No. 17-130

IN THE

Supreme Court of the United States

RAYMOND J. LUCIA AND
RAYMOND J. LUCIA COMPANIES, INC.,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA

BRIEF OF AMICI CURIAE J.S. OLIVER CAPITAL MANAGEMENT, L.P. AND IAN O. MAUSNER IN SUPPORT OF PETITIONERS

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SUMMARY OF THE ARGUMENT AND INTEREST OF AMICI[1]

The question the Court addresses in this case is straightforward: Do the administrative law judges of the Securities and Exchange Commission wield "significant authority," *Buckley v. Valeo*, 424 U.S. 1, 125-26 (1976) (per curiam), such that they are "inferior officers" for purposes of the Appointments Clause? As Petitioners' brief explains and the government concedes, the answer is "yes." In adjudicating enforcement actions brought by the Commission, ALJs exercise a range of court-like powers this Court has already deemed to be characteristic of officers under the Clause, such as ruling on the admissibility of evidence, taking testimony, and conducting trials. *See* Petr. Br. at 21-24 (citing *Freytag v. Commissioner*, 501 U.S. 868, 881 (1991)); Resp. Br. 20-25.

The ALJs' procedural authority, however, is only one marker of their officer status. As demonstrated by the action the Commission instituted against amici, ALJs also have "significant discretion" to impose highly punitive sanctions, *Freytag*, 501 U.S. at 882, a fact that confirms their rank as constitutional officers, *see* Part I.A, and, in light of the Commission's increased resort to administrative enforcement

[1] Counsel for amici certify that they authored this brief in its entirety and that none of the parties or their counsel, nor any other person or entity other than amici or their counsel, made a monetary contribution intended to fund the preparation or submission of this brief. All parties have consented to the filing of this brief.

proceedings in recent years, highlights the constitutional necessity of subjecting the ALJs to the "public accountability" the Clause provides. *Edmond v. United States*, 520 U.S. 651, 660 (1997); *see* Part I.B. That discretion also means that the constitutional violation at issue in this case cannot be remedied by the Commission's ostensible "de novo" review of ALJ decisions; instead, this Court's precedents require an entirely new proceeding before a properly-constituted adjudicator, *see* Part II.A, though in amici's case the expiration of the statute of limitations mandates dismissal outright, *see* Part II.B.

Amicus J.S. Oliver Capital Management was a registered investment adviser that operated from 2004 to 2011, and amicus Ian O. Mausner was its co-founder and chief executive officer. They were respondents in a SEC administrative proceeding in which an ALJ found them liable for numerous violations and imposed a range of punishments. *In re J.S. Oliver Capital Mgmt.*, Release No. 649, 2014 WL 3834038, at *57-58 (Aug. 5, 2014). On review, the Commission largely affirmed the ALJ's decision, including her arbitrary determination as to how many violations amici allegedly committed. *In re J.S. Oliver Capital Mgmt.*, Release No. 4431, 2016 WL 3361166, at *25 (Jun. 17, 2016).[2]

In amici's case, and that of Petitioners, the sanctions included disbarment—a punishment that typically destroys a defendant's entire livelihood. But for

[2] The case is now pending before the United States Court of Appeals for the Ninth Circuit. *J.S. Oliver Capital Mgmt. v. S.E.C.*, No. 16-72703 (9th Cir. filed Aug. 15, 2016).

amici the punishment went further. The ALJ ordered them to pay more nearly $20 million in disgorgement and civil penalties, based on a statutory and regulatory scheme that gives ALJs enormous leeway in defining violations and in assigning monetary sanctions in response.

Amici are not alone. Following statutory changes that granted ALJs virtually all the enforcement powers of a federal district court, in recent years the Commission has increasingly used administrative proceedings—rather than actions in federal court—to secure massive financial penalties against firms and individuals. Over the same time period, the Commission has enjoyed a nearly 50% increase in the total dollar amount defendants have been ordered to pay. This growth has been accompanied by a *decrease* in transparency surrounding the Commission's enforcement actions. In light of this Court's repeated reminders that accountability is the Appointments Clause's touchstone, cases like amici's highlight the importance of subjecting the ALJs "significant authority" to the Clause's requirements.

The constitutional violation at issue in this case raises an additional question of critical importance for amici—that of remedy. If the Commission has its way, and is permitted to brush aside its improper appointments as if they never happened, amici face the real prospect of receiving no relief for their injuries.

Fortunately, this Court has already answered the remedy question: When a federal officer performing adjudicatory functions was unconstitutionally appointed, a person previously subject to that officer's

pretended authority is, at minimum, "entitled to a hearing before a properly appointed" adjudicator. *Ryder v. United States*, 515 U.S. 177, 188 (1995). This Court's precedent and the logic of the Appointments Clause itself require nothing less. The Commission cannot be heard to argue that its ostensible "de novo" review of ALJ decisions—as in amici's case—cures the constitutional defect. That is not a "remedy" this Court has ever endorsed, and for good reason, as it would render the Clause's "inferior officer" requirements a dead letter.

In fact, the only proper remedy for amici is dismissal outright. This Court has made it clear that the statute of limitations governing SEC enforcement actions serves as a critical check on the Commission's considerable powers to impose penalties. *See Kokesh v. S.E.C.*, 137 S. Ct. 1635 (2017); *Gabelli v. S.E.C.*, 568 U.S. 442 (2013). Because that limitations period has expired in amici's case, no new proceeding can be commenced and the action must be dismissed.

ARGUMENT

I. The ALJs' Significant Discretion Makes Constitutional Appointment Essential.

As Petitioners and the government discuss, the procedural authority ALJs exercise makes them "officers" under this Court's precedent. Petr. Br. at 21-24; Resp. Br. at 20-25. As amici's case illustrates, so too does the "significant discretion" ALJs enjoy regarding the range of sanctions they can impose in administrative proceedings. And the Commission's

increasing use of such proceedings to inflict significant punishments on alleged securities violators renders the Appointments Clause's check on government power all the more important.

A. The ALJs' discretionary authority renders them "officers" under the Appointments Clause.

As all parties acknowledge, the key question in this case is whether SEC ALJs wield the sort of "significant authority" this Court has recognized as the primary attribute of an "officer" under the Appointments Clause. *Buckley*, 424 U.S. at 125-26. As this Court explained in *Freytag*, the answer does *not* depend solely on whether the judicial officer has the power to "enter a final decision." 501 U.S. at 881; *contra* Pet. App. 13a (the Appointments Clause analysis "begins, and ends" with the question of "whether Commission ALJs issue final decisions"). Instead, determining officer status requires a holistic assessment of the "significance" of the officer's "duties and discretion." *Freytag*, 501 U.S. at 881. If the officer "exercise[s] significant discretion" in carrying out his functions, the Appointments Clause applies. *Id.* at 882.

As Petitioners explain, ALJs exercise "significant authority" in adjudicating the enforcement actions the Commission chooses to pursue through administrative proceedings. Petr. Br. at 21. That authority parallels the functions typically carried out by a federal district judge, including issuing subpoenas, ordering the production of evidence, ruling on motions,

conducting an evidentiary hearing, and issuing an initial decision. *See* Petr. Br. at 21-24 (listing ALJ powers); *Bandimere v. S.E.C.*, 844 F.3d 1168, 1179-80 (10th Cir. 2016) (describing the "important functions" through which SEC ALJs "exercise significant discretion"). Indeed, in amici's own proceeding, the ALJ conducted a five-day evidentiary hearing, supervised the testimony of thirteen witnesses, and admitted nearly 300 exhibits into evidence. *In re J.S. Oliver Capital Mgmt.*, 2014 WL 3834038, at *1. And when making rulings on evidence, the ALJ in fact had more latitude than a federal district judge, because SEC ALJs are not bound by the Federal Rules of Evidence. 42 C.F.R. § 93.519(b).

Yet as amici's case starkly demonstrates, an ALJ's discretionary authority is by no means limited to "[r]egulating the course of a proceeding." 17 C.F.R. § 201.111(d). ALJs also have broad latitude to impose substantial—even ruinous—punishments on individuals and firms in response to allegations of wrongdoing. Indeed, as the D.C. Circuit has recently explained, "the breadth of agency discretion is, if anything, at zenith when … fashioning … remedies and sanctions." *Am. Tel. & Tel. Co. v. F.C.C.*, 454 F.3d 329, 334 (D.C. Cir. 2006). This expansive punitive authority only confirms what *Freytag* already establishes—that SEC ALJs are indisputably "officers" for purposes of the Appointments Clause. *See* 501 U.S. at 881-82 (concluding that special tax judges' "duties and discretion" rendered them "inferior officers").

1. As amici's case makes evident, ALJs have an impressive range of sanctions available to them, in-

cluding cease-and-desist orders, revocation of investment advisor registrations, suspension and permanent disbarment, and monetary penalties. *See Kokesh*, 137 S. Ct. at 1640 (noting the Commission's "full panoply of enforcement tools"); *In re J.S. Oliver Capital Mgmt.*, 2014 WL 3834038, at *57-58 (imposing such sanctions on amici). And they exercise significant discretion as to each.

Consider an ALJ's power to bar individuals from working in the securities industry. *See* 15 U.S.C. § 80b-3(f) (granting the authority to "bar any … person from being associated with an investment adviser, broker, dealer, municipal securities dealer, municipal advisor, transfer agent, or nationally recognized statistical rating organization"); 15 U.S.C. § 78u-3(f) (granting the authority to permanently prohibit a defendant "from acting as an officer or director of any [securities] issuer"). As many commentators have noted, the authority to prohibit someone from continuing in his chosen profession is one of the most powerful weapons in the Commission's arsenal. *See, e.g.*, *PAZ Sec., Inc. v. S.E.C.*, 494 F.3d 1059, 1065 (D.C. Cir. 2007) (describing a lifetime bar as "the securities industry equivalent of capital punishment").

In determining whether such a severe punishment is warranted, ALJs conduct an open-ended analysis guided by the multiple, non-dispositive factors commonly known as the *Steadman* factors. *See Steadman v. S.E.C.*, 603 F.2d 1126, 1140 (5th Cir. 1979); *see also S.E.C. v. Patel*, 61 F.3d 137, 141 (2nd Cir. 1995) (articulating a similar array of factors). They include broad considerations such as the egregious-

ness of the respondent's actions, the isolated or recurrent nature of the violation, the degree of scienter, and the opportunity for future misconduct. *See In re J.S. Oliver Capital Mgmt.*, 2016 WL 3361166, at *10 & n.53, (enumerating factors and citing *Steadman*). The inquiry into the appropriateness of such a sanction is a "flexible" one, allowing ALJs to pick and choose among the factors in making their determinations. *In re Steven R. Markusen*, Release No. 1079, 2016 WL 6647632, at *6 (Nov. 9, 2016).

As a result, ALJs wield "significant discretion" in determining whether firms and individuals accused of securities laws violations will be able to stay in business. Indeed, such penalties can be crippling, as the order entered against amici demonstrates. Not only did the ALJ order amici to "cease and desist from committing or causing violations," she also revoked J.S. Oliver's investment advisor registration and barred Mausner from association with virtually any securities market participant. *In re J.S. Oliver Capital Mgmt.*, 2014 WL 3834038, at *57-58. In so doing, the ALJ made maximal use of broad new powers Congress conferred in Dodd-Frank at the Commission's request—the authority to bar securities laws violators from associating not only with professionals in their field, but also with members of any other enumerated class of securities market participants—a measure that gives ALJs even greater discretion in determining how harshly to punish individuals for their alleged misconduct. *See Bartko v. S.E.C.*, 845 F.3d 1217, 1220-21 & n.2, 1225-26 (D.C. Cir. 2017) (describing the genesis and effect of rules allowing "collateral bars" precluding individuals from associating with

classes of securities professionals with which they have not previously been associated).

2. Disbarment, however, is only the beginning. ALJs also have broad discretionary authority in imposing monetary sanctions. In fact, they have considerable latitude not only in deciding whether to impose such penalties in the first place, but also in determining their magnitude.

For starters, ALJs can order the disgorgement of any funds "properly attributable" to the defendant's legal violations. *Kokesh*, 137 S. Ct. at 1640; *see also* 15 U.S.C. § 77h-1(e) (empowering the Commission to "enter an order requiring accounting and disgorgement" in "any cease-and-desist proceeding"). This is a loose nexus; the penalty imposed need only be a "reasonable approximation" of the gains resulting from the violation. *Montford & Co. v. S.E.C.*, 793 F.3d 76, 84 (D.C. Cir. 2015) (citing *S.E.C. v. First City Fin. Corp.*, 890 F.2d 1215, 1231 (D.C. Cir. 1989)); *see also* Relief—Disgorgement, 7 Bus. & Com. Litig. Fed. Cts. § 79:42 (4th ed.) (describing reasonable approximation as a "lenient standard"). Indeed, the ALJ oftentimes does not even have to be satisfied that the alleged illegal activity was the proximate cause of the injury a disgorgement order is meant to address. *See S.E.C. v. Teo*, 746 F.3d 90, 107 (3d Cir. 2014) (concluding that the Commission need only "prove but-for causation to assert a reasonable approximation of illegal profits"); *S.E.C. v. DiBella*, 587 F.3d 553, 572 (2d Cir. 2009) (endorsing a but-for theory of causation for disgorgement).

Moreover, in ordering disgorgement, ALJs are not limited to the defendant's actual enrichment. Instead, ALJs have the latitude to include benefits received by third parties, and therefore "exceed[] the profits gained as a result of the violation." *Kokesh*, 137 S. Ct. at 1644; *see also id.* (disgorgement can be ordered even when the defendant has received no benefit at all). As this Court recently noted, "[i]n such cases, disgorgement does not simply restore the status quo; it leaves the defendant worse off." *Id.* at 1645.

ALJs' powers do not end there. If they broadly deem it to be in the "public interest," they can also impose significant civil monetary penalties. *E.g.*, 15 U.S.C. § 80b-3(i)(1). Here, too, ALJs exercise considerable latitude, first in identifying the number of violations committed—a highly flexible determination we discuss in detail below—and then selecting a penalty amount of up to $150,000 per violation for natural persons and $750,000 per violation for an entity. 17 C.F.R. § 201.1004, Subpt. E, Table IV.

By statute, ALJs deciding whether a civil penalty is warranted "may consider" six broad factors, including any "matter[] as justice may require." 15 U.S.C. § 80b-3(i)(3); *see also id.* (listing other factors, including the harm to other persons, the extent of unjust enrichment, and the need for deterrence). ALJs also have significant leeway in setting the penalty amount—the statutory scheme governing securities violations sets an upper limit on civil penalties, but "the actual amount of the penalty is left up to the discretion" of the adjudicator. *S.E.C. v. Kern*, 425 F.3d 143, 153 (2d Cir. 2005).

Importantly, ALJs also get to decide how many "acts or omissions" to sanction. *See* 15 U.S.C. § 80b-3(i)(2) (setting forth the penalties "for each act or omission"). When a respondent's violation consists of an ongoing course of conduct—as it did in amici's case—ALJs have enormous latitude in choosing what subset of that conduct they will count as a discrete violation, and thus in declaring the total number of violations. *See In re Anthony Fields*, Release No. 4028, 2015 WL 728005, at *24 n.162 (Feb. 20, 2015) ("Although the statutory text provides that a penalty may be imposed for 'each act or omission,' it leaves the precise unit of violation undefined."). ALJs have chosen, for example, to define violations in terms of units of time (by month or year, for example), the number of defrauded customers, and the number of individual securities transactions involved in the conduct, or simply to declare all of the conduct at issue to be a single violation. *See In re J.S. Oliver Capital Mgmt.*, 2016 WL 3361166, at *14 (citing examples).

Amici's case offers a telling example of the tremendous discretion ALJs exercise in setting penalties. The law judge determined a total number of violations by assigning one for each month during which amici allegedly engaged in their wrongful course of conduct. *In re J.S. Oliver Capital Mgmt.*, 2014 WL 3834038, at *55. She did so despite the fact there was no basis in the evidence for delimiting their conduct in monthly terms, as it included thousands of securities transactions made on a daily basis. *See In re J.S. Oliver Capital Mgmt.*, 2016 WL 3361166, at *15 ("[T]he law judge did not identify an evidentiary basis to conclude that one or more 'act[s] or omission[s]' violating the securities laws occurred during

each month for which she imposed a civil penalty."); *see also Rapoport v. S.E.C.*, 682 F.3d 98, 107 (D.C. Cir. 2012) (describing as "faulty" an ALJ civil penalty based on an arbitrary time-based determination of the number of violations).

The result was a penalty assessment of $18 million, even though the judge recognized that the conduct in question actually caused far less financial "harm" to the affected parties. *In re J.S. Oliver Capital Mgmt.*, 2014 WL 3834038, at *55. And the penalty could have been even higher. As the Commission explained, the ALJ would have been equally justified in determining the violations based on the number of transactions at issue, finding thousands of violations rather than fifteen. *In re J.S. Oliver Capital Mgmt.*, 2016 WL 3361166, at *19.

3. The considerable discretionary authority ALJs exercise is only magnified by the high degree of deference their decisions enjoy. Though nominally the Commission has the authority to assess the ALJ's findings and conclusions de novo, *In re Theodore W. Urban*, Release No. 63456, 2010 WL 5092728, at *2 (Dec. 7, 2010) (citing 17 C.F.R. § 201.411(a)), in reality such wholesale reconsideration is exceedingly rare. To begin with, the Commission's exercise of such review is largely discretionary. *See* 17 C.F.R. § 201.411(b) (specifying that review is discretionary in all but a handful of contexts). When neither party files a petition for review, the ALJ's "initial" order becomes final. 17 C.F.R. § 201.360(d)(2). In practice, this is almost always what happens. According to the Commission's own records, in 90% of administrative proceedings the ALJ's initial decision becomes final

with no further review by the Commission. *See Bandimere*, 844 F.3d at 1180 n.25 (citing S.E.C., *ALJ Initial Decisions,* https://www.sec.gov/alj/aljdec.shtml (last visited (Feb. 27, 2018)).

Even when the Commission *does* review an ALJ decision, the law judge's findings and conclusions exert significant influence. *See Landry v. F.D.I.C.*, 204 F.3d 1125, 1143 n.3 (D.C. Cir. 2000) (Randolph, J., concurring) (emphasizing that "[d]e novo review does not mean that the ALJ's recommended decisions are without influence"). For instance, the Commission accepts an ALJ's credibility finding "absent overwhelming evidence to the contrary." *In re Robert Thomas Clawson*, Exchange Act Release No. 48,143, 2003 WL 21539920, at *2 (July 9, 2003). And as the Commission itself has emphasized, "the law judge is in the best position to make findings of fact." *In re the Application of Nasdaq Stock Mkt.*, Release No. 57741, 2008 WL 1902073, at *1 (Apr. 30, 2008).

In addition, even under ostensible de novo review, an ALJ's conclusions have a substantial anchoring effect. As the Commission noted in the case at bar, "the findings that a law judge makes … well might inform [its] determination of the appropriate sanction in the event of any appeal." Pet. App. 242a. Amici's case offers a telling illustration. The Commission reduced the total civil penalty the ALJ ordered, but adopted her questionable methodology in determining the number of violations at issue—despite the Commission's acknowledgement that there was no evidentiary basis for the approach taken in this case and that, as a general matter, it was dubious to "assess[] penalties on the basis of a unit of time" in situations

where the unit's relationship to the violating acts was unclear. *In re J.S. Oliver Capital Mgmt.*, 2016 WL 3361166, at *15. In short, as the Commission itself has acknowledged, an ALJ's findings and conclusions play a "vital role … in the Commission's decisional process." Pet. App. 241a.

The Commission's reluctance to deviate from ALJ penalty determinations means that such decisions are often the final word. It goes without saying that, under longstanding principles of administrative law, judicial review of SEC sanctions is "extraordinarily deferential." *Rapoport*, 682 F.3d at 107. Under this Court's precedent, such decisions are not to be disturbed unless they are "unwarranted in law or ... without justification in fact." *Butz v. Glover Livestock Comm'n Co.*, 411 U.S. 182, 185-86 (1973) (quotation marks omitted). As a result, even in the small handful of cases nominally subject to Commission review, in the realm of sanctions SEC ALJs indubitably exercise the sort of "significant discretion" this Court has recognized as being the hallmark of "officer" status under the Appointments Clause. *Freytag*, 501 U.S. at 882.

B. The Commission's increasing use of administrative proceedings makes ALJ accountability all the more important.

In light of the significant discretionary authority SEC ALJs exercise in punishing securities violations, it is imperative that the Commission be publicly accountable for its administrative enforcement efforts. In reality, the ALJs' considerable sanctioning discretion is only enhanced by the Commission's growing

resort to administrative proceedings in order to seek and impose penalties, of which amici's case is but one example. Following recent statutory changes giving ALJs the considerable powers described above, the Commission pursues more of its enforcement objectives out of public view, rendering the Commission's evasion of the Appointments Clause's accountability requirement all the more troubling.

1. As this Court has repeatedly explained, the Appointments Clause's requirements do not "merely deal[] with etiquette or protocol," but instead serve a "less frivolous purpose." *Buckley*, 424 U.S. at 125. They provide one of the "significant structural safeguards of the constitutional scheme"—they "ensure public accountability" in the appointment of federal government officers. *Edmond*, 520 U.S. at 659-60. Accordingly, the Framers carefully structured the appointment power to make sure that those who wielded it "were accountable to political force and the will of the people." *Freytag*, 501 U.S. at 884. This is obviously true with respect to the power to appoint "principal officers," which the Clause "carefully husband[s] … to limit its diffusion," ensuring that nomination and approval of the federal government's most important officials will happen in full public view. *Id.* at 883.

So too with the Clause's "inferior officer" provision. Though for reasons of "administrative convenience" that provision allows for appointment of certain officers without the dual check of nomination by the President and confirmation by the Senate, *Edmond*, 520 U.S. at 660, it nevertheless vests the appointment of those who wield "significant authority" in a select class of government actors, *Buckley*, 424

U.S. at 126—namely the President, the courts of law, and the heads of departments. U.S. Const., art. II, § 2, cl. 2; *see also Freytag*, 501 U.S. at 884 ("Even with respect to 'inferior Officers,' the Clause allows Congress only limited authority to devolve appointment power …."). In so doing, the Clause provides for a "clear and effective chain of command" that permits the public to "'determine on whom the blame or the punishment of a pernicious measure … ought really to fall.'" *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 497-98 (2010) (quoting The Federalist No. 70, at 476 (Alexander Hamilton) (J. Cooke ed. 1961)). In short, by concentrating the appointments power in relatively few hands, the Clause helps ensures that the mechanisms by which federal officers come to power are visible to the public. *See Edmond*, 520 U.S. at 659-60.

2. The *ex ante* accountability the Clause requires is all the more important given the indication that the Commission increasingly channels its enforcement practices into administrative proceedings.

To better understand the Commission's enforcement practices, some background is helpful. As a general matter, the Commission can bring most enforcement actions either in federal district court or in its own administrative forum. Urska Velikonja, *Securities Settlements in the Shadows*, 126 Yale L.J. Forum 124, 124 (2016). The Commission's power to impose sanctions administratively dates back to the New Deal, when Congress first authorized administrative proceedings in a narrow class of cases and for a narrow set of sanctions. These proceedings initially

were limited to actions against members of the securities industry, and administrative sanctions were limited to suspensions or bars; the Commission did not have the power to seek civil penalties. Resp. Br. at 31. In 1990, Congress authorized the Commission to obtain money penalties for violations of the securities statutes via administrative proceedings, but only against parties it already regulated. *Id.* at 31-32. As a result, in many cases the Commission still needed to go to court if it wanted to have access to the full range of penalties available.

That changed with passage of the Dodd-Frank Act of 2010, in which Congress authorized the Commission to use administrative process to impose monetary sanctions on any person, whether regulated or not. *See, e.g.*, 15 U.S.C. § 78u-2(a). With this change, the Commission can now use its internal administrative proceedings—with violations and sanctions imposed by an ALJ subject to discretionary Commission review—to obtain "most of the remedies that civil litigation offers." David Zaring, *Enforcement Discretion at the SEC*, 94 Tex. L. Rev. 1155, 1164 (2016); *see also* Resp Br. at 32.

The results of this increased enforcement authority are notable. Following passage of Dodd-Frank, the Commission has increasingly resorted to administrative enforcement as a means of imposing penalties on alleged violators. While it used to bring about half of its enforcement actions in court, between 2010 and 2013 the Commission pursued approximately two-thirds of its enforcement actions before its own ALJs. Urska Velikonja, *Reporting Agency Performance: Behind the SEC's Enforcement Statistics*, 101 Cornell L.

Rev. 901, 964 (2016). In 2014, that figure jumped to 81%. *Id.* And even when one accounts for the recent increase in the number of cases that have always been brought in an administrative forum, in 2014 the Commission went before an ALJ in nearly two-thirds of the cases that it historically would have considered bringing in court. *Id.* at 965; *but cf.* Brief for Amici Curiae Urska Velikonja and Joseph A. Grundfest at 12-13 (indicating that, since 2014, administrative enforcement has returned to pre-Dodd-Frank levels).

The Commission has been quite upfront that Dodd-Frank has impacted its enforcement choices. *See* Gretchen Morgenson, *At the SEC, a Question of Home-Court Edge*, N.Y. Times (Oct. 5, 2013), http://tinyurl.com/ycpydmgu (quoting SEC enforcement director Andrew Ceresney as saying that the Commission would be "bringing more administrative proceedings given the recent statutory changes"). And although causation is difficult to establish with certainty, it bears noting that, since Dodd-Frank's passage, the total monetary sanctions the Commission has secured have increased significantly—by nearly 50%. *See* S.E.C., *FY 2015 Annual Performance Report* 41 (2016) (noting \$2.85 billion in civil penalties and disgorgement orders in 2010 and \$4.2 billion in 2015).

One less obvious—but no less important—change is the Commission's effort to shift more of its *settlement* activities to the administrative forum as well. Federal regulations give the Commission authority to settle cases rather than litigate them, and the Commission can choose whether to pursue such settlements administratively or in court. *See* Velikonja,

Securities Settlements, supra, at 128; *see generally* 17 C.F.R. § 201.240.

The choice of forum makes a difference: Courts review proposed settlements to ensure they are "fair and reasonable," and will not disserve the "public interest." *S.E.C. v. Citigroup Glob. Markets, Inc.*, 752 F.3d 285, 294 (2d Cir. 2014). The rules governing the Commission's administrative practice impose no such requirements, leading to settlement "review" that is often likely to be no more than a rubber stamp. *See* Velikonja, *Securities Settlements, supra*, at 132-33. And the significant punishments the Commission can now seek administratively give those subject to enforcement actions stronger incentive to reach a compromise. *See* Stephen J. Choi and Adam C. Pritchard, *The SEC's Shift to Administrative Proceedings: An Empirical Assessment*, N.Y.U. Law & Economics Research Paper Series, Working Paper No. 16-10 at 39 (Feb. 2016), *available at* http://tinyurl.com/yazvkvnz ("[T]he SEC's ability to extract settlements has increased with the flexibility to choose its forum provided by Dodd Frank.").

Little surprise, then, that in the wake of Dodd-Frank the Commission pursues far more settlements administratively than in court. The numbers are stark: Before Dodd-Frank, the Commission filed more settlements in district court than it did administratively; by 2015, it was filing five times as many in administrative proceedings than in court. Velikonja, *Securities Settlements, supra*, at 129. Indeed, in 2014 and 2015 *every* settlement with a large bank was handled administratively. *Id.* at 130.

The end result of this broad shift in the Commission's enforcement practices is that SEC ALJs exercise their "significant discretion" in finding and punishing securities violations increasingly out of public view. That lack of "public accountability," *Edmond*, 520 U.S. at 660, is precisely why ALJ appointments must be constitutionally proper.

II. The Proper Remedy For An Appointments Clause Violation Is A New Proceeding Or Dismissal Outright.

The conclusion that SEC administrative proceedings violate the Appointments Clause raises the question of remedy. The Commission likely will contend that it can cure these long-running constitutional defects with a quick but sweeping fix: simply "ratifying" the prior administrative proceedings in all cases that have not reached final judgment. This Court's precedents, however, make ratification impossible. They require that the Commission bring a new proceeding in every case affected by an Appointments Clause violation. And they prohibit a new proceeding in cases—like amici's—where the statute of limitations has expired; in those cases, the required outcome is dismissal.

A. Persons subjected to a proceeding that violated the Appointments Clause are entitled to an entirely new proceeding.

As Petitioners ably explain, under this Court's precedent the necessary remedy for an Appointments Clause violation is an entirely new proceeding. *See* Petr. Br. at 42-49. *Ryder* makes this clear: In light of

the violation in that case, this Court concluded that the petitioner was "entitled to a hearing" before a "properly appointed" adjudicator. 515 U.S. at 188. Numerous cases confirm the principle; a defect in the appointment of an adjudicator undermines "the validity of … the proceeding" itself. *Freytag*, 501 U.S. at 879; *see also Nguyen v. United States*, 539 U.S. 69, 83 (2003) (requiring "fresh consideration of petitioners' appeals" by a properly-constituted appellate panel); *United States v. L. A. Tucker Truck Lines, Inc.*, 344 U.S. 33, 38 (1952) (failure to appoint ALJ in compliance with the Administrative Procedure Act "was an irregularity which would invalidate a resulting order").

Nothing in this Court's precedent justifies a different remedy. The Commission's apparent plan to have its improperly-appointed ALJs simply reaffirm their prior decisions falls well short of the mark, for at least two reasons. First, as Petitioners explain, despite the Commission's "ratification" order, those ALJs have not yet been properly appointed and therefore cannot conduct new proceedings, let alone give legal effect to their earlier findings and conclusions by rubber stamping them. *See* Petr. Br. at 50-53. Second, as Petitioners also note, because the ALJs' prior actions are a nullity, there is nothing for them to "to ratify or revise" in response to the Commission's order. *In re Pending Administrative Proceedings*, Securities Act Release No. 10,440, 2017 WL 5969234, at *1 (Nov. 30, 2017); *see also* Petr. Br. 46-48; *F.E.C. v. NRA Political Victory Fund*, 513 U.S. 88, 98 (1994) ("[I]t is essential that the party ratifying should be able … to do the act ratified at the time the act was done." (quotation marks omitted)).

Nor can the agency argue, as it may on remand, that the Commission's *own* review of the ALJ decision in amici's case has already remedied the constitutional injury they suffered. In *Ryder* this Court addressed—but did not decide—the question of whether a properly-constituted tribunal's de novo review of a decision rendered by an improperly-appointed inferior officer could remedy an Appointments Clause violation. 515 U.S. at 186-88. The Court concluded that, because the superior tribunal in that case (the Court of Military Appeals) exercised "narrower" authority than the inferior, unconstitutional adjudicator (the Coast Guard Court of Military Review), the proceeding in the superior tribunal was not an adequate substitute for the defective prior proceeding. *Id.* at 187.

Under *Ryder*, Commission review does not cure the constitutional defect at issue. To begin with, as in *Ryder*, the properly-constituted tribunal here—i.e., the Commission—exercises "narrower" authority than the SEC ALJs. Though nominally the Commission can review ALJ decisions de novo, in practice its review is limited—as amici have already explained. *See supra* at 12-14. Indeed, both the Commission and the Court of Military Appeals in *Ryder* exercise discretionary review, meaning that many cases are never reexamined at all. *See* 515 U.S. at 187 (citing the "good cause" standard for granting review in the Court of Military Appeals); 17 C.F.R. § 201.411(b) (specifying that Commission review is largely discretionary). And like the Court of Military Appeals in relation to the Court of Military Review below it, the Commission generally defers to the ALJs factual findings. *See Ryder*, 515 U.S. at 187 (the Court of Military

Appeals generally "will not reevaluate the facts"); *supra* at 13-14 (noting Commission's deference to ALJ). Thus the Commission's "scope of review" is comparable to that of the Court of Military Appeals, 515 U.S. at 187, defeating any suggestion that the Commission has special curative powers.

In addition, the reason that hypothetical de novo review was possibly significant in *Ryder* was because, in that scenario, the properly-constituted Court of Military Appeals would have had the *exact same* powers as the improperly-constituted Court of Military Review—i.e., "discretion to review claims of error, revise factual determinations, and revise sentences." 515 U.S. at 187. In this case, however, the Commission's ostensible "de novo" review authority does not give it anything like the same powers the ALJ has. In particular, it lacks all the capability the ALJs have to shape the record. *See, e.g.,* 17 C.F.R. § 201.411(a) (noting the Commission can make new findings and reach new conclusions only "on the basis of the record" created by the ALJ); Petr. Br. at 24-25 (describing the ALJs' record-shaping function). Accordingly, even had the *Ryder* Court concluded that de novo review in that case would have rendered harmless any constitutional violation—which the Court did not, *see* 515 U.S. at 186—such a ruling would not dictate a similar conclusion here.

Most importantly, had the *Ryder* Court actually reached this question, logic and precedent dictate that review by a properly-constituted adjudicator cannot cure the constitutional injury perpetrated by an improperly-appointed adjudicator, for two reasons.

First, permitting superior review to cure an unconstitutional appointment of inferior officers would render pointless the Appointment Clause's two-tier structure. What would be the purpose of setting forth constitutional requirements for the appointment of inferior officers if every violation of those strictures can be remedied by the nominal retention of de novo review authority by a department head? Such a rule would permit Congress and federal agencies to dispense with the Appointments Clause by legislative or administrative fiat. *See, e.g.*, 5 U.S.C. § 557(b) ("On appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial decision …."); 17 C.F.R. § 201.411(a) ("The Commission may affirm, reverse, modify, set aside or remand for further proceedings, in whole or in part, an initial decision by a hearing officer and may make any findings or conclusions that in its judgment are proper and on the basis of the record."). Considering the Clause's status as one of "the most significant structural provisions of the constitutional scheme," *Edmond*, 520 U.S. at 659, such a workaround is impermissible.

Second, this curative theory is incompatible with this Court's decision in *Freytag*. As Petitioners and the government explain, *Freytag* dismissed the suggestion that officer status turns solely on finality in decisionmaking. *See* Petr. Br. at 27-29; Resp. Br. at 33-34. This Court was clear: The fact that an official's actions are subject to review by a superior does not preclude "officer" status under the Clause. *See* 501 U.S. at 880-82 (rejecting the argument that "special trial judges may be deemed employees … because they lack authority to enter a final decision"). Instead,

the test is whether the official exercises "significant discretion." *Freytag*, 501 U.S. at 882.

To hold that the possibility of de novo review by a superior cures any violation stemming from an unconstitutional appointment would contravene *Freytag*. If "inferior officer" status does not depend on scope of superior officer review, then neither can the question of whether there is a redressable constitutional injury. The minimally-satisfactory remedy, therefore, is a new proceeding before a properly-appointed adjudicator.

B. The statute of limitations prohibits the Commission from subjecting amici to a new proceeding.

While a new proceeding is generally the proper remedy for an Appointments Clause violation, that remedy is inapplicable to amici. Because the statute of limitations applicable to SEC enforcement actions has expired with respect to amici's alleged misconduct, the proceedings against them must be dismissed.

1. As this Court has recently and repeatedly made clear, SEC enforcement actions are fully subject to the five-year statute of limitations governing government enforcement actions generally, 28 U.S.C. § 2462. *See Kokesh*, 137 S. Ct. at 1643-45 (Section 2462 applies to SEC claims for disgorgement); *Gabelli*, 568 U.S. at 454 (Section 2462 is not tolled under the "discovery rule"). That statute states, in relevant part, that a "proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be

entertained unless commenced within five years from the date when the claim first accrued." § 2462.

This limitations period prohibits the Commission from re-instituting enforcement proceedings against respondents—like amici here—whose alleged violations occurred more than five years ago.[3] *See In re J.S. Oliver Capital Mgmt.*, 2016 WL 3361166, at *6 (last charged conduct took place in 2011). Under the statute, the Commission must "commence" an enforcement proceeding within the time bar. § 2462. It has not done so in amici's case, because the proceedings it instituted were invalid from the start.

To "commence" the enforcement action against amici, the Commission issued an Order Instituting Proceedings (OIP) that outlined the charges against the respondent and assigned the matter to an ALJ. *In re J.S. Oliver Capital Mgmt.,* Release No. 3658, 2013 WL 4647195, at *9 (Aug. 30, 2013). The Commission's own rules are clear about the OIP's effect: "The Commission *commences* proceedings to enforce the Federal securities laws by issuing an 'order instituting proceedings.'" Rules of Practice, Release No. 35833, 1995 WL 368865, at *27 (June 9, 1995) (commenting on SEC Rule of Practice 141(a)) (emphasis added).

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[3] If the Court rules that the ALJ appointments at issue in this case were constitutionally improper, amici intend to ask the Ninth Circuit to dismiss the enforcement action against them in light of the statute of limitations. Amici take no position as to whether the same remedy would be warranted in other enforcement actions currently pending in the federal Courts of Appeals or before the agency. Such a determination will depend on the particular facts of each case.

Because none of the ALJs employed by the agency at the time of the OIP had been constitutionally appointed, the OIP itself was a nullity. *See Freytag*, 501 U.S. at 879 (a defect in the appointment of an adjudicator "goes to the validity of the [administrative] proceeding"); *L. A. Tucker Truck Lines,* 344 U.S. at 38 (failure to appoint an ALJ in compliance with the Administrative Procedure Act "was an irregularity which would invalidate a resulting order"); *cf. also Papasan v. Allain*, 478 U.S. 265, 276 (1986) (government action taken pursuant to unconstitutional authority is without legal effect, because the "authorization for such action is a nullity" (citing *Ex parte Young*, 209 U.S. 123, 159-60 (1908)). And because the OIP had no legal effect, the Commission never "commenced" a lawful proceeding against amici.

Accordingly, if the Commission wishes to pursue an enforcement action against amici on remand, it will need to institute a new proceeding under a new OIP. That it cannot do, as the five-year limitations period under § 2462 has expired. *See United States v. Crawford*, 60 F. App'x 520, 531 (6th Cir. 2003) (when an original indictment is constitutionally defective, the government cannot file a new indictment outside the limitations period absent statutory permission); *United States v. Gillespie*, 666 F. Supp. 1137, 1141 (N.D. Ill. 1987) (an indictment returned by a grand jury "acting without legal authority" is "void," and cannot toll the statute of limitations); *United States v. Crysopt Corp.*, 781 F. Supp. 375, 378 (D. Md. 1991): ("An invalid indictment ... clearly cannot serve to block the door of limitations as it swings closed.").

Nor can the Commission solve the limitations problem through the alchemy of "ratification," as it purports to do with respect to the unconstitutional appointments themselves. *See In re Pending Administrative Proceedings*, 2017 WL 5969234, at *1 ("[T]he Commission—in its capacity as head of a department—hereby ratifies the agency's prior appointment[s] …."). To be sure, had the OIP in this case instituted proceedings before the Commission *itself*—as it could have—there would be no statute of limitations problem. *See* 17 C.F.R. § 201.110 ("All proceedings shall be presided over by the Commission or, if the Commission so orders, by a hearing officer.").

But the Commission cannot now travel back in time to cure the issuance of an OIP that was invalid at the outset. That is precisely the maneuver this Court squarely rejected in *NRA Political Victory Fund*. In that case, the Court held that the Solicitor General could not retroactively authorize the Federal Elections Commission to file a petition for certiorari after the deadline for filing had passed. *See* 513 U.S. at 98. The Court's reasoning was simple: For "ratification" to be effective, the ratifying party "'should be able not merely to do the act ratified at the time the act was done, *but also at the time the ratification was made*.'" *Id.* (quoting *Cook v. Tullis*, 85 U.S. 332, 338 (1873)). Because the Solicitor General's authorization "simply came too late in the day to be effective," the Court dismissed the petition. *Id.* at 98-99. In amici's case, the same rule applies: The Commission *could* have authorized the issuance of a valid OIP earlier, but because it is "simply … too late" to do so now under § 2462, dismissal is the only proper outcome.

2. Dismissal is also proper in light of the principles underlying § 2462 and statutes of limitations generally. At this point, amici have been subject to the Commission's enforcement efforts for at least five years, with several more to come unless the proceedings are brought to an end. As this Court has long recognized, statutes of limitations "set[] a fixed date when exposure to the specified Government enforcement efforts end[]." *Gabelli*, 568 U.S. at 448. Because such finality is "'vital to the welfare of society,'" *id.* at 449 (quoting *Wood v. Carpenter*, 101 U.S. 135, 139 (1879)), it is "'utterly repugnant to the genius of our laws'" if enforcement actions can be brought "'at any distance of time,'" *id.* at 452 (quoting *Adams v. Woods*, 6 U.S. 336, 342 (1805)).

It will be no answer for the Commission to argue that it should not be subject to the limitations period because it reasonably believed—until now—that its ALJs were properly appointed. In *NRA Political Victory Fund*, the Court dismissed the FEC's petition for certiorari despite the good reasons the agency had for thinking it had the authority to file one independently of the Solicitor General—including that it had repeatedly done so in the past, with no objections raised. *See* 513 U.S. at 97; *cf. also Menominee Indian Tribe v. United States*, 136 S. Ct. 750, 756-57 (2016) (a plaintiff's "mistaken belief" about its legal rights does not warrant equitable tolling of a statute of limitations).

Here, the Commission had notice of the flaws in its appointments regime for years, and persisted in pursuing its enforcement actions—against amici and others—through constitutionally-dubious means. *See, e.g.*, *Hill v. S.E.C.*, 114 F. Supp. 3d 1297, 1316-19

(N.D. Ga. 2015) (addressing Appointments Clause claim); Kent Barnett, *Resolving the ALJ Quandary*, 66 Vand. L. Rev. 797, 809-14 (2013) (same). Given that "even wrongdoers are entitled to assume that their sins may be forgotten," *Wilson v. Garcia*, 471 U.S. 261, 271 (1985), dismissal of the Commission's "stale claims" against amici will "promote justice" and provide the "security and stability" that this Court has recognized as the "basic policies" animating limitations provisions. *Gabelli*, 568 U.S. at 448-49 (quotation marks omitted).

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted,

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