

Handwritten notes:
Muller
Pages

1 Paul Gonson
Associate General Counsel
2 Irving H. Picard
Assistant General Counsel
3 Howard B. Scherer
Attorney

4 Securities and Exchange Commission
5 500 North Capitol Street
Washington, D.C. 20549
6 Telephone: (202) 755-1238

7 Charles R. Hartman
Attorney

8 Securities and Exchange Commission
9 Suite 1710
10 10960 Wilshire Boulevard
Los Angeles, California 90024
Telephone: (213) 984-0011

11 Attorneys for Defendants Securities and Exchange Commission,
12 Roderick M. Hills, Philip A. Loomis, Jr., John R. Evans,
and Irving M. Pollack, Stanley Sporkin, Irwin M. Borowski,
13 James G. Mann, and Ralph Erickson

14 UNITED STATES DISTRICT COURT
15 CENTRAL DISTRICT OF CALIFORNIA

17 _____)
ELLIOT HANDLER, RUTH HANDLER,)
18 SEYMOUR M. ROSENBERG,)

19 Plaintiffs,)

20 v.)

21 SECURITIES AND EXCHANGE COMMISSION;)
RODERICK M. HILLS, PHILIP A.)
22 LOOMIS, JR., JOHN R. EVANS, and)
IRVING M. POLLACK, as Commissioners of the)
23 SEC; STANLEY SPORKIN, Individually and as)
Director, Division of Enforcement, SEC;)
24 IRWIN M. BOROWSKI, Individually and as)
Associate Director, Division of Enforce-)
25 ment, SEC; JAMES G. MANN, Individually)
and as Special Counsel, SEC; RALPH H.)
26 ERICKSON, Individually and as Assistant)
Administrator, Enforcement Division, Los)
27 Angeles Regional Office (Region 7), SEC;)
UNITED STATES DISTRICT COURT FOR THE)
28 CENTRAL DISTRICT OF CALIFORNIA;)

CIVIL No. 77-0067 WEG

MEMORANDUM OF POINTS AND
AUTHORITIES IN SUPPORT OF
THE MOTION OF THE DEFENDANTS
SECURITIES AND EXCHANGE COM-
MISSION, AND ITS COMMISS-
SIONERS AND EMPLOYEES, TO
DISMISS OR, IN THE ALTERNATIVE,
FOR SUMMARY JUDGMENT

1 EDWARD H. LEVI, as Attorney General of)
the United States; WILLIAM D. KELLER, as)
2 United States Attorney for the Central)
District of California;)
3)
Defendants.)
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ARGUMENT	11
I. Plaintiffs may not, through this separate action, prevent, forestall or impede the consideration by a grand jury of certain evidence and the possibility of a criminal indictment and subsequent prosecution arising out of their activities as corporate executives of Mattel, Inc. Plaintiffs must await indictment and prose- cution, at which time they can seek to suppress any evidence which may have been	

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unlawfully obtained. Such fully adequate
remedy makes this pre-indictment challenge
premature, and hence any injunction or
declaration of rights would be improper..... 11

A. The grand jury may properly
consider any evidence whatever its
source 11

B. This action is essentially a motion to
suppress evidence in a possible future
criminal case. It is premature and should
be dismissed..... 15

C. Because there is no criminal case
pending, plaintiffs' complaint
essentially seeks an advisory
opinion from this Court, which this
Court cannot give 17

D. The additional broad relief which the
plaintiffs seek is not within the
power of this, or any, Court to render.... 18

II. A court of equity should grant no relief
to the plaintiffs, for they come before
it with unclean hands, are estopped and
are guilty of laches. Moreover, they seek to
attack collaterally a final judgment entered
in another action which they may not do..... 19

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A. Plaintiffs may not attack
collaterally a final order
entered in another action 20

B. Plaintiffs have been dilatory
and a court of equity should not
countenance this lack of
diligence 22

III. The appointment of a special counsel,
pursuant to the second amended judgment
in Securities and Exchange Commission v.
Mattel, Inc., was entirely proper and in
keeping with the modern equity practice
of according complete relief in a fashion
carefully tailored to protect public
investors from a recurrence of the
violative conduct and to provide remedial
relief from such conduct..... 24

IV. Plaintiffs misconceive the roles of the
special counsel and special auditor in
Securities and Exchange Commission v.
Mattel, Inc., they acted as representatives
of Mattel, and represent no delegation
of authority or functions of the
Commission..... 30

CONCLUSION..... 37

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1 MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF
2 THE MOTION OF THE DEFENDANTS SECURITIES AND EXCHANGE
3 COMMISSION, AND ITS COMMISSIONERS AND EMPLOYEES, TO
4 DISMISS, OR IN THE ALTERNATIVE, FOR SUMMARY JUDGMENT
5

6 PRELIMINARY STATEMENT
7

8 On January 7, 1977, plaintiffs Elliot Handler, co-founder and formerly
9 chief executive officer and co-chairperson of the board of directors of Mattel,
10 Inc. ("Mattel"), Ruth Handler, co-founder and formerly president and co-chairperson
11 of the Mattel board, and Seymour Rosenberg, formerly Executive Vice President
12 Finance and Administration and a director of Mattel, filed this action against,
13 among others, the Securities and Exchange Commission; its Commissioners, Roderick
14 M. Hills, Philip A. Loomis, Jr., John R. Evans, Irving M. Pollack; and, individu-
15 ally and as Commission employees, Stanley Sporkin, Irwin M. Borowski, James
16 G. Mann, and Ralph H. Erickson. 1/
17

18 1/ Mr. Hills is the Chairman of the Commission. Messrs. Loomis, Evans and
19 Pollack are Commissioners. Mr. Sporkin is the Director of the Division
20 of Enforcement of the Commission. Mr. Borowski is the Associate Director
21 of the Division of Enforcement. Mr. Mann is a special counsel assigned
22 to the Division of Enforcement. Mr. Erickson is the Assistant Adminis-
23 trator, Enforcement Division, Los Angeles Regional Office.

24 For convenience, the defendants Securities and Exchange Commission,
25 its chairman and Commissioners will be referred to as "the Commission."
26 Defendants Sporkin, Borowski, Mann and Erickson will generally be
27 referred to as "the Commission staff."
28

(footnote continued)

1 The plaintiffs seek to attack collaterally the authority of this Court
2 (per Whelan, J.) to enter, by consent certain portions of the Second Amended
3 Judgment and Order of Permanent Injunction and Ancillary Relief ("Second Amended
4 Judgment") entered on November 26, 1974, in Securities and Exchange Commission
5 v. Mattel, Inc., Civil Action No. 74-2958-FW. 2/ Specifically, plaintiffs

6
7 1/ (Footnote continued)

8 Plaintiffs have also named as defendants The United States District Court
9 for the Central District of California, Edward H. Levi, as Attorney General
10 of the United States, and William T. Keller, as United States Attorney for
11 the Central District of California.

12 Counsel for the Commission and its staff have discussed this
13 case with counsel for the defendants, Attorney General Levi and
14 United States Attorney Keller. A motion to dismiss or for summary
15 judgment will also be made on their behalf. It is respectfully
16 suggested that this Court consider all memoranda submitted in
17 connection with both sets of motions. While we anticipate that
18 there may be some overlap with respect to certain arguments,
19 other arguments will be covered separately.

20 On January 10, 1977, this Court heard argument on the motion to
21 disqualify the entire District Court for the Central District of
22 California on the ground that the order issued by Judge Whelan in
23 Securities and Exchange Commission v. Mattel, Inc., Civil Action No.
24 74-2958-FW, which is under attack in the instant action, was an order
25 of this Court. Plaintiffs' motion was denied.

26 2/ A copy of the Second Amended Judgment is attached to Plaintiff's
27 Memorandum of Points and Authorities in Support of Motion for
28 Preliminary Injunction, as Appendix A.

1 seek, inter alia, a declaratory judgment that "that portion of the Second
2 Amended Judgment which establishes a Special Counsel and Special Auditor and
3 which confers upon such private persons unlawful powers" is invalid (Complaint
4 ¶ 2). In addition, plaintiffs request "an order striking and expunging from
5 this Court's files and records the 'Reports of Special Counsel and Special
6 Auditor' which were filed with this Court on November 3, 1975, and . . .
7 enjoining the Defendants from using in any manner the information or material
8 which they have obtained as a result of said reports and investigations
9 upon which they were based" (Id.).

10 This memorandum is submitted in support of the motion of the Commission
11 and its staff members to dismiss, or in the alternative, for summary judgment.
12

13 STATEMENT OF FACTS 3/

14 A. Introduction

15 The Securities and Exchange Commission ("Commission") is charged with
16 the responsibility for enforcing the federal securities laws. Pursuant to
17

18 3/ With respect to the alternative motion for summary judgment, the
19 Commission and its staff are not now submitting any affidavits, because
20 it is expected that a stipulated statement of facts will shortly be
21 submitted to this Court. Pursuant to this Court's direction at the
22 hearing held before it on January 10, 1977, counsel for these defendants
23 and counsel for the plaintiffs have met on a number of occasions and
24 are seeking diligently to complete preparation of a stipulated statement
25 of facts. The statement of facts set forth in this memorandum, we
26 believe, will comport with that stipulated statement. In any event,

27 (footnote continued)

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1 that authority the Commission, among other things, conducts investigations
2 into possible violations of the federal securities laws. In instances
3 where the Commission believes that the federal securities laws have been,
4 or are about to be, violated, it may bring an action to enjoin such
5 violations. In addition, it may refer the matter to the Attorney General,
6 who may, in his discretion, initiate criminal proceedings.

7 B. Initial Commission Investigation of Mattel, Inc.

8 In the Spring of 1973, the Commission undertook an informal investigation
9 of Mattel, Inc. ("Mattel"). As a result of that preliminary investigation,
10 and upon the recommendation of the Division of Enforcement, the Commission,
11 on January 22, 1974, entered a Formal Order of Private Investigation styled
12 In the Matter of Mattel, Inc. The staff was directed to focus its inquiries
13

14 3/ (footnote continued)

15 because this Court will hear the merits of this action on January 31, 1977,
16 together with argument on these motions, any deficiency in proof, if not
17 already provided prior to that date, will be supplemented at that hearing.

18 In this memorandum, we also allude to the civil injunctive proceeding,
19 Securities and Exchange Commission v. Mattel, Inc., Civil Action No. 74-
20 2958-FW. Of course, this Court may take judicial notice of all the
21 documents and proceedings in that case.

22 With respect to the motion to dismiss, these defendants respectfully
23 submit that, for the reasons set forth in this memorandum concerning the
24 adequate remedy the plaintiffs have in moving to suppress any illegal
25 evidence, should they be indicted and prosecuted, this case must be
26 dismissed, even assuming that the activities of which they complain
27 have resulted in illegal evidence, a proposition which we emphatically
28 deny. Of course, no affidavits are needed for such motions.

1 on possible violations of Sections 10(b) and 13(a) of the Securities Exchange
2 Act of 1934, 15 U.S.C. 78j(b) and 78(m)(a), and Rules 10b-5, 17 CFR 240.10b-5
3 and 13a-13, 17 CFR 240.13a-13, thereunder.

4 C. The August 1974 Judgment

5 On August 5, 1974 the Commission filed an action in the United States
6 District Court for the District of Columbia, (Securities and Exchange
7 Commission v. Mattel, Inc., Civil Action No. 74-1185), seeking injunctive
8 and ancillary relief against Mattel. The complaint alleged, among other
9 things, that Mattel issued false and misleading press releases during and
10 after its fiscal year ended February 3, 1973 and filed false and misleading
11 quarterly reports on Form 10-Q with the Commission during that fiscal year.

12 On August 5, 1974, pursuant to Mattel's consent, without admitting
13 or denying the allegations in the Commission's complaint, a Judgment
14 and Order of Permanent Injunction and Ancillary Relief ("Judgment") was
15 entered against Mattel. The Judgment enjoined Mattel from violating the
16 antifraud and reporting provisions of the Securities Exchange Act and provided
17 for certain ancillary relief, including a requirement that Mattel appoint two
18 additional directors, satisfactory to Commission and approved by the Court,
19 who had no prior affiliation with Mattel (§§III). Mattel was also required to
20 establish a Financial Controls and Audit Committee and a Litigation and Claims
21 Committee of its board of directors with specified functions and membership
22 (§§ IV and V).

23 The August 1974 Judgment was the result of extensive negotiations between
24 the Commission staff and the sole defendant, Mattel. Mattel's consent to
25 entry of the Judgment was authorized by its board of directors on July 19,
26 1974. Plaintiffs Elliot and Ruth Handler, as members of the Mattel board of
27 directors, voted in favor of the resolution authorizing that consent.

28 ///

1 In connection with the settlement of the Commission's action, all of
2 the officers and directors of Mattel, including the plaintiffs Elliot and
3 Ruth Handler (but not including plaintiff Rosenberg, who was no longer
4 on the board at that time) submitted notarized undertakings to the
5 Commission's staff, in which they acknowledged familiarity with the terms of
6 the then proposed consent Judgment and undertook and agreed that they were
7 bound thereby and would use all reasonable efforts to carry out the terms of
8 the Judgment.

9 In September 1974, representatives of Mattel voluntarily provided the
10 Commission with information obtained during the course of an investigation
11 of the company, which tended to show that Mattel's financial statements and
12 filings with the Commission for the fiscal years 1971 and 1972 also had been
13 false and misleading. This voluntary disclosure to the Commission by the
14 Mattel counsel was authorized by Mattel's board of directors, which included
15 plaintiffs Elliot and Ruth Handler.

16 D. The Amended Judgment

17 Following the voluntary disclosures and further extensive negotiations
18 with representatives of Mattel, the Commission on October 2, 1974, filed an
19 Application for Further Relief in the District Court for the District of
20 Columbia. The Application for Further Relief alleged that Mattel's filings
21 with the Commission for its 1971 and 1972 fiscal years were false and
22 misleading. The district court approved an Amended Judgment and Order of
23 Permanent Injunction and Ancillary Relief ("Amended Judgment") on October 2,
24 1974, also with Mattel's consent, without admission or denial of the allegation.
25 Mattel's consent to entry of the Amended Judgment was also authorized by its
26 board of directors, including plaintiffs Elliot and Ruth Handler who voted
27 in favor of the resolution.

28 ///

1 The Amended Judgment entered by the district court contained significant
2 ancillary relief in addition to injunctive relief. Mattel was ordered to
3 appoint and maintain on its board of directors a majority of directors who
4 had no prior affiliation with the company and who were satisfactory to the
5 Commission and approved by the Court (§ IV). Mattel was also ordered to
6 maintain an executive committee of its board, a majority of whose members
7 were to be designated from among the additional directors to be appointed (§ V).
8 The Financial Controls and Audit Committee, with voting power in the hands
9 of the additional directors, was to be given continuing review functions over
10 financial controls and accounting procedures, quarterly financial reports,
11 public disclosures, and relations with Mattel's independent auditors (§ VI).
12 The Litigation and Claims Committee, consisting of three of the additional
13 directors, was to review litigation and claims against past or present Mattel
14 personnel arising out of their relationship with Mattel and approve settlements
15 or disposition of any claims or actions Mattel may have against past or present
16 affiliated persons (§ VII). The Amended Judgment also required that Mattel
17 correct its filings with the Commission (§ XI).

18 The Amended Judgment further provided that a Special Counsel was
19 to be appointed by a majority of the additional Mattel directors and be
20 satisfactory to the Commission and approved by the Court (§ VIII). The Special
21 Counsel was to conduct a full investigation into the matters set forth in
22 the Commission's application and the report of a Special Auditor he was to
23 retain, pursuant to Paragraph IX, and such other matters as he deemed appropriate;
24 file a report of his findings and recommendations with the Court; and, upon
25 the approval of the additional directors, take action including institution
26 and prosecution of suits and further actions necessary or appropriate for
27 the protection of Mattel's shareholders; in the event of any disagreements
28 between the Special Counsel and the additional directors concerning actions to

1 be taken by Special Counsel, he could apply to the Court for orders resolving
2 the disputes (Id.). Mattel was not to settle or abandon any material claims
3 as a result of the violations alleged by the Commission or found by the
4 Special Counsel except on notice and explanation to the Commission (Id.).

5 The Amended Judgment also provided for confidential treatment of the
6 required reports (§ VIII) as follows:

7 "(6) where appropriate in his judgment, upon notice to the Commission
8 and to Mattel, [Special Counsel may] apply to the Court for appropriate
9 orders that any part of his report and/or any part of the Special
10 Auditor's report be accorded confidential treatment."

11 The Amended Judgment (§ XII) provided in part that : ". . . Mattel,
12 its officers, directors, agents, and controlling persons shall cooperate fully
13 with the aforesaid Committees and Special Counsel and Special Auditor and
14 render such reports and other assistance and meet with said Committees and
15 Special Counsel and Special Auditor as said Committess and Special Counsel
16 and Special Auditor shall reasonably require." (This provision was not
17 applicable to plaintiff Seymour Rosenberg, who was not, at the time the order
18 was entered, an officer, director or a controlling person of Mattel.)

19 By order dated October 2, 1974, District Judge Gesell transferred
20 the Mattel action from the District of Columbia to the United States
21 District Court for the Central District of California.

22 E. The Second Amended Judgment

23 On November 26, 1974, after several hearings and submissions
24 by both parties to this Court, Judge Francis C. Whelan entered the Second
25 Amended Judgment. This Judgment modified the Amended Judgment in one
26 significant respect. Because of the concerns expressed by Judge Whelan,
27 the Court removed itself from evaluating the credentials and qualifications
28 of the additional directors.

1 Pursuant to the Second Amended Judgment the required additional directors
2 were appointed by Mattel. The additional directors appointed have been out-
3 standing leaders in the fields of business, law and education. Most of the
4 persons chosen were suggested by Mattel, its previously appointed additional
5 directors, or by an outside personnel placement firm engaged by Mattel and
6 were not personally known to the Commission staff concerned with the investigation
7 or review of their appointment. Seth Hufstedler, Esquire, of the Los Angeles
8 firm of Beardsley, Hufstedler & Kimble, a former President of the California
9 Bar Association, was appointed as Special Counsel. Price, Waterhouse & Co.,
10 an internationally known firm of certified public accountants, was retained
11 by special counsel as special Auditor. The additional directors, Special
12 Counsel and Special Auditor were found satisfactory by the Commission and
13 approved by this Court.

14 F. Reports of Special Counsel and Special Auditor

15 The Special Counsel and Special Auditor conducted the investigation ordered
16 by the Second Amended Judgment (§ VIII). During or in advance of interviews
17 which they conducted, Special Counsel advised witnesses of their rights, including
18 their right to counsel and to refuse to answer questions, and that their appear-
19 ances were voluntary. The plaintiffs, Elliot and Ruth Handler and Seymour
20 Rosenberg, were interviewed by the Special Counsel during his investigation.
21 They were advised of their rights and were accompanied by counsel of their
22 choosing, who was permitted to participate in the interviews.

23 The Reports of Special Counsel and Special Auditor were filed with
24 this Court on November 3, 1975, and made public contemporaneously. The Special
25 Counsel determined not to identify particular individuals with specific acts
26 or practices discussed in the reports. Accordingly, individuals generally are
27 referred to by categories of positions (e.g., senior management executives,
28 accounting management, etc.) rather than by name. The plaintiffs, however,

1 are identified by name in the beginning of the report (p.11) where Special Counsel
2 states that he has recommended that the Company take whatever steps may be
3 necessary to pursue claims against them. Although plaintiffs are identified
4 elsewhere in the reports by name, specific wrongful actions are not attributed
5 to them.

6 Contemporaneously with the filing of the reports, Mattel issued a press
7 release describing, among other things, the findings of Special Counsel and
8 Special Auditor. A copy of the Reports of Special Counsel and Special Auditor
9 was subsequently filed by Mattel with the Commission as an attachment to a
10 Current Report on Form 8-K, which has been available for public inspection.

11 G. Activities Subsequent to Filing of the Reports

12 The Commission staff has discussed the content of the reports with
13 representatives of the special counsel and with special auditor both before
14 and after filing of the reports. Following the filing of the reports with
15 the Court and their being made public, the Commission staff made a copy of the
16 reports available to the Office of the United States Attorney for the
17 Central District of California. Pursuant to Commission authorization,
18 the Commission's nonpublic investigative files, including copies of investi-
19 gative material received from the Special Counsel, have been referred to
20 the Office of the United States Attorney for possible criminal prosecution.
21 In making such references, the discretion whether to institute prosecution is
22 vested by statute with the Attorney General, not in the Commission. See,
23 e.g., Section 21(d) of the Securities Exchange Act, 15 U.S.C. 78u(d).
24 staff has been, and is, as is customary in cases of this nature, assisting
25 that Office in evaluating the material and preparing its case for grand jury
26 consideration.

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1 prosecution in which it might be alleged that they violated the federal
2 securities laws. To this end, they seek to suppress evidence in two judicial
3 forums--a grand jury investigation and a possible subsequent criminal trial,
4 should an indictment be returned. This Court cannot aid them in their goal.

5 The Supreme Court has noted that ". . .neither the Fifth Amendment
6 nor any other constitutional provision prescribes the kind of evidence
7 upon which grand juries must act." Costello v. United States, 350 U.S.
8 359, 362 (1956). Rather, the function of the grand jury is to insure
9 "fair and effective law enforcement" and to this end its responsibilities
10 include "both the determination whether there is probable cause to believe
11 a crime has been committed and the protection of citizens against unfounded
12 criminal prosecutions." United States v. Calandra, 414 U. S. 338, 343 (1974).
13 To effectuate this dual edged mandate, the investigatory powers of the grand
14 jury traditionally have been accorded wide latitude. Branzburg v. Hayes,
15 408 U. S. 665, 700 (1972); Costello v. United States, supra, 350 U.S. at 364.

16 Plaintiffs cannot prevent the presentation of the Reports of the Special
17 Counsel and Special Auditor to the grand jury for to do so would interfere
18 with its legally recognized investigatory function. For example, it has been
19 held that a taxpayer, who sought, before indictment, to enjoin the presentation
20 to a grand jury of evidence allegedly illegally obtained by the Internal Revenue
21 Service in violation of that taxpayer's constitutional right against self-
22 incrimination, was not entitled to injunctive relief where he had an adequate
23 remedy at law--e.g., by seeking to suppress that evidence by appropriate motions
24 and objections when, and if, he was brought to trial. Chakejian v. Trout,

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1 295 F. Supp 97, 102 (E.D. Pa., 1969). 4/ This holding is the logical extension
2 of the various holdings of the Supreme Court that a grand jury (1) may ask
3 questions based on evidence seized in violation of the Fourth Amendment,
4 United States v. Calandra, supra, 414 U.S. at 349-52; (2) may consider
5 evidence obtained in violation of the Fifth Amendment, United States v. Blue,
6 384 U.S. 251, 255 (1966); and (3) may rely upon hearsay or otherwise incompetent
7 evidence Costello v. United States, supra, 350 U.S. at 368. Moreover, the
8 Supreme Court has held that a court will not conduct a preliminary hearing
9 to determine the source of the evidence on which the grand jury interrogation
10 is based. Lawn v. United States, 355 U.S. 339, 350 (1958). 5/ And, in denying
11 the equitable remedy to the plaintiff in Chakejian, the district court (295
12 F. Supp. at 103) noted, and gave credence to the concerns of the Supreme Court
13 expressed in United States v. Blue, that premature intervention in criminal
14 prosecution would "increase to an intolerable degree interference with the
15

16 4/ The Supreme Court, in a case subsequent to Chakejian, had occasion to dis-
17 cuss the appropriateness of a pre-indictment motion to suppress evidence
18 from grand jury scrutiny. Noting that the respondent in the action before
19 the Court had not been indicted by the grand jury and was not a criminal
20 defendant, the Court opined that "[u]nder traditional principles, he has
21 no standing to invoke the exclusionary rule." United States v. Calandra,
22 supra, 414 U.S. at 352 note 5.

23 5/ These cases have been followed in the Ninth Circuit. See United States
24 v. Rafferty, 534 F. 2d 854 (C.A. 9, 1976); Hunter v. United States, 405
25 F.2d 1187, 1188 (C.A. 9, 1969).

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1 public interest in having the guilty brought to book." 384 U.S. at 255. 6/
2 This court can do no less.

3
4 6/ The full text of the Supreme Court's statement in Blue is:

5 "Even if we assume that the Government did acquire
6 incriminating evidence in violation of the Fifth
7 Amendment, Blue would at most be entitled to suppress
8 the evidence and its fruits if they were sought to be
9 used against him at trial. * * * Our numerous
10 precedents ordering the exclusion of such illegally
11 obtained evidence assume implicitly that the remedy
12 does not extend to barring the prosecution altogether.
13 So drastic a step might advance marginally some
14 of the ends served by exclusionary rules, but it
15 would also increase to an intolerable degree inter-
16 ference with the public interest in having the guilty
17 brought to book." (Emphasis added.)

18 Consequently, even if some of the evidence amassed against the plaintiffs
19 in the instant action as a result of the investigations undertaken by the
20 Special Counsel and Special Auditor had been illegally obtained, plaintiffs
21 are, as the Supreme Court held in Blue, "at most, entitled to suppress
22 the evidence and its fruits if they are sought to be used against [them]
23 at trial." Id.

24 In conformity with this principle, the Court of Appeals for the Second
25 Circuit has held that the denial of a corporation's motion to limit the
26 conduct of a grand jury investigation of possible perjury of the
27 corporation's officials in a prior grand jury's investigation of the

28 (footnote continued)

1 B. This Action Is Essentially A Motion To Suppress Evidence
2 In A Possible Future Criminal Case. It Is Premature And Should
3 Be Dismissed.

4 As our previous discussion shows, the federal courts have a strong policy
5 of avoiding interference in the prosecution of criminal matters until that
6 stage of the litigation when the rights of the accused become fixed. Even
7 in situations in which it has been alleged that basic civil rights were unlawfully
8 compromised or subverted as a result of an abuse of process, absent a showing
9 of bad faith and harassment, the courts have declined to intervene. Kugler v.
10 Helfant, 421 U.S 117 (1975); Younger v. Harris, 401 U.S. 37 (1971). This policy
11 of restraint is founded on "the basic doctrine of equity jurisprudence that
12 courts of equity should not act, and particularly should not act to restrain
13 a criminal prosecution, when the moving party has an adequate remedy at law
14 and will not suffer irreparable injury if denied equitable relief." Younger v.
15 Harris, supra, 401 U.S. at 43-44. Plaintiffs fail to address this point in
16 their memorandum of points and authorities in support of their claim for relief,
17 which was filed in this Court on January 7, 1977.

18 _____
19 6/ (footnote continued)

20 corporation's alleged violation of antitrust laws would not prevent the
21 corporation from asserting in the criminal trial arising out of the prior
22 investigation, if occasion should arise, that the evidence proffered
23 against the corporation had been improperly obtained. In Re Grand Jury
24 Investigation of Violations, of 18 U.S.C. §1621 (perjury) 318 F.2d 533
25 (C.A. 2, 1963).

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1 Plaintiffs' attempt to create a justiciable controversy in this case and
2 their attempt to show extreme circumstances which is based solely on
3 their mere conjecture and speculation as to the ultimate disposition of a
4 possible criminal case against them. In Hill v. United States, 346 F. 2d
5 175 (C.A. 9, 1965), a case directly analogous to the one at bar, a taxpayer
6 filed a motion to have returned and suppressed records which were allegedly
7 in the hands of the Internal Revenue Service pursuant to a consensual agreement
8 whereby the IRS was permitted to make copies of such records. The district
9 court for the Southern District of California denied the taxpayer any relief
10 and he appealed. The Court of Appeals held:

11 "Since this attempt to suppress evidence has developed before
12 any action has even been commenced, and, for that matter, has
13 developed where an action may never even be commenced, we find
14 this motion is nothing more than a premature request. If criminal
15 prosecution does subsequently take place, appellant can raise a
16 motion to suppress any evidence which the government may have
17 secured in violation of his constitutional rights." Id at 178.

18 Hence, the plaintiffs are improperly before this court, and the issues
19 they raise, if valid at all, are premature. As the Court of Appeals for this
20 Circuit has stated:

21 "Since it is impossible to predict what future use may be
22 made of this evidence, an injunction against all use at this
23 time is premature and improper." Midwest Growers Cooperative
24 Corp. v. Kirkemo, 533 F.2d 455, 466 (1976).

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1 The plaintiffs' fully adequate remedy at law, as we have shown, rests
2 with the criminal court judge, before whom, during or prior to trial,
3 they may seek to suppress any and all evidence unlawfully obtained to
4 protect their constitutional rights and vindicate their professional
5 reputations. These rights are no less than those afforded all citizens who
6 are the subjects of criminal prosecutions.

7 The plaintiffs in this action must follow the same procedure.

8 C. Because There Is No Criminal Case Pending, Plaintiffs' Complaint
9 Essentially Seeks An Advisory Opinion From This Court, Which This
10 Court Cannot Give.

11 The essence of plaintiffs' prayer for relief is that the ancillary remedy
12 fashioned by the court in an independent civil action be found unlawful in
13 advance of the happening of any event which may have an impact on them. Yet,
14 in the absence of a criminal enforcement proceeding, this request seeks only
15 an advisory opinion which plaintiffs would then require have binding effect
16 on a court of criminal law in the future. It is well settled that the federal
17 courts are prohibited from rendering advisory opinions by the case or controversy
18 requirement of Article III of the constitution. Notwithstanding the plaintiffs
19 contention that they are seeking a declaratory judgment of an actual case
20 or controversy pursuant to federal law, 28 U.S.C. §2201 (Complaint ¶¶ 2, 3).

21 "[T]his Court is without power to give advisory opinions. It has
22 long been its considered practice not to decide abstract, hypo-
23 thetical or contingent questions, or to decide any constitutional
24 question in advance of the necessity for its decision, or to
25 formulate a rule of constitutional law broader than is required
26 by the precise facts to which it is to be applied, or to decide
27 any constitutional question except with reference to the particular
28 facts to which it is to be applied. * * *" (Emphasis supplied.)

1 Alabama State Federation of Labor v. McAdory, 325 U. S. 450, 461 (1945)
2 (citations omitted).

3 The infirmity in an action such as this is that it has been brought
4 too soon: "ripeness is peculiarly a question of timing." Regional Rail
5 Reorganization Act Cases, 419 U. S. 102, 140 (1974). Essentially an
6 issue is not ripe if its judicial resolution would evoke an advisory opinion.

7 Where, as here, plaintiffs have not yet been criminally charged, and,
8 in any event, they will have ample opportunity to raise their constitutional
9 objections to the manner in which evidence sought to be introduced at trial
10 was obtained, as well as to the admissability of the evidence itself, this
11 action must await further crystallization before judicial determination.

12 United States v. Blue, supra, 384 U.S. at 255; Hunter v. United States
13 405 F.2d 1187, 1188 (C.A. 9, 1969). Those objections will not be lost in
14 the interim, but will be preserved to be raised at an appropriate time
15 and will thus become, if at all valid, all the more apparent. 7/
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17 7/ In support of their motion for a preliminary injunction, plaintiffs
18 argue that "if an injunction is not granted, plaintiffs will lose their
19 only meaningful opportunity to challenge the legality of the investigative
20 procedure here employed, and the deterrent purpose of the exclusionary
21 rule will have been wholly frustrated. By the time of an indictment and
22 subsequent trial, if a trial is ultimately held, the information obtained
23 by the Special Counsel and Special Auditor will have become inextricably
24 intertwined with the evidence developed by the Government." Plaintiffs
25 Memorandum of Points and Authorities in Support of Motion for Preliminary
26 Injunction, p. 59. (Emphasis added).

27 Plaintiffs thus concede that resolution of this controversy is not immediately

28 (footnote continued)

1 D. The Additional Broad Relief Which The Plaintiffs Seek Is Not
2 Within The Power Of This, Or Any Court, To Render.

3 Plaintiffs also seek a ubiquitous form of relief which is not
4 within the power of any court to deliver -- that is, they request the court
5 to somehow turn back the clock to the moment before the filing of the Reports
6 of the Special Counsel and Special Auditor in Securities and Exchange
7 Commission v. Mattel, Inc., on November 3, 1975, and thereby eradicate in all
8 respects the purported harms visited upon them as the result of the
9 investigation which they now allege was unlawful. Such a remedy is, of
10 course, impossible. This Court cannot "expunge" the memories or collective
11 knowledge which currently exists with regard to the information which was
12 contained in reports that have been publicly disseminated. Nor can the
13 Court restore the professional reputations of these plaintiffs, as they
14 appear to ask, by mere edict. Such vindication, if there is any to be had,
15 could come only as a result of a public airing of the charges and defenses
16 thereto, a confrontation which the plaintiffs, by instituting this lawsuit,
17 are consciously attempting to avoid.

18
19 7/ (Footnote continued)

20 imperative since there may never be a criminal trial. Moreover, even
21 if the plaintiffs were to be criminally tried, the prosecution would
22 have the burden of establishing affirmatively that the evidence proposed
23 to be used was not tainted by demonstrating that it was derived from a
24 legitimate source wholly independent of any inadmissible evidence. Cf.,
25 Kastigar v. United States, 406 U.S. 441, 460 (1972).

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1 II. A COURT OF EQUITY SHOULD GRANT NO RELIEF TO THE PLAINTIFFS,
2 FOR THEY COME BEFORE IT WITH UNCLEAN HANDS, ARE ESTOPPED
3 AND ARE GUILTY OF LACHES. MOREOVER, THEY SEEK TO ATTACK
4 COLLATERALLY A FINAL JUDGMENT ENTERED IN ANOTHER ACTION
5 WHICH THEY MAY NOT DO.

6 For an understanding of the plaintiffs claims' it is useful to place
7 in proper perspective the nature of the proceeding in which the Second Amended
8 Judgment and Order, now under attack, was entered with the consent of Mattel.
9 As we have noted, the Commission sued Mattel following an investigation conducted
10 by its staff, in which it alleged, inter alia, that Mattel had issued false
11 and misleading reports and press releases. Mattel consented to the entry of
12 a permanent injunction from future violations of the anti-fraud and reporting
13 provisions of the Securities Exchange Act, without admitting or denying the
14 allegations in the Commission's Complaint (Securities and Exchange Commission
15 v. Mattel, Inc., D.D.C., Civil Action No. 74-1185).

16 At all times relevant to this investigation, the filing of the civil suit
17 against Mattel, the request for further relief, and the amended judgments by
18 consent, defendants Elliot and Ruth Handler were members of the Mattel board of
19 directors. As such, they voted in favor of board resolutions, pursuant to which
20 Mattel consented to the entry of the judgments and orders which they now seek to
21 attack. Plaintiff Rosenberg, at this same time, although no longer a member of
22 Mattel's board of directors, was aware of the civil action brought by the
23 Commission and, if not aware of the terms of the Amended Judgment and Order
24 when entered, became aware of them shortly after their entry.

25 At no time prior to the institution of this action did any of the plaintiffs
26 move to intervene in the Commission action in order to protect the rights which
27 they now contend have been transgressed, nor did they file any motion to prevent
28 or modify the Second Amended Judgment or the ultimate publication of the reports

1 of the Special Counsel and the Special Auditor. Now, more than two years after
2 the entry of the Second Amended Judgment and more than one year after the
3 publication of those reports, plaintiffs ask this Court to invoke its equity
4 powers.

5 A. Plaintiffs May Not Attack Collaterally a Final Order Entered
6 In Another Action.

7 Plaintiffs have devoted a considerable portion of their moving papers
8 to the question of the authority and propriety of the duly appointed Special
9 Counsel and Special Auditor in Securities and Exchange Commission v. Mattel,
10 Inc., to conduct an investigation of the corporate affairs of Mattel. That
11 such a collateral attack cannot be made is well-settled. A consent decree
12 has "the same force and effect as any other judgment, and is a final adjudica-
13 tion of the merits." Securities and Exchange Commission v. Thermodynamics,
14 Inc., 319 F. Supp. 1380, 1382 (D.C. Colo., 1970), affirmed, 464 F.2d 457
15 (C.A. 10, 1972), certiorari denied, sub nom. Strawn v. Securities and Exchange
16 Commission, 410 U.S. 927 (1973). Approval of the terms of a consent order is
17 a "judicial act", Pope v. United States, 323 U.S. 1,12 (1944), which "involves
18 the determination by the chancellor that it is equitable and in the public
19 interest." United States v. Radio Corporation of America, 46 F. Supp 654,
20 655 (D.Del, 1974).

21 Plaintiffs' lawsuit is simply an attempt to attack collaterally the terms
22 of the consent decree and, as such, cannot be considered by this Court. Black
23 and White Children of the Pontiac School System v. School District of Pontiac,
24 474 F.2d 1030 (C.A. 6, 1972); McAleer v. American Telephone and Telegraph Company,
25 416 F.Supp 435, 438 (D.D.C., 1976); Securities and Exchange Commission v.
26 Thermodynamics, Inc., supra, 319 F. Supp. at 1382.

27 McAleer v. American Telephone and Telegraph Company, supra, is particularly
28 relevant to the instant action. In that case an action was brought by an

1 employee and a union alleging that the employee had been denied promotion in
2 favor of a less qualified and less senior employee solely because of her sex.
3 On motions for summary judgment, the district court (Gesell, J.) held that
4 the consent judgment entered in a suit by the Equal Employment Opportunity
5 Commission and pursuant to which American Telephone and Telegraph Company
6 (the employer) agreed to establish an affirmative action program to improve
7 the employment situation for women and minorities, could not be collaterally
8 attacked with respect to the legality of the affirmative action plan contained
9 in the decree. Similarly, plaintiffs here are precluded from attacking, in a
10 different action, the legality of the terms of the consent order agreed to by
11 Mattel in SEC v. Mattel, supra. 8/ As the court in McAleer noted (416 F.
12 Supp. at 438): "A contrary rule would be an aspersion on the integrity of
13 the judicial process and productive of little but the mischief of possibly
14 inconsistent standards and interpretations."

15 Finally, it should be noted that, pursuant to the express terms of the
16 Second Amended Judgment, the district court in Mattel "shall retain juris-
17 isdiction of this action to implement and carry out the terms of its decree and
18 of all additional decrees or orders appropriate in the public interest as
19 for the protection of investors" Second Amended Judgment and Order of
20 Permanent Injunction and Ancillary Relief, ¶ XV. (emphasis supplied). In such
21 situations where the district court retains jurisdiction, the reviewing courts
22 have found that the proper avenue for relief, if there were unanticipated
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24 8/ To the extent that plaintiffs are seeking to vindicate claims which
25 may rightfully belong to Mattel (e.g., attorney-client privilege), it
26 is well-settled that a litigant "has standing to seek redress for
27 injuries done to him, but may not seek redress for injuries done to
28 others." Moose Lodge No. 107 v. Irvis, 407 U.S. 163, 166 (1972).

1 problems which had developed in carrying out the order, is an application to
2 intervene and a motion for additional relief in the principal case. Black
3 and White Children of the Pontiac School System v. School District of Pontiac,
4 supra, 474 F.2d at 1030; McAleer v. American Telephone and Telegraph Company,
5 supra, 416 F. Supp. at 438.

6 Simply put, plaintiffs are in the wrong court.

7 B. Plaintiffs have been dilatory and a court of equity should not
8 countenance this lack of diligence.

9 As we have previously noted, there has been a long and unexplained lapse
10 of time between the entry of the Second Amended Judgment and the reports being
11 attacked, on the one hand, and the filing of the instant action, on the other.
12 At all times, plaintiffs have been on notice of the various consequences that
13 might befall them as a result of the investigation conducted on Mattel's behalf
14 by the Special Counsel. Yet, for reasons unknown to the Commission or stated
15 to the Court, plaintiffs did not seek to establish or to vindicate rights
16 allegedly denied them. Presumably, they elected to straddle -- to sit on
17 the fence and wait and see what would happen.

18 The plaintiffs are before this court in order that they may invoke its
19 equitable powers of injunctive and ancillary relief. However, "the strongest
20 right of equity may be abandoned by conduct and no relief can be granted
21 in the face of unreasonable delay." Greely and Loveland Irrigation Company v.
22 McCloughan, 342 P.2d 1045, 1050 (Colo., 1959). Laches is a form of equitable
23 estoppel. It is a defense in situations where there "is a neglect or failure
24 on the part of a party in the assertion of a right, continuing for an unreason-
25 able and unexplained length of time, under circumstances permitting diligence,
26 resulting in a disadvantage to the other party." Rank v. United States 142
27 F. Supp. 1, 123 (S.D. Cal. 1956).

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1 In the present action, plaintiffs' conduct speaks for itself. They delayed
2 bringing their claims to the attention of any court for more than one year
3 after the filing of the reports, which is alleged to have caused them harm.
4 They never sought, as we have noted, to intervene in the Commission suit,
5 of which they were aware. At no time did plaintiffs seek to assert their
6 Fifth Amendment rights despite the fact that they were informed of their
7 rights by the Special Counsel and were accompanied by and represented by
8 counsel during the course of their investigatory interviews. Despite the
9 fact that they received a copy of the reports of the Special Counsel and
10 Special Auditor shortly before its introduction into the Court's records as
11 a public document, they made no effort to move to seal the report in order
12 that its impact might be minimized or to preserve their rights; nor, after
13 more than one year from the date of its initial dissemination, have they
14 undertaken any action to correct any of the allegedly incorrect or improper
15 items in the report. It is evident that plaintiffs have instituted this
16 lawsuit solely to deter or defeat the prosecution of a criminal action of
17 which they may become the subjects. Accordingly, granting their prayer for
18 relief would be inequitable.

19 We do not contend that even the most flagrant inequitable conduct may
20 work to deprive a person of basic constitutional rights. But plaintiffs
21 are not being deprived of such rights. As we have shown in Point I, supra,
22 their rights will be protected by the criminal court judge if, ever, they
23 should be indicted. And, as we show infra, there have been no violations
24 of law or due process.

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1 III. THE APPOINTMENT OF A SPECIAL COUNSEL, PURSUANT TO THE SECOND
2 AMENDED JUDGMENT IN SECURITIES AND EXCHANGE COMMISSION V. MATTEL,
3 INC., WAS ENTIRELY PROPER AND IN KEEPING WITH THE MODERN EQUITY
4 PRACTICE OF ACCORDING COMPLETE RELIEF IN A FASHION CAREFULLY
5 TAILORED TO PROTECT PUBLIC INVESTORS FROM A RECURRENCE OF THE
6 VIOLATIVE CONDUCT AND TO PROVIDE REMEDIAL RELIEF FROM SUCH CONDUCT.

7 In recent years the Commission has been successful in obtaining orders
8 of ancillary relief to accompany the traditional statutory injunctions against
9 future violations of the federal securities laws. Such ancillary relief has
10 included the appointment of receivers or special counsel and disgorgement of
11 illicit gains. The Commission's ability to obtain such ancillary relief in
12 actions to enjoin violations of federal securities laws is not expressly
13 conferred by statute but rather is rooted in the inherent equity powers of
14 the federal courts, and, as we show below, has been repeatedly upheld. Thus,
15 the authority to obtain such relief, and the power to grant it, are implicit
16 in the provisions which authorize the Commission to institute action in the
17 federal courts to restrain violations of the various acts which it administers.
18 For example, Section 21(d) of the Securities Exchange Act authorizes the
19 Commission to seek injunction relief for violations of that Act, and Section
20 27 of that Act, 15 U.S.C. 78aa, confers jurisdiction on the federal district
21 courts in suits "in equity or actions at law brought to enforce any liability
22 or duty created under this chapter."

23 It has been held repeatedly that such provisions authorize the Commission
24 to seek, and the federal courts to exercise, the full range of equitable relief
25 necessary to effectuate the remedial purposes of the federal securities laws.
26 See, e.g., Securities and Exchange Commission v. United Financial Group, 474
27 F.2d 354 (C.A. 9, 1973); Securities and Exchange Commission v. Manor Nursing
28 Centers, Inc., 458 F.2d 1082, 1103-1104 (C.A. 2, 1972); Securities and Exchange

1 Commission v. Texas Gulf Sulphur Co., 446 F.2d 1301, 1307 (C.A. 2), certiorari
2 denied, 404 U.S. 1005 (1971); Lakenau v. Coggeshall and Hicks, 350 F.2d 61,63
3 (C.A. 2, 1965); Los Angeles Trust Deed and Mortgage Exchange v. Securities and
4 Exchange Commission, 285 F.2d 162, 181-182 (C.A. 9, 1960), certiorari denied,
5 366 U.S. 919 (1961).

6 Once the equity jurisdiction of the federal courts has been properly
7 invoked by a showing of a securities law violation, the courts possess the
8 broad equitable powers "to formulate new and effective remedies where neces-
9 sary to effectuate the purposes of the acts." Farrand, Ancillary Remedies
10 in SEC Civil Enforcement Suits, 89 Harv. L. Rev. 1779, 1784 (1976). In
11 this regard, the Supreme Court has stated, with respect to the federal secu-
12 rities laws, that "[i]t is for the federal courts to adjust their remedies so
13 as to grant the necessary relief when federally secured rights are involved."
14 J. I. Case Co. v. Borak, 377 U.S. 426, 433 (1964). That Court has also
15 observed that it "cannot fairly infer from the Securities Exchange Act of 1934
16 a purpose to circumscribe the courts power to grant appropriate remedies."
17 Mills v. Electric Auto-Lite Co., 396 U.S. 375, 391 (1970). Moreover, in
18 Porter v. Warner Holding Co., 328 U.S. 395, 398 (1945), the Court noted that
19 in those instances in which a public interest is involved, the equitable
20 powers of the district courts assume a broader and more flexible character than
21 when only a private controversy is at stake. District courts are thus possessed
22 of the power "to do equity and to mould each decree to the necessities of the
23 particular case." Hecht Co. v. Bowles, 321 U.S. 321, 329 (1944). Indeed, it
24 has been noted that the increasing scope of equitable relief is "[o]ne of
25 the most striking procedural developments of this century" and that while
26 "[i]t is perhaps too soon to reverse the traditional maxim to read that money
27 damages will be awarded only when no suitable form of specific relief can be
28 devised . . . the old sense of equitable remedies as 'extraordinay' has faded."

1 Chayes, The Role of the Judge in Public Law Litigation, 89 Harv. L. Rev.
2 1281, 1292 (1976).

3 It has become clear that "governmental regulating agencies are not, by
4 virtue of their status, disabled from seeking ancillary remedies in their
5 civil enforcement actions." Farrand, Ancillary Remedies in SEC Civil
6 Enforcement Suits, supra, 89 Harv. L. Rev. at 1784. Accordingly, in connection
7 with its actions to enforce the federal securities laws, the Commission, when
8 it believed it appropriate, has requested ancillary relief in addition to
9 traditional administrative or injunctive remedies. The Commission has sought
10 additional relief in cases where it believed it to be in the interest of public
11 investors to obtain relief beyond that contained in a traditional order. An
12 attempt is made to specifically tailor the form of the request for ancillary
13 relief to the type of conduct that gave rise to the violative activities
14 alleged in the complaint or order for administrative proceedings. Accordingly,
15 the types of ancillary relief sought can be as varied as the types of
16 violative activities giving rise to the request.

17 Where courts have found that certain persons have profited from trading
18 in securities while in possession of information not otherwise publicly
19 available, courts have provided for disgorgement of such profits. See e.g.,
20 Securities and Exchange Commission v. Texas Gulf Sulphur, 446 F.2d 1301
21 (C.A. 2), certiorari denied, 404 U.S. 1005 (1971); Kaiser Resources, Ltd.,
22 (N.D. Cal.), Litigation Release No. 5604 (Nov. 2, 1972); Harvey Stores, Inc.,
23 (S.D.N.Y.), Litigation Release No. 5318 (Feb. 14, 1972); Securities and
24 Exchange Commission v. Allegheny Beverage Corporation, (D.D.C.), Litigation
25 Release No. 6670 (Jan. 8, 1975), 6 SEC Docket 68; Securities and Exchange
26 Commission v. J. Hugh Liedtke, et al., (S.D.N.Y.), Litigation Release No.
27 6414 (July 1, 1974), 4 SEC Docket 544; Securities and Exchange Commission
28 v. OSEC Petroleum, S.A. (D.D.C.), Litigation Release No. 6646 (Dec. 19, 1974),

1 5 SEC Docket 765; Securities and Exchange Commission v. Drew National
2 Corporation, et al., (D.D.C.), Litigation Release No. 6995 (July 18, 1975)
3 6 SEC Docket 449.

4 Where a broker-dealer is alleged to have revealed inside information
5 to favored customers, there have been undertakings to adopt, implement
6 and insure compliance with revised procedures to provide for more effective
7 protection against disclosure of confidential information. See, e.g.,
8 Campbell Advisers, Inc., Investment Advisers Act Release No. 445 (March
9 12, 1975), 6 SEC Docket 461; Merril Lynch, Pierce, Fenner & Smith, Inc.,
10 Securities Exchange Act Release No. 8459 (Nov. 25, 1968); Securities
11 and Exchange Commission v. Stirling Homex Corporation, et al. (D.D.C.),
12 Litigation Release No. 6960 (July 2, 1975), 7 SEC Docket 370.

13 Where questions have been raised with respect to the adequacy and
14 accuracy of information contained in registration statements or periodic
15 reports filed with the Commission, provisions have been made for rescission
16 and disqualification of management. See, e.g., Securities and Exchange
17 Commission v. American Agronomics Corporation (N.D. Ohio), Litigation Release
18 No. 5667 (Dec. 11, 1972), 1 SEC Docket 1; Securities and Exchange Commission
19 v. Minnesota Mining and Manufacturing Company (D. Minn.), Litigation Release
20 No. 6711 (Jan. 31, 1975) 6 SEC Docket 242; Securities and Exchange Commission
21 v. Vesco, et al. (S.D.N.Y.), Securities Exchange Act Release No. 9887 (Nov.
22 27, 1972); Securities and Exchange Commission v. Professional Services
23 Association, Inc. (W.D. Mo.), Litigation Release No. 6347 (May 1, 1974), 4
24 SEC Docket 257.

25 Where a broker-dealer or other financial institution is alleged to
26 have violated the registration provisions of the Securities Act of
27 1933 in connection with the sale of securities, provision have been made
28 for an undertaking to institute certain policies and procedures involving

1 securing specified information before quoting or selling securities, and
2 restrictions have been placed on the securities in which the firm may make
3 a market or solicit retail customers to buy or sell. See, e.g., Southern
4 California First National Bank of San Diego, Securities Exchange Act Release
5 No. 9289 (Aug. 16, 1971); Securities and Exchange Commission v. Goldman,
6 Sachs & Company, (S.D.N.Y.), Litigation Release No. 6349 (May 2, 1974), 4
7 SEC Docket 258; Securities and Exchange Commission v. Paragon Securities Company,
8 et al., (D. N.J.), Litigation Release No. 6539 (Oct. 9, 1974), 5 SEC Docket
9 265.

10 Where insiders have been charged with violations of the anti-fraud
11 provisions of the federal securities laws, restitution has been ordered,
12 a ban has been placed on selling their personally-held securities in
13 the company for a period of time, special reporting requirements have
14 been imposed, and the board of directors and executive committees have been
15 required to be counselled by qualified independent attorneys until the
16 Commission has been satisfied that such counselling is no longer necessary.
17 See, e.g., Securities and Exchange Commission v. William Herbert Hunt,
18 et al., (D.D.C.), Litigation Release No. 6633 (Dec. 11, 1974), 5 SEC
19 Docket 722; Securities and Exchange Commission v. General Refractories Company,
20 (D.D.C.), Litigation Release No. 7098 (Sept. 24, 1975), 7 SEC Docket 960.

21 Where officers, directors, underwriters or investment advisers of invest-
22 ment funds have been charged with gross abuse of trust and gross misconduct,
23 provisions have been made for restitution, rescission of certain transactions,
24 reorganization of securities-handling arrangements for custodial accounts
25 or removal of such accounts. See, e.g., Securities and Exchange Commission
26 v. Falcon Fund, Inc., (S.D.N.Y.), Litigation Release No. 6456 (July 29,
27 1974), 4 SEC Docket 680; Securities and Exchange Commission v. Everest
28 Management Corporation, et al., (S.D.N.Y.), Litigation Release No. 5613

1 (Nov. 9, 1972); Securities and Exchange Commission v. Dynavest Fund, Inc.,
2 et al. (D. N.J.), Litigation Release No. 6623 (Dec. 6, 1974), 5 SEC Docket
3 659; Securities and Exchange Commission v. The Seaboard Corporation, et al.,
4 (C.D. Cal.), Litigation Release No. 11342 (April 8, 1975), 6 SEC Docket 632;
5 Securities and Exchange Commission v. Continental Growth Fund, Inc. (S.D.
6 N.Y.), Litigation Release No. 2973 (June 23, 1964); Financial Programs, Inc.,
7 Securities Exchange Act Release No. 11312 (Mar. 24, 1975), 6 SEC Docket 503.

8 Where an orderly liquidation of a firm and the protection of investors'
9 funds and securities have been found to be necessary, a receiver has been
10 appointed. See, e.g., Securities and Exchange Commission v. Vesco, (S.D.N.Y.),
11 Securities Exchange Act Release No. 9887 (Nov. 27, 1972); Securities and
12 Exchange Commission v. R.J. Allen & Associates, Inc., et al., 386 F. Supp.
13 866, 878-879 (S.D. Fla., 1974); Securities and Exchange Commission v. Fifth
14 Avenue Coach Lines, Inc., 435 F. 2d 510 (C.A. 2, 1970); Securities and Exchange
15 Commission v. Fiscal Fund, Inc., 48 F. Supp. 712 (D. Del., 1943); Securities and
16 Exchange Commission v. United Financial Group, Inc., 474 F. 2d 354 (C.A. 9,
17 1973); Lakenau v. Coggeshall & Hicks, 350 F. 2d 61 (C.A. 2, 1965). The
18 imposition of a receivership, however, may threaten a corporation's credit
19 rating, disrupt its relations with customers or suppliers, and deprive it
20 of management continuity. As a result, the use of receivers, while sometimes
21 justified on the basis of prior violations, likelihood of continuing abuses,
22 and statutory purpose, may in fact serve to impede the recovery of the
23 defendent corporation and to impair problem confidence in the security of
24 its investments." Farrand, Ancillary Remedies in SEC and Enforcement Suits,
25 supra, 89 Harv. L. Rev. at 1790.

26 The Commission and the courts have begun to look beyond receiverships
27 for remedies more carefully tailored both to insure future compliance with
28 the federal securities laws and the needs of the particular case. Thus,

1 as is in the case at bar, several recent consent decree settlements have
2 resulted in the appointment of professionals charged with performing discrete
3 investigations, or supervisory or advisory functions within corporations that
4 have allegedly violated the federal securities laws. See, e.g. Securities
5 and Exchange Commission v. Clinton Oil, (D. Kan.), Litigation Release No.
6 5798 (March 20, 1973), 1 SEC Docket 23; Securities and Exchange Commission
7 v. Canadian Javelin, et al. (S.D.N.Y.), Litigation Release No. 6441 (July
8 18, 1974), 4 SEC Docket 620; Securities and Exchange Commission v. American
9 Agronomics Corporation, (N.D. Ohio), Litigation Release No. 5667 (December
10 1, 1972); International Controls Corporation v. Vesco, 490 F. 2d 1334 (C.A.
11 2), certiorari denied, 417 U.S. 932 (1974); Securities and Exchange Commission
12 v. The Seaboard Corporation, (C.D. Cal.), Litigation Release No. 6540 (October
13 2, 1974), 5 SEC Docket 241; Securities and Exchange Commission v. Charter
14 Diversified Service, (C.D. Cal.), Litigation Release No. 6507 (September 9,
15 1974), 5 SEC Docket 147; Securities and Exchange Commission v. Advance Growth
16 Capital Corporation, (N.D. Ill.), Litigation Release No. 6227 (January 30,
17 1974), 3 SEC Docket 493.

18 Finally, we would emphasize that, in the Mattel case, as in many of those
19 cited above, the Commission obtained a judgment which was entered with the
20 consent of the defendant. Thus, this case raises no issue of the power of
21 the court to decree, over the objection of a defendant, the equitable ancillary
22 relief given here, although we submit that such power exists.

23 IV. PLAINTIFFS MISCONCEIVE THE ROLES OF THE SPECIAL COUNSEL AND
24 SPECIAL AUDITOR IN SECURITIES AND EXCHANGE COMMISSION V. MATTEL,
25 INC., THEY ACTED AS REPRESENTATIVES OF MATTEL, AND REPRESENT
26 NO DELEGATION OF AUTHORITY OR FUNCTIONS OF THE COMMISSION.

27 Plaintiffs argue that the nature of the investigations by the Special
28 Counsel and Special Auditor were unbounded and inquisitorial and that such

1 activities were an improper delegation of the Commission's investigative
2 authority. Hence, they allege unlawful conduct by these special professionals
3 in the course of the investigations and reports undertaken pursuant to the
4 mandate of the Second Amended Judgment. However, their arguments are permeated
5 by a serious misconception of the role of the special professionals employed
6 by Mattel and approved by the Court. Plaintiffs, in the course of their
7 arguments, have lost sight of the essential nature of the settlement agree-
8 ments negotiated by the Commission and the management of Mattel (of which
9 plaintiffs Handlers were members), and which were approved by the Court.

10 The original action, from which this present complaint stems, was an
11 outgrowth of an investigation conducted by the Commission staff into possible
12 violations of the federal securities laws by Mattel. A complaint was filed
13 on August 5, 1974, and Mattel consented to the entry of a Judgment and Order
14 of Permanent Injunction and some ancillary relief. As part of the consent
15 order, Mattel agreed, among other things, to add two directors previously
16 unaffiliated with Mattel and undertake to establish certain committees charged
17 with the responsibilities of reviewing certain of the accounting and management
18 functions of the corporation. See Judgment and Order of Permanent Injunction
19 and Ancillary Relief, dated August 5, 1974.

20 As a result of the company's own investigation, evidence of more serious
21 securities law violations was brought to the attention of the board of
22 directors of Mattel. The corporation disclosed these alleged violations to
23 the Commission, and the Commission subsequently filed an application for
24 further relief. On October 2, 1974, an Amended Judgment and Order of Permanent
25 Injunction and Ancillary Relief was entered by consent which, among other
26 things, provided for the appointment of a Special Counsel satisfactory to
27 the Commission. The Special Counsel was charged with the responsibility to
28 (¶VIII):

1 "(1) conduct a full investigation into the matters set forth in
2 the APPLICATION FOR FURTHER RELIEF, the COMMISSION'S COMPLAINT
3 in this action, the report of the Special Auditor selected pursuant
4 to Part IX below, and such other matters as he shall deem appropriate;
5 (2) prepare and file with this Court and submit to the Commission
6 within sixty (60) days after the submission to the Court of
7 the Report of the Special Auditor or such further time as the
8 Court may allow a report of his findings and recommendations;
9 (3) Upon approval by the majority of the additional directors
10 pursuant to Part IV above, take all appropriate action, including
11 but not limited to the institution and prosecution of suits on
12 behalf of MATTEL against any present or former officers, directors,
13 agents, controlling persons or any other persons;
14 (4) upon approval by a majority of the additional directors pursuant
15 to Part IV above, take such further action as may be necessary
16 or appropriate for the protection of the shareholders of MATTEL:
17 (5) in his discretion, in the event of a disagreement between the
18 Special Counsel and said majority of the additional directors with
19 respect to the matters referred to in subparagraphs (3) and (4)
20 above, apply to the Court, upon notice to the Commission and to
21 Mattel, for appropriate orders resolving any such dispute; and
22 (6) where appropriate in his judgment, upon notice to the
23 Commission and to Mattel, apply to the Court for appropriate
24 orders that any part of his report and/or any part of the
25 Special Auditor's report be accorded confidential treatment."

26 It was further ordered (§ IX) that within thirty days after being
27 appointed, the Special Counsel would retain a Special Auditor. The auditor's
28 duties were as follows (§ IX) to:

1 "(1) conduct an audit to determine whether MATTEL's published
2 financial statements for the fiscal years ended January 30,
3 1971 and January 29, 1972, and for such other fiscal periods
4 as the Special Counsel or MATTEL's Board of Directors may
5 suggest, were prepared in accordance with generally accepted
6 accounting principles and fairly presented the financial
7 condition of MATTEL and what, if any, restatements or changes
8 in any financial statements of MATTEL are necessary or
9 appropriate in the light of such audit; and
10 (2) prepare and file with the Court and submit to the Commission
11 within four (4) months after his appointment, or such further
12 time as the Court may allow, a report of his findings."

13 The Amended Judgment also provided (§8) that (1) the Special Counsel and
14 the Special Auditor should be compensated for their expenses by Mattel as
15 allowed by the court; (2) the Special Counsel may consult with the Commission
16 and the Court and may apply to the Court for advice or direction; and (3) that
17 Special Counsel could resign or be discharged only with Court notice and
18 approval. As the record shows, the plaintiffs were cognizant of the dis-
19 position of the civil suit against Mattel and the terms of the consent decrees.

20 From the terms of the amended judgments, it is plain that, contrary
21 to plaintiff's attempts to characterize the functions of Special Counsel and
22 Special Auditor otherwise, the special professionals at all times functioned
23 independently of the Commission, and they were specifically appointed by
24 the company, Mattel, inter alia, to ferret out and recommend corrective
25 measures for those practices of Mattel that were violative of the federal

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1 securities laws. 8/ Thus, the source of their authority to act comes
2 from the company, which sought to investigate into the sources of possible
3 securities laws violations and available remedies, for the benefit of its
4 public investors.

5 As plaintiffs themselves have pointed out, Special Counsel has denied
6 any working relationship with the Commission's staff.

7 "Mr. Hufstedler; ... I don't represent the SEC in anyway nor
8 do I take any instructions from the SEC. Transcript of
9 proceedings, March 1, 1975 at 127-128." 9/

10 By the same token, the special professionals functioned essentially
11 independently of Court supervision. The District Court specifically
12 retained jurisdiction and could be consulted by the Special Counsel only
13 in instances where:

- 14 (1) a dispute arose between the special professionals and the
15 corporation (Amended Judgment ¶ VIII);
16 (2) the investigation had been completed and a report was to
17 be filed (Id.);
18 (3) there occurred noncooperation by the individuals or the
19 corporation subject to the consent decree (Id. ¶ XV); and
20 (4) the Special Counsel sought judicial advise (Id. ¶ X).

22 8/ Counsel for Mattel and counsel for the Commission have advised the
23 Court on more than one occasion that the purpose of the amended con-
24 sent judgment and order was primarily to protect Mattel's present and
25 prospective stockholders. See, e.g., Transcript of October 2, 1974,
26 hearing at 4, 15, 23-24, 30, 31.

27 9/ Plaintiff's Memorandum of Points and Authorities in Support of
28 Motion for Preliminary Injunction, p. 42, n. 11.

1 The Commission or its staff at no time directed or interfered with the
2 Special Counsel's investigation; the Commission's investigation was substan-
3 tially completed by the time of the entry of the consent order. Although
4 the Special Counsel's investigation at some times may have paralleled the
5 Commission's investigation, it was within the terms of the Second Amended
6 Judgment and independent of the Commission's investigation and was done at
7 the behest of and for the benefit of the corporation. Plaintiffs contend
8 (Memorandum, p. 44) that "...the powers purportedly delegated to the Special
9 Counsel exceeded the SEC's own powers and violated the Due Process Clause
10 of the Fifth Amendment." Once again, plaintiffs simply misunderstand the
11 facts." Special Counsel was not acting as an adjunct or administrator of
12 the Commission and was not bound by the Commission's own rules and regula-
13 tions. To the extent that plaintiffs argue that their due process rights
14 were compromised by the Special Counsel resulting in substantially inferior
15 treatment than they would receive during the course of a formal Commission
16 investigation, they are incorrect. Potential defendants in Commission
17 enforcement actions, contrary to plaintiffs' assertions, are not accorded
18 the right to confront or cross-examine other witnesses. Cf. 17 CFR 203.7(b).
19 The Commission's rules provide that potential defendants be afforded the
20 right to the advice of counsel (17 CFR 203.7(b)), and this right was honored
21 by the Special Counsel in the course of conducting his investigation.

22 The Commission possesses no power to punish for a contempt or to en-
23 force its own subpoenas and therefore must resort to the district court
24 to compel cooperation. Contrary to plaintiffs' assertion that the proviso
25 in the Second Amended Judgment that certain identified groups "shall cooperate
26 fully" was tantamount to a contempt power which was coercive in nature,
27 the Special Counsel could not, as the Commission cannot, independently compel
28 cooperation. Consequently, the Court remains as an unbaised arbitrator .

1 of these important issues irrespective of whether the Commission or the
2 Special Counsel investigate.

3 Finally, the Commission's published procedures (17 CFR 202.5) provide
4 that "(c) Persons who become involved in preliminary or formal investigations
5 may, on their own initiative, submit a written statement to the Commission
6 setting forth their interests and position in regard to the subject matter
7 of the investigation. . . ." Plaintiffs have not alleged that they sought
8 or that they were denied an opportunity to submit any statement in their
9 defense. In fact, despite allegations of potential errors in the Report of
10 the Special Counsel, plaintiffs have made no attempt to either bring them
11 to anyone's attention or to seek their correction. Indeed, neither in their
12 complaint nor in their extensive memorandum do they point to any alleged errors
13 in the Reports.

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