SAC Blog

SECURITIES ARBITRATION COMMENTATOR

SECURITIES LITIGATION

SLC'S WEEKLY ALERT

SECURITIES LITIGATION ALERT: 2015-15 (04/20/2015)

Arbitration

Tawfik-Oshana vs. Wells Fargo Advisors LLC, No. H039626 (Cal. App., 6Dist., 4/2/15)

Award Challenge * Confirmation of Award * Arbitrability (Public Claims) * Agreement to Arbitrate * Contract Enforceability (Unconscionability; Public Policy) * FAA * State Law, Applicability of (Fed. v. CA) * Prejudice to Party * Collection/Debtor Issues * Waiver.

**Filing a notice of objection and nothing else is not participation in an arbitration. **An arbitrator is not required to rule on claims filed in court that are not submitted to arbitration. ***There is no requirement that a FINRA arbitrator be an attorney. ****The FAA preempts a California rule that labor claims cannot be arbitrated. *****An employee cannot argue that a dispute is not arbitrable because the employee is acting as a private attorney general on behalf of the general public when she only asserts claims on behalf of herself.*

When Respondent Mera Tawfik-Oshana resigned from her position as a stockbroker for Washington Mutual in order to accept a similar position with Wells Fargo in 2007, she received a $650,000 promissory note, which would be forgiven after seven years of employment. Four years later, she resigned, an event that triggered the balance due on the note. Wells Fargo then commenced an arbitration proceeding before FINRA, as permitted by both the terms of the note and the U4 that respondent had signed, in order to collect the balance due. Respondent ignored the arbitration proceeding, refusing to sign a submission agreement or file an answer. Her only filing was a "notice of objection" to the proceeding. She also filed suit alleging, *inter alia*, violations of California's Labor Code. Wells Fargo's motion to compel arbitration was granted by the court. After respondent persisted in not filing an answer or signing the submission agreement, FINRA appointed an arbitrator who held a hearing based on the papers, as permitted by FINRA rules when a party refuses to participate in a promissory note collection case. The arbitrator awarded Wells Fargo $386,635, plus $12,586 in attorney fees (FINRA ID #12-00606 (San Francisco, 10/12/12)). Respondent's motion to vacate the Award was denied.
She appealed, asserting many grounds, all of which are rejected by the Court of Appeal. She challenged the lower court's finding that she failed to participate in the arbitration, citing the fact that she filed the notice of objection, but the appellate Court holds that filing an objection does not amount to participation. She claimed that the Arbitrator failed to file a written decision and ignored her Labor Code claims, but the Court wonders how the Arbitrator could have ruled on these claims if she did not submit them. She asserted that the Arbitrator was not qualified because he was not an attorney, but the Court rules that there is no FINRA requirement that its arbitrators needed to be attorneys and, in any event, claimant was not prejudiced thereby. She noted that another California court had held that the type of labor claims that she raised were statutorily protected rights that could not be arbitrated. The Court replies that the activities in which the parties engaged involved interstate commerce, that, therefore, the FAA applied, and that the FAA preempts California law that bars arbitration of certain labor claims. She argued that both the U4 and the arbitration clause in the promissory note were unconscionable. The Court finds that there are no substantively unconscionable terms in either document and that there was no procedural unconscionability, because Wells Fargo did not draft the U4 and the promissory note was not a condition of employment. Finally, she asserted that her claims were not arbitrable because she was acting as a private attorney general on behalf of the general public. But her court complaint does not mention any other aggrieved persons or suggest in any way that she sought relief on behalf of anyone but herself.

(P. Dubow)

(SLC Ref. No. 2015-15-01)

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Business & Employment

Grede vs. Bank of New York, No. 08 C 2582 (N.D. Ill., 12/10/14)

Bankruptcy Issues (Equitable Subordination; Fraudulent Transfers) * U.S. Statutes Interpreted (11 U.S.C. §§ 548, 550) * Culpability Standards (Knowledge of Misconduct; Negligence; Recklessness; Deliberate Indifference; Intent to Defraud; Good Faith) * Trusts/Estates/Receiverships (Powers of Trustees).

Equitable subordination is only appropriate where the claimants engaged in some type of inequitable conduct, the misconduct resulted in injury to the creditors and subordination is not inconsistent with the provisions of the Bankruptcy Code.

This case arises from the collapse and resulting bankruptcy of futures commission merchant Sentinel Management Group, Inc. The Seventh Circuit remanded this case to the District Court for further analysis of the trustee's equitable subordination and fraudulent transfer claims (see *In Re Sentinel Management*, summarized in SLA 2013-40). Courts will subordinate a claim (i.e., choose to disregard an otherwise legally valid transaction) when a claimant engages in some type of inequitable conduct and the misconduct results in injury to other creditors or confers an unfair advantage to the claimant. The "trigger" for equitable subordination is whether BNY's conduct is egregious and conscious-shocking. The Court finds that the testimony and demeanor of the bank witnesses left no doubt that the sudden demise of Sentinel was a complete surprise to BNY officials. The Bank did not foresee the possible demise and default of Sentinel and nothing it did can properly be labeled as egregious or conscious-shocking. While what BNY elected to do was less than the Court thought was wise, mere negligence, or ineptitude, is insufficient to establish inequitable conduct. BNY was neither deliberately indifferent nor reckless in dealing with its legal obligations by failing to investigate Sentinel's misconduct.
As to the fraudulent transfers, the trustee seeks to avoid five transfers from Sentinel to BNY as fraudulent under § 548(a)(1)(A) of the Bankruptcy Code. Here, Sentinel commingled its client assets with Sentinel's assets in an unlawful manner and exposed its clients to a substantial risk of loss of which they were unaware. However, with respect to the finding of actual intent to defraud, the defenses available to BNY had not been addressed. BNY argued that it acted in good faith and that the trustee was precluded from recovery under limitations set forth under 11 U.S.C. § 550. As to the former, whether BNY acted in good faith must be assessed under an objective standard. Based upon the evidence and the testimony of the witnesses, the Court finds that, under a purely objective standard, BNY did act in good faith. Based on the Court's earlier finding that BNY neither knew nor should have known of Sentinel's bad conduct, the purely objective standard is satisfied.
As to the latter, under § 550, a trustee is only allowed to recover property transferred or the value of such property from the transferee. Here, BNY gave full consideration for the specific transfers in the form of cash for loans secured by collateral. What the trustee in effect is requesting is a windfall recovery of the millions loaned to Sentinel by BNY plus the collateral to secure those loans. The trustee cannot force BNY to pay twice the value of its loans by avoiding the fraudulent-specific transfers.

(W. Nelson: We also previously summarized two other decisions in this case in SLAs 2009-28 and 2014-10.)

(SLC Ref. No. 2015-15-02)

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Aspire Commodities, LP vs. GDF Suez Energy North America, Inc., No. H-14-1111 (S.D. Tex., 2/3/15)

CEA (Price Manipulation; Exemptions) * Standing Issues (Case/Controversy) * Private Cause of Action * Derivative/Vicarious Liability Issues (Aiding & Abetting; Conspiracy) * FRCP (Rules 12(b)(1) "Jurisdiction"; 12(b)(6) "Claim for Relief") * Remedies (Injunctive Relief; Declaratory Judgment) * Staff Interpretations, Effect of.

There is no private cause of action for manipulation of the price of commodities with respect to transactions that the CFTC exempts from the reach of the Commodities Exchange Act.

Plaintiffs Aspire Commodities, LP and Raiden Commodities, LP (together, "Plaintiffs") are commodities traders in the derivative commodities market. Defendants are generators of electricity within Texas's energy market, which is operated by the Electric Reliability Council of Texas ("ERCOT"). Defendant GDF Suez Energy North America, Inc. ("GDF") allegedly controls the generation of electricity within ERCOT of the other named Defendants. Plaintiffs filed suit against Defendants, alleging that GDF intentionally withheld electricity generation in times of tight supply, thereby manipulating the prices in two markets operated by ERCOT—the Real Time Market for the physical sale of electricity and the Day-Ahead Market, a forward market that anticipates the following day physical sales of electricity. Plaintiffs further alleged that through this manipulation, GDF violated the CEA, and that all Defendants conspired to violate and aided and abetted in GDF's violation of the CEA. Defendants moved to dismiss Plaintiffs' complaint on the basis that no private right of action is available to Plaintiffs under the CEA because all of Defendants' challenged actions took place in the ERCOT market and are therefore exempt from the provisions of the CEA. The Court agrees with Defendants that no private right of action under the CEA is available to Plaintiffs because, pursuant to a Final Order issued on April 2, 2013, the Commodity Futures Trading Commission exempted from the provisions of the CEA "energy transactions" such as the transactions in the ERCOT market upon which Plaintiffs' claims are based. The Court dismisses the Plaintiffs' cause of action against GDF under the CEA and also dismisses the claims for conspiracy and aiding and abetting against the other Defendants because such claims are premised on a valid claim under the CEA, which is barred.

(J. Ballard)

(SLC Ref. No. 2015-15-03)

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Morgan Stanley & Co., Inc. vs. Director, Division of Taxation, No. 007557-2007 (N.J. Tax Ct., 10/29/14)

Tax-Related Issues * FRCP (Rule 56 "Summary Judgment") * State Statutes Interpreted (New Jersey Corporation Business Tax, N.J.S.A. 54:10-4(k)(2)(I) * Standard of Review (Abuse of Discretion) * Staff Interpretations, Effect of.

The New Jersey Director of Taxation abuses his discretion when he disallows the deduction of interest paid to related parties solely based on a corporation's failure to demonstrate that it paid tax on the interest in another jurisdiction, since the state's Tax Statute does not require such a showing.

The issue involved in this opinion is the interpretation and application of the statutory exceptions of the New Jersey Corporation Business Tax, N.J.S.A. 54:10-4(k)(2)(I) (the "NJ Tax Statute"). In 2004, Plaintiff Morgan Stanley & Co., Inc. ("MS&Co") filed a New Jersey corporate income tax return for the fiscal year ending November 2003, reporting a tax due on transactions in the state of $1,850,764, which it paid. In connection with this return, MS&Co reported related party interest add-back of $206,459,736, which it calculated by netting the total interest paid to related entities with the total interest received from related entities.

In November of 2004, MS&Co filed an amended New Jersey corporate tax return, on which it deducted all of its related party interest add-back in calculating its net income, and requested a refund of $442,126. The New Jersey Director of Taxation (the "Director") denied the refund request and assessed an additional tax of $811,308, plus interest, after disallowing the deduction and recalculating the amount of related party interest that was required to be "added-back" to MS&Co's taxable income to determine MS&Co's "entire net income." MS&Co protested the refund denial and recalculation, and a hearing was held in November 2006. After a hearing, the Director increased the amount of the related party interest add-back, resulting in a deficiency tax of $709,162, plus interest, assessed to MS&Co.

The Court's review of the parties' cross-motions for summary judgment begins with the presumption that determinations made by the Director are valid. With regard to related party interest, the Court explains, the NJ Tax Statute "essentially denies a deduction to the borrowing entity for interest paid to a related lending entity" unless at least one of three exceptions applies: the subject to tax exception, the guarantee exception, or where disallowance would be "unreasonable." The Court rejects the "subject to tax exception" after determining that MS&Co did not satisfy all of the requirements.

The Court also rejects MS&Co's argument that it was unreasonable for the Director to deny the interest deduction whenever the transaction has a valid non-tax business purpose and economic substance, irrespective of the identity of the parties, concluding that the "unreasonable" exception requires "something more." However, the Court then turns to the Director's assertion that, in determining that MS&Co's transactions with related parties did not qualify for the "unreasonable exception," the Director reviewed all of the facts and circumstances applicable to those transactions. The Court finds, contrary to this assertion, that the only fact referenced to support the Director's determination was MS&Co's failure to demonstrate that a tax had been paid on the related party interest income in another jurisdiction. The Court notes that the NJ Tax Statute does not require such a showing, and that, in limiting the inquiry to the question of whether a tax was paid in another jurisdiction, the

Director abused his discretion and acted unreasonably. The Court grants MS&Co.'s Motion for Summary Judgment and denies the Director's Cross-Motion for Summary Judgment on this basis.

(J. Ballard)

(SLC Ref. No. 2015-15-04)

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Class Actions

Johnson vs. Nextel Communications, Inc., No. 14-454 (2nd Cir., 3/4/15)

Class Actions (Certification) * Choice of Law (Various States) * Conflicts of Interest (Attorney) * FRCP (Rule 23 "Predominance" & 'Superiority") * Representation Issues * Damage Calculations * Remedies (Punitive Damages) * Standard of Review (Abuse of Discretion; *De Novo*).

Where a class covers a large number of states and choice of laws principles require the application of the states with the most significant relationship to each class member, common questions of law and fact will not predominate and class certification is inappropriate.

In 2000, almost 600 Nextel employees living in 27 states retained the law firm of Leeds, Morelli & Brown ("LMB") to pursue employment discrimination claims against Nextel. All but 14 of the claims settled, through a global dispute resolution process, for a total of $3.9 million to the employees and $5.2 million to LMB. The payment to LMB was based on an agreed upon formula tied to both the number and timing of the settlements reached. As part of the arrangement, Nextel also agreed to retain LMB as a consultant for a two-year period and to pay the firm an additional $2 million in consulting fees. In 2006, six of the former Nextel employees who had retained LMB brought this putative class action alleging, among other things, that Nextel induced LMB to breach the retainer agreements and its fiduciary duties to plaintiffs. The district court granted class certification, finding that common issues predominated over individual issues. This appeal followed.
Fed. R. Civ. P. 23 sets out a number of factors that must be considered in determining whether a case will be litigated as a class action. Here, the Court focuses on Rule 23(b)(2) -- whether questions of law or fact common to class members will predominate over questions affecting only individual members and whether a class action is a superior means for fairly and efficiently adjudicating the controversy. The Court notes that Rule 23(b)'s predominance requirement is more demanding than Rule 23(a)'s commonality requirement and finds that the lower court erred in certifying the class. The Court first looks at choice of law issues. New Jersey's (the forum state's) choice of law rules require a court to examine whether actual conflicts exist between the laws of relevant states and, if so, to determine the jurisdiction that has the most significant relationship. Here, the states where the individual class members reside have the most significant relationship to the tort and contract claims because those are the states where the class members lived, where they worked for Nextel, where they entered into the retainer agreements with LMB and where, ultimately, they were injured. Resolution of common liability issues will require application of the substantive law of 27 different states and potentially different outcomes on common issues. For example, the law of New York (where six plaintiffs reside) and the law of Colorado (where 164 plaintiffs reside) differ as to whether LMB's conflict of interest could be waived with proper notice to the client. Therefore, the predominance and superiority factors diminish to their vanishing point. Indeed, the Court adds, the issues are so individualized that the litigation would not be advanced, and economies of scale would not be enjoyed, by creating one or more sub-classes.

*(C. Lazarini: *By agreement of the parties, the claims against LMB and its individual attorneys were dismissed before the appeal was taken on the class certification issues. **In dicta, the Court also criticized the manner in which the district court intended the jury to calculate punitive damages.) (EIC: Although this decision is not within the normal scope of our coverage, it raises what we consider to be a significant point: that a nationwide class action based on state causes of action might not succeed at the certification stage.)*

(SLC Ref. No. 2015-15-05)

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Bourbonnais vs. Ameriprise Financial Services, Inc., No. 14-C-966 (E.D. Wis., 2/24/15)

Pleading Requirements/Issues * PSLRA * 1934 Act (§10 "Rule 10b-5") * Class Actions (Class Certification) * FRCP (Rule 9b "Particularity") * Suitability * Misrepresentations/Omissions * Product/Sales Practice Issues (ETF: Exchange Traded Funds) * Jurisdiction Issues (Pendent).

The fact that plaintiffs wish to proceed as a class action does not relieve them of their obligation to plead fraud with requisite particularity, even if doing so might create issues of individual fact that could bar class certification.

Plaintiffs were customers of defendant Paul Renard, a financial advisor who worked at defendants Ameriprise Financial Services Inc. and SII Investments, Inc. Plaintiffs filed this putative class action alleging that Renard sold them unsuitable investments in non-traditional exchange-traded funds ("ETFs") in violation of federal securities law and state law.
The Court grants defendants' motion to dismiss. While the complaint is full of allegations regarding Renard's improper sales practices regarding ETFs – including mismarking sales tickets as unsolicited and making unsuitable ETF purchase recommendations – those allegations do not relate directly to plaintiffs. Rather, those allegations are drawn from legal proceedings involving parties other than plaintiffs.
Notably, plaintiffs fail to include any allegations in their complaint regarding the supposed misrepresentations made specifically to them. Missing is the "who, what, when, where and how of the fraud as to them." Thus, they have failed to plead fraud with the specificity required under the Federal Rules of Civil Procedure and the Private Securities Litigation Reform Act of 1995. The fact that plaintiffs have styled their case as a class action -- and thus need to avoid a pleading that suggests issues of individual fact will predominate – does not relieve them of their obligation to plead fraud with requisite particularity.

(J. Komie) (EIC: Ameriprise terminated Renard from its employ. We know this because we summarized (in SLA 2014-13) the broker's unsuccessful proceeding to vacate an Award holding him liable to Ameriprise for the unpaid balances of several promissory notes, and the predictably successful outcome (FINRA ID #12-00511 (Milwaukee, 4/16/13)).)

(SLC Ref. No. 2015-15-06)

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Regulatory

USA vs. Gupta, No. 12-4448, 747 F.3d 111 (2nd Cir., 3/25/14)

Insider Trading (Tipper/Tippee Liability; Use/Possession; Duty of Confidentiality) * 1934 Act (§10(b) "Rule 10b-5") * Evidentiary Issues/Standards (Hearsay; Character Evidence) * F. R. Evid. (Rules 403, 801(d), 802) * Relevance/Materiality Issues * Standard of Review (Clear Error; Abuse of Discretion) * Prejudice to Party (Harmless Error) * Criminal Issues (Wiretaps) * Constitutional Issues (Search & Seizure).

A statement by an alleged insider trading tippee to third parties admitting that he received inside information may be admissible against the tipper as a statement by a co-conspirator in furtherance of the conspiracy, where the statement is intended to allay the complaints of co-conspirators or to affect trading activity to the tippee's benefit; in any case, it may be admissible against the tipper as a statement against the tippee's penal interest.

Rajat K. Gupta ("Gupta"), a director of Goldman Sachs Group, Inc. ("Goldman"), was convicted in federal court of supplying inside information to hedge fund manager Raj Rajaratnam ("Raj") of The Galleon Group. The conviction stemmed from two instances. On September 23, 2008, Gupta allegedly tipped off Raj shortly before the closing bell that Warren Buffett would invest in Goldman, giving Raj time to buy up a large amount of Goldman stock before the news was announced that evening. Then, on October 24, 2008, Gupta allegedly tipped off Raj to Goldman's unexpected quarterly loss to be announced in December, followed by a selloff of Goldman stock by Raj. In this appeal, Gupta raises a number of evidentiary issues.
The Court first addresses Gupta's hearsay objections to admission of two wiretapped phone conversations that Gupta had with other Galleon personnel, each shortly after one of the two incidents, in which he admitted that he bought or sold the stock on a tip from an unnamed insider. The Court agrees with the district court that the conversations were admissible as statements of a co-conspirator in furtherance of the conspiracy. Gupta and Raj were involved in a number of business ventures, including Galleon. The first call served to allay the complaints of co-conspirators at Galleon who learned of the tip too late to take advantage of it. The second call served to warn a Galleon trader (who was admittedly not a co-conspirator) not to purchase Goldman stock. In addition, the Court finds that Raj's wiretapped admissions are admissible as statements against his penal interest because he incriminated himself, a ground for admission the lower court had rejected.
Next, Gupta objects to the district court's limitations on the testimony of his daughter, who testified about Gupta's statement to her, a few days before the date of the first alleged tip, that he was angry at Raj for withdrawing money from one of their joint

business ventures without telling him. The lower court permitted her to testify that her father was upset at how Raj "was treating the investment," but not that he felt cheated by Raj. The Court finds no abuse of discretion; the testimony was admissible only to prove Gupta's state of mind, but the probative value of Gupta's belief that he was cheated was outweighed by the danger of causing the jury to conclude that Raj did, in fact, cheat him. Moreover, that evidence was cumulative, as Gupta presented other evidence that he was cheated. In any case, the Court concludes, any error in the ruling is harmless. Gupta also objects to the district court's refusal to admit wiretapped phone calls and emails between Raj and David Loeb, a Goldman trader, purportedly showing that Loeb supplied tips to Raj on other securities, which Gupta claims would support his theory that Loeb was the one who supplied the tips for which Gupta was convicted. The Court sustains this ruling as well. Not only is the evidence replete with inadmissible hearsay, but Loeb did not work in a department with access to the information in question. The conviction is affirmed.

*(ed: *Gupta also raised Fourth Amendment objections to the wiretap evidence against him but, since the Court previously rejected an identical objection in Raj's appeal from his own conviction (see SLA 2013-24), it wastes no space explaining why it does so again here. **The Court also affirms the lower court's denial of proffered testimony about Raj's charitable giving and "integrity." ***We summarized a series of decisions in an enforcement action against Gupta, arising from the same insider trading, in SLAs 2011-46 and 2015-03. ****The U.S. Supreme Court denied Gupta's petition for a writ of certiorari on April 20, 2015. ***** Gupta has also filed a second appeal in the Second Circuit, based on the Court's decision in USA v. Newman (which we summarized in SLA 2014-47).)*

(SLC Ref. No. 2015-15-07)

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Zelaya vs. USA, No. 13-14780 (11th Cir., 3/30/15)

Criminal Issues & Product/Sales Practice Issues (Stanford Ponzi Scheme) * Privileges/Immunities (Regulatory; Sovereign) * U.S. Statutes Interpreted (FTCA: Federal Tort Claims Act) * 1934 Act (SIPC Notification) * SIPA (15 U.S.C. §§ 78aaa-lll) * Notice Requirements * Duty of Inquiry (Regulatory) * Statutory Definitions ("Discretionary Function Exception"; "Misrepresentation Exception") * Jurisdiction Issues (Federal Question) * State Law, Applicability of (Good Samaritan Doctrine).

Jurisdiction under the Federal Tort Claims Act is a matter of federal law, but a plaintiff must show that his claim of tortious conduct would stand, under state law, against a private individual, were she to act in the same way as did the federal employee.

In this case, Plaintiffs-Investors Carlos Zelaya and George Glanz claim that the SEC knew for a dozen years before it finally acted in 2009 that Allen Stanford was operating a Ponzi scheme. The Court considers the many allegations suggesting a duty to act by the SEC. In each of four investigations of the broker-dealer, the words "Ponzi scheme" appear in investigators' notes or surrounding staff email exchanges; Stanford Group was assigned the SEC's highest risk rating, due to suspicions about the Stanford Bank's activities; yet, at least five years passed before the SEC sought enforcement action.
Plaintiffs advanced two theories of liability under the FTCA. First, they relied upon a duty to notify under the Securities Investor Protection Act; SIPA requires the SEC to notify SIPC when it finds a broker-dealer in financial difficulty. Secondly, they averred a statutory requirement obliging the SEC, under the circumstances, to revoke Stanford's registration. The Government responded at the trial level with a motion to dismiss, claiming reliance upon the FTCA's "discretionary function exception." The District Court dismissed the registration claim on that basis, but retained the notification claim. In a second round, it dismissed the notification claim, when the Government raised the "misrepresentation exception."
Plaintiffs' appeal covers both dismissals. The waivers of immunity in the FTCA must be strictly construed. The statutory exceptions in 28 U.S.C. § 2860(a) ("discretionary function") and § 2860(h) ("misrepresentation") serve to narrow the window of liability the Government opened by enacting the FTCA. Before even considering the scope of these exceptions, the Court questions *sua sponte* the applicability of the Act. Under the FTCA, a litigant must satisfy the Court that it could prevail on its claim, were the defendant an individual. The FTCA gives the federal courts exclusive jurisdiction to hear waiver claims, but the Act looks to state law for the foundations of liability. Uniquely governmental functions, such as regulatory duties, are difficult to analogize; the Court turns to the Good Samaritan Doctrine and reviews state law in vain for a similar duty. Neither the District of Columbia, nor Texas, "requires a person to prevent a third party from causing harm."
Reluctant to rely upon a ground not briefed by the parties, the Court reviews the exceptions next. The registration claim is more easily disposed of. 15 U.S.C. § 80b-3(c) does impose upon the SEC a duty to disallow a broker-dealer registration in the first instance, but there is no mention in the statute of a duty to revoke a registration that is being amended. Moreover, any such duty would be subject to the "discretionary function" exception, which "is intended to protect any decision grounded in public policy, and all discretionary decisions are presumed to be grounded in public policy."

The duty to notify SIPC is of a less discretionary nature, so the Court turns to the "misrepresentation" exception. Agreeing with the District Court, this Court finds that the exception applies. The "misrepresentation" exception covers a failure to communicate, as well as a miscommunication; the SEC's alleged failure under the "notification" claim was a non-communication of required financial information. While Plaintiffs try to transform the required notification into an omitted "operational" act, it was clearly not a clerical act: "[I]t is the content of any writing sent to SIPC that would be critical to the corporation's determination of the appropriate action to take…," and only a meaningful communication would have held any possibility of action to shut down Stanford. The dismissal below is affirmed.

(SLC Ref. No. 2015-15-08)

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SEC vs. Gibraltar Global Securities, Inc., No. 13 Civ. 2575 (S.D. N.Y., 4/1/15)

Enforcement Practice/Procedure * Discovery Issues (Protective Orders) * Bankruptcy/Insolvency Issues * U.S. Statutes Interpreted (15 U.S.C. §§77e, 78o) * FRCP (Rules 26(a)(1), 34(a)(1) * International Issues * Foreign Statutes Interpreted (Securities Act of the Bahamas, §§55, 73).

An ineffective voluntary liquidation—in effect, a failed attempt at corporate suicide—does not excuse a party from its discovery obligations.

The Court begins its opinion with a pithy summary of its holding: "An ineffective voluntary liquidation – in effect, a failed attempt at corporate suicide – does not excuse a party from its discovery obligations." The SEC charges that Defendants, a Bahamian broker-dealer and its sole shareholder, operated as an unregistered broker-dealer in the U.S. and participated in the unlawful unregistered offering and sale of shares of a company called Magnum d'Or. The SEC seeks production of all Gibraltar files concerning its U.S. customers. Defendants have moved for a protective order on the grounds that (1) the documents located in the Bahamas are not within their possession, custody or control; (2) their disclosure of the documents could expose them to liability in the Bahamas; and (3) in light of issues of comity, the SEC should be required to use alternative means to seek to obtain the information.

Defendants' motion is denied. When the SEC commenced this matter, Defendants represented that Gibraltar retained documents pertaining to its customers and transactions, as required by Bahamian law. Gibraltar's Board passed a resolution dissolving the company and appointing a liquidator, but the Securities Commission of the Bahamas ("SCB") has refused to grant it permission to surrender its brokerage license, and Gibraltar's action to compel the SCB to do so is still pending. Where the alleged obstacle to production is foreign law, the burden of proving what that law is and why it impedes production falls on the party resisting discovery. Defendants have not met this burden. Section 73 of the Securities Act of the Bahamas (the "SIA"), entitled "Voluntary liquidation," is very clear and requires SIA to approve a registrant's decision to proceed to a voluntary liquidation. Because Gibraltar's liquidation and attempted surrender of its license are ineffective, it retains control of the documents sought by SEC.

Defendants have also failed to establish a realistic possibility of civil liability under Bahamian law. They have made no showing that the confidentiality rule applies to broker-dealers; in any case, the duty of bank secrecy does not apply where disclosure is under compulsion of the law, and an order from this court constitutes legal compulsion. Defendants contend that SIA §55 recognizes the right of legal professional privilege in relation to certain documents in possession of the registrant, but it merely provides that no one shall be required under SIA to disclose attorney-client communications.

In the absence of a true conflict between domestic and foreign law, the Court asserts that it is unnecessary to engage in comity analysis, but proceeds to do so anyway. The U.S. Supreme Court has identified five factors to consider in determining whether to order foreign discovery under the FRCP: the importance to the litigation of the requested information, the specificity of the request; whether the information originated in the U.S., the availability of alternative means of securing the information and the relative interests of the U.S. and foreign nations. Courts in the Second Circuit also consider the hardship on the party from whom discovery is sought and the good faith of the party resisting discovery. Here, the Court is satisfied that all of those factors favor granting the SEC the discovery it requests.

(S. Anderson)

(SLC Ref. No. 2015-15-09)

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Securities Customers

National Credit Union Administration Board vs. Barclays Capital, Inc., No. 13-3183 (10th Cir., 3/3/15)

Timeliness Issues (Statute of Limitations; Statutes of Repose) * U.S. Statutes Interpreted (12 U.S.C. § 1787(b)(14) "Extender Statute") * Tolling Principles (Estoppel) * Contract Enforceability (Public Policy) * Settlement Issues.

The National Credit Union Act's Extender Statute is a statute of limitations, not a statute of repose; therefore, its time limits establish only an affirmative defense that may be waived.

The NCUAB was appointed as conservator and liquidating agent for two credit unions that failed. It determined that the credit unions failed because they had invested in residential mortgage-backed securities ("RMBS") sold with offering documents that misrepresented the quality of the underlying mortgage loans. The NCUAB began settlement negotiations with Barclays, which "dragged on." The NCUAB and Barclays therefore entered into a series of tolling agreements that purported to exclude all time that had passed during the settlement negotiations. Barclays also expressly made a separate promise in the tolling agreements that it would not "argue or assert" in any future litigation a statute of limitations defense that included the time passed in the settlement negotiations. After negotiations broke down, the NCUAB filed this action more than five years after the RMBS were sold and more than three years after the NCUAB was appointed conservator of the credit unions. Barclays moved to dismiss on several grounds, including untimeliness. The District Court granted the Motion to Dismiss, holding that the three-year period under the Extender Statute may not be extended by a tolling agreement because the three-year period has set an outer limit that may not be extended by agreement or equitable tolling.

On appeal, while conceding that the litigation was commenced outside the three-year period, the NCUAB argues that the claims are still timely under either of two legal theories, because the Extender Statute itself was lawfully tolled by the tolling agreements, or because Barclays is estopped from pleading a statute-of-limitations defense because of its separate promise not to do so. Regarding the former, the Court of Appeals holds that the Extender Statute's limitations periods cannot be tolled by contract, so tolling agreements purporting to toll the statute of limitations are not effective. The Extender Statute's opening clause, which states that "[n]otwithstanding any provision of any contract" amounts to an express statement that the limitations period cannot be tolled by agreement.

Regarding NCUAB's latter theory, the Court holds that Barclays is estopped from asserting a statute-of-limitations defense by its own separate promise. The Court reasons that the Extender Statute is a statute of limitations, not a statute of repose. The statute refers to itself as a "statute of limitations" and uses that term several times while not ever mentioning the term "repose." It also refers to the date a claim accrues, language consistent with a statute of limitations. Because the Extender Statute is a statute of limitations, its time limits establish only an affirmative defense that can be waived. Here, Barclays expressly promised not to raise the statute-of-limitations defense if doing so would require inclusion of time periods that the parties agreed to exclude and the Court holds Barclays to that promise.

(W. Nelson)

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