No. 15-1416

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

TIMBERVEST, LLC, *ET AL.*,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

On Petition for Review of an Order of
the Securities & Exchange Commission

CORRECTED BRIEF OF *AMICUS CURIAE* CATO INSTITUTE IN SUPPORT OF PETITIONERS

Ilya Shapiro
Counsel of Record
Thaya Brook Knight
CATO INSTITUTE
1000 Mass. Ave., N.W.
Washington, D.C. 20001
(202) 842-0200
ishapiro@cato.org

May 2, 2016

COMBINED CERTIFICATES

Certificate as to Parties, Rulings, and Related Cases

As required by Circuit Rule 28(a)(1), counsel for *amicus curiae* Cato Institute certify as follows: Except for the Cato Institute, all parties, intervenors, and *amici* that have appeared in this Court are listed in the Petitioners' Brief. The rulings at issue and related cases also appear in the Petitioners' Brief.

Certificate of Counsel under Circuit Rules 29(c)(4) and 29(c)(5)

The Cato Institute was established in 1977 as a nonpartisan public policy research foundation dedicated to advancing the principles of individual liberty, free markets, and limited government. Toward those ends, Cato publishes books and studies, conducts conferences, issues the annual *Cato Supreme Court Review*, and files *amicus* briefs with the courts. Cato files this brief to address the implications of core separation-of-powers issues along with the democratic accountability of executive officers—issues that no other *amicus* brief covers.

Corporate Disclosure Statement

Pursuant to Federal Rule of Appellate Procedure 26.1, the Cato Institute certifies that it has no parent corporation, and no publicly held company has 10% or greater ownership in the Cato Institute. All parties have consented to this brief.

/s/ Ilya Shapiro
Ilya Shapiro
Counsel for *Amicus Curiae*

TABLE OF CONTENTS

TABLE OF AUTHORITIES

* Authorities upon which we chiefly rely are marked with an asterisk.

Cases

Constitutional Provisions

Regulations

Statutes

Other Authorities

GLOSSARY

ALJ – Administrative Law Judge

MSPB – Merit Systems Protection Board

STJ – Special Trial Judge

INTEREST OF *AMICUS CURIAE*[1]

The Cato Institute was established in 1977 as a nonpartisan public policy research foundation dedicated to advancing the principles of individual liberty, free markets, and limited government. Cato's Center for Constitutional Studies was established in 1989 to promote the principles of limited constitutional government that are the foundation of liberty. Cato's Center for Monetary and Financial Alternatives was established in 2014 to reveal the shortcomings of today's monetary and financial-regulatory systems and to identifying and promoting alternatives more conducive to a stable, flourishing, and free society. Toward those ends, Cato publishes books and studies, conducts conferences, issues the annual *Cato Supreme Court Review*, and files *amicus* briefs with the courts.

This case is important to Cato because it implicates core separation-of-powers issues along with the democratic accountability of executive officers.

SUMMARY OF ARGUMENT

The Constitution created three branches of government. The legislative and executive branches are controlled by the electorate. The president is vested with all executive power, and thus controls the executive branch. The president also has a

[1] No one other than the *amicus* and its counsel wrote this brief in whole or in part. The cost of its preparation was paid solely by *amicus*.

duty to see that the law is faithfully executed and to do this he must be able to remove those officers who fail in their respective duties.

And yet, administrative law judges ("ALJs") are protected from control by the electorate. The president does not have the ability to remove ALJs should they abuse their powers or fail to use their discretion to act intelligently or wisely.

Some have suggested that the quasi-judicial role of ALJs means they do not need to be subject to the president's control. This proposition was directly refuted by the Supreme Court 90 years ago, when it held that even for a quasi-judicial executive officer the president "may consider the decision after its rendition as a reason for removing the officer, on the ground that the discretion regularly entrusted to that officer by statute has not been on the whole intelligently or wisely exercised." *Myers v. United States*, 272 U.S. 52, 135 (1926). It is also refuted by precedent going back to the Founding in which the Comptroller of the Treasury was considered quasi-judicial for the same reasons as an ALJ, and was still removable by the president. The president has also removed territorial judges, demonstrating that the judicial character of an executive-branch office does not change the fact that the president must be able to remove those officers.

The remedy for this problem here requires dismissal because just removing the multiple for-cause removal barriers would reduce ALJs' independence and would implicate due process concern. The SEC can file this case again before an Article III court, the proper venue for the claims and remedies at issue.

Even if there were no violations of the Appointments Clause, the ALJs' selection process raises an inference of bias. The SEC, which is a party to the case, has selected this ALJ. The selection of a judge by a party to the case raises a reasonable fear of bias. The SEC naturally prefers ALJs who will support the agency's decisions. This has even lead to allegations that actual pressure has been placed upon SEC ALJs, as discussed in an article in the *Wall Street Journal*. Jean Eaglesham, *SEC Wins With In-House Judges*, Wall St. J., May 6, 2015. And yet the only finder of fact in this case is the ALJ. An independent record is needed.

Finally, this case was inappropriate for an administrative forum. Congress is limited in its ability to take cases away from Article III judges and place them into an administrative forum. While it can do this for new public rights, Congress cannot do this for an ancient common-law cause of action heard in courts of law at the Founding. The claim here is almost the same as an action in deceit at common law, which was a cause of action heard at the Founding in a court of law.

The claims and remedies at issue also raise Seventh Amendment concerns given that no option of a jury was provided to the defendants.

ARGUMENT

I. ADMINISTRATIVE LAW JUDGES' PROTECTION FROM REMOVAL IS UNCONSTITUTIONAL UNDER THE APPOINTMENTS CLAUSE

The U.S. Constitution guarantees that even those officers appointed (and not elected) are nonetheless accountable to the people. Although the Constitution includes no explicit guidance on removals, it has been understood to "empower the President to keep these officers accountable" including through the removal of the officers if necessary. *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 483 (2010). For this reason, the Supreme Court has found that if "the President cannot remove an officer who enjoys more than one level of good-cause protection" the removal structure "contravenes the President's constitutional obligation to ensure the faithful execution of the laws." *Id*, at 484 (internal quotation omitted).

A. The SEC's ALJs Are Executive Officers, So Their Removal Implicates Presidential Authority

The discretion and power exercised by ALJs renders them officers. There is no discernable difference between the powers exercised by ALJs and those exercised by the Special Trial Judge in *Freytag,* which were found to be executive officers by the Supreme Court. *Freytag v. C.I.R.,* 501 U.S. 868, 881-82 (1991). As in the case of the *Freytag* Special Trial Judges, SEC ALJs "perform more than ministerial tasks." *Id.* at 881. They also "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders." *Id.* at 881-82; 17 C.F.R. §201.111. And, as in the case of the Special Trial Judges, in the course of carrying out their duties, the ALJs "exercise significant discretion." *Freytag*, 501 U.S. at 881-82; 17 C.F.R. §201.111. Notably, ALJs use their discretion to make findings as to the credibility of witnesses and the SEC defers to ALJs' "credibility finding, absent overwhelming evidence to the contrary." *In re Clawson*, Exchange Act Release No. 48143, 2003 WL 21539920, at *2 (July 9, 2003); *In re Pelosi*, Securities Act Release No. 3805, 2014 WL 1247415, at *2 (Mar. 27, 2014) ("The Commission gives considerable weight to the credibility determination of a law judge since it is based on hearing the witnesses' testimony and observing their demeanor. Such determinations can be overcome only where the record contains substantial evidence for doing so."); *Universal Camera Corp. v. N.L.R.B.*, 340 U.S. 474, 496 (1951). ALJs also have the significant power of issuing opinions that are final unless appealed. 5 U.S.C. § 557(b); *Freytag*, 501 U.S. at 882 (noting that the fact that the STJ can "render the decisions of the Tax Court" in some cases is enough to be considered an officer).

This court's finding in *Landry v. F.D.I.C.*, that the ALJs of the Federal Deposit Insurance Corporation are not inferior officers, is inapposite. 204 F.3d 1125, 1132-1134 (D.C. Cir. 2000). Unlike decisions by FDIC ALJs, which are only recommendations and never a full agency decision, *id*. at 1133, actions by

SEC ALJs are expressly considered to be Commission actions if they are not reviewed by the commissioners. 15 U.S.C. § 78d-1(c) ("If the right to exercise such review is declined, or if no such review is sought within the time stated in the rules promulgated by the Commission, then the action of any . . . administrative law judge . . . shall, for all purposes, including appeal or review thereof, be deemed the action of the Commission."). Of course, this fact in itself is insufficient to render an SEC ALJ an inferior officer, because the delegation applies to many SEC employees. *Id.* But taken in conjunction with the considerable authority held by ALJs, as described above, it demonstrates that ALJs are more than mere employees. *See Freytag*, 501 U.S. at 910 (1991) (Scalia, J., joined by O'Connor, Kennedy, and Souter, JJ., concurring in part) (ALJs "are all executive officers").

B. The Removal Process Involves Two Layers of Protection, Resulting in an Unconstitutional Structure

SEC ALJs are inferior officers who are protected from removal by the president by at least two layers of for-cause removal protection. Permitting an executive officer to enjoy such insulation from removal unconstitutionally prevents the president from exercising the necessary control to be politically accountable for the actions of the officer. *Free Enter. Fund*, 561 U.S. at 477.

The first layer of protection exists at the SEC level. The SEC can only remove an ALJ "for cause." 5 U.S.C. § 7521(a). Second, that determination of cause must be confirmed by the Merit Systems Protection Board ("MSPB"), whose members can only be removed "for cause." *Id.*; 5 U.S.C. § 1202. Therefore, the judgment that an SEC ALJ should be removed for cause is "committed to another officer, who may or may not agree with the president's determination, and whom the President cannot remove simply because that officer disagrees with him." *Free Enter. Fund*, 561 U.S. at 484. Assuming the Court was correct in *Free Enterprise Fund* in accepting the SEC's assertion that commissioners themselves are removable only for cause, *Id*. at 487, there exist in fact three layers of protection between SEC ALJs and the president, as the commissioners themselves must initiate the removal proceedings against SEC ALJs. 5 U.S.C. § 7521(a).

C. ALJs Must Be Removable by the President to Ensure Democratic Accountability for Executive Officers

It has been understood since the Founding that the president, to fulfill his constitutional duty to ensure that the laws be faithfully executed, must have the power to remove executive officers. The Constitution does not specify how an officer can be removed (other than impeachment), and so a debate occurred in the First Congress over the presidential power to remove officers. Some felt that impeachment was the only proper method of removal because it was the only one specifically mentioned. James Madison disagreed, declaring that "it is absolutely necessary that the President should have the power of removing from office; it will make him, in a peculiar manner, responsible for their conduct, and subject him to impeachment himself, if he suffers them to perpetrate with impunity high crimes or misdemeanors against the United States, or neglects to superintend their conduct, so as to check their excesses." 1 Annals of Congress 387 (1789). Such a power to remove officers was seen at the time as "incident to the power of appointment." *Myers*, 272 U.S. at 110 (1926).

Madison did not consider this power to remove to be absolute, but "because Congress may establish offices by law," Congress could decide if the officer's tenure was "either during good behavior or during pleasure." 1 Annals of Congress 389 (1789). He likewise did not view a limitation on the president's ability to remove an executive officer only "for cause" as an impediment to the president's duty to "take Care that the Laws be faithfully executed" because "cause" includes a failure on the part of the officer to faithfully execute the laws. *Id.* at 389. In the end of the debate, the First Congress by a "considerable majority" resolved "the power of removal to be in the President." *Id.* at 399.

Despite Congress's authority to grant tenure for good behavior, as of 1903 "no civil officer [had] ever held office by a life tenure since the foundation of the government" with the exception of Article III judges. *Shurtleff v. United States*, 189 U.S. 311, 316 (1903). When Congress did limit the removal of a postmaster conditioned on congressional approval, the Supreme Court held that to be unconstitutional limitation on the power of the president. *Myers*, 272 U.S. at 176.

If a limitation on the president's removal power is unconstitutional, it is immaterial which entity exercises the limitation. If it would be unconstitutional to condition the president's removal power on the consent of the Senate, it would be equally unconstitutional to condition the removal power on the consent of the MSPB. As Madison said, if the executive officer "shall not be displaced but by and with the advice and consent of the senate, the President is no longer answerable for the conduct of the officer; all will depend on the senate. You here destroy a real responsibility without obtaining even the shadow." 1 Annals of Congress 394-95. Likewise if you say an ALJ cannot be removed by and with the advice and consent of the MSPB (which also cannot be removed but for cause), then the president would no longer be answerable for the conduct of the ALJ. When an ALJ goes beyond the powers of that office, but the MSPB refuses exercise its removal power, which elected official are the American people to blame?

D. ALJs' Quasi-Judicial Role Is Immaterial to the Removability Analysis

With a historical precedent going back to the Founding and direct on-point Supreme Court rulings, it is clear that the "quasi-judicial" nature of the ALJ position is not a legally significant distinction. The Court has held that even executive officers with a quasi-judicial role (such as ALJs) must not be beyond the president's power to remove any officer who fails to exercise the discretion required of the office intelligently or wisely. As it said in *Myers*:

> Then there may be duties of a quasi judicial character imposed on executive officers and members of executive tribunals whose decisions after hearing affect interests of individuals, the discharge of which the President cannot in a particular case properly influence or control. But even in such a case he may consider the decision after its rendition as a reason for removing the officer, on the ground that the discretion regularly entrusted to that officer by statute has not been on the whole intelligently or wisely exercised. Otherwise he does not discharge his own constitutional duty of seeing that the laws be faithfully executed.

272 U.S. at 135.

This power to remove quasi-judicial officer is not absolute as is the power to remove purely executive officers; Congress can limit the removal of such quasi-judicial executive officers to for-cause. *Humphrey's Executor v. United States*, 295 U.S. 602, 629 (1935). The removal for-cause still allows the president to see that the laws "be faithfully executed" but only so long as the president exercises direct authority to remove the officer for cause, or the power is exercised by an individual the President can remove without cause. *Free Enter. Fund*, 561 U.S. at 495-96. In this case, however, the multiple levels of for-cause removal prevent the president from directly addressing a situation in which the "discretion regularly entrusted to [an ALJ] by statute has not been on the whole intelligently or wisely exercised." *Myers*, 272 U.S. at 135.

Not only does the judicial precedent support the notion that quasi-judicial executive officers—including ALJs—must be removable by the president, but historical precedent does as well.

The first discussion of a quasi-judicial executive officer's removal occurred during the First Congress when considering the removal of the Comptroller of the Treasury. The Comptroller of the Treasury, due to his authority to decide claims between the United States and individual citizens, exercised power that was "not purely executive" but also included a "judicial quality." 1 Annals of Congress 635-36 (1789). Because of the quasi-judicial character of the office, Madison proposed that the tenure of the office be for "good behavior," but even so "the Comptroller would be dependent upon the President, because he can be removed by him." *Id.* Tenure based only on "good behavior" was necessary to "secure his impartiality," but even the need for impartiality was not sufficient to shield the officer entirely from the president's removal power. *Id.* Even this protection was too much for many of the other members of the First Congress and Madison eventually withdrew his motion. *Id.* at 637-39. When the Court revived Madison's position in *Humphrey's Executor*, however, the president still retrained the power to remove the quasi-judicial officer for cause.

And yet ALJs fulfill a more purely judicial function than either a member of the Federal Trade Commission or the Comptroller of the Treasury. Their function may be more properly analogous to other non-Article III federal judges. While the president has never removed an Article III judge—the Constitution insulates them from such action—the president has removed many Article I judges (such as territorial judges) without even giving cause and without congressional authorization. The power to remove such judges has been viewed as essential to the president's ability to fulfill his duty. Before the Civil War, Attorney General John J. Crittenden was specifically asked about the presidential power to remove territorial judges, even without specific congressional authorization. He concluded:

> The President of the United States is not only invested with authority to remove the Chief Justice of the Territory of Minnesota from office, but it is his duty to do so if it appear that he is incompetent and unfit for the place. . . . Being civil officers, appointed by the President, by and with the advice and consent of the Senate, and commissioned by the President, they are not exempted from that executive power which, by the constitution, is vested in the President of the United States over all civil officers appointed by him.

5 U.S. Op. Atty. Gen. 288, 290 (1851). He considered the power of such removals "has been long since settled, and the same has ceased to be a subject of controversy or doubt." *Id.*

In *McAllister v. United States* the Supreme Court interpreted the general statutory provisions for removal and replacement of "any civil officer . . . except judges of the courts of the United States" by the president to allow such removal of territorial judges. 141 U.S. 174 (1891). The quasi-judicial character of the office did not change the power of the president to remove executive officers appointed by him or by the heads of departments.

When considering Congress's removal of the Comptroller General, the Court stated that "[i]nterpreting a law enacted by Congress to implement the legislative mandate" and "exercis[ing] judgment concerning facts that affect the application of the Act" are "[d]ecisions of that kind are typically made by officers charged with executing a statute." *Bowsher v. Synar*, 478 U.S. 714, 733 (1986).

This Court, in *Kuretski v. C.I.R*, also considered the presidential removal of tax judges. In that case, the Court held: "A tribunal may be considered a 'Court of Law' for purposes of the Appointments Clause notwithstanding that its officers may be removed by the President. The *Freytag* Court's treatment of territorial courts confirms the point." *Kuretski v. C.I.R.*, 755 F.3d 929, 941 (D.C. Cir. 2014), *cert. denied*, 135 S. Ct. 2309 (2015).

These examples include executive officers' exercising quasi-judicial functions as well as judges in a "court of law." ALJs sit somewhere in the middle of this continuum. That it is well-settled that the president must have the power to remove officers sitting at both ends of this spectrum confirms that he must have the power to remove for cause officers sitting in the middle of it.

E. The Appropriate Remedy Here Is Dismissal without Prejudice

Eliminating one layer of removal protection would not alone address the constitutional tensions at the heart of the current SEC administrative process. The current process creates "constitutional discomfort." Kent Barnett, *Resolving the ALJ Quandary*, 66 Vand. L. Rev. 797, 809 (2013). First, the ALJ presiding over an enforcement action sits in a different position than an ALJ adjudicating, for example, an award of benefits. This distinction makes the executive's control over the ALJ a threat to due process. In a cases such as those typically overseen by ALJs at the Social Security Administration—the agency with the lion's share of the federal government's ALJs—the agency's role is as an "adjudicator and not as an advocate or adversary," and the executive's control over the ALJ would not be sufficient to disqualify the ALJ. *Richardson v. Perales*, 402 U.S. 389, 403 (1971). But, in the case of an enforcement action, such as the SEC's action against Timbervest, the executive stands in the role of both prosecutor and judge.

Additionally, the control the executive must exercise over the ALJ creates for the ALJ an impermissible interest in the outcome of the case. In *Tumey v. Ohio*, the Supreme Court found that a judge who had only a $12 (about $164 in 2016 dollars) interest in the outcome of the case to present a due process violation. 273 U.S. 510, 531-32 (1927); BLS, CPI Inflation Calculator (last visited April 22, 2016), http://www.bls.gov/data/inflation_calculator.htm. While the ALJ here had no pecuniary interest in what was being judged, the ALJ always has a pecuniary interest in keeping his job. That pecuniary interest is far more than $12 or even $164. This is not to impugn the president's integrity—and whether a president would actually remove an ALJ for such cause is irrelevant—but the president's removal power here, and the ALJs' perception of this power, are sufficient.

Every person has a "right to have claims decided before judges who are free from potential domination by other branches of government." *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 848 (1986). The SEC itself recognizes this and states that, "[a] system in which adjudicators are brought more directly within the President's control could undermine that impartiality." *In re Timbervest, LLC*, Release No. 4197, 2015 WL 5472520, at *28 (Sept. 17, 2015). The current structure creates a measure of distance between the executive and the ALJ, which can be argued to provide in some amount that protection afforded by lifetime tenure for Article III judges. *See, e.g.*, *Landry v. FDIC*, 204 F.3d 1125, 1131 (D.C. Cir. 2000) ("[I]n a challenge to the authority of a non-Article III court on the grounds that the challenger is entitled to a court enjoying Article III's exceptional tenure provisions, the assumption that inadequate tenure may prejudice the challenger is so automatic that it usually goes unmentioned.").

We agree with the commission that removing all but one layer of for-cause removal would undermine the ALJs' impartiality, but the remedy for a violation of the Constitution's guarantee of due process is not to retain a structure that violates the Constitution's appointments clause. Another remedy is necessary.

In *Freytag*, the Supreme Court "was ready to throw out the Tax Court's decision simply on the ground that special trial judges ("STJs") held what it viewed as clearly the powers of an 'inferior officer'" without the proper appointment. *Landry*, 204 F.3d at 1131-32. This is the appropriate remedy here: dismissal without prejudice. Such dismissal would prevent the case moving forward under a constitutional cloud while permitting the SEC to, if it so choose, file in district court before an Article III judge.

F. The SEC's Argument that the System Has Existed Since 1946 Is Incorrect—But Also Irrelevant to the Constitutional Question

The Commission claims that the system of appointment and removal applicable to SEC ALJs has "been in place since the Administrative Procedure Act was enacted in 1946." *In re Timbervest, LLC,* Release No. 4197, 2015 WL 5472520, at *28 (Sept. 17, 2015). But, under the laws at the time of the APA, the removal of an ALJ for-cause was reviewed by the U.S. Civil Service Commission. Pendleton Civil Service Reform Act, 22 Stat. 403 (1883). It was not until the Civil Service Reform Act of 1978 that the two layers of for-cause removal were added. And it was not until 2010, with its consideration of *Free Enterprise Fund*, that the Court considered the constitutionality of such a structure. 561 U.S. at 483.

Whether this system has been in place for 70 years is ultimately irrelevant if it is unconstitutional. See *Brown v. Bd. of Ed.*, 347 U.S. 483, 492 (1954) (separate but equal persisted for 86 years, but still unconstitutional); *Lawrence v. Texas*, 539 U.S. 558, 568, 572 (2003) (ancient laws prohibiting sodomy were unconstitutional). Under *Free Enterprise Fund* it is unconstitutional and therefore may not persist.

II. THE SEC'S SELECTION OF AN ALJ TO ADJUDICATE CASES IN WHICH IT IS A PARTY VIOLATES DUE PROCESS

The process for selecting ALJs violates due process because it permits the SEC to select the adjudicator who will serve as the sole finder of fact for hearings in which the SEC will be a party. That process begins with the Office of Personnel Management, which selects, for each ALJ vacancy at the SEC, three candidates. 5 U.S.C. § 3317. From among these candidates, the SEC itself selects the individual who will be offered the position of ALJ. 5 U.S.C. § 3318.

Such a process creates "fears of bias [which] can arise when—without the consent of the other parties—a man chooses the judge in his own cause." *Caperton v. A.T. Massey Coal Co.*, 556 U.S. 868, 886 (2009). Finding a lack of due process, of course, does not require proof of actual bias. *Id*. at 883. Instead, the question before the court is whether "under a realistic appraisal of psychological tendencies and human weakness" there is "such a risk of actual bias or prejudgment that the practice must be forbidden if the guarantee of due process is to be adequately implemented." *Withrow v. Larkin*, 421 U.S. 35, 47 (1975).

"Congress has recognized that the appearance of impartiality is as important as actual impartiality in maintaining the public confidence in" adjudication. *Verniero v. Air Force Acad. Sch. Dist. No. 20*, 705 F2d 388, 395 (1983).

In addition to the question of bias raised by the selection process, there are reasons to question whether the existing structure has actually compromised the ability of ALJs to function appropriately. An article appearing in the *Wall Street Journal* included several serious allegations regarding the impartiality of the SEC's ALJs. Jean Eaglesham, *SEC Wins With In-House Judges*, Wall St. J., May 6, 2015. A newspaper article cannot support a finding of actual bias, but given the severity of the allegations coupled with the selection process for ALJs, there is an appearance of bias that undercuts the legitimacy of the ALJ's fact finding in this case. *Caperton*, 556 U.S. at 884.

III. WITHDRAWING THIS ACTION FROM ARTICLE III COURTS VIOLATES THE SEPARATION OF POWERS AND DEPRIVES PETITIONERS OF THEIR RIGHT TO A JURY TRIAL

The SEC's ability to bring enforcement actions for fraud extends its reach beyond simply enforcing new public rights created by the acts it administers. It is true that precedent allows Congress to "create new public rights" and to "commit their enforcement, if it chose, to a tribunal other than a court of law such as an administrative agency in which facts are not found by juries." *Atlas Roofing Co. v. Occupational Safety & Health Review Comm;n*, 430 U.S. 442, 460 (1977). But Congress's ability to commit the enforcement of rights to administrative tribunals is limited by the Seventh Amendment's preservation of the right to jury trial, and by the principle of separation of powers.

"Congress may not withdraw from judicial cognizance any matter which, from its nature, is the subject of a suit at the common law, or in equity, or admiralty . . . . When a suit is made of the stuff of the traditional actions at common law tried by the courts at Westminster in 1789, and is brought within the bounds of federal jurisdiction, the responsibility for deciding that suit rests with Article III judges in Article III courts." *Stern v. Marshall*, 564 U.S. 462, 484 (2011) (internal quotations omitted). Additionally, "[t]he trial by jury is justly dear to the American people. It has always been an object of deep interest and solicitude, and every encroachment upon it has been watched with great jealousy." *Parsons v. Bedford, Breedlove & Robeson*, 28 U.S. 433, 446 (1830).

The violations with which the petitioners were charged are closely analogous to causes of action recognized at the founding as actions in law, and therefore must be brought before Article III judges. Moreover, because the legal remedies imposed by the SEC implicate petitioners' legal rights, petitioners have a right to a jury trial and therefore such an action must be brought in an Article III court to protect those same constitutional rights.

A. The Petitioners' Alleged Violations Are Analogous to Actions in Law at the Founding and Thus Belong to the Judicial Branch

Because deceit, similar for all purposes to the fraud alleged in the current case, was a cause of action sounding in law at the founding, the current case cannot be consigned to an administrative tribunal without violating the principle of separation of powers.

The ALJ found the petitioners to be liable under § 206(1) and (2) of the Investment Advisers Act of 1940, which proscribes "employing any device, scheme, or artifice to defraud any client" and "engag[ing] in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client." The violation with which the petitioners were charged includes very similar elements to an action in deceit in English common law. English common law at the founding included an action in deceit in which a person was liable for, "[a] false affirmation, made by the defendant with intent to defraud the plaintiff, whereby the plaintiff receives damage." *Pasley v. Freeman*, 100 Eng. Rep. 450 (K.B. 1789). In comparison, a violation of § 206(1) or (2) of the Investment Advisers Act requires a finding that petitioner "made a material misstatement or omission (or engaged in some other fraudulent activity), and that in so doing, it acted with the requisite level of culpability." *In re Timbervest, LLC*, Release No. 4197, 2015 WL 5472520, at *5 (Sept. 17, 2015). Additionally a finding of a violation of § 206(1) requires a finding that petitioner's "officers or employees must have acted with scienter, which is defined as a 'mental state embracing intent to deceive, manipulate, or defraud'" *Id*.

Because the cause of action here has a close analogy in law at the Founding, and does not concern a new "public right" against the government created by congress, the case must be decided by an Article III judge to preserve appropriate separation of powers. In rejecting the dissent in *Stern v. Marshall*, the Supreme Court cited the dissent's claim regarding *Northern Pipeline* as "establish[ing] only that Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without consent of the litigants, and subject only to ordinary appellate review." *Stern*, 564 U.S. at 494. Except the majority opinion went further, noting that "[s]ubstitute 'tort' for 'contract,' and that statement directly covers this case." *Id.* As in *Stern*, this case involves a traditional common law tort (an action in deceit), being resolved by a non-Article III tribunal. As established in *Stern*, removing such cases from Article III courts violates the principle of separation of powers and is therefore not permissible. See *Id.* at 495.

B. The Relief Sought Implicates a Legal Right and Therefore Petitioners Have a Right to a Jury Trial

The question of whether the cause of action was available at the time of founding is also relevant to the question of whether petitioners had a right to a jury trial, but it is not dispositive. *Tull v. United States*, 481 U.S. 412, 420-21 (1987) (concluding that if appropriate analogies could have been heard in either a court of equity or court of law that is sufficient for a jury trial requirement). In determining whether a right to jury trial exists "characterizing the relief sought is '[m]ore important' than finding a precisely analogous common-law cause of action in determining whether the Seventh Amendment guarantees a jury trial." *Id*. at 421 (citing *Curtis v. Loether*, 415 U.S. 189, 196 (1974)). In this case, the defendant has been prohibited from associating with a variety of groups and individuals, in essence limiting the defendant's fundamental right of association with those people under the First Amendment. Jury trials must be available for any "suit[] in which legal rights were to be ascertained and determined." *Parsons*, 28 U.S. at 434.

Petitioners have been permanently "barred from associating with any investment adviser." *In re Timbervest, LLC*, Release No. 4197, 2015 WL 5472520, at *1. "It is beyond debate that freedom to engage in association for the advancement of beliefs and ideas is an inseparable aspect of the 'liberty' assured by the Due Process Clause of the Fourteenth Amendment, which embraces freedom of speech." *NAACP v. State of Ala. ex rel. Patterson*, 357 U.S. 449, 460 (1958). The petitioners have had their legal right to associate with investment advisors for the advancement of beliefs and ideas *eliminated*; this is far more than a mere license revocation. The elimination of any constitutional right must be a "suit[] in which legal rights were to be ascertained and determined" which requires the option of a jury trial. *Parsons*, 28 U.S. at 434.

Of course defendants may waive their right to a jury trial. But that is not what happened in this case. Unlike the defendant in *Schor*, Petitioners have not "freely elected to resolve their differences before the" SEC, nor are the SEC's "orders . . . enforceable only by order of the district court." *Stern*, 564 U.S. at 491.

CONCLUSION

It is up to this Court to see that our government remains democratically accountable; that the bias of allowing a party to select its own judge not be allowed to stand; and to protect the judicial branch from being assigned away to administrative tribunals without even a jury trial to protect constitutional rights. Accordingly, *amicus* asks this Court to reverse the SEC.

Respectfully submitted this 2nd day of May, 2016,

Ilya Shapiro
*Counsel of Record**
Thaya Brook Knight
CATO INSTITUTE
1000 Mass. Ave., N.W.
Washington, D.C. 20001
(202) 842-0200
ishapiro@cato.org
tknight@cato.org

* Counsel would like to thank George Mason University School of Law student Devin Watkins for his help with this brief.

CERTIFICATE OF COMPLIANCE

1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because it contains 5,611 words, excluding the parts exempted by Fed. R. App. P. 32(a)(7)(B)(iii) and D.C. Cir. Rule 32(a)1.
2. This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because it has been prepared in a proportionally spaced typeface using Microsoft Word 2013 in Times New Roman, 14 point font.

/s/Ilya Shapiro
Ilya Shapiro
Counsel for *Amicus Curiae*

CERTIFICATE OF SERVICE

I hereby certify that, on May 2, 2016, I filed the foregoing brief with this Court by causing a true digital copy to be electronically uploaded to the Court's CM/ECF system and by causing nine true and correct copies to be delivered by FedEx next business day delivery to the Court. Service was accomplished by the CM/ECF system on the following counsel, who are registered CM/ECF users:

Dominick V. Freda
Michael Andrew Conely
Daniel Staroselsky
SECURITIES & EXCHANGE COMMISSION
Office of the General Counsel
100 F. Street, N.E.
Washington, D.C. 20549-9040
(202) 551-5143
fredad@sec.gov
conleym@sec.gov
staroselskyd@sec.gov

George Kostolampros
Nancy R. Grunberg
Lawrence S. Ebner
DENTONS US LLP
1900 K Street, N.W.
Washington, D.C. 20006
(202) 496-7500
george.kostolampros@dentons.com
nancy.grunberg@dentons.com
lawrence.ebner@dentons.com

/s/Ilya Shapiro
Ilya Shapiro
Counsel for *Amicus Curiae*