No. 24-3907

In the United States Court of Appeals for the Sixth Circuit

ERIC S. SMITH,

Petitioner,

v.

UNITED STATES SECURITIES AND EXCHANGE COMMISSION,

Respondent,

and

FINANCIAL INDUSTRY REGULATORY AUTHORITY, INC.

Intervenor.

On Petition for Review from the Order
Sustaining Disciplinary Action Taken by FINRA,
Administrative Proceeding File No. 3-20127, Release No. 100762

Petitioner's Reply Brief

Oral Argument Requested

Robert Knuts
GUNGNIR LAW PLLC
P.O. Box 150
Greenport, NY 11944
(631) 477-6300
rknuts@gungnirlaw.com
Counsel for Petitioner

Russell G. Ryan
Daniel Kelly
Mark Chenoweth
NEW CIVIL LIBERTIES ALLIANCE
4250 N. Fairfax Drive,
Suite 300
Arlington, VA 22203
(202) 869-5210
russ.ryan@ncla.legal
Counsel for Petitioner

July 31, 2025

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Other Authorities

SUMMARY OF THE ARGUMENT

This case is not about FINRA's authority to discipline its members—it is about who has authority over members of the public and in what forum that authority may be wielded. SEC and FINRA offer two justifications for their enforcement action against Smith. First, they argue that private companies may exercise authority over members of the public through the simple expedient of defining them as part of the organization. Alternatively, they say FINRA was merely "aiding" and "advising" SEC in the agency's exercise of its own authority. The first option is untenable because private companies cannot definitionally transform members of the public into members of the company. The second option has been conclusively foreclosed by the Supreme Court's judgment in *SEC v. Jarkesy*, 603 U.S. 109 (2024).

The parties agree that FINRA is a private company and that its authority is best described as "self-regulatory." But neither SEC nor FINRA addresses what that *means* for its interactions with the public. They simply assume that *this* private company, alone amongst all others, has the power to define members of the public into its organization. But private companies have no such power, Smith has never been a member

of FINRA, and he has not consented to its exercise of authority. It is therefore impossible for FINRA's enforcement action against Smith to have been an act of private "self"-regulation.

Instead, FINRA and SEC acknowledge that the true source of authority for their enforcement action is the SEC, not FINRA. Specifically, they admit that FINRA merely "aided" and "advised" the SEC. But when private companies act in such a capacity, they are not exercising their own authority—they are just assisting the agency in the exercise of the *agency*'s authority. So, before FINRA may "aid" or "advise" the agency, SEC must show it had the authority to adjudicate this matter without regard for Smith's Article III and Seventh Amendment rights. And that it cannot do.

The Supreme Court says SEC has no authority to adjudicate misrepresentation claims threatening civil penalties.[1] Because SEC lacks that authority, it is not possible for FINRA to "aid" or "advise" its use. In sum, FINRA has no authority to pursue enforcement actions

[1] FINRA's first two claims allege that Smith violated, respectively, the Securities Exchange Act of 1934 ("Exchange Act") and the Securities Act of 1933 ("Securities Act") by engaging in material misrepresentations and omissions. We will refer to these causes of action as the "misrepresentation claims."

against members of the public, and SEC has no authority to adjudicate misrepresentation claims involving civil penalties. There is no alchemy by which the combination of their individual lack of authority could generate the power necessary to sustain their enforcement action. The court should set aside SEC's order in this case.[2]

ARGUMENT

I. FINRA HAS NO LAWFUL AUTHORITY OVER SMITH

The assertion that FINRA is a private company, and *self*-regulatory, cannot be squared with its exercise of authority over the public. Smith has no quibble with the description of FINRA's history, nor with the standard litany of cases FINRA and SEC cite describing the nature of the organization.[3] But none of that material explains the method by which a private "self"-regulatory company could possibly obtain power over those who are neither members nor registrants. Nor has SEC advanced any plausible theory to explain how an admittedly

[2] FINRA worries that ruling for Smith will "eviscerate the self-regulatory framework that has safeguarded the securities market for centuries." FINRA Br. 16. It does not, however, explain why it needs authority over the public to engage in "self"-regulatory activity.

[3] Smith will refer to SEC and FINRA collectively as "SEC" unless context requires otherwise.

self-regulatory private company could also engage in *other*-regulatory activity. SEC's explanation is nothing but a definitional sleight of hand that suggests FINRA is unable to distinguish between "self" and "others" in any meaningful way. And that goes a long way toward understanding why FINRA thinks its "self"-regulating power can extend to "others."

The root of the problem lies in SEC's curious belief about the composition of private companies. It says FINRA may exercise jurisdiction over Smith simply because he is an "associated person" within the meaning of the relevant statutes and FINRA's bylaws.[4] But according to those provisions, "associated person" is a category defined by conduct, not consent—which SEC readily admits: "The Exchange Act and FINRA bylaws definitions of an 'associated person' hinge on the person's conduct, rather than his registration status … ." Respondent's Brief 32 (hereinafter "SEC Br").[5] So, SEC believes a private company may claim it comprises all who engage in any activity the company

[4] "[N]either the Exchange Act nor FINRA's by-laws require that a person register with FINRA to be considered associated with a member firm and thus required to follow FINRA's rules." SEC Br. 23.

[5] When addressing jurisdictional matters, Smith will refer to both "associated persons" and principals as "associated persons" unless context requires otherwise.

chooses to define. And, having capaciously defined its membership, enforcement actions to address the specified activity necessarily would be "self"-regulatory. Except that's not how private companies work.

FINRA's authority as a self-regulatory organization (SRO)—like that of all private companies—is grounded in consent, not conduct. An individual's choice to join the SRO manifests that consent. *Markowski v. SEC*, 34 F.3d 99, 105 (2d Cir. 1994) ("Markowski, who … registered with the NASD …, voluntarily submitted himself to the discipline of what is largely a self-regulating association."); *D'Alessio v. SEC*, 380 F.3d 112, 123 (2d Cir. 2004) (same in reference to the NYSE); *Sloan v. NYSE*, 489 F.2d 1, 4 (2d Cir. 1973) (same). FINRA itself says consent has traditionally been the basis for an SRO's authority, Intervenor's Br. 5 (hereinafter "FINRA Br.") ("exchange members, as parties to a voluntary contract with the exchange, must abide by their agreement") (cleaned up), and even today its registration form warns individuals that registration subjects them to FINRA's enforcement authority.[6]

[6] *See* FINRA, *Rev. Form U4* 16, § 15A, ¶ 2 (consenting to FINRA's authority) https://www.finra.org/sites/default/files/form-u4.pdf.

FINRA cannot gather members and associates through conduct-driven definitions any more than the PGA can do so. SEC professes not to understand this analogy, but it's simple. SEC claims FINRA comprises all those who fit its conduct-based definition ("associated person"), while simultaneously maintaining this is consistent with the authority of a private company. The PGA is a private organization, too, which means—according to SEC—it must also be able to define its membership based on conduct rather than consent. The PGA, therefore, could define itself as comprising all those who have ever swung at a golf ball. That, in turn, would allow it to pursue enforcement actions against weekend golfers who fudge their scorecards—again, according to SEC—on the basis that it is a private organization engaging in "self"-regulation.[7] But weekend golfers are "others" in relation to the PGA until they consent to the organization's authority. The same is true with respect to FINRA and Smith. FINRA's insistence that it may exercise "self"-regulatory authority over Smith notwithstanding the absence of consent is a

[7] *Pace* the SEC, a player does not just barge into a PGA contest; he must *register*, which conveys the necessary consent to be governed by the rules of the organization and the event. What FINRA did here is akin to the PGA rolling up to a weekend golfer one day to inform him he is now part of the association because he golfed.

confession that it is incapable of distinguishing between "self"-regulation and the regulation of "others."

SEC supplements this definitional sleight of hand with the observation that FINRA is statutorily required to arrange its affairs so that it can exercise authority over both member firms and their "associated persons." *See* 15 U.S.C. § 78s(g)(1)(A); 15 U.S.C. § 78*o*-3(b)(2). But just because Congress required FINRA to do so does not mean FINRA followed through. SEC does not identify any effort to extend FINRA's authority over Smith—other than, that is, the attempt to definitionally blur the distinction between itself and others. FINRA could have, for instance, prohibited the registration of prospective member firms unless they simultaneously submitted registrations for all "associated persons." Or it could impose fines on member firms or revoke their memberships if their "associated persons" fail to register. But it took none of those actions here, choosing instead to indulge the fiction that it may extend its jurisdiction over the public simply by announcing that those it wishes to regulate are now definitionally part of "itself."

The only authority FINRA identifies as support for dragooning segments of the public into its organization is a trio of SEC opinions. But

two of them do nothing more than state the proposition; they contain no supporting authority beyond SEC's say so. *See Application of Vladislav Steven Zubkis*, Release No. 34-40409, 1998 WL 564562 (Sept. 8, 1998) (asserting NASD could define itself as comprising all who engage in specified activity, but providing no rationale for why that might be so); *Application of Joseph Patrick Hannan*, Release No. 34-40438, 1998 WL 611732 (Sept. 14, 1998) (same). The third opinion involved a disciplinary action against an "associated person" who registered with FINRA, so it has nothing to say about FINRA's authority over those (like Smith) who do not register. So, the sum total of authority for the proposition that FINRA can define segments of the public as "itself" is that SEC has previously claimed it. Twice, apparently. But a party's recitation of an erroneous proposition does not make it true—however often it repeats it.

SEC's understanding of a private company's definitional powers is untenable and, more importantly, not supported by a single authority. For all these reasons, FINRA—as a private company with mere self-regulatory power—cannot exercise jurisdiction over Smith unless he consents. The record definitively reflects that he has not. In fact, two of FINRA's causes of action were based on his failure to manifest consent.

See Compl. at ¶¶ 101-07 (failure to register as an associated person), ¶¶ 108-14 (failure to register as a principal).

None of this, of course, is in derogation of SEC's *own* authority to investigate and prosecute enforcement actions alleging violations of federal statutes and regulations. *See* 15 U.S.C. § 78u(d)(1). Indeed, SEC's store of authority is more than adequate for it to have initiated and pursued the misrepresentation claims in this very case. Until recently, it could have adjudicated the case itself or enlisted an administrative law judge ("ALJ") to superintend the proceeding. But the Supreme Court told SEC last summer that it has no authority to adjudicate these claims. *SEC v. Jarkesy*, 603 U.S. 109, 120–21 (2024). FINRA cannot, of course, act as an "advisor" with respect to authority SEC does not have, any more than an ALJ could adjudicate matters that belong in an article III court after the *Jarkesy* decision. Therefore, because FINRA has no authority over Smith, and because SEC cannot adjudicate this matter alone or in combination with FINRA (as we discuss further below), this enforcement action must be set aside.

II. NONDELEGATION AND ARTICLE II VIOLATIONS

Because private companies lack the inherent power to exercise disciplinary authority over the public, Smith anticipated that SEC might advance one of two potential justifications for the adjudication of this matter. First, it might argue that Congress had conferred on FINRA the governmental power necessary to exercise authority over the public. Second, it might instead assert that FINRA is merely an "aid" or "advisor" to SEC in the agency's exercise of its own authority.

Smith's discussion of the private nondelegation doctrine in his opening brief anticipated SEC and FINRA making that first argument. So, the presentation focused on explaining how the exercise of authority over the public is necessarily governmental in nature, and why Congress cannot delegate such authority to a private company without violating the nondelegation doctrine. The brief also explained why private hearing officers cannot use delegated authority to adjudicate enforcement actions against the public without violating the Appointments Clause and the Take Care Clause. As it turns out, however, SEC chose to obviate these constitutional concerns by defining away the distinction between "self" and "others" in service of its claim that FINRA's enforcement actions

against the public aren't really against the public. Because it refused to recognize that there is a distinction between itself and those outside the organization, FINRA never offered any authority for the proposition that a private company may bring enforcement actions against the public. It must be taken as established, therefore, that FINRA has no such authority.

SEC asserts that Smith somehow waived his opportunity to raise these constitutional arguments because he did not present them in the SEC proceedings. But that claim misunderstands the role these arguments occupy here. Smith's position is and always has been that FINRA and SEC erred in the adjudication of this matter because FINRA has no jurisdiction over the public. The decisions below, however, rest on the unexplored assumption that FINRA can withdraw members from the public and make them part of the organization (thereby rendering the enforcement proceedings "self"-regulatory) simply by defining them as such. The dearth of authority to support that proposition suggested to Smith that, here in this court, SEC would turn to one of the two theories mentioned above. So, Smith offered the nondelegation and Article II arguments as prophylactic measures in case SEC opted to pursue the

first theory. There is no exhaustion requirement, either in 15 U.S.C. § 78y(c)(1) or elsewhere, that requires Smith to anticipate—in the SEC proceedings—the positions and arguments SEC might adopt once the matter reaches the courts. In any event, because Smith offered the nondelegation and Article II arguments only to ward against a position SEC has not taken (so far), there is no need to address them further.

III. SEC MAY NOT ADJUDICATE THIS ENFORCEMENT ACTION IN DEROGATION OF SMITH'S CONSTITUTIONAL RIGHTS

That leaves SEC with the second theory—that FINRA acted as its adjunct and that it was simply "aiding" and "advising" the agency in the exercise of SEC's own authority. While that arrangement may circumvent private nondelegation and Article II concerns, it unavoidably introduces (at least since *Jarkesy*) an Article III violation for which SEC has no good answer. The advisor/agency relationship works only if the authority being exercised belongs to the agency, not the private company. Consequently, the focus of the analysis must shift to the nature of *SEC*'s authority. If SEC may adjudicate this enforcement action, then FINRA may arguably "aid" or "advise" in the exercise of that authority by trying the case in the first instance, just as the SEC could assign the adjudication to one of its own ALJs. But if SEC *doesn't* have that

authority, then there is nothing for FINRA to "aid" or "advise," which would mean SEC—alone or in combination with FINRA—cannot adjudicate this case.

The Supreme Court has definitively resolved this question—and it resolved it against not just any governmental agency, but against SEC itself in a case involving the same type of misrepresentation claims at issue here. *See Jarkesy*, 603 U.S. at 120–21. However, in a bid to hang on to adjudicatory authority the Supreme Court says it no longer has, SEC demands that this court ignore the binding judgment against it because Smith did not foresee the Supreme Court's *Jarkesy* ruling. Before turning to SEC's substantive response, therefore, we will address its waiver argument.[8]

---

[8] SEC says Smith waived the right to respond to its waiver argument. But waiver is *SEC*'s argument, not Smith's. Smith has no duty to pre-respond to arguments that SEC might make. It was possible (although perhaps not likely) that SEC would choose not to raise its waiver objection, which would itself have disposed of the exhaustion requirement: "'No matter how clear the statutory or nonstatutory law may be that exhaustion is required, the reviewing court will not require exhaustion if the agency fails to oppose review on grounds of lack of exhaustion.'" *Bd. of Trade of City of Chicago v. SEC*, 677 F.2d 1137, 1141 (7th Cir. 1982), *cert. granted, judgment vacated sub nom. Chicago Bd. Options Exch., Inc. v. Bd. of Trade of City of Chicago*, 459 U.S. 1026 (1982), *and cert. granted, judgment vacated sub nom. SEC v. Bd. of Trade*

A. Smith Did Not Waive His Constitutional Arguments

The exhaustion requirement of 15 U.S.C. § 78y(c)(1) applies only when there is no "reasonable ground" for not raising an argument in the SEC proceedings. One of the circumstances typically recognized as a "reasonable ground" is an intervening change in controlling authority, a doctrine FINRA and SEC neither analyzed nor acknowledged. The Supreme Court says exhaustion requirements should not be used to exclude arguments involving "judicial interpretations of existing law after decision below and pending appeal—interpretations which if applied might have materially altered the result." *Hormel v. Helvering*, 312 U.S. 552, 558–59 (1941); *see also Vandenbark v. Owens-Illinois Glass Co.*, 311 U.S. 538, 541–42 (1941) ("'[I]f, subsequent to the judgment, and before the decision of the appellate court, a law intervenes and positively changes the rule which governs, the law must be obeyed, or its obligation denied.'") (quoting *United States v. Schooner Peggy*, 5 U.S. (1 Cranch) 103, 110 (1801)). This court has itself held the same. *Joseph Forrester Trucking v. Dir., Off. of Workers' Comp. Programs*, 987 F.3d 581, 592 (6th

---

of City of Chicago, 459 U.S. 1026 (1982) (quoting Kenneth Culp Davis, Administrative Law Treatise § 20.00 at 127-128 (Supp.1980)) (judgment vacated as moot).

Cir. 2021) (The "'intervening-change-in-law' doctrine … generally serves to excuse a failure to exhaust when an issue was not available to the party below."). This exception also applies to SEC proceedings. *Stoiber v. SEC*, 161 F.3d 745, 754 (D.C. Cir. 1998) ("The failure to raise an issue in a prior forum is excusable when due to an intervening change in the law … .").

Smith's constitutional argument is based on an intervening change in the law occasioned by the Supreme Court's decision in *Jarkesy*. That decision stripped SEC's adjudicatory authority over misrepresentation claims involving civil penalties and affirmatively required SEC to pursue them in a federal court where the defendant may exercise his right to a jury trial. *Jarkesy*, 603 U.S. at 120–21. Prior to this decision, federal statutes allowed SEC to choose between adjudicating such enforcement actions internally or instead bringing them to a federal court: "The SEC may bring an enforcement action in one of two forums. First, the Commission can adjudicate the matter itself. *See* 15 U.S.C. §§ 77h-1, 78u-2, 78u-3, 80b-3. Alternatively, it can file a suit in federal court. *See* 15 U.S.C. §§ 77t, 78u, 80b-9." *Jarkesy*, 603 U.S. at 116-17. The Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-

203, 124 Stat. 1376 (2010) (the "Dodd-Frank Act"), empowered SEC to pursue the same civil penalties (such as fines) in its in-house proceedings it had previously only been able to seek in a federal court. *Id*.

Before *Jarkesy*, courts across the country had routinely affirmed SEC's adjudication of such claims in its in-house proceedings, and they did so while definitively rejecting the defendants' right to a jury. *See, e.g.*, *Kabani & Co. v. SEC*, 733 F. App'x 918, 919 (9th Cir. 2018) ("Petitioners were not entitled to a jury because the Seventh Amendment does not apply to administrative proceedings."); *Desiderio v. NASD*, 191 F.3d 198, 200 (2d Cir. 1999) (Seventh Amendment not applicable to NASD proceedings); *Hill v. SEC*, 114 F. Supp. 3d 1297, 1305 (N.D. Ga. 2015) (Seventh Amendment not applicable to SEC enforcement actions), *vacated and remanded on other grounds sub nom. Hill v. Sec. & Exch. Comm'n*, 825 F.3d 1236 (11th Cir. 2016). These conclusions all reflected the Supreme Court's statement that "the Seventh Amendment is generally inapplicable in administrative proceedings, where jury trials would be incompatible with the whole concept of administrative adjudication." *Curtis v. Loether*, 415 U.S. 189, 194 (1974); *see also id*. at n.8 ("The concept of expertise on which the administrative agency rests

is not consistent with the use by it of a jury as fact finder.") (quoting Louis L. Jaffe, Judicial Control of Administrative Action 90 (1965)).

The SEC had also repeatedly rejected claims that its in-house adjudications violate the Seventh Amendment under the exact circumstances presented by this case. Indeed, in its enforcement proceeding against Mr. Jarkesy himself, SEC addressed the argument that "the provisions of the Dodd-Frank Act that authorize the imposition of civil penalties against unregistered persons in administrative proceedings violate [his] Seventh Amendment right to a jury trial." *John Thomas Cap. Mgmt. Grp. LLC and George Jarkesy, Jr.*, SEC Exchange Act Rel. No. 34-89775, 2020 WL 5291417 at *27 (Sept. 4, 2020). But SEC summarily dismissed that objection, stating "we have repeatedly rejected claims that our administrative proceedings violate the Seventh Amendment." *Id*. In one such rejection, SEC said it was bound by the Supreme Court's conclusion that administrative proceedings are immune from the Seventh Amendment's requirements: "The Supreme Court has similarly held that 'the Seventh Amendment is not applicable to administrative proceedings.'" *Kabani & Co., Inc., for Rev. of Disciplinary Action Taken by PCAOB*, Exchange Act Release No. 34-80201, 116 SEC

Docket 1095 (Mar. 10, 2017) (quoting *Tull v. United States*, 481 U.S. 412, 418 n.4 (1987)).

When this practice finally came under the Supreme Court's scrutiny, SEC vigorously defended its constitutional orthodoxy. While Smith's SEC appeal was pending, SEC was simultaneously arguing to the Supreme Court that it had authority to adjudicate the very type of misrepresentation claims at issue here: "The public rights exception still applies," it said, "because Congress created new statutory obligations, imposed civil penalties for their violation, and then committed to an administrative agency the function of deciding whether a violation had in fact occurred." *Jarkesy*, 603 U.S. at 135 (cleaned up).

Jarkesy changed all this. Whereas the Dodd-Frank Act allowed SEC to adjudicate these misrepresentation claims in its in-house proceedings, the Supreme Court said this statutory grant of authority violates defendants' Seventh Amendment right to a jury. *Id.* at 120–21. A judicial opinion invalidating what a statute prescribes must unquestionably count as a change in controlling authority. As Smith argued in his opening brief, and will address further below, this change necessarily affects the resolution of this case because it removed

FINRA/SEC's authority to pursue this case outside of a federal court. And it counts as an "intervening" change because it was released after the close of briefing in the SEC proceedings (March 2021) and, as a practical matter, contemporaneously with SEC's decision in this case.[9] In fact, briefing before the SEC had been closed for over a year before the Fifth Circuit (in *Jarkesy*) became the first court to ever uphold the Seventh Amendment rights of SEC administrative respondents.

What would have been nothing but the pointless repetition of a uniformly and oft-rejected argument, had Smith raised it in the SEC proceedings, became after *Jarkesy* a controlling authority—an authority that was not available to Smith when he was before the SEC. Even so, SEC says, its in-house proceedings might have turned out differently had Smith raised his constitutional arguments below. SEC Br. 42-43. But this requires of Smith an entirely unwarranted credulousness. In its unbroken chain of opinions and court briefs rejecting Seventh Amendment arguments, SEC had ample opportunity to do something other than summarily dismiss them. The idea that it might have

[9] The Supreme Court released the *Jarkesy* opinion on June 27, 2024, while the SEC released its decision in this case just seven weeks later on August 19, 2024.

changed its mind because *Smith* made the argument (as opposed to all those who preceded him)—or that it would defy what it said were controlling Supreme Court opinions—beggars belief. It has been said that insanity is doing the same thing over and over while expecting different results. Because the Supreme Court has "consistently recognized a futility exception to exhaustion requirements," *Carr v. Saul*, 593 U.S. 83, 93 (2021), SEC may not demand such behavior from litigants.[10]

B. The Adjudicative Authority for This Case

The authority to adjudicate this enforcement action must lie somewhere. The only possible options are FINRA, SEC, or the federal courts. It cannot lie with FINRA because (as explained above) SEC has offered no authority for the proposition that private companies have the inherent power to either discipline members of the public or to define them into the organization so that its actions can be considered "self"-

[10] Wholly apart from futility concerns, the Supreme Court has repeatedly excused exhaustion requirements when addressing this type of claim because agencies like SEC are "ill suited to address structural constitutional challenges," *Carr*, 593 U.S. at 92 (citing cases), and because such challenges exceed an agency's expertise, even "competence," *Axon Enter., Inc v. FTC* and *SEC v. Cochran*, 598 U.S. 175, 194–95 (2023) (quoting *Free Enter. Fund v. PCAOB*, 561 U.S. 477, 491 (2010)).

regulatory. If it lies with SEC, then its adjudication (alone or in combination with FINRA) must comply with constitutional requirements. But the Supreme Court just told SEC it may *not* adjudicate misrepresentation claims seeking civil penalties because doing so violates the defendant's right to an Article III court and a jury trial. *Jarkesy*, 603 U.S. at 120–21. The only legitimate forum for this enforcement action, therefore, was a federal court.

Both SEC and FINRA admit that the adjudicative authority they used in this case lies with SEC. "Admit," however, doesn't quite capture their position on this issue—they advance the argument as the essential ingredient that justifies their disposition of this matter. FINRA, for example, says SEC's "pervasive oversight and control of [its] enforcement activities" establishes that it "operates as an aid to [SEC], nothing more." FINRA Br. at 33 (quoting *Oklahoma v. United States*, 62 F.4th 221, 231 (6th Cir. 2023), *cert. denied*, 144 S. Ct. 2679 (2024), *reh'g granted and opinion vacated*, No. 23-402, 2025 WL 1787679 (U.S. June 30, 2025), *and cert. granted, judgment vacated*, No. 23-402, 2025 WL 1787679 (U.S. June 30, 2025))) (cleaned up). This is so, FINRA explains, because the authority originates not with itself, but with the legislature: "Congress

can delegate federal responsibilities to private companies as long as those private parties function subordinately to the federal government." *Id.* at 14 (cleaned up); *id.* at 26-27 ("Congress may permissibly afford a private entity a role in a regulatory program, provided that the private entity ... is under the authority and surveillance of … a governmental body.") (cleaned up). It acknowledges that its functions are permissible, that is, precisely because its role is derivative of SEC's authority. Courts uphold "the SEC-SRO model," it explains, "because SROs … *have no authority to regulate independently* of the SEC's control." *Id.* at 28 (quoting *Alpine Sec. Corp. v. Nat'l Sec. Clearing Corp.*, 2025 WL 901847, at *7 (D. Utah Mar. 25, 2025)) (cleaned up; emphasis added).

SEC agrees with FINRA's assessment that the authority to adjudicate this case belongs to SEC, and that FINRA acted as nothing more than an "aid." "For nearly 100 years," it says, "the Supreme Court and the courts of appeals have recognized that a private entity may *aid* a public federal entity that retains authority over it." SEC Br. at 47 (emphasis added). It explains that this rule is derived from *Sunshine Anthracite Coal Co. v. Adkins*, 310 U.S. 381 (1940), a case in which the Supreme Court made clear that as between government agencies and

private organizations, decisional authority must lie with the former. Specifically, it said the coal industry could act as an "aid" to the National Bituminous Coal Commission in setting the price of coal, but only because the industry representatives weren't exercising their own authority but rather assisting in the exercise of the *Commission*'s authority: "Nor has Congress delegated its legislative authority to the industry. The members of the code [the industry representatives] function subordinately to the Commission. It, not the code authorities, determines the prices." *Id.* at 399.

If confirmation that the adjudicatory power in this case lies with SEC were necessary, the difference in authority between SEC and FINRA decisions would provide it. FINRA, SEC admits, does not itself have power to issue a binding decision against Smith—that power originates and remains with SEC: "Congress … ensured that any disciplinary decision would not become final until the Commission has the opportunity to take a full and independent review … ." SEC Br. 60. The independence of the SEC review demonstrates that FINRA was acting in an advisory role when it rendered its decision—which is the most it can do within constitutional constraints. As SEC itself said

(quoting this court), its "'ultimate control over the rules and their enforcement makes the SROs [like FINRA] permissible aides and advisors." *Id.* at 51 (quoting *Oklahoma*, 62 F.4th at 228). "Aids and advisors," of course, are not the source of authority with which they are aiding and advising. If they were, they would have no need to aid or advise, they would just act.

The Supreme Court, in the term just concluded, confirmed that the relationship between governmental agencies and private organizations must be structured so that the agencies, not the private entities, are the source of authority being wielded. In *FCC v. Consumers' Research*, the Court said that an agency "may enlist private parties to give it recommendations," but only "[a]s long as [the] agency … retains decision-making power … ." 145 S. Ct. 2482, 2491 (2025). Ensuring that this authority remains with SEC preserves FINRA's proper role as an advisor, not a wielder of governmental power. *See Pittston Co. v. United States*, 368 F.3d 385, 395 (4th Cir. 2004) ("Congress may employ private entities for ministerial or advisory roles, but it may not give these entities governmental power over others."); *Nat'l Horsemen's Benevolent & Protective Ass'n v. Black*, 53 F.4th 869, 872 (5th Cir. 2022) ("A cardinal

constitutional principle is that federal power can be wielded only by the federal government. Private entities may do so only if they are subordinate to an agency.").

FINRA, therefore, was not the source of adjudicative authority in this case. Its role was advisory, and its decision was a recommendation that—as SEC said—it could "approve, disapprove, or modify," SEC Br. 56, "as it deems appropriate," *id.* at 51 (quoting *NASD v. SEC*, 431 F.3d 803, 806 (D.C. Cir. 2005)). Because SEC was the source of adjudicative authority in this case, the exercise of that power must conform to constitutional requirements. Prior to *Jarkesy*, it could have either pursued these claims in its internal tribunal or (arguably) allowed FINRA to try them in the first instance in its advisory role. But no longer.

C. Smith's Right to an Article III Court and a Jury Trial

Smith is entitled to an Article III court and a jury trial because the Supreme Court ruled that SEC may no longer adjudicate misrepresentation claims seeking civil penalties. Because FINRA is limited to serving in an advisory role in SEC's exercise of its own authority, *Jarkesy*'s removal of SEC's authority means there is nothing

permissible on which FINRA can advise. Consequently, the only forum in which this case may be tried is a federal court.

SEC, however, says the court must nevertheless deny the right to a jury because Smith "fails to explain how the Constitution prohibits a private company from using internal procedures to discipline private members." *Id.* at 61 (caption). But that's something that SEC and FINRA themselves have already done. As discussed above, they both forcefully argue that the adjudicative authority used in this case lies with SEC, and that FINRA served in a merely advisory role. So the question isn't about "the historical tradition of self-regulation," as SEC would have it. *Id.* at 65. Rather, it is about the nature of the authority that FINRA and SEC have already admitted was used in this case. And to the extent SEC is looking for someone to examine the interaction between Smith's right to a jury trial and "the nature of the Commission proceedings at issue," *id.* at 66, the *Jarkesy* Court has already done so. Whether SEC is trying the case in the first instance (either before its ALJs, as in *Jarkesy*, or before the Commission itself), or exercising its independent authority to address a FINRA decision *de novo* (as in this case), it is engaging its adjudicative authority. It certainly wasn't exercising *FINRA*'s authority

when it issued what was—as between FINRA and SEC—the only binding opinion against Smith.

SEC cannot have it both ways. It cannot assure the Court that the adjudicative power used in this case was its own, and that FINRA acted in a subordinate and merely advisory role (in satisfaction of the *Adkins* requirements), and then claim that FINRA—not SEC—was the true source of authority when Smith asserts his *Jarkesy*-confirmed rights to a jury trial and an Article III tribunal. If it were otherwise, SEC could reduce *Jarkesy*'s protection of defendants' constitutional rights to a nullity through the simple expedient of assigning to FINRA the responsibility to try all misrepresentation claims seeking civil penalties—the claims at issue in both *Jarkesy* and here.

Constitutional rights are not annoyances to be evaded through sophisticated indirection and manipulation. They are to be honored in full, because they "would be of little value if they could be indirectly denied or manipulated out of existence." *Harman v. Forssenius*, 380 U.S. 528, 540 (1965) (cleaned up). It should be a given that the Constitution "nullifies sophisticated as well as simple-minded modes of impairing the right[s] [it] guarantee[s]." *Id.* at 540–41 (internal quotations omitted).

SEC may not use sophistry to evade Smith's rights to a jury trial and an Article III tribunal.

FINRA tries a different tack to get around *Jarkesy*. The misrepresentation claims here, it says, are not "made of the stuff of the traditional actions at common law tried by the courts at Westminster in 1789," and so are not subject to the Seventh Amendment's provisions. FINRA Br. 48 (quoting *Jarkesy*, 603 U.S. at 127-28). But as Smith explained in his opening brief, the claims FINRA made in this case are the *exact same claims* SEC made in *Jarkesy*. Both Smith and Jarkesy were charged with securities fraud in violation of § 17(a) of the Securities Act, as well as § 10(b) of the Exchange Act and SEC Rule 10b-5, and each suffered exposure to civil penalties. The nature of the claims does not change depending on the forum in which they are tried. They sound in common law whether they are initially heard by an SEC ALJ or by a FINRA hearing officer.

SEC's final effort to avoid Smith's right to a jury trial is based on an apparent belief that defendants must wait until their trials are complete and sanctions (if any) are imposed to learn whether there should have been a jury. "Smith," SEC says, "compares FINRA 'fines' to

the civil monetary penalties at issue in *Jarkesy*, … but FINRA did not impose such a fine against Smith and no such fine was before the Commission." SEC Br. 64. No right to a jury accrued, SEC concluded, because the only monetary sanction actually imposed was restitution, which SEC claims is equitable in nature, not legal. *Id.* at 65.[11] But a defendant's entitlement to a jury trial is determined, for obvious reasons, *before* the trial starts and depends on the nature of the claim as well as the sanctions the defendant is *at risk* of incurring. The sanctions the tribunal imposes at the conclusion of the trial are entirely irrelevant. SEC cannot seriously believe that, in a case based on misrepresentation claims in which the prosecuting agency seeks civil penalties, the proper procedure is to (1) deny a defendant's demand for a jury, (2) try the case to a verdict, and then (3) do it all over again in front of a jury if it succeeds in obtaining the sanctions it sought in the first trial.

Smith was at risk of incurring the exact same civil penalties for the exact same alleged violation as Jarkesy. As SEC knows, FINRA's Department of Enforcement ("DOE") explicitly and consistently urged

[11] *But see Great West Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 213-14 (2002) (restitution is a remedy at law, rather than in equity, when it imposes personal liability for a sum of money).

the imposition of such a sanction against Smith. In its Pre-Hearing Brief, DOE asked for a $73,000 fine for Smith's alleged violation of § 17(a) of the Securities Act. DOE's Pre-Hr'g Br. 32. It continued to advocate that sanction in both its Post-Hearing Brief and its Post-Hearing Reply Brief. DOE's Post-Hr'g Br. 43; DOE's Post-Hr'g Reply Br. 22. The fact that it was unsuccessful in its attempt to have civil penalties imposed on Smith has nothing to do with whether he was entitled to a jury. It was the *risk* of such sanctions that established his right to a jury.

D. The Difference a Jury Would Make

Smith's demand that FINRA/SEC respect his right to a jury trial is about much more than an antiseptic concern for constitutional fidelity. It is about whether the protections promised him by the Seventh Amendment would have occasioned a different result.

One of the key allegations in this case was that Smith engaged in misrepresentations and omissions that were "material" within the meaning of the Securities Act and Exchange Act. Contrary to SEC's conclusion, however, "materiality" is a fact question for the jury. *See, e.g.*, *SEC v. Commonwealth Equity Servs., LLC*, 133 F.4th 152, 168 (1st Cir. 2025) ("the usual rule that materiality is to be decided by the jury applies

in this case"). Smith is confident a jury would have disagreed with FINRA and SEC's resolution of this question. But that's just the tip of the iceberg—this case was rife with contested questions of fact that should have been submitted to a jury, including whether he fits the definition of an "associated person" or "principal," managed a member firm, personally undertook the registration of CSSC-BD with FINRA, engaged in the securities business, controlled CSSC-BD, manifested any agreement that his actions would subject him to FINRA's authority, or acted with scienter.[12]

A jury could, and likely would, resolve any number of these fact questions differently, many of which would require the dismissal of FINRA/SEC's case against Smith. Their violation of Smith's right to a jury, therefore, was almost certainly outcome determinative.

[12] *See* Smith's Pre-Hr'g Br. 10–12; Smith's Initial Post-Hr'g Br. at 1–2, 6–7 (Proposed Findings of Fact); *id.* at 11–13 (Proposed Conclusions of Law); Smith's Rebuttal Post-Hr'g Br. at 1–2; 10–15.

CONCLUSION

For these reasons, Smith asks this Court to set aside SEC's Order in its entirety and to direct SEC to enter an order cancelling and setting aside the sanctions imposed against him by FINRA.

July 31, 2025

Respectfully Submitted,

/s/ Russell G. Ryan
Russell Ryan
Daniel Kelly
Mark Chenoweth
NEW CIVIL LIBERTIES ALLIANCE
4250 N. Fairfax Drive, Suite 300
Arlington, VA 22203
(202) 869-5210
russ.ryan@ncla.legal

Robert Knuts
GUNGNIR LAW PLLC
P.O. Box 150
Greenport, NY 11944
(631) 477-6300
rknuts@gungnirlaw.com

Counsel for Petitioner

CERTIFICATE OF COMPLIANCE

This brief complies with Fed. R. App. P. 32(a)(7)(B)(ii) because it contains 6,499 words. This brief also complies with the typeface and type-style requirements of Fed. R. App. P. 32(a)(4)-(6) because it has been prepared in 14-point Century Schoolbook font using Microsoft Word.

/s/ Russell G. Ryan

CERTIFICATE OF SERVICE

I certify that on July 31, 2025, I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the Sixth Circuit using the CM/ECF system. I also certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the CM/ECF system.

/s/ Russell G. Ryan