JUDICIAL PANEL

ON

MULTIDISTRICT LITIGATION

In Re HARMONY LOAN COMPANY, INC. SECURITIES LITIGATION	Docket No. 154

BRIEF OF THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION TO THE MOTION FOR CONSOLIDATED OR COORDINATED PRETRIAL PROCEEDINGS

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QUESTIONS PRESENTED

Whether a Commission enforcement action seeking to obtain a preliminary and permanent injunction against future violations of and which has 11 parties to it, should be consolidated or coordinated with two private actions seeking primarily money damages which involve numerous factual issues not present in the Commission's action and have as many as 51 parties to them, when such consolidation or coordination will (a) add numerous other parties and issues to the Commission's action as a result of pretrial proceedings which will take place in the private actions and (b) result in substantial delay in prosecution of the Commission's action.

COUNTERSTATEMENT OF THE CASE

The Securities and Exchange Commission submits this brief in opposition to the motion of John A. O'Toole and others for consolidated or coordinated pretrial proceedings of three district court actions, two pending in the Southern District of Ohio and one pending in the Eastern District of Kentucky. The Commission opposes the motion insofar as it requests consolidation or coordination of its enforcement action[1/] seeking injunctive relief to prevent further violations of the federal securities laws with two private actions largely seeking money damages.[2/] All three actions involve inter alia, alleged violations of the federal securities laws by Harmony Loan Company, Inc. ("Harmony"), its officers, directors, principal shareholders and others. As discussed infra, however, the private actions involve numerous other claims and parties not involved in the Commission's action.

The Commission's complaint involves two counts, one involving the alleged fraudulent sale of $1,500,000 of Harmony debentures to

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1/ Securities and Exchange Commission v. Fisher, et al., S.D. Ohio, No. 8876, filed July 5, 1973.

2/ Mathews, et al. v. Fisher, S.D. Ohio, No. 8482, filed July 7, 1972. Monohan, Trustee v. Fisher, et al., E.D. Ky., No. 1733, filed August 9, 1973.

Of the four moving parties, O'Toole is a defendant in both the Commission's action and the Monohan action, and an additional defendant in the Mathews action; King is a defendant in the Monohan action and an additional defendant in the Mathews action; and the other two, O'Toole, Lee and King, a partnership, and O'Toole, Lee and King, Inc., are defendants in the Monohan action only.

the investing public (SEC ¶¶12-21),[3/] and the other involving the alleged fraudulent transfer of control of Harmony from one group of the defendants to another (SEC ¶¶23-29). These allegations are claimed to constitute violations of the anti-fraud provisions of the federal securities laws[4/] and a preliminary and permanent injunction are sought to prevent a recurrence of such violations. Because the Commission has reason to believe there is a danger that the fraud perpetrated by the defendants on the investing public may be repeated, possibly through the manipulation of another small loan company or other corporation, and because the Commission needs no discovery, it has recently moved for summary judgment seeking both a preliminary and permanent injunction.

Mathews v. Fisher (S.D. Ohio, No. 8482), which was filed in July 1972, is a suit by some of the defendants in the Commission's action for a sum of money claimed to be due and owing as a result of the plaintiffs' sale of all the voting stock of Harmony to the defendants (Fisher ¶5). This cause of action is grounded on a

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3/ The referenced pleadings in the three actions for which consolidation is sought are cited herein as follows: "SEC ¶___" refers to the numbered paragraphs of the Commission's Complaint; "Fisher ¶___" refers to the Answer, Counterclaim and Third Party Complaint filed by Fisher in response to the complaint of Mathews et al.; "Monohan ¶___" refers to the Complaint of the trustee in bankruptcy for Harmony Loan Company.

4/ Section 17(a) of the Securities Act of 1933 ("Securities Act"), 15 U.S.C. 77g(a), and Section 10(b) and the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. 78j(b), and Rule 10b-5 promulgated thereunder, 17 C.F.R. 240.10b-5.

contract theory having no relationship at all with the securities laws. Defendant Fisher, however, has set up the defense of fraud in the sale of that stock, claiming that false representations were made with respect to Harmony's financial condition (Fisher ¶2), and that the financial statements given to Fisher by plaintiffs were fraudulent and were not prepared in accordance with generally accepted accounting principles, as warranted by plaintiffs (Fisher ¶4, 6, 7). While it is not entirely clear from the pleadings, it appears that the counterclaim and the Commission's action may contain common issues of fact with respect to some of the alleged false statements attributed to two plaintiffs who are also defendants in the Commission's suit; Fisher is himself a defendant in the Commission's suit.

As another element of the counterclaim, Fisher charges that plaintiffs, in their capacity as officers and directors of Harmony, engaged in self-dealing with other concerns in which they had a management and ownership interest, thereby diverting hundreds of thousands of dollars from Harmony to their own benefit (Fisher ¶10). Again, it is not clear from the pleadings, but it appears that this claim may share some common issues of fact with the charges in the Second Claim of the Commission's complaint. As a result of the wrongful acts charged to the plaintiffs, Fisher claims to have suffered damages in the amount of $300,000 (Fisher ¶11).

Fisher also asserts claims against 19 individual and corporate third-party defendants, including six who are defendants in the Commission's action (Fisher ¶12-28). These additional claims appear to contain some issues of fact common to the Commission's action. Fisher also alleges that two third-party defendants (Rodney Sands and "John Doe, aka Mr. Whitecloud") "threatened the use of force and violence" in pursuit of a conspiracy to defraud Fisher and Harmony Loan Company (Fisher ¶¶17-18). Fisher asserts a claim for money damages against the third party defendants, also in the amount of $300,000 (Fisher ¶28).

On July 14, 1972, three additional parties filed a motion to intervene in the Mathews action in order to assert in a class action the rights of those who had invested in Harmony Loan Co. The substance of the complaint of the intervening plaintiffs is similar to the counterclaim of Fisher described above.[5/] Judgment in the amount of $3,000,000 compensatory and $3,000,000 punitive damages are sought. Further, the intervening plaintiffs have also brought in a number of additional defendants, including the securities regulatory

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5/ One of the original intervening plaintiffs was Arco Financial Corporation which was alleged to be the owner of all the voting stock of Harmony; Fisher is alleged to be the principal shareholder of Arco Financial. On June 29, 1973, notice of dismissal without prejudice as to Arco was filed, at which time the intervening plaintiffs filed their second amended complaint and cross-claims.

agencies of the States of Kentucky and Ohio. In total, there are now 51 parties to the Mathews suit, while there are only 11 in the Commission action. None of the claims in the Mathews suit have as yet been determined to be on behalf of any class.

In Monohan, Trustee v. Fisher, et al. (E.D. Ky., No. 1733), the trustee in bankruptcy for Harmony has brought an action against 32 individual and organizational defendants (including all ten of the defendants named in the Commission's action). Count I alleges violations of the federal securities laws which are, substantially, the two claims asserted by the Commission (Monohan ¶¶7-28). Thus, it appears that the entire substance of the Commission's complaint is covered in the trustee's complaint and there are, therefore, common issues of fact and law. However, the trustee has brought in many additional defendants in his action and he has alleged numerous acts and practices not included in the Commission's complaint. (See e.g., Monohan ¶¶10(a) and (d), 11(a) and (d), 26(c)). Thus, a substantial number of non-common issues of fact are raised, particularly with regard to the twenty-two additional defendants.

In addition, the trustee argues several alternative theories upon which he can recover damages. Although substantially the same issues of fact are involved in these other counts as are involved in the count based on securities laws violations, it would appear that these other theories will also require proof of some additional

elements not required under the federal securities laws. Count II is predicated on breach of fiduciary duties, fraud, fraudulent conveyances, and unjust enrichment in the course of self-dealing activities in which corporate funds and assets of Harmony were allegedly diverted to the defendants' own benefit or to the benefit of corporations owned or controlled by them (Monohan ¶¶29-32). Count III alleges violations of the blue sky statutes of Kentucky and Ohio (Monohan ¶¶33-34). Count IV is based on allegations of malpractice on the part of those defendants who were the attorneys or accountants for Harmony (Monohan ¶¶35-39). Count V alleges a conspiracy by defendants to perpetrate the fraud outlined in the other counts (Monohan ¶¶40-41).

The trustee asks the court for various forms of equitable relief, including the rescission of certain transfers and other transactions, the imposition of constructive trusts for the benefit of Harmony and its creditors, an accounting, and the entering of preliminary and permanent injunctive relief with respect to any further activities concerning Harmony. Money damages in the amount of $6,000,000 are sought.

The posture of the Commission's case is that the Commission is ready to proceed with a motion for summary judgment for a preliminary and permanent injunction and has recently filed such a motion in the District Court for the Southern District of Ohio. Primarily because

of the Commission's participation in the Harmony Loan Co. bankruptcy proceedings,[6/] substantially all of the facts it will rely on in seeking an injunction have been developed, and no further discovery will be required for this motion. Although some of the defendants in the Commission's action had earlier indicated they would require some discovery, none have requested discovery since the suit was filed in July 1973. The record developed in the bankruptcy proceeding is of course, available to these defendants.

In Mathews, et al. v. Fisher, no discovery requests have been made by any party since the suit was filed on July 7, 1972, almost a year and a half ago. In Monohan, Trustee v. Fisher, the trustee made a request for production of documents and propounded interrogatories to various defendants on September 12, 1973. To date, there has been no response to these requests.

Counsel for the trustee has indicated to all the parties in all three suits that he is willing to cooperate with counsel for the other parties involved in this litigation in arranging discovery procedures which are convenient for all concerned.[7/] Since the other two

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6/ In the Matter of Harmony Loan Co., Inc., E.D. Ky., No. 72-8446.

7/ See letter of November 14, 1973 from Lawrence R. Elleman, Esquire, counsel for Monohan, Trustee, to Theodore Sonde, Esquire, Assistant General Counsel, Securities and Exchange Commission, attached hereto as Exhibit A.

actions have been assigned to District Judge Hogan in the Southern District of Ohio, and the trustee himself is the only person not also a party to the two Ohio actions, it would appear that the trustee's offer should enable the one judge in that district to exercise whatever supervision is required to ensure that procedures are developed which are as fair as possible for all parties.

ARGUMENT

I. THE COMMISSION'S INJUNCTIVE ACTION TO PREVENT FUTURE VIOLATIONS OF THE SECURITIES LAWS SHOULD NOT BE CONSOLIDATED WITH TWO SOMEWHAT RELATED PRIVATE ACTIONS.

A. Consolidation of the Few Cases Here Involved Would not Promote the Just and Efficient Conduct of the Litigation.

As we have noted, consolidation is being sought in this litigation for only three district court actions arising in two adjacent districts. The Panel has previously made it clear that where "there are a minimal number of cases involved in the litigation, the moving party bears a strong burden to show that the common questions of fact are so complex and the accompanying common discovery so time-consuming as to overcome the inconvenience to the party whose action is being transferred and its witnesses."[8/] This, we submit, the moving party has failed to do.

8/ In Re Scotch Whiskey, 299 F. Supp. 543, 544 (J.P.M.L., 1969); accord, In Re Homemakers Franchise Litigation, 337 F. Supp. 1342, 1343-1344 (J.P.M.L., 1972), In Re Multidistrict Labor Litigation involving Iowa Beef Packers, Inc. and Amalgamated Meatcutters and Butcher Workmen of North America, 309 F. Supp. 1259 (J.P.M.L., 1970), In Re Multidistrict Civil Antitrust Litigation Involving Photocopy Paper, 305 F. Supp. 60 (J.P.M.L., 1969). Cf., In Re IBM Litigation, 302 F. Supp. 796 (J.P.M.L., 1969), where three private antitrust actions were consolidated because full development of the evidence would require extensive discovery, most of which would be complex and common to all cases, and where the two cases filed in the same district had not been assigned to a single judge. There, the Panel was "convinced" that the "inevitable extent and complexity of projected discovery qualifies these cases as 'exceptional' so that transfer and consolidation is required." Id. at 799.

To meet this burden, the moving parties have submitted to the Panel a brief purporting to show that the actions have common parties (Br. 4-6), that the actions have common questions of fact (Br. 6-9), and that the actions have common questions of law (Br. 9-10). While these assertions are true so far as they go, they ignore the practical effects of consolidation. The introduction by way of consolidation of forty additional parties to the Commission's suit will substantially add to the number of non-common issues of fact. Also, as discussed more fully supra pp. 3-7, the claims asserted in the private suits raise numerous additional issues not present in the Commission's injunctive action, which will further increase the number of non-common issues. Further, the moving parties have made no showing, nor have they even alleged, that the common questions of fact are so complex as to require consolidation or coordination. Similarly, although the moving parties generally allege that consolidation or coordination would be "convenient" for the parties (Br. 10-11), they fail to show or even allege that discovery in these cases will be so time-consuming as to overcome the prejudice to the Commission's action that would result from this Panel's order to consolidate. See discussion infra pp. 17-20.

As noted supra pp. 3-7, the private actions involve many claims not related to the federal securities laws. Those claims will require proof in addition to that which will be required to support the claims under the federal securities laws and accordingly, substantially increase the number of non-common issues of fact as between the various actions. Even in those areas where the Commission's

action and the private actions involve common questions of fact, the difference in the nature of the two types of proceedings means that there are many more additional factual issues involved in the private action than in the Commission's enforcement proceeding. As the Court of Appeals for the Second Circuit explained in Securities and Exchange Commission v. Culpepper, 270 F.2d 241, 250 (1959), an enforcement action under the Securities Act of 1933, quoting from Hecht Co. v. Bowles, 321 U.S. 321, 331 (1944), ". . . the standards of the public interest not the requirements of private litigation, measure the propriety and need for injunctive relief in these cases." See Securities and Exchange Commission v. Everest Management Corporation, 475 F.2d 1236 (C.A. 2, 1972). See also Securities and Exchange Commission v. Great American Industries, Inc. 407 F.2d 453 (C.A. 2, 1968) (en banc), certiorari denied, 395 U.S. 920 (1969) and Securities and Exchange Commission v. Spectrum, Ltd., C.A. 2, No. 72-2369, decided December 4, 1973; compare, Lanza v. Drexel & Co., 479 F.2d 1277 (C.A. 2, 1973) (en banc).

In essence, the Commission's proof will be limited to demonstrating that the defendants engaged in certain acts and transactions which had the effect of operating as a fraud upon Harmony (Count II) and that they sold securities on the basis of materially false statements (Counts I and II). The Commission need not prove "scienter" or that any investor was actually misled by the false statements. Securities and

Exchange Commission v. Everest Management Corp., supra, 475 F.2d at 1240. Also, the Commission will have no obligation to establish reliance upon the false statements as will undoubtedly be an element of proof in the private actions.[9/] Further, the private actions will necessarily involve proof of actual damages, a complicated and time-consuming element of proof that is missing from the Commission's action.

A factor which may simplify matters here, as indicated supra, pp. 8-9, is that the plaintiff in the only action which was not brought in the Southern District of Ohio, the trustee in bankruptcy, has already indicated that he will voluntarily cooperate with counsel in arranging discovery procedures which are convenient for all concerned. The Panel ought not to order consolidation of the Commission's action with the private actions when it is not necessary.

B. Consolidation of the Commission's Action Would not Promote the Just and Efficient Conduct of its Litigation, in Which Discovery has been Substantially Completed.

In a number of cases, this Panel has considered it inappropriate to order consolidation of an action where one or more of the parties'

9/ While the Supreme Court has recently stated that proof of reliance was not necessary in the case before it, which involved a complete failure to disclose, Affiliated Ute Citizens v. United States, 406 U.S. 128, 153-154 (1972), in the instant case some proof of reliance will undoubtedly be necessary in the private actions.

preparation for trial had substantially been completed, on the ground that such consolidation would not contribute to the convenience of such parties or to the just and efficient conduct of their litigation.[10/] As Judge Weinfeld noted, dissenting in In Re National Student Marketing Litigation, CCH Fed. Sec. L. Rep. [1972-73 Transfer Binder] ¶93,743 (J.P.M.L., 1973),[11/] an action brought by the Commission will usually be more advanced than related private actions because of the Commission's prior investigation. In such cases, the Commission

> ". . . has substantially developed the essential facts required to support its application to the courts for equitable relief; therefore, the need for further discovery is minimal and vastly different from those who allege private injury and seek money damages. To lump the SEC action with the private lawsuits would result in a slowdown in its effort to protect the public; it would defeat rather than promote the just and efficient conduct of the SEC litigation" (Slip Op. 1).

Such is the situation in the Commission action which is the subject of this motion. The Commission's Chicago Regional Office has devoted

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10/ In Re Glenn W. Turner Enterprises Litigation, 355 F. Supp. 1402, 1404 (J.P.M.L., 1973); In Re King Resources Securities Litigation, 342 F. Supp. 1179, 1184, n. 13 (J.P.M.L., 1972); In Re Grain Shipments, 300 F. Supp. 1402, 1405 (J.P.M.L., 1969); In Re Protection Devices and Equipment and Central Station Protection Service Antitrust Cases, 295 F. Supp. 39, 40 (J.P.M.L., 1968).

11/ For some reason, the Panel's opinion of January 29, 1973 in In Re National Student Marketing Litigation, Docket No. 105, has never been officially reported, so far as we have been able to determine, and even the unofficial report of it contained in CCH Fed. Sec. L. Rep. is not complete in that it does not include the concurring opinion of Judge Weigel or the dissenting opinion of Judge Weinfeld. A later opinion of the Panel in the same litigation is, however, reported at 358 F. Supp. 1303. For this reason, we refer herein to the dissenting slip opinion of Judge Weinfeld as "Slip Op. __".

considerable time to development of the facts in this case, particularly through its participation in the bankruptcy proceedings for Harmony Loan Company. In the Commission's view, the evidence now available is sufficient to justify the granting of the summary judgment for which it has applied. Furthermore, although the defendants in the Commission's action had earlier indicated that they would require discovery, no requests have been presented in the five months since the suit was filed. Similarly, no discovery has been sought in the Mathews case, even though it has been pending for almost a year and a half.

The private parties in the actions for which consolidation is sought would not be prejudiced if these actions are not consolidated or if the Commission's action should be excluded from any transfer the Panel might order. Those parties will in any event have ample opportunity to pursue whatever discovery they may yet require for proper presentation of their position in those cases. In contrast, the Commission, which has, as a practical matter, completed the discovery it requires, could be greatly prejudiced if it should be required to devote its limited manpower resources to participate in discovery and other pretrial procedures from which it has virtually nothing to gain. On the other hand, any delay in granting the Commission's injunctive relief is likely to result in further violations of the federal securities laws by some of the defendants with consequent injury to public investors. It would be most unfortunate if

those seeking recompense for injury should delay the Commission's injunctive request and thus contribute to the injury of others.

C. Consolidation of the Commission's Action Would Severely Prejudice the Public Interest in Securing Prompt Relief from Violations of the Federal Securities Laws.

As noted above, the Commission has moved for summary judgment seeking a preliminary and permanent injunction in its case against all the defendants, believing that it needs no discovery and that prompt relief is necessary. In these circumstances, consolidation or coordination of the Commission's action with the private actions which are apparently in a far less developed stage would unduly hinder the prosecution of this action to the severe detriment of the public interest in effective securities law enforcement.

The result of consolidation of a government injunctive action with private damage suits is substantial delay during all pretrial phases of the case. The obtaining of fast temporary or preliminary injunctive relief is complicated and slowed, making it more likely that new violations will be committed before the defendants can be enjoined. The Commission believes that expediting of this case is required in order to protect the investing public, which has already been victimized by, among other things, the sale by fraudulent means of over $1,500,000 worth of Harmony Loan Company debentures. It appears that the defendants were planning to continue with the sale of

debentures; they had recently authorized Harmony to issue and sell another $1,250,000 worth of debentures (SEC ¶30). Although Harmony itself is now in receivership, the same type of fraudulent scheme, unless enjoined, may be carried out by using another loan company or other type of corporation.

Because the practice in the Southern District of Ohio has been not to grant preliminary injunctive relief until defendants have had a chance to utilize discovery procedures, and because the defendants in the Commission's case had indicated to the Commission's counsel that they would require discovery, the Commission did not move immediately after the filing of the complaint for a preliminary injunction. However, because the defendants have presented no requests for discovery in the five months since the complaint was filed, we have now moved for summary judgment.

The Commission's experience with the National Student Marketing case since this Panel's decision in In Re National Student Marketing Litigation, supra, is instructive as to why consolidation or coordination of Commission actions should not be encouraged and why in some cases it may result in a disadvantage to the public interest which the Commission seeks to protect. The Commission's experience with motions under Section 1407 indicates that when such motions are filed, the parties attempt to dispose of the matter before the Panel before continuing with the prosecution of the cases in the district courts. District court judges have also adopted this attitude. Thus, in

National Student Marketing, the motion to the Panel was filed in April 1972. Following oral argument before the Panel and in response to a request of Commission counsel for an early trial date, several defendants moved the district court to stay all proceedings pending a determination by the Panel. The judge presiding over the Commission's case subsequently ordered that all proceedings in the Commission's action, including the taking of all depositions and discovery, be held in abeyance "until such time as the Judicial Panel on Multidistrict Litigation has indicated what course of action should be taken in this and other related cases."[12/] While this was done at a time when the Chairman of the Panel had indicated that the Panel had "tentatively decided to transfer" all the actions involving National Student Marketing to the District of Columbia for coordinated or consolidated pretrial proceedings, and that "the Panel desired to order these cases transferred within the next two weeks",[13/] no decision by the Panel was forthcoming for an additional three months. Finally, after a six-month period during which the Section 1407 motion was sub judice, a transfer order was issued on December 1, 1972, without any accompanying opinion. It was only on January 29, 1973, more than ten months after the motion had been filed with the Panel, that an opinion and final order

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12/ See order of August 18, 1972 in Securities and Exchange Commission v. National Student Marketing Corp., D.D.C., Civil Action No. 225-72.

13/ See letter from Chairman Murrah to Chief Judge Edelstein of the United States District Court for the Southern District of New York in that case.

was rendered in the proceeding. For all practical purposes, the filing of the motion with the Panel in April 1972 had the effect of staying the Commission's action until early February 1973.

The effect of the Panel's decision has been to delay further the Commission's action and to add further to the prejudice to the public interest that had already occurred because of the Panel's prior inaction. Although the Commission had hoped to secure disposition of its civil suit prior to any criminal prosecution, the statutory limitations for institution of such prosecution necessitated a referral of the results of the Commission's investigation to the Department of Justice for action in that regard. Now, a grand jury is currently investigating the matter, and if indictments are returned and a parallel criminal proceeding is begun, it will undoubtedly further complicate the Commission's civil injunctive action.

Although the district judge to whom the consolidated National Student Marketing litigation was assigned is clearly exerting his best efforts to move these cases along expeditiously, the long delay arising out of the motion before the Panel meant that when the proceedings were resumed, the district judge was confronted with numerous complex motions to dispose of and no discovery was permitted in the interim. Even now, while discovery has commenced, only documentary discovery has occurred in the Commission's action and even that is far from concluded. Also, the plaintiffs in the private actions have to date not participated in discovery. While the district judge indicated that he hoped to have the Commission's case tried in the

spring of next year, that no longer seems possible, particularly since no depositions have yet been scheduled. In the meantime, although National Student Marketing Corporation has itself consented to an injunction, other defendants whose future conduct poses a threat to public investors are as yet under no restraint whatever, despite the fact that some had earlier indicated a willingness to negotiate a settlement. The Commission feels that the consolidation of its case with the private damage actions has had an inhibiting effect on the obtaining of consent judgments. When the cases are all before the same judge, a defendant is more likely to feel that a concession made to the Commission in its enforcement action will, as a practical matter, operate against his interests in the private damage actions.[14/]

We believe it would be useful for the Panel to reconsider the legislative history of the statute creating the Panel. The legislation was prompted by the institution of more than 2000 private antitrust damage suits filed in 35 federal district courts that followed the successful criminal prosecution under the antitrust laws of electrical equipment manufacturers in 1961. This wave of private litigation threatened to engulf the judicial system and it was only through voluntary joint pretrial proceedings that order was restored. Based

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14/ It should be noted that apparently few cases transferred by the Panel are ever retransferred for trial. See Comment, The Experience of Transferee Courts Under the Multidistrict Litigation Act, 39 U. Chi. L. Rev. 588, 607 (1972).

upon this experience, the statute sought to provide centralized management under court supervision of pretrial proceedings of multidistrict litigation to assure the "just and efficient conduct" of such actions.[15/]

Significantly, the primary focus during the hearings which led to the enactment of Section 1407 was upon the problems posed by multiple litigation involving private damage actions instituted by private parties or government entities acting in a proprietary capacity, principally those brought under the antitrust laws.[16/] As noted by Judge Weinfeld, the legislative history "indicates that no consideration was given to exempting the SEC from its provisions." Slip Op. 2. In fact, the Senate Report accompanying the bill which became Section 1407 indicates that it was not contemplated that any government injunctive actions involving federal remedial statutes were to be encompassed within the provisions of Section 1407. The report recommended passage of the legislation in the context of coordinating "such diverse instances of mass litigation as antitrust damage suits, cases of civil liability arising from mass accidents, products liability claims, and complex patent infringement litigation"

15/ See S. Rep. No. 454, 90th Cong., 1st Sess. 1, 2-4, 6-7 (1967); H.R. Rep. No. 1130, 90th Cong., 2d Sess. (1968), 1968 U.S. Code, Congressional and Administrative News, pp. 1898-1901.

16/ See Hearings before the Subcommittee on Improvements in Judicial Machinery of the Senate Committee on the Judiciary, 89th Cong., 2d Sess. 2, 5-6, 26, 29, 44, 51-53, 123 (1966-1967). Hearings before Subcommittee No. 5 of the House Committee on the Judiciary on H.R. 3991, 6703, 8276 and 16575, 89th Cong., 2d Sess. 21, 26 (1966).

(emphasis added). S. Rep. No. 454, 90th Cong., 1st Sess. 7 (1967). We are unaware of any reported instance prior to enactment of Section 1407 where a court had favorably entertained a request under Rule 42(a) to consolidate, over the government's opposition, a government enforcement action seeking injunctive or similar equitable relief with private damage suits. The reason for this result was set forth by Judge Weinfeld in United States v. American Society of Composers, Authors & Publishers, 11 F.R.D. 511, 513 (S.D.N.Y., 1951), where a private litigant sought to intervene in a government action:

> "Sound public policy dictates that where Government is the complainant in a suit its conduct and control of litigation be free from interference by private citizens. The protection of the public interest rests upon those officials whose special responsibility and duty it is to enforce the laws. To permit intervention by private citizens, whose purpose in the main is self interest, in proceedings instituted by the Government is more likely to hinder rather than help in the enforcement of laws."

As discussed infra pp. 23-26, the standards applicable to granting permissive intervention are not very different from those set forth in Section 1407, nor are the practical effects of such intervention. Had Congress, in enacting Section 1407, sought to change this judicial attitude, we believe it would have done so in clear and unmistakable language or at least adverted to it in the legislative history. To imply, as the Panel has done, that the absence of an express exemption for government injunctive actions, except those under the antitrust laws, requires that they be subjected on the same basis as other civil actions to consolidated pretrial proceedings, is unwarranted. Congress'

silence cannot be deemed to constitute approval of a device which impedes other objectives it has sought to further.

These same considerations recently resulted in the Second Circuit upholding a district court's denial of permissive intervention under the Federal Rules of Civil Procedure. Securities and Exchange Commission v. Everest Management Corporation, supra, 475 F.2d 1236 (C.A. 2, 1972). Under Rule 24(b)(2) of the Federal Rules of Civil Procedure intervention may be permitted:

> ". . . (2) when an applicant's claim or defense and the main action have a question of law or fact in common. . . . In exercising its discretion the court shall consider whether the intervention will unduly delay or prejudice the adjudication of the rights of the original parties."

These standards do not differ materially from those contained in Section 1407.

In Everest Management, as in this litigation, there was no doubt that the private claims and the Commission's claims presented "a number of common questions of law and fact," and in that case the only issue was whether intervention would "unduly delay or prejudice the adjudication of the rights of the original parties." 475 F.2d at 1239. Appellants argued that intervention would avoid a costly and time-consuming duplication of the Commission's efforts. Furthermore, they contended, intervention would further a policy consistently favored by the federal courts, that of securing vigorous enforcement of the securities laws through private actions. Id. The court held, however, that the district court properly resisted the "surface gloss" of these

arguments for intervention. Id.

The Commission's workload, noted the court, "would be substantially increased" if intervention were permitted, since "additional issues would have to be tried in the main action." Thus, the result, as the court perceived it, would be that "[a]lready complicated securities cases would become more confused and complex," imposing a greater burden on the Commission's "limited budget and staff." Id. at 1240.[17/]

Furthermore, the court pointed out, the Commission is able to bring the large number of enforcement actions it does primarily because in all but a few cases consent decrees are entered. The intrusion of private parties into Commission litigation would have an adverse effect on this aspect of the Commission's operations, since "the intervention of a private plaintiff might tend to discourage or at least to complicate efforts to obtain a consent decree." Id. This is, as we have noted, precisely the result that has occurred in the National Student Marketing case.

Moreover, contrary to the Panel's view in National Student Marketing, CCH Fed. Sec. L. Rep. [1972-73 Transfer Binder] ¶93,743 at 93,256, the exclusion of a Commission injunctive action is not precluded

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17/ While the responsibilities the Commission presently faces are much greater than existed in 1940, the Commission's staff in 1972 (1,559) was fewer in number than in 1940 (1,670). See Sixth Annual Report of the Securities and Exchange Commission (Fiscal Year Ended June 30, 1940), at 189; Thirty-Eighth Annual Report of the Securities and Exchange Commission (Fiscal Year Ended June 30, 1972), at 136.

by the language of Section 1407(a), which authorizes the Panel to transfer "civil actions involving one or more common questions of fact pending in different districts" (emphasis added) upon the Panel's determination that such transfer will serve "the convenience of parties and witnesses" and will "promote the just and efficient conduct" of such actions. The Panel has framed the inquiry as to whether these criteria have been satisfied in terms that it must "weigh the interests of all the plaintiffs and all the defendants and must consider multiple litigation as a whole in light of the purposes of the law."[18/] We submit that to accord significant, if not controlling, weight to the interest of the public in securing injunctive relief as quickly as possible does no violence to the standard enunciated by the Panel and indeed is consistent with well-recognized principles that "the public interest, when at conflict with private interest, is paramount." Securities and Exchange Commission v. Culpepper, supra, 270 F.2d at 250.

Finally, in view of the absence of any evidence that Congress affirmatively sought to include government injunctive actions within the purview of Section 1407 and the fact that the exclusion of such actions would not be inconsistent with the criteria enunciated in

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18/ In Re Master Key, 320 F. Supp. 1404, 1406 (J.P.M.L., 1971); In Re Admission Tickets, 302 F. Supp. 1339, 1341 (J.P.M.L., 1969); In Re Children's Book Litigation, 297 F. Supp. 385, 386 (J.P.M.L., 1968). The Commission has never conceded, as the Panel implied in National Student Marketing, supra, CCH Fed. Sec. L. Rep. [1972-73 Transfer Binder] ¶93,743 at 93,256, that the nature of the inquiry framed by the Panel was appropriate where a government injunctive action was involved. To the contrary the Commission has urged that the Panel was required to look at the nature of the Commission as an independent controlling factor.

Section 1407(a), we believe the Panel in National Student Marketing disregarded express legislative policy by failing to give effect to the factors which prompted Congress to exempt government antitrust injunctive actions from the provisions of Section 1407.

It appears that the express exemption for government antitrust injunctive actions contained in Section 1407(g) was inserted out of an abundance of caution in view of the extensive litigation which had occurred in the antitrust area, and was considered only because the views of the Attorney General, the governmental officer responsible for antitrust enforcement, had been specifically requested.[19/] Exclusion of a Commission injunctive action from consolidated pretrial proceedings would in no way contravene any Congressional intent.

In enacting the exemption for government antitrust injunctive suits, Congress was concerned that "consolidation [of such suits] might induce private plaintiffs to file actions merely to ride along on the Government's cases." H. Rep. No. 1130, 90th Cong., 2d Sess. (1968), 1968 U.S. Code, Congressional and Administrative News p. 1902. While private actions must certainly be looked upon with favor under the

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19/ Hearings Before Subcommittee No. 5 of the House Committee on the Judiciary on H.R. 3991, 6703, 8276 and 16575, 89th Cong., 2d Sess. 27 (1966).

It may be of some significance that the Commission was not even asked to comment on the bill and the legislative history does not disclose that any other agency with similar enforcement powers was asked to or did comment on it as did the Department of Justice. If Congress had thought that this bill would affect our enforcement litigation, it is indeed strange that our views were not solicited, as is normally done, when hearings were held on it.

securities laws as well as under the antitrust laws, it would be most unfortunate if those seeking recompense for injury should delay the Commission's request for injunctive relief and thus contribute to the injury of others. Such a result is hardly consistent with the purposes of the federal securities laws. Congress recognized that a similar danger existed with respect to antitrust actions, noting that "[g]overnment suits would . . . almost certainly be delayed, often to the disadvantage of . . . injured competitors. . . ." Ibid. As the House Report explained in adopting the statement of the Attorney General in support of the antitrust exemption (Id. at p. 1905):

> "While exempting the government from this legislation [as to antitrust actions] may occasionally burden defendants because they may have to answer similar questions posed both by the government and private parties, this is justified by the importance to the public of securing relief in antitrust cases as quickly as possible. To treat the government differently is not arbitrary, for the purpose of the government suit normally differs from that of a private suit. The government seeks to protect the public from competitive injury while private parties are primarily interested in recovering damages for injuries already suffered" (emphasis added).

We submit that the Congressional purpose for the enactment of Section 1407(g) requires the Panel to attach significant, if not controlling, weight to the effect that consolidated or coordinated pretrial proceedings would have on the interests of the public in securing prompt relief in Commission suits.

The Court of Appeals in Everest Management held that "the complicating effect of the additional issues and the additional parties outweighs any advantage of a single disposition of the common

issues." 475 F.2d at 1240[20/] (emphasis added). In the context presented by this motion to consolidate or coordinate pretrial proceedings, these same "complicating effects" can be seen. Additional parties and additional issues will be brought in, making a relatively simple case far more complex; these issues will be the subject of discovery activities in which the Commission will have to participate, expending considerable manpower for minimal benefit. A case with eleven parties will become one with 51 parties, if the motion is granted. Furthermore, there is already reason to believe that the filing of this motion to consolidate has had the effect of deterring consent judgments which previously were being negotiated in this case. The same considerations which "outweigh[ed] any advantage of a single disposition of the common issues" in Everest Management also outweigh any advantage to be gained in this litigation through consolidated or coordinated pretrial discovery.

We urge the Panel to recognize the Congressional intent behind the securities laws and to read Section 1407 in a way which recognizes that intent and enables the Commission adequately to enforce those laws and to effectuate their remedial purposes. As Judge Weinfeld, dissenting in National Student Marketing, noted, "The courts have

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20/ See also Securities and Exchange Commission v. General Host Corp., CCH Fed. Sec. L. Rep. ¶94,121 (S.D.N.Y., 1973) and Securities and Exchange Commission v. National Student Marketing Corporation, CCH Fed. Sec. L. Rep. ¶93,968 (D.D.C., 1973).

frequently, in the exercise of their equity powers, and in the public interest, adopted policies adequate to the occasion." Slip Op. at 2. It is respectfully submitted that the Panel should seek to do no less than this.

II. IN THE EVENT THAT THE PANEL NEVERTHELESS ORDERS THE COMMISSION'S ACTION CONSOLIDATED FOR PRETRIAL PROCEEDINGS WITH THE TWO PRIVATE DAMAGE ACTIONS, THE SOUTHERN DISTRICT OF OHIO RATHER THAN THE EASTERN DISTRICT OF KENTUCKY SHOULD BE SELECTED AS THE TRANSFEREE COURT.

The moving parties before the Panel have not suggested which court they believe the various cases should be transferred to. The Mathews case has been pending before the Southern District of Ohio for approximately a year and a half. As is apparent from the description of that case and the direction it has followed (see pp. 3-6, supra), the Court has had to resolve a number of matters in disposing of the various motions that have so far been presented. In addition, we believe the District Judge who has been assigned to both the Commission's case and the Mathews case has developed some degree of familiarity with the underlying facts in the process. Further, since the Mathews case has more parties to it than either of the other two proceedings, and those parties have retained local counsel who have presumably been involved in the course of that litigation with various matters, we believe that it would also suit the convenience of the

parties to have the Monohan case, the one case not presently pending in the Southern District of Ohio, transferred to that district for pretrial proceedings pursuant to Section 1407.

Since the Commission does not contemplate any further discovery in its proceeding, it is difficult to assess which forum may be more appropriate for the discovery plans of the other parties. Nevertheless, an examination of the respective dockets in the two possible transferee districts indicates the desirability of transferring to the Southern District of Ohio.[21/] Although the 1972 annual report of the Administrative Office of the United States Courts indicates that the number of pending civil cases in the Southern District of Ohio (1,237) exceeds the number pending in the Eastern District of Kentucky (955), the fact that the Southern District of Ohio presently has five judges assigned to it while the Eastern District of Kentucky has only two judges assigned full time and one judge assigned to both the Eastern and Western districts of Kentucky strongly suggests that the number of cases assigned to each judge in the Southern District of Ohio is far less than in the Eastern District of Kentucky. Annual Report of the Director of the Administrative Office of the United States Courts (1973), Table C-1, p. 283.

21/ The legislative history of Section 1407 makes clear that one of the factors to be weighed in the selection of the transferee district is the state of its docket. H. Rep. No. 1130, 90th Cong. 2d Sess., 1968 U.S. Code, Congressional and Administrative News, p. 190. See also In Re National Student Marketing Litigation, supra, CCH Fed. L. Rep. [1972-73 Transfer Binder] ¶93,743 at 93,257.

CONCLUSION

For the foregoing reasons the Commission respectfully urges the Panel to deny the motion for consolidated or coordinated pre-trial proceedings pursuant to 28 U.S.C. §1407 insofar as it relates to the Commission's action for injunctive relief presently pending in the Southern District of Ohio. Further, the Commission urges that in the event such pretrial proceedings are ordered, the transfer should be made to the Southern District of Ohio rather than the Eastern District of Kentucky.

Respectfully submitted,

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WALTER P. NORTH
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THEODORE SONDE
Assistant General Counsel

BARRY D. GOLDMAN
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JAMES H. SCHROPP
Attorney

Dated: December 14, 1973

APPENDIX

EXHIBIT A

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November 14, 1973

REC'D - S.E.C.

NOV 16 1973

Theodore Sonde, Esq.
Securities & Exchange Commission
Washington, D.C. 20549

Re: Monohan, Trustee v. Fisher, Civil Action No. 1733,
United States District Court, Covington, Kentucky

Mathews v. Fisher, Civil Action No. 8382,
United States District Court, Cincinnati, Ohio

Dear Mr. Sonde:

We have for some time been considering the best method by which the discovery and pretrial proceedings in the above-entitled cases can be coordinated in a manner which would serve the ends of justice and at the same time not further complicate the proceedings by requiring additional formalities and needless expense and effort on the part of the parties and counsel. Under all the circumstances, we find ourselves unable to assent to a change of venue of the Kentucky case based on Section 1404 of the Code, which in our opinion would further delay and complicate the proceeding. On the other hand, after considerable discussion among ourselves and also with counsel for the investors, we would like to suggest a means by which the advantages of coordinated discovery between the cases can be obtained without a formal consolidation pursuant to Section 1407 of the Code, particularly in view of the fact that all of the attorneys and parties are in close physical proximity to one another.

We suggest that a stipulation and agreement be arrived at whereby depositions and other discovery may be undertaken in such a way as to be usable in both cases. In other words, depositions can be noticed in both cases simultaneously, and anything said by the witness may be used in either or both cases, subject, of course, to the normal evidentiary objections which might be interposed at trial. This procedure would be applicable as to discovery proceedings to be initiated by any party, including any of the defendants.

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OFFICE OF GENERAL COUNSEL

SEC "Exhibit A"

In our opinion, this suggestion will simplify the proceeding while at the same time avoiding unnecessary expense and complexity by reason of formal consolidation, and the attendant procedures employed in such consolidated cases.

Assuming that the general outline of this suggestion is acceptable, we are certain that the details of a stipulated entry can be worked out. Kindly give us your reaction to this suggestion by the end of next week.

Yours very truly,

DINSMORE, SHOHL, COATES & DEUPREE

Lawrence R. Elleman
Counsel for Edward S. Monohan,
Trustee

LRE:sl