UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

ADMINISTRATIVE PROCEEDING
File No. 3-17950

In the Matter of,

David Pruitt, CPA

Respondent.

RESPONDENT DAVID PRUITT'S MOTION TO STAY PENDING SUPREME COURT REVIEW OF APPOINTMENTS CLAUSE CHALLENGE

Respondent David N. Pruitt ("Mr. Pruitt"), through his undersigned counsel, respectfully moves for an order staying these proceedings pending review by the United States Supreme Court of the recent challenge to the appointment of Securities and Exchange Commission Administrative Law Judges under the Appointments Clause of the United States Constitution. A Memorandum of Points and Authorities in Support of Mr. Pruitt's Motion is attached hereto.

Dated: September 22, 2017
New York, New York

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Respondent David N. Pruitt ("Mr. Pruitt") submits this memorandum of points and authorities in support of his motion to stay these proceedings (the "Motion") pending Supreme Court review of the recent challenge to the appointment of Securities and Exchange Commission ("SEC" or the "Commission") Administrative Law Judges ("ALJ") under the Appointments Clause of the United States Constitution.

PRELIMINARY STATEMENT

Mr. Pruitt moves to stay this proceeding because it is highly likely the Supreme Court will address in the coming term the circuit split between *Bandimere v. SEC*, 844 F.3d 1168 (10th Cir. 2016), *reh'g denied*, 855 F.3d 1128 (10th Cir. 2017) (mem.) and *Raymond J. Lucia Cos., Inc. v. SEC*, 832 F.3d 277 (D.C. Cir. 2016), *reh'g en banc granted, judgment vacated*, (Feb. 16, 2017), *on reh'g en banc*, No. 15-1345, 2017 WL 2727019 (D.C. Cir. June 26, 2017) (mem.) regarding whether SEC ALJs are inferior officers subject to appointment consistent with the Appointments Clause of the Constitution of the United States.

As this Court is aware, the Tenth Circuit and D.C. Circuit have reached opposite conclusions as to whether Commission ALJs are "inferior officers" subject to appointment in accordance with the provisions of the Appointments Clause. The Tenth Circuit held that they are inferior officers; the D.C. Circuit held they are not. *Compare Bandimere*, 844 F.3d at 1188, *with Lucia*, 832 F.3d at 285–89. Critically, en banc review of the decision in *Lucia*, which held that there was no constitutional violation, was denied only because the ten-judge en banc court split 5-5, making Supreme Court review highly likely. The fact that the D.C. Circuit is evenly split is particularly significant as the D.C. Circuit is often considered to be a proxy for the Supreme Court.

Both cases now seek Supreme Court review. The government has indicated its intention to file a petition for a writ of certiorari in *Bandimere* with two applications for an extension of

time, both of which have been granted by the Supreme Court. The government's petition is currently due September 29. On July 21, Lucia sought a writ of certiorari in *Lucia*, with a response by the government due October 25.

As set forth below, Respondent submits that the holding in *Bandimere* that an SEC ALJ is an officer, not an employee, subject to appointment consistent with the dictates of the Appointments Clause, will likely be upheld by the Supreme Court. Most recently, in *Burgess v. Federal Deposit Insurance Corporation*, No. 17-60579, 2017 WL 3928326 (5th Cir. Sept. 7, 2017), the Fifth Circuit embraced *Bandimere*, rejected *Lucia* as inconsistent with Supreme Court precedent, and stayed a Federal Deposit Insurance Corporation ("FDIC") administrative order assessing a civil penalty because the respondent demonstrated a likelihood of success on his claim that the FDIC ALJ in his proceeding was unconstitutionally appointed.

The Court should similarly stay this proceeding. Any proceedings before an unconstitutionally appointed ALJ would be void requiring rehearing in a constitutional forum and leading to a tremendous waste of resources. The serious nature of the sanctions sought by the Division make it all the more compelling to temporarily stay these proceedings as the substantial prejudice to Mr. Pruitt of forcing him to litigate in an unconstitutional forum, and then potentially re-litigate in a constitutional forum, outweighs the temporary delay that would result from a stay. As there is substantial doubt about the constitutionality of this proceeding, Mr. Pruitt should not be prejudiced by being made to expend already limited resources to potentially defend himself twice nor should he face the prospect of the imposition of potential career-ending sanctions by an ALJ that may lack the authority to issue those sanctions. Courts have granted stays in similar contexts where Supreme Court review was pending and the outcome of that review would have a significant impact on the proceedings below. A finding by

the Supreme Court that the ALJ appointment process does pass constitutional muster would have a significant impact and likely lead to the termination of these proceedings. In addition, the Commission has already determined that a stay of administrative proceedings in the Tenth Circuit is warranted in light of *Bandimere*, and because the case is likely to be heard and resolved by the Supreme Court in this term, this Court should stay temporarily these proceedings until the Supreme Court has decided the issue.

ARGUMENT

I. LEGAL STANDARD

The Commission's Rules of Practice applicable to administrative proceedings do not contain a rule for a stay in this context. The Commission has considered similar requests for a stay as a request for an adjournment pursuant to Rule 161. *See* 17 C.F.R. § 201.161; *John Thomas Capital Mgmt. Grp. LLC*, Admin. Proc. File No. 3-15255, Exchange Act Release No. 74345, 2015 SEC LEXIS 663, at *7–8, Order (Feb. 20, 2015) ("*John Thomas*"). Although such requests are "strongly disfavor[ed]" absent a showing of substantial prejudice, this Motion meets that standard and the factors outlined in Rule 161(b)(1). *See* 17 C.F.R. § 201.161(b)(1). The substantial prejudice Mr. Pruitt will suffer if this proceeding continues is set forth in Section II below. The remaining factors all weigh in favor of granting the adjournment. The proceeding is still in the early stages of discovery with the hearing still more than five months away. A temporary stay while the Supreme Court decides the issue is reasonable at this early stage. While adjourning these dates may impact the Court's ability to render an initial decision within the timeframes set forth by the Commission's Rules of Practice, the hardship on Mr. Pruitt should outweigh any such concern of delay in the short-term. Considering the substantial prejudice Mr. Pruitt will suffer should he be made to litigate in an unconstitutional forum, and then potentially re-litigate in a constitutional forum, the Court should grant this Motion.

II. THE COURT SHOULD STAY THIS PROCEEDING PENDING SUPREME COURT REVIEW OF THE APPOINTMENTS CLAUSE CHALLENGE

Supreme Court review of the Appointments Clause issue in this term is highly likely. First, three circuits have now weighed in on the issue, and a clear circuit split exists between *Bandimere* (and now *Burgess*) and *Lucia*. Second, there is an intracircuit split in the D.C. Circuit, with the en banc panel evenly splitting 5-5 in *Lucia*. Third, the importance of resolving this issue is readily apparent; the Commission currently has an open-ended stay in place in proceedings in which a respondent can appeal to the Tenth Circuit, while it is exercising intercircuit nonacquiesence in other proceedings, an untenable and unfair approach for any significant period of time. Since the Commission is likely seeking a petition for a writ of certiorari in *Bandimere*, the Commission itself agrees that Supreme Court review of the issue is necessary.

Given the likelihood of Supreme Court review of the issue in this term, and given the fact that any proceeding before this Court would be void should the view of the *Bandimere* and *Burgess* courts prevail, Mr. Pruitt respectfully requests that the Court stay this matter in the interim. Such a stay should not be indefinite—it should last only until the Supreme Court decides the Appointments Clause issue, or alternatively denies a writ of certiorari in both *Bandimere* and *Lucia*.

A stay is also warranted because that is precisely what the Commission ordered in light of *Bandimere*. After the Tenth Circuit denied en banc review in *Bandimere*, the Commission stayed all administrative proceedings "assigned to an administrative law judge in which a respondent has the option to seek review in the Tenth Circuit of a final order of the Commission." *In re Pending Admin. Proceedings*, Exchange Act Release No. 80741, Order (May 22, 2017). The Commission held that the stay would be in effect "pending the expiration

of time in which the government may file a petition for a writ of certiorari in *Bandimere*, the resolution of any such petition and any decision issued by the Supreme Court in that case, or further order of the Commission." *Id.*

The Commission's rationale for staying proceedings in the Tenth Circuit should apply here as well. The Commission acted prudently in acquiescing to *Bandimere* in the Tenth Circuit. Under the doctrine of intracircuit nonacquiescence, the Commission would likely contend it was not legally bound to seek a stay pending its petition for certiorari in that case. However, the Commission instead chose not to overlook the law it was likely seeking to challenge within the Tenth Circuit. That same level of prudence must apply to cases outside the Tenth Circuit such as this one. While the Commission is generally entitled to exercise intercircuit nonacquiesence and follow *Lucia* instead of *Bandimere*, the basis for doing so falls away in light of the petition for certiorari in *Lucia*, which the Commission will likely agree should be heard. Mr. Pruitt should not be forced to expend the time and resources that it would take to litigate in a constitutionally defective forum while individuals residing in any of the six states in the Tenth Circuit are not required to do the same. Accident of geography should not force Mr. Pruitt to suffer the prejudice that would result if the stay requested in this Motion is not granted.

A stay is particularly warranted because should the Supreme Court hold that Commission ALJs are inferior officers, these proceedings will have to be set aside, requiring the Commission to start over again in a constitutionally appropriate forum (or in front of a constitutionally appointed ALJ). *See Bandimere*, 844 F.3d at 1188 (setting aside Commission opinion). That would lead to an unprecedented burden on Mr. Pruitt who would be forced to expend limited resources to defend himself twice. The rigors of the greatly expedited administrative process already impose significant burdens on Mr. Pruitt's ability to prepare his defense. The significant

civil penalty and career-ending bar the Division seeks all weigh in favor of a temporary adjournment. The harm to Mr. Pruitt is real and can be entirely avoided by granting the adjournment sought.

While the Commission has held that being haled into a potentially improper forum does not itself cause irreparable harm, *see John Thomas*, 2015 SEC LEXIS 663, at *17–18, this analysis ignores the significant burdens placed on a respondent who chooses to defend an administrative proceeding. Forcing a respondent to unnecessarily deplete limited resources is fundamentally unfair and a significant prejudice[1] since there is a good chance that the proceeding will have to be repeated in a different forum. Mr. Pruitt, a retired Army officer, will have to travel thousands of miles and incur significant expenses to meet with counsel and prepare for and participate in a hearing that may not count. Mr. Pruitt would also be forced to divulge his trial strategy prematurely heightening the already unfair advantage the Division has in these proceedings based on the benefits of its pre-hearing investigation. While there is an interest in the timely and efficient disposition of administrative proceedings, this oft-cited premise should not be used as a cudgel to deny a temporary adjournment while this unique and outcome determinative constitutional issue is decided. Amendments to the Commission's Rules of Practice, 81 Fed. Reg. 50212, 50212 n.2 (July 29, 2016). The prejudice to Respondent greatly outweighs the theoretical harm of delay that could result from a temporary adjournment of this proceeding. This prejudice can be avoided entirely with a stay while the Supreme Court considers the issue.

[1] Damage or detriment to one's legal rights or claims. *Prejudice*, BLACK'S LAW DICTIONARY (10th ed. 2014).

District courts have stayed proceedings where review by the Supreme Court was pending and a decision would impact the viability of the litigation. *See Salvatore v. Microbilt Corp.*, No. 4:14-CV-1848, 2015 WL 5008856, at *2 (M.D. Pa. Aug. 20, 2015) (finding "that the parties face potential hardship if the stay were denied and the parties were required to expend time and resources engaging in fact and expert discovery over the course of the next year while [the Supreme Court case] remains pending, since a decision in that case will likely have an impact on the viability of this lawsuit"). These district court matters were temporarily stayed to prevent the needless waste and expenditure of limited resources that Mr: Pruitt would similarly be forced to expend should these proceedings continue. *See, e.g.*, *Kamal v. J. Crew Grp., Inc.*, Civil Action No. 15-0190 (WJM), 2015 WL 9480017, at *2 & n.1 (D.N.J. Dec. 29, 2015) (noting several district courts have stayed cases pending the outcome of a Supreme Court case and absent a stay, the defendant "could be compelled to expend significant resources defending this action"); *Munoz v. PHH Corp.*, No. 1:08cv0759 AWI DLB, 2011 WL 4048708, at *4 (E.D. Cal. Sept. 9, 2011) (finding that "a stay will reduce the additional expenditure of the parties' time and resources, which is of particular importance if the Supreme Court's decision ultimately disposes of this action"); *Alvarez v. T-Mobile USA, Inc.*, No. CIV. 2:10-2373 WBS GGH, 2010 WL 5092971, at *2 (E.D. Cal. Dec. 7, 2010) (noting that if motion to stay were denied pending decision by Supreme Court, "Defendant will incur significant costs relating to fact and expert discovery, motion practice, and trial preparation to defend this action"). The Court should apply the same rationale and grant a temporary stay while the Supreme Court considers the Appointments Clause issue.

III. THE SUPREME COURT WILL LIKELY FOLLOW THE HOLDING IN *BANDIMERE*

As the evenly split en banc panel in the D.C. Circuit confirmed, there is a substantial difference of opinion on the issue and it is very likely that this proceeding would in fact need to be repeated in a different forum, or before a constitutionally appointed ALJ. The current state of affairs, with administrative proceedings halted in the Tenth Circuit and a clear circuit split, is not sustainable. The Supreme Court will need to step in to resolve this issue.

The holding in *Bandimere* is more consistent with prior Supreme Court precedent on the issue than *Lucia*. In *Buckley v. Valeo*, 424 U.S. 1, 126 (1976), any appointee to a federal office established by law who exercises "significant authority pursuant to the laws of the United States" is an officer. The position of a Commission ALJ (as with other ALJs) is established by law. *See* 5 U.S.C. §§ 556, 557; 15 U.S.C. § 78d-1. It cannot be seriously disputed that this Court has significant authority, including the authority to issue subpoenas; hold hearings; rule on motions and the admissibility of evidence; order sanctions including civil penalties, bar orders, and disgorgement; issue findings of fact and conclusions of law; and render decisions. *See Bandimere*, 844 F.3d at 1188.

In *Lucia*, the D.C. Circuit held to the contrary because this Court does not issue final decisions. But nothing in the Supreme Court's jurisprudence suggests that the ability to issue final orders is a necessary criterion to the exercise of significant authority. To the contrary, in *Freytag v. Commissioner of Internal Revenue*, 501 U.S. 868, 881 (1991), the Supreme Court specifically rejected this argument, holding that it "ignore[d] the significance of the duties and discretion that special trial judges possess." *Bandimere*, 844 F.3d at 1182–83 (quoting *Freytag*, 501 U.S. at 881).

In *Burgess*, the Fifth Circuit expressly rejected *Lucia*'s holding that an ALJ is not an inferior officer because the ALJ cannot issue final decisions. "The FDIC ALJs' lack of final decision-making authority does not defeat Burgess's assertion that they are inferior Officers." *Burgess*, 2017 WL 3928326, at *4. The Court concurred with *Bandimere* and held that even though FDIC ALJs have *less* final decision-making authority than SEC ALJs, they too are inferior officers because, under *Freytag*, they are empowered to exercise "significant discretion" over "important functions." *Burgess*, 2017 WL 3928326, at *2 (quoting *Freytag*, 501 U.S. at 881–82).

Lucia's holding that an executive appointee can be an inferior officer only if he can render final decisions is also at odds with other Supreme Court decisions holding, inter alia, that district-court clerks, thousands of clerks within the Treasury and Interior Departments, engineers, and assistant surgeons are inferior officers. *See In re Hennen*, 38 U.S. 230, 258 (1839); *United States v. Germaine*, 99 U.S. 508, 511 (1878); *United States v. Perkins*, 116 U.S. 483, 484 (1886); *United States v. Moore*, 95 U.S. 760, 762 (1877). In *Edmond v. United States*, 520 U.S. 651, 665 (1997), the Supreme Court held that the judges of the Coast Guard Court of Criminal Appeals were inferior, not principal, officers because they "have no power to render a final decision on behalf of the United States unless permitted to do so by other Executive officers." Thus, while the inability to issue a final order may distinguish a principal officer (whom the President must appoint with the Senate's advice and consent) from an inferior officer, it does not disqualify one from being an inferior officer. "The agencies' power to overrule, in other words, merely establishes ALJs' status as inferior officers." Kent Barnett, *Resolving the ALJ Quandary*, 66 VAND. L. REV. 797, 809–14 (2013).

Moreover, this Court has previously recognized that there are strong arguments supporting the notion that Commission ALJs are inferior officers, including the fact that ALJs are statutorily exempt from the definition of the term "employee" for certain purposes and the fact that Congress distinguished between ALJs and employees in describing to whom the Commission can assign administrative cases. *See Charles L. Hill, Jr.*, Admin. Proc. File No. 3-16383, Admin. Proc. Rulings Release No. 2675, 2015 SEC LEXIS 1899, at *14 n.5, Order (ALJ May 14, 2015) (citing 5 U.S.C. § 4301(2)(D) and 15 U.S.C. § 78d-1(a)).

Respondent is aware that in 2016, this Court held that it was bound by Commission precedent holding that Commission ALJs are employees, not inferior officers, and that the Commission has declined to acquiesce to *Bandimere*. *See Bennett Grp. Fin. Servs., LLC*, Admin. Proc. File No. 3-16801, Admin. Proc. Rulings Release No. 3494, 2016 SEC LEXIS 112, Order (ALJ Jan. 12, 2016); *Bennett Grp. Fin. Servs., LLC*, Admin. Proc. File No. 3-16801, Exchange Act Release No. 80347, 2017 SEC LEXIS 1003, at *23–24, Order (Mar. 30, 2017). Since the Tenth Circuit's decision in *Bandimere*, however, the validity of the Commission's position that SEC ALJs are not inferior officers has come into serious question. The Court's own observations on the matter echo this. But in any event, Mr. Pruitt does not ask the Court to contravene Commission precedent; he merely seeks a stay pending Supreme Court review where the issue will be decided once and for all.

Although the Commission recently denied a motion to stay an administrative proceeding because of the Appointments Clause circuit split, *see Lynn Tilton*, Admin. Proc. File No. 3-16462, Accounting and Auditing Enforcement Release No. 3885, 2017 SEC LEXIS 2296, Order (July 28, 2017), unlike the instant action, the fact that the hearing had already taken place was central to its decision. Here, in contrast, the proceedings are in the early stages. Moreover, since

briefing in *Tilton*, the certiorari process has begun in *Lucia* with *Bandimere* likely to follow. Finally, in denying a stay, the Commission relied on its authority not to acquiesce to *Bandimere*. But as set forth above, the Commission's rationale for staying cases in the Tenth Circuit must apply to all cases while the matter is being definitively resolved, particularly since the Commission will undoubtedly concur in the appropriateness of Supreme Court review in *Lucia*, the case whose holding the Commission presently follows.[2]

CONCLUSION

For the foregoing reasons, Mr. Pruitt respectfully requests that the Court grant the adjournment staying this action pending Supreme Court review of *Bandimere* and/or *Lucia*.

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[2] Respondent also contends that the proceeding is unconstitutional because the multiple layers of tenure protection enjoyed by Commission ALJs violate the separation of powers. The Court received a career appointment and may be removed from the position only for good cause, which must be "established and determined" by the Merit Systems Protection Board, *see* 5 U.S.C. § 7521(a), and only upon the initiation of the Commissioners, who themselves are removable only for "inefficiency, neglect of duty, or malfeasance in office." *SEC v. Blinder, Robinson & Co, Inc.*, 855 F.2d 677, 681 (10th Cir. 1988). In *Free Enterprise Fund v. PCAOB*, 561 U.S. 477, 484 (2010), the Supreme Court held such "multilevel protection from removal is contrary to Article II's vesting of the executive power in the President." Since the Court is bound by Commission precedent rejecting this contention, *see Timbervest, LLC*, Admin. Proc. File No. 3-15519, Investment Advisers Act of 1940 Release No. 4197, 2015 SEC LEXIS 3854, at *89–112, Order (Sept. 17, 2015), and has rejected this argument on the merits, *see Charles L. Hill, Jr.*, 2015 SEC LEXIS 1899, at *10–22, Mr. Pruitt makes this argument here to preserve the issue for appeal.