

1 UNITED STATES COURT OF APPEALS
2
3 FOR THE SECOND CIRCUIT
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6
7 August Term, 2012
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9 (Argued: March 14, 2013 Decided: April 10, 2013)

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11 Docket Nos. 11-2510-cv(L),
12 11-2532-cv(con), 11-3142-cv(con), 11-3304-cv(con),
13 11-3306-cv(con), 11-3310-cv(con), 12-472-cv(con),
14 12-476-cv(con), 12-502-cv(con), 12-511-cv(con),
15 12-518-cv(con), 12-533-cv(con).
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18 PHYLLIS MOLCHATSKY, CHARLES MEDERRICK, INDIVIDUALLY AND ON
19 BEHALF OF ALL THOSE PERSONS SIMILARLY SITUATED,
20 ALAN GOLDMAN, THE LITWIN FOUNDATION, INC.,
21 THE MICHAEL AND RUTH SLADE FOUNDATION, STEVEN SCHNEIDER,
22 M.D., JUDITH WELLING, INDIVIDUALLY AND ON BEHALF OF ALL
23 THOSE PERSONS SIMILARLY SITUATED, BLAYNE GOLDMAN,
24 ALLAN H. APPLESTEIN, AS TRUSTEE FOR THE BENEFIT OF D.C.A.
25 GRANTOR TRUST, GEORGE R. MARKS, ROBERT MICK, INDIVIDUALLY
26 AND ON BEHALF OF ALL THOSE PERSONS SIMILARLY SITUATED,
27 GEORGE R. MARKS, AS BENEFICIARY FOR THE BENEFIT OF GEORGE R.
28 MARKS I.R.A., HAROLD SCHWARTZ, AS TRUSTEE FOR THE BENEFIT
29 OF HAROLD SCHWARTZ 1997 IRREVOCABLE TRUST, AS BENEFICIARY
30 FOR THE BENEFIT OF HAROLD SCHWARTZ I.R.A. AND AS TRUSTEE OF
31 THE BENEFIT OF HAROLD SCHWARTZ 1998 LIVING TRUST,
32 ROSENMAN FAMILY, LLC, ROBERT I. LAPPIN, AS TRUSTEE FOR THE
33 BENEFIT OF SHETLAND PROPERTIES EMPLOYEE SAVINGS AND
34 RETIREMENT PLAN, DANIEL SILNA, AS TRUSTEE FOR THE BENEFIT OF
35 O.D.D. INVESTMENTS L.P. PROFIT SHARING PLAN,
36

37 *Plaintiffs-Appellants,*
38

39 -v.-
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1 UNITED STATES OF AMERICA, JOHN DOES 1-10,
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3 *Defendants-Appellees.**
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8 Before:

9 WESLEY, DRONEY, *Circuit Judges*, NATHAN, *District Judge.***
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12 Appeal from the April 19, 2011 Opinion and Order by the
13 United States District Court for the Southern District of
14 New York (Swain, J.) granting the United States' motion to
15 dismiss Plaintiffs-Appellants' claims against the United
16 States Securities and Exchange Commission (the "SEC") for
17 lack of subject matter jurisdiction pursuant to Federal Rule
18 of Civil Procedure 12(b)(1), and from the January 24, 2011
19 Memorandum Order denying Plaintiffs-Appellants' motion for
20 relief from judgment under Federal Rule of Civil Procedure
21 60(b). Plaintiffs-Appellants argue that the district court
22 erred by dismissing their complaints pursuant to the
23 Discretionary Function Exception to the Federal Tort Claims
24 Act because the SEC negligently failed to adequately
25 investigate Bernard Madoff despite numerous warnings and, in
26 doing so, violated federal statutes and regulations, as well
27 as internal agency policies. We AFFIRM because the
28 Discretionary Function Exception shields the SEC's conduct
29 from Plaintiffs-Appellants' claims.
30

31 AFFIRMED.
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* The Clerk of Court is directed to amend the official caption to conform to the listing of the parties stated above.

** The Honorable Alison J. Nathan, of the United States District Court for the Southern District of New York, sitting by designation.

1 PATRICIA M. GRAHAM (Howard Elisofon, David R.
2 King, *on the brief*), Herrick, Feinstein LLP,
3 New York, NY, *for Plaintiff-Appellant Phyllis*
4 *Molchatsky*.

5
6 DR. GAYTRI D. KACHROO, Kachroo Legal Services,
7 P.C., Cambridge, MA, *for Plaintiff-Appellant*
8 *Charles Mederrick*.

9
10 Howard Kleinhendler, Sara Spiegelman, Wachtel Masyr
11 & Missry LLP, New York, NY, *for Plaintiff-*
12 *Appellant Allan H. Applestein*.

13
14 SARAH S. NORMAND, Assistant United States Attorney
15 (Neil M. Corwin, Assistant United States
16 Attorney, *on the brief*), *for Preet Bharara,*
17 *United States Attorney for the Southern*
18 *District of New York, New York, NY, for*
19 *Defendants-Appellees*.

20
21 Lawrence R. Velvel, Massachusetts School of Law,
22 Andover, MA; David Bernfeld, Bernfeld,
23 DeMatteo & Bernfeld LLP, New York, NY, *for*
24 *Amicus Curiae Network for Investor Action and*
25 *Protection*.

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30 PER CURIAM:

31 Plaintiffs-Appellants Phyllis Molchatsky, et al.
32 ("Plaintiffs") appeal from an April 19, 2011 Opinion and
33 Order by the United States District Court for the Southern
34 District of New York (Swain, J.) granting Defendant-Appellee
35 the United States' motion to dismiss Plaintiffs' complaints
36 against the United States Securities and Exchange Commission
37 (the "SEC") for lack of subject matter jurisdiction pursuant

1 to Federal Rule of Civil Procedure 12(b)(1). Plaintiffs
2 also appeal from the district court's January 24, 2011
3 Memorandum Order denying Plaintiffs' motion for relief from
4 judgment under Federal Rule of Civil Procedure 60(b).
5 Plaintiffs seek to hold the United States liable for SEC
6 employees' failure to detect Bernard Madoff's Ponzi scheme
7 and for the financial losses that Plaintiffs claim they
8 suffered as a result. Because we find that the SEC's
9 actions, along with its regrettable inaction, are shielded
10 by the Discretionary Function Exception, we affirm the
11 district court's dismissal of Plaintiffs' claims for lack of
12 subject matter jurisdiction.

13 **Background**

14 Plaintiffs are investors who lost money they had
15 entrusted to Bernard Madoff ("Madoff") and his firm, Bernard
16 L. Madoff Investment Securities LLC, after Madoff's massive
17 Ponzi scheme exploded in 2008. Plaintiffs' principal
18 allegation is that the SEC negligently failed to uncover
19 Madoff's fraud despite receiving numerous complaints over a
20 sixteen-year period. Relying on an extensive report from
21 the SEC's Office of the Inspector General, Plaintiffs allege
22 in detail approximately eight separate complaints the SEC
23 received regarding Madoff and the SEC's inadequate and often

1 incompetent response to each. As a result of the SEC's
2 repeated failure to alert other branch offices of ongoing
3 investigations, properly review complaints and staff
4 subsequent inquiries, and follow up on disputed facts
5 elicited in interviews, the SEC missed many opportunities to
6 uncover Madoff's multi-billion-dollar fraud.

7 **Discussion**

8 Plaintiffs claim that the SEC's clear negligence
9 exposes the agency to liability under the Federal Tort
10 Claims Act ("FTCA"). The district court disagreed, as do
11 we. The FTCA provides in relevant part that federal courts

12 shall have exclusive jurisdiction of
13 civil actions on claims against the
14 United States, for money damages,
15 accruing on and after January 1, 1945,
16 for injury or loss of property, or
17 personal injury or death caused by the
18 negligent or wrongful act or omission of
19 any employee of the Government while
20 acting within the scope of his office or
21 employment, under circumstances where the
22 United States, if a private person, would
23 be liable to the claimant in accordance
24 with the law of the place where the act
25 or omission occurred.

26
27 28 U.S.C. § 1346(b)(1).

28 The FTCA is an exception to the rule that the United States
29 is typically immune from suit. The district court
30 determined that the Discretionary Function Exception

1 ("DFE"), an exception to the exception, barred Plaintiffs'
2 claims. The DFE suspends the FTCA from applying to

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4 [a]ny claim based upon an act or omission
5 of an employee of the Government,
6 exercising due care, in the execution of
7 a statute or regulation, whether or not
8 such statute or regulation be valid, or
9 based upon the exercise or performance or
10 the failure to exercise or perform a
11 discretionary function or duty on the
12 part of a federal agency or an employee
13 of the Government, whether or not the
14 discretion involved be abused.

15
16 28 U.S.C. § 2680(a).

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18 The DFE is not about fairness, it "is about power,"
19 *National Union Fire Insurance v. United States*, 115 F.3d
20 1415, 1422 (9th Cir. 1997); the sovereign "reserve[s] to
21 itself the right to act without liability for misjudgment
22 and carelessness in the formulation of policy," *id.* "[T]he
23 DFE bars suit only if two conditions are met: (1) the acts
24 alleged to be negligent must be discretionary, in that they
25 involve an 'element of judgment or choice' and are not
26 compelled by statute or regulation and (2) the judgment or
27 choice in question must be grounded in 'considerations of
28 public policy' or susceptible to policy analysis."
29 *Coulthurst v. United States*, 214 F.3d 106, 109 (2d Cir.
30 2000) (quoting *United States v. Gaubert*, 499 U.S. 315, 322-
31 23 (1991)). Plaintiffs bear the initial burden to state a

1 claim that is not barred by the DFE. *See Gaubert*, 499 U.S.
2 at 324-25. Here, Plaintiffs have failed to make the
3 necessary showing.

4 Plaintiffs' harm ultimately stems from the SEC's
5 failure to investigate Madoff and uncover his Ponzi scheme.
6 As a result, the conduct Plaintiffs seek to challenge is
7 "too intertwined with purely discretionary decisions" made
8 by SEC personnel. *Gray v. Bell*, 712 F.2d 490, 515 (D.C.
9 Cir. 1983); *see generally id.* at 515-16. Despite our
10 sympathy for Plaintiffs' predicament (and our antipathy for
11 the SEC's conduct), Congress's intent to shield regulatory
12 agencies' discretionary use of specific investigative powers
13 via the DFE is fatal to Plaintiffs' claims. *See Berkovitz*
14 *by Berkovitz v. United States*, 486 U.S. 531, 538 & 538 n.4
15 (1988) (quoting H.R.Rep. No. 1287, 79th Cong., 1st Sess., 6
16 (1945)). In satisfaction of the first prong of the DFE, the
17 SEC retains complete discretion over when, whether and to
18 what extent to investigate and bring an action against an
19 individual or entity. *See* 15 U.S.C. § 78u(a)(1); 17 C.F.R.
20 § 202.5(a)-(b). The conduct in question here meets the
21 second prong of the DFE by virtue of the SEC's choices
22 regarding allocation of agency time and resources being
23 sufficiently grounded in economic, social and policy

1 considerations. See *Bd. of Trade of City of Chicago v. SEC*,
2 883 F.2d 525, 531 (7th Cir. 1989); cf. *Coulthurst*, 214 F.3d
3 at 108-11.

4 We find additionally that the district court did not
5 abuse its discretion in denying Plaintiffs' Rule 60(b)
6 motion for relief from judgment, or in denying Plaintiffs'
7 request for jurisdictional discovery. *Boule v. Hutton*, 328
8 F.3d 84, 95 (2d Cir. 2003) (we review denials of Rule 60(b)
9 motions for abuse of discretion); *Best Van Lines, Inc. v.*
10 *Walker*, 490 F.3d 239, 255 (2d Cir. 2007) (we review district
11 court's refusal to permit jurisdictional discovery for abuse
12 of discretion). We have considered Plaintiffs' remaining
13 arguments and find them to be without merit.

14 **Conclusion**

15 For the foregoing reasons, the order of the district
16 court is hereby **AFFIRMED**.