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BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF:
ARTHUR ANDERSEN L.L.P.
501 North 44th Street - 300
Phoenix, Arizona 85008
Respondent.

DOCKET NO. S-03386A-00-0000

RESPONDENT'S MOTION TO DISMISS

(Assigned to the Honorable Marc E. Stern)

(Oral Argument Requested)

Pursuant to Rules R14-3-101(A) and R14-3-105(K), Arizona Administrative Code, and Rules 9(b) and 12(b)(6), Arizona Rules of Civil Procedure, respondent Arthur Andersen, L.L.P., ("Arthur Andersen") hereby moves for dismissal of all claims asserted against it in the above captioned matter. This Motion is supported by the attached Memorandum of Points and Authorities.

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RESPECTFULLY SUBMITTED this 17th day of October, 2000.

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1 [Id. at ¶¶ 39, 48, 50.] Instead of performing the kind of investigation that the Division—with the
2 benefit of hindsight—claims was necessary, the Division claims that Arthur Andersen’s audits
3 were “seriously flawed” because it relied on statements from BFA’s management. [Id. at ¶¶ 47,
4 50-53, 58-60.] The Division also alleges that Arthur Andersen actually noted some of the “red
5 flags” indicating fraud on one of its own internal procedures and that Arthur Andersen was
6 aware of the need for an audit response. [Id. at ¶ 64.] However, the Division alleges that Arthur
7 Andersen failed to perform such an audit response. [Id. at ¶ 65.]

8 In spite of its attempts to characterize Arthur Andersen’s audits as flawed, and Arthur
9 Andersen as a “full participant” in BFA’s fraud, the Division admits that Arthur Andersen
10 attempted to obtain additional information but that BFA’s senior management refused to provide
11 it. [Id. at ¶ 58-59.] It further admits that Arthur Andersen made no representations to investors,
12 but rather gave its audit opinions to BFA. BFA was responsible for making any and all
13 representations to investors. [Id. at ¶ 19-22.] The Division alleged that Arthur Andersen
14 allowed BFA to use its name in promoting the securities sales because BFA stated in its
15 promotional materials that “Arthur Andersen, BFA’s auditor for 14 years, audits the financial
16 statements.” [Id. at ¶ 79.] As a result, the Division alleged that Arthur Andersen violated A.R.S.
17 section 44-1991, and that Arthur Andersen aided and abetted BFA’s violations of A.R.S.
18 sections 44-1841 and 44-1991. [Id. ¶ 84-89.]

19 As more fully explained below, the Division’s allegations fail to state claims against
20 Arthur Andersen for at least three reasons. First, the Division alleged that Arthur Andersen
21 violated Arizona’s securities laws. [Id. at Parts IV, V.] But the Division did not allege that
22 Arthur Andersen sold any securities and, as a matter of law, Arthur Andersen did not participate
23 in or induce BFA’s allegedly unlawful sales. Therefore, Arthur Andersen is not liable for the
24 consequences of BFA’s sales. Second, there is no administrative cause of action in Arizona for
25 aiding and abetting a securities law violation. Third, even if such a cause of action existed, the
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1 Division has not alleged, and cannot prove, sufficient facts to show that Arthur Andersen aided
2 and abetted a violation.

3 As for restitution, even if Arthur Andersen violated the securities laws, the Division is
4 not entitled to such relief. First, the losses, if any, to BFA's investors are too remote to be a
5 condition resulting from Arthur Andersen's audits. Accordingly, restitution is not a proper
6 remedy. Further, the Division's request for restitution is barred by the statute of limitations.

7 **II. THE PLEADING STANDARDS APPLICABLE TO THE DIVISION'S CLAIMS.**

8 **A. Rule 12(b)(6), Arizona Rules of Civil Procedure.**

9 As a general rule, in deciding a motion to dismiss for failure to state claim on which relief
10 can granted, the substantive allegations against the defendant are assumed to be true. *See, e.g.,*
11 *Polaris Int'l Metal Corp. v. Arizona Corp. Comm'n*, 133 Ariz. 500, 502, 652 P.2d 1023, 1025
12 (1982); *see also* Ariz. Admin. Code. R-14-3-101(A) (establishing the Arizona Rules of Civil
13 Procedure for "all actions in which procedure is set forth neither by law, nor by these rules, nor
14 by regulations or orders of the Commission"). However, "conclusions of law or unwarranted
15 deductions of fact" are not considered. *Aldabbagh v. Arizona Dep't of Liquor Licenses &*
16 *Control*, 162 Ariz. 415, 417, 783 P.2d 1207, 1209 (Ct. App. 1989). Therefore, in deciding this
17 motion to dismiss, the Commission must set aside any unsupported, conclusory allegations and
18 consider only whether the factual allegations entitle the Division to the relief it has requested.

19 **B. Rule 9(b), Arizona Rules of Civil Procedure.**

20 The Division alleged that Arthur Andersen committed securities fraud, both directly and
21 by aiding and abetting BFA's separate securities fraud. [Notice, ¶¶ 84-89.] Claims alleging fraud
22 must satisfy the heightened pleading requirements in Rule 9(b), Arizona Rules of Civil
23 Procedure, and must state with particularity the circumstances constituting the fraud. *See State*
24 *ex rel. Corbin v. Goodrich*, 151 Ariz. 118, 123, 726 P.2d 215, 220 (Ct. App. 1986) (applying
25 Rule 9(b) to a securities fraud claim). Rule 9(b) requires a complainant to state the time, place
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1 and specific content of any alleged fraudulent representation, as well as the identities of the
2 parties to it. *See Schreiber Distrib. Co. v. Serv-Well Furniture Co.*, 806 F.2d 1393, 1401 (9th
3 Cir. 1986); *Semegen v. Weidner*, 780 F.2d 727, 731 (9th Cir. 1985). In other words, the
4 complainant must explain specifically how the defendant's alleged conduct constitutes fraud.

5 Rule 9(b) serves to prevent the filing of claims as a pretext to discover fraud and to
6 protect against the injury to reputation that inevitably follows allegations of fraud. *See Semegen*
7 *v. Weidner*, 780 F.2d 727, 731 (9th Cir. 1985). The rule is particularly important when a
8 complainant alleges fraud against "professionals whose reputation in their fields of expertise are
9 most sensitive to slander." *Id.*

10 **III. THE DIVISION FAILED TO STATE A CLAIM AGAINST ARTHUR** 11 **ANDERSEN FOR VIOLATING THE ARIZONA SECURITIES ACT.**

12 The Division's allegations fail to state a claim against Arthur Andersen because an
13 administrative cause of action for violations of the securities laws exists only against those who
14 made, participated in, or induced an unlawful securities sale. *See* A.R.S. § 44-2003 (Supp.
15 1999). The Division did not allege that Arthur Andersen sold any securities and, as a matter of
16 law, Arthur Andersen did not participate or induce any of BFA's securities sale. Consequently,
17 the Division has failed to state claims against Arthur Andersen for securities law violations.

18 **A. Liability For Arizona Securities Act Violations Extends Only To Those Who** **Made, Participated In, Or Induced An Unlawful Securities Sale.**

19 The legislature established both civil and administrative causes of action for securities
20 law violations. *See* A.R.S. §§ 44-2001, 44-2002, 44-2032 (Supp. 1999). From the beginning,
21 the legislature limited liability in civil actions to persons who "made, participated in or induced
22 the unlawful sale or purchase." *See* 1951 Ariz. Sess. Laws ch.18, § 17 (codified at A.R.S. § 44-
23 2003). But in 1996, the legislature amended the Arizona Securities Act and imposed the same
24 limitations on administrative actions as it did on civil actions. *See* 1996 Ariz. Legis. Serv. ch.
25 197, § 7 (West) (amending A.R.S. § 44-2003). Accordingly, liability in administrative actions
26

1 for securities violations is limited to those who make, participate in, or induce an unlawful
2 securities sale or purchase.

3 **B. Arthur Andersen did not make an unlawful securities sale.**

4 The statutory definition of a securities sale is essentially the same under both federal and
5 Arizona law. *Compare* 15 U.S.C.A. § 77b(a)(3) (1997) *with* A.R.S. § 44-1801(19)(Supp. 1999).
6 When Arizona's securities laws are similar or identical to federal law, Arizona's courts try to
7 maintain "consistency in the application of the law." *State v. Gunnison*, 127 Ariz. 110, 112, 618
8 P.2d 604, 606 (1980). Although federal decisions are not binding on Arizona courts interpreting
9 Arizona law, "[u]nless there is a good reason for deviating from the United States Supreme
10 Court's interpretation, we will follow the reasoning of that court." *Id.* at 112-13, 618 P.2d at
11 606-07.

12 The United States Supreme Court has held that a seller under federal securities law is
13 someone who actually transfers title to the security or solicits a plaintiff's investment in order
14 to obtain a financial benefit. *See Pinter v. Dahl*, 486 U.S. 622, 647 (1988). The *Pinter* Court
15 explained that "collateral participants" are not liable as sellers of securities under federal law.
16 *Id.* at 650 n.26. Indeed, the Court specifically noted that a buyer does not purchase securities
17 in any meaningful way from "securities professionals, such as *accountants* and lawyers, whose
18 involvement is only the performance of their professional services." *Id.* at 651 (emphasis
19 added). Accordingly, such persons are outside the reach of seller liability under federal law. No
20 Arizona decision has construed the meaning of "sale" differently under Arizona's securities laws
21 than it is under federal law, and no principled reason exists to do so. Thus, *Pinter* also
22 establishes the meaning of "sale" under Arizona law. By auditing BFA's financial statements,
23 Arthur Andersen neither transferred title to BFA securities, solicited anyone to invest in them,
24 nor received any consideration from those who did. Accordingly, Arthur Anderson is not liable
25 as a seller of securities.

26

1 C. Arthur Andersen Did Not Participate In Or Induce An Unlawful Securities
2 Sale Or Purchase.

3 Similarly, the Division has not stated a claim against Arthur Andersen for participating
4 in or inducing an unlawful securities sale or purchase. In the context of a civil action, an
5 accounting firm does not induce or participate in a securities transaction merely because it
6 performed an audit even if that audit was deficient and influenced the buyer's decision. *See*
7 *Standard Chartered PLC v. Price Waterhouse*, 190 Ariz. 6, 22, 945 P.2d 317, 332 (Ct. App.
8 1996). In *Standard Chartered PLC*, the Price Waterhouse accounting firm performed annual
9 independent audits of an Arizona bank that were integral to merger negotiations between the
10 bank and a foreign corporation. *See id.* at 12-14, 945 P.2d at 323-25. In its unqualified
11 opinions supporting the bank's financial statements, Price Waterhouse reported that its audits
12 conformed with GAAS and GAAP. *See id.* However, Price Waterhouse did not follow GAAS
13 and GAAP and failed to discover that the bank's financial statements were materially misstated
14 and the bank's internal control systems were materially unsound. *See id.* at 14, 945 P.2d at 325.
15 In addition to its audits, Price Waterhouse helped fund the acquisition by preparing financial
16 information for three public securities offerings, consenting to the inclusion of its audit report
17 in regulatory filings, and writing comfort letters confirming that the bank's financial statements
18 complied with federal accounting requirements. *See id.* at 13-14, 945 P.2d at 324-25. Because
19 of Price Waterhouse's representations, the foreign corporation closed the deal and lost over three
20 hundred million dollars. *See id.* at 14-15, 945 P.2d at 325-26. It sued Price Waterhouse under
21 several theories, including securities fraud under A.R.S. section 44-1991. *See id.*

22 The Arizona Court of Appeals held that the plaintiff corporation had no civil cause of
23 action against Price Waterhouse for violating section 44-1991. *See id.* at 22-23, 945 P.2d at 333-
24 34. Because Price Waterhouse had not sold any securities, it could only be liable if it
25 "participated in or induced the unlawful sale or purchase." *Id.* at 18, 945 P.2d at 329 (quoting
26 A.R.S. § 44-2003). But the court concluded that an auditor does not participate in or induce a

1 securities sale simply by preparing an audit. *See id.* at 21, 945 P.2d at 332. Price Waterhouse
2 had no financial stake in the merger and its audit process did not differ from what it would have
3 done had no merger been in progress. *See id.* Thus, it had not participated in the sale. *See id.*
4 Further, the court concluded that “induce” did not extend liability to anyone “who provided
5 information that foreseeably contributed to, and thereby influenced, a buyer or seller’s decision
6 to engage in the transaction.” *Id.* at 21. “Had the legislature intended so extensive a private
7 remedy, it could simply have done so against any person who violated section 44-1991.” *Id.* at
8 22, 945 P.2d at 333. Thus, because it had “merely provide[d] information that contribute[d] to
9 a buyer or seller’s decision to close the deal,” Price Waterhouse was not liable in a civil action
10 for securities law violations. *Id.*

11 Under *Standard Chartered PLC*, the Division has no cause of action against Arthur
12 Andersen for participating in or inducing BFA’s securities sales. Granted, *Standard Chartered*
13 *PLC* concerned civil liability under A.R.S. sections 44-2001 and 44-2003, not administrative
14 liability under section 44-2032. But, the legislature amended section 44-2003 in 1996 and
15 included administrative actions within the “participated in or induced” limitation. *See* 1996
16 Ariz. Legis. Serv. ch. 197, § 6 (West). At the same time, the legislature added language to the
17 statute specifically providing that “[n]o person shall be deemed to have participated in any sale
18 or purchase solely by reason of having acted in the ordinary course of that person’s professional
19 capacity in connection with that sale or purchase.” *Id.* Thus, the scope of administrative liability
20 is coextensive with the scope of civil liability described in *Standard Chartered PLC*. Arthur
21 Andersen merely acted in its professional capacity as an auditor. Arthur Andersen had no stake
22 in BFA’s securities sales and received no consideration from BFA’s investors. Accordingly, the
23 Division has not stated a claim because Arthur Andersen did not make, participate in, or induce
24 an illegal securities sale.

1 **III. THE DIVISION FAILED TO STATE A CLAIM AGAINST ARTHUR**
2 **ANDERSEN FOR AIDING AND ABETTING THE SALE OF UNREGISTERED**
3 **SECURITIES.**

4 The Division's allegations that Arthur Andersen aided and abetted the sale of BFA's
5 unregistered securities fail to state a claim for at least two reasons. First, Arizona no longer
6 recognizes a cause of action for aiding and abetting the sale of unregistered securities. Second,
7 even if Arizona recognized such a cause of action, Arthur Andersen cannot be liable for aiding
8 and abetting because it did not provide any necessary assistance to BFA.

9 **A. Arizona Does Not Recognize A Public Cause Of Action For Aiding And**
10 **Abetting The Sale Of Unregistered Securities.**

11 No Arizona statute or court decision recognizes a public cause of action for aiding and
12 abetting the sale of unregistered securities. Granted, at one time, the Arizona Supreme Court
13 recognized a *private* cause of action for aiding and abetting securities fraud. *See State v.*
14 *Superior Court*, 123 Ariz. 324, 331, 599 P.2d 777, 784 (1979), *overruled in part on other*
15 *grounds, State v. Gunnison*, 127 Ariz. 110, 618 P.2d 604 (1980). However, even if the supreme
16 court's reasoning supported a *public* cause of action for aiding and abetting, *State v. Superior*
17 *Court* is no longer good law because subsequent decisions and legislative acts have stripped it
18 of its force.

19 In 1994, the United States Supreme Court held that no private cause of action exists for
20 aiding and abetting federal securities fraud. *See Central Bank v. First Interstate Bank*, 511 U.S.
21 164, 191 (1994). In reaching its decision, the Court explained that "the text of the statute
22 controls our decision." *Id.* at 173. Thus, because the federal statute did not prohibit aiding and
23 abetting securities fraud, no private civil liability for it existed. *See id.* at 176. The dissent
24 opined that the Court's decision also stripped the Securities and Exchange Commission ("SEC")
25 of its authority to bring a public action for aiding and abetting securities fraud. *See id.* at 200
26 (Stevens, J., dissenting). Congress subsequently restored the SEC's power aiders and abettors

1 in 1995. *See* Private Securities Litigation Reform Act of 1995, Pub. L. No. 106-67, sec. 104,
2 § 78t, 109 Stat. 735, 737 (1995).

3 After *Central Bank* and the subsequent congressional amendments, no cause of action for
4 aiding and abetting the sale of unregistered securities exists in Arizona for three reasons. First,
5 as with the federal statutes before *Central Bank*, Arizona's statutes provide no express cause of
6 action for aiding and abetting the sale of unregistered securities. Second, the legislature
7 amended Arizona's securities laws after *Central Bank* and it could have restored liability for
8 aiding and abetting. It did not. Instead, the legislature expressly refused to determine "whether
9 and in what circumstances aiding and abetting liability exists under [the Arizona Securities
10 Act.]" 1996 Ariz. Legis. Serv. ch. 197, § 11(B) (West). But, the legislature also has directed
11 that "in construing the provisions of [the Arizona Securities Act], the courts may use as a guide
12 the interpretations of the securities and exchange commission and the federal or other courts in
13 construing substantially similar provisions in the federal securities laws." *Id.* ch 197, § 11(C).

14 The legislature did not simply "pass the buck." It wisely and prudently deferred to
15 Arizona's courts to harmonize state and federal securities law. Against this backdrop, unless and
16 until Arizona's courts decide otherwise, no cause of action exists in Arizona for aiding and
17 abetting a sale of unregistered securities.

18 **B. Arthur Andersen Cannot Be Liable For Aiding And Abetting BFA's Alleged**
19 **Securities Law Violations Because It Did Not Make A Necessary**
20 **Contribution To The Violation.**

21 Even if a public cause of action for aiding and abetting existed in Arizona, the Division
22 has not stated such a claim against Arthur Andersen. To establish aider and abettor liability, a
23 plaintiff must show that: (1) a primary violation occurred; (2) the person charged had knowledge
24 of or a duty to inquire about the primary violation; and (3) the person charged made a necessary
25 contribution to the underlying primary violation. *See State v Superior Court*, 123 Ariz. at 331,
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1 599 P.2d at 784 (citing *SEC v. National Student Mktg. Corp.*, 402 F. Supp. 641 (D.D.C. 1975)).²

2 Even if the Division could prove any of its allegations, the Division's claim of aiding and
3 abetting fails because it has not alleged that Arthur Andersen made a necessary contribution to
4 BFA's securities violations.

5 The Division goes to great lengths to describe what it sees as Arthur Andersen's improper
6 auditing practices. But conspicuously absent is any allegation that, without these alleged
7 improprieties, the result would have been any different. The Division has not alleged that any
8 investor would have refused to buy BFA's securities but for the influence of Arthur Andersen's
9 audit opinions. The Division has not alleged that BFA's Board of Directors would have taken
10 any positive steps to stop the securities violations from continuing or to remedy those that had
11 already occurred, but for the influence of Arthur Andersen's audit opinions. Consequently,
12 Arthur Andersen's audits were not necessary to any of the alleged securities law violation.
13 Therefore, Arthur Andersen is not liable for aiding and abetting a violation.

14 **IV. EVEN IF THE COMMISSION CONCLUDES THAT THE DIVISION HAS**
15 **STATED CLAIMS AGAINST ARTHUR ANDERSEN, THE COMMISSION MAY**
16 **NOT ORDER ARTHUR ANDERSEN TO PAY RESTITUTION.**

17 **A. The Commission Has No Authority To Order Arthur Andersen To Pay**
18 **Restitution In This Matter.**

19 The Commission has no authority to order Arthur Andersen to pay restitution as a result
20 of Arthur Andersen's conduct related to BFA's sale of allegedly fraudulent securities. The
21 Commission's authority comes from the Arizona Constitution and, although the legislature may
22 enlarge the Commission's authority over matters given to it by the Constitution, "the
23 Commission 'has no implied powers and its powers do not exceed those to be derived from a
24 strict construction of the Constitution and implementing statutes.'" *Arizona Corp. Comm'n v.*

25 ² Although aiding and abetting securities violations no longer exists in Arizona, the
26 elements for such a cause of action would be those in *State v. Superior Court*.

1 *State ex rel. Woods*, 171 Ariz. 286, 293, 830 P.2d 807, 814 (1992). The Constitution gives the
2 Commission authority over the sale of securities, and “[t]he complete regulatory scheme is found
3 in A.R.S. §§ 44-1801 through 44-2055.” *Jennings v. Woods*, 194 Ariz. 314, 323, ¶ 40, 982 P.2d
4 274, 283 (1999). Under the implementing statutes, the Commission has broad remedial and
5 punitive power over securities laws violations, including the authority to order a culpable party
6 to pay restitution. *See* A.R.S. §§ 44-2032, 44-2036 (1994 & Supp. 1999). However, the
7 Commission’s broad restitution power is not without limits.

8 The Commission’s power to order restitution does not extend to securities act violations
9 that do not directly cause a loss. Restitution has both remedial and punitive aspects, but its
10 primary purpose is to compensate for a victim’s losses caused by the defendant’s illegal act. *See*
11 *State v. Wilkinson*, 2000 WL 1279678, at * 2, ¶ 7 (Ct. App. Sept. 12, 2000) (noting that Arizona
12 courts must order restitution for a crime victim’s economic loss); *FDIC v. Colossi*, 194 Ariz.
13 114, 117, ¶ 11, 977 P.2d 836, 839 (Ct. App. 1998) (explaining that settlement of a civil lawsuit
14 extinguishes an obligation to pay criminal restitution “to the extent that [it] compensates the
15 victim”); *Roberts v. State*, 179 Ariz. 613, 618, 880 P.2d 1159, 1164 (Ct. App. 1994) (allowing
16 the Superintendent of Banks to order an unlicensed lender to compensate a borrower by
17 returning a loan fee); *State v. Iniguez*, 169 Ariz. 533, 536, 821 P.2d 184, 197 (Ct. App. 1991)
18 (holding that criminal restitution and civil damages should be coordinated to fully compensate
19 the victim). The Commission, however, may order restitution only “to correct the conditions
20 resulting from the act, practice or transaction” that violates the securities laws. A.R.S. § 44-
21 2032(1). Thus, for the Commission to have power to order restitution, the restitution must be
22 corrective. In other words, the Commission may only order restitution for a securities act
23 violation when it is a proper remedy.

24 For restitution to be a proper remedy, the defendant’s conduct must directly cause the
25 victim’s losses. *See Wilkinson*, 2000 WL 1279678, at *2, ¶ 7. In *Wilkinson*, two homeowners
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1 entered into residential remodeling contracts with an unlicensed contractor who had represented
2 himself as licensed. *See id.* at *1, ¶ 2. The contractor accepted payment, but left the projects
3 unfinished and failed to correct work. *See id.* The contractor was charged with contracting
4 without a license, a class 1 misdemeanor, and the municipal court fined him and ordered him to
5 pay restitution to the homeowners. *See id.* at *1, ¶¶ 2-3. However, the superior court reversed
6 the restitution order because it found that the homeowners' losses were attributable to the
7 contractor's "shoddy and incomplete work" . . . , [not] his failure to procure a license." *Id.* at
8 *1, ¶ 4. Thus, the losses were not attributable to the contractor's illegal conduct. *See id.*

9 The Arizona Court of Appeals agreed. *See id.* at *6, ¶ 27. The court explained that
10 restitution for an illegal act is proper only when a sufficient nexus exists between the illegal
11 conduct and the victim's loss. *See id.* at *2, ¶¶ 7-8. The contractor's illegal act was contracting
12 without a license. *See id.* at *3, ¶ 12. But if the unlicensed contractor had performed
13 competently, the homeowners would have suffered no losses. *See id.* Therefore, the court
14 reasoned that "unworkmanlike performance is a direct and necessary element of causation in
15 cases of this nature, as is misrepresentation or nondisclosure." *Id.* at *3, ¶ 14. Because neither
16 unworkmanlike performance, misrepresentation, or nondisclosure was an element of the crime
17 with which the contractor was charged, he could not be ordered to pay restitution as a result of
18 his conviction. *See id.*

19 As in *Wilkinson*, Arthur Andersen's alleged conduct, even if true, is too remote from the
20 investors' losses to support a restitution order. Without BFA's securities sales, the investors
21 would have suffered no loss. As discussed above, Arthur Andersen did not participate in or
22 induce any of BFA's securities sales merely because it provided audits, even if those audits were
23 deficient. *See discussion, supra*, Part III.C. Consequently, the investors' losses, if any, are too
24 remote from Arthur Andersen's alleged violations of the securities law to conclude that those
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1 losses are a condition resulting from Arthur Andersen's conduct. Accordingly, Arizona law
2 gives the Commission no authority to order Arthur Andersen to pay restitution to the investors.

3 **B. The Division's Request For Restitution Is Barred By The Two-Year Statute**
4 **Of Limitations.**

5 **1. The State is immune from statutes of limitations when it brings a**
6 **public enforcement action.**

7 Ordinarily, the statute of limitations would bar this action from proceeding. However,
8 the State is not bound by statutes of limitations when it seeks to enforce a public right. *See In*
9 *re Diamond Benefits Life Ins. Co.*, 184 Ariz. 94, 98, 907 P.2d 63, 67 (1995); *City of Bisbee v.*
10 *Cochise County*, 52 Ariz. 1, 8, 78 P.2d 982, 985 (1938); *Trimble v. American Savings Life Ins.*
11 *Co.*, 152 Ariz. 548, 555, 733 P.2d 1131, 1138 (Ct. App. 1986). The State's immunity is rooted
12 in the common law and prevents "the public from suffering 'because of the negligence of it
13 officers and agents' in failing to assert causes of action which belong to the public." *Trimble*,
14 152 Ariz. at 555, 733 P.2d at 1138; *see City of Bisbee*, 52 Ariz. at 8-9, 78 P.2d at 985. The
15 Arizona legislature has expressly recognized the State's immunity by statute, but the statute
16 "does not add to nor subtract from the common-law rule." *City of Bisbee*, 52 Ariz. at 8, 78 P.2d
17 at 985. Thus, for the State to benefit from its immunity, it must assert rights it holds for the
18 benefit of all of Arizona's citizens. *See In re Diamond Benefits Lift Ins. Co.*, 184 Ariz. at 98,
19 907 P.2d at 67 (holding that a receiver's civil action was not barred because "the benefits of the
20 action also run to the citizenry as a whole"); *Trimble*, 152 Ariz. at 555, 733 P.2d at 1138
21 (explaining that the State's immunity "does not apply if the right belongs only to the government
22 or to some small and distinct section of the public"); *City of Bisbee*, 52 Ariz. at 9, 78 P.2d at 985
23 (explaining that State actions to enforce public rights are immune from statutes of limitations
24 because "the purpose of their enforcement is always the common weal, and not the private
25 benefit of any particular individual").
26

1 When the State brings a public enforcement action, incidental benefits may run to
2 individuals without defeating the State's immunity. *See In re Diamond Benefits Life Ins. Co.*,
3 184 Ariz. at 98, 907 P.2d at 67; *Trimble*, 152 Ariz. at 444, 733 P.2d at 1138. In *Trimble*, the
4 State brought a civil action against an insurance company for securities and insurance fraud. *See*
5 152 Ariz. at 550-51, 733 P.2d at 1133-34. Under the insurance rehabilitation statutes, the
6 superior court enjoined further securities sales, appointed a receiver, and ordered development
7 of a reorganization plan for the company. *See id.* at 551, 733 P.2d at 1134. The resulting
8 reorganization plan included a rescission option for investors, but the superior court limited it
9 to those investors who had purchased securities within the two-year statute of limitations. *See*
10 *id.* at 554, 733 P.2d at 1137.

11 The Arizona Court of Appeals held that the statute of limitations did not apply to the
12 rescission remedy. In reaching this result, the court placed particular emphasis on "the
13 importance of the insurance rehabilitation statutes in this matter." *Id.* at 556, 733 P.2d 1131. The
14 insurance company was insolvent because it had materially overstated its financial condition to
15 further its fraudulent investment scheme. *See id.* at 551, 733 P.2d at 1133. Thus, the insurance
16 rehabilitation statutes authorized the State to create a remedy that included a rescission option
17 for investors. *See id.* at 556, 733 P.2d at 1138. Because the legislature intended rehabilitation
18 of insurance companies to benefit the public generally, the benefit to individuals did "not
19 diminish the public interest nature of the proceeding." *Id.* Accordingly, the statute of limitations
20 did not prevent the State from offering a rescission option to all of the investors. *See id.*

21 In a second insurance decision, the Arizona Supreme Court approved the fundamental
22 reasoning in *Trimble*. *See In re Diamond Benefits Ins. Co.*, 184 Ariz. at 98, 907 P.2d at 67. The
23 supreme court held that the statute of limitations did not apply to conversion claims brought on
24 behalf of an insurance company by its statutory receiver. *See id.* The court reasoned that the
25 State was a real party in interest in the conversion action because it supervises a fund that pays
26

1 claims against insolvent insurers. *See id.* at 96, 907 P.2d at 65. Further, the receiver was acting
2 “pursuant to a legislative scheme designed to protect the public from the dangers of a non-
3 complying insurance company.” *Id.* at 97, 907 P.2d at 66. The public interest was not
4 overshadowed by individual benefits and, therefore, the statute of limitations did not bar the
5 receiver’s conversion claims. *See id.* at 98, 90 P.2d at 67.

6 **2. The Division’s request for restitution is not a public enforcement**
7 **action and so is barred by the two-year statute of limitations.**

8 Unlike *In re Diamond Benefits Life Insurance Co.* and *Trimble*, the Division’s claims for
9 restitution are not part of a public enforcement action. The State did not invest in any of BFA’s
10 securities, nor does it manage a fund to protect investors similar to the fund it manages to protect
11 insureds. Therefore, the State is not a real party in interest to any claim for restitution.
12 Restitution is not a tool to rehabilitate Arthur Andersen because, as explained above, Arthur
13 Andersen did not directly cause any of the investors’ losses. Thus, the State merely stands in the
14 shoes of the individual BFA investors and attempts to circumvent the legislatively created time
15 limit on the BFA investors’ causes of action. The Division’s request for restitution does not
16 assert any right held by the State for the general public and, therefore, the statute of limitations
17 runs against the Division’s request.

18 Because the Securities Division brought this action before the Commission more than two
19 years after BFA’s alleged fraud was publicly known, its claim for restitution is barred. No civil
20 claim may be brought under the securities law more than two years after it could have been
21 discovered by the exercise of reasonable diligence. *See* A.R.S. § 44-2004 (Supp. 1999). The
22 Division admits in its Notice that the *Phoenix New Times* published a series of articles in April
23 1998 containing “serious allegations of fraud and insider dealings, mention[ing] specific
24 questionable transactions and impl[y]ing misdealing by” BFA senior management. [Notice, ¶
25 71.] Therefore, allegations against BFA for fraud and misconduct were public knowledge in
26 April 1998. At that time, BFA’s investors reasonably should have known of the allegations and,

1 through the exercise of reasonable diligence, could have known that they had claims against
2 BFA and that such claims would include a claim for restitution. The investors, therefore, are
3 barred by the statute of limitations from asserting any cause of action based on BFA's sale of
4 securities. *See Aaron v. Fromkin*, 196 Ariz. 224, 227, 994 P.2d 1039, 1042 (App. 2000) (holding
5 that the statute of limitations begins to run when the fraudulent practice is discovered). Because
6 the investors' claims are barred by the statute of limitations, the Divisions's claims are likewise
7 barred.

8 **V. CONCLUSION**

9 For the foregoing reasons, Arthur Andersen respectfully requests that all claims raised
10 by the Division against it be dismissed.

11 RESPECTFULLY SUBMITTED this 17th day of October, 2000.

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