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E-ALERT | White Collar

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GABELLI V. SEC AND ITS IMPACT ON GOVERNMENT INVESTIGATIONS

On February 27, 2013, the U.S. Supreme Court, in *Gabelli v. SEC,* unanimously held that the general five-year statute of limitations for federal government civil penalty actions begins to run when a fraud occurs, rather than when the government discovers it.[1] Although *Gabelli* itself is an SEC action to enforce the federal securities laws, the Court's ruling will also apply to a wide range of civil penalty actions brought by the Department of Justice and other federal agencies under, for example, the Foreign Corrupt Practices Act,[2] the Federal Election Campaign Act,[3] and the Clean Air and Clean Water Acts.[4]

We do not expect the decision to stop the government from bringing actions based on stale facts. Especially when government investigators view conduct as egregious or as falling within a high-priority enforcement area, they are likely to seek tolling agreements or attempt to use the "fraudulent concealment" or "continuing violation" doctrines to circumvent the five-year limitations period.

The Supreme Court's decision restored the interpretation of the statute of limitations for civil penalty actions that had generally prevailed for over 170 years, until the Second Circuit issued its decision in *Gabelli* in 2011. It split with four other Circuits and held that the statute of limitations "does not accrue until that claim is discovered, or could have been discovered with reasonable diligence, by the plaintiff."[5]

The Supreme Court made short shrift of the Second Circuit's (and the SEC's) position. In a brief opinion for the Court, Chief Justice Roberts wrote that under the "most natural reading of the statute," a claim accrues—and the five-year clock begins to tick—when the conduct occurs.[6] The Chief Justice could find no historical precedent for applying the "discovery rule" in a government civil penalties action and noted that the rationale for the discovery rule loses force in government actions.[7] Unlike a typical private plaintiff, a central mission of the SEC and other federal agencies is to ferret out potential violations, and they wield investigative tools, such as subpoena power, unavailable to private parties.[8]

Although *Gabelli* closed the door on the discovery rule in government civil penalty actions, it left open the fraudulent concealment doctrine, which tolls the five-year statute when "the defendant takes steps beyond the challenged conduct itself to conceal that conduct."[9] To avail itself of this loophole,

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[1] *Gabelli v. SEC*, 2013 WL 691002 (U.S. Feb. 27, 2013).
[2] *See SEC v. Jackson*, 2012 WL 6137551, at *25 (S.D. Tex. Dec. 11, 2012).
[3] *See Federal Election Comm'n v. National Republican Senatorial Comm.*, 877 F. Supp. 15, 18 (D.D.C. 1995).
[4] *See United States v. Ill. Power Co.*, 245 F. Supp. 2d 951, 954 (S.D. Ill. 2003); *United States v. C & R Trucking Co.*, 537 F. Supp. 1080, 1083 (N.D. W. Va. 1982).
[5] *SEC v. Gabelli*, 653 F.3d 49, 59 (2d Cir. 2011).
[6] *Gabelli*, 2013 WL 691002, at *4. The statute of limitations provides that "an action . . . for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued. . . ." 28 U.S.C. § 2462.
[7] *Gabelli*, 2013 WL 691002, at *5-7.
[8] *Id.* at *6.
[9] *Id.* at *4 n.2.

the government must find acts of concealment separate from the alleged violation, such as concealing bribes after they are paid or making misleading statements to derail an investigation.[10] Government lawyers may also make greater use of the continuing violation doctrine, which can apply to "continual unlawful acts" that began more than five years before an action is filed but continue into the limitations period.[11]

Ideally, *Gabelli* should encourage the SEC and other investigating agencies to apply a more targeted approach to gathering information. Rather than using blunderbuss subpoenas or document requests that often result in extended negotiations over scope and burden, regulators may be more inclined to focus on core issues early on and to make greater use of defense counsel to assist in identifying key documents and witnesses. In practice, however, the decision may result in earlier and more frequent requests for tolling agreements, such as when the government agrees to stand on the sidelines and allow companies to conduct a thorough internal investigation before considering enforcement action. Thus, while *Gabelli* removes a tool from the government legal arsenal, it does not sound the death knell of investigations and civil penalty actions based on events more than five years old.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our white collar practice group:

Bruce Baird	+1.202.662.5122	bbaird@cov.com
David Bayless	+1.415.591.7005	dbayless@cov.com
Christopher Denig	+1.202.662.5325	cdenig@cov.com
David Kornblau	+1.212.841.1084	dkornblau@cov.com
Ben Haley	+1.202.662.5194	bhaley@cov.com
Jason Levy	+1.202.662.5287	jmlevy@cov.com

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[10] *See Jackson*, 2012 WL 6137551, at *28; *UA Local 343 of the United Ass'n of Journeymen & Apprentices of the Plumbing & Pipefitting Indus. v. Nor-Cal Plumbing, Inc.*, 48 F.3d 1465, 1475 (9th Cir. 1995) ("Where a plaintiff suspects the truth but investigates unsuccessfully, fraudulent concealment will toll the statute.").
[11] *SEC v. Kelly*, 663 F. Supp. 2d 276, 288 (S.D.N.Y. 2009); *see also Jackson*, 2012 WL 6137551, at *29.