IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
FORT WORTH DIVISION

MICHELLE COCHRAN,

Plaintiff

v.

U.S. SECURITIES AND EXCHANGE COMMISSION, JAY CLAYTON, in his official capacity as Chairman of the U.S. Securities and Exchange Commission, and WILLIAM P. BARR, in his official capacity as United States Attorney General,

Defendants.

CIVIL ACTION NO: 4:19-cv-00066-A

PLAINTIFF'S REPLY BRIEF IN SUPPORT OF MOTION FOR PRELIMINARY INJUNCTION

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INTRODUCTION

In *Lucia v. SEC*, 138 S. Ct. 2044 (2018), the Supreme Court held that SEC ALJs were "officers of the United States" under Article II. *Id.* at 2053. In *Free Enterprise Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477 (2010), the Supreme Court held that such officers may not be insulated from removal by multiple layers of tenure protection. *Id.* at 484. The SEC's ALJs enjoy multiple layers of tenure protection, a point which the SEC does not deny in its response brief, which is clear from the face of the relevant statutes, and which the government has admitted. *See* Br. For Resp't Supporting Pet'r, *Lucia v. SEC*, 2018 WL 1251862, at *52-53 (U.S. Feb. 21, 2018). The inevitable conclusion is the ALJ assigned to Ms. Cochran's case sits in violation of Article II.

Recognizing this fact, the SEC claims the statutes that govern tenure protections for SEC ALJs can be construed narrowly to avoid a constitutional problem. *See* Defendants' Amended Response to Plaintiff's Motion for Preliminary Injunction ("Op. Br.") at 18-21. Plaintiff disagrees that a narrowing construction would solve the constitutional problem, but, in any event, the SEC never says *who* will impose this construction. It cannot be the Commission or the ALJ in Ms. Cochran's matter. Both lack the authority to rewrite the statutes that govern their tenure protections. According to the SEC, it should not be this Court, as the SEC believes this Court lacks jurisdiction to decide Plaintiff's removal protection claim. And the Supreme Court declined the SEC's invitation to construe the statutes narrowly in *Lucia*. *See* 138 S. Ct. at 2053 n. 1. The consequence, as the SEC admitted in its brief in *Lucia*, is that tenure protections for SEC ALJs remain unconstitutional. *See* Br. For Resp't, *Lucia v. SEC*, 2018 WL 1251862, at *53 (stating that if the Court declines to reinterpret the relevant statute, "then the limitations [it] imposes on removal of the Commission's ALJs would be unconstitutional.")

The SEC claims that the constitutional removal problem is irrelevant to jurisdiction in this case, but, in fact, it is crucial for several reasons. First, the Court in *Lucia* held that the petitioner was entitled to "a new hearing before a *properly appointed official*." *See* 138 S. Ct. at 2055 (emphasis added). But the ALJ in Ms. Cochran's proceeding has not been properly appointed, because she is insulated by multiple layers of tenure protection. From a constitutional standpoint, Ms. Cochran's new ALJ is just as unauthorized to do her job as Ms. Cochran's previous ALJ. If the SEC's position were correct, it could have ignored *Lucia* entirely, refused to refer Ms. Cochran's matter to a new ALJ, and required her to relitigate her matter before an ALJ who continued to violate the appointments clause, because, in the SEC's view, that is what the statutory scheme requires. In fact, after *Lucia* and *Free Enterprise Fund*, the statutory scheme requires the SEC to refer administrative proceedings *only* to ALJs who are properly appointed and not protected by multiple layers of tenure protection. Otherwise, *Lucia* and *Free Enterprise Fund* would be meaningless.

Second, the jurisdictional question is whether Congress intended to assign claims such as Ms. Cochran's exclusively to the administrative process. The SEC continues to ignore the fact that the Supreme Court already held in *Free Enterprise Fund* that Congress did not so intend. But beyond that, it is inconceivable that Congress could have intended individuals to litigate enforcement actions before ALJs who lack constitutional authority to hear those claims, and the SEC has produced nothing to suggest otherwise.

Third, the fact that Ms. Cochran's ALJ is constitutionally unauthorized to adjudicate her claim negates the SEC's argument that Ms. Cochran's claim is not ripe. Ms. Cochran's removal protection claim is not a challenge to an SEC final order, but to the institution of proceedings

before an ALJ who is unauthorized to hear her claims. The cases on which the SEC relies recognize that a challenge to an agency process is ripe when the agency initiates the process.

ARGUMENT

I. Plaintiff Is Likely to Succeed on the Merits

A. Under *Lucia* and *Free Enterprise Fund*, SEC ALJs Hold Office in Violation of Article II

Recognizing that multiple layers of tenure protection for SEC ALJs violate Article II, the SEC contends that the statutes governing tenure can be reinterpreted to avoid the constitutional problem and that *Free Enterprise Fund* does not apply to ALJs in any event. Op. Br. at 19. Both arguments are wrong.

The Supreme Court has upheld one layer of for-cause removal protections for officers of the United States, but as it made clear in *Free Enterprise Fund*, *two* layers goes too far. *See* 561 U.S. at 483-84. Here, SEC ALJs are protected by multiple interlocking layers of tenure protection. ALJs may be removed only "for good cause *established* and *determined* by the Merit Systems Protection Board (MSPB)." 5 U.S.C. § 7521(a) (emphasis added). As Justice Breyer noted in his concurring opinion in *Lucia*, this statute not only restricts the removal of ALJs, it takes the authority to remove them out of the hands of their superiors on the Commission by giving the exclusive power to determine whether good cause exists to the MSPB. *Lucia*, 138 S. Ct. at 2016 (Breyer, J., concurring). And, of course, both the members of the MSPB and the Commission enjoy their own for-cause removal protections. *See* 5 U.S.C. § 1202(d); *Free Enterprise Fund*, 561 U.S. at 487. These statutes are not unclear. Indeed, their obvious purpose is to insulate officers from political control by the President. *See Ramspeck v. Fed. Trial Examiners Conference*, 345 U.S. 128, 142 (1953) (stating that good cause removal protections are designed to prevent removal "for political reasons."). The statutes therefore may not be rewritten at will as

the SEC suggests. *See Chevron, U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837, 842-43 (1984) ("If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress."). But even if this Court could rewrite the meaning of "good cause" and restrict the MSPB's independent judgment on that question, that would not eliminate the additional layer of tenure protection for the members of the MSPB and the Commission. *See Free Enterprise Fund*, 561 U.S. at 492.

The SEC's argument that the holding of *Free Enterprise Fund* does not apply to ALJs is equally flawed. The Court in *Free Enterprise Fund* had no occasion to apply its holding to ALJs in the case, because ALJs were not at issue. The footnote on which the SEC relies simply made that fact clear and stated that whether ALJs were "officers of the United States" was "disputed." *See* 561 U.S. at 507 n. 10. After *Lucia*, of course, that question is no longer disputed.

Now that *Lucia* has established that SEC ALJs are inferior officers, the conclusion that they violate Article II under *Free Enterprise Fund* is unavoidable. The SEC desperately wishes to avoid this conclusion, however, because it has a profound impact on this case. It means that the SEC is attempting to force Ms. Cochran to litigate another void enforcement proceeding. If *Lucia* means anything, it means that the SEC lacks the power to do so.

B. This Court Has Jurisdiction over Plaintiff's Claim

The SEC's tactic in arguing against jurisdiction is to ignore *Free Enterprise Fund* almost entirely, to rely on *Thunder Basin Coal Co. v. Reich*, 510 U.S. 200 (1994), and *Elgin v. Department of Treasury*, 567 U.S. 1 (2012), and to place great weight on the circuit court cases—the "SEC ALJ Cases"—that have found jurisdiction precluded in ostensibly similar situations. Op. Br. at 8-15. There are three problems with that approach. First, *Free Enterprise Fund* cannot be ignored because it involved the same statutory scheme and the same essential

claim that applies in this case. Second, *Thunder Basin* and *Elgin* are distinguishable. Third, the SEC ALJ cases took the same mistaken approach to jurisdiction that the SEC takes here. Those decisions did not so much distinguish *Free Enterprise Fund* as disagree with it.

However, it is also true, as Plaintiff pointed out in her opening brief, that the SEC ALJ cases were in a different posture than this case, because they were decided *before Lucia*. The SEC professes not to understand why that matters. Op. Br. at 13. The reason is that *Lucia* makes clear that Ms. Cochran is correct—SEC ALJs occupy their positions in violation of Article II. That fact is essential in assessing jurisdiction because the analysis turns on congressional intent, and it is inconceivable that Congress could have intended individuals such as Ms. Cochran to litigate their claims before ALJs who are not authorized to hear those claims. Indeed, as Plaintiff argued in her opening brief, construing the statutory scheme in that manner would *create* a constitutional problem by ascribing unconstitutional intent to Congress. Pl. Opening Br. at 7, 19-20. The SEC ignores this argument entirely.

Both the SEC and the circuit cases on which it relies spill much ink parsing the language of 5 U.S.C. § 78y and the statutory scheme in general in search of a congressional intent to limit jurisdiction. Op. Br. at 7-10. But this is a pointless exercise, as the Supreme Court has already concluded that § 78y does not preclude jurisdiction over a constitutional removal claim. *See Free Enterprise Fund*, 561 U.S. at 489. Neither the SEC nor the circuit cases on which it relies explain how the same statute exhibits no congressional intent to foreclose jurisdiction when interpreted by the Supreme Court but do exhibit such intent when interpreted by lower courts.

The SEC and the SEC ALJ cases treat *Free Enterprise Fund* as though it was superseded by *Elgin* or is somehow an outlier, while *Elgin* and *Thunder Basin* are the truly important cases among the three. This reading is both strange and utterly without foundation. It is strange

because *Free Enterprise Fund* is the one case among the three that involves the same statute and the same claim at issue in this case. It is without foundation, because *Elgin* cited *Free Enterprise Fund* only for the test that applies in determining whether the claims at issue are the type Congress intended to be reviewed within the statutory scheme. *See* 132 S. Ct. at 15. *Elgin* in no way altered or limited the holding of *Free Enterprise Fund.*

In fact, it is *Elgin* and *Thunder Basin* that are distinguishable. As Plaintiff has noted, the key jurisdictional question is whether Congress intended to limit review of the claims at issue to the administrative process. *See Free Enterprise Fund*, 561 U.S. at 489-90. Besides ignoring *Free Enterprise Fund*'s holding that § 78y evinces no such intent, the SEC and the SEC ALJ cases misapply the Supreme Court's analysis. The SEC repeatedly states that the statutory scheme here is just as comprehensive as those in *Thunder Basin* and *Elgin*, that an ALJ could resolve Plaintiff's constitutional claim by ruling that she did not violate the '34 Act, and that Congress must therefore have intended to preclude district court jurisdiction over claims such as hers. Op. Br. at 7, 10.

What the SEC ignores is the difference between the constitutional claim at issue here and those in *Thunder Basin* and *Elgin. Thunder Basin* and *Elgin* both involved constitutional challenges to the *statutes* at issue in those cases. *See Elgin*, 567 U.S. at 12-13; *Thunder Basin*, 510 U.S. at 214. Ms. Cochran's removal protection claim does not challenge the '34 Act, however. She challenges the authority of the ALJ to preside over her enforcement action. Complaint ¶¶ 54-58, 77-88. She does not merely "allege" that the ALJ lacks authority, as the SEC repeatedly suggests. Op. Br. at 13-14. She bases her claim on two Supreme Court cases and a government admission that make clear her claim is correct. Contrary to the SEC's assertion (Op. Br. at 10), Ms. Cochran's ALJ could not resolve her removal claim by ruling in her favor on

the SEC's '34 Act claims because, under *Lucia* and *Free Enterprise Fund*, the ALJ lacks authority to preside over the proceeding or issue *any rulings at all*. *Lucia* makes clear that an action presided over by an improperly appointed ALJ is void. *See* 138 S. Ct. at 2055. *See also Freytag v. C.I.R.*, 501 U.S. 868, 879 (1991) (stating that a defect in the appointment goes to the validity of the proceeding). It follows that an ALJ without constitutional authority is not authorized to act in *any* way, whether she issues rulings *for or against* Ms. Cochran.

Indeed, not even the Commission could resolve the removal protection claim, which is a point that none of the SEC ALJ cases considered. While the Commission can fix an Appointments Clause problem by appointing ALJs properly, it cannot rewrite the statutes governing the commissioners' or their ALJs own removal. Thus, Ms. Cochran cannot obtain any relief in the administrative proceeding no matter what the Commission or the ALJ does. Because the SEC ALJ cases did not even consider this point, they are not even persuasive authority in this case.

Ms. Cochran is therefore in the same position as the petitioners in *Free Enterprise Fund*. Her choice is to submit to an unconstitutional proceeding that will ultimately be found void, at which point she will be right back where she started. Or she can refuse to participate in that proceeding and risk losing the right to appeal any of her claims, constitutional or otherwise, to an Article III court. *See* Op. Br. at 12 (stating that to appeal any SEC action, Plaintiff must raise her claims in the administrative proceeding). In short, she can "bet the farm." *See Free Enterprise Fund*, 561 U.S. at 490. It is no answer to claim, as the SEC and the SEC ALJ cases do, that *Free Enterprise Fund* is distinguishable because the petitioner there lacked any "guaranteed path to federal court." Op. Br. at 11. In fact, the petitioner in *Free Enterprise Fund* faced only a critical PCAOB inspection report when it brought its case. *See* 561 U.S. at 487, 490-91. If the firm had

waited, the investigation may not have found any violations, in which case the matter would have ended. If the investigation had resulted in an alleged violation, the SEC would have brought charges against it in an administrative proceeding, and it would have had its "guaranteed path to federal court." Clearly, it was not just the ability to obtain circuit court review that mattered to the Court in *Free Enterprise Fund*, but the fact that the petitioner was "object[ing] to the Board's existence." *Id.* at 490. Ms. Cochran is making an analogous challenge here.

The SEC and the circuit courts on which it relies are fond of quoting the Supreme Court's dictum that litigation is "part of the social burden of living under the government." *See* Op. Br. at 22 (quoting *FTC v. Standard Oil*, 449 U.S. 232, 244 (1980)). But surely the Court did not have in mind pointless litigation before constitutionally deficient ALJs foisted on an individual for no better reason than that an agency has the raw power to do so.

C. Plaintiff's Claim Is Ripe

The SEC contends that Plaintiff's claim is not ripe because the SEC has issued no final order in her matter. Op. Br. at 15. This argument mischaracterizes both Plaintiff's removal claim and the cases on which the SEC relies.

The ripeness doctrine seeks to prevent courts from "entangling themselves in abstract disagreements" where the plaintiff's injury is merely speculative. *Total Gas & Power N.A., Inc. v. FERC*, 859 F.3d 325, 333 (5th Cir. 2017). In a declaratory judgment action, the relevant question is wheher a "substantial controversy of sufficient immediacy and reality [exists] between parties having adverse legal interests." *Id.* (internal citations and quotation marks omitted). Properly understood, Ms. Cochran's removal protection claim easily meets that standard. Despite the SEC's assertions, the purpose of Ms. Cochran's claim is not to absolve her of liability under the '34 Act. Instead, she seeks a hearing before a constitutionally authorized

ALJ. *Lucia* affords her that right. Her claim is thus not an APA claim, but one arising under the Constitution, brought pursuant to 28 U.S.C. § 1331. It is most definitely ripe for adjudication because the SEC has referred her enforcement proceeding to an ALJ who enjoys multiple layers of tenure protection, and Ms. Cochran's position, backed up by two Supreme Court cases and a government admission, is that this referral is unconstitutional. The dispute is thus both adverse and immediate.

Neither of the main cases on which the SEC relies controls here. In both, the plaintiffs conceded that the agency had the authority to bring a proceeding against them, they were seeking to avoid liability, and the courts recognized that a claim attacking the proceeding as beyond the agency's power would present a different situation. *See Total Gas & Power*, 859 F.3d at 333, 335, 338; *Energy Transfer Partners, L.P. v. FERC*, 567 F.3d 134, 143 (5th Cir. 2009). Ms. Cochran's removal protection claim is therefore ripe.

II. Plaintiff Meets the Remaining Requirements for a Preliminary Injunction

The SEC makes two other arguments worth responding to. First, it suggests that Plaintiff's only claim of irreparable harm is the cost of litigation. Op. Br. at 22. But this is far from Plaintiff's only argument for irreparable harm. Plaintiff's primary argument is that forcing her to litigate before an unauthorized ALJ violates the Constitution. *See* Pl. Opening Br. at 11-14. The SEC ignores this argument entirely and mischaracterizes *Valley v. Rapides Parish Sch. Bd.*, 118 F.3d 1047 (5th Cir. 1997), as focusing primarily on harm to the plaintiff's reputation and her ability to find other employment. But in *Valley*, the Fifth Circuit clearly held that a constitutionally invalid hearing constitutes irreparable harm. *See* 118 F.3d at 1056. And Plaintiff cited other cases for the same proposition and for the proposition that she has an independent,

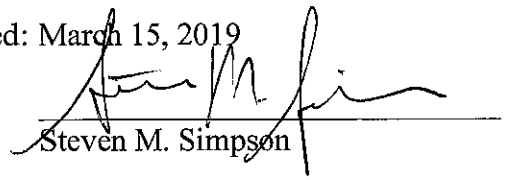
constitutionally-protected interest in maintaining the separation of powers. Pl. Opening Br. at 13. This is more than enough to establish irreparable harm.

Second, the SEC contends that the final two preliminary injunction factors weigh in its favor because of its alleged interest in rapidly enforcing the law. Op. Br. at 24. Curiously, having claimed in its jurisdictional argument that the ALJ might dismiss the claims against Ms. Cochran, the SEC now argues that because Ms. Cochran's first ALJ found her liable, the seriousness of her alleged infractions weighs against further delay. In any event, while the government has an interest in enforcing the law, that interest does not trump the Constitution.

CONCLUSION

For the foregoing reasons, Plaintiff's motion should be granted.

Dated: March 15, 2019

By: 
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I certify that on this 15th day of March, 2019, I served Plaintiff's Reply Brief in Support of Motion for Preliminary Injunction on defendants by transmitting electronic copies to defendants' counsel and by mailing it via prepaid first-class mail to:

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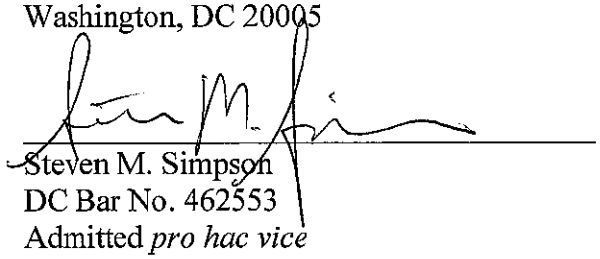

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