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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-17950

In the Matter of **DAVID PRUITT, CPA,** **Respondent.**	**DIVISION OF ENFORCEMENT'S OPPOSITION TO RESPONDENT'S MOTION TO DISMISS THE PROCEEDING**

Respondent David Pruitt moves to dismiss this proceeding on the grounds that the removal provisions governing the Commission's administrative law judges ("ALJs") are unconstitutional and that he has been denied his Seventh Amendment right to a jury trial. Each of these arguments fails, and Pruitt's motion should be denied.

A. The ALJ's removal protections do not violate the Constitution.

Pruitt wrongly asserts (MTD 2-4) that this proceeding should be dismissed because the removal provisions governing the Commission's ALJs are unconstitutional. His argument ignores both the fact that the statute governing ALJ removal can be construed in a manner consistent with constitutional separation of powers principles and that the protections are constitutional in any event in light of the quasijudicial functions that the Commission's ALJs perform.

Article II of the 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." Art. II, § 1, cl. 1; *id.* § 3. Unlike its specific directives governing the power of appointment, "[t]he Constitution is silent with respect to the power of removal from office, where tenure is not fixed." *In re Hennen*, 38 U.S. 230, 258 (1839). The "power of removal" nonetheless has been viewed as

"incident to the power of appointment." *Id.* at 259; *see also Myers v. United States*, 272 U.S. 52, 164 (1926) (the Constitution implicitly reserves to the President the "power of removing those for whom he cannot continue to be responsible").

The Supreme Court has long recognized that Congress may impose limited restrictions on the removal power. Congress may, for example, impose a for-cause removal restriction on the President's power to remove principal officers of certain independent agencies. *See Free Enter. Fund v. Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 493-94 (2010). And the Court has countenanced for-cause limitations on a principal officer's ability to remove inferior officers. *Id.* at 494.

In *Free Enterprise*, however, the Court held that the "novel" and "rigorous" barrier to removing members of the Public Company Accounting Oversight Board ("PCAOB") by the Commission, whose members are presumed to enjoy "for cause" removal protection, left the President with insufficient ability to supervise the PCAOB's execution of the laws. 561 U.S. at 496. The Court noted that it had "previously upheld limited restrictions on the President's removal power" but only where "one level of protected tenure separated the President from an officer exercising executive power." *Id.* Two levels of "for cause" removal for an officer exercising "executive power," the Court held, "result[s] i[n] a Board that is not accountable to the President, and a President who is not responsible for the Board." *Id.*

For two reasons, *Free Enterprise* does not compel the conclusion that the statute providing that the Commission ALJs may be removed only for "good cause" (5 U.S.C. § 7521) violates the separation of powers. First, in his brief in *Lucia v. SEC* (S. Ct. No. 17-130),[1] the

[1] The Solicitor General's brief is available at https://www.supremecourt.gov/DocketPDF/17/17-130/36184/20180221202805163_17-130tsUnitedStates.pdf.

Solicitor General offered an interpretation of ALJs' "good cause" removal protection that comports with constitutional constraints. Drawing from constitutional avoidance principles, the Solicitor General explained (SG Br. 51) that, even where ALJs are embedded "in a structure involving more than one layer of tenure protection," a proper construction of "good cause" may alleviate constitutional concerns. The statutory scheme, the Solicitor General stated (SG Br. 47), must be understood to allow "[a]gency heads [to] be able to remove ALJs who refuse to follow agency policies and procedures, who frustrate the proper administration of adjudicatory proceedings, or who demonstrate deficient job performance." Under that view, Section 7521 should be "interpreted to permit an agency to remove an ALJ for personal misconduct or for failure to follow lawful agency directives or to perform his duties adequately." *Id.* at 45. At the same time, an ALJ may not be removed "'at the whim or caprice of the agency or for political reasons,'" *id.* at 49 (quoting *Ramspeck v. Fed. Trial Exam'rs Conference*, 345 U.S. 128, 142-43 (1953)), and "an ALJ would still be protected from removal for invidious reasons otherwise prohibited by law," *id.* at 50.

According to the Solicitor General, that interpretation of Section 7521 avoids the constitutional defects at issue in *Free Enterprise*. There, "the PCAOB's members could be removed only under an 'unusually high standard' that required a 'willful' violation of the law, a 'willful' abuse of their authority, or an 'unreasonable' failure to enforce legal requirements"; here, by contrast, "[t]he intrusion on presidential authority is significantly less." SG Br. 51 (quoting *Free Enterprise*, 561 U.S. at 503). "ALJs could accordingly be held accountable, by the

Heads of Departments and the President who appoint them, for failure to execute the laws faithfully." *Id.*[2]

Second, crucial to the Court's decision to invalidate the dual for-cause structure in that case was the fact that PCAOB Board members exercised quintessential "executive" functions—and not solely "quasijudicial" functions. 561 U.S. at 496, 502, 505, 507 n.10. Indeed, the Court refused to extend its holding to ALJs, who "of course perform adjudicative rather than enforcement or policymaking functions, or possess purely recommendatory powers." *Id.* at 507 n.10. The Solicitor General in *Lucia* similarly drew a line (SG Br. 45, 50) between quasijudicial duties and purely executive functions when he explained that the President, acting through principal officers, cannot remove an ALJ "to influence the outcome in a particular adjudication," and noted the need to "respect[] the independence of ALJs in adjudicating individual cases."

That is reflective of the Supreme Court's longstanding recognition that Congress's ability to enact limited removal protections depends in part on the functions of the particular office. In *Wiener v. United States*, 357 U.S. 349 (1958), for example, the Court upheld statutory removal restrictions of War Claims Commission members because the members performed "quasijudicial" rather than purely executive functions. *Id.* at 353-54. And in *Morrison v. Olson*,

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[2] The Solicitor General also stated that Section 7521(a)—which allows for removal "only for good cause established and determined by the Merit Systems Protection Board [MSPB] on the record after opportunity for hearing before the Board"—should be construed so that "the MSPB's review is limited to determining whether factual evidence exists to support the agency's proffered good faith grounds." SG Br. 39, 52. Such an approach ensures that the Department Head retains primary control in the decision to remove an ALJ. But it is not necessary to address this aspect of the statutory scheme at this juncture; regardless of how the MSPB's role in the removal process is understood, agencies like the Commission "possess the authority to reassign responsibilities away from ALJs while awaiting MSPB review of a removal decision." *Id.* at 53, 55. Consequently, "[t]hat authority avoids the possibility that an ALJ might continue to adjudicate cases beyond the point at which the Department Head has lost confidence in the ALJ's ability to exercise appropriate judgment." *Id.* at 55.

487 U.S. 654 (1988), the Court upheld good-cause restrictions on the removal of an "independent counsel," who was an executive officer with the power to investigate allegations of crime by high officers, because the restrictions provided structural independence necessary to the proper functioning of the particular office, and the independent counsel had "limited jurisdiction and tenure and lack [of] policymaking or significant administrative authority." *Id.* at 689-91, 695-96. Accordingly, Congress has the latitude to impose removal restrictions to ensure the structural independence necessary for ALJs to properly perform their quasijudicial functions.

Pruitt nevertheless insists (MTD 2-3) that *Free Enterprise*, read in light of *Lucia*, 138 S. Ct. 2044 (2018), establishes that the dual for-cause removal restrictions on ALJs are necessarily unconstitutional. But that argument overreads both decisions, neither of which held that multiple layers of removal protections are always unconstitutional or addressed the constitutionality of removal protections for ALJs. Indeed, the Commission has specifically noted that *Free Enterprise* did *not* hold that multiple layers of removal protections are always unconstitutional. *OptionsXpress, Inc.*, Exchange Act Release No. 78621, 2016 WL 4413227, at *50-52 (Aug. 18, 2016), *abrogated in part on other grounds by* Lucia, 138 S. Ct. 2044; *see also Timbervest, LLC*, Advisers Act Release No. 4197, 2015 WL 5472520, at *26-28 (Sept. 17, 2015), *vacated on other grounds by* Timbervest, LLC et al. v. SEC, No. 15-1416 (D.C. Cir. Nov. 19, 2018). Rather, as the Commission has explained, under *Free Enterprise*, the analysis turns on "whether the removal restrictions [at issue] are of such a nature that they impede the President's ability to perform his constitutional duty." *OptionsXpress, 2016 WL 4413227, at *50.* (quoting *Morrison v. Olson*, 487 U.S. 654, 691 (1988)). And "ALJs differ from the PCAOB members [considered

in *Free Enterprise*] in a number of significant ways" that "obviate any constitutional concerns from the dual for-case removal restrictions in the context of ALJs." *Id.*[3]

B. The proceeding does not violate the Seventh Amendment.

Pruitt's claim that the proceeding violates the Seventh Amendment (MTD 4-6) fares no better. Pruitt ignores the Supreme Court's consistent recognition that the Seventh Amendment's right to a jury trial "is not applicable to administrative proceedings." *Tull v. United States*, 481 U.S. 412, 418 n.4 (1987); *Atlas Roofing Co. v. Occupational Safety & Health Review Comm'n*, 430 U.S. 442, 455 (1977) (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"). Pruitt elides this well-established principle by claiming (MTD 5-6) that Commission administrative enforcement actions are not actions to determine "public rights."

That argument is implausible on its face. As the Supreme Court has explained, "public rights" cases are those "in which the Government sues in its sovereign capacity to enforce public rights created by statutes within the power of Congress to enact." *Atlas Roofing*, 430 U.S. at 450. Commission administrative enforcement actions fall squarely within this description: They are initiated by the government, acting in a quintessentially regulatory capacity, in order to enforce statutes well within Congress's power to enact, and which were enacted specifically to protect the investing public. *See, e.g., Lorenzo v. SEC*, 139 S. Ct. 1094, 1103 (2019) (discussing

[3] *See also* Order, *David. S. Hall, P.C.*, Admin. Proc. Rulings Rel. No.6635 (July 23, 2019), https://www.sec.gov/alj/aljorders/2019/ap-6635.pdf (denying motion to dismiss that argued, in part, that ALJ removal protections were unconstitutional); Order, *Raymond J. Lucia Cos.*, Admin. Proc. Rulings Rel. No. 6628 (July 15, 2019), https://www.sec.gov/alj/aljorders/2019/ap-6628.pdf (same).

the "basic purpose behind" the securities laws, including the need to equip regulators "'to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits'" (quoting *SEC v. W.J. Howey Co.*, 328 293, 299 (1946))).

It is hardly surprising, therefore, that both courts and the Commission have consistently rejected claims that Commission administrative enforcement actions violate the Seventh Amendment. *E.g.*, *Hill v. SEC*, 114 F. Supp. 3d 1297, 1316 (N.D. Ga. 2015) ("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."), *overruled on other grounds by Hill*, 825 F.3d 1236; *Charles L. Hill, Jr.*, Exchange Act Rel. No. 79459, 2016 WL 7032731, at *3 (Dec. 2, 2016) (rejecting Seventh Amendment argument); *Harding Advisory LLC & Wing F. Chau*, Securities Act Rel. No. 9561, 2014 WL 988532, at *9 n.46 (Mar. 14, 2014) (same); *see also Imperato v. SEC*, 693 F. App'x 870, 876 (11th Cir. 2017) (rejecting claim that petitioners were entitled to jury trial in PCAOB administrative proceeding). That result should hold here.

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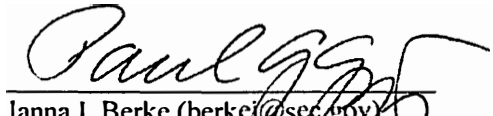
For the foregoing reasons, Pruitt's motion to dismiss should be denied.

Dated: August 21, 2019

Respectfully submitted,

DIVISION OF ENFORCEMENT

By: 

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CERTIFICATE OF SERVICE

I hereby certify that on August 21, 2019, I caused the original and three copies of the foregoing DIVISION OF ENFORCEMENT'S OPPOSITION TO RESPONDENT'S MOTION TO DISMISS THE PROCEEDING to be filed with:

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I further certify that I caused to be served a copy of the foregoing via email upon:

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I further certify that I caused a courtesy copy of the foregoing to be provided by email to:

The Honorable James Grimes
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