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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
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January 30, 2018

BY EMAIL/UPS

The Honorable Brenda P. Murray
Chief Administrative Law Judge
U.S. Securities and Exchange Commission
100 F Street, NE
Mail Stop 1090
Washington, DC 20549

Re: ***Matter of Chiappone, et al.*****, File No. 3-15514**

Dear Chief Judge Murray:

The Division writes in response to the January 18 and 19, 2018 letters submitted by Brian T. Mayer, Philip S. Rabinovich, Frank H. Chiappone, William F. Lex, Thomas E. Livingston and Andrew G. Guzzetti (collectively, "Respondents"). Despite this Court's invitation to present "new evidence that they consider relevant to [the Court's] reexamination of the record in this proceeding," December 15, 2017 Order at 2, Respondents point to almost no new evidence whatsoever. Instead, Respondents — including Chiappone, Lex and Livingston, in adopting Mayer's and Rabinovich's arguments—devote much of their letters to objecting to this Court's authority and Rules of Procedure in general, based largely on arguments Respondents advanced—and the Division refuted—in prior submissions.

I. The Commission's ratification and remand order is valid and has effectively remedied Respondents' alleged injury.

1. The Commission's November 30, 2017 Order itself forecloses Respondents' challenge to the Commission's ratification of the appointment of its ALJs. It is undisputed that the Commission, acting in its capacity as head of a department, has the constitutional authority both to appoint ALJs as inferior officers and to ratify any such appointments after the fact. *See* U.S. Const. Art. II, § 2, Cl. 2; 15 U.S.C. § 78d(b)(1); *Free Enterprise Fund v. PCAOB*, 561 U.S. 477, 512 (2010); *Wilkes-Barre Hospital Company, LLC v. National Labor Relations Board*, 857 F.3d 364, 370–71 (D.C. Cir. 2017). The Commission's order exercising that authority and ratifying the appointment of its ALJs is, moreover, binding on those ALJs. The scope of the inquiry before *this* Court is therefore limited to whether—having had her appointment ratified by the Commission—the presiding ALJ should affirm or revise in any respect her prior actions in this proceeding.

2. Respondents also err in attacking the procedures set forth in the Commission's order as inadequate to remedy their alleged harm. In particular, Respondents complain that the ALJs have been afforded too little time to engage in thoughtful, "detached" reconsideration of their prior decisions. They are mistaken. The Commission made the considered decision to ratify the appointment of its

ALJs and, having done so, it remanded this proceeding with instructions to the presiding ALJ to reconsider the entire existing record. The Commission also specified that Respondents would have the opportunity to introduce new evidence and submit new briefing, which they have done.

Those procedures are more than sufficient to allow for a valid ratification decision. Courts have not hesitated to uphold ratification decisions made after a de novo review of the existing administrative record. *See, e.g., Intercollegiate Broadcasting Sys., Inc. v. Copyright Royalty Bd.*, 796 F.3d 111, 118-19 (D.C. Cir. 2015) (de novo review of the record allows for a valid ratification decision, which does not require "a new hearing."); *Advanced Disposal Servs. E., Inc. v. NLRB*, 820 F.3d 592, 602-03 (3d Cir. 2016) (holding ratification valid where the ratifying authority acted with "full knowledge of the decision to be ratified" and made "a detached and considered affirmation of the earlier decision"). And courts have routinely upheld ratification decisions made after far less rigorous procedures than those applied here. *See CFPB v. Gordon*, 819 F.3d 1179, 1186, 1192 (9th Cir. 2016) (upholding ratification after Director issued a "Notice of Ratification" stating, in part: "To avoid any possible uncertainty [about decisions made during recess appointment]. . . I hereby affirm and ratify any and all actions I took during that period."), *cert. denied*, 137 S. Ct. 2291 (2017); *FEC v. Legi-Tech*, 75 F.3d 704, 709 (D.C. Cir. 1996) (finding no basis to invalidate ratification even though respondent "may well be right in arguing that the Commission's 'review'" for purposes of ratification "was nothing more than a 'rubberstamp'").

3. Respondents appear to also argue, in the alternative, that they should not be required to "incur additional time, resources, and expenses" associated with the reconsideration process. Rabinovich & Mayer Ltr. at 4-5. Not only does this claim conflict with their assertion that the process is not sufficiently deliberative, but it too is wrong. Respondents "ha[ve] no inherent right to avoid" or otherwise short-circuit an administrative proceeding; where they allege that certain aspects of the proceeding may be infirm, such challenges may "be vindicated by a reversal" of any Commission final order by a court of appeals. *Jarkesy v. SEC*, 803 F.3d 9, 27 (D.C. Cir. 2015) (quotation marks omitted); *see also FTC v. Standard Oil Co.*, 449 U.S. 232, 244 (1980). As the D.C. Circuit has explained, "the possibility that [respondents'] challenge may be mooted in adjudication warrants the requirement that [they] pursue adjudication, not shortcut it." *Jarkesy*, 803 F.3d at 27 (quotation marks omitted).

II. Respondents' additional constitutional claims lack merit.

1. Respondents' separation-of-powers challenge also misses the mark. The Commission's decision in *Timbervest, LLC*, Advisers Act Release No. 4197, 2015 WL 5472520, at *26-28 (Sept. 17, 2015), forecloses their claim that the manner of removing ALJs is unconstitutional. *See* Rabinovich & Mayer Ltr. at 2-3. Any suggestion that the government's change of position in *Lucia v. SEC*, No. 17-130 (S. Ct.), compels a different result is also wrong. The Commission in *Timbervest* concluded that its ALJs were employees, but it also expressly stated that "*even if* the Commission's ALJs are considered officers," the method of their removal does not offend separation-of-powers principles because of the long-standing and circumscribed adjudicatory functions that ALJs exercise. *Id.* at *27 (emphasis added). Indeed, in *Free Enterprise Fund v. PCAOB*, the Court expressly declined to extend to ALJs its holding that the dual for-cause structure for removing Public Company Accounting Oversight Board members was unconstitutional, explaining that "unlike members of the Board, many administrative law judges of course perform adjudicative rather than enforcement or policymaking functions." 561 U.S. 477, 507 n.10 (2010).

2. Respondents are similarly mistaken in their suggestion that it would violate due process for the ALJ to ratify decisions that were made before the Commission issued its 2016 amendments to its Rules of Practice. Rabinovich & Mayer Ltr. at 3-4. To the extent Respondents' complaint is that the prior rules were somehow constitutionally deficient because they did not incorporate the additional discovery mechanisms afforded by the amendments (and thus did not more closely track the Federal Rules of Evidence and the Federal Rules of Civil Procedure), that argument fails. It is well settled that the Federal Rules do not apply in the Commission's administrative proceedings, *Ralph Calabro*, Securities Act Release No. 9798, 2015 WL 3439152, at *10 & n.66 (May 29, 2015), and any suggestion that this fact renders an administrative proceeding unfair has been consistently rejected by the courts. *See, e.g.*, *Cunanan v. INS*, 856 F.2d 1373, 1374 (2d Cir. 1988). Respondents also have not shown how the application of the Rules in this proceeding has caused, or will cause, them the type of prejudice sufficient to establish a due process violation. *See, e.g.*, *Horning v. SEC*, 570 F.3d 337, 347 (D.C. Cir. 2009) ("In the absence of any suggestion of prejudice, we cannot conclude that Horning was deprived ... of procedural due process.").

Furthermore, even the 2016 Amended Rules would not afford Respondents any benefit. Rabinovich and Mayer argue that 2016 amendments to Rule 320 render inadmissible certain evidence, including a 1999 letter drafted, but not sent, by David Smith. Rabinovich and Mayer Ltr. at 7-8. But Amended Rule 320 provides that the hearing officer "shall exclude all evidence that is irrelevant, immaterial, unduly repetitious, or unreliable," and Rabinovich and Mayer fail to show how the 1999 Smith letter suffers from any of those deficiencies, let alone how its admission prejudiced their case.[1]

To the extent Respondents' complaint is, more broadly, that the administrative process is lacking—and, thus, it violates due process to require them to proceed in an administrative forum—that too fails. As the Commission has observed, "[s]uch broad attacks on the procedures of the administrative process have been repeatedly rejected by the courts." *Harding Advisory LLC*, Securities Act Release No 9561, 2014 WL 988532, at *8 (Mar. 14, 2014). And courts have correctly recognized that to accept such challenges "would do considerable violence to Congress['s] purposes in establishing" specialized administrative agencies and would "work a revolution in administrative (not to mention constitutional) law." *Blinder, Robinson & Co. v. SEC*, 837 F.2d 1099, 1107 (D.C. Cir. 1988). Due process requires only "the opportunity to be heard 'at a meaningful time and in a meaningful manner,'" *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976), and here Respondents have been afforded such opportunity.

3. Respondents err as well in suggesting that it violated due process for the Commission to have authorized this action in an administrative forum, rather than in district court. *See* Rabinovich & Mayer Ltr. at 3. In the Securities Exchange Act of 1934, Congress granted the Commission discretion to address potential violations of the Act by filing an enforcement action in either district court or administrative proceedings. *See, e.g.*, 15 U.S.C. §§ 78u(d), 78u-1, 78u-2, 78u-3. It is well established

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[1] Rabinovich and Mayer rely *U.S. v. McGinn*, 787 F.3d 128 (2d Cir. 2015) in arguing that the Smith letter should not have been admitted, but that decision contemplated whether the district court's decision to allow portions of the letter to be read during cross examination was "manifestly erroneous" in a *jury* trial. *See id.* at 127-28. There is no jury in an administrative proceeding. Moreover, the Second Circuit found that the jury was not substantially influenced by the reading of the 1999 David Smith letter in light of the "overall strength of the government's case and the fact that the letter was cumulative of other properly admitted evidence." *Id.* at 128. Here, too, the 1999 David Smith letter was cumulative of other admitted evidence indicating Smith and McGinn ran a Ponzi scheme.

that where the law affords such a choice, prosecutors may exercise their discretion in selecting the forum in which to bring an action. *E.g.*, *United States v. Haynes*, 985 F.2d 65, 69 (2d Cir. 1993); *see also Hartman v. Moore*, 547 U.S. 250, 263 (2006) (prosecutorial decision-making is accorded a strong "presumption of regularity").

III. The Division's claims were not time-barred under *Kokesh v. SEC* and Section 2462.

Respondents assert, incorrectly, that certain claims in this case are time-barred, and thus ratification as to those claims is invalid. *E.g.*, Chiappone Ltr. at 2. To begin, this argument misunderstands the Commission's order. As discussed above, the Commission ratified the appointments of its ALJs and directed the ALJs to consider whether to affirm or revise in any respect their prior actions in pending administrative proceedings. The Commission did *not* ratify the issuance of its Order Instituting Proceedings (OIP) in this or any other proceeding. Because OIPs are issued by the Commission itself—and the constitutionality of the Commissioners' appointments is undisputed—there is no need to ratify the Commission's OIPs. The OIP here was therefore valid when issued and remains so, notwithstanding any initial defect in the appointments of the Commission's ALJs.

The OIP also is not time-barred under *Kokesh v. SEC*, 137 S.Ct. 1635 (2017), or Section 2462, 28 U.S.C. § 2462. Section 2462 applies only to certain forms of relief (fines, penalties, and forfeitures) and *not* to entire actions. Thus, absent a congressional enactment to the contrary (and here there is none), the Commission was free to initiate this action at any time; its ability to file charges against Respondents was "subject to no time limitation." *See E.I. Dupont De Nemours & Co. v. Davis*, 264 U.S. 456, 462 (1924); *see also, e.g.*, *Holmberg v. Armbrecht*, 327 U.S. 392, 396-97 (1946); *SEC v. Rind*, 991 F.2d 1486, 1491 (9th Cir. 1993) (collecting examples). The 2013 OIP therefore appropriately sought injunctive relief with respect to all fraudulent conduct, including conduct dating back to 2003. *See Birkelbach v. SEC*, 751 F.3d 472, 482 (7th Cir. 2014) (upholding sanctions ruling that considered conduct outside of the five-year limitations period; "even assuming the five-year period applies, there was no error in the SEC considering events outside that period in crafting its sanction"). And the ALJ may assess Respondents' liability for that conduct—and determine whether to ratify or revise her prior actions in this case—without regard to any limitations period.[2]

The five-year limitations period Respondents invoke thus becomes relevant only on the question of monetary relief. The OIP properly sought penalties based on claims that accrued within five years of the OIP, and the Division has acknowledged that, under *Kokesh*, it is appropriate to reduce the disgorgement previously ordered against all liable respondents other than Guzzetti that was based on claims that accrued outside of that five-year period, as set forth in the Division's August 7, 2017 letter to the Commission.[3]

But the limitations period does not, as Respondents suggest, somehow limit remedies not included within Section 2462's terms. And Respondents' assertion that "all of the relief sought by the

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[2] Respondents' argument that a *new* proceeding would be barred under Section 2462 (*e.g.*, Rabinovich & Mayer Ltr. at 3, 4) is thus beside the point, since no new proceeding is necessary.

[3] As also noted in the Division's August 7, 2017 letter, the Division agrees that the collateral bars imposed by Your Honor should be modified. The Division, however, maintains that bars and suspensions from association with a broker-dealer and an investment adviser are warranted based on the evidence set forth in that letter. Aug. 7, 2017 Ltr. from Div. of Enf. to Comm'n at 3-4.

Division is subject to Section 2462" is flatly incorrect. *See* Rabinovich & Mayer Ltr. at 6. Respondents cite *SEC v. Gentile*, No. 16-1619, 2017 WL 6371301 (D.N.J. Dec. 13, 2017), for the proposition that Section 2462 encompasses non-monetary relief, but *Gentile*'s ruling that an obey-the-law injunction and penny-stock bar are "penalties," and therefore subject to the statutory five-year time limit, contradicts the overwhelming weight of authority, including Commission precedent. Section 2462 does not apply to injunctions and bars because those remedies are used to protect the public from future violations, not to punish the defendant. *See, e.g.*, *Timbervest*, 2015 WL 5472520. In support of its contrary conclusion, the district court relied on the Supreme Court's recent decision in *Kokesh* that claims for *disgorgement* are subject to Section 2462. But *Kokesh* did not address whether injunctive relief or bars are subject to Section 2462. *See* 137 S. Ct. at 1640. And the only appellate court to have considered the issue since *Kokesh* was decided has explained that *Kokesh* does not apply to injunctive relief. *SEC v. Collyard*, 861 F.3d 760, 765 (8th Cir. 2017). Regardless, the district court's ruling in *Gentile* provides no basis for this Court to disregard binding Commission precedent.

IV. Respondents' additional arguments do not weigh against ratification.

Rabinovich and Mayer's complaints of prejudice are not well-founded. Their cite to one question by Your Honor in thousands of pages of transcript, *see* Rabinovich and Mayer Ltr. at 8, does not establish that Your Honor was prejudiced against Respondents by the 1999 David Smith Letter, as reflected in the Initial Decision's ruling, among other things, that at least one respondent (William Gamello) was not liable and in establishing a scienter date of February 2008 (and not earlier).[4]

Rabinovich and Mayer also argue that Your Honor should have admitted affidavits from numerous individuals who were subpoenaed to testify, but unable to attend the hearings "because of their work schedules and because of the distance and cost." Jan. 21, 2014 Pre-Hearing Conf. Tr. at 15 (statement by Rabinovich and Mayer's counsel). The ALJ properly denied admission to these affidavits under her proper application of the existing Rules of Practice. Respondents failed to provide a cognizable reason that these declarants could not testify in person. In stark contrast, the Division took telephone testimony only from one investor witness who was recovering from cancer surgery and deposed via videoconference an investor witness who was located outside the United States. *See* Tr. 1473-1530 (Forsyth testimony); Div. Ex. 704, 705 (Fowler deposition). Moreover, Rabinovich and Mayer fail to advance any argument as to how admission of these affidavits would have materially affected the outcome of the proceeding. The affidavits should not be considered as part of this ratification process, and even if considered, should not impact ratification of the initial decision in any way.[5]

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[4] Rabinovich and Mayer claim that Your Honor also admitted other "unreliable evidence." The Division addressed this argument in its brief to the Commission in response to Respondents' petitions for review. *See* Div. of Enf. Br. in Resp. to Respondents' Jt. Br. at 12-15.

[5] Indeed, even the Amended Rules do not contemplate blanket admission of affidavits from declarants who are subpoenaed, but not willing (for whatever reason) to testify. *See* Rule 235(a)(5) (in exercising discretion to admit a prior sworn statement "due regard shall be given to the presumption that witnesses will testify orally in open hearing"). And while Respondents might have opted to depose some number of their affiants under Amended Rule 233(a)(2), the deposition transcripts themselves would not necessarily have been admissible given Rule 235's presumption that "witnesses will testify orally in an open hearing."

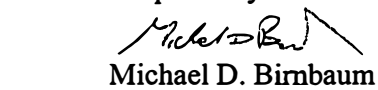
Mayer also argues that the Initial Decision mischaracterizes a settled customer complaint, but Mayer mischaracterizes the Initial Decision and the Division's Proposed Findings of Fact and Conclusions of Law ("FOF"). *See* Rabinovich and Mayer Ltr. at 9. The Initial Decision makes no comment on whether Mayer was personally accused of wrongdoing or whether he contributed to the settlement, I.D. at 48, n.63, and Rabinovich and Mayer cite no prejudice arising specifically from this footnote. The Division similarly made no "acknowledgement" of Mayer's lack of personal responsibility in this dispute; rather, it stated a basic fact: a "customer filed a FINRA complaint against [Mayer] for failure to supervise arising out of his conduct at [a previous firm]." Div. FOF ¶ 522.

Chiappone raises similarly unpersuasive arguments about the Smith letters. Chiappone argues that Livingston Exhibits 31 and 32—letters drafted by David Smith describing certain of his deceptive conduct—"cut[] against your Honor's finding that the brokers should or even could have found out about the misuse of investor Funds." (Chiappone Letter at 2-3.) Chiappone makes a similar argument regarding the amount of time spent by the Division witness Kerri Palen investigating this matter, which he says supports his conclusion that "brokers could not have known of what took place [at McGinn Smith]." *Id.* at 3. But these arguments do not call the Court's attention any new evidence. Rather, they simply repeat what Chiappone argued in his May 12, 2014 Post-hearing Brief with no additional support. *See* Chiappone Br. at 11, n.49 (Smith letters); *id.* at 13 (noting Palen's investigative efforts). This Court properly rejected Chiappone's arguments, *see* Initial Decision at 99-100, and for good reason. The overwhelming evidence demonstrated that Chiappone was liable for fraud. *See* Division Apr. 9, 2014 Posthearing Br. at 24, citing FoF ¶¶ 235, 238-41, 243.

The only "new" evidence Chiappone offers in his January 18, 2018 submission is an affidavit stating he "has not sold, nor [sic] even offered, a single private placement security" since leaving McGinn Smith & Co. Chiappone Letter at 3. Chiappone contends that this evidence supports his argument that he should not be suspended from the securities industry, but this argument fails for the same reasons it did when he first made it. See Chiappone May 12, 2014 Posthearing Br. at 30 (arguing no "likelihood of recurrence" because he had "been conducting his brokerage practice in excess of four hears after he left MS & Co., without ever having sold a private placement.") As the Division noted in its June 12, 2014 Reply brief (at 51), the law supports imposing a suspension (or bar) even for respondents who take a voluntary time out from the securities industry—for fear they might return to the industry—so a suspension is especially warranted for Chiappone, whose January 18, 2018 affidavit acknowledges his continued dealings with "negotiable securities" and "advising clients" regarding their investments. Chiappone Jan. 18, 2018 Aff. at 2, ¶3. Rabinovich and Mayer similarly argue that they pose no threat to the investing public and that a suspension is unwarranted. Rabinovich and Mayer Ltr. at 9.

Finally, Guzzetti argues that Your Honor's finding that he was a supervisor was contradicted by "ample evidence to the contrary." In fact, the finding that Guzzetti was a supervisor was supported by extensive evidence, including Guzzetti's own emails and statements; McGinn Smith's Written Supervisory Procedures; and the testimony of other Respondents. *See* Div. FoF ¶¶ 168-186.

Respectfully submitted,



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cc (by email): All counsel