19-4197-cv

United States Court of Appeals

for the

Second Circuit

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellee,

– v. –

BARRY D. ROMERIL,

Defendant-Appellant,

PAUL A. ALLAIRE, G. RICHARD THOMAN, PHILIP D. FISHBACH, DANIEL S. MARCHIBRODA, GREGORY B. TAYLER,

Defendants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR *AMICUS CURIAE* AMERICANS FOR PROSPERITY FOUNDATION IN SUPPORT OF DEFENDANT-APPELLANT

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RULE 26.1 CORPORATE DISCLOSURE STATEMENT

Amicus curiae Americans for Prosperity Foundation is a 501(c)(3) nonprofit corporation. It has no parent companies, subsidiaries, or affiliates that have issued shares or debt securities to the public.

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INTEREST OF *AMICUS CURIAE*[1]

Amicus curiae Americans for Prosperity Foundation ("AFPF") is a 501(c)(3) nonprofit organization committed to educating and training Americans to be courageous advocates for the ideas, principles, and policies of a free and open society. Some of those key ideas include the separation of powers and constitutionally limited government, as well as bringing the administrative state in line with the U.S. Constitution. As part of this mission, AFPF appears as *amicus curiae* before state and federal courts.

Tyranny begins where a government silences its critics. AFPF has a particular interest in this case because it believes agency "gag clauses" wrongfully insulate government officials from accountability. People and companies—even those that may have violated a securities law—have First Amendment rights, which the government should not be permitted to strip.[2] The First Amendment, AFPF believes, prohibits the government from imposing prior restraints on truthful speech about

[1] Pursuant to FRAP 29(a)(4)(E), *amicus curiae* states that no counsel for a party other than AFPF authored this brief in whole or in part, and no counsel or party other than AFPF made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus curiae* or its counsel made a monetary contribution to its preparation or submission. All parties have consented to the filing of this brief.

[2] AFPF takes no position as to whether Mr. Romeril, in fact, engaged in the charged conduct. Nor does it take a position as to whether the factual allegations in the SEC complaint are true.

matters of public concern. This prohibition extends to targets of government investigations and enforcement actions, regardless of whether the target did anything actionable. Agency "gag clauses," like the one at issue here, not only violate the First Amendment and due process but also wrongly insulate agency officials from meaningful oversight and shield them from accountability.

AFPF stands opposed to agency policies that demand the inclusion of unconstitutional speech bans in agency settlement agreements. Such bans are unenforceable, violate the First Amendment, and are poor public policy that hinders oversight.[3] They are an unjustifiable—and highly successful—muzzling of public criticism of agency action. AFPF believes that the Judiciary must direct agencies like the Securities and Exchange Commission ("SEC") and the Commodity Futures Trading Commission ("CFTC") to abandon their policies of barring settling defendants in perpetuity from publicly disputing the validity of the agency's liability theory and factual allegations.

SUMMARY OF ARGUMENT

"*E pur si muove*" (and yet it moves). The SEC's policy of demanding gag clauses in settlements is reminiscent of Galileo Galilei's fabled mumbled disclaimer after he was forced—on threat of torture—by authorities to publicly recant his

[3] *See* James Valvo, *The CFTC and SEC Are Demanding Unconstitutional Speech Bans in Their Settlement Agreements*, Yale Journal on Regulation (Dec. 4, 2017), https://bit.ly/3a8XDUu.

discovery that the Earth revolves around the Sun. As with the then-official position that the Sun revolves around the Earth, the simple fact is that not *all* allegations in SEC complaints are true—regardless of whether they are ultimately resolved through a settlement agreement with a gag provision.

The SEC gag-clause policy that purports to prevent defendants from ever denying allegations against them suppresses speech critical of the government. The SEC recognizes as much by including what it has described as "escape valves even as to denials of the allegations" such as "[a] defendant 'may testify truthfully about any matter under oath in connection with a legal or administrative subpoena,' which could include a denial of an allegation."[4] If a defendant can *truthfully* deny an allegation in an SEC complaint under oath, then the veracity of the allegation is, at the least, open to interpretation, if not false. By implication, then, the SEC can use the gag provision to suppress truth, substituting instead its own narrative. And the SEC has in fact admitted to using the gag provision to compel private individuals and companies to "retract" or otherwise change their prior public statements.

Agencies should not be permitted to muzzle, in perpetuity, targets of their investigations through gag provisions forced into settlement agreements memorialized in consent orders. Such prior restraints on truthful speech are not only

[4] Mem. in Supp. of Defs.' Mot. to Dismiss, Dkt. No. 12-1, at 29, *Cato Inst. v. SEC*, No. 19-47 (D.D.C. filed May 10, 2019).

void *ab initio* as against public policy but also profoundly unconstitutional, regardless of whether the settling defendant did anything wrong and even if some of the allegations in the agency's complaint are true.

As litigators who have drafted or responded to a complaint would recognize, it blinks reality and defies common sense to suggest that every allegation in a complaint is objectively accurate. As one district court put it, "[b]y definition, an allegation is an assertion without proof. Plaintiff[s] should heed the legal maxim—innocence until proven guilty."[5] Federal Rule of Civil Procedure 8 makes this pellucidly clear. This maxim holds true even where agencies may have a practice of "negotiating" the content of the complaint with the would-be settling defendant.[6]

Agencies may try to justify their unconstitutional gag orders using a circular "trust us, we're the government" line of reasoning: that is, if the target didn't do what was alleged in the agency's complaint, it would not have settled, therefore the target is a bad actor and allegations in the complaint are true. Not so. Regardless, even those who have engaged in misconduct should not be forced to bargain away their First Amendment rights in perpetuity.

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[5] *Rottmund v. Cont'l Assurance Co*., 761 F. Supp. 1203, 1207 (E.D. Pa. 1990).

[6] Settling defendants "often seek and receive concessions concerning the violations to be alleged in the complaint, the language and factual allegations in the complaint, and the collateral, administrative consequences of the consent decree." *SEC v. Clifton*, 700 F.2d 744, 748 (D.C. Cir. 1983).

It is critically important for this Court to be aware of the tremendous disparity in bargaining power and resources between governmental and private parties. It must also consider that many agencies sometimes force targets into settling on unfair terms. Companies may be coerced into settlement because the time, monetary, and reputational costs of fighting are simply too high, or to avoid the uncertainty of litigation and get back to business. Gag clauses prevent the public from learning the extent to which agencies may pursue meritless, unjustified investigations and enforcement actions, as the subjects of such actions are gagged from speaking. Some or all of the allegations in an SEC complaint that accompanies a consent order with a gag provision simply may not be true, or, at the least, are only true in part or open to interpretation. In practice, this means the gag provisions may operate to suppress truthful speech critical of the government, while enshrining in perpetuity a false or misleading government-propagated narrative. Worse, the SEC has shown a willingness to invoke the gag clause to *compel* pro-government speech. That is profoundly unconstitutional. The SEC has no legitimate interest in suppressing the truth about its actions. The First Amendment flatly prohibits it.

SEC gag provisions have two more flaws. First, they cannot satisfy the most basic requirement of due process—fair notice of prohibited or required conduct—or comply with Rule 65(d)'s specificity requirements. Second, the agency's wrongful practice of chilling the exercise of First Amendment rights prevents Congress from

performing its core Article I oversight function, as well as inhibits Executive branch efforts to address and prevent agency overreach.

This Court should reverse the district court and hold the gag clause violates the First Amendment, is void as against public policy, and is unenforceably vague.

ARGUMENT

I. The SEC Gag Clause is Void *Ab Initio* as a Prior Restraint on Truthful Speech that Violates the First Amendment.

Consent judgments have "attributes both of contracts and of judicial decrees." *United States v. ITT Cont'l Baking Co.*, 420 U.S. 223, 236 & n.10 (1975). Consent judgments should be interpreted and construed as a contract. *Id.* at 238. To be enforceable, they must not be illegal or contrary to sound policy. *See Mills v. Everest Reinsurance Co.*, 410 F. Supp. 2d 243, 253 (S.D.N.Y. 2006). *Cf. In re CFTC*, 941 F.3d 869, 873 (7th Cir. 2019) ("So if we understand the consent decree as an effort to silence individual members of the Commission, it is ineffectual[.]"). Consent orders may be void as against public policy, even where the government is a party. *See, e.g.*, *Overbey v. Mayor of Balt.*, 930 F.3d 215 (4th Cir. 2019); *Fomby-Denson v. Dep't of the Army*, 247 F.3d 1366, 1377–78 (Fed. Cir. 2001) (settlement agreement cannot silence defendant from making a report about plaintiff to authorities); *Crosby v. Bradstreet Co.*, 312 F.2d 483, 485 (2d Cir. 1963). Moreover, a court cannot enter an order that "constitutes a prior restraint by the United States against the publication of facts which the community has a right to know and which

[defendant] . . . has the right to publish[.]" *Crosby* 312 F.2d at 485. Whether "the parties may have agreed to it is immaterial." *Id.* Therefore—whether as contract or judicial decree—consent orders may only include terms that are lawful and consistent with public policy.

A. The Gag Clause is An Unconstitutional Prior Restraint on Speech.

"On its face, the SEC's no-denial policy raises a potential First Amendment problem." *SEC v. Citigroup Glob. Mkts. Inc.*, 827 F. Supp. 2d 328, 333 n. 5 (S.D.N.Y. 2011) (Rakoff, J.), *vacated and remanded on other grounds*, 752 F.3d 285 (2d Cir. 2014).[7] A provision in a consent order that is a prior restraint on truthful speech violates the First Amendment. *Crosby*, 312 F.2d at 485. That is exactly what the gag provision here does. It prevents Mr. Romeril from exercising his First Amendment rights by "prohibit[ing him] from disputing the truth of any of the allegations made against [him or other] defendants . . . and . . . [preventing him from] 'tak[ing] any action or mak[ing] . . . any public statement denying . . . any allegation in the complaint or creating the impression that the complaint is without factual basis.'" Mot. for Relief from J., Dkt. No. 23, Ex. B, ¶ 4 (Romeril Aff.), *SEC v.*

[7] "This might be defensible if all that were involved was a private dispute between private parties. But here an agency of the United States is saying, in effect, 'Although we claim that these defendants have done terrible things, they refuse to admit it and we do not propose to prove it, but will simply resort to gagging their right to deny it.'" *SEC v. Vitesse Semiconductor Corp.*, 771 F. Supp. 2d 304, 309 (S.D.N.Y. 2011).

Allaire, No. 03-cv-4087 (S.D.N.Y. filed May 6, 2019) (citation omitted). That provision is unconstitutional.

The First Amendment bars the government from imposing content-based prior restraints on speech enforced by threats of prosecution. *Bantam Books, Inc. v. Sullivan*, 372 U.S. 58, 68–71 (1963). An "injunction, so far as it imposes prior restraint on speech and publication, constitutes an impermissible restraint on First Amendment rights." *Org. for a Better Austin v. Keefe*, 402 U.S. 415, 418 (1971). The SEC gag clause is exactly that. Worse, the SEC uses the gag provision to *compel* pro-government speech through forced "retractions."

B. Enforced Silence About Truthful Matters is an Unconstitutional Condition of Settlement.

The SEC has a long history of imposing this unconstitutional condition of settlement. *Cf. Crosby*, 312 F.2d at 485. Since 1972, the SEC has systematically muzzled settling defendants and respondents, announcing that it would not "permit a defendant or respondent to consent to a judgment or order that imposes a sanction while denying the allegations in the complaint or order for proceedings."[8] 17 C.F.R. § 202.5(e). This policy "prohibit[s] settlement agreements in which a defendant

[8] In 1972, the SEC amended its Rules of Practice and began requiring settling defendants to state they did not deny the allegations against them. *See* Consent Decrees in Judicial or Administrative Proceedings, Securities Act Release No. 33-5337 (Nov. 28, 1972) (codified at 17 C.F.R. § 202.5(e)). Other federal agencies have codified similar policies. *See* 17 C.F.R. § 10 app. A (CFTC); 40 C.F.R. § 22.18 (EPA); 7 C.F.R. § 110.8 (USDA); 45 C.F.R. § 672.11 (Nat'l Sci. Found.).

consents to a judgment that imposes a sanction while denying the allegations in the complaint." *SEC v. Allaire*, No. 03-4087, 2019 U.S. Dist. LEXIS 199887, at *3 (S.D.N.Y. Nov. 18, 2019). According to the SEC, "in any civil lawsuit brought by [the SEC] or in any administrative proceeding of an accusatory nature pending before it, it is important to avoid creating, or permitting to be created, an impression that a decree is being entered or a sanction imposed, when the conducted alleged did not, in fact, occur." 17 C.F.R. § 202.5(e). Under this policy, "[s]ilence was not allowed. The SEC announced that it would treat 'refusal to admit the allegations' as 'equivalent to a denial' unless the settling target explicitly stated that 'he neither admits nor denies the allegations.'" Verity Winship & Jennifer K. Robbennolt, *An Empirical Study of Admissions in SEC Settlements*, 60 Ariz. L. Rev. 1, 5 (2018).

Consistent with this policy, the gag provision here states:

> Defendant understands and agrees to comply with the [SEC]'s policy 'not to permit a defendant . . . to consent to a judgment or order that imposes a sanction while denying the allegations in the complaint . . . .' In compliance with this policy, Defendant agrees not to take any action or to make or permit to be made any public statement denying, directly or indirectly, any allegation in the complaint or creating the impression that the complaint is without factual basis. If Defendant breaches this agreement, the [SEC] may petition the Court to vacate the Final Judgment and restore this action to its active docket.

Allaire, 2019 U.S. Dist. LEXIS 199887, at *3 (quoting 17 C.F.R. § 202.5).

Notably, this gag provision contains two exemptions, which underscore its truth-suppressing functions: "Nothing in [the provision] affects Defendants: (i)

testimonial obligations; or (ii) right to take legal or factual positions in litigation in which the [SEC] is not a party." *Id.* What is the purpose of this provision? One explanation is that the SEC wishes to avoid judicial scrutiny of its efforts to silence settling targets.[9] Another related explanation may be that the absence of the exemption would interfere with the defendant's or respondent's ability to testify truthfully, in essence requiring them to lie under oath—a compelled crime that would open a Pandora's Box of constitutional violations. In other words, sometimes the allegations in the complaint are not true[10]—a reality the SEC acknowledges.[11] Senator Tom Cotton recently explained that this "wrinkle in the rule . . . implies [the SEC gag rule] might require [a settling defendant] to say something untruthful" in public. Sen. Tom Cotton Q&A During Banking Comm. Hearing at 1:53–2:08 (Dec.

[9] "These are strategic exemptions for the agencies to include because they prevent the settlement agreements from coming to the attention of a judge in a future proceeding who would have the power to object to and invalidate the restraint on speech." James Valvo, *The CFTC and SEC Are Demanding Unconstitutional Speech Bans in Their Settlement Agreements*, Yale Journal on Regulation (Dec. 4, 2017), https://bit.ly/3a8XDUu.

[10] The SEC has acknowledged this: "A defendant 'may testify truthfully about any matter under oath in connection with a legal or administrative subpoena,' which could include a denial of an allegation[.]" Mem. in Supp. Def. Mot. to Dismiss at 3, Dkt. No. 12-1, *Cato Inst. v. SEC et al.*, No. 19-47 (D.D.C. filed May 10, 2019).

[11] The SEC stated below that "[t]he no-deny provision also contains an exception to allow denials in certain circumstances. The exception permits Romeril to testify truthfully about any matter under oath in connection with a legal or administrative subpoena." Mem. Opp'n to Mot. for Relief from J. at 23, Dkt. No. 31, *SEC v. Allaire*, No. 03-4087 (S.D.N.Y. filed June 18, 2019) (cleaned up).

11, 2018), *available at* https://bit.ly/3dZEIxL. In response, SEC Chairman Jay Clayton did not attempt to refute the argument, replying instead: "It's a result of the unique nature of testifying in those types of situations." *Id.* at 2:16–22. Senator Cotton then inquired: "So it's okay to have defendants that have reached a settlement with the SEC say things to the public that might be untruthful but not to say them in court? We're talking about a prior restraint on speech that is also content-based." *Id.* at 2:23–35. The Chairman did not directly address the point, a troubling red flag.

The SEC dismisses such objections to its gag provisions largely on the ground that defendants purportedly consent to the agency's First Amendment violations, which are later blessed by the court. *But see Crosby,* 312 F.2d at 485. According to the SEC, "Romeril . . . agreed to this silence[.]" Mem. in Opp'n to Mot. for Relief from J. at 13, Dkt. No. 31, *SEC v. Allaire*, No. 03-4087 (S.D.N.Y. filed June 18, 2019). But Mr. Romeril's purported waiver of his First Amendment rights "is enforceable only if it meets two conditions: First, it was made knowingly and voluntarily. Second, under the circumstances, the interest in enforcing the waiver is not outweighed by a relevant public policy that would be harmed by enforcement." *Overbey*, 930 F.3d at 223. Here, that test is not met. Mr. Romeril's interest in speaking about his experience far outweighs the SEC's interest in keeping him silent.

The SEC's gag-clause policy must be viewed "against the background of a profound national commitment to the principle that debate on public issues should

be uninhibited, robust, and wide-open, and that it may well include vehement, caustic, and sometimes unpleasantly sharp attacks on government and public officials." *N.Y. Times Co. v. Sullivan*, 376 U.S. 254, 270 (1964). "It is well-established that . . . [such] 'sharp attacks on government and public officials' can play a valuable role in civic life and therefore enjoy the protections of the First Amendment." *Overbey*, 930 F.3d at 226 (quoting *Sullivan*, 376 U.S. at 270). "Enforcing a waiver of First Amendment rights for the very purpose of insulating public officials from unpleasant attacks would plainly undermine that core First Amendment principle." *Id.* at 226. The SEC's use of the gag provision to "avoid harmful publicity stumbles out of the gate[.]" *Id.*

Against that backdrop, the SEC claims the agency's policy of gagging settling defendants in perpetuity is supported by putative "compelling reasons": "denials of allegations following entry of a consent judgment undermine the authority of the Court that approved it, undercut the factual basis for the action and the relief obtained, and create confusion for investors and the market." Mem. in Opp'n to Mot. for Relief from J. at 1, Dkt. No. 31, *SEC v. Allaire*, No. 03-4087 (S.D.N.Y. filed June 18, 2019). Not so. Allowing a settling defendant to deny liability subsequent to entry of a consent judgment does not somehow undermine the

authority of the Court. Settlements are, by definition, the product of compromise and negotiation and thus no-fault settlements are customary. *See* Section IV, *infra*.

Elsewhere, the agency has said it "has an interest in . . . ensuring that denials do not undercut the deterrent effect of describing the allegations." Mem. in Supp. of Defs.' Mot. to Dismiss at 3, Dkt. No. 12-1, *Cato Inst. v. SEC*, No. 19-47 (D.D.C. filed May 10, 2019). That purported justification also falls flat with respect to both specific and general deterrence, given the severe relief the SEC routinely obtains in settlements, such as crippling fines—whether labeled as civil penalties or "disgorgement"—that may bankrupt defendants and lifetime bans from serving as an officer of a publicly traded company. Allowing a settling officer to publicly dispute the validity of the SEC's charges or assert that he was over-prosecuted does not meaningfully diminish the deterrent effect of these sanctions.

The SEC also complains that "[i]f a settling defendant can deny the allegations in the complaint after consenting to a judgment[, . . . it] would create public confusion about the accuracy of the allegations in the complaint, which are resolved without a trial. It could also undermine confidence in the Commission's enforcement program by creating an unfair impression that there was no factual or legal basis for the Commission's enforcement action." *Id.* at 27. This appeal to "fairness" fails. The SEC's strawman argument that the public would somehow lose

faith in the SEC's mission if settling defendants are permitted to dispute the evidence and criticize the integrity of the government prosecution should be rejected.

Consider, by way of analogy, the criminal law. Defendants, whether innocent or guilty, routinely waive some constitutional rights when pleading guilty, including the rights to a jury trial and to confront and cross-examine witnesses. *See generally Class v. United States,* 138 S. Ct. 798, 805–06 (2018). Yet plea bargains are not routinely conditioned on barring the defendant from publicly protesting his innocence or barring the defendant from publicly alleging police or prosecutorial misconduct. Criminal defendants who have pleaded guilty routinely publicly proclaim their innocence, allege misconduct, or otherwise criticize the criminal justice system. Whatever other flaws our criminal justice system may have, the fact that even convicted defendants may openly criticize it is a strength not a weakness, a source of legitimacy, and a driving force for reform.

Put simply, courts should never "ratif[y] the government's purchase of a potential critic's silence merely because it would be unfair to deprive the government of the full value of its hush money." *Overbey*, 930 F.3d at 226. Competing accounts and differing opinions about the validity of government assertions is a hallmark of a free and open society, and a core value protected by the First Amendment. The

SEC's thin-skinned aversion to public criticism is not; to the contrary, its gag rule reveals an insecurity that it cannot answer criticism about the quality of its work.

In essence, the SEC's position is that its interest in unchallenged favorable publicity outweighs the public's interest in learning the truth.[12] But as Judge Jed Rakoff explained: "[T]here is an overriding public interest in knowing the truth. In much of the world, propaganda reigns, and truth is confined to secretive, fearful whispers. Even in our nation, apologists for suppressing or obscuring the truth may always be found. But the SEC . . . has a duty, inherent in its statutory mission, to see that the truth emerges[.]" *Citigroup Global Mkts*., 827 F. Supp. 2d at 335. But the SEC has a policy of refusing to do so.

Any suggestion the provision furthers a general interest in using settlements to expedite resolution and conserve government and judicial resources should also be rejected. "[W]hen a settlement agreement contains a waiver of a constitutional right, the government's general interest in using settlement agreements to expedite litigation is not enough to make the waiver enforceable—otherwise, no balance-of-interests test would be required." *Overbey*, 930 F.3d at 225. Such is the case here.

[12] The SEC's concern is with public, not private, speech: "A defendant can make private statements . . . without breaching the no-deny provision, as the anonymous manuscript author and the other settling defendants have already done." Mem. of Points & Authorities in Supp. of Defs.' Mot. to Dismiss at 29, Dkt. No. 12-1, *Cato Inst. v. SEC*, No. 19-47 (D.D.C. filed May 10, 2019).

C. The SEC Uses the Gag Clause to Actively Censor Speech and Compel Pro-Government Speech.

The SEC, in practice, uses the gag clause not only to censor speech but to compel settling defendants and respondents to make pro-government statements. As a former Director of the SEC's Division of Enforcement has candidly advised, "the SEC goes one step further [than other agencies] and not only prohibits defendants from denying wrongdoing in a settlement, but has demanded a retraction or correction on those occasions when a defendant's post-settlement statements are tantamount to a denial." *Examining the Settlement Practices of U.S. Financial Regulators*, Hearing Before H. Comm. on Fin. Servs., 112th Cong. (2012) (statement of Robert Khuzami, Dir., Div. of Enforcement, Secs. & Exchange Comm'n).

Take, for example, the case of Michael Angelos. The SEC "construed" "[s]tatements made on behalf of" him "as denials of the allegations in the Complaint," filing a motion to vacate the settlement. *See* Secs. & Exchange Comm'n, Litigation Release No. 14886 (Apr. 22, 1996), *available at* https://bit.ly/34hrh84 (regarding *SEC v. Michael P. Angelos*, No. B96-834 (D. Md.)). The SEC conditioned withdrawal of its motion on a statement from Mr. Angelos:

> I settled this case without admitting or denying the allegations of the complaint. To comply with my settlement with the [SEC], I withdraw any statement made on my behalf that may have been inconsistent therewith. I am pleased that this settlement resolves the SEC's lawsuit

> against me. I will have no further comment other than any sworn testimony I may give in this or any other matter.

Id.

More recently, the SEC weaponized the gag clause in a very public dispute with Morgan Stanley. In 2003, "the day after the details of the settlement were announced" Morgan Stanley's CEO reportedly told investors at a conference: "'I don't see anything in the settlement that will concern the retail investor about Morgan Stanley. Not one thing.' A reporter from *The New York Times* attended the conference" and published an article the next day. Floyd Norris, *Morgan Stanley Draws S.E.C.'s Ire*, N.Y. Times (May 2, 2003), https://bit.ly/2wWt5Hj. Immediately thereafter, the SEC Chairman wrote a scathing letter to the CEO; apparently, according to agency officials, the CEO's "remarks had been regarded as cavalier and had provoked anger at the agency." *Id*.

The SEC Chairman's "letter began with a reference to the *Times* article." *Id*. Although the CEO had merely expressed his opinion that the settlement itself should not concern investors, and did not even purport to comment on or deny the allegations in the SEC's complaint, the SEC felt that Morgan Stanley did not express sufficient "contrition" for the agency's purposes. The Chairman wrote:

> I am deeply troubled that you would suggest that Morgan Stanley's conduct, *as described in the Commission's complaint,* was not a matter of concern to retail investors. My concerns are two-fold. First, your statements reflect a disturbing and misguided perspective on Morgan Stanley's *alleged* misconduct. *The allegations in the Commission's*

> *complaint* against Morgan Stanley are extremely serious. . . . In light of these charges, your reported comments evidence a troubling lack of contrition[.]
>
> Second, I wish to remind you that among the terms of the settlement to which Morgan Stanley agreed is a requirement that the firm . . . do not deny the Commission's allegations. Like every term of the settlement, this is a legal obligation assumed by the firm (and certainly applicable to you as CEO), that is enforceable by the court. I caution you that the Commission would regard a violation of that obligation as seriously as a failure to comply with any other term of the settlement[.]

Excerpts from Exchange of Letters, N.Y. Times (May 2, 2003) (emphasis added), https://nyti.ms/2V6sZoj.

The SEC's threatening letter had its intended effect, leading Morgan Stanley not only to retract its statement of opinion but publicly *praise the SEC for its efforts*:

> I deeply regret any public impression that the Commission's complaint was not a matter of concern to retail investors. Morgan Stanley views seriously the allegations that the SEC and other regulators have made in their complaints and agrees the allegations are a matter of concern to retail investors[.]
>
> *The reforms, established through the leadership of the SEC and other regulators, are a positive for retail investors, not a concern for retail investors*. We will go forward in the spirit of our agreement to make research and markets better for all investors. I appreciate your reminder on the terms of the settlement and can assure you that no one at Morgan Stanley will violate the settlement agreement's prohibition against denying the Commission's allegations.

Id. (Philip J. Purcell, Morgan Stanley CEO) (emphasis added).

This government-compelled pro-SEC speech is unconstitutional. *See Wooley v. Maynard*, 430 U.S. 705, 714 (1977); *West Virginia State Bd. of Ed. v. Barnette*,

319 U.S. 624 (1943); *see also Pac. Gas & Elec. Co. v. Pub. Utils. Comm'n*, 475 U.S. 1, 16 (1986) (corporations are protected against compelled speech). Moreover, to the extent the Morgan Stanley CEO's initial remarks were truthful and accurate (and later retraction, less so), it raises the troubling specter that the SEC's sensitivity to its public image is more pressing than its mission to ensure that shareholders have access to reliable information. The SEC should not be able to strongarm companies into publicly praising it whenever it thinks that there was insufficient "contrition."

* * *

Therefore, the SEC's policy of requiring gag provisions in settlement consent orders is an unconstitutional prior restraint on truthful speech. As such, those provisions are void *ab initio* as violative of public policy and are unenforceable.

II. The Gag Clause Violates Due Process for Vagueness and Rule 65(d).

The gag provision also violates due process for vagueness. As Mr. Romeril has explained, "[t]he gag order is worded so vaguely and reaches so broadly, that" he is "unable to speak without fear of a reopened prosecution because of the provision of that gag order that allows SEC to 'petition the Court to vacate the Final Judgment and restore this action to its active docket' if they unilaterally deem [him] . . . to be in breach of that provision." Romeril Aff. ¶ 5.

As relevant here, paragraph 11 of the consent states: "Defendant agrees not to take any action or to make or permit to be made any public statement denying,

directly or indirectly, any allegation in the complaint or creating the impression that the complaint is without factual basis." *Allaire*, 2019 U.S. Dist. LEXIS 199887, at *3. That is meaningless. For example, what does it mean to "take any action" to "permit to be made any public statement" that "indirectly" denies an allegation in the complaint or "creates the impression that the complaint is without factual basis"? How is Mr. Romeril to know what "impressions" or "indirect denials" the SEC may later claim to be prohibited? Does it include, for example, attempting to vindicate his rights through this lawsuit? As demonstrated by the Angelos and Morgan Stanley examples above, his concern is well founded.

Due process requires that judicial orders, enforceable by contempt proceedings, be sufficiently specific to provide fair notice of required or prohibited conduct. *See LabMD, Inc. v. FTC*, 894 F.3d 1221, 1235–37 (11th Cir. 2018); *see also* Fed. R. Civ. P. 65(d). "The judicial contempt power is a potent weapon. When it is founded upon a decree too vague to be understood, it can be a deadly one. . . . [T]hose who must obey them . . . [should] know what the court intends to require and what it means to forbid." *Int'l Longshoremen's Ass'n v. Phila. Marine Trade Ass'n*, 389 U.S. 64, 76 (1967). The consent order here fails the test.

The gag provision also violates Rule 65(d) for failure to adequately describe required or prohibited conduct.[13] "Federal Rule of Civil Procedure 65(d)(1) requires that an injunctive order state the reasons for its coercive provisions, state the provisions 'specifically,' and describe the acts restrained or required 'in reasonable detail.'" *LabMD*, 894 F.3d at 1235. Rule 65(d)'s specificity requirements "are no mere technical requirements. The Rule was designed to prevent uncertainty and confusion on the part of those faced with injunctive orders, and to avoid the possible founding of a contempt citation on a decree too vague to be understood." *Schmidt v. Lessard*, 414 U.S. 473, 476 (1974).

Under Rule 65(d), injunctions must "describe in reasonable detail—*and not by referring to the complaint* or other document—the act or acts restrained or required[.]" Fed. R. Civ. P. 65(d) (emphasis added). Rule 65(d) "is phrased in mandatory language. '[It] expressly proscribes the issuance of an injunction which describes the enjoined conduct by referring to another document." *Consumers Gas & Oil v. Farmland Indus.*, 84 F.3d 367, 370–71 (10th Cir. 1996) (cleaned up).

But here the gag provision refers to the complaint on its face. Thus, it is unenforceable. *See, e.g.*, *Hartford-Empire Co. v. United States*, 323 U.S. 386, 410

[13] The SEC appears to recognize as much. In fact, the consent order itself states that "Defendant will not oppose the enforcement of the Final Judgment on the ground . . . that it fails to comply with Rule 65(d) of the Federal Rules of Civil Procedure, and hereby waives any objection based thereon." Consent, ¶ 8.

(1945) (noting the elimination of provision that "generally enjoins . . . violations 'as charged in the complaint' . . . is required by statute, by the Rules of Civil Procedure, and by our decisions"); *City of N.Y. v. Mickalis Pawn Shop, LLC,* 645 F.3d 114, 146 (2d Cir. 2011) (prohibiting conduct by reference to a complaint is a "drafting technique, however efficient, [that] is expressly prohibited by Rule 65(d)").

III. The Gag Clause Impairs Oversight and Transparency.

The gag provision insulates the SEC from criticism by those who are uniquely positioned to expose agency wrongdoing and abuse by virtue of their firsthand experience. Defendants who have been through an agency's enforcement process are often the most informed and best positioned to identify areas in need of reform in that process. By ensuring that those who settle enforcement actions are unable to provide information that would aid oversight, the SEC insulates itself from criticism and the scrutiny accountability demands. That is wrong and nonsensical.

By way of example, in January 2020, the Office of Management and Budget ("OMB") issued a request for information on Improving and/or Reforming Regulatory Enforcement or Adjudication (the "RFI"). *See* 85 Fed. Reg. 5483. The RFI requested "specific, concrete examples of current due process shortfalls" with agency adjudications and investigations, including on topics such as "When do regulatory investigations and/or adjudications coerce Americans into resolutions/settlements?" *Id.* at 5484. The gag provision bars settling defendants

from providing critical factual information to inform this important administrative reform process. Likewise, the gag provision, on its face, prevents settling defendants from providing critical information to congressional committees tasked with conducting oversight of the SEC's enforcement activities.

IV. Allegations in SEC Complaints are Not Always True.

This Court should reject the all-too-common myth that defendants would not settle if the SEC's case was weak on the facts or law, or if the defendant had a decent chance of prevailing. The reality is that few companies and individuals are brave enough to take on a federal agency, especially their own regulator. "Since 2002, the SEC's settlement rate has remained constant at about ninety-eight percent." Priyah Kaul, *Admit or Deny: A Call for Reform of the SEC's 'Neither-Admit-Nor-Deny' Policy*, 48 U. Mich. J. L. Ref. 535, 536 (2015); *see also SEC v. Clifton*, 700 F.2d 744, 748 (D.C. Cir. 1983) ("SEC has traditionally entered into consent decrees to settle most of its injunctive actions."). This means that in the vast majority of cases, the SEC's allegations are never tested in court, and the agency is never required to prove its case. Does this mean that in every case the SEC settles, the allegations are true and the defendant has done something wrong? The short answer is no.

As the Supreme Court has explained, consent decrees "are arrived at by negotiation between the parties and often admit no violation of law[.]" *ITT Cont'l Baking Co.*, 420 U.S. at 236 n.10. And for good reason. "A settlement is by

definition a compromise." *SEC v. Citigroup Glob. Mkts., Inc*., 673 F.3d 158, 166 (2d Cir. 2012). Permitting the defendant to deny liability is entirely consistent with the public interest. *See United States v. Google Inc*., No. 12-04177, 2012 U.S. Dist. LEXIS 164401, at *14–17 (N.D. Cal. Nov. 16, 2012).

Indeed, it "is customary" for consent decrees to "explicitly state[] that '[n]othing in [the] Consent Decree is intended to constitute an admission of fault by either party to this action.'" *Maher v. Gagne*, 448 U.S. 122, 126 n.8 (1980). This custom reflects an important reality: "A defendant may settle a case for a variety of reasons. He may have committed the conduct alleged in the complaint or he may not have[.]" *United States v. Bailey*, 696 F.3d 794, 800 (9th Cir. 2012). For instance, settlement "may be motivated by a desire for peace rather than from any concession of weakness of position." Fed. R. Evid. 408, Advisory Comm. Note; *see also SEC v. Citigroup Glob. Mkts*., 752 F.3d 285, 295 (2d Cir. 2014) ("Consent decrees provide parties with a means to manage risk."). "[J]ust because a party agrees to settle does not mean that it is actually liable[.]" *In re Initial Pub. Offering Sec. Litig*., No. 21-92, 2003 U.S. Dist. LEXIS 23102, at *18 (S.D.N.Y. Dec. 24, 2003).

The reality is that companies often settle with agencies even when the allegations in the complaint are simply not true. Not because they did anything wrong but rather because the time, monetary, and reputational cost of fighting the

agency is simply too great, or to avoid the uncertainty of litigation. As the ABA Section of Antitrust Law has explained:

> Government investigations and enforcement actions are inherently different from private disputes. They are not contests between equals—federal agencies have enormous advantages in terms of resources and power. Businesses, especially smaller companies and their principals, simply cannot afford in many cases to take on the risks and costs of defending themselves during an investigation or when confronted with a complaint and order.

ABA Section of Antitrust Law, Presidential Transition Report: The State of Antitrust Enforcement, 29 (Jan. 2017), *available at* http://bit.ly/2Q82vBf. This places enormous pressure on targets to settle.

As an SEC Commissioner has explained, "[o]ften, given the time and costs of enforcement investigations, it is easier for a private party just to settle than to litigate a matter." Hester Peirce, Comm'r, SEC, The Why Behind the No: Remarks at the 50th Annual Rocky Mountain Securities Conference, *available at* https://bit.ly/34ghu1I. More bluntly, Andrew N. Vollmer, former Deputy General Counsel of the SEC, has observed:

> Many SEC cases lack merit, but the defendants settle. The routine response to this observation is that a defendant would not settle if the SEC case was faulty on the facts or the law. A defendant would not settle if it had a decent chance of winning. That is a myth believed by many, but the reality is that defendants settle for a variety of reasons and frequently settle even when they are confident they could defeat the SEC case in litigation. Defendants settle because their business, job, or personal relationships will not survive sustained adverse publicity repeating the SEC's allegations over and over during the long life of litigation, because they cannot be at odds with their main regulator,

> because they want the matter behind them, or because they do not have the financial resources to fight the government.
>
> When a defendant has strong motivations to settle, which might exist without regard for the strength of the defendant's position, the defendant often puts up weakened resistance to the staff's proposed charges, relief, and language for the charging document. The staff is able to over-reach.

Comments of Andrew N. Vollmer at 4–5, Office of Mgmt. & Budget, Request for Information, OMB-2019-0006 (Mar. 10, 2020), *available at* https://bit.ly/39QzssS.

This Court should not blind itself to the practical reality that, at times, the SEC gag clause prohibits truthful speech and enshrines the SEC's narrative in perpetuity. That is the antithesis of the rights guaranteed by the First Amendment, and this Court should reject the SEC's decades-long project to silence criticism of its actions.

CONCLUSION

For these reasons, the decision below should be reversed.

Respectfully submitted,

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Dated: April 17, 2020

CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limit of FRAP 29(a)(5), FRAP 32(a)(7)(B), and Local Rules 29.1(c) and 31.1(a)(4)(A) because it contains 6,648 words. This brief also complies with the typeface and type-style requirements of FRAP 32(a)(5)-(6) because it was prepared using Microsoft Word 2013 in Times New Roman 14-point font.

Dated: April 17, 2020

/s/ Brian Rosner
Brian Rosner

CERTIFICATE OF SERVICE

I hereby certify that on April 17, 2020, I electronically filed the foregoing Brief of Amicus Curiae Americans for Prosperity Foundation in Support of Petitioners with the Clerk of the Court by using the appellate CM/ECF system. I further certify that the participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

/s/ Brian Rosner
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