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January 6, 2016

Via Electronic Mail and U.S. Mail

Honorable James E. Grimes
Administrative Law Judge
United States Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: In the Matter of Bennett Group Financial Services, LLC and Dawn J. Bennett, Administrative File No. 3-16801

Dear Judge Grimes:

We represent Dawn Bennett and Bennett Group Financial Services, LLC ("Respondents") in connection with the above-referenced matter. By way of this letter, Respondents move to have the Administrative Proceeding declared unconstitutional because the appointment of the presiding Administrative Law Judge ("ALJ") violates the Appointments Clause of the US Constitution. As such, from the time the presiding ALJ was assigned to this matter, the process has been procedurally defective. As such, Respondents seek a stay, dismissal of the matter because the forum is constitutionally defective, and/or such other relief that is just and proper.

Argument

Under the Appointments Clause of the Constitution, inferior Officers must be appointed by "the President," the "Courts of Law," or the "Heads of Departments." U.S. Const., art. II, sec. 2, cl. 2 (emphasis added). 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 "inferior Officers." 561 U.S. at 511-13. *Free Enterprise* also held that, under Article II of the Constitution, such officers may be insulated from Presidential removal by no more than one layer of tenure protection.[1]

The Commission's use of certain SEC ALJs fails both requirements. First, there is no dispute in the present matter that the SEC ALJ presiding over the Administrative Proceeding was not appointed by the Commissioners. Second, there is also no real dispute that SEC ALJs are protected from removal by at least two levels of tenure protection. Thus, the decisive constitutional question in this case is whether SEC ALJs are "inferior Officers" under Article II. As the SEC has conceded in a previous matter if SEC ALJs are determined to be inferior Officers that the SEC would lose on the merits. *Duka III*, 2015 WL 5547463, at *5.

1. The Broad Powers Exercised by SEC ALJs Demonstrate that SEC ALJs Are Inferior Officers

In determining whether administrative officers qualify as "inferior Officers" subject to the restrictions imposed by Article II, courts have repeatedly quoted the general rule formulated

[1] In *Duka I*, Judge Berman held that the tenure protections of SEC ALJs did not violate Article II because they carry out "solely adjudicatory functions, and are not engaged in policymaking or enforcement." *Duka I*, 2015 WL 1943245, at *10. This view is wrong, and would create an unprecedented category of Article II judicial officers unsupervised by the Executive Branch of government. Nevertheless, Judge Berman ultimately issued a preliminary injunction in *Duka II* because he determined that plaintiff would likely succeed on the merits because the appointment process for SEC ALJs "is likely unconstitutional in violation of the Appointments Clause." *Duka II*, 2015 WL 4940083, at *2.

by the Supreme Court in *Buckley v. Valeo*: that "[a]ny appointee exercising significant authority pursuant to the laws of the United States is an 'Officer of the United States' . . . ." 424 U.S. 1, 126 (1976). In other cases challenging the status of SEC ALJs under Article II, the SEC has not claimed that the Commissioners appoint ALJs. Rather, the Commission has argued only that SEC ALJs are mere employees rather than "inferior Officers" subject to Article II appointment and tenure protection rules. *See, e.g.*, *Hill*, 2015 WL 4307088, at * 16; *Gray Financial Group, Inc. v. SEC*, No. 15-cv-0492, Order, dated August 4, 2015.

The Commission's own description of the role played by its ALJs in administrative proceedings easily satisfies the "significant authority" test. Until very recently, the Commission described its ALJs as "independent judicial officers"—the Commission recently took the trouble to excise the word "officer" from this description—who "conduct hearings and rule on allegations of securities law violations . . . ." *See* S.E.C., Office of Administrative Law Judges, *available at* http://edgar.sec.gov/alj.shtml (last visited Nov. 19, 2015) ("Former SEC Website"). Nonetheless, the Commission's current description of SEC ALJs demonstrates the broad range and scope of authority an SEC ALJ possesses, including "issu[ing] subpoenas, hold[ing] prehearing conferences, and rul[ing] on motions and the admissibility of evidence." S.E.C., Office of Administrative Law Judges, *available at* http://www/sec.gov/alj (last visited Nov. 19, 2015) ("Current SEC Website"). A presiding SEC ALJ also "prepares an initial decision that includes factual findings, legal conclusions, and, if appropriate, orders relief." *Id.* And SEC ALJs may "order sanctions, including, "cease-and desist orders; investment company and officer-and director bars; censures, suspensions, limitations on activities, or bars from the securities industry . . . ." *Id.*

The SEC ALJ at issue in this case is indistinguishable from Officers described by the Supreme Court in *Freytag v. Commissioner of Internal Revenue*, 501 U.S. 868 (1994), when it determined that the special trial judges appointed by the Tax Court qualified as inferior Officers. First, the Supreme Court in *Freytag* found that "the office of special trial judge is established by law . . . ." 501 U.S. at 881 (quotations and citations omitted). The position of an SEC ALJ is similarly established by law. *See* 5 U.S.C. § 556, 15 U.S.C § 78d-1. Next, *Freytag* found that "the duties, salary, and means of appointment for [special trial judges] are specified by statute." 501 U.S. at 881 (citations omitted). Again, the same is true for SEC ALJs. *See* 5 U.S.C. §§ 556(c), 557 (setting forth responsibilities and powers of administrative law judges under the Administrative Procedure Act; 5 U.S.C. §§ 5311, 5372 (governing the salaries available to administrative law judges); 5 U.S.C. § 3105 (governing the appointment of administrative law judges by federal agencies).

Regarding the responsibilities performed by special trial judges, the Supreme Court found that they were authorized to take sworn testimony. 501 U.S. at 881. SEC ALJs can also take sworn testimony. *See* 5 U.S.C. §§ 556(c)(1), (4). The Supreme Court found that the special trial judges could conduct trials. 501 U.S. at 881-82. The same is true of SEC ALJs. *See* 17 CFR § 201.111, and the Commission itself compares the hearings conducted by its ALJs to "non-jury trials in the federal district courts." *See* Current SEC Website , *available at* http://www/sec.gov/alj. The Court in *Freytag* found that special trial judges were authorized to rule on the admissibility of evidence, 501 U.S. at 881-82, as are SEC ALJs. 17 CFR § 201.320. Finally, the Supreme Court found that special trial judges had "the power to enforce compliance with discovery orders." 501 U.S. at 881-82. Similarly, SEC ALJs have the authority to oversee discovery efforts, 17 CFR § 201.230; to issue, quash or modify subpoenas, 17 CFR § 201.232;

and to oversee depositions, 17 CFR § 201.233. In short, ALJs are indistinguishable, for purposes of the Appointments Clause, from the judges found to be Officers in *Freytag*. *See Hill*, 2015 WL 4307088, at * 19 ("*Freytag* mandates a finding that the SEC ALJs exercise 'significant authority' and are thus inferior Officers" because "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 . . . ."); *Duka I,* 2015 WL 1943245, at *8 ("*Freytag* . . . would appear to support the conclusion that SEC ALJs are also inferior Officers.").[2]

2. The Finality of SEC ALJ Decisions

The "significant authority" exercised by SEC ALJs over the matters assigned to them is further augmented by the fact that they are able to issue findings and orders that become final, without the requirement of any further review by the Commission itself. Under the relevant provisions of the Administrative Procedure Act, an SEC ALJ is authorized to issue an "initial decision" that "becomes the decision of [the Commission] without further proceedings" unless the Commission affirmatively decides to review the decision in question and take action. 5 U.S.C. § 557(b). The SEC's Rules of Practice also provide that the Commission is not required to review an initial decision issued by an SEC ALJ, and that if the Commission declines to do so, the initial decision will be promulgated by the Commission as a final decision. 17 CFR §

[2] Similarly, in a trilogy of cases involving the constitutional status of military tribunals, the Supreme Court likewise has treated adjudicative officers as "Officers" for purposes of Article II, and the question addressed by the Court in such cases is frequently whether those officers are principal officers requiring direct Presidential appointment with the advice and consent of the Senate, or if they are inferior Officers subject to less stringent appointment restrictions. *See, e.g.*, *Weiss v. United States*, 510 U.S. 163, 169 (1994) ("[t]he parties do not dispute that military judges, because of the authority and responsibilities they possess, act as "Officers" of the United States") (citing *Freytag*, 501 U.S. 868; *Buckley*, 424 U.S. at 126); *Edmond v. United States*, 520 U.S. 651, 661-63 (1997) (evaluation whether military judges qualify as "principal" or "inferior" officers for purposes of Article II); *Ryder v. United States*, 515 U.S. 177, 180 (1995) (acknowledging lower court's determination "that appellate military judges are inferior officers").

201.360(d)(1). 17 CFR § 201.410, 17 CFR § 201.411. Once this process is complete, the federal securities laws provide that "the action of the . . . administrative law judge . . . shall, for all purposes, including appeal or review therefore, be deemed the action of the Commission." 15 U.S.C. § 78d-1(c). Given the practical realities of litigation in front of SEC ALJS—in which the majority of initial decisions (at least 88%) issued by SEC ALJs become final decisions without additional review by the Commission—this structure grants additional plenary powers to SEC ALJs beyond those described above.

Thus, because SEC ALJs are inferior Officers, the fact that they are not appointed by the Commissioners—"the Heads of Department"—the Administrative Proceeding violates the Appointments Clause of the Constitution and makes this process before the presiding ALJ constitutionally defective.

3. The Administrative Proceeding is Unconstitutional Because ALJs, as Inferior Officers, Enjoy at Least Two Levels of Tenure Protection

The Administrative Proceeding is unconstitutional for another reason—because SEC ALJs, as inferior Officers, are protected from removal by at least two-levels of "good-cause" tenure protection. Specifically, the SEC ALJ can only be removed by SEC Commissioners for good cause; and SEC Commissioners can only be removed by the President for neglect of duty or malfeasance. *See MFS Sec. Corp. v. SEC*, 380 F.3d 611, 619-20 (2d Cir. 2004).

In *Free Enterprise*, the Supreme Court reviewed the structure of the PCAOB. *Free Enterprise*, 561 U.S. at 484. The members of the PCAOB are appointed and removable by the Commissioners of the SEC only "for good cause shown" and "in accordance with" 15 U.S.C. 7211(e)(6). *Id.* at 486. The Commissioners of the SEC are removable by the President only for "inefficiency, neglect of duty, or malfeasance in office." *See id.* at 487. The Supreme Court held this "multilevel" removal regime unconstitutional because it is "contrary to Article II's

vesting of executive power in the President" and "contravenes the President's 'constitutional obligation to ensure faithful execution of the laws.'" *Id.*at 484 (quoting *Morrison v. Olson*, 487 U.S. 654, 693 (1988)).

Free Enterprise is controlling here. Because SEC ALJs enjoy at least two-levels of "good-cause" tenure protection, the regime governing their removal suffers from the same infirmity found unconstitutional in *Free Enterprise.* First, 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). Second, SEC Commissioners are themselves protected by "good cause" tenure, in that they cannot be removed except for "inefficiency, neglect of duty, or malfeasance in office." *See Free Enterprise*, 561 U.S. at 487. Third, members of the MSPB, who determine whether "good cause" exists to remove an SEC ALJ, are also protected by tenure, as they can be removed "only for inefficiency, neglect of duty, or malfeasance in office." 5 U.S.C. § 1202(d).

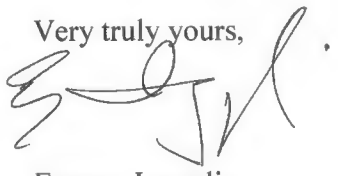
Although the Supreme Court did not expressly decide whether *Free Enterprise* rendered SEC administrative proceedings unconstitutional (*see Free Enterprise*, 561 U.S. at 507 n.10), as recognized by Justice Breyer in dissent, its ruling logically implies just that. *See Free Enterprise*, 561 U.S. at 542-43 (Breyer, J., dissenting) (noting "[t]he potential list of those whom today's decision affects is yet larger . . . [a]s . . . administrative law judges. . . are all executive officers . . . each removable only for good cause . . . determined by the [MSPB] . . . [b]ut members of the [MSPB] are themselves protected from removal . . . absent good cause. . . .") (internal citations and quotations omitted); *see also* Kent Barnett, Resolving the ALJ Quandary, 33 J. Nat'l Admin L. Judiciary 644, 648 (2013) ("if, as five current Supreme Court Justices have now suggested, ALJs are 'inferior Officers' (not mere employees), the manner in which some are

currently selected is likely unconstitutional."). Thus, because the President cannot oversee SEC ALJs in accordance with Article II, the Administrative Proceeding at issue here, as a matter of law, violates the Constitution.

Conclusion

For the reasons stated herein, Respondents move the ALJ to stay the action, dismiss it as constitutionally defective and/or grant other relief that is just ands proper.

Very truly yours,



Eugene Ingoglia

cc: Michael Rinaldi, Counsel for the Division of Enforcement (via e-mail)