

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)

10  
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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17  
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,  
2

3 *Defendants-Appellees.\**  
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8 Before:

9 WESLEY, DRONEY, *Circuit Judges*, NATHAN, *District Judge.\*\**  
10  
11

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.  
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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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29  
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

3  
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).

17  
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**.