UNITED STATES OF AMERICA
BEFORE THE SECURITIES AND EXCHANGE COMMISSION

In the Matter of the Application of SCOTTSDALE CAPITAL ADVISORS CORPORATION, JOHN J. HURRY, TIMOTHY B. DIBLASI, and D. MICHAEL CRUZ For Review of Disciplinary Action Taken by FINRA	File No. 3-18612

PETITIONERS' REPLY IN SUPPORT OF MOTION FOR LEAVE TO SUBMIT SUPPLEMENTAL AUTHORITY

By application dated October 15, 2020, Petitioners sought to present to the Commission certain directives issued by the President and the Office of Management and Budget, intended to underscore and assist the country's economic recovery as it confronts the global pandemic. Included in those issuances was the directive to all heads of agencies, administrative enforcement, and administrative adjudicators to revisit their existing regulations and revise where appropriate to incorporate "principles of fairness in administrative enforcement and adjudication," with the overarching goal of providing regulatory "relief" to facilitate the growth and development of businesses and promote the country's economic recovery.

Remarkably, FINRA actually opposes consideration of those materials and principles, and the underlying goals of regulatory relief to aid the economic recovery, telling the Commission that none of those principles applies to it. FINRA Opp. at 3-4. FINRA insists that it is not bound by those principles and goals because it is a private actor, not an administrative agency. It is, it insists, beyond the authority of the President or the executive branch and can disregard the issues and directives that govern all executive departments and agencies. Its proclamation is both telling and troubling.

FINRA's view that it can ignore the directives to administrative agencies, including the Securities and Exchange Commission, is fundamentally wrong. The extent of FINRA's authority to regulate participants in the securities industry is circumscribed both by statute and by the oversight provided by the Commission, which is, in turn, required to consider the contents of the Ray Memorandum in connection with that oversight.

The degree to which FINRA is subject to the Commission's control is not reasonably debatable. In speaking about SROs in general, Justice Breyer has observed that "those organizations—which rely on private financing and on officers drawn from the private sector—

exercise rulemaking and adjudicatory authority that is pervasively controlled by, and is indeed 'entirely derivative' of, the SEC." *Free Enter. Fund v. PCAOB*, 561 U.S. 477, 527 (Breyer, J., dissenting) (quoting *NASD v. SEC*, 431 F.3d 803, 806 (D.C. Cir. 2005)). "Congress has vested in the Commission the power to supervise SROs as a matter of public interest." Luis A. Aguilar, *The Need for Robust SEC Oversight of SROs* (May 8, 2013), *available at* https://www.sec.gov/news/public-statement/2013-spch050813laahtm. Consistent with the Commission's obligation to oversee SROs, including FINRA, "SROs must file their rule changes with the Commission" and "the Commission has the authority to inspect and examine SROs." *Id.* (citing 15 U.S.C. § 78s). To perform that task, the Commission created the FINRA and Security Industry Oversight ("FSIO") program within the Office of Compliance Inspections and Examinations.

Given the Commission's duty of oversight of FINRA in general, and over its disciplinary proceedings in particular, FINRA's position that the Commission should disregard the Ray Memorandum and Executive Order 13924 in connection with this appeal from a FINRA disciplinary action is nonsensical. By design, "[t]he "statutory scheme governing [FINRA's] actions parallels the Commission's internal adjudicative structures." *NASD*, 431 F.3d at 806. As the D.C. Circuit observed with respect to FINRA's predecessor, the National Association of Securities Dealers ("NASD"):

> The congressional scheme, in short, establishes a system in which the Commission not only closely supervises and approves the processes by which NASD brings disciplinary action, but in which the Commission fully revisits the issue of liability, and can completely reject or modify NASD's decision as it deems appropriate. NASD's disciplinary process essentially supplants a disciplinary action that might otherwise start with a hearing before an ALJ.

Id. To conclude that the Ray Memorandum and Executive Orders have no place in this process because FINRA is not an agency ignores the reality of the system Congress set up.

The Commission has repeatedly had to exercise that oversight authority to address the SROs' failure "to meet their legal and regulatory obligations under the law." Aguilar, *supra*. By way of example, the Commission has had to take action to sanction self-interested or discriminatory conduct by SROs including selective release of data by the NYSE; "self-interested" actions of the Boston Stock Exchange; selective enforcement by NYSE floor officials; and the NASD's failure to adhere to its own rules. *Id*.

The importance of the Commission's oversight of FINRA is reflected in the fact that the Dodd-Frank Act contained a provision directing the Government Accountability Office to prepare an initial report regarding the sufficiency of its oversight, and then triennially conduct reviews and report on the Commission's oversight of FINRA. In its initial report, the GAO identified flaws in the Commission's approach to its oversight of FINRA and made specific recommendations. *See generally* U.S. Gov't Accountability Off., GAO 15-376, *Securities Regulation: SEC Can Further Enhance Its Oversight Program of FINRA* (2015), *available at* https://www.gao.gov/assets/670/669969.pdf.

It is against that background that FINRA brushes aside the directives of the President and the Office of Management and Budget, including its statement that all agencies must specifically assess whether their regulations are properly incorporating principles of fairness and furthering the goals of economic recovery. According to FINRA, those mandates do not apply to it, either directly or by virtue of SEC oversight. It can pursue its own policies and need not adhere to the principles discussed in the Ray Memorandum that bind the agency itself. According to FINRA, essential principles barring "regulation by enforcement," the deployment of shifting arguments and unasserted claims, improper use of guidance, and the imposition of disproportionate sanctions,

do not "apply" to it. It need not assess application of the rule of lenity or incorporation of time-honored rules of evidence.

The Commission should soundly reject FINRA's claim that it answers to no authority, even that which is intended to apply across all aspects of administrative adjudication to assist a struggling national economy. The Commission should reiterate that, even if FINRA thinks that it can ignore the rules and principles applicable to "administrative adjudicators," its rules and procedures must be submitted to and approved by the Commission and so must (or at least should) be consistent with the mandates imposed on the Commission itself.

Finally, and perhaps more importantly, the Commission itself is an administrative agency subject to the contents of the Ray Memorandum and Executive Order 13924 and its reinforcement of principles of fairness across every department and agency of the government. As the Commission conducts this *de novo* review of the determination of the NAC, it should consider and apply those principles. And, as stated in the initial application, those principles reiterated in that Memorandum are *precisely applicable* to its review in this matter.

Dated: October 23, 2020

Respectfully submitted,

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ATTORNEY CERTIFICATION

Pursuant to Rule 154(c) of the Commission's Rules of Practice, I hereby certify that foregoing document contains 1082 words.

Kevin J. Harnisch

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CERTIFICATE OF SERVICE

I hereby certify that on October 23, 2020, I caused the foregoing to be served by email on the following:

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