UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 9789 / May 21, 2015

SECURITIES EXCHANGE ACT OF 1934
Release No. 75021 / May 21, 2015

INVESTMENT ADVISERS ACT OF 1940
Release No. 4094 / May 21, 2015

INVESTMENT COMPANY ACT OF 1940
Release No. 31643 / May 21, 2015

ADMINISTRATIVE PROCEEDING
File No. 3-16554

In the Matter of **GRAY FINANCIAL GROUP, INC., LAURENCE O. GRAY, AND ROBERT C. HUBBARD, IV,** **Respondents.**	**RESPONDENTS' BRIEF IN SUPPORT OF UNOPPOSED MOTION TO STAY ADMINISTRATIVE PROCEEDING**

Respondents Gray Financial Group, Inc., Laurence O. Gray, and Robert C. Hubbard, IV respectfully request that the Administrative Law Judge stay these proceedings pending the resolution of the Motion for a Preliminary Injunction Respondents filed on June 15, 2015 in the United States District Court for the Northern District of Georgia case captioned *Gray Financial Group, Inc., Laurence O. Gray, and Robert C. Hubbard, IV v. U.S. Securities and Exchange Commission*, Civ. Action No. 1:15-cv-0492-LMM. A hearing on the Motion for a Preliminary Injunction has been set for July 13, 2015 before the Hon. Leigh Martin May. In support of their Motion to Stay the Administrative Proceeding, Respondents state as follows:

BACKGROUND AND LEGAL ARGUMENT

A telephonic prehearing conference in this matter has been scheduled for June 30, 2015, pursuant to the parties' request. However, since the scheduling of the prehearing conference, Respondents have filed a Motion for Preliminary Injunction in district court seeking to enjoin this administrative proceeding on constitutional grounds. *See* **Exhibits 1 and 2**, Plaintiffs' Motion for a Preliminary Injunction and Memorandum of Law in Support Thereof, respectively, attached hereto. Respondents believe their Motion for a Preliminary Injunction has considerable merit for the reasons discussed below, and, therefore, good cause exists to stay this administrative proceeding pending the district court's resolution of the pending preliminary injunction motion.

Respondents' district court case has recently been related to another case in which the court granted a preliminary injunction based on "identical constitutional challenges." *See* **Exhibit 3**, *Gray Financial, et al. v. SEC*, Civ. Action No. 1:15-cv-0492-LMM (N.D. Ga. June 10, 2015) ("Totenberg Order"), attached hereto. On June 10, 2015, the Hon. Amy Totenberg issued an Order relating Respondents' district court case to the case captioned *Hill v. SEC*, Civ. Action No. 1:15-cv-1801-LMM. In *Hill*, the plaintiff raised identical claims as Respondents under Article II of the Constitution: 1) that the appointment process for SEC ALJs, including the ALJ presiding in Plaintiffs' Administrative Proceeding, violates the Appointment Clause of Article II because the ALJs were not appointed by the SEC Commissioners; and 2) that the SEC ALJs' two-layer tenure protection violates Article II's vesting of executive power in the President. *See* **Exhibit 4**, Plaintiffs' Second Am. Compl. ¶¶ 1-5, 41-54; 60-70 (June 3, 2015) (Dkt. No. 28), attached hereto, and **Exhibit 5**, *Hill v. SEC*, Civ. Action No. 1:15-cv-1801-LMM, at 34 (N.D. Ga. June 8, 2015) ("*Hill* Order"), attached hereto. Because Judge Totenberg found

Respondents' district court case "involves identical constitutional challenges raised against the Securities and Exchange Commission ("SEC") regarding the appointment of SEC Administrative Law Judges that has been addressed on a motion for preliminary injunction by the Hon. Leigh Martin May" in the *Hill* case, the case was reassigned to Judge May. *See* Totenberg Order.

Notably, Judge May preliminarily enjoined the SEC's administrative proceeding against the *Hill* plaintiff, finding that SEC ALJs are inferior officers and their appointment is likely in violation of Article II. *See Hill* Order at 35-42. Judge May also found that the *Hill* plaintiff satisfied the other criteria for granting a preliminary injunction, a finding that is equally applicable to Respondents. *See id.* at 42-43.

Respondents have filed a Motion for a Preliminary Injunction seeking the same relief that Judge May granted in the related *Hill* case. *See* Exhibit 2 at p. 2. Because the district court has already determined that the *Hill* case and Respondent's district court case "involve identical constitutional challenges" against the SEC, and because Judge May in her well-reasoned decision in the *Hill* matter concluded that the *Hill* plaintiff "will be irreparably harmed if this injunction does not issue because if the SEC is not enjoined, [p]laintiff will be subject to an unconstitutional administrative proceeding, and he would not be able to recover monetary damages for this harm because the SEC has sovereign immunity," Respondents believe their Motion for a Preliminary Injunction has considerable merit. *See Hill* Order at 42. Accordingly, Respondents believe the parties would be best served by waiting until Judge May renders her decision on their preliminary injunction motion before participating in a prehearing conference in the present matter.

The SEC staff does not oppose Respondents' motion. Therefore, in the interests of judicial economy and efficiency, Respondents respectfully request a stay of the administrative

proceeding, including the parties' upcoming prehearing conference, pending resolution of their Motion for a Preliminary Injunction to prevent the unnecessary expenditure of time, money and judicial resources.

CONCLUSION

For good cause shown above and for reasons of judicial economy, efficiency, and fairness to the parties, Respondents respectfully request that the Administrative Law Judge grant Respondents' Motion to Stay the Administrative Proceedings pending the district court's ruling on Plaintiffs' Motion for a Preliminary Injunction.

Respectfully submitted this 18th day of June, 2015.

/s/ Terry R. Weiss
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CERTIFICATE OF SERVICE

The undersigned counsel for Respondents Gray Financial Group, Inc., Laurence O. Gray, and Robert C. Hubbard, IV hereby certifies that he has served a copy of the foregoing **RESPONDENT'S BRIEF IN SUPPORT OF ITS UNOPPOSED MOTION TO STAY ADMINISTRATIVE PROCEEDING** by electronic mail and by United Parcel Service, addressed as follows:

Secretary Brent J. Fields
Securities and Exchange Commission
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Washington, D.C. 20549-1090

Honorable Cameron Elliot
Securities and Exchange Commission
100 F Street N.E.
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Kristin W. Murnahan
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950 East Paces Ferry Road, Suite 900
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This 18th day of June, 2015.

/s/ Terry R. Weiss

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Attorneys for Respondents

EXHIBIT 1

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

GRAY FINANCIAL GROUP, INC., LAURENCE O. GRAY, and ROBERT C. HUBBARD, IV,	)	
Plaintiffs,	)	Civil Action File No. 1:15-cv-0492-LMM
v.	)	
UNITED STATES SECURITIES AND EXCHANGE COMMISSION,	)	
Defendant.	)	

PLAINTIFFS' MOTION FOR A PRELIMINARY INJUNCTION

Plaintiffs Gray Financial Group, Inc., Laurence O. Gray, and Robert C. Hubbard, IV respectfully move this Court for an Order preliminarily enjoining the United States Securities and Exchange Commission from continuing the administrative proceeding brought against them in the matter captioned *In the Matter of Gray Financial Group, Inc. et al.*, Admin. Proceeding File No. 3-16554 (May 21, 2015).

In support of this Motion, Plaintiffs rely on an accompanying Memorandum of Law and the Declaration of Terry R. Weiss, which are being filed concurrently herewith.

WHEREFORE, Plaintiffs request that this Court:

a) enjoin the SEC from conducting the administrative proceeding brought against Plaintiffs, captioned *In the Matter of Gray Financial Group, Inc. et al.*, Admin. Proceeding File No. 3-16554 (May 21, 2015), including the pre-hearing conference scheduled for June 30, 2015 and the final hearing; and

b) grant Plaintiffs such additional relief as this Court deems just.

Dated: June 15, 2015.

Respectfully submitted,

/s/ Terry R. Weiss
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Font Certification

Pursuant to Local Rule 7.1(D), I hereby certify that the foregoing document was prepared using Times New Roman 14 point type as provided in Local Rule 5.1.

/s/ Terry R. Weiss
Terry R. Weiss

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

GRAY FINANCIAL GROUP, INC., LAURENCE O. GRAY and ROBERT C. HUBBARD, IV,	)	Civil Action File No. 1:15-cv-0492-LMM
Plaintiffs,	)	
v.	)	
UNITED STATES SECURITIES AND EXCHANGE COMMISSION,	)	
Defendant.	)	

CERTIFICATE OF SERVICE

This is to certify that I have this day served a copy of the foregoing **MOTION FOR A PRELIMINARY INJUNCTION** via the Court's ECF electronic filing system which will automatically send email notification of such filing to all counsel of record, as follows:

Justin M. Sandberg
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This 15th day of June, 2015.

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EXHIBIT 2

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

GRAY FINANCIAL GROUP, INC., LAURENCE O. GRAY, and ROBERT C. HUBBARD, IV,	)	
Plaintiffs,	)	
v.	)	Civil Action File No. 1:15-cv-0492-LMM
UNITED STATES SECURITIES AND EXCHANGE COMMISSION,	)	
Defendant.	)	

MEMORANDUM OF LAW IN SUPPORT OF PLAINTIFFS' MOTION FOR A PRELIMINARY INJUNCTION

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Plaintiffs Gray Financial Group, Inc., Laurence O. Gray, and Robert C. Hubbard, IV respectfully submit this Memorandum of Law in support of their motion to preliminarily enjoin the United States Securities and Exchange Commission from prosecuting the administrative proceeding brought against them (the "Administrative Proceeding"), captioned *In the Matter of Gray Financial Group, Inc., Laurence O. Gray and Robert C. Hubbard, IV*, Administrative Proceeding File No. 3-16554, including the pre-hearing conference scheduled for June 30, 2015 and the final hearing to be scheduled.

PRELIMINARY STATEMENT

Plaintiffs challenge the authority of the SEC ALJ to preside over the Administrative Proceeding on constitutional grounds, under the Appointments Clause of Article II and Article II's vesting of executive power in the President, as well as on statutory grounds. It is difficult to imagine a more basic defect in a hearing than a presiding judge without lawful authority. For this reason, the United States Supreme Court has held that where a judge serves in violation of the Appointments Clause of the U.S. Constitution, the error is "structural," in part because the role of judge – particularly one acting as finder of both fact and law – is too profoundly essential to be treated otherwise. *See Freytag v. Comm'r of*

Internal Revenue, 501 U.S. 868, 878-80 (1991); *see also Ryder v. United States*, 515 U.S. 177, 182-83 (1995).

Last week, this Court preliminarily enjoined the SEC administrative proceeding in *Hill*, finding that SEC ALJs are inferior officers and their appointment is likely in violation of Article II. *Hill v. SEC*, 1:15-cv-1801-LMM, at 35-42 (N.D. Ga. June 8, 2015) ("*Hill* Order"). Your Honor also found that the *Hill* plaintiff satisfied the other three criteria for granting a preliminary injunction, a finding that is equally applicable to Plaintiffs here. *See id.* at 42-43. Plaintiffs ask for the same relief as the Court granted in *Hill*.

The SEC instituted the Administrative Proceeding against Plaintiffs, to be presided over by SEC ALJ Cameron Elliot, who began working for the SEC in 2011 and has issued 51 straight wins for the SEC and none for a respondent. *See* Declaration of Terry R. Weiss ("Weiss Decl."), ¶¶ 3-5, Ex. 1, Order Instituting Admin. Proceedings (May 21, 2015); Ex. 2, Order Scheduling Hearing and Designating Presiding Judge (May 22, 2015); Ex. 3, Sarah N. Lynch, *SEC Judge Who Took on the 'Big Four' Known for Bold Moves*, Reuters, Feb. 2, 2014. This Administrative Proceeding violates Article II of the U.S. Constitution. In contravention of the Appointments Clause and of statutory requirements, SEC ALJs, including the one presiding over Plaintiffs' administrative process, have not

been appointed by the SEC Commissioners. And, contrary to the Supreme Court's holding in *Free Enterprise,* SEC ALJs enjoy at least two layers of tenure protection. Accordingly, the Administrative Proceeding against Plaintiffs is unconstitutional and should be enjoined.

ARGUMENT

I. THIS COURT HAS SUBJECT MATTER JURISDICTION UNDER 28 U.S.C. §1331 BECAUSE CONGRESS HAS NEITHER EXPLICITLY NOR IMPLICITLY PRECLUDED JUDICIAL REVIEW.

This matter presents the same subject matter jurisdiction question as in *Hill*, where Your Honor correctly analyzed the question and properly found that this Court has original subject matter jurisdiction under 28 U.S.C. § 1331 to resolve the plaintiff's constitutional challenges. *See* 28 U.S.C. § 1331; *Hill* Order at 11-22. Both the *Hill* plaintiff and Plaintiffs in this case bring the very same claims under Article II of the Constitution: 1) that the appointment process for SEC ALJs, including the ALJ presiding in Plaintiffs' Administrative Proceeding, violates the Appointments Clause of Article II because the ALJs were not appointed by the SEC Commissioners; and 2) that the SEC ALJs' two-layer tenure protection violates Article II's vesting of executive power in the President. *See* Second Am. Compl. ¶¶ 1-5, 41-54; 60-70 (June 3, 2015) (Dkt. No. 28); *Hill* Order at 34.

In *Hill*, this Court found that "because Congress created a statutory scheme which expressly included the district court as a permissible forum for the SEC's claims, Congress did not intend to limit § 1331 and prevent [p]laintiff from raising his collateral constitutional claims in the district court." *Hill* Order at 14; *see also id.* at 3 (citing 15 U.S.C. § 78u-2); *cf. Thunder Basin Coal Co. v. Reich*, 510 U.S. 200, 209 (1994) (Mine Act authorized district court forum only for two specific claims). Your Honor also found that even in the absence of Congress's express choice not to restrict district court jurisdiction, "jurisdiction would be proper as Congress's intent can be presumed based on the [three-factor] standard articulated in Thunder Basin, Free Enterprise, and Elgin." *Hill* Order at 14; *see also Touche Ross & Co. v. SEC*, 609 F.2d 570, 575, 577 (2nd Cir. 1979) (where plaintiffs challenge the authority of the agency to act and there is no need for agency expertise, they need not "submit to the very procedures which they are attacking").

For the reasons stated in the *Hill* Order and for the reasons in Plaintiffs' Opposition to Defendant's Motion to Dismiss in this case, this Court should assert subject matter jurisdiction over Plaintiffs' claims. *See Hill* Order at 11-22; Pls.' Opp. to Def.'s MTD at 4-24 (June 3, 2015) (Dkt. No. 24) ("Pls.' MTD Opp.").

II. PLAINTIFFS ARE ENTITLED TO A PRELIMINARY INJUNCTION TO ENJOIN THE SEC'S ADMINISTRATIVE PROCEEDING AGAINST THEM.

To obtain a preliminary injunction, Plaintiffs must demonstrate: "(1) a substantial likelihood of success on the merits; (2) a substantial threat of irreparable injury if the injunction is not granted; (3) the threatened injury to the movant outweighs the damage to the opposing party; and (4) granting the injunction would not be adverse to the public interest." *Hill* Order at 22 (citing *Four Seasons Hotels & Resorts, B.V. v. Consorcio Barr, S.A.*, 320 F.3d 1205, 1210 (11th Cir. 2003)). Plaintiffs meet each of the elements for a preliminary injunction and are thus entitled to preliminary injunctive relief against the SEC on the basis of the same Article II Appointments Clause challenge that the plaintiff in *Hill* successfully raised under identical circumstances. *See Hill* Order at 34-45; Second Am. Compl. ¶¶ 41-47. Moreover, Plaintiffs herein make a similar multi-layer tenure protection argument as in *Hill*, and Plaintiffs respectfully request the opportunity to develop those arguments more thoroughly through discovery, as the Court correctly permitted in *Hill*. *See Hill* Order at 45.

A. Plaintiffs are Likely to Succeed on the Merits that the SEC Administrative Proceeding is Unconstitutional Because the Appointment of SEC ALJs Violates Article II's Appointments Clause and Statutory Law, and SEC ALJs' Dual For-Cause Removal Scheme Violates Article II.

The *Hill* plaintiff and these Plaintiffs present identical Article II challenges based on SEC ALJs being inferior officers and not mere employees. *See Hill* Order at 34-35. Because SEC ALJs are inferior officers under the Constitution, the SEC Commissioners themselves, as "Head of Department" under the Appointments Clause, must appoint the ALJs, and the ALJs cannot be insulated from presidential control by two levels of tenure protection.

1. This Court Correctly Held in *Hill* that SEC ALJs are Inferior Officers.

In *Hill*, Your Honor thoroughly analyzed the question of whether SEC ALJs are inferior officers, including the arguments of the SEC, and found that "*Freytag* mandates a finding that the SEC ALJs exercise 'significant authority' and are thus inferior officers." *Hill* Order at 41; *see Freytag*, 501 U.S. 868 (considering the types of tasks performed by STJs, which the Supreme Court found were "more than ministerial tasks," and evidence of the significant discretion STJs exercised, thus making them inferior officers and not lesser functionaries). For the reasons stated in the *Hill* Order and for the reasons in Plaintiffs' Opposition to Defendant's

Motion to Dismiss in this case, this Court should find that SEC ALJs are inferior officers. *See Hill* Order at 35-41; Pls.' Opp. to MTD at 22-31.

2. This Court Found, Under the Same Circumstances, that there is a Substantial Likelihood of Success on the Appointments Clause Violation.

In *Hill*, Your Honor found that the plaintiff "has established a likelihood of success on the merits on his Appointments Clause claim." *Hill* Order at 41. Plaintiffs make the same Appointments Clause challenge herein.

The Appointments Clause of the Constitution provides that as to "inferior officers," "Congress may by Law vest the Appointment of such inferior Officers ... in the President alone, in the Court of Law, or in the Heads of Department." U.S. Const. art. II, § 2, cl. 2. Embedded in these express limitations is a structural goal of guarding against "the diffusion of the appointment power." *Freytag*, 501 U.S. at 878. In so limiting the power of appointment, the Constitution ensures that those who wield it remain "accountable to political force and the will of the people." *Id.* at 884.

The Supreme Court, in *Free Enterprise Fund v. Public Co. Accounting Oversight Bd.* ("*Free Enterprise*") held that the SEC Commissioners jointly hold the power to appoint inferior officers under the Appointments Clause. 561 U.S. 477, 512-13 (2010). The Supreme Court specifically held that the Commission is a "Department" for purposes of the Appointments Clause and that the

Commissioners jointly constitute the "Head" of that "Department." *See id.* at 511-13.

The SEC has conceded that its Commissioners did not appoint the ALJ presiding over Plaintiffs' Administrative Proceeding. *See* Notice of Filing Suppl. Evidence, at 1-2 & Exhibit 1 (June 9, 2015) (Dkt. No. 35) ("ALJ Elliot was not hired through a process involving the approval of the individual members of the Commission"). The same is true of the other SEC ALJs. *See Hill* Order at 41 (SEC concedes that ALJ Grimes was not appointed by SEC Commissioner); Second Am. Compl. ¶ 51 (SEC acknowledges Commissioners did not appoint ALJ Foelk). There is no reason to believe the remaining two SEC ALJs were appointed in a different manner.

In fact, the U.S. Department of Justice, as counsel for the SEC, recently conceded that if SEC ALJs are "inferior officers," administrative proceedings like the one involving Plaintiffs would probably violate Article II:

> THE COURT: Let me just back up for a minute and ask you a question. If I find that the ALJs are inferior officers, do you necessarily lose?
>
> MS. LIN: We acknowledge that, your Honor, if this Court were to find ALJ Foelk to be an inferior officer, that that would make it more likely that the plaintiffs can succeed on the merits for the Article II challenge, at least with respect to the appointments clause challenge.

Second Am. Compl. ¶ 51 & Exhibit A thereto, Hearing Transcript, *Tilton v. S.E.C.*, 15 CV 2472(RA) (S.D.N.Y.), at 29:10-17 (May 11, 2015).

By abdicating its constitutionally allocated responsibility, the Commission has impermissibly delegated the appointment power to others. This has created a defect that goes to the very core of the administrative proceeding. That is, the SEC ALJ presiding over Plaintiffs' Administrative Proceeding lacks the lawful authority to do so. *See Buckley v. Valeo*, 424 U.S. 1, 126 (1976) (stating that any "'Officer of the United States' … must ... be appointed in the manner prescribed by" the Appointments Clause); *Freytag*, 501 U.S. at 879 ("The alleged defect in the appointment of the Special Trial Judge goes to the validity of the Tax Court proceeding that is the basis for this litigation."); *see also Ryder*, 515 U.S. at 188 (holding that Appointments Clause violation involving two of three judges sitting on an intermediate military appellate court panel entitled petitioner to a hearing before a properly appointed panel of that court); *United States v. Lane*, 64 M.J. 1, 7 (2006) (concluding that the unconstitutional assignment of a Member of Congress to serve as a judge on a military court of appeals rendered the petitioner's proceeding before that court invalid and void). What is more, by not appointing the SEC ALJs, the Commission remains unaccountable for the ALJs' actions.

These are structural infirmities of the first order that render Plaintiffs' Administrative Proceeding unconstitutional.

Because the SEC has admitted that it did not appoint the presiding SEC ALJ, this Court's previous findings that SEC ALJs are inferior officers and that the manner of ALJ appointment is "likely unconstitutional in violation of the Appointments Clause" apply equally to this case. *See Hill* Order at 42.

3. SEC ALJs were Appointed in Violation of Statutory Requirements.

Although not raised as an argument in *Hill,* the manner of appointment of the SEC ALJs is also a violation of statutory law. Unlike the constitutional Appointments Clause claim, the statutory challenge does not depend on a finding that ALJs are constitutional officers. Congress has mandated that the "Commission," defined in 15 U.S.C. § 78d(a) as the SEC Commissioners, "shall appoint and compensate officers, attorneys, economists, examiners, and other employees." 15 U.S.C. § 78d(b)(l). Further, by statute the SEC "shall appoint as many administrative law judges as are necessary." *See* 5 U.S.C. § 3105. Because the SEC has admitted that the Commissioners did not appoint the SEC ALJs, Plaintiffs have established a substantial likelihood of success on the merits of their statutory claim.

4. The Administrative Proceeding is Unconstitutional Under Article II Because It is Presided Over by an Executive Inferior Officer Shielded from Removal by at Least Two Layers of Tenure Protection.

In *Free Enterprise*, the Supreme Court held that if, like here, an inferior officer can only be removed from office upon a showing of good cause, then the decision to remove that officer cannot be made by another official who is also shielded from removal by good-cause tenure protection. 561 U.S. at 484. This arrangement violates Article II because it impairs the President's ability to "take Care that the Laws be faithfully executed." U.S. Const. art. II § 1, cl. 1; *id.* § 3. *Free Enterprise* is dispositive on this issue.

SEC ALJs, including the presiding ALJ, are insulated from presidential removal by at least two layers of good-cause tenure protection. First, an SEC ALJ may be removed by the SEC only upon a finding of good cause by the Merit Systems Protection Board ("MSPB"). 5 U.S.C. § 7521(a)-(b). Second, both SEC Commissioners and members of the MSPB can be removed by the President only for "inefficiency, neglect of duty, or malfeasance in office." *Free Enterprise*, 561 U.S. at 487; 5 U.S.C. § 1202(d). Thus, an SEC ALJ is protected from removal by at least two layers of good-cause tenure protection, possibly three.

In *Hill*, Your Honor did not decide whether there was a likelihood of success on the merits that the SEC ALJs' dual for-cause removal provisions

violate Article II. *Hill* Order at 42 n.12. Although the Court raised doubts about this challenge, Your Honor likewise permitted the plaintiff in *Hill* the opportunity to develop the factual record supporting this argument through discovery. *Id.* at 45. Plaintiffs believe that upon a factual examination of the scope of SEC ALJs' roles and uses within the Commission, the Court will find that the ALJs' multi-layer tenure protection interferes with the President's constitutional obligation to ensure the faithful execution of the laws.

Indeed, even if SEC ALJs perform primarily adjudicatory functions, the constitutional infirmity is not eliminated. The Supreme Court in *Morrison v. Olson* rejected the theory that the President's removal authority operates less stringently for quasi-judicial and quasi-legislative officers, than for officers with "purely executive" functions: "[O]ur present considered view is that the determination of whether the Constitution allows Congress to impose a 'good cause'-type restriction on the President's power to remove an official cannot be made to turn on whether or not that official is classified as 'purely executive.'" 487 U.S. 654, 689 (1988). Similarly, in *Freytag*, the concurring opinion noted that ALJs, "whose principal statutory function is the conduct of adjudication . . . are all *executive* officers" and that "'[a]djudication,' in other words, is no more an 'inherently' judicial function than the promulgation of rules governing primary

conduct is an 'inherently' legislative one." 501 U.S. at 910 (Scalia, J., concurring in part and concurring in judgment, joined by O'Connor, Kennedy & Souter, JJ) (emphasis in original); *see also Kuretski v. Comm'r,* 755 F.3d 929, 936 (D.C. Cir. 2014) (even though Tax Court Judges exercise quasi-judicial power, they are officers of the Executive Branch and their removal at will by the President creates no separation of powers problem), *cert. denied*, 2015 WL 2340860 (May 18, 2015); *Intercollegiate Broad. Sys. Inc. v. Copyright Royalty Bd.,* 684 F.3d 1332, 1340-42 (D.C. Cir. 2012) (tenure protections of Copyright Royalty Judges found unconstitutional). It follows that Congress may not create a class of executive adjudicators for the SEC operating outside the constraints of executive authority over other Commission officers. The board members in *Free Enterprise* had quasi-judicial authority over certain matters, but this fact did not justify their exemption from presidential oversight. *See Free Enterprise*, 561 U.S. at 485.

Further, the Supreme Court has held that the SEC can make policy – an undoubtedly core executive function – through adjudication. *SEC v. Chenery Corp.*, 332 U.S. 194, 201-04 (1947). Addressing an SEC order, the Supreme Court ruled: "There is thus a very definite place for the case-by-case evolution of statutory standards. And the choice made between proceeding by general rule or

by individual, ad hoc litigation is one that lies primarily in the informed discretion of the administrative agency." *Id.* at 203; *see also NLRB v. Bell Aerospace Co.*, 416 U.S. 267, 293 (1974) (choice between announcing policy through rulemaking or adjudication is in agency's discretion).

Thus, it is not surprising that the SEC does develop policy through administrative adjudications. The SEC recently acknowledged the critical policy-making and enforcement roles that SEC ALJs play in the Division of Enforcement Approach to Forum Selection in Contested Actions (the "SEC Memo"). Weiss Decl. ¶ 6, Ex. 4, Division of Enforcement Approach to Forum Selection in Contested Actions. In the SEC Memo, the SEC emphasized that SEC ALJs "develop extensive knowledge and expertise concerning the federal securities laws and complex or technical securities industry practices or products." *Id.* at 3. The SEC also acknowledged that if a matter "is likely to raise unsettled and complex legal issues under the federal securities laws, or interpretation of the Commission's rules," the agency is more likely to proceed through the administrative process, before an SEC ALJ, in order to "facilitate development of the law." *Id.* Thus, the SEC has demonstrated that the nature of its ALJs' authority is solidly executive.

Moreover, the Department of Justice, whose counsel represent the SEC in this case, concluded that Department of Education ALJs are inferior officers

because of their executive policy-making role. *See Sec. of Ed. Review of Admin. Law Judge Decisions*, 15 U.S. Op. Off. Legal Counsel 8, 14, 1991 WL 499882 (Jan. 31, 1991). "By deciding a series of cases, the ALJ presumably would develop interpretations of the statute and regulations and fill statutory and regulatory interstices comprehensively with his own policy judgments." *Id.* This analysis applies equally to SEC ALJs, who also "decid[e] a series of cases," and likewise have tremendous opportunity to formulate executive policy.

In sum, as an inferior officer in the Executive Branch, an SEC ALJ wields executive power when presiding over enforcement actions brought by the Commission. Exercising this power, an ALJ's protection from removal by dual layers of tenure impairs the President's ability to ensure that the laws are faithfully executed. *Free Enterprise*, 561 U.S. at 484, 498. While a dual-layer removal regime protecting ALJs was not before the Supreme Court in *Free Enterprise*, the Court's holding necessarily reaches such a scheme. *See id.* at 507 n. 10; 542-43 (Breyer, J., dissenting); Kent Barnett, *Resolving the ALJ Quandary*, 66 Vand. L. Rev. 797, 800 (2013). This dual-layer removal scheme is thus unconstitutional.

B. The Court Already Found that There is Irreparable Harm if the SEC's Administrative Proceeding Is Not Enjoined.

In *Hill*, this Court determined that the plaintiff "will be irreparably harmed if this injunction does not issue because if the SEC is not enjoined, [p]laintiff will be

subject to an unconstitutional administrative proceeding, and he would not be able to recover monetary damages for this harm because the SEC has sovereign immunity." *Hill* Order at 42 (citing *Odebrecht Const., Inc. v. Sec'y, Fla. Dep't of Transp.*, 715 F.3d 1268, 1289 (11th Cir. 2013) ("In the context of preliminary injunctions, numerous courts have held that the inability to recover monetary damages because of sovereign immunity renders the harm suffered irreparable"). Your Honor also found that in the absence of a preliminary injunction, the requested relief of enjoining the SEC administrative proceeding would be "moot as the Court of Appeals would not be able to enjoin a proceeding which has already occurred." *Id.* at 42-43. The Court's finding of irreparable harm applies equally to Plaintiffs here.

Plaintiffs are in the same position as the *Hill* plaintiff. Plaintiffs must file an Answer to the SEC's Order Instituting Proceedings by June 17, 2015, and a pre-hearing conference is scheduled for June 30, 2015. Weiss Decl. ¶¶ 7-8, Ex. 5, Order on Consent Motion (June 9, 2015); Ex. 6, Order Postponing Hearing and Scheduling Pre-Hearing Conference (June 5, 2015). The final hearing must take place no later than September 21, 2015, but may occur earlier. *See* 17 C.F.R. § 201.360(a)(2). Absent injunctive relief, Plaintiffs will be subjected to the very

proceeding that they claim is unconstitutional. Plaintiffs have thus shown that they will suffer irreparable injury if the injunction does not issue.

C. The Court Also Found that the Remaining Preliminary Injunction Factors Weigh in Favor of Granting the Motion.

Your Honor's findings in *Hill* "that the public interest and the balance of equities" are in favor of granting a preliminary injunction govern Plaintiffs' Motion as well. *See Hill* Order at 43. For the reasons stated in the *Hill* Order, Plaintiffs have met these preliminary injunction factors, and the Court should halt the SEC's Administrative Proceeding.

CONCLUSION

For all of the foregoing reasons, Plaintiffs respectfully request that this Court issue a preliminary injunction enjoining the SEC from continuing the Administrative Proceeding against them.

Dated: June 15, 2015.

Respectfully submitted,

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Font Certification

Pursuant to Local Rule 7.1(D), I hereby certify that the foregoing document was prepared using Times New Roman 14 point type as provided in Local Rule 5.1.

/s/ Terry R. Weiss
Terry R. Weiss

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

GRAY FINANCIAL GROUP, INC., LAURENCE O. GRAY and ROBERT C. HUBBARD, IV,	)	
Plaintiffs,	)	
v.	)	Civil Action File No. 1:15-cv-0492-LMM
UNITED STATES SECURITIES AND EXCHANGE COMMISSION,	)	
Defendant.	)	

CERTIFICATE OF SERVICE

This is to certify that I have this day served a copy of the foregoing **MEMORANDUM OF LAW IN SUPPORT OF PLAINTIFFS' MOTION FOR A PRELIMINARY INJUNCTION** via the Court's ECF electronic filing system which will automatically send email notification of such filing to all counsel of record, as follows:

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This 15th day of June, 2015.

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EXHIBIT 3

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

GRAY FINANCIAL GROUP, INC., LAURENCE O. GRAY, and ROBERT C. HUBBARD, IV,	:	
Plaintiffs,	:	
v.	:	
UNITED STATES SECURITIES AND EXCHANGE COMMISSION,	:	CIVIL ACTION NO. 1:15-cv-0492-AT
Defendant.	:	

ORDER

This matter involves identical constitutional challenges raised against the Securities and Exchange Commission ("SEC") regarding the appointment of SEC Administrative Law Judges that has been addressed on a motion for preliminary injunction by the Hon. Leigh Martin May in a case captioned *Hill v. SEC*, 1:15-cv-1801-LMM. The Court therefore deems the case related. As a matter of judicial economy, this Court **ORDERS** that the instant civil action be **TRANSFERRED** to the Hon. Leigh Martin May. The Clerk is further **DIRECTED** to assign the undersigned the next case assignment in the rotation for Judge May.

IT IS SO ORDERED this 10th day of June, 2015.

Amy Totenberg
United States District Judge

EXHIBIT 4

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

GRAY FINANCIAL GROUP, INC., LAURENCE O. GRAY, and ROBERT C. HUBBARD, IV,	)	
Plaintiffs,	)	Civil Action File No. 1:15-cv-0492-AT
v.	)	**SECOND AMENDED COMPLAINT FOR DECLARATORY AND INJUNCTIVE RELIEF AND DEMAND FOR JURY TRIAL**
UNITED STATES SECURITIES AND EXCHANGE COMMISSION,	)	
Defendant.	)	

Pursuant to the Federal Rule of Civil Procedure 15(a) and with the express written consent of counsel for the Defendant, Plaintiffs Gray Financial Group, Inc. ("Gray Financial"), Laurence O. Gray ("Mr. Gray"), and Robert C. Hubbard, IV ("Mr. Hubbard") (collectively, "Plaintiffs") submit their Second Amended Complaint for Declaratory and Injunctive Relief (the "Second Amended Complaint") against the United States Securities and Exchange Commission ("SEC" or the "Commission") and allege as follows:

Preliminary Statement

1. SEC administrative proceedings violate Article II of the U.S. Constitution, which states that the "executive Power shall be vested in a President

of the United States of America" and that "the Congress may by Law vest the Appointment of such inferior Officers, as they think proper, ... in the Heads of Departments." U.S. Const., Art. II, §§ 1-2.

2. An SEC Administrative Law Judge ("SEC ALJ") presides over an administrative proceeding. Federal statutes and SEC rules and regulations make clear that SEC ALJs are executive branch "officers" within the meaning of Article II.

3. The United States Supreme Court has held that the SEC is a "Department" of the United States, and that the SEC Commissioners (the "Commissioners") collectively function as the "Head" of the SEC with authority to appoint such "officers" as Congress authorizes. *Free Enterprise Fund v. Pub. Co. Accounting Oversight Bd.,* 561 U.S. 477 (2010) ("*Free Enterprise*").

4. The Supreme Court has also held that such officers – charged with executing the laws, a power vested by the United States Constitution solely in the President – may not be separated from Presidential supervision and removal by more than one layer of tenure protection. *Id.* In particular, if an officer can only be removed from office for good cause, then the decision to remove that officer cannot be vested in another official who, too, enjoys good-cause tenure. *Id.*

5. Yet, in recent federal court proceedings, the SEC has admitted that SEC ALJs have not been appointed by the SEC Commissioners as required by the U.S. Constitution and statutory law. Additionally, ALJs enjoy at least two – and likely more – layers of tenure protection. The SEC administrative proceedings therefore violate Article II and relevant statutes, and are unconstitutional.

6. On May 21, 2015, the SEC issued an Order Instituting Proceedings ("OIP") commencing an administrative proceeding against Plaintiffs. The OIP alleges violations of the federal securities laws and seeks disgorgement, civil penalties, and a cease-and-desist order. The OIP ordered a public hearing to be held within 60 days before an SEC ALJ. The OIP further ordered that the ALJ issue the initial decision within 300 days of the OIP.

7. Declaratory and injunctive relief is necessary to prevent Gray Financial, Mr. Gray and Mr. Hubbard from being compelled to submit to an unconstitutional proceeding and from suffering irreparable reputational and financial harm – all without meaningful judicial review.

Jurisdiction, Venue, and Parties

8. This Court has subject matter jurisdiction pursuant to 28 U.S.C. §§ 1331, 1337, 1346, 1651, 2201 and 5 U.S.C. §§ 702 and 706. Venue is proper in this district pursuant to 28 U.S.C. § 1391(b) and (e).

9. It is appropriate and necessary for this Court to exercise jurisdiction over Plaintiffs' claims because (a) without judicial review at this stage, meaningful judicial review will be foreclosed; (b) Plaintiffs' claims are wholly collateral to the review provisions of the federal securities laws; and (c) Plaintiffs' claims are not within the particular expertise of the SEC.

10. Gray Financial is a corporation organized and existing under the laws of the State of Georgia, having its principal place of business in Fulton County, Atlanta, Georgia, and does business under the names of Gray & Co., Gray & Company and GrayCo Global Advisors.

11. Laurence O. Gray is a natural person, citizen of the State of Georgia, and resident of Fulton County, Georgia, and resides in the Northern District of Georgia. Mr. Gray is the founder and principal of Gray Financial and its related entities.

12. Robert C. Hubbard is a natural person, citizen of the State of Georgia and resident of Cobb County, Georgia, and resides in the Northern District of Georgia. Mr. Hubbard is the Co-Chief Executive Officer of Gray Financial.

13. The SEC is an agency of the United States government, headquartered in Washington, D.C. The SEC operates 11 regional offices, including one located at 950 East Paces Ferry Road, Atlanta, Georgia 30326.

Background

14. Gray Financial is an investment advisory firm properly registered with the SEC and with the States of Georgia and Michigan. Gray Financial has remained a small, privately held registered investment advisor and has focused its business almost exclusively on consulting – primarily to public and private pension plans, many of which are Georgia plans. Gray is minority owned and appears to be one of the last – if not the last – remaining minority owned investment consulting firm serving public pension plans in any metropolitan city in the United States.

15. As an investment consultant, Gray Financial provides consulting services on a non-discretionary basis to both public and private entities with plan assets that at times have totaled nearly $10 billion. In that capacity, the services provided by Gray Financial may include assisting pension boards with the preparation, monitoring and annual review of investment policy guidelines, conducting searches, due diligence and presentations by investment money managers, and monitoring investment performance and providing a performance analysis.

The New Georgia Pension Law (O.C.G.A. 47-20-87)

16. On April 16, 2012, the Governor of Georgia signed into law the Public Retirement Systems Investment Authority Law (the "New Georgia Pension

Law"), which for the first time allowed Georgia public pension plans – managing over $82 billion in cash and investment holdings[1] – the opportunity to diversify the risk of their multi-million dollar investment portfolios with "alternative investments."

17. Indeed, allocating a portion of portfolio funds to alternative investments – such as private equity, hedge funds and funds of funds – is recognized as an appropriate and important investment technique to reduce volatility and increase potential returns. Prior to passage of the New Georgia Pension Law, other states recognized the benefits of making alternative investments and had statutes authorizing their public pensions to make alternative investments.

18. Although other state public pension laws may share the same underlying objectives as the New Georgia Pension Law to allow alternative investing, that is where the similarity ends. Those other states' pension laws are straightforward and are relatively clear in identifying the specific conduct that is authorized and that which is prohibited. In contrast, the New Georgia Pension Law, codified as O.C.G.A. 47-20-87, is unclear, vague and ambiguous. It uses

[1] U.S. Census Bureau, 2013 Annual Survey of Public Pensions: State- and Locally-Administered Defined Benefit Pension Systems - All Data by State and Level of Government.

unusual and, indeed, unique, language and undefined technical terms. Unlike other states' pension laws, it does not define clearly who must act, what must be done and when and how it must be done. Indeed, different but equally intelligent readers of the New Georgia Pension Law can and do arrive at reasonable but different interpretations of what specific conduct is and is not permitted by the statute.

19. There has not been any publicly available formal statutory interpretation of the unique language of the New Georgia Pension Law, either through reported legislative history or reported appellate case law. As a result, every reader of the New Georgia Pension Law – including the staff members of Gray Financial on one hand and the SEC on the other – is left to his or her own devices to discern the intent of the statute because there is no guidance to be had.

Assisted by Competent New York Based Legal Counsel, Gray Financial Successfully Develops Two Alternative Investment Fund of Funds

20. For some time, Gray Financial had consulted with a number of its clients outside of Georgia about adding alternative investments as part of a diverse investment portfolio. To attempt to meet client demand for alternative investments, Gray Financial, through an affiliate, conceptualized an alternative investment fund-of-funds to be named GrayCo Alternative Partners I, LP ("Fund

I"), which Gray Financial could offer to pension plans seeking access to alternative investments.

21. Neither Mr. Gray nor Mr. Hubbard has any formal legal training and typically would rely on legal professionals when needed. Accordingly, and before proceeding with the concept of Fund I, Gray Financial, through its affiliate, sought out and retained a well-regarded and experienced New York based law firm to handle all legal issues associated with the project and to assist with and advise on important business decisions. The project was successfully developed, clients outside of Georgia invested in Fund I, and those clients that remain have indicated that they have been pleased with their investment decision.

22. After the New Georgia Pension Law passed, Gray Financial considered offering to its Georgia pension plans a fund-of-funds alternative investment. Because its experience with Fund I had been successful, Gray Financial and its affiliate turned to its New York based legal and business advisory team to create what would become known as GrayCo Alternative Partners II, LP ("Fund II"). Fund II would be largely based on the same structure that its New York-based counsel created for Fund I. Accordingly, Gray Financial, through its affiliate, retained the same New York based legal counsel for Fund II to evaluate all related legal issues impacting the project, including compliance with the New

Georgia Pension Law. As with Fund I, the project was successfully developed, Georgia-based clients invested in Fund II and did so with no reported client losses.

The SEC Begins an Onerous Investigation into the Marketing of Fund II to Georgia Pension Plans

23. Although there had been no indication of any client losses in Fund I or Fund II, the SEC – a federal agency which is responsible for enforcing the federal securities laws – advised Gray Financial formally in August 2013 that it was conducting a confidential and non-public investigation into Gray Financial, Mr. Gray and Mr. Hubbard, and whether Fund II complied with the New Georgia Pension Law. This investigation was against the backdrop that there had never previously been any allegations by any securities industry regulator – let alone proof – of any prior wrongdoing by Gray Financial, Mr. Gray or Mr. Hubbard, or that any of them had violated any securities laws. Nevertheless, in providing notice that its investigation had begun, the SEC stressed that severe penalties could be imposed if it was not afforded complete cooperation from those involved.

24. Although the SEC told Gray Financial that its investigation was "private," somehow the fact the SEC was investigating and the nature of that investigation were released to the local and national press, and in a significant way. It appeared that guilt was presumed, although the SEC had not issued formal charges, let alone proven in an unbiased forum that Gray Financial, Mr. Gray or

Mr. Hubbard had engaged in any wrongdoing. The adverse impact to an investment advisor when a "private" investigation becomes a public one is predictable; but it is all the more substantial when the investment advisor is a small and locally owned one. The consequences of this became a harsh reality for Gray Financial and all of the employees of the firm. Once the investigation became public, Gray Financial had numerous consulting clients terminate their business relationships, RFPs for new business opportunities vanished, and revenues declined.

25. On August 1, 2014, the SEC issued Wells notices indicating that it had reached a preliminary conclusion that Gray Financial, Mr. Gray and Mr. Hubbard had violated certain specific federal securities laws. The SEC's primary theory of liability was – and indeed still is – that Gray Financial, Mr. Gray and Mr. Hubbard had violated the Investment Advisers Act, sections 206(1), 206(2), and 206(4), and Rules 206(4)-8(a)(1) and (2) thereunder, by offering for sale to Georgia-based clients, an alternative investment fund that the SEC alleges is not in compliance with its interpretation of the New Georgia Pension Law. The SEC has even gone so far as to argue that the violations must have been intentional – not merely negligent – in order to seek more aggressive sanctions that the SEC can muster. This practice was not new or unique in this case.

26. On August 29, 2014, Gray Financial, Mr. Gray and Mr. Hubbard each provided written submissions in response to the SEC's Wells notices. In their responses, each demonstrated that a reasonable interpretation of the New Georgia Pension Law permits Georgia public pension plans to invest in Fund II. Moreover, to the extent there was a misinterpretation of the New Georgia Pension Law, it was as a result of the many ambiguities and defects in an unclear law and not the result of a willful or reckless disregard of the statute's requirements. To the contrary, Gray Financial, Mr. Gray and Mr. Hubbard relied on highly compensated and, what it reasonably believed to be, skilled counsel. They therefore had every reason to believe that the Fund II offering prepared by counsel complied with the New Georgia Pension Law. Finally, faced with a matter of first impression on the interpretation of a unique state statute that is at best unclear, the SEC should have reserved judgment for the Georgia legal system that is in a better position to interpret a Georgia law.

The SEC's Chosen Forum and Sanction

27. The securities laws provide the SEC with the discretion – guided by no statute, regulation, or established practice – to bring an enforcement action either in federal district court or in internal SEC administrative proceedings.

28. The SEC staff had indicated to counsel for Gray Financial, Mr. Gray and Mr. Hubbard that the only action they can take to avoid charges being brought by the SEC is for them to agree to draconian settlement terms that would inflict a significant risk of financial, professional, and reputational harm to them, and, derivatively, the investors in Funds I and II, which includes Georgia public pensions.

29. On February 19, 2015, Plaintiffs filed the instant declaratory and injunctive action challenging the SEC's administrative proceedings as being in violation of Article II of the United States Constitution. Afterward, and following through on its threat, the SEC on May 21, 2015 initiated its enforcement action against Plaintiffs in an SEC administrative proceeding before an SEC ALJ, rather than in federal district court, SEC Case No. 3-16554.

The Administrative Proceeding

30. An administrative proceeding is an internal SEC hearing, governed by the SEC's Rules of Practice ("Rules of Practice," or "RoP") and litigated by SEC trial attorneys.

31. Administrative proceedings differ in several critical ways from federal court proceedings. Those differences make administrative proceedings more advantageous to the SEC, which include:

a. In administrative proceedings, an SEC ALJ serves as finder of both fact and of law.

b. Administrative proceedings do not afford juries to litigants, unlike federal court.

c. The Federal Rules of Civil Procedure do not apply in an administrative proceeding; they do apply in federal court.

d. The Federal Rules of Evidence, together with their associated protections, do not apply in an administrative proceeding; they do apply in federal court. Any evidence that "can conceivably throw any light upon the controversy," including unreliable hearsay testimony, "normally" will be admitted in an administrative proceeding. *In the Matter of Jay Alan Ochanpaugh*, Securities Exchange Act Rel. No. 54363, 2006 SEC LEXIS 1926, *23 n.29 (Aug. 25, 2006).

e. Defendants' ability to conduct discovery is limited in administrative proceedings. For example, pre-trial depositions are generally not allowed in administrative proceedings; they are allowed in federal court. RoP 233, 234.

f. The SEC Rules of Practice do not provide respondents the opportunity to challenge the SEC's legal theories before trial through dispositive motions; dispositive motions are available in federal court.

g. The SEC Rules of Practice do not allow respondents to assert counterclaims against the SEC. Federal court defendants may assert counterclaims against their adversaries.

h. The SEC Rules of Practice require the hearing to take place, at most, approximately four months from the issuance of the SEC's Order Instituting Proceedings ("OIP"). In its discretion, the SEC can require the hearing to occur as early as one month after the OIP is issued. While the SEC can allow itself years of investigation and research to prepare an administrative case, the SEC does not need to start making available the limited discovery afforded to administrative proceeding respondents until seven days after the OIP is issued.

i. Administrative proceedings are private, closed to the public and the news media, unlike federal court proceedings. Nevertheless, the SEC uses the press affirmatively by issuing

press releases to broadcast the fact it is bringing administrative cases.

32. Not surprisingly, the SEC has succeeded much more often in administrative proceedings, where it enjoys the procedural advantages described above, than in federal district courts, according to several observers. In fact, one recent study found that the SEC has won the last 219 decisions before its ALJs – a "winning streak, which began in October 2013 and continues today" – at a time when it has lost several high-profile decisions in the federal courts. Jenna Greene, *The SEC's on a Long Winning Streak*, National Law Journal, Jan. 22, 2015; Gretchen Morgenson, *At the S.E.C., a Question of Home-Court Edge*, N.Y. TIMES, Oct. 5, 2013; and others. The SEC's apparently unstoppable series of "wins" in administrative proceedings brings to mind long-ago discredited systems like monarchical Star Chambers and hard-line regimes' show trials. In contrast, when forced to bring cases before unbiased United States District Court Judges, on the level playing field of federal court where defendants are protected by juries, broad discovery rights, robust rules of evidence, and other procedural safeguards, the SEC's win-loss record is far less pristine. In fact, in some cases, the federal courts have been openly critical of the SEC in the cases it selects to bring and how it brings them. One U.S. District Judge, noting that the SEC won 61% of its federal

court trials versus 100% of its administrative proceedings, said that the courts have "functioned very effectively for decades," adding that he saw "no good reason to displace that constitutional alternative with administrative fiat." Nate Raymond, *U.S. Judge Criticizes SEC Use of In-house Court for Fraud Cases*, Reuters, Nov. 5, 2014. Indeed, at least one SEC Commissioner, a former SEC ALJ, and a U.S. District Court Judge are reported to have raised fairness concerns about the proliferation of SEC administrative enforcement actions. *See, e.g.*, Jean Eaglesham, *SEC Wins With In-House Judges*, The Wall Street Journal, May 6, 2015; Commissioner Michael S. Piwowar, *A Fair, Orderly and Efficient SEC*, Remarks at "SEC Speaks" Conference, Feb. 20, 2015.

33. Moreover, any appeal of an SEC ALJ's decision is heard by the SEC itself, the very body which, prior to the administrative proceeding, originally authorized the bringing of an administrative proceeding. Further, the SEC is empowered to decline to hear the appeal, or to impose even greater sanctions. A final order of the Commission, after becoming effective, would then need to be appealed to a United States Court of Appeals.

SEC ALJs

34. SEC ALJs, who preside over administrative proceedings, exercise authority and discretion that makes them officers for the purposes of Article II of the U.S. Constitution.

Broad Discretion to Exercise Significant Power

35. SEC ALJs enjoy broad discretion to exercise significant authority with respect to administrative proceedings. Under the SEC Rules of Practice, an SEC ALJ – referred to in the Rules of Practice as the "hearing officer" – is empowered, within his or her discretion, to perform the following, among other things:

a. Take testimony. RoP 111.

b. Conduct trials. *Id.*

c. Rule on admissibility of evidence. RoP 320.

d. Order production of evidence. RoP 230(a)(2), 232.

e. Issue orders, including show-cause orders. *See, e.g.*, 17 CFR 201.141(b); *In the Matter of China Everhealth Corp.*, Admin. Proc. Rel. No. 1639, 2014 SEC LEXIS 2601 (July 22, 2014).

f. Rule on requests and motions, including pre-trial motions for summary disposition. *See, e.g.*, RoP 250(b).

g. Grant extensions of time. RoP 161.

h. Dismiss for failure to meet deadlines. RoP 155(a).

i. Reconsider their own or other SEC ALJs' decisions. RoP 111(h).

j. Reopen any hearing prior to the filing of a decision. RoP 111(j).

k. Amend the SEC's OIP. RoP 200(d)(2).

l. Impose sanctions on parties for contemptuous conduct. RoP 180(a).

m. Reject filings that do not comply with the SEC's Rules of Practice. RoP 180(b).

n. Dismiss the case, decide a particular matter against a party, or prohibit introduction of evidence when a person fails to make a required filing or cure a deficient filing. RoP 180(c).

o. Enter orders of default, and rule on motions to set aside default. RoP 155.

p. Consolidate proceedings. RoP 201(a).

q. Grant law enforcement agencies of the federal or state government leave to participate. RoP 210(c)(3).

r. Regulate appearance of amici. RoP 210(d).

s. Require amended answers to amended OIPs. RoP 220(b).

t. Direct that answers to OIPs need not specifically admit or deny, or claim insufficient information to respond to, each allegation in the OIP. RoP 220(c).

u. Require the SEC to file a more definite statement of specified matters of fact or law to be considered or determined. RoP 220(d).

v. Grant or deny leave to amend an answer. RoP 220(e).

w. Direct the parties to meet for prehearing conferences, and preside over such conferences as the ALJ "deems appropriate." RoP 221(b).

x. Order any party to furnish prehearing submissions. RoP 222(a).

y. Issue subpoenas. RoP 232.

z. Rule on applications to quash or modify subpoenas. RoP 232(e).

aa. Order depositions, and act as the "deposition officer." RoP 233, 234.

bb. Regulate the SEC's use of investigatory subpoenas after the institution of proceedings. RoP 230(g).

cc. Modify the Rules of Practice with regard to the SEC's document production obligations. RoP 230(a)(1).

dd. Require the SEC to produce documents it has withheld. RoP 230(c).

ee. Disqualify himself or herself from considering a particular matter. RoP 112(a).

ff. Order that scandalous or impertinent matter be stricken from any brief or pleading. RoP 152(f).

gg. Order that hearings be stayed while a motion is pending. RoP 154(a).

hh. Stay proceedings pending Commission consideration of offers of settlement. RoP 161(c)(2).

ii. Modify the Rules of Practice as to participation of parties and amici. RoP 210(f).

jj. Allow the use of prior sworn statements for any reason, and limit or expand the parties' intended use of the same. RoP 235(a), (a)(5).

kk. Express views on offers of settlement. RoP 240(c)(2).

ll. Grant or deny leave to move for summary disposition. RoP 250(a).

mm. Order that hearings not be recorded or transcribed. RoP 302(a).

nn. Grant or deny the parties' proposed corrections to hearing transcript. RoP 302(c).

oo. Issue protective orders governing confidentiality of documents. RoP 322.

pp. Take "official notice" of facts not appearing in the record. RoP 323.

qq. Regulate the scope of cross-examination. RoP 326.

rr. Certify issues for interlocutory review, and determine whether proceedings should be stayed during pendency of review. RoP 400(c), (d).

The SEC ALJ's Decision

36. At the close of an administrative proceeding, the SEC ALJ issues his or her decision, referred to in the Rules of Practice as the "initial decision." RoP 360. The initial decision states the time period within which a petition for

Commission review of the initial decision may be filed. The SEC ALJ exercises his or her discretion to decide that time period.

37. The initial decision becomes the final decision of the SEC after the period to petition for review expires, unless the Commission takes the petition for review. With certain exceptions that do not apply in this matter, the Commission is not required to take up any SEC ALJ's decision for review.

38. As applied to this matter, Commission review is entirely discretionary. The Commission can deny a petition for review for any reason, after considering whether the petition for review makes a reasonable showing that: (i) the decision embodies a clearly erroneous finding of material fact, an erroneous conclusion of law, or an exercise of discretion or decision of law or policy that is "important"; or (ii) a prejudicial error was committed during the proceeding.

39. If no party requests review, and if the Commission does not undertake review on its own initiative, no Commission review occurs. Instead, the Commission enters an order that the decision has become final, and "the action of [the] administrative law judge ... shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission." 15 U.S.C. § 78d-1(c). The order of finality states the date on which sanctions imposed by the SEC ALJ, if any, will become effective. RoP 360(d)(2).

40. Nothing in the rules or statutes prevents the Commission from making the ALJ's sanction effective before the respondent has had an opportunity to appeal the Commission's order, and in fact the Commission routinely makes sanctions effective immediately. *See, e.g., In the Matter of Mark Andrew Singer,* Exchange Act. Rel. No. 72996, 2014 SEC LEXIS 3139 (Sept. 4, 2014).

The Appointment Process for SEC ALJs Violates the Appointments Clause of Article II of the U.S. Constitution and Statutory Law

41. The U.S. Constitution states in relevant part that the President, with the advice and consent of the Senate, shall appoint "...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." U.S. Const., Art. II, § 2.

42. SEC ALJs are "officers" of the United States due, among other things, to the significant authority they exercise; the broad discretion they are afforded; their career appointments; the statutory and regulatory requirements governing their duties, appointment, and salary; the statutory authority creating their position; and their power, in certain instances, to issue the final decision of the agency.

43. The ALJ position is established by statute, which provides that each department/agency "shall" appoint as many ALJs as necessary for the agency's administrative proceedings. 5 U.S.C. § 3105.

44. In *Free Enterprise*, the Supreme Court ruled that for purposes of the Appointments Clause, the Commission is a "Department" of the United States, and that the Commissioners collectively function as the "Head" of the Department with authority to appoint such "inferior Officers" as Congress authorizes through legislation. 561 U.S. 477 (2010).

45. Under the federal statutory scheme governing the SEC, the SEC is required to appoint and compensate its officers, such as ALJs. 15 U.S.C. § 78d(b)(1).

46. Also under federal statute, "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...including functions with respect to hearing, determining, ordering, certifying, reporting, or otherwise acting as to any work, business, or matter." 15 U.S.C. § 78d-1(a).

47. Despite constitutional and statutory mandates, the Commissioners have not appointed ALJs as required.

48. On May 27, 2015, Plaintiffs, through counsel, first received a transcript from a May 11, 2015 oral argument in a lawsuit captioned *Tilton v. SEC*, Case No. 15-cv-02472-RA, United States District Court for the Southern District of New York. A true and correct copy of the May 11, 2015 transcript (the "*Tilton* Transcript") is attached hereto as "**Exhibit A**".

49. *Tilton* involves certain issues substantially similar to this matter – namely, challenges to the constitutionality of the SEC's administrative proceedings.

50. During the course of the May 11 oral argument in *Tilton*, Ms. Jean Lin of the U.S. Justice Department – the same attorney who has appeared in this case on behalf of the SEC – admitted that the SEC Commissioners did not appoint the ALJ in the pending administrative proceeding, and that the appointment of certain SEC ALJs is likely unconstitutional, assuming the ALJs are considered "inferior officers" under the Appointments Clause of Article II of the Constitution.

51. Specifically, the relevant *in judicio* admission from the May 11, 2015 hearing in *Tilton* is as follows:

> THE COURT: Can I ask you the factual question that I asked of Mr. Gunther? Who exactly appoints SEC ALJs? Can you tell me more about the appointment process?

MS. LIN: Your Honor, those facts are not in the record here, but we acknowledge that the commissioners were not the ones who appointed, in this case, ALJ Foelk, who is the ALJ presiding –

THE COURT: There is no factual dispute, okay.

...

THE COURT: Let me just back up for a minute and ask you a question. If I find that the ALJs are inferior officers, do you necessarily lose?

MS. LIN: We acknowledge that, your Honor, if this Court were to find ALJ Foelk to be an inferior officer, that that would make it more likely that the plaintiffs can succeed on the merits for the Article II challenge, at least with respect to the appointments clause challenge.

See Tilton Transcript, attached hereto as "**Exhibit A**", p. 25, ln. 22-25, p. 26, ln. 1-4, p. 29, ln. 10-17.

52. Therefore, the Commission admits *in judicio* that it has not appointed ALJs, but has not come forward and identified who appoints SEC ALJs, let alone the specific ALJ now assigned to hear the Plaintiffs' administrative proceeding. On information and belief, SEC ALJs may be appointed by the SEC's Office of Administrative Law Judges, with input from the Chief Administrative Law Judge,

human resource functions and the Office of Personnel Management. Also on information and belief, in some cases, ALJs have been simply transferred to the Commission from the Federal Energy Regulatory Commission (FERC) and other federal agencies.

53. Improper appointments are a structural defect in the ALJ program. The Commissioners are sworn to faithfully carry out the executive authority entrusted to them, including the power to appoint key officers. Governing regulations provide:

> The members of this Commission have undertaken in their oaths of office to support the Federal Constitution. Insofar as the enactments of the Congress impose executive duties upon the members, they must faithfully execute the laws which they are charged with administering.

17 C.F.R. § 200.54.

54. Commissioners have the power and responsibility to ensure that the office of ALJ – an office wielding significant authority – is filled by an individual whom the Commissioners (as the collective Head of the Department) have evaluated and deemed appropriate to this critical function. Without the scrutiny and approval inherent in collective appointment by the Commissioners, ALJs lack the imprimatur of the Department Head necessary to carry out such a sensitive and powerful role. It is one thing for Commissioners appointed by the

President and confirmed by the Senate to use their collective judgment to appoint individuals who preside over SEC administrative proceedings. It is quite different, and in derogation of Article II and statutory law, to fill that crucial presiding role through bureaucratic means far removed from our elected President and Congress.

55. The Administrative Procedure Act ("APA"), 5 U.S.C. § 500 *et seq.*, establishes ALJs' powers with respect to adjudication. 5 U.S.C. 556, 557. The securities laws empower the SEC to delegate certain functions to SEC ALJs, including those listed above at paragraphs 35.a through 35.rr and 36 through 39. 15 U.S.C. § 78d-1.

56. SEC regulations establish the "Office of Administrative Law Judges," and outlines their authority. *See, e.g.,* 17 C.F.R. § 200.14; 17 C.F.R. § 200.30-9; 17 C.F.R. § 201.111. Those regulations provide that SEC ALJs' authority with respect to adjudications is to be as broad as the APA allows. 17 C.F.R. § 201.111 ("No provision of these Rules of Practice shall be construed to limit the powers of the hearing officer provided by the Administrative Procedure Act, 5 U.S.C. 556, 557.").

57. The salary of SEC ALJs is specified by statute. There are eight levels of basic pay for ALJs, the lowest of which may not be less than 65% of the rate of

basic pay for level IV of the Executive Schedule, and the highest of which may not be more than the rate of basic pay for level IV of the Executive Schedule. 5 U.S.C. § 5372. (The Executive Schedule is a system of salaries given to the highest-ranked appointed positions in the executive branch of the U.S. government. 5 U.S.C. § 5311.)

58. The means of appointing an ALJ is specified by statute. Appointments are made by agencies based on need. 5 U.S.C. § 3105. By regulation, ALJs may be appointed only from a list of eligible candidates provided by the Office of Personnel Management ("OPM") or with prior approval of OPM. 5 C.F.R. § 930.204. OPM selects eligible candidates based on a competitive exam, which OPM develops and administers. The SEC, like other agencies, is supposed to select ALJs from OPM's list of eligible candidates, based on the SEC's need. *See* 5 U.S.C. § 3105; 5 C.F.R. § 930.204.

59. All ALJs receive career appointments and are exempt from probationary periods that apply to certain other government employees. 5 C.F.R. § 930.204(a). They do not serve time-limited terms.

The SEC ALJs' Removal Scheme Violates Article II's Vesting of Executive Power in the President

60. SEC ALJs are removable from their position by the SEC "only" for "good cause," which must be "established and determined" by the Merit Systems Protection Board ("MSPB"). 5 U.S.C. § 7521(a).

61. This removal procedure involves two or more levels of tenure protection.

62. First, as noted, SEC ALJs are protected by statute from removal absent "good cause." 5 U.S.C. § 7521(a).

63. Second, the SEC Commissioners, who exercise the power of removal, are themselves protected by tenure. They may not be removed by the President from their position except for "inefficiency, neglect of duty, or malfeasance in office." *See, e.g., Free Enterprise*, 561 U.S. at 487; *MFS Sec. Corp. v. SEC*, 380 F.3d 611, 619-20 (2d Cir. 2004).

64. Third, members of the MSPB, who determine whether sufficient "good cause" exists to remove an SEC ALJ, are also protected by tenure. They are removable by the President "only for inefficiency, neglect of duty, or malfeasance in office." 5 U.S.C. § 1202(d).

65. As executive officers, SEC ALJs may not be protected by more than one layer of tenure.

66. Article II of the U.S. Constitution vests "[t]he executive Power ... in a President of the United States of America," who must "take care that the Laws be faithfully executed." U.S. Const., Art. II, § 1, cl. 1; id., § 3. In light of "[t]he impossibility that one man should be able to perform all the great business of the State," the Constitution provides for executive officers to "assist the supreme Magistrate in discharging the duties of his trust." 30 Writings of George Washington 334 (J. Fitzpatrick ed. 1939); *see also Free Enterprise*, 561 U.S. at 483.

67. Article II's vesting authority requires that the principal and inferior officers of the Executive Branch be answerable to the President and not be separated from the President by attenuated chains of accountability. Specifically, as the Supreme Court held in *Free Enterprise*, Article II requires that executive officers, who exercise significant executive power, not be protected from being removed by their superiors at will, when those superiors are themselves protected from being removed by the President at will.

68. The SEC ALJs' removal scheme is contrary to this constitutional requirement because SEC ALJs are inferior officers for the purposes of Article II Section 2 of the U.S. Constitution, and because:

a. SEC ALJs are protected from removal by a statutory "good cause" standard; and

b. The SEC Commissioners who are empowered to seek removal of SEC ALJs – within the constraints of the "good cause" standard – are themselves protected from removal by an "inefficiency, neglect of duty, or malfeasance in office" standard; and

c. The MSPB members who are empowered to effectuate the removal decision – again limited by a "good cause" standard – are themselves protected from removal by an "inefficiency, neglect of duty, or malfeasance in office" standard.

69. Under this attenuated removal scheme, "the President cannot remove an officer who enjoys more than one level of good-cause protection, even if the President determines that the officer is neglecting his duties or discharging them improperly. That judgment is instead committed to another officer, who may or may not agree with the President's determination, and whom the President cannot remove simply because that officer disagrees with him. This contravenes the President's 'constitutional obligation to ensure the faithful execution of the laws.'"

Free Enterprise, 561 U.S. at 484 (quoting *Morrison v. Olson*, 487 U.S. 654, 693 (1988)).

70. Because the President cannot oversee SEC ALJs in accordance with Article II, SEC administrative proceedings violate the Constitution.

The SEC's Chosen Course Will Cause Plaintiffs Severe and Irreparable Harm

71. Without injunctive relief from this Court, Plaintiffs will be required to submit to an unconstitutional proceeding. This violation of a constitutional right, standing alone, constitutes an irreparable injury. The lack of traditional procedural safeguards in SEC administrative proceedings further exacerbates that harm.

72. Allowing the SEC to pursue an administrative proceeding while the instant complaint is pending would require the expenditure of substantial legal fees defending against an unconstitutional action. Moreover, Plaintiffs cannot assert counterclaims or seek declaratory relief in an administrative proceeding, foreclosing any possibility of review until an appeal to a federal circuit court of appeals. The burdens incurred during an administrative proceeding would be for naught, because such administrative proceeding is unconstitutional and the SEC likely would try to reprise its case in a lawful setting, such as federal district court. However, forcing Plaintiffs to litigate twice would compound costs, lost time, and reputational risk.

73. Furthermore, if Plaintiffs were to lose in an administrative proceeding, the damage could be severe and irreversible, well before Plaintiffs could obtain meaningful judicial review of the Article II claims.

74. This severe harm, which threatens to damage Plaintiffs' business and potentially those investors in Fund II, is irreparable. The availability of an appeal after an administrative proceeding to a federal circuit court of appeals cannot avoid it, because the administratively-imposed sanction already may take effect – and the damage therefore already substantially and harmfully done – by the time the appellate court made a ruling.

75. Likewise, the harm cannot be effectively remedied after the fact by money damages. Various immunity doctrines substantially constrain Plaintiffs' ability to seek damages from the SEC. Furthermore, even if damages were procedurally available, the reputational harm to Plaintiffs – possibly permanent and devastating to Plaintiffs' trust-based investment business – should the SEC impose administrative sanctions would be impossible to monetize.

76. By contrast, the SEC will suffer relatively little to no harm from a pause in an administrative proceeding against Plaintiffs pending final resolution of these important constitutional issues. Any claim of harm by the SEC would be particularly fanciful because the SEC maintains the option of bringing its

enforcement action against Plaintiffs in federal court, as it routinely does with other investment advisers.

COUNT ONE

APPLICATION FOR INJUNCTIVE RELIEF

77. Plaintiffs repeat and re-allege each of the foregoing paragraphs of this Second Amended Complaint as if fully set forth in full.

78. Plaintiffs' constitutional rights will be irreparably harmed if a permanent injunction (and, if necessary, a preliminary injunction and temporary restraining order) are not issued against the SEC's administrative proceeding. Plaintiffs have a substantial likelihood of success on the merits of their claims. Plaintiffs will be irreparably injured without injunctive relief, as described above, and the harm to Plaintiffs, absent injunctive relief, far outweighs any harm to the SEC if they are granted. Finally, the grant of an injunction will serve the public interest in the protection of parties' constitutional rights.

COUNT TWO

DECLARATORY JUDGMENT

79. Plaintiffs repeat and re-allege each of the forgoing paragraphs of this Second Amended Complaint as if fully set forth in full.

80. Plaintiffs request a declaratory judgment that (i) the SEC's appointment process for SEC ALJs is unconstitutional and violates statutory law; and (ii) the statutory and regulatory provisions and practices providing for the positions, tenure protections, and removal of SEC ALJs are unconstitutional.

Jury Demand

81. Plaintiffs hereby demand a trial by jury on all issues so triable.

WHEREFORE, Plaintiffs pray for judgment and relief as follows:

A. An order and judgment declaring the SEC's appointment process for SEC ALJs is unconstitutional and violates statutory law.

B. An order and judgment declaring unconstitutional the statutory and regulatory provisions and practices governing the removal of SEC ALJs.

C. An order and judgment enjoining the Commission from carrying out the administrative proceeding against Plaintiffs.

D. Such other and further relief as this Court may deem just and proper, including reasonable attorneys' fees and the costs of this action.

Dated: June 3, 2015.

Respectfully submitted,

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

GRAY FINANCIAL GROUP, INC., LAURENCE O. GRAY and ROBERT C. HUBBARD, IV,	)	
	)	Civil Action File No. 1:15-cv-0492-AT
Plaintiffs,	)	
v.	)	
UNITED STATES SECURITIES AND EXCHANGE COMMISSION,	)	
Defendant.	)	

CERTIFICATE OF SERVICE

This is to certify that I have this day served a copy of the foregoing **SECOND AMENDED COMPLAINT** via the Court's ECF electronic filing system which will automatically send email notification of such filing to all counsel of record, as follows:

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EXHIBIT A

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK
----------x

LYNN TILTON, et al.,

Plaintiffs,

v. 15 CV 2472 (RA)

SECURITIES AND EXCHANGE COMMISSION,

Defendant.

----------x

New York, N.Y.
May 11, 2015
3:00 p.m.

Before:

HON. RONNIE ABRAMS,

District Judge

APPEARANCES

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U.S. DEPARTMENT OF JUSTICE
Attorneys for Defendant
BY: JEAN LIN
JEANNETTE A. VARGAS

(In open court)

THE DEPUTY CLERK:

THE COURT: In the matter of Tilton, et al., versus SEC, Docket Number 15 CV 2472.

Counsel, please state your name for the record.

MR. GUNTHER: Good afternoon, your Honor. For the plaintiffs, Christopher Gunther, from Skadden, Arps. I'm here with my colleague, David Zornow, from Skadden, and co-counsel Susan Brune and MaryAnn Sung, from Brune & Richard.

THE COURT: Good afternoon, all.

MS. LIN: Good afternoon, your Honor. Jean Lin on behalf of the Securities and Exchance Commission, and with me is co-counsel, Jeannette Vargas.

THE COURT: Good afternoon.

Mr. Gunther, would you like to begin?

MR. GUNTHER: Thank you, your Honor.

Lynn Tilton is in the fight of her life. She is facing the trial of her life. Ms. Tilton is here in court.

THE COURT: Good afternoon.

MR. GUNTHER: She is facing an SEC proceeding that has an unconstitutional component right at its core. She is not in the fight alone. She and Patriarch control more women-owned businesses than anyone in the United States. Ms. Tilton, through her entities, employs more individuals, more Americans, than any woman in the United States.

For 75 years, the Securities and Exchange Commission, if they were going to bring a case of this type against Ms. Tilton, had to come to this courthouse and appear before the principal officer of the United States, a United States district judge appointed by the president and confirmed by the senate. For 75 years, that was the case. And the appointments clause governs no less, yet Congress has changed the options available to the Securities and Exchange Commission, because in Dodd-Frank, for the first time, a proceeding of this type can be brought before an administrative law judge. That is a sea change, and the SEC has now doubled the amount of its ALJs to prepare for that sea change.

The problem is the appointments clause governs there, and the Supreme Court has held that the commissioners themselves have to appoint officers, inferior officers, who do the Commission's work. And you can go back to the 1933 Act, when the Commission was first formed, for a statute that specifically says that if somebody is going to stand in the commissioner's shoes at an SEC hearing, it has to be an officer. That is the language that was used in the '33 Act itself.

When the case was brought in the administrative proceedings, we now face a situation where we don't even know who the presiding officer was appointed by. The appointments clause demands more than that.

THE COURT: Can I ask a question about that? I should have asked that at the start. Are there factual issues like that in dispute? Is discovery necessary? I assume no one has requested putting any evidentiary matter on today; no one is going to call any witnesses. But are there factual issues in dispute that we need to resolve before I can resolve these issues?

MR. GUNTHER: I don't think that your Honor has to deal with -- just in evaluating the likelihood of success on the merits, I don't think your Honor has to deal with factual issues for this reason: The SEC and the government concede that they do not view their ALJs, the SEC ALJs, as officers of the United States. They are not taking the position in defense to our lawsuit that, oh, wait, the SEC ALJs are actually officers that were properly appointed under the appointments clause. Instead, they put all their eggs in this basket claiming that the SEC ALJs are mere employees appointed to government service, just in the manner that paralegals and correctional officers can be appointed. So because of that concession, so to speak, the issue is joined before your Honor very directly where either they're officers or they're not. If they're officers, we win, and I think the SEC would not say we have a backup defense to that.

Now, there are details in the internal workings of the SEC that are curious. It is curious to me that in a 26-page

brief, the government hasn't told us who within the bureaucracy actually appoints the ALJs. As long as it is not the commissioners themselves, the constitutional violation exists, and your Honor should see the likelihood of success on the merits of our claim.

THE COURT: Please proceed.

MR. GUNTHER: So, here's the problem. Justice Kennedy said it well when he said, if structure fails, liberty is always in peril. And he said that in a case where he described in detail why the separation of powers in the appointments clause are critical to the preservation of individual liberty.

You can see actually what is happening here at the SEC when they don't even have -- it is slipping from the grip of government, sort of slipping from the people, when you have a situation where the ALJ is going to find not just the law but also the facts at this very important trial, is not connected to the commissioners themselves through an appointment or in the chain of command of the executive branch, with the attendant protections the Free Enterprise case says is invalid.

There is nothing more important than the presiding officer at a trial, and we're facing a trial that is now scheduled for October in which the presiding officer we're being told is a mere employee. And it speaks volumes about how the SEC views the process; that they would say any employee can do for purposes of this hearing. But that is not what Congress

did in 1933, when they established a federal hearing before the commissioners. The commissioners themselves have to take part in that hearing; and if they are not going to do it, the people that stand in their shoes have to be officers. It says that in the statute.

It is not just in 1933. Because after the Administrative Procedure Act was passed in 1946, the Commission instituted rules of practice in which it said the presiding officer at a hearing of this type will be deemed a hearing officer. Again, that word "officer," and all of the rules of practice constantly used the refrain a "hearing officer" who will preside at the hearing.

THE COURT: Does that matter what they're called as opposed to what they do, and if they issue final orders, and how much power they have ultimately?

MR. GUNTHER: I think what they're called matters because it shows what the original understanding was at the institution of the SEC, about what level of employee had to conduct the hearing. It has to be an officer. So the name matters.

But what ultimately is the most important thing is what your Honor is alluding to, what they do, and what they do is conduct trials. This is from the SEC's website. They conduct trials in the same manner as federal district courts do when they conduct a bench trial. That is what the SEC says

about what the role is of their own ALJs.

THE COURT: The Commission has to issue a final order; right?

MR. GUNTHER: They do not have to actually issue a final order. What they have to do, the finality comes from the statutes itself, and it says, as long as no one seeks review of the initial decision of the ALJ and no commissioner him or herself initiates review, then the initial decision of the ALJ becomes final as a matter of law. And that is the practice. If you look at --

THE COURT: Isn't it the Commission that issues the final order and, before doing so, makes that determination?

MR. GUNTHER: If no one seeks review as a matter of formality --

THE COURT: They make a determination letter sua sponte they want to review it; correct?

MR. GUNTHER: They can, yes. They have the opportunity --

THE COURT: Even if they don't, it is the Commission that is issuing the final order; is that right?

MR. GUNTHER: What the statute says is that -- this is 15 U.S.C. 78(d)(1)(C) -- finality of delegated action. And it says, 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, commission, individual commissioner, administrative law judge, in this case, shall for all purposes, including appeal or review, be deemed an action of the Commission.

So it comes by operation of law. If no one does, as matter of protocol, as a matter of formality, if no one initiates the review before the commissioners themselves, a form document -- it's a boilerplate document -- gets issued by the Commission to say, no one has taken advantage of review and, therefore, the ALJ decision is final. But that doesn't reflect any reasoning, thinking, critical analysis by the Commission. It is just a formality because no one has taken action.

Now, to back up from the point, your Honor doesn't even have to reach the finality or lack of finality in the ALJ's decision making for a couple of reasons:

The first is in the Samuels case in the Second Circuit, the Second Circuit analyzed the special trial judges who were within the tax area and concluded that they were inferior officers of the United States without regard to whether they could issue final or non-final decisions. They looked just at what is the role, what are the specific acts performed by the special trial judge, and they listed them. They said, they take testimony, they make credibility findings, they issue rulings on evidence. And the Second Circuit concluded from that alone, without reaching questions about

finality or lack of finality, they say that makes the person who holds that role an inferior officer of the United States that has to be appointed consistent with the appointments clause.

THE COURT: Didn't the Samuels, Kramer case come before the Supreme Court's decision in Freytag; and in Freytag, while it agreed with the Second Circuit's holding, seemed to indicate that the dispositive factor in the inferior officer determination was the finality of certain decisions?

MR. GUNTHER: Your Honor is correct that Samuels came before Freytag, and Freytag followed Samuels. It is also correct that there was an additional piece of the analysis in Freytag that looked at the finality or lack of finality authority of the special trial judge.

We think Judge Randolph, in a separate opinion in the Landry case, had it exactly right. He said what happened in Freytag, the holding of Freytag was just the powers and responsibilities of the special trial judge alone made that special trial judge an officer of the United States. It was only an alternative holding offered by the Freytag court that that looked at the finality question.

There is a very interesting and instructive opinion by the Officer of Legal Counsel with respect to --

THE COURT: I'm sorry. Before you get there, you referenced Landry. But in Landry, the holding was the ALJs are

not inferior officers.

MR. GUNTHER: Correct. Speaking about the FDIC context. There's a few things to say about that.

THE COURT: Please.

MR. GUNTHER: One is Landry is inconsistent with the Samuels case. It is a D.C. Circuit opinion, and we're in the Second Circuit, and we ask your Honor to follow Samuels, which is the controlling authority here.

Second, the better part of the argument among the split decision in the Landry case was by Judge Randolph in his separate opinion where he said, like Samuels, Samuels got it right, that you don't have to reach the issue of finality, and in fact, Freytag, which is the highest court in the land, only offered an alternative holding on finality.

The third point about Landry is what I was going to speak about, about the Department of Education and the way the Office of Legal Counsel has dealt with the issue there. Just to start, when the Department of Education was formed in 1978, the Congress structured things exactly the way we think Congress structured them here, which is they said, the head of the department, the Secretary of Education, is going to be the one who appoints the ALJs. The reason why the statute said that is precisely because the ALJs within the Department of Education are inferior officers of the United States, consistent with the appointments clause. The same thing with

regard to the SEC. The SEC commissioners themselves are the head of the department. They're the ones who have to appoint an inferior officer holding the responsibilities of an SEC ALJ. What the Office of Legal Counsel did in analyzing the Secretary of Education structure is they indicate very strongly that the idea of finality doesn't matter. It is the responsibilities that are held by the sitting judge that control and make that sitting judge an inferior officer of the United States.

I should add the Office of Legal counsel is a special area within the Department of Justice whose authority and opinions on matters of separation of powers like this are controlling on the federal government. It is a very important opinion that we ask your Honor to take into account. It takes the finality issue off the table. But as I have said, even if your Honor had to reach the issue of finality, the way that it is structured under 78(d)(1)(C), it is effectively a final decision of the ALJ, as long as no one objects.

When you're analyzing whether someone is an officer of the United States or not, you have to look broadly. That's what Freytag did. In Freytag, it was a specific tax dispute that was before the court. It was not an instance in which the special trial judges could issue a final decision, but the Supreme Court said you have to look at all of the authority of the judge. If there are instances in which the judge can issue a final order, then that's something that again as an

alternative holding shows that special trial judges are an inferior officer.

THE COURT: Let me ask you this: Looking at Footnote 10 from Free Enterprise, where the Court made clear that its holding does not address administrative law judges -- and I just want you to speak to this particular language -- it says, unlike members of the board, many administrative law judges, of course, perform adjudicative rather than enforcement or policy-making functions -- I'm going to skip the cites -- or possess purely recommendatory powers. What should I do with this language? How should I analyze this?

MR. GUNTHER: I think what the Court was doing there, your Honor, was basically teeing up the issue to be decided another day. I think also what that court had in mind is the vast spectrum of administrative law judges who serve within the federal system. Let me give you an example. There's about 1,500 administrative law judges in the federal system. Only five sit in the SEC. But they have very different roles and responsibilities across varying agencies. The agency that has by far the most administrative law judges is the Social Security administration. Of 1,500, it has more than 1,200 of the ALJs. They perform a function that is in no way analogous to what an ALJ at the SEC has to do. An SEC ALJ holds and presides over an adversary proceeding in which the government is trying to seek penalties, monetary penalties and other

penalties, against individuals. In the Social Security Administration context, they're not even considered adversary proceedings. They are proceedings at which a claimant is asking for government benefits, usually without even the representation of counsel, and where the administrative law judge is assembling a record to make a recommendation as to how to deal with the claim for government benefits. I think it was really in recognition of the vast spectrum that the Supreme Court was teeing up the issue to be decided later on a case-by-case basis based on the responsibilities and powers exercised by particular ALJs.

Here, with the SEC ALJs, they are really at the other side of the spectrum from where the Social Security Administration and other public claims ALJs reside.

What is going to happen here if your Honor doesn't step in and enjoin what is going on is we'll wind up in a two-to-three-week trial in October before an SEC ALJ where that ALJ is going to make the critical findings of fact and conclusions of law, including probably, most critical in this case, the evaluation of the credibility of witness testimony. In a real sense, that is going to be binding on the administrative process from then on.

Ms. Tilton will surely testify at that hearing. It is going to be critical testimony. And the ALJ is going to have an opportunity to look her in the eyes. But the odd thing is

when Ms. Tilton is looking at the administrative law judge, it is going to be her one day in court, the one chance to tell the judge her story and what happened here, what really happened. And the credibility determinations are going to be made by somebody who is sitting in the chair in a constitutionally defective way, somebody who hasn't been appointed by the Commission as the statutes and Constitution require to be done.

What I think the government is trying to do in putting off the day of reckoning, so to speak, resolving this important constitutional issue now, they want to say, wait until if there is an appeal to the circuit after all is said and done, which by the way could be two years easy or more from this day. At that point, the judges who are going to hear that challenge or that appeal are going to be potentially bound by the credibility determinations that are key to any ALJ decision.

THE COURT: Isn't that true if you have a jury trial or a bench trial, that the circuit is still looking at the record, and the credibility determinations were made by either jury or judge?

MR. GUNTHER: Absolutely. And my point is, though, the person who actually is going to fill that role is somebody who isn't constitutionally permitted to play it. It is a critical role, and we're going to be in a situation where the person who plays that role and weighs in -- we hope she weighs in in our favor -- but if she doesn't, we're going to be up

making an argument years from now when the wrong person was sitting in the chair, so to speak. So it is critically important in this case the right person, the person who actually has the constitutional authority, play the role.

THE COURT: Can we talk about jurisdiction --

MR. GUNTHER: Yes.

THE COURT: -- in particular, and you have alluded to the fact of the ability to appeal to a circuit court. Can we talk about meaningful judicial review in particular and why review by a circuit court, after exhausting administrative procedures, is inadequate, in your view.

MR. GUNTHER: I think Judge Berman got it just right, completely right in Duka, when he said -- and he really put it in a pithy way -- you can't unscramble the egg. The claim here is that the proceeding itself, unrelated to anything to the merits -- and I can tell your Honor a lot about the merits, but that is not what this hearing is about. Completely unrelated to the merits at all, our point is it is unconstitutional that Ms. Tilton should have to go through a two-or-three-week trial before someone who is not an officer of United States, wasn't appointed. If two years from now plus a circuit court agrees with us on that point after we have had to fight for two years plus, the reason she has come to this courthouse today to prevent an unconstitutional proceeding from going forward is law. You can't unscramble the egg. You can't take that away.

There is a real impact, a real world impact from that delay of resolution of this important matter, this important question, which is for two years she and her fund and the portfolio companies within those funds have to deal with and grapple with everything that is brought on by this SEC case. So there is real world effect. Real world effect, your Honor.

The other aspect of jurisdiction that we asked your Honor to focus on is the distinction between a facial challenge and an as-applied challenge. Your colleagues here in the Southern District have seen that distinction quite clearly.

THE COURT: That is Judge Kaplan, in particular; correct?

MR. GUNTHER: Judge Kaplan spelled it out quite clearly. He said the challenge before him was an as-applied challenge, and he dismissed it for want of jurisdiction, but he clearly made the point that a facial challenge is one that can be brought and jurisdiction is proper. That's what Judge Rakoff found in Gupta. It is what Judge Berman found in Duka. And it makes entire sense because it is completely consistent with Free Enterprise itself. Free Enterprise had a facial challenge. Basically, the PCAOB doesn't have valid sitting members. And the Supreme Court, applying the same three-factor test your colleagues applied, said this is a facial challenge that meets the test, and it can be brought pre-enforcement.

THE COURT: Is there any way to reconcile the Duka

case with the Bebo case, or do you think Judge Randa got it wrong?

MR. GUNTHER: I don't know of any way to reconcile it. I think Judge Randa got it wrong. It is interesting that on the merits, he offered an opinion on the Article II issues, the issues were meritorious, but I think he just got the issue wrong.

If the Court has any other questions on jurisdiction, I would be happy to address them.

THE COURT: No, I don't think so.

Thank you.

MR. GUNTHER: Just in sum, your Honor, this is an extraordinary case. The choice that the SEC has made to send this to an administrative forum by a split three-two vote of the Commission has an enormous impact on Ms. Tilton and her companies and leaves us in a case that we think is going to be critically determined by a fact finder who evaluates her testimony in the hands of someone who doesn't have the constitutional authority to do it. And the way this case has been teed up to your Honor, it couldn't be more squarely presented. There is only one issue on likelihood of success on the merits, and that's this legal issue about whether an SEC ALJ is an inferior officer of the United States. Given the authorities that we have cited, including the Samuels case, including Judge Randolph's separate opinion in Landry,

including the '33 Act saying that these people are officers to stand in the Commissioner's shoes, we think the answer is easily on our side on that question.

THE COURT: Thank you very much.

MR. GUNTHER: Thank you.

MS. LIN: Your Honor, if I may, I will address the jurisdictional question, as well as the Article II challenges, the likelihood of success on the merits; and my colleague, Janet Vargas, will address irreparable harm, as well as other factors for the preliminary injunction.

THE COURT: Let me start with the same preliminary question. In your view, no facts are needed at this stage for me to rule on this motion; is that correct? You don't need any discovery?

MS. LIN: That's correct, your Honor.

THE COURT: Thank you. You may proceed.

MS. LIN: Yes.

Your Honor, our position is that this Court has no jurisdiction over the plaintiffs' Article II challenges to the SEC's administrative proceeding because, as the Second Circuit has held in Altman v. the SEC, the federal securities laws dissuade a discernible intent to channel reviews of challenges to Commission actions and orders through the administrative process with direct review in the Court of Appeals.

This case is an attempt to circumvent that exclusive

review scheme by effectively seeking to stop the Commission from issuing an adverse decision. We think that under Altman, the circuit's decision, this case does not belong in this court, and the plaintiffs must go through the administrative process. If they're aggrieved at the end of that process, they can take an appeal directly to the Court of Appeals.

THE COURT: Let me ask this: How is it that judicial review can be meaningful if by the time the plaintiff reaches the appellate court she has already undergone the very proceeding she is challenging, she is seeking to enjoin?

MS. LIN: Your Honor, that argument can be raised in any case where people are trying to circumvent an exclusive review scheme, is that why wait when my claims are meritorious. The Congress has devised the scheme to make sure that people go through this process that Congress wanted, as long as they have meaningful judicial review at the end. And what it means to have meaningful judicial review, as the Supreme Court has made clear in Thunder Basin and Elgin is that there will be Court of Appeals review and a competent Article III court to address the constitutional questions.

There is no doubt in this case that the plaintiffs can raise their Article II claims in the Court of Appeals if and when the time comes, if they are aggrieved by a Commission order at the end of the administrative process.

THE COURT: How should they raise them? They should

raise them now as affirmative defenses, or they should raise them on appeal?

MS. LIN: They can raise it as an affirmative defense, as they have already done. The first affirmative defense to their answer filed in the administrative process, they challenged the ALJ's authority to preside over the proceeding, and the Commission will address that argument, as it is doing right now in another proceeding where someone else has raised an Article II challenge and in fact oral argument is occurring in June for that argument. Ultimately, this issue can be addressed by the Court of Appeals. And in fact, in the Landry vs. FDIC case, the D.C. Circuit case we discussed earlier, in that case, the Article II challenge was raised through the administrative process. It was raised through the final decision of the board of the FDIC and appealed to the D.C. Circuit. So that's how they can raise that claim. And I think there was some concern about if they have to go through this process, I think that the Supreme Court's decision in FTC v. Standard Oil made it very clear that just because someone has to go through the process of being subjected to an enforcement proceeding doesn't make that an escape route to skip the review scheme that Congress has devised.

I think that given the exclusive review scheme clearly bars these claims, we think that this Court has no jurisdiction. And more importantly, the distinction that

opposing counsel was making about the difference between this case and Free Enterprise also highlights the fact that this case just does not fall within the exception to the exclusive review scheme that Congress requires.

I think, most significantly, in Free Enterprise, what was happening there was that we were talking about a board that's a sub-agency of the SEC. Not every action of the board resulted with the Supreme Court -- is encapsulated in a final Commission order or rule. That is one thing that distinguishes because there is not something from which the accounting firm in that case could appeal.

Secondly, there was no direct path to judicial review because there was no formal action taken against the accounting firm by the PCAOB, which is the Public Company Accounting Oversight Board. So there was no proceeding from which the accounting firm could appeal and ultimately get review in the Court of Appeals pursuant to federal securities laws.

Clearly, we have a very different situation here. The plaintiffs are already subject to the administrative proceeding. If they are aggrieved, they can challenge the claims in the Court of Appeals. So that certainly distinguishes this case from Free Enterprise.

And I think there was also the argument about how this case is wholly collateral to the securities case, and the main argument that the plaintiffs have raised is that this case

raises only facial challenges, and your Honor's recognition of Judge Kaplan's comment about facial challenges sometimes can be more likely addressed, and if I could just speak about that.

THE COURT: Let me just ask you: As to the point about whether it is wholly collateral, by your standard, there would never be a challenge that is actually collateral if an administrative proceeding has already been initiated; correct?

MS. LIN: It is hard to imagine a situation. I think the Free Enterprise definitely is an example where it is, in fact, wholly collateral because it was not bound up in the administrative proceeding from which an appeal could be taken. But in this case here, we know that the purpose, the very purpose of this lawsuit is to stop the administrative proceeding. The challenge to the authority of the ALJ is bound up in this administrative process because we're saying someone has no authority to preside over the administrative proceeding, which is, by the way, the identical challenge raised in Altman, the Second Circuit's binding decision where the challenge similarly was saying that the Commission didn't have the constitutional or statutory authority to issue the sanction order in that case. So this is at least, putting aside hypotheticals, this case falls squarely within the kind of Supreme Court discussion about how this is not wholly collateral. I think the Supreme Court decision in Elgin is also very clear on this point, where the Court said that the

employees' constitutional claims in Elgin are the vehicle by which they seek to reverse the adverse agency decision.

Similarly, here, the very purpose of this lawsuit is to stop the Commission from issuing adverse Commission order, from which the plaintiff could challenge.

Also, I forgot, I want to address the facial versus the as-applied argument. What is important is that in the Supreme Court's decision in Elgin, the court was very clear that facial and as-applied challenges are not meaningful distinctions. The court said, when you determine whether an exclusive review scheme applies, you don't look at the nature of the constitutional claim. In fact, in Elgin itself, the court rejected the dissent suggestion that facial constitutional challenges may be brought. That argument, by dissent, was directly rejected by Elgin. Elgin, by the, way was decided after Judge Rakoff's decision in Gupta. So Judge Kaplan's decision recognized that Elgin does talk about the fact that the nature of a constitutional claim is not dispositive at all. It just says that sometimes it may be easier for a court to address a facial challenge.

So we submit that the distinction the plaintiffs are trying to draw between facial and as-applied challenge was already rejected by Supreme Court.

In fact, I think there was some reference earlier about the fact that Free Enterprise itself is a facial

challenge. That is not the case at all. The case challenges the structure, the existence of the PCAOB; but more importantly, the court said that the challenge here was not to any Commission orders or rules from which review might be sought. That was the distinction. There was no discussion of any kind of facial/as-applied challenge there.

As to the last prong of the exception to the exclusive review scheme was whether the constitutional claims are within the agency's expertise, and we submit that it is, because, as the Supreme Court has recognized in Elgin, agencies are experts on many threshold questions that may a constitutional claim. Here, the agency, the SEC, obviously, is in the best position to interpret its own rules and regulations and to determine the relationship between the ALJ, the finality of the ALJ's decision, and the Commission and whether the Commission has plenary authority.

THE COURT: Is it in a better position to decide a constitutional question than the district court?

MS. LIN: For this prong of the test to be satisfied, the Supreme Court said it is satisfied if the agency has expertise that it can bring to bear. Certainly, the district court may be equipped to address constitutional claims --

THE COURT: I hope so.

MS. LIN: -- but the question here for purposes of determining whether they can circumvent the exclusive review

scheme, some of the relevant questions the Supreme Court said are: Does the agency have some expertise that it can bring to bear on the constitutional question, which they do here; and whether the interpretation sometimes may alleviate some constitutional concerns. For example, if the Commission itself determines what the duties and functions are of the ALJ, that could alleviate the constitutional question of whether these ALJs are, in fact, officers. It is possible, for example, the constitutional question may not even be addressed at all because the Commission could potentially decide the case in the plaintiffs' favor. That would eliminate the constitutional question altogether.

So looking at the various factors, we submit this Court has no jurisdiction to proceed and, certainly, none to issue the injunction that they're seeking.

THE COURT: Thank you.

MS. LIN: If I may move on to the Article II question.

THE COURT: Yes.

MS. LIN: I think there was some references to a few items that were not in the plaintiffs' opening brief that were mentioned in the reply brief, so I will address them.

THE COURT: Can I ask you the factual question that I asked of Mr. Gunther? Who exactly appoints SEC ALJs? Can you tell me more about the appointment process?

MS. LIN: Your Honor, those facts are not in the

record here, but we acknowledge that the commissioners were not the ones who appointed, in this case, ALJ Foelk, who is the ALJ presiding --

THE COURT: There is no factual dispute, okay.

MS. LIN: If I may start with the idea that when deciding whether someone is a constitutional officer, we always begin and we believe that the proper framework is to first look at the authority of the ALJ or the government personnel at issue. And here, we submit that the ALJs are subject to the Commission's plenary review from start to finish for the entire administrative process.

And I think there was some discussion earlier about whether, when there is no petition for review, whether the agency's final decision is issued by the ALJ. And the answer is that no, the final agency decision is made by the Commission. This is so because when there's no petition for review, two things have to happen first before there is final agency decision. First is that the Commission has to first decide whether to review the case on its own initiative, and it certainly has done so from time to time where the Commission sua sponte decided that it will review an ALJ's initial decision even when no petition is filed.

THE COURT: Is a review conducted in every case in which there is no appeal filed by a party to the SEC action? Is a review conducted by the Commission in every case to

determine, number one, whether or not it is going to sua sponte evaluate the findings below or to sign off on those findings?

MS. LIN: That's correct. So the first thing that happens, as your Honor acknowledges, is that the Commission has to firstly determine are they going to, on its own initiative, review this initial decision. And then when it decides not to, it is at that point the Commission issues the final decision of the agency by issuing a finality order. It is only that order that the sanctions can take effect. So the initial decision has no legal force or effect until the Commission acts, and so that certainly is not what was portrayed earlier.

And I think there was some reliance on the statutory language about delegated functions; in particular, your Honor had a colloquy about 15 U.S.C. 78(d)(1)(C). So that statutory language talks generally about what happens when functions are delegated to anyone within the Commission, including ALJ, but for the Commission's rules of practice, the Commission decided specifically to add this extra layer of saying, okay, in the case of an ALJ decision, when there is no initial petition filed, we're going to decide whether we're going to grant review on our own. And by the way, that only takes one commissioner to grant review. So through the rules of practice, the Commission sets forth this extra step of making sure that it decides whether to grant review on its own, and then if not, then to make clear that the sanction, if any, or

the initial decision can become final. So that's, certainly, acts of the Commission, not of the ALJ. So we submit only the Commission has the final decision-making authority.

But that's only one small aspect of the Commission's plenary authority over the ALJ. You look at the entire process from start to finish. The Commission can at any time grant review, even before or after the initial decision, and when it reviews, it can decide to review the issues in the petition or that it can find some other issues that it deems material to review, and it can reverse, set aside, remand the initial decision. And it can make any findings that it deems appropriate based on the record. Or if the Commission doesn't like the record, the Commission can order supplemental proceeding or hear evidence itself. So there was some, I believe, misconception about to what extent the Commission is bound by the ALJ. It is not bound by the ALJ for anything that the ALJ does, and that includes credibility findings. I think there was some discussion earlier about the fact that the ALJ makes important findings, including credibility determinations and the Commission somehow is bound by the credibility determination, and that is not the case. When the Commission reviews the record, of course it may decide and it does give some deference or gives some great weight to the ALJ who sits before the witness and makes a credibility determination, but the Commission is not bound by it. In fact, if the Commission

doesn't like it, it can hear the evidence itself or order additional proceedings. This is not the kind of situation, for example, comparing to the special trial judges in the tax court where the higher court or the tax court is actually required to defer, for example, to factual findings and the credibility determinations of the special trial judges. So this is a wholly different scenario here where we have a Commission that retains control from the conclusions of law, findings of fact. The Commission can make any determination it deems appropriate.

THE COURT: Let me just back up for a minute and ask you a question. If I find that the ALJs are inferior officers, do you necessarily lose?

MS. LIN: We acknowledge that, your Honor, if this Court were to find ALJ Foelk to be an inferior officer, that that would make it more likely that the plaintiffs can succeed on the merits for the Article II challenge, at least with respect to the appointments clause challenge.

THE COURT: How do you respond to the language Mr. Gunther cited, which I believe was in plaintiffs' reply brief, as well, from Section 21 of the Securities Act, which provides that hearings may be held before the Commission or an officer or officers of the Commission designated by it? How do you get around the language that refers to officers?

MS. LIN: Your Honor, we don't believe that any reference to officers necessarily means a reference to a

constitutional officer. There is no indication that Congress intended them to be synonymous. I think even Free Enterprise itself recognizes -- for example, in Free Enterprise, the board members of the PCAOB, the Supreme Court recognized that they're inferior officers, but the court also expressedly declared that the board members were not considered government officers or employees for statutory purposes. So we think that what it means to be an officer for statutory purposes is not synonymous with constitutional officer. In fact, Congress knows how to define those officers. I think that the ordinary meaning of the word "officer" has to be what Congress intended, because in 1933, '34, the term "officer" doesn't have any special meaning, even today. It typically means someone who holds an office, who is charged with a duty, and even the Administrative Procedure Act sometimes uses "officer" interchangeably with "employee." But there is no indication anywhere to say that just because Congress uses the word "officer," it necessarily means constitutional officer, and I think the Supreme Court's recognition in Free Enterprise answers that question.

On the question of whether the Education Department's administrative law judges are indicative of how this Court should decide the question here, we think that this case closely parallels with the FDIC ALJs, which the D.C. Circuit found, in Landry, to be not inferior officers. The parallel with FDIC ALJ is significant. In both instances, the FDIC

board and here the SEC Commission retain plenary authority over the ALJs. Both have de novo review powers, and both issue final decisions for the agency.

THE COURT: Other than Landry, is there any other authority distinguishing the kind of ALJs at issue here from the special trial judges that were found to be inferior officers in Samuels, Kramer and Freytag.

MS. LIN: No, we're not aware of other cases. But I think, if I may, the Freytag and Samuels, Kramer cases fall on the other side of the line, because in Freytag, as your Honor noted, that came after Samuels, Kramer, D.C. Circuit has said, Freytag, the critical part of the court's decision is that the special trial judges had final decision-making authority, which the SEC ALJs do not. But what is important to examine for these purposes, the special trial judges in the Freytag and the Samuels, Kramer cases, their duties and functions have to be viewed within the context of the power of the tax court, and that's the court where the Supreme Court said they exercise a portion of the judicial power of the United States and they function very much like federal or trial judges. More importantly, they have the power of contempt, the power to issue fines, to put people in jail when they don't comply. Whereas, if you look at the ALJ in the SEC situation, they have to go to District Court just to enforce the subpoenas that they issue. So I think in order to examine whether this case is

similar to Freytag or not, the power of the Court has to be taken into consideration, the context in which these duties and authorities are issued.

And I think one other significant factor is that even if the final decision-making authority is just an alternative holding in Freytag, that they're still important authorities that the special trial judges have, the discretion that they have in cases that they don't exercise final decision authority that are not present in the case of the SEC ALJs. As I noted earlier, their factual findings have to be deferred to, which we don't have that here. In fact, as mentioned earlier, the Commission can hear evidence itself. Even when you have the case go up to the Court of Appeals, the Court of Appeals can remand for further proceedings. The other is the contempt power of the special trial judges, which again the SEC ALJs do not have. Even Samuels, Kramer, as the Court noted, the legislative history shows that Congress was increasingly giving power to the special trial judges and recognizes the significance of that. So I think we can't divorce the special trial judges' duties and functions from the context within which their powers were exercised.

THE COURT: You talk about legislative history. If the purpose of the present inquiry is to determine whether Congress stepped beyond its constitutional authority in the appointment and removal scheme that we're talking about here,

why should the Court be deferring to Congress in that fashion?

MS. LIN: Your Honor, we're not saying that Congress' method of appointment itself is dispositive. I was talking earlier about Education AJLs. In that context, Congress specifically said the ALJ in the Education Department shall be appointed by the secretary, which we don't have here. So I'm just saying that Congress, by Constitution, is assigned the job of first determining whether the position they created is one of officer or employee. So it is for that reason we think that in case of doubt, we should defer, this Court should defer to Congress' judgment. We're not saying that is in any way dispositive in this case. But the context of the Education ALJ, Congress did assign, at least specified by statute, that the ALJs need to be appointed by the secretary. What is more important in the Education ALJ context -- and we don't know anymore beyond what was discussed in the opinion -- but we also know that in the context of the Education ALJs, Congress also by statute says that their decisions should be considered final for purposes of judicial review, which is something we don't have here. I don't want to get into the Education case because that's not what is before this Court. What is enough to say here is that we agree that in every case the Court needs to look at the duties and functions of the government personnel at issue and examine that personnel's relationship to the agency's higher decision-making authority and how it fits within the

decision-making scheme. So the reference about how the Office of Legal Counsel apparently had taken the finality issue out of the picture, I don't see that anywhere in the opinion, so we certainly disagree with that reading of the opinion. In fact, that opinion doesn't even address whether the ALJs are in fact inferior officers. The only issue in that case was much narrower, and I can get into the details, but they're not directly relevant here.

Your Honor, if I may just address one last point that was mentioned in the plaintiffs' reply brief but we didn't have an opportunity to respond, was the idea that in Footnote 7 of the plaintiffs' reply brief, the footnote gives the misimpression that the Commission rarely reviews decisions, and at least gave the statistics that there were 185 decisions in the year 2014 but only three reached substantive decision, and we believe that gives the misimpression as if the Commission rarely reviews. What really happened was that, in 2014, only 14 petitions of review were filed, and all 14 were granted by the Commission. And as of now, three decisions have been made, and the others are pending. And the bulk of the other decisions that were mentioned to supposedly automatically become final, we obviously disagree. The bulk of those decisions have to do with the 12J proceedings that are about whether a public company properly files periodic reports, and if they didn't, then that's a violation of securities law, and

most of the time they're uncontested. Just to avoid that misimpression.

To sum up, your Honor, just on the constitutional question as to whether the ALJs are inferior officers, we think it is important to look at Congress' judgment, to defer to Congress' judgment, but also the placement of the ALJs within the competitive service to see how they fit within the constitutional scheme. The fact that they're in the competitive service is one indicator of their status within the federal structure and, specifically, how they're viewed within the -- the authority and powers they have under the laws of the United States.

THE COURT: Thank you.

MS. VARGAS: Good afternoon, your Honor.

THE COURT: Good afternoon.

MS. VARGAS: Jeannette Vargas from the U.S. Attorney's Office on behalf of the SEC.

I'm going to briefly address the irreparable harm prong, specifically because the Second Circuit has described irreparable harm as the single most important prerequisite for the issuance of a preliminary injunction, yet plaintiffs only briefly address it in their brief and pretty much gave it the back of hand today, and arguing, at the same time, they must establish irreparable harm in order to get the extraordinary injunctive relief they're seeking of enjoining an SEC

enforcement proceeding that's been taken in the public interest. They must also show that the balance of equities in this case weighs in favor of the granting of an injunction. We suggest they haven't been able to demonstrate either of those prongs.

First of all, here is what is going to happen, as Ms. Lin demonstrated during her argument. If an injunction does not issue, all that is going to happen here is that an ALJ will preside over the initial stage of a proceeding and will issue nothing more than an initial decision in Ms. Tilton's case. It is the Commission, and not the ALJ, that is going to issue the final decision of the agency. That's it. That's the supposed harm we're talking about, an initial decision by an ALJ that will be reviewed de novo by the Commission. A final decision will be issued by the Commission. And finally, there will be an available appeal to the Second Circuit. Nothing in this set of facts show that plaintiff will suffer any injury at all, let alone an injury that could not be remedied in the ordinary course of the administrative process.

In their papers, plaintiffs argue that they don't have to show irreparable harm because such harm may simply be presumed in any case involving a constitutional issue. This argument flows from a flawed premise. Plaintiffs essentially are arguing the harm that they are going suffer is being required to go through the administrative proceeding before

they can raise their constitutional claim in the federal Court of Appeals. It is not surprising that plaintiffs have not found any support for the notion that going through the administrative process, each an allegedly unconstitutional process, inherently constitutes irreparable harm. Indeed, the very notion contradicts the well established principle of administrative exhaustion that applies here. Both the Supreme Court and the Second Circuit in Altman have repeatedly affirmed in numerous contexts that raising a claim regarding the constitutionality of an administrative proceeding is not a get-out-of-jail-free card from having to exhaust your remedies and go through the exclusive jurisdictional scheme. You still have to go through the process, and then you obtain your judicial review. It would be axiomatic to hold that Congress can require plaintiffs to submit to the administrative process before making their claims in a Court of Appeals, but somehow that this administrative process that they have to go through is irreparable harm that allows them to get an injunction from a district court. In fact, as Ms. Lin alluded to earlier in the Altman case itself, which was the Second Circuit's decision addressing the jurisdictional scheme, this very issue came up, which is the attorney who had been debarred by the Commission argued that the Commission proceeding was unconstitutional and, therefore, he could evade the proceeding itself and go through district court. And the Second Circuit said no, if your claim

is that it is an unconstitutional proceeding, you have to go through the process and then raise your claim. Just as that decision speaks to the jurisdictional issue, it also speaks to irreparable harm because it can't be an irreparable harm if the scheme that Congress requires you to go through and the scheme that the Second Circuit has said that you're required to go through is itself the irreparable harm that can give rise to an injunction.

Now, in making their argument about presumed irreparable harm, plaintiffs rely on a series of cases that concern personal or individual civil rights, usually First Amendment cases, freedom of speech or privacy rights. Specifically, they rely very heavily on a Second Circuit decision in Statharos, a 199 decision. The language of Statharos that actually addressed it is a single sentence in a parenthetical, and they claim that this decision is, therefore, the one decision from the Second Circuit that speaks to this issue of, broadly speaking, any constitutional deprivation can be per se presumed to give rise to irreparable harm.

But the Second Circuit's subsequent decisions and, actually, prior line of cases on this issue show that that simply is not the case. There are many, many decisions by the Second Circuit beyond Statharos that address when irreparable harm can be presumed even in the First Amendment context. In the First Amendment context, there are a special set of rules

that apply, generated out of Supreme Court jurisprudence, such as Elrod, which say that because the First Amendment is a bedrock constitutional right, any infringement of that right is per se irreparable. Even if it is just a momentary infringement, that is irreparable harm. That is what cases in that line of jurisprudence are referring to. Even there, the Second Circuit has said post-Statharos that the issue is not that simple. Simply alleging a First Amendment violation is not enough in every case to get you out of a showing of irreparable harm. We cite one of those cases, Amandola v. Town of Babylon. There are other cases. I will refer the Court to Bronx Household of Faith v. Board of Education, 331 F.3d 342, which is a 2003 Second Circuit case, which again speaks at length about whether or not one broad sentence from Statharos can be read simply as weeding out the requirement for a showing of irreparable harm across constitutional deprivations, and of course it can't be read as broadly as plaintiff would like it to be. Instead, the Second Circuit said, even in the First Amendment context where we're talking about a special set of rules because of the deprivation of a bedrock right of our democracy, even then there are situations in which one may have to make a showing of irreparable harm, depending upon the nature of the speech rights infringed. It certainly doesn't speak to other constitutional rights such as the structural constitutional rights that are at issue here. But numerous

courts in this circuit have. For example, we have cited several decisions by SDNY courts and EDNY courts, both pre and post Statharos that have specifically addressed this issue and held that structural constitutional violations are not presumed to give rise to irreparable harm in the same way that a deprivation of an individual personal right would be.

And this case, I think, perfectly illustrates why that is the case. The deprivation of your right to free speech is personal to you. It can't be compensated by money damages. But whether the executive branch exercises sufficient control over a subordinate officer is not a right personal to any individual. It is an issue of the proper separation of power between the branches of government.

That plaintiffs will not suffer irreparable harm in this particular case is clear by looking at what the harm is he's alleging from this constitutional violation. Ironically, what plaintiffs are complaining about is that in the initial stage of her administrative case, it is going to be heard by a government official that is too independent of the executive branch, that is what it comes down to; that the ALJ, under Free Enterprise, should be appointed directly by the commissioner and subject to more direct control by the president under the double tenure provisions of the Free Enterprise decision. Plaintiffs have not explained how this problem of too much independence for an adjudicated official deprives her of any

personal right, let alone one that causes her irreparable harm. To the extent there has been congressional encroachment upon executive branch authority, this is a purported harm that affects all citizens equally and not Ms. Tilton in particular.

They also refer to cases that discuss whether or not due process infringements also constitute irreparable harm. I would simply say on this that there are cases that go both ways. There's certainly decisions where looking at the facts of a particular case, courts have held that due process rights, again, much more like individual rights than the structural types of rights that we're discussing here, those kinds of infringements constitute irreparable harm, but there are certainly decisions that go the other way. The Seventh Circuit has held that due process violations do not give rise to irreparable harm in the Flower Cab decision that we cited in our brief.

There are other decisions from EDNY courts I believe also cited in our brief that have similarly held that due process violations are not the types of rights that are like First Amendment violations that give rise to a finding of irreparable harm.

Finally, I would like to refer to one last Second Circuit case even though it is not an irreparable harm case, but I think it is illustrative of the point. That's the case we cited, Aref v. United States, which was a 2006 Second

Circuit case. Specifically, it arose in the mandamus context. But there the issue was whether or not someone could obtain a mandamus to stop an unconstitutional trial, alleging that the district court trial below infringed upon their due process, constitutional rights, as well as their Sixth Amendment rights. The Second Circuit said that any potential harms that would arise from having to go through the trial and then having to appeal would be remedied through the judicial review process and a reversal of the decision below. That's essentially all we're saying here, is that all that will happen to plaintiffs is they have to go through the process and then raise their claims. That itself is not an irreparable harm within the meaning of the case law.

Unless your Honor has any further questions on the irreparable harm prong --

THE COURT: No.

MS. VARGAS: Thank you.

THE COURT: Would you like to respond briefly?

MR. GUNTHER: Yes, your Honor. I will be brief.

To start, your Honor asked a question of the government who does appoint the ALJs. It is illustrative of the appointments clause issue. No answer was given. If you come to this courthouse and walk into the district judge's courtroom, you know exactly how your Honor got there. If you walk into the magistrate court, inferior officer for the United

states appointed by courts of law, we know how they got there. Bankruptcy court, same thing. How strange it is we're going to walk into a trial at the SEC and nobody is going to be able to explain how is it that the ALJ got there to preside. It really speaks to the erosion of responsibility and accountability and the diffusion of power within the agency at an unconstitutional level.

On irreparable harm, Statharos is not the only case in the Second Circuit that speaks of the presumption of an irreparable harm flowing from a constitutional violation. We cite also the Jolly case, which says -- and I'm quoting -- "presumption of irreparable injury flows from a violation of constitutional rights."

I don't know -- I have read very carefully my adversary's brief, and I don't know what line of Second Circuit law is being referred to. What I see there is a bunch of district court cases, mostly out of the Eastern District of New York, which have tried to carve out an exception from the rule I just read to your Honor for a certain class of cases that are remediable by basically the government just writing a check. But that's not where we're at. That's not the rule of this circuit. The only circuit cases I saw in response to the irreparable harm prong in my adversary's brief were cases from outside the Second Circuit. They cite a Third Circuit case and a First Circuit case that say maybe structural issues stand on

a different constitutional footing for purposes of irreparable harm. The problem there is not just they're in the wrong circuit, but those cases were decided before Free Enterprise. The government argued in Free Enterprise, hey, the Article II type structural arguments should not be on the same footing as other constitutional rights. Justice Roberts' opinion said, we see no authority for that. It is part of the Constitution like every other part. No different. And so it is here.

The issue about deference to the credibility findings of the ALJ is critically important here. The regulations that the SEC has promulgated speak of them deferring to credibility findings. It doesn't mean that they can't in an egregious case, like the circuit does after the district judge has made a clearly erroneous credibility finding, but there is an element of deference to it that's going to impact the way the Commission decides an appeal and then has a double impact if you get up to the circuit and the Commission has already passed on it that.

My adversaries kept trying to position this as, so what, we're just going to have a hearing, just like every other case where there is some objection being raised by the potential defendant. But the very objection we're raising is the constitutional structure of the proceeding that we have to sit through, and that makes it different from that someone just saying, I don't think the proceeding is going to, in an

as-applied way, provide me the due process I'm entitled to.

The other question that was asked by your Honor that had sort of a telling silence or a non-answer to it was when your Honor asked if I conclude that the SEC ALJ was an inferior officer of the United States, do plaintiffs win? Do you have any path escaping the plaintiffs win? I didn't hear any path, I didn't hear any answer to that question that leads to a different conclusion than what we said, which is likelihood of success is over. We win on the merits if your Honor concludes that way here.

I heard Freytag distinguished on the theory that the Supreme Court said that the special trial judges act as federal trial judges in the same manner as federal trial judges. You have to look at the SEC website. They say that's what their SEC ALJs do, they conduct bench trials in the manner of federal district court judges.

Quickly, there was a reference to the competitive service and the idea that the ALJs are members of the competitive service like the vast majority, as Justice Breyer put it, of all officers of United States. If you look at the dissent, Justice Breyer takes you through the Supreme Court's prior cases addressing that. And if you would have followed your analysis, you would have to demote the vast majority. That's Justice Breyer's language. Being in the competitive service or being in a particular classification of the civil

service doesn't mean you're not an officer of the United States. Most of them are.

And finally, your Honor, the idea that the Commission itself should be the arbiter here of a serious constitutional issue like this -- and perhaps they'll decide it soon -- as an answer to why your Honor shouldn't address it and this court shouldn't address it at this time is just completely inadequate. This is the mother court. This is the court that's existed before all other federal courts, and it's here to decide important constitutional questions that are brought within its jurisdiction. This claim is within your Honor's jurisdiction. It squarely presents an issue that shows this is a fundamental core structural constitutional defect in the SEC proceeding that Ms. Tilton faces. She shouldn't have to face it. And your Honor should, in the finest traditions of this court, enjoin the administrative proceeding.

Thank you, your Honor.

THE COURT: Thank you.

I want to thank the lawyers for their excellent advocacy both in the briefs and today.

I will reserve decision.

Have a nice afternoon.

(Adjourned)

EXHIBIT 5

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

CHARLES L. HILL, JR.,	:	
	:	
Plaintiff,	:	
	:	
v.	:	CIVIL ACTION NO.
	:	1:15-CV-1801-LMM
SECURITIES AND EXCHANGE COMMISSION,	:	
	:	
Defendant.	:	

ORDER

This case comes before the Court on Plaintiff Charles L. Hill, Jr.'s Motion for a Temporary Restraining Order, or in the Alternative, a Preliminary Injunction [2]. On May 19, 2015, Plaintiff filed this action in federal court, seeking to (1) declare an SEC administrative proceeding unconstitutional, and (2) enjoin the administrative proceeding from occurring until the Court issues its ruling. Plaintiff seeks a stay of the administrative proceeding prior to its June 15, 2015, scheduled evidentiary hearing to allow the parties to conduct limited discovery and brief the declaratory judgment claims. The Court heard oral argument on May 27, 2015. After a review of the record and due consideration, Plaintiff's Motion [2] is **GRANTED, in part** and **DENIED, in part** for the following reasons:

I. Background[1]

Plaintiff Charles L. Hill, Jr. is unregistered with the Securities and Exchange Commission ("SEC"). Am. Compl., Dkt. No. [17] ¶ 1. Plaintiff is a self-employed real estate developer. Id. ¶ 14. In June and July 2011, Plaintiff purchased and then sold a large quantity of Radiant Systems, Inc. ("Radiant") stock, making a profit of approximately $744,000. Id. ¶¶ 23-26. The SEC alleges that Plaintiff made these transactions because he received inside information about a future merger between Radiant and NCR Corporation. Id. ¶ 33.

Plaintiff contends he never received inside information and bought and sold stock based upon (1) his personal knowledge of and experience with Radiant's product and management, and (2) his stock broker's suggestion to sell. See id. ¶¶ 2, 14-28. Plaintiff argues that the SEC (1) does not have any direct evidence of insider trading, and (2) relies on a "speculative theory that Mr. Hill must have had access to inside information on Radiant merely on the timing and concentration of his purchases." Id. ¶¶ 29, 31.

The SEC conducted a "nearly two-year investigation" between March 2013 and February 2015. Id. ¶¶ 27, 30, 39. It took "12 examinations, issued at least 13 subpoenas for documents[,] and received tens of thousands of documents. . . ." Id. ¶ 30. On February 17, 2015, the SEC served Plaintiff with an Order Instituting Cease-And-Desist Proceedings ("OIP") under Section 21C of the Securities

[1] The following facts are drawn from the Amended Complaint unless otherwise indicated, and any fact finding is made solely for the purposes of this Motion.

Exchange Act of 1934 ("Exchange Act"), alleging he is liable for insider trading in violation of Section 14(e) of the Exchange Act and Rule 14e-3. Ex. 4, Dkt. No. [2-6]. The SEC seeks a cease-and-desist order, a civil penalty, and disgorgement. Id.

A. The Exchange Act

In 1990, through the Securities Enforcement Remedies and Penny Stock Reform Act, Pub. L. No. 101-429, 104 Stat. 931, 939 (1990), Congress first authorized the SEC to pursue "any person" for Exchange Act violations through an administrative cease-and-desist proceeding. See 15 U.S.C. § 78u-3. This proceeding allows the SEC to obtain an order enjoining violations of the Exchange Act. Id. In 2010, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), Pub. L. No. 111-203, 124 Stat. 1376 (2010), which authorized the SEC to seek civil monetary penalties from "any person"—both those registered and unregistered with the SEC—in an administrative hearing. See 15 U.S.C. § 78u-2.

Prior to the passage of Dodd-Frank in 2010, the SEC could not seek civil penalties from an unregistered individual like Plaintiff in an administrative proceeding; it could only have brought an administrative proceeding against "regulated person[s]" or companies. See Duka v. S.E.C., ___ F. Supp. 3d ___, No. 15 Civ. 357 (RMB) (SN), 2015 WL 1943245, at *2 (S.D.N.Y. Apr. 15, 2015) (citing Gupta v. S.E.C., 796 F. Supp. 2d 503, 507 (S.D.N.Y. 2011)). The earlier version of the statute allowed the SEC to pursue unregistered individuals like Plaintiff for civil penalties only in federal court where these individuals could invoke their

Seventh Amendment right to jury trial. In sum, the Exchange Act currently authorizes the SEC to initiate enforcement actions against "any person" suspected of violating the Act and gives the SEC the sole discretion to decide whether to bring an enforcement action in federal court or an administrative proceeding. See 15 U.S.C. §§ 78u(d), 78u-1, 78u-2, 78u-3.

B. SEC Administrative Process

The Administrative Procedure Act ("APA"), 5 U.S.C. § 500, *et seq.*, authorizes executive agencies, such as the SEC, to conduct administrative proceedings before an Administrative Law Judge ("ALJ"). SEC administrative proceedings vary greatly from federal court actions.

The Federal Rules of Civil Procedure and Evidence do not apply in SEC administrative proceedings. Instead, the SEC uses its own Rules of Practice. 17 C.F.R. § 201.100(a).[2] "[A]ny evidence 'that can conceivably throw any light upon the controversy, including hearsay, normally will be admitted in an administrative proceeding.'" Am. Compl., Dkt. No. [17] ¶ 53 (quoting In re Ochanpaugh, Exchange Act Release No. 54363, 2006 WL 2482466, at *6 n.29 (Aug. 25, 2006)) (internal quotations omitted). And respondents such as Plaintiff "are generally barred from taking depositions under Rules of Practice 233 and 234," and can "obtain documents only through the issuance of a Subpoena under

[2] However, the SEC could order an "alternative procedure" or refuse to enforce a rule if it determined "that to do so would serve the interests of justice and not result in prejudice to the parties to the proceeding." 17 C.F.R. § 201.100(c).

Rule of Practice 232." Am. Compl., Dkt. No. [17] ¶ 54; see also 17 C.F.R. §§ 201.232-234.

SEC administrative proceedings also occur much more quickly than federal court actions. Following an OIP's issuance, an evidentiary hearing must occur within four months. 17 C.F.R. § 201.360(a)(2).[3] The SEC also has discretion to hold the evidentiary hearing as soon as one month following the OIP. See id. Counterclaims are not permissible in administrative proceedings. Am. Compl. Dkt. No. [1] ¶ 56. And the Rules of Practice do not allow for the equivalent of 12(b) motions in federal court which test the allegations' sufficiency. Id. ¶ 57.

The SEC's Rules of Practice, 17 C.F.R. § 201.100, *et seq.*, provide that the SEC "shall" preside over all administrative proceedings whether by the Commissioners handling the matter themselves or delegating the case to an ALJ; there is no right to a jury trial. 17 C.F.R. § 201.110. When an ALJ is selected by the SEC to preside—as was done by the SEC in Plaintiff's case—the ALJ is selected by the Chief Administrative Law Judge. Id. The ALJ then presides over the matter (including the evidentiary hearing) and issues the initial decision. 17 C.F.R. § 201.360(a)(1). However, the SEC may on its own motion or at the request of a party order interlocutory review of any matter during the ALJ proceeding;

[3] The SEC or ALJ can enlarge any time limit for "good cause shown," but the SEC and ALJ are cautioned to "adhere to a policy of strongly disfavoring such requests, except in circumstances where the requesting party makes a strong showing that the denial of the request of motion would substantially prejudice their case." 17 C.F.R. § 201.161(a)-(b).

"[p]etitions by parties for interlocutory review are disfavored," though. 17 C.F.R. § 201.400(a).

The initial decision can be appealed by either the respondent or the SEC's Division of Enforcement, 17 C.F.R. § 201.410, or the SEC can review the matter "on its own initiative." 17 C.F.R. § 201.411(c). A decision is not final until the SEC issues it. If there is no appeal and the SEC elects not to review an initial order, the ALJ's decision is "deemed the action of the Commission," 15 U.S.C. § 78d-1(c), and the SEC issues an order making the ALJ's initial order final. 17 C.F.R. § 201.360(d)(2).

If the SEC grants review of the ALJ's initial decision, its review is essentially *de novo* and it can permit the submission of additional evidence. 17 C.F.R. §§ 201.411(a), 201.452. However, the SEC will accept the ALJ's "credibility finding, absent overwhelming evidence to the contrary." In re Clawson, Exchange Act Release No. 48143, 2003 WL 21539920, at *2 (July 9, 2003); In re Pelosi, Securities Act Release No. 3805, 2014 WL 1247415, at *2 (Mar. 27, 2014) ("The Commission gives considerable weight to the credibility determination of a law judge since it is based on hearing the witnesses' testimony and observing their demeanor. Such determinations can be overcome only where the record contains substantial evidence for doing so.") (footnote and internal quotation marks omitted).

If a majority of the participating Commissioners do not agree regarding the outcome, the ALJ's initial decision "shall be of no effect, and an order will be

issued in accordance with this result." 17 C.F.R. § 201.411(f). Otherwise, the SEC will issue a final order at the conclusion of its review.

If a respondent such as Plaintiff loses with the SEC, he may petition for review of the SEC's order in the federal court of appeals (either his home circuit or the D.C. Circuit). 15 U.S.C. § 78y(a)(1). Once the record is filed, the court of appeals then retains "exclusive" jurisdiction to "to affirm or modify and enforce or to set aside the order in whole or in part." 15 U.S.C. § 78y(a)(3). The SEC's findings of facts are "conclusive" "if supported by substantial evidence." 15 U.S.C. § 78y(a)(4). The court of appeals may also order additional evidence to be taken before the SEC and remand the action for the SEC to conduct an additional hearing with the new evidence. 15 U.S.C. § 78y(a)(5). The SEC then files its new findings of facts based on the additional evidence with the court of appeals which will be taken as conclusive if supported by substantial evidence. Id.

C. SEC ALJs

SEC ALJs are "not appointed by the President, the Courts, or the [SEC] Commissioners. Instead, they are hired by the SEC's Office of Administrative Law Judges, with input from the Chief Administrative Law Judge, human resource functions, and the Office of Personnel Management" ("OPM"). Am. Compl., Dkt. No. [17] ¶ 80; see also 5 C.F.R. § 930.204 ("An agency may appoint an individual to an administrative law judge position only with prior approval of OPM, except when it makes its selection from the list of eligibles provided by OPM. An administrative law judge receives a career appointment and is exempt

from the probationary period requirements under part 315 of this chapter."). An ALJ's salary is set by statute. 5 U.S.C. § 5372.

Congress has authorized the SEC to delegate any of its functions to an ALJ. 15 U.S.C. § 78d-1(a). Pursuant to that authority, the SEC has promulgated regulations, which set out its ALJ's powers. 17 C.F.R. § 200.14 makes ALJs responsible for the "fair and orderly conduct of [administrative] proceedings" and gives them the authority to: "(1) Administer oaths and affirmations; (2) Issue subpoenas; (3) Rule on offers of proof; (4) Examine witnesses; (5) Regulate the course of a hearing; (6) Hold pre-hearing conferences; (7) Rule upon motions; and (8) Unless waived by the parties, prepare an initial decision containing the conclusions as to the factual and legal issues presented, and issue an appropriate order." 17 C.F.R. § 200.14(a);[4] see also 17 C.F.R. § 200.30–9 (authorizing ALJs to make initial decisions).

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[4] The SEC Rules of Practice provide a similar list of powers for "hearing officers," or ALJs. 17 C.F.R. § 201.101(a)(5) ("(5) Hearing officer means an administrative law judge, a panel of Commissioners constituting less than a quorum of the Commission, an individual Commissioner, or any other person duly authorized to preside at a hearing"). 17 C.F.R. § 201.111 provides,

> The hearing officer shall have the authority to do all things necessary and appropriate to discharge his or her duties. No provision of these Rules of Practice shall be construed to limit the powers of the hearing officer provided by the Administrative Procedure Act, 5 U.S.C. 556, 557. The powers of the hearing officer include, but are not limited to, the following:
>
> (a) Administering oaths and affirmations;

(b) Issuing subpoenas authorized by law and revoking, quashing, or modifying any such subpoena;

(c) Receiving relevant evidence and ruling upon the admission of evidence and offers of proof;

(d) Regulating the course of a proceeding and the conduct of the parties and their counsel;

(e) Holding prehearing and other conferences as set forth in § 201.221 and requiring the attendance at any such conference of at least one representative of each party who has authority to negotiate concerning the resolution of issues in controversy;

(f) Recusing himself or herself upon motion made by a party or upon his or her own motion;

(g) Ordering, in his or her discretion, in a proceeding involving more than one respondent, that the interested division indicate, on the record, at least one day prior to the presentation of any evidence, each respondent against whom that evidence will be offered;

(h) Subject to any limitations set forth elsewhere in these Rules of Practice, considering and ruling upon all procedural and other motions, including a motion to correct a manifest error of fact in the initial decision. A motion to correct is properly filed under this Rule only if the basis for the motion is a patent misstatement of fact in the initial decision. Any motion to correct must be filed within ten days of the initial decision. A brief in opposition may be filed within five days of a motion to correct. The hearing officer shall have 20 days from the date of filing of any brief in opposition filed to rule on a motion to correct;

(i) Preparing an initial decision as provided in § 201.360;

(j) Upon notice to all parties, reopening any hearing prior to the filing of an initial decision therein, or, if no initial decision is to be filed, prior to the time fixed for the filing of final briefs with the Commission; and

D. Plaintiff's Administrative Proceeding

As stated supra, the SEC filed an OIP against Plaintiff on February 17, 2015. In the administrative proceeding, Plaintiff moved for summary disposition, asserting three constitutional arguments before the ALJ: (1) that the proceeding violates Article II of the Constitution because ALJs are protected by two layers of tenure protection; (2) that Congress's delegation of authority to the SEC to pursue cases before ALJs violates the delegation doctrine in Article I of the Constitution; and (3) that Congress violated his Seventh Amendment right to jury trial by allowing the SEC to pursue charges in an administrative proceeding. ALJ decision, Dkt. No. [2-4] at 2. ALJ James E. Grimes found on May 14, 2015, that he did not have the authority to address issues (2) and (3) and "doubt[ed] that [he had] the authority to address [] issue" (1). Id. at 7, 10-11. However, he did deny Plaintiff's Article II removal claim on the merits. Id.

Plaintiff's administrative evidentiary hearing is scheduled for June 15, 2015, before the ALJ. On May 19, 2015, Plaintiff filed his Complaint, asking this Court to (1) declare the administrative proceeding unconstitutional for the same reasons asserted in the administrative proceeding, and (2) enjoin the administrative proceeding from occurring until the Court can issue its ruling. The

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> (k) Informing the parties as to the availability of one or more alternative means of dispute resolution, and encouraging the use of such methods.

17 C.F.R. § 201.111.

Court heard oral argument on May 27, 2015. On May 29, 2015, Plaintiff amended his Complaint, adding a claim that the SEC ALJ's appointment violated the Appointments Clause of Article II as the ALJ is allegedly an inferior officer and he was not appointed by the President, the courts of law, or a department head. See U.S. Const. art. II, § 2, cl. 2. The Court allowed Plaintiff and the SEC to file supplemental briefs on this issue following the hearing. Dkt. No. [18].

The SEC opposes Plaintiff's Motion, arguing that (1) this Court does not have subject matter jurisdiction, and (2) even if it does, Plaintiff has failed to meet his burden under the preliminary injunction standard.

II. Discussion

A. Subject Matter Jurisdiction

The SEC first contends that this Court does not have subject matter jurisdiction because the administrative proceeding, with its eventual review from a court of appeals, has exclusive jurisdiction over Plaintiff's constitutional claims. In other words, the SEC contends that its election to pursue claims against Plaintiff in an administrative proceeding, "channels review of Plaintiff's claims through the Commission's administrative process, with review in the courts of appeals." Def. Br., Dkt. No. [12] at 18; see 15 U.S.C. § 78y; supra at ____ (explaining the administrative review procedure). The SEC thus argues that § 78y is now Plaintiff's exclusive judicial review channel, and this Court cannot consider Plaintiff's constitutional claims; judicial review can only come from the

courts of appeal following the administrative proceeding and the SEC's issuance of a final order in Plaintiff's case.

The SEC's position is in tension with 28 U.S.C. § 1331, which provides that federal district courts "have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States," and 28 U.S.C. § 2201, which authorizes declaratory judgments. "[I]t is established practice for [the Supreme] Court to sustain the jurisdiction of federal courts to issue injunctions to protect rights safeguarded by the Constitution." Bell v. Hood, 327 U.S. 678, 684 (1946); Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., 561 U.S. 477, 491 n.2 (2010). And "injunctive relief has long been recognized as the proper means for preventing entities from acting unconstitutionally." Corr. Servs. Corp. v. Malesko, 534 U.S. 61, 74 (2001); see also 5 U.S.C. § 702 (stating that under the Administrative Procedure Act, any "person suffering legal wrong because of agency action, or adversely affected or aggrieved by agency action within the meaning of a relevant statute, is entitled to judicial review thereof" and may seek injunctive relief).

To restrict the district court's statutory grant of jurisdiction under § 1331, there must be Congressional intent to do so. The Supreme Court has held that, "[p]rovisions for agency review do not restrict judicial review 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, 561 U.S. at 489 (quoting Thunder Basin Coal Co. v. Reich, 510 U.S. 200, 207, 212, 114 S.Ct. 771, 127 L.Ed.2d 29 (1994)).

At the hearing, the SEC argued that despite statutory language providing that these types of enforcement actions could be heard in *either* the district court *or* administrative proceedings, once the SEC selected the administrative forum, Plaintiff was bound by that decision and § 78y became the exclusive judicial review provision. The SEC contends that Congress declared its intent for the administrative proceeding to be the exclusive forum for judicial review for these cases by allowing the SEC to make the administrative proceeding its forum choice.

The Court finds, however, that Congress's purposeful language allowing *both* district court and administrative proceedings shows a different intent. Instead, the clear language of the statute provides a choice of forum, and there is no language indicating that the administrative proceeding was to be an exclusive forum. There can be no "fairly discernible" Congressional intent to limit jurisdiction away from district courts when the text of the statute provides the district court as a viable forum. The SEC cannot manufacture Congressional intent by making that choice for Congress; Congress must express its own intent within the language of the statute. Similarly, in Free Enterprise, the Supreme Court held that the text of § 78y—the provision at issue here—"does not expressly limit the jurisdiction that other statutes confer on district courts. See, e.g., 28 U.S.C. §§ 1331, 2201. Nor does it do so implicitly." 561 U.S. at 489.

Here, the Court finds that because Congress created a statutory scheme which expressly included the district court as a permissible forum for the SEC's claims, Congress did not intend to limit § 1331 and prevent Plaintiff from raising his collateral constitutional claims in the district court. Congress could not have intended the statutory review process to be exclusive because it expressly provided for district courts to adjudicate not only constitutional issues but Exchange Act violations, at the SEC's option. See Elgin v. Dep't of Treasury, ___ U.S. ___, 132 S. Ct. 2126, 2133 (2012) ("To determine whether it is 'fairly discernible' that Congress precluded district court jurisdiction over petitioners' claims, we examine the [the Exchange Act]'s text, structure, and purpose.").

But even if Congress's intent cannot be gleaned from Congress's purposeful choice to include the district court as a viable forum, the Court still finds that jurisdiction would be proper as Congress's intent can be presumed based on the standard articulated in Thunder Basin, Free Enterprise, and Elgin. A court may "presume that Congress does not intend to limit jurisdiction" if (1) "a finding of preclusion could foreclose all meaningful judicial review"; (2) "if the suit is wholly collateral to a statute's review provisions"; and if (3) "the claims are outside the agency's expertise." Free Enterprise, 561 U.S. at 489 (quoting Thunder Basin, 510 U.S. at 212-213) (internal quotations omitted). A discussion of these factors follows.

1. Barring Plaintiff's Claims Would Prevent Meaningful Judicial Review.

The SEC first argues that because Plaintiff has a "certain path" to judicial review through a court of appeals, Plaintiff cannot demonstrate he lacks meaningful judicial review. Def. Br., Dkt. No. [12] at 20. But the Court finds that requiring Plaintiff to pursue his constitutional claims following the SEC's administrative process "could foreclose all *meaningful* judicial review" of his constitutional claims. Free Enterprise, 561 U.S. at 489 (emphasis added) (quoting Thunder Basin, 510 U.S. at 212-213); see Duka, 2015 WL 1943245, at *5.

Plaintiff's claims go to the constitutionality of Congress's entire statutory scheme, and Plaintiff specifically seeks an order enjoining the SEC from pursuing him in its "unconstitutional" tribunals. If Plaintiff is required to raise his constitutional law claims following the administrative proceeding, he will be forced to endure what he contends is an unconstitutional process. Plaintiff could raise his constitutional arguments only after going through the process he contends is unconstitutional—and thus being inflicted with the ultimate harm Plaintiff alleges (that is, being forced to litigate in an unconstitutional forum). By that time, Plaintiff's claims would be moot and his remedies foreclosed because the Court of Appeals cannot enjoin a proceeding which has already occurred.

The SEC argues that Plaintiff's argument "boils down to the assertion that administrative respondents need not wait for actual adjudication of their cases in order to challenge their legality," and the Eleventh Circuit has "rejected precisely

this argument." See Def. Br., Dkt. No. [12] at 21 (quoting Chau v. U.S. S.E.C., ___ F. Supp. 3d ___, No. 14-CV-1903 LAK, 2014 WL 6984236, at *12 (S.D.N.Y. Dec. 11, 2014) (internal quotation marks omitted)); see also Def. Br., Dkt. No. [12] at 21 (citing Doe v. F.A.A., 432 F.3d 1259, 1263 (11th Cir. 2005)). However, this Court does not read those Eleventh Circuit decisions so broadly.

In Doe, thirteen aircraft mechanics sued the FAA, seeking a preliminary injunction "instructing the FAA how to proceed in its process of reexamination." 432 F.3d at 1260. An investigation revealed that the school where plaintiffs received their airmen certificates had fraudulently examined and certified some mechanics who were unqualified to hold the certification. Id. Because the FAA was unable to determine which certifications were fraudulent, the FAA wrote all relevant mechanics requiring them to recertify. Id. "The parties agreed that the FAA ha[d] the power to reexamine airmen and to suspend and revoke their certificates." Id. at 1262. But the plaintiffs sought and received an injunction on the basis that their due process rights would be violated by the FAA pursuing its administrative procedure.

The Eleventh Circuit reversed, finding that the Court did not have subject matter jurisdiction. The Court held that the mechanics' constitutional arguments were "inescapably intertwined" with the merits of an FAA order. Id. at 1263 ("The mechanics' constitutional claims (that the FAA has infringed upon their due process rights by failing to observe statutory and administrative processes) necessarily require a review of the procedures and actions taken by the FAA with

regard to the mechanics' certificates. Therefore, the constitutional claims fall within the ambit of the administrative scheme, and the district court is without subject-matter jurisdiction."); see also Green v. Brantley, 981 F.2d 514, 521 (11th Cir. 1993) (holding that the Circuit lacked subject matter jurisdiction because "the merits of [plaintiff's] claims are inescapably intertwined with a review of the procedures and merits surrounding the FAA's order."). The Court therefore held that "delayed judicial review (that is, review by a federal court of appeals after determination by the administrative commission rather than initial review by a federal district court)" was still meaningful in those circumstances. Doe, 432 F.3d at 1263.

The Court finds that Doe is distinguishable. The plaintiffs in Doe conceded the FAA had the authority to initiate administrative proceedings, but claimed that because the FAA had not yet initiated administrative proceedings against them, they were not required to go through the administrative process. Id. at 1262. The FAA did not have a forum selection decision, and the plaintiff conceded the FAA's ability to pursue reexamination. The Eleventh Circuit found that plaintiff's due process challenges were "inescapably intertwined" with the merits of the FAA's actions.

Here, Plaintiff's claims rise or fall regardless of what has occurred or will occur in the SEC administrative proceeding; Plaintiff does not challenge the SEC's conduct in that proceeding or the allegations against him—he challenges the proceeding *itself*. See Free Enterprise, 561 U.S. at 490 ("But petitioners object

to the Board's existence, not to any of its auditing standards."); Touche Ross & Co. v. SEC, 609 F.2d 570, 577 (2d Cir. 1979) ("While the Commission's administrative proceeding is not 'plainly beyond its jurisdiction,' nevertheless to require appellants to exhaust their administrative remedies would be to require them to submit to the very procedures which they are attacking.").

Plaintiff's claims here are not "inescapably intertwined" with the merits of the SEC's insider trading claims against him. Therefore, while the delayed judicial review in Doe was acceptable because the constitutional claims depended on how long the FAA took to complete an admittedly constitutional *process*, delayed judicial review here will cause an allegedly unconstitutional *process* to occur.

Waiting until the harm Plaintiff alleges cannot be remedied is not *meaningful* judicial review.[5] See LabMD, Inc. v. F.T.C., 776 F.3d 1275, 1280 (11th

[5] The cases the SEC cites from other districts on this issue can be distinguished from the facts here. Chau, Jarkesy v. S.E.C., 48 F. Supp. 3d 32 (D.D.C. 2014), and Altman v. U.S. S.E.C., 768 F. Supp. 2d 554 (S.D.N.Y. 2011), all addressed substantive challenges to the merits of the administrative proceedings. See Chau, 2014 WL 6984236 (challenging the SEC's conduct within the administrative proceeding, such as failing to postpone a hearing following a document dump); Jarkesy, 48 F. Supp. 3d at 32 (claiming that he could not obtain a fair hearing before the SEC because the SEC's settlements with two others stated that the plaintiff was liable for securities fraud); Altman, 768 F. Supp. 2d at 561 (involving a challenge to the SEC's own rules and stating that this was not a case where the plaintiff disputed the SEC had the expertise to hear challenges to its own rules and noted that the plaintiff did not challenge the "existence" of the proceeding but rather the "extent of the SEC's ability to sanction attorneys under the SEC's own rules").

Cir. 2015) ("We have consistently looked to how 'inescapably intertwined' the constitutional claims are to the agency proceeding, reasoning that the harder it is to distinguish them, the less prudent it is to interfere in an ongoing agency process.") (citing Doe, 432 F.3d at 1263; Green, 981 F.2d at 521). Therefore, the Court finds that § 78y does not provide meaningful judicial review under these circumstances.

2. Plaintiff's Claims Are Wholly Collateral to the SEC Proceeding.

The Court also notes that Chau's reasoning supports this Court's ruling. Specifically, The Chau court stated,

> There is an important distinction between a claim that an administrative scheme is unconstitutional in all instances—a facial challenge—and a claim that it violates a particular plaintiff's rights in light of the facts of a specific case—an as-applied challenge. As between the two, courts are more likely to sustain pre-enforcement jurisdiction over "broad facial and systematic challenges," such as the claim at issue in Free Enterprise Fund. This tendency is not a hard-and-fast rule, as "the distinction between facial and as-applied challenges is not so well defined that it has some automatic effect or that it must always control the pleadings and disposition in every case involving a constitutional challenge." Rather, it is a recognition that the Thunder Basin and Free Enterprise factors militate against jurisdiction when a pre-enforcement constitutional claim relates to factual issues that are the subject of a pending administrative adjudication.

Chau v. U.S. S.E.C., No. 14-CV-1903 LAK, 2014 WL 6984236, at *6 (S.D.N.Y. Dec. 11, 2014) (footnotes omitted) (quoting Elk Run Coal Co. v. Dep't of Labor, 804 F. Supp. 2d 8, 21 (D.D.C. 2011) (describing Free Enterprise as a "broad facial and systemic challenge"); Elgin, 132 S. Ct. at 2135 (explaining that the as-applied vs. facial distinction is not talismanic)).

The SEC also argues that Plaintiff's claims are not wholly collateral to the SEC proceeding because it is possible that Plaintiff may not be found liable in the administrative proceeding or he may eventually obtain relief on appeal. The SEC cites Elgin and argues that "Plaintiff's claims are not collateral to the statutory provisions governing review of SEC administrative proceedings because they are the means by which Plaintiff seeks to halt his SEC proceeding." Def. Br., Dkt. No. [12] at 22 (citing Elgin, 132 S. Ct. at 2139). But Elgin is distinguishable.

In Elgin, the plaintiffs had been terminated from their civil service jobs for failing to register for the selective service. Rather than appealing their terminations to the Merit Systems Protective Board or the Court of Appeals for the Federal Circuit, as required by the Civil Service Reform Act, plaintiffs filed an action in federal district court, claiming that their termination was unconstitutional. The Supreme Court ruled that the plaintiffs' claim was not "wholly collateral to the CSRA scheme," but was "a challenge to CSRA-covered employment action brought by CSRA-covered employees requesting relief that the CSRA routinely affords,"—i.e., reversal of employment decisions, reinstatement, and awarding back pay. Elgin, 132 S. Ct. at 2139-40 (internal quotation marks omitted).

Plaintiff is not challenging an agency decision; Plaintiff is challenging whether the SEC's ability to *make* that decision was constitutional. What occurs at the administrative proceeding and the SEC's conduct there is irrelevant to this proceeding which seeks to invalidate the entire statutory scheme. See Free

Enterprise, 561 U.S. at 490 ("But petitioners object to the Board's existence, not to any of its auditing standards."); Duka, 2015 WL 1943245, at *6; Gupta, 796 F. at 513 (noting the plaintiff would state a constitutional claim "even if [plaintiff] were entirely guilty of the charges made against him in the OIP"). Accordingly, Plaintiff's constitutional claims are wholly collateral to the administrative proceeding.

3. Plaintiff's Constitutional Claims Are Outside the Agency's Expertise.

The SEC claims that Plaintiff's challenges "fall within the Commission's expertise," and the "SEC is in the best position to interpret its own policies and regulations in the first instance." Dkt. No. [12] at 13. The Court finds that Plaintiff's Article I, Seventh Amendment, and Article II claims are outside the agency's expertise.[6]

Plaintiff's constitutional claims are governed by Supreme Court jurisprudence, and "the statutory questions involved do not require technical considerations of agency policy." Free Enterprise, 561 U.S. at 491 (alteration and internal quotations omitted) (quoting Johnson v. Robison, 415 U.S. 361, 373 (1974)); see also Thunder Basin, 510 U.S. at 215 ("[A]djudication of the constitutionality of congressional enactments has generally been thought beyond the jurisdiction of administrative agencies.") (quoting Johnson, 415 U.S. at 368). These claims are not part and parcel of an ordinary securities fraud case, and

[6] The SEC ALJ agrees with this conclusion. See ALJ decision, Ex. 2, Dkt. No. [2-4].

there is no evidence that (1) Plaintiff's constitutional claims are the type the SEC "routinely considers," or (2) the agency's expertise can be "brought to bear" on Plaintiff's claims as they were in Elgin. Elgin, 132 S. Ct. at 2140.

The Court finds that as to this factor, Plaintiff's constitutional claims are outside the SEC's expertise, and that this Court has subject matter jurisdiction.

B. Preliminary Injunction

To obtain a preliminary injunction, the moving party must demonstrate: (1) a substantial likelihood of success on the merits; (2) a substantial threat of irreparable injury if the injunction is not granted; (3) the threatened injury to the movant outweighs the damage to the opposing party; and (4) granting the injunction would not be adverse to the public interest. Four Seasons Hotels & Resorts, B.V. v. Consorcio Barr, S.A., 320 F.3d 1205, 1210 (11th Cir. 2003). "The preliminary injunction is an extraordinary and drastic remedy not to be granted unless the movant 'clearly carries the burden of persuasion' as to the four prerequisites." United States v. Jefferson Cnty., 720 F.2d 1511, 1519 (11th Cir. 1983) (quoting Canal Auth. v. Callaway, 489 F.2d 567, 573 (5th Cir. 1974)). The same factors apply to a temporary restraining order. Ingram v. Ault, 50 F.3d 898, 900 (11th Cir. 1995). The Court first analyzes whether Plaintiff has met his burden to demonstrate a substantial likelihood to succeed on the merits of each of his constitutional arguments.

1. Non-Delegation Doctrine

Plaintiff first argues that the Dodd-Frank Act violates Article I of the Constitution because it gives the SEC unfettered discretion to select its forum. As stated supra, prior to the Dodd-Frank Act, the SEC could not have brought an administrative proceeding seeking civil penalties against unregistered individuals such as Plaintiff. Now, the SEC may choose between two forums for violations: federal district court or an SEC administrative proceeding.[7] Plaintiff argues that the Dodd-Frank Act violates Article I of the Constitution because it "delegates decisionmaking authority to the Commission to bring an administrative proceeding for civil penalties against unregulated individuals . . . without any intelligible principle as to when the Commission is to bring an enforcement action against an unregulated individual in an administrative forum." Pl. Br., Dkt. No. [2-1] at 9.

Article I, § 1 of the U.S. Constitution vests, "[a]ll legislative Powers herein granted . . . in a Congress of the United States." Pursuant to the delegation doctrine, Congress may delegate this legislative decisionmaking power to agencies, but only if it "lay[s] down by legislative act an intelligible principle to which the person or body authorized to [act] is directed to conform." Whitman v. Am. Trucking Assocs., 531 U.S. 457, 472 (2001) (quoting J.W. Hampton Jr., & Co. v. United States, 276 U.S. 394, 409 (1928)). "Whether the statute delegates

[7] At the hearing, the SEC noted that available penalties vary slightly based on choice of forum. Hr'g Tr., Dkt. No. [19] at 99:4-7 (noting that treble damages are only available in federal court and not in an administrative proceeding).

legislative power is a question for the courts, and an agency's voluntary self-denial has no bearing upon the answer." Whitman, 531 U.S. at 473. Exercise of legislative power depends not on form but upon "whether [the actions] contain matter which is properly to be regarded as legislative in its character and effect." I.N.S. v. Chadha, 462 U.S. 919, 952 (1983) (quoting S. Rep. No. 1335, 54th Cong., 2d Sess., 8 (1897)).

The SEC contends that the non-delegation doctrine is inapplicable because the "Executive [Branch] does not act in a legislative capacity by selecting the forum in which to enforce a law; that authority is a part of the Executive power itself." Def. Br., Dkt. No. [12] at 24; see also U.S. Const. art. II, § 3 (stating the Executive "shall take Care that the Laws be faithfully executed"). The SEC argues that its forum selection decision is no different from any other decision made by prosecutors, and courts consistently reject non-delegation challenges to prosecutorial-discretion-related decisions. See United States v. Batchelder, 442 U.S. 114, 126 (1979) (rejecting a non-delegation challenge where "the power that Congress has delegated to those officials is no broader than the authority they routinely exercise in enforcing the criminal laws."); United States v. I.D.P., 102 F.3d 507, 511 (11th Cir. 1996) (noting that the Government's "authority to decide whether to prosecute a case in a federal forum [is the] type of decision [that] falls squarely within the parameters of prosecutorial discretion . . . ."). This Court agrees.

In Batchelder, the Supreme Court was asked to resolve whether the Government's "unfettered" prosecutorial discretion to decide between two identical statutes except for their penalty provisions was constitutional, when one statute had a much higher sentencing range. 442 U.S. at 116-17, 125. The defendant had been convicted under the statute with the higher penalty, and the defendant challenged Congress's delegation of authority to prosecutors to (1) decide between the statutes, and (2) thus choose a higher sentencing range for identical conduct. The court of appeals had remanded the case to the district court for resentencing, finding that the defendant could only be subject to the maximum sentence under the statute with the lower penalty. The court of appeals found that the "prosecutor's power to select one of two statutes that are identical except for their penalty provisions implicated important constitutional protections." 442 U.S. at 117 (internal quotations omitted).

The Supreme Court reversed, finding that there is a "settled rule" in prosecutorial choice, 442 U.S. at 124, and "[m]ore importantly, there is no appreciable difference between the discretion a prosecutor exercises when deciding whether to charge under one of two statutes with different elements and the discretion he exercises when choosing one of two statutes with identical elements." 442 U.S. at 125. "Just as a defendant has no constitutional right to elect which of two applicable federal statutes shall be the basis of his indictment and prosecution neither is he entitled to choose the penalty scheme under which

he will be sentenced." Id. The Court specifically rejected defendant's delegation argument, finding that:

> [t]he provisions at issue plainly demarcate the range of penalties that prosecutors and judges may seek to impose. In light of that specificity, the power that Congress has delegated to those officials is no broader than the authority they routinely exercise in enforcing the criminal laws. Having informed the courts, prosecutors, and defendants of the permissible punishment alternatives available under each Title, Congress has fulfilled its duty.

442 U.S. at 126.

The Court finds that this case is similar to Batchelder. Just as the Supreme Court held that the defendant in Batchelder could not choose the statute of his indictment, Plaintiff here may not choose his forum when Congress has dedicated that decision to the Executive. See United States v. Allen, 160 F.3d 1096, 1108 (6th Cir. 1998) (rejecting defendant's "attempt to end-run the doctrine of prosecutorial discretion" by arguing the prosecutor's charging decision violated the non-delegation doctrine); see also Whitman, 531 U.S. at 474-475 ("In short, we have almost never felt qualified to second-guess Congress regarding the permissible degree of policy judgment that can be left to those executing or applying the law.") (internal quotations omitted). When the SEC makes its forum selection decision, it is acting under executive authority and exercising prosecutorial discretion. See Chadha, 462 U.S. at 951 ("When the Executive acts, it presumptively acts in an executive or administrative capacity as defined in Art. II.").

Plaintiff argues that unlike Batchelder, where the Supreme Court found that Congress set out clear parameters as to the possible punishments, Dodd-Frank does not provide the SEC any criteria to make its forum selection decision. Pl. Reply, Dkt. No. [13] at 12-13. However, just as the prosecutor was allowed to select between two statutes which prevented identical conduct but provided different possible penalties in Batchelder, the Court finds that the SEC may select between two statutes which allow for different forum choices. The statutes in Batchelder did not tell the prosecutor what factors to consider in making his decision between the statutes, and the effect of the prosecutor's decision in Batchelder was equally paramount to Plaintiff's claims here—the defendant there would spend more time incarcerated if the prosecutor selected the higher penalty statute.

Congress has advised the SEC through the enactment of specific statutes as to what conduct may be pursued in each forum. It is for the enforcement agency to decide where to bring that claim under its exercise of executive power. Because the SEC has been made aware of the permissible forums available under each statute, "Congress has fulfilled its duty." Batchelder, 442 U.S. at 126.

Plaintiff also argues that the SEC's forum decision is an improper exercise of legislative power. Specifically, the SEC contends that "by virtue of the Act, the SEC received additional power from Congress to alter the rights, duties, and legal relations of individuals," and that under Chadha, this action constituted legislative action not executive action. Pl. Reply, Dkt. No. [13] at 10-11.

In Chadha, the Supreme Court found that the one-House veto provision was unconstitutional, but it did so without using the non-delegation doctrine. 462 U.S. at 959. In invalidating the statute, the Supreme Court first noted the presumption that "[w]hen any Branch acts, it is presumptively exercising the power the Constitution has delegated to it." Id. at 951. Beginning with that presumption, the Court held that the one-House veto was legislative in effect because "[i]n purporting to exercise power defined in Art. I, § 8, cl. 4 to 'establish an uniform Rule of Naturalization,' the House took action that had the purpose and effect of altering the **legal rights, duties, and relations of persons**, including the Attorney General, Executive Branch officials and Chadha, all outside the legislative branch." Id. at 952 (emphasis added). Plaintiff seizes on the bolded language above to claim that because the SEC's forum selection decision affects him—specifically, his ability to assert his 7th Amendment rights—the SEC has been delegated legislative authority.

The Court does not agree with Plaintiff's reading of Chadha. Instead, Chadha stands for the basic proposition that when *Congress* acts pursuant to its Article I powers, the action is legislative. If Plaintiff's broad reading were true as to actions of the executive branch, that would mean any SEC decision which affected a person's "legal rights, duties, and relations of persons"—to include charging decisions which the Supreme Court has held involve prosecutorial discretion, see Batchelder, 442 U.S. at 124 —would be legislative actions. See Chadha, 462 U.S. at 953 n.16 (noting that when the head of an executive agency

performs his duties pursuant to statute, "he does not exercise 'legislative' power.") (citing Ernst & Ernst v. Hochfelder, 425 U.S. 185, 213-214 (1976)).

Plaintiff's reading does not comport with the Executive's constitutional role in faithfully executing the laws. Because Congress has properly delegated power to the executive branch to make the forum choice for the underlying SEC enforcement action, the Court finds that the Plaintiff cannot prove a substantial likelihood of success on the merits on his non-delegation claim.

2. Seventh Amendment

Plaintiff next argues that the SEC's decision to prosecute the claims against him in the administrative proceeding rather than the district court violates his Seventh Amendment right to a jury trial. Pl. Br., Dkt. No. [2-1] at 15. The Seventh Amendment provides, "[i]n Suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved . . . ." "The phrase 'Suits at common law' has been construed to refer to cases tried prior to the adoption of the Seventh Amendment in courts of law in which jury trial was customary as distinguished from courts of equity or admiralty in which jury trial was not." Atlas Roofing Co. v. Occupational Safety & Health Review Comm'n, 430 U.S. 442, 449 (1977) (citing Parsons v. Bedford, 3 Pet. 433, 7 L.Ed. 732 (1830)). "[T]he Seventh Amendment also applies to actions brought to enforce statutory rights that are analogous to common-law causes of action ordinarily decided in English law courts in the late 18th century, as opposed to those customarily heard

by courts of equity or admiralty." Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 42 (1989) (citing Curtis v. Loether, 415 U.S. 189, 193 (1974)).

> The form of [the Court's] analysis is familiar. "First, we compare the statutory action to 18th-century actions brought in the courts of England prior to the merger of the courts of law and equity. Second, we examine the remedy sought and determine whether it is legal or equitable in nature." Tull v. United States, 481 U.S. 412, 417–418 (1987) (citations omitted). The second stage of this analysis is more important than the first. Id., at 421. If, on balance, these two factors indicate that a party is entitled to a jury trial under the Seventh Amendment, we must decide whether Congress may assign and has assigned resolution of the relevant claim to a non-Article III adjudicative body that does not use a jury as factfinder.

Granfinanciera, 492 U.S. at 42.

The SEC does not dispute Plaintiff's argument that an enforcement action for civil penalties is "clearly analogous to the 18th-century action in debt," Tull, 481 U.S. at 420, and this remedy is legal in nature. See Tull, 481 U.S. at 422 ("A civil penalty was a type of remedy at common law that could only be enforced in courts of law. Remedies intended to punish culpable individuals, as opposed to those intended simply to extract compensation or restore the status quo, were issued by courts of law, not courts of equity.").

Rather, the SEC contends that "Plaintiff's claim fails because it is firmly established that Congress 'may assign th[e] adjudication' of cases involving so-called 'public rights' to 'an administrative agency with which a jury trial would be incompatible[] without violating the Seventh Amendment[] . . . even if the Seventh Amendment would have required a jury where the adjudication of those rights is assigned instead to a federal court of law.'" Def. Br., Dkt. No. [12] at 26

(alteration in the original) (quoting Atlas Roofing, 430 U.S. at 455). This Court agrees.

"Public rights" cases are those which "arise between the Government and persons subject to its authority 'in connection with the performance of the constitutional functions of the executive or legislative departments.'" Atlas Roofing, 430 U.S. at 457 (internal quotation omitted) (quoting Crowell v. Benson, 285 U.S. 22, 31 (1932)). Plaintiff does not dispute that this SEC enforcement action involves a public right. See Pl. Reply, Dkt. No. [13] at 19-20. Because the SEC is acting as a sovereign in the performance of its executive duties when it pursues an enforcement action, the Court also agrees that this is a public rights case.

Despite this being a public rights case, Plaintiff argues that Congress must make the decision as to whether or not a new cause of action will contain a right to a jury trial when Congress originally creates the cause of action. That is, Plaintiff contends that the Seventh Amendment right can only be taken away at the time Congress is creating the "*new* public right." Id. at 17-21 (emphasis added). Plaintiff seizes on language from Atlas Roofing and Granfinanciera that the public right must be "new" or "novel," to be excluded from the Seventh Amendment's protections. See Atlas Roofing, 430 U.S. at 455 ("[W]hen Congress creates *new* statutory 'public rights,' it may assign their adjudication to an administrative agency with which a jury trial would be incompatible, without violating the Seventh Amendment's injunction that jury trial is to be 'preserved'

in 'suits at common law.'") (emphasis added); Granfinanciera, 492 U.S. at 51 ("Congress may devise *novel* causes of action involving public rights free from the strictures of the Seventh Amendment if it assigns their adjudication to tribunals without statutory authority to employ juries as factfinders.") (emphasis added). This Court disagrees.

Plaintiff's argument puts form over substance and defines "new" in a way that the Supreme Court did not intend. See Tull, 481 U.S. at 418 n.4 ("[T]he Seventh Amendment is not applicable to administrative proceedings."). Plaintiff's position is that Congress could have sent all enforcement actions for unregistered persons to an administrative proceeding at the time the original statute was drafted—because at that time, the public right was "new." But once it decided unregistered persons such as Plaintiff would get a jury trial, as it initially did in the Exchange Act, Plaintiff became "vested" with a Seventh Amendment right that Congress is now powerless to remove.

The Court does not find Plaintiff's argument persuasive. In Atlas Roofing, the Supreme Court stated, the "Government could commit the enforcement of statutes and the imposition and collection of fines to the judiciary, in which event jury trial would be required . . . , but [] the United States could also validly opt for administrative enforcement, without judicial trials." 430 U.S. at 460 (internal citation omitted). For cases involving public rights, Congress has the choice as to whether or not a jury trial will be required. Congress does not tie its hands when it initially creates a cause of action. Plaintiff cites no authority which specifically

holds that Congress may not change its mind and reassign *public rights* to administrative proceedings.[8]

As the Supreme Court has stated,

> The point is that the Seventh Amendment was never intended to establish the jury as the exclusive mechanism for factfinding in civil cases. It took the existing legal order as it found it, and there is little or no basis for concluding that the Amendment should now be interpreted to provide an impenetrable barrier to administrative factfinding under otherwise valid federal regulatory statutes. We cannot conclude that the Amendment rendered Congress powerless when it concluded that remedies available in courts of law were inadequate to cope with a problem within Congress' power to regulate to create new public rights and remedies by statute and commit their enforcement, if it chose, to a tribunal other than a court of law such as an administrative agency in which facts are not found by juries.

Atlas Roofing, 430 U.S. at 460.

In enacting Dodd-Frank, Congress specifically noted that it was doing so in response to the financial crisis. Dodd-Frank Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) (stating the statute was enacted "[t]o promote the financial stability of the United States by improving accountability and transparency in the financial system, to end 'too big to fail', to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices . . . ."). Congress thus decided that to carry out its mission to "clean up" the financial

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[8] Plaintiff argues under Granfinanciera that Congress may not reclassify or relabel a cause of action to avoid the Seventh Amendment. See Pl. Reply, Dkt. No. [13] at 18. However, Granfinanciera involved Congress relabeling a *private* right—to which the Seventh Amendment always attaches, see Atlas Roofing, 430 U.S. at 458—to create a supposed *public right*. See Granfinanciera, 492 U.S. at 60-61. It is undisputed that even the pre-Dodd-Frank claim involved a public right.

system, it would allow the SEC to bring actions in administrative proceedings "to administrative agencies with special competence in the relevant field." Atlas Roofing, 430 U.S. at 455. Congress found that the prior scheme was not working, and it redrafted the legislation. Because the legislation related to public rights, the Seventh Amendment does not prevent Congress from doing so. See Atlas Roofing, 430 U.S. at 460; id. at 461 ("Congress found the common-law and other existing remedies for work injuries resulting from unsafe working conditions to be inadequate to protect the Nation's working men and women. It created a new cause of action, and remedies therefor, unknown to the common law, and placed their enforcement in a tribunal supplying speedy and expert resolutions of the issues involved. The Seventh Amendment is no bar to the creation of new rights or to their enforcement outside the regular courts of law."). The Court finds that Plaintiff cannot prove a substantial likelihood of success on the merits on his Seventh Amendment claim as this claim involves a public right, and Congress has the right to send public rights cases to administrative proceedings.

3. Article II

Plaintiff next brings two claims under Article II of the Constitution: (1) that the ALJ's appointment violates the Appointments Clause of Article II because he was not appointed by the President, a court of law, or a department head, and (2) the ALJ's two-layer tenure protection violates the Constitution's separation of powers, specifically the President's ability to exercise Executive power over his inferior officers. Both of Plaintiff's arguments depend on this Court finding that

the ALJ is an inferior officer who would trigger these constitutional protections. See U.S. Const. art. II § 2, cl. 2; Freytag v. Comm'r of Internal Revenue, 501 U.S. 868, 880 (1991); Free Enterprise, 561 U.S. at 484, 506. Therefore, the Court will consider this threshold issue first.

a. Inferior Officer

The issue of whether the SEC ALJ is an inferior officer or employee for purposes of the Appointments Clause depends on the authority he has in conducting administrative proceedings. The Appointments Clause of Article II of the Constitution provides:

> [The President] 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.

U.S. Const. art. II, § 2, cl. 2. The Appointments Clause thus creates two classes of officers: principal officers, who are selected by the President with the advice and consent of the Senate, and inferior officers, whom "Congress may allow to be appointed by the President alone, by the heads of departments, or by the Judiciary." Buckley v. Valeo, 424 U.S. 1, 132 (1976). The Appointments Clause applies to all agency officers including those whose functions are "predominately quasi judicial and quasi legislative" and regardless of whether the agency officers

are "independent of the Executive in their day-to-day operations." Id. at 133 (quoting Humphrey's Executor v. United States, 295 U.S. 602, 625-26 (1935)).

"[A]ny appointee exercising significant authority pursuant to the laws of the United States is an 'Officer of the United States,' and must, therefore, be appointed in the manner prescribed by § 2, cl. 2, of [Article II]." Freytag, 501 U.S. at 881 (quoting Buckley, 424 U.S. at 126) (alteration in the original). By way of example, the Supreme "Court has held that district-court clerks, thousands of clerks within the Treasury and Interior Departments, an assistant surgeon, a cadet-engineer, election monitors, federal marshals, military judges, Article I [Tax Court special trial] judges, and the general counsel for the Transportation Department are inferior officers." Kent Barnett, Resolving the ALJ Quandary, 66 Vand. L. Rev. 797, 812 (2013) (citing Free Enterprise, 561 U.S. at 540 (Breyer, J., dissenting) (citing cases)).

Plaintiff claims that SEC ALJs are inferior officers because they exercise "significant authority pursuant to the laws of the Unites States" while the SEC contends ALJs are "mere employees" based upon Congress's treatment of them and the fact that they cannot issue final orders and do not have contempt power,[9] *inter alia*. The Court finds that based upon the Supreme Court's holding in Freytag, SEC ALJs are inferior officers. See also Duka, 2015 WL 1943245, at *8

[9] ALJs can find people in contempt, but cannot compel compliance with their order. See 17 C.F.R. § 201.180 (noting an ALJ can punish "[c]ontemptuous conduct"); Def. Br., Dkt. No. [12] at 24 (stating ALJs lack "contempt power" and stating an ALJ cannot compel compliance with any subpoenas he issues).

("The Supreme Court's decision in Freytag v. Commissioner, 501 U.S. 868, 111 (1991), which held that a Special Trial Judge of the Tax Court was an 'inferior officer' under Article II, would appear to support the conclusion that SEC ALJs are also inferior officers.").

In Freytag, the Supreme Court was asked to decide whether special trial judges ("STJ") in the Tax Court were inferior officers under Article II. 501 U.S. at 880. The Government argued, much as the SEC does here, that STJs do "no more than assist the Tax Court judge in taking the evidence and preparing the proposed findings and opinion," id., and they "lack authority to enter a final decision." Id. at 881; see also Def. Br., Dkt. No. [12] at 30-33 (arguing that SEC ALJs are not inferior officers because they cannot enter final orders and are subject to the SEC's "plenary authority"). The Supreme Court rejected that argument, stating that the Government's argument

> ignores the significance of the duties and discretion that special trial judges possess. The office of special trial judge is "established by Law," Art. II, § 2, cl. 2, and the duties, salary, and means of appointment for that office are specified by statute. See Burnap v. United States, 252 U.S. 512, 516–517 (1920); United States v. Germaine, 99 U.S. 508, 511–512 (1879). These characteristics distinguish special trial judges from special masters, who are hired by Article III courts on a temporary, episodic basis, whose positions are not established by law, and whose duties and functions are not delineated in a statute. Furthermore, special trial judges perform more than ministerial tasks. They take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders. In the course of carrying out these important functions, the special trial judges exercise significant discretion.

Freytag, 501 U.S. at 881-82.

The Court finds that like the STJs in Freytag, SEC ALJs exercise "significant authority." The office of an SEC ALJ is established by law, and the "duties, salary, and means of appointment for that office are specified by statute." Id.; see supra (setting out the ALJ system, to include the establishment of ALJs and their duties, salary, and means of appointment). ALJs are permanent employees—unlike special masters—and they take testimony, conduct trial, rule on the admissibility of evidence, and can issue sanctions, up to and including excluding people (including attorneys) from hearings and entering default. 17 C.F.R. §§ 200.14 (powers); 201.180 (sanctions).

Relying on Landry v. Federal Deposit Insurance Corp., 204 F.3d 1125 (D.C. Cir. 2000), the SEC argues that unlike the STJs who were inferior officers in Freytag, the SEC ALJs do not have contempt power and cannot issue final orders,[10] as the STJs could in limited circumstances. In Landry, the D.C. Circuit considered whether FDIC ALJs were inferior officers. The D.C. Circuit found FDIC ALJs, like the STJs, were established by law; their duties, salary, and means of appointment were specified by statute; and they conduct trials, take testimony,

[10] Plaintiff argues that SEC ALJ's can issue final orders because if the respondent does not petition the SEC to review the ALJ's initial order and the SEC does not decide to review the matter on its own, the action of the ALJ will be "deemed the action of the Commission." 15 U.S.C. § 78d-1(c). The SEC argues that the SEC retains plenary authority over ALJs and the regulations make clear that only when the SEC itself issues an order does the decision become final. Def. Br., Dkt. No. [24] at 2-3 (citing 17 C.F.R. § 201.360(d)(2)). This Court agrees with the SEC. Because the regulations specify that the SEC itself must issue the final order essentially "confirming" the initial order, the Court finds that SEC ALJs do not have final order authority.

rule on evidence admissibility, and enforce discovery compliance. 204 F.3d at 1133-34. And it recognized that Freytag found that those powers constituted the exercise of "significant discretion . . . a magic phrase under the Buckley test." Id. at 1134 (internal citation omitted).

Despite the similarities of the STJs and the FDIC ALJs, the Landry court applied Freytag as holding that whether the entity had the authority to render a final decision was a dispositive factor. According to the D.C. Circuit, Freytag "noted that [(1)] STJs have the authority to render the *final* decision of the Tax Court in declaratory judgment proceedings and in certain small-amount tax cases," and (2) the "Tax Court was required to defer to the STJ's factual and credibility findings unless they were clearly erroneous." Landry, 204 F.3d at 1133 (emphasis in original). While recognizing that the Freytag court "introduced mention of the STJ's power to render final decisions with something of a shrug," Landry held that FDIC ALJ's were not inferior officers because did not have the "power of final decision in certain classes of cases." Id. at 1134.

The concurrence rejected the majority's reasoning, finding that Freytag "cannot be distinguished" because "[t]here are no relevant differences between the ALJ in this case and the [STJ] in Freytag." Id. at 1140, 1141. After first explaining that the Supreme Court actually found the Tax Court's deference to the STJ's credibility findings was irrelevant to its analysis,[11] the concurrence

[11] The Supreme Court stated that Tax Court Rule 183, which established the deferential standard, was "not relevant to [its] grant of certiorari," and noted that

stated that the majority's "first distinction of Freytag is thus no distinction at all." Id. at 1142. The concurrence also noted that the majority's holding in Landry (which ultimately relied on the FDIC ALJ's lack of final order authority) was based on an *alternative* holding from Freytag as the Supreme Court had already determined the STJs were inferior officers before it analyzed the final order authority issue. Landry, 204 F.3d at 1142.

Similarly, this Court concludes that the Supreme Court in Freytag found that the STJs powers—which are nearly identical to the SEC ALJs here—were independently sufficient to find that STJs were inferior officers. See also Butz v. Economou, 438 U.S. 478, 513 (1978) ("There can be little doubt that the role of the . . . administrative law judge . . . is ' functionally comparable' to that of a judge. His powers are often, if not generally, comparable to those of a trial judge: He may issue subpoenas, rule on proffers of evidence, regulate the course of the hearing, and make or recommend decisions."); see also Edmond v. United States, 520 U.S. 651, 663 (1997) ("[W]e think it evident that 'inferior officers' are officers whose work is directed and supervised at some level by others who were appointed by Presidential nomination with the advice and consent of the Senate."). Only after it concluded STJs were inferior officers did Freytag address the STJ's ability to issue a final order; the STJ's limited authority to issue final orders was only an additional reason, not *the* reason. Therefore, the Court finds

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it would say no more about the rule than to say that the STJ did not have final authority to decide Petitioner's case. Freytag, 501 U.S. at 874 n.3; see also Landry, 204 F.3d at 1142 (Randolph, J., concurring).

that Freytag mandates a finding that the SEC ALJs exercise "significant authority" and are thus inferior officers.

The SEC also argues that this Court should defer to Congress's apparent determination that ALJs are inferior officers. In the SEC's view, Congress is presumed to know about the Appointments Clause, and it decided to have ALJs appointed through OPM and subject to the civil service system; thus, Congress intended for ALJs to be employees according to the SEC. See Def. Br. [12] at 33-37. But "[t]he Appointments Clause prevents Congress from dispensing power too freely; it limits the universe of eligible recipients of the power to appoint." Freytag, 501 U.S. at 880. Congress may not "decide" an ALJ is an employee, but then give him the powers of an inferior officer; that would defeat the separation-of-powers protections the Clause was enacted to protect. The Court finds that SEC ALJs are inferior officers.

b. Appointments Clause Violation

Because SEC ALJs are inferior officers, the Court finds Plaintiff has established a likelihood of success on the merits on his Appointments Clause claim. Inferior officers must be appointed by the President, department heads, or courts of law. U.S. Const. art. II § 2, cl. 2. Otherwise, their appointment violates the Appointments Clause.

The SEC concedes that Plaintiff's ALJ, James E. Grimes, was not appointed by an SEC Commissioner. See Def. Br., Dkt. No. [15] at 2; see also Free Enterprise, 561 U.S. at 511-512 (finding that the SEC Commissioners jointly

constitute the "head" of the SEC for appointment purposes). The SEC ALJ was not appointed by the President, a department head, or the Judiciary. Because he was not appropriately appointed pursuant to Article II, his appointment is likely unconstitutional in violation of the Appointments Clause.[12]

4. Remaining Preliminary Injunction Factors

The Court finds that Plaintiff has also satisfied the remaining preliminary injunction factors. First, Plaintiff will be irreparably harmed if this injunction does not issue because if the SEC is not enjoined, Plaintiff will be subject to an unconstitutional administrative proceeding, and he would not be able to recover monetary damages for this harm because the SEC has sovereign immunity. See Odebrecht Const., Inc. v. Sec'y, Fla. Dep't of Transp., 715 F.3d 1268, 1289 (11th Cir. 2013) ("In the context of preliminary injunctions, numerous courts have held that the inability to recover monetary damages because of sovereign immunity renders the harm suffered irreparable.") (collecting cases); see also Cunningham v. Adams, 808 F.2d 815, 821 (11th Cir. 1987) ("An injury is 'irreparable' only if it cannot be undone through monetary remedies."). If the administrative proceeding is not enjoined, Plaintiff's requested relief here would also become

[12] Because the Court finds Plaintiff can establish a likelihood of success on his Appointments Clause claim, the Court declines to decide at this time whether the ALJ's two-layer tenure protections also violate Article II's removal protections. However, the Court has serious doubts that it does, as ALJs likely occupy "quasi-judicial" or "adjudicatory" positions, and thus these two-layer protections likely do not interfere with the President's ability to perform his duties. See Duka, 2015 WL 1943245, at *8-10; see also Humphrey's Executor, 295 U.S. at 628-29, 631-32.

moot as the Court of Appeals would not be able to enjoin a proceeding which has already occurred. See supra at 15, 18-19 (explaining Plaintiff's harm).

Second, the Court finds that the public interest and the balance of equities are in Plaintiff's favor. The public has an interest in assuring that citizens are not subject to unconstitutional treatment by the Government, and there is no evidence the SEC would be prejudiced by a brief delay to allow this Court to fully address Plaintiff's claims. The SEC claims that the public interest weighs in its favor because the SEC is charged with "protect[ing] investors and maintain[ing] the integrity of the securities markets." Def. Br., Dkt. No. [12] at 44 (citing Duka, 2015 WL 1943245, at *7 n.13). But the Court does not find that it is ever in the public interest for the Constitution to be violated. The Supreme Court has held that the Appointments Clause "not only guards against [separation-of-powers] encroachment but also preserves another aspect of the Constitution's structural integrity by preventing the diffusion of the appointment power." Freytag, 501 U.S. at 878. Both are important to the public interest. The Court further notes that the SEC is not foreclosed from pursing Plaintiff in federal court or in an administrative proceeding before an SEC Commissioner, and thus any small harm which it might face could be easily cured by the SEC itself.

III. Conclusion

Because the Court finds Plaintiff has proved a substantial likelihood of success on the merits of his claim that the SEC has violated the Appointments Clause as well as the other factors necessary for the grant of a preliminary

injunction, the Court finds a preliminary injunction is appropriate to enjoin the SEC administrative proceeding and to allow the Court sufficient time to consider this matter on the merits.

The Court notes that this conclusion may seem unduly technical, as the ALJ's appointment could easily be cured by having the SEC Commissioners issue an appointment or preside over the matter themselves. However, the Supreme Court has stressed that the Appointments Clause guards Congressional encroachment on the Executive and "preserves the Constitution's structural integrity by preventing the diffusion of appointment power." Freytag, 501 U.S. at 878. This issue is "neither frivolous or disingenuous." Id. at 879. The Article II Appointments Clause is contained in the text of the Constitution and is an important part of the Constitution's separation of powers framework.

In addition, the Appointments Clause may not be waived, not even by the Executive. Id. at 880 ("Neither Congress nor the Executive can agree to waive this structural protection."). As this likely Appointment Clause violation "goes to the validity of the [administrative] proceeding that is the basis for this litigation," id. at 879, it is hereby **ORDERED** that Defendant, the Securities and Exchange Commission, is preliminarily enjoined from conducting the administrative proceeding brought against Plaintiff, captioned In the Matter of Charles L. Hill, Jr., Administrative Proceeding File No. 3-16383 (Feb. 11, 2015), including the hearing scheduled for June 15, 2015, before an Administrative Law Judge who has not been appointed by the head of the Department. This order shall remain in

effect until it is further modified by this Court or until resolution of Plaintiff's claim for permanent injunctive relief, whichever comes first.

The parties are **DIRECTED** to confer on a timetable for conducting discovery and briefing the remaining issues. The parties are then **DIRECTED** to submit by June 15, 2015, a consent scheduling order to the Court for consideration. If the parties are unable to agree to the terms of a scheduling order, the parties can submit their alternative submissions.

IT IS SO ORDERED this 8th day of June, 2015.

LEIGH MARTIN MAY
UNITED STATES DISTRICT JUDGE