees to inspect a park boat ramp daily and wash "when needed" and "to identify, report, and mitigate hazardous conditions" (*Sakal v. United States*, 2010 U.S. Dist. LEXIS 101826, *4, 9-10 (S.D. Fla. June 14, 2010)); (3) an Army Corps of Engineers' duty to conduct "field safety inspections every time they visit a construction site" and "take necessary action to insure that corrective measures are taken as needed" (*Philips v. United States*, 956 F.2d 1071, 1073, 1076 (11th Cir. 1992)); (4) the duty of the Forest Service to "notify the Contractor of any noncompliance with these requirements and of the corrective action required" (*Routh v. United States*, 941 F.2d 853, 854, 857 (9th Cir. 1991), citing *Kennewick Irrigation District v. United States*, 880 F.2d 1018 (9th Cir. 1989)); (5) the term "non-rocky, sandy material similar to that of the existing beach" (*Downs v. United States*, No. 06-20861-CIV-HUCK/O'SULLIVAN, 2010 U.S. Dist. LEXIS 83196, at *19 (S.D. Fl. Aug. 16, 2010)); and (6) "accepted industry practice," which the court noted "is not defined in the regulations," but "places a specific, mandatory obligation on the government. The definition of accepted industry practice can be easily ascertained by the district court" (*Baker v. San Carlos Irrigation Project Dist.*, No. 02-15086, 58 Fed. Appx. 303, 2003 U.S. App. LEXIS 3353 (9th Cir. Feb. 21, 2003)). A standard for "financial difficulty" can be as easily ascertained by this Court as was the standard for "accepted industry practice" at issue in *Baker*.

In short, Section 78eee(a)(1) prescribes a specific course of action to follow when the SEC believes, as it did here, that SGC met the readily ascertainable standard of "in or approaching financial difficulty." The SEC must notify SIPC of this fact. The SEC's failure to do so did not, therefore, involve an element of judgment or choice and is therefore not within the discretionary function exception.

The government makes a strained argument that all conduct pursuant to Section 78eee is discretionary, and therefore protected, because parts of that section grant the SEC and SIPC discretion about whether to take action against a financially ailing broker-dealer and what action to take. Again, the government focuses on the wrong stage in the process, attempting to insert discretion that may exist <u>after</u> the SEC had already violated its duty by negligently failing to notify SIPC. Thus, the presence of discretion in Section 78eee about what action to take, if any, against a financially failing broker-dealer <u>after</u> SIPC has been notified as required does not prove—and is irrelevant to demonstrating—that the obligation to notify SIPC in the first place is discretionary as well. *See Collins v. United States*, 783 F.2d 1225, 1229 n.3 (5th Cir. 1986) ("We disagree … however, that the presence of discretion in any aspect of the regulatory process means that at any stage of it, negligent conduct is within [the discretionary function exception]."). The government's suggestion that notification of SIPC may not have led to any action against SGC is an improper attempt to cast doubt on the causal connection between the SEC's negligence and plaintiffs' losses. On a motion to dismiss, plaintiffs are entitled to the reasonable inference that SIPC or the SEC would have taken some action against SGC.

2. <u>Any judgment exercised by the SEC was not grounded in public policy considerations, and therefore falls outside the discretionary function exemption.</u>

Even if notification of SIPC under Section 78eee(a)(1) involves some element of judgment or choice, which it does not, the government fails to demonstrate, as required, that any choice or judgment exercised by the SEC in this case was grounded in considerations of public policy. *See Drake Towing Company, Inc. v. Meisner Marine Construction Co.*, 765 F.2d 1060, 1064 (11th Cir. 1985) (citations omitted) ("For the government to show merely that some choice was involved in the decision-making process is insufficient to activate the discretionary function exception. The balancing of policy considerations is a necessary prerequisite."); *see also Gaubert*, 499 U.S. at 322-23 (if the conduct at issue involves exercise of judgment, court must determine whether that judgment is grounded in policy considerations because only policy judgments are protected by discretionary function).

Thus, for example, in *Aslakson v. United States*, 790 F.2d 688, 693 (8th Cir. 1986), the policy at issue required the Western Area Power Administration to elevate its power lines if they constituted "a safety hazard." The court held that WAPA's determination that the power lines over Creel Bay were not a safety hazard was not the kind of judgment that involved weighing public policy considerations, but rather, required experience and professional expertise, and was therefore not immunized from judicial review as a discretionary function. *See also Hendry v. United States*, 418 F.2d 774, 783 (2d Cir. 1969) (Public Health Service doctor's judgment that seaman employed by Merchant Marines was paranoid schizophrenic was a professional expert judgment, not the kind of policy judgment shielded from judicial review by the discretionary function exception); *Griffin v. United States*, 500 F.2d 1059, 1066 (3d Cir. 1974) ("Where the conduct of Government employees in implementing agency regulations requires only performance of scientific evaluation and not the formulation of policy, we do not believe that the conduct is immunized from judicial review as a 'discretionary function.'"), cited with approval in *Alabama Electric Cooperative, Inc. v. United States*, 769 F.2d 1523, 1529-30 (11th Cir. 1985) ("we think that *Griffin* is consistent with the *Varig Airlines* decision.").

The determination of "financial difficulty," to the extent that it involves an exercise of judgment at all, requires accounting expertise, not the weighing of public policy considerations. Indeed, as noted above, the government has failed to come forward with any policy considerations that might have influenced or could influence the determination of whether to notify SIPC that a broker-dealer is in financial difficulty.

B. The SEC Had A Mandatory Statutory Duty To Deny SGC Continued Registration As An Investment Advisor And The Failure To Do So Was Not A Policy Judgment.

SGC applied to become a registered broker-dealer and investment advisor in 1995 and was registered by the SEC that same year. Every year thereafter, through 2009, SGC was required to and did file an updated and amended registration and was re-registered by the SEC in each of those years. Complaint, ¶ 54. Under 15 U.S.C. § 80b-3(c), the SEC had a mandatory statutory duty to determine annually whether SGC and other registered investment advisors continued to satisfy the requirements for registration and to deny amended registration to those investment advisors that did not. Complaint, ¶ 52. The SEC violated that mandatory statutory duty by failing to deny amended registration to SGC after its investigation revealed that SGC could not meet the requirements for registration under Section 80b-3 because SGC was violating the anti-fraud provisions of the Investment Advisors Act of 1940 and willfully violating federal securities laws. Complaint, ¶ 58. Such a finding requires the SEC to deny registration or amended registration to a broker-dealer. 15 U.S.C. § 80b-3(c).

15 U.S.C. § 80b-3 sets forth the statutory scheme for regulating investment advisors. In general, investment advisors that use the mail or other instrumentalities of interstate commerce in connection with their business must be registered with the SEC. To register, an investment advisor must file an application with the SEC. That application consists of a Form ADV (*see* 17 C.F.R. 279.1). Once registered, an investment advisor is required to submit an "*annual updating amendment* to your registration"—which consists of the same Form ADV—within 90 days of the end of their fiscal year. *See* Form ADV, Part 1A (emphasis in original); 17 C.F.R. 275.204; SEC Rule 204-1.

15 U.S.C. § 80b-3(c), by express reference, governs the "[p]rocedure for registration; filing of application; effective date of registration; amendment of registration." This subsection prescribes a specific course of action that the SEC must follow in acting on applications for registration and amendments of registration and directs the SEC to grant registration if it finds that the requirements are satisfied and to deny registration if it does not. *Id*.

The government argues that, under Section 80b-3(c), investment advisors, once registered, are not required to undergo a similar application process to re-register on an annual basis. This is patently false. Indeed, the government cites no support for that assertion and it is wholly at odds with both the language of the statute and the process set forth therein. By SEC regulation and rules, all registered investment advisors are required to submit a Form ADV as their initial application for registration and the very same form as an "*annual updating amendment*" to their registration, subject to the very same examination and approval process. *See* Form ADV, Part 1A (emphasis in original); 17 C.F.R. 275.204; SEC Rule 204-1. In short, under the SEC's own rules and regulations, the re-registration or amended registration process is identical to the initial application process, requiring reapplication annually.[4]

Under the mandatory directive in Section 80b-3(c), the Commission: "shall grant" amended registration if it finds that the requirements of Section 80b-3 are satisfied and "shall deny" amended registration if no such finding is made. 15 U.S.C. § 80b-3(c). Indeed, requiring a Form ADV on an annual basis, and sometimes, even more frequently than that, enables the SEC to discharge its mandatory duty to determine registered investment advisors' ongoing compliance with the requirements of Section 80b-3. The registration and amended registration process is an integral part of the regulatory scheme and essential for the protection of investors. The government's unsupported assertion to the contrary is unavailing.

Finally, the government, once again, focuses on the wrong stage of the regulatory process, arguing that because the SEC has enforcement discretion under subsection (e), it must also have discretion with respect to registration under subsection (c). This argument is equally unavailing because proof that the SEC has discretion in some aspect or at some stage of the regulatory process does not prove that negligent conduct falls within the discretionary function exception at every stage. *See Collins*, 783 F.2d at 1229 n.3. Section 80b-3 treats the SEC's registration duties separately from its enforcement duties, and therefore, so must the Court.[5]

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[4] After all, 15 U.S.C. § 80b-3(c), by express reference, applies to "amendments to registration."

[5] The government does not argue that SGC's annual amended registration as an investment advisor reflected any policy choice on the part of the SEC. To the contrary, the government denies that the SEC made a choice at all, arguing instead that amended registration is pro forma. Either way, this Court need not consider the second prong of

Because the registration duties, viewed appropriately in isolation from the SEC's broad enforcement powers, do not involve discretion or policy judgments, the discretionary function exception does not apply, and the government's motion to dismiss must be denied.

CONCLUSION

For all of the foregoing reasons, plaintiffs respectfully request that the Court deny the United States of America's Motion to Dismiss the Complaint in its entirety.

Dated: April 6, 2012

KACHROO LEGAL SERVICES, P.C.

By: /s/ Brandon R. Levitt
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the Supreme Court's discretionary function test, namely, whether that choice, if there was one, was grounded in public policy. *See Gaubert*, 499 U.S. at 322-23.

CERTIFICATE OF SERVICE

I, Brandon R. Levitt, hereby certify that on April 6, 2012, a true and correct copy of the foregoing opposition was served upon all the parties of record by the Court's CM/ECF system.

Dated: April 6, 2012

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