IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Securities and Exchange Commission, Plaintiff/Applicant,	)	Misc. No. 11-MC-678-RLW
v.	)	
Securities Investor Protection Corporation, Defendant/Respondent.	)	Oral Hearing Requested Under LCvR 7(f)

SECURITIES INVESTOR PROTECTION CORPORATION'S
(1) MOTION TO STRIKE SECURITIES AND EXCHANGE COMMISSION'S *EX PARTE* MOTION FOR ORDER TO SHOW CAUSE, AND (2) MOTION FOR RULE 16 CASE MANAGEMENT CONFERENCE ON SEC'S "APPLICATION" FOR ORDER REQUIRING SIPC TO INITIATE LIQUIDATE PROCEEDING

On December 12, 2011, the Securities and Exchange Commission filed what it described as an unprecedented lawsuit to require the Securities Investor Protection Corporation ("SIPC") to start a liquidation proceeding on over $1 billion in alleged claims relating to the Allen Stanford fraud. In so doing, the SEC also filed an *ex parte* motion for an order to show cause in the case, arguing that the "regular rules of civil procedure do not apply" (SEC's *Ex Parte* Mot. at 2) and that its position on the merits of the case is "not subject to judicial review" (SEC's Mem. of Pts. and Auth. in Supp. of App. at 4). For the reasons discussed in the accompanying Memorandum of Points and Authorities, SIPC, through the undersigned counsel of record, respectfully submits this Motion to Strike the SEC's *Ex Parte* Motion for Order to Show Cause, and also moves for a Rule 16 Case Management Conference so that the parties can present their views on the appropriate next steps in this unprecedented case.

SIPC received the SEC's papers initiating this case shortly before 5:00 PM on Monday, December 12, 2011. The undersigned outside counsel for SIPC contacted the SEC's counsel (Messrs. Martens and Mendel) that evening to ask whether the SEC would oppose having a Rule 16 Case Management Conference as the appropriate next step in the case. Although the parties are still conferring on that question, SIPC is constrained to submit these motions given the SEC's express attempt in its papers to proceed *ex parte*.

Dated: December 13, 2011

Respectfully submitted,

/s/ Eugene F. Assaf

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December 13, 2011

INTRODUCTION

The Securities and Exchange Commission's ("SEC's") *ex parte* motion for an order to show cause—like the "application" for a liquidation proceeding that it has filed in lieu of an actual Complaint—is an extraordinary example of over-reaching. This proceeding is literally unprecedented: in the 40 years since its enactment, the SEC has never before invoked the judicial review provisions of 15 U.S.C. § 76ggg(b). Seeking to take advantage of that vacuum, the SEC makes the astonishing claim that it need only file an "application" that is "not subject to judicial review" and for which the "regular rules of civil procedure do not apply." (Dec. 12, 2011 SEC's Mem. of Pts. and Auth. in Supp. of App. ("SEC Mem.") at 4, 30; *see also* Dec. 12, 2011 SEC's *Ex Parte* Motion at 2.) The problem for the SEC, however, is that nothing in the Securities Investor Protection Act ("SIPA") entitles it to dispense with the Federal Rules of Civil Procedure just on its say-so, or to employ an Article III Court to rubber-stamp the agency's position without any judicial review of whether that position is right. Simply put, there is no basis for this Court to use heretofore unheard of summary proceedings to require the Securities Investor Protection Corporation ("SIPC") to launch a liquidation proceeding on over *$1 billion* in CDs issued by an offshore bank that is not a SIPC member. Indeed, the approach urged by the SEC would be squarely at odds with the decisions of other courts giving minimal deference to the SEC's interpretations of SIPA. No court has ever authorized that sort of "shoot first, ask questions later approach"—especially in an unprecedented dispute between SIPC and the SEC, and this Court should not be the first to do so.

To be clear, there is a reason why the SEC wants to avoid judicial scrutiny and to obtain relief based only on its say-so: because the SEC cannot prevail under any serious analysis of the facts and the law in this case. The SEC knows that Congress created SIPC to protect the delivery of missing cash or securities in the custody of failing or insolvent SIPC-member brokerage firms, whereas this case involves investments in CDs from an Antiguan bank that was not a SIPC member. Under the statute, SIPC does not guarantee an investment's value or protect against fraud, and SIPC does not cover investments with offshore banks or other non-member firms.

The implications of this case are far-reaching. Because this is the first lawsuit initiated by the SEC against SIPC, this case presents important statutory construction questions that will impact the investing public as well as the financial markets, and could result in billions of dollars of exposure. In short, it is decidedly not the type of case that should be decided in an expedited fashion without the full and fair deliberative process afforded under the Federal Rules of Civil Procedure. For these reasons and as explained below, SIPC respectfully moves to strike the SEC's *ex parte* motion for an order to show cause, and also moves for a Rule 16 Case Management Conference so that the parties' counsel can present their views on the appropriate next steps in this unprecedented high-stakes dispute.

BACKGROUND

The SEC has brought suit against SIPC, demanding that it liquidate claims for investors who purchased offshore Certificates of Deposit from the Stanford International Bank Ltd. in Antigua ("Stanford Antiguan Bank"). SIPC is a private, non-profit corporation created by the SIPA statute, with policies set by a seven-member Board of Directors (five of whom are appointed by the President of the United States and confirmed by the Senate and two of whom, respectively, are from the Treasury and the Federal Reserve). 15 U.S.C. § 78ccc(c)(1) and (2).

Because SIPA offers only limited protection against the loss of missing cash or securities in the custody of failing or insolvent SIPC-member brokerage firms, SIPC has determined it may not commence a liquidation proceeding in the Stanford matter—including because the Stanford Antiguan Bank is not a SIPC member, and because this case is about CDs that were delivered, not a situation in which a SIPC-member brokerage firm had custody of securities but failed before delivery could occur.

Where legally proper, in cases such as Lehman Brothers, Madoff and MF Global—cases actually covered by the statute—SIPC has not hesitated to promptly commit billions of dollars of funds. In the case of the Stanford matter, however, SIPC explained to a Receiver in August 2009 why there was no lawful basis for initiating a liquidation proceeding here. The SEC voiced no disagreement for nearly two years (indeed, its own General Counsel at the time agreed with SIPC). It was only in June 2011 that the SEC abruptly reversed course, after two nominees to become SEC Commissioners were poised for confirmation but a member of Congress announced that he would block their nominations until the SEC decided whether to refer the Stanford matter to SIPC for the commencement of a liquidation proceeding.[1] The next day, the SEC notified SIPC that it would "bring a court action against SIPC" if SIPC did not initiate a proceeding. (*See* June 15, 2011 Letter from E. Murphy of the SEC to O. Johnson of SIPC (attached as Ex. 2 to Declaration of Matthew T. Martens) at 1).[2]

Over six months later, the SEC has filed this lawsuit, in which it seeks *ex parte* treatment, claims that its position is "not subject to judicial review by this Court," and asserts that the "regular rules of civil procedure do not apply" to its demands. (SEC Mem. at 4; SEC's *Ex Parte* Motion at 2.) SIPC respectfully disagrees and files this motion accordingly.

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[1] *See* June 14, 2011 Senator David Vitter Press Release, available at http://www.vitter.senate.gov/public/index.cfm?FuseAction=PressRoom.PressReleases&ContentRecord_id=8f2e65df-802a-23ad-458d-e0eb0391d4ef&Region_id=&Issue_id= (Vitter to Block SEC Nominees Until Stanford Victims Get Answers).

[2] *See also* June 11, 2011 Senator David Vitter Press Release, *available at* http://vitter.senate.gov/public/index.cfm?FuseAction=PressRoom.PressReleases&ContentRecord_id=94d9898a-e3f7-d209-fd93-8135fd77c2b8 ("[SEC] Ruling on SIPC coverage comes day after Vitter blocked SEC nominations.").

ARGUMENT

First, there is no basis for proceeding *ex parte*—especially against a party with whom the SEC has been dealing for years, and whom it knows to be represented by counsel. "[C]ourts routinely express their disfavor with *ex parte* proceedings and permit such proceedings only in the *rarest* of circumstances," which "are both few and tightly contained." *United States v. Libby*, 429 F. Supp. 2d 18, 21 (D.D.C. 2006) (emphasis added); *see also Berntsen v. C.I.A.*, 511 F. Supp. 2d 108, 110 (D.D.C. 2007) (recognizing three exceptions to a prohibition on *ex parte* proceedings, including "(1) where materials are submitted for inspection by the Court because a party seeks to prevent their use in litigation; (2) where the government has made a demonstration of compelling national security concerns; or (3) where such review is specifically contemplated by statute") (internal citation and quotation omitted). The SEC has not argued—because it cannot argue—that any of those exceptions is remotely applicable here.

Second, the SEC's resort to a show cause procedure is a particularly inappropriate attempt to place the burden of proof on *SIPC* to demonstrate why it should *not* be ordered to start a liquidation proceeding. The SEC has it exactly backwards and would turn SIPA on its head—it is the *SEC's burden* to prove that SIPC has failed to discharge its obligations under SIPA. 15 U.S.C. § 78ggg(b) does not grant the SEC plenary authority to require SIPC to institute a liquidation proceeding. It merely provides what the Supreme Court correctly described as a "*right of action*." *SIPC v. Barbour*, 421 U.S. 412, 421 & n. 3 (1975) (describing section 78ggg(b) as "governing *suits* to compel the SIPC to act for the benefit for investors") (emphasis added). Section 78ggg(b) in turn requires the SEC to prove that SIPC is not "discharg[ing] its obligations under" the statute. *Id*. § 78ggg(b). Put differently, *before* the Court may enter an order directing SIPC to initiate a proceeding, the SEC must prove that SIPC has, in fact, refused "to act for the protection of customers of any member of SIPC." *Id*.

Third, the SEC seeks to disregard this threshold obligation by declaring it unreviewable by this Court. The SEC's position is utterly unprecedented—while seeking an order from this Court, it simultaneously argues that this Court has no authority whatsoever to exercise "judicial review" of the very issue before the Court. Instead, the SEC insists that it may simply file an "application" and circumvent what the Federal Rules of Civil Procedure require—including (among other things) filing a complaint, conducting discovery, and filing/responding to dispositive motions—and instead use a "summary proceeding against SIPC" in which the Court does nothing but rubber-stamp the SEC's position. (SEC Mem. at 29; *see also id*. at 30 ("[T]he regular rules of civil procedure do not apply.").)

Specifically, the SEC argues that its determination that there are "customers" that warrant SIPC protection "is not subject to judicial review by this Court." (SEC Mem. at 4.) That is an astonishing proposition. To accept the SEC's position would mean that Congress created a judicial review provision in SIPA in which the Court does not "review" anything, but instead simply rubber-stamps the SEC's decision on its say-so. If that were Congress's intent, it could have directly provided for the SEC to order SIPC to initiate a proceeding—there would have been no reason to involve the courts at all. Yet that is not what Section 78ggg(b) says, in stark contrast to other provisions of SIPA, which give the SEC an unequivocal right to compel SIPC to undertake other types of specific actions. Section 78ccc(e)(3), for example, states that "the Commission may … *require* SIPC to adopt, amend, or repeal any SIPC bylaw or rule, whenever adopted." 15 U.S.C. § 78ccc(e)(3) (emphasis added); *see also id*. § 78ggg(c)(1) ("The Commission may … *require* SIPC to furnish it with such reports and records or copies thereof as the Commission may consider necessary or appropriate in the public interest …." (emphasis added)). Far from entitling the SEC to an order just on its say-so or to flip the burden of proof on

SIPC, Section 78ggg(b) requires the SEC to prove that SIPA has "obligations" that it has failed to "discharge." Unless and until the SEC can make that showing, there is no basis for an Article III court to make findings to that effect.

The SEC relies on cases from the APA context, in which courts rejected challenges brought *against an agency* on the grounds that its actions are "committed to agency discretion by law," 5 U.S.C. § 701(a). Those cases are entirely irrelevant. This is not a case where a party seeks to challenge a decision committed to an agency's discretion. Rather, it is the SEC that seeks to have this Court render a decision that will impose the SEC's will on a third party. It makes no sense to say, as the SEC in effect does, that an agency's decisions are unreviewable but nonetheless judicially enforceable. Section 78ggg(b) did not transform the courts into mere instrumentalities of the SEC.

It is understandable why the SEC seeks to avoid the Federal Rules of Civil Procedure and the fundamental protections that they afford defendants—it knows full well that if put to the test it cannot possibly meet its burden before this Court on the merits. Thus, the SEC tries to analogize to other proceedings in which Courts have permitted summary resolution, but those cases actually show why the SEC's requested approach fails. In *SEC v. McCarthy*, 322 F.3d 650 (9th Cir. 2003), on which the SEC mistakenly relies in its papers, the Ninth Circuit permitted a summary proceeding to enforce an SEC order precisely because the matter *had been previously adjudicated*: "Summary proceedings are particularly appropriate where the merits of the dispute have already been litigated extensively before the NASD, the Commission, and on appeal to a circuit court, *where the only remedy sought is enforcement of the previously upheld order*." *Id.* at 657 (emphasis added). Here, of course, there has been no adversarial adjudication, much less one that an Article III court previously reviewed. There is no record. There have been no findings. Instead, the SEC's self-styled "application" is based on nothing more than a letter that it sent to SIPC six months ago, which, in turn, was based on allegations and innuendo with no formalized or meaningful proceedings of any kind. Make no mistake; what the SEC seeks is nothing less than a fait accompli.

The SEC's reliance on *New Hampshire Fire Ins. Co. v. Scanlon*, 362 U.S. 404 (1960), is similarly mystifying. There the Supreme Court rejected the plaintiff's attempt to circumvent the Federal Rules by filing a "petition" rather than a complaint, and held that summary proceedings were "the exception in our method of administering justice." *Id*. at 406. In language salient here, the Court observed:

> [T]he Federal Rules of Civil Procedure provide the normal course for beginning, conducting, and determining controversies. Rule 1 directs that the Civil Rules shall govern all suits of a civil nature, with certain exceptions stated in Rule 81 none of which is relevant here. Rule 2 directs that "There shall be one form of action to be known as 'civil action.'" Rule 3 provides that "A civil action is commenced by filing a complaint with the court." Rule 56 sets forth an expeditious motion procedure for summary judgment in an ordinary, plenary civil action. Other rules set out in detail the manner, time, form and kinds of process, service, pleadings, objections, defenses, counterclaims and many other important guides and requirements for plenary civil trials. The very purpose of summary rather than plenary trials is to escape some or most of these trial procedures.

Id. Although the SEC tries to distinguish between "actions" and "applications," the Supreme Court drew no such distinction when opining on SIPA's judicial review provisions in *SIPC v. Barbour*. Tellingly, the SEC completely disregards the Supreme Court's description of section 78ggg(b) as "governing *suits* to compel the SIPC to act for the benefit for investors." *Barbour*, 421 U.S. at 421 n.3 (emphasis added). Likewise in *Barbour*, the Court specifically relied on the SEC's "*right of action*" against SIPC as grounds for finding SIPA did not provide a private cause of action. *Id*. at 421 (emphasis added). And in its June 15, 2011 Letter to SIPC, the SEC itself characterized 78ggg(b) as authorizing it to "bring a court *action* against SIPC" if SIPC did not initiate a liquidation proceeding. The SEC, however, would simply ignore the Supreme Court's characterization of SIPA, as well as its own earlier characterization, in favor of its new unprecedented approach.

At bottom, nothing in SIPA supports a rush to judgment based only on the SEC's say-so. The Court should reject the SEC's attempt to have this entire proceeding resolved in response to an unprecedented *ex parte* show-cause motion. Instead, the Court should strike the motion and set an initial Case Management Conference to address the SEC's application and the proper nature of proceedings that should follow.

* * * *

With all respect to the SEC's position, SIPC submits that the SEC's resort to demanding *ex parte* relief and abbreviated procedures is telling, because litigants ordinarily do not seek to bypass the rules if they are confident of their claims on the merits. Whatever the SEC's motivation for its approach may be, however, it cannot seriously deny that it is asking the Court to take an extraordinary position. This Court need not and should not go down that unprecedented path just on the SEC's say-so, especially given the circumstances of this case.

First, adopting the SEC's alleged findings "without judicial review" of whether those findings are right would conflict with SIPA itself—where again, the statute says only that the SEC may "apply" for an order if it can show that SIPC has "failed to discharge its obligations" (all of which presupposes the SEC can show that "obligations" to covered "customers" exist). Far from simply enforcing SIPA as the SEC wrongly suggests, its approach would up-end the 40-year operation of the statute, which vests SIPC with the power to "determine" whether a liquidation proceeding should be filed. *See* 15 §78eee(a)(3)(A)(A) (authorizing ***SIPC*** to institute a liquidation proceeding against a SIPC member only "if ***SIPC*** determines that (A) the member

… has failed or is in danger of failing to meet its obligations to customers ….” (emphasis added)).

Second, the SEC's approach would create a conflict among the circuits. What the SEC's papers fail to disclose is that the Second Circuit considered the degree of deference that the SEC should receive if the agency and SIPC disagree. *See In re New Times Sec. Servs., Inc.*, 371 F.3d 68, 80-82 (2d Cir. 2004). Far from finding that the SEC's positions are not subject to judicial review, the Second Circuit found that the SEC was not even entitled to *Chevron* deference—especially where (as here) its position was not the product of agency adjudication or some other fully developed record. *See id.*

Third, the stakes of this case present an especially compelling reason why the parties should *follow* the Federal Rules of Civil Procedure and would benefit from careful (rather than cursory) review by an Article III court. After all, the SEC's case demands that SIPC start a liquidation proceeding for investors in CDs issued by the Stanford International Bank Ltd. in Antigua—a proceeding that could involve claims by as many as 21,500 people who purchased approximately $7.2 billion of these offshore CDs. (SEC Mem. at 7.) If ever there were a case to follow procedural protections and not to ignore them, surely this is it.

Fourth, the SEC's own record of action (or inaction) also weighs strongly against the rush to judgment that it now seeks to employ. Even after the SEC filed an enforcement complaint against Stanford in February 2009, the SEC still did not contend that SIPC was required to reimburse these victims, nor did it “immediately notify” SIPC as the statute demands. 15 U.S.C. § 78eee(a)(1). When SIPC explained to Stanford's U.S. Receiver a letter on August 14, 2009 that there was no basis for SIPC to initiate a proceeding under SIPA, the SEC voiced no objection at the time. And although the SEC ultimately changed its position in June 2011, it then waited another six months before filing this case on December 12, 2011. By contrast, the SEC cannot dispute that SIPC has acted immediately—even within 24 hours—in multi-billion dollar cases like Lehman Brothers, Bernard Madoff and MF Global, where (unlike here) a U.S. broker-dealer actually retained possession of investors' cash or securities so as to trigger protection under the statutory regime.

While the SEC's newfound sense of urgency may be explained by the criticism its own Inspector General has made of its handling of the Allen Stanford matter, nothing in SIPA entitles the SEC to prevail just on its say-so—especially when the value of the Antiguan CDs at issue in the Stanford matter would exceed the entire value of the SIPA Fund and thus threaten SIPC's ability to cover future claims involving customer cash and securities on deposit with SIPC-member brokerage firms (the types of claims that SIPA was actually designed to protect). Indeed, the SEC's attempt to force expedited treatment would be particularly unprecedented because, far from *preserving* the status quo to avoid irreparable harm, its case is a backdoor attempt to obtain an *affirmative* injunction that would place SIPC on a path toward paying over $1 billion in claims. All of this also shows that the case is solely about monetary losses, and thus not a situation for which the law permits injunctive relief (which is what an order requiring SIPC to launch a liquidation proceeding would be).

Finally, it is no answer for the SEC to say that this case is "only" about starting a liquidation proceeding and that the extent of any SIPC coverage for investors could be adjudicated then. (SEC Mem. at 12.) As the SEC well knows, the statute does not permit a private right of action to challenge SIPC's decision not to start a liquidation proceeding or to force it to pay contested claims. *Barbour*, 421 U.S. at 425. Once a liquidation proceeding begins, however, private plaintiffs can sue SIPC to seek relief, 15 U.S.C. § 78fff-2(a)(2)—thus opening the door to years of litigation for persons who, in the end, are not entitled to protection under the statute because (for example) they cannot show that the Stanford Antiguan Bank was or is a SIPC-member brokerage firm. Requiring SIPC to defend years of litigation in order to litigate claims that *exceed* the bounds of the statute is hardly something that the Court should require based only on one side's say-so, especially given the irreparable investment of time and resources that years of litigation would require (not only from SIPC, but also from the courts). By contrast, following the Federal Rules of Civil Procedure and conducting a Case Management Conference to discuss a *fair* and *efficient* way forward will not prejudice the SEC (or investors) in any way.

CONCLUSION

For the foregoing reasons, the SEC's *ex parte* motion for an order to show cause should be stricken, and the Court should conduct a Rule 16 Case Management Conference to determine the appropriate next step in this unprecedented case.

Dated: December 13, 2011

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on the 13th day of December, 2011, I served SECURITIES INVESTOR PROTECTION CORPORATION'S (1) MOTION TO STRIKE SECURITIES AND EXCHANGE COMMISSION'S EX PARTE MOTION FOR ORDER TO SHOW CAUSE, AND (2) MOTION FOR CASE MANAGEMENT CONFERENCE ON SEC'S "APPLICATION" FOR ORDER REQUIRING SIPC TO INITIATE LIQUIDATE PROCEEDING via courier, ECF, and/or email to the following:

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