No. _____

In the Supreme Court of the United States

CHRISTOPHER M. GIBSON,
Petitioner,
v.
SECURITIES AND EXCHANGE COMMISSION, ET AL.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Since the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act in 2010, the Securities and Exchange Commission (SEC) has brought an increasing number of enforcement actions before the agency itself, rather than in federal court. The SEC routinely delegates its authority to preside over these actions to its own cadre of administrative law judges (ALJs). Because these ALJs exercise "significant authority," they are "'Officers of the United States'" for purposes of the Constitution's Appointments Clause. *Lucia v. SEC*, 138 S. Ct. 2044, 2051-55 (2018) (quoting U.S. Const. art. II, § 2, cl. 2). For individuals subject to SEC enforcement proceedings, the ALJs' actions and findings can have significant, often life-ruining consequences.

The SEC's ALJs, however, suffer from a blatant constitutional defect: they are insulated from removal by multiple "layers of good-cause tenure" protection, which this Court found "incompatible with the Constitution's separation of powers" in *Free Enterprise Fund v. Public Co. Accounting Oversight Board*, 561 U.S. 477, 497-98 (2010). The ALJs' actions also are subject to the same administrative review scheme that the Court held in *Free Enterprise Fund* did not "expressly" or "implicitly" strip federal district courts of their usual jurisdiction to adjudicate federal "separation-of-powers claim[s]." *Id.* at 489-91 & n.2; *see* 28 U.S.C. § 1331. The question presented is:

Whether Congress has implicitly stripped federal district courts of jurisdiction to adjudicate separation-of-powers challenges to the authority of SEC ALJs to preside over enforcement proceedings.

PARTIES TO THE PROCEEDING

Petitioner (plaintiff-appellant below) is Christopher M. Gibson.

Respondents (defendants-appellees below) are the Securities and Exchange Commission; Jay Clayton, in his official capacity as Chairman of the Securities and Exchange Commission; and William P. Barr, in his official capacity as Attorney General of the United States.

RELATED PROCEEDINGS

United States Court of Appeals (11th Cir.):

Gibson v. SEC, No. 19-11969 (Dec. 30, 2019), *reh'g denied* (Apr. 1, 2020)

United States District Court (N.D. Ga.):

Gibson v. SEC, No. 19-cv-01014 (May 8, 2019)

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PETITION FOR A WRIT OF CERTIORARI

Petitioner Christopher M. Gibson respectfully petitions this Court for a writ of certiorari to review the judgment of the United States Court of Appeals for the Eleventh Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. 1a-6a) is available at 795 F. App'x 753. The order of the district court (App. 7a-10a) is available at 2019 WL 5698679.

JURISDICTION

The court of appeals entered its judgment on December 30, 2019 (App. 1a) and denied a timely petition for rehearing on April 1, 2020 (App. 11a). On March 19, 2020, this Court entered an order extending the deadline for filing a petition for a writ of certiorari to 150 days from the date of an order denying a timely petition for rehearing. This Court has jurisdiction under 28 U.S.C. § 1254(1).

CONSTITUTIONAL, STATUTORY, AND REGULATORY PROVISIONS INVOLVED

Pertinent constitutional, statutory, and regulatory provisions are reproduced at App. 113a-30a.

INTRODUCTION

This case concerns the statutory jurisdiction of federal district courts to consider structural constitutional claims that directly impact individual liberty. When individuals like petitioner Christopher Gibson are accused of violating the securities laws in a civil enforcement proceeding brought by the Securities and Exchange Commission (SEC or Commission), they typically find themselves before administrative law judges (ALJs) who preside over

lengthy proceedings in which, statistics show, the SEC enjoys a distinct home-court advantage. As has been true for Gibson, these proceedings often impose a crushing personal and financial burden on their subjects, jeopardizing their very livelihood. Yet, according to the SEC, there is no right of judicial review in an Article III court for structural constitutional claims challenging the legitimacy of this administrative decisionmaker until an enforcement action has made its way past the ALJ and past the Commission, and the respondent has paid any penalty assessed by the SEC. This can be, and typically is, a lengthy ordeal that leaves most respondents—even those who vigorously maintain that they have not violated the securities laws—with little choice but to settle with the SEC before they ever have an opportunity to see an Article III judge.

What makes this ordeal all the more troubling is that a glaring constitutional defect pervades the structure of these proceedings and undermines the legitimacy of the SEC's use of ALJs as the primary decisionmaker. As this Court has held, SEC ALJs—who exercise "extensive" authority over enforcement proceedings and the subjects of such proceedings—are full-fledged "'Officers of the United States'" for purposes of the Constitution's Appointments Clause. *Lucia v. SEC*, 138 S. Ct. 2044, 2049-52 (2018) (quoting U.S. Const. art. II, § 2, cl. 2). Yet the ALJs are insulated from removal by a regime of multiple "layers of good-cause tenure" protection—a regime that this Court declared "incompatible with the Constitution's separation of powers" in *Free Enterprise Fund v. Public Co. Accounting Oversight Board*, 561 U.S. 477, 497-98 (2010). This multilayered protection is a structural constitutional

violation that taints the authority of these frontline decisionmakers and all the proceedings that follow.

Faced with the prospect of ruinous proceedings superintended by an Executive-branch officer acting without legitimate constitutional authority, private citizens like Gibson naturally seek relief in the federal courts, which have long exercised their federal-question jurisdiction to "'protect rights safeguarded by the Constitution'" by "'preventing entities from acting unconstitutionally.'" *Id.* at 491 n.2 (citations omitted). But five circuits—including the Eleventh Circuit below—have nevertheless held, over the disagreement of several federal judges, that an individual like Gibson cannot obtain immediate judicial review in an Article III court of his claim that perhaps the most important decisionmaker in his case lacks constitutional authority. Instead, these circuits require first running the entire gauntlet of the SEC's own enforcement proceedings, something that can take years and often destroys its subjects before any opportunity for judicial review arises.

This makes no sense. As this Court itself recognized in *Free Enterprise Fund*, the securities laws do *not* "expressly" strip district courts of jurisdiction over such claims. *Id.* at 489. Instead, the circuits have held that, under the multifactor test of *Thunder Basin Coal Co. v. Reich*, 510 U.S. 200 (1994), Congress *impliedly* stripped district courts of jurisdiction over structural constitutional challenges merely by creating an administrative review scheme for resolving individual SEC enforcement proceedings. But *Free Enterprise Fund* squarely rejected such a sweeping application of *Thunder Basin* in the context of a directly analogous challenge to unconstitutionally insulated officers. The Court

held that this same SEC review scheme did *not* "implicitly" strip federal district courts of their usual jurisdiction to adjudicate "an Appointments Clause or separation-of-powers claim" in the first instance. 561 U.S. at 489-91 & n.2.

As two dissenting judges from the Second and Fifth Circuits and multiple district court judges have persuasively reasoned, there is no basis for departing from *Free Enterprise Fund*'s jurisdictional holding for challenges to ALJs' constitutional authority to preside over enforcement actions. Nor is there any valid reason to bar individuals like Gibson who find themselves in the crosshairs of an SEC enforcement action from bringing this kind of first-order, structural constitutional challenge in a federal district court. Because this rule has become entrenched, this Court's intervention is needed to ensure that individuals are not improperly denied a federal forum in which to seek relief *before* they have suffered at the hands of an unconstitutionally insulated agency official. The petition should be granted.

STATEMENT OF THE CASE

A. SEC Enforcement Actions

1. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 "dramatically expanded" the authority of the SEC to impose penalties administratively, making administrative proceedings "essentially 'coextensive with [the SEC's] authority to seek penalties in Federal court.'" *Tilton v. SEC*, 824 F.3d 276, 279 (2d Cir. 2016) (alteration in original) (citation omitted), *cert. denied*, 137 S. Ct. 2187 (2017). Since then, the SEC has shifted its enforcement efforts to its home court, where the

SEC's own ALJs preside over cases. *See Lucia*, 138 S. Ct. at 2049. In fiscal year 2019, for example, the SEC brought nearly 77% of its enforcement proceedings in its in-house tribunal before its own ALJs. Div. of Enf't, SEC, *2019 Annual Report* 29 (2019).[1]

This is hardly a coincidence. Unsurprisingly, the SEC fares far better before its own ALJs than it does before Article III judges. One study found that, between October 2010 and March 2015, the Commission won more than 90% of cases it brought before its own ALJs, a rate markedly higher than its 69% success rate in federal court over the same period. Jean Eaglesham, *SEC Wins with In-House Judges*, Wall St. J. (May 6, 2015).[2]

In presiding over these in-house proceedings, SEC ALJs wield "extensive powers." *Lucia*, 138 S. Ct. at 2049. ALJs "'regulat[e] the course of' the proceeding and the 'conduct of the parties and their counsel'"—*e.g.*, by "supervising discovery; issuing, revoking, or modifying subpoenas; deciding motions; ruling on the admissibility of evidence; administering oaths; hearing and examining witnesses; . . . and imposing sanctions"—which can be "severe"—for "violations of [their] orders," "violations of procedural requirements," or otherwise "'contemptuous conduct.'" *Id.* at 2049, 2053 (citations and internal alterations omitted). Once the proceedings conclude, ALJs issue publicly available "decisions containing factual findings, legal conclusions, and appropriate remedies." *Id.* at 2053. As a result of their expansive

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[1] https://www.sec.gov/files/enforcement-annual-report-2019.pdf.

[2] https://www.wsj.com/articles/sec-wins-with-in-house-judges-1430965803.

powers—nearly coextensive with those of "federal trial judges"—this Court has held that SEC ALJs "are 'Officers of the United States,' subject to the Appointments Clause." *Id.* at 2053, 2055.

Nevertheless, SEC ALJs are separated from the oversight and removal of the Chief Executive by not just one but *multiple* "layers of good-cause tenure" protection. *Free Enter. Fund*, 561 U.S. at 496-97. At a minimum, there are two layers of protection from removal: ALJs can be removed "only for good cause established and determined by the Merit Systems Protection Board [(MSPB)]," 5 U.S.C. § 7521(a), and MSPB officials are removable by the President "only for inefficiency, neglect of duty, or malfeasance in office," *id.* § 1202(d). This scheme thus establishes at least "dual for-cause limitations" on ALJs' removal. *Free Enter. Fund*, 561 U.S. at 492.

2. Parties can petition the Commission for "discretionary" review of adverse ALJ decisions. 15 U.S.C. § 78d-1(b). If the Commission declines review, "the ALJ's decision itself 'becomes final' and is 'deemed the action of the Commission.'" *Lucia*, 138 S. Ct. at 2054 (citations omitted). Moreover, even when the Commission grants review, it typically defers to the ALJ's "findings of fact," and when the "factfinding derives from credibility judgments, as it frequently does, acceptance [by the Commission] is near-automatic." *Id.* at 2054-55; *see also* Eaglesham, *supra* (noting that the Commission adopted the ALJ's factual findings 95% of the time).

A party "aggrieved by a final order of the Commission" may then seek judicial review of that order in a federal court of appeals. 15 U.S.C. § 78y(a)(1); *see id.* §§ 80a-42(a), 80b-13(a). But the sanctions imposed by the SEC do not await judicial

review. Absent a stay—which typically is difficult to obtain—the SEC can collect any monetary penalties as well as suspend an individual's professional licenses and, accordingly, upend his or her livelihood, all before the individual ever sees the inside of an Article III court. *See id.* §§ 78y(c)(2), 80b-13(b); 17 C.F.R. § 201.360(d); *see also, e.g.*, *In re Se. Invs., N.C., Inc.*, Exchange Act Release No. 86097, 2019 WL 2448245, at *2 (June 12, 2019) (describing a stay as an "'extraordinary remedy'" (citation omitted)).

Because it can take years to get to this point, at enormous financial cost, many individuals—despite vigorously contesting their guilt—have little practical choice but to settle with the SEC and try to rebuild their lives before they get to a federal court. *See* Gideon Mark, *SEC and CFTC Administrative Proceedings*, 19 U. Pa. J. Const. L. 45, 57 (2016) (noting that between 2002 and 2014, the SEC settled "about 98%" of cases). As a result, most individuals never have an opportunity to present their claims to an Article III court, even when they dispute the authority of the decisionmaker.

In *Free Enterprise Fund*, this Court concluded that this same administrative review scheme did not "strip" federal district courts of their jurisdiction over "an Appointments Clause or separation-of-powers claim" challenging the authority of the Public Company Accounting Oversight Board, another body of inferior officers exercising authority under the SEC. 561 U.S. at 487-91 & n.2. As the Court explained, this review scheme "does not expressly limit the jurisdiction that other statutes confer on district courts." *Id.* at 489. Likewise, the Court held, it does not do so "implicitly" under *Thunder Basin*—the "'statutory scheme'" does not "display[] a 'fairly

discernible' intent to limit jurisdiction," and claims challenging the constitutional authority of decisionmakers are not "'of the type Congress intended to be reviewed within th[e] statutory structure.'" *Free Enter. Fund*, 561 U.S. at 489-91 (second alteration in original) (quoting *Thunder Basin*, 510 U.S. at 207, 212).

To date, however, the five circuits to consider the issue have held that, contrary to *Free Enterprise Fund*'s application of *Thunder Basin* to the same statutory scheme, district courts lack jurisdiction to adjudicate challenges to the constitutional authority of SEC ALJs. *See infra* at 17-18. According to these circuits, such challenges must be brought before the SEC ALJs themselves, and then the Commission, before they can reach an Article III court.

B. Facts and Proceedings Below

1. Christopher Gibson, a former investment adviser, has been trapped in an SEC nightmare for much of his professional life. Gibson graduated from college in 2006. App. 18a. Following a two-year stint working in investment banking in New York, he returned home to Augusta, Georgia. *Id.* at 18a-19a. He passed the investment advisers examination and began working for James Hull, a friend of Gibson's family and successful real estate developer. *Id.* at 18a-20a. After Gibson generated six months of successful returns for Hull on various commodities investments, Hull had Gibson set up the Geier International Strategies Fund, LLC (the Fund). *Id.* at 12a, 20a-21a.

By February 2010, the Fund held some $32 million, with 80% belonging to Hull and 10% to his friends. Compl. ¶ 42, D. Ct. Doc. 1 (Mar. 4, 2019). The

remaining 10% belonged to Gibson and his family, and it reflected Hull's insistence that Gibson and his family have "skin in the game"—Hull required Gibson to invest his entire net worth in the Fund or in the securities in which the Fund invested, and he loaned Gibson and his father more than $1 million to invest in demand notes that he refused to let them extinguish. App. 24a-25a, 94a. This severe arrangement meant that "if the Fund lost money," Gibson and his family "would lose more than other investors." *Id.* at 24a-25a.

In late 2010, Hull directed Gibson to move the Fund's investments from commodities into the securities of a single company that could serve as a proxy for gold. *Id.* at 29a-30a. After researching the matter, Gibson recommended Tanzanian Royalty Exploration Corporation (TRX) as an investment vehicle. *Id.* Hull agreed and approved the Fund's investment in TRX shares. *See id.*

By the end of April 2011, the Fund had invested all of its assets in TRX. *Id.* at 30a. Hull, Gibson, and Gibson's family members had also purchased TRX shares outside of the Fund. *See id.* at 36a-38a. But later that year, the TRX share price began to inexplicably decline, and Hull and Gibson ultimately decided to reduce their and the Fund's TRX position. *Id.* at 30a-35a. By November 2011, the Fund had sold all of its TRX shares at a substantial loss. *Id.* at 36a-55a. Gibson had also sold the TRX shares he and his family owned outside of the Fund as well as the TRX shares personally owned by Hull. *See id.* Gibson personally lost more than $700,000—wiping out his own assets. *Id.* at 56a.

2. a. Following a two-year investigation, the SEC issued an Order Instituting Proceedings (OIP) in 2016

charging Gibson with violating the Securities Exchange Act and the Investment Advisors Act based on the particular order in which Gibson executed the sales of the TRX shares. *In re Gibson*, Exchange Act Release No. 77466, 2016 WL 1213259 (Mar. 29, 2016).

Specifically, the SEC claimed that Gibson engaged in impermissible "front running," in breach of his fiduciary duties to the Fund as its investment adviser, by selling a small fraction (less than one percent) of the shares he personally owned or controlled just before selling a portion of the Fund's shares, and by purchasing put options as the TRX price tumbled to mitigate his losses. *Id.* at *4-8.[3] The SEC also claimed that Gibson "favored" Hull over the Fund (despite Hull's 80% ownership in the Fund) by consolidating Hull's personally owned TRX shares with the Fund's shares to facilitate a block sale. *Id.* at *5-6. Notably, *none* of these mechanical aspects of the TRX sales actually harmed the Fund. App. 92a, 101a.

Consistent with its preference to litigate before its in-house tribunal, the Commission elected to proceed administratively rather than in federal court. The case was assigned to ALJ Brenda Murray, who had

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[3] The term "front running" generally means "trading a security while in possession of unreported information concerning" a client's imminent "block transaction in the same or a related security." Exchange Act Release No. 14156, 1977 WL 190058, at *1 (Nov. 9, 1977). There is, however, "no specific statute or regulation prohibiting front running," and "unlike insider trading, which courts have long addressed under the federal securities laws, there is little case law addressing front running under the antifraud provisions of federal securities law." App. 66a-67a. As a result, the SEC has largely defined the scope of this practice on an ad hoc basis.

not been properly appointed for purposes of the Appointments Clause. Compl. ¶ 73. ALJ Murray ruled on pre-hearing motions, received substantial briefing, and presided over a week-long trial-like hearing at which witnesses testified and were cross-examined, documents were introduced, and objections were made and ruled on. *See id.* ¶¶ 73-75. One witness, however, was notably absent—Hull, who refused to testify after SEC officials misrepresented to him during an investigative interview that, while serving as the Fund's investment adviser, Gibson had personally taken a short position in TRX, essentially betting that the stock's price would decline. App. 106a; Compl. ¶¶ 64-70. This claim was patently untrue, and it pitted Hull against Gibson and his family for years. *See* App. 106a.

In January 2017, ALJ Murray issued an initial decision concluding that Gibson violated various provisions of the Securities Exchange Act, the Investment Advisers Act, and the rules thereunder. *In re Gibson*, Initial Decision Release No. 1106, 2017 WL 371868 (ALJ Jan. 25, 2017). ALJ Murray accordingly banned Gibson from the industry and ordered him to pay more than $292,000 in civil penalties and disgorgement. *Id.* at *36-42.

Gibson petitioned the Commission for review of ALJ Murray's decision, which the Commission granted in March 2017. *In re Gibson*, Exchange Act Release No. 80163, 2017 WL 1035744 (Mar. 6, 2017). Eighteen months later, the Commission vacated ALJ Murray's decision and all of the proceedings preceding it in light of this Court's decision in *Lucia*, which held that the remedy for an "adjudication tainted with an appointments violation" is a new

proceeding before a different and properly appointed official. 138 S. Ct. at 2055; *see* App. 14a-15a.

b. In October 2018—now more than seven years after the underlying trades occurred—the SEC served Gibson with a second OIP, identical to the first. Compl. ¶ 93. This time, Gibson's case was assigned to ALJ James Grimes. Like ALJ Murray, ALJ Grimes ordered pre-hearing proceedings, ruled on several motions, and then presided over a week-long hearing beginning in July 2019. *See* App. 15a. By this time, Hull had learned that Gibson had *not* taken a short position in TRX as the SEC staff had previously misrepresented, so he agreed to testify. *Id.* at 106a.

In March 2020, ALJ Grimes issued a lengthy initial decision concluding that Gibson violated various provisions of the Securities Exchange Act, the Investment Advisers Act, and the rules thereunder. *Id.* at 12a-112a. He summarily rejected Gibson's constitutional arguments, including his contention that "the tenure protections that apply to the Commission's administrative law judges violate the Constitution's separation of powers." *Id.* at 105a-109a. ALJ Grimes banned Gibson from the securities industry for at least three years and ordered him to pay more than $184,000 in civil penalties and disgorgement. *Id.* at 87a-104a, 109a-111a.

Gibson once again petitioned the Commission for review. The Commission granted the petition, *In re Gibson*, Exchange Act Release No. 88799, 2020 WL 2097824 (May 1, 2020), and the parties completed briefing in July 2020. The case remains pending before the Commission, which has given no indication that it intends to resolve Gibson's case anytime soon.

3. In 2019, while the administrative proceedings were underway, Gibson filed suit against the SEC in the District Court for the Northern District of Georgia. App. 7a. Relying on *Free Enterprise Fund*, Gibson sought declaratory and preliminary injunctive relief based on the constitutional deficiencies in the SEC's administrative proceedings. Compl. ¶¶ 96-112. As relevant here, Gibson claimed that SEC ALJs cannot preside over the proceedings because they are unconstitutionally insulated from removal by a multilayer for-cause structure analogous to the structure this Court held unconstitutional in *Free Enterprise Fund*. App. 7a-8a; *see* Compl. ¶ 112.

The district court denied Gibson's motion for a preliminary injunction and dismissed the case for lack of jurisdiction. App. 7a-10a. The court concluded that it was bound by the Eleventh Circuit's decision in *Hill v. SEC*, 825 F.3d 1236 (11th Cir. 2016), which held that, under *Thunder Basin*, the "statutory review scheme" provided in the securities laws "preclude[s] district court jurisdiction." App. 8a-9a (citing *Hill*, 825 F.3d at 1241, 1252).

4. The Eleventh Circuit affirmed. *Id.* at 1a-6a. Relying on its prior decision in *Hill*, the court "discerned no Congressional intention" for *not* forcing Gibson's constitutional separation-of-powers claim into "the SEC statutory scheme." *Id.* at 4a-6a. The court marched through the *Thunder Basin* factors, concluding that "meaningful judicial review" is available in the court of appeals after the administrative proceedings have run their course; that the SEC "may" have "expertise" in deciding "threshold issues" unrelated to the constitutional question; and that Gibson's challenge to the ALJ's authority is "'inextricably intertwined'" with the

administrative proceeding. *Id.* at 6a (citation omitted). The Eleventh Circuit denied Gibson's petition for rehearing en banc. *Id.* at 11a.

REASONS FOR GRANTING THE PETITION

This case presents a recurring question of exceptional importance concerning the right of individuals, like Gibson, to access a federal district court to vindicate a structural constitutional safeguard "'critical to preserving liberty.'" *Free Enter. Fund v. Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 501 (2010) (citation omitted). By holding that federal district courts have been impliedly stripped of their jurisdiction to enjoin SEC ALJs from unconstitutionally wielding their "extensive powers," *Lucia v. SEC*, 138 S. Ct. 2044, 2049 (2018), the decision below imposes unwarranted—and in many cases life-ruining—burdens on those individuals before they may ever present their challenges to an Article III court. That decision conflicts with decisions of this Court and opinions of several lower-court judges. And it improperly strips federal district courts of their statutorily granted jurisdiction to hear a critical class of structural constitutional claims based on untenable implications drawn from a general statutory scheme. Certiorari is warranted.

A. The Circuits Have Divested District Courts of Jurisdiction over an Important Class of Constitutional Claims

1. Congress granted federal district courts "original jurisdiction of all civil actions arising under the Constitution." 28 U.S.C. § 1331. This federal-question jurisdiction "'has long been recognized'" as a bulwark for "'protect[ing] rights safeguarded by the Constitution.'" *Free Enter. Fund*, 561 U.S. at 491 n.2

(citations omitted). And while Congress of course can, and occasionally does, "exclude[]" certain claims from the jurisdiction of federal district courts, it typically does so "expressly." *Verizon Md., Inc. v. Pub. Serv. Comm'n of Md.*, 535 U.S. 635, 644 (2002); *see also, e.g.*, *Shalala v. Illinois Council on Long Term Care, Inc.*, 529 U.S. 1, 5 (2000) ("explicitly"); *Board of Governors of the Fed. Reserve Sys. v. MCorp Fin., Inc.*, 502 U.S. 32, 44 (1991) ("clearly and directly").

This Court has held that, in certain instances, the provisions of an administrative review scheme may demonstrate that "Congress intended" for that scheme to be "exclusive," even if it does not "facially" eliminate federal-question jurisdiction. *Thunder Basin Coal Co. v. Reich*, 510 U.S. 200, 208, 212-16 (1994). But this kind of "implied" jurisdiction-stripping, *Elgin v. Department of Treasury*, 567 U.S. 1, 12 (2012), is "[g]enerally" confined to instances in which "'agency expertise [will] be brought to bear on particular problems,'" *Free Enter. Fund*, 561 U.S. at 489 (citation omitted). And every case in which this Court has found such implied jurisdiction-stripping involved challenges to the agency's decision, not to the constitutional legitimacy of the decisionmaker.

In *Thunder Basin*, for example, the Court held that an administrative review scheme impliedly precluded a pre-enforcement challenge brought by a mining company seeking to enjoin an order issued by the Mine Safety and Health Administration. 510 U.S. at 216. The company's challenge raised discrete, individualized claims that fell "squarely within the Commission's expertise" and could be "meaningfully addressed" in federal court after agency proceedings had concluded. *Id.* at 214-18 & n.22. Similarly, in *Elgin*, the Court held that the administrative review

scheme established by the Civil Service Reform Act (CSRA) impliedly precluded employees from "challeng[ing] an adverse employment action" in federal court on the ground "that [the applicable] federal statute is unconstitutional." 567 U.S. at 5. "'[A]t bottom,'" the case involved a "challenge to CSRA-covered employment action brought by CSRA-covered employees requesting relief that the CSRA routinely affords." *Id.* at 22-23 (citation omitted).

Under *Thunder Basin*, a statutory scheme does not impliedly strip district courts of "the jurisdiction that other statutes confer"—such as federal-question jurisdiction under 28 U.S.C. § 1331—"unless the 'statutory scheme' displays a 'fairly discernible' intent to limit jurisdiction, and the claims at issue 'are of the type Congress intended to be reviewed within th[e] statutory structure.'" *Free Enterprise Fund*, 561 U.S. at 489 (alteration in original) (quoting *Thunder Basin*, 510 U.S. at 207, 212). Moreover, courts must "presume that Congress does not intend to limit jurisdiction if 'a finding of preclusion could foreclose all meaningful judicial review'; if the suit is 'wholly collateral to a statute's review provisions'; and if the claims are 'outside the agency's expertise.'" *Id.* (quoting *Thunder Basin*, 510 U.S. at 212-13).

2. Lower-court judges have disagreed over whether Congress has impliedly stripped federal courts of jurisdiction over the structural constitutional claim at issue in this case—a challenge to the constitutional legitimacy of ALJs overseeing SEC administrative proceedings. Applying this Court's precedents, including the *Thunder Basin* framework, multiple judges have concluded that Congress has not done so. *See, e.g.*, *Cochran v. SEC*, — F.3d —, 2020 WL 4593226, at *8-9 (5th Cir. Aug.

11, 2020) (Haynes, J., dissenting in part); *Tilton v. SEC*, 824 F.3d 276, 292 (2d Cir. 2016) (Droney, J., dissenting), *cert. denied*, 137 S. Ct. 2187 (2017); *Duka v. SEC*, 103 F. Supp. 3d 382, 390 (S.D.N.Y. 2015) (Berman, J.); *Gray Fin. Grp., Inc. v. SEC*, 166 F. Supp. 3d 1335, 1343-44 (N.D. Ga. 2015) (May, J.), *vacated and remanded sub nom. Hill v. SEC*, 825 F.3d 1236 (11th Cir. 2016); *Ironridge Glob. IV, Ltd. v. SEC*, 146 F. Supp. 3d 1294, 1303-04 (N.D. Ga. 2015) (May, J.); *Hill v. SEC*, 114 F. Supp. 3d 1297, 1306 (N.D. Ga. 2015) (May, J.), *vacated and remanded*, 825 F.3d 1236 (11th Cir. 2016); *see also Gupta v. SEC*, 796 F. Supp. 2d 503, 512-13 (S.D.N.Y. 2011) (Rakoff, J.).

Nevertheless, five circuits have held—albeit over two strong dissenting opinions—that district courts have been impliedly stripped of their general federal-question jurisdiction to adjudicate claims challenging the constitutional legitimacy of SEC ALJs. *See Cochran*, 2020 WL 4593226, at *1 (5th Cir.); *Bennett v. SEC*, 844 F.3d 174, 188 (4th Cir. 2016); *Hill v. SEC*, 825 F.3d 1236, 1241 (11th Cir. 2016); *Tilton*, 824 F.3d at 291 (2d Cir.); *Bebo v. SEC*, 799 F.3d 765, 767 (7th Cir. 2015), *cert. denied*, 136 S. Ct. 1500 (2016).[4] These circuits hear the vast majority of the country's securities cases.[5] And under their rule, individuals

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[4] The D.C. Circuit reached the same conclusion in a case involving a constitutional "non-delegation challenge." *Jarkesy v. SEC*, 803 F.3d 9, 17-18 (D.C. Cir. 2015). *Jarkesy*, however, did not involve Article II appointments or removal claims challenging the authority of ALJs.

[5] *See* Admin. Office of U.S. Courts, Table B-7: U.S. Courts of Appeals—Civil and Criminal Appeals Commenced, by Cases and Nature of Suit or Offense, During the 12-Month Period Ending September 30, 2019 (2019), https://www.uscourts.gov/sites/default/files/data_tables/jb_b7_0930.2019.pdf.

ensnared in SEC enforcement proceedings helmed by unconstitutionally insulated federal officers have no recourse until the "unlawful administrative process has run its course"—no matter how "great [the] cost" financially, professionally, or personally. *Hill*, 825 F.3d at 1245. These often ruinous and unconstitutionally imposed consequences are deemed by these courts to be "'part of the social burden of living under government.'" *Bennett*, 844 F.3d at 185 (citation omitted); *see Tilton*, 824 F.3d at 285 ("financial and emotional costs" are "simply the price of participating in the American legal system").

Ordinarily, of course, this Court awaits a circuit conflict before granting review. But as explained below, the circuits' position squarely conflicts with this Court's own precedent. *See* Sup. Ct. R. 10(c). The fact that so many circuits have followed one another in committing this error is a reason for *granting*, not denying, review. Indeed, the courts have relied on the entrenched nature of this rule as a reason for hewing to it. *Cf. Cochran*, 2020 WL 4593226, at *6 n.9 (chiding the dissent for "taking the position that we should create a split with five other circuits"). This Court's intervention is needed. That is especially true because the prevailing rule in the circuits not only departs from this Court's precedent on a question of federal jurisdiction over a critical class of constitutional claims, but also exacts a harsh toll on individuals otherwise condemned to expensive and protracted proceedings before the very officials whom they claim lack constitutional authority. This state of affairs is "deeply concern[ing]" to say the least. *Cochran v. SEC*, No. 4:19-CV-066-A, 2019 WL 1359252, at *2 (N.D. Tex. Mar. 25, 2019), *aff'd*, 2020 WL 4593226 (5th Cir. Aug. 11, 2020).

This Court has granted certiorari in similar circumstances, despite the absence of a circuit split. *See, e.g.*, *Sackett v. EPA*, 566 U.S. 120 (2012); *see also Seila Law LLC v. CFPB*, 140 S. Ct. 2183 (2020); *Home Depot U.S.A., Inc. v. Jackson*, 139 S. Ct. 1743 (2019); *Bank of Am. Corp. v. City of Miami*, 137 S. Ct. 1296 (2017). It should do so here as well, before more circuits join the "parade [that] is marching in the wrong direction." *United States v. Smith*, 440 F.2d 521, 527 (7th Cir. 1971) (Stevens, J., dissenting).

B. The Circuits' Entrenched Jurisdiction-Stripping Rule for This Important Class of Structural Constitutional Claims Conflicts with This Court's Precedent

The entrenched jurisdiction-stripping rule in the circuits sharply conflicts with this Court's precedent.

1. As this Court has long stressed, federal courts have jurisdiction under 28 U.S.C. § 1331 "to issue injunctions to protect rights safeguarded by the Constitution." *Bell v. Hood*, 327 U.S. 678, 684 (1946). Federal-question jurisdiction serves as a bulwark against the deprivation of individual liberty and civil rights, ensuring that an immediate Article III tribunal stands ready to "'prevent[] [governmental] entities from acting unconstitutionally.'" *Free Enter. Fund*, 561 U.S. at 491 n.2 (citation omitted).

In *Free Enterprise Fund*, the Court held—in a portion of its opinion that elicited no dissent—that the same administrative review scheme at issue here (15 U.S.C. § 78y) did not "strip" district courts of that jurisdiction with respect to claims that the members of the Public Company Accounting Oversight Board were unconstitutionally insulated from removal. 561 U.S. at 489-91. As the Court explained, the "text [of

Section 78y] does not expressly limit [such] jurisdiction," "[n]or does it do so implicitly." *Id.* at 489. The Court thus rejected the Government's efforts to reimagine that scheme "as an exclusive route to review." *Id.* In doing so, the Court considered each of the *Thunder Basin* factors—the availability of "'meaningful judicial review,'" the claim's "'wholly collateral'" nature, and agency "'expertise'"—and concluded that they "point[ed] against any limitation on review" of the constitutional separation-of-powers claims at issue in that case. *Id.* at 489-91 (quoting *Thunder Basin*, 510 U.S. at 212-13).

As multiple judges—including judges on the Second and Fifth Circuits—have concluded, the Court's analysis in *Free Enterprise Fund* "controls here," and compels the conclusion that federal district courts have jurisdiction to hear challenges to the constitutional legitimacy of SEC ALJs. *Tilton*, 824 F.3d at 292 (Droney, J., dissenting); *see Cochran*, 2020 WL 4593226, at *9-10 (Haynes, J., dissenting in part). The Eleventh Circuit's contrary conclusion in this case directly conflicts with *Free Enterprise Fund*. At the same time, it erroneously extends *Thunder Basin*'s implied jurisdiction-stripping rule far beyond the circumstances presented in *Thunder Basin* and later cases applying it. The ever-deepening conflict with this Court's decisions warrants review.

2. Rather than follow *Free Enterprise Fund*, the circuits, including the Eleventh Circuit below, have tried to distinguish it based on their own application of the *Thunder Basin* factors. These efforts fail—and ultimately undermine the foundation for *Thunder Basin*'s jurisdiction-stripping rule.

a. In holding that federal district courts have been stripped of their jurisdiction over this class of

claims, these circuits have effectively converted *Thunder Basin*'s "meaningful judicial review" factor into a mere *possibility*-of-review test. *See* App. 6a; *see also, e.g.*, *Tilton*, 824 F.3d at 284 (claiming that this factor "turn[s] on the accessibility of post-proceeding review by a federal court of appeals—not on whether such review, if accessible, could adequately remedy the [constitutional] violation"). That is wrong.

In *Free Enterprise Fund*, this Court held that "'meaningful judicial review'" would not be possible absent district court jurisdiction because the plaintiffs were "object[ing] to the Board's *existence*, not to any of its auditing standards" or other actions. 561 U.S. at 489-90 (emphasis added) (citation omitted). Requiring the plaintiffs to submit to the authority of the very administrative body they challenged as unconstitutional in order to "win access to a court of appeals"—either by challenging a Board rule at random or by refusing to comply with a Board decree and seeking review of the resulting sanction—was not a "'meaningful' avenue of relief." *Id.* at 490-91 (quoting *Thunder Basin*, 510 U.S. at 212).

By contrast, the Eleventh Circuit below concluded that Gibson could "receive meaningful judicial review . . . in a court of appeals" *after* the conclusion of agency proceedings because that court could "vacate or set aside any adverse SEC order." App. 6a. But that review would not be *meaningful*. Gibson is not seeking judicial review of a specific adverse SEC order; instead, he is challenging the very legitimacy of the SEC decisionmaker presiding over his proceedings. Leaving Gibson "to await a final Commission order before [he] may assert [his] constitutional claim in a federal court means that by the time the day for judicial review comes, [he] will

have already suffered the injury that [he] is attempting to prevent." *Tilton*, 824 F.3d at 298 (Droney, J., dissenting). Judicial review at that point would not, in any practical sense, be "meaningful."[6]

This Court recently reached a similar conclusion in *Jennings v. Rodriguez*, 138 S. Ct. 830 (2018). There, the Court held that channeling a noncitizen detainee's "prolonged detention" claim into review of a final removal order would "depriv[e] that detainee of any *meaningful* chance for judicial review" because, "[b]y the time a final order of removal was eventually entered, the allegedly excessive detention would have already taken place." *Id.* at 840 (emphasis added). So too here. Depriving individuals of the opportunity to challenge the constitutional legitimacy of SEC ALJs in a federal district court, and instead delaying those challenges until review of a final agency order, likewise deprives those individuals of "any meaningful chance of judicial review" of those claims.

In addition, review in the courts of appeals is limited to parties "aggrieved" by a "final order of the Commission." 15 U.S.C. § 78y(a)(1). As a result, the vast number of individuals who simply cannot afford protracted agency proceedings and are forced to settle have no remedy at all for the discrete "'here-and-now' injury" they suffered by each and every "executive act that allegedly exceeds the official's authority." *Seila Law*, 140 S. Ct. at 2196 (citation omitted); *see Bond v. United States*, 564 U.S. 211, 222 (2011) ("[I]ndividuals

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[6] As one commentator explained, the circuits' "doctrinally dubious" reasoning on this *Thunder Basin* factor essentially "excises the 'meaningful' from 'meaningful judicial review.'" Adam M. Katz, Note, *Eventual Judicial Review*, 118 Colum. L. Rev. 1139, 1142-43, 1163-72, 1179-81 (2018).

sustain discrete, justiciable injury from actions that transgress separation-of-powers limitations.").

Like other circuits, the Eleventh Circuit has dismissed these harms by declaring that "[e]nduring an unwanted administrative process, even at great cost, does not amount to an irreparable injury on its own." *Hill*, 825 F.3d at 1245 (citing *FTC v. Standard Oil Co. of Cal.*, 449 U.S. 232, 244 (1980)); *accord, e.g.*, *Tilton*, 824 F.3d at 285-86; *Bebo*, 799 F.3d at 775. None of the circuits, however, has explained *how* these "great"—and unconstitutionally imposed—"cost[s]" are supposed to be recovered or are otherwise "reparable," particularly given that the remedy for the constitutional defect may well be simply *additional* costly agency proceedings. *Cf. Lucia*, 138 S. Ct. at 2055. And as Judge Droney explained in *Tilton*, *Standard Oil*'s considerations of "'irreparable injury'" say very little about the "meaningful judicial review" factor in any event. *Tilton*, 824 F.3d at 298-99 (Droney, J., dissenting) (citation omitted).

Indeed, the circuits' reliance on *Standard Oil*—a case about "final agency action," 449 U.S. at 238—is fundamentally misplaced. The plaintiff in *Standard Oil* did not challenge the constitutional authority of the adjudicator; rather, it challenged the legal sufficiency of the allegations in the agency's administrative complaint. *Id.* at 235. Any agency-imposed sanctions would not become effective "until judicial review [was] complete." *Id.* at 241. Thus, the plaintiff's only claimed injury was "the expense and disruption of defending itself in protracted adjudicatory proceedings," which for a massive corporation had no "practical effect upon [its] daily business other than the disruptions that accompany any major litigation." *Id.* at 243-44.

For individuals subject to SEC proceedings, however, far "more is at stake." *Cochran*, 2020 WL 4593226, at *10 (Haynes, J., dissenting in part). Virtually every ruling an ALJ makes can impact how a case proceeds—and its ultimate outcome. Moreover, the harms suffered by individuals having to appear before an unconstitutionally insulated ALJ extend well beyond mere litigation expenses, and those harms are not suspended pending judicial review. For example, an ALJ has the power to impose a bar on securities-industry employment—"'the securities industry equivalent of capital punishment.'" *Saad v. SEC*, 718 F.3d 904, 906 (D.C. Cir. 2013) (citation omitted). This bar, initially imposed by an officer acting unconstitutionally, will remain in place during the pendency of any review. *See* 15 U.S.C. § 80b-13(b). The same goes for monetary sanctions—individuals like Gibson must pay monetary sanctions imposed against them *before* they can make it to an Article III court.[7]

For Gibson, that means that, should the Commission ultimately affirm the ALJ's decision against him, he will be barred from the industry and have to come up with more than $184,000 before he can ever present his constitutional claim to a federal court. This pay-now-review-later regime stands in stark contrast not only to *Standard Oil*, *see supra* at

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[7] Although a party facing an adverse ruling can seek a stay pending judicial review, *see* 5 U.S.C. § 705; 15 U.S.C. §§ 78y(c)(2), 80b-13(b), the SEC and the courts generally insist that the "financial losses" caused by these sanctions do not warrant a stay. *In re Clifton*, Exchange Act Release No. 70639, 2013 WL 5553865, at *4 & n.27 (Oct. 9, 2013) (citing *Wisconsin Gas Co. v. FERC*, 758 F.2d 669, 674 (D.C. Cir. 1985)); *see Associated Sec. Corp. v. SEC*, 283 F.2d 773, 775 (10th Cir. 1960).

23, but also to *Thunder Basin* itself, where meaningful review was available because the agency's "penalty assessments became final and payable only *after* full review by both the Commission *and the appropriate court of appeals*." 510 U.S. at 218 (emphasis added). This difference alone should be dispositive.

The *possibility* of some judicial review after the SEC proceedings eventually have run their course "cannot be considered truly 'meaningful' at that point," because it cannot stop, or even remedy after the fact, many of the life-ruining harms imposed by the proceedings themselves. *Tilton*, 824 F.3d at 298 (Droney, J., dissenting). In this situation, review delayed is, for all practical purposes, review denied.

b. In holding that federal district courts lack jurisdiction to hear freestanding challenges to the constitutional legitimacy of ALJs, the circuits have also "stripped [*Thunder Basin*'s] 'wholly collateral' and 'outside the agency's expertise' factors of any significance." *Id.* at 292 (Droney, J., dissenting).

In *Free Enterprise Fund*, the Court held that the separation-of-powers claim at issue was "collateral to any Commission orders or rules" because it was a "general challenge to the Board" itself. 561 U.S. at 490. The claim was also plainly "outside the Commission's competence and expertise" because it implicated "standard questions of administrative [and constitutional] law," requiring no "agency fact-bound inquiries" or "'technical considerations of [agency] policy.'" *Id.* at 491 (alteration in original) (citation omitted). Given that the separation-of-powers claim at issue here is identical to the one raised in *Free Enterprise Fund*, the Court's analysis in that case should control.

Nevertheless, lower courts have circumvented this Court's precedent in two ways. First, some circuits have discounted or discarded these factors, candidly concluding that an administrative review scheme can foreclose federal court jurisdiction even when the claim "can reasonably be characterized as 'wholly collateral' to the statute's review provisions and outside the agency's expertise." *Bebo*, 799 F.3d at 767; *see Hill*, 825 F.3d at 1245, 1250 ("briefly" considering these factors before declaring that they "do not cut strongly either way").

Dispensing with these two factors, however, blatantly contravenes this Court's decisions. In both *Thunder Basin* and *Elgin*, *all three* factors supported jurisdiction stripping. And as the three-Justice dissent in *Elgin* explained (without dispute from the majority), *Thunder Basin* "emphasized *two* important factors"—the "agency's expertise" and "wholly collateral" factors. 567 U.S. at 26 (Alito, J., joined by Ginsburg and Kagan, JJ., dissenting) (emphasis added). The possibility of judicial review in the future "is not the only consideration." *Id.* at 33. For these circuits, however, it is just that.

Second, other courts, including the Eleventh Circuit in this case, have held that, notwithstanding *Free Enterprise Fund*, these factors somehow *support* channeling separation-of-powers challenges into administrative proceedings. This, too, contravenes this Court's decisions as well as common sense.

Regarding the "wholly collateral" factor, these courts have held that a separation-of-powers claim challenging the authority of ALJs is not collateral because it is "'intertwined with the conduct of the very enforcement proceeding the statute grants the SEC the power to institute and resolve as an initial

matter.'" App. 6a (citation omitted); *see Tilton*, 824 F.3d at 287-88. But no amount of "intertwining" can give the SEC the authority to resolve the separation-of-powers claim in Gibson's favor. Far from "requesting relief that [the decisionmaker] routinely affords," *Elgin*, 567 U.S. at 22, Gibson's separation-of-powers claim "has no relation to the securities laws entrusted to the SEC and the requested remedy of disallowing the proceedings before the ALJ is obviously not a routine outcome," *Tilton*, 824 F.3d at 295 (Droney, J., dissenting). Thus, just as in *Free Enterprise Fund*, Gibson's "general challenge" to the constitutional authority of ALJs is wholly "collateral." 561 U.S. at 490; *see also McNary v. Haitian Refugee Ctr., Inc.*, 498 U.S. 479, 492, 497-98 (1991) (holding that an administrative scheme did not preclude federal jurisdiction by emphasizing the "critical difference" between challenges to individualized agency determinations an "general collateral challenges to unconstitutional practices and policies used by the agency").[8]

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[8] Some courts have analogized this extreme situation to having to wait for a final court judgment before filing an appeal. *Tilton*, 824 F.3d at 285; *see Cochran*, 2020 WL 4593226, at *7. Gone here is any pretense of ascertaining what "Congress intended" with respect to "*this* statutory structure." *Thunder Basin*, 510 U.S. at 212 (emphasis added). Moreover, the analogy is obviously inapt. A party waiting to appeal a final decision from a federal district court has already enjoyed what Gibson lacks—an Article III decisionmaker who is, without question, constitutionally authorized to take actions against individuals in the first place. The separation-of-powers claim here, by contrast, "transcends any particular proceeding" and instead challenges the very "'existence'" of the adjudicators "within their current structure." *Cochran*, 2020 WL 4593226, at *10 (Haynes, J., dissenting in part) (quoting *Free Enter. Fund*, 561 U.S. at 490).

The circuits have similarly negated the "agency expertise" factor. *Free Enterprise Fund* held in no uncertain terms that a separation-of-powers challenge to a regulator's authority is a "constitutional claim[]" that is "outside the Commission's competence and expertise." 561 U.S. at 491. Nevertheless, the court below claimed that this factor supports preclusion because the SEC might have expertise in resolving *other* issues unrelated to the constitutional claim. App. 6a; *accord Bennett*, 844 F.3d at 187.[9] Asking about the SEC's expertise in possibly deciding unrelated issues, of course, says nothing about whether the agency is competent to resolve *this* issue challenging the constitutional structure of the administrative scheme itself—especially where this Court has already held the agency lacks competence to hear it.

Faced with this disconnect, some lower courts have reasoned that this Court's decision in *Elgin* effectively abrogated *Free Enterprise Fund*'s analysis. *See Cochran*, 2020 WL 4593226, at *6; *Bennett*, 844 F.3d at 187. But this Court has admonished against such secondhand overrulings by lower courts, stressing that lower courts must follow the decision that "directly controls" until expressly overruled by this Court. *Rodriguez de Quijas v. Shearson/Am. Exp., Inc.*, 490 U.S. 477, 484 (1989). Here, the directly controlling decision is *Free Enterprise Fund*.

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[9] Although this logic assumes that there *are* other unrelated issues for the agency to resolve, the lower courts have not felt constrained by that logic. *See Bennett*, 844 F.3d at 187-88 & n.15 (speculating that the SEC might use its "expertise" to "fully dispos[e]" of the case in the individual's favor even where the individual had "eschewed all . . . defenses" in the proceeding itself).

Besides, there is no basis for concluding that *Elgin* abrogated *Free Enterprise Fund*. Indeed, *Elgin* did not even mention *Free Enterprise Fund* in discussing agency expertise, and "[t]his Court does not normally overturn, or so dramatically limit, earlier authority *sub silentio*." *Illinois Council*, 529 U.S. at 18. *Elgin* involved an instance in which the agency could "apply its expertise" to resolve "threshold questions" that "accompan[ied] [the] constitutional claim," such as whether the allegedly unconstitutional statute applied to the claimant at all. 567 U.S. at 22.

Reading *Elgin* as broadly as these courts do "would mean that as long as a proceeding is ongoing, the 'outside the agency's expertise' factor *must* weigh against jurisdiction—because any time a proceeding has commenced there is of course some possibility that a plaintiff may prevail on the merits." *Tilton*, 824 F.3d at 296 (Droney, J., dissenting) (emphasis added). There is no basis to believe *Elgin* intended such a radical expansion of *Thunder Basin*'s narrowly tailored "agency expertise" analysis. At a minimum, the confusion underscores that the lower courts need "further guidance from [this] Court" on this important issue. *Id.* at 288 (majority opinion).

3. The circuits' application of *Thunder Basin* to separation-of-powers claims undermines the doctrinal foundation for *Thunder Basin* itself. Stripping federal courts of their statutorily granted jurisdiction based on implications of what "Congress intended" in enacting general statutory schemes, 510 U.S. at 212, already fits uncomfortably with this Court's usual reluctance to engage in "'speculation about what Congress might have' intended," *Wisconsin Cent. Ltd. v. United States*, 138 S. Ct. 2067, 2073 (2018) (citation omitted). Implied jurisdiction-

stripping is also in tension with "the 'stron[g] presump[tion]' that . . . 'Congress will specifically address' preexisting law when it wishes to suspend its normal operations in a later statute." *Epic Sys. Corp. v. Lewis*, 138 S. Ct. 1612, 1624 (2018) (alterations in original) (citation omitted); *cf., e.g.*, *Illinois Council*, 529 U.S. at 10 (statute expressly provided that "'[n]o action . . . shall be brought under section 1331'" (alteration in original) (citation omitted)).

But in the circuits that have barred jurisdiction over separation-of-powers claims, the *Thunder Basin* factors have taken on a life of their own, divorced from any conventional statutory analysis of Congress's intent. Indeed, it makes little sense to even ask whether the "claim[] [is] of the type Congress intended to be reviewed *within* this statutory structure," *Thunder Basin*, 510 U.S. at 212 (emphasis added), when the claim is challenging the constitutionality of the statutory structure itself. And, notably, in *Thunder Basin*, the "petitioner expressly disavow[ed] any abstract challenge to the Mine Act's statutory review scheme." *Id.* at 218 n.22. So the circuits flip *Thunder Basin* and insist instead on proof that the claim is of the type "Congress intended to *exempt* from the statutory review scheme." *Hill*, 825 F.3d at 1245 (emphasis added). In effect, this creates a presumption *against* jurisdiction, which has no basis in *Thunder Basin*.

The circuits have also glossed over fundamental differences between the separation-of-powers challenge at issue here and other constitutional and non-constitutional claims in a way that will "cause crucial collateral claims to be lost and potentially irreparable injuries to be suffered." *Mathews v. Eldridge*, 424 U.S. 319, 331 n.11 (1976). Gibson is

seeking to challenge the authority of the agency decisionmaker within the administrative scheme to take *any* action against him. *Each action* taken by an unconstitutionally insulated ALJ "is an executive act that allegedly exceeds the official's authority" and "inflicts a 'here-and-now' injury." *Seila Law*, 140 S. Ct. at 2196; *see Bond*, 564 U.S. at 222. Those injuries are irreparable; no amount of post-agency relief can erase them. And the actions and findings made by a constitutionally illegitimate decisionmaker have a snowballing effect as the case proceeds.

Moreover, forcing these structural constitutional challenges into agency review means that litigants who raise such challenges must raise them before the very decisionmaker whom they contend lacks constitutional legitimacy. Given that this same decisionmaker will "issue an opinion complete with factual findings, legal conclusions, and sanctions" in their cases, litigants face enormous pressure to "stay in line" and not challenge ALJs' authority or "resist [their] order[s]." *Lucia*, 138 S. Ct. at 2054.

All this explains why several judges have concluded that *Thunder Basin* cannot be extended to strip federal courts of their jurisdiction over the first-order constitutional claim at issue here. But because the circuits in lockstep have done precisely that, this Court's review is necessary.

C. The Enormous Practical Importance of the Question Presented Underscores the Need for This Court's Review

The question presented not only is recurring, but also has vital importance to the hundreds of individuals forced each year to defend themselves in SEC administrative proceedings.

The fact that so many circuits—including those hearing the lion's share of securities enforcement actions—have already weighed in on this issue underscores its national significance. That will not subside. Since Dodd-Frank expanded the SEC's ability to try cases before its in-house administrative tribunal, the SEC has brought the vast majority of its enforcement actions before its own ALJs, where it enjoys a home-court advantage. *See supra* at 4-6. As a result, individuals like Gibson are currently forced to litigate for years in a distinctly hostile forum, at great expense, before they can challenge the constitutional legitimacy of the decisionmaker presiding over their agency proceeding. This regime exacts an enormous personal and financial toll before they can ever present their constitutional claim to a federal court. *See Tilton*, 824 F.3d at 298 n.5 (Droney, J., dissenting). And the SEC has exploited this vulnerability in "'a number of cases'" by "'threaten[ing] administrative proceedings'" before its ALJs in a calculated effort to compel a settlement. *Id.* (citation omitted).[10]

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[10] The fact that Gibson's case is now before the Commission does not obviate the need for this Court's review. First, if this Court grants review and reverses, then this case will return to the district court for it to decide how to proceed. But importantly, the Court will have established that federal-question jurisdiction exists over this important class of constitutional claims. Second, because of the glacial pace of cases before the Commission, it still may be a year or more before Gibson could appeal any final agency decision to a federal court. Third, if Gibson prevails before the Commission on the merits, he very well may be right back before an unconstitutionally insulated ALJ—for a third time. Fourth, requiring Gibson to present his constitutional claim to a federal court of appeals in the first instance on review from an SEC decision would deprive

Stripping courts of jurisdiction to hear separation-of-powers claims will allow these unconstitutional officers to wield their expansive powers for years before they can be stopped. Indeed, this Court expressly acknowledged, but declined to "address," the constitutionality of ALJs' insulation from removal ten years ago in *Free Enterprise Fund*, 561 U.S. at 507 n.10. And yet, in the decade since that decision came down, the issue has not been addressed by a single court of appeals. Even the Government, which itself has acknowledged the constitutional concerns created by the ALJs' dual-layered protections from removal, has lamented that the lack of a resolution on this "critical[]" issue has produced "uncertainty and turmoil" for the agency as well as litigants. Gov't Cert. Resp. 20-21, *Lucia*, 138 S. Ct. 2044 (No. 17-130). Denying review will only continue to thwart the resolution of this issue, unnecessarily perpetuating the SEC's systematic violation of a structural safeguard that "'[t]he Framers recognized'" as "'critical to preserving liberty.'" *Free Enter. Fund*, 561 U.S. at 501 (alteration in original) (citation omitted).

A recurring jurisdictional question of this magnitude, on which federal judges have strongly disagreed, warrants resolution by this Court. Federal jurisdiction has long served as a critical protection for individual rights and liberties. Jurisdiction has been

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Gibson of the full benefit of federal-question jurisdiction—including the opportunity to develop his claim and obtain a ruling from a federal district court. Finally, even apart from the impact on Gibson's case, this Court's guidance is needed on the question presented given the numerous individuals in Gibson's situation. There is no reason for this Court to wait any longer to decide the important question presented. The issue is squarely raised in this case and, if granted, may be resolved this Term.

denied for too long over the critical class of structural constitutional claims at issue in this case. If this Court believed the circuits would straighten this out on their own when it denied certiorari in *Tilton*, experience has proven otherwise. While the chorus of dissenting views has grown since then, the circuits have only grown more entrenched in their misreading of this Court's precedent. Only this Court can right this wrong—and this case presents an ideal vehicle in which to resolve this issue this Term.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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August 31, 2020

APPENDIX

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IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

No. 19-11969
Non-Argument Calendar

D.C. Docket No. 1:19-cv-01014-WMR

CHRISTOPHER M. GIBSON,

Plaintiff - Appellant,

versus

SECURITIES AND EXCHANGE COMMISSION,
CHAIRMAN OF THE SECURITIES AND
EXCHANGE COMMISSION,
UNITED STATES ATTORNEY GENERAL,

Defendants - Appellees.

Appeal from the United States District Court
for the Northern District of Georgia

(December 30, 2019)

Before WILSON, ANDERSON and DUBINA, Circuit Judges.

PER CURIAM:

Appellant, Christopher M. Gibson, appeals the district court's order denying his motion for preliminary injunctive relief, requesting that the district court preliminarily enjoin, based on constitutional grounds, the Securities and Exchange Commission ("SEC") from continuing an administrative proceeding against him. Relying on circuit precedent, the district court determined that it lacked subject matter jurisdiction over the case,

denied the request for injunctive relief, and dismissed Gibson's complaint in its entirety. After reviewing the record and reading the parties' briefs, we affirm the district court's order.

I. BACKGROUND

In 2016, the SEC instituted an administrative enforcement proceeding against Gibson to determine whether he had violated the Securities and Exchange Act by acting as an investment adviser to a private pooled investment fund. The allegation was that in his role, Gibson had "engaged in a deceptive scheme to front-run [the Fund's] trades and benefit himself and those close to him at the expense of the Fund and his other clients by exploiting the investment advice he provided to the Fund." *See* Order Instituting Administrative and Cease-and-Desist Proceedings, at 9 (SEC Mar. 29, 2016) (Violations E. 54.), https://go.usa.gov/xVA7g. An Administrative Law Judge ("ALJ") held a hearing and issued an initial decision adverse to Gibson. The SEC granted Gibson's request to review that initial decision and ordered merits briefing. While Gibson's case was pending, the United States Solicitor General submitted a brief in the Supreme Court in *Lucia v. SEC*, No. 17-130, agreeing with the petitioner's argument that the ALJ's are inferior officers under the Appointments Clause who must be appointed by the President, a Court of Law, or the Head of a Department, such as the SEC. Because of this brief, the SEC issued an order that ratified the previous appointments of its ALJs and remanded all pending administrative proceedings, including Gibson's case, to its ALJs. The ALJ assigned to Gibson's case ratified her earlier decision, and Gibson petitioned for SEC review.

While Gibson's petition for review was pending, the Supreme Court issued its decision in *Lucia v. SEC*, ___ U.S. ___, 138 S. Ct. 2044 (2018), holding that the SEC's ALJs were inferior officers who had not been properly appointed at the time of petitioner's administrative proceeding. The Court's remedy was a remand to the agency for a new hearing before a properly appointed officer; however, the properly appointed officer could not be the same officer who previously heard the case. *Id.* at ___, 138 S. Ct. at 2055. Hence, the SEC remanded Gibson's case for a new hearing before a different, properly appointed, ALJ.

Gibson filed an answer and raised several objections to the administrative proceedings, such as (1) the proceedings violated the separation of powers, (2) the statutory restrictions on removing the SEC's ALJs violated Article II, (3) the SEC's ALJs had not been properly appointed, (4) the proceedings were based on an impermissible delegation of legislative authority, (5) the proceedings violated his due process rights, (6) the proceedings violated his equal protection rights, (7) the proceedings violated his right to a jury trial, (8) the statute of limitations had run, and (9) the proceedings were barred by laches. The ALJ held proceedings in July and August 2019, took the case under advisement, but has not issued an initial decision.

While these administrative proceedings were underway, Gibson sued in the district court to enjoin these proceedings. Gibson raised in the district court many of the same claims he raised in his administrative proceeding. The district court dismissed the complaint for lack of jurisdiction based on our court's holding in *Hill v. SEC*, 825 F.3d 1236,

1237 (11th Cir. 2016), which construed the judicial review provisions of the Securities and Exchange Act, 15 U.S.C. § 78y. The district court also denied Gibson's motion for preliminary injunctive relief.

II. DISCUSSION

On appeal, Gibson primarily challenges the district court's reliance on our *Hill* decision by attempting to distinguish his case from the *Hill* case. He also argues that the SEC administrative proceedings deny him his Seventh Amendment right to a jury trial, that the district court should exercise its jurisdiction to consider whether the SEC proceedings are now barred by the statute of limitations, and that his due process claims can only be determined by the district court. We are unpersuaded by Gibson's arguments.

We review *de novo* the district court's determination of subject matter jurisdiction. *Hill*, 825 F.3d at 1240. We note that federal district courts generally have jurisdiction over claims that seek declaratory and injunctive relief based on constitutional violations. *See* 28 U.S.C. §§ 1331, 2201. However, Congress may allocate to an administrative body the initial review of such claims, and when it does, the court must undertake the analysis set forth in *Thunder Basin Coal Co. v. Reich*, 510 U.S. 200, 114 S. Ct. 771 (1994).

In *Hill*, we employed the framework established in *Thunder Basin* to examine whether Congress allocated initial review of claims raising constitutional challenges that seek declaratory and injunctive relief to the SEC's administrative process. *Hill*, 825 F.3d at 1241. We first decided whether Congress's intent to preclude initial review in the

district court is "fairly discernible in the statutory scheme." *Id.* (quoting *Thunder Basin*, 510 U.S. at 207, 114 S. Ct. at 776). We then considered whether the respondents' claims were "of the type Congress intended to be reviewed within this statutory structure." *Id.* (quoting *Thunder Basin*, 510 U.S. at 212, 114 S. Ct. at 779). We also examined whether the respondents' claims would receive meaningful judicial review within the statutory structure. Lastly, we questioned whether "agency expertise could be brought to bear on the . . . questions presented" and the extent to which the litigants' claims are "wholly collateral to [the] statute's review provisions." *Id.* (quoting *Thunder Basin*, 510 U.S. at 212, 214–15, 114 S. Ct. at 780). Applying this framework, we concluded that the respondents' claims had to proceed initially in the administrative forum and then through the judicial review scheme enacted by Congress in 15 U.S.C. § 78y. *Id.*

As our court noted, Congress authorized the SEC to bring civil actions to enforce violations of the Securities and Exchange Act in either federal district court or in an administrative proceeding before the SEC. *Id.* at 1237 (citing 15 U.S.C. § § 78u(d), 78u-1, 78u-2, 78u-3). "An SEC administrative enforcement action culminates in a final order of the Commission, which in turn is reviewable exclusively by the appropriate federal court of appeals." *Id.* (citing 15 U.S.C. § 78y). We concluded that respondents in an SEC administrative enforcement action could not bypass the Exchange Act's review scheme by filing a collateral lawsuit in federal district court challenging the administrative proceedings on constitutional grounds. *See id.* at 1243. Because we discerned no Congressional intention to exempt the type of claims

the respondents raised from the review process Congress created, we vacated the district court's preliminary injunction orders and remanded to the district court with instructions to dismiss the actions for lack of jurisdiction. *Id.* at 1252.

Like the district court, we conclude that *Hill* controls in this case. Gibson can receive meaningful judicial review of his claims in a court of appeals, and if the appellate court finds merit in any of his claims, it may vacate or set aside any adverse SEC order. Moreover, the SEC may bring its expertise to bear on Gibson's claims because it will necessarily have to decide threshold issues, such as whether Gibson has violated the securities laws or whether the statute of limitations has expired. Further, Gibson's constitutional and statutory claims are "inextricably intertwined with the conduct of the very enforcement proceeding the statute grants the SEC the power to institute and resolve as an initial matter." *Jarkesy v. SEC*, 803 F.3d 9, 23 (D.C. Cir. 2015). Accordingly, we conclude that because Gibson cannot bypass the SEC statutory scheme by filing a collateral action in federal district court, the district court properly dismissed his action for lack of jurisdiction. Moreover, we find no merit to the other arguments raised by Gibson on appeal.

AFFIRMED.

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

CHRISTOPHER M. GIBSON, PLAINTIFF, *v.* SECURITIES AND EXCHANGE COMMISSION, ET AL., DEFENDANTS.	Civil Action No. 1:19-cv-01014-WMR

ORDER DENYING PLAINTIFF'S
MOTION FOR PRELIMINARY INJUNCTION

This case comes before the Court on Plaintiff's Complaint [Doc. 1] and Motion for Preliminary Injunction [Doc. 4]. After due consideration and a hearing on Plaintiff's Motion for Preliminary Injunction, the Court enters the following Order:

I. BACKGROUND

On March 4, 2019, Plaintiff Christopher M. Gibson filed the Complaint [Doc. 1] along with a Motion for Preliminary Injunction and Request for Expedited Hearing [Doc. 4], requesting that the Court preliminarily enjoin the Securities and Exchange Commission ("SEC") from continuing an administrative proceeding against him on constitutional grounds. Plaintiff primarily raises four claims against Defendants: (1) that SEC staff violated his due-process rights by making misrepresentations regarding Plaintiff having maintained a short position in certain securities;

(2) that the removal protections of the Administrative Law Judge ("ALJ") presiding over the administrative proceeding unconstitutionally infringe upon the President's control over officers of the United States; (3) that the Order Instituting Proceedings ("OIP") that the SEC issued to Plaintiff was invalid and therefore the current proceeding is barred by the five-year statute of limitations contained in 28 U.S.C. § 2462; and (4) that the administrative proceeding deprives Plaintiff of his Seventh Amendment right to trial by jury. On March 22, 2019, Defendants filed their Response in Opposition to Plaintiff's Motion [Doc. 9]. On April 8, 2019, the Court held oral argument on the Motion.

II. LEGAL STANDARD

"A preliminary injunction is an extraordinary and drastic remedy not to be granted unless the movant clearly establishes the 'burden of persuasion' as to the four requisites." *All Care Nursing Serv., Inc. v. Bethesda Mem'l Hosp., Inc.*, 887 F.2d 1535, 1537 (11th Cir. 1989) (quoting *United States v. Jefferson Cty.*, 720 F.2d 1511, 1519 (11th Cir. 1983)). To obtain such relief, Plaintiff must show "(1) a substantial likelihood of success on the merits; (2) that irreparable injury will be suffered unless the injunction issues; (3) that the threatened injury to the movant outweighs whatever damage the proposed injunction may cause the opposing party, and (4) that if issued the injunction would not be adverse to the public interest." *Id.*

III. DISCUSSION

In *Hill v. SEC*, 825 F.3d 1236 (11th Cir. 2016), the Eleventh Circuit considered whether a respondent in a SEC enforcement action could bypass the

administrative scheme of the federal securities laws by filing a district-court lawsuit raising constitutional challenges to the administrative proceeding. Applying the framework laid out by the Supreme Court in *Thunder Basin Coal Co. v. Reich*, 510 U.S. 200 (1994), the *Hill* court concluded that the statutory review scheme of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78y, precluded district court jurisdiction over the plaintiffs' claims. *Hill*, 825 F.3d at 1241, 1252. Analyzing the considerations articulated in *Thunder Basin*, the Eleventh Circuit concluded that it was "'fairly discernible' from the review scheme [of the Exchange Act] that Congress intended the respondents' claims to be resolved first in the administrative forum, not the district court, and then, if necessary, on appeal to the appropriate federal court of appeals." *Id.* at 1237. Accordingly, the *Hill* court vacated the district court's preliminary-injunction orders and remanded with instructions to dismiss the case for lack of subject-matter jurisdiction. *Id.*

The Court finds that *Hill* governs here. Thus, the Court concludes that it lacks subject-matter jurisdiction over this case, and, accordingly, that Plaintiff cannot show a substantial likelihood of success on the merits.

IV. CONCLUSION

For the reasons discussed herein and at the April 8, 2019, hearing on this matter, the Court hereby ORDERS that Plaintiff's Motion for Preliminary Injunction is DENIED. Further, in light of the Court's determination that it lacks subject-matter jurisdiction, the Court ORDERS that the Complaint

be DISMISSED in its entirety pursuant to Federal Rule of Civil Procedure 12(h)(3).

SO ORDERED, this 8th day of May, 2019.

s/ William M. Ray II
WILLIAM M. RAY, II
United States District Court Judge
Northern District of Georgia

IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

No. 19-11969-AA

CHRISTOPHER M. GIBSON,

Plaintiff - Appellant,

versus

SECURITIES AND EXCHANGE COMMISSION,
CHAIRMAN OF THE SECURITIES AND
EXCHANGE COMMISSION,
UNITED STATES ATTORNEY GENERAL,

Defendants - Appellees.

Appeal from the United States District Court
for the Northern District of Georgia

[April 1, 2020]

ON PETITION(S) FOR REHEARING AND
PETITION(S) FOR REHEARING EN BANC

BEFORE: WILSON, ANDERSON, and DUBINA, Circuit Judges.

PER CURIAM:

The Petition for Rehearing En Banc is DENIED, no judge in regular active service on the Court having requested that the Court be polled on rehearing en banc. (FRAP 35) The Petition for Rehearing En Banc is also treated as a Petition for Rehearing before the panel and is DENIED. (FRAP 35, IOP2)

Initial Decision Release No. 1398
Administrative Proceeding
File No. 3-17184

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

In the Matter of **Christopher M. Gibson**	**Initial Decision** March 24, 2020

Appearances:	Nicholas C. Margida, Gregory R. Bockin, George J. Bagnall, and Paul J. Bohr for the Division of Enforcement, Securities and Exchange Commission
	Thomas A. Ferrigno, Stephen J. Crimmins, and Elizabeth L. Davis, Murphy & McGonigle PC, and David E. Hudson, Hull Barrett PC, for Respondent
Before:	James E. Grimes, Administrative Law Judge

Summary

Christopher M. Gibson was an investment adviser to Geier International Strategies Fund, LLC (the Fund), that had invested virtually all its assets in a single security, the common stock of Tanzanian Royalty Exploration Corporation (TRX). The Division of Enforcement alleges that Gibson engaged in three

courses of conduct that breached his fiduciary duties to his client fund and created undisclosed conflicts of interest, in violation of the antifraud provisions of the Investment Advisers Act of 1940, the Securities Exchange Act of 1934, and rules under those Acts.

First, Gibson engaged in a practice known as front running. The day before he executed a large block sale of the Fund's position in TRX, he sold all the TRX shares in his personal brokerage account and two other accounts he controlled. Gibson did this while actively seeking to sell the Fund's position in TRX.

Second, Gibson caused the Fund to buy a large block of additional TRX shares from the Fund's majority owner in a private transaction. He later sold those shares with the Fund's remaining shares in a market transaction. Gibson operated under a conflict of interest when he executed this transaction; the investor effectively paid Gibson's salary, and Gibson owed him a substantial debt at the time.

Third, Gibson engaged in another instance of front running. He bought put options in TRX for himself and his then-girlfriend, and he advised his father to do the same, while knowing that the fund sought to sell its remaining TRX shares. He then sold the Fund's remaining TRX shares before the expiration date of the personal put contracts. This sale caused a drop in TRX's share price. Gibson, his girlfriend, and his father exercised their put options the same day.

The evidence establishes that Gibson recklessly breached his fiduciary duties and failed to either eliminate or disclose conflicts of interest. I therefore find that Gibson violated Advisers Act Section 206(1),

(2), and (4) and Rule 206(4)-8, and Exchange Act Section 10(b) and Rule 10b-5(a) and (c).[1]

For sanctions, I order Gibson to cease and desist from further violations of the securities laws he violated; prohibit Gibson from the activities listed in Section 9(b) of the Investment Company Act of 1940 and bar him from the securities industry under Advisers Act Section 203(f), with the right to reapply for reentry after three years for both sanctions; order disgorgement of $82,088.81 plus prejudgment interest; and impose second-tier civil penalties totaling $102,000.

Procedural Background

The Commission initiated this proceeding in March 2016 with an order instituting proceedings (OIP) under Exchange Act Section 21C, Advisers Act Section 203(f) and (k), and Investment Company Act Section 9(b).[2] The OIP alleges that Gibson committed securities fraud through the three instances of conduct summarized above.

An administrative law judge held a hearing in 2016 and issued an initial decision in 2017.[3] In August 2018, following the Supreme Court's decision in *Lucia v. SEC*, the Commission remanded this proceeding, ordered that it be reassigned to an administrative law judge who had not previously

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[1] 15 U.S.C. §§ 78j(b), 80b-6(1), (2), (4); 17 C.F.R. §§ 240.10b-5,275.206(4)-8.

[2] 15 U.S.C. §§ 78u-3, 80a-9(b), 80b-3(f), (k).

[3] *Christopher M. Gibson*, Initial Decision Release No. 1106, 2017 WL 371868 (ALJ Jan. 25, 2017).

participated in the matter, and directed that Gibson be given the opportunity for a new hearing.[4]

I held a one-week hearing in July and August 2019. Post-hearing briefing concluded in October 2019.

The parties stipulated that nine affirmative defenses raised by Gibson alleging constitutional infirmities in this proceeding are preserved for Commission review.[5] I briefly discuss aspects of these constitutional claims at the end of the decision to put matters in context.

In conducting this proceeding, I gave no weight to the opinions, orders, or rulings of the administrative law judge who presided over this proceeding before the Commission's remand.[6]

Motions to Strike

I previously reserved ruling on two motions to strike, one filed by the Division and the other by Gibson. I now DENY both.

The Division asks me to strike all portions of Gibson's proposed findings of fact and conclusions of law containing argument, citing my post-hearing order indicating that I would do so.[7] In this instance,

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[4] *Pending Admin. Proc.*, Securities Act of 1933 Release No. 10536, 2018 WL 4003609, at *1, *4 (Aug. 22, 2018); *see also Lucia v. SEC*, 138 S. Ct. 2044 (2018).

[5] *Gibson*, Admin. Proc. Rulings Release No. 6668, 2019 SEC LEXIS 2319 (ALJ Aug. 29, 2019).

[6] *See Pending Admin. Proc.*, 2018 WL 4003609, at *1.

[7] Div. Reply at 2; Div. Resps. to Resp't's Proposed Findings of Fact & Conclusions of Law at 2 (Oct. 4, 2019); *see Gibson*, Admin. Proc. Rulings Release No. 6648, 2019 SEC LEXIS 1937, at *3 (ALJ Aug. 5, 2019) ("I will strike findings or conclusions that contain argument.").

there is no point in removing improper arguments from the record that I can simply ignore or decline to adopt. Similar to a federal bench trial, concerns about confusion or undue prejudice from improper argument or evidence do not apply in this proceeding.[8] Instead of striking portions of Gibson's findings and conclusions that contain improper argument, I have simply not relied on those points.

Invoking Rule of Practice 152(f), Gibson asks me to strike what he considers "scandalous or impertinent matter" in the hearing record and in the Division's post-hearing brief concerning Gibson's current financial activities as reflected in his recent tax filings.[9] In particular, Gibson wants any insinuation that he has been committing tax fraud excised from the record. The Division opposes the motion, arguing that the portions of testimony and argument objected to by Gibson are not scandalous and are relevant to Gibson's claim of inability to pay and to his credibility.[10]

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[8] *See Harris v. Rivera*, 454 U.S. 339, 346 (1981) ("In bench trials, judges routinely hear inadmissible evidence that they are presumed to ignore when making decisions."); *City of Anaheim*, Exchange Act Release No. 42140, 1999 WL 1034489, at *2 (Nov. 16, 1999) ("Administrative agencies such as the Commission are more expert fact-finders, less prone to undue prejudice, and better able to weigh complex and potentially misleading evidence than are juries.").

[9] Resp't's Mot. Pursuant to Rule 152(f) for an Order Striking Scandalous & Impertinent Matter at 1 (Sept. 26, 2019); *see* 17 C.F.R. § 201.152(f).

[10] Div. Opp'n to Resp't's Mot. to Strike at 2–3 (Oct. 2, 2019).

Rule 152(f) is mirrored, in part, by Rule 12(f) of the Federal Rules of Civil Procedure.[11] In the federal court context, scandalous material "unnecessarily reflects on the moral character of an individual," such as a party or other person, or contains "repulsive language that detracts from the dignity of the court."[12] Impertinent matter "consists of statements that do not pertain, and are not necessary, to the issues in question."[13]

The only portion of the hearing transcript objected to by Gibson that *might* qualify as scandalous or impertinent is Division counsel's remark that he could prove tax fraud if he wanted to, but was not going to try.[14] I already stated that I would disregard that remark, so I need not strike it.[15] The sentence in the Division's brief suggesting that Gibson's current financial activities are further reason to bar him from the securities industry is not scandalous or impertinent.[16] It is argument, it cites the record, and it has a modicum of relevance. I will not strike it.

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[11] *Compare* 17 C.F.R. § 201.152(f) ("Any scandalous or impertinent matter contained in any brief or pleading or in connection with any oral presentation in a proceeding may be stricken on order of the Commission or the hearing officer."), *with* Fed. R. Civ. P. 12(f) ("The court may strike from a pleading . . . impertinent, or scandalous matter.")

[12] *Pigford v. Veneman*, 215 F.R.D. 2, 4 (D.D.C. 2003); *see Collura v. City of Philadelphia*, 590 F. App'x 180, 185 (3d Cir. 2014).

[13] *Fantasy, Inc. v. Fogerty*, 984 F.2d 1524, 1527 (9th Cir. 1993), *rev'd on other grounds*, 510 U.S. 517 (1994).

[14] Tr. 1516.

[15] Tr. 1516–17.

[16] Div. Br. 39.

Findings of Fact

I base the following factual findings and legal conclusions on the entire record before me and the demeanor of the witnesses who testified at the hearing, applying preponderance of the evidence as the standard of proof.[17] All arguments that are inconsistent with this decision are rejected.

1. Gibson and Hull set up the Fund in 2009 and 2010.

The relevant facts in this case are largely undisputed. But because the implication of the facts is vigorously disputed, I consider in detail what happened and the overall context. Although Gibson is the respondent in this matter, James Hull, the majority owner of the Fund, played a significant part in many of Gibson's actions. I therefore detail Hull's role below as well.

Gibson, now in his mid-thirties, was in his mid and late twenties during the relevant period.[18] He graduated from Williams College in 2006, and immediately started working at Deutsche Bank Securities in New York in the securitized products group.[19] In that position, he worked on auto and mortgage loan securitizations.[20] Gibson left Deutsche Bank in early 2009, took and passed the series 65 investment adviser exam, and returned to Augusta,

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[17] *See Rita J. McConville*, Exchange Act Release No. 51950, 2005 WL 1560276, at *14 (June 30, 2005), *pet. denied*, 465 F.3d 780 (7th Cir. 2006).

[18] Div. Ex. 216 (joint stipulations) ¶ 1.

[19] Tr. 76–77.

[20] Tr. 76.

Georgia—where he had grown up and where his parents lived.[21]

At that time, Gibson's father, John Gibson, was one of Hull's business partners.[22] John Gibson suggested that Gibson speak to Hull for career advice.[23] Hull founded a real estate development business, then called Hull Land Company, in 1977.[24] By 2010, the firm was called Hull Storey Gibson (as in Gibson's father, John Gibson).[25] Hull's company bought and ran shopping malls around the United States.[26] By all accounts, the various iterations of Hull's companies have been successful. According to one witness, Hull and his partners "made a lot of money" by "cut[ting] . . . costs to the bone," in part by cutting the number people involved in running the malls.[27] Hull is also quite involved in his community. In 2018, he was chair of the board of regents of the 26-institution university system of Georgia, and he sits on the board of the Augusta University health system and a number of other civic entities.[28]

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[21] Tr. 77–79, 1083, 1105. Gibson had previously passed the series 7 and 63 exams. Tr. 78–79.

[22] Tr. 79, 670.

[23] Tr. 1096–97.

[24] Tr. 79, 520.

[25] Tr. 79–80, 520–21.

[26] Tr. 79.

[27] Tr. 1257.

[28] Tr. 668, 679. Additionally, Hull is a member of Augusta National Golf Club, annual host of the Masters Tournament, and home of one of the most famous golf courses in the world. *See* Tr. 143. He was also instrumental in securing government funding for the $100 million Hull McKnight Georgia Cyber

From an office at Hull Storey Gibson, Gibson initially provided Hull with personal investment advice and helped with Hull's real estate business.[29] Hull and Gibson often discussed investing and Hull became quite interested in Gibson's investment ideas.[30] So he took roughly $20 million he held in accounts with two firms and had Gibson manage it.[31] Gibson soon formed the Hull Fund and the Gibson Fund, investment partnerships that principally invested in physical gold and silver.[32] It is apparent that Hull gave Gibson the opportunity to manage his investments in large part because of Hull's business relationship with John Gibson.[33]

Gibson and Hull then began working together to set up the Fund as an investment hedge fund.[34] Before setting up the Fund as a Delaware company in December 2009, Gibson formed Geier Group, LLC, in April 2009, and registered it as a Georgia investment advisory firm.[35] It initially served as the Fund's investment manager.[36] In June 2009, he formed Geier Capital, LLC, also a Georgia company, and it

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Center. Tr. 679; *see* https://georgia.gov/agencies/hull-mcknight-georgia-cyber-center-innovation-and-training.

29 Tr. 86, 1097–98; Div. Ex. 10.

30 Tr. 1098–99, 1257.

31 Tr. 1257; *see* Div. Ex. 10.

32 Tr. 86–87.

33 Tr. 1255.

34 *See* Tr. 140; Div. Ex. 10; Div. Ex. 31 at 2.

35 Div. Exs. 11, 12; Div. Ex. 21 at 1; Div. Ex. 216 ¶¶ 3, 10.

36 Div. Ex. 21 at 3; *see* Div. Ex. 64 (certificate of termination of Geier Group).

was the Fund's managing member for a time.[37] Geier Group and Geier Capital were each owned 50% by Gibson, 35% by Hull, and 15% by John Gibson.[38]

In January 2010, the Hull Fund and the Gibson Fund rolled into the Fund.[39] Starting in that month, Gibson distributed the Fund's confidential private offering memorandum, operating agreement, and subscription agreement to potential investors.[40] Each person who invested signed the operating and subscription agreements.[41] Gibson signed the operating agreement as the managing director of the Fund's managing member—Geier Capital—and as the managing director of Geier Group—the investment manager.[42] The offering memorandum informed investors that "The success of the Company is significantly dependent upon the expertise and efforts of Chris Gibson."[43]

Despite this information, and the fact that Hull is not mentioned in the offering memorandum or operating agreement, no one actually thought that Gibson was making major investment decisions for the Fund without Hull's involvement.[44] Gibson knew

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[37] Div. Ex. 21 at 1; Div. Ex. 216 ¶ 5; *see* Div. Ex. 63 (certificate of termination of the Georgia Geier Capital).

[38] Div. Ex. 216 ¶¶ 4, 9.

[39] Tr. 87.

[40] *See* Tr. 115–16; *see* Div. Ex. 24.

[41] Tr. 116; *see, e.g.*, Resp't Exs. 9–16.

[42] Div. Ex. 22 at 12; Div. Ex. 23 at 12.

[43] Div. Ex. 24 at 17.

[44] Tr. 1308–10, 1332.

Hull was in control[45] and even Gibson's father believed the Fund was ultimately being run by Hull.[46] Hull, who approved the Fund's structure, believed he exercised approval authority over any "major decision."[47] And many investors who knew Hull invested not so much because of Gibson's involvement, as described in Fund documents, but because Hull was involved in the Fund.[48]

In 2011, the Fund had 21 members total.[49] Hull owned over 80% of the Fund valued at about $26 million.[50] Gibson, Gibson's parents, and Giovanni Marzullo, the father of Gibson's girlfriend, Francesca Marzullo, held another 10% of the Fund.[51] With the exception of one investor connected to Gibson, every remaining investor was one of Hull's business associates or life-long friends or both.[52]

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45 *See* Tr. 1366–67, 1509–10; *see also* 1386 (discussing process of getting Hull's approval for possible transactions), 1393 (same), 1411–12 (same).

46 Tr. 1258, 1287.

47 Tr. 570–71, 672–73.

48 *See* Tr. 1332; *see also* Tr. 754 (investor affirming that he did not read the operating agreement), 771–75 (investor affirming that he invested because his father, who invested and vacationed with Hull, wanted him to invest), 835–36 (investor confirming he only "scanned over" certain Fund documents).

49 Div. Ex. 216 ¶ 11.

50 Tr. 529, 588, 669–70; Resp't Ex. 206.

51 Tr. 561; Div. Ex. 33; Resp't Ex. 206.

52 Tr. 134, 142–43, 529, 541, 675–80; Resp't Ex. 206.

2. The Fund's offering documents disclosed features of the investment, and Hull required an "alignment of interest" between Gibson and the Fund.

Gibson and Hull spoke with nearly every investor before they invested.[53] In these conversations, Hull made clear that the Fund was a "high-risk type venture."[54] The offering memorandum likewise stated that the Fund was "a highly speculative investment" that was "designed only for sophisticated" investors.[55] The offering memorandum further affirmed that the Fund, like many such funds, "generally will not disclose all of its positions to Members on an ongoing basis," suggesting that it could remain secretive about its positions and strategies.[56]

The operating agreement and offering memorandum both warned investors that affiliates of the Fund, such as Gibson, may conduct business "in competition with the" Fund.[57] The offering memorandum further warned that affiliated parties, like Gibson, might serve as investment advisers to others, and might invest in the same securities as the Fund in separate accounts.[58] Gibson in fact did both:

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53 Tr. 680, 1337–38.

54 Tr. 681. *But cf*. Tr. 836 (testimony that investor did not remember whether he was told the investment was "risky").

55 Div. Ex. 24 at 1, 7, 10.

56 *Id.* at 17; *see Goldstein v. SEC*, 451 F.3d 873, 875 (D.C. Cir. 2006) ("[Hedge funds typically remain secretive about their positions and strategies, even to their own investors.").

57 Div. Ex. 21 at 2; Div. Ex. 24 at 19.

58 Div. Ex. 24 at 19.

he served as a personal adviser to Hull without further disclosing that relationship to the Fund, and he invested in TRX in his personal account.[59]

The offering memorandum also made clear that Gibson was to invest "the majority of his liquid net worth" in the Fund.[60] This was because Hull wanted Gibson to have "total focus" on the Fund he was managing.[61] In fact, Gibson, Hull, and John Gibson each mentioned Hull's desire to establish an "alignment of interest" between Gibson on one side and Hull and the Fund on the other.[62] Hull wanted both Gibson and his father "to have skin in the game and to be totally focused on this fund being successful."[63] When asked if he wanted "Gibson to be aligned with" him or with the Fund, Hull responded "I would view them one and the same."[64]

Gibson was thus required to borrow close to $650,000 from Hull, invest virtually all of his money in the Fund, and invest outside the Fund in what the Fund invested in.[65] And Hull loaned money to John Gibson to invest as well.[66] John Gibson agreed to this arrangement because of his "loyalty" to Hull and

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59 Tr. 145, 254, 763, 827; Div. Ex. 86 at 1, 3 (statement from Gibson's personal Schwab account); Div. Ex. 216 ¶ 23.

60 Div. Ex. 24 at 1, 7.

61 Tr. 561–62. Both Gibson and his father testified that Hull wanted a "severe alignment of interest" between himself and the other investors in the Fund. Tr. 1112, 1472.

62 Tr. 562, 674, 736, 1112, 1259, 1340.

63 Tr. 674.

64 Tr. 736.

65 Tr. 1340, 1358–59; Resp't Ex. 117 at 5.

66 Tr. 1359; *see* Tr. 1259.

because he "had complete confidence in" him.[67] By design, if the Fund lost money, Gibson would lose more than other investors, and his family and "individuals close to" him would be "exposed."[68] Indeed, when Gibson paid off his note to Hull in 2011, after receiving his bonus for 2010, Hull became "visibly upset," and required Gibson to re-borrow the same amount.[69] And the approximately $650,000 that would otherwise have gone to pay off the note went back into the Fund, not into Gibson's pocket.[70] Although the Fund's offering documents disclosed Gibson's investment in the Fund—and in fact required it—the documents did not disclose the loan from Hull, and Gibson did not otherwise reveal it to investors.[71]

3. Gibson managed the Fund and received compensation for doing so.

As noted, Hull had great success in his real estate business by "cut[ting] . . . costs to the bone."[72] Hull decided to apply this idea to managing the Fund.[73] And this meant that Gibson, at about 26 years of age, was managing a $32 million fund with little experience and without "a full staff" or an experienced investment adviser to give him guidance or advice.[74] Gibson was thus alone in managing the Fund's day-

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67 Tr. 1259.

68 Tr. 1358.

69 Tr. 1360–61.

70 Tr. 1361–62.

71 Tr. 765–66, 828.

72 Tr. 1257.

73 Tr. 1257.

74 Tr. 1257.

to-day operations and performing investment advisory services for it.[75] He also negotiated securities transactions on its behalf, tracked market conditions and the performance of the Fund's portfolio, sent status reports about the Fund to investors, communicated with brokers and counterparties, spoke with the management of TRX, and submitted filings to the Commission.[76] Major decisions about the Fund's investment strategy, such as which stocks to invest in and when to hold or sell, were approved by Hull in close consultation with Gibson.[77]

Gibson was compensated for his services to the Fund. From 2010 until early 2013, he received a salary from Hull's real estate business.[78] These payments were for his advisory services to the Fund.[79] Through 2010, Geier Group repaid Gibson's salary to Hull's company; effectively, Gibson's salary was paid by Geier Group while the entity existed.[80]

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[75] Tr. 129, 186, 567. The offering memorandum stated that Gibson was the managing member of Geier Group, and that Geier Group was "responsible for certain administrative and investment advisory matters" for the Fund. Div. Ex. 24 at 1. Gibson told investors that he was Geier Group's investment adviser. Tr. 109–110; Div. Ex. 16 at 24407.

[76] Tr. 185–87; *see, e.g.*, Tr. 242–44, 279–80, 320–21; Div. Exs. 31, 39, 70, 71.

[77] Tr. 569–71, 673; *see, e.g.*, Div. Exs. 80, 91; Resp't Exs. 59, 102.

[78] Tr. 246–52; Div. Exs. 43, 128, 147, 156.

[79] Tr. 247–49, 251–52; Div. Ex. 188 at 472–74 (Gibson's investigative testimony).

[80] Tr. 248–54. The salary was distributed through Hull's company and its payroll services to avoid the need to set up a

Under the Fund's operating agreement and offering memorandum, Geier Group was also entitled to an annual investment management fee equal to 1% of each member's capital account.[81] The agreements also entitled Geier Capital to a 10% "incentive allocation" if the Fund met certain benchmarks.[82] Both the management fees and incentive allocation were compensation for Gibson's advisory services to the Fund.[83] The Fund paid investment management fees in 2010 and 2011.[84] As a 50% owner of Geier Group and Geier Capital, Gibson was entitled to half this amount, which was around $250,000 for 2010 and 2011 combined.[85] He reinvested the money in the Fund.[86] In 2010, the Fund also paid Geier Capital an incentive allocation of around $3 million.[87] Gibson was entitled to half of this amount, which he reinvested in the Fund.[88]

4. Geier Group is dissolved and Gibson substitutes Geier Capital for another entity of the same name.

At the end of December 2010, Gibson allowed Geier Group's registration as a Georgia investment

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separate payroll for Gibson's advisory services to the Fund. Tr. 248.

81 Tr. 121; Div. Ex. 21 at 4; Div. Ex. 24 at 8; Div. Ex. 216 ¶ 12.

82 Tr. 123; Div. Ex. 21 at 5; Div. Ex. 24 at 8–9.

83 Div. Ex. 188 at 407, 461.

84 *Id.* at 402, 457, 461.

85 *Id.* at 403, 461; Div. Ex. 216 ¶ 13.

86 Div. Ex. 188 at 363–64, 461–62.

87 Div. Ex. 42 at 4; Div. Ex. 216 ¶ 14.

88 Tr. 123, 125–27; Div. Ex. 216 ¶ 13.

adviser to lapse.[89] He did not tell the Fund's investors, and in fact, solicited two new investors using offering documents stating that Geier Group was a registered investment adviser even though it was no longer registered.[90] Geier Group was dissolved in April 2011; nonetheless, Gibson falsely indicated in Commission filings that it still existed.[91] Despite Geier Group's dissolution, Gibson continued to advise the Fund in 2011 just as he had in 2010.[92] Gibson created a new Geier Capital entity in Delaware in December 2010 with the same ownership structure as the old one.[93] He dissolved the Georgia Geier Capital in March 2011.[94] Gibson neither disclosed to investors the dissolution of Geier Group nor the substitution of the Delaware Geier Capital for the Georgia entity, and he failed to amend the Fund's offering documents to reflect these changes.[95] The Fund's operating agreement, however, stated that the managing member had the "sole discretion" to retain a different entity than Geier Group "to serve as the [c]ompany's investment manager."[96]

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89 Div. Ex. 167; Tr. 149–51.

90 Tr. 151–52, 176–77; Div. Exs. 54, 56.

91 Div. Exs. 60, 64; Tr. 159–60, 177–82.

92 Tr. 184, 187.

93 Tr. 182–83; Div. Ex. 40; Div. Ex. 216 ¶¶ 7, 9.

94 Div. Ex. 216 ¶ 6; Div. Exs. 49, 63.

95 Tr. 162, 184.

96 Div. Ex. 21 at 3.

5. The Fund invests all its money in TRX, but as 2011 progresses, the stock's value declines.

Initially, the Fund invested in gold and other commodities.[97] During 2010, the Fund was "up 110 percent."[98] But Hull became "irritated" in late 2010 on learning that the Fund's successful commodities trading resulted in a large tax bill.[99] To deal with this "unfavorable tax" situation, and to generate fees, he decided to increase the Fund's equity investments instead.[100] Although Gibson thought the Fund should add additional employees to "cover a number" of potential investments, Hull favored a leaner operation.[101] Based on his real estate experience, Hull favored having one employee—Gibson—and "owning a single stock."[102]

Gibson knew that investing all of the Fund's assets in one stock was risky.[103] But he deferred to Hull's experience and identified TRX as a suitable investment for the Fund.[104] According to Gibson, TRX is a "junior" gold mining company that explores for

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[97] Tr. 539–40, 1350; *see* Tr. 1363–64 (the Fund was trading in commodities in 2010).

[98] Tr. 1362.

[99] Tr. 540, 575, 672, 1364–66.

[100] Tr. 540, 575, 672, 1366.

[101] Tr. 1257, 1366.

[102] Tr. 1257, 1366.

[103] Tr. 1366–67.

[104] Tr. 575, 1367 ("I . . . had . . . supreme respect for Mr. Hull's judgment. Who am I? You know, I haven't had nearly the success he has and I believed it would -- and I certainly also believed it was an achievable objective.").

gold resources in Africa.[105] He testified that it had 46 mining properties in Tanzania.[106] The Fund began investing in TRX in late 2010 and early 2011.[107] By the end of April 2011, the Fund's assets were invested solely in TRX, and the Fund owned approximately 9.7 million shares of TRX stock (worth approximately $70 million), which was around 10.3% of all outstanding TRX shares.[108]

The Fund's fortunes began to change soon after it concentrated its investments in TRX. In June 2011, TRX peaked at $7.46 a share, and then slowly declined the rest of the summer.[109] Given that TRX was a gold-mining company and the price of gold was high, Gibson had difficulty understanding why TRX's share price was declining.[110] And Hull was concerned that TRX's president and CEO, Jim Sinclair, was not doing the exploration necessary for TRX to succeed.[111] On August 5, Hull communicated his concerns to Gibson, noting that the Fund had lost most of its gains and "incurred a huge income tax obligation."[112] Hull also pointed out that "none of" his and Gibson's

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[105] Tr. 189. Gibson testified that a junior gold mining company "is one that is entire[ly] or generally exploratory in nature, less capitalized, typically does not have the resources to fully develop the asset and is more dependent upon access to the capital markets and typically has a greater leverage to the gold price." Tr. 1350.

[106] Tr. 1351.

[107] Tr. 1345; Div. Ex. 53 at 1.

[108] Tr. 188; Div. Ex. 216 ¶¶ 15, 16.

[109] Tr. 1347; Joint Ex. 1 at 3–4.

[110] Tr. 1373.

[111] Tr. 582.

[112] Div. Ex. 75 at 71133.

"reasoning/predictions have come to [bear]."[113] Gibson felt the pressure.

6. Gibson berates TRX's president and considers a potential sale.

On August 10, when TRX was trading a little below six dollars a share, Gibson e-mailed Sinclair, saying that he was "physically ill over our performance," it would "[v]ery soon . . . make sense to exit our positions," and "[t]here is no time left."[114] In a separate e-mail, Gibson berated Sinclair, complaining about statements made by TRX's chief geologist that contradicted both Sinclair and TRX press releases and that Gibson worried would be publicly reported.[115] Gibson demanded, "What is the answer," and told TRX's CEO to "make sure [the geologist] is on the same page."[116]

Sinclair replied and tried to reassure Gibson that he was doing what he could to move the company forward.[117] Gibson quickly responded asking whether certain things Sinclair had previously said were no longer accurate.[118] Receiving no immediate response, Gibson e-mailed Sinclair again (in all caps), asserting that "everything you say is always

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[113] *Id.*

[114] Div. Ex. 76; Joint Ex. 1 at 4. Although all the e-mails discussed in this paragraph appear to have been sent on August 10, 2011, the time stamps are confused, and it is unclear whether this e-mail was sent before or during a separate exchange shown in Division Exhibit 77.

[115] Div. Ex. 77 at 71655; *see* Tr. 1348 (identifying chief geologist).

[116] Div. Ex. 77 at 71655.

[117] *Id.* at 71654–55.

[118] *Id.* at 71654.

inaccurate," "this is the last straw," and Gibson was in danger of losing credibility with his investors because of Sinclair's lapses.[119] Sinclair responded that he "totally disagree[d]" and did "not intend to continue" the conversation.[120] A few hours later, Gibson told Sinclair that "our share price is a disaster" and "[w]hatever we are doing is failing."[121] Gibson then instructed that "We need to be all hands on deck. We need to be mapping out a calendar or announcements for the next six weeks. We need to be planning a roadshow. We need to be PRODUCING the gravels and tailings. We need to be announcing that."[122]

On August 15, Gibson and Sinclair traded e-mails again about planning a roadshow to attract additional investors. Gibson felt that "[t]his is a priority whose significance I cannot sufficiently emphasize" and added that this was a "do or die moment" and if "we do not move by [September 2011], we are toast."[123] Sinclair assured Gibson that he was "working as hard and fast as possible."[124]

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[119] *Id.* ("I TOLD MY INVESTORS YOU SAID THIS AND NOW IT IS NOT TRUE? HOW DO YOU EXPECT THEM TO STAND BY ME WHEN THIS HAPPENS OVER AND OVER AND OVER?").

[120] *Id.* The parties presented little evidence about the nature of Gibson's relationship with Sinclair. The record reveals, however, that at this point, Gibson was about 27 years old and Sinclair, who was approaching 70 years of age, *see* Div. Ex. 183A at 5, was TRX's president and CEO.

[121] Div. Ex. 77 at 71654.

[122] *Id.*

[123] Div. Ex. 78 at 73888.

[124] *Id.*

In context, it is clear that although Gibson was worried about TRX's share price, perhaps thought TRX's management was not doing enough to raise that share price, and was trying to "[i]nstill a sense of urgency in Mr. Sinclair," he still believed that TRX had substantial value as a company.[125] For one thing, he did not immediately sell his own TRX shares. And he told the Fund's investors in a letter on August 22, that although his "performance year to date ha[d] been an exceptional failure," the Fund was "positioned exceedingly well" and investors should "sit tight."[126]

Gibson was, however, starting to consider selling the Fund's interest in TRX. On the same day he communicated with Fund investors, he reached out to Richard Sands, a banker at Casimir Capital, and told Sands that he would be willing to sell the Fund's entire position, but wanted $6.25 per share, which would have been a premium above the then-current market price of $5.85.[127] Sands did not think the price Gibson sought was "doable," but looked into it, and came back with a buyer who was willing to buy at market price.[128] Hull and Gibson "seriously" considered the offer, but rejected it because they "did not [think it] reflect[ed] the value of [the Fund's]

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[125] Tr. 1380–82. According to Hull, the hyperbolic language Gibson used with Sinclair was typical of his "personality." Tr. 583. Gibson would "run very hot an d cold" and "go unhinged on them" but then be "nice." Tr. 583. Gibson would sometimes "rant and rave about . . . Jim Sinclair in a negative way." Tr. 584.

[126] Resp't Ex. 51 at 2; *see* Tr. 1382.

[127] Resp't Ex. 177 at 1–4.

[128] *Id.* at 1; Tr. 1384–86.

position."[129] Hull and Gibson were therefore still sufficiently bullish in late August about TRX's value that they would only have sold for a premium.

7. Gibson suspends management fees for the Fund in light of its poor performance.

But TRX's share price continued to decline. On September 22, it tumbled from around $5.50 to around $4.50.[130] Gibson again expressed displeasure to Sinclair, but in a more measured tone than in August.[131] Meanwhile, Hull asked Gibson whether Hull should increase his personal investment in TRX because the stock had gone so low.[132] Gibson told him that although he remained "bullish" on TRX, and expected the share price to recover over time, he did not recommend buying more shares.[133] Later that evening, however, Gibson opined that the Fund should buy more TRX shares.[134] Gibson also told Hull that although he would personally hold "TRX until its share price has the opportunity to better reflect its underlying value," he had "failed to fulfill the expectations our partners and I have had for its performance" and would cease taking management fees for his work on behalf of the Fund.[135]

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[129] Tr. 1386; *see* Resp't Ex. 62 at 6 (e-mail from Sands noting in late September that Gibson had backed away from previous sale).

[130] Joint Ex. 1 at 4.

[131] Div. Ex. 79.

[132] Tr. 1389; *see* Resp't Ex. 52.

[133] Resp't Ex. 52 at 1; Tr. 1389–90; *see* Resp't Ex. 54.

[134] Resp't Ex. 53 at 1 ("I think it is extremely compelling to do so. I would not buy anything else.").

[135] *Id.*

The following day, Gibson backed off his advice to Hull to buy TRX shares and instead urged caution.[136] Gibson also told investors that the Fund was down "to only slightly above original principal investments last year," and that at the end of the month, he would stop assessing management fees until the Fund's performance returned to "acceptable levels."[137] He nonetheless reiterated his faith in TRX's "underlying value" and wrote, "Personally, I will not redeem my interest in Geier and TRX until the bull market matures over the coming years at what I strongly believe will be significantly higher levels."[138] Two investors responded to Gibson's email stating that they remained supportive of his efforts.[139]

TRX's share price dropped again on Friday, September 23, to $4.07.[140] Around the end of the trading day, Gibson sold 78,000 of the Fund's TRX shares for $4.04 per share.[141] An investor urged Hull that day to consider diversifying the Fund's portfolio in the near future, but Hull rejected the proposal.[142]

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[136] Resp't Ex. 54.

[137] Resp't Ex. 56 at 1.

[138] *Id.*; Div. Ex. 81 at 1 (same letter). Context shows that when Gibson said he would not redeem his "interest in Geier and TRX," he was talking about his personal investment in the Fund, and not about any investment he had in TRX outside the Fund.

[139] Resp't Exs. 57, 58.

[140] Joint Ex. 1 at 4.

[141] Resp't Ex. 17 at 4; Tr. 1391; Div. Ex. 216 ¶ 22.

[142] Resp't Ex. 59 at 1 ("[C]oncentration into one stock provides equal benefits (you can truly understand one company) and a thinly traded company has benefits as well.").

8. Hull and Gibson decide to sell the Fund's investment in TRX.

Over the following weekend, however, Hull had a change of heart about holding TRX. He told Gibson that he was not sure "he had a tolerance for more losses," which Gibson took to mean that he (Gibson) should "consider a sale" and "solicit a bid" for the Fund.[143] Hull's general guidance was to get out at good prices.[144] Gibson never informed the Fund's investors of Hull's change in strategy.[145]

Over the next month and a half, Gibson tried to sell the Fund's TRX shares at good prices. Although there were times during this period when Hull and Gibson were content to briefly hold and wait for better offers,[146] the evidence shows—as will be detailed below—that Gibson regularly reached out to brokers and counterparties from September 25 until November 10 to try to liquidate the Fund's holdings in TRX on favorable terms.

9. Gibson sells personal shares ahead of the Fund's sale of a third of its TRX investment.

On Sunday evening, September 25, Gibson wrote to Sands at Casimir asking if there was a buyer for up to the Fund's entire position in TRX.[147] Gibson offered 10,250,000 shares, which was the total held by the Fund, combined with a block of around 680,000

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[143] Tr. 1392–93.

[144] Tr. 219–20, 605; Div. Ex. 187 at 77–78 (Gibson's investigative testimony).

[145] Tr. 220.

[146] Resp't Exs. 89, 101; Div. Ex. 91.

[147] Resp't Ex. 62 at 6, 8.

shares held separately by Hull.[148] Sometime on September 26, Sands informed Gibson that he thought he had a buyer for about three to five million shares.[149] Gibson told Sands to "maximize the number of shares" and "price and book the sale" on September 27.[150]

As noted above, Gibson held TRX shares in his personal account outside of the Fund.[151] Sometime on September 26, he sold 2,000 TRX shares from his personal Schwab brokerage account.[152] He also sold 1,000 TRX shares from Geier Group's Schwab account.[153] Finally, he sold 18,900 TRX shares from the account of his girlfriend, Francesca Marzullo.[154] Ms. Marzullo was not invested in the Fund.[155] Her account "was conceived by" and funded solely by her father.[156] Gibson was "exclusively responsible for the trades in [Ms. Marzullo's] account," and he "reported those trades and discussed them daily with Mr. Marzullo."[157] He did not, however, speak with Mr.

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[148] Tr. 1404–05.

[149] Resp't Ex. 62 at 4–5.

[150] *Id.* at 4.

[151] Div. Ex. 216 ¶ 23.

[152] *Id.* ¶ 26; Div. Ex. 86 at 3; Tr. 226, 1394.

[153] Div. Ex. 88 at 7; Div. Ex. 216 ¶¶ 25, 28; Tr. 231–32, 1394.

[154] Div. Ex. 87 at 2–3; Div. Ex. 216 ¶¶ 24, 27; Tr. 230. As noted, Ms. Marzullo was the daughter of Giovanni Marzullo, an investor in the Fund. Tr. 135, 227, 1336.

[155] Tr. 143.

[156] Tr. 1395–97. Ms. Marzullo was an unemployed graduate student at the time. Tr. 1397.

[157] Tr. 1396–97.

Marzullo before selling Ms. Marzullo's shares on September 26.[158]

Gibson obtained an average share price of $4.04 to $4.05 for sales from the three accounts.[159] No TRX shares remained in these accounts after the sales.[160] Gibson never disclosed these transactions to Fund investors.[161] In light of Gibson's investment in the Fund and its concentration in TRX, Gibson's sale of his personal shares amounted to a "little under 1 percent" of his total exposure to TRX through the Fund.[162] So he remained "significantly long" in TRX.[163] As Gibson testified, because of their relatively small size, there is no evidence that his September 26 sales materially affected TRX's share price.[164]

Gibson testified that he sold his personal TRX shares because he had no liquid assets and management fees from the Fund had just been suspended.[165] But given that Francesca Marzullo's shares were funded by her father, Gibson's testimony regarding a need for liquidity does not explain why he sold her shares.[166] Most importantly, Gibson's explanation does not sufficiently address the timing

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[158] Tr. 1471.

[159] Div. Ex. 86 at 3; Div. Ex. 87 at 2–3; Div. Ex. 88 at 7.

[160] Tr. 226, 230, 232.

[161] Div. Ex. 188 at 662–63, 665–66, 669–71; Tr. 760, 823–24 (two investors testified that they were unaware of Gibson's personal sales of TRX).

[162] Tr. 1395.

[163] Tr. 1398.

[164] Tr. 1424.

[165] Tr. 1394, 1472–73.

[166] *See* Tr. 1395–97, 1473.

of the sale. On the morning of Monday, September 26, Gibson was actively working to sell the Fund's entire position.[167] Gibson understood that Sands likely would have a buyer for a block sale and urged Sands "to price and book the sale" on Tuesday, September 27.[168] Although Gibson did not know exactly when the Fund's block sale would take place, and any sale was still dependent on Hull's approval,[169] he was in the midst of a negotiation that he hoped would lead to a sale. The timing of the sale in the three accounts outside the Fund suggests that at the very least, Gibson was attempting to avoid potential losses by selling personal shares ahead of the Fund's impending block sale.

TRX closed at $4.11 on Monday, September 26, and opened at $4.24 on Tuesday, September 27.[170] Following Sands's instructions, Gibson transferred all of the Fund's TRX shares to an account at Casimir.[171] The volume of trading in TRX was heavy all day, with the share price rising to $4.34 and then dropping to $3.70 around 3 p.m.[172] Around that time, Sands

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[167] Resp't Ex. 62 at 6–7.

[168] *Id.* at 4–5.

[169] Tr. 1415–16, 1421–23.

[170] Joint Ex. 1 at 4.

[171] Resp't Ex. 62 at 1–3; Resp't Ex. 66; Div. Ex. 90 at 3. Sands told Gibson that Gibson needed to place all the Fund's shares in its Casimir account in order to reassure the buyer because "no buyer will buy that quantity if they know another 5mm is being sold behind it." Resp't Ex. 62 at 1.

[172] Joint Ex. 1 at 4; Tr. 1007–08; Div. Ex. 184 at Exhibits p. 4 (Dr. Taveras Expert Report – TRX intraday trading for September 27); *see* Tr. 1679 (reflecting Gibson's counsel's

phoned Gibson with an offer of $3.50 a share for around 3.5 million of the Fund's TRX shares.[173] Gibson and Hull decided "in one minute to accept it."[174] The Fund sold 3,734,395 TRX shares for around $3.50 a share.[175] TRX closed at $3.54 on a volume of over six million shares traded that day.[176] If Gibson had sold his personal TRX shares immediately after the Fund sold its shares and obtained the same price as the Fund, he would have received around 54 cents less per share than he did.[177]

10. Gibson considers other offers for the Fund in late 2011.

Gibson attempted to sell the remainder of the Fund's TRX position throughout the end of September and in October. At the end of September, Gibson reached an agreement with Luis Sequiera, a principal at Roheryn Investments S.A., to buy the rest of the Fund's TRX position, plus the additional block of shares held separately by Hull, at $3.50 a share.[178] In early October, however, the sale fell through.[179] When he told Hull the deal fell through, Gibson said that "[w]e're going to very likely be best served holding our position" and "I would assume we are

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concession that Division expert Dr. Carmen A. Taveras's calculations, as opposed to her conclusions, are not in dispute).

[173] Tr. 1422; Div. Ex. 82 at 6711.

[174] Tr. 1422–23.

[175] Div. Ex. 82 at 6710; Div. Ex. 90 at 3.

[176] Joint Ex. 1 at 4.

[177] Tr. 234–35.

[178] Resp't Ex. 92 at 3; Resp't Ex. 93; Tr. 1427–30.

[179] Resp't Ex. 101; Tr. 611–12, 1430–31.

where we are for the next several months."[180] Hull wanted Gibson to keep trying to find a different buyer or work with Sequiera to make a deal.[181] Negotiations with Sequiera picked up again when Sequiera offered to buy about 200,000 of the Fund's shares a day, but Gibson rejected the offer in mid-October.[182] Gibson told Hull on October 14, "I am contemplating our options but waiting for at least a few weeks."[183] Nonetheless, on October 16, Gibson e-mailed a broker at GarWood Securities and said that the Fund "will be closing [its] TRX position in the next few weeks with a pre-arranged buyer beginning" the next day.[184] Indeed, Gibson testified that at this time, "[o]n a near-daily basis, we had a belief that we were imminently close to the consummation of that full sale."[185] But the planned transaction that was to begin on October 17—and which may again have been a deal with Sequiera—also fell through.[186] The Fund, however, did sell 364,495 TRX shares at an average price of $3.42 per share on October 17.[187]

11. The Fund purchases a block of TRX shares separately held by Hull.

The Fund's offering memorandum provided that "purchase and sale transactions" between the Fund and "other entities or accounts" could take place

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[180] Resp't Ex. 101.

[181] Resp't Ex. 102.

[182] Resp't Ex. 104; Tr. 1433–34.

[183] Resp't Ex. 104 at 1.

[184] Resp't Ex. 108; Div. Exs. 92, 93.

[185] Tr. 1434; *see* Tr. 260.

[186] Tr. 260, 1434–35; *see* Resp't Exs. 107, 109.

[187] Tr. 1475.

subject to the following guidelines: (1) the sale had to be "for cash" at the "current market price" of the securities; and (2) "no extraordinary brokerage commissions or fees (i.e., except for customary transfer fees or commissions) or other remuneration shall be paid in connection with any such transaction."[188]

On October 18, Gibson caused the Fund to buy the block of 680,636 TRX shares owned by Hull at the closing price that day, $3.60 a share.[189] The purchase price was about $2.45 million.[190] Given Hull's over 80% interest in the Fund, the cost borne by other investors for this transaction was about $470,000.[191] Neither the Fund nor Hull paid a commission on the transaction.[192] Gibson provided investment advisory services to both Hull and the Fund on this transaction.[193]

Gibson testified that he proposed this sale to Hull.[194] Hull first suggested that Gibson proposed the idea before conceding that he was unsure who proposed the sale.[195] But both agreed that they were trying "to achieve a block sale" of all shares held by the

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[188] Div. Ex. 24 at 19.

[189] Div. Ex. 95; Joint Ex. 1 at 5; Tr. 260–61.

[190] Div. Ex. 95. The exact figure was $2,450,589.60. *Id.*

[191] In October 2011, Hull owned 80.702% of the Fund. Resp't Ex. 206.

[192] Tr. 262, 629–30.

[193] Tr. 261.

[194] Tr. 1438–39.

[195] Tr. 706, 737.

Fund and its affiliates, consistent with Sequiera's previous request.[196]

The Division's expert, Dr. Gary Gibbons, opined that since the market volume for TRX on October 18 was just under 500,000 shares traded, if Hull had sold 680,000 shares into the market on that day, it would have depressed TRX's share price.[197] One potential implication of Dr. Gibbons's observation is that the Fund should have received a block discount.[198] In other words, the Fund should have purchased Hull's shares for less than the closing price, because if those shares had been sold on the market, Hull would not have been able to obtain $3.60 for each share.[199] The Fund, however, did not receive a block discount.[200]

Gibson's expert, Daniel R. Bystrom, disagreed with Dr. Gibbons and the Division.[201] He testified

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[196] Tr. 705–06, 1435, 1438–39.

[197] Div. Ex. 185 at 23; Joint Ex. 1 at 5; *see* Tr. 1484–85. Dr. Gibbons is a professor of finance and entrepreneurship at the Thunderbird School of Global Management, which is an independent college at Arizona State University. Tr. 346–47. His work focuses on securities valuation, and he is a registered investment adviser. Tr. 347–48.

[198] *See* Tr. 630, 1628. Dr. Gibbons did not say in his report or testimony that the Fund should have received a block discount in this transaction; he testified only that, because the shares were not sold in the market, the transaction did not occur at the current market price, even though the shares were sold at the closing market price on the day the Fund purchased them. *See* Tr. 945–46, 950–52.

[199] *See* Tr. 945–46, 1628.

[200] Tr. 262.

[201] Bystrom currently oversees risk management at a New York-based investment adviser. Tr. 1552. He has worked in the financial sector since 1992, and has been a portfolio manager at

that it is hard to know whether TRX prices would have been depressed if Hull sold his shares on the market.[202] He admitted that a block discount could be appropriate when a private transaction avoids the price-depressing impact of a sale into the market, but noted that "[t]hose situations are really case by case" and that a motivated buyer "may be willing to pay at market price or even above market price."[203]

When the Fund eventually liquidated its TRX holdings on November 10, which is discussed below, it paid a commission on that sale.[204] Although the parties dispute whether the Fund's purchase from Hull caused it to pay $1,360 or $6,866 in extra commissions, because the Division is not asking for disgorgement of this extra commission, I need not

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hedge funds. Tr. 1553. He is not a registered investment adviser. Tr. 1590.

[202] Tr. 1628–31.

[203] Tr. 1628, 1630. Dr. Gibbons proved to be a difficult witness on cross- examination. He sometimes refused to answer simple yes-or-no questions with a yes or no, Tr. 408–09, 494–96, 501–03, 892–94, and fought counsel's *hypothetical* premises because the premises did not match his view of the facts, *e.g.* Tr. 501, 503, 927–28. On occasion, I had to ask Dr. Gibbons to simply answer the question asked. Tr. 495–96, 883–84. A particularly frustrating exchange occurred when Gibson's counsel asked Dr. Gibbons about a treatise on options. Counsel twice walked Dr. Gibbons through a point in the treatise and concluded by asking whether Dr. Gibbons agreed with the point only to have Dr. Gibbons ask, "In what context?" Tr. 915, 917.

Dr. Gibbons's demeanor diminished his credibility. These sorts of problems generally did not mar Bystrom's testimony, however.

[204] Tr. 1440–41.

decide who is correct.[205] In any event, because Hull owned over 80% of the Fund, only about 19.3% of the extra commission was borne by investors other than Hull.[206]

Dr. Gibbons opined that the Fund's purchase of Hull's shares was "counterproductive to the goals of" the Fund because "the decision to liquidate" the Fund's TRX holdings had already been made.[207] Dr. Gibbons therefore believed that the trade was made to benefit Hull at the expense of the Fund.[208] But both Gibson and Hull testified that the purchase was in the Fund's interest. According to Hull, the Fund purchased his shares in order to consolidate a larger block of shares available for sale, which could

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[205] Gibson testified that the Fund paid a commission of .2 cents per share when it liquidated its TRX assets. Tr. 1441. Multiplied by 680,636 shares, the total commission to sell Hull's former shares would come to $1,361. Relying on the GarWood account statements detailing the sales, the Division notes that a mathematical comparison of the amounts sold with the proceeds received demonstrates that the commission was approximately one cent per share. Div. Ex. 122 at 14–24. The second to last row on page 24 of Division Exhibit 122 indicates 100,000 shares were sold for $2.106 a share with proceeds of $209,594. Multiplying 100,000 by 2.106 equals 210,600. Subtracting 209,594 from that amount yields 1,006. And dividing that by 100,000 shares yields approximately 1 cent per share. According to the Division's calculation, which is based on more concrete evidence than Gibson's, the total extra commission paid was $6,866. *See* Div. Proposed Findings of Fact ¶ 143.

[206] Tr. 1441. Gibson, his parents, and Giovanni Marzullo, together owned 10.278% of the Fund. Resp't Ex. 206. Subtracting this percentage and Hull's percentage from the total means that 9.01% of the extra commission was borne by the remaining Fund investors. And 9.01% of $6,866 is $618.63.

[207] Div. Ex. 185 at 23.

[208] *Id.*

"entice the buyer" and could garner a "substantially increased price."[209] Gibson testified, "We wanted to be in a position to sell the full shares of the fund and its affiliates in a single transaction."[210] Bystrom confirmed based on his industry experience that consolidating the shares "greatly simplifies the process of entering into a block transaction" because a "buyer would want to know that he's seeing the whole piece for sale" and that there are no additional shares left behind.[211]

The evidence lends some support Gibson's contention that there were reasons to sell Hull's shares in a block with the Fund's shares.[212] Both Sands on September 26 and Sequiera on October 1 wanted confirmation from Gibson that the Fund's entire position would be available to sell, and that no shares would be left behind.[213] When Gibson communicated with them, he included Hull's 680,000 shares in the total amount he had available to sell in an effort to identify other large blocks as they had

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[209] Tr. 624, 627, 639.

[210] Tr. 1435; *see* Tr. 1438–39. Elsewhere, however, Gibson was somewhat vague as to his reasons for the Fund's purchase of Hull's shares. On October 17, he told Hull that the consolidation would "help me for regulatory and other reasons." Div. Ex. 94. The same day, he told a banker involved with Hull's account that it would be "easier to manage this position in one place." Resp't Ex. 110.

[211] Tr. 1567; Resp't Ex. 228 at 6 (Bystrom expert report).

[212] Tr. 1435 (Gibson testified that the Hull transaction was consistent with Sequiera's request that all shares of the Fund and its affiliates needed to be sold together).

[213] Resp't Ex. 62 at 7 (Sands said, "whatever we do needs to be a clean up"); Resp't Ex. 93 at 1–2 (Sequiera wanted to make sure the Fund has no other shares to sell).

requested.[214] And Sands asked Gibson to move all of the Fund's shares to an account at Casimir for this very reason; even though he was only brokering the sale of three to five million shares, he wanted everything in one account because "no buyer will buy that quantity if they know another 5 [million] is being sold behind it."[215] But the evidence also shows that the Fund did not need to purchase Hull's shares for all of the shares to be sold at once.[216]

Gibson never disclosed the purchase of Hull's stock to the Fund's investors.[217]

12. Gibson buys puts for himself, his girlfriend, and recommends puts to his father.

After arranging the purchase of Hull's shares on October 18, Gibson continued to search for a buyer for the Fund's remaining TRX position. On October 24, he told one Fund investor that he was planning to liquidate the Fund but, "to ensure we can achieve good execution on the sale," had not disclosed his intent to investors.[218]

On October 26, Hull's executive assistant, Laurie Underwood, e-mailed Gibson a "sixteenth amended and restated demand promissory note," evidencing that he owed Hull $636,921 with an 8% interest

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[214] Tr. 1404–05, 1429–30.

[215] Resp't Ex. 62 at 1.

[216] *See* Tr. 1429–30, 1621–22; Resp't Ex. 92 at 3–4. It is true that Gibson did not consolidate Hull's shares before the September 27 sale or as part of the failed deal with Roheryn. *See* Resp't Ex. 92. But the September 27 sale was anticipated to be for three to five million shares, or less than all of the Fund's shares. Resp't Ex. 62 at 4–5.

[217] Tr. 261–62.

[218] Div. Ex. 98 at 10236; Tr. 635.

rate.[219] Ms. Underwood, who included accounting figures for the note, asked Gibson to execute the amended note and return it to her.[220] Gibson realized at that point that a 50-cent drop in TRX's share price would render him "insolvent."[221]

The next day, Gibson began purchasing $4 TRX put option contracts with an expiration date of November 19 for his personal account and for Francesca Marzullo's account.[222] A put option gives the purchaser of the put the right, but not the obligation, to sell a security at a specified "strike price" (in this case $4) by a specified date.[223] If the price of the underlying security declines below the strike price, the put is "in the money" and the put's purchaser can sell it for a profit. Conversely, if the prices rises above the strike price, the put will expire worthless and the purchaser will only have lost the cost of the put.

On October 27 and 28, Gibson bought a total of 1,604 $4 TRX put contracts in Ms. Marzullo's account, paying approximately $50,000.[224] On October 28, November 2, and November 8, Gibson bought a total of 565 $4 TRX put contracts for his own account, paying approximately $20,000.[225] Each put contract

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[219] Resp't Ex. 117 at 1, 5.

[220] *Id*. at 1; *see* Tr. 1445–46.

[221] Tr. 312–13, 1446–47.

[222] Tr. 300–01, 1446–47; *e.g.* Div. Ex. 102 at 2.

[223] Div. Ex. 184 at 20–22.

[224] Div. Ex. 216 ¶ 31; *see* Div. Ex. 102 at 2–3; Tr. 308.

[225] Div. Ex. 216 ¶ 30; Div. Ex. 99 at 3; Div. Ex. 124 at 3. Gibson also bought some $2 TRX puts on November 10, which he was able to sell later that day for a profit of about $2,500. Div.

covered 100 TRX shares and cost between 30 and 45 cents a share.[226] Gibson did not disclose his put purchases to the Fund or any of its investors, including Hull.[227]

Gibson testified that he purchased protective puts, fearing he might become insolvent, to hedge against a potential loss should TRX decline in value.[228] As Bystrom explained, a protective put acts like an insurance policy.[229] If one is long in a stock, then purchasing puts to cover a percentage of that exposure can "mitigate your loss below the strike price of the option" should the value of the stock decline.[230] Purchasing protective puts could allow an investor "to maintain long exposure, particularly through bouts of volatility."[231] A naked put, on the other hand, is the purchase of a put option by an investor who does not have a long position in the underlying security.[232] For example, if an investor who does not own a stock buys a put contract for that

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Ex. 124 at 3. Although it may be that he timed his purchase and sale of these puts based on knowledge about the Fund's activity, *see* Div. Ex. 184 at 23, Exhibits p. 18; *see also* Div. Ex. 187 at 103, the Division does not press this point or seek disgorgement of the resulting profit, *see* Div. Br. 41.

[226] Tr. 1443; Div. Ex. 99 at 3; Div. Ex. 102 at 2–3; Div. Ex. 124 at 3.

[227] Div. Ex. 187 at 120, 215–16.

[228] Tr. 312–13, 1445–46.

[229] Tr. 1577; *see* Robert J. Aalberts & Percy S. Poon, *Derivatives and the Modern Prudent Investor Rule: Too Risky or Too Necessary?*, 67 Ohio St. L.J. 525, 566 & n.262 (2006).

[230] Tr. 1633.

[231] Tr. 1574.

[232] Tr. 1576–77.

stock and exercises the put when the stock drops, the investor has made money even though the share price has fallen. If the same investor has a long position in the underlying stock even after purchasing puts, the best the investor will do by exercising the puts when the share price falls is mitigate a portion of the overall loss suffered.[233]

When Gibson bought the puts in his personal account, his interest in the Fund equated to over 100,000 shares of TRX.[234] The puts covered 56,500 shares.[235] According to Bystrom, because Gibson was still long in TRX after purchasing the puts, his puts were protective.[236] The Division's experts, Dr. Gibbons and Dr. Taveras,[237] agreed in substance with the definition of a protective put, and acknowledged that Gibson's puts could be characterized as protective puts because of Gibson's long exposure to TRX through the Fund.[238]

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[233] *See* Tr. 1633.

[234] Tr. 1444. Gibson's counsel asserted that Gibson held around 220,000 shares of TRX through his interest in the Fund. *See, e.g.*, Tr. 1063–64. But Gibson stated that although he originally held over 230,000 shares, he only held about "half of those shares" when he purchased the puts. Tr. 1444. Indeed, when Gibson bought puts at the end of October and the beginning of November, the Fund had already liquidated half of its TRX position.

[235] Div. Ex. 216 ¶ 30.

[236] Tr. 1580.

[237] Dr. Taveras is a financial economist at the Commission. Tr. 963. Her report concerns the profits made by Gibson and others on the transactions at issue in this proceeding. Tr. 964–66.

[238] Tr. 918–19, 928–30 (Dr. Gibbons acknowledged that although Gibson did not have any TRX stock in his personal

Although Gibson bought as many puts as he could, he felt in hindsight that he "wildly underhedged [his] risk" because he still lost a lot of money when the Fund liquidated its TRX holdings.[239] Gibson further testified that he bought puts for Francesca Marzullo's account to hedge her father Giovanni Marzullo's exposure to TRX through the Fund.[240] Gibson said he considered Francesca Marzullo's parents as advisory clients of his, and he purchased puts to hedge their TRX exposure because "[t]hey were elderly[,] . . . living on a fixed income[,]" and "had all of their liquid assets in the Fund."[241] Although the puts were really for Ms. Marzullo's parents, Gibson testified that he bought them in Ms. Marzullo's account because he had access to her account.[242] But after Gibson received the proceeds from the sale of Ms. Marzullo's puts on November 10, he continued to trade in her account and lost all of the proceeds from the put sales

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account when he purchased the puts, he intended to hedge his exposure to TRX through the Fund); Tr. 1043, 1060–62 (Dr. Taveras agreed with Gibson's counsel that because Gibson was long in TRX through his exposure to the Fund, his puts could be characterized "as a hedge").

[239] Tr. 312–13, 1447; *see* Div. Ex. 187 at 130–31. The Division emphasizes that in his investigative testimony, Gibson called his put purchases "a short bet" against TRX. Div. Ex. 187 at 118–19; Tr. 301–03. But because Gibson was net long in TRX through his exposure to the Fund's investment, his puts are better characterized as protective. *See* Div. Ex. 187 at 118–20 (agreeing that while in his personal account, he "had a short bet against TRX," he was overall through the Fund "exceptionally long and far longer than anyone else in the Fund").

[240] Tr. 1447–48.

[241] Tr. 1448.

[242] Div. Ex. 187 at 113.

on other options trades.[243] I therefore doubt that Gibson's actions were motivated solely out of concern for the Marzullos as an elderly couple on a fixed income.

When asked the obvious question, Gibson testified that he did not buy puts to hedge the Fund's position because he believed buying puts would not have been a responsible investment for the Fund.[244] The puts cost money, and Gibson said he "expected them to expire worthless."[245] The Fund had already sold about half of its interest in TRX, and given that the Fund was no longer one of the largest owners of the stock, Gibson said that he did not expect the impending sale of the remainder of the Fund's shares to push TRX's stock price down enough to render the puts valuable.[246]

In addition to his own put purchases, Gibson advised his father on November 8 to buy $4 TRX puts, sell the TRX shares he held in a personal IRA account, and then sell the puts.[247] John Gibson was one of his

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[243] Tr. 331, 1507.

[244] Tr. 1450–51. Gibson purchased some $2 and $3 puts for the Fund on the day that the Fund sold the balance of its TRX shares. Div. Ex. 187 at 103; Resp't Ex. 204. But neither party has raised any issue about those puts.

[245] Tr. 1450.

[246] Tr. 1450–51.

[247] Tr. 322–23, 1107–08, 1114, 1243–44, 1253; Resp't Ex. 207; *see* Tr. 1277–79. On November 8, John Gibson spoke with Hull, who reported that "we're going to do something here in Geier." Tr. 1108. John Gibson asked what Hull meant and Hull told John Gibson to "just call Christopher and whatever he tells you to do, you do that." Tr. 1108. So John Gibson called his son who, in a brief conversation, said "get a pen, buy a put, sell the stock, sell the put, do it immediately." Tr. 1108.

son's advisory clients.[248] After speaking to his son, John Gibson phoned his broker, which did not execute the sale of his TRX stock or the purchase of the puts until the next day.[249] When Gibson told his father to execute these transactions, he knew the Fund was planning imminently to sell the remainder of its TRX holdings.[250] Gibson testified that he told his father to buy puts as "a hedge for execution risk."[251] In other words, he wanted his father to sell his personal TRX shares as soon as possible but was afraid the sale transaction would not be executed immediately.[252] Gibson, therefore, told his father to buy puts so he would not lose out if TRX's share price dropped in the interim.[253]

13. The Fund sells the rest of its TRX stock into the market at great loss.

At the beginning of November, the Fund continued to incrementally sell its shares on the market or in negotiated transactions at around market price.[254]

Then, on November 7 or 8, Sands from Casimir contacted Gibson and told him "he had an offer that would make us very pleased."[255] On November 9,

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[248] Tr. 145.

[249] Tr. 1108, 1114–18; Resp't Ex. 191 at 2–3; Resp't Ex. 192 at 1; *see* Tr. 1277–79.

[250] Tr. 322–25.

[251] Tr. 1449.

[252] Tr. 1449.

[253] Tr. 322–24, 1449.

[254] Tr. 879–81, 885, 1455–56; Resp't Ex. 121 (November 8 sale to Sequiera); Resp't Ex. 153 at 1 (summary chart of the Fund's sales).

[255] Tr. 1456.

after the market had closed for the day, Gibson met with Sands and Platinum Partners's CFO, David Levy.[256] In prior meetings with Levy, Gibson had tried to negotiate a sale of the Fund's TRX shares to Platinum.[257] But during the November 9 meeting, Levy instead told Gibson that Platinum would pay the Fund $10,000 a month not to sell any TRX shares for six months.[258] Gibson was "shocked and disappointed," and he told Hull, who was concerned that Platinum was trying to lock up the Fund's shares so it could sell its TRX holdings before the Fund could sell.[259] Hull and Gibson decided to sell the remainder of the Fund's TRX position the next day into the market.[260] Hull and Gibson were hoping that if they sold the Fund's shares, other large TRX investors like Platinum would be forced to buy TRX to prevent the share price from dropping and to protect their own positions.[261] Gibson and Hull hoped that as other investors rushed in to buy the stock, the Fund would lose less money on the shares it sold as the day progressed.[262] But Gibson was aware that his strategy was risky.[263]

On the morning of November 10, Gibson emailed his broker at GarWood and told him to sell, noting,

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[256] Tr. 323–24, 1456.

[257] Tr. 319–21.

[258] Tr. 321, 1457.

[259] Tr. 1457–58.

[260] Tr. 1458–59.

[261] Tr. 1458.

[262] Tr. 658–59, 1458–59.

[263] Div. Ex. 105 at 11858; *see* Tr. 659.

"We are going to potentially tank this stock."[264] Gibson explained that he told this to his broker to signal that there was no need to sell slowly and get best execution prices.[265] Rather, Gibson wanted to sell aggressively to force the other large shareholders to buy the Fund's shares as he had discussed with Hull.[266]

Gibson was half right. His strategy did not work but he did tank the stock. As the Fund sold its remaining 4.9 million shares of TRX into the market, other big investors sold too, and the stock price declined dramatically.[267] TRX fell so fast that the New York Stock Exchange twice briefly halted trading in it.[268] Around 10:00 a.m., when TRX's share price had fallen to approximately $2.00, Gibson sold all of the $4 puts in his account and in Francesca Marzullo's account.[269] The $4 puts from John Gibson's account were also sold that day.[270] The Fund liquidated its TRX holdings for average prices ranging from $3.15 to $1.65 per share.[271] TRX's share price, which had opened at $3.41, went as low as $1.56 and closed at $2.29 on a volume of over 17 million shares traded.[272]

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[264] Div. Ex. 105 at 11585; Tr. 1459–60.

[265] Tr. 1461–62.

[266] Tr. 1461–62.

[267] Tr. 324–25, 659, 1462–63; Div. Ex. 216 ¶ 32.

[268] Tr. 325; Div. Ex. 184 at Exhibits p. 12.

[269] Div. Ex. 123 at 14; Div. Ex. 124 at 3; Div. Ex. 184 at 23, Exhibits p. 18.

[270] Div. Ex. 114 at 46; Div. Ex. 184 at 23; *see* Tr. 1119–20.

[271] Tr. 1051; Div. Ex. 184 at Exhibits p. 11.

[272] Joint Ex. 1 at 5.

Gibson made $81,930 ($81,008.81 after commissions) on the sale of his $4 puts. The puts in Francesca Marzullo's account generated a profit of $254,380 ($251,879.81 after commissions). John Gibson made $43,240 ($41,823.06 after commissions).[273] Even with his profit from the puts, Gibson lost $724,660 in the Fund.[274] Giovanni Marzullo lost $965,318, and Gibson's parents lost $1,399,053.[275]

At some point, possibly as early as mid-February 2012, Gibson spoke with Sequiera by phone.[276] During the call, Gibson used profane and often hyperbolic language to express his anger toward Sinclair.[277] Relevant to this proceeding, Gibson said that Sinclair "lied to [Gibson] for a year," had "taken everything from" Gibson, was "a complete crook," and "screws everyone he deals with."[278]

According to the Division, Gibson's assertion that Sinclair had been lying for a year shows that Gibson knew Sinclair was dishonest in August 2011, when he berated Sinclair but gave investors a more positive view of TRX.[279] But Gibson did not sell his personal shares in August 2011; rather, he remained sufficiently bullish about TRX to decline a liquidation sale at $5.85 per share, advised Hull in September 2011 that he remained "bullish" on TRX, and before

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[273] Tr. 330–31; Div. Ex. 185 at 47; *see* Resp't Ex. 205.

[274] Resp't Ex. 205.

[275] *Id.*; Tr. 1143.

[276] *See* Div. Exs. 183, 183A; *see* Tr. 845–46, 1487.

[277] Div. Ex. 183A; *see* Tr. 847.

[278] Div. Ex. 183A at 3–4, 6.

[279] Tr. 848.

September 23, told Hull the Fund should consider buying more shares. So the record does not show that before November 2011, Gibson thought Sinclair might be lying.[280]

In context, therefore, Gibson's phone conversation supports Hull's observation—relevant to Gibson's August 2011 berating e-mails to Sinclair—that Gibson tended to "rant and rave about different things," and sometimes would "rant and rave about . . . Sinclair in a negative way."[281] The phone call otherwise has little relevance.

14. The Fund shuts down in April 2013.

Gibson continued to manage the Fund until April 2013, when he closed it and returned money to its 13 remaining investors.[282] In his wind-up letter to investors, Gibson admitted that the Fund's performance had been "disastrous" and he accepted full responsibility for its failure.[283] In his testimony, Gibson explained that he and Hull had made bad decisions, such as not accepting the buyout offer for its TRX stock at $5.85 a share in August 2011 and flooding the market with shares on November 10.[284]

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[280] In a sarcastic e-mail sent November 4, 2011, Gibson asked Sinclair whether he'd done a number of things Gibson said Sinclair had promised to do. Div. Ex. 103. Gibson added that if Sinclair did not "fix what you've broken, it will be my life's goal to ensure your children will know you were a crook and the pain you caused so many people all in an effort at self glorification." *Id*.

[281] Tr. 584.

[282] Tr. 334–35; Div. Ex. 154.

[283] *E.g.*, Div. Ex. 154 at 2149.

[284] Tr. 1464–66.

Gibson currently lives in Montevideo, Uruguay, where he works for East Century Capital, Ltd., a Hong Kong consulting firm that advises companies in Africa.[285]

Discussion and Conclusions of Law

The Division alleges that Gibson willfully violated Advisers Act Section 206(1) and (2) by engaging in a transaction that favored Hull over the interests of his advisory client, the Fund, and by engaging in front running transactions that benefited him and persons close to him.[286] I will first consider the allegations under these provisions and then consider whether, as the Division further alleges, Gibson also willfully violated Exchange Act Section 10(b) and Rule 10b-5(a) and (c), and Advisers Act Section 206(4) and Rule 206(4)-8, through the same conduct.[287]

1. *The antifraud provisions of Advisers Act Section 206(1) and (2) impose federal fiduciary standards on investment advisers and require elimination or disclosure of even potential conflicts of interest.*

Advisers Act Section 206 makes it:

> unlawful for any investment adviser, by use of the mails or any means or instrumentality of interstate commerce, directly or indirectly—
>
> (1) to employ any device, scheme, or artifice to defraud any client or prospective client; [or]

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[285] Tr. 1492, 1498, 1502.

[286] OIP ¶¶ 2, 55, 56.

[287] *Id.* ¶¶ 54, 57.

> (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client.[288]

Section 206 "establishes 'federal fiduciary standards' to govern the conduct of investment advisers."[289] As a result, investment advisers "owe their clients 'an affirmative duty of utmost good faith, and full and fair disclosure of all material facts, as well as an affirmative obligation to employ reasonable care to avoid misleading [their] clients.'"[290] To this end, the Act "reflects a congressional recognition 'of the delicate fiduciary nature of an investment advisory relationship,' as well as a congressional intent to eliminate, or at least to expose, all conflicts of interest which might incline as investment adviser—consciously or unconsciously—to render advice which was not disinterested."[291] An adviser must therefore "disclose information that would expose any" actual or potential conflicts of interest with a client.[292] The Commission "has long held that

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[288] 15 U.S.C. § 80b-6(1), (2).

[289] *Transamerica Mortg. Advisors, Inc. v. Lewis*, 444 U.S. 11, 17 (1979) (quoting *Santa Fe Indus. v. Green*, 430 U.S. 462, 471 n.11 (1977)).

[290] *Montford & Co.*, Advisers Act Release No. 3829, 2014 WL 1744130, at *13 (May 2, 2014) (alteration in original) (quoting *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194 (1963)), *pet. denied*, 793 F.3d 76 (D.C. Cir. 2015).

[291] *Capital Gains*, 375 U.S. at 191–92 (quoting Louis Loss, *Securities Regulation* 1412 (2d ed. 1961)).

[292] *Montford*, 2014 WL 1744130, at *13 (quoting *Kingsley, Jennison, McNulty & Morse, Inc.*, Advisers Act Release No. 1396, 1993 WL 538935, at *3 (Dec. 23, 1993)).

'[f]ailure by an investment adviser to disclose potential conflicts of interest to its clients constitutes fraud within the meaning of Section[] 206(1) and (2).'"[293] "It is indisputable that potential conflicts of interest are 'material' facts with respect to clients and the Commission."[294]

To establish liability under Section 206(1), the Division must show that a respondent acted with scienter.[295] A showing of negligence, however, is sufficient to establish a violation of Section 206(2).[296] Scienter may be shown by evidence of recklessness.[297] In this context, recklessness is "an extreme departure from the standards of ordinary care . . . present[ing] a danger of misleading [clients] that is either known to the [actor] or is so obvious that the actor must have

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[293] *Robare Grp. v. SEC*, 922 F.3d 468, 472 (D.C. Cir. 2019) (first alteration in original) (quoting *Fundamental Portfolio Advisors, Inc.*, Securities Act Release No. 8251, 2003 WL 21658248, at *15 & n.54 (July 15, 2003), *pet. denied sub nom. Brofman v. SEC*, 167 F. App'x 836 (2d Cir. 2006)).

[294] *Vernazza v. SEC*, 327 F.3d 851, 859 (9th Cir. 2003). A misstatement is material if there is a substantial likelihood that a reasonable investor would view "disclosure of the omitted fact . . . as having significantly altered the 'total mix' of information made available." *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 38 (2011) (quoting *Basic Inc. v. Levinson*, 485 U.S. 224, 231–32 (1988)).

[295] *Montford*, 2014 WL 1744130, at *14; *see SEC v. Steadman*, 967 F.2d 636, 641 & n.3 (D.C. Cir. 1992).

[296] *Montford*, 2014 WL 1744130, at *14.

[297] *Id.* at *14 n.108.

been aware of it."[298] "Negligence is the failure to exercise reasonable care."[299]

2. Gibson was an investment adviser to the Fund and used instrumentalities of interstate commerce.

Section 206 only applies to investment advisers.[300] An investment adviser is "any person who, for compensation, engages in the business of advising others . . . as to the advisability of investing in, purchasing, or selling securities."[301]

Gibson was the managing director of both the Fund's managing member, Geier Capital, and the Fund's investment manager, Geier Group, while those entities existed.[302] He acknowledged that he provided investment advisory services to the Fund.[303] He devised the strategy of investing in TRX,[304] negotiated purchases and sales with brokers and counterparties,[305] communicated with Fund investors

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[298] *Id.* (final alteration in original) (quoting *David Henry Disraeli*, Securities Act Release No. 8880, 2007 WL 4481515, at *5 (Dec. 21, 2007), *pet. denied*, 334 F. App'x 334 (D.C. Cir. 2009)).

[299] *IFG Network Sec., Inc.*, Exchange Act Release No. 54127, 2006 WL 1976001, at *11 (July 11, 2006).

[300] 15 U.S.C. § 80b-6.

[301] 15 U.S.C. § 80b-2(a)(11); *see Abrahamson v. Fleschner*, 568 F.2d 862, 871 (2d Cir. 1977) (holding that advice can take the form of "exercising control over what purchases and sales are made with their clients' funds").

[302] Div. Ex. 22 at 1, 12; Div. Ex. 23 at 1, 12; Div. Ex. 24 at 1.

[303] Tr. 184, 186, 187, 335 (admitting provision of advisory services both before and after dissolution of Geier Group); *see* Tr. 570 (Hull agreeing).

[304] Tr. 575, 1367.

[305] *See, e.g.*, Resp't Exs. 62, 92.

regarding the Fund's future performance,[306] and held himself out as an adviser to regulators.[307] For these services, he was paid a salary through April 2013 and, through Geier Group, was entitled to annual management fees and incentive allocations even if he did not receive them once the Fund started to fail.[308] For these reasons, Gibson meets the statutory definition of an investment adviser to the Fund.[309]

Liability under Section 206 requires that the adviser make "use of the mails or any means or instrumentality of interstate commerce."[310] This element is satisfied because when Gibson engaged in the problematic trading activities and the transaction with Hull, he used the telephone, e-mail, and the internet.[311]

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[306] *See, e.g.*, Resp't Ex. 51.

[307] *See, e.g.*, Div. Exs. 31, 39, 70, 71.

[308] Tr. 246–52, 334–35; Div. Exs. 43, 128, 147, 156; Div. Ex. 24 at 2.

[309] *See SEC v. Fife*, 311 F.3d 1, 11 (1st Cir. 2002) (finding that an investment adviser received compensation when "he understood that he would be compensated for his efforts by a commission based on a percentage of the profits from the investments, *if successful*"); *SEC v. Ahmed*, 308 F. Supp. 3d 628, 652–53 (D. Conn. 2018) (finding a similar involvement in recommending investment opportunities and in negotiating the terms of transactions to be sufficient to establish that the defendant was an investment adviser); *Timothy S. Dembski*, Advisers Act Release No. 4671, 2017 WL 1103685, at *10 n.33 (Mar. 24, 2017), *pet. denied*, 726 F. App'x 841 (2d Cir. 2018).

[310] 15 U.S.C. § 80b-6.

[311] *Larry C. Grossman*, Securities Act Release No. 10227, 2016 WL 5571616, at *4 n.11 (Sept. 30, 2016), *vacated as to certain sanctions*, 2019 WL 2870969 (July 3, 2019).

3. Elimination or disclosure of conflicts where the client is a hedge fund.

Investment advisers owe their clients a duty of full disclosure.[312] But Gibson's advisory client was the Fund, not its individual investors.[313] Indeed, the Division conceded that although the Fund was Gibson's advisory client, the Fund's investors were not Gibson's advisory clients simply by virtue of their investment in the Fund.[314] The Fund, however, was a mere legal entity with no independent decision-makers. Gibson was therefore essentially "in the perverse position" of disclosing conflicts or potential

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[312] *Montford*, 2014 WL 1744130, at *13.

[313] *See Goldstein*, 451 F.3d at 881 (a hedge fund "adviser owes fiduciary duties only to the fund, not to the fund's investors," because "[i]f the [individual] investors are owed a fiduciary duty and the entity is also owed a fiduciary duty, then the adviser will inevitably face conflicts of interest"). To be clear, Gibson had separate advisory relationships with his parents and the Marzullos, but those relationships had nothing to do with any investment in the Fund those individuals might have had. *See* Tr. 804; Inv. Adviser Advertisements; Comp. for Solicitations, 84 Fed. Reg. 67,518, 67,527 & n.66 (Dec. 10, 2019) (noting that an "adviser's 'clients' . . . are the pooled investment vehicles themselves" and explaining that "[t]here are circumstances under which an investor in a pooled investment vehicle is also a client of the investment adviser" such as "when the investor has its own investment advisory agreement with the investment adviser"). In this regard, *Goldstein*, "did not hold that no hedge fund adviser could create a client relationship with an investor," *United States v. Lay*, 612 F.3d 440, 446–47 (6th Cir. 2010), and the OIP could be read as alleging that Gibson breached duties as to other clients as well as the Fund, *see*, *e.g.*, OIP ¶ 2. The Division, however, has focused on the allegation that Gibson breached his fiduciary duties to the Fund. *See*, *e.g.*, Div. Br. 1–2, 12; Tr. 804.

[314] Tr. 804.

conflicts to himself as the client's agent.[315] This sort of disclosure to himself, which would have amounted to no disclosure at all, could not have been sufficient.[316]

Because this is the case, the question is to whom Gibson should have made disclosures once conflicts of interest arose. Arguably, disclosure to investors in the Fund would not have been sufficient, and could have even been harmful. The interests of individual investors could have easily been drawn into conflict with the Fund's interests.[317] Moreover, individual investors had no decision-making authority for the Fund, and no meaningful recourse had they known of

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[315] J. Tyler Kirk, *A Federal Fiduciary Standard Under the Investment Advisers Act of 1940: A Refinement for the Protection of Private Funds*, 7 Harv. Bus. L. Rev. Online 19, 20 (2016).

[316] *See id.* Gibson has not argued that disclosure to himself as an agent of the Fund would have been sufficient to remedy any conflict that arose, nor is such an argument viable. *See id.* at 28–31 & n.77 (arguing that an agent's knowledge should not be imputed to the principal when the principal is the agent's intended victim); *Kirschner v. KPMG LLP*, 938 N.E.2d 941, 952 (N.Y. 2010) ("[T]he presumption that an agent will communicate all material information to the principal operates except in the narrow circumstance where the corporation is actually the victim of a scheme undertaken by the agent to benefit himself."); *see also* Div. Ex. 185 at 20 (Dr. Gibbons opined that "it was not adequate that the intended misconduct of Gibson as adviser was known to Gibson as managing member. Gibson's own knowledge of his plans to engage in improper conduct cannot be attributed to the Fund or its investors.").

[317] *See Goldstein*, 451 F.3d at 881. For example, a disclosure that Gibson intended to sell his personal shares of TRX due to a potential conflict with the Fund's impending block sale could have caused other investors to attempt to sell their personal shares, which in turn could have adversely affected TRX's share price or limited the Fund's ability to later sell its shares.

Gibson's intended actions. The operating memorandum limited their ability to even withdraw money and permitted Geier Capital to suspend their right to withdrawal under certain conditions.[318]

For these reasons, because the transactions Gibson intended to effectuate posed conflicts or potential conflicts of interest, he should have refrained from engaging in those transactions or, failing that, established an appropriate disclosure mechanism through which a disinterested committee or person could have independently evaluated those conflicts and transactions on behalf of the Fund.[319] Thus, in Gibson's circumstances, a failure to obtain independent advice or abstain from a transaction in

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[318] Div. Ex. 24 at 3, 16, 20–22.

[319] Independent disclosure mechanisms may involve, for example, disclosure to an independent conflicts committee or an independent person in management to evaluate the conflict and render a decision for the Fund. *See SEC v. DiBella*, 587 F.3d 553, 568 (2d Cir. 2009); Asset Managers' Committee, Best Practices For The Hedge Fund Industry 42, 48–49 (2008), https://www.treasury.gov/press-center/press-releases/Documents/amcreportapril152008.pdf; Div. Ex. 185 at 20. As "[c]onflicts are inherent in the asset management business as in many other financial services businesses," a fund "[m]anager should adopt policies and procedures to identify and address potential conflicts of interest that may arise in its specific businesses" and "establish a Conflicts Committee." Best Practices at 47–48. Typically, a fiduciary must seek independent, disinterested advice when he or she has divided loyalties or lacks the ability to make the decision at hand. *Accord Leigh v. Engle*, 727 F.2d 113, 132 (7th Cir. 1984) (addressing ERISA fiduciaries with divided loyalties).

the event of even a potential conflict would constitute a violation of the Advisers Act.[320]

4. Front running in the investment adviser context.

The Division argues that Gibson is liable for front running.[321] "Frontrunning may be generally defined as involving trading a stock, option, or future while in possession of non-public information regarding an imminent block transaction that is likely to affect the price of the stock, option, or future."[322] As is the case with insider trading, there is no specific statute or regulation prohibiting front running. But unlike insider trading, which courts have long addressed under the federal securities laws, there is little case

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[320] *See Capital Gains*, 375 U.S. at 191 (an adviser must "eliminate, or at least . . . expose" all potential conflicts of interest).

[321] Div. Posthearing Br. at 4–7, 16–20, 26–27.

[322] Memorandum Prepared by the Division of Market Regulation in Response to the Questions Contained in the Letter of March 4, 1988, from the Honorable John D. Dingell and the Honorable Edward J. Markey Regarding Short Selling and Frontrunning 11 (May 13, 1988), http://www.sechistorical.org/museum/papers/1980/page-14.php (scroll to May 13); *see* Lewis D. Lowenfels & Alan R. Bromberg, *Securities Market Manipulations: An Examination and Analysis of Domination and Control, Frontrunning, and Parking*, 55 Alb. L. Rev. 293, 313 (1991); *see also John R. D'Alessio*, Exchange Act Release No. 47627, 2003 WL 1787291, at *2 (Apr. 3, 2003) (stating that a broker who times "the purchase or sale of shares of a security for his own account so as to benefit from the price movement that follows execution of large customer orders, [engages in] a practice commonly known as trading ahead or frontrunning"), *pet. denied*, 380 F.3d 112 (2d Cir. 2004).

law addressing front running under the antifraud provisions of federal securities law.[323]

In *Capital Gains*, the Supreme Court found that scalping, a manipulative technique related to front running, violated the Advisers Act.[324] An investment adviser purchased shares of a stock for his own account, recommended the security to his clients, and

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[323] *See* Thomas A. Russo & Marlisa Vinciguerra, *Financial Innovation and Uncertain Regulation: Selected Issues Regarding New Product Development*, 69 Tex. L. Rev. 1431, 1527–28 (1991); Lowenfels & Bromberg, 55 Alb. L. Rev. at 313–21, 337; *see, e.g.*, *SEC v. Yang*, 795 F.3d 674, 680 (7th Cir. 2015) (declining to reach defendant's argument that front running should never be considered fraudulent conduct under Section 10(b) and Rule 10b-5 because he had failed to preserve the issue). The Commission has largely left it to self-regulatory organizations—most recently the Financial Industry Regulatory Authority, Inc. (FINRA)—to regulate front running. *See, e.g.*, Self-Regulatory Organizations; FINRA; Order Approving Proposed Rule Change, as Modified by Amendment No. 1, To Adopt Existing NASD IM-2110-3 as New FINRA Rule 5270 (Front Running of Block Transactions) With Changes in the Consolidated FINRA Rulebook, 77 Fed. Reg. 55,519, 55,522 (Sept. 10, 2012) (approving adoption of FINRA Rule 5270); *D'Alessio*, 2003 WL 1787291, at *3, *7–9 (affirming a violation of NYSE Rule 92 prohibiting front running); *E.F. Hutton & Co.*, Exchange Act Release No. 25887, 1988 WL 901859, at *1, *4 (July 6, 1988) (affirming a violation of NASD rules); *Smith, Barney, Harris Upham & Co.*, Exchange Act Release No. 21242, 1984 WL 472586, at *3–4 (Aug. 15, 1984) (affirming a finding by AMEX). Private firms often also have codes of ethics prohibiting front running. *See, e.g.*, Div. Ex. 185 at 22 n.41 (Dr. Gibbons noted in his report that Deutsche Bank, Gibson's former employer, explicitly prohibited front running).

[324] *Capital Gains*, 375 U.S. at 181, 196–97; *see* David M. Bovi, *Rule 10b-5 Liability for Front-Running: Adding A New Dimension to the "Money Game"*, 7 St. Thomas L. Rev. 103, 106–07 (1994) (noting that scalping is sometimes confused with front running, but that the two practices are different).

then immediately sold his personal shares at a profit upon the stock's gain due to his buy recommendation.[325] The Court held that one who

> secretly trades on the market effect of his own recommendation may be motivated—consciously or unconsciously—to recommend a given security not because of its potential for long-run price increase (which would profit the client), but because of its potential for short-run price increase in response to anticipated activity from the recommendation (which would profit the adviser).[326]

The Advisers Act required the "adviser to make full and frank disclosure of his practice of trading on the effect of his recommendations," and his failure to do so was fraud.[327]

The conflict of interest in *Capital Gains* between the adviser and his clients is clear. As one commentator has noted: "Scalpers seek to move the market price of a security by triggering client investment action and to profit by taking action opposite to the clients immediately after the movement."[328] In a sense, "Scalping is little more than price manipulation as an end in itself."[329] Front running "is less blatant a breach of the duty of loyalty

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[325] *Capital Gains*, 375 U.S. at 181.

[326] *Id.* at 196.

[327] *Id.* at 196–97.

[328] Harvey E. Bines & Steve Thiel, *Investment Management Law and Regulation* 807 (2d ed. 2004).

[329] *Id.*

than scalping," but is still a "deliberate subordination of the client's interest."[330]

Cases have usually analyzed front running as a violation of a broker's duty of best execution, since the price obtained for the customer's order may not be as favorable as it would have been had the customer's order been executed first.[331] Whether or not the price obtained for a client order would have been the best price but for the investment adviser's front running is, however, not a dispositive consideration. Under the Advisers Act, it is immaterial whether the conduct actually harmed the client or whether the adviser intended to harm the client.[332] Investment advisers are fiduciaries "governed by the highest standards of conduct."[333] An investment adviser has not only a duty of best execution,[334] but also a duty of undivided

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[330] *Id.*

[331] *See, e.g.*, *United States v. Dial*, 757 F.2d 163, 168–69 (7th Cir. 1985) (analyzing a broker's practice of trading ahead of client under mail and wire fraud statutes); *D'Alessio*, 2003 WL 1787291, at *3–4 (analyzing a broker's practice of trading ahead of a client under NYSE Rules).

[332] *See Capital Gains*, 375 U.S. at 192.

[333] *Fundamental Portfolio Advisors*, 2003 WL 21658248, at *15 (quoting *Victor Teicher & Co.*, Exchange Act Release No. 40010, 1998 WL 251823 (May 20, 1998), *pet. granted in part on other grounds*, 177 F.3d 1016 (D.C. Cir. 1999)); *see also Montford*, 2014 WL 1744130, at *13 ("The 'fundamental purpose of [the Advisers Act is] to substitute a philosophy of full disclosurefor the philosophy of caveat emptor and thus . . . achieve a high standard of business ethics in the securities industry.'" (quoting *Capital Gains*, 375 U.S. at 186) (alterations in original)).

[334] *See Clarke T. Blizzard*, Advisers Act Release No. 2253, 2004 WL 1416184, at *2 (June 23, 2004).

loyalty[335] and an affirmative duty of utmost good faith and must eliminate or expose even potential conflicts of interest.[336]

The exact contours of front running need not be defined to capture or contemplate every form of misconduct. Here, it suffices to say that there is a potential conflict of interest when an investment adviser's personal trading or recommendation to close friends or relatives coincides with the adviser's possession of confidential information about a client's forthcoming trading plans in the same security. An adviser is "not entitled to benefit from the fiduciary relationship except to the extent provided for by fees and compensation the client expressly consents to pay."[337]

Absent the client's consent, it is a breach of an adviser's fiduciary duties to use confidential client information to benefit himself or others—whether to avoid losses or realize gains.[338] Moreover, front

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[335] *See IMS/CPAs & Assocs.*, Securities Act Release No. 8031, 2001 WL 1359521, at *8 (Nov. 5, 2001), *pet. denied sub nom. Vernazza v. SEC*, 327 F.3d 851 (9th Cir. 2003).

[336] *See Capital Gains*, 375 U.S. at 194; *Montford*, 2014 WL 1744130, at *13; *Fundamental Portfolio Advisors*, 2003 WL 21658248, at *15. "One activity specifically mentioned and condemned by investment advisers" leading up to the passage of the Advisers Act "was trading by investment [advisers] for their own account in securities in which their clients were interested." *Capital Gains*, 375 U.S. at 189. Although the Supreme Court did not go as far as to say that all such personal trading is prohibited, there is little doubt that it could lead to conflicts of interest. *See id.* at 196.

[337] *Feeley & Willcox Asset Mgmt. Corp.*, Securities Act Release No. 8249, 2003 WL 22680907, at *12 (July 10, 2003).

[338] *See Thomas W. Heath, III*, Exchange Act Release No. 59223, 2009 WL 56755, at *4 (Jan. 9, 2009) (observing that the

running can potentially undermine the client's interests or involve conflicting motivations that cannot be adequately judged in hindsight. For example, the adviser might usurp a trading opportunity that otherwise should have gone to the client. Or the adviser's front running, even in small quantities, could cause unexpected price movements in a thinly traded stock. The adviser could also be motivated, even in part, to execute a client's block trade so that he or someone close to him can realize gains before the expiration date of previously purchased put option contracts in the same security. None of these scenarios need be proven or realized, however. The point is that front running poses the potential for the adviser's outside interests to conflict

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duty to maintain confidentiality of client information, which "is grounded in fundamental fiduciary principles," is "one of the most fundamental ethical standards in the securities industry"), *pet. denied*, 586 F.3d 122 (2d Cir. 2009); Restatement (Third) of Agency § 8.01 (2006) ("Unless the principal consents, the general fiduciary principle . . . requires that an agent refrain from using the agent's position or the principal's property to benefit the agent or a third party."); *id.* § 8.05 (setting forth an agent's duty "not to use or communicate confidential information of the principal for the agent's own purposes or those of a third party," and stating that "it is a breach of an agent's duty to use confidential information of the principal for the purpose of effecting trades in securities although the agent does not reveal the information in the course of trading"). The same principle is expressed in case law on insider trading. *See United States v. O'Hagan*, 521 U.S. 642, 652 (1997) ("[A] fiduciary's undisclosed, self-serving use of a principal's information to purchase or sell securities, in breach of a duty of loyalty and confidentiality, defrauds the principal of the exclusive use of that information."); *Dirks v. SEC*, 463 U.S. 646, 662 (1983) ("[A] purpose of the securities laws was to eliminate 'use of inside information for personal advantage.'" (quoting *Cady, Roberts & Co.*, Exchange Act Release No. 6668, 1961 WL 60638, at *4 n.15 (Nov. 8, 1961))).

with those of the client. This makes the practice especially problematic.[339]

Given the potential conflict in this context, the client must be permitted to evaluate the adviser's "overlapping motivations" and "decid[e] whether an adviser is serving 'two masters' or only one."[340] And if the client does not consent, then the adviser must abstain from his outside trading or recommendations to others. Requiring anything less—or subjecting the client's interests to hindsight analysis—would undermine the Advisers Act's manifest purpose.

5. Gibson's trading ahead of the Fund violated fiduciary duties and posed potential conflicts of interest.

Gibson's sale of personal shares on September 26, 2011, constituted a fraud in violation of the Advisers Act. When he sold, he was actively negotiating a block sale of millions of shares of the Fund's TRX position. The particulars of that impending sale was not known to anyone but Gibson, his broker Sands, and maybe

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[339] In discussing conflicts in the investment-adviser context, the Supreme Court relying on precedent on the problems that flow from contingent-fee arrangements for obtaining government contracts, noted that a person "who occupies confidential and fiduciary relations toward another" should remove "any temptation" to violate those trust relations. *Capital Gains*, 375 U.S. at 196 n.50 (quoting *United States v. Miss. Valley Generating Co.*, 364 U.S. 520, 550 n.14 (1961)). The Court further posited: "The objection rests in their tendency, not in what was done in the particular case. The court will not inquire what was done. If that should be improper it probably would be hidden, and would not appear." *Id.* (ellipses omitted) (quoting *Miss. Valley Generating*, 364 U.S. at 550 n.14).

[340] *Id.* at 196.

Hull, rendering the information non-public.[341] Gibson testified that he sold his personal shares and those of his girlfriend to earn some liquidity, but the timing of the sale suggests that he was attempting to avoid potential losses by selling the shares ahead of the Fund's impending block sale. Perhaps he was concerned that the Fund's block sale, even though it was negotiated in the upstairs market, could lower TRX's share price.[342] But whatever the reason, he should not have engaged in outside trading while negotiating his client's trades in the same security. As discussed earlier, the Fund lacked any independent disclosure mechanism to evaluate Gibson's outside activities. He failed to fully consider—and lacked the independence to consider—the impact that his personal trading may have had on the Fund. In trading when he did, Gibson breached his fiduciary duties to his client and created a potential conflict of interest. Whether or not, in hindsight, his actions actually harmed the Fund is irrelevant.

Gibson's purchase of put options for himself and in Francesca Marzullo's account, and his recommendation to his father to purchase puts also

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[341] Although market participants knew that the Fund was willing to consider offers for its TRX shares because Gibson previously sought to sell the Fund's TRX shares at the end of August, this fact does not change the confidential nature of the block sale on September 27, 2011. *See* Resp't Br. 21. No one aside from Gibson and his broker knew exactly what the Fund intended to do or when, even if some knew that the Fund was willing to negotiate a transaction.

[342] *See* Tr. 1022; *cf.* Div. Ex. 187 at 108 (Gibson acknowledged that large sales of a stock—at least ones into the market—generally lowered its share price).

constituted a fraud. When he purchased the puts, he used the Fund's confidential information that it was in the process of liquidating its TRX holdings for his own potential advantage and the advantage of those close to him. The Fund never waived the use of its information for its adviser's personal advantage. Moreover, by all appearances, when Gibson bought $4 puts for himself and others but not for the Fund, he was favoring his own position over his client's. He explained at the hearing why he did this: puts are not free, and he had assessed that the Fund should not take on the additional financial burden because the puts might have expired worthless.[343] Still, he lacked the independence necessary to evaluate the conflict between the position he was taking for himself and those close to him versus the one appropriate for the Fund.[344] Finally, at the same time as he was negotiating the Fund's sale, Gibson was seeking to mitigate losses through a hedging strategy of buying put options. He thus lacked the independence to decide the appropriate timing of the Fund's

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[343] Tr. 1450–51.

[344] *See* Commission Interpretation Regarding Standard of Conduct for Investment Advisers, 84 Fed. Reg. 33,669, 33,677 (July 12, 2019) ("When allocating investment opportunities among eligible clients, an adviser may face conflicts of interest either between its own interests and those of a client or among different clients. If so, the adviser must eliminate or at least expose through full and fair disclosure the conflicts associated with its allocation policies, including how the adviser will allocate investment opportunities, such that a client can provide informed consent."); *see also Montford*, 2014 WL 1744130, at *16 ("The soundness of [an adviser's] investment advice is irrelevant to their obligation to be truthful with clients and to disclose a conflict of interest").

liquidation of its TRX position, as that decision could significantly affect the value of those puts.

On each occasion, Gibson's misconduct demonstrated scienter. Even though he never intended to harm the Fund, he was a licensed securities professional who was well aware of his fiduciary responsibilities.[345] And he knew that front running was a problematic practice.[346] In this context, Gibson's decision to use the Fund's non-public information to protect his and others' investments was "an extreme departure from the standards of ordinary care" which created conflicts with his duties "so obvious" that he "must have been aware of" them.[347]

Contrary to Gibson's argument, the disclosures in the offering documents were insufficient to alert investors to the potential conflicts created by Gibson's front running.[348] The offering memorandum allowed Gibson to invest in the same securities as the Fund, advise his other clients in ways that differed from his advice to the Fund, and conduct business in competition with the Fund.[349] It noted that Gibson might have conflicts of interest when effecting transactions for the Fund and when transacting in other entities in which he had a financial interest.[350] But "for disclosure to be full and fair, it should be

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[345] Tr. 77–78.

[346] *See* Div. Ex. 68; Tr. 235–36, 1426–27.

[347] *Montford*, 2014 WL 1744130, at *14 n.108 (quoting *Disraeli*, 2007 WL 4481515, at *5).

[348] Resp't Br. at 19–20.

[349] Div. Ex. 24 at 19.

[350] *Id.*

sufficiently specific so that a client is able to understand the material fact or conflict of interest and make an informed decision whether to provide consent."[351] The offering memorandum speaks in generalities. It was not specific enough to disclose that Gibson might front run the Fund for his own personal advantage and the advantage of those close to him. The Fund did not consent to Gibson's behavior nor were there any conflict resolution mechanisms in place.[352]

As a result of his front running, Gibson violated Advisers Act Section 206(1) and 206(2).

6. Gibson violated fiduciary duties when he arranged the Fund's purchase of Hull's shares.

On October 18, 2011, during the period when Gibson and Hull were trying to sell the Fund's entire position in TRX, Gibson had the Fund purchase 680,636 TRX shares from Hull for the closing market price that day. Hull was not charged a commission, but the Fund paid a commission when it later sold Hull's shares together with its remaining TRX shares in a market transaction. The Division argues that Gibson had a conflict of interest that he recklessly failed to disclose when he executed the Hull transaction.[353]

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[351] Commission Interpretation, 84 Fed. Reg. at 33,676.

[352] Investors essentially gave Gibson control over how conflicts would be managed, as the offering documents lean on his expertise and provide no mechanism for conflict disclosure or remediation should one arise. *See* Div. Ex. 24 at 17. If anything, this makes Gibson's decision to breach the investors' trust and front run the Fund even more problematic.

[353] Div. Br. 20–26.

The Division claims that Gibson burdened the Fund with additional TRX shares at a time when he was trying to sell the Fund's position in TRX, and that the only plausible explanation was that Gibson intended to benefit Hull at the Fund's expense.[354] The evidence, however, shows that Gibson suggested consolidating Hull's TRX shares with the Fund's because he believed that it might put the Fund in a better position to liquidate its TRX position.[355] As noted earlier, Bystrom opined that consolidating shares made block transactions easier because buyers would then know that no shares were being left behind.[356] Gibson's experiences with Sequiera and Sands provided examples of this, although those experiences also show that the Fund did not necessarily need to purchase Hull's shares for them to be sold as a block.[357] In short, it is true, as the Division maintains, that Hull's shares did not necessarily need to be consolidated with the Fund's in one account to facilitate their sale,[358] but because Gibson was the one to suggest the consolidation, the Division has not established that he lacked a good-faith belief that it would be helpful *to the Fund*. I cannot retrospectively critique Gibson's judgment on the current record.

But this does not mean that the transaction was free of conflicts of interest. As the Division argues, when Gibson arranged the trade with Hull on the

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354 *Id.* at 20–21, 24–25.

355 *See* Div. Ex. 94.

356 Tr. 1567; Resp't Ex. 228 at 6.

357 Resp't Ex. 62 at 1; Resp't Ex. 93 at 1–2; Tr. 1404–05.

358 Div. Reply at 9–10.

Fund's behalf, Gibson owed Hull over $600,000 and Hull was paying Gibson's salary for advising the Fund.[359] Gibson had a clear and obvious conflict of interest. His impartiality in arranging any purchase from Hull for the Fund would thus be questionable, regardless of the transaction's merit. In fact, Gibson testified that he was acting as an adviser to both Hull and the Fund on this transaction.[360] This is the kind of situation where an advisory client must "be permitted to evaluate such overlapping motivations, through appropriate disclosure, in deciding whether an adviser is serving 'two masters' or only one."[361]

As mentioned earlier, the Fund lacked any independent disclosure mechanism. It is not possible to say how disclosure by Gibson would have played out. It's also not possible to say on the current record that the Fund's purchase of Hull's shares harmed the Fund or that it lacked a legitimate purpose. The problem is not that Gibson caused the Fund to buy Hull's shares but rather that he did so while operating

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[359] Div. Br. 23–24; Div. Reply at 9.

[360] Tr. 261.

[361] *Capital Gains*, 375 U.S. at 196; *cf. Frey v. Fraser Yachts*, 29 F.3d 1153, 1156 (7th Cir. 1994) (a broker and fiduciary "cannot act as the representative for both buyer and seller in the same transaction unless both parties are fully aware of such dual representation and consent to it" and must "disclose to each all facts which he knows or should know would reasonably affect the judgment of each in permitting such dual agency" (quoting *Quest v. Barge*, 41 So.2d 158, 160 (Fla. 1949))); *UBS AG, Stamford Branch v. HealthSouth Corp.*, 645 F. Supp. 2d 135, 144 (S.D.N.Y. 2008) (explaining that under New York law, a fiduciary violates his duty if he "omits to disclose any interest which would naturally influence his conduct").

under a serious, undisclosed conflict of interest.[362] It thus suffices to say that Gibson's conduct failed to account for the potential conflict of interest and he failed to take measures to remedy or eliminate the conflict before executing the transaction.

Gibson's conduct was reckless. He knew of his fiduciary responsibilities. It should have been obvious to him that a transaction with Hull, to whom he owed so much money and on whose salary payments he depended, conflicted with his duties to the Fund. Again, it does not matter whether Gibson believed the transaction would promote the Fund's interest. There were still obvious conflicts that Gibson recklessly disregarded in carrying out the Hull transaction.

I reject, however, the Division's arguments that the Hull transaction violated the terms of the Fund's offering memorandum. The Division asserts that the sale was not done "at the current market price" as required.[363] But TRX closed at $3.60 that day and the Fund purchased at $3.60 per share. The transaction was thus in accordance with the plain meaning of words "current market price."

The Division also contends that the transaction contravened the offering memorandum because the Fund paid an extra commission to sell Hull's shares when it liquidated its holdings on November 10.[364]

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[362] It is true that Hull sold without giving a block discount or paying a commission. But, as explained below, it's not clear that the lack of a block discount was problematic, and the failure to charge a commission was marginal compared to the conflict of interest.

[363] Div. Ex. 24 at 19; Div. Br. 21–22.

[364] Div. Br. 22–23.

But the offering memorandum proscribed only "extraordinary brokerage commissions . . . in connection with . . . [a] transaction," and not "customary transfer fees or commissions."[365] Even if the commission paid on November 10 can be considered "in connection with" the purchase of Hull's shares on October 18— an issue I do not decide—there is no evidence that it was not a "customary" commission usually charged for such transactions, let alone evidence that it was "extraordinary."

The Division argues that notwithstanding the offering memorandum, $3.60 per share was not the appropriate price for this transaction.[366] As noted above, if Hull had sold his shares into the market instead of to the Fund, then given the stock's trading volume, it would likely have depressed TRX's share price and he would not have been able to sell for $3.60 per share.[367] But Hull did not sell his shares into the market, and the Division has not shown that a block discount is always appropriate in upstairs-market transactions like this one.[368] Even if some discount

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[365] Div. Ex. 24 at 19.

[366] Div. Br. 21–22; Div. Reply at 10–11.

[367] *See supra* at 24–25.

[368] The Division tried to show that on several occasions when the Fund sold its shares in the upstairs market, it had to give a block discount, but Gibson demonstrated that this was untrue. Tr. 265–78. Even though Dr. Gibbons opined that the Fund did not purchase Hull's shares at the current market price—because the sale did not occur in the market—he did not specifically say that Gibson should have obtained a block discount for the Fund in the Hull transaction. *See* Tr. 945–46, 950–52. And Bystrom said that the appropriateness of a block discount depends on the situation, and sometimes buyers pay a premium to buy a stock. Tr. 1628, 1630.

was warranted, it is not apparent what price would have been more appropriate. Dr. Gibbons opined that Gibson could have hired a valuation expert to determine fair market value, but presumably such experts charge for their services.[369] I cannot determine on this record whether it would have been more cost effective for the Fund to hire an expert to value the shares at a discount or just to pay the market price of $3.60 a share. Maybe, as Dr. Gibbons opined, the Fund could have bought Hull's stock slowly over time in the market, and then each transaction would have been at market price.[370] But nothing required the Fund to structure the transaction in this manner. In any event, whether or not the Fund charged Hull the wrong price, Gibson was reckless in ignoring the conflicts inherent in the transaction.

Finally, the Division argues that because the Fund charged Hull no commission, the transaction allowed Hull to avoid paying a commission when the Fund ultimately sold his shares along with its own, and this needlessly favored Hull.[371] The Division is right about this. Even though Gibson concluded that it was in the Fund's best interest to purchase Hull's shares, he should have conducted the sale in a manner that did not favor Hull in any manner. Because it was likely that the Fund would pay a commission when it sold its shares into the market, Gibson should have recouped those costs for the Fund by charging Hull a commission when purchasing his shares or disclosed

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[369] Tr. 951.

[370] *See* Tr. 950–51.

[371] Div. Br. 22–23; Div. Reply 11.

what he was doing.[372] Yet, the Fund paid at most $6,866 extra to sell Hull's shares, of which Hull effectively paid more than 80% because of his ownership stake in the Fund.[373] Gibson's failure to disclose this aspect of the transaction only marginally adds to his reckless behavior surrounding this transaction.

Accordingly, Gibson violated Advisers Act Section 206(1) and (2) for his conduct related to the Hull transaction.

7. Gibson violated Exchange Act Section 10(b) and Rule 10b-5.

The Division also alleges that Gibson's front running and the Hull transaction violated Exchange Act Section 10(b) and Rule 10b-5(a) and (c).[374] Section 10(b) prohibits any person, using any means or instrumentality of interstate commerce or the mails, "[t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance" that contravenes Commission rules promulgated under this section.[375] Rule 10b-5(a) and (c) prohibit any person, directly or indirectly, from "employ[ing] *any* device, scheme, or artifice to defraud," and from "engag[ing] in *any* act, practice, or course of business which operates or would operate as a fraud or deceit upon any person."[376] The

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[372] Indeed it seems that the offering memorandum would have permitted the Fund to charge Hull a "customary" commission. *See* Div. Ex. 24 at 19.

[373] *See supra* at 25; *see also supra* nn. 205–06.

[374] OIP ¶ 54; Div. Br. 34–36.

[375] 15 U.S.C. § 78j(b).

[376] 17 C.F.R. § 240.10b-5(a), (c) (emphasis added).

terms used in Rule 10b-5(a) and (c) "'provide a broad linguistic frame within which a large number of practices may fit'" and "connote a broad proscription against conduct that deceives or misleads another."[377] The Division must demonstrate scienter to establish any violation of Section 10(b) and Rule 10b-5.[378]

Gibson's conduct involved interstate commerce and the purchase and sale of TRX stock. As to whether his actions were a fraudulent scheme or practice, "for the purpose of rule 10(b)-5, an investment adviser is a fiduciary and therefore has an affirmative duty of utmost good faith to avoid misleading clients. This duty includes disclosure of all material facts and all possible conflicts of interest."[379] And "nondisclosure in violation of a fiduciary duty involves 'feigning fidelity' to the person to whom the duty is owed and is therefore deceptive."[380] Gibson breached his duty to the Fund because he recklessly failed to disclose or otherwise remediate his conflicts of interest.[381] This deceptive and fraudulent conduct violated Exchange Act Section 10(b) and Rule 10b-5(a) and (c).

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[377] *Dennis J. Malouf*, Securities Act Release No. 10115, 2016 WL 4035575, at *7 (July 27, 2016) (quoting *SEC v. Clark*, 915 F.2d 439, 448 (9th Cir. 1990)), *pet. denied*, 933 F.3d 1248 (10th Cir. 2019).

[378] *Aaron v. SEC*, 446 U.S. 680, 701–02 (1980).

[379] *Laird v. Integrated Res., Inc.*, 897 F.2d 826, 835 (5th Cir. 1990).

[380] *Malouf*, 2016 WL 4035575, at *8 (quoting *O'Hagan*, 521 U.S. at 655).

[381] *Vernazza*, 327 F.3d at 859 ("It is indisputable that potential conflicts of interest are 'material' facts with respect to clients and the Commission.").

8. Gibson violated Advisers Act Section 206(4) and Rule 206(4)-8.

The Division also alleges that Gibson's conduct violated Advisers Act Section 206(4) and Rule 206(4)-8.[382] Advisers Act Section 206(4) prohibits an investment adviser from engaging "in any act, practice, or course of business which is fraudulent, deceptive, or manipulative" as further prescribed by Commission rule.[383] Rule 206(4)-8 makes it prohibited under Section 206(4)

> for any investment adviser to a pooled investment vehicle to:
>
> (1) Make any untrue statement of a material fact or to omit to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading, to any investor or prospective investor in the pooled investment vehicle; or
>
> (2) Otherwise engage in an act, practice, or course of business that is fraudulent, deceptive, or manipulative with respect to any investor or prospective investor in the pooled investment vehicle.[384]

The Division need not prove scienter to establish a violation of Section 206(4); a showing of negligence is sufficient.[385]

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[382] OIP ¶ 57; Div. Br. 30–34.

[383] 15 U.S.C. § 80b-6(4).

[384] 17 C.F.R. § 275.206(4)-8.

[385] *Steadman*, 967 F.2d at 647.

Gibson violated Section 206(4) and Rule 206(4)-8 for the conduct discussed above. The rule applies because the Fund was a type of pooled investment vehicle.[386] And Gibson's potential conflicts with the Fund would have been material information to investors.[387] Since, for the reasons discussed earlier, Gibson's actions constituted a fraud within the meaning of the securities laws, he also deceived investors.

Gibson argues that he could not have violated this rule because he owed a duty exclusively to the Fund and not to its investors.[388] But Gibson misreads the rule. It is true that because he breached no fiduciary duty to investors, he did not directly defraud them under Section 206(2) through his lack of disclosure.[389] By its terms, however, Rule 206(4)-8 applies even when there is no fiduciary duty to the investors.[390] Conduct that operates as a fraud against the Fund can also by extension be materially misleading as to investors under Rule 206(4)-8. The investors were

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386 *See* 17 C.F.R. § 275.206(4)-8(b); *see also* 15 U.S.C. § 80a-3(a)(1); Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles, 72 Fed. Reg. 44,756, 44,758 (Aug. 9, 2007); Tr. 140; Div. Ex. 31 at 2.

387 *Vernazza*, 327 F.3d at 859.

388 Resp't Br. 26–27 (citing *Goldstein*, 451 F.3d at 881).

389 *See* Prohibition of Fraud, 72 Fed. Reg. at 44,760 ("Rule 206(4)-8 does not create under the Advisers Act a fiduciary duty to investors or prospective investors in a pooled investment vehicle not otherwise imposed by law.").

390 *See* 17 C.F.R. § 275.206(4)-8; Inv. Adviser Advertisements, 84 Fed. Reg. at 67,527; *SEC v. Quan*, No. 11-cv-723, 2013 WL 5566252, at *16 n.10 (D. Minn. Oct. 8, 2013) ("the existence of a fiduciary duty is not required to prove a violation of Rule 206(4)-8"), *aff'd*, 870 F.3d 754 (8th Cir. 2017).

deceived by Gibson's failure to disclose his front running and the Hull transaction or abstain from those transactions, which brings his conduct within the ambit of Section 206(4) and Rule 206(4)-8. In fact, this is exactly the type of misconduct the rule was designed to capture.[391]

9. Gibson is not charged with making false statements to investors regarding Geier Group and Geier Capital, and, in any event, such misstatements appear immaterial.

Gibson contends that two additional allegations should not be grounds for liability under Rule 206(4)-8: (1) his failure to disclose the dissolution of Geier Group and the Georgia Geier Capital; and (2) his solicitation of two investors for the Fund using offering documents falsely stating that Geier Group was a registered investment adviser at the time.[392] I agree. Although the OIP mentions these facts—and they were proven at the hearing—the OIP specifically predicates liability on the front running and the Hull transaction.[393] Furthermore, the Division, which does not contend in its opening brief that these failures or false statements give rise to liability, failed

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[391] *See* Prohibition of Fraud, 72 Fed. Reg. at 44,756–57 (explaining that the rule, which the Commission promulgated in response to *Goldstein*, "clarifies that an adviser's duty to refrain from fraudulent conduct under the federal securities laws extends to the relationship with ultimate investors" in pooled investment vehicles), 44,759 ("section 206(4) encompasses 'acts, practices, and courses of business as are * * * deceptive,' thereby reaching conduct that is negligently deceptive as well as conduct that is recklessly or deliberately deceptive").

[392] Resp't Br. 27.

[393] OIP ¶¶ 2–11, 14, 15; *see supra* at Facts Section 4.

to preserve this argument.[394] The OIP appears to mention these matters for a different reason: to show that despite the dissolution of Geier Group and Geier Capital, Gibson was still the Fund's investment adviser.[395]

In any event, the Division failed to prove that the status of Geier Group or Geier Capital was material to investors. Most, if not all of the Fund's investors invested because of their personal relationships with Hull and Gibson, and knew that Gibson and Hull were managing the Fund.[396] Moreover, Gibson testified that after Geier Group was dissolved, his role as adviser to the Fund did not change.[397] And the Fund's operating agreement stated that a different entity could be substituted for Geier Group at the sole discretion of the Fund's managing member.[398] Gibson's false statements about Geier Group and his failures to disclose the dissolution of Geier Group and Geier Capital did not violate Rule 206(4)-8 because the Division did not establish their materiality.

Sanctions

The Division requests that Gibson be ordered to cease and desist from violations of the securities laws, be permanently barred from the securities industry under the Advisers Act and the Investment Company

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394 *See Dembski*, 2017 WL 1103685, at *8. In its response to Gibson's proposed findings of fact and conclusions of law, the Division counters that these facts were material, but does not elaborate. *See* Div. Responses to Resp't's Proposed Findings of Fact & Conclusions of Law ¶ 135.

395 *See* OIP ¶¶ 14, 15.

396 *See, e.g.*, Tr. 529, 541, 1337–38.

397 Tr. 184, 187.

398 Div. Ex. 21 at 3.

Act, disgorge $82,088, and pay civil money penalties of $825,000.[399] I impose a portion of the sanctions the Division requests for Gibson's misconduct.

1. Industry bars.

Advisers Act Section 203(f) authorizes the Commission to bar or suspend any person from associating with various segments of the securities industry if, in relevant part, that person willfully violated any provision of the Advisers Act, Exchange Act, or rules promulgated under either Act; was associated with an investment adviser at the time of the misconduct; and the sanction is in the public interest.[400]

Investment Company Act Section 9(b) authorizes the Commission to prohibit any person, either permanently or temporarily, from serving or acting in various capacities with respect to a registered investment company, if that person has willfully violated a provision of the Advisers Act or Exchange Act, or a rule promulgated under them; and the sanction is in the public interest.[401]

In considering the public interest, the Commission starts with the factors set out in *Steadman v. SEC*.[402] These factors include:

> the egregiousness of a respondent's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of

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[399] Div. Br. at 37–43.

[400] 15 U.S.C. § 80b-3(e)(5), (f).

[401] 15 U.S.C. § 80a-9(b)(2).

[402] 603 F.2d 1126, 1140 (5th Cir. 1979), *aff'd on other grounds*, 450 U.S. 91 (1981); *see Brendan E. Murray*, Advisers Act Release No. 2809, 2008 WL 4964110, at *10 (Nov. 21, 2008).

> the respondent's assurances against future violations, the respondent's recognition of the wrongful nature of his or her conduct, and the likelihood that the respondent's occupation will present opportunities for future violations.[403]

The Commission also considers the public at large,[404] the welfare of investors as a class, standards of conduct in the securities business generally,[405] and the threat a respondent poses to investors and the markets in the future.[406] The public-interest inquiry is flexible, and no single factor is dispositive.[407]

Gibson acted as an investment adviser to the Fund, and was therefore associated with an adviser for the purposes of the sanctions requested under the Advisers Act.[408] His violations were willful because he

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[403] *Schield Mgmt. Co.*, Exchange Act Release No. 53201, 2006 WL 231642, at *8 (Jan. 31, 2006).

[404] *Christopher A. Lowry*, Advisers Act Release No. 2052, 2002 WL 1997959, at *6 (Aug. 30, 2002), *pet. denied*, 340 F.3d 501 (8th Cir. 2003).

[405] *Arthur Lipper Corp.*, Exchange Act Release No. 11773, 1975 WL 163472, at *15 (Oct. 24, 1975), *penalty modified*, *pet. otherwise denied*, 547 F.2d 171 (2d Cir. 1976).

[406] *Tzemach David Netzer Korem*, Exchange Act Release No. 70044, 2013 WL 3864511, at *5 (July 26, 2013).

[407] *Conrad P. Seghers*, Advisers Act Release No. 2656, 2007 WL 2790633, at *4 (Sept. 26, 2007), *pet. denied*, 548 F.3d 129 (D.C. Cir. 2008).

[408] *Anthony J. Benincasa*, Investment Company Act of 1940 Release No. 24854, 2001 WL 99813, at *2 (Feb. 7, 2001) (a person who "function[s] as an investment adviser in an individual capacity . . . meets the definition of a 'person associated with an investment adviser'"); *Alexander V. Stein*, Advisers Act Release No. 1497, 1995 WL 358127, at *2 (June 8, 1995) ("[A]uthority to

intended to take the actions that resulted in the violations.[409]

Turning to the public interest, the Commission considers misconduct involving a breach of fiduciary duty to be egregious.[410] In September 2011, Gibson sold personal shares ahead of the Fund's sale, and in October and November, he purchased and recommended that others purchase put options while the Fund was trying to find a buyer for its remaining TRX shares. In doing so, Gibson recklessly used his client's confidential information without consent to benefit himself and those close to him, which created potential conflicts with his client. He further recklessly engaged in the Hull transaction in October 2011, despite his numerous conflicts of interest with respect to Hull. Gibson's recurrent failures to appropriately disclose or remediate his conflicts of interest breached his fiduciary duty and were therefore egregious. Given that Gibson was a securities professional with several exam licenses, his misconduct—committed with scienter—cannot be excused.[411]

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proceed under Section 203(f) . . rest[s] on whether or not an entity or individual in fact acted as an investment adviser").

[409] *See Wonsover v. SEC*, 205 F.3d 408, 413–14 (D.C. Cir. 2000) (willfulness means the intentional commission of the act that constitutes the violation of the securities laws; there is no requirement that the actor be aware that he or she is violating any statutes or regulations); *accord Robare Grp.*, 922 F.3d at 479.

[410] *James S. Tagliaferri*, Securities Act Release No. 10308, 2017 WL 632134, at *6 (Feb. 15, 2017).

[411] *See Blizzard*, 2004 WL 1416184 at *5 ("Securities professionals are required to be knowledgeable about, and to comply with, requirements to which they are subject.").

Gibson has not expressed remorse or made any assurances against future violations. Although he is not directly involved in the securities industry now, given his relative youth, he could work in the industry in the future. Gibson presents some risk to the investing public, particularly since the "existence of a violation raises an inference that it will be repeated."[412]

In a typical case in which a respondent committed fraud and showed no remorse, consistent with Commission precedent, I would impose a permanent bar and be disinclined to give the individual a second chance.[413] But this is not a typical case and there are several mitigating factors.

First, there is no evidence that Gibson intended to harm the Fund. When he liquidated the personal accounts on September 26, he believed that the small size of his personal trades would have no effect on the Fund's impending sale.[414] Indeed, when he traded, it was unclear when the Fund's sale would go through. Gibson's front running is thus different from a case in which a broker holds a client's order and then executes personal trades immediately ahead of a client's trades, which could lead to the client receiving

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[412] *Korem*, 2013 WL 3864511, at *6 n.50 (quoting *Geiger v. SEC*, 363 F.3d 481, 489 (D.C. Cir. 2004)).

[413] *See id.* at *5 ("Ordinarily, and in the absence of evidence to the contrary, it is in the public interest to bar a respondent who is enjoined from violating the antifraud provisions."); *see, e.g.*, *Stanley Jonathan Fortenberry*, Initial Decision Release No. 748, 2015 WL 860715, at *32–33, *35 (ALJ Mar. 2, 2015).

[414] Tr. 1424.

a worse execution than the broker.[415] And the puts Gibson purchased for himself were hedging transactions; Gibson was not taking a short position contrary to the Fund's long one.[416] He was nearly insolvent because Hull required him to execute a promissory note he didn't need and was trying to protect his own investments rather than trying to harm the Fund. The same is also true with regard to the Hull transaction. Although he was deeply conflicted, the evidence shows that Gibson thought the purchase of Hull's shares would improve the Fund's chances of selling its remaining shares. And in addition to the fact that Gibson did not intend to harm the Fund, it is not clear that his front running transactions or the Fund's purchase of Hull's shares actually caused investors any significant losses.

Second, Gibson's lack of remorse must be seen in context. Throughout this proceeding, the Division has claimed that: Gibson misled investors by telling them that he still had faith in TRX even though he privately believed it was failing; and gave Hull a "sweetheart" deal by dumping his shares on the Fund after the

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[415] *See, e.g.*, *Dial*, 757 F.2d at 168–70; *D'Alessio*, 2003 WL 1787291, at *3.

[416] The puts Gibson purchased for Francesca Marzullo might be different, although the record is not entirely clear. On the one hand, she was not a Fund investor and owned no TRX shares in late October and early November 2011, which suggests that her puts were not hedges. And although Gibson testified that he purchased Ms. Marzullo's puts to hedge her father's position in the Fund, he later lost her profits in other options trades. This fact diminishes the credibility of Gibson's explanation. On the other hand, these facts are not strictly contradictory: it is possible that Gibson purchased the puts to hedge Giovanni Marzullo's position in the Fund and later decided to risk the profits in other trades.

decision had been made to exit TRX.[417] At times, the Division has also suggested that by purchasing puts, Gibson was taking a short position in TRX.[418] The record does not support these claims. I therefore do not hold against Gibson his vigorous defense of these particular charges. Still, Gibson's reckless disregard of his fiduciary duties is on its own a serious matter which he has failed to acknowledge.

Finally, Gibson ended up in a nearly impossible situation as investment adviser to the Fund. No one presented evidence about why he left Deutsche Bank in early 2009, but within a year after he left, he found himself, at about 27 years of age, "managing" a $32 million fund involving not just his father's business partner, Hull, but also Hull's contemporaries and their children, and Gibson's family and his girlfriend's family.

Gibson only received this opportunity because Hull was his father's business partner. And although Gibson's name was on Fund documents, Gibson knew Hull was the Fund's ultimate decision-maker and that he was not in a position to question Hull's judgment.[419] Moreover, Hull enjoyed the respect of a large portion of his community. The pressure all of this might have placed on Gibson was evidenced at

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[417] *See, e.g.*, Div. Br. 3–4, 19–21, 24–25.

[418] *See* OIP ¶ 45; Tr. 49, 301–03.

[419] Hull described himself as irascible. Tr. 568, 583. From watching his testimony and demeanor, that description is apt. It is clear that he has little tolerance for incompetence. Given this trait plus Hull's forceful personality, experience, and standing in his community and among his peers, it would have been difficult for Gibson—at age 26 or 27 with no prior advisory experience—to question Hull's judgment if he disagreed with Hull.

times in Gibson's over-the-top and desperate sounding e-mail and phone communications.

What's more, this opportunity came with a significant string attached. Gibson and his family had to be all in. Hull required Gibson and his family to be aligned with Hull and the Fund. As a condition to managing the Fund, Hull required Gibson to invest his entire net worth in the Fund, and even loaned him money to do so, which increased the pressure on him.[420] This meant that if the Fund's investments declined, Gibson and those close to him would feel that decline the most. Gibson recalled that Hull required:

> that at all times, over any period of time -- a year, a month, a week, a day, an hour -- at every point in time, that if the securities or investments that we owned in that fund declined, I would lose more than other investors and that the individuals close to me and everything that mattered to me in my life would be exposed in that regard.[421]

And when Gibson wanted to repay Hull's loan, Hull refused to let him.[422] Additionally, in late 2010, Hull decided to invest all the Fund's money in one stock, TRX, which made Gibson's fortunes even more precarious.[423]

In hindsight, the problems with this situation are obvious. The entire setup created a conflict of interest

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[420] Div. Ex. 24 at 1, 7; Resp't Ex. 117 at 5; Tr. 1358–59.

[421] Tr. 1358.

[422] Tr. 1360.

[423] *See* Tr. 1366–67.

between Gibson and the Fund. But at the time and given Gibson's circumstance, it is not difficult to understand how Gibson ended up in the situation that led to this proceeding. Gibson's reckless violations of his fiduciary duties to mitigate his losses cannot be excused, but should be seen in context.

Gibson's lapses of judgment were serious. He cannot, at this time, be permitted to remain in the securities industry. But because of the mitigating factors I've noted, I will give him the opportunity to return. I impose full industry bars under Advisers Act Section 203(f) and a prohibition under Investment Company Act Section 9(b), with the right to reapply for reentry after three years for both sanctions.

2. Cease-and-desist order.

Exchange Act Section 21C and Advisers Act Section 203(k) authorize the Commission to issue a cease-and-desist order against any respondent who violates a provision of those acts or a rule promulgated under them.[424] The public interest factors discussed above inform the decision whether to impose a cease-and-desist order.[425] The Commission also considers "whether the violation is recent, the degree of harm to investors or the marketplace resulting from the violation, and the remedial function to be served by the cease-and-desist order in the context of any other sanctions being sought in the same proceedings."[426] No single

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[424] 15 U.S.C. §§ 78u-3(a), 80b-3(k)(1).

[425] *KPMG Peat Marwick LLP*, Exchange Act Release No. 43862, 2001 WL 47245, at *23 & n.114, *26 (Jan. 19, 2001), *pet. denied*, 289 F.3d 109 (D.C. Cir. 2002); *see Dembski*, 2017 WL 1103685, at *14.

[426] *KPMG Peat Marwick*, 2001 WL 47245, at *26.

factor in this analysis is dispositive, and the entire record is considered when deciding whether to issue a cease-and-desist order.[427]

To issue a cease-and-desist order, "there must be some likelihood of future violations."[428] But the "risk" of future violations "need not be very great to warrant issuing a cease-and-desist order. Absent evidence to the contrary, a finding of violation raises a sufficient risk of future violation."[429]

Giving the length of time this case has been pending, Gibson's violations are not recent. Although his failures to remediate his conflicts of interest did not necessarily cause his client to lose money, an adviser who fails to address conflicts of interest poses a risk to the securities industry as a whole. Moreover, Gibson has shown no remorse, and until he fully understands the need to take his fiduciary duties more seriously, there remains a risk of future violations. In combination with the other sanctions imposed, a cease-and-desist order is warranted.

3. Disgorgement.

Advisers Act Section 203(j) and (k)(5), Exchange Act Sections 21B(e) and 21C(e), and Investment Company Act Section 9(e) authorize disgorgement, including reasonable interest, in this proceeding.[430] "Disgorgement is an equitable remedy designed to deprive a wrongdoer of his unjust enrichment and to

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[427] *Id.*

[428] *Id.* at *24.

[429] *Id.*; *see also id.* at *26.

[430] 15 U.S.C. §§ 78u-2(e), 78u-3(e), 80a-9(e), 80b-3(j), (k)(5).

deter others from violating the securities laws."[431] To establish the appropriate amount of disgorgement, the Division need show only "a reasonable approximation of profits causally connected to the violation" in question.[432] Ordinarily, once the Division makes the required showing, the burden shifts to the respondent to show that the disgorgement figure was not a reasonable approximation.[433]

The Division seeks disgorgement of the losses Gibson avoided by selling the TRX shares in his personal account on September 26, 2011, as well as the profits he made from the purchase of $4 put options in his own account in October and November 2011.[434]

The Division wants Gibson to disgorge $1,080 for the September front running. This sum represents the difference between the price he obtained per share on September 26 for the 2,000 personal shares ($4.04), and the price he would have obtained had he sold on September 27 directly following the Fund's sale, when he would have received 54 cents less per share

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[431] *Montford*, 2014 WL 1744130, at *22 (quoting *SEC v. First City Fin. Corp.*, 890 F.2d 1215, 1230 (D.C. Cir. 1989)).

[432] *First City Fin.*, 890 F.2d at 1231; *see also Montford & Co. v. SEC*, 793 F.3d 76, 83–84 (D.C. Cir. 2015).

[433] *SEC v. Calvo*, 378 F.3d 1211, 1217 (11th Cir. 2004).

[434] Div. Br. 40. The Division does not ask that Gibson disgorge the losses he avoided in September by selling the shares in Ms. Marzullo's account or the shares in the Geier Group account that belonged to him because of his 50% ownership of the entity. *See id.* at 41. The Division also does not request that Gibson disgorge any profits realized on puts other than his own.

($3.50).[435] This figure represents a reasonable approximation of the losses Gibson avoided, because in the analogous insider trading context, "the proper amount of disgorgement is generally the difference between the value of the shares when the insider sold them while in possession of the material, nonpublic information, and their market value 'a reasonable time after public dissemination of the inside information.'"[436] Although Gibson could have sold his shares at any time, such as when TRX was slightly higher at the end of October, he testified that he sold when he did to obtain liquidity due to his suspension of management fees, which shows he would not have wanted to wait much longer to sell.[437] The Division has therefore met its burden of showing that $1,080 is a reasonable approximation of the amount by which Gibson was enriched but-for his front running.[438] Gibson does not attempt to rebut the Division's reasonable approximation.

Gibson also does not dispute that he sold his $4 TRX puts for $81,930 more than he purchased them.[439] These profits are causally connected to his violation; had he refrained from purchasing the puts or obtained independent advice as his fiduciary obligations demanded, he would not have made the

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[435] Div. Br. 41; *see* Tr. 234–35.

[436] *SEC v. Happ*, 392 F.3d 12, 31 (1st Cir. 2004) (quoting *SEC v. MacDonald*, 699 F.2d 47, 54–55 (1st Cir. 1983) (en banc)); *see also SEC v. Patel*, 61 F.3d 137, 139 (2d Cir. 1995).

[437] Tr. 1394; *see* Joint Ex. 1 at 5.

[438] *See Jay T. Comeaux*, Securities Act Release No. 9633, 2014 WL 4160054, at *3 (Aug. 21, 2014) (requiring but-for causation for disgorgement).

[439] Tr. 330.

profits from the puts which mitigated his losses in the Fund. I will, however, deduct the broker commissions he paid to sell his puts.[440] Gibson must therefore disgorge his $81,008.81 net profit from his sale of the $4 puts.[441]

In total, Gibson must disgorge $82,088.81, plus prejudgment interest as calculated according to the ordering paragraphs below.[442]

4. Civil penalties.

Exchange Act Section 21B(a)(2) and Advisers Act Section 203(i)(1)(B) authorize civil penalties in cease-and-desist proceedings against a respondent who has violated a provision of those acts or a rule promulgated under them.[443] Investment Company Act Section 9(d)(1)(A) and Advisers Act Section 203(i)(1)(A) authorize civil penalties against a respondent who has willfully violated a provision of the Advisers Act or Exchange Act, or a rule promulgated under them, if a penalty is in the public interest.[444]

The statutes set out a three-tiered system for determining the maximum monetary penalty for each act or omission constituting a violation.[445] First-tier

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[440] The Division deducts broker commissions from the requested disgorgement amount. *See* Div. Br. 41–42. This deduction of "expenses customarily incurred in the purchase and sale of stock" is permissible. *See SEC v. JT Wallenbrock & Assocs.*, 440 F.3d 1109, 1114 (9th Cir. 2006).

[441] Div. Ex. 185 at 47 (Dr. Gibbons's calculation of Gibson's net profits).

[442] 17 C.F.R. § 201.600(a) (requiring the payment of prejudgment interest on disgorgement ordered).

[443] 15 U.S.C. §§ 78u-2(a)(2), 80b-3(i)(1)(B).

[444] 15 U.S.C. §§ 80a-9(d)(1)(A), 80b-3(i)(1)(A).

[445] 15 U.S.C. §§ 78u-2(b), 80a-9(d)(2), 80b-3(i)(2).

penalties are available based on the fact of the violation alone.[446] Second-tier penalties are permitted if a respondent's misconduct involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement.[447] Third-tier penalties require the additional finding that the misconduct, directly or indirectly, resulted in either "substantial losses or created a significant risk of substantial losses to other persons" or "substantial pecuniary gain to the person who committed the act or omission."[448] For the time period from March 4, 2009, to March 5, 2013—when Gibson's misconduct occurred—the maximum first-, second-, and third-tier penalties for each violation are, respectively, $7,500, $75,000, and $150,000 for a natural person.[449]

When determining whether civil penalties are in the public interest, the Commission considers six factors listed in the securities statutes: (1) whether the violation involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement; (2) the resulting harm, directly or indirectly, to other persons; (3) any unjust enrichment and prior restitution; (4) whether the respondent has prior violations of the securities laws; (5) the need to deter the respondent and other persons, and (6) such other matters as justice may require.[450]

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[446] 15 U.S.C. §§ 78u-2(b)(1), 80a-9(d)(2)(A), 80b-3(i)(2)(A).

[447] 15 U.S.C. §§ 78u-2(b)(2), 80a-9(d)(2)(B), 80b-3(i)(2)(B).

[448] 15 U.S.C. §§ 78u-2(b)(3), 80a-9(d)(2)(C), 80b-3(i)(2)(C).

[449] 17 C.F.R. § 201.1001, tbl. I; *see* 15 U.S.C. §§ 78u-2(b), 80a-9(d)(2), 80b-3(i)(2).

[450] 15 U.S.C. §§ 78u-2(c), 80a-9(d)(3), 80b-3(i)(3).

The Division requests second-tier penalties for Gibson's reckless front running violations, which I agree are justified given that his violations of the relevant laws were willful and committed with scienter.[451] Considering the public interest, Gibson recklessly deceived the Fund by using its confidential information. The Division has not shown that the violations harmed investors monetarily, although they unjustly enriched Gibson. Gibson also has no prior convictions or securities law violations. Still, he must be deterred from further violations, and others in the industry must realize that front running is a serious offense that is actionable under the securities laws. Commensurate with the disgorgement amount imposed, I impose two second-tier penalties totaling $82,000, comprised of $41,000 for Gibson's September 26 front running, and $41,000 for all of his put transactions and recommendations.

The Division argues that Gibson's conduct regarding the Hull transaction deserves third-tier penalties because it burdened the Fund with additional TRX stock that it sold at a loss on November 10, which means that the Fund's investors lost a substantial sum.[452] It was not clear at the outset, however, that the transaction was to the Fund's detriment. To the contrary, Bystrom opined that the purchase could have aided the Fund.[453] And Gibson believed that consolidation would encourage a buyer to come forward. When Gibson engaged in the

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[451] *See SEC v. M & A W. Inc.*, 538 F.3d 1043, 1054 (9th Cir. 2008) ("[T]he imposition of second-tier penalties requires an assessment of scienter.").

[452] Div. Br. 43.

[453] Tr. 1567; Resp't Ex. 228 at 6.

Hull transaction, he did not know that TRX's share price would fall farther, and most importantly, he had no plans to sell the Fund's shares into the market, which precipitated the tremendous decline in TRX's value. And it is possible that the Hull transaction could have saved the Fund money; it prevented Hull from separately selling his personal shares into the market at some point and depressing the price of TRX. I will impose second-tier penalties for this instance of reckless misconduct.

Regarding the public interest, as noted, it is difficult to measure the harm, if any, that Gibson's reckless conduct caused to the Fund and its investors. Further, unlike with the front running violations, Gibson was not unjustly enriched in this transaction. And Gibson believed he was looking after the Fund's best interests. Thus, even though Gibson's compliance with his fiduciary duties was severely wanting, I impose a reduced second-tier penalty of $20,000, for total civil penalties of $102,000.[454]

5. Gibson has ability to pay monetary sanctions.

In determining whether disgorgement, interest, or monetary penalties are in the public interest, the Commission or its administrative law judges may consider evidence concerning ability to pay.[455] Considering this evidence is an exercise of discretion, and even if the Commission considers ability to pay,

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[454] *Cf. Rockies Fund, Inc.*, Exchange Act Release No. 54892, 2006 WL 3542989, at *7 (Dec. 7, 2006) (imposing only mid- to upper-level second tier penalties, despite the seriousness of the fraud, as there was no harm to investors or unjust enrichment), *pet. denied*, 298 F. App'x 4 (D.C. Cir. 2008).

[455] 17 C.F.R. § 201.630(a).

it "is only one factor . . . and is not dispositive."[456] A respondent bears the burden of proving his inability to pay.[457]

Gibson has not established that he is unable to pay sanctions. His primary liabilities are large loans he owes to his father.[458] One loan is for some of the costs John Gibson incurred in paying for Gibson's legal defense in this proceeding.[459] The other is the loan that Gibson originally owed to Hull and that he now owes to his father after his father assumed his obligation to Hull.[460] Although both notes accrue interest annually, they are only payable upon demand, and so far, no demand has been made for the principal or the interest.[461] Gibson's father could also forgive the notes at any time.[462] I will therefore discount these liabilities in considering Gibson's ability to pay. Although Gibson has some credit card debt, it appears to be short term. The documentation Gibson provided for his credit card accounts is deficient, but it appears he has not carried over a significant credit card balance from month to

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[456] *Thomas C. Bridge*, Securities Act Release No. 9068, 2009 WL 3100582, at *25 (Sept. 29, 2009) (reserving power to impose full sanction when conduct is sufficiently egregious), *pet. denied sub nom. Robles v. SEC*, 411 F. App'x 337 (D.C. Cir. 2010).

[457] *Philip A. Lehman*, Exchange Act Release No. 54660, 2006 WL 3054584, at *4 & nn.29–30 (Oct. 27, 2006).

[458] *See* Gibson's Form D-A at 3 (of 114) (August 25, 2019).

[459] Div. Ex. 217; Tr. 1224–25.

[460] Tr. 566.

[461] Tr. 1228.

[462] Tr. 1228.

month.[463] Similarly, although he has not yet paid his 2018 taxes, and he believes his liability will be substantial, he is not carrying over any tax liability from year to year.[464]

Gibson's expenses between August 2018 and August 2019 exceeded his income by a couple thousand dollars.[465] His salary from East Century Capital fluctuates from year to year, and it is hard to understand Gibson's testimony about the amount he has made and in what years he received such income.[466] He has not submitted any W-2s or other tax forms that might help determine his exact compensation. Nonetheless, in 2018 at least, his income was well in excess of $100,000, which is substantially higher than his average basic living expenses.[467] And given his age, education level, ability to find work, and lack of dependents to support, it is reasonable to assume that he will continue to earn a sufficient income. Perhaps most significantly, in addition to some cash on hand, he has a large securities investment that alone could be sold to pay a significant percentage of the disgorgement and penalties I am ordering.[468] For these reasons, I reject Gibson's inability-to-pay defense.

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[463] *Compare* Form D-A at 3 (of 114) (listing significant credit card debt) *with* Resp't Ex. 240 (relying on account statements from early July 2019 and listing virtually no credit card debt).

[464] Tr. 1505; Form D-A at 3, 26 (of 114).

[465] Form D-A at 4–5 (of 114).

[466] *See* Tr. 1498–1505.

[467] Form D-A at 26 (of 114).

[468] *Id.* at 3, 22 (of 114).

Constitutional Issues

Gibson raised a number of constitutional affirmative defenses in his answer to the OIP.[469] Because Gibson did not address all of these defenses in his prehearing brief, I asked his counsel during the final prehearing conference which defenses were actually at issue.[470] Counsel reserved answering and in advance of the merits hearing filed a letter asserting three constitutional defenses: (1) "Respondent has been denied due process,"[471] (2) "the appointment of the ALJ violates the [Constitution's] removal provisions," and (3) Gibson "is entitled to a trial by jury."[472]

After the merits hearing, the parties filed a stipulation in which they agreed that Gibson had preserved these arguments and others not discussed in Gibson's counsel's letter.[473] Although the Commission will decide what issues Gibson has preserved and will ultimately decide those issues, I include the following observations about the

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[469] Answer 11–13.

[470] Prhr'g Tr. 24 (July 23, 2019).

[471] This argument includes several sub-arguments: (1) unfairness because I am situated in the agency whose officials allegedly engaged in misconduct in this case, (2) the lack of counterclaims in Commission proceedings, (3) the lack of discovery in Commission proceedings regarding alleged due process violations, and (4) the Commission issued the OIP that contained alleged misstatements of Division staff, but allowed the OIP to be re-served after *Lucia*. Letter from Thomas A. Ferrigno at 1 (July 28, 2019).

[472] *Id*. at 1–3. Counsel's letter also referenced a statute-of-limitations defense. *Id*. at 4.

[473] Jt. Stipulation at 1 (Aug. 27, 2019).

constitutional issues raised in Gibson's counsel's July 28, 2019 letter in order to set those issues in context.

Throughout this proceeding Gibson has attempted to raise a due process claim related to the Division's conduct when it took Hull's February 2015 investigative testimony.[474] Specifically, during Hull's investigative testimony, Division counsel defined a short position as "borrowing stock and selling stock in the hope that the stock's price will decline."[475] Counsel then represented to Hull that "in October and November 2011 . . . Gibson took a short position in TRX in his" personal investment account.[476] After hearing this, Hull hit the roof and asked for a tolling agreement with Gibson and his father so that he could potentially sue them.[477] Hull also spoke to other Fund investors about what he learned.[478] But when Hull learned that Gibson had not taken a short position in TRX, his views about Gibson and his put purchases changed.[479] No one who witnessed Hull's testimony during the merits hearing has any doubt that he currently is more favorably inclined toward Gibson and has a decidedly negative view of the Division's position and its attorneys.[480]

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[474] See Prehr'g Tr. 63 (July 9, 2019); *see* Opp'n to Mot. to Preclude Testimony of Current and Former Division Counsel at 4–5, 10–15 (June 3, 2019).

[475] Resp't Ex. 187 at 37.

[476] *Id*. at 43.

[477] *See* Tr. 711–12.

[478] Tr. 712.

[479] Tr. 712.

[480] *See* Tr. 1526–27.

Believing the Division's conduct during Hull's investigative testimony amounted to a due process violation, Gibson listed three Division attorneys on his witness list, explaining that he expected them to testify about their "representations to James Hull during his investigative testimony regarding short sales and short positions in TRX securities by Christopher Gibson."[481] The Division moved to bar Gibson from calling its attorneys to testify and Gibson opposed the Division's motion.[482] I granted the Division's motion because Gibson had not shown that the testimony he sought from counsel was crucial or unavailable from other sources.[483] I did not, however, rule on the validity of Gibson's then-unspecified due process claim.

Fast forward to early July 2019, when I heard oral argument on the parties' motions. During the argument, I asked Gibson's counsel "what exactly is your due process claim?"[484] Counsel and I engaged in an extended discussion during which the basis for Gibson's claim shifted.[485]

During the merits hearing, we again discussed Gibson's claim with reference to his counsel's letter.[486] After some discussion, counsel stated that Gibson's due process claim had two parts, the first being part of a systemic attack on Commission

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[481] Resp't Witness List at 4 (May 10, 2019).

[482] *See Gibson*, Admin. Proc. Rulings Release No. 6615, 2019 SEC LEXIS 1544, at *1 (ALJ June 28, 2019).

[483] *Id.* at *10–11.

[484] Prhr'g Tr. 63 (July 9, 2019).

[485] Prhr'g Tr. 63–68 (July 9, 2019).

[486] Tr. 1520–29.

administrative proceedings and the second being that the Division "soured" Hull toward Gibson.[487] But counsel conceded that however Hull may have previously felt about Gibson, by the time of the hearing, his "understanding of the situation . . . [was] very different" from immediately after his investigative testimony.[488] After counsel seemed to suggest that Hull's former antipathy toward Gibson, resulting from what Division counsel told him, might have leaked to other witnesses, I remarked on the fact that Gibson had presented no evidence on that score.[489] At that point, counsel stated that although he needed to consult with his client, he was satisfied with the record on the prejudice argument.[490] Indeed, Gibson did not raise the prejudice argument in his briefing, and consistent with my order following the parties' joint stipulation on constitutional issues, I need not say anything further on the matter.[491]

Similar to many respondents in recent Commission administrative proceedings, Gibson also argued that the tenure protections that apply to the Commission's administrative law judges violate the

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[487] Tr. 1523–25.

[488] Tr. 1527.

[489] Tr. 1527–28.

[490] Tr. 1529, 1532. During the discussion, I disagreed with counsel's argument that respondents in Commission administrative proceedings cannot obtain discovery relevant to due process claims, pointing out that I had previously "granted discovery on due process claims." Tr. 1531; *see Charles L. Hill, Jr.*, Admin. Proc. Rulings Release No. 2706, 2015 SEC LEXIS 2016 (ALJ May 21, 2015). Counsel agreed that such discovery is allowed. Tr. 1531–32.

[491] *See Gibson*, 2019 SEC LEXIS 2319, at *1.

Constitution's separation of powers.[492] I've previously addressed and rejected this argument.[493] In any event, if either party appeals this initial decision, the Commission will have the opportunity to decide the issue.

Record Certification

I certify that the record includes the items set forth in the record index issued by the Secretary of the Commission on January 10, 2020, and five additional items: (1) a letter dated July 28, 2019, from Thomas A. Ferrigno to me concerning Gibson's constitutional challenges; (2) another letter dated July 28, 2019, from Mr. Ferrigno concerning the admissibility of Division Exhibits 183 and 183A; (3) a March 20, 2020 e-mail from Stephen J. Crimmins waiving paper service of all opinions and orders; (4) a March 20, 2020 e-mail from Gregory R. Bockin also waiving paper service; and (5) a stipulation and notice of parties' agreement on service of papers dated March 23, 2020.[494]

Order

Under Section 21C of the Securities Exchange Act of 1934 and Section 203(k) of the Investment Advisers Act of 1940, Christopher M. Gibson must CEASE

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[492] *See* Letter from Thomas A. Ferrigno at 2–3 (July 28, 2019) (relying on *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477 (2010)).

[493] *See David Pruitt, CPA*, Admin. Proc. Rulings Release No. 6675, 2019 SEC LEXIS 2850, at *1–24 (ALJ Sept. 16, 2019). In that order, I also rejected a Seventh Amendment challenge. *Id.* at *24–30 (discussing *Atlas Roofing Co. v. Occupational Safety and Health Review Comm'n*, 430 U.S. 442 (1977) and *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989)).

[494] *See* 17 C.F.R. § 201.351(b).

AND DESIST from committing any violations or future violations of Section 10(b) of the Securities Exchange Act of 1934 and Exchange Act Rule 10b-5(a) and (c), and Section 206(1), (2) and (4) of the Investment Advisers Act of 1940 and Advisers Act Rule 206(4)-8.

Under Section 203(f) of the Investment Advisers Act of 1940, Christopher M. Gibson is BARRED from associating with an investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization—with the right to reapply for reentry after three years to the appropriate self-regulatory organization, or if there is none, to the Commission.

Under Section 9(b) of the Investment Company Act of 1940, Christopher M. Gibson is PROHIBITED from serving or acting as an employee, officer, director, member of an advisory board, investment adviser or depositor of, or principal underwriter for, a registered investment company or affiliated person of such investment adviser, depositor, or principal underwriter—with the right to reapply for reentry after three years to the appropriate self-regulatory organization, or if there is none, to the Commission.

Under Sections 21B(e) and 21C(e) of the Securities Exchange Act of 1934, Section 203(j) and (k)(5) of the Investment Advisers Act of 1940, and Section 9(e) of the Investment Company Act of 1940, Christopher M. Gibson must DISGORGE $82,088.81, plus prejudgment interest. The prejudgment interest owed will be calculated from December 1, 2011, the first day of the month following Gibson's last violation, to the last day of the month preceding the

month in which payment of disgorgement is made.[495] Prejudgment interest will be computed at the underpayment rate of interest established under Section 6621(a)(2) of the Internal Revenue Code, 26 U.S.C. § 6621(a)(2), and compounded quarterly.[496]

Under Section 21B(a) of the Securities Exchange Act of 1934, Section 203(i) of the Investment Advisers Act of 1940, and Section 9(d) of the Investment Company Act of 1940, Christopher M. Gibson must PAY A CIVIL MONEY PENALTY in the amount of $102,000.

Payment of civil penalties, disgorgement, and interest must be made no later than 21 days following the day this initial decision becomes final, unless the Commission directs otherwise. Payment must be made in one of the following ways: (1) transmitted electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request; (2) direct payments from a bank account via Pay.gov through the SEC website at http://www.sec.gov/ofm; or (3) by certified check, bank cashier's check, bank money order, or United States postal money order made payable to the Securities and Exchange Commission and hand-delivered or mailed to the following address alongside a cover letter identifying Respondent and Administrative Proceeding No. 3-17184: Enterprise Services Center, Accounts Receivable Branch, HQ Bldg., Room 181, AMZ-341, 6500 South MacArthur Blvd., Oklahoma

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[495] *See* 17 C.F.R. § 201.600(a); *see, e.g.*, *Terence Michael Coxon*, Advisers Act Release No. 2161, 2003 WL 21991359, at *14 (Aug. 21, 2003) (ordering "that the interest run from the date of the last violation"), *aff'd*, 137 F. App'x 975 (9th Cir. 2005).

[496] *See* 17 C.F.R. § 201.600(b).

City, Oklahoma 73169. A copy of the cover letter and instrument of payment must be sent to the Commission's Division of Enforcement, directed to the attention of counsel of record.

This initial decision will become effective in accordance with and subject to the provisions of Rule 360.[497] Under that rule, a party may file a petition for review of this initial decision within 21 days after service of the initial decision. Under Rule of Practice 111, a party may also file a motion to correct a manifest error of fact within ten days of the initial decision.[498] If a motion to correct a manifest error of fact is filed by a party, then a party has 21 days to file a petition for review from the date of the order resolving such motion to correct a manifest error of fact.

The initial decision will not become final until the Commission enters an order of finality. The Commission will enter an order of finality unless a party files a petition for review or motion to correct a manifest error of fact or the Commission determines on its own initiative to review the initial decision as to a party. If any of these events occur, the initial decision will not become final as to that party.

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James E. Grimes
Administrative Law Judge

Served by e-mail on all parties.

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[497] *See* 17 C.F.R. § 201.360.

[498] *See* 17 C.F.R. § 201.111.

U.S. Const. art. II, § 1, cl. 1

Section 1. The executive Power shall be vested in a President of the United States of America.

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U.S. Const. art. II, § 2, cl. 2

Section 2.

* * *

He shall have Power, by and with the Advice and Consent of the Senate, to make Treaties, provided two thirds of the Senators present concur; and he shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

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15 U.S.C. § 78d-1

§ 78d-1. Delegation of functions by Commission

(a) Authorization; functions delegable; eligible persons; application of other laws

In addition to its existing authority, the Securities and Exchange Commission shall have the authority to delegate, by published order or rule, any of its functions to a division of the Commission, an individual Commissioner, an administrative law judge, or an employee or employee board, including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any work, business, or matter. Nothing in this section shall be deemed to supersede the provisions of section 556(b) of Title 5, or to authorize the delegation of the function of rulemaking as defined in subchapter II of chapter 5 of title 5, with reference to general rules as distinguished from rules of particular applicability, or of the making of any rule pursuant to section 78s(c) of this title.

(b) Right of review; procedure

With respect to the delegation of any of its functions, as provided in subsection (a) of this section, the Commission shall retain a discretionary right to review the action of any such division of the Commission, individual Commissioner, administrative law judge, employee, or employee board, upon its own initiative or upon petition of a party to or intervenor in such action, within such time and in such manner as the Commission by rule shall prescribe. The vote of one member of the Commission shall be sufficient to bring any such action before the Commission for review. A person or party shall be

entitled to review by the Commission if he or it is adversely affected by action at a delegated level which (1) denies any request for action pursuant to section 77h(a) or section 77h(c) of this title or the first sentence of section 78*l*(d) of this title; (2) suspends trading in a security pursuant to section 78*l*(k) of this title; or (3) is pursuant to any provision of this chapter in a case of adjudication, as defined in section 551 of title 5, not required by this chapter to be determined on the record after notice and opportunity for hearing (except to the extent there is involved a matter described in section 554(a)(1) through (6) of such title 5).

(c) Finality of delegated action

If the right to exercise such review is declined, or if no such review is sought within the time stated in the rules promulgated by the Commission, then the action of any such division of the Commission, individual Commissioner, administrative law judge, employee, or employee board, shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission.

15 U.S.C. § 78y

§ 78y. Court review of orders and rules

(a) Final Commission orders; persons aggrieved; petition; record; findings; affirmance, modification, enforcement, or setting aside of orders; remand to adduce additional evidence

(1) A person aggrieved by a final order of the Commission entered pursuant to this chapter may obtain review of the order in the United States Court of Appeals for the circuit in which he resides or has his principal place of business, or for the District of Columbia Circuit, by filing in such court, within sixty days after the entry of the order, a written petition requesting that the order be modified or set aside in whole or in part.

(2) A copy of the petition shall be transmitted forthwith by the clerk of the court to a member of the Commission or an officer designated by the Commission for that purpose. Thereupon the Commission shall file in the court the record on which the order complained of is entered, as provided in section 2112 of title 28 and the Federal Rules of Appellate Procedure.

(3) On the filing of the petition, the court has jurisdiction, which becomes exclusive on the filing of the record, to affirm or modify and enforce or to set aside the order in whole or in part.

(4) The findings of the Commission as to the facts, if supported by substantial evidence, are conclusive.

(5) If either party applies to the court for leave to adduce additional evidence and shows to the satisfaction of the court that the additional evidence

is material and that there was reasonable ground for failure to adduce it before the Commission, the court may remand the case to the Commission for further proceedings, in whatever manner and on whatever conditions the court considers appropriate. If the case is remanded to the Commission, it shall file in the court a supplemental record containing any new evidence, any further or modified findings, and any new order.

(b) Commission rules; persons adversely affected; petition; record; affirmance, enforcement, or setting aside of rules; findings; transfer of proceedings

(1) A person adversely affected by a rule of the Commission promulgated pursuant to section 78f, 78i(h)(2), 78k, 78k-1, 78*o*(c)(5) or (6), 78*o*-3, 78q, 78q-1, or 78s of this title may obtain review of this rule in the United States Court of Appeals for the circuit in which he resides or has his principal place of business or for the District of Columbia Circuit, by filing in such court, within sixty days after the promulgation of the rule, a written petition requesting that the rule be set aside.

(2) A copy of the petition shall be transmitted forthwith by the clerk of the court to a member of the Commission or an officer designated for that purpose. Thereupon, the Commission shall file in the court the rule under review and any documents referred to therein, the Commission's notice of proposed rulemaking and any documents referred to therein, all written submissions and the transcript of any oral presentations in the rulemaking, factual information not included in the foregoing that was considered by the Commission in the promulgation of the rule or proffered by the Commission as pertinent to the rule,

the report of any advisory committee received or considered by the Commission in the rulemaking, and any other materials prescribed by the court.

(3) On the filing of the petition, the court has jurisdiction, which becomes exclusive on the filing of the materials set forth in paragraph (2) of this subsection, to affirm and enforce or to set aside the rule.

(4) The findings of the Commission as to the facts identified by the Commission as the basis, in whole or in part, of the rule, if supported by substantial evidence, are conclusive. The court shall affirm and enforce the rule unless the Commission's action in promulgating the rule is found to be arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; contrary to constitutional right, power, privilege, or immunity; in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; or without observance of procedure required by law.

(5) If proceedings have been instituted under this subsection in two or more courts of appeals with respect to the same rule, the Commission shall file the materials set forth in paragraph (2) of this subsection in that court in which a proceeding was first instituted. The other courts shall thereupon transfer all such proceedings to the court in which the materials have been filed. For the convenience of the parties in the interest of justice that court may thereafter transfer all the proceedings to any other court of appeals.

(c) Objections not urged before Commission; stay of orders and rules; transfer of enforcement or review proceedings

(1) No objection to an order or rule of the Commission, for which review is sought under this section, may be considered by the court unless it was urged before the Commission or there was reasonable ground for failure to do so.

(2) The filing of a petition under this section does not operate as a stay of the Commission's order or rule. Until the court's jurisdiction becomes exclusive, the Commission may stay its order or rule pending judicial review if it finds that justice so requires. After the filing of a petition under this section, the court, on whatever conditions may be required and to the extent necessary to prevent irreparable injury, may issue all necessary and appropriate process to stay the order or rule or to preserve status or rights pending its review; but (notwithstanding section 705 of title 5) no such process may be issued by the court before the filing of the record or the materials set forth in subsection (b)(2) of this section unless: (A) the Commission has denied a stay or failed to grant requested relief, (B) a reasonable period has expired since the filing of an application for a stay without a decision by the Commission, or (C) there was reasonable ground for failure to apply to the Commission.

(3) When the same order or rule is the subject of one or more petitions for review filed under this section and an action for enforcement filed in a district court of the United States under section 78u(d) or (e) of this title, that court in which the petition or the action is first filed has jurisdiction with respect to the order or rule to the exclusion of any

other court, and thereupon all such proceedings shall be transferred to that court; but, for the convenience of the parties in the interest of justice, that court may thereafter transfer all the proceedings to any other court of appeals or district court of the United States, whether or not a petition for review or an action for enforcement was originally filed in the transferee court. The scope of review by a district court under section 78u(d) or (e) of this title is in all cases the same as by a court of appeals under this section.

(d) Other appropriate regulatory agencies

(1) For purposes of the preceding subsections of this section, the term "Commission" includes the agencies enumerated in section 78c(a)(34) of this title insofar as such agencies are acting pursuant to this chapter and the Secretary of the Treasury insofar as he is acting pursuant to section 78*o*-5 of this title.

(2) For purposes of subsection (a)(4) of this section and section 706 of title 5, an order of the Commission pursuant to section 78s(a) of this title denying registration to a clearing agency for which the Commission is not the appropriate regulatory agency or pursuant to section 78s(b) of this title disapproving a proposed rule change by such a clearing agency shall be deemed to be an order of the appropriate regulatory agency for such clearing agency insofar as such order was entered by reason of a determination by such appropriate regulatory agency pursuant to section 78s(a)(2)(C) or 78s(b)(4)(C) of this title that such registration or proposed rule change would be inconsistent with the safeguarding of securities or funds.

15 U.S.C. § 80a-42

§ 80a-42. Court review of orders

(a) Any person or party aggrieved by an order issued by the Commission under this subchapter may obtain a review of such order in the United States court of appeals within any circuit wherein such person resides or has his principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the entry of such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall be forthwith transmitted by the clerk of the court to any member of the Commission or any officer thereof designated by the Commission for that purpose, and thereupon the Commission shall file in the court the record upon which the order complained of was entered, as provided in section 2112 of title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record shall be exclusive, to affirm, modify, or set aside such order, in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission or unless there were reasonable grounds for failure so to do. The findings of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If application is made to the court for leave to adduce additional evidence, and it is shown to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceeding before the Commission, the court may order such additional

evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court affirming, modifying, or setting aside, in whole or in part, any such order of the Commission shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in section 1254 of title 28.

(b) The commencement of proceedings under subsection (a) to review an order of the Commission issued under section 80a-8(e) of this title shall operate as a stay of the Commission's order unless the court otherwise orders. The commencement of proceedings under subsection (a) to review an order of the Commission issued under any provision of this subchapter other than section 80a-8(e) of this title shall not operate as a stay of the Commission's order unless the court specifically so orders.

15 U.S.C. § 80b-13

§ 80b-13. Court review of orders

(a) Petition; jurisdiction; findings of Commission; additional evidence; finality

Any person or party aggrieved by an order issued by the Commission under this subchapter may obtain a review of such order in the United States court of appeals within any circuit wherein such person resides or has his principal office or place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the entry of such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall be forthwith transmitted by the clerk of the court to any member of the Commission, or any officer thereof designated by the Commission for that purpose, and thereupon the Commission shall file in the court the record upon which the order complained of was entered, as provided in section 2112 of title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record shall be exclusive, to affirm, modify, or set aside such order, in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission or unless there were reasonable grounds for failure so to do. The findings of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If application is made to the court for leave to adduce additional evidence, and it is shown to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to

adduce such evidence in the proceeding before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court affirming, modifying, or setting aside, in whole or in part, any such order of the Commission shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in section 1254 of title 28.

(b) Stay of Commission's order

The commencement of proceedings under subsection (a) shall not, unless specifically ordered by the court, operate as a stay of the Commission's order.

28 U.S.C. § 1331

§ 1331. Federal question

The district courts shall have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States.

17 C.F.R. § 201.360

§ 201.360 Initial decision of hearing officer and timing of hearing.

(a)(1) *When required*. Unless the Commission directs otherwise, the hearing officer shall prepare an initial decision in any proceeding in which the Commission directs a hearing officer to preside at a hearing, provided, however, that an initial decision may be waived by the parties with the consent of the hearing officer pursuant to § 201.202.

(2) *Time period for filing initial decision and for hearing*—(i) *Initial decision*. In the order instituting proceedings, the Commission will specify a time period in which the hearing officer's initial decision must be filed with the Secretary. In the Commission's discretion, after consideration of the nature, complexity, and urgency of the subject matter, and with due regard for the public interest and the protection of investors, this time period will be either 30, 75, or 120 days. The time period will run from the occurrence of the following events:

(A) The completion of post-hearing briefing in a proceeding where the hearing has been completed; or

(B) The completion of briefing on a § 201.250 motion in the event the hearing officer has determined that no hearing is necessary; or

(C) The determination by the hearing officer that, pursuant to § 201.155, a party is deemed to be in default and no hearing is necessary.

(ii) *Hearing*. Under the 120-day timeline, the hearing officer shall issue an order scheduling the hearing to begin approximately four months (but no more than ten months) from the date of service of the order instituting the proceeding. Under the 75-day

timeline, the hearing officer shall issue an order scheduling the hearing to begin approximately 2½ months (but no more than six months) from the date of service of the order instituting the proceeding. Under the 30-day timeline, the hearing officer shall issue an order scheduling the hearing to begin approximately one month (but no more than four months) from the date of service of the order instituting the proceeding. These deadlines confer no substantive rights on respondents. If a stay is granted pursuant to § 201.161(c)(2)(i) or § 201.210(c)(3), the time period specified in the order instituting proceedings in which the hearing officer's initial decision must be filed with the Secretary, as well as any other time limits established in orders issued by the hearing officer in the proceeding, shall be automatically tolled during the period while the stay is in effect.

(3) *Certification of extension; motion for extension.* (i) In the event that the hearing officer presiding over the proceeding determines that it will not be possible to file the initial decision within the specified period of time, the hearing officer may certify to the Commission in writing the need to extend the initial decision deadline by up to 30 days for case management purposes. The certification must be issued no later than 30 days prior to the expiration of the time specified for the issuance of an initial decision and be served on the Commission and all parties in the proceeding. If the Commission has not issued an order to the contrary within 14 days after receiving the certification, the extension set forth in the hearing officer's certification shall take effect.

(ii) Either in addition to a certification of extension, or instead of a certification of extension,

the Chief Administrative Law Judge may submit a motion to the Commission requesting an extension of the time period for filing the initial decision. First, the hearing officer presiding over the proceeding must consult with the Chief Administrative Law Judge. Following such consultation, the Chief Administrative Law Judge may determine, in his or her discretion, to submit a motion to the Commission requesting an extension of the time period for filing the initial decision. This motion may request an extension of any length but must be filed no later than 15 days prior to the expiration of the time specified in the certification of extension, or if there is no certification of extension, 30 days prior to the expiration of the time specified in the order instituting proceedings. The motion will be served upon all parties in the proceeding, who may file with the Commission statements in support of or in opposition to the motion. If the Commission determines that additional time is necessary or appropriate in the public interest, the Commission shall issue an order extending the time period for filing the initial decision.

(iii) The provisions of this paragraph (a)(3) confer no rights on respondents.

(b) *Content.* An initial decision shall include findings and conclusions, and the reasons or basis therefor, as to all the material issues of fact, law or discretion presented on the record and the appropriate order, sanction, relief, or denial thereof. The initial decision shall also state the time period, not to exceed 21 days after service of the decision, except for good cause shown, within which a petition for review of the initial decision may be filed. The reasons for any extension of time shall be stated in

the initial decision. The initial decision shall also include a statement that, as provided in paragraph (d) of this section:

(1) The Commission will enter an order of finality as to each party unless a party or an aggrieved person entitled to review timely files a petition for review of the initial decision or a motion to correct a manifest error of fact in the initial decision with the hearing officer, or the Commission determines on its own initiative to review the initial decision; and

(2) If a party or an aggrieved person entitled to review timely files a petition for review or a motion to correct a manifest error of fact in the initial decision with the hearing officer, or if the Commission takes action to review as to a party or an aggrieved person entitled to review, the initial decision shall not become final as to that party or person.

(c) *Filing, service and publication.* The Secretary shall promptly serve the initial decision upon the parties and shall promptly publish notice of the filing thereof on the SEC website; provided, however, that in nonpublic proceedings no notice shall be published unless the Commission otherwise directs.

(d) *Finality.* (1) If a party or an aggrieved person entitled to review timely files a petition for review or a motion to correct a manifest error of fact in the initial decision, or if the Commission on its own initiative orders review of a decision with respect to a party or a person aggrieved who would be entitled to review, the initial decision shall not become final as to that party or person.

(2) If a party or aggrieved person entitled to review fails to file timely a petition for review or a motion to correct a manifest error of fact in the initial decision, and if the Commission does not order review of a decision on its own initiative, the Commission will issue an order that the decision has become final as to that party. The decision becomes final upon issuance of the order. The order of finality shall state the date on which sanctions, if any, take effect. Notice of the order shall be published on the SEC website.