U.S. SECURITIES AND EXCHANGE COMMISSION

Matter of

CHRISTOPHER M. GIBSON, A.P. No. 3-17184

Respondent.

RESPONDENT CHRISTOPHER M. GIBSON'S BRIEF SUPPORTING PETITION FOR REVIEW

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U.S. SECURITIES AND EXCHANGE COMMISSION

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Respondent.

RESPONDENT CHRISTOPHER M. GIBSON'S REPLY BRIEF SUPPORTING PETITION FOR REVIEW

Respondent Christopher M. Gibson ("Gibson") submits this reply brief in response to the Division's 7/1/2020 opposition brief, and in further support of Gibson's petition for review of the 3/24/2020 initial decision in this matter.

The Division's brief demonstrates (i) an unsustainable record, which would not withstand Court of Appeals scrutiny, on its claim of September 2011 frontrunning (**Point I below**); (ii) an unsustainable record on its claim based on GISF's October 2011 transaction with GISF's 81% owner, James Hull (**Point II**); and (iii) an unsustainable record on its claim involving October-November protective put purchases, which the Division has oddly characterized as Gibson's short bets against his own long position (**Point III**). The Division's brief compounds its lack of proof on these claims with errors of law, and a rejection of the Commission's June 2019 interpretation on standards for investment advisers (**Point IV**).

Additionally, the Constitution's removal clause bars this proceeding (**Point V**). The statute of limitations also bars this proceeding (**Point VI**). And the Supreme Court's recent *Liu* decision bars disgorgement here (**Point VII**).[1]

PRELIMINARY STATEMENT

Our opening brief began with a number of due process concerns. The Division's opposition brief has responded by doubling down on the false narrative of frontrunning and favoritism that led to these concerns.

While the Division for years claimed that Gibson shorted TRX and thus betrayed GISF's investors, its opposition brief now inconsistently contends that its OIP "never alleged that Gibson was not 'net long' in TRX." (Div.Br. 27) Yet on its face the OIP twice repeats that Gibson's put contracts "represented a short position, *i.e.* a bet that TRX's share price would decline." (OIP-¶9,

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[1] **Abbreviations**: Hearing transcript ("Tr."); Division Exhibit ("DX"); Respondent Exhibit ("RX"); Joint Exhibit ("JX"); Order Instituting Proceedings ("OIP"); 3/24/2020 Initial Decision ("ID"); Administrative Law Judge ("ALJ"); Division's 7/1/2020 brief ("Div.Br.").

45). At the hearing, THREE experts (two for the Division and one for Respondent) all rebutted this core OIP claim and agreed that Gibson was consistently "long" in his exposure to TRX stock, and thus with interests aligned with GISF investors. (Tr. 1060-70, 929-30, 1576-82, 1647-48). With this unanimity of experts, the ALJ found that "the record does not support" the Division's theory that Gibson was short. (ID-61).

The Division's brief claims it "never misled" James Hull," a critical witness, over whether Gibson had a short position in TRX. (Div.Br. 27-28) To the contrary, the ALJ found that, in taking Hull's pre-litigation investigative testimony, the Division "represented to Hull that 'in October and November 2011 ... Gibson took a short position in TRX in his' personal investment account"; that "[a]fter hearing this, Hull hit the roof and asked for a tolling agreement with Gibson and his father so that he could potentially sue them"; and that "Hull also spoke to other [GISF] investors about what he had learned." (ID-70-71). Hull viewed this as an act of extreme disloyalty, did not appear as a witness during the first (pre-*Lucia*) hearing in 2016, and for years would not speak to Gibson or his father. It was not until the second (post-*Lucia*) hearing in this matter in 2019 that "Hull learned that Gibson had not taken a short position in TRX," and "his views about Gibson ... changed." (ID-71).

The Division continues, throughout its opposition brief, its additional false narrative that Gibson made all major decisions for GISF. To the contrary, and as the ALJ found in the initial decision the Division wants affirmed, the record shows that "Hull was in control, and even Gibson's father believed [GISF] was ultimately being run by GISF's 81% owner Hull. Hull, who approved [GISF's] structure, believed he exercised approval authority over any 'major decision.'" (ID-8).

The Commission would likely never have instituted this proceeding if the Division's OIP allegations had fairly portrayed the key facts and circumstances. The Division's opposition brief dismisses its OIP omissions as mere "supposed defects" and enough for "notice" pleading. (Div.Br. 28-29). But the point is that fair presentation would likely have thwarted authorization, including the following absolutely critical facts left out of the OIP: **(i)** Hull personally owned 81% of GISF. **(ii)** GISF was a small and local private fund held by accredited investors. **(iii)** Apart from Hull's 81%, GISF was 9% comprised almost entirely of a small number of Hull's longtime close friends and colleagues in Augusta GA, who spoke personally with Hull before and after investing. **(iv)** The remaining 10% of GISF was owned by Gibson and his and his girlfriend's parents. **(v)** The 9% Hull-related investors, like the 10% Gibson-related investors, all approved of the 81% Hull's decision-making control over GISF, and would not have invested without Hull's involvement.

The Division's OIP additionally told the Commission (and ultimately the hearing witnesses who would learn of the OIP) that Gibson was a greedy profiteer who made large sums betting against GISF's investors. But the evidence shows not only that Gibson was never "short," but also that he and his family lost millions on GISF, more than anyone save Hull. Gibson personally lost $724,660, his parents lost $1,399,053, and his former girlfriend's father lost $965,318. (ID-34).[2]

[2] The ALJ erred by excluding the expert testimony and report of Jeffrey M. Smith (RX-227 not admitted), which would have discussed standards applicable to the conduct of this matter. AP Rel. 6624 (7/11/2019).

I. THE DIVISION'S UNSUSTAINABLE RECORD ON PURPORTED SEPTEMBER 2011 FRONTRUNNING

A. Making New Law. The Division's brief unwisely asks the Commission to make new law. Frontrunning has long meant trading ahead of a customer's order. The Division asks the Commission to change the definition of frontrunning by extending it to situations where there is no existing customer order, but where there might be an order soon, and where that order might be placed during market conditions that might let it impact price. Or in the Division's words, where there is a possible customer order that is both (i) "imminent" and (ii) "likely" to affect the price. (Div.Br. 12). No case has held this, and the Division cites no precedent holding this. The Division relies simply on the ALJ's citation to a letter from staff in the former Division of Market Regulation to two members of Congress in 1988. (ID-42 and n.322; Div.Br. 12)

The Division's proposal is a bad idea. Such a change in the law would create chaos in the securities industry. Brokers receiving clients' orders would, before executing, have to survey colleagues for other customers' possible orders – orders not appearing in any order book but rather merely discussed with the broker as possible but not yet placed. Possible orders that might (after-the-fact) be deemed to have been imminent and likely to have affected price. Depending on the seriousness of the possible orders (and size and market conditions), the Division would say that the brokers could not let the newer actual orders "frontrun" the older possible orders.

The Division's brief would lead the Commission into error. First, on appellate review the Division's formulation could not be supported under existing case law, as discussed in our opening brief. And second, applying the Division's formulation to the record here would violate the fundamental principle that the antifraud provisions are limited to conduct that is "deceptive." This is not a record showing deception. The only two GISF investor witnesses called by the Division both testified that Gibson's sale was not a problem. One investor testified it did not "bother' him that Gibson made just over $1,000 on the sale "without letting ... the other investors know." (Tr. 795). The other, GISF's largest investor Hull, testified it was "incidental," "small," and supported by "probably good reasons." (Tr. 608-10). And the ALJ found that Gibson's supposed loss avoided was merely $1,080, that this was under 1% of Gibson's total TRX exposure through GISF, and that Gibson remained significantly long. (ID-20, 64-65).

B. Division's "Imminence" Prong Not Satisfied. The Division has not proven its case under even its proposed new standard for frontrunning. As to the first half of the standard, the Division's own expert's testimony showed that a GISF trade was not "imminent":

> Q: Were there any orders [by GISF to sell TRX shares on 9/26/2011, at the time Gibson made his small sales]?
>
> A: Not that I know of.
>
> Q: If they [GISF then] were looking for a buyer for additional TRX shares, would they do it as a block sale?
>
> A: They could. They could also sell on the market.

> Q: And if they [GISF] were having somebody, [a] broker perhaps, look for a block purchaser, when would that block purchaser appear? Would it be the same day, Monday?
>
> A: Could be, if they found it.
>
> Q: And could it be Wednesday?
>
> A: Could be.
>
> Q: And could it be the following Monday?
>
> A: Yes.
>
> Q: Could it be in two weeks?
>
> A: Yes. ...
>
> Q: So if a block purchaser appeared and it wasn't an offer to their liking, they didn't have to take it, they could have just continued to hold the TRX stock, is that right?
>
> A: Yes.
>
> Q: And whether they would take it or not take it, I think is obvious it would depend on the terms of the block purchase, how much was being purchased, the price, what the market was doing, things like that. Is that right?
>
> A: Yes. ...
>
> Q: Right. And buyers, I think we've seen in the evidence, have been known to agree to purchase a block and then walk away? ...
>
> A: The answer is that's possible. Yes. (Tr. 499-504).

The Division has thus not proven an "imminent" order, the first half of its proposed new standard, where its expert agrees that a block bidder may have taken days or weeks to arrive. Nor when such a block bidder, once arrived, could have walked away, as actually happened to GISF with a different block bidder that breached a "legally binding" share sale agreement the following week. (RX-92; Tr. 1427-30, 1435).

And no GISF trade was "imminent" until Hull blessed it. The Division cites nothing to support its theory that Gibson had "power to control" GISF's trading (Div.Br. 14), and all of the record evidence is contrary. Hull testified plainly and forcefully that, as GISF's 81% owner, "any major decisions would first have to be approved by me," and "if I approved [Gibson's]

decision, we would go forward. If I didn't, then we wouldn't." (Tr. 570-71). And the ALJ found that when GISF got a block bid after 3 pm on 9/27/2011, it was "Gibson and Hull" who accepted it. (ID-21).

C. Division's "Price-Impact" Prong Not Satisfied. Nor has the Division proven the second half of its proposed new standard – that the possible imminent customer order must also be "likely" to affect the price. TRX was falling steeply on its own, from $5.54 on Wednesday 9/21 (closing price), to $4.58 on Thursday 9/22, to $4.07 on Friday 9/23. After stabilizing at $4.11 on Monday 9/26, it fell again to $3.54 on Tuesday 9/27. (JX-1).

The Division offered no evidence to connect this multi-day TRX tumble to TRX's late-day Tuesday 9/27 receipt and acceptance of a block bid at $3.50. TRX's trade occurred after the drop on 9/27 and hence did not cause it. That day, 9/27, TRX fell from $4.34 to $3.70 before the block bid arrived. And after GISF executed at $3.50, TRX closed up at $3.54, just above the block bid price. TRX then closed the next day again at the same $3.54; closed over the next five trading days at $3.70, $3.59, $3.51, $3.28, and $3.56; and traded mostly in the mid-$3s over the ensuing weeks. (JX-1)

So the timing of the price movements relative to when GISF got the block bid indisputably proves that GISF's 9/27 block sale had no impact on the TRX stock price. And that it is pure fantasy for the Division to speculate about an imaginary "price depressing effect of GISF's large block sale" resulting in "losses of more than $0.50/share" (Div.Br. 4).

The Division's own expert confirmed that the price dropped on its own on 9/27/2011, before GISF received and executed on a block bid:

> Q: ... My question was, were there any transactions by GISF [on 9/27/2011] before the one you described at 3:01 [pm]?
>
> A: So no. Those are the first GISF trades occurring on that day [9/27/2011]. ...
>
> Q: So then would you agree with me that the price [on 9/27/2011] ... went from an open [$]4.24 up to [$]4.34 and then down to [$]3.70 at 3 o'clock, yes?
>
> A: Yes. (Tr. 1009-10).
>
> Q: Were the prices influenced by demand and supply in the market?
>
> A: They can be, but – right.
>
> Q: Is there anything else you can tell us that would provide us with a reason why the stock price went down to [$]3.70 at 3 o'clock?
>
> A: I am not sure why the price went down to [$]3.70 at 3 o'clock.

Q: And do you have any evidence that there was activity by Gibson or GISF that caused the decline to [$]3.70?

A: There was no trading activity by Gibson or GISF.

Q: Okay. Now, the GISF sale [of TRX stock], am I correct was printed on the tape, publicly reported at 3:01 pm and 3:02 pm, is that right?

A: Yes. (Tr. 1011).

The ALJ agreed that the TRX price dropped before GISF got a bid, not that GISF's acceptance of the bid impacted the price: "The volume of trading in TRX was heavy all day [on 9/27/2011], with the share price rising to $4.34 and then dropping to $3.70 around 3 pm. Around that time, Sands [a broker] phoned Gibson with an offer of $3.50 a share for around 3.5 million of [GISF's] TRX shares." After GISF accepted the late day bid, "TRX closed at $3.54 on a volume of over six million shares traded that day." (ID-21-22). This is obviously not anything that has ever been understood as "frontrunning."

II. THE DIVISION'S UNSUSTAINABLE RECORD ON GISF'S TRANSACTION WITH GISF'S 81% OWNER

A. Purpose of the Transaction. All of the evidence cited by the ALJ (ID-26) – and all of the evidence in the record – shows that on 10/18/2011, Hull consolidated his 680,636 TRX shares with GISF's TRX shares in order to facilitate GISF's sale of TRX, and not for Hull's personal gain. Hull testified that GISF purchased his separately-held TRX shares to consolidate a larger block that could "entice the buyer" and garner a "substantially increased price." (Tr. 624, 627, 639). Gibson testified that he and Hull "wanted to be in a position to sell the full shares of [GISF] and its affiliates in a single transaction." (Tr. 1435, 1438-39).

The unchallenged evidence further showed that representatives of two prospective block purchasers for GISF's TRX shares demanded confirmation that GISF's entire position, including shares separately held by affiliates like Hull, would be available for sale in a "clean-up" transaction, and that no shares would be left behind with GISF or its affiliates like Hull. One prospective bidder even demanded that Gibson sign a formal "certification" that GISF's sale would include "any of its affiliates," meaning Hull. (Tr. 1429-30, 1435; RX-93; RX-62, p.7).

The ALJ noted that GISF "did not need" to consolidate its TRX shares with Hull's separate shares for both to be sold. But the ALJ credited Gibson's expert, who "confirmed based on his industry experience that consolidating the shares 'greatly simplifies the process of entering into a block transaction' because a 'buyer would want to know that he's seeing the whole piece for sale' and that there are no additional shares left behind." (ID-26-27; Tr. 1567; RX-228).

B. Transaction's Impact on Hull. The Division's brief offers no response to our opening point that the transaction disadvantaged Hull, and certainly did not "favor" him. Hull sold his separate TRX shares to GISF at $3.60 on 10/18/2011, but GISF was economically ahead

on the transaction in just a week when TRX hit $4.09 on 10/25/2011, and then closed well above $3.60 for most of the next three weeks. (JX-1; Tr. 891-92). Rather than consolidating with GISF, Hull could instead have given his separate TRX shares to a broker to sell into the ensuing substantial TRX volume – including 1,355,974 shares on 10/25/2011 and 1,901,168 shares on 11/3/2011 – ample room to absorb sales by Hull. (Tr. 624, 1571-73; JX-1). This is undisputed.

Hull owned 81% of GISF, so he was actually selling 81% of his 680,636 shares (or 551,315 shares) back to himself, and getting paid with 81% his own money. So he really disposed of only 19% (or 129,321 shares). (Tr. 706, 1573, 1030, 904-05). Hull "believe[d] firmly" that he could have disposed of these shares in market sales "and ended up in exactly the same place." (Tr. 625). No evidence contradicts this either.

C. Transaction's Impact on Others. The only investor witness the Division called on this point testified on cross-examination that it would not "offend" him if Hull "sold his shares to [GISF] for market price," and that he would not consider it a "disservice to ... the other investors." (Tr. 795-96). The transaction was at the closing market price that day. (DX-95; Tr. 619-21, 1435). This precisely complied with GISF's Offering Memorandum, which specified that "purchase and sale transactions ... may be effected between" GISF "and any other entities or accounts," if "for cash consideration at the current market price of the particular securities." (DX-24, p.19). The ALJ agreed. (ID-51).

So the transaction was permitted and made sound business sense based on unchallenged evidence. It should also be noted that, beyond the Division's speculation, there is no evidence that the transaction resulted in any benefit for Gibson. Before and after the transaction, Gibson still owed Hull the same $640,000 that Hull had in 2010 required Gibson to borrow to invest in GISF to give him a "severe" alignment of interest, skin in the game. No forgiveness was sought, expected or given. (RX-117; Tr. 561-66). Before and after the transaction, Hull's company paid Gibson a salary, beginning in 2009 and continuing through early 2013. (Tr. 334-35, 1230-38, 1313-1320; DX-147; DX-156). There is no evidence that this was under review or subject to change, and Hull flatly denied in testimony that the salary influenced the transaction in any way. (Tr. 708). Again, the record has no contrary evidence.

III. THE DIVISION'S UNSUSTAINABLE RECORD ON OCTOBER-NOVEMBER 2011 PROTECTIVE PUTS

A. Making More New Law. Having asked the Commission to change the definition of frontrunning by extending it to situations where there is no existing customer order, but where there might be an order soon, and where that order might be placed during market conditions that might let it impact price, the Division's brief next carries its request a step further. It also asks the Commission to apply this new formulation to a different security – TRX put options, when GISF held and might determine to sell TRX common shares at a time when a share sale could impact price. And to apply this new formulation in a context where the put option transactions began up to two weeks before GISF determined to sell the common shares. (Div.Br. 19-21).

Again, the Division's further expanded proposal is a bad idea that will have serious repercussions for the industry and investors. Securities professionals routinely must hedge long

positions for themselves and their clients. And buying "protective puts" against a long position in the security underlying the puts, as was done here, represents a core tool for this risk-management responsibility. Here, as the Division's own expert noted, **(i)** after buying the puts, Gibson "was long exposed to the stock through his involvement in [GISF]" (Tr. 1060); **(ii)** the options he bought are thus "characterize[d] ... as a protective put," and "as a hedge" (Tr. 1061); and **(iii)** a "protective" put protects an investor's long exposure in the underlying asset (Tr. 1070).

Fundamentally, it is not and should not be considered frontrunning to buy puts where all of the record evidence shows that it is in the put buyer's economic self-interest for the underlying stock price to rise and for the puts to expire worthless. The Division's expert explained that such was the case here, as **(i)** Gibson's puts protected only about a third of his and his friend's family's long exposure to TRX stock (Tr. 1064-67); and **(ii)** in the aggregate, Gibson was still personally making a "bullish" bet on TRX (Tr. 1076-77).[3]

Respondent's expert likewise agreed that **(i)** Gibson's puts only "partially" covered his TRX exposure (Tr. 1582, 1647-48); **(ii)** Gibson demonstrated a "bullish" view on TRX because a protective put holder "root[s] ... for higher stock prices, not lower stock prices," with the put simply a partial "insurance policy" (Tr. 1576-78); and **(iii)** Gibson remained in alignment with the other GISF investors throughout (Tr. 1587).[4]

B. Division's Proposed New Standard Not Satisfied. Again, the Division has not proven its case under even its proposed new standard for frontrunning. The Division has not shown that, at the time Gibson bought protective puts – on 10/27, 10/28, 11/2 and 11/8/2011 – Gibson or anyone else anticipated or thought it "imminent" that GISF would sell on 11/10/2011 in the middle of a TRX selling panic. All of the record evidence is contrary.

At the time Gibson bought protective puts, GISF was executing an orderly liquidation of its remaining TRX common stock at market prices. On 11/3/2011, GISF sold 485,397 shares, 289,100 shares and 8,200 shares in market transactions at market prices. (Tr. 879-80, 1455). On 11/8/2011, GISF did a negotiated off-market block sale of 500,000 shares at or near the market price. (Tr. 880-81, 884). On 11/9/2011, GISF sold 119,971 shares at near the market price. (Tr. 885). On these days GISF was doing its orderly sales, TRX common stock closed at $3.67 (11/3), $3.69 (11/8), $3.42 (11/9), and TRX had been trading in a stable mid-$3 range for the previous six weeks. (JX-1).

All of the evidence in the record shows that this orderly selling was expected to continue, and that throughout the period of these protective put purchases, GISF's panic sell orders on

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[3] The Division's citation to *Oleagues v. Icahn*, 866 F.3d 70, 72 n.1 (2d Cir. 2017), misleadingly quotes dicta describing a "naked" put as a "short" position. (Div.Br. 22). This is the opposite of a "protective" put that exists to protect a put buyer's "long" position, as discussed in the text and in our opening brief.

[4] Gibson also bought protective puts in an account he traded for another advisory client, an account in the name of his former girlfriend and funded by her parents. The parents had invested substantially in GISF and ultimately lost about $965,000 on GISF. Daughter (a graduate student) and parents are treated as an economic unit "because they were a family" living in the same household. (RX-205; Tr. 1098, 1301-02, 1328, 1337, 1448, 1649). *See* Exchange Act Rule 16a-1(a)(2) ("beneificial owner" includes "immediate family sharing the same household").

11/10/2011 were not in any way anticipated, and certainly not "imminent." If there were any more sales over the days ahead, including before, on or after 11/10/2011, they were likely to continue to be at the six-week prevailing market prices and were not "likely" to affect the price. As Gibson testified, without contradiction:

> ... From the day that we [GISF] began to sell our shares ... we were able to liquidate five and a half million shares.... And as can be demonstrated in [the price/volume exhibit, JX-1], the share price was essentially flat, did not move. We remained bullish on the shares. The view was we're trading 50 percent below where we had earlier in the year [2011] and that we had now liquidated more than half of our position and the expectation would be we would liquidate the remainder of the position without moving the market either.
>
> In addition, when we began liquidating our shares, we were one of the largest owners of the stock. We're now not one of the largest owners. We now own less than 5 million [shares]. BPI [a bank] owns 10 million. The sheik [a UAE investor] owns 10 million. Platinum Partners [a hedge fund] owns nearly 10 million.
>
> So the likelihood that if, during the six-week period that we liquidated half of our position, it didn't move the share price, and those owners were smaller owners of the shares and now they're larger owners of the shares and we are a much smaller owner of the shares, all things equal, it would be logical to assume that the past is indicative of the future and we would be able to liquidate the remaining position without a material move of the market. (Tr. 1450-51).

All of the record evidence shows that the 11/10/2011 panic selling first became anticipated, or "imminent," on the evening before, 11/9/2011. That evening, Gibson was summoned to a meeting with Platinum Partners, a hedge fund that by then owned twice as many TRX shares as GISF. Gibson expected to get an offer to buy GISF's remaining TRX shares, but instead Platinum wanted to pay GISF for it to agree to a six-month lock-up of its TRX shares. (TR. 1456-57). This news made GISF's 81% owner Hull "very concerned" that Platinum "may want to sell their shares before we would." (Tr. 1457-58).

All of the evidence shows that this new development happened on the evening of 11/9/2011, and that it was not known or suspected any time before. At that point, a GISF sale indeed became "imminent," as Hull and Gibson then and there decided on "aggressive" open market sales the next day, 11/10/2011, to force large holders to buy the shares TRX was selling. (Tr. 1461-62; DX-105). Hull testified that "our theory was the price was going to be going up because they're going to have to defend their shares and they didn't want the price to go down. What happened was the opposite. All the other large shareholders sold." (Tr. 658-59). Hull acknowledged that this plan "could potentially tank the stock," but said "that was not our plan or theory of the sale." (Tr. 659). The ALJ accepted this evidence concerning the events of 11/9-11/10/2011. (ID-32-33).

So all of the evidence shows that Gibson bought protective puts before GISF's "tank-the-stock" sale of common shares became "imminent" – indeed before it was ever even conceived of. This is what happened, and there is no contrary evidence. This is not frontrunning even under the Division's proposed and mistaken theory.

IV. THE DIVISION'S REJECTION OF THE COMMISSION'S JUNE 2019 INTERPRETATION ON THE STANDARD OF CONDUCT FOR INVESTMENT ADVISERS

A. The Commission's Guidance. Last year, the Commission made clear that "fiduciary duty follows the contours of the relationship between the adviser and its client, and the adviser and its client may shape that relationship by agreement." The Commission said that "fiduciary duty must be viewed in the context of the agreed-upon scope of the relationship between the adviser and the client," and that "the specific obligations that flow from the adviser's fiduciary duty depend upon what functions the adviser, as agent, has agreed to assume for the client, its principal." "Interpretation Regarding Standard of Conduct for Investment Advisers," Rel. IA-5248 (6/5/2019), pp. 9-10 (emphasis added).

The Commission stressed that the relationship with a retail client "will be significantly different from the obligations of an adviser to a registered investment company or private fund [like GISF] where the contract defines the scope of the adviser's services." *Id.* at pp. 9-10 (emphasis added). An adviser and client "may even agree that certain investment opportunities will not be allocated or offered to a client." *Id.* at p.26 n.65.

The Division argues that fiduciary duty cannot be "waived." (Div.Br. 10-11). But that is not the point. The actual question here is not waiver but instead, under the Commission's June 2019 Interpretation, the application of fiduciary duty in the context of the relationship that GISF created by agreement. Here, as the Commission's June 2019 Interpretation directed, the Division's charges against Gibson must be considered in the context of the agreement that "defin[ed] the scope of [Gibson's] services."

B. GISF's Agreed Scope of Services. GISF had its agreement defining its scope of services prepared by New York-based Seward & Kissel LLP, which Gibson understood to be "the leading and preeminent law firm providing advice to form a hedge fund of this nature." (RX-184; DX-24, p. 3; Tr. 1334-35). Seward & Kissel prepared both GISF's' Operating Agreement, and its accompanying Private Offering Memorandum. (DX-21; DX-24). The Division's own expert found that these contained what he viewed as "standard" provisions.

GISF's Operating Agreement (DX-21) and its Offering Memorandum (DX-24) defined a role for Gibson that allowed him to engage in other investment activities independent of GISF, even where these other activities actually "competed" with GISF. And the Division's expert confirmed that such provisions are "standard language in a fund agreement that gives the managing members of the fund the right to do other things." (Tr. 463-64). These provisions expressly allowed him to:

- Engage in "any other business, including securities business," "in competition with" GISF, while working only part-time for GISF. (DX-21, p.2).

- Manage other accounts or funds making investments, including accounts or funds with investment strategies similar to or different from GISF. (DX-21, p.2; DX-24, p.19).

- Have personal investments and interests in the same securities as GISF. (DX-24, p.19).

- "Give advice or take action" that "differs" as between GISF and other entities or accounts. (DX-24, p.19).

- Have conflicts of interest in "effecting transactions" for multiple entities, including entities in which Gibson has "a greater financial interest." (DX-24, p.19).

- Make "simultaneous identical portfolio transactions" for "other clients" that could impact prices received or paid for portfolio transactions. (DX-24, p.19).

- "In effecting transactions" for GISF and others, "take or liquidate the same investment positions" at different times and different prices. (DX-21, p.2).

It will come as a shock to investment managers large and small across the securities industry if such "standard" provisions do not mean what they plainly say. And if investment managers cannot simultaneously manage different portfolios for themselves and other clients with differing investment objectives. And if the managers and their various other clients must always stand aside and not trade shares or options until the moment when all of the manager's clients are ready to trade simultaneously and on the same terms. Or until the manager has completely informed and obtained consents from all the manager's clients when the manager or any particular client wants to do a trade – particularly a trade that will have no economic or positional impact on the other clients.[5]

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[5] For all the reasons above and in our opening memorandum, Gibson did not violate Advisers Act §§206(1)-(2), Exchange Act §10(b) and Rule 10b-5. Nor did he violate Advisers Act §206(4) and Rule 206(4)-8. Noting that Gibson "breached no fiduciary duty to investors" (ID-55), the ALJ bases the finding of a Rule 206(4)-8 violation solely on the frontrunning charges and the Hull transaction, and rules that "Gibson is not charged with making false statements to investors," or that any such alleged misstatements "appear immaterial." (ID-56). As the Rule 206(4)-8 determination is thus based on the same frontrunning charges and Hull transaction as the other Advisers Act and Exchange Act violations, it should be dismissed for the same reasons.

Further, the contention that Gibson violated Rule 206(4)-8 by failing to disclose alleged frontrunning and the Hull Transaction to investors is erroneous. After stating that Rule 206(4)-8 does not require scienter, that GISF was "a type of pooled investment vehicle," and that Gibson's potential conflicts were material, the ALJ concludes that "Since ... Gibson's actions constituted a fraud ..., he also deceived investors." ID at 55. However, the ALJ overlooks a required element for fraud based on nondisclosure – a duty to disclose. *Chiarella v. United States,* 445 U.S. 222, 232 (1980) (duty to disclose required to make silence fraudulent). The ALJ acknowledged that Gibson did not breach a fiduciary duty to investors and did not identify another duty to disclose to which Gibson was subject. The ALJ's observation that Rule 206(4)-8 applies when there is no fiduciary duty does not supply the requisite duty. And the ALJ's reliance upon *SEC v. Quan,* No. 11-cv-723, 2013 WL 5566252 (D. Minn. Oct. 8, 2013) is misplaced as the denial of motion for summary judgment has no precedential value.

V. THE CONSTITUTION'S REMOVAL CLAUSE BARS THIS PROCEEDING

The Division's opposition brief advises against "overreading" controlling Supreme Court precedent as the Division tries vainly to escape the inevitable conclusion that the ALJs have a removal clause problem that bars this proceeding. The Division shows itself unable to meet head-on what is a simple argument:

- *Free Enterprise Fund v. PCAOB*, 561 U.S. 477 (2010), held "that the dual for-cause limitations on the removal" of PCAOB members "contravene the Constitution's separation of powers." *Id.* at 492. The Supreme Court had "never before addressed" the question of "two layers of for-cause tenure." *Id.* at 501.

- The *Free Enterprise* holding applies to other "inferior officers" *Id.* at 493-94. This category includes SEC ALJs. *Lucia v. SEC*, 138 S. Ct. 2044 (2018). *See also Seila Law, LLC v. CFPB,* 2020 US Lexis, (Sup.Ct. 6/29/2020).

- SEC ALJs have multiple layers of removal protection – removal only for "good cause" determined by the MSRB (5 U.S.C. §7521(a)), whose members can only be removed for "good cause shown" (5 U.S.C. §7211(e)(6)). This gives SEC ALJs "two levels of protection from removal without cause – just what *Free Enterprise Fund* interpreted the Constitution to forbid." *Lucia*, 138 S. Ct. 2060 (Breyer, J., concurring).

- Additionally, SEC commissioners cannot remove ALJs without the MSRB's approval, and cannot themselves be removed except for "inefficiency, neglect of duty, or malfeasance in office." *Free Enterprise*, 651 U.S. at 487; *MFS Sec. Corp. v. SEC,* 380 F.3d 611, 619-20 (2d Cir. 2004).

The Division's opposition brief urges the Commission to revise the meaning of "good cause" for removal of ALJs under 5 U.S.C. § 7521, and to reinterpret the MSRB's role. (Div.Br. 29-34). But such a change in the removal powers would require Congressional or federal court action. And the SEC has so far resisted federal court jurisdiction in challenges to ALJs under the removal clause. *Bennett v. United States SEC*, 844 F.3d 174 (4th Cir. 2016); *Hill v. SEC*, 825 F.3d 1236 (11th Cir. 2016); *Tilton v. SEC*, 824 F.3d 276 (2d Cir. 2016); *Jarkesy v. SEC*, 803 F.3d 9 (D.C. Cir. 2015); *Bebo v. SEC*, 799 F.3d 765 (7th Cir. 2015); *Gibson v. SEC*, 2020 U.S. App. LEXIS 4591 (11th Cir. 2020).

The Division's brief urges a reformation of all or a part of three levels of impermissible tenure protection. The Division would have the Commission pretend that "good cause" doesn't mean what a common understanding of those words import. The Supreme Court has repeatedly told lower courts, much less an administrative agency, that they may not rewrite statutes based on policy concerns. *See, e.g., Azar v. Allina Health Servs.*, 139 S. Ct. 1804, 1815 (2019).

Finally, the position urged in the Division's opposition brief appears to be the opposite of the position taken by the Justice Department, which often represents the SEC on Constitutional issues like this. In *Lucia*, "the Solicitor General ... argued strongly that [the Supreme Court] should now decide the constitutionality of the administrative law judges' removal protections as well as the means of appointment. And in his view, the administrative law judges' statutory removal protections violate the Constitution (as interpreted in *Free Enterprise Fund*), unless we construe those protections as giving the Commission substantially greater power to remove administrative law judges than it presently has." *Lucia*, 138 S. Ct. 2061 (Breyer, J., concurring).

VI. THE STATUTE OF LIMITATIONS BARS THIS PROCEEDING

The OIP was issued on 3/29/2016. Following the Supreme Court's *Lucia* ruling, it is undisputed that Gibson was served with a copy of the OIP on 10/10/2018. (RX-201). The statute of limitations expired in November 2016, five years after the 2011 events at issue. Penalties have long been subject to the five-year statute of limitations in 28 U.S.C. §2462. *Gabelli v. SEC*, 568 U.S. 442, 454 (2013). And the Supreme Court has indicated that equitable relief should likewise be so time limited. *Kokesh v. SEC*, 137 S.Ct. 1635, 1643, 1645 (2017). The applicable five-year statute of limitations expired before service of the OIP in 2018, and this proceeding is now time-barred.

VII. *LIU* DECISION LIMITING DISGORGEMENT

There is no sustainable record for a finding of liability here, and for the reasons in our opening brief, there separately is no basis for imposition of remedies on these 2011 facts. Following the Supreme Court's recent decision in *Liu v. SEC*, 140 S.Ct. 1936 (2020), there are additional reasons not to impose disgorgement. While not disputing that *Liu* is controlling authority, the Division's brief contends without support that the initial decision "comports with" the *Liu* decision by offering to "submit further briefing on the appropriateness and feasibility of any distribution of such disgorgement." (Div.Br. 40).

To the contrary, *Liu* cannot be satisfied here. *Liu* recognized that "[t]he equitable nature of the profits remedy generally requires the SEC to return a defendant's gains to wronged investors for their benefit," and that "the SEC's equitable, profits-based remedy must do more than simply benefit the public at large by virtue of depriving a wrongdoer of ill-gotten gains." *Id.* at 1948. On this record there can be no doubt that the Division cannot realistically pay funds to anyone but the Treasury. This does not satisfy *Liu*.

Likewise, the Division ignores Gibson's and his family's massive losses by staying loyal to GISF and riding the ship down when its TRX investment soured. *Liu* noted that "[c]ourts may not enter disgorgement awards that exceed the gains 'made upon any business or investment, when both the receipts and payments are taken into the account.'" *Id.* at 1949-50. Again, requiring disgorgement on top of massive losses does not satisfy *Liu*.

CONCLUSION

Nine years after the events, it is time to lay this matter to rest. It is time to lift the cloud of these charges that hangs over the now-36-year old Gibson's head. It is time to let him come home to Augusta and have a reasonable chance at an American job and life among family and friends. This proceeding should never have been instituted, and it is time to end it.

Dated: July 15, 2020

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Certificate of Service and Filing

I certify that on July 15, 2020, pursuant to the Commission's March 18, 2020 order in all pending administrative proceedings, Rel. Nos. 33-10767, 34-88415, IA-5467, and IC-33820, I caused the foregoing to be filed with the Commission by sending it electronically to apfilings@sec.gov; and that pursuant to the parties' March 23, 2020 stipulation, I caused the foregoing to be served on Nicholas C. Margida and Gregory R. Bockin, counsel for the Division of Enforcement, by sending it electronically to margidan@sec.gov and bocking@sec.gov.

/s/ Thomas A. Ferrigno

Certificate of Compliance

The undersigned certifies that this brief contains 6404 words, excluding cover, tables of contents and authorities, and certificates of service and compliance, and based on the word-count function of the Microsoft Word software used to prepare the brief.

/s/ Thomas A. Ferrigno